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Chapter 2

Definition and History of Local Marketing

2.1 Introduction

We study the definition and history of local marketing in this chapter. First we study how to define local marketing in Section 2.2. In the next two sections we consider local marketing in a historical perspective. Section 2.3 describes the relevant changes in marketing in the past century. We relate these changes to developments in local marketing in Section 2.4.

Local marketing can be studied from both the retailer and manufacturer perspective. For the retailer, local marketing implies the optimization of the store's marketing mix. For the manufacturer, local marketing implies optimizing the product's marketing mix at the store level. We focus on the interaction between manufacturers and retailers, that is, how manufacturers and retailers optimize the marketing mix for a product (category) at the store level.

2.2 Local marketing, definition

In this section we discuss (i) the different definitions of local marketing used and (ii) how to derive the most appropriate definition.

Kotler et al. (2002) position local marketing on a scale ranging from mass marketing to individual marketing. Mass marketing implies the same marketing mix for all consumers. Individual marketing entails the products and marketing programs being tailored to the needs and preferences of individual customers. Local marketing lies between these two extremes and implies segmentation on a local level:

Local marketing involves tailoring brands and promotions to the needs and wants of local customer groups - cities, neighbourhoods and even specific stores. (Kotler et al. 2002 p. 318)

Kotler et al. (2002, p. 318) consider local marketing and individual marketing as parts of micromarketing:

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Micromarketing is the practice of tailoring products and marketing programmes to suit the taste of specific individuals and locations. Micromarketing includes local marketing and individual marketing.

Pearce (1997) uses this definition implicitly when he discusses micromarketing in a retailing context. Others define micromarketing in a different way. For example, Hoch et al. (1995) describe micromarketing as follows:

Micromarketing seeks to customize retailing policies to exploit differences across stores in consumer characteristics and the competitive environment.

Montgomery (1997) gives a similar but less explicit definition:

Micromarketing refers to the customization of marketing mix variables to the store-level.

The definition Kotler et al. (2002 p. 318) use for local marketing is what Hoch et al. (1995) define as micromarketing. However, it should be noted that Hoch et al. (1995) focus their definition at the store level. The local marketing definition of Kotler et al. (2002 p.318) is broader and it includes strategies for clusters of nearby stores.

Marketing practitioners use the expression local marketing to refer to store-specific use of the marketing mix. ACNielsen (Netherlands), for example offers a product called local marketing for this purpose (see www.acnielsen.com, and Chapter 4).

We asked some practitioners to indicate what they consider local marketing to be^{1,2}:

Local marketing is adapting the merchandise offered in an individual store, based on local factors.

Local marketing is born from the desire of the storekeeper: the storekeeper wants to distinguish himself from colleagues, he wants a local market. He wants specific customized actions.

Local marketing is the translation of marketing from the national level to local consumer needs.

Local marketing is the use of tactical instruments like assortment, logistics and promotion, at the store level.

¹ These answers have been chosen from the responses to a survey of Dutch supermarket practices. See also Chapter 3.

² We translated the answers from Dutch

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Hence, marketing practitioners and Kotler et al. (2002 p.318) use the expression local marketing where Hoch et al. (1995) and Montgomery (1997) use micromarketing. We prefer the term local marketing because (i) it indicates that we are dealing with a geographic location, and (ii) it is more generally accepted. Although the expression micromarketing indeed indicates that it involves marketing at a disaggregate level, it is less explicit because it lacks a geographical connotation.

It appears that most of the practitioners' definitions are related to customization at the store level. This is in line with Hoch et al. (1995) and Montgomery (1997), but discordant with Kotler et al. (2002, p.318). We prefer a definition that makes the level of customization explicit.

Furthermore, the definitions differ in how they specify the customization basis. Hoch et al. (1995), for example, mention consumer characteristics and competitive environment, while Kotler et al. (2002, p. 318) mention local needs and wants. Reinartz and Kumar (1999) show that store, market (competitor), and consumer variables determine the store's performance. We therefore include these variables in our definition.

Hence, we define local marketing as follows:

Local marketing is the customization of marketing mix variables to the store level based on consumer, competitor, and store characteristics.

