A contingency model for the company's use of relationship building

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Abstract

Literature shows that relationship orientation, relationship marketing and relationship management have become a must when an industrial company wants to establish a lasting competitive advantage. The strong interest in relations between industrial companies has resulted in the idea of relationship and relationship building being spread to other areas such as distribution, service and consumers. Now one must also build relations to middlemen, service suppliers and end consumers.

This paper analyses whether or not relationship orientation and relationship marketing actually is a must to all companies – no matter their position in the value chain, their size, their product range, and their degree of internationalisation etc. In other words, under what conditions shall a company seek to build relations and under what conditions is a traditional marketing called for. The problem suggests that a contingency model is developed because it deals with what strategy to use – and when.

To analyse all the factors relevant to a company's decision on whether or not to pursue a relationship strategy will be too extensive in a paper, and therefore this paper focuses on the situation factor: The company's position in the value chain. A specific analysis of the distribution of groceries in Western Europe illuminates the importance of the situation factor in question. The analysis shows that relationship orientation is not equally relevant for companies at different levels in the value chain. This also applies to large and small companies at the different levels and companies that produce different types of products. Consequently, the conclusion is that the company's position in the value chain is considered to be an important situation factor.

1. Introduction and objective

Relationship orientation, relationship marketing and relationship management have become modern. During the past few years it has become a must that companies build relations to customers and suppliers and concentrate their marketing on the choice of important customers and suppliers, whom they must cultivate in order to build long-lasting relations. This is the only way that a company can get a permanent competitive advantage and thus ensure its own survival and growth. It seems that relationship building is considered to be a key factor to success. This trend has come about as a contrast to the more traditional type of marketing, especially to the phenomenon transaction orientation.

However, the question is if relationship orientation and relationship marketing is a must to all companies – no matter their position in the value chain, their size, their product range, and their degree of internationalisation etc., or if one has to take a more varied view. Under some circumstances some companies might benefit from a combination of the two views.

The objective of this paper therefore is to analyse this problem. Under what conditions and in what situations can (should!) companies make more or less use of relationship building and relationship marketing. In other words, the idea is to make the relationship approach and the network theory more normative and application-oriented.

2. From business to business relations to customer relationship management

Relationships between companies in the industrial market are built, kept and cultivated. It is documented by numerous presentations made by the IMP group (see e.g. Håkansson and Snehota 1995). Researchers have devoted some time to find out how to define such relations, how they have developed, and who had relations to whom. Lately, they have been interested in finding out how to manage such relations (Ford et. al. 1998). An examination of the extended supplier concept in Danish Industry (Mikkelsen et. al. 2000) confirms that production companies attach much importance to their supplier relations, and that they plan to build even closer relations especially to their main suppliers.

The intense interest in the inter-relations between industrial companies has resulted in the idea being spread to other areas than the industrial marketing. Relations are now an issue in various connections, such as innovation, distribution, service and end users (Sheth and Parvatiyar 1995; Peterson 1995; Ford et al. 1998). Questions to be answered are how are companies to build relationships to their middlemen, to their end customers, and to their service suppliers. The concept Customer Relationship Management (CRM) has gained ground.

The question is if diffusion of the relationship approach will water down the concept and so reduce it use. In reality, when everyone builds relations to anybody, relationship marketing becomes marketing in a more traditional sense. E.g., when creation of brand loyalty tantamount building of relations to the end-consumers, and when the contact with wholesalers and retailers in distribution channels tantamount the building of networks and create relations to middlemen, and when service businesses (such as hotels, airlines) start loyalty programmes calling it relationship building, all they have done is to rename well known activities.

Also, the popularity of relationship building may make companies try to build relationships in unproductive situations where the resources would be better used on other activities. Further, it is possible that a number of companies may suffer from a kind of self-delusion thinking that they are relationship oriented without being so – because they speak a lot about customer and supplier relations – and thus make the wrong decisions (Jørgensen and Freytag, 2000).

