

Japanese convenience stores and drugstores: Opportunities for European snack and beverage products under Corona

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Executive summary

The aim of this report is to (a) present an overview of trends and opportunities on the Japanese convenience store and drugstore market under the Corona pandemic and to (b) deliver strategic insight, tactical guidance and real-life examples of how to succeed in the Japanese convenience store and drugstore market.

This report includes:

1. An overview of the Japanese convenience store and drugstore market, including key industry players and current market opportunities under the Corona pandemic.
2. Presentation of new ways to rethink strategy and market entry on the Japanese convenience store and drugstore market. Case studies and company examples drawn from the experiences of European small and medium sized enterprises (SMEs) are introduced to show novel approaches to market entry.

This report has two main target groups: (1) European SMEs selling snack and beverage products with an interest in entering the Japanese convenience store and drugstore market, and (2) companies with an existing setup on the Japanese market but sending the need to rethink strategy: for example, by revitalising the company's sales and marketing activities in the Japanese market.

Introduction

Despite almost three decades of recession, Japan remains the third largest economy in the world. Close to 126 million sophisticated consumers with high purchasing power and discerning tastes make Japan the third largest consumer market in the world.¹ No other country in the world is as concentrated a source of revenue for so many brands as Japan.

Despite the sheer size of the total Japanese market, there are many other reasons for European snack and beverage brands to consider market entry to Japan – especially right now under the Corona pandemic:

- Japan has close to 60,000 convenience stores and well over 20,000 drugstores which are basically thriving right now as shoppers are reluctant to travel far to buy daily necessities during the Corona pandemic.
- The total retail industry market in Japan exceeds JPY 145,000 billion (EUR 1,175 billion), and in combination, convenience stores and drugstore sales amount to a staggering JPY 19,019 billion (EUR 154 billion) and jointly represent more than 13 percent of the total Japanese retail market.
- The processed food and beverage category accounts for more than 30 percent of the total sales in Japanese convenience stores and drugstores and the share is increasing further under the Corona pandemic.
- Competition for customers has intensified among convenience stores and drugstores and especially in the snack and beverage product category, major Japanese chain stores are using for example imported European products to diversify themselves in the competition.
- Despite a drop of nearly 10 percent in the number of store visitors during the first months of the Corona pandemic, the largest convenience store operator in Japan, Seven-Eleven, still boasts 25 million store visits *every day* to its more than 21,000 shops in Japan.

Apart from the market size and a generally increasing demand for European snack and beverage products in Japanese convenience stores and drugstores, there is another important reason for targeting the Japanese market. In the 1960s there was a lot of talk about a Japanese model called ‘the Flying Geese’. In this analogy, the Flying Geese model shows how one economy, like the first goose in a V-shaped formation, will lead other economies toward industrialization, passing older technologies down to the followers as its own incomes rise and it moves into newer technologies. Decades ago, Japan was the technological lead-geese in Asia. While this may have changed over time, Japan has developed to become the influential lead-geese in Asia in *new* areas like music, lifestyle, fashion, and other trends. This is also the case with the Japanese snack and beverage market. When international snack or beverage brands, for example, discuss market entry to Korea, Taiwan, or the huge Chinese market with potential local distributors or partners, the first question is often: “Do you sell in Japanese convenience stores, and what are the results?”. Japan is

¹ Statistics Bureau of Japan, December 2020: <https://www.stat.go.jp/>

very often the key reference for the large players on other Asian markets of interest to European firms, and if a brand succeeds in Japan it will automatically create demand from other markets in Asia. In other words, succeeding in the Japanese market is of strategic importance for European snack and beverage brands.

This report has two main target groups: (1) European snack and beverage brands with an interest in entering the Japanese market, and (2) companies with an existing setup on the Japanese market but sending the need to rethink strategy: for example, by revitalising the company's sales and marketing activities in the Japanese market.

Most reports on the Japanese snack and beverage market focus on the overall development of the market and macro trends – or on the more technical aspects such as legislation and import regulations etc. that govern the market. While this may be very helpful for an initial and general orientation, the contribution of this particular report is a targeted focus on European SMEs and with lots of pragmatic advice on how to actually establish sales in convenience stores and drugstores on the Japanese market. Rather than a presentation of data, regulations (e.g. labelling, tariffs, procedural requirements etc.)² and trends, *this report aims to deliver strategic insight, tactical guidance and real-life examples of how to succeed with European snack and beverage products in the Japanese convenience store and drugstore market.*

The report is structured as follows:

- Following the introduction, part 1 will present an overview of the Japanese convenience and drugstore market. This will include the overall development of the market, but also a closer look at all the key segments, trends and opportunities under Corona. This part also includes an overview of key players on the market.
- Part 2 will provide a critical discussion of distribution channels on the Japanese convenience and drugstore market and, through a number of company examples, offer detailed advice and practical guidance on strategic pricing and how to evaluate the different market entry options. Also, in this part of the report we will discuss and evaluate new ways to rethink strategy and market entry for European snack and beverage brands on the Japanese convenience store and drugstore market. Case studies and company examples will be introduced to show novel approaches to market entry.

Throughout the report, case studies of European SMEs on the Japanese market will be introduced. For reasons of confidentiality, there are company names which we cannot disclose. In each case, however, we will describe the company's profile, product and price range, enabling the reader to better understand the context of the case study.

To complete this report, we have analysed publicly available data and industry reports, studied companies' annual reports, and interviewed a wide range of executives at international snack and beverage companies, convenience stores, drugstores, and industry associations.

The exchange rate used throughout this report for converting Japanese yen into Euros is 0.81

² Please see the website of The EU-Japan Centre for Industrial Cooperation for information <https://www.eubusinessinJapan.eu/>

1. Overview of the Japanese convenience store and drugstore market

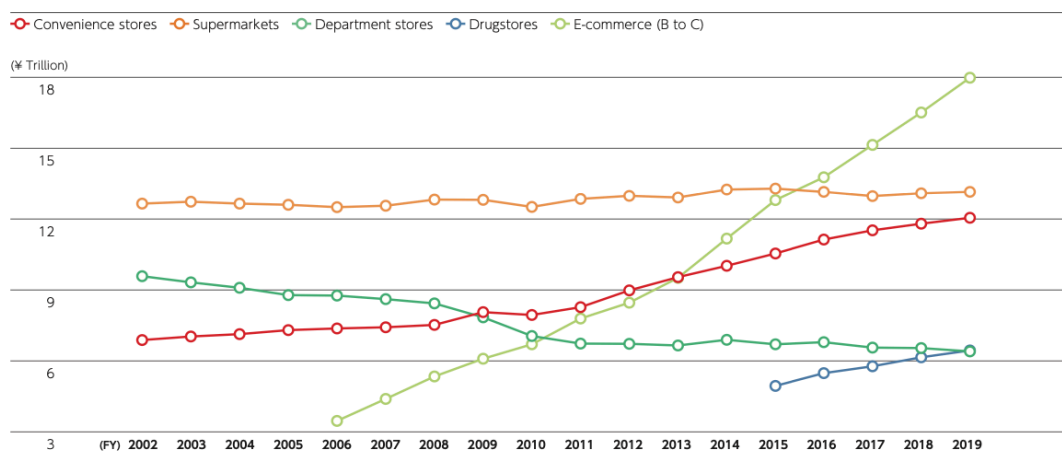
In this part, we will present an overview of the Japanese convenience store and drugstore market. The discussion is structured as follows:

- A. Overall development of the Japanese convenience store and drugstore market.
- B. Key players and opportunities in the market.
- C. Opportunities under Corona.
- D. Import regulations and market access to Japan.

a. Overall development of the Japanese convenience store and drugstore market

According to the Ministry of Economy, Trade and Industry, the total Japanese retail industry market had an estimated value of JPY 145,047 billion (EUR 1,175 billion) in 2019.³ The retail market can be segmented in various ways. It is customary to distinguish between for example supermarkets, department stores, convenience stores, drugstores and B2C e-commerce. Compared to most Western markets, the Japanese retail market has a slightly unfamiliar structural feel to it. Apart from a booming e-commerce market, the landscape is dominated by the growth of convenience stores and drugstore groups.

Trends in net sales at major store formats:



Source: Ministry of Economy, Trade and Industry Japan (2020)

³ The main sources on the Japanese convenience store and drugstore market are statistics from the Ministry of Economy, Trade and Industry, Japanese industry organisations, annual reports, and investor relations material from key industry players. Please see the list of references for details.

The total retail market continues to grow and as illustrated with the table below, convenience store sales make up 8.4 percent of the total sales. In sales value, this represents total convenience store sales in 2019 of JPY 12,184 billion (EUR 99 billion). Drugstore sales represent 4.7 percent of the total Japanese retail market in 2019 and accordingly account for total sales of JPY 6,835 billion (EUR 55 billion). Together, convenience store sales and drugstore sales amount to JPY 19,019 billion (EUR 154 billion) and represent more than 13 percent of the total Japanese retail market - and the share is increasing.

Market share of convenience stores share and drugstores in Japan (billion JPY):

	2017	2018	2019
Total retail market	142,514	144,965	145,047
Convenience store sales	11,745	11,978	12,184
Drugstore sales	6,057	6,364	6,835
Convenience store share	8.2%	8.3%	8.4%
Drugstore share	4,3%	4,4%	4,7%

Source: Own model based on data compiled from the Ministry of Economy, Trade and Industry (2020)

From the monthly statistics on trade, published by the Ministry of Trade, Economy and Industry, it is clear that while the revenue of supermarkets, department stores and most other physical stores have been suffering under the Corona pandemic, convenience stores and drugstores, however, seem less affected and sales of have been quick to recover and reach somewhat normal pre-Corona levels. In fact, if subtracting the sale of services which has dropped almost 25 percent under the Corona pandemic, the sales of physical goods (food, beverages, non-food items) have even increased.⁴

In Asia Nikkei,⁵ Mr. Sadanobu Takemasu, president of the Japan convenience chain store Lawson, offers the following explanation as to why convenience stores sales have been growing under the Corona pandemic: "Customers are reluctant to travel far to buy daily necessities during the pandemic (...) The number of customers within a 354-meter radius of each store has increased, especially in the evening (...) This shows exactly the current consumer behaviour." So, with the huge numbers of local shops all over Japan, convenience stores and drugstore chains are fundamentally better positioned to adjust to new consumer behaviour amid the pandemic.

⁴ See the monthly publications by the Ministry of Trade, Economy and Industry, *Shōgyō dōtai tōkei*, available for download here: <https://www.meti.go.jp/english/statistics/tyo/syoudou/index.html>

⁵ Asia Nikkei, 8 October 2020: <https://asia.nikkei.com/Business/Retail/Japan-s-convenience-chains-see-ray-of-hope-despite-COVID>

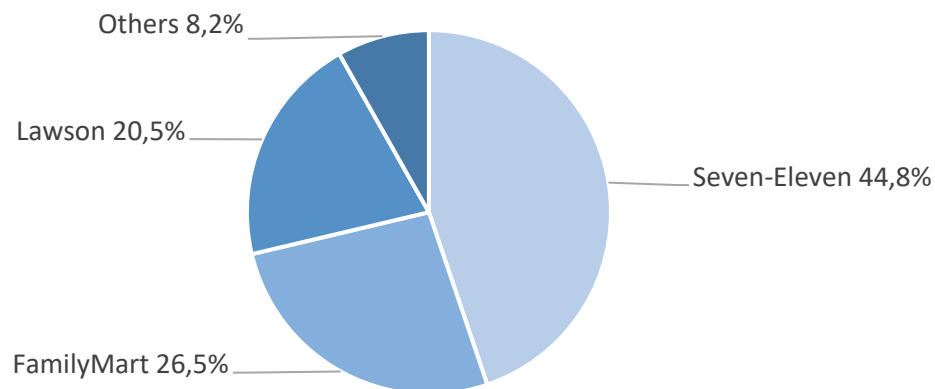
b. Key players and opportunities in the market

Let us take a closer look at the two categories: (i) convenience stores, and (ii) drugstores, including an overview of the key players and (iii) trends and opportunities in the market for European exporters of snack and beverage products.

i. Convenience stores

In October 2020, The Japan Franchise Association, which is the main Japanese industry organisation for convenience stores, estimated that there is a total of 55,852 convenience stores in Japan.⁶ Together, the three largest convenience store chains in Japan, Seven-Eleven, FamilyMart and Lawson, jointly represent close to a 92 percent share of the total convenience store sales in Japan.

