JAPANESE CONVENIENCE STORES AND E-RETSUS

An Alternative Approach to Capturing an E-Commerce Advantage

Prepared By

William V. Rapp¹ and Mazhar ul Islam²

¹ The New Jersey Institute of Technology
   School of Management
   Newark, NJ 07102, USA
   973-596-6414 (Fax: 3704)
   E-mail: rappw@adm.njit.edu

² International University in Germany
   School of Business Administration
   Bruchsal, D-76646, Germany

June 2002
ABSTRACT

Japanese Convenience Stores and E-Commerce

This paper analyzes how Japanese Convenience Stores (CVS) are organizing themselves to exploit the promise of e-commerce. The three biggest CVS, Seven Eleven Japan (SEJ), Lawson and FamilyMart (FM) over the last year or two have positioned themselves to take advantage of Japanese consumers interest in e-commerce but reluctance to make credit card payments over the Internet or via telecommunications. In this approach they have exploited and leveraged their heavy investment in IT infrastructures, a natural evolution in their third party payment business, and their fundamental business model based on increasing store traffic. At the same time they have shown the way towards a different e-commerce B2C business model than those typical in the US. The basic approach incorporates a heavy dependence on IT-based alliances or “e-retsus”, a range of services and products, and the use of smart cell phones rather than PCs. This alternative business model may therefore offer an interesting alternative to the US paradigm in markets or market segments that possess similar characteristics.
Introduction

The retail business worldwide entered a new era when Jeffrey Bezos, a Wall Street analyst and Princeton graduate, opened a website to sell books on July 16, 1995. Naming this online store after the mighty Amazon River, he initiated the first serious pioneering effort to sell products directly to consumers using the Internet. This e-commerce business model is often referred to as Business to Consumer or “B2C”.

It is in fact an electronic emulation of catalogue retailing, where consumers order standard products from producers or retailers. An Internet website substitutes for the traditional paper catalogue. Because there was an existing US retail catalogue segment that was well developed, substituting the Internet for the paper catalogue was readily understood by consumers. The perceived advantages to the consumer of B2C included the convenience of twenty-four hour shopping without having to make a phone call and real-time availability to freely browse information related to promotional sale prices or out-of-stock items.

A number of start-ups followed Amazon, offering a range of products and services online. Companies like e-Toys, Pet.com, JourneyEd.com, Priceline.com and E-Bay.com emerged, some with viable business models, but many organized primarily to respond to the rapidly inflated demand for Internet-related IPOs that encouraged Internet entrepreneurs to raise hundreds of millions of dollars. Yet, most of these B2C online sellers (e-tailers) could not break-even for several reasons. Many used their cash hoards to attract customers by offering products at steep discounts to get buyers to change their traditional purchasing habits and thus to compete effectively with traditional retailers. In several cases they had to compensate consumers for the additional expense of shipping. Moreover, they spent large amounts on advertising to develop brand recognition and make consumers aware of their websites.

These factors along with the substantial initial investment required for computer hardware and systems development generally created a negative cash flow or “burn-rate” that their business operations could not justify, so they quickly used the billions of dollars they raised from venture capitalists and investors in their IPOs. Indeed, it was because venture capitalists (VCs) and investment bankers were very optimistic about these new business models that enormous amounts of money were invested into many e-commerce start-ups. Investment banks then took them to the capital markets to raise even larger amounts through IPOs. Unfortunately, many failed. Yet, the
approach remains an important e-commerce B2C e-tailing business model, which in this paper we will term as the Amazon or “A” model.

The phenomenal growth of the B2C e-tailing start-ups combined with the Wall Street and media hype shook the retail industry. Under pressure to be part of the “new economy” traditional retailers often took seemingly desperate moves to aggressively enter into e-tailing themselves. Several created their own websites and many established tracking stocks for these activities so they could also raise capital quickly and cheaply or make acquisitions for stock on a comparable basis to the e-tailing start-ups. Barnes & Noble, a hundred year old book retailer with large stores across the United States, opened its barnesandnoble.com website in May 1997 and established a separate tracking stock somewhat later. (It subsequently collapsed this back into the parent in 2001 given the large losses in the its e-tailing activities and the collapse of the dot.com mania.) Other retailers, such as Toys “R” Us, L. L. Bean and Wal-Mart, followed similar strategies to enter the e-tailing business. This type of e-commerce B2C e-tailing model is popularly known as “bricks-and-clicks” due to these firms’ existing physical retailing infrastructures. In this paper, we term this kind of B2C e-tailing business as the “B&N” model after Barnes & Noble.

Over time, the “B&N” business model seemed to have some obvious advantages over the “A” model e-tailing businesses. First, they often had their own capital and cash flow to invest in their e-tailing ventures. This made them less dependent on the VCs, gave them better control over their business operations, and meant they were not totally dependent on online sales and their website to generate cash flow. Moreover, most of these companies effectively managed to leverage their existing brands and name recognition, permitting them to spend less on advertising compared to A-type e-tailers.

A related advantage was greater consumer confidence since the stores’ physical presence meant that consumers had the option of picking-up or returning merchandise at those locations. This meant customers could order online but take delivery at a nearby store, saving shipping charges. Similarly, they were not totally dependent on trips to the post office or calls to UPS for returns, especially when some e-tailers forced customers to pay for return shipping. In addition, complaints could be handled in person if necessary, not always remotely online. B&N e-tailers also accepted payment for online purchases in their retail establishments, reassuring customers that were
reluctant to give away credit card information online. All these options made delivery, payment and returns faster, less expensive, and more convenient for customers living close to the e-tailer’s retail stores. Yet, they did not sacrifice the convenience of 24-hour access or the ability to conveniently browse for information in their own homes. To emulate these advantages of the B&N e-tailers, the A type businesses started to build their own physical infrastructures such as automated warehouses and selling booths in shopping malls.

Some also used inflated stock values prior to the dot.com collapse to acquire existing retailers in their markets. In this way there has been some convergence between the e-tailing start-ups that have survived and the traditional retailers that entered the online retailing business, with each trying to achieve some optimal competitive combination of web and “bricks-and-mortar” based sales. This is because the “bricks and clicks” or B&N model seems to have emerged during the 1998-2001 period as the e-tailing approach most likely to succeed in the “new economy” or even the “new, new economy”. This is especially true when one recognizes another key competitive advantage for traditional firms - management’s existing knowledge of their customers, business and industry’s particular economics. Amazingly, many new A-type retailers had no previous experience in their industries or markets.