However, if it has become a prevailing opinion that relationship building to suppliers, customers, middlemen, and service companies is all that matters, it is time to change the opinion so that the companies become aware of when building, maintenance, and cultivation of relationships makes sense and when a more traditional type of marketing is the best to use. It is not logical that all companies in any situation should build close relationships to their environment.

Of course this raises the question when, under what circumstances, and to what extent a company should seek to build relations, and when and to what extent it should not do so - or attach only a moderate importance to closer customer and supplier relations. It is obvious that there is a need for a model - or at least some kind of method - that can help the companies to decide, i.e. a contingency model.

3. The contingency model

The contingency approach is developed within the organization area. The aim is to study how organizations can adapt the best to their environment under different circumstances. The theory is that organizations that know how to create accordance between the internal qualities and the environment will be the most effective ones.

"The design of an effective organization as necessarily having to be adapted to cope with the "contingencies" which derive from the circumstances of environment, technology, scale, resources and other factors in the situation in which the organization is operating" (Stacey 1993).

According to Stacey the most important situation factors are:

1. Environment, especially the market.
2. The size of the organization.
3. The applied technology.
4. The historical development.
5. The expectations of customers and employees.

The demand is that the various situation factors and the so-called design parameters must agree closely with each other. They must also be internally consistent.

The contingency approach has also been used within logistics (which puts us close to the value chain view). Here, you must try to describe the patterns that make it possible to specify under what circumstances and in what situations a given logistic strategy is preferable to other strategies. This means that you must define alternative strategies, specify various situations and indicate when to prefer one strategy to another. In this way the model can be used normatively.

It seems natural to use the same approach when building a model for when to use a relationship oriented strategy and when not to. Here, the demand is also that you can specify different situations and different alternative strategies, and state the connection between situations and strategies. "Correct" strategy and implementation of this can be divided into company specific situations or situations dealing with "partner" decisions and activities.

Situation factors could be:

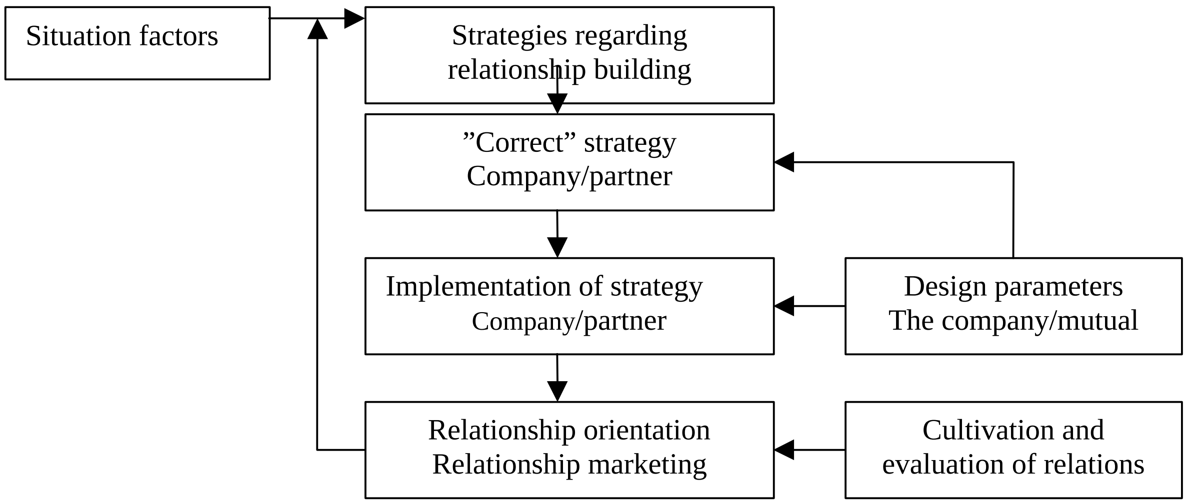
- The company's placing in the value chain
- The company's product range
- The complexity of the product range
- The company's size and growth
- The company's historical development
- The company's degree of internationalisation
- The structure of the market and the suppliers
- The competitive situation, including the competitors' relationship build-up
- Customer and supplier expectations

