UNIT-4

Channels of Distribution

Learning Outcomes
By the end of this unit the learner will be able to:
✓ Explain the meaning and role of distribution channels in overall marketing of products ✓ Explore various functions of the channels of distribution

Unit 4

Channels of Distribution

Product and pricing are the two important aspects of marketing mix that you have already studied about. However, one has to realise that just creating a good product, with all the wished for qualities, beautiful packing and branding, and reasonable prices do not necessarily lead to the success of markets. 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 the distribution choices and strategies related to force of distribution will all be explored in detail.

What is a Channel of Distribution?

Distribution system deals with moving goods from where they are produced to the point where they will be consumed. The main players in the d Distribution System are

i) manufacturers;
ii) Intermediaries;
iii) facilitating agencies;
iv) consumers.

Manufacturers are responsible for producing the product. This is the point where distribution system begins. The next category of participants i.e. the intermediaries, take part in direct talks between sellers and buyers whether they take the goods or not. Intermediaries seek out manufacturers that produce varying products, pinpoint the needs of the customer, and dispense them. In the process, the carry out a number of functions like selling, assembling, buying, standardizing and packing, grading, bearing risks etc. Besides intermediaries, independent business firms like facilitating agencies also exist. Such agencies make possible the unhindered 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 himself.

The channel of distribution is mostly involved with the second participant i.e. 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 effected either through 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 middle men 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 in 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 a majority of the situations, goods are manufactured in one location while they are utilised at a large number of other places and 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 it turns into a waste. A distribution channel aids in the movement of merchandise from the producer to the customer and therefore, gives utility to the products.

Another that springs up is the time difference between the time of production and when it is consumed. All merchandise 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 the rainy season, woollen clothing is only used in the winter season. 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 the farmer 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 a convenience value. Distribution channel allows the consumer to get the goods at a price that he is ready to pay and under conditions which are satisfactory to him with the pride of ownership. In this way it creates the possession utility. To restate, the distribution channel that shifts goods from where they were manufactured and makes them available to the customer at the right place, time, and form.

Functions of Channels of Distribution

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

1) Transactional Functions;
2) Logistical Functions; and
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. Players 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, title to goods change hands, and merchandise flows from the manufacturer to consumer. If no one is 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 form the manufacturer with the aim of selling it at a profit. However, he 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 switching of goods are known as logistical functions. The distribution channel carries out certain functions like storage, assembling, grading and transportation that are imperative for physical exchange of merchandise. Good are manufactured in great enough quantity so a sufficient selling and shipping quantity is available. At times, it becomes necessary to put together a big number of products so a variety of items wanted by buyers can be available. Grading and packing of merchandise helps in 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 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 final consumer.
3. **Facilitating Functions:** These functions aid both the transaction along with the physical switching of goods. These assistance functions of channel include after purchase service and upkeep, financing, market information etc. Sellers give all required information to buyers along with after sales service and financial help in the way of sale on credit. Likewise, traders are frequently steered by producers to aid them in making sales, and the traders usually inform manufacturers about the customer preferences and opinions about products. In this was 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 case of perishable materials and heavy duty materials like coal, iron, petroleum products, whereas in 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 character of channels of distribution. We will now cover channels of distribution most employed by manufacturers. These can only be grouped into two groups:

i. Direct channels and
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 use the post office. Orders are booked from the customers who contact you by mail, telephone or respond to letters and advertisements mailed to their homes directly. The goods are delivered to them through mail or some other carrier. The next alternative is to set up your own retain 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 case of some products, it is just not feasible for the manufacturer to supply merchandise to the customer directly. So, middlemen agents such as, retailers, mercantile, and wholesalers participate in the distribution channel, which is known as the indirect channel. As it 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 retailers at regular intervals and supply the merchandize according to needs. If the need arises, the retailer has the option of securing merchandize form 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 his products in bulk to wholesalers. The retailer in turn has the option of buying from the wholesaler periodically, and then turning around and selling to customers located in his 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.