Major convenience store chain's market share in Japan:



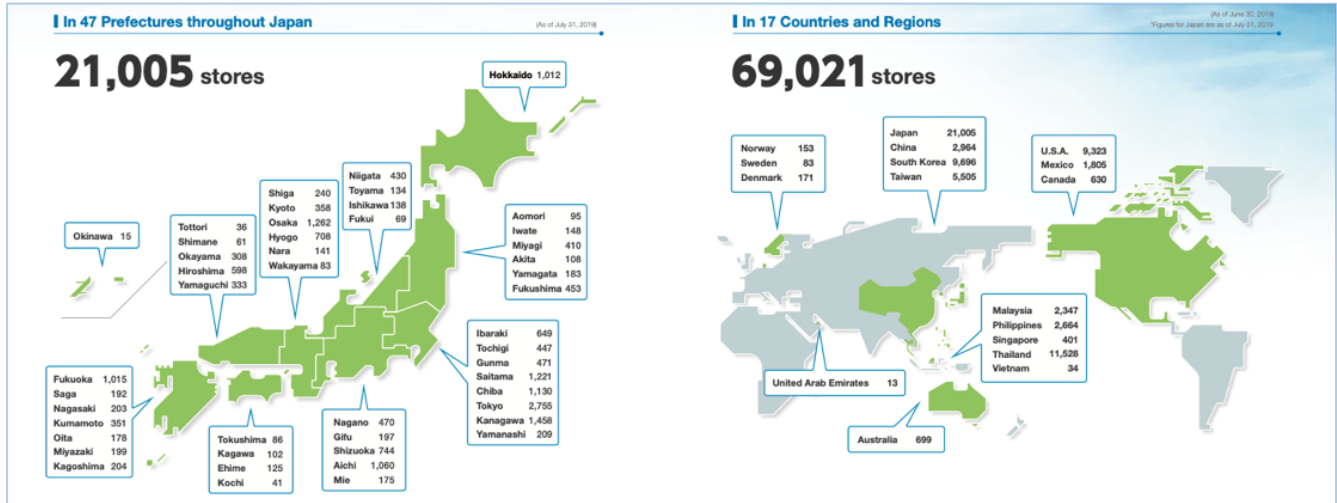
Source: Own model based on annual reports from Seven-Eleven Japan, Lawson, FamilyMart and Japan Franchise Association's Convenience Store Statistics Investigation Monthly Report, October 2020.

Below, we will present a brief outline of the three major convenience store chains: Seven-Eleven, FamilyMart and Lawson. First, Seven-Eleven⁷ is the largest of the three main convenience store groups with 21,005 shops in Japan and a grand total of 69,021 shop spread across 17 countries.

⁶ The Japan Franchise Association, <https://www.jfa-fc.or.jp>, October report 2020.

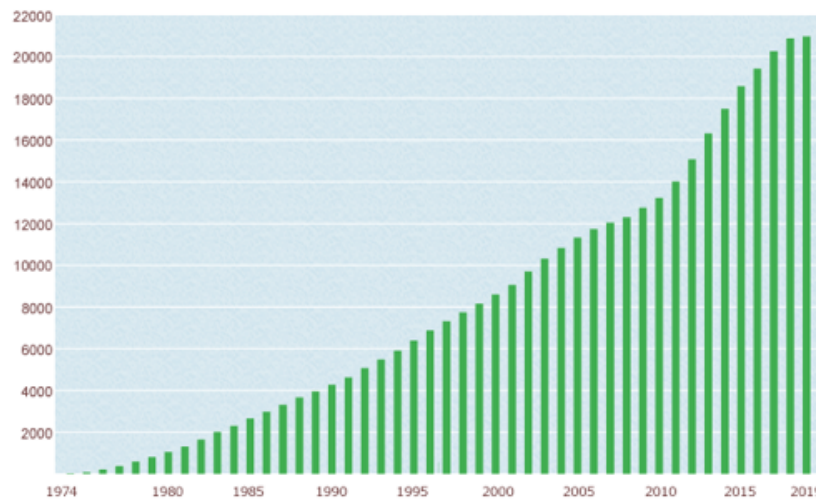
⁷ Information about Seven-Eleven Japan is primarily based on Seven-Eleven Corporate Outline FY 2020 available here: https://www.7andi.com/en/ir/file/library/co/pdf/2020_all.pdf

Seven-Eleven convenience stores globally and in Japan:



Source: Seven-Eleven Corporate Outline FY 2020

Seven-Eleven Japan: Number of stores opened 1974-2019:



Source: Seven-Eleven Corporate Outline FY 2020

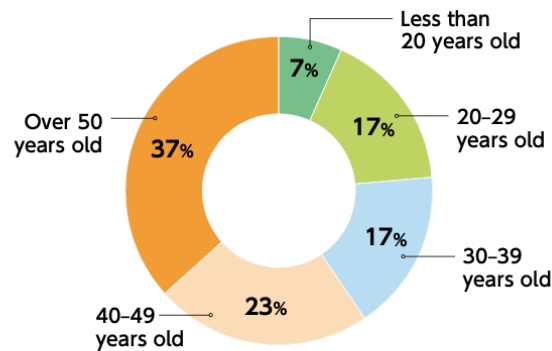
The revenue and operating income of Seven-Eleven Japan has been growing every year, and in Japan alone almost 25 million people visit a Seven-Eleven convenience store every day.⁸ Compared with the other convenience chain stores in Japan, Seven-Eleven has the highest average number of customers per day. The customer profile for Seven-Eleven and other convenience stores in Japan has, however, changed over the years, whereas almost 50 percent of the

⁸ For further details, see the English version of Seven-Eleven Corporate Outline FY2020, available through this link: https://www.7andi.com/en/ir/file/library/co/pdf/2020_all.pdf

customers were under 30 years old two decades ago, today 60 percent of all Seven-Eleven customers are above 40 years old and the vast majority over 50 years old.

Composition of customers by age group, Seven-Eleven FY 2020:

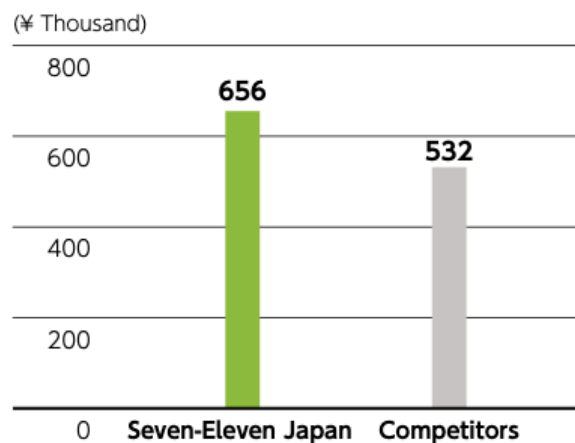
■ Composition of Customers by Age Group (FY2020)



Source: Seven-Eleven Japan Corporate Outline FY 2020

The average spending per customer in a Seven-Eleven shop in 2020 is JPY 656 (EUR 5.31), which is higher than the industry average of JPY 532 (EUR 4.31), as calculated by The Japan Franchise Association.⁹

Average spending per customer in Japanese convenience stores:

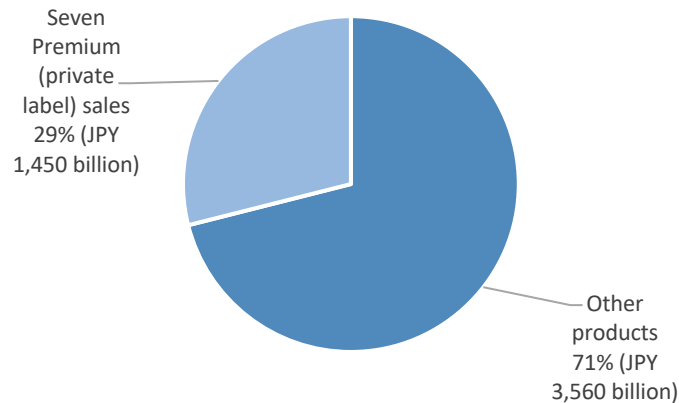


Source: Seven-Eleven Corporate Outline FY 2020 and Japan Franchise Association

⁹ The Japan Franchise Association, <https://www.jfa-fc.or.jp>, October report 2020.

Apart from having the largest network of stores both in Japan and world-wide, Seven-Eleven is differentiated from competitors by focusing strongly on a private label strategy. Under its private brand, Seven Premium, Seven-Eleven has developed a wide range of products and according to the latest annual report, total sales of Seven Premium products accounts for nearly 30 percent of the total sales in all Seven-Eleven stores in Japan!

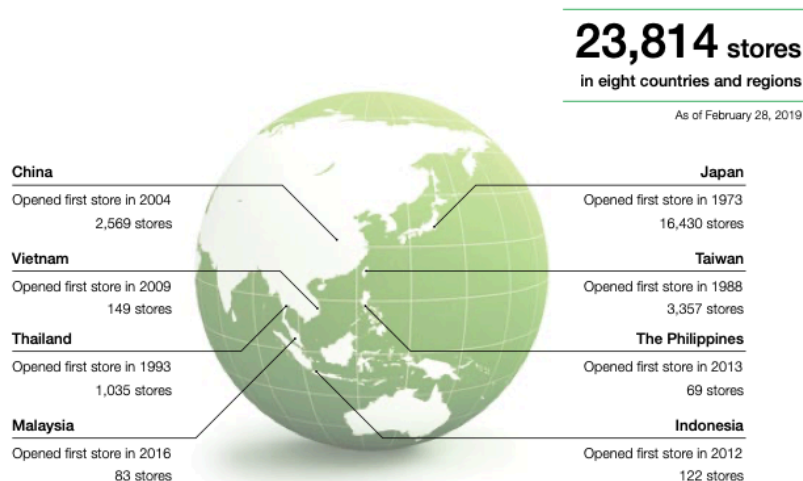
Seven-Eleven private label, Seven Premium, sales:



Source: Own model based on Seven-Eleven Corporate Outline FY 2020

With 16,430 shops in Japan and an international network of totally 23,814 shops, FamilyMart is the second largest convenience chain store in Japan.¹⁰ The existing FamilyMart network is the result of a merger with Sunkus and Circle K Japan in 2016.

