**MARKET POWER AND REGULATION:
THE LAST GREAT US DEPARTMENT STORE CONSOLIDATION?**

Revised version submitted to the *International Journal of Retail & Distribution Management*
following referees comments and Editor's guidance

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Abstract

Purpose – To examine the impact of the merger of the two largest US department store companies on the competitive state of the sector and specifically the anti-trust implications of the consolidation.

Approach – Based on semi-structured interviews with leading US department store executives as well as an ongoing close dialogue with US retail analysts.

Findings – The consolidation raises considerable anti-trust issues with the creation of a \$30bill sales company. Consistent with previous recent rulings, the Federal Trade Commission (FTC) has adopted a broad view of the department store market from the standpoint that the consolidation is essentially defensive – in short, the sector is failing because it is not a separate and distinct market. However, the divestiture of 75 stores will give competitors footholds in new markets thereby changing the geography of competition in many catchments. This is likely to be the largest consolidation that the competition authorities will effectively allow, representing the last opportunity for the sector to become a more robust competitor against alternative formats that have intervened in its key product lines.

Originality/Value – Recent restructuring of the US department store industry has generated a relatively limited academic literature, despite considerable M&A activity, subsequent organisational reorganisation, and sales of \$88 bill per year. Transformation of the competitive landscape of the industry raises important issues of market regulation and corporate strategy.

Article type – Viewpoint

Keywords: department store; regulation; merger

Introduction

Retail academics with an interest in corporate restructuring and market regulation will have turned their attention to events occurring in the US department store industry throughout 2005. The two leading US department store operators, May and Federated, with fiscal 2004 sales of \$14.4bill and \$15.6bill respectively, agreed to merge creating a retailer accounting for 35% of what the US Dept. of Commerce terms 'conventional and chain department store' sales in the USA, and a significantly higher share of the more tightly defined traditional department store sector. In turn, this acquisition is part of the broader ripple effects that have spread throughout the industry as the sector has consistently lost share of total retail sales, with sixth ranked firm Neiman Marcus agreeing to a \$5.1bill acquisition by private equity groups Texas Pacific and Warburg Pincus, and fourth ranked firm Saks Inc announcing a splitting and partial sale of its business.

The Federated/May merger represents a further seismic shift within an industry that has experienced constant restructuring over the past two decades. Initially this was seen in the leveraged buy-out phenomenon of the late 1980s which ultimately led to the leading department store companies of the time filing for Chapter 11 bankruptcy protection – notably Macys; Allied Stores; Carter Hawley Hale and Federated (Hallsworth, 1991; Wood, 2001). There then followed, during the 1990s, a period of strategic portfolio restructuring whereby regional department store chains were acquired by newly emerging conglomerates (Wood, 2002a). In turn this was accompanied by an intense period of cost cutting and organisational restructuring in order to attain the synergistic benefits that had been used to justify the consolidations (Wood, 2002b). The latest shifts in the industry, in one sense, merely take the logic of that organizational restructuring further. However they also raise a number of important issues which have wider implications for conceptual debate concerning merger & acquisition activity in retailing.

In particular, the consolidation raises significant questions about US antitrust regulation. The main issue is whether the Federal Trade Commission (FTC) was correct to adopt a laissez-faire stance in

allowing the transaction to proceed, leaving State Attorney Generals to rule only on local divestment of stores in some catchments thereby protecting competitive conditions. Clearly, the regulatory agency adopted the view that the transaction represented a 'defensive merger' given that the sector has been struggling because of strong competition from both discount operators (e.g. Wal-Mart, Target) and speciality apparel stores.

While the merger was allowed to proceed by the FTC, a significant degree of local-market divestiture results – 75 stores in 72 malls - of which 47 were made to satisfy regulators. As a result, it is important to interrogate how that geography of store disposal will alter the competitive landscape of the industry – giving a foothold to operators currently outside market leadership positions. Analysis indicates that operators such as Nordstrom, JC Penney, Neiman Marcus and Sears are likely to be the main beneficiaries of any divestiture, gaining footholds in markets in which they are currently under-represented.

