



INDUSTRIAL AND ORGANIZATIONAL MARKETING

MICHAEL H. MORRIS

INDUSTRIAL AND ORGANIZATIONAL MARKETING

MICHAEL H. MORRIS

University of Central Florida

Merrill Publishing Company
A Bell & Howell Information Company
Columbus Toronto London Melbourne

Published by Merrill Publishing Company
A Bell & Howell Information Company
Columbus, Ohio 43216

This book was set in Garamond

Administrative Editor: Pam Kusma
Production Coordinator: Rex Davidson
Art Coordinator: James H. Hubbard
Copyeditor: H. E. B. Anderson
Cover Designer: Cathy Watterson

Copyright © 1988 by Merrill Publishing Company. All rights reserved. No part of this book may be reproduced in any form, electronic or mechanical, including photocopy, recording, or any information storage and retrieval system, without permission in writing from the publisher. "Merrill Publishing Company" and "Merrill" are registered trademarks of Merrill Publishing Company.

Library of Congress Catalog Card Number: 87-61944
International Standard Book Number: 0-675-20519-0
Printed in the United States of America
1 2 3 4 5 6 7 8 9—92 91 90 89 88

*To my wife, Lois,
and my saintly mother*

PREFACE

The discipline of marketing has grown in many diverse directions over the past two decades. There are now courses, seminars, books, and journals devoted to high-tech marketing, nonprofit marketing, social marketing, international marketing, sports marketing, health care marketing, and financial services marketing, among others. Many of these represent new fields, or new applications of marketing. One of the most rapidly growing areas, however, is the field of industrial marketing, or marketing to organizations. This is an interesting development, because industrial marketing has been around for quite a long time. Yet, many business schools have only recently added industrial marketing courses, and some have yet to create such a course.

Why has industrial marketing come of age? One of the leading reasons involves industrial companies themselves. Marketing has traditionally been underemphasized by the managers of these firms, while technical and production-related concerns have received priority. Marketing was equated with personal selling and sales promotion. But the challenges and opportunities confronting these organizations have undergone great change in recent times, and with this has come a general recognition of the important contributions modern marketing has to offer.

These times are exciting for those who work with industrial products/services and markets. The rate of new product and service introduction is high, as companies rush to implement the latest technologies. Entirely new markets are appearing and old ones are being redefined. Meanwhile, industrial firms are devoting more resources to finding customers, studying customer needs, communicating with customers, and keeping customers satisfied. Many are creating marketing departments, appointing marketing vice-presidents, developing marketing plans, and implementing marketing strategies. At the same time, new concepts and tools are being developed to aid the efforts of the industrial marketer.

The purposes of this book are threefold: to provide an introduction to the distinctive nature of the marketing task when the customer is an organization; to provide an appreciation for the growing role of marketing within industrial companies; and, to provide insights into ways in which a number of marketing principles, concepts, and techniques can be used by the industrial marketing manager. The book is intended for undergraduate students who have completed at least a basic

marketing principles course, as well as for M.B.A. students with some background in marketing.

ORGANIZATION

The book is structured around five major sections, and includes fourteen chapters and nineteen case studies. The five sections represent the rudiments of the marketing management process.

Part I introduces the reader to industrial marketing. The marketing philosophy is explained as it relates to the rapidly changing environment of industrial firms. Differences between consumer and industrial marketing are analyzed. Detailed attention is given to the nature of industrial products and markets, including international markets, and an overview of the procurement practices of organizations is presented.

Part II focuses on how to examine or analyze the industrial marketplace. This includes a detailed assessment of organizational buying behavior, industrial marketing research, demand analysis (including sales forecasting), and market segmentation. The abilities and insights of the marketer in each of these four areas often represent the difference between market success and failure, because they determine his or her ability to identify and serve customer needs.

Part III investigates the development of marketing strategies and tactics. Each component of the marketing mix is covered. Separate chapters are devoted to strategic marketing, product development, pricing, advertising, personal selling, and distribution. Importantly, these chapters build on the market analysis foundation established in Part II.

