

A Comparison of Retailer-Wholesaler Relations in Administered, Contractual and Corporate Vertical Marketing Systems in Grocery Distribution

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The expression “*vertical marketing system*” is no longer part of the mainstream channels vocabulary used by most researchers. It has been replaced by such expressions as “value chain analysis”, with its related terms such as downstream and upstream analysis. And much of what is referred to as “strategic alliances” either with suppliers or distributors is in reality another way of describing and studying vertical marketing systems. As a result, this research will henceforth use the original term coined by McCammon almost 30 years ago and our understanding of channel practices in the grocery industry in the province of Quebec.

INTRODUCTION

The basic objective of this research is to understand and explain how vertical marketing systems function in the food distribution, especially for consumer packaged goods purchased mainly in supermarkets, through the political economy framework (Stern and Reve, 1980). Vertical marketing systems theory has yet to be updated to take into account the theoretical and empirical contributions offered by the political economy framework (Dwyer and Oh 1987, 1988; Robicheaux and Coleman 1994). Thus, the study contributes to our understanding of internal political economy through the dimensions of transactional form (i.e., locus of decision making and administrative procedures) and interorganizational climate (i.e., cooperation and trust).

So far, a number of authors have examined one or more aspects of this frame empirically. However, very few of these studies have been concerned with the differences in the structure and functioning of vertical marketing systems (Brown, 1981; Dwyer and Oh, 1988; Etgar 1976). In the words of Kaynak and Savitt (1984, p. 283), “*there is much to be done within domestic marketing systems...*”. A similar concern was expressed by Dwyer and Oh (1988, p. 32), to the effect that:

It is vital that empirical work on the structure and processes of interfirm relationships be extended to other channel forms in different industries... We can learn much about the political and economic phenomena of the diverse contractually integrated systems evident, for example, in the drug, grocery, and industrial supplies and equipment sectors.

Corporate chains, voluntary groups and unaffiliated retailers also referred to as corporate, contractual and administered vertical marketing systems are the main entity under study (Stern, El-Ansary and Coughlan, 1995). More specifically, the research pursues the following objectives :

- to empirically validate the corporate, contractual and administered vertical marketing systems typology proposed over 30 years ago but has so far never been tested empirically in grocery distribution;
- to test for differences in transactional form among corporate, contractual and administered

vertical marketing systems; and

- to test for differences in interorganizational climate among corporate, contractual and administered vertical marketing in grocery distribution.

Answering these objectives are important in that they will improve our understanding of the interorganizational links retailers have with their grocery distributors and corresponding managerial requirements needed to manage such vertical arrangements. The food distribution market selected for this study was the province of Quebec. While the retail food distribution structure in the province differs significantly from the rest of Canada, it is precisely for this reason why this geographic area was selected. The food distribution maybe atypical relative to other markets in Canada. For example, corporate chains market share is only at 25.5 %, well below the Canadian average of 53.9 % (Canadian Grocer, January-February 1996). Independents affiliated retailers (i.e., contractual arrangements) dominate the market with approximately 62.8 % of retail food sales. The remaining food sales are realised by independent unaffiliated retailers with 11.7 %. This market is now in transition as more corporate chains are grabbing market share from other types of distribution outlets (from 19.9 % in 1991 to 25.5 % in 1995). As a result the market provides an ideal testing ground for our research endeavours.

LITERATURE REVIEW

Vertical marketing systems differ from conventional distribution channels (McCammon, 1970; Stern, El-Ansary and Coughlan 1995). What follows next merely highlights some major points of comparison pertinent to the study and is not intended to be a comprehensive review of this domain of marketing channels. Conventional distribution channels are composed of a set of independent businesses where transactions are coordinated through a process of negotiation on one or more independent, vertically aligned markets. The number of players on each market is fairly high, and the businesses themselves are usually small, with no real negotiating power. More specifically, retailers are small, with little training and few qualified staff, and a financial structure that is often deficient. Their investments, few in number, are directed solely at reducing operating expenses or improving the firm's financial situation on the market. In such a situation, purchasing and sales conditions are negotiated firmly, with no concern for economies of scale that could potentially be achieved through interorganizational management of business tasks. The scope of the decisions made by managers in this type of channel arrangement is characterised basically by tradition and experience. Vertical marketing systems, on the other hand, are professionally managed, centrally programmed networks. By rationalizing activities through a strategy of vertical integration, coordination and synchronization of marketing flows from points of production to points of consumption, accompanied by massive capital investments, such systems can achieve economies of scale by using the most appropriate technology, management techniques and marketing strategies so as to ensure their viability and continuity.

