An Essay on Distributive Organization in the 20th Century (4) (Social Science)

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An Essay on Distributive Organization in the 20th Century (4)

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PART II: General Strategies of Distributive Organizations

CHAPTER 4: Organizational Approaches

1. Horizontal and Vertical Organization

(1) Horizontal Organization

There are two major types of organization, generally known as vertical and horizontal organization. In this text, vertical organization will be used as a virtual synonym for the organization of a distribution channel. This essay is, of course, mainly concerned with strategies for vertical organization. However, for the following two reasons, I would like to touch briefly upon horizontal organization we can lay a basis for the clearer understanding of the vertical organization of distribution channels. Secondly, it is indisputable that horizontal organization has frequently been utilized as an important strategic element by distributors.

By way of definition, horizontal organization involves the coherence of firms engaged in the same distributive activity (i. e., wholesaling, retailing, etc.). Such firms thus occupy the same distributive level. In some cases, this coherence accompanies vertical organization. For the present discussion, however, such cases will simply be considered as the examples of vertical organization.

Horizontal organization among the manufacturers or producers of different products may be accomplished through a means of coherence, such as capital, cooperation, or membership. The example of the first approach would be a manufacturer with divisions or subsidiaries producing different product groups. Cooperation, on the other hand, might carry out joint research and production projects for independent manufacturers. Finally, membership might carry out general cooperative projects centering around informational exchanges among member manufacturers.

Wholesale and retail firms utilized the same basic approaches in forming horizontal organization. Thus, for wholesale firms, a wholesale chain, a mart, or simply the membership system of similar firms might be the result.

However, when retailers utilize capital as a coherent means, the result is invariably a store chain, which involves vertical organization as well. This fact reflects the intrinsic advantage enjoyed by retailers which we mentioned previously. Quite frequently when retailers organize horizontally, as in the forms of a buying group, vertical organization also takes palace. However, the shopping center does represent the purely horizontal organization of retailers. In addition, a franchise chain that does not provide cohered wholesale functions can also be considered the purely horizontal form of retail organization. Finally, retailers, of course, have their own membership systems, as do manufacturers and wholesalers. Such organization must always be distinguished from organized distribution channels, which incorporate vertical organization as well.

(2) **Vertical Organization**

As mentioned previously, vertical organization as used in this text is virtually synonymous with the systematic organization of a distribution channel. Once again, capital, cooperation, and membership constitute the major means of vertical organization, cohering manufacturing, wholesaling, retailing, and even consumption. The organization of a distribution channel by these means can, of course, be accomplished by any type of distributor.

Firms which do organize distribution channels generally do so in order to secure stable sales and inventory flow, achieved through the maximum control of the distribution channel. As mentioned above, the basic strategic options open to a manufacturer are product diversification (or specialization), organization (or unorganization) of a distribution channel, and internationalization (or domesticization). The wholesaler has recourse to the diversification (expansion) or specialization (limitation) of functions in addition to the options regarding distribution channels and geographical expansion. Similarly, the retailer has the option of expanding (diversifying) or limiting (specializing) the number of outlets in addition to the other two choices shared by producers and wholesalers as well. In this context, expansion or diversification represents the pursuit of economies of scale, while specialization or limitation seeks instead to create a closely-knit, tightly-controlled organization highly responsive to consumer needs and wants.

Any potential channel managers first judge the value of an organized channel as opposed to other strategic alternatives. Next, the most suitable means of coherence (i. e., capital, cooperation, and membership) has to be selected. This process constitutes the selection of a strategic mix. Naturally, a firm can devise and execute its growth strategies on the basis of its own capital and other resources, as well as such factors as the analysis of the competitive situation and the strategic mixes employed by competitors.

2. Coherent Means of Organization

(1) Organization through Capital Coherence

In the following discussion, the term 'organization' will denote only vertical organization. As previously mentioned, complete ownership allows the maximum control of a distribution channel. However, enormous capital outlay is required, and the managerial risk is correspondingly great. Moreover, when considered in terms of the effective utilization of capital and other resources, complete ownership cannot be judged to be the optimum means of organization.

As described in the previous chapter, complete ownership results in severely diminished organizational flexibility. Nonetheless, under certain conditions, and particularly if excessive reliance on outside capital can be avoided, the complete ownership of a distribution channel can quite definitely be a highly effective organizational strategy.

