RETAIL COMPETITION IN THE FAST-MOVING CONSUMER GOODS INDUSTRY: THE CASE OF FRANCE AND THE UK

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Retail Competition in the Fast-Moving Consumer Goods Industry: The Case of France and the UK

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1. Introduction

In the last ten years, the competitive behavior among fast-moving consumer goods (FMCG) retailers in France has been surprisingly different to that observed in the UK, given the proximity of the countries and their many shared conditions (similar products, income level, same manufacturer suppliers, common market, etc.). In France, the rivalry between the major retail chains has been largely price driven, while on the other side of the channel, the largest and most successful retail chains have competed on quality: in particular store differentiation via own labels and fresh products, range, and size of store. The profitability and market value of retailers resulting from these contrasting strategies has been correspondingly different. Tables 1 & 2 show how on these measures the French retailers are significantly outperformed by their English counterparts.

In our analysis we illustrate the differences by focusing on six of the largest (grocery) retail chains: for the UK, the big three, Sainsbury, Tesco and Argyll; and for France, Carrefour, Promodes and Casino. These chains account for over 50% and 40% respectively of the national total sales. Two of the four largest grocers in France (Leclerc and Intermarché) are not included because, due to their private ownership, figures are not available. We believe their situation to be substantially similar to those examined.

Table 1: Profit Margins (Net Profit after tax/sales)

	1983	1987	1992	1993
Carrefour	1.4	1.3	1.1	1.3*
Promodes	0.8	0.4	0.7	0.8
Casino	0.9	1.0	0.8	0.8
Sainsbury	3.4	4.2	5.2	5.2
Tesco	5.5	3.7	5.5	4.5
Argyll	2.3	2.4	5.8	4.5

Source: Authors' calculations based on company reports
* Excluding exceptional profits.

Table 2: Size in terms of Sales compared to Market Value of Major Retailers

	Sales (excluding taxes) Billion FF. (1993)	Market Capitalization (end 1993) Billion FF.	Ratio: Market Value / Sales
French			
Carrefour	123	55	0.44
Promodes	90	21	0.22
Casino	63	14	0.22
English			
Sainsbury	93	61	0.66
Tesco	74	38	0.51
Argyll	48	24	0.50

Source: Company reports and authors' calculations

The reported profit margins of the three French retailers, (Table 1), small though they are, are in fact overstated because of these retailers' significant international involvement (Southern Europe, South America, Taiwan, and Vietnam). Their profit margins are higher in foreign markets because in those markets they face more inefficient, smaller competitors. Further, they carry a much higher proportion of higher margin non-food products in their assortment than do UK food retailers. These two factors reinforce the profit margin discrepancies between the French and UK retail markets in the food area, and in their home markets.

The question we would like to address in this paper is why such significant differences can persist for a decade in two seemingly similar industries, in neighboring countries. Investigating the underlying causes and contributing factors will hopefully lead us to a better understanding of the nature of retail competition. It might also help us to make educated guesses about how competition between retailers will evolve in the future, and in other parts of the world.

Our first task is to analyze in more depth the true difference in profitability between French and UK retailers. Our conclusion will be that although there are distortions that complicate direct comparison, there remain definite differences (in favor of the UK's profitability) to explain.

2. Uncovering the true Profit Margins

According to their published accounts (Table 1 above), it appears that by 1992 UK retailers were about 5 times as profitable as their French colleagues.

In fact, this enormous difference in margin is partly due to differences in accounting practices that are in turn related to the nature of company ownership.

The three major UK retailers are dependent on the stock market to finance their growth, Carrefour, Promodes, and Casino, like the other major French retailers, are still dominated by family or other private ownership. As such, French retailers are reluctant to raise money via the stock market because this would have the effect of diluting the current owners' control.

Conversely dependence on the stock market for funds gives UK retailers a strong incentive (or even obligation) to return consistently high profits. Their French counterparts, on the other hand, are motivated to reduce their declared profits in order to minimize taxes on profits. Thus, it is not surprising to find that UK retailers estimate their depreciation on assets to be much smaller than that of French retailers. The latter use accelerated depreciation schemes to reduce their taxable profits (see Table 3).

Table 3: Depreciation/Fixed Assets (1993)

Carrefour	10%
Promodes	12%
Casino	9%
Sainsbury	4%
Tesco	5%
Argyll	6%

Source: Authors' calculations based on company reports.

If the profit margins from Table 1 are corrected to take into account the effect of this depreciation we get the results shown in Table 4.

Table 4: Corrected Margins (Profits + Depreciation/Sales)

	1983	1987	1992	1993
Carrefour	2.9	3.0	3.6	3.5
Promodes	2.2	1.9	2.1	2.5
Casino	2.1	3.5	3.0	3.1
Sainsbury	4.6	5.5	6.8	7.1
Tesco	3.2	5.2	7.2	7.0
Argyll	3.4	3.4	5.9	6.5

Source: Authors' calculations based on company reports.

