Hybrid systems are hard to manage—and an important way to increase sales and decrease costs.

Managing Hybrid Marketing Systems

by Rowland T. Moriarty and Ursula Moran

There was a time when most companies went to market only one way—through a direct sales force, for instance, or through distributors. But to defend their turf, expand market coverage, and control costs, companies today are increasingly adopting arsenals of new marketing weapons to use with different customer segments and under different circumstances. In recent years, as managers have sought to cut costs and increase market coverage, companies have added new channels to existing ones; they use direct sales as well as distributors, retail sales as well as direct mail, direct mail as well as direct sales. As they add channels and communications methods, companies create hybrid marketing systems.

Look at IBM. For years, IBM computers were available from only one supplier, the company's sales force. But when the market for small, low-cost computers exploded, IBM management realized that its single distribution channel was no longer sufficient. In the late 1970s, it started expanding into new channels, among them dealers, value-added resellers, catalog operations, direct mail, and telemarketing. IBM had built and maintained its vaunted 5,000-person sales force for 70 years. In less than 10 years, it nearly doubled that number and added 18 new channels to communicate with customers.

Apple Computer also started out with a clear and simple channel strategy. It distributed its inexpensive personal computers through an independent dealer network. But when the company began to sell more sophisticated computers to large companies, it had to change. Apple hired 70 national account managers as part of a new direct sales operation.

In adding these new channels and communications methods, IBM and Apple created hybrid marketing systems. Powerful forces lie behind the appearance of such hybrid systems; all signs indicate that they will be the dominant design of marketing systems in the 1990s. At the same time, smart managers recognize the high risks of operating hybrid systems. Whether the migration is from direct to

Despite their risks, hybrids will be the dominant marketing design in the 1990s.

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indirect channels (such as IBM) or from indirect to direct (like Apple), the result is the same—a hybrid that can be hard to manage.

The appearance of new channels and methods inevitably raises problems of conflict and control—conflict because more marketing units compete for customers and revenues; control because indirect channels are less subject to management authority than direct are. As difficult as they are to manage, however, hybrid marketing systems can offer substantial rewards. A company that can capture the benefits of a hybrid system—increased coverage, lower costs, and customized approaches—will enjoy a significant competitive advantage over rivals that cling to traditional ways.

Examples of hybrid marketing systems extend beyond high-tech businesses such as computers to older industries such as textiles, metal fabrication, and office supplies and to service industries such as insurance. Many of the examples in this article are high-tech companies because the accelerated pace of high-tech industries foreshadows trends that tend to occur more slowly in other industries. The trend to hybrid systems, however, appears to be accelerating in many industries. According to one recent senior manager survey, 53% of the respondents indicated that their companies intend to use hybrid systems by 1992, a dramatic increase over the 33% that used those systems in 1987.

Two fundamental reasons explain this boost in the move to hybrids: the drive to increase market coverage and the need to contain costs. To sustain growth, a company generally must reach new customers or segments. Along the way, it usually supplements existing channels and methods with new ones designed to attract and develop new customers. This addition of new channels and methods creates a hybrid marketing system.

The need to contain costs is another powerful force behind the spread of hybrid systems, as companies look for ways to reach customers that are more efficient than direct selling. In 1990, the loaded cost of face-to-face selling time for national account managers can reach $500 per hour, for direct sales representatives, the average is about $300 per hour. Selling and administrative costs often represent 20% to 40% of a company's cost structure and thus have a direct effect on competitive advantage and profitability. For instance, Digital Equipment's selling and administrative costs in 1989 were 31% of revenues, for Sun Microsystems, the figure was only about 24%.

Given such economics, many companies are pursuing techniques such as telemarketing, which costs about $17 per hour, or direct mail, which runs about $1 per customer contact. A marketing strategy built on such low-cost communications methods can yield impressive results. Tessco, a distributor of supplies and equipment for cellular communications, emerged as one of the industry's fastest growing competitors by relying on low-cost communications methods. Tessco generates leads through direct mail and catalog operations; it uses telemarketing to qualify sales leads, make its sales pitch, answer questions, and close the sale. It then follows up each sale with service telemarketing and maintains accounts through an automatic reordering process. The result: Tessco enjoys significantly lower costs than most of its competitors, which continue to rely on traditional methods such as direct sales.

Wright Line's Problems

Despite the proliferation of marketing methods, few companies pay sufficient attention to the design of marketing systems or seek to manage them in ways that optimize coverage and costs. Indeed, most companies decide to add new channels and methods without a clear and realistic vision of an ultimate "go to market" architecture. These decisions are usually made separately and independently—and often swiftly as well. As a consequence, companies can find themselves stumbling over their hastily constructed, overlapping hybrid system.

