CHAIN GOVERNANCE MODELS IN RETAILING: CAPABILITY DEVELOPMENT AND PATH DEPENDENCY.

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October 2007

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Abstract

We identify and study two retail chain governance models and the environments favoring each. Firms pursuing the "Individual Store Oriented Form" (ISOF) hold that nurturing store level resources and capabilities is the key for success. In contrast "Chain Organization Oriented Form" (COOF) firms focus on developing integrative chain level capabilities and resources. These governance models shape the firm's direction, the process of resource acquisition and capability development. Using historical data we analyze retail firms' behavior during two historical juncture points when a shift in environmental conditions necessitated a change from the ISOF to the COOF governance model. We provide a path-dependency explanation for why some retail firms continued to practice the ISOF model in the face of evidence of its ineffectiveness.

Key Words: Path dependency; retailing; governance models; chain store retailing; retail history.

1. Introduction

We study the persistence of a retail chain governance model we label "Individual Store Oriented Form" (ISOF). Firms practicing this model adhere to the retail business philosophy that store level resources and capabilities hold the key to success. ISOF firms place little value on the development of chain level capabilities and systems and eschew making investments in their development. They rely on the knowledge held by local managers, both tacit and formal, and allow store managers a high degree of decision autonomy. This autonomy is not monitored or controlled by higher level managers. Firms pursuing the ISOF model view the firm as a collection of stores where growth and success is determined by how well each individual store competes in its local area. Where chain level institutions are established and resources invested in firm level capabilities these are geared to the support of the individual stores. They particularly avoid investing in control and monitoring systems interfering with store managers' autonomy and make limited use of supply, logistic and distribution systems requiring a close alignment of the stores to the firm. Finally, ISOF firms display a "local orientation". Each store attempts to exploit the sales potential in its "locality" .

We contrast the ISOF with the alternative governance model, the Chain Organization Oriented Form (COOF) where attention is focused on the chain. The firm holds that individual stores are "outlets" of the firm implementing its policies. Here the key to achieving competitive strength, growth and profitability is considered to be the development of chain level capabilities, systems and institutions. These will generate firm wide efficiencies, cost and scope economies, facilitate taking advantage of business and technology opportunities and secure the effective implementation of initiatives and strategies across the chain. COOF firms are often proactive, molding rather than merely adapting their supply and demand environments. COOF firms invest in systems designed to integrate the stores into the chain. These firms may grant decision autonomy to store managers but it is always defined, monitored and controlled.

These governance models are of central importance because they determine the firm's direction and shape the nature of its capability development process. Firms practicing each of the two governance models focus on different sets of problems, challenges, and growth and profit opportunities. These, in turn, determine the types of resources acquired, capabilities developed and firms' response to problems and opportunities. The notion of a development trajectory captures the dynamic, evolutionary aspect of the process.

The ISOF model is associated with relatively simple, informal, low technology and low cost management structure. It relies on local management capabilities rather than complex systems and technologies. Therefore it is often the first model used by young retail firms. The ISOF model operates well in environments where the market is fragmented: consumers shop locally, their outreach limited, supply and logistics largely handled by local firms and competition localized. Also, it fits situations when retail management technologies are simple and underdeveloped. Historically, these conditions were prevalent in North America and Western Europe only a few decades ago. At present they are typical in emerging economies at the early stages of retail development.

The COOF model is associated with more complex, formal, high technology and costly retail management structures. It is associated with heavier investments in infrastructures and with the use of more robust, sophisticated and complex capabilities. It makes better use of state of the art technologies and systems. The COOF model operates best when the environmental conditions favoring the ISOF change: markets become less fragmented, consumers' shopping scope becomes wider; supply and distribution firms consolidate and they operate over wider territories. Also, it better fits situations when management methods and technologies become more powerful, sophisticated and complex. Finally, it is appropriate when the nature of competition changes, from competition among individual stores in a locality into competition among large retail firms operating over a wide geographical area.

Firms need to adapt their governance model to changes in environmental conditions. When the new conditions favor the COOF model the firms still practicing the ISOF model will find it increasingly difficult to prosper and effectively compete. On the other hand COOF firms will incur high costs and inefficiencies when operating in conditions favoring the ISOF model. The retailing scene is replete with examples of firms persisting in practicing their governance model in face of evidence that it is no longer effective. These situations are of interest not only to retail historians and retail theorists but also to present day retail management and strategy. For example, international retailers operating in emerging markets often encounter conditions favoring the simpler, low cost and locally oriented ISOF model rather than their transferred COOF model.

The question we study in this paper is why firms continue to practice the ISOF model in face of evidence that the conditions favoring it have changed. We provide a path- dependency, "lock-in" explanation for this phenomenon. (Booth, 2003; Teece et. al., 1997; Schoenberger, 1997). We argue that the firm's past history exerts a constraining effect on its present behavior

(Penrose, 1995). The business philosophy, strategies, capabilities and institutions that served ISOF firms well in the past are no longer relevant. But they continue to shape how ISOF firms perceive the new conditions, the problems and opportunities, the solutions they contemplate and their actual responses. Also, managers may resist the new model because they are committed to the old. ISOF firms become locked-in into irrelevant concepts and strategies and into inefficient practices and responses .They find it difficult to break with the past, reorient their behavior, reinvent the firm and set on the path of developing the new capabilities and institutions required in the new environment. While our interest in this paper is in the shift to COOF, our concepts and framework can be applied to the reverse scenario of COOF firms facing conditions requiring a reverse shift to an ISOF model.

These issues can be studied in three contexts. The first is an analysis of firms' behavior during historical juncture points when a shift in market conditions necessitated a change of the governance model. The second is researching the evolution of retail firms. At the early stages of their life cycle young, founder-owner managed firms typically practice the ISOF model. It is comparatively simple, low cost and heavily relies on the abilities and resources of the retail entrepreneur. As the environment changes and these firms expand geographically they will face conditions favoring the COOF model. The shift to the new model is often traumatic requiring reorganization, replacement of most practices and the development of new capabilities and systems. Thirdly, these issues can be studied in the context of retail internationalization often involving a move by retail firms from one set of market conditions to a different one. Our interest in this paper is in studying these issues in an historical context. Using historical data we analyze UK supermarkets and US department stores behavior during two historical juncture points when a shift in environmental conditions necessitated a change from the ISOF to the COOF governance model.

The phenomenon we study may be easily confused with the centralization /decentralization (CD) concepts. Therefore the differences are discussed in this paper. The CD concepts relate to two organization structure/design options. Organization and strategy researchers study the conditions where each design is appropriate and the impact of CD structures on performance (e.g. Ulrich and Weiland, 1980; Olson *et al.,* 2005). Retail geographers discuss CD in the context of their study of tacit /local knowledge and knowledge codification at the firm center (e.g. Wood, 2002). Our governance concepts relate to a much more fundamental characteristic of the firm. They encompass the firm's retail/business philosophy, coordination among its components and the level of monitoring and control. These elements are anchored in the firm's traditions and institutions.

