

# Recent Trends in Personal Consumption in Japan

By Jiji Press

SIGNS are emerging that Japan is seeing a full recovery in personal consumption, which accounts for approximately 60% of the country's gross domestic product (GDP). To be sure, the current picture remains spotty, as income and employment environments vary depending on age bracket, business size and industry. While demand for high-priced items is booming, Miura Atsushi's book *Karyu Shakai* (Lower-Class Society) ranks on the list of best-sellers, and discount ¥100 convenience stores have become a major attraction for consumers. It is clear that consumption patterns are polarizing. Although it will take more time for overall consumption to bottom out, Kiuchi Takahide, Senior Economist at the Nomura Securities Financial & Economic Research Center, expects that the "broad-based effects from improved income and employment conditions will spread to the society by 2006 or 2007, and personal consumption which will reach 2% growth, despite depopulation, will drive the economy replacing capital expenditure."

## Current Outlook

Personal consumption in GDP has been growing steadily for three consecutive quarters as of September 2005. According to the Bank of Japan's quarterly Preliminary Estimate of Flow of Funds on Dec. 15, 2005, households' financial assets at the end of September reached over ¥1,453.7 trillion, which was ¥20 trillion higher than the previous record at the end of June.

The wealth effect from rising stock prices has enticed high-income consumers to spend more lavishly. Visible signs of this include rising sales of high-priced items at department stores, the growing popularity of Toyota's Lexus luxury sedan, and brisk sales of flat-panel TV sets. At the same time, the employment climate has been improved with

young part-time workers becoming full-time employees, increasing consumption among the young. Still, better wage effects have not spread to the middle and senior age brackets, and the number of young people with poor work motivation called NEETs (people Not in Education, Employment or Training) is increasing. Consumption growth varies depending on age brackets.

While recruitment demand has been increasing in such areas as the securities industry, the construction and textiles industries still hold surplus workers. Moreover, wage levels at small and medium-sized enterprises (SMEs) remain low compared with large corporations. According to the Japan Business Federation (Nippon Keidanren), winter bonuses at large corporations grew 4.35% year-on-year, while Nomura Securities estimates that the overall growth rate is only 1.4% if SMEs are included. These differences make an uneven consumption landscape.

## Splurging on O-Sechi Traditional New Year's Dishes

The demand wave for luxury items is also visible in other areas. At the Mitsukoshi department store in Nihombashi, Tokyo, ¥70,000 or higher priced *o-sechi*, traditional dishes for the New Year in Japan, have gained popularity. Compared with the previous year, sales of *o-sechi* sets under ¥30,000 declined, while those priced at ¥100,000 or more have increased. In particular, advance orders for *o-sechi* sets supplied by a first-class Japanese restaurant priced at ¥205,800 for six and ¥152,250 for five people surpassed the year-earlier sales at the end of November.

One group of luxury items selling particularly well at department stores is imported wristwatches. At the Mitsukoshi Nihombashi store, sales of wristwatches recorded double-digit growth during a one-week "World

Photo: Jiji Press



Mitsukoshi's special *o-sechi* set for three to six people is priced at ¥157,500. *O-sechi* sets priced at ¥100,000 or more are in high demand. (Mitsukoshi Nihombashi store in Tokyo)

Watch Fair" held last August, rising 15% year-on-year, with purchases averaging ¥600,000 apiece. The most popular luxury brand has a core price of band above ¥2 million. Demand for art objects priced at over ¥100 million is also strong, mainly among business owners, while an increasing number of individuals are purchasing art objects ranging from some ¥100,000 to over ¥1 million, expanding that customer base.

Not a few see this craving for luxury items as a mini-bubble riding on the back of a rising stock market, with the bubble economy of the 1980s in one's mind. However, a manager at a department store, the forefront of retailing in Japan, says, "Purchasing behavior today is different from the bubble economy days, when people went for anything that was expensive. Today people are more refined in their tastes and choose

Photos : Rakuten, Inc.



The polarization of consumption patterns has also spread to the online shopping sector. Rakuten's luxury goods market (left and center-left) and its regular market.



merchandise that suits their style.”