**Emerging E-tailing Difficulties**

This is why the hype and promise of the “new economy” did not last long and a more rational e-commerce business model has emerged. In this model e-tailing has become another channel to reach the customer but not the only channel. Further it must be combined with various support facilities. Reflecting this reality has been the collapse of the NASDAQ, which has housed most e-commerce stocks and their hi-tech suppliers. The first crash came on April 17, 2000, when the NASDAQ fell to 3227 or 37% below its historical (hysterical) high. Over the next several months almost all e-commerce stocks deflated and many e-tailing firms such as e-Toys went bankrupt. Amazon has yet to register a profit. In 2001, it managed to reduce its net loss to 567 million dollars from 1.4 billion dollars from the pervious year (Amazon 2002). As of the end of June 2002, the NASDAQ was hovering around 1500, or more than 70% below the March 2000 high.

This collapse in stock values along with retrenchment by even the relatively successful B&N e-tailers in turn hit the providers of technology very hard. Systems and networking hardware suppliers such as Cisco, Lucent,
Hewlett-Packard, Sun Microsystems and even IBM lost potential sales. More importantly, several firms such as HP, Lucent and Cisco had made sales on suppliers’ credit that included stock options or warrants too. Having booked profits on both their sales and the related securities portfolios, the dot.com bankruptcies forced them to take major write-offs and restate earnings, resulting in enormous reported losses that heavily impacted their own stock values and future sales. Many could not recover their loans to these companies. For example, Cisco wrote off 1.2 billion dollars in 2001 and registered a net loss of 1 billion dollars compared to a net profit of 2.6 and 2.0 billion dollars respectively in the previous two years. Only IBM, which had stricter credit policies and had not used easy credit as a way to buy sales, appeared to be relatively unscathed. Indeed, these other suppliers often met their own recently installed equipment and systems selling in the market at substantial discounts as other creditors dumped these assets. Then with the demise of the dot.com competition and having already invested furiously, the B&N e-tailers pulled back sharply on their new investments as well.

Clearly, there were some problems with these initial e-tailing business models since in retrospect even most of the B&N firms lost money. For the purposes of this paper, three issues seem especially important. First, these e-tailing businesses did not really add significant value within the total retailing value chain. Almost all the e-tailers have depended on third party shippers such as FedEx, DHL or UPS for merchandise delivery. These delivery services are expensive and e-tailers were unable to economically compensate their customers for the shipping charges given their overall margins and the cost of building, operating and advertising their sites. Secondly, while sales growth was certainly impressive, consumers did not flock to online purchasing to the extent or with the rapidity that the industry expected. Though it is often much easier to order online and get delivery to one’s home rather than go to a store, many customers continued to go to stores for the final sale in order to kick the tires or to see and feel the dress prior to purchase. Finally, the e-tailers had no proprietary interest in the products they were selling and given consideration number two were not able to achieve volume purchases that would give them any advantage over the large B&N sellers in their category.

These three factors when combined with potentially insecure payment mechanisms, limited Internet access, and higher than expected advertising costs have so far made many B2C e-commerce business models unprofitable even for the B&N retailers. This raises the question as to whether there is another approach that could overcome
some of these drawbacks and help realize the potential of e-tailing, especially in countries that do not have the US’s extensive PC/Internet infrastructure.

**An Alternative E-tailing Business Model – The Japanese Convenience Store (CVS)**

Such a model appears to be developing very rapidly in Japan. This B2C model is based on several traditional aspects of the Japanese business and consumer retailing culture. These factors include two that seem particularly important. One is that most consumers still pay cash for purchases and two, firms are used to forming cooperative alliances to take advantage of new business opportunities with each delivering its own expertise. The latter in turn occurs because Japan’s long-term employment system makes it difficult to quickly recruit new expertise in the way the US e-tailing start-ups could rapidly attract new personnel at all levels by offering stock incentives and other perks. The new IT-based alliances, however, are different than the traditional and heavily researched horizontal and vertical Keiretsu or company groupings that are often cited for Japan’s economic success in certain industries.

This is because these latter groupings are generally of two types. One is the horizontal groupings of firms in different industries that are often historically based in family controlled zaibatsu with pre-World War II origins. They generally have a large bank at their center. Probably the best known are Mitsubishi, Mitsui and Sumitomo. Conversely, the vertical keiretsu are usually headed by a large industrial concern such as a Toyota, Matsushita or Hitachi and are composed of the lead company, its subsidiaries, and their suppliers. In both cases, there has been extensive inter-firm ownership as well as exchange of personnel over several years. In the new IT based alliances, however, which we term e-retsu, there is often no previous alliance relationship, either vertical or horizontal, and no cross shareholdings. Common shareholding is only in the e-retsu company itself.

Rather, the firms have come together to pool their expertise in a new venture in which all parties have a shareholding and where the common objective is to cooperatively use their expertise and shared personnel to exploit what they jointly see as an e-commerce business opportunity. In addition to quickly raising capital and pooling the principals’ business and technical expertise, this structure also substitutes for the relative scarcity of venture capital in Japan while leveraging the investors’ R&D and consumer brand recognition. Further, because each partner is providing its own products and expertise to the venture, these B2C e-tailing activities cover a much
larger part of the value added chain than either the A or B&N models. From an e-tailing perspective the most interesting of these e-retsurs are those based on the convenience store (CVS), which as we shall see can capture a larger part of the payment and delivery parts of the value chain too. The rest of this paper will focus on these and especially the strategies of the three leading firms and how they and their partners view their e-tailing ventures’ value chain.

**CVS in Japan**

In order to understand this e-tailing model, however, it is important to grasp certain fundamentals about the convenience store in Japan, how it differs from such stores in the US, and the strategies of the leading firms that are driving its development, especially Ito-Yokado and its 7/11 subsidiary, Seven-Eleven Japan (SEJ). CVS in Japan generally have enjoyed relatively better performance than general merchandise stores (GMS) in the 1990s. Sales rose from ¥3.89 trillion in fiscal 1993 to ¥6.18 trillion in fiscal 1998, with sales falling slightly in fiscal 1999 to ¥6.13 trillion. CVS sales remained at that level in fiscal 2001(¥6.14). This situation contrasts with the GMS that experienced declining sales due to increased competition and Japan’s economic downturn.

However, competition among CVS and against other retail sectors has been increasing, and the time is gone when the whole sector could enjoy huge growth. Now, only the better managed CVS have a chance to grow faster given their better merchandising strategy, including more services; greater use of IT; superior strategic site selection; and finally better owner development. Deregulation that will increase the kinds of merchandise and services the CVS can offer will further favor the leading chains given these advantages. For example, increased financial services will require more sophisticated training of store owners and their employees as well as good field support. Only, the leading chains have this capability. This is because the bigger chains, and especially 7/11, can offer a larger number of seasonal and promotional items, geographical variations in what is carried, and extensive and constantly changing fast-food offerings.

In deed, it is generally agreed that Seven-Eleven Japan (SEJ) has achieved its leading position through flexibility supplying its stores with a wide variety of goods and services, especially with different food items during the day. Having sales per store and per square meter at least 50 percent higher than its major competitors became an even more important advantage as the Japanese CVS market saturated during the 1990s with a surge in the number of CVS. During this period the population per store fell below the 3,000 usually regarded as the critical viability level. In major urban areas the situation became even more unfavorable: in Tokyo around 2,000 and in Osaka, even
less. However, it was during this period that the major chains could distinguish between their high-quality stores and the lower-quality ones called CVS just because they are open 24 hours. In 1996 for example, the total number of CVS in Japan, 48,567, included every type that satisfied the minimum definition.

