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Oligopoly and the structural paradox of retail TNCs: an assessment of Carrefour and Wal-Mart in Japan

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Abstract

This research focuses on the case of international chains facing significant competition from domestic chains in advanced industrialized economies. In this article, I question the assumptions behind the perceived, simultaneous process of globalization and retail concentration by taking the cases of the world's two largest retailers, Wal-Mart and Carrefour, entering the Japanese market in the early 2000s. Both retail TNCs have so far failed to meet initial high expectations for their performance. I argue that there is a structural paradox inherent among retail TNCs, which is expressed as contradictory forces between standardization and localization. Empirical evidence is provided on how these forces complicate retail TNCs' front-end (store-front) and back-end (distribution) operations in the case of Japan. Emphasis is placed on the role of oligopoly in the retail sector and how its absence affects retail TNCs' operation in foreign markets.

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1. Introduction

A US-based study suggested that 'retailers that develop competency at home have a transferable advantage overseas' (Vida, et al., 2000, p. 52). Following this argument, global retailers such as Wal-Mart and Carrefour should have already conquered the world's consumer markets. Indeed, with their formidable capital, market power and knowledge in operational efficiency, achieving global oligopoly by those retail TNCs is too often assumed to be simply a matter of time, as competitors are driven out and consumers readjust their shopping practices. Yet, it cannot be farther away from the truth. The recent divestments by Carrefour from Japan and South Korea, and Wal-Mart from South Korea and Germany suggest accomplishing global oligopoly remains highly problematic, and particularly so in markets where highly competitive and modern domestic retailers are already present. In this context, it is difficult to conceive of a successful global oligopoly in the retail sector, both conceptually and empirically.

In this article, I analyze the challenges faced by retail TNCs by taking the case of foreign food retailers, Carrefour and Wal-Mart, in the Japanese market. I analyze both objectives and obstacles in enforcing global standardization in the front-end

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(retail formats, branding) and back-end (distribution) operations, as well as implementing necessary localization. I argue that a structural paradox works to prevent retail TNCs from accomplishing vertical and horizontal oligopoly simultaneously. The study demonstrates how forces of global convergence and institutional embeddedness manifest themselves in the retail sector.

2. Oligopoly and the structural paradox of retail TNCs

Researchers agree that theoretical investigation is urgently needed to better situate the significance of emerging retail TNCs as a process of globalization (Alexander and Myers, 2000; Coe, 2004; Wrigley et al., 2005). Various aspects of retail TNCs activities have been examined, including cross-border merger and acquisitions (Wrigley, 1997, 2000a, 2000b), mode of foreign market entry (Quinn, 1998; Palmer and Owens, 2006), foreign penetration of retail formats (Goldman, 2001, Goldman et al., 2002, Chang and Dawson, 2006) and supply network formation in emerging economies (Coe and Hess, 2005). The emergence of retail TNCs exemplify a simultaneous process of globalization and concentration, allegedly leading to global oligopoly. But as I will show in the subsequent sections, oligopoly is difficult to accomplish even by the largest and the most powerful of the retail TNCs.

Global oligopoly by retail TNCs is of particular concern for the public for several reasons. First, the view that the retail sector has traditionally been a local and relatively labor-intensive industry with low barriers to entry (i.e. mom-and-pop stores) persists even in many advanced industrialized economies where chain-stores dominated for decades. Second, the *quoditien* nature of the retail sector and the way consumers come in frequent and direct contact with TNCs on their essential daily activities of 'shopping' exacerbate the concern for decreased product variety and increased prices as outcomes of oligopoly. Furthermore, retail oligopoly can have an impact on wages in local labor markets (Basker, 2005; Goetz and Swaminathan, 2006). Finally, a condition of oligopsony, i.e. oligopoly of the demand side, has detrimental consequences on the bargaining power of manufacturers and food suppliers. By being powerful buyers in the market, oligopsonistic retailers can place downward pressures on prices of commodities that ripple vertically down the supply chain globally. Oligopsonistic retailers can theoretically become so powerful as to 'free-ride' on manufacturers (Waterman, 1996). Wal-Mart is already well-known as a global *buyer* and particularly for its success in globalizing sourcing activities for the US market. The question remains, however, as to whether Wal-Mart is equally successful in establishing itself as a global *seller*, which requires them to transfer store-front oligopoly across markets.

In understanding the emergence of retail TNCs, few empirical studies exists that demonstrates the dual process of vertical oligopsony (down the commodity chain) combined with horizontal (cross-national) oligopoly. In fact, research on oligopoly in economics by definition assumes intra-national (or, in the case of retail, intra-regional) scales, and therefore are almost exclusively conducted at the subnational level (Baumol et al., 1964; West and von Hohenbalken, 1984; Williams and Kim, 1990; Morelli, 1998; Chidmi et al., 2005). Among a few studies that stand as exceptions, Franko (2003) conducted an analysis of concentration ratio of global industries by focusing on 14 industrial sectors for the period 1960–2000. He showed that global oligopolistic conditions are rare and transitory in reality in the manufacturing sector. For retail

TNCs, achieving global oligopoly involves a particular structural paradox. The structural paradox in retail TNCs lies in the balance between their objective in enforcing standardization (at the supra-national level) and the need to conduct localization (at the sub-national level) to ensure customer acquisition. From the operational perspective, standardization, or a direct transfer of retail TNCs' strategic assets—formats, commodities, various retail practices and know-how (e.g. shelving and display, sales events, distribution practices), is an important and cost effective means to achieve scale economies. However, standardization can be hindered in many circumstances. For one, retail regulations and labor laws specific to the country may prevent implementing certain retail practices. As suggested by Bianchi and Ostale (2006), because retail firms are 'embedded in a general environment comprising several social actors that guide and shape the strategy, practices and formats of retail firms' (p. 141), retailers face a set of new institutional attributes that require them to reconsider 'retail norms'. In the case of Wal-Mart in Germany, due to stringent planning regulations and labor laws, the firm was unable to practice the same locational strategies and wage practices as in the United States (Aoyama and Schwarz, 2006; Christopherson, 2006).

