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Stanley C. Hollander

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# CONGLOMERATES IN THE RETAIL TRADES

STANLEY C. HOLLANDER\*

Words have both denotations and connotations. Although the word "conglomerate" may denote any organization which undertakes relatively diverse activities, much of the current discussion of conglomerate enterprise has focused on large scale financial and industrial, *i.e.*, manufacturing, aggregations. The term evokes an image of high technology companies centered in the United States or other advanced industrial countries. Thus, for example, a recent *Fortune* study of conglomerate performance is based on an analysis of diversification among the 500 largest American manufacturers.<sup>1</sup> Similarly a current House Antitrust Subcommittee investigation is concentrating on six companies. Five of these, Ling Temco Vought, Litton Industries, Leasco Data Processing Equipment Corporation, International Telephone and Telegraph, and Gulf & Western Industries are primarily associated with complex production processes, electronic technology and/or capital intensive financial services. The sixth firm, National General Corporation has its base in movie theatre operation, but has intensively diversified into insurance and other financial sector activities.<sup>2</sup> At least one of the issues frequently raised in evaluations of the conglomerate movement, the question of the firms' ability to impose reciprocity requirements on their suppliers, is usually framed in terms of the conglomerate's role as a producer of industrial goods and services.

But conglomerate enterprises have actually developed in a much wider variety of trades and environments. The varying origins, roles and effects of these enterprises suggest that conglomerates can most properly be evaluated through a performance criterion, rather than on a structural or *per se* base. The history and current development of merchandising conglomerates, both in the United States and elsewhere, raise important issues that warrant exploration.<sup>3</sup>

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\* Professor of Marketing, Graduate School of Business Administration, Michigan State University, B.S., New York University, 1941; M.A., The American University, 1945; Ph.D., The University of Pennsylvania, 1954.

<sup>1</sup> O'Hanlon, *The Odd News about Conglomerates*, *FORTUNE*, June 15, 1967, at 174-77.

<sup>2</sup> *Congress Turning Spotlight on Conglomerate Mergers*, *SUPERMARKET NEWS*, Aug. 4, 1969, at 18. Some of the five firms have made substantial investments in such consumer services as automobile leasing and hotel operation.

<sup>3</sup> Some recent studies of conglomeration have paid at least some attention to the distributive trades. See STAFF OF HOUSE SELECT COMM. ON SMALL BUSINESS, 87TH CONG., 2D SESS., *REPORT ON MERGERS AND SUPERCONCENTRATION* (Comm. Print 1962) which is concerned with the acquisition patterns of both the 500 largest industrials and the 50 largest merchandising corporations. The textual portion of S. REID, *MERGERS, MANAGERS AND THE ECONOMY* (1968) is primarily devoted to manufacturing and mining firms, but some of the tables and footnotes, especially n.25, at 175, extend the analysis to merchandising companies. Other specialized discussions are cited *infra*.

## SOME OLDER RETAIL CONGLOMERATES

The current diversification pattern in retailing is not entirely new. The western frontier merchant often qualified as a conglomerate since he not only retailed groceries, drugs and dry goods, but also often acted as local financier, dealer and perhaps processor in agricultural crops, and sometimes also as farmer or pioneer industrialist on his own account. Atherton concludes that merchant diversity permitted specialization on the part of the other settlers, and thus accelerated the development process.<sup>4</sup> Ante-bellum southern storekeepers frequently conducted highly diverse commercial activities for their communities.<sup>5</sup> Close scrutiny of small-town business even today would probably reveal many instances of leading merchants owning two or more quite different stores.

Larger scale retail conglomerates also developed at various times. During the latter half of the nineteenth century, the then-emerging and developing department stores were widely criticized in terms very similar to the current merger debate. A good portion of Volume VII of the Industrial Commission's *Report* was devoted to the question of whether the burgeoning giant stores would gradually absorb all available trade and become insurmountable barriers to competitive entry.<sup>6</sup> The trade press of the period contained many comments, both laudatory and cautionary, on what was then called "the sell-everything system," and today is called "scrambled merchandising."<sup>7</sup> Geographical growth, as embodied in the chain store system, evoked even more intense criticism, particularly during the 1920's and 1930's.<sup>8</sup> It is somewhat reassuring to note that, at least so far, American retailing has remained more fluid, more innovative, and more viably competitive than the direr predictions of the last 90 years or so would have forecast.

