FUNDAMENTALS OF MARKETING:
MANAGING MARKETS, PRODUCTS, CHANNELS AND PROGRAMS

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Introduction

Remember that best selling book "All I really need to know I learned in kindergarten" by Robert Fulgham?[1] In it he suggests that it is the little things in life - like playing fair, sharing, and cleaning up your own mess - that truly define who you are, your happiness, and your success. For many organizations, the principles we learn in introductory marketing classes play that same role. It is the basic concepts of who is my customer, what do they want and need, and how can I make them happy that should drive the organization.

Marketing is among the most misunderstood of business activities. Often, the term marketing is used synonymously with sales. It is true that "sales" is one of the functions that occur within the overall marketing system; yet sales is simply one small component of a much broader marketing role that properly includes functions ranging from product conception and design to packaging, pricing, and service following the sale.

Given the broad role of marketing it is perhaps not surprising that for some products, marketing accounts for a majority of the product cost. To illustrate consider the twenty-cent product in the two-dollar package (e.g. a package with one bolt for two dollars versus a box of 50 bolts for ten dollars). Rationally, we might suggest that it is crazy to spend two-plus dollars for a twenty-cent part. Yet, the customer may well be achieving benefits from this approach beyond the specific needs addressed by the part (e.g. they don't have to buy 49 bolts they don't need – so from their point of view they save eight dollars!). It is the job of marketing to identify and assess such wants and needs, and to ensure that the organization's product offerings satisfy them.

Good marketing is the process by which organizations better understand the inner nature of those they wish to serve. Does the person looking for a pet cat have a problem with mice – or loneliness? Are they buying coffee for the flavor, the warmth, or the experience at the coffee shop? Is the person buying a boat seeking a means of transportation across water, or seeking a state-of-the art fishing craft, or are they buying quality time with their family? Not that many years ago one boat did it all. Today, astute marketers have identified the many independent customer needs and desires in boating and, as a result, there is a boat tailored for almost every use.

This report looks at some of the core activities that fall within the marketing realm and are at the heart of all businesses. We aim to just hit the highlights of those areas that everyone should be familiar with. You might say that we are covering the "everything you really need to know about marketing" lessons of kindergarten.

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[1] Fulgham, Robert. 2003. All I Really Need to Know I Learned in Kindergarten, Ballantine Books, Random House Publishing, Inc. NY.

Discussion

Marketing can be defined as "those human activities directed at satisfying wants and needs through voluntary exchange processes."[2] In this case "needs" are those basic "lacks" or missings that humans are trying to address and "wants" are specific, e.g. branded, versions of those needs. The goal of the marketing process is the creation of what economists call economic utilities, and the marketing process primarily focuses on the creation of time, place, and ownership utility. It is common to hear managers talk about getting their products to the right place at the right time and at the right price. Utilities are basically forms of satisfaction you can put an economic value on.

In the broadest terms, marketing activities within an organization can be divided into four components, based on the major decision that must be made. These four components are:

- Markets,
- Products,
- Channels, and
- Marketing Mix or "Programs"

Markets – Whom do I sell to?

Markets are simply groups of people - people with needs to satisfy, money to spend, and both the ability and willingness to spend. All four aspects are essential to the creation of a satisfactory transaction.

In general, people and organizations are always in some state of need, so the goal of marketing is to stimulate their willingness to act on that need. Their access to money is dependent on past income (wealth), current income (and cash flow), and future income (e.g. credit). The ability to buy is impacted by both physical access (including Internet and phone) and legal issues. Willingness to buy involves a much more complex set of issues that will be discussed later.

Successful companies are careful to break their market into relatively homogenous groups in order to design the company's marketing mix to most effectively meet each group's need. These homogenous groups are called market *segments*, and the process is called *segmentation*. A "good" market segment is based on a number of characteristics that are common to those within a given segment; those within a defined segment should be:

- Accessible (both for communication and supply),
- Sufficiently significant in terms of current or potential purchasing requirements to meet the volume and financial needs of your organization (including profit potential),
- Clearly definable in terms of "uniqueness," and
- Likely to respond similarly to your marketing stimuli.

