



UNIT-10

Channels of Distribution

Staff Training Solutions

Learning Outcomes

By the end of this unit the learner will be able to:

- ✓ Understand the meaning and role of distribution channels in the overall marketing of **products**
- ✓ Explain the various functions of the channels of distribution

Unit 10

Channels of Distribution

Product and pricing are two important aspects of marketing mix that you have already studied. However, it is important to realise that just creating a good product, even with all the required qualities, beautiful packing and branding, reasonable prices etc., does not necessarily lead to success. It is just as important to ensure that the product is available where the consumer is most likely to purchase it. To put it simply, the product has to be made available at the right time *and* at the right place. To make sure this happens, the manufacturer has to make strategic decisions for methodical circulation of its products. One of these decisions has to do with the means of distribution. This unit will cover this aspect. The definition, functions and role of a channel of distribution, aspects effecting distribution choices and strategies related to force of distribution will all be explored in detail.

What is a Channel of Distribution?

Distribution systems deal with moving goods from where they are produced to the point where they will be consumed. The main players in the distribution system are:

- i) manufacturers;
- ii) intermediaries;
- iii) facilitating agencies;
- iv) consumers.

Manufacturers are responsible for producing the product. This is the point where the distribution system begins. The next category of participants - the intermediaries - take part in direct talks between sellers and buyers, whether they take the goods or not. Intermediaries seek out manufacturers that produce various products, pinpoint the needs of the customer, and dispense them accordingly. In the process, they carry out a number of functions like selling, assembling, buying, standardizing and packing, grading, risk management etc. Besides intermediaries, independent business firms like facilitating agencies also exist. Such agencies help ensure the simple and smooth distribution of goods, starting with producers through intermediaries and finally to consumers. Some of the major facilitating agencies include banking institutions, insurance companies, transport organizations and warehouse companies. The fourth and final category in the chain of participants in the distribution system is the customer.

The distribution channel is mostly involved with the second participant - the intermediaries. The term 'Channel of Distribution' deals with the course the goods pass through as they are moved from the producer to the consumer. This flow can be related to physical distribution and/or switching of title (ownership). Channels of delivery generally deal with the transfer of product title, which may be affected either through a chain of intermediaries or directly. The majority of producers do not sell their goods directly to the consumer. They utilise intermediaries, who are also known as middlemen. These middlemen take title to the goods or help in moving the title to goods as they flow from producer to

consumer; this is called channel of distribution. So, the channel is actually a group of associations that carry out interconnected and harmonized functions, moving goods from manufacturers to consumers. A distribution channel creates time, place, form and possession utilities to the goods by punctual and efficient presentation of the purpose of physical delivery. In contemporary societies, the manufacture of goods takes place on huge scales in factories located in a few localities, while the customers are spread throughout the country.

In the majority of situations, goods are manufactured in one location, though they are utilised at a large number of other places and customers cannot contact the producers directly. Likewise, not all producers can contact the consumers directly to sell their products. So it becomes imperative to move the merchandise from the place of manufacture to the markets where consumers can purchase them. Otherwise, manufacture has no worth and becomes wasteful. A distribution channel aids in the movement of merchandise from the producer to the customer, and therefore gives utility to the products.

Another consideration is the time that passes between the time of production and when the product is consumed. All merchandise that is produced is not consumed at the same time. Certain goods are manufactured continuously throughout the year, however their utilization is seasonal. For instance, raincoats and umbrellas are only needed during rainy periods, woollen clothing is only used in the winter season and so on. In other situations, goods are produced during a certain time of the year, yet they are used all year round.

An example of such a situation would be food grains, which are cultivated by farmers during a given season, but eaten throughout the year. So, in this case, there is a time lag between the time of production and when it is consumed. It is the distribution channel that provides utility to the grain, by making it possible for the consumer to get it whenever they need it through the channel. Furthermore, the channel makes the goods available to the consumer in a convenient unit size, shape, style and package. Hence, it adds convenience value. Distribution channels allow the consumer to get the goods at a price that they are ready to pay and under conditions which are satisfactory. In this way, it creates the possession utility. To repeat the key point, the distribution channel takes goods from where they were manufactured and makes them available to the customer at the right place, time and in the right form.

