

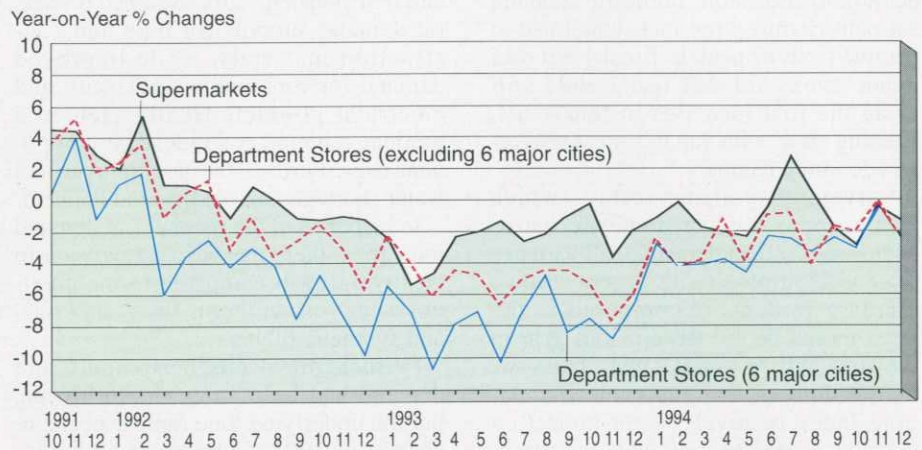
# Discounting, Upscaling, Refinement

According to the Family Income and Expenditure Survey, household expenditure has risen since the latter half of 1994 as an income tax cut and an exceptionally hot summer pushed up the demand for air conditioners and other consumer durables. Still, the effects of the tax cut, the purpose of which was to boost disposable income, have been limited and have fallen short of leading to substantial improvement in consumer sentiments.

Especially following the Great Hanshin Earthquake of January 1995, weakness in consumer sentiment has halted a recovery in consumer spending. Monthly department store sales (reported by the Japan Department Store Association) have fallen from last year's level, for nearly three years since March 1992, due to a sharp decline in non-floor sales, accounting for 20% to 30% of total sales. A combination of consumers' walking away from high-priced goods, corporate cost savings, and weakness in floor sales due to falling unit prices for clothing—a mainstay for department stores—reflecting a recent tendency of price decreases appear to be the main reasons for the drop. Despite efforts to concentrate wholesalers and increase non-returnable purchases in the midst of the current situation of severe earnings, department stores as a whole are likely to remain weaker in earnings, partly due to the severe damage relating to the earthquake in some major stores.

Supermarket sales (reported by the Japan Chain Store Association) temporarily picked up in July and August, supported by the income tax cut and severe summer weather, after falling year-on-year for 21 months in a row through June last year. Thereafter, sales have tended to recover in volume, while falling in value, due to falling prices. For the full-year fiscal 1994, supermarket sales are likely to rise only slightly from last year. Profits, however, should continue to fall, reflecting the impact of

**Sales Trends in Department Stores and Supermarkets (adjusted by store bases)**



**Source:** The Japan Department Store Association and the Japan Chain Store Association

quake-related damages and higher fixed costs, such as store and labor expenses, due to aggressive new store opening. Factors behind falling unit prices include a stronger yen, cheaper import goods due to deregulation, and more fundamentally, retailers efforts to develop private brands (PB) jointly with makers and wholesalers, and an advancement in cost saving technologies for labor and store expenses as well as the lower cost of goods resulting from the increasing use of point of sales and other information systems and more direct contract with both Japanese and overseas producers.

For fiscal 1995, we expect consumer spending to recover in the latter half of the year as corporate earnings recover while consumer prices remain stable. However, prices should continue to fall and the business environment for retailers should remain tough. Department store sales are likely to remain weak despite the fact that post-bubble adjustments are largely completed. This is because consumers, who became more conscious about quality-price balance, are ignoring expensive department store goods, and corporations should continue their cost savings. Accordingly, both sales and earnings should remain in

severe condition for department stores even after fiscal 1995. For supermarkets, we expect sales to continue to grow supported by new store openings. Companies are responding to continued price competitions and a lower gross margin with an emphasis on expanding product alignment in their PB goods. However, fiscal 1995 earnings are likely to remain flat due to higher expenses for new store openings.

With a recent relaxation in the retail store opening regulations, new openings of large-scale stores or power centers—a kind of shopping center—have been activated throughout Japan. It appears that this trend will continue because of the low proportion of large stores in Japan compared to that of the U.S. Consequently, competition should increase between major supermarkets, local supermarkets and road-side shops. In these circumstances, major supermarkets are undertaking three strategies: 1) a stronger emphasis on discounting by Daiei and Jusco, 2) up-scaling by Nichii, and 3) refinement of the traditional style of general merchandise store by Ito Yokado. We will carefully watch the future successes or failures in each of these strategies.

(Kato Koji, economist)