Upscale supermarkets are seeing a somewhat different trend. At food counters, for example, more customers plainly demand “the most expensive steak” or “*sashimi* from the best fish.” To buy luxury goods without asking the price may be reminiscent of the bubble economy, but in fact it is not the same customers who are buying expensive items every day. Queen’s Isetan, an upscale food retailer, analyzes that “People live frugally everyday, but on birthdays or other special occasions they splurge and enjoy themselves.”

### IT Corporations Also Set Sights on Expensive Items

Internet-based enterprises, too, are starting to pay closer attention to sales of expensive items. Rakuten, the largest e-

commerce company in Japan, set up a new luxury goods market site within its online shopping mall, Rakuten Ichiba, at the end of August 2005. Every two weeks a special theme is selected, and related items are sold.

Rakuten Ichiba was established in 1997. Currently it is home to around 15,000 shops that carry over 15 million items. It has developed into Japan’s largest online mall, boasting 17.29 million members as of the end of September 2005.

The luxury goods market is the first attempt to create a site with a focus on the affluent. Although the market was started with no pre-set sales target by testing the waters for users’ responses, the access count sharply exceeded forecasts.

Why did Rakuten set up the luxury goods market? According to Tsunetzawa

Kishiko of its Business Division, “It was because we found out that consumption patterns were quickly bipolarizing at Rakuten Ichiba, too.”

At Rakuten Ichiba, the percentage of discrete purchases worth ¥1 million or more has grown by 63% year-on-year. A survey among the members who expressed interest in luxury goods revealed that about 30% had a clear preference to buy such items online.

Visiting its sites opens the door to a dream-like world of luxury. Items include a teddy bear – the only one of its kind on earth – crafted by the hands of a renowned stuffed-animal doll artist (¥1,984,000), a model Ferrari sports car made partly of the exact same materials as a real one (¥750,000), or a diamond-studded fountain pen, Visconti “Alchemy” (¥5,670,000). These articles may not exactly be selling like hotcakes,

Photo : Jiji Press



Demand is increasing for high-priced premium beers and low-priced beer-like beverages

Premium beers are becoming popular as a small luxury for the weekend and for greeting gifts. Continued expansion of the market is expected. (Ito-Yokado Oimachi store in Tokyo)

but according to Tsunazawa, “We have already sold champagne for ¥20,000 to ¥30,000 a bottle as well as wristwatches exceeding ¥1.5 million apiece.”

Rakuten has also started high-end sales with its travel-booking-site. Four times so far, the luxury goods market has featured 3-day trips with accommodation for two nights at ¥1 million. The offer elicited a total of 50 applications. Encouraged by this result, starting from October 2005, Rakuten launched a ¥4-million trip. A two-night-stay-package gives guests an outright lease on a luxurious traditional Japanese-style hotel in Shimoda, Shizuoka Prefecture, renowned for its hot springs. Further included are up-market features such as airlifts by helicopter to and from guests’ homes, sightseeing yacht cruises and unlimited wine tasting.

Unlike department stores and supermarkets, where purchases are made face-to-face, buyers’ profiles are not readily visible on the Internet. Tsunazawa conjectures that many purchases come from

well-to-do male seniors. “I expect that demand for luxury goods will remain high,” she says. Rakuten plans to offer new up-market travel packages this year.

### The Polarization of Beer Market Patterns

In the beer market, as well, a gradual bifurcation of consumption patterns is under way. While high-priced premium beers with top-class ingredients and manufacturing techniques are steadily expanding their shares, low-price beer-like beverages produced without malt (third beers) look back on an explosive market expansion since their launch in 2004. Amid the gradual contraction of the overall beer market, only products with high added-value and a low-price focus are seeing demand growth.

Premium beers began proliferating in the second half of the 1990s. While this segment accounts for just around 2% of the total market for beer and beer-like beverages, premium beers gained

approximately 20% in scale over the course of five years. Although priced ¥15-¥25 above regular brews, consumers who drink non-premium beers during weekdays often buy premiums as a small luxury for the weekend. They are also popular items for greeting gifts.

