Multinational Channel Strategy and Customer Value in an Emerging Economy

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ABSTRACT

This paper examines the impact of multinational channel strategy on customer value by assessing customer demand side issues. It assess the relationship between order cycle time, stock availability and sales to describe the impact of distribution strategy on customer value. The study was carried in locations comprised of Equator Bottlers Limited franchise territory within five districts in Western Kenya. A cross-section survey using a structured questionnaire was used to collect data. Data was prepared for analysis by editing, coding, categorizing and analyzed using both descriptive and inferential statistics. Majority of distributors were found to be located within the major urban areas of Kisumu and Kericho as a result of proximity to the plant and high rates of consumption. In order to increase the value offered to customers, there is need to reduce order cycle times to the bare minimum of one day for stock replenishment.

Keywords: Multinationals corporations, channel strategy, customer value, emerging economy

1. INTRODUCTION

According to Ajayi (2001), globalization may be defined as the increasing interaction among, and integration especially of economic activities. Johannesson (2010) noted that globalization takes companies on eternal search for market niches for their goods and services worldwide and much focus has been on emerging markets in China and South-East Asia. However the emerging markets in the five countries of the East African Community (EAC) - Kenya, Uganda, Tanzania, Burundi, and Rwanda have received little attention in the academic literature. The region is experiencing rapid economic growth as indicated by the region’s economic growth in 2008 which was 6.8% and the projections for 2009 and 2010 are even better at 7.5% (EAC Int, 2010).

Luo (2002) defined emerging economies as countries whose national economies grow rapidly, industries are structurally changing, markets are promising but volatile, regulatory frameworks favour economic liberalization and the adoption of a free-market system, governments are reducing bureaucratic and administrative control over business activities. Emerging economies experience high growth or growth potential, but without the
sophistication of the institutional framework seen in Western Europe and North America. Their main attraction is high economic growth and the corresponding expectation of rapidly increasing demand for consumer goods (Meyer & Tran, 2006). They comprise very diverse groups of customers that may have to be targeted with different products; brands and even business models. They are continually planned based on Western models especially those linked with market liberalization and globalization. Despite their attractiveness, especially to multinational corporations (MNCs), emerging economies typically lag behind in terms of economic development and intricacy of the institutional environment (Dawar & Chattopadhay, 2002).

Delivering commercially viable products that meet the needs of emerging economies depends on MNCs leveraging their expertise in governance, business processes, and management while still providing autonomy to their local operations. Despite their efficiency, global value chains need to be adjusted to local realities (Deloitte, 2006). Meyer and Tran (2006) assert that emerging economies are highly volatile due to frequent changes in institutions, industry structure and the micro-economy; their institutional frameworks may require different ways of interacting with business partners and authorities; many capabilities needed to compete in emerging economies are context-specific; and that many industries are highly fragmented, as many firms compete for a share of the market.

Academic literature also increasingly classifies Brazil, Russia, Mexico, Indonesia, Malaysia, Poland, Lithuania, Vietnam and Turkey as emerging economies (Luo, 2002; OSAA, 2009; Chandra & Tirupathi, 2003; London & Hart, 2004; Meyer & Tran, 2006). Herrero and Simón (2003) and Meyer et al (2007) however include Africa generally as an emerging economy. Their conditions match Luo (2002) and Meyer and Tran (2006) definitions of emerging economies. Multinationals such as Coca-Cola, which has a rich experience in Sub-Saharan Africa began their operations in Johannesburg in 1928 (CCAF, 2006) and adopted a global strategy (Batra, 1997; Clarke et al 2001, Dawar & Chattopadhay, 2002; Herrero & Simón 2003; Deloitte, 2006). The company relies heavily on local talent to fix its situations abroad and turn modest profits. Its best practices are replicated by South African Bottling Company (SABCO), the Seventh Anchor Bottler excelling in all The Coca-Cola Company Quality Standards (TCCCQS). All other local bottling companies in Sub-Saharan Africa strive to articulate these standards consistently. The Coca-Cola Africa Foundation channels programmes and funds towards livelihood concerns such as HIV/AIDS, water and environment, jobs, politics, business and law. In essence, Coca-Cola has a full-blown out strategy for Sub-Saharan Africa.