As an alternative to the stock market French retailers are interested in negotiating long delays of payment from their suppliers (manufacturers) to finance expansion. UK retailers, by contrast, value long payment credits less, and value other manufacturer support, including lower prices, more (see Table 5).

Table 5: Growth Financing (1993)

	Assets/Equity	Supplier Credit/Sales
Carrefour	3.7	19%
Promodes	5.5	17%
Casino	3.2	16%
Sainsbury	1.2	7%
Tesco	1.4	7%
Argyll	1.2	10%

Source: Authors' calculations based on company reports.

Because of their lower cost of capital ("stock market darlings"), it is rational for UK retailers to be less interested in payment credits than their French colleagues. However, this difference in type of manufacturer support shows up in declared profit margins. The benefit of the delays of payment given to French retailers do not show up in the profit margins, but as reduced financial costs (or increased financial returns). In contrast, all the profits that UK retailers make on reselling the manufacturers' goods show up as healthy profit margins. Current delay of payments are approximately 70 days for French retailers. This 30-day differential with their UK colleagues would amount to an additional margin on sales of about 1.7%. Correcting for the different accounting practices and asymmetries in delay of payment substantially reduces the discrepancy in profit margins (see Table 6).

Table 6: Corrected Profit Margins for 1993, including the additional 1.7% for delay of payment differentials (at a 20% cost of capital).

	1993
Carrefour	5.2
Promodes	4.2
Casino	4.8
Sainsbury	7.1
Tesco	7.0
Argyll	6.5

Source: Authors' calculations based on company reports and EEC reports.

The adjusted figures indicate that French retailers are not doing nearly as badly as they sometimes like to claim. However, although the profit difference with UK retailers is less than a direct comparison would lead one to believe, there is still a marked discrepancy to explain.

3. Comparison of the Two Industries

There are several clearly observable differences between the retailing sectors in France and the UK: in particular, the degree of concentration, the importance and the nature of own-label brands, the level and sophistication of investments in technology, the quality of personnel employed, and lastly, the presence of certain high profile, influential retail management styles. We now argue that these differences are part of a pattern that can explain the observed differences in profitability.

The task is to argue which of the several differences are the real causes of the differences in the profit margins and market valuations of French and UK retailers, and which are simply corollaries. We will argue that the influence, amounting to hegemony, of certain retail chains, has been at the center of the differences. In the UK, Sainsbury and Marks & Spencer have lead the market towards high-quality private label; in France, Leclerc and Intermarché have railroaded grocery retailing towards price. Concentration, though a major issue for all involved in the industry, has been a facilitator, rather than a direct cause. Much more important, in our opinion, is the role allocated to private-label (that is, retailer) brands (J. Corstjens and M. Corstjens, 1995).

3.1. Nature of Retail Competition

Retailers can compete for customers on the basis of location, services, low prices, or the appeal and quality of product assortment, including fresh products. We will argue that location now gives less edge than it did and that services are rarely sources of sustainable advantage, particularly in the face of intense price competition. The two remaining alternatives, price and product assortment (including fresh) can create a sustainable, profitable consumer proposition in the long run.

3.1.1. Location

Location was once a major protection from price competition, but increasing mobility in all industrialized countries, and the car parks/out-of-town center locations used by modern retailers to exploit this mobility, have to a large extent overtaken this traditional protection.

Due to the vast increase in the number of supermarkets in recent years, most consumers in England and France now choose from at least two major supermarkets when making their shopping choice (J. Corstjens et al, 1995) Location is still the major factor in choice, but it no longer holds sway in the final choice of supermarket. The market is saturated to a point such that stores must actively compete for shoppers.

3.1.2. Service

Although service is sometimes an important competitive tool in U.S. retailing, experience in most Western European states (including rich ex-West Germany) shows that for large proportions of European shoppers, retailing is essentially a **low added-value activity**. This is evident in the massive vote away from friendly local suppliers and helpful specialist stores, in favor of wide choice, low price, low service stores, in every retail sector (for example, electrical, clothes, toys, furniture, DIY). A pleasing environment, help at check-outs, and other conveniences are welcome only up to the point where their cost becomes apparent in the final price of goods. High-service food retailers seem only to be viable on a very small scale simply because the high-quality market segment in any one place except, say, Knightsbridge (Harrods's Food Hall) and Place Vendôme (Fauchon), is not large or dense enough. Experiments in higher quality stores (such as Somerfields in the UK) have not been successful. In fact, because price is often perceived rather than calculated objectively, in an environment of high price sensitivity, high-service stores can be penalized simply for "looking more expensive". This lack of value added contrasts notably with many of the FMCG products retailers handle, where good quality premium brands are often also the market leaders.

