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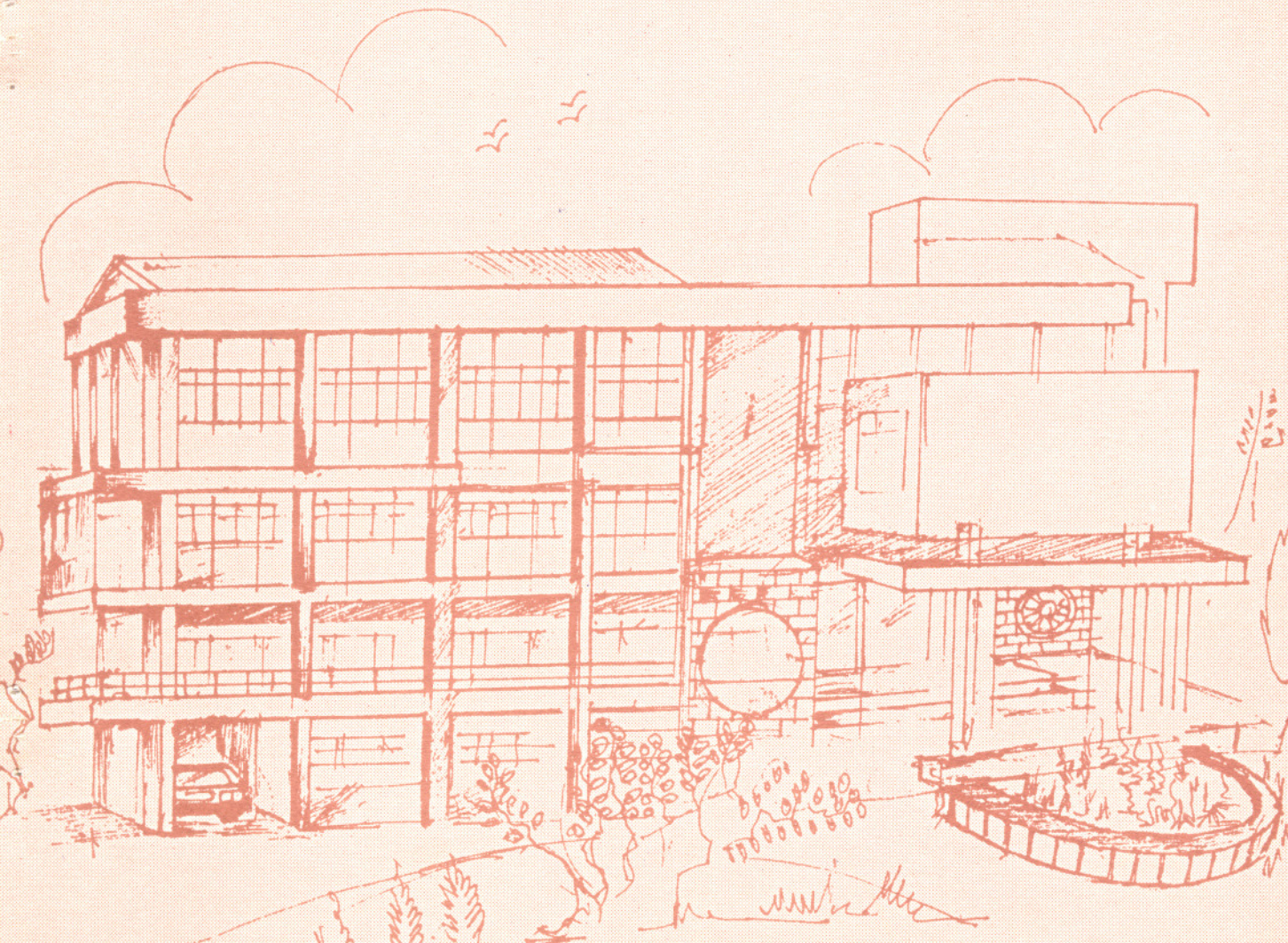
Challenges and Opportunities from Own-Store Brands



Challenges and Opportunities from Own-Store Brands

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Abstratct

Private labels of retail stores in India are on growth path. With the retail sector poised for growth, national brand manufacturers will have to contend with competition within distribution channel, which calls for revised marketing strategy locally, to thwart the threat of the private label in a store. The phenomenon also offers national brand manufacturers the opportunity to service the production needs of the private labels efficiently. The paper offers an insight into the economics of private labels and the challenges and opportunities for the national brands arising out of the growth of private labels. A few lines of possible research are also suggested at the end.

Key words: Private Labels, Postponement, Marketing Strategy, Distribution Channels

Introduction

Private labels in India are poised to grow in near future. Store-brand labels in apparel industry in India are on a complete upswing. With more and more retailers offering products under their own private labels, consumers have not had it so good as far as shopping for apparels is concerned.[1] The Government of India is looking for foreign direct investment in retail sector [2] and therefore one can expect greater growth in large retail chains or outlets in the first decade of the current century. Marketing managers struggle between cost-saving standardization for a mass market and high-cost customization for a specific niche to improve consumer-acceptance. Given the technological developments in recent times, standardized products no more enjoy unique selling propositions as imitations cannot be prevented from entry. Organizations continuously strive to find a method of creating unique selling proposition (USP) to retain their existing customers and acquire new customers. Such

[1] Quoted from "Invading Private Labels", *Retail Biz*, Sep. 2004, p. 19

[2] "FDI for Retail Brands", *Business India*, Jan. 2, 2005, p.30.

an outlook, in recent times, has called for a better understanding of distribution channels in meeting specific customer-needs. The current thinking emphasizes mass customization, a seeming synthesis of the two extremes of mass production and customisation. This has been enabled by innovation in the area of distribution management that provides scope for modification of production process to suit customers' specific needs. This phenomenon is becoming increasingly relevant in the changing scenario of distribution in India, where the urban markets witness frequent birth of private labels introduced by large retail stores, posing challenge to the brand-strength of national players. *Private label products encompass all merchandise sold under a retailer's brand. That brand be the retailer's own name or a name created exclusively by that retailer. In some cases, a retailer may belong to a wholesale group that owns the brands that are available only to the members of the group* (PLMA). A popular private label changes the status of the retailer from a customer to a competitor for a national brand marketer. When customers are competitors, standard predatory strategies and tactics may not be appropriate; instead, there is a premium on creating a successful basis for coexistence (Dhar and Hock, 1997, p. 209). This calls for improvisation in the elements of marketing strategy of the national brands. Manufacturers of national brands need to look for ways of carrying out business due to the potential loss of business resulting from such local onslaughts.