Consider how an ill-conceived and mismanaged hybrid system contributed to the 1989 hostile takeover of Barry Wright Corporation. Many factors made the Massachusetts-based company vulnerable, but a principal cause of its troubles was the performance of a major subsidiary, Wright Line, Inc. A leading supplier of accessories used to store, protect, and provide access to computer tapes, diskettes, and other media, Wright Line was struggling vainly to halt the erosion of its market position.

Wright Line's troubles stemmed from a decision made in the early 1980s to reorganize its marketing and sales functions. Previously, the company had sold its products exclusively through a direct sales force. Although the company had been growing rapidly and adding new sales reps every year, Wright Line's management was alarmed by several trends: inability to increase market penetration, declining sales productivity, high turnover of sales reps, and what appeared to be a fundamental shift in the market away from the company's traditional stronghold in large, central computer installations.

After analyzing these trends, Wright Line supplemented its direct sales force with additional marketing channels and communications methods. The
A simple graphic captures the elements of a hybrid marketing system. Along the top are the basic marketing tasks required to obtain and maintain customers: generation of leads; qualification of these leads; presales activities, such as sales calls to woo specific customers; closing the sale; provision of postsales service; and ongoing management of the account.

Along the side of the grid are the various marketing channels and methods used to reach customers, ranging from elaborate direct to elaborate indirect options. The shaded areas represent one possible approach through a direct channel: direct mail to generate leads, telemarketing to qualify leads and manage presales and postsales activities, and a direct sales force to close deals and manage the account on an ongoing basis.

The hybrid grid can be a useful diagnostic tool to identify points of overlap and conflict in a marketing system. It can also aid in the design of a new marketing system tailored to the needs of specific customers. As a marketing map, the grid depicts the situation at a particular moment and needs to be updated as changes occur.

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### MAPPING THE HYBRID

At the heart of the problem of designing and managing hybrid systems is the fundamental question of what mix of channels or communication methods can best accomplish the assortment of tasks required to identify, sell, and manage customers. The trick to designing and managing hybrid systems is to disaggregate demand-generation tasks both within and across a marketing system—recognizing that channels are not the basic building blocks of a marketing system; marketing tasks are. This analysis of tasks and channels will identify the hybrid’s basic components and permit managers to design and manage the system effectively.

A map of tasks and channels—what we call a hybrid grid—can help managers make sense of their hybrid system. [See insert, “The Hybrid Grid.”] A hybrid grid, for example, can be used to illustrate graphically what happened at Wright Line and what might have happened differently.
Before its reorganization, Wright Line used direct sales for all demand-generation tasks and all customers (see the chart "Wright Line's Marketing System: What It Had"). When it reorganized in 1982, Wright Line wanted the direct sales force (unit 1) to perform all demand-generation tasks for big customers, the new direct response unit (unit 2) to concentrate exclusively on midsize customers (using catalogs and telemarketing), and the new third party and resale unit (unit 3) to market to small customers and nonusers through indirect channels (see the chart "What It Wanted").

Instead, Wright Line wound up with a marketing system that was neither what it wanted nor what it needed (see the chart "What It Got"). The three marketing units were performing all of the demand-generation tasks for many different types of customers. Units 1 and 2 bickered constantly over account ownership. To avoid losing accounts, for example, some sales reps improperly classified accounts to hide them from the direct response marketing division. Those who complied were frustrated by guidelines that prohibited them from calling on smaller and midsize accounts in their territories and growing with them. The activities of unit 3 added fuel to the fire. Among major customers, purchasing managers who read catalogs and received visits from the sales reps of office supply vendors found that Wright Line products were available at a substantial discount off the direct sales price.

In many respects, Wright Line's experience was typical, both in terms of the problems the company faced and its approach to solving them. Management's effort focused on identifying new channels that could be added to or substituted for all of the marketing tasks performed by the existing direct sales force channel. But this approach incorrectly assumes that each channel must perform and control all demand-generation tasks. The hybrid grid forces managers to consider various combinations of channels and tasks that will optimize both cost and coverage.

In addition, the company assumed that certain channels could best serve all the needs of certain customer segments. Hence, units 1, 2, and 3 were aligned with big, midsize, and small customers. The process of aligning high-cost channels—that is, the direct sales force—with big customers and low-cost channels with small customers is very logical, if that is the way customers buy. In Wright Line's case, however, customers bought from multiple sales channels. The attempt to use a single channel to reach a single customer group resulted in severe channel conflicts, along with customer confusion.