On the other hand, if a retailer does discover some service that genuinely adds more value than cost, it can often be easily copied. Any superior service that *does* attract shoppers successfully (for example, the provision of plastic bags or extended opening hours) will soon be duplicated, and the only long-term effect will be to increase costs for all competitors and/or increase consumer surplus.

Thus service is constrained as a differentiator, on the one hand beause European shoppers seem relatively uninterested in service as compared to price, and on the other because successful service innovations are often copiable.

3.1.3. The Lure of Price

Price competition, by contrast, is a natural tendency in FMCG retailing.

Firstly, because price propositions are effective, and this has been proved equally true in both the UK and France. In the UK in the late '70s, Tesco lost market share as a result of their deteriorating image and their slow reaction to the out-of-town locations of their competitors. To recover market share Tesco dropped their long-running promotion with Green Shield Stamps and initiated a program of deep price cuts called "Operation Check-Out". The price cutting was so effective that their major competitors, in particular Sainsbury, were forced to follow suit ("Discount '78") and amplified the price war only to discover its devastating effects on their respective bottom lines. Subsequently, Tesco repositioned towards Sainsbury on the "quality-value" spectrum through

better-quality merchandise, a higher proportion of quality own-label merchandise and out-of-town locations orchestred with heavy advertising campaigns. The newly formed Argyll (via the purchase of the UK operation of U.S. retailer Safeway) also followed suit and this led to a new equilibrium of "quality-value" competition between the major UK grocers for the next 10 years.

In 1993, forced to react to a new wave of discounters, Sainsbury's was the first major chain to respond by launching its "Essential for the essentials" campaign, and cut prices on many of its basic groceries. Tesco was forced to follow with a "value" initiative, which was extremely successful in terms of volume sales. Again the effectiveness of theses initiatives set off price deflation in the whole sector. By mid-1994 smaller chains such as William Low and Budgen were buckling under the attractive power of the cost cutting by the large chains (including by then Asda and Safeway).

Meanwhile in France, Leclerc and Intermarché, with their inexorable focus on price and corresponding rise in market share, have shown that a price platform is equally attractive to French shoppers.

Secondly, the ownership and financial structure of retailers often predisposes them towards price competition. French retailers (recall Table 1, above) are typical of businesses with low margins and correspondingly high break-even levels, in that they are highly sensitive to volume (or market share) fluctuations. Working with small net-profit margins and high fixed costs makes the French retailers very sensitive to sales volume to reach their high break-even points. High leverage usually results in more aggressive market behavior because price cutting has more immediate volume effects than quality-type competitive warfare. The resulting fixation on short-run sales volume makes French retailers very vulnerable to entering price wars that are then difficult to end.

Price, as a competitive strategy, is expensive but difficult to avoid. Because price is so important in European FMCG retailing, no retail chain can afford to back off and suffer the immediate loss in sales. As has been seen in France, for many chains, following Leclerc is most likely to lead to bankruptcy in the longer run. Thus although price is a continual lure for FMCG retailers and, it is a cul de sac for the industry as a whole except for the lowest cost hard discounter.

UK retailers, despite having lost the traditional protection of location, have managed to achieve comfortable profit margins, making them less price driven and more similar to manufacturers, where high margins reinforce their ability to play the quality game. Given the powerful forces in favor of price competition within retailing, the UK phenomenon seems to be the one that needs explaining.

3.1.4. Concentration, and the Effect of Price Competition

The theory of industrial organization predicts that the higher the concentration ratio, the lower the likelihood of purely price competition. Retail concentration has been significantly higher in the UK than in France; although in France it is increasing, and rapidly catching up to that in the UK. Table 7 shows the high degree of concentration of the top UK retailers and the significant consolidation in the French retail sector compared to 13 years ago.

Table 7: Retail Concentration in France and UK 1980-1993

	Cumulative Market Share Top 3		Cumulative Market Share Top 4		Cumulative Market Share Top 5	
	1980	1993	1980	1993	1980	1993
France	18	40	22	49	25	58
UK	30	49	35	60	39	66

Source: Nielsen, AGB, and Verdict Market Research for the UK, and Casino Market Research for France

It is clear that French retailing has become considerably more concentrated in the past 10 years. At the top-three level, concentration has more than doubled from 18% to 40%, well above the UK level of 1980.

This concentration has come about largely because of the fierce price competition in the French market during this period. The weakest of the price-driven retailers become attractive take-over targets for the stronger players because of their low acquisition price (weak performance), and their store locations are also attractive in an environment of saturation and government control of new store openings. Table 8 illustrates the concentration in action in France in the early 90's, during which established players have been able to pick-up "exhausted" competitors at very reasonable prices (about 25% of sales).

