Segmenting, Targeting and Positioning Channel Design

Channel design: Segmentation

One of the fundamental principles of marketing is the segmentation of the market. Segmentation means the splitting, of a market into groups of end-users who are

(1) Maximally similar within each group

(2) Maximally different between groups

For the channel manager, segments are best defined on the basis of demands for the outputs of the marketing channel. A marketing channel is more than just a conduit for product; it is also a means of adding value to the product marketed through it. In this sense, the marketing channel can be viewed as another "production line" engaged in producing not the product itself that is sold, but the ancillary services that define how the product is sold. These value added services created by channel members and consumed by end-users along with the product purchased are called service outputs. Service outputs include (but may not be limited to) bulk-breaking, spatial convenience, waiting and delivery time, and assortment and variety.

End-users (be they final consumers or business buyers) have varying demands for these service outputs. Consider, for example, two different soft drink buyers: an office employee at work, looking for a soft drink during her afternoon coffee break, and a family buying for at-home consumption. The office employee has high demands for all service outputs except assortment and variety (for which her demand is moderate, implying willingness to brand switch within reason), whereas the family has the opposite pattern of service output demands. Clearly, a different marketing channel meets the needs of these two segments of shoppers. The office employee cannot travel to a grocery store to buy a can of soda during her break, nor does she want to buy a six-pack or more of cans of soft drinks. She is willing to pay a slightly higher price for the convenience of getting just a single can of soda close to her office. A vending machine would be an ideal retail outlet for her. The family, on the other hand, would not find the vending machine an attractive retail purchase alternative. The family's demand for assortment and variety may not be met by a vending machine, and other service outputs are offered at too high a level, resulting in a higher per-unit price than the family wants (or needs) to pay. A local super market does a better job of meeting the family's service output demands for soft drinks. This example shows how the same product can be demanded with a widely varying set of service outputs, resulting in very different demands for the product-plus service-output bundle by different segments of end-users. An analysis of service output demands by segment is thus an important input into a manufacturer's marketing plan, and can help increase the reach and marketability of a good product to multiple market segments.

Service Output Demand Differences in soft drink market

SERVICE OUTPUT	FAMILY		OFFICE EMPLOYEE	
	DESCRIPTOR	SERVICE OUTPUT DEMAND LEVEL	DESCRIPTOR	SERVICE OUTPUT DEMAND LEVEL
Bulk breaking	"I buy groceries weekly for my family, and all of us like soft drinks."	Low	"I'm on my coffee break and I have time for only one can of soft drink."	High
Spatial convenience	"I drive to the supermarkets in my area to shop."	Low	"I have only 15 minutes for my break, so I need to buy whatever is handy."	High
Waiting and delivery time	"We usually have some extra cans of soft drinks in the house, so I'll just come back the next time if I can't find the soft drinks I want on this trip."	Low	"If I don't get my soft drink right "at 3:00 when my break starts, I'll never have a chance to go back later arid get one."	High
Assortment and variety	"My husband and I like Coke and Pepsi, but our kids aren't permitted to drink caffeinated soft drinks. They like caffeine free fruit-flavored soft drinks."	High	"I can't be too particular about which soft drink I pick. It's important to me to get one, as long as it has caffeine."	Moderate

Channel design: Targeting

At this stage of the analysis, the channel manager is equipped to decide what segments to target. This also means that the channel manager is now equipped to decide what segments not to target! Knowing what segments to ignore in one's channel design and management efforts is very important, because it keeps the channel focused on the key segments from which it plans to reap profitable sales.

A question arises that why not target all the segments identified in the segmentation and positioning analyses. It requires the channel manager to look at the internal and external environment facing the channel. Internally, managerial bounds may constrain the channel manager from implementing the zero-based channel. For example, top management of a manufacturing firm may be unwilling to allocate funds to build a series of regional warehouses that would be necessary to provide spatial convenience in a particular market situation. Externally, both environmental bounds and competitive benchmarks may suggest some segments as higher priority than others. For example, legal practices can constrain channel design and hence targeting decisions. Many countries restrict the opening of large mass-merchandise stores in urban areas, to protect small shopkeepers whose sales would be threatened by larger retailers. Such legal restrictions can lead to a channel design that does not appropriately meet the target segment's service output demands, and may cause a channel manager to avoid targeting that segment entirely.