This paper examines the impact of multinational channel strategy on customer value by assessing customer demand side issues. It assess the relationship between order cycle time, stock availability and sales to describe the impact of distribution strategy on customer value. This is critical because as Webster (1994) underscores, value is defined by the customer in the marketplace and not by the supplier in the factory. Thus value is not what the producer puts in but what the customer gets out. Moreover Bookbinder and Lynch (1997), reporting on a study of customer service in physical distribution using a utility-function approach, concluded that execution of distribution activities adds value to customers.

2. DISTRIBUTION STRATEGY

Distribution, according to Lilien, Kotler and Moorthy (2003), comprises those functions of the firm involved in getting products from the manufacturer to the customer. They include: distribution planning with its related activities of production planning and materials procurement; inventory management and the related problems of receiving, in-bound transportation, and order processing; packaging; in-plant warehousing; shipping; out-bound transportation; field warehousing; and retail-outlet planning, operations and control.

Johannesson (2010) suggested that although the distribution channels selected depend on the goods sold, intensive distribution channels are most appropriate in East Africa for most consumer goods as most customers don't have personal transportation therefore they do most of their shopping in local stores and supermarkets. The distribution channels are typically long and rely on multiple levels of agents and distributors. Often manufacturers sell their production at the factory door to authorized distributors who transport the goods at their own cost to wholesale markets. These wholesale markets sell to retailers who arrange transportation of the goods to their retail outlets. However in the last 10 years, the trend has been to shorten the distribution channels by direct deliveries from manufacturers to retail stores. A push channel strategy is most appropriate for basic consumer goods and the emphasis on push channel strategy in East Africa concurs with the findings of researchers investigating distribution strategies in other emerging economies (Batra, 1997; Samiee, 1993; Mueller, Wenthe and Baron, 1993).
Subramanian and Matthijs (2007) identified speed-to-market as among five “critical factors” for effective participation in global network trade. Other factors included price, labor productivity, flexibility and product quality. Underlying competitive performance of these critical factors are a country’s policies and institutions. In order to improve the depth and sustainability of these five critical factors, it is critical that emerging economies create a supportive policy and institutional framework from the outset. The order cycle time therefore refers to the elapsed time between placing the order and receipt of delivery and is critical to the customer. Companies today try to shorten this cycle (Kotler, 2001) since the longer this cycle takes, the lower the customer’s satisfaction and the lower the company’s profits. An inefficient transport facilitation system can create obstacles and incurs real costs in terms of the product value (Schware and Kimberley, 1995) thus time and transportation costs seem to be inversely related (Keh and Teo, 2001). Dollar and Kraay (2001) suggested that it is essential for countries to have access to or be integrated in international production networks and in order to get a better understanding of where exactly the opportunities for Africa lie, it is helpful to analyze country-level industry value chains and compare industry performance with their direct international competitors. Devlin and Yee (2005) quantified the effects of inefficient trade infrastructure at the individual product level through logistics chain analysis.

Stock levels represent a major distribution strategy decision. Sub-optimization and other inefficiencies may result in large stocks or in stock outs (Keh and Teo, 2001). Storage costs reflect the opportunity cost of tying up capital in inventory and allocating physical storage cost to it while stocks represent an investment that must be available to produce sales. It is thus directly linked to sales and salespeople desire their companies to carry sufficient stocks to fill all customer orders immediately. Product availability is essential in attracting consumer demand and consumers would not patronize a firm without some form of assurance that they can find what they are looking for. Despite technological and managerial advances, stockouts are a common phenomenon and product availability remains a key issue in marketing (Balachander and Farquhar 1994, Anderson et al. 2006). Gruen and Corsten (2008) found that about 8% of retail items are out of stock at any one time, and the percentage can be much higher for advertised items while Su and Zhang (2009) showed that the ability to commit enhances the seller’s profits because consumers make patronage decisions based on their expectations of product availability. Secondly they found that availability guarantees are useful contractual mechanisms, which can help the seller, commit to higher service levels, thereby attracts customer patronage and increases willingness to pay. In fact, with availability guarantees, the seller can attain or even surpass profit levels under commitment.