Table 8: French retailer concentration

	Acquirer	Target
1990	Rallye	Genty Cathiard
1990	Comptoirs Modernes	Major
1990	Casino	La Ruche Méridionale
1990	Promodes	Codec
1991	Carrefour	Montlaur
1991	Carrefour	Euromarché
1992	Casino	Rallye

Source: M. Benoun and M.L. Helies-Hassid, 1993

Low concentration tends to lead to price competition, but that same price competition provides an incentive to the stronger players to engage in prolonged price wars to achieve higher levels of concentration in the hope of thereby achieving higher profitability in the long run. Industry experts (and simple extrapolation) suggest that price competition will weed out more retailers in France, leading eventually to the concentration levels observed in the UK.

However, these dramatic changes in concentration in France have had little impact on profit margins (even taking into account our corrections), at least as yet.

During the period illustrated in Table 7, profit margins in the UK fattened significantly, although concentration increased more slowly. If we want to believe that concentration improves profit margins, it seems that either there must be a threshold, or a significant lag.

3.1.5. Hegemony - the Unelected Leaders

Sometimes a few retailers, and sometimes a single player, set the scene and influence the competitive behavior in the whole sector. In the UK, Marks & Spencer and Sainsbury have been building their store image through quality store brands for a century. This has resulted in confidence among shoppers that a store's name can be equivalent to a manufacturer's brand name; i.e., the store's name can guarantee the quality of goods sold under that name. In more recent times, Sainsbury has clearly led the pack towards non-price competition. For over a decade, Sainsbury's food advertising has set the standard in terms of approach and

photography, and Sainsbury's new stores have set a standard for range and quality. As a result, even hard-discounters feel they have to upgrade compared to, say, Denmark or Belgium, to be acceptable to the "spoilt English shopper".

In France, Intermarché and especially Edouard and Jean-Michel Leclerc have established a strong price-competitive retail sector, and have consistently indoctrinated French consumers on the importance of low retail prices. In Germany, notwithstanding even higher concentration than in the UK, Aldi, a privately held efficient hard-discounter, has imposed price-competitive behavior on everyone.

Although KwikSave and a variety of other small, low price chains have operated successfully in the UK, their presence cannot compare with the impact of the two aggressive, franchised buying groups Leclerc and Intermarché in the French retail market. Over a period of 20 years they have increased their combined share to about 30% through a fast-expansion program for their supermarkets and hypermarkets. This fast expansion of price-oriented Leclerc and Intermarché was made possible in part because of the relatively high prices being charged by family-owned regional retail chains, which tacitly agreed not to encroach on each other's territories. When the regional family-owned retailers increased their national drive, they were constrained to respond to this market environment by being price competitive.

Fast expansion was possible by Leclerc's and Intermarché's system of franchising. Each store is owned by an independent operator. In exchange for the Leclerc or Intermarché name, and buying and merchandising support, the operator is committed to central directives on pricing, buying, and general store policy. By their own rules, no individual franchisee is allowed to own more than a very limited number of stores, so growth is generated by recruiting new store owners. These, on average, are only able to bring in limited equity and are therefore very dependent on Intermarché and Leclerc and on very long supplier credits. Their positioning as low-price supermarkets is controlled from the center, and they are known by manufacturers as very tough and aggressive negotiators using delisting as a run-of-the-mill policy. Intermarché, in particular, has specialized in relatively small units (around 1,200 sq. meters) selling mainly food products, located close to the center of medium-sized towns. This strategy is interesting in a saturated market, as it can overcome increasingly tight location regulations.

The charismatic leaders Edouard Leclerc and his son Jean-Michel of Leclerc gain much free publicity by taking up controversial "consumer" causes. Intermarché was in fact founded (in 1969) by the secession of 90 Leclerc stores. Calling themselves "the Musketeers", their approach again puts an enormous focus on price, publishing an "Argus" magazine listing many of the prices within their stores and inviting shoppers to use this publication to compare their prices with competitors. All this PR and publicity activity constantly pounds the importance of low

prices. Both Leclerc and Intermarché were favorites of the socialist French government in their drive to reduce inflation without price controls.

Beyond certain tendencies to price competition, and the effects of concentration that should have a similar influence in both countries, one cannot ignore or explain the idiosyncratic existence of industy leaders. That the Sainsbury family should be devoted to high-quality food and the Leclerc family to "grocery" as an efficient business at the service of the consumer totally contradicts the national stereotypes, but seems to be the case.

3.2. Private Label (P.L.)

The private-label situation at English and French retailers is quite different in two respects: its volume and its positioning.

Table 9 shows how for the major UK players private-label sales represent about half of their sales whereas for French retailers, although its share is increasing, private label represents at most half of what it is for UK retailers.

