

chapter

2

The Channel Participants

Learning Objectives:

After reading this chapter you should:

- Be familiar with the classification of the major participants in marketing channels.
- Understand why producers and manufacturers often find it necessary to shift many of the distribution tasks to intermediaries.
- Identify the major types of wholesalers as reflected in the *Census of Wholesale Trade*.
- Be aware of major trends in wholesale structure, including patterns of size and concentration in wholesaling.
- Recognize and explain the value of distribution tasks performed by the major types of wholesalers.
- Appreciate the complexity of retail structure and be familiar with the different approaches used to classify retailers, including the classifications used by the *Census of Retail Trade*.
- Know about major trends occurring in retail structure, especially with regard to size and concentration in retailing.
- Have an overview of the distribution tasks performed by retailers.
- Be cognizant of the retailer's changing role in the marketing channel.
- Appreciate the role played by facilitating agencies in marketing channels.



FOCUS ON CHANNELS

Buy a Magazine at a Newsstand: Help a Wholesaler from Being Shredded

Newsstands that sell magazines include supermarkets, drugstores, kiosks, and other miscellaneous retailers. Sales have been declining at all these outlets from 2.1 billion magazines in 1996 to 1.7 billion in the year 2000—almost a 20 percent drop in four years. What's going on? Well, all of these newsstands obtain their magazines from wholesalers, who buy the magazines from the publishers. Trouble is, there are a lot fewer of these wholesalers than there used to be. Tough demands by the giant retail supermarkets and drug chains for bigger discounts, special deals, and more service have either driven dozens of magazine wholesalers out of business or forced them to sell out to larger wholesalers. The small wholesalers had been used to buying from the publisher at 40 percent off the cover price and selling to retailers at 20 percent off cover price. But when the big retailers demanded 30 percent off cover price plus cash signing bonuses as high as \$25,000 per store, and then required wholesalers to use their own people to stock the stands rather than the retailers' employees, the burden was too great. Only a handful of large wholesalers survived. Indeed, by

2000, four wholesalers—Anderson News, News Group, Chas. Levy Circulation, and Hudson News—accounted for well over 80 percent of magazine sales to newsstands.

This high concentration of magazine distribution in the hands of just a few giant wholesalers makes it more difficult for publishers to gain timely access to newsstands and for consumers to find the magazines they are looking for when and where they want them. One measure of this poor matching of magazine supply with demand is the extraordinarily high rate of magazines left unsold on the newsstands—65 percent at the time of writing, which is an all-time high. What happens to these unsold magazines? Most are shredded and later turned into paper bags or newsprint.

While it's encouraging to know that the shredded magazines are put to good use, the shredded wholesale marketing channels for magazine distribution have not been so fortunate.

Source: Based on Mathew Rose, "Magazine Wholesaler Pressures Publishers, Adding to Their Woes," Wall Street Journal (March 5, 2000): A1, A6.

The marketing channel was defined in the previous chapter as the external contactual organization that management operates to achieve its distribution objectives. We noted that the channel manager should use intermediaries in the channel, based on the principles of specialization and division of labor as well as contactual efficiency. If the channel manager does a good job of allocating the distribution tasks among a well-chosen group of channel participants, the resulting channel structure should achieve the firm's distribution objectives with a high level of effectiveness and efficiency.

In the present chapter we build on these concepts by discussing the various types of channel participants and the distribution tasks they perform. The information provided should help the channel manager to recognize the contributions that various intermediaries can make to marketing channels. Armed with this knowledge, the channel manager can then make better decisions about who should participate in the firm's marketing channels.

An Overview of the Channel Participants

Figure 2.1 illustrates the basic dichotomy between channel membership based on performance or nonperformance of the negotiatory functions (buying, selling, and transferring title). Participants who engage in these functions are linked together by the flows of negotiation or ownership (see Figure 1.4 in Chapter 1) and are therefore members of the contactual organization (the marketing channel).

The three basic divisions of the marketing channel depicted in Figure 2.1 are (1) producers and manufacturers, (2) intermediaries, and (3) final users. The latter two are broken down further into wholesale and retail intermediaries and consumer and industrial users, respectively. The final users, though technically members of the marketing channel because they are involved in negotiatory functions, from this point on will *not* be viewed as channel members in this text. In the context of the management perspective we are using, it is more appropriate to view final users as **target markets** that are served by the commercial subsystem of the channel. The **commercial channel**, then, by definition excludes final users. Thus, whenever the term *marketing channel* is mentioned in the remainder of the text, it is understood that we are referring to the commercial channel. Final users viewed as target markets are the subject of Chapter 8.

Since facilitating agencies do not perform negotiatory functions, they are not members of the channel. They do, however, participate in the operation of the channel by performing other functions. Six of the more common types of facilitating agencies are shown in Figure 2.1.

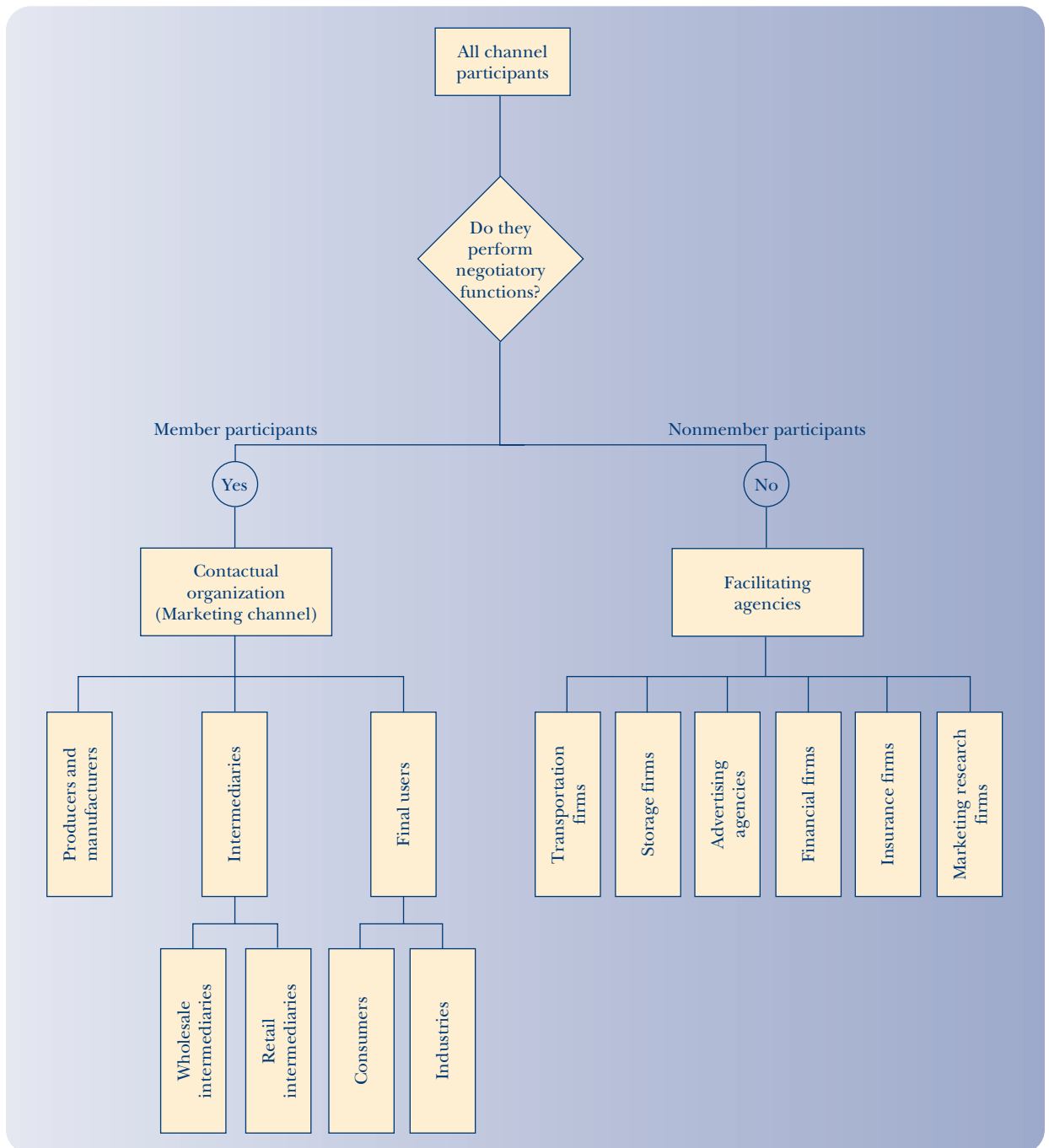
The structure of this chapter is derived from the diagram shown in Figure 2.1. We begin by discussing the commercial channel: producers/manufacturers and intermediaries. We then move to a discussion of the facilitating agencies.

Producers and Manufacturers

For the purpose of this text, producers and manufacturers consist of firms that are involved in extracting, growing, or making products. This category includes those firms that the U.S. Bureau of the Census classifies under agriculture, forestry and fishing, mining, construction, manufacturing, and some service industries.

The range of producing and manufacturing firms is enormous, both in terms of the diversity of goods and services produced and the size of the firms. It includes firms that make everything from straight pins to jet planes and that vary in size from one-person operations to giant multinational corporations with many thousands of employees and multibillion-dollar sales volumes. But even with all this diversity, a thread of commonality runs through produc-

Figure 2.1
Classification of Channel Participants



ing and manufacturing firms: All exist to offer products that satisfy the needs of customers. For the needs of those customers to be satisfied, products *must be made available to customers when, where, and how they want them*. Thus, producing and manufacturing firms must somehow see that their products are distributed to their intended markets. Most producing and manufacturing firms, both large and small, however, are not in a favorable position to distribute their products directly to their final user markets.¹ Quite often, they lack the requisite expertise and the economies of scale (and/or scope) to perform all of the distribution tasks necessary to distribute their products effectively and efficiently to their final users.

With respect to expertise, many producers and manufacturers do not have nearly the level of expertise in distribution that they have attained in production or manufacturing. An electronics manufacturer may be operating at the leading edge of electronics technology and yet know very little about the best way to distribute its sophisticated products to its markets. A drill bit manufacturer may make the finest products using the most advanced alloys and yet be quite naive when it comes to performing the tasks necessary to distribute those products. A West Coast farm that grows the finest produce based on the latest developments in agricultural technology may know very little about how to make that produce available, in good condition and at low cost, to consumers on the East Coast. In short, expertise in production or manufacturing processes does not automatically translate into expertise in distribution.

But even for those producing and manufacturing firms that do have (or are capable of developing) expertise in distribution, the economies of scale that are necessary for efficient production do not necessarily make for efficient distribution. To illustrate this point, consider a company such as Binney & Smith (B&S), the manufacturer of the famous Crayola Crayons. B&S is a relatively small manufacturer located in Easton, Pennsylvania, but it is the world's foremost manufacturer of crayons. From a manufacturing standpoint, B&S is generally recognized as a very efficient manufacturer of crayons. With sales totaling approximately 80 percent of the U.S. crayon market, the firm is able to manufacture crayons in huge quantities and has thus achieved considerable economies of scale in production. If one were to visualize the average total cost curve (ATC) for the production of crayons by B&S, it might appear as in Figure 2.2a. The figure shows that B&S, by producing at the output level of Q_1 , is incurring a cost of C_1 per box of crayons produced. This is just about at the optimum point on the average cost curve. In other words, B&S is able to achieve economies of scale in production by spreading the firm's fixed costs over a great many crayons.

When it comes to the performance of distribution tasks, however, such economies of scale may not be attainable. Suppose B&S were to attempt to distribute its crayons *directly* to the millions of consumers who use crayons. To provide adequate purchase convenience for these consumers, B&S would probably need a huge order processing facility to handle the volume of small individual orders received. Moreover, B&S would need to maintain a huge inventory to meet demand, would probably need at least several separate warehouse locations around the country, and would have to provide for transportation of the product to consumers.

The cost of setting up such an organization to perform these distribution tasks would be prohibitive. Indeed, it would be extremely unlikely that B&S could ever sell enough crayons to absorb these costs. If one were to visualize the average cost curve for the distribution of crayons directly to consumers by B&S, it might appear as in Figure 2.2b. When Figure 2.2b is compared to Figure 2.2a, we can see that at the Q_1 level of boxes of crayons distributed, the cost of distribution per box of crayons is C_2 . Note that this is not even close to the optimum point on the ATC curve and is much higher than the cost per box of crayons produced at the same level of output shown in Figure 2.2a. Thus, even though the Q_1 level was close to the optimum

1. George J. Stigler, "The Division of Labor Is Limited by the Extent of the Market," *Journal of Political Economy* (June 1951): 185-193.

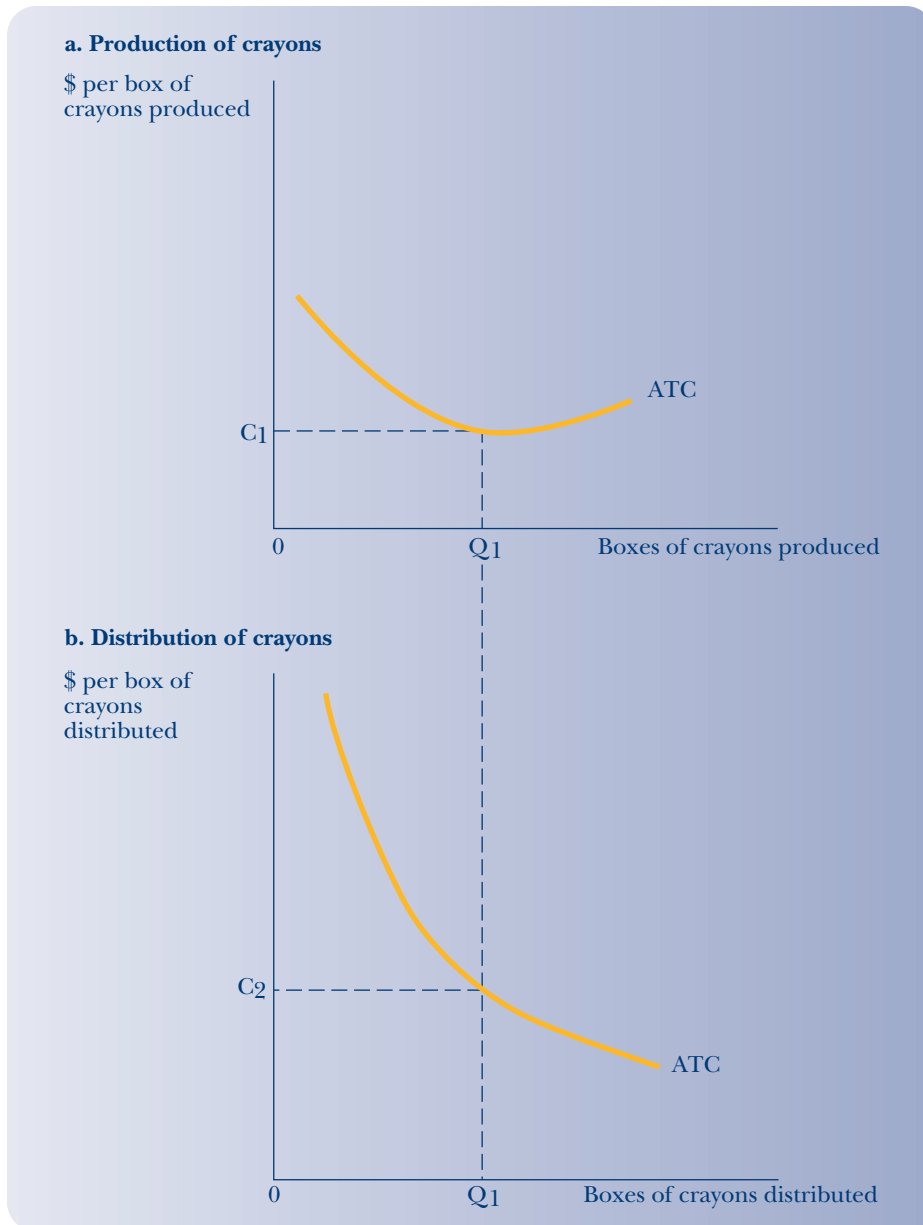


Figure 2.2
Hypothetical Average
Cost Curves for the Pro-
duction and Distribution
of Crayons

point on the average cost curve for the production of crayons (see Figure 2.2a), it does not even approach the optimum point on the average cost curve for distribution. In short, B&S would probably never be able to sell enough crayons to absorb the enormous fixed costs associated with the performance of the distribution tasks. However, by shifting the distribution tasks to other channel participants, such as wholesalers and/or retailers, B&S achieves substantial savings. The reason for this is that the intermediaries distribute the products of many other manufacturers and are therefore able to spread the high fixed costs of performing the distribution tasks over large quantities of diverse products, thus achieving economies of scope as well as economies of scale in distribution. This allows the intermediaries to operate

closer to the optimum points on their average cost curves, which are often well below the corresponding points on manufacturers' average cost curves for distribution tasks.²

