

E-commerce Trends in Japan

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Voting with Their Feet

The ministers may be sitting in for a long haul at the TPP talks but consumers in Japan are not waiting. They have voted, are voting, and will vote with their computers, credit cards and *keitais* (cell phones). And that vote is the harbinger of an entire sea change in many facets of the Japanese economy.

Much of that vote is being dismissed as an aftereffect of 3.11 (buying staple food from overseas, buying radiation monitoring equipment from overseas) or as a simple reaction to the high yen exchange rate, but these are both blips in what is a major long-term shift that will radically alter buying patterns, in almost every industry, in some cases necessitating simple revisions in domestic retail strategy, in others in trade relations with other countries, and in still others, changes in existing law.

Many Japanese companies have long relied on the “captive home market” strategy, even when dealing with foreign luxury goods. In this respect it is worth noting that at the height of the bubble economy it was not at all unusual for savvy Japanese shoppers to fly to New York, where the same Louis Vuitton bag could be had for a fraction of the price, and they could enjoy a Broadway show and a few good meals before flying home.

That pattern changed, of course, with the end of the bubble economy.

However, even as that pattern changed, the building of a very

robust fiber-optic backbone network in Japan along with a very advanced mobile system continued apace. The generation that grew up with i-mode as their first internet connection when dial-up was still expensive, now has high-speed internet at home as well as 4G on mobile.

Technology is an enabler and, in and of itself, does not change consumer patterns. However, those who think that the 3.11 event or even the high yen exchange rate are prime causes are not paying attention to long-term trends. In September 2010, the Japan Direct Marketing Association together with Nomura Research Institute showed a 22% rise in online purchasing of \$67.2 billion, a figure that rises further if catalog spending is also included. (*Chart*; the data are in yen base.) *The Economist* in a June 2010 article placed growth at 1% but noted that was year-on-year since 2005 and predicted 10% growth for the five years beginning with 2010.

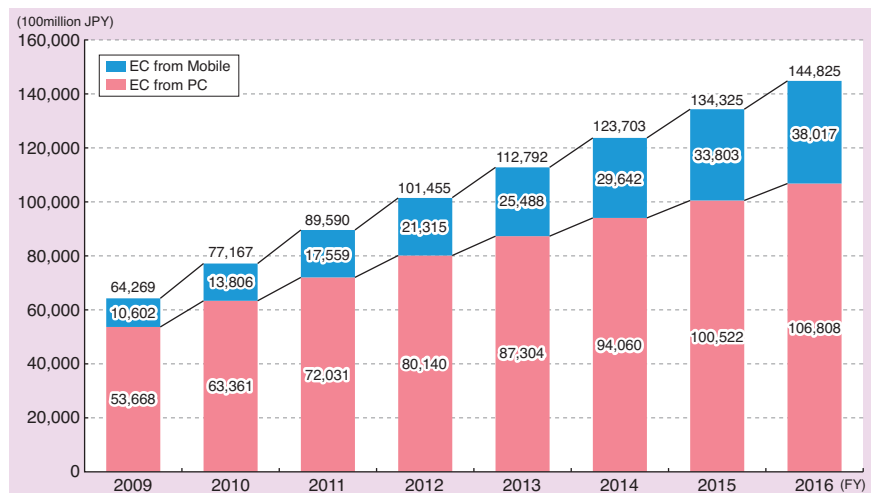
Of course, e-commerce is a very large category, and to illustrate the point it is necessary to separate such things as purchasing a railroad or plane ticket, or even a concert ticket. Those are all purchases, but they are not purchases of durable goods.

Durable goods and even groceries and certain gray-market purchases are where the changes are most profound and have the ability to completely reshape the landscape of “bricks and mortar commerce.”

Groceries are a good example because it is almost counterintuitive that anyone would want to go online to shop for

food - until price and convenience are taken into account. A look at Rakuten alone will show literally dozens of online shops selling everything from cheese from France and Switzerland to sausages from Germany. When there was a run after 3.11 on staple foods, there were many outlets in the US and EU that were able to pick up the slack, particularly for longer-lasting items such as canned soup and vegetables, dried fruit, oatmeal and other foods. They were not only available, they were *cheaper*. Add into this equation the aging population in Japan, and in groceries alone, all of the elements for large growth in sales are already present. And if they were present before 3.11, the aftermath, the various fears of food contamination, will certainly be a factor in pushing the numbers higher.

CHART
BtoC EC Market Forecast in Japan



Note: Up to FY2010 - Estimated by NRI based on statistics from METI, etc.
Source: FY2011 - NRI forecast

In durable goods (here anything from a book to a DVD to a pair of shoes) the trend is even more startling. The revolutionary concept of Amazon.com at first was simply selling books, saving a trip to the bookstore. If a consumer knows they want a certain book then, unless they enjoy being in a bookstore, the convenience of ordering that book and having it delivered to the door cannot be overestimated. At the time Amazon started, no one, especially not the company's founder, would have envisioned the company becoming a publisher in its own right (as it has now done in the US). But books, DVDs, etc. are easy, and have motivated consumers, a very dedicated fan base.

That kind of base is a solid foundation, but it does not account for the phenomenal rise of e-commerce in Japan.

Rise & Fall of Department Stores

For that, in one way, we must look to the demise or at least diminishment of the importance of the traditional Japanese department stores that, from food halls in the basement to antiques at the top level, offered a one-stop shop for generations of shoppers. That is no longer true and most Japanese department stores now have "shops within shops" featuring particular brand names.