FamilyMart convenience stores:

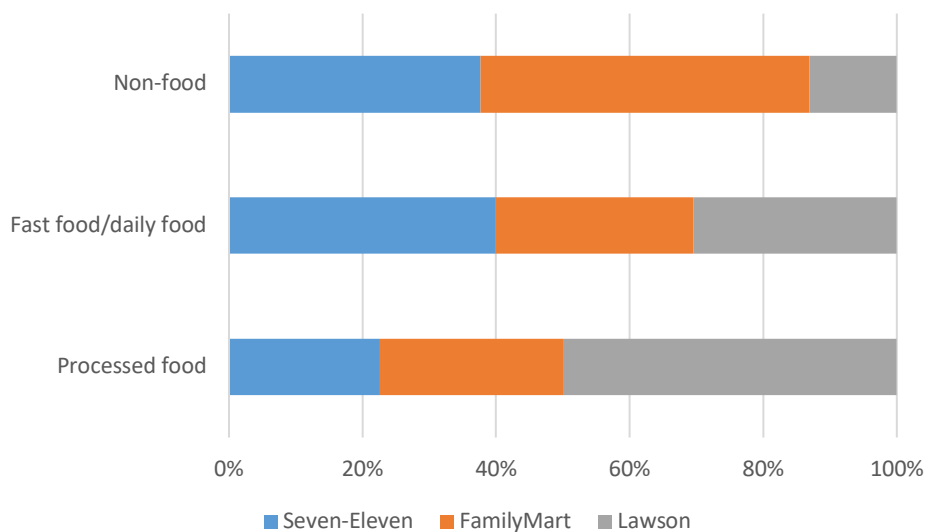


Source: FamilyMart Integrated Report 2019

¹⁰ Information about FamilyMart in this section is primarily based on: FamilyMart Integrated Report 2019 available here: https://www.family.co.jp/content/dam/family/english/ir/library/annual/document/FM_AR19E_all.pdf

Compared to the two main competitors, Seven-Eleven and Lawson, FamilyMart is strongest in the non-food segment which accounts for 34 percent of the total sales. Non-food items include primarily cigarettes and magazines. The fast food and daily food categories include perishable foods (vegetables, fruits, meat etc), bakery items, ice creams, fresh foods, rice, noodles and over-the-counter fast food. Beverages and snack products are categorised under processed food. Below we will take a closer look at the convenience store chain, Lawson, which by far outnumbers both FamilyMart and Seven-Eleven in terms of revenue generated from processed food and thereby beverages and snack products which is our main interest in this report.

Sales by category in Japanese convenience stores:



Source: Own model based on corporate material from Seven-Eleven, FamilyMart, and Lawson.

The convenience store chain, Lawson, has the third largest network of shops in Japan.¹¹ The total number of Lawson stores in Japan is 14,805 and in addition to this the company operates 2,210 stores overseas. In Japan, Lawson also operates a sub-branded chain of convenience stores under the name of Natural Lawson which may be of special interest for European snack and beverage brands. The slogan of Natural Lawson is “Contributing to more beautiful, healthy and relaxed lifestyles”. As of August 2020, the number of Natural Lawson shops in Japan is 146.¹² The shops are located in business districts of large Japanese cities to cater to especially working women. Natural Lawson shops focus on carefully selected healthy, low-calorie foods, snacks and drinks made from select ingredients, and environmentally friendly detergents and cosmetics. Accordingly, Natural Lawson stores have won a following among internationally minded and health-conscious Japanese consumers.

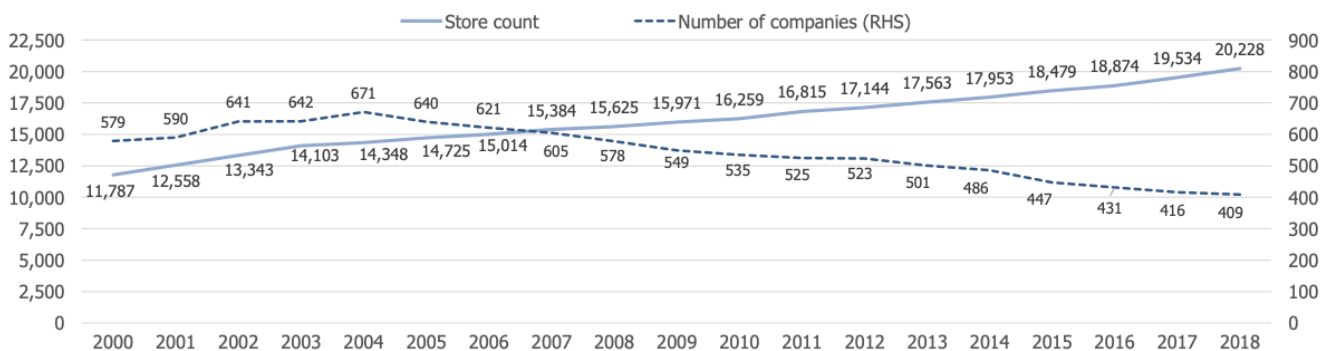
¹¹ Information about Lawson and Natural Lawson is primarily based on Lawson Integrated Report 2020, available here: https://mldata.lawson.jp/en/ir/library/pdf/annual_report/ar_2020_e.pdf

¹² Ibid.

ii. Drugstores

There are currently more than 20,000 drugstores in Japan and the number continues to rise due mainly to aggressive new store openings by the large Japanese drugstore chains. At the same time, the number of companies operating drugstore chains in Japan has fallen, from 579 in 2000 to 409 in 2018.¹³ Over the years, large drugstore chains have continued to acquire small and medium sized drugstore chains, while others have basically gone out of business due to increasingly hard competition.

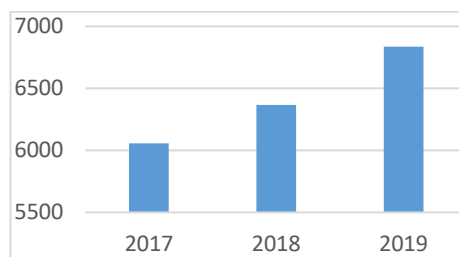
Total number of drugstores and drugstore companies in Japan:



Source: Shared Research, based on data from the Japan Association of Drugstores

According to the Ministry of Economy, Trade and Industry, the drugstore sales in Japan have been growing for the past twenty years, and in 2019 total drugstore sales amounted to JPY 6,835 billion (EUR 55 billion). The growth rate has been moving in the 5-7 percent range since 2016, closing the gap with the convenience store market and supermarkets in Japan.

Total drugstore sales in Japan:

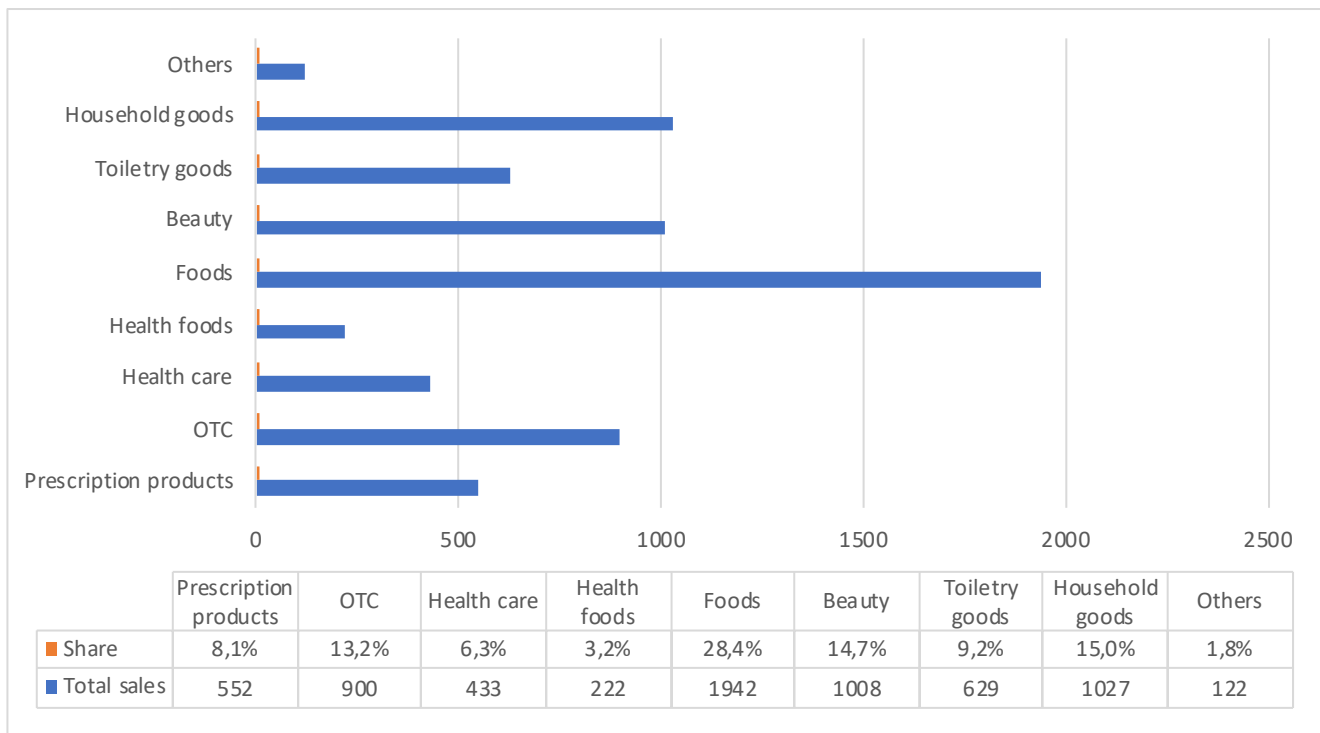


Source: Own model based on Shōgyō dōtai tōkei. Ministry of Economy, Trade and Industry Japan, 2020

¹³ This part is primarily based on analysis from Shared Research (<http://sharedresearch.jp/>), data from the Japan Association of Drugstores (<https://www.jacds.gr.jp>), and investor relations material from major drugstore chains in Japan.

One of the main drivers of growth for the drugstore sector in Japan has been a steady increase in food sales over the years.¹⁴ As illustrated with the model below, food and beverage products account for 28.4 percent of total drugstore sales in Japan. In addition to this comes the category of healthy food products with 3.2 percent of sales, so together, food and beverage products make up totally almost 32 percent of all drugstore sales in Japan. This is an astonishingly high number, compared to the low 8.1 percent for prescription pharmaceuticals and 13.2 percent for over-the-counter (OTC) pharmaceuticals which is where one would otherwise expect drugstores to make the most revenue.

Drugstore sales by category (JPY billion). Industry average 2019:



Source: Own model based on Shōgyō dōtai tōkei. Ministry of Economy, Trade and Industry Japan (2020)

Below, let us take a closer look at the top drugstore chains in Japan. Welcia is the drugstore chain with highest revenue and one of the leading drugstore chains in Japan. In the following section we will examine Welcia and their operations on the Japanese market in further detail.