In fact, success of foreign retailers in new markets has widely been understood to primarily hinge upon localization. Owing to the 'distribution-based' nature, retail TNCs are required to embed themselves in new markets and quickly understand local cultures of consumption to a far greater degree than 'production-based' firms (Currah and Wrigley, 2004). In identifying the types of embeddedness that are relevant for the operations of retail TNCs, Wrigley et al. (2005) used three types of embeddedness (societal, network, territorial) developed by Hess (2004). Furthermore, performances of retail TNCs in various markets have been attributed to 'business distance' (Dupuis and Prime, 1996) or 'psychic distance' (Evans et al., 2000). Wal-Mart's early lessons from Argentina and Brazil also suggested the importance of understanding cultural and market infrastructural differences (Friedland and Lee, 1997; Burt and Sparks, 2001).

However, implementing localization incurs cost of adaptation, which can multiply as retail TNCs attempt to identify market-specific issues and customize their operation accordingly. Furthermore, localization not only goes against the rationale of scale economies, it also challenges TNCs' corporate identity. There is a significance resistance within a corporation in implementing new strategies that counteract and challenge established corporate identity. This is particularly the case with retail TNCs, as their corporate identity is often closely associated with 'trade-mark' retail format and know-how in store-front and back-end operations. Manufacturing TNCs also perform a number of local adaptations, but often with cosmetic (e.g. design) changes, without having to challenge their own corporate identity bundled in technology or products. Thus, on the one hand, underlocalized retail TNCs face the possibility of sacrificing customer acceptance. On the other hand, overlocalized retail TNCs may lose their very *raison d'être* and, in addition, may fail to retain a niche of their own by adequately differentiating themselves from domestic competitors.

Consider a scenario in which standardization, efficiency and corporate identity combined translate into a retail TNC's strategic asset, established through its oligopolistic power in its home market. One of the most important strategic assets of retail TNCs is their know-how in achieving distribution efficiency by employing the factory-direct model. Yet, implementing standardization of distribution practices in a new market without oligopolistic power has proved to be a significant challenge for retail TNCs, even with their seemingly powerful incentives in having access to a variety of markets. Evidence shows that transfer of oligopoly is accomplished more easily in neighboring countries of retail TNCs' home markets as cultural proximity allows retail TNCs to experience a lower degree of the structural paradox between standardization and localization. Cultural proximity also facilitates oligopsony to cross borders as manufacturers and food suppliers find it easier to expand their markets across borders through alliances with retail TNCs. Finally, evidence also shows that retail TNCs tend to be more successful in developing country contexts (Coe and Hess, 2005). Conceivably, this is in part be due to the newness in retail formats introduced by retail TNCs, but is also in part because manufacturers and food suppliers perceive a bigger incentive in forging alliances with retail TNCs as they can offer price-competitive merchandise to international markets. In a mature market with strong competition from domestic retailers, the transfer of oligopoly and oligopsony is a formidable task for retail TNCs.

This study offers additional empirical evidence to the research on failure and divestment, long neglected in the study of retail TNCs (see, for example, Alexander and Quinn, 2002; Wrigley and Currah, 2003; Burt et al., 2003, 2005; Alexander et al., 2005). As the subsequent case studies of Wal-Mart and Carrefour in Japan show, initial expectations were high for these firms to successfully develop oligopolistic control. In the case of the Japanese market, however, the structural paradox of retail TNCs, coupled with the lack of oligopoly, prevented these firms from bringing about changes in the retail/distribution sector.

3. Foreign food retailers in Japan

Foreign grocery supermarket chains did not enter the Japanese market until 1995. In addition to its short history, the scope of operation has been generally limited. Aside from Wal-Mart's participation in the Seiyu chain, foreign TNCs with presence in Japan in the general merchandise store (GMS) category are mostly limited to small-scale operations, as exemplified by CostCo (USA, 1999, five stores) and Metro (Germany, joint venture with Marubeni Trading, 2002, three stores).[1] These foreign TNCs entered the Japanese market when GMS as a category of retailing was becoming rapidly obsolete. A recent article in Toyo Keizai, one of Japan's major weekly magazines, ran with a title 'GMS going Extinct' (Toyo Keizai, 2005).[2] Today, GMS faces an increasing competition from convenience stores and specialized supermarket chains of various types, such as 99-yen grocery stores (food items), 100-yen stores (non-food items), private-label discount stores (apparel) and electronics stores. Japan's retail floor area in 2005 was projected to grow 3% from the previous year, while its population has begun its decline (*Shukan Daiyamondo, 2005a*), thereby intensifying retail competition further.

1 Tesco's purchase of C Two-Network in 2003, a convenience store chain with 78 stores in the Tokyo area is one exception, yet because it is privately held, no information is available. Tesco can potentially use the chain as a springboard for building bigger outlets (Rowley, 2004).

2 For a brief history of foreign retailers in Japan since the 1960s and a discussion on the demise of the GMS, see (Aoyama and Schwarz, 2006).

Divestments of retail TNCs from Japan have not been uncommon. Past examples of divestments in the retail sector include Sports Authority (USA, 1996), OfficeMax (USA, 1997–1999), Footlocker (USA, 1997–2000), Warner Studio Store (USA, 1996–2000), OfficeMax (USA, 1997–2001) and JC Penney (USA, 1998–1999). In the supermarket category, Daily Farm, a successful Hong Kong retailer with over 2500 stores in Hong Kong, Taiwan, China, Singapore, Britain and Australia, set up a joint venture with Seiyu and opened four stores in Japan, but was forced into closure due to lackluster sales in 1998. Lack of competitiveness in fresh food items, unattractive store/shelf design and competition from domestic stores that reduced prices are cited as reasons for its failure (Sato, 2005).

