SOCIAL ACTION, INNOVATION, REFLECTION AND EXCHANGE LABORATORY

12TH LASAIRE BIENNIAL

"Anticipation and Participatory Change Management in Companies during a Period of Crisis and Technological Change"

THE FNAC-DARTY GROUP

(by Christian Dellacherie)

FNAC/DARTY MERGER: A STRATEGIC OPERATION OR SIMPLY RACING FOR SIZE AGAINST THE AMERICAN GIANT AMAZON?

The two brands have just gone through a long period of crisis. The same is true of all specialised retailers. They have been rapidly impacted by the development of e-commerce, on several fronts. When it comes to cultural products, the first "victims" are music sellers, the most emblematic example of which is Virgin, a global giant pushed into bankruptcy because of lack of anticipation and insufficient investment. Electronic commerce, spearheaded by Amazon since 1995 in the United States, has been approached differently by the French chains. Launched in 1999, one year before the American giant arrived in France, the website fnac.com continues to be a powerful platform. According to the sociology researcher Vincent Chabault[1], buying on the Internet would not explain in and of itself the decline of the model of those retailers that held sway in the 1980s. The new modes of purchasing and ownership of cultural goods on the web should be underscored.

A survey[2] conducted among avid readers who visit e-commerce websites shows that online bookstores have given rise to the figure of the "*reader – consumer,"* who compares the websites, cross-checks information and seeks for free shipping and handling. Furthermore, in November 2003 Amazon launched a "marketplace"[3] geared to professional sellers and private individuals. There is another model of a reader-consumer who seeks to refer to the second-hand market and turns into an amateur bookseller to sell part of his library. Amazon.com lost money for a long time on each book sold because of its sizeable investments to expand and to secure the complete bibliographical description and digitisation of every document put up for sale, thereby establishing a global virtual store. Bezos, its founder, stemming from financial circles in Wall Street, is not concerned with books as such. He embarked on his "Amazonian"

[1] Lecturer at Paris Descartes and member of the Centre for Research on Social Ties (CNRS), author of *La FNAC entre commerce et culture (PUF 2010),* a book based on his doctoral dissertation.

[2] *Librairies en ligne*, Presses de Sciences Po, June 2013.

[3] Since then, most retailers, including Fnac, followed its lead…

adventure in 1994 because he foresaw the potential of Internet marketing, and opted for books as a point of entry because they are "*easy to ship and difficult to break.*"[4] Today, he uses information on customers that he has acquired through the sale of books to market a wide range of products. In fact, Amazon made a profit for the first time only in 2004, i.e. the year when equipment sales exceeded sales of cultural products. In July 2005, Amazon launched its French electronics section, selling such items as LCD TVs. In 2006, Amazon diversified and launched its *Amazon Web Services* (AWS)[5] based on a *cloud computing* platform.

For Fnac as well as for Darty, this occurrence has entailed, well before the offer of purchase, the adoption of an omni-channel sales strategy in the store and sales on line (click and mortar), offering the withdrawal from a store of an object sold online (click and collect).[6] In the first six months of 2015, omni-channel sales at Fnac approached the 48% mark of orders, and at Darty, the product pickup rate in the store compared to articles sold on line largely exceeds the 30% mark. These signs have the advantage of strong name recognition and a large territorial coverage thanks to their network of stores that they are actively trying to expand through franchising. The competition remains very keen and it is not limited to Amazon and its emulators: "all the retail players are competing with us," Alexandre Bompard, CEO of Fnac repeats endlessly: "Carrefour with Rueducommerce, Casino with Cdiscount, Auchan avec Boulanger and Cultura, Leclerc with its cultural spaces." Accordingly, Fnac management considers that the "exit from the crisis," heralded by positive results after several years, remains fragile.