¹⁴ Shōgyō dōtai tōkei. Ministry of Economy, Trade and Industry Japan (2020)

Top drugstore chains in Japan: Profile and latest full-year sales as per October 2020 (JPY million):

Sales ranking	Drugstore chain	Latest full-year sales	Profile
1	Welcia	868,280	One of the leading drugstore chains in Japan. An Aeon group company. Has strength in running pharmacy business and 24 hour stores.
2	Tsuruha	841,036	One of the leading drugstore chains in Japan. Originally based in Hokkaido, expanded Coverage southward to now include Okinawa.
3	Sundrug	617,769	Drugstore chain based in Tokyo, emphasizing low-cost operations. Operates discount stores mainly in West Japan.
4	Cosmos	611,137	Drugstore chain based in the Kyushu region. Has expanded business with area-dominance strategy opening multiple large stores in small trade areas and emphasizing low pricing.
5	Matsumoto Kiyoshi	590,593	Pioneer in city-type drugstore business. Operates nationwide, centring on the Kanto region
6	Sugi	541,964	Based in the Tokai region. Operates Sugi Pharmacies, a chain of drugstores with pharmacies.
7	Cocokara Fine	403,875	A major drugstore chain. Born and expanded out of M&A, starting with consolidation of Seijo in the Kanto region and Segami in the Kansai region

Source: Own model, based investor relations material from each of the companies, and analysis by Shared Research based on Japan Company Handbook 2020

As of April 2020, Welcia operates 2,005 drugstores in Japan.¹⁵ Annual sales in the financial year ending February 2020 amounted to JPY 868 billion (EUR 7 billion). For the last couple of years, Welcia has opened around 100 new stores every year and achieved around 10 percent sales growth. Future forecasts by Welcia Holdings indicate more or less the same growth in revenue and in the number of new store openings, reaching more than JPY 1 trillion (EUR 8.1 billion) in sales by End-February 2022 and more than 2,300 stores by the end of the financial year in February 2023.¹⁶

In Welcia stores, food and beverage sales account for 22.2 percent which is below the aforementioned industry average of 32 percent.¹⁷ With more than 56 percent of total sales coming from food and beverages, the drugstore chain, Cosmos, is by far the chain with the highest percentage of food and beverage sales in Japan. The closest competitors in this category are Welcia and Tsuruha, both with food and beverage sales ranging only around 22 percent of total sales. In sales ranking, Cosmos is the fourth largest drugstore chain and in Japan they operate a total of 1092 drugstores.¹⁸ The largest number of Cosmos stores is in the Kyushu region. The presence of Cosmos is also strong in Western Japan while significantly weaker when approaching the Kanto region and Northern prefectures. This is in line with the Cosmos strategy of dominating specific areas where they open multiple large stores emphasizing low pricing.

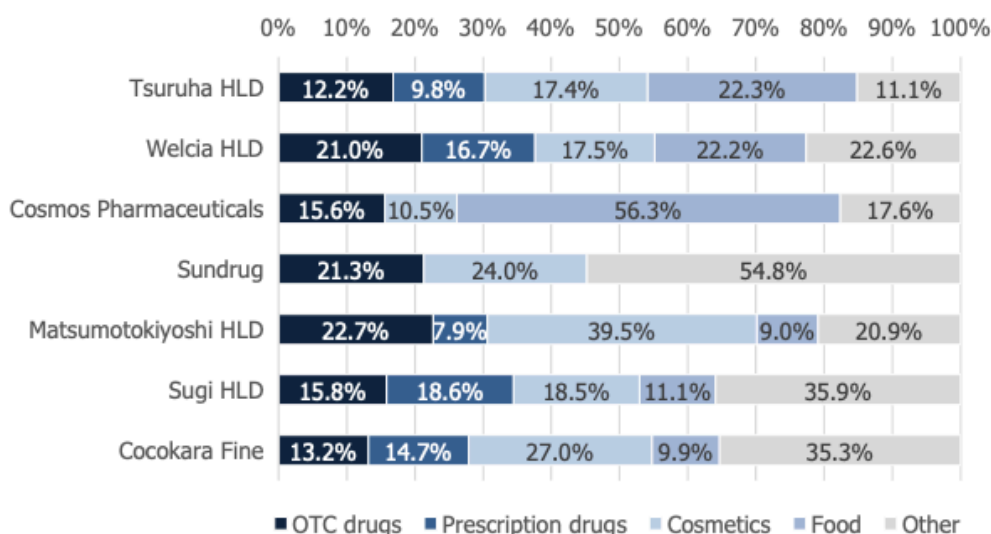
¹⁵ The section on Welcia is based on: Welcia Holdings Co., Ltd. Financial Results Briefing for the Fiscal Year Ended February 2020 (<http://www.welcia.co.jp/en/latest/main/08/teaserItems1/0/linkList/09/link/FYE2020%204Qfinancialresults200417en.pdf>)

¹⁶ Ibid.

¹⁷ See the model *Drugstore sales by category (JPY billion). Industry average 2019* earlier in this section.

¹⁸ Based on (<https://www.cosmospc.co.jp/> Read on 30 November 2020. Website and material only available in Japanese.

Categorized sales by major Japanese drugstore chains:



Source: Welcia Holdings Co., Ltd. Financial Results Briefing for the Fiscal Year Ended February 2020

A notable point in the ranking of size and sales of the Japanese drugstore market players is that Matsumoto Kiyoshi in the 5th place and Cocokara Fine in the 7th place have agreed to a business merger planned for October 2021. After the upcoming merger, the two companies will jointly become the biggest player in the Japanese drugstore market with combined sales of more than JPY 1 trillion (EUR 8.22 billion) and nearly 3,000 stores all across Japan. The main partner in the merger is Matsumoto Kiyoshi with 1,726 shops all across Japan per 30 June 2020.¹⁹ Matsumoto Kiyoshi is strongest in the Kanto region, including Tokyo, where the company was the pioneer in city-type drugstore business. For Matsumoto Kiyoshi, the health and beauty-related product categories of drugs, cosmetics, and toiletries account for roughly 70% of the total revenue while the food and beverage category is relatively small, only accounting for 9 percent. If the appeal of convenience stores – our other main category of chain stores - is that they are "close and convenient", then Matsumoto Kiyoshi has been expanding its support by being "cheap and convenient".

After the planned merger In October 2021, Cocokara Fine will join forces with Matsumoto Kiyoshi and the joint mission is to be the “Number one in Asia in beauty and health”.²⁰ Matsumoto Kiyoshi’s partner, Cocokara Fine, currently has a network of 1,145 drugstores and is particularly strong in the Kansai region including the main city, Osaka.²¹ As with merging partner, Matsumoto Kiyoshi, the food and beverage category for Cocokara Fine is also relatively low compared with both the industry average and all main competitors in the aforementioned top-7 list of drugstore chains in Japan.

¹⁹ Based on 2020-2021 Corporate Profile, Matsumoto Kiyoshi Holdings (<https://www.matsumotokiyoshi-hd.co.jp/ir/>) accessed on 30 November 2020. Only available in Japanese.

²⁰ Global Media Corporation, <https://www.gm-group2.net/industry-trends/burgeoning-drugstore-industry.html>

²¹ Based on Shared Research’s report on Cocokara Fine (<https://sharedresearch.jp/en/3098>), updated version 12 November 2020.

iii. Convenience stores versus drugstores

In this section we will highlight the main differences between the two categories of sales channels we have been discussing so far: Japanese convenience stores and drugstores.

Main differences between convenience stores and drugstore chains in Japan:

	Convenience stores	Drugstores
Number of stores	60,000+	20,000+
Total sales 2019 (billion JPY)	12,184	6,835
Food and beverage share of sales	33%	32%
Image	'Close and convenient'	'Cheap and convenient'
Competition strategy	Differentiation	Low price
Chain store operators	Very few: Three largest chains account for 92% of the market	Relatively many: Seven largest chains account for 34% of the market

Source: Own model

The number of convenience stores in Japan is almost three times higher than the number of drugstores on the market. The convenience store market is dominated by three main players, jointly representing 92 percent of the market while the drugstore market, despite consolidation, is represented by a larger number of different chains. The total sales of convenience stores are almost double the total sales of drugstores in Japan, but individual shop sales are much higher for drugstores due to larger size of individual stores and a significantly wider selection of products. The average share of processed food and beverage sales is about the same for both categories, but a major difference is that for the top seven drugstore chains in Japan processed food and beverage sales represents only 18 percent, which is far below the drugstore industry average of 32 percent.

A vast majority of the executives we have interviewed for this report and worked with over the years mention that it has been easier for them to establish business relations with drugstores than convenience store chains in Japan. This will be discussed and elaborated in the following part on distribution and strategy. First, let us delve further into the most important difference between convenience stores and drugstore chains: Competition strategy and strategic fit for European SME exporters to Japan.

In very general terms, drugstores compete on price, while convenience stores compete on differentiation. Here are two simple examples: You can buy a 525ml bottle of Oi Ocha, a popular green tea, for JPY 78 (EUR 0.63) at the drugstore chain Welcia. At Seven-Eleven a 600ml bottle of Oi Ocha costs 120 yen (EUR 0.97). On a per milliliter price comparison, Seven-Eleven's price is 34 percent higher than Welcia. Additionally, when comparing the same cup of ice cream that you can buy at Welcia for 108 yen (EUR 0.87) is sold at Seven-Eleven for 130 yen (EUR 1.05). The same ice cream is 17 percent cheaper at Welcia.

This is something Welcia can do because the company captures its margin in cosmetics, over-the-counter drugs, and prescription pharmaceuticals. For example, in the latest annual report, Welcia announces a gross margin for food products of 20.9 percent which is the lowest gross margin for the company among the other main categories: Gross margin for pharmaceuticals 41 percent, cosmetics 34.5 percent and household goods 29 percent.²² So, while food and beverage products in drugstores are sold at lower retail prices, the drugstore chains apparently seem to accept a comparatively lower margin on food and beverage products and will surely expect the same from suppliers, including European SMEs. As will be elaborated in the following part on distribution and strategy, EU exporters should be prepared for tough discussions on margins and price points in the market. While price competition is fiercer among drugstores, you will on the other hand find a larger number of different drugstore chains to negotiate with. For the convenience store market, there is basically only three chain stores to approach and negotiation power is naturally huge on the buyer side.

c. Opportunities under Corona

History tells us that any big crisis will disrupt the competitive order. In this section we will examine how the Corona pandemic may present new and unique business opportunities for European SMEs on the otherwise complex and somewhat conservative Japanese market. Prior to delving into the changes, disruption and opportunities that the pandemic may offer for European exporters of snack and beverage products to Japan, we will briefly discuss how Japanese consumer preferences are currently changing and how this may further support the business opportunities for European exporters of snack and beverage products to convenience stores and drugstores in Japan.

In general, Japanese consumers tend to be highly demanding, putting great emphasis on quality and convenience. While especially quality may continue to top the list of important product features for Japanese consumers, a recent trend is for people to pay more attention to price than ever before.²³ Another noteworthy trend is that preferences are progressively shifting towards health oriented, organic and sustainable products, - including Western-style meals. There may be many reasons for these changes (increasing number of single households, ageing population and families in which both parents work etc.), but Japanese consumers have traditionally been curious to try different foods and drinks, resulting in a market that is characterized by a wide selection of products and an abundance of new product launches.

²² Welcia Holdings Co., Ltd. Financial Results Briefing for the Fiscal Year Ended February 2020, <http://www.welcia.co.jp/en/latest/main/08/teaserItems1/0/linkList/09/link/FYE2020%204Qfinancialresults200417en.pdf>

²³ For an overview of Japanese consumer profiles and preferences see: The Food and Beverage Market Entry Handbook Japan: A Practical Guide to the Market in Japan for European Agri-food Product. Published online by the Consumers, Health, Agriculture and Food Executive Agency Promotion of Agricultural Products Unit under the European Commission in 2019, available at: https://ec.europa.eu/chafea/agri/sites/chafea/files/handbook-japan-2019_en_0.pdf

Japanese consumer preferences:

Traditional characteristics:	Quality
	Product packaging
	Storytelling
	Convenience
Increasing attention to:	New products and variations
	Competitive pricing
	Health oriented products
	Sustainability
	Organic products

Source: Own model

In addition to changing consumer preferences, the table below will summarise how the Corona pandemic may potentially present new business opportunities for European SMEs on the Japanese market. As previously discussed, convenience stores and drugstore chains are doing comparatively well under Corona. Under the pandemic, a general trend is for Japanese consumers turn to the conveniently located stores with often wide selections of competitively priced, healthy snacks and drinks on the shelves. Competition among the stores is, however, increasing and the industry is witnessing both a growing number of mergers and focus on differentiation strategies for winning in the increasingly fierce competition. This has implied that almost all convenience and drugstore chains in Japan are looking for ways and products to differentiate themselves in the competition. Differentiation strategies go hand in hand with the aforementioned changes in consumer preferences, which means that stores are increasingly looking for healthy and competitively priced products with strong storytelling.²⁴

Due to the Corona pandemic, all trade fairs and conventional channels for searching and sourcing new products for the stores are fundamentally under constraint, and as travel restrictions also apply, convenience and drugstore buyers will have to find new ways of finding new products to support the all-important differentiation strategy. As case studies later in this report will show,²⁵ convenience and drugstore buyers are opening up for direct contact, dialogue and even direct import from overseas brands, unprecedentedly circumventing some of the traditional intermediaries in the value chain.