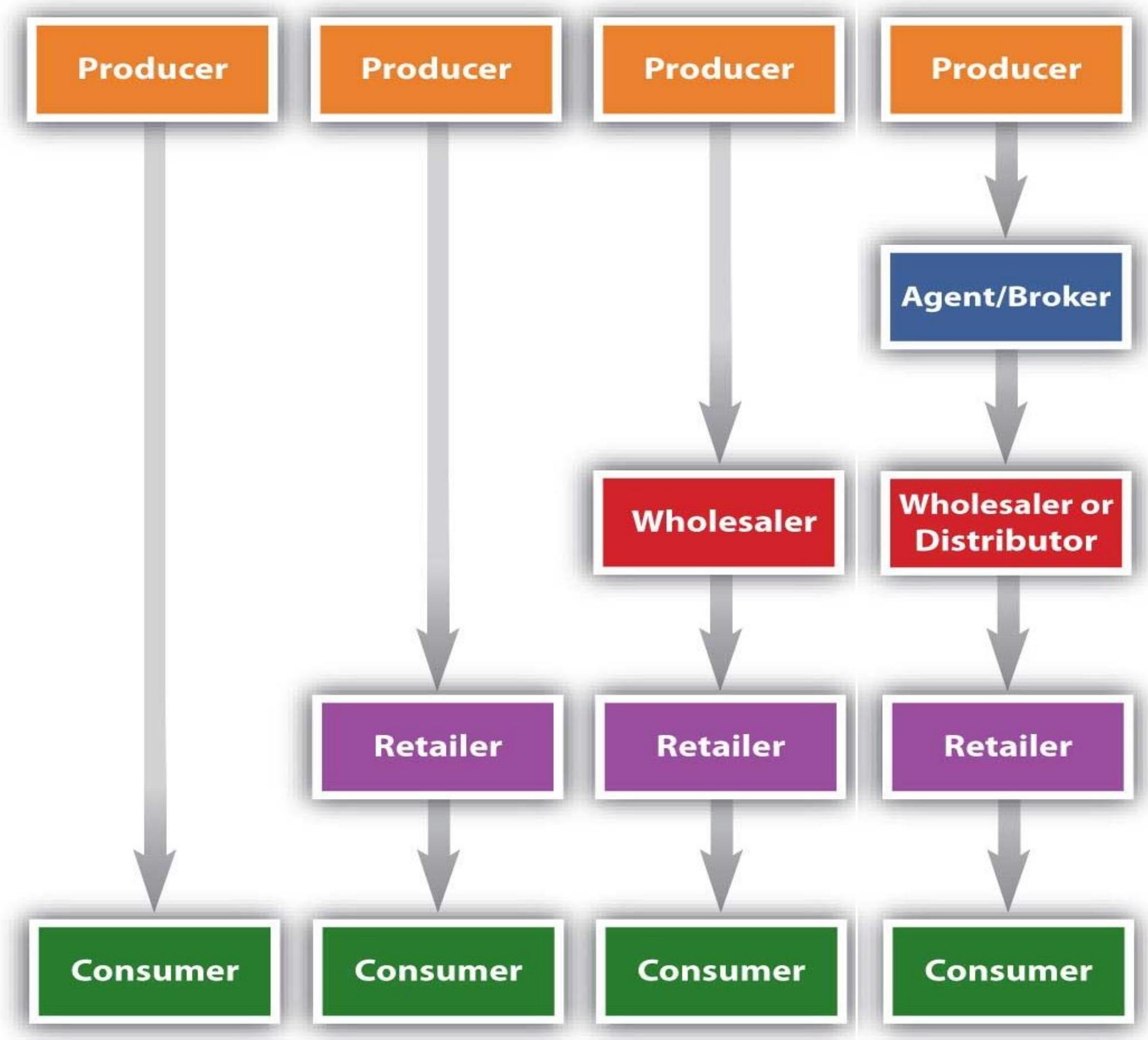
Then, the wholesalers purchase the goods from these agents and sell them to retailers. The retailer finally carries out sales to the final consumer. This kind of channel is called as the three level channel, as there are three kinds of middlemen through whom distribution takes place. As we have seen there are a number of prevalent methods of distribution. From the manufacturer's stand point, the greater the number of middlemen employed, the poorer his 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 items, cars, stationery, clothing, electrical appliances, shoes, transistors, Tand V sets etc. The channel of delivery employed for different items is not 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 of the 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 setup by the manufacturer which takes up the retail trade. Other consumer goods like stereos, auto spare parts, video recorders etc. are dispersed through wholesalers and retailers. The daily need consumer goods like food grains, sugar, soap, edible oil, salt, paper, and pencils, etc. are usually delivered through a broker or an agent, wholesaler and retailer.



Catalogue Shopping
Direct Factory Buying

Cars, Clothing, Furniture, Textbooks

Stereos
Video Recorders
Auto parts

Food Items

Fig. 10.3

Channels of Distribution Used for Industrial Goods

As you may have guessed, the goods that are consumed so 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. sugarcane, coffee, cotton iron ore, oilseeds, electrical, and 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., the high value goods are dispersed to the buyers directly.

In cases like this producers gain orders by mail using catalogues and price lists. In some situations salesmen may be used to contact the buyers. The comparatively cheaper items like conveyor systems, trucks etc. are delivered through distributers. As you may know, industries consume a number 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 the industrial purchasers through middlemen. If electrical components are brought in from outside the country, they are acquired through an agent and an industrial distributor.