Functions of Channels of Distribution

The functions carried out by the distribution channels can be grouped into three main categories, which are outlined below:

- 1) Transactional Functions;
- 2) Logistical Functions;
- 3) Facilitating Functions

1. Transactional Functions: The tasks required for transaction of the merchandise are known as transactional functions. Selling, buying and risk carrying functions are placed in this category.

Contributors in the channel of circulation assume these three functions. Manufacturers sell the merchandise and intermediaries purchase them. Then, intermediaries sell the merchandise and consumers purchase them.

Due to this process of sale and purchase by the channel participants, titles to goods change hands, and merchandise flows from the manufacturer to the consumer. If no one was willing to purchase or sell, there wouldn't be any transactions. With the purchase of goods, there is risk. For example, the intermediary buys merchandise from the manufacturer with the aim of selling it at a profit. However, they may end up incurring a loss due to fall in prices. All participants involved in the distribution channel take this risk of losing funds.

2. **Logistical Functions:** All tasks involved in the physical exchange of goods are known as logistical functions. The distribution channel carries out certain functions like storage, assembling, grading and transportation, which are imperative for the physical exchange of merchandise. Goods are manufactured in large enough quantities to ensure a sufficient selling and shipping quantity is available. At times, it becomes necessary to put together a vast array of products, so that a variety of items wanted by buyers can be made available. Grading and packing of merchandise helps the handling and sale of the product in a timely manner. Proper storage of merchandise stops loss or damage and ensures a regular supply of goods to consumers when they need it. Transport makes the goods available at locations where the consumers are located. In the channel of distribution all these tasks are carried out so goods can make it to the market at correct time and be sold to the end-consumer.
3. **Facilitating Functions:** These functions aid both the transaction and the physical exchange of goods. These assistance functions of the channel include after-purchase service and upkeep, financing, market information etc. Sellers give all the required information to buyers, along with after-sales service and financial help in the way of credit. Likewise, traders are frequently guided by producers to assist them in making sales, and the traders usually inform manufacturers about customer preferences and opinions about their products. This way, the channel of distribution carries out a variety of tasks like selling, buying, risk bearing, assembling, grading, storage, transport, post-purchase service, upkeep, financing, marketing information, etc. However, the comparable importance of storage is a greater priority in the case of perishable materials and heavy duty materials like coal, iron, petroleum products. Whereas in the case of cars and sophisticated electronic merchandise like computers, after-sales service takes on greater importance.

Channels of Distribution Used

You have gained knowledge about the tasks and nature of distribution channels. We will now look at the channels of distribution most commonly used by manufacturers. These can only be grouped into two groups:

- i. Direct channels
- ii. Indirect channels.

Direct Channel

When manufacturers sell their merchandise to consumers directly, it is known as a direct channel. No middleman exists between the manufacturer and consumer. For direct selling, the first choice involves supplying the goods to the consumer using your own salespeople and making arrangements for delivering the goods on your own. The other option is to send the goods by post. Orders are placed by the customers who contact you by mail, telephone, online or in response to letters and advertisements mailed to their homes directly. The goods are delivered to them through standard mail or some other carrier/courier service. The next alternative is to set up your own retail stores. Zero-level is another name for direct channel, as there is no middleman between the manufacturer and consumer. The three main methods of direct selling are summarised in the figure below:



Fig.10.1

Fig: Distribution through direct channels

Indirect Channels

In the case of some products, it is just not feasible for the manufacturer to supply merchandise to the customer directly. So, middlemen agents including retailers and wholesalers participate in the distribution channel, which is known as the indirect channel. As can be seen in the figure below, there are four indirect channels.



Fig. 10.2

Indirect channels of distribution

A manufacturer has the option of supplying goods to retail traders directly. In such a situation, the manufacturer will determine the needs of the retailers at regular intervals and supply the merchandise according to their needs. If the need arises, the retailer has the option of securing merchandise from the producer's warehouse in the vicinity. Similarly, the manufacturer can also make goods available to consumers by using the facilities of a wholesale trader. Since only one middleman exists in this channel, either the retailer or wholesaler, this is called the one-level channel.

