Dynamics in Chains and Networks

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SALES PROMOTION ARRANGEMENTS IN THE FMCG CHANNEL

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ABSTRACT

Sales promotions in FMCG involve some form of coordination/cooperation between
manufacturer and retailer. The result is a sales promotion agreement (SPA). First, we examine
which elements are agreed upon in SPAs (e.g. goals, budgets, etc.). Second, we explain the
differences in SPAs (e.g. the characteristics of the parties and of the product). Third, we will
study the success of sales promotions (for the manufacturer, the retailer and the channel) and
how this success is related to the nature of the agreement. The present paper deals with the
first issue, and contains some preliminary findings with respect to the second issue.

Keywords: agreements, promotions, relationship, channels

1. INTRODUCTION

Sales promotions are a diverse collection of incentive tools designed to stimulate faster
and/or larger purchases of products or services by consumers or traders (Kotler, 2000). In this
paper we focus on sales promotion businesses within grocery channels, because of:
• The high frequency of sales promotions in this industry.
• The existence of promotion efficiencies and inefficiencies (e.g. Drèze and Bell, 2003).
   Current sales promotions often do not meet the objectives of the parties involved.

In order to improve sales promotions, it is important to have more insight into the
driving forces and success of sales promotions. Our perspective is the sales promotions
offered to consumers in grocery stores. These promotions can be initiated by the:
• Manufacturer, e.g. coupons on the package.
• Retailer, e.g. price discounts, feature advertising, contests, displays, etc.
• Manufacturer and retailer together, as a joint activity.

Increasing attention has been given to the interaction between retailers and
manufacturers with respect to the coordination of sales and/or brand-driven activities. The
channel literature shows that with coordination satisfying results can be obtained for both
retailer and manufacturer (e.g. Mulhern and Leone, 1991). However, achieving coordination
is difficult, because each party has an incentive that prevents it from achieving the channel
optimum (Jeuland and Shugan, 1983). The suboptimality problem in channels has been
demonstrated for sales promotions in grocery channels (Wierenga and Soethoudt, 2002).
Therefore, it is interesting to study how and why a manufacturer and retailer coordinate their
promotional activities in actual sales promotion arrangements. The most important form of
interaction between a manufacturer and a retailer is the 'annual meeting', which takes place at
the end of the year. In these meetings the parties negotiate the terms of trade, and set the sales
promotion agreement (SPA) for the coming year. This agreement is the focus of our study:
What types of SPAs are made, what are the antecedents (marketing variables and relationships), and what are the consequences (profits and satisfaction) of these agreements?

2. CONCEPTUAL FRAMEWORK AND RESEARCH QUESTIONS

Figure 1 depicts the framework underlying our research. Antecedents (marketing and relationship variables) influence the SPA that will result in certain actions and consequences, and in turn influence the antecedents of subsequent agreements.

**Antecedents**
- Marketing variables (e.g., type of retailer, brand equity, market share)
- Relationship variables (e.g., trust, power, information sharing)

**Sales Promotion Agreement**
- (e.g., budgets, goal, timing)

**Consequences**
- (e.g., satisfaction, turnover, profit)

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Sales Promotion Agreement

First, we concentrate on the nature of SPAs, e.g., the circle in Figure 1. Our first question with regard to SPAs is:

- What are the characteristics of SPAs as they actually occur in practice?

**Antecedents**

Characteristics of the product and parties can cause differences in SPAs. Effects can be distinguished for:

- The retailer (e.g., type of retailer, number of stores, private label share and market share);
- The manufacturer (e.g., brand equity and market share in the product group);
- The product (e.g., product benefits, shelf-life, buying frequency, promotional intensity).

For example, large manufacturers are expected to agree more with monitoring, and a small retailer needs to allow for more monitoring. Also, we expect that parties involved with fresh produce will agree more on the timing of sales promotions than parties involved with dry groceries, because it is more difficult for manufacturers of fresh produce to adapt their supply and production than for manufacturers of dry groceries.

The study of SPAs should be performed within the context of the manufacturer-retailer relationship, because the extent to which activities are co-ordinated depends largely on the relation between the channel actors (Murphy and Heide, 1998). Therefore, we need to take into account effects of the relationship (e.g., on power Frazier and Rody, 1991, and trust Geyskens et al., 1998).

