**12**Global Marketing Channels and Physical Distribution

Learning Objectives

1. [**12-1 Identify and compare the basic structure options for consumer channels and industrial channels.**](https://jigsaw.vitalsource.com/books/9780134899763/epub/OPS/xhtml/fileP700101539500000000000000000373E.xhtml#P700101539500000000000000000373E)
2. [**12-2 List the guidelines companies should follow when establishing channels and working with ­intermediaries in global markets.**](https://jigsaw.vitalsource.com/books/9780134899763/epub/OPS/xhtml/fileP7001015395000000000000000003795.xhtml#P7001015395000000000000000003795)
3. [**12-3 Describe the different categories of retail operations that are found in various parts of the world.**](https://jigsaw.vitalsource.com/books/9780134899763/epub/OPS/xhtml/fileP70010153950000000000000000037B7.xhtml#P70010153950000000000000000037B7)
4. [**12-4 Compare and contrast the six major international transportation modes and explain how they vary in terms of reliability, accessibility, and other performance metrics.**](https://jigsaw.vitalsource.com/books/9780134899763/epub/OPS/xhtml/fileP7001015395000000000000000003908.xhtml#P7001015395000000000000000003908)

**Case 12-1 Welcome to the World of Fast Fashion**

The world of global fast-fashion is like a three-way horse race. Spain’s Inditex SA is the parent company of specialty retailer Zara; Sweden is home to Hennes & Mauritz AB, better known to shoppers as H&M; and Uniqlo is the flagship brand of Japan’s Fast Retailing.

Part of the appeal of fast fashion is the low prices. Also attractive is the speed at which ­inventories are replenished and updated with affordable versions of the latest runway trends from the world’s ­fashion capitals. The need for speed is fueled in part by social media. A key element for some fast-fashion brands is sourcing clothing from countries with low-cost labor in Asia and elsewhere. In Cambodia, for example, more than 400 garment factories are registered exporters.

However, some industry observers note that low prices actually carry high social and environmental costs. Chasing the latest trends means that shoppers often discard inexpensive garments after wearing them just a few times. This leads to a consumer mindset that clothing purchases are disposable, rather than long-term investments. Critics assert that unwanted clothing often ends up in landfills, and that the fast-fashion trend is not sustainable (see [**Exhibit 12-1**](https://jigsaw.vitalsource.com/books/9780134899763/epub/OPS/xhtml/fileP7001015395000000000000000003719.xhtml?create=true&favre=brett#P700101539500000000000000000372D)).

**Exhibit 12-1**

Some critics assert that the fast fashion trend contributes to overproduction and a “throw-away” mentality. The result is vast quantities of discarded clothing as well as "deadstock" (out-of-season garments and unused textiles). This Saks Fifth Avenue window display by Vetements was designed to call attention to the problem.

*Source: Michael Ross Photography.*

For years, Tadashi Yanai, the founder of the Uniqlo (“Unique Clothing”) chain, pursued a business model that differentiated his company from its European rivals. Uniqlo’s focus was on everyday basics and a new-product development process that relied heavily on innovative materials.

Inditex is the world’s largest fashion retailer, with more than 7,000 stores in 92 countries. In addition to Zara, its brands include Bershka, Pull & Bear, and Massimo Dutti. The company does not advertise, and its motto is “The company doesn’t speak; the customer speaks for the company.” Unlike some of its competitors, Inditex keeps nearly two-thirds of its production in Spain or neighboring countries.

Zara entered India in 2010, and today has more than 18 stores in that country; H&M has been in India since 2015. Global fashion trends are the mainstay in fast fashion. However, many women’s fashions can be considered “racy” because they feature plunging necklines, deep backs, and exposed midriffs. An Indian company, Future Group, has invested in Cover Story, a brand of Western-style clothing with more-modest tailoring that better suits the tastes and needs of Indian shoppers. The clothes also feature brighter colors. In a perhaps unexpected twist, Cover Story has a design studio in London. As Future Group CEO Kishore Biyani explains, “You can’t take on the Zara’s and H&M’s of the world sitting in India. You need to look and feel what they do to beat them at their own game.”

Prior to 2017, H&M was growing at a torrid pace. Revenue growth was driven by store openings; today, the company has approximately 4,700 stores. However, profits have been stagnant, and the company is feeling pressure from several directions. Discount retailer Primark has lower prices, while some shoppers perceive Zara to offer higher quality. Moreover, online-only competitors, ­including Britain’s Asos and Germany’s Zalando, offer free shipping and generous return policies that lure customers away from brick-and-mortar stores. One industry analyst likens H&M’s position to that of former industry titans such as Nokia, Ericsson, and IBM: All had successful business models until market conditions changed faster than their respective managements realized it.

Specialty retailers such as Zara, H&M, and Uniqlo are just three of the many elements that make up distribution channels around the globe. Today, global supply chains connect producers in all parts of the world, and sophisticated logistics are utilized to ensure the smooth flow through the system. The American Marketing Association defines a [**channel of distribution**](https://jigsaw.vitalsource.com/books/9780134899763/epub/OPS/xhtml/fileP7001015395000000000000000004BB6.xhtml#P7001015395000000000000000004C58) as “an organized network of agencies and institutions that, in combination, perform all the activities required to link producers with users to accomplish the marketing task.”[**1**](https://jigsaw.vitalsource.com/books/9780134899763/epub/OPS/xhtml/fileP7001015395000000000000000003AA7.xhtml#P7001015395000000000000000003AAB) Physical distribution is the movement of goods through channels; channels, in turn, are made up of a coordinated group of individuals or firms that perform functions that add utility to a product or service.

Distribution channels are one of the most highly differentiated aspects of national marketing systems. Retail stores vary in size from giant hypermarkets to small stores in Latin America called *­pulperías*. The diversity of channels and the wide range of possible distribution strategies and market-entry options can present challenges to managers who are responsible for designing global marketing programs. Channels and physical distribution are crucial aspects of the total marketing program; without them, a great product at the right price and effective communications mean very little.

12-1 Distribution Channels: Objectives, Terminology, and Structure

1. **12-1**Identify and compare the basic structure options for consumer channels and industrial channels.

Marketing channels exist to create utility for customers. The major categories of channel utility are [**place utility**](https://jigsaw.vitalsource.com/books/9780134899763/epub/OPS/xhtml/fileP7001015395000000000000000004BB6.xhtml#P7001015395000000000000000004FA2) (the availability of a product or service in a location that is convenient to a ­potential ­customer), [**time utility**](https://jigsaw.vitalsource.com/books/9780134899763/epub/OPS/xhtml/fileP7001015395000000000000000004BB6.xhtml#P70010153950000000000000000050A8) (the availability of a product or service when desired by a customer), [**form  ­utility**](https://jigsaw.vitalsource.com/books/9780134899763/epub/OPS/xhtml/fileP7001015395000000000000000004BB6.xhtml#P7001015395000000000000000004DE5) (the availability of the product processed, prepared, in proper condition, and/or ready to use), and [**information utility**](https://jigsaw.vitalsource.com/books/9780134899763/epub/OPS/xhtml/fileP7001015395000000000000000004BB6.xhtml#P7001015395000000000000000004E8B) (the availability of answers to questions and general ­communication about useful product features and benefits). Because these utilities can be a basic source of ­competitive ­advantage and represent an important element of a firm’s overall value ­proposition, choosing a channel ­strategy is one of the key policy decisions that management must make. For example, the Coca-Cola ­Company’s global marketing leadership position is based in part on its ability to put Coke “within an arm’s reach of desire”—in other words, to create place utility.

The starting point in selecting the most effective channel arrangement is a clear focus of the company’s marketing effort on a target market and an assessment of the way(s) in which ­distribution can contribute to the firm’s overall value proposition. Who are the target customers, and where are they located? What are their information requirements? What are their preferences for service? How sensitive are they to the product’s or service’s price? Moreover, each market must be analyzed to determine the cost of providing channel services.

What is appropriate in one country may not be always effective in another. Even marketers concerned with a single-country program should study channel arrangements in different parts of the world for valuable information and insight into possible new channel strategies and tactics. For example, retailers in Europe and Asia studied self-service discount retailing in the United States and then introduced the self-service concept in their own countries. Similarly, governments and business executives from many parts of the world have examined Japanese trading companies to learn from their success. Walmart’s formula has been closely studied and adapted by competitors in the markets it has entered.

As mentioned previously, distribution channels are systems that link manufacturers to customers. Although channels for consumer products and industrial products are similar, there are also some distinct differences between them. In [**business-to-consumer marketing**](https://jigsaw.vitalsource.com/books/9780134899763/epub/OPS/xhtml/fileP7001015395000000000000000004BB6.xhtml#P7001015395000000000000000004C2C) (also known as b-to-c or B2C marketing), consumer channels are designed to put products in the hands of people for their own use. By contrast, [**business-to-business marketing**](https://jigsaw.vitalsource.com/books/9780134899763/epub/OPS/xhtml/fileP7001015395000000000000000004BB6.xhtml#P7001015395000000000000000004C29) (also known as b-to-b or B2B marketing) involves industrial channels that deliver products to manufacturers or other organizations that then use them as inputs in the production process or in day-to-day operations. Intermediaries play important roles in both consumer and industrial channels. A [**distributor**](https://jigsaw.vitalsource.com/books/9780134899763/epub/OPS/xhtml/fileP7001015395000000000000000004BB6.xhtml#P7001015395000000000000000004D49) is a wholesale intermediary that typically carries product lines or brands on a selective basis. An [**agent**](https://jigsaw.vitalsource.com/books/9780134899763/epub/OPS/xhtml/fileP7001015395000000000000000004BB6.xhtml#P7001015395000000000000000004BE1) is an intermediary who negotiates exchange transactions between two or more parties but does not take title to the goods being purchased or sold.

Consumer Products and Services

[**Figure 12-1**](https://jigsaw.vitalsource.com/books/9780134899763/epub/OPS/xhtml/fileP700101539500000000000000000373E.xhtml?favre=brett#P7001015395000000000000000003756) summarizes six channel structure alternatives for consumer products. The characteristics of both buyers and products have an important influence on channel design. The first alternative is to market directly to buyers via the Internet, mail order, various types of door-to-door selling, or manufacturer-owned retail outlets. The other options use retailers and various combinations of sales forces, agents/brokers, and wholesalers. The number of individual buyers and their geographic distributions, incomes, shopping habits, and reactions to different selling methods frequently vary from country to country and may require different channel approaches.

**Figure 12-1 Marketing Channel Alternatives: Consumer Products**

Product characteristics such as degree of standardization, perishability, bulk, service requirements, and unit price have an impact as well. Generally speaking, channels tend to be longer (require more intermediaries) as the number of customers to be served increases and the price per unit decreases. Bulky products usually require channel arrangements that minimize shipping distances and the number of times products change hands before they reach the ultimate customer.

The Internet and related forms of new media are dramatically altering the distribution landscape. For example, eBay pioneered the [**peer-to-peer marketing**](https://jigsaw.vitalsource.com/books/9780134899763/epub/OPS/xhtml/fileP7001015395000000000000000004BB6.xhtml#P7001015395000000000000000004F93) (p-to-p) model, whereby individual consumers market products to other individuals. eBay’s success was one reason that traditional merchants quickly recognized the Internet’s potential. To sustain revenue growth, eBay began assisting large companies such as Disney and IBM in setting up online “storefronts” to sell items for fixed prices in addition to conducting b-to-c auctions. “As we evolved from auction-style bidding to adding Buy It Now, the logical next step for us was to give sellers a place to showcase their listings,” said Bill Cobb, eBay’s senior vice president for global marketing.[**2**](https://jigsaw.vitalsource.com/books/9780134899763/epub/OPS/xhtml/fileP7001015395000000000000000003AA7.xhtml#P7001015395000000000000000003AAD) Some observers predict that interactive television (ITV) will also become a viable direct-distribution channel in the coming years as more households are wired with the necessary two-way technology. Time-pressed consumers in many countries are increasingly attracted to the time and place utility created by the Internet and similar new media technologies.

Low-cost mass-market products and certain services can be sold on a door-to-door basis via a direct sales force. Door-to-door and house-party selling is considered a mature channel in the United States; however, it is now growing in popularity elsewhere. For example, Orlando, Florida–based Tupperware has a sales force of 200,000 in Indonesia. Brand-conscious consumers there have embraced the company’s plastic food-storage containers, and Tupperware’s direct-sales business model gives it an advantage in a country with a limited retail infrastructure (see [**Exhibit 12-2**](https://jigsaw.vitalsource.com/books/9780134899763/epub/OPS/xhtml/fileP700101539500000000000000000373E.xhtml?favre=brett#P700101539500000000000000000375E)). Today, Indonesia is Tupperware’s biggest market. As former CEO and current executive chairman Rick Goings notes, “This is an incredible sweet spot for us. It’s where the population of the world is. You cannot fight that.”[**3**](https://jigsaw.vitalsource.com/books/9780134899763/epub/OPS/xhtml/fileP7001015395000000000000000003AA7.xhtml#P7001015395000000000000000003AAF)

**Exhibit 12-2**

Tricia Stitzel became CEO of Tupperware in 2018. According to former CEO and current executive chairman Rick Goings, “The United States is less than 10 percent of our business. We happen to have our headquarters in the United States, but we’re a global company.”[**4**](https://jigsaw.vitalsource.com/books/9780134899763/epub/OPS/xhtml/fileP7001015395000000000000000003AA7.xhtml#P7001015395000000000000000003AB1)

*Source: Edward Linsmier Photography.*

In 1995, Mary Kay entered the Chinese cosmetics market with its network of independent sales agents. After successfully penetrating China’s first-tier cities, the company expanded into second- and third-tier locations.[**5**](https://jigsaw.vitalsource.com/books/9780134899763/epub/OPS/xhtml/fileP7001015395000000000000000003AA7.xhtml#P7001015395000000000000000003AB3) In April 1998, China’s state council imposed a blanket ban on all types of direct selling. Because the ban was aimed most directly at illegal pyramid schemes, several foreign companies, including Amway, Avon, Mary Kay, and Tupperware, were allowed to continue operations in China. However, they were forced to adapt their business models: Their sales agents had to be affiliated with brick-and-mortar retailers. Although the ban was lifted in 2005, because it had restricted competition, the handful of foreign direct-sales marketers that had maintained a presence in China had had a unique growth opportunity during the years the ban was in force. Mary Kay is a case in point: By 2011, Mary Kay’s Chinese sales were more than 50 times higher than they had been in 1999. Today, Mary Kay has dozens of branch offices in China.

In Japan, the biggest barrier facing U.S. auto manufacturers isn’t high tariffs, but rather the fact that half the cars that are sold each year are sold door-to-door. Toyota and its Japanese competitors do maintain showrooms, but they also employ more than 100,000 car salespeople. Unlike their American counterparts, many Japanese car buyers never visit dealerships. The close, long-term relationships between auto salespersons and the Japanese people can be thought of as a consumer version of the *keiretsu* system discussed in [**Chapter 9**](https://jigsaw.vitalsource.com/books/9780134899763/epub/OPS/xhtml/fileP7001015395000000000000000002BDB.xhtml#P7001015395000000000000000002BDB).

Japanese car buyers expect numerous face-to-face meetings with a sales representative, during which trust is established. The relationship continues after the deal is closed; sales reps send cards and continually seek to ensure the buyer’s satisfaction. American rivals such as Ford, meanwhile, try to generate showroom traffic. In the 1990s, Nobumasa Ogura managed a Ford dealership in Tokyo. “We need to come up with some ideas to sell more cars without door-to-door sales, but the reality is that we haven’t come up with any,” he said.[**6**](https://jigsaw.vitalsource.com/books/9780134899763/epub/OPS/xhtml/fileP7001015395000000000000000003AA7.xhtml#P7001015395000000000000000003AB5) As it turned out, the challenge proved to be insurmountable, and Ford pulled out of the Japanese market in 2016.[**7**](https://jigsaw.vitalsource.com/books/9780134899763/epub/OPS/xhtml/fileP7001015395000000000000000003AA7.xhtml#P7001015395000000000000000003AB7)

Another direct-selling alternative is the *manufacturer-owned store* or *independent franchise store*. One of the first successful U.S.-based international companies, Singer, established a worldwide chain of company-owned and operated outlets to sell and service sewing machines. As noted in [**Chapter 9**](https://jigsaw.vitalsource.com/books/9780134899763/epub/OPS/xhtml/fileP7001015395000000000000000002BDB.xhtml#P7001015395000000000000000002BDB), Japanese consumer electronics companies integrate stores into their distribution groups. Apple, Levi Strauss, Nike, Sony, well-known fashion design houses, and other companies with strong brands sometimes establish flagship retail stores as product showcases or as a means of obtaining marketing intelligence (see [**Exhibit 12-3**](https://jigsaw.vitalsource.com/books/9780134899763/epub/OPS/xhtml/fileP700101539500000000000000000373E.xhtml?favre=brett#P700101539500000000000000000376B)). These stores are designed to provide an interactive shopping experience and build brand loyalty.[**8**](https://jigsaw.vitalsource.com/books/9780134899763/epub/OPS/xhtml/fileP7001015395000000000000000003AA7.xhtml#P7001015395000000000000000003AB9) Such channels supplement, rather than replace, distribution through independent retail stores.