In addition, it is also important to understand the broader implications of a merger that creates a 950 store/\$30bill sales company will have on the suppliers of that firm. This is particularly the case in the context of the debates which have recently taken place in the UK concerning 'market power' and 'codes of practice' relating to retailers dealings with suppliers, following the Competition Commission's inquiry into the supermarket sector in 2000 and its rulings in the case of the takeover of Safeway in 2003 (Wrigley, 2001, Burt and Sparks, 2003).

Finally, the consolidation will drive another wave of organisational restructuring for these firms - a restructuring which is likely to see the Federated approach to merchandising, widely regarded to be more sophisticated than May's, being applied to the acquired stores with a subsequent slimming of the supplier base. The issue here is how this restructuring will rework the tension between national control that generates efficiencies and economies of scale, and local execution which demands sensitivity to local cultures of consumption (Wood, 2002b).

Background to the Merger

Historical perspective

Since the 1930s there has been consistent and regular forecasts of the imminent demise of the traditional department store in the US (see Nystrom, 1930 for an early example). While the sector has steadily lost market share throughout the post war period, this deterioration was more marked during the 1990s when the format was essentially pressured from both ends of the quality/value spectrum. In particular, apparel was increasingly merchandised across a wider range of value-focused retailers with discount department stores such as Kohl's and "big box" operators such as Wal-Mart and Target experiencing significant growth (see Figure 1 for a comparison of traditional and discount department store performance), whilst both middle market apparel specialists (e.g. Gap, The Limited) and fashion designer retailers (e.g. Prada, Gucci, etc – see Moore et al 2000) were also squeezing the department stores. Between 1992 and 2004 market share of the traditional department store sector fell from nearly 6% of US retail sales to just over 3% (Figure 2). However, it still represented a market of \$88 billion.

During the 1990s, traditional *regional* department stores in the USA, in particular, were left in a precarious position. Lacking sufficient scale economies to secure sizeable discounts from suppliers they typically experienced only lower single digit or negative sales growth and their stock traded at low levels. They were classic examples of companies effectively 'stuck in the middle' between larger operators, benefiting from scale-based efficiencies, and smaller operators who were more flexible and able to respond rapidly to opportunities (cf. Amatoa and Amatob, 2004). As Michael Gould, Chairman of Bloomingdale's suggested in interview:

'If you are a stand alone business today in the department store world ... what do you mean – what do you stand for? Let's say you are a \$1 billion chain store in Pennsylvania – what's [your] power when [you] go into the marketplace... what's [your] power when

[you] are up against \$16 billion Federated or \$14 billion May Company? Awful difficult!’

(Interview 16).

The reaction to this predicament was predictably a round of strategic consolidation throughout the 1990s in efforts to centralise resources, take advantage of economies of scale, and focus on department store brands that could be leveraged nationwide (Table 1).

Select firms, such as the seemingly insignificant Southern state operator Proffitt’s, were at the forefront of a wave of consolidation of regional department store chains not large enough to attract the attention of the larger players. Proffitt’s growth was impressive: between 1988 and mid 1998 it increased its store portfolio by 340 and its square footage by 31.6 million square feet. By 1999, revenues had increased to over \$6.4 billion and culminated in the acquisition of Saks Holdings at the end of 1998 (Wood, 2002a).

With the rapidly growing store portfolios that came from the consolidation wave, the major department store operators were faced with the task of rationalising and streamlining their organisational structures. In the past, US department stores had operated as many as 15 divisions or fascias, each with its own buying, accounting, credit and distribution facilities. The high costs that resulted made the format increasingly uncompetitive - they simply had too many decentralised divisions with too many buyers, hampered by a bureaucratic decision-making process, often lacking a central theme. In addition, and particularly in the case of larger companies, there was a lack of information flow through the retailer-supplier interface due to a dearth of coordinated systems with consequent difficulties executing key trends across divisions (see Biederman, 1991). As a result, the 1990s was also a period of centralisation of the organisation of these larger players with the provision of shared administrative services, the concentration of buying and merchandising and the consolidation of formally autonomous divisions. Terry Lundgren, President of Federated explained the rationale for the developments:

‘...we have a point of view that if the customer does not see it or feel it then it is an opportunity to be reduced or eliminated Every division used to have their own separate organisation – we don’t need that anymore....All of our technology, all of our systems, computer operations – every division used to have their own set up for that. Now there is one state of the art organisation outside of Atlanta that services all of the systems needs for our stores. One credit facility in Ohio services all of them’ (Interview 23).