2.3 Retailing in a historical perspective

The retailing landscape changed dramatically during the last century. In around 1900, retailing was characterized by a great number of often privately owned small stores (Messinger and Narasimhan, 1995). Storekeepers, owners of one or two small stores, had to deal with powerful manufacturers. Management focused mainly on products and production. Nowadays, a few retail organizations dominate the market in which the consumer takes a central place. In this section we describe the developments in retailing and marketing relevant for local marketing. We focus on the following topics: (i) increase in concentration, (ii) power, (iii) sales and customer information, and (iv) marketing and management. We provide data on developments in Europe and in the U.S.

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Concentration

Retail chains driven by economies of scale started to grow in the 1920s (Ghosh, 1994). In the beginning, chains were not more than groups of independently operating grocery stores. Major changes in retailing started with the introduction of self service in the 1940s in the U.S. and in the 1950s in Europe. This introduction marks the start of the emergence of supermarkets, characterized by a dramatic increase over the years in size, turnover, and merchandise sold. Figure 2.1 illustrates the development in store size for the last 20 years in Europe. Between 1980 and 1999, the percentage of stores with more than 1000m² selling area increased from about 25 percent to 53 percent. We can observe a similar increase in size for the US; the average chain store size increased by 38 percent over the period between 1983 and 1993 (Messinger and Narasimhan, 1995). Together with the increase in size, we see a dramatic reduction in the number of stores. Table 2.1 shows the development in number of stores per inhabitant for several countries over the last decade. Although the trend in all countries is a decrease in number of stores per inhabitant, there are large differences between countries. The number of stores per inhabitant tends to be low in Northern Europe and higher in Southern Europe.

Parallel to the increase in size, we can observe an increased concentration in retail organizations. An ongoing process of national and international mergers and takeovers has resulted in a market that is dominated by a few firms. Table 2.2 shows the change in market shares for the top-3 supermarket organizations per country in the period 1990-1999. The market share increased in all countries. The largest changes occurred in countries where the market share was relatively low in 1990. For the U.S. (not shown in the table) the concentration takes place in metropolitan areas. We find that the average market share per metropolitan area for the top-4 increased from 49 percent to 58 percent in the period 1958-1991, while at the national level the market share of the top 4 decreased from 22 percent to 16 percent (Messinger and Narasimhan, 1995).

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Figure 2.1 Developments in store size in Europe, percentage of stores with more than 1000m² sales area (source: ACNielsen).

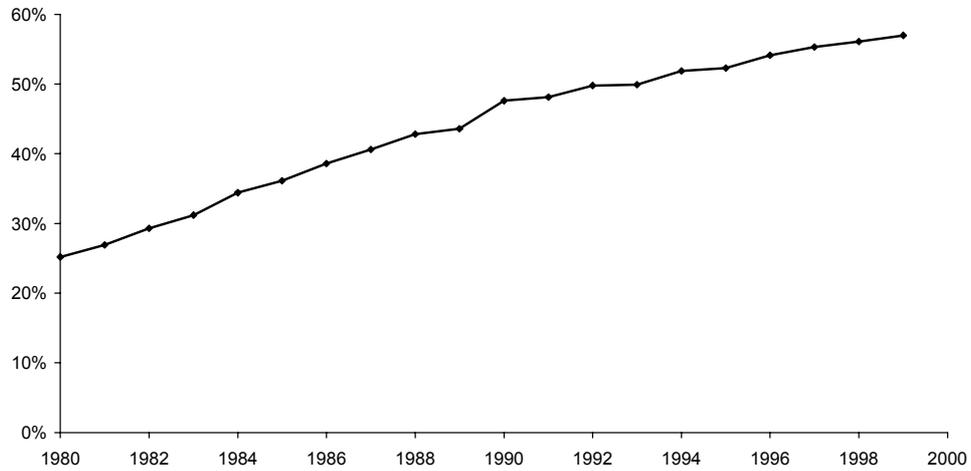


Table 2.1 Developments in number of stores per inhabitant (source: ACNielsen)

Country	Number of stores per 1000 inhabitants	
	1990	1999
Belgium	1.40	1.05
Germany	1.16	0.80
France	1.12	0.64
United Kingdom	0.79	0.58
Sweden	0.90	0.60
Finland	1.41	0.57
Austria	1.33	0.85
Italy	5.41	2.09
Portugal	3.28	2.66
Norway	1.49	1.04
Spain	2.67	1.71
The Netherlands	0.62	0.38
United States	0.67 ^a	0.48