**Exhibit 12-3**

Apple operates more than 500 retail stores in 22 countries. Each store features a Genius Bar, where customers can seek one-on-one technical support with a knowledgeable employee. Many stores, such as this one in London, feature a signature glass staircase that Apple cofounder and former CEO Steve Jobs helped design. Although Jobs died of cancer in 2011, his legacy includes a far-reaching impact on global retailing strategies and tactics. Apple recently hired Angela Ahrendts, former CEO of Burberry, to head its retail operations.

*Source: View Pictures/UIG via Getty Images.*

Other channel structure alternatives for consumer products include various combinations of a manufacturer’s sales force and wholesalers calling on independent retail outlets that, in turn, sell to customers (retailing is discussed in detail later in the chapter). For mass-market consumer products such as ice cream novelties, cigarettes, and light bulbs that are bought by millions of consumers, a channel that links the manufacturer to distributors and retailers is generally required to achieve market coverage. A cornerstone of Walmart’s phenomenal growth in the United States has been its ability to achieve significant economies by buying huge volumes of goods directly from manufacturers. By contrast, some companies elect to pursue very selective distribution strategies to ensure that products are displayed in attractive surroundings. For example, menswear designer Alexandre Plokhov’s collections have been available at Barney’s and Selfridge’s; Plokhov recently launched a new line, Nomenklatura, that will be available online only (see [**Exhibit 12-4**](https://jigsaw.vitalsource.com/books/9780134899763/epub/OPS/xhtml/fileP700101539500000000000000000373E.xhtml?favre=brett#P7001015395000000000000000003775)).

**Exhibit 12-4**

Alexandre Plokhov is a menswear designer with a noir sensibility. Some of his designs—these combat boots, for example—are inspired by vintage military uniforms. After launching Cloak and the eponymous Alexandre Plokhov lines, he designed for Versace and Helmut Lang. His new venture is called Nomenklatura.

*Source: © NomenklaturaStudio.*

Perishable goods impose special demands on channel members, who must ensure that the merchandise (e.g., fresh fruits and vegetables) is in satisfactory condition (form utility) at the time of customer purchase. In developed countries, either a company’s own sales force or independent channel members may handle distribution of perishable food products. In either case, the distributor organization checks the stock to ensure that it is fresh. In less-developed countries, public marketplaces are important channels; they provide a convenient way for producers of vegetables, bread, and other food products to sell their goods directly. Notably, the high perishability rate for fresh produce is one of the biggest supply-chain issues in modern India.

Sometimes, a relatively simple channel innovation in a developing country can significantly increase a company’s overall value proposition. In the early 1990s, for example, the Moscow Bread Company (MBC) needed to improve its distribution system. Russian consumers queue up daily to buy fresh loaves at numerous shops and kiosks. Unfortunately, MBC’s staff was burdened by excessive paperwork, which resulted in the delivery of stale bread. Andersen Consulting found that as much as one-third of the bread the company produced was wasted. In developed countries, approximately 95 percent of food is sold packaged; the figure is much lower in the former Soviet Union. Whether a consumer bought bread at an outdoor market or in an enclosed store, it was displayed unwrapped. The consulting team thus devised a simple solution—plastic bags to keep the bread fresh. Russian consumers responded favorably to the change; not only do the bags guarantee freshness and significantly extend the bread’s shelf life, but the bags themselves also create utility. In a country where such extras are virtually unknown, the bags constitute a reusable “gift.”[**9**](https://jigsaw.vitalsource.com/books/9780134899763/epub/OPS/xhtml/fileP7001015395000000000000000003AA7.xhtml#P7001015395000000000000000003ABB)

The retail environment in developing countries presents similar challenges for companies marketing nonperishable items. In affluent countries, Procter & Gamble (P&G), Kimberly-Clark, Unilever, Colgate-Palmolive, and other global consumer-products companies are accustomed to catering to a “buy-in-bulk” consumer mentality. By contrast, in Mexico and other emerging markets, many consumers shop for food, soft drinks, and other items several times each day at tiny, independent “mom-and-pop” stores, kiosks, and market stalls (see [**Exhibit 12-5**](https://jigsaw.vitalsource.com/books/9780134899763/epub/OPS/xhtml/fileP700101539500000000000000000373E.xhtml?favre=brett#P7001015395000000000000000003781)). The products offered, including shampoo, disposable diapers, and laundry detergent, are packaged in single-use quantities at a relatively high per-use cost.

**Exhibit 12-5**

Brazil’s middle class is growing rapidly, but reaching consumers in far-flung rural areas can be a challenge for global marketers. Nestlé’s channel strategy includes a floating supermarket. Nestlé Até Você a Bordo (“Nestlé Takes You on Board”) is a boat that travels the Amazon by night and welcomes shoppers in 18 different municipalities by day. Consumers who don’t have access to hypermarkets can stock up on dog food, chocolates, powdered milk, and nearly 300 other Nestlé products and brands.

*Source: Marcia Zoet/Bloomberg via Getty Images.*

At P&G, these operations are known as “high-frequency stores”; in Mexico alone, an estimated 70 percent of the population shops at such stores. To motivate shopkeepers to stock more of P&G’s products, the company launched a “golden store” program. In exchange for a pledge to carry at least 40 different P&G products, participating stores receive regular visits from P&G representatives, who tidy display areas and arrange promotional material in prominent places. Although P&G initially used its own sales force for these activities, it has since begun relying on independent agents who buy inventory (paying in advance) and then resell the items to shop ­operators.[**10**](https://jigsaw.vitalsource.com/books/9780134899763/epub/OPS/xhtml/fileP7001015395000000000000000003AA7.xhtml#P7001015395000000000000000003ABD) P&G’s experience illustrates the fact that the channel structures shown in [**Figure ­12-1**](https://jigsaw.vitalsource.com/books/9780134899763/epub/OPS/xhtml/fileP700101539500000000000000000373E.xhtml?favre=brett#P7001015395000000000000000003756) represent strategic alternatives; firms can and should vary their strategies as market conditions change.

Industrial Products

[**Figure 12-2**](https://jigsaw.vitalsource.com/books/9780134899763/epub/OPS/xhtml/fileP700101539500000000000000000378A.xhtml?favre=brett#P700101539500000000000000000378D) summarizes marketing channel alternatives for an industrial or business products ­company. As is true with consumer channels, product and customer characteristics have an impact on channel structure. Three basic elements are involved: the manufacturer’s sales force, ­distributors or agents, and wholesalers. A manufacturer can reach customers with its own sales force, a sales force that calls on wholesalers who sell to customers, or a combination of these two arrangements. A manufacturer can also sell directly to wholesalers without using a sales force, and wholesalers, in turn, can supply customers.

**Figure 12-2 Marketing Channel Alternatives: Industrial Products**

Italy’s Saeco distributes its products through both b-to-c and b-to-b channels. Marketing ­managers responsible for domestic appliances arrange for retail distribution for consumer purchase. The managers who service the vending and professional segments provide vending machines to organizational customers and professional espresso-making equipment to bars and cafés.

Channel innovation can be an essential element of a successful marketing strategy. Dell’s rise to a leading position in the global PC industry was fueled by Michael Dell’s decision to bypass conventional channels and instead sell direct and build computers to customers’ specifications. Dell began life as a b-to-b marketer; its business model proved so successful that the company then began marketing directly to the home PC market.

As another example, consider Boeing aircraft: Given the price, physical size, and complexity of a jet airliner, it is easy to understand why Boeing utilizes its own sales force. Other products sold in this way include mainframe computers and large photocopy systems—both are expensive, complicated products that require both explanation and applications analysis focused on each customer’s needs. A company-trained salesperson, sales engineer, or sales team is well suited for the task of creating information utility for computer buyers.

# 12-2 Establishing Channels and Working With Channel Intermediaries

1. **12-2**List the guidelines ­companies should follow when ­establishing channels and ­working with intermediaries in global markets.

A global company expanding across national boundaries must either utilize existing [**­distribution  channels**](https://jigsaw.vitalsource.com/books/9780134899763/epub/OPS/xhtml/fileP7001015395000000000000000004BB6.xhtml#P7001015395000000000000000004D46) or build its own. Channel obstacles are often encountered when a ­company enters a competitive market where brands and supply relationships are already established. If management chooses *direct involvement*, the company establishes its own sales force or operates its own retail stores.

The other option is *indirect involvement*, which entails utilizing independent agents, ­distributors, and retailers. In Asia, for example, Western luxury goods marketers such as Jean Paul Gaultier (France) and Harmont & Blaine (Italy) have long relied on non-exclusive, independent distributors. One such company is Hong Kong–based Fairton International Group, whose local market knowledge and network of stores are keys to success in Greater China. Similarly, as noted in [**Chapter 11**](https://jigsaw.vitalsource.com/books/9780134899763/epub/OPS/xhtml/fileP7001015395000000000000000003306.xhtml#P7001015395000000000000000003306), DeBeers uses independent intermediaries to market its diamonds in the United States.

The channel strategy used in a global marketing program must fit with the company’s ­competitive position and overall marketing objectives in each national market. Direct ­involvement in distribution in a new market can entail considerable expense, as sales representatives and sales management must be hired and trained. The sales organization will inevitably be a massive loser in its early stages of operation in a new market because it will not have sufficient volume to cover its overhead costs. Therefore, any company contemplating establishing its own sales force should be prepared to underwrite its losses for a reasonable period of time.

Channel decisions are important because of the number and nature of relationships that must be managed. Channel decisions typically involve long-term legal commitments and obligations to various intermediaries. Such commitments are often extremely expensive to terminate or change, so it is imperative for companies to document the nature of the relationship with the foreign partner. As the saying goes, “The shortest pencil is better than the longest memory.” At a minimum, the written agreement should include a definition of what constitutes “good cause” for termination. Also, as noted in [**Chapter 5**](https://jigsaw.vitalsource.com/books/9780134899763/epub/OPS/xhtml/fileP700101539500000000000000000187D.xhtml#P700101539500000000000000000187D), it is often preferable to settle business disputes through arbitration rather than in a local court. Thus, the distributor or agent agreement should provide for arbitration in a neutral forum in a third country. In many instances, local laws protect agents and distributors; thus, even in the absence of a formal written agreement, the law will be applied in a civil-law country. In addition to written obligations, commitments must be backed by good faith and feelings of mutual obligation. In short, the careful selection of distributors and agents in a target market is critically important.

Companies entering emerging markets for the first time must exercise particular care in choosing a channel intermediary. Typically, a local distributor is required because the market entrant lacks knowledge of local business practices and needs a partner with links to potential customers. In addition, newcomers to a particular market generally want to limit their risk and financial exposure. Sometimes, even though the initial results may be satisfactory, headquarters may eventually become dissatisfied with the local distributor’s performance. In such a case, ­managers from the global company often intervene and attempt to take control. Harvard ­professor David Arnold offers seven specific guidelines to help prevent such problems from arising:[**11**](https://jigsaw.vitalsource.com/books/9780134899763/epub/OPS/xhtml/fileP7001015395000000000000000003AA7.xhtml#P7001015395000000000000000003ABF)

1. **Select distributors. Don’t let them select you**. A company may link up with a distributor by default after being approached by representatives at a trade fair. In fact, such eager ­candidates may already be serving a company’s competitors. Their objective may be to maintain control over the product category in a given market. A proactive market entrant can identify potential distributors by requesting a list from the U.S. Department of ­Commerce or its equivalent in other countries. The local chamber of commerce or trade association in a country can provide similar information.
2. **Look for distributors capable of developing markets, rather than those with a few good customer contacts**. A distributor with good contacts may appear to be the “obvious” choice in terms of generating quick sales and revenues. However, a better choice is often a partner that is willing to both make the investment necessary to achieve success and draw upon the marketing experience of the global company. Such a partner may, in fact, have no prior experience with a particular product category. In this case, the distributor may devote more effort and assign the new partner a higher priority simply because taking on the product line does not represent the status quo.
3. **Treat local distributors as long-term partners, not as temporary market-entry vehicles**. A contractual agreement that provides strong financial incentives for customer acquisition, new-product sales, or other forms of business development is a signal to the distributor that the market entrant is taking a long-term perspective. Such development can take place with the input of managers from the global company.
4. **Support market entry by committing money, managers, and proven marketing ideas**. In addition to providing sales personnel and technical support, management should ­consider demonstrating its commitment early on by investing in a minority equity stake in an ­independent distributor. Of course, the risks associated with such investment should be no greater than the risks associated with independent distribution systems in the ­manufacturer’s home country. The earlier such a commitment is made, the better the ­relationship that is likely to develop.
5. **From the start, maintain control over the marketing strategy**. To exploit the full potential of global marketing channels, the manufacturer should provide solid leadership for ­marketing in terms of which products the distributor sells and how those products are positioned. Again, it is necessary to have employees on site or to have country or regional managers monitor the distributor’s performance. As one manager told the author of the study, “We used to give far too much autonomy to distributors, thinking that they knew their markets. But our value proposition is a tough one to execute, and time and again we saw ­distributors cut prices to compensate for failing to target the right customers or to sufficiently train salespeople.” This is not to say that the intermediary should not be allowed to adapt the ­distribution strategy to suit local conditions. Rather, the point is that the manufacturer should take the lead.
6. **Make sure distributors provide the company with detailed market and financial performance data**. Distributor organizations are often a company’s best source—and sometimes the only source—of market information. The contract between a manufacturer and a ­distributor should include specific language to the effect that local market information and financial data will be transferred back to the manufacturer. One sign that a successful ­manufacturer–distributor relationship can be established is the latter’s willingness to provide such information.
7. **Build links among national distributors at the earliest opportunity**. A manufacturer should attempt to establish links between its networks of national distributors. This can be accomplished by setting up a regional corporate office or by establishing a distributor council. At any point in time, a company may have some excellent agents and distributors, others that are satisfactory, and a third group that is unsatisfactory. By creating opportunities for ­distributors to communicate, ideas for new product designs based on individual market results can be leveraged and overall distributor performance can be improved.

When devising a channel strategy, it is necessary to be realistic about the intermediary’s motives. It is the intermediary’s responsibility to implement an important element of a company’s marketing strategy. Left to their own devices, however, middlemen may seek to maximize their own profit rather than the manufacturer’s revenues. These agents sometimes engage in [**cherry picking**](https://jigsaw.vitalsource.com/books/9780134899763/epub/OPS/xhtml/fileP7001015395000000000000000004BB6.xhtml#P7001015395000000000000000004C5E), the practice of accepting orders only from manufacturers with established demand for certain products and brands. Cherry picking can also take the form of selecting only a few choice items from a vendor’s product lines. The cherry picker is not interested in developing a market for a new product, which is a problem for an expanding international company.

As noted previously, a manufacturer should provide leadership and invest resources to build a solid relationship with a desired distributor. Conversely, a manufacturer with a new product or a product with a limited market share may find it more desirable to set up some arrangement for bypassing the cherry-picking channel member. In some cases, a manufacturer must incur the costs of direct involvement by setting up its own distribution organization to obtain a share of the market. When the company sales finally reach critical mass, management may decide to shift from direct involvement to a more cost-effective, independent intermediary.

An alternative method of dealing with the cherry-picking problem does not require setting up an expensive direct sales force. Rather, a company may decide to rely on a distributor’s own sales force by subsidizing the cost of the sales representatives the distributor has assigned to the company’s products. This approach has the advantage of holding down costs by tying the manufacture in with the distributor’s existing sales management team and physical distribution system. It is possible to place managed direct-selling support and distribution support behind a product at the expense of only one salesperson per selling area. The distributor’s incentive for cooperating in this kind of arrangement is that he or she obtains a “free” sales representative for a new product that has the potential to be a profitable addition to his or her line. This cooperative arrangement is ideally suited to getting a new export-sourced product into distribution in a market. Alternatively, a company may decide to provide special incentives to independent channel agents.

