

Strategies for Reduction of Channel Conflict Caused by Direct Marketing in Electronic Commerce

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I. Introduction

Internet-based business-to-consumer electronic commerce (B2C EC) can provide direct linkages between manufacturers and customers via a manufacturer's web site without traditional distribution channel intermediaries like distributors, retailers, and resellers. The direct marketing through manufacturer's web site would give manufactures more margins by absorbing intermediary markup. Manufacturers know that they can also reduce cost for intermediary control by using the direct Internet channel. But, it can cause channel conflicts and even end to total revenue decrease. One of the main reasons that manufactures hesitate to launch direct marketing channel is channel conflict problem.

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In this paper, we examine and analyze some off-line manufacturers with established off-line channels who successfully introduce direct marketing with minimized channel conflict. And we provide strategies for channel conflict reduction and channel partner's new roles when direct marketing is introduced.

II. Channel Conflict and Direct Marketing

Channel conflict is one of the often-discussed topics in marketing research area. Manufacturers usually manage more than one distribution (or sales) channels. Especially when a manufacturer tries to introduce new distribution chain, partners in established channels resist by refusing to distribute or resell the manufacturer's product or services. A definition of channel conflict is 'competition between two or more different distribution chains to sell the products or services of the same company' [4]. There could be several questions to ask as some check points, before we examine conflicts caused by direct marketing [3].

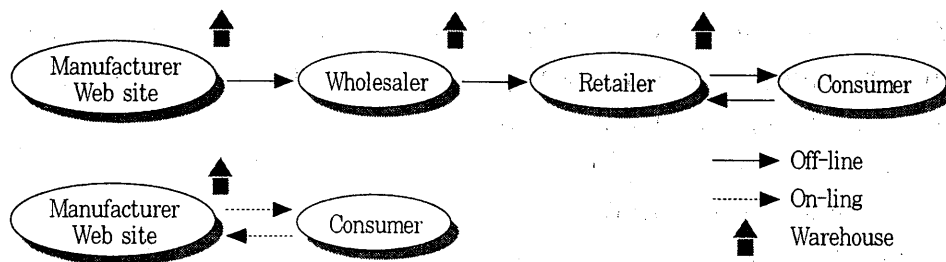
Is more than one channel attempting really the same consumers? Are channel conflicts innocuous and necessary frictions in competitive business environment? Is decreasing profitability of a channel caused by genuinely other channel's encroachment? Is one channel's decline a really harmful to the total revenue of a company? You had better answer these questions, before you plan or do action to deal with channel conflicts.

Channel conflict issues have been researched more than before by marketers, because direct marketing via Internet channel become an important alternative to manufacturers. A fact that sales volume of EC has grown beyond expert's expectation within recent several years means that new sales chain is being established [4] [9] [e]. One type of EC, B2C EC makes it possible for manufacturers to sale their product and services directly to consumers without intermediaries like

distributors, retailers, and resellers. Some manufacturers adopted and implemented the B2C direct marketing model and have made a great success within 2 or 3 years. Dell computer and Cisco systems are two manufacturers of the most successful in sales using direct marketing model.

Figure 1 shows us the difference between traditional off-line distribution channel and Internet-based direct marketing channel. At the direct marketing model, you can see that intermediaries are removed. However, manufacturers lose buffers of inventories and should deliver products to consumer's door for himself or by outsourcing to logistics service provider.

<Figure 1> Offline Traditional Channel and Direct Marketing Model



As more manufactures implemented or plan to introduce direct marketing, the more conflicts between on-line Internet and the traditional off-line channels occur. In this paper, we focus conflicts between on-line and off-line channels, and provide strategies for channel conflict resolution for manufacturers who have already had traditional distribution channels.

III. Strategies for Channel Cooperation

Strategies for channel cooperation can be categorized into two groups: conflict minimization and cooperation maximization. Manufac-

turers in the passive position to the traditional channel partners often use conflict minimization strategies. By separating on-line channel from the established off-line channel as possible, channel conflict can be minimized. Cooperation maximization strategies are focused on how to maximize the synergy effects with on-line and off-line channels in the cooperative manner. Companies in the proactive position of on-line channel usually take cooperation maximization strategies.

3.1 Conflict Minimization

Product, price, place, and promotion are four distinct control factors for marketers, when he makes a marketing plan. When manufacturers try to introduce on-line channel and expect to have a channel conflict, these four control variables can be also used as well to minimize conflict. In this section, examples of conflict minimization efforts done by off-line manufacturers are provided.

