The localized merchandising for international retailers:
a study of Tesco's failure in Japan

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Abstract

Considering Tesco's record of successful retail operations in global markets, its failure in the Japanese market and subsequent withdrawal surprised many people. This study aims to investigate the main factors for Tesco's failure in the Japanese market. We focus on the company's localized merchandising (MD) strategy, utilizing the Structure-Conduct-Performance (SCP) paradigm of industrial organization. Based on several interviews and secondary data, this study summarizes the key reasons why Tesco could not develop a localized merchandising strategy. In particular, it investigates Tesco's partner selection, store size and format, centralized merchandising authority, and private brand-focused (PB-focused) merchandise assortments. The findings and suggestions of this study will help retailers internationalize as well as help those who want to thrive in the Japanese market.

Keywords:

Keywords: localized merchandising, Tesco, industrial organization paradigm, retailing, Japan

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1. Introduction

Over the past few decades, internationally recognized retail chains, such as Walmart, Carrefour, and Tesco, have achieved tremendous growth and posed a threat to local retailers in host countries. In spite of their significant successes in many international markets, they have also decided to withdraw from countries such as Germany, South Korea, and Japan (Arnold and Fernie, 2000; English, 2016; Ghehard and Hann, 2005; Suh and Howard, 2009) after failing to establish a clear competitive advantage.

Existing literature has discussed that the success or failure of global retailers depends on their capability and willingness to adapt to local markets (Burt *et al*., 2003; Dawson and Mukoyama, 2014; Dupuis and Prime, 1996; Wood *et al*., 2016; Yoder *et al*., 2016). Even though the factors and antecedents of the success or failure of global retailers have been widely studied, there is limited literature on the localized merchandising (MD) strategy of global retailers.

For example, Tesco, one of the giant global retailers in U.K., entered the Japanese market in 2003, after Carrefour and Walmart. Before Tesco's entry, these two giant global retailers had struggled in the Japanese market and faced losses for several years (Haddock-Fraser *et al*., 2009). Surprisingly, in spite of the accumulated international experience and knowledge especially from South Korea which is geographically and culturally closest to Japan, Tesco finally ended up exiting the Japanese market after eight years in business. However, very few studies have investigated the story of failure of Tesco in Japan.

Against this background, this study aims to investigate reasons and factors of Tesco's failure in the Japanese market through the lens of localized merchandising strategy, utilizing Structure-Conduct-Performance (SCP) paradigm of industrial organization. The SCP paradigm is a management tool which explains how the characteristics of the market structure of a firm's industry influences market conduct (i.e., firm strategy) and the performance of the firm (Bain, 1968). Information and data used in this study have been obtained from both primary and secondary sources. Primary data are from interviews with

employees of some companies in the Japanese food retail market. Secondary sources include annual reports, reputed Japanese-language newspapers and business journals, as well as academic articles.

Drawing on retail merchandising strategy, the findings and suggestions of this study will guide other international retailers or domestic retailers who plan to enter international markets with internationalization strategies. In addition, this study will also provide useful lessons for global grocery retailers who are entering the Japanese market.

2. Localized merchandising in retail internationalization

The internationalization of retailing is considered as an ongoing process (Alexander and Myers, 2000), in which retailers have valuable opportunities to learn about the ways of successfully expanding their operations in foreign markets (Bianchi and Ostale, 2006; Palmer and Quinn, 2005). The selection of foreign markets is influenced by their similarity to home country characteristics, as well as growth opportunities. That is, international retailers consider the cultural distance, geographical distance, and psychic distance while selecting foreign markets they want to enter.

Many studies have discussed the different approaches of international retailers (Alexander and Myers, 2000; Helfferich *et al.*, 1997; Salmon and Tordjman, 1989). Salmon and Tordjman (1989) addressed two internationalization strategies: global strategy and multinational strategy. The global strategy refers to the retailers' decision to replicate their core business concept in other countries. In the multinational strategy, retailers modify their core business concept (or format) to meet local market conditions without sacrificing its basic elements.

