Retail Management
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Lecture-42
Special Merchandising Contexts-2

Hello everybody, welcome to this NPTEL swayam course on retail management, this is Professor Swagato Chatterjee from VGSOM, IIT-Kharagpur who is taking this course for you. We are in week 8, this is lecture 42 and I will be discussing about special merchandising context 2. The last video we also talked about certain special merchandise in context, we are continuing the discussion in this class as well.

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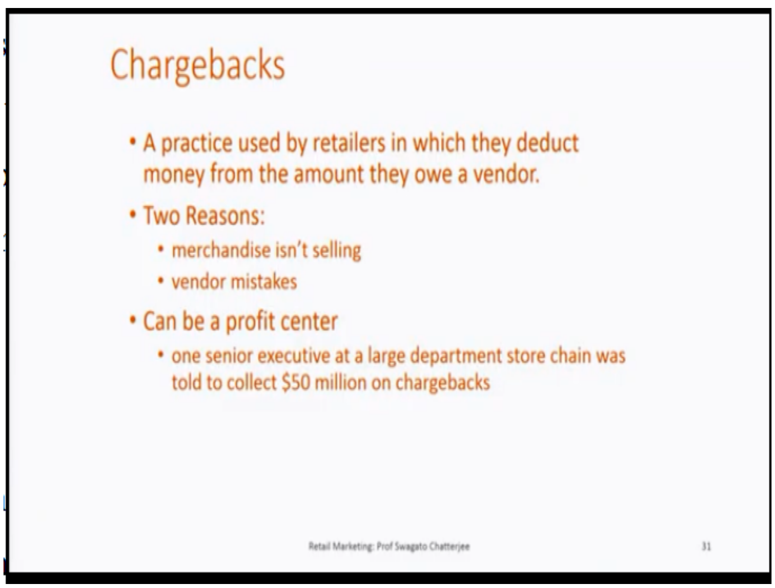

Now in the last class at the end of the last class we discussed about certain ethical issues that can come up and one of those ethical issues was bribing. And now we will talk about something called chargeback. What is chargeback? It is a practice used by retailers in which they deduct money from the amount they owe to a vendor for 2 reasons majorly. Merchandise is not selling or vendor does done some mistakes, so this is called chargeback.

So, you have already made a deal but sometimes if you have more negotiation power or in the supply chain you are the powerful person then sometimes vendor has to follow whatever you are saying. And you might not want to take the pressure of the non-sale or inventory buildup of the merchandises in your retail store, so you pass it on to the vendor. And the vendor is generally taking up this particular issue or they consider this particular issue because they do not have the negotiation power.

And they think that the relationship with this retailer is very important for them, they want to keep on going with this relationship because they are feeling that ok, it might be a some a little bit less profit in this particular term. But if I can give any kind of better product or better services in the next term the overall revenue or overall profit will go up. So, these are majorly 2 reasons one is merchandise is not selling.

And now this can be a profit center, for example see one senior executive at a large departmental store chain was told to collect 50 million on chargebacks. Now if you can collect that much money for chargeback for basically any kind of vendor mistake or any kind of merchandise not selling that kind of a condition that itself that particular money can be a huge profit center for the retailer.

So, retailer keeps on finding out the loopholes in the whole process whether the vendor has delayed in delivering, whether the vendor have not delivered whatever they wanted to order whatever as per the rule. So, some small, small loopholes they pick it up and they sometimes inflate it and show that this is a very big problem. And that is how they sometimes ask for chargebacks which oftentimes can become a negative issue.

Oftentimes can also become a unethical issue, probably the problem is not that much bigger problem but you know that if I can inflate it and if I can negotiate on that then I can get a quite a bit of discount, quite a bit of chargeback money. So, that is where the retailers also start playing.

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Then another thing which comes very common which is called slotting allowance. So, this is the fees paid by a vendor for a space in a retail store, so not only when you are selling your product, not only you are giving certain kind of margin to the retailer to get the favourable position in the retail store also you should ensure that you give some money. It is like in the airline when you are going taking a trip in a airline you want to have a favourite seat and for the favourite seat you have to pay more.

So, similar kind of thing, why slotting allowances why there is a favourable position? Because there are certain positions in the retail store where the visibility will be high, for example anything in the eye level the visibility will be high, anything a little bit above of the eye level is something where the brands are more I would say the celebrated. And anything which is below the ground level their brands are generally not seen in a good line.