Governance models shape the firm's long term direction, the process of resource acquisition and capability development, and the firm evolution. In the body of the paper we discuss in detail the relationship between our governance models and the CD concept. We argue that because ISOF firms eschew the establishment of firm level control and coordination capabilities they are obliged to pursue an extreme (“full and complete”) version of the decentralized organization design. In contrast COOF firms possessing these capabilities are free to choose between a centralized or decentralized design. Indeed a growing number of COOF retail firms combine the merits of centralized and decentralized designs allowing what we label a “controlled and limited” decentralization.

Our use of the two historical examples positions our study within the broad research stream studying retail history (e.g. Bucklin, 1972; Jefferys, 1954; Zimmerman, 1955; Longstreth, 1997; Alexander and Akehurst, 1999; Benson and Shaw, 1992; Benson and Ugolini, 2003). Our study differs from these in emphasizing the process of resource and capability development (Raff, 2000) drawing on concepts and findings developed by researchers in the strategy, organization and evolutionary economics areas. Specifically, our theoretical perspective is grounded in the research streams studying the role of resources and capabilities in shaping a firm’s evolution, dynamic capabilities and the relationships between governance structure and capability development.(e.g. Jacobides and Winter, 2005; Teece *et al.*, 1997). We use historical data to validate our concepts and support our hypotheses.

The paper is organized as follows: we start by discussing three research streams most closely relating to our concepts. We then discuss the ISOF and COOF governance models, the two ensuing development trajectories and the relationship between governance models and decentralized/centralized organizational designs. Next we look at the two governance models in an historical perspective identifying the conditions where each fits. We emphasize the importance of strategic junctures in the history of retailing when conditions favoring the ISOF model change. We then discuss two cases of retail sectors at these historical junctures: the case of supermarkets in Britain and of department stores in the US. We then turn to the question why retail firms continue to practice the ISOF model in face of evidence about the changing conditions. A path dependency, lock-in explanation for this behavior is presented. In our concluding section we discuss the contribution of our analysis to retail theory and management and to the research streams on which we draw.

2. Related research

2.1 Centralization vs. decentralization

The issue of centralization/decentralization (CD) was studied by organization and strategy researchers (e.g. Ulrich and Weiland, 1980). Most relevant are studies of the linkages among the environment, organizational structure and strategy implementation (Chang and Harrington: 1998; 2000; 2003; Olson *et al.*, 2005). Most attention focused on market conditions: whether the market is localized and heterogeneous or wide and homogenous. In relation to retailing these market conditions are influenced by two factors. The first is consumers' sensitivity to store outputs (e.g. price, assortment, and service). Low sensitivity to local stores' deviations from the standards held by consumers reinforces localization. An increase in sensitivity leads consumers to shop around, broadens the market and increases homogeneity. The second factor is competition. An increase in competitive intensity accelerates the rate of innovations and leads to improvements in outputs. In turn, this enhances consumers search across stores and markets further increasing market homogeneity. Decentralized firms perform better when markets are localized and heterogeneous. When consumers are largely confined to their local markets and accept what the local stores offer localized responses are adequate. These are best generated by decentralized firms strongly embedded in the locality. Centralized organizations perform better when markets and competitive scope become wider , competition more intensive and markets more homogenous.. This occurs when consumers become more sensitive to store outputs and increasingly shop outside their locality. In this situation centralized firms which possess superior search and learning capabilities, are more effective in evaluating new ideas, devising responses to new situations and sharing them across the firm. These advantages become more pronounced in environments with richer opportunities.

Retail geography researchers discuss CD in the context of studying the role of tacit and local versus codified, firm level knowledge (Wood, 2002). One issue discussed is how the new integrative information technologies and expert systems reduce the importance of local knowledge and consequently impact decentralization. Another is the continued importance of local knowledge. Amin and Cohendet (1999) hold that firms should operate a dual organizational structure where knowledge associated with the firm's core competencies should be centralized while knowledge regarding others, decentralized. In a study of the reorganization of US department stores in the

1990s Wood (2002) identified the cost savings from elimination of duplications and the improved marketing and merchandising as the main benefits from centralization. However, he finds that in spite of the introduction of the new technologies and expert systems a need still exists for decision making based on local knowledge. Retail firms need to find the right balance between central control and local autonomy. Another relevant research stream in Geography (e.g. Schoenberger , 1997) emphasizes management resistance as the barrier to centralization. We discuss in detail how our concepts relate to this research .In the paper we draw on this research in delineating the conditions fitting each of our governance models.

2.2 Governance Models.

Our interest here is in the study of the relationships among firm's governance model, the environment, and the process of resource and capability development**.** Recent studies by Zahra and Filatotchev (2004) and Gedajlovic *et al.* (2004) provide relevant insights. Both studies analyze the evolution of young, owner-founder managed firms contrasting two governance models: Founder-Managed Firm (FMF) and Professionally Managed Firm (PMF). In the first, decision authority and control are concentrated at the hands of the owner-manager. In the second, these are at the hands of a hierarchy of professional managers. FMFs are simple and lean while PMFs are complex and costly. FMFs' resources and capabilities are limited and idiosyncratic, reflecting founder-manager's personal abilities and experiences, and often confined to specific markets and sets of circumstances. Also, FMFs' ability to learn, develop capabilities and generate resources is limited. FMFs can react fast to opportunities, but only in their immediate environment.

Gedajlovic *et al.* (2004) argue that FMFs operate well in small, fragmented, simple and resource scarce markets. PMFs outperform FMFs in munificence environments (rich in resources and in growth opportunities), and in complex and stable environments. Historical evolution in markets and industries as well as the natural tendency of FMFs to venture beyond their niche means that many FMFs will eventually encounter such environments. They will than find that the FMF governance model is no longer adequate. FMF firms in effect reach a juncture where they need to change governance models. A PMF model is required for the exploitation of the new growth and profit opportunities. This model direct firm towards the development of the resources, capabilities and institutions that fit better the new conditions. The authors recognize the difficulties in switching to the PMF model. They expect FMFs trying to switch to PMF to suffer from "intractable path dependencies and learning disabilities" (Gedajlovic *et al.,* 2004: 909) hampering their ability to successfully negotiate the governance model transition.

While the study context is different there are many similarities with our approach. These authors too emphasize the key role governance models play; discuss how they shape the capabilities and resources firms develop and how they affect firms' growth. Also, they too emphasize the strategic importance of the point in time when market conditions change necessitating a change governance model.

2.3 Development trajectories and path dependencies.

A firm's capabilities, resources, repertoires, and institutions were developed in response to problems, challenges and opportunities. They constitute the firm's development trajectory (path). As the process of challenge-response unfolds, these become increasingly specialized. Each subsequent action reinforces the commitment to that path and further "locks" the firm into it. The further advanced is the firm on this trajectory the more difficult it becomes to change directions (Garrouste and Loannides, 2001; Stack and Gartland, 2003). Many researchers hold that a firm's present actions are influenced by its history and past actions. These constrain the firm's ability to adapt to new conditions: recognize problems, utilize relevant new knowledge and develop appropriate responses. In the words of Teece *et al.,* (1997: 515), *"At any given point in time firms must follow a certain trajectory or path of competence development. This path not only defines what choices are open to the firm today, but it also puts bounds around what its repertoire is likely to be in the future…firms, at various points in time, make long term quasi-irreversible commitments to certain domains* of *competence deciding…which long term paths to commit to."* In effect path dependency is the mechanism capturing the effect of the organization's history on current practices (Booth, 2003).