The producer can also make use of the facilities provided by the wholesaler *and* a retailer at the same time. In this scenario, the manufacturer supplies products in bulk to wholesalers. The retailer in turn has the option of buying from the wholesaler periodically, and then selling to customers located in the vicinity. In the case of two middlemen (wholesaler and retailer), this method is known as the two-level channel. Mercantile agents, wholesalers and retailers combined is yet another channel of distribution. In this case, the manufacturer does business with a mercantile agent.

Then, the wholesalers purchase the goods from these agents and sell them to retailers. The retailer carries out sales to the final consumer. This kind of channel is called a three-level channel, as there are three kinds of middlemen through which distribution takes place. As you can see, there are many prevalent methods of distribution. From the manufacturer's standpoint, the greater the number of middlemen employed, the poorer their control over the overall distribution process. We can now examine how these different distribution channels differ from each other, when the type of product is changed.

Essentially, merchandise can be divided into two classifications:

1. Consumer goods
2. Industrial goods

We can now look at the channels of distribution, which are utilised in these categories.

Channels of Distribution Used for Consumer Goods

Consumer goods are the products used by the general household consumer. A very large range of items fall under this heading, which includes items like food, cars, stationery, clothing, electrical appliances, shoes, TVs etc. The channel of delivery employed for different items is rarely the same. Channels differ for different types of products. Study the Figure below with care. It gives a good idea of the distribution channels for some customers. At times, customers order directly from the factory or make a purchase through a catalogue. Goods of higher durability such as clothing, furniture, cars, shoes, textbooks etc. are usually distributed through retailers. In some instances, showrooms can even be set up by a manufacturer which takes up the retail trade. Other consumer goods like stereos, auto parts, video cameras etc. are dispersed through wholesalers and retailers. Daily-need consumer goods like food grains, sugar, soap, oil, salt, paper, pencils, etc. are usually delivered through a broker or an agent, wholesaler and retailer.