So, this kind of psychological process goes in the mind. Similarly at the corner of the aisle probably that is not a favourable position because visibility at that point is very low. Many people will basically ignore the corner and go to the next aisle probably, so the corner slots I would say below slots or 2 above slot where it is not possible to reach by common person, this kind of slots are not favourable positions.

On the other hand middle slot, middle in terms of the width I am saying and in terms of height in the eye level or a little bit above the eye level these are the areas where it is preferred slots. And to get your brands, get your products in those preferred slots you have to pay certain amount of slotting fees. So, slot entry at this moment is not legal activity, so what they do is they come they bridge this particular thing inside the deal itself.

So, whenever you are writing a contract you might also probably you might give a hint that if the percentage of sales is this much, say this much money will be given, if the percentage of sales is that much, that much money will be given. So, that is sometimes trying to push the slotting fee because you cannot say in the deal that I have to give this particular slot to you, that is something which is not legal.

Because if you are charging for the slotting fee also then there has to be a tax component for that particular space as well. Now how retailers will actually manage these components and how they will give service tax or goods tax is something that is a question till now? So, it is not legal. Retailers argue that there is a reasonable method for ensuring that their valuable space is used efficiently.

So, retailers want this kind of slotting fee to be legal. So, they charge in one way or other they charge, sometimes not as a monetary component, sometimes some other component like let us say certain benefits, certain huge margin discounts or probably certain amount of fringe benefits that they sometimes ask for this slotting fee. Because they know that unless there is a fee, there is a formal kind of recognition of this particular service that the retailer is providing to the manufacturer.

Unless there is a recognition there will be very less incentive for a retailer to put a particular brand in a particular position. So, they are valuable positions, the value of various positions will not be totally realized which is a problem. Manufacturers on the other hand view them as an extraction and that because till now retailers and manufacturers are competing each other and as of today manufacturers are more stronger than retailers till now.

That is why this slotting fee has remained as a basically what I would say as an illegal kind of a activity. However over time this will change, because for example in the e-commerce setup we actually ask for slotting fee. For example in the sorting when you search some product descriptions comes up we actually pay advertisements fees to come up at the top and their ads are written.

So, as long as those kind of special the things are mentioned in the e-commerce that ok, there will be no slotting fee but there will be a separate component there in the retail store which we where you can put your product as a advertisement expenditure as well. So, if you allow that, is probably possible to be done because that is what is happening in the e-commerce site as well. Nine billion dollars, so 16% of all new product introduction costs in grocery industry are basically slotting fees.

So, this is a very important, so any new grocery product that you are bringing in has to be given a favourable position to push the initial campaign or promotions that we are doing and that is why it is not very, very mere amount, it is 16% of the total cost of grocery industry, so there is a very big amount which is also come up as a slotting allowance. Now why slotting allowance is one kind of extraction from retailers?

Because manufacturers think that this is something that they are charging to them just because they have the space. So, it is like a bullying the manufacturers, they sometimes feel like that. So, this is also an ethical concern whether you want to do or do not want to do how will you do it, in what cover you will do it? It is something that has to be discussed. But this makes sense because if there is space and consumer behaviours are different.

Actually it was considered for the manufacturers as an extraction because consumer behaviour probably 10 years back have not supported that or there was no evidence that people have different kind of behaviour to different kind of slots. But things have changed now and it is actually true that people give different kind of preferences to products which has put in different positions.

So, if those things are actually true now, if that has been proved by experiments then it has to be taken care of in the pricing as well irrespective of the cost of the product or the margin share that people are doing.

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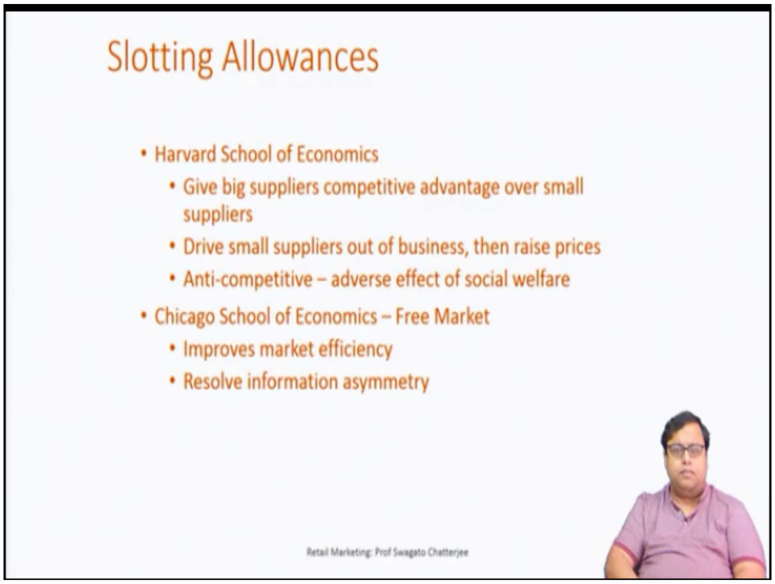