3. The ISOF and COOF governance models.

We identify two chain governance models. Firms practicing the "Individual Store Oriented Form" (ISOF) view the chain as a collection of individual stores. Its performance is determined by how well each store is doing in its local area. ISOF firms hold that the key to growth and profitability are store level capabilities. Resources are largely invested in stores rather than in firm level systems and capabilities. The success of local stores is viewed as being totally dependent on store management's capabilities, motivation and knowledge. Store managers are allowed autonomy over a wide range of decisions. These include assortment, pricing, merchandising as well as supply and logistic arrangements. ISOF firms avoid investments in monitoring and control capabilities .Therefore; store managers' autonomy is not monitored nor controlled by higher level hierarchies. To the extent investments are made in chain level institutions and capabilities the intent is that of providing support to store managers.

The alternative governance model is Chain Organization Oriented Form (COOF). Here, management's attention is focused on the chain. The firm holds that organization level capabilities determine the firm's competitive position, deliver growth and profitability and will largely determine how well each of its stores will perform. Individual stores are merely viewed as "outlets" of the firm implementing its policies. The company invests its resources in building chain level institutions and capabilities. These are aimed at reducing costs, generating efficiencies and taking advantage of opportunities. COOF firms are often proactive, molding rather than merely adapting their supply and demand environments. They invest in coordination systems designed to integrate the network of stores ensuring effective implementation of firm wide strategies. Note that strict standardization across the chain is only one of a range of options. COOF firms may choose to allow variations across the stores. Similarly, COOF firms may place high value on locally developed knowledge and initiatives and grant decision authority to store managers. But, in contrast to ISOF firms, these variations are always planned and systematic and store managers autonomy defined and monitored. Finally the formats and the spatial development of the firms practicing these two governance models differ. ISOF firms display a "local orientation". Each store attempts to exploit the sales potential in its "locality". Each store will adapt its product and service assortment to local demand . As the firm level mechanisms for spatial expansion are underdeveloped ISOF firms are likely to increase the size of the chain mostly through local initiatives involving gradual expansion into adjoining localities through mergers or acquisitions.

Four elements are especially important in distinguishing between the two governance models. These are the "retail philosophy" guiding firm's behavior, the existence and use of an organizational level coordination, monitoring and control systems, the existence of an integrated , firm wide, supply system and the proportion of resources devoted to the stores vs. organization level activities.

3.1. The ISOF and COOF development trajectories.

Firms continuously acquire or develop resources, capabilities, institutions, systems and repertoires. They represent responses to the problems, difficulties, challenges and opportunities firms encounter. These development trajectories are related to the governance models firms practice .The reason is that COOF and ISOF firms face completely different types of problems , challenges and opportunities. Similarly, their response to the same problems may differ. As companies continually react to unfolding problems and opportunities the process is dynamic (Hooper et al, 2003) .Consequently, COOF and ISOF companies will develop increasingly specialized assets and capabilities evolving along increasingly divergent development trajectories.

ISOF firms benefit from two capability components: those accumulated at the store level and those at the firm's level. The knowledge, resources and capabilities developed at the store level are highly idiosyncratic reflecting local problems and opportunities. Since ISOF companies show limited or no interest in applying this knowledge across the firm, it largely remains tacit. The local embeddedness, closeness to local customers, community and suppliers dictate a strong reliance on personal interaction skills and on informal contracts and arrangements. The above means that the store level component of the firm's set of capabilities and resources is highly diffused and difficult to access. Its growth is likely to be slow rather than exponential.

The firm level capabilities' component reflects the ISOF firms' focus on investing only in capabilities and activities directly helping the stores. These include merchandising and accounting techniques, training programs and brand advertising. ISOF firms will avoid investing in coordination; control and monitoring systems . To the extent these firms invest in central buying they will avoid moves posing a threat to stores' autonomy .Central buyers will try to persuade store managers to source from central buying rather than impose the practice .These firms lack the capabilities needed to take advantage of opportunities identified by local managers or identify global business and technology opportunities. They lack the ability to apply new innovative responses across the firm. Furthermore, store managers often oppose company wide demand and supply initiatives disputing their relevance to local conditions.

COOF firms focus on three broad issues: firm integration, firm level economic and marketing efficiencies, and exploiting external growth, efficiency and profit opportunities .They develop knowledge, resources, capabilities and institutions designed to achieve these. First, COOF firms invest in coordination, monitoring, control and communication systems. They continuously perfect these in response to problems or opportunities. For example, in a widely cited HBR article Stalk et al (1992) analyze how Wal-Mart used the new information technologies to develop its supply system, connecting all levels of the organization to its distribution centers and suppliers. Second, cost reduction and organizational wide operational efficiencies were historically mostly achieved through standardization. More recently through coordination and reshaping of supply, logistics and distribution to better serve firm's requirements. A notable example is Seven-Eleven Japan's restructuring of its supply and distribution environment. (Kunitomo, 1997; Bell and Hogan, 2004; Chopra, 2005). Finally, COOF firms set up mechanisms for identifying growth and profit opportunities in their environment manage knowledge and test new concepts and systems. For example supermarket firms such as Tesco continually experiment with new categories and new formats (Seth and Randall, 2001; 2005, Bevan, 2005; Tesco Annual Report 2006).

3.2. Increased divergence of development trajectories.

ISOF firms use relatively simple retail technologies .The reason is that these firms mostly rely on local knowledge and capabilities .These often remain local and are not easily accessible to the others in the firm. Furthermore, as ISOF firms avoid investments in systems and capabilities posing a potential threat to individual stores' autonomy they often miss on those advancements in retail technology that are based on a cross firm integration of processes. These innovations, especially those associated with integrated supply systems, have revolutionized retail management in recent decades (Fernie, 1994; Smith and Sparks, 1993).

COOF firms deal with problems and opportunities involving both the firm as a whole and individual stores. Consequently, these firms encounter a larger number ,variety and complexity of problems and opportunities. They end up developing more elaborate and complex body of resources, capabilities and knowledge.

This discussion leads us to expect ISOF firms to display a largely flat capabilities and knowledge development trajectory while COOF firms' accumulation of capabilities and knowledge is exponential. With time these two trajectories will become increasingly divergent. The type of environment in which firms operate may impact the size of the gap between trajectories through its effect on COOF firms. It will be smaller in environments presenting COOF firms with fewer challenges and opportunities to develop capabilities.