An interesting question is whether marketing and relationship variables have different effects on the SPA. Therefore, we formulate the following research question:

- To what extent do marketing and relationship variables influence SPAs?

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Consequences

Insight has been gained through promotions (e.g., Blattberg et al., 1994):

- What are the effects of different variables on sales?
- What proportion of turnover is contributed by promotions?

In order to provide an answer, we conducted a questionnaire, which enabled us to collect data on the following elements:

- The sales promotion agreement (e.g., type of product);
- Which items were agreed upon;
- Common goal (about the image);
- Budget of the manufacturer;
- Budget of the retailer;
- Type of promotions;
- Promotion period (time and duration);
- Payment method (settling)
- Incentive (an addition to the previously established);
- Monitoring (of the石家庄);
- Advertisement (in the store);
- Evaluation.

The questionnaire was designed to capture the specific agreement on sales promotion, which takes place from June 2003 onward. A total of 200 questionnaires were returned from each of two markets, implying a response rate of 50%.

Sales Promotion Agreement

In the questionnaire, the selected items were agreed upon definitively (AD), with reservation definitively (AR), no negotiation (NR), and an agreement to negotiate (AG).
Insight has been gained into the effectiveness, efficiency and satisfaction of sales promotions (e.g. Blattberg et al., 1995; Neslin, 2002). Our research questions are as follows:

- What are the effects of differences in SPA on the consequences, and what type of SPA contributes most to success?

3. RESEARCH DESIGN

In order to provide answers to the research questions, we carried out a survey using a questionnaire, which enabled us to study SPAs from a broad perspective. The questionnaire consisted of the following elements:

- The sales promotion agreement and its outcomes: respondents were asked to indicate which items were agreed upon in the SPA for the year 2003. The following list of items had been compiled based on preliminary interviews with retail/manufacturer managers and from the literature:
  - Common goal (about the contribution of sales promotions to turnover and brand/store image);
  - Budget of the manufacturer;
  - Budget of the retailer;
  - Type of promotions;
  - Promotion period (timing of sales promotions in the year);
  - Payment method (settling of the discount);
  - Incentive (an additional ex-post discount for the retailer, for example, when a previously established sales target was achieved);
  - Monitoring (of the store environment by the manufacturer);
  - Advertisement (in the retailer magazine);
  - Evaluation.

- Decision making around SPAs (ideas, content, initiative, and timing);

- Interaction processes: frequency of face-to-face contact, type of relationship;

- Characteristics of the parties: private label share, store area (m²), type of store formula, brand type, market share;

- Relationship variables: trust (Kumar et al., 1995), power (Frazier and Rody, 1991) and satisfaction (Geyskens and Steenkamp, 2000).

The questionnaire was sent to category managers of retailers of four product groups: dairy desserts, ketchup/mayonnaise, carbonated beverages, and margarine. The data collection took place from June 2003 until November 2003. Of the questionnaires sent out, 26 were returned from each of two manufacturers; thus we have information from 52 SPAs. The 26 questionnaires returned imply a response rate of 51%.

4. EMPIRICAL ANALYSIS

Sales Promotion Agreements Defined

In the questionnaire, the respondents were asked to indicate which of the ten pre-selected items were agreed upon in the SPA, and whether each had been agreed upon definitively (AD), with reservation (AR), or not at all (Å). If the parties agreed on an item definitively (AD), no negotiations took place about the item for the rest of the year. If the
parties agreed on an item with reservation (AR), the agreement was conditional and flexible for both parties.

As can be seen from Table 1, items with high scores of AD were budget of the manufacturer (39 cases - 81%), and common goal and payment method (both 30 cases - 63%).

In contrast, items with low scores of AD were budget of the retailer, promotion period, type of promotion, and evaluation. Interestingly, the budget of the manufacturer was agreed upon definitively in most SPAs, whereas the budget of the retailer was agreed upon definitively in a minority only of the SPAs (8%). Some asymmetry was expected, as it is very common for retailers to demand promotion allowances (e.g. Mulhern and Leone, 1991).

Items with high scores on AR were type of promotion in (30 cases - 63%) and promotion period (28 cases - 58%). These items are particularly relevant in the tactical completion of the SPAs, and through this type of agreement the parties are still in the position to react to market circumstances. Apparently, the type of promotion, promotion period, incentives, and evaluation are agreed on per sales promotion, rather than for the full period.

