

## Guest Editorial

# Retail Power: Monster or Mouse?

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*Many industry observers contend that retailers have increased their power relative to manufacturers over the past twenty years. The alleged growth in trade power has been attributed to higher concentration of retail buying power, buyers who have access to scanner information, and more frequent sales promotions. Increased sales promotions are said to achieve short-term gains in sales, but at the expense of long-term increased consumer price sensitivity and decreases in funds for pull programs. If this power shift has really occurred, a shift in the relative profitability of manufacturers and retailers would have been expected to also occur. We use data on the food industry to examine this hypothesis and find that manufacturer profits have been increasing at a fairly steady rate over the past ten years while retailer profits have been quite stable. This evidence casts doubt on whether a shift in power has really occurred and we offer some speculations on why the evidence does not support the conventional marketing wisdom.*

### INTRODUCTION

It has become a cliché to speak of the growing power of the trade in consumer marketing. The picture painted by many knowledgeable re-

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searchers and industry observers is of the emergence of giant retailers who use their power to extract promotions from manufacturers:

And now with retailers calling most of the shots, manufacturers are resigned to bow to their wishes. (Johnson 1988)

One of the most significant phenomena in retailing in recent years has been the shift in power from manufacturers to the trade . . . the dominant players have become the big chains. (Buzzell, Quelch, and Salmon 1990)

. . . the historical shift in market power from manufacturers to large-scale retailers. This has enabled the latter to exercise their enhanced buying power in order to extract advertising allowances and additional discounts from manufacturers. (Fulop 1988)

Forces and trends have shifted a great deal of market power to the retailers, who can now use allowances and coupons for their own purposes, and, in the process reduce their dependence on the manufacturers. (Achenbaum and Mitchel 1987)

Retailers don't want to openly discuss how much power has shifted from the manufacturers to them. They don't want to bite the hands that feed them. (Elman and Hughes 1988)

Chain executives have reported increases in the number and value of discounts and other incentives offered by manufacturers, but decreased acceptance of manufacturer-provided displays. Clearly, their power relative to the manufacturer's power is growing. (Oliver and Farris 1989).

Researchers often point out that retailers now have access to current product movement data from scanner technology and that this information should improve their negotiating position versus manufacturers. It is easy to conclude that the industry is undergoing a series of self-reinforcing trends:

- (1) the growing concentration among retailers has given the trade the ability to force promotional allowances and other concessions from manufacturers;
- (2) these discounts and allowances are argued to come at the expense of spending for advertising and "pull" programs and the negotiating leverage of the manufacturer is further weakened; and
- (3) because of frequent discounting consumers become more price sensitive and the short-term effect of trade discounts is further enhanced.

Although a few articles have taken both sides of the issue or even defended selected use of discounts (Haponieu 1989; Farris and Quelch 1987), the bulk of opinion seems to support a significant and widespread increase in trade power versus the manufacturer.

#### POWER AND PROFITABILITY

The industrial organization literature provides a strong theoretical basis for viewing "super-normal" profits as an indicator of possible market power (see Bain 1968 for a theoretical treatment). In fact, empirical research on the structure-conduct-performance relationship relies heavily on the positive correlation between advertising, profitability, and concentration, interpreting the positive impact of market concentration on profitability as evidence of market power. These empirical studies invariably use the Price-Cost Margin or rates of return like ROS, ROE, and ROA as measures of market power (e.g., Gomes 1986; Martin 1979, 1988). Thus, the concept of market power and the size of profit margins have been used almost synonymously.

Some early work distinguishes between consumer goods manufacturers and retailers in the context of industrial organization theory. For instance, Boyer (1974) provides empirical evidence for the difference in the Advertising-Profit relationship between manufacturers and retailers. Porter (1976) discusses the effect of interactions between manufacturer and retailer actions on product differentiation and manufacturers' profit rates.