²⁴ While consumer preferences may be changing to include health, sustainability and price consciousness etc., the Japanese preference for, quality, packaging and new product development, will unquestionably continue to top the list. Put differently, products will not be able to compete on the Japanese market if quality, packaging and product development is not among the highest in the world.

²⁵ Please see the part 'Rethinking Strategy for Japan' for company case studies.

General trends; and opportunities for EU SMEs under Corona:

<ul style="list-style-type: none"> • Japanese convenience stores and drugstore chains are doing well under Corona.
<ul style="list-style-type: none"> • The chain stores are looking for products to differentiate themselves in the increasingly fierce competition.
<ul style="list-style-type: none"> • Consumer preferences are changing (price consciousness, storytelling, sustainability and health orientation).
<ul style="list-style-type: none"> • Trade fairs and normal channels for the search and sourcing of new product are under constraint, so convenience store and drugstore buyers may be unprecedentedly open for direct contact and discussions.
<ul style="list-style-type: none"> • As travel restrictions apply, Japanese buyers cannot travel abroad to search for new products to draw customers into the stores. Again, this implies that buyers may be increasingly open for direct contact, and perhaps even from overseas brands.
<ul style="list-style-type: none"> • Local Japanese importers and distributors to convenience stores and drugstores suffer from the same market conditions and have similar difficulties in providing convenience stores and drugstores with new products from abroad.
<ul style="list-style-type: none"> • While travel and business restrictions related to the Corona pandemic may prevent Japanese convenience stores and drugstore chains from finding new products in the conventional way through trade fairs, international travel and designated importers and distributors, the current disruption in these patterns may also imply that Japanese convenience stores and drugstores open up to sourcing products more directly from overseas companies, circumventing some of the traditional intermediaries in the value chain.

Source: Own model

The above-mentioned trends and the way in which these may present new business opportunities for European SMEs on the Japanese market is the topic of the next part of this report: Rethinking strategy for Japan. First, however, let us round of this part with a brief overview of import regulations, tariffs, taxes and the impact of the recent Economic Partnership Agreement between EU and Japan.

d. Food and beverage products: Import and market access to Japan

This section provides a brief overview of the requirements for entry of European companies' products into the Japanese food and beverage market, explaining the procedures, documentation and Japanese authorities involved.

i. Import certification

First of all, access to the market for foreign foods and beverages in Japan requires an import permit from the Ministry of Health, Labour and Welfare (MHLW), in accordance with the 1947 Food Sanitation Law.²⁶

The Japan External Trade Organization (JETRO) is a good general source of information regarding the requirements and procedures regarding the import notification, inspection and certification needed for import of food and beverages to Japan.²⁷ For specific information on the documents and import clearance processes pertaining to a particular product, it is recommended that European exporters team up with a local Japanese importer specialized in assisting in with the preparation for import of the company's products to Japan.

Documents required for import certification:

Submitted to	Required documents
Imported food monitoring departments of Quarantine Stations, Ministry of Health, Labour and Welfare (Food sanitation inspection under the Food Sanitation Act)	Notification for importation
	Material and ingredient table
	Production flow chart
	Certificate and table of analysis results issued by a designated inspection institute

Source: Ministry of Health, Labour and Welfare, <http://www.mhlw.go.jp>

As noted in the table above, prior to ship-off for for Japan, exporters must submit an 'Import Notification' form to a Quarantine Station at the intended port of entry. The Import Notification must be completed in either English or Japanese and can be submitted either electronically (MHLW registration required) or in hardcopy. It must be submitted before the products have cleared customs, but no more than seven days prior to their estimated time of arrival. A detailed account of materials and ingredients, along with a production flow chart showing the manufacturing methods used for the product, is required as supporting documentation. Products being imported for the first time require greater details than those with an established import record. Lastly, all food and beverage Import Notifications must be accompanied by a certificate or table of analysis from an accredited laboratory in the exporting country. Independent of MHLW testing, this document is required for customs clearance and market access. Based on the information provided in the Import Notification and the product classification, the MHLW may very likely conduct an

²⁶ Import procedure under the Food Sanitation Law available at: <https://www.mhlw.go.jp/english/topics/importedfoods/1.html>

²⁷ www.jetro.go.jp

inspection during quarantine. For details of the documents and processes required by the Ministry of Health, Labour and Welfare, see the Ministry’s ‘Import Procedure under Food Sanitation Law’.²⁸

Advice regarding new or unknown products in Japan:

In case of shipping new or unknown products to Japan, the MHLW recommends prior contact and delivery of a small sample in order to guarantee the compliance with existing law. The importer may also test the product in one of the accredited foreign laboratories and attach the result. In this case the inspection of the sample at the Japanese port might be waived.

Source: The Food and Beverage Market Entry Handbook Japan: A Practical Guide to the Market in Japan for European Agri-food Product (2019)

ii. Customs clearance

Customs clearance can begin after the product for importation has been deemed admissible and received its Certificate of Import Notification from MHLW. Customs in Japan are administered by a separate agency from the MHLW, namely the Customs and Tariff Bureau of the Ministry of Finance, and are accountable to a different legal framework, namely the Customs Law.²⁹

Documents required for customs clearance:

Submitted to	Required documents
Local customs offices (Customs clearance under the Customs Act)	Declaration of import
	Commercial invoice
	Packing list
	Bill of lading (B/L) or airway bill
	Relevant product licenses and/or certificates

Source: based on Ministry of Finance, <http://www.mof.go.jp>

Compliance with customs procedures can appear difficult and time consuming for companies entering the market for the first time, however, as with the import permit discussed in the previous section, suitable partners can offer assistance during all steps of the import procedure to help you get into the market. As the mini case outlined below will help illustrate, it is very important to comply with all Japanese requirements and standards, as non-compliance –

²⁸ See ‘Import Procedure under Food Sanitation Law’ from the Ministry of Health, Labour and Welfare here: <http://www.mhlw.go.jp/english/topics/importedfoods/1.html>.

²⁹ For details, see: The Food and Beverage Market Entry Handbook Japan: A Practical Guide to the Market in Japan for European Agri-food Product. Published online by the Consumers, Health, Agriculture and Food Executive Agency Promotion of Agricultural Products Unit under the European Commission in 2019, available at: https://ec.europa.eu/chafea/agri/sites/chafea/files/handbook-japan-2019_en_0.pdf

and even unforeseen and unintended non-compliance - may potentially lead to significant delays and perhaps even the permanent rejection of products.

Mini case: unforeseen problems with customs clearance:

In 2018, an EU-based manufacturer of snack products teamed up with a Japanese importer and customs clearance agent to enter the Japanese market. After almost a year of communication and sharing documentation regarding the product, all relevant import permits were finally obtained from the Japanese authorities and the actual import of products could begin. In the course of the following year, five big shipments were successfully exported to Japan. Although all paperwork had been properly prepared, the customs clearance rarely took less than a week after the goods had arrived in Japan. While this continued to baffle the EU-based exporter of the goods, a very serious – and completely unforeseen – problem occurred one day when a shipment had arrived in Japan and was stopped by the customs authorities. The problem was that: The country of origin of the goods was Sweden and this had been duly noted in all paperwork, and on all products and products and boxes, but this time the exporter had been used some old cardboard boxes for wrapping the shipment and on these boxes it said, made in Denmark. The exporter of the goods had failed to understand the potential problem since many other markets simply require a ‘made in the EU’ conformity and apart from that never seem to care how the products, and otherwise correctly branded packing material, are wrapped for shipment. But the Japanese customs inspectors immediately noticed this apparent inconsistency and it sparked a whole range of problems for the exporter. After weeks of documentation, formal apologies and discussions back-and-forth, the products were finally released, but with a strict notice from the customs authorities that the company would lose its import permit if this was to ever happen again.

Source: Mini case based on interviews with the EU exporter, the Japanese importer and local customs clearance agent.

Contacts of competent authorities:

Food Sanitation Act	Inspection and Safety Division, Department of Food Safety, Pharmaceutical and Food Safety Bureau, Ministry of Health, Labour and Welfare	TEL: +81-3-5253-1111 http://www.mhlw.go.jp
Customs Tariff Act	Customs and Tariff bureau, Ministry of Finance Japan	TEL: +81-3-3581-4111 http://www.mof.go.jp
Act for Standardization and Proper Labelling	Labelling and Standards Division, Food Safety and Consumer Affairs Bureau, Ministry of Agriculture, Forestry and Fisheries	TEL: +81-3-3502-8111 http://www.maff.go.jp

Source: Own model

iii. Tariffs, taxes and the Economic Partnership Agreement

In 2018, the European Union and Japan signed an Economic Partnership Agreement (EPA) and in 2019 the agreement entered into force. To support EU SMEs to better understand the regulations and applicable tariffs under the EPA, the EU-Japan Centre for Industrial Cooperation recently launched a designated EPA-helpdesk with downloadable factsheets and webinar recordings that cover a wide range of product categories. The webpage is accessible here: <https://www.eu-japan.eu/epa-helpdesk>

Another source of information on regulations, taxes and the EPA is the European Commission’s Access2Markets database which also help companies navigate their way to the right data for exporting their products. The database can be accessed through this link: <https://trade.ec.europa.eu/access-to-markets/en/content/welcome-access2markets-trade-helpdesk-users>

In 2019, the consumption tax in Japan was raised from 8 percent to 10 percent. Many categories of food will, however, be exempt. Please consult The Japan External Trade Organization (JETRO) for information about consumption tax and other taxes in Japan: www.jetro.go.jp

2. Rethinking strategy for Japan

For decades, Japan has ranked as a market of unusual complexity. As discussed, the distribution system permanently baffles; choosing market intermediaries is an art in itself, while securing a business foothold and market presence entails massive costs. Prescriptions for how to do business in many Japanese sectors are largely the same that dominated Western thinking in three decades ago, as if Japan has not moved on. Many companies that apply the conventional thinking have floundered.³⁰

Based on interviews and case studies of two European snack and beverage brands entering the Japanese market,³¹ a clear picture emerges that the conventional ‘push strategy’ does not work well in the market. Push strategy will be explained and exemplified in the following section.

After (a) discussing push strategy and evaluating which other options European SMEs have to re-position themselves on the market, we will (b) suggest and introduce a novel approach to market entry: pull strategy.

a. Traditional ways of market entry: Push strategy

Traditionally, market entry to Japan has been a question of choosing ‘the right partner’,— often an importer or wholesaler of food and drinks. A push strategy implies that the Japanese partner assigned by the foreign brand will ‘push’ the company’s products through all the market intermediaries needed to reach the end-customers in Japan.