Table 9: Percent Private Label inPackaged Grocers (1992)

Sainsbury	56	Carrefour	17
Tesco	45	Promodes	12
Safeway	39	Casino	27
Asda	34	Auchan	13
Gateway	32	Intermarché	21
Morrison	29	Leclerc	9

Source: R. Piper and A. Breese, 1993 (UK retailers) and A. Boudet, 1993 (French Retailers).

We will argue that these store brands play a pivotal role in explaining the differences between the retailers on either side of the channel. Firstly, we wish to explain how English retailers Sainsbury,

Tesco and Argyll (Safeway) have managed to achieve a reputation for high-quality store brands, whereas French retailers' store brands are perceived as poor substitutes for brands.

3.2.1. History of Own Label in the Two Countries

Sainsbury and Marks & Spencer have a century-long history of quality private label. For many years most other UK retailers didn't follow or weren't able to replicate Sainsbury and Marks & Spencer's high quality. However, when Tesco and Argyll realized that it was necessary and profitable to compete on this dimension, the consumer was able to understand and accept their proposition.

In France, retailers are the prisoners of a confused concept of private labels. In the seventies, store brands were introduced as a cheap "no frills" alternative and were perceived as poor quality. Furthermore, consumers were exposed to a variety of private labels: "white products", "orange products", "no-brand products" and "generic products", depending upon the creativity of the different retailers. These store brands had low procurement costs and were used by the retailers as means of generating margins and as instruments to continue the price game. (A. Duverdier and F. Cabaret, 1990).

A few retailers, e.g., Casino and Monoprix, have tried to develop a quality store brand, but their efforts were mostly lost in the overall market trend of price competition. French consumers have been led to believe, by their experiences with the majority of retailers, that store brands are cheap and inferior alternative to quality manufacturer brands. In the late '80s and early '90s, several major French retailers have been inspired by the success of their English counterparts to try to reverse their store brands' image.

3.2.2. Television Advertising

An additional hurdle to build quality own-label brands for French retailers is the unavailability of television advertising. Whereas in the UK the quality retailers are also the highest advertising spenders, even outspending the biggest manufacturer's brands, French retailers are not allowed to advertise on television.

Table 10: Rank order of top retailers' advertising spending in France and UK

		1991	1992
UK	Tesco	1*	1
	Sainsbury		9
	Safeway	8	11
	Asda	14	21
		13	
FRANCE	Leclerc	17	16
	Carrefour	21	18
	Auchan	22	23
	Intermarché	24	33

* In 1991 Tesco was the heaviest advertising spender of all **brands** in the UK, though some companies spent more across many brands.

Source: UK: Campaign, April 1992 and 1993; France: AACC, 1992 and 1993

This constraint has been imposed on retailers by the political lobbying of the owners of small retail outlets. In the fast-moving consumer goods industry, television advertising is probably the single most important force in creating quality brands. It is hard to imagine manufacturers in the FMCG area being able to develop quality brands without television advertising.

Marks & Spencer's built their quality image without spending any money on advertising, but they have built this image over many years. Advertising allows the telescoping of time in putting across a quality image. Lack of television advertising similarly reduces the possibility of retailers establishing quality (private) brands.

The absence of television advertising can reinforce price competition. Retail stores compete on the basis of location, price or "product differentiation". Product differentiation implies a unique perception of the store on dimensions such as service, quality of goods, assortment, convenience, and in-store help. A store can position itself in the minds of the consumers either by only providing products that communicate this positioning through experience alone, or by using advertising to communicate (and therefore reinforce) such a positioning. In the absence of television advertising, it is more difficult to build such an image through consumer experience only. Furthermore, this

consumer experience must be consistently reinforced over a significant amount of time, à la Marks & Spencer's, to be successful. Such an apporoach leads to severe constraints in the management of the retail outlet and therefore reduces the flexibility to compete in the short run. Competing on the basis of price becomes a more attractive option, as this type of competition is less constrained by the availability of national advertising. A price message is relatively simple to communicate, and radio, newspapers, and leaflets can do the job well. Image advertising, on the contrary, is much more powerful via the television medium. FMCG manufacturers use television advertising to get product messages and the associated images across to consumers. The lack of television advertising is therefore a severe handicap for French retailers in following a quality own-label strategy.

French retailers, we will argue in this paper, can succeed in developing a quality image but it will take longer because television advertising is note available to them, and because they have started from a base of cost claims and poor quality.

3.2.3. Own Labels' Link with Profits

Tesco's history suggests the degree to which private label can help a store increase its profitability. As Tesco's private-label share moved from 23% of sales in 1982 to 50% in 1992, Tesco was able to raise its net margin from 2.6% to 6.6% during the same time period (see Figure 1).