The acquisition of Darty has given rise to a bidding war, leading to an overvaluation of the share, given Darty's liabilities (negative equity and debt). The cost of acquisition is some 100 times Darty's results in 2014/2015. Doesn't this risk weighing down the profitability of the operation? The management of Fnac considers that, even if it would have preferred to avoid this episode, it did not go beyond what is reasonable. By way of proof (or as an indicator), it points out that the share has gone up by 30% since, thereby attesting to the confidence of the markets in the merger's success. The overbid was the result of a struggle between Fnac and Conforama. We can continue to question the objectives[7] of the South African group Steinhoff International, which counts Conforama as a subsidiary after the latter was sold in 2011 by the PPR group (to which Fnac belonged at the time…). Unlike the managers of Fnac, for whom the concentration of players is presented as inevitable in the struggle against Amazon, the American giant does not appear as a direct global competitor for Conforama, because it is not very positioned on furniture and seems to have decided not to establish a foothold on the sector of large household appliances.[8] Furthermore, after (and undoubtedly in response to) the Darty episode, Conforama entered into a partnership with Casino for its purchases in France and then abroad, which it would have probably done with Darty, had it managed to acquire it. The two distributors have thus created a central purchasing organisation christened "SICA" (Steinhoff International Casino) to manage jointly a volume of purchase exceeding €1 billion, concerning Conforama France and all the companies of the Casino group that distribute household appliances, including Cdiscount.

[4] Comments reported by Georges Packer, journalist at the New Yorker, writer and playwright.

[5] AWS offers a set of products such as the online storage service with *Amazon Simple Storage Service* (Amazon S3), the cluster of servers on demand *Amazon Cloud* (Amazon EC2), the payment service (Amazon FPS) etc...

[6] The SNCF [French Rail] is a pioneer of this strategy in France…

[7] We should point out that Conforama has lost nothing in the case, because the overvalue of the Darty share is expected to bring in some €40 million in capital gains…

[8] But, as we shall see further, the Amazon war machine continues to be deployed and its system may extend in all fields of commerce…

The inflation in the price of the Darty share forced Fnac to resort to debt and undoubtedly induced the simultaneous arrival of a new shareholder (Vivendi). Is this an "ordinary" financial operation or should it be seen as the beginning of a strategic partnership? The new cultural agitator which Vincent Bolloré, the boss of Vivendi, aspires to be (or to appear), willingly presents himself as "*standard bearer of European culture in the face of American entertainment and Asian abstruseness"*[9] with, in addition, a target for the longer term, the African continent where his industrial group has been a long-time investor. For the management of Fnac, such a partnership seems capable of falling in line with a drive to enhance its global positioning and to broaden its mix of products by combining a publisher of contents and a distributor. Nevertheless, the current behaviour of Vincent Bolloré on Canal+ and on I-télé does not seem to presage a deliberate and bold vision from a specialist of financial "coups." The strategic inspiration of Fnac appears to be, if not guided at least very influenced by the "example" of Amazon. The reference to the American giant is ubiquitous, they are fascinated by its "unprecedented power," its capacity for global initiative. Amazon is constantly innovating. Its «Kindle Direct publishing» has enabled young writers to publish their novels online in the form of e-books, often after being refused by publishers several times, and thus to reach millions of readers and get 70% of the selling price, compared with the "30% maximum" paid by a conventional publisher. Amazon, already n° 1 in the distribution of digital books, wants to control the production thereof. It strengthens its publishing capacity in Europe to "gain greater control over the entire chain" by feeding the offer for its Kindle reader, launched in 2007. If, under pressure from Amazon which weighs on (or even cuts) prices,[10] and therefore on publishers, the publication of physical books were to decline continuously as digital books expand, Amazon, which has a very large part of this market, will have the means and resources to promote selecting books based on discussion groups, polls and computer algorithms, rather than on the judgements of publishers, then bookselling professionals, on the literary value or quality of the contents. One of the winning assets of Amazon Publishing is also that it is a worldwide striking force, and is therefore able to promote its authors on an international scale. That is why certain genres that are easier to export are given priority: sentimental literature, thrillers, historical novels, etc. It is a different rationale from that shared by publishing bosses, far removed from the idea that European tradition has of the world of books, obviously very far removed from that of the first generation of France "expert sellers," a "sales force" to whom the company's image still owes a lot.