So, Harvard schools of economics are given big suppliers competitive advantage over small suppliers, obviously. So, big suppliers want to even if their product is not so good they can pay the slotting fee and put up their product at a particular position where there will be no fair competition anymore. So, that is something that sometimes they say. Drive small suppliers out of business then raise prices, so it might create a monopoly kind of situation or oligopoly kind of situation while small suppliers.

Because they cannot pay the slotting fee they will be out of the market and it is anti-competitive that is why it has an adverse effect on social welfare. So, however Chicago school of economics which is more opinionated towards or not opinionated more I would say inclined towards free market, they say that it improves market efficiency and resolve information asymmetry because ultimately based on the actual value of a particular slot you are paying.

Now you see the similar kind of thing is done in advertising also, so a sales goes increasing, sales gets increased when you do advertisement expenditure. And there is no limit of how much advertisement expenditure you are allowed to do, you can do as much and obviously a big seller can do more advertisement expenditure than a small seller. Now if you say that ok favourable positions are taken by the big competitive companies because of slotting allowance and etcetera, etcetera.

I will name it something else, I will say that ok this rack to this rack all my favourable positions are basically advertisement racks. And you can put the your products there to advertise your new entries your whatever, whatever**.** So, people can charge that as a advertisement racks because those kind of racks are there in commercial stores. So, just this anti-competitive is a term which Harvard school of economics comes up with but however there are these markets itself is a anti-competitive market where small players have to fight a lot to make a space for in front of the big player.

So, it is not like your access towards the market is actually being stopped, nobody is stopping your access you can also have your product position in the retail store. But sometimes if this happens that big suppliers buy out the whole retail store itself then that is a problem. So, that cannot be allowed and that probably people can put a limit or regulators can put a limit that what percentage of a retail store can be advertisement oriented or something like that. However, there are options even today there are options to bring in slotting allowance in the context of organization.

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Next topic that I will be discussing is called buyback, where is buyback? It is used to get product into the retail stores. For example there are 2 scenarios where the buyback comes in. Retailer allows a vendor to create space for it is goods by buying back a competitors inventory and removing it from a retailer system. So, it allows the vendor to create space, means it is basically they are saying that why do not you do one thing, you buy out the competitors whatever your product is there, your competitor's product is there.

You buy your competitors product and then remove it from the retailer system and then you put your product. So, then you will get more space which is again a probably an unethical way of doing it where you are basically not letting your competitors product reach to the customer. Retailer forces a vendor to buyback slow moving merchandise, so sometimes if there is a merchandise which is very slow moving which is not selling a lot, to make space you might push a particular good high moving vendor that ok why do not you buyback that?

So, if you buyback then you can put more products from your high moving product list in my retail setups. And then what happens is whatever investment I did actually to buy the slow moving products basically and I made a mistake, that mistake is taken care of. Because now I can basically make money from that buybacks where a high moving product seller or vendor is buying a slow moving product irrespective of whether it is it is competitor or not and then making his space.

So, it is like let us say I bought certain detergent A, so detergent A from brand A I bought as a retailer and never wanted to sell but detergent A is very slow moving. But I have already bought quite a bit, so I cannot sell it to the customers or these are basically taking space in my retail store, so what can I do? I can either discard or give discounts or something like that, so I feel that if I ask and then there is another person who is let us say selling certain kind of I would say it is not detergent, let us say some floor cleaner.

So, floor cleaner B let us say and now floor cleaner B is very high moving product let us assume. So, I will go and say to (()) (16:06) why do not you buy this detergent A? Buy this detergent A and then sell it off or do whatever you want to do, I will give you some discount. But if you buy the whole bulk you will get the whole space and then I can allocate that space to you.