Transportation choices affect product pricing, on-time delivery performance, and the condition of the goods when they arrive, all of which affect customer satisfaction. The speed with which deliveries are executed is related to the order cycle time. Delayed deliveries are a common complaint among distributors (Kotler, 2001; Berkowitz et al 1993).

Stock-outs result from improper inventory system (Lucey, 2002) and represent lost contribution for the stated period. It has a ripple effect on sales as customers migrate or lose goodwill in the supplier. Management needs to establish the profit consequences of running out of stocks and balance the known cost of service against the estimated market response (Christopher and McDonald, 1995). The frequency of stock outs varies inversely with sales and profits (Lucey, 2002). Keh and Teo (2001) identified adjustment costs as a result of the unavailability of products or services at the time of consumption or purchase. Inventory requirements are higher in the EAC than in more developed countries because of the long transport distances, poor infrastructure, and bureaucratic delays which all contribute to longer delivery times and frequent interruptions in supply (Johannesson, 2010). Zinn and Liu (2001) asserted that measuring the cost of stockouts remains an unresolved problem because the relationship between the stockout and the value of the potentiality resulting lost sales has not been quantified. At the retail level, customers may decide to either substitute the item they sought, or delay the purchase or leave the store and either forgo the purchase or search for the item elsewhere. Stockouts may also affect future patronage of the store. Therefore understanding consumer reaction to stockouts will ultimately lead to better merchandising and inventory policies.

Economic value to the customer is the fundamental premise underlying value-based strategies (Forbis and Mehta, 1981). The marketer must first evaluate all of the customer’s costs related to buying the product. Finally, through a comparison of the incremental value of both products, the marketer can establish a price that reflects the relative value of the product to the customer. Porter (1985) proposed the value chain analysis as a tool for identifying ways to create more customer value. Every firm is a collection of activities that are performed to design, produce, and market, deliver, and support its products. Successful firms need to look for competitive customers. According to Weatherspoon and Reardon (2003), supplying supermarkets presents both potentially large opportunities and big challenges for producers. Supermarkets procurement systems involve purchase
consolidation, a shift to specialised wholesalers, and tough quality and safety standards. To meet these requirements, producers have to make investments and adopt new practices. This is hardest for small producers, who risk exclusion from dynamic urban markets increasingly dominated by supermarkets. Many companies have partnered with specific suppliers and distributors to create a superior value-delivery network. Distribution decisions are more enduring than the other marketing mix variables. Management needs to search for distribution economies in inventory control, warehouse locations, and transportation modes. Producers vary in skill in managing distributors. Kotler (2001) stated distributor functions as selling and promoting, buying and assortment building, bulk breaking, warehousing, transportation, financing, risk bearing, market information, and management services and counselling.

3. METHODOLOGY

The study was carried out in Western Kenya, which is characterized by low crop yields and low household cash incomes (Kelly et al., 2003). Portable water, paved roads, electricity and telephone landlines are all scarce in this region. Most residents are subsistent farmers with small farm sizes often in the neighbourhood of 0.1 hectares (Chianu et al., 2008). Industrial activities in the region comprise fishing along the Lake Victoria shores, Tea plantations and factories in the Kericho Highlands and Sugarcane plantations in Mumias-Butere and Muhoroni-Chemelil area. The study area comprised of the Equator Bottlers Limited franchise territory in Western Kenya. For sales purposes, the area was divided into five territories (districts) namely; Kisumu, Kakamega, Kericho, Siaya and Busia.

The study surveyed Coca-Cola distributors in order to ascertain how they perceived the channel policy advanced by the multinational. The local franchise holder, Equator Bottlers Ltd, contracts these distributors to distribute soft drinks in the territory on its behalf. Distributors were ideal study candidates because they are the first set of customers in the value delivery process. Being immediate customers (Slywotzky and Morrison, 1997), they are fundamental in conveying value throughout the channel. The distribution model includes key distributors (KDs), strategic sales depots (SSDs) or manual distribution centers (MDCs), ice plant operators and company depots.