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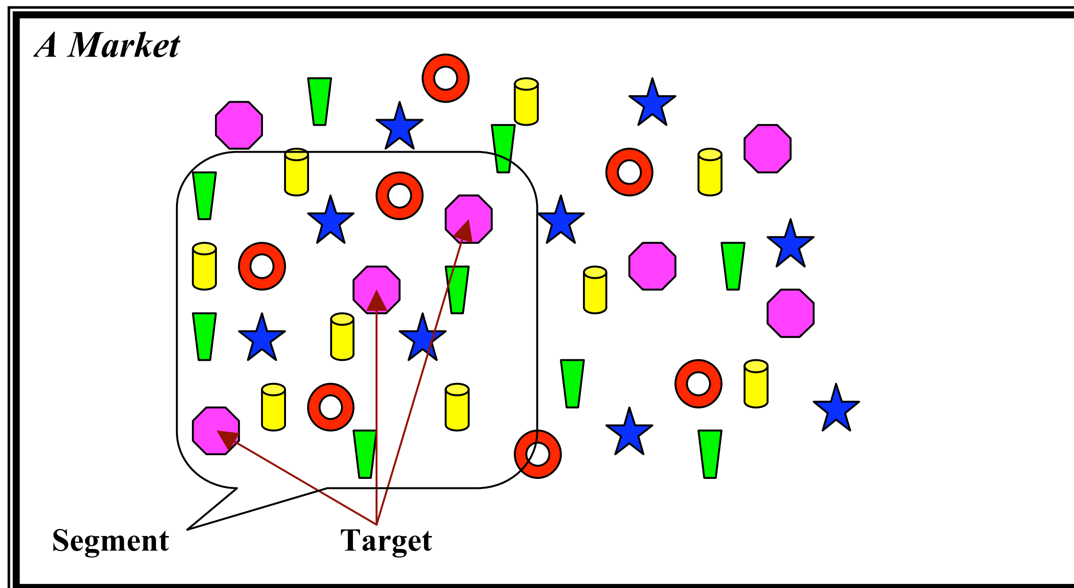
[2] Naor, Jacob. 1992. Introduction to Marketing Seminar. University of Maine Lecture Series. Orono, Maine.

There are two subjective and two objective approaches to segmentation. The two most common objective approaches are segmenting by geographic location and demographic characteristics. The segmentation of the market based on lifestyle characteristics (sometimes referred to as psychographic segmentation) and behavior are more subjective approaches. Naturally, in large enough markets these approaches may be layered, such that you might focus on a segment that includes, for example, companies within 500 miles of your factory (geographic), that have male purchasing agents over the age of 35 (demographic) who like to fish (psychographic), and that tend to buy their products monthly in bulk (behavior). This might be a very good segment for your firm – if enough customers exist that meet these criteria and your financial goals.

The process of focusing in on a very specific market segment, so that you can aim your marketing mix directly at that segment, is called *targeting*. Having a major golf tournament for your selected segment does you little good if no one with influence or purchasing power plays golf. Having a fishing tournament if all your targets love to fish might bring in a whopper of an order. And yes, even a company like Coca Cola is very careful about its target marketing. Sure, they believe everyone should drink Coke, but did you know they also make many different flavors of coke to meet the different tastes of different regions of the world?



By carefully selecting a target market a firm can create the mental image they want in that customer's eye. This process is called *positioning*, and the purpose is to create a favorable comparison between what your firm has to offer and the products of the competition. For example, nonprofits trying to attract donations from many individuals might emphasize their large size to create the image of power and influence, such that potential donors feel their money is going to have real impact on an issue. The key is that your targeting and positioning strategies go hand in hand. You select targets that match the image you are trying to portray and you emphasize in your marketing mix only those characteristics that fit the characteristics on which you made your target selection.

Products – What am I selling?

Customers pay for products as "bundles of benefits." The benefits perceived by the customer can be economic, social, or psychological. Services also fit in this description of products. Products have both tangible and intangible attributes. The difference between an attribute and a benefit is: an *attribute* is a characteristic of your product offering, while a *benefit* is the perceived value of that attribute to the customer. For example, an attribute of a certain car may be that it goes from 0-60 in 4.5 seconds. However, this may or may not be a benefit to a particular customer. To successfully design and sell products, it is important to recognize the difference between attributes and benefits! Ideally, those involved in product conception and design should know the perception of benefit by potential customers long before a new product is brought to the marketplace.