Table 1 Frequency and percentage an item is agreed upon definitively (AD), with reservation (AR), and at all (AD and AR combined) in a SPA. The item score expresses the extent to which an item is agreed upon in an SPA (n=48).

<table>
<thead>
<tr>
<th>Item score</th>
<th>AD</th>
<th>AR</th>
<th>AD + AR</th>
</tr>
</thead>
<tbody>
<tr>
<td>Common Goal</td>
<td>30</td>
<td>17</td>
<td>47</td>
</tr>
<tr>
<td>Budget Manufacturer</td>
<td>39</td>
<td>8</td>
<td>47</td>
</tr>
<tr>
<td>Budget Retailer</td>
<td>4</td>
<td>9</td>
<td>23</td>
</tr>
<tr>
<td>Type Promotion</td>
<td>8</td>
<td>30</td>
<td>38</td>
</tr>
<tr>
<td>Promotion Period</td>
<td>6</td>
<td>28</td>
<td>34</td>
</tr>
<tr>
<td>Payment Method</td>
<td>30</td>
<td>12</td>
<td>42</td>
</tr>
<tr>
<td>Incentive</td>
<td>0</td>
<td>23</td>
<td>23</td>
</tr>
<tr>
<td>Monitoring</td>
<td>21</td>
<td>7</td>
<td>28</td>
</tr>
<tr>
<td>Advertisement</td>
<td>23</td>
<td>14</td>
<td>37</td>
</tr>
<tr>
<td>Evaluation</td>
<td>8</td>
<td>23</td>
<td>31</td>
</tr>
</tbody>
</table>

Table 2. Rotated factor loadings of agreement items (AD, AR, and AD + AR) for component 1 explained 44% of variance.

Correlation coefficients were computed as input for the factor analysis that resulted in the loadings as depicted in Table 2. For the calculation a new variable was created: 3= agreed definitively (AD); 2= agreed with reservation (AR); and 1= not agreed (A). The first component (variance explained = 44%) characterises SPAs. Apparently, the extent to which the financial implication for the retailer is agreed upon is a pivotal element in SPAs. The financial well-being of the manufacturer is a less important characteristic of SPAs, represented in component 2.
was conditional and flexible. Of AD were budget of the method (both 30 cases - 63%).

The retailer, promotion period, the manufacturer was agreed. A retailer was agreed upon anyway was expected, as it is very rare and Leone, 1991).

in (30 cases - 63%) and largely relevant in the tactical parties are still in the position promotion, promotion period, here than for the full period.

sitivity (AD), with reservation score expresses the extent to

<table>
<thead>
<tr>
<th>Component</th>
<th>1</th>
<th>2</th>
<th>3</th>
</tr>
</thead>
<tbody>
<tr>
<td>Cogoal</td>
<td>0.720</td>
<td>0.145</td>
<td>-0.018</td>
</tr>
<tr>
<td>Budgmf</td>
<td>0.199</td>
<td>0.767</td>
<td>0.273</td>
</tr>
<tr>
<td>Budgrt</td>
<td>0.838</td>
<td>0.069</td>
<td>0.099</td>
</tr>
<tr>
<td>Typepp</td>
<td>-0.046</td>
<td>0.128</td>
<td>0.945</td>
</tr>
<tr>
<td>Period</td>
<td>0.421</td>
<td>0.704</td>
<td>0.103</td>
</tr>
<tr>
<td>Paymen</td>
<td>0.086</td>
<td>0.893</td>
<td>0.188</td>
</tr>
<tr>
<td>Incent</td>
<td>0.722</td>
<td>0.193</td>
<td>0.410</td>
</tr>
<tr>
<td>Monito</td>
<td>0.405</td>
<td>0.236</td>
<td>0.411</td>
</tr>
<tr>
<td>Advert</td>
<td>0.515</td>
<td>0.595</td>
<td>-0.014</td>
</tr>
<tr>
<td>Evalua</td>
<td>0.533</td>
<td>0.293</td>
<td>0.643</td>
</tr>
</tbody>
</table>

The variables are scored as follows: 3=AD; 2=AR; 1=A. Cut-off for loadings >0.70 (.75 in a sample of 50, Hair et al., 1998)

For identification of a hierarchy between items in SPAs, the Guttman analysis was performed. The analysis implies the presence of hierarchy of a criterion (agreement on an item) in a set of cases, e.g. an item is agreed upon if a successive item is also agreed upon. The response categories used were in the form of yes/no answers (Yes = AD+AR; No = A).