The predicament in 2005

The upshot of this round of portfolio and subsequent organisational restructuring by 2005 was a highly concentrated sector dominated by a handful of operators – notably May and Federated (see Tables 2 and 3). However, so intense was the pressure on the department store operators that even the market leaders struggled to perform relative to market expectations. The May Company in particular saw its comparable store sales follow a largely negative trend since the late 1990s (Figure 3). In an effort to achieve scale related efficiencies and access good store locations May paid £3.2 billion for Marshall Field’s in 2004. There was an essential logic to this acquisition as May was able to acquire a strong retail brand and market presence particularly in Illinois, Michigan and Minnesota. Nevertheless, the consensus of the capital markets was that May paid an unjustified premium for Marshall Field’s, and coupled with poor performance from its core business, this precipitated the exit of CEO, Gene Kahn, in January 2005.

The removal of Kahn offered the opportunity for Federated to re-open merger discussions with May and a deal was agreed on the basis of a purchase price of \$11 billion. The logic of the May-Federated tie up is geographically sound. Federated is particularly strong on the East and West coasts as well as in the South-East/Florida market. May had stores in Southern California, the North-East and Midwest. The acquisition of May essentially offered Federated a new presence in important markets such as Texas, Chicago, Minneapolis and St. Louis, plus the opportunity to

introduce its up-market Bloomingdale's fascia into affluent catchments (e.g. in the Chicago area) well suited to such an offer. Strategically, Federated is also well placed in terms of expertise at executing department store acquisitions given its previous acquisitions of Macy's and Broadway in the mid 1990s.

Retail Regulation and the US Department Store Industry

Elsewhere we and others have documented the make up of the regulatory framework impacting the US retail industry and how previous mergers and acquisitions have been dealt with by the competition authorities (Balto, 2001; Wood, 2001; Wrigley, 1992, 1999, 2001, 2002). We have noted how the FTC has essentially operated what might be termed a "fix-it-first" approach, agreeing not to oppose mergers and acquisitions where the acquiring firm committed itself in advance (under the spirit of the Celler Kefauver Act) to divest itself of all clear horizontal market overlaps that might be deemed to be uncompetitive at the local level. In contrast, individual State Attorney Generals, have often sought to impose far more rigorous antitrust enforcement with much stronger impacts on the nature of retail competition in particular local markets.

The continued employment of a "fix-it-first" approach by the FTC was made clear by the current Chairman of the FTC, Deborah Platt Majoras, who confirmed 'a willingness to accept *fix-it-first* offers from parties' (Majoras, 2004, p 8). Previously there had been growing concerns over retailers essentially making ineffective divestitures and thereby keeping the better stores for themselves (Cotterill, 1999) which raised question marks about the approach. Nevertheless as the Director of the FTC noted:

'If the Commission concludes that a proposed settlement will remedy a merger's anticompetitive effects in the relevant market, it will likely accept that settlement and not seek to prevent (or unwind) the merger. In most situations, the [FTC] is most likely to support the parties' offer to divest an autonomous, on-going business unit that comprises at

least the entire business of one of the merging parties in the relevant market, attempting to recreate the premerger competitive environment' (Simons, 2003, p 4/5).

The execution of "fix-it-first" involves, as George Strachan of Goldman Sachs observed, the acquirer making 'some strategic decisions regarding what the likely outcome of the FTC will be'. In its turn:

'the acquirer probably makes an educated guess as to what the FTC is likely to demand and they try to accommodate the most obvious overlaps before the FTC orders them to do so. It is probably built into their plan before the FTC has even announced it' (Interview 8).

This has frequently allowed competitors to take advantage of stores divested due to overlap, though rarely on a scale that is suggested by the scale of the Federated/May merger.