Vertical marketing systems can be divided into three types: administered systems, contractual systems and corporate systems. In administered vertical marketing systems, vertical coordination is provided through particular programs geared to such systems. Traditionally, they are associated with a manufacturer-retailer trading relationship, where the manufacturer offers retailers marketing programs for its products (McCammon, 1970; Stern, El-Ansary and Coughlan, 1995). However, this type of system also exists in the wholesaler-independent unaffiliated retailer relationship in food distribution. An administered vertical marketing system exists in fact when

some of the wholesaler's services are offered to such retailers (Stern, El-Ansary and Coughlan, 1995; Robicheaux and Coleman, 1994). The services are generally of a kind that will improve the activities and marketing of the retailers. However, the potential economies of scale in such a relationship are minimal. Investments are made mainly by the system leader, i.e. the wholesaler, to improve its own productivity and financial performance. The leader's expertise in management and marketing will provide the system with a certain continuity and viability, although at a fairly low level, given the leader's lack of control over the channel members and the possibility for the members, if they so wish, to buy from other food distributors.

In contractual vertical marketing systems, the production, wholesale or retail function coordinates its business activities by means of a contractual agreement and a desire to cooperate through a comprehensive marketing program. This latter element leads to rationalization and formalization of exchange procedures, leading in turn to major savings in commercial operations. Moreover, investments are made in production, wholesaling or retailing to support the cost rationalization strategy in the distribution system. The managers are skilled in the management of marketing function activities, and the system's viability depends on the contractual agreement setting out the terms binding the two parties.

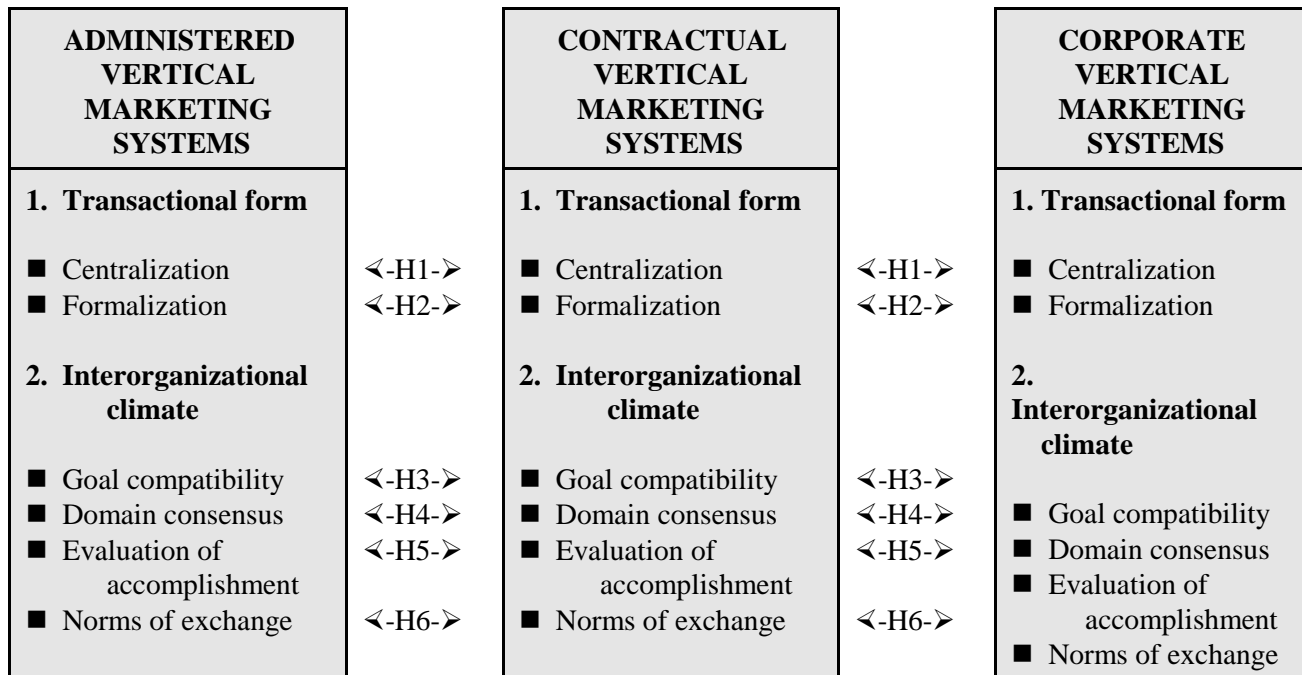
In corporate vertical marketing systems, the production, wholesale or retail functions are subjected to the same financial control. The economies of scale available in such systems are generated by division and tight coordination of trading tasks. Therefore, ownership at one or more levels ensures coordination and control of marketing activities. In addition, investments are made to reduce the system's distribution costs, whether for the wholesale or retail function. The managerial and marketing skills of the managers ensure a certain continuity and viability for the system.