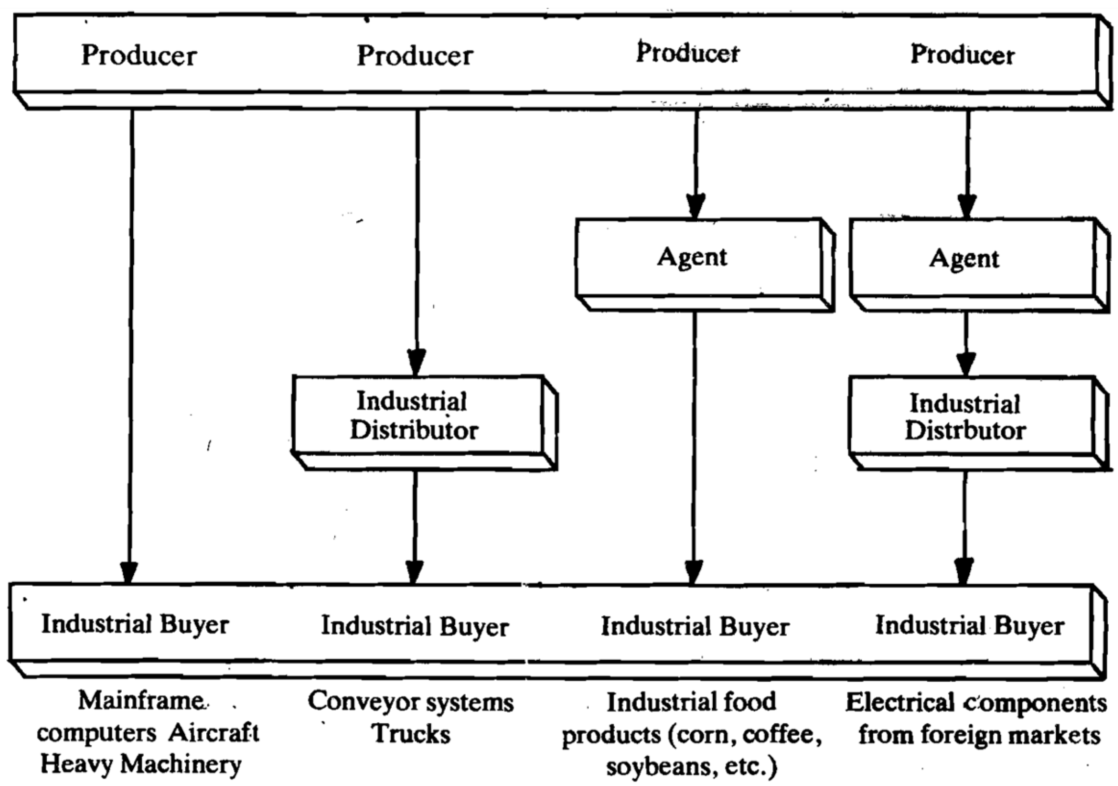


Fig. 10.4 Channel of Distribution for Industrial Goods

Factors Influencing the Choice of Channel

As we have seen there are many different channels used in distribution of merchandise. We have seen direct channels and indirect channels, 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 a variety of channels available to a manufacturer, choosing the proper channel and becomes a critical decision for the manufacturer. 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 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 which channel is chosen. Perishable items like eggs and milk, etc. have to be supplied directly or through short channels. Choosing long channels can lead to the good being spoiled by the time they make it to their destination and finally the customer. That is why perishable items have to be quickly rushed through short channels.

2. **Bulkiness:** Where heavy or bulky products are concerned (e.g., cement, steel, and heavy machinery, etc.) and distribution and handling expenses are greater, again short channels are preferable. Conversely, long channels are more appropriate for light-weight and smaller sized items like readymade garments, dress material, pocket calculators, toothpaste, stationery, and toothbrush, etc.

3. **Product Technicality:** Complex electrical and electronics equipment that need handling care are usually dispersed directly or through short channels. In cases where things like Xerox machine or computers are concerned a large amount of presale and after sales service is required. Wholesalers and retailers are not always able to provide this, so producers frequently just distribute them directly. Products involving simple mechanics like electronic toys, time-clocks, etc. can easily be supplied through the long 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, at times, short channels, too, may 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 several 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 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 sale 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 can be feasible where buyers are limited to a few localities. Conversely, if buyers are scattered over a large geographic area, short channels can become quite expensive and the producer may have to end up using several long channels.
4. **Purchase order size:** When large scale purchasers are involved, the manufacturer can distribute directly or by using short channel. Long channels are cost effective in situations where purchase orders are not large enough to justify direct sale.

