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Rethinking the Role of Middlemen

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Abstract

Middlemen and intermediaries are established concepts in the distribution channel literature. Recent developments of practice make the use of the concept of middleman problematic. For example, firms traditionally labelled as distributors are increasingly involved in specifying design, materials, and production methods of products. The ongoing restructuring of distribution has been characterised as a process blurring the role of the respective actors. This paper argues that the problems with the concept rather stem from the fact that "middleman" is used to describe actors whose roles vary a great deal. The aim of the paper is to explore the characteristics of the different roles middlemen can take in the market network.

Keywords: Middleman, intermediary, distribution, marketing channels

Middlemen in the market network

The middleman (or intermediary) concept is frequently used in marketing literature to denote a particular category of market actors. A major problem is that the notion of a middleman is used to describe actors with quite different roles in the market system. Consequently, the interpretation of the concept becomes somewhat fluid and vague. In the literature taking the marketing management perspective of the manufacturer, middlemen are generally considered as important - but often antagonistic - counterparts. They are perceived to be part of distribution channels. This one-sided perspective conceals the real impact of middlemen in the market system. In particular it becomes problematic when we want to interpret the recent trends in distribution. The very concept of a middleman implies an actor in-between two other actors. In many cases the middleman is analysed primarily in terms of its relation to these two other actors. The purpose of this paper is to put in focus the business of the middleman rather than its role as perceived by others. We believe this perspective to yield more accurate insight in the business logic of middlemen. Therefore, this approach may be of help both in order to deal more effectively with middlemen and to identify alternative strategies for their businesses.

Before analysing the various middleman roles we need to elaborate a little on the system in which they are involved – i.e. the market network. It is common to conceive marketing as the process of bridging the gap between production and consumption. In its broadest sense marketing can thus be thought of as the 'link between a society's material requirements and its economic patterns of response' (Kotler 1988:xvii). Thus it is the process by which needed and valued resource elements are made available to users. This task of bridging can be carried out in many ways involving different actors performing the various activities required. In its most elementary form the bridging of the gap is a matter of exchange and transfer of resources between the provider and the user of a given resource entity – i.e. a product. The process appears relatively straightforward when we limit the perspective to a given and tangible ‘product’. The core of the marketing process then becomes carrying out exchange transactions between two parties - who may or may not be assisted by a middleman. When the perspective is expanded to cover more than exchange and transfer of a single given product gap bridging becomes more complex. The reason being that what is normally exchanged is a bundle of resource elements (different products and services) combined by the provider and in turn used by the user in combination with other resources. The gap bridging involves thus series of exchange relationships between numerous actors who all, apart from carrying out the exchange transactions, perform the task of combining resource elements to meaningful resource bundles. Alderson (1965) pointed out this function of the market system as sorting toward meaningful resource collections.

Once we broaden the perspective in this way a whole network of exchange relationships and actors appears involved in resource transfer and sorting, i.e. in bridging the production – consumption gap. Various actors in the market system buy and sell resource bundles that are re-combined. The market network is in continuous evolution as new exchange opportunities are enacted and various categories of actors perform different roles and display different activity focus and links to others. These changes cause problems with a “middleman” concept if defined as something that is in-between. The evolution of the market network reshapes both what is in-between and what it is between. Since the conduct of middlemen is one of the forces shaping the market system we need to consider the business of a middleman from its own perspective, rather than from the perspective of others.

The starting point of our discussion is a broad review of the historical changes in the role of middlemen in the market place. The core of our argument is that middlemen always fulfil important business functions in the market system, and that the roles they take complement those of other market actors. Our analysis focuses on three roles in which middlemen actually follow different business logic and perform widely different functions. In the following sections we discuss the middleman as trader, the middleman as distributor and the middleman as provider.

The Middleman as Trader

The essence of what many middlemen do is in the broadest sense captured in a figure common in many marketing textbooks (see figure 1). The figure illustrates that middlemen offer to their customers an assortment - a combination, of products (resources) acquired from various sources. The assortment offered to the customers by the middleman is different from what can be offered by each of the firms supplying the middleman. The middleman offers thus an own ‘product/service’ in which the various suppliers’ products are but components. The business, like any other business, depends on developing and maintaining exchange relationships with customers – and suppliers - for which it competes with others.