Beer-like beverages closely resemble normal beer in appearance and flavor, but are subject to lower tax rates because no malt is used in their production. As a result, these products are priced ¥93-¥97 below standard beer, and have gained popularity. Sapporo Breweries was the first to develop this market with a product called “Draft One” launched in 2004. With other major breweries following suit, this beer substitute increased its share to almost 15% of the market for beer and beer-like beverages within just one year.

Hashimoto Seiichi, head of Kirin Brewery’s Laboratory for New Product Development, explains these consumption trends by saying that “the reason is that breweries have come to market with



A key concept, called 5P (PCs, pagers including cell phones, PlayStation, PET bottles and potato chips) explains the lower stratum

a plethora of different products, giving consumers a wider range of choice,” adding that, for the brewing industry with its strongly price-conscious customers, a conspicuous bipolarization of consumption patterns was not yet discernible.

He concedes, however, that the wider range of alternatives has made consumers more discriminating. The more customers learn to appreciate price and quality, instead of price alone, products whose main appeal is their low price will no longer sell. By contrast, higher price brackets will attract demand so long as the price is seen to be in line with the quality. According to Hashimoto’s analysis, future polarization in consumption patterns will grow more conspicuous as a result.

### ■ Polarization Is Taking Root

Related to the bipolarization in consumption patterns, two books that deal with a deepening social class divide

became bestsellers. Examples are Yamada Masahiro’s *Kibo Kakusa Shakai* (Society of the Hope-Divide) and Miura’s *Karyu Shakai*. Both books explain that the gap between the upper and lower classes is widening, and that people in these respective social positions are becoming fixtures within these strata. The gradual downdrift from the middle class, which used to be the driving force of consumption, to the lower class is a particularly grave development. The lower class is defined not only by a lower income level, but is also defined through a lack of motivation to climb higher on the social ladder, particularly among the young generation, associated with a weakening will to consume or to look for a job, although they could gain a decent income.

Miura’s book proposes a key concept, called 5P (PCs, pagers including cell phones, PlayStation, PET bottles and potato chips), to explain the lower stratum. It combines to give a picture of the typical youngster sitting in front of

a PC, sipping a bottled drink, web surfing or playing games and exchanging e-mails on a cell phone. Miura noted that once this generation takes center stage in society, it will accelerate the downshift toward the lower class with its penchant for the “readily available indoors,” leading to the eventual collapse of the conventional business model that has long been focused on middle-class society.

### ■ Consumers Seeking Low Prices

The arrival of the discount ¥100 shop, where every item is priced at ¥100, appeared at exactly the right time to match the changes in consumption trends. With their sights on housewives and senior citizens, who were not normally considered major drivers of consumption, ¥100 shops have gradually become a serious force.

The pioneer among small-sized ¥100 shops in the convenience store format was Shop 99 operated by Ninety-nine

Photo: Jiji Press



Fruit, vegetables and commodities are all priced at ¥100 at "LAWSON STORE 100" operated by the LAWSON convenience store chain (LAWSON STORE 100 Adachi-Takenotsuka store in Tokyo)

Plus, which inceptioned this business in 2000. Convenience store operators including LAWSON, am/pm Japan and Three F followed suit, intensifying the competition.

LAWSON initiated its ¥100 shop operations in May 2005. Selling fresh foods and household goods all priced at ¥100, the aim was to acquire new customers who are not frequent users of existing convenience stores.

At the shops, there are a full range of fresh foods, such as cabbage and tomatoes as well as other items including frozen foods, kitchen knives and water buckets. Judged by product range, the shops resemble supermarkets. The number of items sold per shop ranges between 3,000 and 3,500.

Over half of the customers at ¥100 shops are females, mostly housewives. The shops' popularity is due to the full range of merchandise combined with low prices. Customers include many elderly people, a segment distinct from that of convenience stores. One special feature is the high number of items purchased per customer. This is a natural result of the fact that they can choose without caring much about the price.