Arriving in 2000 and 2002 respectively, Carrefour and Wal-Mart represented recent newcomers to the Japanese market. The two firms have been contrasted for their strategic orientation, marketing innovation and globalization (Colla and Dupuis, 2002), and likewise, their entry to Japan's market took different forms. However, they had a common strategy, which was to conquer the Japanese market by delivering lower prices. Carrefour divested after 5 years and Wal-Mart's has so far barely turned profits in Japan. In the following section, I briefly describe the circumstances of entry for these two firms, and analyze their strategies and failure.

3.1. Carrefour Japan

As the largest foreign investor in the retail category in Japan's recent past, Carrefour operated eight stores in Japan starting 2000. Carrefour's entry to Japan was significant as it was the first large global retailer to enter Japan by setting up new, greenfield sites for their stores, without relying on joint-venture. Although this strategy is in stark contrast to entry-via-acquisition strategy adopted by most foreign retailers, it is typical of Carrefour's overseas expansion to seek out partnerships with local firms only after it acquires market-specific knowledge, and only if it is deemed necessary. In addition to this mode of entry, Carrefour insisted that operational format in Japan was one that conformed to the corporate global standards. In hindsight, these strategies cost Carrefour dearly.

Carrefour's initial plan was to expand its operation in Japan to 13 stores by the end of 2003. When Carrefour's first store opened in a Tokyo suburb of Makuhari in December 2000, there was media frenzy, with 50,000 customers clamoring the store on the first 2 days of business (Larke, 2003). Domestic chains nearby, however, managed to undercut many of Carrefour's prices on the first day, effectively preventing consumers from associating Carrefour with price competitiveness. An article written shortly after its first anniversary already predicted its demise, describing the store's feel as a 'ghost-town' in an early afternoon of a weekday, in spite of the ongoing anniversary sale (Asano, 2002, p. 36). Fresh seafood section was reportedly full of advertisements but displayed few merchandise and among 40 cash registers, only four or five were open. In contrast, its main competitor, Ito Yokado's store within half-a-mile away was thriving with housewives from the neighborhood arriving on their bicycles, and in-season products such as spring vegetables, citrus fruits and fresh-cut bonito were prominently displayed at the store front. By March 2002, Carrefour planned to open just seven stores. Rumors of divestment began circulating among industry insiders, which eventually became persistent at least a year before its sell-out in March, 2005. It has been suggested that Carrefour planned to divest

Table 1. Top 5 food supermarkets in Japan: mid-year report, 2005

	Revenue (in million Yen)	Profits (in million Yen)
Aeon	922 185	9918
Ito-Yokado	743 036	15 018
Daiei	612 471	−3759
Uny	343 776	3139
Seiyu	329 373	−5245

Source: Mizuho Bank, 2006.

even earlier, but was delayed due to the inability to secure a buyer. In the end, all eight brand-new stores, three in the Tokyo region and five in the Osaka region, were sold to Aeon, Japan's largest GMS chain that operates Jusco stores. Carrefour's estimated loss incurred in Japan was reported to be between €200–300 million (*Nikkei Business, 2005*).

3.2. Seiyu (Wal-Mart Japan)

Wal-Mart entered the Japanese market through a minority stake of a domestic chain.[3] After briefly considering purchase of a small retail chain facing bankruptcy in 2001, Wal-Mart formed a strategic alliance with Sumitomo Trading and purchased a 34% share of Seiyu in 2002, with an option of increasing its share to 50.1% by the end of 2005 and to 66.7% by the end of 2007. Seiyu was established in 1963 as a domestic supermarket chain and belonged to Seibu conglomerate, which at its peak included in their assets suburban commuter railroads, a hotel chain, a department store chain, amusement parks and golf courses, as well as a professional baseball team and a stadium. Seiyu has consistently been among the top five supermarket chains in Japan in the past few decades. Partly due to Seiyu's established name recognition among Japanese consumers, Wal-Mart opted for adopting a strategy of keeping a low profile by making no visible changes in storefront design and product variety. It has been widely speculated that this strategy, as well as much delayed entry to the Japanese market, were direct outcomes of its own difficulties in the German market, as well as that of Carrefour's in Japan.[4] However, some blame Wal-Mart's risk-averse strategy in Japan in restricting the firm's success.

In fact, Seiyu's financial performance since Wal-Mart's involvement has been less than notable. At the time of Wal-Mart initial involvement, Seiyu was Japan's fourth largest retailer, now down to the fifth, lagging far behind its competitors. Seiyu's loss in 2005 was larger than Daiei, a company that had been under bankruptcy protection (Table 1). Seiyu momentarily yielded profits in mid-2004 for the first time since Wal-Mart's takeover, largely as a result of a major restructuring which included

3 Wal-Mart's first experimented with the Japanese market in 1994 through a partnership with a major domestic chain, Ito-Yokado. Ito-Yokado agreed to sell some of Wal-Mart's private brands, such as ketchup, snacks, and casual apparel, but within a year this partnership was dissolved as the revenue reached only half of the initial target (JCMRI, 2002).

4 For an analysis of Wal-Mart in Germany, see (Aoyama and Schwarz, 2006).

voluntary early retirement of 25% of its full-time employees and raising the share of part-time employees to 85%. However, the lay-off reportedly had negative impacts on the moral of Seiyu employees. In addition, introduction of new IT-based supply chain system placed significant burden on Seiyu's part-time employees.

In July 2005, Seiyu's CEO was forced to resign without completing his term, still a rare occurrence in Japan's corporate world. Seiyu's stock price, which doubled immediately after the announcement of Wal-Mart's involvement, plummeted to a third of its peak by mid-year 2005. One Seiyu executive was quoted as saying 'we were hopeful that Wal-Mart will save us. Changes in the way we do things and lay-offs put strains on us, but we had faith in Wal-Mart's management because we believed things will get better. Now I am at a loss.' (*Gekiryu,* 2005 April, 14).