This example suggests the following generalization: *Producing and manufacturing firms often face high average costs for distribution tasks when they attempt to perform them by themselves.* This applies not only to small producers and manufacturers, but to many very large ones as well. (Even General Motors, IBM, and Procter & Gamble do not attempt to distribute all of their products directly to final customers.) The scale economies that enable producers and manufacturers to operate at a low average cost for production processes are often absent in the performance of distribution tasks. Even the power of Internet-based E-commerce, which provides the technology for producers and manufacturers to be directly connected with final customers, could not overcome the underlying economic limitations so often present with direct distribution. Disintermediation, which was expected to occur rapidly across numerous industries, did not materialize as expected.³ Consequently, even in the high-tech age of E-commerce and the Internet, producing and manufacturing firms still must frequently search for channel members to whom they can shift some or all of the distribution tasks. Intermediaries at the wholesale and retail levels are the two basic types of institutions they can call upon to participate.⁴

Intermediaries

Intermediaries (or middlemen) are independent businesses that assist producers and manufacturers (and final users) in the performance of negotiatory functions and other distribution tasks. Intermediaries thus participate in the negotiation and/or ownership flows (see the section titled "Flows in Marketing Channels" in Chapter 1). They operate basically at two levels: wholesale and retail.

Wholesale Intermediaries

Wholesalers consist of businesses that are engaged in selling goods for resale or business use to retail, industrial, commercial, institutional, professional, or agricultural firms, as well as to other wholesalers. Also included are firms acting as agents or brokers in either buying goods for or selling them to such customers.⁵

Types and Kinds of Wholesalers

The most comprehensive and commonly used classification of wholesalers is that used by the *Census of Wholesale Trade*, published by the U.S. Department of Commerce every five years, which breaks them down into three major types:

1. Merchant wholesalers
2. Agents, brokers, and commission merchants
3. Manufacturers' sales branches and offices

2. Bruce Mullen, "Functional Spin-Off: A Key to Anticipating Change in Distribution Structure," *Journal of Marketing* (July 1973): 18–25.

3. Nicholas G. Carr, "Hypermediation: Commerce as Clickstream," *Harvard Business Review* (January–February 1999): 46–47.

4. For related discussion, see Arlene Weintraub, "The Year of the E-Piggyback," *Business Week e.biz* (December 3, 2001): EB24–EB46.

5. For some very interesting background on wholesaling, see Mushtaq Luqmani, Donna Goehle, Zahir A. Quraeshi, and Ugur Yavas. "Tracing the Development of Wholesaling Practice and Thought," *Journal of Marketing Channels* 1, no. 2 (1992): 75–77; see also William P. Danenburg, Russell L. Moncrief, and William E. Taylor, *Introduction to Wholesale Distribution* (Englewood Cliffs, N.J.: Prentice-Hall, 1978).

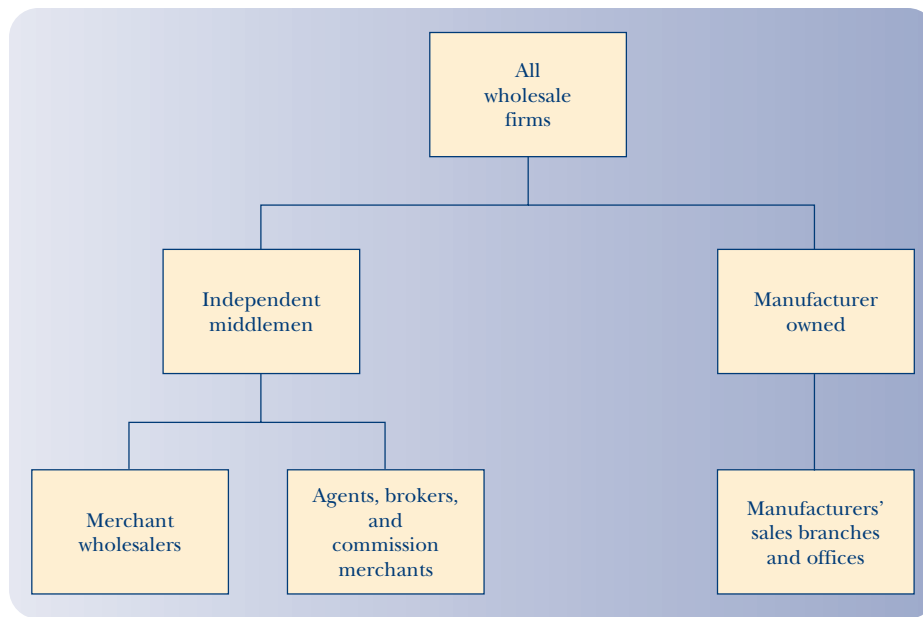


Figure 2.3
Schematic Overview of
the Three Major Types
of Wholesalers

Figure 2.3 provides a schematic diagram of these three types of wholesalers.

Merchant wholesalers are firms engaged primarily in buying, taking title to, usually storing, and physically handling products in relatively large quantities and then reselling the products in smaller quantities to retailers; to industrial, commercial, or institutional concerns; and to other wholesalers. They go under many different names, such as wholesaler, jobber, distributor, industrial distributor, supply house, assembler, importer, exporter, and others.

Agents, brokers, and commission merchants are also independent middlemen who do not, for all or most of their business, take title to the goods in which they deal, but who are actively involved in negotiatory functions of buying and selling while acting on behalf of their clients. They are usually compensated in the form of commissions on sales or purchases. Some of the more common types are known in their industries as manufacturers' agents, commission merchants, brokers, selling agents, and import and export agents.

Manufacturers' sales branches and offices are owned and operated by manufacturers but are physically separated from manufacturing plants. They are used primarily for the purpose of distributing the manufacturer's own products at wholesale. Some have warehousing facilities where inventories are maintained, while others are merely sales offices. Some of them also wholesale allied and supplementary products purchased from other manufacturers.

The *Census of Wholesale Trade* has a further classification for wholesalers, by kind of business—of which there are 18 different categories. These kind-of-business groupings are shown in Table 2.1. For data gathering and reporting purposes, the *Census of Wholesale Trade* cross-classifies these kind-of-business groupings with the three major types of wholesalers. Hence data are available for the three types of wholesalers by various kind-of-business classifications for the United States as a whole and for many smaller geographical areas.

Structure and Trends in Wholesaling

The latest comprehensive *Census of Wholesale Trade* for which data are available, taken in 1997, showed that there were about 358,000 wholesaler firms and approximately 453,000

Table 2.1
Kind-of-Business
Groupings for
Wholesalers

Source: U.S. Census Bureau, Statistical Abstract of the United States: 2001 (121st edition) Washington, DC, 2001.

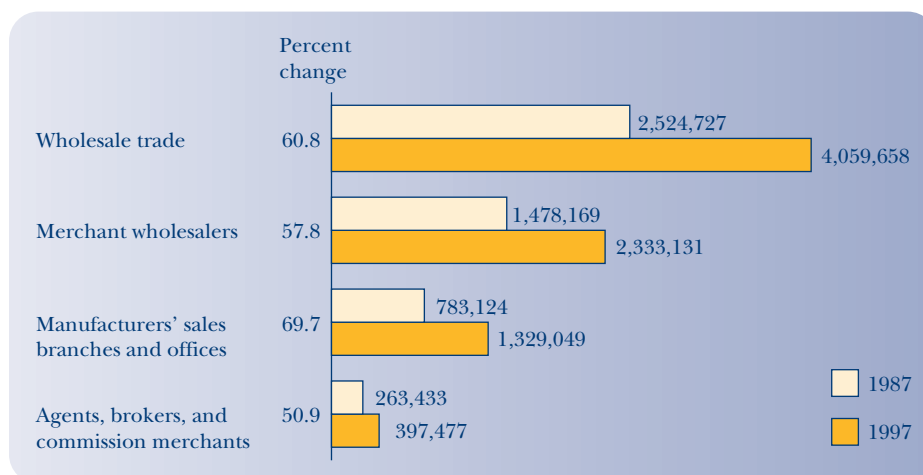
Kind-of-Business Group	NAICS Code
Durable Goods	
1. Motor vehicles and automotive parts and supplies	4211
2. Furniture and home furnishings	4212
3. Lumber and other construction materials	4213
4. Professional and commercial equipment and supplies	4214
5. Metals and minerals (except petroleum)	4215
6. Electrical goods	4216
7. Hardware, plumbing, heating equipment and supplies	4217
8. Machinery equipment and supplies	4218
9. Miscellaneous durable goods	4219
Nondurable Goods	
10. Paper and paper products	4221
11. Drugs, drug proprietaries, druggists' sundries	4222
12. Apparel, piece goods, notions	4223
13. Groceries and related products	4224
14. Farm products—raw materials	4225
15. Chemicals and allied products	4226
16. Petroleum and petroleum products	4227
17. Beer, wine, distilled alcoholic beverages	4228
18. Miscellaneous nondurable goods	4229

individual wholesale establishments, with combined total sales in excess of \$4 trillion. A look at how this total breaks down among the categories of wholesalers reveals important trends in wholesaling for the decade between 1987 and 1997.

Figure 2.4 compares total sales of all wholesalers and sales broken down by the three major types of wholesalers for the years 1987 and 1997; Figure 2.5 compares the percentage of total sales for each of the three types of wholesalers for the same two years.

Figure 2.4
Wholesaler Sales
(in millions of dollars)
by Type of Wholesaler,
1987 and 1997

Source: U.S. Department of Commerce: Census of Wholesale Trade (Washington, DC, various years).



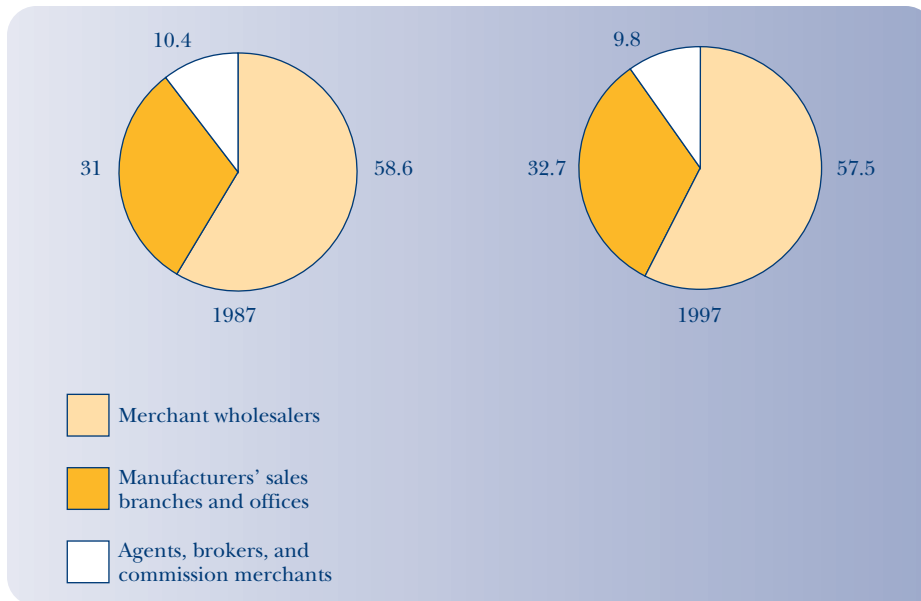


Figure 2.5
Percentage of Wholesaler Sales by Type of Wholesaler, 1987 and 1997

Source: U.S. Department of Commerce: Census of Wholesale Trade (Washington, DC, various years).

As shown in Figure 2.4, absolute sales of all three types of wholesalers increased substantially over this ten-year period, although the percentages of increase varied somewhat. The largest increase (69.7%) was for manufacturers' sales branches and offices; the smallest increase (50.9%) was for agents, brokers, and commission merchants. The result, as Figure 2.5 indicates, is that the percentage of total wholesale sales enjoyed by manufacturers' sales branches and offices increased from 31 percent in 1987 to 32.7 percent in 1997, while the share of total wholesale sales of agents, brokers, and commission merchants slipped from 10.4 percent to 9.8 percent during that ten-year period. The percentage of total wholesale sales of merchant wholesalers also slipped during that same period, from 58.6 percent to 57.5 percent. This decrease for merchant wholesalers represents a reversal of a trend dating back to 1948 of steady growth in merchant wholesalers' percentage of wholesaler sales relative to manufacturers' sales branches and offices and agents, brokers, and commission merchants.⁶ This pattern of increase as well as the most recent downturn is shown in Figure 2.6.