Federal regulators had rarely blocked a merger in the department store industry. Partly, as an Ernst & Young analyst suggested, that is because the FTC 'are not as sensitive as they are in apparel as they are in food'. But more so, it is because the FTC historically argues that the department store sector is, in practice, not a separate market. Indeed, as a prominent former major department store CEO commented:

'I think what the FTC has historically done is smart and appropriate and that is they have looked at retail as a broader issue than just department stores. Our competitor for our business is not just another department store. ...In a typical market, department stores may in the aggregate have 25% of the general merchandise, apparel and furniture [the GAF figure], so clearly 75% of the competition is not department stores - it is other forms of retail. So the FTC appropriately has looked at these from that perspective and concluded

that even after the merger of two companies the share of the market they have is not counter to the beliefs of the FTC’.

However, some strong arguments were mounted for outright refusal of the merger by the FTC: The combination of Federated and May creates a \$30 billion retailer accounting for approximately 70% of traditional department store sales among public companies, and approximately 30% of the mall anchor stores in the US. The combined entity also accounts for 40%-50% of the moderate to high end apparel market in the US, and 25%-50% of the sales of many of the upscale suppliers (Merrill Lynch 2005a).

There were some precedents for regulatory action; even in the department store sector. In 1994, for example, May attempted to purchase six McCurdy’s department stores in Rochester NY, to add to the four Kaufmann’s stores it already owned there. An independent regional chain (Bon-Ton) with nine stores in the area protested. The FTC rejected the complaint, taking the view that the department store sector was merely part of a larger market for apparel and furniture. Undeterred, Bon-Ton took the matter to the Federal Court, and the New York Attorney General joined the case successfully convincing the judge that the department store sector was a separate market and therefore blocked the merger. However, it is notable that this example concerned a small local transaction where there was a high percentage of local market overlap and at a time when the department store sector accounted for a higher share of apparel sales than today. In contrast, the Federated/May merger did not generate high amounts of store duplication except in two or three core markets.

Outcomes: Divestiture and Market Entry for Competitors

Consistent with previous rulings, the FTC took the view that the Federated /May case represented a defensive merger driven by the continuous poor performance of the department store sector vis-à-vis alternative retail formats. In short that the reason the sector is failing is because it is *not* a

separate and distinct market. In a document submitted to the Securities & Exchange Commission, Federated had argued:

‘The retail environment is intensely competitive and department stores today compete against all retail formats. Success is contingent on our ability to realize greater economies of scale, and that is beneficial to consumers in the long run because it means more competition overall’ (FDS, 2005b, p 4).

The FTC’s findings mirrored the retailer’s submission very closely as the regulatory body noted that a broad definition of the market must be taken as ‘today’s mall is itself a real competitor against traditional department stores’ (FTC, 2005, p 2) and that ‘conventional department stores...no longer occupy the unique position they once held, even for the more limited range of products that they sell. While department stores once were a distinctive niche market, they now face pressures both from “above” and “below” even in the same mall, not to mention mass market, mail order, and Internet alternatives’ (FTC, 2005, p 2).

Given the FTC’s view of the market, it appears that Federated’s pre-emptive voluntary disposal proposition of 68 stores in 66 mall locations was largely irrelevant in winning FTC permission. In fact the FTC went even further to effectively argue that divestitures should not be necessary as ‘(t)he evidence shows that the parties’ conventional department stores *do not comprise a separate relevant product market*, and that *an individual mall does not constitute a relevant geographic market*’ (FTC, 2005, p 4, my emphasis). However, the FTC is the *national* anti-trust regulatory agency and *localised* individual divestitures are determined by individual State Attorney Generals, *not* the FTC.

The markets of California and the North-Eastern USA were the areas of highest store overlap between the two retailers (Figure 4). In California, Federated faced its most considerable

difficulties. Having volunteered to the divestiture of 22 stores in its “fix-it-first” submission, it was forced by the State of California Attorney General to increase this by a further four outlets to take total divestiture to 26 stores. This accounts for over 4 million square feet of retail space that will be sold and approximately 5,000 jobs in this single state (Figure 5). Under this agreement, when divesting stores Federated must ‘give priority to Macy’s and Robinsons-May traditional competitors in the department store market’ thereby retaining competition levels in these catchments (Office of the Attorney General, 2005a).