^a Estimate for 1990, source Messinger and Narasimhan (1995)

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Table 2.2 Developments in the market share of the top-3 retail organizations (source: ACNielsen, FoodTrends)

Country	Market share top-3 retail organizations	
	1990	1999
Belgium	55%	62%
Germany	29%	53%
France	37%	66%
United Kingdom	31%	52%
Sweden	81%	86%
Finland	79%	80%
Austria	42%	66%
Italy	13%	32%
Portugal	37%	57%
Norway	55%	86%
Spain	35%	n.a.
The Netherlands	45%	78%

Sales- and customer information

The introduction of scanning in the 1970s marks a fundamental change in available sales- and customer information. Before scanning, data collection focused on *reporting* the current state (what is the market share, relative price etc.). Data were typically collected on a bi-monthly basis (ACNielsen's bimonthly store audits). This changed after the introduction of scanning, which allowed for a more accurate and detailed data collection. Importantly, it is now possible to *explain or predict* market share or sales and use this information to develop better decision support systems (Leeflang and Wittink, 2000).

On the other hand, firms have to find ways to analyze the dramatic increase in the quantity of available information, the so called *data explosion*. McCann and Callagher (1990) illustrate that for a typical category the transition from bimonthly store audit data to weekly store level scanner data has led to a 10,000 times increase in database size and a 9 times increase in the frequency.

The development of customer information systems in the 1980s and 1990s provides even more insight. Supermarkets introduced customer cards (or loyalty cards) that link customers to sales (who buys what). In addition, we can see that list brokers started to collect detailed customer information on a large scale. Household level information is now available on supermarket choice, product preferences, and a variety of background characteristics.

Power

In retailing, the power shift from manufacturer to retailers is often taken for granted. The possible causes include (i) concentration among retailers, (ii) consolidation into fewer and bigger stores, (iii) improved information systems, (iv) the fragmentation of consumer markets, (v) improved quality of retail management personnel, and (vi) a decline in manufacturers' advertising (e.g. Wahl, 1992). On the other hand there are both practitioners and scientists who question this supposed shift.

Table 2.3 shows the results of two different surveys about power among practitioners in Europe and the U.S. Although the questions in these surveys are different, they provide useful insight into about the power perceptions in Europe and the U.S. The first two columns of the table show European retailers' expectations (in 1994) about the future purchasing power of European retailers. We observe that 74 percent of the respondents expect a shift in power toward the retailers and hence, that 26 percent does not. The last three columns in Table 2.3 refer to the U.S. They show chains, retailer and wholesaler answers to the question whether there has been a power shift and the direction of this shift. We see that the majority of the respondents agrees that a power shift toward the has occurred.

In academic studies the power shift is addressed by several authors. The definition of power is important in this discussion. Many studies follow Stern and El-Ansari (1992), who define power as "the ability of one channel member to control the decision variables in the marketing strategy of another member in a given channel at a different level of distribution". The key aspect of this definition is that power refers to influencing the other's *conduct*. Ailawadi et al. (1995) and Messinger and Narasimhan (1995) use a narrower power definition. They define power as the influencer's ability to affect the other's actions to improve his own position (profits). This means that one only has power if it results in a *performance* improvement.

Studies that use a performance based power definition show that there is little evidence of a power shift. Messinger and Narasimhan (1995) conclude that neither accounting nor stock market data clearly indicate a shift in power from manufacturers to retailers. Ailawadi et al. (1995) report that a shift in market power can only be found in a few categories.

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Table 2.3 Purchasing power in Europe and the U.S. (source: Europe: ACNielsen, 1994, U.S: Progressive Grocer, 1992)

Europe		U.S.		
Expectations about future retailer purchasing power		Respondent	Has there been a power shift?	Is it toward the retailer?
Strong increase	18%	Chains	61%	65%
Increase	66%	Wholesalers	74%	55%
		Manufacturers	85%	87%
Constant	14%			
Decrease	1%			
Strong decrease	1%			