Though private labels have attracted attention of channel researchers about forty years ago (Stern, 1966; Boyd and Frank, 1966), in India, private brands have attracted attention primarily only in the last decade. However, research work in this area appears to leave a void. For Indian conditions, the current era symbolises the wake up call that national brand manufacturers should take note of, to effectively combat the threat of private labels. This paper assesses the recent trends in the changing scenario of distribution in India with specific reference to the growth of large retail stores and their private labels. It dwells deeper into the performance of private labels and its implications to national brands in their marketing strategy. The paper explores the aspect of customization and cost of such a proposition and examines the application of postponement in the context of private labelling. Terms such as *private label, private brand, own store-brand* and *store brand* are used interchangeably in this paper.

Changing Face of Distribution in India

The turn of the twenty first century witnessed many changes in distribution channels in India. Smaller sized convenience stores encounter challenge from large chains of

departmental stores that offer many product categories under one roof. Though convenience stores such as general merchants, grocers and mini self-service outlets will continue to exist in our country, large cities will witness the growth in one-roof shopping malls of different kinds. Already, large specialty stores such as *Subhiksha*, *Food World* in FMCG sector have set their firm foot in South India, surpassing local chain stores such as *Nilgiris* and *Vitan* in size and reach. As of September 2004, there were over 72 outlets of *Food World*.[3] *Subhiksha* has 115 outlets and is still growing in number and gaining popularity among consumers. The RPG Group that owns *Food World* has plans afoot to expand into the hyper store category even more vigorously.[4] *Home Store India Limited* (HSIL) is reported to be planning for expansion in the North. This will result in expansion in two types of retail stores: one in the hyper malls and the other in large chain of *The Sabka Bazar*.[5] Mega malls such as *Shoppers' Stop* and *Forum* have gained currency among upper middle class shoppers seeking one-roof shopping combined with class and exclusivity, and discount stores such as *Big Bazaar* are frequented by middle class families who seek one-roof shopping combined with value for money. *Shopper's Stop* is said to have plans for expansion which symbolizes more growth in private labels. Reports based on European experience reveal that private labels grow faster than national brands, the former's growth rate being estimated to be two to three times of the latter.[6] Interestingly, consumers will witness more and more of competition in retail stores between national brands and the store's brands. A case in example is the South Indian retail chain *Nilgiris* that stocks dairy products under its own brand and under national brands such as *Amul*. *Food World* has its own brand of jams selling over its counters side by side of *Kissan* and *Sil*. It is easy to comprehend that when the retail store uses its own private label on an otherwise generic product, it commits to the customers its guarantee for the quality of the store's brand. Such quality assurance will lead to greater trust among the store's customers, resulting in greater store-loyalty. This enables the store to charge a premium on an otherwise generic product, thus making private labelling an attractive proposition to the large retailers. However, in FMCG sector, the current practice is in contrast to this phenomenon, where mainly destination goods good are packed under retail labels, mostly at

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[3] "The Rising", *Retail Biz*, January 2004, p.38.

[4] "RPG Retail Blue Print Ready for 21 Giant Hypermarkets by 2006", *Financial Express*, Feb.20, 2004, p.4.

[5] "HSIL: From Homes to Malls", *Images Retail*, Sep.30, 2004, p.12.

[6] "The Ebony In-house", *Retail Biz*, Sep.30, 2004, p.21.

cheaper prices than other retail outlets (Raghuram *et al*, p.5). If this becomes the trend, then retail labels can be expected to offer value for money to customers mainly on price-plank and price-competition to national brands. Price wars often breakout when most brand leaders in a particular category do not provide private label products, and when competition comes mostly from smaller companies with lower cost structures and overheads.[7] If such be the case, then Indian companies of national brands will have a lesson to learn from the disposition of the American consumer goods manufacturers, captured comprehensively in the following statement: *Private labels are anathema to many consumer goods manufacturers. They are viewed as "category killers" – cheap, me-too products that suck all the profits out of a market by making consumers more price-sensitive. And they are also a painfully visible symbol of retailers' growing control over the distribution chain. By diminishing the power of traditional brands, private labels remove a key source of manufacturers' influence over consumers, and in turn, their leverage over merchants. They threaten to turn manufacturers into invisible vendors who must contend themselves with supplying cut-rate commodities to all-powerful retailers* (Dunne and Narasimhan, 1999, p.41). A similar assessment of Indian manufacturers' disposition towards store brands is not readily available. However, the margins on own-store brands are nearly two-and-half times higher than on FMCG brands[8] and this is likely to attract more and more private labels in FMCG sector. Though private labels in FMCG sector in India account for less that 1% of the overall sectoral sales, private labelling is a phenomenon that will grow in near future, owing to the benefits it provides the stores. It is predicted by industry sources that retail sector in FMCG will grow by 30% per year in a few years.[9]