The most recent reports from the Japanese media continue to show a pessimistic outlook for Seiyu. In 2006, Seiyu downgraded its revenue projection twice during the year, which led not only to widespread speculations about the negative impacts of Wal-Mart-initiated strategies on Seiyu, but also of its potential exit from Japan. Lee Scott, the CEO of Wal-Mart, went to the Japanese media to explicitly deny rumors of exit (*Nippon Keizai Shimbun,* 2006).

4. Front-end operations: resolving the paradox

What explains the problems of retail TNCs in Japan? As the subsequent section shows, Carrefour and Wal-Mart on the one hand insisted on standardization with a strong belief in their proven strategies seeking operational efficiency and offering customers low prices, and on the other hand, implemented localization, but in a way that eroded customer appeal. Here I focus on two major aspects of front-end operations, one on implementing operational efficiency and another on branding.

4.1. Operational efficiency: marketing on low prices

In the supermarket category, the most common strategy employed among foreign retailers is low price. As shown sebsequently, both heads of Wal-Mart and Carrefour insisted on the importance of price. McAllister (Wal-Mart) claimed 'the Japanese consumers have been asked to pay such high prices. After 12 years in recession, Japanese suppliers feel that they need to make their business more efficient'. Similarly, Jarry (Carrefour) commented 'I know that low-price-strategies of foreign retailers have been criticized as unsuitable for the Japanese market. I am convinced, however, that prices are extremely important for consumers in any country. The richest people in every country love discount stores. Every consumer prefers to be economical, rich or poor.' (*Shukan Daiyamondo,* 2005a, p. 103). Why, then, did Japanese consumers not flock to their stores?

First, Carrefour and Wal-Mart focused on the low-price strategy in spite of the relatively small share of low-income households in Japan and, a smaller market for low-end products (JCMRI, 2002). Inequality measures published by the United Nations (United Nations Development Programme, 2006) showed GINI coefficient to be 0.408 for the United States, 0.360 for United Kingdom, 0.283 for Germany and 0.249 for Japan. The ratio of income or consumption for the richest 10% to the poorest 10% was 15.9 in the United States, 13.8 for United Kingdom, 6.9 for Germany and 4.5 for Japan.

Second, it is well known that the attitude of the Japanese consumers toward price is particularly complex. Japanese consumers are far more willing to trade after-market service, convenience and proximity for a higher price (McCraw and O'Brien, 1986; Goldman, 1991; Hancock, 1993). As a result, Japanese consumers have been understood as relatively price-insensitive. This calls into question the effectiveness of Carrefour and Wal-Mart's fundamentally scale economy-driven approach in Japan.

Wal-Mart introduced its trade-mark 'every-day-low-price' (EDLP) strategy at its Seiyu stores with much fanfare, but without desired outcomes. The major factor behind EDLP's failure was not because Japanese consumers were non-responsive to prices, however. Rather, it was because Seiyu failed to consistently undercut competitors' prices. A typical Japanese grocery shopper, more often than not a woman in the household, closely examines several flyers of nearby supermarkets and identifies frequently changing sales items, and switches where to shop daily. They are trained to navigate through traditional high-low pricing models that employ limited-time sales and discounts to lure customers. Consumers find it more economical to continue with the practice of price comparisons and switching places to shop on the daily basis. Seiyu's now former CEO admitted failure of EDLP: 'I am embarrassed to admit that it is meaningless to sell an item 10% off every day at Seiyu, when competitors are selling the same item at 20% off at their weekly sales events.' (Ishibashi, 2004, p. 19). The failure of EDLP in Japan in fact points to the extremely price-sensitive nature of the Japanese consumers.

In an attempt to lure back customers, within 18 months of implementing EDLP Seiyu reverted back to the traditional high-low pricing model, using newspaper inserts to announce limited-time sales. Wal-Mart executives however, have not given up hopes for its prized strategy. McAllister (Wal-Mart) was quoted as saying 'I acknowledge the use of limited time sale is well accepted in Japan so I wouldn't call [EDLP] a mistake, but there must be a better alternative.' (*Shukan Diamondo,* 2005a, p. 103).

Third, Carrefour and Wal-Mart prioritized standardization over localization. Both companies insisted that their strategies for low-cost operations that worked elsewhere would eventually win customers in Japan. One example of low-cost operations is a display method known as 'statement merchandising', otherwise known as stack-them-up-and-sell-them-cheap strategy, where products are displayed without being taken out of corrugated boxes, and stacked up high in large quantities on shelves for visibility and shelf space maximization, but at the expense of store attractiveness. From an operational perspective, mass display of a single item introduces efficiency and reduces worker time by simplifying ordering and transactions. In practice, however, statement merchandising resulted in halving Seiyu's sales revenue out of end-cap (end of an aisle) areas. One-pound-size packages of Belgian chocolates occupying strategic display shelves in huge quantities for months did not yield anticipated revenue growth at Seiyu's stores, as Seiyu's clientele was mainly the middle-aged and elderly loyal customers, who were not impressed with low-cost display of bulk items. After the failure of statement merchandising, Seiyu reverted back to the costlier practice common in Japan's supermarkets, i.e. frequent changes of multiple products in end-cap display area. Yet, a recent customer satisfaction survey showed that Seiyu trailed far behind its competitors (Table 2).

The statement merchandising strategy also backfired for Carrefour in Japan. Carrefour reportedly conducted a huge 'promotion' of sewing machines, which only generated contempt among consumers and competitors alike, as the days of housewives

Table 2. Customer survey (percentage of respondents citing reasons for shopping)

	Quality (%)	Display (%)	Variety/inventory (%)
Ito-Yokado	16.9	12.6	36.1
Jusco (Aeon)	12.1	9.2	29.5
Aeon shopping center	7.9	3.9	34.4
Seiyu	5.4	3.3	17.0
Daiei	3.6	3.0	14.3

Source: Nikkei Research Report 2006-I.

sewing clothes for themselves and for their children were long gone in Japan. In observing another ‘promotion’ of electric appliances by Carrefour, industry magazine *Gekiryu* reported that the shelves were filled with ‘products you’ve never seen or heard of. Some were even discontinued merchandise or from dubious manufacturers from overseas’ (Asano, 2002, p. 37).