So, this is a buyback situation where I made a wrong investment as a retailer but that is taken care of by a high moving kind of a vendor. Now high moving vendor is also think that ok, ok, if I make out this space I am investing some amount of money through but if I make out this space then I can you to keep on utilizing this space. It is not one time period I can use it for multiple time periods, so my high moving product will be sold in a huge volume and that will be beneficial for me.

So, that is something that where buybacks comes in, again it might be unethical because you are actually asking one person to buy out all the products which are slow moving and they are basically not reaching to the customer. And if by chance if it is a competitor's item then you are basically ensuring that the competitor’s item does not reach to the customers and customers do not know about your competition. So, market reaches of your competition you are cutting it down, probably unethically, so that is also a question.

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Then counterfeit merchandise. So, goods made and sold without the permission of the owner of a trademark, a copyright or a patented invention that is legally protected in the country where it is marketed. So, you are basically creating products of the same design or same kind of features but you are not taking permission or you are not telling your brand owner or you are not telling the copyright owner and you have made it. So, it is a major problem is in counterfeiting intellectual property, it is counterfeited like anything.

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So, what to do about counterfeits? So, trademark, copyright and patent products in the countries in which they are sold, so if you try to sell them separately in the counter product that is a problem. So, US government is engaged in bilateral and multilateral negotiations, multicultural negotiations and education to limit counterfeiting. Similar kinds of activities are done in India also by department of consumer affairs to how to identify counterfeits?

How to identify the ISO trademarks? And this various trademarks which is trying to BIS trademark which is trying to say that this is a right item, you have bought a right particular thing. Hallmarks are there in the case of gold, there are other tags, GI tags are there for different kind of geographically focused products. So, you cannot go for counterfeits or there are policies or there are strategies to identify and manage the counterfeits. However still counterfeits comes up in the retail store.

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So, what kind of things happen? So, there is something called gray-market and diverted merchandise. So, what is gray-market merchandise? Gray-market merchandise possesses a valid US registered trademark. So, they are not counterfeit, they are more or less legal. So, they have a valid US registered or in different countries that register trademark and is made by a foreign manufacturer but is important to the country without the permission of the trademark owner, so that is a gray-market.

So, it is coming inside the market and it is sold in the flea market or gray-market. Even in India we will find lots of gray-markets in various cities, there will be china bazaars and these and that where you will get electronics items or jeans or these and that at very low price. So, they are basically actual products but are sold without the permission of the trademark owner or copyright owner.

Another diverted merchandise is similar to gray-market merchandise except that there need to be distribution across international boundaries. So, when you send one product to another you will see diverted merchandise kind of markets comes up in border areas a lot. For example if you go to the Darjeeling in West Bengal there is a small city called Medin where if you go a little bit ahead there is the Nepal border.

From Nepal border there are lots of in the border area lots of trade happens of garments and these and that and meeting bazaar is known for that kind of diverted merchandise, people go there and get to buy products at a very lower cost. Now sometimes this has become a part of your identity, part of a culture that it has been there for so long where it has become a culture for very long time why because it was further more true in Indian context because India had liberalization 1991 and from then onward you got lots of products which are foreign products, better quality production.

Later we learnt how to create better quality day-to-day consumer products in India. But before 1991 day-to-day consumer products, consumer apparel etcetera was not of that good quality inside the country, so what happened? It used to get imported and import was stopped to take care of Indian industry but people used to this import used to come from different sources with different lines. So, one of those are this kind of diverted merchandise.

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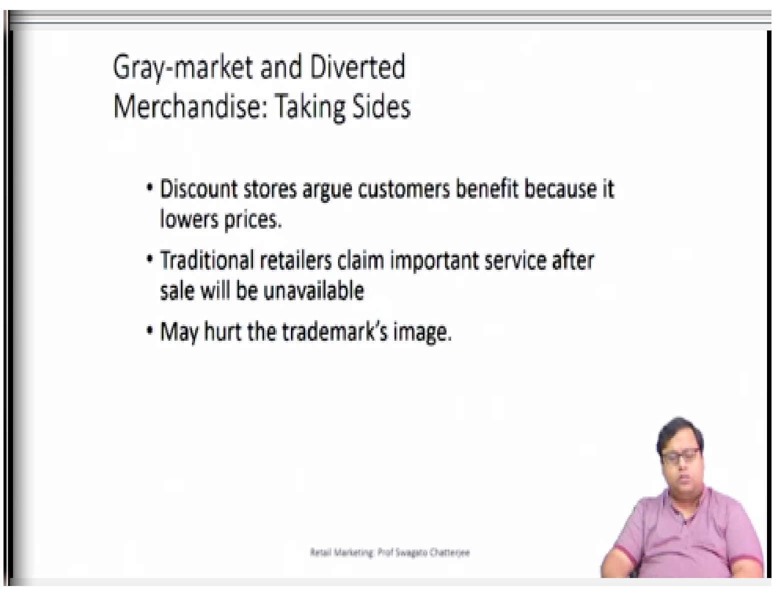

