Chapter 1

SHIFTING OF POWER IN THE VALUE CHAIN

DURING THE LATTER half of the twentieth century, manufacturers had control of virtually all the marketing variables – such as price, promotions and presence on shelf – that resided within the retail environment. Brand-positioning strategies always included the consumer price point for the brand, which could then be counted on to appear in-store. A shortfall in distribution was seen as a tactical failure of the manufacturer's sales department to negotiate properly with their customers, a failure that could be easily rectified. Manufacturers cared little in whose shops their brands were bought as distribution was near universal. However, shifts in the balance of power between manufacturers and retailers have made this era obsolete. In June 2009, Progressive Grocer reported:

> Five years ago, manufacturers and retailers say they held equal shares of power in their partnerships, but today, manufacturers believe that retailers control almost two-thirds of the overall power and will extend their control to 71 percent five years from now, while retailers believe they currently control 60 percent of the overall power, and expect to control nearly two-thirds in five years' time.[1]

Manufacturers' sources of power from the past no longer work today. They used to be the sole provider of consumer knowledge, but they have been overtaken by retailers' own information, analysed by experts. For example, 28.5 million shoppers use Tesco's loyalty programmes.[2] In 1994 Tesco's hired dunnhumby to help them analyse their database, and within three months then Tesco Chairman Lord MacLaurin was moved to say, 'What scares me about this is that you know more about my customers after three months than I know after 30 years.'[3]

The conversation between retailers and manufacturers used to be dominated by the manufacturers' latest brand initiatives, but it is now dominated by retailers' latest supply chain initiatives. Retailers used to welcome brand innovation for the store traffic it would drive, now they often lead the way innovating under their store brands. Whereas the marketing budget used to be dominated by television advertising, now manufacturers pay more for retailer-related costs than consumer-related costs, spending anywhere between 10 and 25% of their annual revenues on trade deals, the second-biggest cost after manufacturing. Savings from reducing overheads and improving productivity have been generated to help offset the increase in trade spending, but many manufacturers are forced to spend less on consumer marketing to balance the books and remain profitable.

The outcome of these shifts is that manufacturers now have to consider retailers as a separate and dominant force in the market rather than compliant minions who could be relied upon to do their bidding. Thanks to the success of private label strategies (see Chapter 9), five of the top eight FMCG manufacturers in the world are actually retailers; giants such as Unilever and Coca-Cola are no longer even in the top ten, their global sales dwarfed by products under the names of Wal-Mart (now the world's largest FMCG manufacturer), Carrefour, Tesco, Aldi and Lidl. The branded manufacturers who have been tempted to produce private label are in no doubt where the power now lies. Indeed, it is rare for a branded company to even admit to being involved in private label; Weetabix are an example of one being open about their involvement.[4] Unilever, PepsiCo, Nestlé, Heinz, Playtex, Ralston Purina, Hershey, RJR Nabisco and McCain are less public about their move to the dark side.

But such shifts are neither a recent phenomenon nor an irreversible tide of history. To better understand how and why they have occurred we need to analyse the basis of retail power and examine how and why the balance of power in the value chain has shifted over time between manufacturers, distributors and retailers.

The emergence of branding as a value chain weapon

The history of trade is dominated by a struggle for the control of profits between producers, distributors and retailers. In the early days of the consumer economy, 'Mom and Pop' retailers were serviced by a complex network of middlemen who supplied mostly generic products sourced from a multitude of small-scale manufacturers. The anonymity of the products meant that manufacturer accountability for product quality was non-existent; shoppers neither knew nor really cared who made them. Retailers were the key players. Since they were the last stop in the supply chain, they were the only party the shopper could hold accountable as guarantor of the quality of goods purchased. As a counterbalance to retailers' necks being on the line with regards to quality, they had the ability to set prices, most often individually by shopper, which gave them a large degree of control on the transaction profits.

The more enlightened retailers realised they could increase turnover and hence profits by becoming an attractive destination. One way of achieving this was by gathering themselves under one roof, where their combined pulling power benefited all with the extra shoppers who thronged in their thousands. While the first recognisably modern shopping mall was the Southdale Shopping Centre, opened in Minneapolis in 1956, London's Royal Exchange, opened in 1568, fulfilled a very similar purpose. The invention of plate glass revolutionised retailing and was used to impressive effect in Paris' Palais Royal in the late eighteenth century, which spawned the nineteenth-century retail cathedrals that were to be found in London, Paris, Vienna and most large cities, attracting shoppers from far and wide.