Furthermore, Carrefour reportedly insisted on transferring other proven strategies from their home markets. For example, its store layout was designed to direct customers to form a one-way traffic from entrance to exit, even though it was unfamiliar to Japanese consumers and caused confusions. Consumers also reacted with a shock to the sight of one-way revolving iron-cage gates at store entrances, common in stores and subway stations in France but seldom seen in Japan. Both were eliminated subsequently. Carrefour workers on roller-skates initially provided entertainment, until consumers realized that the stores were too large and therefore exhausting, and western-style shopping carts were too large, heavy and difficult to maneuver. Carrefour also insisted on maintaining the ‘hypermarket’ model, which hinged upon selling food and non-food items as well as various household appliances all on one floor for the convenience of the consumers. This however, necessitated acquisition of sizable land, which proved to be difficult and extremely costly.[5] Carrefour in the end decided to experiment with building multifloor stores and shopping malls at the expense of intra-mall competition. In sum, after being forced to adjust their shelf design, shopping carts, distribution system, and the floor area devoted to perishable items, Carrefour could not exercise effective differentiation from their domestic competitors in both appearance and prices.

Although ‘weekend-bulk purchase’ is increasing, Japanese consumers still shop almost daily for items such as vegetables, noodles and bread, and in small quantities (Mizuho Corporate Bank Industry Research Department, 2006). According to an executive in the food industry, ‘supermarkets substitute for refrigerators in Japan’ (Ishibashi, 2004, p. 21). Japan’s consumers today, particularly those that face acute shortage in storage space in their households, are known to practice ‘lean consumption’, i.e. consumers buy what they need when they need it and exactly the quantity they require. This directly goes against the bulk-purchase-at-low-prices model being

5 Data for Wal-Mart shows that, in comparison to its US counterparts, its operating cost is estimated to be 5-fold in Japan in terms of property cost, 3-fold in terms of operating cost per-store and 2-fold in terms of constructing new buildings (JCMRI, 2002).

promoted by Carrefour and Wal-Mart. Because Japan's consumers shop frequently, they want the experience to be as varied and interesting as possible.[6] Thus, in a country where population is shrinking, low prices alone can no longer effectively increase one's customer base as the consumers are looking for the experience, entertainment and discovery of particularly savory food, and expect retailer input in enriching their lifestyles.[7]

Domestic competitors employed strategies that went directly against the retail TNC's low cost approach. Otherwise known as 'cross-merchandising', this strategy involved selling a great variety of food and non-food merchandise under one theme, and bundling multiple items at their well-publicized, special events to increase visibility and customer appeal. The Japanese consumers prefer to shop in an environment of rapidly changing merchandise with great variety, and in a vigorous, thriving atmosphere, simulating wholesale markets filled with sellers shouting low prices and special deals. They also exhibit particular sensitivity to seasonal changes in food items, awareness to gift giving seasons, love new products and consider freshness as extremely important. Ito Yokado's Makuhari store adjacent to Carrefour's first store conducted theme-based sale by scrutinizing demographic data since 1999. A limited time 'strawberry fair' in the spring included not only the fruit, but also T-shirts and stationary. In addition, Ito Yokado implemented a variety of labor-intensive strategies to increase customer appeal. For example, merchandise in its fresh seafood section changed three times a day; whole fish from nearby ocean in the morning, sliced into sashimi in the afternoon; and marinated and grilled fish in the evening. For special events, displays were converted overnight after store hours. However, all these strategies were costly—and went against the low-cost, scale-driven approaches of foreign retailers. These strategies were practiced by Seiyu before the take-over, but were subsequently eliminated as they created operational complexities for the distribution data structure developed and used by Wal-Mart.

4.2. Branding: localization or overlocalization?

Inflexible corporate strategies such as those mentioned in the previous section are not the sole cause behind the failure of localization. Retail TNCs face the issue of 'branding' in foreign markets, a particularly complex issue in the Japanese market (Jacobson, 2002). The Japanese consumer has been referred to as the 'most difficult consumer to strategize, as they require high quality on everything, and are knowledgeable about products, service, quality and prices from around the world. . . . They are also extremely

6 Granted, the importance of entertainment in shopping is not an attribute unique to Japanese consumers. Fishman (2006, 19) made a similar observation in his book entitled *The Wal-Mart Effect*. 'My wife went shopping once at Wal-Mart in the last year, and vowed not to return anytime soon. My wife doesn't go to stores to buy things, she goes to shop. . . . to explore, to be surprised and persuaded. She doesn't want to work while she's shopping. She finds Wal-Mart harsh, disorienting, exhausting, frustrating. For her, the prices aren't worth the cost.'

7 Interestingly, the Japanese consumers adapted their consumption strategy when shopping at CostCo's stores in Japan. Because they allow two 'friends' per member, a group of three women are often seen shopping together at CostCo, who subsequently split bulk-items amongst them and perhaps a few additional friends and relatives. CostCo has in fact become a phenomenon in Japan, with the emergence of 'CostCo tourism' and numerous 'CostCo blogs' appearing on the internet. CostCo's case suggests that Japanese consumers increasingly seek leisure and entertainment even for grocery shopping activities. It also suggests the consumers' ability to interpret, adapt and appropriate a particular store format to suit their own lifestyles on the other.

brand-conscious, and demand brand products even on groceries' (*Nikkei Business*, 2005, p. 130).