The expected pattern appears in Figure 1. Capabilities are measured in terms of the number of types of capabilities and their complexity (heterogeneity and range).Time indicates the time elapsing since the adoption of the governance models. These patterns may be used to compare individual firms (e.g. similar firms choosing different governance models),groups of firms belonging to different sectors (e.g. “convenience” versus “multiple” supermarkets in the UK, or discount versus the conventional department stores in the US) or the same firm at different periods in its history (e.g. Sears Roebuck at its ISOF and COOF periods).

We hypothesize that the longer firms practice an ISOF model the more difficult it will become to switch to the COOF governance model. This reason is the increase in divergence with time as well as the path dependency logic. A related hypothesis is that when conditions no longer favor the ISOF, the longer firms persist in practicing the model the less likely they are to try and change their governance model. The growing costs of catching up and the path dependency mechanism decrease the expected benefits from switching. This leads us to conclude, as did Teece *et al.* (1997), that at some point the choice of the inferior model become irreversible.

Figure 1 here

3.3. Retail governance and centralized/decentralized designs.

The phenomenon captured by the Centralization /decentralization (CD) concept differs from the one covered by our governance model . CD describes differences in organization design whereas our governance models capture key differences among firms in the direction they choose to invest their resources and develop their capabilities. Specifically ,our governance models relate to more fundamental and higher level characteristics of the firm. These include the firm's retail and business philosophy, relationships among its components and the level of control and coordination. ISOF firms' lack of coordination and control capabilities confine them to a decentralized design. In contrast COOF firms can choose among the two options, many choosing to operate decentralized designs.

It is useful to distinguish among types of decentralized organizational designs rather than treat decentralization as a single option. One dimension on which decentralized designs vary is the degree of control and monitoring of the decision autonomy granted. A “full” decentralization means that store manager’s decisions are not monitored nor controlled by head office, while “controlled” decentralization means autonomy exists but decisions are monitored and controlled. The other dimension relates to the number of issues. A “complete” decentralization means that autonomy involves a very wide spectrum of issues while “limited” means decentralization is restricted to a number of areas. To the extent ISOF firms lack control and monitoring capabilities they have no choice but allow store managers a “full” autonomy. Also, their retail philosophy leads them to allow store managers a “complete” autonomy. In contrast, COOF firms that do grant decision autonomy to stores are expected to apply the “controlled” and “limited” version of decentralization (Figure 2). Specifically, decision autonomy will be well defined and confined to specific issues and while store managers are not required to consult higher management they know their decisions will be monitored. The degree of control as well as the types of decisions left by COOF firms to store managers will vary across companies and situations. Differences reflect company strategies, demand and supply environments, firm’s capabilities and its culture. Best Buy’s recent move into a “customer-facing” supply chain (Supply Chain Digest, 2006; Harvard Business School, 2006) provides an example of a COOF firm reconfiguring its organizational design towards a controlled and limited decentralization. Firms may choose to apply different approaches towards different product categories. In China, for example, Carrefour, Auchan and Wal-Mart allow their local hypermarket managers a large degree of autonomy in buying, assortment and merchandising decisions in many fresh food lines but limit their decision autonomy in the other categories (Goldman and Vanhonacker, 2006).

Figure 2 here

3.4. Practicing the ISOF and COOF

At a conceptual level, the two models exclude each other. A firm can not adhere to these two opposing business philosophies. However, the reality is more complex as we may observe firms at various intermediate points on the ISOF-COOF continuum. Thus we may observe firms in a transition mode using elements of the two models. Also, firms may hold an ISOF retail philosophy, leaving decision autonomy to store management and investing most resources in the stores, but, still, build chain institutions and capabilities in areas they deem important to future growth. These may include experimenting with new formats and exploring new supply arrangements.

Similarly, firms holding a COOF retail philosophy may apply the governance model partially: develop chain level capabilities only in part, leaving decision autonomy to store managers in issues viewed as marginal and of little strategic importance. For example, in the past COOF firms typically attached little strategic importance to relationships with local stakeholders leaving this area at the discretion of store managers. The increasing difficulties large chains experience in this area increases its strategic importance forcing these firms to take a way this autonomy. Also, store managers may be given decision autonomy over certain product categories where supply and /or demand are highly fragmented and localized.

Additional complexities exist. Firms operating a number of formats and /or operating in a number of regions or countries may practice different models in different parts of their business. Also, as the transition from one governance model to the other may be long, this can lead to the appearance of hybrid models where ISOF firms adopt certain features of the COOF model. Finally, we may find ISOF firms selectively applying the COOF model, for example shifting to a COOF model in product categories subject to scale economies in buying but continuing to practice the ISOF in others.

4. The transition from ISOF to COOF in an historical perspective.

The history of modern retailing is linked to the transition from the ISOF to the COOF governance models. The transition reflects the changes from conditions favoring the ISOF to those favoring the COOF model.

The nature of the transition process and its speed will vary across economies, firms and formats. In some cases it will be fast in others slow stretching over years or even decades. In some cases it will encompass all or most retail firms in the sector, in others only few. When competition is strong firms are more likely to imitate the pioneers and the transition will be faster. When competition is weak, or when ISOF firms successfully shield themselves from competition , the transition will be slower. First mover advantages from switching to the COOF model will be higher where the gap between the ISOF and COOF development trajectories is large and increasing fast. In these situations latecomers will find it increasingly difficult and costly to switch and catching-up increasingly unlikely.

The above means that both pure governance models and hybrid versions, where ISOF firms selectively adopt COOF model features, are likely to appear during transition periods. Researchers analyzing the transition can use the four criteria mentioned before ("retail philosophy" ; organizational level coordination, monitoring and control systems; integrated firm wide supply system; the proportion of resources devoted to the stores versus organization level activities)to distinguish between the pure and the hybrid governance models.

The periods when conditions favoring the ISOF model change constitute strategic juncture points in retail history. Firms will react differently to the change in conditions. Some will change fast to the pure COOF model, others will remain locked-in and committed to their ISOF governance model and still others will go through a slow transition process selectively adopting elements of the new COOF model. Firms failing to respond will lag, stagnate, become marginalized or fail. Furthermore, not all firms reacting to the changes will effectively navigate the transition. Only the better managed firms will effectively leverage the COOF model advantages and achieve superior results.

The pure COOF governance model began to be widely practiced only decades after the appearance of the retail chain concept; in British supermarket retailing only in the 1970s, and in the US department stores only in the early 1990s. Before these periods ISOF or ISOF/COOF hybrid models dominated because they fitted the prevailing demand, supply and retail technology conditions. Specifically, in both cases demand was generally localized and heterogeneous and consumers' shopping outreach limited. Supply of most product categories was comparatively fragmented and competition was largely localized. This is true not only for the local/regional chains but also for the larger/national ones. The COOF model became viable only when these conditions changed. These issues are discussed in the second part of the paper in which we analyze two specific examples of retail firms behavior at strategic juncture points in retail history.

5. Strategic junctures in retail history.

A study of the two governance models at the juncture points , when conditions favoring the ISOF governance model change, holds great promise . A comparison of the behavior of firms making the transition into a pure or hybrid models with those staying with the previous model creates in effect a situation of an historical natural experiment. Note however that while the history of retailing can provide rich examples for management researchers, the nature of source material often limits researchers' ability to study these complex historical developments.