The only way for distributors and manufacturers to end this relative dictatorship of the retailers on the size of the cake and their taking the biggest slice, was to take away their status as the 'agents of trust'. If a member of the supply chain was willing to take responsibility for product quality and to stake their reputation on it, they could then inform the consumer of the product's quality by placing some kind of mark on the product and (it was hoped) thus create a demand for their products as opposed to anyone else's – and the notion of brands evolved.

The first brand used on packaged goods was created almost 2000 years ago in Pompeii. The product, Vesuvinum, which combined Mt Vesuvius with the Latin word for wine, *vinum*, was a type of red wine – a category highly vulnerable to middlemen adulterating the quality with cheaper wine, water or worse. Rome's brick-makers also employed branding devices imprinted onto the bricks such that buyers in the city's brick market could recognise those bricks built to last. The United Kingdom's first brand trademark was registered in the late eighteenth century: the red triangle on bottles of Bass Pale Ale Beer, sold around the world.

It was essential that the branded manufacturer be able to package their product securely if their guarantee of quality was to be worth anything. Many packaging breakthroughs came about as a result of the demands of warfare. Foods became practical for mass manufacturing and branding with the invention of airtight food preservation in bottles by Nicholas Appert, in response to a prize offered by France's Napoleonic government as a means of feeding the Emperor's armies. The process for canning food was patented in 1810 but was slow to catch on, not least because the can opener was not invented for another 45 years. Similarly, the American Civil War gave a huge boost to embryonic food producers as the massive military orders forced them to scale up and reap huge economies of scale; prices consequently plummeted, making their products much more affordable when peace returned.

Many of the famous early consumer brands, such as Procter & Gamble's Ivory Soap in the United States, and Pear's Soap in Britain, came from the first manufacturers in the value chain to stake ownership of product quality. Their competition was not other brands – theirs was the first – it was the unbranded and largely untrustworthy generics.

Towards the end of the nineteenth century, after industry manufacturers grasped both the advantages of economics and technology to make branding synonymous with manufacturing, they were able to take the initiative ahead of distributors and retailers because of the scale economies of mass manufacturing combined with developments in packaging and transportation technologies. Together, these enabled the efficient production, transportation and retailing of individually sealed, branded packages, giving the manufacturer a route with which to build and own the relationship of trust with the consumer, and thus leverage with which to squeeze the distributor and have some influence over the shopkeeper.

The demise of the middleman

The middleman had had a good life in the nineteenth century. His monopoly on distribution, particularly in America, gave him substantial leverage over the manufacturer, who was a distant third in the battle for power. But, as middleman, he was vulnerable as he had no direct contact with the consumer and did not have the means to establish branding on the thousands of product lines in which he dealt.

When Procter & Gamble (P&G) were building their new soap brand, Ivory, their route to market was through the middleman. The early advertising was not just singing the praises of Ivory, but directing the shopper to make sure it was Ivory they were buying, thus hoping to generate a pressure on the retailer to ask for it specifically from the distributor.

Figure 1.1 'Examine Before You Buy'. *Century Magazine*, printed in 1886. *Source*: The National Museum.

This advertisement (Figure 1.1),[5] 'Examine Before You Buy', ran in the *Century Magazine* in 1886 – it indirectly encouraged grocers to stock Ivory Soap so that their customers would not be fooled into buying soap of a lesser quality.

The brand sold well with this approach, but P&G were still the poor relation in the value chain and had not been able to shake the grip of the retailer and the middleman on the profits. Despite increasing the investment in consumer advertising – up to $146 000 in 1886, Harley Procter reported that 'soap is in excellent demand but prices are low and profits small.'[6]

P&G began to experiment in 1913 with cutting out the middleman by selling and delivering to retailers direct, and by 1921 they adopted the approach nationwide. This was a big bet by P&G.

> Overnight, the sales force had to be expanded from 150 to 600, 125 more warehouses had to be acquired, 2000 contracts had to be written for deliveries by trucks and the accounting department had to be reorganised to handle 450 000 accounts.[7]

A boycott of P&G products by enraged distributors meant that the initiative was on a knife-edge for a while, but ultimately the gamble proved a success. Many other major goods manufacturers were able to follow P&G's lead to reap the benefits of greater profits of doing distribution for themselves, as well as the incremental benefits of having their own salespeople and merchandisers regularly visiting shops and building relationships with the shop owners. The original reason for P&G considering the initiative – greater predictability in orders and shipments – paled into insignificance with the benefits that influence over the point of sale were to bring.