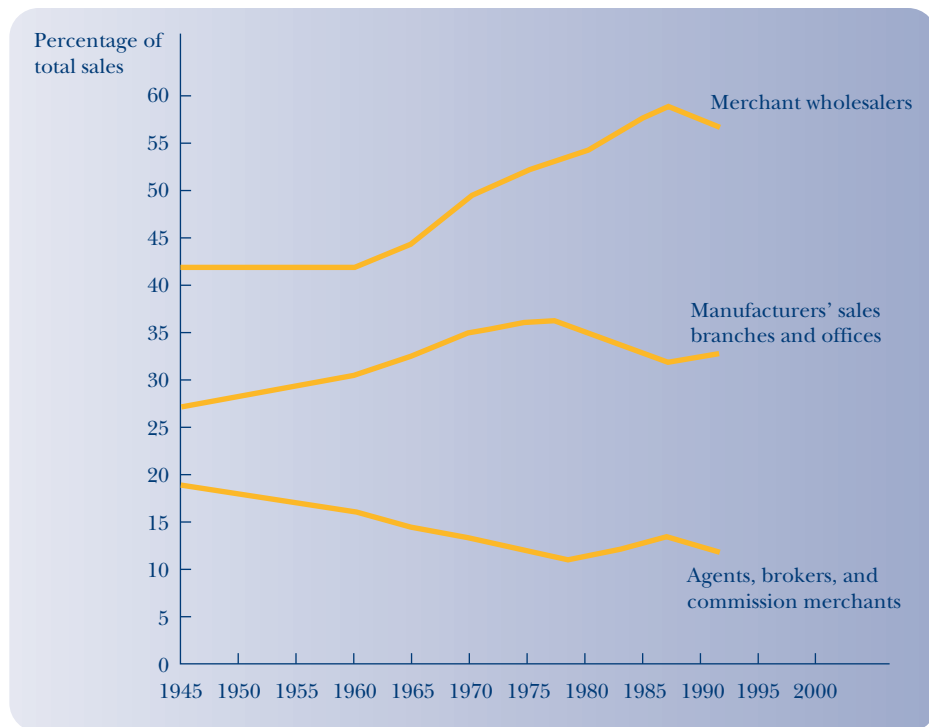
Size and Concentration in Wholesaling

Although wholesalers vary widely in size, the industry is still made up chiefly of small businesses. In terms of sales volume, many wholesalers are quite small, with almost 40 percent of all wholesale firms having annual sales of less than \$1 million. Table 2.2 provides a further breakdown of wholesaler sales volume. As shown in the table, almost 86 percent of all wholesale establishments reported total sales below \$10 million, while just over 6 percent of all establishments had total sales of \$25 million or more.

When size is measured in terms of number of employees per wholesale firm, the small size of most wholesalers is also quite evident. Table 2.3 shows this pattern. It is obvious from the table that relatively few wholesalers have large numbers of employees. Indeed, just over

6. For a related discussion on trends involving merchant wholesalers, see Stephen F. Pirog III and Michael F. Smith, "A Market-Oriented Approach to Identifying Structural Change in Wholesaling," *Journal of Marketing Channels* (Winter 1996): 37.

Figure 2.6
Percentage of Wholesaler Sales by Type of Operation, 1948–1997



2 percent had 100 or more employees, while almost 50 percent had fewer than five employees. So, while there are some large—even giant—wholesalers, the majority, especially merchant wholesalers as well as agents and brokers, are still privately held, family-run businesses with small numbers of employees.⁷

Economic concentration in terms of the percentage of total wholesale sales enjoyed by the largest firms is relatively low for merchant wholesalers as well as agents, brokers, and commission merchants but significantly larger for manufacturers' sales branches and offices. As shown in Figure 2.7, the 50 largest merchant wholesalers and the 50 largest agents, brokers,

Table 2.2
Sales Volume of Wholesale Firms, 1997

Source: U.S. Department of Commerce, Census of Wholesale Trade (Washington, DC, 1997).

Annual Sales (in millions of dollars)	Number of Firms	Percentage of Firms
25 or over	23,415	5.9
10 but under 25	32,974	8.3
5 but under 10	42,587	10.6
2.5 but under 5	56,217	14.1
1.0 but under 2.5	85,265	21.3
Under 1	158,928	39.8
Total	399,386	100.0

7. For an extensive and in-depth look at wholesaling, see Robert F. Lusch et al., *Foundations of Wholesaling: A Strategic and Financial Chart Book* (Norman, Okla.: Distribution Research Program, College of Business Administration, 1996).

Number of Employees	Number of Firms	Percentage of Firms
100 or more	6,840	2.2
50 to 99	9,338	3.0
20 to 49	30,924	9.8
10 to 19	45,877	14.5
5 to 9	66,214	21.0
Less than 5	156,015	49.5
Total	315,208	100.0

Table 2.3
Numbers of Employees
in Wholesale Firms, 1997

Source: U.S. Department of Commerce, Census of Wholesale Trade (Washington, DC, 1997).

and commission merchants accounted for only 16 percent and 27.8 percent of total sales, respectively, while the 50 largest manufacturers' sales branches and offices accounted for almost 53 percent of total sales for this type of wholesaler. We should point out, however, that more consolidation is occurring among merchant wholesalers due to increasing numbers of mergers and acquisitions. Thus, both the average size of merchant wholesalers and the degree of concentration in the industry are increasing.

Distribution Tasks Performed by Merchant Wholesalers

Merchant wholesalers serve manufacturers as well as retailers and other customers. They have survived as intermediaries in the marketing channel because, as specialists in the performance of distribution tasks, they can operate at high levels of effectiveness and efficiency.⁸

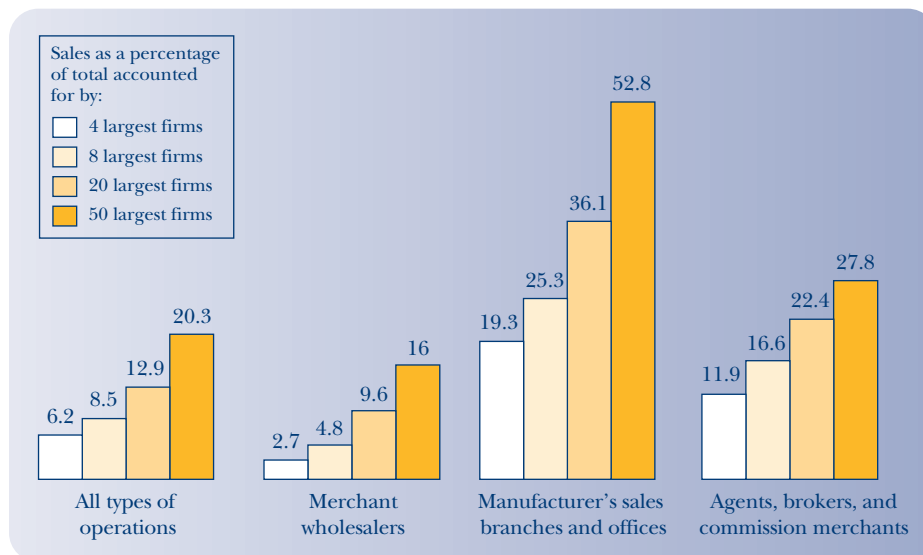


Figure 2.7
Concentration of Wholesale Sales (in percent) by Type of Wholesalers of Various Sizes, 1997

8. Ronald D. Michman and Stanley D. Sibley, "Wholesaling: A Neglected Area," in *Proceedings of the Annual Meeting of the Southern Marketing Association*, eds. David M. Klein and Allen E. Smith (Boca Raton, Fla.: Florida Atlantic University, 1985), 118–123.

Often the average cost curves for distribution tasks are lower for wholesalers, or they are able to operate closer to the optimum points on the curves than their suppliers.⁹ Modern, well-managed merchant wholesalers are especially well suited for performing the following types of distribution tasks for producers and manufacturers.¹⁰

1. Providing market coverage
2. Making sales contacts
3. Holding inventory
4. Processing orders
5. Gathering market information
6. Offering customer support

Market coverage is provided by merchant wholesalers to manufacturers because the markets for the products of most manufacturers consist of many customers spread over large geographical areas. To have good market coverage so that their products are readily available to customers when needed, manufacturers often rely on merchant wholesalers to secure the necessary market coverage at reasonable cost.¹¹ In the magazine industry, for example, the mass consolidation of magazine wholesalers from almost 3,000 to fewer than 50 in the past decade has publishers worried that their ability to reach small retail vendors in more remote markets will suffer.¹²

As Jackson and d'Amico point out in their study of merchant wholesalers serving industrial markets, "when large markets are dispersed geographically among several industries, and customers order frequently and require shorter lead times, distributors [merchant wholesalers] are more likely to be employed."¹³ Table 2.4 shows the findings from their study, which compared the use of agents and merchant wholesalers by manufacturers selling industrial products. As shown in the table, 43 percent of the manufacturers operating in dispersed markets used merchant wholesalers, as compared to only 22 percent who used agents—a ratio of about two to one.

Table 2.4
Percentage of Manufacturers' Use of Merchant Wholesalers versus Agents in Concentrated versus Dispersed Markets

Channel Structure ^a	Market Characteristics	
	Concentrated ^b	Dispersed ^c
Merchant wholesalers	57	43
Agents	78	22

^aBased on 90 merchant wholesalers and 109 agents
^b1 to 4 market centers
^c5 to 10 market centers

Source: Adapted from Donald M. Jackson and Michael F. d'Amico, "Products and Markets Served by Distributors and Agents," *Industrial Marketing Management* 18 (February 1989): 29.

9. *Facing the Forces of Change: Transforming Your Business with Best Practices* (Washington, D.C.: Distribution Research and Education Foundation, 1995).

10. Bert Rosenbloom, *Marketing Functions and the Wholesaler-Distributor: Achieving Excellence in Distribution* (Washington, D.C.: Distribution Research and Education Foundation, 1987), 17–28.

11. For a related discussion, see Denis F. Healy and H. Lee Mathews, *Branching and Market Coverage: Growth Strategies for Wholesaler-Distributors* (Washington, D.C.: Distribution Research and Education Foundation, 1984).

12. Mathew Rose, "Magazine Wholesaler Pressures Publishers, Adding to Their Woes," *Wall Street Journal* (March 5, 2001): A1, A6.

13. Donald M. Jackson and Michael F. d'Amico, "Products and Markets Served by Distributors and Agents," *Industrial Marketing Management* 18 (February 1989): 33.

Sales contact is a valuable service provided by merchant wholesalers. For manufacturers, the cost of maintaining an outside sales force is high. If a manufacturer's product is sold to many customers over a large geographical area, the cost of covering the territory with its sales force can be prohibitive.¹⁴ By using wholesalers to reach all or a significant portion of their customers, manufacturers may be able to reduce substantially the costs of outside sales contacts because their sales force would be calling on a relatively small number of wholesalers rather than the much larger number of customers.

The value of wholesalers in providing sales contact becomes even more apparent for manufacturers entering foreign markets. As Brown and Herring point out for the case of an American manufacturer attempting to sell its products in the U.K.:

The costs of setting up a U.K. sales operation are enormous: an office must be rented and equipped with all the necessary communication and data-processing equipment, staff must be recruited and trained (or relocated from America), the products must be marketed, and the potential customer base identified. There is a very large investment to be made, with no possibility of quick returns. A distributor, on the other hand, has all the infrastructure in place, knows the market, and should be able to provide sales very quickly.¹⁵

Holding inventory is another crucial task performed by wholesalers for manufacturers. Merchant wholesalers take title to, and usually stock, the products of the manufacturers whom they represent. By doing so, they can reduce the manufacturers' financial burden and reduce some of the manufacturers' risk associated with holding large inventories. Moreover, by providing a ready outlet for manufacturers' products, wholesalers help manufacturers to better plan their production schedules. For example, Fort Howard Corporation, a paper products manufacturer, uses paper products wholesalers such as Darter Inc. of University Park, Illinois, to perform the inventory holding task. Fort Howard and Darter arranged a "partnership" agreement whereby Darter agrees to buy virtually all of its products from Fort Howard in exchange for favorable terms, including assured availability of products and faster deliveries. In exchange, Fort Howard has an assured high-volume outlet for its products as they come out of the factory and thus does not have to carry them in its own inventory.

Order processing performed by wholesalers is very helpful to manufacturers because many customers buy in small quantities. Yet manufacturers both large and small find it extremely inefficient to attempt to fill large numbers of small orders from thousands of customers. Many of the original dot-com firms engaged in E-commerce were undermined by the high fulfillment costs associated with thousands of small orders. For most of them, order processing costs were a major cause of their demise because the costs were very high relative to the value of the products being sold.¹⁶ Wholesalers, on the other hand, are specifically geared to handle small orders from many customers. By carrying the products of many manufacturers, wholesalers' order processing costs can be absorbed by the sale of a broader array of products than that of the typical manufacturer. An outstanding example of a wholesaler that has achieved a very high level of expertise in performing the order-processing task is the McKesson Corporation, the world's largest wholesaler of pharmaceutical products. McKesson has always made order processing for its wide range of customers, including

14. James D. Hlavacek and Tommy J. McCuiston, "Industrial Distributors—When, Who, and How?" *Harvard Business Review* (March–April 1983): 96–101; and James A. Narus, N. Mohan Reddy, and George L. Pinchak, "Key Problems Facing Industrial Distributors," *Industrial Marketing Management* (August 1984): 139–147.

15. Reva Berman Brown and Richard Herring, "The Role of the Manufacturer's Distributor," *Industrial Marketing Management* 24 (October 1995): 285–295.

16. Bert Rosenbloom, "The Ten Deadly Myths of E-Commerce," *Business Horizons* (March–April 2002): 61–66.

chains and independent retail drug stores, hospitals, food stores, and mass merchandisers, the keystone of its operations. Its distribution centers are highly automated with high-speed order-processing systems, flow racks with lighted displays that direct workers' order selection, special carousels that bring orders to order fillers, and conveyor systems that automatically route boxes to shipping points. Few manufacturers can match McKesson's level of order processing in scale, sophistication, and efficiency.¹⁷

Gathering market information is another task of substantial benefit to manufacturers. Wholesalers are usually quite close to their customers geographically and in many cases have continuous contact through frequent sales calls on their customers. Hence, they are in a good position to learn about customers' product and service requirements. Such information, if passed on to manufacturers, can be valuable for product planning, pricing, and the development of competitive marketing strategy. Some wholesalers are using the Internet to provide information to link suppliers and customers together. For example, in the business of online sales of computer hardware and software, a half dozen wholesalers provide information on over 150,000 products from more than 800 manufacturers. Customers ranging from small businesses to giant corporations use these wholesalers to compare prices, locate hard-to-find parts, configure computer systems from multiple sources, and actually place orders over the Internet.¹⁸

Customer support is the final distribution task that wholesalers provide for manufacturers. Products may need to be exchanged or returned, or a customer may require setup, adjustment, repairs, or technical assistance. For manufacturers to provide such services directly to large numbers of customers can be very costly. Instead, manufacturers can use wholesalers to assist them in providing these services to customers. This extra support by wholesalers, often referred to as **value added services**, plays a crucial role in making wholesalers vital members of the marketing channel from the standpoints of both the manufacturers who supply them and the customers to whom they sell. Consider the case of F. F. Despard located in Utica, New York. This wholesaler deals in abrasive and cutting tools for customers in the woodworking and metalworking industries. Dick Wagner, vice president of F. F. Despard, comments about the firm's approach to providing customer support: "We only employ abrasives specialists [rather than mere salespeople] who are qualified to assist our customers with a wide range of questions concerning applications. We throw in technical assistance as a bonus and it distinguishes us from our competition."¹⁹

In addition to performing the six distribution tasks for manufacturers, as discussed in the preceding paragraphs, merchant wholesalers are equally well suited to perform the following distribution tasks for their customers:²⁰

1. Assuring product availability
2. Providing customer service
3. Extending credit and financial assistance
4. Offering assortment convenience
5. Breaking bulk
6. Helping customers with advice and technical support

Product availability, providing for the ready availability of products, is probably the most basic distribution task performed by wholesalers for customers. Because of the closeness of

17. Sharon L. Oswal and William R. Boulton, "Obtaining Industry Control: The Case of the Pharmaceutical Distribution Industry," *California Management Review* (Fall 1995): 139–162.

