LESSON 5: ANALYSING BUSINESS MARKETS

5.1: WHAT IS ORGANIZATIONAL BUYING?

Organizational buying is the decision-making process by which formal organizations establish the need for purchased products and services and identify, evaluate, and choose among alternative brands and suppliers.

The Business Market versus the Consumer Market

The business market consists of all the organizations that acquire goods and services used in the production of other products or services that are sold, rented, or supplied to others. The major industries making up the business market are agriculture, forestry, and fisheries; mining; manufacturing; construction; transportation; communication; public utilities; banking, finance, and insurance; distribution; and services.

Business marketers face many of the same challenges as consumer marketers. In particular, understanding their customers and what they value is of paramount importance to both. A survey of top business-to-business firms identified the following as challenges they faced:

1. Understanding deep customer needs in new ways;
2. Identifying new opportunities for organic business growth;
3. Improving value management techniques and tools;
4. Calculating better marketing performance and accountability metrics;
5. Competing and growing in global markets, particularly China;
6. Countering the threat of product and service commoditization by bringing innovative offerings to market faster and moving to more competitive business models; and
7. Convincing C-level executives to embrace the marketing concept and support robust marketing programs.

Business marketers contrast sharply with consumer markets in some ways, however:

Fewer, larger buyers: The business marketer normally deals with far fewer, much larger buyers than the consumer marketer does, particularly in such industries as aircraft engines and defense weapons.
Close supplier–customer relationship; Because of the smaller customer base and the importance and power of the larger customers, suppliers are frequently expected to customize their offerings to individual business customer needs.
Professional purchasing: Business goods are often purchased by trained purchasing agents, who must follow their organizations' purchasing policies, constraints, and requirements. Many of the buying instruments—for example, requests for quotations, proposals, and purchase contracts— are not typically found in consumer buying.
Multiple buying influences: More people typically influence business buying decisions. Buying committees consisting of technical experts and even senior management are common in the purchase of major goods. Business marketers need to send well-trained sales representatives and sales teams to deal with the well-trained buyers.
Multiple sales calls: A study by McGraw-Hill found that it took four to four and a half calls to close an average industrial sale. In the case of capital equipment sales for large projects, it may take many attempts to fund a project, and the sales cycle—between quoting a job and delivering the product—is often measured in years.

Derived demand: The demand for business goods is ultimately derived from the demand for consumer goods. For this reason, the business marketer must closely monitor the buying patterns of ultimate consumers.
Inelastic demand: The total demand for many business goods and services is inelastic—that is, not much affected by price changes. Shoe manufacturers are not going to buy much more leather if the price of leather falls, nor will they buy much less leather if the price rises unless they can find satisfactory substitutes.
Fluctuating demand: The demand for business goods and services tends to be more volatile than the demand for consumer goods and services. A given percentage increase in consumer demand can lead to a much larger percentage increase in the demand for plant and equipment necessary to produce the additional output.
Geographically concentrated buyers: At the same time, business marketers need to monitor regional shifts of certain industries.
Direct purchasing: Business buyers often buy directly from manufacturers rather than through intermediaries, especially items that are technically complex or expensive such as mainframes or aircraft.

Categories of Business Buyers

Producers	- Manufacturers and service providers - Purchase goods and services to produce other products, to incorporate into other products, or to support the day-to-day operations of the organization
Resellers	- Wholesalers and retailers - Resell products to other resellers or consumer at large
Government	- Federal, state and local municipalities - Provide service to the public
Institutions	- Non-profit organizations like universities, schools, hospitals, social clubs, etc. - Provide goods and services for people under their responsibilities e.g. students, patients, and patrons.

Table 5.0: Categories of Business Buyers

<u>Buying Situations</u>

The business buyer faces many decisions in making a purchase. How many depends on the complexity of the problem being solved, newness of the buying requirement, number of people involved, and time required. Three types of buying situations are the straight rebuy, modified rebuy, and new task.

Straight rebuy: In a straight rebuy, the purchasing department reorders supplies such as office supplies and bulk chemicals on a routine basis and chooses from suppliers on an approved list. The suppliers try to maintain product and service quality and often propose automatic reordering systems to save time. "Out-suppliers" attempt to offer something new or exploit dissatisfaction with a current supplier. Their goal is to get a small order and then enlarge their purchase share over time.

Modified rebuy: The buyer in a modified rebuy wants to change product specifications, prices, delivery requirements, or other terms. This usually requires additional participants on both sides. The in-suppliers become nervous and want to protect the account. The out-suppliers see an opportunity to propose a better offer to gain some business.