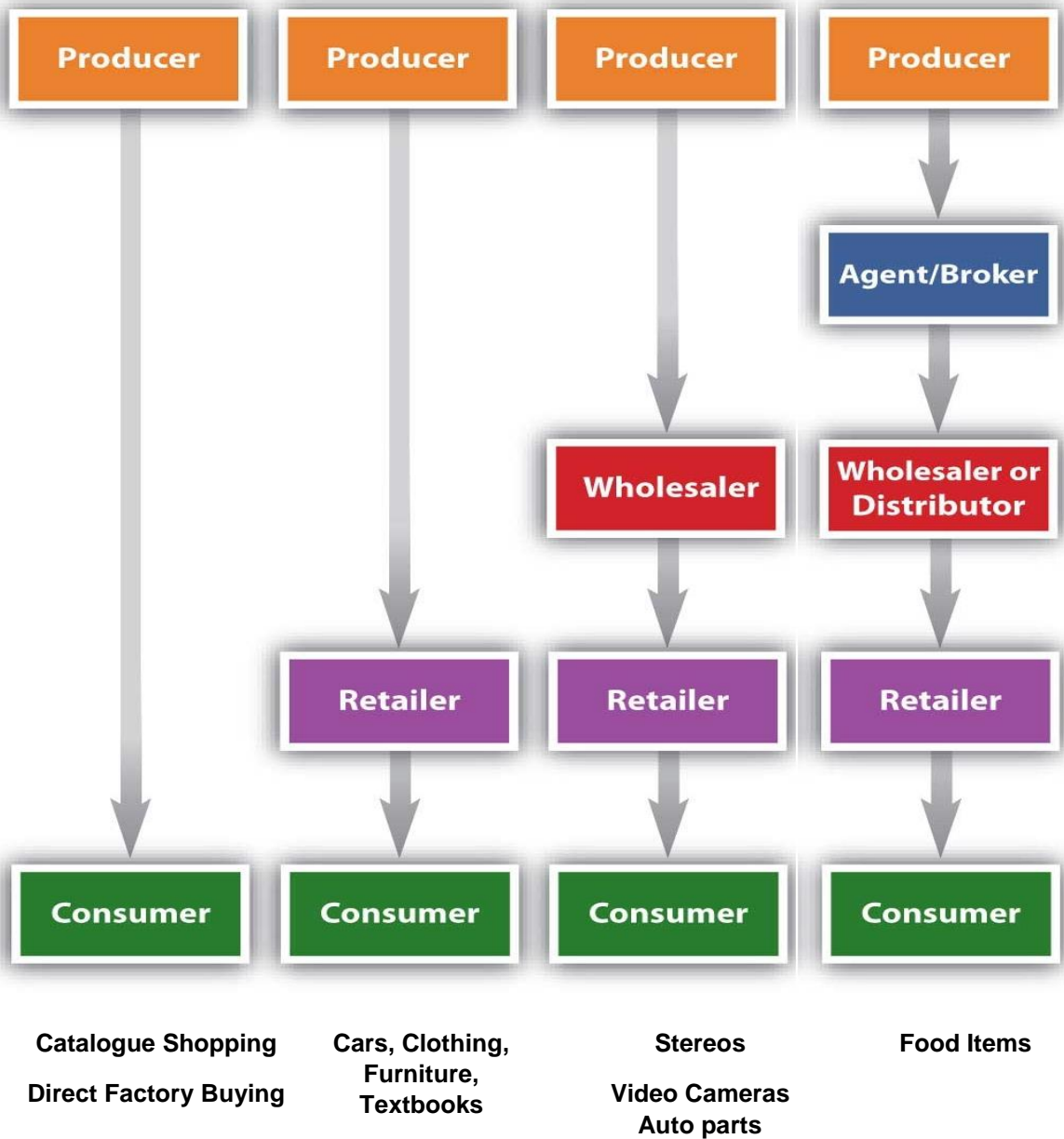
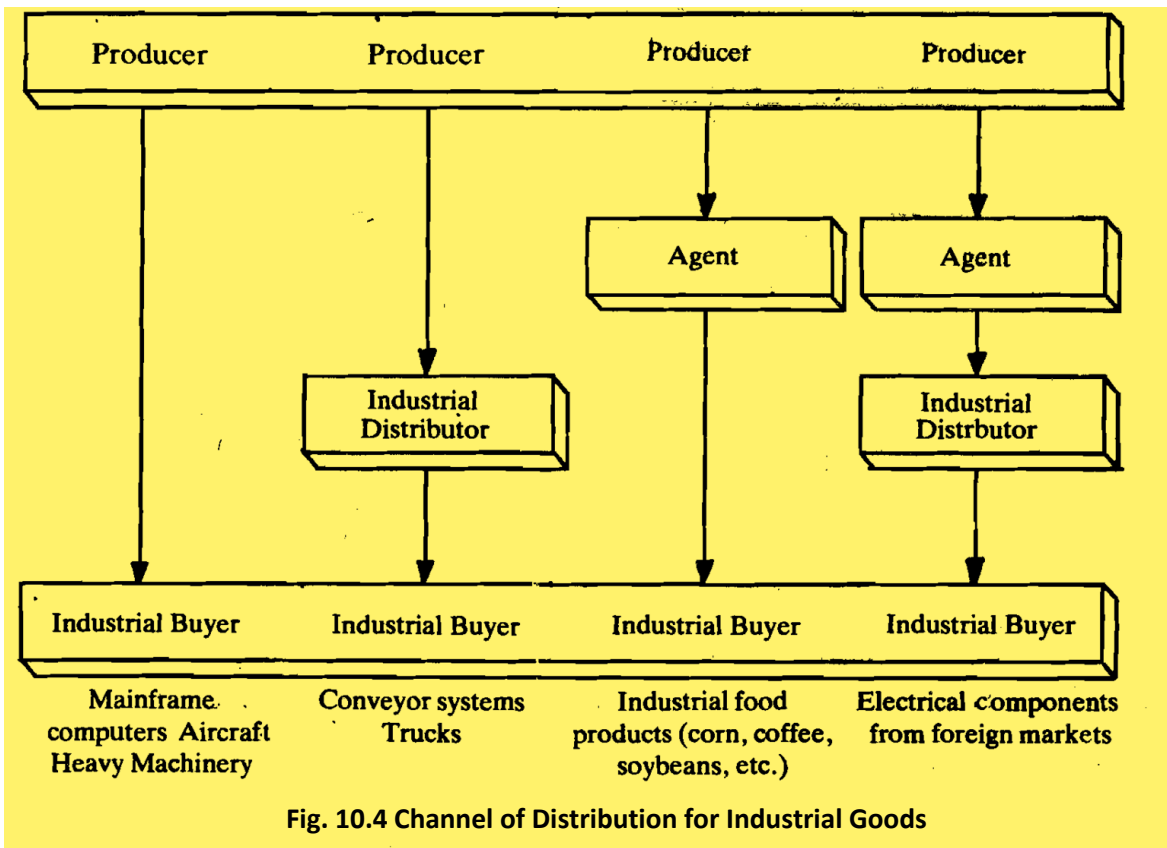