Branding was particularly problematic for Carrefour, which needed to resolve the discrepancy between consumer expectation and merchandise offerings (Nippon Kogyo Ginko, 2002; Sato, 2004). Japanese consumers' previous experience with French retailers was largely shaped by luxury boutiques such as Chanel, Louis Vitton and Hermes. Partly as a result of this experience, consumers expected Carrefour to offer a distinct experience of shopping at a foreign, and in particular, a 'French' store. A survey conducted by a local bank prior to Carrefour's first store opening showed that consumers had hoped to find designer French apparel, accessories and cosmetics products at competitive prices. The director of research of the bank which conducted the survey was quoted as saying 'for Japanese consumers, the country of France is in itself a brand' (Asano, 2002, p. 37). Upon entering a Carrefour store, however, the Japanese consumers found a flavor of France only in a select few corners, in cheese, wine and fresh rotisserie sections. Marketing the country of its origin was decidedly not part of Carrefour's global strategy. Rather, Carrefour's objective was to establish itself as an everyday food supermarket for Japanese consumers offering low-prices. In sum, over-localization implemented by Carrefour led to the mismatch between consumer expectations and retail strategies, which in turn resulted in disappointing revenues (Ishibashi, 2004).

Subsequently, Carrefour was forced to alter its localization strategies. 'Japan is the only place where we considered France as part of our marketing strategies', admitted an executive at Carrefour (*Gekiryu*, 2003, p. 23). Carrefour added 150 private brand food items to the existing 120 sold in Japan, introduced prepared food in 'French home-style' and increased French imports from 240 in 2003 to 500 items in 2005. Carrefour also organized special events that emphasized its country of origin, including French wine-tasting events and sweepstakes to win a trip to Paris, and conducted limited-quantity sale of luxury accessories from Louis Vitton and Hermes. In one store they even developed an area called 'La Maison', and stocked with imported dining sets, fancy wine glasses and other kitchen accessories from France. Carrefour also began developing various services to enhance customer appeal, including staffing its cosmetic counters to provide better service accustomed by the Japanese consumers, showcasing freshly caught fish delivered directly from a well-known fishing port in Northern Japan, and opening in-store bread shops with freshly baked breads (found in most Japanese supermarkets) accompanied by a café next door. Carrefour even introduced gift items to accommodate year-end gift-giving practices and offering specialty food items for the Japanese New Year. These initiatives were well received by Japanese customers, even though they went directly against Carrefour's low-cost approach and the strategy for standardization.

Wal-Mart in Japan experienced a reverse problem that arises from branding. While Japanese consumers at Seiyu stores had not noticed price changes in food items, they recognized lower prices, up to 26% decline in a single quarter, in Seiyu's apparel section since Wal-Mart's take-over. These lower prices did not translate into revenue growth, however. Instead, it led to the perception that Seiyu products were cheap which, to most customers, also meant low-quality (Ishibashi, 2004; *Asahi Shimbun* 2005; *Shukan Daiyamondo*, 2005a). Customers complained about discontinued items, and lack of high-priced items made the store unappealing. The GMS format had been successful in the previous decades in Japan, as they offered lower priced apparel in comparison to department stores and boutiques. The format succeeded by luring customers into the store through their low-margin grocery section but generating revenues from high-margin apparel section. Wal-Mart's low-cost, low-quality approach was widely blamed for its most recent poor performance as it ruined Seiyu's highly profitable apparel section. Others argue that Wal-Mart represents non-urban, down-to-earth, basic American values and life-styles, which were not well suited for the Japanese market (Shimada, 2003). As a result of disappointing performance, Seiyu's executives, who had been consistently overruled by Wal-Mart executives since the take-over, were finally beginning to speak up. A Seiyu executive was quoted as follows: 'in the past two years, Wal-Mart believed that their strategy is absolute. Seiyu was carefully watching Wal-Mart. But what Seiyu should have been doing is to carefully watch its customers instead' (Ishibashi, 2004, p. 19).

5. Back-end operations: transferring the strategic asset without oligopoly

One of the most significant and persistent challenges faced by foreign retailers in Japan is in the distribution practices. Without achieving control over distribution, retailers are unable to achieve vertical oligopsony and exert effective pressures on manufacturers/suppliers on prices. Both Wal-Mart and Carrefour had difficulties convincing manufacturers to adopt a factory-direct model, in part due to the lack of established track-record in Japan, and in part due to the lack of oligopolistic position they enjoy in their home markets. Without being able to control and reduce prices as planned, retail TNCs were unable to offer competitive prices. The failure in implementing distribution revolution in Japan therefore turned powerful oligopolists with global reach and strategic assets into newcomers disadvantaged by insufficient local market knowledge. In the subsequent section, I examine organizational characteristics of Japan's distribution system and analyze issues encountered by Carrefour and Wal-Mart.

5.1. Japan's distribution system

Japan's distribution system is allegedly so complex that it is supposedly incomprehensible by outsiders. The US government declared it a non-tariff barrier and a structural impediment for US–Japan trade in the mid-1990s. After Carrefour's divestment, Philippe Jarry (Carrefour Asia) was quoted as saying 'we succeeded in many other countries by employing the factory-direct method—China, South Korea,[8] Indonesia—but in Japan, there are first-tier wholesalers, and then there are second-tier wholesalers . . . multiple layers of wholesalers each taking a bite off the margin. It is fair to say that this is a unique practice of the Japanese market, and it is true that we were very troubled by the complexity of it all. Wholesalers exist in France too, but not to this degree. In France, wholesalers are used only occasionally, and only for non-food items' (*Nikkei Business*, 2005, p. 130).

8 Subsequent to this interview, in April 2006, Carrefour divested out of South Korea. This suggests that an allegedly successful transfer of the factory-direct model alone does not guarantee overall success.

