

Adaptive Strategies for Japan's Retail Industry Facing a Turning Point

— Rebuilding corporate strength to respond to change with agility —

Hirokazu TAKEI, Ken-ichi KUDO, Tomoaki MIYATA, Yoshifumi ITO

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Since the Meiji Restoration, the structure of Japan's retail business had been changed substantially four times. At these turning points, major changes always occurred in the following aspects: "population," "income," "competition," "technology" and "legal framework," which led to the emergence of new retail formats. Japan's retail industry has grown by following such processes. Looking at the current situation, we find that Japan's retail industry is just now facing the fifth turning point.

While overall real consumption expenditure in Japan is expected to remain at the same level from the mid- and long-term perspective, increases or decreases in real consumption expenditure will become apparent by area, products and age bracket, accelerating mosaic patterns of consumption expenditure in the market.

According to our survey, the consumption behavior of seniors who will be important target consumers in the future can be characterized by their preference for relatively short travel times to stores and a relatively strong inclination towards one-stop shopping. It is also possible to measure the strengths and weaknesses of each type of retailer based on consumer ratings of each retail format.

New retail formats that are assumed to emerge during the fifth turning point include the neighborhood shopping center (NSC) that can respond to the consumption characteristics of seniors. Another possibility is the emergence of new retail businesses in the blank fields on the map of retail formats that have been created because of competition among different retail formats in recent years. Nevertheless, at this turning point, the retail industry faces major but uncertain changes in the competitive environment. Accordingly, retail companies must not only focus on the development of new formats, but also promote restructuring within their company to increase the probability of growth, thereby rebuilding corporate capabilities to meet any possible changes with agility.

I Japan's Retail Business Meets a Turning Point

In looking at the history of Japanese retailing since the Meiji era, we find that there seems to be a dynamic process wherein new formats emerge and others fade away. This phenomenon appears to be governed by a rule that transcends time and place. Those formats that adapt to major changes in the environment flourish, while those that do not adapt decline and fail. Factors leading to such major environmental changes include those related to “population,” “income” and “competition,” as well as “technological innovation” and “legal reforms.”

1 Factors Leading to Innovation in the Retail Business

After the Meiji Restoration, Japan implemented a policy of increasing production and promoting industry. This led, at the beginning of the 20th century, to an explosive increase in the population and incomes in urban areas. In addition, because of the development of the railway network, it became much easier for people living in rural areas to travel into the cities to shop and so on. This was the first turning point for the retail industry.

It was these changes that led to the appearance of a new format, namely, department stores. Department stores grew as they became “the place to spend time” where people could become exposed to the latest western culture. These large and fascinating stores offered a wide selection of Japanese and western clothing and foodstuffs, and attracted many consumers. Compared to other stores available at the time, department stores were characterized not only by a wide selection of goods available for purchase, but also by a business model that depended on gathering customers from a wide range of commercial areas.

Between the Great Kanto Earthquake in Tokyo (1923) and World War II, retail innovation did not occur. However, with the war over and the coming of the 1950s, the industry reached its second turning point. The “Second Department Store Law” (enforced in June 1956; regulating the establishment and expansion of department stores, and selling methods used by the department stores) imposed much stricter regulations on the department stores. In addition, this decade saw the importation of cash registers (as an innovative technology) and their impact on retail business. The fifties also saw increases in the incomes of “salaried worker households,” with the average per-capita income of Japanese people rising steadily. The retail format that emerged through adapting to these environmental changes was a “general merchandise store (GMS).”

In 1957, Daiei Pharmaceutical Industries (now Daiei) opened retail stores and proposed “total life” for the households of salaried workers in residential areas

throughout the country. Its large-scale stores offered food, medicine, clothing, furniture and home electrical appliances—all at low prices. From the perspective of business operations, Daiei introduced self-service stores that used cash registers at checkout lines on a nationwide basis. The fact that restrictions had been imposed on department stores (that had been the retailing giants up until then) worked favorably for Daiei. As such, Daiei was successful in steadily increasing the number of its stores.

The 1970s saw various environmental changes that included an increase in the population of suburban dormitory towns, a temporary drop in incomes due to two occurrences of an oil crisis, fierce competition between GMSs, the decline of small, individual stores, and strengthened regulations imposed on GMSs by the Large-Scale Retail Store Law. Under these circumstances, the retail format of convenience stores that targeted small commercial zones of a 500-m radius had grown. This was the third turning point.

In 1974, York-Seven (now Seven-Eleven Japan) opened its first convenience store. Each of the stores of this chain had its own specific group of target customers, and stocked goods that would specifically appeal to the target group. By providing “convenience” as an added value, these stores did not sell merchandise at a discount. Seven-Eleven Japan continuously implemented reforms and achieved continued success and growth. Specifically, the characteristic business functions adopted by Seven-Eleven Japan included a franchise system, standardized stores and work practices, “Tanpin Kanri (unit control),” team distribution, direct central buying, team merchandising with manufacturers and the use of POS terminals for marketing.

The 1990s brought the fourth turning point for the retail industry. The collapse of the bubble economy led to a prolonged slump in the market. Deregulations such as the Large-Scale Retail Store Law brought about changes in the competitive environment. Consequently, so-called “category killers” grew, which overwhelmed other formats in their business (product) category with their strength. These category killers included volume retailers of home electrical appliances, home centers, drugstores, etc. In addition, the number of large suburban shopping centers (RSC: Regional Shopping Centers) also increased. In contrast, we find many downtown areas where shopping malls are losing their competitiveness and are becoming known as “shuttered malls.”

As such, when we consider the history of the retail business from the time of the Meiji Restoration, we can see that there have been four major turning points.

2 The Fifth Turning Point

Considering the current environment, the retail industry seems to be facing another major change such as the four turning points described above.

From the perspective of “population,” accelerated trends have been seen in Japan towards a declining birthrate and an aging society. Starting in 2005, the population actually began to decrease. Regarding “income,” many are noting how incomes have polarized (differentials have expanded). In addition, the lump-sum payments received when a baby boomer retires must be having a major influence. When we then look at “legal reforms,” amendments to the first two laws among the following three urban planning laws have recently passed the National Diet: the City and Town Planning Law, the Law on Improvement and Vitalization of City Centers and the Large-Scale Retail Store Location Law. Through these amendments, essentially strict regulations will be imposed on the construction of large-scale stores having a floor space exceeding 10,000 m² in rural areas.

From the perspective of “technological innovation,” we find that there are several major environmental changes. These include the development and spread of IT (information technology) and the planned introduction of GDS (Global Data Synchronization) in 2007, which will enable global sharing of product information.

These changes in the business environment are more than sufficient in scale to give rise to the emergence of new formats as well as to trigger the extinction of existing formats. We can say that each retail format, faced with this fifth turning point since the Meiji Restoration, stands at a crossroads with the route it takes determining whether it can survive (Table 1).

II Zero-Growth in Real Consumption Causes Major Changes in Consumption Patterns

Before we examine how existing formats adapt to these environmental changes, or what the new formats are that will emerge and grow, we must adopt a macroscopic view of how consumption patterns are changing.

First, how are Japanese consumption patterns being affected by the decline in population?

