

Advertising and Price Competition in a Manufacturer-Retailer Channel

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Abstract

We investigate how manufacturers' advertising competition, when advertising has a dynamic impact on the goodwill that affects current period demand, affects price competition in a manufacturer-retailer channel. We find that advertising and retail price promotion are strategic complements in the laundry detergent category as manufacturer advertising increases the price elasticity of demand. Advertising competition intensifies price competition although it improves the profitability of manufacturers. The presence of retailers in the channel leads to increased advertising spending but also mitigates the extent of price competition. Compared to the case of when price is the only strategic variable, the presence of an intermediary leads to higher profitability for manufacturers when they compete in both price and advertising. This implies that previous channel studies (e.g. McGuire and Staelin 1983) may have underestimated the benefits of manufacturers employing retailers to avoid direct competition. We also find that the benefits are asymmetric across manufacturers as brands with a higher goodwill level and advertising effectiveness seem to benefit more even when there is no cost advantage relative to its competitors.

Speaker Profile

Chakravarthy Narasimhan is Philip L. Siteman Professor of Marketing, Olin Business School, Washington University, St. Louis. Previous to this, Dr. Narasimhan was an assistant and associate professor at the University of Chicago from 1981 to 1988. His principal research interest is in the economic analysis of marketing problems. He builds models, measurements and metrics to quantify firms and consumers responses to marketing strategies in competitive markets. His work has been published in top journals like Marketing Science, Journal of Marketing, Journal of Econometrics, and Marketing Letters. His publication, "A Price Discrimination Theory of Coupons," was selected best paper of 1984 by Marketing Science. He is a past secretary-treasurer of the TIMS College on Marketing. He is a member of the Business to Business Steering Committee at MSI. He is also on the editorial board of Marketing Science and is an Associate Editor of Management Science.