Economics of Private Labelling

Store brands are the only set of brands for which the store is entirely responsible. Thus, the store has to bear all the costs (development, sourcing, marketing effort, time, risk and promotion) and it reaps all the rewards of the brand's success. It is intuitively evident that a store will enter into that product category that has (a) high profit margin (b) low entry barrier to labelling and (c) low switching cost to the consumers, which may be either monetary of affective. Commodities offer the best scope to stores for private labelling since competition

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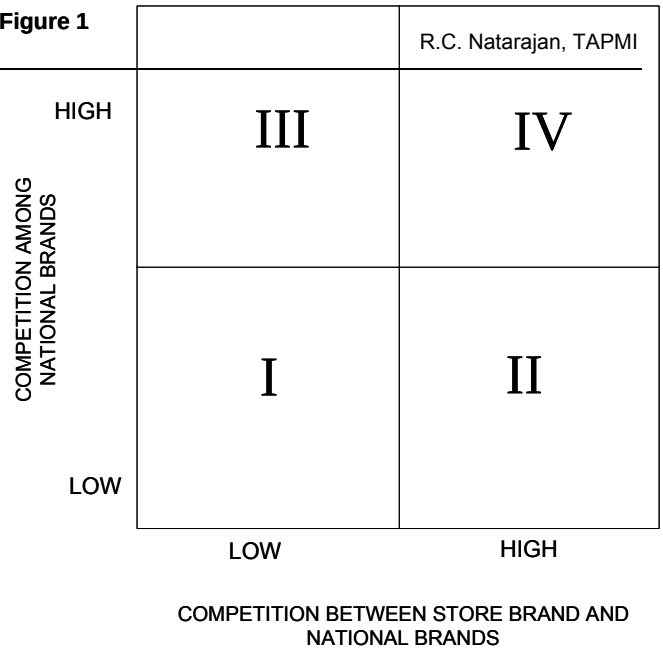
[7] "Into Our Own", *Retail Biz*, September 2004, p.17

[8] Raghu Pillai, President & CEO, RPG (Retail) quoted in "The Rising", *Retail Biz*, January 2004, p. 38.

[9] "The Rising", *Retail Biz*, January 2004, p.38.

against the store label will be minimal from the unorganised market. Further, commodities are products over which, through allocation of shelf or floor space, retail control can be quickly established (Stern, 1966, p.44). This is because the suppliers of commodities do not "purchase" shelf-space and therefore there will be little restriction or objection to the store's stacking and shelf-display of its own brands. These commodities are called "Destination" categories, normally stacked at the far end of a store, inviting the consumers to take a long walk through a maze of other products so that they may pick up some of them on the way. For retail chains such as *Food World*, these categories represent *high tactical usage* to bring in more customers and the price-related promotion of these categories falls under *aggressive* classification (Raghuram *et al*, 1999, p.5). In the case of manufactured products being introduced under private labels, the characteristics that enable store brand introduction are: (a) inexpensive, easy, low risk purchase for customer (b) easy to make from commodity ingredients (c) perishable, therefore local supplies are favoured (d) category sales are growing fast, enabling the private brand's garnering reasonably high volumes and (e) low number of national players dominating the category so the retailer feels the need to reduce dependency on them (Quelch, 1996, p.102). However, Raju *et al* (1995) propose, in a counterintuitive manner, to suggest that retailer's profits will increase more likely in product categories consisting of a large number of national brands. They explain that the profitability of a store's brand depends more on the directness of high competition between the private brand and the leading national brand, as against a high competition *among* national brands which is detrimental to the store brand (Raju *et al*, 1995, p.958). Though this aspect is not clearly explained by the authors, it seems to be their assumption that high competition among national brands implies high brand loyalty among consumers for the national brands and therefore the affective switching costs will be high. They also found support to their argument that where large number of national brands were available, introduction of a store brand increased the category profits, thus falsifying the much-held belief that a crowded category has no place for store brands. An aspect that is left wanting in their analysis is the independence of competition *among* national brands and competition *between* store brand and national brand. Evidently, this poses four possibilities of one being low or high and the other being low or high, as shown in Figure 1. The figure has been constructed with the underlying assumption that (a) it is technically feasible for the store to introduce its own brand (b) the competitive scenario does not change the position from one quadrant to another and (c) the switching costs for the consumers are not high, *per sé* .

Figure 1



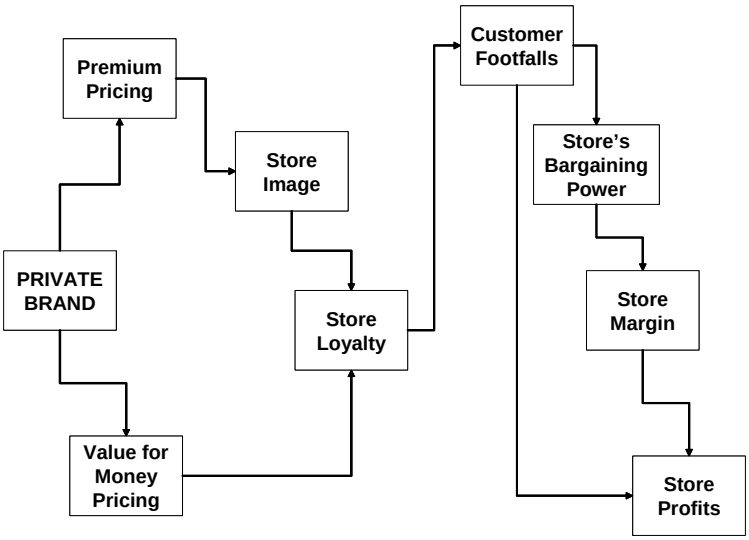
- *Quadrant I: Low-Low*: This quadrant represents a situation in store where both types of competition are low. A category that manifests low competition in both dimensions may be, *per sé*, unattractive for private label. Such a phenomenon may be caused by (a) high degree of commoditisation (b) low importance of the product category for the customers (c) high input-output ratio in manufacturing. The retail store may never enter such a category with its own label.