Comparing the two different approaches, some researchers believe that it is easier for a retailer with unique offerings to expand its business in new markets in a standardized manner than adaptation (Salmon and Tordjman, 1989; Treadgold, 1990). However, others insist that adapting to the local culture, taste, and purchasing behavior is essential if international retailers are to achieve a better performance in each market (Baek, 2014; Burt and Mavronmmatis, 2006). In practice, the adaptation strategy is frequently considered as more effective for international retailers who are entering global markets and setting up their business there. Interestingly, Treadgold (1990) suggested a transnational strategy as a type of hybrid strategy, which is a mix of standardization and adaptation strategies. The

mixed strategy needs to be modified at the time of entry, as well as at each stage of operations to deal with the standardization-adaptation issue (Baek, 2005).

To implement the adaption or hybrid strategy, global retailers must adopt flexible organizational arrangements that permit the use of country-specific knowledge (Sashi and Karuppur, 2002). The specific knowledge enables retailers to develop localized merchandising. Merchandising refers to a series of retailers' activities to plan merchandise assortments, select suppliers, purchase merchandise, set selling price, and devise sales promotion. In this study, we use the term "localized merchandising strategy" to refer to the retailers' strategy of localizing their merchandising activities.

We posit that retailers who are aware of the importance of the localized merchandising strategy prioritize to build attractive merchandise assortments. To this end, the localized merchandising strategy should consider carefully the operation of stores through optimal store size and format, selection of local partners including suppliers, planning for merchandise assortments, and design of the merchandising organization within host countries. This suggests that the localized merchandising strategy in international retailing should include the entire organizational design, rather than just the merchandise assortment plan for the local market. Retailers with an effective organization design can develop cooperation between the merchandising and store divisions for better decision making on merchandising (Takashima and Kim, 2015), encourage retail buyer innovativeness through optimal design of management control systems for better purchasing performance (Kim and Takashima, 2016), and manage their suppliers in order to receive relationship-specific investments (Takashima and Kim, 2016).

3. Conceptual framework

3.1 Research context

Food retailing in Japan is highly developed and strongly resistant to competition from foreign food retailers. All foreign grocery retailers like Carrefour, Costco, Walmart, and Tesco attempted to introduce a new consumption culture to the Japanese food/grocery market. For example, Carrefour brought its hypermarket format to Japan in 2000, but from the Japanese consumers' viewpoint, it was not much different from the Japanese general merchandise stores. In fact, the domestic food/grocery retailers were so well entrenched that it made it difficult for the Western retailers to penetrate the Japanese market. It is no

exaggeration to say that domestic retailers have been dominating the Japanese market. Not being able to achieve expected results, Carrefour had to finally exit Japan in 2005.

The Japanese domestic retailers are more sophisticated in terms of handling technology and know-how of perishable food, such as fishes, fruits and vegetables, and meat, than the Western retailers because they have to satisfy the needs of Japanese consumers who are sensitive to the freshness and quality of these foods (Baek, 2014). When Walmart entered the Japanese market, they realized that the procurement capabilities and reinforcement of handling know-how in perishable food would be critical to success in the Japanese market after witnessing of Carrefour's struggling in Japan. Walmart believed that having a local partner might be better to operate its business in Japan due to its lack of knowledge of the market. At that time, Seiyu, one of the largest retail chain stores who developed Muji as its private brand since 1980, looked for business partners to overcome its financial issue. Meanwhile, Walmart evaluated that Seiyu was one of the leading retailers in terms of better understanding of the local market, local consumers, and handling know-how of perishable food.

Given this, Walmart first acquired a 6.1% stake of Seiyu, and in 2005, acquired a majority stake, making Seiyu Walmart's subsidiary. Walmart proceeded to acquire the remaining shares, and Seiyu finally became a wholly-owned subsidiary of Walmart in 2009. It was ironic that although Walmart acquired Seiyu as a local partner in Japan, it struggled to enhance store operations and merchandise procurement capabilities by fully leveraging its global networks and acquiring a competitive advantage.

3.2 Research questions

Tesco, the most successful retailer in U.K., entered the Japanese market in 2003. Before entering Japan, Tesco accumulated localization experiences and knowledge, especially from South Korea, which is geographically and culturally the most similar to the Japanese market. Their business in South Korea was stable at that time. Tesco must also have analyzed and researched the previous success and failure of some global retailers (Palmer, 2005). Although Tesco wanted to provide a better shopping experience and more valuable products to Japanese consumers, they met the same fate as their predecessors. Tesco withdrew from Japan in 2011.

