QUESTIONS

1. **Distinguish between direct and indirect selling channels. What are the advantages and disadvantages of these channels?**

   Indirect selling is employed when a manufacturer in the United States, for example, markets its product through another U.S. firm that acts as the manufacturer's sales intermediary. There are several advantages to be gained by employing an indirect domestic channel. The channel is simple and inexpensive. The manufacturer incurs no start-up cost for the channel and is relieved of the responsibility of physically moving the goods overseas. Since the intermediary very likely represents several clients who can help share distribution costs, the costs for moving the goods are further reduced.

   An indirect channel also has limitations. The manufacturer has to give up control over the marketing of its product to another firm. The channel may not be permanent because the intermediary can easily discontinue handling a manufacturer's product if there is no profit.

   Direct selling is employed when a manufacturer develops an overseas channel so that it deals directly with a foreign party without going through an intermediary in the home country. One advantage gained in using the direct selling channel is active market exploitation. Another advantage is greater control. The channel also improves communication and consistency.

   Direct selling, however, is a difficult channel to manage if the manufacturer is unfamiliar with the foreign market. It is time consuming and expensive.

2. **Explain these types of direct-channel intermediaries: foreign distributor and state-controlled trading company.**

   A foreign distributor is a foreign firm that has exclusive rights to carry out distribution for a manufacturer in a foreign country or specific area. The distributor purchases merchandise from the manufacturer at a discount and then resells or distributes the merchandise to retailers and sometimes final consumers.

   A state-controlled trading company is a company that has a complete monopoly in the buying and selling of goods. Being government sanctioned and controlled for trading in certain goods, buyers of state-controlled trading companies are very definitely influenced by their governments' trade policies and politics.

3. **Explain these types of indirect-channel agents: EMC, cooperative exporter, and purchasing agent.**

   An export management company (EMC) manages, under contract, the entire export program of a manufacturer. It functions as an export department for several allied but non-competing manufacturers.
A cooperative exporter is a manufacturer with its own export organization that is retained by other manufacturers to sell in some or all foreign markets.

A purchasing agent represents the foreign buyer. This agent resides and conducts business in the exporter's country and seeks a product that matches the foreign principal's preferences and requirements.

4. **Explain these types of indirect-channel merchants: export merchant, export drop shipper, export distributor, and trading company.**

An export merchant seeks out needs in foreign markets and makes purchases from manufacturers in its own country to fill those needs. After having the merchandise packed and marked to specifications, the export merchant resells the goods in its own name.

An export drop shipper is a special kind of export merchant. It requests a manufacturer to "drop ship" a product directly to the overseas customer.

An export distributor deals with the manufacturer on a continuous basis and is authorized and granted an exclusive right to represent the manufacturer and to sell in some or all foreign markets. It pays for goods in its domestic transaction with the manufacturer and handles all financial risks in the foreign sale.

A trading company trades on its own account. It performs many functions. It may buy and sell as a merchant. It may handle goods on consignment, or it may act as a commission house for some buyers.

5. **Explain hot, moderate, and cold countries as classified by the country temperature gradient. What are the channel implications of this classification system?**

The classification is based on these environmental characteristics: (1) political stability, (2) market opportunity, (3) economic development and performance, (4) cultural unity, (5) legal barriers/restrictions, (6) physiographic barriers, and (7) geocultural distance. A hot country is one that scores high on the first four characteristics and low on the last three. A cold country is exactly the opposite, and a moderate one is medium on all seven characteristics.

The channel implications of this classification are that marketers must be alert to any new channel development in hot countries. Unlike cold countries, hot countries force marketers to change with the environment. For a hot country, environmental forces may be so hot that new institutional structures arise. Both the manufacturer and middlemen will need to adjust in order to survive.

6. **What are the factors that affect the length, width, and number of marketing channels?**

Factors that must be taken into account include legal regulations, product image, product characteristics, intermediary's loyalty and conflict, and local customs. A country may have
specific laws that rule out the use of particular channels or middlemen. A product with a low-price image requires intensive distribution. So do low-priced, high-turnover, convenience products. As the channel widens and as the number of channels increases, price competition increases and dealers' loyalty is reduced. Finally, local customs may force a manufacturer to employ a channel of distribution that is longer and wider than desired.