Contemporary retailing also provides opportunities for studying this transition. One context in which these developments can be studied is the emerging economies. Retail firms face there conditions favoring the ISOF governance model: demand and competition are localized, supply fragmented and the underdeveloped infrastructures and consumers’ focus on price push retailers to use simple and low cost retail technologies. The second context involves traditional retailers in developed economies. Organic and natural products and flowers are still largely retailed by small , traditional retailers. The market, supply , demand and competitive conditions that in the past favored the ISOF model are changing . Increasingly these retailers are in a decision juncture point as to their appropriate governance model.

In this research we use historical data to study two periods in retail history when conditions favoring the ISOF model changed. The first is a turning point in British supermarket history when the shortcomings of the ISOF and the hybrid ISOF/COOF models became clear pushing firms to shift into the pure COOF model . The second is the transition point in US department stores when the shortcomings of the ISOF model became clear. In both cases the COOF model potential was released by the wider availability of powerful information technology based systems. The example of the Tesco anchors the first example and that of Sears Roebuck the second. Tesco serves as an example of a firm that made the transition to the pure COOF, while Sears as an example of a firm that failed to change adequately. We chose these two juncture points and the two companies because these periods and these firms' behavior at that point in time are relatively well documented. As is customary in historical analysis of this nature (e.g. Alexander *et al.,* 2005) we draw on reports in the retail trade journals, company histories and studies analyzing retail structure during these periods.

5.1 British supermarkets: the transition to COOF

The late 1960s and the 1970s were a period of turmoil and flux in British supermarket retailing. Developments included the increased geographical coverage of the major chains, growing importance of large, out of-town superstores, expanding assortment into non-foods, the appearance of discount superstores and limited range firms, attempts by foreign retailers to enter the market, and owner-management being replaced by professional management (Davies and Sparks, 1989; Sparks, 1990, 1993; Burt and Sparks, 1994; Seth and Randall, 2001; Bevan, 2005; Shaw and Alexander, 2006).

Most supermarket firms entered this period of flux practicing the ISOF governance model or a hybrid ISOF/COOF model in which key elements of business practice still bore the hallmarks of the ISOF approach. Supermarket chains viewed themselves as engaging in store rather than firm wide competition (Akehurst, 1984). They saw competition as being to a large extent local rather than national, success as a function of how well each store performed against its local competitors. This, in turn, was believed to be determined as much by decisions and actions made by the local store managers as by firm level policies or activities. Akehurst (1984) captured this well in the context of his study of the price competition in Britain at that time. He reports that head offices viewed competition as being among stores not among firms (p.210) and that multiples pursued an "individual goods" competitive pricing approach (which further encouraged the setting of prices at the store level) rather than a firm level "market basket" approach where firms compete on the basis of their price image. In these circumstances firms did not recognize existence of competitive "interdependence" among themselves[1] (Akehurst, 1984).

Local managers enjoyed a significant degree of autonomy. The situation at Tesco at the time is informative, with the stores being seen as "the driving force of the business" (Corina, 1971; Powell, 1991): store managers made decisions about range, display, store layout, promotions and merchandising. In relation to pricing, Tesco Board Member and later Managing Director David Malpas recollected "*we had a price list that was in the way of being a suggested price list, and then branches did what they liked with it. It was all done on an ad hoc basis, branch by branch…*" (Powell, 1991: 153). Suppliers continued to deliver directly to stores and managers made their own deals with suppliers. As Tesco head office saw it: store managers made "*their own little decisions, careless of their impact on the company as a whole*" (Powell, 1991:183). Tesco "*had inadequate stock control systems throughout the business …. Store managers really looked after themselves ...stocked what they like*" (Powell, 1991: 186). *"With direct to store delivery, store managers were "encouraged" to "buy in" extra products in secondary lines to cover stock losses"* (Fernie and Sparks, 1997).

Firms allocated substantial investments to retail outlets rather than investing in firm-level control and coordination systems or in firm wide policies and initiatives (Jefferys, 1954; Akehurst , 1984). Fernie and Sparks(1997) state that *"the (Tesco supply) system allowed almost no control or standardization of the retail outlets and of store managers"* and Akehurst (1984) states that supermarkets, with the exception of the new discounters, saw little advantage in instituting firm wide price policies or promotions. Note that some supermarket chains did establish firm level structures and institutions and employed professional managers at the center. Supply and logistics in particular were recognized as being of central importance and supermarkets attempted to generate cost advantages through large-scale central buying investing resources in developing firm level capabilities in central buying teams, distribution and logistic systems and distribution centers. (Dawson and Shaw, 1989; Smith and Sparks, 1993). For example, Tesco House opened in 1959 with a reported "*130 000 square feet of scientifically arranged automatic invoicing, warehousing and covered loading-bays*" (Corina, 1971: 143). However, these efforts were typical of only few firms and even in these were partial. For example, McKinnon (1985) reports that relatively few supermarket firms operated distribution centers. In fact in late 1970s only 66 centers existed and only 35% - 40% of grocery supplies traveled to retail

[1] Awareness of such "interdependence" emerged earlier in the competitive London market. A reading of the archive of the London Cooperative Society reveals emerging recognition of the potential for enhanced competition between the multiple supermarket chains across parts of the city during the early 1960s (London Cooperative Society, 1959-1960; Grocers' Gazette, 1962)

outlets via such central warehouses. Supermarket firms mostly relied on suppliers' direct deliveries to their stores. The number for Tesco was even lower, some 17 % indicating a partial and selective adoption of this practice (Fernie and Sparks, 1997).

Market conditions prior to the above period of flux and turmoil were compatible with the chains maintaining an ISOF governance model. Most supermarket chains were still local and small carrying only a food assortment. Consumers shopped for food mostly within their local area and their shopping outreach was limited. Competition was keen and promotions extensively used but consumers' sensitivity to price was moderated by lingering product shortages, and remaining government controls. Many food categories were still supplied by a multitude of small suppliers. In addition retail management methods were relatively simple and underdeveloped, as utilization of computers was at an incipient stage (Boswell, 1969; Dawson and Sparks, 1986; McClelland, 1990). Large supermarket firms found the task of coordinating and managing central buying and distribution highly complex. Head Office buyers often faced problems in enlisting store managers' cooperation and commitment to the products purchased by the central buying.

These conditions were changing in the late 1970s. Growing inflationary pressures increased consumers' price sensitivity and reduced their ability to judge the value of local promotions. Shopping outside the trade area at a destination firm increased the new superstores' offer of non-foods and their one stop shopping option attracted consumers. The appearance of discounters further enhanced consumers' price sensitivity creating pressures on supermarket firms to support firm-level price policies (Akehurst, 1984). Firms turned to the development of their overall price image, uniform prices across the chain and to "market basket" pricing policies. The nature of competition changed. It became more aggressive and intense and shifted from competition among the local stores to competition among firms. The widespread reporting of supermarkets' rankings and performance data in the business and popular media further increased competitive pressures.