New task: A new-task purchaser buys a product or service for the first time (an office building, a new security system). The greater the cost or risk, the larger the number of participants, and the greater their information gathering—the longer the time to a decision.

5.2: PARTICIPANTS IN THE BUSINESS BUYING PROCESS

The buying center includes all members of the organization who play any of the following seven roles in the purchase decision process:

1. **Initiators**—Users or others in the organization who request that something be purchased.
2. **Users**—Those who will use the product or service. In many cases, the users initiate the buying proposal and help define the product requirements.
3. **Influencers**—People who influence the buying decision, often by helping define specifications and providing information for evaluating alternatives. Technical personnel are particularly important influencers.
4. **Deciders**—People who decide on product requirements or on suppliers.
5. **Approvers**—People who authorize the proposed actions of deciders or buyers.
6. **Buyers**—People who have formal authority to select the supplier and arrange the purchase terms. Buyers may help shape product specifications, but they play their major role in selecting vendors and negotiating. In more complex purchases, buyers might include high-level managers.
7. **Gatekeepers**—People who have the power to prevent sellers or information from reaching members of the buying center. For example, purchasing agents, receptionists, and telephone operators may prevent salespersons from contacting users or deciders.

5.3: STAGES IN THE BUSINESS BUYING PROCESS

Problem Recognition

The buying process begins when someone in the company recognizes a problem or need that can be met by acquiring a good or service. The recognition can be triggered by internal or external stimuli. The internal stimulus might be a decision to develop a new product that requires new equipment and materials, or a machine that breaks down and requires new parts. Or purchased material turns out to be unsatisfactory and the company searches for another supplier, or lower prices or better quality. Externally, the buyer may get new ideas at a trade show, see an ad, or receive a call from a sales representative who offers a better product or a lower price. Business marketers can stimulate problem recognition by direct mail, telemarketing, and calling on prospects.

General Need Description and Product Specification

Next, the buyer determines the needed item's general characteristics and required quantity. For standard items, this is simple. For complex items, the buyer will work with others—engineers, users—to define characteristics such as reliability, durability, or price. Business marketers can help by describing how their products meet or even exceed the buyer's needs.

The buying organization now develops the item's technical specifications. Often, the company will assign a product-value-analysis engineering team to the project. Product value analysis (PVA) is an approach to cost reduction that studies whether components can be redesigned or standardized or made by cheaper methods of production without adversely impacting product performance. The PVA team will identify overdesigned components, for instance, that last longer than the product itself. Tightly written specifications allow the buyer to refuse components that are too expensive or that fail to meet specified standards.

Supplier Search

The buyer next tries to identify the most appropriate suppliers through trade directories, contacts with other companies, trade advertisements, trade shows, and the Internet. The move to Internet purchasing has far-reaching implications for suppliers and will change the shape of purchasing for years to come. Companies that purchase over the Internet are utilizing electronic marketplaces in several forms:

Catalog sites – Companies can order thousands of items through electronic catalogs distributed by e-procurement software.

Vertical markets – Companies buying industrial products such as plastics, steel, or chemicals or services such as logistics or media can go to specialized Web sites (called e-hubs).

"Pure Play" auction sites – Ritchie Bros. Auctioneers for example, is the world's largest industrial auctioneer, with more than 40 auction sites worldwide. It sold $3.5 billion of used and unused equipment at more than 300 unreserved auctions in 2009, including a wide range of heavy equipment, trucks, and other assets for the construction, transportation, agricultural, material handling, mining, forestry, petroleum, and marine industries.

Barter markets – In barter markets, participants offer to trade goods or services.

Buying alliances – Several companies buying the same goods can join together to form purchasing consortia to gain deeper discounts on volume purchases.

E-Procurement

Web sites are organized around two types of e-hubs: vertical hubs centered on industries (plastics, steel, chemicals, paper) and functional hubs (logistics, media buying, advertising, energy management).

Lead Generation

The supplier's task is to ensure it is considered when customers are— or could be—in the market and searching for a supplier. Identifying good leads and converting them to sales requires the marketing and sales organizations to take a coordinated, multichannel approach to the role of trusted advisor to prospective customers. Marketing must work together with sales to define what makes a "sales ready" prospect and cooperate to send the right messages via sales calls, trade shows, online activities, PR, events, direct mail, and referrals.

Proposal Solicitation

The buyer next invites qualified suppliers to submit proposals. If the item is complex or expensive, the proposal will be written and detailed. After evaluating the proposals, the buyer will invite a few suppliers to make formal presentations.