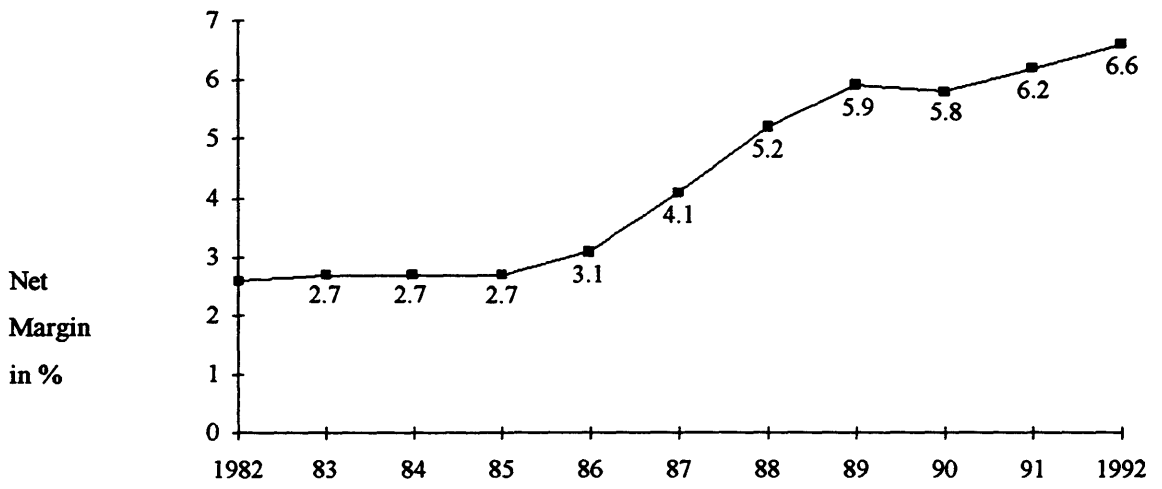

Figure 1: Tesco net-profit margin during the period when it was strongly developing its quality own-label sales

Source: A. Boudet, 1993

A comparison between the gross margins of the six sample stores and their shares of private-label sales also suggests that private label might be an important lever for improving profits (see Table 11).

Table 11: Gross Margins of English and French Retailers compared to private-label sales (1993)

	Carrefour	Promodes	Casino	Sainsbury	Tesco	Argyll
Sales	100	100	100	100	100	100
Cost of goods sold	88	89	84	79	79	80
Gross margin	12	11	16	21	21	20
Private-label share	17	12	27	56	45	39

Source: B. Beaumont, 1994 and Table 10.

There are two reasons why private label helps to increase a store's profitability.

3.2.3.1. Direct Profitability of Own Label

Due to savings in marketing compared to large FMCG manufacturers and competitive prices offered by industrial suppliers, retailers can make *higher margins* on own brands and still offer good value to the consumer in comparison to similar manufacturer brands. On a rather standardized grocery product (milk, canned products) the major brands will bring a store a gross margin of only between zero and 10%. The comparable own label often gives a gross margin of between 10% and 20% (while still being supplied cheaper to the consumer). A store such as Sainsbury's, with 56% of sales in private label, is making good margins on this 56%.

But this is not all.

3.2.3.2. Indirect Influence on the Profitability of National Brands

Price competition is inevitable when buyers can costlessly substitute the offer of one supplier with that of another. Conversely, when suppliers manage to differentiate their offerings and create

consumer loyalty for their 'brand', they can improve their profits. Retailers cannot differentiate themselves by using manufacturer brands except by competing on price. However, if they develop differentiated, high-quality own brands, they create *consumer loyalty* which in turn translates to store loyalty. Many high quality own labels are not *directly* substitutable on switching to another store: private label serves to differentiate the store and create loyalty, the key to profits. Quality own-label brands can earn their retail owners more money because the same product is not on sale elsewhere, and is thus not directly substitutable from another supplier.

French retailers complain that they lose money on the 300 largest-selling manufacturer brands. It is difficult for an outsider to get factual confirmation that these brands are indeed being sold below cost -for example, whether all incentives given by manufacturers 'delay of payment, year-end bonuses, promotional support, etc.) are taken into account in the profit calculations. Whether the real profitability of these top brands is negative or positive, it is probably fair to say these brands are less profitable to French retailers than they are to their counterparts in the UK, and also that these top brands are relatively less profitable than smaller brands and own label.

This is because during periods of intense price competition between retailers, major brands are used to establish the price image of the store in order to generate store traffic. At the same time, other brands and own label are used for generating profits. Because all stores carry the most popular brands, and many consumers are interested in them, the prices of these major brands affect store image and traffic most significantly.

Indeed, some American stores argue that the high margins on own label should be used to subsidize traffic generating national brands: this is close to the approach in France, but not the philosophy in the UK.