Design parameters could be:

- The information system, including ECR and EDI
- Quality certification
- Criteria as for choice of suppliers
- Customer portfolio
- Logistic system building, e.g. degree of integration with suppliers and customers
- Outsourcing
- The type of organization, e.g. Key-Account-Management
- Incentive structure
- Cooperation on research and development
- Cultivation and evaluation systems for suppliers and customers

Design parameters are the building stones available when a chosen strategy is to be carried out and afterwards when to revise and keep it. The model indicates how design parameters more or less will be the company's parameters whether they will be mutual, i.e. where management decision and activities cut across the companies.

Figure 1 The structure of a contingency model



4. The situation factor: The company's placing in the value chain

As mentioned above, a number of factors may influence the relevancy of a company pursuing a relationship strategy or not. In this paper, however, it will be too much to try to analyse all factors, their influence and interaction. Instead, a single factor will be analysed, including its connection to other factors. Through the recent years, development has been to try to use the relationship approach in other areas than the business-to-business and so it is only natural to concentrate on analysing if relationship building will be just as relevant in other parts of the value chain as defined by Porter (1985). For example, would it be as relevant for companies that produce and distribute consumer goods to build relationships to their suppliers/customers as for producers of industrial products and components?

A relationship is a long lasting, binding cooperation where you adapt to your partner and visa versa, and where there is a close interaction (Håkansson and Snehota 1995). There is also complexity, symmetry and a low degree of formalization.

If you look at the producers of groceries there are many reasons why they want to build relations to the next link in the value chain – wholesalers, retailers, transportation suppliers and the end consumers. It can be a question of maintaining or develop their market share, ensuring access to distribution channel and customers, controlling quality, ensuring access to information etc.

However, one must assume that the competitive companies are interested in doing so as well, and in many situations therefore, they will compete in building relationships to important customers and middlemen. Also, the question is if the middlemen and customers in question are interested in close relationships with the suppliers. Presumably, they will only engage themselves in such if they will profit from it.

Usually, there are two types of relationships in distribution systems. Firstly, contractual systems, such as franchise systems and sole agent systems, where the middlemen's businesses and economic conditions are defined and where the middlemen act as the producers auxiliary arm. Relationships of this type fall outside the framework of this paper, cf. the above definition of a relationhips.

Secondly, middlemen, where the products are part of an extensive product range along with products from other suppliers. Here, the middlemen can be different kinds of wholesalers and retailing chains. In this type of system, the relations may be close, but it may also be that the supplier relation is impersonal and neutral. The question is what decides what it is going to be. In some situations it may be irrelevant to try to build relations to important customers whereas it in other situations may be quite relevant to do so by means of different design parameters.

In situations where a producer of consumer goods is interested in building relations to one or more important customers, you may assume that the customers' interest will depend on factors such as the producers' size and importance. Again, the importance depends on how big a share the suppliers' products forms of the customer's product range and of the competitive situation as for this type of products. In the following, the interaction between producers and middlemen will be discussed on the basis for the marketing situation of non-durables in Western Europe.

5. Relations in the value chain for consumer goods

Companies producing consumer goods usually sell their product range to end users through one or more groups of retailers in the geographic markets. Retailers distributing a company's products determine the level of service towards the end users. Retailers are in direct contact with the users, and the number of retailers, their function performance, and their location determine the users' trouble and costs in connection with the purchasing of the company's products. Therefore, sales are widely influenced directly by decisions concerning number and composition of the distribution system's retailing elements.

However, according to the producer, not all retailer combinations are just as good. This is due to the retailer's development pattern. Retailing constantly changes. Some types of retailing companies grow, whereas others stagnate or are on the decline, and new types of retailing arise. Furthermore, shops constantly open and close down which means that the geographic location changes, and that the shops continuously change their parameters such as product range, prices and function performance.