A battle that had always been biased in favour of retailers because of their ability to influence the consumer and the middlemen for control of the route to market now began to swing inexorably in favour of the producer. This switch prompted innovation within the retail sector to fight back against the increasing power of the manufacturers.

An early appearance by private label

The Atlantic and Pacific Tea Company (A&P) opened their first store in 1859, founded on the principle of importing tea direct from China and Japan, thus cutting out the middleman and passing on the extra profits in the form of lower prices. This was an early example of the retailer realising that, having the key position of being in direct contact with the shopper, they had the potential to cut out one or even both of the other players in the value chain.

Within six years, they had expanded to 25 stores and decided that the same principle could be extended to other grocery items, which, for the most part, they executed by selling under a private label strategy. By 1930, A&P had become the largest retailer in the world, selling over a billion dollars' worth of goods a year through their 15700 stores.[8] While they did sell the most popular brands from manufacturers, slightly over half of the 300 products they sold were under the A&P private label – a ratio that a modern retailer would see today as a reasonable target to aim for. As part of their strategy, A&P had vertically integrated back into producing their private label products, thus also cutting out the manufacturer from the equation. They owned and operated coffee roasting plants, bakeries, food factories, cheese warehouses and salmon canneries, making them, at their peak, one of the world's largest FMCG manufacturers.

However, within the strength and success of the A&P retail model was the Trojan horse that would lead to it being eclipsed: manufacturer brands.

The rise of the brand retailer

The Piggly Wiggly chain pioneered the supermarket concept in terms of layout and self-service in the 1920s. But it wasn't until 1930, when Michael J. Cullen, an imaginative retailer then working for Kroger, came up with the idea to have a supermarket stocked with nothing but well-known manufacturers' brands sold at wafer-thin margins, an idea he enthusiastically proposed to Kroger's senior management:

> Can you imagine how the public would respond to a store of this kind? To think of it – a man selling 300 (branded) items at cost and another 200 at 5% above cost – nobody in the world ever did this before . . . People would break down the doors to get in, it would be a riot. I would have to call out the police and let the public in so many at a time.[9]

Kroger, who had a large private label business themselves, failed to see the potential of Cullen's idea of only stocking 1000 branded items and selling half of them at cost or marginally above: they thought him a lunatic. But Cullen realised that, as manufacturer brands were by then being advertised nationally via the powerful medium of radio, they would do all of the selling for him. So he left to develop the idea in his new grocery chain, the King Kullen Grocery Company. His prices on the most popular 500 lines substantially undercut other retailers, leaving A&P and Kroger, with all of their vast upstream costs associated with the private label, high and dry. The core of Cullen's idea has endured to this day: most major retailers today will have 400–500 lines they sell at or below cost.

Cullen was doubly fortunate in the timing of his idea: not only was radio advertising, the most powerful medium the world had yet seen, selling his stock for him, courtesy of the manufacturers' marketing budgets but rapidly increasing car penetration meant shoppers would gladly drive past their local A&P to reach his store and buy their favourite brands for less. He thus was able to overcome the two biggest challenges to succeeding in retail: attracting shoppers and the limitations of location. His formula was widely copied immediately. Independent store owners who could not hope to match the new grocery chains' prices and private label specialists who were not selling the advertised brands people wanted to buy both stood no chance and began a long, inexorable decline.

The triumph of branded manufacturers

Cullen had created a concept that was successful in horizontal competition with other retailers, but he had sown the seeds of retailers losing the vertical battle for profits to the manufacturer. He had unwittingly created the situation where power, consumer influence and consequently the bulk of the profits increasingly rested with the branded manufacturers. As manufacturers and retailers got accustomed to retailers earning uniformly thin margins, pricing control also fell into the hands of the brand owners via their list pricing, which translated into a very predictable on-shelf price.

Broadcast media for advertisers provided a perfect marriage of the economies associated with scale of production and communication – for the first time advertisers could talk to millions of customers at once, and fill the retailers' shelves with thousands of products to satisfy their needs. The brand message delivered repeatedly had a mesmerising effect on consumers, and on corporate bottom lines. By 1965, Coca-Cola were selling an annual average of 260 drinks per person in America, Camel dominated with 33% market share and Pampers were raking in $14.4 million. The manufacturers seemed unstoppable.