But of those, only about 32,000 actually provided the other usual CVS services such as postage stamp sales, copiers, fax machines, video games, utility bill payment, and package delivery. Therefore, the population per high-quality store at that time may actually have been around 4,000. This is why for quality operations there was a chance during the late 1990s to add as many as 10,000 stores. However, the number of CVS actually declined by 9,000 to 39,627 in early 2001. So the general feeling now is that saturation has finally been reached even for higher-quality stores while the number of marginal stores has been substantially reduced. Therefore the recently announced strategies even among the leading firms has been not to expand the total number of stores but rather to replace those among their existing stores that are operating less successfully, with the replacement stores in locations with better market potential and that can sell alcohol. For example, SEJ’s percentage of stores that can sell alcohol has risen from about 35% in 1991 to about 63% in 2001 (SEJ Outline 2001).

This approach at the same time is being combined with an expanded range of services for all stores. It is the latter part of this two-prong strategy that is the key motivator behind their e-retsu e-tailing initiatives. The competitive pressures in this direction are indicated by the fact that low-quality stores that do not belong to a franchise have been closing or converting to become part of a larger chain for some time. In 1996 there were 1,486 such closures, equal to 45% of the 3,218 newly opened stores, which were virtually all franchises or owned by a CVS chain. That these smaller stores were the first to go is also indicated by the fact that the major CVS companies were only doing a little scrap-and-build of their existing franchise stores during this period. The number of scrapped stores per listed CVS at this time was only some 100 per year, or about 20% of new openings compared to the current rough equality.

For this reason the share of stores related to the eight major CVS companies actually rose from 21% in 1985, to 30% in 1990, to 40% in 1995 and 43% in 1996. Thus by 1996 their share was almost twice that in 1985. Then in the 1990s even some larger chains came under pressure so that by 2000 the top six had 65% of the stores and over 80% of total CVS sales. This is why now even leading stores are reining in their rapid expansion, with Lawson and FamilyMart in early 2001 announcing closures and relocations of hundreds of lower-performing stores.
with planned openings in more-promising locations or those having liquor licenses. For example FamilyMart’s stores with such licenses increased from 1901 in FY 2000 to 2279 in 2001. However, there will be little net change in their total number of stores.

Similarly, Lawson’s Executive Vice President, Koji Wada, noted in Lawson’s 2001 Annual Report that in fiscal 2001 they “expect to open 650 stores, a roughly 10% decline compared to openings in fiscal 2000. Thereafter, we will adhere to our policy of not overextending ourselves by opening new stores where the numbers don’t justify it.” For the same reason, SEJ currently evaluates some 135 factors in deciding whether to open a new store. But despite this increasingly competitive environment, SEJ appears to be using its greater efficiency to further increase its market share.

That is, since 1993 SEJ has opened about 400-500 stores per year and during 2001 had a backlog of about 500 waiting to be opened while publicly stating its intention to steadily increase its number of stores and location dominance. The apparent success of this strategy is reflected in average daily sales for new stores since 1995 of over 520,000 yen, which is greater than the average for even existing stores among its competitors. Further, most of these new openings seem to have a license to sell liquor since the number of such SEJ stores increased from 5115 in FY 2000 to 5427 in FY 2001. This may also be why average daily visits per store are up about 20% since 1982 while the average sale per customer has risen from 600 yen to over 800 yen and the average gross margin has gone from a little over 26% to over 30%. This compares with FamilyMart’s sales per customer of about 600 yen in 2001. Due to the availability of liquor, logically SEJ’s sales to those over 20 have increased steadily.

CVS Merchandising Strategy

As noted above, a key strategy for the leading Japanese CVS has been to continually add services to attract traffic, even if these services do not contribute directly to profits. Thus, many have long offered copiers, fax services, and video games. Beginning in 1987 they became payment points for electricity, gas, and water bills. (SEJ was the first and reports having 3% of the total Japanese payments market in 2000, which includes payments made through banks and the postal system.) In February 1989 SEJ also became a payment-point for Daiichi Seimei (life insurance). As deregulation has allowed, CVS stores have added sales of money orders and postage stamps. Sale of rice was allowed in 1996. Foreign exchange services started in April 1998. Package shipping was started in the mid-1990s. SEJ works primarily with Yamato Unyu (Black Cat), by far Japan's largest package-delivery firm. During FY 2001, SEJ handled over 13.5 million packages.

In November 1999 SEJ began accepting payment for purchases made over the Internet as part of its e-retsu strategy. Reservation services for travel packages became available beginning in late 2000. With these new
offerings, sales of existing CVS began rising again. Looking ahead, stores even may be able to sell some prescription pharmaceutical products. One idea is to have them act as a pick-up and payment point for an on-line pharmacy.

The success of these activities reflects that Japan is still very much a cash-using society since even those with credit cards are reluctant to give the number over the phone or Internet. This is demonstrated by the fact in the year ending February 2001 SEJ handled over ¥800 billion in third-party payments on behalf of 245 companies. This involved over 100 million transactions. Furthermore, over 75% of Internet purchases are currently paid for in CVS. More recently banking and financial services are being offered as deregulation continues. Working couples needing financial services outside normal banking hours already have been targeted. Several CVS have initiated their plans to act as automated bank branches with ATMs. While IY has established its own bank, as discussed later, Lawson, FamilyMart and other CVS have entered into alliances with banks who install and service the ATMs in their stores. Other IT alliances are focused on games, entertainment and other services as detailed in the case studies that follow.

Yet it is clear that handling this wide range of services requires thought, support, and staff training. For example, when CVS started selling game software in 1996, the makers selected stores based on distribution power. This relates to how extensive the franchise network is and how well the distribution system works to supply stores. The implication is that although a CVS can add items and services, not all chains may be able to do it well and profitably. Further, many of these new products and services, especially financial ones, are very IT intensive. The store ideally wants the customer to buy lunch, a snack and magazine for later, and a toiletry, while checking bank balances, making payments, or trading stocks. All this tends to favor the leading firms with the most sophisticated and wealthy partners.

This also means that selection of franchisees and good site selection will be key aspects of a successful CVS strategy including its e-tailing component. This is because the competition among CVS firms for new stores in promising areas has reduced the average quality of franchisees and CVS stores. At some CVS chains the staff responsible for developing new stores and advising new franchise owners are not very competent. Competence is very important when more complex services are added. SEJ's store-support staff of 1500 thus is key to its competitive strength. Since franchise-closing costs are much higher than opening costs, CVS firms have to pay
careful attention to their relations, support, and contracts with franchisees. Since sophisticated partners want to optimize their chances for e-commerce success they will tend to align themselves with the more successful better managed CVS, which in turn will contribute to the potential success of the e-tailing venture and the CVS, a beneficial loop.