Since all distribution systems are both economic and political (Palamountain, 1955; Stern and Reve, 1980; Robicheaux and Coleman, 1994), the political economy framework can be used to identify the internal dimensions that characterize their management modes and functional structure. More specifically, the internal economic structure describes and analyzes the level of vertical integration between the organizations or business units making up the distribution channel. The internal economic process is concerned with the interorganizational management of marketing functions and activities in the system. Internal polity is defined according to its structure, which highlights the relationship of power and dependency between the partners of the distribution channel. The internal polity process expresses the interorganizational climate that characterizes exchanges between system members.

HYPOTHESES

Empirically, as shown in Figure 1, marketing researchers have modified the internal political economy framework so that it can be used on samples of respondents from distribution channels (Dwyer and Oh, 1987; Dwyer and Welsh, 1985; Reve, 1980; John and Reve, 1982). Essentially, constructs are grouped under the headings of transactional form and interorganizational climate and are defined in Table 1. Transactional form is a representation of the internal economic and political structure and the internal economic process. In this research, it is defined through centralization and formalization, and is directly linked to the vertical coordination of vertical marketing systems (Reve 1980; Brown 1981; Robbins, Speh and Mayer 1982; Eliashberg and Michie 1984; Schul, Little Jr. and Pride 1985; Dwyer and Oh 1987, 1988). The question of interest here is whether the data will support the following hypotheses.

FIGURE 1
Empirical model of the internal political economy of vertical marketing systems



H₁ : As integration increases among the different vertical marketing systems, centralization will increase.

H₂ : As integration increases among the different vertical marketing systems, formalization will increase.

The theory of vertical marketing systems and the literature on political economy support these hypotheses (Anderson and Weitz, 1986; Hansen, 1965; Hansen and Harvey, 1974; McCammon, 1970; Stern and Reve, 1980; Stern, El-Ansary and Coughlan, 1995). In fact, the shift from a market structure to a vertically integrated structure is followed by a change in the level of centralization and formalization of the exchange procedures. The locus of decision and authority in corporate vertical marketing systems lies at the pinnacle of the hierarchical structure. The consequence of this is that decision-making is centralized at the head offices of the corporate chains. On the other hand, the level of centralization is not as high in contractual and administered vertical marketing systems. The informal structure of the division of labour in administered systems, together with the low level of vertical integration, mean that decision-making power is in the hands of the independent unaffiliated retailers. In contractual vertical marketing systems, however, under the agreement between the wholesaler and the retailer, decision-making control tends to be much more centralized, although less so than in corporate vertical marketing systems. The locus of decision-making lies at the top of the structure, that is, at the level of the wholesale function, although decisions must be ratified by the retailers, who own their businesses.

