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Marketing's Four P's: First Steps for New Entrepreneurs

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EXPERT REVIEWED

Audience: Business managers

Content: Presents the four elements of marketing your products and business

Outcome: Readers will be aware of the range of marketing decisions they need to make

Marketing your business is about how you position it to satisfy your market's needs. There are four critical elements in marketing your products and business. They are the four P's of marketing.

1. **Product.** The right product to satisfy the needs of your target customer.
2. **Price.** The right product offered at the right price.
3. **Place.** The right product at the right price available in the right place to be bought by customers.
4. **Promotion.** Informing potential customers of the availability of the product, its price and its place.

Each of the four P's is a variable you control in creating the marketing mix that will attract customers to your business. Your marketing mix should be something you pay careful attention to because the success of your business depends on it. As a business manager, you determine how to use these variables to achieve your profit potential. This publication introduces the four P's of marketing and includes worksheets that will help you determine the most effective marketing mix for your business.

Product

"Product" refers to the goods and services you offer to your customers. Apart from the physical product itself, there are elements associated with your product that customers may be attracted to, such as the way it is packaged. Other product attributes include quality, features, options, services, warranties, and brand name. Thus, you might think of what you offer as a bundle of goods and services. Your product's appearance, function, and support make up what the customer is actually buying. Successful managers pay close attention to the needs their product bundles address for customers.

Your product bundle should meet the needs of a particular target market. For example, a luxury product should create just the right image for "customers who have everything," while many basic products must be positioned for price-conscious consumers. Other important aspects of product may include an appropriate product range, design, warranties, or a brand name.

Customer research is a key element in building an effective marketing mix. Your knowledge of your target market and your competitors will allow you to offer a product that will appeal to customers and avoid costly mistakes.

If you are considering starting a new business or adding a new product, then make sure the product bundle will fit your business's strengths and weaknesses, and that it will provide an acceptable risk/return tradeoff. For instance, if your business is very good at timely response to customers, then timely service should be an important part of your product bundle.

Think long term about your venture by planning for the ways you can deepen and broaden your product bundle. For instance, you may be able to take advantage of opportunities to add value through processing, packaging, and customer service. Other future growth may allow you to offer your product to different customers. Start-up businesses are most successful when they concentrate their efforts on one product or one market, like a restaurant or a car service center does. Later growth may occur in the same location or may be in different geographic regions.

A different type of growth would be a diversification of products, with your business offering related products. Offering a whole range of products is most successful if the raw materials, production processes, and distribution methods are similar, which means you do not have to acquire new suppliers, skills and equipment, and distribution methods.

Price

"Price" refers to how much you charge for your product or service. Determining your product's price can be tricky and even frightening. Many small business owners feel they must absolutely have the lowest price around. So they begin their business by creating an impression of bargain pricing. However, this may be a signal of low quality and not part of the image you want to portray. Your pricing approach should reflect the appropriate positioning of your product in the market and result in a price that covers your cost per item and includes a profit margin. The result should neither be greedy nor timid. The former will price you out of the market; pricing too low will make it impossible to grow.

As a manager, you can follow a number of alternative pricing strategies. In the next column are eight common pricing strategies. Some price decisions may involve complex calculation methods, while others are intuitive judgments. Your selection of a pricing strategy should be based on your product, customer demand, the competitive environment, and the other products you will offer.

- **Cost-plus:** Adds a standard percentage of profit above the cost of producing a product. Accurately assessing fixed and variable costs is an important part of this pricing method.
- **Value-based:** Based on the buyer's perception of value (rather than on your costs). The buyer's perception depends on all aspects of the product, including non-price factors such as quality, healthfulness, and prestige.
- **Competitive:** Based on prices charged by competing firms for competing products. This pricing structure is relatively simple to follow because you maintain your price relative to your competitors' prices. In some cases, you can directly observe your competitors' prices and respond to any price changes. In other cases, customers will select vendors based on bids submitted simultaneously. In those cases, gathering information will be more difficult.
- **Going-rate:** A price charged that is the common or going-rate in the marketplace. Going-rate pricing is common in markets where most firms have little or no control over the market price.
- **Skimming:** Involves the introduction of a product at a high price for affluent consumers. Later, the price is decreased as the market becomes saturated.
- **Discount:** Based on a reduction in the advertised price. A coupon is an example of a discounted price.
- **Loss-leader:** Based on selling at a price lower than the cost of production to attract customers to the store to buy other products.
- **Psychological:** Based on a price that looks better, for example, $4.99 per pound instead of $5.00 per pound.

After you decide on your pricing strategy, the amount of money you will actually receive may be complicated by other pricing aspects that will decrease (or increase) the actual amount of money you receive. You will also have to decide how to determine:

- **Payment period:** Length of time before payment is received.
- **Allowance:** Price reductions given when a retailer

agrees to undertake some promotional activity for you, such as maintaining an in-store display.

- **Seasonal allowances:** Reductions given when an order is placed during seasons that typically have low sales volumes to entice customers to buy during slow times.
- **Bundling of products/services:** Offering an array of products together.
- **Trade discounts** (also called "functional discounts"): Payments to distribution channel members for performing some function such as warehousing and shelf stocking.
- **Price flexibility:** Ability of salesperson or reseller to modify price.
- **Price differences among target customer groups:** Pricing variance among target markets.
- **Price differences among geographic areas:** Pricing variance among geographic regions.
- **Volume discounts and wholesale pricing:** Price reductions given for large purchases.
- **Cash and early payment discounts:** Policies to speed payment and thereby provide liquidity.
- **Credit terms:** Policies that allow customers to pay for products at a later date.

The methods discussed here should be a base from which to construct your price. Your options will vary depending on how you choose to sell your product. For instance, if you make a product but don't sell it directly to the customer, then you will want to know who sets the retail price and what margin they will require. Tracing the path of your product from production to final purchase is a useful exercise to discover this information. The research needed to understand the pricing along the distribution path will be more than worth the time it takes.

Whatever your price may be, ultimately it must cover your costs, contribute to your image by communicating the perceived value of your product, counter the competition's offer, and avoid deadly price wars. Remember, price is the one "P" that generates revenue, while the other three "P's" incur costs. Effective pricing is important to the success of your business.

Place

"Place" refers to the distribution channels used to get your product to your customers. What your product is will greatly influence how you distribute it. If, for example, you own a small retail store or offer a service to your local community, then you are at the end of the distribution chain, and so you will be supplying directly to the customer. Businesses that create or assemble a product will have two options: selling directly to consumers or selling to a vendor.

Direct Sales

As a producer, you must decide if supplying direct is appropriate for your product, whether it be sales through retail, door-to-door, mail order, e-commerce, on-site, or some other method. An advantage of direct sales would be the contact you gain by meeting customers face to face. With this contact you can easily detect market changes that occur and adapt to them. You also have complete control over your product range, how it is sold, and at what price.

Direct sales may be a good place to start when the supply of your product is limited or seasonal. For example, direct sales for many home-produced products can occur through home-based sales, markets, and stands.

However, direct sales require that you have an effective retail interface with your customers, which may be in person or electronic. If developing and maintaining this retail interface is not of interest to you or you are not good at it, you should consider selling through an intermediary.

Reseller Sales (Sales Through an Intermediary)

Instead of selling directly to the consumer, you may decide to sell through an intermediary such as a wholesaler or retailer who will resell your product. Doing this may provide you with a wider distribution than selling direct while decreasing the pressure of managing your own distribution system. Additionally, you may also reduce the storage space necessary for inventory. One of the most important reasons for selling through an intermediary is access to customers. In many situations, wholesalers and retailers have customer connections that would not be possible to obtain on your own.

However, in selling to a reseller you may lose contact with your end consumer. In some cases, you may also lose some of your company identity. For example, your distributor may request that your product be sold under the reseller's brand name.

One factor that may influence whether you can find an intermediary to handle your product is production flow. Wholesalers want a steady year-round supply of product to distribute. If you can deliver a steady year-round supply that is of consistent quality, then selling through an intermediary may be a good strategy for you.

Market Coverage

No matter whether you sell your product direct or through a reseller, you must decide what your coverage will be in distributing your product. Will you pursue intensive, selective, or exclusive coverage?

Intensive distribution is widespread placement in as many places as possible, often at low prices. Large businesses often market on a nationwide level with this method. Convenience products—ones that consumers buy regularly and spend little time shopping for, like chewing gum—do better with intensive (widespread) distribution.

Selective distribution narrows distribution to a few businesses. Often, upscale products are sold through retailers that only sell high-quality products. With this option, it may be easier to establish relationships with customers. Products that people shop around for sell better with selective distribution.

Exclusive distribution restricts distribution to a single reseller. You may become the sole supplier to a reseller who, in turn, might sell only your product. You may be able to promote your product as prestigious with this method, though you might sacrifice sales volume. Specialty products tend to perform better with exclusive distribution.

Other Place Decisions

Product characteristics and your sales volumes will dictate what inventories to maintain and how best to transport your products. Additionally, the logistics associated with acquiring raw materials and ensuring that your final product is in the right place at the right time for the right customers can comprise a large percentage of your total costs and needs careful monitoring.

You may decide to have a combination of all the distribution methods. Whatever you decide, choose the method which you believe will work best for you.

Promotion

"Promotion" refers to the advertising and selling part of marketing. It is how you let people know what you've got for sale. The purpose of promotion is to get people to understand what your product is, what they can use it for, and why they should want it. You want the customers who are looking for a product to know that your product satisfies their needs.

To be effective, your promotional efforts should contain a clear message targeted to a specific audience reached via an appropriate channel. Your target audience will be the people who use or influence the purchase of your product. You should focus your market research efforts on identifying these individuals. Your message must be consistent with your overall marketing image, get your target audience's attention, and elicit the response you desire, whether it is to purchase your product or to form an opinion. The channel you select for your message will likely involve use of a few key marketing channels. Promotion may involve advertising, public relations, personal selling, and sales promotions.

A key channel is advertising. Advertising methods to promote your product or service include the following.

- **Radio:** Radio advertisements are relatively inexpensive ways to inform potential local customers about your business. Mid-to-late week is generally the best time to run your radio ad.
- **Television:** Television allows access to regional or national audiences, but may be more expensive than other options.
- **Print:** Direct mail and printed materials, including newspapers, consumer and trade magazines, flyers, and a logo, allow you to explain what, when, where, and why people should buy from you. You can send letters, fact sheets, contests, coupons, and brochures directly to new or old customers on local, regional, or national levels.
- **Electronic:** Company Web sites provide useful information to interested consumers and clients. Password-protected areas allow users to more

intimately interact with you. Advertisements allow broad promotion of your products. Direct e-mail contact is possible if you have collected detailed customer information.

- **Word of Mouth:** Word of mouth depends on satisfied customers (or dissatisfied customers) telling their acquaintances about the effectiveness of your products.
- **Generic:** Generic promotion occurs when no specific brand of product is promoted, but rather a whole industry is advertised. For instance, generic advertising is commonly found for milk, beef, and pork.

Public relations (PR) usually focuses on creating a favorable business image. Important components of a good public relations program include being a good neighbor, being involved in the community, and providing open house days. News stories, often initiated through press releases, can be good sources of publicity.

Personal selling focuses on the role of a salesperson in your communication plans. Salespeople can tailor communication to customers and are very important in building relationships. While personal selling is an important tool, it is costly. So you should make efforts to target personal selling carefully.

Sales promotions are special offerings designed to encourage purchases. Promotions might include free samples, coupons, contests, incentives, loyalty programs, prizes, and rebates. Other programs might focus on educating customers through seminars or reaching them through trade shows. Your target audience may be more receptive to one method than another. Additional sources of promotion may be attending or participating in trade shows, setting up displays at public events, and networking socially at civic and business organizations.

Final Comment

The four P's—product, price, place, and promotion—should work together in your marketing mix. Often, decisions on one element will influence the choices available in others. Selecting an effective mix for your market will take time and effort, but these will pay off as you satisfy customers and create a profitable business. The worksheets that follow will help you construct your marketing plans.

Once you have a good marketing mix—the right product at the right price, offered in the right place and promoted in the right way—you will need to continue to stay on top of market changes and adopt your marketing mix as necessary. Marketing is a part of your venture that will never end.

Four P's Worksheets

The following set of worksheets will help you understand and tailor your marketing mix to your customers' needs. The four sections relate to the four P's of product, price, place, and promotion. In the first part of each section, you will complete a table to help you gain a better understanding of what you are offering and what your competitors are offering. In the "Further Assessment" part of each section, you will answer questions to help you tailor your marketing mix to your customers' needs.

Product

Describe your product's characteristics in the first column and the characteristics of your competitors' product in the second column.

	Your Product	Your Competitors' Product
Product (e.g., fresh fruit beverage)		
Product Variety		
Product Appearance		
Product Quality		
Product Features		
Product Functionality		
Services		
Brand Name		
Packaging		
Warranties		

Further Assessment

1. What features are considered basic features by your customers (ones that must be offered)?	
2. What features are missing from the existing product/service choices in the market place? How can your product/service address this gap?	
3. What are the key features/benefits of your product and service, especially as they compare to what your competitors are supplying?	
4. How can your product give you an advantage in the marketplace?	

Price

For each of the following pricing strategies, describe the advantages and disadvantages of using that method for your product. Which is the best one for you to use?

	Advantages and Disadvantages for Your Product
Cost-Plus	
Value-Based	
Competitive	
Going-Rate	
Skimming	
Discount	
Loss-Leader	
Psychological	

For each of the following pricing aspects, describe the advantages and disadvantages for your product in the first column.
In the second column, describe to what extent your competitors are following that approach.

	Advantages and Disadvantages for Your Product	To What Extent Are Your Competitors Using This Policy for Their Products?
Payment Period		
Allowance		
Seasonal Allowances		
Bundling of Products/Services		
Trade Discounts		
Price Flexibility		
Price Differences Among Target Customer Groups		
Price Differences Among Geographic Areas		
Volume Discounts and Wholesale Pricing		
Cash and Early Payment Discounts		
Credit Terms		

Further Assessment

1. How sensitive is your target market to changes in prices?	
2. How does your expected pricing compare to your competition's pricing?	
3. Will pricing make your business special?	
4. How will your products/services provide a better price-performance balance than your competitors' products/services?	

Place

In the first column, describe how your product is distributed. Describe your competitors' product distribution in the second column.

	Your Product	Your Competitors' Product
Direct Sales		
Reseller Sales		
Market Coverage		
Inventory		
Transportation		
Logistics		

Further Assessment

1. What is the best way to sell your product? Direct selling? Through a reseller? Will this be a competitive advantage or disadvantage?	
2. How will your plan for coverage and other place decisions compare to those of your competitors? Will this be a competitive advantage or disadvantage?	

Promotion

Describe your product's promotion in the first column and your competitors' promotion in the second.

	Your Product	Your Competitors' Product
Advertising		
Radio		
Television		
Print		
Electronic		
Word of Mouth		
Generic		
Public Relations		
Personal Selling		
Sales Promotion		

Further Assessment

1. What promotion efforts are most effective for your target market?	
2. How can your promotion strategy give you an advantage in the marketplace?	

Notes

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Characteristics of a Successful Enterpreneur

Vision – The successful entrepreneur has the ability to see the end results of goals while working to achieve them and is completely dedicated to making this vision a reality.

Determination – The successful entrepreneur must be completely determined to succeed even when it means taking risks.

Motivation – The successful entrepreneur has the desire to work hard and lets very little get in the way of making vision into reality.

Focus – The successful entrepreneur is self-disciplined and has the ability to stick to a schedule and deadlines.

Devotion – The successful entrepreneur has a high degree of commitment to the ideas and beliefs on which the project is founded.

Skills – The successful entrepreneur must have the skills necessary to develop the product or service or to take an idea and figure it out.

Perseverance – The successful entrepreneur must have the willingness to keep goals in sight and to work toward them despite obstacles.

Adaptability – The successful entrepreneur must have the ability to cope with new situations and find creative solutions to problems.

Organization – The successful entrepreneur knows his or her own strengths and weaknesses and assembles the right team and resources to accomplish goals.

Creative thinking – The successful entrepreneur has to be able to think through the innovative idea and deal with the many variables facing the business.

Passion – The successful entrepreneur has to really love what he or she is doing.

Flexibility – The successful entrepreneur must be adaptable to changing demands of the business, employees and customers.

Concept of Finance:

Business concern needs finance to meet their requirements in the economic world. Any kind of business activity depends on the finance. Hence, it is called as lifeblood of business organization. Whether the business concerns are big or small, they need finance to fulfil their business activities. In the modern world, all the activities are concerned with the economic activities and very particular to earning profit through any venture or activities. The entire business activities are directly related with making profit. (According to the economics concept of factors of production, rent given to landlord, wage given to labour, interest given to capital and profit given to shareholders or proprietors), a business concern needs finance to meet all the requirements. Hence finance may be called as capital, investment, fund etc., but each term is having different meanings and unique characters. Increasing the profit is the main aim of any kind of economic activity.

MEANING OF FINANCE

Finance may be defined as the art and science of managing money. It includes financial service and financial instruments. Finance also is referred as the provision of money at the time when it is needed. Finance function is the procurement of funds and their effective utilization in business concerns. The concept of finance includes capital, funds, money, and amount. But each word is having unique meaning. Studying and understanding the concept of finance become an important part of the business concern. Various sources of finance available to businesses:

1. **The Founders**

   Explanation: have some savings left yourself? Just received a nice bonus? Why not invest it in your own company! You don’t necessarily have to invest in terms of cash. If a co-founder or a partner invests his/her hours in helping you start your business next to his/her job that is also an investment. Or what about a founder making an office, machines or a technology license available? All of these are sources of investment. Temporarily not paying yourself any wage is also an option.

When to choose this source of financing: founders can obviously invest in their own company at all times. However, you usually see this happening when the company has just been founded. When a company is set up, in many cases no revenues or external financing is available, while there are always some start-up costs to cover.

In terms of the size of the investment you can go all out (as far as your bank account allows you to).

Advantage of this form of investment: it can be perceived as positive by an external financer that a founder has some “skin in the game” as well. Why would another person take the risk of investing in your company if you have never been prepared to take the risk yourself?

2. The 3F’s: family, friends and fools

Explanation: before you start approaching professional investors, it might be worthwhile to try to raise some funding within your network of family, friends and fools. These are often people from your family or social network who are close to you and mainly invest because they have faith in your idea or in you as a person/entrepreneur. As they are usually not professional investors you should not expect a professional assessment of your plans from such an investor.

When to choose this source of financing: this type of financing is often pursued to cover the costs of setting up a new company or to bridge the gap to a first round of seed funding. The advantage of this funding type is that it is a quick and cheap way of collecting cash, especially if you take into account the risk that the 3Fs take (which they are not always aware of themselves: hence “fools”).

Usually the amounts concerned with this type of investment are not too high and are typically repaid as a loan (with or even without interest) or are invested in exchange for a small equity share in the company. When the invested amounts, share percentages and the level of professionalism increase, then we speak of angel investing.

3. Angels/informals

Explanation: angel or informal investors are experienced entrepreneurs who have some funds available (often from previously exited ventures) and invest those in new companies to help other entrepreneurs succeed in their business. Angel investments start around €50,000 and can amount up to (more than) a million euros, as angels often invest together in groups.

When to choose this source of financing: go for an angel if you are looking for seed funding within the abovementioned range. Angels typically offer “smart capital”: so not just money, but also network and knowledge within specific sectors. Try to find an angel that fits with your company in terms of experience and sector knowledge. You can find two overviews of active angel investors in the Netherlands here and here.

4. Crowd-funding

Explanation: nowadays it is hard to imagine crowdfunding once didn’t exist in the Dutch (and international) financing ecosystem. With crowdfunding, the “crowd” finances the funding need of a company. Usually crowdfunding is performed via an online platform where entrepreneurs offer investment opportunities on one side of the platform and on the other side of the platform a large group of people invest small amounts to meet the entrepreneur’s investment need.

When to choose this source of financing: in general there are three types of crowdfunding: loans, pre-orders/donations and convertible loans. Are you looking for a loan, but is it hard to secure one from the bank because your risk profile is too high? Then try loan crowdfunding. Do you have a prototype available and do you want to test the product/market fit, but you cannot finance the production/delivery of the first batch of actual products? Then go for pre-orders/donations.

Well-known examples of suitable platforms are Kickstarter and Indiegogo. These platforms are mainly suitable for products/projects/gadgets aimed at the consumer market with a strong design element to them.

Convertible loans have the following advantages: 1) no shares are being issued, 2) valuation discussions are postponed until the moment the value of a company can be better determined and 3) it is an easier, faster and cheaper process than an actual share transfer. Leapfunder is an example of a Dutch crowd-funding platform that works with convertible loans.

Since the people that invest via crowd-funding platforms are not always professional investors, crowd-funding is better suited for propositions that are not too complex or technical and that are easily understood by the general public (that’s why it’s called “crowd” funding). Think for example of consumer products.

There are also crowd-funding platforms with a specific focus, so take that into account in your choice. Dutch crowd-funding platform One planet crowd for instance focuses specifically on sustainable projects with a positive impact.

5.Subsidies

Explanation: a huge number of tax/financial schemes and subsidies exist. The aim of subsidies/schemes is typically to stimulate entrepreneurship, innovation/R&D or economic growth within a certain geographical area. That is why every region, every country and even the entire EU has its own subsidies.

When to choose this source of financing: ALWAYS, we can be very brief about that;) Subsidies are relevant during almost every company stage. From start-up to corporate, from freelancer to publicly traded company.

As mentioned before, many subsidies only focus on a certain geographical area and often there is also a specific sector focus. Therefore it is important to look for a subsidy that fits with your company. For an overview of available subsidies/schemes in the Netherlands, check out the website of the RVO.

Keep in mind that administrative and reporting requirements often apply to subsidy applications and grants. You need to be able to justify the costs for which you request a subsidy and sometimes it is mandatory to have this justification audited as well.

6. Venture capital/private equity

Explanation: private equity is the collective name for professional investment firms that invest in companies that are not publicly listed. Venture capital (VC) is a type of private equity which focuses specifically on risky investments in terms of early stage companies.

People often speak of private equity when investing in larger organizations that are existing for some time already. Venture capital on the other hand involves investing in growth capital of young companies. In general, VCs have a fund available of a specific size (e.g. € 100 million) that has to be invested within a certain period of time (e.g. 10 years) in a bunch of companies with different risk profiles to spread the risk across the portfolio. The aim is to sell the shares after a couple of years with a certain return/profit.

When to choose this source of financing: venture capital is mainly suitable for companies that have already passed the “seed stage” and are looking for series A or series B funding. This type of funding is therefore meant to help companies grow faster than when they would grow organically, for instance if a firm wants to internationalize.

VCs typically invest in the range of about €500,000 to €20 million. To raise funding from a VC a company’s product/market fit has to be proven already and steadily growing revenue streams have to exist (except perhaps in the medical sector). However, there are also venture capitalists with seed funds (starting at €200,000) that offer seed capital to companies that have not met the abovementioned criteria yet.

The advantage of VCs is that they can fund multiple rounds, where an angel or other seed investor is not always capable of doing so. VCs often also have a specific sector focus and good knowledge/network within this sector. For a list of VCs active in the Netherlands, take a look at this overview.

7. Debt financing: the bank

Explanation: even though there are a number of banks in the Netherlands that have started venture capital funds (including Rabobank, ING and ABN AMRO), banks are generally more risk averse than for example angels, seed investors and normal VCs. This does not mean that banks do not finance entrepreneurs, on the contrary!

However, they are more likely to invest in SMEs, in companies with lower risk profiles (than start-ups for instance) and when companies can offer collateral. For an early-stage start-up that does not fit in the focus of the VC funds, it can thus be difficult to secure funding from a bank. However, a number of banks in the Netherlands do have partnerships with crowdfunding platforms.

When to choose this source of financing: as mentioned, banks generally take less risk than, for example, VCs and angels. However, if you can provide collateral then the bank is a very good option. Are you thus looking for working capital financing, stock financing or financing to cover investments in buildings/machines, then the bank is a very good option to consider.

Companies generating stable income streams and that have been growing organically for a number of years (and are thus less risky) can certainly also turn to the bank. A big advantage of debt financing: you do not have to give away a part of your company in terms of equity, which means that in the long term it can turn out to be a much cheaper way of financing than for example securing funding from an angel investor or VC.

8. Factoring

Explanation: in short, factoring is a way of financing working capital by lowering the size of accounts receivable. Example: if you send an invoice to a customer, but it takes him/her 60 days to pay, then you can decide to ‘sell’ this invoice to a factoring company (against a certain payment of course).

The factoring company will pay for the invoice immediately (or provides you with a loan) so that you do not have to wait 60 days before the invoice is paid. A factoring company can also take over the risk that a customer does not pay.

When to choose this source of financing: first of all, it goes without saying that you must have clients in order to be eligible for factoring. If you do not have any paying customers, factoring is not an option. If you do have customers, factoring can be very useful if you have to deal with long payment terms.

Do you have large corporates as your customers? Then it can take a while for invoices to be paid and there is often not much you can do about it. In order to keep your working capital position healthy, factoring can be a good choice. Is accounts receivable management costing you a lot of time and effort? Do you often suffer from bad debtors? Then factoring could also be an outcome.

9. Leasing

Explanation: do you have to make large investments in assets such as computers and/or machines? Why don’t you lease instead of purchasing them? By leasing assets companies can spread payments over a longer period of time instead of having to fulfill the full payment of an investment upon the moment they decide to purchase an asset.

When to choose this source of financing: when a company is capital-intensive, meaning it is dependent on the use of (sometimes expensive) assets such as machinery.

10. Suppliers

Explanation: do you purchase a lot from suppliers? Then try to negotiate favorable payment terms with them. If your customers have long payment terms, for instance, you can try to agree to longer payment terms with your suppliers as well so that you do not run into any problems concerning your working capital. On the other hand, you could also try to discuss discounts in the event you pay your suppliers very fast.

When to choose this source of financing: choose this form of financing if you have good relationships with your suppliers or if you have a good negotiating position towards them (for example if you are a large/important customer for them).

CHAPTER I

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CHAPTER I

INTRODUCTION

1.0.1 Meaning Of Market

Though the world is spinning in new millennium, there are things, which are always omnipresent in the Universe. Market is one among them. The term 'market' is very familiar with every individual in the society. Any person, who has any kind of need, cannot keep away from the influence of market. The market is so immensely and intimately associated with everyone's life that it has become an inseparable component of modern lifestyle.

The term 'market' is derived from the Latin word '*marcatus*' implying to trade, merchandise, ware traffic, trading place where business is conducted. A layperson has the same annotation and by market, one refers to a place where buyers and sellers meet personally to finalize the deal after personal inspection. However market means something broader wherein the buyers and sellers are brought in contact with one another and by means of prices of goods and services transactions tend to be equalized easily and quickly. Prof. H.E. Mitchell in his popular book, 'Principles of Marketing' stated, in fact, market must be thought not as a geographical meeting place, but as any place getting together of buyers and sellers, in person, by mail, telephone, telegraph or any means of communication".(1)

A market is an arrangement that provides opportunity for exchanging goods and services for money or money's worth. Therefore, a market consists of a group of persons or persons on one side holding the goods that they want to sell and on the other, a group of prospective buyers who want to pay for and buy. It means that three points are interlinked namely place, area and demand. Place stands for the convenient point for the buyers and sellers to come together to effect the exchange of goods and services; area or atmosphere stands for the place where contact between the buyers and sellers is established to strike the dealing, demand stands for the people with needs and wants to satisfy and purchasing power.

According to Philip Kotler, " market consists of all the potential customers sharing a particular need or want who might be willing and able to engage in exchange to satisfy their need or want".(2) It is, an area, for potential exchanges. The American Marketing Association defined market as "the aggregate demand of the potential buyer for a product or service".(3) Thus, a market is a group of buyers and sellers involved and interested in negotiating the terms of purchase/sale of goods and services.

1.0.2 Concept Of Marketing

Market involves marketing. The basis of market is marketing. Marketing refers to any body, persons or institutions that are in business relations and carry on extensive transaction in any product. Marketing is perhaps the most complex and challenging function performed by every business firm. The term 'marketing' is a comprehensive one. Marketing thought starts well before manufacturing commences and ends only after rendering after-sales satisfaction. It is the set of those activities necessary and incidental to bring about exchange relationships. It encompasses the entire economic process by means of which goods and services are exchanged and their values are determined in monetary units. It is that phase of business activity through which human wants are satisfied by the exchange of goods and services. It is the skill of selecting and fulfilling consumer desires in such a way that a dose of money put in brings back maximum returns.

Various experts on marketing thoughts have defined the term 'marketing' in various ways that ultimately lead to the comprehensive and common definition of modern thought on marketing. According to Prof. William Stanton, marketing is " the total system of interacting business activities to plan, process, promotion and distribute, want satisfying products and services to present and potential customers".(4) According to Clark and Clark, " marketing consists of those efforts which affect transfer in ownership of goods and come for their physical contribution".(5) Prof. Harry L. Hanson, in his book entitled ' Marketing: Texts, Techniques and Cases', wrote that "marketing is the process of discovery and translating consumer needs and wants into product and service specifications, creating demand for these products and services and then, in turn, expanding this demand".(6) The American Marketing Association defined marketing as " the performance of business activities that direct the flow of goods and services from producer to customer or user".(7) Institute of Marketing, United Kingdom, defined marketing as "the management process which identifies, anticipates and supplies customer requirements efficiently and profitability".(8) Prof. Kotler defined marketing as "a social and managerial process by which individuals and groups obtain what they need and want through creating, offering and exchanging products' value with others." (9) It is the relationship between the consumer and the producer occurring at time and place and a value mutually agreeable and acceptable to the concerned parties. In his book ' Marketing Management-Analysis, Planning and Control', Prof. Philip Kotler defined marketing management as "the analysis, planning, implementation and control of programme designed to bring about the desired exchanges with the target audience for the purpose of mutual or personal gains. It relies heavily on the adaptation and co-ordination of product, price and promotion to achieve effective responses….." (10) It is clear from his definition that marketing management is a process that includes analysis, planning and implementation and control activities. Further it is carried for mutual or personal gains and stresses upon the adaptation and coordination of several factors namely product, price, and promotion to achieve effective responses. It can be practiced by seller or by buyer whoever seeks to simulate the process of exchange. Marketing expert Theodre Levitt defined marketing as a "viewpoint which looks at the entire business process as a highly integrated effort to discover, create, arouse and satisfy customer needs." (11) According to Leslie Rodger, "Marketing is the primary management function which organizes and directs the aggregate of business activities involved in customer purchasing power into effective demand for a specific product or service and is making the product or service available to the final consumer or user so as to achieve the profit target or the other objectives set by the company". (12) In view of above definitions, it is evident from the above discussions that marketing is a process of exchange involving two distinct aspects namely mental and physical involvement of the buyers and sellers. The seller must know what the buyers want, at what price, when and where, of what quality and quantity. Similarly the buyers must know what there for sale, at what price, where and when is it available.

During the new millennium marketing has become more attractive at all levels. In the early days, there was no difference between selling and marketing but today the difference between these two terms has been clearly apparent. The developing nations are giving much importance in marketing to develop their internal and external markets. Even the socialist nations have started studying the marketing concepts in a scientific way to introduce them actively in their internal distribution system.

Marketing is typically seen as the task of creating, promoting and developing goods and services to customers and businesses. **Effective marketing** can take many forms; it can be entrepreneurial formulated or entrepreneur and marketers involved in marketing different entities, goods, services, experiences, events, persons, places, properties, organization, information, ideas and so on.

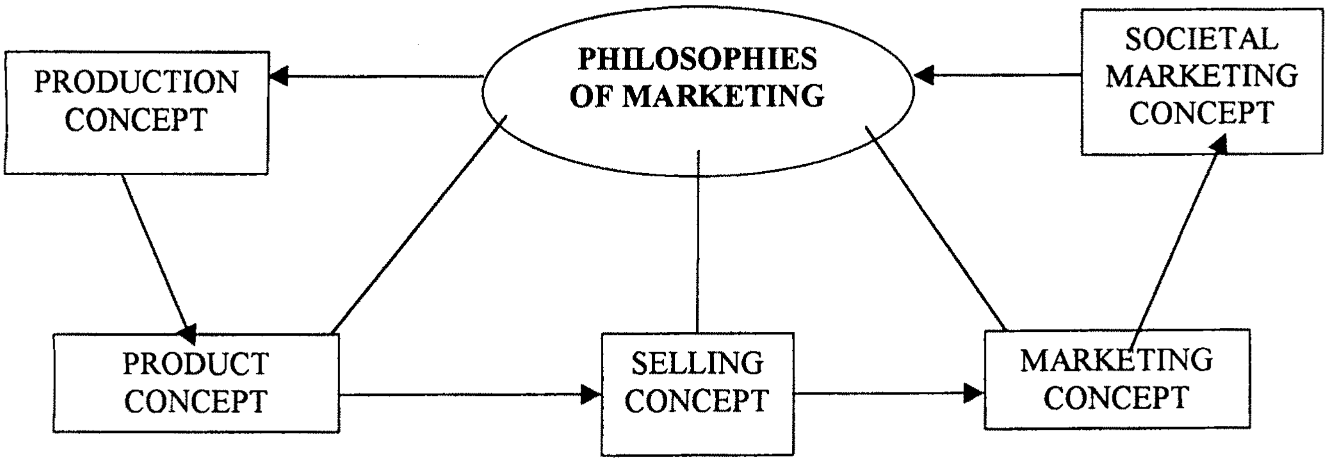
Marketing, as indicated in definitions, denotes a process that remains continuous in nature. The market should be continuously involved in initiating, conducting and finalizing transactions and exchanges. This is an unending task and would continue till production and consumption cease to exist in the world.

Marketing encompasses all the activities of exchange conducted by producers and middlemen in commerce for the purpose of satisfying consumer demand.

Marketing is, thus, more than a set of activities undertaken by a company to sell its products.

1.0.3 Philosophies Of Marketing

Since industrial revolution, marketing management has undergone six distinct concepts of marketing namely, the exchange concept, production concept, the product concept, the sales concept, the marketing concept and the societal marketing concept. Earlier marketing involved only the exchange of a product between a seller and a buyer usually based on money. The prime thought developed on idea of marketing was that it is a process of exchange of products between the sellers or producers and the prospective buyers. But as the markets developed and matured, various philosophies formulated to understand the mechanism and concept of market.


PHILOSOPHIES OF MARKETING
PRODUCTION CONCEPT
SOCIETAL MARKETING CONCEPT
PRODUCT CONCEPT
SELLING CONCEPT
MARKETING CONCEPT

The Production Concept

According to Prof. Philip Kotler, the production concept holds that consumers will prefer products that are widely available and inexpensive. (13)

This philosophy rests on the thought that the consumers will favor those products that are available and highly affordable and the management should, therefore, focus on improving production and distribution efficiency.

The Product Concept

The product concept holds that the consumers will favor those products that offer the most quality, performance, or innovative features. (14) The idea that consumers will favor those products that offers most quality, performance and features and that the organization should therefore, devote its emphasis on making continuous product improvements. A detailed version of the new product idea started in meaningful consumer terms.

The Selling Concept

In the words of Philip Kotler, the selling concept holds that the consumers and businesses, if left alone, will ordinarily not buy enough of the organization's products. (15) The organization must, therefore, undertake an aggressive selling and promotion event. Here the idea is that consumers will not buy enough of the organization's product unless the organization undertakes a large-scale and promotion effort.

The Marketing Concept

As Prof. Kotler states, the marketing concept holds that the key to achieving its organizational goals consists of the company being more effective than competitors in creating, delivering and communicating customer value to its chosen target markets. (16) That is, achieving organizational goals depends upon determining needs and wants of target markets and delivering the desired satisfactions more effectively and efficiently than competitors do.

The Societal Marketing Concept

As Prof. Kotler puts it, the societal marketing concept holds that the organization's task is to determine the needs, wants, and interests of target markets and to deliver the desired satisfactions more effectively and efficiently than competitors in a way that preserves or enhances the consumer's and the society's well-being. (17) **This idea of marketing stresses that the organization should** determine the needs, wants and interests of target markets and deliver the desired satisfaction more effectively and efficiently that the competitors in a way that it maintains and improves the consumers' and society's well-being.

In modern world of marketing it is realized and tested that the Customers increasingly expect higher quality and service and some customization. They perceive fewer real product differences and show less brand loyalty. They can obtain extensive product information from the multi-media and other sources, permitting them to shop more intelligently. They are showing greater price sensitivity in their search for value.

1.0.4 Consumer Behaviour

A customer in business is a person or body of individuals involved in purchase of goods and services. He is a single unit that is actively participating in the decision making process and completes the purchase cycle. A consumer is a person or body of persons who ultimately uses or consumes a product or a service.

A consumer is the end user of a product and may not necessarily be a customer in the market. His behavior in the market is called as consumer behavior. It has been defined as 'those actions directly involved in obtaining, consuming, and disposing of products and services, including the decisions process that proceeds and follows the action' as **stated by Engel, Blackwell, Mini and Paul. (18) It is the behavior** that the consumers display in searching for purchasing, using, evaluating and disposal of products and services that they expect will satisfy their needs. The study of consumer behavior is the study of how individuals and organizations make decisions to spend their available resources i.e. time, money and efforts on consumption related items. It includes the study of what they buy, when they buy, why they buy and where they buy, how often they buy and how often they use it. Thus, consumer behavior is mainly aimed at the consumer and the marketer and study the benefits both consumers and marketers derive.

The consumers differ in their behavior due to their psychological, demographical, cultural and social status. Their way of acting and reacting to different factors differs while making purchase decisions. Further their behavior will not be the same for the same product at all times. As such, it is imperative to the marketer to study the consumer behavior towards an industry or a product with in-depth approach. For this various models of consumer behavior are studied to understand how and when certain decisions are made.

According to a theory in Economics angles it is assumed that a rational consumer evaluates all the alternatives in view of costs and values received and selects that product or service which gives him/her maximum utility or satisfaction. According to Prof. Marshall, with limited purchasing power, and a set of needs and tastes, a consumer allocates his expenditure over different products at given prices so as to maximize utilities.(18) This model is criticized by behavioral scientists on the ground that it ignores psychological factors that govern the consumer actions in the market.

The learning model developed by classical psychologists states that living beings are influenced by both innate needs and learned needs. The various products and services will act as stimuli to satisfy the drives. Further few cognitive theorists added that human beings not only learn to link stimulus with response, but also results in the formation of other cognitive processes such as attitudes, values, beliefs, motivations and so on.

Sigmund Frued proposed the psychoanalytical model of consumer behavior and had the opinion that the human needs and motive operated at the conscious and sub-conscious levels. (19) Marketers are using this approach towards understanding consumer behavior in generating or developing new product ideas-design, features, advertising and promotional techniques.

Sociological model of consumer behavior assumes that the consumer is a member of society and that the society plays an active role in moulding and influencing his buying behaviour. Intimate groups comprising of family, friends, peers and colleagues influence on the lifestyle and mindset of the consumer and shape his buying behaviour. The marketers through the process of market segmentation understand the behavioural pattern of a specific class of buyers and try to influence their buying pattern.

In the Howard-Sheth theory of consumer behaviour, the most significant stimulus affecting the buying behaviour is the information cues about the characteristics of the product. (20) These cues may be significant and symbolic which represent marketing efforts of a firm. The social information cues which affect the buying behaviour for a product or service includes family, friends, and other group members with whom the buyer deals personally. Marketers do not have control over this source of influence.

Francesco Nicosia, (1966) developed the Nicosia model explains buyers behaviour through the messages from the firm that influence predisposition of the consumer towards the product or service. (21) The marketers try to utilize the attitude of consumers towards the product or service through appropriate marketing strategies.

Webster and Wind's model of organizational buying behaviour is an attempt to discover the nature of organizational buyer. (22) It refers to the environmental, organizational, interpersonal and individual buying determinants that influence the organizational buyer. This model, however, is criticized on the view that it statically represented a dynamic situation.

The model that stated consumer behaviour as a decision making process in the form of five steps is the Engel-Kollat-Blackwell model. (23) A process of problem recognition-information search-alternative evaluation-choice-outcome along with other variables explains the conscious decision making process adopted by consumer. However, in case of repurchases, a consumer may not go through all the steps and it ignores the impact of environmental and motivational forces on the buyer's behaviour.

This model further was modified as Engel-Blackwell-Miniard model which puts forth the decision making process, augmented with inputs from information processing and other influencing factors. Finally, the Sheth model of industrial buying concentrates on purchasing process and highlights importance of individual expectations, characteristics of product as well as organization and situational variables that influence the industrial buyer's behaviour.

Thus, in the backdrop of above models of consumer and organizational buyers' behaviour, it can be said that consumer behaviour is a study of how individuals and organizations decide their purchases, what factors influence their decisions, and how do they undergo the process of purchase behaviour.

1.0.5 What Is A Product?

A product refers to the unit that is transacted between the seller and the buyer-a synthesis of what the seller intends and the buyer perceives. A product is the one that satisfies the needs of consumers. As Prof. Kotler states, " a product is anything that can be offered to a market for attention, acquisition, use, or consumption that might satisfy a want or need. It includes physical objects, services, persons, places, organizations and ideas". (24) In the words of Prof. Stanton, ' a product is a set of tangible and intangible attributes, including packing, colour, price, manufacturer's prestige, retailer's prestige and manufacturer's and retailer's services which the buyer may accept as offering satisfaction of wants or needs". (25) It is evident from the above definitions that a product is a bundle of satisfaction that a customer buys. It is a set of attributes combined together in a distinct form that required by the consumer to satisfy his specific need. A consumer is buying what is expressed as want satisfaction. A product is, therefore, not just a physical object but also a bundle of expectations that the customers perceive to be. In short, a product can be anything like a commodity or a good, a service, an idea, a person or a place that is marketed to fulfill a certain want of the customer.

Product can be referred as 'core' one when it is bought by the customer for its fundamentality and benefits that the customers genuinely are interested in buying. Here the marketer acts as the benefit provider. It becomes a basic product when the marketer converts this core benefit into a basic product. When the buyers expect a set of attributes when they purchase a product, it becomes an expected product. And when the buyers think beyond these expectations towards a product, it becomes an augmented product.

1.0.6 Concept Of Service

Since the concept of product is a wider one, denoting a set of utilities to the customers and various inputs and processes that deliver profits to the organization, it also includes the important component of 'service'. The ultimate aim of marketing is to facilitate the flow of goods and services for the satisfaction of customer's wants. A commodity since it is tangible, it is easily identifiable and customers can feel the presence in many ways. A service product refers to the benefit or performance that the customer buys from a service provider to satisfy a desire or a want. What customer purchases from the service provider is an experience personally felt. As such, conceptualization of service is a specific thought conceived by the marketing experts.

In the words of Prof. Kotler again, " a service is any activity or benefit that one party can offer to the another that is essentially intangible an does not result in the ownership of anything". (26) The American Marketing Association defined services as "activities, benefits or satisfaction that are provided in connection with the sale of goods". (27) According to Prof. William Stanton, " services are those separately identifiable, essential intangible activities which provide want satisfaction, and are not necessarily tied to the sale of a product or another service".(28) It is apparent from the above definitions of services that a service "is an intangible activity or benefit or satisfaction that is bought by the customers to satisfy the want without really buying the ownership of it".

1.0.7 Characteristics Of Services

Services being very distinct and unique compared to the products, have peculiar characteristics that create special marketing problem. Rather it is a challenging task posed before the providers of services to market their services. The basic feature of any services as a product is its intangibility. It has no specific shape, design, size or any physical dimension. This results in customers not visually feeling the service product; standardization and patenting being nearly impossible and with no inventories to maintain absolutely no chances of transferring the ownership of services to its purchasers.

It is a difficult task for both the buyers and sellers since none of them can project or present the service product effectively to each other.

In most cases of services, the service product cannot be separated from the service provider or the person who sells it. Therefore, production and consumption of services become one entity and cannot be produced and stored for sale in future. Further the consumer or buyer of the service product becomes part of the process of service delivery that often happens to be existence of both the parties necessary for the marketing act. The coverage of marketing also is limited since the provider cannot make himself available simultaneously in two different locations.

The perishability character of services makes production and storage an impossible task. Further the indecisive demand for services often results in underutilization or expansion of services whenever required to adjust with the fluctuating demand for services. The heterogeneity of services further poses the impossibility of standardization of common quality of similar services.

Unlike the purchase of a product, the buying of services does not transfer the ownership from the seller to the service buyer. The service is purchased for the benefit it provides. As such, greater creativity and ingenuity is expected from the seller or provider of services and most of the occasions, the customer has to place himself vis-à-vis service provider in the service delivery process. All these unique characteristics of services create special marketing problems ahead of service providers or sellers to market them effectively and efficiently.

1.0.8 Marketing Of Services

Services are basically classified as: professional and consumer oriented. In case of professional services like financial advisory, advertising, business and management consultancy, engineering, architectural and interior designs, legal and medical services etc., provided by the professionals, the service providers directly deal with individuals, or market segments. The customer oriented services, also called as business to business services are specialized service firms like office catering, cleaning, tours and travels, entertainment companies that cater to those customers who are more acquainted with them with prior or first time experience.

Marketing of services poses a much potent and viable market opportunity for the service providers in the new millennium. Since there is a shift to service sector in most of the developed as well as developing nations, service sector is the emerging and devouring field for profits by service organizations.

The twenty first century is witnessing the phenomenal prominence of services in the developed and developing economies. In the era of global village, marketing of services is to be focused with more competition and quality from the service providers. The fact that service sector emerging as most core sector throws open new avenues of employment, profits and growth for private as well as public service providers. The basic differences of services unlike products like intangibility, perish ability, heterogeneity and requirements for presence of both buyers and sellers in the buying process i.e. of the service purchaser/consumer and service provider make the marketing managers to face a number of challenges in marketing of services.

As quoted earlier, Prof. Kotler's definition of marketing which recognized the process of marketing management as analysing, planning, implementing and controlling programmes, designed to create, build, and maintain beneficial exchange with target buyers for the purpose of achieving organizational goals holds the same notion towards marketing of services also. When marketing is concerned, the concepts of goods and services remain the same entity though involving different strategies for customer satisfaction. In case of services marketing, along with the conventional four P's of marketing mix-Product, price, place and promotion, added components are physical evidence, process and people.

Service as a product refers to the activities and benefits a service provider offers to sell or hire for satisfying customer wants of a target segment. The service marketer must overcome the intangibility of services to satisfy and retain customer in providing superior and competent quality, trustworthy brand image, guarantees, courteous staff, prompt service and so on as package.

Customers usually associate the price of services with its quality and this must correspond with the customers' perception of value. Since demand for services being fluctuating and indecisive, the services pricing is a sensitive issue and marketers of services often face the problem of pricing of services.

Since the services are heterogeneous in nature, standardization and location are often problems encountered by the service providers. In most of the services, the distribution of the services must take place where both buyers and sellers are present, production and consumption takes place simultaneously and franchising becomes necessary when supply is to be adjusted with the demand of services.

The promotion mix required for services marketing of advertising, publicity, sales promotion, word-of-mouth promotion, personal selling and telemarketing should focus on communicating the essence and benefits of services to the potential buyers of services. Since personal component is vital in the service buying process, it becomes a major task for service marketers to communicate the quality and lesser risk of buying a particular service.

The service production processes starts with people and ends with the consumption of services with people again. Further services marketing becomes effective and efficient only because of people involved in the service marketing process. People are a very important component of marketing mix for services marketing since the political dictum of "for the people, of the people, and by the people" holds good in case of services marketing.

The intangibility of services gives scope for physical evidence of services to be marketed. The essential evidence refers to existence of tangible assets like building, interiors, logos etc. of service provider and peripheral evidence implies the availability and marketing information of services. The physical evidence helps the consumer to reduce the risk involved in buying a particular services and believe in the service as a product.

The final component of marketing mix involved in services marketing is of process-which refers to the system by which the service provider sells the service to the potential buyer of services. It mainly involves adding value or utilities that are essential in satisfying the customer wants and result in brand retention. Thus, the seven P's employed in marketing of services are to be blended in such an effective manner that ultimately it becomes as good as a tangible product in the cognition of customers.

1.0.9 Quality Of Services

The concept of quality is a relative term. Generally, quality refers to the standard or specification that an organization promises to its customers on the product or service offered for sale. Crosby defined quality as "a conformance to requirements for satisfying human want".(29) Garvin measured quality by counting the incidence of internal failures and external failures. (30) Quality is a comparison between expectations and performance of a product or services was the stand of Gronroos, Smith and Houston, Churchill and Surprenant, and Lewis and Booms. (31) It can be stated that quality is a standardized promise that a seller makes to his prospective customers of meeting their requirements of expectations of his product or service.

Quality of services is the hallmark of marketing of services. It is the only parameter that makes the customer to buy the service product, satisfy him, retain him and result in brand loyalty. McConnel, Olander, Zeithaml and Gronroos stated in the initial development of services marketing concept that it is very difficult to define service quality and distinguish it from other service providers on the basis of quality. (32) Further, Parasuraman, Berry and Zeithaml and Boulding stated that customer perceptions of service quality are multi-dimensional and include perceptions like reliability, responsiveness, tangibles assurance and empathy from the service providers. (33)

For effective marketing of services, the service organization or the service provider should focus on the quality component of their service product by linking the internal and external customer base satisfaction as priority.

1.0.10 Customer Satisfaction

Quality of services results in customer satisfaction and ultimately leads to customer retention. Bitner and Bolton and Drew defined customer satisfaction as transaction specific and an antecedent of perceived service quality. (34) Cronin and Taylor opined that customer satisfaction is a cumulative evaluation and a consequence of perceived service quality. (35) The act of buying or using a service generates a certain level of satisfaction for a customer depending on the benefits he derives from the key attributes of that product or service. Customer satisfaction can be understood as the satisfaction derived by the customer after purchase upon the offer's performance in relation to the buyer's expectations. Customer satisfaction is thus, the function of the difference between the perceived performance and expectations.

In marketing, according to LaBarbera and Mazursky, "customer's levels of satisfaction are positively related to repeat purchase behaviour". (36) Service organizations can increase customer retention through increased customer satisfaction is quoted by Crosby and Stephens. Further there are empirical relationships between customer satisfaction and customer loyalty.

1.0.11 Marketing Of Public Utility Services

Marketing of services is undertaken by two distinct service providers in an economy- the private service provider and the public sector service provider. The public utility services marketing falls under the domain of social marketing. In the words of Kotler and Zaltman, " social marketing is the design, implementation and control of programmes calculated to influence the acceptability of social ideas and involving considerations of product planning, pricing, communications, distribution and marketing research". (37) It means, social marketing is nothing but adaptation of the methodology of marketing to social imperatives with the objective of achieving social change. Social marketing is usually undertaken by the private non-profit organizations and public service organizations. Public utility services are those services that are demanded by the general masses irrespective of social, economic or cultural background.. They include health, education, sanitation, transport, communicaticn, family planning, community development, resource mobilization and so on.

The modes of transportation- railway and road form some of the significant public utility services. Transportation acts as a catalyst of economic development. A well-managed and efficient transport system accelerates the pace of development and economic transformation. The developing economy like India has significant magnitude of dependence on transportation for her infrastructure and economic progress.

According to Prof. Jha, the concept of transport marketing focuses on some important issues like managerial efficiency, profit making, competence and delivering transport services according to the perceptions of transportation services by the transport users.(38) Further it is a great task ahead of the public organizations of transport to face the private transport operators and competitively exhibit their excellence.

1.0.12 Need For Assesment Of Service Quality And Customer Satisfaction In Railway Transport

The service quality leads to customer satisfaction, that in turn leads to customer loyalty and customer retention. Satisfaction level is a function of the difference between perceived performance and expectations. Expectations are formed on the basis of the buyer's past buying experience, statements made by friends and peers, and marketer and competitor information and promises. If marketers raise expectations too high, the buyer is likely to be disappointed. On the other hand, some successful companies are raising expectations and delivering performance to match. These companies are aiming high because customers who are just satisfied will still find it easy to switch when a better offer and better quality of service comes along. Those who are highly satisfied are less ready to switch. The fact is that high satisfaction or delight is created by service quality that links an emotional affinity with the brand, not just a rational preference, and this creates high customer loyalty and retention.

Service organizations seeking to win in today's markets must track their customers' expectations, perceived company performance, quality of service and customer satisfaction. Since decades, the marketing experts have realized the significance of direct relationship between service quality and customer satisfaction. Competitiveness and success depends upon management's ability to effectively interpret the provider's and the consumer's perception of customer satisfaction.

Many researchers have linked the service quality with customer satisfaction in marketing of services and thereby achieving customer loyalty and profitability. As such there is a need for assessing the service quality and customer satisfaction of South-Western Railway so as understand its potentiality and betterment of services to compete with the cutthroat competition from the roadway transport and private transport operators. Indian Railways is undergoing metamorphosis. An exercise of assessing service quality and customer satisfaction of one of its subsidiaries would lead to ways and means of establishing a mechanism for effective customer satisfaction to be commercially viable and sustainable. As such an attempt is made in the present research study to assess the service quality and customer satisfaction of a public utility service- the transport system of Indian Railways by applying the Servqual model of service quality. It focuses on assessment of service quality and customer satisfaction of one of the zones of Indian Railways specifically the Bangalore Division of South-Western Railway located in State of Karnataka in India.

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UNIT – I

Lesson 1.1 Introduction to marketing
Lesson 1.2 Marketing concepts
Lesson 1.3 Marketing process
Lesson 1.4 Marketing environment
Lesson 1.5 Buyer Behaviour
Lesson 1.6 Market segmentation, targeting and positioning
Lesson 1.7 Introduction to marketing mix

Answer key
Glossary of terms
References

Unit – I

Lesson 1.1
Introduction to Marketing

Objectives

In this lesson, we will introduce you to the business function of marketing. After you work out this lesson, you should be able to:

- Define marketing and the utility (value) it creates for the customer
- Trace the origin of marketing and explain how it has evolved
- Describe the elements of a marketing strategy
- Understand the scope of marketing

In this lesson, we will discuss the following:

- What is marketing?
- Evolution of marketing
- Marketing framework
- Extending the traditional boundaries of marketing
- Functions of marketing

Introduction

Production and marketing of goods and services are the essence of economic life in any society. All organizations perform these two basic functions to satisfy their commitments to their stakeholders – the owners, the customers and the society, at large. They create a benefit that economists call utility which is the want-satisfying power of a good or service. There are four basic kinds of utility – form, time, place and ownership utility. Form utility is created when the firm converts raw materials and component inputs into finished goods and services. Although marketing provides important inputs that specify consumer preference, the organization’s production function is responsible for the actual creation of form utility. Marketing function creates time, place and ownership utilities. Time and place utility occur when consumers find goods and services available when and where they want to purchase them. Online retailers with 24*7 format emphasize time utility. Vending machines focus on providing place utility for people buying snacks and soft drinks. The transfer of title to goods or services at the time of purchase creates ownership utility.

Type	Description	Examples	Responsible function
Form	Conversion of raw materials and components into finished goods and services	Pizza made from several ingredients	Production
Time	Availability of goods and services when consumers want them	Dial-a-pizza; delivery guaranteed in 30 min.	Marketing
Place	Availability of goods and services where consumers want them	Delivery at your doorstep	Marketing
Ownership (possession)	Ability to transfer title to goods or services from marketer to buyer	Pizza sales (in exchange for rupees or credit card payment)	Marketing

To survive, all organizations must create utility. Designing and marketing want-satisfying goods, services and ideas is the foundation for the creation of utility. Management guru, Peter F.Drucker emphasized the importance of marketing in his classic book, *The Practice of Management* as:

> 'If we want to know what a business is, we have start with its purpose. And its purpose must lie outside the business itself. In fact, it must lie in society since a business enterprise is an organ of society. There is one valid definition of business purpose: to create a customer'.

How does an organization create a customer? Guiltinan and Paul explain it this way:

> Essentially, 'creating' a customer means identifying needs in the marketplace, finding out which needs the organization can profitably serve and developing an offering to convert potential buyers into customers. Marketing managers are responsible for most of the activities necessary to create the customers the organization wants, These activities include:
>
> - Identifying customer needs
> - Designing goods and services that meet those needs
> - Communication information about those goods and services to prospective buyers

- Making the goods and services available at times and places that meet customers' needs
- Pricing goods and services to reflect costs, competition and customers' ability to buy
- Providing for the necessary service and follow-up to ensure customer satisfaction after the purchase

Activity 1.1.1

Think of a recent purchase you made. How did the company provide you with the following utilities?

Form ____________________________
____

Time ____________________________
____

Place ____________________________
____

Ownership ____________________________
____

What is Marketing?

Continuous exposure to advertising and personal selling leads many people to link marketing and selling, or to think that marketing activities start once goods and services have been produced. While marketing certainly includes selling and advertising, it encompasses much more. Marketing also involves analyzing consumer needs, securing information needed to design and produce goods or services that match buyer expectations and creating and maintaining relationships with customers and suppliers. The following table summarizes the key differences between marketing and selling concepts.

Table 1.1.1 Selling Vs. Marketing

Point of difference	**Selling**	**Marketing**
Starting point	Factory	Marketplace
Focus	Existing products	Customer needs
Means	Selling and promoting	Integrated marketing
End	Profits through volume	Profits through satisfaction

The difference between selling and marketing can be best illustrated by this popular customer quote: 'Don't tell me how good your product is, but tell me how good it will make me'.

The American Marketing Association, the official organization for academic and professional marketers, defines marketing as:

> *Marketing is the process of planning and executing the conception, pricing, promotion and distribution of ideas, goods and services to create exchanges that satisfy individual and organizational objectives*

Another definition goes as ' … process by which individuals and groups obtain what they need and want through creating and exchanging products and value with others'. Simply put: Marketing is the delivery of customer satisfaction at a profit.

The notion of exchange as central to marketing is reinforced by many contemporary definitions such as 'marketing is the process of creating and resolving exchange relationships' and 'marketing is the process in which exchanges occur among persons and social groups'. The essence of marketing is the exchange process, in which two or more parties give something of value to each other to satisfy felt needs. In many exchanges, people trade tangible goods for money. In others, they trade intangible services.

Exchanges in marketing are consummated not just between any two parties, but almost always among two or more parties, of which one or more taken on the role of buyer and one or more, the role of seller. A common set of conditions are present in the marketplace, viz.,

1) Buyers outnumber sellers
2) Any individual buyer is weaker than any individual seller economically, but

3) The total economic power of even a fraction of the buyers is enough to assure the existence of, or to put out of business, most sellers or groups of sellers, and
4) Consequently, the sellers compete to sway the largest number of buyers they can to their, rather than another seller's (competitor's) offerings. Finally and intriguingly,
5) The sellers in their attempt to meet competition and attract the largest number of buyers, are influenced as well, regularly modifying their behaviours so they will have more success, with more buyers, over time.

The expanded concept of marketing activities permeates all organizational functions. It assumes that the marketing effort will follow the overall corporate strategy and will proceed in accordance with ethical practices and that it will effectively serve the interests of both society and organization. The concept also identifies the marketing variables – product, price, promotion and distribution – that combine to provide customer satisfaction. In addition, it assumes that the organization begins by identifying and analyzing the consumer segments that it will later satisfy through its production and marketing activities. The concept's emphasis on creating and maintaining relationships is consistent with the focus in business on long-term, mutually satisfying sales, purchases and other interactions with customers and suppliers. Finally it recognizes that marketing concepts and techniques apply to non-profit organizations as well as to profit-oriented businesses, to product organization and to service organizations, to domestic and global organizations, as well as to organizations targeting consumers and other businesses.

Activity 1.1.2

The following list consists of some MARKETING MYTHS. Tick the myths you thought about marketing before reading this section? Add some new myths you might have discovered.

- Marketing and selling are synonymous
- The job of marketing is to develop good advertisements
- Marketing is pushing the product to the customers
- Marketing is transaction-oriented than relationship-oriented
- Marketing is a short-term business strategy
- Marketing is an independent function of a business
- Marketing is part of selling

Evolution Of Marketing

As noted earlier, exchange is the origin of marketing activity. When people need to exchange goods, they naturally begin a marketing effort. Wroe Alderson, a leading marketing theorist has pointed out, 'It seems altogether reasonable to describe the development of exchange as a great invention which helped to start primitive man on the road to civilization'. Production is not meaningful until a system of marketing has been established. An adage goes as: Nothing happens until somebody sells something.

Although marketing has always been a part of business, its importance has varied greatly over the years. The following table identifies five eras in the history of marketing: the production era, the product era, the sales era, the marketing era and the relationship marketing era.

Table 1.1.2 The Evolution Of Marketing

Era	Prevailing attitude and approach
Production	▪ Consumers favor products that are available and highly affordable ▪ Improve production and distribution ▪ 'Availability and affordability is what the customer wants'
Product	▪ Consumers favor products that offer the most quality, performance and innovative features ▪ 'A good product will sell itself'
Sales	▪ Consumers will buy products only if the company promotes/ sells these products ▪ 'Creative advertising and selling will overcome consumers' resistance and convince them to buy'
Marketing	▪ Focuses on needs/ wants of target markets and delivering satisfaction better than competitors ▪ 'The consumer is king! Find a need and fill it'
Relationship marketing	▪ Focuses on needs/ wants of target markets and delivering superior value ▪ 'Long-term relationships with customers and other partners lead to success'

In the production era, the production orientation dominated business philosophy. Indeed business success was often defined solely in terms of production victories. The focus was on production and distribution efficiency. The drive to achieve economies of scale was dominant. The goal was to make the product affordable and available to the buyers. In the product era, the goal was to build a better mouse trap and it was assumed that buyers will flock the seller who does it. However, a better mousetrap is no guarantee of success and marketing history is full of miserable failures despite better mousetrap designs. Inventing the greatest new product is not enough. That product must also solve a perceived marketplace need. Otherwise, even the best-engineered. Highest quality product will fail. In the sales era, firms attempted to match their output to the potential number of customers who would want it. Firms assumed that customers will resist purchasing goods and services not deemed essential and that the task of selling and advertising is to convince them to buy. But selling is only one component of marketing. Next came the marketing era during which the company focus shifted from products and sales to customers' needs. The marketing concept, a crucial change in management philosophy, can be explained best by the shift from a seller's market – one with a shortage of goods and services – to a buyer's market – one with an abundance of goods and services. The advent of a strong buyer's market created the need for a customer orientation. Companies had to market goods and services, not just produce them. This realization has been identified as the emergence of the marketing concept. The keyword is customer orientation. All facets of the organization must contribute first to assessing and then to satisfying customer needs and wants. The relationship marketing era is a more recent one. Organization's carried the marketing era's customer orientation one step further by focusing on establishing and maintaining relationships with both customers and suppliers. This effort represented a major shift from the traditional concept of marketing as a simple exchange between buyer and seller. Relationship marketing, by contrast, involves long-term, value-added relationships developed over time with customers and suppliers. The following table summarizes the differences between transaction marketing (i.e. exchanges characterized by limited communications and little or no on going relationship between the parties) and relationship marketing.

Table 1.1.3 Comparing transaction-based marketing and relationship marketing

Characteristic	**Transaction-Based Marketing**	**Relationship Marketing**
Time orientation	Short term	Long term
Organizational goal	Make the sale	Emphasis on customer retention
Customer service priority	Relatively low	Key component
Customer contact	Low to moderate	Frequent
Degree of customer commitment	Low	High
Basis for seller-customer interactions	Conflict manipulation	Cooperation; trust
Source of quality	Primarily from production	Companywide commitment

Activity 1.1.3

Make a statement to describe each of the stages in the evolution of marketing. You may consider the given examples before coming up with your own statements.

1. Production era
    a. 'Cut costs. Profits will take care of themselves'

2. Product era
    a. 'A good product will sell itself'

3. Sales era
    a. 'Selling is laying the bait for the customer'

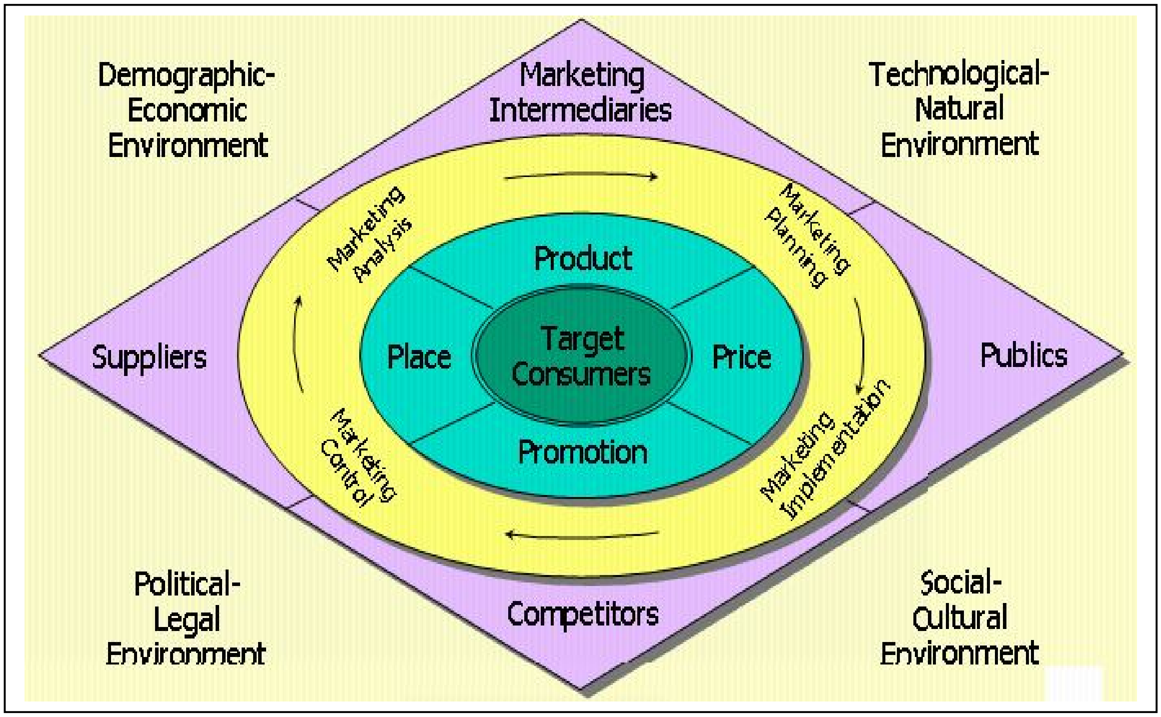
4. Marketing era
    a. 'The customer is King!'

5. Relationship marketing era
    a. 'Relationship with customers determine our firm's future'

Marketing Framework

The basic elements of a marketing strategy consist of (1) the target market, and (2) the marketing mix variables of product, price, place and promotion that combine to satisfy the needs of the target market. The outer circle in Figure 1.1.1 lists environmental characteristics that provide the framework within which marketing strategies are planned.

Figure 1.1.1 Elements of a marketing strategy and its environmental framework


Demographic-
Economic
Environment
Marketing
Intermediaries
Technological-
Natural
Environment
Marketing
Analysis
Marketing
Planning
Product
Suppliers
Place
Target
Consumers
Price
Publics
Marketing
Control
Marketing
Implementation
Promotion
Political-
Legal
Environment
Competitors
Social-
Cultural
Environment

Marketing activities focus on the consumer. Therefore, a market-driven organization begins its overall strategy with a detailed description of its target market: the group of people toward whom the firm decides to direct its marketing efforts. After marketers select a target market, they direct their activities towards profitably satisfying that target segment. Although they must manipulate many variables to reach this goal, marketing decision making can be divided into four areas: product, price, place (distribution) and promotion (marketing communication). These 4 Ps of marketing are referred to as the marketing mix. The 4 Ps blend to fit the needs and preferences of a specific target market. These are the four variables that a marketer can use and control in different combinations to create value for customers. Figure 1.1.1 illustrates the focus of the marketing mix variables on the central choice of consumer or organizational target markets. In addition, decisions about the 4 Ps are affected by the environmental factors in the outer circle of that figure. Unlike the controllable marketing mix elements, the environmental variables frequently lie outside the control of marketers.

The product strategy involves deciding what goods and services the firm should offer to a group of consumers and also making decisions about customer service, brand name, packaging, labeling, product life cycles and new product development. The pricing strategy deals with the methods of setting profitable and justifiable prices. Marketers develop place (distribution) strategy to ensure that consumers find their products available in the proper quantities at the right times and places. Place-related decisions involve the distribution functions and marketing intermediaries (channel members). In the promotional strategy, marketers blend together the various elements of promotion to communicate most effectively with their target market. Many firms use an approach called Integrate Marketing Communications (IMC) to coordinate all promotional activities so that the consumer receives a unified, consistent and effective message.

Marketers do not make decisions about target markets and marketing mix variables in a vacuum. They must take into account the dynamic nature of the five marketing environmental dimensions as shown in Figure 1.1.1 – competitive, political-legal, economic, technological and social-cultural dimensions. Marketers compete for the same consumers. So the developments in the competitive environment will have lot of repercussions. The political-legal environment includes the governing and regulatory bodies who impose guidelines to the marketers. Adherence to the law of the land is an imperative for a marketer to be a good and responsible corporate citizen. The economic environment dictates the mood in the target market who take decisions such as to buy or save, to buy now or later. The technological environment can spell life or death for a marketer with break-through technologies. Marketers often leap forward or get left behind owing to the changes in the technological environment. The social-cultural environment offers cues for the marketers to ‘connect’ well with the target market. Failure on part of the marketer to understand the social-cultural environment will have serious consequences. A marketers can not afford to rub a society/culture on the wrong side!

Extending the Traditional Boundaries of Marketing

Until fairly recently, marketing focused primarily on exchanges of goods between individuals (business-to-consumer (B2C) marketing) and businesses (business-to-business (B2B) marketing). Industrial marketing deals with the organizational purchases of goods to support production of other goods or daily operations or for resale. Table 1.1.2 highlights the differences between consumer marketing and industrial marketing.

Table 1.1.2 Differences between Industrial and Consumer Marketing

Areas of Difference	Industrial Markets (B2B)	Consumer Markets (B2C)
Market characteristics	▪ Geographically concentrated ▪ Relatively fewer buyers	▪ Geographically dispersed ▪ Mass markets
Product characteristics	▪ Technical complexity ▪ Customized products	▪ Standardized products
Service characteristics	▪ Service, timely delivery and availability are critical	▪ Service, timely delivery and availability are somewhat important
Buyer behaviour	▪ Involvement of cross-functional teams in both buyer and supplier firms ▪ Purchase decisions are mainly made on rational/performance basis ▪ Technical expertise sought ▪ Stable interpersonal relationship between buyer and seller	▪ Involvement of family members ▪ Purchase decisions are mostly made on physiological/social/ psychological needs ▪ Less technical expertise ▪ Non-personal relationship
Channel characteristics	▪ More direct channels ▪ Fewer intermediaries/ middlemen	▪ Indirect channels ▪ Multiple layers of intermediaries
Promotional characteristics	▪ Emphasis on personal selling	▪ Emphasis on advertising
Price characteristics	▪ Competitive bidding and negotiated prices ▪ List prices for standard products	▪ List prices or maximum retail price (MRP)

With the growth of the services sector, marketers realized that services cannot be marketed in the same way as the products. Certain characteristics of services posed serious problems for marketers who realized that services marketing must be done differently and not with the same marketing mix (4 Ps) variables. Service characteristics like intangibility (service firms don’t sell a tangible thing, but a promise) inseparability (production and consumption of services take place at about the same time), heterogeneity (the problem due to the fact that no two service providers are like, nor are the service consumers) and perishability (service providers cannot maintain inventories of their products). To cope with these challenges, service marketers suggest additional 3 Ps – process, physical evidence and people. The process is aimed at solving the heterogeneity or variability problem associated with the services by providing a service blueprint. The physical evidence solves some of the problems associated with the intangible nature of services. The physical evidence in terms of service environment, equipment, personnel and so on attempts to tangibilize the intangible. The final P – People – gives lot of attention to the service providers because they are, strictly speaking, part of the service provided. They can influence the perceived service quality in a big way.

With the world becoming a global village, marketers started targeting global audience for their products and services. International marketers implement the basic marketing framework discussed earlier. However transactions that cross national boundaries encounter an additional set of environmental factors. For example, differences in laws, economic conditions, cultural and business norms and consumer preferences other demand variations in marketing strategies. The biggest challenge in international marketing is managing the international business environment. With many uncontrollable factors, sharing complex relationships among them, the international marketer faces the dilemma of whether to standardize or differentiate his marketing mix.

Non-profit organizations encounter a special set of characteristics that influence their marketing activities. Like for-profit firms, non-profit firms may market tangible goods and/or intangible services and operate in B2C and B2B markets. An important distinction is that profit-seeking businesses tend to focus their marketing on just one public – their customers. Non-profit businesses however must often market to multiple publics (say, their clients and sponsors), which complicates decision making regarding the markets to target. Also a customer or service user may wield less control over the organization's destiny than would be true for customers of a profit-seeking firm. As a result, non-profit marketing must fine tune its marketing variables to adjust to these conditions.

Activity 1.1.4
Match the following:

(1) Product marketing	-	(A) AIDS awareness campaign
(2) Service marketing	-	(B) Selling iron ore to a steel manufacturer
(3) Consumer marketing	-	(C) Selling ice creams to adults
(4) Industrial marketing	-	(D) Disney setting up a park in Hong Kong
(5) International marketing	-	(E) Setting up an ayurvedic massage center
(6) Non-profit marketing	-	(F) Selling electric bulbs

Functions of Marketing

Firms must spend money to create time, place and ownership utilities as discussed earlier. Several studies have been made to measure marketing costs in relation to overall product costs and service costs and most estimates have ranged between 40-60 percent. These costs are not associated with raw materials or any of the other production functions necessary for creating form utility. What then does the consumer receive in return for this proportion of marketing cost? This question is answered by understanding the functions performed by marketing.

In the following table, marketing is responsible for the performance of 8 universal functions: buying, selling, transporting, storing, standardizing and grading, financing, risk taking and securing marketing information. Some functions are performed by manufacturers, others by marketing intermediaries like wholesalers and retailers. Buying and selling, the first two functions represent exchange functions. Transporting and storing are physical distribution functions. The final four marketing functions – standardizing and grading, financing, risk taking and securing market information – are often called facilitating functions because they assist the marketer in performing the exchange and physical distribution functions.

Table 1.1.3 Functions of Marketing

Marketing function	Description
A. Exchange functions	
1. Buying	Ensuring that product offerings are available in sufficient quantities to meet customer demands
2. Selling	Using advertising, personal selling and sales promotion to match goods and services to customer needs
B. Physical distribution functions	
3. Transporting	Moving products from their points of production to locations convenient for purchasers
4. Storing	Warehousing products until needed for sale
C. Facilitating functions	
5. Standardizing and grading	Ensuring that product offerings meet established quality and quantity control standards of size, weight and so on
6. Financing	Providing credit for channel members or consumers
7. Risk taking	Dealing with uncertainty about consumer purchases resulting from creation and marketing of goods and services that consumers may purchase in the future
8. Securing marketing information	Collecting information about consumers, competitors and channel members for use in marketing decision making

Case Study: Master of the Online Supermall
(excerpt from Business Today, May 2004)

Amazon.com could well go down in history as a love child born of the heady fling that the stockmarket had with dotcoms in the late 1990s. But the company, founded by Jeff Bezos in July 1995 when the internet was still an untested business medium, is a survivor-par-excellence. It floundered a bit in the swirl of the dotcom bust, but unlike thousands that were swept away, Amazon.com reinvented itself and emerged stronger.

The 40-year old Bezos, a computer science grad from Princeton University, is the pioneer of Internet Retailing. His compelling vision introduced a new paradigm for retail, the click-and-buy model; buy goods from a website instead of a physical store, from wherever there is an internet connection: home, office or cyber-café. A model that gave convenience to buyers, and mind-boggling market reach to sellers.

Named after the mighty Amazon river and its numerous tributaries that surge through dense rain forests, Amazon.com was started with an initial investment of a few thousand dollars. In less than three weeks after the website went live, Bezos and his wife Mackenzie were pulling in sales of over $20,000 a week. And soon after going public in 1997, the company had a market capitalization higher than that of its brick-and-mortar rivals. In 1999, Bezos was chosen as *Time* Magazine's 'Person of the Year'. But things changed soon after and the dotcom bust saw Amazon.com lose almost 90 percent of its market cap in 2000.

Bezos didn't give up on his vision. He set about transforming Amazon.com from a website selling books into something much bigger: the world's largest online retailing platform. A series of tie-ups with companies like Toys R Us and Target helped give the website the feel of an online supermall where a customer could buy almost anything. Marketing initiatives followed – from free shipping to highly discounted prices to very customized offerings (based on customer profile) to wide distribution through sites which can divert traffic to Amazon.com for a small commission. But the biggest move was Bezos' decision to make the site 'more global'.

The moves have paid off. The company announced its first full-year profit in 2003. It has been making money now for three straight quarters and revenues have exceeded a billion dollars for the last six quarters. If proof was needed that there is money to be made in online retailing, this is it. And Bezos has proved that the right idea, coupled with perseverance, pays in the end.

Questions: How does Amazon.com bring utility or create value for its customers? Explain the marketing framework of Amazon.com? What do you learn about marketing from the Amazon story?

Unit – I

Lesson - 1.2
Marketing Concepts

Objectives

In this lesson, we will introduce you to the conceptual ideas that makeup the marketing function of a business. After you work out this lesson, you should be able to:

- List out the concepts of marketing
- Understand how these concepts are interconnected
- Explain how marketing is changing in a connected world

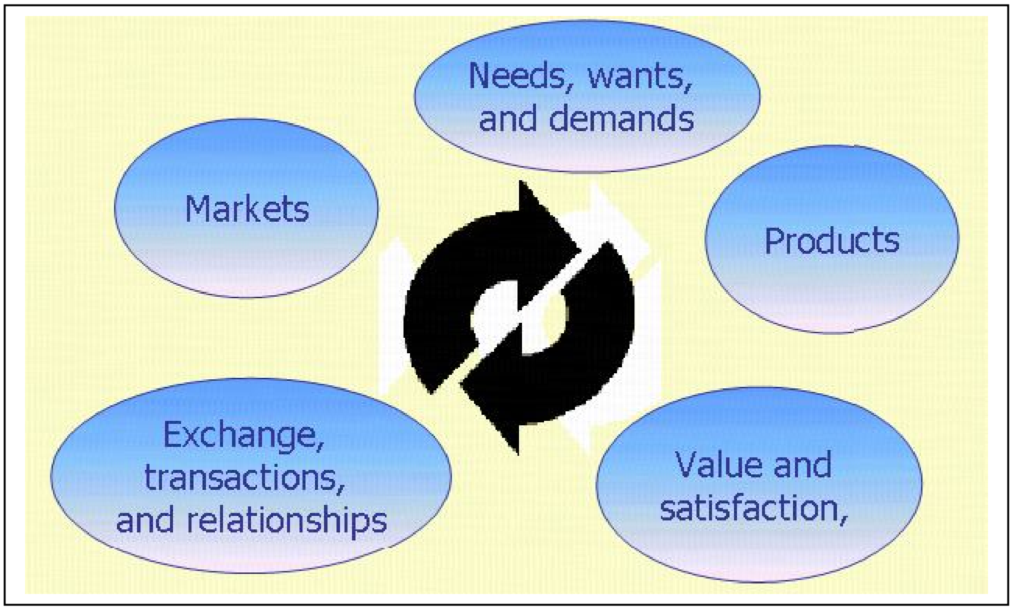
In this lesson, we will discuss the following:

- Needs, wants and demands
- Products
- Value and satisfaction
- Exchange, transactions and relationships
- Markets
- Marketing in a connected world

Introduction

Having defined marketing in the previous lesson as a social and managerial process by which individuals and groups obtain what they need and want through creating and exchanging products and value with others, this lesson examines the important concepts that are included and implied in this definition. These concepts are indicated in Figure 1.2.1 and it is important to note that they are linked, with each one building on the one before it.

Figure 1.2.1 Marketing concepts


Needs, wants, and demands
Markets
Products
Exchange, transactions, and relationships
Value and satisfaction,

Needs, Wants and Demands

The most basic concept underlying marketing is that of human needs. A need is a state of felt deprivation. It is a part of the human makeup. Humans have many needs, viz., physical needs, social needs, spiritual needs and so on. Wants are the form taken by needs as they are shaped by the one's culture and personality. Wants are thus shaped by both the internal and external factors. Wants are described in terms of objects that will satisfy needs. For example, thirst is a need. To quench this thirst, a person may consider a number of options – drink water or a soft drink or a fruit juice. These objects (which represent the different choices for a person to fulfill his/her need) comprise the potential want-list. As people are exposed to more objects that arouse their interest and desire, marketers try to provide more choices, that is, more want-satisfying products. People have almost unlimited wants but limited resources. Therefore, they want to choose products that provide the most satisfaction for their money. When backed by buying power (ability), a want becomes a demand.

Products

A product is anything that can be offered to a market to satisfy a need or want. People satisfy their needs and wants with products. Though the word suggests a physical object, the concept of product is not limited to physical objects. Marketers often use the expressions goods and services to distinguish between physical products and intangible ones. These goods and services can represent cars, groceries, computers, places, persons and even ideas. Customers decide which entertainers to watch on television, which places to visit for a holiday, which ideas to adopt for their problems and so on. Thus the term 'product' covers physical goods, services and a variety of other vehicles that can satisfy customers' needs and wants. If at times the term 'product' does not seem to be appropriate, other terms such as market offering, satisfier are used.

Value and Satisfaction

When the customers have so many choices to choose from to satisfy a particular need, how do they choose from among these many products? They make their buying choices based on their perceptions of a product's value. The guiding concept is customer value. A customer will estimate the capacity of each product to satisfy his need. He/She might rank the products from the most need-satisfying to the least need-satisfying. Of course, the ideal product is the one which gives all the benefits at zero cost, but no such product exists. Still, the customer will value each existing product according to how close it comes to his/her ideal product and end up choosing the product that gives the most benefit for the rupee – the greatest value.

Exchange, Transactions and Relationships

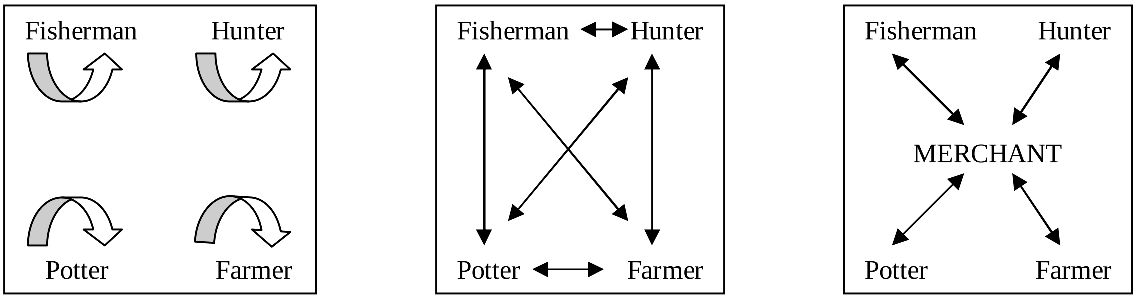
Marketing occurs when people decide to satisfy needs and wants through exchange. Exchange is the act of obtaining a desired object from someone by offering something in return. Thought it is only one of the many ways people can obtain a desired object, it allows a society to produce much more than it would with any alternative system. For an exchange to take place, several conditions must be satisfied. Of course, at least two parties must participate, and each must have something of value to the other. Each party also must want to deal with the other party and each must be free to accept or reject the other's offer. Finally, each party must be able to communicate and deliver. These conditions simply make exchange possible. Whether the exchange actually takes place depends on the parties' coming to an agreement. If they agree, we must conclude that the act of exchange has left both of them better off or at least not worse off. After all, each was free to reject or accept the offer. In this sense, exchange creates value just as production creates value. It gives customers more consumption possibilities.

A transaction is marketing's unit of measurement. It consists of a trade of values between two parties. A monetary transaction involves trading goods and services in return for money whereas a barter transaction involves trading goods and services for other goods and services. Transaction marketing is part of the larger idea of relationship marketing. Marketing is shifting from trying to maximize the profit on each individual transaction to maximizing mutually beneficial relationships with consumers and other parties. This is based on the assumption that if good relationships are built, profitable transactions will simply follow.

Markets

The concept of transactions leads to the concept of a market. A market is the set of actual and potential buyers of a product. It may exist in a physical environment as a marketplace or in a virtual environment (on the internet platform) as a marketspace. To understand the nature of a market, imagine a primitive economy consisting of only four people – a farmer, a fisherman, a potter and a hunter. Figure 1.2.2 shows the different ways in which these traders could meet their needs. In the first case, self-sufficiency, they gather the needed goods for themselves. In the second case, decentralized exchange, each person sees the other three as potential buyers who make up a market. In the third case, centralized exchange, a new person called a merchant appears and locates in a central area called a marketplace. Each trader brings goods to the merchant and trades for other needed goods. Merchants and central marketplaces greatly reduce the total number of transactions needs to accomplish a given volume of exchange. As economies grow, exchange becomes even more centralized, as seen in the growth of huge companies. Large supermarkets now serve millions of people who formerly shopped in smaller outlets.

Figure 1.2.2 Moving towards centralized exchange



Marketing in a connected world

The internet and the resultant connected world has posed some special challenges and opportunities for marketers. Prof. Mohanbir Sawhney (Kellogg School of Management) has used two interesting metaphors (hunting Vs. gardening) to describe marketing hither-to and marketing hence-forth.

Marketing Hhither-to:	Marketing Hence-forth:
Marketing as hunting	**Marketing as gardening**
Market as a jungle Customers as targets Marketers as hunters Segmentation as rifle Vs. shotgun approach Products as mousetraps Salespeople as baiters-and-switchers Promotions as campaigns Relationships as conquests/acquisitions Loyalty as lock-in and retention Customer visits as eyeballs and traffic	Customer relationships as garden to be tended Marketer as gardener Partners as players in the ecosystem Customer loyalty as roots Lifetime profits as harvest Marketing process as seed, feed and yield

The underlying reason for this shift is the rise of information democracy made possible by the internet. For information symmetry (characterized by scarce information, ill-informed customers, monologue kind-of exchanges and 'command-and-control' marketing) the society is moving towards information democracy (characterized by ubiquitous information, well-informed customers, conversations kind-of exchanges and 'connect-and-collaborate' marketing). The Cluetrain Manifesto (www.cluetrain.org) describes markets as conversations in the following manner: *Markets are conversations.*

Their members communicate in language that is natural, open, honest, direct, funny and often shocking… Most corporations, on the other hand, only know how to talk in the soothing, humorless monotone of the mission statement, marketing brochure, and your-call-is-important-to-us busy signal. Same old tone, same old lies. No wonder networked markets have no respect for companies unable or unwilling to speak as they do.

In the connected world, the empowered customers can: (1) Get objective information for multiple suppliers without relying on the manufacturer or the retailer (e.g., Edmunds.com); (2) Initiate requests for information and advertising from manufacturers (e.g., DealTime.com); (3) Design and configure customized offerings (e.g., Dell.com); (4) Use buying agents to pit sellers against each other (e.g., Freemarkets Online); (5) Unbundle offerings and arbitrage across channels (e.g. Ritz Camera); (6) Pay by the minute, by the month, by the mile (e.g., IBM e-business on demand) and (7) Communicate with peers and experts for feedback on products and brands (e.g. Amazon.com and Epinions.com)

Unit – I

Lesson 1.3
Marketing Process

Objectives

In this lesson, we will introduce you to the activities that makeup the marketing process. After you work out this lesson, you should be able to:

- Identify the parts of the marketing process
- Understand the relationships among the parts of the marketing process
- Explain how the marketing process creates, captures and sustains value for the customer

In this lesson, we will discuss the following:

- Formulation of marketing strategy
- Marketing planning
- Marketing programming, allocating and budgeting
- Marketing implementation
- Monitoring and auditing
- Analysis and research
- Schematic of marketing process

Introduction

While there is lot of focus on the substance of marketing, particularly the marketing mix, an equally important aspect of marketing is the marketing process – how marketers do their job. The process is equal in importance to the substance because the process determines the nature and quality of the decisions made. A good process is likely to lead to a good decision. On the other hand, a faulty process will produce a good decision only on a random or accidental basis.

The marketing process can be divided in several different ways. One popular conceptualization of marketing tasks is:

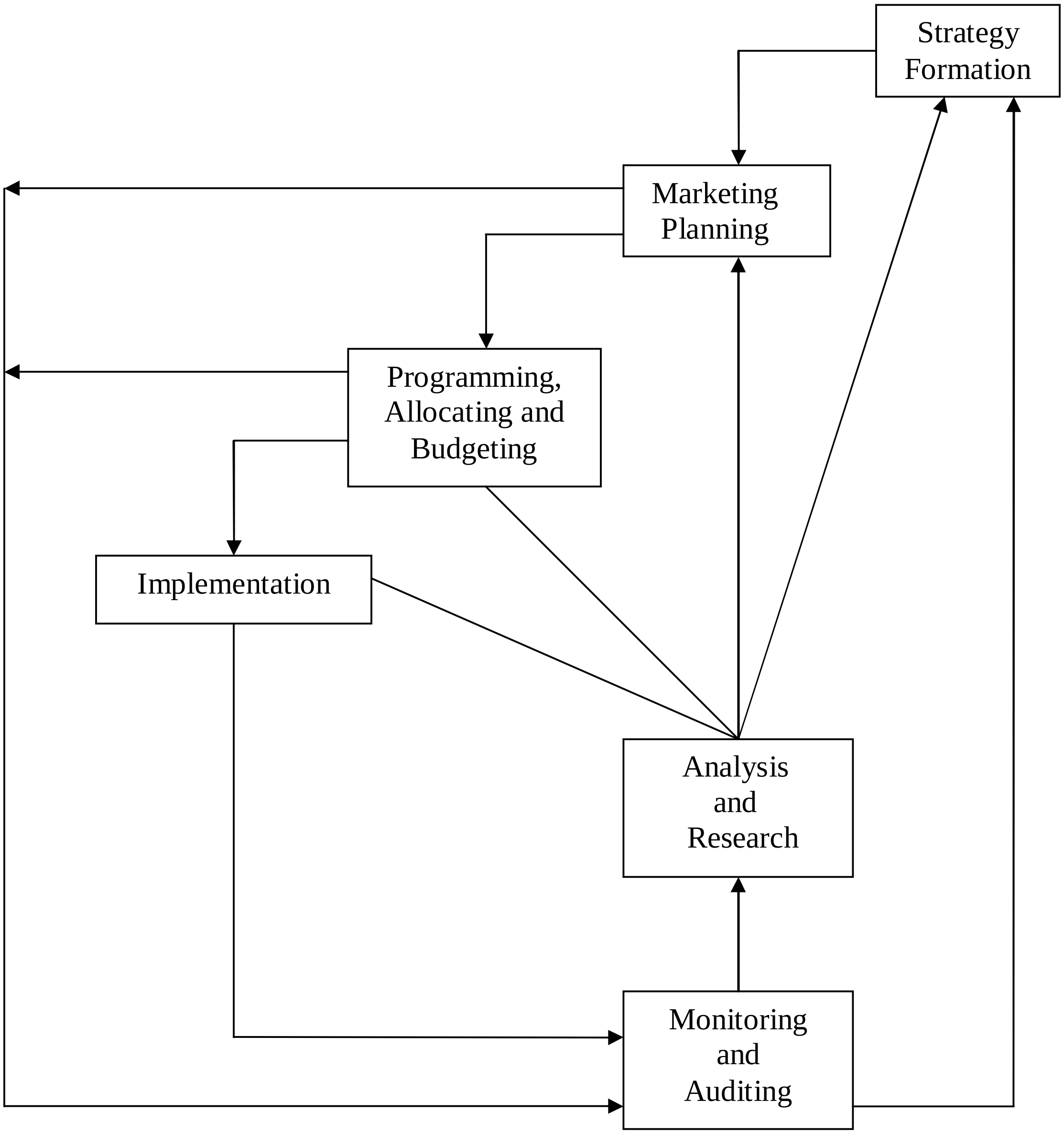
1. Strategy formulation – the development of the broadest marketing/business strategies with the longest term impact

2. Marketing planning – the development of longer-term plans which have generally stronger impact than the short-term programs
3. Marketing programming, allocating and budgeting – the development of short-term programs which generally focus on integrated approaches for a given product and on the allocation of scarce resources such as sales effort or product development time across various products and functions
4. Marketing implementation – the actual task of getting the marketing job done
5. Monitoring and auditing – the review and analysis of programs, plans and strategies to assess their success and to determine what changes must be made
6. Analysis and research – the deliberate and careful acquisition and examination of qualitative and quantitative data to improve decision making

Though implied and considered as part of the overall corporate planning, the importance of situation analysis can never be undermined during marketing strategy formulation. Especially under product policies, but throughout the marketing mix elements, the company, customer and competitive scanning is so essential to marketing success. Situation analysis describes the process by which environmental assessment, marketing research and market size/growth estimates get done. It pays particular attention to environment scanning skills useful in forecasting and modeling consumer behaviour.

It is important to note that each part of the process is intimately related to the other parts of the process. Figure 1.3.1 is an attempt to capture the more important relationships. The dividing lines between any two parts of the process are vague and unclear. This is particularly true of those elements of the processes which are clearly connected. For example, the distinction between a marketing plan and a marketing program is very unclear for many. But the precise boundaries are not as important as the general concept. Each element can be divided into smaller subelements. For example, marketing planning includes market assessment which is the evaluation and selection to serve specific customer markets. Product line planning is another subelement of marketing planning.

Figure 1.3.1 Relationships among the six parts of the marketing process


Strategy Formation
Marketing Planning
Programming, Allocating and Budgeting
Implementation
Analysis and Research
Monitoring and Auditing

Formulation of marketing strategy

Strategy formulation is the broadest, longest-term marketing activity. At this stage, complex and subtle integration with other corporate functions is required. All of the functional strategies must fit together into a business strategy. Because marketing deals with customers and the competitive environment, it is an early part of the total strategy formulation process. When done well, it is impossible to separate the marketing strategy from the corporate strategy. The two meld into a unified whole.

The strategic process is one of working with market dynamics (a particular segment or selection of the market) to achieve a solid positioning of the product/service offering that contains a clear ‘benefit promise’ to the consumer which is differentiable from the offers of the competition and which thus positions the firm well for potential competitive responses to its actions.

Marketing Planning

Marketing planning involves objectives and plans with a 2-5 year time horizon and is thus further from day-to-day activity of implementation. Because of their broader nature and longer-term impact, plans are typically developed by a combination of higher-level line managers and staff specialists. If the specialists take over the process, it loses the commitment and expertise of the line managers who are responsible for carrying out the plan. The planning process is probably more important than the final planning document. The process ensures that a realistic, sensible, consistent document is produced and leads to important organizational learning and development in its own right.

Marketing Programming, Allocating and Budgeting

This part of the marketing process involves a good deal of detail and focuses generally on the one-year time horizon.

Programs can be related to either one element of the marketing mix such as distribution for one or more products or to all elements of the mix for a single product or market. To some extent, the choice will be determined by the nature of the company’s organization. The more functional the organization (i.e. separation of marketing functions such as advertising, sales, etc.), the more likely it is that the programs will focus on one aspect of the mix across all products and markets. On the other hand, companies which organize around products or markets tend to also develop programs for each of them.

Allocating is a necessary function because there is never enough of any scarce resource such as advertising budget or distribution effort to meet the ‘needs’ of all products, markets and programs. In many ways, marketing is deciding what not to do: which prospects not to sell to, which products not to produce to, etc. Allocation is the formal process of choosing what to do and what not to do, as well as choosing how much to do. Because marketers tend to be optimists, they often underestimate the amount of effort which will be required to accomplish a goal. Allocation requires the stark realism to separate the clearly feasible from the hopeful. It forces the marketer to set explicit priorities and to make hard decisions.

Budgeting reflects the programs and allocations in a set of quantitative forecasts or estimates which are important within and beyond the marketing function. The budgets generally include financial pro formas which are used by the control and finance functions to forecast cash flows and needs. They also generally include unit sales forecasts which are used by production scheduling personnel to 'load the factory' or service operation. If the forecasts are too low, customer needs are unmet and sales are lost. If the forecasts are too high, capacity sits idle and costs are much higher than they should have been.

Marketing Implementation

Strategy formulation, marketing planning, and programming, allocating and budgeting all lead to marketing implementation as shown in Figure 1.3.1. This is the execution phase which, in part produces the actual results. Poor implementation can ruin even the best strategies, plans and programs. The total purpose of all that goes before implementation is to ensure excellent execution.

Implementation means different things to different people in the organization. To the salesperson, it means going through all of the steps of the selling process, while to the sales manager, it might mean reorganizing the whole sales force. Because of the relatively short time frame involved in most implementation activities, monitoring and auditing are generally easier than for the longer-term strategies and plans. Implementation is very people-oriented. The results of implementation are manifested in people doing things – buying, selling, training, reorganizing, etc. Marketing implementation is unique compared to implementation in most other functional areas because the primary focus of marketing is outside the company. Thus marketing implementation focuses on prospects, customers, distributors, retailers, centers of influence (who are the influencers in a buying decision – they specify but do not purchase). But marketing implementation also includes dealing with other functional areas to gain support and to develop coordination. For example, product managers must implement their plans and programs through product development, production, service and logistics personnel in other functional areas.

Marketing implementation involves a very interesting tension between the structures the firm puts in place to guide marketing efforts and the skills of the managers doing the marketing job. In most firms, what happens is that over time the structures become rigid and dysfunctional to changing marketplace needs, which guides the firm to destinations it does not want to reach! It is only by the timely intervention of the marketers, using their personal skills to 'subvert the organization toward quality' that good marketing actions result.

Monitoring and Auditing

One reason to develop plans, programs and budgets is to have a set of goals or standards against which to measure performance. Marketing audits usually include two parts. The first is an assessment of performance against quantitative goals. The second part of a comprehensive audit reviews the processes and other non-quantifiable aspects of the marketing operation. Because marketing is a mixture of art and science, quantitative and qualitative, and because it involves so many interactive variables, it is hard to audit. Standards are few and comparisons are difficult.

The audit raises a variety of important topics:

1. Who should perform the audit? Can the planners, programmers and executors audit their own performance without bias? If they cannot, who knows enough about the operation to perform the audit? Should outsiders such as consultants be involved and in what capacity?
2. How often should the audit be performed? Should it be on a regular basis or only at certain important points?
3. How comprehensive should the audit be? Should it involve all aspects of marketing or just some?

While auditing normally refers to an activity which is done only on certain occasions, monitoring generally refers to a more day-to-day review activity. It also often refers more to a review of external data than internal activities. It, too, is an important part of the total marketing process because it provides a frequent check of progress against plans and programs.

Analysis and Research

All marketing decisions should be based upon careful analysis and research. The analysis and research need not be quantitative, but it should be deliberate and should be matched to the magnitude of the decision being made. While formal analysis and research are important, nothing replaces common sense and good judgment. The marketer's kit has some very powerful analytical tools and the rapid development of decision support systems, mathematics including statistics, and other supporting disciplines such as psychology and sociology insure that the diversity and power of the tools will continue to increase. All of the tools must be applied carefully and intelligently to the decision at hand. It is a fine line, indeed between healthy skepticism and arrogant neglect of useful tools. The right analytical tool well applied can substantially improve marketing decision making.

Table 1.3.1 has two dimensions. The first is temporal – it shows the natural development from strategy formulation through planning, programming, allocating and budgeting on to implementation. This process is not nearly as 'clean and separated' as the table implies. The activities are interrelated and contemporaneous. The second dimension is the lateral connection to other functional parts of the organization, such as production and operations, finance, control and human resources management. Each step has a company or business counterpart in the right-hand column. The marketing strategy thus becomes part of the total corporate strategy, which includes all functional areas. The marketing plan is often part of a broader corporate business plan. The marketing plan is usually the 'front end' of the corporate plan, because it spells out the operation, human and financial resources needed to support the organization's approach to its markets.