Similarly, the New York Attorney General insisted upon sale of two stores in Long Island that were in addition to the initial Federated “fix-it-first” submission (Office of the Attorney General, 2005b) while the Massachusetts Attorney General insisted on one additional divestiture (see Table 4). Clearly Federated was extremely accurate in forecasting the reactions of the competition authorities.

The overall divestiture of 75 stores in 72 mall locations – equivalent to \$2.1 billion in sales at 2004 prices - has the effect of giving market access to competitors currently without any strong presence, in the process fundamentally changing the geography of department store retailing on the east and west coasts of the USA. The firm most likely to be the primary beneficiary of the divestiture is Nordstrom, acquiring units primarily in New York and New Jersey where it is currently under-represented. Nordstrom’s store portfolio is currently 95 department stores of about 200,000 sq ft each spread across 27 states, but primarily focused on the West Coast and the North-West. Neiman Marcus, JC Penney and Saks (in its pre-sale/split form) also have opportunities to take advantage of the divestitures due to occur in 2006 - again dependent on issues of current market presence relative to competitors and the affluence of specific catchments (Table 5). Clearly the geography of divestiture has the effect not only of reworking the spatial spread of the firms involved in the merger, but equally firms whose store networks are currently far removed from the areas of horizontal market overlap between the merging firms.

Implications of the Commercial Logic of the Merger

Increasing pressure on suppliers

A key argument for the merger, and not least an issue that the FTC could have used to bar it outright, are the potential implications for suppliers. While the formation of a \$30 billion sales department store chain does not represent an unduly high share of total US apparel sales, it represents a significant proportion of upper-end apparel sales and therefore a high proportion of the sales of suppliers such as Liz Claiborne and Ralph Lauren. Indeed Merrill Lynch (2005a) estimates that the combined entity could account for up to 50% of sales of many of the upper-end suppliers. This is evidently a level at which price discrimination could become a real possibility. However, this view was rejected as the FTC viewed department store companies competing in a broader retail market and that higher end apparel was not itself an independent product market.

Another way in which the supplier base is likely to be impacted results from the likely consolidation of the private label brands of the merged company. As widely discussed in the literature, private label offers a range of advantages to the retailer. First, the retailer has control over the offer, arrangement and development (Sayman and Raju, 2004). Second, private labels offer the potential for margin enhancement (Porter, 1999). Third, own label provides distinctive ranges that are unique to the firm and not available through competitor's stores. This is especially important in the department store sector as many of the difficulties with the retail format have been centred on competitors selling the same branded products at lower prices elsewhere.

Federated has put considerable effort into building a strong portfolio of private labels via its centralised support operation, Federated Merchandising Group. As with many other retailers, it offers a range of private labels that are specific to certain 'lifestyle' or age categories. The result is that Federated's penetration of private label at 17.4% of sales is significantly higher than that of

May at 13%. Given that Federated has publicly stated its aim to increase private label penetration to over 20% of sales, this presents a considerable opportunity at the acquired May stores.

The power of brand over regional identity

Another major motivation for the merger is the recognition of the power of Federated lead brands: Macy's and, to a lesser extent, Bloomingdale's. Indeed prior to the announcement of the May acquisition, Federated had already started to convert its regional department store nameplates (Bon Marche; Burdines; Rich's; Lazurus and Goldsmith's) to the Macy's brand (Table 6) attempting to leverage Macy's historic importance in US commercial and public life – not least Macy's Thanksgiving Day Parade in New York City (Wrigley and Lowe, 2002, 2003).

With May Department Stores currently operating from 12 nameplates¹, Federated has decided to further enhance its Macy's-focused marketing strategy on a national scale by converting the vast majority of the estate to the nameplate and gaining considerable scale economies in advertising as a result. The customer loyalty to Macy's that is built up and sustained by hundreds of thousands of customer visits each week can clearly be leveraged into new geographical locations. However, there are obvious risks – not least that retailers are embedded within the community and regional nameplates are a source of local pride (Landy et al., 2005). As a result, a sense of local disenfranchisement, felt in the short term by some customers is a key issue which the merged firm will have to sensitively negotiate - not least in Chicago where the venerated identity of Marshall Fields will be lost forever.