Typical push strategy:



Source: Own model

Managers of both case companies mention that their international sales activities basically started with participation in trade fairs and Government supported export promotion programmes. Despite differences between the two brands (short versus long company history, new and innovative healthy snack product versus old and traditional tea brand, very low capital for market investment versus money set aside for market development), the experience with trade fairs and export promotion programmes remains more or less the same for both companies: Their products had been favourably looked upon by potential Japanese buyers and these can be grouped into two main categories:

³⁰ For details and examples see M. Glisby & N. Holden (2005).

³¹ Case material pertains to the period 2018 - 2020. For reasons of confidentiality, we cannot disclose any company or brand names. In each case, however, we will describe the company’s profile, product and price range, enabling the reader to better understand the context of the case study.

- A. Department stores and distributors.
- B. Individually owned select shops, and retail chains.

Before we explain what the contact from these potential buyers meant for our two case companies, let us briefly introduce the two common categories of potential buyers and sales channels:

Ad A: Department stores and distributors:

Exporting companies are often very excited to receive contact from one or more of the large Japanese department stores during a trade fair. According to the Ministry of Economy, Trade and Industry,³² the total number of department stores in Japan 2019 is 201, down almost 9 percent from the year before. The stores are spread throughout Japan, but almost 50 percent of total department store sales in Japan takes place in three major cities: Tokyo, Osaka and Nagoya. The table below lists the top 50 department stores in Japan, including location and sales.

Top 50 department stores in Japan (2016):

	Place	Name of Store	Group or Company name	Sales (JPY 100 mio)	Vs last year %
1	Tokyo	Isetan Shinjuku	Mitsukoshi Isetan G.	2.685	-1,4
2	Osaka	Hankyu Umeda	Hankyu Hansin G.	2.205	1,0
3	Tokyo	Seibu Ikebukuro	Sogo Seibu G.	1.865	-1,8
4	Tokyo	Mitsukoshi Nihonbashi	Mitsukoshi Isetan G.	1.651	-1,9
5	Tokyo	Nihonbashi Takashimaya	Takashimaya G.	1.329	-2,7
6	Osaka	Nanba Takashimaya	Takashimaya G.	1.299	1,8
7	Kanagawa	Yokohama Takashimaya	Takashimaya G.	1.294	-2,0
8	Aichi	JR Nagoya Takashimaya	JR Tokai Takashimaya	1.286	-1,1
9	Aichi	Nagoya Matsuzakaya	J Front G.	1.206	-3,3
10	Kanagawa	Sogo Yokohama	Sogo Seibu G.	1.096	-4,0
11	Osaka	Abeno Kintetsu	Kintetsu D.S.	1.023	-0,3
12	Tokyo	Ikebukuro Tobu	Tobu D.S.	987	-3,1
13	Tokyo	Shibuya Tokyu Honten	Tokyu D.S.	918	-0,1
14	Tokyo	Shinjuku Odakyu	Odakyu D.S.	914	-3,7
15	Kyoto	Kyoto Takashimaya	Takashimaya G.	848	-1,3
16	Hyogo	Kobe Daimaru	J Front G.	824	-3,1
17	Tokyo	Ginza Mitsukoshi	Mitsukoshi Isetan G.	810	-5,0
18	Tokyo	Shinjuku Keio	Keio D.S.	770	-2,2
19	Kyoto	JR Kyoto Isetan	JR Nishinohon Isetan	752	-6,2
20	Tokyo	Daimaru Tokyo	J Front G.	748	2,2
21	Osaka	Shinsaibashi Daimaru	J Front G.	739	-18,8

³² *Shōgyō dōtai tōkei*. Ministry of Economy, Trade and Industry Japan (2020).

22	Aichi	Nagoya Mitsukoshi	Nagoya Mitsukoshi D.S.	737	-6,8
23	Fukuoka	Iwataya Honten	Iwataya Mitsukoshi D.S.	735	-0,6
24	Tokyo	Shinjuku Takashimaya	Takashimaya G.	708	0,6
25	Tokyo	Matsuya Ginza	Matsuya D.S.	705	-7,7
26	Kyoto	Kyoto Daimaru	J Front G.	673	-3,8
27	Osaka	Daimaru Umeda	J Front G.	637	-2,3
28	Hokkaido	Sapporo Daimaru	J Front G.	622	-0,7
29	Chiba	Sogo Chiba	Sogo Seibu G.	614	-9,7
30	Oita	Tokiwa Honten	Tokiwa D.S.	605	-1,7
31	Kumamoto	Kumamoto Tsuruya	Tsuruya D.S.	571	-0,7
32	Osaka	Hanshin Umeda	Hankyu Hansin G.	558	-5,2
33	Fukuoka	Hakata Daimaru	Hakata Daimaru D.S.	539	-5,0
34	Hiroshima	Fukuya Honten	Fukuya D.S.	512	-0,5
35	Osaka	Moriguchi Keihan	Keihan D.S.	494	-3,0
36	Okayama	Okayama Tenmaya	Tenmaya D.S.	456	-2,1
37	Aichi	Meitetsu Honten	Meitetsu D.S.	455	-1,4
38	Fukuoka	Izutsuya Honten	Izutsuya D.S.	455	-0,3
39	Hyogo	Kobe Sogo	Sogo Seibu G.	451	-3,3
40	Fukuoka	Hakata Hankyu	Hankyu Hansin G.	444	1,4
41	Kagoshima	Kagoshima Yamagataya	Yamagataya D.S.	432	-3,1
42	Tokyo	Tamagawa Takashimaya	Takashimaya G.	430	0,4
43	Miyagi	Sendai Fujisaki	Fujisaki D.S.	425	-1,5
44	Tokyo	Seibu Shibuya	Sogo Seibu G.	417	-1,4
45	Hiroshima	Sogo Hiroshima	Sogo Seibu G.	414	-3,9
46	Tokyo	Ueno Matsuzakaya	J Front G.	408	-1,7
47	Saitama	Isetan Urawa	Mitsukoshi Isetan G.	403	-3,7
48	Kanagawa	Keikyu Department Store	Keikyu D.S.	387	1,0
49	Chiba	Funabashi Tobu	Tobu D.S.	386	-3,7
50	Hokkaido	Maruimai Sapporo Honten	Sapporo Marui Mitsukoshi D.S.	370	-0,4

Source: Own model based on industry organisations and corporate websites

For the last couple of years total department store sales in Japan has been dropping about 5 percent per year and amounted to JPY 6,042 billion (EUR 49 billion) in 2019.³³ The total sales of drugstores in Japan ended up outnumbering total department store sales in 2019, and combined with convenience store sales of totally JPY 12,184 billion (EUR 99 billion) in 2019, drugstore and convenience store sales combined was almost three times higher than total department store sales in Japan in 2019.

³³ *Shōgyō dōtai tōkei*. Ministry of Economy, Trade and Industry Japan (2020).

In department stores, food and beverage products account for 29 percent,³⁴ and while the image of selling to Japanese department stores may be appealing to European exporters of food and beverage products it is worth noticing that department stores in Japan have generally been struggling for years (well before the start of the Corona pandemic). Apart from the unfavourable conditions which most Japanese department stores are currently in, it is of even greater importance to note the perplexingly complicated road to actually selling your products in a Japanese department store.

To sell products in a Japanese department store, you need to build trust with the department store first and then subsequently establish a *kōza*,³⁵ which may take a very long time – if possible at all. So, what is often the case is that exporters need to team up with a local partner (in the shape of an importer, distributor or wholesaler) who will then use the company's existing relations and *kōza* with the department store chain in question. This is also what happened in our case study of the European tea brand on the Japanese market. At the trade fairs, the company successfully collected business cards from a number Japanese department stores, but after many failed attempts at creating a dialogue and direct business relations, department store buyers would inform the company that they can only deal with a local Japanese partner of their choice. One of the department store representatives directed the company to a Japanese distributor who would then take care of the import, stockkeeping and distribution to the department store. While the European exporter was excited about the business potential, the sales never really took off.

Teaming up with a Japanese distributor is the market entry option chosen by many European SMEs. The resulting examples and experiences of European brands working with Japanese distributors, are, however, that (1) the annual sales to the distributor begin to stagnate very quickly and rarely exceed JPY 20 million yen (148,007 Euro) per year. Also, (2) the companies interviewed speak of low profitability and difficulties in communicating the brand value and brand image through their distributors.³⁶

Over the years, the European tea company changed its Japanese distributor a couple of times, but the results were more or less the same: The annual sales to the distributor begin to stagnate very quickly and rarely exceed JPY 20 million yen (148,007 Euro) per year. As the company started to ask fellow exporters for their experiences with distributors, the stories were almost the same.³⁷ While there may be many reasons for the lack of success, the common story when interviewing company executives across a wide range of companies remains that:

1. *Branding and storytelling is diluted:* When dealing through the distributors, companies are left with a huge challenge of *pushing* the products – and ultimately the brand – through all the intermediaries in the market. Needless to say, communication of the brand profile and stories quite often get diluted along the way.
2. *Profitability is too low for all parties involved:* Including too many market intermediaries in the process inevitably means lower profitability, which essentially makes it less motivating for all parties involved (from the European exporter to the distributor and its designated wholesale and retail partners in the value chain).

³⁴ Ibid.

³⁵ A *kōza* is an account (with e.g. a department store). Far more than a simple bank account is, however, implied with the notion of *kōza* (trust, relationship, time etc.). It is hard, if not impossible, for foreign companies to establish a *kōza* with a Japanese department store – let alone open a simple bank account in Japan.

³⁶ Based on interviews with European food and beverage companies during 2010-2020.

³⁷ European SME exporters of chocolates and beverage products.

To literally push the European company's products through all the intermediaries on the market, the distributor often demands a purchasing price (Ex Works) equivalent to 20 percent of the retail price excluding sales tax in the home country of the brand.³⁸

3. *Retail prices become too high:* Having to include too many intermediaries on the way to the end consumer will inevitably also mean that shop prices become higher in Japan than in the host country. This is very much contrary to the current consumer trend of price consciousness.³⁹ In our case with the tea brand, the company could simply not meet the requirements regarding purchasing price, so what happened instead was a doubling of the retail price for the company's products in Japan.
4. *Information and business development opportunities become limited.* The distributor will for historical and cultural reasons typically use and favour existing partners and market channels. They will often ask for development of customized products for partners in their existing network, and focus less on developing new business opportunities in the market.

We all know that knowledge, network and personal relations are exceedingly important in Japan. So why is it that so many companies rush to surrender exclusive distribution rights to a partner in Japan? Put differently, why do so many companies 'outsource' the all-important relationship building, brand communication, knowledge sharing and so forth to an external partner? Obviously, most European SMEs cannot invest time and money in establishing and operating their own company in Japan, so the challenge is how to secure a strong market presence without incurring exceptionally high costs. This is made possible through a pull strategy. Before discussing pull strategy and how this became a significant game changer for the European tea brand in Japan, let us briefly discuss the other category of buyers who the case companies would meet at the trade fairs: individually owned select shops and retail chains.

Ad B: Individually owned select shops and retail chains

For our other case company, the newly established European exporter of healthy snack bars, Japanese market entry basically started with small orders from Japanese select shops during trade shows in Europe. A select shop is typically an individually owned and operated retail shop with a product assortment ranging from clothing and shoes to handbags, perfumes, accessories and sometimes a limited assortment of snacks and beverages.