- *Quadrant II: High-Low*: This quadrant represents high competition between the store's brand and the major national brand and low competition among the national brands. This occurs when the consumers' affective attachment to national brands is high and achieving brand loyalty is a short-term process. This implies that the retail brand is in direct competition with the national brand and therefore the chances of consumers' positioning it along with the national brand are also high. The retail brand will not suffer from me-too syndrome. The store can promote it extra vigorously and the brand is likely to be among the top two brands in shelf-movement. The store is likely to witness a counter move by the national brand through extra point of sales promotion. Thus, the total profit through the product category will be high for the retail outlet. So, the store is better off launching its brand.

- *Quadrant III: Low-High*: This quadrant represents high competition among national brands but low competition between the store brand and national brands. This happens when the national brands are highly advertised and the customers' awareness of those brands is high, both cognitive and affective, while facing the store brand on their visit to the store. Such a situation is not favourable to the store brand since the switching costs for customers is high and hence the store will find its brand positioned among fringe brands. Therefore, if the store assesses its position in this quadrant, it is better off not launching its brand.

- *Quadrant IV: High-High*: This quadrant depicts an all-out competition among the national brands and if the store introduces its private label, it will come under direct fire as much as it will be caught in the cross-fires of the national brands. Therefore, it is expected that a store that views itself in this quadrant is better off not introducing its private label.

Figure 2



Essentially, a retail store introduces its own private label (a) to increase customer loyalty (b) to improve their positioning and image (c) to improve margins in the category (d) to lower prices to provide value for money to its customers and (e) to improve its bargaining power vis-à-vis national brand manufacturers who use the store for distribution (Bergès-Sennou *et al*, 2004, p.5). The list should also include (f) to enable the store to differentiate customers through price-quality association by premium pricing the store brand. This is represented in Figure 2 as a model of store-brand's attractiveness.

By introducing a private label, the store creates a situation of conflict with the national brand; this also makes the store's position better on the bargaining table. Thus, it shifts the power in the channel downstream (Bergès-Sennou *et al*, 2004, p.7). This may compel the national brand manufacturer to offer greater commission or discount to promote his brand in the store. Another, but important benefit of introducing private label for the retail store is the differentiation it provides to the store itself, and thus store loyalty. Therefore, the benefits of store brand cannot be confined to merely the profits the category yields but the additional footfalls it brings in. These economic benefits are not amenable to simple numerical calculations. More importantly, such benefits cannot be confined to any specific period and therefore calculation of economics of a private brand is more complex than what a static economic analysis can do. In sum, the benefits to a retailer from the introduction of store brands are (i) higher unit margin on national brands (ii) expansion of the category sales and (iii) higher category margin from sales volume (Pauwels and Srinivasan, 2004, p.366).

Managerial Aspects of Store Brands

Research is available on (a) motivation for store brand entry (b) strategic positioning of store brand (c) success of store brand (d) impact of store brand on retailer profitability and (e) impact of store brand entry on the national brand.

(a) Motivation for store brand entry: Store brand entry is motivated by the following (Scott-Morton and Zettlemeyer, 2000) :

(i) Store brand enables the store to discriminate consumers on price dimension. In most of the product categories, there are two types of consumers, namely, those who prefer quality-guarantee even at higher price and those who expect reasonable quality at reasonably low prices. The former display brand loyalty, purely due to their faith in the quality of nationally advertised brand. The latter are not affected by national advertising. They are either ready to risk the quality aspect for the gain in price or not ready to risk. Those who are ready to risk quality for price choose one of those brands from the competitive fringe in the store shelf. Those who are not ready to risk quality need a brand that is an acceptable balance between quality and price. These are the customers who can be targeted by store brand, since the quality assurance by the store that is in the vicinity provides them the confidence of accessibility in case anything goes wrong with the product. Thus, such price discrimination is possible only when national / regional advertising does not create high level of utility to a sizable chunk of the store's customers. In Indian conditions, table butter stands as an example for such products where the national advertising offers high utility to the customers, and thus there is no significant growth in any store brands in this category. On the contrary, pulses and cereals such as gram, rice and wheat flour offer least utility through their advertising and thus we see a growth of store brands in this category.

(ii) Gap between marginal and average costs is another motivating factor for the store brand. Normally, the average cost of the national brand is more likely to be higher than the marginal cost, due to national level advertising. If not very high degree of economies of scale is present in the product category, this difference between average cost and marginal cost is an attraction to the store to launch its private label. This cost-gap is availed by the store by getting its brand manufactured or packed by a smaller producer, perhaps locally, or in its own premises.

(iii) Store brands enable the retailer to differentiate the store from other stores in the vicinity. By standing guarantee to a variety of store brands, the retailer signals to the consumers his USP of higher quality. When consumers face large number of stores, their uncertainty about the outlets is high. Store labels cuts through such uncertainty and enables their faster and frugal heuristic decision.

(b) Strategic positioning of store brand: Store brand positioning is motivated by the aspects given below (Sayman *et al*, 2002):

(i) In a situation when more than one national brand is sold in the store, it makes profit-sense for the store to sell the store brand priced as high as the leading brand to offer its customers the utility of perceived quality associated with the price. Thus, though there may be a temptation to sell at lower price, on par with fringe brands, the store will be better off reaping a higher profit through a higher price. If one thinks of a perceptual map, the perceptual positioning of the store brand is guided primarily by the price-quality association and therefore the pricing should be such that it is closer to the leading national brand.

(ii) On aspects such as product packaging, pack size, design etc, it is suggested that by positioning the store brand to mimic the leading national brand the retailer can strengthen its bargaining position (Scott-Morton and Zettlemeyer, 2000, p.5).