The dazzling power of mass media and the allure of branded products in self-service stores meant that there was no real need for someone in the value chain to engage the consumer and listen to their individual needs: everyone wanted to buy the big brands. This love affair with brands negated the one real source of advantage previously held by retailers: direct contact with their shoppers.

Retailers battle for the scraps

By the 1960s, retailers found themselves hopelessly outgunned by the branded manufacturers, who dictated the terms on what they should stock, how and where it should be displayed, at what price, how much they would be allowed to order and how much of the selling price they could keep as profit. As the branded manufacturers became financial goliaths with easy access to capital, retailers, especially in Europe, remained predominantly family businesses reluctant or unable to borrow substantial funds to fuel growth, thus widening further the scale mismatch between manufacturers and retailers. Rendered almost powerless, retailers disengaged from the vertical value chain battle for transaction profits and focused almost entirely on the horizontal battle with other retailers for market share, primarily in a race to be seen as the cheapest place to buy well-known brands.

Retailers thus embarked on a discounter strategy by developing large sites and maximising efficiency, building high volume with low prices and then negotiating appropriate discounts from manufacturers, investing in technology and reducing logistics costs. This strategy has worked across the globe, from Coles in Australia to Carrefour in Brazil and Loblaws in Canada, and across the sectors (e.g. food, electrical appliances, toys, pet care), but left most of the power and profits with the brand manufacturers.

The retailers' discounter strategy is most successful and appropriate when there is share to be taken from smaller, less efficient competitors. Sam Walton's US Wal-Mart chain grew dramatically through the 1970s and 1980s by being the epitome of this model. He placed many of his new stores in small towns where they could all but close down an entire Main Street of specialist shops.

This development of large, efficient retailers was not initially a threat to manufacturers. In fact, the efficient stores were better customers, shifting greater volumes per location and often increasing overall consumption. The better deals given by the manufacturers were justified by their savings servicing the high-volume discounter, compared to the costs of servicing a multitude of smaller, less tightly managed stores.

Discounters' profits came and still come from buying competitively while handling financial operations, logistics and property business more astutely than other retailers can. The high-volume, low-operating-cost model allowed them to offer lower prices and more choice, while maintaining acceptable service levels; their goal was to move a lot of product and make small percentage profits on high volumes, which improves efficiency and gives them the power to negotiate with manufacturers.

Manufacturers encouraged and favoured these 'model traders' with discounts, advantageous delivery arrangements and information technology link-ups. Most large manufacturers introduced systems where their computers were linked directly with the stock controlling computers in their clients' stores. Stock sold was reordered automatically as the goods moved out of the shop. Inventories could be minimised and administration reduced. The independents stood no chance. By the end of the 1950s, grocery chain stores had accounted for 50% of US food sales, which then rose steadily to 80% by the early 1990s; today, US grocery chain stores account for 89.6% of all food sales.[10] Elsewhere, Russia went from a situation in 1990 of virtually all trade being through small, grossly inefficient shops to 30% being through modern chain supermarkets within the space of 20 years.

The discounter strategy was unstoppable when there exist weaker competitors to crush, and the better discounters did very well because their sales were always increasing. Consumer demand for discount retailers was greater than supply, with towns begging retailers to open big-box stores in their vicinity. The competition between the discounters centred on being the first to develop new sites servicing these consumers who were waiting to benefit from the retail revolution.

The same situation exists today in the rapidly expanding emerging markets. The Russian retail food market, worth $239 billion in 2011, is growing at 13% a year, and yet the leading 10 retailers are growing at between 30 and 40% as they build upon their current modest 11% share. In India, organised chain retailers account for only 7% of the $435 billion market, a share forecast to rise to 20% by 2020.[11] The discounter model is unstoppable in fragmented, unorganised markets.

The end of the golden age for discounters

But all good things must come to an end. Once there is supermarket or hypermarket saturation, profitable growth via the discounter strategy becomes almost impossible. New sites have to be placed not in virgin discounter territory but in areas already served by other discounters. In saturated markets, such as Germany, this led to the emergence of the hard discounter as being a new way to compete.