12-3 Global Retailing

1. **12-3**Describe the different ­categories of retail operations that are found in various parts of the world.

[**Global retailing**](https://jigsaw.vitalsource.com/books/9780134899763/epub/OPS/xhtml/fileP7001015395000000000000000004BB6.xhtml#P7001015395000000000000000004E36) is any retailing activity that crosses national boundaries. It has a long history: For centuries, entrepreneurial merchants have ventured abroad to seek out merchandise and ideas and to establish retail operations. During the nineteenth and early twentieth centuries, British, French, Dutch, Belgian, and German trading companies established retailing organizations in Africa and Asia. Indeed, international trading and retail store operations were two of the economic pillars of that era’s colonial system. In the twentieth century, Dutch apparel and footwear retailer C&A expanded across Europe. In 1909, Harry Gordon Selfridge traveled from Chicago to London to open a ­department store that ended up reshaping retailing. That same year, another American, Frank Woolworth, took his five-and-dime concept across the Atlantic, opening his first British store in Liverpool.

Global retailers serve an important distribution function. For example, when Carrefour, Tesco, and Walmart set up shop in developing countries, they provide customers with access to more products and lower prices than were available previously. As we have noted throughout the text, when global companies expand abroad, they often encounter local competitors. The retail sector is no exception; India is a case in point. *Organized retail*, a term that is used to describe ­modern, branded chain stores, currently accounts for less than 5 percent of India’s total market. The ­sector is expected to exhibit double-digit growth in the future—a rosy outlook that has attracted the giants of global retailing. Today, however, they must compete with stores operated by local retail chains. One such company is Reliance Industries; its Reliance Retail division is opening thousands of modern supermarkets across India. What’s more, Reliance itself is developing plans for global expansion.[**12**](https://jigsaw.vitalsource.com/books/9780134899763/epub/OPS/xhtml/fileP7001015395000000000000000003AA7.xhtml#P7001015395000000000000000003AC1)

In some instances, it is a local retailer, rather than a global one, that breaks new ground by transforming the shopping experience. Nakumatt, a supermarket chain in Kenya, is a case in point. As Wambui Mwangi, a political science professor at the University of Toronto, notes, “Nakumatt is where you go to show you are educated and prosperous and cognizant of larger affairs. It’s an aspirational space that appeals to everyone, especially the people who can’t really afford to shop there.”[**13**](https://jigsaw.vitalsource.com/books/9780134899763/epub/OPS/xhtml/fileP7001015395000000000000000003AA7.xhtml#P7001015395000000000000000003AC3)

Retail business models may undergo significant adaptation outside the country in which they originated. For example, after the first 7-Eleven Japan franchise opened in 1973, the stores quickly attracted customers seeking greater convenience in purchasing. Today, “conbinis” are ubiquitous in Japan, with tens of thousands of store locations. Seven & I Holdings, which operates 7-Eleven, is Japan’s largest grocer. The convenience store operators use cutting-edge electronic point-of-sale (EPOS) data to track customer behavior and ensure that perishable products and other merchandise are delivered on a just-in-time basis during high-traffic periods. Even in the recent difficult economic environment, convenience store sales have remained strong in Japan. Now the operators are moving to further differentiate themselves: For example, 7-Eleven has Seven Bank ATMs in its stores and a lower-priced line of own-brand merchandise, Seven Premium.[**14**](https://jigsaw.vitalsource.com/books/9780134899763/epub/OPS/xhtml/fileP7001015395000000000000000003AA7.xhtml#P7001015395000000000000000003AC5)

Today’s global retailing scene is characterized by great diversity (as seen in [**Table 12-1**](https://jigsaw.vitalsource.com/books/9780134899763/epub/OPS/xhtml/fileP70010153950000000000000000037B7.xhtml?favre=brett#P70010153950000000000000000037C5), which lists the top five companies by revenue). We will begin the discussion of this area with a brief survey of some of the different forms retailing can take. Retail stores can be divided into categories according to the amount of square feet of floor space, the level of service offered, the width and depth of product offerings, or other criteria. Each represents a strategic option for a retailer considering global expansion.

**Table 12-1 Top Five Global Retailers, 2017**

*Source: Company reports.*

| **Rank** | **Company** | **Country** | **Formats** | **Sales ($ millions)** |
| --- | --- | --- | --- | --- |
| [***\****](https://jigsaw.vitalsource.com/books/9780134899763/epub/OPS/xhtml/fileP70010153950000000000000000037B7.xhtml?favre=brett#P70010153950000000000000000037EC)*2016 data.* |
| 1 | Walmart Stores | United States | Discount store, wholesale club | $485,873 |
| 2 | Carrefour | France | Hypermarket | 82,996[**\***](https://jigsaw.vitalsource.com/books/9780134899763/epub/OPS/xhtml/fileP70010153950000000000000000037B7.xhtml?favre=brett#P70010153950000000000000000037D7) |
| 3 | Tesco PLC | United Kingdom | Supermarket/hypermarket | 69,501 |
| 4 | Metro AG | Germany | Diversified | 43,828 |
| 5 | Aldi | Germany | Discount store | NA |

Types of Retail Operations

[**Department stores**](https://jigsaw.vitalsource.com/books/9780134899763/epub/OPS/xhtml/fileP7001015395000000000000000004BB6.xhtml#P7001015395000000000000000004D1C) literally have several departments under one roof, each representing a distinct merchandise line and staffed with a limited number of salespeople. Departments in a typical store might include men’s, women’s, children’s, beauty aids, housewares, and toys. [**Table 12-2**](https://jigsaw.vitalsource.com/books/9780134899763/epub/OPS/xhtml/fileP70010153950000000000000000037B7.xhtml?favre=brett#P7001015395000000000000000003810) lists major department stores that have expanded outside their home-country markets. However, in most instances, the expansion is limited to a few countries. As Maureen Hinton, a retail analyst with a London-based consultancy, notes, “It’s quite difficult to transfer a department store brand abroad. You have to find a city with the right demographic for your offer. If you adapt your offer to the locality, you dilute your brand name.” Marvin Traub, former chief executive of Bloomingdales, has a different perspective: “Conceptually, department stores are global brands already because we live in a world with an enormous amount of travel between cities and continents,” he says.[**15**](https://jigsaw.vitalsource.com/books/9780134899763/epub/OPS/xhtml/fileP7001015395000000000000000003AA7.xhtml#P7001015395000000000000000003AC7)

**Table 12-2 Department Stores with Global Branches**

| **Store** | **Original Store Location** | **Global Locations** |
| --- | --- | --- |
| Harvey Nichols | United Kingdom | Saudi Arabia, Hong Kong, Ireland, Dubai |
| Saks Fifth Avenue | United States | Dubai, Bahrain, Mexico |
| Barneys New York | United States | Japan |
| Lane Crawford | Hong Kong | China, Macao, Taiwan |
| Mitsukoshi | Japan | United States, Europe, Asia |
| H&M (Hennes & Mauritz) | Sweden | Austria, Germany, Kuwait, Slovakia, United States, 20 others |

[**Specialty retailers**](https://jigsaw.vitalsource.com/books/9780134899763/epub/OPS/xhtml/fileP7001015395000000000000000004BB6.xhtml#P7001015395000000000000000005052) offer less variety than department stores; that is, they are more narrowly focused and offer a relatively narrow merchandise mix aimed at a particular target market. Specialty stores do offer a great deal of merchandise depth (e.g., many styles, colors, and sizes), high levels of service from knowledgeable staff, and a value proposition that is both clear and appealing to consumers. Gap, the Disney Store, Lululemon, Superdry, and Victoria’s Secret are examples of global retail operators that have stores in many parts of the world. In some countries, local companies operate the stores. In Japan, for example, the giant Aeon Group runs The Body Shop stores and has a joint venture with Sports Authority.

[**Supermarkets**](https://jigsaw.vitalsource.com/books/9780134899763/epub/OPS/xhtml/fileP7001015395000000000000000004BB6.xhtml#P7001015395000000000000000005085) are departmentalized, single-story retail establishments that offer a variety of food (e.g., produce, baked goods, meats) and nonfood (e.g., paper products, health and beauty aids) items, mostly on a self-service basis. On average, supermarkets occupy between 50,000 square feet and 60,000 square feet of floor space.

U.K.-based Tesco is one retailing group that expanded globally for many years. While home-country sales still account for approximately 80 percent of its overall sales, the company has operations in 11 international markets. Company officials typically study a country market for several years before choosing an entry strategy. For example, Tesco’s initial entry into Japan came via the acquisition of the C Two-Network, a chain of shops in Tokyo. As former Tesco chairman David Reid once explained, Tesco has succeeded globally because it does its homework and pays attention to details. Even so, in the 2000s, Tesco’s efforts to penetrate the U.S. market failed.

Although Walmart is generating headlines as it moves around the globe, American retailers lag behind the Europeans in expanding outside their home countries. One reason is the sheer size of the domestic U.S. market.[**16**](https://jigsaw.vitalsource.com/books/9780134899763/epub/OPS/xhtml/fileP7001015395000000000000000003AA7.xhtml#P7001015395000000000000000003AC9) In fact, Walmart’s lack of experience outside North America undoubtedly contributed to its failures in South Korea and Germany.

[**Convenience stores**](https://jigsaw.vitalsource.com/books/9780134899763/epub/OPS/xhtml/fileP7001015395000000000000000004BB6.xhtml#P7001015395000000000000000004CAA) offer some of the same products as supermarkets, but the merchandise mix is limited to high-turnover convenience and impulse products. Prices for some products may be 15 to 20 percent higher than supermarket prices. In terms of square footage, these venues are the smallest organized retail stores discussed here. In the United States, for example, the typical 7-Eleven occupies 3,000 square feet. Most convenience stores are located in high-traffic locations and offer extended service hours to accommodate commuters, students, and other highly mobile consumers. 7-Eleven is the world’s largest convenience store chain; it has more than 64,000 locations, including franchisees, licensees, and stores that the company operates itself.

The current trend in convenience store retailing is toward smaller stores placed inside malls, airports, office buildings, and in college and university buildings. As Jeff Lenard, spokesperson for the National Association of Convenience Stores, has noted, “All the good street corners are gone, and the competition is so fierce for the ones that are left.”[**17**](https://jigsaw.vitalsource.com/books/9780134899763/epub/OPS/xhtml/fileP7001015395000000000000000003AA7.xhtml#P7001015395000000000000000003ACB)

[**Discount retailers**](https://jigsaw.vitalsource.com/books/9780134899763/epub/OPS/xhtml/fileP7001015395000000000000000004BB6.xhtml#P7001015395000000000000000004D3D) can be divided into several categories. The most general characteristic that they have in common is their emphasis on low prices. *Full-line discounters* typically offer a wide range of merchandise, including nonfood items and nonperishable food, in a limited-service format. As [**Table 12-1**](https://jigsaw.vitalsource.com/books/9780134899763/epub/OPS/xhtml/fileP70010153950000000000000000037B7.xhtml?favre=brett#P70010153950000000000000000037C5) clearly shows, Walmart is the reigning king of the full-line discounters. Many of its stores cover 120,000 square feet (or more) of floor space; food accounts for approximately one-third of floor space and sales. Walmart stores typically offer a folksy atmosphere and value-priced brands. This company is also a leader in the *warehouse club* segment of discount retailing; shoppers “join” the club to take advantage of low prices on a limited range of products (typically 3,000 to 5,000 different items), many of which are displayed in their shipping cartons in a “no-frills” atmosphere.

When Walmart expands into a new country market, local discounters must respond to the competitive threat it poses. In Canada, for example, Hudson Bay’s Zellers is the largest discount store chain. After Walmart acquired a bankrupt Canadian chain, Zellers countered by brightening the décor in its stores, widening aisles, and catering to women with young children.[**18**](https://jigsaw.vitalsource.com/books/9780134899763/epub/OPS/xhtml/fileP7001015395000000000000000003AA7.xhtml#P7001015395000000000000000003ACD) French discounter Tati is also going global; in addition to opening a store on New York’s Fifth Avenue, Tati currently has stores in Lebanon, Turkey, Germany, Belgium, Switzerland, and the Côte d’Ivoire.

*Dollar stores* sell a select assortment of products at one or more low prices. In the United States, Family Dollar Stores and Dollar Tree Stores dominate the industry. However, a recent industry entrant, My Dollarstore, is experiencing rapid international growth; it now has franchises in Eastern Europe, Central America, and Asia. To succeed in global markets, My Dollarstore has adapted its U.S. business model. For example, the typical U.S. dollar store has a “bargain basement” image. By contrast, in India, My Dollarstore targets affluent, middle-class shoppers who are attracted by the lure of low prices on brands associated with “the good life” in America. Goods are priced at 99 rupees—the equivalent of $2—and the stores are decorated in red, white, and blue with the Statue of Liberty on display. In the United States, dollar stores operate on a self-service basis with lean staffs; My Dollarstore’s Indian locations have significantly higher staffing levels, the better to answer customers’ questions about new or unfamiliar products.[**19**](https://jigsaw.vitalsource.com/books/9780134899763/epub/OPS/xhtml/fileP7001015395000000000000000003AA7.xhtml#P7001015395000000000000000003ACF)

[**Hard discounters**](https://jigsaw.vitalsource.com/books/9780134899763/epub/OPS/xhtml/fileP7001015395000000000000000004BB6.xhtml#P7001015395000000000000000004E59) include retailers such as Germany’s Aldi and Lidl (“Where quality is cheaper!”) and France’s Leader Price (“Le Prix La Qualité en Plus!”). These discounters offer a limited assortment of goods—typically 1,000 to 3,000 different items—at rock-bottom prices. Starting in 1976, Aldi began opening a few stores each year in the United States (where Aldi also owns the Trader Joe’s “neighborhood grocery” chain). Aldi stores have a relatively small footprint; 17,500 square feet of floor space is typical. As Jason Hart, co-president of Aldi’s U.S. operation, noted recently, “We carry 1,500 of the most popular grocery items out there. When you look at the large supermarkets that may have 20,000 to 30,000 items, it’s surprising to the customers how much of the shopping list we’re able to fit in our smaller store.”[**20**](https://jigsaw.vitalsource.com/books/9780134899763/epub/OPS/xhtml/fileP7001015395000000000000000003AA7.xhtml#P7001015395000000000000000003AD1) The company recently announced expansion plans calling for a total of 2,500 stores in the United States by 2022.[**21**](https://jigsaw.vitalsource.com/books/9780134899763/epub/OPS/xhtml/fileP7001015395000000000000000003AA7.xhtml#P7001015395000000000000000003AD3)

When Walmart entered the German market, Aldi and Lidl were already well entrenched. By mid-2006, after years of losses, Walmart decided to close up shop in that country. In the recent economic downturn, hard discounters thrived as cash-strapped consumers sought ways to stretch their household budgets. Hard-discount retailers, which account for approximately 10 percent of grocery sales in Europe, rely heavily on “own-label” or private brands. Some items sell for much less than well-known global brands; tight cost control and supply-chain optimization are critical to maintain the companies’ profits. Carrefour and other large supermarket operators are responding to the challenges posed by hard discounters by offering more own-brand products at lower prices. A decade ago, Tesco began offering hundreds of new, cheaper products under its own brands, including tea bags, cookies, and shampoo. “If there is a war, we will win it,” said Tesco’s one-time commercial director, Richard Brasher.[**22**](https://jigsaw.vitalsource.com/books/9780134899763/epub/OPS/xhtml/fileP7001015395000000000000000003AA7.xhtml#P7001015395000000000000000003AD5)

[**Hypermarkets**](https://jigsaw.vitalsource.com/books/9780134899763/epub/OPS/xhtml/fileP7001015395000000000000000004BB6.xhtml#P7001015395000000000000000004E6E) are a hybrid retailing format combining the discounter, supermarket, and warehouse club approaches under a single roof. Size-wise, hypermarkets are huge, ranging from 200,000 to 300,000 square feet.