In fact, that idea, lately touted by retail consultants as the way to "save" department stores, is not at all new. It is the essence of the Grand Bazaar in Istanbul, which contains over 4,000 stores on 58 covered streets that sell carpets, clothing, food, jewelry and on one adjacent street, weapons. But the Grand Bazaar has been in continuous use since 1461 and the area it covers is larger than every department store in Tokyo and Osaka combined, with quite a bit of room left for entire shopping districts. In this way it is almost the real world opposite of the classic Japanese department store.

Tyler Brule, whose company Monocle has a boutique and a café in Tokyo, noted in a recent essay, "The simple explanation is that the Japanese post-luxury consumer wised up to the absurd margins charged by high-end European brands for a logo and a pattern applied to a bit of canvas..." Brule goes on to note, "These consumers grew weary of seeing the same products show up in department store windows across the country." He might well have added "Sic transit LVHM."

While Brule points to a number of Japanese companies that make products as good as, if not better than, any of the well-known luxury goods companies (and at a lower price point) he sees this as "turning in" or "return to authenticity." That may be true for a

Photo: UNIPHOTO PRESS



Turkey, Istanbul. Interior of Grand Bazaar (Kapali Carsi)

segment of the Japanese consumer market but as a trend marker, it ignores the numbers.

Every Number Tells a Story

The numbers here mean prices. Prices, quality and availability are the three key factors in e-commerce or regular commerce. Using two personal examples, last winter, I needed scarves. I found in Britain two scarves made of completely natural wool, untreated with lanolin still in them; the total for both, with shipping, was about \$40 (at that time, under 4,000 yen). And, recently, looking for a rugby shirt, locally some of the best brands are available at 8,800 yen. Again in Britain I found a comparable one, with shipping a bit over 6,000 Yen.

It is not a coincidence that many well-known sites for clothing or other durables will instantly price in yen, and a number have Japanese language capability. Although there are sometimes issues about selling directly to Japan because the Japanese distribution rights for some items may be held by companies in Japan, in the US there is a thriving side industry of "remailers." These allow a consumer to take a "virtual US address" that is the remailer's own address. The item is shipped there, and then, for a fee, shipped to Japan from the remailer, and thus is clear of any violation of distribution agreements here.

Contender

Rakuten is not the only company to have set its sights abroad.

Photos: Vvego International®



There are smaller virtual bazaars of small workshops and craftsmen that have also set up shop online. There are also companies that have, even from very small beginnings, set up on their own. These are companies that may never set up an actual shop in Ginza or Ometasando or anywhere else, because there is no need to. They are already as close as the computer screen.

Robert Porter is a former airline pilot who had been thinking of setting up a company to make fine accessories (*photos*) for some years. His company, Vvego International, has only had its own freestanding website since the second half of 2011. Yet already he has taken orders from as far away as Australia.

His company is preparing to enter the Japanese online market this year. In a point that echoes Brule, Porter commented, "I believe the Japanese consumer appreciates fine, unique items." And he adds, "The other Asian countries that now have their own populations that have more disposable income, and more exposure to world trends, still look to and at Japan, and what is popular there." (For purposes of comparison it is useful to point out that, while not cheap, most of the products offered at Vvego International cost a fraction of what their prices would be in a terrestrial department store or boutique in Tokyo.)

Dark Side of Gray Market

It is no accident that one of the most contentious issues in the TPP talks is pharmaceuticals. There is no question that Japan has lagged behind both the US and the EU in the approval of new medications and licensing of existing ones. The average time for approval of a new medicine in the US is approximately two years; in Japan, at present, approximately seven years.

There are medicines in the US and EU that will shortly revert to generic status that have never even been approved for primary prescription in Japan. With a rapidly aging population, by itself, that is a recipe for a huge amount of unnecessary expenditure of both public and private monies.

In the interim, pharmaceutical companies in countries like India and Brazil have moved aggressively into the current gap (in Japan,

among other places) by making products cheaper and widely available online.

Editorials in regular newspapers consistently warn of the perils of buying medicinal products online, warning of the dangers of counterfeits, product substitutions and credit card fraud. These are all valid concerns. But if the product is not available in Japan, *at any price*, or if the buyer is an adult taking care of an older parent with a painful condition who seeks only the kind of

pain relief that would be available if more products were approved here (and more doctors trained in their use), then such warnings are unlikely to dissuade very many.

Japanese law itself has an almost built-in loophole in that a product that is not approved here, but not forbidden here, is almost always allowed in (at least 30 days' worth for personal use).

Quo Vadis?

Ten years ago a government-sponsored IT Council called for, among other things, increasing the amount of online purchasing (then estimated by Andersen Consulting and the Electronic Commerce Promotion Council of Japan (Ecom) to be \$3 billion, all purchases included) by 50 times. While that goal has not yet been reached, it is in sight.

What could not have been envisioned then is the coming together of the technical means to create the convenience of the grocery store and the world market at a scale that dwarfs even the Grand Bazaar, on any laptop, desktop, or even mobile phone.

It was inconceivable then, but it has already happened, and what the Japanese government, and other players can do is recognize what has happened, standardize (in terms of measurements, quality, etc), establish an effective inter-country enforcement agency for matters when that is called for and, to the extent possible, offer aid and assistance to companies that want to transition to more effective virtual forms of business, as well as encourage start ups.

At the same time, companies that insist on pursuing "captive market" strategies should be dissuaded publicly and, if necessary, by legal means.

Finally, foreign companies must be allowed to sell to Japanese consumers as easily as Japanese companies can. The playing field has to be as even as possible for the great World Bazaar to even begin to emulate the real Grand Bazaar and to last as long as that complex of streets and warrens and shops has. **JS**

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