(c) & (d) Success of store brand and Profitability: Success of store brands depends on the following factors:

(i) Introduction of a store brand in a category that consists of *large number of national brands* increases store's profitability. A caveat must be added here that this is possible only in such a situation where the competition among the national brands is low (Raju *et al*, 1995).[10] These two aspects should be present in conjunction for the introduction of store brand to lead to greater category-profits. The intuitive explanation of this phenomenon is as follows: In a situation when large number of national brands is present, the store's dependence in any one brand is small. Therefore, if the leading national brand retaliates to the store brand's introduction by stoppage of supplies, the loss of opportunity profits to the store is minimal. On the contrary, when the national brands compete within themselves fiercely, the utility to the consumer about the quality of the brands is high. In such a situation, the store brand

[10] See point (ii) in this subsection and the explanation for Quadrant II in Figure 1.

may not be able to effectively cause a switch from the national brand, and the cost of promoting the store brand may prove exorbitant. Also, despite the store's efforts to promote the store brand, the consumers may perceive it as a fringe brand. This means, in this situation, the profits (after such promotional expenses) will be lower from the category.

(ii) Dhar and Hock (1997) find six factors affecting the success of the store brand. They are

- Quality of store brand relative to national brands is high.
- The quality of store brand is consistent over a period of time.
- The product category is large in absolute value terms in store's sales revenue.
- The percentage of gross margins in the product category is high
- The number of national players is fewer than in other categories. Interestingly, this seemingly opposes the suggestion by Raju *et al* (1995) mentioned in the previous paragraph. Raju *et al* are talking, in effect, of low competitive battle in a set up of high number of competitors whereas Dhar and Hoch are talking of low competition through sheer number of brands. Thus, both the works converge on one point that the store brand will be successful when it doe not have to contend with high competitive retaliation or cross-fire.

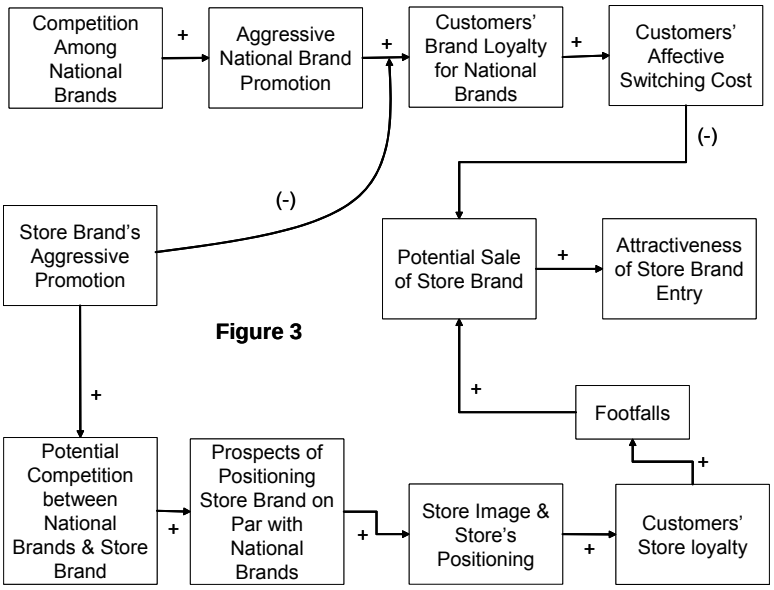


Figure 3

- National advertising expenditure in the product categories is low.

All these works cited above lack in analysis as to the specific aspects of marketing strategy to be adopted by the retailer in various conditions. Evidently, the quadrants in Figure 1 can be influenced by the strategic approach by the retailer. For example, if the store reckons itself falling in Quadrant III which prescribes non-introduction of the store-brand, it can generate competition between its brand and the national brand by aggressive in-store promotion of its

private label. This shifts the in-store context from Quadrant III to Quadrant IV in the short-run and eventually, once customer loyalty for the store brand has been built up to Quadrant II, which is favourable to the store-brand. Such a dynamic reasoning is shown in Figure 3.

Marketing Strategy against Private Label

In this section, we shall view competitive strategy from the national brand's view-point. Marketing strategy will no more be restricted to boardrooms and strategy tables. The real battle is taken to the war-field - the retail space - where the thick of action is witnessed. Companies no more compete solely with other companies for mind-space and shelf-space, but with their own distribution partners. Distribution management will no more be confined to managing distributors, ensuring supplies to retailers and sporadic managing of product movement from retail shelves through promotions. Managing large retail chains and mega malls will be a reality, which calls for different types of business-deals, calibre, aptitude and attitude among the boundary personnel. Pricing strategy will not be simply based on competitors' moves; it will consider how the retail outlets act as well as will react to the company's strategy. This may have a bearing on the segment-targeting strategy of national brands, due to the competition arising out of retailers' private labels. Introduction of private labels reduce advertising space at the points of sales, since the retail outlets may prefer promoting their own brands to promoting national brands. Alternatively, advertising through points of sales may become more expensive, with the retail outlets charging premium on shelf space and advertising space. These may cause a fundamental change in the approach of the national brands in their overall strategy of segmentation, targeting and positioning. Companies may revert to mass-media advertising by giving up the costlier point-of-sale advertising. In the following paragraphs, the impact of private labels on the elements of marketing strategy is assessed.

(a) Product: Introduction of private labels at retail stores implies to the national brands that the consumers have greater options among products they buy. This means that a wider product-range will be available. When the store competes vis-à-vis national brands on product range, the short term inability of the national brands to respond to the challenge is a matter to be contended with, since (i) a large enterprise requires longer time to respond with changes in product-strategy and (ii) the minimum quantity of production that enables the national brands to avail the economies of scale may not be available when it reacts to a single store. Alternatively, if a chain store introduces a premium or

economy brand in a category, then the national brand gets the benefit of market testing from the experience of the store brand and can thus decide whether or not it, too, should enter that segment. Thus, store brands offer an opportunity for national brands to know about consumer-response to different variants of a product category.