Table 1.3.1 Activities and Lateral Connections

Time Horizon	Activities	Names of Activities	Lateral Connections
Long	1. set overall, long-term goals and basic approach to marketplace	1. formulation of marketing strategy	1. corporate strategy
Medium	2. set two- to five-year objectives and plans with more detail for shorter time horizons	2. marketing planning	2. business plan

Short	3. set one-year objectives and detailed plans; allocate resources to achieve goals specified in 3 and 4	3. marketing programming, allocating and budgeting	3. operating programs and budgets
	4. execute plans, programs and budgets	4. marketing implementation	4. operating activities
	5. evaluate results of execution against goals set in steps 1, 3 and 4, above; specify corrective action where necessary	5. monitoring and auditing	5. business audits
	6. gather and analyze quantitative and qualitative data from within and outside the company	6. analysis and research	6. business analysis and research

Marketing programs and budgets are usually part of the organization's fundamental operating documents. For example, the sales forecasts in the programs and budgets become the production schedule for the manufacturing function. Those, in turn, become the staffing programs for the human resource function and indicate the working capital needs to be supported by the financial function. If finance cannot support such a high level of inventory and accounts receivable, the sales forecast, production schedule and staffing program must be scaled down. In most organizations, great effort must be devoted to such lateral connections. The coordination needs are very high and the amount of conflict often great. Risk aversion and opportunity sensitivity differ among functions. Varying reward systems sometimes encourage different types of behaviour. The organization must develop formal and informal ways to foster good, open lateral connections.

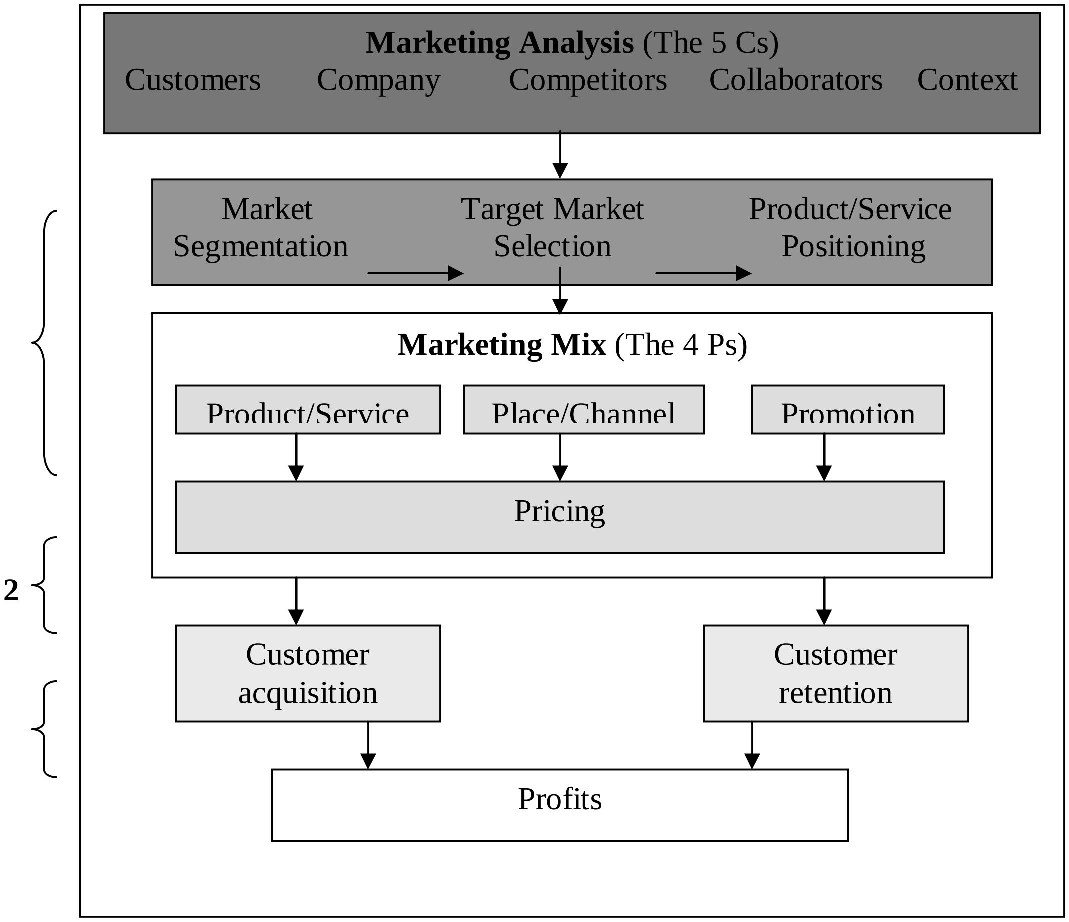
Schematic of Marketing Process

Figure 1.3.2 represents a schematic describing a general process of marketing strategy development. As shown, five major areas of analysis (5 Cs) underlie marketing decision making – customers, company, competitors, collaborators and context. The questions to raise in each of these areas are:

- Customer needs - What needs do we seek to satisfy?
- Company skills - What special competencies do we possess to meet those needs?
- Competition - Who competes with us in meeting these needs?
- Collaborators - Who should we enlist to help us and how do we motivate them?
- Context - What environmental (say, cultural, technological or legal) factors limit what is possible?

This leads first to specification of a target market and desired positioning and then to the marketing mix (4 Ps). This results in customer acquisition and retention strategies driving the firm’s profitability. In this schematic, value creation happens by identifying target segment, establishing a product/service positioning and developing the suitable product, place (distribution) and promotion for the chosen market segment. The pricing decision helps to capture value – for the company and for the customer. Value is sustained by acquiring and retaining the customers at a profit for the firm.

Figure 1.3.2 Schematic of marketing process


Marketing Analysis (The 5 Cs)
Customers
Company
Competitors
Collaborators
Context
Market Segmentation
Target Market Selection
Product/Service Positioning
Marketing Mix (The 4 Ps)
Product/Service
Place/Channel
Promotion
Pricing
2
Customer acquisition
Customer retention
Profits

Unit – I

Lesson 1.4
Marketing Environment

Objectives

In this lesson, we will introduce you to the forces that define marketing's external environment. After you work out this lesson, you should be able to:

- Identify, analyze and monitor external forces and assess their potential impacts on the firm's goods and services
- Understand how marketers formulate their strategy within the frame of reference provided by the forces in the external environment

In this lesson, we will discuss the following:

- Competitive environment
- Political-legal environment
- Economic environment
- Technological environment
- Social-cultural environment

Introduction

Industry competition, legal constraints, the impact of technology on product design and social concerns are some of the many important conditions that shape the business environment. This lesson examines the forces that define marketing's external environment. Every organization needs to think seriously about the environments in which it operates. All firms must identify, analyze and monitor external forces and assess their potential impacts on the firm's goods and services. Although external forces frequently operate outside the marketing manager's control, decision makers still must consider those 'uncontrollable' influences together with the variables of the marketing mix in developing the firm's marketing plan and strategies.

Environmental Scanning and Environmental Management

Marketers must carefully and continually monitor crucial trends and developments in the business environment. Environmental scanning is the process of collecting information about the external marketing environment to identify and interpret potential trends. This activity then seeks to analyze the collected information and determine whether identified trends represent opportunities or threats to the company. This judgment, in turn, allows a firm to determine the best response to a particular environmental change.

Environmental scanning is a vital component of effective environmental management. Environmental management is the effort to attain organizational objectives by predicting and influencing the firm's competitive, political-legal, economic, technological and social-cultural environments. The development of a global marketplace has complicated environmental scanning and environmental management. These processes may now need to track political developments, economic trends and cultural influences anywhere in the world.

While the marketing environment may exceed the confines of the firm and its marketing mix components, effective marketers continually seek to predict its impact on marketing decisions and to modify its conditions whenever possible.

The Competitive Environment

The interactive exchange in the marketplace as organizations vie with one another to satisfy customers creates the competitive environment. Marketing decisions by each individual firm influence consumer responses in the marketplace. They also affect the marketing strategies of competitors. As a consequence, decision makers must continually monitor competitors' marketing activities – their products, channels, prices and promotions.

Few organizations enjoy monopoly positions in the marketplace. Utilities such as electricity, water and cooking gas accept considerable regulation from local authorities. Other firms, such as manufacturers of pharmaceutical products, sometimes achieve temporary monopolies as a result of patents. Marketers actually face three types of competition. Their most direct competition occurs among marketers of similar products, as when an insurance firm competes with other insurance firms. The second type of competition involves products that users can substitute for one another. In the transportation industry, the no-frills, low-cost airliners compete with train and luxury bus services. A change such as a price increase or an improvement in a product's capabilities can directly affect demand for substitute products. The final type of competition occurs among all other organizations that compete for consumers' purchases. Traditional economic analysis views competition as a battle among companies in a single industry or among firms that product substitute goods and services. Marketers must, however, accept the argument that all firms compete for a limited pool of discretionary buying power.

Because the competitive environment often determines the success or failure of a product, marketers must continually assess competitors' marketing strategies. A firm must carefully monitor new product offerings with technological advances, price reductions, special promotions or other competitive variations, and the firm's marketing mix may require adjustments to counter these changes.

Every firm's marketers must develop an effective strategy for dealing with its competitive environment. One company may compete in a broad range of markets in many areas of the world. Another may specialize in particular market segments, such as those determined by customers' geographic, age or income characteristics. Determining a competitive strategy involves answering three questions:

(1) Should we compete?

The answer to this questions depends on the firm's resources, objectives and expectations for the market's profit potential. A firm may decide not to pursue or continue operating a potentially successful venture that does not mesh with its resources, objectives or profit expectations.

(2) If so, in what markets should we compete?

The answer requires marketers to acknowledge their limited resources (sales personnel, advertising budgets, product development capabilities and so on). They must accept responsibility for allocating these resources to the areas of greatest opportunity.

(3) How should we compete?

This requires marketers to make product, pricing, distribution and promotional decisions that give their firm a competitive advantage in the marketplace. Firms can compete on a wide variety of claims, including product quality, price and customer service. For example, a retailer may gain competitive advantage by providing superior customer service, while another retailer competes by providing low prices.

With increased international competition and rapid changes in technology, many firms are using time as a strategic competitive weapon. A time-based competition strategy seeks to develop and distribute goods and services more quickly than competitors. The flexibility and responsiveness of a time-based strategy enables the firm to improve product quality, reduce costs, respond to competition and expand the variety of its products to cover new market segments and enhance customer satisfaction.

The Political-Legal Environment

No one should start playing a new game without first understanding the rules, yet some businesses exhibit remarkably limited knowledge about marketing's political-legal environment – the laws and their interpretations that require firms to operate under certain competitive conditions and to protect consumer rights. Ignorance of laws, ordinances and regulations or failure to comply with them can result in fines, embarrassing negative publicity and possibly expensive civil damage suits.

Businesses need considerable diligence to understand the legal framework for their marketing decisions. Numerous laws and regulations affect those decisions, many of them vaguely stated and inconsistently enforced by a multitude of different authorities. Regulations affect marketing practices, as do the actions of independent regulatory agencies. These requirement and prohibitions touch on all aspects of marketing decision making – designing, labeling, packaging, distributing, advertising and promoting goods and services. To cope with the vast, complex and changing political-legal environment, many large firms have in-house legal department; small firms often seek professional advice from legal experts. All marketers, however, should be aware of the major regulations that affect their activities.

Some of potential issues from the political-legal environment to affect businesses include:

- The national foreign policy can dominate the international business decisions of the local firms
- The political ideology of the Government can affect the international brands wanting to enter a market
- The competitors who work closely with the government can help erect trade barriers for a firm
- Global trade organizations can enforce trade barriers when their regulations and guidelines are not observed
- A host nation may levy anti-dumping duties on a foreign firm and such a decision may be dominated by the local businesses lobbying with the government
- Copyright infringements, trademark and intellectual property rights violations
- Direct comparative advertisements may not be allowed in few countries

- Use of children is advertising and advertising to children are banned in certain countries
- Price regulations preempt any pricing strategy of a firm
- A detailed displaying of the ingredients in product labels is mandatory in most countries
- The channel members are given the additional responsibility of verifying the eligibility of the prospective buyers for certain products
- Use of certain raw materials or methods of manufacturing are prohibited in certain countries
- Industry watch dogs and consumer groups are always on the prowl for any unethical trade practices

Each one of the above issues has serious implications for the marketer in his marketing decision making. Ignorance of the law is no excuse and breaking of the law is an offence.

The Economic Environment

The overall health of the economy influences how much consumers spend and what they buy. This relationship also works the other way. Consumer buying plays an important role in the economy's health. Indeed, consumer outlays perennially make up around two-thirds of overall economic activity. Since all marketing activity is directed toward satisfying consumer wants and needs, marketers must understand how economic conditions influence consumer buying decisions.

Marketing's economic environment consists of forces that influence consumer buying power and marketing strategies. They include the stage of the business cycle, inflation, unemployment, resource availability and income.

Historically, a nation's economy tends to follow a cyclical pattern consisting of four stages: prosperity, recession, depression and recovery. Consume buying differs in each stage of the business cycle and marketers must adjust their strategies accordingly. In times of prosperity, consumer spending maintains a brisk pace. Marketers respond by expanding product lines, increasing promotional efforts and expanding distribution in order to raise market share and raising prices to widen their profit margins. During recessions, consumers frequently shift their buying patterns to emphasize basic, functional products that carry low price tags. During such times, marketers should consider lowering prices, eliminating marginal products, improving customer service, and increasing promotional outlays to stimulate demand. Consumer spending sinks to its lowest during a depression. In the recovery stage of the business cycle, the economy emerges from recession and consumer purchasing power increases. While consumers' ability to buy increases, caution often restrains their willingness to buy. They may prefer to save than to spend or buy on credit. Business cycles, like other aspects of the economy, are complex phenomena that seem to defy the control of marketers. Success depends on flexible plans that can be adjusted to satisfy consumer demands during the various business cycle stages.

Inflation devalues money by reducing the products it can buy through persistent price increases. It would restrict purchases less severely if income were to keep pace with rising prices, but often it does not. Inflation increases marketers' costs such as expenditures for wages and raw materials and the resultant higher prices may therefore negatively affect sales. Inflation makes consumers conscious of prices, especially during periods of high inflation. This influence can lead to three possible outcomes, all of them are important to marketers. (1) consumers can elect to buy now, in the belief that prices will rise later, (2) they can decide to alter their purchasing patterns and (3) they can postpone certain purchases.

Unemployment is defined as the proportion of people in the economy who do not have jobs and are actively looking for work. It rises during recessions and declines in the recovery and prosperity stages of the business cycle. Like inflation, unemployment affects marketing by modifying consumer behaviour. Instead of buying, consumers may choose to build their savings.

Income is another important determinant of marketing's economic environment, because it influences consumer buying power. By studying income statistics and trends, marketers can estimate market potential and develop plans for targeting specific market segments. For marketers, a rise in income represents a potential for increasing overall sales. But they are most interested in the disposable income, which is the amount of money that people have to spend after they have paid for necessities. Consumers' disposable income varies greatly by demographic variables such as age group and educational levels.

Resources are not unlimited. Brisk demand may bring in orders that exceed manufacturing capacity or outpace the response time required to gear up a production line. A shortage may also reflect a lack of raw materials, component parts, energy or labour. Regardless of the cause, shortages require marketers to reorient their thinking. One reaction is demarketing, the process of reducing consumer demand for a product to a level that the firm can reasonably supply. A resource shortage presents marketers with a unique set of challenges. They may have to allocate limited supplies which is a sharply different activity from marketing's traditional objective of expanding sales volume.

The Technological Environment

The technological environment represents the application to marketing of discoveries in science, inventions and innovations. New technology results in new goods and services for consumers; it also improves existing products, strengthens customer service and often reduces prices through new, cost-efficient production and distribution methods. Technology can quickly make products obsolete, but it can just as quickly open up new marketing opportunities. Technology is revolutionizing the marketing environment. Technological innovations not just create new products but also whole new industries. Recently, the Internet has been transforming the way companies collaborate with different stakeholders to create more value for the customers. Technology can sometimes address social and environmental concerns by offering a cheap, non-polluting, energy-conserving, safe product and also create parity among consumers by providing equal access and opportunity.

Marketers must closely monitor the technological environment for a number of reasons. Creative applications of new technologies give a firm a definite competitive advantage. Marketers who monitor new technology and successfully apply it may also enhance customer service.

The Social-Cultural Environment

The social-cultural environment of marketing describes the relationship between marketing and society and its culture. Marketers must cultivate sensitivity to society's changing values and to demographic shifts such as population growth and age distribution changes. These changing variables affect consumers' reactions to different products and marketing practices. The social-cultural context often exerts a more pronounced influence on marketing decision making in the international arena than in the domestic arena. Learning about cultural and social differences among countries prove a paramount condition for a firm's success abroad. Marketing strategies that work in one country often fail when directly applied in other countries. In many cases, marketers must redesign packages and modify products and advertising messages to suit the tastes and preferences of different cultures.

Changing social values have led to the consumerism movement which is a social force within the environment designed to aid and protect buyers by exerting legal, moral and economic pressures on business. Consumerism also advocates the rights of the consumers such as:

1. The right to choose freely – consumers should be able to choose among a range of goods and services
2. The right to be informed – consumers should have access to enough education and product information to make responsible buying decisions
3. The right to be heard – consumers should be able to express legitimate complaints to appropriate parties – be it manufacturers, sellers, consumer assistance groups and consumer courts.
4. The right to be safe – consumers should feel assured that the goods and services they purchase will not cause injuries in normal use. Product designs should allow average consumers to use them safely.

The social-cultural environment for marketing decisions at home and abroad is expanding in scope and importance. Today no marketer can initiate a strategic decision without taking into account the society's norms, values, culture and demographics. Marketers must understand how these variables affect their decisions. The constant influx of social input requires that marketing managers focus on addressing these questions instead of concerning themselves only with the standard marketing tools.

Activity 1.4.1

Choose an industry. Search from recent business news to look for examples of influences of competitors, economy, politics, law, technology, society and culture on marketing decision making.

Competitive Environment

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Economic Environment

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Political-Legal Environment

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Technological Environment

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Social-Cultural Environment

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Case study 1.4.1 EuroDisney – managing the marketing environmental challenges

Michael Eisner joined the Walt Disney company as the chairman of the board in 1984, after his successes at the ABC television network and Paramount. The same year, Tokyo Disney was completing its first year of operations after five years of planning and construction, when the Walt Disney Co. entered into an agreement with Oriental Land Company in Japan. More than 10 million people visited the park that year, spending $355 million. This was $155 million more than had been expected and was partially attributed to the average expenditure per visitor being $35, rather than the estimated $21. The timing of the Tokyo Disneyland opening coincided with a rise in income and leisure time among the Japanese. Tokyo Disneyland thus became quickly profitable. Growth continued, and by 1990 more than 14 million people visited the park, a figure slightly higher than the attendance at Disneyland in California and about half the attendance at Walt Disney World in Florida. Though, Disney was not a financial partner in the Tokyo venture, it was reaping the profit from its franchise (10% royalty from admission and 5% from merchandise and food sales).

The Tokyo park was in some ways a paradox. Tokyo Disneyland is nearly a replica of the two parks in US. Signs are in English, and most food is American style. The management of the Oriental Land Company demanded this because they wanted visitors to feel they were getting the real thing and because they had noted that such franchises as McDonald's have enormous success in Japan, as Japanese youth embraced American-style culture. Yet, a few changes were necessary, such as the addition of a Japanese restaurant. The product was readily accepted by the Japanese, an acceptance attributed by some to the enthusiastic assimilation of the Japanese to Western ways. The success of the Tokyo Disneyland led the company to consider expansion into Europe.

In 1984, a few months after his arrival at Disney, Eisner decided to create a Disney resort in Europe. In 1985, Disney announced that it had narrowed its locational choice to two countries, Spain and France. The park was scheduled to open in 1992 at either location. Since the park was estimated to provide about 40,000 permanent jobs and would draw large numbers of tourists, the two countries openly courted Disney. If Disney opted for a Spanish location, the park would have to be like the ones in the U.S, where the visitors are outside for almost all amusements. However, Disney had learnt from the Tokyo experience that the cold weather does not necessarily impede attendance. But the colder climate in Paris area would require more indoor shows. Furthermore, France would require more focus on technology and historical themes.

After three years of discussions, the search culminated with the selection of a site at the heart of Europe: Marna-la-Vallee, France. Euro Disney was officially born. The total investment by 1992 was estimated at between $2.4 to 3 billion. Disney opted for a 49% stake. France was in full economic crisis and Disney was taking advantage of this crisis. In a real estate coup, the French Government sold Disney some very expensive land at a bargain price and. In spite of the economic benefits the park was expected to bring, many people in France feared that the Park would be one more step toward the replacement of the French culture with that of the US. Critics called EuroDisney "a cultural Chernobyl".

Disney headed off the criticism by explaining in the French press that Walt Disney was of French Huguenot descent, with an original name of D'Isigny rather than Disney. Disney also agreed to make French the first language in the park, although relying heavily on visual symbols. Disney would build an attraction, Discovery Land, based on the science fiction of France's Jules Verne; and a movie theater featuring European history. Many concessions were made to soothe the French resistance. Disney admitted that it may have to alter its no-alcohol policy for this park, but it didn't. The park also emphasized that Pinocchio was Italian, Cinderalla was French and Peter Pan flew in London.

The marketing campaign began in October, 1991. The sales division began ambitious programs to inspire European families to mark the Euro Disney resort on their vacation agendas. The Sales division established a strong presence in all the major markets through special partnerships with leading companies in the travel industry. On April 12, 1992, Euro Disney hosted the biggest event in Disney history, the official opening of the Euro Disney resort. Looking at the future, Euro Disney had two primary objectives : to achieve profitability as quickly as possible and to better integrate Euro Disney into its European environment while reinforcing its greatest asset – Disney heritage. Disney announced plans to add a second theme park, the Disney MGM Studios-Europe and a water park. Disney was so optimistic that it was negotiating the possibility of creation of creating a third theme park at the beginning of the new millennium.

The Park admission fee cost US $45 for an adult and $30 for a child under 11, a price about 50% higher than the corresponding Disney World price. The US Disney park's formula in terms of inelasticity of demand did not apply and the demand fell sharply (a 15% decrease in attendance for a 10% increase in price.) Attendance figures were kept secret, but this attitude reinforced the idea that even in terms of attendance, the objectives were not reached. The financial results were not as strong as hoped and the very difficult economic environment contributed to not meeting the ambitious objectives.

As Eisner started an interview with Larry King, he quipped, "Everybody is giving us 42 reasons why we've made a mistake, because we have financial problems… We are not either responsible for the real estate crisis nor the high French interest rate, which are dreadfully penalizing us. Not a single manager, whomever he be, could manage so many uncontrollable forces."

Questions: Describe the importance of environmental scanning for Disney in its EuroDisney venture. How does the marketing environment affect Disney's marketing? Single out each of these environmental variables and suggest ways for Disney to manage them.

Unit – I

Lesson 1.5
Buyer Behaviour

Objectives

In this lesson, we will introduce you to the process through which the ultimate buyer makes purchase decisions. After you work out this lesson, you should be able to:

- Identify what stimulates a consumer to consider buying
- Describe the buyer's decision making process and the several factors which influence this decision
- Understand the response of the buyer to the marketing and other stimuli

In this lesson, we will discuss the following:

- What is buyer behaviour?
- Models of consumer/buyer behaviour
- Determinants of consumer behaviour
- The consumer decision process
- Marketing implications of consumer behaviour

Introduction

Why do people buy one product and not another? Answering this question is the basic task of every marketer. The answer directly affects every aspect of marketing strategy, from product development to pricing and promotion. Discovering that answer requires an understanding of buyer behaviour, the process by which consumers and business-to-business buyers make purchase decisions. Buyer behaviour is a broad term that covers both individual consumers who buy goods and services for their own use and organizational buyers who purchase business products. A variety of influences affect both individuals buying products for themselves and professional buyers purchasing products for their firms. This lesson focuses predominantly on individual consumer behaviour.

What is Buyer Behaviour?

Consumer behaviour is the process through which the ultimate buyer makes purchase decisions. Here is a sample of popular definitions for consumer behaviour:

> '… the study of the buying units and the exchange processes involved in acquiring, consuming, and disposing of goods, services, experiences, and ideas' (Mowen)
>
> '… the decision process and physical activity individuals engage in when evaluating, acquiring, using or disposing of goods and services' (Loudon and Della Bitta)
>
> '… reflects the totality of consumers' decisions with respect to the acquisition, usage and disposition of goods, services, time and ideas by (human) decision making units (over time)' (Jacob Jacoby)

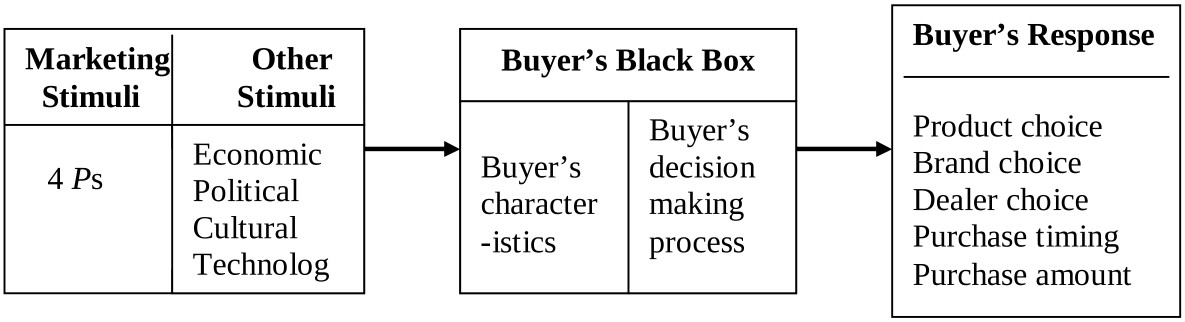
The definition by Jacoby can be further illustrated. The totality of consumers' decisions include whether to buy or not, what to buy, why to buy, how to buy, when to buy, where to buy and also how much/ how often/ how long. The idea of consumption not only includes purchasing and using, but also disposing. The marketer's offering can mean many things – be it product, service, time, ideas, people and so on. The term decision making units obviously refers to people involved. In a typical purchase, many people may be involved and they play different roles such as information gatherer, influencer, decider, purchaser and user. In a consumer buying context, it may mean a family or group influence where as in the industrial buying context, it means a cross-functional team with each member of the team performing a particular role in the buying decision. The word 'time' could mean different units of time like hours, days, weeks, months and years.

Models of Consumer/Buyer Behaviour

Consumer behaviour is a dynamic, multi-disciplinary process. The study of consumer behaviour builds upon an understanding of human behaviour in general. In an effort to understand why and how consumers make buying decisions, marketers borrow extensively from the sciences of psychology and sociology. The work of psychologist Kurt Lewin provides a useful classification scheme for influences on buying behaviour. Lewin's proposition is $B = f(P,E)$ which means that behaviour (B) is a function (f) of the interactions of personal influences (P) and pressures exerted by outside environmental forces (E). This statement is rewritten to apply to consumer behaviour as $B = f(I,P)$ (i.e.)

consumer behaviour (*B*) is a function (*f*) of the interactions of interpersonal influences (*I*) such as culture, role models, friends and family – and personal factors (*P*) such as attitudes, learning and perception. Therefore inputs from others and an individual’s psychological makeup both affect a consumer’s purchasing behaviour. This model is further explained in the following sections of this lesson. There are many other models of consumer behaviour. The most generic model of consumer behaviour suggests a stimulus-response pattern of understanding the consumer’s behaviour (Figure 1.5.1). The stimulus can be marketing stimuli (which can be manipulated by the marketer) and other external stimuli (like the economy, culture, technology and so on). The response includes the decision to buy, product choice, dealer choice and choices regarding time, quantity, etc. The consumer is at the center of this model. The stimulus is applied to this consumer who in turn comes up with a response. The consumer has his/her own characteristics and a multi-staged decision-making process. There are also several influencing factors acting upon the consumer. The influencing factors may include personal and interpersonal influences.

Figure 1.5.1 A generic model of consumer behaviour


Marketing Stimuli
Other Stimuli
4 *P*s
Economic
Political
Cultural
Technolog
Buyer’s Black Box
Buyer’s character -istics
Buyer’s decision making process
Buyer’s Response
Product choice
Brand choice
Dealer choice
Purchase timing
Purchase amount

Determinants of Consumer Behaviour

Consumers don’t make purchase decisions in a vacuum; rather, they respond to a number of external, interpersonal influences and internal, personal factors.

Consumer often decide to buy goods and services based on what they believe others expect of them. They may want to project positive images to peers or satisfy the unspoken desires of family members. Marketers recognize three broad categories of interpersonal influences on consumer behaviour: cultural influences, group influences and family influences.

> Cultural influences: Culture can be defined as the values, beliefs, preferences and tastes handed down from one generation to the next. Culture is the broadest environmental determinant of consumer behaviour. Therefore, marketers need to understand its role in customer decision making. They must also monitor trends to spot changes in cultural values. Marketing strategies and business practices that work in one country may be offensive or ineffective elsewhere because of cultural variations. Hence cultural differences are particularly important and complex to understand for international marketers. Cultures are not homogeneous entities with universal values. Each culture includes numerous subcultures – groups with their own distinct modes of behaviour.
>
> Group (Social) influences: Every consumer belongs to a number of social groups. Group membership influences an individual’s purchase decisions and behaviour in both overt and subtle ways. The influences may be informational and/or normative. Every group establishes certain norms of behaviour. Group members are expected to comply with these norms. Difference in group status and roles can also affect buying behaviour. The surprising impact of groups and group norms on individual behaviour has been called the Asch phenomenon because it was first documented by psychologist S.E.Asch. Discussions of the Asch phenomenon raises the subject of reference groups – groups whose value structures and standards influence a person’s behaviour. Consumers usually try to coordinate their purchase behaviour with their perceptions of the values of their reference groups. Children are especially vulnerable to the influence of reference groups. They often base their buying decisions on outside forces – what is popular with their friends, what is fashionable and trendy, what is popular, what are their heroes and role models (usually, celebrities) using. In nearly every reference group, a few members act as opinion leaders. They are the trendsetters who are likely to purchase new products before others in the group and they share their experiences and opinions via word of mouth. Other members’ purchase decisions are affected by the reports of the opinion leaders. Closely related to reference groups is the concept of social class. A social class is an identifiable group of individuals who tend to share similar values and behavior patterns different from those of other classes. These values and behaviour patterns affect the purchase decisions.
>
> Family influences: The family group is perhaps the most important determinant of consumer behaviour because of the close, continuing interactions among family members. Like other groups, each family typically has norms of expected behaviour and different roles and status relationships for its members. The traditional family structure consists of a husband and wife. Although these and other members can play a variety of roles in household decision making,

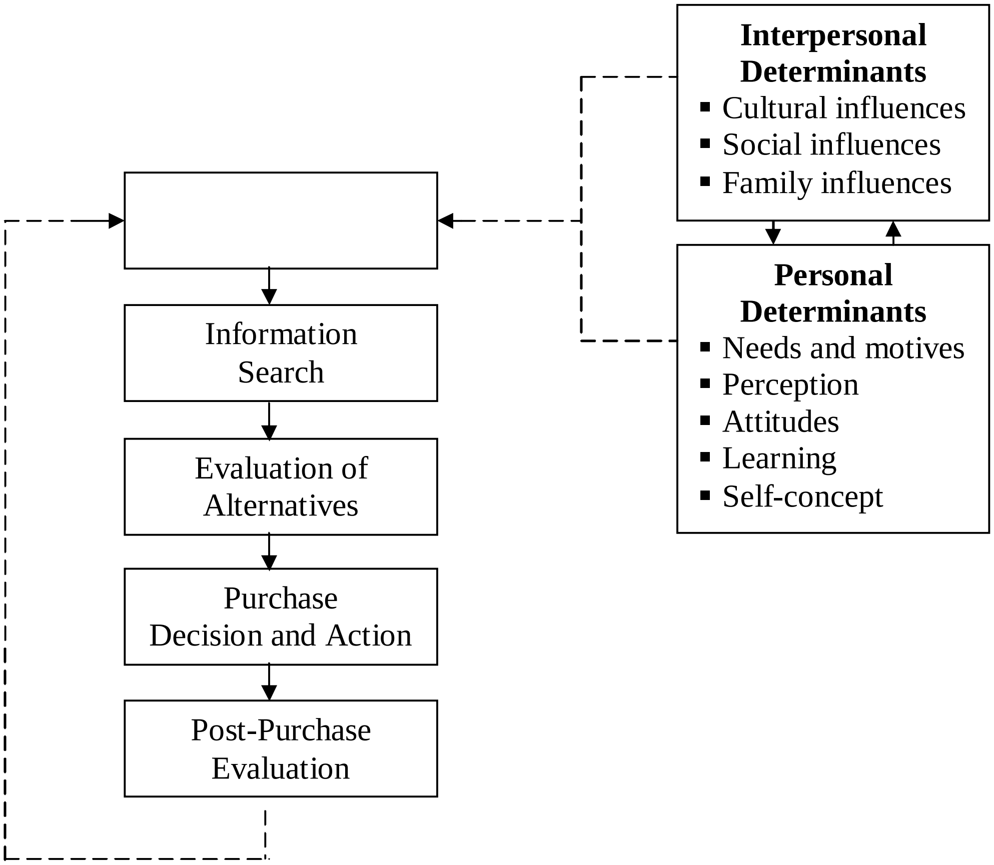
> marketers have created four categories to describe the role of each spouse: (1) Autonomic, in which the partners independently make equal numbers of decisions (e.g. personal-care items) (2) Husband-dominant, in which the husband makes most of the decisions (e.g. insurance) (3) Wife-dominant, in which the wife makes most of the decisions (e.g. children's clothing) and (4) Syncratic in which both partners jointly make most decisions (e.g. vacation).

Consumer behaviour is affected by many internal, personal factors, as well as interpersonal ones. Each individual brings unique needs, motives, perceptions, attitudes, learning and self-concepts to buying decisions.

> Needs and motives: Individual purchase behaviour is driven by the motivation to fill a need. A need is an imbalance between the consumer's actual and desired states. Someone who recognizes or feels a significant or urgent need then seeks to correct the imbalance. Marketers attempt to arouse this sense of urgency by making a need 'felt' and then influence consumers' motivation to satisfy their needs by purchasing specific products. Motives are inner states that direct a person toward the goal of satisfying a felt need. The individual takes action to reduce the state of tension and return to a condition of equilibrium.
>
> Perceptions: Perception is the meaning that a person attributes to incoming stimuli gathered through the five senses – sight, hearing, touch, taste and smell. Certainly a buyer's behaviour is influenced by his or her perceptions of a good or service.
>
> Attitudes: Perception of incoming stimuli is greatly affected by attitudes. In fact, the decision to purchase a product is strongly based on currently held attitudes about the product brand, store or salesperson. Attitudes are a person's enduring favourable or unfavourable evaluations, emotional feelings or action tendencies toward some object. Because favourable attitudes likely affect brand preferences, marketers are interested in determining consumer attitudes toward their products.
>
> Learning: In a marketing context, refers to immediate or expected changes in consumer behaviour as a result of experience (that of self or others'). Consumer learning is the process by which individuals acquire the purchase and consumption knowledge and experience that they apply to future related behaviour. Marketers are interested in understanding how consumers learn so that they can influence consumers' learning and subsequently, their buying behaviour.
>
> Self-concept: The consumer's self-concept – a person's multifaceted picture of himself or herself – plays an important role in consumer behaviour. The concept of self emerges from an interaction of many of the influences – both personal and interpersonal – that affect buying behaviour.

The Consumer Decision Process

Figure 1.5.2 An integrated model of the consumer decision process


Interpersonal Determinants
▪ Cultural influences
▪ Social influences
▪ Family influences
Personal Determinants
▪ Needs and motives
▪ Perception
▪ Attitudes
▪ Learning
▪ Self-concept
Information Search
Evaluation of Alternatives
Purchase Decision and Action
Post-Purchase Evaluation

Consumers complete a step-by-step process to make purchasing decisions. The length of time and the amount of effort they devote to a particular purchasing decision depends on the importance of the desired good or service to the consumer.

Purchases with high levels of potential social or economic consequences are said to be high-involvement purchase decisions. Routine purchases that pose little risk to the consumer are low-involvement decisions. Consumer generally invest more time and effort to purchase decisions for high-involvement products than to those for low-involvement products. For example, a car buyer will probably compare prices, spend time visiting dealer showrooms, read auto reviews and ask for advice from friends before making the final decision. Few buyers invest that much effort in choosing between two brands of candies. They will still go through the steps of the consumer decision process but on a more compressed scale. Purchase decisions can be thought-based (cognitive) or feeling-based (emotive). While it is true that both cognition and emotion will be present in every purchase decision, either one of them will dominate the decision. As a result, we can construct a grid as follows to analyze different consumer purchase decisions.

Figure 1.5.3 Classification of consumer purchase decisions

	Thought-based	**Feeling-based**
High effort	Example: Investment decisions	Example: Jewellery
Low effort	Example: Home maintenance products	Example: Snacks

Figure 1.5.2 shows the five steps in the consumer decision process. First, the consumer recognizes a problem or an unmet need. Then he/she searches for goods or services that will fill that need and evaluates the alternatives before making a purchase decision (and the actual purchase). After completing the purchase, the consumer evaluates whether he/she has made the right choice. Much of marketing involves steering the consumers through the decision process in the direction of a specific item. Consumers apply the decision process in solving problems and taking advantage of opportunities. Such decisions permit them to correct differences between their actual and desired states. Feedback from each decision serves as additional learning experience to help guide subsequent decisions.

During the first stage in the consumer decision making process, the consumer becomes aware of the discrepancy between the actual state (‘where we are now’ and the ideal state (‘where we want to be’). Problem recognition motivates the individual to achieve the desired state of affairs. A marketer can stimulate problem recognition either by creating a new ideal state or by creating dissatisfaction with the actual state. In the second stage, the consumer gathers information related to his/her attainment of a desired state of affairs. This search identifies alternative means of problem solution. High-involvement purchases may elicit extensive information searches, while low-involvement purchases require little search activity. The search may cover internal or external sources of information. During internal search, stored information, feelings and experiences relevant to the problem-solving situation are recalled from the consumer’s memory. An external search gathers information from outside sources, which may include family members, associates, store displays, sales representatives, advertisements and product reviews. The external search may be a general on-going search or a specific pre-purchase search. The search identifies alternative brands for consideration and possible purchase. The number of brands that a consumer actually considers in making a purchase decision is known as the evoked set. Marketers try to influence consumer decisions during the search process by providing persuasive information about their goods or services in a format useful to consumers.

The third step in the consumer decision making process is to evaluate the evoked set of options identified during the search step. The outcome of the evaluation stage is the choice of a brand or product in the evoked set or possibly a decision to renew the search for additional alternatives, should all those identified during the initial search prove unsatisfactory. To complete this analysis, the consumers develop a set of evaluative criteria to guide the selection. These criteria can either be objective facts or subjective impressions. Marketers can attempt to influence the outcome from this stage in many ways. First, they can try to educate consumers about attributes that they view as important in evaluating a particular class of goods. They can also identify which evaluative criteria are important to an individual and attempt to show why a specific brand fulfills those criteria. They can try to induce a customer to expand his/her evoked set to include the product they are marketing.

The search and alternative evaluation stages of the decision process result in the eventual purchase decision and the act of making the purchase. At this stage, the consumer has evaluated each alternative in the evoked set based on his/her personal set of evaluative criteria and narrowed the alternatives down to one. Marketers can smooth the purchase decision and action by helping consumers through financing, delivery, installation and so on.

The purchase act produces one of two results. The buyer feels either satisfaction at the removal of the discrepancy between the actual and the ideal states or dissatisfaction with the purchase. Consumers are generally satisfied if purchases meet their expections.

Sometimes, however, consumers experience some post purchase anxieties, called cognitive dissonance. It is a perception that one has not made the right decision. The consumer attempts to reduce this dissonance by searching for additional information that confirms his/her choice. The marketer can help by providing reassuring information to the buyer and also by positive marketing communications.

Marketing Implications of Consumer Behaviour

Marketers study consumer behaviour because it has serious marketing implications – be it in marketing strategy (as defined by market segmentation, targeting and positioning) formulation or in designing the marketing mix (defined by the 4 Ps of marketing, viz., product, price, place and promotion). The following is a list of questions related to marketing strategy and marketing mix. The answers obviously arise from insights and findings from the study of consumer behaviour. Consider this.

Developing a Customer-Oriented Strategy

Market segmentation
How Is the Market Segmented?
How Profitable Is Each Segment?
What Are the Characteristics of Consumers in Each Segment?
Are Customers Satisfied with Existing Offerings?
Selecting the target market

Positioning

How Are Competitive Offerings Positioned?
How Should Our Offerings Be Positioned?
Should Our Offerings Be Repositioned?

Developing Products or Services

What Ideas Do Consumers Have for New Products?
What Attributes Can Be Added to or Changed in an Existing Offering?
What Should Our Offering Be Called?
What Should Our Package and Logo Look Like?
What About Guarantees?

Making Promotion (Marketing Communications) Decisions

What Are Our Advertising Objectives?
What Should Our Advertising Look Like?

Where Should Advertising Be Placed?
When Should We Advertise?
Has Our Advertising Been Effective
What About Sales Promotion Objectives and Tactics?
When Should Sales Promotions Happen?
Have Our Sales Promotions Been Effective?
How Many Salespeople Are Needed to Serve Customers?
How Can Salespeople Best Serve Customers?

Making Pricing Decisions

What Price Should Be Charged?
How Sensitive Are Consumers to Price and Prices Changes?
When Should Certain
Price Tactics Be Used?

Making Distribution Decisions

Where Are Target Consumers Likely to Shop?
How Should Stores Be Designed?

Here are some specific real-life examples to emphasize the marketing implications that arise from the study of consumer behaviour. Product positioning and competition: Remember the classic ad campaign for CoffeeBite. It talks about the positioning identities - What am I and Who am I. The Axe Deo campaigns strongly bring out the positioning identity of ‘For whom am I?’. Also the positioning of different supermarkets like FoodWorld, Nilgris, ApnaBazar and Subiksha answer the question ‘For whom am I?’. While designing the competitive marketing strategy, one question that bothers marketers is ‘Who am I competing with?’. For instance, is Xerox competing with other photocopier makers or computer printer makers or printers? With a positioning as ‘the Document company’ it protects itself from marketing myopia and positions itself to take on competition even from the substitute products. If Style-Spa, the high-end home furniture retailer considers itself as a home expressions company, it invites competition from antique furniture shops. Similarly, Archies, a social expressions company selling cards and gifts, in reality competes with florists! These insights emerge from an understanding of the consumer needs and motives which is central to consumer behaviour.

Marketers are concerned about how consumers perceive their products. For example, brands like Strepsil (with all its colours and flavours), Crocin (with interesting mass media campaigns) can possible confuse the consumers – are they pharmaceutical products? self-help relievers? Are they specialty or common-place products. Consumer perception determines the evoked set for the problem. No brand wants to be categorized with wrong competition in the evoked set! Itchguard represents a classic case of the creation of a new product category. The consumer need was always there until this brand arrived and addressed this need exquisitely and exclusively. In many markets, orange juice enjoys different perceptions – as a breakfast drink, as a refresher drink, as a health drink and as a health recovery drink. Same product but different consumer perceptions! This understanding is vital for a brand like Tropicana which sells orange juice in different markets. Also the use of celebrity endorsements (as reference groups, opinion leaders) is attributed to its role in consumer behaviour. The use of cricketers like Sachin Tendulkar and Bollywood stars like Aishwarya Rai in advertisements attempts to shape and influence consumer behaviour in favour of the brands they endorse. Another classic example is the 'Got milk?' campaign featuring several celebrities in support of milk as a healthy drink and endorsing its consumption. Check out for more about this campaign at www.whymilk.com. In Eastern cultures, group values are stressed over the individual's. So the appeal to normative beliefs takes on greater significance while designing marketing communications in the Eastern cultures.

A study of consumer learning reveals how consumers generalize related marketing stimuli. Based on this, there are several marketing applications – product-line extension (Pepsi Lemon), product-form extension (Pepsi can), product-category extension (Aquafina), Family branding (Nestle's Maggi, HP Pavillion), Licensing (Tommy, CK, Disney – in several product categories to several merchandisers), usage situation generalization (an all-hair shampoo).

The study of consumer behaviour is a very exciting field of marketing. Marketing begins and ends with consumers. As a result, the study of consumer behaviour permeates all of marketing.

Case Study 1.5.1 Marketing Beyond the Veil

Many marketers think that marketing to Saudi Arabian women is a very difficult task. Women in Saudi remain behind the *purdah* and it is difficult to *talk* to them.

Saudi Arabia is one of the largest markets in west Asia and is a homogenous society. There exists a wrong notion among some marketers that Saudi women are passive consumers. Many Saudi women are often highly educated. About 3,80,000 women work in Saudi Arabia and the number of female students in the colleges is set to rise about 1,75,000 in the next two years. Most women work in the traditional fields of health and education. Some are even employed in retailing, designing, publishing and manufacturing.

They are exploring ways to sell products to Saudi women since Saudi Arabia is considered a young market. Shopping malls are an utter flop as women find these out-of-town malls inconvenient. MNCs have realized that Saudi women are brand conscious and make the buying decision for household items. MNCs have been searching intensively for women who can act as intermediaries between the company and the clients and those who have links with colleges, women groups, etc.

Marketers should now stop underestimating the sophistication of Saudi women as consumers. It is time they recognized that they are the emerging economic force. A women emerging out of a car fully covered by the *purdah*, may hold a degree in finance or law or medicine and so on, and she may be a potential consumer given her educational background and culture.

Questions: List out the differences between Consumer Behaviour of Women in a *closed culture* (as described by this case) in Saudi Arabia and in a *open culture* (say, in Western Eupore). Highlight the cultural implications for a Woman consumer and also for a marketer in the given context. Think of creative applications of ‘reference groups’ to market to the Saudi Arabian Women, say for a personal care product.

Case study 1.5.2 That CSR (Corporate Social Responsibility) thing!
[Source: Business Today, May 8, 2005]

It shouldn’t surprise anyone that Indian companies have just discovered the marketing pay-off of their corporate social responsibility (CSR) initiatives. They could get by with focusing on real or perceived product attributes, and with profit-mindedness being considered a coarse sentiment, any CSR programme they launched was far removed from their core businesses, brands, even consumers.

There has been a spate of corporate CSR initiatives over the past few years. Companies have been quick to respond to crises (such as the Gujarat earthquake or the Tsunami that hit the southern part of the country) or shown inherent goodness in plugging gaps in the government's efforts to provide healthcare and education to all – in a country as vast as India, there will always be gaps – but there has been little effort to link such work to things such as marketing, even corporate strategies. Most CSR activities are, at best, charity, not very different from discrete acts of philanthropy and, at worst, a mere humane façade of a for-profit-only capitalist system.

This is why recent advertising campaigns by the country's two largest fast moving consumer goods (FMCG) companies, Hindustan Lever Limited (HLL) and ITC are significant. The first, a campaign for Surf Excel Quick Wash with the tagline *Do bucket paani ab rozana hai bachnai* (I will save two buckets of water a day), has struck a chord in a country where the shortage of water is an endemic phenomenon. "We decided it would be of immense benefit to a household if a technology could be developed that would reduce the water consumed in the washing of clothes and the amount of effort required while rinsing while delivering superlative cleanliness", says an HLL spokesperson. Surf's sales, say sources in the market, have gone up by as much as 15% since the advertisement, starring actress-turned-social-activist and former Member of Parliament, Shabana Azmi, went national (the company had tested the strategy in water-starved Tamil Nadu last year with another actress-turned-social-activist Revathy Menon).

Then, there is ITC's *Working for you, working for India* campaign, one strand of which focuses on the company's e-choupal initiative, an effort that seeks to enhance rural incomes, then, sell a variety of products and services to rural customers (apart from sourcing agricultural produce from them). The tagline itself smacks of old-style image-led CSR activity, but given what the e-choupal does, it is actually an attempt to build and position the company's brand around the idea of doing something for the country.

In some ways, ITC's e-choupal is a far stronger example of a CSR-brand linkage than the Surf Excel campaign. It is a programme that is obviously advantageous to the company, yet it is accomplished by enough socially relevant goodies to make it look the way a government programme targeted at rural development ideally should. HLL, coincidentally, has an initiative that fits the bill, its Project Shakthi that uses Women’s self help groups in rural areas to further its reach. “The problem with old-style CSR was that the benefactors were not in control of what they would get”, says Vivek Vaidya, a brand consultant. With brand or corporate strategy driven CSR, they are.

Questions: Explain the success of *Do bucket paani ab rozana hai bachnai* (I will save two buckets of water a day) campaign for Surf Excel. What consumer behaviour insights can you draw from this case. Identify the personal and interpersonal factors that affect consumer behaviour for the product/service described in the case.

Unit – I

Lesson 1.6
Market Segmentation, Targeting and Positioning

Objectives

In this lesson, we will introduce you to the activities, viz., segmentation, targeting and positioning, that are collectively referred to as marketing strategy. After you work out this lesson, you should be able to:

- Segment the markets based on several segmentation variables
- Target a segment by identifying the fit between segment profitability and organizational capability
- Position your product/service so that it occupies a distinct and valued place in the target customers' minds

In this lesson, we will discuss the following:

- The logic of segmentation
- Segmentation analysis
- Segmentation variables for consumer markets and industrial markets
- Targeting approaches
- Positioning identities
- Differentiation across the consumption chain

Introduction

Development of a successful marketing strategy begins with an understanding of the market for the good or service. A market is composed of people or institutions with need, sufficient purchasing power and willingness to buy. The market place is heterogeneous with differing wants and varying purchase power. The heterogeneous marketplace can be divided into many homogeneous customer segments along several segmentation variable. The division of the total market into smaller relatively homogeneous groups is called market segmentation. Products seldom succeed by appealing to everybody. The reasons are simple: not every customer is profitable nor worth retaining, not every product appeals to every customer. Hence the organizations look for a fit between their competencies and the segments' profitability. The identified segments are then targeted with clear marketing communications. Such communications are referred to as positioning the product or service in the mind of the customer so as to occupy a unique place. This involves identifying different points of differentiation and formulating a unique selling proposition (USP). In today's marketplace, differentiation holds the key to marketing success. This lesson is about marketing strategy formulation which consists of market segmentation, targeting and positioning.

The logic of Segmentation

The concept of market segmentation has helped marketing decision making since the evolution of marketing. The goal of market segmentation is to partition the total market for a product or service into smaller groups of customer segments based on their characteristics, their potential as customers for the specific product or service in question and their differential reactions to marketing programs. Because segmentation seeks to isolate significant differences among groups of individuals in the market, it can aid marketing decision making in at least four ways:

1. Segmentation helps the marketer by identifying groups of customers to whom he could more effectively 'target' marketing efforts for the product or service
2. Segmentation helps the marketer avoid 'trial-and-error' methods of strategy formulation by providing an understanding of these customers upon which he can tailor the strategy
3. In helping the marketer to address and satisfy customer needs more effectively, segmentation aids in the implementation of the marketing concept
4. On-going customer analysis and market segmentation provides important data on which long-range planning (for market growth or product development) can be based.

Although it is a very useful technique, segmentation is not appropriate in every marketing situation. If, for instance, a marketer has evidence that all customers within a market have similar needs to be fulfilled by the product or service in question (i.e. an undifferentiated market), one 'mass' marketing strategy would probably be appropriate for the entire market. However, in today's market environment, it is unlikely that one would find either an entirely homogeneous market,

Activity 1.6.1

Consider the toothpaste market. Nearly everyone uses it. Yet, the toothpaste manufacturers have found that consumers have different ideas about what they would like the product to do. Prepare a list of what consumers want their toothpastes to do to them.

1.
2.
3.
4.
5.
6.
7.
8.

Criteria for Segmentation

If segmentation has to be useful in marketing decision making, then it must possess the following characteristics:

1. Segments must be internally homogeneous --- consumers within the segment will be more similar to each other in characteristics and behaviour than they are to consumers in other segments.
2. Segments must be identifiable --- individuals can be ‘placed’ within or outside each segment based on a measurable and meaningful factor
3. Segments must be accessible --- can be reached by advertising media as well as distribution channels. Only then, the segments can be acted upon.
4. Segments must have an effective demand --- the segment consists of a large group of consumers and they have the necessary disposable income and ability to purchase the good or service.

Segmentation Analysis

Here is a list of few general steps, referred to as segmentation analysis, that will be most often followed after the decision to employ market segmentation has been made. Examples of questions to be answered during each step are also given.

Step-1 Define the purpose and scope of the segmentation

- What are our Marketing Objectives?
- Are we looking for new segments or determining how to better satisfy existing ones?
- Will we use existing data or invest time and money in new research?
- What level of detail will be needed in the segmentation analysis?

Step-2 Analyze total Market Data

- What is the character of the total market? (e.g. size)
- Are there basic differences between users and non-users of the product class?

- Are there any factors which clearly distinguish users from non-users or users of different brands?
- What is our competitive position in the market now?
-

Step-3 Develop segment profiles

- What factor seems to differentiate groups of consumers most clearly?
- Are the profiles of each segment internally consistent?
-

Step-4 Evaluate segmentation

- What are the major similarities and differences among segments?
- Should the number of segments described be reduced or increased?
- How sensitive is this segmentation of the market to growth?
-

Step-5 Select target segment(s)

- Which segment(s) represent our best market opportunity?
- What further details do we know about the target segment's characteristics and market behaviour?
- If complete data on market behaviour for the target segment are not available, can we make reasonable assumptions?
- Are we alone in competing for this target segment?
-

Step-6 Designing the marketing strategy for the target segment

- What type of product do these consumers want?
- What kinds of price, promotion or distribution tactics will best suit their needs?
- Would other segments react positively to a similar strategy? (if so, the segments should probably be merged)
-

Step-7 Reappraisal of segmentation

- Do we have the resources to carry out this strategy?
- If we wish to broaden or change our target definition in the future, how flexible is the strategy?
- If we wish to change some element of the strategy in the future, how would that change probably influence the target segment?
- Does the target segment/strategic plan meet our objective? Does it fit our corporate strengths?

Segmenting the Consumer Markets

Consumer markets are those where the products are purchased by ultimate consumers for personal use. Industrial markets are those where the goods and services are purchased for use either directly or indirectly in the production of other goods and services for resale. Market segmentation of these markets use different variables. The consumer market segmentation variables appear to fall into two broad classes: consumers' background characteristics and consumers' market history. The following tables illustrate the most important factors and variables that have been found useful for market segmentation.

Table 1.6.1 Segmentation using consumer background characteristics

Segmentation variable	**Some examples of variables Measured**	**Comments**
Geography	▪ Region of product distribution ▪ Cultural differences ▪ Mobility of consumers	Geographic segmentation is one of the oldest and most basic of market descriptors. In most cases, it alone is note sufficient for a meaningful consumer segmentation
Demographic	▪ Age ▪ Sex ▪ Income ▪ Educational level ▪ Social status	Also basic and included as a variable in most segmentation analyses. Demographic profiles of segments are important especially when making later advertising media decisions
Psychographic	▪ Personality traits ▪ Perceptual styles ▪ Attitudes ▪ Reference groups ▪ Social roles	Psychographic variables are more useful because there is often no direct link between demographic and market behaviour variables. These consumer profiles are often tied more directly to purchase motivation and product usage
General life-style	▪ Correlation of demographic and psychographic variables ▪ Activities and interests	Provides a rich, multi-dimensional profile of consumers that integrates individual variables into clearer pattern that describes the consumer's routines and general 'way of life'

Table 1.6.2 Segmentation using consumers' market history

Segmentation variable	Some examples of variables measured	Comments
Product usage	▪ Frequency of brand/product use ▪ Brand loyalty ▪ Attitudes toward product	Segmenting the market into heavy, medium, light and non-users gives good understanding of present situation in market
Product benefit	▪ Expectations of product performance	Very useful if product can be positioned in a number of ways. Primary use of this

	▪ Needs product must fill ▪ Perceptions of brands ▪ Satisfaction (dissatisfaction measures)	variable segments the market into groups that look for different product benefits
Decision-process	▪ Shopping patterns ▪ Media-use patterns ▪ Product information searches ▪ Sensitivities to price, to promotion and to place (channel)	Use of this variable segments the market into price/non-price sensitive, shoppers/impulse buyers and other segments which characterize the market behaviour of each group. Must be used in conjunction with analysis of consumer characteristics to allow identification of the individuals involved

Activity 1.6.2

Refer to the activity 1.6.1. From what you had noted down as the 'wants' of toothpaste consumers, match each of those wants with the segmentation variables listed below

1. Consumer background characteristics
    1.1 Geography -
    1.2 Demographic -
    1.3 Psychographic -
    1.4 General life-style -
2. Consumers' market history
    2.1 Product usage -
    2.2 Product benefit -
    2.3 Decision-process -

Segmenting the Industrial Markets

Industrial marketing needs to consider two important sets of characteristics of the business buyers: (1) the characteristics of the buyer as a consuming organization and (2) the behavioural characteristics of the buyer. The first set includes such factors as the type of the organization, the size, the product requirements, the end use of the product, the organization capabilities and so on. The second set includes factors like the buying decision making process and considers the fact that it is in effect people and the organization, who take the decision. These characteristics have led to a two-stage approach to industrial market segmentation starting with a macro segmentation and then going into a micro segmentation. Between the macro and micro bases of industrial market segmentation, there lie some useful bases of segmentation, as suggested by Shapiro and Bonoma in the Nested approach to segmenting the industrial markets. These intermediate bases of segmentation, viz., demographics, operating variables, purchasing approaches, situational factors and personal characteristics, are explained in Table 1.6.3. The table lists major questions that business marketers should ask in determining which customers they want to serve. By targeting these segments instead of the whole market, companies have a much better chance to deliver value to customers and to receive maximum rewards for close attention to their needs.

Table 1.6.3 Major Segmentation variables for Industrial Markets

Segmentation variable	Examples of variables measured	Comments
Demographics	▪ Industry ▪ Company size ▪ Location	Which industries that buy this product should we focus us? What size companies should we focus on? What geographical areas should we focus on?
Operating variables	▪ Technology ▪ User/non-user status ▪ Customer capabilities	What customer technologies should we focus on? Should we focus on heavy, medium or light users or non-users? Should we focus on customers needing many or few services?
Purchasing approaches	▪ Organization ▪ Power structure ▪ Nature of existing relationship ▪ General purchase policies ▪ Purchasing criteria	Should we focus on companies with centralized or decentralized purchasing? Should we focus on engineering or finance or marketing –dominated companies? Should we focus on companies with which we already have strong relationships or just go after the most desirable companies? Should we go after companies that prefer leasing? Service contracts? Systems purchases? Sealed bidding? Should we focus on companies that are seeking Quality? Service? Price?
Situational factors	▪ Urgency ▪ Specific	Should we focus on companies that need quick delivery or service? Should we focus on certain applications of

	application ▪ Size of order	our product rather than all applications? Should we focus on small or large orders?
Personal characteristics	▪ Buyer-seller similarity ▪ Attitudes toward risk ▪ Loyalty	Should we focus on companies whose people and value are similar to ours? Should we focus on risk-taking or risk-avoiding customers? Should we focus on companies that show high loyalty to their suppliers?

Targeting Approaches

Target market selection is the next logical step following segmentation. Once the market-segment opportunities have been identified, the organization got to decide how many and which ones to target. Lot of marketing effort is dedicated to developing strategies that will best match the firm’s product offerings to the needs of particular target segments. The firm should look for a match between the value requirements of each segment and its distinctive capabilities. Marketers have identified four basic approaches to do this:

1. **Undifferentiated Marketing**

A firm may produce only one product or product line and offer it to all customers with a single marketing mix. Such a firm is said to practice undifferentiated marketing, also called mass marketing. It used to be much more common in the past than it is today. A common example is the case of Model T built by Henry Ford and sold for one price to everyone who wanted to buy. He agreed to paint his cars any colour that consumers wanted, ‘as long as it is black’. While undifferentiated marketing is efficient from a production viewpoint (offering the benefits of economies of scale), it also brings in inherent dangers. A firm that attempts to satisfy everyone in the market with one standard product may suffer if competitors offer specialized units to smaller segments of the total market and better satisfy individual segments.

2. Differentiated Marketing

Firms that promote numerous products with different marketing mixes designed to satisfy smaller segments are said to practice differentiated marketing. It is still aimed at satisfying a large part of the total market. Instead of marketing one product with a single marketing program, the firm markets a number of products designed to appeal to individual parts of the total market. By providing increased satisfaction for each of many target markets, a company can produce more sales by following a differentiated marketing approach. In general, it also raises production, inventory and promotional costs. Despite higher marketing costs, a company may be forced to practice differentiated marketing in order to remain competitive.

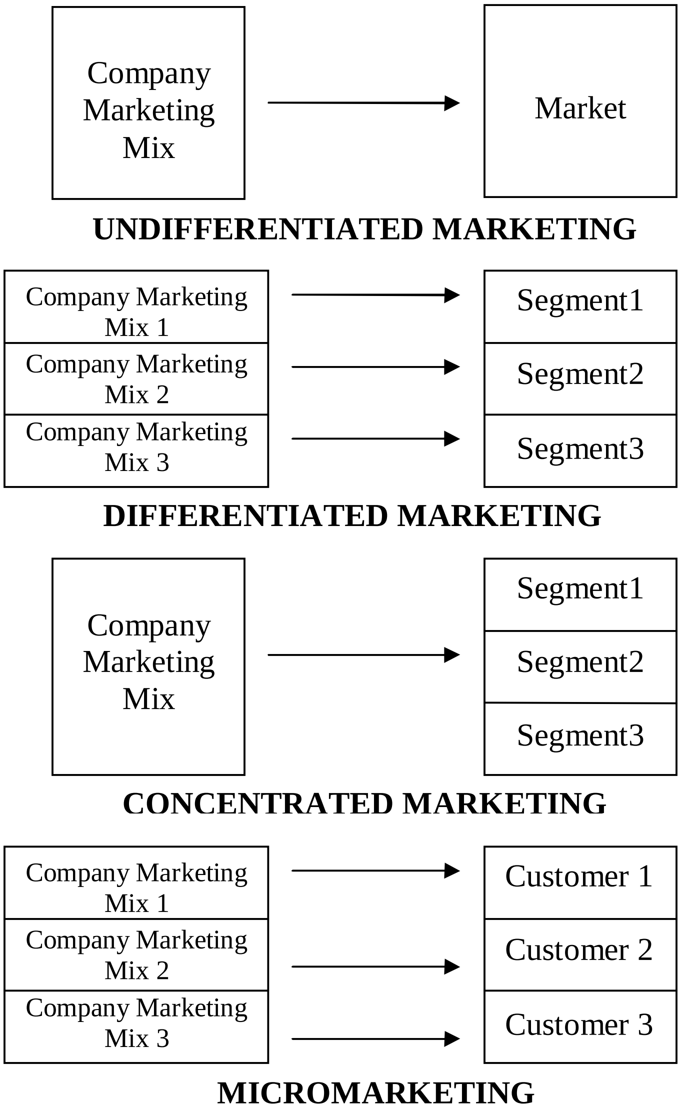
2. Concentrated Marketing

Rather than trying to market its products separately to several segments, a firm may opt for a concentrated marketing approach. With concentrated marketing (also known as niche marketing), a firm focuses its efforts on profitably satisfying only one market segment. It may be a small segment, but a profitable segment. This approach can appeal to a small firm that lacks the financial resources of its competitors and to a company that offers highly specialized good and services. Along with its benefits, concentrated marketing has its dangers. Since this approach ties a firm’s growth to a particular segment, changes in the size of that segment or in customer buying patterns may result in severe financial problems. Sales may also drop if new competitors appeal successfully to the same segment. Niche marketing leaves the fortunes of a firm to depend on one small target segment.

3. Micro Marketing

This approach is still more narrowly focused than concentrated marketing. Micro marketing involves targeting potential customers at a very basic level, such as by the postal code, specific occupation or lifestyle. Ultimately, micromarketing may even target individuals themselves. It is referred to as marketing to segments of one. The internet allows marketers to boost the effectiveness of micromarketing. With the ability to customize (individualization attempts by the firm) and to personalize (individualization attempts by the customer), the internet offers the benefit of mass customization – by reaching the mass market with individualized offers for the customers.

Figure 1.6.1 Market targeting approaches


Company Marketing Mix
Market
UNDIFFERENTIATED MARKETING
Company Marketing Mix 1
Company Marketing Mix 2
Company Marketing Mix 3
Segment1
Segment2
Segment3
DIFFERENTIATED MARKETING
Company Marketing Mix
Segment1
Segment2
Segment3
CONCENTRATED MARKETING
Company Marketing Mix 1
Company Marketing Mix 2
Company Marketing Mix 3
Customer 1
Customer 2
Customer 3
MICROMARKETING

Activity 1.6.3

Match the following real life marketing examples with the above mentioned targeting approaches.

1. Titan now selling fashion eyewear and watches apart from the regular watches
2. A promotional email from Amazon.com based on your previous purchases
3. Air Deccan with its no-frills, single-class airline model
4. The battery-operated, eco-friendly electric car, Reva

Positioning

Having chosen an approach for reaching the firm's target segment, marketers must then decide how best to position the product in the market. The concept of positioning seeks to place a product in a certain 'position' in the minds of the prospective buyers. Positioning is the act of designing the company's offer so that it occupies a distinct and valued place in the target customers' minds. In a world that is getting more and more homogenized, differentiation and positioning hold the key to marketing success!

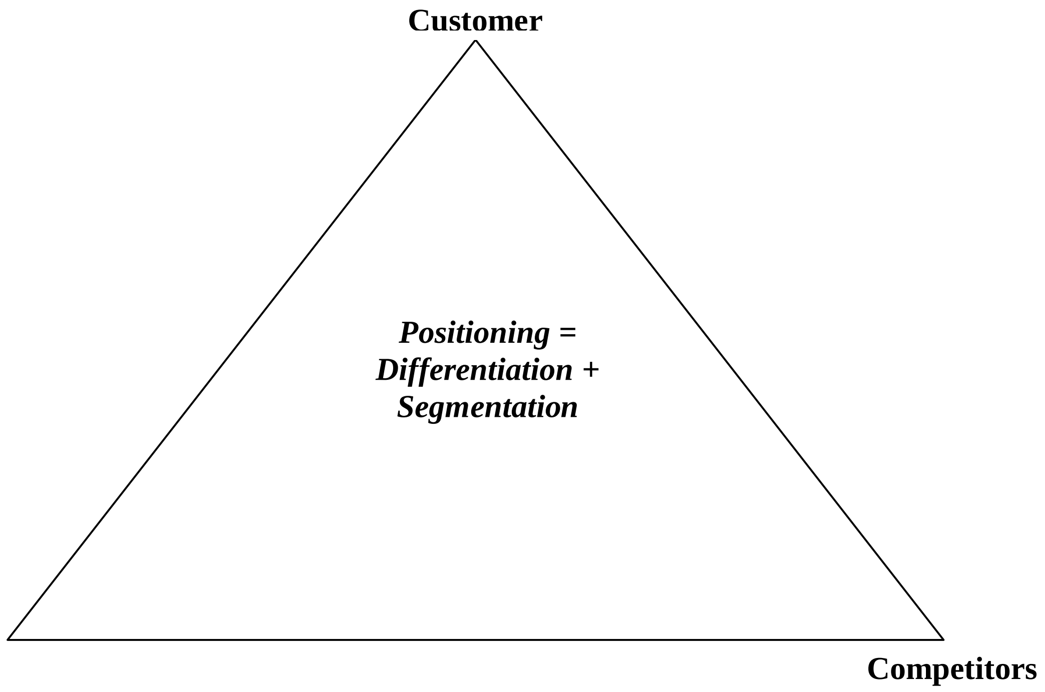
The positioning gurus, Al Ries and Jack Trout define positioning as: Positioning is … your product as the customer thinks of it. Positioning is not what you do to your product, but what you do to the mind of your customer. Every product must have a positioning statement. A general form of such a statement is given below:

Product X is positioned as offering (benefit) to (target market) with the competitive advantage of (competitive advantage) based on (basis for competitive advantage)

For example, the positioning statement of toothpaste X may read as follows:

Toothpaste X is positioned as offering to kids a toothpaste made especially for those kids who don't like to brush with the competitive advantage of a mild fruit taste and lower foaming.

One way to think about positioning is to imagine a triangle, with the baseline anchored by the organization and competitor concerns and the apex, the customers. The marketer's job is to find a positioning of the product or service that is both possible and compatible with organization constraints which uniquely places the product/service among competitive offerings so as to be most suitable to one or a number of segments of customers.



Positioning can be done along different possibilities. Attribute positioning is when the positioning is based on some attribute of the product. Benefit positioning is when a derived benefit is highlighted as the unique selling propositioning. Competitor positioning is when a comparison is drawn with the competitor and a differentiation from the competitor is emphasized. Product category positioning is when a product is positioned to belong to a particular category and not another category which probably is crowded. Quality/price positioning is when the product is positioned as the best value for money. For example, a Pizza may be positioned on its taste or it's natural contents or as an easy meal or with a thicker topping or as the lowest priced offering the best value for money. Each one of them offers a distinct positioning possibility for a pizza.

In the positioning decision, caution must be taken to avoid certain positioning errors: Underpositioning is done when a unique, but not so important attribute is highlighted. As a result, the customer does not see any value in such a position. Overpositioning is done when the product performance does not justify the tall claims of positioning. Confused positioning is when the customer fails to categorize the product correctly and the product ends up being perceived differently from what was intended.

Doubtful positioning is when the customer finds it difficult to believe the positioning claims.

Positioning map is a valuable tool to help marketers position products by graphically illustrating consumers' perceptions of competing products within an industry. For instance, a positioning map might present two different characteristics, price and quality, and show how consumers view a product and its major competitors based on these traits. Marketers can create a competitive positioning map from information solicited from consumers or from their accumulated knowledge about a market.

Activity 1.6.4

Draw a positioning map to describe the toothpaste market. Choose any two characteristics to show how the different brands can be viewed based on these traits.

Sometimes, changes in the competitive environment or cultural environment force marketers to reposition a product – changing the position it holds in the minds of prospective buyers relative to the positions of competing products. Nestle's Milkmaid brand has undergone few repositionings in the last few decades. The original positioning as 'sweetened condensed milk as a milk substitute' became obsolete when India attained self-sufficiency in milk production and milk products. So Milkmaid was repositioned as a 'ready ingredient' in preparing home-made sweets. Recipes started appearing on the labels. It succeeded for a certain period of time. Soon the Indian households were no longer making home-made sweets, but rather consuming ready-made, packaged sweets. If it was an economic environment factor that necessitated a repositioning earlier, it was now the changing demographic of the Indian homes. Milkmaid took another successful attempt at repositioning. Milkmaid was then repositioned as a 'central ingredient' in making the deserts at home. The recipes naturally changed. Repositioning helps a firm to tide over the environmental changes and the changes in consumers' preferences. It extends the life of a brand.

Positioning Identities

Positioning is creating an identity to your product. This identity is a cumulative of the following four positioning identities.

1. Who am I?
   It refers to the corporate credentials like the origin, family tree and the 'stable' from which it comes from. For instance, think of the mental associations when a buyer buys a Japanese car and it is a Honda!
2. What am I?
   It refers to the functional capabilities. The perceived brand differentiation is formed using the brand's capabilities and benefits. For instance, the Japanese cars are known for their fuel-efficiency, reasonable-price and utility-value.
3. For whom am I?
   It refers to the target segment for the brand. It identifies the that market segment for which his brand seems to be just right and has competitive advantage. For instance, the Japanese car makers have traditionally focused on the quality-conscious, value-seeking and rather-serious car buyer
4. Why me?
   It highlights the differential advantage of the brand when compared to the competing brands. It gives reasons as to why the customer should select this brand in preference to any other brand. For instance, Japanese car makers have tried to score a competitive advantage on the lines of quality and technology

Differentiation Across the Consumption Chain

A research finding suggests that there are one million branded products in the world today. As a result, the market is increasingly competitive and confusingly crowded. For the customers, it means more choices than they know how to handle and less time than they need to decide. For the marketers, it is hyper-competition and continuous struggle to win the attention and interest of choice-rich, price-prone customers. The tyranny of choice for the buyers are represented by the following facts:

- An average hypermarket stocks 40,000 brand items (SKUs)
- An average family gets 80% of its needs met from only 150 SKUs
- That means there's a good chance that the other 39,850 items in the store will be ignored

The implication is that those that don't stand out will get lost in the pack! The average customer makes decisions in more than 100 product/service categories in a given month. He/she is exposed to more than 1600 commercials a day. Of this, 80 are consciously noticed and about 12 provoke some reaction. The challenge for marketers is: how to get noticed (i.e. *differentiation*) and be preferred (i.e. *positioning*)?

Most profitable strategies are built on differentiation (i.e.) offering customers something they value that competitors don't have. A close look at consumer behaviour reveals that people buy on the differences. An ability to create compelling differences remains at the heart of a firm's competitive advantage. The battle has always been (and still is) about differentiation - create winning differences in customers' minds.

People pay attention to differences (though at different levels) and tend to ignore undifferentiated products. Here is an example of how Nike (the top-dog sports shoe brand) creates winning differences at cognitive, normative and wired-in levels in the buyer.

1. **Cognitive (conscious decisions) Level**
   - *'I buy Nike because it's made of engineered materials which enable higher athletic performance'*
2. **Normative (semiconscious feelings) level**
   - *'I buy Nike because it's "in" with my crowd'*
3. **Wired-in (subconscious determinants) level**
   - ('*Nike appeals to my desire to be cool, fashionable, strong, aggressive …*')

Organizations use several differentiation dimensions. The most popular are product differentiation, service differentiation, personnel differentiation, channel differentiation and image differentiation.

Activity 1.6.5

Match the following brands with their chosen differentiation dimensions.

1. Apple's iMac (with an innovative product design)
2. Honda's bikes (In the US market, they did an image make-over for bike riders to differentiate from the image created by Harley-Davidson bike riders)
3. Singapore airlines (highlighting the 'Singapore airlines girl' is its campaign)
4. Dell computers (Dell becoming synonymous with Direct (channels) selling)
5. Cemex cement (using GPS to deliver ready-mix concrete just-in-time)

Most firms while seeking to differentiate themselves from the competition focus their energy only on their products and services. In a Harvard Business Review article, MacMillan and McGrath, advocate that a company has the opportunity to differentiate itself at every point where it comes in contact with its customers – from the moment the customers realize that they need a product or service to the time when they no longer want it and decide to dispose of it – that is, anywhere along the spectrum of the Consumption chain – from need recognition to product disposition. Based on this idea, some avenues for differentiation are listed below:

- How do people become aware of their need for your product/service?
  - If you can make consumers aware of a need in a way that is unique and subtle, that's a powerful source of differentiation!
- How do customers find your offering?
  - Opportunities for differentiating on the basis of the search process that is made less complicated, more convenient, less expensive and more habitual.
- How do customers order and purchase your product/service?
  - Differentiating by making the process of ordering and purchasing more convenient
- How is your product/service delivered?
  - Delivery affords many hard-to-duplicate opportunities for differentiation
- What happens when your product/service is delivered?
  - An often overlooked opportunity between product/service delivery and usage; opening, inspecting, assembling are real issues for customers
- How is your product installed?
  - Differentiation that is particularly relevant for companies with complex products
- What help do customers need when they use your product?
  - Most helpful and fastest response gives a cut above the rest
- How is your product moved around?
  - Addressing the difficulties experienced in transporting a product from one location to another
- How is your product repaired or serviced or exchanged?
  - Differentiating by being proactive and practicing acceptance
- What happens when your product is disposed of or no longer used?
  - Differentiation opportunities through Responsible marketing and Green Marketing

Activity 1.6.6

Think of how the petrol bunks have evolved over the years – starting from selling a commodity to marketing a branded product in landscaped locations! Is there a way to differentiate selling petrol?

Case study: HLL goes adult with its ice creams
(Excerpt from *Business Today*, May 8, 2005)

The summer looks hot. That isn't the weatherman talking, but the ice cream marketer, who seems to have abandoned an age-old positioning of the product (as a fun, family treat) in favour of a new one: as an adult indulgence. Leading the new strategy is HLL, which has reworked the marketing communication of its Kwality brand to something more risqué. Its TV and billboard ads show adults "pleasuring it up" quite suggestively. What's up? According to an HLL spokesperson, the repositioning is "a bid to reflect the sensorial awakening in society". "Evidence of which", the spokesperson continues, "is to be found in the spending one sees at malls and multiplexes". At any rate, says the spokesperson, given that half of the country's population is between 18 and 34, its new communication better reflects its image as a youthful and indulgent brand. Rivals haven't yet followed suit. On the contrary, ones like the Anand-based milk marketing cooperative Amul, whose officials were not available for comment, are sticking to their family-centric campaigns, Will HLL's new positioning put its Rs.89 crore (2004 revenue) ice cream business on the boil? Hard to say. For, this is one category where availability plays a bigger role than just branding.

Question: What are the market segmentation, targeting and positioning insights that you draw from this case? Why is HLL repositioning its Kwality brand of ice creams?

Unit – I

Lesson 1.7
Introduction to Marketing Mix

Objectives

In this lesson, we will introduce you to the activities that comprise a firm's marketing program. These activities are popularly referred to as the 4 Ps – product, price, place and promotion. After you work out this lesson, you should be able to:

- Understand the major product decisions in marketing planning
- Know the pricing objectives and the factors that influence the pricing decisions
- Appreciate the role of marketing channels and understand the important channel decisions to be taken
- Comprehend the Promotion Mix of marketing and the different elements in the promotion mix
- Learn how the 4 Ps combine to create effective marketing programs

In this lesson, we will discuss the following:

- The sub-elements of each of the 4 Ps of marketing
- Marketing programs
- Product management decisions
- Channel management
- Marketing communications
- Pricing basis, objectives and approaches

Introduction

After marketers select a target market, they direct their activities towards profitably satisfying that segment. Although they must manipulate many variables to reach this goal, marketing decision making can be divided into four areas: product, price, place (distribution) and promotion (marketing communication). The total package forms the marketing mix – the blending of the four elements to fit the needs and preferences of a specific target market. These are the four variables that a marketer can use in different combinations to create value for customers. Several of the sub-elements in each of the four Ps that constitute the marketing mix are listed in the following table.

Elements of the Marketing Mix	Sub-Elements
Product	Product design Product positioning Product name and branding Packaging and labeling Breadth and depth of product line Level and type of customer service Product warranty New product development process Product life cycle strategies
Price	Manufacturer, wholesaler and retailer selling prices Terms and conditions Bidding tactics Discount policies New product pricing (Skim Vs. Penetrating pricing)
Promotion (marketing communications)	Advertising Sales force policies Direct marketing (mail, catalog) Public relations Price promotions – for the consumers and the channel Trade shows and special events
Place (distribution channels)	Direct Vs. Indirect channels Channel length Channel breadth (exclusive, selective or intensive) Franchising policies Policies to ensure channel coordination and control

Marketing Programs

A marketing program is made up of the various elements of the marketing mix and the relationships among them. The concept of the marketing mix emphasizes the fit of the various pieces and the quality and size of their interactions. There are three degrees of interaction – consistency, integration and leverage. Consistency is the lack of a poor fit between two or more elements of the marketing mix. For example, to sell a high quality product through a low quality retailer would seem inconsistent. While consistency is the lack of a poor fit, integration is the presence of a positive, harmonious interaction among the elements of the mix. For example, heavy advertising can sometimes be harmonious with a high price, because the added margin from the high price pays for the advertising and the high advertising creates the brand differentiation that justifies the high price. Leverage is the situation in which each individual element of the mix is used to the best advantage in support of the total mix.

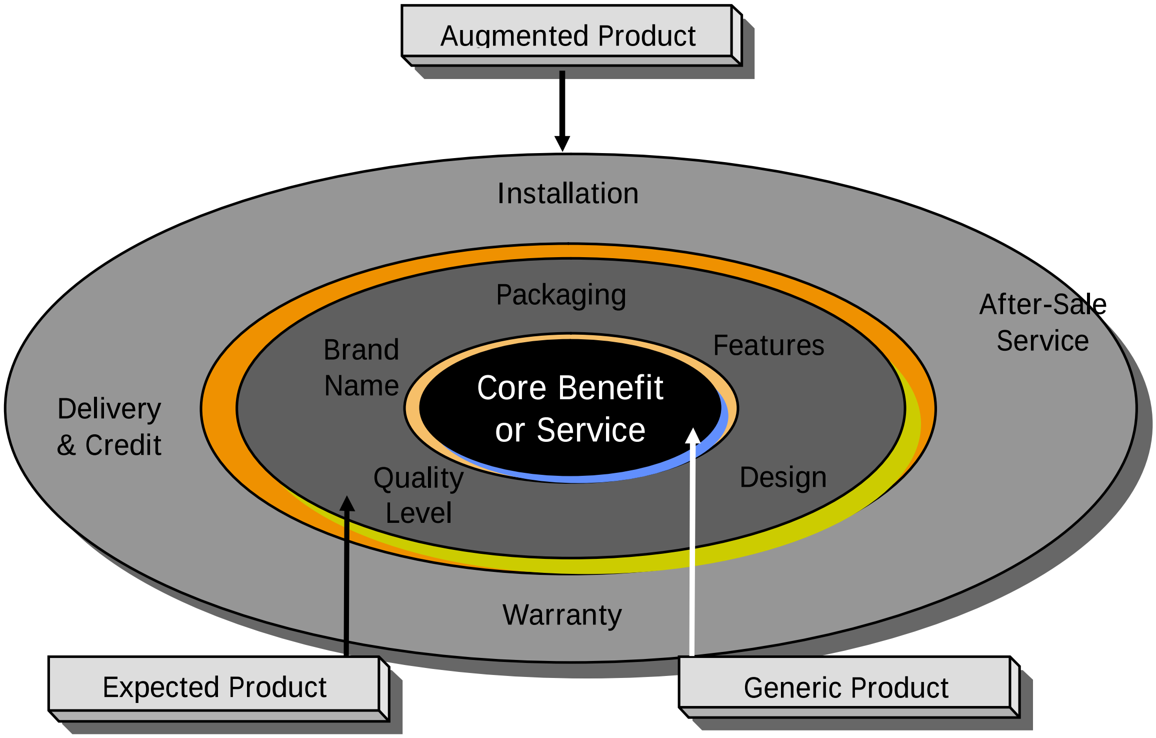
Once the elements of the marketing mix have met the internal tests of consistency, integration and leverage, the next step is to check that the proposed program fits the needs of the target customers, the core competencies of the company and the likely responses of key competitors.

The concept of program/customer fit encompasses development of a marketing program that fits the needs of the target-market segments. For that, the market must first be carefully and explicitly delineated. If the target has not been defined, it cannot be reached! The program must not only fit the market, but also fit the company. A marketing program must match the core competencies of the company that is implementing it. For example, an organization with extensive mass advertising experience and expertise is more likely to be able to carry out a program that leans heavily on advertising than an organization less strong in that particular area. An effective marketing program must not only fit the company's own core competencies, it must also take account of competitors' programs. Competitive/program fit can be defined as the characteristic of a marketing program that, while building on a company's strengths and shielding its weaknesses, protects it from competitors by capitalizing on their weaknesses, in the process creating a unique market personality and position.

Like most concepts, the marketing mix is an abstraction and real marketing programs do not always fit perfectly the product, price, place and promotion paradigm. In fact, several parts of the mix fall at the interface of two elements. For example, brand, which is often views as an aspect of product, is clearly also part of marketing communications and can serve to help coordinate product policy and communication.

Product Management Decisions

Product decisions start with an understanding of what a product is, viz., the product offering is not the thing itself, but rather the total package of benefits obtained by the customer. This is called as the total product concept. For example, a watch from Rediff.com is not just a watch but one shipped within 24 hours of order and unconditionally guaranteed. This broad conception of a ‘product’ is key to seeing possible points of differentiation from competitors. The following chart illustrates the total product concept.


Augmented Product
Installation
Packaging
After-Sale Service
Brand Name
Features
Core Benefit or Service
Delivery & Credit
Quality Level
Design
Warranty
Expected Product
Generic Product

The ‘generic’ product is no longer sought (leave alone bought!) by the customers. It merely represents customer need fulfillment. The expected product represents the customers’ minimal purchase conditions. When such customer expectations are met, it leads to customer satisfaction. The augmented product represents the customers’ wish-list. It leads to customer delight. Beyond the augmented product, lies the potential product which represents all that this product can become in the future. It represents the customers’ dream.

Activity 1.7.1

Illustrate the product hierarchy or ‘total product concept’ with an example.

Core benefit -
Basic product -
Expected product -

Augmented product -
Potential product -

A taxonomy of product line planning decisions can be developed by considering some product planning decisions firms face. Product line breadth: How many different lines will the company offer? A guiding principle in answering breadth questions is the company's position on desired consistency or similarity between the lines it offers.

Product line length: How many items will be there in a line providing coverage of different price points?

Product line depth: How many types of a given product?

Individual item decisions: decisions on individual items need to be considered within the context of the firm's full product line due to item interrelationships. At the individual item level, decisions to be made are whether to undertake efforts to delete an item from the line (pruning), reposition an existing product within the line (balancing), improve the performance of an existing product to strengthen its positioning (modernization), introduce a new product within an existing line (filling) and introduce a product to establish a new line (extension). The assortment of product lines and individual product offerings is called as the product mix.

A proactive approach to new product development follows some form of a sequential process, for example,

- opportunity identification
- design
- testing
- product introduction and
- life cycle management.

In the opportunity identification stage, the firm identifies a customer problem that it can solve. In addition it identifies the concept for a product through idea generation and screening initiatives. The next two stages, design and testing are linked in an iterative process. The firm must first embody the product idea in a concept statement which is tested via presentation to potential customers. After the firm has settled on the product and a supporting plan, it reaches product introduction. Decisions at this stage involve the geographic markets to which the product will be introduced and whether markets will be approached at the same time or sequentially over time. After introduction, a process of Product Life Cycle Management begins. The Life Cycle stages are introduction, growth, maturity and decline. The marketing objectives vary across these stages – so do the sales, profits and costs. The marketing mix also changes from stage to stage.

The first P of marketing, namely, the product also looks at how firms build and maintain identity and competitive advantage for their products through branding. Functions like packaging and labeling also perform specific functions within the ambit of product management.

Place (Channel Management)

The marketing channel is the set of mechanisms or network via which a firm 'goes to market' or is 'in touch' with its customers for a variety of tasks ranging from demand generation to physical delivery of the goods. The customer's requirements for effective support determine the functions which the members of the channel must collectively provide.

Eight generic channel functions can be identified, viz.,

1. Product information
2. Product customization
3. Product quality assurance
4. Lot size (e.g. the ability to buy in small quantities)
5. Product assortment (refers to breadth, length and width of product lines)
6. Availability
7. After-sale service
8. Logistics

Marketers develop channels and formulate distribution plans to ensure that consumers find their products available in the proper quantities at the right times and places. Distribution decisions involve transportation, warehousing, inventory control, order processing and selection of marketing channels. Marketing channels are made up of institutions such as wholesalers and retailers – all those involved in a product's movement from producer to final consumer. The two major decisions in channels are: (1) Channel design – which involves both a length and breadth issue, and (2) Channel management – what policies and procedures will be used to have the necessary functions performed by various parties

An important point with respect to channel design is that while there are options about whether a particular institution (e.g. a distributor) is included in the channel or not, the setting implicates specific tasks which need to be accomplished by someone in the channel. One can eliminate a layer in the chain but not the tasks that layer performed.

Promotion (Marketing Communications)

The next element of the marketing mix is deciding the appropriate set of ways in which to communicate with customers to foster their awareness of the product, knowledge about its features, interest in purchasing, likelihood of trying the product and/or repeat purchasing it. Effective marketing requires an integrated communications plan combining both personal selling efforts and non-personal ones such as advertising, sales promotion, direct marketing and public relations. Put together, they are referred to as the promotion mix.

A useful mnemonic for the tasks in planning communications strategy is the 6 *M*s model:

1. Market – to whom is the communication to be addressed?
2. Mission – what is the objective of the communication?
3. Message – what are the specific points to be communicated?
4. Media – which vehicles will be used to convey the message?
5. Money – how much will be spent in the effort?
6. Measurement – how will impact be assessed after the campaign?

The marketing communications or promotions mix is potentially extensive – including non-personal elements as well as personal selling. The popular non-personal vehicles are advertising, sales promotion and public relations. Advertising in media is particularly effective in

- Creating awareness of a new product
- Describing features of the product
- Suggesting usage situations
- Distinguishing the product from competitors
- Directing buyers to the point-of-purchase
- Creating or enhancing a brand image

Advertising is limited in its ability to actually close the sale and make a transaction happen. Sales promotions may be an effective device to complement the favourable attitude development for which advertising is appropriate. One trend in advertising is the movement to more precisely targeted media vehicles. Direct marketing to households or email marketing to individuals are just instances of this trend.

Sales promotion includes things such as samples, coupons and contests. These are usually most effective when used as a short-term inducement to generate action. The three major types of sales promotion are:

(1) consumer promotions – used by a manufacturer and addressed to the end consumer
(2) trade promotions – used by the manufacturer and addressed to the trade partners
(3) retail promotions – used by the trade partners and addressed to the end consumer

Public relations refers to non-paid communication efforts, such as press releases. These efforts do entail a cost to the firm, but generally are distinguished from advertising by virtue of the fact that the firm does not pay for space in the media vehicle itself.

Personal selling as the communication vehicle presents the advantage of permitting an interaction to take place between the firm and a potential customer rather than just the broadcast of information. The importance of personal selling in the promotions mix typically increases with the complexity of the product and the need for education of potential customers.

The proper allocation of budget across the various media vehicles varies greatly depending upon the market situation. A fundamental decision is whether to focus on a ‘push’ or ‘pull’ strategy. In a push strategy, focus is on inducing intermediaries, such as a retailer, to sell the product at retail. Advertising’s job may be to make the consumer aware of the product, but the closing of the deal is left to the intermediary. Alternatively, a pull strategy means the end consumer develops such an insistence on the product that he or she ‘pulls’ it through the channel of distribution, and the retailer’s role is merely to make the product conveniently available.

Activity 1.7.2

Sort the following promotion mix elements in the order of importance for consumer marketing (B2C) and industrial marketing (B2B)

1. Advertising
2. Personal selling
3. Public relations
4. Sales promotions
5. Direct marketing

Pricing Basis, Objectives and Approaches

One of the most difficult areas of marketing decision making, pricing, deals with the methods of setting profitable and justifiable prices. It is closely regulated and subject to considerable public scrutiny. In comparison to the other 3 Ps – product, place and promotion - of marketing mix, the price element is the only revenue element whereas the others are cost elements. Also, this is the element which can be easily copied. To a large extent, the combination of the 3 Ps determine the target customer's perception of the value of the firm's product in a given competitive context. Conceptually, this perceived value represents the maximum price which the customer is willing to pay. This should be the primary guide to pricing the product. Once the firm has created value for customers, it is entitled to capture some of that value for itself to fund future value-creation efforts. This is the role of effective pricing.

Pricing Basis and Objective

In most situations, cost should act as a floor on pricing. In some circumstances, a firm intentionally sells at a loss for a time to establish a position in the market, but it is often difficult to increase prices later due to the customer's use of the introductory price as a reference point. With perceived value in mind, the first question is what is the marketing objective and how does the pricing objective derive from that? For example, the price that would maximize short-term profit is typically higher than the one which would maximize market penetration subject even to making some profit on each item. It can be described as a choice between a 'skim' and 'penetration' pricing strategy. In a skim strategy, the focus is on those consumers with high value. Starting with a high price and targeting a segment that is willing to pay this price, skimming happens. Later on, prices are reduced to reach the segments below. In penetration pricing, the firm sets a lower price to generate lots of sales quickly. It is designed to preempt competition and gain a significant number of customers early on. The appeal of a penetration strategy increases to the extent that (1) customers are sensitive to price, (2) economies of scale are important, (3) adequate production capacity is available, and (4) there is a threat of competition.

Since customers typically place different values on the product, the firm should consider whether it is worth trying to capitalize on these value variations by charging different customers different prices. In some cases, legal constraints and logistical practicalities can make this infeasible. However many firms owe their economic well-being to their ability to customize prices. In many cases, for example, prices are varied depending on when the buyer is booking, for how long, for what days of week and so on. These characteristics are used as indicators of the value the customer places on the product. Price customization can be achieved by:

- developing a product line – e.g. developing 'economy' versions of the product
- controlling the availability of lower prices – e.g. select availability in certain stores
- varying prices based on observable buyer characteristics – e.g. new vs. existing customers
- varying prices based on observable characteristics of the transaction – e.g. purchase volume

Another pricing approach is product life cycle pricing in which different prices are charged at different stages of the product's life cycle. Since the marketing objective and the cost structure various across the stages, the pricing approach also varies.

While product marketing mix consists of the 4 Ps, services marketing brings in additional 3 Ps into an extended marketing mix. The additional 3 Ps – People, Process and Physical evidence – are necessitated by the characteristics of the services. While products are tangible, services are intangible. While products can be manufactured and inventoried, production and consumption take place at the same time and hence are inseparable. While products can be standardized, services cannot be – thanks to the human interaction in service delivery. The perceived quality of service depends on who provides it, when and where it is provided and also to whom it is provided. Because of this, the heterogeneity in services throws a quality challenge. Finally, the services are perishable – so managing the demand and supply is crucial. Because of these characteristics of services, viz., intangibility, inseparability, heterogeneity and perishability, there is a need for industrializing and standardizing the services (Process), tangibilize the intangibles (through Physical evidence) and managing the service personnel (People) who are part of the service. The sub-elements of these additional 3 Ps are:

Additional 3 Ps in Services Marketing	Sub-Elements
Process	Flow of activities Service script (number of steps) Customer involvement
Physical evidence	Facility design Service ambience Equipment Signage Employee dress Point-of-sale displays Other tangibles (e.g. business cards)
People	Employees ▪ Recruiting ▪ Training ▪ Motivation ▪ Rewards ▪ Teamwork Customers ▪ Education ▪ Training

Answer key
Activity 1.1.1

An example purchase: Mobile phone

Form:

Conversion of raw materials (required to manufacture a watch) into a finished product (a watch)

Time:

During the festival season. Though there was a heavy demand, the product was readily available in many outlets

Place:

An authorized dealer in the same locality making the product available

Ownership:

In exchange for the price of the mobile phone, the title (ownership) of the phone is transferred to you.

Activity 1.1.2

MARKETING MYTHS

(The student may tick the myths that he/she thought about marketing from the following list and also add to the list since the given list is not exhaustive)

- Marketing and selling are synonymous
- The job of marketing is to develop good advertisements
- Marketing is pushing the product to the customers
- Marketing is transaction-oriented than relationship-oriented
- Marketing is a short-term business strategy
- Marketing is an independent function of a business
- Marketing is part of selling

Activity 1.1.3
(Students may coin their own statements to describe each era in the Evolution of Marketing)

Activity 1.1.4
Match the following: 1-F, 2-E, 3-C, 4-B, 5-D, 6-A

Activity 1.4.1
Industry: Aviation industry
Competitive environment

The entry of several low-cost carriers and the subsequent pressure on the standard carriers to come up with their own low-cost subsidiaries in the aviation industry

Economic environment.

The upbeat economy, booming businesses, growing leisure and tourism industry all of them contributing to high growth in the civil aviation industry Political-legal environment

The open-sky policy of the government and all-weather flying skills training made mandatory for all domestic carriers

Technological environment

Advanced airplanes with increased carrying capacity and better fuel utilization directly contributing to sales increase and cost decrease Social-cultural environment

The growing concept of travel and vacation, desire to cut travel time and cost resulting in a migration of many train travelers to low-cost carriers

Activity 1.6.1

1. Preventing tooth decay
2. enhanced sex appeal
3. whiter teeth
4. removal of smoking stains
5. fluoride protection
6. appeal to kids
7. Natural (herbal) contents
8. Traditional (ayurvedic) contents

Activity 1.6.2

1. Consumer background characteristics

1.1 Geography	- traditional product (neem) domination
1.2 Demographic	- ‘appeal to kids’
1.3 Psychographic	- preferring ayurvedic contents
1.4 General life-style	- enhanced sex appeal

2. Consumers’ market history

2.1 Product usage	- twice a day usage
2.2 Product benefit	- whiter teeth
2.3 Decision-process	- ‘buy 1 and get 1 free’

Activity 1.6.3

1 – Differentiated marketing
2 – Micromarketing
3 – Undifferentiated marketing
4 – Concentrated marketing (Niche marketing)

Activity 1.6.4

Positioning map for the toothpaste market can be drawn based on characteristics like ingredients (herbal Vs. chemical), benefits (emotional Vs. functional utilities), age (kids Vs. adults), usage (normal Vs. treatment), price (low Vs. high), attribute (taste Vs. contents) and so on. Different brands of toothpastes can then be plotted on the map depending on their positioning in the marketplace.

Activity 1.6.5

product differentiation	-	Apple’s iMac
service differentiation	-	Cemex cement
personnel differentiation	-	Singapore airlines

channel differentiation	-	Dell computers
image differentiation	-	Honda’s bikes

Activity 1.6.6
How to differentiate selling petrol?
Clue: Consider the ‘purchase links’ of the consumption chain for this product.

Activity 1.7.1
Product hierarchy – an example

Core benefit	-	lodging/accommodation
Basic product	-	A room
Expected product	-	A clean room with bath attached
Augmented product	-	Bed and breakfast; pick-up
Potential product	-	Customized room and menu (from your past preferences)

Actitivity 1.7.2

Promotions Mix elements (in the order of importance)

For consumer marketing (B2C)	-	1,4,2,5 and 3
For industrial marketing (B2B)	-	2,5,1,3 and 4

Glossary of Terms

Utility – Want-satisfying power of a good or service
Marketing – Process of planning and executing the conception, pricing, promotion and distribution of ideas, goods and services to create and maintain relationships that satify individual and organizational objectives
Marketing concept – Organization-wide consumer orientation with the objective of achieving long-run success
Relationship marketing – Development and maintenance of long-term, cost-effective exchange relationships with individual customers, suppliers, employees and other partners for mutual benefit
Customer orientation – Business philosophy incorporating the marketing concept that emphasizes first determining unmet customer needs and then designing a product/service for satisfying them
Market – The set of all actual and potential buyers of a product or service
Demands – Human wants that are backed by buying power
Buyer – The person who makes an actual purchase
Exchange – The act of obtaining a desired object from someone by offering something in return
Product – Anything that can be offered to a market for attention, acquisition, use or consumption that might satisfy a want or need. It includes physical objects, services, persons, places, organizations and ideas
Potential market – The set of consumers who profess some level of interest in a particular product or service

Environmental scanning – The process of collecting information about the external marketing environment in order to identify and interpret potential trends

Environmental management – An effort to attain organizational objectives by predicting and influencing the firm’s competitive, political-legal, economic, technological and social-cultural environments

Time-based competition – a strategy of developing and distributing goods and services more quickly than competitors can achieve

Demarketing – The process of reducing consumer demand for a good or service to a level that the firm can supply

Marketing audit – A thorough, objective evaluation of an organization’s marketing philosophy, strategies, plans, programs, practices and results

Consumerism – A social force within the business environment designed to aid and protect buyers by exerting legal, moral and economic pressures on businesses

Buyer behaviour – Process by which consumers and business buyers make purchase decisions

Consumer behaviour – Buyer behaviour of ultimate consumers

Reference group – Group with which an individual identifies strongly enough that it dictates a standard of behavior

Opinion leader – Trendsetter likely to purchase new products before others and then share the resulting experiences and opinions via word of mouth

Evoked set – Number of brands that a consumer considers buying before making a purchasing decision

Cognitive dissonance – Post-purchase anxiety that results from an imbalance among an individual’s knowledge, beliefs and attitude

Segmentation – Dividing a consumer population into several homogeneous groups based on characteristics like geography, demography, psychography and life style.

Target market – A homogeneous group of people in a heterogeneous marketplace toward whom a firm markets its goods and services with a strategy designed to satisfy their specific needs and preferences

Positioning – Consumers’ perceptions of a product’s attributes, uses, quality and advantages and disadvantages in relation to those of competing brands

Repositioning – Marketing strategy to change the position of a product in consumers’ minds relative to the positions of competing products

Undifferentiated marketing – Marketing strategy to produce only one product and market it to all customers using a single marketing mix

Differentiated marketing – Marketing strategy to produce to produce numerous products and promote them with different marketing mixes designed to satisfy smaller segments

Niche market - A firm targets its efforts on profitably satisfying only one market segment. It may be a small but a profitable segment

Marketing mix – blending the four elements of marketing decision making – product, price, distribution and promotion – to satisfy chosen consumer segments

Product strategy – element of marketing decision making involved in developing the right good or service for the firm’s customers, including package design, branding, trademarks, warranties, product life cycles and new product development

Product mix – A company’s assortment of product lines and individual offerings

Product life cycle – The four basic stages through which a successful product progresses – introduction, growth, maturity and decline

Pricing strategy – Element of marketing decision making dealing with methods of setting profitable and justifiable prices

Distribution strategy – Element of marketing decision making concerned with activities and marketing intermediaries that get the right good or service to the firm's customers

Promotional strategy - Element of marketing decision making that involves appropriate blending of promotional mix elements, namely, personal selling, advertising, sales promotions, direct marketing and public relations – to communicate with and seek to persuade potential customers.