Business marketers must be skilled in researching, writing, and presenting proposals. Written proposals should be marketing documents that describe value and benefits in customer terms. Oral presentations must inspire confidence and position the company's capabilities and resources so they stand out from the competition. Proposals and selling are often team efforts.

Supplier Selection

Before selecting a supplier, the buying center will specify and rank desired supplier attributes. The choice of attributes and their relative importance varies with the buying situation. Delivery reliability, price, and supplier reputation are important for routine-order products. For procedural-problem products, such as a copying machine, the three most important attributes are technical service, supplier flexibility, and product reliability. For political-problem products that stir rivalries in the organization (such as the choice of a computer system), the most important attributes are price, supplier reputation, product reliability, service reliability, and supplier flexibility.

Order-Routine Specification

After selecting suppliers, the buyer negotiates the final order, listing the technical specifications, the quantity needed, the expected time of delivery, return policies, warranties, and so on. Many industrial buyers lease heavy equipment such as machinery and trucks. The lessee gains a number of advantages: the latest products, better service, the conservation of capital, and some tax advantages. The lessor often ends up with a larger net income and the chance to sell to customers that could not afford outright purchase.

In the case of maintenance, repair, and operating items, buyers are moving toward blanket contracts rather than periodic purchase orders. A blanket contract establishes a long-term relationship in which the supplier promises to resupply the buyer as needed, at agreed-upon prices, over a specified period of time. Because the seller holds the stock, blanket contracts are sometimes called stockless purchase plans. The buyer's computer automatically sends an order to the seller when stock is needed. This system locks suppliers in tighter with the buyer and makes it difficult for out-suppliers to break in unless the buyer becomes dissatisfied with prices, quality, or service.

Companies that fear a shortage of key materials are willing to buy and hold large inventories. They will sign long-term contracts with suppliers to ensure a steady flow of materials. DuPont, Ford, and several other major companies regard long-term supply planning as a major responsibility of their purchasing managers. For example, General Motors wants to buy from fewer suppliers, who must be willing to locate close to its plants and produce high-quality components. Business marketers are also setting up extranets with important customers to facilitate and lower the cost of transactions. Customers enter orders that are automatically transmitted to the supplier.

Some companies go further and shift the ordering responsibility to their suppliers in systems called vendor-managed inventory (VMI). These suppliers are privy to the customer's inventory levels and take responsibility for replenishing automatically through continuous replenishment programs. For example, Plexco International AG supplies audio, lighting, and vision systems to the world's leading automakers. Its VMI program with its 40 suppliers resulted in significant time and cost savings and allowed the company to use former warehouse space for productive manufacturing activities.

Performance Review

The buyer periodically reviews the performance of the chosen supplier(s) using one of three methods. The buyer may contact end users and ask for their evaluations, rate the supplier on several criteria using a weighted-score method, or aggregate the cost of poor performance to come up with adjusted costs of purchase, including price. The performance review may lead the buyer to continue, modify, or end a supplier relationship.

Many companies have set up incentive systems to reward purchasing managers for good buying performance, in much the same way sales personnel receive bonuses for good selling performance. These systems lead purchasing managers to increase pressure on sellers for the best terms.

POINTS TO PONDER

1. Organizational buying is the decision-making process by which formal organizations establish the need for purchased products and services, then identify, evaluate, and choose among alternative brands and suppliers. The business market consists of all the organizations that acquire goods and services used in the production of other products or services that are sold, rented, or supplied to others.
2. Compared to consumer markets, business markets generally have fewer and larger buyers, a closer customer supplier relationship, and more geographically concentrated buyers. Demand in the business market is derived from demand in the consumer market and fluctuates with the business cycle. Nonetheless, the total demand for many business goods and services is quite price inelastic. Business marketers need to be aware of the role of professional purchasers and their influencers, the need for multiple sales calls, and the importance of direct purchasing, reciprocity, and leasing.
3. The buying center is the decision-making unit of a buying organization. It consists of initiators, users, influencers, deciders, approvers, buyers, and gatekeepers. To influence these parties, marketers must be aware of environmental, organizational, interpersonal, and individual factors.
4. The buying process consists of eight stages called buy-phases: (1) problem recognition, (2) general need description, (3) product specification, (4) supplier search, (5) proposal solicitation, (6) supplier selection, (7) order routine specification, and (8) performance review.

REFERENCES

- Kotler, P. & Keller, K. (2016). Marketing Management. 15th edition. New Jersey: Pearson/Prentice Hall.
- Kotler, P., Keller, K. L., Ang, S. H., Leong, S. M., Tan, C. T. (2017). Marketing Management: An Asian Perspective. 7th edition. Singapore: Pearson.