18. David Bank, "Middlemen Find Ways to Survive Cyberspace Shopping," *Wall Street Journal* (December 12, 1996): B1.

19. "Value Added, the Key to Distributor Survival," *Industrial Distribution* (November 1986): 58.

20. Rosenbloom, *Marketing Functions*, 21–27.

wholesalers to their customers and/or their sensitivity to customers' needs, they can provide a level of product availability that many manufacturers could not easily match. Consider what happened to Doug's TV, a retailer of television sets located in Beverly Hills, Florida. Doug's TV had been buying RCA brand television sets from Raybro Electric Supplies, Inc., a local wholesaler. When RCA decided to drop Raybro and sell direct to retailers, Doug's TV found it faced serious product availability problems. Instead of two-day truck delivery, it now took a month to get TVs. To partially alleviate this problem, Doug's now has to place larger orders, thus tying up more money in inventory.

Customer service is another valuable distribution task performed by wholesalers. Customers often require services such as delivery, repairs, or warranty work. By making these services available to their customers, wholesalers save their customers effort and expense.²¹ Alco Standard Corporation, for instance, the largest wholesaler of paper and office products in North America, provides repair services to its customers for their Ricoh, Canon, and Sharp copy machines, something that customers have found to be extremely convenient and helpful.²²

Credit and financial assistance are provided by wholesalers in two ways. First, by extending open account credit to customers on products sold, wholesalers allow customers to use products in their business before having to pay for them. Second, by stocking and providing ready availability for many of the items needed by their customers, wholesalers significantly reduce the financial inventory burden their customers would bear if they had to stock all the products themselves.

The case of Doug's TV, cited earlier in relation to product availability, also underscores the importance of wholesalers in providing credit and financial assistance. The wholesaler had let Doug's use favorable floor-plan financing terms on any size order, no matter how small. The manufacturer, on the other hand, allows such terms only on orders of at least \$2,000.

Assortment convenience refers to the wholesaler's ability to bring together from a variety of manufacturers an assortment of products, greatly simplifying customers' ordering tasks.²³ Instead of having to order separately from dozens or even hundreds of manufacturers, customers can turn to one or a few general line or specialist wholesalers who can provide them with all or most of the products they need. For example, Alco Standard Corporation, the giant paper products wholesaler cited earlier, fills literally thousands of orders for thousands of different products every day. In the process of doing so, it saves its customers enormous amounts of time and expense.²⁴

Breaking bulk is important because often customers do not need large quantities of products, or they may prefer to order only a small quantity at a time. Many manufacturers find it uneconomical to fill small orders and will establish minimum order requirements to discourage them. By buying large quantities from manufacturers and breaking down these "bulk" orders into smaller quantities, wholesalers provide customers with the ability to buy only the quantity they need. Alco Standard Corporation can also be cited as an outstanding example of the wholesaler's ability to perform this task. Many, if not most, of the orders it receives from customers would be too small to be ordered directly from manufacturers because of minimum order requirements. Alco, however, buys in huge quantities and then breaks them down into whatever amounts its customers wish to order.

Advice and technical support is the final distribution task wholesalers are called on to perform for their customers. Many products, even those that are not considered technical,

21. For related discussion, see Eric Panitz, "Distribution Image and Marketing Strategy," *Industrial Marketing Management* (November 1988): 315–323.

22. Gautam Naik, "Pieces in Alco's Distribution Network Fall into Place," *Wall Street Journal* (November 13, 1992): B6.

23. Wroe Alderson, *Marketing Behavior and Executive Action* (Homewood, Ill.: Irwin, 1957).

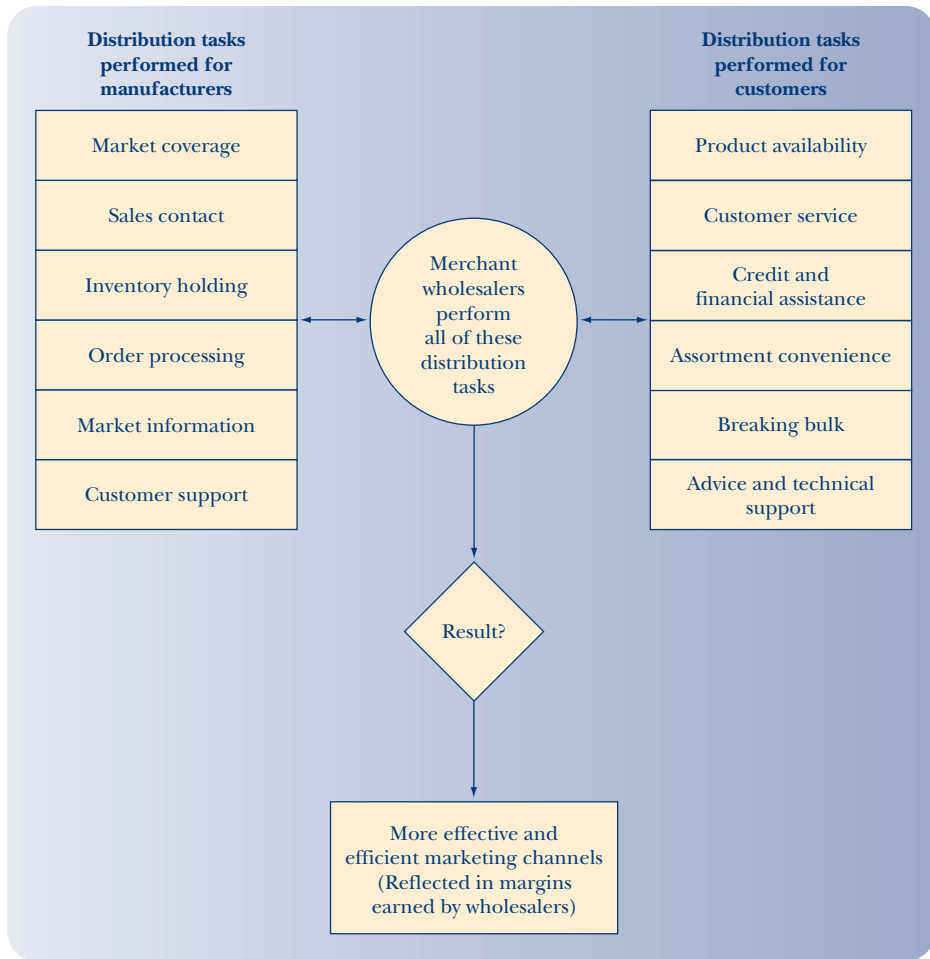
24. *Ibid.*

may still require a certain amount of technical advice and assistance for proper use, as well as advice on how they should be sold. Wholesalers, especially through a well-trained outside sales force, are able to provide this kind of technical and business assistance to customers. Ace Hardware Corporation, a large wholesaler based in Oak Brook, Illinois, offers a good example of a wholesaler that is especially adept at providing its customers (mostly independent hardware retailers) with advice and technical support. Ace offers its dealers a wide range of help with inventory planning, advertising, store layout, customer service, computer applications, and more.²⁵

Figure 2.8 provides a summary of the preceding discussion of the distribution tasks performed by merchant wholesalers. As shown in the figure, merchant wholesalers are placed between the set of six distribution tasks they perform for manufacturers and the six they perform for customers. The arrow leading down from the merchant wholesalers shows the result of performance of the distribution tasks: more effective and efficient marketing channels reflected in the margins received by merchant wholesalers. In effect, the margins earned by

Figure 2.8
Distribution Tasks
Performed by Merchant
Wholesalers and Their
Effect on the Marketing
Channel

Source: Bert Rosenbloom, Marketing Functions and the Wholesaler-Distributor: Achieving Excellence in Distribution (Washington, D.C.: Distribution Research and Education Foundation, 1987), 26.



25. Joseph Weber, "Wholesaling, It's Like Somebody Had Shot the Postman," *Business Week* (January 13, 1992): 82.

merchant wholesalers represent payment for services rendered by them and for value received by manufacturers and customers who bought the merchant wholesalers' only real product—*efficient performance of the distribution tasks*.

We should point out that not all merchant wholesalers in all lines of trade perform all of these distribution tasks all of the time. There are differences among merchant wholesalers in the extent to which they participate in the performance of distribution tasks. Many do indeed perform all of the distribution tasks discussed here most of the time, or at least they attempt to. At the other end of the spectrum are some merchant wholesalers traditionally referred to in the marketing literature as **limited function wholesalers** who, though taking title to products, do not perform all of the distribution tasks discussed. For example, mail-order wholesalers do not provide sales contact through personal selling, cash-and-carry wholesalers do not extend credit, drop shippers do not carry inventory, and rack jobbers generally do not provide much in the way of advice and technical support.

Distribution Tasks Performed by Agent Wholesalers

As mentioned earlier in the chapter, agent wholesalers—defined by the *Census of Wholesale Trade* as agents, brokers, and commission merchants—do not take title to the products they sell. Also, as a rule, they do not perform as many distribution tasks as a typical merchant wholesaler. **Manufacturers' agents** (also referred to as manufacturers' representatives or "reps"), for example, specialize mainly in performing the market coverage and sales contact distribution tasks for manufacturers. In effect, the manufacturers' agents substitute for the manufacturer's outside sales force. Thus, they are especially valuable to manufacturers who are not capable of fielding their own sales forces, or to supplement the selling efforts of those manufacturers who do have their own sales forces but who find it uneconomical to use them for certain product categories or territories. Manufacturers' agents generally represent several manufacturers at the same time and operate in a wide range of product and service categories such as housewares, hardware, paint, chemicals, food-processing equipment, electronics and electrical components, steel, and packaging. Services sold by manufacturers' agents include painting, plating services, machinery rebuilding, cleaning, and a variety of business services.

Selling agents, another type of agent wholesaler, usually perform more distribution tasks than manufacturers' representatives. In fact, they may handle virtually the entire marketing and sales effort for the manufacturers they represent. Thus, although selling agents usually do not physically hold inventory or take title to it, they may perform many if not most of the other distribution tasks, such as providing market coverage, sales contact, order processing, marketing information, product availability, and customer services.

Although the basic marketing literature discusses manufacturers' agents and selling agents as though a clear and precise distinction exists between them, in practice such a distinction is not usually made. In fact, it is quite common to use terms such as *sales agent*, *selling agent*, *manufacturers' agent*, *manufacturers' representatives*, *reps*, or *export/import agents* interchangeably to refer to all types of agent wholesalers without any strict distinctions made about the degree to which they perform distribution tasks. Historical patterns of usage of terms in various trades is the actual basis for referring to various types of agent wholesalers, rather than conceptual clarity or logic.

Brokers, the second major category of non-title-taking wholesalers defined in the *Census of Wholesale Trade*, offer another example of the wide deviation between definitions based on the performance of distribution tasks presented in the marketing literature and performance in actual practice. In the marketing literature the broker is usually defined as a go-between, or a party who brings buyers and sellers together so that a transaction can be consummated. In the strictest definition sense, then, a broker would perform only one distribution task—providing market information. Yet, in practice, some brokers may perform many if not most

of the distribution tasks, so that for all practical purposes there is little to distinguish them from manufacturers' representatives or selling agents.

Consider the case of food brokers. A study by the National Food Brokers Association (NFBA) found that the overwhelming majority of food brokers perform a wide range of distribution tasks in marketing channels, which places them on a par with manufacturers' representatives or selling agents. For example, many food brokers help manage marketing funds, recommend and execute trade promotions, and even help create consumer promotion plans. Many are also involved with developing and executing the marketing programs of the manufacturers they represent. In so doing, they provide (in addition to market information) market coverage, sales contact, order processing, and customer support and advice, as well as product availability.²⁶ Figure 2.9 provides a further description of the services provided by food brokers.

Clearly, as Figure 2.9 indicates, the range of distribution tasks performed by food brokers places them well beyond the limited scope specified in the marketing textbook definition of brokers. Here again, the terminology used is more a function of historical accident than strict adherence to terminology. In fact, the term *food broker* is something of a misnomer because food brokers actually deal in many products besides food.²⁷ While food brokers are not indicative of all brokers in other product categories, the role of brokers in performing distribution tasks is generally expanding to the point that use of the word *broker* may understate the range of activities involved.

Finally, the third major category of agent wholesalers in the *Census of Wholesale Trade* is the **commission merchant**, of significance mainly in agricultural markets. Commission merchants actually perform a wide range of distribution tasks, including physically holding inventory (though not taking title), providing market coverage, sales contact, breaking bulk, credit, and order processing. These distribution tasks are performed in the course of the commission merchant's acting on behalf of his or her principals (producers or manufacturers). Essentially the commission merchant receives and warehouses products, helps locate

Figure 2.9 Distribution Tasks Commonly Performed by Food Brokers

Source: National Food Brokers Association, "Specialized Services: How Brokers Serve You (Washington, D.C.: National Food Brokers Association, 1993), 2–3.

Brokers provide a variety of specialized services that add value to the distribution process and help increase profits for their principals and customers. Brokers typically are engaged in one or more of the following:

- Introducing their principals' new products to local market buyers.
- Regularly contacting retailers to ensure that a principal's products are in distribution and placed properly on the retail shelf.
- Coordinating with retailers to implement promotions, advertising campaigns, and couponing programs; to arrange in-store displays; and to conduct product demonstrations.
- Ensuring that a principal's products are ordered correctly, that shipments are received and priced correctly, and that unsalable items are credited and disposed of properly.
- In conjunction with their principals' marketing departments and customers, developing promotional programs for consumers in the local market.
- Through the use of advanced technologies, furnishing their principals with demographic data about consumer trends, product placement, marketing, and other information.

26. "Food Brokers Seek Compensation for Expanding Role in Marketing Plans," *Marketing News* (July 4, 1988): 7.

27. See, for example, National Food Brokers Association, *How Brokers Serve You* (Washington, D.C.: National Food Brokers Association, 1993), 1–7.

buyers, makes sales, extends personal credit, processes orders, and may arrange for delivery. After completing the sale and collecting the money from the buyers, the commission merchant remits it (less the commission for services supplied) to the principals, who sometimes remain anonymous to buyers.

What should be apparent from this discussion of distribution tasks performed by the various types of agent wholesalers is that generalizations about their roles in performing distribution tasks based on their “official” definitions can be misleading. A more meaningful way of determining just which distribution tasks are performed by which type of agent wholesaler is to look at the line of trade they are in or, better yet, the particular agent wholesaler in question. It might well turn out that a broker in one line of trade performs a much wider array of distribution tasks than a manufacturers’ representative in another, or that a given selling agent does the same set of distribution tasks as a particular “rep,” broker, or commission merchant.

Finally, regardless of whether the wholesaler in question is a merchant wholesaler or a so-called agent, broker, or commission merchant, the wholesaler’s participation in marketing channels is predicated on the performance of distribution tasks (services) that are desired by manufacturers and customers. Moreover, any of these wholesalers must be able to perform these distribution tasks more efficiently than either manufacturers or customers. With so many manufacturers and customers aggressively seeking ways to increase their productivity and reduce costs, they are taking a very hard look at the wholesaler’s role in their marketing channels. Only those wholesalers who do an especially good job of performing distribution tasks at a very high level of efficiency are likely to remain in, let alone improve, their positions as viable members of the marketing channel.

Retail Intermediaries

Retailers consist of business firms engaged primarily in selling merchandise for personal or household consumption and rendering services incidental to the sale of goods.