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UNIT-II

LESSON – 2.1 PRODUCT DECISIONS

LESSON – 2.2 CONCEPT OF A PRODUCT

LESSON - 2.3 PRODUCT MIX DECISIONS

LESSON – 2.4 BRAND DECISION

LESSON –2.5 NEW PRODUCT DEVELOPMENT STRATEGIES

LESSON - 2.6 PRODUCT LIFE CYCLE STRATEGIES

2.1 PRODUCT DECISIONS

This unit on the first *P* of marketing, namely the Product, will help you answer the following questions:

- What product should the company make?
- Where exactly are these products to be offered?
- What should be the width of the product mix?
- How many different product lines can the company accommodate?
- How should the products be positioned in the market?
- What should be the brand policy?

OVERVIEW

It is a fact that product/service is a 'mixer of ingredients' where in the manufacturer / service provider who blends various marketing activities in a manner that strengthen the business the interests of the firm. As we seen in lesson 11, the crux of any marketing strategy is to bring about the desired operation in the light of prevailing circumstances. We also learned from the pervious lesson that the planned manipulated to get optimum results in limiting environments. This lesson narrates the important concepts like marketing mix, products, brand, trademark, packing and labeling with suitable example from Indian marketing environmental.

SIGNIFICANT OF MARKETING MIX

The most popular 4 Ps' framework as suggested by McCarthy with the marketing mix variables- products, place, promotion and price had origination from the study of the manufacturers – i.e. the organization engaged in production and marketing of goods – it is more oriented to deal with goods marketing situations. However service characteristics are radically different fro goods; and so are the challenges in their marketing. It is wrong to imply that services are just like products except for intangibility. But such wax-like logic as "apples are just like oranges, except for their apple ness'' does not stand the heat of nuts-and-bolts.

Marketing Product / service characteristics and add new dimensions to a marketing situation that is faced by the service manager. Given the product / service characteristics and activities in product/service firms, eight Ps' framework for services has been proposed. For the services, the additional prescribed Ps given below refer to activities that are service marketing mix can be summarized as follows:

Product - service core, levels, additional services, branding.
Price - price, discounts, terms of payment.
Place - location, channels of distribution, coverage.
Promotion - Advertising, sales promotion, personal selling and publicity.

FOR SERVICE ADDITIONAL 4 Ps WERE ADDED FOR MARKETING SERVICES. THEY ARE:

People - customer-provider relationship, training, culture, skills, and attitudes.
Physical- ambience, appearance, equipment, machines
Evidence – Buildings, physical facilities
Process – Activity sequence, quality management, customer participation and delivery process
Productivity – Efficiency of human and non-human capitals in the production process. But our discussion limits only to the first four Ps.

2.2 CONCEPT OF A PRODUCT

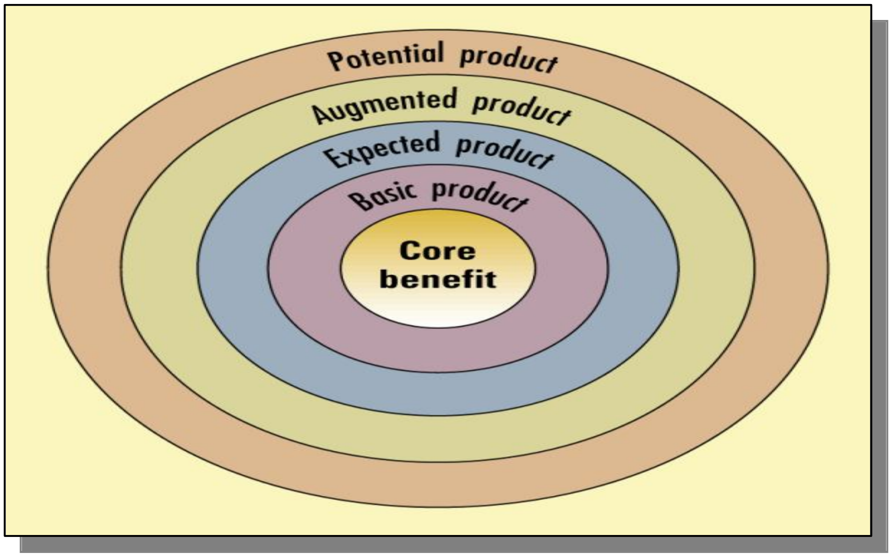
The term ‘product’ is widely used to refer a market offering of any kind. In its broadest sense this may be anything from the physical to the abstract – an idea or a moral issue. Generally, however, most products are made up of a combination of physical elements and services. This is true in services marketing, where the service offering can include tangible features, such as food in a restaurant, or be a ‘pure’ service, intangible in nature.

A service product refers to an activity or activities that a marketer offers to perform, which results in satisfaction of a need or want of predetermined target customers. It is the offering of a firm in the form of activities that satisfies needs such as hair styling done by a barber.

Consumers will buy only what suits them. As customers, we buy different kinds of products and services to satisfy our various needs. We buy toothpaste, butter, shaving cream, pen, scooter, and ticket for the U.S.A and many other such items in our daily life. As we understand, our decision to buy an item is based not only on its tangible attributes but also on psychological attributes such as services, brand, package, warranty, image, and etc. discussions about the marketing of goods apply to services as well. Services have special characteristics that make them different than products.

According to Alderson, W., “Product is a bundle of utilities consisting of various product features and accompanying services” according to Schwarte, D.J., “A product is something a firm markets that ill satisfy a personal want or fill a business or commercial need”.

At the time of product planning, the marketer has to think about FIVE types of benefits.



From Generic to Potential product - Most of you would be aware that a product has a personality of several components-like the physical products, the brand name, the package, the label etc. all of us know that most of the products are undergoing a constant change and the marketing man has been constantly engaged in enriching his product offer. In his attempt to score over competition, he has been bringing about refinement on his basic product offer, but managing the product was becoming more and more difficult. Hence the product traveled various levels:

- The Core Product
- The Generic product
- The branded Product
- The Differentiated product
- The customised product
- The augmented product
- The potential product

The **Core** benefits: what does the product mean to the customer? For example, a car offers generic benefits of convenience in traveling.

The **Generic product** Is the unbranded and undifferentiated commodity like rice, bread, flour or cloth.

The **Branded Product** The branded product gets an identity through a 'name'. Modern bread, Harvest are branded products. We would study in detail about brand name in the brand section.

The **differentiated product** The differentiated product enjoys a distinction from other similar products/brands in the market. The differential claimed may be 'real', with a real distinction on ingredient, quality, utility, or service, or it may be 'psychological' brought about through subtle sales appeals.

The **customised product** - *C*ustomer specific requirements are taken into account while developing the product. Commonly practised in the industrial product marketing, where the manufacturer and the user are in direct contact and the product gets customised to the requirements of the customer.

The augmented product

The augmented product is the result of voluntary improvements brought about by the manufacturer in order to enhance the value of the product, which are neither suggested by the customer nor expected by them. The marketer on his own augments the product, by adding an extra facility or an extra feature to the product.

The potential product

The potential product is tomorrow's product carrying with it all the improvements and finesse possible under the given technological, economic and competitive condition. There are no limits to the 'potential product'. Only the technological and economic resources of the firm set the limit.

Product differentiation - Is the act of designing a set of meaningful differences to distinguish the companies offering from competitor's offerings? The number of differentiation opportunities varies with the type of industry. The Boston consulting group has distinguished four types of industries based on the number of available competitive advantages and their size.

1. **Volume industry**: One in which companies can gain only a few, but rather large, competitive advantages.
2. **Stalemated industry**: One in which there are a few potential competitive advantages and each is small.

3. Fragmented industry: One in which companies face many opportunities for differentiation, but each opportunity for competitive advantage is small.

4. Specialised industry: One in which companies face many differentiation opportunities, and each differentiation can have a high payoff.

Theodore Levitt in one of his books “Marketing Success, through differentiation of anything” explains that in a market place, there is no such thing as commodity .All goods and services are differentiable. In a market place differentiation is everywhere .All the companies try to distinguish their offer from that of their competitor. This is true of even those who produce and deal in primary metals, grains, chemicals, plastics and money. Starting from technology to plant location to post sale service firms to the personnel/procedures employed for various functions like sales, production etc., companies can differ their offers in many ways. Companies usually choose those functions, which give them greatest relative advantage.

There are different strategy stances that firms can adopt

It is natural for different firms to take different strategy stances as the requirement; situational design of each is different from the other. One firm might find it appropriate to have direct confrontation with the market leader; another may find it appropriate to keep aloof for some time from the competition; and the third might may find it relevant to chalk out a strategy of sheer survival. No strategy stance is universally valid. Broadly strategy stances can be classified under three heads-Offensive/ confrontation strategy, Defensive and Niche strategy.

Offensive Strategy -Is the strategy of aggression usually employed by the firm that is not presently the leader, but aspires to leadership position in the industry. It acts as a challenger and the leader is mostly its target. It tries to expand its market share and utilises all the elements of the marketing mix in attacking the leader.

Defensive Strategy -Is usually employed by the leader who has the compulsion to defend his position against the confrontation of powerful existing competitors or strong new entrants trying to remove the leader from the topmost position. The leader has to maintain constant vigilance and defend its position against the attack of the challengers.

Niche Strategy - Is usually employed by firms, which neither confronts nor defend it. It cultivates a small market segment for itself with unique products/services; supported by a unique marketing mix. Small firms with distinctive capabilities adopt this stance. A market niche to be worthwhile must have characteristics such as reasonable size, profit potential and growth potential.

PRODUCT CLASSIFICATION

The nature of product is found to have considerable impact on the method of product positing. There are two classes of products consumer goods, and industrial goods, and this classification is useful in product positioning. The table given below shows the categories of consumer and industrial goods. Marketers have traditionally classified products on the basis of there characteristics: durability, tangibility and use. The following figure shows the products classification:

PRODUCTS CLASSIFICATION					
1.	Durability and tangibility	2.	Consumer goods	3.	Industrial goods
a.	N on-durable goods	a.	Convenience goods	a.	Material and parts
b.	Durable goods	b.	Shopping goods	b.	Capital items
c.	Services	c.	Speciality goods	c.	Supplies and business services
		d.	Unsought goods		0

Tangible / Intangible Attributes – key points

Tangible
Touch
See
Taste
Smell

Intangible
Can’t see
Can’t touch
Can’t smell
Can’t taste

Exercise: Think of examples of product/services possessing above tangible and intangible attributes

DURABILITY AND TANGIBILITY

(a) Non – durable goods: non-durable goods are tangible goods normally consumed In one or a few uses, for example, soap, salt and biscuits.

(B) Durable goods: for example, colour TV, Refrigerator, washing machine and Vacuum cleaners.

(c) Services: services rate intangible, inseparable, variable and perishable products, for example, airline and banking services

CONSUMER GOODS CLASSIFICATION

a. Convenience Goods: these are goods that the customer usually purchases frequently immediately and with a minimum of efforts, example includes soaps and newspapers.

Convenience goods can be further classification into three categories:

- i. Stable goods: consumer purchase on regular basis.
- ii. Impulse goods: consumer purchase without any planning or search efforts.
- iii. Emergency goods: consumer purchase on urgent need.

b. Shopping Goods: these are goods that the customer, in the process of selection and purchase characteristically compare on such bases as suitability and quality. Example: furniture, electrical appliances etc.

c. Specialty goods: these are goods with unique characteristic or brand identification for which a sufficient number of buyers are willing to make a special purchasing effort. For example, cars.

a. Unsought goods: these are goods the consumer does not know about or does not normally think of buying. The classic example of known but unsought goods is life insurance.

INDUSTRIAL GOODS CLASSIFICATION

a. **Material and Parts:** these are goods that enter the manufacturer's product completely. They fall into two classes. Raw material and manufactured material part

b. Capital Items: these are long lasting goods that facilitate developing or managing the finished products. They include two groups: installation and equipments.

C. Supplies and Business Services: these are short-listing goods and services that facilitate developing or managing the finished products.

DECISIONS, WHICH ARE USEFUL FOR PRODUCTS MANAGEMENT

The search for competitive advantage – and escape from price-based competition – often centers on the value – creating supplementary services that surrounds this core and add differentiation. Managers should be aware of the important of selecting the right mix of supplementary service elements-no more and no less than needed –and creating synergy by ensuring that they are all internally consistent. Customer research, evaluation of competitive offering and feedback from employees can all provide important inputs to the decision making process. Three principal factors should be considered here are.

- The nature of the market and competition from the product
- The nature of assistance needed by the product regarding production, engineering, financing, staffing and so on,
- Strategic requirement of a border nature, namely, those affecting the product line, the business or the whole corporation.

FACTORS TO BE CONSIDERED IN ORGANIZING FOR PRODUCT MANAGEMENT

- What do we want to out of product management
- What do we want our product manager to do?
- How do we want our product manager to do their jobs?
- What operational guidelines will we established?
- What expectation do we have for the specific contribution of product manager and product management?
- What authorities will be assigned to product managers?
- What are the number and nature of products and managers?
- What are product objective?
- How will we measure the effectiveness of our product management?

ROLE OF PRODUCTS MANAGER IN AN ORGANIZATION

In assessing the product manager's performance the following checklist can be used:

- Product line control
- Product life cycle, analysis and capitalization
- Product development and success of new products recommended
- Improved communication
- Improved supplies and sourcing
- More and better market information
- Wider and better market information
- Centralized products planning
- Coordination of activities
- Achievement of planned profits
- Cost and profit control

SUMMARY

What is a Product

- ❈ What you but, that satisfied what you want to be able to do
- ❈ It can be "good felling" causes you bought some cosmetic and someone said you looked pretty
- ❈ It could be a happy stomach cause you bought a meal that tasted great
- ❈ It could be easier homework cause you bought new software for your company
- ❈ Most customer think about product in terms of the total satisfaction
- ❈ This can lead t statements such as "we don't sell cars, we sell safety!"
- ❈ We don't sell houses, we sell homes

PRODUCT LINE

- ❈ A series of related products
- ❈ A group of products that are physically similar in performance, use or feature and intended for a similar market
- ❈ "… A set of products that are closely related."
- ❈ Shoes Nike, Adidas, Rebook, file, new balance, British knight, books, converse, vans, sic, puma notebooks, Toshiba, NEC, TI, compaq, IBM, DELL

- Apple, HP, Hitachi, mitsubishi, matsushita.

Cannibalization

- Situation involving one products taking sales from another offering in a product line
- Cannibalization occurs when sales of a new product cut into (reduce)the sales of a firm's existing products

2.3 Product Mix Decisions

- What product should the company make?
- Where exactly are these products to be offered?
- What should be the width of the product mix?
- How many different product lines can the company accommodate?
- How should the products be positioned in the market?
- What should be the brand policy?

Basically the answers to these will constitute the product policy of a firm .It constitutes the following:

Appraisal of the product line and the individual products- No product line is perfect and also does not run for all times to come. Changes happen in the business environment, customer tastes and preferences, extent of competition that pressurise the product policy of the firm. New, changed, advanced products are introduced or even old products are withdrawn from the market by the companies to revive the lost market image, to overcome the treat of functional obsolescence due to new improved /substitute products introduced by competitors, to regain profitability or when the product has entered a stage of decline. Firm needs to constantly monitor the company's product policy.

This topic of Product Mix & Product Line is very important so concentrate on it.

When we say a firm's product mix we are actually discussing about all product items it offers.

Hindustan Lever's product mix includes agro-chemical products, soaps, detergents, toothpaste, shampoos, Talcum powders, cosmetics and now, frozen foods. Just suppose any organization is marketing more than one product then it has a product mix.

Product item—a single product

Product line—all items of the same type

Product mix—total group of products that an organization markets

Now if I say a product line what do you understand from this?

It is basically a group of products that are **related because of customer, marketing and or production considerations. I hope all of you know that** Rin, Wheel, Rin Solarox, Rin detergent powder, Surf, and Surf Ultra are part of Lever's detergents line and Le Sancy, Lux, Rexona, Lifebuoy, are part of its soaps line. When we are discussing about a typical large multi-product firm's product mix includes new, growing, maturing and declining products.

Reasons many firms do not want to limit themselves to one product.

1. To counteract the effects of the PLC on a one product firm.
2. To even out seasonal sales patterns.
3. To use company resources and capabilities more effectively.
4. To capitalize on middlemen and consumer acceptance of established products.
5. To spread production and marketing costs over a wider product mix.
6. To become better known and respected by middlemen and consumers.

Breadth & Depth

Now you have a fair idea on what is a product mix. In product you have to define the structural dimensions of breadth (or width) and depth. Breadth refers to the number of different product lines. Depth refers to the number of product items within each line.

A firm can expand its product mix by increasing the number of product lines **or** the depth within one or more product lines. HLL expanded in breadth when it entered the agro-chemical business. It expanded in depth when it bought TOMCO a soaps and detergents company.

Width of product mix

Lever's Product Mix and Product Lines (partial listing)

Detergent	***Soap***	***Toothpaste***	***Talcum Powder***	***Cosmetic***
Rin bar	***Le sancy***	***Close up***	***Ponds***	***Fair & lovely***
Wheel bar	***Lux***	***Pepsodent***	***Liril***	***Lakme***
Rin Powder	***Rexona***			
Wheel Powder	***Lifebuoy***			
Surf	***Liril***			
Surf Ultra				

You would have noticed that so many companies market just one or two product lines, and hence their product mix is narrow. **Do you know in which all areas General Electric operates?** It basically operates in diverse fields, and has broad product mix. You can see in Fig that each product mix has a *depth, which* is given by models, colours, sizes, available in each individual product lines.

As all of us know that pharmaceutical company has a product line of antibiotics. It has several dosage forms like it can be in the form of capsules, dispersible tablets for children, vaginal suppositories, injections, eardrops, eye drops and Syrups under the dosage form and then the size of the package can be different. The company has several brands of antibiotics, and each brand has several dosage forms and sizes. We can say, that its product mix has depth. On the contrary, a few products, in one size only as one brand is an example of a shallow product depth.

All the decisions related to product lines offers are from company's strategic plan and marketing plan. It considers the segmentation of the market and targeting. Just suppose an organization wishes to target young' children, it can add a whole new product line for it. New product lines are either a matter internal development or can be acquire. Each product line also can be expanded. The important idea is that the product line of a company reflects the objectives of the organization, the targeting decided upon and the buyer behaviour in a given market.

You can modify existing Product lines:

We have a number of reasons to alter either an existing product or a product line. The reasons could be to support marketing strategy, to improve sales, to improve profits, to expand market share. We can also consider what the product as such contributes to the product portfolio. We can modify a product line by altering either one or more than one of the following attributes:

(1) Composition of the product line

(2) Expansion or contraction of product line

(3) Value addition process

(4) Brand

(5) Packaging

(6) Physical characteristics

(7) Positioning

The first two attributes are relevant to a set of products in the product line. The rest are relevant to either individual products or product lines.

Expanding and Reducing the Product Line:

As you are aware that there are many models of TV available in the market. There is a large variety of radio sets from Sony. Underlines bras are available in a number of styles. Syrups and crushes are available in many flavours, e.g., Rasna concentrates and Mala's crushes. There are technical products with higher and lesser sophistication. We find many product categories where consumers prefer to have a great variety for their satisfaction. Marketers are adopting strategies of adding new versions with new specifications, while retaining the old versions for the less sophisticated consumers.

Sometimes this addition of new products to existing line is done to include complementary products, e.g., a toothpaste marketer may add toothbrushes to the product line. Camel may introduce paintbrushes, which go welt with its watercolours. Sometimes, there are occasion to delete a product/products from the line. A product, which shows decline in terms of sales, may be abandoned. Non-contributing products may be eliminated. While doing so, it should be seen that other products in the product line are not affected.

Product line length:

Now you should ask a question what is the optimum size of a product line?

A line is too long if after eliminating a product is results into increased profits. A line is too short when any addition to it results into increased profits.

One thing should be clear to you that the Company's overall objectives do affect the length of its product line. For instance, a company may have the objective of expanding its market share. It will then have a longer product line. Contribution of individual products to profits may be ignored. However, a company whose objective is to have larger profits will have a shorter product line consisting of those items, which contribute to profits substantially Product lines have a tendency, to lengthen over a period of time. Many a time, a firm may, have extra capacity, which is used for developing new items. . Sales people and trade put pressure on management to keep on adding items to a product line so as, to satisfy their customers.

Lengthening of the line shoot up costs. At some point, this must come to halt. Loss making items are then eliminated. The contribution of items to profits is studied. Thus in the life of an organization, there is a cycle of longer product line followed by a pruned product line. This cycle is repeated again arid again.

Line stretching

Most of the companies have range of products in its existing product lines, like Videocon has a range of TVs in its product line, right from budget TVs to premium TVs. Line stretching occurs when this range is lengthened. This stretching could be upward, downward or both ways.

Upward stretching:

Here a company operates in the lower end of the market. By upward stretch, it proposes to enter the higher end. Perhaps, it is motivated by higher margin of profits, higher growth rate or a position of a full-range marketer. This decision has its own risks. A well-established high-end marketer might assault the stretcher by stretching downwards. Besides, it is a question *of* credibility of a lower-end marketer -whether he will be able to produce high quality products. There is one more risk. The existing infrastructure of a low-end marketer may not be competent to deal with the high-end market.

Downward stretch:

Lets start with an example: like all of you know parker, parker started with pens only at high price but if we look at parker today we can see products available in the range of 50 Rupees which no one could have though of in older times.

Many companies start with high-end products, but later stretch downwards by adding 1ow-priced products. The down-end products are advertised heavily so as to pull customers to the whole line on the basis of price. Videocon advertises its budget line 14" inches TV at Rs. 8,000. Once the customer is pulled, he may decide to buy a higher priced model- he trades up. This strategy needs careful handling. The budget brand being promoted should not dilute the overall brand image. Besides, the budget brand must be available. Consumers should not get a feeling that they were hooked to a bait, for switching later. Downward stretch is practiced in the following situations:

- A competitor stretches upward and challenges the marketer. He counter-attacks him stretching downwards
- Most companies start at the upper end, and then roll downwards.
- The high-end market has a slow growth rate.
- By filling the gap at the low-end, new competition is avoided.

Downward stretch has its own risks. The down-end item might cannibalize the high-end items. Besides, our downward stretch might provoke a competitor to move upward. Down-end product may not be managed properly as the company may not have that capacity. It may dilute the brand image of the company's products. It is, however, needs careful consideration - a product line should not have a gap at the lower-end. It exposes the company to competition, e.g., American car companies faced the competition from small-sized, Japanese cars at the lower-end of the market.

Two way stretch

Beside upward and downward stretch *you* can even stretch in two ways like several companies serve the middle-end market. They can stretch their product line in both the directions. A hotel company operating hotels in the comfort category where each room has a tariff 2000-3000 a day might decide to have elite upper-end hotels with tariffs of Rs. 5000-7000 a lower-end budget hotels with tariffs of Rs. 600-1500 a day. Ashoka group of ITC has thus elite 5-Star hotels, at the upper-end comfort hotels at the middle-end and budget hotels like Ashoka Yatri Niwas at lower end.

Application exercise:

Go to the area of your town that has a number of restaurants. Compare the product mix of one with the other. Are there any differences in width or depth? How could they stretch their lines?

Another concept, which is very important and should be know to you, is cannibalization:

When the sales of the firms new products are due mainly because of decreasing sales of its existing and established product then we say that cannibalization has occurs in brief we can say by this you are actually eating away your own market. A good example of it would be Hyundai Santro they have introduced Santro Xing as a new product in the market in other way they have cannibalized their own market, like a person who wanted to buy Santro old model will buy Xing as it latest so they are not capturing new customer but converting their own customers only if they are able to make a person buy their product where he was planning to buy some product of Maruti then it is not cannibalization.

If you want to avoid cannibalization, the new product should not be identified too closely with established products. Instead it should be targeted with new appeals to different market segments. Cannibalization is desirable when margins on new products are higher than those on established Products. In highly competitive industries, it is often desirable to induce target customers to trade up to the firm’s newer products. This strategy is adopted by Videocon International, Which entered the market with a low priced color TV with basic features and then introduced more sophisticated models up the price scale in order to ensure that customers in all segments would buy only Videocon products.

PRODUCT LINES AND BRANDS

Most service organization offers a line products rather than just a single product. Some of these products are distinctly different from one another. Again in response to changing market opportunities, companies may revise the mix of products that they offer. Following example illustrate this concept.

British airways (BA), which explicitly reorganizes eight different air travel products – or brand – under the British airways umbrella. (The company also has equity shares in several other airlines). There are four intercontinental service brands –

Concorde (supersonic deluxe service), first class (deluxe subsonic service), club world (business class) and world (business class), and world traveler (economy class) ; two intra –European brands-club world (business class) and euro – traveler (economy class) : and within the united kingdom, the super shuttle brand, offering a graduated economy seat and high – frequency service. In additional, six commuter airlines, flying in British airways colors, operate service in partnership with BA under the British airways express brand. As described by Douglas each British airways brand has a key brand proposition and a set of clearly stated product specifications for preflight, in-flight and on-arrival service element. To provide additional focus on product, pricing and marketing communications, responsibility for managing and developing each brand is assigned to a brand management team. Through internal training and external communication, staff and passengers alike are kept informed of the characteristic of each brand.

2.4 BRAND DECISION

Many consumers products their basic feature, need attractive packing and a ‘brand name’. A brand is a symbol or a mark that helps customers in instant recall, differentiating it thereby roam the competing products of a similar nature.

What is the brand? too often even marketing professional don’t have an answer and to many have their ‘own’ answer. Which makes life very confusing! We’ve trawled though our resources to find some of the best definitions: the dictionary of business and management defines a brand *Asia name, sign or symbol used to identify items or services of the seller(s) and to differentiate the from goods of competitors*

Signs and symbols are parts of what a brand is, but to us this is a very incomplete definition. Walter Land or one of the greats of the advertising industry, said: “ *simply put, a brand is a promise. By identifying and* authenticating a products or service it delivers a pledge f satisfaction and quality. In his book, ‘ building strong brand’ David Aaker suggests the brand is a ‘mental box’ and gives s definition of brand equity as : ‘a set of assets (or liabilities) linked to a brand’s name and symbol that adds to (or subtracts from) the value provided by a product or service. According to the American marketing association, “A brand name is a part consisting of a word, letter, groups of words or letters to identify the goods or services of a seller or a group of seller and to differentiate them from those of the competitors.” David Ogilvy defined a brand are not necessarily positive! Building from this idea of a ‘mental box’ a more poetic definition might be : these are all great definitions, but we believe the best is this : “a brand is a collection of perceptions in the mind of the consumer. A brand is the most valuable real-state in the world, a corner of the consumer’s mind” . Why is the best? Well, first of all it is easy to remember, which is always useful! But it is also best because it works to remind us of some key point:

1. This definition make it absolutely clear that a brand is very different from a product’ or service. A brand is intangible and exists in the mind of the consumer.

This identification helps us understand the idea of brand loyalty and the ‘loyalty ladder’. Different people have different perceptions of a product or service, which places then at different point of loyalty ladder. A brand mark is a symbol or a design used for the purpose of identification. For example: Air India’s MAHARAJA. The legal version of a brand mark is the ‘trade mark’ e.g., Ashok Masal and Good Health Atta. A brand is given legal protection from being used by others because it is capable of exclusive approbation. A brand distinguishes a product or service from similar offerings on the basis of names are: LUX, LIRIL, REXONA, EVITA, PROTEX, HAMAM AND LE SANSI in case of toilet soaps; SUR, ARIEL, and NIRMA in case of detergents and NIVEA, FEM, OIL OF OLEY, CHARMIS AND VASELINE in case of vanishing creams.

Building Brands in the new economy –Heidi and Don Schultz urge companies to:

•Clarify the corporation’s basic values and build the corporate brand.

•Use brand managers to carry out the tactical work.

•Develop a more comprehensive brand-building plan.

•Define the brand’s basic essence to be delivered wherever it is sold.

•Use the brand-value proposition as the key driver of the company’s strategy, operations, services, and product development.

•Measure their brand-building effectiveness, not by the old measures of awareness, recognition, and recall, but by a more comprehensive set of measures including customer-perceived value, customer satisfaction, customer share of wallet, customer retention, and customer advocacy

Brand preference

- **Aaker’s five levels of customer attitude:**

  –The customer will change brands, especially for price reasons. No brand loyalty.

  –Customer is satisfied. No reason to change brands.

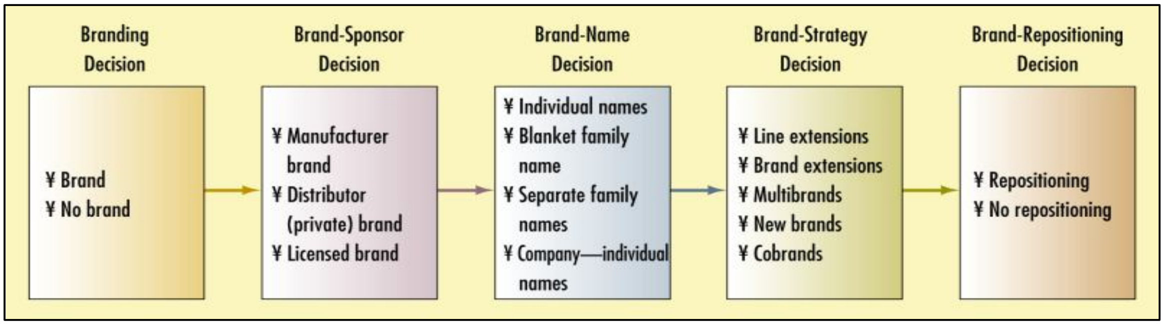
  –Customer is satisfied and would incur cost by changing brand.

  –Customer values the brand and sees it as a friend.

  –Customer is devoted to the brand.

Branding Decision: To Brand or Not to Brand?

An Overview of Branding Decisions


Branding Decision
¥ Brand
¥ No brand
Brand-Sponsor Decision
¥ Manufacturer brand
¥ Distributor (private) brand
¥ Licensed brand
Brand-Name Decision
¥ Individual names
¥ Blanket family name
¥ Separate family names
¥ Company—individual names
Brand-Strategy Decision
¥ Line extensions
¥ Brand extensions
¥ Multibrands
¥ New brands
¥ Cobrands
Brand-Repositioning Decision
¥ Repositioning
¥ No repositioning

Brands provide a strong competitive advantage to the companies owning them and hence they are increasingly becoming important tradable assests. In 1993, Coca-Cola paid about Rs.175 crore to buy Thums-up, Limca, Citra and Gold Spot brands. In 1994 Godrej soaps paid Rs.12 crore to acquire the Rs.67 crore translectra.

In 1995, Smithkline Beecham paid Rs.42 crore to acquire the Crocin brand from Duphar Interfan. In 1997, Knoll Pharma sold Coldarin and Burnol for Rs.34 crore Ranbaxy paid Rs.80 crore to Gufic Labs for Mox, Zole Excel and Suprimox. In 1997, Hindustan Lever paid Rs.110 crore for Lakme's basket of brands and only Rs.29 crore for Lakme's two plants.

In 1999, Marico industries bought parachute and Suffola brands from Bombay oil industries for Rs.30 crore. The Gramophone company of India acquired Sangeetha, a leading audio producer of classical and devotional songs in the South. Acquiring a brand is a better, superior option over purchasing the entire operations of the company owing them for 3 months. The buyer buys only the brand name. The brand name could be used to sell anything, which comes under the established brand personality. For example, the Burnol brand name could be used to sell an antiseptic like Dettol. Buying a brand provides a ready-made market. Apparently, Ranbaxy bought Mox because its own brand in the name family, Amoxycillin was not doing too well. Buying a brand saves a lot of brand building time and cost. Drug companies are known to recoup the cost of acquiring a brand in less than four years.

SUMMARY

1.What is a brand?

A name, term, sign, symbol, or design used to identify the products of one firm and to differentiate them from competitive offerings.

Something used to show customers that one product is different then the products of another manufacturer. Worlds, letters, or symbols that make up a name used to identify and distinguish the firm's offerings from those of its competitors.

2. Generic Name Brand

A brand name over which the original owner has lost exclusive claim because all offerings in the associated class of products have become generally known by the brand name (usually that of the first or leading brand in that product class).

3. Trademark

Brand that has been given legal protection and has been granted solely to its owner Originally helped trace the source of the guild producer

In modern era, makes it easier to identify all the products from a particular company.

Makes shopping easier

Helps the companies launching new products

Brand Recognition – awareness, loyalty, quality, emotion "customers remember the brand"

Brand Preference / Loyalty – the degree to which customers are committed to further purchases e.g. "choose the brand over other brands"

Brand Insistence – "willing to search for it." and if they don't find the brand they want, will not but a substitute

Brand Equity – "… the values of a brand's overall strength in the market…"

Brand Awareness – your product is the first that comes to mind in a certain product category e.g. Snapple ice tea, jeans – Levi's, Walkman – SONY

Brand Awareness – your product is the first that comes to mind in a certain product category e.g., ice tea = Snapple, running shoes = Nike

Trademark

A brand that has been given exclusive legal protection – name and the design

PACKAGING

Earlier, packaging was considered a major expense in marketing. For some toiletries, packaging costs actually exceeded the costs of contents. Today, it is however, fully recognized that packaging helps in branding and promoting brand loyalty. It also enables the buyers to handle and carry their products with case. Moreover, packaging may cut marketing costs thus adding to profit.

QUALITIES OF GOOD PACKAGING

- Attractive appearance
- Convenient for storage and display
- Shield against damage or spoiling
- Product description shown on the package

FUNCTION OF PACKAGING ESPECIALLY FOR CONSUMER GOODS

i. Protection and presentation are the basic functions of a packaging

ii. Modern marketing methods demand that, package be convenient to handle transport requirements.

iii. A package must be made to consistent and rigid quality standards. The consumer demands uniformity each time he purchases a product.

iv. Transport economics

v. Every package must be recognizable and

vi. Every package must have eye appeal

Packing to be satisfactory should satisfy the following conditions:

i. It should be capable of withstanding the hazards of handling and transport. The cargo may be handled manually and mechanically. The handling methods may differ between places. When manually handled, it may be tilted, draped, thrown, pulled, pushed, rolled etc. further it may also be subject to compression dude to stacking. The packing should, therefore, be capable of withstanding such hazards of handling and transportation.

ii. It should be easy to handle. To facilitate easy handling, bulk packs may be provided with handling facilities like books, handles, gripper's etc. in case of products which shall not be turned upside down, the position should be clearly indicated like marking 'this side up'. In case of fragile articles, which shall not be subject to rough handling, the size, shape and weight of the pack should be amendable for smooth handling. Further, it should also be indicated on the pack.

iii. It should be amendable to quick examination of contents. It may be remembered that the customs authorities of the exporting and importing countries may want to examine the contents.

iv. It should be easy to identify

v. It should be adequately marked.

vi. Unless it is necessary, the contents shall not be disclosed.

vii. It should be easy to dispose of.

viii. Packing must confirm to the buyer's specifications. If any and the regulations in the exporting and importing countries, guidelines and regulation by the shipping company, etc. care should be taken to observe the established has prescribed packing standards for certain goods. The British standard packing code, published by the British standards institution and Exporters Encyclopedia, USA, give detailed packing instruction. Shipping companies also given certain packing instructions especially for highly dangerous products. According to the products he intends to export, the exporter has to choose the right type of packing 1 to send the goods in good condition to the destination. A right package always guarantees the right quality of the product at the time of delivery.

LABELLING

Labeling is regarded as part of marketing because packaging decision making involves the consideration of the labeling requirements. In international trade, many countries insist that labeling should be done in the absence of such a statutory requirement. Statutory obligations are important aspects of labeling. Many countries have laid down labeling requirements in respect of a number for commodities. According to the regulations labeling of food items should disclose information about a number of aspects like date of manufacturing, expiry date or optimum storage period for good which do not have an indefinite storage period, composition, storage conditions, necessary method of use, if necessary etc.

ROLE OF PACKAGING

1) It helps increase sales
2) It adds to the use of a product
3) It helps promote a product
4) It contributes to the safety of a product
5) It helps in storage
6) It helps in product differentiation

PACKAGING DECISIONS

Packaging Design

It is not easy to design a package for various items. For example, all shaving creams come in tubes, but different brands of shaving cream have different packaging. Because of the high cost of packaging some companies have resorted to refill packs.

Color

Color is an important factor for determining customer acceptance or rejection of a product. The use of right colors in packaging may help marketers reap huge advantage. Packaging color should be attractive so that it may help promote sales.

Packaging the Product Line

A company must decide whether to develop a family resemblence in the packaging of its several products. Families packaging involves the use of identical packages for all products or the use of packages with some common feature.

CASE STUDY

In the processed meat industry, Sara Lee Meats (SLM) is a star. It owns and operates meat-processing plants in 40 different nations. SLM's business strategy includes product innovation, acquisitions and mergers, and market leadership in a number of different categories. Its growth strategies support an annual 6 percent growth in sales. Important U.S. brands in the Sara Lee product line are Kahn's, Jimmy Dean, Hillshire Farms, Bryan, State Fair, Best's Kosher, and Tastefuls!. According to SLM executive George Chivari, "We work very hard at Sara Lee on brand equity. . . . We have to make sure our new ideas are not only profitable and achieve big volume for our [retail] customers, but also that they are consistent with the quality of the brand and there is a good fit." Tastefuls! is a product that SLM feels is a particularly good fit with the company's other products. The lunch combination features two small sandwiches, chips, and dessert and was developed and marketed by a subsidiary of SLM, Jimmy Dean foods. Up until the development and marketing of Tastefuls!, Jimmy Dean has just made produced sausage.

QUESTIONS

1) Given what you have read about Sara Lee Meats, you would think its executives want you to classify the SLM products as
2) One method SLM can use to maintain its brand equity would be to:

QUESTIONS

1) Define a product
2) What do mean by product line
3) Explain the components of management
4) Describe major options available for branding a consumer product
5) How do you classify consumer product
6) Discuss in detail how productization will help IT products manager in India
7) Explain the significance of packing and labeling
8) List major industrial products
9) Explain the significance of product management. How branding packaging and labelling help product manager in realising their business goals.

10) Classification products both industrial and consumer according to the type and use of products

11) What do you mean by productization? How do you position an IT product like SPSS for Indian managers?

12) Explain products positioning. Describe the importance of selecting a products line for gaining competitive advantage in FMCG industry India

13) Explain the concept of brand equity, brand awareness and trademark based on the example taken from a software industry.

2.5 NEW PRODUCTS DEVELOPMENT STRATEGIES

OVERVIEW

With advances in technology and intense competition, the creation of new products has become a way of life in India. However, begin a developing country, India is yet to face a situation of too many products chasing a handful of customers. Moreover, the sheer size of the Indian market and the continuing economic development has opened up new vistas for launching new products. This lesson discusses new products development process in detail and also analyses the new product launches in India in the new millennium.

NEW PRODUCTS LAUNCHES

An analysis of new products development in the recent past shows that these products have been either offshoots of technological development in the west or improvement over the existing products in the areas of their, style, substance or packing. In the recent past, new product launches in India have shown that these launches can be broadly classified into three categories.

b. Marketing Innovations

Companies have been improvement on existing products and have launched these as new products in the market. For instance, magi noodles, soft drink in tetra pack, shrikh and pan parag. Etc. are basically slightly alternated version of existing or old products. Here, consumers did not require changing their consumption habits drastically to accommodate these new products. These are example of improvement in the products whose success was derived more from marketing innovation such as packing, branding and easy availability, rather than any significant change in the substance of the product itself.

c. Product Improvement

The launch of 100cc two-wheelers, radical types, instamatic cameras are basically slight innovations on the technology / design of existing products, although the products category as such already existed in its primitive form. Such new products are generally targeted for a new class of buyers. The success of such ventures depends upon the ability of the marketers to convince the consumer about the improvement in the performance over traditional brands(s) as well as over similar new extract. For example, in the 100cc two wheelers vehicle market, TVS Suzuki was the entrant and it had captured a sizable market. Subsequently, hero Honda became the market leader in this category of motorcycle by virtue of better performance and marketing techniques.

d. Technological Innovations

The Indian market has experienced a rapid induction of products like personal computers, photocopiers and colour television. Generally these products require some kind of assembling of improved kits. Although adaptation of such products calls for substantial change in the consumption pattern, yet these products have succeeded in view of their significant utility to the user. Such venture require an initial awareness building and persuasion to install the product. Initial resistance to change may delay any adoption of new technologies. However, a look at the track record of such new product shows that early entrants have reaped the benefits of leadership. Subsequent entrants have faced difficult in established themselves.

THE TECHNOLOGY / MARKET MATRIX

Another way to look at new products is through one of strategic planning's most useful analytical devices – an array of future options or alternative such as that shown in figure 1.1, A firm has roughly four way to gain new business – see quadrants A, B, C and D in the figure 13.1

New Product Growth Opportunities		**Technological Newness**	
		Present Or Improved Technologies	**New Technologies**
Market Newness	Current Market	A improved products	B Line Extension
	New Markets	C new use and market extensions	D Diversification

The easiest strategy is quadrant A – selling more of the product line to current customers. This involves product improvement, smarter marketing and increasing market shares. New products management plays a minor role and the activity is often called market, development, not product development.

Quadrant B and C involves capitalizing on the firm's current strengths. If the strengths is franchise with a particular customer group, quadrant B's strategy is to develop more product t sell to them. Such products don't have to be unique because the franchise will help sell them. Quadrant C says the firm's strength is technology – something the firm known or does especially well. Example are coca-cola's bottling system. Coming's glass skills and Hewlett packand's electronics capabilities. Such firms try to develop new products that exploit their technology.

Quadrant D, commonly called diversification, involves leaving both the firm's customer base and its technology base. This high-risk strategy should be used only under special circumstances. The new products may come by acquisition rather than through internal product development.

OVER VIEW OF NEW PRODUCTS DEVELOPMENT PROCESS

New products development consists of the certain of new ideas, their evaluation in terms of sales potentials and profitability, production facilities, resource available, designs and production testing and marketing of the products. The main task of the product planners is to identify specific customer needs and expectations and align company's capabilities with the changing market demands. In each of these stages, the management must decide :(a) whether to move on to the next stage, (b) to abandon the product, or (c) to seek additional informations.

ROUTES OF NEW PRODUCTS DEVELOPMENT

Transfer of Technology

New Products have often been launched, based on new technology, either acquired from the parent company or with foreign collaboration. Launch of the personal computer or photocopying machine is a move in this direction.

Diversification

Sometimes companies have entered into new lines of business and catered to altogether new markets for the first time. DCM'S entry into the LCV market fits into this category. Similarly, ITC's decision to enter into hotels, paperboards, edible oil, and tissue paper is a diversification strategy. Likewise, Shaw Wallace diversified to real estate business. In general, diversification strategy tries to reduce the dependence of a company on a limited line of products. At times, companies find the new business more profitable than their former activities.

Additions to Existing Product Lines

New product lines and brand extensions have sometimes supplemented a company's existing business. Videocon's entry in to washing machines and music systems form color televisions is a case in point. Similarly, as a business group, Godrej's strategy to expand its product range from consumer non-durables like toiletries to durable such as refrigerators, cupboards and even office equipments is a classic example of product line extension.

Improvements / Revisions in Existing Products

New products that offer superior performance and replace existing products are another way of entering the market. For example, the launch of transistor sets and cassette players, though primitive by today's standards, were at one time new to the market. They eventually replaced radios and gramophones. More recently Bata has successfully launched many sportswear, fashion jeans and apparels.

Cost Reductions

New products that provide similar performance at lower cost e.g., Nirma detergent, Tata – 407 LCV.

Products Relaunch

Sometimes old products have been relaunched with minor improvements and targeted at completely new markets or consumer segments, e.g., the launch of many food products like Good day biscuits, Tata Tea, Pan Parag, et. Fall under this type of new product launches.

SIGNIFICANCE OF NEW PRODUCT DEVELOPMENT

Whatever may be nature of operation of a concern, product planning and development is necessary for its survival and growth in the long run. Every product has a life cycle and t become obsolete after the completion of its life cycle. Therefore, it is essential to develop new products and alter or improve the existing ones to meet the requirements of customers. One of the most common products – planning problems relates to the addition of new products to the existing product line. Addition of new products involves generation of new product ideas, appraisal of various possibilities, economic analysis, product development, product testing, test marketing and developing markets. Another important problem of product planning is modification or elimination of existing products. The need for continuous of the product is great because society's needs are always changing and improved products must be introduced to fulfill them. All products have certain deficiencies, as they are the result of great many compromises. The perfect product has yet to be made. Research makes possible the reduction of these deficiencies and brings about improved products.

NEW PRODUCT DEVELOPMENT PROCESS

The developers must be conscious of the probabilistic nature of their endeavors. New product development endeavors are complex, strongly dependent on diversified human resources and significantly affected by factors and events beyond the developers control. Thus, the belief that the implementation of a mechanical methodology can assure success is an illusion and at times a delusion.

SOURCES OF NEW PRODUCT IDEAS

Customers: Customers are sometimes able to discuss their requirements and offer ideas that will meet those problems.

Competitors: Systematic comparison or bench marking with the competition may offer good source of new product ideas.

Distributors: Suggestions from distributors and their problems in handling present products often thrown up new ideas.

Creative techniques: Brainstorming, focused interviews and technological forecasting enable one to find out the latent capabilities of innovations.

External world: The external world, especially the use of their technology, offers a good source of ideas for implementation in the home market.

Research and development: Create new product ideas through R&D.

From initial generation of ideas to full commercialization and well into the mature age of a product, the developers should strive to control what is in their power to control a do to monitor what is beyond their control. No single facet of new product development can assure success. Few facets are so deter mental that they are cannot be at least alleviated. Because of the probabilistic nature of new product development, planning and assessments must consider long-term repercussions.

Organizational Structure and Staffing

Given a clear strategy it is necessary to build the organizational capability to meet the challenge. At times this is simply appointing a committee. Other times it is creating an entirely new team and physically separating it from the ongoing organization. Selecting the right persons for such a team is difficult.

Concept Creation and Development

Once the enabling conditions of strategy and organization are identified, actual ideation can begin. First, the team must focus on one area of interest or activity – specifically, a product category, a group of team may study floppy discs and try to improve them. Another team may try to find better ways to solve the problems of teachers. Or they may work to develop improved gold balls or golf balls or golf clubs. They may focus on their design capability and find new applications. Or they may focus on combinations of two or more of these areas.

CONCEPT DEVELOPMENT

Concept development involves asking question such as the following:

Need: Do customers find a strong perceived need for the benefit offered?

Trust: Do they believe that the new product has the benefits claimed?

Communicability: Do customers easily understand the key benefits being offered?

Usage: Does it offer easy adoption?

Perceived Value: Do Customers see it as offering value at the price being considered?

After the working area is defined, concept generation begins, often at a hectic pace. Ideas flow fast and in most cases rejection is equality fast. The team looks for the few fast and inmost cases rejection is equally fast. The team looks for the few concepts the warrant concepts development – the evolving of an original ideation attempt into a specific statement of need, form and technology that can be evaluated.

Concept Evaluation

Often considered the heart of the new products process, the Evaluation State is long, involved, and difficult. Evaluation actually begins when the strategist evaluates the organization's abilities. And it continues long after a product is marketed since a product often needs revision to remain competitive. Concept testing and other prescreening marketing research prepare the team for the actual screening evaluation. This evaluation is a full, detailed analysis of the proposal. If the concept passes screening, technical development begins. The technical work produces prototypes, which can then be evaluated and if all goes well, the finished product can be prepared for use testing. Next, the team joins the new product to its marketing plan for a test of them combined – called market testing. All of the above data combine to permit a full financial analysis near the end of development.

Commercialization

Management's decision that the new item is worth marketing either in a test market situation or in a full – scale launch – is called the point of commercialization. Pilot processes are then converted to full-scale manufacturing. Final design specifications are written. Marketing strategy is finalized, including actual brand, packaging, service commitment etc. The team gradually moves the company from tentative exploration of a concept into production and marketing of a new product.

Review and Evaluation

After launch the entire project must be reviewed to see how successful the team was, those problems they faced and what they can learn to facilitate the next project.

ANALYSIS OF NEW PRODUCT LAUNCHES IN INDIA

Empirical data suggests that in highly competitive markets such as in the US, the success rate of new launches, depending on the strictness of definition of success, varies from a low of two per cent to a high of 10 per cent. Markets in India are not as competitive as in the West and therefore, the success rate of new launches is likely to be healthier. A study by Abraham Koshy, revealed the following facts

On an overall basis, out of all the new launches, 53 per cent were successes and the remaining 47 per cent were failures. This implies that, cater is paribus, even at an optimistic level, new launches are likely to have a probability of success of around 50 per cent. In reality, this proportion may even at an optimistic level, new launches in the country today, given the level competitiveness in the market and professionalism of companies, is likely to be less than 30 per cent! This is worse than even the odds when an unbiased coin tosses; no company can invest huge resources for new launches if the probability of success is so unfavorable. The message from this insight is clear when the chances of survival are so low, the only way to beat the odds is through a systematic and professional approach to managing new launches. Other wise it is 50 – 50.

The mortality rates of new brands indeed tend to the high; only about 36 per cent of new products launched in the market with new brand names survived, the remaining 64 per cent were failures. This is indeed more unfavorable than the overall situation presented in the preceding paragraph it means that if you do not have a strong brand to leverage and therefore, there is a need to build brand awareness and create brand preferences afresh, then you should be even more thorough in your new launch efforts.

Life extensions and brand extensions were significantly more successful than the launch of new brands. Thus, 71 per cent of new launches that were line extensions and 63 per cent of brand extensions were successful in the market place. From one perspective, this suggests that your chances of success in a new launch are far greater if you leverage. From a different perspective, it also means that a levering strategy will not automatically guarantee you success; the results show that nearly a third of line extensions as well as brand extensions were failure. These in other words imply that even if you have strong brands, you need to be systematic in configuring your offer in tune with market needs. Inappropriate leveraging of brand names, leveraging weak brands and improper alignment of marketing mix elements are certified formulae for failures.

How can one Influence Success of New Launches?

A perplexing question that a practitioner is often confronted with is the reasons for product failures. Marketing literature suggests several reasons for product failures. These reasons are broadly classified under product (or offer) related factors, market by the research team (or consumer) related factors, market by the research team related factors and competition related factors. The latter two reasons, namely market related and competition related factors provide the context of a firm’s marketing operations and hence these are factors on which the firms can exert little control. All that a firm can do is to understand these given conditions and then align the total market offer based on these realities. And this is given where many firms slip rather badly. Findings of the study conducted by IIM, Calcutta provided interesting insights into the ways in which firms manage their new product activities.

Failure in Utilizing / Adopting Marketing Research Technique

The fundamental condition to succeed in any market is a deep understanding of consumers and an excellent appreciation of competitors and their activities. This can come about only if your company has strong systems and methods, not only to collect and analyze market data, but also to disseminate the information thus obtained to relevant decision makers within the organization. Studies revealed that nearly 67 per cent of the executives noted that market research agencies are seldom utilized by their companies to collect market data in a formal and structured manner; only the remaining 33 per cent of companies either frequently or almost always used marketing research agencies. Granting that it may be somewhat costly to use market research agencies on a regular basis, the extent of utilization of internal mechanisms to collect market data also does not seem to be very high. Nearly half the companies do not have strong formal mechanisms to collect systematic data on a regular basis from their own sales people and about a third of the companies rarely collect data from their retailers. If this is the general trend, then it is not very surprising that the success of new brand launches is low. The message, therefore, is that you need to review your internal systems and processes for gathering and utilizing market data relating to your consumers and competitors to what your decisions become sharper and data based. Success otherwise will be elusive.

Failure in Identifying Market Opportunities for New Brand Launches

One of the weakest links in many organizations is the absence of any systematic approaches for identifying market opportunities, either for introducing new brands and products, or for relaunching and\or repositioning of existing products. A glimpse at the mindset of companies, obtained from the survey of executives suggests that in most companies, the major source of new products ideas is the top management. These efforts are supplemented with analysis of foreign technology/ products or competitors’ products. Seldom do companies obtain idea for new product launches from consumers. This is not surprising since the extent of utilization of market research for new products development. The picture then becomes clearer for new product opportunities; companies depends either on the secondary technology available in some markets. There is hardly any serious and systematic effort to understand consumer's needs and requirement in the context of competing offers and naturally the market opportunities thus imagined to have existed turn out to be here mirages!

Failure in Integrating Customer's Choice / Ideas in New Product Offering

Consumers do not pay for mere ideas; they only buy tangible offers that satisfy their needs. Companies, therefore, need to translate their brilliant ideas for new brand sand products into tangible offers that spell out the specific benefits that the new offer will provide, the needs that they will satisfy and the cost that the consumers will have to bear. This phase of transforming new ideas into tangible and viable market offer is very critical stage and is perhaps the stage where the firms commit major resource. But then can any firm take such major decisions without an assessment of likely consumer acceptance of the proposed new offer? In reality, unfortunately, many firms do not seem to be marking sufficient efforts in assessing consumers' reaction abut the new proposal and thus estimating the risks involved before investing huge resource to develop new offers. Further findings of the study suggest that 44 per cent of the firms do not carry out a formal concept testing and another 30 percent do it only occasionally. Data further suggests that 53 percent of the companies never or seldom make a per assessment of the financial viability of the proposed new products/brand before proceeding further with introduction plans. These indications suggest that many a firms let pass occasion's access consumer preference carefully and fine-tune their proposal to reflect the value propositions of consumers. They slides over issues like leverage strengths of brands and appropriateness of equity of the brand for the proposed new product. Many a times firms even underplay the question as to whether or not the whole scheme makes the commercial sense. Given such limited in sight in to the likely future potential of the new venture, companies end up courting disaster. In fact, many sad endings could have been averted if only companies showed little more diligence in assessing consumer reactions to the new proposal and estimating commercial viability before making major resource commitments.

Failure In Product Testing

If the core product that you are offering to consumers does not provide the functional benefits that it is intended to provide, then no amount of advertisement and publicity can salvage the situation. Therefore, it is extremely important to ensure that the basic product meets consumer requirement. Research data revealed that nearly 56 percent of companies do test their products either frequently or almost always. Out of the remaining, 44 percent either never or rarely test their products. In all probability, the proportion of your offer, you do not have much to worry. However, even a good product will not survive if it needs to be made either before the invest in manufacturing and/or later. Many new brand failures in India today are more failures of concept rather than failures of basic product. This observation suggests that you not only need to test the product to ensure that the functional performance under the laboratory as well as field conditions is satisfactory, but also it does address the felt needs of consumers better than competitors. This is also an activity, which will provide valid inputs to assess the likely market acceptance of the proposed new brand by way of volume prediction. This input certainly helps in assessing commercial viability of the proposal. Research findings suggest that most of the firms carry out some financial analysis at this stage.

CREATIVITY IN NEW PRODUCT DEVELOPMENT

Consider a recent transformation at Procter & Gamble. Once a hotbed of creativity, P & G had in recent years seen the number of its product innovations decline significantly. In response, the company established Corporate New Ventures, a small cross-functional team that embodies creativity – enhancing practices. In terms of challenge for instance, members of the CNV team were allowed to elect themselves. How better to make sure someone is intrinsically motivated for an assignment than to ask for volunteers? Building a team from volunteers, it should be noted, was a major departure from standard P & G procedures. Members of the CNV team also were given a clear, challenging strategic goal: to invent radical news products that would build the company’s future. Again departing from typical P & G practices, the team was given enormous latitude around how, when and where they approached their work.

In the three years since its inception. CNV has handed off II projects to the business sectors for execution. And as of early 1998, those products were beginning to flow out of the pipeline. The first product, design to provide portable heat for several hours relief of minor pain, was already in test marketing. And six other products were slated to go to test market within a year. Not surprisingly, given CNV’s success, P & G is beginning to expand both the size and the scope of its CNV venture.

a. Flexible Product Design for New Product Development

Product design is fast emerging as a force in the new ICE – age economy – for Internet devices, Websites, office equipment and even household gadgets. All these technological changes are reducing the product life cycle and bringing in more and more design innovation. The market that has taken most of the beating is an electronic gadget, be it computers pocket devices or phones. Trendier, more vibrant than the earlier versions, they are getting smaller too. The shift towards sleek devices has come from the need for physical mobility, something that is crucial with almost all these gadgets. Studies indicate that the shift has more to do with analysis on human interaction with the devices. Product designs, today, focus on aspects of functionality, unlike the time when designs were incorporated to have a product extension in the market. The best product example to describe this is the hands- free option that most third generation cellular phones carry. Whether it is as simple as a pen or as complicated as a keyboard that can be folded and carried in the pocket, design is changing the way products are looked at. Another field that is witnessing a lot of design change is pharmaceutical and medicine and medical equipment. With new technological improvements and design innovations, one gets to know his or her blood pressure with a guage attached to one’s watch. The watch gives out danger signals each time the pressure varies beyond the specified standards. It is amazing how quickly designers are able to conceptualize designs that are then incorporated into products. With designs playing such an important role in product differentiation, design specifications will change beyond imagination – soon.

Product design, the painstaking process by which prototypes are developed and specifications are created and implemented in actual production, is an integral part of any business strategy. For the process to work effectively, every aspect of each activity related to the product and its life cycle must be taken into account. These include supplier involvement, customer involvement, manufacturability, cost, time, management, usability, marketability and disassembly or recyclability. With such wide-ranging elements coming to play, a well – thought out design can provide a company with the competitive edge needed for achieving greater profits and higher market share. Organizations are always looking for better ways to design products. Intel, for example, has emphasized design ethnography, which focuses on understanding the customer and the culture in which a product is used. The world wide web is increasingly used for product design activities such as finding information on parts and materials, sharing designs among people, automating design sign-off's and linking geographically dispersed designed teams.

Majority of Chief Executives believe that design issues will be of increasing competitive importance in the coming years. Many product failures – even those by otherwise successful companies – might have been avoided if better product design methods were used. Author Tom Peters coined the phrase "design mindfulness" to refer to the benefits of a committed creative, an energetic focus on great design.

b. Integrating Consumer and Designer Preferences

Improved product design can be achieved by taking the viewpoints of both designers and consumers into account. In conventional product design, the marketing department sends consumers preferences to the designer, who then creates a design to meet those preferences. A delicate balance must be struck between the struck between the consumer and the designer since plans based solely on consumer preferences may be unfeasible or unrealistic. Designers acting alone, on the other hand, may come up with a product that is a technological marvel, but that consumers see as silly and unusable. Consumer's decision-making processes are not perfect and may given an inaccurate picture of preferences. They often think in terms of abstract goals that are difficult to translate into product features. A lack of expertise or incomplete consideration of alternatives can also lead consumers to make choices based on vague preferences, rather than considering ways to realize concrete operation benefits that would realized with greater experience and exploration.

Designers can make up for some of the short-comings of consumer input, since they usually understand more about future technologically possibilities and look at a longer time line. They are also in a better position to know that competitors might offer. For example, consumers may desire a "user – friendly" personal computer that is easy to get started with, but the designer realizes the computer should also meet longer – term needs. Therefore, designers should have the freedom to create innovative product designs that not only meet current user requirements but are also up to the demands of future consumer expectations. This give and take requires a delicate balance between designers and consumers since research has shown a high correlation between inadequate feedback from users and the failure of a new product containing technical innovations.

c. Striking a Balance between Consumers and Designers

The way a consumer looks at product attributes is usually much different from the way a designer looks at product "characteristics". For example, a consumer may want a boat to be fast, but a designer looks at characteristics that affect the speed of the boar, such as engine size and full shape. A distinction can be made between product characteristics and attributes: Product characteristics physically define the product and influence the formation of product attributes; product attributes define consumer perceptions and are usually fewer in number and more abstract than product characteristics.

Past product design research has focused on optimization with respect to either consumer attributes or designer characteristics. However, both the consumer and the designer will benefit from a balanced design. Plans based solely on consumer attributes ignore the relationship between attributes and characteristics; using only designer characteristics inadequately accounts for the consumer's preferences. A better approach to product design would account for the relationship between the two. In other words, what design characteristics would bring about the desired consumer attributes? In short, translating consumer attributes into the appropriate and corresponding design characteristics can optimize product design. This is the great benefit of multi-source product design: it optimizes both sides of the equation simultaneously.

13.5 THE FUTURE OF NEW PRODUCTS MANAGEMENT

In the new millennium, we are seeing more segmentation there will be even more competition for almost everyone than there is today; and life cycles of products will continue to get shorter or stay short. Similarly, most of the forces acting to increase the costs of innovation will remain high or will increase. In most instances productivity will increase as all producers focus so intently on it as the path to lower costs and higher-quality product. On the positive side, three forces acting to at least partially forces acting to at least partially offset the negative forces described above. All three of these positive forces will get stronger, not weaker. The first, technology, is the strongest of all it can and that there is little left to invent, we know that this simply not so. Computerization, automated manufacturing, molecular biology, fiber optics and surface ceramics are just a few of many fields that offer what almost certainly will be more technological opportunities in the next 25 years than in the past 50. Molecular biology has the potential for outstripping anything else done so far in this century. Moreover, there is an amazing move to invest large sums of money in older technologies, especially in the so-called mature industries. And as a final plus international opportunity continues to grow and contribute new markets, new skills and new concepts of management.

The second positive force is the general willingness of consumers to accept new items – otherwise there is absolutely no basis for forecasting. And third, management's general capability has been growing almost exponentially, particularly by taking advantage of the many MBAs entering the work force and the wide array of continuing education opportunities for managers today. The combined results of these negative and positive forces are mixed, of course, but the negatives had no perceived effect on the development and marketing of home video systems or on the development of new drugs in recent years.

SUMMARY

The general environment of social, economic and other forces seems to favor the continued viability of new products activities. At present no environmental force on the horizon has the power to blunt the force of product innovation. The leading on is the attitude of firms and their managements toward new products. More companies will eagerly seek such products and their searches will be more vigorous. Due primarily to (1) the interest in strategic market planning, (2) the subsequent growth in portfolio analysis and (3) marketing planning by individual business segments, more and more managements have come to see the dangers. The second force that will act directly on the motivation of new products managers is customer lifecycles – both consumer and industrial. In total, the above set of forecasts paints the following picture.

1.There are many basic new needs – an ever-growing number of them, amid an ever-growing population, with ever more money to spend.

2. Technology is fully capable of meeting many of this needs-never have we had find had the immediate technology potential that exists today?

3. And never have we had such knowledge and sophisticated new products profession and such industrial capability. We do indeed know how to develop new products successfully. Given trained individual as working in corporate environments that provide the conditions known to be effective output, the only reason for a new product failure is deliberate circumvention of correct procedure.

In summary regarding the new product process, we should expect that failure rates would fall, that budgets will be up and that there will be better all-round performance as expertise is build up both inside and outside the firm.

QUESTIONS

1. Define a new products
2. What do you mean by technology / market matrix?
3. Explain the source of new products idea
4. Describe major components of business creativity
5. What do you men by concept development
6. Discuss the detail business creativity will help IT products managers in India
7. Explain the significance of new products development in India
8. List major steps in new products developments
9. Explain the significance of new product management. Explain the reason for failure and give your suggestion for improvement to India manager
10. Classify new products and explain how business creativity technology and markets positioning will help the new products managers to click success in India
11. Want do you mean by concept testing? How do you test an IT products like people soft for Indian managers
12. Explain products innovation. Describe the important of innovation for gaining competitive advantage in FMCG – consumer durable say, air conditioner in India.

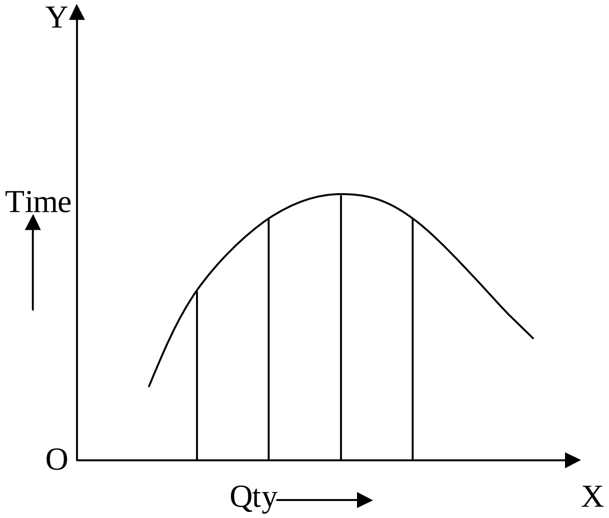
2.6 THE LIFE CYCLE OF THE LESSON

Overview

Many products generally have a characteristic known as perishable distinctiveness'. This means that a products, which is distinct when new, degenerate over the year into a common commodity. The process by which the distinctiveness gradually disappears as the product merge with other competitive degeneration. The cycle begins with the invention of a new product and is often followed by patent projection and further development to make it salable. This is usually followed by a rapid expansion in its sales as the products grains market acceptance. Then competitors enter the field with imitation and rival product and the distinctiveness of the new products. While some products fail immediately on birth or a little later, other may live long enough BPL's picture in pictures TV was eliminated and the introduction stage itself. This lesson focuses exclusively on the PLC of various products and its implications for managers in detail.

The Concept

The innovation of a new product and its degeneration into common products is termed as the life cycle of products is termed as the life cycle of products. There are five distinct stages in the life of products as shown below:



a. Introduction: Research or engineering skill leads to product development. The product is put on the market; awareness and acceptance are minimal. There are high promotional costs. Sometimes a product may generate a new demand, for example, Maggi, Volume of sales is low and there may be heavy losses.

b. Growth: The product begins to make rapid sales gains because of the cumulative effects of begins to make rapid sales gains because of the cumulative effects of introductory promotion, distribution, and word of mouth influence. High and sharply rising profits may be witnessed. But to sustain growth, consumer satisfaction must be ensured at this stage.

c. Maturity: Sales growth continues, but at a diminishing rate, because of the declining number of potential customers who remain unaware of the product or who have taken no action. Also, the last of the unsuccessful competing brands will probably withdraw from the market. For this reason, sales are likely to continue to rise while the customers for the withdrawn barads are mopped up by the survivors. There is no improvement in the product but changes in selling effort are common. Profit margins slip despite rising sales.

The following table shows the product life cycle and its different stages and the various characteristics, which they reflect, in the varying stages:

PCL Elements	**Introduction**	**Growth**	**Maturity**	**Decline**
CHARACTERISTICS				
1. Sales	Low	Fast Growth	Slow Growth	Declining
2. Profits	Negligible	Peak Level	Declining	Low
3. Cash inflow	Negative	Moderate	High	Low
4. Competitors	Few	Growing	Many	Declining
5. Customers	Innovative	Mass Market	Mass Market	Laggards

Source: Peter Dayle, “The Realities of the product life cycle”, Quarterly Review of marketing, summer 1976

Pattern of Growth – A Life Cycle Analysis for New Products

Even then the existence of initiative products/services and the emphasis of management on such products cannot be ignored. This may be due to the recognized marketing gap hitherto unfilled by the existing producers, product deficiencies and identified consumer dissatisfaction with available products in the market.

The super cautious attitude of management towards innovation, which may be due to fear and high cost of product failures, may also be a reason for increased emphasis on imitative new products. Just like a human being pass through different stages of the life cycle, a product in the market should also different stages of the life cycle a product in the market should also pass through different stages from introduction to decline and possible abandonment.

The concept of the product lifecycle indiscriminately applies both to innovative and imitative products. The noted stages of a product's life cycle include introduction, growth, maturity and saturation, decline and possible abandonment. He challenges and characteristics for innovative product imitative new product in their respective product life cycle stages are analyzed here.

The strategies for meeting these challenges, at each stage of the life cycle for the respective products are also discussed.

DIFFERENT STRATEGIES

Innovative and imitative products require different kinds of marketing strategies. Right from the embryonic stage of product development, these differences in dealing with innovative and imitative new products are noticeable. For instance, a new brand of soap, toothpaste, scooter or car is an imitative new product; on the other hand, a flying car or scooter is an innovative product. Imitative new products have to overcome the existing competition to establish them in the market. But in the case of innovative products prospective and not the present competition is a challenge.

a. Introduction and Growth Stage

The introduction stage of the product life cycle is the entry of the product in the market. Generally, in the earlier days of introduction, because of the product is known and its positive characteristics are less known to the consumer, sales or less. Even though there is increase in sales, it is at a slow place. The ease of introducing a product depends on the degree of its novelty, improvements over the existing products, distinctiveness and a host of other factors. Innovative products can be introduced in the market with relative competitive ease because there is no competition to be broken. This is much easier if the product has with a highly technical or utilitarian aspect. But for imitative products it is difficult even to enter the market under competitive conditions. No doubt, the degree of this difficulty is much influenced by the extent of market satisfaction number of existing rival products and the marketing and product advantage they offer to the customer.

Generally, the prospective consumers for a newly introduced product is already selective in his nature. Therefore new imitative products should have some step-up features and marginal improvements so as to divert the attention, affiliation and loyalty of the consumer from the already existing alternative brands in the market. But in the case of innovative or really new products, convincing the consumer about the product's marketing advantage or utility is enough to find a place in market. However, the initial positioning of the products should be on sound lines with a long run competitive perspective, so as to be less vulnerable to the competitor's strategies.

The introduction stage of any product is generally charactersied by low sales volume, limited distribution and high costs of promotion. These may be common to a great extent for innovative and imitative products. But with respect to promotion strategy, for truly innovative products the main objective is primary demand creations, whereas it is secondary demand for imitative products. In other words, due to the real newness of the product appeal to the consumer rather than bran appeal as in the case of imitative products .on the other hand, where the existing products dominate the market, imitative products as new entrants should try to snatch away the market of other products and thus establish their share of the market.

The success of innovative products in the introducing phase depends largely on the promotional efforts and their positioning. But the success of imitative products is conditioned by the extend of competition, the existing competitors, strength and quality of their products, offered to the consumers through promotion and the life stage of the exiting products. The duration of the introduction stage for innovation is generally less, provided the products are effectively and extensively promoted.

Moreover, the number of possible product failures is also less with respect to an innovative product. Because the direct competitive forces are absent the internal marketing effort and efficiency is the major deciding factor for the product's success. On the other hand, the imitative products often fail because of the competition and counter market strategies by the existing competitors.

Therefore, imitative products, which enter the growth stage should try to counter the marketing efforts of the marketers and at the same time develop a good image and a competitive edge by capitalizing the weakness of the existing products. The intensity of competition will also differ in this stage for innovative and imitative products should plan for product improvement or finding new uses for the product.

Thus the marketer can maintain his competitive edge and retain his distinction and market market share. The duration of this stage of product life cycle may also vary in both cases. Imitative products, unless they are highly distinctive, of better quality and exceptionally appealing to the consumers, have a short span of growth stage. On the other hand, ceteris paribus, innovative products are likely to stay in the growth stage for a longer period because they take considerable time for the imitators to come up with their own versions of innovative products.

b. Maturity and Saturation Stages

Once the product passes through the growth or market acceptance sage in due course, it enters the maturity stage followed by saturation. The former is characterized by increase in sales but at a low rate and the alter by stagnation in sales. The maturity stage in a product's life cycle is characterized by increasing sales and profit, but the rate of increase is less than that in the growth stage. This reduced growth rate is certainly due to imminent competition in the market. Here one should not forget that innovative products face competition from new and improved imitative market entrants from time to time, whereas imitative products have to content with existing products. When the question of guarding against the phenomena of maturity and saturation stages arises a clear forecast of the setting in of these phases is essentially required. Otherwise, designing of effective marketing strategies to prevent the early setting in of maturity and saturation is not possible. Sometimes, if the products sales are close to the break-even levels, losses become inevitable especially in the saturation stage.

Moreover, there may be a drop-out of the products at this stage if actual sales fall below the break-even levels. In order to prevent such as eventuality, strategies such as product improvements, price reductions, effective advertising and sales promotion activities should be intensified. When compared to imitative products, innovative products, generally experience a longer span of maturity and saturation stages. This may be due to the early life cycle or the introduction stage of competing products and consequent less competition; or the competing and newly emerging imitations of the innovative products may have a low level of consumer acceptance. Moreover, innovative products may have a scope to adopt improvements through planned obsolescence when their imitations try to emerge a strong product in the market.

The strategy of systematic and timely planned untouched, potential segments of the markets and a number of other such strategies are quite significant to prevent the early entry of the product in to the decline stage. Especially, innovative products should not go for planned obsolescence before the entry of vital competitors with their own imitative versions. And growth so as to reserve it for maturity and saturation to revitalize the life cycle curve.

Just like any human being enters into the life cycle phase of inevitable physical deterioration and death, products also do enter into the stage of decline and possible abandonment. How fast a product approaches this stage is dependent on the marketing environment, market forces, product characteristics, and competitive strengths of the product and extent of product differentiation. As the new products enter the market, from time to time, virtually all the products enter the market, from time to time, virtually all the products are certainly caught in the clutches of obsolescence.

When the competing products establish their firm footing and consolidate their position in the market, the earlier entrants to the market fall prey to the clutches of decline. If a product, either innovative or imitative, stays in the saturation stage competitors try to aggravate their promotional effort to establish their superiority and push the innovative product to decline and consequently to the wall. How far a product can withstand the threat of the decline and curse of obsolescence depends on the managerial efficiency, efficiency of the marketing management and product strategies.

This stage of any product’s life poses challenges to the management. In this stage, the competitive strategies of promotion, re-pricing and repositioning are warranted to inject a new lease of life to the product. No one should be left unturned to revitalize the product lifecycle. For a successful revitalization, every effort to maintain the morale and loyalty of middlemen to carry out the product on their shelves as against those competitors is highly significant.

Strategic Considerations in the PLC Concept

a. Competition

At the introductory stage, competition is given no important the growth stage, it is given a little important while at the maturity stage, there are many in the market slowly, however, the number of competitors or rivals gets reduced with the declining srage.

b. Over all Strategic Focus

At the first stage, emphasis is laid on market establishment. At the growth stage, market penetration and persuasion of mass market are emphasis. Creation of brand loyally and brand preferences is focused at the maturity stage. At the decline stage, the strategy aims at overall preparation for renewal.

c. Profit

At the introductory stage, profit are negligible but all the growth stage, they reach the peak levels as a result of growing demand. At the maturity stage, they decline due to the increasing competition. At the last stage, the declining volume pushes costs up and eliminates profits.

d. Distribution Strategies

At the introduction stage, distribution is selective. However growth and maturity stages, it is intensive. At the decline stage, it becomes selective and hence low-end strategies are used.

e. Advertising Strategies

At the introduction stage, advertising strategies aim at the needs of early adopters; at the growth stage. An attempt is made to make the mass market aware of brand benefits. At maturity stage, advertising is used as a vehicle for differentiating among otherwise similar brands. At the last stage, however it emphasizes, on low price of the product and minimum advertising expenditure.

CASE STUDY

Kellogg’s

Kellogg the $ 10 billion Michigan – based food major, is knocking at corporate doors. Retails strategy did encourage consumers to try cereal for breakfast, but it was painful slow going. If what Kellogg’s Indian subsidiary is doping in Delhi is any indication, the company seems to have settled on an alternative route of the consumer’s palate. It’s abandoning its breakfast plank in favour of round the clock consumption and not just at home either. As a part of its new strategy, k0lloss India recently installed cereal dispensers in 120 odd officers in Delhi. The results have encourage the company to contemplate similar efforts in other metros, even as it expand its chain of dispensers in Delhi officers. At a details off-take of 4-5 kg per office per day (which amount to over 100 helpings a day) this could be just the tip of the iceberg for Kellogg's. the new strategy is in line with current trends, with companies emphasizing health consciousness, the time is right for Kellogg to perk up and get in on the action.

For years, Kellogg's been focusing on retail marketing and new products launches, without any significant breakthrough. Its small sachet initiative early this year didn't make a significant impact either. With no fresh infusion of investment from the parent in sight, the Indian arm clearly had to manager on it own. This is one step in that director. In marketing you've to do a 360-degree job, explain R.C.Venkateish managing director. Kellogg India." You just can't afford to bombard the consumer with products and communication and relax, hoping that she will lap them up", he says. For the last eight years Kellogg had done just that. Now it wants a more calibrated approach to new products a launches and consolidate gains it's made for. The key lies in expanding penetration fro home to out-of-home situations, while increasing more occasions to eat the products. And by targeting offices Kellogg is trying to do just that. Kellogg roped in solutions, a Delhi based marketing consultancy, for the track. The mandate was to see how best the consumption of Kellogg cereals could be perked up. Solutions, along with Kellogg's three – member marketing team, decided to test the concept of snack junction Kellogg as a snack for office staff. "Snack because there are many more opportunities for the consumer to pick up snacks through out the day", says Kanika Mathur **COO** and director, solutions.

The 'healthy breakfast' plank had restricted space for Kellogg to operate. With the traditional 9to 5 officer culture going out of fashion corporates seemed to be the obvious target to test the concept, especially as most companies are now willing to provide employees as much facilities as possible within the office itself. Solution shortlists around 1,000 large companies to start with and its 30-member team fanned out t sell the idea. The customer includes **MNCs** like whirlpool, Electrolux, Coke, Samsung, Amex; call center like spectramind and consultancies like PWC and KPMG. According to a KSA grow fast study, there are over one-lakh officers in Delhi with 50 or more employees. And for 50 employees, an average company spends Rs.6, 000 - 8,000 per month on test and coffee alone. At a cost of Rs.4,000 – 5,000 per dispensing unit (depreciable and to be written off), payback for the new approach seems pretty attractive. It's created much needed awareness for a concept that's much in nature", says Mathur. The company is capitalizing on this excitement by poster campaigns at the 'snack junction' within the site. The exercise has helped Kellogg increase visibility, generate trails, which weren't quick in retaining alone and make it popular.

SUMMARY

Introduction

The seller tries to stimulate demand promotion campaigns to get increase public awareness. Explain how the product is used.

Feature, Advantage, Benefits

You will lose money, but you expect to make profits in the future Sales are low, and profits are below the line because your costs greater than the amount of money you make You have "negative" profit Need to spend a lot of money on promotion

Growth

A lot is sold- the seller tries to sell as much as possible other competitor companies watch and decide about joining in with a competitor product "success breeds imitation". Growth will continue until too many competitors in the market – and the market is saturated.

At the end of the growth stage, profits starts, profit start to decline when competition means you have to spend more money on promotion to keep sales going.

Spending money on promotion cuts into your profit.

Maturity

Many competitors have joined-the market is saturated. The only way to sell is to begin to lower the price – and profits decreases. It is difficult to tell the different between products since most have the same F.A.B. – features & Benefits. Competitions can get "nasty" and commercial are intense.

Decline

Newer products are now more attractive – even a low price does not make consumers want to buy. Profit margin decline – and so the only way to make money is to sell a high volume. To increase volume you try to.

1. Increase the volume number of customers – get new customers
2. Increase the amount each customer uses.

Speed of the PLC

Since the intro stage is getting shorter and something the growth stage doesn't last too long (because competitors move in) companies must continually come up with new products.

You can tell when they are in growth stage because this is when there introduce new model variations and some improvement to the products.

Products Life Cycle Considerations In Marketing Strategy

Understanding that profits have a predictable pattern

In the early stages, focus is on products information

In the later stages, focus is on brand promotion

Use market segmentation in maturity stage to maintain strong core customer basis.

QUESTIONS

a. Define products life cycle of a ladies garment, say a royal jeans from lifestyle
b. What do you mean by maturity stage in PLC?
c. Explain the PLC of new product.
d. Describe major strategic consideration in PLC.
e. Explain the significant of PLC for managers.
f. What do you mean by products life cycle? How do you develop PLC for an IT product like SPSS?
g. Describe the important of PLC for gaining competitive advantage in FMCG – consumer durable say, personal computer in India.

UNIT – III

Lesson 3.1

Pricing Decisions

Objectives

In this lesson, we will introduce you to the 2nd *P* of marketing – Price. While the other 3 *P*s represent costs, this element in the marketing mix produces revenue. After you work out this lesson, you should be able to:

- Appreciate the importance of pricing decision
- Identify the considerations that come to bear on pricing decisions
- Understand why customers may be price sensitive

In this lesson, we will discuss the following:

- Product costs
- Customer value
- Elements in the pricing decision

Introduction

A price is an expression of value. The value rests in the usefulness and quality of the product itself, in the image that is conveyed through advertising and promotion, in the availability of the product through wholesale and retail distribution systems, and in the service that goes with it. A price is the seller's estimate of what all of this is worth to potential buyers, recognizing the other options buyers will have for filling the need the product is intended to satisfy. To the extent that the product or service finds markets and is profitable at given price levels, it provides a viable economic base for building and maintaining a business.

In the competitive marketplace, pricing is a game. The struggle for market share focuses critically on price. Pricing strategies of competing firms, therefore, are highly interdependent. The price one competitor sets is a function not only of what the market will pay but also of what other firms charge. Prices set by individual firms respond to those of competitors; they also are intended often to influence competitors' pricing behaviour. All of marketing comes to focus in the pricing decision.

A way to think about making a pricing decision is that price should be set somewhere between what the product costs to make and sell and its value to the customer. If price exceeds the perceived value of the product to potential purchasers, it has no market. If the price is below what the product costs to produce, the business cannot survive for very long. Where a price should be set between cost and customer value is a strategic decision. Many factors can influence this decision, viz., competitors' product/price strategies, governmentally imposed constraints and the seller's and the buyer's sense of what is fair. Finally the most important determinant of price is the marketer's objectives – what is the firm trying to do. The discussion on pricing objectives is taken up in the next lesson.

Product costs

Costs may be classified as variable, fixed and semi-fixed. Take the case of an airline. It may consider the annual depreciation on an aircraft as a fixed cost. Taking the plane off the ground to fly from one city to another incurs certain semi-fixed costs like the fuel, the compensation of flight personnel, the airport fees and so on. These costs are approximately the same for any given flight whether the plane is empty, half-loaded or completely full of passengers. The variable costs of the flight would include primarily the costs of food and beverage. They vary directly with the number of passengers.

If fixed and semi-fixed costs make up a larger portion of total costs, as in the airline example, pricing to get maximum capacity utilization is crucial. Until the seller covers fixed costs, money is lost. After fixed costs are covered, each incremental sale contributes proportionally large amounts to profits. If variable costs are a relatively high percentage of total costs (which is quite likely in many manufacturing firms), pricing to maximize unit contribution (i.e. the difference between the unit variable cost and price) will be critical to profitability. Under these cost conditions, the manufacturer would naturally work to maximize unit prices and to reduce variable costs.

Above are two examples. In the first one, the objective of the airline's pricing strategy will be to generate enough total revenue to cover its fixed costs and above that to get maximum capacity utilization to make profits. In the second one, a manufacturer will price to cover its high variable costs per unit and get enough contribution to amortize fixed costs and make a profit.

Under certain conditions, firms may elect to price at less than full cost. In conditions of capacity underutilization, for instance, firms with high fixed costs may take business at prices that cover variable costs and make some incremental contribution to fixed costs (or overheads). The idea is to get through bad times, keep the factory running and hold some critical team of managers, skilled technicians and labour.

Pricing temporarily at less than full cost may also be used as a strategy to get a particularly large order. The expectation is that by taking the business, the firm may be able to reduce its unit costs and/or later raise its prices so as to make a profit on subsequent orders. Taking business below cost with the hope of offsetting near-term losses with longer-term profits may be a risky tactic, since there is no assurance that the losses can be made up.

Pricing near or below cost may also be done to gain a large market share. Generally pricing low to preempt market share is predicted on the assumption that unit costs will come down significantly as volume increases. This may happen through gaining manufacturing experience. In fact, in many firms, a so-called experience or learning curve is used to calculate what the effect will be of volume growth on unit costs. To a large extent, learning curve experience reduces the variable cost component of unit costs. Labour gains in efficiency and purchases of materials and parts in larger volumes all result in lower prices and manufacturing process improvements produce cost savings. Indeed, the fixed-cost component of unit costs may also come down with volume increases. Larger plants may be more cost efficient. Large-scale selling and advertising programs may also be more cost efficient. If product sales are particularly sensitive to heavy advertising, or the product requires widespread distribution or extensive field service support, fixed marketing expenditures for these purposes must usually be at a high level.

These so-called *scale economies* come in certain cost categories depending on the product, the processes used to manufacture it and the level of marketing spending required to be competitive. If significant scale economies are achievable, some competitors may be willing to price low enough to gain volume, thus preventing other competitors from going down the learning curve and hoping to emerge as low-cost producers with dominant market shares.

Product cost, then, is not a simple ‘hard’ number. How cost is calculated for pricing purposes is a matter of managerial judgment. It may be construed as full cost or as variable cost. It may be the cost levels being experienced or experience curve estimates of future costs. The interpretation of cost factors for pricing will depend greatly on product/market objectives.

Customer value

Some business managers set prices simply by adding a percentage over costs to provide an acceptable profit. That approach has two advantages. Price is simple to calculate and if a firm is a low-cost producer, relative to competitors, so-called ‘cost-plus’ pricing may seem to provide some protection from competitive attack. The trade-off for simplicity and security may be lost profits. In theory, the amount of profit that is sacrificed is the difference between what customers actually paid and what they would have been willing to pay. Compared with cost-plus pricing, pricing according to the value of the product to the customer is more difficult and speculative. The challenge is to determine what the value of the product is in the customer’s mind.

First, it is useful to distinguish between perceived value and potential value. Perceived value is what the buyer now recognizes. Potential value is what the buyer can be educated to see in the product. That is the task of marketing. It may be accomplished through advertising, personal selling and getting the buyer to try the product.

Second, product value may be perceived differently by different customer groups or market segments. Different segments may place different values on the several elements that make up the set of product (which in the broadest sense, includes the product or service itself, its brand image, its availability, and the service that the seller provides) attributes. For example, a large firm may place little value on the technical service a supplier offers it (the large firm) has comparable or superior technical resources of its own. But a small company may be highly dependent on the supplier’s technical services and place high value on them in making purchasing decisions.

A third factor to consider in establishing customer value is the options that a potential buyer may have. Clearly, if the buyer can purchase a product at a lower price from one source than another, the lower price sets the upper bound in the marketplace. But for the buyer to have such effective options, he/she must have knowledge of them.

Another option the customer has may be not to buy the product at all but to make-do with what one has. Given this choice, the buy-not buy decision may be made by comparing the outcome of one course of action with the other.

These actions are quantifiable. One may calculate the operative savings in either instance and relate this to the cost of buying new, as the case may be. The anticipated savings may be expressed as a percentage return on investment (ROI). This, the amount of realizable savings establishes the value of a product to the customer. Calculated for each of several possible uses for available funds, ROI measures may serve to establish the buyer's purchasing priorities. The choice between buy-not buy, of course, may not always be easily quantified with reference to expected savings. Nevertheless, it is a real and important consideration.

Finally, the price set by the seller is often taken by the potential customer as one measure of the value of the product. It is often interpreted by buyers as the supplier's estimate of the worth of the product it sells. If the seller does not value the product highly, it is not likely that the buyer will. Therefore, pricing a product significantly below what the buyer might pay for its functional equivalent can be self-defeating. The buyer may infer that value is, in fact, connoted by price and choose the higher-priced option.

Value, then, for a given product tends to be a function of (1) the utility of its several attributes to the prospective buyer, (2) the options the buyer has and is aware of (i.e. the offerings of competing suppliers and the option of not buying at all), and (3) the extent to which the buyer perceives price itself as a measure of product value.

If the seller truly value-prices, then different prices would be charged for the product to different customer groups. It is referred as price discrimination. A relevant consideration in thinking about price as an expression of product value is how sensitive is the buyer to price. Price sensitivity will vary considerably among purchasers and, for the same purchaser, it will vary from one time and one set of circumstances to another. Buyers who can pass on the cost of the purchase are less sensitive to price than those who cannot. Price sensitivity also relates to the performance standards by which the purchaser measures. Viewed differently, performance measures effectively establish the relative worth of different product attributes for the manager who has to make the decision and be judged for it. Another factor in price sensitivity is the uncertainty that attends switching from one supplier to a lower-priced source. Modest price differences are often insufficient to overcome the purchaser's uncertainties about an untried supplier's product quality, reliability and service.

Factors affecting price decisions:

There are a number of factors which influence the pricing decisions of marketers. While some of these are external or environmental factors (such as competition, demand conditions and so on), others are internal factors (like marketing objectives, cost conditions and so on). Figure 3.1.1 represents these factors. The important factors affecting the pricing decision are the following.

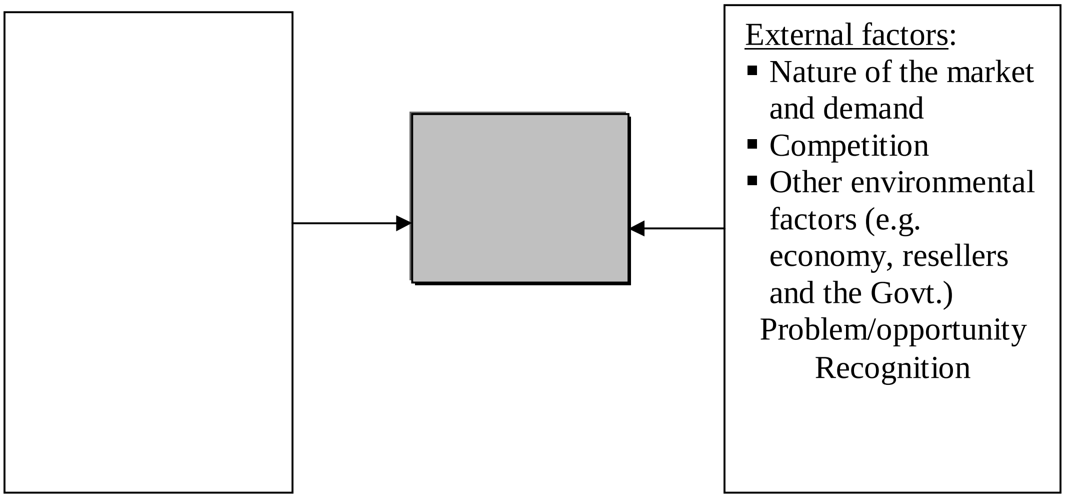

External factors:
Nature of the market and demand
Competition
Other environmental factors (e.g. economy, resellers and the Govt.)
Problem/opportunity Recognition

Figure 3.1.1 Factors affecting a firm's pricing decision

Internal factors: The internal factors, as the term implies, are mostly internal to the organization and therefore, largely controllable by the organization. They also have a direct bearing on the firm's pricing decision. The following are the important internal factors that must considered in pricing a firm's product/service.

- Marketing objectives – Before setting price, the firm must decide on its strategy for the product. This reiterates the idea that the corporate strategy must precede the marketing strategy and then marketing strategy must precede the pricing strategy. If the firm has selected its target market and positioning carefully, then its marketing-mix strategy (i.e. the 4 *P*s) will be fairly straightforward. For example, if the Coimbatore-based Paramount Airways decides to target the corporate/business travelers with its single-class airplanes, this suggests charging a high price. Whereas, a no-frills, low cost carrier would charge a low price, as dictated by its targeting and positioning. Thus pricing strategy is largely determined by past decisions on marketing strategy. At the same time, the firm may seek additional objectives. The clearer a firm is about its marketing objectives, the easier it is to set price. Some of the common objectives include survival, current profit maximization, market-share leadership and product-quality leadership.

- Other objectives – Sometimes a firm might set prices so low as to prevent competition from entering the market as they might lead the competition to regard the market as less attractive. Non-profit organizations may adopt a number of other pricing objectives such as full cost recovery, partial cost recovery or set a social price geared to the distributed income situations of different clients.
- Marketing-mix strategy – Price is only one of the marketing-mix elements that a firm uses to achieve its marketing objectives. Therefore, logically pricing decisions must be coordinated with product design, distribution and promotion decisions to form a consistent and effective marketing program. Decisions made for other marketing-mix elements may affect pricing decisions. For instance, the decision to position the product on quality plank will imply that the seller must charge a higher price to cover higher costs and/or to match the price-quality perception in the mind of the customers. It is common for marketers to design a price position wherein a target cost is set, then met and the target price is set. However some marketers deemphasize price and use other marketing-mix elements to create non-price positions. The marketer must consider the total marketing mix when setting prices. If the product is positioned on non-price factors, then decisions about quality, promotion and distribution will strongly affect price. If price is a crucial positioning factor, then price will strongly affect decisions made about the others marketing-mix elements. In most cases, the

company will consider all of the marketing-mix decisions together when developing the marketing program.

- Costs – Though this topic was dealt with earlier in this lesson, some finer aspects related to costs are described here. Costs set the floor for the price that the firm can charge for its product. A firm's costs may be an important element in its pricing strategy. The firm wants to charge a price that both covers all its costs for producing, distributing and selling the product and delivers a fair rate of return for its effort and risk. The types of costs were explained earlier. To price wisely, managers need to know how costs vary with different levels of production. The concept of economies of scale comes into play here. Also, costs vary as a function of production experience. There is a drop in the average cost with accumulated production experience and this is attributed to the experience curve or the learning curve. Consider the semiconductor industry as an example. It has a strong experience curve effect. As a given chip is produced, manufacturing speeds go up, defect rates drop and costs plummet. These effects are seen dramatically in the PC market, where computing power increases and costs drop every year.
- Organisation for pricing – Management must decide who within the organization should set prices. Firms handle pricing in a variety of ways. In small firms, prices are often set by top management rather than by the marketing or sales departments. In large firms, pricing typically is handled by product line managers. In industrial markets, salespeople may be allowed to negotiate with customers within certain price ranges. Even so, top management sets the pricing objectives and policies, and it often approves the prices proposed by lower-level management or salespeople. In industries where pricing is a key factor, companies will often have a pricing department to set the best prices or help others in setting them. Others who have an influence on pricing decisions include sales managers, production managers, finance managers and accountants.

External factors: The external factors, as the term implies, are external to the organization and therefore, treated as uncontrollable by the organization. They have an indirect, but definite bearing on the firm's pricing decision. The following are the important external factors that must considered in pricing a firm's product/service.

- Nature of the market and demand – While costs set the lower limit of prices, the market and demand set the upper limit. Buyers balance the price of a product or service against the benefits of owning it. Therefore, before setting prices, the marketer must understand the relationship between price and demand for his product. Price-demand relationship varies for different types of markets and how buyer perceptions of price affect the pricing decision. Economists recognize four types of markets, viz. pure competition, monopolistic competition, oligopolistic competition and pure monopoly. Each presents a different pricing challenge and pricing freedom.
    - Under pure competition, the market consists of many buyers and sellers trading in a uniform commodity. A seller cannot charge more than the going price because buyers can obtain as much as they need at the going price. Nor would sellers charge less than the market price because they can sell all they want at this price.
    - Under monopolistic competition, the market consists of many buyers and sellers who trade over a range of prices rather than a single market price. A range of prices occurs because sellers can differentiate their product/service offering to buyers. Buyers see differences in sellers' offerings and will pay different prices for them.
    - Under oligopolistic competition, the market consists of a few sellers who are highly sensitive to each other's pricing and marketing strategies. The product may be uniform (as a commodity) or non-uniform. Each seller is alert to competitors' strategies and moves. An oligopolist is never sure that it will gain anything permanent through a price cut or a price hike.
    - In a pure monopoly, the market consists of one seller. The seller may be a government monopoly (the Indian Postal service), a private regulated monopoly (a power company) or a private non-regulated monopoly (e.g. Sify, when it introduced Virtual Private Networks for corporate users). Pricing is handled differently in each case. A government monopoly can set the price below cost to make the product/service affordable, or set price to recover costs or set a high price to slow down consumption (an instance of demarketing). In

a regulated monopoly, the government permits the firm to set rates that will yield a fair return. Non-regulated monopolies are free to price at what the market will bear. However, they will be careful not to attract competition nor invite government regulation.

- The price-demand relationship must also be studied before taking the price decision. Each price the firm might charge will lead to a different level of demand. The relation between the price charged and the resulting demand level is described as the Demand curve. In the normal case, demand and price and inversely related. For 'prestige' goods, raising the price may result in more sales. In measuring the price-demand relationship, the marketer must not allow other factors affecting demand to vary. They also need to know price elasticity, that is, how responsive demand will be to a change in price. If demand hardly changes with a small change in price, the demand is said to be inelastic. If demand changes greatly, it is said to be elastic. Price elasticity of demand is determined by many situations. For example, buyers are less price sensitive when the product they are buying in unique or when it is high in quality, prestige or exclusiveness. They are also less price sensitive when substitute products are hard to find or when they cannot easily compare the quality of substitute products. Buyers are less price sensitive when the total expenditure for a product is low relative to their income or when the cost is shared by another party.
- Competition – Another external factor affecting the company's pricing decisions is competitors' costs and prices and possible competitor reactions to the company's own pricing moves. For so-called commodities (i.e. virtually undifferentiated products), all competitors generally charge identical prices. If one goes above the market price, sales will drop off sharply; if one goes below, all others are likely to follow or risk significant reductions in market share. How much any individual firm is constrained by competitors' prices, therefore, depends largely on how differentiated its product is. A product that is set apart from other market offerings by its functional design, appearance, brand image and the supplier's reputation for service and availability in ways that have value to customers can command a price premium. There are circumstances, however, in

which firms will price over competitive levels even though the price differences are not really justified by superior product quality and service. A company may consciously elect, for example, not to meet competitive prices in a strategy of ‘milking’ the business, that is, yielding market share and gradually withdrawing from the market. It may continue to sell profitably for some time to its loyal customers, in the mean time gradually cutting back on selling and promotional expenses until it eventually phases out of the market. Some companies may choose not to price competitively because to do so would mean selling below cost. These so-called marginal firms eventually go out of business. Some large companies may not elect to meet the low price of a smaller competitor because to do so might mean giving up unit profits on a large sales base. It may be less costly in the short run to hold prices and give up some small percentage of market share. In the long run, the smaller competitor encroaches increasingly on the market positions of its major competitors until it becomes, itself, a major factor. Under shortage conditions, some firms may price opportunistically above prevailing market levels, knowing that demand far exceeds available supply and that some buyers will pay the high price. Finally, some firms may unknowingly be underpriced by competitors on some of their products. These products may be part of a broad line and the reporting system may not allow for monitoring the sales-profit performance of each item on the list. Thus the company may be losing sales and market position because of price and never realize, until too late, that the business has gone to more aggressive competitors. Generally, pricing strategies must inevitably be shaped with regard for present and future competition. In this respect, there is significant pricing interdependency among firms in an industry with each being heavily influenced by others’ strategies and tactics. Some firms follow price trends; others, the larger ones, seek to lead them. Accordingly, in contemplating price changes, the marketing manager will often seek to anticipate competitive responses.

- Other environmental factors – When setting prices, the firm also must consider other factors in its external environment. Economic conditions can have a strong impact on the firm’s pricing strategies. Economic factors such as inflation, boom or recession, and interest rates affect pricing decisions because they affect both the costs of producing a product and consumer perceptions of the product’s price and value. The firm also must consider what impact its prices will have on other parties in its environment. How will resellers react to various prices? The firm should set prices that give resellers a fair margin, encourage their support, and help them to sell the product effectively. The government is another important external influence on pricing decisions. In regulated industries such as utilities, transport and so on, the government has the authority to approve or reject price changes. Finally, social concerns may have to be taken into account. In setting prices, a firm’s short-term sales, market share and profit goals may have to be tempered by broader societal considerations.

Unit – III

Lesson 3.2

Pricing Objectives and Approaches

Objectives

In this lesson, we will introduce you to the pricing objectives and highlight the reasons because of which pricing has come to occupy center-stage in marketing rivalries. After you work out this lesson, you should be able to:

- Understand the different pricing objectives
- Identify the developments that have added to the importance of the pricing decision
- Classify the different pricing approaches

In this lesson, we will discuss the following:

- Situations that have pushed pricing to marketing center-stage
- Pricing objectives
- Cost-bases pricing approach
- Buyer-based pricing approach
- Competition-based pricing approach

Introduction

Ancient philosophers recognized the importance of price in an economic system. Some early written accounts refer to attempts to determine fair and just prices. Price continues to serve as a means of regulating economic activity. All the four factors of production, viz. natural resources, capital, human resources and entrepreneurship, depends on the prices that those factors receive. An individual firm's prices and the resulting purchases by its customers determine how much revenue the firm receives. Prices, therefore, influence a firm's profits as well as its employment of the factors of production.

