Foreign Firms Overcome Obstacles

By Virginia Kouyoumdjian

In any study of Japanese trade protectionism, real or imagined, distribution is always targeted as one of the principal culprits. The American Chamber of Commerce in Japan (ACCJ) has it listed as the fifth most important barrier to successful imports. On the other hand, the Japanese government frequently retorts that the only significant roadblock is lack of effort. Where does reality lie in this delicate and controversial matter?

The answer may be found in the possibility that the issue is deeply rooted in an economic and social system, and that swiftly and permanently "correcting" it in the manner many of Japan's trade partners might wish would probably bring about some very negative results for Japan.

The fact that, from days of old, the wholesaler has been the most powerful link in the commercial chain has left both manufacturers and retailers at a serious disadvantage. Although there has been considerable change over the past few years and the distribution map will continue to change quite rapidly, dismantling a system hundreds of years old is a slow and painful procedure.

One factor which is helping to bring this about is the changing balance of power among manufacturers, wholesalers and retailers. Manufacturers have become bigger, more streamlined and more cost-conscious. Retailers have also grown in size, and modern technology has aided in obtaining electronically much of the vital information that once came from wholesalers. As a result, wholesalers have been squeezed at both ends.

Pressure from overseas seems welcome at times as a way to implement changes that might otherwise be politically difficult. As a result of pressure from the U.S. and other trading partners, a reform of the Large-scale Retail Store Law was enacted, making it easier for major retailers and importers to establish premises to sell their wares. Whereas opening any retail outlet larger than 500 square meters was a gargantuan task, since approval from neighborhood retail associations could take up to 10 years or never come, the maximum waiting period now has been cut to one year.

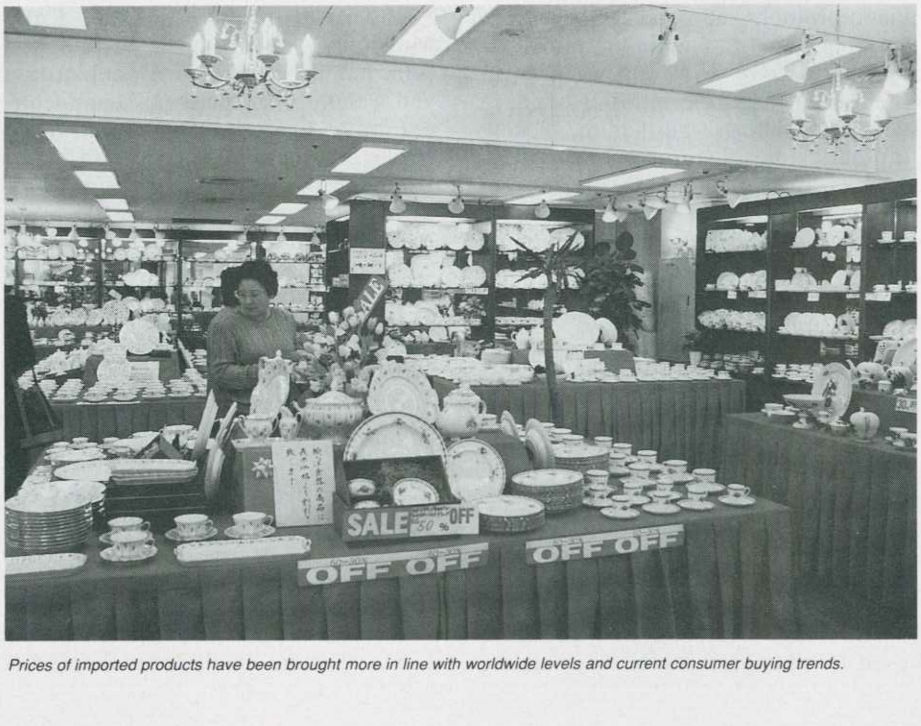
In addition, special concessions have been implemented which exempt from coordination procedures imported goods tied in to any new store or store expansion involving a surface of less than 1,000 square meters. Finally, the Japanese government continues to devote a section of its economic stimulation package to import promotion through the construction of foreign access zones (FAZ), and a greater emphasis towards regionalized promotion throughout the country with the help of the Japan External Trade Organization (JETRO).

Not just a trade problem

Although the ACCJ points a finger squarely at the Japanese distribution system as one of the main inhibitors to success of U.S. companies (ranked after high land/rent costs, staffing problems, strong interlinked business group relationships, and exclusionary business practices), there is also a fairly generalized recognition that the same problems often affect Japanese businesses. With the strength of certain established groupings and the tendency to rely on long-established relationships at all levels, it is extremely difficult even for a domestic newcomer to break into a new market.