3.1.1 Product Differentiation

Sony (i) used this strategy in U.S. market. Products such information-related as monitor, CD, game software are ordered and pay at Sony's web site directly, while products of consumer electronics category like TV, DVD, Play Station are sold only at traditional off-line channel. This implies that distributors and retailers of consumer electronics are so strong enough to have negotiation power over Sony. The second implication is that characteristics of a product make an effect on decision whether to use on-line or off-line channel. For consumer electronics, orders taken via web site are forwarded to the nearest dealer of Sony.

Other manufacturers use this product differentiation strategy with various tactics. Gibson Musical Instrument (c) and Harley Davidson (b) sell their main products, electronic guitar and auto-bike at off-line channel only, and accessories of the products are sold at both on-line

and off-line. Web sites also provide community functions and useful information for their mania users. Not only consumers but also dealers can order repair parts via these manufacturer's web sites. View Sonic [k] sells their overstock monitors only at on-line web site.

3.1.2 Price, Place and Promotion Control

The easiest way to handle channel conflict for manufacturers is controlling price at their web site. Because price posting to their own web site can be done just by sending data to web server or data base update, product managers can simultaneously control prices of many products tightly with ease and timely manner. On the other hand, market managers have to do more efforts to control prices for the traditional channel. Sega of America [h], U.S. subsidiary of Japanese game hardware and software manufacturer keeps their on-line price to the same level with off-line channel. Many other manufacturers such as Levis, and Milacron control prices to keep balance with off-line channels.

Another way to deal with conflict is to differentiate their on-line sales channel by regional basis. Nike [g] operates its on-line sales channel only at U.S. market. At its early stage of on-line sale, Nike sold only its premium high-end products in U.S. market. Nike used both product and place differentiation strategies. At now, Nike expands into its all products but still limits within U.S. market. IBM [d] has also used both product and place differentiation strategies. IBM used both on-line and off-line channels, but throw up off-line for PC in U.S. market, and now IBM sells PC only at on-line for U.S. market. IBM's change of its channel strategy is a reaction to cope with Dell's great success in U.S. market.

Sega adopts both price and promotion control. Internet is accepted as a good promotion tool for a marketing on-line. Sega do marketing event of providing free game character-printed T-shirt only for on-line buyers. The event could be a compensation for on-line buyers of Sega,

because buyers of other similar products usually purchase with reduced prices.

3.2 Cooperation Maximization

On-line and off-line channels might be competing each other. But manufacturers can re-designs its multiple channels as a whole to get a synergy effects when they introduce on-line channel.

3.2.1 Profit Sharing

Volume of on-line stock trading has increased sharply in Korean stock market. Commissions of on-line stock trade belonged to an off-line branch where the account is opened. Employees at information system department complain that sales and brokerage revenues should belong to their performances. Commissions of on-line stock trading are now divided fairly by information system and off-line sales part. Another example is of travel agency, Uniglobe [j] gives commission to its branches, when they forward orders of airplane ticket and hotel reservations to Uniglobe. Branches can focus their efforts into the high-value yield products and services such like packaged or customized group tour products rather than simpler and low-value transactions.

A profit-sharing model between on-line and off-line channels can help manufacturers to make sound competitive business environment. Some companies formulate on-line sales part as an independent organization and promote competition publicly.

3.2.2 Cooperative Role Taking

On-line and off-line channel can cooperate each other with many ways. From the manufacturers point of view, the traditional channel partners have done lots of roles and functions such as inventory buffer, providing consumer feed-back, door-to-door delivery, after service, and so on. Cooperation model should be designed and implemented to obtain

synergy effects by keeping strong points from both off-line and on-line channels. Channel portfolio design will be explained next section.

Among many functions and roles that traditional distribution channel partners take, one of the most important and indigenous role is logistics. Logistics is in the physical world and provides contact points of consumers for manufacturers. Consumers feel convenience to search product information in web and to make an order via web site, and convenience is a number one factor of survey question, why are you shop via Internet? [5] [7] On the other hand, it is not convenient for singles and dual-income family to get their product delivered.

Chain of convenience stores spread widely and can be a good partner as contact points between consumers and manufacturers, especially for pure players who use only on-line channels. 7dream.com of Japan [a] and lotte.com [f] of Korea are the two of the most prominent examples who adopt the integration model of physical network and on-line channel. Users of these sites can order at web site and pick up and pay at the off-line convenience store. Users make an on-line order with kiosk in the store or an order with face-to-face mode. This model applies to general trading companies and financial companies and expands to video rental house and subway stations as a physical network in the metropolitan area like Seoul.