Traditionally, price has operated as the major determinant of buyer choice. This is still the case in the poorer economies and with commodity-type products. Although non-price factors have become more important in recent decades, price still remains one of the most important elements determining market share and profitability. Pricing has come to occupy center-stage in many marketing rivalries. Many reasons can be attributed to this. Some of them are outlined below:

- In some cases, product differentiation is getting blunted, thanks to the homogenization of technology. This is more relevant in the context of global business where the million dollar question is whether the firms should offer a standardized offering or a differentiated offering.
- There is intense inter-firm rivalry in some industries. It may be attributed to the removal of entry/exit barriers. Also the cost of fighting these marketing wars must be recovered and often, it is transferred to the customer.
- In certain industries, the products and the markets are mature. The only way to differentiate may be is through an augmented service or price cuts. Here again, pricing decisions are crucial to the survival of the firm.
- Customers' value perception correlates with the quoted price. To a customer, price always represents product's value. The price-quality perception must be taken into account during the product decision and the price decision.
- Inflation in the economy may also contribute to the significance of pricing decision in a marketing program. It lowers customer's purchasing power and increases input costs. As a result, the marketer has to make the price decision after careful evaluation.

Pricing objectives

Just as price is a component of the total marketing mix, pricing objectives also represent components of the organization's overall objectives. The objectives of the firm and its marketing organization guide the development of pricing objectives, which in turn lead to development and implementation of more specific pricing policies and procedures. For example, a firm might set a major overall objective of becoming the dominant producer in its domestic market. It might then develop a marketing objective of achieving maximum sales penetration in each region, followed by a related pricing objective to set prices at levels that maximize sales. These objectives might lead to adoption of a low-price policy implemented by offering substantial price discounts to channel members.

While pricing objectives vary from firm to firm, they can be classified into four major groups:

(1) Profitability objectives

(2) Volume objectives

(3) Meeting competition objectives, and

(4) Prestige objectives

Profitability objectives include profit maximization and target-return goals. Volume objectives pursue either sales maximization or market-share goals.

Profitability objectives: Classical economic theory bases its conclusions on certain assumptions. It presumes that firms will behave rationally. Theorists expect that rational behaviour will result in an effort to maximize gains and minimize losses. Profits are a function of revenue and expenses.

$$\text{Profits} = \text{Revenue} - \text{Expenses}$$

Revenue is determined by the product's selling price and number of units sold:

$$\text{Total revenue} = \text{Price} * \text{Quantity sold}$$

A profit maximizing price, therefore, rises to the point at which further increases will cause disproportionate decreases in the number of units sold. A 10% price increase that results in only an 8% cut in volume will add to the firm's revenue. However, a 10% price hike that results in an 11% sales decline will reduce revenue. Profit maximization is identified as the point at which the addition to total revenue is just balanced by the increase in total cost. Consequently, marketers set target return objectives – short-run or long-run goals usually stated as percentages of sales or investments. Target return objectives offer several benefits for marketers in addition to resolving pricing questions. For example, they serve as tools for evaluating performance. They also satisfy desires to generate 'fair' profits as judged by management, stockholders and the public.

Volume objectives: Many marketers argue that pricing behaviour actually seeks to maximize sales within a given profit constraint. They set a minimum acceptable profit level and then seek to maximize sales in the belief that the increased sales are more important than immediate high profits to the long-run competitive picture. Such a firm continues to expand sales as long as its total profits do not drop below the minimum return acceptable to management. Another volume-related pricing objective – the market share objective – sets a goal to control a portion of the market for a firm's good or service. The company's specific goal may target maintaining its present share of a particular market or increasing its share. Volume-related goals such as sales maximization and market share objectives play important roles in most firms' pricing decisions.

Meeting competition objectives: A third set of pricing objectives seeks simply to meet competitor's prices. In many lines of business, firms set their own prices to match those of established industry price leaders. These kinds of objectives de-emphasize the price element of the marketing mix and focus competitive rivalries more strongly on non-price variables. Pricing is a highly visible component of a firm's marketing mix and an easy and effective tool for obtaining a differential advantage over competitors; still other firms can easily duplicate a price reduction themselves. Because such price changes directly affect overall profitability in an industry, many firms attempt to promote stable prices by meeting competitors' prices and competing for market share by focusing on product strategies, promotional decisions and distribution – the non-price elements of the marketing mix. When price discounts become normal elements of a competitive marketplace, other marketing mix elements gain importance in purchase decisions. In such instances, overall product value, not just price, determines product choice. Value pricing emphasizes benefits a product provides in comparison to the price and quality levels of competing offerings. This strategy typically works best for relatively low-priced goods and services. Value-priced products generally cost less than premium brands, but marketers point out that value does not necessarily mean cheap. Value is not just price, but also is linked to the performance and meeting expectations and needs of consumers. The challenge for those who compete on value is to convince customers that low-priced brands offer quality comparable to that of a higher-priced product.

Prestige objectives: The final category of pricing objectives, unrelated to either profitability or sales volume, encompasses prestige objectives. Prestige pricing establishes a relatively high price to develop and maintain an image of quality and exclusiveness that appeals to status-conscious consumers. Such objectives reflect marketers' recognition of the role of price in creating an overall image for the firm and its goods and services.

General pricing approaches

The price the firm charges will be somewhere between on that is too low to produce a profit and one that is too high to produce any demand. Product costs set a floor to the price and consumer perceptions of the product's value set the ceiling. The firm must consider competitors' prices and other external and internal factors to find the best price between these two extremes. Firms set prices by selecting a general pricing approach that includes one or more of these three sets of factors. Let us examine the following approaches:

(1) Cost-based approach

(2) Buyer-based approach, and

(3) Competition-based approach

Cost-based approach

The simplest pricing method is cost-plus or markup pricing - adding a standard markup to the cost of the product. Markups vary greatly among different goods. Some common markups (on price, not cost) in supermarkets are 9% on baby foods, 14% on tobacco products, 27% on dried foods and vegetables and 50% on greeting cards. Markups are generally higher on seasonal items (to cover the risk of not selling) and on specialty items, slower moving items, items with high storage and handling costs and items with inelastic demand. It must be noted that any pricing method that ignores current demand and competition is not likely to lead to the best price. Hence markup pricing only works if that price actually brings in the expected level of sales.

Advantages:

(1) It covers all the costs

(2) It is designed to provide the target rate of margin

(3) It is generally a rational and widely accepted method

(4) It is an easy to comprehend and simple method

Disadvantages:

(1) The cost calculations are based on a predetermined level of activity. If the actual level of activity varies from this estimated level, the costs may vary, rendering this method unrealistic.

(2) If the costs of the firm are higher than its competitors, this method would render the firm passive in relation to price.

(3) Another drawback is that sometimes the opportunity to charge a high price is foregone.

(4) It ignores the price elasticity of demand.

(5) The cost-based pricing would not be helpful for some of the objectives or tasks like market penetration, fighting competition and so on.

(6) It imparts an in-built inflexibility to pricing decisions.

Another cost-based pricing approach is break even pricing, or a variation called target profit pricing. The firm tries to determine the price at which it will break even or make the target profit it is seeking.

Buyer-based approach

An increasing number of firms are basing their prices on the product's perceived value. Perceived-value pricing uses buyers' perceptions of value, not the seller's cost, as the key to pricing. The company uses the non-price variables in the marketing mix to build up perceived value in buyers' minds. Price is set to match the perceived value. A company using perceived-value pricing must find out what value buyers assign to different competitive offers. Sometimes consumers are asked how much they would pay for each benefit added to the offer. If the seller charges more than the buyers' perceived value, the firm's sales will suffer. Many firms overprice their products, and their products sell poorly. Other firms underprice. Under-priced products sell very well, but they produce less revenue than they would if prices were raised to the perceived-value level.

Competition-based pricing

Many firms follow the dominant competitors, particularly the price leader, in setting the price. The main advantages of this method are:

(1) It is a very simple method

(2) It follows the main market trend

(3) It has relevance to the competitive standing of the firm

(4) Holding to the going price will prevent harmful price wars

The major disadvantages and limitations of following competitors are:

(1) If the competitors' price decisions are unrealistic, the follower will also be going wrong on the price

(2) The cost factors of the follower may not be similar to that of the competitors'

(3) The pricing objective of the firm could be different from that of the competitors'

(4) Sometimes the competitor may initiate price change for wrong reasons

Competition-based pricing approach may take the form of going-rate pricing or sealed-bid pricing. In going-rate pricing, the firm bases its price largely on competitors' prices, with less attention paid to its own cost or to demand. In oligopolistic industries that sell commodities, firms normally charge the same price. It is a popular pricing method. When demand elasticity is hard to measure, firms feel the going price represents the collective wisdom of the industry concerning the price that will yield a fair return. Competition-based pricing is also used when firms bid for jobs. Using sealed-bid pricing, a firm bases its price on how it thinks competitors will price rather than on its own costs or on the demand. The firm wants to win a contract and winning the contract requires pricing lower than other firms. Yet, the firm cannot set its price below a certain level. It cannot price below cost without hurting its position. In contrast, the higher the firm sets its price above its costs, the less its chance of getting the contract.

Unit – III

Lesson 3.3

Pricing Policies and Constraints

Objectives

In this lesson, we will introduce you to Pricing policies and constraints. After you work out this lesson, you should be able to:

- Understand the procedure in formulating a pricing policy
- Identify the constraints that come to bear on pricing decisions
- Appreciate the nuances of pricing in industrial marketing

In this lesson, we will discuss the following:

- Pricing policy – as a 6-step procedure
- Pricing and product life cycle
- Pricing across the four product life cycle stages
- Distinguishing characteristics of pricing the industrial products/services
- Pricing on the Internet (Pricing in E-Commerce)

Introduction

Firms do their pricing in a variety of ways as discussed in the previous lesson. Executives complain that pricing is a big headache and one is wary of committing a go/drop error in the pricing decision. Pricing less than what the customer wants to pay and pricing more than what the customer wants to pay are both costly errors. 'There are two fools in every market: one asks too little, one asks too much', says a Russian Proverb. Many companies do not handle pricing well. Some common mistakes are:

- Price is not revised often enough to capitalize on market changes
- Price is set independently of the rest of the marketing mix rather than as an intrinsic element of market-positioning strategy
- Price is not varied enough for different product items, market segments, distribution channels and purchase occasions

The importance of pricing for profitability was demonstrated in a 1992 study by McKinsey & Company. Examining 2,400 companies, McKinsey concluded that a 1% improvement in price created an improvement in operating profit of 11.1%. By contrast, 1% improvements in variable cost, volume and fixed cost product profit improvements of only 7.8%, 3.3% and 2.3% respectively. Effectively designing and implementing pricing strategies requires a systematic approach to setting, adapting and changing prices.

Procedure for a pricing policy

A firm must set a price for the first time when it develops a new product, when it introduces its regular product into a new distribution channel or geographical area, and when it enters bids on new contract work. The firm has to consider several factors in setting its pricing policy. A useful 6-step procedure to develop the pricing policy is discussed below.

1) Selecting the pricing objective: The firm first decides where it wants to position its market offering. The clearer a firm's objectives, the easier it is to set price. A firm can pursue any of the objectives classified under four major groups, viz. profitability objectives, volume objectives, meeting competition objectives and prestige objectives. This was discussed in the previous lesson.
2) Determining demand: Each price will lead to a different level of demand and therefore have a different impact on a firm's marketing objectives. The relation between alternative prices and the resulting current demand is captured in a demand curve. In the normal case, demand and price are inversely related: the higher the price, the lower the demand. In the case of prestige goods, the demand curve sometimes slopes upward. However, if the price is too high, the level of demand may fall. The demand curve sums the reactions of many individuals who have different price sensitivities. The first step is estimating demand is to understand what affects price sensitivity. Generally speaking, customers are most price sensitive to products that cost a lot or are bought frequently. They are less price sensitive to low cost items or items they buy infrequently. They are also less price sensitive when price is only a small part of the total cost of obtaining, operating and servicing the product over its lifetime. Firms, of course, prefer customers who are less price sensitive. The following is a list of factors leading to less price sensitivity, as identified by Nagle and Holden.
    - The product is more distinctive
    - Buyers are less aware of substitutes
    - Buyers cannot easily compare the quality of substitutes

- The expenditure is a smaller part of the buyer’s total income
- The expenditure is small compared to the total cost of the end product
- Part of the cost is borne by another party
- The product is used in conjunction with assets previously bought
- The product is assumed to have more quality, prestige or exclusiveness
- Buyers cannot store the product

Most firms make some attempt to measure their demand curves using methods like statistical analysis, price experiments and surveys. In measuring the price-demand relationship, the marketer must control for various factors that will influence demand. The competitor’s response will make a difference. Also, if the company changes other marketing mix factors besides price, the effect of the price change itself will be hard to isolate and measure.

3) Estimating costs – In the earlier discussion on costs, it was noted that demand sets a ceiling on the price, whereas costs set the floor. Also, the types of costs and the impact of economies of scale and learning curve on pricing was explained. To price intelligently, management needs to know how its costs vary with different levels of production. It is important to be aware of the risks presented by pricing based on the experience/learning curve. It assumes that competitors are weak followers. It leads the company into building more plants to meet the demand, while a competitor may be innovating a lower-cost technology. Then the market leader will be stuck with the old technology. Today’s firms try to adapt their offers and terms to different buyers. A manufacturer may negotiate different terms with different retail chains. One retailer may want daily delivery (to keep inventory lower) while another may accept twice-a-week delivery in order to get a lower price. The manufacturer’s cost will differ with each chain and so will its profits. To estimate the real profitability of dealing with different customers with differing requirements, the manufacturer needs to use activity-based cost (ABC) accounting instead of standard cost accounting. ABC accounting tries to identify the real costs associated with serving each customer. It allocates indirect costs like clerical costs, office expenses, supplies and so on, to the activities that use them, rather than in some proportion to direct costs. Both variable and overhead costs

are tagged back to each customer. Another interesting costing concept is target costing. Costs change with production scale and experience. They can also change as a result of a concentrated effort by designers, engineers and purchasing agents to reduce them through target costing. Market research is used to establish a new product's desired functions and the price at which the product will sell, given its appeal and competitors' prices. Deducting the desired profit margin from this price leaves the target cost that must be achieved. Each cost element - design, engineering, manufacturing, sales – must be examined and different ways to bring down costs must be considered. The objective is to bring the final cost projections into the target cost range. If this is not possible, it may be necessary to stop developing the product because it could not sell for the target price and make the target profit.

4) Analysing competitors' costs, prices and offers – Within the range of possible prices determined by market demand and company costs, the firm must take competitors' costs, prices and possible price reactions into account. The firm should first consider the nearest competitor's price. If the firm's offer contains features not offered by the nearest competitor, their worth to the customer should be evaluated and added to the competitor's price. If the competitor's offer contains some features not offered by the firm, their worth to the customer should be evaluated and subtracted from the firm's price. Now the firm can decide whether it can charge more, the same or less than the competitor. But competition can change their prices in reaction to the price set by the firm.

5) Selecting a pricing approach – Given the three *C*s – the Customer's demand schedule, the cost function and the competitors' prices – the firm is now ready to select a price. Figure 3.3.1 summarizes the three major considerations in price setting. Costs set a floor to the price. Competitors' price and the price of substitutes provide an orienting point. Customers' assessment of unique features establishes the price ceiling. Firms select a pricing approach that includes one or more of these three considerations. The pricing approaches are cost-based or buyer-based or competition-based. These approaches were discussed at length in the previous lesson.

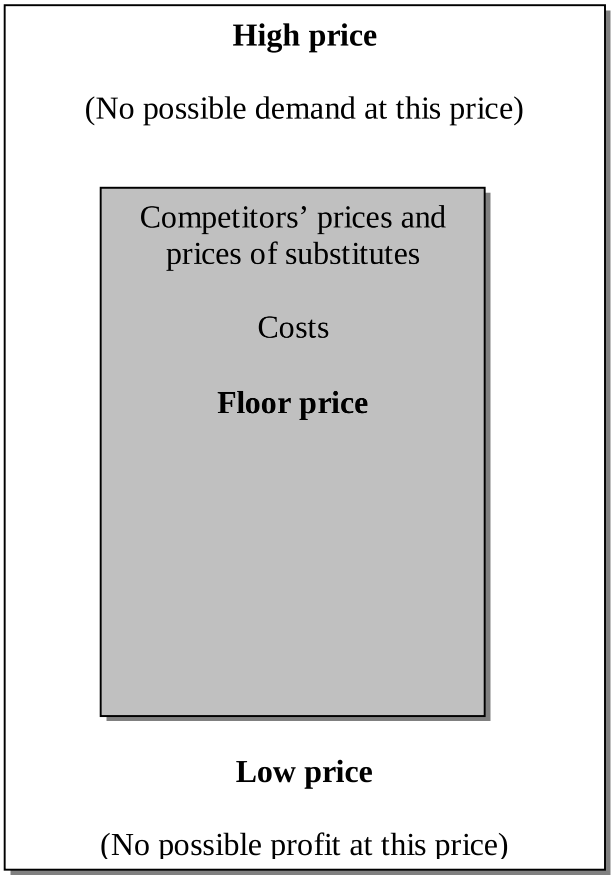

High price
(No possible demand at this price)
Competitors' prices and prices of substitutes
Costs
Floor price
Low price
(No possible profit at this price)

Figure 3.3.1 The three *C*s model for price setting

(Source: Marketing Management, 12e, Kotler and Keller)

6) Selecting the final price – Pricing methods narrow the range from which the company must select its final price. In selecting that price, the company must consider additional factors, including the impact of other marketing activities, company pricing guidelines, gain-and-risk-sharing pricing and the impact of price on other parties. The final price must take into account the brand's quality and advertising relative to the competition. The price must be consistent with the firm's pricing guidelines. When a firm establishes pricing penalties, it must be done judiciously so as not to unnecessarily alienate customers. Sometimes, buyers may resist accepting a seller's proposal because of a high perceived level of risk. The seller has the option of offering to absorb part or all of the risk if it does not

deliver the full promised value. Management must also consider the reactions of other parties to the contemplated price. For instance, the reaction of marketing intermediaries must be thought about. The reaction of the sales force must be taken note since they will be the ones to sell at that price in the marketplace. All these reactions might hold clues to fine tune the final price.

Pricing and Product Life Cycle

From a strategic point of view, the product life cycle provides a framework for thinking about pricing decisions. You may recall the discussion in Unit-2 about the product life cycle (Figure 3.3.2). Four phases may be identified in the product life cycle: introduction, growth, maturity and decline as shown in the figure below.

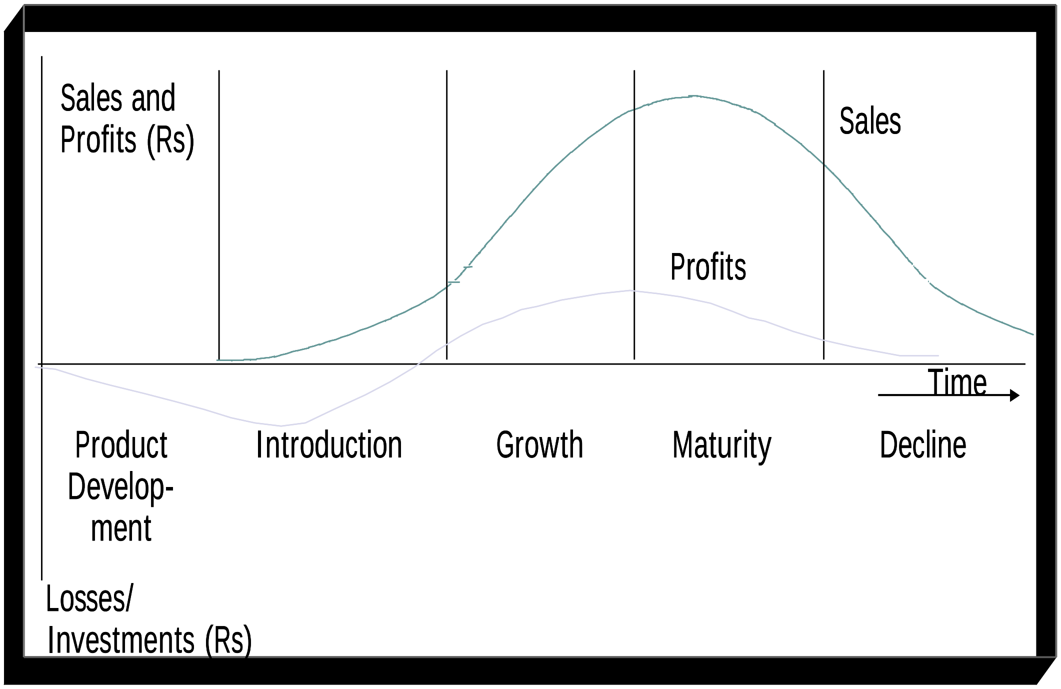


Figure 3.3.2 The Product Life Cycle curve

Each phase presents different opportunities and constraints on price.

Introduction phase: During the introduction phase, pricing can be a quandary, especially if you enjoy a temporary monopoly. In that situation, there may be no direct competitor and thus no benchmark for what buyers will tolerate or for their sensitivity to price differences. There may be indirect competitors (substitutes), however, and they can be used as starting points for the pricing decision. The total economic value equation becomes relevant, wherein the price of the best alternative is known but the value of the performance differential of the new product is unknown. Customers themselves may have difficulty in sizing up the value of something that is new and different. They too lack benchmarks of value. In such instances, any of the following strategies may be adopted:

- Skimming: Some people will be happy to pay a high price for anything that is new and unique. This strategy, of course, is short term and contains dangers like attracting competition.
- Penetration pricing: A low price may have the threefold benefits of (1) getting established as the market share champion, (2) discouraging market entry by competitors, and (3) creating broad-based demand for the product.
- Cost-plus: In a monopoly, the producer can administer its own price and cost-plus is one way of determining that price. However, product monopolies are short-lived.

Pricing decisions in this introductory phase are not only difficult but also deadly important. Putting too high a price on a newly introduced product may kill it in its infancy, undoing the work of many employees over a long period of development.

Growth phase: The growth phase is characterized by increasing unit sales and accelerating customer interest. If competitors have not yet surfaced (which is an unlikely event), skimming may be appropriate. All the deep-pocketed buyers who simply had to be the first in their neighbourhoods to own the product have already been skimmed in the introduction phase. So now, the price must be reduced gradually, skimming other market segments that are progressively more price sensitive.

A producer that enjoys prime position on the experience curve will also want to progressively reduce prices during this phase. Doing so will maintain its margins even as the strategy expands unit sales and punishes late-into-the-game rivals in the marketplace. Some of these rivals will either take a loss on every sale or simply wind up.

Mature phase: By the time a product enters this phase, growth in unit sales is leveling off and the remaining competitors are trying to find ways to differentiate their products. During this phase, one may see sellers offer different versions of the product, each version trying to colonize a targeted segment. Price is one of the factors used in this strategy (i.e. by developing and pricing good, better and best versions to expand the product line).

Decline phase: Competition gets ugly in this phase. Total demand for the product category is now visibly slipping, perhaps because of the appearance of superior substitutes or because of market saturation. Whatever the case, unit sales will continue to decline. Some companies will get out of the business entirely; those that remain will aggressively try to take business away from the rivals. Every player in the market is trying to harvest as much as possible from a contracting market. Price tactics include the following:

- Beat a retreat on price, but work overtime to reduce production costs. Success in the latter will maintain a decent profit margin
- Increase the price on the few remaining units in inventory. This is because there may be a small number of customers who still rely on that particular product. This is particularly true of replacement parts. Here the seller hopes that the higher price will compensate for fewer sales. When the inventory is exhausted, the product line is terminated.

Pricing is one of the linchpins of marketing strategy and success. How is the company making its pricing decisions? Are these decisions appropriate for the current phase of the product life cycle? The most reliable method of pricing is to get inside the heads of customers, because how they value the firm's products relative to those of competitors and substitutes matters more than anything else.

Pricing in industrial (business-to-business) markets

As Lesson 1.1 outlined the differences between consumer marketing and industrial marketing, those differences can further be explained based on the distinguishing characteristics of industrial pricing. Some of those characteristics are listed below:

- The true price as industrial customer pays is often different from the list price because of factors like delivery and installation costs, discounts, training costs, trade-in allowance, financing costs and so on.
- Pricing is not an independent variable. It is highly intertwined with product, promotion and distribution strategies.

- Price for industrial products cannot be set out without considering other products that are compliments or substitutes sold by the firm. Cross elasticities exist, where the price of one item affects sales of other items.
- Prices can be changed in numerous ways such as changing the quantity of goods and services provided by the seller, changing the premiums and discounts that are offered, changing the time and place of payment, and so on. This implies that pricing is often a more flexible decision than product or distribution decisions.
- Industrial prices are established, in many cases, by competitive bidding on a project-by-project basis. In a number of cases, prices are resolved through negotiation.
- Industrial pricing is often characterized by an emphasis on fairness. Industrial buyers, who are experienced and able to estimate the vendors' approximate production costs expect the price increases to be justifiable on the basis of either the cost increases or product improvements.
- Industrial prices are affected by a host of economic factors such as inflation, interest rate changes, exchange rate fluctuations and so on. This problem is particularly critical for the marketer locked into a long term contract with no escalation cause.

Pricing on the Internet

E-Commerce has been arguably the Web's hottest application. Yet the Internet is more than simply a new 'marketspace'. Internet-based technologies are actually changing the rules of the market. Here is a short list of how the Internet allows sellers to discriminate between buyers and buyers to discriminate between sellers.

- Buyers can …
    - Get instant price comparisons from thousands of vendors – Consumers now regularly check online prices, compare them with those in their local stores and may well take a peek at what customers in other places/countries are paying and order from overseas. Consumers also may unbundle product information from the transaction themselves. For instance, someone might use the Internet to research on a holiday destination, but visit a travel agency to get some procedural requirements

done, go home to use a search engine to find the lowest airfare to that destination. Sites like PriceScan.com lure thousands of visitors a day, most of them corporate buyers. Intelligent shopping agents (known as 'bots') take price comparison a step further and seek out products, prices and reviews from as many as 2,000 merchants.

    - Name their price and have it met – Taking the example of Priceline.com, the customer states the price he wants to pay for an airline ticket, hotel or car rental and Priceline checks whether any seller is willing to meet that price. Consumers can fix their own prices, and sellers can use it too. Airlines can fill in demand for empty seats and hotels welcome the chance to sell vacant rooms at near zero marginal cost. Volume-aggregating sites combine the orders of many customers and press the supplier for a deeper discount.
    - Get products free – Open Source, the free software movement that started with Linux, will erode margins for just about any company doing software. Open Source software is popping up everywhere. The biggest challenge confronting major software producers is now: how to compete with programs that can be had free?
- Sellers can …
    - Monitor customer behaviour and tailor offers to individuals – Although shopping agent software and price comparison web sites provide published prices, consumers may be missing out on the special deals they can get with the help of new technologies. GE Lighting, which gets 55,000 pricing requests a year, has Web programs that evaluate about 300 factors that go into a pricing quote, such as past sales and discounts, so that it can reduce processing time from up to 30 days to 6 hours.
    - Give certain customers access to special prices – CDNOW, an online vendor of music albums, emails certain (loyal) buyers a special website address with lower prices. Unless you know the secret address, you pay full price. Business marketers are already using extranets to get a precise

handle on inventory, costs and demand at any given moment in order to dynamically adjust prices.

- Bother buyers and sellers can …
    - Negotiate prices in online auctions and exchanges – Want to sell hundreds of excess and slightly worn widgets? Post a sale on ebay.co.in (formerly, Bazee.com). Want to purchase air tickets at a bargain price? Go to air ticket auctions at Rediff.com. Thanks to the Internet, pricing is no longer a rigid entity of marketing. It is the era of dynamic pricing in many categories.

Unit – III

Lesson 3.4

Pricing Methods

Objectives

In this lesson, we will introduce you to the Pricing dynamics. This lesson examines the major dynamic pricing strategies available to the marketer. After you work out this lesson, you should be able to understand:

- The new product pricing strategies for products in the introductory stage of the product life cycle
- The product-mix pricing strategies for related products in the product mix
- The price-adjustment strategies that account for customer differences and changing situations.

In this lesson, we will discuss the following:

- New Product pricing strategies
  - Market Skimming pricing
  - Market Penetration pricing
- Product Mix pricing strategies
  - Product-line pricing
  - Optional-product pricing
  - Captive-product pricing
  - By product pricing
  - Product-bundle pricing
- Price Adjustment strategies
  - Discount and allowance pricing
  - Discriminatory pricing
  - Psychological pricing
  - Value pricing
  - Promotional pricing
  - Geographical pricing
  - International pricing

Introduction

Firms translate pricing objectives into pricing decisions in two major steps. First, someone must accept responsibility for making pricing decisions and administering the resulting pricing structure. Second, someone must set the overall pricing structure – that is, basic prices and appropriate discounts for channel members, quantity purchases, and geographic and promotional considerations. Hence a firm sets not a single price, but rather a pricing structure that covers different items in its line. This pricing structure changes over time as products move through their life cycles. The company adjusts product prices to reflect changes in costs and demand and to account for variation in buyers and situations.

New Product Pricing Strategies

Pricing strategies usually change as the product passes through its life cycle as illustrated in the previous lesson. The introductory stage is especially challenging. Firms bringing out an innovative patent-protected product can choose between two options, viz. market-skimming pricing and market-penetration pricing.

Market-skimming pricing: Many firms that invent new products initially set high prices to 'skim' revenues layer by layer from the market. At product introduction in the marketplace, the firm may charge the highest price it could given the benefits of its new product over competing products. The firm sets a price that made it just worthwhile for some affordable segments of the market to adopt the new product. After the initial sales slowdown, the firm may lower the price to draw in the next price sensitive layer of the customers. In this way, a firm skims a maximum amount of revenue from the various segments of the market. It is important to note that skimming works well only under certain conditions. The quality and image must support its higher price and enough buyers must want the product at that price. Also the cost of producing a small volume cannot be so high that they cancel the advantage of charging more. In the mean time, competitors should not be able to enter the market easily and undercut the price. A skimming strategy offers several benefits to the markets, as listed below:

- It allows a manufacturer to quickly recover its research and development costs.
- It also allows a firm to maximize revenue from a new product before competitors enter the field.

- A skimming strategy offers a useful tool for segmenting a product's overall market on a price basis.
- It permits marketers to control demand in the introductory stages of a product's life cycle and then adjust productive capacity to match demand.

The chief disadvantage of skimming strategy is: it attracts competition. Potential competitors see innovative firms reaping big financial gains and decide to enter the market. This new supply forces the price even lower than its eventual level under a sequential skimming procedure. However, if patent protection or other proprietary ability allows a firm to exude competitors from its market, it may continue a skimming strategy for a relatively long period.

Market-penetration pricing: Rather than setting a high initial price to skim off small but profitable market segments, some firms set a low initial price in order to penetrate the market quickly and deeply – to attract a large number of buyers quickly and win a large market share. A penetration pricing strategy may also extend over several stages of the product life cycle as the firm seeks to maintain a reputation as a low-price competitor. Since many firms begin penetration pricing with the intention of increasing prices in the future, success depends on generating many consumer trial purchases. Penetration pricing works well under the following conditions:

- A good or service experiences highly elastic demand
- The market is highly price sensitive and a low price stimulates market growth
- Production and distribution costs fall with accumulated production experience
- A low price helps discourage actual and potential competition

Product-Mix pricing

The strategy for setting a product's price often has to be changed when the product is part of a product mix. In this case, the firm looks for a set of prices that maximizes the profits on the total product mix. This pricing is difficult because the various products have related demand and costs and face different degrees of competition. The following section outlines the five product-mix pricing situations depicted in Figure 3.4.1

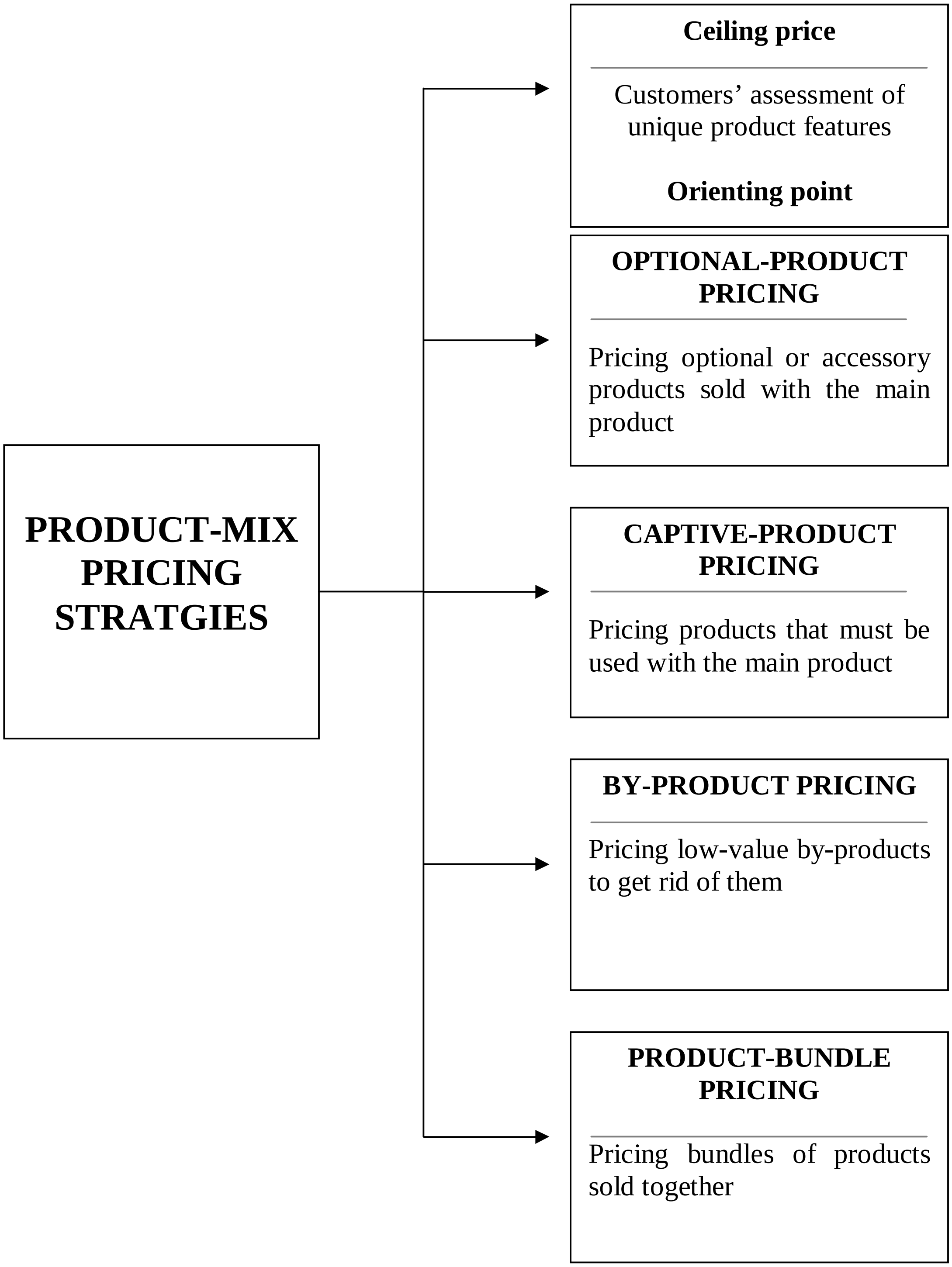

PRODUCT-MIX PRICING STRATGIES
Ceiling price
Customers' assessment of unique product features
Orienting point
OPTIONAL-PRODUCT PRICING
Pricing optional or accessory products sold with the main product
CAPTIVE-PRODUCT PRICING
Pricing products that must be used with the main product
BY-PRODUCT PRICING
Pricing low-value by-products to get rid of them
PRODUCT-BUNDLE PRICING
Pricing bundles of products sold together

Figure 3.4.1 Product Mix pricing strategies

Product-line pricing: Since most firms market multiple product lines, an effective pricing strategy must consider the relationships among all of these products instead of viewing each is isolation. In product line pricing, management must decide on the price steps to set between the various products. The price steps should take into account cost differences between the products, customer evaluations of their different features and competitors' prices. In many industries, marketers use well-established price points for the products in their line. The customer will probably associate low, average and high quality with the price points. The marketers task is to establish perceived quality differences that support the price differences.

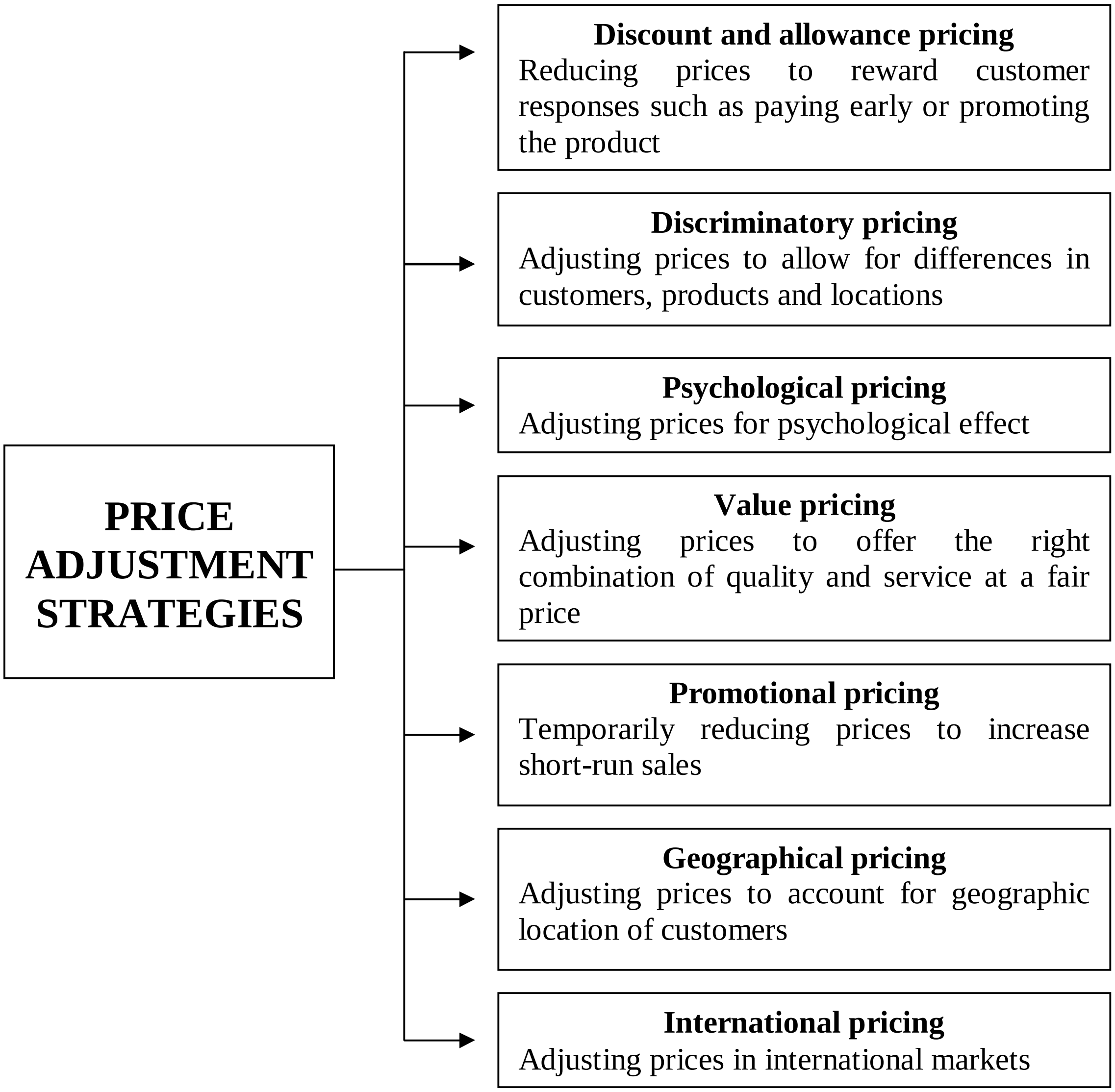
Optional-product pricing: Many firms use this strategy by offering to sell optional or accessory products along with their main product. These firms have to decide which items to include in the base price and which to offer as options. Often the basic model which is stripped of many comforts and conveniences sought by the customers gets rejected.

Captive-product pricing: Firms that make products that must be used along with a main product are using this pricing strategy. Producers of the main products often price them low and set high markups of the supplies. For a competitor who does not sell these supplies, he will have to price his product higher in order to make the same overall profit. In case of services, this strategy is called two-part pricing where the price of the service is broken into a fixed fee plus a variable usage rate. The service firm must decide how much to charge for the basic service and how much for the variable usage. The fixed amount should be low enough to induce usage of the service and profit can be made on the variable usage fees.

By-product pricing: In producing certain products, there are by-products. If these by products have no value and if getting rid of them is costly, this will affect the pricing of the main product. Using by-product pricing, the manufacturer will seek a market for these by-products and should accept any price that covers more than the cost of storing and delivering them. This practice allows the marketer to reduce the main product's price to make it more competitive.

Product-bundle pricing: Using this strategy, marketers combine several of their products and offer the bundle at a reduced price. Price bundling can promote the sales of products consumers might not buy otherwise, but the combined price must be low enough to get them to buy the bundle.

Price-adjustments



PRICE ADJUSTMENT STRATEGIES

Discount and allowance pricing
Reducing prices to reward customer responses such as paying early or promoting the product

Discriminatory pricing
Adjusting prices to allow for differences in customers, products and locations

Psychological pricing
Adjusting prices for psychological effect

Value pricing
Adjusting prices to offer the right combination of quality and service at a fair price

Promotional pricing
Temporarily reducing prices to increase short-run sales

Geographical pricing
Adjusting prices to account for geographic location of customers

International pricing
Adjusting prices in international markets

. **Figure 3.4.2** Price adjustment strategies

Firms usually adjust their basic prices to account for various customer differences and changing situations. Figure 3.4.2 summarizes seven price-adjustment strategies.

Discount and allowance pricing: Most firms adjust their basic price to reward customers for certain responses, such as cash payment, early payment of bills, volume purchases and off-season buying. Some of those adjustments are described below:

- Cash discounts – A cash discount is a price reduction to buyers who pay their bills promptly. The discount must be granted to all buyers meeting these terms. Such discounts are customary in many industries and help to improve the sellers' cash situation and reduce bad debts and credit collection costs.

- Quantity discounts – A quantity discount is a price reduction to buyers who buy large volumes. It must be offered to all customers and must not exceed the seller's cost savings associated with selling large quantities. These savings include lower selling, inventory and transportation expenses. Discounts provide an incentive to the customer to buy more from one given seller, rather than from many different sources.
- Functional discounts – A functional discount (also called trade discount) is offered by the seller to trade channel members who perform certain functions, such as selling, storing and record keeping. Manufacturers may offer different functional discounts to different trade channels because of the varying services they perform, but manufacturers must offer the same functional discounts within each trade channel.
- Seasonal discounts – A seasonal discount is a price reduction to buyers who buy out of season. It allows the seller to keep productions steady during the entire year.
- Allowances – They are another type of reductions from the list price. Trade-in allowances are price reductions given for turning in an old item when buying a new one. Promotional allowances are payments or price reductions to reward dealers for participating in advertising and sales-support programs.

Discriminatory pricing: Firms will often adjust their basic prices to allow for differences in customers, products and locations. In discriminatory pricing, the firm sells a product or service at two or more prices, even though the difference in prices is not based on differences in costs. Discriminatory pricing takes many forms as indicated below:

- Customer-segment pricing – Different customers pay different prices for the same product or service.
- Product-form pricing - Different versions of the product are priced differently, but not according to differences in their costs.

- Location pricing – Different locations are priced differently, even though the cost of offering in each location is the same.
- Time pricing - Prices vary by the season, month, day and even hour.

Psychological pricing: It applies the belief that certain prices or price ranges make products more appealing to buyers than others. In using psychological pricing, sellers consider the psychology of prices and not simply the economics.

- Pricing based on perceptions – The relationship between price and quality perceptions indicate that consumers perceive higher-priced products as having higher quality. When consumers cannot judge quality because they lack the information or skill, prices becomes an important quality signal.
- Reference pricing – Reference prices are those prices that buyers carry in their minds and refer to when looking at a given product. It might be formed by noting current prices, remembering past prices or assessing the buying situation. Sellers can influence or use these consumers' reference prices when setting price.
- Odd pricing – In odd pricing, marketers set prices at odd numbers just under round numbers. An odd ending conveys the notion of a discount or bargain to the customer.

Value pricing: During slow-growth times, many firms adjust their prices to bring them into line with economic conditions and with the resulting fundamental shift in consumer attitudes toward quality and value. Value pricing is offering just the right combination of quality and good service at a fair price. In many cases, value pricing has involved redesigning existing brands in order to offer more quality for a given price or the same quality for less.

Promotional pricing: In promotional pricing, a lower-than-normal price is used as a temporary ingredient in a firm's selling strategy. Some promotional pricing arrangements form part of recurrent marketing initiatives. Some may be to introduce a promotional model or brand with special pricing to begin competing in a new market. Promotional pricing takes several forms and some of them are described below.

- Loss-leader pricing – It happens when retailers drop price on well-known brands to stimulate store traffic in the hope that customers will buy other items also, at normal mark-ups

- Special-event pricing – Sellers use special-event pricing in certain seasons to draw in more customers. The seasonal need of the customers is capitalized on by the sellers using this pricing strategy.
- Cash rebates – Manufacturers will sometimes offer cash rebates to consumers who buy the product from dealers within a specified time.
- Low-interest financing, longer payment times, longer warranties – all these represent the promotional incentives offered by the sellers to the buyers. Since they provide some flexibility and also bring down the perceived risks (in case of longer warranties), buyers are motivated to make the buying decision.
- Psychological discounting – The seller may simply offer discounts from normal prices to increase sales and reduce inventories. For the buyer, the motivation to buy below normal prices may be compelling.

Geographical pricing: Geographical considerations strongly influence prices when costs must cover shipping heavy, bulky, low-unit-cost materials. Buyers and sellers can distribute transportation expenses in several ways: (1) The buyer pays all transportation charges; (2) The seller pays all transportation charges; or (3) the buyer and the seller share the charges. This choice has particularly important effects for a firm seeking to expand its geographic coverage to distant markets. The seller's pricing can implement several alternatives for handling transportation costs.

- FOB-origin pricing – It means that the goods are placed free on board (FOB) a carrier, at which point the title and responsibility pass to the customer, who pays the freight from the factory to the destination. Though it looks fair, the disadvantage is that the firm will be a high-cost firm to distant customers.
- Uniform delivered pricing – It is the exact opposite of FOB pricing. The company charges the same price plus freight to all customers, regardless of their location. An advantage is that it is fairly easy to administer and it lets the firm advertise its price nationally.
- Zone pricing – It falls between FOB-origin pricing and uniform delivered pricing. The company sets up two or more zones. All customers within a given zone pay a single total price; the more distant the zone, the higher the price.

- Basing-point pricing – The seller selects a given city as a ‘basing point’ and charges all customers the freight cost from that city to the customer location, regardless of the city from which the goods actually are shipped.
- Freight-absorption pricing – The seller who is anxious to do business with a certain customer or geographical area might use freight-absorption pricing. This strategy involves absorbing all or part of the actual freight charges in order to get the desired business. It is used for market penetration and to hold on to increasingly competitive markets.

International pricing: A wide variety of internal and external conditions can affect a marketer’s global pricing strategies. Internal influences include the firm’s goals and marketing strategies, the costs of developing, producing and marketing its products, the nature of the products and the firm’s competitive strengths. External influences include general conditions in international markets, especially those in the firm’s target markets, regulatory limitations, trade restrictions, competitors’ actions, economic events, customer characteristics and the global status of the industry. In general, a firm can implement one of three export pricing strategies, as described below.

- Standard worldwide price – Exporters often set standard worldwide prices, regardless of their target markets. This strategy can succeed if foreign marketing costs remain low enough that they do not impact overall costs, or if their prices reflect average unit costs. A firm that implements a standard pricing program must monitor the international marketplace carefully, however, to make sure that domestic competitors do not undercut its prices.
- Dual pricing – It distinguishes prices for domestic and export sales. Some exporters practice cost-plus pricing to establish dual prices that fully allocate their true domestic and foreign costs to product sales in those markets. Others opt for flexible cost-plus pricing schemes that allow marketers to grant discounts or change prices according to shifts in the competitive environment or fluctuations in the international exchange rate.
- Market-differentiated pricing – It makes even more flexible arrangements to set prices according to local marketplace conditions. Effective market-differentiated pricing depends on access to quick, accurate market information.

Case study: Dynamic pricing – smart pricing?

DHL used to have one-price-fits-all list prices for shipping packages in the United States and around the world, and when potential customers called for rates DHL scared them off by asking for more than FedEx or UPS. With Web pricing tools, DHL tested the market by offering cold callers different prices to see how low prices could go and still make a profit. In the end, DHL wound up changing hundreds of prices. There were plenty of surprises. Most prices did go down, but the company did not have to match the competition. In fact, by lowering prices a bit, DHL's "ad hoc" business not only stabilized but it also grew. For instance, of people who called to get a quote, 17% actually shipper prior to the pricing overhaul. The new prices have increased the ratio to nearly 25%.

Constant price revision, however, can be tricky where consumer relationships are concerned. Research shows it tends to work best in situations where there is no bond between the buyer and the seller. One way to make it work is to offer customers a unique bundle of products and services to meet their needs precisely, making it harder for them to make price comparisons. This tactic is being used to sell software, which is vulnerable to price wars because the cost of producing more copies is near zero. Application service providers are 'renting' their software and support by the month instead of selling an unlimited-use license.

The tactic most companies favour, however, is to market perfect pricing as a reward for good behaviour rather than as a penalty. For instance, shipping company APL, Inc., rewards customers who can better predict how much cargo space they will need with cheaper rates for booking early. Customers are getting savvier about how to avoid buyer's remorse. They are changing their buying behaviour to accommodate the new realities of dynamic pricing – where prices vary frequently by channels, products, customers and time.

Questions

1. Under what conditions will dynamic pricing be smart and successful pricing?
2. Explain the success of DHL's ad-hoc business from a pricing perspective.

Activity

Read the Pricing lesson's learning goals that follow and consider the questions for each goal. Answering these questions will reinforce your understanding of the key concepts in this unit and allow you to check how well you have achieved these learning goals. Where a blank appears before a question, answer with *true* or *false*; for multiple choice questions, circle the letter of the correct answer.

Major categories of pricing objectives

1. _ _ _ _ Pricing objectives include all of the following except
    a. profit maximization objectives
    b. meeting competitors' prices
    c. market-share objectives
    d. quality performance objectives
    e. prestige objectives
2. _ _ _ _ Profits are
    a. the most important objective for a firm
    b. the result of supply and demand
    c. a function of revenue and expenses
    d. depend primarily on the quantity of product sold

The concept of price elasticity and its determinants

3. _ _ _ _ Elasticity measures the responsiveness of manufacturers and distributors to inventory levels
4. _ _ _ _ If customers can easily find close substitutes for a good or service, producers tend to encounter elastic demand for it.

Major cost-plus approaches to price setting

5. _ _ _ _ Cost-plus pricing methods include incremental cost pricing and full cost pricing
6. _ _ _ _ Full cost pricing bases decisions on competition and demand for the product

Major issues related to price determination in international marketing

7. _ _ _ _ Global pricing strategies almost always depend on demand in the domestic market

8. _ _ _ _ A firm's global pricing strategy reflects its global marketing strategy

Comparing alternative pricing strategies

9. _ _ _ _ Marketers often practice penetration pricing in industries with few products and little competition
10. _ _ _ _ A skimming pricing strategy sets a high market-entry price for a product with little or no initial competition

Pricing policy decisions that marketers must make

11. _ _ _ _ Marketers follow pricing policies in making long-term competing pricing decisions
12. _ _ _ _ Pricing policy choices includes psychological pricing, price flexibility, product line pricing and promotional pricing

Relating price to consumer perceptions of quality

13. _ _ _ _ In general, consumers perceive a high price as a symbol of high quality
14. _ _ _ _ Price limits are directly associated with supply and demand
15. _ _ _ _ The concept of price limits suggests that unusually low prices may indicate poor quality

Price negotiations

16. _ _ _ _ Buyers and sellers negotiate prices most often when
    a. Multiple suppliers compete for an order
    b. Only one available supplier can fill an order
    c. Contracts over unchanging and routine purchases
    d. Prices are set once and remain unchanged

Alternative strategies for pricing exports

17. _ _ _ _ Firms almost always implement the same pricing strategies for domestic and export sales
18. _ _ _ _ Market-differentiated pricing allows a firm to price its products according to local marketplace conditions

Answer key

1. d
2. c
3. F
4. T
5. T
6. F
7. F
8. T
9. F
10. T
11. F
12. T
13. T
14. F
15. T
16. a
17. F
18. T

Glossary of terms

Price – The exchange value of a good or service

Profit maximization – The point at which the additional revenue gained by increasing the price of a product equals the increase in total costs

Target return objective – A short-run or long-run pricing practice intended to achieve a specified return on either sales or investment

Value pricing – A pricing strategy that emphasizes benefits a product provides in comparison to the price and quality levels of competing offerings

Demand – A schedule of the amounts of a firm's product that consumers will purchase at different prices during a specified time period

Supply – A schedule of the amounts of a good or service that a firm will offer for sale at different prices during a specified time period

Elasticity – A measure of the responsiveness of buyers and suppliers to changes in price

Cost-plus pricing – The practice of adding a percentage or specified amount (as markup) to the base cost of a product to cover unassigned costs and provide a profit

Price skimming – A pricing strategy involving the use of a high entry price relative to competitive offerings

Penetration pricing – A pricing strategy involving the use of a relatively low entry price as compared with competitive offerings to help secure initial market acceptance

Psychological pricing – A pricing policy based on the belief that certain prices or price ranges make a good or service more appealing than others to buyers

Product line pricing – The practice of setting a limited number of prices for a selection of merchandise

Promotional pricing – A technique that temporarily lowers prices below normal levels in a temporary marketing campaign

By-product pricing – Setting a price for by-products in order to make the main product's price more competitive

Captive-product pricing – Setting a price for products that must be used along with a main product

FOB-origin pricing – A geographic pricing strategy in which goods are placed free on board a carrier; the customer pays the freight from the factory to the destination

Going-rate pricing – Setting price based largely on following competitors' prices rather than on firm's costs or demand

Mark-up – The percentage of the cost or price of a product added to cost in order to arrive at a selling price

Product-bundle pricing – Combining several products and offering the bundle at a reduced price

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Unit – IV

Place (Marketing Channels)

Lesson 4.1 **Nature of marketing channels**

Lesson 4.2 **Structure and design of marketing channels**

Lesson 4.3 **Retailers and Wholesalers**

Lesson 4.1

MARKETING CHANNELS

At the end of the chapter, you will be familiar with

- What are marketing channels?
- Types of channel flows
- Functions of distribution channels

What's new in marketing channels in India?

Project Shakti: Among the new channels is Project Shakti, which is already operational in 11 states. The vision is to reach over 100,000 small villages, touching over 100 million rural Indians. Project Shakti provides micro-enterprise opportunities for women from Self-help Groups, making them direct-to-home distributors of HLL. The 'Shaktiammas' work as brand ambassadors for HLL and they sell its products directly to village consumers at their homes.

Hindustan Lever Network: Hindustan Lever Network leverages the opportunity of Direct Selling, and already presents customized offerings in 11 Home & Personal Care and Foods categories. With a consultant base of over 250,000 entrepreneurs, it operates in over 1,500 towns and cities, covering 80% of the urban population. Out-of-Home Opportunity: HLL is also aggressively responding to the rapidly growing trend of out-of-home consumption. The company is already the largest in hot beverages vending with over 15,000 tea and coffee vending points. This is being aggressively expanded in offices, the burgeoning services sector and, through specially designed kiosks, in the education, entertainment, leisure and travel segments. Health & Beauty Services: To respond to the increasing consumer need for health and beauty services and products, HLL has pioneered Lakme Salons and Ayush Therapy Centres. Lakme already has 64 salons in 26 cities, servicing over 4 lakh consumers a year. The Ayush Therapy Centres provide easy access to authentic Ayurvedic treatments and products, addressing the ever-growing concern for health among consumers. Mr. Banga of HLL concluded, "Our distribution initiatives create significant employment and vocational opportunities. Our countrywide network of 7,000 Stockists and 6,000 sub-stockists employs over 60,000 people. In our current channels, we work with the local retail trade, which has dispersed ownership and already involves a large number of people. Our new initiatives by themselves create large vocational opportunities for people. Hindustan Lever Network aims to create over a million self-employed entrepreneurs. Project Shakti aims to engage 25,000 underprivileged rural women, giving them economic independence. Services, by their very nature, are employment intensive and will also provide significant employment. All our channel initiatives are thus completely aligned with the national interest and priority of employment generation."

One of the major purposes of marketing is to satisfy the human needs and wants by delivering products to buyers when and where they want them at a reasonable cost. One of the key aspects we find in this process is *delivery*. Over the past two decades, economic clout has shifted from the producers of goods to distributors of goods. The shift in economic power has been significant in the retail level of marketing channels, where mass merchandisers like Wal-Mart, Big Bazaar have become dominant players. As a strategic marketing tool, the distribution channels had for many years taken something of a backseat to the other three strategic areas of the marketing mix namely the product, price and promotion. Today there has been a shift in the emphasis and this has been credited to four developments, viz.

- Explosion of information technology and e-commerce
- Greater difficulty of gaining a sustainable competitive advantage
- Growing power of distributors especially retailers
- The need to reduce distribution costs

DEFINING DISTRIBUTION CHANNELS

Different people perceive marketing channels in different ways, some see it as a route taken by a product as it moves from the producer to the consumer, and others describe it as a loose coalition of business firms that have come together for purpose of business. Customers may view marketing channels as simply 'a lot of middlemen' standing between the producer and the product. Given all these different perspectives it is not possible to have one single definition for marketing channels. Marketing channels can be defined as the external contractual organization that management operates to achieve its distribution objectives.

There are four terms in this definition that has to be given a special mention namely *external, contractual organization, operates and distribution objectives*. The term **external** means that the marketing channel exists outside the firm. Managing of the marketing channel therefore involves the use of interorganizational management (managing more than one firm) rather than intraorganizational management (managing one firm). The term **contractual organization** refers to those firms who are involved in the negotiatory function as the product moves from the producer to the end user. The function of these firms involves buying, selling and transferring of goods and services. Transportation companies, public warehouses, banks ad agencies do not come under these and are referred to as facilitating agencies. The third term **operates** suggests the involvement of management in the channels and this may range from the initial development of the channel structure to the day-to-day management. Finally the **distribution objectives** explain the distribution goals the organization has in mind. When the objectives change, variations can be seen in the external contactual organizations and the way in which the management operates. In simpler terms a channel then consists of producer, consumer and any intermediary.

Marketing channel strategy is one of the major strategic areas of marketing. In most cases eliminating middlemen will not reduce prices, because the amount that goes to the intermediaries compensates them for the performance of tasks that must be accomplished regardless of whether or not an intermediary is present. In simple terms, *a company can eliminate intermediaries but cannot eliminate the functions they perform.*

FLOWS IN MARKETING CHANNELS

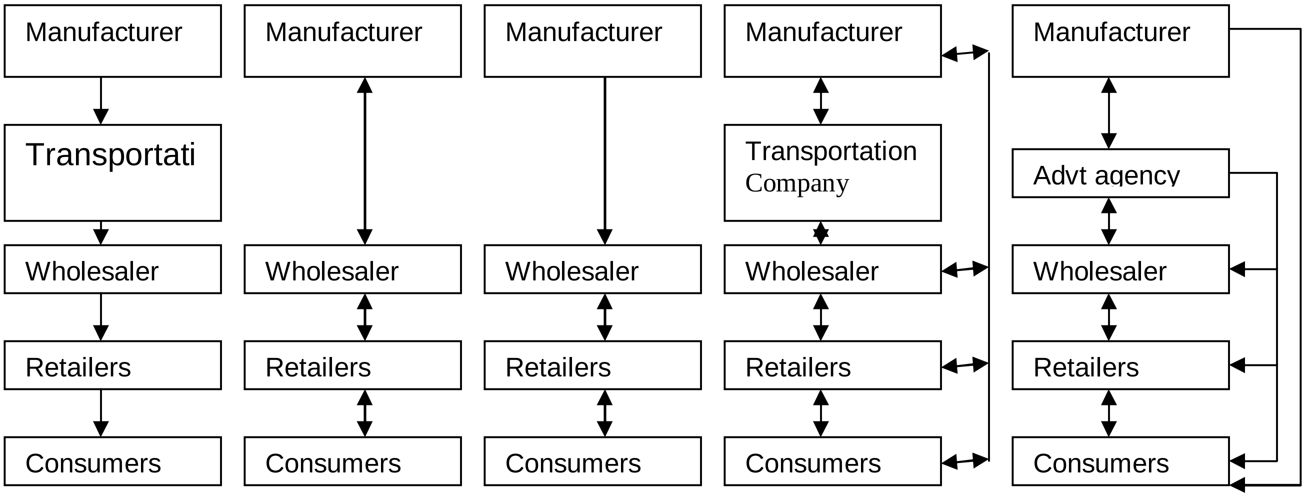
As discussed a conventional channel of distribution consist of a manufacturer, a wholesaler, a retailer and the ultimate consumer. Not all the channels include all these marketing institutions. At times the product passes directly from the manufacturer to consumer. When a marketing channel has been developed a series of flows emerge. These flows provide the links that tie channel members and other agencies together in the distribution of goods and services. There are five most important flows namely

- Product flow

- Negotiation flow
- Ownership flow
- Information flow
- Promotion flow

4.1 Flows in the Marketing channel

Product Flow Negotiation Flow Ownership Flow Information Flow Promotion Flow


Manufacturer
Transportati
Wholesaler
Retailers
Consumers
Manufacturer
Wholesaler
Retailers
Consumers
Manufacturer
Wholesaler
Retailers
Consumers
Manufacturer
Transportation Company
Wholesaler
Retailers
Consumers
Manufacturer
Advt agency
Wholesaler
Retailers
Consumers

The orgin and concept of flows in marketing channels is generally attributed to Ronald S. Valie, E.T Grether and Reavis Cox

The **Product flow** refers to actual physical movement of the product from the manufacturers through all the parties who take physical possessions of the product from the point of production to the final consumer.

In the **negotiation flow**, this represents the interplay of the buying and the selling functions associated with the transfer of title. If you note the diagram you find the transportation firm is not included in the flow because it does not participate in the negotiation function, also you can find the arrows flow in both the directions, indicating the negotiation is mutual at all levels of the channels. The ownership flow shows the movement of the title to the product as it is passed along from the manufacturer to the consumer, here as well we find the transportation function missing since the transportation firm does not take title or is actively involved in the facilitating function. It merely involves in transporting physical products

In case of the **Information flow**, we can see that the transportation function has reappeared and all the arrows are two-directional. All the parties participate in the exchange of information. For example Coke may obtain information from the transportation company about its shipping schedules and the rates, while the transportation firm may seek information regarding when and in what quantities it plans to ship its products. Some times the information bypasses the transportation company directly to the wholesaler or the retailer when the information does not concern the transportation firm. If there is an offer, or a price reduction these information are not needed by the transportation firms.

Finally the **Promotion flow** refers to the persuasive communication in the form of advertising, personal selling, publicity. There is a new component that is added to the flow and that is the advertising agency and this actively provides and maintains the information flow. The organizations work closely with the promotional organizations so we find a two-directional arrow.

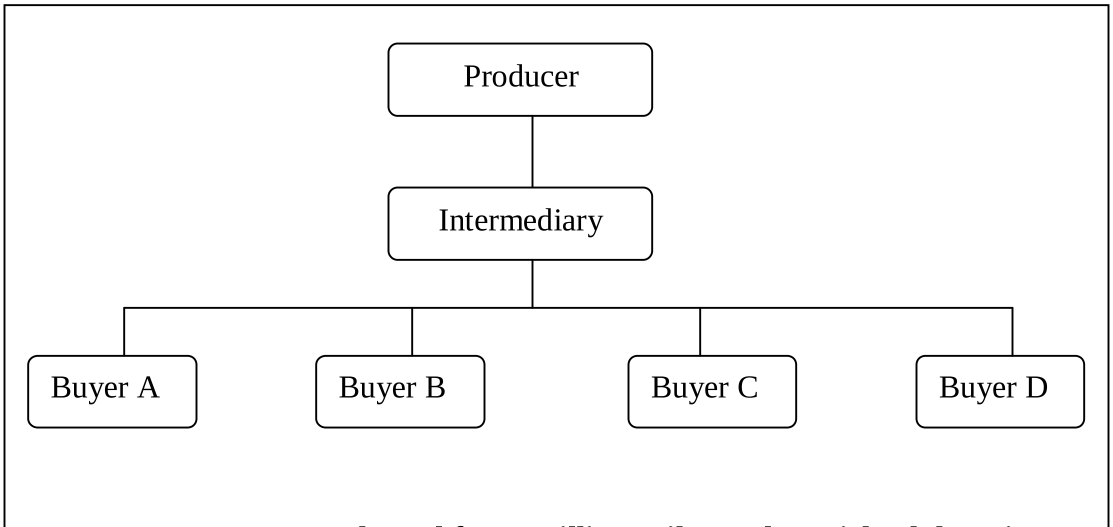
From the management view, the concept of channel flows provides a useful framework for understanding the scope and complexity of channel management. Changing scenario does make the role of the firms' complex, as a result of which innovative channel strategies and effective channel management are needed to make this happen.

FUNCTIONS OF DISTRIBUTION CHANNELS

Some of the major functions performed by the intermediaries are mainly *physical distribution, communication and facilitating functions*. When we talk about physical functions, they include braking bulk, accumulating bulk, creating assortments, reducing transactions and transporting and storing.

Breaking bulk: One of the important role intermediaries perform is bulk-breaking function. Here these organizations buy in large quantities and break them into smaller quantities and pass them to the retailers, wholesalers or even to the customers. By doing so, the intermediaries reduce the cost of distribution for the manufacturers as well as the consumers. This particular function is also termed as 'resolution of economic discrepancies'. Exhibit 4.2 gives a pictorial description of bulk breaking

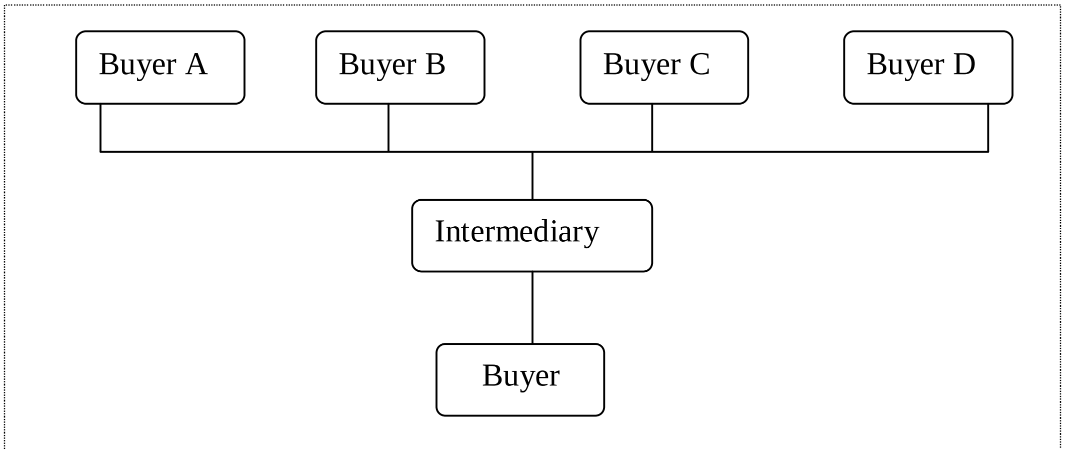
4.2 Bulk-breaking function



Adapted from William Zikmund &Michael d'Amico,

Accumulating Bulk: At times the intermediaries also do the task of accumulating the bulk. The intermediaries may buy bulk from different small producers accumulate them and offer to those buyers who prefer large quantities. The intermediaries in accumulating the bulk are mostly found in the agricultural businesses, whereby the intermediary will procure vegetables from local farmers and assemble them and sell it to the wholesalers. Exhibit 4.3 gives a clear picture on accumulating bulk. Once the marketers accumulate bulk they start to sort the products identifying differences in the quality, grades and classify them into different categories

4.3 Bulk-accumulating Function

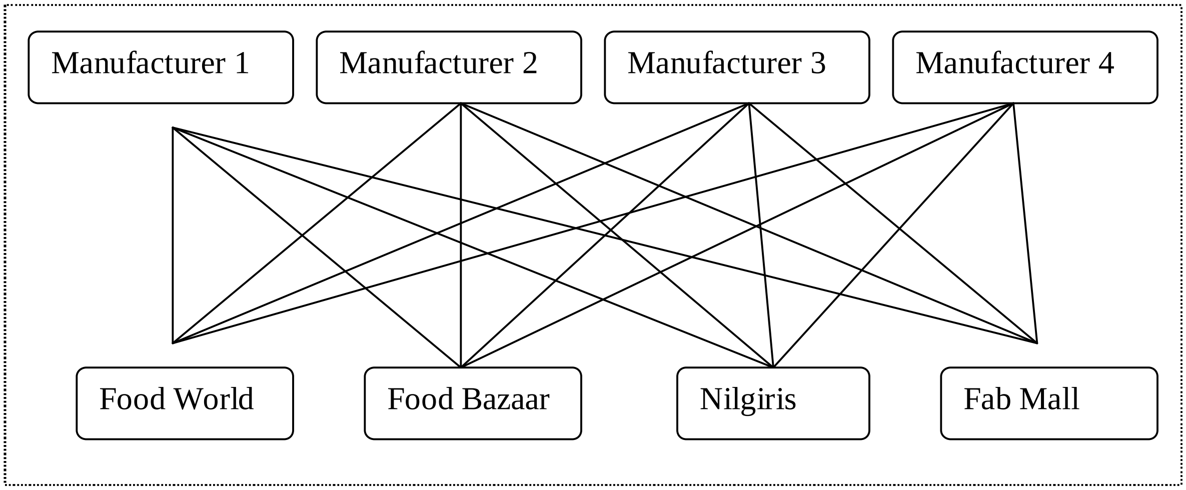


Adapted from William Zikmund &Michael d'Amico,

Creating Assortments: The third important function of the intermediaries is creating assortment. When we take the case of magazines, on an average there are around thousands of magazines being published in a month and it is impossible for a particular newsstand to get it going, here big distributors and agents work in creating assortments and enable a speedy process. This needs a lot of teamwork and timing. Certain magazines become outdated within certain period of time.

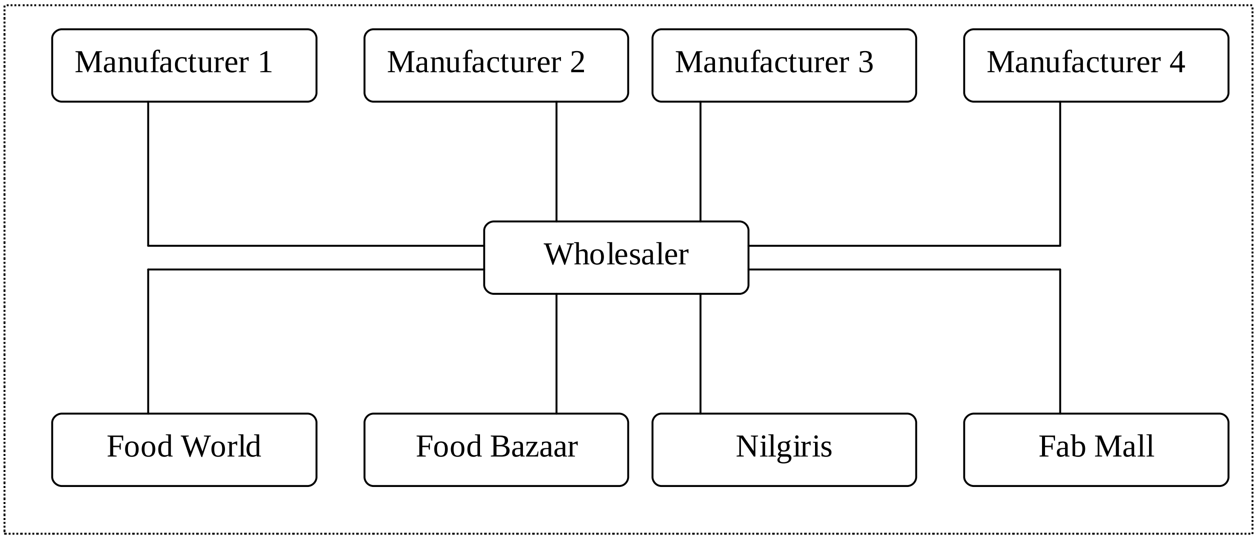
Reducing Transactions: One of the biggest reasons that keep the economy moving and the customer smiling is the presence of intermediaries, they reduce the number of transactions necessary to accomplish the exchange of goods. Exhibit 4.4 shows the complicated nature of the transaction if an intermediary does not come in place

4.4 Transaction without an intermediary



In the above exhibit, we find that it becomes a complicated process for the manufacturers to work on with different retailers, when a intermediary comes in the form of a wholesaler we find the whole situation becomes different. Intermediaries do not only reduce the number of transactions but also help in the reduction of the geographical distances that both buyers and sellers have to cover. Channel intermediaries doing the roles of a buying agent for their customer and selling agents for the manufacturers does simplify the process of transaction considerably From exhibit 4.5, we find the reduction in the number of transactions that happen between the manufacturer and the retailer.

4.5 Reduction of transactions by an intermediary



Transporting and Storing: Apart from breaking, accumulating, creating assortments and reducing transactions they also perform two key marketing functions namely transporting and storing. The final product has to be moved from the point of production to the point of consumption. This means it involves storing the product along the way till it is delivered. Most of the big retailers hold enough of the product in order to cater to the consumers

Credit Services: Apart from the function of physical distribution the intermediaries also help in offering credit services. Even though there are firms like Metro, which are predominantly cash and carry kind of intermediaries, most of the intermediaries provide credit facility or even paying in parts. Many intermediaries offer about 30 to 45 days to the retailers for paying back.

Risk Taking: one of the vital functions of the intermediaries is risk taking. Not every product finds favor in the eyes of the customer, much fallout within few months, as a result of which the intermediaries would be at risk. An uncontrollable factor like floods, earthquakes or even contamination or fire could pose a serious threat. The intermediaries have to bear these risks along with the market risks. These are some of the core functions intermediaries perform enabling goods and services to reach consumers at the right time

Lesson 4.2

STRUCTURE AND DESIGN OF MARKETING CHANNELS

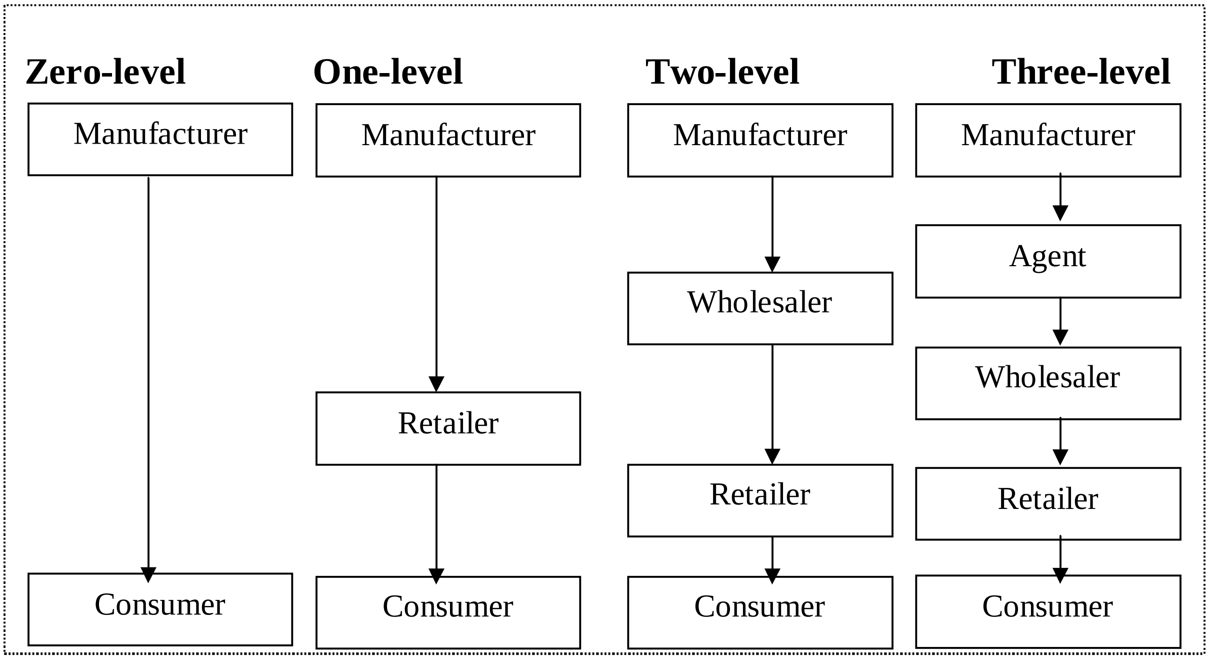
At the end of the chapter, you will be familiar with

- Marketing channel structure and its levels
- Channel structure in consumer and industrial markets
- Designing distribution channels
- Channel dynamics
- Channel conflicts

CHANNEL STRUCTURE

Channel structure is distinguished on the basis of the number of intermediaries. There are different levels in a channel structure. The common levels are zero-level, one-level, two-level, three-level. Each level presents both opportunities and challenges for the marketer. Exhibit 4.6 gives a picture of the different levels

4.6 Typical channel structure for Consumer Goods


Zero-level
Manufacturer
Consumer
One-level
Manufacturer
Retailer
Consumer
Two-level
Manufacturer
Wholesaler
Retailer
Consumer
Three-level
Manufacturer
Agent
Wholesaler
Retailer
Consumer

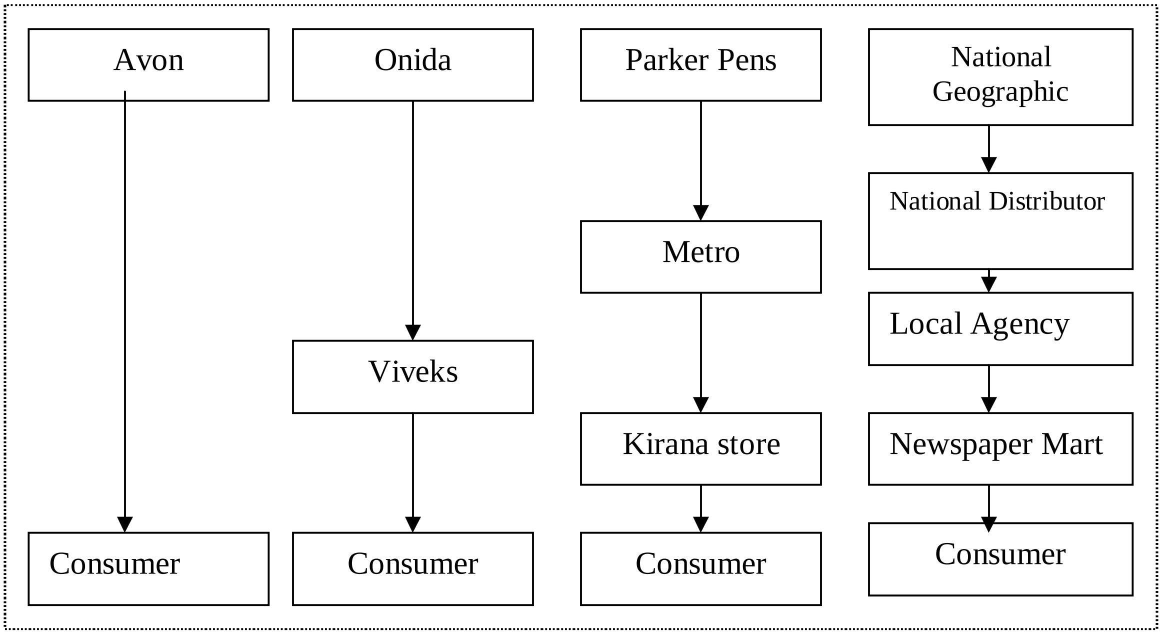
Zero-level structure is one of the simplest forms of the channel structure. Here organizations like Avon, Eureka Forbes use direct selling mode to take the products from their production houses to the consumers directly. A lot of money has to be spent in order to make this channel structure effective, as there is no third party to take your product to the consumer. Even a bakery can come as a firm, which bakes cakes and sells it directly to the consumers. Marketers who use the mailing services, toll-free numbers are also using this service.

One-level structure is one in which we have one intermediary acting as a link between the manufacturer and the consumer. Here the retailers procure goods directly from the manufacturer and supply it to the consumers. Retailers like Viveks, Wal-Mart deal directly with the manufacturer. In some cases in order to retain profitable and reputed retailers the manufacturers act as wholesalers. One of the advantages for the intermediaries is the customization and the discounts they receive.

Two-level channel has two people interceding before the product reaches the consumer. Here there would be a wholesaler and a retailer who takes the efforts for a speedy delivery and this is one of the most commonly used structures for consumer goods. In the case of Metro, most of the small retail and Kirana stores buy all the merchandise from Metro and in urn sell them to the consumer. One of the advantages of the four-level structure is the benefit of using the wholesaler in the distribution of services.

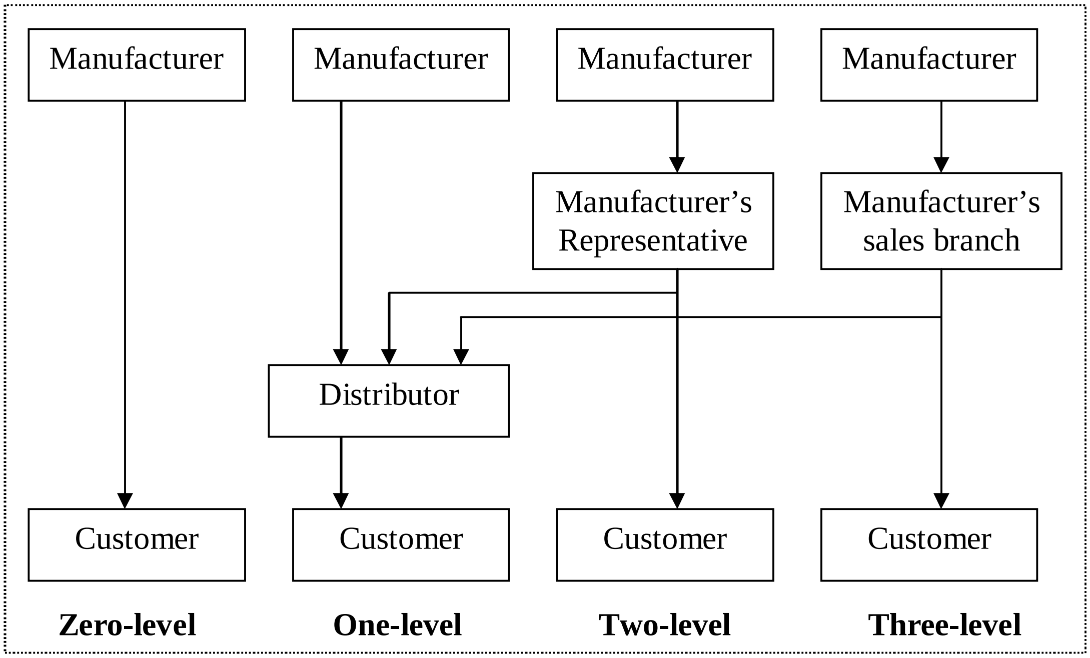
Three-level channel happens predominantly when the firms plans to go global. When a manufacturer enters another country, it always holds good when he uses the help of agents to operate in that environment. The agents are people who know the legal procedures and who can negotiate with the host country in case of a problem. Most of the airline firms that operate in different countries take the help of agents to penetrate the market

4.7 Example for Consumer Markets


Avon
Onida
Parker Pens
National Geographic
National Distributor
Metro
Local Agency
Viveks
Kirana store
Newspaper Mart
Consumer
Consumer
Consumer
Consumer

When it comes for Business-to-Business operations, the channels differ from the consumer markets, in this structure, firms predominantly may use their existing sales force to sell the products to the customers, they may even use industrial distributors to take their products to the industrial customers. Exhibit 4.8 details the Business-to-Business model of channel structure

4.8 B2B Marketing Channels


Manufacturer
Manufacturer
Manufacturer
Manufacturer
Manufacturer's Representative
Manufacturer's sales branch
Distributor
Customer
Customer
Customer
Customer
Zero-level
One-level
Two-level
Three-level

Mark Andy is one of the big names in the printing machines industry. In India Mark Andy supplies its printing machines to the industrial customers through Heidelberg, an industrial distributor. It also has its own representatives who pitch in when the customer needs information. In case of Industrial Channel, the zero-level, one-level and two-level are the most commonly used method. When it comes for Business-to-Business channels agents become the integral point of the whole process, since the characteristic of the business-to-business market is oligopolistic and are huge buyers.

In this digital economy, a shift has started in the channels on either side of the markets i.e. in both the consumer marketing channels and the business-to-business market channels. The web has created a platform whereby organizations can now directly communicate with the customers, as a result of which many of the channels are being disintermediated. This disintermediation does not necessarily mean that they completely eliminate the intermediaries, but rather when it comes to shipping the products it may outsource some of the distribution functions like the storage, transportation from third party firms.

DESIGNING DISTRIBUTION CHANNELS

Channel design refers to those decisions that involve in the development of new marketing channels or modifying the existent ones. The channel design decision can be broken down into six steps namely:

1. Recognizing the need for channel design decision
2. Setting and coordinating distribution objectives
3. Specify the distribution tasks
4. Develop alternative channel structures
5. Evaluate relevant variables
6. Choose the best channel structure

1. Recognizing the need for a channel design decision

First and foremost task for the organization is to recognize the need for a channel design. An organization would go in for a new channel design for the following reasons namely

-When a new product or product line is developed, mainly when the existing channels are not suitable for the new line

-When the existing product is targeted to a different target market. This is common when an organization is used to catering the B2B, plans to enter the consumer market

-When there is a change in the marketing mix elements, when an organization reduces its prices on certain offering the channel worked out will be based on the price points, they may look in for discounters

-When facing major environmental changes namely in economic or technological or in legal spheres.

-Finally when the organization opens up new geographic marketing areas

The list by no means is comprehensive, but gives a picture about some of the most common conditions when channel design decisions are worked out.

2. **Setting and Coordinating Distribution Objectives**

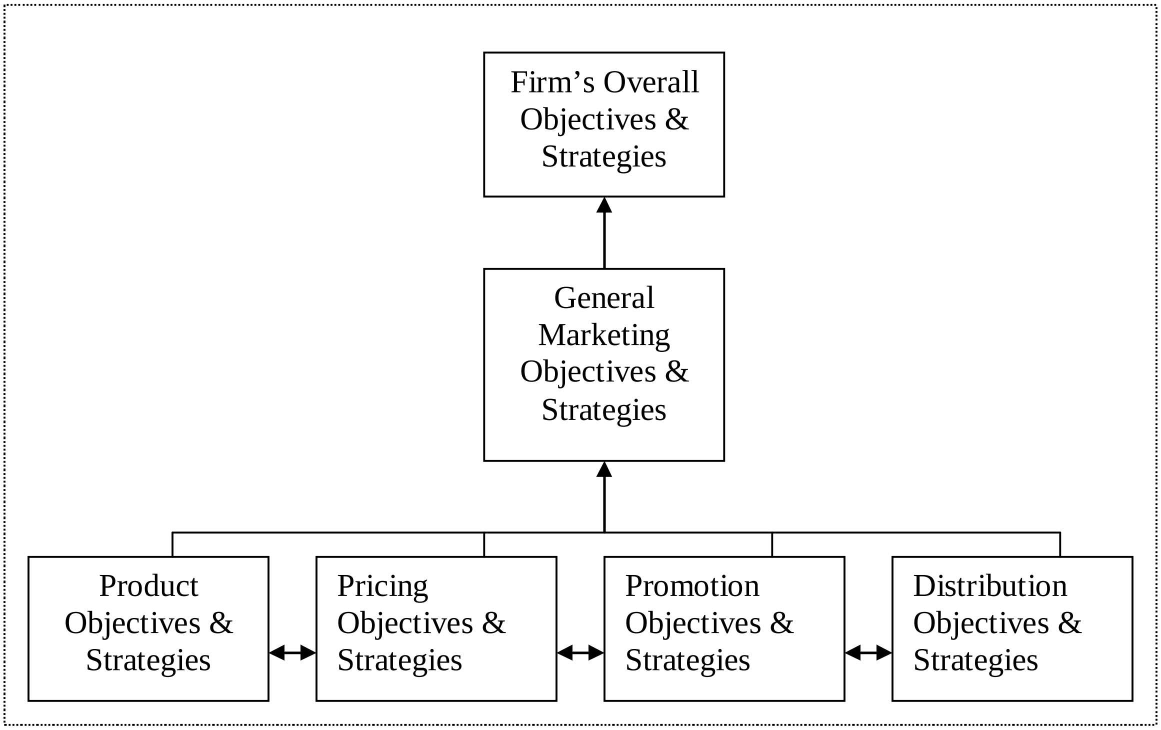
Once a need for a design is recognized the next task for the channel manager is to work out to develop the channel structure, either form the scratch or by modifying the existing one. It is necessary for the channel manager to carefully evaluate the firm's distribution objectives. In order for the distribution objectives to be effective and well coordinated the channel manager need to perform three tasks namely

▪ Become familiar with the objectives and strategies in other marketing mix areas and other relevant objectives and strategies of the firm. In most cases the person or the group that sets the objectives of the other marketing mix elements will also set the objectives for distribution as well.

▪ Set the objectives and state them explicitly. A good objective is one, which is clear, and explicit, and has a greater role in achieving the firm's overall objectives. Some examples of a good distribution objectives are as follows, at the start of the new millennium, *Apple Computers set a distribution objective to reach more consumers with what it refers to as the 'Apple experience'. So, Apple reinvigorated and reestablished relationships with large retail chains, which it had neglected in recent years* .In the same way *Coca-Cola seeks to* *broaden its penetration in schools and college markets, as a result of which it has entered into contact with many schools and colleges, whereby these institutions would sell only Coca-Cola products on their campuses.*

- Check and see if the distribution objectives set are congruent with marketing and other general objectives and strategies of the firm. This involves verifying if the distribution objectives do not conflict with the objectives in the other areas of marketing mix or even to the overall objectives of the company. In order to cross check, it is essential to examine the interrelationships and hierarchy of the objectives of the firms. Exhibit 4.9 gives a clear picture of the same

Exhibit 4.9 Interrelationships & hierarchy of Objectives


Firm's Overall Objectives & Strategies
General Marketing Objectives & Strategies
Product Objectives & Strategies
Pricing Objectives & Strategies
Promotion Objectives & Strategies
Distribution Objectives & Strategies

3. **Specifying the Distribution Tasks**

Once the objectives are formulated, a number of functions need to be performed in order for the distribution objectives to be met. The manager therefore has to specify the nature of the tasks that needs to be carried out in order to meet the objectives. The tasks need to be precisely stated so that it meets the specified distribution objectives. For e.g. a manufacturer of a consumer product, say a high quality cricket bats aimed at serious amateur cricket players would need to specify distribution tasks such as gathering info on target markets shopping patterns, promote product availability to the target, maintain inventory, and timely availability, compile info about the product features, provide hands on experience using the product, process and fill customers orders, transport the product, arrange for credit provisions, provide warranty, provide repair and service, establish product return to make the offering readily available. Sometimes these functions may appear to be production oriented rather than distribution tasks, but when we talking about meeting customers, they are indeed distribution tasks.

4. **Developing Possible Alternative Channel Structures**

Once the tasks have been specified by the channel manager he should find out alternate ways of allocating these tasks. In most cases the channel manager chooses from more than one channel to reach the consumer effectively. Britannia would sell their biscuits thorough wholesale food distributor, departmental stores, convenience stores and even in pharmacies. Whatever may be the channel structure, the allocation alternatives should be in terms of (a) the number of levels in the channel (b) the intensity at various levels, and (c) the types of intermediaries.

The number of levels can be from two level upto five levels. The channel manager can think of going for a direct way of meeting the customers to using two intermediaries as an appropriate way. Intensity refers to the number of intermediaries at each level. Generally the intensities can be classified into three categories namely intensive, selective and exclusive. *Intensive saturation* means as many outlets as possible are used at each level of the channel. *Selective* means that not all possible intermediaries at a particular level are used. *Exclusive* refers to a very selective pattern of distribution. A firm like Parle may use intensive distribution channel structure, while Rolex may use high degree of selectivity. The types of intermediaries, third component has to be carefully dealt. The firms should not overlook new types of intermediaries that have emerged in recent years particularly the auction firms such as baazee, bid or buy as possible sales outlet for their products.

4.1. (A) ACTIVITY

Would you use exclusive, selective or intensive distribution for the following products?

- Maruthi Automobiles
- MTR food products
- Samsung Electronics

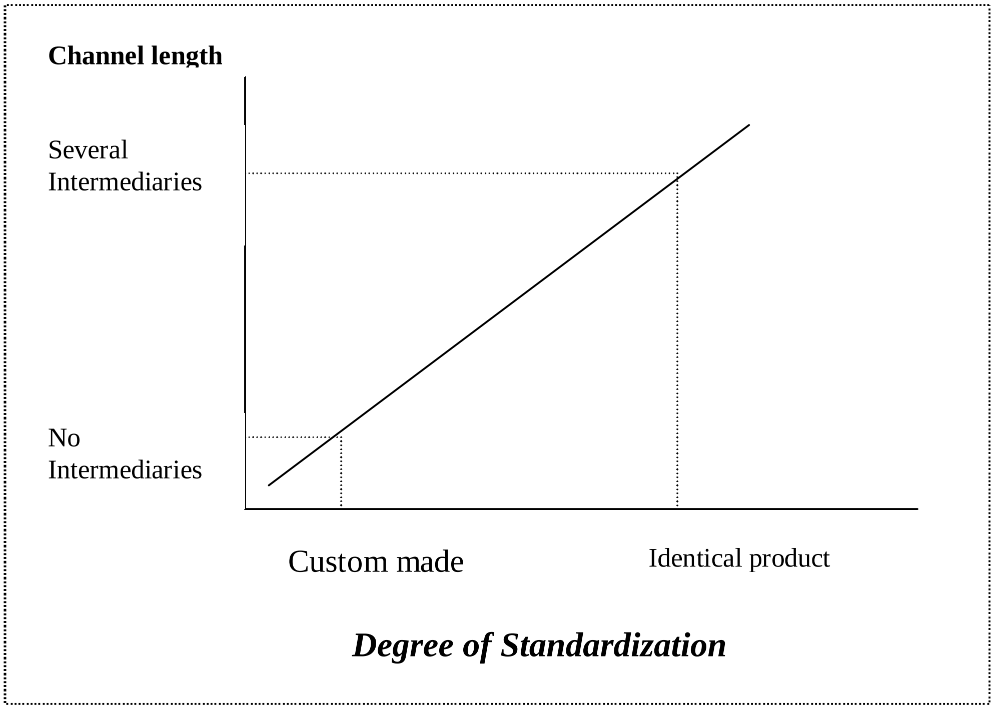
5. **Evaluating the variables affecting Channel structure**

Once the alternative structures have been outlined, each channel structure has to be evaluated on a number of variables. There are five basic categories namely,

Market variables - marketing management is based on the philosophy of marketing concept, which stresses on the consumers needs and wants, the managers have to take the cues from the market. The subcategories that have a greater influence on the market structure are market geography, market size, market density and market behavior

Product variables - some of the most important product variables are bulk and weight, Perishability, unit value, degree of standardization, technical vs. non-technical and newness. Heavy and bulky products have a high handling and shipping costs relative to their value. The manufactures of such products have to keep in mind to ship in large lots to a fewer possible points. It would always be better if the channel structure remains short. Food products, flowers are considered to be highly perishable. When products are highly perishable, the channel structure should be designed to provide rapid delivery from producers to consumers. One important consideration is lower the unit value of a product, the longer the channels should be as low unit value leaves small margins for distribution costs. Exhibit 4.10 explains the relationship between the degree of standardization and channel length. If the product flows directly from manufacturer or producer to the user the degree of customization is more, but as the product becomes more standardized it passes through many channels. Mostly the B2B machinery has a great degree of customization as it passes from the manufacturer to the industrial user, while many consumer market is predominantly a standardized one. When it comes for the technical component, the industrial products are mostly distributed through direct channels because of the technical expertise and service while many technical consumer products do use shorter channel structure. When the product is new and is in the introductory stage in order to capitalize on the aggressive promotion, a shorter channel is preferred to gain awareness.

Exhibit 4.10 Relationship between degree of standardization and channel length



Company Variables- the important variables that affect a good channel design are size, financial capacity, managerial expertise and objectives and strategies. Larger the firms in terms of size it enables them to exercise a substantial amount of power in the channel. The size does give flexibility for the firm in picking the channel structures. The same hold true when it comes for the financial capability. Greater capital available with a firm, less dependency is seen on the intermediaries. When a firm is into industrial marketing, it prefers to have its own sales force, warehousing, order processing capabilities and larger firms with good financial backing are better able to bear the high cost of these facilities. When a firm lacks quality managerial skills, a comprehensive channel structure ranging from wholesalers to brokers are needed to perform the distribution activity, once the firm gains experience it can change or reduce the number of intermediaries. The objectives and strategies a firm has may limit the use of intermediaries. These strategies may emphasis on aggressive promotion and may even alter the distribution tasks. Overall this is one of the prime variables used for evaluating.

Intermediary Variables- the important intermediary variables are availability, costs and services offered. The availability is one of the key variables as this influences the channel structure. If we take the case of Dell Computers, due to lack of a proper channel structure he designed a direct mail order channel, which provided a strong technical backup as well. The cost is another variable a channel manager considers. If the cost of using a particular intermediary is too high compared the services it offers the manager may consider in minimizing the use of intermediaries. The services performed by the intermediaries is another integral component, a good intermediary is one, which offers efficient services at the lowest cost.

Environmental Variables- the uncontrollable or the macro environmental forces may affect the different aspects of channel development and management. Forces like the Sociocultural, economic, technological, legal forces have a significant impact on the channel structure. The other variables are those the organization can work upon or change to the situation but the environmental forces are those the organization has to cope up with.

6. **Choosing the 'Best' Channel structure**

In deciding the manager should choose an optimal channel structure that would offer desired level of effectiveness at the lowest possible cost. Even though there is not one set method to pick an optimal channel structure, it all depends on the orientation of the firm. If the goal of the firm were profit maximization, the channel structure would be in line with the goal. Most channel choices are still however made on the basis of managerial judgment and the data that is available.

MANAGING CHANNEL MEMBERS AND THEIR CONFLICTS

After a particular channel is selected, the marketer must manage or administer the channel members or intermediaries. Managing channel members include

a. selecting intermediaries
b. motivating channel members or middlemen
c. controlling or managing channel conflicts, and
d. evaluating performance of channel members

Selecting intermediaries: Selection of intermediaries or middlemen is a continuous process because some of them leave the channel or get terminated by the marketer. Hence it is not part of channel design. It is necessary for the marketer to determine criteria or factors for selection of intermediaries. These criteria differ depending on the type of middlemen and the firm's particular product/market conditions. Some of the common factors considered are financial standing, location, prior experience and type of customers served.

Motivating middlemen: The marketer must continuously motivate his intermediaries to achieve long-term success. Motivating the intermediaries to achieve top performance should start with understanding the middlemen's needs, perceptions and outlook. The quality of support from middlemen will depend on the motivational techniques used and incentives offered.

Controlling channel conflicts:

Even though a manufacturer's channel design is well done, there will be some conflict because of the differences in the objectives and perceptions of the channel members. The conflicts or tensions between the channel members can damage channel performance. Marketers should periodically undertake surveys of intermediaries or conduct formal/informal discussions with them to assess the areas or sources of conflicts. Some of the sources of conflict are indicated in Exhibit 4.11.

	Sources of conflict	**Examples**
1.	Differences in objectives	Manufacturers want long-term profitability but middlemen prefer short-term
2.	Dealings with customers	Middlemen feel cheated when the manufacturer deals with large customers and asks them to serve small customers
3.	Differences in interests	The manufacturer feels that the middlemen are not giving attention to the firm's products. The middlemen are interested in products that are fast moving or have higher margins for them

4.	Differences in perceptions	The manufacturer wants the middleman to carry a higher inventory due to the perception of good market conditions. The middleman does not share this optimism
5.	Compensation	Manufacturer’s representatives (agents) feel that the commission percentage offered by the manufacturer is not adequate. The manufacturer thinks otherwise
6.	Unclear territory boundaries	The territory boundaries between middlemen are not clear, resulting in competition among the firm’s intermediaries to secure business from the same customers

Exhibit 4.11 Sources of channel conflicts

The channel conflicts can be controlled or managed in several ways, including:

- effective communication network
- joint goal-setting
- diplomacy
- mediation
- arbitration and
- developing a vertical marketing system (which is described in the next section).