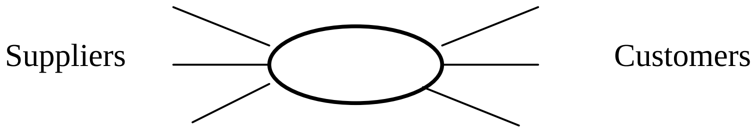

Figure 1: The middleman as trader

The middleman trader exercises the essential entrepreneurial functions of exploring and creating market exchange opportunities and bears the risk entailed in this task. It operates in two markets – helping the customers access resources needed and the holders of resources to reach the users. The middleman has an important function in the economy of the gap bridging activities in the market network. By creating a different bundle of resource elements offered to customers the middleman takes on the function to "economise" on costs of bridging the supplier - customer gap, i.e. lowering the costs of transactions.

The middleman as trader played an important role in a historical perspective. According to Chandler (1977) a type of trader was the dominant market actor in the pre-industrial society. This kind of middleman

> 'bought and sold all types of products and carried out all the basic commercial functions. He was an exporter, wholesaler, importer, retailer, ship-owner, banker, and insurer' (ibid. p.15)

Even if some of the activities of this middleman entail minor resource transformation, such as packaging, sorting etc., the distinctive trait of the business of the middleman as trader is that it does not transform resources physically to any significant extent. Middlemen do not carry out the production function in the narrow sense, trading is the core activity in this role of the middleman.

Towards the end of the 19th century large industrial manufacturing businesses started to emerge and gradually became more and more important actors in the market. This change has affected the status and the function of the middleman and many shifted to a new role – the middleman as distributor.

The Middleman as Distributor

The industrial manufacturing businesses typically take on a number of business functions: they identify exchange opportunities, they define a product (a bundle of resource elements) that they also produce and they acquire the necessary resources. In doing that they take on some of the functions of Chandler's 'great trader' by connecting different markets. However, this function is often overshadowed by the complexities of organising the production activities. The most prominent example is the River Rouge plant established by Ford in the 1920s. Ford not only assembled the cars and manufactured the components, but also

> 'built his own steel mill and glass plant. He founded plantations in Brazil to grow rubber for tires. He bought the railroad that brought supplies to River Rouge and carried away finished cars' (Drucker 1990, p. 100).

Large-scale production of this type typically causes two problems for manufacturers. First, production at large-scale entails speculation because manufacturing must be initiated before customers have ordered and bought. Second, the manufacturer faces the problem of reaching numerous users in such a way that the cost benefits of mass production are not offset by the costs of transfer and transaction. Middlemen can be instrumental to manufacturers in solving both these problems. They can share the entrepreneurial risk and they can economise on the transaction and transfer costs. These conditions provide the opportunities for a new role of middlemen – the role as distributor (see figure 2).

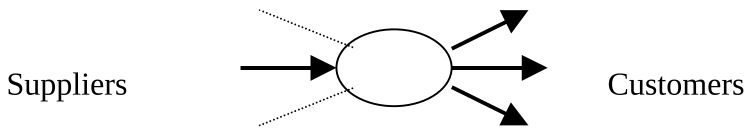

Figure 2: The middleman as distributor

The middleman as distributor represents the dominating view on intermediaries in the marketing literature, which takes a manufacturer's perspective. Middlemen are perceived as 'business firms that help the company find customers or close sales with them' (Kotler 1988:137). Furthermore they hold inventories and 'push' the products, which are crucial marketing activities when speculation rules the game. The distributor role maintains the basic characteristic of the middleman as trader but the emphasis shifts. The inputs are to large extent given, identified and provided through the manufacturer.

The figure illustrating the role of the middleman as distributor is to some extent extreme as it reflects the perspective of one manufacturer. Of course, most distributors represent more than one manufacturer. The middleman is dependent on individual manufacturers for developing exchange relationships with customers, but many of the middlemen as distributors continue to fulfil the assortment function and serve several, more or less differentiated manufacturers. However, in each manufacturer's perspective they are part of its channel. The middleman as distributor has been *the* view of the role of an intermediary for long time.

However, dynamics of the market place reshape business opportunities for the actors involved. The user side have turned towards increasing differentiation. As users become more acquainted with the products/services offered they tend to require customised solutions rather than standardised. This development has been re-enforced by supplier ambitions to differentiate from competitors. Continuous entrepreneurial innovation of the product offering is inherent in the marketing process (Kirzner 1973). This in turn requires closeness and proximity to users and – in particular – the operations of the users. The middleman distributor who interacts directly with users stands in many cases better chance than the manufacturer to conceive a 'superior offering' in the eyes of the user. This explains why many distributors have developed the third of the middleman roles.