These distributors connect with retailers who eventually reach the final consumers. Global brands (adapted to local situations) are pushed through the channels to deliver its promise to consumers. Incentives are programmed to desesasonalize low season sales and to optimize the sales of high season sales. Coca-Cola Sabco has set up entrepreneurs as small, independent distributors since 2002 with its innovative Manual Distribution Center System initiative. It has now been implemented in four East African countries: Kenya, Tanzania, Uganda and Ethiopia. As of year end 2005, 900 such small businesses existed, employing up to seven people each and generated total revenues of $114 million. Together with the International Finance Corporation and the Africa Project Development Facility, Coca-Cola Sabco has helped these entrepreneurs to obtain favorable financing and business skills training.

For administrative purposes, each area is headed by a district sales manager or area sales manager who report market performances executed to the general sales manager who has overall responsibility for sales volume attainment. A cross-section survey using a structured questionnaire was used to collect data from 88 of the Coca-Cola distributors operating within Equator Bottlers Limited franchise in Western Kenya. They were randomly sampled from a total of 114 registered as of 1st January 2006. Data collection was done during the month of June 2006 coinciding with a consumer and trade promotion mounted around the 2006 FIFA World Cup Football Finals theme. Among others, the main variables on which data were collected included distributor characteristics such as type, location, experience, preferred supplier, stocks and sales information. Data were also gathered on average order cycle times, presence of stock outs, delay in deliveries and degree of satisfaction on the delivery speed. Level of agreement was measured by an 11-item Likert-type scale based on distribution strategy variables. The importance of the distribution strategy variables to the distributor were measured on a 5-point scale with 1=very unimportant and 5= very important. Data gathered were prepared for analyses by editing, coding, categorizing and recording then analyzed using both descriptive and inferential statistics.

4. RESULTS AND DISCUSSION

Distributor characteristics

Majority of distributors were located within Kisumu sales territory (36.4%) followed by Kericho at 20.5%. Proximity to the plant and high rates of consumption may have accounted for the high number of distributors in these areas. Locations offer different opportunities for exploitations. Given the rate of consumption, economic activities, and the company’s investment in a given area, distributors ought to optimize their sales. Management
however must shorten order cycle times for all distributors regardless of their respective locations (Kotler, 2001). The majority of distributors (52.3%) got supplies from Equator Bottlers Ltd followed by its Company Sales Depots (39.8%) giving a cumulative percentage of 92.0%. Key distributors served other categories of distributors in rare occasions (8%). Being the preferred supplier to distributors, the firm has a mandate to shorten order cycle times to increase their value. Supplier flexibility should affect the linkages between customer service and customer satisfaction. Providing flexibility offers the firm an opportunity to meet and exceed the customer’s expectations, thereby resulting in customer satisfaction (Oliver, 1980).

SSD operators were the highest category of distributors studied at 68.2% followed by Key Distributors at 19.3%. Ice Plant Operators and CompanyDepots were below 10% each. The type of distributor here dictates recommended stock holding levels. SSD operators and ice plant operators individually account for a relatively small proportion of stock available compared to other forms of distributors. Their sales are equally low individually. CompanyDepots (5.7%) and key distributors (19.3%) accounted for the majority of sales. About 28.4% of respondents had operated for less than five years and 35.2% up to 10 years. Experience reflects that distributors have learnt to minimize their costs by increased activity learnt over time. Customer loyalty is important because once there is loyalty; customers can exhibit behaviour that translates into higher profits for the firm (Keh and Teo, 2001). During the period of study, only 33 respondents (37.5%) experienced a stock out, which reduces the stocks available for sales. According to Lucey (2002), when distributors experience stock outs, they lose opportunity to sale reflecting a poor inventory policy or inefficiency in managing distributor operations. All respondents had experienced delayed deliveries during the study period. Delayed deliveries lengthens the order cycle times since delivery speed, which is a part of the order cycle time is determined by the mode of transportation chosen. Management therefore, needs to invest in proper fleet management that ensures speedy delivery.