¥100 shops, whose appeal is based on low prices, have been gaining market recognition year after year. They have been successful in capturing customer

segments which they had not initially expected. As Ninety-nine Plus puts it, "Ingredients for home cooking are available at low prices, so we are seeing increasing numbers of part-time workers and students among our customers." In light of this consumption trend, Circle K Sunkus is also showing interest in entering this market.

Referring to the market growth for ¥100 shops, Watanabe Tadanao, Senior Managing Director of LAWSON, says, "Fixed-price convenience stores which offer 24/7 operations impose limits on new customer development. Identifying consumers' needs and providing services that intersect with these needs is critical for us to carry on in business."

### Food Service Industry Finally Leaving Deflation Behind

Japan's food service industry experienced an episode of "food service deflation," i.e., a period of wide price decline between 2000 and 2002. Spearheaded by McDonald's Japan's weekday half-price sales campaign for hamburgers, competitive price cuts intensified. Same-store customer transaction value, the amount spent per customer, finally swung round to year-on-year positive growth in 2003, but consumers still



Convenience store, am/pm's ¥100 shop



Shop 99 is the pioneer among small-sized ¥100 shops in the convenience store format

keep a close watch on prices. Naturally, food service companies would like to see customer transaction value go up, but higher prices without good justification could invite consumers' resistance with fatal results. The situation leaves many food service operators in a dilemma.

SKYLARK, the largest family restaurant operator running multiple brands including Gusto, Jonathan's and Bamiyan, is no exception. Its consolidated sales for the fiscal year that ended in December 2005 are estimated at ¥379.0 billion, down 1.2% from the previous year, with operating profit, a measure of core profitability, of ¥19.9 billion, on a par with a year earlier. While sales have been flat for the past five years, operating profit has been below ¥20.0 billion since 2003, down from over ¥25.0 billion in 2002.

As a countermeasure, SKYLARK is working on a model change for its Gusto outlets. The strategy is to get customers to say yes to an offer of enhanced product quality in exchange for a higher customer transaction value. If this strategy finds acceptance, the reward would be improved profitability.

In detail, key changes include a shift from a conventional Drink Bar to a Premium Café concept. This change implies better quality by selecting different coffee beans, or by serving 100% orange juice instead of products with lower fruit content, as well as new products on offer such as Calpis drinks. The mark-ups on prices are ¥40-¥320; and ¥60-¥180 when ordered together with a meal.

How have consumers reacted to this major price increase? SKYLARK has been testing its new pricing at one location in Tokyo from April 2005, and gradually introduced it at other locations. As of the end of September 2005, the number



The Gusto family restaurant

of outlets with the new pricing reached 360.

The result was no decline in the number of customers, which the company initially feared would drop, while customer transaction value increased by ¥20-¥30. Suzuki Makoto, who leads Corporate Communications, is relieved: "Consumers have accepted our new policy." The company has been introducing the Premium Café concept at 400 outlets.

To be sure, the majority of consumers still look for lower prices. In fact, in the Kyushu area, where low prices are a competitors' selling point, the company has set lower prices than Gusto in Tokyo. This is, according to Suzuki, "Because we cannot beat competitors with this new pricing."

SKYLARK once had a bitter experience in losing customers because of its pricing. During the 1990s, as the number of SKYLARK restaurants climbed steadily, the company raised prices, and its profits increased. Almost as soon as transaction value reached ¥1,000, however, visitor

numbers collapsed. Customers, sensitive over prices, left SKYLARK all at once.

The company made the biggest renovation since its founding, changed the store name from SKYLARK to Gusto, and lowered customer transaction value to ¥700. This step worked, and customers started coming back.

Yet changes are fast-paced in the food service business. "Going forward, health and safety will be the keys. If we look at each action required of us, be it an indication of the place of origin for ingredients or of potentially allergy-inducing substances contained in the food, each and every requirement incurs cost. But these are costs that we cannot work into our pricing. That is our plight," says Suzuki. The episode of food service deflation may be over, but the war of nerves between consumers and companies over pricing is set to continue. **JS**

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