TABLE 1 Definitions of transactional form and interorganizational climate constructs within the internal political economy framework	
Transactional form	
Constructs	Definition of construct
1. Centralization	Degree of retailers` perception on their autonomy to make and implement marketing decisions such as promotion, merchandising and purchasing.
2. Formalization	Degree of retailers` perception on the routinization of administrative procedures, logistical activities and flows of information.
Interorganizational climate	
3. Goal compatibility	Degree of retailers` perception that market and marketing objectives are coherent to the ones pursued by their wholesalers.
4. Domain consensus	Degree of retailers` perception regarding mutual responsibilities with their wholesalers to the implementation of marketing programs.
5. Evaluation of accomplishment	Degree of retailers` perception to the extent of accomplishment of distributive activities by their wholesalers.
6. Norms of exchange	Degree of retailers` perception on mutual trust and cooperation with their wholesalers.

As regards formalization, fully integrated wholesale-retail distribution structures have highly coordinated, very simple and highly standardized distribution activities and exchanges (Hansen, 1965; Hansen and Harvey, 1974; Stern, El-Ansary and Coughlan 1995). This dimension of the transactional form is directly related to the level of vertical integration between wholesaling and retailing. As a result, the level of formalization will be low in administered systems and moderate in contractual systems. Empirically, the work of Brown (1981) and Dwyer and Oh (1988) also suggest this type of relationship, although in the latter case corporate chains were not considered in the empirical analysis.

The level of vertical coordination between the wholesale and retail functions is directly related to the interorganizational climate in the distribution system - that is, goal compatibility domain consensus, evaluation of accomplishment and norms of exchange (Stern and Reve, 1980). The following hypotheses are tested :

- H₃ : As integration increases among the different vertical marketing systems, goal compatibility will increase.
- H₄ : As integration increases among the different vertical marketing systems, domain consensus will increase.
- H₅ : As integration increases among the different vertical marketing systems, evaluation of accomplishment will increase.

H₆ : As integration increases among the different vertical marketing systems, norms of exchange will increase.

These hypotheses are based mainly on the vertical marketing systems literature and the theoretical framework of political economy in marketing (Alderson, 1965; Hansen and Harvey, 1974; McCammon, 1970; Reve and Stern, 1979; Stern, 1969; Stern and Reve, 1980; Stern, El-Ansary and Coughlan, 1995; Williamson, 1975, 1985). In fact, the control systems are stricter and tighter in corporate vertical marketing systems, which help reduce opportunist behaviour contrary to the system's objectives and increase transaction costs. Thus, corporate vertical marketing systems generally have more goal compatibility, a better definition of their domain of responsibilities, greater satisfaction with the result of accomplishment and a better understanding of the system norms of exchange. However, system's coordination effort tends to decline in a quasi-integration or non-vertical wholesale-retail integration structure. Such channel arrangements leave greater freedom of action to the parties, who may find themselves in a system that does not meet the individual and shared goals of its members, in which roles and tasks are poorly defined, where satisfaction with the result is generally lower, and which does not comply as well with exchange standards and procedures. These hypotheses are supported empirically by the work of Wiek (1969), Robbins, Speh and Mayer (1982), Eliashberg and Michie (1984), and Schule, Little Jr. and Pride (1985). All these authors tend to show that, as the level of vertical integration in a distribution structure increases, the level of conflict decreases, leading to greater goal compatibility and domain consensus, and increased satisfaction with the result of accomplishment. To a lesser extent, the work of Reve (1980) and Dwyer and Oh (1987) produced empirical support for the relationship between level of formalization and interorganizational climate. However, these latter authors also found a negative or inverse relationship between level of centralization and interorganizational climate. In this study, we will test the positive and direct relationship between level of vertical integration and interorganizational climate as formulated in the theoretical framework of vertical marketing systems.