When Japan entered this era of declining population, there had been varied projections of GDP (gross domestic

Table 1. Environmental Changes Leading to Innovation of the Retail Formats and Growing Formats

Turning point		1900s (1st turning point)	1950s (2nd turning point)	1970s (3rd turning point)	1990s (4th turning point)	2010s (5th turning point)
Environmental factors and changes	Population change	Centered on urban areas	Increase in number of salaried workers, nuclear families	Increase in population of suburban dormitory towns	Return to urban areas	Decline in population, retirement of baby boomers
	Change in incomes (economic climate)	Increase in incomes of persons living in urban areas	Increase in incomes of households of salaried workers	Oil crisis	Collapse of bubble economy and deflation	Polarization of incomes, mosaic pattern of consumption expenditure
	Changes related to competition			Excessive competition among GMSs, decline in small, individual stores, price-fixing by stores affiliated with electrical manufacturers	Declining appeal of centers in rural areas	Excess stores and competition between different formats
	Technological innovation	Railways, escalators	Cash registers, development of private railway network	Increase in automobile ownerships, POS	Development of regional road network	Spread and advance of IT, update of IT infrastructure (GDS), RFID, etc.
	Legal reforms		Second Department Store Law	Large-Scale Retail Store Law	Large-Scale Retail Store Location Law, urban redevelopment, deregulations governing urbanization control areas	Three urban planning laws
Growing formats		Department stores	GMSs (general merchandise stores)	Shopping centers, convenience stores, “category killers” (volume home electrical appliance retailers, etc.)	Building complexes, large-scale suburban shopping centers	NSC (neighborhood shopping centers), mail order/online shopping

Notes: GDS = global data synchronization, POS = point of sale information management, RFID = radio frequency identification.

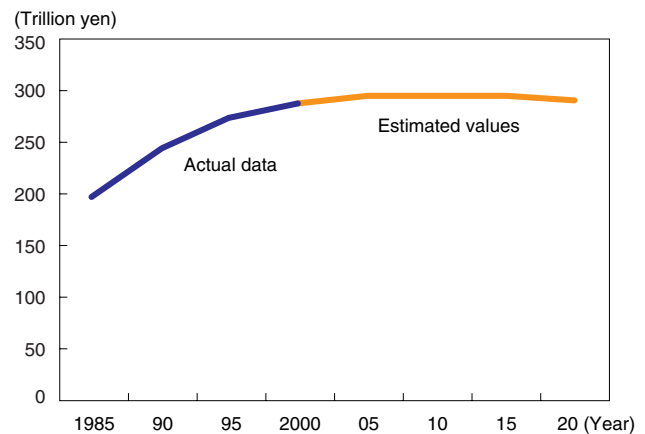
product) and consumption expenditure. Depending on the assumed preconditions such as consumption taxes and labor force, one prediction was for continued growth in the future, while others forecast a shift to a decline in growth.

In this section, we estimated the amount of real consumption expenditure for about the fifteen years leading up to 2020 by considering only changes in demographic data. These changes include a high probability of a declining population and a slight increase in the number of households (due to there being fewer people per household) as well as an aging society. We found that real consumption expenditure in Japan will remain flat until 2015, and will then fall slightly after that (Figure 1).

A notable point that this estimate revealed was that it is possible to clearly identify those areas where consumer spending will increase and those where it will decrease. For the years from 2005 to 2010, the separation will become distinct between those areas in which consumer spending will increase and those in which it will decrease. As we move towards 2020, the difference in consumption expenditure between these areas will

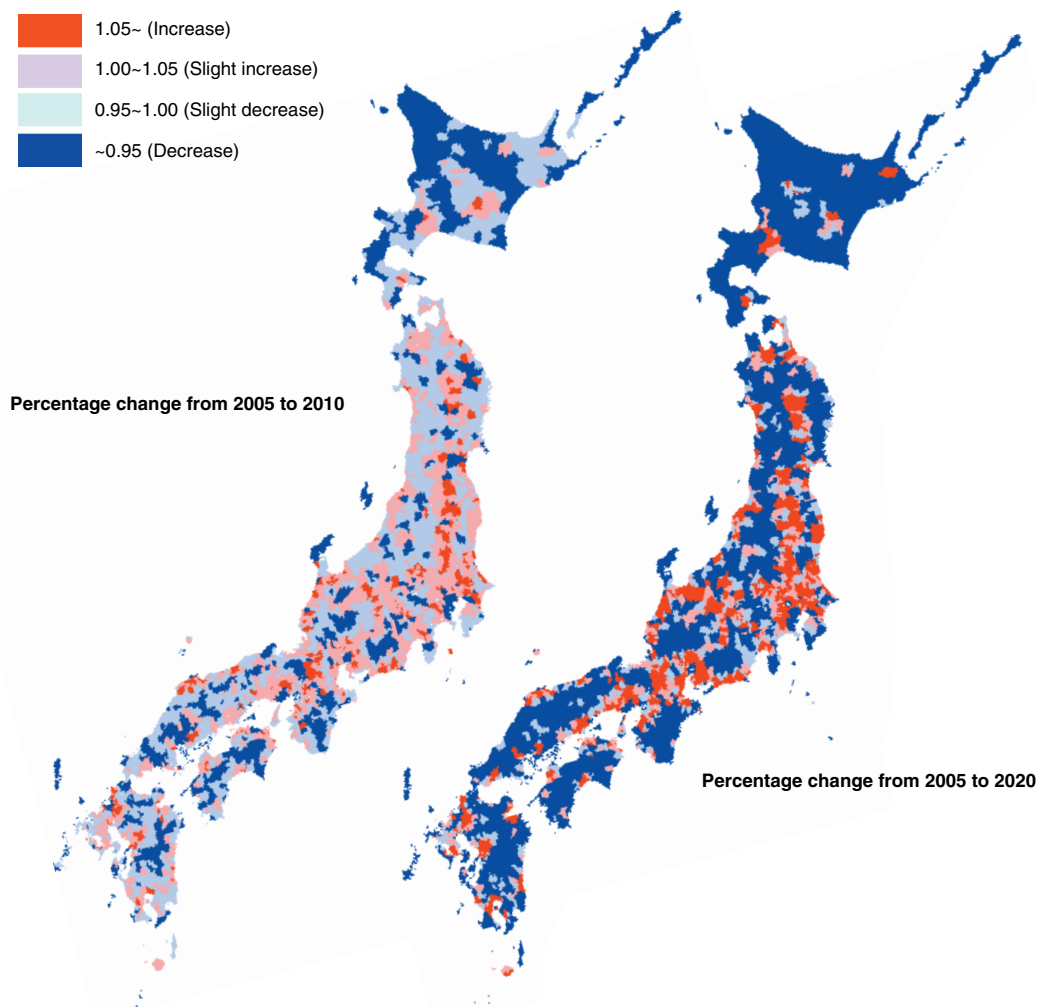
increase further, accelerating the “speckled” or “mosaic” patterns of consumption expenditure (Figure 2).

Figure 1. Estimate of Future Japanese Real Consumption Expenditure



Source: Actual data are based on “National Account for 2004,” the Cabinet Office. Estimated values are based on “Household Projections for Japan by Prefectures, August 2005,” the National Institute of Population and Social Security Research, “National Survey of Family Income and Expenditure for 1999,” the Ministry of Internal Affairs and Communications, etc.

Figure 2. Accelerated Trends towards Mosaic Patterns of Consumption Expenditure in Japan



Note: Projections of percentage change relative to the amount of real consumption expenditure by municipalities.