(2) Organization through Cooperation Coherence

When a distribution channel is organized on the basis of cooperation, a core firm or channel manager creates an organization that performs all or part of the marketing activities performed in common with a number of other totally independent firms that becomes the associates or members of the new structure. The concrete examples of this approach include the voluntary chain and buying group. Organization on this basis does not, of course, yield to the channel manager the same high degree of control offered by complete ownership. Consequently, organizational solidarity is also relatively weak. However, since member firms remain independent, a cooperative group does provide relatively great organizational flexibility. Moreover, even a small and medium-scale firm with relatively weak capital and other resources can organize a distribution channel utilizing cooperation.

(3) Organization through Membership Coherence

We have already seen how cash-and-carry wholesalers and resident buying offices introduce membership systems aimed at the retailer. In addition, speciality stores such as audio and camera stores have instituted membership systems aimed at the consumer.

Organization on the basis of membership is never as strong or stable as that based on capital or cooperation. Consequently, control over the channel is extremely weak. Nevertheless, compared to totally unregulated dealings between independent, unorganized firms, membership does provide some measure of control. Moreover, although membership does not allow strong control over a distribution channel, it does provide the significant means of forming selective trade relationship. Moreover, since member firms retain their autonomy to the greatest degree possible in this form of organization, they retain almost all of their own decision-making. Of course, since organizational solidarity is quite weak, member firms cannot always expect stable sales or inventory flow.

3. Channel Managers

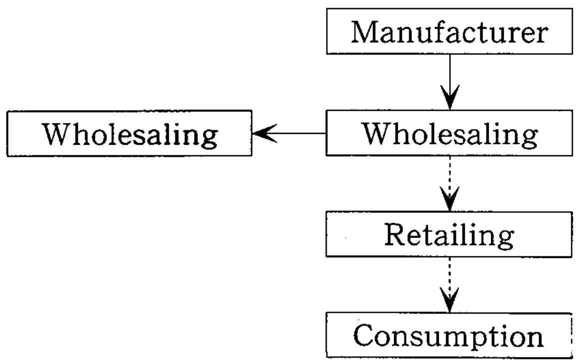
(1) Manufacturers as Channel Managers

The nature of the channel manager is of primary importance in considering organizational strategies. Below differentiated according to the type of channel manager. These patterns will take note of the coherent means (i.e., capital, cooperation, and membership) utilized as well.

Figure 1 depicts an organizational pattern with a manufacturer as a channel manager. In this as well as all following figures, the solid line indicates the existence of an organized channel formed by one of the means of coherence such as capital, cooperation or membership. The broken lines indicate unorganized transactional relationship.

When a manufacturer organized a distribution channel through capital, it usually takes the form of manufacturer's sales firms

Figure 1 Manufacturer as Channel Manager–1



(branches or offices). When cooperation is the approach used, 'manufacturer-sponsored cooperative groups' aimed at independent wholesalers result.

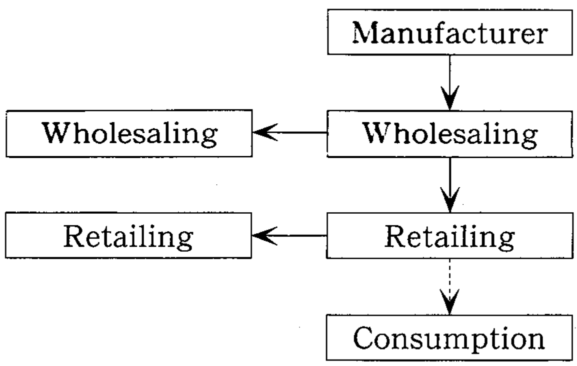
In Japan, a counterpart to the manufacturer-sponsored cooperative group exists in the vertical franchise system, the special contract dealership system. Strictly speaking, the latter is not a real membership system, but like the membership system it does allow an ordered, selective trade relationship between manufacturers and wholesalers.

Figure 2 portrays a distribution channel in which the manufacturer exercises control over or ownership of retail outlets. When ownership is utilized, these outlets would normally take the form of mail-order firms or wholly-owned retail stores. With retailing cohered under the manufacturer, wholesale functions automatically are performed within the channel formed.

Cooperation under the manufacturer's management would produce a vertical franchise chain aimed at retailers or the system of direct door-to-door sales to consumers. The typical examples of the former are visible in the sewing machine industry, and of the latter, in the cosmetic industry. Membership would be utilized as a coherent means on this pattern with extreme rarity.