7. Why is it difficult--financially and legally--to terminate the relationship with overseas middlemen? What should be done to prevent or minimize such difficulties?

Based on the assumption that an agent or distributor has invested considerable effort and money to develop the local market for the principal, many countries have enacted agency termination laws to protect the interests of agents and distributors. Such laws have a tendency to penalize unilaterally foreign principals that have terminated the agency relationships. These laws often forbid a manufacturer from terminating its relationship with even incompetent channel members without a lengthy notice in advance or without an expensive settlement.

To minimize risk and problems, the principal should carefully structure the representation agreement, making sure that certain contract terms are included in writing. The agreement must identify the parties and state their business, residences, and a time period during which the agreement will be operative. The agreement should set forth the benefits to and the rights and obligations of both parties. The jurisdiction to handle any legal disputes and the arbitration body or forum should be included. Finally, foreign laws must be considered to avoid including invalid clauses.

8. What are gray market products? Are they legal?

Gray market products are those imported by an unauthorized party. Gray marketing may be illegal in the case that the protection is granted to an independent American trademark owner. In general, however, it is legal to import and sell gray market goods.

DISCUSSION ASSIGNMENTS AND MINICASES

1. Do you think that the U.S. ETCs can compete effectively with Japanese trading companies?

U.S. ETCs should be able to compete with Japanese trading companies. At least, they will be more competitive. The new competitiveness is due to the fact that they are able to overcome financing and antitrust problems previously encountered by other similar entities. EMCs and Webb Pomerene associations have not grown satisfactorily because of lack of financing and antitrust restrictions. The ETC Act allows banks to hold equity positions in ETCs. The benefits of the participation of banks in export trading include financial resources, branch networks, and market information.
ETCs are able to obtain binding antitrust preclearance for specified export activities. The prior antitrust immunity creates a favorable environment for the formation of joint export ventures. Such ventures, through large-scale operations and economies of scale, can reduce cost and risk while promoting efficiencies.

One legal requirement that may harm ETCs’ overall performance is that American ETCs must focus primarily on exports. Import activities are secondary and undertaken only when they are needed to promote exports. As a result, ETCs may lack an efficient infrastructure for developing two-way trade and are not as well-rounded and international as their Japanese counterparts.

2. How should Japan be classified: hot, moderate, or cold? Do you think this classification may change in the future?

Japan should be classified as a moderate country. Although Japan scores high on political stability, market opportunity, economic development, and cultural unity, it is not exactly a hot country. With regard to other characteristics, Japan looks more like a cold country because it scores high on legal barriers, physiographic barriers, and geocultural distance.

It is possible that, with all the changes going in Japan, the pressure from its trading partners to remove legal barriers may be great enough to make Japan move in the direction of "hot" category, albeit slowly.

3. Should the distribution channels of Volkswagen and Porsche be the same?

The foreign automobile segment is a good example of the relationship between product image and channel width. The distribution channels of Volkswagen and Porsche should not be the same due to their different target markets. Whereas Volkswagen, as an economy and mass car producer, requires an intensive channel, Porsche, with its high price tag in excess of $20,000, does not need that kind of distribution. Subsequently, when Porsche decided to enhance its image by severing its U.S. ties with Volkswagen which handled Porsche distribution, it then tried to lure 130 of Audi’s 320 dealerships as exclusive dealers. As a matter of fact, studies have shown that Porsche can cover 80 percent of the U.S. market with as few as 50-80 dealerships. This is a legitimate assumption since consumers are willing to go through considerable effort to seek out prestigious products even when they are not readily available.

4. Honda created a separate dealer network for its Acura brand. Is there a need for this expensive strategy?

Honda, in its attempt to trade up with its Acura brand, needed a distinct image to build snob appeal for Acura. Toward this goal, it created a new division with a separate dealer network to handle the more expensive automobile. Honda's strategy thus prevents Honda dealers from mingling the two brands.