[**Supercenters**](https://jigsaw.vitalsource.com/books/9780134899763/epub/OPS/xhtml/fileP7001015395000000000000000004BB6.xhtml#P7001015395000000000000000005082) offer a wide range of aggressively priced grocery items plus general merchandise in a space that occupies about half the size of a hypermarket. Supercenters are an important aspect of Walmart’s growth strategy, both at home and abroad. Walmart opened its first supercenter in 1988; today, it operates more than 3,275 supercenters in the United States, plus hundreds of stores in Mexico and units in Argentina and Brazil. Some prices at Walmart’s supercenters in Brazil are as much as 15 percent lower than competitors’ prices, and some observers wondered if the company had taken the discount approach too far. Company officials insist, though, that profit margins are in the 20 to 22 percent range.[**23**](https://jigsaw.vitalsource.com/books/9780134899763/epub/OPS/xhtml/fileP7001015395000000000000000003AA7.xhtml#P7001015395000000000000000003AD7)

[**Superstores**](https://jigsaw.vitalsource.com/books/9780134899763/epub/OPS/xhtml/fileP7001015395000000000000000004BB6.xhtml#P7001015395000000000000000005088) (also known as [**category killers**](https://jigsaw.vitalsource.com/books/9780134899763/epub/OPS/xhtml/fileP7001015395000000000000000004BB6.xhtml#P7001015395000000000000000004C46) and *big-box retail*) is the label many in the retailing industry use when talking about stores such as Home Depot and IKEA (see [**Exhibit 12- 6**](https://jigsaw.vitalsource.com/books/9780134899763/epub/OPS/xhtml/fileP70010153950000000000000000037B7.xhtml?favre=brett#P7001015395000000000000000003857)). The name refers to the fact that such stores specialize in selling vast assortments of specific product categories—home improvement supplies or furniture, for example—in high volumes at low prices. In short, these stores represent retailing’s “900-pound gorillas,” which put pressure on smaller, more traditional competitors and prompt department stores to scale down merchandise sections that are in direct competition with the bigger selections found at the superstores.

**Exhibit 12-6**

STIHL Inc. manufactures and markets chainsaws, trimmers, and other types of outdoor power equipment. The distribution (*P*) factor of the marketing mix is an integral part of STIHL’s marketing strategy: Its products are available only at independent dealers that provide full after-sale service. STIHL also sponsors “Independent We Stand,” an initiative among independent businesses to help educate consumers about the importance of “buying local.”

*Source: Courtesy of STIHL Inc; ad campaign from 2010-2011.*

“There is a new middle class of savvy consumers in South Africa. A shopping mall in South Africa is not very different from an ­Australian shopping mall or a British shopping mall.”[**24**](https://jigsaw.vitalsource.com/books/9780134899763/epub/OPS/xhtml/fileP7001015395000000000000000003AA7.xhtml#P7001015395000000000000000003AD9)

*Simon Susman, CEO, Woolworths Holdings*

[**Shopping malls**](https://jigsaw.vitalsource.com/books/9780134899763/epub/OPS/xhtml/fileP7001015395000000000000000004BB6.xhtml#P7001015395000000000000000005036) consist of a grouping of stores in one place. Developers assemble an assortment of retailers that will create an appealing leisure destination; typically one or more large department stores serve as anchors (see [**Exhibit 12-7**](https://jigsaw.vitalsource.com/books/9780134899763/epub/OPS/xhtml/fileP70010153950000000000000000037B7.xhtml?favre=brett#P7001015395000000000000000003868)). Shopping malls offer acres of free parking and easy access from main traffic thoroughfares. Historically, malls were enclosed, allowing shoppers to browse in comfort no matter the weather outside. More recently, the trend has been toward outdoor shopping centers, now called “lifestyle centers.” Food courts and entertainment encourage families to spend several hours at the mall. In the United States, malls sprang up as people moved from city centers to the suburbs. Today, global mall development reflects the opportunity to serve emerging middle-class consumers who seek both convenience and entertainment.

**Exhibit 12-7**

The LP12 Mall of Berlin opened in September 2014. Located in Leipziger Platz, the mixed-use ­complex features 270 stores as well as apartments.

*Source: Art Kowalsky/Alamy Stock Photo.*

The world’s five largest malls are in Asia (see [**Table 12-3**](https://jigsaw.vitalsource.com/books/9780134899763/epub/OPS/xhtml/fileP70010153950000000000000000037B7.xhtml?favre=brett#P7001015395000000000000000003871)). The reasons for their presence in this region are clear-cut: Economic growth led to rising incomes; in addition, tourism is ­booming in Asia. Some industry observers warn, however, that the megamalls and their ­glamorous global brand offerings are luring shoppers away from markets that sell goods produced by local ­craftspeople. Somewhere along the way, the thrill of discovering something new has been lost. Emil Pocock, a professor of American studies at Eastern Connecticut State University, is an expert on shopping malls. As he has noted, “I find it very disconcerting that shopping malls are more or less the same wherever you go in the world. I’m not sure I want 100 international companies determining our choices for consumer goods.”[**25**](https://jigsaw.vitalsource.com/books/9780134899763/epub/OPS/xhtml/fileP7001015395000000000000000003AA7.xhtml#P7001015395000000000000000003ADB)

**Table 12-3 The World’s Largest Shopping Malls (ranked by gross leasable retail space)**

*Source: Author research.*

| **Rank** | **Mall** | **City/Country** | **Millions of Square Feet** |
| --- | --- | --- | --- |
| 1 | New South China Mall | Dongguan, China | 7.1 |
| 2 | Golden Resources Mall | Beijing, China | 6.0 |
| 3 | SM Megamall | Philippines | 5.45 |
| 4 | SM City North EDSA | Philippines | 5.2 |
| 5 | 1 Utama | Malaysia | 5.0 |

[**Outlet stores**](https://jigsaw.vitalsource.com/books/9780134899763/epub/OPS/xhtml/fileP7001015395000000000000000004BB6.xhtml#P7001015395000000000000000004F82) are a variation on the traditional shopping mall: retail operations that allow ­companies with well-known consumer brands to dispose of excess inventory, out-of-date ­merchandise, or factory seconds. To attract large numbers of shoppers, outlet stores are often grouped together in [**outlet malls**](https://jigsaw.vitalsource.com/books/9780134899763/epub/OPS/xhtml/fileP7001015395000000000000000004BB6.xhtml#P7001015395000000000000000004F7F). The United States is home to hundreds of outlet malls, such as the giant Woodbury Common mall in Central Valley, New York. Now, the concept is catching on in Europe and Asia as well. The acceptance of this type of venue reflects changing attitudes among consumers and retailers alike; in both Asia and Europe, brand-conscious consumers are eager to save money (see [**Exhibit 12-8**](https://jigsaw.vitalsource.com/books/9780134899763/epub/OPS/xhtml/fileP70010153950000000000000000037B7.xhtml?favre=brett#P70010153950000000000000000038AB)).

**Exhibit 12-8**

McArthurGlen operates several upscale designer outlets in Europe. Although the retail tenants include popular American companies such as Nike, the majority of stores represent a veritable “who’s who” of exclusive European fashion brands: Fendi, Ferrari, Harmont & Blaine, Jil Sander, Prada, Salvatore Ferragamo, and Versace (to name just a few). Fashion-forward bargain hunters can find prices that represent discounts of 30 percent to 70 percent off regular retail prices.

*Source: McArthurGlen Designer Outlets.*

# Trends in Global Retailing

Currently, a variety of environmental factors have combined to push retailers out of their home markets in search of opportunities around the globe. Saturation of the home-country market, recession or other economic factors, strict regulation on store development, and high operating costs are some of the factors that prompt management to look abroad for growth opportunities. Walmart is a case in point; its international expansion in the mid-1990s coincided with ­disappointing financial results in its home market.

Even as the domestic retailing environment grows more challenging for many companies, an ongoing environmental scanning effort is likely to turn up markets in other parts of the world that are underdeveloped or where competition is weak. In addition, high rates of economic growth, a growing middle class, a high proportion of young people in the population, and less stringent regulation combine to make some country markets very attractive.[**26**](https://jigsaw.vitalsource.com/books/9780134899763/epub/OPS/xhtml/fileP7001015395000000000000000003AA7.xhtml#P7001015395000000000000000003ADD) For example, Laura Ashley, The Body Shop, Disney Stores, and other specialty retailers were lured to Japan by developers who needed established names to fill space in large, suburban, American-style shopping malls.[**27**](https://jigsaw.vitalsource.com/books/9780134899763/epub/OPS/xhtml/fileP7001015395000000000000000003AA7.xhtml#P7001015395000000000000000003ADF) Such malls are being developed as some local and national restrictions on retail development are being eased and as consumers tire of the aggravations associated with shopping in congested urban areas.

However, the large number of unsuccessful cross-border retailing initiatives suggests that any chief executive contemplating a move into global retailing should do so with a great deal of ­caution and due diligence. A few years ago, Frank Blake, Home Depot’s CEO, noted, ­“International expansion has proved to be a competitive advantage for us. In Canada, Mexico, and now, China, we’ve shown we can enter a market, tailor our model to the local customer and see the same sort of growth we saw in our early days here in the U.S.”[**28**](https://jigsaw.vitalsource.com/books/9780134899763/epub/OPS/xhtml/fileP7001015395000000000000000003AA7.xhtml#P7001015395000000000000000003AE1) Despite this pronouncement, by the end of 2012 Home Depot had been forced to scale back its China operations. Other failures include the following:

* Walmart pulled out of Germany and South Korea.
* Best Buy closed several stores in China.
* Mattel closed its six-story flagship Barbie store in Shanghai.
* Tesco shut down its Fresh & Easy stores in the United States after incurring $1.6 billion in losses.

These are just a few of the examples that illustrate that it’s not always possible to export a retail business model that has proved successful in the domestic market. As one industry analyst noted, “It’s awfully hard to operate across the water. It’s one thing to open up in Mexico and Canada, but the distribution hassles are just too big when it comes to exporting an entire store concept overseas.”[**29**](https://jigsaw.vitalsource.com/books/9780134899763/epub/OPS/xhtml/fileP7001015395000000000000000003AA7.xhtml#P7001015395000000000000000003AE3)

The critical question for the would-be global retailer is, “Which advantages do we have relative to local competition?” After taking into account the existing competition, local laws governing retailing practice, distribution patterns, or other factors, the answer will often be “Nothing.” Sometimes, however, a company may possess competencies that can be the basis for competitive advantage in a particular retail market. A retailer may have several attractions to offer consumers, such as selection, price, and the overall manner and condition in which the goods are offered in the store setting. Store location, parking facilities, in-store atmosphere, and customer service also contribute to the value proposition. Competencies can also be found in less visible value-chain activities such as distribution, logistics, and information technology. As Thomas Hübner, CEO of Metro Cash & Carry International, noted, “Stores are just the tip of the iceberg—90 percent of the work is under water.”[**30**](https://jigsaw.vitalsource.com/books/9780134899763/epub/OPS/xhtml/fileP7001015395000000000000000003AA7.xhtml#P7001015395000000000000000003AE5)

For example, Japanese retailers traditionally offered few extra services to their clientele. There were no special orders or returns, and stock was chosen not according to consumer demand, but rather according to the purchasing preferences of the stores. Typically, a store would buy limited quantities from each of its favorite manufacturers, leaving consumers with no recourse when the goods sold out. Instead of trying to capitalize on the huge market, many retailers simply turned a deaf ear to customer needs and desires. From the retailers’ point of view, this came out fine in the end; most of their stock eventually sold because buyers were forced to purchase what was left over—they had no other choice.

Then Gap, Eddie Bauer, and other Western retailers entered Japan, often by means of joint ventures. Their stores offered liberal return policies, a willingness to take special orders, and a policy of replenishing stock; in response, many Japanese consumers switched loyalties. Also, thanks to economies of scale and modern distribution methods unknown to some Japanese ­department store operators, the foreign retailers offered a greater variety of goods at lower prices. Although this upscale foreign competition hurt Japanese department store operators, Japan’s depressed economy was another factor. Traditional retailers are also being squeezed from below as recession-pressed consumers flock to discounters such as Uniqlo and the Y100 Shop chain.

The retailing environment continues to be challenging in many parts of the world. For ­example, the French Connection Group PLC closed all of its U.S. and Japanese stores, as well as underperforming stores in Europe. One problem faced by that company: higher prices ­relative to competitors such as Zara and H&M, without a well-known brand and the higher ­quality that justifies the prices. Likewise, a traditional department store such as Macy’s has neither the ­advantages of H&M and other affordable fast-fashion retailers nor the aspirational appeal of ­luxury ­specialty retailers.[**31**](https://jigsaw.vitalsource.com/books/9780134899763/epub/OPS/xhtml/fileP7001015395000000000000000003AA7.xhtml#P7001015395000000000000000003AE7) Even so, global opportunities still attract some companies. For example, value retailer Primark, whose product assortment ranges from lingerie and athleisure to housewares, has expanded beyond its United Kingdom base and continental Europe by opening stores in the United States.[**32**](https://jigsaw.vitalsource.com/books/9780134899763/epub/OPS/xhtml/fileP7001015395000000000000000003AA7.xhtml#P7001015395000000000000000003AE9)

[**Figure 12-3**](https://jigsaw.vitalsource.com/books/9780134899763/epub/OPS/xhtml/fileP70010153950000000000000000038B3.xhtml?favre=brett#P70010153950000000000000000038C9) shows a matrix-based scheme for classifying global retailers.[**33**](https://jigsaw.vitalsource.com/books/9780134899763/epub/OPS/xhtml/fileP7001015395000000000000000003AA7.xhtml#P7001015395000000000000000003AEB) One axis ­represents a private- or own-label focus versus a manufacturer-brand focus. The other axis differentiates between retailers specializing in relatively few product categories and retailers that offer a wide product assortment. IKEA, in quadrant A, is a good example of a global retailer with a niche focus (assemble-yourself furniture for the home) as well as an own-label focus (IKEA sells its own brand). IKEA and other retailers in quadrant A typically use extensive advertising and product innovation to build a strong brand image.

**Figure 12-3 Global Retailing Categories**

*Source: Adapted from Jacques Horovitz and Nirmalya Kumar, “Strategies for Retail Globalization,” Financial Times—Mastering Global Business, Part VII (1998), pp. 4–8.*

In quadrant B, the private-label focus is retained, but many more product categories are offered. This is the strategy of Marks & Spencer (M&S), the British-based department store ­company whose St. Michael private label is found on a broad range of clothing, food, home ­furnishings, jewelry, and other items. Private-label retailers that attempt to expand internationally face a double-edged challenge: They must attract customers to both the store and the branded merchandise. M&S has succeeded by virtue of an entrepreneurial management style that has evolved over the last 100-plus years. The company opened its first store outside the United Kingdom in 1974; it currently operates more than 450 stores in 54 countries, including 15 locations in Shanghai.

“Apparel has always been extremely competitive and retail is one of the least consolidated sectors. Brands have to evolve or risk becoming less relevant.”[**34**](https://jigsaw.vitalsource.com/books/9780134899763/epub/OPS/xhtml/fileP7001015395000000000000000003AA7.xhtml#P7001015395000000000000000003AED)

*Jamie Merriman, analyst, Bernstein Research*

In 1997, then chairman Sir Richard Greenbury announced an ambitious plan to put M&S “well on its way to establishing a global business.” It was his belief that consumer tastes are globalizing, at least with respect to fashion apparel. Food is a different story; because tastes are more localized, M&S executives anticipated that the proportion of revenues from global food sales would be lower than they are in Great Britain.[**35**](https://jigsaw.vitalsource.com/books/9780134899763/epub/OPS/xhtml/fileP7001015395000000000000000003AA7.xhtml#P7001015395000000000000000003AEF)

Retailers in quadrant C of [**Figure 12-3**](https://jigsaw.vitalsource.com/books/9780134899763/epub/OPS/xhtml/fileP70010153950000000000000000038B3.xhtml?favre=brett#P70010153950000000000000000038C9) offer many well-known brands in a relatively tightly defined merchandise range. Some well-known historical examples include Toys ‘R’ Us, ­Blockbuster Video, and Virgin Megastores. A few decades ago, this type of store tended to quickly dominate smaller established retailers by out-merchandising the local competition and offering customers superior value by virtue of extensive inventories and low prices. Typically, the low prices were the result of buyer power and sourcing advantages that the local retailers lacked. As it turns out, the three companies mentioned here have virtually disappeared from the retail ­landscape. All fell victim to changing consumer tastes and buying habits and were slower to adapt and innovate than industry disrupters such as Netflix and Spotify and e-commerce titan Amazon.