Figure 3 illustrates an organizational pattern that might be typified by an agricultural cooperative. Within an agricultural cooperative, there is no complete ownership of channel members. However, individual producers and wholesalers within the agricultural coopera-

Figure 2 Manufacturer as Channel Manager–2



tive may be linked through capital. Consequently, the agricultural cooperative is a distribution channel based on cooperation coherence, not capital. Manufacturer's membership using this format is extremely rare.

The next organizational pattern (Figure 4) is rather unusual. Organization along these lines (involving the direct organization of the consumer into the distribution channel) is not possible through capital or cooperation. It illustrates, rather, a direct marketing strategy utilized by firms such as Hoover and Tupperware, wherein consumers become, in a sense, a part of membership systems. By employing 'a party plan format', sales activities are conducted by consumers to consumers additionally.

Figure 3 Manufacturer as Channel Magager-3

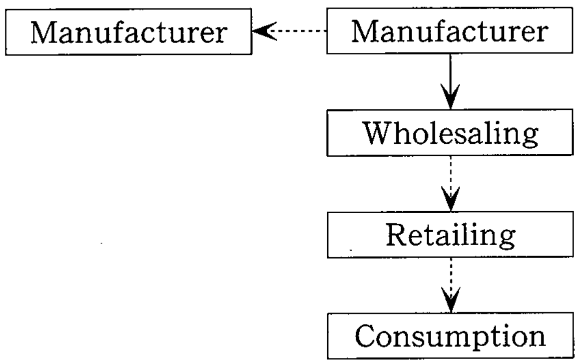
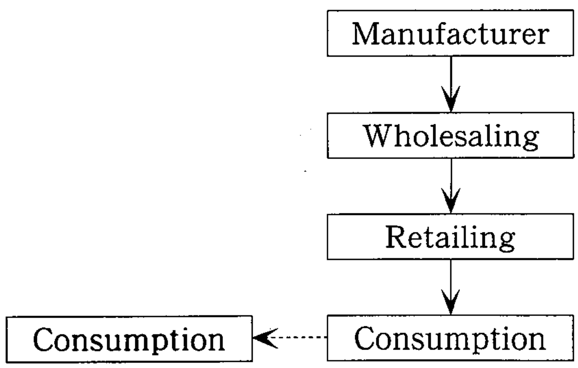


Figure 4 Manufacturer as Channel Manager-4



(2) Wholesalers as Channel Managers

Figure 5 presents one organizational pattern possible when a wholesaler takes the role of a channel manager. However, in reality this pattern appears with extreme rarity, no matter what means of coherence may be used. Theoretically, of course, it does not lie beyond the realm of possibility, but its strategic practicability is highly doubtful.

The next pattern (Figure 6) may depict organization based on capital. However, the creation of a network of retail outlets requires an enormous amount of capital as well as other resources. Consequently, the majority of wholesalers seeking to organize a retail network through capital would do so by the merger with or purchase of existing retail firms.