These developments pushed firms to look more aggressively for ways to generate cost efficiencies, establish a cohesive image and implement marketing strategies across the chain. Store managers' decision autonomy was increasingly viewed as interfering with firm-wide efficiencies and management ability to implement firm-wide initiatives. Small chains such as the discounter Kwik-Save presented a visible template of a highly efficient firm. This limited line discounter heavily invested in firm level capabilities and systems and operated the full COOF model (Sparks, 1990; 1993).

These changes in market conditions must have impacted all supermarket chains but their effect on Tesco was widely reported. At the time Tesco was perceived as being relatively expensive and lost market share. A growing number of chains began to introduce company level price campaigns and were viewed as leading in price. In an effort to change course Tesco decided to drop the use of Green Shield Stamps as its major consumer attraction device and institute its first substantial across-the-board price cut. The move, labeled “Operation Checkout”, was extremely successful and had a lasting impact on UK supermarket retailing (Akehurst, 1984; also Powell, 1983). It is important in our context because the difficulties management faced in effectively supplying the stores in response to the increased demand that ensue exposed the shortcomings of the previous governance model. In response Tesco, which at the time operated a hybrid ISOF/COOF model, abandoned the still considerable elements of ISOF in its governance model transforming itself into a pure COOF firm. It took away store managers' autonomy and made substantial investments in firm-level buying, supply, logistics and distribution capabilities .It strengthened firm-level institutions developing control and monitoring systems enabling the center to measure performance and rein in store managers (Sparks, 1986; Powell, 1991; Smith and Sparks, 1994)**.**

Similar transformations took place in other British supermarket firms (Boswell, 1969; Williams, 1994; Emerson, 2006). However, there were many supermarket firms which failed to change their governance model. Prominent among these were the retail societies and stores belonging to the cooperatives, voluntary chains, symbol groups and some of the small chains. They continued to adhere to the retail philosophy emphasizing the importance of the store manager, to see the center's role as mostly supporting the individual store activities and consequently failed to invest in resources required to enable effective firm level buying and in logistics capabilities and system. These firms’ continued adherence to the ISOF model’s retail philosophy is well documented in the trade literature. The 173 outlet Budgens chain business formula was described in 1975 as “*to trade on a concept in which catering for the food requirements of the neighborhood, and in total relating to that neighborhood, would be an essential ingredient.”* (Tanburn , 1975; see also The Grocer, 1985). This ISOF mentality has remained the Budgens’ symbol group. In an interview in 2002 a director of ACS, part of Budgens, is quoted as stating “*ACS stores conform to the Budgens Local concept but they don’t always see eye to eye on every detail…A store must trade to its location in terms of price, promotion and range”* (Convenience Store, 2002). Another example of retailer’s maintaining an ISOF governance model is provided in a 1991 interview with the CEO of Europa Foods, a London chain of supermarkets operating 45 stores, in which he says "*no two stores contained the same product mix.……We don’t arrange two stores the same…They will be arranged in conjunction with the neighborhood in which they are situated…”* (Convenience Store News, 1991: 111).

These chains chose not to invest in building the firm level capabilities and consequently found themselves unable to compete effectively against the supermarket firms which during the 1970s were moving toward a pure COOF governance model. Failing to compete effectively, they adopted a niche strategy positioning themselves as “convenience” supermarkets. With time the differences between the firms practicing the ISOF and COOF governance models became increasingly pronounced .The COOF firms were assigned by the trade press and retail experts to the “multiples” sector and the ISOF firms to the “convenience” sector. The ISOF firms stagnated while the COOF firms evolved into world class supermarket retailers. Indeed, none of the major innovations that transformed British supermarket retailing in the last decades were contributed by the ISOF firms. Perhaps the most visible signal of the COOF model superiority is the recent re-entry of firms such as Tesco and Sainsbury's into neighborhood retailing. The COOF governance model enhanced the development of a robust set of capabilities enabling them to outperform the convenience firms specializing in local supermarket format.

5.2 Department stores in the US

Department store chains in the US traditionally operated an ISOF model. Local management enjoyed a high degree of decision authority and the chains emphasized local focus. Most firms operated as a collection of individual stores, rather than a cohesive organization. They eschewed investments in organization-level capabilities and systems and lacked effective coordination and control, central purchasing and logistic systems (Raff and Temin, 1997). Head Office and regional managers largely viewed their role as providing support to store managers. Wood, (2002) studied the movement of US department stores away from a decentralized towards a centralized organizational form. While his interest is mostly in how these firms managed local knowledge his study contains many relevant observations. Relying on historical sources and interviews with executives he characterizes the situation prior to the change: “*As such, there was an emphasis on tacit/local market knowledge, above any centralizing tendency, as markets were regarded as complex, each one differing from the other and for that matter having differences between themselves….It is for these reasons that…knowledge was acquired and decisions made largely at the divisional decentralized spatial scale……..The geography of the US department store retailing had become a highly decentralized activity. Merchants were locally embedded within their core markets, knew them well, and performed ably*” Wood (2002: 13, 14). These companies used a variation of the Mazur Organizational Plan (Mazur, 1927) that served as the organizational template to department stores. The plan recognized that most authority was at the branch level and that store managers had decision autonomy in merchandising, operation and buying. The strategic juncture point occurred in the 1970s. At that time the split between the traditional department stores, largely practicing the ISOF governance model, and the newly established firms, mostly discount department stores and the specialty chains, moving towards the new COOF model became clearer. The transition was gradual, different firms experimenting and developing capabilities and systems that were later incorporated into the sector's standard COOF model.

The history of Sears Roebuck's anchors our discussion. Sears entered the department store business with a general merchandise (GMS) department store format in the 1920s. While it practiced a COOF model in its mail order business, it chose an ISOF model for its department stores (Emmet and Jeuck, 1950). Like the other department stores of the time it set up a Head Office, a functional management system and regional buying. However, store managers enjoyed substantial decision authority (Emmet and Jeuck, 1950). Sears' CEO at the time is quoted saying: "*It is essential that the responsibility be placed on the store manager…. If he is visited constantly by supervisors and inspectors … (if) we set up a system of checks and inspection that will (uncover) weaknesses (at the store level)…. The remedy will be worse than the disease*" (Worthy, 1984: 119-20). Central management saw Sears as a *"federation of independent merchants, each local store manager to a considerable extent autonomous within the four walls of his own store. The store managers oversaw the sales, they lived in the communities" (*Raff and Temin, 1997). Sears central buyers *"had to persuade the store managers to stock the goods they procured."* Also, while there was a layer of supervising managers their job was to help and support local managers not dictate to them. The situation in the other department stores was even more extreme as the local managers "*had a free hand as to which vendors they use"* (Raff and Temin, 1997).