The Middleman as Provider

Middlemen distributors are in good position to exploit the closeness to users. Therefore, many of these have gone through another shift in the middleman's role in the business network, and we can observe a change in the allocation of business functions among the actors involved in gap bridging. The focus of many middlemen's business becomes the identification of exchange opportunities based on the user's conception of suitable resource bundles and then searching for appropriate sources of these resources.

This logic of the middleman's business is derived from a customer/user perspective (figure 3). In this view the middleman is part of the user's supply network, rather than a manufacturer's channel. Using the terms of Bucklin (1965) speculation is replaced by postponement as the main business logic for the middleman and the whole network. The 'supply chain perspective' mirrors the changes in the allocation of the business functions in the overall net of market relationships.

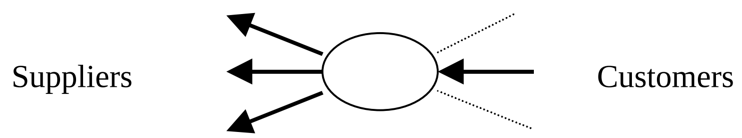

Figure 3: The middleman as provider

The current concern with supply chain management both in practice and in theory indicates that the emergence of the middleman as provider is not a marginal phenomenon and concerns numerous middleman businesses. In fact the supply chain management perspective is not applicable only to the user-manufacturer but to user tout court. It is interesting to note that this perspective of middlemen is not at all new – it has only been more or less obscured by the dominant paradigm of middleman as distributor. Already back in 1960 it was argued that

> 'the middleman is not a hired link in a chain forged by a manufacturer, but rather an independent market, the focus of a large group of customers for whom he buys' (McVey 1960:64)

Analysis and implications

The historical perspective taken in this paper has helped us to identify three different roles of middlemen: trader, distributor and provider. It suggests that the role of the middleman and his business changes as business conditions and roles of other actors in the overall market network change. The main conclusion of our analysis is that middleman's role is increasingly differentiated. However, the differentiation in middleman's roles must not be confused with a general shift. Not all middlemen-traders did become middleman-distributors or will become middlemen-providers. The different roles of middleman coexist. The three categories suggested in this paper are only tentative and can probably be further refined.

Middlemen's businesses fall into different categories, depending on how they identify the best business opportunities which in turn is contingent on the network of actors they interact with. Which role becomes more appropriate depends on the context. In the historical perspective unsolved problems on the user side paved the way for the differentiation in middlemen's roles. Mass-production required mass-distribution and opened an opportunity for middlemen to act as distributors. User initiated need for customisation and differentiation of supply opened for middlemen to act as providers. The entire middleman business sometimes becomes a set of different types of businesses and one middleman company may have different roles in relation to different business partners. Parts of its operations may be aiming at providing resources to customers, while others serve as a distributor for a specific manufacturer.

The claim we make is that interdependencies among the various actors in the network of market relationships have to be considered if we are to understand how the business and role of middlemen change. It is not enough to look at the middlemen from the manufacturer's angle only. "Economy" from a business perspective cannot be reduced to static cost efficiency considerations, it has also the facet of the "dynamic efficiency". All actors in the market network that participate in gap bridging are subject to the dictate of the two facets of "economy". The net of interdependent actors has to perform well on both criteria. Depending on prevailing conditions the mutual roles of the actors have to be modified accordingly – both in terms of its practice in business reality and its conceptualisation in business models. For long time the need to pursue transfer efficiency in gap bridging has been in focus in analysis of distribution systems and the model of middleman as distributor became the dominant one. The shift in role towards the middleman as provider that we currently observe implies shifting the focus from transfer efficiency to co-ordinating effectiveness.

The main analytical implication stemming from our analysis is that the generic notion of a middleman looses much of its meaning. Considering the varying roles of the middlemen's practices the generic middleman concept becomes weak and analytically imprecise. Taking an extreme interpretation any business can be seen as a middleman business, since most companies are in-between other companies. As the roles of the middlemen differentiate we need to differentiate the analytical tools and therefore the concepts. Unless the differentiation in roles of middlemen is matched by differentiation of the concept of middleman it becomes increasingly a somewhat blunt analytical tool.

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