Porter (1974) also uses the rates of return of manufacturers and retailers synonymously with their bargaining power vis-a-vis each other. However, in view of the fact that profit and power are so closely connected in the economics literature, we find it somewhat curious that there is an absence of empirical evidence on relative profitability of retailers and manufacturers of consumer goods.

If the retailer-manufacturer balance of power has indeed shifted toward the retailer, whatever the reasons for the shift might be, we would expect other changes to occur: specifically, retailers should now earn higher profits and manufacturers lower profits relative to each other and as compared to periods before the power shift occurred. Clearly such a comparison cannot be made in terms of "absolute" sizes of profit margins as a fraction of sales. Retailers, because of their high rates of inventory turnover and lower investment costs, typically earn much lower profits as a percentage of sales (ROS) than manufacturers, even though their ROIs may be more comparable. The relevant question is whether the ratio of these profit rates has changed over the preceding years during which the balance of

power has supposedly been shifting toward retailers. Grant (1987) does address this issue in his analysis of Manufacturer-Retailer relations in the UK, during 1975-1983. He notes that manufacturers' Return on Capital has been decreasing, both in absolute terms and relative to retailers, in the UK.

#### EMPIRICAL ANALYSIS

We analyzed trends in the profitability of food manufacturers and retailers using 20 years of data, from 1971-1990, available on the COMPUSTAT industrial database. There were too few non-missing observations to analyze for the year 1971. Our analysis is therefore based on 19 years of data, from 1972 to 1990. The number of food retailers with non-missing data ranged from a low of 25 in 1972 to a high of 51 in 1989 and 1990. Similarly, the number of food manufacturers with non-missing data was lowest in 1972, at 63, and highest in 1989, at 152. The data are available from the authors upon request.

The variables downloaded and analyzed were: (1) Sales; (2) Cost of Goods Sold; (3) Net Profit after depreciation, interest, and extraordinary expenses/income, but before taxes; (4) Net Profit after taxes; and (5) Total Assets. Three standard profitability measures were calculated: Gross Margin/Sales (GM), Net Return on Sales (ROS), and Net Return on Assets (ROA). The two net rates of return were calculated using Net Profit before taxes (ROSBT and ROABT). ROS was also calculated using Net Profit after taxes (ROSAT), to ensure that taxes did not alter the general pattern of profitability trends observed.

#### Trends in Retail and Manufacturer Profits in the Food Industry

Tables 1 and 2 show the mean levels of four Profitability measures, weighted by Sales, for food manufacturers and retailers, respectively, during the period 1972-1990. The profitability indices, *do not* show a relative increase for retailers. On the contrary, if any change in relative profitability is present, it seems to favor the manufacturers. Even gross margins, which have, on average, been increasing for retailers, have increased much more rapidly for manufacturers (see Figure 1). Manufacturers' ROS depicts an *increasing* trend while retailers' ROS stays relatively stable at first and then *decreases* from 1984-85 onwards. The pattern remains the same for both ROSBT and ROSAT. ROA depicts an interesting trend. It tends to decrease for manufacturers but vacillates for the retailers.

Figure 2 depicts the ratio of manufacturer to retailer profitability, for each of the three measures—Gross Margin, ROSBT, and ROABT. Note

**TABLE 1  
MEAN PROFIT LEVELS FOR FOOD MANUFACTURERS**

YEAR	MARGIN (%)	ROSBT (%)	ROSAT (%)	ROABT (%)	SALES (\$ mill)	NO. OF FIRMS
1972	25.12	8.03	4.29	13.04	745.37	63
1973	23.88	7.72	4.11	13.20	845.34	68
1974	21.23	6.37	3.33	11.34	974.29	74
1975	22.21	6.82	3.61	12.73	1037.84	77
1976	23.88	7.75	4.07	14.13	1107.60	78
1977	23.74	7.58	4.02	13.43	1274.29	77
1978	24.44	7.62	4.06	13.06	1442.39	78
1979	23.97	7.00	3.98	12.16	1683.35	80
1980	24.82	7.05	3.93	12.29	1814.63	84
1981	25.93	7.33	4.26	12.01	1906.69	85
1982	25.54	6.82	3.81	10.73	2064.90	89
1983	27.18	7.68	4.31	12.08	2068.91	92
1984	32.03	7.38	4.24	11.51	2072.93	96
1985	33.15	7.66	4.30	10.91	2057.84	111
1986	34.27	7.79	4.36	10.83	2144.74	124
1987	36.49	8.92	5.15	12.65	2141.76	141
1988	35.41	8.36	4.96	10.87	2116.61	145
1989	34.87	7.92	4.78	10.38	2430.27	152
1990	35.61	8.58	5.16	10.63	2793.18	147