The design of an effective hybrid system depends not only on a thorough understanding of channel costs but also on a thorough understanding of buying behavior. When a new channel is added to service a particular customer segment, the segmentation scheme must clearly reflect the customer's buying behavior—not just the channel costs of the company. The design of an effective hybrid system requires balancing the natural tension between minimizing costs and maximizing customer satisfaction. In Wright Line's situation, the hybrid design was driven by costs, without regard for buying behavior.

Wright Line's fatal flaw was basing its marketing strategy on what was best for the company, not what customers wanted.
was best for its customers. In focusing its costliest marketing resources on the targets with the highest potential payoff and devoting less expensive resources to less promising accounts, it ignored the buying behavior of its customers. Too late, Wright Line discovered that its customers could not be segmented so neatly, nor would they conform docilely to the company's perception of its most efficient channel structure. Its hybrid system was intended to lower costs and increase coverage. Instead, Wright Line lost control of both its channels and its customers.

The hybrid grid illustrates how Wright Line might have successfully designed and managed its hybrid system [see the chart "What It Needed"]. The company could have used direct mail and response cards to generate leads among potential customers of all sizes and to perform most other tasks for small accounts. It could have used telemarketing to qualify leads among big and midsize prospects and determine approximate order size. It could have routed qualified prospects interested in buying a certain amount of equipment to direct sales reps. (Qualified prospects that turn out to be current national accounts would be turned over to the appropriate national account managers.) To midsize customers, it could have made phone calls to close sales and handle accounts; a direct sales rep or a national account manager could have performed these tasks for larger customers. For all customers, telemarketing could have been used for postsales tasks like reordering.

This version assigns demand-generation tasks to various channels, balancing both cost and customer buying behavior. Distributors were a principal part of Wright Line's setup. But this approach avoids using indirect channels, thereby allowing the company to maintain broad coverage without sacrificing control of pricing and product policy. (Of course, indirect channels are appropriate and necessary in many situations.) By establishing boundaries around genuine segments and building bridges across tasks, Wright Line might have gained the advantages of expanded market coverage and cost-effective marketing management without losing control of its marketing system and its customers.

Managing Conflict in Hybrid Systems

Conflict is an inevitable part of every hybrid system. When a company adds a channel or substitutes a new communication method within a channel, existing stakeholders—sales reps, distributors, telemarketers—invariably resist. And why not: each faces a potential loss of revenue as well as competition for ownership of customers. In seeking to build and manage a hybrid system, therefore, companies must recognize and communicate the existence of conflict as the first and most important step.

The next step is to assess the magnitude of the conflict, asking some simple but penetrating questions: How much revenue does the company have in conflict? (Revenue is in conflict whenever two or more channels simultaneously attempt to sell the same product to the same customer.) Where is this conflict? How do channels and customers react to it? How much management time is devoted to dealing with the conflict?
The answers to these questions will vary by industry and by company, but some generalizations are possible. Clearly, a company with no revenue in conflict may be sacrificing coverage, failing to attract new customers by focusing too narrowly on a particular segment. Indeed, a certain amount of conflict in a hybrid marketing system is not only inevitable but also healthy. On the other hand, as the Wright Line story illustrates, conflict that is pervasive across channels is debilitating and potentially destructive.

Of course, the concept of having revenue in conflict is alien to many CEOs and senior managers, particularly those who are accustomed to using only a single channel. They should seek a point of balance where conflict is neither too little nor too much. Although the location of this point depends on many variables—as a rule of thumb, destructive behavior occurs when 10% to 30% of revenues are in conflict—managers can estimate it by monitoring feedback from customers and marketing personnel. When phone calls and letters become angry, or when a significant portion of management time is absorbed in mediating internal disputes or dealing with customer complaints, warning bells should go off.

**Bounding the Conflict**

After they determine the amount and location of conflict, managers can establish clear and communicable boundaries and specific and enforceable guidelines that spell out which customers to serve through which methods.

Most companies observe some natural boundaries in the marketplace—areas defined by the interaction between buyer behavior and channel costs. Typically, companies target the largest and most profitable customers for some form of direct personal selling and serve smaller, less profitable accounts through less expensive methods. The problems arise with those customers residing somewhere in the middle: midsize accounts or markets with fuzzy boundaries, such as large national accounts that use a combination of centralized and decentralized purchasing practices that vary by product, location, or order size.