"If you do the same thing as Amazon, you have every reason to lose," Régis Schultz, head of Darty since 2013, told the magazine Challenges. It is obvious that the management of Fnac has its eyes constantly riveted on what the American ogre is doing to try and do so in turn. It has thus decided to compete head on with Amazon on cultural and electronic products using a subscription model similar to that initiated by Amazon in 2005, which has developed spectacularly throughout the world since. With an annual subscription, members no longer pay any shipping and handling charges for their orders (provided they do not request a particular delivery option). Amazon Prime subscribers in the United States spend more[11] ($1100 on average per year, compared with $600 by standard customers), are increasingly more numerous (54 million in the US at the end of 2015, 63 million at the end of June 2016, or more than one out of two American households). This naturally leads to an increase of deliveries and a reduction of the margin. But as is the case in ordinary food and

[9]« *Vivendi:la stratégie de Vincent Bolloré en question »,* Le Monde Economie § Entreprise, 18 November 2016
[10] Which is not possible in France because of the Lang law. It should be borne in mind that the conventional bookstore has almost completely disappeared. It cannot be ruled out, that this very same law, which the founder of Fnac had vehemently opposed in the name of defence of the consumer, will not provide protection, including for Fnac.
[11] Notamment grâce aux « irrésistibles » opérations de recrutement que sont les Prime Days...

non-food retail, Amazon's business is absolutely not to sell products, but to capitalise on the money spent by its customers. Thanks to the enormous volume of sales, the inventory is renewed every 20 days. Bearing in mind that the standard terms for paying the supplier are around 45 days, Amazon is sitting on a lot of money that it can make grow in an intelligent – and above all far more lucrative – manner than on focusing on margins. Are the others capable of doing so on the same scale, or is something else needed in a different cultural universe? The same question arises concerning local management methods, digital "policing" methods and often inhuman working conditions, particularly in warehouses. It is only by understanding its modus operandi in depth that we will be able to find solutions and develop alternative offers to the omnipotence of Amazon and other major Internet industries.

In a nutshell, the competitive environment is very dense and is dominated economically and symbolically by Amazon. The "omni-channel" strategy that has enabled the two brands Fnac and Darty to resist does not constitute all-risk insurance against the established power of the American giant, and its capacity to develop and innovate. The merger will make it possible to boost the purchasing power of the new company and to expand the diversification of the products sold by Fnac, initiated[12] in recent years, on more promising markets than cultural products, in particular CDs and DVDs. Beyond this foreseeable result, can it become the basis for a redefined strategy by relying on a synergy between the two brands? They both have an image that remains strong; Fnac, based on its cultural "capital" which enables it to continue to create or support events; Darty based on the quality and reputation of its after-sales service. Will the new group under construction aspire to rely on the "digital revolution" to give itself the means to imbue new dynamism into those images by updating them?

TWO PROCESSES ARE ALREADY LAUNCHED

A double process has just been launched by the management of Fnac. The first in the summer, in the wake of the success of the financial operations, consisted of the creation of 12 workgroups of 6 to 20 persons, equally divided between the two brands, corresponding to 12 key areas including logistics, services, commerce, the Internet, franchise, etc. Fnac and Darty are now in the process of building a single group, a European leader in specialised distribution, capitalising on their respective expertise and the marketing approach of each brand. The second launched by a presentation to the respective works councils is described in a draft method agreement[13] that provides in particular for the creation of an "ad hoc body at group level known as the trade union coordination committee," the composition of which was decided after discussions with the works councils of Fnac SA and UES Darty Paris Ile-de-France. The management of Fnac proposes that the purpose of this committee must be to "receive information on the plan to merge the headquarters gradually as it is defined, using this information, which would make it possible to **negotiate and conclude agreements."** It moreover proposes that in case of success, "this innovative approach to the social dialogue" helps "sustain this new model and its deployment" in the group. This proposal has already come under fundamental criticism from the trade union, because it questions the principle of the trade union's negotiation monopoly. The proposal of management defines the schedules of the different stages concerning the coordination committee and the consultations of the works councils and the committees on hygiene, safety and working conditions of the two brands. The coordination and consultation process should last until 15 June 2017. As indicated in the introduction to its proposal, the management of Fnac considers that the "birth of this leader in the omni-channel distribution of technical, cultural and household

[12] Marginal, without really being able to measure the success.
[13] Cf. the summary appended.

appliance products in France opens up tremendous development opportunities for the two brands, which can provide an enlarged offer and benefit from better negotiation power among suppliers." It continues by stating that "bringing Fnac and Darty together, and identifying and implementing synergies, is a far-reaching process that will take time." The latter task has been assigned to the aforementioned 12 workgroups, but nothing of their investigations or initial guidelines or possible conclusions has filtered through yet.[14] Now, essential aspects of proposals made about the tasks of the coordination committee and their schedule seem delicate in the absence of this information, which has already elicited reactions from the trade unions. The statement in the introduction to the effect that "respect, throughout the process, of the identity and culture of each brand, a heedful ear for the employees and social dialogue will be accorded our undivided attention to build a shared future together and to devise the organisations of our new Group," appears in fact to require an osmosis between the two processes, one for reflection on the organisation and the other on consultation. Fnac announces savings of ca. €130 million, probably by reducing the workforce in "support positions" (administrative, IT, and logistics). The trade unions are talking about 250 to 500 jobs cut. The simple reduction of costs cannot constitute an efficient strategic vision, especially in the case of extensive debt. Many economists think that the size race makes sense only if profitability is obtained and if the corporate project is shared massively by the employees.