**Trend Regressions for (i) 19 Years; (ii) '72-'79; (iii) '80-'90**

	MARGIN (%)	ROSBT (%)	ROSAT (%)	ROABT (%)	SALES (\$ mill)	NO. OF FIRMS
β '72-'90	0.85* (0.10)	0.06* (0.02)	0.07* (0.01)	-0.14* (0.03)	---	---
β '72-'79	0.05 (0.21)	-0.04 (0.09)	0.00 (0.05)	0.01 (0.14)	---	---
β '80-'90	1.27* (0.18)	0.16* (0.04)	0.12* (0.02)	-0.13 (0.07)	---	---

\* Significant at the 95% Confidence Level  
Note: Standard Errors are in Parentheses

**TABLE 2  
MEAN PROFIT LEVELS FOR FOOD RETAILERS**

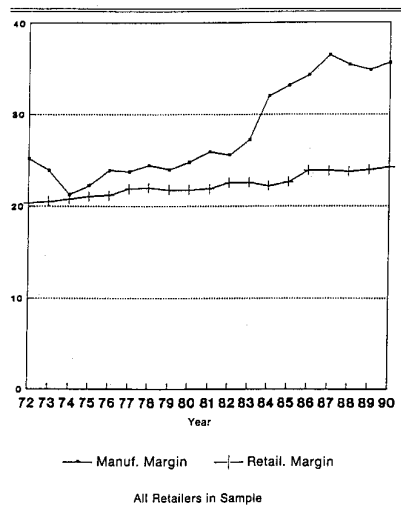
YEAR	MARGIN (%)	ROSBT (%)	ROSAT (%)	ROABT (%)	SALES (mill \$)	NO. OF FIRMS
1972	20.34	1.25	0.71	5.80	1001.12	25
1973	20.50	1.71	0.95	8.59	1078.44	26
1974	20.75	1.18	0.43	5.24	1142.89	29
1975	21.03	2.03	1.09	11.19	1269.07	29
1976	21.15	1.93	1.04	10.37	1404.63	29
1977	21.87	1.92	1.04	9.31	1551.70	29
1978	21.96	2.10	1.09	9.09	1706.08	30
1979	21.77	2.00	1.17	8.88	1907.93	31
1980	21.75	1.73	0.99	7.91	2206.75	31
1981	21.87	1.49	0.74	6.79	2408.24	31
1982	22.54	2.20	1.30	9.98	2341.68	34
1983	22.54	2.25	1.32	9.62	2577.79	35
1984	22.21	2.29	1.36	9.46	2983.36	35
1985	22.60	2.29	1.36	9.32	3159.06	36
1986	23.89	2.02	1.08	7.61	2985.22	39
1987	23.86	1.78	0.97	7.13	2882.94	41
1988	23.77	0.95	0.52	4.25	3014.66	46
1989	23.95	-0.28	-0.77	0.87	3136.65	51
1990	24.21	1.09	0.46	4.38	3304.07	51

**Trend Regressions for (i) 19 Years; (ii) '72-'79; (iii) '80-'90**

	MARGIN (%)	ROSBT (%)	ROSAT (%)	ROABT (%)	SALES (mill \$)	NO. OF FIRMS
β '72-'90	0.21* (0.01)	-0.03 (0.03)	-0.02 (0.02)	-0.20 (0.09)	---	---
β '72-'79	0.25* (0.03)	0.11* (0.04)	0.07* (0.03)	0.42 (0.30)	---	---
β '80-'90	0.26* (0.03)	-0.13 (0.06)	-0.11 (0.05)	-0.59* (0.218)	---	---