Studies that use a conduct based power definition find evidence for a power shift in different areas. Retailers, for example, have more pricing power (Kadiyali, Chintagunta, and Vilcassim, 2000) and can enforce guaranteed profit margins (Krishnan and Soni, 1997). Likewise, we see that retailers are able to demand a monetary contribution (*slotting fee*) for the inclusion of a new product in the assortment (see e.g. Bloom and Gundlach, 2000). Furthermore, retailers use increased store loyalty to introduce private labels. Table 2.4 shows private label shares for several European countries for 1986, 1992, and 1999. We see that, although the private label share differs dramatically between countries, the private label share grows in all countries except the Netherlands. In the Netherlands the share of private labels fluctuates at around 20 percent in the last 20 years. Based on separate data, we know that in the U.S. the private label share increased from 14 percent in 1958 to 19 percent in 1987.

Table 2.4 Private label share (source: ACNielsen, FoodTrends)

Country	1986	1992	1999
Belgium	15%	20%	26%
Germany	n/a	7%	23%
France	14%	16%	19%
United Kingdom	21%	37%	46%
Italy	5%	7%	8%
Spain	5%	8%	17%
The Netherlands	19%	16%	20%

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Thus, although changes in retailing have led to a situation where retailers exert more control at the instrument level (e.g. pricing power, slotting fees), this has not been translated into an increase in retailer performance (no support for a performance-based power shift). This phenomenon can be explained by the fact that manufacturers took actions to defend their position. The possible actions a manufacturer may take include:

- reducing the competition
- reinforcing the position toward the consumer
- cooperating with the retailer
- circumventing the retailer.

Manufacturers may reduce horizontal *competition* and in this way limit retailer possibilities. Consequently, retailers become more dependent and manufacturers more powerful. Manufacturers can reduce horizontal competition through (i) cooperation with other manufacturers or (ii) mergers with and takeovers of other manufacturers. Critical for the success of this approach is concentration at the retailer side. Manufacturers are more likely to stay in power if they are more concentrated than the retailers.

Table 2.5 shows the top-5 largest manufacturers and retailers worldwide. We observe that although the top-5 manufacturers are large in size they are much smaller than the top-5 retailers. The total turnover of the top-5 manufacturers is about half the turnover of the top-5 retailers. If we include the buying alliances between retailers the balance would shift even further (for example, Carrefour has a buying alliance with Metro, and Ahold with Safeway and Casino).

Table 2.5 Worldwide turnover top-5 manufacturers and retailers (source: Fortune 500, 2002)

Manufacturers^a	Turnover in billion \$	Retailers^b	Turnover in billion \$
Altria (Philip Morris, Kraft)	73	Wal-Mart	220
Nestlé	50	Carrefour	62
Unilever	46	Ahold	60
Procter&Gamble	39	Kroger	50
ConAgra	27	Metro	44
Total	236	Total	436

^aBased on the following branches: Beverages, Tobacco, Consumer Food, Household and Personal products.

^bBased on the following branches: Food&Drug stores, general Merchandisers.

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Another strategy is to reinforce the *position* toward the consumer. It is more difficult for retailers to circumvent the manufacturer when consumers have stronger preferences for specific manufacturer brands. A stronger position toward the consumer implies that the brand is so important that it may determine the store choice. Absence of the brand may lead to store switching (Lal and Narasimhan, 1996). Krishnan and Soni (1997) state that the power issue between retailers and manufacturers is secondary to the question of who has the power over the consumer. They indicate that manufacturers may reinforce their position by being innovative and by striving for sustainable differentiation for their brands. Additionally, manufacturers may stimulate demand through increased advertising and consumer promotion (*pull strategy*).

Third, manufacturers may choose to *cooperate* with the retailer. Cooperation serves to maintain the channel relationships and is often initiated by the dependent channel member (Rosenberg and Stern 1970, Schemerhorn, 1975, Frazier et al., 1989, and Skinner et al., 1992). Cooperation in general will result when the goals of channel members are compatible (e.g. Mohr and Nevin, 1990). One way to promote cooperation is through account management. The task of the account manager is to operate as an intermediary between manufacturer and retailer.

Chu and Desai (1995) consider two tools to enhance retailer cooperation:

1. *Customer satisfaction assistance*; an investment by a manufacturer to reduce the retailer cost of improving customer satisfaction (e.g. training the retailer's employees, free consultancy services etc.).
2. *Customer satisfaction index bonus*; a lump sum monetary reward to the retailer based on some measure of customer satisfaction.