People value individual attributes differently. It is important to understand not only exactly what people are interested in, but also either how much they are interested or how important that attribute is to them. In a study a number of years ago of attributes offered by a hotel chain, one of the new "benefits" management felt they were providing and putting in every advertisement was the fact they offered fax service for the first time. The study did what was called an importance-performance analysis of a number of attributes about the hotel. In this type of study the researcher asks two questions about each attribute the hotel offers; basically, how well does the hotel provide this service, and how much do you care. What they found was that customers reported the hotel did a great job of providing a fax service, but nobody really cared. What they really did care about was a hot shower, a comfortable bed, and a clean room – and the hotel only did a mediocre job of providing those things. (Interestingly, one of the comments was, "instead of posting notices about the new fax machine, post the number of who to call when the hot water runs out!" Not a bad idea!)

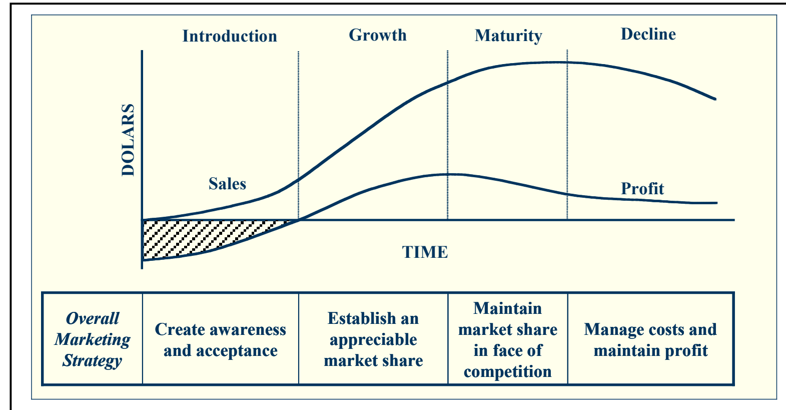
Marketers also talk about *product extensions*, such as Kodak's extension from film into cameras, or Nike's extension from shoes into other sportswear. Often most or even all the profits are in the product extensions, rather than in the generic product itself.

Augmentation is the process of allowing the customer to modify or add to a product in some way, such as the ability to customize athletic footwear to include team name and player number. Heated seats, sunroofs, and stereos are examples of how cars can be augmented.

Product Life Cycle (PLC)

As briefly introduced in last month's report, all individual products go through a life cycle that has predictable characteristics in a free-market system. Generally this cycle is broken into four phases: introduction, growth, maturity and decline. New products tend to lose money at first (in the *Introduction* phase) due to both the costs of development and the weight of fixed costs to sales revenues. In fact, most new products fail. The *Growth* phase is characterized by both rising sales and rising profits, although profits tend to peak during this phase as the competition heats up. In the *Maturity* phase sales volume begins to level off. It becomes more and more important to increase the number of users,

increase the frequency of use, and/or increase the variety of uses. Finally, in the *Decline* phase sales decrease at a greater rate than expenses, and profits can even go back to a loss. These cycles are not about your company's product specifically, but generally represent either the general category your product is in (e.g. bicycles), or the form of the product (e.g. racing bikes).



Product Classifications

It is useful to break products into different classifications based on the typical behavior of those that purchase them. There are two primary product classifications, consumer and industrial. *Consumer goods* are those that are "used up" by the purchaser, whereas *industrial goods* are those utilized to produce other products. Consumer goods are often further categorized into convenience, shopping, or specialty items.

Convenience items are regularly purchased items for which minimal purchasing effort can be expected and that brand awareness exists but that particular brand may not be an imperative. A good example of a convenience item is bread. In general, when people go to the grocery store they have a brand of bread in mind that they usually buy. However, rarely do they bother to go to another store just because that particular brand is unavailable; instead they simply grab the next best option.

Shopping goods involve a higher level of purchasing effort and product comparison activities, but there is less brand awareness and attachment than for specialty or convenience items. Lumber is an example of a material that people shop for (e.g. they call around to get the cheapest price) but for which they have little brand awareness.

Specialty goods are those goods where shopping effort is maximized and brands are of high importance. Many luxury goods such as Rolex watches are specialty goods. But so are products like books. People put a lot of effort into obtaining the J.K. Rowling (brand) of novel, and are not swayed by substitutes.

The challenge is that the categories vary by individual and by product! For example, to some people blue jeans are a shopping item ("just get me the cheapest") and to others they are a specialty item ("I want Levi's"). There are also additional categories such as emergency goods (e.g. tow truck) and unsought goods such as those sold by door-to-door salespersons.