The utilization of cooperation to organize a retail network would

Figure 5 Wholesaler as Channel Manager–1

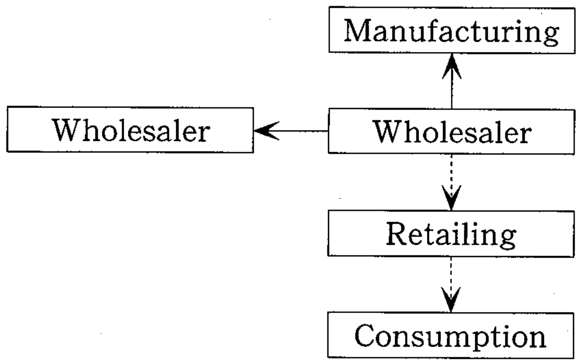


Figure 6 Wholesaler as Channel Manager–2

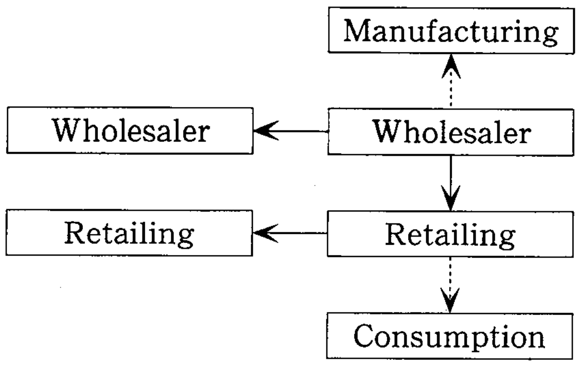
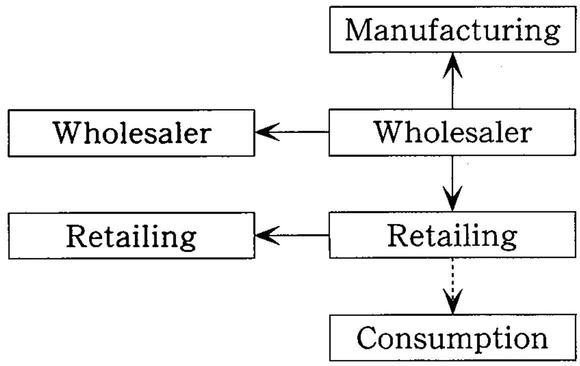


Figure 7 Wholesaler as Channel Manager–3



produce the voluntary chain. In the same way, if membership is employed, the result would be cash-and-carry wholesalers or resident buying offices.

Figure 7 obviously presents the extension of wholesaler control over production facilities. This organizational pattern is seen frequently when using capital in the food industry of the United Kingdom and the United States. However, as in the preceding organizational pattern, capital coherence overwhelmingly takes the form of the purchase of or merger with existing retail firms. When cooperation is employed in this format, the result is a voluntary chain into which manufacturing facilities have been directly cohered.

(3) Retailers as Channel Managers

When based on complete ownership, Figure 8 pattern represents chain stores. This pattern is never used with cooperation or membership as a means of coherence.

The organizational pattern in Figure 9 can clearly be seen as the extension of that in Figure 8. Consequently, assuming capital as a means of coherence, the pattern represents a store chain with the direct control or ownership of its own manufacturing or production facilities. This is a quite common phenomenon among large-scale retail chains in the United States. However, due to the inherent organizational inflexibility of this pattern, there has been a tendency in recent years for such chains to divest themselves of these facilities. As was also the case in Figure 8, the pattern shown in Figure 9 does not occur with cooperation or membership as a means of coherence.

Figure 10 depicts the organizational pattern represented by the buying group. The buying group, of course, is formed through coop-