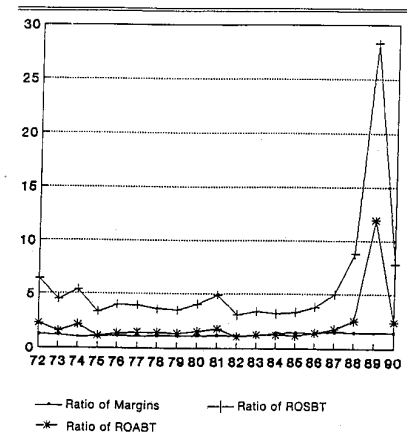
\* Significant at the 95% Confidence Level  
Note: Standard Errors are in Parentheses

FIGURE 1  
Food Manufacturer and Retailer Margin  
1972-1990



that this ratio remains relatively flat during the 19-year period we have analyzed. When there is a change in the relative profitability of manufacturers and retailers, evidenced by the ratio of the two ROSs (and, to a lesser extent, the ROAs) during 1986-1990, the change favors the manufacturers.

FIGURE 2  
Ratio of Manufacturer to Retailer Profit  
1972-1990



Retailer ROS became negative in 1989. The absolute value is used to avoid the illusion of a drop in the ratio.

As might be expected from the plots, a regression of these mean levels of ROS on time provides a significantly *positive* coefficient for manufacturers, and an insignificant but *negative* coefficient for retailers. These coefficients are also listed at the bottom of Tables 1 and 2.

Trends of Mean Profitability for Two Separate Time Periods. The

SIZE OF FIRM	TREND COEFFICIENT FOR		
	Gross Margin	ROSBT	ROABT
Small	0.03 (0.14)	-0.36* (0.07)	-0.74* (0.12)
Large	0.86* (0.10)	0.06 (0.03)	-0.15* (0.03)

\* Significant at 95% Confidence Level  
Note: Standard Errors are in Parentheses

plots suggested that there may be different patterns for the first and second halves of the 19-year-period we are analyzing. Therefore, we estimated the above regression coefficients separately for the two periods 1972-79 and 1980-90. These coefficient estimates are also reported in Tables 1 and 2. The results are very interesting. Note that, over the most recent ten-year period, manufacturers' average margin and ROS have improved more significantly than over the earlier ten-year period. Similarly, the average margins and rates of return earned by retailers have gone down much more significantly over the past ten years. Any tendency for improved returns to retailers, if it exists, was exhibited in the 1972-79 period. Thus the data for recent years, during which concern about relative power shifts has really intensified, defy expectations even more strongly than in the past.

**Profitability of Small Versus Large Firms.** Industrial organization theory hypothesizes differential effects of market power on small and large firms within an industry, the latter being expected to gain more (e.g., Gomes 1986). Therefore, we examined the above trends *separately* for large manufacturers (1989 Sales greater than \$100 mm) and retailers (1989 Sales greater than \$500 mm) versus small manufacturers and retailers.<sup>1</sup>

Table 3 summarizes some of the results for manufacturers for the entire 19-year period from 1972 to 1990. Regressions of mean profit measures on time showed a difference in trends between small and large manufacturers. For small manufacturers, the regression coefficients for all three profit measures were significantly negative. For large manufacturers, on the other hand, Margin and ROSBT had significantly positive coefficients.

<sup>1</sup> In order to minimize missing values, 1989 sales figures were used to decide whether the firm would be classified as large or small.

The coefficient for the ROABT regression remained significantly negative, although its magnitude was much smaller. This negative trend in ROA is consistent with our earlier finding for the pooled sample. Thus small manufacturers seem to have experienced a decline in profitability, while large ones have not. We must note, however, that these results must be used with caution, since the number of firms with non-missing data, in the small firm sample, is quite small. It varies from a low of only 4 in 1979 to a high of 48 in 1989. The number of large manufacturers, on the other hand, is much larger. It varies from a low of 58 in 1972 to a high of 104 in 1989. Given that the mean sales level for large firms is more than \$3000 mm, none of the measures of manufacturers' profitability have suffered, on average.