The scaling coefficients (Hij coefficients) for the items were then calculated (Mokken, 1971). Table 3 depicts these coefficients for the items included in SPAs. The final row summarises the frequency that an item is dominant over another item. For example, type of promotion is agreed upon when budget of the manufacturer, common goal, and payment are also agreed upon.

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<table>
<thead>
<tr>
<th>Hij</th>
<th>Cogoal</th>
<th>Budgmf</th>
<th>Typepp</th>
<th>Period</th>
<th>Paymen</th>
<th>Incent</th>
<th>Monito</th>
<th>Advert</th>
<th>Evalua</th>
</tr>
</thead>
<tbody>
<tr>
<td>Cogoal</td>
<td>1</td>
<td>1</td>
<td>1</td>
<td>1</td>
<td>1</td>
<td>1</td>
<td>1</td>
<td>1</td>
<td>1</td>
</tr>
<tr>
<td>Budgmf</td>
<td>1</td>
<td>1</td>
<td>1</td>
<td>1</td>
<td>1</td>
<td>1</td>
<td>1</td>
<td>1</td>
<td>1</td>
</tr>
<tr>
<td>Budgrt</td>
<td>0.0</td>
<td>0.0</td>
<td>0.0</td>
<td>0.0</td>
<td>0.0</td>
<td>0.0</td>
<td>0.0</td>
<td>0.0</td>
<td>0.0</td>
</tr>
<tr>
<td>Typepp</td>
<td>0.0</td>
<td>0.0</td>
<td>0.0</td>
<td>0.0</td>
<td>0.0</td>
<td>0.0</td>
<td>0.0</td>
<td>0.0</td>
<td>0.0</td>
</tr>
<tr>
<td>Period</td>
<td>0.1</td>
<td>0.1</td>
<td>0.1</td>
<td>0.1</td>
<td>0.1</td>
<td>0.1</td>
<td>0.1</td>
<td>0.1</td>
<td>0.1</td>
</tr>
<tr>
<td>Paymen</td>
<td>0.1</td>
<td>0.4</td>
<td>0.4</td>
<td>0.5</td>
<td>0.5</td>
<td>0.5</td>
<td>0.5</td>
<td>0.5</td>
<td>0.5</td>
</tr>
<tr>
<td>Incent</td>
<td>0.0</td>
<td>0.0</td>
<td>0.0</td>
<td>0.0</td>
<td>0.0</td>
<td>0.0</td>
<td>0.0</td>
<td>0.0</td>
<td>0.0</td>
</tr>
<tr>
<td>Monito</td>
<td>0.0</td>
<td>0.4</td>
<td>0.4</td>
<td>0.4</td>
<td>0.4</td>
<td>0.4</td>
<td>0.4</td>
<td>0.4</td>
<td>0.4</td>
</tr>
<tr>
<td>Advert</td>
<td>0.1</td>
<td>0.6</td>
<td>0.6</td>
<td>0.6</td>
<td>0.6</td>
<td>0.6</td>
<td>0.6</td>
<td>0.6</td>
<td>0.6</td>
</tr>
<tr>
<td>Evalua</td>
<td>0.0</td>
<td>0.5</td>
<td>0.5</td>
<td>0.4</td>
<td>0.4</td>
<td>0.4</td>
<td>0.4</td>
<td>0.4</td>
<td>0.4</td>
</tr>
<tr>
<td>Total</td>
<td>7</td>
<td>3</td>
<td>4</td>
<td>2</td>
<td>5</td>
<td>2</td>
<td>5</td>
<td>2</td>
<td>5</td>
</tr>
</tbody>
</table>
Clearly, the budget of the retailer and incentives, both seven dominant coefficients, are most difficult to agree upon. Therefore these items have the highest position in the hierarchy: these are the key elements in SPAs. In a study by Murry and Heide (1998) several factors were raised for attractive SPAs for the retailer. In that study as well, incentives appeared to be very important.