An effective communication network between the manufacturer and the intermediaries can be developed through periodic formal and informal meetings and co-optation of intermediaries in board of directors or advisory committees. In joint-goal setting, the channel members come to an agreement on the super-ordinate (or fundamental) goals they jointly seek. Such goals can be market share leadership, customer satisfaction or product/service quality in a highly competitive market where survival and success of channel members depend on their performance and cooperation. The channel members may resort to diplomacy, mediation or arbitration, when conflicts are sharp. Diplomacy is used when the conflict is resolved through discussions between the persons from both the parties. In mediation a neutral third party tries to conciliate the interests of the two parties. In arbitration, both the parties present their arguments to a third party (i.e. the arbitrator) and agree to accept the arbitration decision.

Evaluating channel members:

It is a good policy for the marketer to evaluate the performance of each channel member periodically. An evaluation is useful to know which intermediaries are achieving favourable results and which are not. The intermediaries not performing well need to be counseled, re-trained, re-motivated or terminated. An evaluation data can also be used while deciding which type of middlemen to be used. The factors or criteria to be used for an evaluation of middlemen’s performance can include sales achieved versus sales quota, average inventory levels, customer delivery performance, customer complaints, cooperation in market feedback, support for new products and new customers generated.

CHANNEL DYNAMICS

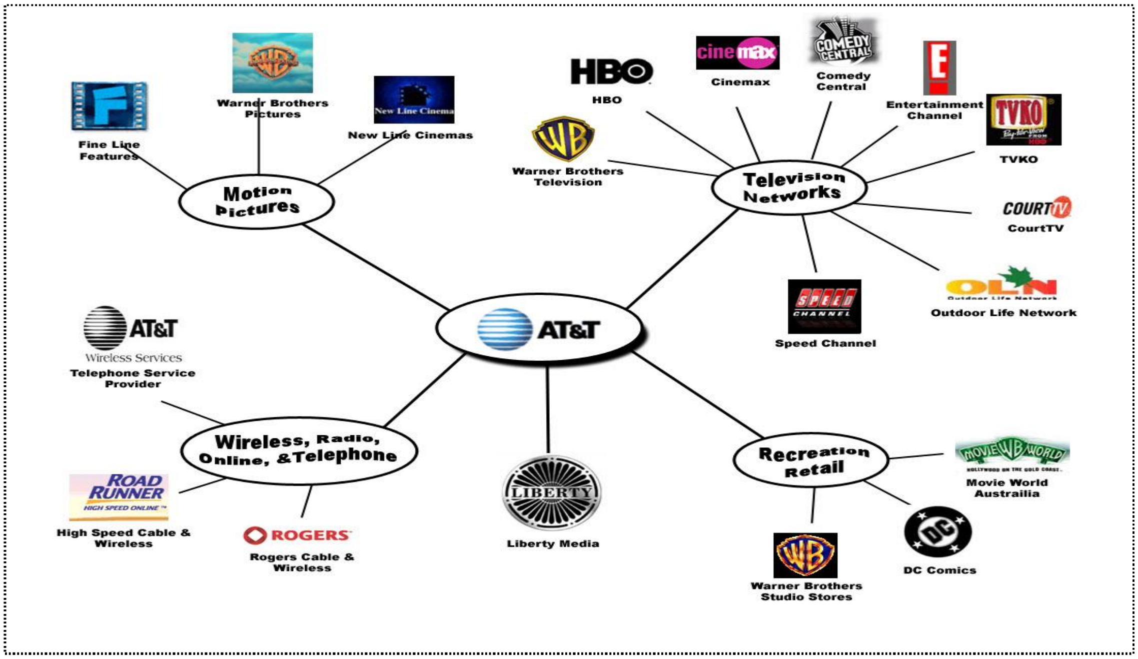
Like any other concept, channel systems do change according to the development and the need of the hour. With consumers becoming conscious of where they buy and how they want things to be delivered there has emerged different systems namely the vertical, horizontal and multichannel marketing systems.

The conventional or the traditional marketing channel encompasses a producer, one or few wholesalers and one or few retailers. The objective of theses different players is to see that they make enough profits, they are highly independent and don’t have control over other channel members. In contrast, the **Vertical Marketing System** (VMS) has the three members acting as one unified team, there is one channel member who owns the other members or allows franchising but ensures a greater role in the execution. Many organizations have started to operate in this format as strong channel members try to dictate terms for the producer as well as when they found the objectives of different channel members differ from that of the producer. There are three variants of vertical marketing system namely corporate, administered and contractual vertical marketing system. In case of corporate the organization combines the production and the distribution under one roof. Organisations like Asian paints, Amul are not only involved in the production of the products but they also own a considerable no of outlets. An administered vertical marketing system coordinates the production and distribution efficiencies but use their size as a dominant influence. HLL commands a greater shelf space or Samsung gets better displays in retail outlets purely because of their size and the reputation they carry with them. The third variant namely contractual vertical marketing system coordinates the activities of individual firms at different levels integrating their programs at contractual levels. Firms like McDonalds, KFC use this type of vertical marketing systems for the integration of their businesses.

The **Horizontal marketing systems** is one where two or more unrelated businesses come together pull in resources to exploit the emerging opportunities. Many private players especially banks have got into the act of tie-ups with retail stores or even with fuel outlets in order to gain greater market. ICICI bank has got tied with Big Bazaar, and this has greatly enhanced the reputation of both these firms as well as increasing the customer base respectively.

The **Multi-channel marketing systems** as the term simplifies it is one in which a firm uses multiple channels to reach different customer segments. In the present scenario most organizations have started to use multiple channel method because it helps in the expansion of the market coverage, it costs little when the target segment is small instead of using a bigger channel and mainly helps in customizing the offering according the need of the segments. Exhibit 4.12 gives an idea about the different products and AT & T uses different channels to reach out to different segments.

Exhibit 4.12 AT&T different products and segments



Warner Brothers Pictures
New Line Cinemas
Fine Line Features
Motion Pictures
HBO
Cinemax
Comedy Central
Entertainment Channel
TVKO
Warner Brothers Television
Television Networks
CourtTV
Outdoor Life Network
Speed Channel
AT&T
AT&T Wireless Services
Telephone Service Provider
Wireless, Radio, Online, &Telephone
High Speed Cable & Wireless
Rogers Cable & Wireless
Liberty Media
Recreation Retail
Movie World Austrailia
DC Comics
Warner Brothers Studio Stores

When distribution when goes overseas they are bound to face a lot of restraints and problems like the host country laws, the laws of the country to which the goods are shipped, the laws of the nations through which the goods pass must be abided by the company. Apart from this, other environmental factors do play an active role when considered from a macro-marketing perspective. In the next lesson, we deal with the role of retailers, wholesalers and logistics in this value chain and how do they facilitate the process of performing the channel function effectively

Key Terms

- Contractual Organisation
- Horizontal Marketing Systems
- Retailers
- Atmospherics
- E-tailers
- Vertical Marketing Systems
- Multichannel Marketing Systems
- Specialty store
- Convenience Stores
- Wholesalers

Glossary of terms

Horizontal Marketing System- Two or more unrelated businesses come together pull in resources to exploit the emerging opportunities

Marketing channels - The external contactual organization that management operates to achieve its distribution objectives

Multichannel Marketing System- A firm uses multiple channels to reach different customer segments

One Level structure- one intermediary acting as a link between the manufacturer and the consumer

Three Level structures- Firms when they go global they use the help of agents to take their products to the wholesalers and then to the retailers before reaching the end consumer

Two level structure- two people interceding before the product reaches the consumer

Vertical Marketing System- members acting as one unified team, there is one channel member who owns the other members or allows franchising but ensures a greater role in the execution

Zero Level structure- the product is moves from the manufacturer directly to the consumer without any intermediary

Lesson 4.3

RETAILERS AND WHOLESALERS

The objectives of this lesson are:

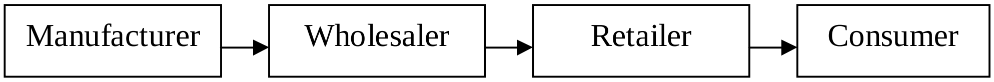
- To understand the concept of retailing
- Different Theories in Retailing
- Types of Retailers
- Retail strategy
- Wholesaling
- Types of Wholesalers

INTRODUCTION

Retailing is one of the largest sectors in the global economy. It employees almost 23 million people in United States alone, generating about $3 trillion in sales annually. About 50 organizations in the Fortune 500 are from the retail sector. Retail is one among the fastest growing industry. Consider Wal-Mart, the biggest retailer in the world with approximately $250 billion in sales was started in the early sixties, while Fortune came with its annual ranking of top 500 organizations in 1952, a year when nobody would have dreamt about Wal-Mart. In the early nineties for the first time Wal-Mart became the top organization according to Fortune Magazine, which it still continues to hold.

Retail is the buzzword today and this lesson explores the emerging retail scenario and the strategies available for different retail formats. Exhibit 4.2.1 shows that distribution of the product begins from the producer or the manufacturer and ends with the consumer, between them are the retailers who act as a link. The word '*retail*' is derived from the French word retaillier, meaning 'to cut a piece off' or 'to break bulk'.

Exhibit 4.2.1 Distribution Channel



Wholesalers buy products from manufacturers and sell them to retailers while retailers take the product from wholesalers to the consumers. While the wholesalers try to satisfy the retailers, the retailers make all the effort in satisfying the needs of the consumers. Retailing has become an intrinsic part of our everyday lives that and this has been evident with the nations that have enjoyed the greatest economic and social progress have been those with a strong retail sector. Retailing encompasses selling through mail, the internet, door-to-door visits apart from brick and motor stores.

INDIAN SCENARIO

Retailing is the second largest industry in India next only to agriculture and contributes to about 11 percent of the GDP; it is likely that India will have about 220 shopping malls by 2006 up from 25 in 2003. The sector provides employment for 8% of the total workforce of the country. The sector is highly fragmented and is dominated by large traditional formats. Even though the total retail businesses are estimated at $180 billion only 2 percent comes from the organized sector. According to one of the sources, the size of the organized retail was estimated at about Rs 16,000 crores in 2002-03. India has the largest retail density in the world with 12 million retail outlets for a population of over 1000 million.

In the organized retail there are few big names like RPG’s, viveks, Rahejas etc who dominate the market to a greater extent. From what was once considered a conservative and a traditional society India has emerged as the hot pot for every organization that even firms like Reliance, Mahindra’s are planning to foray into retail. According to the study conducted by the Euroconsumer study there has been an increase in the disposable income of the Indian middle class, apart from this the Indian middle and high income group is increasing by 10% annually over the last decade. Moreover the falling interest rates, easier consumer credits, varieties and different price points have all been credited to the booming retail market. The Urban customers have started to experience the western lifestyle, and they have become more demanding than ever before. Scenario has changed from what once was a forced way of buying has not led to the age where shopping is considered as an experience. The consumers are becoming highly knowledgeable and this in turn has had a positive effect on the consumers.

DRIVERS OF CHANGE

- Changing Demographics- One of the biggest reasons for the growth of retail in India is the changing demographics. The number of middle-income class and the people in the age group 18-35 has been ever increasing and this has changed the consumer’s preference. According to a world study India is considered as one of the youngest economies and this is helping in the growth of the sector.
- Emphasis on Convenience – With the ever-expanding cities and upcoming towns, people are becoming choosier with the things they buy and the places they shop. This has resulted in the emergence of new retail ventures trying to be niche in some area.
- Explosion of Knowledge and Technology- With the emergence of internet, people have become aware of what’s happening in the other part of the world and this has led him in comparing the prices, assortment, ambience etc. To cope up with this knowledge explosion different retail formats have emerged and this has made shopping more of fun and a experiences.
- Added Experimentation- Back in the 1980s, people were highly loyal to the brands they bought and the outlets they shopped, but the present generation of consumers like to experiment. Long back people never felt shopping for vegetables and groceries at retail outlets were a good idea, but things have changed and vegetable retailing has grown by 35 percent

FUNCTIONS OF RETAILING

Retailers perform four major activities in the value chain. They are:

1. Arranging assortment
2. Breaking bulk
3. Holding stock and,
4. Providing service

Each of these activities holds significance when the product gets transferred from the manufacturer or the wholesaler to the retailer. We will discuss about each of the activities in detail and their contribution in the value addition to the offering.

- Arranging Assortment- an assortment is a retailer’s selection of merchandise and this includes the length and breadth of the products. The assortment may include substitutable items of the same brands with different price points. Making decisions on the assortments is one of the crucial elements for a retailer; a small retailer makes decisions based on the perceptions he holds for a particular product and by past experiences. Those in the organized sector rely on future projections, past sales record and on detailed study on various factors that may affect the sales. Retailers need to consider other factors such as the store layout, the ambience, and merchandise mix to create an urge. Subhiksha one of the leading grocery and pharmaceutical chain in Tamil Nadu has an impressive assortment of only the fast moving brands and stock keeping units (SKU’s) rather than all that is available, while Food World positions itself as a one stop shop as a result of which it holds multiple brands. Subhiksha works on its layout, price (value for money) as it’s tool in reaching the consumer groups

In the News

Subiksha, the pharma and FMCG products retail chain in Chennai, uses price discounting as a major unique selling proposition. Subiksha offers a 10 per cent discount on the 'maximum retail price' of all products it sells. Foodworld and Vitan, both South-based, have also started offering sales promos and discounts on select products' MRPs

Source: www.etretailbiz.com

- Breaking Bulk- another activity that retailers perform is breaking bulk. Breaking bulk means physical repacking of the products by the retailers in small unit sizes according to the customer’s requirement and convenience. The retailers procure goods from the wholesalers in large quantities in order to reduce transportation costs and time. They further break the products or arrange them into convenient units. The entire operation not only adds value to the end user but also send a positive word of mouth about the manufacturer or the supplier. This particular function is losing its prominence due to the advent of the different categories like the ready to wear segment.

In the News

With big brands from textile companies growing weary in adapting to the fast-paced changing scenario in the ready-to-wear industry, it's the small brands, including private labels that are completely transforming the way men, women and children dress. A whole bunch of players have plunged into this branded ready-to-wear business. According to current KSA Technopak reports, the branded ready-to-wear segment contributes 21% to the apparel sector. And the present total market size of the ready-to-wear segment is pegged at around Rs 40,000 - 45,000 crore

Source:

- Holding Stock- the third activity retailers perform is holding stock. Retailers maintain appropriate levels of inventory. In the current scenario holding stock has got its own positives and negatives. Retailers have to face a negative consequence for holding unwanted stocks while at the same time keeping low stocks may affect the business. Based on the size of the retailer inventory decisions are worked. A large retailer uses specialized software's for maintaining inventory levels while small retailers use day to day transactions as a yardstick in maintaining the inventory
- Extending Service- the service the retailer's offer is more than just the core product. It may be an add-on to the core product itself. The add-ons may be the credit facility they may provide, after sales service or even providing information about the latest products to the customers. For the suppliers the retailers may provide with information pertaining to the trends in the market, information about a particular target group and even provide storing facility. Time zone, a part of the Titan group were the one of the pioneers in organized sector to some up with specialized people who were trained in handling any complexities in the instrument.

Activity

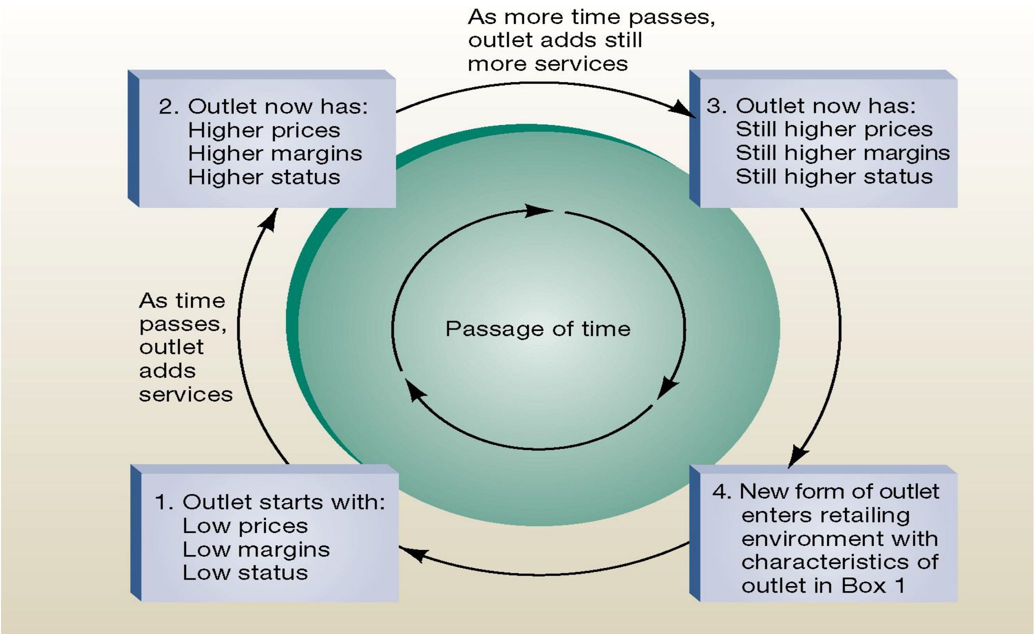
Visit a near by Kirana store and a departmental store, try to find out what different activities the retailers provide for the customers and the suppliers. Discuss your findings in a group. Check if you can find more activities that the retailers perform

THEORIES IN RETAIL

Like every other industry new retail firms have brought innovative approaches in retailing. Retail development can be looked at from different theoretical perspective, as no one theory is universally acceptable. The reason for this unacceptability is mainly because of different market conditions, different socio-economic conditions in the market. This session deals with the following theories namely

- Wheel of Retailing
- Retail Accordian Theory
- Theory of Natural Selection
- Retail life cycle

Wheel of Retailing


As more time passes, outlet adds still more services
2. Outlet now has: Higher prices Higher margins Higher status
3. Outlet now has: Still higher prices Still higher margins Still higher status
As time passes, outlet adds services
Passage of time
1. Outlet starts with: Low prices Low margins Low status
4. New form of outlet enters retailing environment with characteristics of outlet in Box 1

This theory talks about the structural changes in retailing. The theory was proposed by Malcomb McNair and according to this theory it describes how retail institutions change during their life cycle. In the first stage when new retail institutions start business they enter as low status, low price and low margin operations. As the retail firms achieve success they look in for increasing their customer base. They begin to upgrade their stores, add merchandise and new services are introduced. Prices are increased and margins are raised to support the higher costs. New retailers enter the market place to fill the vacuum, while this continues to move ahead as a result of the success. A new format emerges when the store reaches the final stage of the life cycle. When the retail store started it started low but when markets grew their margins and price changed. The theory has been criticized because they do not advocate all the changes that happen in the retail sector and in the present scenario not all firms start low to enter the market

Retail Accordian Theory

This theory describes how general stores move to specialized stores and then again become more of a general store. Hollander borrowed the analogy ‘accordian’ from the orchestra. He suggested that players either have open accordion representing the general stores or closed accordions representing narrow range of products focusing on specialized products. This theory was also known as the general-specific-general theory. The wheel of retailing and the accordion theory are known as the cyclical theories of retail revolution

Theory of Natural selection

According to this theory retail stores evolve to meet change in the microenvironment. The retailers that successfully adapt to the technological, economic, demographic and political and legal changes are the ones who are more likely to grow and prosper. This theory is considered as a better one to wheel of retailing because it talks about the macro environmental variables as well, but the drawback of this theory is that if fails to address the issues of customer taste, expectations and desires

Retail Life cycle

Like products, brands retail organizations pass through identifiable stages of innovation, accelerated development, maturity and decline. This is commonly known as the retail life cycle. Any organization when in the innovation stage is nascent and has few competitors. They try to create a distinctive advantage to the final customers. Since the concepts are new at this stage organizations try to grow rapidly and the management tries to experiment. Profits will be moderate and the stage may last for a couple of years. When we talk about our country e-buying or online shopping is in the innovation stage.

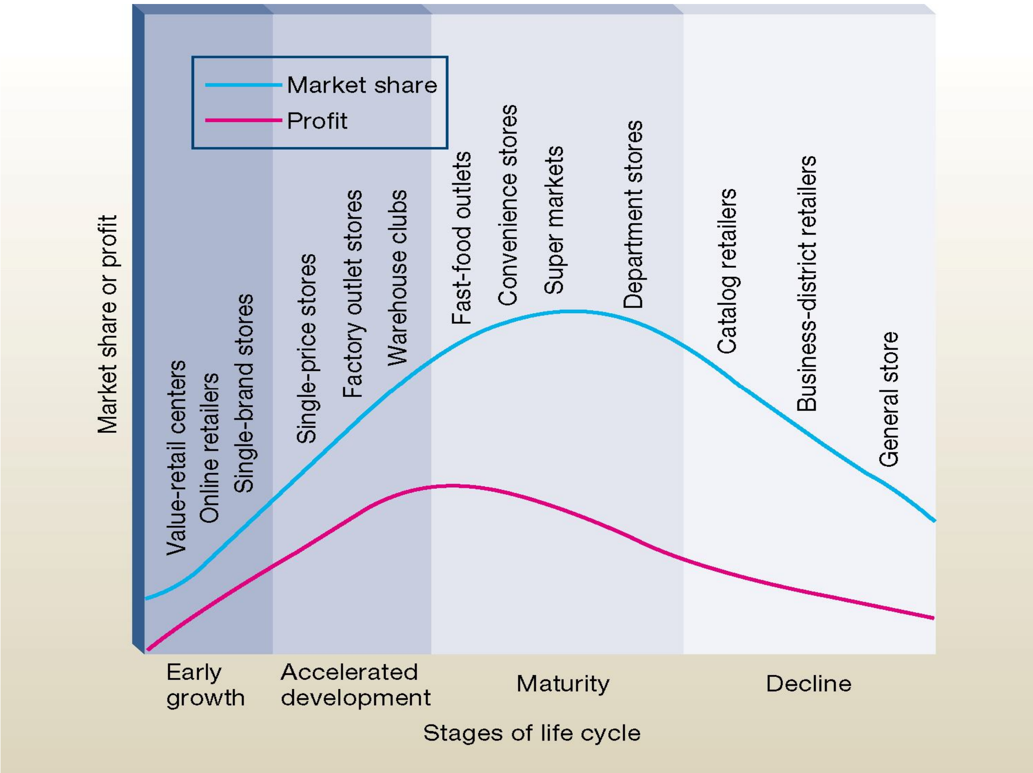


Exhibit 4.2.3 Retail Life Cycle

In the accelerated growth phase the organizations face rapid increase in sales, competitors begin to emerge and the organizations begin to use leadership and their presence as a tool in stabilizing their position. The investment level will be high as there are others who will be creating a lot of competition. This level may go up to eight years. Hypermarkets, Dollar stores are in this stage. In the maturity stage as competition intensifies newer forms of retailing begin to emerge, the growth rate starts to decline. At this stage firms should start work on strategies and reposition techniques to be in the market place. Supermarkets, cooperative stores are in this stage. In the final stage of the retail life cycle is the declining phase where firms begin to loose their competitive advantage. Profitability starts to decline further and the overheads starts to rise. Thus we see that organizations needs to adopt different strategies at each level in order to sustain in the marketplace

CLASSIFICATION OF RETAIL FORMATS

Retailers have changed dramatically according to the changing trends and the evolving needs of the consumers. Different retail format have emerged over the years and each have been an improvisation over the earlier formats. Retail stores can be classified broadly based on store based and non-store based, the store based is otherwise the brick and the motor stores while the non-store based are those, which do not use the traditional format. Ownership in store based is further divided based on ownership and merchandise. This section discusses some of the prominent formats under each classification

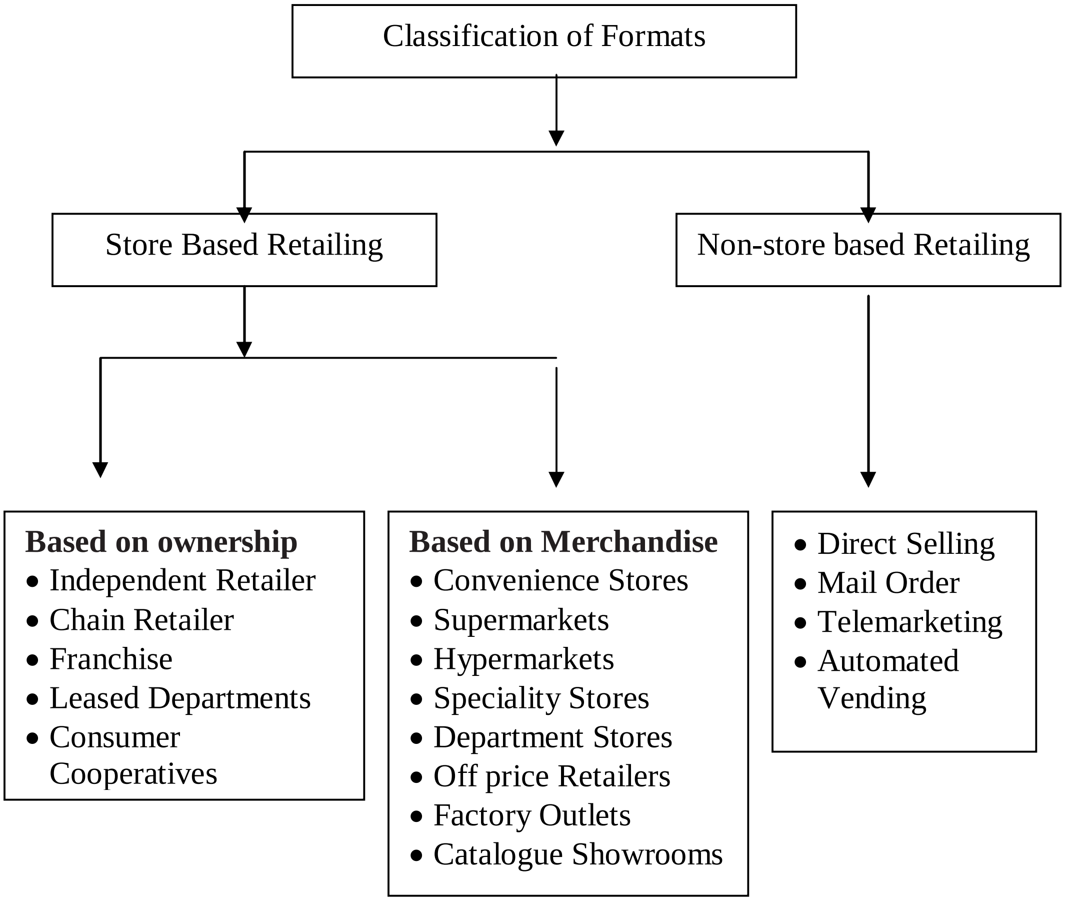

Classification of Formats
Store Based Retailing
Non-store based Retailing
Based on ownership
• Independent Retailer
• Chain Retailer
• Franchise
• Leased Departments
• Consumer Cooperatives
Based on Merchandise
• Convenience Stores
• Supermarkets
• Hypermarkets
• Speciality Stores
• Department Stores
• Off price Retailers
• Factory Outlets
• Catalogue Showrooms
• Direct Selling
• Mail Order
• Telemarketing
• Automated Vending

Exhibit 4.2.4 ***Classification of Retail Formats***

Retail formats are broadly classified into store based and non-store based retail formats. The store based formats are the traditional models where you have brick and motor stores while a direct relationship with the customer is the trust area of the non-store based. The store based is further divided based on the ownership and the merchandise held by the stores.

CLASSIFICATION BASED ON OWNERSHIP

An independent Retailer- these are retail stores which owns only one retail outlet. Usually the format is passed from generation to generation and this is has a proprietor who owns the store. 80 percent of the retail stores fall under this class in our country. From the paan shops to the kirana stores we find this type of stores in our country. Saravana stores is a good example.

A Chain Retailer- they are otherwise known as the corporate chain where we find two or more outlets under a common ownership. These stores have commonality in merchandise, store layout, ambience etc. The advantage of this particular type of format is the economies of scale they enjoy. Here since they are scattered all over consumer preference may not be given greater importance. Some of the chain retailers are Mega mart and Nilgris.

Franchising- this is a contractual agreement between two parties where the franchiser allows the franchisee to conduct the business under an established name in return for a fee. Some of the well-known franchisers are Mc Donald's, Archie's stores, Pizza Hut etc

Leased Departments- These is otherwise known as shops in shops. In this particular type a portion of a store is rented or leased to a third party. We see Coffee Day having outlets in Crossword bookstores or Pizza Corners in multiplexes.

Consumer Cooperatives- these are retail institutions owned by consumers and this is mainly because of dissatisfied customers whose needs were never fulfilled by the existing retailers. Some of these are either owned by the government or backed by government. This helps in price negotiations and is one of the prime players when price quality is considered as an important parameter.

CLASSIFICATION BASED ON MERCHANDISE

Convenience Stores- these are relatively small stores near residential area and are open for long hours. They carry limited line of high turnover products and have self-service formats. This format is emerging in India and they work seven days a week. BP's In&Out, HP Speed mart fall under this category.

Supermarkets- These stores are relatively large and operate on low costs, low margins, high volume and offering a self-service format. The store houses food, laundry, and household maintenance products. Some examples for this format are Nilgiris and Food World.

Hypermarkets- has it's origins in the US, these are stores that have a space of about 80,000 to 2,20,000 sq ft. the combine supermarket, discount stores and the warehouse principles in setting up them. They are usually situated on the outskirts of big cities and towns. In India the size is proportional and is not too big. Big bazaar is considered as a hypermarket.

Specialty Stores- they are characterized by narrow line, with deep assortments in that particular product line. For the speciality stores a well-defined target market is essential. Personal attention, store ambience, customer service are important to the retailers. Music World, Gautier Furniture's are examples of this type of retailers. A new form of speciality stores have emerged and are called the category killers, who offer products from a single product line at economical prices. This particular concept has found tremendous appeal with the Indian market. Toys kemp in Bangalore is a classic example of this type of stores

Departmental Stores-This format originated in the mid-nineteenth century and is popular in many parts. They are large scaled retail outlets whose merchandise offer runs across different product lines. Apparel and home furnishing are the most common categories found in the departmental stores. The size of an average Indian departmental store varies between 20,000-40,000 sq ft, while that of the western stores are around 75,000 + sq ft. Some of the big players in this format are Life style, Globus, Ebony and so on.

Off-price Retailers- In this format, the merchandise is sold less than the MRP. The retailers buy manufacturer's seconds or overruns as a result of which the merchandise may be in odd sizes or may be minor defects. Some off-price retail stores are manufacturer run and are called the factory outlets and sell the manufacturer's products at lesser prices compared to other retailers. Mega Mart, Levi's factory outlets are some of the examples of this format.

Catalogue showrooms- they are retailers who specialize in goods like jewellery, electronics. Customers have to check through a catalogue and then order the product they need. This concept s still in the nascent stage in the Indian market

NON-STORE RETAILING

A form that is gaining ground in the non-store retailing, in this type of retailing the customers have a direct relationship with the retailers. The non-store retailing is broadly classified into direct selling and direct response marketing, which incorporates mail orders, television shopping and electronic shopping

Direct selling- this form of retailing is common for products like cosmetics, food products, educational materials and basic home appliances where the consumer will be in his place while the marketer brings the products to his doorsteps. Over the last decade the concept has grown leaps and bounds and according to the direct selling industry in India, there has been a 60-65 percent growth in sales turnover from this industry alone every year.

Telemarketing- Using the telephone to sell directly to consumers has become the major direct marketing tool. Marketers use outbound telephone charges to help sell their products and services. Some telemarketing systems are fully automated. Marketers also use inbound toll-free numbers to receive orders arising from interactive marketing done through television and radio ads, direct mail or catalogs. Telemarketing is used in industrial as well as consumer marketing. The recent explosion in unsolicited telephone marketing has annoyed many consumers who object to the almost daily junk phone calls that pull them away from their normal routines.

Mail order Retailing- this form eliminates personal selling and the physical store operations. This format is appropriate to speciality products or narrow product lines and where the target market is well defined. The main advantage of this type of retailing is the convenience they offer to the customers.

Television Shopping- the television based retailing has received fair amount of success in India. With players like Asian Sky shop, TSN products are advertised on televisions with features, warranties and prices discounts. Phone numbers are given for different cities where the customers has to give a call to the nearest place and order the products. The products are then home delivered.

Electronic Shopping- the fastest growing medium to do retailing is electronic medium. Every brick and motor retailers are looking for click only models whereby customers can order products at the click of a button. This format virtually eliminates the physical infrastructure needed and can help in reducing the cost of operations. An effective supply chain is what these players need. It has been estimated that the Indian online shopping market is worth Rs.150 crores with 25% growth in 2005-06. The industry is expected to grow in the next 3-5 years. E-bay, rediff.com are some of the online shopping portals in the country.

Pantaloon: Fashion by Pantaloon

Pantaloon is the company's departmental store and part of life style retail format. In fact, PRIL took its very initial steps in the retail journey by setting up the first Pantaloon store in Kolkata in 1997. In a short time Pantaloon has been able to carve a special place for it self in the hearts and minds of the aspirational Indian customers. The company has depth of offering for both men and women at affordable prices. A striking characteristic of Pantaloon has been the strength of its private label programme. John Miller, Ajile. Scottsvile, Lombard, Annabelle are some of the successful brands created by the company.

Big Bazaar: Is se sasta aur acha kahin nahin

Big bazaar is the company’s foray into the world of hypermarket discount stores, the first of its kind in India. Price and the wide array of products are the USP’s of Big Bazaar. Close to two lakhs products are available under one roof at prices lower by 2 to 60 per cent over the corresponding market prices. The high quality of service, good ambience, implicit guarantees and continuous discount programmes have helped in changing the face of the Indian retailing industry. A leading foreign broking house compared the rush at Big Bazaar to that of a local suburban train

Food Bazaar – Wholesale prices

Food Bazaar’s core concept is to create a blend of a typical Indian Bazaar and International supermarket atmosphere with the objective of giving the customer all the advantages of Quality, Range and Price associated with large format stores and also the comfort to See, Touch and Feel the products. The company has recently launched an aggressive private label programme with its own brands of tea, salt, spices, pulses, jams, ketchups etc. With unbeatable prices and vast variety (there are 42 varieties of rice on sale), Food Bazaar has proved to be a hit with customers all over the country

Courtesy: www.pantaloon.com

ELEMENTS OF RETAIL STRATEGY

The retail strategy is an overall plan and guidelines that guides a retailer. A retail strategy is a clear and well-defined plan that the retail organizations outline to tap the market and create a long-term relationship with the customers. The steps that are involved in strategy formulation are the same in every industry. Exhibit 4.2.5 brings out the steps in retail strategy.

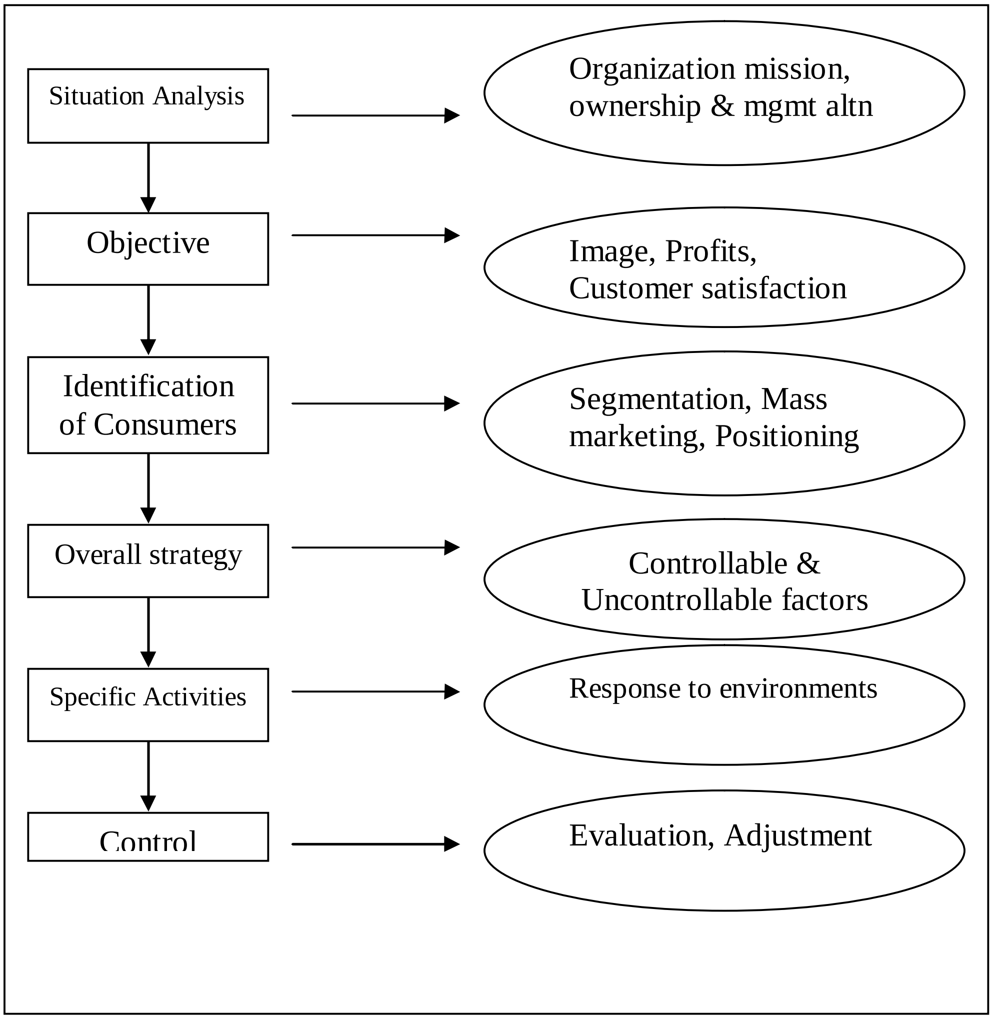

Situation Analysis
Organization mission, ownership & mgmt altn
Objective
Image, Profits, Customer satisfaction
Identification of Consumers
Segmentation, Mass marketing, Positioning
Overall strategy
Controllable & Uncontrollable factors
Specific Activities
Response to environments
Control
Evaluation, Adjustment

Exhibit 4.2.5 S*teps in Retail Strategy*

Situation Analysis- The first stage in retail strategy is establish the organizational mission. A mission statement acts as a motivator for the organization. The mission statement is one, which inspires the employees in the organization to stay focus on the goals of the organization. Evaluating ownership and management options like whether to go it alone or have a partnership or to buy an already existing organization has to be clearly outlined. Apart from this the merchandise that would be sold should also be evaluated.

Objectives- these are the long, short and the mid term goals the retailer hopes to attain. The goals may be based on profits that may include ROI, sales which include market share, and the customer and the stakeholders' satisfaction. Te objectives need to be well defined keeping in mind the mission of the organization and should see that the strategies get translated into results.

Identification of customers- Even though the strategy of a particular retailer may be executable and the mission of the organization looks inspiring, but if a wrong target market is chosen, it may prove a failure. It is essential for the retailer to understand the needs of the customer. A retailer has three options which he may choose according to his objective, he can try selling different product categories to a broad spectrum of customers which is known as mass marketing or work on one particular segment which is market segment or have two or more segments which is commonly called as selective segments.

Overall Strategy- The overall strategy is broadly classified into controllable and uncontrollable factors. The location of the store, merchandise decision, communication, objectives come under controllable factor since the firms has a element of autonomy n deciding about them. In case of uncontrollable factors, the factors that a retailer must try and adapt like the technological changes, legal imperatives, cultural factors, economic situation get categorized. This step is one of the most essential steps in retail strategy because this stage demonstrates the firm's ability to adapt to different changing conditions.

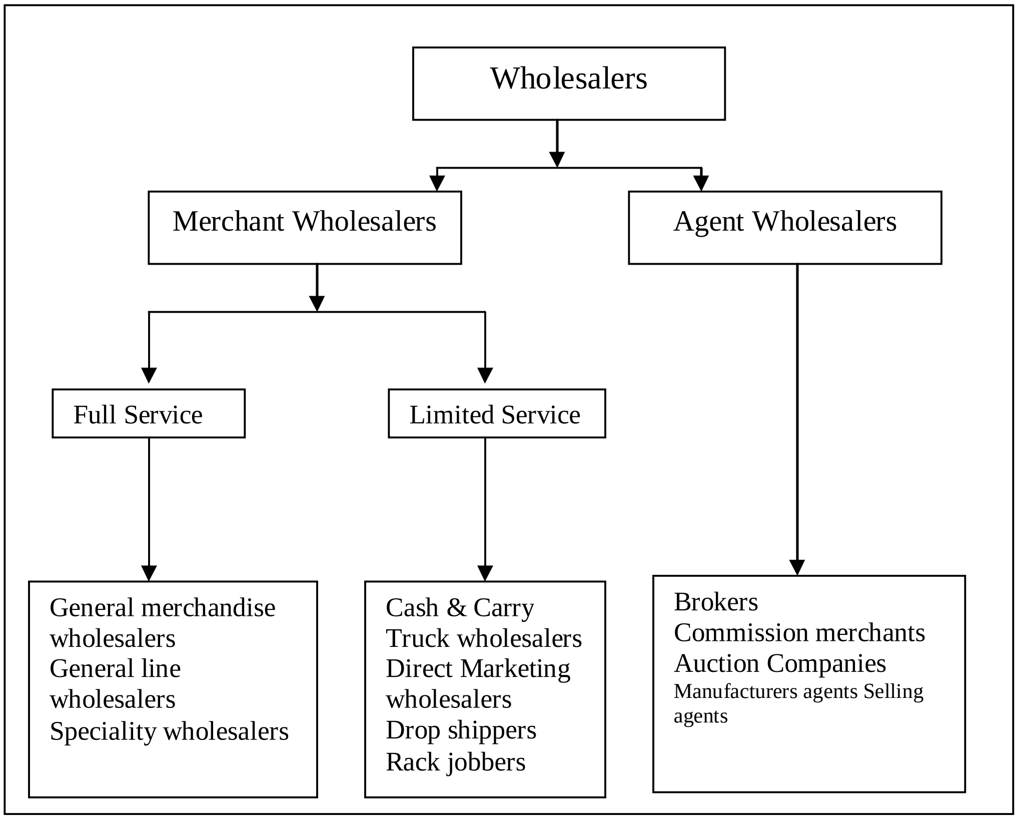
Specific Activities- this deals with the tactical decisions and the day-to-day operations of the firm. The firm's responsiveness to the environmental factors with the help of the marketing mix elements is the actual functioning of the firm's activities.

Control- in the final phase of strategy formulation is the review of the firm's performance of a period of time. The firm's strategies and the tactics have to be evaluated to find the effectiveness and if it fall in place wit the organizational objectives and the with the firm's mission. In case if the firm finds that some of the tactics are time consuming and not much of benefit could be figured out the organization should ensure that such tactics have to be modified or be dropped from the firm’s future course of action.

WHOLESALING

This includes all the activities involved in selling goods and services to those who buy for resale purpose. In the case of wholesaling this excludes manufacturers or producers who are involved directly in the production of the goods. They are the marketing intermediaries that buy from one source and sell it to another. The main function of a wholesaler is facilitating the transportation of the product and at times in the transfer of the titles. The intermediaries’ performing the wholesaling function is predominantly divided into two types namely merchants and agents. The difference between the two forms lies in if they take title to the goods they sell.

CLASSIFICATION OF WHOLESALERS



Wholesalers
Merchant Wholesalers
Agent Wholesalers
Full Service
Limited Service
General merchandise wholesalers
General line wholesalers
Speciality wholesalers
Cash & Carry
Truck wholesalers
Direct Marketing wholesalers
Drop shippers
Rack jobbers
Brokers
Commission merchants
Auction Companies
Manufacturers agents Selling agents

Exhibit 4.2.6 Classification of Wholesalers

The classification is based on whether the intermediaries take title to the goods they sell. Taking title to the goods means the intermediaries own that merchandise and must be prepared to handle the risk associated with the ownership, including getting stuck with merchandise even if it turns out to be un-sellable

CLASSIFICATION OF MERCHANT WHOLESALERS

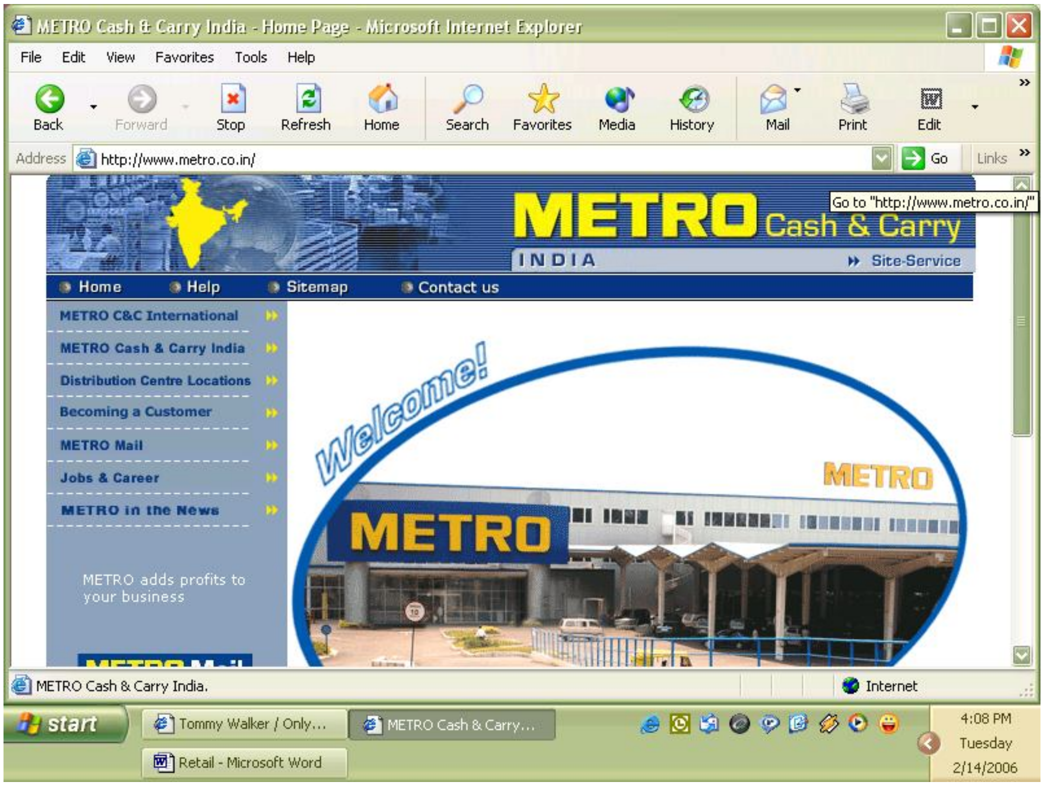
The merchant wholesalers are independently owned concerns that take title to the goods they distribute. Some of the merchant wholesalers operate at the national level while some of them are more into regional levels. The merchant wholesalers are classified in terms of the number and the types of service they provide to the customer. The major division of the merchant wholesalers is termed as the *Full-service merchant wholesaler* and *Limited –service merchant wholesaler*.

The ***Full-service merchant wholesaler*** provides customers with a complete array of services in addition to the merchandise they offer. The service may include delivery, credit facility, advice and even assistance as accountant aid. These people are also called as full-function wholesalers. The full-service wholesalers are further classified into three types by the line of the goods they offer.

- *General Merchandise Wholesalers* are those who sell large number of different product types or lines. It would be a one stop shop for the retailers to procure things from them at a much bargainable prices
- *General Line Wholesalers* are those who limit their offerings to one particular product line. They may hold all the products and variants in one particular product line
- *Speciality Wholesaler* reduce the line further, they may hold only select products in a particular product line. The traders of spices can be classified under this category

The choice of being a more general merchant wholesaler or a much-specialized wholesaler depends on the choice of the target customers, whether their customers are speciality stores or a general stores

The ***Limited-Service Merchant Wholesaler*** is one who offers less than full service and charges lower prices. These types of wholesalers are also known as limited-function wholesalers. This model comes to prominence when some customers may not want or may not be interested to pay for some of the services the Full-service merchant wholesaler offers. They may prefer to sacrifice the services offered to get lower prices. As a result of this particular category has emerged. This Limited-service merchant wholesaler is further divided into five types based on the various services they try to render and the on the basis of the payment for the goods they sell.


METRO Cash & Carry India - Home Page - Microsoft Internet Explorer
File Edit View Favorites Tools Help
Back Forward Stop Refresh Home Search Favorites Media History Mail Print Edit
Address http://www.metro.co.in/
Go Links
Go to "http://www.metro.co.in/"
METRO Cash & Carry
INDIA
Site-Service
Home Help Sitemap Contact us
METRO C&C International
METRO Cash & Carry India
Distribution Centre Locations
Becoming a Customer
METRO Mail
Jobs & Career
METRO in the News
Welcome!
METRO
METRO
METRO Cash & Carry India.
Internet
start
Tommy Walker / Only...
METRO Cash & Carry...
Retail - Microsoft Word
4:08 PM
Tuesday
2/14/2006

METRO adds profits to your business

Exhibit 4.2.7 ***Metro Cash & Carry***

- *Cash and Carry Wholesalers* are buyers who do not want certain specialized service such as delivery or credit. The wholesalers prefer the buyers to come to their warehouses and buy the products and pay for them at the same time. Metro, the German wholesaler refer exhibit 2.6.7 is a classic example for this type for this category
- *Truck Wholesalers* are otherwise called the truck jobbers sell limited line of items. They operations are predominantly with the help of trucks and this helps in the immediate delivery offers. Some of the items used to be considered in this method are perishables and those which have great

demand. Although this method is a expensive form of distribution this definitely a aggressive form of selling the offering

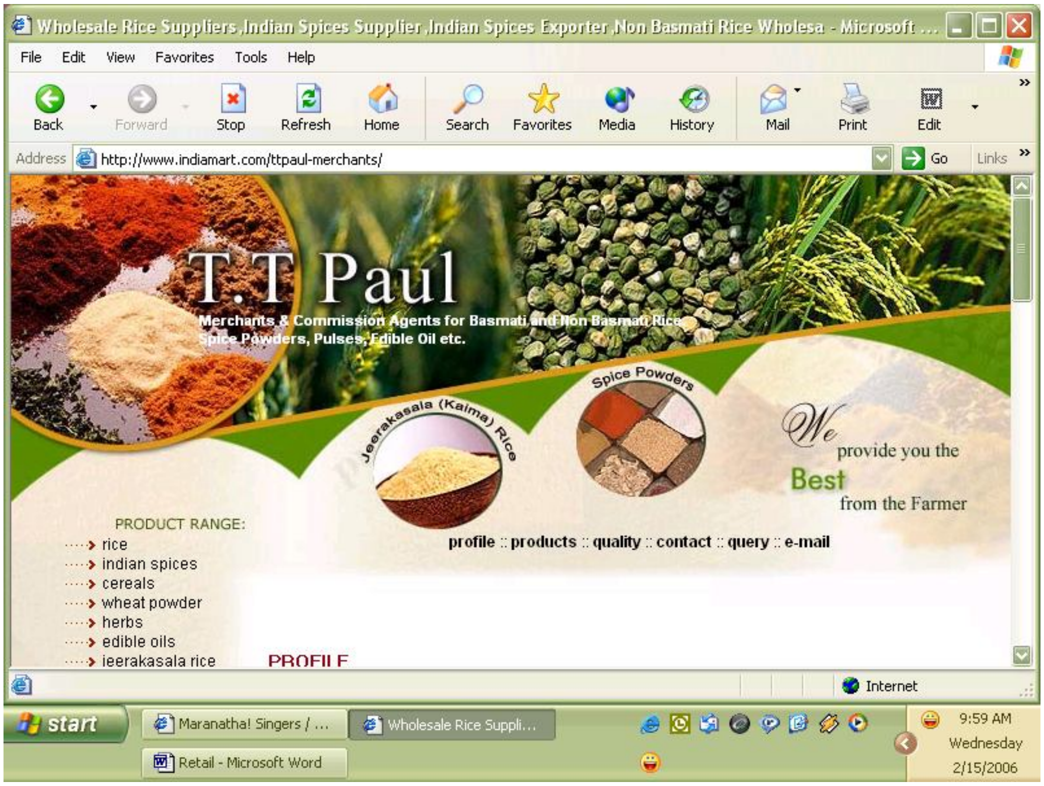
- *Drop Shippers* are merchants who take title to the goods but not the possession of the goods. These merchants take orders form the buyers pass it to the manufacturers, which will, then ship the product directly to the buyer. As the product goes directly to the buyer, it minimizes in the loading and unloading of the product. This type is commonly used for commodities like cement, coal etc. The drop shippers are also called as the desk jobbers as they need minimum infrastructure. Since they do not handle the shipping, there is even no need for a warehouse to keep the products.
- *Rack Jobbers* are another type of merchant wholesalers who contract with the retailers to set up display racks in the store and stock them with merchandise. This particular category of wholesalers gained prominence after the emergence of departmental stores

CLASSIFICATION OF AGENT WHOLESALERS

The agents are the next category of wholesalers, they take possession of the goods but at the same time they do not take title to them. The agents in no way provide warehouse facility or credits but provide facilities like arranging credit or delivery as a part of their service. The agents make business through commissions based on selling prices of the product. The percentage of the commission varies based on the industry as well on the perishable nature of the product. The agents can be classified as follows namely

- *Brokers* who are intermediaries who bring the sellers in touch with the buyers and also facilitate in the contractual negotiations and receive commissions based on the work. Brokers are considered to be neutral and are found in every field. The commissions they receive from both the parties will be relatively less and this requires minimum investment. Most organizations prefer brokers because they work on commissions and do not have long-term relationships with one particular organization.

- *Commission Merchants* are similar to brokers but are given certain powers by the sellers of the product. They perform majorly the pricing function and work closely with the producers of the products. The commission merchants are most common in the agricultural products. The commission merchants take possession of the goods so that the prospective buyers have a chance to inspect the products; once the deal is finalized the commission merchants deduct their commission past and return the balance to the producer. Exhibit 4.2.8 shows the homepage of a commission merchant
- *Manufacturer's Agents* are those who are available for the producer who are not interested in performing the sales activity or who lack the expertise to have one. The manufacturer's agents work in limited geographical areas and in low priority zones. If a producer of electronic goods feels having a separate sales force for the rural areas is an expensive decision they may go in for a merchant's agent to do the job of selling their offering. The merchant's agents will be familiar with the area they operate and this is one reason why producers opt for the merchant's agents. One another benefit of these people is that they need not be paid till the deal is finalized.
- *The Selling Agents* are paid a commission and are expected to be familiar with the products and the markets. Unlike the manufacturer's agents they do not restrict themselves to one particular geographical area but rather to all places where the product has got a market. Since they concentrate on a much larger scale they are given more responsibility including the elements of promotions and pricing of the products. The organizations who utilize these people are otherwise called as external marketing department



Wholesale Rice Suppliers ,Indian Spices Supplier ,Indian Spices Exporter ,Non Basmati Rice Wholesa - Microsoft ...
File
Edit
View
Favorites
Tools
Help
Back
Forward
Stop
Refresh
Home
Search
Favorites
Media
History
Mail
Print
Edit
Address
Go
Links
Internet
start
Maranatha! Singers / ...
Wholesale Rice Suppli...
Retail - Microsoft Word
9:59 AM
Wednesday
2/15/2006

http://www.indiamart.com/ttpaul-merchants/

T.T Paul

Merchants & Commission Agents for Basmati and Non Basmati Rice
Spice Powders, Pulses, Edible Oil etc.

Jeerakasala (Kaima) Rice

Spice Powders

We provide you the Best from the Farmer

profile :: products :: quality :: contact :: query :: e-mail

PRODUCT RANGE:
- rice
- indian spices
- cereals
- wheat powder
- herbs
- edible oils
- jeerakasala rice

PROFILE

Exhibit 4.2.8 Commission Merchants

Key Terms

- Accordian Theory
- Convenience Stores
- Franchising
- Full service merchant wholesaler
- Hyper Markets
- Leased Departments
- Limited service merchant wholesaler
- Retail Life Cycle
- Retailing
- Speciality Stores
- Theory of Natural Selection
- Wheel of Retailing
- Wholesaler

UNIT-V

LESSON – 5.1 PROMOTION DECISION

LESSON – 5.2 PROMOTION MIX

LESSON - 5.3 ADVERTISING DECISION

LESSON – 5.4 OBJECTIVE AND CAMPAIGN

LESSON – 5.5 AD EFFECTIVENESS

LESSON - 5.6 SALES PROMOTION AND PUBLICITY

LESSON - 5.7 SALES FORCE DECISION

5.1 PROMOTION DECISION

Overview

Marketing communications is one of the four major elements of the company’s marketing mix. Marketers must know how to use advertising, sales promotion, direct marketing, public relations, and personal selling to communicate the product’s existence and value to the target customers.

The communication process itself consists of nine elements: sender, receiver, encoding, decoding, message, media, response, feedback, and noise. Marketers must know how to get through to the target audience in the face of the audience’s tendencies toward selective attention, distortion, and recall.

Developing the promotion program involves eight steps. The communicator must first identify the target audience and its characteristics, including the image it carries of the product. Next the communicator has to define the communication objective, whether it is to create awareness, knowledge, liking, preference, conviction, or purchase. A message must be designed containing an effective content, structure, format, and source. Then communication channels both personal and non-personal must be selected. Next, the total promotion budget must be established. Four common methods are the affordable method, the percentage-of-sales method, the competitive-parity method, and the objective-and-task method.

The promotion budget should be divided among the main promotional tools, as affected by such factors as push-versus-pull strategy, buyer readiness stage, product life-cycle stage and company market rank. The marketer should then monitor to see how much of the market becomes aware of the product, tries it, and is satisfied in the process. Finally, all of the communications effort must be managed and coordinated for consistency, good timing, and cost effectiveness.

Learning Objectives

- The nine elements of the communication process
- How to identify the target audience
- How to determine the communication objectives
- How the message should be designed
- The selection of communication channels
- How the promotion budget is determined
- How the promotion mix is established
- How to evaluate and manage the communication process

I. Introduction—the five major modes of communication (advertising, sales promotion, public relations, personal selling, and direct marketing)

II. The communication process—communications as the management of customer buying processes over time, the nine elements of the communications model, reasons why message may not get through the receiver (selective attention, selective distortion, and selective recall)

III. Developing effective communications

   A. Identify the target audience

      1. Image analysis is a major part of audience analysis that entails assessing the audience's current image of the company, its products, and its competitors

         a) First step is to measure target audience's knowledge of the subject using a familiarity scale

b) Second step is to determine feelings toward the product using a favorability scale

2. Specific content of a product's image is best determined with use of semantic differential (relevant dimensions, reducing set of relevant dimensions, administering to a sample, averaging the results, checking on the image variance)

B. Determine the communication objectives

1. Based on seeking of a cognitive, affective, or behavioral response

2. Assuming the buyer has high involvement with the product category and perceives high differentiation within the category, base objectives on the hierarchy-of-effects model (hierarchy: awareness, knowledge, liking, preference, conviction, purchase)

C. Design the message (AIDA model)

1. Message content—choosing an appeal (rational appeal to audience's self interest, emotional appeal attempt to stir up either positive or negative emotions, moral appeals are directed to the audience's sense of what is right and proper)

2. Message structure—one-sided presentation versus two-sided argument

3. Message format—must be strong, based on headline, copy, "sound," nonverbal clues, color, expression, dress, etc.

4. Message source —expertise, trustworthiness and liability

D. Select the communication channels

1. Personal communication channels—direct (advocate, expert and social)

2. Non-personal communication channels—indirect (media, atmospheres, events)

E. Establish the total marketing communications budget

1. Affordable method

2. Percentage-of-sales method

3. Competitive-parity method

4. Objective-and-task method

IV. Deciding on the marketing communications mix

A. Promotional tools—benefits of each tool (advertising, sales promotion, public relations and publicity, personal selling, direct marketing)

B. Factors in setting the marketing communications mix (type of product market, buyer-readiness stage, product-life-cycle stage)

C. Measure the communications’ results

V. Managing the integrated marketing communications process

A. A concept of marketing communications planning that recognizes the added value of a comprehensive plan

1. Evaluates the strategic roles of a variety of communications disciplines

2. Combines these disciplines to provide clarity, consistency and maximum communications impact through the seamless integration of discrete messages

PROMOTION MIX

Advertising—the use of paid media by a seller to communicate persuasive information about its products, services, or organization—is a potent promotional tool. Advertising takes on many forms (national, regional, local, consumer, industrial, retail, product, brand, institutional, etc.) designed to achieve a variety of objectives (awareness, interest, preference, brand recognition, brand insistence).

Advertising decision-making consists of objectives setting, budget decision, message decision, media decision, and ad effectiveness evaluation. Advertisers should establish clear goals as to whether the advertising is supposed to inform, persuade, or remind buyers.

The factors to consider when setting the advertising budget are: stage in the product life cycle, market share, competition and clutter, needed frequency, and product substitutability.

The advertising budget can be established based on what is affordable, as a percentage budget of sales, based on competitors' expenditures, or based on objectives and tasks, and based on more advanced decision models that are available.

The message decision calls for generating messages, evaluating and selecting between them, and executing them effectively and responsibly.

The media decision calls for defining the reach, frequency, and impact goals; choosing among major media types; selecting specific media vehicles; deciding on media timing; geographical allocation of media. Finally, campaign evaluation calls for evaluating the communication and sales effects of advertising, before, during, and after the advertising.

Sales promotion and public relations are two tools of growing importance in marketing planning. Sales promotion covers a wide variety of short-term incentive tools designed to stimulate consumer markets, the trade, and the organization's own sales force. Sales promotion expenditures now exceed advertising expenditures and are growing at a faster rate.

Consumer promotion tools include samples, coupons, cash refund offers, price packs, premiums, prizes, patronage rewards, free trials, product warranties, tie-in promotions, and point-of-purchase displays and demonstrations.

Trade promotion tools include price-off, advertising and display allowances, free goods, push money, and specialty-advertising items. Business promotion tools include conventions, trade shows, contests, sweepstakes, and games. Sales promotion planning calls for establishing the sales promotion objectives, selecting the tools, developing, pretesting, and implementing the sales promotion program, and evaluating the results.

Marketing public relations (MPR) is another important communication/promotion tool. Traditionally, it has been the least utilized tool but is now recognized for its ability in building awareness and preference in the marketplace, repositioning products, and defending them. Broadly, MPR is those activities that support the ultimate sale of a product or service. Some of the major marketing public relations tools are news, speeches, events, public service activities, written material, audio-visual material, corporate identity, and telephone information services. MPR planning involves establishing the MPR objectives, choosing the appropriate messages and vehicles, and evaluating the MPR results.

ADVERTISING DECISION

Modern marketing calls for more than developing a good product, pricing it attractively and making it accessible to the target consumer. Companies must also communicate with the present and potential customers. In this respect, advertising is a potent promotion tool of marketing communication mix, while the rest four are :

Sales Promotion
Direct Marketing
Public Relations and Publicity
Personal Selling

WHAT IS ADVERTISING ?

Various marketing Gurus have defined advertising according to their own views:

" Advertising *Consists* of all the activities involved in presenting to a group a non –personal, oral or visual openly – sponsored, identified message regarding a product, service or idea. This message, called an advertisement, is disseminated through one or more media and paid for by the identified sponsor".

W.Z. Stanton

"To give public notice or to announce publicly".

"Advertising is mass communication of information intended to persuade buyers so as to maximize profits".

J.E. Littlefield

To summarise, advertising means any paid form of non – personal presentation and promotion or ideas, goods or services by an identified sponsor.

IMPORTANCE OF ADVERTISING

It is just not enough to manufacture a product. People must be informed of its existence and should be given good reasons to buy it. This is a job which is sought to be done by advertising. Without advertising, people would not be aware of the attributes of the product nor of its price. Let us now discuss the role and importance of advertising.

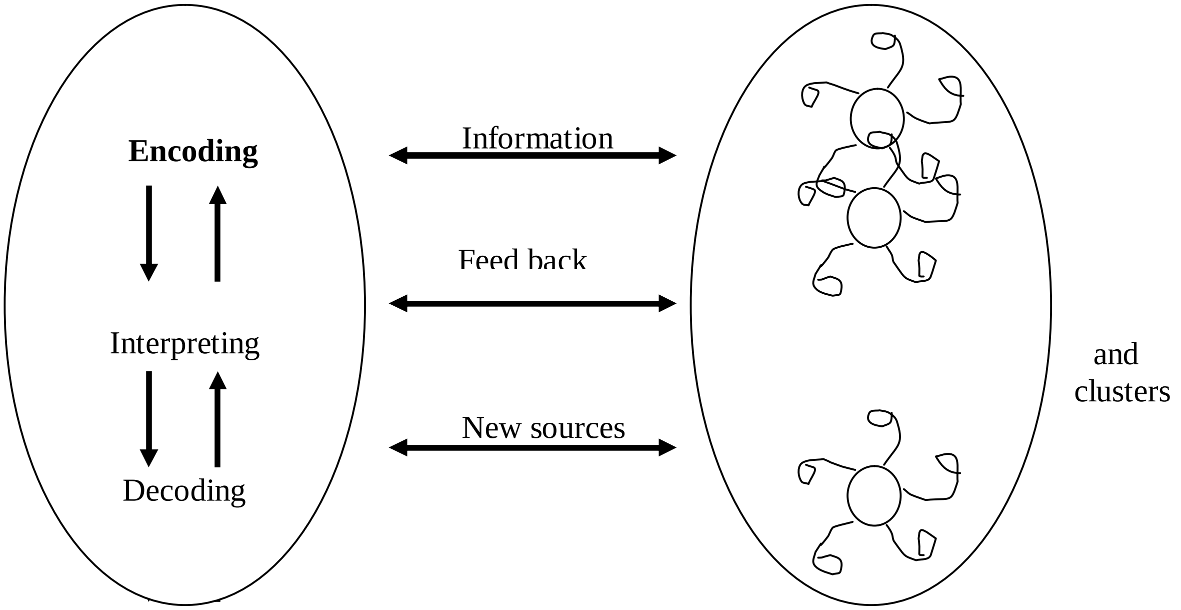
(i) Way of Informing

Advertising is a way of communicating information to the consumer –information which enables him to compare and choose from the products and services available. Advertising enables consumbers to exercise their right of *free choice*[1] " *Encyclopedia Bitannica"* such diverse media as handbills, newspapers, magazines, billboards, letters, radio and television broadcasts and motion pictures.

(ii) Manufacturer's concerns

Advertising is the most economical means by which a manufacturer or an institution can communicate to an audience either to sell a product or to promote a cause of social welfare, such as, civic drive, or an immunization programme. This includes the process of mass communication which is different from ordinary communication. Here a macro level mass communication is between manufacturer and his mass audience. This is also connected through new sources. Mass audience gives various reactions as responses. Here audience is interconnected as a group within groups. The 5 elements of mass communication are shown in the above chart.

MODEL OF NEWS COMMUNCATION



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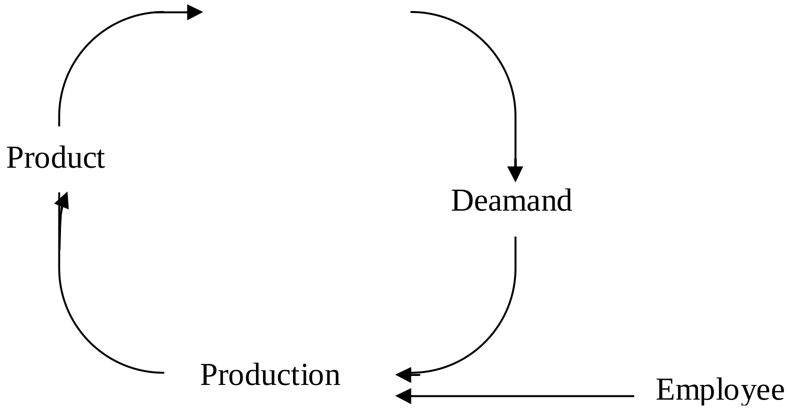
1. *In India, an ordinary grocery store keeps as many as 20 brands of toilet soaps, 10 brands of toothpastes, 9 brands of cooking oils and over100 varieties of other packaged goods. In such a situation, advertising helps consumers to make an intelligent and well – considered purchase. The Economic Times, December 21, 1989.*

(iii)Fundamental Right of Freedom of Speech

Advertising being a necessary means of communication is an inseparable part of free speech. Any restriction on the right to recommend legitimate services or ideas in public will diminish the fundamental right of freedom of speech.

(iv) Improving productivity

Advertising can help in improving the economies of developed and developing countries. There is ample evidence to support this view. Advertising stimulates production and consequently generates more employment. It can help stabilize prices and leads to wider distribution and greater availability of goods an services.



(v) Economic Growth of Country

Advertising is an essential and integral part of the marketing system. It is sometimes maintained that the marketing system is nothing but requirement of a country's social and economic growth. Advertising stimulates sales and compels the firm to improve its productivity and contributes substantially to the growth of the economy. Thus marketing and advertising are key tools used to aid a country's growth.

Even though advertising costs a lot of money, and the costs are increasing day by day, a skillfully used advertising campaign can be the cheapest means of reaching the market and commutating with the consumers effectively. Advertising is wasteful if it fails to produce sales.

Advertisement leads to an increase in sales and market share. Pepsi came to India with a zero market share. By December, 1995, it had captured 40 per cent of Indian market [1] *Promise,* a toothpaste manufactured by a small –scale unit, was able to snatch a 15 per cent share of the market by strong customer –oriented advertisement.[2]

People feel safe in purchasing products they know of. Advertising makes them aware of the products and their attributes. In promoting a product or a brand, the manufacturer/ advertiser stakes his reputation. No manufacturer/ Advertiser would be foolish enough to risk his reputation by making misleading claims in his advertisements. Hence advertised goods are trusted the world over and India is no exception.

ADVERTISEMENT AND SALES PROMOTION

Difference between Advertising and Sales Promotion

Advertising is a message which promotes ideas, good or services communicated through one or more media by an identified sponsor while sales promotion consists of short – terms incentives provided by the identified sponsors to consumers and traders to persuade them to purchase and stock his products. The major differences between Advertising and Sales Promotion are :

Advertising	*Sales Promotion*
(i) A reason is offered to buy.	An incentive is offered to buy.
(ii) Theme is to build up brand loyalty	Theme is to break down the loyalty to a competing brand.
(iii) Aim is to attract the ultimate Consumers.	Aim is to attract not only consumers but retailers, wholesales and Sales force also.
(iv) Effective in the long run.	Effective in the short run.
(v) Heavy advertising makes the brand image of the product and accords it the perception of higher quality	Heavy Sales promotion leads to the product being perceived as having a brand image of cheaper and lower quality product.

(vii) Advertising includes messages delivered through various types of Media.	Various types of incentives are offered for - Consumer promotion - Trade Promotion - Sales force Promotion

DEVELOPING THE ADVERTISING PROGRAMME

It is difficult to make an all – embracing generalization about distinctive qualities of advertising mainly because of its many forms and uses. Various companies do their advertising in different ways. In a small company advertising is handled by someone in the sales or marketing department who coordinates with an advertising agency. On the other side, large companies setup their own advertising departments, where Marketing Manager reports to the Vice –President, Marketing. The advertising department's job is to develop the total budget, help and develop advertising strategy and approach an advertising agency for advertising and designing a campaign. Most of the companies use an outside agency to help them design an advertising campaign and to select the media and decide about the timings and booking space.

In developing an advertising programme, marketing managers must always start by identifying their target market and the buyers involved. Thereafter, they have to make five major decisions in the programme development process known as the five Ms which are explained in the following chart:

STEPS IN ADVERTISING PROGRAMME

Before Advertising		After Advertising
(i)	Market	

	- Define Market - Select the target market	- Measure the effect of advertising to determine whether it would help achieve the target.
(ii)	Motive	
	- Identify what makes people buy	- Compare the consumer buying motive and the advertising appeal.
(iii)	Media	- Evaluate the effectiveness of media
	- Decide about the media mix - Allocate budget among TV, Radio, Press etc.,	- Assess the effc, of the messge.
(v)	Measurement	
	- Assesses effectiveness of advertising	- Study sales graph
	- Evaluate possible achievement.	- Take a decision about future profile of advertising programme.

Advertising Goals

If an organization is spending crores of rupees on advertisement, then as managers we must attempt and be able to measure its effectiveness and delivery to find out whether we are receiving the value for money. However, advertising is only one part of marketing mix and the final delivery in rupees terms would involve the various marketing variables. The tragedy of advertising is that if it does not lead to an increase in sales of the product, the entire blame is put on advertising. Hence a clear definition of advertising goals in required. A successful advertising campaign can be compared with a military compaign where goal is set as " capture the army post No. 11" and the goal is achieved.

Advertising goal can be defined as a clear and concise description of exactly what advertising is intended to accomplish, i.e.,

-- To increase sales,

-- To establish brand equity, and

-- To enter the target market.

Sometimes these objectives are considered as marketing objectives instead of advertising objectives.

Need to set Advertising Objectives

Some of the possible objectives that are stressed are :

(i) Return on Investment (R.O.I) Advertising involves an investment of funds. Hence, it should produce a measurable return on the said investment in order to assess the desirability and profitability of advertising.

(ii) Selection of media. The most effective advertising tool should be chosen in order to get the most profitable result.

(iii) Coordination An appropriate co-ordination and integration of marketing and advertising efforts is imperative. Otherwise objectives of advertising are superimposed on objectives of marketing.

VARIOUS APPROACHES FOR SETTING ADVERTISING OBJECTIVES

(I) DAGMAR Approach

This is the most popular method of setting advertising goals and was proposed by Russel M. Colley. DAGMAR stands for - Defining advertising Goals for Measured Advertising Results.

Colley outlined this method for turning advertising objectives into specific measurable goals. He lists 52 possible advertising objectives under the same approach. The theory is based on the following: " The consumer passes through a hierarchy of stages between the time when the first ideas about the product comes to his mind and when he actually buys it" For example, an advertisement of a Generator should highlight fuel efficiency, easy start, after –sales service and ready availability of spares.

-- Initially it would inform us and we shall become aware of such a product. Then through product endorsement and trial we shall develop a favourable attitude and ultimately, we shall buy the product.

-- To set advertising objectives, we shall need to identify the stage in which the product is available and then we can set the objective.

Example :

A detergent manufacturing company wanted to position its product as the most powerful cloth cleaner and as a low cost detergent.

-- They worked out a campaign targeted to 3 crore households who own automatic washers.

-- Prior to the campaign release, they did an attitude survey on brand perception. After the campaign was over, they repeated the attitude survey.

The questions were focused on three areas :

(i) Which brand is the most effective in removing the spots ?

(ii) Which brand will you buy when you go to the market next ?

SURVEY RESULT

	Before Campaign	**After 6 months**	**After 1 year**
Awareness	38	46	52
Image	9	17	24
Preference	13	15	21

Specific advertising objectives could have been :

Increase awareness from 38 per cent to 52 per cent

Top image ranking to 24 per cent than 9 per cent

Increase preference to 21 per cent.

(ii) Product Life Cycle Approach

Advertising effectiveness varies according to the different stages of product life cycle.

(iii)Primary and Selective Demand Theory

According to this approach the advertising objective is categorized into two ways

Informative Advertising and Persuasive Advertising.

(a) Informative Advertising. This advertising is important when the product is in the pioneering stage and the objective is to build *Primary demand.* Primary demand is sought to be created especially by concept selling for a category of products. Some particular conditions are required necessarily to advertise for creating a primary demand. The existence of a strong and basic consumer need is the most important prerequisite as advertising cannot create demand for a new product. It can only stimulate an existing demand. There must be strong buying motives in existence.

Besides this, social trends, design, price, etc. also play a crucial rate at this stage. For example, the manufacturer of “VIM” initially had to inform potential consumers of VIM Bar’s economic benefits and many other advantages.

(b) Persuasive Advertising. This becomes important in the competitive stage, where a company’s objective is to build *selective demand* for a particular brand. Most advertising falls in this category. Persuasive advertising is undertaken when a strong primary demand is in existence. The product should be distinctive, its benefits should be visible and also a strong brand consciousness must be generated.

MEDIA PROFILE FOR ADVERTISING

Role of Media. Media has a vital role in the process of advertising communication. Effective advertising is possible only if suitable media are available. The appropriateness of media used *vis – a –vis* the target audience and their reach are also of crucial importance.

Advertising Message ⇒ Media Mix ⇒ Target Audience

⇓

Result will reflect on the sales graph of the company ⇐ Maximum Reach

A substantial portion of the advertising budget allocation to the mass media is spent on buying space and time. Therefore media decisions assume a considerable importance when financial implications come to the force.

Media Planning. Advertisement becomes effective only when it reaches the desired audience. The value of the advertisement is determined by the number of persons seeing it, reading it and thus becoming aware of the product or the service.

Media Selection. Each media has a specific function to perform and its selection depends upon the requirements of the job. Media can be divided into two categories :

Main Media -- *a*lso called *“above the line”* media, e.g., newspapers, T.V. Radio, Magazines, etc.

Secondary Media- also called “ below the line” media, e.g., hoarding, direct mail, point of purchase, etc. These are also known as reminder media.

Media Planning Process. The steps involved in media planning are :

(i) Media planning and buying space is the financial side of advertising.

(ii) It interacts with the creative process to form an important part of the overall marketing process.

(iii) Whereas the creative process is a descriptive process, the media process is one of transforming their description to the public, i.e., a vehicle of communication.

(iv) The primary responsibility of media practitioners is to ensure that the advertising message is seen, heard, read or recognized by the target audience. We believe this is a crucial role as there is no point in having the best advertising if nobody sees the advertisement.

ROLE OF MEDIA IN THE ADVERTISING PROCESS

Media Selection for Rural Marketing. The following points have in be considered while selecting the media for the rural markets :

(i) The total number of literates in the rural market and their reading habits.

(ii) The extent and type of contribution of the product.

(iii) The number of cinemas and video parlours, panchayat viewing and listening facilities and the type of audience.

(iv) The number of publications which are circulated in the area concerned, the number of readers and their categories, whether casual, regular or headline readers.

(v) Whether the publications circulated in the area concerned are issued locally or are obtained fro the neighboring areas ?

MEDIA SELECTION DECISIONS

While selecting the advertising media the following factors should be borne in mind:

Cost of advertisement,

Nature of the product,

Comparison of the medium selected with other media,

Popularity of the media,

Characteristics of customers, and

Competition in the market.

TYPES OF MEDIA FOR ADVERTISING

Print Media	**Electronic Media**	**Outdoor Media**	**Direct Mail**
- Newspapers	- TV	- Billboards	- Price Lists
- Direct Mail	- Video	- Hoardings	- Catalogues
-Folders	- Radio	- Balloons	- Personal letters
- Product Literature	- Voice mail	- Advertising on transport means	- Circulars
- Journals	- Cinema	- Electric Display	

STRENGTHS AND WEAKNESSES OF EACH TYPE OF MEDIA

A. Press

Advantages	**Disadvantages**
News value and immediacy Area and ethnic selectivity Wide market coverage Advertisement flexibility	Casual readers not reading the whole magazine or newspaper High cost of brand usage Little demographic selectivity

Allow long message Moderate cost Publication with pictures possible Continuous publication.	Short message life Suitable only for educated class Poor quality of printing creating readers’ aversion Lack of faith in what appears in the Press.

B. Magazines

Strengths	**Weaknesses**
Long shelf life Durability of ad message Ad size flexibility Quality reproduction Demographic selectivity May cater to special interest groups More affluent audience Increased response of the consumers in response to the magazine ad. Possibilities of reproducing full colour effect.	Small reach Slow exposure build up Less impact than T.V. Lack of urgency

C. Outdoor-Hoardings, etc.

Advantages	**Disadvantages**
Attractive Long life Advertising at specific places	Limited scope Lack of personal touch

D. Direct Mail

Advantages	**Disadvantages**
Possibilities of covering a wide audience Economy Flexibility Easy to answer Personal Touch	Difficult to obtain the right mailing lists. Possibility of misleading information Frequent changes in mailing list

E. Radio

Advantages	**Disadvantages**
Low production cost Wide coverage High frequency possible Audience segmentation like 'Mahila Jagat', 'Krishi Darshan', etc. Flexibility of timing Catching attention of listeners	No visual information No visual impact Low recollection Short message life Small audience per station Very often message not clear Low attention value Lack of detailed advertising

F. Television

Strengths	**Weaknesses**
Attractiveness Wide reach Opportunity for high frequency campaign	Relative high cost Very brief, lacking details Short message life Production expensive and complicated

Demonstration “how it works” Prestige Emotionally involving	Long production lead live Lack of TV ownership by all.

G.Cinema

Advantages	**Disadvantages**
Allow product demonstration Emotionally involving Appropriate for products catering to low income segments	Short message life Cinema losing popularity because of cable operation. Slow exposure build up Long production lead time.

EFFECTIVENESS OF EACH MODE OF MEDIA

Mode	**Verbality**	**Visual Impact**	**Colour**	**Processing Time**	**Reach**	**Frequency**
TV	Low	High	High	Low	High	High
Radio	High	-	-	Low	Very high	High
Newpapers	High	OK	-	High	High	Low
Magazines	High	High	High	High	Low	Low
Outdoor	Can be high	High	High	High	Low	Low
POP	Can be high	High	High	High	Low	Low
Direct Mail	Very High	High	High	Very high	Depends	Very low

ADVERTISING AGENCY

An advertising agency acts as a consultant to the client, the advertiser, in formulating the advertising plans and translating them into an advertising campaign.

Another role of the agency is placing the advertisement in the media, since it has a traditional association with the media. The placement aspect has assumed considerable importance owing to media boom and the resultant complexities.

An advertising agency can be defined as an independent organisation of creative business people who develop, prepare and release the advertisements for the sellers seeking to find customers for their goods and services.

In India, there are about 7,000 advertising agencies out of which 700 ad agencies are recognized by the Indian Newspapers Society (INS). INS is a regulatory organisation regulating ad agencies for

- National Income Accounting
- Annual Billing
- Creditworthiness

The relationship between an advertiser and its advertising agency represents professionalism to the core. At the same time, capability in terms in culture and style of the two parties and the concerned persons is highly facilitatory for a fruitful relationship. Courage and candidness on the part of the agency can contribute much towards getting the client to appreciate the constructive use of a creative approach. It is in the interest of the client to provide the required reassurance to the agency so that communication is inhibited. The selection of an agency by a potential client has a degree of mutuality. A well considered and wise selection can pave the way for a productive relationship.

Functions of Ad Agencies

Ad agency will be in a position to take an objective view of the advertiser’s plan and proposals and thus venture to put forward its opinions and comments.

Creativem qualified and trained personnel are required for an advertising agency. It may not be worthwhile for an advertiser to have on its permanent staff all the variety of skill required to produce appropriate advertisements.

An agency provides an opportunity as well as flexibility for various combinations of agency personnel from different departments to form a team to work as per the specific requirements of their varied clients.

Advertising agency has regular contacts with various support systems required for the production of appropriate ad material. A major advantage of an agency is its regular dealing with the media and the expertise in developing advertisements to suit the requirements of its clients.

The ad agency's skills can also be useful in the preparation of campaigns where the risks involved are high such as in the introduction of new products.

Clients' Expectations

Account Service: Responsive – prompt - accessible – listens – economical.

Creativity Review: Provide innovative proposals – ideas – visuals.

Production Review: Quality – timeliness – accuracy – economical.

Media Planning: Innovative media strategy – capable of coping with the budget changes – provide media trends update.

Buying Media Space: Explore cost effective alternatives – ability to negotiate attractive terms.

Market Research: Relate existing studies to the specific situation of the client – organize timely and meaningful research.

Retail Advertising and Sales Promotion: Innovative ideas – POP material, creative events – timeliness – economical.

Financial Control: Detailed estimates – accuracy in billing – reasonable rates – mutual trust.

AGENCY EDUCATION PARAMETERS

- Knowledge of Client’s Business
- Contribution to Market Planning
- Responsiveness to brief
- Listen, understand pro-act (be responsive)
- Develop Strategies and Plan Creativity
- Ability to involve Key Agency Resources
- Readily Accessible
- Cost Consciousness
- Effective Event Planning

MEASURING ADVERTISING EFFECTIVENESS

Good planning and control of advertising depend critically on measurement of advertising effectiveness. A lot of effort is, therefore, spent on fundamental research on advertising effectiveness.

The most important measurement of advertising effectiveness is of an applied nature, dealing with specific ads and campaigns. Most of the money is spent by ad agencies on pre-testing ads, and much less is spent on post-evaluation of their effects. Many companies develop an advertising campaign, put it on the national market and then evaluate its effectiveness. It would be better for them to limit their campaign to one or a few cities first and evaluate its impact before rolling the campaign throughout the country with a very large budget.

Measuring advertising effectiveness could be of two types according to the objectives of the advertisers:

Communication Effect Research,

Sales Effect Research.

Communication Effect Research

The study seeks to discover if advertising is achieving the intended communication effect. This method is also known as “Copy Testing”. The objective of this research is an improvement in the present system.

The testing can be categorized into two types:

Pre-testing of advertising campaign, and

Post-testing of advertising campaign.

Three major methods of ad pre-testing are:

- Direct Rating
- Portfolio Test
- Laboratory Test

Direct Rating

In this type, respondents are asked questions to rate the alternative ads. These ratings are used to evaluate an ad’s attention, read through, cognitive, effective and behavioural strengths.

The following steps can be adopted.

Evaluate ad’s

- Attention strength
- Read through strength
- Cognitive strength
- Effective strength
- Behavioural strength

Method of evaluation through rating scale.

Primarily helps in screening out poor ads rather than identifying great ads.

Case Study

Volkswagen

Volkswagen, the fifth-largest automaker in the world, was founded in 1937. The first prototype was actually built in 1935 by Ferdinand Porsche, founder of the car company bearing his name, who had been commissioned by Hitler to build a “Peoples Car.” Volkswagen began selling its Beetles in North America in 1949, a year in which only two of the vehicles sold in the United States for $995 each. By 1955, the company had sold one million vehicles worldwide. Today, Volkswagen manufactures a number of other car brands, including Audi, Lamborghini, Bugatti, Bentley, Rolls-Royce, Skoda, and Seat.

Growth Years

With the help of creative and effective marketing, Volkswagen became a household name in America during the 1960s. The company’s marketing program in the United States during this decade was designed to make the brand’s underdog status an advantage. This was accomplished with self-deprecating advertising that made light of the Beetle’s shortcomings. Some memorable slogans for the Bug include “Think Small,” “It’s Ugly But It Gets There,” and “Nobody’s Perfect.” These self-effacing slogans ran counter to the advertising tradition of U.S. automakers, which usually involved lofty descriptions of a car’s style, power, grace, and superior design. The classic Beetle rapidly became a cult favorite, then a popular favorite, and eventually was to become the number-one selling car in history with over 22 million units sold. Volkswagen was not afraid to use the occasional hard sell. One particularly persuasive print ad paired a Volkswagen with a snowplow and a heavy blanket of snow on the ground and asked, “What do you think the snowplow driver drives to work?” Volkswagen also developed a stylish automobile called the Karmann Ghia, which was humorously advertised as the car “for people who can’t stand the sight of a Volkswagen.”

Decline and Recovery

After sales of VW cars in America peaked at 569,000 units in 1970, cutthroat competition among compacts, especially from Japanese manufacturers, hurt Volkswagen’s sales. The company also made an unfortunate marketing move that compounded its problems. It “Americanized” its image, by advertising the opening of an VW assembly line in

Pennsylvania—the first U.S. assembly line set up by a foreign auto maker—at a time when imports were become popular. The 1980s were not much better for the company, as sales continued to decline.

By 1990, Volkswagen was looking for ways to revitalize its business in the United States. Sales had slipped to a mere 1.3 percent of the American market from a high of 7 percent in 1970. The company developed an advertising campaign that centered on the word Fahrvergnugen, German for "driving pleasure." This strategy was considered a risk at the time because many assumed Americans would not adopt a German word as a slogan. The hard-to-pronounce word nevertheless became an instant pop-culture buzzword, but U.S. sales continued to drop to under 50,000 units. The company clarified its brand message under the umbrella of the "Drivers Wanted" slogan in 1995, and U.S. sales rose 18 percent to 135,907 cars in 1996.

Classic Influences Tempt Consumers

In 1998, Volkswagen released a modernized version of its iconic Beetle to a car-buying public nostalgic for the vintage style. Ads for the New Beetle echoed the irreverent humor of the ads from the 1960s, with one ad reading "If you sold your soul in the '80s, here's your chance to buy it back." Another ad emphasized the difference between the modern engine and notoriously underpowered traditional Beetle with the slogan "Less Flower, More Power." American buyers leapt at the chance to buy the classically influenced—but clearly modern—cars, often at well above sticker price. Waiting lists for the new cars, which sold more than 55,000 units in 1998, were common. The company also experimented with the Internet as a marketing and sales medium, holding a special Web-only launch of 2,000 New Beetles in two previously unavailable colors, Reflex Yellow and Vapor Blue. Volkswagen sold out its inventory immediately. By drawing consumers into Volkswagen showrooms, the New Beetle helped the company achieve 50 percent growth in sales volume between 1998 and 1999.

In 2001, the company unveiled its latest retro offering—the Microbus—as a concept car. The car, not expected to be available to the American public until 2003, will likely set off another wave of nostalgia and help the company achieve further sales growth. Other new models slated for introduction include a sport utility vehicle and a luxury V-8 Passat sedan designed to compete with BMW and Mercedes. Volkswagen's history of brilliant marketing will likely lead to success for these new models.

Source: Marketing Management , Philip Kotler

Questions

1. What are some of the ways in which Volkswagen epitomizes the meaning and value of the marketing concepts in the text?

2. Suggest creative extensions of VW's marketing tactics and strategies in applications of advertising, promotion, public relations and other promotional techniques?

Questions

1. "Money spent on advertisement is not wasteful." Critically examine this statement.
2. What are the objectives of advertising? Discuss the major ones?
3. What are the uses of advertising to various parties? Discuss?
4. How are the advertising functions organized in an organization?
5. Differentiate between the Advertising and Salesmenship?
6. What is advertising? Discuss its objectives and point out the problems of advertising in India?
7. Define Sales promotion? What are its objectives? Describe the various steps to be taken for promoting the sales of a big concern?
8. What are the various steps to be followed in planning the sales promotion?

Sales Force Decision

Sales Force Decision is generally termed as the backbone of marketing. Brech defines it as "overall management of sales and it refers to only a socialized application of the process of Management as a whole." According to the American Marketing Association the "planning, direction and control of the personal selling activities of a business unit include recruiting, selecting, training, equipping, assigning, rating, supervising, paying and motivating as these tasks apply to the personal sales force." The ultimate objective of Sales Management is to influence the consumers of the target market to get sales orders. A sales force serves as a company's personal link to customers.

Functions of A Sales organization

1. Analysing markets and sales policy.
2. Sales planning and sales forecasting
3. Deciding prices and terms of sales.
4. Selecting, training and controlling the sales force.
5. Deciding Sales programmes and sales promotion.
6. Advising about advertising and publicity.
7. Deciding and allocating territory and setting targets.
8. Preparing and maintaining customers' records, etc.
9. Preparing Sales Reports.

STEPS IN DESIGNING AND MANAGING A SALES FORCE

-- Setting of Objectives

-- Training for Sales Policies

-- Designing Sales Force Structure and Size

-- Deciding Sales Force Compensation

-- Recruiting and Motivating Sales Force

-- Guiding and Motivating Sales Force

-- Performance Rating of Sales Force

Organising and Managing a Sales Force

Sales force is regularly assigned particulars territories. Various factors are taken into account in deciding on the physical size of a territory, transportation links within territory, purchasing power of consumers and their educational and living standards.

Therefore, a sales force is deployed according to the geographical and product or consumer requirements. A company should also devote considerable effort in training and development of its sales force. There are two types of training which can be provided to sales force : (a) In –house training, and (b) on –the-job training. It is also necessary for a company to arrange periodic meetings and discussions with its Sales Force. Finally, the performance can be evaluated on the basis of targets and actual.

Sales Manager’s Duties and Responsibilities

The Sales Manager is the most important person in a Sales organization. All Activities are based on his functions and responsibilities. The following are some of the prime duties of a Sales Manager.

1. Organising sales research, product research, etc.
2. Getting the best output from the sales force under him.
3. Setting and controlling the targets, territories, sales expenses, distribution expenses etc.
4. Advising the company on various media, Sales promotion schemes, etc.
5. Monitoring the company’s sales policies.

Reid gives the following chart of the steps necessary for getting success in selling :

To Yourself	**To the Company**	**To our Customers**
Increase basic selling skills.	Be proud of your association with you company.	Work closely with decision takers and influencers in each account. Point out the advantages of an association with our company . Keep accounts current On all company advertising and promotional activities.
Study the latest products, promotion policies and procedures. Be alert to new sales and merchandising ideas.	Ges and developments in your territory. Be prompt in handing records, reports, correspondence, etc. Cut selling costs by economical routing, good use of time, planning and greater awareness of opportunity.	Suggest ideas, methods, techniques and tips that can stimulate sales. Inform the customers about the trends in their areas.

Grow so that you can assume greater responsibilities as opportunities permit. Maintain the appearance and deportment expected of a Territory Sales Manger. Analyse your weak and strong points and then think about them.	Check demand and movement of products in the territory. Report activities of the competitions	Handle complaints effectively and to the complete satisfaction of the complainants. Suggest the best technique For selling our products to the customers. Organise presentations to inform and save time.
	Strive to reach the best goals	Make the customers aware of the changes in the company's policies or procedures.
	Ask for help, when you need it.	Stimulate and maintain enthusiasm for your products.
	Co-operate with order departments of the company.	Build and maintain good will.

Source : Reid, A.L., Modern Applied Salesmanship 1971, p. 418

OUTLINE FOR COMPILING SALES JOB DESCRIPTIONS

Sales

-- Make regular visits

-- Market the full line

-- Handle questions and objections

-- Check finished goods stock

-- Interpret sales points of the line to the customer

-- Explain company policy on credit, merchandising, stock rotation, etc.

-- Get the order

-- Install product displays and other POP's

-- Report product weaknesses, complaints

-- Handle adjustments, returns, and allowances

-- Handle request for credit

-- Handle special orders for customers

-- Establish priorities, if any

Territory Management

-- Arrange route for best coverage

-- Balance effort with the customer against his potential volume

-- Maintain sales and important territory records.

Sales Promotion

-- Develop new prospects and accounts

-- Make calls with customer's salesmen in areas where " stockiest" are in force

-- Train the personnel of wholesalers, distributors, stockiest, etc. whenever requested by them.

Sales Executives

-- Each right make a daily work plan for the next day.

-- Organise field activity for minimum travel and maximum calls

-- Prepare and submit special report on trends, competition

-- Prepare and submit daily reports to home office.

-- Collect and submit daily reports to home office.

-- Attend sales meetings

-- Collect overdue accounts

-- Collect credit information

Goodwill

-- Counsel customers on their problems

-- Maintain loyalty and respect for the company

Source: S. Ramachandran, *Field Sales Management,* pp. 10-11

Sales Supervision

Sales supervision consists of giving instructions to sales force and seeing that they are carried out . Good supervision involves the development of skills in working with people and influencing them to do what you want them to do, and do it well.

It is true that salesmen are made, they are not born because, they are trained by their superiors. Personality, the ability to get along with people, was considered all-important. There are three areas in which sales trainer can impart the training to the sales force :

1. Product Training

It is most important that a salesmen must be thoroughly familiar with his product as well as product ranges. Proper emphasis should be given to teach product information in terms of the benefits which can be obtained by the customer. Salesmen must know the following aspects of the products:

-- Technical features

-- Technology

-- Quality

-- Packaging

-- Grading

-- Branding

2. Selling areas

-- Product history for sales quota attainment in each territory.

-- Sales ratios

-- Workload per sales person

-- Bills receivable analysis

-- Sales analysis report

3. Selling Skills

The sales person should be good in human relations and should have the following qualities :

-- Good Appearance

-- Good Communications
-- Self - Confidence
-- Creative
-- Proud of his association
-- Satisfy the curiosity of customers
-- Up – to –date knowledge of products

Takes of Sales organization

Organising the sales force is a typical sales management task, since its has direct impact on the sales manager's job performance. The universal adoption of the marketing concept has meant that most companies have reorganized their sales and marketing activities to reflect the stronger commitment to their customers. This trend has enhanced the importance of Sales force organization.

Developing a Sales Organisation

Developing a Sales organistion structure is not an easy task. The key to organizational design are consistency and coherence. The importance is highlighted as :

"Spans of control, degrees of job enlargement, forms of decentralization, planning systems and matrix structure should not be picked and chosen at random. Rather, they should be selected according to internally consistent groupings, and these groupings should be consistent with the situation of the organization – its age and size, the conditions of the industry in which it operates, and its production technology".

This means that sales managers must recognize, and then deal with, some basic organizational issues when developing a sales organization. The five major issues are :

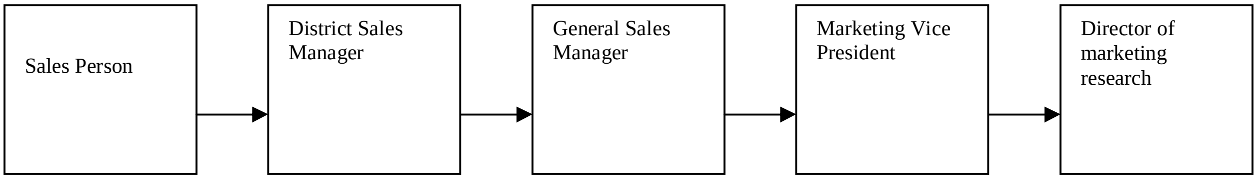
1. Formal and informal organisations

Every organization has a formal organisation and an informal organisation. The formal organisation is the creation of management, whereas the informal organisation is often developed from the social organisation. Also called the grapevine, the informal organization is basically a communication pattern that emerges to facilitate the operation of the formal organisation.

Consider the case of a field salesperson who is responsible for collecting certain competitive information, such as prices and trade discounts. If this information were forwarded through the formal organization, the data would be outdated and would be useless to management. The informal communication system, however, allows the information to be transmitted directly to the director of marketing research. The figure on page 490 shows an informal communication pattern that might exist in a marketing organization.

The figure below shows a lengthy formal communication channel:

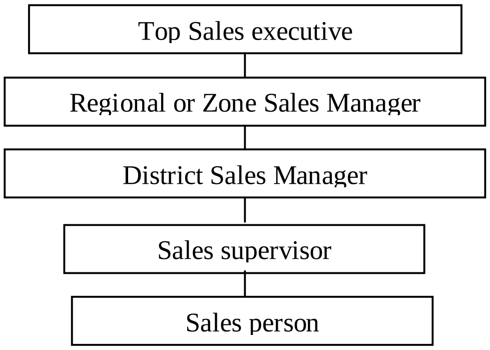
LENGTHY FORMAL COMMUNICATIONS CHANNEL


Sales Person
District Sales Manager
General Sales Manager
Marketing Vice President
Director of marketing research

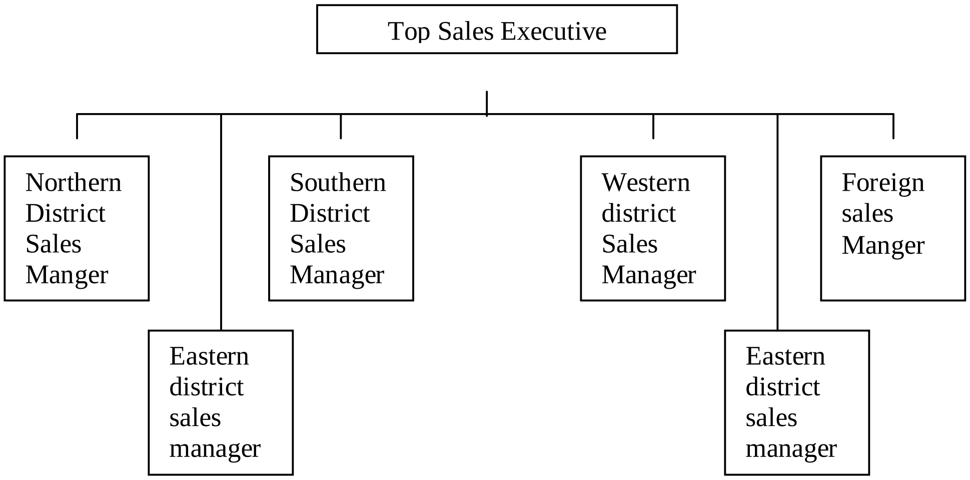
2. Horizontal and Vertical Organisations

Sales force can have either horizontal or vertical organizational format. The arrangement varies among companies, even within the same industry. The factor that determines whether a vertical or horizontal organizational structure should be employed is the effective span of control. The span of control refers to the number of employees who report to the next higher level in the organization. The following figures shows the formats of vertical sales organization and horizontal sales organistion.