Of course, the corollary of this statement is that when superior competitive offerings do not exist to serve a particular segment's demands for service outputs, the channel manager may recognize an unexploited market opportunity and create a new channel to serve that under served segment. Meeting previously unmet service output demands can be a powerful competitive strategy for building loyal and profitable consumer bases in a marketplace. But these strategies can best be identified with knowledge of what consumers want to buy, and importantly, how they want to buy it, and the necessary response in terms of channel flow performance and channel structure.

Channel design: Positioning

When the market has been segmented into groups of end-users, each of which can be described by a set of service output demands and targeted thereafter, the channel manager should next define the optimal channel to serve each segment. This is called positioning or configuring the channel (positioning to parallel the segmentation-targeting-positioning paradigm in marketing management). Just as positioning a product means setting its product attributes, price, and promotional mix to best fit the demands of a particular segment, so also positioning refers to the design of the distribution channel to meet the segment's demands. This exercise should be done, even if the channel ends up not selling to some of the segments in the end. The channel analyst may then discover that some segments simply do not make good targets because their demands cannot be adequately met with the channel's current resources. Alternatively, the positioning exercise may reveal some unexpectedly attractive segments to target. Unless the optimal channel is defined for each segment, it is impossible to make a thorough decision about what segments to target.

The optimal channel is defined first and foremost by the necessary channel flows that must be performed in order to generate the specific segment's service output demands. Channel flows are all the activities of the channel that add value to the end user. In enumerating the list of channel flows, we go beyond the concept of the mere handling of the product to include issues of promotion, negotiation, financing, ordering and payment. Each product or service-selling situation can have its unique set of service output demands by segment, implying that the differential importance of different sets of channel flows depends on the segment.

Further, the channel analyst must identify the optimal-channel structure to produce the necessary channel flows, which themselves, of course, result in the generation of the required service outputs that are demanded by a particular segment of end-users in the market. The design of the channel structure involves two main elements. First, the channel designer must decide who are to be the members of the channel. For example, will a consumer packaged-goods manufacturer sell its grocery products through small independent retailers with in-city locations, or through large chain stores that operate discount warehouse stores? Or will it use an outlet such as Indiangrocer.com, an on-line seller of Indian' food and household products that operates no retail stores at all? Moving up the channel from the retail level, decisions must be made whether to use independent distributors, independent sales representative companies (called "reps" or "rep firms"), independent trucking companies, financing companies, export management companies, and any of a whole host of other possible independent distribution channel members that could be incorporated into the channel design.

Beyond this decision, the channel manager must also decide the exact identity of the channel partner to use at each level of the channel. For example, if it is deemed advisable to sell a line of fine watches through retail stores, should the outlets chosen be more upscale, such as Tiffany's, or should they are family-owned local jewelers? The choice can have implications both for the efficiency with which the channel is run and the image connoted by distributing through a particular kind of retailer. In a different context, if a company seeks distribution for its products in a foreign market, the key decision may be which distributor is appointed to carry the product line into the overseas market. The right distributor may have much better relationships with local channel partners in the target market and can significantly affect the success of the foreign market entry.

The other main element of the channel structure is the decision of how many of each type of channel member will be in the channel. This is the channel intensity decision. In particular, should the channel for a consumer good include many retail outlets (intensive distribution), just a few (selective distribution), or only one (exclusive distribution) in a given market area? The answer to this question depends both on efficiency and on implementation factors. More intensive distribution may make the product more easily available to all target end-users, but may create conflict among the retailers competing to sell it.

The channel structure decisions of types, identity, and intensity of channel members all should be made with the minimization of channel flow costs in mind. That is, each channel member is allocated a set of channel flows to perform, and ideally the allocation of activities results in the reliable performance of all channel flows at minimum total cost. This is a nontrivial task, particularly because it involves comparing activities across different companies who are members of the channel.

This exercise results in one channel profile for each segment that is identified in the market segmentation stage of the exercise. Each of these channel profiles is called a zero-based channel, because it is designed from a zero base of operations that is, as if no preexisting channel exists in the market. The concept of a zero-based channel means that the segment's service output demands are met and that they are met at minimum total channel cost.