## CURRENT TRENDS

Most of the earlier conglomerates, however, involved either the aggregation of diverse products at the establishment level, or the replication of existing establishments at new locations. There were some exceptions to this generalization. By the end of the 1920's, United Cigar Stores Company (itself a Tobacco Products Corporation subsidiary) controlled the Whelan Drug and Happiness Candy retail chains as well as its namesake tobacco

<sup>4</sup> Atherton, *The Pioneer Merchant in Mid-America*, 14th U. MISSOURI STUDIES 10 (1939).

<sup>5</sup> Atherton, *The Southern Country Store*, U. MISSOURI STUDIES, *supra* note 4, especially at 167.

<sup>6</sup> See REPORT OF THE INDUSTRIAL COMMISSION ON THE RELATIONS AND CONDITIONS OF CAPITAL AND LABOR EMPLOYED IN MANUFACTURING AND GENERAL BUSINESS, 56th Cong., 1st Sess. (1901).

The Commission finally concluded that, at least under contemporary conditions, the department store was a healthy procompetitive institution. See FINAL REPORT OF THE INDUSTRIAL COMMISSION, 57th Cong., 1st Sess. 549 (1902).

<sup>7</sup> See *The Sell-Everything System*, THE AMERICAN GROCER, Jan. 20, 1892.

<sup>8</sup> See G. LEBHAR, CHAIN STORES IN AMERICA: 1859-1962 (3d ed. 1963); J. PALAMOUNTAIN, THE POLITICS OF DISTRIBUTION (1955).

stores. The growth patterns of Sears, Roebuck and Montgomery Ward are well known, but the current retail conglomeration movement does seem to involve unprecedented diversification at the enterprise, rather than the establishment, level. Gross comments that:

The retail conglomerate is shaping up as a major force among the retail giants of the 1970's. This retail institution may be defined as a financial aggregation of substantially different types of retail operations. This involves *multiple* avenues of expansion, such as into both high and low margin operations, into unrelated as well as related offerings of merchandise and services, and into catering simultaneously to quite different types of clientele.<sup>9</sup>

*Fairchild's Financial Manual of Retail Stores* attempts to list all publicly-held American and Canadian corporations with substantial retail investments. Perhaps 10, or at the most 15 percent of the 209 American firms listed in the 1959 edition could be considered conglomerates under the above definition. In contrast, 25 to 33 percent of the firms listed in the 1969 edition had taken on conglomerate characteristics. *Chain Store Age* notes that less than half of the 50 largest food chains are now "pure supermarket corporations." Organizations that started as grocery chains now also own gasoline filling station, quick service restaurant, discount store, drugstore, and non-retailing subsidiaries.<sup>10</sup>

The diversified retail companies range greatly in size and in probable market impact. *Fairchild's* conglomerate listings range from the Begley Drug Company (\$14 million sales in 34 drugstores and pharmacies, 7 restaurants and 44 dry cleaning establishments) to Sears, Roebuck & Company (\$8.2 billion sales in the United States, Canada, Latin America and Spain). The firms also vary in both degree of heterogeneity and in expansion route. Thus S. S. Kresge, a variety store company, developed its own somewhat closely related K-Mart discount operation. Federal's, Inc., has used merger and acquisition to augment its original chain of popular-priced junior department stores with both discount outlets and specialty jewelry, cutlery and giftware, and fireplace supplies chains.

#### FOREIGN RETAIL CONGLOMERATES

Similar complex retail organizations have emerged in many other countries. Stacey and Wilson predicted in 1965 that the future likelihood of conglomerate mergers among British retail chains would be "high,"<sup>11</sup> and even at that time some of the largest British retailers, such as Great Universal Stores and The John Lewis Partnership had expanded into diverse branches of distribution. Both Printemps-Prisunic-SAPAC in France and La Rinas-

<sup>9</sup> Barmash, *Retail Mergers*, MERGERS AND ACQUISITIONS, Spring 1967, at 34; Gross, *Retailing in the Seventies: A Projection of Current Trends*, 79 BAYLOR BUS. STUDIES 25 (1969).