Source: Estimated based on “Household Projections for Japan by Prefectures, August 2005,” the National Institute of Population and Social Security Research, “National Survey of Family Income and Expenditure for 1999,” the Ministry of Internal Affairs and Communications, etc.

This growing difference in the increase/decrease in consumption expenditure by area is, over the medium to long term, not only important in deciding where to open new stores but also in estimating whether sales in existing stores will rise or fall.

In the future, the retirement of more and more baby boomers and their receipt of lump sum payments will also result in a major difference in spending by age bracket. This, again, will be another major environmental change for retail businesses. For example, between 2005 and 2010, the age of those households currently aged between 55 and 59 (age of the head of household), known as the baby boomers, will become 60 to 64. (Below, households are classified by the age of the head of household and, for example, called “60 to 64 households.”) As a result, in 2010, annual expenditure by 55 to 59 households will fall by about 1.7 trillion yen, while that of the “baby boomer” (60 to 64) households will increase by about 0.7 trillion yen.

The amount of consumption expenditure per household by the 55 to 59 households greatly exceeds that of other household categories, while the amount drops for the retired 60 to 64 households. This tendency is one of the reasons why the drop in the amount of consumption expenditure by the 55 to 59 households in 2010, caused by the drop in the number of such households, cannot be compensated for by the increase in spending by the 60 to 64 households, caused by the increase in the number of such households. As Japan’s society ages, annual spending by households aged 75 and above will increase by about 1.4 trillion yen (Figure 3).

Accordingly, while the overall amount of consumer spending will not increase, this disparity in consumption expenditure according to the age of the consumer has a huge effect on retailers.

III Direction of Changes in Consumption Behavior

In October 2005, NRI conducted a questionnaire survey in an attempt to clarify the current and future status of Japanese consumers in terms of consumption behavior and store selection.

The Internet was used to conduct this survey, in which 500 people in Tokyo’s 23 wards participated as well as 3,500 people in six prefectures in the Tohoku region (Aomori, Iwate, Akita, Miyagi, Yamagata and Fukushima). Because the survey used the Internet, middle-aged and elderly respondents were considered at least familiar with IT, and were likely to have been comparatively active.

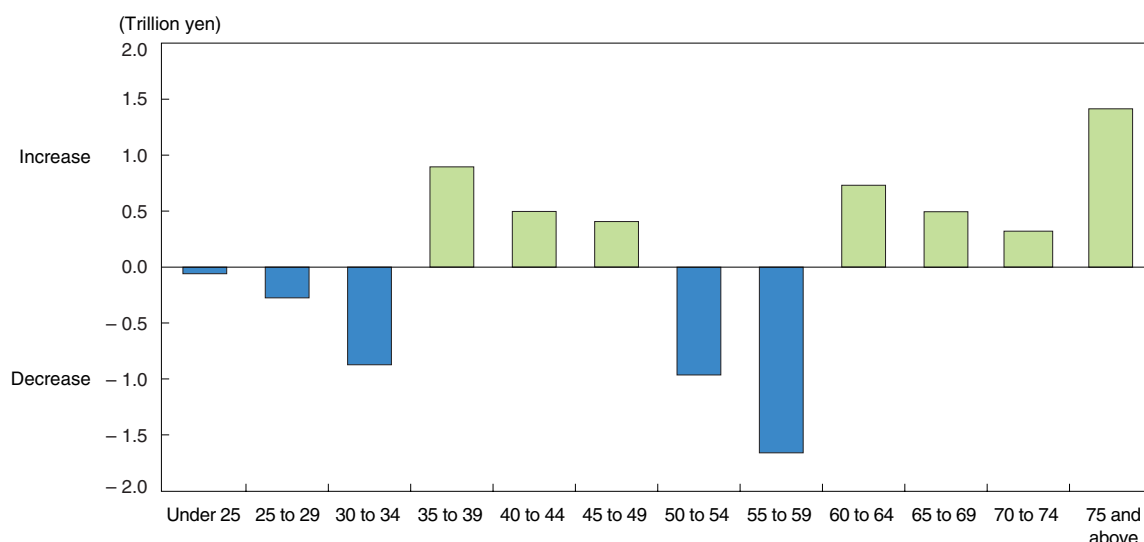
In addition, to ensure that the respondents shared the same ideas concerning the types of retail formats (e.g., the differences between GMSs and supermarkets), they were provided with a table listing the formats together with actual store names in their respective areas. The results were weighted based on age to take the makeup of the population into account for each prefecture.

The major findings of the survey are given below. The classification of each age segment is based on: senior segment = 50s and 60s, middle-aged segment = 30s and 40s, and young segment = 20s.

1 Towards an Era of “Region-Based” Competition

In the past, every prefecture had a local department store—often located in the vicinity of the prefectural office—that formed the summit of the retail pyramid in that prefecture. In recent years, however, department

Figure 3. Potential Household Consumption by Age Bracket (2005 to 2010)



Note: Projections of the amount of increase/decrease in consumption expenditure by age bracket of a household head in households consisting of two or more members.

Source: Estimated based on “Household Projections for Japan by Prefectures, August 2005,” the National Institute of Population and Social Security Research, “National Survey of Family Income and Expenditure for 1999,” the Ministry of Internal Affairs and Communications, etc.

stores based in major cities such as Tokyo, Osaka and the so-called “regional capitals,” have begun to attract customers away from these local department stores.

In the Tohoku region, the city of Sendai is a regional capital and is also capital of Miyagi Prefecture. It has been revealed that the high demand for department stores is being absorbed by the department stores in Miyagi Prefecture from the other prefectures in the Tohoku region (Figure 4).

This trend is most apparent in Yamagata Prefecture, with 8.6 percent of local department store demand being absorbed by the department stores in Miyagi Prefecture (Sendai City). Similarly, those same department stores are absorbing 5.6 percent of the demand in Fukushima Prefecture and 2.6 percent of that in Iwate Prefecture. Given that the department store industry makes or breaks with a 1-percent difference in sales, these figures obviously have a major impact.

With these consumption behaviors as a background, we will see an accelerated trend toward the restructuring of retail formats. In particular, local department stores located in cities other than regional capitals must develop new market positioning and a new format that can win the “prefecture- and region-based” competition.

2 Keywords to Tap the Senior Market are “Leisure Pursuits” and “Safety”

There has been much discussion from a variety of aspects about how the retail industry should respond to the super-aged society. Until now, however, neither the industry as a whole nor individual companies have come up with a clear answer. While the American market provides us with many examples of progress in retail business, it has not yet been faced with the problem of a super-aged society. Accordingly, Japan must face this issue before other world markets.