This raises the following research questions: 1) How does the Japanese retail industry differ from that of other countries? In other words, what are the unique structural features

of the Japanese retail industry?; 2) How did the characteristics of the Japanese retail industry impact Tesco's operations in Japan? In other words, how did Tesco develop strategies to compete with the Japanese retail industry?; and 3) How was Tesco's performance in Japan? To respond to these research questions, this study applies the SCP paradigm based on the industrial organization. The SCP paradigm is a management tool which explains how the characteristics of the market structure of a firm's industry influences market conduct (i.e., firm strategy) and the performance of the firm (Bain, 1968). However, it limits the research scope to one retail company, focusing on Tesco's store operations, its selection of local partners, merchandise planning, and the design of its merchandising organization during its eight years in Japan.

Figure 1. The conceptual framework

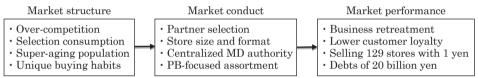| Market structure	Market conduct	Market performance
· Over-competition · Selection consumption · Super-aging population · Unique buying habits	· Partner selection · Store size and format · Centralized MD authority · PB-focused assortment	· Business retreatment · Lower customer loyalty · Selling 129 stores with 1 yen · Debts of 20 billion yen

Figure 1, which draws on the SCP paradigm, shows the research framework used to suggest the key reasons for Tesco failing to develop retail organizational capabilities for the localized merchandising strategy and finally exiting. First, in order to focus on the analysis of the failure of Tesco Japan, the history of Tesco Japan and its market performance is summarized. Then, the market structure of Japan which has four major factors—over-competition, selection-oriented consumption, super-aging population, and unique product buying habits—is discussed. Finally, Tesco's efforts to establish its business in the Japanese market, through decisions on partner selection, store size and format, centralized merchandising, and private brand-focused (PB-focused) merchandise assortment are analyzed.

4. History and performance of Tesco in Japan

Tesco entered the Japanese market by acquiring C2 Network, a discount retailer, for 32.8 billion yen in July 2003. In order to expand its business in the Japanese market, Tesco invested a further 20 billion yen, and officially changed its name to Tesco Japan in September 2007. Although Tesco actively invested and extended its business in Japan, it finally decided to exit from the Japanese market in August 2011.

When Tesco entered the Japanese market, it received huge media attention due to the scale of its M&A with local retailers. In order to expand its business scale, in August of 2004, Tesco started M&A with Frec holding twenty-five stores, where operates in Chiba. In October, 2005, Tesco acquired a medium-sized retailer, Tanekin, which had eight stores in Tokyo. Because of the active expansion of business through mergers and acquisitions, Tesco Japan had one hundred five stores by February 2006 (*Syukan Diamond*, 8 October, 2011). Additionally, Tesco developed and diversified its own store format. They opened the first store of Tesco Express, which is synonymous with convenience-based, small-sized supermarkets, in April 2007. Then, it opened Tesco, a new supermarket brand, in December 2009.

Even though Tesco aggressively operated its business in Japan, it announced its decision to exit the Japanese market in August 2011. The reason they exited from the Japanese market is similar to the reason due to which Carrefour (entered in 2000, but exited in 2005) left and also the reason for Walmart struggling (entered in 2002). All of them encountered a concrete barrier in the Japanese market. When Tesco declared that it was closing its Japanese business, it was operating 129 stores in metropolitan areas around Tokyo, and its revenue reached 50 billion yen (*The Nikkei*, 1 September, 2011a).