<sup>10</sup> *Now Retailing Conglomerates?*, CHAIN STORE AGE (exec. ed.), Aug. 1969, at E33.

<sup>11</sup> N. STACEY & A. WILSON, *THE CHANGING PATTERN OF DISTRIBUTION* 377 (rev. ed. 1965).

cente-UPIM in Italy embrace department, food and variety stores. The non-profit Migros organization in Switzerland is based upon food stores and truck-selling routes, but also includes gasoline stations, home craftsmen's shops, book and record clubs, a wholesale-retail travel agency, a taxicab company and a mountain railway line. General Shopping, S.A., a financial conglomerate headquartered in Luxembourg, holds interests in department, food and specialty stores in several European countries, participates in shopping center development, and also operates a retail management consulting organization. Several of the *zaibatsu* (the big Japanese manufacturing-trading conglomerates) are now reported to be involved in major retail ventures.<sup>12</sup> Much of the expatriate-owned or dominated trading business in many of the developing countries also exhibits conglomerate characteristics. Numerous other examples could be cited. As Carson says: "There are many varieties of giantism in retail systems, but the growth to larger enterprises seems to be the most common bond of overall retail trends in the free-enterprise nations."<sup>13</sup>

#### RETAIL EXPANSION AND THE CONGLOMERATE CONCEPT

But while it is easy enough to label some extremely heterogeneous merchandising firms as retail conglomerates, precise definition is, as with conglomerates in other lines, very difficult. In one sense a very high percentage of all retail growth activities is technically conglomerate in nature. Outside of routine improvement of on-going operations, a retail organization normally has only two avenues for expansion without conglomerating:

(1) it can try to attract trade through increased specialization, offering an increasingly complete selection within one merchandise or commodity division. The early American shift from general store to specialty shop is a large-scale illustration of this option. (Hence, as already suggested, except for the historical accident of precedence, the general store might have been labelled a conglomerate in comparison to the specialty outlet). But, as Adam Smith noted, the degree of possible specialization is limited by the size of the available market. And, as he probably did not point out, it is also limited by the consumer desire for the convenience of "one-stop shopping."

(2) the retail firm can try to attract a larger market share in its existing product lines at its current locations through lower prices, increased services and/or increased promotion. The possibilities here, however, are limited by statutory restrictions on price cutting (fair trade and unfair practices acts), vendor controls, and most importantly, by cost considerations. Geographical or product expansion in pursuit of scale economies may be a prerequisite to price or service competition.

Thus, most substantial retail growth takes the technically conglomerate

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<sup>12</sup> Williamson, *Japanese Industry Straightens Its Distribution Pipeline*, BUS. ABROAD, Oct. 1969, at 38.

<sup>13</sup> D. CARSON, INTERNATIONAL MARKETING 317 (1967).

forms of product and geographical expansion. But while much retail firm growth thus falls under the technical rubric of conglomerateness, relatively little such expansion may merit the implied connotation of "totally unrelated." There may be no such thing as a "pure conglomerate" in retailing, or in any other field for that matter. The current diversification movement in American retailing is unique in the extent to which it involves product extension at the enterprise rather than the establishment level. But even so, at least some potential or actual "node commonality," to use Narver's term,<sup>14</sup> is likely to integrate the various divisions of even the most diverse retail organizations.

#### EFFICIENCY

Whether those node commonalities have been fully realized in the current diversified retail firms, and especially those built by merger and acquisition, is an open question. A superficial impression, based upon the almost conventional post-acquisition press releases assuring continuance of the previous organization and staff, is that both the economies and diseconomies of integration are often slow to emerge. The Weston Canadian-American group of retailing and manufacturing companies is reported to have grown so quietly that many subordinate division heads were unaware of their affiliations and thus passed up many opportunities for integration economies.<sup>15</sup> Companies, of course, differ, and research is needed before any definitive statement can be made. Some guesses are offered below in the form of hypotheses, but they should not be treated as conclusions.