Despite the demise of most brick-and-mortar record shops, the retailing environment in which Richard Branson originally built the Virgin Megastore chain illustrates the type of success that can be achieved through an entrepreneurial management style:

It required little retailing expertise to see that the sleepy business practices of traditional record shops provided a tremendous opportunity. To rival the tiny neighborhood record shops, with their eclectic collections of records, a new kind of record store was coming into being. It was big; it was well-lit, and records were arranged clearly in alphabetical order by artist; it covered most tastes in pop music comprehensively; and it turned over its stock much faster than the smaller record retailer . . . . It was the musical equivalent of a supermarket.[**36**](https://jigsaw.vitalsource.com/books/9780134899763/epub/OPS/xhtml/fileP7001015395000000000000000003AA7.xhtml#P7001015395000000000000000003AF1)

Starting with one megastore location on London’s Oxford Street in 1975, Branson’s Virgin retail empire once extended throughout Europe, North America, Japan, Hong Kong, and Taiwan.

Another of Branson’s ventures, Virgin Atlantic Airlines, reflects the same effort to provide a different service experience. As Steve Ridgway, former CEO of Virgin Atlantic, explained, ­“Fundamentally it’s around the value proposition and what consumers will pay for. Our single biggest innovation was always to try to wrong-foot the market. We’ve always positioned our products half a notch out of the convention.”[**37**](https://jigsaw.vitalsource.com/books/9780134899763/epub/OPS/xhtml/fileP7001015395000000000000000003AA7.xhtml#P7001015395000000000000000003AF3)

Amazon, Carrefour, Primark, Walmart, and other retailers in quadrant D of [**Figure 12-3**](https://jigsaw.vitalsource.com/books/9780134899763/epub/OPS/xhtml/fileP70010153950000000000000000038B3.xhtml?favre=brett#P70010153950000000000000000038C9) offer the same type of merchandise available from established local retailers. What the newcomers bring to a market, however, is competence in distribution or some other value-chain element. To date, Walmart’s international division has established more than 6,360 stores outside the United States; it is already the biggest retailer in Mexico and Canada. Other store locations include Central America, South America, China, and, until recently, Germany.

Global Retailing Market Expansion Strategies

Retailers can choose from four market-entry expansion strategies when expanding outside the home country. As shown in [**Figure 12-4**](https://jigsaw.vitalsource.com/books/9780134899763/epub/OPS/xhtml/fileP70010153950000000000000000038DF.xhtml?favre=brett#P70010153950000000000000000038E3), these strategies can be diagrammed using a matrix that differentiates between (1) markets that are easy to enter versus those that are difficult to enter and (2) culturally close markets versus culturally distant ones. The upper half of the matrix encompasses quadrants A and D and represents markets in which shopping patterns and retail structures are similar to those in the home country. In the lower half of the matrix, quadrants B and C represent markets that are significantly different from the home-country market in terms of one or more cultural characteristics. The right side of the matrix, quadrants A and B, represents markets that are difficult to enter because of the presence of strong competitors, location restrictions, excessively high rent or real estate costs, or other factors. In quadrants C and D, any barriers that exist are relatively easy to overcome. The four entry strategies indicated by the matrix are organic, franchise, chain acquisition, and joint ventures and licensing.

**Figure 12-4 Global Retailing Market Entry Strategy Framework**

*Source: Adapted from Jacques Horovitz and Nirmalya Kumar, “Strategies for Retail Globalization,” Financial Times—Mastering Global Business, Part VII (1998), p. 5.*

[**Organic growth**](https://jigsaw.vitalsource.com/books/9780134899763/epub/OPS/xhtml/fileP7001015395000000000000000004BB6.xhtml#P7001015395000000000000000004F76) occurs when a company uses its own resources to open a store on a greenfield site or to acquire one or more existing retail facilities from another company. In 1997, for example, M&S announced plans to expand from one store to four in Germany via the purchase of three stores operated by Cramer and Meerman. When Richard Branson set up the first Virgin Megastore in Paris, he did so by investing millions of pounds in a spectacular retail space on the Champs-Élysées. From the perspectives of M&S and Virgin, the retail environments of Germany and France are both culturally close and easy to enter. The success of this strategy hinges on the availability of company resources to sustain the high cost of the initial investment.

[**Franchising**](https://jigsaw.vitalsource.com/books/9780134899763/epub/OPS/xhtml/fileP7001015395000000000000000004BB6.xhtml#P7001015395000000000000000004DEB), shown in quadrant C of [**Figure 12-4**](https://jigsaw.vitalsource.com/books/9780134899763/epub/OPS/xhtml/fileP70010153950000000000000000038DF.xhtml?favre=brett#P70010153950000000000000000038E3), is the appropriate entry strategy when barriers to entry are low, yet the market is culturally distant in terms of consumer behavior or retailing structures. As defined in [**Chapter 9**](https://jigsaw.vitalsource.com/books/9780134899763/epub/OPS/xhtml/fileP7001015395000000000000000002BDB.xhtml#P7001015395000000000000000002BDB), franchising is a contractual relationship between two companies. In this arrangement, the parent company–franchisor authorizes a franchisee to operate a business developed by the franchisor in return for a fee and adherence to franchise-wide policies and practices. The key to a successful franchise operation is the ability to transfer company ­know-how to new markets. Benetton, IKEA, and other focused, private-label retailers often use franchising as a market-entry strategy in combination with wholly owned stores that represent organic growth. The IKEA Group has more than 260 company-owned stores across Europe, in North America, and in China; 34 additional stores in various global locations are franchise operations.

In global retailing, [**acquisition**](https://jigsaw.vitalsource.com/books/9780134899763/epub/OPS/xhtml/fileP7001015395000000000000000004BB6.xhtml#P7001015395000000000000000004BC3) is a market-entry strategy that entails purchasing a company with multiple retail locations in a foreign country. This strategy can provide the buyer with quick growth as well as access to existing brand suppliers, distributors, and customers. For example, when Walmart first entered the Japanese market in 2002, it did so by acquiring a 6.1 percent stake in the Seiyu retail chain. In 2007, Walmart upped its stake to 95.1 percent; the following year, Seiyu and its 414 stores became a wholly owned subsidiary. Now Walmart is seeking to expand by making additional acquisitions. As Walmart Asia CEO Scott Price explained, “We see scale as being the next level of being able to change the value proposition for Japanese customers.” Organic growth is not an option, however: “We do not want to build more retail in Japan. The last thing Japan needs is more retail space,” Price said.[**38**](https://jigsaw.vitalsource.com/books/9780134899763/epub/OPS/xhtml/fileP7001015395000000000000000003AA7.xhtml#P7001015395000000000000000003AF5)

[**Joint ventures**](https://jigsaw.vitalsource.com/books/9780134899763/epub/OPS/xhtml/fileP7001015395000000000000000004BB6.xhtml#P7001015395000000000000000004EB5) and [**licensing**](https://jigsaw.vitalsource.com/books/9780134899763/epub/OPS/xhtml/fileP7001015395000000000000000004BB6.xhtml#P7001015395000000000000000004ECF) were examined in detail in [**Chapter 9**](https://jigsaw.vitalsource.com/books/9780134899763/epub/OPS/xhtml/fileP7001015395000000000000000002BDB.xhtml#P7001015395000000000000000002BDB). Global retailers frequently use these strategies to limit their risk when targeting unfamiliar, difficult-to-enter markets. For example, Barneys New York licensed its name to Barneys Japan for a period of 10 years; Saks Fifth Avenue has licensed stores in the Middle East. In some countries, local regulations mandate the use of joint ventures. For example, prior to 2005, China had regulations that required foreign retailers entering the market to have local partners. In 2005, Chinese authorities liberalized the country’s retail climate, and today IKEA and other retailers that initially used joint ventures as an entry strategy are shifting to wholly owned stores in China.

Virgin Group’s retail expansion in Asia provides a case study of the appropriateness of the joint venture approach. In Japan, commercial landlords typically require millions of dollars in upfront payments before they will lease retail space. Accordingly, in 1992, Virgin established a joint venture called Virgin Megastores Japan with Marui, a local retailer with a good track record of catering to the preferences of young people. The first megastore was set up in the basement of an existing Marui department store in Japan’s Shinjuku district. That site and subsequent stores have been wildly successful; Virgin has duplicated the joint venture approach elsewhere in Asia, including Hong Kong, Taiwan, and South Korea. In each location, Virgin establishes a joint venture with a leading industrial group.[**39**](https://jigsaw.vitalsource.com/books/9780134899763/epub/OPS/xhtml/fileP7001015395000000000000000003AA7.xhtml#P7001015395000000000000000003AF7)

Achieving retailing success outside the home-country market is not simply a matter of consulting a matrix and choosing the recommended entry strategy. Management must also be alert to the possibility that the merchandise mix, sourcing strategy, distribution, or other format elements will have to be adapted. Management at Crate & Barrel, for example, is hesitant to open stores in Japan. Part of the reason is research indicating that at least half the company’s product line would have to be modified to accommodate local preferences. Another issue is whether the company will have the ability to transfer its expertise to new country markets.

**Entrepreneurial Leadership, Creative Thinking, and the Global Startup**

Mr. Selfridge: An American Retailer in London

Harry Gordon Selfridge was an entrepreneur, an enthusiast, and a dreamer. Selfridge developed an innovative product, created a brand, and started a business. And not just any business: He launched Selfridge & Company, called by some “the most beautiful department store the world has ever seen.” By applying the basic tools and principles of marketing decades before modern marketing had emerged as a discipline, Selfridge achieved remarkable success. As is true with many entrepreneurs, Selfridge’s idea was based on his own needs, wants, and vision. He declared, “We are going to show the world how to make shopping thrilling!” (See [**Exhibit 12-9**](https://jigsaw.vitalsource.com/books/9780134899763/epub/OPS/xhtml/fileP70010153950000000000000000038DF.xhtml?favre=brett#P70010153950000000000000000038FB).)

**Exhibit 12-9**

Harry Gordon Selfridge was a marketing and retail genius. His spirit lives on today in London, where Selfridge's continues to find innovative ways to lure shoppers to the store. For example, when designer Michel Lamy launched a special collaboration with Everlast, Selfridge's installed a boxing ring in the store and invited Olympic boxing champion Nicola Adams to stop by.

*Source: PA Images/Alamy Stock Photo.*

Retailers may have a difficult time crossing borders if they fail to appreciate differences in retailing environments and consumer behavior and preferences. However, just the opposite was true when Selfridge opened his department store just off Oxford Street in London. He broke with convention on a number of fronts. Noting that there were more horse-drawn carriages than cars at the time, he moved perfume and fragrances to the front of the store, putting them front and center. This arrangement served to neutralize any foul odors from horse dung that shoppers might track in on their shoes. In traditional British stores, articles were kept behind counters and shoppers had to ask clerks for help. By contrast, Selfridge put the goods out for people to see and touch. “The customer always comes first,” Selfridge declared. Londoners had never seen anything like it.

If the Selfridge story sounds fascinating, well, it is! It has been the subject of a book, *Shopping, Seduction, and Mr Selfridge*, as well as a television series that aired on ITV in Great Britain and on public television in the United States. Although ratings were higher in Britain, the series was renewed for a fourth season for American viewers. As the book and the TV series clearly demonstrate, Selfridge loved the theater, performers, and artists. Not surprisingly, there was more than a hint of theatricality in some of Selfridge’s marketing tactics and publicity stunts. These included early-bird specials, an in-store appearance by Russian ballerina Anna Pavlova, and a display on the store’s ground floor of the first airplane to cross the English Channel.

As it turns out, the human story ended badly; Selfridge fell victim to various demons and vices and was ousted from the company he had founded. His legacy endures, however, and in the twenty-first century, Selfridges continues to be at the forefront of retailing innovation. Its flagship London store is home to Europe’s largest cosmetics department. Window displays have featured buzz-building “performances” such as humans in animal costumes modeling lingerie. As Peter Williams, CEO of Selfridges, said, “Our competitors are not just other department stores. Our competitors are restaurants, theaters, a weekend away, or other entertainment venues.”

*Sources: Nancy Dewolf Smith, “Tales of the Counter Culture,” The Wall Street Journal (March 28, 2014), p. D7; Mike Hale, “Fogging up the Windows of a Big Store,” The New York Times (March 30, 2013), p. C1; Nancy Dewolf Smith, “The Dawn of Shopping,” The Wall Street Journal (March 29, 2013), p. D5; Vanessa O’Connell, “Department Stores Are Hard Sell Abroad,” The Wall Street Journal (May 22, 2008), p. B3; Cecilie Rohwedder, “Harvey Nichols’s Foreign Affair,” The Wall Street Journal (February 18, 2005), p. B3; Erin White, “Dress for Success: After Long Slump, U.S. Retailers Look to Britain for Fashion Tips,” The Wall Street Journal (April 22, 2004), pp. A1, A8; Rohwedder, “Selling Selfridges,” The Wall Street Journal (May 5, 2003), p. B1.*

12-4 Physical Distribution, Supply Chains, and Logistics Management

1. **12-4**Compare and contrast the six major international ­transportation modes and explain how they vary in terms of ­reliability, accessibility, and other performance metrics.

In [**Chapter 1**](https://jigsaw.vitalsource.com/books/9780134899763/epub/OPS/xhtml/fileP70010153950000000000000000005BA.xhtml#P70010153950000000000000000005BA), marketing was described as one of the activities in a firm’s value chain. The distribution (*P*) of the marketing mix is a critical value-chain activity. After all, Coca-Cola, IKEA, Nokia, P&G, Toyota, and other global companies create value by making sure their products are available where and when customers need and want to buy them. As defined in this chapter, physical distribution consists of activities involved in moving finished goods from manufacturers to customers. However, the concept of the value chain is much broader: It is a useful tool for assessing an organization’s competence as it performs value-creating activities within a broader [**supply chain**](https://jigsaw.vitalsource.com/books/9780134899763/epub/OPS/xhtml/fileP7001015395000000000000000004BB6.xhtml#P700101539500000000000000000508B). The latter includes *all* the firms that perform support activities by generating raw materials, converting them into components or finished products, and facilitating their delivery to customers.

The particular industry in which a firm competes (e.g., automobiles, consumer electronics, furniture, or pharmaceuticals) is characterized by a value chain. The specific activities an individual firm performs help define its position in the value chain. A company or activity that is somewhat removed from the final customer is said to be *upstream* in the value chain. Consider the following comment from Anders Moberg, the former CEO of IKEA: “At IKEA, we went out into the forest to see which were the right trees to pick to optimize production and cost efficiency in the saw mills.”[**40**](https://jigsaw.vitalsource.com/books/9780134899763/epub/OPS/xhtml/fileP7001015395000000000000000003AA7.xhtml#P7001015395000000000000000003AF9) That’s a pretty good description of an upstream activity! A company or activity that is relatively close to customers—a retailer, for example—is said to be downstream in the value chain.

Logistics, in turn, is the management process that integrates the activities of all companies—both upstream and downstream—to ensure an efficient flow of goods through the supply chain. Logistics was not really a household term until UPS launched its global “We ♥ Logistics” advertising campaign. The TV ads utilize a catchy jingle: a Harry Warren–penned tune, “That’s Amore,” popularized by the 1953 motion picture *The Caddy* starring Jerry Lewis and Dean Martin. In the UPS ads, the original lyrics (e.g., “When the moon hits your eye like a big pizza pie, that’s amore!”) have been replaced by an ode to, well, logistics! Here’s a sample:

“When it’s planes in the sky for a chain of supply, that’s logistics.

When the parts for the line come precisely on time, that’s logistics.”

You can find the U.S. version of the ad, plus Chinese and Spanish versions, on YouTube.

Analogy and metaphor can also help you gain a better understanding of logistics; consider the following passage from a book written in 1917:

Strategy is to war what the plot is to the play. Tactics is represented by the role of the players; logistics furnishes the stage management, accessories, and maintenance. The audience, thrilled by the action of the play and the art of the performers, overlooks all of the cleverly hidden details of stage management.[**41**](https://jigsaw.vitalsource.com/books/9780134899763/epub/OPS/xhtml/fileP7001015395000000000000000003AA7.xhtml#P7001015395000000000000000003AFB)

As this quote suggests, many activities associated with logistics and supply-chain ­management take place “behind the scenes.” However, the supply chain’s vital role in global marketing has become more evident in recent years. The catastrophic earthquake and tsunami that struck Japan in March 2011 resulted in a tragic loss of life—but they also disrupted supply chains for a variety of industries, including automobiles and consumer electronics.