Fig. 10.3

Channels of Distribution Used for Industrial Goods

As you may have guessed, the goods that are consumed so that *other* goods may be produced are known as industrial goods. This category includes a large variety of products, such as machinery, raw materials (e.g. sugar cane, coffee, cotton, iron ore, oil seeds, electronic components etc.) and equipment. Distribution channels are not the same for the products covered in this category. Study the Figure below. It shows the main channels of distribution for selected industrial goods. Mainframe computers, aircraft, and heavy machinery, etc., - these kinds of high-value goods are delivered to the buyers directly. In cases

like this, producers secure orders by mail or online using catalogues and price lists. In some situations, salesmen may be used to contact the buyers. Comparatively cheaper items like conveyor systems, trucks etc. are delivered through distributors. As you may know, industries also consume a lot of agricultural products. For example, tea leaves are treated to develop tea powder used to make drinking tea. Additionally, other agricultural products like coffee, corn, soybeans, etc. are acquired by industrial purchasers through middlemen. If electrical components are brought in from outside the country, they are acquired through an agent and an industrial distributor.



Factors Influencing the Choice of Channel

As you can see, there are many different channels used in the distribution of merchandise. We have seen direct channels and indirect channels, but there are also short channels along with long channels. We have learned that different types of channels are appropriate for different kinds of merchandise. Where there are multiple channels available to a manufacturer, choosing the proper channel becomes a critical decision. The main criteria behind choosing a channel for dispersal of goods should be such that the chosen medium meets the requirements of the customers in the various markets at a realistic cost. The aspects that usually affect the choice of channel for dispersal of goods can be fitted into four groups as described below:

- 1) Market considerations
- 2) Product considerations
- 3) Middlemen considerations
- 4) Company considerations

Product Considerations

1. **Perishability:** The type of merchandise determines the choice of channel chosen. Perishable items like eggs and milk, etc. have to be supplied directly or through short channels. Choosing long channels can lead to the goods being spoiled by the time they make it to their destination and to the customer. This is why perishable items have to be quickly passed through short channels.
2. **Bulkiness:** Where heavy or bulky products are concerned (e.g., cement, steel, heavy machinery, etc.) and distribution and handling expenses are greater, again short channels are preferable. Conversely, long channels are more appropriate for lightweight and smaller-sized items like readymade garments, certain materials, toothpaste, stationery etc.
3. **Product Technicality:** Complex electronics and electrical equipment that needs handling care is usually dispersed directly or through short channels. In cases where things like Xerox machines or computers are concerned, a large amount of pre-sale and after-sales service is required. Wholesalers and retailers are not always able to provide this, so producers frequently distribute them directly. Products involving simple mechanics like electronic toys, clocks, etc. can easily be supplied through a longer channel for more extensive distribution.
4. **Product value:** The unit price of the product is another important aspect that has to be taken into account, when deciding the channel of distribution. Usually, longer channels are preferable for products with low unit value. However, short channels may at times be equally economical. This happens when such products are sold as a part of a bulk sale, in combination with other goods.