Part IV discusses the need to monitor, evaluate, and adjust marketing programs after they have been implemented. A number of problems and approaches are reviewed. Also included here are some of the ethical issues that industrial marketers continually face in managing the marketing mix.

The final section, Part V, consists of a variety of case studies. These cases require the student to analyze actual company situations and develop marketing solutions that address the opportunities and/or threats confronting the firms.

Rather than simply focus on identifying, defining, and providing examples of key concepts, this text attempts to integrate these concepts into a logical managerial process. A process approach is used to explain many of the major subject areas, including buyer behavior, marketing research, segmentation, strategic planning, product development, pricing, advertising, sales management, distribution channel management, and control. Approaching the management of such key areas as a process provides the student with a practical framework that can then be applied to industrial products, markets, and firms of all types in the real world.

HIGHLIGHTS

Some of the distinctive features of *Industrial and Organizational Marketing* include the following:

A detailed and systematic breakdown of how industrial markets differ from consumer markets, including a mini-situation that challenges students to cite the differences;

treatment of some of the newer technological developments in organizational purchasing and production, including just-in-time inventory, electronic data interchange, materials requirement planning, and flexible manufacturing systems;

two comprehensive chapters on the buying behavior of the industrial customer, including an extensive treatment of the buying center concept and simplified versions of the leading buying models;

a discussion of marketing intelligence systems and decision support systems as they relate to the traditional marketing research function in organizations;

a cost-benefit method for segmenting markets and targeting customers, based on a comprehensive set of managerial criteria;

a separate chapter devoted to industrial marketing strategy, types of strategies, and the meaning of a *strategic orientation* for industrial firms;

an examination of the role of marketing in corporate entrepreneurship;

contribution analysis as a marketing tool is stressed throughout the book, encouraging students to incorporate profit considerations in their analyses of marketing decisions;

a value-based approach to pricing; extended discussion of probabilistic bidding and transfer pricing;

emphasis on the two-way dyadic relationship in sales management;

detailed treatment of the importance of marketing control, and of techniques which can be used to monitor marketing performance, including spreadsheets;

nineteen real-life cases covering a wide range of products (including high-tech and defense-related) and services, and a variety of markets (including governmental, nonprofit, and international).

Also, the book includes chapter-by-chapter objectives, chapter summaries, end-of-chapter discussion questions, and an index of names as well as a subject index. Most chapters contain two or three exhibits that include real examples of successful marketing practices, examples of industrial advertisements or promotional materials, and summaries of the findings of major research projects on industrial marketing-related issues.

ACKNOWLEDGEMENTS

The author would like to thank all those who made this project a reality. Chief among these are Gordon Paul and Al Burns, both of the University of Central Florida, whose encouragement and helpful insights substantially improved the text. Much appreciation also goes to the case contributors, especially Roger Calantone and Tony di Benedetto of the University of Kentucky, who coordinated most of the case sec-

tion. A number of reviewers made invaluable suggestions for revisions and additions, including P. Renee Foster, Delta State University; Robert R. Harmon, Portland State University; Dr. Jon Hawes, University of Akron; Richard Hise, Texas A & M University; C. Boyd Johnson, Central Washington University; Ramnath Lakshmi-Ratan; University of Wisconsin-Madison; Michael J. Messina, Gannon University; Dr. Charles O'Neal, University of Evansville; David Reid, Clarkson University; Marti J. Rhea, North Texas State University; John K. Ryans, Jr., Kent State University; William A. Staples, University of Houston–Clear Lake; Joe W. Thompson, Michigan State University; Lewis R. Tucker, University of Hartford; Wayland E. Vaughn, Slippery Rock University; and Gary G. Young, University of Massachusetts-Boston.

Finally, personal thanks to Joy Tatlonghari, Ceceile Lindo, Nathelle Gross, Jeanne Holman, Karla DeSousa, and Sarah Gorman for their many hours of high quality word processing and research assistance.