Figure 8 Retailer as Channel Manager–1

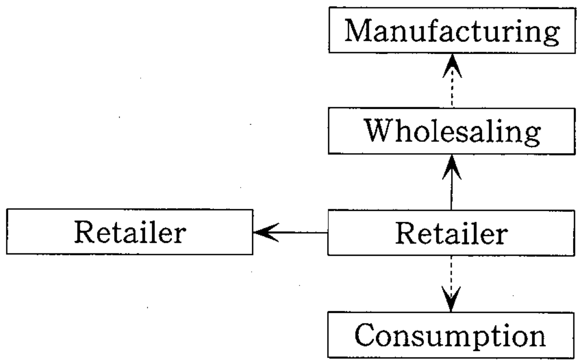


Figure 9 Retailer as Channel Manaegr–2

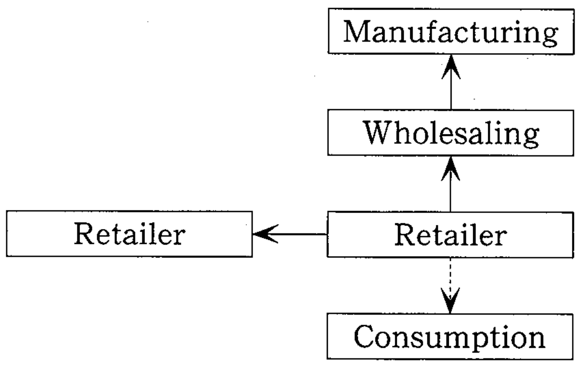


Figure 10 Retailer as Channel Manager–3

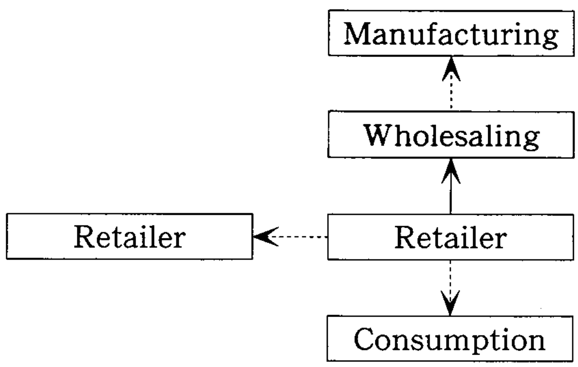


Figure 11 Retailer as Channel Manager–4

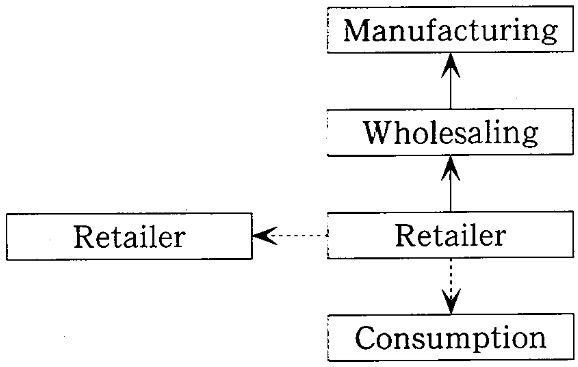
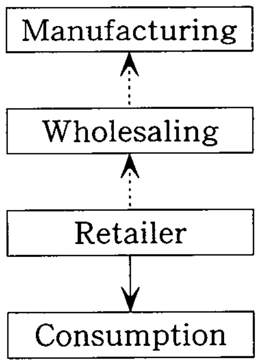


Figure 12 Retailer as Channel Manager–5



eration. Membership is not utilized by retailers organizing distribution channels on this pattern.

The pattern in Figure 11 represents a buying group with the control of production or manufacturing facilities. Like the pattern in Figure 9, this configuration involves the serious loss of organizational flexibility. Again, membership is not used as a coherent means in this pattern.

The next pattern (Figure 12) obviously depicts the form of organization in which the retailer enjoys considerable formal control over consumption. Such control is achieved, of course, only through membership, directly organizing the consumer.

(4) Consumers as Channel Managers

To speak of the consumer as a channel manager is, in effect, to speak of the consumer cooperative. Although 'a cooperative', the consumer cooperative is formed through capital with investment by all consumer members.

Figure 13 illustrates the way in which the consumer cooperative, like the store chain, may completely control or wholly own wholesale facilities as well as multiple retail outlets. In this respect, the consumer cooperative and store chain share a highly similar organizational character. However, the consumer cooperative has a long historical background which usually gives its management a conservative bent.

Once again, we can see that Figure 14 represents the extension of organizational control as depicted in Figure 13. This pattern is quite prevalent among highly-developed consumer cooperatives in such countries as the United Kingdom, Switzerland, and Sweden, where

Figure 13 Consumer as Channel Manager–1

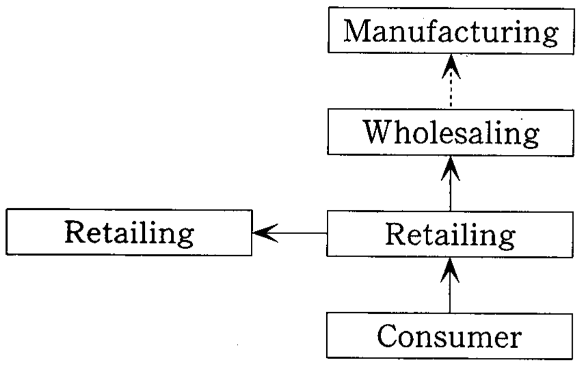
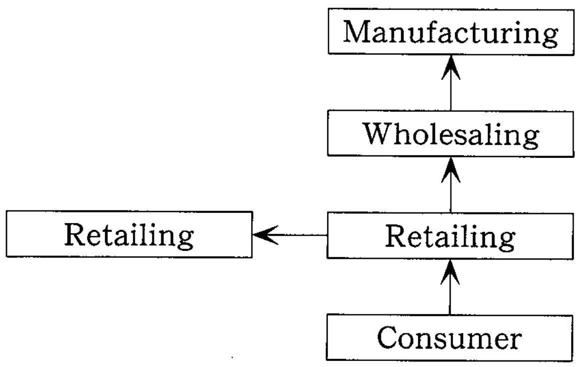


Figure 14 Consumer as Channel Manager–2



consumer cooperatives control or own production facilities for certain specific products. The reason for this lies in the fact that most consumer cooperatives strive to provide goods at the lowest possible price through direct buying from the production point.