So, discount stores argue that customers benefit because it lowers prices. So, whoever selling this kind of gray-market and diverted merchandise they think that customer gets benefit obviously. But traditional retailers claim important service after sale will be unavailable, so the customer should not go there and they should buy from us. And trademark owners think that ok, this is hurting my image, this is hurting my brand value, so this is not good.

So, there will be 2 side of the story customers might feel that ok, I should get the product at the lower cost, actually I have to pay for the brand name a lot. And the trademark say that ok this brand name is something that I am giving because I am giving value, you do not know what will be the service provided whether there will be alteration, whether there will be any kind of changes if quality issues comes up they will not take care of that.

Customers might feel that ok; I do not need those things. So, there will be always 2 sets of customers who need the brand name in originality, who need all these services and all these promises in originality. And there are other group of customers who want to take risk, so although there are laws and rules and etcetera these kinds of things will always remain obviously in different proportions. And some customers will always go to this gray-market and diverted merchandise to buy products and some other customers will not want to go there.

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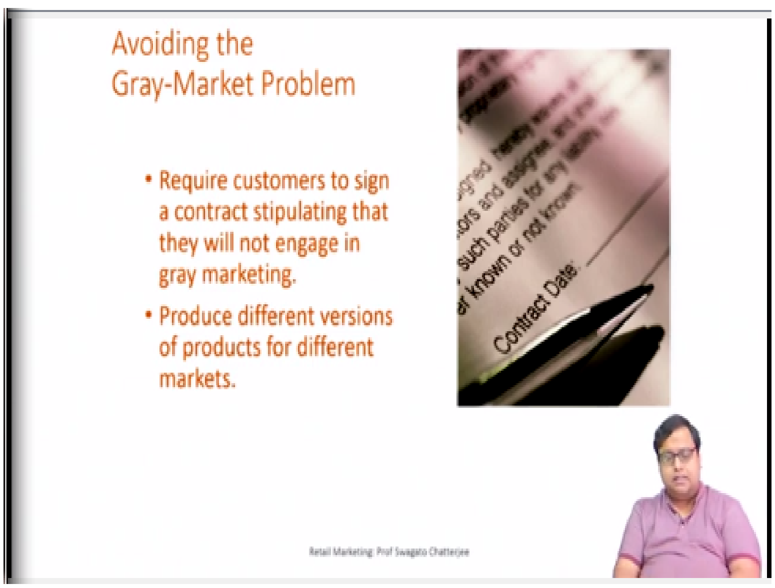

How to avoid this gray-market problem? It require customers to sign a contract stipulating that they will not engage in gray marketing which is very difficult to do and product different to produce different versions of product for different markets. So, sometimes bigger brands do that for a market where the purchasing power is not so high, let us say developing countries they produce one particular type of product.

Very common in let us say books let us say, at one point of time what we used to do that we had hard cover books only, foreign printed very, very glossy kind of papers. And then what people used to do is take print outs of them or take xeroxes of them and still going on. However, to (()) (23:55) to this market these publishers have created 2 different kinds of products, one is for foreign market, one is for developing countries which is let us say paperback version.

So, paperback version will be not so glossy kind of the binding will be not so hard or the paper should be not so glossy or the prints will be not colour prints there will be black and white prints or something like that to cater to 2 different kinds of markets, so that is something that is possible. And what other things are possible? Also this thing is possible that you sometimes come up with the probably off-sell market.

So, we talked about that in a previous class where you can sell your products in a rejects kind of a market also. So, you have a bigger brand store and you have those smaller store somewhere, your product the same brand names product will be sold at a lesser price and some a little bit of quality issues will be there or non recognizable quality issues may be there or certain older inventory will be sold. So, those kinds of things are also put up. So, that a person can legitimately buy a product which is not selling or but coming from the same brand name.