The ongoing political upheaval in the Middle East has also highlighted the importance of flexibility in global supply-chain design. For example, in spring 2011, P&G was forced to briefly close plants in Egypt that supply products for South Africa. During the closure, production from plants in Hungary and Turkey was redirected to supply the South African market. Such incidents explain why supply-chain managers use a term borrowed from the military, VUCA, to describe places that are “volatile, uncertain, complex, and ambiguous.”[**42**](https://jigsaw.vitalsource.com/books/9780134899763/epub/OPS/xhtml/fileP7001015395000000000000000003AA7.xhtml#P7001015395000000000000000003AFD)

For decades, Walmart’s mastery of logistics and supply-chain management was an important source of competitive advantage. The retailing giant’s basic value proposition is simple: getting goods to people as efficiently as possible. To do this, Walmart exploited a core competency: It leveraged its vast customer database to determine and anticipate what customers want and got it to them quickly and efficiently.

**Entrepreneurial Leadership, Creative Thinking, and the Global Startup**

Malcom McLean: Containerization Visionary

Malcom McLean was an entrepreneur. He developed an innovative industrial product and used it to help his business grow. Along the way, he revolutionized the way goods are shipped, thereby helping usher in the era of globalization. By applying the basic tools and principles of modern marketing, McLean achieved remarkable success. As is true with many entrepreneurs, McLean’s idea was based on his recognition of a problem that needed to be solved and the needs of his growing business. Recognizing the significant inefficiencies in terms of the time and costs associated with loading and unloading oceangoing freight, Maclean set about devising a solution that would streamline those labor-intensive processes.

Until the mid-twentieth century, shipping goods was slow and expensive. Longshoremen would unload as many as 200,000 separate pieces of cargo from trucks or warehouses near the docks and then stow each item on an oceangoing freighter. The process was reversed at the end of the voyage. The solution seemed obvious to McLean: What if freight was preloaded in boxes, and then those boxes could be picked up and loaded on the ship—and vice versa? The solution was containerization—the use of standardized steel boxes that could be loaded with freight at the factory and shipped by rail or by truck to a port. There, the entire box would be loaded onto the deck or into the ship’s hold.

As the late management guru Peter Drucker noted, innovation can occur when the wealth-producing potential of an existing resource is enhanced. This is exactly what happened when, in the 1950s, McLean helped change the definition of a “cargo vessel” from a “ship” to a “cargo-handling device.” In other words, McLean was pragmatic: He didn’t care about the “romance of the sea.” For him, freight was just freight. For years, innovation in the industry had focused on building faster ships that used less fuel and smaller crews. However, these costs were relatively small to start with. The real cost came when the ship was sitting idle when it was docked at port. The innovative solution was quite simple, focused, and specific; McLean’s insight was to uncouple the loading of freighters from the loading of the cargo.

As Marc Levinson notes in his book about McLean, the container turned the economics of location on its head. Containerization revolutionized the handling of cargo. McLean, the man who spearheaded the revolution, was originally a trucking industry magnate. His innovation—containerization—represented a profoundly disruptive technology. In the 1950s, Maclean sold his successful trucking company and bought Pan-Atlantic Steamship Company, which was renamed Sea-Land Service in 1960. Container and multimodal transportation quadrupled the productivity of oceangoing freighters and enabled the explosive growth of world trade after World War II.

“McLean’s real ­achievement was in changing the ­system that surrounded his box: the way that ships, ports, and docks were designed.”[**44**](https://jigsaw.vitalsource.com/books/9780134899763/epub/OPS/xhtml/fileP7001015395000000000000000003AA7.xhtml#P7001015395000000000000000003B01)

*Tim Harford, author, Fifty Inventions That Shaped the Modern Economy*

As is often the case when a disruptive technology is introduced, the container revolution created both winners and losers. Among the losers: New York City’s port system, which, in the 1950s, was the largest in the United States. Immortalized by Hollywood in the motion picture *On the Waterfront*, New York’s port system had several disadvantages. Notably, freight arriving by rail had to be floated across the Hudson River by barge, which resulted in higher costs in terms of both money and time. In addition, wildcat strikes and cargo theft, and the fact that many piers had fallen into disrepair, made New York increasingly unattractive as a shipping center. Today, things have come full circle, and the Port of New York is bustling again (see [**Exhibit 12-10**](https://jigsaw.vitalsource.com/books/9780134899763/epub/OPS/xhtml/fileP7001015395000000000000000003908.xhtml?favre=brett#P700101539500000000000000000392D)).

**Exhibit 12-10**

Prior to 1985, the Port of New York was the busiest container port in the world. Subsequently, it went into decline as ports on the West Coast and the South courted freight lines. Now, thanks to a high tide of imports from Asia, as well as major disruptions at West Coast ports, the Port of New York is experiencing a resurgence of traffic. Giant freighters leave China and travel through the Panama Canal en route to the East Coast.

*Source: Randy Duchaine/Alamy Stock Photo.*

*Sources: Mark Levinson, Keynote Address, Moving Iowa Forward Conference, Des Moines, Iowa, October 21, 2014; Mark Levinson, The Box: How the Shipping Container Made the World Smaller and the World Economy Bigger (Princeton, NJ: Princeton University Press, 2008); Peter F. Drucker, Innovation and Entrepreneurship (New York, NY: Harper & Row, 1985).*

Today, however, the company faces significant competitive threats in both food and nonfood categories. In the United States, more than two-thirds of Walmart customers also shop at dollar stores; meanwhile, Aldi is stepping up the pace of its new-store openings. Online giant Amazon has moved into brick-and-mortar grocery retail with its acquisition of Whole Foods. The shift to online shopping is gaining momentum as social media apps such as Pinterest add new functionality such as “Buy Now” buttons. In an effort to improve its e-commerce capabilities as it searches for new sources of competitive advantage, Walmart paid $3 billion to acquire Jet.com in 2016.[**43**](https://jigsaw.vitalsource.com/books/9780134899763/epub/OPS/xhtml/fileP7001015395000000000000000003AA7.xhtml#P7001015395000000000000000003AFF)

An industry’s value chain can change over time. In pharmaceuticals, for example, research, testing, and delivery were the three steps that historically defined the industry from its beginnings in the early nineteenth century. Then, starting in the mid-1960s, after Crick and Watson published their groundbreaking work on DNA, two new upstream steps in the industry’s value chain emerged: basic research into genes associated with specific diseases and identification of the proteins produced by those genes. More recently, with the mapping of the human genome largely complete, value in the pharmaceuticals industry is migrating downstream to identifying, testing, and producing molecules that operate on the proteins produced by genes.[**45**](https://jigsaw.vitalsource.com/books/9780134899763/epub/OPS/xhtml/fileP7001015395000000000000000003AA7.xhtml#P7001015395000000000000000003B03)

“We are trying to take advantage of the global factory. We are a global company; we should have a supply chain that reflects our customer base.”[**46**](https://jigsaw.vitalsource.com/books/9780134899763/epub/OPS/xhtml/fileP7001015395000000000000000003AA7.xhtml#P7001015395000000000000000003B05)

*Keith Sherin, former chairman and CEO, GE Capital*

The value chain, logistics, and related concepts are extremely important as supply chains stretch around the globe. As export administrator Beth Dorrell notes, “A commodity raw ­material from Africa can be refined in Asia, then shipped to South America to be incorporated into a ­component of a final product that is produced in the Middle East and then sold around the world.” [**Figure 12-5**](https://jigsaw.vitalsource.com/books/9780134899763/epub/OPS/xhtml/fileP7001015395000000000000000003908.xhtml?favre=brett#P7001015395000000000000000003941) illustrates some of these concepts and activities at IKEA, the global furniture marketer. IKEA purchases wood and other raw material inputs from a network of suppliers located in dozens of countries; these suppliers are upstream in the value chain, and the process by which wood is transported to the factories is known as *inbound logistics*. IKEA’s factories add value to the inputs by transforming them into furniture kits that are then shipped to IKEA’s stores. These stores are downstream in IKEA’s value chain; the activities associated with shipping furniture kits from factory to store are known as *outbound logistics*.[**47**](https://jigsaw.vitalsource.com/books/9780134899763/epub/OPS/xhtml/fileP7001015395000000000000000003AA7.xhtml#P7001015395000000000000000003B07)

**Figure 12-5 Supply Chain, Value Chain, and Logistics**

Physical distribution and logistics are the means by which products are made available to customers when and where they want them. The most important distribution activities are order processing, warehousing, inventory management, and transportation.

Order Processing

Activities related to order processing provide information inputs that are critical in fulfilling a customer’s order. [**Order processing**](https://jigsaw.vitalsource.com/books/9780134899763/epub/OPS/xhtml/fileP7001015395000000000000000004BB6.xhtml#P7001015395000000000000000004F73) includes *order entry*, in which the order is actually entered into the company’s information system; *order handling*, which involves locating, assembling, and moving products into distribution; and *order delivery*, the process by which products are made available to the customer.

In some instances, the customer is a consumer, as is the case when you place an order with [**Amazon.com**](http://amazon.com/) or Lands’ End. In other instances, the customer is a channel member.

Order processing can be targeted for improvement as a means to increase a company’s efficiency in distribution. For example, Pepsi Bottling Group overhauled its supply chain in an effort to eliminate out-of-stock inventory problems. The company’s handheld computers lacked ­wireless capability and required a hookup to a landline telephone service; by upgrading the technology, sales representatives can now enter orders wirelessly. Warehouse workers are equipped with barcode scanners and headsets so they can do a better job of ensuring that each pallet of drink ­products contains exactly what retailers ordered.[**48**](https://jigsaw.vitalsource.com/books/9780134899763/epub/OPS/xhtml/fileP7001015395000000000000000003AA7.xhtml#P7001015395000000000000000003B09)

In addition to using radio frequency identification (RFID) tags, retailers—especially those with e-commerce operations—are exploring the potential of industrial robots to pick out items in warehouses and distribution centers and put them in boxes for shipping. The drive to ­automate ­fulfillment holds the promise of significantly reducing the time and labor cost involved in ­preparing an order for shipment. The development process includes creating massive data sets and 3D ­renderings of individual inventory items. Meanwhile, just in the United States alone, [**Amazon.com**](http://amazon.com/) and other companies are hiring hundreds of thousands of distribution center employees in an effort to keep up with the torrid pace of online sales growth.[**49**](https://jigsaw.vitalsource.com/books/9780134899763/epub/OPS/xhtml/fileP7001015395000000000000000003AA7.xhtml#P7001015395000000000000000003B0B)

# Warehousing

Warehouses are used to store goods until they are sold; another type of facility, the *distribution ­center*, is designed to efficiently receive goods from suppliers and then fill orders for ­individual stores or customers. Modern distribution and warehousing is such an automated, high-tech ­business today that many companies outsource this function. For example, ODW Logistics Inc. operates several warehouses on behalf of Deere & Company, Limited Brands, and other ­customers. Much of ODW’s capacity is in Columbus, Ohio, a major U.S. port of entry for textiles.

One of the driving forces behind the growth of third-party warehousing is the need to reduce fixed costs and speed up delivery times to customers. ODW Logistics adds additional utility by tracking shipments from the time they leave the factory in, say, China, until they reach ­Columbus. This enables the company to alert retailers of possible delays due to weather issues or port ­congestion. In addition, as manufacturers ramp up adoption of RFID technology, ODW will split the cost of the new technology with its customers. As consultant John Boyd noted a decade ago, “Distribution warehousing is the next arena of corporate re-engineering and corporate cost-cutting.”[**50**](https://jigsaw.vitalsource.com/books/9780134899763/epub/OPS/xhtml/fileP7001015395000000000000000003AA7.xhtml#P7001015395000000000000000003B0D)

# Inventory Management

Proper inventory management ensures that a company neither runs out of manufacturing components or finished goods nor incurs the expense and risk of carrying excessive stocks of these items. As part of this quest, order-processing costs must be balanced against inventory-carrying costs. The more often a product is ordered, the higher the order-processing costs associated with unloading, stocking, packing for shipping, and related activities. The less frequently a product is ordered, the higher the inventory-carrying costs, because more product must be kept in inventory to cover the longer period between orders.

Social media can play an important role in inventory management. For example, Vetements is a luxury fashion label founded by Guram Gvasalia in 2014. Even with eye-popping prices such as $1,300 for a pair of jeans made from recycled denim, the company quickly scaled up to $100 million in annual sales. How? For one thing, rigorous wholesale management and a digital strategy that connects the brand’s nearly 2 million Instagram followers to its global inventory.[**51**](https://jigsaw.vitalsource.com/books/9780134899763/epub/OPS/xhtml/fileP7001015395000000000000000003AA7.xhtml#P7001015395000000000000000003B0F)

Transportation

Transportation decisions concern the method, or *mode*, a company should utilize when moving products through domestic and global channels. The word *mode* implies a choice, and the major transportation mode choices are rail, truck, air, water, pipeline, and the Internet. Each of these modes has its advantages and disadvantages, as summarized in [**Table 12-4**](https://jigsaw.vitalsource.com/books/9780134899763/epub/OPS/xhtml/fileP7001015395000000000000000003956.xhtml?favre=brett#P7001015395000000000000000003959). However, a particular mode may be unavailable in some countries because of an underdeveloped infrastructure or geographic barriers. In addition, pipelines are highly specialized and are used only by companies transporting energy-related resources such as oil and natural gas.

**Table 12-4 Comparison of Major International Transportation Modes**

| **Mode** | **Reliability** | **Cost** | **Speed** | **Accessibility** | **Capability** | **Ease of Tracing** |
| --- | --- | --- | --- | --- | --- | --- |
| Rail | Average | Average | Average | High | High | Low |
| Water | Low | Low | Slow | Low | High | Low |
| Truck | High | Varies | Fast | High | High | High |
| Air | High | High | Fast | Low | Moderate | High |
| Pipeline | High | Low | Slow | Low | Low | Moderate |
| Internet | High | Low | Moderate to fast | Moderate; increasing | Low | High |

By the numbers: 8.5 million barrels of oil are pumped in the United States every day. Most is transported by pipeline, but 1.6 million ­barrels—almost 20 percent of the total—travels by rail.

*Source: US. Energy Information Agency.*

*Rail* provides an extremely cost-effective means for moving large quantities of merchandise long distances. In the United States, carriers such as CSX and Burlington Northern Santa Fe (BNSF) account for nearly half of all cargo moved when measured by ton-miles. Rail’s capability is second only to water in terms of the variety of products that can be transported. However, trains are less reliable than trucks. Poor track maintenance leads to derailments, and bottlenecks on heavily traveled lines can create delays.

*Trucks* are an excellent mode for both long-haul, transcontinental transport and local delivery of goods. In nations with well-developed highway systems, truck freight combines the advantage of fast delivery times with the highest level of accessibility of any mode. Thanks to modern information technology, truck shipments are also easily traced. However, in countries with poorly developed infrastructures, truck deliveries can move much more slowly. India is a case in point.

The two main types of water transportation are inland water and ocean transportation. *Inland water transportation* is an extremely low-cost mode generally used to move agricultural commodities, petroleum, fertilizers, and other goods that, by their nature, lend themselves to bulk shipping via barge. However, inland water transportation can be slow and subject to weather-related delays. Virtually any product can be shipped via *ocean transportation*. The world’s deepwater ports can receive a variety of types of oceangoing vessels, such as container vessels; bulk and break-bulk vessels; and roll-on, roll-off (ro-ro) vessels. Although sailing times are not competitive with air transportation, it is generally more cost-effective to ship large quantities of merchandise via ocean than by air. Denmark’s Maersk Sealand is the world’s largest shipping container line (see [**Table 12-5**](https://jigsaw.vitalsource.com/books/9780134899763/epub/OPS/xhtml/fileP7001015395000000000000000003956.xhtml?favre=brett#P70010153950000000000000000039C9)).

**Table 12-5 Leading Container Shipping Lines**

*Source: Compiled by authors from company reports.*

| **Carrier** | **Number of Vessels** |
| --- | --- |
| A. P. Moller-Maersk (Denmark) |  600+ |
| Mediterranean Shipping Company MSC (Switzerland) | 458 |
| CMA-CGM (France) | 414 |
| Evergreen Marine (Taiwan) | 182 |
| Cosco (China) |  130+ |

Why is water rated “low” in reliability? In any given year, approximately 200 freighters sink due to bad weather or other factors (see [**Exhibit 12-11**](https://jigsaw.vitalsource.com/books/9780134899763/epub/OPS/xhtml/fileP7001015395000000000000000003956.xhtml?favre=brett#P70010153950000000000000000039E8)). Compounding the tragic loss of human lives is the fact that the cargo ends up on the ocean floor. Cargo can also sometimes be lost without a ship sinking. For example, in 1997 a huge wave rocked the freighter *Tokio Express* in the waters off Land’s End, England. Several dozen shipping containers were tossed overboard, including one containing nearly 5 million LEGO pieces. The container was bound for Connecticut, where the pieces were to be assembled into kits. One year later, LEGO pieces began washing ashore in Florida!