RESEARCH METHODOLOGY

The research seeks to test for differences between corporate, contractual and administered vertical marketing systems in Quebec's food retail distribution industry. The data were collected by means of a structured mail questionnaire through a key informant approach (Dillman, 1978). Owners of independent supermarkets and managers of corporate supermarkets stores were asked to complete the questionnaire.

We followed Churchill's (1979) advice for developing better measures and to assess reliability and validity of each of the constructs. The questionnaire was pre-tested for content validity through personal interview as recommended by Dillman (1978) with wholesale executives and store owners and managers of supermarkets within the different vertical market structure under study. One of the challenges of the research was to draw up a list of supermarkets that was as representative as possible of Quebec's food retail distribution industry in order to minimize exclusion error, i.e. exclusion of potential respondents from the sample list. As our sample population, we used the list of grocer-butcher permits issued by Quebec's Ministry of Agriculture, Fisheries and Food. Access to the corporate stores listing and affiliates of all the major companies (Provigo, Hudon et Deaudelin, Épiciers Unis Métro-Richelieu and the Colabor Group) were also

obtained in arriving at our final list. We obtained a final list of 2,212 grocers/butchers : 150 corporate stores under corporate names such as Provigo, Héritage, Maxi, Super C and Sobeys; 1,244 affiliates, the main banners being Métro, IGA, Provigo, Richelieu and Bonichoix; and 818 unaffiliated stores. We then proceeded by sampling affiliated and unaffiliated stores for the research, together with the list of corporate stores. In the case of the affiliates, one store in every two was selected, for a final list of 622. In the case of the unaffiliated stores, three out of four were selected, for a total of 613. For the corporate stores, we retained all 150 from the list of respondents. As a result, 1,385 questionnaires were mailed for data collection purposes.

To avoid a low participation rate among questionnaire recipients, we adopted the integrated mail survey approach developed by Dillman (1978). The overall response rate obtained in this way was 32%. This compares favourably with other mail surveys, although it is below the anticipated rate of 59% as suggested by Dillman (1978, p. 56). However, if we look at responses per respondent group, we observe that the highest response rate was obtained from the corporate stores (60%), followed by the affiliates (43.5%) and finally, the non-affiliates (12.9%). The high rate of participation among corporate store managers can be explained by the support received from the head offices. The affiliate rate is extremely satisfactory if compared with the rates generally obtained in mail surveys ($\pm 25\%$). However, the comparatively low response rate among non-affiliated stores is probably due to a lack of interest or time in completing the questionnaire. Non respondents were not analyzed. However, a chi-square analysis of the respondents' geographical location with their correspondent population revealed no significant difference (non affiliated $\chi^2 = 8.46$; affiliated $\chi^2 = 6.32$; corporate $\chi^2 = 2.985$ for $\alpha = 0.01$ and 3 d.f.). Therefore, we can conclude on the external validity of the study.

Respondents were asked to indicate on a 5-point Likert scale the extent of channel practices. Then, an inter-item correlation was used to purify the measurement scale for each construct. All variables obtaining a correlation coefficient below 0.30 were eliminated from the scale. The statements were then subjected to principal component analysis to test construct validity (Churchill, 1979). As a guideline, a value in excess of 1 was used as the selection criterion for the factorial structure. Two factors were identified for formalization and norms of exchange by this process, giving a bivariate dimension to both concepts. Formalization is achieved by the process of routinization of common administrative procedures (i.e. transactional formalization) such as billing, ordering, receiving and by use of communication systems (i.e. exchanges computerization) such as electronic data interchange (EDI) and electronic courier (E-mail newsletters). The bi-dimensionality of norms of exchange was no surprise since by definition the construct is a representation of cooperation and trust between food retailers and wholesalers. Internal consistency was then analyzed using Cronbach's Alpha (α) to ensure the reliability of the scale. A factorial score was then calculated for each concept and each respondent, to compare the vertical marketing systems (Spector, 1992). The convergent and discriminant validity was analyzed using the correlation matrix between the operational concepts (Kim and Mueller, 1978; Spector, 1992). The reliability coefficient was placed on the diagonal of the matrix (TABLE 2). Basically, this procedure showed whether or not the statements for each construct measured by the reliability coefficient were more strongly correlated with the factor (convergent validity) and less strongly with the separate concepts (discriminant validity). The correlation coefficients between goal compatibility, domain consensus and cooperation were close to the Cronbach Alpha coefficient value for goal compatibility and, to a lesser extent, for domain consensus. This was no surprise, because John and Reve (1982) also experienced difficulty in validating these same concepts. There are several possible explanations for this.