In this no-man's-land, neither the customer's buying behavior nor the company's transaction economics indicates definitively which method is the most effective way to serve the customer. Because no single method is clearly superior or appropriate, several may compete with each other—an example of a situation where clear boundaries will not work. These no-man's-land customer segments should be identified and clearly communicated to all marketing units so they know they will have intracompany competition.

Once the "jump ball" selling situations are identified, it is easier to construct barriers where natural segments exist. Boundaries between classes of customers are frequently couched in terms of sales, but effective boundary design involves much more than spelling out who makes which sale. It should instead indicate who owns and who doesn't own certain customers. Boundary mechanisms that help achieve this goal are generally based on customer characteristics, geography, and products.
Customer Characteristics. Customer size is a familiar boundary criterion. One large computer manufacturer specifies that, for its banking customers, its value-added resellers (VARs) should sell to small community financial institutions with less than $250 million in assets. For larger institutions, the manufacturer should sell through its direct sales force or some combination of that group and a third-party software supplier.

Order size provides another standard for drawing boundaries. A leading maker of PCs, for example, specifies that orders for more than 25 units must go through its direct sales force and orders of less than 5 units through independent dealers. Either direct or indirect channels may handle orders in the no-man’s-land between 5 and 25 units.

Customers can also be classified by decision-making process or decision-making unit. A manufacturer of specialty and commodity chemicals uses a direct sales force to sell specialty chemicals because the purchasing process for these products is complex and requires several engineers to develop specifications and participate in supplier selection. The company’s commodity products, however, are most often bought by a purchasing agent, and price is the key consideration. Hence, commodity chemicals are handled by distributors.

Finally, customers can be categorized by industry, particularly when there are genuine differences both in the product, price, and service package and in the expertise demanded of salespeople. The paper industry is a good example of differences in end use or applications. A different channel serves each of the four major end-use groups—newsprint, magazines, office products, and business forms.

Geographic Boundaries. Bounding by geography is clear and easy to enforce. A major manufacturer of computer-aided design/computer-aided manufacture (CAD/CAM) systems sells its offerings in the United States and Europe through a direct sales force; in Japan, it uses an exclusive distributor. The company has little difficulty preventing major conflict (except in global accounts) because the channels are physically separated. Many companies serve large, urban markets through some form of direct sales and use distributors or reps to cover less densely populated areas.

Product Boundaries. Xerox used product boundaries when it entered the personal copier market. It sells mid-range and high-end machines through a combination of direct sales and dealer distribution; it sells low-end machines exclusively through retail channels. Electronics and appliance stores, mass merchants, department stores, and an American Express direct mail program are all sources of Xerox personal copiers. The company has tried to avoid excessive conflict among these different retail channels by producing distinct models for each. The basic model 5008 personal copier was designed in three different versions so retailers would not compete with one another over an identical product.

Boundary mechanisms will help contain and control conflict when it arises, but they do not—and should not—eliminate it. It is impossible to hermetically seal each segment or customer group. Astute marketers identify and communicate to their channels not only those areas where clear boundaries exist but also those where they are either impossible or impractical.

Managing Channel Additions

Maintaining order in a hybrid marketing system is a complex administrative challenge. The addition of new channels and methods inevitably requires modifications to existing reporting relationships, organization structure, and management policies with respect to motivation, evaluation, and compensation. The stakes are high since organizational moves issue a strong signal about the direction of change and top management’s commitment to it. In the past decade, for example, Wang Laboratories struggled through three separate attempts to create an indirect sales organization to supplement direct sales of its products. Each new attempt foundered after meeting entrenched resistance inside the company. Indeed, Wang’s inability to solve this problem is a hidden cause of its much-publicized troubles in recent years.

Although each hybrid system presents unique challenges to managers, two general administrative guidelines may be helpful. First, decisions about structure and support policies should conform to the overall goals of the marketing system. Each potential configuration should be measured against the obvious tests: Will it satisfy customers in the most cost-effective manner? Will it maximize the prospect of achieving greater coverage and control throughout the system? Will it limit destructive conflict inside the organization?
Second, the timing of changes in structure and policies should reflect a realistic assessment of revenue flows through various channels and methods over time. In a large company, for example, it is extremely unlikely that a new channel or method will account for a significant fraction of total revenues in its first year. A new indirect channel added to a system dominated by a direct channel may account for 3% to 5% of revenues in the first year and perhaps 20% by the fifth. During such a transition, management should weight its policies heavily in favor of the new channel to ensure its success.