As the CEO of Federated recently made clear, the merger also allows Federated access to more affluent catchments currently inadequately served by the May stores.

¹ Famous-Barr, Filene's, Foley's Hecht's, Kaufmann's, Lord & Taylor, L.S. Ayres, Marshall Field's Meier & Frank, Robinson-May, Strawbridge's, and the Jones Store

‘May Company has many locations whose demographics are higher than what their current assortments would indicate, and we believe we will add considerable value there’ (FDS, 2005a, p 4).

In these more affluent catchments, Federated’s strategy will be to introduce its higher end Bloomingdale’s fascia - converting less well-suited mid-market May fascias such as Hecht’s or Stawbridge’s².

Reworking of merchandising scale

The final commercial argument for the merger centres on the fact that Federated has a superior system of buying and merchandising than May and has the potential to leverage this to the acquired stores. Similar to sophisticated food retailers such as Tesco, Federated centralises its buying yet attempts to remain sensitive to local markets by employing models of customer behaviour, affluence and catchment type (cf. Humby et al., 2003). Indeed, much of the popular criticism of US department store retailing has focused on the lack of tailoring of the offer to local markets resulting in a ‘sea of merchandise’ that is available but not adequately segmented (Wileman, 1993). As a result, much of the merger activity throughout the 1990s was centred on unleashing the potential economies of scale that exist in department store retailing, but were traditionally neglected due to a previous overly regionalised buying and operational focus (Wood, 2002a).

Federated’s strategy of micro-merchandising from a centralised organization is crucial to its success. The Macy’s Merchandising Group (MMG) support office³, using models of customer behaviour at the local level, allows more intelligent decisions to be made. As Federated CEO, Terry Lundgren commented,

² No decision has yet been made regarding any conversion of the May division, Lord & Taylor.

³ Until 2005 MMC was known as Federated Merchandising Group (FMG) and renamed with the divisional consolidation that left two Federated divisions – Macys and Bloomingdales - the latter of which merchandises some of its stores via Associated Merchandising Corporation (AMC).

‘We’re very focused on the location analysis of what the consumer wants in that particular store and market. To that end we have defined our customers into four segments – traditional, updated, neotraditional and contemporary....We have a.....distributor organization [MMG] whose responsibility is to tailor those assortments into these stores’ (FDS, 2005a, p 7.).

In addition to providing a lifestyle template specific to each store, MMG supplies a matrix of core vendors from which the Federated divisions are strongly encouraged to select. As Vice President of Federated, Carol Sanger suggested in an interview, the merchandising group ‘scouts the market and determines what everybody should look at....and makes some decisions based on economies of scale....but allow the divisions, where the customers see it, to have their own identity’ (Interview 3).

Historically the tension between local and centralised merchandising has been much more difficult to negotiate in fashion rather than food retailing owing to regional variations in demand (Wood, 2002b). Gradually a centralised model of organisation has emerged albeit with sensitivity to local markets so as ‘to enable the store management to maintain links to the buyers and strategists in head office as well as to the customers but within the structure of a very large firm’ (Dawson, 2000, p 125). It is these efficiencies that the merger has the potential to realise.

Conclusions

The Federated/May merger promises to be the last great consolidation of the US department store industry – a process that has a rich history and can be traced back to the 1920s with the construction of large ownership groups (Pasdermadjian, 1954), into the 1980s with the period of financial restructuring (Hallsworth, 1991; Rothchild, 1991), subsequent department store bankruptcies, followed by the round of strategic regional consolidations throughout the 1990s (Wood, 2002b). While the Federated/May merger has been waved through by the FTC given the strong wider

competition for department store retailers, further M&A activity by these operators will not escape regulatory action at the State level. In many respects therefore, the merger represents the last great ‘throw of the dice’ for these formerly powerful retail giants in a consolidation vital to the survival prospects of the sector.