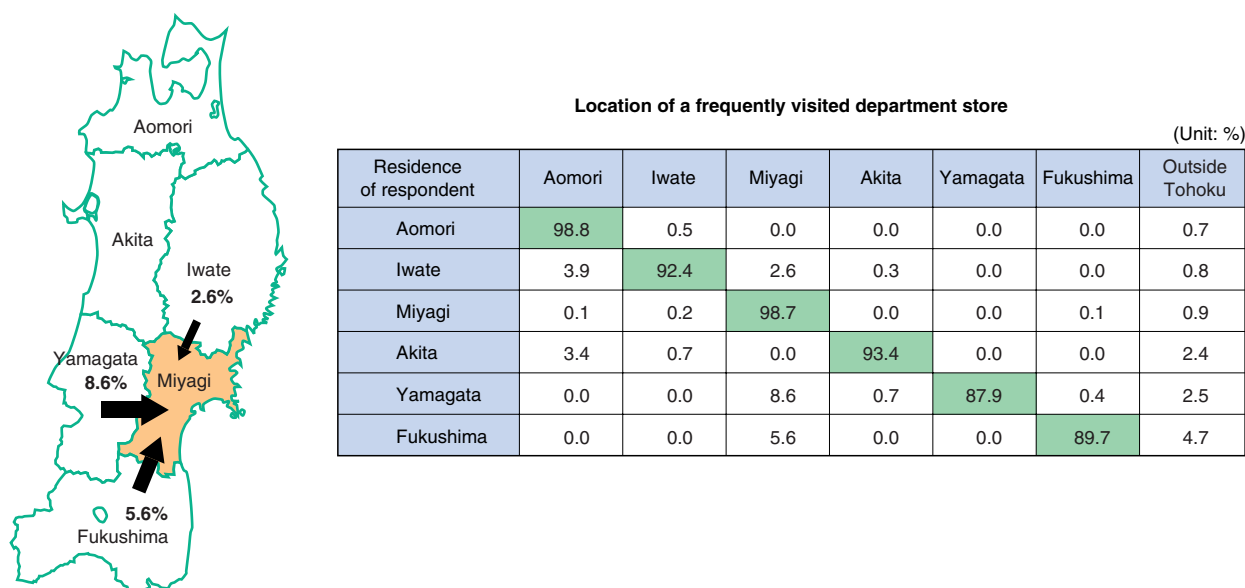
One particular characteristic of consumption behavior in the senior market can be seen in the usage frequency of retail stores by format. Compared to younger markets, the senior market shows a relatively low usage frequency in the following four formats: drugstores, GMSs, 100-yen stores and convenience stores. If we say that the average usage frequency of these formats by all age groups can be expressed as 100, the usage frequency of these four formats by the senior market is 68, 76, 79 and 80, respectively. From the perspectives of these formats, such findings indicate that these retail formats do not actually regard the senior market as an important customer group.

In contrast, we can find retail formats for which the usage frequency by the senior market is relatively high. These are cooperatives (group purchasing), home centers and volume home electronics retailers. As above, if we set the average usage frequency of these retail formats by all age groups at 100, the usage frequency by the senior market is high at 129, 111 and 109, respectively.

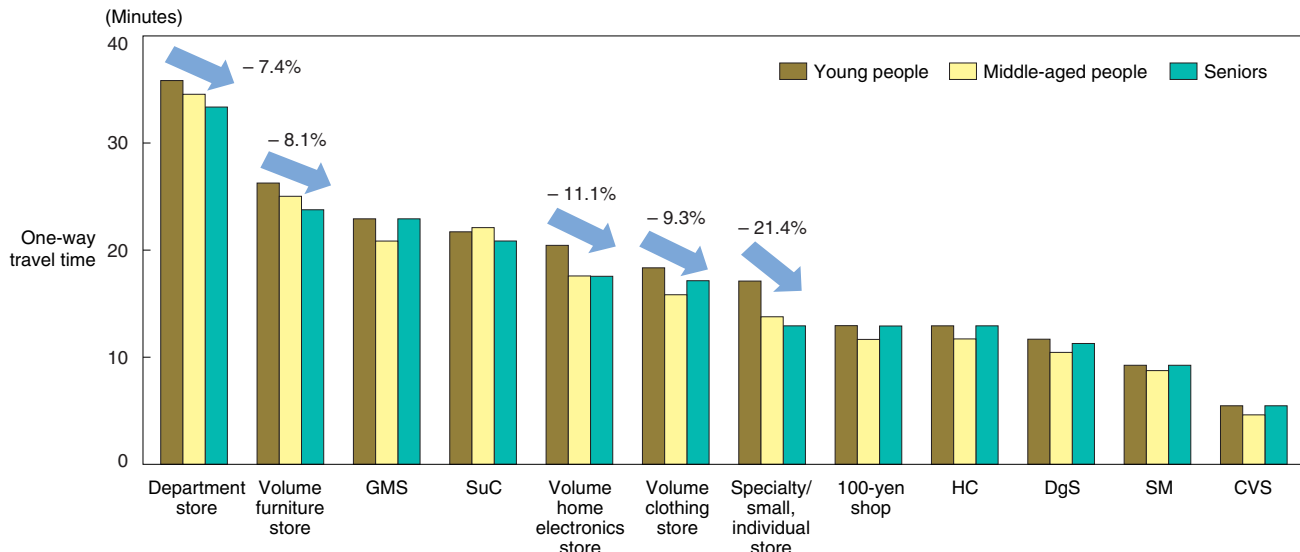
The high popularity of cooperatives among the senior market can be interpreted as that seniors opt for the image of security and safety that their brands offer. One of the reasons for the high usage frequency of home centers and volume home electronics retailers can be attributed to the fact that seniors began to spend their time and money on “leisure pursuits” because they have already passed the most difficult times of their lives of raising children and have now reached the stage where they can use their time and money for themselves.

While the usage frequency of retail stores by format by seniors provides one kind of data about the senior market, these data nevertheless seem to suggest the keywords that the retail industry should take into account in responding to the super-aged society, namely, “safety” and “leisure pursuits.”

Figure 4. Shifting Demand for Department Stores by Prefecture/Region (As Represented by the Tohoku Region)



Source: Compiled based on “Questionnaire Survey on Shopping” by NRI, October 2005.

Figure 5. Average Time Spent for Traveling to Stores by Retail Format and by Age Bracket of Consumer

Notes: (1) Travel time was totaled by limiting the target to users of each retail format. Percentages indicate the ratios of travel time of seniors to that of young people. (2) CVS = convenience store, DgS = drugstore, GMS = general merchandise store, HC = home center, SM = supermarket, SuC = super center.
Source: Compiled based on "Questionnaire Survey on Shopping" by NRI, October 2005.

3 Senior Market with a Strong Inclination towards One-Stop Shopping and a Limited Area of Consumption Activity

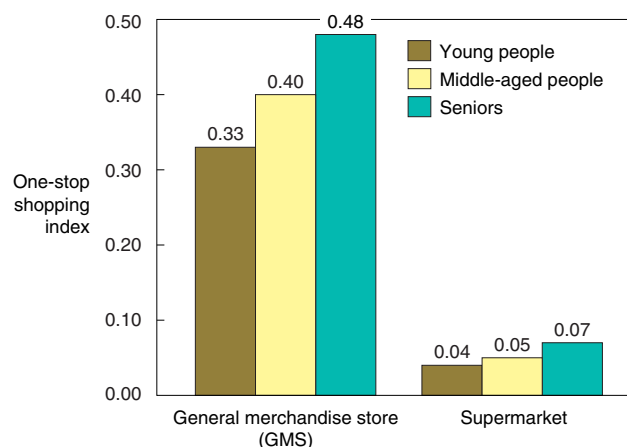
Another aspect of the impact that an aging society will have on retail business is a limitation of the area of a commercial zone.

A comparison of the time to travel from home to a store between seniors and young people indicated that seniors use less time than young people to travel to purchase relatively high-priced goods (generally, people visit several stores to compare prices and quality before they finally decide on the one to buy). For example, seniors use less time to go to a department store than young people do by about an average of 7 percent. Similarly, travel time is less by 8 percent for a volume furniture retailer, 11 percent for a volume home electronics retailer, 9 percent for a volume clothing retailer and 21 percent for a specialty/small, individual store.