Discounters have powerful differential advantages compared to traditional small stores, but as protection from each other all they have is location. As long as they stay apart, and the consumer isn't too mobile, they are differentiated by the cost involved in travelling to competitive stores. As the accessibility of transport increases, the advantage of location decreases. Even in countries like Australia, where a relatively small population is distributed across a continent, location is no longer a meaningful advantage. Coles and Woolworths compete toe to toe for the vast majority of grocery dollars spent in every major town and city. Retail competitors face each other with similar offerings of similar stores selling similar products at similar prices. Since there are no new supermarket shoppers, growth implies taking share away from competitive stores. The golden age of discount retailing, where developing a store in a well-chosen location was a formula for printing money, has come to an end.

The shift to selling orientation

The fastest route to maintain sales volume in such a competitive retail environment is a transition to selling, or 'hustle', strategies. *Hustling* means holding the basic product offering (store, range, service) constant while increasing the selling pressure. This involves price cutting, promotions, special 'discount' days, dump bins, checkout displays, piles of stock on the main floor with special offer etc., etc.

These techniques do not create greater value, except in impulse-buy categories such as soft drinks and confectionery, because most of them are easy to copy. The simplest way to increase sales volume is by dropping your prices, and the easiest way for competitors to recover their lost sales volume is by copying your strategy and dropping their prices even lower. Hence the price wars of the 1980s, which reduced retailers' margins to the bone. Hustle techniques almost always escalate beyond their break-even point: the value of the total market does not increase enough, if at all, to repay the combined investments of the participants.

Competing retailers thus hope to outdo each other in this situation by becoming more sophisticated. By analysing their promotions better than the competition does, they believe they can adjust their offers more efficiently to create greater profits. This is true for some competitors at some points, but it can't sustain the FMCG retail industry over time. As the techniques for analysing the effects and costs diffuse to the slower retailers, the outcome is similar layouts and promotions across the board.

At first glance the consumer would seem to benefit from such a competitive climate. However, the resulting oversupply of retail outlets is inefficient: supermarkets working at below-optimal capacity have higher fixed costs. They also have less money to invest in efficient technology. Selling strategies also tend to breed other, more complicated, inefficiencies.

Inefficiencies of the selling orientation

Selling strategies have detrimental effects on logistics. For example, they encourage forward buying. This practice is a result of regular and significant promotions, which are supposedly forced on manufacturers by the price-obsessed retailers. Once an expectation of promotions is established, retailers are motivated to buy as much of their turnover as possible during promotions, often to be resold later at regular prices, this being known as the *bull-whip effect*.

In simple terms, the trade start buying the product on discount to hold in stock for future sale at a higher margin rather than sell immediately. They make money by taking advantage of contradicting discounts and promotional schedules and then selling the product for a higher price at a later date. This is not uncommon. If a manufacturer offers promotional prices every other month, a retailer will forward buy five weeks' supply at the end of each promotional month. It is not unknown for a retailer to buy a year's supply ahead of a major price rise. At the extreme, forward buying necessitates special warehousing capacity, and the stop–go purchasing creates inventory inefficiencies both for the manufacturer and for the retailer: the average FMCG product spends more than 100 days in inventory supply. Freelance warehousing companies can generate a separate, parasitic business. These 'brokers' buy in bulk during promotions and sell to retailers out of promotion time.

Although forward buying is still a problem today, the opportunity to make money from it isn't as viable as it once was, because manufacturers have realised the costs to their business of such inefficiencies. In October 2011, John DeJesus, president of Foodmaster, explained that this is due to recent changes in the relationship between retailers and manufacturers:[12]

> We used to be able to take a [forward buying] position but manufacturers are getting smart now and saying no . . . If you sell everything on sale, no one will make any money, and if the manufacturer sells everything on deal, he won't make any money.

Retailers in a selling war sometimes ask manufacturers to create artificial differences in a product sold through competing chains (e.g. different-size packs) so that direct price comparison becomes more difficult. In the 1980s, Woolworths in the United Kingdom had major cost and thus selling price disadvantages compared to the 'selling' retailers who were pushing the same products at lower prices. They responded by demanding exclusive presentations of products from the main manufacturers. The strategy worked for a while as Woolworths had the size to order economically efficient quantities of such 'exclusives' in specific product categories where Woolworths were strong, while their competitors did not. But this approach added extra costs to the manufacturers, who soon began to regret agreeing to the idea. It also only masked Woolworths' cost inefficiencies rather than addressed them and no retailer can carry major cost inefficiencies forever, as

Woolworths demonstrated by finally closing the doors on its 800+ UK stores in January 2009.