(1) Probably surprisingly few commonalities emerge in the selling and promotional activities of merged retail organizations with different product bases. Managerial strategy often requires different identities or images for the various store groups, particularly if they handle different price lines or relatively incompatible products. Joint advertising is largely precluded, although conceivably joint purchase of space or time might be possible in some cases. Most retail selling expense is a function of the counters or check-out stands to be serviced, and is not likely to be reduced through common ownership of disparate stores.

(2) More commonalities may arise in the purchasing process, if the various divisions of the corporation handle the same products. An organization that includes supermarkets, drugstores and discount stores will probably sell some identical cosmetic and patent medicine products in all stores. The extent of utilization of such quantity purchasing opportunities would be an interesting question for research. One impression is that many companies maintain separate divisional purchasing and merchandising staffs, which suggests that at least some part of the product-mix is usually not susceptible to joint procurement.

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<sup>14</sup> J. NARVER, *CONGLOMERATE MERGERS AND MARKET COMPETITION* 3 (1969).

<sup>15</sup> *Weston-Loblaw Empire: Big Food Group Tells All*, FIN. POST (Toronto), Dec. 10, 1966, at 18, col. 1.

(3) Membership in a conglomerate might give a small chain increased access to desirable sites in planned shopping centers. Center developers and their financiers have some preferences for dealing with large retail organizations, in part because of greater assurance of financial stability. They also usually like large chains because of the chains' known ability to attract patronage, but that attribute is a function of the establishment's identity rather than of its ownership.

Suspensions of a "coattail riding" effect might also occur, in fears that conglomerates could use the desirability of one of their units to force acceptance of other, less desirable, stores. Thus, a firm that owned diverse outlets could say to a center promoter: "We will not place one of our variety stores, which you want, in your center unless you also offer an attractive lease for one of our pet shops, which you don't want." But successful instances of this sort should be rare and would depend upon imperfections in the bargaining process. A rational, knowledgeable developer would offer maximum concessions to secure the desired variety store and would make a less attractive offer for the two-store combination. Similarly, rational management in the conglomerate would accept the maximum concession offer.<sup>16</sup>

(4) The conglomerate organization does receive insurance against fluctuations in one branch of trade, or in the acceptability of a given merchandising policy. Heterogeneity provides a hedge against shifts in consumer preference for discount versus full service or for specialty versus general assortment stores.

(5) Probably one of the most significant commonalities lies in the transferability of merchandising skills from one commodity group to another. Such skills are not always perfectly exchangeable; there have been both failures and successes among the many attempts, for example, at crossing the barrier between food and non-food retailing. Yet, certain talents and abilities can often be applied with equal success in the retailing of very diverse commodity groups.

Most department store managements today believe in the rotation of merchandising executives. A promising assistant buyer of, say, curtains and draperies may be promoted to be buyer of drugs and cosmetics and then eventually be transferred to men's furnishings. Merchandising and marketing ability, rather than commodity expertise, are usually the essential attributes. In this sense, drugstore, variety store, discount store and supermarket operations have many characteristics in common, as well as some differences, and provide opportunities for the use of common managerial tools.

Thus, The Dayton Company (now Dayton-Hudson), a department store-based conglomerate, is credited with having introduced a new competitive thrust in book retailing through the application of department store

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<sup>16</sup> See Bork, *Antitrust in Dubious Battle*, FORTUNE, Sept. 1969, at 103, for one discussion of this point.

merchandising and control techniques in its bookstore subsidiary, the B. Dalton and Company chain.<sup>17</sup>

#### IMPLICATIONS

The extent of utilization of such commonalities in retail conglomerates is a question of fact, and presumably researchable. The question of the desirability of such utilization is much more a question of values and judgement. The critics of some marketing activities, such as advertising, usually depict the activities under discussion as all-powerful and controlling, while paradoxically, the defenders usually talk about the lack of influence and power. Similarly, some critics might say that the best thing about retail conglomerates is that they have not utilized their full potential.