VERTICAL SALES ORGANISATION


Top Sales executive
Regional or Zone Sales Manager
District Sales Manager
Sales supervisor
Sales person

HORIZONTAL SALES ORGANISATION


Top Sales Executive
Northern District Sales Manger
Southern District Sales Manager
Western district Sales Manager
Foreign sales Manger
Eastern district sales manager
Eastern district sales manager

3. Contralised and decentralized organisation

In a decentralized organisation, responsibility and authority are delegated to lower levels of sales management. In a centralised sales organization, the responsibility and authority for decisions are concentrated at higher levels of management. A related concern is the degree of centralization in the sales organization. This issue has to do with the organizational location of the responsibility and authority for specific management tasks.

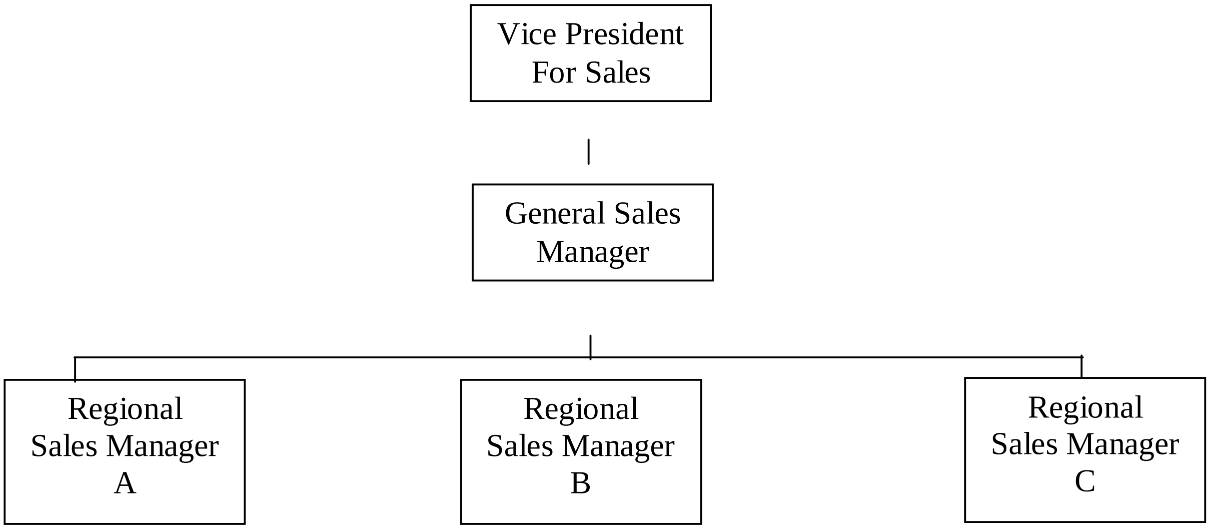
A decentralized organization structure is ineffective unless commensurate responsibility and authority accompany the assignment of decision to a specific level of sales management.

4. Line and Staff components

Marketing organizations also feature line and staff components. A line function is a primary activity and staff function is a supporting activity. In a marketing organization, the selling function is the line component, whereas advertising, marketing research, marketing planning, sales training and distributor relations are usually considered staff roles.

The following figure and the figure on the next page show a' line marketing organsation' and a 'line and staff marketing organsation'.

A LINE MARKETING ORGANISTION


Vice President
For Sales
General Sales
Manager
Regional
Sales Manager
A
Regional
Sales Manager
B
Regional
Sales Manager
C

MOTIVATING AND LEADING THE SALES FORCE

There are several rules which help a sales manger in developing sales force through motivation and leadership.

Rule 1

Work with sales team and not as members of groups. To achieve this, do the following :

-- Know your sales force personally

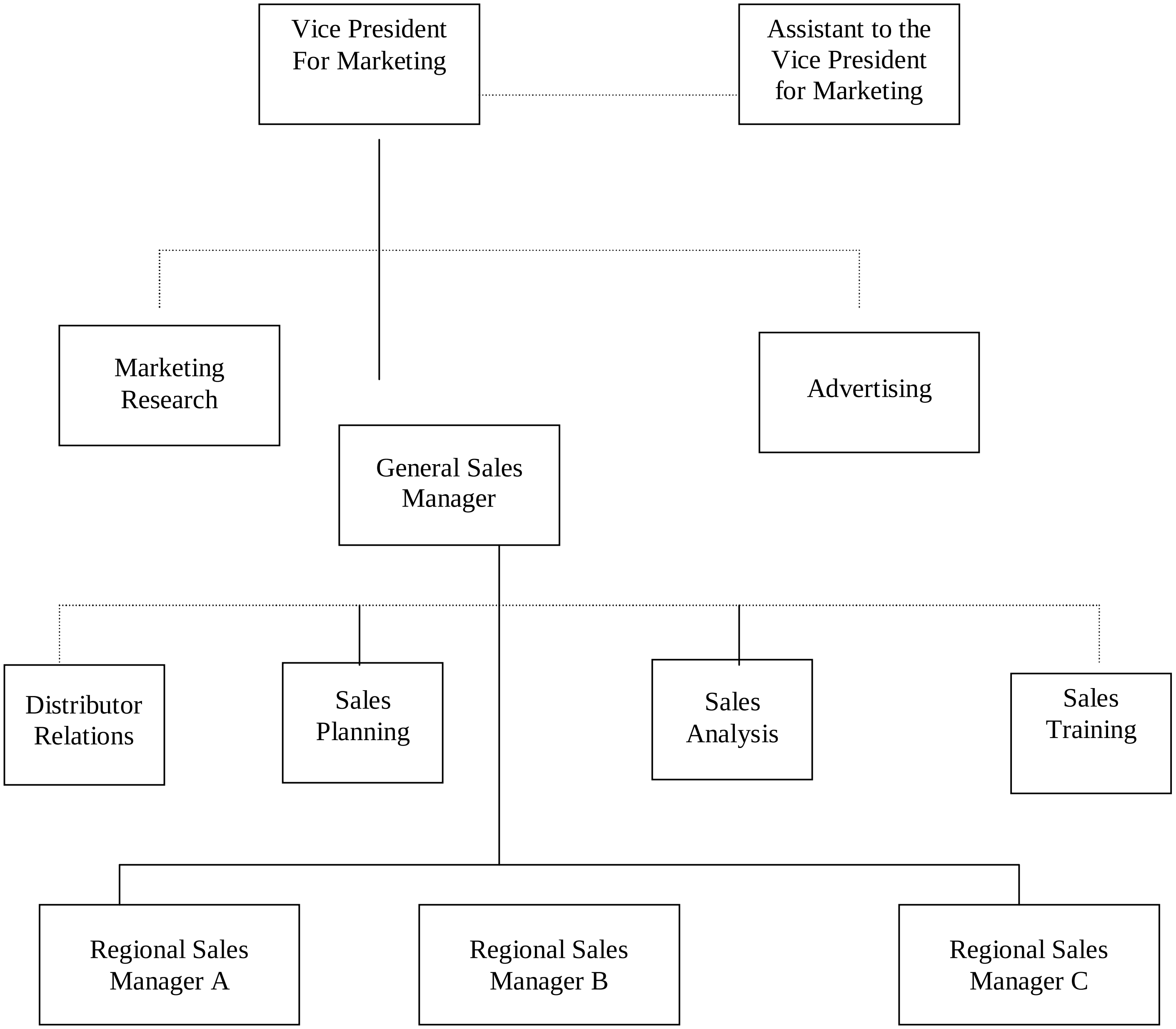
-- Give extra time for discussion and personal problem solving.

-- Do proper home work on sales assignments, be clear to the point of a fault, avoiding personal affront.

-- Explain your reason for change in territory and product likings. Change is always for the better.

-- Learn from your sales force about their hopes, aspirations, abilities and self worth.

LINE AND STAFF MARKETING ORGANISATION


Vice President For Marketing
Assistant to the Vice President for Marketing
Marketing Research
Advertising
General Sales Manager
Distributor Relations
Sales Planning
Sales Analysis
Sales Training
Regional Sales Manager A
Regional Sales Manager B
Regional Sales Manager C

Key ----- Line organization

_____ Staff Organization

-- Develop creative personality traits for example : Self esteem, self confidence, self worth to become a self starter and freedom from fear of failures.

-- Assume responsibility for mistakes, that is, be pro-active.

-- Be internally motivated.

Rule 2

-- Set high standards but realistic ones for your sales force.

-- Set high personal examples and accept mistakes as errors of judgment.

-- Ensure frankness in criticism which is self rewarding and educating to others.

Rule 3

Ensure that sales force are collaborative among themselves, that is , they work as a team and make full use of each other for collective goal achievement through.

-- Good means of communication, open and purposive.

-- Fostering full co-operation among seniors and juniors.

-- Developing individual capabilities, creative attitude and respect for each employee.

-- Encourage juniors to settle their own grievances themselves, rather than letting them rush up to you.

Rule 4

Fight for your people and for your ideas :

-- You are responsible for people under you ; so protect and promote them.

-- Support the men in trouble, don't be afraid of telling the faults of superiors against the juniors.

-- Help them in progress, get promotions, get noticed and remunerated.

Rule 5

-- Retain the principle of accountability as a check on exercise of delegated authority.

-- Promote the right 'men', pay right salaries and perks and put them in positions as deserved by them.

-- Pursue the policy of promotion from within as a win-win strategy.

-- Accept sales force feelings. Encourage them to open up, to address you as a friend in reed.

PERSONAL SELLING

This is a promotional tool. It is the oldest and a very lucrative and effective tool of promotion. Here the foot soldiers have the responsibility of promoting the product. Sales people form the very important part of a marketing group. According to 'AMA' : Personal selling is oral presentation to a buyer for the purpose of making sales'.

Basically, it is an art to persuade the customer to buy the product. A sales person should have the persuasive power. In addition a good sales person must have a detailed knowledge about four things :

1.Company

2.Competitors

3.Consumer

4. Product

A sales person should have positive attitude. Personal selling involves personal confrontation, *i.e.,* presentation should be lively. We can make changes according to the feed back and therefore it is a bit flexible tool as compared to advertisement.

In personal selling, some kind of a lasting and social relationship develops. This personal touch can only come in personal selling. Another advantage in the personal selling is that it can be used for consumer as well as for industrial goods.

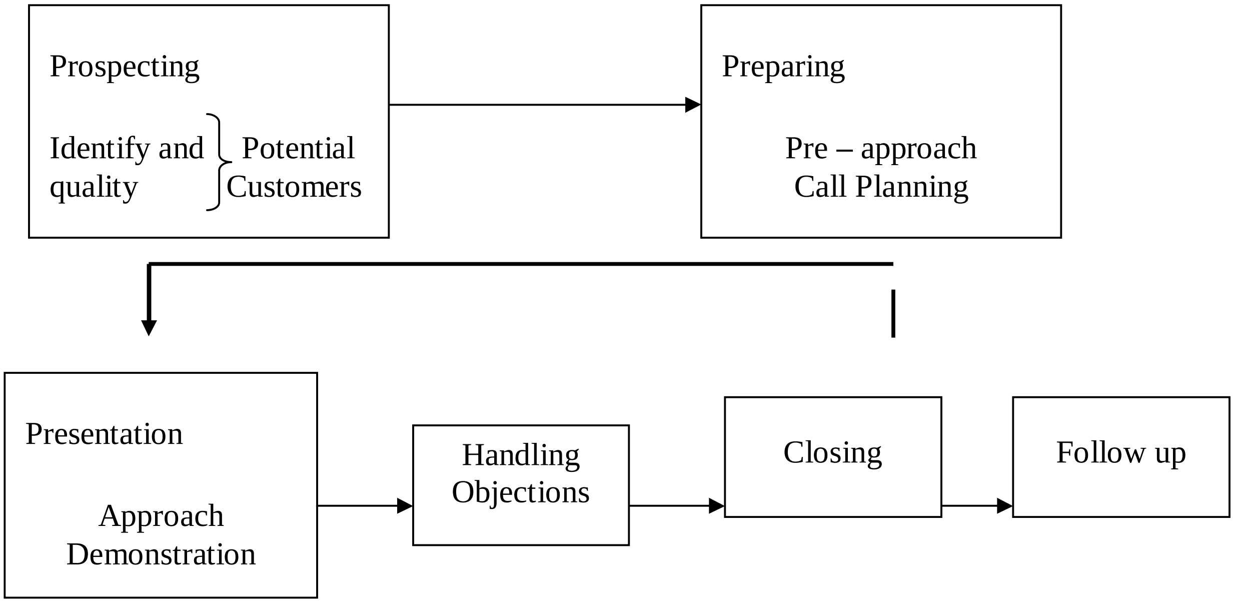
When Personal selling is required

1. When the product requires some kind of demonstration.
2. When the market under consideration is comparatively smaller.
3. For the specific needs of the customer, i.e., in case industrial goods.
4. For selling a service, *e.g.,* five star hotels, banking etc., sales people have got an edge.
5. When you have got an edge.
6. When you have got big orders.
7. When confidence is to be built up in the minds of customers.

Objectives of Personal Selling

Personal selling has been defined as the oral presentation to prospective customers of one's goods and services for the purpose of ultimately making a sale. All selling processes contain the same basic steps, though the detail of each step and time required to complete it, will vary according to the product that is being sold. For example, a door –to – door sales representative may go through all the steps from prospecting to closing of sale in a matter of ten to fifteen minutes ; in contrast, the selling process for computer or electronic typewriter may take several visits, even years, for getting an order. The selling process is shown below :

The Selling Process


Prospecting
Identify and quality
Potential Customers
Preparing
Pre – approach
Call Planning
Presentation
Approach
Demonstration
Handling Objections
Closing
Follow up

Source : *Sales Management Concepts, Practices* and Cases by Eugene M. Johnson, David L. Kurtz, Eberhard. E. Scheuing, McGrow- Hill Book Company.

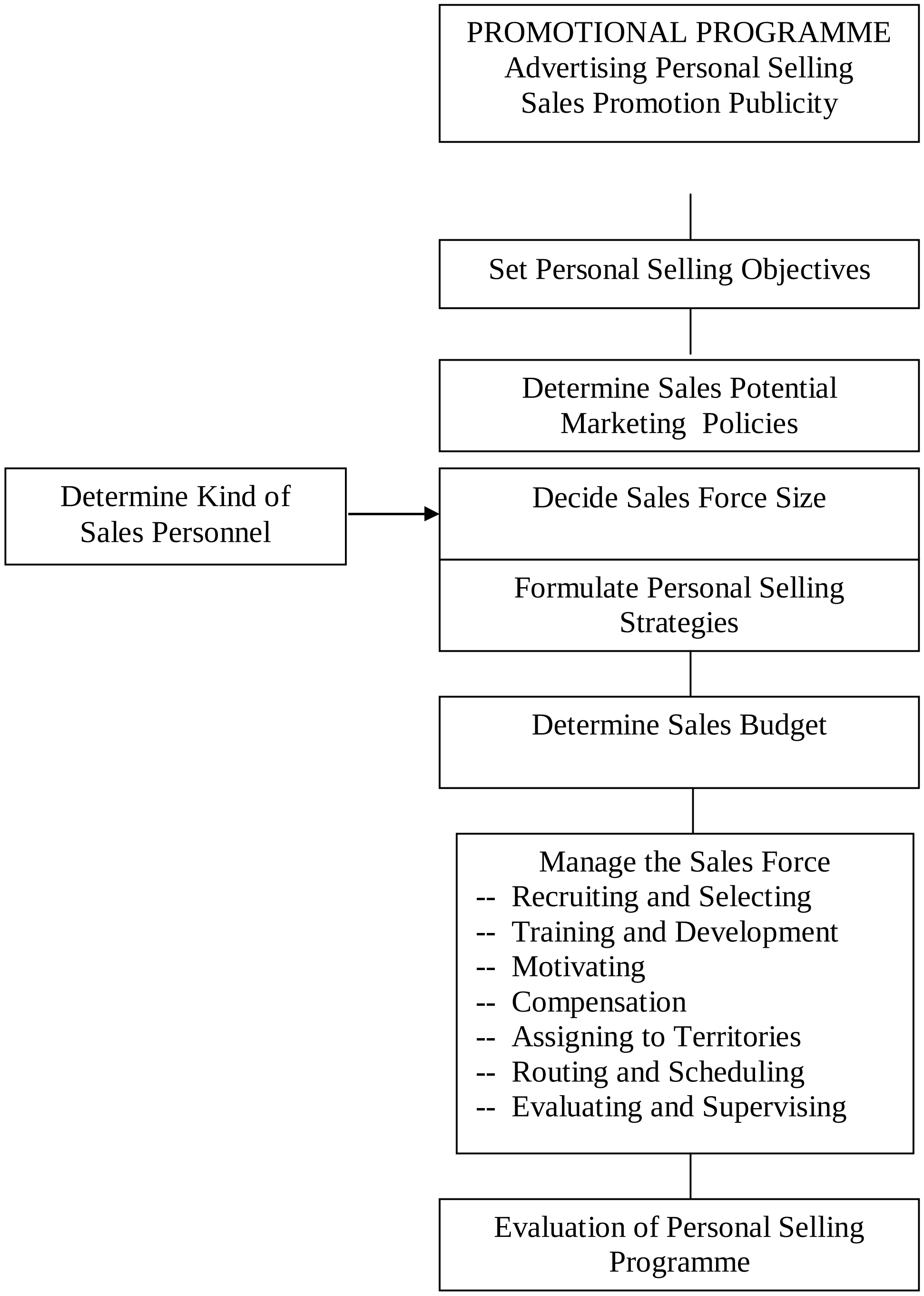
Objectives of personal selling can be briefly stated as sales, profits and growth for the organization in a continuum in order to ensure its survival. The following objectives are achieved through personal selling :

1. To carry out the complete selling job when some elements of the promotion mix are missing.

2. To serve the existing customers efficiently and effectively.

3. To look for new perspective customers for new / more orders.

PERSONAL SELLING MANAGEMENT CHART


PROMOTIONAL PROGRAMME
Advertising Personal Selling
Sales Promotion Publicity
Set Personal Selling Objectives
Determine Sales Potential
Marketing Policies
Determine Kind of
Sales Personnel
Decide Sales Force Size
Formulate Personal Selling
Strategies
Determine Sales Budget
Manage the Sales Force
-- Recruiting and Selecting
-- Training and Development
-- Motivating
-- Compensation
-- Assigning to Territories
-- Routing and Scheduling
-- Evaluating and Supervising
Evaluation of Personal Selling
Programme

4. To encourage the existing customers for their co-operation in the promotion of the various products of the company.

5. To keep the consumers informed time after time about the various changes in aspects of the marketing strategy and the product line of the company.

6. To provide complete assistance to the customers for selling the product line.

7. To provide proper assistance and advice to the customers regarding certain complicated products and the products for specific uses.

8. To assist and advise regarding the training programmes for the sales personnel of the middlemen / dealers.

9. To help the dealers in their management and related problems.

10. To collect recent information regarding the market and report this to the company (Information of company's use)

The quantitative objectives are assigned for a short term and they keep on changing depending upon the market situation from time to time. They are :

1. To retain the existing market share and try for increasing it.
2. To increase the sales volume and hence the profits. It also includes the striking of a proper balance between the different elements of the marketing mix of the different products of the company.
3. To make attempts to open new accounts and maintain the existing ones properly, effective and efficiency.
4. To exercise expense management and to keep the expenses within limits.
5. To achieve the targets and try to exceed them.

THEORIES OF SELLING

Old Approach : Generally the selling theories emphasized 'What to do' and 'How to do' rather than 'Why to do'. The theories are based upon the practical and experimental knowledge accumulated from the years of " living in the market", rather than on a systematic, fundamental body of knowledge.

The second or the *new approach* made use of the findings of the behavioural sciences. Theories according to the new approach :

1. AIDAS theory of selling – seller oriented
2. ‘Right set of the circumstances’ Theory of Selling – Seller – oriented.
3. ‘Buying Formula’ Theory of Selling – Buyer -oriented
4. ‘Behavioural Equation’ theory – Buyers’ decision process.

AIDAS Theory of Selling : In this theory AIDAS stands for

A - Attention

I - Interest

D - Desire

A - Action

S - Satisfaction

This theory tells about the consumer readiness stage. It is a psychological theory of selling which tells us about the consumer mind – the stages through which the mind passes. These stages are attention, interest, desire, action and satisfaction. This theory tells about the fact that the salesman should make the consumer pass through these five stages so that the purchase should occur.

Phase – I – Securing Attention :

1. Get the appointment with the consumer
2. Salesperson must show mental alertness and be a skilled conversationalist.
3. He should establish a good rapport at once and should be a conversation opener.
4. He should do his homework properly.
5. Good conversation opener causes the prospect to relax and sets stage for the overall presentation.

Phase –II – Gaining Interest : This deals with the evolvement of the strong interest of the consumer in the product, to develop a contagious enthusiasm for the product and to give facts and figures about the product. There should be a strong selling appeal to make their interest in the product. There should be a strong selling appeal to make their interest in the product very effective. Also the attitudes and the feelings toward the product should be clarified. Sales – person must take all these into account in selecting the appeal to be emphasized.

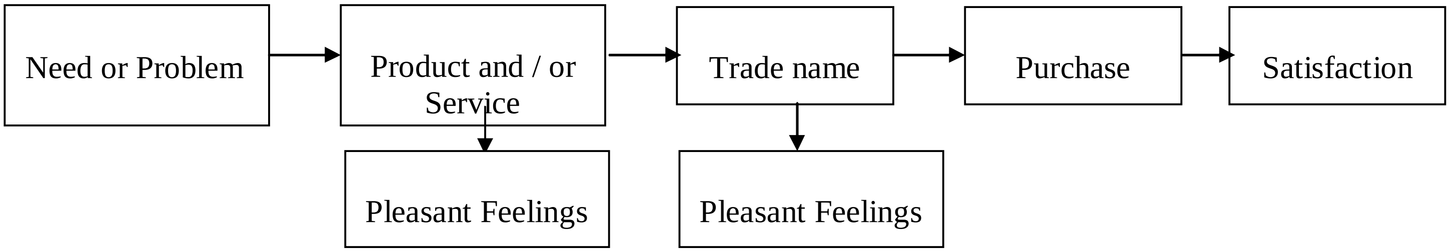
Phase III – Kindling Desire : Here the interest of the consumer is to be converted into the desire for buying the product. The ways should be found to face and dispose of the sales obstacles, the consumer objections, external interruptions, digressive remarks, etc. The consumer should be satisfied in all respects and all of his doubts should be cleared.

Phase IV – Inducting Action : The perfect presentation results in the readiness of the consumer to buy the product. All this requires experience of the sales personnel as the buying is not automatic and it should not be closed until the sales persons are positive that the right time has come. Most prospects find it easier to shy away from the hints than from frank requests for an order.

Phase V – Building Satisfaction : After the purchase generally the customer passes through the state of mental cognitive dissonance in post – purchase anxiety. Now this is the job of the sales person to relieve him of this tension and convince him that him decision was correct. Building satisfaction means thanking the customer for the order and also to make the customer feel delighted and also to assure him of the promises made by the salesman.

'Right set of circumstances' Theory of Selling : This theory is the 'situation response' theory which tells that everything was right for the sale. It also states that the skills of the sales persons have a lot of effect on the sales to take place. Also, if the sales persons have a lot of effect on the sales to take place. Also, if the sales person presents the proper stimuli or appeals, the desired response will result. This theory tells about two types of factors which constitute the set of circumstances. The factors are internal and external. This theory stresses the external factors at the expenses of the internal factors. This is a seller – oriented theory and stresses the importance of the sales persons in the process of selling of a product. The major drawbacks of this theory are : 1. It does not take care of the internal factors. 2. It fails to attach appropriate weight to the response side of the situation – response interaction.

‘Buying Formula’ Theory of Selling : This theory is buyer –oriented theory. This is a psychological theory and takes care of the buyer – related problems and revolves round the buyer. This theory explains the cognition process which goes on in the mind of the buyer when he has to take the decision regarding to buy or not to buy. This theory has come through various stages of its development and thus has taken its present picture.



When a buying habit is being established, the buyer must know why the product or service is an adequate solution to the need or problem, and why the trade name is the best one to buy. This theory tells that :

1.The need should be created/ Emphasized.

2.The relation between the need and the product or service should be emphaised.

3.The brand image should be created.

4. The need, product/ service and the trade name / brand image should be associated with each other.

5. The brand loyalty and the customer delight should be emphasized.

‘Behavioural Equation’ Theory : This theory takes care of the buyer’s decision making process and goes in the detail of the process at the micro / internal level. The buyer goes through various stages of learning process. The essential elements of the learning process are :

1. Drive (Motivation)
2. Cue
3. Response
4. Reinforcement

Drives are strong internal stimuli which impel the buyers’ response. These drives are of two types. They are 1. Innate drives – psychological or biogenic drives and 2. Learned drives – social drives.

Cues are the weak stimuli that determine when the buyer will respond. There are 2 types of cues : 1. Triggering cues – activate the decision process. 2. No triggering cues- influence but does not activate the decision process.

Response is what the buyer does.

Reinforcement strengthens the buyer's tendencies to make a particular response.

Hence this theory takes care of the behavioral aspects of the buyer and how it influences his decisions and his learning process. This also tells about the sales person's role in all this to make it happen and at the same time it reduces buyer dissonance.

SALES STRATEGIES

Sales strategies are the policies which are made to provide the guidelines for taking key decisions in personal selling. It includes the following :

1. Size of the sales force required
2. Kind of the sales force required
3. Roles of the sales person
4. Assigning of the sales territories.

The effectiveness and the efficiency with which these roles are played by the sales force, determine the extent to which overall personal selling objectives are achieved. The company's competitive posture is shaped by :

1. Product Market Analysis
2. Sales person's order securing analysis
3. Choice of the basic selling style :

(a) Trade Selling
(b) Missionary Selling
(c) Technical Selling
(d) New business selling

The size of the sales force can be determined by utilizing one or more of the following methods in combination with each other :

1. Work Load Method
2. Sales Potential Method
3. Incremental Method

Individualizing selling strategies to Customer

The acid test of the appropriateness of personal selling strategy comes when particulars salespersons interact with particular customers. The Management makes its first key decision on personal selling strategy. When it determines the size of the company's sales force, each salesperson must individualise his own dealing with each customer. The decisions of the above kind are implemented after the required kind and size of the sales force has been recruited, trained and assigned their fields and territories. The strategies should be such so as to benefit the customer and help the firm in achieving its objectives. The strength of the sales force depends upon its communication and convincing power to persuade the customer to buy the product. The approach of the sales person towards different buyers is a matter of his selling skills. This skill is the function of the preplanning and performance on the call of the sales person itself.

The individual members of the sales force determine the success and failure of the company's overall personal selling strategy and sales management. The efficiency and effectiveness of the sales management in the personal selling field. The sales persons should combine their efforts in such a way so as to achieve their personal objectives through the achievement of the firm's objectives.

Questions

1. What do you mean by personal selling? What is the importance of personal selling?
2. What are the advantages and disadvantages of personal selling?
3. How is personal selling different from advertising?
4. Discuss the process of selling? Also discuss the AIDA concept of personal selling?
5. What is sales management? What are the various functions of sales management?
6. Explain the basic theories of sales management?
7. What is meant by training of sales personnel? Discuss?

Debt and Equity Financing

Company financing is a prior concern for operating any business, and financing is arranged before any business plans are made. Debt financing and equity financing are the two financing options most commonly pursued by companies. Debt financing refers to borrowing funds which must be repaid, plus interest, while equity financing refers to raising funds by selling shareholding interests in the company.

Most companies use a combination of these two different types of financing in the course of their business life. Loan borrowing, bond issuance, and issuance and sale of shares are the main vehicles for company financing. Direct financing from the capital markets (i.e. stock and debt markets) dominates the indirect financing intermediated by banks and finance companies. With this in mind, certain types of bank loans will require that the company maintain a balance of equity and debt (called its leverage ratio) that is appropriate for the industry and the stage of business in which it is operating.

Typical Uses for Debt and Equity Financing

Equity investment is generally required for funding the start-up plant assets and the company's initial operating expenses, as there is no track record of transactions resulting in cash flows, which the business uses in support of debt and interest payments. Presently, the stock market has been functioning well in Hong Kong, channelling substantial amounts of capital to the corporate sector.

Short-term debt is used to finance current assets that can be quickly turned back into cash; examples of this type of debt are accounts receivable and inventories. Noncurrent liabilities in the form of long-term debt, or loans, are used to finance long term assets, such as the purchase of land and the construction of a building or ship.

Debt Financing

Debt financing refers to the borrowing of loans from other companies, banks, or financial institutions in order to support a business's operations. The loan principal is repaid at a later point in time, with some interest expenses being paid before the debt's maturity.

Advantages of Debt Financing

The first advantage is maintenance of complete control over the business. The lender charges a company interest for the use of a loan, but the lender does not have the right to say how a company should manage its business. The ownership of the business stays completely in the hands of the corporate directors and shareholders. This also means that lenders will not be entitled to any of the profits that companies make from the business; the borrowing company is merely required to repay the loan within the fixed time period.

Debt financing is appropriate for companies which pursue an aggressive growth strategy, especially when they have access to low interest rates. Though a company may lose some of its assets if it is unable to repay its loans, the company won't lose corporate control or ownership to outsiders. Companies wishing to make use of debt financing are recommended to seek appropriate legal advice from the company's lawyers and accountants for better information on asset protection.   The second advantage of debt financing is related to loan repayment interest. Companies can deduct their interest payments (but not the principal repayments) as a business expense. The interest rate which a company pays is usually based on the prime interest rate, and the interest that the company has to pay on a company loan is tax-deductible. This means that debt financing covers up part of a company's business income from taxes and reduces the company's tax liability.

The third advantage to debt financing is credit maintenance. Continuity of debt borrowing can help to establish a company's record of creditworthiness. This will prove beneficial in the future when a company seeks to obtain bank loans and to achieve competitive company insurance rates from banks.

Disadvantages of Debt Financing

The first major disadvantage of debt financing is that companies need to pay back not only the principal of the loans, but also the interest, which may create a financial burden. This financial obligation must be treated as a liability on a company's statement of financial position. Since a company will often choose to borrow funds to pay for its business operations, the company may end up committing itself to large business expenses, thereby forcing it to transfer its holding rights to another company. The company may also be under pressure to repay its loans with cash that it badly needs for some other aspects of its business, and the company's business will suffer as a consequence.

The second disadvantage of company financing concerns the process of securing a loan. If companies borrow from banks or other financial companies, they will often be required to pledge company properties as collateral to secure the loan. This means that if a company does not repay its loans, then the lender can take the properties and sell them on the market in order to recover the value of the loan obligation. Thus, if a company pledges its business assets as collateral for the loans, and it is unable to pay back its creditors, then the company may lose important corporate assets.

Similarly, if a company pledges its personal assets, such as company properties or its stock portfolio, then it may risk losing them to pay back business loans.

The third disadvantage of credit financing is that obtaining business loans can be very difficult if a company does not have a good credit rating and strong track record of loan repayment. Furthermore, if a company carries too much debt, then that company may come to be seen as "high risk" by potential investors; this will limit the company's ability to raise capital via equity financing as well; this constraint can severely limit future cash flow.

The fourth disadvantage of debt financing is that debt can stifle a company's growth because of the high cost of repaying the loan, especially in the case of repaying compounding interest. This in turn increases a company's risk of bankruptcy. Related to this and the previous point, banks will often not accept a high leverage ratio for company, as high leverage ratios can be seen to be very risky. In such a scenario, a company may instead have to resort to the use of equity financing, i.e. issuing share capital, to balance its sources of financing.

Equity Financing

Equity financing refers to the issuing of shares to investors in order to support a company's business operations. This mode of financing is especially important during a company's start-up stage. In this method of financing, investors make gains when there is an increase in the share price, as well as through the distribution of dividends by the company in which the investor has purchased a stake.

Advantages of Equity Financing

The first advantage of equity financing is that it offers another source of funding besides arranging for loans from banks or other financial companies. A company may use funds from business investors when it begins its business operations to cover the start-up costs. The company can then use the cash flow from its operations to directly grow the company or to diversify into other areas. Related to this is the fact that investors tend to take a long-term view, and typically don't expect an immediate return on their investment. This allows the company to keep more cash on hand to expand the business, rather than having to pay a portion of its profits to repay loans. For this reason, this method of financing is less risky than debt financing because the company doesn't have to pay back its shareholders. This fact also makes equity financing a good option when a company cannot afford to take on (more) debt.

A second, related advantage to equity financing is that equity financing helps to confer legitimacy, by enabling companies to tap into investor networks and thereby to enhance their credibility.

The third advantage of equity financing is that if companies have prepared prospectuses for corporate investors and explained to them that their money is at risk in the companies' brand new start-up business, then investors will understand that if the business fails, they will not get their investment back.

Finally, equity financing offers additional advantages in terms of management of the company. Some prospective investors may be able to offer valuable business assistance that a company may not be able to provide for itself. Investors provide invaluable assistance in the form of management expertise, business contacts and access to other sources of capital. Quite a number of good investors and Venture Capitals assume the role of business advisors or even come on board fully as part of the management team. This can be important, especially in the start-up period of a new business.

Disadvantages of Equity Financing

The most important disadvantage is that investors must be granted some ownership of the company and a certain percentage of the profits. If the company's business takes off, then the company will have to share a portion of its earnings with the equity investors. Over time, the distribution of profits to shareholders may exceed the sum that a company would have had to pay for loans.

Venture Capitals often request an equity stake of 35–51%, especially when companies are just start-up companies without a strong financial background. The potential for equity financing may be limited for this reason, as company directors are sometimes unwilling to dilute their controlling power through equity financing.

Demand Forecasting: Evidence-based Methods

A chapter for the forthcoming book
Strategic Marketing Management: A Business Process Approach,
edited by Luiz Moutinho and Geoff Southern.

J. Scott Armstrong
The Wharton School, University of Pennsylvania

Kesten C. Green
Department of Econometrics and Business Statistics, Monash University

Demandforecasting35.doc
January 13, 2006

INTRODUCTION

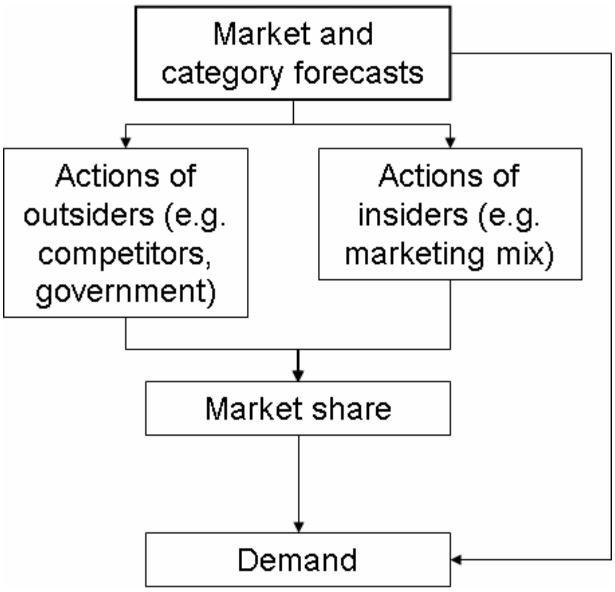
We looked at evidence from comparative empirical studies to identify methods that can be useful for predicting demand in various situations and to warn against methods that should not be used. In general, use structured methods and avoid intuition, unstructured meetings, focus groups, and data mining. In situations where there are sufficient data, use quantitative methods including extrapolation, quantitative analogies, rule-based forecasting, and causal methods. Otherwise, use methods that structure judgement including surveys of intentions and expectations, judgmental bootstrapping, structured analogies, and simulated interaction. Managers' domain knowledge should be incorporated into statistical forecasts. Methods for combining forecasts, including Delphi and prediction markets, improve accuracy. We provide guidelines for the effective use of forecasts, including such procedures as scenarios. Few organizations use many of the methods described in this paper. Thus, there are opportunities to improve efficiency by adopting these forecasting practices.

Marketing practitioners regard forecasting as an important part of their jobs. For example, Dalrymple (1987), in his survey of 134 US companies, found that 99% prepared formal forecasts when they developed written marketing plans. In Dalrymple (1975), 93% of the companies sampled indicated that sales forecasting was 'one of the most critical' aspects, or a 'very important' aspect of their company's success. Jobber, Hooley and Sanderson (1985), in a survey of 353 marketing directors from British textile firms, found that sales forecasting was the most common of nine activities on which they reported.

We discuss methods to forecast demand. People often use the terms 'demand' and 'sales' interchangeably. It is reasonable to do so because the two equate when sales are not limited by supply.

Sometimes it is appropriate to forecast demand directly. For example, a baker might extrapolate historical data on bread sales to predict demand in the week ahead. When direct prediction is not feasible, or where uncertainty and changes are expected to be substantial, marketing managers may need to forecast the size of a market or product category. Also, they would need to forecast the actions and reactions of key decision makers such as competitors, suppliers, distributors, collaborators, governments, and themselves – especially when strategic issues are involved. These actions can help to forecast market share. The resulting forecasts allow one to calculate a demand forecast. These forecasting needs and their relationships are illustrated in Figure 1.

FIGURE 1
Needs for marketing forecasts


Market and category forecasts
Actions of outsiders (e.g. competitors, government)
Actions of insiders (e.g. marketing mix)
Market share
Demand

FORECASTING METHODS

In this section we provide brief descriptions of forecasting methods and their application. Detailed descriptions are provided in forecasting textbooks such as Makridakis, Wheelwright, and Hyndman (1998).

Forecasting methods and the relationships between them are shown in Figure 2, starting with the primary distinction between methods that rely on judgement and those that require quantitative data.

Put FIGURE 2: Methodology Tree for Forecasting about here

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Methods Based on Judgment

Unaided judgment

It is common practice to ask experts what will happen. This is a good procedure to use when

- experts are unbiased
- large changes are unlikely
- relationships are well understood by experts (e.g., demand goes up when prices go down)
- experts possess privileged information
- experts receive accurate and well-summarized feedback about their forecasts.

Unfortunately, unaided judgement is often used when the above conditions do not hold. Green and Armstrong (2005a), for example, found that experts were no better than chance when they use their unaided judgement to forecast decisions made by people in conflict situations. If this surprises you, think of the ease with which producers of current affairs programmes seem able to assemble plausible experts who confidently express forecasts on how a situation will turn out, or how things would have turned out had they followed another approach.

Prediction markets

Prediction markets, also known as betting markets, information markets, and futures markets have a long history. Between the end of the US Civil War and World War II, well-organized markets for betting on presidential elections correctly picked the winner in every case but 1916; also, they were highly successful in identifying those elections that would be very close (Rhode and Strumpf, 2004). More recently, in the four elections prior to 2004, the Iowa Electronic Markets (IEM) has performed better than polls in predicting the margin of victory for the presidential election winner. In the week leading up to the election, these markets predicted vote shares for the Democratic and Republican candidates with an average absolute error of around 1.5 percentage points. The final Gallup poll, by comparison, yielded forecasts that erred by 2.1 percentage points (Wolfers and Zitzewitz, 2004).

Despite numerous attempts since the 1930s, no methods have been found to be superior to markets when forecasting prices. However, few people seem to believe this as they pay handsomely for advice about what to invest in.

Some commercial organisations provide internet markets and software that to allow participants to bet by trading contracts. Markets can be used to market to predict such things as the percentage of US households with an HDTV by the end of a given time period. Confidential betting markets can also be set up within firms to bet on such things as the sales growth of a new product. Some unpublished studies suggest that they can produce accurate sales forecasts when used within companies. However, there are no empirical studies that compare forecasts from prediction markets with those from traditional groups or from other methods.

Delphi

The Delphi technique was developed at RAND Corporation in the 1950s to help capture the knowledge of diverse experts while avoiding the disadvantages of traditional group meetings. The latter include bullying and time-wasting.

To forecast with Delphi the administrator should recruit between five and twenty suitable experts and poll them for their forecasts and reasons. The administrator then provides the experts with anonymous summary statistics on the forecasts, and experts' reasons for their forecasts. The process is repeated until there is little change in forecasts between rounds – two or three rounds are usually sufficient. The Delphi forecast is the median or mode of the experts' final forecasts. Software to guide you through the procedure is available at forecastingprinciples.com.

Rowe and Wright (2001) provide evidence on the accuracy of Delphi forecasts. The forecasts from Delphi groups are substantially more accurate than forecasts from unaided judgement and traditional groups, and are somewhat more accurate than combined forecasts from unaided judgement.

Structured analogies

The outcomes of similar situations from the past (analogies) may help a marketer to forecast the outcome of a new (target) situation. For example, the introduction of new products in US markets can provide analogies for the outcomes of the subsequent release of similar products in other countries.

People often use analogies to make forecasts, but they do not do so in a structured manner. For example, they might search for an analogy that suits their prior beliefs or they might stop searching when they identify one analogy. The structured-analogies method uses a formal process to overcome biased and inefficient use of information from analogous situations.

To use the structured analogies method, an administrator prepares a description of the target situation and selects experts who have knowledge of analogous situations; preferably direct experience. The experts identify and describe analogous situations, rate their similarity to the target situation, and match the outcomes of their analogies with potential outcomes in the target situation. The administrator then derives forecasts from the information the experts provided on their most similar analogies.

There has been little research on forecasting using analogies, but results are promising. Green and Armstrong (2005b) found that structured analogies were more accurate than unaided judgment in forecasting decisions in eight conflicts. Further information on structured analogies is available at conflictforecasting.com.

Game theory

Game theory has been touted in textbooks and research papers as a way to obtain better forecasts in situations involving negotiations or other conflicts. A Google search for “game theory” and “forecasting” or “prediction” identified 147,300 sites. Despite a vast research effort, there is no research that directly tests the forecasting ability of game theory. However, Green (2002, 2005) tested the ability of game theorists, who were urged to use game theory in predicting the outcome of eight real (but disguised) situations. In that study, game theorists were no more accurate than university students.

Judgmental Decomposition

The basic idea behind judgemental decomposition is to divide the forecasting problem into parts that are easier to forecast than the whole. One then forecasts the parts individually, using methods appropriate to each part. Finally, the parts are combined to obtain a forecast.

One approach is to break the problem down into multiplicative components. For example, to forecast sales for a brand, one can forecast industry sales volume, market share, and selling price per unit. Then reassemble the problem by multiplying the components together. Empirical results indicate that, in general, forecasts from decomposition are more accurate than those from a global approach (MacGregor 2001). In particular, decomposition is more accurate where there is much uncertainty about the aggregate forecast and where large numbers (over one million) are involved.

Judgmental bootstrapping

Judgmental bootstrapping converts subjective judgments into structured procedures. Experts are asked what information they use to make predictions about a class of situations. They are then asked to make predictions for diverse cases, which can be real or hypothetical. For example, they might forecast next year’s sales for alternative designs for a new product. The resulting data are then converted to a model by estimating a regression equation relating the judgmental forecasts to the information used by the forecasters. The general proposition seems preposterous. It is that the model of the man will be more accurate than the man. The reason is that the model applies the man’s rules more consistently.

Judgemental bootstrapping models are most useful for repetitive complex forecasting problems where data on the dependent variable are not available (e.g. demand for a new telecommunications device) or data does not vary sufficiently for the estimation of an econometric model.

Once developed, judgmental bootstrapping models provide a low-cost procedure for making forecasts. The review in Armstrong (2001a) found that judgmental bootstrapping was more accurate than unaided judgment (the normal method for these situations) in 8 of the 11 comparisons, with two tests showing no difference, and one showing a small loss. The typical error reduction was about 6%.

Judgmental bootstrapping also allows experts to see how they are weighting various factors. This knowledge can help to improve judgmental forecasting. For example, with respect to personnel selection, bootstrapping might reveal that some factors, such as height, weight or looks, are used, even though they are not relevant for the job. Bootstrapping also allows for estimating effects of changing key variables when historical data are not sufficient to allow for estimates.

Expert systems

As the name implies, expert systems are structured representations of the rules experts use to make predictions or diagnoses. For example, '*if* local household incomes are in the bottom quartile, *then* do not supply premium brands'. The forecast is implicit in the foregoing conditional action statement: i.e., premium brands are unlikely to make an acceptable return in the locale. Rules are often created from protocols, whereby forecasters talk about what they are doing while making forecasts. Where empirical estimates of relationships from structured analysis such as econometric studies are available, expert systems should use that information. Expert opinion, conjoint analysis, and bootstrapping can also aid in the development of expert systems.

Expert systems forecasting involves identifying forecasting rules used by experts and rules learned from empirical research. One should aim for simplicity and completeness in the resulting system, and the system should explain forecasts to users.

Developing an expert system is expensive and so the method will only be of interest in situations where many forecasts of a similar kind are required. Expert systems are feasible where problems are sufficiently well-structured for rules to be identified.

Collopy, Adya, and Armstrong (2001), in their review, found that expert systems forecasts are more accurate than those from unaided judgement. This conclusion, however, was based on only a small number of studies.

Simulated interaction

Simulated interaction is a form of role playing for predicting decisions by people who are interacting with others. It is especially useful when the situation involves conflict. For example, one might wish to forecast how best to secure an exclusive distribution arrangement with a major supplier.

To use simulated interaction, an administrator prepares a description of the target situation, describes the main protagonists' roles, and provides a list of possible decisions. Role players adopt a role and read about the situation. They then improvise realistic interactions with the other role players until they reach a decision; for example to sign a trial one-year exclusive distribution agreement. The role players' decisions are used to make the forecast.

Using eight conflict situations, Green (2005) found that forecasts from simulated interactions were substantially more accurate than can be obtained from unaided judgement. Simulated interaction can also help to maintain secrecy. Information on simulated interaction is available from conflictforecasting.com.

Intentions and expectations surveys

With intentions surveys, people are asked how they intend to behave in specified situations. In a similar manner, an expectations survey asks people how they expect to behave. Expectations differ from intentions because people realize that unintended things happen. For example, if you were asked whether you intended to visit the dentist in the next six months you might say no. However, you realize that a problem might arise that would necessitate such a visit, so your expectations would be that the event had a probability greater than zero. This distinction was proposed and tested by Juster (1966) and its evidence on its importance was summarised by Morwitz (2001).

Expectations and intentions can be obtained using probability scales such as Juster's eleven-point scale. The scale should have descriptions such as 0 = 'No chance, or almost no chance (1 in 100)' to 10 = 'Certain, or practically certain (99 in 100)'.

To forecast demand using a survey of potential consumers, the administrator should prepare an accurate and comprehensive description of the product and conditions of sale. He should select a representative sample of the population of interest and develop questions to elicit expectations from respondents. Bias in responses should be assessed if possible and the data adjusted accordingly. The behaviour of the population is forecast by aggregating the survey responses.

Useful methods have been developed for selecting samples, obtaining high response rates, compensating for non-response bias, and reducing response error. Dillman (2000) provides advice for designing surveys. Response error (where respondent information is not accurately reported) is probably the largest component of total error for marketing problems.

Expectations are most likely to be useful in cases where survey respondents have previously indulged in the behaviour of interest, for example visited a theme park. Other conditions favouring the use of expectations surveys are: (1) responses can be obtained; (2) the behaviour is important to the respondent; (3) the behaviour is planned; (4) the plan is reported correctly; (5) the respondent is able to fulfil the plan; (6) the plan is unlikely to change (Morwitz 2001).

Intentions and expectations surveys are especially useful when demand data are not available, such as for new product forecasts.

One popular type of survey, focus groups, violates five important principles and they should not, therefore, be used in forecasting. First, focus groups are seldom representative of the population of interest. Second, the responses of each participant are influenced by the expressed opinions of others in the group. Third, a focus group is a small sample – samples for intentions or expectations surveys typically include several hundred people whereas a focus group will consist of between six and ten individuals. Fourth, questions for the participants are generally not well structured. And fifth, summaries of focus groups responses are often subject to bias. There is no evidence to show that focus groups provide useful forecasts.

Conjoint analysis

By surveying consumers about their preferences for alternative product designs in a structured way, it is possible to infer how different features will influence demand. Potential customers might be presented with a series of perhaps 20 pairs of offerings. For example, various features of a personal digital assistant such as price, weight, battery life, screen clarity and memory could be varied substantially such that the features do not correlate with one another. The potential customer is thus forced to make trade-offs among various features by choosing one of each pair of offerings in a way that is representative of how they would choose in the marketplace. The resulting data can be analysed by regressing respondents' choices against the product features. The method, which is similar to bootstrapping, is called 'conjoint analysis' because respondents *consider* the product features *jointly*.

In general, the accuracy of forecasts from conjoint analysis is likely to increase with increasing realism of the choices presented to respondents (Wittink and Bergesteun 2001). The method is based on sound principles, such as using experimental design and soliciting independent intentions from a sample of potential customers. Unfortunately however, there do not appear to be studies that compare conjoint-analysis forecasts with forecasts from other reasonable methods.

Methods requiring quantitative data

Extrapolation

Extrapolation methods use historical data on that which one wishes to forecast. Exponential smoothing is the most popular and cost effective of the statistical extrapolation methods. It implements the principle that recent data should be weighted more heavily and 'smoothes' out cyclical fluctuations to forecast the trend. To use exponential smoothing to extrapolate, the administrator should first clean and deseasonalise the data, and select reasonable smoothing factors. The administrator then calculates an average and trend from the data and uses these to derive a forecast (Makridakis, Wheelwright & Hyndman 1998).

Statistical extrapolations are cost effective when forecasts are needed for each of hundreds of inventory items. They are also useful where forecasters are biased or ignorant of the situation (Armstrong 2001b).

Allow for seasonality when using quarterly, monthly, or daily data. Most firms do this (Dalrymple 1987). Seasonality adjustments led to substantial gains in accuracy in the large-scale study of time series by Makridakis et al. (1984). They should be dampened because seasonal adjustment programs tend to over-adjust for seasonality (Miller and Williams 2004); this follows the principle of being conservative in the face of uncertainty. Software for calculating damped seasonal adjustment factors is available at forecastingprinciples.com.

Retail scanner technology provides reliable and up-to-date data for extrapolating sales of existing products. As a result, forecast accuracy should improve, especially because error in assessing the current situation is reduced. Not knowing where you are starting from is often a major source of error in predicting future values.

Quantitative analogies

Experts can identify situations that are analogous to a given situation. These can be used to extrapolate the outcome of a target situation. For example, to assess the loss in sales when the patent protection for a drug is removed, one might examine the historical pattern of sales for analogous drugs.

To forecast using quantitative analogies, ask experts to identify situations that are analogous to the target situation and for which data are available. If the analogous data provides information about the future of the target situation, such as per capita ticket sales for a play that is touring from city to city, forecast by calculating averages. If not, construct one model using target situation data and another using analogous data. Combine the parameters of the models, and forecast with the combined model.

While Duncan et al. (2001) provide evidence that accuracy can be improved by using data from analogous time series we found no other evidence on the relative accuracy of quantitative analogies forecasts.

Rule-based forecasting

Rule-based forecasting (RBF) is a type of expert system that allows one to integrate managers' knowledge about the domain with time-series data in a structured and inexpensive way. For example, in many cases a useful guideline is that trends should be extrapolated only when they agree with managers' prior expectations. When the causal forces are contrary to the trend in the historical series, forecast errors tend to be large (Armstrong and Collopy 1993). Although such problems occur only in a small percentage of cases, their effects are serious.

To apply RBF, one must first identify features of the series using statistical analysis, inspection, and domain knowledge (including causal forces). The rules are then used to adjust data, and to estimate short- and long-range models. RBF forecasts are a blend of the short- and long-range model forecasts.

RBF is most useful when substantive domain knowledge is available, patterns are discernable in the series, trends are strong, and forecasts are needed for long horizons. Under such conditions, errors for rule-based forecasts are substantially less than those for combined forecasts (Armstrong, Adya, and Collopy 2001). In cases where the conditions were not met, forecast accuracy is not harmed. Information on rule-based forecasting is available from the special-interest-group pages at forecastingprinciples.com.

Neural nets

Neural networks are computer intensive methods that use decision processes analogous to those of the human brain. Like the brain, they have the capability of learning as patterns change and updating their parameter estimates. However, much data is needed in order to estimate neural network models and to reduce the risk of over-fitting the data (Adya and Collopy 1998).

There is some evidence that neural network models can produce forecasts that are more accurate than those from other methods (Adya and Collopy 1998). While this is encouraging, our current advice is to avoid neural networks because the method ignores prior knowledge and because the results are difficult to understand. Information on neural networks is available from the special interest group pages on the forecastingprinciples.com site. Reviews of commercial software are available from the same site.

Data mining

Data mining uses sophisticated statistical analyses to identify relationships. It is a popular approach. For example, an August 2005 Google search using the term "data mining" found over seven million sites. When we included either "prediction" or "forecasting" in the search, Google found over 560,000 sites.

Data mining ignores theory and prior knowledge in a search for patterns. Despite ambitious claims and much research effort, we are not aware of evidence that data mining techniques provide benefits for forecasting. In their extensive search and reanalysis of data from published research, Keogh and Kasetty (2002) found little evidence for that data mining is useful. A large part of this, they said, was due to the fact that few studies have used a proper design to assess data mining. To find out more about data mining, see the-data-mine.com.

Causal models

Causal models are based on prior knowledge and theory. Time-series regression and cross-sectional regression are commonly used for estimating model parameters or coefficients. These models allow one to examine the effects of marketing activity, such as a change in price, as well as key aspects of the market, thus providing information for contingency planning.

To develop causal models, one needs to select causal variables by using theory and prior knowledge. The key is to identify important variables, the direction of their effects, and any constraints. One should aim for a relatively simple model and use all available data to estimate it (Allen and Fildes 2001). Surprisingly, sophisticated statistical procedures have not led to more accurate forecasts. In fact, crude estimates are often sufficient to provide accurate forecasts when using cross-sectional data (Dawes and Corrigan 1974; Dana and Dawes 2005).

Statisticians have developed sophisticated procedures for analyzing how well models fit historical data. Such procedures have, however, been on little value to forecasters. Measures of fit (such as R^2 or the standard error of the estimate of the model) have little relationship with forecast accuracy and they should therefore be avoided. Instead, holdout data should be used to assess the predictive validity of a model. This conclusion is based on findings from many studies with time-series data (Armstrong, 2001c). Statistical fit does relate to forecast accuracy for cross-sectional data, although the relationship is tenuous.

Causal models are most useful when (1) strong causal relationships are expected, (2) the direction of the relationship is known, (3) causal relationships are known or they can be estimated, (4) large changes are expected to occur in the causal variables over the forecast horizon, and (5) changes in the causal variables can be accurately forecast or controlled, especially with respect to their direction. Reviews of commercial software that can be used to develop causal models are provided at the forecastingprinciples.com site.

Segmentation

Segmentation involves breaking a problem down into independent parts, using data for each part to make a forecast, and then combining the parts. For example, a company could forecast sales of wool carpet separately for each climatic region, and then add the forecasts.

To forecast using segmentation, one must first identify important causal variables that can be used to define the segments, and their priorities. For example, age and proximity to a beach are both likely to influence demand for surfboards, but the latter variable should have the higher priority; therefore, segment by proximity, then age. For each variable, cut-points are determined such that the stronger the relationship with dependent variable, the greater the non-linearity in the relationship, and the more data that are available the more cut-points should be used. Forecasts are made for the population of each segment and the behaviour of the population within the segment using the best method or methods given the information available. Population and behaviour forecasts are combined for each segment and the segment forecasts summed.

Where there is interaction between variables, the effect of variables on demand are non-linear, and the effects of some variables can dominate others, segmentation has advantages over regression analysis (Armstrong 1985). Segmentation is most useful when there are benefits from compensating errors. This is likely to occur where the segments are independent and are of roughly equal importance, and when information on each segment is good.

Segmentation based on *a priori* selection of variables offers the possibility of improved accuracy at a low risk. Dangerfield and Morris (1992), for example, found that bottom-up forecasting, a simple application of segmentation, was more accurate than top-down forecasts for 74% of the 192 monthly time series tested.

In some situations changes in segments are dependent on changes in other segments. For example, liberalisation of gambling laws in city-A might result in decreased gambling revenue in already liberal cities B, C, and D. Efforts at dependent segmentation have gone under the names of microsimulation, world dynamics, and system dynamics. While the simulation approach seems reasonable, the models are complex and hence there are many opportunities for judgemental errors and biases. Armstrong (1985) found no evidence that these simulation approaches provide valid forecasts and we have found no reason to change this assessment.

SELECTING METHODS

To use a new forecasting method, one must at least know about it. The traditional methods of gaining knowledge, such as attending courses, reading textbooks, and using consultants, are being augmented by the Internet. The latest methods can be fully disclosed on web sites and they can be incorporated into software packages. For example, the complete set of rules for rule-based forecasting is available on the forecastingprinciples.com website.

Choosing a method based on evidence

Choosing the best forecasting method for any particular situation is not a simple task, and sometimes more than one method may be appropriate. We used empirical findings and expert opinions to develop the flowchart for selecting methods shown in Figure 3.

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INSERT FIGURE 3: Selection Tree about here
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The first issue the analyst needs to address is whether the data are sufficient to permit quantitative analysis. If not, judgmental procedures are called for. Some cases call for both approaches.

For judgmental procedures, the first issue is whether the situation involves small or large changes. For small changes, where no policy analysis is needed and where one gets good feedback – such as with the number of diners that will come to a restaurant at a given time – unaided judgement can work well. But if the feedback is poor, it helps to use many experts as with Delphi or prediction markets. Where the analyst wishes to predict the effects of different policies, he must determine whether predictions from experts or from participants such as potential customers would be most appropriate. If it is inappropriate to ask potential customers for predictions, judgemental bootstrapping or decomposition will help to use experts' knowledge effectively. Where the conditions are met for conjoint analysis, it may be possible to obtain useful forecasts from surveys of potential customers. For cases where large changes are expected but policy analysis is not required, one should consider expectations or intentions surveys.

Where large changes are expected and only a few decision makers are involved, competitors or suppliers for example, simulated interaction is the best method. If experts are able think of several analogous situations, structured analogies is also likely to provide useful forecasts.

If one has a lot of time-series data, the analyst should determine whether there is knowledge about what empirical relationships might exist, and their magnitudes. For example, in most situations there is excellent prior knowledge about price elasticities (Tellis 1988). If empirical knowledge of relationships is available, use causal models. In addition, one should consider using domain knowledge, such as a manager's knowledge about the situation. Extrapolation or neural networks may be useful in situations where large changes are unlikely.

For time-series situations where one lacks causal knowledge, extrapolation is appropriate. If there is no prior knowledge about relationships, but domain knowledge exists (such as if a manager knows that sales will increase due to advertising of a price reduction), use rule-based forecasting.

In situations where one lacks time-series data and knowledge about relationships, quantitative analogies are appropriate. In the presence of domain knowledge or where policy analysis is needed, expert systems can be used.

The conditions may not always be clear. In such cases, one should use two or more relevant methods, and then combine the forecasts.

Combining forecasts

Combined forecasts improve accuracy and reduce the likelihood of large errors. In a meta-analysis, Armstrong found an average error reduction of about 12% across 30 comparisons. They are especially useful when the component methods differ substantially from one another. For example, Blattberg and Hoch (1990) obtained improved sales forecast by averaging managers' judgmental forecasts and forecasts from a quantitative model. Considerable research suggests that, lacking well-structured domain knowledge, unweighted averages are typically as accurate as other weighting schemes (Armstrong, 2001d).

Judgmental and statistical methods should be integrated. Armstrong and Collopy (1998) summarize research in this area. Integration is effective when judgments are collected in a systematic manner and then used as inputs to the quantitative models, rather than simply used as adjustments to the outputs. Unfortunately, the latter procedure is commonly used.

In the light of the above guidelines, we now examine the needs for the types of marketing forecasts that we identified in Figure 1.

FORECASTING MARKET SIZE

Market size is influenced by environmental factors such as economic conditions. For example, the demand for alcoholic beverages will be influenced by such things as the size and age distribution of the population, distribution of disposable income, publication of health research findings, laws, culture, and religious beliefs. To forecast market size, one can use Delphi, intentions or expectations, extrapolation, causal methods, and segmentation.

Methods that rely on judgment

Market forecasts are often based on judgement, particularly for relatively new or rapidly changing markets. Given the risk of bias from unaided judgement, we recommend using structured methods. For example, the Delphi technique could be used to answer questions about market size such as: 'By what percentage will the wine market grow over the next 10 years?' or 'What proportion of households will subscribe to movies on demand over telephone or cable lines?'

Methods requiring quantitative data

When considering forecasts of market size, one can use either time-series extrapolation methods or causal methods. Time-series extrapolation is inexpensive. Causal methods such as econometrics, while more expensive, are expected to be the most accurate method when large changes are expected.

Organizations should use systematic procedures for scanning the environment to be sure that they do not overlook variables that may have a large impact on their market. Periodic brainstorming with a diverse group of experts should be sufficient to identify which variables to track.

FORECASTING DECISION MAKERS' ACTIONS

The development of a successful marketing strategy sometimes depends upon having good forecasts of the actions and reactions of competitors who might have an influence on market share. For example, if you lower your price, will competitors follow? A variety of judgmental methods can be used to forecast competitive actions. These include:

- expert opinion (ask experts who know about this and similar markets);
- intentions (ask the competitors how they would respond in a variety of situations);
- structured analogies;
- simulated interaction (formal acting out of the interactions among decision makers for the firm and its competitors); and
- experimentation (trying the strategy on a small scale and monitoring the results).

It may also be important to forecast the actions of suppliers, distributors, collaborators, governments, and people within one's firm in order to develop a successful marketing strategy. Sometimes one may need to forecast the actions of other interest groups, such as 'concerned minorities.' For example, how would an environmental group react to the introduction of plastic packaging by a large fast food restaurant chain? Techniques similar to those for forecasting competitors' actions are likely to be useful.

Company plans typically require the cooperation of many people. An organization may decide to implement a given marketing strategy, but will it be able to carry out the plan? Sometimes an organization fails to implement a plan because of a lack of resources, misunderstanding, opposition by key stakeholders, or a lack of commitment by key people. The need to forecast organizational behaviour is sometimes overlooked and can be important. Better forecasting here might lead to more realistic plans and to plans that are easier to implement. Surveys of key decision makers in an organization may help to assess whether a given strategy can be implemented successfully. Simulated interactions can provide useful forecasts in such situations.

It is also important to predict the *effects* of the various actions. One can make such forecasts by using expert judgment, judgmental bootstrapping, or econometric methods.

FORECASTING MARKET SHARE

If one expects the same causal forces and the same types of actions to persist into the future, a simple extrapolation of market share, such as from a naive no-change model, is usually sufficient.

When large changes are expected, one should draw upon methods that incorporate causal reasoning. If the anticipated changes are unusual, judgmental methods such as Delphi would be appropriate. If the changes are expected to be large, the causes are well-understood, and if one lacks historical data, then judgmental bootstrapping can be used to improve forecasting.

The conditions for using econometric models for forecasting market share are described by Brodie et al. (2001). Econometric methods should be used when (1) the effects of current marketing activity are strong relative to the residual effects of previous activity; (2) there are enough data and there is sufficient variability in the data; (3) models can allow for different responses by different brands; (4) models can be estimated at store level; (5) competitors actions can be forecast. Methods for predicting competitors' actions are identified in the previous section.

There are many ways to formulate market share models and much prior research exists to help specify them. For example, a meta-analysis by Tellis (1988) of price elasticities of demand for 367 branded products, estimated using econometric models, reported a mean value of -2.5. Hamilton et al.'s (1997) analysis of 406 brand price elasticities also reported a value of -2.5. Estimates can also be made about other measures of market activity, such as advertising elasticity.

FORECASTING DEMAND DIRECTLY

By direct forecasts, we mean those that focus only on the last box in our Figure 1. We first describe methods that rely on judgment. The most important application here is to new products. Following that we describe methods that can be used when quantitative data are available.

Methods that rely on judgment

The choice of a forecasting method to estimate customer demand for a product depends on what stage it has reached in its life cycle. As a product moves from the concept phase to prototype, test market, introduction, growth, maturation, and declining stages, the relative value of the alternative forecasting methods changes. In general, the movement is from purely judgmental approaches to quantitative models.

Surveys of consumers' intentions and expectations are often used for new product forecasts. Intentions to purchase new products are complicated because potential customers may not be sufficiently familiar with the proposed product and because the various features of the product affect one another (e.g., price, quality and distribution channel). This suggests the need to prepare a good description of the proposed product. A product description may involve prototypes, visual aids, product clinics or laboratory tests. They can also improve forecasts even when you already have other data (Armstrong, Morwitz, & Kumar 2000).

Expert opinions are widely used in the concept phase. For example, it is common to obtain forecasts from the sales force. It is important to properly pose the questions, adjust for biases in experts' forecasts, and aggregate their responses. The Delphi method provides a useful way to conduct such surveys.

Errors in the description can be critical. For example, one of us was asked to forecast demand for the product of a new electricity retailer. As the retailer described the proposed product, an important feature was the ease with which customers would be able to swap their account to the new supplier. All they would have to do was to call the toll-free number and tell the friendly operator their telephone number. Despite our concern that this level of ease might not be achievable we proceeded to forecast demand using the electricity company's description. In the event, the existing supplier refused to transfer accounts without onerous proof, and demand was lower than predicted. This suggests the need to prepare alternative descriptions so as to forecast for possible changes.

Intentions surveys are most likely to be useful for short-term forecasts and business-to-business sales. As an alternative to asking potential customers about their intentions to purchase, one can ask experts to predict how consumers will respond. For example, Wotruba and Thurlow (1976) discuss how opinions from members of the sales force can be used to forecast demand. One could also ask distributors or marketing executives to make forecasts. Experts may be able to make better forecasts if the problem is decomposed in such a way that the parts to be forecast are better known to them than the whole. Thus, if the task was to forecast the sales of high-definition television sets rather than making a direct forecast, one could break the problem into parts such as 'How many households will there be in the U.S. in the forecast year?' 'Of these households, what percentage will make more than $30,000 per year?' 'Of these households, how many have not purchased a large screen TV in the past year?' and so on. The forecasts are obtained by multiplying the components. Unfortunately, experts are often subject to biases when they make forecasts for new products (Tyebjee 1987). Sales people may try to forecast on the low side if their forecasts will be used to set quotas. Marketing executives may forecast high, believing that this will gain approval for the project or motivate the sales force. If possible, you should avoid experts who would have obvious reasons to be biased. Another strategy is to use a heterogeneous group of experts in the hope that their differing biases tend to cancel one another.

Conjoint analysis is widely used by firms (Wittink and Bergestuen, 2001). It was used successfully in the design of a new Marriott hotel chain (Wind et al., 1989). The use of the method to forecast new product demand can be expensive because it requires large samples of potential customers, the potential customers may be difficult to locate, and the questionnaires are not easy for respondents to complete. Respondents must also understand the concepts that they are being asked to evaluate.

Expert judgments can be used in a manner analogous to conjoint analysis. That is, experts would make predictions about situations involving alternative product designs and alternative marketing plans. These predictions would then be related to the situations by regression analysis. It has advantages as compared to conjoint analysis in that few experts are needed (probably between five and twenty). In addition, expert judgments can incorporate policy variables, such as advertising, that are difficult for consumers to assess.

Analogous products can be used to forecast demand for new products. One collects a set of analogous products and examines their growth patterns (Claycamp and Liddy, 1969). The typical pattern can then be used as a forecast.

Large errors are typical for new product forecasts. Tull (1967) estimated the mean absolute percentage error for new product sales to be about 65 percent. It is not surprising then, that pre-test models have gained wide acceptance among business firms. Shocker and Hall (1986) provided an evaluation of some of these models Because of the lack of systematic and unbiased forecast validation studies they could draw no conclusions about which methods were most accurate.

Methods requiring quantitative data

Once a new product is on the market, it is possible to use extrapolation methods. For early sales, much attention has been given to the selection of the proper functional form. The diffusion literature uses an S-shaped curve to predict new product sales. That is, growth builds up slowly at first, becomes rapid if word of mouth is good and if people see the product being used by others. Then it slows as it approaches a saturation level. A substantial literature exists on diffusion models. Despite this, the number of comparative validation studies is small and the benefits of choosing the best functional form are modest (Meade and Islam, 2001).

When many demand forecasts are needed, extrapolation is often preferred. Relatively simple methods suffice. Sophistication beyond a modest level does not improve accuracy, but it does increase costs and reduce understanding. Decomposition is appropriate when component series can be forecast more accurately than the aggregate.

UNCERTAINTY

In addition to improving accuracy, forecasting is concerned with assessing uncertainty. This can help manage the risk associated with alternative plans.

Traditional error measures, such as the mean square error (MSE), do not provide a reliable basis for comparison of forecasting methods (Armstrong and Collopy, 1992). The median absolute percentage error (MdAPE) is more appropriate because it is invariant to scale and is not influenced by outliers. When comparing methods, especially when testing on a small number of series, control for degree of difficulty in forecasting by using the median relative absolute error (MdRAE), which compares the error for a given model against errors for the naive, no change forecast (Armstrong and Collopy, 1992).

Statisticians have relied heavily on tests of statistical significance for assessing uncertainty. However, statistical significance is inappropriate for assessing uncertainty in forecasting. Furthermore, its use has been attacked as being misleading (e.g., see Cohen, 1994). It is difficult to find studies in marketing forecasting where statistical significance has made an important contribution.

Instead of statistical significance, the focus should be on prediction intervals. Chatfield (2001) summarizes research on prediction intervals. Unfortunately, prediction intervals are not widely used in practice. Tull’s (1967) survey noted that only 25% of 16 respondent companies said they provided confidence intervals with their forecasts. Dalrymple (1987) found that 48% did not use confidence intervals, and only 10% ‘usually’ used them.

The fit of a model to historical data is a poor way to estimate prediction intervals. It typically results in confidence intervals that are too narrow. It is best to simulate the actual forecasting procedure as closely as possible, and use the distribution of the resulting *ex ante* forecasts to assess uncertainty. For example, if you need to make forecasts for two years ahead, withhold enough data to be able to have a number of two-year-ahead *ex ante* forecasts.

Uncertainty in judgmental forecasts

Experts are typically overconfident (Arkes, 2001). In McNee’s (1992) examination of economic forecasts from 22 economists over 11 years, the actual values fell outside the range of their prediction intervals about 43% of the time. This occurs even when subjects are warned in advance against overconfidence. Fortunately, there are procedures to improve the calibration of judges. Where possible, judges should be provided with timely and unambiguous information on outcomes along with reasons why they were right or wrong. When feedback is good, judges’ confidence intervals are well-calibrated. For example, 60% of the times weather forecasters say that there is a 60% chance of rain, it rains. This suggests that marketing forecasters would do well to seek the standard of feedback received by weather forecasters.

In cases where good feedback is not possible, ask experts to write all the reasons why their forecasts might be wrong (Arkes, 2001). Alternatively, use the devil’s advocate procedure, where someone is assigned for a short time to raise arguments about why the forecast might be wrong. But, be warned, being a devil’s advocate can be make you unpopular with your group.

Still another way to assess uncertainty is to examine the agreement among judgmental forecasts. For example, Ashton (1985), in a study of forecasts of annual advertising sales for *Time* magazine, found that the agreement among the individual judgmental forecasts was a good proxy for uncertainty.

Uncertainty in quantitative forecasts

Prediction intervals from quantitative forecasts tend to be too narrow even when based on *ex ante* n-ahead forecasts. Some empirical studies have shown that the percentage of actual values that fall outside the 95% prediction intervals is substantially greater than 5%, and sometimes greater than 50% (Makridakis et al., 1987). One reason this occurs is because the estimates ignore various sources of uncertainty. For example, discontinuities might occur over the forecast horizon. In addition, forecast errors in time series are often asymmetric, so this makes it difficult to estimate prediction intervals. Asymmetry of errors is likely to occur when the forecasting model uses an additive trend. The most sensible procedure is to transform the forecast and actual values to logs, then calculate the prediction intervals using logged differences. Interestingly, researchers and practitioners seldom follow this advice (except where the original forecasting model has been formulated in logs). Evidence on the issue of asymmetrical errors is provided in Armstrong and Collopy (2001).

Loss functions can also be asymmetric. For example, the cost of a forecast that is too low by 50 units may differ from the cost if it is too high by 50 units. But this is a problem for the planner, not the forecaster.

GAINING ACCEPTANCE OF FORECASTS

Forecasts that contradict management’s expectations have much potential value. However, they may be ignored (Griffith and Wellman, 1979). One way to avoid this problem is to gain agreement on what forecasting procedures to use prior to presenting the forecasts. This may involve making adjustments to the forecasting method in order to develop forecasts that will be used.

Another way to gain acceptance of forecasts is to ask decision makers to decide in advance what decisions they will make given different possible forecasts. Are the decisions affected by the forecasts?

Prior agreements on process and on decisions can greatly enhance the value of forecasts, but they are difficult to achieve in many organizations. The use of scenarios can aid this process. Scenarios involve providing information about a future situation to a decision maker and asking him to project himself into the situation and write the stories about what he did. They should be written in the past tense. Detailed instructions for writing scenarios are summarized in Gregory and Duran (2001). Scenarios are effective in getting managers to accept the possibility that certain events might occur. They should not be used to make forecasts, however, because they distort one’s assessment of the likelihood that the events will occur.

CONCLUSIONS

Significant gains have been made in forecasting for marketing, especially since 1960. Advances have occurred in the development of methods based on judgment, such as Delphi, simulated interactions, intentions studies, opinions surveys, bootstrapping, and combining. They have also occurred for methods based on statistical data, such as extrapolation, rule-based forecasting, and econometric methods. Most recently, gains have come from the integration of statistical and judgmental forecasts.

General principles

- Managers' domain knowledge should be incorporated into forecasting methods.
- When making forecasts in highly uncertain situations, be conservative. For example, the trend should be dampened over the forecast horizon.
- Complex methods have not proven to be more accurate than relatively simple methods. Given their added cost and the reduced understanding among users, highly complex procedures cannot be justified.
- When possible, forecasting methods should use data on actual behaviour, rather than judgments or intentions, to predict behaviour.
- Methods that integrate judgmental and statistical data and procedures (e.g., rule-based forecasting) can improve forecast accuracy in many situations.
- Overconfidence occurs with quantitative and judgmental methods.
- When making forecasts in situations with high uncertainty, use more than one method and combine the forecasts, generally using simple averages.

Methods based on judgment

- When using judgment, rely on structured procedures such as Delphi, simulated interaction, structured analogies, and conjoint analysis.
- Simulated interaction is useful to predict the decisions in conflict situations, such as in negotiations.
- In addition to seeking good feedback, forecasters should explicitly list all the things that might be wrong about their forecast. This will produce better calibrated prediction intervals.

Methods based on statistical data

- With the proliferation of data, causal models play an increasingly important role in forecasting market size, market share, and sales.
- Methods should be developed primarily on the basis of theory, not data.

Finally, efforts should be made to ensure forecasts are free of political considerations in a firm. To help with this, emphasis should be on gaining agreement about the forecasting methods. Also, for important forecasts, decisions on their use should be made before the forecasts are provided. Scenarios are helpful in guiding this process.

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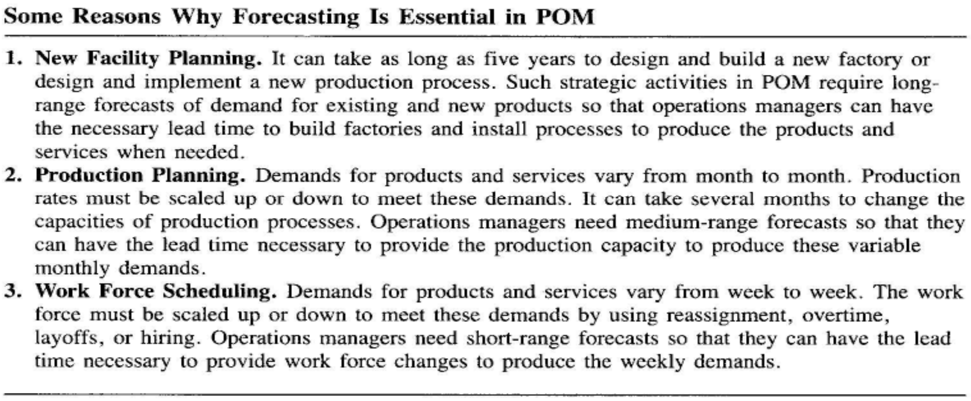
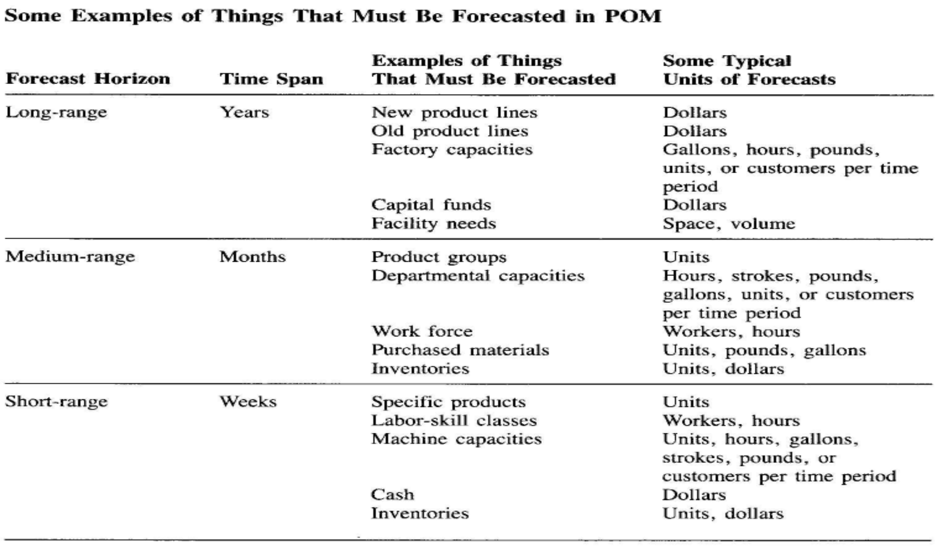
Demand Forecasting

- When a product is produced for a market, the demand occurs in the future.
- The production planning cannot be accomplished unless the volume of the demand known.
- The success of the business in supplying the demand in the most efficient & profitable way will then depend on the accuracy of the forecasting process in predicting the future demand.



Some Reasons Why Forecasting Is Essential in POM

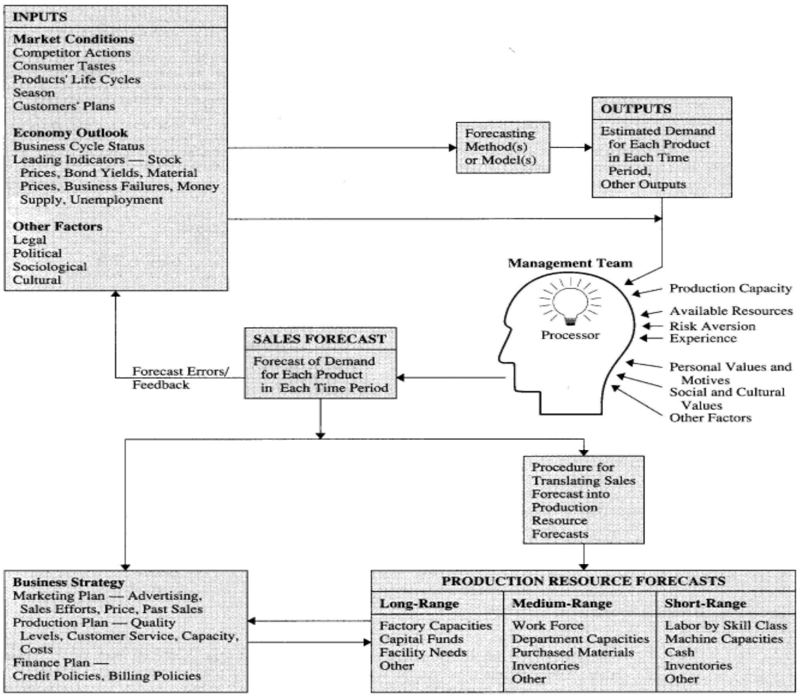
1. **New Facility Planning.** It can take as long as five years to design and build a new factory or design and implement a new production process. Such strategic activities in POM require long-range forecasts of demand for existing and new products so that operations managers can have the necessary lead time to build factories and install processes to produce the products and services when needed.
2. **Production Planning.** Demands for products and services vary from month to month. Production rates must be scaled up or down to meet these demands. It can take several months to change the capacities of production processes. Operations managers need medium-range forecasts so that they can have the lead time necessary to provide the production capacity to produce these variable monthly demands.
3. **Work Force Scheduling.** Demands for products and services vary from week to week. The work force must be scaled up or down to meet these demands by using reassignment, overtime, layoffs, or hiring. Operations managers need short-range forecasts so that they can have the lead time necessary to provide work force changes to produce the weekly demands.

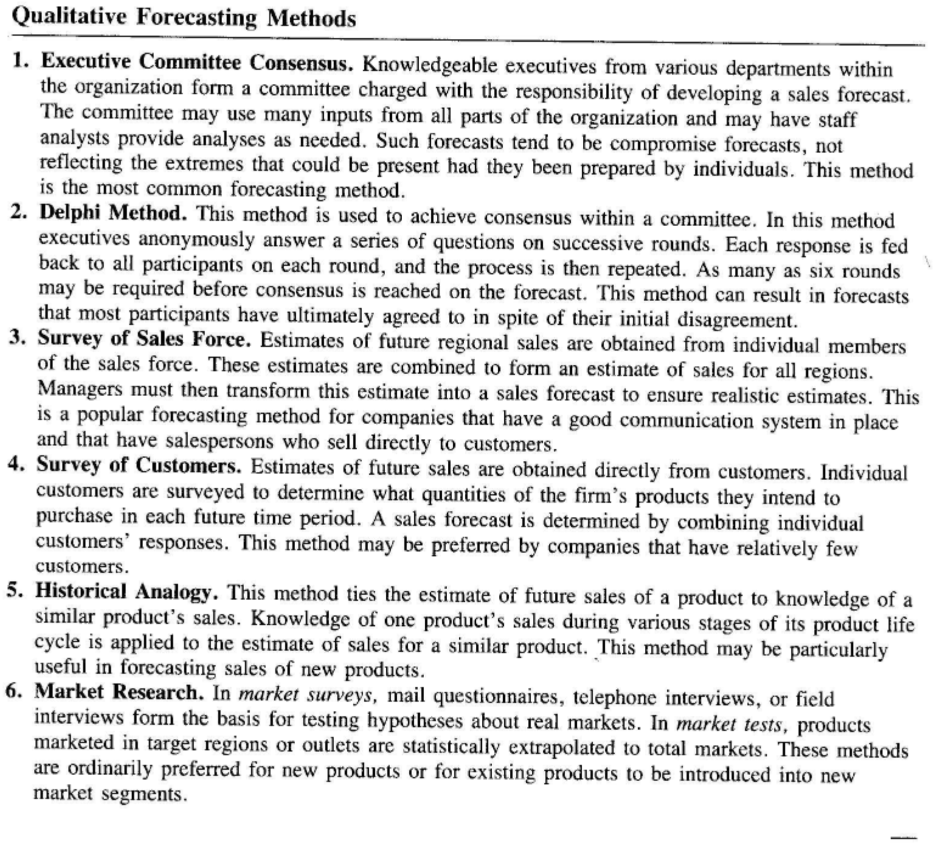


Some Examples of Things That Must Be Forecasted in POM

Forecast Horizon	Time Span	Examples of Things That Must Be Forecasted	Some Typical Units of Forecasts
Long-range	Years	New product lines	Dollars
		Old product lines	Dollars
		Factory capacities	Gallons, hours, pounds, units, or customers per time period
		Capital funds	Dollars
		Facility needs	Space, volume
Medium-range	Months	Product groups	Units
		Departmental capacities	Hours, strokes, pounds, gallons, units, or customers per time period
		Work force	Workers, hours
		Purchased materials	Units, pounds, gallons
		Inventories	Units, dollars
Short-range	Weeks	Specific products	Units
		Labor-skill classes	Workers, hours
		Machine capacities	Units, hours, gallons, strokes, pounds, or customers per time period
		Cash	Dollars
		Inventories	Units, dollars

1 **Forecasting as an Integral Part of Business Planning**


INPUTS
Market Conditions
Competitor Actions
Consumer Tastes
Products' Life Cycles
Season
Customers' Plans
Economy Outlook
Business Cycle Status
Leading Indicators — Stock Prices, Bond Yields, Material Prices, Business Failures, Money Supply, Unemployment
Other Factors
Legal
Political
Sociological
Cultural
Forecasting Method(s) or Model(s)
OUTPUTS
Estimated Demand for Each Product in Each Time Period,
Other Outputs
Management Team
Processor
Production Capacity
Available Resources
Risk Aversion
Experience
Personal Values and Motives
Social and Cultural Values
Other Factors
SALES FORECAST
Forecast of Demand for Each Product in Each Time Period
Forecast Errors/ Feedback
Procedure for Translating Sales Forecast into Production Resource Forecasts
Business Strategy
Marketing Plan — Advertising, Sales Efforts, Price, Past Sales
Production Plan — Quality Levels, Customer Service, Capacity, Costs
Finance Plan —
Credit Policies, Billing Policies
PRODUCTION RESOURCE FORECASTS
Long-Range
Factory Capacities
Capital Funds
Facility Needs
Other
Medium-Range
Work Force
Department Capacities
Purchased Materials
Inventories
Other
Short-Range
Labor by Skill Class
Machine Capacities
Cash
Inventories
Other



Qualitative Forecasting Methods

1. **Executive Committee Consensus.** Knowledgeable executives from various departments within the organization form a committee charged with the responsibility of developing a sales forecast. The committee may use many inputs from all parts of the organization and may have staff analysts provide analyses as needed. Such forecasts tend to be compromise forecasts, not reflecting the extremes that could be present had they been prepared by individuals. This method is the most common forecasting method.
2. **Delphi Method.** This method is used to achieve consensus within a committee. In this method executives anonymously answer a series of questions on successive rounds. Each response is fed back to all participants on each round, and the process is then repeated. As many as six rounds may be required before consensus is reached on the forecast. This method can result in forecasts that most participants have ultimately agreed to in spite of their initial disagreement.
3. **Survey of Sales Force.** Estimates of future regional sales are obtained from individual members of the sales force. These estimates are combined to form an estimate of sales for all regions. Managers must then transform this estimate into a sales forecast to ensure realistic estimates. This is a popular forecasting method for companies that have a good communication system in place and that have salespersons who sell directly to customers.
4. **Survey of Customers.** Estimates of future sales are obtained directly from customers. Individual customers are surveyed to determine what quantities of the firm's products they intend to purchase in each future time period. A sales forecast is determined by combining individual customers' responses. This method may be preferred by companies that have relatively few customers.
5. **Historical Analogy.** This method ties the estimate of future sales of a product to knowledge of a similar product's sales. Knowledge of one product's sales during various stages of its product life cycle is applied to the estimate of sales for a similar product. This method may be particularly useful in forecasting sales of new products.
6. **Market Research.** In *market surveys,* mail questionnaires, telephone interviews, or field interviews form the basis for testing hypotheses about real markets. In *market tests,* products marketed in target regions or outlets are statistically extrapolated to total markets. These methods are ordinarily preferred for new products or for existing products to be introduced into new market segments.

Technique for Demand Forecasting

1. Naïve techniques - adding a certain percentage to the demand for next year.
2. Opinion sampling - collecting opinions from sales, customers etc.
3. Qualitative methods
4. Quantitative methods - based on statistical and mathematical concepts.
   a. Time series - the variable to be forecast has behaved according to a specific pattern in the past and that this pattern will continue in the future.
   b. Causal - there is a causal relationship between the variable to be forecast and another variable or a series of variables.

Quantitative Methods of Forecasting

1. Causal – There is a causal relationship between the variable to be forecast and another variable or a series of variables. (Demand is based on the policy, e.g. cement, and build material.
2. Time series – The variable to be forecast has behaved according to a specific pattern in the past and that this pattern will continue in the future.

Causal:

Demand for next period

= ***f*** (number *of permits, number of loan application....*)

Time series:

1. $\boldsymbol{D} = \boldsymbol{F}\ (t)$

Where *D* is the variable to be forecast and *f*(*t*) is a function whose exact form can be estimated from the past data available on the variable.

2. The value of the variable for the future as a function of its values in the past.

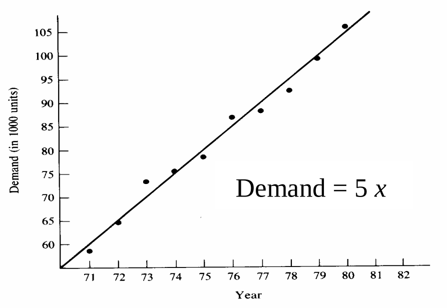
$D_{t+1} = f\ (D_t, D_{t-1}, D_{t-2}, ...)$

- There exists a function whose form must be estimated using the available data..
- The most common technique for estimation of equation is regression analysis.

Regression Analysis: is not limited to locating the straight line of best fit.

Example A: Following data on the demand for sewing machines manufactured by Taylor and Son Co. have been compiled for the past 10 years.

year	1971	1972	1973	1974	1975	1976	1977	1978	1979	1980
Demand in (1000 units)	58	65	73	76	78	87	88	93	99	106



1. *Single variable linear regression*

Year = x where x = 1, 2, 3,...., 10

Demand = y

D = $y + \varepsilon$ Where D is actual demand

$\varepsilon = D - y$

To find out whether this is the line of best fitted to be sure that this sum of squares is a min.

Determination of the regression line

In general form

$y = a + bx$

Where y is dependent variable, and x is independent data variable.

When a and b specified this line will be specified.

$\varepsilon_1 = y_1 - y(x_1) = y_1 - a - bx_1$

$\varepsilon_2 = y_2 - y(x_2) = y_2 - a - bx_2$

.

$\varepsilon_n = y_n - y(x_n) = y_n - a - bx_n$

The sum of square of error (SSE)

SSE = $\sum\varepsilon^2 = \varepsilon_1^2 + \varepsilon_2^2 + \ldots \quad + \varepsilon_n^2$

$= (y_1 - a - bx_1)^2 + \ldots. + (y_n - a - bx_n)^2$

To minimize SSE, its partial derivatives with respect to a and b may be equated to zero and solve a and b

$$\frac{\partial SSE}{\partial a} = -2(y_1 - a - bx_1) - 2(y_2 - a - bx_2) \cdots - 2(y_n - a - bx_n) = 0$$

$$\frac{\partial SSE}{\partial b} = -2x_1(y_1 - a - bx_1) - 2x_2(y_2 - a - bx_2) \cdots - 2x_n(y_2 - a - bx_n) = 0$$

or

$$-2(y_1 + y_2 \cdots y_n) + 2(a + a + \cdots a) + 2b(x_1 + x_2 \cdot \cdot\cdot x_n) = 0$$

and

$$-2(x_1y_1 + x_2y_2 + \cdots x_ny_n) + 2a(x_1 + x_2 + \cdots x_n) + 2b(x_1^2 + x_2^2 + \cdots x_n^2) = 0$$

$$a = \frac{\Sigma x^2 \Sigma y - \Sigma x \Sigma xy}{n\Sigma x^2 - (\Sigma x)^2} \qquad b = \frac{n\Sigma xy - \Sigma x \Sigma y}{n\Sigma x^2 - (\Sigma x)^2}$$

$$b = \frac{n\Sigma xy - \Sigma x \Sigma y}{n\Sigma x^2 - (\Sigma x)^2}$$

or

$$b = \frac{n\Sigma xy - \Sigma x \Sigma y}{n\Sigma x^2 - (\Sigma x)^2} \qquad a = \frac{\Sigma y - b\Sigma x}{n}$$

Coefficient of correlation

$$r = \frac{n\Sigma xy - \Sigma x \Sigma y}{\sqrt{[n\Sigma x^2 - (\Sigma x)^2][n\Sigma y^2 - (\Sigma y)^2]}}$$

Where $-1 \le r \le 1$

*Perfect interdependence between variables when ± 1

2. *Exponential*: sometimes a smooth curve provides a better fit for data points than does a straight line $y = ab^x$ indicates that y changes in each period at the constant rate b.

Determine the value for a and b by the least squares method:

$\log y = \log a + x \log b$

The logarithmic version plots as a straight line on semi-logarithmic paper: the Y scale is logarithmic and the X scale arithmetic.

$$\sum(\log Y) = N(\log a) + \sum X(\log b)$$

$$\sum(X \log Y) = \sum X(\log a) + \sum X^2(\log b)$$

$$\log a = \frac{\sum(\log Y)}{N}$$

and

$$\log b = \frac{\sum(X \log Y)}{\sum X^2}$$

- If the curved line from the exponential equation does not represent the data adequately, forecasting equation can be based on algebraic series such as,
  $Y = a + b_1X + b_2X^2 + \ldots + b_nX^n$
- Or trigonometric functions such as
  $Y = a + b_1 \sin(2\pi X/b_2) + b_3 \cos(2\pi X/b_4)$

3. *Regression time series forecasting*

Demand = Trend + Error

The error part is decomposed to

(a). Seasonal

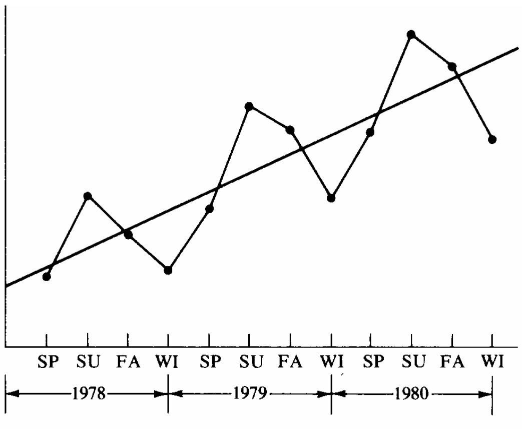
(b). Cyclical – Similar to seasonal variations except for the fact that the cycle has long period.

(c). Random variations – do not follow any pattern that cannot control or accounted.

Seasonal

Regression time series forecasting without seasonal variation (Same as we had discussed)

Regression time series forecasting with seasonal variation



Example:

- Demand for sporting goods for sports, golf, swimming
- Different types of clothing, food, and heating and cooling systems

Example B: The demand for a certain soft drink in the past four years in given in following on a quarterly basis.

Year	Period	Demand (in Million)	Year	Period	Demand (in Million)
1	Spring	15	3	Spring	20
	Summer	25		Summer	30
	Fall	16		Fall	18
	Winter	8		Winter	11
2	Spring	17	4	Spring	18
	Summer	29		Summer	32
	Fall	14		Fall	19
	Winter	10		Winter	12

$$b = \frac{n\Sigma xy - \Sigma x\Sigma y}{n\Sigma x^2 - (\Sigma x)^2} = \frac{16(2,551) - (136)(294)}{16(1,496) - (136)^2} = 0.153$$

$$a = \frac{\Sigma y - b\Sigma x}{n} = \frac{294 - 0.153(136)}{16} = 17.075$$

$$r = \frac{n\Sigma xy - x\Sigma y}{\sqrt{[n\Sigma x^2 - (\Sigma x)^2][n\Sigma y^2 - (\Sigma y)^2]}}$$

$$= \frac{16(2551) - (136)(294)}{\sqrt{[16(1496) - (136)^2][16(6194) - (294)^2]}}$$

$$r = 0.1002$$

r very small almost indicating that no relation. We may be able to use the trend line by adjusting its forecast value such that it is acceptable.

Seasonal adjustment

i. Additive model: Adjustment is made by adding or deducting a specific amount from the value obtained from the trend line to determine the forecast for the respective season. This is very depended on experiences.

ii. Multiplicative model: This is made by multiplying the value estimated by the trend by a factor of either more or less than one to forecast the demand for the season.

$\tilde{A}_j = SF_j \bullet D$

Where, $\tilde{A}_j$: the adjusted forecast for the season j

And SF_j: the seasonal factor

Example C: Use the example from B finds the seasonal factor.

Take summer as example

For year 1, $t = 2$,

Actual value = 25,

The value of trend line D = 17.075 + 0.153 (t) = 17.381

The seasonal factor = $(SF_2)_1$ = 25/17.381 = 1.438

For year 2, $t = 6$,

Actual value = 29,

The value of trend line D = 17.075 + 0.153 (t) = 17.993

The seasonal factor = $(SF_2)_2$ = 25/17.993 = 1.612

For year 3, t = 10,
Actual value = 30,
The value of trend line D = 17.075 + 0.153 (t) = 18.605
The seasonal factor = $(SF_2)_3$ = 25/18.605 = 1.612

For year 4, t = 14,
Actual value = 32,
The value of trend line D = 17.075 + 0.153 (t) = 19.217
The seasonal factor = $(SF_2)_4$ = 25/19.217 = 1.665

Average these four values yield the seasonal adjustment factor for the summer season of any year.

$SF_2 = [(SF_2)_1 + (SF_2)_2 + (SF_2)_3 + (SF_2)_4]/4 = 1.582$

Now to find the forecast for the summer of year 5, i.e. t = 18

$$D = 17.075 + 0.153\,(t) = 19.829$$

$$\tilde{A}_j = SF_j \bullet D = 1.582 \bullet 19.829 = 31.369$$

With the same techniques we may find

Spring	$SF_2 = 0.963$
Fall	$SF_2 = 0.906$
Winter	$SF_2 = 0.549$

Forecasting by Time Series Analysis(short-range forecast) - Without using regression analysis

These models are especially helpful when there is no clear upward or downward pattern in the past data to suggest a kind of linear relationship between the demand and time.
In general

$$D_{t+1} = F\,(D_t, D_{t-1}, ..., D_2, D_1)$$

Where D_{t+1} is forecast demand for the next period

(a). Simple moving average forecasting
(b). Exponential smoothing

Simple moving average forecasting

- All past data are given equal weight in estimating.

$D_{t+1} = 1/k \bullet (D_t, + D_{t-1} + ...+ D_2 + D_1)$

Example C. Simple Moving Average Forecasting

The demand for the past 12 years of certain type of automobile alternator is given below

year	*Demand*	*year*	*Demand*
	(in 10,000 units)		*(in 10,000 units)*
69	32	75	40
70	40	76	25
71	50	77	52
72	28	78	48
73	30	79	40
74	44	80	44

A. Three period moving average forecast for the demand

$$D_{t+1} = \mathit{1/3} \bullet (D_t, + D_{t-1} + D_{t-2})$$

B. Five period moving average is given by

$$D_{t+1} = \mathit{1/5} \bullet((D_t, + D_{t-1} + D_{t-2} + D_{t-3} + D_{t-4})$$

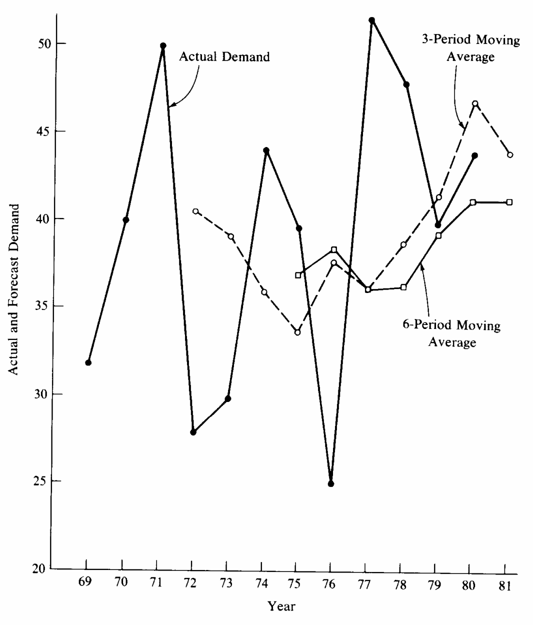
For example:

$$D_{81} = \mathit{1/3} \bullet (D_{80}, + D_{79} + D_{78}) = 44$$

$$D_{81} = \mathit{1/5} \bullet (D_{80}, + D_{79} + D_{78} + D_{77} + D_{76}) = 41.8$$

Results of Applying the Simple Moving Average Forecasting

Year	Demand	3-period	6-period
69	32		
70	40		
71	50		
72	28	40.7	
73	30	39.3	
74	44	36.0	
75	40	34.0	37.3
76	25	38.0	38.7
77	52	36.3	36.2
78	48	39.0	36.5
79	40	41.7	39.8
80	44	46.0	41.5
1981 Forecasting		44	41.5



Conclusions:

1. A large number for k is suitable for data that fluctuate very much.
2. Small values of k are better for data which follow a pattern with less fluctuations.
3. *k* = n is the most extreme case, in such a case the curve representing the forecast would approximate a horizontal line.
4. If the past data suggest an increasing or decreasing pattern the most recent data provide better estimates of the future values. Thus small k is suggested.