It had been said that it expected to get 20-30 billion yen by disposing its assets. However, it was hard to find a company who was interested in taking over their stores. There were several reasons for this. For example, prospective buyers found that the store size and format were unsuitable for their business model. More than half its stores were running deficit operations. Further, Tesco suggested during the sale negotiations that the buyer should absorb all 1,900 employees of Tesco, which included part-time employees. After struggling to sell its business for some time, it finally sold its business to AEON for just one yen (*Business Journal*, 2012). Further investment of five billion yen for rebuilding the supermarket business was one of the terms of the sale agreement reached between the two companies. In addition, Tesco agreed to pay the debt of 20 billion yen accumulated by Tesco Japan before finalizing the sale deal with AEON.
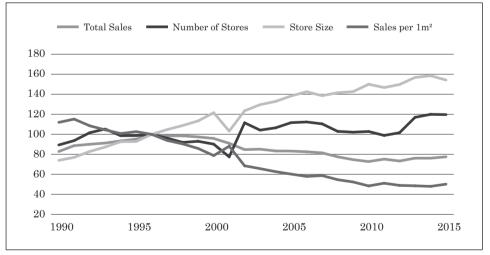
Tesco Japan received huge attention before entering the Japanese market and on its exit, but interest in it was muted during the eight years it operated in Japan. The Japanese people expected that Tesco would exit the Japanese market sooner or later due to the market barriers (i.e., the structure of the Japanese market, unique consumers' preference, and purchase behaviors) that had led to Carrefour's retreat and left Walmart struggling with its
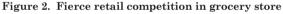
business due to depressed demand. However, we conclude that the main failure of Tesco Japan was not only the unique structure of Japanese market, but also its inability to exhibit organizational learning, coupled with a misunderstanding of the local consumers. The rest of this study addresses these main factors for Tesco Japan's failure.

5. The characteristics of market structure

5.1 Over-competition in the retail market

The excessive competition among retailers is often considered as one of main characteristics of the Japanese retail industry. Tamura (2008) argued that it is not difficult to predict the outcome of the intense competition among retailers in Japan. Those who build organizational capabilities to create value innovation would be winners in such a market. It is also known that supermarkets have reached the maturity stage in the retail life cycle. That is, the market is extremely saturated and fragmented. However, supermarkets mainly carry groceries and food; thus, it is hard to believe the prediction about the fading away of supermarkets. Given this, differentiation at the store level is strongly recommended and indispensable to survive the competition.

Figure 2. Fierce retail competition in grocery store

Note: 1. Data is based on sales statistics of Japan chain stores association
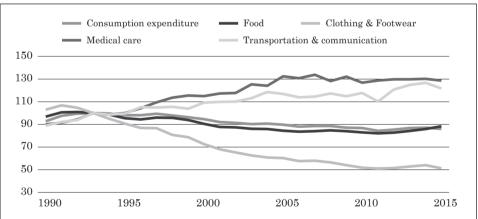(https://www.jcsa.gr.jp/public/statistics.html/).
   2. The index of each year is relative percentages when we set the value of the 1996 sales volume (the peak of total sales volumes of members) and other retail parameters as 100.

The data drawn from member firms of the Japan chain store association depicts the

severity of the competition among supermarkets (see Figure 2). If we set the value of the 1996 sales volume (16.98 billion yen) and other retail parameters as 100, the value represents 85.2% of sales, 65.6% of sales per $1m^2$, 104.2% of numbers of stores, and 129.6% of the store size in 2003—the year when Tesco Japan entered the Japanese market. However, when Tesco Japan announced its exit from the Japanese market in 2011, the size of stores had increased by 146.8%, but sales per $1m^2$ had dropped to 51.3% of the 1996 levels. From these figures, we can easily infer the uphill struggle Tesco Japan had to face in order to just survive.

5.2 Selective consumption

Figure 3 shows the variation in monthly expenses on diverse consumption categories, based on the total monthly expenses of households having two or more people. In Figure 3, the average monthly expense value of 335,246 yen in 1993—the year with the highest average monthly expenses—are taken as base 100. In 2003, the total expenses had dropped by 9.7%; those on food and clothing & footwear had decreased even more drastically by 13.9% and 37.4%, respectively. In contrast, medical care and transportation & communication expenses increased by 25.4% and 13.2%, respectively.

Figure 3. Yearly average of monthly disbursements

Note: 1. Data is based on family income and expenditure survey announced by statistics bureau in ministry of internal affairs and communications (http://www.stat.go.jp/data/kakei/longtime/index.htm#longtime).
　　　2. The index of each year is relative percentage when we set the value of 1993 (the highest average monthly expenses) and other parameters as 100.
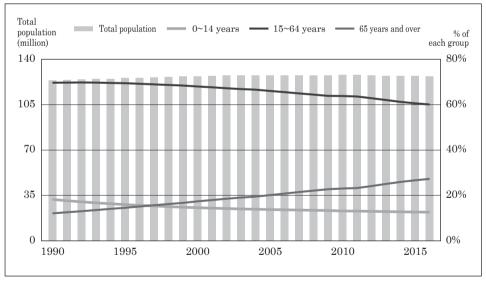　　　3. The data is not including agricultural, forestry, fisheries workers' households.
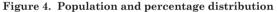　　　4. Tabulated households in 1967-1984 include households additionally surveyed in cities with prefectural office. Gas is included in 1963-1966. Sewerage charges are not included in 1963-1984. Medicines include health fortification since 1993.