(b) Price: In case the store competes with the national brand on price range, it can effectively do so, by locally promoting the price-advantage to the price-sensitive consumers and by highlighting the higher quality of the premium-range products to quality-conscious consumers through its counter-salesmen. Under such conditions, the national brand has two options: (i) it can fight the store brands on price or (ii) it may increase its prices and highlight its higher quality through national campaigns. Fighting is an option the national brand can exercise when the customers' loyalty to the national brand is greater than the customers' store-loyalty. The decision to fight price-reduction in kind has both advantages and disadvantages. The advantage is that the store brand will find it difficult to gain acceptance among consumers, if an established national brand is available at a similar price. The national brand may succeed in nipping a budding store brand. For a national brand, response to a reduction of price need not be in kind. It can respond with special consumer-offer or discount which prevents long term commitment as well as avoids reduction of price across all markets or stores. The response may be confined only to the specific store. Further, price-reduction by the national brand can cause a setback to it in the form of price-quality association. Therefore, the best response is to counter the threat with promotional offers. One common tactic is to *change customers' choices* and limiting price reductions to areas where the national brand is vulnerable, thus localizing a price war (Rao *et al*, 2000, p.8). However, fighting on price can cause vertical conflict in the distribution channel between the company and the store, a proposition that is unhealthy to the national brand's success in the long run. In all, the best response to a store's introduction of a low price brand is to resist the temptation to respond with a similar move and focus on other aspects of marketing mix.

(c) Place: Private labelling symbolizes the shift of intra-channel power downstream. Whereas the national brands have conditioned the perceptions and preferences of consumers by the quality of their brands and the content of their communication, retailers who own private labels are in a position to dictate terms to their manufacturers about the standards to be adopted in quality (and even in production process) that may

well change the consumer perceptions and preferences away from the national brands. Where the specific quality of the product is not contractible by a private label owner, the retailer may contract the method of production or insist on obtaining certain certifications such as ISO. This may result in shift of certain investment costs upstream, an eventuality that the manufacturers of national brands and private brands should be aware of. In essence, the major impact of private labels may well be the increase in transaction costs for the manufacturers. Every channel arrangement is characterized by a common goal on the one hand and a channel conflict on the other. The common goal is to achieve transfer of utility from manufacturer to consumer whereas the conflict is about the sharing of costs and benefits of this transfer. Private labelling heightens such conflicts by adding a dimension of contrary marketing interests; that is, the national brand competes with the private label of the retail store for shelf space and consumer-attention. Which way the needle will tilt in this power struggle will depend on the relative degrees of brand loyalty and store loyalty. When the national brand enjoys greater brand loyalty than store loyalty, the retailer is compelled to store the brand. Besides, the national brand manufacturer may be in a position to penalize an opposing retailer by supplying less quantity of such high-loyal brands or withdrawal of supplies altogether, an eventuality that may affect the image of the retailer among the public. Manufacturers of near-monopoly brands enjoy this position, vis-à-vis retailers. In a situation where the brand loyalty enjoyed by the national brand is less than the store loyalty, the retailer is in a position to dictate terms about the terms of supplies, delivery and payment in addition to further schemes and discounts. Depending upon the quantum of business the retail stores provides to the manufacturer, the manufacturer acquiesces or withdraws his dealings. Manufacturers of large national brands may be tempted by the thought that private labels can be choked if the national companies refuse to manufacture such brands. This thinking can be myopic and harm the national brands if the stores are able to locate alternate sources of supply.[11] Dunne and Narasimhan (1999, p. 44-45) provide the example of Coke and Pepsi in Canada when they refused to supply private labels to grocers in Canada. The grocers located a small company, Cott, who gained 20% market share in the process, bringing down the bigger brands' margins considerably.

[11] For a detailed explanation of the consequences of national brand's refusal to supply private labels, see Louis W. Stern, *op. cit.*, p.45.

(d) Promotion: As is evident from the previous paragraphs, private labels take the brand-battle to the point of sales. The national brands compete with the private labels for store's shelf-space and consumers' attention-space. With the store brands understandably getting the best shelf space in terms of visibility at eye level, strategic points such as entry point and shelf display, national brands need to compete for the same facilities at higher cost than earlier. Thus, private labelling increases transaction costs for the national brands through higher promotion costs. However, given an understanding that it may be difficult to beat the retail brand in its own store through promotion, national brands may resort to increased mass media advertising to create consumer pull. This will prove meaningful only if the national brand faces competition from private labels all over the country. Though regional mass media advertising can be increased, the cost may still prove to be supra-optimal.

Opportunities for National Brand Manufacturers

Private labels also offer opportunities to national companies. The retail labels need to maintain high quality to survive and compete with established national brands. This provides the opportunity to the national level manufacturers to offer manufacturing to the retail outlets under private labels. This will make business sense especially when private labels' being introduced may affect capacity utilization adversely. This also poses peculiar challenges of customized production. When retail stores choose to carry their own brands, the merchandise requires packaging and standardisation to meet the needs of the local consumers. It will be cheaper for the retail stores to outsource the packaging work than to carry out the job themselves. National brand manufacturers stand a better chance to service the retail outlets in this regard since the job requires no additional overheads. Marginal cost based calculations may well work favour of the national brands in winning such job orders that may enable them to utilise their production capacities better.

However, such job-orders also pose a new type of challenge to the manufacturers. The job orders, which may follow partly stochastic variations in time and quantity, mean a newer type of production planning than when a standardised product was manufactured. Suppose a national brand manufacturer reconciles to the phenomenon of manufacturing own brand as well as a few private labels has a new challenge of scheduling production that meets the two opposing ends effectively: (i) minimising inventory carrying cost and (ii) minimising waiting time for the retailer. Whereas the former warrants postponing production after getting the

retailer's orders, the latter demands speculative, anticipatory production. *Postponement* as a concept is useful in this context, which enables balancing between these two opposing needs.