The strategy is also appropriate because the company wants Honda dealers to be small-car specialists, unlike GM's dealers which must carry parts for and offer services to many kinds
of cars, large and small. The strategy circumvents state laws as well since some states require showrooms of the same brand to be at least ten miles apart. The success of Acura seems to confirm that Honda's strategy is a correct one.

5. Sony Corp. of America, in an effort to include retailing in its operations, runs its own licensed stores in Japan and Europe. In the United States, Sony has opened Sony Gallery of Consumer Electronics in Chicago. Inside the store, "boom boxes" and camcorders are displayed on pedestals as if they were art objects, and the Walkman is displayed on trendy mannequins. The gallery includes a life-size mock-up of an apartment with a built-in Sony home theater system. Some retailers are concerned that Sony might turn out to be both their supplier and competitor. How should Sony deal with this concern?

Sony's effort is a good illustration of the benefits and problems derived from having multiple or parallel channels. On the one hand, it employs middlemen in its regular, long channel. On the other hand, it has begun to add the second and direct channel (see "Sony's 'Gallery' Has Retailers Hearing Footsteps," *Business Week*, 23 December 1991, 29).

From manufacturers' standpoint, it is only natural that they all want to utilize all channels that can contribute to corporate sales and image. In the case of Sony, such a goal becomes even more critical because the consumer-electronics business is maturing.

Sony claims that the purpose of the Chicago Gallery is to further strengthen its positive image by offering in-depth product information, demonstrations, and services. The Gallery showcases Sony's full product line, including new Sony technologies that many retailers have yet to carry (e.g., Data Discman--books on compact discs). Because retailers, as a rule, emphasize price rather than product features, Sony wants to make the demand for its products less price elastic. According to the president of Sony Consumer Products Group, Sony must explain why its products deserve to be "higher-value purchases." The Gallery allows the firm to explain its premium technology for image building. In other words, the new channel is more of a promotional tool than a distribution tool.

From the perspective of Sony's retailers, it is hardly surprising that they have a cause for concern: their own supplier may take sales away from them and may create price war which hurts profit margin. To allay such fears, Sony has stated that the goal of the Gallery is not to make money but rather to make consumers comfortable with Sony's products, making them want to buy Sony's products regardless of the retail outlets. If this goal is accomplished, it will benefit both Sony and its retailers. To assure retailers that Sony is not a competitor, Sony's Gallery sells products at full retail price and even steers shoppers toward local Sony dealers who usually have lower prices. This strategy, if executed properly, should allow Sony to bolster its positive image, keep its premium price, minimize dealer conflict, and maintain dealer loyalty.

6. Do gray marketers serve useful marketing functions--for consumers and manufacturers?
In spite of all the criticisms, gray marketers do serve useful marketing functions. For manufacturers, gray marketers help distributing surplus goods and perform some of the service functions. As a matter of fact, many manufacturers tolerate or even encourage the practice of gray marketing.

For consumers, gray marketers provide an alternative-- essentially the same product for a lower price. They promote the free enterprise system.

This assignment can be tied to the discussion of price equalization in Chapter 3. The discrepancy of prices in two countries for the same product causes gray marketing to exist which in turn narrows the price differential. Gray marketers thus bring about more uniform prices.

7. U.S. Customs regulations require watches to have a small inked stamp on the movement. Seiko thus charged that the gray market Seiko watches imported into the United States were unfit because the opening for marking harmed dust- and water-resistant seals and contaminated the watch movement.

a) Do you feel that gray marketers' marking to comply with customs regulations is harmful to the product?

Theoretically, gray marketers' marking may be potentially harmful to seals and the watch movement. Realistically, there is no reason why gray marketers cannot utilize proper care and control in opening the watches. The criticism is also not persuasive given the fact that such watches, when repaired by Seiko or its authorized dealers, must be opened as well. If the procedure were indeed harmful, no watch can be repaired, and Seiko should make its watches tamperproof.

b) Because Seiko is a popular brand and gray market Seiko watches are carried by a number of discounters and catalog showrooms, what should Seiko do to alleviate the problem of unauthorized imports?

One thing that Seiko can do is to reverse its policy of not selling watches to discounters. In return, Seiko can ask discounters to stop carrying gray-market watches. Another strategy is to simply reduce production so as to force up prices which gray marketers must pay.