**Key Strategic Differences in CVS E-tailing Business Model**

As already explained, one difficulty that has emerged in widely applying the “A” type e-tailing business model has been the relatively small part of the value chain it occupies between the production of a good or service and its delivery to the final customer. In the case of Amazon, for example, it does not produce the books, CDs and other items that it sells and actual delivery (UPS or Fed-Ex) and payment (credit card) are also provided by third parties. This is why to amortize the high fixed cost of its hardware and software systems Amazon has needed to generate economies of scope by dramatically expanding the goods and services it offers. Indeed, E-bay in particular shows how economies of scope can be effectively employed to achieve a successful e-tailing venture using the “A” model.

At the same time, the failure of ventures with more limited markets such as E-toy that were not able to generate economies of scope shows the strategic risks involved in the using the A model to penetrate an e-tailing market segment. This is especially true if it is occupied or can be occupied by a B&N type competitor such as Toys “R” Us and where the interaction between returns and customer satisfaction are important. The B&N model has generally proved superior because it is able to capture a larger part of the value added stream including some parts of delivery and payment as well as a lower cost of returns with better customer satisfaction.

However, the B&N model is less well positioned to develop economies of scope since the “bricks” part of the business is generally specialized, e.g. Barnes & Noble or Charles Schwab. As will be seen in the following case studies for Seven-Eleven Japan, Lawson and FamilyMart, the Japanese CVS model appears to address the potential e-tailing limitations of both the “A” and “B&N” business models. That is, through their websites and catalogues, they can generate economies of scope while by using their convenience stores as payment and pick-up centers they can also achieve the greater value added and better handling of returns of the B&N model. In addition, through their e-retsu partnerships they can create and/or capture some of the product value as well.
That is, by including content providers as shareholders in their e-tailing ventures, they gain some of this part of the value added income stream, which neither of the two US type e-tailing models can do. Finally, via their multimedia kiosks, they are increasing store traffic that improves the revenue stream of their basic retailing business, an externality to the e-tailing venture. For these reasons, these cases bear closer study both now and in the future as an approach to e-tailing’s emergence as a growth market in various countries in the years ahead.

**Seven Eleven Japan (SEJ)**

SEJ and Sony, for example, have an agreement to offer high-speed downloading of games for PlayStation 2. This means an SEJ store can offer a total selection of games, but only has to inventory blank CDs. Players in turn will have an alternative to downloading over a slow (and expensive) residential telephone line. In addition, upgrades will be easy to provide for a small fee. The pressure on video game rental stores and software shops will be enormous.

Thus e-commerce has definitely been taking hold in Japan, but it has been evolving differently than in the United States, and changing Japanese retailers' strategies. In fact with Nomura Research Institute’s (NRI) help, IY and SEJ are moving quickly and decisively to have an impact on this e-commerce development, using a customer-driven strategy in which the concept of convenience goes well beyond the types of items one normally associate with a CVS. A critical area in this approach to making e-commerce work is developing a convenient and secure payment mechanism with which customers feel comfortable. As just explained, many Japanese do not trust giving a credit card number over the Internet or telephone, while others just prefer to pay cash. So combining e-commerce websites with a large CVS chain allows people to pay at conveniently located stores, as well as to take delivery. This process also facilitates returns, as they can be done on the spot. This is analogous to a perceived advantage in the B&N model. It is also an evolutionary extension of SEJ’s third-party payment service, which did about 105 million transactions in FY 2001 up from 86 million in 2000 with a value of 813 billion yen compared to 641 billion in FY 2000.

In Japan it is therefore now common to order items such as books, video games, and CDs through the Internet using the CVS for payment and delivery. In fact IY and SEJ have led this change. In 1999 SEJ established joint ventures such as e-Shopping!Books with Softbank, Tohan, and Yahoo! Japan, and CarPoint Japan for car sales
with Softbank, Microsoft, and Yahoo! Japan. In addition, the 3 million customers of Japan's largest virtual mall, Rakuten Ichiba (rakuten.co.jp), can use SEJ stores to make their payments and pick-up packages if they do not want them delivered. Indeed, IY reports that about 75% of the shoppers on its websites pick-up and pay at the store. Further, SEJ and NRI jointly have started providing clearing services for purchasing through the Internet.

There is also Seven-Meal Service “for customers who find daily meal preparation inconvenient …”; they “place orders through telephone, fax, the Internet and at stores and choose whether to receive the products at home or at a nearby Seven-Eleven store.” (SEJ Corporate Outline)

**7dream.com**

More directly, in January 2000, SEJ and NRI announced the formation of a new B2C e-retsu (a company based solely on IT relationships) with capital of ¥5 billion. Called 7dream.com, SEJ intends it to be “one of the largest EC [e-commerce] businesses in Japan and operate at the forefront of its field”. 7dream provides a range of services on its website, all of which eventually will be accessible from the multimedia kiosks installed in SEJ stores. In keeping with NRI's recommendations that any e-commerce access strategy should be “ubiquitous”, 7dream also can be accessed directly over the Internet and other networks, including those open to mobile phones and direct TV, or by using catalogues available in all SEJ stores.

As seen in Table 1, through its e-retsu members the new firm is offering a range of services. These relate to travel, music, gifts, mobile phones, event tickets (tie-up with PIA Corp, Japan's largest ticket agency), books (arrangement with e-Shopping!Books Corp), car-related services (sales via CarPoint and, later, arranging auto inspections, repairs, driving lessons, and rental cars), and information services related to entertainment, digital photographs, and special examinations in partnership with firms such as Toppan Printing and JMA Management Center. Table 1 lists the ownership relations and what expertise and services each brings to the venture.

As of August 2001 there were about 1,200 7dream terminals in 7-Eleven stores in the Tokyo area, with the rollout elsewhere planned over the next few years. Meanwhile, anyone can order from the web site, the call center, or in the store using a monthly catalog available at all stores. The offerings in the catalog are non-bulky because the stores have limited storage space for holding items until they are picked up. The catalog contains items not offered
via the kiosks, which currently are more focused on tickets, CDs, and games. (This is currently true of the kiosks at all the CVS chains.)

SEJ expects start-up costs to be around ¥40 billion and projects annual sales of about ¥150 billion for 2002 and ¥300 billion for 2004. This obviously offers IY tremendous opportunities to enlarge the goods and services available at SEJ stores throughout Japan, including banking and financial services. While ultimately SEJ’s objective is to operate in all 47 Japanese ken currently its focus is on the ones in which it is already dominant. SEJ estimates that it has about 9 million customers in its service areas and it is supporting its sales to those clients via an ISDN based network that was jointly developed with NRI and NEC. Similarly they work together to operate and update this system.