Postponement

Postponement is defined as the act of delaying the completion of production for achieving cost-saving by moving differentiation nearer to the time of purchase (Bucklin, 1965). The purpose of postponement can be two; it can be for (a) meeting unpredictable demand for specific variants (b) ensuring higher level of customization. Benetton casual ware is an oft quoted example. The casual ware market in the West witnesses frequent change of fashion. The company could not plan its production of various colours accurately, which resulted in stock-out in some colours and excess inventory in other colours. The problem was overcome by shifting the completion of dying to (a) the time of purchase by the consumers and (b) to the location of such purchase. That is, "the company began dying assembled garments rather than yarn" (Signorelli and Heskett, 1984, p.4). This enabled the company to meet the local demand accurately, simultaneously reducing the costs of both excess inventory and stock-outs. In mid-90s, Hewlett-Packard reduced its costs in channel through customization achieved by postponement of assembling its printers and transporting components to its regional warehouses (Feitzinger and Lee, 1997). In the case of hi-tech products such as semiconductor, it has been shown that postponement of both production and process have enabled mass customization to suit the customers' specific needs that display a wide range (Lee and Petrakian, 2000).

Postponement becomes desirable when the degree of customization expected by customers is high. However, this requires *modularization*, which means that (a) production involves such processes where a part of the sub-process can be shifted in space without the need for re-entry into factory for completion or (b) production involves such processes where a part of the sub-process can be delayed and *resequencing*, which means that production involves such processes that do not depend upon one another and shifting the order of the processes is a possibility. Majority of the common processes are finished at the factory and the semi-finished components are either kept aside for finishing later (time postponement) or sent to regional warehouses for assembling depending upon the local demand (form postponement).

The first known paper on postponement dates back to 1950 by Wroe Alderson, quoted by Bucklin (1965). In that paper, the Bucklin contrasts postponement in time against holding speculative inventory. The aspect of postponement for better customization was not touched upon. For over half-century, the bicycle industry in India has been following this practice while distributing products to dealers. Much of the consignments shipped to the dealers were in components. This gave three advantages to the companies: (i) Components could be packaged compactly and therefore more could be shipped, economizing shipping cost (ii) compact packaging implied less transit damages, as compared to finished products and (iii) customization at dealer-point was enabled. Paint industry in India adopted postponement concept by creating a simple technology that enabled the companies to ship the common base-liquid to its regional hubs along with small quantities of tinge materials. The specific colour needs of the customers, today, can be met by a dealer in as short a time as a few minutes. This process is aided by the use of computers that calculate the specific quantities of different colour pigments needed to achieve the customer-specific colour-needs. Computer assemblers practice postponement by first getting the requirement of the customers before even ordering for the components to be assembled. The customer is happy as his needs are met; the dealer / assembler is happy as his inventory holding is minimized, improving his bottom line. Essentially, postponement aids *delayed product differentiation* through customization and *quick response* to customer's needs as opposed to standardization where the customer-specific model may not be readily available and where the cost of keeping inventory of customer-specific models in anticipation of demand is too prohibitive.

Types of Postponement

Zinn and Bowersox (1988) identify five types of postponement one of which is *Labelling Postponement*. This occurs, typically, when large retail outlets outsource manufacturing and packaging of their products to a third party manufacturer. The manufacturer of such products undertakes production and packaging for many retail chains, though the core product is the same. Under conditions where the preferred pack sizes are identical across retailers, the manufacturer faces the problem of uncertainty of demand in terms of the specific labelling to be done. Whereas the retailers expect quick delivery, packing and storing the specifically labelled packs increases the cost to the manufacturer. Postponing labelling to the time of receiving the order from the retailer enables the manufacturer to economize on

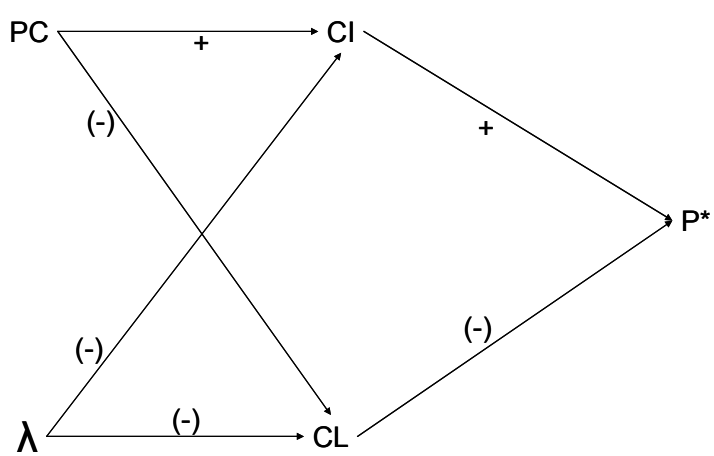
cost of inventory. However, to the extent the labelled packs are not kept ready, it involves waiting cost to the retailer. Increased levels of postponement cause lead time, caused by certain customers shunning the manufacturer, unwilling to wait long. Since greater customization is achieved through postponement, the inventory holding by both the manufacturer and the retailer is reduced, thus decreasing the inventory-holding cost. Thus, two forces cost-reduction and cost-increase, work on the decision on postponement. The optimum level of postponement, implying the cost minimizing level of postponement is determined by these two opposing forces. The optimum level of postponement is also influenced by the technology level and the degree of customization demanded by customers.