Kinds of Retailers

Retailers in the United States comprise an extremely complex and diverse conglomeration. They range in size from the so-called mom-and-pop neighborhood stores, with sales of less than \$100,000 per year, to giant mass merchandise chains such as Wal-Mart, with over \$200 billion in annual sales. Methods of operation run from minimum service, spartan discount, and outlet stores to elaborate operations with magnificent architecture in grand shopping malls. The category includes store retailers as well as nonstore retailers such as mail-order firms, direct selling (in-home) retailers, TV shopping show retailers, and retailers operating on the Internet.²⁸ There are specialty retailers, broad-line department store retailers, giant superstore retailers, “wholesale” club retailers, and factory outlet retailers as well as global, national, regional, and local retailers. The list can go on and on.

Over the years, a variety of classification schemes has been developed to help lend some order to this bewildering complexity. Table 2.5 outlines the most commonly used classification categories.

The most comprehensive and widely used approach to classifying retailers is that used by the *Census of Retail Trade*, which places all retailers into more than 50 kind-of-business classifications within 12 major groups. These twelve major groups are shown in Table 2.6 in bold type with three-digit North American Industry Classification System (NAICS) codes. Most kind-of-business classifications used by the *Census of Retail Trade* are also listed in the table.

28. See “Integrating Multiple Channels,” *Chain Store Age* (August 2001): 24A–25A.

Table 2.5
Alternative Bases for Classifying Retailers

A. By Ownership of Establishment

1. Single-unit independent stores
2. Multiunit retail organizations
 - a. chain stores
 - b. branch stores
3. Manufacturer-owned retail outlets
4. Consumers' cooperative stores
5. Farmer-owned establishments
6. Company-owned stores (industrial stores) or commissaries
7. Government-operated stores (post exchanges, state liquor stores)
8. Public utility company stores (for sale of major appliances)

B. By Kind of Business (Merchandise Handled)

1. General merchandise group
 - a. department stores
 - b. dry goods, general merchandise stores
 - c. general stores
 - d. variety stores
2. Single-line stores (e.g., grocery, apparel, furniture)
3. Specialty stores (e.g., meat markets, lingerie shops, floor-covering stores)

C. By Size of Establishment

1. By number of employees
2. By annual sales volume

D. By Degree of Vertical Integration

1. Nonintegrated (retailing functions only)
2. Integrated with wholesaling functions
3. Integrated with manufacturing or other form-utility creation

E. By Type of Relationship with Other Business Organizations

1. Unaffiliated
2. Voluntarily affiliated with other retailers
 - a. through wholesaler-sponsored voluntary chains
 - b. through retailer cooperation
3. Affiliated with manufacturers by dealer franchises

F. By Method of Consumer Contact

1. Regular store
 - a. leased department
2. Mail order
 - a. by catalog selling
 - b. by advertising in regular media
 - c. by membership club plans
3. Household contacts
 - a. by house-to-house canvassing
 - b. by regular delivery route service
 - c. by party plan selling

G. By Type of Location

1. Urban
 - a. central business district
 - b. secondary business district
 - c. string street location
 - d. neighborhood location
 - e. controlled (planned) shopping center
 - f. public market stalls
2. Small city
 - a. downtown
 - b. neighborhood
3. Rural stores
4. Roadside stands

H. By Type of Service Rendered

1. Full service
2. Limited service (cash-and-carry)
3. Self service

I. By Legal Form of Organization

1. Proprietorship
2. Partnership
3. Corporate
4. Special types

J. By Management Organizations or Operational Technique

1. Undifferentiated
2. Departmentalized

Table 2.6
Twelve Major Kind-of-Business Classifications Used in the *Census of Retail Trade*

Kind of Business	NAICS code	Kind of Business	NAICS code
Retail trade	44–45	Gasoline stations	447
Motor vehicle & parts dealers	441	Gasoline stations with convenience stores	44711
Automobile dealers	4411	Other gasoline stations	44719
New car dealers	44111	Clothing & clothing accessories stores	448
Used car dealers	44112	Clothing stores	4481
Other motor vehicle dealers	4412	Mens clothing stores	44811
Recreational vehicle dealers	44121	Womens clothing stores	44812
Motorcycle, boat, & other motor vehicle dealers	44122	Childrens & infants clothing stores	44813
Automotive parts, accessories, & tire stores	4413	Family clothing stores	44814
Automotive parts & accessories stores	44131	Clothing accessories stores	44815
Tire dealers	44132	Other clothing stores	44819
Furniture & home furnishings stores	442	Shoe stores	4482
Furniture stores	4421	Jewelry, luggage, & leather goods stores	4483
Home furnishings stores	4422	Jewelry stores	44831
Floor covering stores	44221	Luggage & leather goods stores	44832
Other home furnishings stores	44229	Sporting goods, hobby, book, & music stores	451
Electronics & appliance stores	443	Sporting goods, hobby, & musical instrument stores	4511
Appliance, television, & other electronics stores	44311	Sporting goods stores	45111
Computer & software stores	44312	Hobby, toy, & game stores	45112
Camera & photographic supplies stores	44313	Sewing, needlework, & piece goods stores	45113
Building material & garden equipment & supplies dealers	444	Musical instrument & supplies stores	45114
Building material & supplies dealers	4441	Book, periodical, & music stores	4512
Home centers	44411	Book stores & news dealers	45121
Paint & wallpaper stores	44412	Prerecorded tape, compact disc, & record stores	45122
Hardware stores	44413	General merchandise stores	452
Other building material dealers	44419	Department stores (incl. leased depts.)	4521
Lawn & garden equipment & supplies stores	4442	Department stores (excl. leased depts.)	4521
Outdoor power equipment stores	44421	Other general merchandise stores	4529
Nursery & garden centers	44422	Warehouse clubs & superstores	45291
Food & beverage stores	445	All other general merchandise stores	45299
Grocery stores	4451	Miscellaneous store retailers	453
Supermarkets & other grocery (except convenience) stores	44511	Florists	4531
Convenience stores	44512	Office supplies, stationery, & gift stores	4532
Specialty food stores	4452	Office supplies & stationery stores	45321
Meat markets	44521	Gift, novelty, & souvenir stores	45322
Fish & seafood markets	44522	Used merchandise stores	4533
Fruit & vegetable markets	44523	Other miscellaneous store retailers	4539
Other specialty food stores	44529	Pet & pet supplies stores	45391
Beer, wine, & liquor stores	4453	Art dealers	45392
Health & personal care stores	446	Manufactured (mobile) home dealers	45393
Pharmacies & drug stores	44611	All other miscellaneous store retailers	45399
Cosmetics, beauty supplies, & perfume stores	44612	Nonstore retailers	454
Optical goods stores	44613	Electronic shopping & mail-order houses	4541
Other health & personal care stores	44619	Vending machine operators	4542
		Direct selling establishments	4543
		Fuel dealers	45431
		Other direct selling establishments	45439

For data gathering and reporting purposes, the *Census of Retail Trade* cross-classifies these 12 major groups and the more specific kind-of-business categories with a variety of data, for the United States as a whole and for many smaller geographical areas as well.

Structure and Trends in Retailing

As of 1997 (the latest year for which data are available from the *Census of Retail Trade*), there were 1,118,447 retail establishments in the United States, producing a sales volume of almost \$2.5 trillion. When the previous census was taken in 1992, there were 1,526,215 retail establishments with a combined sales volume of almost \$1.9 trillion. Given the decrease in number of establishments between 1992 and 1997 and the 32 percent increase in sales, the size of retail establishments measured by average sales volume per store must have increased significantly during those five years. This was indeed the case, and in fact continues a long-term trend dating back to 1948. As shown in Table 2.7, average sales for retail establishments were almost \$2.2 million by 1997, up from \$1.24 million in 1992. This is an increase of almost 77 percent.

This pattern of increasing total sales as well as average sales per retail establishment was consistent across all major kind-of-retail-business groups between 1992 and 1997.

Concentration in Retailing

From the standpoint of economic concentration, retailing in the United States is increasingly dominated by large firms. In 1997, for example, large retailers (those with sales of \$10 million or more), though comprising just 4 percent of all retail firms, accounted for almost 80 percent of total retail sales. On the other hand, small retailers (those with sales of less than \$1 million) accounted for almost 70 percent of all retail firms but only 6.5 percent of total retail sales (see Figure 2.10).

The domination of retailing in the United States by large retailers is also evident in Figure 2.11, which shows that in 1997 for retail trade as a whole, the 50 largest firms accounted for 26 percent of total retail sales. When one looks at particular kinds of retail businesses, the domination of large firms is even more striking. Figure 2.12, for example, shows four kinds of retailers where the four largest firms account for at least 70 percent of total sales in that category.

Table 2.7
Total Retail Sales, Number of Establishments, and Average Sales per Establishment, 1948–1997

Source: U.S. Department of Commerce, Bureau of the Census, Census of Retail Trade (Washington, D.C.: G.P.O., various years).

Year	Total (billions)	Number of Stores (millions)	Average Sales per Store
1997	\$2,460.9	1.12	\$2,197,000
1992	1,894.1	1.53	1,242,000
1987	1,494.1	1.50	996,000
1982	1,038.2	1.42	731,000
1977	723.1	1.86	389,000
1972	470.8	1.91	246,000
1967	310.2	1.76	176,000
1963	244.2	1.71	143,000
1958	199.2	1.78	112,000
1948	130.5	1.77	74,000

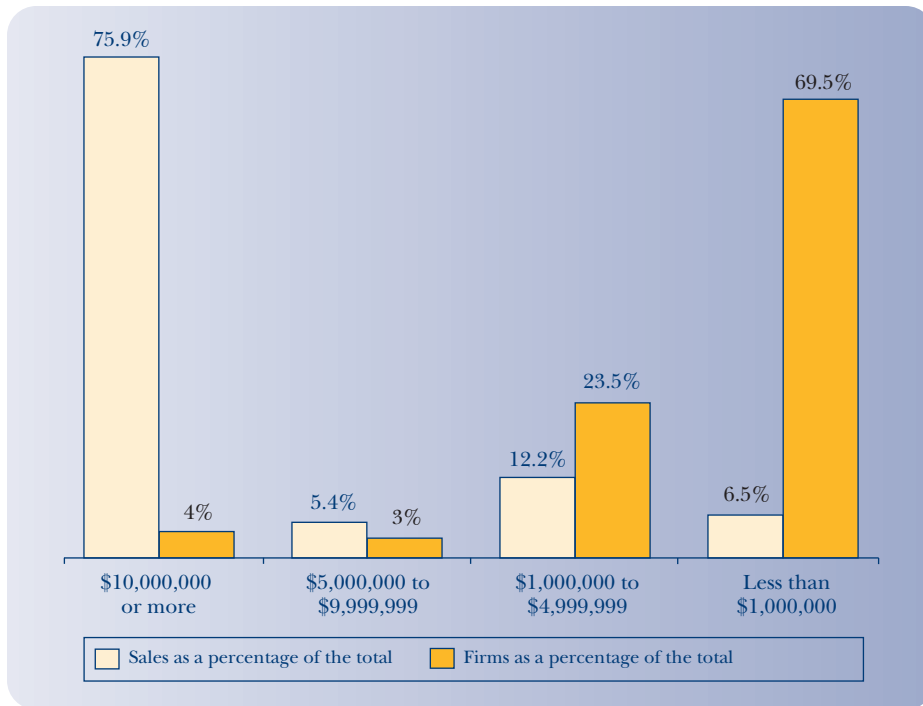


Figure 2.10
Percentage Distribution of Retail Firms and Sales by Size of Firms, 1997

Source: U.S. Department of Commerce, Bureau of the Census, Census of Retail Trade: Establishment and Firm Size (Washington, DC: G.P.O., 1997).

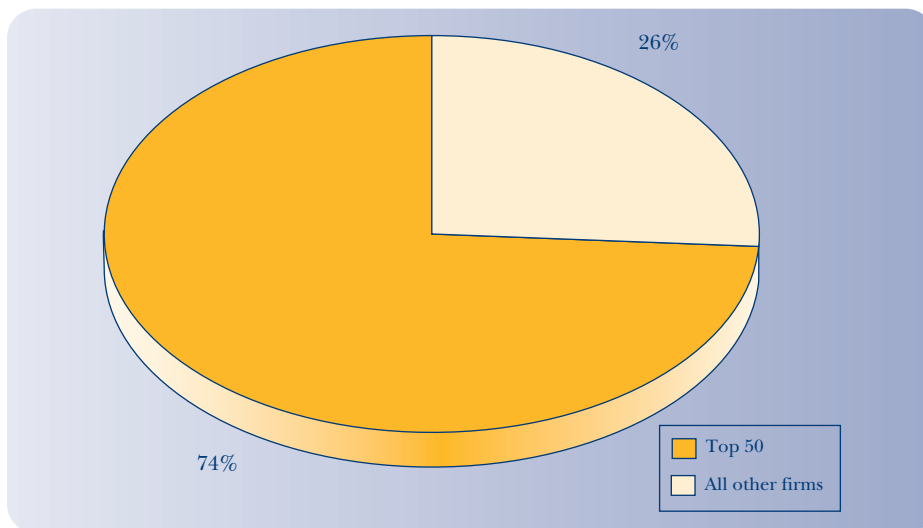


Figure 2.11
Concentration of Sales Among the Top 50 Retail Firms, 1997

Source: U.S. Department of Commerce, Bureau of the Census, Census of Retail Trade: Establishment and Firm Size (Washington, DC: G.P.O., 1997).

The preceding data shown up through figure 2.12 on the next page just begin to convey the size and concentration of retailing. A more vivid picture emerges when the absolute size of retailers is considered. Table 2.8, for example, lists the 100 largest retailers in the United States, all of which have sales in excess of \$1 billion. Moreover, as shown in the table, each of the top ten retailers had sales of more than \$32 billion, the top four each produced sales of more than \$40 billion, and the largest retailer—Wal-Mart—achieved sales of almost \$220 billion.

Figure 2.12
Kinds of Retailers
Where Largest Four
Firms Account for at
Least 50 Percent of
Total Sales

Source: U.S. Department of Commerce, Bureau of the Census, Census of Retail Trade: Establishment and Firm Size (Washington, DC: G.P.O., 1997).