However, Federated faces a tall order given that it is embarking on a defensive merger with a troubled retailer currently experiencing negative like-for-like sales in a sector itself characterised by low growth. Recent academic research has noted that the lead company must pay immediate attention to remove “them and us” perspectives and encourage a shared organisational identity (Marks and Mirvis, 2001). Therefore, the construction of a “Transition Team” containing executives from both companies has important symbolic as well as practical overtones, as does the commitment not to eliminate jobs before March 1 2006. Beyond cultural obstacles, the task to turnaround May by integrating the systems, retail fascias and customer offer remains the overarching challenge on the horizon.

The consolidation is indicative of the wider ripple effects spreading throughout the sector as retailers reassess their store portfolios in the light of the emergence of more efficient operators focusing on a handful of powerful retail brands. This has partly led to Saks Inc disposing of its Proffitt’s and McRae department store divisions to Belk Inc while Neiman Marcus Group (which also owns Bergdorf Goodman) has been taken private via its purchase by two private equity groups. These smaller transactions are likely to continue in the short term in moves, that while less extreme than the 1990s period of restructuring, are still fundamentally driven by the same imperatives of maximising returns through the realisation of operational efficiencies.

More broadly for the sector, this merger raises issues of retail regulation, market power, leveraging market scale economies, and tensions between spatial scales of buying and merchandising. The merger also has a distinct spatial logic. In turn, that triggers a geography of divestment which offers

the opportunity for competitors to gain footholds in markets - in the process transforming the competitive landscape of the industry. All these we believe, are significant themes worthy of attention by retail academics with interests in corporate strategy and market regulation.

Acknowledgements

We would like to gratefully acknowledge the continued input and assistance of Daniel Barry, Managing Director, Merrill Lynch New York and Howard Biederman. In addition, we are grateful for discussions with Terry Lundgren, current CEO of Federated, as well as Jim Zimmerman and Allen Questrom, both of whom were previous CEO's of the firm. Thanks also go to Hayley Myers on comments on a previous draft of the paper. The usual disclaimers apply.

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Figures

Figure 1: US conventional department store sales 1992 - 2004

Source: US Department of Commerce

Figure 2: Conventional & chain department store sales as a % of total retail sales 1992-2004

Source: US Department of Commerce

Figure 3: May and Federated like-for-like performance 2001-2004

Source: Company accounts

Figure 4: Federated and May Pre-Merger Store Geography

Located in a separate Powerpoint document

Figure 5: Divestment in California from Federated/May Merger

Located in a separate Powerpoint document

Tables

Table 1: Selected U.S. Conventional Department Store Acquisitions, 1990-2005

Date	Acquirer	Acquired	Cost (\$ bill) (If known)	No of Stores (If known)
1990	May	Thalhimers,	N/D	26
1990	Dayton Hudson	Marshall Field	1.40	N/D
1990	Investcorp.	Saks Fifth Avenue		N/D
1992/3	Proffitt's	Hess	0.21	18
1994	Proffitt's	McRae's	0.34	28
1994	Bon-Ton	Hess	N/D	20 and distribution centre
1994	May	10 stores from Hess's.	N/D	10
1994	Federated	Joseph Horne Co. of Pittsburgh.	N/D	N/D
1994	Federated	R. H. Macy	4.10	123
1994	Proffitt's	Parks-Belk	N/D	3
1995	May	16 Wanamaker and Woodward & Lothrop stores	N/D	16
1995	May and J. C. Penney	Woodward	0.46	N/D
1995	Federated	Broadway	1.60	82
1996	May	13 Strawbridge & Clothier stores	0.48	13
1996	Proffitt's	Younker's	0.26	51
1996	Proffitt's	Parisian	0.45	38
1996	Belk	Leggett Stores	0.92	
1997	Proffitt's	Herberger's	0.16	40
1998	Proffitt's	Carson Pirie Scott	0.96	55
1998	Proffitt's	Broady's	N/D	6
1998	Dillard	Mercantile	2.9	103
1998	Gottschalks	The Harris Company	0.04	9
1998	Proffitt's	Saks Holdings	2.10	96
1999	May	ZMCI	0.05	14
2001	May	Saks Inc.	0.31	9
2001	Target	Montgomery Ward	N/D	35
2003	Bon-Ton	Elder Beerman	0.09	68
2004	May	Marshall Field from Target	3.20	62
2005	Federated	May	11.00	491
2005	Belk	Proffitt's & McRae stores	0.70	47
2005	Texas Pacific Group & Warburg Pincus LLC	Neiman Marcus Group	5.1	51