First, the statements for the concepts may not measure the conceptual field very clearly. This, however, is not very likely, given the internal consistency measure

Cooperation	0,4802	0,1293	0,4138	0,5732	0,6309	-0,1111	<u>0,8556</u>	
Trust	-0,0486	-0,0268	-0,0878	0,2469	0,1918	-0,5651	0,0295	<u>0,7136</u>

obtained for each concept, and the high correlation between the statements and the factors. It is also possible that respondents were not able to estimate the statements properly for the retail trade. This is also unlikely, given the efforts made to pretest the questionnaire so as to ensure that the questions were clear and easily understood. In fact, the problem is likely to be conceptual in nature (John and Reve, 1982). Goal compatibility and domain consensus are two dimensions of conflict, and therefore of the same construct. Moreover, although theoretically speaking conflict and cooperation are not part of the same *continuum*, the results suggest otherwise. Consequently, the factorial analysis shows the extent to which these operational concepts are related, and that it is difficult to obtain measures that will satisfy all the conditions for validity. Nevertheless, these concepts were retained for analysis, although we were careful to ensure that the results were interpreted in light of their low level of divergence in terms of construct validity.

The results were analyzed and processed on the VAX system using the SPSS statistical data analysis software package (Version 4). A multiple variance analysis (Manova) was carried out on the internal variables of the vertical marketing systems, i.e. on the transactional form and interorganizational climate variables. If there is a significant difference with the univariate test, it is possible, using simple variance analysis, to compare the means of the groups in order to discover which does not correspond to the values of the other groups under study. A number of comparison procedures exist, the most common being the tests of Scheffé, Tukey, Duncan and Newman-Kuels. The aim of all these procedures is to control type 1 errors during multiple comparisons of variable means. In this research, we used Scheffé's paired test because of its robustness and its results, which are known to be more conservative (Duncan, 1975; Tabachnick and Fidell, 1989).

EMPIRICAL RESULTS

We can therefore conclude that there is a significant difference in the internal political economy of the various vertical marketing systems (TABLE 3). Univariate analysis of each of the concepts provided information on the nature of the differences between the vertical marketing systems under study. It revealed that all the empirical measures used to describe transactional form and interorganizational climate in the empirical model were significant at the threshold of $\alpha = 0.05$. Consequently, the results seem to confirm hypotheses 1 to 6. Scheffé's two-by-two comparison process, applied to the vertical marketing systems at the level $\alpha = 0.05$, revealed significant differences in centralization, exchange computerization, goal compatibility, domain consensus and cooperation. However, no significant difference was found in the level of trust, and only partial difference was found for transactional formalization and evaluation of accomplishment.

In fact, our results support a separate transactional form for voluntary groups, corporate chains and unaffiliated retailers as suggested by vertical marketing systems theory. The structure, characterized by the concepts of centralization, transactional formalization and exchange computerization, varies with the level of vertical integration between the wholesale and retail functions. An exception is transactional

TABLE 3
Multivariate and univariate analyses (MANOVA) of the internal political economy
of vertical marketing systems