New Product Development Process

One of the most challenging components of marketing for many organizations is the process of developing a new product. Over the years, numerous research studies have shown that a formal, structured new product development process can have a significant impact on the potential success of that product. The flipside of the coin is equally true. That is, a full and thorough implementation of the process is equally critical.

There are a number of formal approaches to new product development, but most revolve around a core set of activities that include the following:

- An idea generation phase, where lots of ideas from lots of places are critical,
- An initial idea screening process that weeds out ideas that don't fit company capabilities or customers,
- The analysis of the business potential of the top few ideas, including forecasts of sales, profits, and the investment required,
- The actual product development phase, including:
  - Concept development
  - Creation of detailed specifications
  - Prototyping
  - Testing, and
  - Creation of marketing plan
- Test marketing of the new product under real conditions (test the product and the marketing plan), and
- Commercialization (introductory stage of PLC).

By following a formal *New Product Development* process fully, a company increases its control and ability to react quickly to feedback from the marketplace (e.g. we should have made it bigger, or smaller, or … blue!).

Product Adoption Process

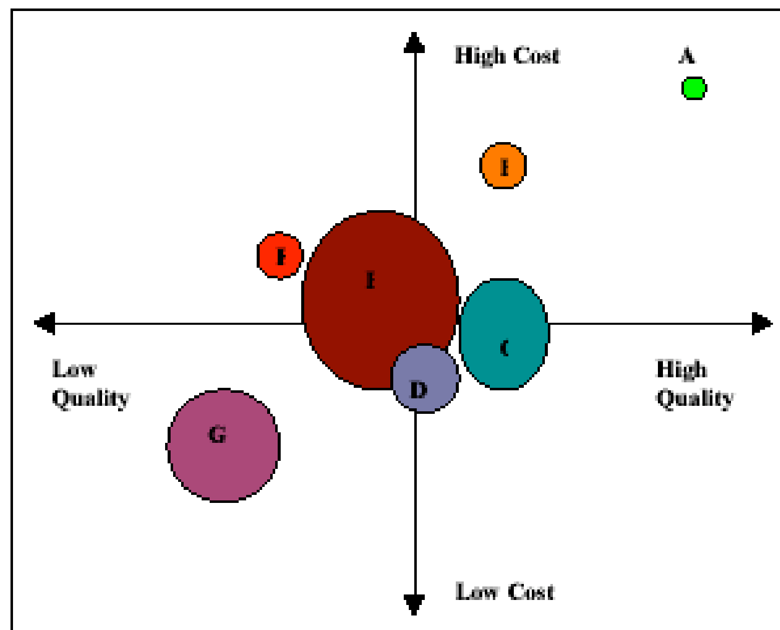
There are some consistent characteristics of how people learn about, and decide to purchase and use a new product. There are five phases people go through to in making a purchasing decision. These steps are:

- They become *aware* of the product, that is they have limited knowledge and some base perceptions (right or wrong) about the product,
- They become *interested* in the product to the extent that they seek more information,
- They begin to *evaluate* the product and to make comparisons to perceived alternatives,
- They *try* or test the product in some way, and
- They take actions to acquire or *purchase* the product.

Jumping right to the trial stage often shortens the term of this process. Hence product demonstrations, test drives of cars, and taste samples in the grocery stores are designed to hasten the purchasing decision.

Positioning Your Product
It is really important that companies have a realistic understanding of how their customers view their products. It is not enough that your product manager thinks your product is the highest quality. What matters is what the customers think. A fairly simple way to find this out is to do three things.

1. Find out the approximate sales volume of your competitors for a particular product or product line (if you don't know this, your customers or the library might),
2. Ask your customers to rank the quality of your product and that of your competitors from very low to very high quality, and
3. Ask your customers to rank the relative price of your product and that of your competitors, from very low price to very high price.



From this you can map the relative price and quality relationship between you and your competitors. This provides you with the customer's perceived image (or position) of your company. This process is called perceptual mapping, and thi A icular image is called the *product-positioning map*. Below is an example of the results from this process. The size of the circle reflects the percent of the total market this competitor represents (their *market share*).