They show that if retailers have a long-term orientation, customer satisfaction assistance is more effective than a monetary reward.

A fourth possibility for manufacturers to defend their position is to *circumvent* the retailer, thus approaching consumers directly (*direct marketing*), or setting up vertical-marketing systems. A vertical-marketing system is distribution structure in which all members act as a unified system. Examples outside the supermarket business include Levi's original stores and Vodafone stores. Few such initiatives are successful in the food business. Examples in the Netherlands include Unilever-owned stores and De Gruyter.

*Management and marketing*³

Markets became more saturated in the 1930s. Managers shifted their focus from “production” and “the product” to the selling of products and adopted *the selling concept*. The selling concept centralizes methods and techniques for selling products and services. At that time, marketing viewed the customer as a party *to whom* something is to be sold. This concept dominated until the early 1950s.

With the occurrence of higher degrees of market saturation, the marketing concept was introduced. This concept is based on the idea that, at least within established product categories, manufacturers benefit from understanding customer preferences and needs. Thus, if manufacturers first evaluate the market, identify heterogeneity in consumer preferences, and use this knowledge to produce goods or services, the position toward the consumer will be improved. Under the marketing concept market segmentation is a key activity. The customer is viewed as a party *for whom* products and services are developed.

A more recent development in marketing is the adoption of the customer concept. The customer concept is a management orientation that implies that firms initiate relationships with selected individual customers *with whom* superior customer values are designed, offered, redefined and realized in close cooperation with other partners in the marketing system in order to realize long-term profits through customer, partner, and employee satisfaction (Hoekstra et al., 1999).

A consequence of the increased customer orientation is that stores and manufacturers pay more attention to positioning. In this way they aim to deliver more customer value. The store’s positioning is defined by the merchandise offered, the quality of the service, the pricing strategy, the store format and related aspects that influence perception and buying behavior (Mulhern, 1997). The increased focus on positioning raises the question of how customer value should be delivered.

In the past, customers judged the value of a product or service on the basis of a combination of quality and price. Today’s customers, on the other hand, consider aspects such as convenience of purchase, after-sales service, dependability, etc. (Treacy and Wiersema, 1993). However, companies can be successful without meeting all customer expectations. Successful firms should focus on delivering superior customer value in line with at least one of the three value disciplines introduced by Treacy and Wiersema (1993) (operational

³ This section is partially based on Hoekstra et al. (1999).

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excellence, product leadership, and customer intimacy), while meeting industry standards in the others.

Firms that strive for operational excellence want to be leaders in price and convenience. They do not cease to look for ways to reduce process costs, eliminate intermediate production and transaction steps and increase the efficiency of business processes. In general, the search for costs reductions leaves few opportunities for realizing individual customer values. Examples of such firms in retailing include Lidl, Aldi, Wal-Mart, and Ikea.

Firms that choose product leadership focus on the production of a continuous stream of state-of-the-art products and services. R&D is very important for this discipline, which may make it difficult to develop innovations that can be commercialized quickly i.e., before competitors. Marketing in these firms serves to promote the acceptance of innovations. Nike is an example of a firm that excels in product leadership in the sport-shoe category.

Firms that adopt a customer intimacy strategy to deliver superior customer value tend to customize products and services to the needs of individual customers. The customer lifetime value to the company is used for profit considerations as the costs per customer are high. In food retailing, we observe customer intimacy in manufacturer-retailer relationships. Examples of manufacturers that develop supermarket specific marketing programs include Kraft USA, and Nutricia (Numico). Both Kraft and Nutricia use information on stores sales, consumer demographics and buying behavior, and geo-demographic data to aid their sales force to customize marketing programs to individual stores. Home Depot is an example of a retailer that adopts a customer intimacy strategy. Home Depot clerks aim to decide together with the customer which product he or she needs.

2.4 Local marketing in a historical perspective

About a century ago, storekeepers applied local marketing in a natural way. Storekeepers typically owned one or two independently operated stores. The storekeeper knew all customers and therefore could tailor his products and marketing programs to individual customer needs (*individual marketing*).

Manufacturers then focused on products and production and had little reason to customize the marketing mix at the store level. Customization was not necessary as markets were unsaturated. That is, it was easier to find other growth opportunities. The manufacturer was more powerful than the retailer.

