

# Power Struggle in the Distribution Channel: Case of the French Supermarkets

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## Abstract

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An area of emerging research is managing a multi-product and multi-echelon supply chain. This paper will begin an investigation of one component of this: the power struggle in the distribution channel. Shift in the balance of power in the distribution channel from the manufacturer to the retailer has precipitated a power struggle. This struggle has prompted manufacturers to rethink their distribution strategy in the channel. The case of the French Supermarket chain is presented. A brief history of the French Supermarket chain and the consequences of their advent are discussed. A set of action alternatives are listed and described for the manufacturer/suppliers in the industry to help them gain some control in this power struggle. Plans for future research include the expansion of the study with quantifying methodology and inclusion of US and South American distribution channels' observations for comparison and contrasting to the French model.

## Keywords

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Distribution channel, retailers, manufacturers, French supermarkets

# Introduction

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Setting up sales branches at remote locations has long been practiced by manufacturers. The primary reason is to be closer to customers and respond to their target market quickly. Such practice has gained tremendous momentum in recent years for several reasons. First, it becomes popular in response to the observed power shift in the distribution channel. Building regional distribution centers has helped retailer giants, such as Wal-Mart in the United States to improve its performance significantly and contributed to the increasingly growing power of such retailers. To compete with retailer giant, manufacturers have found that building a regional warehouse may provide a solution for their survival and future growth in the power struggle in the channel relationships. Second, sales branches and regional warehouses have become a necessity as firms rapidly expand internationally, especially when they are unable to locate a local distributor in a foreign market. Regional warehouses not only contribute to the efficiency in the physical distribution of products, but also enhance the ability to adapt to local market condition, especially to the unexpected demand variations. Finally, the emergence of e-commerce has dramatically changed the landscape of retailing and the system of channel distribution. It has opened the door for direct selling for manufacturers and it has also created powerful retail giants such as Amazon.com. Never before has it been so apparent that the efficiency in logistics may lend great competitive edge to manufacturers.

There is emerging research on managing a multi-product and multi-echelon supply chain (Chen & Chen, 2006). One component of this chain is the distribution channel. The choice of a distribution channel not only depends on economic objectives (how to put a product to market at the lowest possible cost), but also on the specific constraints of each market and of each company operating in a particular market. According to Jallais (1994), the functional approach brings to light three main functions of a distribution channel: (1) spatial functions, related to the transport and the assorting of products, (2) time functions, related to stocking and to the financing of transactions, and (3) commercial functions, which deal with product assortment management, communication, and customer services. In his analysis of the criteria influencing a company's distribution policy, Jallais (1994) observes that certain functions become more important than others according to the specific constraints of each company. For example, a company that operates in a market where the customers are scattered out (i.e., consumer goods) will pay special attention to the spatial functions of the channel it is going to choose. In addition, a company that distributes products requiring maintenance such as cars or computers will favor the commercial functions. It is also noted that a small company with limited financial resources will be more interested in the time functions.

Along with these criteria for choice linked to the characteristics of the supplier, other choices linked to a company's environment may come into play, such as during an economic recession leading to a drop in consumer consumption, a company will favor a short distribution channel limiting the profit margins of each channel intermediary. This short distribution channel is distinguished by a direct relationship between the manufacturer and the retailer, as opposed to a long distribution channel that associates one or more intermediaries between the manufacturer and the retailer (De Blic, 2000).

Therefore, it can be seen that the choice of a distribution channel is a major decision for a company involving economic, commercial, and strategic aspects. This power struggle between the manufacturers and retailers with ownership of the distribution centers is the central theme of this research. Specifically, the dynamics of this power struggle and the origin of the shift in control of the distribution channels are of particular interest to the researchers. The objective of this study is to begin to qualify and intimately quantify this complex network of relationships between the manufacturers and the retailers from an historical perspective. It is contended that there are myriad ways to achieve a balance of power in the distribution channel by taking certain action, and by being proactive as well as responsive to market needs. To that end, this study will present an action plan for manufacturers that will allow them to achieve some

modicum of power in the channel. In the next section, a brief history of the French Supermarket will be presented with the consequences of its advent. A discussion on the channels of distribution in the Supermarket industry will be discussed in section III. Section IV will present the courses of action for Manufacturers to achieve a balance of power in the channel. The study will be concluded with observations for the future of the industry and suggestions for future research.

## 1. French Supermarket Distribution

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Created in the nineteenth century<sup>1</sup>, the modern supermarket distribution concept really began to develop in the second half of the twentieth century with the appearance of the first self-service discount store<sup>2</sup>. It was not until 1963 before this new form of distribution really began to be popularized and accepted with the appearance of the first Carrefour hypermarket in the Parisian suburbs.