Weighted Moving Average Method

- In some situations, it may be desirable to apply unequal weights to the historical data

	Actual	Weight
72	28	.20
73	30	.30
74	44	.50

Modification of Forecast$_{75}$=36.6

Exponential smoothing

- Exponential smoothing is assumed that the future demand is the same as the forecast made for the present period plus a percentage of the forecasting error made in the past period.

$$F_{t+1} = F_t + \alpha (D_t - F_t)$$

Where α is smoothing factor

Example D. Exponential Smoothing

A new product demand for January and February of this year has been 40,000 and 48,000 respectively. New product has no additional information. Forecast the demand for March with α = 0.4.

Solution:

$$F_M = F_F + \alpha (D_F - F_F)$$

$$F_F = F_J + \alpha (D_J - F_J)$$

F_J is unknown, since no additional information is available, we assume

$$F_J = D_J = 40{,}000 \quad \text{and} \quad F_F = F_J = 40{,}000$$

$$\Rightarrow \quad F_M = 4{,}000 + 0.4\ (48{,}000 - 40{,}000) = 43{,}200$$

- More detail about exponential smoothing (if we know more past).

$$F_{t+1} = F_t + \alpha (D_t - F_t)$$

Expand the equation

$$F_{t+1} = \alpha\ D_t + (1- \alpha)\ F_t$$

Substitute F_t with F_{t+1}

$$F_{t+1} = \alpha\ D_{t-1} + (1- \alpha)\ F_{t-1}$$

$$\Rightarrow \quad F_{t+1} = \alpha\ D_t + \alpha\ (1- \alpha)\ D_{t-1} + (1- \alpha)^2\ F_{t-1}$$

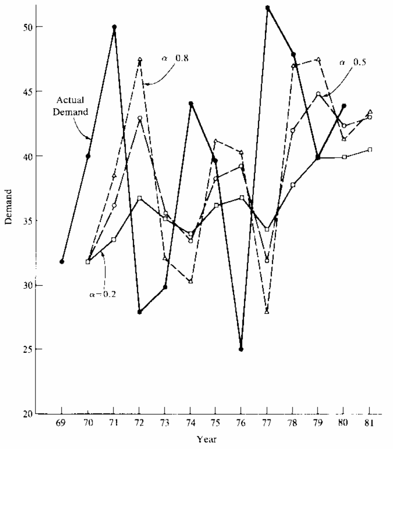
With the same procedure on F_{t-1} and F_{t-2}

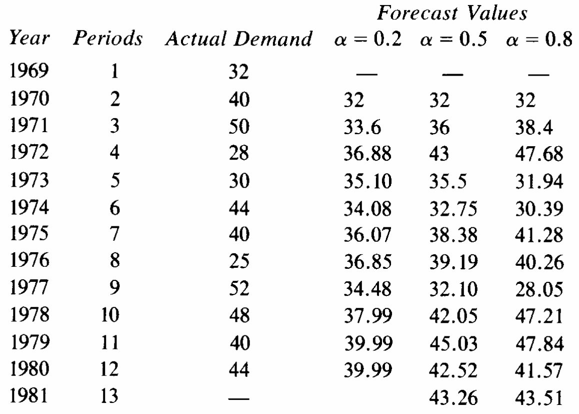
The general form can be written as

$$F_{t+1} = \alpha\ D_t + \alpha\ (1- \alpha)\ D_{t-1} + \alpha\ (1- \alpha)^2\ D_{t-2} + \ldots.+ \alpha\ (1- \alpha)^{t-1}\ D_1 + (1- \alpha)^t\ F_1$$

The effect of α analysis

Example E. let's applied exponential smoothing to previous example C. To study the effect of α, α = 0.2, 0.5, and 0.8





			Forecast Values		
Year	*Periods*	*Actual Demand*	$\alpha = 0.2$	$\alpha = 0.5$	$\alpha = 0.8$
1969	1	32	—	—	—
1970	2	40	32	32	32
1971	3	50	33.6	36	38.4
1972	4	28	36.88	43	47.68
1973	5	30	35.10	35.5	31.94
1974	6	44	34.08	32.75	30.39
1975	7	40	36.07	38.38	41.28
1976	8	25	36.85	39.19	40.26
1977	9	52	34.48	32.10	28.05
1978	10	48	37.99	42.05	47.21
1979	11	40	39.99	45.03	47.84
1980	12	44	39.99	42.52	41.57
1981	13	—		43.26	43.51

1. From the graphic with 0.2 is the smoothest of the three, indicating that the smaller values of α have more smoothing effect.
2. The pattern of variations in the forecast in very similar to that of the actual demand except that the forecast curve lags the actual curve by a number of periods.
3. As the smoothing effect is increased (α decreased) this similarity becomes less visible.
4. The small value of α is suitable for data that behave very randomly.
5. The large value of α is suggest for data with less fluctuation and with a recognizable pattern.

$\mathbf{F_{t+1} = F_t + \alpha\,(D_t - F_t)}$

$\alpha \approx 0$ →Future forecast in very closed to present forecast (Similar to moving average with *k* large)

$\alpha \approx 1$ Present forecast much be adjusted a great deal to yield future forecast (similar to moving average with *k* small)

Moving average and exponential smoothing

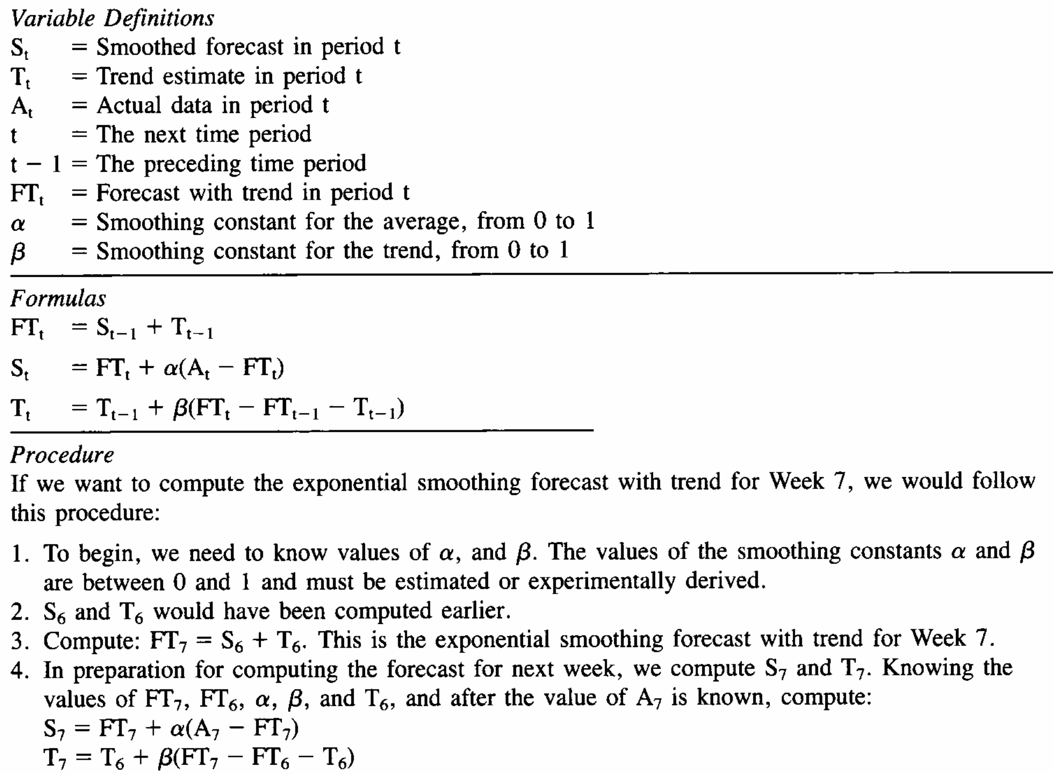
- An earlier term for exponential smoothing was exponentially weighted moving average. This term reminds us the exponential smoothing, like the moving average and the weighted moving average models, develops forecasts that are averages.
- Exponential smoothing weights data from recent periods heavier than data from more distant periods
- Moving average and exponential smoothing are similar in this regard. The number of period (AP) and a are related by the following expression:

$$\alpha = \frac{2}{AP + 1}$$

Exponential Smoothing with Trend

- As we move from short-range forecasts toward medium-range forecasts, however, seasonality and trend become more important.
- Incorporating a trend component into exponentially smoothed forecasts is called double exponential smoothing, because the estimate for the average and the estimate for the trend are both smoothed.
- Both a, the smoothing constant for the average, and b, the smoothing constant for the trend, are used in this model.

Formulas, variable definitions, and procedure for exponential smoothing forecasts with trend



Variable Definitions

S_t = Smoothed forecast in period t
T_t = Trend estimate in period t
A_t = Actual data in period t
t = The next time period
t − 1 = The preceding time period
FT_t = Forecast with trend in period t
α = Smoothing constant for the average, from 0 to 1
β = Smoothing constant for the trend, from 0 to 1

Formulas

$FT_t = S_{t-1} + T_{t-1}$

$S_t = FT_t + \alpha(A_t - FT_t)$

$T_t = T_{t-1} + \beta(FT_t - FT_{t-1} - T_{t-1})$

Procedure

If we want to compute the exponential smoothing forecast with trend for Week 7, we would follow this procedure:

1. To begin, we need to know values of α, and β. The values of the smoothing constants α and β are between 0 and 1 and must be estimated or experimentally derived.
2. S_6 and T_6 would have been computed earlier.
3. Compute: $FT_7 = S_6 + T_6$. This is the exponential smoothing forecast with trend for Week 7.
4. In preparation for computing the forecast for next week, we compute S_7 and T_7. Knowing the values of FT_7, FT_6, α, β, and T_6, and after the value of A_7 is known, compute:
   $S_7 = FT_7 + \alpha(A_7 - FT_7)$
   $T_7 = T_6 + \beta(FT_7 - FT_6 - T_6)$

Why Causal Forecasting

- There is no logical link between the demand in the future and what has happened in the past. – statistic
- There are other factors which can be logically linked to the demand

Example 1: There is a strong cause and effect relationship between future demand for doors and windows and the number of construction permits issued at present.

Example 2: The demand for new house or automobile is very much affected by the interest rates changed by banks.

Economic indicators

General form for one: Simple linear regression in causal forecasting

$$F_{t+1} = f\,(x)_t$$

- This indicates the future demand is a function of the value of the economic indicator at the present time.

Where F_{t+1}: the forecast for the next period

And x is the relevant economic indicator

$$F = a + bx$$

More than one economic indicators: multiple regression analysis in causal forecasting

$$F_{t+1} = f\,(x_1, x_2, x_3, \ldots\ldots., x_n)_t$$

$$F = a + b_1x_1 + b_2x_2 + b_3x_3 + \ldots\ldots + b_nx_n$$

Multiple regression analysis in causal forecasting

- Sometimes one economic indicator alone does not show a very strong relationship. One way consider the use of combination of economic indicators as a means of forecasting.
- Another way stating as a function of several economic indicators.

$$F = a + b_1x_1 + b_2x_2 + b_3x_3 + \ldots\ldots + b_nx_n$$

- The Determination of these parameters a, b_1, b_2, b_3, ... b_n may use SPSS (Statistical Programs For Social Scientists) or IMSL (International Mathematical and Statistical Library) by computer input the past data.

Example of two economic indicators involved.

$$y = a + b_1x_1 + b_2x_2$$

Using the criterion of the least squared error

$$\begin{aligned}
\Sigma y &= na + b_1\Sigma x_1 + b_2\Sigma x_2 \\
\Sigma x_1y &= a\Sigma x_1 + b_1\Sigma x_1^2 + b_2\Sigma x_1x_2 \\
\Sigma x_2y &= a\Sigma x_2 + b_1\Sigma x_1x_2 + b_2\Sigma x_2^2
\end{aligned}$$

$$R = \sqrt{\frac{r_{01}^2 + r_{02}^2 - 2r_{01}r_{02}r_{12}}{1 - r_{12}^2}}$$

Where

$$r_{01} = \frac{n\Sigma x_1y - \Sigma x_1\Sigma y}{\sqrt{[n\Sigma x_1^2 - (\Sigma x_1)^2][n\Sigma y^2 - (\Sigma y)^2]}}$$

$$r_{02} = \frac{n\Sigma x_2y - \Sigma x_2\Sigma y}{\sqrt{[n\Sigma x_2^2 - (\Sigma x_2)^2][n\Sigma y^2 - (\Sigma y)^2]}}$$

$$r_{12} = \frac{n\Sigma x_1x_2 - \Sigma x_1\Sigma x_2}{\sqrt{[n\Sigma x_1^2 - (\Sigma x_1)^2][n\Sigma x_2^2 - (\Sigma x_2)^2]}}$$

Market Share

- Since most of the time the producer is not the sole supplier of the product to the market.

a. The market share has remained fairly constant.

$$D = MS \bullet D_{total}$$

$$MS = \sum(MS)_i / n$$

Year	Total D	Amount Sold by A	Market Share
1	125	43	0.344
2	140	47	0.336
3	160	54	0.338
4	130	44	0.338
5	200	68	0.340
6	175	60	0.343

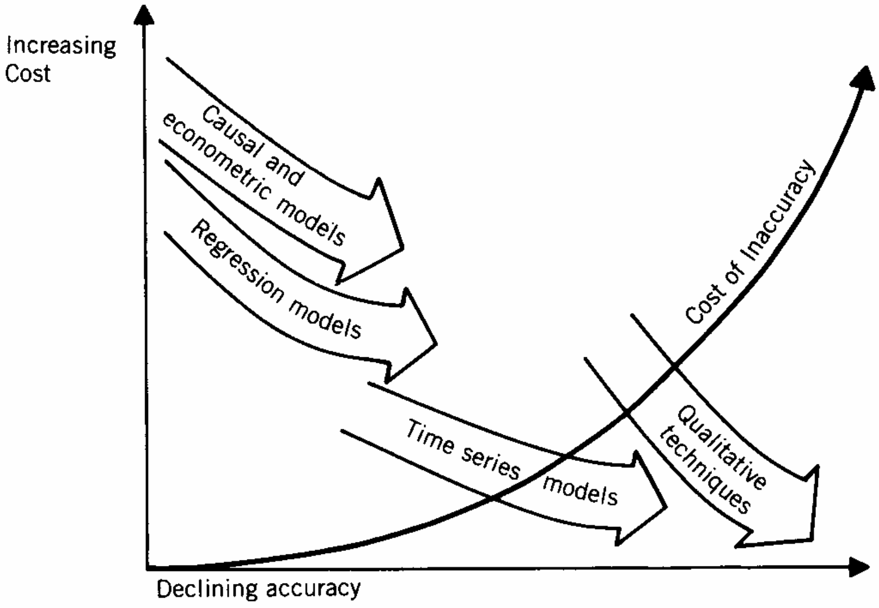
b. The market share is not fixed.

i. Market share is increasing every year, then linear regression
ii. Use the methods discussed previously.

Selection of a forecasting method

- A single organization may use several different forecasting methods to anticipate the future of its various actives. It also will likely use different methods during the life cycle of a single product. The selection may depend on any or all of the following factors:
  1. Availability and accuracy of historical data.
  2. Degree of accuracy expected from the prediction.
  3. Cost of developing the forecasting.
  4. Length of the prediction period.
  5. Time available to make the analysis.
  6. Complexity of factors affecting future operations.

- Comparison of forecasting costs for different forecasting methods ad the cost of inaccuracy. For example, qualitative techniques range from the expensive and accurate market research method to the less costly but also usually less reliable method of relying on one individual's prophecy.


Increasing Cost
Causal and econometric models
Regression models
Time series models
Qualitative techniques
Cost of Inaccuracy
Declining accuracy

Evaluating Forecasting Model Performance

- Impulse response: respond very fast to changes in historical data are described as having a high impulse response.
- Noise dampening ability: forecasts that reflect every little happenstance fluctuation in the past data are said to include random variation, or noise.
- Measure of forecast accuracy: the accuracy of a forecasting model refers to how close actual data follow forecasts
- The larger the number of period, the greater is the noise-dampening ability and the lower impulse response of the forecast and vice versa.

Three measures of forecast accuracy are commonly used

- Standard error of forecast or standard deviation of the forecast s_{yx}

$$S_{yx} = \sqrt{\frac{\sum y^2 - a\sum y - b\sum xy}{n-2}}$$

- Mean squared error (MSE), $(s_{yx})^2$
- Mean absolute deviation (MAD)

$$MAD = \frac{\sum_{i=1}^{n} |Actualdemand - Forecastdemand|}{n}$$

How to Select a Forecasting Method (how to have a successful forecasting system)

- Several factors should be considered:

1. Cost
2. Accuracy
3. Data available
4. Time span
5. Nature of products and services
6. Impulse response and noise dampening

There may be a trade-off between cost and accuracy.

Syllabus

Entrepreneurship Development (HSS-801)

1. **Semester:** 8th Sem "Department of Chemical Engineering" **L:T:P** 3:0:0 **Credits**: 03

2. **Course Objectives:**

I. Understanding basic concepts in the area of entrepreneurship, the role and importance of entrepreneurship for economic development

II. Developing personal creativity and entrepreneurial initiative for elaboration of business idea

III. Understanding the stages of the entrepreneurial process and the resources needed for the successful development of entrepreneurial ventures.

3. **Details of Course**

S. No	**Contents**
1	**Entrepreneurship:** Concept, nature, importance and need of Entrepreneurship. Concept of innovation, risk taking, opportunity seeking. Characteristics of an entrepreneur, Environmental Scanning (internal & external) Entrepreneurship development programs. Concepts and theories of Personality, Motivation and learning
2	**Enterprises:** Concept of enterprise. Types of enterprise: sole proprietorship, Partnership firm, Joint stock companies. Types of Companies. Process of incorporation of a company in India.
3	**Financing an Enterprise:** Concept of Finance, Sources of finance, concept of equity and debt financing. Types of shares.
4	**Market dynamics:** Concept of Marketing, concept of product and service, deeper concept of 4 P's of marketing, Intellectual property rights, Trademark, patent, copyright.
5	**Market:** Defining market, Classification of markets, Basic concepts about types of market structure (perfect market, monopoly, monopolistic, oligopoly and duopoly). Concept of Demand forecasting and techniques of demand forecasting.

Course outcomes

On successful completion of this course, student should be able to:

I. define basic terms and analyse the business environment in order to identify business opportunities

II. identify the elements of success of entrepreneurial ventures and the legal and financial conditions for starting a business venture

III. evaluate the effectiveness of different entrepreneurial strategies and specify the basic performance indicators of entrepreneurial activity

IV. explain the importance of marketing and management in small businesses venture and interpret their own business plan.

Entrepreneurship Development Programmes: Meaning, Need and Objectives of EDP

Meaning:

As the term itself denotes, EDP is a programme meant to develop entrepreneurial abilities among the people. In other words, it refers to inculcation, development, and polishing of entrepreneurial skills into a person needed to establish and successfully run his / her enterprise. Thus, the concept of entrepreneurship development programme involves equipping a person with the required skills and knowledge needed for starting and running the enterprise.

Let us also consider a few important definitions of EDPs given by institutions and experts:

Small Industries Extension and Training Institute (SIET 1974), now National Institute of Small Industry Extension Training (NISIET), Hyderabad defined EDP as "an attempt to develop a person as entrepreneur through structural training.The main purpose of such entrepreneurship development programme is to widen the base of entrepreneurship by development achievement motivation and entrepreneurial skills among the less privileged sections of the society."

According to N. P. Singh (1985), "Entrepreneurship Development Programme is designed to help an individual in strengthening his entrepreneurial motive and in acquiring skills and capabilities necessary for playing his entrepreneurial role effectively. It is necessary to promote this understanding of motives and their impact on entrepreneurial values and behaviour for this purpose." Now, we can easily define EDP as a planned effort to identify, inculcate, develop, and polish the capabilities and skills as the prerequisites of a person to become and behave as an entrepreneur.

Need for EDPs:

That, entrepreneurs possess certain competencies or traits. These competencies or traits are the underlying characteristics of the entrepreneurs which result in superior performance and which distinguish successful entrepreneurs from the unsuccessful ones.

Then, the important question arises is: where do these traits come from? Or, whether these traits are in born in the entrepreneurs or can be induced and developed? In other words, whether the entrepreneurs are born or made? Behavioural scientists have tried to seek answers to these questions.

A well-known behavioural scientist David C. McClelland (1961) at Harvard University made an interesting investigation-cum-experiment into why certain societies displayed great creative powers at particular periods of their history? What was the cause of these creative bursts of energy? He found that 'the need for achievement (n' ach factor)' was the answer to this question. It was the need for achievement that motivates people to work hard. According to him, money-making was incidental. It was only a measure of achievement, not its motivation.

In order to answer the next question whether this need for achievement could be induced, he conducted a five-year experimental study in Kakinada, i.e. one of the prosperous districts of Andhra Pradesh in India in collaboration with Small Industries Extension and Training Institute (SIET), Hyderabad.

This experiment is popularly known as 'Kakinada Experiment'. Under this experiment, young persons were selected and put through a three-month training programme and motivated to see fresh goals.

One of the significant conclusions of the experiment was that the traditional beliefs did not seem to inhibit an entrepreneur and that the suitable training can provide the necessary motivation to the entrepreneurs (McClelland & Winter 1969). The achievement motivation had a positive impact on the performance of entrepreneurs.

In fact, the 'Kakinada Experiment' could be treated as a precursor to the present day EDP inputs on behavioural aspects. In a sense, 'Kakinada Experiment' is considered as the seed for the Entrepreneurship Development Programmes (EDPs) in India.

The fact remains that it was the 'Kakinada Experiment' that made people appreciate the need for and importance of the entrepreneurial training, now popularly known as 'EDPs', to induce motivation and competence among the young prospective entrepreneurs.

Based on this, it was the Gujarat Industrial Investment Corporation (GIIC) which, for the first time, started a three-month training programmes on entrepreneurship development. Impressed by the results of GIIC's this training programme, the Government of India embarked, in 1971, on a massive programme on entrepreneurship development. Since then, there is no looking back in this front. By now, there are some 686 all-India and State level institutions engaged in conducting EDPs in hundreds imparting training to the candidates in thousands.

Till now, 12 State Governments have established state-level Centre for Entrepreneurship Development (CED) or Institute of Entrepreneurship Development (lED) to develop entrepreneurship by conducting EDPs. Today, the EDP in India has proliferated to such a magnitude that it has emerged as a national movement. It is worth mentioning that India operates the oldest and largest programmes for entrepreneurship development in any developing country.

The impact of India’s EDP movement is borne by the fact that the Indian model of entrepreneurship development is being adopted by some of the developing countries of Asia and Africa. Programmes similar to India’s EDPs are conducted in other countries also, for example, ‘Junior Achievement Programme’ based on the principle of ‘catch them young’ in USA and ‘Young Enterprises’ in the U. K.

Objectives of EDP:

The major objectives of the Entrepreneurship Development Programmes (EDPs) are to:

a. Develop and strengthen the entrepreneurial quality, i.e. motivation or need for achievement.

b. Analyse environmental set up relating to small industry and small business.

c. Select the product.

d. Formulate proposal for the product.

e. Understand the process and procedure involved in setting up a small enterprise.

f. Know the sources of help and support available for starting a small scale industry.

g. Acquire the necessary managerial skills required to run a small-scale industry.

h. Know the pros and cons in becoming an entrepreneur.

i. Appreciate the needed entrepreneurial discipline.

j. Besides, some of the other important objectives of the EDPs are to:

k. Let the entrepreneur himself / herself set or reset objectives for his / her enterprise and strive for their realization.

l. Prepare him / her to accept the uncertainty in running a business.

m. Enable him / her to take decisions.

n. Enable to communicate clearly and effectively.

o. Develop a broad vision about the business.

p. Make him subscribe to the industrial democracy.

q. Develop passion for integrity and honesty.

r. Make him learn compliance with law.

Environmental Scanning - Internal & External Analysis of Environment

Organizational environment consists of both external and internal factors. Environment must be scanned so as to determine development and forecasts of factors that will influence organizational success. Environmental scanning refers to possession and utilization of information about occasions, patterns, trends, and relationships within an organization's internal and external environment. It helps the managers to decide the future path of the organization. Scanning must identify the threats and opportunities existing in the environment. While strategy formulation, an organization must take advantage of the opportunities and minimize the threats. A threat for one organization may be an opportunity for another.

Internal analysis of the environment is the first step of environment scanning. Organizations should observe the internal organizational environment. This includes employee interaction with other employees, employee interaction with management, manager interaction with other managers, and management interaction with shareholders, access to natural resources, brand awareness, organizational structure, main staff, operational potential, etc. Also, discussions, interviews, and surveys can be used to assess the internal environment. Analysis of internal environment helps in identifying strengths and weaknesses of an organization.

As business becomes more competitive, and there are rapid changes in the external environment, information from external environment adds crucial elements to the effectiveness of long-term plans. As environment is dynamic, it becomes essential to identify competitors' moves and actions. Organizations have also to update the core competencies and internal environment as per external environment. Environmental factors are infinite, hence, organization should be agile and vigile to accept and adjust to the environmental changes. For instance - Monitoring might indicate that an original forecast of the prices of the raw materials that are involved in the product are no more credible, which could imply the requirement for more focused scanning, forecasting and analysis to create a more trustworthy prediction about the input costs. In a similar manner, there can be changes in factors such as competitor's activities, technology, market tastes and preferences.

While in external analysis, three correlated environment should be studied and analyzed —

- immediate / industry environment

- national environment
- broader socio-economic environment / macro-environment

Examining the industry environment needs an appraisal of the competitive structure of the organization’s industry, including the competitive position of a particular organization and it’s main rivals. Also, an assessment of the nature, stage, dynamics and history of the industry is essential. It also implies evaluating the effect of globalization on competition within the industry. Analyzing the national environment needs an appraisal of whether the national framework helps in achieving competitive advantage in the globalized environment. Analysis of macro-environment includes exploring macro-economic, social, government, legal, technological and international factors that may influence the environment. The analysis of organization’s external environment reveals opportunities and threats for an organization.

Strategic managers must not only recognize the present state of the environment and their industry but also be able to predict its future positions.

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Importance of Entrepreneurship

Entrepreneurship is the dynamic process of creating incremental wealth and innovating things of value that have a bearing on the welfare of an entrepreneur.

It provides civilization with an enormous amount of goods and services and enhances the growth of social welfare.

The main importance of entrepreneurship is the creation of job opportunities, innovation, and improve the economy. The importance of entrepreneurship can be stated as under:

1. Growth of Entrepreneurship.
2. Creation of job opportunities.
3. Innovation.
4. Impact on community development.
5. The consequence of business failure.
6. Political and economic integration of outsiders.
7. Spawns entrepreneurship.
8. Enhances the standard of living.
9. Promotes research and development.

1. Growth of Entrepreneurship

Entrepreneurship the advent of new venture particularly small ventures to materialize the innovative ideas of the entrepreneurs. Thus, the growth or establishment of small enterprises ii the specific contribution of entrepreneurship in every economy of the world.

2. Creation of job opportunities

Entrepreneurship firms contributed a large share of new jobs. It provides entry-level jobs so necessary fur training or gaining experience for unskilled workers. The small enterprises are the only sector that generates a large portion of total employment every year. Moreover, entrepreneurial ventures prepare and supply experienced labor to large industries.

3. Innovation

Entrepreneurship is the incubator of innovation. Innovation creates disequilibria in the present state of order. It goes beyond discovery and does implementation and commercialization, of innovations. “Leapfrog” innovation, research, and development are being contributed by entrepreneurship. Thus, entrepreneurship nurses innovation that provides new ventures, products, technology, market, quality of good, etc. to the economy that increases Gross Domestic Products and standard of living of the people.

4. Impact on community development

A community is better off if its employment base is diversified among many small entrepreneurial firms. It promotes abundant retail facilities, a higher level of homeownership, fewer slums, better, sanitation standards and higher expenditure on education, recreation, and religious activities. Thus, entrepreneurship leads to more stability and a higher quality of community life.

5. The consequence of business failure

The collapse of the large industry almost has irresistible damage to the development of the state and the state of the economy and the financial condition of the relevant persons. The incumbents lost their jobs: suppliers and financial institutions face a crisis of recovery. Customers are deprived of goods, services, and government losses taxes. This could not happen in the case of failure of entrepreneurship.There shall be no measurable effect upon the economy and no political repercussions too.

6. Political and economic integration of outsiders

Entrepreneurship is the most effective way of integrating those who feel disposed of and alienated into the economy. Minorities, migrants, and women are safely integrated into entrepreneurship that will help to develop a well-composed plural society.

7. Spawns entrepreneurship

Entrepreneurship is the nursing ground for new inexperienced adventurists. It is the field where a person can start his/her idea of the venture, which may be ended up in a giant enterprise. All the large industrial ventures started as a small entrepreneurial enterprise. Therefore, entrepreneurship provides a wide spectrum of ventures and entrepreneurs in every economy. The vast open arena of entrepreneurship thus acts as an incubator to entrepreneurs.

8. Enhances the standard of living

The standard of living is a concept built on an increase in the amount of consumption of a variety of goods and services over a particular period by a household. So it depends on the availability of diversified products in the market. Entrepreneurship provides enormous kinds of a product of various natures by their innovation. Besides, it increases the income of the people who are employed in entrepreneurial enterprises. That also capable employed persons to consume more goods and services. In effect, entrepreneurship enhances the standard of living of the people of a country.

9. Promotes research and development

Entrepreneurship is innovation and hence the innovated ideas of goods and services have to be tested by experimentation. Therefore, entrepreneurship provides funds for research and development with universities and research institutions. This promotes the general development, research, and development in the economy. Entrepreneurship is the pioneering zeal that provides events in our civilization.

Innovation, Risk-taking and Opportunity Seeking in Entrepreneurship

Entrepreneurship The simple meaning of entrepreneur is a person who is brave in taking risks to open a business on various opportunities.

Dare to take the risk means independent mentality and courage to start a business, without fear or anxious even in uncertain conditions with enough consideration. Entrepreneurial activity can be done alone or in groups. An entrepreneur is someone who is always trying to look, utilize, and create business opportunities that are expected to have benefits. Successful entrepreneurs are entrepreneurs that can survive with all the limitations, exploit it, and increase it to market the opportunity well and continue creating reputation that makes the company grow. It can be concluded that entrepreneurship is an ability to manage something in themselves to be utilized and enhanced to be better so it can improve the standard of living in the future. An entrepreneur has clear characteristics that distinguish himself from others who are not entrepreneurs. Ciputra University teachs 7 entrepreneurship characters to all students, namely:

a) Passion, has enthusiasm and love for what he does.

b) Independent, able to act alone without relying on others in making choices and making decisions.

c) Opportunity creation, sensitive to market condition so as to be capable utilize and create opportunities.

d) Creative & innovative, bring up original idea and make it happen.

e) Calculated risk taker, always taking into account the likelihood of success and failure in the implementation of activities to achieve goals.

f) Persistent, persistent and diligent in reaching the goal.

g) High ethical standard, always refer to and pay attention to ethics in making decisions and achieving goals. The opportunity creation and calculated risk taker characters will be discussed more because they have important role in the development of business owned by Mr. Agus.

Opportunity Creation:

One of the characteristics of entrepreneur is smart to see market opportunities. Entrepreneurs must be able to find and recognize problem in business and seek answer to that problem. Business opportunities can arise from the answers generated from the problems that occur. This means that when there is an opportunity that fits with the financial condition or expertise, then this opportunity can be a profitable business potential. An entrepreneur is trained to discover or create opportunities in any business or organizational development. An entrepreneur should be able to see an opportunity or opportunity from different perspective from others, or something that other people do not think of which can be shaped into value. There are several indicators that can be used by entrepreneurs to capture the available business opportunities, which are:

a) The ability to identify markets. This is needed so an entrepreneur can see the need of their consumers, especially with regard to products and services.

b) Ability to be sensitive to the market. Entrepreneurs are expected to know changes in market demand, know the number of their competitors, and what advantages are owned.

c) Ability to seize the market. This is really needed for small companies or growing companies because they have to compete to survive.

d) Attractive. Looking for attractive market is needed to keep the market growing and profitable. Competitors will not feel threatened, so it can increase sales of the company.

e) Enlarge market capacity. The greater the market capacity the greater the demand.

A new product creation is a market opportunity, it needs to be accompanied by innovations so it can survive in the marketplace. There are several aspects in exploiting a market opportunity, which are:

a) The cause of an opportunity arises from something unexpected, discomfort, need for process improvement, industry and market structural change, demographic changes, perceptual changes, or new technologies and knowledge.

b) Benefits provided from the products created.

c) Product advantages that can attract consumers to buy.

d) Ability to control the price and cost of the product.

e) Calculation of capital and the rate of return of the project.

f) The company's commitment to the products to be marketed.

Calculated Risk Taker Risk is the willingness of entrepreneurs to commit to manage all the resources they have to finance a business fully in spite of the high probability that the business may fail. People are afraid to take risk because of the chance of being fail. Entrepreneurs are the opposite, they are willing to take the risk. Risk-taking firm is a company that has a high tendency to bravely take a business that promises big profits, although that also comes with big risks. The risk of loss is common because entrepreneurs hold the principle that loss factor must exist. An entrepreneur must have good planning, able to manage risk, and minimize risk that may occur. Entreprenenur will face several types of different risks that are grouped into four parts :

a) Financial risk: This risk is a risk that must be faced by every entrepreneur. Capital is definitely needed in starting a business, be it in small or large scale. The capital may come from personal funds, or from other parties. If the business failed then the capital can be lost.

b) Career risk: This risk is faced by entrepreneurs who had previous permanent jobs. If being an entrepreneur means he must leave his old job that provided fixed income for a new business that is not yet certain.

c) Family and social risk: This risk relates to the time consumed in starting a new business, reducing the time usually spent with family or friends.

d) Psychic risk: This risk is to be avoided by an entrepreneur. Psychic problems can occur if the business owner has a very severe problem that gets to the point of depression.

A company, in this case the company owned by an entrepreneur must have risk management that has the following benefits:

a) Provide a foundation in determining strategy or consideration when dealing with problems

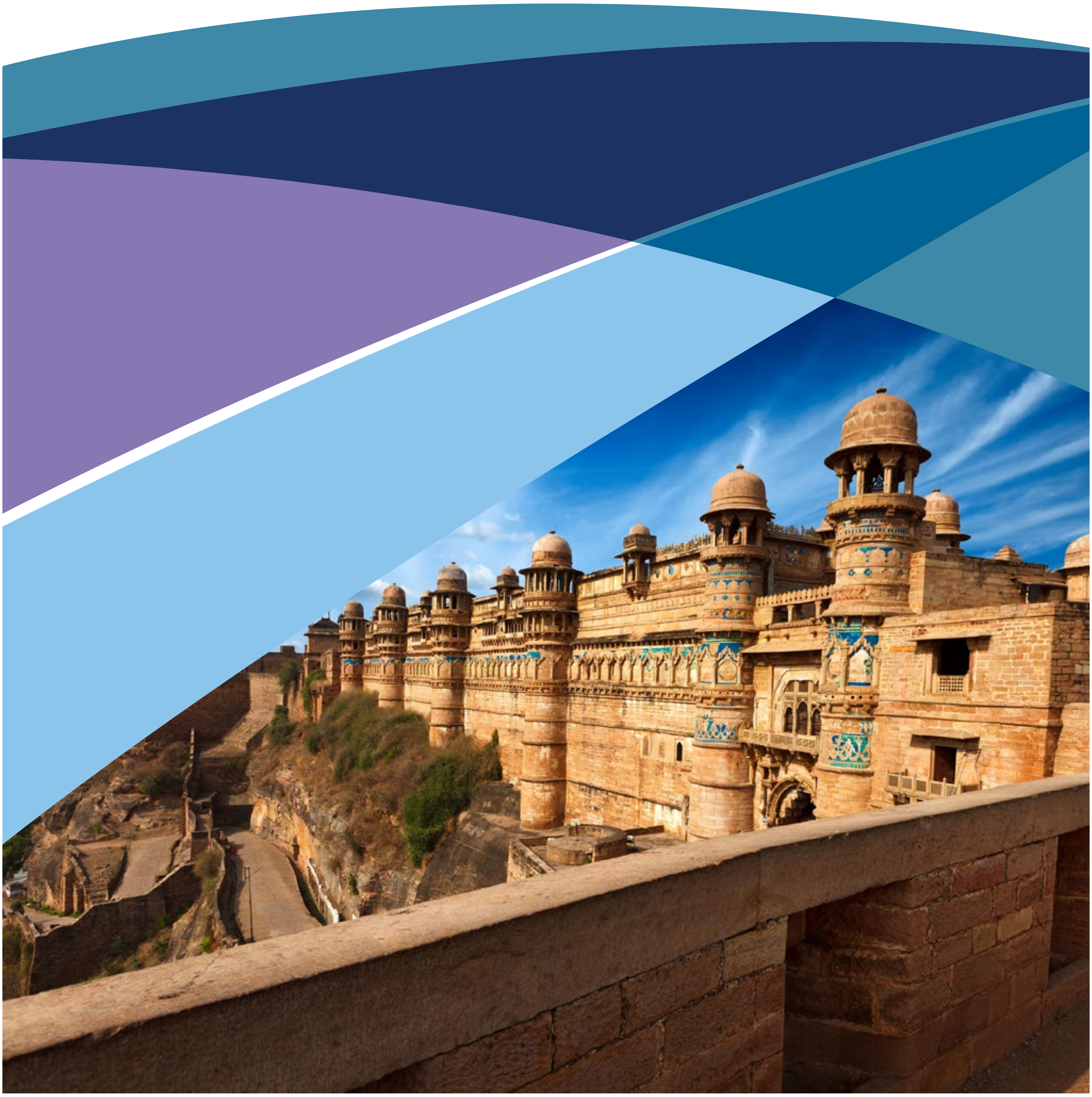
b) Provide direction and purpose where company will move

c) Allow company to reduce risk

d) Provide guidance, direction and mechanism in a sustainable manner.

Intellectual
Property
Office

Intellectual property rights in India



Intellectual Property Office is an operating name of the Patent Office

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Intellectual property rights in India

India is one of the UKs priority overseas markets.

If you plan to do business in India, or if you are already trading there, it is essential to know how to use, guard and enforce the rights you have over the intellectual property (IP) that you or your business own.

This guide explains about IP in general, and gives guidance on how to apply these principles in the Indian market. It describes the issues you may face with IP infringement in India, offers advice on how you can effectively tackle these, and provides links to sources of further help.

What are intellectual property rights?

Intellectual property (IP) is a term referring to a brand, invention, design or other kind of creation, which a person or business has legal rights over. Almost all businesses own some form of IP, which could be a business asset.

Common types of IP include:

- **Copyright –** this protects written or published works such as books, songs, films, web content and artistic works;

- **Patents –** this protects commercial inventions, for example, a new business product or process;

- **Designs –** this protects designs, such as drawings or computer models;

- **Trade marks –** this protects signs, symbols, logos, words or sounds that distinguish your products and services from those of your competitors.

IP can be either registered or unregistered.

With **unregistered** IP, you automatically have legal rights over your creation. Unregistered forms of IP include copyright, unregistered design rights, common law trade marks and database rights, confidential information and trade secrets.

With **registered** IP, you will have to apply to an authority, such as the Intellectual Property Office in the UK, to have your rights recognised. If you do not do this, others are free to exploit your creations. Registered forms of IP include patents, registered trade marks and registered design rights. Copyright is also registerable.

International considerations

India has been a World Trade Organisation (WTO) member since 1995. WTO member nations must include some IP protection in their national laws. This means that if you are doing business with India, you will find some similarity between local IP law and enforcement procedures, and those in force in the UK.

Treaties and reciprocal agreements

India is also a signatory to the following international IP agreements:

- the Paris Convention – under this, any person from a signatory state can apply for a patent or trade mark in any other signatory state, and will be given the same enforcement rights and status as a national of that country would be;

- the Berne Convention – under this, each member state recognises the copyright of authors from other member states in the same way as the copyright of its own nationals;

- the Madrid Protocol – under this, a person can file a single trade mark application at their national office that will provide protection in multiple countries;

- the Patent Cooperation Treaty – this is a central system for obtaining a 'bundle' of national patent applications in different jurisdictions through a single application.

India is not a signatory to the Hague Agreement, which allows the protection of designs in multiple countries through a single filing.

Intellectual property rights – systems in India

Copyright

India is a signatory to the Berne Convention on copyright. However, it may be a good idea to register your copyright as doing so may help to prove ownership if there are criminal proceedings against infringers. In most cases though, registration is not necessary to maintain a copyright infringement claim in India. Registration is made, in person or via a representative, with the Copyright Office. Since 2016, copyright policy was moved to India's Ministry of Commerce and Industry. All IPRs are now administered by the Department for Industrial Property and Promotion (DIPP).

Internet piracy of films, music, games and software is an issue in India, as is unauthorised copying of physical books.

Patents

India's Patents Act of 1970, 2003 Patent Rules and the 2016 Patent Amendment Rules set out the law concerning patents. As in the UK, there is no provision for utility model patents.

The regulatory authority for patents is the Patent Registrar under the office of the Controller General of Patents, Designs and Trade Marks, which is part of India's Ministry of Commerce and Industry. Patents are valid for 20 years from the date of filing an application, subject to an annual renewal fee.

India's patent law operates under the 'first to file' principle – that is, if two people apply for a patent on an identical invention, the first one to file the application will be awarded the patent.

Designs

The laws governing designs are the Designs Act 2000 and the Designs Rules 2001. Designs are valid for a maximum of ten years, renewable for a further five years.

Trade marks

India’s trade mark laws consist of the 1999 Trade Marks Act and the Trade Marks Rules of 2002 and 2017.

The regulatory authority for patents is the Controller General of Patents, Designs and Trade Marks under the Department of Industrial Policy and Promotion. The police now have more robust powers in enforcing trade mark law, including the ability to search premises and seize goods suspected of being counterfeit without a warrant. But these powers are tempered by the requirement for the police to seek the Trade Mark Registrar’s opinion on the registration of the mark before taking action. This adds to the delay and may result in counterfeit goods being removed or sold.

Trade names also constitute a form of trade mark in India, with protection, irrespective of existing trade names, for those wishing to trade under their own surname.

Because of the widespread practice of ‘cybersquatting’ – the registration in bad faith of marks by third parties registering domain names for certain well known marks in order to sell them to the original rights owners – it is advisable for rights owners to register their domain names in India as trade marks as soon as possible.

Registration takes up to two years. A trade mark in India is valid for ten years and can be renewed thereafter indefinitely for further ten-year periods.

Registering and enforcing intellectual property rights in India

To enjoy most types of intellectual property (IP) rights in India, you should register them.

For patents, individual registrations must be made in India, but for rights other than industrial designs you can apply under the terms of the Patent Cooperation Treaty, which is usually easier and quicker.

For trade marks, you should register them within India, either through the domestic trade mark system or under the Madrid system.

For copyright, no registration is required but registering copyrights with the copyright authorities is advisable.

‘Priority rights’ under the Paris Convention can help in the local registration of trade marks, designs and patents by allowing rights previously registered elsewhere to become effective in India, if filed within a time limit.

Enforcing IP rights in India

IP rights can be enforced by bringing actions to the civil courts or through criminal prosecution. India's IP laws set out procedures for both civil and criminal proceedings, as does the Competition Act. Criminal proceedings do not apply to patent and design infringements.

A disadvantage of civil litigation is that you are unlikely to recover large damages, and punitive damages against an infringer are rare. However, if you have an identified infringer, it may be advisable to launch civil litigation, because if an interim injunction is granted the infringement can be halted pending the outcome of the case. Damages are routinely awarded in cases of copyright piracy and trade mark infringement (which come under criminal litigation); less so in patent cases. Over the years, however, decisions in favour of foreign companies against local infringers have demonstrated the judiciary's impartial approach.

As in other countries, the Indian Government brings actions in criminal cases, although in most cases actions follow complaints to magistrates or police authorities by rights owners. Criminal proceedings against infringers carry the prospect of much harsher remedies, including fines and imprisonment.

Mediation or negotiation with an infringer can also be effective as an alternative form of dispute resolution. The Civil Procedure Code provides for a formal mediation process.

Self-help considerations

There are various things you can do to make it harder in general for infringers to copy your product. For example, you could:

- Think about the design of your product, and how easy it would be for somebody to reproduce it without seeing your original designs;

- When you hire staff, have effective IP-related clauses in employment contracts. Also make sure you educate your employees on IP rights and protection;

- Have sound physical protection and destruction methods for documents, drawings, tooling, samples, machinery etc.;

- Make sure there are no 'leakages' of packaging that might be used by counterfeiters to pass off fake product;

- Check production over-runs to make sure that genuine product is not being sold under a different name.

Potential problems faced in India and how to deal with them

India's intellectual property (IP) legislation covers every significant aspect of the protection of IP. The regulations relating to all forms of IP have been amended or reissued in recent years, mainly in response to India's accession to the World Trade Organisation in 1995.

Although Indian IP law is thorough and generally comparable with European IP laws, there are still significant concerns over IP enforcement. A major cause for concern in enforcement is bureaucratic delay, with a backlog of cases at both the civil and criminal courts. This means that cases can run for five years or more. There is also a lack of transparency, particularly at a local level.

A significant feature of the IP environment in India is the large number of small players infringing IP rights. This means that seizures tend to be small, which requires a sustained and financially draining effort in order to make an impact.

An advantage for UK businesses operating in India is that the legal system is based on common law, as in the UK, so the fundamental processes are familiar.

Avoiding problems

The most important way to avoid problems when defending IP rights in India is to be prepared. To make sure that you can anticipate any potential issues, you should:

- take advice from Indian IP rights experts at an early stage on how to protect your IP – prevention is better than cure;
- consult publications and websites on Indian IP rights and protection in general;
- carry out risk assessment and due diligence checks on any organisations and individuals you deal with;
- take professional advice from other experts – for example lawyers, local diplomatic posts, Chambers of Commerce and the UK India Business Council;
- talk to other businesses already doing similar business in India;
- consult agents, distributors and suppliers on how best to safeguard your rights;
- check with trade mark or patent attorneys to see whether there have been previous registrations of your own marks, or other IP, in India;
- stick to familiar business methods – don't be tempted to do things differently because you're trading in a different country.

Who should take responsibility for your IP protection?

You should make sure that everyone in your business takes some responsibility for IP protection. Many businesses depend on the integrity of their IP, and it can often be one of their most valuable assets. So it should be given proper attention by both management and employees, as well as other businesses that you have relationships with.

It may be sensible to nominate a manager to have particular responsibility for understanding and protecting your IP rights. In businesses with legal departments, a legally-trained manager would be a good choice.

Where to get intellectual property help in India

Whether you're resident in and doing business in India, or trading internationally with the country, there are a number of professional organisations that can offer you advice and support:

- The British High Commission, New Delhi offers advice on working with India, including details of cultural relations. It provides a full range of diplomatic, consular and business-related services: https://www.gov.uk/government/world/organisations/british-high-commission-new-delhi

- The UK India Business Council (UKIBC) helps and supports British businesses with regard to trade with India: http://www.ukibc.com

- The Department for International Trade (DIT) India has a range of online information on doing business in India: https://www.gov.uk/government/world/organisations/department-for-international-trade-india

- Local law firms in India can offer you legal advice and services specific to your business. The Chambers and Partners website offers a search facility listing Indian local law firms: http://www.chambersandpartners.com/Asia/Search/Location/110

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INVESTORS
IN PEOPLE

CUSTOMER
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CSE

Meaning of Enterprise:

Organisation or Enterprise means to plan a business, to start it and run it. It means to bring the factors of production together, assign each its proper task, and pay them remuneration when the work is done. It implies not only running of a business, but also shouldering the loss, if any. The man who undertakes all this work is called an organiser, or, more commonly, an entrepreneur. Organising and risk-taking are the two main functions of the entrepreneur.

Joint Stock Company:

A company form of business orgnisation is known as a Joint Stock Company. It is a voluntary association of persons who generally contribute capital to carry on a particular type of business, which is established by law and can be dissolved only by law. Persons who contribute capital become members of the company. This form of business has a legal existence separate from its members, which means even if its members die, the company remains in existence. This form of business organisations generally requires huge capital investment, which is contributed by its members. The total capital of a joint stock company is called share capital and it is divided into a number of units called shares. Thus, every member has some shares in the business depending upon the amount of capital contributed by him. Hence, members are also called shareholders.

The companies in India are governed by the Indian Companies Act, 1956. The Act defines a company as an artificial person created by law, having a separate legal entity, with perpetual succession and a common seal.

Characteristics of Joint Stock Company

i. Legal formation

No single individual or a group of individuals can start a business and call it a joint stock company. A joint stock company comes into existence only when it has been registered after completion of all formalities required by the Indian Companies Act, 1956.

ii. Artificial person

Just like an individual, who takes birth, grows, enters into relationships and dies, a joint stock company takes birth, grows, enters into relationships and dies. However, it is called an artificial person as its birth, existence and death are regulated by law and it does not possess physical attributes like that of a normal person.

iii. Separate legal entity

Being an artificial person, a joint stock company has its own separate existence independent of its members. It means that a joint stock company can own property, enter into contracts and conduct any lawful business in its own name. It can sue and can be sued by others in the court of law. The shareholders are not the owners of the property owned by the company. Also, the shareholders cannot be held responsible for the acts of the company

iv. Common seal

A joint stock company has a seal, which is used while dealing with others or entering into contracts with outsiders. It is called a common seal as it can be used by any officer at any level of the organisation working on behalf of the company. Any document, on which the company's seal is put and is duly signed by any official of the company, become binding on the company. For example, a purchase manager may enter into a contract for buying raw materials from a supplier. Once the contract paper is sealed and signed by the purchase manager, it becomes valid. The purchase manager may leave the company thereafter or may be removed from the job or may have taken a wrong decision, yet for all purposes the contract is valid till a new contract is made or the existing contract expires.

v. Perpetual existence

A joint stock company continues to exist as long as it fulfils the requirements of law. It is not affected by the death, lunacy, insolvency or retirement of any of its members. For example, in case of a private limited company having four members, if all of them die in an accident the company will not be closed. It will continue to exist. The shares of the company will be transferred to the legal heirs of the deceased members.

vi. Limited liability

In a joint stock company, the liability of a member is limited to the extent of the value of shares held by him. While repaying debts, for example, if a person owns 1000 shares of Rs. 10 each, then he is liable only upto Rs 10,000 towards payment of debts. That is, even if there is liquidation of the company, the personal property of the shareholder can not be attached and he will lose only his shares worth Rs. 10,000.

vii. Democratic management

Joint stock companies have democratic management and control. That is, even though the shareholders are owners of the company, all of them cannot participate in the management of the company. Normally, the shareholders elect representatives from among themselves known as 'Directors' to manage the affairs of the company.

Meaning of Partnership

It is basically a relation between two or more persons who join hands to form a business organisation with the objective of earning profit. The persons who join hands are individually known as 'Partner' and collectively a 'Firm'. The name under which the business is carried on is called 'firm name'. Sultan Chand & Co, Ram Lal & Co, Gupta & Co are the names of some partnership firms.

The partners provide the necessary capital, run the business jointly and share the responsibility. You must be thinking how much capital each partner contributes? Do all the partners jointly manage the business or can any of them manage the business on behalf of others? Who will take the profits? If there is any loss then who will suffer the loss? Yes, these are the few questions that might be coming to your mind. Actually, when you invite your friends to start such a business, it should be the duty of all of you to decide (i) the amount of capital to be contributed by each one of you; (ii) who will manage; (iii) how will the profits and losses be shared. Thus, there must be some agreement between the partners before they actually start the business. This agreement is termed as 'Partnership Deed', which lays down certain terms and conditions for starting and running the partnership firm. This agreement may be oral or written. Actually, it is always better to insist on a written agreement among partners in order to avoid future controversies.

A partnership firm is governed by the provisions of the Indian Partnership Act, 1932. Section 4 of the Indian Partnership Act, 1932, defines partnership as "a relation between persons who have agreed to share the profits of a business carried on by all or any of them acting for all."

Features of Partnership form of business organisation

After having a brief idea about partnership, let us identify the various features of this form of business organisation.

i. Two or more Members - You know that the members of the partnership firm are called partners. But do you know how many persons are required to form a partnership firm? At least two members are required to start a partnership business. But the number of members should not exceed 10 in case of banking business and 20 in case of other business. If the number of members exceeds this maximum limit then that business cannot be termed as partnership business. A new form of business will be formed, the details of which you will learn in your next lesson. ii. Agreement: Whenever you think of joining hands with others to start a partnership business, first of all, there must be an agreement between all of you. This agreement containso the amount of capital contributed by each partner; o profit or loss sharing ratio; o salary or commission payable to the partner, if any; o duration of business, if any ; o name and address of the partners and the firm; o duties and powers of each partner; o nature and place of business; and o any other terms and conditions to run the business. iii. Lawful Business - The partners should always join hands to carry on any kind of lawful business. To indulge in smuggling, black marketing, etc., cannot be called partnership business in the eye of the law. Again, doing social or philanthropic work is not termed as partnership business. iv. Competence of Partners - Since individuals join hands to become the partners, it is necessary that they must be competent to enter into a partnership contract. Thus, minors, lunatics and insolvent persons are not eligible to become the partners. However, a minor can be admitted to the benefits of partnership i.e., he can have a share in the profits only.

v. Sharing of Profit - The main objective of every partnership firm is sharing of profits of the business amongst the partners in the agreed proportion. In the absence of any agreement for the profit sharing, it should be shared equally among the partners. Suppose, there are two partners in the business and they earn a profit of Rs. 20,000. They may share the profits equally i.e., Rs.

10,000 each or in any other agreed proportion, say one forth and three fourth i.e. Rs 5,000/- and Rs. 15000/-.

vi. Unlimited Liability - Just like the sole proprietor the liability of partners is also unlimited. That means, if the assets of the firm are insufficient to meet the liabilities, the personal properties of the partners, if any, can also be utilised to meet the business liabilities. Suppose, the firm has to make payment of Rs. 25,000/- to the suppliers of goods. The partners are able to arrange only Rs. 19,000/- from the business. The balance amount of Rs. 6,000/- will have to be arranged from the personal properties of the partners. vii. Voluntary Registration - It is not compulsory that you register your partnership firm. However, if you don't get your firm registered, you will be deprived of certain benefits, therefore it is desirable. The effects of non-registration are: o Your firm cannot take any action in a court of law against any other parties for settlement of claims. o In case there is any dispute among partners, it is not possible to settle the disputes through a court of law. o Your firm cannot claim adjustments for amount payable to or receivable from any other parties.

viii. No Separate Legal Existence - Just like sole proprietorship, partnership firm also has no separate legal existence from that of it owners. Partnership firm is just a name for the business as a whole. The firm means the partners and the partners collectively mean the firm. ix. Principal Agent Relationship - All the partners of the firm are the joint owners of the business. They all have an equal right to actively participate in its management. Every partner has a right to act on behalf of the firm. When a partner deals with other parties in business transactions, he/she acts as an agent of the others and at the same time the others become the principal. So there always exists a principal agent relationship in every partnership firm. x. Restriction on Transfer of Interest - No partner can sell or transfer his interest to any one without the constent of other partners. For example - A, B, and C are three partners. A wants to sell his share to D as his health does not permit him to work any more. He can not do so until B and C both agree.

xi. Continuity of Business - A partnership firm comes to an end in the event of death, lunacy or bankruptcy of any partner. Even otherwise, it can discontinue its business at the will of the partners. At any time, they may take a decision to end their relationship.

Advantages of partnership form of business organisation

Partnership form of business organisation has certain advantages, which are as follows

a) Easy to form: Like sole proprietorship, the partnership business can be formed easily without any legal formalities. It is not necessary to get the firm registered. A simple agreement, either oral or in writing, is sufficient to create a partnership firm. b) Availability of large resources - Since two or more partners join hand to start partnership business it may be possible to pool more resources as compared to sole proprietorship. The partners can contribute more capital, more effort and also more time for the business. c) Better decisions - The partners are the owners of the business. Each of them has equal right to participate in the management of the business. In case of any conflict they can sit together to solve the problems. Since all partners participate in decision-making, there is less scope for reckless and hasty decisions. d) Flexibility in operations - The partnership firm is a flexible organisation. At any time the partners can decide to change the size or nature of business or area of its operation. There is no need to follow any legal procedure. Only the consent of all the partners is required. e) Sharing risks - In a partnership firm all the partners share the business risks. For example, if there are three partners and the firm suffers a loss of Rs. 12,000 in a particular period, then all partners may share it and the individual burden will be Rs. 4,000 only. f) Protection of interest of each partner - In a partnership firm every partner has an equal say in decision making. If any decision goes against the interest of any partner he can prevent the decision from being taken. In extreme cases a dissenting partner may withdraw himself from the business and can dissolve it. g) Benefits of specialization - Since all the partners are owners of the business they can actively participate in every aspect of business as per their specialisation and knowledge. If you want to start a firm to provide legal consultancy to people, then one partner may deal with civil cases, one in criminal cases, another in labour cases and so on as per their specialization. Similarly two or more doctors of different specialization may start a clinic in partnership.

Meaning of Sole Proprietorship The term ‘sole’ means single and ‘proprietorship’ means ‘ownership’. So, only one person is the owner of the business organization. This means, that a form of business organization in which a single individual owns and manages the business, takes the profits and bears the losses, is known as sole proprietorship form of business organization. A sole proprietorship is a business owned by only one person. It is easy to set-up and is the least costly among all forms of ownership. The owner faces unlimited liability which means that the creditors of the business may go after the personal assets of the owner if the business cannot pay them. The sole proprietorship form is usually adopted by small business entities. These firms are owned by one person, usually the individual who has day-to-day responsibility for running the business. Sole proprietorships own all the assets of the business and the profits generated by it. They also assume complete responsibility for any of its liabilities or debts. In the eyes of the law and the public, you are one in the same with the business.

With this type of business organization, you are the sole owner, and fully responsible for all debts and obligations related to your business.

1.3 Definition of Sole Proprietorship According to J.L. Hanson, Sole Proprietorship is defined as:

“A type of business unit where one person is solely responsible for providing the capital and bearing the risk of the enterprise, and for the management of the business.”

Thus, ‘Sole Proprietorship’ form of business organization refers to a business enterprise exclusively owned, managed and controlled by a single person with all authority, responsibility and risk.

Characteristics of Sole Proprietorship

The features of sole proprietorship are enlisted as below:

Single Ownership: The sole proprietorship form of business organization has a single owner who himself/herself starts the business by bringing together all the resources.

No Separation of Ownership and Management: The owner himself manages the business as per his own skill and intelligence. There is no separation of ownership and management as is the case with company form of business organization.

Less Legal Formalities: The formation and operation of a sole proprietorship form of business organization does not involve any legal formalities. Thus, its formation is quite easy and simple.

No Separate Entity: The business unit does not have an entity separate from the owner. The businessman and the business enterprise are one and the same, and the businessman is responsible for everything that happens in his business unit.

No Sharing of Profit and Loss: The sole proprietor enjoys the profits alone. At the same time, the entire loss is also borne by him. No other person is there to share the profits and losses of the business. He alone bears the risks and reaps the profits.

Unlimited Liability: The liability of the sole proprietor is unlimited. In case of loss, if his business assets are not enough to pay the business liabilities, his personal property can also be utilized to pay off the liabilities of the business.

One-man Control: The controlling power of the sole proprietorship business always remains with the owner. He runs the business as per his own will.

Formation of Sole Proprietorship Business

It is very simple to establish a sole proprietary concern. Any person who is willing to start a business and has the necessary resources can set up this form of business organization. To start and operate the business in this form, practically does not require any legal formalities to be fulfilled. In some cases like restaurant, chemist shop etc. however, permission from the competent authority is required to be obtained before starting the business. Similarly, setting up a factory may involve taking permission from the local authority. But, formation of business unit as such does not involve any complexities.

Advantages of Sole Proprietorship

Sole proprietorship is a form of business organization which is very simple to initiate and can be run by a single person with small amount of money also. Thus, following are the significant benefits of sole proprietorship:

Easy to Form and Close: It is very easy and simple to form a sole proprietorship form of business organization. No legal formalities are required to be observed. Similarly, the business can be wind up any time if the proprietor so decides. There are fewer forms to file than with other business organizations. The business is structured in such a manner that legal documents are not required to determine how profit-sharing from business operations will be allocated.

Quick Decision and Prompt Action: Nobody interferes in the affairs of the sole proprietary organization. So the owner can take quick decisions on the various issues relating to business and accordingly actions can be initiated at appropriate time.

Direct Motivation: In sole proprietorship form of business organizations, the entire profit of the business goes to the owner. This motivates the proprietor to work hard and run the business efficiently to maximize his profits. Profits from the business flow-through directly to the owner's personal tax return.

Minimal working capital required for start-up: The money required to meet the day to day expenses of the business is very less. The business can be started with a small amount of initial and working capital.

Flexibility in Operation: It is very easy to effect changes as per the requirements of the business as decision making power lies with only one person. The expansion or curtailment of business activities does not require many formalities as in the case of other forms of business organization.

Maintenance of Business Secrets: The business secrets are known only to the proprietor. He is not required to disclose any information to others unless and until he himself so decides. He is also not bound to publish his business accounts and share his investment and profit details.

Personal Touch: Since the proprietor himself handles everything relating to business, it is easy to maintain a good personal contact with the customers and employees. By knowing the likes, dislikes and tastes of the customers, the proprietor can adjust his operations accordingly and can build personal goodwill. Similarly, as the employees are few and work directly under the proprietor, it helps in maintaining a harmonious and one to one relationship with them.

Least expensive form of ownership: It is very easy and inexpensive to register the business under sole proprietorship. The process of its formation does not require any registration process and so it saves money at the initial establishment level. In case of partnership, a partnership deed is required and in case of a company, the full process of incorporation is mandatory which makes it expensive affair at the preliminary level only.

Regulatory burden is generally light: There are less number of regulatory bodies who control the working of sole proprietorship. Thus, one can work in an autonomous manner without any interference of the regulatory bodies. In case of partnership, it is governed by Indian Partnership Act 1932 and a company form of business organization is governed by Companies Act, 2013. There is no specific act which governs the working of sole proprietorship.

Tax advantages if your business is not doing well: The sole proprietorship business can lead to certain tax benefits in particular situations for example, deducting your losses from your personal income, and a lower tax bracket when profits are low. This is because the owner and the business are not treated as separate legal entity. Thus, business income becomes a part of the personal tax return filed by the sole proprietor.

MOTIVATION AND ENTREPRENEURSHIP DEVELOPMENT

Introduction

Motive refers to drive and motivation means drive to achieve a goal. Motivation refers to the way in which urges, drives, desires, aspirations, and strivings or needs direct, control or explain the behaviour of human beings.

Motivation is related with human behaviour. Motivation is a complex phenomenon. In general motivation is a psychological phenomenon as it is related to those factors operating within the individual employee which compel him to act or not to act in a certain way. These phenomena have been a subject of research by many people.

Characteristics of Motivation

1. Motivation is internal feeling of a person.

2. Motivation is a continuous process.

3. Motivation varies with person and time.

4. Motivation may be positive or negative.

What motivates an entrepreneur to undertake risk and start new enterprise? Is it financial scarcity or financial abundance which motivates an individual to start an enterprise? Is it the family, social status or satisfaction from present life that motivates an entrepreneur to start a new enterprise? The answer to such questions lies in the study of motivation.

Motivational factors involve the inner urge within an individual. Due to such an urge an individual is motivated to do something new, unique and perform better than others. :Research studies associated with finding an answer to the most important question as “To what makes an entrepreneur?” reveals the following important points.

1. Entrepreneurship is associated with personality.

2. Personality development is closely associated with early childhood experiences.

3. Economic deprivation also acts as a motivating factor.

4. Family environment plays an important role. In a family where security and non risk bearing situations are given importance, there are less chances of developing entrepreneurs, whereas family environments which foster venturing in to uncertain risky environment, tend to develop entrepreneurs.

5. Entrepreneurial characteristics are results of combination of various social, economic and psychological factors which are developed right from childhood.

Motivation Theories

Motivation acts as key to enterprise effectiveness. Motivation is originated from the word motive. Motive means want, need, impulse or drive. Motivation is internal to person. It varies from person to person and time to time. Motivation is on going process and may be positive or negative. There are financial and non financial motivation techniques which can be used by entrepreneur for effective functioning of the enterprise. Incentives directly or indirectly related with money are referred to as financial motivations. Money acts as important and most effective source of motivation. Salary and wages, bonus, leave with pay, medical and housing facilities, profit sharing, vehicle allowance etc are some of the examples of financial motivators which should be used by the entrepreneur for the employees of the enterprise. Non financial motivators are psychological in nature. Status, respect, prestige, participation, job enrichment, recognition, safety of job, responsibility, etc are examples of non financial motivators.

Many motivation theories have evolved over the passage of time. These theories can be grouped as follows

Theories of motivation

Content theories	**Process theories**	**Theories related with human nature**
1. Maslow's need hierarch theory. 2. Herzberg two	1. Vroom's theory of valence and	1. McGregor theory of X and Y. 2. Ouchi's theory Z.

factor theory. 3. McClelland theory of achievement, affiliation and power. 4. Alderfer’s theory of existence, relatedness and growth.	expectancy. 2. Porter and lower model of motivation. 3. Equity theory.	3. Contingency approach.

Maslow’s of theory holds that human needs form a hierarchy ranging from lowest order of physiological need, security need, social need, esteem need to highest order need of self actualisation. The theory suggests that various levels are interdependent and overlapping. Each higher level need emerges before the lower level need is completely satisfied. As the need does not disappear when other emerges, all needs tend to be partially satisfied in each area. When the peak of a need is passed, that need does not work as a primary motivator. The next level need then begins to dominate. Even though a need is satisfied it still influences behaviour due to interdependent and overlapping characteristics of need.

Fredrick Herzberg and his associate of case western reserve university has conducted research study by administering survey questions to 200 engineers and accountants in nine different companies in the Pittusberg, U.S.A. Based upon analysis of the information, two independent set of factors affecting human behaviour were found out. One set of factors operate primarily to dissatisfy employees when they are absent, however their presence does not motivate them in a strong way. They are referred to as hygiene factors. Another set of factors are responsible for strong motivation and high job satisfaction. They are referred to as hygiene factors. Hygiene factors found out by Herzberg include company policy and administration, technical supervision, interpersonal relationship with subordinates, salary, job security, personal life, working conditions and status. The motivation factors found out by Herzberg include achievement, recognition, advancement, work itself, possibility of growth and responsibility. The suggestion of Herzberg is to keep hygiene factors constant or higher while increasing motivational factors.

Important guidelines for motivation

1. The enterprise must consider human resources as the most valuable resource from among all the resources and give them respectable and honorable treatments.
2. Good quality working conditions should be maintained at the enterprise / factory place
3. Safety and health should receive topmost priority.
4. Adequate and fair salary structure should be provided to employees so as to maintain good standard of living.
5. Job security and enough opportunities to rise ahead in their careers should be given to employees.
6. Superiors should praise the subordinates when they deserve it.
7. Adequate tools and equipments should be provided to employees so as to perform their task effectively.
8. Proper feedback system should be implemented so that subordinates can come to know about their strengths and weaknesses.
9. The employees should be provided with opportunities to show their skills and creative instincts in work performance through giving them more freedom, encouraging their participation, implementing management by objectives and latest management concepts.
10. Principles of natural justice should be followed in handling grievances of employees. Full freedom should be provided to employees to express their problem.
11. Adequate training should be provided to the employees to develop skills and creative abilities of the employees.

Entrepreneurship Development Training Programme

Entrepreneurship development is one of the key elements for promotion of MSME sectors. To undertake this task on regular basis, the Ministry has set up three national level institutes. These are 1) National Institute of Micro, Small and Medium Enterprises, Hyderabad; ii) National Institute of Entrepreneurship and small Business Development, Noida; and iii) Indian Institute of Entrepreneurship, Guwahati. All would be entrepreneurs, can avail the multi-faceted training programmes geared for entrepreneurship cult which are tailor-made for their individual needs and application within the country. Various training programmes are organized on regular basis to cultivate the latent qualities in youths by enlightening them on various aspects that are necessary to be considered while setting up micro or small enterprises. These training programmes have attracted the attention of the educated unemployed youths and have created confidence in them which led to the self employment and creation of better employment. The individual MSME-DIs conduct the following training programmes:-

a) Industrial Motivation Campaign

b) Entrepreneur Development Programme

c) Entrepreneurship Skill Development Programme

d) Management Development Programme

e) Skill Development

f) Business Skill Development Programme

Patents, Trademarks, and Copyrights

1.1 Introduction

Welcome to SBA’s online training course: Patents, Trademarks, and Copyrights.

SBA’s Office of Entrepreneurship Education provides this self-paced training exercise as an overview of how to protect intellectual property and the steps you should take to safeguard your intellectual property.

You will find this course easy to follow and the subject matter indexed for quick reference and easy access. It will take about 30 minutes to complete the course. Additional time will be needed to review the included resource materials and to complete the suggested next steps at the end of the course.

Audio is used throughout the training, so please adjust your speakers accordingly. A transcript and keyboard shortcuts are available to assist with user accessibility.

When you complete the course, you will have the option of receiving a course completion confirmation from the SBA.

1.2 Course Objectives

The course has four key objectives:

- One, explain the importance of protecting your intellectual property
- Two, determine the differences between patents, trademarks, and copyrights
- Three, list examples of times when you would file for a patent or trademark, or register for a copyright
- Four, identify parts of the process of filing for protection

1.3 Course Topics

This course will focus on three common areas of intellectual property. They are:

- Patents
- Trademarks, and
- Copyrights

For a small business owner, it is important to know what intellectual property can be protected and how to take the necessary steps to get it protected. This course will be a stepping stone to learning these necessary actions.

Let’s get started!

1.4 Background

As an entrepreneur or an aspiring small business owner, you need to protect your ideas, business name, logo, inventions, and other work products that give your business a competitive edge in the market. In today’s competitive market, it is highly possible that other businesses or individuals are copying your intellectual properties for their own benefit, thereby threatening your growth.

1.5 Intellectual Property

Intellectual Property encompasses a variety of rights and items owned by small businesses. You can safeguard your intellectual property with the help of laws that grant you certain time-limited rights to control the use of your intellectual goods and services.

These laws or rights include Patent, Trademark, and Copyright. Click each button to learn more.

Patent

A patent is a property right recognized by the Government of the United States of America to an inventor for a limited time **—**to exclude others from making, using, offering for sale, or selling the invention throughout the United States or importing the invention into the United States‖ in exchange for public disclosure of the invention when the patent is granted.

Trademark

A trademark is a word, phrase, symbol, or design, or a combination of words, phrases, symbols, or designs, that identifies and distinguishes the source of the goods of one business from those of others.

Copyright

A copyright protects works of authorship, such as writings, music, and works of art that have been tangibly expressed.

1.6 Types of Patents

Let’s now learn more about patents. There are three types of patents:

- **Utility patents**, which protect the ownership of an invention or discovery of a new and useful process, machine, article of manufacture, or composition of matter or any new and useful improvement of those items
- **Design patents**, which protect the ownership of a new, original, and ornamental design for an article of manufacture
- **Plant patents**, which protect the ownership of any distinct and new variety of plant that was invented or discovered and asexually reproduced

1.7 Patent Laws

Patent laws help you safeguard your intellectual properties. These laws can specify the methods for obtaining a patent and the conditions of the patent. In the U.S., patent laws are governed by the United States Patent and Trademark Office (USPTO).

1.8 What Can Be Patented?

Almost anything and everything that is made by man and the processes for making the products can be patented.

You can patent the following:

- A process which is defined by law as a process, act, or method and primarily includes industrial or technical processes
- A machine which has parts or certain devices or a combination of devices

- A manufacture, which refers to articles that are made and includes all manufactured articles, and
- A composition of matter which relates to chemical compositions and may include mixtures of ingredients as well as new chemical compounds

1.9 Conditions for Obtaining a Patent

You need to meet the following requirements in order to obtain a patent:

- The invention you want to patent shouldn't already be known or used by others in the U.S.
- Your intellectual property shouldn't have been described in a printed publication in any country before the application for patent, and
- Your intellectual property shouldn't have been in public use or sale in the U.S. for more than one year prior to the application for patent

1.10 Who May Apply for a Patent?

Next, let's look at who may apply for a patent.

You may apply for a patent if you are:

- An inventor or a co-inventor
- An executor of an estate, or
- A legal representative of an inventor

1.11 Application for Patent

Your patent application should include:

- A written document
- Drawings, if necessary
- An oath or a declaration, and
- Filing, search, and examination fees

Click each puzzle piece to learn more.

A written document

The specification should have the following sections in order:

1. Title of the invention
2. Cross-reference to related applications (if any). Related applications may be listed on an application data sheet, either instead of or in addition to being listed in the specification
3. Statement of federally sponsored research or development (if any)
4. The names of the parties to a joint research agreement if the claimed invention was made as a result of activities within the scope of a joint research agreement
5. Reference to a ‖Sequence Listing,‖ a table, or a computer program listing appendix submitted on a compact disc and an incorporation by reference of the material on the

compact disc. The total number of compact discs, including duplicates, and the files on each compact disc shall be specified

6. Background of the invention
7. Brief summary of the invention
8. Brief description of the several views of the drawing (if any)
9. Detailed description of the invention
10. A claim or claims
11. Abstract of the disclosure
12. Sequence listing (if any)

Drawings (if necessary)

In most cases, drawings or images can be helpful or even required for the granters to understand the intervention.

The drawing must:

- Show every feature
- Be in a particular format which meets the specifications on:
    - Ink
    - Color
    - Forms
    - Margins
    - Views
    - Scales
    - Shading, and
    - Symbols

An oath or a declaration

An oath or a declaration of the applicant is required, and the applicant may be asked to answer questions about the invention.

It must be signed with full first and last names, and middle initial or name. You must also include the details of your citizenship.

Filing, search, and examination fees

- There are basic and additional fees that are required when filing for a patent.
- Fees are subject to change every October.
- If you are a small entity, your fees may be reduced in half.

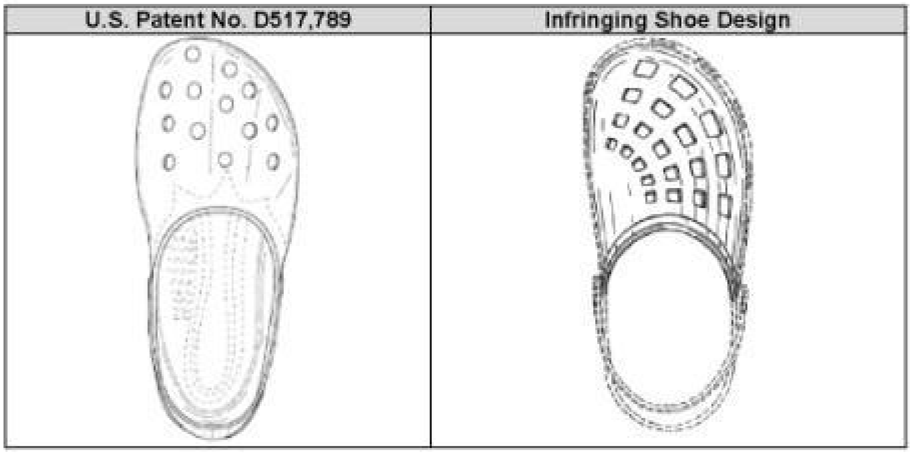
1.12 Application for Patent (cont'd.)

When you have a good product, people will want to imitate it. Therefore, it is crucial to protect your products and other business items. Here's a case study that illustrates how important it is to obtain patents for your intellectual property.

Click the Case Study button to learn about the importance of patenting your intellectual property.

Case Study

The Accusation:



Can You Recognize the Shoe?

The company Crocs, started in 2002, paved the way for a foam shoe intended for outdoor and boating use.

Other people thought it was a good idea and started copying the design. They sold the copycat shoes at large retail stores, such as Wal-Mart and K-Mart.

What Happened?

Crocs sued. The judge found the copycat shoes to be a case of infringement because they were too similar to Crocs.

The Importance:

When you have a good product, people will want to imitate it. Be sure you have guarded your brand and product properly, as Crocs did.

1.13 Trademarks

Next, let's look at trademarks and how to secure your intellectual property by registering your trademark.

To start, let's look at what trademarks are and how to register them.

A trademark includes a word, name, device, or any combination of them to be used to identify and distinguish the goods and services of one seller or provider from those of others and to indicate the source of goods and services. It is essentially your brand.

1.14 Trademarks—Initial Considerations

Registering a trademark is not required in the U.S.; however, there are benefits to obtaining a trademark registration officially. Trademarks are territorial. Unlike the United States, most countries require registration of trademark rights.

If you decide to register officially with the U.S. Patent and Trademark Office, before starting the initial process, make sure you have thought through:

- The mark you want to register
- The goods or services in connection with which you wish to register the mark in the future, and
- Whether you will be filing the application based on actual existing use of the mark or a bona fide intention to use the mark in the future

1.15 Registering Your Trademark

Registering your trademark involves steps such as:

1. Identifying Your Mark
2. Identifying Your Goods/Services
3. Identifying the Proper Basis
4. Filing a Trademark Application
5. Remitting the Fees
6. Monitoring Your Status
7. Protecting Your Rights

Click each step to learn more.

Identifying Your Trademark

Your representation of your trademark must be extremely clear.

The three possible trademark formats available are:

- Standard character format
- Stylized/Design format
- A sound mark

For more information, visit: http://www.uspto.gov/trademarks/basics/mark.jsp

Identifying Your Goods/Services

Once your mark is chosen, you will need to identify very specifically the goods or services to which the mark applies.

Identifying the Proper Basis

Before filing, you must demonstrate that you have used your mark in commerce. You can file under either ―"use in commerce" basis or "intent to use‖ basis.

"Use in Commerce" Basis

You may file under this basis when you have already used your mark in commerce. There is no need for filing additional forms or fees prior to registration.

"Intent to Use" Basis

You may file under this basis when you plan to use your mark in the future. It requires filing an additional form and fee prior to registration.

The main difference between these two is whether or not you use the mark on ALL the goods or services identified in your application.

Filing a Trademark Application

The two ways to file your application are:

- Via online using Trademark Electronic Application System (TEAS). For more information, visit: http://www.uspto.gov/trademarks/basics/online_filing.jsp
- Using paper forms (you may contact the Trademark Assistance Center at 1-800-786-9199 (1-571-272-9250) for a paper form)

Remitting the Fees

The fees for filing will be based on following factors:

- Number of marks
- Number of classes
- The version of the form being used

Monitoring Your Status

You will want to check the status of your application after the initial filing, based on the following criteria.

- What?—To keep up with the timelines for filing post-registration documents, you need to follow up the status of your application.
- Why?—Failure to follow up may result in late submissions and as a result, denial of your request for reconsidering the application.
- When?—You should check the status of your application every 3 to 4 months after the initial filing of the application.
- How?—You can check the status via Trademark Search and Document Retrieval system.

Protecting Your Rights

You are the only policeman for your marks. The United States Patent and Trademarks Office does not enforce your rights against others once you receive registration.

It will be up to you to bring any legal action to stop a party from using an infringing mark.

1.16 Copyrights

Today, the distribution of copyrighted work has never been easier. However, nowadays, reserving intellectual property rights is made much easier than in the past because of technological advances online.

Small businesses should be aware of copyright and copyright ownership issues when doing business.

1.17 Examples of Copyrighted Material

Copyrighting is a legal protection for the creators of original work. It can protect the following intellectual properties:

- Literary works
- Musical works
- Dramatic works
- Pantomimes and choreographic works
- Architectural works
- Pictorial, graphic, and sculptural works
- Motion pictures and other audiovisual works
- Sound recordings, and
- Computer programs

1.18 Business Materials Protected

All businesses have some form of materials that could be protected by copyright.

Common examples include:

- Brochures and catalogs
- Magazines
- Advertisements
- Blogs
- Logos, and
- Web sites

1.19 Copyright Benefits

Once your material is copyrighted, you have the right to do, or authorize others to perform, the following tasks with the copyrighted work:

- Copy
- Change
- Distribute publicly, and
- Perform or display the work publicly

1.20 Getting a Copyright

Copyright protection is less formal than obtaining a trademark or patent.

A creative work is considered protected by copyright as soon as it exists if it is original or is a Fixed in a Tangible Form.

Click each requirement to learn more.

Original

To be ―Original, the work has to be independently created by the creator and have some minimal degree of creativity. "Independently created‖ simply means that the work must be the independent product of the author and not copied from someone else's work. A work can be original without being novel or unique.

Fixed in a Tangible Form

To be ―fixed in a tangible form,‖ the work has to be sufficiently permanent or stable to permit it to be perceived, reproduced, or otherwise communicated for a period of more than transitory duration. It makes no difference what the form, manner, or medium of expression is.

1.21 Ownership

The creator of a work is considered the author and owner of the copyright. However, there are exceptions to this rule.

Make sure to clarify who owns the intellectual property and what types of work are covered in contracts.

For example, contract graphic artists and web-site designers own copyrights in the commissioned work in the absence of a written transfer of the copyright.

1.22 How Long Will the Protection Last?

The validity of intellectual property may vary depending on the country. But in the U.S., a copyright is protected for the life of the creator and an additional 70 years or 95 years from the creator's publication or 120 years from creation of the work, whichever is shorter.

A patent is usually protected from 14 to 20 years, depending on the type of patent.

A trademark usually lasts as long as it is being used in commerce and defended against infringement.

1.23 Protection Outside the United States

Patents and trademarks are territorial. So if you are seeking protection outside the country in which you originally registered, you will need more than just the U.S. protection.

Click each button to learn about protection outside the U.S.

Copyright Protection

- Most countries do not require you to register in order to be protected. However, registration can offer several benefits. While the U.S. honors relationships with most countries when it comes to copyrights, you will want to double-check if you are concerned about a particular country.
- For more information, visit: http://www.copyright.gov/circs/circ38a.pdf

Patent Protection

- The Patent Cooperation Treaty (PCT) is an international filing mechanism that permits a single applicant to file for some or all of 146 countries.
- The creator must request examination in each country under the PCT in order to be evaluated for a patent in the specific country.

Trademark Protection

- Filing for trademark protection in other countries can also be a one-stop shop. This is facilitated with the help of the Madrid System, which offers the owner to have the trademark protected in many countries by filing one application directly with his/her own national or regional trademark office.

1.24 Summary

This course focused on getting your intellectual property protected as a small business owner. It shed light on three categories: patents, trademarks, and copyrights. Hopefully, you now know what can be protected and how to take the necessary steps to get it protected.

Specifically, you learned how to:

- Explain the importance of protecting your intellectual property
- Determine the differences between patents, trademarks, and copyrighted material
- List examples of times when you would file for a patent or trademark, or register for a copyright
- Identify parts of the process in filing for protection

More information can be found online at www.USPTO.gov or in the resources of this course.

1.25 Next Steps

Much material has been discussed in this course. The instructional part of the program is complete. It is now up to you to apply what you have learned. This is the most important part of the course.

Consider taking these next steps to protect your intellectual property:

- Step 1 – Figure out what protections you need to apply for. You can apply for a patent, trademark, or copyright
- Step 2 – Research existing protected work to ensure that the work or idea you are planning to protect is not already protected or to discover whether your work meets the basic requirements for obtaining protection
- Step 3 – Fill out the paperwork or register for a patent, trademark, or copyright
- Step 4 – Wait for a response for your application

1.26 Resources

SBA has a broad network of skilled counselors and business development specialists. Below is a short description of our resource partners:

- **Small Business Development Centers (SBDCs)** are associated with institutions of higher education—universities, colleges, and community colleges. More than 900 SBDCs offer no-cost, extensive, one-on-one long-term professional business advising, low-cost training, and other specialized services, such as procurement, manufacturing, and technology assistance, which are critical to small business growth.
- **SCORE** offers free, confidential small business advice from successful entrepreneurs. SCORE is a nationwide program and boasts more than 12,000 volunteers to give you guidance to grow your business.
- **Women's Business Centers (WBCs)** provide free management and technical assistance to help women and men start and grow small businesses. There are over 100 WBCs located throughout the U.S. and Puerto Rico.

- SBA's 84 **District and Branch offices** connect entrepreneurs to resources, products, and services that can help them start, manage, and grow their business. These offices are located in all 50 states, Puerto Rico, the U.S. Virgin Islands, and Guam.
- The **SBA Learning Center** is an online portal that hosts a variety of self-paced online training courses, quick videos, web chats and more to help small business owners explore and learn about the many aspects of business ownership. Content is filtered by topic, so no matter the stage of your business, or the kind of insight you need, you can quickly get answers.

Find your local resource using our handy ZIP-code tool: www.sba.gov/local-assistance

1.27 Have a Question?

- Call SBA at 1-800 U ASK SBA (1-800 827-5722)
- E-mail SBA at answerdesk@sba.gov
- Locate a SCORE counselor, SBA district office near you, or an SBDC office near you atwww.sba.gov/local-assistance
- To provide feedback, comments, or suggestions for other SBA online content, please use the following email: learning@sba.gov

1.28 Certificate

Congratulations on completing this course. We hope it was helpful and provided a good working knowledge of what intellectual property can be protected, and how to protect it by obtaining patents, trademarks, and copyrights for intellectual property. Click the certificate to receive a course completion confirmation from the U.S. Small Business Administration.

2. Recommendations

A.C.T. NOW!

The Article, Course and the Tools below are related to the course you just completed. They are provided to help you take action on your path to entrepreneurial success. You can also get in-person assistance for all of your business needs through a local resource center. And if you liked the course, please help spread the word by sharing it with your friends!

Click here to share on Twitter
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Read an SBA Article.

Small Business Patents, Copyrights and Trademarks, offers more information and resources for the small business community.
LINK: http://1.usa.gov/1oGMcHF

Take Another Course.

The *Financing Options for Small Businesses* Online course helps you to determine your financial needs such as loans, grants, venture capital, angel investors, crowd funding and other options available to small businesses.
LINK: http://1.usa.gov/1inDVW8

Try a Tool.

The U.S. Patent and Trademark Office offers a downloadable *Patent Calculator Tool* that can help estimate the expiration date of utility, plant, or design patents.
LINK: http://1.usa.gov/1kYfdL0

Find local assistance!

SBA has a broad network of skilled counselors and business development specialists.

LINK: http://1.usa.gov/1kihdhJ

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Clarifying the concept of product-service system

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Abstract

A new trend of product-service systems (PSS) that has the potential to minimise environmental impacts of both production and consumption is emerging. This article attempts to build a theoretical framework for PSS and serves as a background for identifying possible investment needs in studying them. There are three main uncertainties regarding the applicability and feasibility of PSS: the readiness of companies to adopt them, the readiness of consumers to accept them, and their environmental implications. The main finding is that successful PSSs will require different societal infrastructure, human structures and organisational layouts in order to function in a sustainable manner.

Keywords**: product-service systems, sustainability, functional economy**

1 Introduction

Sustainable production and consumption is an issue of current international concern. Many different approaches and concepts have been developed over the last decades to address environmental problems, such as cleaner production, cleaner technologies, waste minimisation and recycling approaches, eco-design and design for sustainability. However, a new strategy is called for in order to stimulate the change in current production and consumption patterns.

Rising levels of consumption by the rich and doubling of the world's population over the next 40–50 years would require a factor 4 increase in food production, a factor 6 increase in energy use and at least a factor of 8 of growth income [1]. It is estimated that by the middle of the century, resource productivity must have improved by a factor of 10.[1] This can be done by reducing the population, lowering the level of consumption or changing technology. The first option does not seem to be feasible in the short term. Decreasing consumption levels do not appear to be a simple option either because, on the one hand, people from industrialised countries do not show any obvious willingness to minimise consumption and, on the other hand, there is a need to increase consumption levels in developing countries just to provide basic amenities.

Recent thinking has focused on "dematerialising" the economy—reducing the material flows in production and consumption; creating products and services that provide consumers with the same level of performance, but with an inherently lower environmental burden. Several authors have proposed the concept of product-services—providing utility to consumers through the use of services rather than products—as a possible example of a strategy for

[1] This means reduced by 90% compared to current levels.

dematerialisation and a possible answer to the sustainability challenge. However, so far, little attention to this concept has been given at policy and operational levels.

The aim of this article is to contribute to building a theoretical background about the concept, and to stimulate debate about the sufficiency of existing efforts at academic and company levels.

2 Functional economy

At the turn of the millennium we are witnessing an escalation of service economies with society experiencing a transition from mass-production to flexible production. A service economy is defined as one in which more than half of the total labour force is employed by the service sector [2]. Approximately 70% of all workers in highly industrialised countries are employed in industries commonly thought of as services: communications, transportation, health care, wholesale and retail redistribution, and financial services. This new, more service-oriented model of manufacturing growth has key competitive factors such as the capability for continuous innovation, improved design and quality and customised goods, rather than the production of large volumes of standardised products.

What are the drivers of such structural change in our society? Some of the shifts in composition of output and employment depend, of course, on demographic factors. The environment itself has become a force for structural change. The industrial revolution, which shaped the development of the 20th century, worked by its own rules, at odds with those of the natural world. Resources were viewed as inexhaustible and the ecosystem as an infinite "sink" for wastes. As the troubling symptoms of environmental decline have emerged, fundamental questions have been raised about the environmental profile and sustainability of existing industries. However, services have generally escaped this critical concern, being considered as less environmentally harmful.

Services have increased in share within the manufacturing industry [3]. The traditional boundary between manufacturing and services is becoming increasingly blurred. Of the employees that are working in traditional manufacturing industries, 65 to 75% perform service tasks ranging from production-related activities like research, logistics (transportation), planning, and maintenance, as well as product and process design, to the all-supportive services existing at any company (e.g., accounting, financing, law services and personnel functions).

The role of services in providing value is ever more important. Not long ago, most of a product's added value came from the production processes that transformed raw materials into products. Now added value is created by technological improvements, intellectual property, product image and brand names, aesthetic design and styling; all nonmaterial aspects of products. These help producers to differentiate and diversify their products to better respond to customers' demands—the so-called move from mass production to customised production or mass customisation. Therefore, there is an increased interest among manufacturers in adding value through the provision of services that extend the spectrum of their products. Thus "services" extend into every part of the value chain.

The concept of a service society as a means of achieving sustainable development was proposed by Stahel [4]. He advocated the need to distinguish between

industrial economy and service-oriented economy. Industrial economy places the central value on the exchange of the products that are consumed. The service economy, on the contrary, recognises the value of utilisation, a performance driven orientation where the consumer pays for utilisation of the product. Therefore, the service economy is often referred to as functional economy, in which both product and technology are mere modes of providing function. The idea of functional economy rests upon the notion that function is the key to customers' satisfaction, not products per se. In a functional economy consumers are buying mobility instead of cars, cleaning services instead of washing powders and movies instead of videocassettes [5], [6], [7]. A functional economy has the potential to be more environmentally benign because it addresses current levels of material/resource consumption, seeking options that may provide function/service to consumers without minimising their level of welfare. But realisation of this potential is not automatic.

In a functional economy, the role of the manufacturer is shifted towards provision of services [8]. Stahel notes that a functional economy "optimises the use (or function) of goods and services and thus the management of existing wealth (goods, knowledge, and nature). The economic objective of the functional economy is to create the highest possible use value for the longest possible time while consuming as few material resources and energy as possible"[9]. In the functional economy, material products are treated as capital assets rather than as consumables, thus increasing value-added services to prolong the product's life and minimise loss of resources.

Present economies are mostly service economies saturated with products reinforced by services and some examples of alternative systems of product use. Empirical studies have indicated that even in industrialised countries with a high level of consumption, the penetration of new products and services is of more complementary nature rather than substitutional [10].

3 What is a product-service system?

The term "product-service systems" has been defined as "a marketable set of products and services capable of jointly fulfilling a user's need. The product/service ratio in this set can vary, either in terms of function fulfilment or economic value"[11]. Thus, more traditional material intensive ways of product utilisation are replaced by the possibility to fulfil consumers' needs through the provision of more dematerialised services, which are also often associated with changes in the ownership structure. Various approaches and trends towards the development of PSS can be outlined:

- **the sale of the use of the product instead of the product itself [12],**
- **the change to a "leasing society"[13],**
- **the substitution of goods by means of service machines [14],**
- **a repair-society instead of a throw-away society [15],**
- **the change in consumer attitudes from sales to service orientation.**

Jansen and Vergragt have been working on the concept of sustainable product systems that crosses company boundaries and includes all stakeholders in the process [16]. Manzini proposes the idea of strategic design as a new approach for companies to engage in an increasingly "turbulent" market. Strategic design focuses the design process on an integrated body of products, services and

communications, as a model for companies to address changes in technology and social and consumer attitudes [17].[2]

Aforementioned efforts obviously provide only parts of the solution. Each of these approaches is a separate element of a PSS, with its own strong and weak sides and limitations and possibilities to minimise environmental impact. However, when one is to integrate them into a system, sub-optimisation might occur and overall environmental impact might not necessarily be reduced. Therefore, there is a need for a product-service system, where the main focus on system solution is important. Understanding the difference between service and product is not relevant from an environmental point of view, since both generate environmental impacts. The challenge with the new approach lies in developing system solutions, where bits and pieces fit together, integrated into a system of people satisfaction. Such system-based solutions should facilitate the shift from separate systems of producing and consuming to a system, in which products, services, supporting infrastructure, and necessary networks are designed so that to provide a certain quality of life to consumers and, at the same time, minimise environmental impacts of the system.

Thus, a product-service system should be defined as a system of products, services, supporting networks and infrastructure that is designed to be: competitive, satisfy customer needs and have a lower environmental impact than traditional business models.

For consumers, product-service systems mean a shift from buying products to buying services and system solutions that have a potential to minimise the environmental impacts of consumer needs and wants. This requires a higher level of customer involvement and education by producers.

For producers and service providers, product-service systems mean a higher degree of responsibility for the product's full life cycle, the early involvement of consumers in the design of the product-service system, and design of the closed-loop system.

For both consumers and producers, product-service systems might sometimes involve a change in property rights. In general, product-service systems are likely to give more attention to the use phase of the product's life cycle (consumer stage), than current product systems do.

A *paramount goal of product-service systems* should be to minimise the environmental impact of consumption by:

- closing material cycles;
- reducing consumption through alternative scenarios of product use;
- increasing overall resource productivity and dematerialisation of product-service systems;
- providing system solutions seeking the perfection in integrating system elements along with improving resource and functional efficiency of each element

The concept of a product-service system in this interpretation is still theoretical. Examples of some PSS elements can be found in some companies, mainly driven by business and economical considerations, and therefore, environmental potential of such PSS elements has not been yet evaluated.

4 Why a product-service system?

[2] See also the development of this idea in the handbook of the Masters of Strategic Design, Politechnico di Milano (www.mip.polimi.it/mds).

4.1 Benefits

The PSS concept has the potential to bring about such changes in production and consumption patterns that might accelerate the shift towards more sustainable practices and societies. According to some authors, the concept might be promising for commercial companies, governments, and customers [18].

For companies

Understanding PSSs provides the opportunity to see strategic new market opportunities, market trends and developments and potentially to stay competitive as patterns of production and consumption are transformed by environmental limits. The concept of a product-service system facilitates innovation at a more than incremental level and has the potential to bring financial benefits.

Some companies are employing elements of product-service systems as a natural extension of their existing offers to customers. Others see it as a survival strategy where the application of a PSS is seen as the centre of a new business plan. Usually such companies are forerunners and see the opportunity of being first on the market as a basis for survival.

There are different benefits to developing a PSS for manufacturing and service companies.

For manufacturing companies **a service component adds/allows:**

- To attach additional value to a product, for example, financial schemes or refurbishing or upgrading.
- To base a growth strategy on innovation in a mature industry.
- To improve relationships with consumers because of increased contact and flow of information about consumers' preferences.
- To improve the total value for the customer because of increased servicing and service components, which include activities and schemes that make the existing product last longer, extend its function (upgrading and refurbishment), and make the product and its materials useful after finishing its life cycle (recycling and reuse of parts or entire product).
- To anticipate the implications of future take-back legislation, and might have the potential to turn them into a competitive advantage.

For service companies**, product components:**

- Extend and diversify the service.
- Safeguard market share by bringing the service component into the offer that is not so easy to copy.
- Facilitate communicating product-service information, because it is easier to convey information about more tangible products than about intangible services [19].
- Safeguard a certain level of quality that is difficult to change (product quality).

For government and society

Understanding PSSs can therefore help to formulate policies that promote sustainable patterns of consumption and sustainable lifestyles. PSSs have the potential to offer a new way of understanding and influencing stakeholder relationships and viewing product networks, which again may facilitate development of more efficient policies.

At the same time, it is expected that the promotion of added services or substitutes of products and alternative schemes of product-service use can assist in the creation of new jobs. The functional economy might be more labour-intensive than an economy based on mass production and throwaway patterns of consumption. More jobs per unit of material product might be created because of such labour-intensive services as take back systems, repair, refurbishment, or disassembly. With time, however, these services might become large-scale operations that will require automatisation, and which will decrease employment.

For consumers

Consumers benefit from a product-service system because they receive greater diversity of choices in the market; maintenance and repair services; various payment schemes; and the prospect of different schemes of product use that suit them best in terms of ownership responsibilities. Consumers get added value through more customised offers of a higher quality (from the product/service per se and the delivery/provision). The service component, being flexible by nature, induces new combinations of products and services, better able to respond to changing needs and conditions. Consumers may be relived from the responsibility for a product that stays under ownership of a producer for its entire life span. Through product-service systems consumers might more easily learn about environmental features of products and how they can contribute to minimising the environmental profile of consumption.

For the environment

A PSS has the potential to decrease the total amount of products by introducing alternative scenarios of product use, for example, sharing/renting/leasing schemes to consumers, however, not affecting design of the products. With PSS, producers become more responsible for their product-services in case material cycles are closed. Producers are encouraged to take back their products, upgrade and refurbish them and offer them again. In the end, less waste is incinerated or landfilled.

The PSS approach changes the price cost systems of the present economy because "the costs of production are only a very small part of the costs involved in making a product available to the customer" [20]; consumers pay not for material goods but for intangible services. This can amplify the technical development of dematerialisation, which is already an on-going process [21].

4.2 Drivers

The drivers for the development of PSS have largely been canvassed in previous sections. Product-service systems more appropriately respond to the demands of today than existing systems of mass production. This is an evolution of the economic transition away from standardised and mass production towards flexibility, mass-customisation and markets driven by quality and added value rather than cost. Core competencies, rather than physical assets, increasingly define leadership of companies on the market.

Improved competitiveness through improved environmental performance is also named among the drivers of the shift from selling products to provision of services. Others include legislative threats, particularly relating to extended producer responsibilities (EPR), and consumers behaviour/demands [22].

There are certain conditions under which development and application of PSS might be profitable [18]. First of all, PSS will be profitable if the costs of use and

disposal phases (and the collection of end-of-life products) are internalised. The development of a proper PSS with an efficient take back system could stimulate consumers to return products. Second condition is if the product at the disposal stage has a high market value. The third condition of a profitable PSS is when an alternative scenario of product use generates additional profit (or reduces a current cost). For example, the legislation requires that a producer of a chemical takes care of her/his chemicals after they are sold. In this case product "maintenance" becomes an additional cost. If the producer, instead of selling the chemical, provides its function, it becomes a profit generator and a stimulus to minimise the consumption of the chemical, which is beneficial for the consumer as well. Thus, it appears that one of the most important external drivers for a company is supplier development.

5 PSS elements

The study of literature on product-services and eco-efficient services, and communication with experts and researchers working with PSS revealed a clear lack of common understanding of PSS elements. The following figure provides a list of the main PSS elements, which may provide a common term of reference for studying and designing product-service systems (Figure 1).