This ISOF governance model persisted in Sears for the next five decades. In the 1970s Sears increasingly found itself in difficulties. It was losing customers and sales to two new types of retailers: discount department stores and focused specialty stores and, in some markets, to department stores that emulated these new retailers. These firms were, in effect, gradually transforming themselves into COOF firms. The debate taking place at the time within Sears is well documented (Raff and Temin, 1997). One group of executives held that a radical move was needed. They advocated abandoning the old (ISOF) governance model switching to the model practiced by the discount department stores and the focused specialty stores. They saw the autonomy of local stores as the root problem and proposed that Sears take away store managers' sweeping authority to determine product ranges, inventory policies , price levels, sales and promotion events, and on advertising. These executives noted that Sears' central management and regional offices did not have control and coordination capabilities, their knowledge of stores' performance was sporadic and sketchy, and no formal mechanisms existed for the accumulation, evaluation of using locally acquired knowledge. These executives recommended a shift of focus towards building of organization level infrastructures (Raff and Temin, 1997). The executives promoting the alternative approach, the one that prevailed, believed in the value of each store's independence and in preserving store managers' decision autonomy. They recommended investment of resources in store renovations rather than in chain-level infrastructures. Head office should also invest its resources in activities supporting store operations such as the advertising of the Sears brand.

Sears' management was aware of examples of highly successful retail companies that practiced the new (COOF) model. One approach was developed by Wal-Mart and the other discount department stores such as Target and Kmart and the other by focused specialty retailers such as the Gap and the Limited. Wal-Mart's approach is well documented (e.g. Stalk *et al.,* 1992). Essentially the firm focused its efforts on the development of firm-level capabilities enabling it to buy goods cheaply and deliver them to its stores in a highly effective way, minimizing inventory and stock out costs. Goods were bought by a centralized buying system and delivered to the stores from a network of distribution centers. This contrasted contrast the practice in Sears and other department stores where goods were delivered directly to each store by vendors (Wood, 2002). Wal-Mart invested substantial resources in building its information technology capabilities: scanner and POS systems and data capturing, processing and transmission systems. This enabled Wal-Mart to use store space more effectively and ,by monitoring sales in each store, improve their performance. Raff and Temin (1997, p. 37), who had access to internal Sears documents; hint that Sears' managers did not understand Wal-Mart's model. They were convinced that Wal-Mart's success was due to its down-market positioning rather than its adherence to a different governance model.

The COOF model developed by the Gap and the Limited was based on the reorganization of the buying function for fashion goods. These firms built new types of organizational capabilities that generated not only cost efficiencies but also marketing ones: faster reorder-delivery cycles, minimization of stock-outs and an increase in the selection offered. At the time merchandising decisions in department stores were made by store buyers overseeing both the buying and store merchandising decisions. Procurement was made directly from vendors on the basis of knowledge acquired by these buyers through directly observing customers in store behavior. Each store employed a large number of buyers often for each major department (Wood, 2002).Thus ,buyers in each of the 60 Macy's East stores ordered goods directly from the same vendors. In contrast, the Gap and the Limited invested heavily in central buying and developed the information technology based systems and capabilities providing central office buyers with the information needed to make effective buying and merchandising decisions (Raff and Temin, 1997).

The negative consequences of Sears' failure to switch from its ISOF model to the COOF were recognized only a decade later by its new CEO. After studying Target he commented that its approach was "*a far cry from the Sears way, where each store still reflected the tastes and experiences of the manager*" (Katz, 1987: 256). The increased use of information technology led to dramatic changes in retail management methods. The new systems made possible both the generation of major economic efficiencies in purchasing and the speeding up of the replenishment cycle, revolutionizing merchandising and marketing. The benefits in price, availability and selection to consumers far out weighted any loss of tacit information about local preferences. Sears ignored the implications of the changes in the retail environment and stayed with the irrelevant ISOF model. When Sears eventually shifted to the COOF model it was too late and the firm verged on the brink of bankruptcy.

6 .The persistence of the ISOF model: the impact of path dependency

In this section we discuss the reason why firms persist in pursuing the ISOF governance model when the environmental conditions no longer support this model. We advance a path –dependency explanation for this behavior. Two aspects of the path dependency phenomenon are relevant in our context. The first is a perceptual myopia and managerial lock-in, and the second is a capabilities /resource limitation problem. A third aspect, that of the lock –in into increasingly specialized capabilities and technologies, is less important in our case. The reason is that the ISOF governance model is associated with simple retail management techniques. These do not avail themselves to much specialization and development.

6.1 Perceptual myopia and lock –in.

Firms institutionalize their repertoire of practices and habits and deeply embed their retail philosophy. These put blinders on firms' management ability to recognize problems and opportunities and react to them. In the case of ISOF firms local managers will be slow to notice and /or understand the meaning of macro changes taking place outside of their local markets. While higher level management is more likely to notice such changes they will find it difficult to fully comprehend their implications. Another issue is management inability to undertake new response patterns and lack of commitment to the need to change. In the case of Sears managers became locked-in to the old ways of doing things. They deluded themselves into believing the practices and philosophy associated with the new governance model are not relevant for Sears .They continued to respond to the changes in their competitive environment in terms of the familiar response repertoire: such as putting more resources into the refurbishing of stores. In the case of Tesco a dramatic crisis was needed for management to realize the need of moving into the pure COOF governance model.

ISOF firms may face another set of constrains that often hamper the transition to a COOF model. These involve inter-organizational politics. Managers, local or others ,who often develop a stake in present arrangements and often oppose the move into a COOF model. They either fear loss of authority and position and/or genuinely believe in the local approach. The weakness of the center not only emboldens their resistance but often helps legitimize it. This factor is especially important at the early stages of the transition process when the superiority of the new model may still be in doubt. The ISOF oriented managers can then claim that the ISOF model performs better than the new COOF model promoted by the center. Local managers' resistance to the transition may slow down the transition process leading to the persistence over extended periods of intermediate governance forms involving hybrids of the ISOF/COOF.

6.2 Capabilities and resource limitations.

The COOF governance model is associated with more complex and resource heavy organization. Consequently, ISOF firms intending on making the switch need to literally transform and reinvent themselves. These firms need to secure financial resources and develop many new firm-level capabilities, systems and institutions. While this transformation is expected to be difficult for all firms it is likely to be especially hard and painful for small chains. Also, firms based on a grouping of independents are in a weaker position than corporate retail firms. They will find it harder to generate the required financial resources and develop the needed managerial capabilities.

The timing of the switching decision is important. The longer ISOF firms wait, the more difficult the transition becomes. As Figure 2 indicates, the underlying process of capability development favors COOF firms leading to an increase in the size of the capabilities gap with time.

Even when off the shelf technologies and systems are available, laggards will suffer from the imitator curse. The firms making the switch earlier will enjpy a head start in developing the next generation of the COOF systems and technologies. The recent example of the convenience supermarkets in Britain illustrates the point. The intensifying competitive climate in the sector as a result of the entry of the COOF multiples pushed the largely ISOF convenience supermarket firms to explore more aggressively a shift into a COOF model. While many purchased information technology systems off the shelf, the gap in capabilities was extremely large making catching up highly unlikely. These firms are faced with the option of pursuing a niche strategy or succumb to the pressure from the multiple supermarkets and be acquired by them (Mintel, 2004).