Since 1965, supermarket distribution has developed very quickly, first of all through internal growth with the opening of more than 7,000 hypermarkets and supermarkets in the span of 25 years, and then through external growth after the laws limiting the expansion of supermarket distribution had been voted on and ratified<sup>3</sup>. This policy of external growth has led to a concentration in this sector of activity with five companies today representing 96 percent of the turnover in the French supermarket distribution market. Parallel to this concentration, distribution companies have begun international development either through the opening of new shops abroad, or through the buying out of established distribution groups.

The following revealing figures from 2000 enable us to better understand the power of these companies: (1) two out of three food products in France are sold in hypermarkets or supermarkets, (2) one non-food product out of five in France is sold in hypermarkets or supermarkets, (3) the turnover of the Carrefour Group, the premier French supermarket distributor, is approximately twice as high as the Nestlé Group turnover, the world agro-business leader, (4) there are more than thirty one thousand stores in France for a total sales surface area of 18,500 thousand square meters, and (5) originally specialized in everyday consumer products (food, detergents, hygiene, small household items), little by little the French supermarket distributors are gaining ground in the major sectors of consumer markets (gasoline, clothing, pharmacy, jewelry, press items) and also in the service sector (travel, insurance, loans). Certain retail companies have even tested the sale of cars and homes. The development of the French supermarket distribution sector can be explained by several different factors. These include, but are not limited to a favorable economic environment. For example, the French supermarket distribution sector was born after the Second World War, making the most of the "glorious thirties", which were thirty years of uninterrupted economic growth in France that led to an increase in consumer purchasing power in the consumer demand. Also, there is an attractive concept during a time of reconstruction. This means there have been low prices for a very wide assortment of self-service sold products. Lastly, there is a policy of additional services appreciated by the consumer. For example, big car parks at the hypermarkets, shopping malls including cinemas, restaurants, and various boutiques.

The consequences of this distribution sector and the mediating factors are obvious. In 1948, Edoard Leclerc, the founder of "Centres Leclerc"<sup>4</sup> was having difficulty in obtaining food supplies because the manufacturers wanted to protect their main clients (small green grocers) from Leclerc's low price policy. Today, no national or international manufacturer is able to get by without the turnover represented by "Centres Leclerc." In 1964, manufacturers delivered a standard product to the supermarket distribution sector. Today, they more than not develop specific packaging for this type of customer. At the end of the

1 : Creation of the first department store in Paris in 1852

2 : Creation of the first Leclerc discount store in 1949

3 : 1973 Royer Law, and especially the 1996 Galland and Raffarin Laws

4 : Current the number two French supermarket distributor

sixties manufacturers demanded payment on delivery; today they have difficulty in "negotiating" payment 60 days after delivery. At the beginning of the seventies, retailers needed the top national brands in order to enhance the value of their offer, today they favor own brands or bargain brands over national brands.

## 2. Power Dynamics in Supermarket Distribution Channels

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It is evident that the power previously held by the manufacturers now belongs to the distributors. In order to better understand the reasons for this domination, it is necessary to examine the factors of economic dependence existing in this distribution channel. Dubost (1997) in his research in the Journées de l'IAE de Nantes and Pfeffer and Salancik (1978) show there is an economic dependence between a company A and a company B if the following conditions exist: (1) essentiality of the resource: the resource that A obtains from B is essential, i.e., absolutely vital to its running; (2) concentration of the resource: B is either a major supplier or a unique supplier or resource to A; and (3) replaceability: it is difficult to replace B, i.e., no alternative source of supplies exists for A. If this model is now applied to the French supermarket distribution sector (company B) and to its suppliers (company A), it is possible to show that a supplier is indeed dependent on the supermarket distribution sector and conversely the supermarket distribution sector is absolutely not dependent on one of its suppliers.

### 2.1 - Essentiality of the Resource

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The supermarket distribution sector operates in a large number of different markets, whether this for everyday products, for semi-durable goods or durable goods, or in the service sector. On average, a hypermarket sells between 25,000 and 60,000 referenced goods items. If a hypermarket were to withdraw a referenced item due to a disagreement with one of its suppliers it could continue to operate without any difficulty. In this way the resource obtained from its supplier is not essential to its running. On the contrary, a manufacturer of food products, for example, knows that two thirds of market sales are made in the supermarket distribution sector, which it cannot do without in order to reach its market.