Table 3. Commonly observed practices in the distribution sector by region

Practice	Description	Europe	USA	Japan
Rebate: Time restricted	Rebates provided for the sales record of a particular period (bi-annual, annual, etc.)	Yes	No	Yes
Rebate: Price adjustment	Rebates provided for either a particular product or a particular retailer	No	No	Yes
New account bonus	Incentive for opening an account with a new client	Yes	No	No
New product discount	Discount for new product introduction	Yes	Yes	Yes
Circular development support	Incentive for advertising specific items	Yes	Yes	Yes
Special promotion support	Incentives for a special promotion including special sale, special end-cap displays and various marketing campaigns	Yes	Yes	Yes
New store opening support	Incentive or discount offered at new store opening, or new item	Yes	No	Yes
Price identification discount	Discount offered to display item prices on shelf	Yes	No	Yes
Advertisement support	Incentive for general advertising	Yes	Yes	Yes
Store renovation support	Assistance requested by the retailer to support store renovation	Yes	No	No
Center fee	Usage fee for delivery to retailer-owned distribution centers	No	No	Yes

Source: translated and adapted from Takahashi, 2001, p. 11.

Japan's distribution system includes some unique features, as do those in other countries. Takahashi's (2001) analysis for Japan, USA and Europe shows among 11 types of rebates and incentives used in distribution, four were commonly observed in all three regions, two were practiced only in Europe but neither in the US nor Japan, and two were observed only in Japan (Table 3). It is noteworthy that in the United States only four out of 11 practices analyzed were observed, while nine out of 11 were observed in both Europe and Japan, suggesting that European and Japanese distribution practices tend to include more features than US counterparts.

Power asymmetry between manufacturers and retailers does complicate Japan's distribution sector further. Traditionally, Japan's manufacturers dictated the behavior of wholesalers, which in turn governed, sustained and at times sanctioned behavior of retailers (Goldman, 1992). Manufacturers determined final store-front prices through Manufacturer's Suggested Retail Prices (MSRP) (Tsukiizumi, 2004). Retailers were often protected from financial risks by wholesalers and manufacturers through a number of distribution practices (such as rebates), and manufacturers and wholesalers controlled prices by enforcing districting and exclusive dealerships (Tamura, 1986). Because wholesalers sanctioned those who broke exclusive distribution agreements, Japan's retailers faced an additional disincentive in generating a new retail category, particularly those that require diversification of distribution networks to offer multiple categories of commodities. As a result, closed-network distribution dominated the Japanese retail sector and provided significant barriers to retail innovation and new entry.

An analysis by Bradford (2005) showed that margins earned by Japan's distribution sector are among the highest in the advanced industrialized economies. Yet, wholesalers do not disappear in Japan because logistics expertise has accumulated almost exclusively in the hands of wholesales.[9] Wholesalers in Japan provide expertise in coordinating both the flows of money and the flow of merchandise, and provide frequent and small-volume delivery 365 days per year with extreme precision and low incidences of errors or delays. In the case of Japan where the retail sector remains relatively fragmented and the concentration ratio is low, wholesalers function effectively as mediators between numerous manufacturers and retailers, often managing incompatible information databases and handling various complex distribution requirements.

Wholesaler expertise also includes reverse logistics and other value-added services. For example, wholesalers conduct such labor-intensive tasks as receiving an order for a discontinued item number from a retailer, identifying a new replacement item from the manufacturer and arranging a courier service for immediate delivery. Retailers in Japan are also accustomed to 'service in excess', with wholesalers conducting tasks that are generally in the retailers' realm, such as shelving and display arrangements at stores. Wholesalers arrange dispatching of additional workers to assist new store openings to handle shelving, display work, as well as directing traffic in retailers' parking lots. These services provided by wholesalers have slim margins and neither manufacturers nor retailers are willing to take over these services. Because Japan's wholesalers hold extensive logistics expertise and are deeply involved in the day-to-day operations of the retail sector, they have so far successfully defied disintermediation.

5.2. Restructuring distribution without oligopolistic power

One of Wal-Mart's major impacts in the retail sector is 'destabilization', a strategy to overwhelm other competitors through the combined effects of price-cutting and the economies of scale, and to induce catalytic changes in the retail sector (Burt and Sparks, 2001). Because the scale of investment has so far been small in Japan, the impacts of retail TNCs on distribution practices has been small. Most manufacturers refused to develop the factory-direct scheme with Carrefour and Wal-Mart at the expense of potentially alienating their long-term wholesalers and much larger domestic customers such as Aeon's Jusco or Ito Yokado.[10] In fact, attempts to restructure distribution without oligopolistic power proved to be perhaps the biggest

9 Recently, some Japanese retailers have begun internalizing some logistics functions, typically by establishing distribution centers and handling logistics. These retailers typically charge manufacturers 'center-fees' to compensate for the additional logistics costs.

10 Carrefour claimed that they used factory-direct model for 15% of groceries, 75% factory direct for household items at their first store in Makuhari, Japan. (Imai, 2004). This contradicts evidence provided in another report, which claimed that Carrefour's Makuhari store dealt with several wholesalers, with 99.9% of the processed food items supplied by one wholesaler, Asahi Shokuhin (*Gekiryu*, 2001, March). The household items were supplied by another wholesaler, Chuo Bussan. Both wholesalers were reportedly chosen by Carrefour for their efforts in increasing transparency by itemizing each category of work in their billing process and using information technology.

miscalculation, on the part of retail TNCs. One of the first successfully implemented factory-direct model in the US, the partnership between Wal-Mart and Proctor & Gamble in 1987, suggests that the condition of 'bilateral oligopoly', a condition that oligopoly exists both in the retail and the manufacturing sector, may be an important condition for its successful implementation. Incentives for establishing factory-direct model are high between large retailers and large manufacturers, both with significant market share. Without bilateral oligopoly, manufacturers need to maintain relationships with wholesalers to cater to the fragmented retail sector.