In contrast, there was no major difference between seniors and other consumers for travel time to convenience stores and supermarkets that handle everyday goods (Figure 5).

These findings suggest that seniors do not make efforts to visit stores located far from their homes to purchase high-priced goods, while middle-aged and young people do. This means that retailers that handle high-priced goods for which consumers generally visit multiple stores to compare goods are destined to face two adverse winds of declining population and a limited area of a commercial zone because of aging.

In recent years, an increased tendency has been seen among consumers to select stores where they purchase goods according to their individual situations. Under such a tendency, seniors are more inclined to go the way

Figure 6. One-Stop Shopping Index by Age Bracket (Concentration on GMSs and Supermarkets)

Note: One-stop shopping index monitors whether consumers buy three product groups of "foodstuffs," "daily necessities" and "clothing" at a single store or at multiple stores. The larger the index, the higher the degree of one-stop shopping. If the index is "1," consumers buy all these three product groups at a single store.

Source: Compiled based on "Questionnaire Survey on Shopping" by NRI, October 2005.

of one-stop shopping (purchasing as many goods as possible at one store) than other generations are (Figure 6). However, on the other hand, seniors tend to avoid shopping at huge shopping centers because of the level of their physical strength.

These changes in consumption behavior caused by aging as well as the restricted construction of large-scale retailing facilities through amendments to the three town-planning laws may likely lead to the emergence of small-scale neighborhood shopping centers (NSCs) in the future. NSCs will target seniors as the principal customer group and will have a selection of products focused on everyday goods. A scenario that

also merits consideration is the reconstruction of existing GMS facilities to create NSC-like stores.

4 Expanded Shopping Time because of an Enhanced Selection of Products

When we plot travel time to a store and time spent for shopping by retail format on a graph, we find a clear proportional relationship between these two factors (Figure 7). In other words, consumers spend almost the same amount of time at the destination store as that spent for traveling there and back. In addition, as is clear from the fact that a department store is positioned at the upper right, the depth of an assortment of goods affects the time spent for shopping.

We went one step further from these findings and tried to establish a model using shopping time as an explained variable. The result is the following model formula.

$$\begin{aligned} \text{Shopping time (minutes)} &= 0.8 \times \text{time to travel} \\ &+ 14 \times \text{evaluation of product selection} \\ &(1 \sim 5 \text{ points}) - 28 \end{aligned}$$

The model formula indicates that “time to travel to a store” and the results of the “rating by a consumer on a selection of goods” are major factors in determining the time spent for shopping at a store. With respect to the selection of goods, this formula indicates that the time spent for shopping will be increased by about 14 minutes if, for example, a store that consumers evaluated as “ordinary (3 points)” is raised one step to “somewhat good (4 points).”

These findings suggest that if consumers evaluate a store as having a “good selection of products,” they will

spend more time at such a store, contributing to an increase in sales per customer. An effective measure for enhancing the selection of goods within a limited floor space is to explicitly identify the target customer segment. However, such a strategy can only be effective if the consumption potential of the target customer segment in the relevant area is adequately large.

IV Consumer Evaluation of Each Retail Format

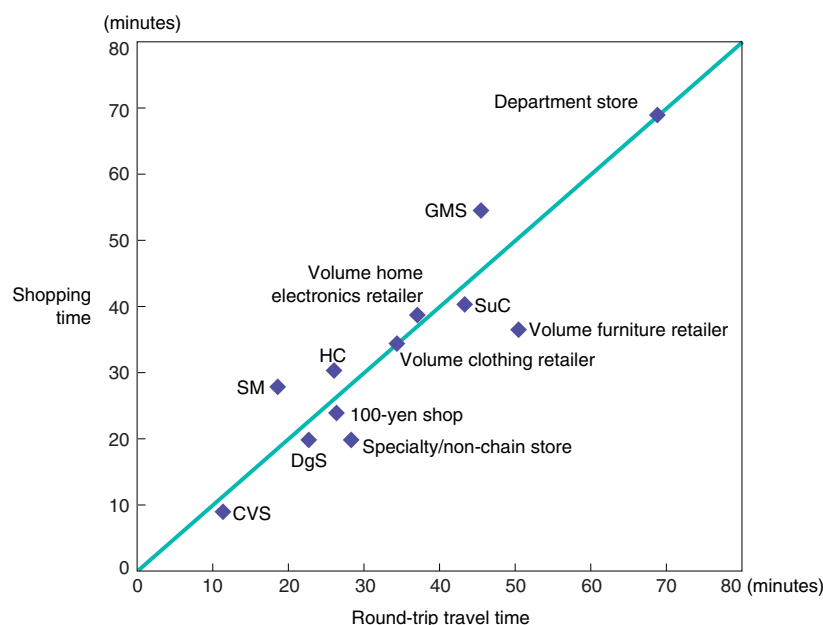
1 Strengths and Weaknesses of Each Retail Format from the Consumer Perspective—Format Radar Charts

In the retail industry, attempts are being made for differentiation in every aspect including quality, selection of goods, prices, etc. How these efforts are recognized and evaluated by consumers and the resulting brand image formed will become increasingly more important in the future.

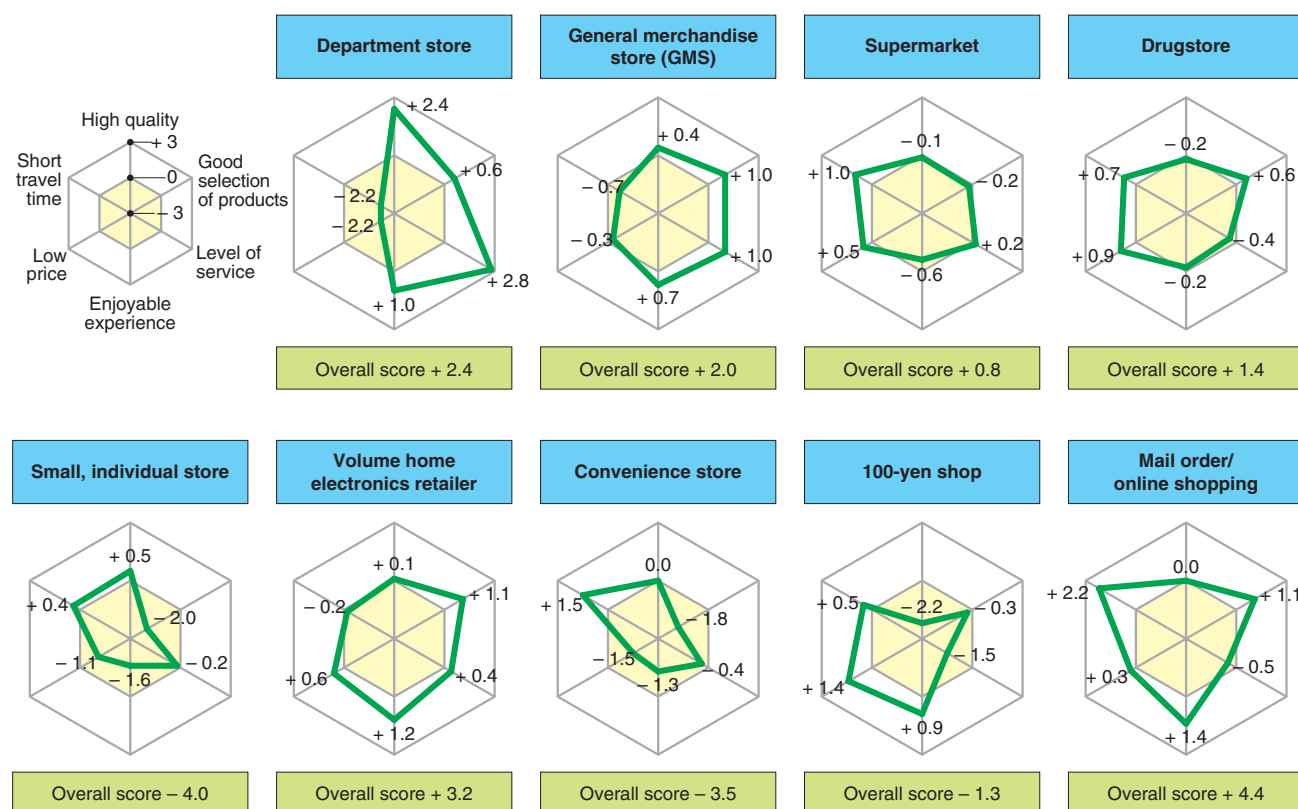
In this section, consumer evaluations of each retail format are analyzed based on six indexes, namely, (1) quality, (2) selection of goods, (3) level of service, (4) enjoyable experience, (5) prices and (6) travel time. The results of this analysis are indicated in radar charts (Figure 8).

