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Direct or indirect channel structures. Evaluating the impact of channel governance structure on export performance

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ABSTRACT

The purpose of the study is to examine the impact of channel governance structure on export performance ex post. The study surveyed 105 foreign buyers of crane services from five countries and used MANOVA to test the effects of channel governance structure on export short term and long term performance outcomes. The study found that short term profitability was higher for indirect distribution channel arrangements while longer term outcomes of buyer economic satisfaction and loyalty were higher for direct. The results suggest that exporters are more likely to achieve immediate financial objectives with the support from indirect channels; however, long term objectives are more effectively achieved through direct channels.

1. Introduction

Although there is a great deal of research on business performance, international business researchers are yet to agree on the composition of export performance (Hult et al., 2008). Katsikeas, Leonidas, Leonidou, and Morgan (2000) suggests that performance is a multi dimensional construct that encompasses a wide range of determinants like managerial, organizational and environmental, while Nevin (1995) focused on the effect of distribution channels. Distribution channels are designed as either a direct structure (through direct sales force), indirect (through agents and dealers) or a combination of both. The structure depends on the advantages from ownership of assets; location of market; and operations (Dunning, 1980). Since Dunning's (1980) contribution, a series of studies investigated the factors that influence channel choices (Anderson & Gatignon, 1986; Brouthers, 2013; Frazier, 1999; Frazier and Lassar, 1996). Most of these investigations drew on two fundamental business management theories: (1) theory of transactional cost economies (Canabal & White, 2008) and (2) relationship theory (Weitz & Jap, 1995). To date, literature on channel choices is widely available, but only a few studies have evaluated the outcome of channel choices (Canabal & White, 2008; Chang, Chung, & Moon, 2012). Academics have attributed the paucity in research to the general lack of data on the performance of privately owned companies (Chang et al., 2012).

This study overcomes this limitation by selecting a single multinational company willing to provide full support and access to financial records under the condition of anonymity and confidentiality. It addressed the academic deficit by investigating the effect of channel governance structure on both long term and short term performance outcomes. The study makes a specific contribution to the international business literature. Firstly, it provides empirical evidence to demonstrate the effects of channel governance structure on export performance. Specifically, our findings show that exporter short term profitability can be higher when indirect channel arrangements are used in foreign markets however, longer term performance outcomes of buyer satisfaction and loyalty are greater when a direct channel is employed. Secondly, the study supports the multi dimensionality of performance outcomes by showing that performance outcomes vary by channel structure highlighting the need for exporters to define their strategic intentions before entering foreign markets.

The paper is divided into four main sections. Firstly, it reviews the academic literature in the area of channel structure and performance outcomes and presents research hypotheses that guided our study. Secondly, the paper discussed the study's research methodology and data analysis. The paper ends with a

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discussion on the theoretical and practical implications of the findings and makes suggestions for future research.

2. Theoretical rationale and research hypotheses

Channel governance structures help exporters capitalize on growth opportunities in foreign markets (Lee, Knight, & Kim, 2008). Channel structures in foreign markets presume two extreme options: (1) direct distribution, which involves maintaining full control of distribution activities; and (2) indirect distribution, where distribution is contracted to external independent service providers. A direct distribution channel is preferred when the maintenance of power is important to the exporter. However, a major hindrance is the commitment of time, financial and human resources in unfamiliar and distant markets.

There is general disagreement among academics on the impact of channel governance structures on export performance (Aulakh, Kotabe, & Teegen, 2000; Ramaseshan & Patton, 1994; The Economist, 2013). Arguably, the indirect distribution channel enhances immediate profitability, requires lower resource commitment, and has a lower risk index. It also creates a higher local appeal and increases brand acceptance (Ramaseshan & Patton, 1994). These advantages are realized through augmented services offered by external intermediaries such as warehousing, financing, bulk breaking, physical distribution and promotions. However, recent arguments suggest that contracting services to external independent agents can lead to the exporter's detriment. A recent article published by The Economist (2013), suggested that the cost savings realized from contracting external independent service providers are short term and lead to compromising consequences on long term interests of the company. Arguably, indirect arrangements can retard a firm's ability to develop and expand technical competencies, and create a catastrophic dependency on external agents. Therefore, while companies may enjoy cost benefits and savings in the short term, contracting external companies to act as market intermediaries can be detrimental to the firm's long term development and growth. Channel literature also demonstrates that firms who perform poorly in foreign markets often invest in poorly conceived partnership arrangements or engage in inefficient unproductive assets (Aulakh et al., 2000). The reasons for suboptimal channel performance are vast and range from cultural differences to conflict, opportunism and unfairness. These factors either diminish or destroy channel relations (Samaha, Palmatier, & Dant, 2011). In this regard, exporters should pay careful attention to channel decisions in foreign markets. The main thrust of this research is to evaluate the impact of channel structures on performance outcome ex post. A detailed discussion is presented in the following sections.