7. Conclusions

We study a central characteristic of the retail firm, its governance model. We focus on the two basic models and discuss the differences between them. Governance models are of central importance because they determine the direction of capability development and resource acquisition of firms and shape the types of capabilities they develop. In the paper we delineate the development trajectories ensuing from each governance model. We study two historic examples of strategic junctures in retail history when the conditions favoring the ISOF governance model changed. We use historical examples drawn from company histories and the trade literature as a basis of our discussion of these juncture points, to illustrate our concepts and to provide face validity. The phenomenon of path dependency explains why retail firms at these junctures continued to practice the ISOF governance model.

We contribute to retail theory in a number of directions. First, we introduce new concepts including ISOF and COOF governance models and capability development trajectories. We then demonstrate their relevance by showing how they can be used to provide a richer interpretation of retail change at important historical junctures. Second, these concepts draw heavily on recent research in organization, strategy and evolutionary economics and thus our work should also be viewed as a bridge to these highly relevant research streams (Savitt, 1999). Third, we clarify a number of issues that were discussed before in the retail literature but in a less systematic manner than in this paper. For example, we differentiate among two types of decentralized organizational designs and point out that strong monitoring and control capabilities and a culture of tight supervision of local managers' performance does not preclude a decentralized design. Indeed, as the recent experience of Best Buy (Lal *et al.,* 2006; Supply Chain Digest, 2006) demonstrates these capabilities enable firms to tailor formats to local conditions. To capture this phenomenon, increasingly used by COOF firms, we differentiate among two different types of decentralized organizational designs (Figure 2). Fourth, we argue that firms consisting of independent store owners can successfully practice a COOF model and are not confined to an ISOF governance model. Independents' based organizations in Germany (e.g. Rewe and Edeka) in Japan (Seven-Eleven) or in Switzerland (Coop Swiss) successfully navigated the change into the COOF model and perform well. To the extent differences in performance between these firms and corporate owned ones exist, as is the case in the UK ,where numerous firms consisting of independents (voluntary chains, cooperatives, symbol and buying groups) and small chains continue and practice the ISOF model despite mounting evidence of the COOF model superiority, they reflect specific historical circumstances. These seemingly "weak" retail forms are not fated to be confined to the simpler governance model.

Our concepts are clearly relevant for the interpretation of historical developments. They can, however, also be used for understanding present day retail management issues and help in devising better strategies. We discuss here two applications. First, moves by UK “convenience sector” supermarket firms to strengthen their competitive position against Tesco and Sainsbury involve a rush to adopt features of the COOF model such as advanced information technology systems. These moves are not likely to succeed as long as these firms fail to deal with the core issue: the continued adherence to the retail philosophy and practices associated with the ISOF governance model. Furthermore, the huge capabilities gap between them and the COOF supermarkets keeps growing, further reducing their chances of success. Another interesting application concerns retail internationalization. Increasingly this involves the entry of European and US supermarket retailers with sophisticated capabilities and systems into emerging economies. These firms encounter market conditions compatible with the ISOF governance model rather than the COOF one. The markets are fragmented and heterogeneous, demand for key food categories such as fresh food is localized, and supply and logistic fragmented and localized. In addition, price sensitivity is high and consumers unwilling to pay the premium for higher value products. Retailers find that their capabilities and their COOF governance model do not fit these conditions and that using their sophisticated systems and technologies raises operational margins but not their competitive effective. These conditions favor switching to an ISOF governance model involving granting substantial, unmonitored, decision authority to hypermarket managers. In China, for example, these conditions are especially pronounced in the fresh food categories (Goldman and

Vanhonacker, 2006; Dinghuan *et al.*, 2004). Surprisingly, many international supermarket firms operating in China have been slow to understand the incompatibilities and react appropriately. Their record of successes in the home market and in other developed economies and their commitments to the technologies and systems that worked well in the past limits head office ability to understand the new environment. Also, their COOF retail and business philosophy prevent them from considering the simple solution of reverting back to the ISOF model. These firms become locked-in into their specialized technologies, systems, and response repertoires. They are trapped in a path dependency situation, some simply waiting for the conditions to change. This is an interesting example of a reverse path dependency in retailing. Adherence to the more complex and sophisticated COOF governance model constrains firms' ability to operate well in environments favoring the practice of the less advanced ISOF model.

Finally our study is also relevant to the related research streams in strategy, organization and evolutionary economics. Most discussions in these areas draw on the history of manufacturing and technology firms. While the history of retailing provides rich examples it is very largely ignored. An analysis of key trends in the retailing history using conceptual frameworks drawn from this literature is likely to increase exposure to that rich source.

Figure 1

ISOF AND COOF DEVELOPMENT TRAJECTORIES

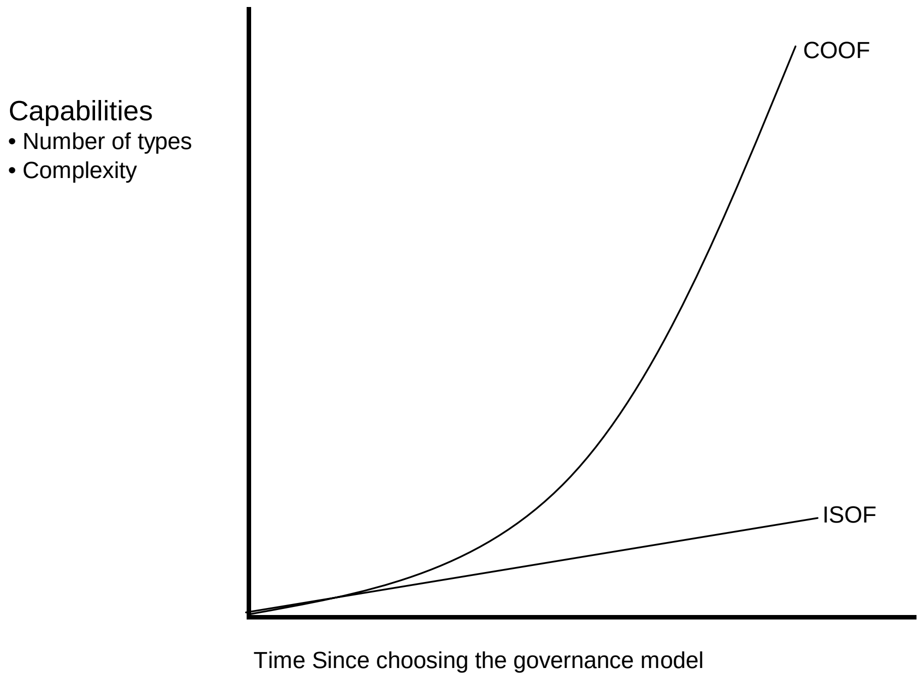

Figure 2

CHAIN GOVERNANCE AND ORGANIZATION DESIGN

ORGANIZATION DESIGN	GOVERNANCE MODELS	
	ISOF	COOF
Centralization	Not possible	Possible
Decentralization • Level of autonomy and number of decision areas	Full and Complete	Controlled and Limited

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