Table 1
7dream.com Owners/e-retsu Members

<table>
<thead>
<tr>
<th>Ownership (percentage)</th>
<th>Expertise and services provided</th>
</tr>
</thead>
<tbody>
<tr>
<td>SEJ (51%)</td>
<td>Principal organizer; provides places for kiosks to access the web site.</td>
</tr>
<tr>
<td>NRI (13%)</td>
<td>Advises on structuring business, as well as developing and operating e-commerce system.</td>
</tr>
<tr>
<td>NEC (13%)</td>
<td>Built, operates website. Designed/developed multimedia terminals, all connected via dedicated lines.</td>
</tr>
<tr>
<td>Sony (6.5%)</td>
<td>Supplies technological support related to its MD (mini-disk) and IC card technologies.</td>
</tr>
<tr>
<td>Sony Marketing (6.5%)</td>
<td>see Sony, includes online packaged music and games</td>
</tr>
<tr>
<td>Mitsui &amp; Co (6%)</td>
<td>A trading company providing information, merchandising support, and distribution.</td>
</tr>
<tr>
<td>JTB (2%)</td>
<td>A travel agency (formerly Japan Travel Bureau)</td>
</tr>
<tr>
<td>KINOTROPE (2%)</td>
<td>A software firm consulting on Internet business design and systems development</td>
</tr>
</tbody>
</table>

Currently, 7Dream has 250,000 members in its system and its biggest selling items are books, CDs (Sony), travel services (trips via JTB) and tickets to various entertainment and sporting events via PIA (Japan’s largest ticket agent). SEJ provides a monthly catalogue to all stores. It lists items that cover travel, events and items for sale. (Interestingly FamilyMart has 500,000 members and has a more extensive list of items for sale.) SEJ sees the number of system users expanding as PC use of the Internet expands since it can then show more about its services. Customers still want some way to view the product or service first for review and comparative shopping prior to purchase. But even in that case they will come to the store to pay and pick-up just as they do for many of their other
bills. So this is an evolutionary process where SEJ is positioning itself to eventually provide full B2C e-commerce but for now it is doing more via the store.

Currently even the multimedia kiosk (MMK) has limited functions such as buying tickets and downloading CDs and games. It does not yet give access to the Internet or to the full catalogue of products that can be purchased via phone or at the store using SEJ’s proprietary online system or the catalogue. Further, prices are still a bit high as one is paying for convenience. But SEJ expects prices will drop with experience, use and the number of goods or services sold. So they see this as early in the competitive game. This is true for the IY-Bank too, as IY’s and SEJ’s approach is very different than other convenience stores. Yet, IY feels it is fulfilling a definite customer need since the firm’s market research indicates that its customers are dissatisfied with traditional banks that are ‘far from residential areas,” have “limited operating hours,” and do not offer “financial products and services that really meet customer needs.” (IY Bank 2001)

IY Bank

Because many customers want the convenience of paying for their e-Commerce purchases at the CVS stores in cash, most CVS have combined their multimedia e-commerce strategy with 24-hour ATMs in addition to the multimedia kiosks (MMKs). However, as under Japanese law, only banks can have ATMs, the CVS other than SEJ have invited one or more banks to locate ATMs in their stores. That means the bank controls the ATM. Therefore as IY and SEJ want to control the services available through the ATMs in their stores, they decided to organize their own bank to serve their 10 million customers per day plus their 200,000 employees. This is despite the greater capital and systems reporting required. It began in May 2001 with 130 employees to start and initial capital of yen 20.2 billion.

IY was in fact the first non-bank to apply for an on-line banking license and was joined in this e-venture by Bank of Tokyo-Mitsubishi, Sanwa Bank (UFJ Group), NEC, and NRI as shareholders. Nomura Securities, Nikko Securities, and Sony have joined the venture too and three other banks (regional banks - Asahi Bank, Shizuoka Bank, and Bank of Yokohama) have become affiliated. The shareholding and affiliated banks have provided staff, as has SEJ, while the bank's president is a former Bank of Japan official. The participation of two securities firms reflects IY and SEJ’s expectation that on-line brokerage services will eventually be provided.
Further, Sony has affiliates that offer life and auto insurance, while it is also planning an e-bank. The participating banks expect to be able to close branches without sacrificing customer service since depending on store locations, the ATMs accept different affiliated bankcards besides IY’s. By the end of December 2001 there were about 2,200 of these ATMs installed, all in metropolitan Tokyo and adjacent areas. By the spring of 2002 over 3,600 stores will be served and over 7,100 throughout Japan by the spring of 2006. Services offered will eventually include bank accounts, remittances, money transfers, a debit card within the IY group, credit cards, purchase point cards, loans, Internet banking, and settlement services with member firms such as 7dream.com or Seven-Meal Service. There will also be services such as brokerage, insurance and credit cards offered through affiliated firms.

Installation costs have been about ¥2.5 million per ATM, and because an ATM is a bank branch under Japanese banking rules, the accounts can be opened only at a bank branch (or by mail). So SEJ can open accounts only in the stores with ATMs. In the first two months of operation (June and July 2001) about 10,000 accounts were opened. Not surprisingly, ATM use has been primarily on weekends and after 8PM. Besides the Seven-Eleven CVS, ATMs ultimately will be placed in IY’s other operations such as Denny’s restaurants and IY’s general-merchandise stores. Because IY and SEJ control the bank, they control the services offered and the ATMs’ functions. So they can target services important to their clients and can leverage advances in technology since the first ATMs were introduced.

Thus, these CVS ATMs are electronically sophisticated and can be programmed to handle a variety of functions over time as services evolve while also being very compact, which is important for the storeowners. However, so far SEJ has not trained store personnel in these functions. So from a store’s perspective the ATMs are for now just being used to generate traffic with the bank partners handling the actual service. (SEJ has admitted that it was tougher getting the ATMs up and operating than it expected.) In this way IY and SEJ’s e-commerce support system is an extension of its already very sophisticated IT system that is largely independent of the Internet. This reflects the fact it was largely in place by the time the potential of the Internet was widely recognized. But the company feels the advantages of a proprietary network are such that it would not have made the system Internet-based even if that had been an option. This is not to say SEJ’s management are ignoring the Internet in areas where they feel it is appropriate. And they are certainly monitoring its use by others since Lawson and Mitsubishi Corp,
Japan's largest trading company, are constructing an Internet-based system that is intended to emulate SEJ's proprietary IT system. But for the time being they prefer the control and competitive barriers their current approach creates.