BRIEF HISTORY AND KEY CHARACTERISTICS OF THE 2 GROUPS

***Fnac**:*

- Created in 1954 (Fédération nationale d'achat des cadres [National Purchasing Federation of Managers]) initially focused on photography products and records and, as of 1965, ticketing;
- 1974: introduction of books; 1980: launch on the Paris stock exchange; and 1981 opening of outlet abroad (Brussels);
- 1993: establishment in Madrid, with the Crédit lyonnais being the principal shareholder; 1994: acquisition by the Kering group (Pinault Printemps Redoute); 1999: creation of the website fnac.com; 2013: leaves the Kering group and is relaunched on the stock exchange; 2015: bid to acquire Darty; 2016 Vivendi acquires a 15% shareholding state;
- 14100 employees, of whom 8489 in France, 3962 in Belgium and Switzerland, 968 in the Iberian peninsula and 888 in Brazil;
- Turnover in 2015: €3.88 billion, 37% from editorial products, 58% from technical products, 5% from services (ticketing, etc.); 199 stores; ca. 15% of sales on the web (3rd e-commerce website in France)…

***Darty**:*

- Created in 1957; acquired by its employees in 1988, then acquired by the British group Kingfisher in 1993;
- Kesa, electrical appliances branch of Kingfisher comprising Darty, But and Comet, is disposed of in 2003; But is sold in 2007, Comet in 2011 and Kesa is rechristened Darty in 2012; refocusing of activities in France and the Benelux (disposals in the UK, Italy, Spain, Turkey, the Czech Republic, Slovakia, etc.); 2014, acquisition of the e-commerce website mistergooddeal…

[14] "Wagging tongues" say that nothing will come out before Christmas so as to "protect" the year-end sales…

- More than 12000 employees;
- Turnover: €3.66 billion (80% in France and 20% in the Benelux).

ANNEX 1

AMAZON, CDISCOUNT, FNAC: THE UNLIMITED DELIVERY MATCH

Apprehensions… that are rather justified, if a recent study by Consumer Intelligence Research Partners is to be believed. In his Amazon Premium service (called Amazon Prime in the USA), Jeff Bezos seems to have found the lethal weapon, in fact. It runs on the following principle: Members take out an annual subscription and are no longer charged any shipping and handling charges (provided they do not ask for a particular delivery option). Prime subscribers in the US spend more ($1100 on average per year, compared with $600 for “standard” customers), are increasingly more numerous (54 million in the US at the end of 2015, 63 million at the end of June 2016, or more than one out of two American households), particularly thanks to the irresistible recruiting operations known as the Prime Days. All these customers are lost to other distributors…... often for good.

CDISCOUNT IS 60% CHEAPER

Far from crazy, the latter have felt the threat. For two years, the main challengers of Amazon in France, Fnac and Cdiscount, have also launched their delivery service by subscription. Do they have sufficient winning assets not to be crushed by Amazon? To find out, we analysed what Amazon Premium, Cdiscount à volonté, and Fnac Express+ have to offer.

First element of comparison: the price. With an annual subscription of only €19, Cdiscount stays true to its positioning of price cutter, and is significantly cheaper than its 2 competitors (€49 for Amazon and Fnac, with the latter offering a €10 rebate for holders of its loyalty card). Unusually, Amazon is not the lowest bidder. But it has a powerful argument nonetheless: from nephew to grandmother, a Premium member can have any member of his family use the subscription, at no additional cost.

SCOPE OF THE OFFER: AMAZON TAKES ALL

Conversely, there is no contest when it comes to the number of references. With 200 million references, the Amazon supermarket is far better stocked than Cdiscount (15 million products) and Fnac (10 million). The merger with Darty should enable the latter to catch up somewhat.