In stores that aim to build traffic with their innovative, added-value own-label brands and fresh products, in-store service, etc., the major brands play a different role. Shoppers are attracted to the stoes by non-price factors, by loyalty to the store's own brands and an overall quality/value promise (supported by television advertising). The popular national brands are available to add choice, variety, and *to satisfy those shoppers who are truly brand loyal, and less swayed by price*. The more value-conscious shopper will usually take the private-lavel alternative, leaving the retailers to generate profits even on the most popular national brands. In other words, under intense price competition national brands are there to generate traffic; in a quality store they are there to satisfy the range needs of less price-sensitive brand loyalists.

Clearly, if this is the case, the national brands will earn stores better margins in the second scenario (M. Corstjens and R. Lal, 1995).

3.3. Other Differences

Once the importance of own label is recognized, the other observable differences between French and UK retailers can be seen as flowing from this fundamental policy difference.

3.3.1. Quality of Personnel

The nature of competition plays an important role in how retailers develop the human resources needed to manage the stores. In France the key positions in a retail organization are in functions directed at the internal operations of the retailers. For example, operations, buying, logistics, and finance are the functions with the most power and prestige in the organization. In UK retail organizations, functions directed at interacting with customers and their needs have been relatively more important. The marketing know-how and expertise of UK retailers is even admired by their manufacturing counterparts, whereas in France, manufacturers' marketing specialists are frequently scornful about the degree of sophistication of their retailing counterparts.

Marketing expertise involves a lot of people. It requires that more time be spent in analyzing data from the stores; in buying, researching, developing, and testing products; in designing packaging; in quality control; and in liaison with suppliers. More time implies more people. UK retailers are taking over many of the functions previously carried out by FMCG manufacturers, and this implies more people. Furthermore, UK retailers follow a strategy that is heavier in personnel needs and significantly higher than UK labor costs, yet as a percentage of sales, UK retailers spend more on personnel.

Table 12: Personnel Costs/Sales

Carrefour	8.6%
Promodes	7.3%
Casino	12.3%
Sainsbury	11.2%
Tesco	10.2%
Argyll	10.6%

Source: Authors' calculations from company reports (1993)

French retailers, as in so many other dimensions, are catching up. In the '90s, several French retailers began recruiting marketing managers from FMCG manufacturers to develop their understanding of shoppers, to extend their use of category management, and to develop their store brands.

3.3.2. Investment in Technology

Another noticeable difference between French and English retailers concerns their respective mastery of technology. English retailers are considered to be significantly more advanced than their French counterparts in logistics and information technology.

Table 13: Inventory Value as a Percentage of Sales Value (1992)

France	Carrefour	7%	or	21 days
	Promodes	8%	or	24 days
	Casino	10%	or	30 days
UK	Sainsbury	4%	or	13 days
	Tesco	3%	or	10 days
	Argyll	5%	or	15 days

Source: Authors' calculations from company reports.

Investing significant financial and managerial resources in the management of logistics and in-store operations has been a priority among English retailers for many years now. They have invested to achieve a favorable cost position and enviable efficiency. French retailers are much less sophisticated in their use of advanced technology.

Why have French retailers been less motivated or able to realize these efficiency savings?

For the UK competitors, early investments were fueled from their profitable differentiation strategy and from a favorable attitude of the English stock market towards the retailing industry.

Partly due to their lower profitability and to their family-ownership structure, the lack of availability of funds to French retailers to invest and integrate these new technologies has not allowed them to capitalize on the potential longer-term efficiency gains. For example, Direct Product Profitability (DPP) is commonly used by English retailers to evaluate the marketing programs of their suppliers and to maximize their product assortment profitability. Although the concept of DPP is quite straightforward, putting it into practice requires very detailed cost and demand information at the Stock Keeping Unit (SKU) level, and this for many thousands of SKUs. French retailers are lagging behind in this respect and it is therefore far more difficult for them to optimize their product-assortment profitability. In their negotiations with suppliers, French retailers are driven by competitive parity rather than demanding marketing support to enhance their competitive strategy. In other words, French retailers' mindset is "we want to have at least as good conditions as our competitors to be able to compete successfully with them on price". This approach led to Machiavelian strategies of manufacturers, who, in the '80s, agreed to terms dictated by the retailers, only to subsequently raise the list prices (which are the same for all retailers) of their brands to the retailers. Thus, though French retailers seemed to succeed through their aggressive stance in the negotiations, the manufacturers were able to maintain good margins. This approach was more easily implemented in inflationary times. Today, with increasing sophistication of the retailers and low inflation, this strategy is less viable and is evident in the lower profitability of manufacturers in France.

Similarly, UK retailers have almost completely switched to centralized distribution resulting in operational, financial, and marketing advantages. For example, using centralized networks instead of local distribution centers has enabled UK retailers to cut deliveries to stores from 60 per day to a dozen or less.

This centralization, coupled with EDI systems, multi-temperature vehicles, and substantial outsourcing to efficient service companies have given UK retailers a substantial advantage over their French colleagues. The latter are moving in the same direction but still have a serious efficiency gap to bridge.