It shows a continuous drop in the expenses. By 2011, total expenses had fallen 15.6 % from the 1993 levels; food and clothing & footwear fell by 17.9% and 48.9%, respectively. However, the expense on medical care has witnessed a consistent increase. By 2015, it was 28.7% more than the 1993 value, whereas the expense on the transportation & communication had increased by 21.7%. Given this data, the market size of food items—in which Tesco Japan was a new player—has been shrinking while the size of the medical care market has been growing much faster. Hence, apart from Tesco Japan, it is vital for Japanese retailers to reflect on this market trend when practicing merchandising to differentiate themselves from their competitors.

5.3 Super aging society

When Tesco Japan entered the Japanese market in 2003, the Japanese population was increasing gradually. The drop in population after 2010 (nearly 128,057,000) was not seen as a big concern for businesses and the economy. In contrast, multinational corporations are required to more deeply understand the issue of aging population in Japan.

Figure 4. Population and percentage distribution

Note: 1. Data is based on population census announced by statistics bureau in ministry of internal affairs and communication (http://www.e-stat.go.jp/SG1/estat/NewList.do?tid=000000090001).
      2. Data is announced in October of each year.

According to Figure 4, those under 14 years and above 65 years accounted for 14% and 19% of the population, respectively, in 2003. In 2011, the share of those under 14 years in

the population had fallen to 13.1% and that of people above 65 had increased to 23.3%. It shows the shrinking of the working population, which constitutes the main consumer group targeted by retailers. More importantly, Japan is an aging society, with one fourth of the population aged 65 years or above. As shown in Figure 3, the elderly have a tendency to consume lower quantities of food and clothing & footwear, spending more on health and medical care. Consequently, satisfying the elderly, who have purchasing power and a regular stream of expenses, has become the key to survival in Japan.

5.4 Unique buying habits

The unique habits of the consumers are linked to their needs and wants. It would be summarized as twofold of consumers' needs and wants for supermarkets. First, Japanese consumers are very sophisticated, not only in terms of the taste of fresh food, but also in demanding quality, newness, and variety. Many Japanese consumers visit supermarkets daily to purchase fresh and high quality merchandise. In particular, the elderly often wait for stores to open so that they can purchase fresh food before others arrive. Second, the Japanese consumers demand variety in merchandise. They are easily bored with the same merchandise and layout. In other words, the Japanese consumers want to purchase and try newness. In line with this, retailers should actively carry and treat new merchandise in stores, and are required to provide a range of differentiated merchandise.

6. The characteristics of market conduct

6.1 Partner selection

Tesco targeted consumers in metropolitan areas and wanted to operate small-sized supermarkets, to avoid the path taken by Carrefour and Walmart, who operated hypermarkets. To enter the Japanese market, Tesco tried to localize by partnering with a local company, C2 Network, in 2003. C2 Network, the cash cow among discount stores, had an income to sales ratio of 7%. C2 Network operated its stores in metropolitan areas. In order to acquire the advantages of C2 Network, Tesco selected it as the local partner. However, choosing a discount retailer was considered as one of the factors leading to Tesco's failure (*Syukan Diamond*, 8 October 2011). It has been remarked that Tesco, a supermarket retailer focused on groceries and fresh food, should have selected a retailer with a concept similar to it as its partner.

Apparently, there were differences between the two partners on store opening strategy. C2 Network was focused on a low-price strategy and preferred to open stores at locations that had lower rent, even if it was inconvenient to reach them. C2 Network could maintain its price competitiveness by saving on rent. Even if the location had lower population density, there was a higher probability of expanding its trading area because of its efficiency achieved through lower opening and operating costs of discount stores. For this reason, they did not pay much attention to the standardization of store size and their stores were of different sizes. In contrast, supermarkets like Tesco typically have a narrow trading area; therefore, it is better to be located in areas with higher population density. Moreover, operating stores of different sizes proved difficult for Tesco as it was used to standardizing the store size and operating them centrally from its headquarter. This led to poor efficiency in operating stores.