Select shop owners are often active buyers at international trade fairs in Europe. They typically buy (with no right to return or exchange products) directly from overseas companies and thereby skip the costly intermediaries in the shape of importers, distributors, wholesalers and the like. So, the resulting profitability for all parties involved is comparatively high. A select shop typically buys directly from the manufacturer at 40 – 55 percent of the retail price excluding sales tax. While this may to some extent seem attractive, multiple experiences from European SMEs show that starting business directly with Japanese select shops typically results in: (1) on-off orders with only very few (if

³⁸ Despite a strong brand and the title of Purveyor to the Royal Court, the company realised that (1) prices were simply too high compared to competing products from well-known competing brands, and (2) the brand story could not be properly communicated through all the market intermediaries. Especially the latter was a great frustration to the company owners.

³⁹ See section 1.c. 'Opportunities under Corona' for a discussion of changing consumer preferences.

any) reorders, and (2) the so-called 80-20 principle, which states that roughly 80 percent of the sales will come from 20 percent of the customers. While the image of select shops in Japan is generally good and provides a good 'window' for new brands to be spotted by Japanese consumers and press, there is currently no record of European snack or beverage brands that have truly gained a foothold in the Japanese market through only selling directly to select shops.

Another - more interesting - category of select shops exist: The retail chains. Essentially, the retail chains carry more or less in the same product categories as the individually owned select shops. The main difference, however, is (1) the size of the chains, and (2) a centralized purchasing function. These two characteristics will theoretically ensure the expandability of your business in Japan, but in reality, this rarely happens. Let us explain.

Many European brands are often approached by Japanese chain stores such as Actus, Tomorrowland, Beams, United Arrows, Ships, And A, Via Bus Stop and especially during trade fairs. When they realise that these chains have anything between 20 and up to 150 directly managed stores in their network, the business potential seems interesting. But as all cases (so far) have shown, the chain store will typically place an order for only a carefully selected and very limited range of items. While this may not be enough to duly represent the brand and the brand universe, it corresponds well with the (often not so explicit) target of the retail chain: namely, to introduce new and interesting products and concepts from abroad which can help reel in customers, to whom the retail chains ideally want to sell original items under the chain store's own brand label. Private label products, from which the retail chains clearly (and understandably) generate their profit, often represent between 60 – 80 percent of the total sales in retail chains.

The common story from the managers of our case studies and interviews is that the direct business with the select shops (individually owned or chain store based) never really developed according to their expectations. The reasons may be that:

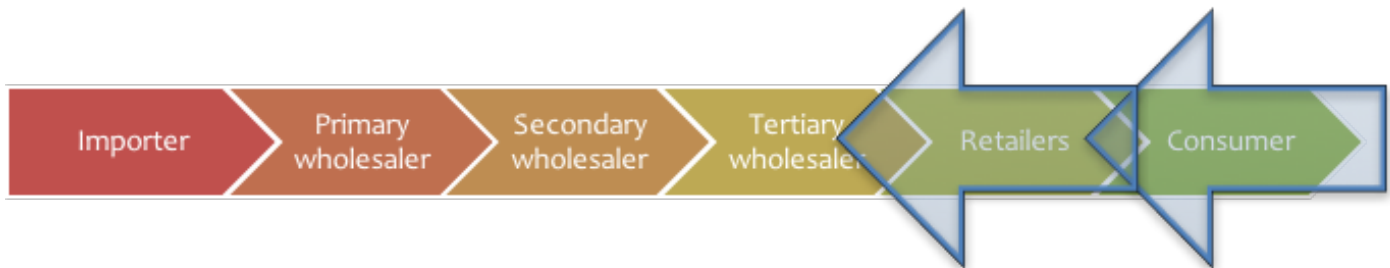
1. *No re-orders from chain stores.* Contrary to the expectations of the European managers, products were not re-ordered and only used for promotional activities during one or two seasons in a selected number of stores. In other words, new brands and products are primarily used to attract customers to visit the stores, and ultimately buy products manufactured and owned by retail chain itself.
2. *Difficult to manage:* For a European company to provide customer service and after-care (by Japanese standards, that is) to a network of individually operated select shops can be a daunting task.

So, after a very short time, the European snack brand was also back at square one on the Japanese market. Having been 'spotted' and selected by one of the top retail chains can, however, lead to new business opportunities. Many of the importers, distributors and wholesalers keep an open eye on what is being launched in the top select shops, and often approach the brands afterwards to secure the exclusive distribution rights in Japan.

b. Pull strategy

A pull strategy takes a point of departure in creating demand directly with Japanese consumers. With the growing importance of social media and marketing via influencers in Japan, it is becoming much easier for European brands to communicate directly with end customers in Japan.

Pull strategy:



Own model

As shown with the model above, the point of departure for a pull strategy is the end consumer. In other words, the starting point is to create a source (or multiple sources) through which the brand can communicate directly with end consumers. Having created brand awareness and demand directly among Japanese consumers, the next steps of finding the right retailers and perhaps later a wholesaler or importer becomes a significantly easier task.

Let us revert to the case study of the European snack brand to show the effects of a pull strategy. While the company has a wide and extensive product range, the first step in creating a pull strategy was for the company to decide on a spearhead product for Japan. The company decided on a healthy snack bar available in six variations. As opposed to creating awareness and brand recognition based on the – often very generic – profile and characteristics of an overall brand (e.g. high quality, design etc.) it proved to be much easier for the company to create awareness and recognition based on a single product. Below is a short summary of how the European snack brand started out, and the challenges it encountered with its push strategy for the Japanese market.

The company contacted two model agencies and a wide range of influencers with profiles suitable for promoting the healthy snack bar, – and later the overall brand name. Also, through the use of network and relations of a well-connected local partner in Japan, the company also succeeded in placing the snack bar in various physical settings spanning industry borders (from fitness centres to interior shops). The pull effect had started, and soon this generated a number of inquiries regarding the snack bar *directly* from Japanese drugstores and convenience stores.

Both drugstores and convenience stores were interested in buying the products directly from the European company, in effect circumventing all the traditional importers, distributors and wholesalers on the way to reaching the end consumers in Japan. This was a dream scenario for the European exporter, but even more so because the convenience store and drugstore chains in Japan had a centralized purchasing function and would be handling the stockkeeping and physical distribution in Japan themselves. There would be no need to involve the traditional market intermediaries in order to reach the shelves of both convenience stores and drugstores in Japan. While that was really good news for

the European exporter, the company soon realised the massive amount of preparations and homework needed in order to deal directly with the convenience and drugstore chains in Japan. Here is a summary of the process the European company went through after having successfully established direct contact with the Japanese chain stores:

1. Product modifications for the convenience and drugstore market:

The company quickly realised that the product itself would have to be modified to fit the current line-up of similar products in the stores. This was important. The company's product was a 55 gram healthy snack bar which was selling reasonably well in most other markets, but selling in Japanese convenience stores and drugstores the product would have to be downsized to exactly 40 grams which was apparently the bestselling size of snack bars on the Japanese market. One of the smaller convenience store chains, Natural Lawson,⁴⁰ showed interest in launching the snack bar as it was in its original size, but expectations (and commitment) was too low for the European company to follow that strategy. Instead, the company chose to modify the size of its product to hit mass market in the large chain stores.

2. Packaging

It was not only the product that needed modification. A marketing company was brought in to evaluate what kind of changes to the packaging that the company could make to increase the awareness and potential sales in Japan. After much dialogue and a keen focus on not changing the overall brand image too much, the company finally accepted an amended product design for Japan, which would then undergo translation into Japanese and check for compliance with various authorities for correct labelling, etc.

3. Import certification

Only after having produced the final product for Japan in its new size and with the new packaging, the process with application for import certification could begin. The company soon realised that professional help was needed, so they teamed up with an industry professional who would manage the process with the Japanese authorities on behalf of the European company. The process ended up lasting almost 18 months from the initial contact from Japanese customers to having the final product and import certification in place. Needless to say, this was a very long process, especially since neither convenience stores or any of the drugstore chains had yet committed to any concrete orders – or even as much as offered a sales forecast.

4. Price and profit structure

Hitting the right retail price point with the product was extremely important for both the convenience stores and drugstore chains. Downsizing the product with 15 gram in Japan of course helped the European company with some leverage to hit a lower price point than on the company's other markets. In Japan, the retail price including 10 percent sales tax could be maximum JPY 297 (EUR 2.41). So, the retail price excluding sales tax

⁴⁰ The convenience store chain Lawson operates totally 14,805 stores in Japan. The company also operates a sub-branded chain of convenience stores under the name of Natural Lawson which may be of special interest for European snack and beverage brands. As of August 2020, the number of Natural Lawson shops in Japan is 146. The shops are located in business districts of large Japanese cities to cater to especially working women. Natural Lawson shops focus on carefully selected healthy, low-calorie foods, snacks and drinks made from select ingredients, and environmentally friendly detergents and cosmetics.

would amount to JPY 270 (EUR 2.19) and based on this price, the chain stores would typically offer to pay between JPY 135 - 140 (EUR 1.10 - 1.13) for the product. So, as a general rule of thumb, the drugstore and convenience store chains would expect to pay around 50 to 52 percent of the retail price excluding sales tax for the product.

5. Business setup

While the chain stores had agreed to do business directly with the European company, one of their requirements to really commit to the brand was the establishment of a local legal entity in Japan, which the convenience stores and drugstore chains would then be dealing with. Direct import from Europe was also an option, but only for the import of the existing product (the too-large 55 gram snack bar, and then with a white label on the back to show that this was a special import product). The latter would clearly limit the sales, so the European company was quick to involve a European-based advisor with pre-established relations with convenience stores in Japan - and the Japanese businessman who had originally helped the company kickstart the pull strategy with influencers and model agencies. Together they formed a joint venture in Japan to handle the everyday business, operations and relationship building with the convenience store and drugstore chains in Japan.

The orders started ticking in, and the forecast for 2021 is for almost 1 million snack bars with a retail value of nearly JPY 300 million (EUR 2.34 million). While this is a fantastic achievement considering the short company history and relatively insignificant sales on all other markets, two very important points remain:

First, as the above-mentioned discussion shows, a company interested in business with the Japanese convenience and drugstore chains will have to be extraordinarily patient, zealous and diligent throughout the long preparation processes. One really has to be attentive to details and should not expect any short-term gains in the process. Starting up business with a convenience or drugstore chain in Japan is – in all respects – to be considered a long-term project.

The second important point to notice is that one should not scale down the commitment or focus in any way just because they have succeeded with the above-mentioned processes and now started selling in Japan. One may be tempted to start looking at including other markets and pass the responsibility for operations and relationship building with Japanese clients to junior staff. We would strongly advise against that. As one of the convenience store executives told us during an interview for the case study, the real test is whether the company keeps focus on getting everything right and keeps on building the relationship. The executive had often experienced that foreign businesspeople would soon begin to scale down the number of visits to Japan once sales had begun to materialise. This truly baffled the executive. As he said, “you have to keep building the relationship. It’s just like breathing. You can’t just stop or slow down!”.⁴¹

Let us round off the discussion of pull strategy with an epilogue to our second case study: the European tea brand. As discussed in the previous part on push strategy, over the years the company had been partnering with a number of

⁴¹ For a thorough discussion of relationship building and the importance of tacit knowledge in Japan, see: Holden, N.J. and Glisby, M. (2010): *Creating Knowledge Advantage: The Tacit Dimensions of International Competition and Cooperation*. CBS Press. Copenhagen.

different distributors on the Japanese market, but with limited success in every case. The company needed to fundamentally rethink strategy for the Japanese market; they needed a strategy that would deal with the difficulties that the company had experienced so far in Japan: low profitability, too high retail prices, passive (if any) business development, and dilution of branding and storytelling through involvement of too many market intermediaries.