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Then another ethical issue is or special issue I will not say ethical issue, it is a special issues which is called exclusive territories. So, it is granted to retailers, so no other retailer in the territory can sell a particular brand. It benefits vendors by assuring them that quality retailers represent their products. So, you are do not want to make sure that you are saying that the retailer's who will be selling in various parts should be quality retailers.

They should present the brand name or the products, manufacturer brands image very strongly. It assures retailers with adequate supply, grant retailers a monopoly but it illegal's when they restrict competition. So, by chance us say if you are trying to put up this kind of retail stores where you are not ensuring any other competing retailer can come up that sometimes can be a illegal issue.

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Exclusive dealing agreements, so occur when a manufacturer or a wholesaler restricts a retailer into carrying out it is products and nothing from competing vendors. So, probably let us say illegal one also the restrict competition for example let us say if sometimes Pepsi and Coca-Cola have seen this kind of problem. That you go to a retail store you get Pepsi's product and they say that ok, we only carry Pepsi's product, we do not have Coco-Cola's product and vice versa.

Probably there is no exclusive dealing agreement is there in pen and paper but there will be certain informal kind of association that ok you can only sell my product or you cannot. I will pay you more if you do not sell other person's product or if you put that with other particular manufacturer's products at the back of the retail store and my product the front of the retail store, something like that can be done. And these are very common in Indian context more so on those kind of markets where regulations are not reached at such a high level probably on those kind of market this kind of problems are there.

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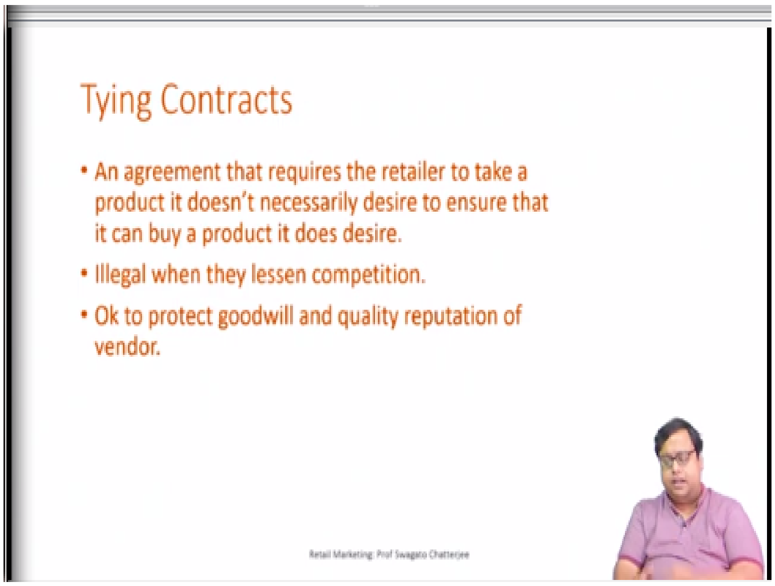

Tying contracts, it is an agreement that requires the retailer to take a product it does not necessarily desire to ensure that it can buy a product in does desire. So, you tie it up, you say that ok if you want to buy this product from me and sell it to somebody else you have to buy the other product also. So, probably there will be a very high moving product and the manufacturer now is tagging a low moving product along with it and selling it off.

So, that is also illegal when they lessen competition and ok to protect goodwill and quality reputation of the vendor but not always it might be not something that the retailer want to have. So, not only the retailer can create problems for the vendor within ethical issues for the vendor, the vendor can also create ethical issues or ethical delivers or ethical challenges for the retailer.

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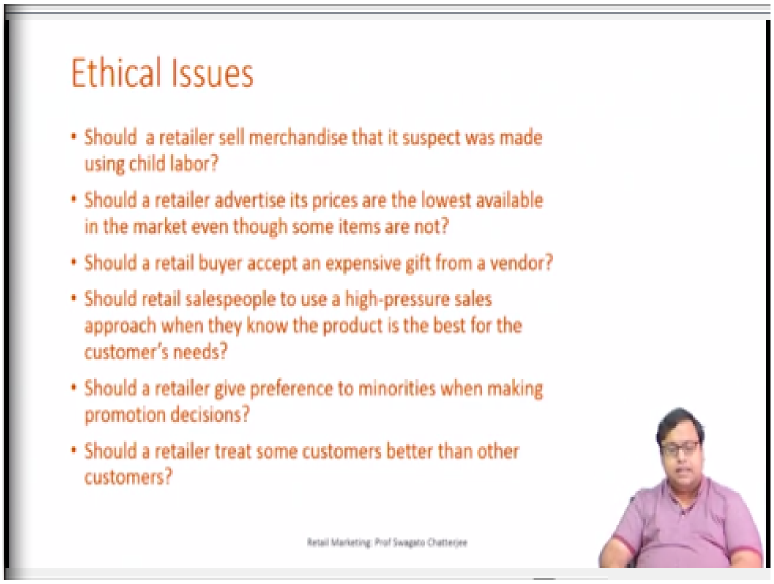