To analyze this map, you can see company A is using a niche strategy, with very high price, but also very high quality. Company B is in danger from the competition because their price is significantly higher than company C's, but their quality is perceived to be similar. Company F is in big trouble because they have the third highest price and the second lowest perceived quality. The rest of the competitors may have positioned themselves appropriately, depending on their individual needs. Determining where your company's products fit in a product-positioning map provides a lot of valuable

information. The product-positioning map depicted above shows that there are no big companies trying to compete with a high quality product. This might represent an opportunity for a firm to attempt to do so. For example, improving product quality might allow company D to both raise prices and take greater market share. The firm just needs to figure out exactly what attributes the customer requires in order to perceive a product as high quality.

Channels – How does my product get to the consumer?

One of the most important decisions a company makes is how they reach the end consumer, and this decision becomes increasingly complex the closer a firm is to the original raw material source. The sum of all the interdependent companies involved in the creation and use of a product, from raw material to end consumer, is called the *channel*. For complex products (meaning made from many resources) the channel discussion starts at the assembly point and flows down to the consumer. For raw material intense products such as concrete, oil, iron, and wood products, it is common to consider the entire channel from extraction to consumption. In general we refer to channels like rivers: they have a flow to them. The flow is forward *down* the channel to the customer, or back *up* the channel to the resource. Companies integrate *vertically* by taking on roles further up or down the channel (e.g. a manufacturer starting a wholesale operation), or *horizontally* by expanding at the same channel level (e.g. a wholesaler opening another wholesale outlet).

From the customer's point of view the channel is irrelevant. He or she wants the right product at the right price at the right time and in the right place, and really doesn't want to worry about how it got there. This means they won't pay for channel inefficiencies, or alternately can mean that a company that considers the entire channel in their management processes has strategic advantages over competitors. Some people refer to this as *value-chain management, supply-chain management, or vendor management*. These are all examples of channel management strategies.

A channel is a complex system that is critically important to the competitiveness of a product, because considerable costs can be incurred within the system. It is not the excess inventory at the retail store that is a problem, it is the total costs incurred because of the sum of the entire excess inventory throughout the channel. It is not the waste that occurs at the manufacturer of the product that matters, but the sum of all the waste of the entire channel.

Too often organizations feel un-empowered to influence their channel members. Yet, as discussed in the March 2005 commentary on middlemen, the Internet provides the ability to access options like never before. The Internet is also shortening channels like nothing before it. For the first time almost anyone can access almost anyone else in any portion of a channel with minimal cost. By taking advantage of this strategy, organizations can identify ways that the entire channel can be the most efficient and effective, and enhance their competitive stature with other products, other materials, or other regions. This is one way to compete against foreign competition.

Marketing Mix – How do I manage my efforts?

Only now do we get to the activities that many people think of as marketing, and truly determining the marketing mix is at the heart of managing the "business" of marketing. That is, generally, marketing activities in an organization are broken up into four program areas: *pricing* activities, *promotional* activities, *product* characteristics (including packaging), and distribution issues (channel management). This latter area is often called "*place*" and the four programs are called the four-P's of marketing.

Pricing

In many ways pricing is the most complex of marketing activities, and requires the most research, which is why it is often recommended that companies seek expert help in pricing their products. Too often companies use a cost plus system (take costs and add a percentage) or competitor pricing to determine their prices. Although this may be appropriate in some cases, it ignores the counter-intuitive realities of many pricing approaches. For example, it often ignores the potential to significantly (meaning double, triple or even quadruple) prices on some specialty items while lowering your prices on the core items. This is in many ways counter-intuitive, but if you do the math – lowering your price five percent on 95 percent of your highly competitive products can be more than offset by a tripling of the five percent of your items that are specialty activities. It also ignores situations where unusual market situations may make your product worth more than you think. Companies tend to under price many of their products without expert help. Remember, even tripling your specialty prices should be an individualized not blanket change activity. How many things do you "give" away, or don't charge handling fees for? Part of increasing pricing on specialty goods is actually accounting for the real costs of providing those little extras.

> **Pricing Example**
> Before:
> Sales - $1,000,000
> Commodity $950,000
> Specialty - $50,000
> Profit - $40,000 (4%)
> After:
> Sales - $1,002,500 up 2.5%
> Commodity $902,500 down 3%
> Specialty - $100,000 up 100%
> Profit - $52,500 (5.25%)
>
> *Without accounting for a potential increase in commodity sales due to lower prices!*

One other key pricing issue is in linking your pricing approach to your overall business strategies. If you are trying to grow market share, does your pricing approach support that, or are you pricing like you are a niche? Alternately, if you are trying to establish a niche, are you pricing as if you were a commodity? Linking overall business and pricing strategies is essential to business growth.