But if the promotion of competition and consumer welfare, rather than the protection of competitors, are the ultimate criteria, the formation and full exploitation of trading conglomerates would seem beneficial. It must be admitted that the largest retailers have not always been the most innovative. Both the supermarket and the self-service discount store, to cite only two illustrations, started primarily outside the conventional large chain network. The conventional department store managements were somewhat lethargic in moving to the suburbs. But on the whole, the big retailers have been vigorous competitors. They have been charged at times with overly-aggressive behavior, but there are few cases in which they have been found guilty of defensive behavior such as the imposition of horizontal collusive restraints.<sup>18</sup> Although consumers may not be completely informed judges, they certainly have some degree of competency in evaluating the services of retail institutions. Thus, the growth in market share among the larger and medium-sized organizations does suggest that those organizations have been the leaders in providing what the consumer wants.

Growth and diversification trends in distribution in the opinion of many foreign observers appear beneficial. The chairman of the British National Economic Development Committee for the Distributive Trades expresses one view that sees current growth patterns as essentially "not harmful":

In the present state of play the danger of monopoly and mergers in restricting competition is far less in distribution than in manufacturing, while the advantages of mergers in leading to greater efficiency are also probably less and probably slower to achieve.

There is considerable scope for increased efficiency in distribution and this is most likely to come from unfettered competition and the minimum of regulations, (other than those which protect the public from

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<sup>17</sup> *Dayton Turns Its Talents to Books*, BUS. WEEK, Sept. 7, 1968, at 68.

<sup>18</sup> S. HOLLANDER, RESTRAINTS UPON RETAIL COMPETITION 77-79 (M.S.U. Mktg. & Trans. No. 14, 1965).

misrepresentation and risks to health) and from better educated and more selective consumers.<sup>19</sup>

An official Irish investigative committee is somewhat more confident of beneficial results:

Developments in the Irish distributive sector, such as the tendency towards greater size (whether of organizations or outlets), aggressive trading methods, the rise of new companies, the appearance of a new kind of retailer-manager and widespread disregard for traditional boundaries between trades, have not always been welcomed. . . . But there were good economic reasons for these developments; apart from those already mentioned there is the undoubted fact that there are certain economies of scale in distribution. Experience abroad, where the developments mentioned have been underway for longer than in Ireland, does not suggest that they lead to any important socially undesirable changes, such as a reduction in employment or the disappearance of independent traders. Neither are they expected to have such results in the foreseeable future.<sup>20</sup>

In stronger terms, a trade press report, cited above, considers the current retail expansion of the major Japanese trading conglomerates as almost a necessity:

Simplification and straightening of Japan's distribution pipeline is long overdue. . . .

But now, with the nation's modern production system generating finished goods at record clips—and with a well-heeled home market to be served along with export customers—both industry and government leaders have begun moving to streamline what Mitsui spokesmen have described as the “often long and tortuous route between supply and demand.”

And this is exactly what Mitsubishi, Mitsui, and the other big trading companies have set out to do.<sup>21</sup>

Any expansion movement among large scale enterprises, carried far enough, does contain some inherent potential dangers. The current interest, not only in Japan but in the United States and elsewhere, in “vertical market systems,” *i.e.*, vertically integrated or quasi-integrated manufacturing and distributing organizations, could eventually lead to super-concentration when combined with conglomeration tendencies. At some point such concentration seems almost inevitably dysfunctional and undesirable, although the recent Japanese experience makes one wonder what level of concentration is incompatible with economic growth. But at least many instances of conglomeration in current American retailing seem to stop far short of being barriers to competition. In fact, they probably intensify competition and thus certainly deserve to be judged on their merits.

<sup>19</sup> WEEKS, PAPER, CONF. ON MONOP. & RESTRICT. PRAC., Kings College, Cambridge Univ. (Unpublished, 1968).

<sup>20</sup> NATIONAL INDUSTRIAL ECONOMIC COUNCIL OF IRELAND, NO. 21, REPORT ON CHANGE IN DISTRIBUTION 104 (1968).

<sup>21</sup> See Williamson, *supra* note 12, at 38.