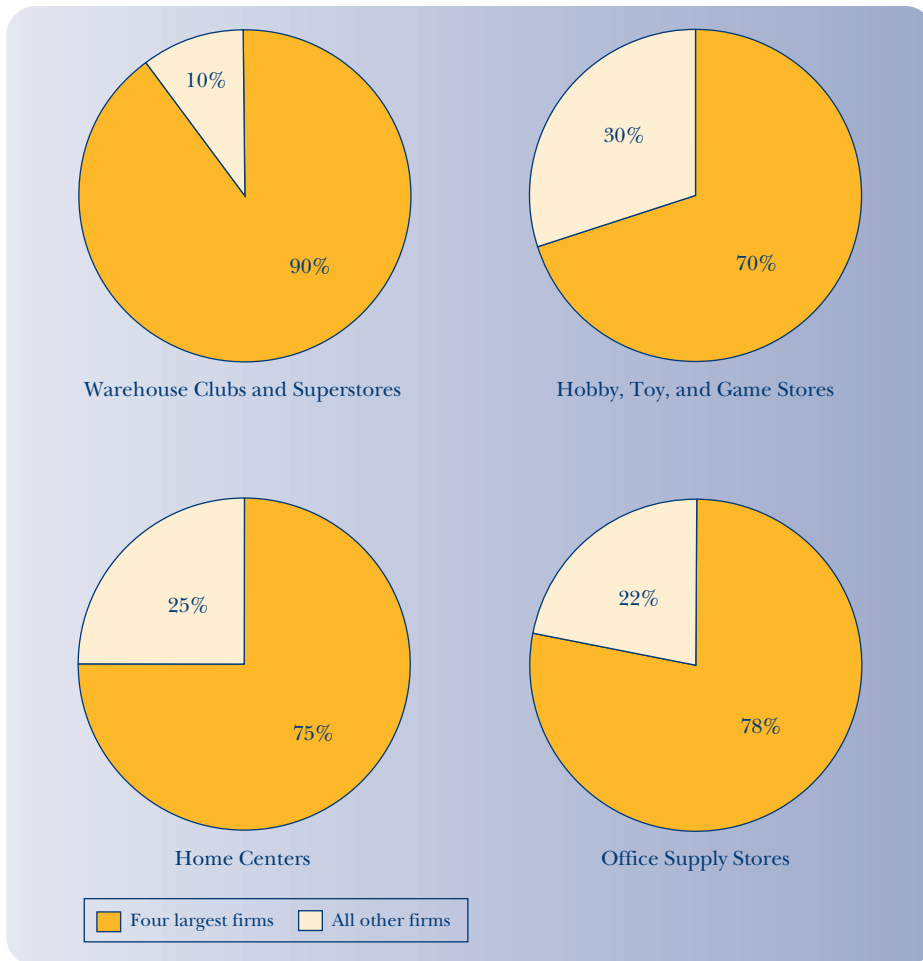


Table 2.8
The 100 Largest Retailers in the United States, 2001

Company/Headquarters/ Main Retail Segments/ Fiscal Year End	2001 Revenues (000)	2000 Revenues (000)	2001 Profits (000)	2000 Profits (000)	Stores 2001 2000
1 Wal-Mart Stores Inc. Bentonville, Ark. (DS, SC, WC, S, E) 1/31/02	\$219,812,000	\$193,295,000	\$6,671,000	\$6,295,000	4,414 4,189
2 The Home Depot Atlanta (HC) 2/3/02	53,553,000	45,738,000	3,044,000	2,581,000	1,333 1,134

* Estimate ** Retail operations only; operating income reported *** Excludes fuel sales † Continuing operations () Loss
 AS = Apparel Specialty D = Department GM = General Merchandise SC = Supercenter WC = Warehouse Wholesale Club
 C = Catalog DR = Drug Store HC = Home Center SF = Specialty Food
 CS = Catalog Showroom DS = Discount HS = Hard Line Specialty SH = Shoe Store DNA = Does not apply
 CV = Convenience Store E = Electronic S = Supermarket V = Variety NA = Not available

Source: Chain Store Age, "State of the Industry" (August 2002): 3A-8A.

Table 2.8 (continued)

	Company/Headquarters/ Main Retail Segments/ Fiscal Year End	2001 Revenues (000)	2000 Revenues (000)	2001 Profits (000)	2000 Profits (000)	Stores 2001 2000
3	The Kroger Co. Cincinnati (S, CV, SC, HS) 2/2/02	\$50,098,000	\$49,000,000	\$1,043,000	\$877,000	3,634 3,541
4	Sears, Roebuck and Co. Hoffman Estates, Ill. (D, HS, C, HC, E) 12/29/01	41,078,000	40,937,000	735,000	1,343,000	2,185 2,199
5	Target Corp. Minneapolis (DS, D, SC, E) 2/2/02	39,888,000	36,903,000	1,368,000	1,264,000	1,381 1,307
6	Albertson's Boise, Idaho (S, DR) 1/31/02	37,931,000	36,762,000	501,000	765,000	2,421 2,512
7	Kmart Corp. Troy, Mich. (DS, SC, E) 1/30/02	36,151,000	37,028,000	(2,587,000)	(244,000)	2,114 2,105
8	Costco Issaquah, Wash. (WC, E) 9/2/01	34,797,037	32,164,296	602,089	631,437	369 335
9	Safeway Pleasanton, Calif. (S, E) 12/29/01	34,301,000	31,976,900	1,253,900	1,091,900	1,773 1,688
10	JC Penney Plano, Texas (D, C, DR, E) 1/26/02	32,004,000	31,846,000	98,000	(705,000)	3,770 3,800
11	Dell Computer Round Rock, Texas (C, E) 2/1/02	31,168,000	31,888,000	1,246,000	2,236,000	DNA DNA
12	Walgreen Co. Deerfield, Ill. (DR) 8/31/01	24,623,000	21,206,900	885,600	776,900	3,520 3,165
13	Ahold USA** Chantilly, Va. (S, E) 12/30/01	23,212,000	20,949,000	1,285,500	1,101,100	1,430 1,317
14	CVS Corp. Woonsocket, R.I. (DR, E) 12/29/01	22,241,400	20,087,500	413,200	746,000	4,191 4,133
15	Lowe's Cos. Wilkesboro, N.C. (HC, E) 2/1/02	22,111,108	18,778,559	1,023,262	809,871	744 650
16	Best Buy Eden Prairie, Minn. (CE, E) 3/2/02	19,597,000	15,326,552	570,000	395,839	1,896 1,741

* Estimate

** Retail operations only; operating income reported

*** Excludes fuel sales

† Continuing operations

() Loss

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Source: Chain Store Age, "State of the Industry" (August 2002): 3A-8A.

Table 2.8 (continued)

	Company/Headquarters/ Main Retail Segments/ Fiscal Year End	2001 Revenues (000)	2000 Revenues (000)	2001 Profits (000)	2000 Profits (000)	Stores 2001 2000
17	Federated Department Stores Cincinnati (D, C, E) 2/2/02	\$15,651,000	\$16,638,000	\$(276,000)	\$(184,000)	459 440
18	Publix Super Markets Lakeland, Fla. (S) 12/29/01	15,370,019	14,652,741	530,421	530,406	684 647
19	Rite Aid Camp Hill, Pa. (DR) 3/2/02	15,171,146	14,516,865	(761,092)	(1,431,764)	3,497 3,648
20	Delhaize America Salisbury, N.C. (S) 12/31/01	14,900,000	12,700,000	260,656	125,910	1,459 1,420
21	May Department Stores St. Louis (D, AS) 2/2/02	14,215,000	14,372,000	706,000	858,000	839 550
22	Gap Inc. San Francisco (AS, E) 2/2/02	13,847,873	13,673,460	(7,764)	877,497	3,097 2,848
23	Winn-Dixie Jacksonville, Fla. (S) 6/27/01	12,903,373	13,697,547	45,311	(228,895)	1,153 1,079
24	Meijer Grand Rapids, Mich (SC) 12/31/01	11,923,000	11,000,000	NA	NA	155 143
25	Office Depot Delray Beach, Fla (HS, E) 12/29/01	11,200,000	11,569,696	201,000	49,332	1,002 1,020
26	Toys "Я" Us Paramus, N.J. (HS, AS, E) 2/2/02	11,019,000	11,332,000	67,000	404,000	1,599 1,581
27	A&P Montvale, N.J. (S) 2/23/02	10,973,315	10,622,866	(71,906)	(19,500)	702 752
28	Staples Framingham, Mass. (HS, E) 2/2/02	10,744,373	10,673,671	264,970	59,712	1,436 1,307
29	TJX Cos.† Framingham, Mass. (AS, HS) 1/26/02	10,708,998	9,579,006	540,397	538,066	1,665 1,493
30	7-Eleven Dallas (CV) 12/31/01	9,894,100	9,451,100	83,700	108,300	5,829 5,756
31	Circuit City Stores*** Richmond, Va. (HS, E) 2/28/02	9,589,803	10,458,037	217,320	223,144	624 629

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Source: Chain Store Age, "State of the Industry" (August 2002): 3A-8A.

Table 2.8 (continued)

	Company/Headquarters/ Main Retail Segments/ Fiscal Year End	2001 Revenues (000)	2000 Revenues (000)	2001 Profits (000)	2000 Profits (000)	Stores 2001 2000
32	SuperValu** Minneapolis (S) 2/23/02	9,549,068	9,353,992	375,009	301,287	1,260 1,194
33	The Limited Inc.† Columbus, Ohio (AS, C, E, HS) 2/2/02	9,363,000	10,105,000	519,000	428,000	4,614 5,129
34	H. E. Butt Grocery Co. San Antonio (S) 10/28/01	9,000,000	7,900,000	NA	NA	300 277
35	Circle K Tempe, Ariz. (CV) 12/31/01	8,866,440	8,429,850	NA	NA	3,933 3,940
36	Dillard's Little Rock, Ark. (D) 2/2/02	8,154,911	8,566,560	71,798	(5,850)	338 337
37	Kohl's Department Stores Menomonee Falls, Wis. (D) 2/2/02	7,488,654	6,151,996	495,676	372,148	382 320
38	Army & Air Force Exchange Dallas (GM) 2/1/02	7,132,000	7,369,000	373,110	381,436	162 162
39	Gateway North Sioux City, S.D. (E, HS) 12/31/01	6,079,524	9,600,600	1,033,915	241,483	277 327
40	Saks Inc. Birmingham, Ala. (D, E) 2/2/02	6,070,568	6,581,236	322	75,216	356 362
41	Nordstrom Seattle (D, AS, C, E) 1/31/02	5,634,130	5,528,537	124,688	101,918	156 140
42	Dollar General Goodlettsville, Tenn. (DS) 2/1/02	5,322,895	4,550,571	207,513	70,642	5,540 5,000
43	BJ's Wholesale Club Natick, Mass. (WC) 2/3/02	5,279,730	4,932,095	82,348	131,501	130 118
44	Menard Eau Claire, Wis. (HC) 12/31/01	5,200,000	4,850,000	NA	NA	160 150
45	Blockbuster Dallas (HS) 12/31/01	5,156,700	4,960,100	(240,300)	(75,900)	7,981 7,677
46	Barnes & Noble New York City (HS, E) 2/2/02	4,870,390	4,375,804	63,967	(51,996)	1,934 1,886

* Estimate

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Table 2.8 (continued)

	Company/Headquarters/ Main Retail Segments/ Fiscal Year End	2001 Revenues (000)	2000 Revenues (000)	2001 Profits (000)	2000 Profits (000)	Stores 2001 2000
47	AutoZone Memphis, Tenn. (HS) 8/25/01	4,818,185	4,482,696	175,526	267,590	3,040 2,928
48	RadioShack Fort Worth, Texas (HS, E) 12/31/01	4,775,700	4,794,700	291,800	367,400	7,246 7,199
49	OfficeMax Shaker Heights, Ohio (HS, E) 1/26/02	4,636,024	5,133,925	1,086,128	1,220,728	993 995
50	Shaw's Supermarkets** East Bridgewater, Mass. (S) 3/30/02	4,400,000	4,000,000	196,000	171,000	185 185
51	Foot Locker† New York City (SH, AS, HS, C, E) 2/2/02	4,379,000	4,356,000	111,000	107,000	3,590 3,582
52	Giant Eagle Pittsburgh (S) 6/30/02	4,336,000	4,111,000	NA	NA	201 204
53	Longs Drug Stores Walnut Creek, Calif (DR) 1/31/02	4,304,734	4,027,132	47,168	44,884	436 430
54	CompUSA Dallas (HS, E) 12/31/01	4,152,450	5,067,377	NA	NA	226 226
55	Pathmark Stores Carteret, N.J. (S) 2/2/02	3,963,300	3,698,100	(242,000)	198,100	141 138
56	CDW Computer Centers Vernon Hills, Ill. (C, E) 12/31/01	3,961,545	3,842,450	168,700	162,269	2 2
57	QVC** West Chester, Pa. (E) 12/31/01	3,917,300	3,535,900	722,300	619,200	8 8
58	Hy-Vee West Des Moines, Iowa (S) 9/30/01	3,800,000	3,600,000	NA	NA	215 213
59	Family Dollar Stores Matthews, N.C. (DS) 9/1/01	3,665,362	3,132,639	189,505	172,017	4,141 3,689
60	Big Lots Inc.† Columbus, Ohio (DS, E) 2/2/02	3,433,321	3,277,088	(20,234)	(380,652)	1,335 1,290
61	Borders Group Ann Arbor, Mich. (HS, E) 2/27/02	3,387,900	3,271,200	87,400	43,600	1,190 1,204

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Table 2.8 (continued)

	Company/Headquarters/ Main Retail Segments/ Fiscal Year End	2001 Revenues (000)	2000 Revenues (000)	2001 Profits (000)	2000 Profits (000)	Stores 2001 2000
62	ShopKo Stores Inc. Green Bay, Wis. (DS) 2/2/02	3,386,989	3,530,535	28,217	(15,818)	366 393
63	Raley's West Sacramento, Calif. (S) 6/30/02	3,300,000	2,849,000	NA	NA	149 149
64	Ames Department Stores Rocky Hill, Conn. (DS) 2/2/02	3,291,800	4,000,000	240,600	813,100	333 452
65	Sherwin Williams** Cleveland (HS) 12/31/01	3,206,000	3,185,000	390,000	411,000	2,573 2,488
66	Amazon.com Seattle (E) 12/31/01	3,122,433	2,761,983	(567,277)	(1,411,273)	DNA DNA
67	Spiegel Downers Grove, Ill. (C, AS, E) 12/29/01	3,079,000	3,346,000	(17,800)	8,900	607 563
68	Neiman Marcus Group Chestnut Hill, Mass. (D, C, HS) 7/28/01	3,015,500	2,926,400	107,484	134,011	48 47
69	Ross Stores Newark, Calif. (AS, E) 2/2/02	2,986,596	2,709,039	155,045	151,754	452 409
70	Bed Bath & Beyond Union, N.J. (HS, E) 3/2/02	2,927,962	2,396,655	219,599	171,922	396 311
71	Aldi Batavia, Ill. (S) 12/31/01	2,917,200	2,650,000	NA	NA	596 578
72	Payless ShoeSource Topeka, Kan. (SH) 2/2/02	2,913,700	2,948,400	45,400	120,600	4,964 4,912
73	Wegmans Food Markets Rochester, N.Y. (S) 12/31/01	2,900,000	2,800,000	NA	NA	62 60
74	MicroWarehouse Inc.* Norwalk, Conn. (C, E) 12/31/01	2,600,000	2,243,000	NA	NA	DNA DNA
75	Burlington Coat Factory Warehouse Corp. Burlington, N.J. (AS, HS) 6/1/02	2,577,000	2,400,000	NA	71,025	319 295
76	Stater Bros. Markets Colton, Calif. (S, E) 9/30/01	2,573,900	2,417,710	7,800	(6,167)	155 155
77	Michaels Stores Irving, Texas (HS) 2/2/02	2,530,727	2,249,440	89,030	78,589	835 748
78	Advance Auto Parts Roanoke, Va. (HS) 12/29/01	2,517,639	2,288,022	11,442	19,559	2,484 1,681

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Table 2.8 (continued)