To achieve sufficient scale within a national market, Carrefour's typical strategy in a new market is to build a dozen or two stores in suburbs of a major metropolitan area, before locating new stores to small towns in the periphery. As Jarry commented in a magazine interview, 'Carrefour's goal is to be one of the top 3 retailers in any market. The chance of success in our business is only available to the top 2 or 3 companies. We know from experience that it is difficult to succeed in the long-run by being No 4. or 5' (*Nikkei Business*, 2005, p. 129). The significant difficulties in land acquisition in Japan contributed to derailing Carrefour's initial plans for rapid expansion. Jarry claimed that Carrefour could have continued its operation in Japan if they had successfully launched 15–20 stores in the first 5 years. Furthermore, Carrefour's split approach between Tokyo and Osaka metropolitan areas (three in Tokyo and five in Osaka) prevented them to develop a sizable share in one regional market. Even for Seiyu, with their 400 stores nationwide, negotiating the factory-direct model with suppliers proved to be a challenge. During one negotiation, a representative from a powerful manufacturer reportedly asked Seiyu, 'What's the advantage for us to give you a special deal, when Seiyu's volume is declining every year?' (*Shukan Daiyamondo*, 2005b).

More importantly, the potential global market access via retail TNCs did not serve as an adequate incentive for Japan's manufacturers/food suppliers. One Japanese supplier commented that while Carrefour 'maybe No. 2 in the world, it is less than a regional supermarket in Japan' in terms of the negotiation power it commands with their suppliers (Ishibashi, 2004, p. 23). Manufacturers in mature economies are either price-uncompetitive in many emerging markets or they already have their own global distribution networks. Food suppliers either handle perishable items or market-specific products with limited demand outside Japan, thereby making retail TNCs' overseas networks irrelevant. To wholesalers, foreign retailers' global reach functioned neither as an incentive nor a threat, as their main line of business is to cater to Japan's supermarkets. This suggests that while retail TNCs can have global impacts on prices by being a global buyer via establishing vertical oligopsony in one market, such control does not necessarily transfer horizontally to another market.

It is neither Carrefour nor Wal-Mart, but Aeon, Japan's largest GMS firm, which is well positioned to execute destabilization in Japan's distribution sector. Since 2000, Aeon quickly became Japan's largest retailer in February 2004 surpassing the former giant Ito Yokado through an aggressive M&A strategy. Between 1998 and 2004, Aeon grew twice the size in floor space as it merged with various chains, including Yaohan Japan, Kasumi, Maikaru and Inageya. Aeon began investing in logistics, first by taking part in the global e-commerce market WorldWide Retail Exchange (WWRE), which promotes reverse auctions for sourcing and logistics, and second by building its own distribution centers with 40 suppliers participating in the new logistics scheme. Yet, even Aeon experienced difficulties in convincing manufacturers; in 2001 for example, Aeon approached Ajinomoto General Foods, one of Japan's largest food manufacturer, to develop a factory-direct model. Ajinomoto rejected this proposal, however, which led Aeon to refuse carrying some Ajinomoto products in their stores.

6. Conclusions

The cases of Carrefour and Wal-Mart in Japan show that the challenges faced by retail TNCs are forces and counter-forces of standardization and localization intersecting in a complex manner. Retail TNCs face such a structural paradox because the *raison d'etre* of retailers is based on how-they-sell-what-they-sell, yet a fundamental change necessitated by local adaptation goes against their trade-mark corporate strategies. The case of Carrefour is particularly interesting because it suggests that, while on the one hand, localization led to insufficient differentiation and clearly worked against consumer expectation, and yet on the other hand, localization sacrificed operational efficiency, thereby forcing Carrefour to adopt new practices of high-cost retailing without success. In the case of Wal-Mart, the challenge was to encourage standardization by introducing their trade-mark strategies to already well-localized stores. Wal-Mart overestimated the strength of Seiyu's scale, while underestimating the chain's weaknesses. Wal-Mart's risk-averse strategy allegedly prevented much-needed up-front investment on buildings and physical infrastructure to improve on customer appeal in Japan (Isomi, 2004). In both cases, retail TNCs executed strategies with a belief that appeal to prices was universal and prices alone would win customers in Japan. Thus, localization and differentiation are often at odds with each other. Also, an absence of a retail format/model may not suggest poor retail innovation, but rather may turn out to be an indicator of its ineffectiveness in a particular market.

This study also emphasized the importance of inter-dependence in front-end and back-end strategies and operations in achieving success in foreign markets. Carrefour's and Wal-Mart's initial plans of introducing and implementing low-cost retailing to out-compete high-cost, high-maintenance retailing practiced by domestic competitors were compromised in part by its inability to draw customers, and in part by the lack of sufficient price-differentiation, which was impossible without successful restructuring of the distribution practices. In the end, retail TNCs failed to deliver on their trade-mark strategy of low-cost retailing. Furthermore, both firms over-estimated the power of their 'global' networks on local suppliers. They believed that their market share elsewhere would function as a credible pressure and a catalyst to introduce new practices in Japan's distribution sector. Global scale economies, however, meant little to most suppliers because most merchandises cater to specific demand of the domestic market.

Thus, there is a considerable challenge in transferring strategic assets developed in their home markets to cross borders. Significant barriers exist for retail TNCs to transfer oligopoly across markets, even if retail TNCs may have an established oligopsony. Even though retail TNCs may have achieved global vertical oligopsony to some degree (by becoming a global *buyer* in a particular market), retail TNCs are nowhere near accomplishing *horizontal* oligopoly (i.e. global *seller*). In fact, firms that are often being tauted as 'global' are no more than the firms on the international list of the 'largest' firms. Retail TNCs in particular are more accurately described as either multidomestic or regional (Rugman, 2005). In fact, only a handful of retailers operate in more than 20 countries (Futagami, 2003; Coe, 2004; Coe and Hess, 2005).

Geographically, contemporary globalization involves varying scales at different levels of market engagements—and in this particular case, not only were front-end operations intensely local, but so were the back-end operations. Localization of both front- and back-ends, however, may sustain a highly localized nature of retailing, vis-à-vis trends toward standardization across borders. Because retailing directly engages day-to-day habits such as food choices and the diet, it is difficult to conceive of standardization to become the norm in the near future.

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