Manufacturers and selling strategies

Selling strategies by retailers are not all bad news for manufacturers. Discounting big brands makes them exceptionally good value and, when advertised in flyers by retailers, reinforces the brand's advertising presence, and thus share of mind (mindspace) together with the retailer usually devoting more space to the promoted lines, increasing their shelfspace. Meanwhile, since these popular brands are so essential to selling-oriented retailers, the manufacturers can hold out for high margins in their negotiations.

In the long term it is a disadvantage to the manufacturer for big brands to be sold at a loss, because the retailer loses the incentive to merchandise the brands in favourable, high-traffic locations. The retailer features them in advertising to generate store traffic, but once the shopper is in the store the retailer has every incentive via prominent merchandising to sell that person a competitive brand, one on which they will make a profit. Manufacturers who cultivate high added-value, brand-building strategies are undermined when the retail trade promotes their brands with aggressive price promotion. This is because the exaggerated importance attached to price overwhelms the other attributes, encouraging brand switching and substitutability.

The gradual commoditisation of brands has been the outcome, a fact epitomised by specialist retailers such as Costco and Sam's Club, who might only stock one brand per category and are more than happy to switch that brand by the month if the right selling price/margin is on offer. Their customers do not mind which brand is stocked as the scale of the price discount trumps any brand preference.

Selling-oriented retailers can be tough to deal with because they are determined to secure better terms than their quasi-identical competitors. Their biggest fear during negotiations is that they did not squeeze manufacturers hard enough and left some margin on the table that may be given up to a more determined competitor, who will use it to undercut them on price.

However, during negotiations, retailers can sometimes focus on their competition so much that they are often less astute when buying (i.e. their competitive effort is directed horizontally rather than vertically). In these circumstances it is not unusual for a manufacturer to find that it is possible to raise the list price offered to all retailers without being criticised. The retailers are focusing on the discount from the given list price, as the list price is known to be common to all retailers. Thus, the objective for retailers in the negotiations is to win greater discounts, bonuses, promotions support, delays of payment and so on than other retailers, but not primarily to compete for profit with the manufacturer.

The winners of the selling phase and the quest for market orientation

Retailer selling strategies can dominate for a long time, but not indefinitely. Eventually, all the weaker competitors get squeezed out or bought up. In the late 1990s, the pace of consolidation accelerated in America when Kroger acquired Fred Meyer, the sixth-largest retailer, and Albertsons, the fourth-largest; they gained 4700 stores and became the country's second-biggest grocery retailer.[13] Consolidation was also happening in all other mature markets, especially in Europe, as Wal-Mart, Carrefour and Ahold were pushing out smaller chains, and Australia, which became dominated by two retailers, Coles and Woolworths.

The United States, while being by far the largest national grocery market, is still a series of regional markets, which accounts for the relatively low percentage of sales held by the top four grocery chains (Figure 1.2).

In the smaller European markets a greater degree of retail concentration has occurred.

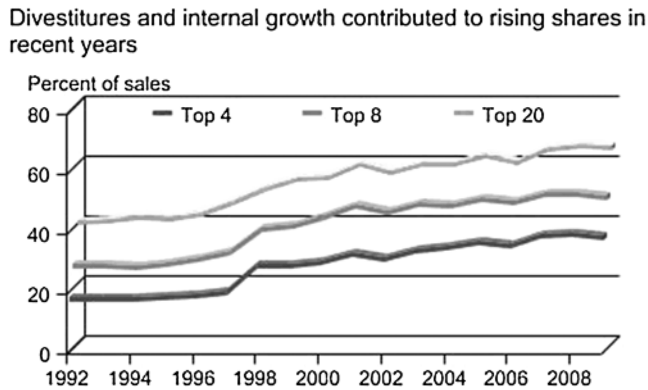

Figure 1.2 Top 4, 8 and 20 firms' share of US grocery store sales, 1992–2009.[14]
Note: Sales based on North American Industry Classification System (NAICS).
Source: USDA, ERS calculations using data from US Census Bureau, Monthly Retail Trade Survey, 1992–2009 and company annual reports.