4. Conclusions

Our main conclusion is that, in contrast to the French, UK retailers have followed a loyalty-building strategy based on quality own label. It is their success in creating their own brands that has led to their better profit position. This "national approach" has come about through the hegemony of certain leading retailers. Their task has been facilitated by retail concentration, the availability of television advertising, and their heritage of quality. In contrast, French retailers have been driven to price cutting (once location ceased to offer protection) by their ownership

structure, the hegemony of Leclerc (and spin-off Intermarché), and the impossibility of grasping the UK solution in the short run (because of history, television, and -earlier- lack of concentration).

How will retail industries for FMCGs evolve in the future, as location ceases to provide competitive protection? Will it be the French model of price competition or will it be the UK model quality own label and store differentiation?

It is our view that either:

1. a two-tiered system will evolve, in which a group of retailers emphasizing the price dimension and another group focusing on quality coexist. By "quality" we mean above-average quality at reasonable prices -the need to limit the appeal of the cheaper stores will ensure that the "quality" stores must always keep their pricing very competitive. The idea of a two-tier industry is also grounded in sound economic theory in which a firm can compete either on the basis of cost leadership or on the basis of product differentiation.

or

2. that either model may dominate in the short run, but that a national industry will tend to oscillate from one to the other in the long run. Oscillation could be caused by price competition causing concentration, enabling quality to emerge. Conversely, high quality and profits can leave a gap in the market for price cutters to enter, and drive price back onto the competitive agenda. The risk of opening up a stable, quality market to a new wave of discounters will again ensure that any "quality" competitors are always constrained to offer competitive prices.

In any and both scenarios, price will always remain an important part of the retailer's offer.

Similar to the manufacturers' problem of justifying price premiums for high-quality brands and sometimes having to reduce the price of these brands to bring them back in line with the perceived quality difference, quality retailers must manage their price premiums. Marlboro Friday illustrated how even the world's best known brand needs to justify its price premium. Generic cigarette brands forced Marlboro to re-calibrate its perceived value at a price 30% below its previous level.

In the last year in the UK, the quality-value retailers have had to respond to the increasing physical coverage of the market by hard-discounters, mostly due to the entry of foreign players such as Aldi (Germany), Netto (Denmark), Ed (France) and Costco (U.S.). The major chains have responded by expanding the part of their assortment known as "tertiary brands" (i.e., "cheapos") while dropping lesser-known manufacturers' brands and slightly reducing the prices of their quality

own label. This move was also caused by the fact that the "cozy" competition between the quality-value retailers had raised suspicions, voiced in the English media, about excessive prices and margins (Skipworth and Ruddock, 1993).

The price reductions made in 1993/1994 by Sainsbury, Tesco, and Safeway are of the same nature as the price reduction made by Marlboro. Although their quality image was still high, their price premium was out of line with the value provided by a set of expanding low-price competitors. This forced Sainsbury, Tesco, and Argyll to re-establish their value through selective price reductions.

In recent times in France, concentration has increased and French retailers have improved their image with stockmarket investors. Large French retailers have understood the choice between "price" or "non-price" competition, and the advantages of the latter. Their efforts to develop quality own label seem to be bearing fruit and they are investing seriously in improving their technology, developing more sophisticated marketing, R&D and logistics management. All in all, the major French chains are evolving towards the UK model as described above. The hard-discounters and quality-value retailers thus seem to be currently establishing a new equilibrium in France. As the non-price sector of French retailing develops, it leaves a defined position for the focused hard-discounters (small assortment and low-cost driven operators [cf. Table 14]). This again illustrates the fundamental two-tier structure of the industry. The speed and degree to which this will be achieved will depend upon the availability of television advertising, which is so crucial for quality-value retailers.

Table 14: New Supermarket Openings in France

	New supermarket openings in France			
	1989	1990	1991	1992
New hard-discounter supermarkets	25	78	121	231
Total new supermarket openings	364	355	326	398
Share of hard-discounters in new store openings	6.9%	22%	37%	58%

Source: INSEE 1991-1993

Overall it is clear that price will continue to play a major, but variable and fluctuating, role in FMCG retail competition and marketing. Both manufacturers and retailers need to reflect carefully

on the implications and monitor the tides of price competition. Manufacturers must consider how they handle negotiations with retailers, through time and by strategy: they need to negotiate and flourish both with price-oriented and quality-value retailers. In markets ripe for a move towards quality competition, manufacturers must be ready to face the danger posed to their brands by retailers wishing to establish quality own label.

Retailers, on the other hand, must know to which of the two camps they belong. We believe that trying to straddle the two strategies, or worse, changing between the two, is the cause of many retailing failures. Quality retailers should also bear in mind (most crucially when planning expensive new stores) that the price tide could turn and leave them trying to pay back their investment on margins determined by hard-discounters.

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