A full hexagon created inside each radar chart indicates the average values of all retail formats. The farther the value is plotted from the center, the higher the consumer evaluation. These charts are based on the results of 3,500 samples in six prefectures in the Tohoku region.

Figure 7. Relationship between Travel Time to a Store and Shopping Time at a Store



Notes: CVS = convenience store, DgS = drugstore, GMS = general merchandise store, HC = home center, SM = supermarket, SuC = super center.
Source: Compiled based on “Questionnaire Survey on Shopping” by NRI, October 2005.

Figure 8. Format Radar Charts (Consumer Evaluation of Each Retail Format in Tohoku)

Source: Compiled based on "Questionnaire Survey on Shopping" by NRI, October 2005.

(1) Supermarkets and drugstores with balanced indexes

Compared to other retail formats, supermarkets and drugstores are well balanced in terms of all six indexes and can be regarded as receiving average evaluations from consumers. However, if we look at each item, supermarkets received a relatively low appraisal (-0.6) for "enjoyable experience" and drugstores similarly received a low rating (-0.4) for "level of service." Accordingly, these items represent issues requiring improvements in the future for these respective retail formats.

In recent years, drugstores have been offering food-stuffs and daily necessities, encroaching on the offerings of supermarkets. Under such a situation, consumers have rated drugstores higher than supermarkets in terms of enjoyable experience and prices. The supermarket industry should pay attention to such a relatively low rating.

Unlike supermarkets and drugstores, the consumer rating of 100-yen shops and convenience stores mostly differs by index item. While 100-yen shops are rated high for low prices (+1.4) and enjoyable experience (+0.9), they are rated low for quality (-2.2) and level of service (-1.5). Similarly, while convenience stores received a high rating for travel time (+1.5), they received a low rating for selection of goods (-1.8) and prices (-1.5).

In view of the fact that these retailers have been performing relatively well, it is assumed that consumers

support these retail formats but use them for different purposes.

The rating of GMS is well balanced from an overall perspective. In particular, GMS is rated relatively high for selection of goods (+1.0), level of service (+1.0) and enjoyable experience (+0.7). Since that is the case, why have GMSs been having a tough time recently?

One way of looking at this situation is that while GMSs overall still garner consumer support, the GMS industry in general does not have a robust revenue structure. Under such a fragile revenue structure, sales have been encroached upon by other retail formats in all product categories, probably causing a problem. The fact that GMSs overall still appeal to consumers also suggests that there is an adequate chance for the GMS industry to become revitalized through industrial restructuring such as the creation of NSCs.

(2) Volume home electronics retailers and mail order/online shopping are highly rated

As is clear by seeing the overall score, volume home electronics retailers and mail order/online shopping garnered relatively high consumer support. While volume home electronics retailers do not have any particular weaknesses, they are rated high for selection of goods (+1.1) and enjoyable experience (+1.2). Mail order/online shopping is highlighted by high ratings in terms of supreme convenience (+2.2) enabling shopping at home, selection of goods (+1.1) and enjoyable

experience (+ 1.4). While these retail formats have been achieving good performance in recent years, the high ratings given to these formats by consumers endorses such good performance.

The rating of small, individual stores by consumers is poor. These retailers were rated lowest among all retail formats in terms of overall score (− 4.0), which takes into account all scores for the six indexes. The government is planning to support the revitalization of central shopping areas through the passing of amendments to three town-planning laws. However, under the current circumstances where there are an excessive number of stores and each retail format is fiercely fighting for sales, specialty (small, individual) stores will be required to make greater efforts to survive than will retailers in other formats.

(3) Department stores are rated higher in large cities

This section compares the consumer evaluation of department stores in Tokyo's 23 wards and six prefectures in Tohoku.

Department stores acquired a higher rating than other formats in terms of quality and level of service. This means that their brand image is still effective. However, what is notable is that there is a large difference in their status between rural and large cities.

When evaluations of department stores in Tokyo's 23 wards and the Tohoku region are compared, Tokyo's 23 wards acquired higher ratings in all indexes. In particular, large differences were seen in selection of goods (+ 1.8 for Tokyo's 23 wards vs. + 0.6 for Tohoku), level of service (+ 3.9 for Tokyo's 23 wards vs. + 2.8 for Tohoku) and enjoyable experience (+ 2.2 for Tokyo's 23 wards vs. + 1.0 for Tohoku) (Figure 9).

As explained in Chapter III, consumers' purchasing behavior relative to high-priced products has been expanding from the range of prefectures to that of

regions. In light of this situation, it is vital for department stores in rural cities to establish a new position in their rivalry with stores in large cities.

2 Positioning of Each Retail Format from the Consumer Perspective

We created a "Map of Retail Formats" based on the survey results as one that indicates the positioning of each retail format from the consumer perspective (Figures 10 and 11).

The map of retail formats uses product groups for the horizontal axis and relative price rating by consumers for the vertical axis. In addition, usage frequency by "format × product group" is expressed by the shading (dark or light) of the blocks. Simply glancing at this map enables us to understand what consumers think about and how they use each retail format.

This map does not plot the retail formats for which respondents replied with a lower usage frequency than the prescribed value (i.e., usage frequency between "do not use at all" and "occasionally use"). The center of each block expresses the average of a relative pricing image concerning the relevant "format × product group" block. The height of each block expresses the standard deviation of the price rating of the respondents.

(1) Large cities have many options

Looking at the map of retail formats for Tokyo's 23 wards and 6 prefectures in Tohoku, we find a greater diversity in Tokyo than in Tohoku, providing consumers with more options. For example, in Tokyo, while small, individual (specialty) stores are performing well, low-price businesses such as 100-yen shops are also showing their presence. Consumers are divided into many segments, making it difficult to develop marketing strategies that target the mass market. Under such an environment, in large consumer markets such as Tokyo and Osaka, retail formats with a small commercial zone that targets subdivided consumers might show potential for growth.