Additionally, the merchandise assortment strategy of the two companies varied. C2 Network carried inventories that were unsold at wholesalers, non-branded merchandise, or merchandise with a short use-by date to offer cheaper prices to consumers; thus, they could survive during the period of deflation. Given this, C2 Network focused mainly on groceries rather than fresh food. Not being able to handle fresh food in a market that required differentiation in supermarket for success was said to be the main reason for Tesco's failure. Finally, Tesco Japan struggled due to the disagreement with the top management of its partner on prioritization relating to store operations and the high turnover of talented employees to its competitors, which worsened the poor performance.

Generally, M&A in retail sector involves improperly-run enterprises. However, Tesco took over a successful local partner and it was expected that Tesco would have an advantage in expanding its operation in Japan. However, Tesco failed to build a competitive advantage (*Nikkei Marketing Journal*, 5 September 2011b). Moreover, given the long deflation after the collapse of the bubble economy in 1991, value for money had been emphasized by giant retailers such as AEON. Therefore, the low-price strategy of Tesco was unable to attract the Japanese consumers.

6.2 Store size and format

Tesco Japan aggressively expanded the number of stores over the short term. Since they targeted metropolitan dwellers, Tesco actively took over additional supermarket companies in metropolitan areas (*Nikkei Marketing Journal*, 5 September 2011a). Tesco Japan acquired

25 stores of Frec and eight stores of Tanekin in 2004 and 2005, respectively. In 2010, Tesco Japan was running 137 stores. In line with the expansion of stores, Tesco Japan also opened new formats. These included Tesco Express and Tesco, which were started in April 2007 and December 2009, respectively. When Tesco Japan announced its exit from the Japanese market, it had 129 stores. Of these, it had Tsurukame 76 stores, the representative store type of C2 Network; 30 stores of Tesco; 10 stores of Tesco Express and 13 stores of other types.

The aggressive M&A and the development of new formats of stores had the advantage of achieving economies of scale, expanding market coverage, and responding appropriately to the variety of needs of consumers over the short term. However, as Tesco Japan focused mainly on achieving scale in a short-time, it also had rather negative effects on the system of store operations, such as inconsistency of store size and merchandise assortments across stores (*Nikkei Marketing Journal*, 5 September 2011b). For instance, the store size ranged from 70 m^2 to 800 m^2. Under this situation, it is hard to realize the anticipated scale merits by standardizing store operations from the headquarter.

"Regardless of the retail format, it will be hard for retailers who emphasize economies of scale by operating chain stores underpinned by standardization to achieve great efficiency from diversified store size." (from an interview with the CEO of a retail company)

The small-sized stores on which Tesco focused have limited spaces; thus, the merchandise on the shelves is also limited. Tesco Japan was not much attractive to customers due to its lack of merchandise assortments—especially brand new merchandise— and no differentiation in its merchandise assortments, when compared with its competitors. Additionally, the store expansion strategy had a negative effect on store branding. After 2007, Tesco planned to strength the format of Tesco Express, which was identical to what it ran in U.K., and Tesco, which is new store concept. Yet, the store branding strategy of Tesco did not succeed and the store name remained Tsurukame. From the standpoint of consumers, having an unified store image of Tesco Japan is considered difficult.

6.3 Centralized merchandising authority

What makes an international retailer suffer in the Japanese market? In addition to the high labor cost and rent, the unique culture and practices of transaction (*The Nikkei*, 1

September 2011b) cannot be ignored. In particular, it is a fact that grocery stores in Japan are extremely competitive, when compared with those in European countries; therefore, profits and profit margins are relatively low. Therefore, the lifecycle of groceries becomes short. In order to survive the competition, manufacturers resort frequently to new product development, which further shortens the product life cycle.

Retailers need to display popular merchandise without running out of stock and replace non-popular merchandise with better selling merchandise on their shelves. This is a way to satisfy the needs of Japanese consumers, who require both differentiation and newness in merchandise. In order to meet consumers' needs, it is required to achieve significant localization of merchandise and provide attractive merchandise assortments by closely cooperating with suppliers.