Management sends the most powerful and immediate signals through the compensation system. Companies with hybrid systems rely heavily on compensation policies to reinforce new boundaries and routinely subsidize new activities during transition periods. The most common approach involves paying personnel in the older units to allow personnel in the newer units to make the sale. An example reveals the reasoning behind such a tactic. A large computer company was struggling with the familiar problem of adding low-cost direct methods and indirect channels to supplement its direct sales force. In seeking to motivate the direct sales reps to relinquish revenue responsibilities, the company considered three options: a penalty, a modest incentive, and a strong incentive.

In weighing the penalty option, the company reasoned that requiring direct sales reps to forfeit commissions on each sale that should be made elsewhere would discourage them from stealing sales from new units. The risks of such an approach, however, seemed overwhelming: the company saw that conflict and petty rivalries were bound to erupt throughout the marketing organization as soon as it instituted the policy.

The modest incentive option would entail paying direct sales reps a portion of their normal commission when the new units made a sale. On reflection, this solution appeared too cumbersome: it would be difficult to determine appropriate compensation levels and to define and enforce a policy that would avoid sending mixed signals.

In the end, the company chose the strong incentive option—and eventually implemented it successfully. After a thorough analysis of long-term costs and benefits, the company paid the direct sales reps their normal commission for every sale regardless of whether they were responsible. Once the new units became established, the company phased out this system of double pay.

Orchestrating a Hybrid System

Once a hybrid system is up and running, its smooth functioning depends not only on management of conflict but also on coordination across the channels and across each selling task within the channels. Each unit involved in bridging the gap between the company and the customer must "hand off" all relevant information concerning the customer and the progress of the sale to the next appropriate unit.

A recent technical tool called a marketing and sales productivity (MSP) system can be an invaluable
Coordinating the handoffs within its hybrid system and knowing the cost of acquiring and maintaining its customers gives Data Translation significantly lower marketing costs than its competitors. These lower costs translate directly into competitive advantage and bigger margins.

Capturing the Benefits

Staples, a Massachusetts-based office supplies company, is achieving outstanding growth through clever allocation of marketing tasks based on what it has learned about customer behavior. At its birth in the mid-1980s, Staples's founders decided to offer discounted office supplies in a retail superstore format, targeting white-collar companies with up to 100 employees. Staples encouraged customers to accept a free savings card that granted additional discounts and, more important, allowed the company to track purchases and to build up a customer database.

Armed with this information, management discovered that its penetration of businesses with 2 to 10 employees was good, those with 10 to 20 not so good, and those with more than 20 quite weak. Customers in the latter two segments wanted more service. In response, Staples started accepting phone orders and added a delivery service. It has also used direct mail, telemarketing, and catalogs and has considered adding a direct sales force to handle large accounts. An MSP system orchestrates and monitors the entire hybrid system and provides management with performance and productivity information on each marketing element. Staples credits much of its success to the design and implementation of its hybrid system.

Many signs indicate that hybrid systems will be the dominant design for going to market in the 1990s. How a company manages its system will help determine its fate in the marketplace. A company that designs and manages its system strategically will achieve a powerful advantage over rivals that add channels and methods in an opportunistic and incremental manner. A company that makes its hybrid system work will have achieved a balance between its customers' buying behavior and its own selling economics. A well-managed hybrid system enables a marketer to enjoy the benefits of increased coverage and lower costs without losing control of the marketing system. Further, it enables a company to customize its marketing system to meet the needs of specific customers and segments.

In sum, a company with a successful hybrid marketing system will accomplish the following:

An MSP system acts as the central nervous system that coordinates the channels and tasks of a hybrid system.

1. Channels are either direct or indirect. Methods are the communications options companies can use to reach potential customers; they may also be direct or indirect. For example, through a direct channel, a company may use account managers, a sales force, or telemarketing. The same methods may also be used singly or in combination through indirect channels.

It will recognize that the design and management of its marketing system is a powerful weapon in an increasingly competitive and continually shifting battle for customers.

It will construct its marketing system using marketing tasks, not entire marketing channels, as the fundamental building blocks.

It will anticipate, recognize, communicate, and contain conflicts inherent in the marketing system.

In designing boundaries between customer segments, it will strike a balance between too loose and too strict limits.

It will form policies and an organizational structure that allow new channels to grow, minimize internal conflict, and reinforce segment boundaries.

It will exploit information technology and other managerial tools to coordinate handoffs of customers and accounts from one channel or method to another and eventually develop customized marketing systems for each important customer or segment.

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