CONTENTS

PART I: INTRODUCTION	1
Chapter 1: The Basics of Industrial Marketing	3
Introduction	4
Defining Industrial Marketing	4
Customer Needs as the Driving Force	6
The Industrial Marketing Mix	6
Why Study Industrial Marketing?	7
The Size of the Industrial Market Growth Markets of Today and Tomorrow	
The External Environment of Industrial Firms	14
Technological Environment Customer Environment Competitive Environment Legal/Regulatory Environment Economic Environment	
Distinctive Aspects of Industrial Marketing	21
Product Characteristics The Nature of Demand Buyer Behavior Communication Processes Economic/Financial Factors	
Where Are We Going From Here?	28
Summary	30
Chapter 2: Industrial Markets, Products, and Purchasing Practices	33
The Nature of Industrial Markets	34
Commercial Enterprises Institutional Markets Government Markets	
The International Industrial Market	47
The Nature of Industrial Products	51
The Purchasing Function	54
Purchasing Procedures Organizing the Purchasing Operation	
Key Analytical Tools in Purchasing Industrial Goods	61
Life Cycle Costing Value Analysis Time-Based Buying Strategies Just-in-Time Inventory Materials Requirement Planning	
Summary	69

PART II: EXAMINING INDUSTRIAL MARKETS 73

Chapter 3: Marketing to the Organizational Customer 75

Marketing Starts with the Buyer	76
Selling to Organizations	77
Technical, Commercial, and Behavioral Complexities	78
The Industrial Marketer's Lament: Who Buys?	80
Internal and External Publics	81
Is Industrial Buying Rational?	83
Buying as a Process: The Buystages	86
Buying Scenarios	91
The Buygrid	92
Purchasing as Mutual Problem Solving	94
The Dyadic Approach	96
Summary	98

Chapter 4: Concepts and Models of Organizational Buying Behavior 101

Introduction	102
The Buying Center	102
A Communications Perspective A Power Perspective A Risk Perspective A Problem-Solving Perspective A Reward Perspective	
Two General Frameworks	113
The Webster-Wind Framework The Sheth Framework Limitations of the Frameworks Source Loyalty as an Outcome of Buyer Behavior	
Summary	128

Chapter 5: Industrial Marketing Research and Intelligence 130

The Role of Information in Marketing Decisions	131
When Not to Do Research	132
Major Responsibility Areas of Marketing Research	133
Development of Market Potential Market Share Analysis Determination of Market Characteristics and Attitudes Sales Analysis Forecasting Studies of Business Trends New Product Acceptance and Potential Competitor Analysis Determination of Sales Quotas and Territories	
Marketing Research as a Process	136
Describing the Steps in the Process	138
Problem Recognition and Definition Specify the Study Objectives Establish the Study Hypothesis Identify Information Needed Secondary Data Search Develop the Research Design, Including Sampling Strategy Determine the Method of Data Collection Develop the Questionnaire Data Collection Data Analysis Interpretation and Presentation	
Are There Differences Between Industrial and Consumer Market Research?	143

From Marketing Research to Marketing Intelligence	146
Steps in Establishing and Operating an MIS	149
From Intelligence to Decision Support	152
Use of Secondary Data Sources in Industrial Marketing Intelligence	153
Internal Secondary Data Sources External Secondary Data Sources General Business Indices Government Sources Commercial Sources Secondary Data and the SIC System Problems with Secondary Data Trends in Industrial Marketing and Intelligence Systems	
Summary	162

Chapter 6: Assessing Markets: Demand Measurement and Sales Forecasting

165

Introduction	166
Basic Concepts in Examining Industrial Demand	166
Types of Market Potential The Company Sales Forecast Customer Budgets Assumptions Market Response Curves	
Special Characteristics of Industrial Demand	172
The Derived Nature of Demand Concentrated Demand Source Loyalty Price Bidding for Capital Equipment	
The Uses of Demand Analysis	173
Demand Estimation and Marketing Planning Demand Estimation and Control of Industrial Marketing Efforts Demand Estimation and New Product Development	
Basic Options When Selecting Demand Analysis Techniques	180
Qualitative versus Quantitative Techniques: How Much Judgment? Breakdown versus Build-up Methods: Where to Begin? Internal versus External Sources: Where to Get the Data? Assumptions: Simple versus Complex?	
Commonly Used Techniques in Estimating Market Potential	182
Chain-Ratio Method of Market Measurement Statistical Series Method of Market Measurement	
Commonly Used Techniques in Forecasting Sales	185
Qualitative Approaches Quantitative Approaches Resolving the <i>Final</i> Sales Forecast	
Summary	195