The ratio is even more lopsided when one of the flagship arguments of these offers of delivery by subscription is taken into account, because Amazon is the only one that undertakes to deliver products offered by some merchants in its market place. Neither Fnac’s "Vendeurs partenaire" [partner sellers], nor the "C le Marché" merchants [play on words meaning that’s the market] at Cdiscount (which accounts for the overwhelming majority of references, as the Bordeaux-based website markets only 150,000 references itself) are concerned by this option.

4 MILLIONS “PREMIUM” FRENCHMEN THIS YEAR?

The results of this marketing offensive? On this issue, certainly for Fnac.

ANNEX 2

Amazon is well on its way to monopolizing book distribution. Its strategy is like Walmart's.

First you gain an initial advantage through economies of scale and introducing new efficiencies. So far, so good. That is how free enterprise is supposed to operate.

Then you leverage your initial advantage in the marketplace to squeeze suppliers and lower your costs. This enables you to keep prices low so as to knock out small competitors and keep new competitors from emerging.

Meanwhile you treat your rank-and-file employees like dirt.

The parallel is not complete, because the current Walmart owners are destroying their company through their short-sighted greed and stupidity, while Jeff Bezos, the founder and CEO of Amazon, may be greedy but he is anything but short-sighted and stupid.

And he is just getting started. According to one analyst, 93 percent of Amazon's $75 billion in annual revenues come from products other than books.

George Packer, writing in the New Yorker, says that 50 to 60 percent of the price of a book sold through Amazon goes to Amazon itself. Another 10 to 15 percent goes for sales, warehousing and shipping. What's left over covers printing, editing, publicity and, oh yes, royalties to the author and, oh yes, any profit the publisher may earn.

This is new. Historically retailers got 30 to 40 percent of the price of a book.

It is illegal for retailers to demand special discounts from publishers, but, according to Packer, Amazon gets around that by charging "cooperative promotion fees." Amazon charges publishers this fee for placement of a book title on its page. Most of the ranking of books on Amazon's lists are determined by these fees. The few publishers who have been brave enough to refuse to pay this fee have found there is no longer a "buy" button on Amazon's page.

"The only point at which Bezos enters the chain is to take all the money and the e-mail address of the buyer," Colin Robinson, a publisher, told Packer. "There's an entire community of people and Bezos stands in the middle and collects the money."

While Amazon offers bargain prices, its squeeze on publishers is bad for literature in the long run. Bezos seeks to transition from physical books to digital books, from which Amazon has 90 percent market share. If traditional book publishing dies out, Amazon will step into the gap, with book selection based on focus groups, surveys and computer algorithms rather than editors' judgments of literary value.

Packer reported that Bezos doesn't care about books as such. He started Amazon (named for a river into which all things flow) in 1994 because he had vision enough to foresee the importance of Internet marketing, and he chose books as his entry point because they are "easy to ship and hard to break". Now he uses the information on customers he gained through book selling to market a wide array of products.

The saving grace of a well-ordered free enterprise system is that when big business executives overreach themselves, there is an opportunity for a smart entrepreneur to jump into the gap they leave. Such is Colin Robinson, who has started a publishing firm called OR Books, which bypasses Amazon and sells directly to consumers. OR Books gives up sales but earns a higher profit which, presumably, can be shared with the author.

Robinson is able to stay in business because of Net Neutrality the law that says Internet service providers have to provide service to all customers on the same terms. There's currently a legislative drive to abolish Net Neutrality (and some say the proposed Trans Pacific Partnership Agreement has an anti-Net Neutrality provision). If that were to happen, dominant businesses such as Amazon could squeeze out small competitors by demanding special terms from IPPs, just as Amazon does with publishers.
Another public policy favorable to Amazon is anti-trust policy. Historically anti-trust laws were directed against "the curse of bigness". But in the Carter-Reagan years, policy-makers decided that it was all right for a company to dominate its market if there was some benefit to consumers. The problem with this reasoning is that the benefit to consumers is likely to last only so long as the dominant company has effective competition. Without competition, the benefits of efficiency and economies of scale don't necessarily flow to consumers.

Click on **Cheap Words: Is Amazon Bad for Books?** to read the whole article by George Packer in the New Yorker. It's long, but packed with good information.

Click on a review of **Brad Stone's *The Everything Store*** by Deborah Friedell for The London Review of Books for more. Her review has additional good information that's not in the Packer article.