Market Considerations

1. **Customer size:** If customer quantity is big, long and multiple channels are required for extensive dispersal of goods. Short channels and direct selling are feasible when a small customer base buys large volumes on regular basis, and if they are located in a relatively small area.
2. **Probable sales volume:** The target volume of the manufacturer also plays a role in the choice of channel. The sales volume and the ability to reach the target consumer varies in different channels. If a single outlet is insufficient for reaching the target, additional channels have to be used. Naturally, the competition also has to be considered when looking at the potential volume of sales through the varying channels.
3. **Concentration of buyers:** If the buyers are located in a few limited areas, the manufacturer can set up its own sales divisions in those areas and sell directly to the buyers. So, short channels

are feasible where buyers are limited to a few localities. Conversely, if buyers are scattered over a large geographic area, short channels can become expensive and the producer may have to use several long channels.

4. **Purchase order size:** When large-scale purchases are involved, the manufacturer can distribute directly or by using short channel distribution. Long channels are more cost-effective in situations where purchase orders are not large enough to justify direct sale.

Middleman Considerations

1. **Types of middlemen:** Another factor when selecting a distribution channel is the suitable availability middlemen. This is because the middleman performs a variety of functions like standardization, packing, grading, storage, branding, post-sales service etc. All these functions are determined by the size, financial position and location of the middlemen. If the middleman in a given channel is dependable and proficient, that channel may be preferred by manufacturers.
2. **Channel competition:** Manufacturers compete with one another to gain the services of certain wholesalers in some situations. Wholesalers also frequently compete with one another for the attention of retailers, or to display certain brands of goods. At times manufacturers use the same channels as those used by their competitors. If one manufacturer makes arrangements for exclusive dispersal through a given wholesaler, the other manufacturers also follow suit. So, channel selection is partially dependent on the prevailing competition in the distributing system.
3. **Middlemen availability:** Some producers may wish to use the services of a certain group of middlemen. However, such middlemen may not be free in the market. They may be booked-up with the competitors' goods and may not want to take on additional product lines. In this case, the producer has no choice but to use whoever is available in the market at the time.

Company Considerations

1. **Distribution costs:** The extensive variety of functions carried out in the channel of distribution adds extra distribution costs. So, the distribution costs of every channel have to be calculated and its effect on the final price to consumer analysed, before a distribution channel is selected. The least expensive channel is normally the channel selected. At other times, a channel that is more convenient for the consumer is selected, even if it is more expensive. In these cases, customer convenience is given priority over the cost of distribution.
2. **Long-run effect on profit:** All modes of distribution - direct distribution, long channels, and short channels - have differing implications when it comes to profits in the long-run and short-run. If product demand is high, then reaching the biggest number of customers by using multiple channels may become more profitable. However, demand can dwindle as more competitors enter the market. In which case, it may no longer be profitable to use more than one channel or long channels. Before deciding on the final mode of distribution therefore, future market trends have to be kept in mind.

3. **Experience and ability:** A producer with experience and marketing know-how may wish to distribute their own goods. But producers that are not well-versed in marketing would generally rather use middlemen.
4. **Financial strength:** To properly establish a distribution system, strong financial resources are needed. So, only a financially strong manufacturer can establish his/her own distribution system. A weaker organisation may have to rely on middlemen.
5. **Extent of channel control:** Manufacturers wishing to maintain full control over distribution of their goods find short channels better. Being able to control channels is important in aggressive promotion, to keep stocks fresh and manage retail prices.

Hence, before making a selection, the manufacturer has to think through all objectives, assets, and available channels. They also need to keep in mind the type of product and the buyer's characteristics. They should use the channel that provides a mixture of sales volume and costs that provide the biggest profit.

Since there are no set rules, the producer will have to decide based on personal experience and judgement. The majority of the manufacturers make use of a number of channels to make sure that their goods get to the greatest number of people possible.

A manufacturer's job does not end with the selection of the distribution channel. They have to carry out regular checks to make sure good service is provided, keep an eye on developments relating to dispersal of goods and attempt to improve marketing methods on a constant basis. They may come to understand that the best channel when the product was initially introduced is not longer the most effective one, after the produce is accepted in the market. Here are some of the ways to evaluate the channels:

- (i) Through sales performances;
- (ii) Marketing abilities;
- (iii) Motivation to enhance sales volume;
- (iv) The amount of competition faced;
- (v) Prospects of growth.