Often, the biggest problem facing the foreign company is to find the combination of resources and long-term planning that are the basic requirements for making it in the Japanese market. There are several large companies, including Coca-Cola and IBM Corp., which are constantly held up as examples of just how well a foreign corporation can do, but successes such as these were not achieved overnight and required unusual commitment on the incoming side.

The pitfalls to finding a successful



Prices of imported products have been brought more in line with worldwide levels and current consumer buying trends.

path through the Japanese distribution maze are many, from establishing the right method to finding the right partners or collaborators, to pricing the product fairly and attractively. For many years, conventional wisdom stated that imported goods should be expensive and there was even a deeply held belief that sales volume would drop if prices were cut. Luxury goods and even everyday products sold at two or three times their retail price in their home or other export markets. This is one perception which has changed quite noticeably since the bursting of the Japanese economic bubble and it is now strictly unfashionable to buy expensive products simply because they are expensive. Brands like Cartier, Chanel and Wedgwood have all lowered their Japanese prices in recent months to bring them closer into line with worldwide levels.

Snobbery aside, one reason why many imported products have been so much more expensive than elsewhere is the higher cost of the distribution system. Often, a product has to go through a whole series of wholesalers (primary, secondary and even tertiary) with everyone taking a cut, before it gets anywhere near the retail level. Distribution costs have soared so dramatically that many Japanese companies have targeted that end of the business in order to substantially reduce their overhead. A prime example was the cosmetics and household goods manufacturer Kao Corporation which put in place its own delivery system, cutting out wholesalers completely.

Since there are numerous distribution routes for foreign companies to choose from, ranging from trading companies to tie-ups with manufacturers or retailers to setting up an independent system, there is plenty of room for error and many companies find that their first option is not necessarily the best one. One example of this is Apple Computer of the U.S. which started out with two negatives: its products were not formatted for the Japanese market (the computers could not handle *kanji*) and the distribution network was very limited, being centered mainly around Canon Sales Inc. Although the computers were always favorites among the design and small-scale publishing crowds, the real breakthrough did not come until both Japanese language and a wider distribution network were operational.

Since the end of 1992, the Japanese personal computer industry has been totally shaken by the advent of foreign companies such as Compaq Computer Corp. and Dell Computer which have seemingly bulldozed through perceived barriers to establish themselves in two very different ways. Compaq sells through a network of over 70 dealers, uses aggressive comparative advertising and places great emphasis on the very low price of its products. Dell sells almost exclusively though telephone and mail order and places emphasis on the high flexibility of its systems which can be configured exactly to the buyers' needs. Although neither company has yet to make a significant impact on the competition in term of sales, the reaction of both press and buying public has been extremely positive.

Another foreign company which has had a major affect on its industry is the retailer, Toys"R"Us. Opening its first store in Japan in 1991, the company now has six outlets and plans for another 14. The attraction of Toys"R"Us is that it offers a complete contrast to the average Japanese toy retailer, with more than five times as many items on display in its large stores, as well as competitive pricing. Toys"R"Us created a major flurry by attempting to cut out the wholesaler altogether and insisting on dealing directly with toy and game manufacturers. In theory, this would have been possible due to the scale of its stores, in turn made possible by the changes in the Large-scale Retail Store Law. In reality, however, the process is taking time and only a few manufacturers have so far accepted the direct route. The Japanese consumer, however, is responding enthusiastically and 1992 sales were more than twice what the company had originally estimated.

Aside from offering the Japanese consumer an unusual combination of great variety of products at low prices, Toys"R"Us has also been lucky in terms of the cost of setting up its business. Since it entered the market as the economic bubble burst, land prices and building prices have been highly negotiable. Despite this boon, costs remain considerably higher than in the U.S. and discounts are smaller since there is still fairly heavy use of wholesalers. Even though it has eliminated Japanese practices, such as wrapping everything carefully in paper and having a large staff ready to explain and show items not in use, Toys"R"Us does make some concessions to local ways by having some products that can be tried before buying. Finding the right balance between what works in the country of origin and what will be accepted and even welcome by the Japanese consumer is one of the greatest challenges.