Chapter 7: Industrial Market Segmentation

198

Introduction	199
Defining Market Segmentation	199
An Example of Market Segmentation	200
The Process of Segmentation	201
Identify Relevant Market Segmentation Bases Determine Homogeneous Groupings Evaluate the Attractiveness of Each Market Segment Select Target Market(s) Align the Marketing Strategy to Market Segment(s) Implement and Monitor	
Degrees of Segmentation	205

What Segmentation Does For the Industrial Marketer	206
Decision Criteria in Market Selection and Targeting	206
Criteria for the Usefulness of Market Segmentation Criteria for the Selection of Target Markets Criteria for the Allocation of Resources Applying the Criteria: The Cost-Benefit Perspective	
Methods and Bases for Segmenting Industrial Markets	214
The Macro and Micro Approach Intermediate Bases: The Nested Approach A Dynamic Cost-Benefit/Nested Approach to Industrial Market Segmentation	
Summary	222

PART III: INDUSTRIAL MARKETING MANAGEMENT FUNCTIONS 225

Chapter 8: Strategic Management of Industrial Products and Services 227

The Concept of Strategy	228
Strategies versus Tactics	230
Types of Marketing Strategies	231
Strategic Marketing Management	234
The Strategic Planning Process	234
A Case Example of the Need for Strategic Planning Pitfalls of Strategic Planning	
Conceptual Planning Tools	241
Product Life Cycle Product Portfolios Business Screens Alternative Portfolio Approaches Experience Curves/Economies of Scale Technology Life Cycles	
The Role of the Product in Industrial Marketing Strategy	253
Products: Items, Lines, and Mixes	255
Depth and Breadth	256
Positioning the Line	257
Industrial Product Elimination	258
Summary	260

Chapter 9: Marketing and Product Innovation 263

The Importance of New Products	264
Types of Innovative Product Activity	265
Risks and Dangers in Product Innovation	267
Why Do New Industrial Products Fail?	268
Dimensions of Success	270
The Product Innovation Charter	271
Product Innovation as a Process	275
Idea Generation and Screening Concept Testing Technical Feasibility Analysis and Product Testing Profitability Analysis Test Marketing Market Launch and Life Cycle Management	
Organizing for New Products	284

The Marketing—R&D Interface	288
Corporate Entrepreneurship	290
Marketing as the Home for the Entrepreneurial Process	291
Summary	292

Chapter 10: Industrial Pricing **295**

Complications and the Utilization of Price	296
Price as a Measure of Value	298
Economic Value to the Customer (EVC)	
A Framework for Setting Industrial Prices	300
Setting Price Objectives Examining Costs Assessing Demand Analyzing the Competition Putting the Four Together	
Pricing Over the Life Cycle	319
Special Topics in Industrial Pricing	321
The Role of Discounts and Incentives Leasing Transfer Pricing Legal Issues	
Summary	326

Chapter 11: Introduction to Industrial Communication: Advertising and Sales Promotion **328**

What is Industrial Promotion?	329
Industrial Promotion is Different	329
Promotion and the Buyer: A Micro Approach	330
Promotion and the Buyer: A Macro Approach	333
Why Advertise?	336
Managing the Industrial Advertising Effort	342
Objectives Budgets The Message The Media Decision: Some Industrial Alternatives Evaluating Advertising	
The Role of Sales Promotion	357
Summary	360