	Company/Headquarters/ Main Retail Segments/ Fiscal Year End	2001 Revenues (000)	2000 Revenues (000)	2001 Profits (000)	2000 Profits (000)	Stores 2001 2000
79	PETsMART Phoenix (HS, E) 2/3/02	2,501,012	2,224,222	39,567	(30,904)	560 533
80	Footstar Mahwah, N.J. (SH) 12/29/01	2,460,500	2,237,100	(23,500)	60,400	7,400 3,691
81	Harris-Teeter** Matthews, N.C. (S) 9/30/01	2,416,799	2,332,908	31,800	59,100	137 156
82	Penn Traffic Syracuse, N.Y. (S) 2/2/02	2,404,302	2,413,295	(95,716)	(99,902)	218 220
83	Fleming Cos.** Oklahoma City (S) 12/29/01	2,361,000	3,275,000	57,000	62,000	116 187
84	Value City Columbus, Ohio (DS, SH, AS) 2/2/02	2,283,878	2,213,017	(28,723,000)	(101,791,000)	246 221
85	Whole Foods Market Austin, Texas (S) 9/30/01	2,272,231	1,838,630	67,880	(4,831)	126 117
86	Speedway SuperAmerica LLC*** Enon, Ohio (CV) 12/31/01	2,253,000	2,160,000	NA	NA	2,104 2,148
87	Belk Charlotte, N.C. (D, E) 2/2/02	2,243,151	2,269,695	63,382	57,333	207 207
88	The Pep Boys Philadelphia (HS) 2/2/02	2,183,715	2,418,468	35,335	(51,094)	628 628
89	Williams-Sonoma San Francisco (C, HS, E) 2/3/02	2,096,000	1,829,483	76,100	56,782	415 382
90	Zale Dallas (HS) 7/31/01	2,068,242	1,814,362	82,048	111,514	2,344 1,389
91	Medicine Shoppe International St. Louis (DR) 6/30/01	2,041,000	1,830,000	NA	NA	1,336 1,273
92	Price Chopper/Golub Corp. Schenectady, N.Y. (S) 4/30/02	2,001,000	1,750,000	NA	NA	114 104
93	Schnuck Markets St. Louis (S) 10/31/01	2,000,000	2,100,000	NA	NA	91 92
94	Berkshire Hathaway** Omaha, Neb. (HS) 12/31/01	1,998,000	1,864,000	175,000	175,000	329 310
95	Charming Shoppes Philadelphia (AS, C) 2/2/02	1,993,843	1,607,079	20,104	51,638	2,446 1,754

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Table 2.8 (continued)

	Company/Headquarters/ Main Retail Segments/ Fiscal Year End	2001 Revenues (000)	2000 Revenues (000)	2001 Profits (000)	2000 Profits (000)	Stores 2001 2000
96	Weis Markets Sunbury, Pa. (S, HS) 12/29/01	1,988,246	2,060,976	50,055	73,823	196 196
97	Dollar Tree Chesapeake, Va. (DS) 12/31/01	1,987,321	1,688,105	123,081	120,209	1,975 1,729
98	Navy Exchange Service Command Virginia Beach, Va. (GM) 2/2/02	1,982,337	2,045,402	75,758	76,141	111 113
99	Ingles Markets Asheville, N.C. (S) 9/27/01	1,953,440	1,916,200	17,850	21,091	203 208
100	Smart & Final City of Commerce, Calif. (S, WC) 12,30/01	1,946,723	1,863,895	14,425	11,044	224 230

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Retailers' Growing Power in Marketing Channels

The power and influence of retailers in marketing channels have been growing. This trend follows three major developments: (1) increase in size and buying power, (2) application of advanced technologies, and (3) use of modern marketing strategies.

As discussed earlier, the size of many retailers is increasing due to growth as well as to mergers, acquisitions, and buyouts. Based on the data presented in Table 2.8, there is little question that many retailers are big—even huge—businesses. Since size translates into power, as retailers become larger, their capacity to influence the actions of other channel members (wholesalers and manufacturers) also becomes greater. Most of the manufacturers who supply Wal-Mart, for example, are considerably smaller than Wal-Mart and are hardly in a position to exert a significant influence on Wal-Mart's operating policies. On the contrary, because of Wal-Mart's huge size and buying power, it is in a position to exert considerable influence on its suppliers. Indeed, in many cases Wal-Mart and other giant retailers can literally dictate to manufacturers the terms of sale they want. Department store chains such as Federated Department Stores, Inc. and May Department Stores Co., for example, are in such a powerful position that they can put the squeeze on suppliers to guarantee the department stores' profits on the suppliers' products. If the products do not sell as well as expected and significant markdowns have to be taken, the manufacturers must agree to rebates or discounts on future orders to make up for lost profits.²⁹ Toys "Я" Us, the world's largest toy retailer with over \$12 billion in sales, often gets shipments of hot new toy products from the

29. Laura Bird and Wendy Bounds, "Stores' Demands Squeeze Apparel Companies," *Wall Street Journal* (July 15, 1997): B1, B3.

leading toy makers such as Mattel well in advance of smaller retailers. Home Depot, the world's largest home improvement retailer, has used its power to tell any of its suppliers that had plans to sell their products online directly to consumers to drop that idea or be dropped by Home Depot. Such giant retailers with their enormous buying power, large market shares, and sophisticated managements have been referred to as **power retailers** and **category killers**, terms that convey the dominant positions these retailers enjoy.³⁰

In short, Wal-Mart, Home Depot, Federated and May department stores, Toys "Я" Us, and virtually any of the multibillion-dollar retailers listed in Table 2.8—which in many cases are bigger than the manufacturers that supply them—have the capacity to assume dominant positions in the marketing channel.³¹ This is especially the case for those kinds of retail businesses that are controlled by relatively few firms (refer again to Figure 2.12).

Growing size and concentration of retailers, as discussed on the foregoing pages, is the most fundamental reason for greater retailer power in marketing channels.³² But two other factors are also important. The first is the increased application of **advanced technology** by retailers, and the second is the growing emphasis by retailers on the use of modern marketing strategy.³³

The many technological innovations of recent years have not gone unnoticed by retailers. Indeed, retailers have become astute followers and (more important) ardent users of many new technologies that have made them more sophisticated and demanding channel members. Giants such as Wal-Mart, Home Depot, Target, Costco, Best Buy, Safeway, and numerous others have become world-class in their use of information technology for inventory control and merchandise management as well as supply chain management. But even the "smaller" retailers listed in the bottom 50 of the 100 largest retailers shown in Table 2.8 are using sophisticated information technology to spot slow-moving items and keep them off the shelf as well as to identify hot-selling merchandise so that it is available when and where customers want it. Many of these retailers have also been making better use of their scanner data for promotion and pricing decisions as well as to calculate profits on individual items through direct product profitability (DPP) analysis, shelf management, forecasting, and consumer shopping trip studies.

Perhaps the most exciting technological development being embraced by retailers is their growing use of the Internet to enhance the shopping experience of their customers. While the "pure-play" online retailers such as Amazon.com, which sells all of its product via the Internet, have gotten much of the attention in recent years,³⁴ the real revolution in E-commerce technology is in the way conventional retailers are integrating Internet-based E-commerce with their store and catalog operations. In fact, a new term called **threetailing** has emerged to describe this convergence of in-store, catalog, and online channels. Some retailers, such as JCPenney, are inviting customers to come in (store), call in (catalog), or log on (online) to shop. Circuit City, a large consumer electronics chain, has fully integrated its online capabili-

30. See Zachary Schiller and Wendy Zellner, "Clout! More and More Retail Giants Rule the Marketplace," *Business Week* (December 21, 1992): 66–74.

31. Some large retailers, however, are facing serious challenges. See, for example, "Department Stores Fight to Preserve Role That May Be Outdated," *Wall Street Journal* (March 12, 2002): A1, A17.

32. For some possible exceptions to this pattern, see Roger R. Betancourt and David A. Goutschi, "Distribution Services and Economic Power in a Channel," *Journal of Retailing* (Fall 1998): 37–60; Kisum L. Ailwadi, Norm Boria, and Paul W. Farris, "Market Power and Performance: A Cross-Industry Analysis of Manufacturers and Retailers," *Journal of Retailing* (Fall 1995): 211–248; Paul R. Messinger and Chakravarthi Narasimhan, "Has Power Shifted in the Grocery Channel?" *Marketing Science* 14, no. 2: 189–223.

33. Bert Rosenbloom, "From Merchants to Marketers: Trends in U.S. Retailing for Europe to Watch," *THEXIS* (Spring 2001): 8–11.

34. See Patricia B. Seybold, *Customers.com* (New York: Random House, 1998); John Hagel III and Marc Singer, *Net Worth* (Boston, MA: Harvard Business School Press, 1999).

ties with its retail operations so that consumers can order online from the firm's extensive website and then pick up the product in the store. And if they want to return it, they can bring it back to the store.

These are, of course, just a small sample of the technologies being used by retailers, but they are indicative of the role of technology in increasing their capabilities and, in turn, their power in the marketing channel. We will examine technology as it affects marketing channels in greater detail in Chapter 3.

Turning now to retailers' growing emphasis on marketing, a fundamental change has been the evolution in thinking by leading retailers about the application of marketing strategy in a retail setting.³⁵ Retailers have traditionally been more supplier (vendor) driven than market driven. In recent years, however, more retailers are discovering the power of modern marketing methods for surviving and prospering in fiercely competitive retail markets. Indeed, some retailers now rival the best of the major U.S. consumer packaged goods manufacturers in the application of marketing strategies.

Consider, for example, the case of Blockbuster Video, the world's largest video store chain. Blockbuster has used marketing methods such as market segmentation and customer profiling at a level of sophistication that has astounded skeptics who thought retailers were still in the "dark ages" of marketing. Blockbuster's fully computerized marketing information system enables the firm to track its customer base for each of its thousands of stores throughout the world. The system provides complete and timely data for precise target marketing. For example, the system will automatically track customers who have a particular liking for a category of titles such as horror films, James Bond films, westerns, oldies, comedies, and so forth, and automatically sends them promotional flyers about new stock or new releases in those categories. Moreover, the system balances the inventory mix of customer demand in the trade area served by each store. Thus, even though Blockbuster is a giant international retail chain with more than 7,500 stores, each of its stores mirrors the localized desires of its customers better than the local independent video stores that are attempting to compete with Blockbuster.

Some category killer-type retailers, such as CompUSA with over \$6 billion in sales and 200-plus superstores, have used **relationship marketing** by emphasizing customer training and service to build long-term relationships with customers.

Medium-sized and smaller stores have become as adept as giant retailers at using marketing strategy to attract and sustain enthusiastic and loyal customers. For example, Kohl's, one of the fastest-growing discount department stores in the U.S., has managed to differentiate itself from the pack by stressing a radically different store layout compared with its competitors. Kohl's uses what it refers to as a "racetrack" layout, designed to expose customers to the maximum amount of merchandise in the shortest time. Rather than walk up and down aisles, shoppers circle around the merchandise as they move through the store. Though they spend less time in the store, they buy more merchandise. This flies in the face of conventional retailing layout theory, which is based on the assumption that the more time customers spend in the store, the more merchandise they will purchase. All the manufacturers of the brand name apparel that Kohl's sells are eager to please this astute and fast-growing retailer.

Even relatively small retailers such as Fresh Market Incorporated, a family-owned 30-store supermarket chain, can become a force in the marketing channel through adept use of marketing strategy. Fresh Market has been recognized in the super-competitive supermarket arena as a leader in using market segmentation to zero in on its target market—educated high-income consumers in upscale neighborhoods. Fresh Market's stores are 18,000

35. Bert Rosenbloom and Marc Dupuis, "Low Price, Low Cost, High Service: A New Paradigm for Global Retailing?" *The International Review of Retail Distribution and Consumer Research* (April 1994): 149–158.

square feet (compared to the typical 40,000 square feet of U.S. supermarkets) and feature warm lighting, classical background music, and elegant décor to create the kind of shopping environment sought by the well-heeled market segment the store is targeting. The results have been spectacular. Fresh Market has enjoyed a same-store sales growth rate of over 9 percent, compared with the 2 percent rate of mass-market supermarkets. Even giant suppliers in the marketing channel have learned to respect Fresh Market's considerable marketing expertise and are eager to get and keep their products on this posh supermarket's shelves.

To sum up, retailers in the United States have become much larger and more concentrated, more technologically adept, and more sophisticated marketers. As a result, they have become far more powerful members of marketing channels and indeed have come to dominate many of the marketing channels in which they participate. In short, retailers are now the "gate-keepers" into consumer markets.³⁶

From the suppliers' perspective, both at the producer and wholesaler levels, the implications of the retailers' new position are potentially ominous. To an increasing extent their basic marketing strategies in the areas of product planning and development, pricing, and promotion will be constrained and even shaped by the considerable demands of a powerful retail sector. Those suppliers that are not able to adjust to this new reality will have a difficult if not impossible task in gaining access to consumer markets.

Distribution Tasks Performed by Retailers

The role of retailers in performing distribution tasks is summarized very succinctly in a classic statement by Charles Y. Lazarus:

The role of the retailer in the distribution channel, regardless of his size or type, is to interpret the demands of his customers and to find and stock the goods these customers want, when they want them, and in the way they want them. This adds up to having the right assortments at the time customers are ready to buy.³⁷

Elaborating on Lazarus's list, we may specify the distribution tasks for which retailers are especially well suited, as follows:

1. Offering manpower and physical facilities that enable producers/ manufacturers and wholesalers to have many points of contact with consumers close to their places of residence
2. Providing personal selling, advertising, and display to aid in selling suppliers' products
3. Interpreting consumer demand and relaying this information back through the channel
4. Dividing large quantities into consumer-sized lots, thereby providing economies for suppliers (by accepting relatively large shipments) and convenience for consumers
5. Offering storage, so that suppliers can have widely dispersed inventories of their products at low cost and enabling consumers to have close access to the products of producers/manufacturers and wholesalers
6. Removing substantial risk from the producer/manufacturer (or wholesaler) by ordering and accepting delivery in advance of the season

36. Bert Rosenbloom and Diane Mollenkopf, "Dominant Buyers: Are They Changing the Wholesalers' Role in Marketing Channels?" *Journal of Marketing Channels* (Fall 1993): 73–89.

37. Charles Y. Lazarus, "The Retailer as a Link in the Distribution Channel," *Business Horizons* (February 1961): 95–98.

The level at which retailers perform these distribution tasks varies enormously across the spectrum of retailing, from an all-out effort to do everything to a “bare bones” level of doing little.

Nordstrom, a West Coast–based chain of 140 department stores, is an excellent example of a retailer that puts forth all-out effort for its customers. In fact, this retailer has become famous for providing the highest level of service at the retail level. At Nordstrom, stocking the stores perfectly with highly desirable assortments of merchandise in impeccable surroundings and selling it through knowledgeable and helpful salespeople is only the beginning. Salespeople also gift wrap packages at no extra charge and drop off orders at customers’ homes. Piano players serenade shoppers year-round. In Alaska, Nordstrom employees have been known to warm up cars while drivers spend a little more time shopping. There is even a story about a customer who got his money back on a tire even though Nordstrom does not sell tires! Nordstrom was simply attempting to live up to its no-questions-asked returns policy.

