The Design and Management of Marketing Channels 2
Overview

Refresher
- Coordination
- Incentives

Solutions
- Channel Design
- Channel Management
Refresher
Coordination and Incentives

Coordination
Decisions are mutually dependent

Incentive Conflicts
Goals not aligned
When is Coordination Difficult?

Too many decision makers
  – large firms

Decision makers too far from information
  – May Company

Specialization
  – different languages (May Company)
  – different information systems (Continental)

Incentive problems
  – Continental
Incentives: When Do Problems Arise?

Goals not congruent

– Within firms: vacations
– Between firms: wholesale price

Implications

– Distort information
– Distort actions and decisions

Relationship between incentives and coordination
Solutions

Channel Design
- Resources
- Coordination
- Incentives

Channel Management
- Contracts
- Co-location
- Standardization
- Exclusivity
Channel Design
Does Outsourcing Help or Hinder Coordination?

Helps: Coordination is difficult at large firms
   – Decision makers too far apart (decentralized)
   – Decision makers too far from information (centralized)

Hinders: Coordination is difficult between firms
   – The procurement process (Knez and Simester)
   – More decision makers (Burger King)
   – Proprietary information (Continental)
   – Harder to standardize (Continental)
   – Co-location less likely
Channel Design
Does Outsourcing Help or Hinder Incentive Issues?

Helps: if goals are consistent
- Owners are more motivated than managers
- Example: owners are better at supervising employees than managers

Hinders: if goals are inconsistent
- Example: Burger King cannot implement the McDonald’s ordering system
Two Intermediate Solutions

1. **Hybrid channels**
   Channel conflict (State Farm)

2. **Outsourcing is not the only option**
   Vertically integrated *Chicago Tribune*
   Franchising *Pizza Hut*
   Licensing *Tiger Woods*
   Cooperatives *Ace Hardware*
   Joint Venture *Sematech*
   Strategic Alliances *Coke and McDonalds*
   Outsourced *Nike*
Franchising

Resources
- Means of raising capital / sharing risk
- Human capital

Incentives
- Owners instead of managers
- Objectives of franchisor and franchisee not perfectly aligned
- Must credibly signal demand to initial franchisees
- Franchisees often slow down and balk at ongoing royalties

Coordination
- Decision-makers closer to the information
- More decision-makers
Joint Ventures

Resources
- Success depends upon complementary resources
- Common reason for failure: parents fail to contribute

Incentives
- Objectives aligned within the joint venture but not with parents
- More likely to fail if parents compete

Coordination
- Standardization and co-location within joint venture
- Remove proprietary concerns within joint venture
- Resulting organizations often smaller
- An additional decision-maker
Bose: JIT Program

Coordination
Standardize (information systems)
Co-locate
No negotiating of prices

Incentives
Owners watch over suppliers’ employees
Give suppliers market power
Channel Management

Use contracts to align objectives

Co-location

Standardization

Exclusivity
Contracts

Enforcement
- Input measures (accountants)
- Output measures (sales people)

Complexities
- Multiple tasks
- Group performance
- Uncertainty
Exclusive Distribution
Guarantee not to supply competing retailers

Benefits
Aligns objectives
Facilitates coordination: fewer retailers to contact
Economies of scale

Costs
Risk is less diversified
May lose market coverage
Give retailers some market power
Harder to measure performance
Summary

Channel Design: perform the task yourself
– Are your resources suited to the task?
– Will the firm become too big to coordinate?
– Who is easier to manage: owners or managers?

Channel Management
– Use contracts to align incentives
– Co-location
– Standardization
– Exclusivity