**Exhibit 12-11**

Container ships can be lost in storms or run aground, resulting in tragic loss of life. If cargo containers can’t be salvaged, they may end up on the ocean floor.

*Source: Maritime New Zealand/ZUMAPRESS/Newscom.*

Losses can occur even when the cargo remains on board and the ship doesn’t sink. For example, the *Cougar Ace*, a freighter loaded with 4,700 new Mazdas, narrowly avoided sinking in the Pacific in 2006. The cars were strapped down, but the ship listed at a 60-degree angle for weeks before being righted. Concerned that the cars might not be saleable, management decided to destroy the entire shipment, which was valued at $100 million.[**52**](https://jigsaw.vitalsource.com/books/9780134899763/epub/OPS/xhtml/fileP7001015395000000000000000003AA7.xhtml#P7001015395000000000000000003B12)

Piracy on the high seas is another factor affecting the reliability of water as a transport mode. In recent years, pirates operating in the Indian Ocean off the coast of Africa have fired upon and attempted to board dozens of commercial vessels. In some instances, the pirates have succeeded in boarding ships and hijacking the cargo. In one case, pirates captured the captain of an American-flagged ship carrying food aid to East Africa.

*Air* is the fastest transport mode and the carrier of choice for perishable exports such as flowers or fresh fish, but it is also the most expensive. The size and the weight of an item may indicate that it is more cost-effective to ship the product via air rather than ocean transportation. If a shipment’s delivery is time sensitive, such as an emergency parts replacement, air is also the logical mode.

Thanks to the digital revolution, the *Internet* is an important transportation mode that is associated with several advantages and one major disadvantage. First, the bad news: The Internet’s capability is low. As Nicolas Negroponte, former director of MIT’s Media Lab, has famously observed, as long as something consists of atoms, it cannot be shipped via the Internet. However, anything that can be digitized can be sent via the Internet. Advantages of this mode include low cost and high reliability. Accessibility is increasing as the mobile revolution picks up speed; today, it is estimated that half the world’s population has Internet access. Speed depends on several ­factors, including bandwidth. In recent years, improvements in broadband technology and cellular infrastructure have provided much of the world with on-ramps to the Internet superhighway. Facebook, Netflix, Spotify, and WhatsApp are just a few of the beneficiaries of this trend.

*Channel strategy* involves an analysis of each shipping mode to determine which mode, or combination of modes, will be both effective and efficient in a given situation. A number of firms specializing in third-party logistics are available to help companies with transportation logistics. For example, C. H. Robinson Worldwide matches shippers with trucking companies and other carriers in all parts of the world. One aspect of transportation technology that has revolutionized global trade is containerization—a concept that was first utilized in the United States starting in the mid-1950s. [**Containerization**](https://jigsaw.vitalsource.com/books/9780134899763/epub/OPS/xhtml/fileP7001015395000000000000000004BB6.xhtml#P7001015395000000000000000004C9E) refers to the practice of loading oceangoing freight into steel boxes measuring 20 feet, 40 feet, or longer. Containerization offers many advantages, including flexibility in the products that can be shipped via container, as well as flexibility in shipping modes.

[**Intermodal transportation**](https://jigsaw.vitalsource.com/books/9780134899763/epub/OPS/xhtml/fileP7001015395000000000000000004BB6.xhtml#P7001015395000000000000000004E9E) of goods involves a combination of land and water shipping from producer to customer.[**53**](https://jigsaw.vitalsource.com/books/9780134899763/epub/OPS/xhtml/fileP7001015395000000000000000003AA7.xhtml#P7001015395000000000000000003B14) In the United States alone, railroads handle more than $150 billion in seaport goods—a statistic that is a testament to intermodal transportation’s growing importance. Unfortunately, lack of investment in America’s rail infrastructure has resulted in delays at seaports. As Bernard LaLonde, a professor of transportation and logistics, noted two decades ago, “It’s the Achilles’ heel of global distribution. The ships keep getting bigger and faster. Trade keeps growing. But we don’t have the rail links we need.”[**54**](https://jigsaw.vitalsource.com/books/9780134899763/epub/OPS/xhtml/fileP7001015395000000000000000003AA7.xhtml#P7001015395000000000000000003B16)

The decision of which mode of transportation to use may be dictated by a particular market situation, by the company’s overall strategy, or by conditions at the port of importation. For example, every November, winemakers from France’s Beaujolais region participate in a promotion celebrating the release of the current vintage. Although wine destined for European markets may travel by rail or truck, U.S.-bound wine is shipped via air freight: Speed is of the essence when producers of Beaujolais nouveau are racing to get their products to the market. Normally, owing to weight and bulk considerations, French wine makes the transatlantic journey by water. Similarly, Acer Group ships motherboards and other high-tech components from Taiwan via air freight to ensure that the latest technology is incorporated into its computers. Bangladesh’s primary port, Chittagong, is subject to congestion, frequent delays, and strikes, which forces Gap and other clothing companies to ship via air.

Every Christmas, supplies of the season’s hottest-selling toys and electronics products are shipped via air from factories in Asia to ensure their just-in-time delivery by Santa Claus. Sony’s PlayStation 3 is a case in point; in the fall of 2006, the company shipped hundreds of thousands of PS3 units by air to the United States. Likewise, in 2007, the first shipments of Apple’s highly anticipated iPhone arrived from Asia via air freight. An estimated $1 billion is added to U.S. shipping costs each year because companies are forced to compensate for railway delays by keeping more components or parts in inventory or by shipping via air.

# Logistics Management: A Brief Case Study

The term [**logistics management**](https://jigsaw.vitalsource.com/books/9780134899763/epub/OPS/xhtml/fileP7001015395000000000000000004BB6.xhtml#P7001015395000000000000000004EDE) describes the integration of activities necessary to ensure the efficient flow of raw materials, in-process inventory, and finished goods from producers to ­customers. JCPenney provides a case study in the changing face of logistics, physical distribution, and retail supply chains in the twenty-first century. Several years ago, Penney’s management team made a key decision to outsource most elements of its private-label shirt supply chain to TAL Apparel Ltd. of Hong Kong. Penney’s North American stores carry almost no extra inventory of house-brand shirts; when an individual shirt is sold, EPOS scanner data are transmitted directly to Hong Kong. TAL’s proprietary computer model then determines whether to replenish the store with the same size, color, and style. Replacement shirts are sent directly to stores without passing through Penney’s warehouse system; sometimes the shirts are sent via air, sometimes by ship.

This approach represents a dramatic departure from past practices; Penney’s typically carried 6 months’ worth of inventory in its warehouses and 3 months’ inventory in stores. By working closely with TAL, the retailer can lower its inventory costs, reduce the quantity of goods that have to be marked down, and respond more quickly to changing consumer tastes and fashion styles. However, as Wai-Chan Chan of McKinsey & Company Hong Kong noted, “You are giving away a pretty important function when you outsource your inventory management. That’s something that not a lot of retailers want to part with.”[**55**](https://jigsaw.vitalsource.com/books/9780134899763/epub/OPS/xhtml/fileP7001015395000000000000000003AA7.xhtml#P7001015395000000000000000003B18)

# Summary

A *channel of distribution* is the network of agencies and institutions that links producers with users. *Physical distribution* is the movement of goods through channels. *Business-to-consumer (b-to-c) marketing* uses consumer channels; *business-to-business (b-to-b) marketing* employs industrial channels to deliver products to manufacturers or other types of organizations. *Peer-to-peer* marketing via the Internet is another channel. *Distributors* and *agents* are key intermediaries in some channels. Channel decisions are difficult to manage globally because of the variation in channel structures from country to country. Marketing channels can create *place utility*, *time utility*, *form utility*, and *information utility* for buyers. The characteristics of customers, products, middlemen, and the environment all affect channel design and strategy.

Consumer channels may be relatively direct, utilizing direct-mail or door-to-door selling, as well as manufacturer-owned stores. A combination of manufacturers’ sales forces, agents/brokers, and wholesalers may also be used. Channels for industrial products are less varied, with manufacturers’ sales forces, wholesalers, and dealers or agents being used.

*Global retailing* is a growing trend as successful retailers expand around the world in support of their growth objectives. Retail operations take many different forms, including *department stores*, *specialty retailers*, *supermarkets*, *convenience stores*, *discount retailers*, *hard discounters*, *hypermarkets*, *supercenters*, *superstores*, *shopping malls*, *outlet stores*, and *outlet malls*. Selection, price, store location, and customer service are a few of the competencies that can be used strategically to enter a new market. One way to classify retailers is by using a matrix that distinguishes companies offering few product categories with an own-label focus, many categories with an own-label focus, few categories with a manufacturer-brand focus, and many categories with a manufacturer-brand focus. Global retail expansion can be achieved via *organic growth*, *franchising*, *acquisition*, *joint venture*, and *licensing*.

Transportation and physical distribution issues are critically important in a company’s value chain because of the geographical distances involved in sourcing products and serving customers in different parts of the world. A company’s *supply chain* includes all the firms that perform support activities such as generating raw materials or fabricating components. *Logistics* and *logistics management* integrate the activities of all companies in a firm’s value chain to ensure an efficient flow of goods through the supply chain. Important activities include *order processing*, *warehousing*, and *inventory management*. To cut costs and improve efficiency, many companies are reconfiguring their supply chains by outsourcing some or all of these activities. Six transportation modes—air, truck, water, rail, pipeline, and Internet—are widely used in global distribution. *Containerization* was a key innovation in physical distribution that facilitates *intermodal transportation*.

# Discussion Questions

1. 12-1. In what ways can channel intermediaries create utility for buyers?
2. 12-2. Which factors influence the channel structures and strategies available to global marketers?
3. 12-3. Compare and contrast the typical channel structures for consumer products and ­industrial products.
4. 12-4. Identify the different forms of retailing, and cite an example of each. Identify retailers from as many different countries as you can.
5. 12-5. Identify the four retail market expansion strategies discussed in the text. Which factors determine the appropriate mode?
6. 12-6. Many global retailers are targeting China, India, and other emerging markets. In terms of the strategies described in [**Figure 12-4**](https://jigsaw.vitalsource.com/books/9780134899763/epub/OPS/xhtml/fileP70010153950000000000000000038DF.xhtml#P70010153950000000000000000038E3), what would be the most likely entry ­strategies for these countries?
7. 12-7. Which special distribution challenges exist in Japan? What is the best way for a non-Japanese company to deal with these challenges?

# Case 12-1 continued (refer to page 376) Welcome to the World of Fast Fashion

So, what puts the “fast” in “fast fashion”? A behind-the-scenes peek at Zara shows how, say, a woman’s winter coat can go from a designer’s sketchpad to store display racks in less than one month.

The product development process begins with a designer in Spain creating a sketch that incorporates feedback from Zara’s worldwide network of store managers about the latest trends (zippers? plaids? Millennial Pink?). Next, a pattern maker creates a prototype of the garment; if it’s approved, a pattern is created and used to cut fabric. These steps take a total of about seven days.

Over the course of the next two weeks, pattern cutters and seamstresses physically produce the correct number of units (typically, a few thousand). It takes an additional week for the coats to be pressed; tags and labels are added, and each garment undergoes a quality inspection. The entire production lot is then transported to the company’s centralized logistics center, where the items are boxed and dispatched within 48 hours. For example, orders bound for New York may be shipped by air to John F. Kennedy Airport on Long Island, and then sent by truck to various Zara stores in the metro New York area. All stores receive orders twice weekly.

As this scenario shows, one key to Zara’s success has been keeping manufacturing close to its home base—if not in Spain, then in nearby Morocco, Portugal, or Turkey. Another key is flexibility; if a particular item is not selling well in one location, that inventory can be quickly shifted to another location where demand is strong. Also, production runs of even hot-selling items are limited; this helps Zara convey an air of exclusivity that translates into higher prices and fewer markdowns.

“Think of Zara not as a brand, but as a very speedy chameleon that adapts instantly to fashion trends.”[**56**](https://jigsaw.vitalsource.com/books/9780134899763/epub/OPS/xhtml/fileP7001015395000000000000000003AA7.xhtml#P7001015395000000000000000003B1A)

*Anne Chrichlow, analyst, Société Générale*

The production process is somewhat different at Zara’s competitors. The bulk of H&M’s production is ordered months ahead of time, and then shipped to warehouses. By the time an item gets to stores, however, fashion trends may have changed. Unsold stock must then be marked down for clearance, which dampens profits. The company has continued to open more brick-and-mortar stores even as the movement of consumers to online shopping gains traction.

As noted in the chapter introduction, H&M has faced other challenges in recent years. Unlike Zara, H&M’s decentralized supply chain stretches to Asia, where company-approved subcontractors may redirect some orders to other factories that have not passed inspections. Such instances result in a loss of control over where products are sourced.

Uniqlo founder Tadashi Yanai has also faced challenges. After Japan’s economy had suffered from more than a decade of deflation, Yanai made a strategic bet that he could raise profits by increasing prices in Uniqlo stores by 5 to 10 percent. It didn’t work; as at H&M, the company had to resort to markdowns to clear out unsold inventory. In 2016, Yanai announced that Uniqlo’s Japanese stores would return to “everyday low pricing.” Although sales have recovered since the change in the pricing policy, the number of shoppers visiting Uniqlo stores has been falling. Taking a page from Zara’s strategy book, Yanai will open a new distribution center in Japan and centralize product development in an effort to get inventory into stores more quickly.

# Is Fast Fashion Sustainable?

Some observers criticize the fast-fashion business model on the grounds that it can lead to worker exploitation; that it encourages uniformity of consumption; that it feeds a culture of disposability; and that it creates waste. In addition, it breeds the perception among consumers that the prices charged by some purveyors of well-made, high-quality apparel are exorbitant ($300 Brunello Cucinelli T-shirts, anyone?).

In a 2005 book titled *The Travels of a T-Shirt in the Global Economy: An Economist Examines the Markets, Power, and Politics of World Trade*, author Pietra Rivoli examined the global apparel supply chain. Among her conclusions: While the global apparel trade has its downsides, it can also be beneficial. Elizabeth L. Cline, author of a recent book on fast fashion, frames her own critique this way:

A half-century of competition based on low price has forced the fashion industry to cut corners on quality, construction, and detail, leaving most of us wearing very basic and crudely slapped together clothes.

Worker safety in the garment industry is a key issue in Bangladesh, which ranks as the world’s number 4 clothing exporter. Bangladesh has benefited from rising wages in China that have increased the cost of manufacturing there. Indeed, approximately 80 percent of Bangladesh’s export earnings comes from its network of more than 5,000 garment manufacturing operations. However, the garment industry has been roiled by a series of tragedies that have highlighted the often-dangerous conditions facing workers.

In 2010, dozens of Bangladeshis were killed in two separate fires in factories that made clothing for Western clients such as H&M, JCPenney, and Gap. In November 2012, 117 garment workers were confirmed to have died when a fire broke out at Tazreen Fashions, a clothing manufacturer in Dhaka, Bangladesh. Tazreen’s clients included Walmart and other well-known global retail brands. The tragedy highlighted failures to adhere to the Bangladesh Fire and Building Safety Agreement, a contract that increasing numbers of workers, unions, and marketers have signed.

In April 2013, tragedy struck another factory in Dhaka. The death toll—most of the victims were women—ultimately came to 1,134 people. In this instance, however, fire was not the cause. Rather, the eight-story Rana Plaza building in Dhaka collapsed. The building housed garment factories that employed about 5,000 garment workers making clothing such as the Joe Fresh line for Loblaw, a Canadian retailer; Italy’s Benetton was another customer.

In the aftermath of the tragedy, it was revealed that the building’s owner was a local politician who had not obtained the necessary permits from Dhaka’s building-safety authority. Some of the factories in the Rana Plaza building had been certified in audits conducted by the Business Social Compliance Initiative (BSCI). The BSCI was launched by the Foreign Trade Association, an agency that represents hundreds of European retailers. Its auditors were not engineers, however, and had not made recommendations regarding building safety and stability.

The response from Western retailers was swift. For example, although Walmart had forbidden its contractors from using the Tazreen factory, some of its clothing was found at the scene of the 2012 fire. Walmart has since implemented a “zero-tolerance policy” for contractors who use factories without authorization. Walmart also donated $1.6 million to provide fire-safety training to garment workers in Bangladesh.