However, when visiting one of Tesco Japan's stores, fresh fish products like sashimi were out of stock at noon (*Nikkei Marketing Journal*, 5 September 2011b). This stock-out happened because headquarter reduced the quantity of fresh fish supplied based on the forecast of rain for the next day. In Tesco, the headquarter had the authority to make merchandising purchase decisions. In this situation, even if store managers want to order additional merchandise based on demand in the store, they cannot get it because the headquarter decides the quantity of merchandise distributed to each store the day before actual delivery.

Tesco Japan also employed information systems which were utilized in other countries in which they operated stores in 2008 (*Nikkei Marketing Journal*, 5 September 2011b). Employing information systems created centralized management of many functions, including order fulfillment. This centralization hands over administrative power for merchandise display and store layout, selling price, and order quantity of merchandise, as well as the choice of merchandise and/or suppliers, to the headquarter. In Japanese practice, it is essential for a store to rapidly respond to local rivalries by scrutinizing the merchandise that had sold well and the prices in the store. However, once the authority of the store is restricted, it is hard to react quickly and provide satisfactory merchandise and price, or changing shelf allocation in tune with local needs and competition.

"It can vary by firm. However, by checking on prices and merchandise of competitors every day, it is quite common in a localized store operation to change merchandise, prices, and promotions to attract customers. Additionally, because this requires a quick reaction, the store

manager is given to certain degree of authority to make decisions and handle the urgent issues without reporting to the headquarter." (from an interview with a grocery store manager)

As opposed to the decision-making system of Tesco Japan, Ito-Yokado recently gave the authority to placing an order for merchandise to not only its store manager but also employees in stores. It did this in order to provide localized merchandise assortments (*Nikkei Marketing Journal*, 22 June 2015). In addition, the single biggest factor for Yaoko achieving growth in both sales and profits for 27 consecutive years is localization.

"The acceleration in the aging of society is guaranteed to increase the number of localized stores. In order to be localized, stores need to empower their employee, by involving them in planning and taking their suggestions on store management; this leads to a competitive advantage for the stores." (from an interview with a grocery store manager)

6.4 Private brand-focused merchandise assortment

Tesco Japan was quite active in the development of private brands (PBs) (*Nikkei Marketing Journal*, 18 August 2010). There are two types of PB development—low price-oriented PBs and high quality-oriented PBs. In addition to the two types of PBs, policy of merchandise assortments was reinforced by cheaper national brands. Yet, attractive merchandise assortments were not a priority for Tesco Japan. They focused mainly on low-priced merchandise with some core PBs.

Tesco Japan did not seem to realize that the awareness about, or preference for, PBs is quite low among the Japanese consumers, compared with that among consumers in the U.K. In Japan, there are few supermarket retailers that have over a 10 percent share of PB merchandise in total sales. The fact that consumers' national brand (NB) loyalty is strong and manufacturers offer aggressive price reduction on NBs further explains the lower awareness about PBs among the Japanese consumers.

For the Japanese consumers, both price and quality benefits are significant; therefore, it is easily conceivable that a lack of differentiation in merchandise assortments and restricted merchandise choices of Tesco Japan caused it to struggle for existence in Japan (Kim and Baek, 2011). On the other hand, Costco has been popular and famous in Japan due to the attractive merchandise assortment through successful local and global sourcing.

"As a retailer, the existence of differentiated, unique merchandise which consumers are willing to pay for is critical. A retailer is meaningless if he/she offer merchandise which consumers do not want to buy and pay for." (from an interview with a management planning manager)

The personal interviews made it clear that newness, popularity, quality, and freshness of merchandise are the main considerations for Japanese consumers. On average, the Japanese consumers usually visit a supermarket three to four times in a week. Some visit the supermarket on a daily basis. Furthermore, as consumers have a strong inclination to try something that is brand new, manufactures respond by actively developing new products. Japanese consumers are easily bored with retailers who do not continuously improve merchandise and run store promotions; in most such cases, they do not visit such a store again. This partly explains why Walmart has been struggling in Japan. Thus, specifying the local consumers' needs and wants and providing attractive assortments are the most important factors to satisfy consumers, particularly in Japan.