<table>
<thead>
<tr>
<th>Basic Financial Data SEJ FY1996-2001 (February)</th>
</tr>
</thead>
<tbody>
<tr>
<td>Total Store Sales (yen billions)</td>
</tr>
<tr>
<td>Revenue (yen billions)</td>
</tr>
<tr>
<td>Operating Income (yen billions)</td>
</tr>
<tr>
<td>Number Stores (Japan)</td>
</tr>
<tr>
<td>Average Daily Sales per store</td>
</tr>
<tr>
<td>(yen thousands)</td>
</tr>
<tr>
<td>Gross Margin (%)</td>
</tr>
</tbody>
</table>

Source: SEJ Corporate Outline; Brief Summary Results FY2001; does not include Hawaiian stores

**Lawson**

Japan’s second largest CVS, Lawson, was established in 1975 as a subsidiary of Daiei, Japan’s largest GMS, but it only became listed on the Tokyo Stock Exchange in July 2000. As of May 2002, Lawson had 7,624 stores (including 69 in Shanghai, China) and 3,548 total employees. Annual sales for FY2001-2002 were yen 1,282.3 billion. In May 2002 average daily visits and sales per store were around 790 customers and yen 478,000 respectively. Responding to SEJ’s e-commerce challenge Lawson has developed a multi-channel e-commerce system based on the Internet, mobile phones and multimedia kiosks (MMK). It calls this B2C e-commerce activity “@Lawson” and its website is: [www.at-Lawson.com](http://www.at-Lawson.com), launched in December 1999. An affiliated company, ECONTEXT, handles product delivery, agency transaction settlements and other @Lawson agency activities. Because this is an open platform Internet based service, their strategy is to add other convenience stores, gas stations, etc, to their system as payment and pick-up points giving them greater economies of scope. In May 2001, about the same time that IY was launching IY Bank, Lawson and a consolidated subsidiary, i-Convenience, initiated i-Lawson, a mobile e-kiosk system which allows customers to shop using their mobile phones if they are
among NTT DoCoMo’s customers using i-mode\(^1\). They can order products for delivery at Lawson stores, make payments at Lawson cash registers using a special connection, and access Lawson’s various entertainment services.

This m-commerce activity thus allows customers to use their mobile phones to order various products and services as well as to connect their mobile phones to a store register to settle bill payments and receive products ordered over the Internet. Established in October 2000 and capitalized at about $20 million, i-Convenience is an e-retsu between NTT DoCoMo Inc., Matsushita Electric Industrial Co., Ltd. (Panasonic), Lawson Inc. and Mitsubishi Corporation, which is currently Lawson’s largest shareholder.

Further to competitively respond SEJ’s e-retsu relationship with Sony, Lawson has entered into its own game software alliance relationship with Nintendo along with a second alliance that includes Dentsu, Japan’s largest advertising agency. The goal of the first alliance is to sell video games through Lawson’s online market, and of the second to develop game software for portable machines and mobile phones.

Nintendo signed the agreements to counter similar moves made by Sony with SEJ.

**Loppi Multimedia Kiosks (MMK)**

Having begun installing Loppi (stands for “Lawson Online Shopping Print and Pay Information”) kiosks in its stores as early as 1998, Lawson is currently the CVS leader in installed multimedia kiosks. These kiosks which Lawson sources in terms of development and manufacture from IBM are currently found in all Lawson stores, around 7700. This contrasts with SEJ and FamilyMart, which are not yet Nationwide and where the respective totals as of the summer of 2001 were only about 1000-1200 each. Sales, mostly entertainment related, increased 16.5% in fiscal 2000 (end 2/2001) to yen 39.6 billion and the company expected them to rise another 21.2% during fiscal 2001 (end 2/2002).

Loppi offers many different kinds of products and services while also providing popular information such as the appearance of a certain band. Loppi has two specific features: an entertainment element for purchasing concert tickets or downloading game software and an information platform element to support payments by customers, such as to loan repayments to financial institutions, or to obtain public information on such things as cultural events or the weather. Tickets for concerts, sporting events, and movies are sold in collaboration with

---

\(^1\) NTT DoCoMo is the largest mobile phone operator in Japan. As of June 2002, it has a 59% market share in Japan with 33.1 million i-mode subscribers.
Lawson Tickets Co., Ltd. (LTCL), a consolidated subsidiary. Other LTCL channels are the Lawson and Daiei stores or by phone. In addition, it now handles airline tickets and tickets to Disneyland and Universal Studios. Further, in 2001 Loppi launched a hotel booking service in conjunction with JTB, indicating that not all e-retsu alliances are exclusive. (See Table 1.) In the future it plans to integrate Loppi with its ATMs and related financial services.

**E-commerce Strategy**

Using their own combination of clicks and bricks Lawson believes its can effectively counter and even surpass SEJ and IY in becoming Japan’s leading B2C e-commerce company. One reason for this is that Lawson recognized early that their entrance into e-commerce began with the development of 3rd party bill settlement services in 1995-96 since their e-commerce initiatives are a direct outgrowth of this and still incorporate it as an essential feature. In turn these payment services have grown at a rate of about 20% per year since. During FY 2000 (ending February 2001) Lawson processed 82 million transactions for a total of 650 billion yen. Those 82 million transactions of course represent store traffic in addition to the small fee made on each transaction.

So their storeowners have an incentive to make it work especially when the owner owns both the land and the store, as in these cases Lawson’s margin is only 34%. This compares to Lawson’s margin of 45% and 50% respectively when Lawson owns the land and the owner of the store but leases the land or when Lawson owns both and the franchisee leases them. The scanner records all sales electronically so the margin calculations are all done automatically even though the customer pays cash. This is also true for sales through their new MMKs (Loppi), which were installed in all Lawson stores by October 1998.

What happens is that when a customer makes a travel reservation through the kiosk, buys the right to download music, or purchases as concert ticket, the customer gets a bar coded coupon from the machine. The bar-coded coupon has information on the type of purchase, the amount, and delivery (pick-up at Lawson, mail, or parcel service). He or she then takes the coupon to the counter where it is recorded like any other sale, and the customer pays (cash or credit card) along with any other purchases. This procedure
enables Lawson to easily and efficiently handle payments to their 150 partners (actually 500 if one includes credit card companies) by electronically using the banking system as an intermediary.

As part of their e-commerce strategy Lawson does not deal directly with the providers since this would cost them printing and mailing charges. So they try to be non-paper as much as possible in using the kiosks, though they do have the physical record of the bill from the bar-coded coupon. Eventually they hope that even this will be eliminated and everything can be electronic and connected, but right now each area still operates independently in terms of supply and service. That is, strategically they are working with e-tailers so the customer can just click and route the order and the payment, and they do not have to issue the bar-coded bills at all. In terms of downloading games (Nintendo) and music (Sony), these are handled in the store. Stores are not connected to a central server but rather each store has the Mother software for the games in the store and then downloads the game selected onto a blank game cartridge or rewrites an existing one. In the case of music, the songs are also available in the store and what one purchases is the right to download the music onto a cassette that one brings or buys. Eventually though Lawson hopes to have this done centrally online from a central server the same way that much Karaoke in Japan is currently done.