Food industry challenges

The greatest shock faced by one European retailer of wine and food on trying to establish business links with Japanese restaurants was the discovery that they would only buy wine by the bottle, never by the case. This was not a plot to send the importer on the road to ruin, it was necessitated since most restaurant premises simply do not have enough room to stock wine by the case. The result is that restaurants require very frequent deliveries of wine, which makes it virtually impossible for a small- or medium-sized importer to bypass the wholesale system, given the cost of making frequent small-scale deliveries. This logistics issue is typical of the kind of uniquely Japanese problem that importers are faced with.

Another issue with food and wine is the enormous sophistication gap between the large cities of Tokyo and Osaka and the rest of the country. A metropolis like Tokyo offers an enormous concentration of potential customers who are easy to reach and often familiar with foreign products. Away from this concentration, even larger regional cities offer much more limited markets that can be time-consuming and difficult to access. This is true of virtually any product or service although recent years have seen some interesting new networks that can be

Photo: PRAP JAPAN, inc.

The opening of foreign capital retail outlets such as Toys"R"Us has accelerated the revision of the Large-scale Retail Store Law.

used to the advantage of importers.

Any foreigner in Japan is familiar with the difficulty of finding "foods from home" once in the heartland of the country. Many importers deal with department store chains, large supermarkets and high-end grocers that are not easily found in smaller towns and villages across the country. One type of retail outlet, however, which is found everywhere is the convenience store. Between them, the 10 largest chains have close to 20,000 stores throughout the country and these 24-hour outlets are being used on a regular basis by an increasingly diverse range of customers.

An American premium ice-cream manufacturer, Häagen Dazs, plugged early into the convenience store network and its products can now be easily found in the most remote parts of the country. It has done this, however, while still insisting on keeping a tight grip on the distribution process, keeping its products to a single wholesaler while most ice cream manufacturers use two and even sometimes three.

Luxury goods and direct mail orders

As Japanese consumers have traveled overseas in greater numbers, the discrepancy between prices charged for luxury goods at home and abroad has become an increasing source of discontent. As a result, and also driven by the economic slowdown, many luxury goods manufacturers have cut prices on their products to make them no more than 1.5 or 1.6 times as expensive as in their country of origin.

At the same time, there has been a move by a number of these companies to reorganize their distribution routes. Rather than aiming to expand rapidly and sell through as many outlets as possible, the companies are now eager to reduce the number of outlets for their products so as to simplify their access to retailers and cut out the need to deal with numerous wholesalers. In addition, the companies thus hope to maintain their prices at a certain level.

One way for foreign companies to break through the various difficulties in selling their products in Japan is to adopt a totally different approach to marketing, thereby avoiding certain problem areas. Direct mail is one such route but it comes with its own set of problems, basically the traditional Japanese perception of direct mail products as being cheap in both price and quality. The French company Damart, purveyor of thermal underclothing to several generations of Europeans, originally set up its business in Japan on a very small scale and concentrated on building up a viable information database. In order to gain the confidence of customers, all-encompassing guarantees were offered along with the possibility of returning products that were not satisfactory. The company completely avoided conventional sales channels and whereas in France half of sales are through retail outlets, virtually all Japan sales are by mail.

The concept of reinventing the image of direct mail products has proved a timely one, especially given the growing sophistication of customers who know just what they want and are unwilling to do the rounds of several department stores looking for one that has the item in stock. In order to ensure the swift flow of products to customers, Damart took the plunge and built a major logistics center in Tochigi Prefecture, north of Tokyo. The company's business is seasonal and the idea is to make the warehouse available to other companies during the annual slow times. This in turn fits in well with the growing tendency for companies to assume their own distribution, moving away from wholesalers, which makes the availability of rentable warehouses crucial.

Although there is no doubt that a great deal can still be done to improve the efficiency of Japan's distribution system, the changes that have already taken place have improved the situation a great deal. The breaking away of a number of major manufacturers and the increasing strength of major retailers have loosened the grip of the wholesalers on the traffic of goods. The availability of large quantities of point of sales-based computerized data from many different sources has also made it easier to be fully prepared for the conditions of the local market. In addition, the efforts of the government to move the situation along have resulted in concrete improvements despite the continuing push for even more from overseas.

There are still a number of points of contention: for example the fact that distributors, wholesalers and retailers are not allowed to pass on manufacturer price discounts to customers, and the restrictions on premium giving as a way to help a new product into the market. Overall, however, the trend is certainly positive. And perhaps most significantly, some foreign companies are taking a much more positive approach to the whole issue by buying out their distributors and so opening up a whole new world of possibilities for themselves. The most efficient way of turning the dinosaur into a modern juggernaut once and for all may well be from the inside.

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