While Sweden has the highest level of concentration among the top five grocery retailers, it is interesting to note that the concentration among those five is intense. The top three retailers, ICA, KF Group and D-Group, have 70% of the market share (35%, 20% and 15% respectively), leaving the fourth- and fifth-largest retailers, Hemkop and Bereghals, with the remaining 18%.

Once sufficient concentration and merging have taken place, the winners hope to be free to establish a more orderly form of competition between themselves, one where they create differential advantages for their stores, so that 'their shoppers' no longer see one store as substitutable for any other.

The information revolution

The biggest change that enabled the transfer of power from manufacturers to retailers was the introduction of UPC scanning and its universal adoption across FMCG. Described as the industry's Manhattan

Project,[15] UPCs and the supporting technologies took 20 years to develop before a pack of Wrigley's gum became the first product ever scanned in a grocery store on 26 June 1974.

Originally developed as a cost-saving efficiency tool, once all product categories adopted UPCs and computing became powerful and cheap enough to handle the unimaginable quantity of data, the benefits of retail information dwarfed the anticipated cost benefits from efficiencies. Real-time knowledge of sales at the item level dramatically illustrated the truism of knowledge equating to power, especially when the data could be measured at the individual shopper level through loyalty cards.

Perhaps the next information revolution in FMCG will be QR codes, short for 'quick response'. Whereas the utility of UPC codes is confined to retailers and manufacturers, QR codes can be used by end consumers, who scan them with their smart phones and can be directed to anything: a website, a promotional video, even an in-store coupon. This opens up a direct channel of communication with the consumer that can be used by both manufacturer and retailer.

The concept is in its infancy, but will undoubtedly have a huge effect on the retail market. For example, in 2011, AaramShop, an Indian online retail platform for small independent stores, added another dimension to what can be done with a QR code. Consumers can now scan the code on the product when they are running low, and it will be ordered and delivered within hours to their home, completely side-lining all the tools and techniques of competing manufacturers who would wish to get the consumer to brand switch. Tesco's Homeplus in South Korea also launched a campaign that engages shoppers to buy products using QR codes. Homeplus created virtual billboards of their store aisles in subway stations, allowing passengers to shop while they waited by scanning the products' QR codes – the groceries being delivered when they arrived home. The goal of the campaign was to help Homeplus compete with the number-one retailer, E-MART, without increasing their store numbers. Since the launch, their online sales have increased 130%, making them the top online retailer in

South Korea, and a close second offline.[16] For the 2011 Christmas season, J. C. Penney gave each shopper a 'Santa Tag' with every gift purchase containing an individualised QR code. The shopper could use the QR code to record a personalised gift message that could be heard by the recipient when they scanned the code after receiving it with the gift. The commercial uses of QR technology continue to evolve, illustrating that the battle between retailers and manufacturers is never static.

Key learnings

- The fact that **retailers are expanding their influence** and control over the value chain is not a new phenomenon; it is the **latest episode in a struggle for power and profits** that began over 200 years ago.
- The **shift of power to retailers is not an inevitable phenomenon**: technological changes and associated innovative ideas have been instrumental in moving power and profits in both directions around the value chain at different times.
- It is crucial to earn the consumer's trust ahead of horizontal competitors and ahead of other players in the value chain. It is not enough to be trustworthy, or even more trusted than one's direct competitors; **one must be the *most trustworthy* player in the value chain**. For example, Wal-Mart's strategy is that their commitment to EDLP (Every Day Low Prices) will make them the most trustworthy player because it confirms their honesty; in 2011, when a magnitude 9.0 earthquake devastated large areas of Japan, prices for items like bottled water stayed the same after Wal-Mart Seiyu outlets in the hit region reopened, while rival shops raised their rates.

- The days when manufacturers had a de facto advantage in winning consumer trust are over. All other things being equal, **the retailer will have an advantage** because of their direct contact with the shopper.
- The manufacturers' **old branding tools are now insufficient** to win the battle of the value chain. In order to develop new, more effective approaches, a much deeper understanding of the modern retailer is needed than has hitherto been the case.
- Brand **loyalty is not an absolute**; it can be bought for a price, a feature display or an optimal shelf location.

While much has changed over time in the relationship between retailers and manufacturers, one thing that has not changed is that they are very different kinds of businesses. They are structured differently, operate differently and are financed differently, all of which are at the root of much of the tension that exists between the two. In the next chapter, we will explore these differences and how a better understanding of them can lead to more productive retailer–manufacturer interactions and relationships.

Notes

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