7. Conclusion and discussion

This study investigated Tesco's failure in the Japanese market and examined the key reasons why Tesco couldn't develop the localized merchandising strategy. This study contributes to the current literature of retail internationalization process by using the industrial organizational approach and addressing the concept of the localized merchandising. It examines key factors which retailers should consider when they internationalize. Our findings help retailers take advantage of the knowledge that can be gained from failure.

This study emphasizes that retail strategies must respond to market structures, consumers' needs, employees' characteristics and personalities, competitor behaviors, unique transaction practices with suppliers, etcetera, in the market that retailer enters. In other words, adaptation toward the local market is vital. Even if Tesco truly understood the characteristics of the market structure in order to provide attractive merchandise assortments, however, it was unable to develop organizational capabilities for the localized merchandising strategy.

In analyzing the failure of a global retailer, the focus is commonly on market conduct,

and less attention is paid to analyze the key reasons why it could not develop retail organizational capabilities for executing the localized merchandising strategy after understanding the market structure and market performances. This suggests that it may be more beneficial in future research to focus on whether a global retailer holds organizational capabilities, including partner selection, the centralized merchandising authority and PB-focused merchandise assortments, as well as the store size and format to develop the localized merchandising strategy.

Apart from Tesco Japan, the performance of a global retailer can be viewed as a continuum of the internationalization process. The performance is often described with either of the following two keywords: success and failure. The choice of strategies leads a global retailer to ascertain the success or failure of its operations in foreign countries.

With regards to failure, majority of research picked up global retailers' withdrawal from a foreign market, which has been evaluated in mostly negative, but sometimes also in positive terms. Even if a global retailer's withdrawal from a foreign market is described as a failure to adapt to local market conditions, it can still be seen as a lesson that can benefit the company when setting up future operations in other foreign countries (Palmer and Quinn, 2005). In this sense, the failure can also make a positive contribution to the internationalization process. At the very least, the experience of a retailer's withdrawal can be an important step leading to a development of new internationalization strategies (Burt *et al.*, 2002; Jackson *et al.*, 2004).

Given this, Tesco Japan's case provides us useful lessons. Tesco's significant success in the South Korean market and knowledge learnt from the Carrefour and Walmart's experiences did not lead to the Tesco's success in Japan. The reasons for the failure are summarized as following.

First of all, how did Tesco analyze and define the Japanese market? As Japan has a significant market size in terms of purchasing power, the Japanese market is often considered as a potential market for global giant companies. However, consumers' spending on food has been decreasing continuously because of a rapidly aging population. Despite the decrease in consumers' spending, they are extremely choosy about fresh food, freshness of merchandise, differentiation of merchandise; further, they demand deep and wide assortments. Even Japanese companies, who are already aware of consumers' needs, can fail if they do not meet such consumers' needs. Tesco Japan had a competitive advantage in groceries and frozen food, rather than in fresh food. However, it was not a leading company

in Japan. Considering fierce competition in Japanese supermarket industry, some said that entering the Japanese market with a supermarket format itself led to Tesco's failure although it did make a huge investment and developed strategic plans in order to overcome various pitfalls.

Second, were the strategies of Tesco to meet the Japanese consumers' needs appropriate? According to Kim and Baek (2011), an attractive merchandising assortment is the most important factor leading to consumers' store loyalty in Japan. Japanese consumers frequently visit a retail store in pursuit of unique and differential merchandise. Here are some tips for global grocery retailers considering entry into the Japanese market. Retailers must develop differentiated, attractive merchandise assortments, particularly in fresh food. In pursuit of differentiated, attractive merchandise assortments, they should build concrete relationships with local suppliers; invest on localized store operations underpinned by store cooperation; and devise organizational structures for better organizational decision-making processes that respond to the local market.

Carrefour and Tesco withdrew from the Japanese market. Walmart seems to be still struggling with the Japanese market. In contrast to these global retailers, Costco has steadily expanded its market size in Japan due to the exclusive merchandise assortment via well-balanced local and global sourcing. Consequently, retailers should remember that they need to source merchandise as agencies who offer it in order to meet their customers' needs and wants. It is not a good idea for retailers to source merchandise that they want to sell.

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