1. A product-service system may consist of products, services, or their combinations. Products substituted by services is largely an ideal category without many practical or consistent examples, because any service, even nonmaterial per se, requires material or energy input.
2. Services at the point of sale comprise personal assistance in shops, financial schemes provided to customers, explanations about product use and, of course, marketing.
3. Different concepts of product use consist of two categories: use oriented, where product utility is extracted by the user, and result oriented, where product utility is extracted by the utility provider for the user.
4. Maintenance services include servicing of products with the goal of prolonging product life cycle, comprising maintenance and upgrading.
5. Revalorisation services include offers that aim at closing the product material cycle by taking products back, secondary utilisation of usable parts in new products, recycling of materials if reuse is not feasible.

Thus, product-service systems consist of a combination of eco-designed products, reinforced by designed services at different stages of a product's life cycle, and comprising different concepts of the product use (both use and result oriented, depending on the logistics and ultimately environmental profile of the product-service system), closely involving final consumers and actors in the chain and beyond.

6 Characteristics of PSS systems

6.1 The role of producers

The successful development of a product-service system requires that manufacturers and service providers extend their involvement and responsibility to phases in the life cycle, which are usually outside the traditional buyer-seller relationship, such as take back, recovery, reuse and refurbishment and remanufacturing. Usual responsibilities for products are extended through the additional or deepened responsibility for service, including the responsibility for

proper organisation of take back arrangements and systems for reuse, remanufacturing and recycling and for educating consumers about efficient product use. Reduced material flow also requires a stronger co-operation with suppliers. Information and economic benefits from the service provision stage (consumer stage) can be easily transferred to the manufacturing, development/design stage, thus the entire system becomes more responsive to changing market parameters and is probably inherently more likely to stimulate innovation.

6.2 The role of consumers

The relationship between the company and a customer plays a key role if the product-service systems are to be designed and run effectively. Some proactive companies have started working more closely with their customers, who then have depended on them for many types of information, including environmental. In turn, these companies often have early insights into consumer tastes, preferences and regional buying habits. Thus, such companies play a critical role in both satisfying and creating consumer preferences for goods and services, including their environmental dimensions.

6.3 Organisational basis for PSSs

Companies that are pursuing the concept of product-service systems will need to change traditional structures, regardless of whether they are manufacturing or service organisations. Close co-operation with consumers extends the role of the marketing division. Information management will play an increasing role in improving organisational efficiency and customer communication. As product-service development occurs during interaction with the consumer, the structure of decision making is likely to be more decentralised.

The extended involvement of the organisation with other companies leads to intra-organisational changes that include performance indicators and the demand for human capital. These intra-organisational changes modify the relationships between the business functions within the company. Inter-organisational changes, such as a closer interaction with other actors in the product-service chain and outsourcing, may create the demand for intermediates.

New networks may need to be established in order to develop product-service systems. These can be research networks that can investigate market changes and consumer preferences; information-sharing networks developed to share information that is relevant for entire product chain or industry sector; or regional or sectoral networks that bring together industries located in the same region or representing the same sector to exchange the best practices, set levels of performance or exchange by-products or wastes.

6.4 Design particularities

There are few existing examples of design projects/attempts where an entire product-service system is being designed. The design methodology of the entire product-service system will probably differ from the product design methodology due to the number of reasons:

- **Designing a PSS requires close integration of all actors within the life cycle of a product-service. Tight integration, especially between the service and**

manufacturing organisations, is more likely to permit the clear "transmission" of the economic incentives, allowing service activities to drive manufacturing or design changes.

- **Schemes for taking back products at the end of their life, as well as all necessary arrangements with business partners, should be focused on ensuring maximum closing of the product flow and reduction of transport distances.**
- **Alternative scenarios of product use could be analysed and the range of these scenarios may be presented to the consumer, providing information on economic and environmental features of offers.**
- **Marketing strategies could be developed in ways that teach and promote an environmentally and socially more acceptable way of function fulfilment. They could include communication campaigns during which the producer would provide consumers with information and presentations about utilising her/his products most efficiently.**
- **Alternative scenarios of servicing the products could also be given at the point of sale to ensure the proper product exploitation during the use phase.**

6.5 Environmental profile

Services are not necessarily less environmentally problematic than manufacturing industries, but in an economy in which they dominate and serve as some of the most dynamic drivers of change, it is important to examine them directly in search for opportunities to halt environmental degradation and to improve their environmental quality. PSSs are focused on addressing the use phase to reduce the total environmental burden of consumption. However, there is a need to consider carefully the impact of other phases such as production and post-production activities.

What are the possibilities to reduce environmental burden with a PSS? The following can be deduced from the discussion so far:

- **The environmental impacts of the use phase come from the efficiency of each unit of function delivered and the total amount of a delivered service. The design of product-service systems can provide an incentive to manufacturers to design products that are more efficient in their use phase only when the producer will be paying for the environmental effects and resource consumption during this phase, that is, when the conditions internalise use-related environmental costs.**
- **A number of economic advantages can arise from the sale of services. For instance, it may encourage the producers' interest in the reuse and increase of the recyclability rate of products. The services could include new, used and refurbished products. Ideally, this could lead to completely closed product cycles under the responsibility of the manufacturers.**
- **The substitution of energy and materials with efficiency services may influence overall resource consumption. Increasing the intensity of use, if products are shared or used jointly, may potentially minimise the total number of products and the capacity for use can be more fully realised resulting in greater resource efficiency and less impact on the environment.**
- **If the operation of the product-service is a cost for the company that has internalised it, the producer might be interested in providing maintenance that helps to extend product life and thus reduce the quantity of the product required for delivering the service that is less product per unit of services and thus less environmental burden.**

In order to assess the environmental performance of product-service systems, there is a need to develop criteria that could reflect the life span of a product, efficiency of resource consumption, closed cycle efficiency, and potential for improvement.

7 Barriers for PSSs

The concept of product-service systems is still being developed, but has already been suggested as a possible scenario of moving towards more sustainable production and consumption systems. It, therefore, is important to examine all conceivable barriers to its development, application and continuous betterment.

- **It may be difficult to develop scenarios of alternative product use because they often include elements that are situated between production and consumption (sales) and several stakeholders may need to be involved in designing both the product and the service system.**
- **A social system or infrastructure that would accept or support the suggested product-service scenario should be found. If such a system does not exist, a completely new infrastructure or network might need to be designed that can support the environmentally benign performance of the new product.**
- **Product-service systems require from their producer close co-operation with suppliers and service producers or final consumers. While relationships with suppliers are addressed by ISO 14000-series standards and environmentally conscious purchasing practices, downstream practices are addressed by EPR and Product Stewardship concepts. Integrated Chain Management specifically addresses the issue of involving several actors in order to improve the environmental performance of products. However, problems associated with ICM are also going to be relevant for PSS due to similar value chain basis, that is extended in PSS into a value network. These problems include trade-offs between co-operation and internal environmental management; the problem of choosing wrong actors who do not have the power to change or influence events; information sharing and transparency, and barriers from material flows crossing borders and a variety of regulatory frameworks in different countries.**
- **Although, ideally, ownerless consumption offers many advantages and hopes, it has its own problems. For instance, studies conducted so far show that the multiple use does not automatically lead to less impact on the environment [23]. The environmental impact depends, to a large extent, on the circumstances, schemes and conditions of use. Leasing, for example, can promote use of products which otherwise would not be affordable for customers. Without the option of leasing, the purchase could have to be postponed to a later date. On the other hand, leasing can facilitate the return of old appliances since the duration of use is monitored and they are returned after the lease has run out, if the purchase option is not executed. This could strengthen the manufacturers' interest in their own products and would thus considerably improve the economic conditions for a closed-cycle economy.**
- **Changing systems and sources of gaining profit could deter producers from employing this concept. Where point-of-sale becomes a point-of-service that operates over an extended period of time, traditional incentives can fail to reflect the real drivers of profit for the firm. A particular problem is the changeover from short-term profit realisation at the point-of-sale to medium- and long-term amortisation periods at the point-of-service. Moreover, another characteristic of PSSs that affect the usual ways of gaining profits is the possibility to raise revenue and get profit not through sales but through**

efficiency provision (energy services; Demand Side Management and Chemical Management Services).

- The resistance of companies to extend involvement with a product beyond point-of-sale and historical practice has been identified as a major barrier to increased manufacturer responsibility for environmental impacts of products [24]. The extended involvement leads to intra-organisational and inter-organisational changes, such as closer interaction with other actors in the product-service chain. This happens partially due to inertia and fear of innovation.
- The reorientation of companies towards product-service systems requires a fundamental shift in corporate culture and market engagement, which, in turn, requires time and resources to facilitate the shift. Changing the orientation of the company from product to service sale means also changing the traditional marketing concepts. This is often met with psychological barriers in companies.
- It is quite difficult to trace the shift in service or manufacturing industries because of differences in how services are reported in national and international statistics.[3] For example, in manufacturing companies, human resources, canteens and medical care centres for workers may be included as services or as manufacturing departments.
- Adding environmental considerations to the product development cycle is often seen as lengthening the time to market. This is even more so if the entire product-service system should be designed with criteria of environmental efficiency in mind.
- Consumers might not be very enthusiastic about ownerless consumption. Numerous examples of practical applications of product-service ideas in the commercial sector did not facilitate operationalisation in the private market [9]. The successful models such as car sharing are still limited to small market niches.
- Customers' demands and purchasing behaviour appears to be potentially more complicated than expected. The assumptions that the customer is more interested in use rather than the ownership [25] or is looking for the use rather than the product itself does not exactly represent reality.

8 Conclusions

An important conclusion is that there are many examples that illustrate parts of the solution (eco-design, optimisation of distribution, product customisation, added services, take-back systems, remanufacturing, and recycling), but there are few examples of complete product-service systems that are being designed on a life cycle basis in companies. The companies often lack a system approach. Another reason for such a limited application of product-service systems in companies is the fact that PSS is a new area and even at the academic level the PSSs have not yet been studied and shaped for practical applications. Therefore, a number of uncertainties concerning the characteristics of the product-service systems can be highlighted. These uncertainties can be combined into three main categories:

- Readiness to adopt the product-service systems into a company's strategic decisions. The shift from selling products to providing PSS entails substantial changes in the companies' structure and organisational frameworks, production and marketing strategies, as well as their relationships with

[3] This problem was recognised and discussed at the World Service Congress '99 with Ms. Gunnel Mohme, the Head of the Service Business Unit at Svenska Industriförbundet.

stakeholders. Few studies have evaluated the profitability of product-service systems for companies, although present economic difficulties within some companies serve as a counter-argument to the outcome of the evaluation.

- **Readiness to accept the product-service systems by consumers. Little research has been conducted on evaluating the competitiveness of product-service systems and their profitability for consumers.**
- **Environmental characteristics of product-service systems are also not yet studied. A number of studies evaluated the environmental features of particular stages and activities, such as remanufacturing and take back as favourable. On the other hand, other studies showed that environmental characteristics of, for example, eco-services should be accounted for carefully, because they are not always preferable in comparison to products.**

The results of the study provide a background for setting future research directions. There is a need to further explore the design side of PSSs and to develop a methodological basis for their development, practical implementation and evaluation of economic, environmental and social consequences.

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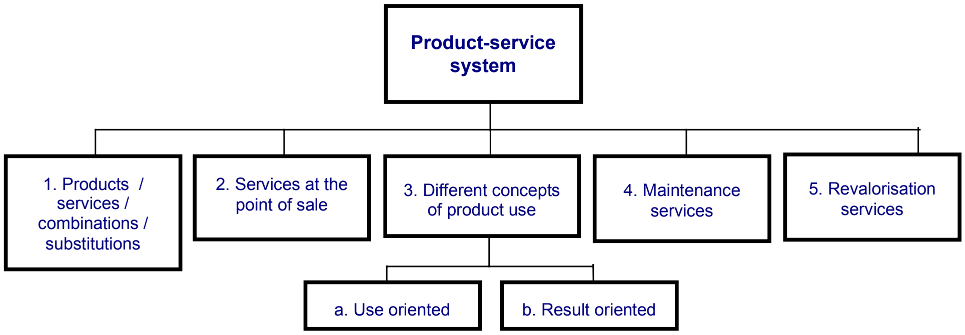
Product-service system
1. Products / services / combinations / substitutions
2. Services at the point of sale
3. Different concepts of product use
4. Maintenance services
5. Revalorisation services
a. Use oriented
b. Result oriented

Figure 1 Classification of a product-service system

Registration of a Company in India

The present article aims to briefly describe the procedure for registration of a "Company" in India and procedure followed for establishment of Liaison and Branch Office of a Foreign company in India.

The Companies Act, 1956 governs the formation, regulation and winding up of companies in India and the Registrar of Companies appointed under the Companies Act registers companies and ensure all statutory requirements are compiled by the Company.

Objective of Registration of a Company

The Companies Act defines the procedure that governs the registration or incorporation of a Company which leads to formation or birth of a Company. It is highly significant to register a Company as the Companies Act bestows a legal personality on registered company and by virtue of registration, the company can enjoy the benefits that are bestowed on a company by virtue of the Act.

Registration of a Private Limited Company

A private limited company can be registered by making an application to the Registrar of Companies in place where the registered office shall situate. The following are the guidelines and procedure prescribed by the Act for registering a private limited company.

- ➢ The proposed name of the company is not required to be prohibited under any law in force. The applicant is required to file e form- I A with the Ministry of Corporate Affairs to check the availability of name. This name should end with suffix "Pvt Ltd". In case of rejection of the proposed name then fresh application is required to be made.
- ➢ Minimum paid up capital for a "private limited company" shall not be less than 1 lakhs Indian rupees.
- ➢ A private limited company is required to have minimum 2 members and not more than 50 members.
- ➢ The promoters or directors of the Company are required to file the "Memorandum of Association" and it shall include:
    - Name clause stating the name of the company. The company is required to include in suffix to the company's name "Pvt. Ltd".
    - Object clause stating the object of carrying on business activity and the business activities that shall be undertaken by the company.
    - Registered office clause stating the office where main business activity or business shall be carried out.
    - The capital clause mentioning about the paid up capital of the company.
    - Any other information mentioning directors, promoters of the company.
- ➢ The Articles of Association shall mention about the directors of the company and how the company shall carry the affairs of the company. It mentions about the internal management of the company and restrictions placed on the powers directors and members of the company.

- Any agreement that have entered regarding appointment of directors etc.
- The requisite stamp duty prescribed by the Stamp Act is required to be paid on "Memorandum of Association" and "Articles of Association".
- The registration fee for registering the form I A and on Memorandum and Articles of Association is required to be paid. Form 1 is required to be filed declaring compliance to the legal requirements prescribed by the Act.
- The Registrar on being satisfied that conditions prescribed for the registration of the company are fulfilled shall issue certificate of commencement and incorporation certificate.
- This company is prohibited to invite any member of general public for subscription to any shares or debentures.

Registration of Public Limited Company

A Public limited company can also be registered by making an application to the Registrar of Companies just like a private limited company. The following are the documents and requirements that are mandatory for registration of a public limited company.

- The "Public limited company" name should be suffixed by "Ltd" or "limited".
- The minimum paid up capital required for formation of a "public limited company" shall not be less than 5 lakhs rupees.
- The minimum members to the public limited company shall be 7.
- The Promoters of the Company are required to inform to the Registrar of Companies for invitation of capital from general public for subscriptions of the shares.
- The Memorandum of Association just like the one in "private limited company" is required to be filed mentioning name, object, and registered office of the company. This document is required to be as prescribed by the Companies Act.
- The Articles of Association mentioning about the directors and procedure of working of the company are required to be filed with Registrar of the Companies. This document is also required to be as prescribed by the Act.
- The Prospectus containing invitation to the public to subscribe to the shares of the company is required to be filed with the Registrar.
- Consent of all directors to act for establishment of company in Form 29 is required to be filed with the Registrar.
- The company is order to commence the business is required to seek commencement of business certificate. It is only after this certificate is issued from the Registrar of Companies that the public limited company can commence its business.
- The promoters or directors of the Company are required to file a declaration of the compliance of the conditions prescribed by provision section 149 of the Act in form 19 and a statement in lieu of prospectus in form 20 for obtaining certificate of commencement of business.
- All the stamp duties and registration fees are required to be paid.
- Thereafter on being satisfied that all the conditions prescribed are fulfilled by the company, the Registrar of Companies shall issue certificate of Commencement of Business

and Incorporation certificate and the company comes into existence and can commence its business.

Establishment of Liaison office

The FEMA (Establishment in India of branch office or other place of business) regulation 2000 governs the process of establishment of Liaison office in India. The RBI or Reserve Bank of India is the controlling authority for setting up Liaison Office in India. The applications are required to be made in form FNC I to the RBI. RBI shall scrutinise the application. It should be accompanied by:

- Attested copy of certificate of registration or incorporation attested by Indian Embassy or Indian Notary Public.
- Attested copy of memorandum of association and articles of association attested by Indian embassy or notary.
- The copy of latest audited balance sheet of the applicant company who wish to set up liaison office.
- All the other documents or brochures mentioning about activity, operations and countries of operations are required to be submitted to the RBI.
- Letter of authorisation by the applicant company authorising the local representative to file applications with RBI and receive letter of approval from the RBI in case of approval.
- The approval shall be granted by the RBI only if :
    - If the Liaison office that is being set up in India is involved only liaison activity and promise not undertake any activity that shall generate income.
    - If the liaison office does not offer or take any funds from any person in India without prior approval from RBI.
    - The liaison office shall follow all the laws of India and comply with all other conditions prescribed by the FEMA regulation.
    - The liaison office shall only be allowed to set up if minimum of 100,000 US dollars or equivalent was the profit in immediately preceding 5 financial years in the home country.
- The liaison office shall continue to function only for 3 years and further subject to approval of RBI.
- After the approval given by RBI, the liaison office is required to inform RBI about the place of office of liaison office and apply in form 44 and register with the Registrar of Companies of New Delhi within 30 days from date of approval for the registration of Liaison office.

Establishment of a branch office of Foreign Company

The branch office of a foreign company is governed by the FEMA (Establishment in India of branch office and other place of business) regulation 2000. RBI is governing body for the establishment of branch office. The procedure that has been followed for establishment of liaison office is required to be followed in establishment of branch office of a foreign company by making application in form FNC-I with all accompanied documents of certificate of incorporation, memorandum and article of association. This is also subject to approval of RBI and some of the conditions are:

- The branch office shall indulge in only those activities approved by the RBI and not expand or extend to any other activities.
- The branch office after the approval from RBI shall intimate RBI regarding its registered office and register the branch office under Companies act by making application in form 44 with the Registrar of Companies, New Delhi.
- The branch office can only be allowed to set up office in India in case the minimum profits immediately preceding 3 financial years in home country were 50,000 US dollars or its equivalent.

Conclusion:

The Companies Act is the sole legislation that governs establishment of “all companies” in India along with other guidelines prescribed by FEMA (Establishment in India of branch office or other place of business) Regulation 2000.

DISCLAIMER:

The information contained herein is of a general nature and is not intended to address the circumstances of any particular individual or entity. The contents should not be construed as legal advice or an invitation for a lawyer-client relationship and should not rely on information provided herein. Although we Endeavour to provide accurate and timely information; there can be no guarantee that such information is accurate as of the date it is received or that it will continue to be accurate in the future. No one should act on such information without appropriate professional advice after a thorough examination of the particular situation.

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The financing of your business is the most fundamental aspect of its management. Get the financing right and you will have a healthy business, positive cash flows and ultimately a profitable enterprise. The financing can happen at any stage of a business's development. On commencement of your enterprise you will need finance to start up and, later on, finance to expand.

Finance can be obtained from many different sources. Some are more obvious and well-known than others. The following are just some of the means of finance that are open to you and with which we can help.

Bank loans and overdrafts

The first port of call that most people think about when trying to obtain finance is their own bank. Banks are very active in this market and seek out businesses to whom they can lend money. Of the two methods of giving you finance, the banks, especially in small and start-up situations, invariably prefer to give you an overdraft or extend your limit rather than make a formal loan. Overdrafts are a very flexible form of finance which, with a healthy income in your business, can be paid off more quickly than a formal loan. If, during the period you are financing the overdraft, an investment opportunity arises, then you could look to extend the options on your overdraft facility to finance the project.

Many businesses appreciate the advantages of a fixed term loan. They have the comforting knowledge that the regular payments to be made on the loan make cash flow forecasting and budgeting more certain. They also feel that, with a term loan, the bank is more committed to their business for the whole term of the loan. An overdraft can be called in but, unless you are failing to make payments on your loan, the banks cannot take the finance away from you.

Many smaller loans will not require any security but, if more substantial amounts of money are required, then the bank will certainly ask for some form of security. It is common for business owners to offer their own homes as security although more risk-averse borrowers may prefer not to do this. Anyone offering their house as security should consult with any co-owners so that they are fully aware of the situation and of any possible consequences. Another source of security may be the Enterprise Finance Guarantee Scheme. A start-up business unable to provide any other form of security may be able to get a guarantee for loans up to £1,200,000. Under the scheme, you pay a 2% premium on the outstanding balance of the loan, and in return, the government guarantees to repay the bank (or other lender) up to 75% of the loan if you default.

Savings and friends

When commencing a new business, very often the initial monies invested will come from the individual's personal savings. The tendency of business start-ups to approach relatives and friends to help finance the venture is also a widespread practice. You should make it clear to them that they should only invest amounts they can afford to lose. Show them your business plan and give them time to think it over. If they decide to invest in your business, always put the terms of any agreement in writing.

Issue of shares

Another way of introducing funds to your corporate business is to issue more shares. This is always a welcome addition to business funds and is also helpful in giving additional strength to the company's balance sheet. However, you need to consider where the finance is coming from to subscribe for the new shares. If the original proprietor of the business wishes to subscribe for these shares, then he or she may have to borrow money in a similar way to that discussed earlier. Typically, however, shareholders in this position are often at the limit of funds that they can borrow. Therefore, it may be necessary to have a third party buy those shares. This may mean a loss of either control or influence on how the business is run. An issue of shares in this situation can be a very difficult decision to make.

Venture capital

Approaching venture capital houses for finance will also mean an issue of new shares. The advantage of going to such institutions is the amount of capital they can introduce into the business. The British Private Equity and Venture Capital Association offers useful free publications (www.bvca.co.uk). Because of the size of their investment, you can expect them to want a seat on your Board. They will also make available their business expertise which will help to strengthen your business, although inevitably this will come with an additional pressure for growth and profits.

On a smaller scale, the government has introduced various tax-efficient schemes for entrepreneurs to invest in growing businesses. The current schemes available are called the Enterprise Investment Scheme (EIS), Seed Enterprise Investment Scheme (SEIS) and Venture Capital Trusts (VCT). We have separate factsheets providing details on these areas.

The SEIS is designed to help small, early-stage companies to raise equity finance by offering a range of tax reliefs to individual investors who purchase new shares in those companies. It complements the EIS which offers tax reliefs to investors in higher-risk small companies. The SEIS is intended to recognise the particular difficulties which very early stage companies face in attracting investment, by offering tax relief at a higher rate than that offered by the EIS.

Retained earnings and drawings

Since ultimately the well-being of a business is connected with the cash flow of that enterprise, if a proprietor would like more liquidity, then it is sometimes necessary to re-examine the amount of money they are withdrawing from the business for their personal needs. In this way, additional funds earned by the business can be retained for future use.

Other sources of finance

Other possible sources of finance are outlined below.

Factoring

Factoring provides you with finance against invoices that your customers have not yet paid. Typically you can receive up to 85% of the value of the invoice immediately and the balance (less costs) when the customer pays.

Hire Purchase (HP)

This is used to finance the purchase of equipment. Your business buys the equipment but payments of capital and interest are spread over an agreed period.

Leasing

This is a method of financing equipment you do not need to own. It is often used for vehicle finance. The equipment is rented rather than owned and the rental payments spread over several years. There can also be the option to fix maintenance costs as part of the agreement (contract hire).

Matching

It makes sense to match the finance you are seeking to the purpose for which it will be used.

- Working capital - overdraft or factoring
- Equipment and vehicles - fixed-term loan, HP or leasing
- Property - long-term mortgage
- Development/start-up - investment finance

How we can help

We have the expertise and the contacts to help you at all stages of your business development and to help you finance the business along the way. If you have any questions or proposals, please contact us as we would be happy to discuss them with you.

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PROCESS FOR COMPANY FORMATION IN INDIA

The Processes enumerated below are mostly common for a Private as well as a Public Limited company. There are some additional processes for Public Limited companies which are mentioned separately.

Step No.	Process	Documents required
1	Obtain Digital Signature of one of the promoter.	Copy of Passport and a Signed Form
2	Apply for Director Identification Number (DIN) of the Promoters (2 Promoters in case of a Private company and 3 Promoters in case of a Public Company) and send the hard copy along with documents to Noida, (U.P. – India)	Copy of Passport and a Signed Form by the Indian Director and the same documents attested by the Indian Embassy / Notary in the foreign country for the foreign Director/s.
3	Apply for Name approval of the company in Form 1A to the Registrar of Companies (ROC) along with necessary documents.	Digital Signature
4	After receipt of Name approval, Apply for Incorporation of the company in Form No. 1, 18, 32, etc and the Memorandum and Articles of Association, etc. There are several tasks here like Franking of Documents, etc.	No major documents required from the clients side. Most of the documents will be prepared by the consultants. Only signatures of the Promoters will be required at many places and documents attested by the Indian Embassy ~~/ Notary~~ in the foreign country for the foreign Director/s.
5	After the above documents are uploaded digitally the same will have to be submitted manually with the ROC and then they will have to be verified by the ROC and any changes suggested by the ROC will have to be	No Documentation required from the client.

	incorporated in the same. Any other requirements of the ROC will have to be fulfilled.	
6	On receipt of the Approved Memorandum and Articles and the Incorporation Certificate, the procedure for incorporation of a Private Limited company will be complete and the company can go ahead with other registrations like PAN, TAN, Shop Act, Profession Tax, VAT, Service Tax Excise, etc.	Basically the Incorporation Certificate, Memorandum and Articles and Address proof of the company will be required for other registrations and also signatures of one director on several forms.
7	For a Public Limited company, the company will have to Apply for a Commencement Certificate for which several documents like; Statement in Lieu of Prospectus (SLP), Auditors NOC, Statement of Preliminary Expenses, Power of Attorney, etc. will have to be filed along with Form No. 20.	No additional documents will be required

- *Government Fees for various levels of Authorized Share Capital are given separately in a separate Sheet.*

Other Registrations -

The company will be required to obtain various other registrations – as listed below. These registrations will be obtained after incorporation of the company.

1. Income Tax Permanent Account Number (PAN) – universal for entire India irrespective of place/s of business anywhere in India. (Under control of Central Government) If the foreign nationals are to be remunerated in India, they will also be required to obtain individual PAN.

2. Tax Deduction Account Number (TAN) – separate number may be obtained for different offices – if required. If the accounts are centralized, you can have only one number. (Under control of Central Government)

3. Professional Tax Registrations – For the Company as taxable identity & another one for company as Employer - Separate number required for different offices in different states. (Under control of State Government)

4. Shop & Establishments Act Registration - Separate Registration required for different offices in different cities. (Under control of local authority or Municipal corporation)

5. Import-Export code no. (IEC code) – If you are expecting any import & export of goods/services. (Under control of Central Government)

6. Formalities with RBI – Correspondence regarding appointment of foreign directors, share allotment & transfers to foreign entities, etc. ***(If the nature of the company is of a Controlled nature then prior approval of RBI is necessary for company incorporation)***

7. VAT, Excise and Service Tax registrations - Separate numbers may be obtained for different offices – if billing is from separate places. If the accounts are centralized, you can have only one number. (Excise and Service Tax is under control of Central Government and VAT is under the control of State Government) ***(This will be applicable only if the company plans to make any sales in India)***

8. Provident fund registration – if you are going to set up a PF scheme & contribute towards PF of employees. ***(This will be applicable only if your Employee strength increases beyond 10 Nos.)***

9. There are certain other registrations like Factories Act, STPI, etc. which will depend on the nature of the Company Incorporated.

The Concept of Entrepreneurship

Entrepreneurship is a common vocabulary to many people, a topic occupying a prominent position on the research agenda of scholars from variety of backgrounds and disciplines; a subject that has elicited lots of interests from people of different occupations including scholars, educators and policy makers. The innovations and high value products getting into the market each day are results of entrepreneurial efforts, making entrepreneurship development a major strategy for sustainable socio-economic development. The purpose of this study was to find out a universal meaning/definition of entrepreneurship. The study was secondary, involving detailed analysis of published materials on the subject matter. According to the findings, entrepreneurship is the heart of the modern business, a force behind innovative businesses that characterize the modern economy and a dynamic process of creating incremental wealth by individuals who assume. The analysis, there are many definitions of entrepreneurship as there have many attempts to define it. However, entrepreneurship is action-oriented, involving immense creativity and innovativeness. Entrepreneurship can either be opportunity-based or necessity-based but whatever the motivation; it is pursued as a viable career option by people of all works of live, levels and occupations. It is also evident that there continues to be new thoughts on the subject and it is still an evolving concept with more room for study, discovery and development.

Various authors have used a number of terms and concepts to define entrepreneurship; creativity, innovation, creative destruction, risk taking, creation of new products, new business methods, creations of new organizations and enterprises among others, all showing its richness in meaning, application and manifests. Entrepreneurship can either be opportunity-based or necessity-based but whatever the motivation; it is pursued as a viable career option.

The Four Types of Market Structures

There are quite a few different market structures that can characterize an economy. However, if you are just getting started with this topic, you may want to look at the four basic types of market structures first: perfect competition, monopolistic competition, oligopoly, and monopoly. Each of them has its own set of characteristics and assumptions, which in turn affect the decision making of firms and the profits they can make.

It is important to note that not all of these market structures exist in reality; some of them are just theoretical constructs. Nevertheless, they are critical because they help us understand how competing firms make decisions. With that being said, let’s look at the four market structures in more detail.

1. Perfect Competition

Perfect competition describes a market structure, where a large number of small firms compete against each other. In this scenario, a single firm does not have any significant market power. As a result, the industry as a whole produces the socially optimal level of output, because none of the firms can influence market prices.

The idea of perfect competition builds on several assumptions: (1) all firms maximize profits (2) there is free entry and exit to the market, (3) all firms sell completely identical (i.e., homogenous) goods, (4) there are no consumer preferences. By looking at those assumptions, it becomes quite obvious that we will hardly ever find perfect competition in reality. That is an essential aspect because it is the only market structure that can (theoretically) result in a socially optimal level of output.

Probably the best example of a market with an almost perfect competition we can find in reality is the stock market. If you are looking for more information on perfect competition, you can also check our post on perfect competition vs. imperfect competition.

2. Monopolistic Competition

Monopolistic competition also refers to a market structure, where a large number of small firms compete against each other. However, unlike in perfect competition, the firms in monopolistic competition sell similar, but slightly differentiated products. That gives them a certain degree of market power, which allows them to charge higher prices within a certain range.

Monopolistic competition builds on the following assumptions: (1) all firms maximize profits (2) there is free entry, and exit to the market, (3) firms sell differentiated products (4) consumers may prefer one product over the other. Now, those assumptions are a bit closer to reality than the ones we looked at in perfect competition. However, this market structure no longer results in a socially optimal level of output because the firms have more power and can influence market prices to a certain degree.

An example of monopolistic competition is the market for cereals. There is a huge number of different brands (e.g., Cap’n Crunch, Lucky Charms, Froot Loops, Apple Jacks). Most of them probably taste slightly different, but at the end of the day, they are all breakfast cereals.

3. Oligopoly

An oligopoly describes a market structure that is dominated by only a small number of firms. That results in a state of limited competition. The firms can either compete against each other or collaborate (see also Cournot vs. Bertrand Competition). By doing so, they can use their collective market power to drive up prices and earn more profit.

The oligopolistic market structure builds on the following assumptions: (1) all firms maximize profits, (2) oligopolies can set prices, (3) there are barriers to entry and exit in the market, (4) products may be homogenous or differentiated, and (5) there is only a few firms that dominate the market. Unfortunately, it is not clearly defined what a “few firms“ means precisely. As a rule of thumb, we say that an oligopoly typically consists of about 3-5 dominant firms.

To give an example of an oligopoly, let’s look at the market for gaming consoles. This market is dominated by three powerful companies: Microsoft, Sony, and Nintendo. That leaves all of them with a significant amount of market power.

4. Monopoly

A monopoly refers to a market structure where a single firm controls the entire market. In this scenario, the firm has the highest level of market power, as consumers do not have any alternatives. As a result, monopolies often reduce output to increase prices and earn more profit.

The following assumptions are made when we talk about monopolies: (1) the monopolist maximizes profit, (2) it can set the price, (3) there are high barriers to entry and exit, (4) there is only one firm that dominates the entire market.

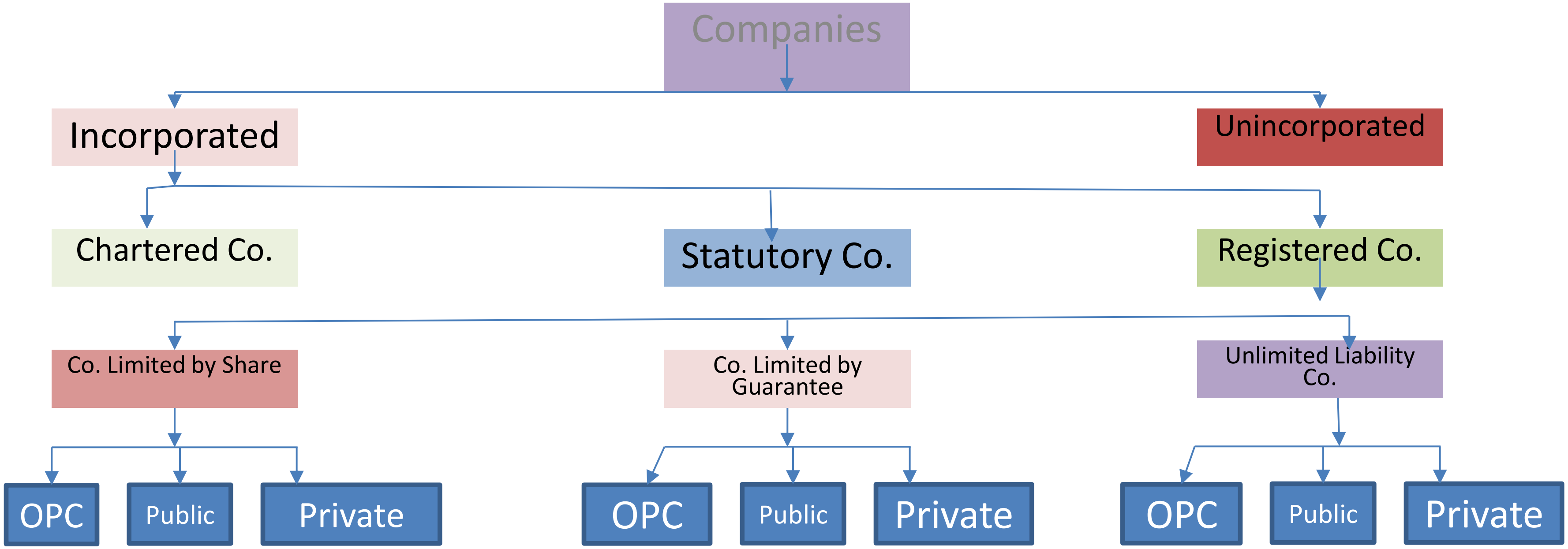
From the perspective of society, most monopolies are usually not desirable, because they result in lower outputs and higher prices compared to competitive markets. Therefore, they are often regulated by the government. An example of a real-life monopoly could be Monsanto. This company trademarks about 80% of all corn harvested in the US, which gives it a high level of market power. You can find additional information about monopolies in our post on monopoly power.

Summary

There are four basic types of market structures: perfect competition, imperfect competition, oligopoly, and monopoly. Perfect competition describes a market structure, where a large number of small firms compete against each other with homogenous products. Meanwhile, monopolistic competition refers to a market structure, where a large number of small firms compete against each other with differentiated products. An Oligopoly describes a market structure where a small number of firms compete against each other. And last but not least, a monopoly refers to a market structure where a single firm controls the entire market

Chapter-II

Types of Companies



Companies

Incorporated

Unincorporated

Chartered Co.

Statutory Co.

Registered Co.

Co. Limited by Share

Co. Limited by Guarantee

Unlimited Liability Co.

OPC

Public

Private

OPC

Public

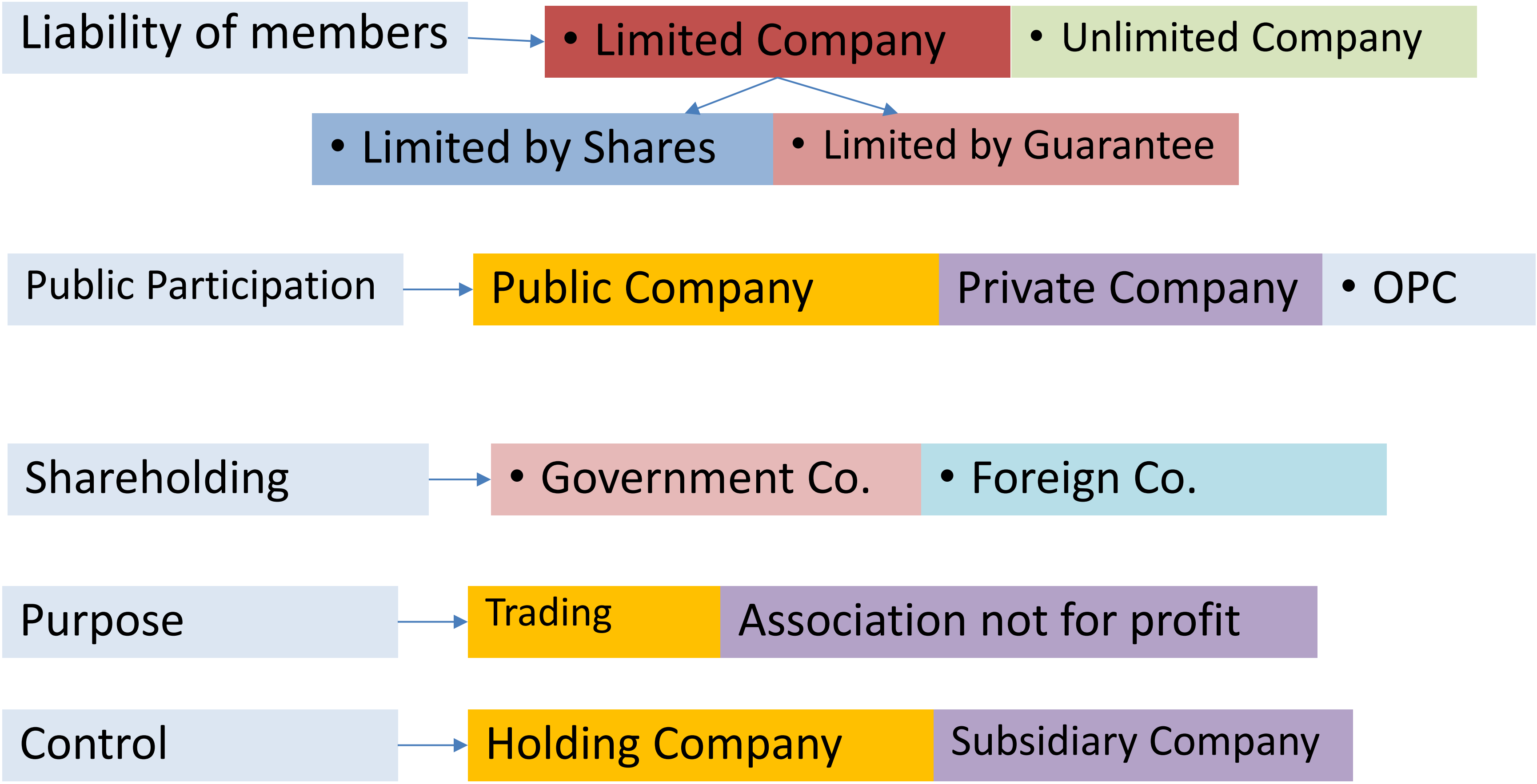
Private

OPC

Public

Private

REGISTERED COMPANIES



Liability of members

- Limited Company
- Unlimited Company
- Limited by Shares
- Limited by Guarantee

Public Participation

Public Company

Private Company

- OPC

Shareholding

- Government Co.
- Foreign Co.

Purpose

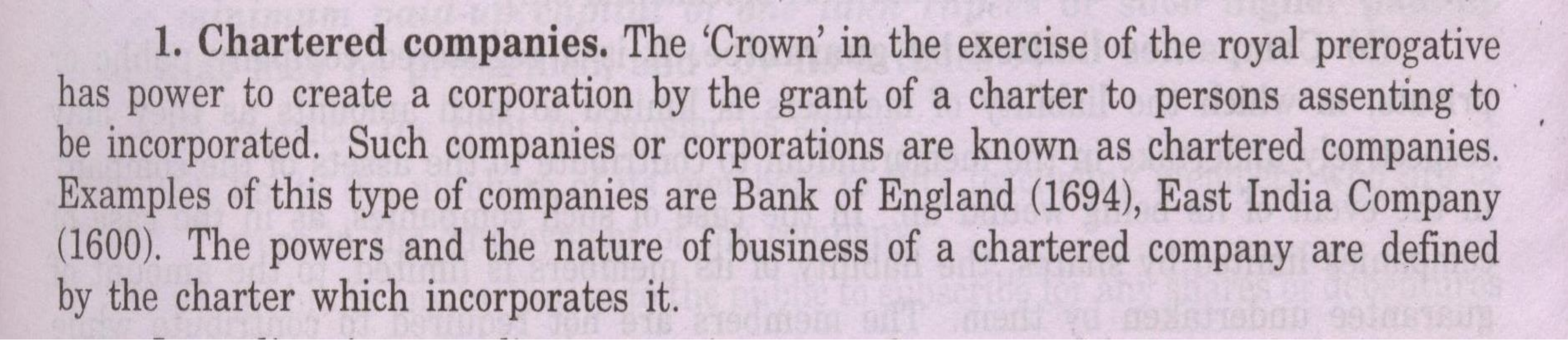
Trading

Association not for profit

Control

Holding Company

Subsidiary Company



1. Chartered companies. The 'Crown' in the exercise of the royal prerogative has power to create a corporation by the grant of a charter to persons assenting to be incorporated. Such companies or corporations are known as chartered companies. Examples of this type of companies are Bank of England (1694), East India Company (1600). The powers and the nature of business of a chartered company are defined by the charter which incorporates it.

2. **Statutory Companies**:

•Created by **Special Act** of Parliament or State Legislature.

•The Objectives, powers, liabilities, responsibilities are laid in that Special Act

•Mostly concerned with public utilities (e.g Railways, Gas, Electricity) and enterprises of National Importance.

•Examples: Reserve bank of India, State bank of Inida, RBI, LIC, IFC, UTI, etc.

•The Company Act applies only when Special Act is silent on any issue.

3. Registered Companies:

- The companies formed and registered under the Companies Act 2013 or earlier Companies Acts.
- Most commonly found companies.

Types of registered Companies :

On the Basis of Liability:

-Limited Liability Companies: Limited by Shares or Gaurantee

-Unlimited Liability Companies

a) **Companies Limited by Shares:**

- Sec-2(22) “company limited by shares” means a company having the liability of its members limited by the memorandum to the amount, if any, unpaid on the shares respectively held by them.
- **Company Allots shares to the members.**
- **Liability of members is limited to the amount unpaid on shares held.**
- **The Liability can be enforced at any time during the existence of the company and also at the time of winding up.**

- **b) Companies Limited by Guarantee (and not having share capital): Sec2(21)** “company limited by guarantee” means a company having the liability of its members limited by the memorandum to such amount as the members may respectively undertake to contribute to the assets of the company in the event of its being woundup;

- **The members undertake to contribute a fixed amount to the assets of the company, called Guarantee, at the time of joining the company.**
- **Company does not allot shares to the members.**
- **Liability of members is limited to the amount of Guarantee.**
- **The Amount of guarantee may differ from member to member**
- **The Liability can be enforced only at the time of winding up.**
- **Also referred as Non-Trading companies.**
- **Mostly such companies are incorporated not for the purpose of profit but to promote Art, Science, Charity, Sports, Commerce ,etc.**

c) Companies Limited by Guarantee and having share capital:

- **The members undertake to contribute a fixed amount to the assets of the company, called Guarantee, at the time of joining the company**
- **Company also allot shares to the members.**
- **Liability of members is two fold –**

  i) limited to the amount of Guarantee and

  ii) limited to the amount unpaid on shares held.
- **The Liability towards amount of Gaurantee can be enforced only at the time of winding up.**
- **The Liability towards shares can be enforced at any time during the existence of the company and also at the time of winding up.**

Unlimited Companies:

- Sec2(92) “unlimited company” means a company not having any limit on the liability of its members.

- The members will be liable for all the debts of the company like partners in a Partnership firm.
- The Articles must state the number of members with which the company is to be registered.
- It is a contingent liability of the members which will fall due only on the winding up of the company.
- The Unlimited Company can be re-registered as Limited Company through appropriate alterations in Liability Clause of MOA and alterations in AOA.
- The re-registrations will not affect any debt, liabilities, obligations or contracts of the company before the re-registration.

Private Company:

- According to **Section 2(68),** “private company” means a company having a minimum paid-up share capital of one lakh rupees or such higher paid-up share capital as may be prescribed,and which by its articles,—

(i) restricts the right to transfer its shares;

(ii) except in case of One Person Company, limits the number of its members to two hundred:

Provided that where two or more persons hold one or more shares in a company jointly, they shall, for the purposes of this clause, be treated as a single member:

- Provided further that—

(A) persons who are in the employment of the company; and

(B) persons who, having been formerly in the employment of the company, were members of the company while in that employment and have continued to be members after the employment ceased, shall not be included in the number of members; and

(iii) prohibits any invitation to the public to subscribe for any securities of the company;

- XYZ Company has 32 members to whom shares are allotted. In addition to that shares are allotted to following employees/ex-employees.
- Present Employees : 112
- Ex-Employees allotted shares during the course of their employment: 18
- Ex-Employees allotted shares after leaving the job: 8

Total Membership in the company for the purpose of Sec-3(1)(iii):

Non Employee Members	: 32
Ex-Employees allotted shares after leaving the job:	8
Total Membership	: 40

Public Company:

- According to **Section 2(71)** “public company” means a company which—
- (a) is not a private company;
- (b) has a minimum paid-up share capital of five lakh rupees or such higher paid-up capital, as may be prescribed:

- Provided that a company which is a subsidiary of a company, not being a private company, shall be deemed to be public company for the purposes of this Act even where such subsidiary company continues to be a private company in its articles ;
- A PUBLIC Company should have minimum of 7 members

Distinction between Private Company & Public Company

		Public	**Private**
1.	Minimum Number of Members	7	2
2.	Maximum Number of members	no limit	200
3.	Minimum Paid up capital	5Lakh	1 Lakh
4.	Number of Directors	minimum 3	Minimum 2
5.	Restriction on appointment of directors	Consent required	No such Req.
6.	Invitation to Public to subscribe for shares	No Restriction	Restricted
7.	Transferability of shares	Fully Transferable	Restriction
8.	Issue of Prospectus	Required	Not reqd.

Conversion of a Private Company into a Public Company

1. Conversion by Default: (Section-14):

- A private company can enjoy certain privileges as long as it complies with the requirements of Sec-2(68).
- If any default is made in complying with the provisions of the Act, the company will be regarded as a Public Company.
- However, the company may be relieved of the consequences on an application to the Central Govt., and Central Govt. on being satisfied that the default was not willful and it is just and equitable.

2. Conversion by Choice: (Sec-14)

- A private company may deliberately chose to become a public company if it deletes from its Articles the requirements/restrictions of Sec 2(68)by passing Special Resolution.
- The company will cease to be a private company from the date of the alteration of articles.
- It has to file with the registrar a prospectus or a statement in lieu of prospectus and a copy of special resolution, within 30 days of its becoming the public company.
- If the number of members are less than seven then it must be raised to seven.
- If the number of directors are less than three then it must be raised to three.
- The word Pvt. Should be deleted from its name.
- Conversion doesn't affect the legal personality of the company.

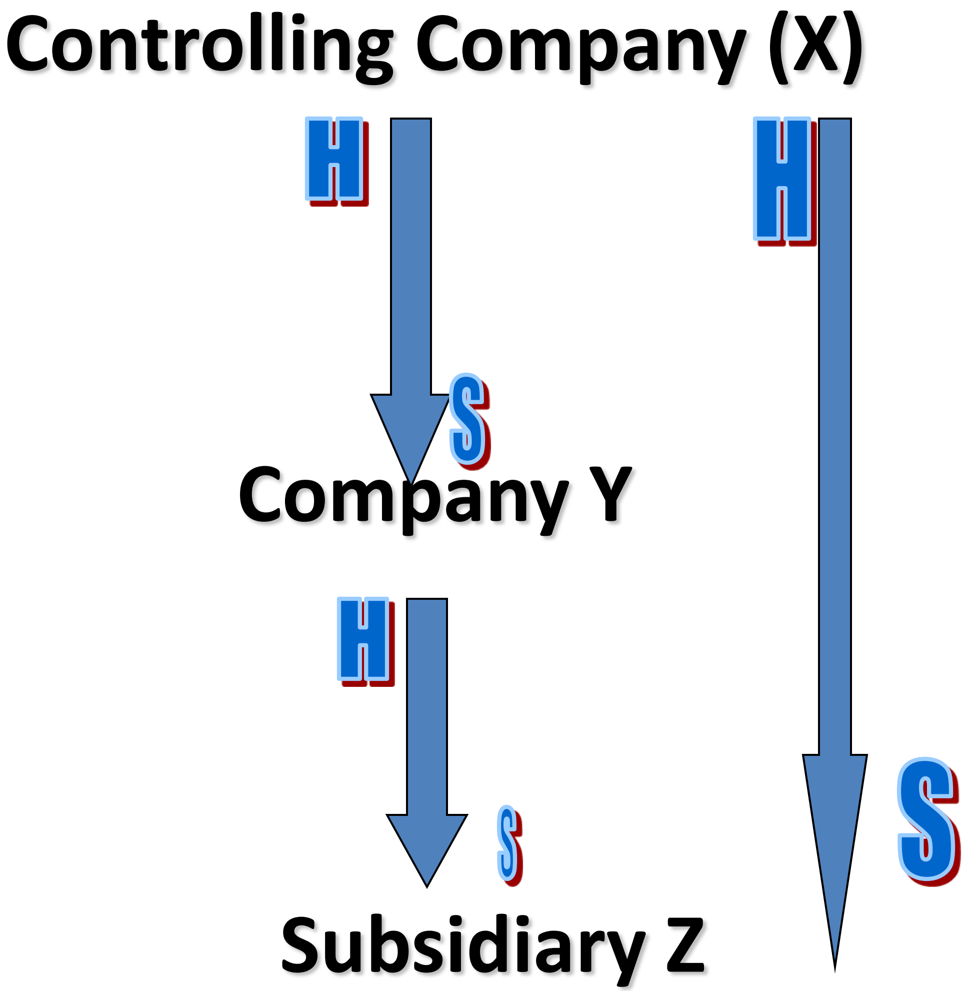
Holding Company and Subsidiary Comapny:

According to Section 2(87) of Companies Act, a holding company is one which;

i) Controls the composition of board of directors of another company (Subsidiary) i.e. no director can be appointed or removed without its consent ;or

ii) Holds more than 50% of the nominal value of equity share capital of another company (Subsidiary); or

iii) Where a company (Z) is a subsidiary of another company (Y) which is itself subsidiary of controlling company (X), the former company (Z) becomes subsidiary of the controlling company (X)



Controlling Company (X)

Company Y

Subsidiary Z

Government Company

As per Section 2(45) of Companies Act, a Government company means any company in which not less than 51% of the share capital is held by;

i) The Central Government; or

ii) Any State Government or Governments; or

iii) Partly by Central Govt. and partly by one or more State Governments

- Shares held by Municipal and other Local authorities are not to be taken into consideration.
- A subsidiary of a Govt. Company is also a Govt. Company.

Special Provisions Applicable to Govt. Company

1.Appointment of Auditors:

- Auditors shall be appointed or re-appointed by the Comptroller and Auditor General of India (CAG).
- CAG will direct the manner in which account to be audited.
- CAG have power to conduct supplementary/ test audit.

2. Audit Report: Section :

- Auditor shall submit Audit Report to CAG
- CAG may supplement or Comment upon Audit Report.
- The Audit Report along with CAG Comments/Supplements shall be placed before the AGM.

3. Annual Reports:

- In case Central Govt. is a member of a Govt. Company, an Annual Report on the working and affairs of the Govt. Company shall be laid before both Houses of Parliament (Lok Sabha and Rajya Sabha) along with Audit Report and comments/Supplements of CAG.

- In case only State Government/Governments is/are member/s of a Govt. Company, an Annual Report on the working and affairs of the Govt. Company shall be laid before the State Legislature of respective State Govts., along with Audit Report and comments/Supplements of CAG.

NOTE:

- The Central Govt. may by Notification in the Official Gazette, direct that any of the provisions of the Act, shall not apply or apply with such exceptions, modifications and adaptations as may be specified to the Govt. Companies.
- Govt. company is permitted to delete word ‘Private’ from its name.
- Government Companies are non-statutory companies like any other company registered under the Companies Act.
- Employees of Govt. Companies are not employees of the Union or State Government. (Praga Tools Corporation Vs C.V. Imanual AIR 1969) not even when all the share capital is subscribed by the Government (Ranjit Kumar Vs Union of India AIR 1969).
- Government Companies are not agents of Central Government or State Governments. (State Trading Corp. of India Ltd. Vs Commercial Tax Officer AIR 1963)
- A Govt. Company, like any other company may be wound up under the Companies Act

Foreign Company: Sec-2(42)

*“***Company or Body Corporate incorporated** outside India having

a. a place of business in India whether by itself or through an agent, physically or through **electronic mode** and

b. conducts any business activity in India in any other manner.

.

- *However, where not less than 50% of the paid up share capital of a company incorporated outside India having an established place of business in India, is held by none or more Indian citizens or by one or more companies incorporated in India, it shall comply with such provisions of the Act as may be prescribed as if it were a company incorporated in India*

- Companies (Registration of Foreign Companies) Rules, 2014 defines '**electronic mode**' as carrying out electronically based, whether main server is installed in India or not, including but not limited to-
- **Business to business and business to consumer transactions, data interchange and other digital supply transactions;**
- **offering to accept deposits or inviting deposits or accepting deposits or subscriptions in securities in India or from citizens of India;**
- **financial settlements, web based marketing, advisory and transactional services, database services and products, supply chain management;**
- **online services such as telemarketing, telecommuting, telemedicine, education and information research; and**
- **all related data communication services.**
- These transactions may be conducted by e-mail, mobile devices, social media, cloud computing, document management, voice or data transmission or otherwise.

A Company has an established place of business in India if it has a specific or identifiable place at which it carries on business such as an office, store, house, godown, or other such premises with some visible sign or physical indications that the company has a concrete connection with the particular premises
(Deverall Vs. Grant Advertising Inc. (1954)

Note: As regard status of the company, the law of the place of incorporation applies but in the case of contractual and other obligations, the law of the place of business alone will apply.

Rules of Companies Act 2013 applicable to foreign companies

1. **DOCUMENTS** **(Sec-380):** Every foreign company, within 30 days of establishing place of business in India, shall furnish to the Registrar the following documents for registration:

i) A certified copy of Charter, Statue, MOA, AOA, in English Language or certified translated copy in English Language if original documents are not in English language.

ii) The full address of the registered office of the company.

iii) A list of directors and secretary of the company with particulars as to name, nationality, etc.

iv) The name & address of person/persons resident in India authorised to accept services of legal processes and notices.

v) The full address of principal place of business in India.

2.Accounts (Sec-381)

- It will prepare P& L Account and Balance Sheet once in every calendar year.
- And shall file with the registrar three copies.
- Such documents must be in English language and if they are not then certified translated copies in English langauge have to be furnished.
- In addition to P&L A/c and B/S it shall also furnish list of all places of business in India.

3. Name (Sec-382):

- Every foreign company shall exhibit name and country of incorporation outside of every place of business in India in English Language and in one of the local languages.
- The name and country of incorporation is also required to be printed on business letters, bill heads, notices, and other official publications of the company.
- It shall state the name of the country of incorporation on every prospectus inviting subscription in India for its shares and debentures.

4. Service on Foreign Company: (Sec-383):

Any process, notice, or other document required to be served on a foreign company shall be deemed to be sufficiently served, if addressed to any person whose name and address have been delivered to the Registrar under section 380 and left at, or sent by post to, the address which has been so delivered to the Registrar or by electronic mode..

5. Delivery of Documents : Sec-597:

- All documents required to be filed by the foreign company shall be delivered to the Registrar of Companies at New Delhi and also to the Registrar of the State in which the principal place of business of the company is situated.

6. Penalty: (Sec-598)

- In case of default with any provision applicable, the company and every officer or agent of the company shall be punishable with a fine upto Rs. 10000/- and in case of continuing default an additional fine of Rs.1000/- per day of the default period.

One Person Company

Section 2(*62) "One Person Company" means a company which has only one person as a* member; one person, where the company to be formed is to be One Person Company that is to say, a private company, by subscribing their names or his name to a memorandum and complying with the requirements of this Act in respect of registration:

- Provided that the memorandum of One Person Company shall indicate ***the name of the other person***, with ***his prior written consent*** in the prescribed form, **who shall, in the event of the subscriber's death or his incapacity to contract become the member of the company** and the written consent of such person shall also be filed with the Registrar at the time of incorporation of the One Person Company along with its memorandum and articles:
- Provided further that such other person may withdraw his consent in such manner as may be prescribed:

- Provided also that the member of One Person Company may at any time change the name of such other person by giving notice in such manner as may be prescribed:
- Provided also that it shall be the duty of the member of One Person Company to intimate the company the change, if any, in the name of the other person nominated by him by indicating in the memorandum or otherwise within such time and in such manner as maybe prescribed, and the company shall intimate the Registrar any such change within suchtime and in such manner as may be prescribed:

Associations not for Profits

- The name of the company must end with the word “Private Limited” in case of Private company and “Limited” in case of Public Company.
- Companies Act permits the registration, under license granted by the Central Government, of an association not for profit with limited liabilty without using the words “Limited” or “Private Limited” to its name.

Conditions for grant of License by the Central Govt. ;

- Association to be formed as limited liability, is for promoting commerce, science, religion, charity, or any other useful object ; and
- It intends to apply its profits, if any, or other income in promoting its objects and to prohibit any payment of dividend to its members.

Advantages of Associations not for Profits

- Such an association, under sec-25, becomes body corporate with perpetual succession.
- It can adopt a more suitable name such as Chamber, Club, Guild, Association, etc.
- It enjoys all the characteristics of body corporate.
- The affairs can be conducted with much more efficiency.

Illegal Associations (Sec-464)

An association will be regarded as illegal association if;

- Its membership is more than 50 in any business
- The association must have been formed for the purpose of carrying on a business to acquire profits for itself or for its members.
- The association must not have been registered as a company under Companies Act, nor must have been formed in pursuance of some other Indian law.

Consequences of illegal Association

- Personal Liability: Every member becomes personally liable for all the liabilities incurred in the business and is punishable with a fine which may extend to Rs. 100000
- Contracts: An Illegal Associations cannot enter into any valid contracts.
- It can not sue and be sued for debts due to it or from it.
- No member can sue any other member in respect of any matter connected with the association.
- Illegal association cannot be wound up under the Companies Act either at the instance of the creditor or a member or association itself.
- Court doesnot even entertain a petition for its winding up.

One Man Company

- These are companies in which one man holds practically the whole of share capital.
- In order to meet the statutory minimum membership requirement some dummy member (relative or friend) holds 1 or 2 shares.
- Being the largest shareholder such a person enjoys complete control over the company.
- Enjoys profits of the company with Limited Liability.
- Such companies are Legal Entities and separate from the members as established under Saloman V Saloman & Co. Ltd.
- Only when the company is proved to be acting as an agent of its largest shareholder, it looses its separate entity status. (Exp- F.G. Films Ltd.)

T.R. Pratt Ltd. V. Sasson & Company Ltd. AIR 1936

“ Under the law an incorporated company is a distinct entity, and although all the shares may be practically controlled by one person, in law a company is a distinct entity and it is not permissible or relevant to enquire whether the directors belonged to same family or whether it is compendiously described as one man company.”

Officer who is in default

- The officer in default is that officer and directors who are incharge of management or who have been given responsibility of complying with any provision of the Act are held responsible for any contravention of the Act.

(The Company Amendment Act 1988)

- This section would be applicable only to those provisions which provide for punishment of officer in default.

Officer in Default means all the following officers:

a) the Managing Director or Managing Directors

b) the whole time director or directors

c) the manager;

d) the secretary;

e) Any person in accordance with whose directions or instructions the Board of Directors is accustomed to act (CEO)

f) Any person charged with by the BOD with the responsibility of complying with the provision, provided the person so charged has given his consent in this behalf.

g) Where any company does not have any of the officers specified in clauses (a) to (C), any director or directors who may be specified by the Board in this behalf or where no director is so specified, all the directors.

TYPES OF ENTERPRISES - MAIN RISK AND IMPACT FACTORS SPECIFIC TO THE COMPLEX BUSINESS AREA

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Abstract: *All the progress achieved in various fields of activity (technology, communication etc.) considerably diminishes its distribution time and distance. A consequence of this fact is the market globalization phenomenon, in the context of local peculiarities conservation and maintenance. Currently, even small enterprises are involved in international business. In other words, the internationalization process is not only specific to large important enterprises any more. As for the amplitude and complexity of the business field, this requires a high level of investment of professional and creative resources, as well as a close-to-reality forecast of its main effects. On an international level, business is the collection of commercial transactions which take place between two or more countries. Private companies take part in such transactions with the purpose of gaining profit, while government authorities may or may not pursue this goal. Thus, most enterprises, regardless of their size, are deeply affected both by international competition and by all the events taking place at the level of world economy.*

Keywords: *enterprises, typology, business, risk, criteria, small and medium-sized enterprises, performance, management, internationalization.*
Jel classification: *F23, L20, M21.*

1. INTRODUCTION

At present, it has been approved that, from an economic point of view, a profitable business can turn unprofitable because of changes in the initial environment. Risk may have as approach a company's inability to adapt in real time and at the lowest possible cost to market changes. From this point of view, the investment risk is generated by the high instability of the business environment, as well as by the company's incapacity to react in time and with low costs in order to counteract this trend.

Company management approaches the notion of risk both from the point of view of gaining profit and from the point of view of possible losses. So, the risk may be a real drawback for any economic activity development in good conditions. Unless this major impact is controlled, the decision-making process is hard, because there is a decrease in business volume and also the company must suffer certain smaller or larger damages. The attempt to eliminate or even diminish the risk's negative effects is based on the company's development of an efficient activity.

2. RESEARCH OBJECTIVES AND METHODOLOGY

The main research objectives of this article are:

- Presentation and analysis of basic criteria for defining and grouping companies;

- Short analysis of small and medium-sized enterprises as main „motors” of global economy development;
- Interpretation of the „risk” notion's meanings, specific to the complex business field.

The research methodology used in issuing this article is based on the empiric analysis of company „behavior”, at the same time emphasizing the „presence” of a risk which comes with any business that takes place on a national, as well as on an international level.

3. BASIC CRITERIA FOR ENTERPRISE DEFINITION AND GROUPING

There are multiple criteria for the definition and grouping of enterprises:

- Form of organization;
- Use of production factors;
- Property subjects;
- Field of activity;
- Cover area etc.

1. According to the form of ownership, multiple types of enterprises can be defined (N *et al*., 1999), such as:

- Private companies – their main characteristic is that their entire patrimony belongs to either one single person or one single group of people. This type of company appeared since early times and, as society developed, its diversity increased.

- Current realities make possible the existence of multiple private companies all over the world (hundreds of millions of companies). They cover a wide range of parameters and functions.

- Private companies have the following basic characteristics: the establishment and operation decision belongs entirely to the entrepreneur, as well as the ownership of the minimum required funds necessary to establish it, the economic and social risks which derive from the development of the company's activities are completely assumed by the entrepreneur etc.

If we consider the number of capital owners, private enterprises can be divided into two very important categories:

- The individual company, which patrimonial belongs to a single individual, is presently the most commonly used for small and medium-sized enterprises;
- The group company, which patrimonial belongs to at least two persons. Some of the most frequent forms of group companies are: the family company, the corporate company, the joint stock company.

The patrimony of the family company is in the common property of a certain family's members. This type of enterprise is small and often the family members are not only its owners, but its employees as well. In this environment, there are strong cooperation and solidarity relationships.

The corporate company is created with the participation on several individuals who, in the past, had performed similar activities, in similar conditions, and who freely expressed their will to cooperate. These persons, through the act of company constitution, become co-participants in the management activities.

The most frequent form of private group enterprise used on a large scale in contemporary economy is the joint stock company. From a patrimony point of view, the capital splits in a high number of parts, each part having its own face value called a stock.

Owing a significant number of stocks gives the owner the right of property over a certain part of the enterprise. Through stock market transactions or through direct sell – buy transactions, the right of ownership can be given over an important part of the company.

State companies – are characterized by the fact that the entire patrimony of the enterprises belongs to the state. The constitution and operation of state enterprises depend exclusively on the will of the state decision factors, according to each country's laws. (R, 1993)

Mixt companies – is a combination between private and state enterprises. Often, these take the form of joint stock companies, where the state becomes one of the most important stockholders. Its fundamental characteristics are tightly connected to the percentage of stocks owned by the state. The profile of mixt companies is very close to the profile of private enterprises, differing from one branch of economy to another and from one country to another. If we study carefully the division of companies according to their form of ownership, it is clear that, while companies increase in size, the percentage of private enterprises decreases; at the same time, the percentage of state companies, as well as of mixt companies increases. On the other hand, if the size of societies decreases, then there is an increase of the percentage of private companies, as well as a significant decrease of the percentage of state and mixt companies.

Although small and medium-sized enterprises are more frequent in the field of economy and at the level of economic sectors, they have lower percentages if we refer to a certain set of indicators which comprises: turnover, gross profit, number of employees.

2. In Romania, according to the law, companies are divided into two main categories: autonomous administrations and trading companies.

Autonomous administrations are organized and operate mainly in the national economy's strategic branches – weapons industry, energetic industry, mining and natural gas exploitation, post-office and train transportation. (…)

Most state enterprises turned into trading companies. These are established in order to perform economic actions, they are legal persons and take the following forms:

- Unlimited company, whose social obligations are guaranteed with the social patrimony and with the unlimited and common responsibility of the partners;
- Limited partnership company, whose social obligations are guaranteed with the social patrimony and with the unlimited and solidary responsibility of the partners; the partners are only responsible up to the point of their input convergence;
- Partnership limited by shares company, whose corporate funds are split in shares and the social obligations are guaranteed with the social patrimony and with the unlimited and solidary responsibility of the partners; the partners are only obliged to pay for their stocks;

- Joint stock company, whose social obligations are guaranteed with the social patrimony; stockholders are only obliged to pay for their stocks;
- Limited liability society, whose obligations are guaranteed with the social patrimony; partners are only obliged to the payment of social parties. (N *et al.*, 1999)

3. Another important classification of enterprise types is their size. It must be said that there are multiple parameters which can be used to asses a company's size, but the most frequent one is the number of employees. Its main advantage is the easiness of obtaining information and also the possibility to use it for comparison regardless of economy branch or country.

Both in the European Union and in Romania, companies are divided into:

- Microenterprises, which have up to 9 employees;
- Small-sized companies, with 10 to 49 employees;
- Medium-sized companies, which have between 50 and 249 employees;
- Large companies, with over 250 employees.

In the Romanian economy, the evolution of small and medium-sized enterprises is tightly connected to multiple causes and to the existence of certain conditions:

- The absence of this sector before the year 1989;
- An adequate legislative frame for the constitution of small and medium-sized enterprises;
- The benefits offered when starting a business;
- The acceleration of national economy privatization;
- The increase of the reorganization phenomenon specific to state companies.

The size of an enterprise is a heterogeneous complex of micro-economic and organizational components, which is approached in different ways. If we refer to the structure configuration and the organizational dimension of a company, these can be influenced by:

- The division of work and the specialization of the performed activities;
- The standardization which refers to the company formalization procedures;
- The extension phenomenon specific to procedures, rules and written communications;
- The structural organization of the enterprise, meaning its general configuration;
- The traditionalism of the enterprise.

Basically, the most important dimensions of a company refer to:

- The structure of company activities;
- Concentration of the specific authority;
- Workflow coordination and control;
- The sizing process of company activities.

The different size of societies can influence: the appearance of dependency relations or domination relations between different enterprises, relations between decision-makers and subordinates, the companies' efficiency degree etc.

If we analyze in detail the size of an enterprise, we can explain at large the competitively differences between various categories of companies. So, there is an ideal organization size, where the long term medium cost increases, and decreases in the opposite situation. In other words, a company's ideal size implies a detailed knowledge of the market capacity, taking into account mainly the dimension of the demand and the situation of sales at a certain moment in time.

Also, the different company sizes can lead to obtaining the same goods for different prices and this means issuing a thorough analysis of both competitively factors and profitability factors present in each organization. The conclusion of these previous facts is that a company's organizational structure differs according to the company's size.

4. SMALL AND MEDIUM-SIZED ENTERPRISES - „MOTORS” OF GLOBAL ECONOMY DEVELOPMENT

In the context of a modern market economy, it is absolutely necessary that small, medium-sized and large enterprises are able to coexist in a rationally proportional balance, each of them having advantages, as well as disadvantages. They generate most of the national income and, at the same time, ensure workplaces for the population.

There are generally various approaches for the definition of small and medium-sized enterprises; these approaches consider different meanings of enterprise sizes and also of the main existing ways of expression and quantification. For example, the Georgia, Atlanta Institute of Technology performed analyses in 75 countries and compiled a synopsis of 50 definitions of small and medium-sized enterprises, which was adopted by the World Bank. (W B, 2010)

In our opinion, the different approaches in defining S.M.E.'s can be grouped as shown in Table 1: (N, 2001)

Table 1 Main types of approaches for the definition of S.M.E's

Current number	Approach categories		
	Criteria	Name	Main characteristic
1.	Economy cover area	General	They set the same S.M.E.'s definition criteria for all economy branches.
		Differential	They set different S.M.E.'s definition criteria, according to their field of activity (industry, commerce, transportation etc.).
2.	Number of used indicators	One-dimensional	They define S.M.E.'s based on a single indicator, most often the number of employees.
		Multidimensional	They define S.M.E.'s based on multiple indicators; the most commonly used are the number of employees, turnover and authorized capital.

Source: Nicolescu, 2001

During the last several years, the general tendency is to approach small and medium-sized enterprises from a general and one-dimensional perspective. This means that the definition of small and medium-sized enterprises is done according to the

„number of employees” indicator, regardless of the branch and the field of activity. This kind of approach is specific to most European countries and is also practiced in Romania.

Nevertheless, the previous approach also has a series of disadvantages, the most important one being the lack of austerity. The fact that the advantages which derive from the use of the previously-mentioned criteria are more important than its disadvantages allows it to be used on a large scale. In this respect, the following advantages can be mentioned:

- It is easy to use;
- It’s periodical quantification in official statistics;
- The economic factors' impossibility to change the company size;
- The possibility to compare companies to one another, even if they belong to different branches and economic fields.

Small and medium-sized enterprises have a series of characteristics which reflect their reduced size and its consequences as regards the embedded activities being designed and made operational. Thus, according to a group of prestigious specialists who issued, under the aegis of U.N.I.D.O., a reference paper in the field of S.M.E.'s their defining characteristics are those in Figure 1. (N, 2001)

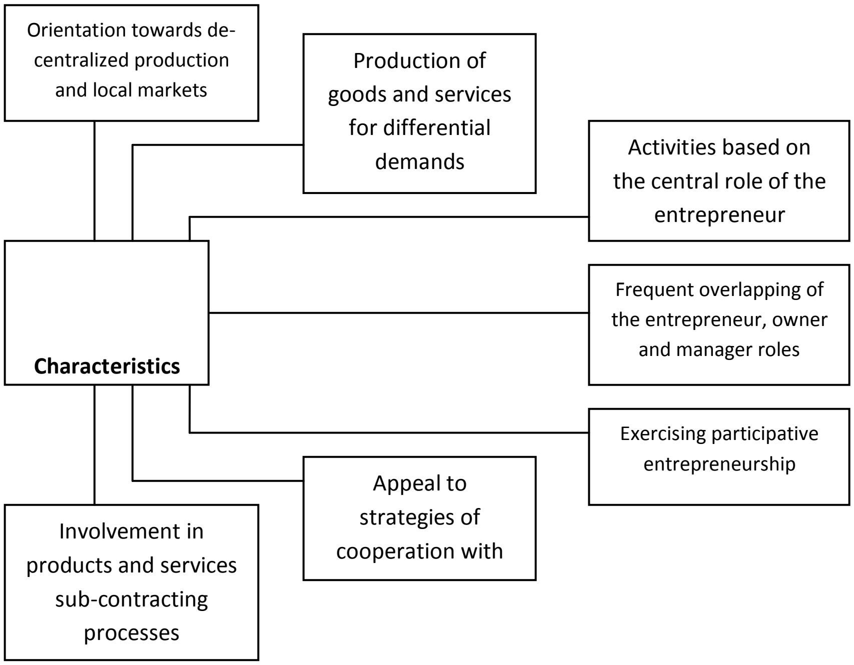
Orientation towards de-centralized production and local markets
Production of goods and services for differential demands
Activities based on the central role of the entrepreneur
Characteristics
Frequent overlapping of the entrepreneur, owner and manager roles
Exercising participative entrepreneurship
Appeal to strategies of cooperation with
Involvement in products and services sub-contracting processes

Figure 1: The dominant characteristics of small-sized enterprises

Another extremely important characteristic adds to the previously-presented ones, that is the high flexibility of small and medium-sized enterprises. This flexibility is mainly due to:

- The small size of small and medium-sized enterprises;
- The entrepreneur's permanent contact with the relations within the company and outside it;

- A favorable climate for organizational innovation and change processes.

So, there are multiple factors which can directly influence the activity performed in small and medium-sized enterprises.

Thus, Japanese professor Tanaka (T, 1998) considers that these factors are:

- Technological innovations;
- Changes in the structure of raw materials;
- Changes which refer to the market demands;
- Changes in the labor force offer;
- Commerce liberalization and globalization;
- Evolutions of the fund sources regime;
- The context of national economy and the internationalization process.

Specialists, among which American professor Bruce Kirhhoff (K, 1998) have determined the major impact of certain variables or factors on activities performed by small and medium-sized enterprises. Based on a thorough analysis of 179.136 S.M.E.'s, he established 6 main factors on which a company's survival depends, as results from the information in Figure 2. The factor with the highest impact on the company's evolution and survival is the entrepreneur's strategic options or choices with regard to the economy branch of the company, the offered goods and/or services, the size of the organization etc. (N, 2001)

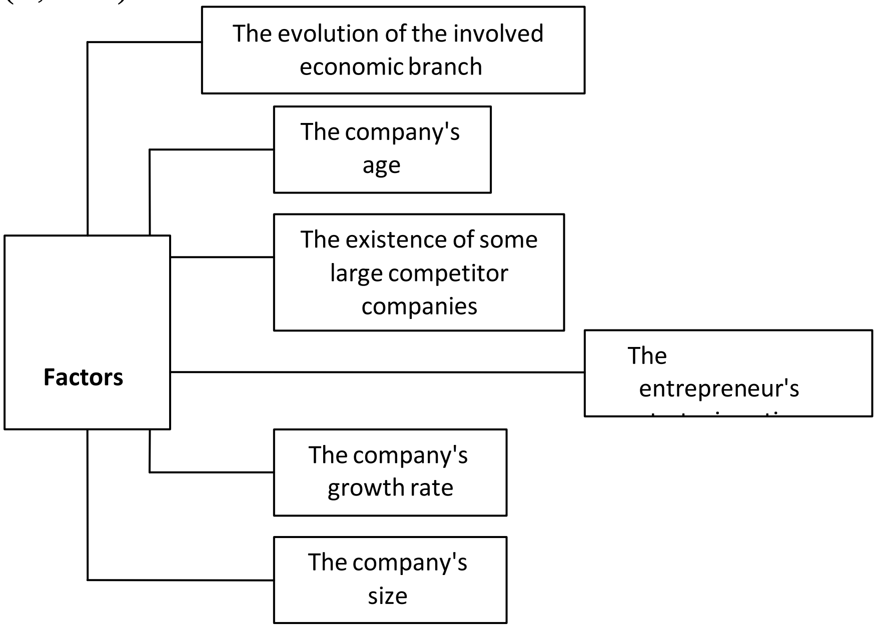
The evolution of the involved economic branch
The company's age
The existence of some large competitor companies
Factors
The entrepreneur's
The company's growth rate
The company's size

Figure 2: The main factors on which an S.M.E.'s survival depends

The typology of small and medium-sized enterprises is a very important theoretical and practical element, so there is an entire range of types according to the involved variables.

The famous consulting company Arthur & Little recently established a new small and medium-sized enterprises typology, Table 2, according to the nature of their activities and innovation and knowledge requirements: (N, 2001)

Table 2 Types of S.M.E.'s

Current number	Type	Definition (characteristics)
1.	Companies based on new technologies	Companies which continuously use advanced technologies in certain fields, characterized by rapid technological progress.
2.	Companies focused on market niches	Companies which successfully turn to profit value added specific to market niches.
3.	Technological leaders companies	Enterprises which, due to their performances, become leaders in a certain sector, promoting their own products.
4.	Companies which develop in (joint) partnership	Enterprises which act as subcontractors, taking part in new products design.
5.	Classic subcontractor companies with good performances	Companies which use subcontractors in order to produce goods usually designed by others.
6.	Resilient companies	Enterprises which reacted successfully, recovering after suffering due to market challenging conditions.
7.	Reactive companies	Enterprises of the previous type, which did not manage to recover.
8.	Passive, „calm” companies	Enterprises which follow their traditional course, without many changes and development.
9.	Companies on the verge of survival	Low performance companies which feel their existence is threatened.

Source: Nicolescu, 2001

Thus, two economy specialists, S. Birley and P. Westhead (B *et al.*, 1990), have established eight classification criteria for small and medium-sized enterprises:

- The company's longevity;
- The form of property;
- The company management's origin;
- The organizational structure;
- The production potential;
- The industry to which the company belongs;
- The product – market relation profile;
- The company's site.

Considering the approach, economists J. Clicha and P.A. Julien considered that the main types of small and medium-sized enterprises are:

- Traditional;
- Entrepreneurial;
- Administrative.

Other authors, like O.F. Collins and D.G. Moore, greatly emphasize the innovation degree of S.M.E.'s, dividing them into:

- Innovative;
- Mimetic;
- Repetitive.

According to J. Fillion (F, 1997), the evolution dynamics criterion divides S.M.E.'s into two types:

- Classic;
- „Comet” type.

In the category of traditional small-sized companies there are, usually, two sub-categories or types:

- Companies which have a single entrepreneur, while the other employees, regardless of their kinship with the entrepreneur, are in the position of performers, without special implication in the company's management;
- Family companies, where the entrepreneur is practically the entrepreneur's family, made up of at least 2 persons, who virtually participate in managing the company's activities; this generates multiple and complex entrepreneurial and management relations. In these companies, there are frequent conflict situations, also generated by family relations meeting with company relations; certain models for facilitating the solving of these conflicts have been issued. Some of these models are: Kopelman, Greenhouse and Connolly and also Stoner, Hartman and Arora. (N, 2001)

In contemporary times, there is great focus on small and medium-sized enterprises which activate in „high-tech” top sectors. According to a piece of research, small and medium-sized enterprises from the mentioned sectors can be structured as such:

- S.M.E.'s which activate in „high-tech” and mass-media sectors and which are prone to performing their activities on the internet, at the same time considering the latest discoveries;
- S.M.E.'s established by self-employed entrepreneurs, which focus on using the opportunities from the services sector, as well as electronic commerce;
- S.M.E.'s embedded in the structure of large companies.

Specialists consider that the three types of small and medium-sized enterprises previously mentioned are the base of the European Union's development, ensuring it both its functioning and its performance.

Presently, a new type of small and medium-sized enterprise gradually shapes up, that is the knowledge-based enterprise, which combines some essential features like:

- Predominance of intangible assets;
- Inclusion of activities which require a wide range of knowledge;
- Use of labor force with a high degree of specialization;
- Speedy development of company research and development activities;
- Use of the latest technological discoveries in the field;
- An offer of goods and services which can be exported;
- The goods and services offered by the company have a relatively short life spam.

Regardless of characteristics and types, S.M.E.'s have – like any other company – a triple dimension:

- Instrumental, which refers to the economic aspects that, in the end, reflect in the company's practicality and efficiency;
- Socio-political, which mainly reflects the organization’s relation and decision elements, where divergent aspects are especially important;

Cultural-reflexive, expression of behavioral values, in fact of the organizational culture which manifests in the company and greatly affects the content and form of manifestation of the previous two dimensions and, implicitly, the performances of S.M.E.'s. (F *et al.*, 1997)
So, small and medium-sized enterprises are companies of relatively small dimensions, but which have a complex variety and a high degree of performance, which ensures the growth of a country's socio-economic performances.

5. THE MEANINGS OF THE TERM „RISK" IN THE COMPLEX BUSINESS FIELD

In the business field, the notion of risk is associated to deprivation of goods (tangible goods and intangible goods), as well as to the company's potential benefits. It is the situation in which the possibility of an unexpected deviation from the expected, predicted or hoped for result manifests.

If we analyze the risk from a business perspective, then it is somewhat different from the general risk. The performance of a business also involves the existence of risk in its purest form, because, in this field, the risk is tightly connected to earnings, to reward.

The notion of risk was and will always be an ongoing preoccupation for different specialists who analyzed this phenomenon. Thus, plenty of theories, concepts, instruments, methods and models appeared which are meant to „facilitate" the transition from abstract to concrete. Nevertheless, it can be said that, for some entrepreneurs, all these tools are too little known and applied, unlike strong companies which have the power to successfully apply them. The specialty economic literature tries to roughly delimit the correct behavior of such an entrepreneur, on the background of an uncertain and risky environment. In the economic environment, „threats" may appear at any level and may be highly varied. In these difficult conditions, each potential entrepreneur must make sure that the performed activity implies as small risks as possible. The first step which they need to take is to identify the risk's emergence and manifestation process. The basic idea is that any entrepreneur must know their business very well, as well as the main characteristics of the environment with which it permanently interacts. This step seems to be the easiest step in a company's struggle with the unforeseen, because most of the risks can be identified long before they actually occur.

The next step is much more difficult, focusing on the assessment of risk occurrence odds and also on the thorough analysis of the major consequences involved. All the observations made along the way and the adjustments that can be made afterwards will become concrete by the correct appreciation of this phenomenon's odds of happening (objective probability).

The major problems occur when the evolution in time of these complex phenomena is forecast. The entrepreneur cannot wait for too long, so that they have the full informational collection at hand, because they are in urgent need for present objective probabilities, not future ones. The correct and real time assessment process of risk occurrence probability and also of their intensity is very complicated and, as a consequence, the help of real specialists in the field is necessary. Nevertheless, also they need concrete and complete information in order to accurately assess the particular nature of the risk and also its level of predictability.

In the context of risk assessment, the fact that it is seldom that specialists, when analyzing a phenomenon perceived as random, have different opinions is not neglected. Based on their own research, one of them might say that there is no <<reason for concern>> - meaning that either the risk occurrence odds are very small or that the effects of a possible occurrence are not assessed as severe. Another expert, studying the same risk, may say that, on the contrary, the issue should cause concern. The results of this type of difference of opinions are plenty everywhere and do not support the public opinion's trust in the field of economic education. There are usually three types of public reaction to these contradictions between specialists; these are:

An economic agent very little familiar to the problems that are the object of polemics, a person often called a <<profane>>, will decide that they cannot rely on the judgment of any specialist and that those alone can find the best answer to the respective issues. As a consequence, they will act according to their own point of view and the results will be seen in time.

Another economic agent, from a second category of reaction, may choose to join the opinions of the expert who backs up their own point of view on the discussed issues. In this way, the individual remains the prisoner of their own level of knowledge and rejects beforehand any valid argument which the other specialist may bring.

At last, a third category is that of economic agents who listen to more opinions in the field, so that, before they form an opinion about the phenomenon, they have already gathered enough information and they have formed a broad vision on the phenomenon. (D, 2006)

It is easy to see that being in the last of these categories is the way to possible success. It should not be overlooked that, when some entrepreneurs can call for the help of specialists in this field, they should not appeal to them willingly. The main reason for this is not only the frequent disputes among specialists, but also a certain approach focused on the „study of perception”, which considers both the psychological and the emotional factors. These factors have a strong impact on the economic behavior of individuals, like many psychologists, such as Slovic, Baruch, and Fischhoff, emphasized. These psychologists analyzed the reactions of certain subjects to different types of risks which can appear in everyday activities. They concluded that, numerous times, certain individuals perceive the risk completely different from specialists in the field. Major problems appear when an insufficiently informed individual is put in the position to make major decisions for the company in a risky and unstable environment.

For a long period of time, the scientific community chose to ignore the public perception of risks, as long as the forecasts led to objective conclusions – although sometimes difficult to understand by non-specialists. For this reason, people became less confident with experts and their prognoses especially that the communication of results was not always done in a clear language, but in a difficult to understand manner. (…) It is obvious that the public's low awareness regarding certain risks and the people's lack of trust in experts makes most of the <<profanes>> avoid those actions which they perceive as very risky. (…) Apparently, there is a social stigma associated to some technologies, places and products which the public perceives as being hazardous, even though, in most cases, scientific evidence suggests no reasons for concern. There is definitely the need for an appropriate publicity of information's and for including the psychological and emotional factors in the risk analysis process. Research shows that regular people have difficulties processing information from experts regarding risky events and this makes it necessary to establish a common language for the two parties, in order for data communication to be made efficiently. (D, 2006)

In some economy dictionaries, the total risk which appears in an economic activity is surprisingly assimilated to the corporate risk, which definitely comprises the common „vision" of two important risks: the financial risk and the economic risk. Other dictionaries refer directly to the concept of profit, which is considered the synthetic expression of a company activity's efficiency. Hirschey and Pappas consider that the business risk is the „chance" to lose, which is directly associated to the management decision. Economist Petru Prunea considers that the business risk manifests within the growth process specific to the company. A higher profit can be obtained through:

- The qualitative increase of assortments;
- Offered products and services diversification;
- Increasing the company's production capacities;
- The use of advanced technologies.

6. CONCLUSIONS

According to the Investment Electronic Encyclopedia, the business risk is the risk which can make a company unable to fulfill its permanent and growing cash-flow needs to cover its operating expenses. Consultancy Company McGladery defines the risk as the event or action which has a great impact and side effects over the company's stability. Both the company's capacity to fulfill its own objectives is influenced, as well as the go-live means of management strategies.

Therefore, it is easily noticeable that, although there is a wide range of opinions, all of these have in common the idea that the rise and manifestation of a risk is a source of potential problems for any company (problems come from the difference between the actual result and the expected result).

It is necessary, for the performance of a company's activities, that the manager issues and applies coherent, functional and efficient strategies, with the purpose of achieving the set goals. In other words, there is a complex relation between strategy and objective from the „risk" concept point of view.

The idea of total risk is fundamental in order to reflect the notion of business risk. It must be said that an entrepreneur's „opportunity" is directly influenced by their permanent preoccupation for the analysis and management of risk in its whole complexity.

The great development of economic activities, permanent novelties which make all risks even more diverse, as well as the multiple ways in which these manifest call for the need of scientific specialty research generalization.

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CHAPTER-6

Forms of market or Types of Market

In common parlance by market is meant a place. Where commodity is bought and sold-but it is rough interpretation of the term.

In economics the term market does not refer to a particular place but it refer to a commodity.e.g.when we say wheat market. We do not refer to a particular place.

The market is a set of conditions in which buyers and sellers come in contect for the purpose of exchange

Economics usually classify market structure on the basis of two criteria-

(1)The number of firms working in the market.
(2)The characteristics of product.

On the basis of these criteria economics consider four important types of market perfect competition is one of them-

(1)Perfect Competition:-

In the study of market structure perfect competition is an important type of market. It has been formulated by classical economist. According to classical economist.

Perfect Competition may be defined as a market situation in which a single market price is ruling for the commodity, which is determined by the forces of total demand and total supply in the market.

Characteristics	Assumptions	Conditions	Features of Perfect competition	

Perfect Competition is said to prevail in the market when the following condition exist-

(i)Large number of buyers and sellers:-

The first condition of perfect competition is that there is a large number of buyers and sellers in the market, in such a situation each individual buyer and seller deal with a very small quantity in market.

Each buyer buys so little and each seller sells so little that none of them is in a position to influence the market.

In other words we can say that in the Perfect Competition there should be large number of firm in the industry. The output of an individual firm is a very small of the total output of the industry therefore an individual firm has no command over the price. But an individual firm has to accept the price. Which is determined in the market by the forces of total supply and total demand.

(ii)Existence of homogeneous product:-

The second important feature of perfect competition is that the product being sold by the various sellers must be homogeneous or identical in eye of buyers. The product are homogeneous in the sense that they are perfectly substitute from the buyers point of view. This ensures that no firm can change a price even slightly above the ruling market price. Because if it does so, the firm will lose all his customers.

(iii)Perfect Knowledge about Market:-

The important condition of perfect competition is the existence of perfect knowledge on the part of buyers and sellers. Since we assume that the buyers have perfect knowledge about the market conditions there is no need to do any expenditure on publicity and advertisement. In this way sellers also possess perfect information especially regarding the market price.qauality of product, number of competitors, substitute etc.

(iv)Non existence of transport costs:-

A perfectly competitive market also assumes the non existence of transport cost. It assume that the various firms so close to each other that there are no transport cost. This condition essential because only then there will prevail a single uniform price for the same product .If transport cost are added to the price of the product even a homogeneous commodity will have different price.

(v)Perfect mobility of factors of production:-

Another important condition of Perfect Competition relates to the perfect mobility of factors of production. This implies that the various factors of production move freely from one occupation to another occupation, from one place to another place. The factors of production move where they get maximum rewards.

(vi)Free entery and exit:-

There is free entery of new firms in to the market.There is no legal-technical,fiannce or any other barrier to their entery.Similarly existing firms are free to leave the market.Thus the mobility of firms eusure that whenever there is scope in the business new firms will enter and competition will be always stuff

When above all conditions are together satisfied in the market, we can say there is a Perfect Competition. But according to Prof.Joel Dean it is a myth of classical economist. It has never existed and it can never exist.

(2)Monopoly:-

The term monopoly is made up of two words.Mono and Poly.Where Mono means Single and Poly means to Sell. Monopoly thus means power to sell alone, in other words when there is only one single seller of a product in the market, that situation will be referred to as monopoly. But this is only a literal meaning of the term Monopoly.

Types of Monopoly:-Actually the term Monopoly in economics is linked with the degree of competition prevailing in the market. on the basis of degree of competition we can classify Monopoly in to two types. They are as under.

(i)Pure or Perfect or absolute Monopoly:-

If in a market there is one single seller of a product and there is no competition at all. The situation will be known as pure-perfect or absolute Monopoly

In technical language we may define pure Monopoly as single firm industry. Where the cross elasticity of demand between the product of the firm and that of other commodity in the market is zero.

Zero cross elasticity implies that there is no substitute (close or far)available in the market.and monopolist has perfect control over the supply of product But in reality there is no pure Monopoly in the market in any commodity.

(ii)Limited, imperfect or relative Monoploy:-

Limited Monopoly is very much realistic market situation-limited monopoly may define as a market situation in which there is a single seller of the product for which there are no close substitute. In other words the substitute of the product is available in the market but they are not close substitute. In this way under imperfect monopoly far substitute are available and therefore the monopolist is not so powerful as the pure monopolist.

In technical language we may defined imperfect monopoly as a single firm industry.Where the cross elasticity of demand between the product of the firm and that of other commodity in the market is small or above zero.

Characteristics or Conditions of Monopoly:-

(i)In monopoly there should be only one seller in the market.

(ii)Monopolist has full control over the supply because he is alone in the market.

(iii)In a monopoly market the monopoly firm itself is the industry-therefore monopoly know as single firm industry.

(iv)In monopoly, firm is in a position to determine the price in this way monopolist is price maker.

(v)The demand curve of monopoly firm is relatively inelastic. It is downward slopping curve. It suggests that the monopolist can sell more output only by reducing the price.

(vi)In monopoly firm is in a position to earn abnormal profit.

(vii)In monopoly the unity of product is homogeneous.

According to Prof Joel dean product under monopoly is lasting distinctiveness. Its distinctiveness lasts for several years-pure monopoly is a myth but imperfect monopoly is a very much realistic.

(3)Monopolistic Competition:-

The term Monopolistic competition is frequently used as synonyms of imperfect competition. This however is wrong because there does exist a distinction between two terms.

According to the classical economist there are only two types of market in market structure.(1)Perfect competition (2)Monopoly- But in actual life it is almost impossible to discover a single commodity which is sold under perfect competition and it is equally difficult to discover example of pure Monopoly. The reality however is to be found somewhere between the two extreme situations. The large majority of markets in real life display the characteristics of both monopoly as well as competition in some the monopoly element predominates while in other competition hold.

Such market situation is referred to as imperfect competition. In other words, imperfect competition is that market situation which lies between the two extremes of perfect competition and Monopoly.

Before 1933 imperfect competition as a market situation did not receive any attention at all. In 1933 Mrs Joan Robinson (Economist of great Britain) Published a book named Economics of imperfect competition and at the same time in America Prof.E.H. Chamberlin Published a book named theory of Monopolistic Competition; in this book they have developed the theory of imperfect competition.

A major difficulty in formulating the theory of imperfect competition is that it takes too many forms, important forms of imperfect competition are (1)Duopoly(2)Oligopoly (3)Monopolistic

From the above discussion it becomes evidence that imperfect competition and Monopollistic competition are not inter changeable term .Imperfect Competition is a much wider and more comprehensive term than monopolistic competition.Infact Monopolistic Competition is only one of the Many sub-categories of imperfect Competition.

Characteristics of Monopolistic Competition:-

(1)Existence of many Firms:-

We have seen that under Perfect Competition there is a large number of firms working in industry.and we have also seen that under monopoly there is only one firm.While under Monopolistic Competition there are many firms working in the industry.each of them producing differentiated product which are relatively close substitute for each other,under Monopolistic Competition there does not exist only one firm as in Monopoly at the same time the number of firm is not so large as under Perfect Competition here the number of firm is fairly large and therefore the size of the each firm under Monopolistic Competition is small.As result an individual firm has relatively small part of the total output.So that any action on its part to increase or decrease the output and price will have little or no effect on the rival firms.

(2)Product differentiation:-

The second important Characteristic of Monopolistic Competition is product differentiation this means that the various firms under monopolistic competition produce not homogeneous or identical product but differentiated product which are closely related to each other. According to Prof.Stonier and Hague product differentiation means that the product are different in some way but not altogether so.

Product differentiation can be bought by various way.

(i)The firms may bring about product differentiation through quality.

(ii)The firms may bring about product differentiation by offering to their customers supplementary and other services along with the sale of the product.

(iii)The firms may bring about product differentiation by advertisement and publicity .This known as sales promotion.

(3)Easy entry and exist:-

The third important feature of Monopolistic Competition is that there is no difficulty for a new comer or an existing firm to leave the industry. And it is due to simplicity of production technique and smallness of capital requirement.

(4)Existence of selling cost:-

The important condition of Monopolistic Competition is the existence of selling cost. Under perfect Competition various firm produce identical Commodity. and there is perfect knowledge of market. Selling cost therefore is not necessary. Under Monopoly there is only one firm in industry. There is no competition at all therefore here selling cost becomes unnecessary. But under Monopolistic Competition there is a fairly large number of firms and each one producing differentiated products which are relatively close substitutes for each other. Therefore it becomes essential for the firm to do selling cost.

(5)Different prices for differentiated product:-

We have seen under Perfect Competition each firm produces a homogeneous product and there is Perfect knowledge of market .Therefore there is a single price ruling in the market. But under Monopolistic Competition each firm produces a differentiated product and consumer has no perfect knowledge about the market condition. Therefore here prices are different.

(6)Control over the Price:-

We know that under Perfect Competition an individual firm has no control over the price. Because it is one of the very many firms in the industry. But under Monopolistic Competition this is not so because of the product differentiation. Each firm has partially independent market.and there fore it has some control over the price.

(4)Oligopoly:-

The term Oligopoly is made up of two words.Oligos and Pollen .Where Oligos means a few and Pollen means to sell. Thus Oligopoly is that form of imperfect competition where there are few firm in market producing either an homogeneous or differentiated product which are closely substitute.

According to Prof.George Stigler-Oligopoly is that market situation in which a firm formulates its market policy in part on the expected behavior of few close rivals.

Oligopoly is a real world market situation. Even in India we find that very few firms are controlling the whole market in certain commodities.Moter car industry in India is an example of Oligopoly.

Characteristics of Oligopoly:-

(1)Few firms are working in the industry.Number of firms should be between 3 to 20 in Oligopoly market.

(2)The sellers supply either homogeneous product or differentiated product.

(3)The firm has a high degree of interdependence in their business policy about fixing of price and determination of output.

(4)The product under Oligopoly contain high degree of cross elasticity of demand.

(5)Advertising and selling costs have strategic importantance in an oligopoly market.

(6)Competition is of unique type in an Oligopolistic market.each firm has to make constant struggle with rivals.

(7)There are two conflicting attitudes on the part of the firm operating in the market in Oligopoly.

- To remain independent in decision making.
- At times each firm desires to combine or unite together to maximize the profit.

(8)The pre-dominant element of monopoly is present in Oligopoly.

(9)Each firm prefers to follow rigid price policy in Oligopoly market. therefore there is a kinked demand curve.

(10)In economics Oligopoly is known as cat mouse competition.

Types of Shares

“A share is the interest of the shareholder in the company. It is measured by the sum of money for the purpose of liability in the first place and of interest in the second place”. Holders of the shares are called shareholders or members of the company. The share of a company shall be a moveable property. It is transferable in the manner provided by the articles of the company. The share capital is non refundable except in the case of winding up and reduction of capital. Each share in a company shall have a distinctive number.

Types of Shares

Basically there are three types of shares into which the whole capital of the company is divided.

1. Equity shares
2. Preference shares
3. Deferred Shares

1. Equity Shares

Equity share are also called ordinary shares. The holders of equity shares are the real owners of a company. The ordinary shareholders have voting rights in the meetings of the company. They are entitled to receive dividend as are declared by the board of directors. The equity share capital cannot be redeemed during the life time of the company.

Merits of Equity Shares

The merits of equity shares are as under:-

01- Venture capital. Equity Shares are the most important and popular type of shares. It is therefore, called a venture capital of the company.

02- No burden on a company’s resources. Since the dividend is to be paid out of the profit of the company, therefore they impose no load on the resources of a company.

03- Provision of long term finance. The equity shares provide long term finance to the company.

04- No charge on the assets. The equity shares do not create any charge on the assets of a company. The Company can raise further funds. If it desires, through mortgage of property or other assets.

05- Payment of profit. Equity shareholders are paid profit after all the other claims are met by the company.

06- Rate of dividend. The rate of dividend on ordinary shares depends upon the profit of the company.

2. Preferences Shares

Preferences Share as the name suggested, it has certain preferences as compared to other types of shares. The main preferences of these shareholders over others in brief are as under:-

1. The first preference is for compensation of dividend. Whenever the company distributes profits, the dividend is first paid on preferences share capital.
2. In case of winding up the company, the preferences shareholders have a prior right in regard to repayments of capital.

Classes of Preferences Shares

The main types of preference shares are as under:-

01- Cumulative preference shares. In this type of preference share, dividends were paid also for those years in which no profit is earned. Whenever, the company declares profits, the cumulative preference shares are paid dividend for all the previous years in which dividend could not be declared.

02- Non cumulative preference shares. In this type of preference shares, the holders do not have any claim regarding amount outstanding of dividend. They are paid dividend if a company earns profit.

03- Convertible preference shares. The convertible preference shares are those which the holders can convert into equity shares at specified period of time. The right of conversion is to be authorized by the Articles of Associations of the company.

3. Deferred Shares

Deferred Shares are also called founders Shares. They were used to be issued to the promoters of the company. Dividend on deferred shares was paid after the claim of all other shareholders has been met including equity shareholders. The deferred shareholder has one vote. These shares enabled the promoters to control the working of the company with a very small investment.