Hierarchical structure in SPAs:

High
Budget Retailer / Incentive
Evaluation
Monitoring
Period
Type of Promotion
Payment / Advertisement
Budget Manufacturer / Common Goal
Low

Determinants of Sales Promotion Agreements
A preliminary analysis of the effects of product-group characteristics on the ten items of SPAs was performed. Table 4 depicts the significant relations. Differences in product-groups have an effect on agreement of the budget of the manufacturer (F = 3.55, p < 0.05), promotion period (F = 6.54, p < 0.05), and incentive (F = 5.41, p < 0.05). For beverages, the parties make significantly more agreements on these items, than they do for desserts. The manufacturers of beverages are global and wealthy players compared to the manufacturers of dairy desserts. This makes it easier for the retailer to obtain a promotion budget from the manufacturers of beverages. However, these manufacturers can enforce agreement on more items, apparently the promotion period, which is advantageous for the manufacturer.

Table 4. Relation between product-group (dairy desserts, carbonated beverages, ketchup/mayonnaise, and margarine) and an item agreed upon in the SPA.

<table>
<thead>
<tr>
<th></th>
<th>F</th>
<th>Sig.</th>
<th>Product-group</th>
<th>Mean</th>
<th>Std. Error</th>
</tr>
</thead>
<tbody>
<tr>
<td>Budget of manufacturer</td>
<td>3.55</td>
<td>.022</td>
<td>Desserts</td>
<td>2.53</td>
<td>.103</td>
</tr>
<tr>
<td></td>
<td></td>
<td></td>
<td>Beverages</td>
<td>3.00</td>
<td>.118</td>
</tr>
<tr>
<td></td>
<td></td>
<td></td>
<td>Ketchup</td>
<td>2.88</td>
<td>.107</td>
</tr>
<tr>
<td></td>
<td></td>
<td></td>
<td>Margarine</td>
<td>3.00</td>
<td>.301</td>
</tr>
<tr>
<td>Promotion period</td>
<td>6.54</td>
<td>.001</td>
<td>Desserts</td>
<td>1.47</td>
<td>.131</td>
</tr>
<tr>
<td></td>
<td></td>
<td></td>
<td>Beverages</td>
<td>2.08</td>
<td>.150</td>
</tr>
<tr>
<td></td>
<td></td>
<td></td>
<td>Ketchup</td>
<td>1.88</td>
<td>.135</td>
</tr>
<tr>
<td></td>
<td></td>
<td></td>
<td>Margarine</td>
<td>3.00</td>
<td>.383</td>
</tr>
<tr>
<td>Incentives</td>
<td>5.41</td>
<td>.003</td>
<td>Desserts</td>
<td>1.24</td>
<td>.108</td>
</tr>
<tr>
<td></td>
<td></td>
<td></td>
<td>Beverages</td>
<td>1.85</td>
<td>.124</td>
</tr>
<tr>
<td></td>
<td></td>
<td></td>
<td>Ketchup</td>
<td>1.50</td>
<td>.111</td>
</tr>
<tr>
<td></td>
<td></td>
<td></td>
<td>Margarine</td>
<td>1.00</td>
<td>.315</td>
</tr>
</tbody>
</table>

p < 0.05
in the hierarchy:

In the study of Blattberg, R.C., R. Briesch and E. J. Fox, 1995, they found that promotions work by creating win-win trade promotions. This aligns with the findings of Drèze, X. and D.R. Bell, 2003, who also identified the importance of creating win-win trade promotions.

The study by Geyskens, I., J.E.M. Steenkamp and N. Kumar, 1998, highlighted the importance of trust in marketing channel relationships. This is consistent with the findings of Geyskens, I. and J.E.M. Steenkamp, 2000, who emphasized the economic and social satisfaction in marketing channel relationships.

The study by Mokken, R.J., 1971, provided a theoretical framework for scale analysis. This is relevant to the findings of Mulhern, F. J. and R.P. Leone, 1991, who explored implicit price bundling of retail products.

The study by Wierenga, B. and J.M. Soethoudt, 2002, investigated the suboptimality of sales promotions and improvement through channel coordination. This aligns with the findings of Neslin, S.A., 2002, who focused on sales promotion.

5. CONCLUSIONS

This paper presented the items that are agreed upon in SPAs, from a retailer perspective. Asymmetry is present in agreement on the budgets of the parties. The extent to which the financial implications for the retailer are agreed upon is a pivotal element in SPAs, and also the most difficult item as it is not agreed upon before there is agreement on the other items. This result could be caused by the fact that the analysis is performed from the perspective of the retailer. Therefore it would be interesting to know if the same patterns emerge from a manufacturer perspective.

REFERENCES