The company deliberately wanted to create a pull strategy – one that would keep the company in control of business development, pricing, profitability, branding and storytelling. Drawing on vast experiences with business in Japan, the top executives of the company clearly understood the importance of network and careful preparation prior to contacting (or even better: being contacted by) the desired retail partners: in this case, the Japanese convenience stores and drugstore chains. Specifically, what the company did to create interest and direct inquiries from the convenience and drugstore chains was this:

Case study: three steps to start creating a pull effect:

Step 1: Secure the product/market fit upfront

To be able to upfront communicate the ‘right’ product to convenience and drugstore chains from the very beginning, company representatives went to Japan to simply examine the price points, product sizes and packaging formats, enabling the company to create and present the ‘right’ product from the start.

Step 2: Define the spearhead product

While the company had wide and extensive range of teas, packaging formats and designs, one of the first steps in creating the pull strategy was for the company limit the range to only one spearhead product for Japan. As opposed to creating awareness and brand recognition based on the (often very generic) profile and characteristics of an overall brand it proved to be much easier for the company to create awareness and recognition based on a single product. The product chosen was then to be offered in ten different variations.

Step 3: Create the pull effect

Having successfully re-designed and re-packaged a spearhead product for Japan, the company engaged with advisors to identify a handful of targeted influencers who would essentially help make the product visible for key stakeholders and buyers from the convenience and drugstore chains. To further strengthen the pull effect, the company also reached out to a number of carefully chosen select shops and offered them to carry the brand. As expected, selling to a number of select shops did not create a very big revenue, but on the other hand it was instrumental in creating awareness for the product in Japan as reporters and influencers in general keep an open eye on what is being launched in the top select shops.

Source: Own model

As both case studies clearly show, a pull strategy where the company starts out communicating directly with end consumers in the market can be a very effective way for European SMEs to enter the Japanese market.

The merits of a pull strategy:

<ul style="list-style-type: none">• First of all, the fixed costs remain very low, whilst most of the costs (kick back fees for influencers, shipping costs etc.) are fundamentally variable costs, in the sense that they only occur once a product sale is made.
<ul style="list-style-type: none">• Second, the company will get valuable information and knowledge from the direct interaction with end consumers which can later be used in marketing and product development.
<ul style="list-style-type: none">• Third, the company – very importantly – does not get sucked into the complexities of working with a wholesaler to push products through the long chain of intermediaries. Rather, with a pull strategy, the company retains the flexibility to freely navigate and pursue the best opportunities that may arise from the promotional activities among end consumers.
<ul style="list-style-type: none">• Fourth, the company is in full control (or at least in as much control as possible) to handle and influence the communication of the brand, and the successive brand building activities in Japan.
<ul style="list-style-type: none">• Fifth, the retail price level will be strategically set to secure the highest possible revenue (as opposed to a retail price level which automatically becomes too high if profitability for all the traditional market intermediaries (importers, wholesalers, distributors etc.) has to be included.
<ul style="list-style-type: none">• Sixth, the company will enjoy higher profitability (when selling at 50-52 percent directly to convenience and drugstore chains with their own centralized purchasing function and distribution in Japan - as opposed to selling to a distributor at 15-25 percent of the retail price excluding tax.

Source: Own model

Conclusions, advice and recommendations

The purpose of this report has been (a) to present an overview of trends and opportunities on the Japanese convenience store and drugstore market under the Corona pandemic and (b) to deliver strategic insight, tactical guidance and real-life examples of how to succeed in the Japanese convenience store and drugstore market.

Despite almost three decades of recession, Japan remains the third largest economy in the world. Close to 126 million sophisticated consumers with high purchasing power and discerning tastes make Japan the third largest consumer market in the world. No other country in the world is as concentrated a source of revenue for so many brands as Japan. Despite the sheer size of the total Japanese market, there are many other reasons for European snack and beverage brands to consider market entry to Japan – especially right now under the Corona pandemic:

- Japan has close to 60,000 convenience stores and well over 20,000 drugstores which are basically thriving right now as shoppers are reluctant to go far to buy daily necessities during the Corona pandemic.
- The total retail industry market in Japan exceeds JPY 145,000 billion (EUR 1,175 billion), and in combination, convenience stores and drugstore sales amount to a staggering JPY 19,019 billion (EUR 154 billion) and jointly represents more than 13 percent of the total Japanese retail market.
- The processed food and beverage category accounts for more than 30 percent of the total sales in Japanese convenience stores and drugstores and the share is increasing further under the Corona pandemic.
- Competition for customers has intensified among convenience stores and drugstores and especially in the snack and beverage product category, major Japanese chain stores are using for example imported European products to diversify themselves in the competition.
- Despite a drop of nearly 10 percent in the number of store visitors during the first months of the Corona pandemic, the largest convenience store operator in Japan, Seven-Eleven, still boasts 25 million store visits *every day* to its more than 21,000 shops in Japan.

This report has been targeted two main groups: (1) European SMEs selling snack and beverage products with an interest in entering the Japanese convenience store and drugstore market, and (2) companies with an existing setup on the Japanese market but sending the need to rethink strategy: for example, by revitalising the company's sales and marketing activities in the Japanese market.

Part 1: Overview of the Japanese convenience store and drugstore market

Part 1 of this report provided an overview of Japanese convenience store and drugstore market.

Convenience store sales make up 8.4 percent of total retail sales in Japan. In sales value, this represents total convenience store sales in 2019 of JPY 12,184 billion (EUR 99 billion). Drugstore sales represent 4.7 percent of the total Japanese retail market in 2019 and accordingly accounts for total sales of JPY 6,835 billion (EUR 55 billion). Together, convenience store sales and drugstore sales amount to JPY 19,019 billion (EUR 154 billion) and represent more than 13 percent of the total Japanese retail market. While the revenue of supermarkets, department stores most other physical stores have been suffering under the Corona pandemic, convenience stores and drugstore chains, however, seem less affected and sales of have been quick to recover and reach somewhat normal pre-Corona levels.

According to The Japan Franchise Association, there is a total of 55,852 convenience stores in Japan. Together, the three largest convenience store chains in Japan, Seven-Eleven (21,005 shops in Japan), FamilyMart (16,430 shops in Japan) and Lawson (14,805 shops in Japan), jointly represent close to a 92 percent share of the total convenience store sales in Japan.

According to the Ministry of Economy, Trade and Industry, there are currently more than 20,000 drugstores in Japan and the number continues to rise. Drugstore sales in Japan have been growing for the past twenty years, and in 2019 total drugstore sales amounted to JPY 6,835 billion (EUR 55 billion). The growth rate has been moving in the 5-7% range since 2016, closing the gap with the convenience store market and supermarkets in Japan. The leading drugstore chain (by revenue) in Japan is Welcia with 2,005 stores in Japan. The fourth largest chain store (by revenue), Cosmos has 1,092 stores and is the drugstore chain with the highest percentage of food and beverage sales in Japan. In October 2021, the two drugstore chains, Matsumoto Kiyoshi and Cocokara Fine, will merge and the two companies will jointly become the biggest player in the Japanese drugstore market with combined sales of more than JPY 1 trillion (EUR 8.22 billion) and nearly 3,000 stores all across Japan.

Main differences between convenience stores and drugstore chains in Japan:

	Convenience stores	Drugstores
Number of stores	60,000+	20,000+
Total sales 2019 (billion JPY)	12,184	6,835
Food and beverage share of sales	33%	32%
Image	‘Close and convenient’	‘Cheap and convenient’
Competition strategy	Differentiation	Low price
Chain store operators	Very few: Three largest chains account for 92% of the market	Relatively many: Seven largest chains account for 34% of the market

Section 1.C. of this report provided an overview of the current trends and opportunities on the Japanese market for European exporters of snack and beverage products.

In general, Japanese consumers tend to be highly demanding, putting great emphasis on quality and convenience. While especially quality may continue to top the list of important product features for Japanese consumers, a recent trend is for people to pay more attention to price than ever before. Another noteworthy trend is that preferences are progressively shifting towards health oriented, organic and sustainable products. In addition to changing consumer

preferences, the table below summarises how the Corona pandemic may potentially present new business opportunities for European SMEs on the Japanese market.

General trends; and opportunities for EU SMEs under Corona:

- Japanese convenience stores and drugstore chains are doing well under Corona.
- The chain stores are looking for products to differentiate themselves in the increasingly fierce competition.
- Consumer preferences are changing (price consciousness, storytelling, sustainability and health orientation).
- Trade fairs and normal channels for the search and sourcing of new product are under constraint, so convenience store and drugstore buyers may be unprecedentedly open for direct contact and discussions.
- As travel restrictions apply, Japanese buyers cannot travel abroad to search for new products to draw customers into the stores. Again, this implies that buyers are increasingly open for direct contact, and perhaps even from overseas brands.
- Local Japanese importers and distributors to convenience stores and drugstores suffer from the same market conditions and have similar difficulties in providing convenience stores and drugstores with new products from abroad.
- While travel and business restrictions related to the Corona pandemic may prevent Japanese convenience stores and drugstore chains from finding new products in the conventional way through trade fairs, international travel and designated importers and distributors, the current disruption in these patterns may also imply that Japanese convenience stores and drugstores open up to sourcing products more directly from overseas companies, circumventing some of the traditional intermediaries in the value chain.

Part 2: Rethinking strategy for Japan

Part 2 of this report provided a detailed discussion of two different strategies for competing on the Japanese market: push strategy and pull strategy.

Based on case studies of two European brands entering the Japanese market, a clear picture emerged that the conventional 'push strategy' does not work well in the market. A push strategy implies that the foreign brand assigns a Japanese partner (typically an importer, distributor or wholesaler) who will then 'push' the company's products through all the market intermediaries needed to reach the end-customers in Japan. With a push strategy, the communication of the brand profile and stories quite often get diluted along the way, whilst including too many market intermediaries in the process inevitably means lower profitability - and higher shop prices too.

A pull strategy takes a different point of departure: namely, in creating demand directly with Japanese consumers. With the growing importance of social media and marketing via influencers in Japan, it is becoming much easier for European brands to communicate directly with end customers in Japan. In part 2 we discussed two company cases to

introduce pull strategy as a very effective way for European SMEs to enter the Japanese snack and beverage market. The advantages of a pull strategy are that:

- The fixed costs remain very low, whilst most of the costs (kick back fees for influencers, shipping costs etc.) are fundamentally variable costs, in the sense that they only occur once a product sale is made.
- The company will get valuable information and knowledge from the direct interaction with end consumers which can later be used in marketing and product development.
- The company – very importantly – does not get sucked into the complexities of working with a wholesaler to push products through the long chain of intermediaries. Rather, with a pull strategy, the company retains the flexibility to freely navigate and pursue the best opportunities that may arise from the promotional activities among end consumers.
- The company is in full control (or at least in as much control as possible) to handle and influence the communication of the brand, and the successive brand building activities in Japan.
- The retail price level will be strategically set to secure the highest possible revenue (as opposed to a too high retail price level which automatically becomes too high if profitability for all the traditional market intermediaries (importers, wholesalers, distributors etc.) has to be included.
- The company will enjoy higher profitability (when selling at 50-52 percent directly to convenience and drugstore chains with their own centralized purchasing function and distribution in Japan - as opposed to selling to a distributor at 15-25 percent of the retail price excluding tax.

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