A similar analysis was done for the retailer sample. However, the number of small retailers was even lower; in 1972, there was data for only one retailer with sales of less than \$500 mm in 1989. Therefore, we do not wish to draw any inferences from these results, and do not report them here. They are, however, available from the authors upon request.

**Controlling for Differences in Sample Composition.** For each of the 19 years, we included all the firms for which data is available in that particular year. There are several firms for which data is unavailable for the earlier years but is available for later years. Consequently, the mean profit measures are based on a smaller sample of firms for the first few years. In order to ensure that the change in sample composition over the years does not account for the trends we observe, we repeated our analyses on only those firms for whom data were available for all of the 19 years. There were 25 retailers and 60 manufacturers in this reduced sample. A comparison of the results based on this reduced sample with the results reported earlier, that include all non-missing observations in any given year, did not show any significant differences. We have not reported the results here in the interest of space. They are, however, available from the authors upon request.

**Removal of Outliers.** We found the large decrease in retailers' ROS and ROA during 1989 intriguing. Further study of the retailer sample revealed that this dip was attributable to two large firms, whose debt and interest expense had escalated during 1988-89, consequently leading to highly negative ROS (-22% and -16% respectively). In order to ensure that these two outliers did not bias the overall retail profitability trends downwards, we deleted them from the sample and repeated our analysis. There was no significant change in any of the trends that we observed in the complete sample. The only difference lay in the reduction of the 1989 retailer profit dip. Whether the debt and interest increases shown by these

two, relatively large firms (1989 sales of \$3736 mm and \$7916 mm) is an indicator of what is to come for other retailers, is something to think about.

#### Power and Profits: The Evidence and Conclusions

Clearly there is no evidence in these data to support the increase in profitability of the retail trade relative to food manufacturers. Assuming that these data are an accurate reflection of national trends in food marketing, three explanations occur to us for the failure to find an increase in trade profitability and a decrease in manufacturer profitability (at least a relative decrease):

1. A shift in power may not have occurred. Manufacturers might have an equal or even greater amount of power relative to retailers compared to 20 years ago.
2. Power may have shifted to the retailer, but retailers may not have been able to translate this power into increased profits because of a combination of managerial ineptness, market constraints, and ferocity of inter-retailer competition (Porter 1976).
3. The whole concept of measuring power of manufacturers relative to retailers may be in need of reconsideration.

These three explanations are not mutually exclusive. We briefly consider some arguments for each of the three.

**Trade Power has not Increased.** Although it is popular to write of the demise of brands, the fastest growing outlets are the large discounters who depend on brands for their success. WalMart has prospered while Sears has languished. In the past, studies have reported that 60% of the respondents refused to switch brands (Peckham 1963; *Progressive Grocer* 1968). It appears, however, that brand loyalties are still very strong. Recent studies have shown that a large percentage of buyers will refuse to switch brands. In some categories, consumers are even reluctant to switch SKUs (sizes, flavors) within the assortment of a given brand. Emmelhainz, Stock, and Emmelhainz (1991) report that 27% of the people sampled *delayed* purchase rather than *switch* to another brand or even a different SKU of the same brand. Of the 27%, more than half went to another store rather than return.

"The battle of the brands" is part of the yin and yang of marketing. It is not a recent phenomenon. Even the private label market is well segmented: store brands, generic, distributor brands, and "in and out" brands. While they stay in hot pursuit of the innovations offered by national brand marketers, there is no evidence that the distance has closed.

The fact that *some* manufacturers' have weak brands with little or no leverage over retailers is not evidence that manufacturers, in general, have weaker positions than retailers or that the relative power of manufacturers is declining.