Similar to their arrangement with Nintendo and Sony music is a recent contract with HMV, a large international retailer, which sells a wide range of CDs through mega-stores and which is now opening in Japan. Through this arrangement, Lawson customers via Loppi have access to HMV’s catalogue of titles. Selecting from this catalogue, customers can order a CD through a Loppi, pay for it, and then pick it up at the store the next day. The payment part is quite easy but the physical delivery is tougher to do efficiently when a given store may only be receiving one or two CDs a day. But it is a way for HMV to extend its e-commerce reach beyond its mega-stores while Lawson can extend the titles it can offer beyond Sony Music downloads. As a transition it began payment for the CDs at Lawson stores with the CDs being mailed rather than picked-up at the Lawson store, but the latter is coming. There will also be potential for downloading directly onto a CD or cassette at each store as stores become connected via satellite.
In this manner the Loppi will ultimately serve two e-commerce functions. One will be as an electronic multimedia platform for third party providers such as HMV and Sony. The second will be for Lawson’s own business merchandising. For instance it has its own concert and event ticket company (like Ticketmaster in the US) which competes with PIA, Japan’s largest such company. (PIA uses SEJ and FamilyMart as its convenience store outlets.)

This business has been growing about 20% per year and now amounts to 32 billion yen per year and is second in Japan to PIA’s 50 billion yen. Lawson’s profit on this business after only three years is 52 million yen, and this does not include increases in sales due to greater store traffic. Further, its business model is simpler than PIA’s, which sells tickets for a wider range of events. Lawson instead targets customers that are in their 20s and 30s and like music. Lawson then promotes in their stores and on their delivery trucks special “Glory” concerts that will attract perhaps 300,000 fans and for which they control the ticket sales. The idea seems to be working.

Also, by buying 3% of Nintendo it has converted this part of their business from a third party activity to part of their own business merchandising while from Nintendo’s standpoint they have gained a strong e-commerce ally against the Sony PlayStation-SEJ combination. They have also joined with JTB to offer last minute or “Quick” travel packages that are unique to Lawson. So while JTB also sells travel services through SEJ and FamilyMart, these particular packages can only be purchased via Lawson and its Loppis. They also offer such things as flowers for birthdays and personalized golf balls. Yet among these varied initiatives, currently entertainment accounts for about 80% of their total Loppi related sales. To provide technical support they have a subsidiary Lawson ePlanning while the ECONEXT affiliate handles delivery.

**Bricks and Clicks**

As part of their e-commerce strategy they have leveraged their physical stores and distribution network by developing an online catalogue, which is connected to the Internet so customers can access it via PC or i-Mode phones. They also advertise items in newspapers or in their stores using posters and paper catalogues. The latter are in the form of various guides that are broken into “Shopping” for products such as
flowers, toys and golf merchandise, “Travel,” “Schools” for learning everything from the tea ceremony and flower arranging to using computers, and finally services such as motorcycle insurance or airline reservations. The ads and guides explain about how to access the products or services on-line along with delivery information and the lead-time for every product or service. Ultimately these will all be combined electronically, but it will take until the summer of 2003 or 2004 to accomplish this. Lawson launched a new TV advertising campaign in January 2002. The “Weekly Lawson” series, which runs a new TV commercial every week. The concept of a weekly cycle of new TV ads derives from the fact that more than 80% of Lawson’s customers visit stores at least once a week. Lawson thus hopes to stimulate customers’ interest and even introduce an element of surprise to its stores and online site by renewing its attractions on a weekly basis and directly linking these initiatives to the TV commercials. In FY2000 Lawson sold about 40 billion yen worth of products and services through Loppi with 32 billion entertainment related. So while its e-commerce activities are growing, they are not exploding. Lawson thinks they might have to wait for broadband and 3-G for this to happen.

This is one reason why they entered into the site access joint venture with NTT DoCoMo, Japan’s largest mobile phone company and the leader in introducing Internet access by mobile phone (i-Mode) and 3-G. It is called i-Lawson and has a membership of 65,000, the largest among convenience stores in Japan. They hope to establish the standard for the Internet connections between convenience stores and i-Mode in terms of how to arrange purchase, payment, and delivery. Once the system is created and is working they hope to license it to other stores and to collect a royalty. Their partners in this effort are Matsushita (technical partner) and Mitsubishi Corp. (content partner). This compares with C. Itoh and Toyota/NTT Data for FamilyMart and Mitsui and NEC/NRI for SEJ. So all firms seem to be pursuing somewhat parallel strategies, though Lawson believes it is in the lead.

The members of i-Lawson get an IC card and accumulate points for their purchases, which they can then use for discounts on other Lawson purchases including breakfast at a Lawson store. Management believes this concept has led to an increase in store traffic, one of their key strategic aims. Some other related e-retsu companies include i-Convenience, which offers a Lawson m-commerce site and is 52%
owned by Lawson and 18% by Mitsubishi and e-Context that provides connections to the Internet, 3rd party
payments, and Lawson’s in-store ATMs. Mitsubishi owns 10% of this firm. The ATM operating company
is 65% owned by Lawson, 5% Mitsubishi, and 5% each for the banks that actually own the ATMs. These
are UFJ, Mitsui-Sumitomo, Tokyo Mitsubishi, and Mizuho. They also have connections with regional
banks depending on the area each store serves such as in Aomori, Nagasaki, and Nagoya. As of April 2002
there were 2,103 ATMs in their stores, mostly in the Tokyo and Osaka areas. Further, by having the local
or regional banks provide the actual ATMs they save capital.

According to Lawson, IY Bank’s ATMs along with those of Lawson, FamilyMart, Sunkus, and
Circle K are all supported by something called e-net, involving IBM and NTT. Currently Lawson has
divided the Kanto area into 4 areas for managing the ATMs and supplying yen currency. The bank partners
supply the latter on a 24-hour basis and charge customers fees to use bank cards from outside the bank
support group for that area. Lawson bears the risk and cost associated with each ATM up to some amount
but above that the banks bear these. Lawson management feels their approach is more convenient for their
customers at least so far than IY’s and SEJ’s as Lawson has more machines (both kiosks and ATMs) in
place. But they admit they do not have the same control over the system and are thus not sure when they
can add additional financial services such as loans, insurance, or brokerage. So while Lawson seems to
have a lead in some e-commerce areas, the winner of the race is not yet clear. What is clear is that the CVS-
based e-commerce model is working, growing and profitable. How many US firms can say that?

Therefore it is not surprising that Lawson’s 2001 Annual Report views e-Retailing as both
currently and prospectively important. “In e-commerce and mobile commerce, which include the Internet
and NTT DoCoMo’s i-mode mobile service, our store network facilitates Lawson’s existing services-
settlement services and product pick-up at stores. We aim to provide these services for a fee to retailers and
service providers that sell on line. The key element differentiating Lawson from other chains is our
nationwide presence. Clients using Lawson services will thus have access to consumers throughout Japan,
unlocking a host of new Net business opportunities. Leading companies have already honed in on our
strengths. We have, for example, launched joint ventures with NTT DoCoMo, Inc., Matsushita Electric
Industrial Co., Ltd. and Mitsubishi Corp. Indeed, Lawson’s competitive advantage also lies in being able to tap into these companies’ wealth of resources.” However, given the similar initiatives of its major competitors SEJ and FamilyMart it is less clear whether they will be able to meet the objective to “improve customer convenience and set ourselves apart from other industry chains by promoting e-commerce and financial services.”