### 2.2 - Concentration of the Resource

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To give more understanding, the case of the French branch of a major world-wide agro-business group is examined. This company, the market leader, has the equivalent of a 1,047,800,000 Euros turnover in France, accounting for an average of only 0,2 percent of the turnover of the supermarket distributors with whom it works. The distributors are not therefore dependant on this company. On the contrary, this supplier makes 96 percent of its turnover from four supermarket distributors. Its turnover is therefore totally concentrated on these customers and this company is totally dependant on the supermarket distribution sector.

## 2.3 - Replaceability of the resource

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Very early on, the supermarket distribution sector realized that it had to make several producers compete with each other if it were to obtain favorable purchasing conditions. This is the reason why it always works with several national suppliers per market segment. This same tactic brought it to develop own brands to compete with national supplier brands, or to favor the development of bargain brands. In brief, the supermarket distribution sector can at any time replace a supplier's offer by other equivalent offers without seriously penalizing its own activity. For the manufacturers themselves, these characteristics of the supermarket distribution sector are inescapable. As far as everyday consumer goods are concerned, no other distribution channel exists that could make up for the sales made (or lost) in the supermarket distribution sector. No distribution channel can therefore replace this one with equivalent results.

## 3. A Model for Manufacturers' Reaction in the Distribution Chain

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Before examining the possible responses open to manufacturers, it is relevant to this study to examine the fundamentals of the relational dynamics existing between customers and suppliers. According to Guibert (1999), a relational exchange between a customer and a supplier can only happen if the following three conditions exist: (1) economic dependency must be balanced, (2) a feeling of trust must be established, and (3) partners must be committed to each other. Morgan and Hunt (1994) consider in particular that commitment and trust are the key factors of cooperation since they encourage partners. They observe that "to preserve relational investments by cooperating with partners, to resist the attraction of short-term alternatives in favor of long-term benefits and to see potentially risky actions as in fact not being risky is the belief that partners will not react in an opportunist way." This rather ideal plan of relations is very difficult to put into practice in the supermarket distribution sector, as the latter has precisely built up its power through making suppliers compete with each other in the short-term and by continuously training its buyers to negotiate lower prices at the risk of jeopardizing the financial balance of its suppliers. Guibert (1999) thus explains that in a situation of unbalanced economic dependence where it is more in the interest of one partner (the supplier) than the other (the supermarket distributor) to maintain the relation, it is far easier for one of the partners to unilaterally break this relationship. For instance, if the supermarket distributor obtains better prices from another supplier, it can very easily end its relationship with the previous supplier.

For the supplier, the solution is therefore to oppose this force, thus enabling it (partly, at least) to fight the hegemony of its customers for want of being able to impose a lasting relationship based on trust. Different elements can be put forward representing the final form of resistance open to suppliers in order to oppose the force of the supermarket distributors.

While this preliminary study is only qualitative in nature, it is understood that these themes will benefit from the future quantitative exploration of correlations between the putting into action of certain plans by suppliers and the level of dependence of the supermarket distributors in relation to their suppliers. The initial aim of this study is more modest in nature: it aims to describe the levers current activated by the suppliers to the supermarket distribution sectors and to show how they have loosened the stranglehold in which they are caught. The following areas are examined: product innovation, support from top brands, the management of commercial relationships, and the new distribution channels.

## 4. An Examination of the Current Levers Activated by the Suppliers

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Product innovation has been observed when the supermarket distributors receive their power, partly from being able to choose between several different suppliers in order to obtain products of similar quality. Here the notion of quality is that of marketing, namely the ability of a product to more or less completely satisfy the needs of the target population. This system works in a stable market where product offer develops little and is the same from one supplier to another. It is therefore possible to imagine that the balance of power can be shifted when product innovation coming from just one supplier challenges the interchangeable nature of suppliers in a market. The supplier from which the product innovation originates clearly becomes the only supplier capable of supplying its customers with this type of product. For a while, until its competitors develop a similar product, it therefore has an important role to play. The resource it offers is a rare one and its value can be enhanced. Because there are no competitors, it cannot be easily replaced. Innovation therefore allows for a relationship of dependence between a supplier and a distributor to be balanced out. It goes without saying that this innovation must satisfy the needs of customers whose spontaneous demand would justify that a distributor be interested in the product.