Channel strategy

Sales, stock availability, order cycle time and frequency of stock outs were measured on ratio scales. Satisfactory delivery speed was measured on a 5-point interval scale. The minimum sales (measured in physical cases) was zero and maximum sales were 21, 064 cases. A promotion had been programmed to provide distributor sales incentives to deseasonalize the low sales. Stock availability (measured in physical cases) had minimum of 123 cases and maximum 5234 cases. Management desired a minimum stock of 300 cases for stock operators and ice plant operators. Other types of distributors need to carry at least four days stocks based on daily sales. McCarthy and Perreault (1996) proposed that inventory should be stored to smooth out sales, increase profits and customer satisfaction. Order cycle time (measured in days) was minimum one day and maximum five days. Management desired a maximum order cycle time of one day. Clearly order cycle times exceeding one day reduces the stock available if daily sales are held constant.

Frequency of stock outs was measured in the number of times distributors experienced stock outs during the study period. Maximum number of stock outs was 17 times during the study period. Management needed to reduce the frequency of stock outs to nil for all distributors. Satisfactory delivery speed was measured on a 5-point interval scale where 1=not very satisfactory, 5=very satisfactory. Satisfactory delivery speed indicated that the respondents were somewhat neutral on whether the delivery speed was satisfactory or not. Delivery speed impacts on the order cycle time. A very satisfactory order cycle time tends to shorten the order cycle time holding other factors constant. Somewhat neutral satisfactory delivery speed, as the study found, indicated that factors other than delivery speed contributes to the high order cycle times. Management needs to provide a very satisfactory delivery speed to the distributors and to mitigate all other factors that impact on order cycle time such that distributor sales are maximized.

Customer value

Pearson’s product moment correlations for study variables showed a high positive correlation between stock availability and sales \((R=+0.726)\) and a weak positive correlation between satisfactory delivery speed and sales \((R=+0.094)\). The sign of the correlation between stock availability \((R=+0.726)\) and sales was significant at \((.0001)\) 2-tailed significant level. This indicates a strong positive relationship between stock availability and sales. This is because a satisfactory delivery speed, being a subset of order cycle time, tends to increase the speed of stock replenishment. Equally weak but negative was the correlation between frequency of stock outs and sales in cases \((R=-0.196)\). High frequency of stock outs reduces the stocks available for sales holding other factors constant and stock outs reflect a poor inventory policy. Stock outs may result from insufficient investment in stocks or from unpredictable order cycle times. The correlation between order cycle time and sales was in the expected direction \((R=-0.012)\) though weak. Shorter order cycle times translates to faster stock
replenishment at distributor warehouses. This avails stocks ready to produce sales hence profitability. Conversely, longer order cycle times increases the stock replenishment times reducing the stocks available to produce sales.

**Multiple Regressions for Stock Availability**

A backward stepwise regression solution was performed on the four independent variables (Nargundkar, 2003). According to the model, stock availability per distributor had a stable coefficient of 2.777 and a t-value of 9.786. It was therefore, the only independent variable that was significant in determining the customer value. In equation form:

\[ Y = 726.46 + 2.777X_1 + \epsilon \]

where \( Y \) = Sales in cases; \( X_1 \) = Stock availability in cases; and \( \epsilon \) = error term

Hence to increase customer value by one case of sales, management needs to increase distributor stock availability by about 2.777 cases. The correlation between stock availability and sales was \( R=0.726 \). The results mean that 53% of the variance (R-square) of sales has been significantly explained by only one independent variable, stock availability, \( X_1 \). The positive beta weight indicates that if sales are to be increased, it is necessary to increase stock availability. As a result the hypothesis that the order cycle time, delivery speed, stocks availability and stock out frequency will significantly describe the impact of distribution strategy on customer value was rejected because only stock availability significantly described the variance.

**5. CONCLUSION**

In order to increase the value offered to customers who are distributors, there is need to reduce order cycle times to the bare minimum of one day, preferably the same day so as to increase stock replenishment speed, reduce delayed deliveries and to avoid stock outs. There should be optimal increases of stock availability to avail sufficient quantities of all brands and packages to customers for selling. There is also need to use an appropriate mix of the predictor variables to continuously predict customer value and make improvements in view of offering the highest value to customers.

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