IV. Channel Cooperation Planning

Manufacturers who want to introduce on-line channel via their web site, they have to plan channel management including both off-line and on-line channels. In this section, how to make a plan of channel management will be explained.

4.1 Pre-Marketing Research

It is required for a manufacturer to do a marketing research of

analyzing the impact of on-line channel introduction. Here is an example and a counter-example that shows the necessity of pre-marketing research. Avon sells its beauty products through its web site as well as through its sales force. By the result of pre-marketing research, Avon found that web site primarily attracts new customers and does not compete with its traditional sales channel of using door-to-door representatives. But Avon will need to check regularly if there appears any channel conflict, because Internet is the fastest media to carry product and discount information to consumers.

A counter example is of Gibson Musical Instruments. Gibson opened a web site and sold its electronic guitars with 10 % discounts without any pre-marketing research and any consult with its dealers. This made dealers irate and Gibson was so dependent on them that it gave up its online sales of electronic guitars within a month. As above-mentioned in section 2.1.1, Gibson restricts its on-line sales to its accessories and repair parts.

4.2 Functional Decomposition

Channel functions are the basic building blocks of the channel design process. Followings are example channel functions: products display and comparison, product information providing and sales negotiation, order generation and taking, payment generation and fulfillment, delivery and installment, after service inquiry taking and fulfillment or forwarding. Because channel functions cannot be eliminated, functions should be allocated either on-line or off-line. This means that roles of the off-line channel partners should be re-designed according to the newly allocated functions. Analyses and decisions of which functions are suitable for which channel should be done. Information providing and comparison functions are more suitable for on-line channel. Appropriateness should be totally viewed from the customer's point of view: quality of function and convenience for

customers.

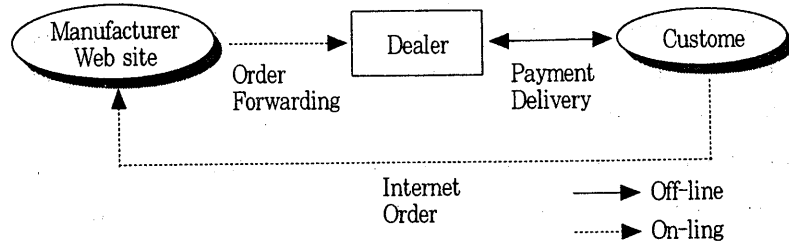
After service function as an example, analysis of how much off-line partners take the function role should be done. According to convenience and quality of AS service, sub-functions of AS (AS inquiry taking, physical inspections for minor repair, or sending to manufacturer, repair tracking service) should be re-assigned to on-line and off-line.

4.3 Channel Portfolio

What is the optimal portfolio of on-line and off-line channels? The answer is dependent upon many factors such as characteristics of product, negotiation power of off-line distributors, flexibility of back-end system, and so on. Following characteristics are of products that are suitable for on-line channel: 1) information-laden products like insurance, travel, book, information providing by DB access, 2) digital products such as software, book, video, pictures, 3) perishable products like airplane, train, and concert tickets, 4) products that provide high margins for distributors, 5) products which need customization, configuration, and option selections. On the other hand, products which need touch, feel, and deep explanations and products of which design aspects are very important are suitable for off-line channel.

Automobiles are products that have mixed characteristics of on-line suitable products like computers and off-line one like fashion products. Ford takes a mixed strategy of on-line and off-line channels (Figure 2). Off-line partners do order fulfillment, payment reception, and delivery, while model and option selections and price calculation at order-taking phase are done at Ford's on-line web site. Orders taken at web site are forwarded to the nearest dealer who has the inventory of the customer-selected car. Therefore, information system for inventory checking and order forwarding between Ford and its dealers are basic structure for channel portfolio design and implementation.

<Figure 2> Order Forwarding Model



V. Conclusion

For manufacturers, web site could be a good marketing channel and tool that provides multiple functions of product information providing, customer feedback taking, direct sales, payment, after service inquiry tacking and fulfillment with more convenient and timely manner for customers. But, manufacturers have had some obstacles to introduce direct marketing model, and one of them is channel conflict. To reduce channel conflict, several strategic options should be considered. For channel design, a transition from conflict reduction point of view to channel portfolio point of view for channel synergy maximization is needed. Channel functions should be re-designed according to characteristics of each industry and product.

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