Retailers have not been able to translate Power into Profit. Power is a concept that must be grounded in some action or *potential* for action to give it meaning. What is it that retailers are alleged to have the power to accomplish? How might retailers use power over manufacturers? Here are some ways that occur to us:

(i) *Some retailers extract larger discounts and allowances from manufacturers* than other retailers are able to obtain. This may hurt smaller retailers, but overall manufacturer margins can still stay intact. Also the law prohibiting certain forms of price discrimination may be influential enough to limit the exercise of this power against other retailers. Government and academic interest in the practice of slotting allowances and the potential application of the Robinson-Patman Act and anti-trust laws to this area may have thwarted overt exercise of retailer power to demand excessive slotting allowances and "pay to stay" fees.

It may also be that manufacturers have managed to stay ahead of retailers with a combination of allowances, deals, and rebates that make every retailer feel as if he or she "got a better deal." The move by Procter & Gamble to cut the level of these deals (Karolefski 1992) is not only an exception, but has been opposed by many retailers.

The greatest expenditures on consumer price promotion are for manufacturer coupons. Coupons may sensitize consumers to price in the long-term, but the immediate effect is to have a subset of consumers looking for the item to be in stock at their local grocery store. Somewhat perversely, many coupons with relatively low rates of redemption might be the cheapest way for manufacturers to keep brands in stock that otherwise would be dropped completely. Since retailers often double or even triple the value of the manufacturer coupon, even low coupon rates can have the effect of reducing retailer margin and increasing temporary consumer pull. When all is said and done, might retailers be paying for some of this increase in pull?

(ii) *Retailers use national brands to sell store brands.* The most obvious and powerful techniques, "bait and switch" tactics and deliberate stock-outs of advertised specials, have been held by the courts to be illegal. Private labels enjoy better shelf position and sometimes more sales attention, but these techniques can backfire and waste resources if the products do not sell well. Although these practices certainly exist there is no evidence that the net effect is a profitable exercise of power for retailers. The

low margins or even negative margins required to price national brands as loss leaders give the national brands a powerful price lever over the private labels.

(iii) *The opposite of (ii) is to price national brands so high that private labels are a much better buy.* This can work for retailers when retail competition is not hard-fought. Indeed, it can be a problem for manufacturers who have given retailers an exclusive territory for the distribution of their products. Theoretical analyses have demonstrated the use of techniques such as quantity discounts to properly motivate the channel in such cases (e.g., Jeuland and Shugan 1983; Ingene and Parry 1991) provide a recent review of this literature and some extensions to the case of multiple retailers.

Increasing the price of national brands can backfire on the retailer when competition exists, however. If other retailers are nearby, the prices on the national brands are the ones that are most likely to be used for cross-store comparisons. We conclude that the possession and exercise of this kind of retail power is rare, especially in convenience goods markets.

(iv) *Drop the national brand from the assortment.* The ultimate threat of retailers against manufacturers is to simply not stock the product. A decision by retailers to drop a product from the assortment often signals the demise of the product or SKU. However, the power to deny the manufacturer access to the retailer's customers is effectively the same as denying the retailer's customers access to the manufacturer's products. That is unlikely to be a good strategy if brands have loyal customers. For multi-product retailers, the losses that can potentially result from such an action are not limited to the sales of one product/brand. Uncertainty about the strength of consumer loyalty to brands may lead retailers to retain products in their assortments that *could* be dropped with no appreciable loss in overall sales or profits.

The hope that scanner data might reduce this uncertainty about the real strength of consumer pull has not yet materialized. If and when it does, it offers the greatest potential for retailers to negotiate with manufacturers from a position of strength.

(v) *Convert data into information.* Although retailers apparently have access to large quantities of detailed scanner data only a few have the staff with abilities to harness information from it. Quite often the data are sold to market research organizations or others who process it and resell it to manufacturers before the retailer does anything with it. Moreover, some manufacturers, like Pepsico, equip their staff with computers for immediate information collection. Thus many retailers may have lost control over

their own data. If manufacturers have a more complete picture of the market for their product category, they may still have the advantage in negotiations. Recently, however, some retailers, like Ukrops, have developed frequency marketing programs, which, if successful, may provide the retailers with a useful tool in negotiations and a means of differentiating themselves (Quelch and Farris 1992).