Another observed mediating factor is that of support of top brands. The majority of the big groups operating in the supermarket distribution sector has a portfolio of top brands backed by major advertising campaigns. The current policy of these big groups is to reduce the number of brands put to the forefront, and to group together an increasingly wide product range underneath these brands whose positive values will be of benefit to all the products, as explained by Kapferer (1998). Kapferer showed in particular that these brands were in some cases a rallying sign for the consumer who then decided to purchase a product according to the level of trust associated with a particular brand. Distributors therefore find it more difficult to do without products backed by top brands, even if equivalent products are available from other suppliers. The supplier gets its legitimacy from the consumer demand generated around a brand. It therefore challenges the power of its clients by the support from consumers who overwhelmingly approve of the branded product offer. Unable to ignore consumer expectations over the long-term, the distributor has to endeavor to keep these brands in its selections, obliging it to give greater importance to a long-term relationship with its supplier. It is possible to argue against this in as much as brand value, in particular for everyday consumer products, is less important than it was in the eighties since the consumer reasons more objectively than in the past being more attached to the concrete benefits of a product purchased than the subjective promises made by a brand. Nonetheless, leading brands have remained a certain value. It is also noted that this strategy of "lobbying by brands," the privilege of companies such as Danone, is not within the reach of just any company, given the high cost of creating and maintaining top brands.

The management of commercial relationships is also an area of observed significance. Certain companies very early on understood the supermarket distribution sector was becoming inescapable in numerous markets, and that long-term development was only possible if they established long-lasting relationships with these clients. It was therefore important to create and maintain a partnership based on trust and cooperation. The usual climate of confrontation and conflict was eliminated to be replaced by a climate of collaboration with close links and regular meetings. Products and services adapted to these customers were proposed instead of imposing standard products based on consumer surveys. Customers were informed upstream of any event rather than presenting them with a *fait accompli*. Internal logistic, administrative and production organization was optimized in order to adapt better to customer constraints. The aim of this approach was to generate a collaborative reflex between the supplier and the manufacturer thus enabling them to work hand in hand toward a common goal. Examples of this kind of close collaboration between the supplier and the distributor include the development of Trade Marketing style promotions and the setting up of electronic data interchange (EDI) systems. This is therefore no longer a situation of aggressive opposition force, but rather a situation where there is the desire to establish mutual trust favoring the creation of a long-term relationship. On the same subject there is an observational example of the initiative taken by Procter and Gamble (P&G) and the American distribution

giant Wal-Mart: P&G asked some of its members of staff to go and work for Wal-Mart in order to understand the “internal” organization of this store. This understanding thereafter enabled P&G to optimize its organization in line with Wal-Mart. This is probably the most interesting tactic of all, in as much as it attacks the problem at its root, namely the historical distrust existing between suppliers and the supermarket distribution sector. Unfortunately, it is not an easy one to put into practice, given the high level of cultural resistance between these two partners.

It is observed that faced with the operational difficulties encountered with the supermarket distribution sector, at one point some manufacturers considered creating parallel distribution channels to sell their products. Very little is known about the feasibility studies carried out by companies on this subject, apart from the fact that these studies brought out the risks of this strategy, for example the loss of traditional customers, limited market coverage, very high setting up costs. Further interest has been shown in this subject over the last few years boosted by e-commerce. Some economic journalists have studied the impact of e-commerce on traditional distribution activities. The survey implemented by them is extremely complex to conduct under current circumstances as numerous factors are still almost uncontrollable. Examples of such problems include: (1) a great difference from one sector of activity to another: big differences exist in terms of transport costs, purchasing frequency, and shelf life between everyday consumer goods and semi-durable items, which generate very different forms of production, logistic, and invoicing organization; (2) imperfect technology: slow throughput, e-commerce sites that are overloaded and too complex to navigate through, all of which contributes to preventing the consumer from spontaneously using existing electronic channels; (3) unstable economic actors: as it is the case in every new sector, e-commerce favored an explosion of new company start-ups whose technical skills and financial soundness were non sufficient to fulfill their promises. Many sites disappeared soon after having been created thus reinforcing the perception of risk for the consumer. In general, the start-ups that appeared on this market did not sufficiently master the complexity of the logistics of the delivery of complex product assortments to varied populations that were geographically widespread which led to endless delivery errors and billing problems.

## Conclusion

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As previously stated, this preliminary study only touches the surface. The greatest limitation of the study rests with the qualitative and observational nature of the research. Implications for future research abound. Ongoing research into the distribution channels of supermarkets include both qualitative and quantitative methodologies. Examination of the supermarket distribution chain not only in France, but within the U.S. and South America will be explored to add richness and robustness to this very interesting topic. The comparative and quantitative nature of the next stage of this research will continue to add much to the body of knowledge. It has been observed that as e-commerce has begun to take off in France, the players in the distribution chain who are most able to offer a polished service in this domain already master the logistic aspect, including the mail order specialists and the supermarket distribution sector. A diversification strategy of distribution channels supported by e-commerce will only see the day once consumers have integrated this tool into their everyday lives. It is up to the French manufacturers to contribute to the continual development of supply chain and distribution chain technology and tools to reap benefit from them.

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