Now what other kind of small, small ethical issues can come up? Should a retailer sell merchandise that it suspect was made using child labour? It is a very common problem in many developing countries or even developed countries but the sourcing is coming from developing or underdeveloped countries. Should a retailer advertise this prices are the lowest available in the market even though the some items are not?

So, often retailers do that this the lowest price guarantee and if you find out somewhere else I will give you the balance. So, that is a wrong, so there will be some amount, so there are papers which say that this is a good strategy. Because there will be always some informed customer and some uninformed customer, informed customer will basically take the lower price and the uninformed customer will take the higher price.

And there is very low chance that the uninformed customer will talk about that to the informed customer because that customer to customer talking is not happening in a retail context if it is a FMCG kind of retailer, general merchandise retailer. So, often retailers take this strategy, question is whether that is ethical or not? Should a retail buyer accept an expensive gift from the vendor obviously the driving thing comes up?

Should retail sales people to use should be allowed to use a high pressure sales approach when they know that the product is best for the customer needs? So, can push sales should be done in the detail context. Should a regular give preference to minorities when making promotion decisions? So, this is a question that ok I want to be minority friendly, so should my promotion be also related to minorities that if you are from a minority group you will get higher points or higher discounts and etcetera? That can be a question. Should a retailer treat some customers better than other customers? So, should there be any discrimination?

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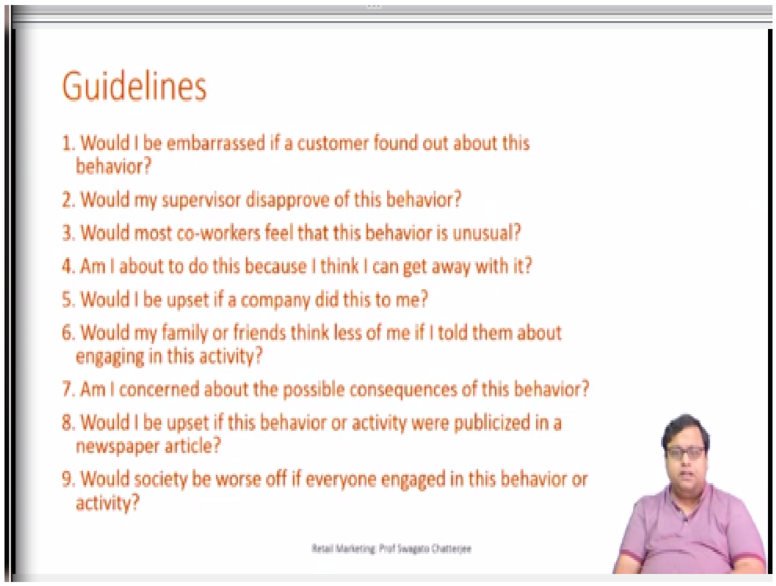

Sometimes that is there because of the loyalty of the customers and etcetera, so whether that is. There are certain other guidelines also, so would I be embarrassed if a customer found out about this behaviour, would my supervisor disapprove this behaviour? So, whatever you want to do, you have to ask these questions and try to have more yes or basically not always yes more favourable answers from these questions.

Would most co-workers feel this behaviour is unusual? Am I about to do this because I think I can get away with it, so these are all probably negative questions? The more no’s are there the better, so you try to find out that whatever ethical issues that has been written here whether you can fit that in this guidelines and get more number of no’s. If there are more number of no’s then you can be sure that ok you are doing probably fairly well.

So, these are some ethical guidelines the dilemmas that can happen in the agreement context from a vendor and retailer relationship context we have discussed about that. Thank you very much; I will come up with a new topic in the coming lecture.