Chapter 12: Personal Selling and Sales Management **364**

Personal Selling is the Centerpiece	365
The Distinctive Requirements of Industrial Selling	367
The Salesperson Selling Aids The Selling Process Negotiation Sales Management	
A Dyadic Perspective on Industrial Selling	374
Relational Characteristics Social Structural Characteristics Characteristics of the Players Roles and Rules of the Game A Negotiated Social Process	
Managing the Industrial Sales Force	380
Sales Force Size and Organization Recruiting and Selecting Salespeople Training and Motivating the Sales Force Territory Management and Allocation Decisions Determining Performance Standards and Evaluating Salespeople	
Summary	398

Chapter 13: Industrial Channel Strategy	400
What is a Channel of Distribution?	401
What's An Intermediary Worth?	402
Distinctive Aspects of Industrial Channels	402
Major Types of Industrial Middlemen	403
Manufacturers' Representatives Industrial Distributors	
Conflict in Industrial Channels: The Need for a Systems View	412
Designing and Managing Industrial Channel Strategy	414
Considerations in Formulating Initial Distribution Strategy Forces	
Necessitating a Change in Distribution Strategy Forces of Resistance to	
Strategy Changes	
The Need to Evaluate Middlemen	420
Evaluating Middlemen—The Contribution Approach Evaluating	
Middlemen—The Weighted-Factor Approach	
Implementation of Distribution Strategy: The Role of Logistics	424
Summary	427
 PART IV: CONTROL OF INDUSTRIAL MARKETING PROGRAMS	 429
 Chapter 14: Control and Evaluation of Industrial Marketing Programs	 431
Introduction	432
The Process of Control	433
Categories of Marketing Control	435
Strategic Control Annual Plan Control Profitability	
Control Efficiency Control	
Selected Inputs to the Control Process	446
The Budget Data Requirements Scenario Analysis Productivity	
Judgments and Sensitivity Analysis Environmental Monitoring Systems	
Analyzing Performance Deviations	457
Evaluating Ethical Aspects of Marketing Programs	460
Summary	462
 PART V: CASES	 465
 References	 640
 Author Index	 649
 Subject Index	 651

PART I INTRODUCTION

The initial section of the book, consisting of the first two chapters, provides an overview of the nature and scope of industrial marketing and the industrial marketplace. A foundation is laid for understanding the diverse set of institutions and activities involved, and the challenging tasks confronting the marketing manager in today's industrial environment. An attempt is also made to dispel some of the common misconceptions regarding industrial markets—such as the belief that they consist primarily of declining smokestack industries, or that the technical nature of the products being sold means that little marketing is required.

Chapter 1 defines industrial marketing and illustrates how the task of the industrial marketer differs significantly from that of the consumer goods marketer. This chapter sets the tone for the entire book, in that many of the key points introduced here are emphasized and elaborated upon throughout the subsequent chapters. The chapter also establishes the basic philosophy of the book; namely, that marketing is a creative, managerial process that serves to enhance the *value* that a firm is able to provide to customer organizations.

Chapter 2 introduces the reader to the many different types of goods and services sold by industrial marketers, and the wide array of customers who purchase these items. Ways are suggested for grouping industrial products and markets so that better insights can be drawn regarding how both can best be managed. Because the customer is an organization, usually with a formal procurement operation, some basic purchasing practices and procedures are also introduced in this chapter.

CHAPTER 1

THE BASICS OF INDUSTRIAL MARKETING

Key Concepts

Characteristics of industrial demand	Marketing mix
Customer orientation (Marketing concept)	Marketing myopia
Customer value	Organizational environment
Environmental turbulence	Product attribute bundle
Exchange process	Production chain
Industrial marketing	Product life cycle
Information revolution	Product orientation
	Technological orientation

Learning Objectives

1. Define *industrial marketing* and the *industrial marketing mix*.
2. Establish the critical need for industrial firms to adopt a customer orientation.
3. Describe the size and importance of the industrial marketplace.
4. Discuss the dynamic environment facing industrial marketers.
5. Identify key differences between consumer and industrial marketing management.