It should be noted that postponement is possible only when the pack containers are identical across the retail brands, so that unlabelled packs can be packed in advance and labelling can be done as and when orders are received. This implies that variance in ordering by all retail brands are combined, which is less than the sum of individual variances for each brand. Only if the production and packing process enables this separation of packing and labelling, postponement solves the inventory problem effectively.

Cost of Postponement

The best model of cost of postponement is available in Waller *et al* (2000). The cited work considers production postponement in a supply chain and does not provide a systemic model. Rather, the model emerges to a keen reader. Cost of postponement is divided into (a) Cost of Inventory (C_I) and (b) Cost of Lead Time (C_L). The former varies negatively due to (i) reduction in stock-holding of common components and (ii) holding finished stocks is always costlier than holding raw materials or semi-finished products. Cost of lead time varies positively since postponement results in some waiting time for customers, and some of them may not like to wait, and therefore may switch to other brands / outlets. Thus, the cumulative effect of C_I and C_L determines the total cost of postponement and there exists a

Figure 4



cost-optimising level of postponement, denoted by P* for a given level of C_I and C_L. When the desired level of product customisation (PC) increases, the optimal postponement level too increases, since when PC increases, it increases C_I and decreases C_L. When the speed of production (λ) increases, decreases the total cost. But the impact of increase in speed of production on the optimal level of postponement is indeterminate. This model is summarised in Figure 4.

Future Research Prospects

Based on the foregoing analysis, the following aspects can be researched taking the retail sector in India separately:

- Currently, private labelling is a legacy in clothing (*West Side*) and in FMCG (mainly destination categories, with a few dairy products as exception in the case of *Nilgiris* and jams in *Food World*). Products that require high level of consumer confidence – such as baby food and health products – do not the entry of private labels. What are the endogenous and environmental factors that facilitate private labelling? How do different product categories fare in such an analysis? Work by Raju *et al* (1995) may prove useful as a guide. The cited work is a study for understanding (in the USA) what makes a product category suitable for store brands introduction. Do the findings in India differ significantly?
- What are the different strategies adopted by retail stores to promote their private brands? What explains the commonalities and what explains the variations?
- How are the national (or even regional) brands disposed toward the phenomenon of private labelling? Is there a difference in the promotional practices of the national brands between the private labelled stores and others?
- Current literature, mainly based on the Western nations' experiences, deal with national brand versus retail brand as one-on-one issue. However, in reality, a national brand manufacturers / marketers sell many product categories through retail stores. In the context of multiple brand sales by a national brand manufacturer, what is the effect of the product-range sales on the power position in the channel? This aspect can be effectively studied through case study research method.
- Does private label result in better store loyalty? Or, does perceived store loyalty cause retailers to introduce store brands? Alternatively, what is the cause-effect direction between store-loyalty and private labelling?
- Are there differences in the way in which channel conflict due to store brands is perceived by the stores and the national brand manufacturers? Intuitively, it ought to be so. Is there significant difference? Why?
- Has there been an impact on the prices of national brands sold in the specific store after the store has launched its own brands in a specific category?

- In what categories, store brands are imitations of national brands? How are they positioned against the original? (Premium, economy or fringe)
- How are private brands positioned in consumers' perceptual space vis-à-vis national brands?
- What research methods stores that own private brands use to collect consumers' perception about their brands? Is systematic research pursued? This can be studied through case method research.

Conclusion

This study has not attempted to test empirically the theories and concepts proposed since it is too early in India to undertake any such work meaningfully. Experience with private labels in the US, Europe and Australia have been studied and recorded whereas in India the effect of it on the national brands is yet to strike alarm. However, private labelling in India is here to stay. It is likely to grow significantly, especially in major urban areas, where the national brands will find this phenomenon a force to reckon with. Though at this juncture private labelling occurs predominantly in "destination" categories such as cereals and pulses in FMCG sector, it will not be long before the mega stores move towards labelling other packaged products as well. Brand loyalty will face assault not only from other brands but also from store loyalty, aiding the growth of private labels. Such a growth of private labels offers challenges to the national brands in terms of the elements of marketing strategy. It also provides the manufacturers of national brands the opportunity to (a) move away from mass marketing to segment or niche oriented marketing in the specific market area and (b) utilise their production capacity better by tying up with the retail stores to pack their brands under the store labels.

However, whether private labelling is worth bothering about in India where the share of private brands is far below 0.5% - borne out by the country's name not figuring in the AC Nielson's July 2003 report – is a question that deserves attention. Whereas it is understandable that retail chains are more powerful vis-à-vis national brands in Europe due to the sheer size (small) of European countries as compared to the USA, the largeness of India may well allow the national brands in our country to wield considerable power over retailers for more years to come. Possibly, the national brands may obtain their power position vis-à-vis large retail stores through direct dealing – bypassing distributor network – thus passing off better commissions to the large retailers. This means that the retail brand introductions in India may cause win-win arrangements between the manufacturers and

retailers at the cost of other intermediaries. Manufacturers may be better off avoiding a direct confrontation with retailers. The phenomenon of introduction of retail brands in India offers the greatest scope to testify that marketing ceases to focus merely on competition and has started to look at the prospects of *co-opetition* as the core of strategy, a phrase that has gained currency in recent times in marketing literature. It can be expected that retail outlets will focus more on quality of their brands for better positioning. To counter their quality-threat, the national brands may come up with innovations in packaging as well as the same quality at lower prices. Since retail outlets are predominantly unorganised, localised competition may set the national brands thinking of unique methods by which they can ward off all such dispersed threats in one sweep. Store brand entry (a) increases consumer choice in store and (b) it makes the national brands to switch to just price and to avoid near-monopoly pricing. What was prophesized for the US will hold true for India: Private labels will grow; and, national brands will dominate (Salmon and Cmar, 1987, p.99). Consumers will be better off due to this brewing conflict, a sign of competition promoting consumers' welfare.

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