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Manufacturers for example, imposed prices the storekeeper had to charge (*manufacturer resale price maintenance*) and could easily ignore retailer requests. This reduced possibilities for the storekeeper to apply local marketing.

From the 1920s onward, we see that the pursuit of economies of scale led to a change from an individual- to a mass approach. Chains started to emerge and store size increased dramatically. Store managers of these larger stores no longer knew their customers personally and were no longer able to approach them individually. Furthermore, chains' increased attention for positioning resulted in a focus on similarity between stores. The idea was that all stores should sell the same products and have the same prices and promotions (*mass marketing*).

The chain's focus on a similar policy in all stores led to a centralization of the locus of control over marketing mix decisions. Store managers now had to operate within limits set by the chain, and this restricted the opportunities to apply local marketing. In a similar way, communication shifted from the local- to the national level. The consequence was that store managers were forced to implement the advertisement's contents. For example, an advertised price discount of 10 cents off the regular price of €1.00 (both announced) would force the store manager to give the announced discount and set the regular price at €1.00.

Over time the adoption of the marketing concept induced managers to use a more differentiated approach. For example, retailers might be better off if they approached different consumer segments in different ways. A first form of differentiation is that chains are starting to differentiate between stores of different sizes. Albert Heijn (a format of Ahold in the Netherlands), for example has five size-dependent assortments. Another form of differentiation is induced by increased attention for positioning. Retail organizations use differently positioned store formats for different consumer segments. This differentiation allows them to make location specific format choices based on consumer- and competitor characteristics.

On the manufacturer side we see an increased focus on retailer preferences and needs. This change has been induced by the adoption of the marketing concept and the need to meet increased retailer demands. As a consequence, manufacturers have introduced account management which allows them to treat each retailer individually. For example, manufacturers are designing retailer-specific promotions (*tailored promotions*).

The introduction of scanning and customer information systems in the 1990s allowed retailers to map the types of customer a store attracts. Retailers now have

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detailed knowledge about what their consumers buy and how consumers react to the marketing instruments. This information is used to further adapt stores to customer needs. Some retailers do this for groups of stores and other retailers do this for individual stores. Thus, we see that some retailers have returned to the situation of 100 years ago when store keepers customized individual stores to customer needs.

Another effect of the introduction of scanning and customer information systems is that manufacturers also may know the store's customers. This situation is entirely new and is an important difference with the situation 100 years ago. Manufacturers use this opportunity to give store level advice on the marketing instruments. Importantly, the shifted power balance requires manufacturers to focus on optimization at the category-level instead of optimization at the brand level (see also Stern and Weitz, 1997).

The consequences of local marketing for the retailer and manufacturer marketing strategies are different. For the retailer local marketing fits within the marketing concept. That is, the retailer adapts his product to fulfill the needs of the store's customers. For the manufacturer, the application of local marketing implies a shift from the marketing concept to the customer concept. Under the marketing concept account management was used to tailor products and services to groups of stores (the chain). Adoption of the customer concept requires customization at the individual store level.

2.5 Summary and conclusions

In this chapter we have studied several aspects of local marketing. We have defined local marketing as the customization of marketing mix variables to the store-level based on consumer-, competitor-, and store profiles. Local marketing is a strategy that customizes the marketing mix at the store level and is the opposite of an undifferentiated strategy. Differentiation between groups of stores is an intermediary strategy.

About a century ago storekeepers often owned one single store and applied local marketing implicitly. Management orientation in this era focused on product and production. Local marketing disappeared as a consequence of increased retailer concentration and the focus on similarity between stores. The same marketing mix was used in all stores. From the 1970s onward we see a shift to a more market oriented approach. Stores paid increasingly attention to positioning and differentiation. Since the 1990s we see that retailers have been increasingly

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taking advantage of the opportunities offered by improved customer information to customize the marketing mix at the store level.

During the last century, manufacturers faced increasingly demanding retailers. Retailers forced manufacturers to guarantee profit margins, pay slotting fees, and produce private labels. Manufacturers reacted to these changes by approaching retailers more directly. They focused on cooperation in order to avoid conflicts. Local marketing initiated by the manufacturer can be seen as a further development of this strategy.