(vi) *The power of large retailers.* Larger retailers are presumably those with the most power, but even here there are factors that offset their ability to exercise that power. Large retailers are large *because* they typically offer larger assortments, not just larger stores (clearly this statement does not apply to price clubs and other forms of limited assortment retail formats, but these are still exceptions and not the rule). The size of retail assortments offers consumers advantages in breadth and depth of assortments, but it brings its own retail management problems. Shelf-management programs are often designed to minimize out-of-stocks and retailers find it much easier to measure sales than the power of brands.

**Fierce Inter-Retailer Competition.** Ultimately, the inability of retailers to wield trade power against manufacturers may boil down to the existing fierce competition between retailers. In the absence of the ability to collude, punitive action by one retailer toward a manufacturer may simply create an opportunity for the punishing retailer's competition. As mentioned above, common "punishments" a retailer might consider are dropping a item from the assortment, increasing retail margins and prices, decreasing shelf space, and reducing retail advertising. Not only are these actions risky, but for an item that is in high demand, they could hurt the retailer *more* than the manufacturer *if other retailers take advantage of the situation*. In the present climate, retailers seem to be looking for manufacturers as potential partners in their war against other retailers.

#### CONCLUSION AND IMPLICATIONS FOR RESEARCH

The concept of power is well grounded in theory. Industrial organization researchers have studied market power in the Structure-Conduct-Performance paradigm for several years, starting with the treatise by Bain (1968). The social bases of power (French and Raven 1959) and their application to channels have also been extensively written about (see Stern and El-Ansary 1982 for an overview).

This paper has concerned itself with profit—a measure that is routinely used as an economic indicator and effect of market power in the industrial organization literature. It is certainly critical to the business world. The following quote from Robert Crandall, chairman of American Airlines, in an interview with *Time* magazine (May 4, 1992), says it in a nutshell:

"It's a pretty sorry commentary on power when a company loses \$40 million in 1990, when it loses \$240 million in 1991, when it is compelled to cancel \$8 billion worth of capital commitments such as new-airplane purchases, and when it formally gives up its long-term growth plan because of its inability to earn a return on its shareholders' investment. That's not really very much power, is it?"

We have not addressed the antecedents of retailer and manufacturer power, nor have we examined other possible effects of power. Our analysis of the COMPUSTAT data does not provide support for the relative increase in retail power, based on this important indicator. We believe a combination of the forces discussed above prevent the retailers from exercising power over manufacturers and translating it into profitability.

#### Promotional Allowances and Partnerships

The ability of retailers to obtain promotional allowances from manufacturers, even if it is growing, has *not* automatically led to increased retailer power and profits. Recent modeling work in channel coordination shows how quantity discounts (Jeuland and Shugan 1983; Ingene and Parry 1991) and two-part tariffs in general (Moorthy 1987) may be used by manufacturers to encourage retailers to set prices so as to maximize the *joint* profit of the retailer and the manufacturer. Perhaps promotional allowances should be viewed similarly. Many of the manufacturers' promotional programs are effective in giving retailers incentive to sell more and are mutually beneficial. Over the long-term, trade discounts may function as elements of partnerships that have not been fully appreciated. Even the "under-the-table" aspects of such deals may have some positive effects. If every retailer thinks their deal is the "best deal," then they may be even more likely to actively promote national brands.

#### Private Labels and National Brands

The inability of retailers to dominate manufacturer brands is intrinsic. Retailers may use the national brands to provide reference prices for their private labels, but those reference prices are only credible if the national brands are priced at competitive levels with other retailers. This provides a ceiling for prices and margins on private labels. Further, there is only very limited evidence of the ability of retailers to succeed without using manufacturer brand names. Private labels, by definition, have limited market coverage and, for most product lines, they may be impractical because of the consumer's desire for "one-stop shopping."