In 2013, the owners of several global brands in the ready-made garment industry signed a five-year agreement known as the Bangladesh Accord on Fire and Safety. The purpose of the Accord was to provide factory inspections and ensure that repairs and upgrades such as fire-safety systems were being made. In 2018, H&M and Zara parent Inditex announced that the Accord would be extended for another three years.

Despite such efforts, the Workers Rights Consortium, the International Labor Organization, the Interfaith Center for Corporate Responsibility, and other groups that monitor labor issues are stepping up pressure on the companies that participate in the global garment supply chain. Too often, the activists charge, Western retailers pay lip service to concerns about factory safety; in reality, critics say, the retailers continue to focus on low prices rather than the welfare of workers. As the head of the Cambodian garment manufacturers association told the Financial Times, “The buyer and consumer must be willing to pay more.”

The Robotics Revolution

While many labor abuses have been documented in the garment industry, it is also true that the jobs in apparel factories may be the only opportunities for employment available to some people living in developing countries. In Bangladesh alone, nearly 4 million people work in the clothing business, earning a minimum wage of about $64 per month (see [**Exhibit 12-12**](https://jigsaw.vitalsource.com/books/9780134899763/epub/OPS/xhtml/fileP7001015395000000000000000003A3F.xhtml?favre=brett#P7001015395000000000000000003A42)). Their jobs are not necessarily secure, however, as the industry is gradually becoming automated. Today, computerized machinery can make the same sweater for H&M or Zara that humans operating sewing machines have traditionally made. Just as advances in machine learning and artificial intelligence are making robotic inventory picking possible, so, too, can robots be trained to handle soft materials such as thread and fabric.

**Exhibit 12-12**

Contract apparel manufacturers in India and other low-wage countries are integral to fast fashion's global supply chain. The factory shown here is "fair trade" certified, paying above-average wages and embracing sustainability practices such as using organic textiles.

*Source: Joerg Boethling/Alamy Stock Photo.*

The upshot is that Bangladesh’s garment industry is not creating enough new jobs to accommodate the country’s growing labor force. As is the case in India, an estimated 1 million Bangladeshis join the work force every month. With automation threatening to take the place of low-skilled labor in the industry, many women may lose their jobs. Industry observers worry that job-retraining opportunities may not be available for these women.

Recycling and Upcycling

The myriad choices of inexpensive clothing mean that many items are donated or discarded after being worn just a few times. In many developed countries, donation bins are widely available; some retailers, including H&M, offer discounts to shoppers who bring in donations of used clothing when they visit a store to make new purchases.

Those cast-off items find their way into a separate supply chain that winds through India and then on to Africa and other developing countries. Donations made to charity shops in the United States and elsewhere may be sold to intermediaries who bundle them into giant bales and ship them to India for recycling (see [**Exhibit 12-13**](https://jigsaw.vitalsource.com/books/9780134899763/epub/OPS/xhtml/fileP7001015395000000000000000003A4B.xhtml?favre=brett#P7001015395000000000000000003A4F)). There, processing companies employ sorters to divide the contents of each bale into scores of different apparel categories for resale. Sometimes the sorters make valuable finds, such as vintage denim jeans or luxury brands.

**Exhibit 12-13**

Overproduction is a problem in the fashion industry. Sometimes, unsold merchandise ends up in landfills. India imports tons of used clothing; after processing, the majority of items are re-exported to emerging markets.

*Source: Allison Joyce.*

Items that are damaged or stained are separated out. Some items that are in good shape can’t be resold, however; this is especially true of garments that originate in the United States. The reason? In the case of men’s and women’s trousers, the waist sizes are often too big for customers in the rest of the world. Some items that can’t be resold are broken down into rags after buttons, zippers, and other ornamentation are removed. Any remaining items are ground into fiber that can be spun into yard that is upcycled into new items.

Markets Are Local, Markets Are Global

As noted in the chapter introduction, local fashion designers in India are beginning to emerge from the shadow of the global giants. A similar trend is taking shape in Rwanda, where an NGO called Fashion Hub Kigali has been established to help support designers. For example, Priscilla Ruzibuka started a label focusing on casual clothing for children (see [**Exhibit 12-14**](https://jigsaw.vitalsource.com/books/9780134899763/epub/OPS/xhtml/fileP7001015395000000000000000003A58.xhtml?favre=brett#P7001015395000000000000000003A5B)). Ms. Ruzibuka employs underprivileged women, some of whom suffered ill effects from the violence and genocide that occurred in Rwanda in the 1990s.

**Exhibit 12-14**

Ki-Pepeo is the brainchild of Rwandan entrepreneur Priscilla Ruzibuka. After recognizing an opportunity to design and produce children's apparel locally, Ruzibuka teaches women to sew clothing and helps them become skilled tailors.

*Source: JACQUES NKINZINGABO/The New York Times/Redux.*

Other Rwandan designers include Muhire Patrick, an entrepreneur who established his own atelier after he couldn’t find suitable attire to wear to his sister’s wedding. Joselyne Umutoniwase, founder of Rwanda Clothing, creates modern African designs for both men and women. These and other designers take advantage of Made in Rwanda, a government initiative designed to support locally produced clothing and reduce the flow of imported apparel.

Discussion Questions

1. 12-8. What is so appealing about fast-fashion brands such as H&M and Zara?
2. 12-9. Fast fashion has been criticized on the grounds that the same “looks” are found on display racks everywhere and that the clothing itself may be poorly constructed. Do you agree?
3. 12-10. Is the fashion industry doing enough to create sustainable supply chains? What about the issue of discarded clothing items that have never been worn or barely been worn?

*Sources: Shivani Vora, “Trying to Create Many Threads That Run True,” The New York Times (April 8, 2018), p. 10; John Emont, “Bangladesh Still Grapples with Safety Issues,” The Wall Street Journal (March 30, 2018), p. B1; Tiffany Hsu, “How to Prevent a Racist Hoodie,” The New York Times (March 30, 2018), pp. B1, B5; Richard Milne, “H&M Faces a New Reality in Fashion,” Financial Times (February 9–10, 2018), p. 13; Patricia Kowsman, “A Model for Fast Fashion,” The Wall Street Journal (December 7, 2016), pp. B1, B2; Kana Inagaki, “Uniqlo’s Pricing U-Turn Pays Off,” Financial Times (July 25, 2016), p. 14; Preetika Rana, “Indian Retailer Makes ‘Fast Fashion’ Local,” The Wall Street Journal (July 22, 2016), p. B6; Eric Bellman, “Fashion Feeds a Recycling Network,” The Wall Street Journal (June 27, 2016), pp. B1, B2; Joseph Allchin and Amy Kamzin, “Clothes Groups in Factory Safety Row,” Financial Times (October 2, 2015), p. 16; Kate O’Keeffe, “Supply Chain Trips H&M,” The Wall Street Journal (May 22, 2013), p. B3; Elizabeth L. Cline “Overdressed: The Shockingly High Cost of Cheap Fashion.” Published by Portfolio/Penguin. Copyright © Elizabeth L. Cline, 2012. Wall Street Journal.*

**Case 12-2 Can Walmart Crack the Retail Code in India?**

Walmart, the discount retail giant whose very name can strike fear in the hearts of small-town retailers in the United States, has gone global. To reach customers around the world, the company utilizes a variety of retail formats, including discount stores, supercenters that feature a full line of groceries and general merchandise, and Sam’s Club, a warehouse operation offering goods in unbroken bulk packages. As Walmart extends its reach around the globe, observers are using words such as “assault” and “invasion” to describe what it’s like for a nation on which the company has fixed its sights. As the chief executive of one supplier noted, “Walmart is going to change the retailing landscape internationally exactly the same way it’s done domestically.”

Not surprisingly, the BRICS (Brazil, Russia, India, China, and South Africa) nations are integral to Walmart’s global expansion plans. In India, for example, strict government regulations once meant that the retail market was essentially closed to foreigners, but that situation is now changing. Walmart began its foray into that country by operating a liaison office in India from which it conducted market research and lobbied Indian policymakers. India’s annual retail market is worth $500 billion, and analysts expect the retail sector to grow at a rate of 7 percent over the next few years. Today, more than 90 percent of retail activity is generated by small shops, newspaper kiosks, and tea stalls (see [**Exhibit 12-15**](https://jigsaw.vitalsource.com/books/9780134899763/epub/OPS/xhtml/fileP7001015395000000000000000003A73.xhtml?favre=brett#P7001015395000000000000000003A78)).

**Exhibit 12-15**

This Bharti-Walmart store on the outskirts of Chandigarh, India, is a wholesale supplier to India’s many small shopkeepers. In 2012, India agreed to open its market to foreign retailers such as Walmart as part of an economic reform program aimed at jump-starting growth in the country’s sputtering economy. The reforms mean that Walmart will be able to open retail stores.

*Source: Saurabh Das/Associated Press.*

Regulatory reforms passed in fall 2012 will finally allow Walmart and other foreign big-box retailers to sell directly to consumers. Yet, despite Walmart’s potential to transform India’s retail sector for the better, some observers have concerns about the company’s presence there. Western-style, big-box retailing is anathema to many Indian activists and policymakers, who fear that Walmart will drive some of India’s millions of shopkeepers out of business. Legislators are also suspicious of the company’s motives—an attitude that can be traced back to the colonial era and the operations of the British East India Company. Perhaps, they fear, the foreigners will raise prices after they have driven small ­operators out of business.

So why does Walmart persist? Because success in India is critical to CEO Doug McMillon global marketing strategy. Confronted with saturated markets in the United States and other developed countries, McMillon understands that the company needs to establish a bigger presence and build scale in emerging markets, such as India, where modern stores make up roughly 7 percent of the country’s retail industry.

Global retailers that have set their sights on India face special challenges. As noted previously in this chapter, the term *organized retail* is used to describe activity by large branded retail chains such as ­Woolworths, Tesco, and Walmart. Such stores currently account for only a small percentage of India’s nearly $500 billion in annual retail sales.

There have been many calls for regulatory reform, and some ­observers believe organized retailing will grow at a rate of 30 to 35 ­percent in the next few years. For now, however, some members of the ruling National Congress Party are concerned about the impact of organized retail on the millions of small-scale, “mom-and-pop” stores. The vast majority of Indian retail activity is conducted in cramped stalls with approximately 50 square feet of floor space.

Modernization of the sector is inevitable, although it has been slow in coming. Until the law was changed in 2012, Walmart and other global retailers that sell multiple brands were barred from participating directly in the Indian market. In 2006, Bharti Enterprises, a local business group that operates India’s largest cellular network, announced a joint-venture partnership with Walmart. However, because of restrictions in place at the time, the venture consisted of wholesale stores. When single-brand retailers such as Benetton, Nike, Pizza Hut, Reebok, and Subway first came to India, they were required to use franchising as a market-entry strategy.

The recent regulatory changes will make it easier for such companies to have a majority stake in Indian operations. Even so, the deal comes with strings attached: The government has demanded that foreign retailers invest $100 million in India, with at least half the money going to “back end” operations and infrastructure, including cold storage facilities and transportation infrastructure. For its part, the government pledged more than $4 billion in infrastructure improvements. In addition, each of India’s 28 states retains the right to approve or ban foreign-owned stores.

Western retailers often have to work with local vendors to help them improve their quality. For example, when the Bharti–Walmart venture was opening its wholesale cash-and-carry supercenters that serve small retailers, it had to contend with India’s poor infrastructure and inefficient supply chains, which stem from producers using outdated techniques. Produce is typically transported on open trucks, horse-drawn carts, and tractors to wholesale markets in large cities. There, it passes through the hands of traders and agents licensed by the Agriculture Produce Marketing Committee. It is then transferred to smaller markets or warehouses that are not temperature-controlled. By the time it gets to consumers, the produce has passed through as many as seven intermediaries; perhaps not surprisingly, much of it is spoiled. In fact, according to government estimates, one-third of the country’s produce—worth $10 billion—spoils each year.

In India, Walmart must do much more than just set up wholesale and retail stores. For example, it is trying to transform India’s agriculture sector by using its hyperefficient practices to improve productivity and speed the flow of produce and other goods. Walmart and a partner, Bayer Cropscience, are working with farmers to improve yields and quality. In addition, Walmart has begun bypassing traditional middlemen by signing up farmers and sending its own refrigerated trucks to the farms. One reason farmers like working with Walmart: The global giant pays the farmers promptly.

Meanwhile, anticipating the arrival of the global retailers, local operators in India are investing for the future. For example, Pantaloon Retail Ltd., India’s largest retailer, operates the Central and Big Bazaar department store chains and Food Bazaar, a supermarket chain. Kishore Biyani, Pantaloon’s chief executive, has succeeded by giving lower-middle-class shoppers a familiar retail experience: cramped stores with an environment that Western shoppers would find chaotic. Large business groups such as Reliance Industries, a petroleum refiner, and Birla Group have also entered the retail sector. Meanwhile, Hindustan Lever, the Indian unit of packaged goods giant Unilever, has launched a consultancy service to help the “mom-and-pop” retail operators become more competitive.

During his tenure as Walmart’s CEO, Mike Duke was undaunted by the challenges his company faced. In his view, the Indian people are missing out on the opportunity because of supply chain inefficiencies. But he expressed faith that, over time, the process, would get worked out. Meanwhile, Duke moved ahead in other key emerging markets. In Africa, for example, Walmart spent $2.4 billion to acquire a stake in Massmart, a chain with 288 stores in South Africa and 13 other African countries. Although South Africa’s population numbers only 50 million, those people have embraced shopping, and the transportation infrastructure and banking and telecommunications systems are well developed. A successful market entry in South Africa will serve as a springboard for Walmart to expand throughout the continent. Needless to say, managers at local companies that win contracts to supply the global giant are hoping that they can tag along and join the global supply chain.

# Discussion Questions

1. 12-11. What are the biggest obstacles facing Walmart and other foreign retailers in India?
2. 12-12. Summarize some of the elements in India’s political, economic, and cultural environments that can impact the market opportunity there.
3. 12-13. Review [**Figure 12-4**](https://jigsaw.vitalsource.com/books/9780134899763/epub/OPS/xhtml/fileP70010153950000000000000000038DF.xhtml#P70010153950000000000000000038E3). Which quadrant of the matrix applies most directly to India? Why?
4. 12-14. Going forward, to what degree will Walmart be required to adapt its business model in India?

*Sources: Amol Sharma, “Bad Roads, Red Tape, Burly Thugs Slow Wal-Mart’s Passage to India,”*The Wall Street Journal*(January 12–13, 2013), pp. A1, A10; Shelly Banjo, “Japan, Ready for Wal-Mart,”*The Wall Street Journal*(September 26, 2012), p. B6; Vikas Bajaj, “Skepticism and Caution Greet India’s New Policy on Retailers,”*The New York Times*(September 20, 2012), p. B1; Sharma, “India Revives Plan to Let in Retailers,”*The Wall Street Journal*(September 15–16, 2012), p. A8; Robb M. Stewart, “Wal-Mart Checks out a New Continent,”*The Wall Street Journal*(October 27, 2010), p. B1; Bajaj, “In India, Wal-Mart Goes to the Farm,”*The New York Times*(April  13, 2010), p. B1; Eric Bellman and Cecilie Rohwedder, “Western Grocer Modernizes ­Passage to India’s Markets,”*The Wall Street Journal*(November 28, 2007), p. B2; ­Bellman, “Chaos Theory: In India, a Retailer Finds Key to Success Is Clutter,”*The Wall Street Journal*(August 8, 2007), p. A8; Bellman, “India’s Reliance Looks Abroad,”*The Wall Street Journal*(March 16, 2007), pp. A1, A10; Jo Johnson and Jonathan Birchall, “‘Mom and Pop’ Stores Braced for Challenge,”*Financial Times*(November 28, 2006), p. 16; Joe Leahy, “Indian Regulation Hampers Retail Growth,”*Financial Times*(October 26, 2006), p. 21; Anita Jain, “The ‘Crown Jewel’ Sector That’s Ripe for ­Modernization,”*Financial Times Special Report—India and Globalization*(January  26,  2006), p. 16; Ann Zimmerman and Emily Nelson, “With Profits Elusive, Wal-Mart to Exit Germany,”*The Wall Street Journal*(July 29/30, 2006), pp. A1, A6.*

# MyLab Marketing

Go to the Assignments section of your MyLab to complete these writing exercises.

1. 12-15. What is *cherry picking*? Which approaches can be used to deal with this problem?
2. 12-16. Briefly discuss the global issues associated with physical distribution and ­transportation logistics. Cite one example of a company that is making efficiency improvements in its channel or physical distribution arrangements.