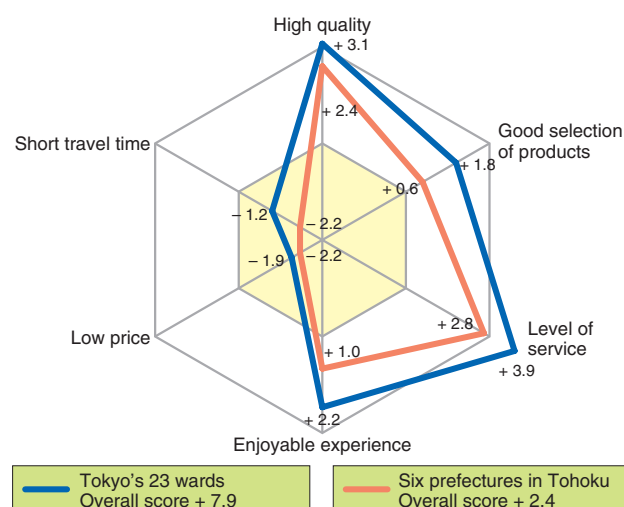
However, in rural areas such as Tohoku, because there is no such subdivided consumption potential as in Tokyo, the deployment of a retail format with a small commercial zone that targets specific consumers will face limitation. Companies in Tohoku should deploy strategies that are different from those for large consumer cities such as Tokyo.

(2) Regional differences also seen in the price-based positioning of department stores and convenience stores

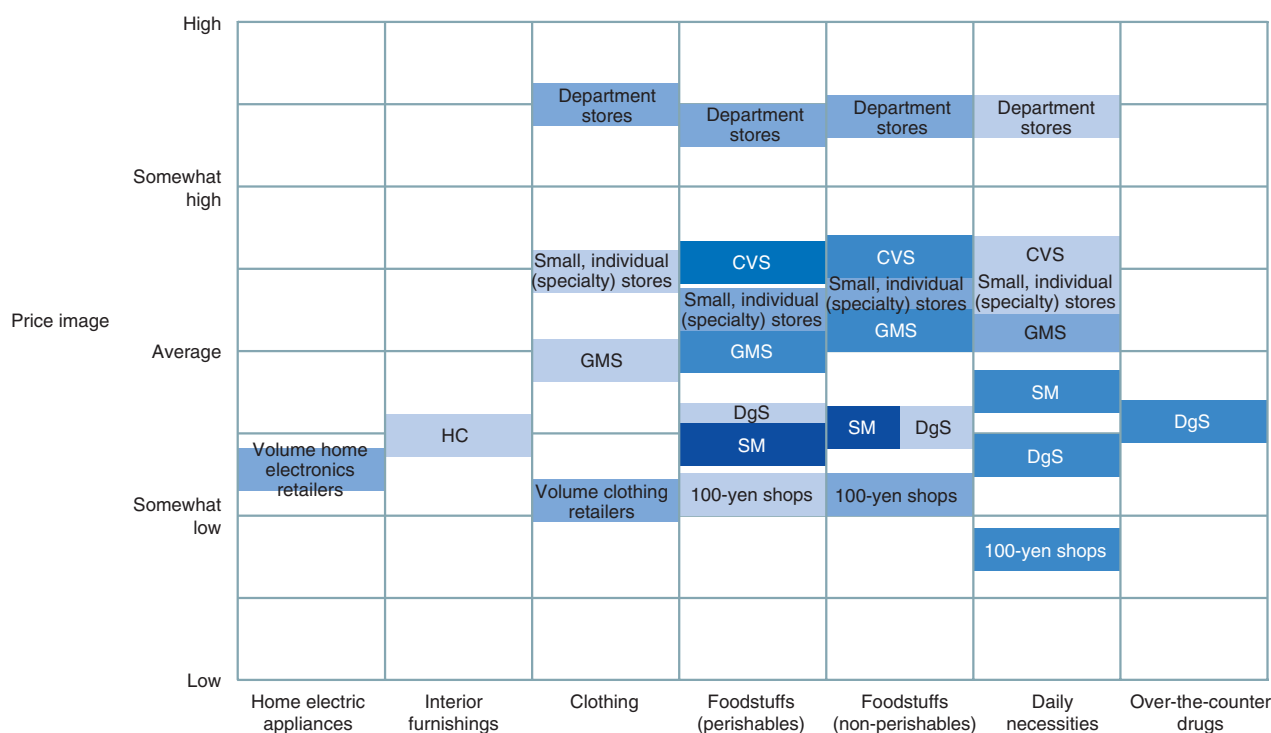
In Tokyo, department stores are positioned higher in terms of prices than are other retail formats. In contrast, the positioning of department stores in Tohoku has been shifting towards the low price range.

The survey also shows interesting findings for convenience stores. Basically, convenience stores sell goods at

Figure 9. Consumer Rating of Department Stores (Comparison between Tokyo's 23 Wards and 6 Prefectures in Tohoku)

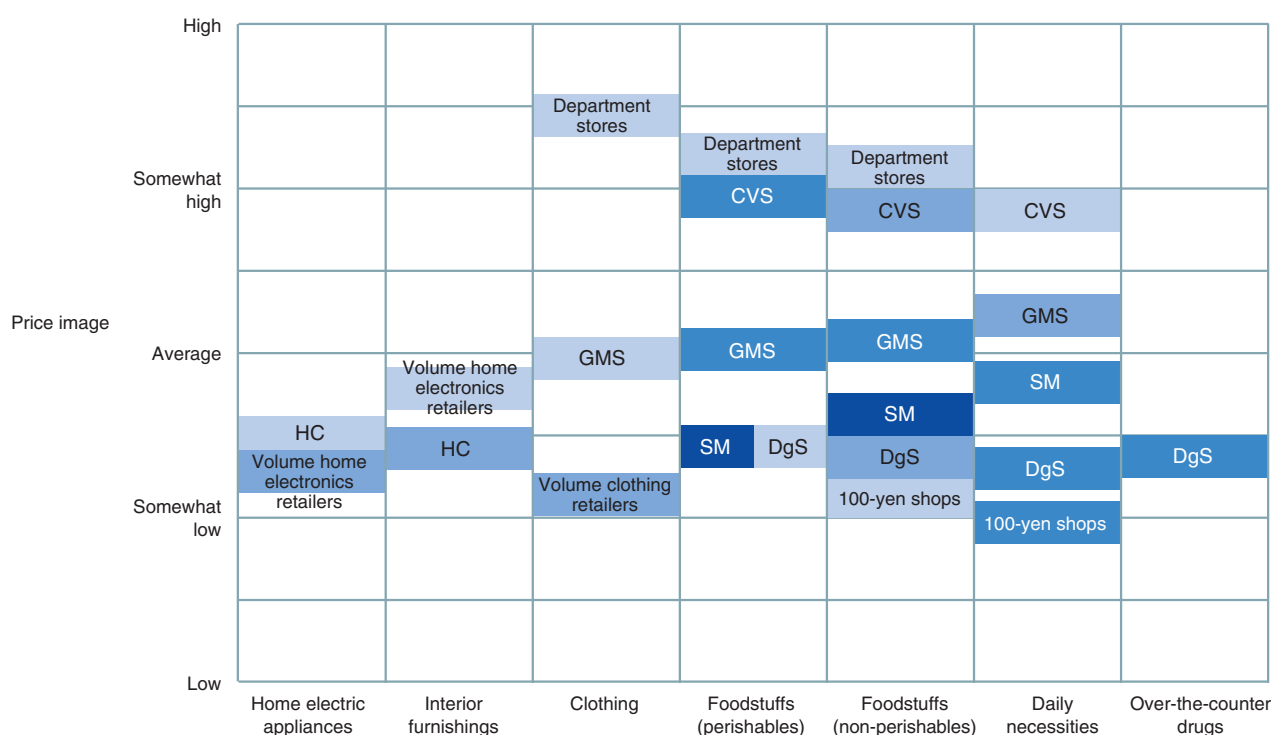


Source: Compiled based on "Questionnaire Survey on Shopping" by NRI, October 2005