Source: Author's database

Table 2: Leading conventional US department store sales, 2004

Department Store Retailer	2004 (\$ mill)	Implied Market Share of Conventional and Chain Department Store Sales**
Federated	15,630	17.8%
May*	14,441	16.4%
Dillards	7,529	8.6%
Nordstrom	7,131	8.1%
Saks	6,437	7.3%
Neiman Marcus	3,534	4.0%
Conventional & Chain Department Store Sales 2004	87,857	

Sources: US Department of Commerce and retailer's annual reports

* By the end of 2004, May was the largest department store operator given its acquisition of Marshall Field's.

** The US Dept of Commerce's definition of 'conventional and chain department stores' also includes operators such as JC Penney and Sears. Therefore, this analysis essentially underplays the concentration in the conventional department store sector if it was classified separately (which it is not).

Table 3 Major Department Store Rationalisation, 1985-2004

Fiscal 1985		
Company	No. of Divisions	Sales (\$ mill)
Federated Dept. Stores	11	6,685
RH Macy	4	4,368
Carter Hawley Hale	6	3,979
Allied Stores	17	3,349
May Dept. Stores	10	3,327
Associated Dry Goods	10	2,724
Batus	5	2,300
Mercantile Stores	13	1,880
Dillard Dept. Stores	5	1,601
Dayton Hudson	2	1,448
Nordstrom	1	1,302
Total	84	32,963

Fiscal 2004		
Company	No. of Divisions	Sales (\$ mill)
Federated Dept. Stores	2	15,630
May Dept. Stores	7	14,441
Dillard Dept. Stores	1	7,529
Nordstrom	1	7,131
Saks Inc	10	6,437
Neiman Marcus	2	3,534
Total	23	54,702

Source: Fiscal 1985 data from Goldman Sachs (1996) *Department Stores: Rediscovering the Reinvented*, Goldman Sachs Investment Research, New York, May 3, 1996, p 30. The remainder developed from company reports.

Table 4: Attorney General Rulings versus Initial Federated “fix-it-first” Divestiture Proposals

State	Original Federated “fix-it-first” submission	State Attorney General Ruling	Additional stores for divestiture (in excess of original “fix-it-first” submission)
California	22	26	4
Maryland	4	4	0
Pennsylvania	9	7	0
New York	1	3	2
Massachusetts	6	<u>7</u>	<u>1</u>
		47	7

Source: Reports from the Attorney General’s for the 5 States and press releases from Federated Department Stores

Table 5: Forecast beneficiaries of divestiture

Department Store	Current Geographical Market Focus	Region of likely gains
Nordstrom	West Coast & North-West	New York; New Jersey
JC Penney	Nationwide	Various locations – principally California
Saks	Nearly nationwide	California New Jersey, Illinois most likely
Neiman Marcus	Texas, Florida, California, New Jersey	Various but principally California; Florida; Connecticut, Illinois; Texas; New York; Ohio; Virginia

Source: adapted and developed from Merrill Lynch analysis

NB. It should be noted that Sears are likely to have the largest claim on divested stores. However, this retailer is excluded from this analysis as it is generally recognised as being outside of the conventional and chain department store sector

Table 6 : Consolidation of Federated fascias, March 2005

				Adding Macys to their name		
	Macys West	Macys East	Bloomingdale's	Rich's, Lazurus & Goldsmith's	Burdines	Bon Marche
2003 sales (\$bill)	4.2	4.7	1.9	2.0	1.3	1.0
Numbers of stores	146	93	36	71	61	51
Total gross sq feet (bill)	23.4	23.1	8.1	13.4	10.4	5.7
Employees	29,900	28,100	11,100	15,000	10,600	7,00
Markets	Southwest, Minnesota, Hawaii, Guam	Northeast, Mid Atlantic, Minnesota and Puerto Rico	Southwest, Southeast, East and Central	Southeast, Central and Pennsylvania	Florida	Northwest

Source: Federated Department Stores, 2004