Promotion

For many, promotion means *advertising*, and again, it is true that advertising is part of the promotional toolbox. But it is only one tool. Remember that old saying, "if all you have is a hammer, everything looks like a nail?" If you only think that your promotional options are advertising, you are ignoring the key ways most business is transacted which

includes *personal selling* and *publicity*. Publicity is a free way to get your name in front of your customers, and it doesn't have to happen by accident. Astute companies create opportunities for increased positive publicity through regular press releases, articles, invitations to the press for grand openings, new equipment purchases you name it. In addition, there is still nothing quite as effective as calling or going to see your potential customer. This is especially important to companies whose client base is currently made up of a relatively small number of customers. Trying to expand that through advertising makes little sense when you can just figure out who your ideal customer would be, find a few examples of that, and call or go see them.

This doesn't mean advertising is bad, just that it is not the best solution in all cases. Advertising is most effective when you are trying to get a simple message to large number of people (e.g we sell bird feeders, or all hemp clothing is on sale).
People adopt new products at different rates. The goal of promotion is to move a potential customer through that product adoption process (discussed above) as quickly as possible. Although this can vary for a lot of reasons, as discussed in last month's commentary, people are generally broken into five categories based on their level of risk aversion habits in adopting products new to them. These categories are:

- Innovators – represent about 2-3 percent of eventual adopters and are risk takers
- Early adopters – are very influential and represent about 11 percent of adopters
- Early majority – more deliberate in their decisionmaking, like less risk
- Late majority – tend to be skeptical, even less risk (early and late majority combined make up about 70 percent of the adopters)
- Laggers – are risk averse, even suspicious at first, and make up about 17% of adopters

For promotional reasons it is critical to know which of the above groups you are aiming at, as the message you carry will be very different for each. This is equally true if you are advertising in a national newspaper, as it is if you are visiting the client's office.

Product
As we said above, from the customer's point of view the product is the total accumulation of all the benefits received for the price paid. This includes things like:

- The product itself
- Packaging
- Credit terms
- Freight
- Delivery schedule or lead times
- Product extensions or augmentations
- Purchasing access (e.g. over the phone or over the Internet)
- Information provided (manuals, the market, the economy)
- Promotional benefits (trips, gifts, lunches)
- Service
- Reliability
- Quality

The product itself is just one little item in a laundry list of attributes and potential benefits. It is recognition of the existence of this list that facilitates an organization's ability to compete even in highly competitive markets. Think of what cutting lead times in half does to your customer's inventory. What about improving quality performance so the customer no longer needs to do incoming inspections? What about returnable packaging or recycling? There are a host of options to be explored, and most of them have little to do with what we usually think of as the product.

Place (distribution)
For some organizations the channel discussion above pretty much covers their activities in terms of identifying appropriate distribution pathways. For others, particularly those that deal directly with consumers; however, a whole additional level exists. This has to do with a higher level of detail, such as defining routes for delivery trucks, shelf space for store goods, and the location of facilities for all levels of the channel. Successful companies leave no stone unturned and no activity to chance. They watch over every step of the process until the product is in the hands of the customer, and then many even follow up after the sale to glean even more information or value from the transaction.

Conclusion

For businesses struggling to survive, sometimes Occam's Razor[3] clearly applies. That is, the simplest explanation is best, and a review of basic marketing principles is a valuable activity in assuring ourselves that we are providing our customers what they truly want. In this article we review the basics of marketing with the goal of clarifying those core activities that can drive an organization and lead to success. All these things are aimed at pleasing the customer.

Too often we fool ourselves. I am reminded of a company recently that lost a great deal of their business to foreign competition, a problem many American companies are facing. The comment of the owner was that "our customers don't understand that paying a little extra for our higher quality will benefit them in the end. They are really being short-sighted by switching to cheap low-quality imports." A number of the customers that they lost were questioned in a blind survey (meaning they didn't know that it was for the company under discussion) and the top three areas listed for changing suppliers were: service, quality, reliability; and in some cases they reported they were paying a bit more for the imported products. This is certainly not the case in every situation where business is lost, but we mustn't fool ourselves by assuming we know our customers reasons – we must ask. We must link ourselves closely to our customers to truly know their needs. Good marketing skills lead to good relationships and good business.

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[3] Occam's Razor is generally attributed to William of Ockham, fourteenth century English logician who basically stated - make no more assumptions than those necessary.

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