Figure 10. Map of Retail Formats (Tokyo's 23 Wards)

Notes: (1) The shading of the blocks indicates usage frequency: the darker the block, the higher the usage frequency. In order to avoid complexity in the diagram, the retail formats for which respondents answered with a lower usage frequency than the prescribed value (i.e., usage frequency between "do not use at all" and "occasionally use") are not shown. (2) Foodstuffs (perishables) refer to items that must be consumed within a few days such as perishable foods; foodstuffs (non-perishables) refer to items that need not be consumed within a few days such as frozen foods. (3) CVS = convenience store, DgS = drugstore, GMS = general merchandise store, HC = home center, SM = supermarket.

Source: Compiled based on "Questionnaire Survey on Shopping" by NRI, October 2005.

Figure 11. Map of Retail Formats (Six Prefectures in Tohoku)

Notes: (1) The shading of the blocks indicates usage frequency: the darker the block, the higher the usage frequency. In order to avoid complexity in the diagram, the retail formats for which respondents answered with a lower usage frequency than the prescribed value (i.e., usage frequency between "do not use at all" and "occasionally use") are not shown. (2) Foodstuffs (perishables) refer to items that must be consumed within a few days such as perishable foods; foodstuffs (non-perishables) refer to items that need not be consumed within a few days such as frozen foods. (3) CVS = convenience store, DgS = drugstore, GMS = general merchandise store, HC = home center, SM = supermarket.

Source: Compiled based on "Questionnaire Survey on Shopping" by NRI, October 2005.

regular prices and, therefore, there should be no price difference between areas. However, from the consumer perspective in Tokyo's 23 wards, the pricing image of convenience stores is positioned between "somewhat high" and "ordinary." From the consumer perspective in Tohoku, the image is positioned in the vicinity of "somewhat high," indicating a clear difference by area. If we examine this difference in terms of per-capita income (fiscal 2003), such income (4.27 million yen) in Tokyo is about 1.8 times greater than that (about 2.40 million yen) in Tohoku. Such a large gap is attributed to regional differences.

If we take into account such a difference in consumer ratings, we think that it may even be necessary for convenience stores to flexibly set their retail prices if they are in an area where fierce competition with other retail formats is happening.

(3) Possibility of new formats for the areas represented by the blank blocks

With reference to the low-price blocks, these fields were blank fields that were considered not accepted by consumers in Japan in the past, unlike in the United States. However, in recent years, new retail formats such as drugstores, 100-yen shops and volume clothing retailers have grown rapidly and developed these blank fields. Such a situation can be seen in both Tokyo and Tohoku.

Moreover, with respect to the product groups of home electric appliances, interior furnishings and over-the-counter drugs, an oligopolistic status has essentially been formed by volume home electronics retailers, home centers, volume furniture retailers and drugstores, respectively. In the past, department stores, GMSs and small, individual stores showed their presence even for these product groups. However, they lost their presence due to the emergence of category killers equipped with a wide selection of goods and price competitiveness. However, such oligopolies will not remain perpetually. In the blank fields created by such an oligopoly, new formats may emerge.

In terms of price rating, these blank fields are positioned between department stores and GMSs in the case of the clothing product group. While these fields are regarded as attractive, there have only been a limited number of companies that have achieved success in these fields. ZARA, which is operating on a worldwide basis, is considered to be a company that has been growing by developing these fields.

V New Retail Formats at a Turning Point and Adaptive Strategies

We have so far explained that the current retail industry of Japan has been facing a turning point from a historical

perspective in Chapter I. In Chapters II – IV, the following ten conclusions were drawn through macroscopic and consumer analyses.

- (1) In the future, Japan's total real consumption expenditure will not grow.
- (2) The contrast in the increase/decrease (mosaic patterns) of real consumption expenditure by area will expand.
- (3) The contrast in the increase/decrease of real consumption expenditure by age bracket will expand.
- (4) The range of consumer purchasing behavior will expand from the prefectural to the regional level.
- (5) The keywords that will tap the growing senior market are "leisure pursuits" and "safety."
- (6) The senior market shows a relatively strong inclination towards one-stop shopping, and the radius of consumption behavior of seniors is small.
- (7) Each retail format must respond to "strengths and weaknesses from the consumer perspective" (format radar charts).
- (8) The mail order/online shopping format is highly rated by consumers.
- (9) The competitive environment of each retail format differs between urban and rural areas (map of retail formats).
- (10) New retail formats may emerge in the blank fields that are on the map of retail formats.

1 New Retail Formats in Rural and Senior Markets

The conclusions listed above in (1) through (4) suggest that the basis for business on which existing retail formats depend has been largely undermined, and shakeups might occur in the overall retail industry.

For example, one assumed phenomenon is that the GMS sector that ceased to grow and is striving to find new opportunities for growth may participate in the market of shopping centers in rural areas by adopting a new retail format. Such moves may revitalize shopping centers in rural areas through the introduction of new capital. Another possibility is that the potential value of some GMS stores that lost their vitality may be recovered by the three town-planning laws. For example, GMSs may be developed into NSCs that chiefly target seniors. Furthermore, the widening of the range of shopping areas of consumers will promote a shift of the department stores in rural areas towards a new retail format.

The conclusions listed above in (5) through (10) simply reveal some current aspects of consumers and have not yet reached the stage of identifying the overall picture of consumer trends. Nevertheless, the senior market has apparently been expanding, and it is only natural that new formats that adapt to the characteristics of the senior market will emerge.

The blank fields on the map of retail formats are created because withdrawals took place as a result of competition among different formats in recent years. As an inevitable consequence, new retail formats may emerge in such blank fields. We expect such an emergence of new retail formats in these blank fields in the future. In view of consumer ratings of the existing retail formats, there are plenty of possibilities that non-store retail channels such as online and mail order shopping will grow to form a major power.

2 Building Corporate Strength Capable of Meeting Environmental Changes

In the face of shakeups of the market environment and/or market structure, it is important to thoroughly analyze the market environment and the trends in suppliers and consumers to identify possible new formats that are suitable for the relevant changes.

However, in order to increase the probability of growth under a situation where such a change is substantial but uncertain, it is similarly important that a company promote structural reforms and rebuild its corporate strength so that it can quickly cope with these changes through innovation.

To increase corporate strength, “information analysis capabilities” to analyze and correctly understand market trends and “merchandising capabilities” to deploy prod-

ucts and/or services suitable for the market identified according to such analyses are required. In addition to a company’s own efforts, “collaboration strength” is also essential to implement product development, supply chain management (SCM) and category management in cooperation with partner companies such as wholesalers and manufacturers.

In addition, what is most important to fully demonstrate these functions is to restructure the corporate organization. The most evident and important measures that are required to survive a turning point are to promote these corporate reforms.

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