Different combinations of retailing elements in a producer's distribution channels therefore have different basis for preservation or growth in market shares. Further, different combinations have consequences for the company's marketing in general, and by and large it may have consequences for the distribution and the marketing of the company's other products.

When a producer wants to have his products or part of his product range marketed through certain types of stores considered to provide a satisfactory level of service towards the end users, the key question is how the various retailers or groups of retailers purchase their product range. What criteria determine the choice of suppliers? Retailers are independent institutions seeking to fulfil their own goals and taking care of their own interests, and they must continuously be convinced that it is in keeping with these goals and interests that the products of the producer in question are part of the product range. On the one hand the producer wants to distribute through certain middlemen, and on the other hand the individual retailers consider if they want to have the various products in their product range. Retailers usually have good changes of getting suppliers and can change supplier if they want to. Therefore, a producer who wants to include certain retailers in his distribution channels must market himself to these units and try to build relations to them.

During recent years the West European retailing of grocery products has experienced a considerable structural rationalization and concentration process, and this development is expected to continue. There is a general agreement on that (see, e.g. Bates and Whittington, 1997, Grunert i.a., 1996, Jørgensen, 1997, Larsen and Grych, 1997).

"Retailing shows equal development tendencies across frontiers. These tendencies may be summarized in the following key words: increasing concentration, increasing integration, change of business area with a tendency to focus on "core business", changes in assortment policy with a tendency to give priority to fresh meat products and own brands, increasing internationalisation, increased use of technology" (Larsen and Grych, 1997, p. 6).

This concentration and integration process is largely a result of a very keen competition, which has resulted in new establishments, competition on prices, acquisition of chains and big mass communication campaigns. Furthermore, the process has been intensified by changed consumer wants as a consequence of their changed situation and the development of new shop concepts like e.g. discount shops. The keen competition has caused that the various actors in the market have made an effort to implement scale economies with regard to purchase, organization of shops, employee training, mass communication and technology. In this way the structural development process has become cumulative - in order to secure one's competitive position it has been necessary to pursue and implement scale economies, and the implementation of scale economies has made it possible to buy other chains which has increased scale economies further.

The process has resulted in a number of demands to producers from retailing. These demands are: increased product development, low prices, quality control, listing fees, trade marks, packaging, JIT delivery etc. In this way the chains have tried to limit their costs, but at the same time they have also tried to differentiate towards the consumers by establishing a profile.

The result of the structural change has been a drastic fall in the traditional kind of shops while the number of supermarkets, hypermarkets, and discount shops has increased considerably. At the same time the number of actors has decreased, and each actor has developed a number of chain concepts that he tries to profile, streamline, and spread to a large geographical area.

We must presume that the process described above will continue in the coming years.

"The most dominant trends in the future retailing structure in all West European countries include concentration, integration, internationalisation, changes in business domain and assortment policy, and the growth of own label". (Grunert, i.a., 1996, p. 131).

The authors of the publication also emphasize formation of cross-frontier purchasing groups among retailers and spreading of discount chains.

Furthermore, we must presume that the described structural development will create barriers to new actors who might want to enter the market. It will be impossible to start from the bottom and expand. The only possibility of entering a given market will be to acquire existing chains, and this will be still more difficult in the future, as the remaining chains grow bigger. Consequently, in the long run we must expect a cemented structure with few large and internationally oriented groups of retail chains.

The power is in the hands of the big retail chains, and consequently they can press their suppliers in all directions and make them deliver goods and services which suit them and their interests - and if they do not, the chains simply choose a more cooperative supplier.