At the other end of the spectrum of retail service levels are off-price retailers such as Marshalls, an apparel chain that stocks an unpredictable assortment of merchandise, in spartan surroundings, with no personal service and often long checkout lines. In the middle range are retailers such as Target, a chain of more than 1,300 discount department stores that has some of the ambience of upscale department stores and carries merchandise that is chic and fashionable, yet priced well below what conventional department stores charge. Although there is little sales help, store signage is excellent and wide aisles, attractive displays, and short checkout lines create a different and better shopping experience than what customers would ordinarily expect from a discount mass merchandiser.

In essence then, each retail channel member makes its own decisions about how it will approach the performance of distribution tasks. But to remain a viable member of the marketing channel, each must offer something of value to its customers as well as its suppliers.³⁸ If it fails to do so, existing competitive retailers, other channel members, or new forms of channel institutions will be only too happy to take its place in the marketing channel.³⁹

The growing size of retailers, discussed earlier, has also affected the allocation of distribution tasks among the channel members. Specifically, distribution tasks that were formerly the province of the wholesaler or manufacturer have increasingly been taken over by the large-scale retailer. For example, most large chain store organizations and department stores have their own modern warehousing facilities enabling them to perform storage and order processing tasks very efficiently. This in turn has reduced their use of merchant wholesaler intermediaries to a very marginal level. Voluntary associations of retailers—such as retailer cooperatives, wholesaler-initiated voluntary chains, and franchise systems—have also grown, enabling many of these organizations to rival the scale economies of the corporate chains.⁴⁰ Even single-unit independent retail stores have, on average, grown larger, utilized more modern facilities and equipment, and performed distribution tasks more efficiently.

This poses a dilemma for the producer or manufacturer. On the one hand, the potential of retail intermediaries to perform distribution tasks effectively and efficiently has increased. But on the other hand, the larger scale of retailers has increased their power and independence, and hence they are less easily influenced by the producer or manufacturer.⁴¹ This

38. Joann Muller, “Attention Kmart: Find A Niche,” *Business Week* (February 4, 2002): 72.

39. See, for example, Roger Dickinson and Bixby Cooper, “The Emergence of Cost-Based Strategies in Retailing,” *Journal of Marketing Channels* 2, no. 1 (1992): 29–45. Also, for an excellent and comprehensive review of institutional changes in retailing, see Stephen Brown, “Institutional Change in Retailing: A Review and Synthesis,” *European Journal of Marketing* 21 (1987): 5–36.

40. See, for example, Carl Quintanilla, “Hardware Stores Try to Rattle Big Chains,” *Wall Street Journal* (December 11, 1996): B1, B4.

41. Philip McVey, “Are Channels of Distribution What the Textbooks Say?” *Journal of Marketing* (January 1960): 61–65.

means that the channel manager in the producing or manufacturing firm will face both increased opportunities and greater difficulties in the course of using retailers in the channel of distribution. This will place an especially high premium on effective channel management.

Facilitating Agencies

Facilitating agencies are business firms that assist in the performance of distribution tasks other than buying, selling, and transferring title. From the standpoint of the channel manager, they may be viewed as subcontractors to whom various distribution tasks can be “farmed out,” based on the principle of specialization and division of labor. By properly allocating distribution tasks to facilitating agencies, the channel manager will have an ancillary structure that is an efficient mechanism for carrying out the firm’s distribution objectives. Here are some of the more common types of facilitating agencies:

- » **Transportation agencies** include all firms offering transportation service on a public basis, such as United Parcel Service (UPS) and Federal Express. Because of great economies of scale and scope, these and other common carriers are able to perform transportation services far more efficiently and cost-effectively than manufacturers, wholesalers, or retailers.
- » **Storage agencies** consist mainly of public warehouses that specialize in the storage of goods on a fee basis. Many of these firms provide great flexibility in performing the storage tasks. For example, in some instances the goods of a channel member (producers/manufacturers, wholesalers, or retailers) are not physically stored in the warehousing firm’s facilities, but rather in the channel member’s own facilities. Under this so-called field warehousing arrangement, the warehousing agency locks up the goods and issues a receipt, which often serves as collateral on a loan taken by the channel member.
- » **Order processing agencies** are firms that specialize in order fulfillment tasks. They relieve manufacturers, wholesalers, or retailers from some or all of the tasks of processing orders for shipment to customers. For example, Catalog Resources Inc., based in Dover, Delaware, handles the order processing for the catalog sales of Laura Ashley, Caswell-Massey, Winterthur, and Hallmark Cards, thus relieving these firms of the “nuts and bolts” involved in processing customers’ orders themselves.
- » **Advertising agencies** offer the channel member expertise in developing promotion strategy. This can range from providing a small amount of assistance in writing an ad to complete design and execution of the advertising campaign.
- » **Financial agencies** consist of firms such as banks, finance companies, and factors that specialize in discounting accounts receivable. Common to all of these firms is that they possess the financial resources and expertise that the channel manager often lacks.
- » **Insurance companies** provide the channel manager with a means for shifting some of the risks inherent in any business venture, such as fire and theft losses, damage in transit of goods, and in some cases even inclement weather.
- » **Marketing research firms** have grown substantially in the past 20 years. Most large cities now have a number of marketing research firms offering a wide range of skills. The channel manager can call on these firms to provide information when his or her own firm lacks the necessary skills to obtain marketing information relevant to distribution.

Some facilitating agencies have become especially innovative in helping channel members with various distribution tasks. A case in point is Distribution Centers Inc. (DCI), a pub-

lic warehousing firm that helped Lever Brothers, one of the world's largest manufacturers of soaps and detergents, solve a serious distribution problem. Lever Brothers had a problem common to all manufacturers of laundry soaps and detergents—large numbers of boxes of these products became torn or dented in transit. These boxes could not be sold in supermarkets, and the cost and effort to return them for repackaging was not economically feasible. DCI solved Lever Brothers' problem by offering its facility in St. Louis to serve as a collecting point for damaged boxes from all over the country. When the St. Louis warehouse receives damaged boxes, they are transferred into large drums that are shipped back to a Lever Brothers manufacturing facility on a regular basis. These recovered products are not sold for household use, but Lever Brothers is able to sell them profitably for industrial applications.

As this example suggests, the potential of facilitating agencies for going beyond their traditional or routine role in the performance of distribution tasks to provide new kinds of services can significantly enhance their value to members at all levels of the marketing channel.



SUMMARY

Many different types of parties participate in the marketing channel. Some are considered to be members while other participants are nonmembers. The former perform negotiatory functions and participate in the flows of negotiation and/or ownership while the latter participants do not. Although final users (target markets) are members of the marketing channel, they are excluded from the commercial channel, which by definition excludes final users.

Producers and manufacturers consist of firms that are involved in extracting, growing, or making products. Though the range of types and sizes of producing and manufacturing firms is enormous, all are faced with the common task of distributing their products to their intended users. Many producers and manufacturers, however, lack the expertise and economies of scale and scope to distribute their products directly to their final users. Hence, in most cases it is difficult and inefficient for manufacturers to distribute their products directly to final users. They often call on intermediaries at the wholesale and/or retail levels as well as facilitating agencies to share in the performance of the distribution tasks.

Wholesalers consist of businesses that are engaged in selling goods for resale or business use to retail, industrial, commercial, institutional, professional, or agricultural firms or organizations, as well as to other wholesalers. Wholesalers are classified into three basic types: (1) merchant wholesalers; (2) agents, brokers, and commission merchants; and (3) manufacturers' sales branches and offices. The first two are independent intermediaries, while the third is owned by the manufacturer. Most wholesalers are relatively small businesses, and the level of economic concentration in wholesaling is generally quite low but it is increasing.

Merchant wholesalers are especially well suited for performing distribution tasks for producers or manufacturers such as providing market coverage, making sales contacts, holding inventory, processing orders, gathering market information, and offering customer support. For their customers, merchant wholesalers are equally well suited to efficiently perform such distribution tasks as assuring product availability, providing customer service, extending credit and financial assistance, offering assortment convenience, breaking bulk, and helping customers with advice and technical support.

Agent wholesalers as a rule do not perform as many distribution tasks as merchant wholesalers. However, the range varies greatly from performance of most tasks at a level similar to that of merchant wholesalers to far less. Moreover, the names given to various agent wholesalers—such as manufacturers' representative, selling agent, sales agent, rep, broker, and so

on—are generally not accurate guides as to the level of distribution tasks performed by each category.

Retailers consist of businesses engaged primarily in selling merchandise for personal or household consumption and rendering services incidental to the sale of the goods. Retailers comprise an extremely diverse group in both type and size. The *Census of Retail Trade* classifies retailers into different kind-of-business categories to provide some degree of order to this great diversity. Retail firms have been steadily growing larger over the past three decades and the level of economic concentration has become relatively high. Retailers are particularly well suited for performing such distribution tasks as:

- » Offering manpower and physical facilities that enable producers, manufacturers, and wholesalers to have many points of contact with consumers
- » Providing personal selling, advertising, and display to sell suppliers' products
- » Interpreting consumer demand and relaying it through the channel
- » Dividing large quantities of products into consumer-sized lots
- » Offering storage close to points of consumer contact
- » Reducing risks of producers, manufacturers, and wholesalers by accepting delivery of merchandise in advance of the selling season

As retailers continue to grow larger and more technologically sophisticated, and as more of them embrace modern marketing strategy, their role in the marketing channel will become an even more independent and dominant one. This will pose an increasing challenge to channel management in producing and manufacturing firms.

Facilitating agencies such as transportation companies, storage firms, order-processing firms, advertising agencies, financial institutions, insurers, and marketing researchers, while not members of the marketing channel, are still called upon frequently by any or all of the channel members to help perform many different distribution tasks.

Review Questions

1. Explain the classification scheme of the channel participants shown in Figure 2.1.
2. Expertise and economies of scale in production do not automatically translate into expertise and economies of scale and/or scope in distribution. Discuss this statement.
3. Why do you suppose the average costs of performing many distribution tasks are lower for intermediaries and facilitating agencies than for producers and manufacturers?
4. How does the *Census of Wholesale Trade* classify wholesale intermediaries?
5. Contrary to some prophecies, wholesalers have not died out. What has happened to wholesalers in recent years?
6. Discuss the basic trends over the past 30 years with regard to total wholesale sales for (a) merchant wholesalers, (b) manufacturers' sales branches and offices, and (c) agents, brokers, and commission merchants.

7. Describe the distribution tasks that wholesalers are especially well suited for performing.
8. The average size of retail units (as measured by sales volume) has been increasing. What are some of the implications of this trend for channel management in producing and manufacturing firms?
9. Describe the distribution tasks that retailers are especially well suited for performing.
10. Discuss retailers' growing power in the marketing channel in terms of the possible implications for channel management.

Issues for Discussion

1. Wrigley is the world's leading manufacturer of chewing gum, producing literally millions of packages of gum every day. Its manufacturing technology for producing gum is state-of-the-art, and it is a large and financially strong company. It sells its products to millions of gum-chewing consumers all over the United States and many other countries around the world. Still, Wrigley has never attempted to sell its chewing gum directly to consumers, but instead uses a wide variety of intermediaries at the wholesale and retail levels.

Why do you suppose Wrigley has chosen to use intermediaries rather than sell direct to consumers? Explain the underlying economics of the company's policy.

2. The *Census of Wholesale Trade* and the *Census of Retail Trade* are published every five years by the Department of Commerce. The most recent census was taken in 1997 and the one before that was in 1992—however, the actual findings from the census are not made available until two and one-half to three years later. Thus the findings from the 1992 census did not appear until 1995, and the 1997 census did not appear until the year 2000.

How serious a problem do you think this is in terms of the timeliness of information provided by the census?

3. W. W. Grainger, headquartered in Skokie, Illinois, is one of the nation's largest wholesalers, with more than 300 branch locations. The company sells mainly industrial products such as electric motors, fans, blowers, air compressors, power transmission equipment, and thousands of different components and replacement parts. Inventories and order processing are managed with advanced computer systems. Grainger buys products from about 2,000 manufacturers and resells them to more than 920,000 customers. The principal means by which Grainger competes, according to the company's top management, is by offering such extras as wide availability of local stocks, outside salespeople, and customer

service. Grainger has also put its complete catalog online so that customers have the option of visiting the company's Web site to place their orders.

In a fundamental sense, is giant W. W. Grainger different from the host of mostly much smaller wholesalers in any other line of trade? Discuss in terms of the set of distribution tasks presented in the chapter.

4. Fleming Companies is the largest grocery wholesaler in the United States. But Fleming may be catering to a dying breed—small independent grocers. As an intermediary between grocery stores that are too small to have their own warehouses and large manufacturers who prefer to deal directly with giant retailers, Fleming's future growth seems in doubt, while a shrinking of its present size seems more likely.

Does such a scenario necessarily have to occur? Discuss a scenario that might be more likely to result in growth rather than shrinkage for Fleming.

5. Office Depot, the giant office products retailer with sales in excess of \$10 billion, is seeking to distance itself from similar office products giants Staples and Office Max. It is experimenting with an online finance center that will offer Office Depot's vast number of small business customers instant access to sources of business finance. The company believes that this capability will get customers to think of Office Depot not just as another office supply retailer but as a valuable resource to supply a crucial service to small business—easy and convenient access to financing. Customers can visit Office Depot stores, use the company's catalog, or go online not only to shop for paper clips and print cartridges but for the best loan deals as well.

How might this differentiation strategy being tried by Office Depot affect its role in the marketing channel?

6. Home Depot is the world's largest chain of home centers, with sales of more than \$40 billion and over 1,200 giant stores across the United States. Besides offering a huge array of building materials, hardware, electrical supplies, plumbing fixtures, and gardening supplies, Home Depot prides itself on offering excellent customer service. Home Depot's sales staff, many of whom were former tradespeople such as carpenters or electricians, are carefully trained by Home Depot. All new sales employees go through a five-day training seminar on everything from how to greet customers to how to help customers make sure they have all the products they need for the projects they are working on. Home Depot uses the latest computer technology to manage its merchandise and control inventory and has built its reputation as an astute marketer to almost legendary levels among retailers. Indeed, no less an authority than David Glass, the president of Wal-Mart, says that Home Depot is the best-managed retailer in the country.

How has the emergence of large-scale, technologically sophisticated, and marketing-oriented retailers such as Home Depot changed the retailer's role in

the marketing channel? What are the major implications of these changes for manufacturers and customers?

7. Web fulfillment companies may start a new trend in online retailing. These firms allow conventional retailers to operate their online divisions without the expense and hassle of developing and running their own E-commerce operations. Global Sports Inc., for example, handles Web site design, order fulfillment, and customer service for retailers who do not want to perform these distribution tasks themselves. Major retailers such as Dick's, Modell Sporting Goods, QVC, and Kmart have already outsourced their online business to Global Sports. As far as customers know, when they visit the Web site they are dealing only with the retailer. The Web fulfillment company stays completely behind the scenes. So, with almost no capital or human resources invested, retailers can still have a first-rate Web site as well as online sales and service capabilities. The catch is that the Web fulfillment company gets to keep as much as 90 percent of online revenue. But on the other hand, the 10 percent that goes to the retailer is virtually pure profit.

Do arrangements such as these make sense? What are the advantages and disadvantages from the retailer's point of view?