As pointed out earlier, the number of levels in a channel can vary from one – which is the simplest, most direct (manufacturer to user) - all the way up to three levels, depending on a number of factors. Once the number of levels is decided, then the number of intermediaries has to be decided at each level. Now comes the question of distribution intensity. This refers to the number of intermediaries at every stage of the process. For example, say that the producer of refrigerators decides to go for a single-level structure made up of the producer, retailer and consumer. The decision regarding

intensity of distribution in this situation concerns the number of retailers that will be carrying the firm's goods. Simply put, will a few retailers be trusted with the job of distributing them, or will a large number of retailers be used to distribute the goods? In general, just three options are open to a business when it comes to intensity of distribution.

These are:

1. Intensive Distribution;
2. Selective Distribution;
3. Exclusive Distribution.

1. **Intensive Distribution Policy:** This deals with the sale of goods through a large number of outlets. This policy focuses on giving the product the maximum possible exposure available in the market for sale. Usually, it is convenience goods producers like soft drinks, cigarettes, eggs, bread, soap, biscuits, toothpaste, etc. that adopt this intensive distribution policy. All of these items have a low unit cost, are normally purchased repeatedly and have a large turnover. The aim of this policy is to reach each and every potential customer, so that not a single opportunity to make a sale is missed. This policy allows a firm to spread distribution costs over a larger network of dealers and keep communication delays to the minimum. However, the policy is an expensive one, as the firm is stuck with collecting and serving small orders from a great many outlets.
2. **Selective Distribution Policy:** As the name implies, this type of policy places a restriction on the number of outlets that will be allowed to carry the item. So, unlike making use of all the possible intermediaries at a given level, only a limited number of outlets are chosen to display the product. Manufactures of merchandise like washing machines, TV, motorbikes, scooters etc. (types of items for which customers are happy to travel further) usually choose selective distribution. The policy is better-suited to products with preferences of brand, because the customers of such items are expected to approach the channel employed by the manufacturer. Since the marketing firm does not have to spread its work over a large number of outlets, it is cheaper than the intensive distribution policy. Lastly, it allows the manufacturer to secure adequate market cover with more contracts compared to an intensive policy.
3. **Exclusive Distribution Policy:** In this policy, very few select dealers are given the right to disperse the firm's goods in their areas. Under this policy, the manufacturer and middlemen have an agreement. The firm agree to channelize the products exclusively through the chosen middleman, either in all of the market or a part of it. The middleman in turn agrees to serve the manufacturer exclusively in terms of the goods handled and the market served. When an agreement is made with middleman agent, it becomes known as the only selling agency. But when this type of agreement is between manufacturer and a merchant, it becomes known as a dealership at wholesale level and distributorship at retail level.

The exclusive distribution policy is more appropriate for items that are slow to move, come with an enhanced unit value and need post-sales service. That is why many motor vehicle manufacturers use exclusive distribution policies for their products. This type of exclusive distribution policy allows for enhanced control over prices, services, and promotions, etc. by the firm manufacturing the product. exclusive distribution is normally used up when the producer wants more forceful aggressive by the middleman, or when more control over distribution is of key important. Another benefit of exclusive distribution is that it promotes and targets specialisation for the dealer, which in turn yields better after-sales services for the customer. However, issues may arise in gaining the cooperation of dealers in the first place. Therefore, there is the need for vigilant management of the channel members within this arrangement.

The decision regarding the strength of distribution is a critical factor of channel structure, and is quite often said to be a main factor in the organisation's basic marketing plan. It is also an indication of the organization's overall business procedures. For instance, a marketing plan that aims to blanket the market with a product will need a channel structure that can provide the highest-level distribution force

However, low intensity or an enhanced degree of selectivity will have to be constructed into the channel format, when marketing strategies concentrate on a cautiously-selected target market. Usually when an organization's basic marketing policies need mass acceptance for its goods, intensive distribution is utilized. Whereas, when a policy requires more focused segmentation, more selective channels are employed.

Further Reading:

- ✓ **Distribution Channels: Understanding and Managing Channels to Market, (2011), By Julian Dent**
- ✓ **Managing Channels of Distribution, (1998), By Kenneth Rolnicki**
- ✓ **Channel sales and management in distribution, (2011), By Robert Hastings**