Chains demand central negotiations, annual agreements, control, ability to supply, stable quality, technological and logistical adjustments etc. Chains also demand new products, promotion and mass communication to support sales. At the same time the producers compete for the favour of the still smaller number of chains. Beside the ordinary price competition including discounts, campaign subsidies and fulfilment of delivery and quality demands this competition results in attempts to establish more permanent cooperative relations with the various chains (Grunert, i.a., 1996, Jørgensen, 1997, Jørgensen and Freytag, 1995). The producers cultivate the big customers by means of Key Account Managers; they enter into product development cooperation, develop private brands, deliver according to the chains' specifications, and enter into cooperation about logistics and technology.

The existence as small or medium sized producers is made difficult because of the mentioned demands from the chains. The creation of more permanent relations with one or more big chains demands a certain size.

Now the question is what possibilities a producer under these conditions has to build up relations with chains and thereby maintain a distribution system. As mentioned above, the company's size will be decisive, but to both large, small and medium-sized companies a decisive choice will be what chain/chains the company work first with a view to becoming supplier. Being in one chain may prevent the company from being part of others, and so it may be cut off from considerable market shares in the long run.

Further, large producers must decide if they want to sell their products as their own brand or if they want to produce private brands for the various chains. They must also decide to what extent they want to cooperate with the various chains in the logistics area and to what extent they want to build close relations with these important customers and thus organize their own organization according hereto.

The small and medium-sized producers may only have had the possibility to be represented in the product range of a single chain. It may even be a piece of good luck for a producer to get to be a supplier at all. The producer's capacity can also limit his possibilities of becoming a supplier. These producers, however, probably have to supply the chain's brand.

The chains' incentive to build close relations to the various suppliers, i.e. producers of non-durables, will not be overwhelming – that is not as long as it is easy to find suppliers that can match the different criterion. Firstly, there are many suppliers that each represents a moderate part of the chain's product range, and secondly, a chain may profit from playing off the different suppliers against each other in order to keep the prices down. However, the chain may be interested in building relations to small and medium-sized companies as suppliers of private brands, but here the relationship is not equal. The power of the relationship is fully with the chain.

Thus, the parties in the two levels in the value chain regarding this type of products seem to have different interests in the relationship building and therefore, the producers' attempt to build closer relations by means of the different design parameters may therefore seem wasted. Instead of pursuing a relationship building strategy it would perhaps be more productive to concentrate on rationalisations in the production and logistics in order to keep down the costs, or to develop more unique products. An alternative strategy could be to merge and acquire to make oneself a more attractive partner and to get access to a product range that carries more weight in the chains' product range.

6. Conclusion

This paper has pointed out that there is a need for a tool that can help the companies to formulate a strategy concerning relationship building. The tool could be a contingency model. It must contain a number of situation factors that decide what type of strategy a specific company must follow and it must also contain a number of design parameters that can be used to implement the strategy.

Such a contingency model is be very complex and therefore, an extensive analysis must be made before it is possible to define it. The correlation between the relevant situation factors and the strategy formulation must be analysed closer, and so must the question of how different combinations of situation factors influence the strategy. Such an extensive analysis has not been possible within the framework of this article. In stead, focus has been put on a single situation factor – the value chain – whose influence on the strategy has been discussed on the basis of material regarding the distribution of groceries in Western Europe. The two situation factors, range and company size, has been included to a certain degree.

The analysis shows that the different links in the value chain do not have an equally strong wish for building supplier/customer relations and that this fact has consequences for the companies' strategy. Also, the possibilities for building relations depend on the companies' size and on the types of products and their importance to the customers. Therefore, the "normal" situation in the distributions systems makes a relationship building strategy less relevant for the producers. The conclusion, therefore, is that relationship building in this sector in considerable less relevant than in the B-to-B market. The company's placing in the value chain must be considered an important situation factor.

To the companies the implications are that they must consider their situation closely – from relevant factors – before they plunge into an extensive relationship marketing, and that they must remain critical towards repeated recommendations of this.

This paper analyses only in general a moderate part of the assumed relevant situation factors and deals not with the specific combination of the design variable. Therefore, an extensive research must be made before a more direct applicable contingency model can be defined.

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