Multivariate Test of Significance							
Test Name	Value	Approximate F	Degrees of Freedom		F	Significance of F statistic	
			Between Groups	Within Groups			
Pillais	0,71756	24,61928	16	704		0,000	
Hotellings	1,19236	26,08286	16	700		0,000	
Wilks	0,40172	25,34869	16	702		0,000	
Univariate Test of significance							
Variables	Between Groups Sum of Squares	Within Groups Sum of Squares	Between Groups Mean Square	Within Groups Mean Square	F Statistic	Significance of F	Scheffé ($\alpha = 0,05$) (Anova)
Centralization	0,00171	0,00361	0,00086	0,00001	84,82154	0,000	1>2>3
Transactional Formalization	0,08230	0,30028	0,04115	0,00084	49,06094	0,000	1=2>3
Exchange computerization	8,72713	24,45066	4,36357	0,06830	63,89017	0,000	1>2>3
Goal compatibility	6,86579	21,27498	3,43289	0,05943	57,76626	0,000	1>2>3
Domain consensus	10,99738	18,42552	5,49869	0,05147	106,83717	0,000	1>2>3
Evaluation of accomplishment	1,10367	17,77582	0,55183	0,04965	11,11379	0,000	1=2>3

Cooperation	10,24180	19,83882	5,12090	0,05542	92,40880	0,000	1>2>3
Trust	0,02054	0,99298	0,01027	0,00277	3,70242	0,026	1=2=3

1: corporate systems 2: contractual systems 3: administered systems

formalization, where the corporate systems have the same level of perception as the retailers in administered systems. Consequently, the highest level of trade formalization is found in voluntary groups. In the other cases, the higher the level of vertical integration, the higher the level of centralization and exchange computerization. Also, a direct link was found between vertical integration and goal compatibility, domain consensus and cooperation. There is also a significant difference in terms of evaluation of accomplishment between retailers affiliated with voluntary groups and unaffiliated retailers. This same difference, however, is not significant between corporate chains and affiliated retailers, or between corporate chains and unaffiliated retailers. Consequently, the level of accomplishment is highest among retailers belonging to voluntary groupings. Finally, there is no significant difference in the level of trust between managers of chain stores, affiliated retailers and unaffiliated retailers.

CONCLUSION AND IMPLICATIONS

Our work has revealed the differences in the organization and functioning of administered, contractual and corporate vertical marketing systems in grocery distribution in the province of Quebec. As a result, we were also able to highlight conceptual developments in the management of distribution channels (Ardnt 1979; Stern and Reve 1980; Achrol, Reve and Stern 1983; Williamson 1975, 1985). The work was also useful in testing the measurement instruments used in previous research. The reliability coefficients almost all obtained scores in excess of those quoted in the literature, and when compared to the standards generally considered acceptable for exploratory research, they all achieved the minimum pass standard (Nunnally 1967).

In term of managerial implications, this research shows significant differences in retailers' perceptions within the different channel structure. Since most grocery distributors are governing or managing these different vertical marketing systems within their own organization, knowing these differences may help grocery distributors in developing appropriate strategy with their food retailers in order to achieve their market objectives. For instance, unaffiliated food retailers need wholesaler's expertise in management and marketing. But this can only be accomplish through a partnership kind of relationship since the final decision is made by the store owner. Affiliated store or contractual vertical marketing systems are less autonomous. The danger for grocery distributor is to manage them as if there were corporate vertical marketing systems and forgetting in the process that they are first in business for themselves. Therefore, the contractual agreement should specify the roles and responsibilities of both parties in terms of management, operational and marketing responsibilities. Entrepreneurial values are still important as shown by the degree of centralization in marketing decisions. Corporate vertical marketing systems are managed in order to achieve the greatest operational efficiencies. However, the standardization of operational procedures leave little room to store managers in terms of autonomy. This lack of flexibility, as perceived by store manager, may inhibit local initiatives to meet more adequately consumer demand.

The study points out to a number of possible avenues for future research. First, a different focus on channel participants other than retailers, would be interesting, for example on food processors. Second, vertical marketing systems are common in almost all retail sectors. Thus, it would be possible to carry out a study in a sector other than food to validate the results for the retail trade in general. This could lead to a classification or typology or even a general

retailing theory related to organization and functioning of various vertical marketing systems.

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