2.1. Theories of channel governance

Theories of transaction cost and relationship marketing are commonly cited paradigms in channel governance (Aulakh & Kotabe, 1997; Weitz & Jap, 1995; Woodcock, Beamish, & Makino, 1994). Transaction cost describes the cost of implementing and managing a distribution system. It suggests that buyer–seller relationships exist to minimize costs and maximize benefits. Critics describe this paradigm as a short-sighted vision, which promotes opportunistic behaviour (Brown, Dev, & Lee, 2000; Weitz & Jap, 1995). Brown et al. (2000) examined the impact of opportunistic behaviour and suggested that exporters choose integrated channel structures to insulate themselves against negative perceptions. Ownership provides foreign buyers with a level of comfort and reassurance of fair opportunities, especially since buyers have higher levels of trust in relationships cultivated through direct channels (Brown et al., 2000). While channel research continues to recognize the importance of cost related factors, channel management research recognizes the role of relationships (Weitz & Jap, 1995). Channel structures built on relationships focus on long-term satisfaction and commitment, two essential determinants of success (Morgan & Hunt, 1994). Relationships built on satisfaction and commitment are generally stronger and more resilient to challenges. According to the relationship marketing literature (Palmatier, 2008; Palmatier, Jarvis, Bechkoff, & Kardes, 2009; Weitz & Jap, 1995) relations are constructed socially, structurally and financially. Social relationships are interpersonal, forged through social interaction and direct engagement. In channel relations, such interactions occur on two levels: among firms (supplier–distributor or supplier–customer) and among individuals (sales person–buyer). Palmatier (2008) supports the idea that intra personal relationships have a stronger impact on financial outcomes. The author argues that strong intra personal relationships create emotional bonds based on gratitude and reciprocity, which subsequently convert short term business arrangements into long lasting emotional friendship. However, the author warns, that relationships based on intra personal relations are often transient, and migratory. Structural relationships focus on forging ties with channel members through investment initiatives that integrate operations such as electronic ordering system and packaging systems. Palmatier (2008) contend that successful structural relationships increase the efficiency and productivity of members and discourage channel members from adopting conflicting behaviours. Financial relationships focus on economic returns and cost saving initiatives. Channel members can realize fiscal benefits from this relationship including discounts, extended terms of payment, after service support, warrantees and guarantees in exchange for loyalty and support.

2.2. Channel governance and export performance

Export performance measures the extent to which an exporter's objectives (strategic and financial) are achieved (Lages, Jap, & Griffith, 2007). Performance is usually described as inclusive of both short and long term results based on direct and indirect foreign market activities. Although there is an abundance of research on export performance, there is still a large amount of ambiguity in conceptualizing and measuring performance in export markets (Hult et al., 2008; Katsikeas et al., 2000). In reality, most exporters focus on immediate financial returns (Lages & Lages, 2004) at the expense of longer term rewards (Kaplan & Norton, 2004). Hult et al. (2008) suggested that an evaluation of export performance on basic standards which include financial wellbeing (economic performance), operational advantages (skills and knowledge, efficiency, innovation, productivity), and overall market effectiveness (brand reputation, customer satisfaction competitiveness) should be conducted. Katsikeas et al. (2000) advocated economic and non-economic returns as key performance indicators. Economic indicators are objective outcomes such as sales volume, profitability and market share, while non-economic outcomes are non-financial outcomes, which include market competitiveness and operation efficiencies (Anderson, 2008; Schramm-Klein, Morschett, & Swoboda, 2008). Woodcock et al. (1994) examined export markets and concluded that performance is a direct function of channel structure. This conclusion is also supported by recent contributions (Anderson, 2008; Schramm-Klein et al., 2008). A direct channel provides companies with greater control over business operations, increasing profits and long term performance indicators (Schramm-Klein et al., 2008). Direct sales representatives are more willing to perform additional activities, push new products or push products with a declining selling cycle (Anderson, 2008). In contrast, an indirect channel offers more immediate returns. Independent