Middleman Considerations

1. **Types of middlemen:** another point in the choosing of a distribution channel is the suitable availability of a middleman. 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 size, financial position, location of the middlemen. If the middleman in a given channel is dependable and proficient, then that channel may be preferred by manufacturers.

2. **Channel competition:** Manufacturers contest with one another for gaining the services of certain wholesalers in some situations. Wholesalers too frequently compete with one another for attention of some retailers or for displaying certain brands of goods. At times manufacturers use same channels as those used by their competitors. If one manufacturer makes arrangements for exclusive dispersal through a given wholesaler, then 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 desire to use the services of a certain group of middlemen, however, such a class of middlemen may not be free in the market. They may be booked 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.

Company Considerations

1. **Distribution costs:** The large variety of functions carried out during the channel of distribution adds extra cost to distribution. So, the distributions cost of every channel have to be calculated and it effect on final price to consumer analysed before a distribution channel is selected. The least expensive channel is normally 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 all have differing implications when it comes to profits in the long-run and short-

run. If the product demand is high, then reaching the greatest number of customers by using multiple channels may become more profitable. However, demand can dwindle as more competitors enter the market. In that case, it may no longer be profitable to use more than one or long channels. So, before deciding on the final mode of distribution, 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 his own goods. But producers not well versed in marketing, would much rather use the middlemen.

4. **Financial strength:** To properly establish a Distribution System, strong financial resources are needed. So, only a financially strong manufacturer can establish his own Distribution System. A weaker organisation may have to rely on the middlemen.

5. **Extent of channel control:** Manufacturers wishing to maintain a strong control over distribution of their goods, such as, short channels better. Being able to control channels is important in aggressive promotion, to keep stocks fresh, and retail prices.

   Hence, before making a selection, the manufacturer has to think through his objectives, assets, and available channels; he also needs to keep in mind the type of product and buyer characteristics. He should use the channel that provides a mixture of sales volume and costs that provide the greatest profit.
   Since there are no set hard and fast rules, the producer will have to decide based on his own 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.
   A manufacturer's job does not end with the selection of the channel of distribution. He has to maintain regular checks to make sure good service is provided keep an eye on developments relating to dispersal of his goods and attempt to improve his marketing methods nonstop. He may come to understand that the best channel when the product was initially introduced is not longer the most effective one, once the produce is accepted in the market. Here are some ways to evaluate the channels.

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

As pointed out earlier, the number of levels in a channel can vary from one, 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.

No comes the question of distribution intensity. This refers to the number of intermediaries at every stage of the marketing. Assuming that the producer of refrigerators decides to go for a single level structure made up of producer, retailer and consumer. The decision regarding intensity of distribution in this situation has to deal with the number of retailers who will be carrying the firm's goods. Simply put, will a few retailers be trusted with the job of dispersing or will a large number of retailers be used to distribute the goods. In general, just three options are open to the firm regarding 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 targets giving the product the greatest possible exposure to the item available in the market for sale. Usually it is the convenience goods producers like soft drinks, cigarettes, eggs, bread, toilet soap, biscuit, chewing tobacco, and toothpaste, etc. that adopt this intensive distribution policy. All of these items have a low unit cost, and 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, after a very selective process, only a limited number of outlets are chosen to display the product. Manufactures of shopping merchandise like fans, fabrics, washing machines, TV, coolers, mopeds, and scooters, etc. (types of items for which customers will go the extra mile) usually choose Selective Distribution. The policy is better suited for 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. Inclusive of the marginal ones, it is cheaper than the intensive distribution policy. Lastly, it allows the manufacturer to secure adequate market cover with more contracts compared to intensive policy.

3. In this policy, just a 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 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 an 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 those items that are slow to move, come with an enhanced unit value and need post sales service. That is why many motor cycle, scooter, car, and truck, etc. manufacturers use exclusive distribution policy for their products. This type of Exclusive Distribution Policy allows the most control over prices, services, and promotions, etc. by the firm manufacturing the product. Exclusive Distribution is normally taken up when the producer wants more forceful selling by the middleman or when more control over dispersal seems to be important. Another benefit of exclusive distribution is that it gives rise to specialisation for the dealer which in turn yields better after sales services for the customers. However, issues may pop up in gaining the cooperation of dealers. Therefore, there is the need for vigilant management of the channel members with this arrangement.

The decision, regarding the strength of distribution, is a critical factor of channel structure and is quiet frequently thought 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 drape the market with a product will need a channel structure that can provide the top level of 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 cautiously selected target market. Usually when an organization's basic marketing policies need mass acceptance for its goods, intensive dispersal is utilized. Whereas, when a policy requires stressing 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***