#### Repeat Purchase, Brand Loyalty, and Distribution

Even if there do exist certain manufacturer brand names that are weak and could be dropped without much loss to the retailer, those brands are often not easily identifiable by the retailer. One reason is the lack of expertise required to use the information provided by scanner data. Another is the fact that brand loyalty is hard to measure. Even sophisticated researchers often use simple repeat purchase data as indicators of brand loyalty when it may only measure breadth of availability or depth of assortment. For example, *Supermarket News* publishes a list of the percentage of category volume accounted for by the three largest brands in the category. The data used for this list do not account for distribution breadth and therefore cannot really measure the concept of brand loyalty.

Even the current academic literature often does not distinguish between simple repeat purchase and other measures of brand loyalty. Ehrenberg, Goodhardt, and Barwise (1990) write that large share brands have higher rates of repeat purchase. They offer several hypotheses for why smaller brands are in "double jeopardy" because penetration and repeat rates are positively correlated. None of these explanations refer to the higher breadth and depth of distribution held by high-share brands. See Farris, Olver, and deKuyver (1989) for a formal model and empirical evidence on the relationship between distribution and market share.

The neglect of distribution as an explanatory variable will, almost always, make existing market leaders look stronger than they are and may reduce retail willingness to take advantage of the categories where brand loyalty is weak.

#### Manufacturer Power versus Retailer Power

Perhaps retailers have been able to coerce better deals from manufacturers, but, for a variety of reasons, including those discussed above, they have not been able to exercise power and translate it into profit.

Or perhaps the emphasis on retailer power *versus* manufacturer power is misplaced and needs reconsideration. After all, retailers compete with other retailers for Profits far more directly than they do with manufacturers. They exist because they serve consumers by providing access to manufacturer products. If retailers could collude, or become large enough, then perhaps they could force manufacturers to provide concessions that would not be immediately competed away. This does not seem to have happened so far.

Given that situation, manufacturers who believe that appealing retailer



demands for larger discounts will win more than a temporary advantage would be hopelessly naive. Periodically, the base price may have to be adjusted to keep the system manageable. It will be interesting to see whether P&G's current change to a manufacturer's version of "everyday low prices" will be such an adjustment or a permanent change in policy.

In any case, it may be far better for retailers and manufacturers to view each other as partners toward a common goal, instead of as competitors vying for power and the maximum share of profit. There are definitely potential gains from expanding partnerships between manufacturers and retailers. The fact that some of these gains may be quickly imitated and competed away merely means that the advantages gained are temporary. They are still worth pursuing. The current emphasis on relationship management and frequency marketing appears to be well-justified. It is applicable to relationships at all levels, manufacturer-retailer, manufacturer-consumers, and retailer-consumers.

#### Conventional Wisdom versus Real Data

A final question we would like to address is, "Why does everyone know that trade power has been increasing"? Part of the conventional wisdom on trade power, we believe, is due to the attitude that the media have taken toward trade promotions. Even the trade's own *Progressive Grocer* has few kind words for trade promotions. The aspects of promotion that function as cooperative devices to allow manufacturers and retailers to "pull and push" together, to share the risks of introducing new products, and to reward effective merchandising of productive retailers have been neglected. Instead, the media have emphasized their shrinking share of the pie of marketing dollars. Marketers have long known that all dollars are not equal in terms of risk for the marketer. However, only recently is evidence being brought forward that the claims of damage to brand franchises have been greatly exaggerated. But again, this is from the manufacturers' point of view. And it appears that manufacturers have been able to take care of themselves quite well. Many retailers have not been as fortunate.

We have offered several hypotheses about why retailers have not been able to either achieve more power over manufacturers or convert power into profits. These hypotheses need to be investigated and it is in the collective interest of the retailers to undertake such a project. Academics might be useful partners in projects that have retailers cooperating with each other to learn more about why conventional wisdom on retail power and data on relative profits are not in agreement.

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