**Basic Financial Data Lawson FY1996-2001 (February)**

<table>
<thead>
<tr>
<th></th>
<th></th>
<th></th>
<th></th>
<th></th>
<th></th>
<th></th>
</tr>
</thead>
<tbody>
<tr>
<td>Total Store Sales (yen billions)</td>
<td>885</td>
<td>985</td>
<td>1094</td>
<td>1157</td>
<td>1221</td>
<td>1275</td>
</tr>
<tr>
<td>Revenue (yen billions)</td>
<td>N/A</td>
<td>N/A</td>
<td>304</td>
<td>302</td>
<td>291</td>
<td>280</td>
</tr>
<tr>
<td>Operating Income (yen billions)</td>
<td>N/A</td>
<td>N/A</td>
<td>N/A</td>
<td>34</td>
<td>40</td>
<td>41</td>
</tr>
<tr>
<td>Number Stores</td>
<td>5683</td>
<td>6252</td>
<td>6649</td>
<td>7016</td>
<td>7378</td>
<td>7683</td>
</tr>
<tr>
<td>Average Daily Sales per store</td>
<td>N/A</td>
<td>N/A</td>
<td>N/A</td>
<td>482</td>
<td>483</td>
<td>486</td>
</tr>
<tr>
<td>(yen thousands)</td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Gross Margin (%)</td>
<td>N/A</td>
<td>N/A</td>
<td>N/A</td>
<td>30.0</td>
<td>30.3</td>
<td>30.3</td>
</tr>
</tbody>
</table>

Source: SEJ Company Outline; Lawson 2001 Annual Report; does not include stores in Shanghai

**FamilyMart (FM)**

FM’s CEO Michio Tanabe foresees FM’s “E-retail business as having boundless potential and expect operations in the field to become a pillar of our efforts to build FamilyMart into a Super CVS. Even with additional investment, we expect that fiscal 2002 will be an incubation period for our E-Retail business. However, we anticipate related operations will begin to achieve significant growth from fiscal 2000.” (See FamilyMart 2001 Annual Report.) In turn, FamilyMart’s e-retsu for developing its e-retailing business is composed of FamilyMart (50.5%), C. Itoh (14.5%), Toyota (10%), NTT Data (10%), Dai Nippon Printing (5%), JTB (5%), PIA (5%). Though some of the e-retsu partners and their motivation are different, FamilyMart’s e-commerce strategy shares some common elements with SEJ’s and Lawson’s in that in cooperation with Sharp (a major electronics company) it is deploying Famiport kiosks in stores to allow downloading of game software and e-books. The kiosks were in over 20% of FamilyMarts by May 2001. The service is aimed at users of Sharp's Zaurus, a PDA with almost a quarter of the Japanese market. The kiosks are being made by e-plat, a joint venture of Toyota and NTT Data,
Japan’s largest IT systems integrator and an affiliate of Japan’s dominant telecom carrier. The ordering and payment system connects to a communications and computer center run by Toyota. NTT Data handles the actual settlement in conjunction with IBM and the Japanese bank clearing system, e-net, as explained above. FamilyMart also is cooperating with Toyota to promote the automaker’s gazoo.com web site.

FamilyMart.com as a B2C business was organized in October 2000 and started its operation in May 2001 including an Internet shopping site with about 30,000 items. It projects that Japan’s B2C e-tailing business will grow in 3 phases to 7.1 trillion yen by 2005 as it penetrates older and older households. This compares with Accenture’s estimate of 13.3 trillion yen. NTT Data is a partner, and supplies and manages the system. The content providers are the other shareholders, including Toyota and C. Itoh. FM is also collaborating with firms other than the e-retsu shareholders. Their spokesman noted that the CVS in particular recognize the special advantages to them of e-Commerce and Internet-based services. This is because the leading CVS already have systems and logistics in place and thus represent the ideal mix of “bricks and clicks” with good penetration of the younger part of the population most disposed to e-related activities such as Lawson’s concert ticket and CD sales. Large Japanese CVS are well placed to facilitate payment by cash or credit card and because of their tie-ups with delivery services as well as having their own logistics systems, they can support these aspects of B2C e-commerce too. (For example, FM often uses Yamato on a non-exclusive basis. So Yamato is not completely in IY’s and SEJ’s pocket.)

The fact they have their own brands available in their stores and over the net FM sees as an advantage too. The Internet service they are now offering allows for an i-Mode connection, which puts them in contact with a huge customer base, especially among younger customers that favor the convenience store. Furthermore, like SEJ they have segmented the market by starting a service for older people that are rapidly becoming a very large part of the population. Statistics indicate that persons over 65 will account for over 25% of the population by 2015. Called “home car”, it will provide older people with meal service, general merchandise and all daily necessities.

For both the Internet based service and the home support service FM is encouraging each franchise store to establish their own on-site virtual store on-line at which their own local customers will shop. FM
calls this their electronic franchise system. That is, under their business model “each franchised store handles and accepts famima club membership registrations from customers. When a customer subsequently purchases an item on the famima.com site, the franchised store that handled the registration is credited with the sale.” (FM 2001) That is, the franchisee gets a benefit when one of their customers shops on-line through that franchisee’s virtual shop. “By combining virtual shopping with physical stores, franchised stores can significantly upgrade their store management capabilities.” FamilyMart’s e-commerce approach therefore differs a bit from those pursued by Lawson and SEJ and it “has submitted a patent application for this innovative business model”. In the case of Lawson and SEJ, the parent companies get the e-commerce related sales in the case of FM it flows to the local franchisee. In this approach FM appears to be the first to extend the franchise system to e- and m-commerce.

Added to this are the in-store multimedia kiosks called “Famiports,” which are manufactured by Toyota and Fujitsu with the system platform developed by a joint venture between Toyota and NTT Data call e-plat. C. Itoh is part of e-plat as a provider of financial services content. Famiport is FM’s own name for e-plat. FM plans to announce in 2002 a broadband service for its multi-media kiosks that will be tied to Toyota’s navigation system allowing people to do things like order tickets while driving and to then pick them up and pay for them at the next FamilyMart store. This is apparently one of the reasons that Toyota has become a shareholder in FamilyMart.com and has invested in the joint venture with NTT Data. It is a natural extension of Toyota’s ITS (Intelligent Transportation System) concept. Another Toyota connection is the fact that while the Internet service is currently available via i–Mode, connection via J-phone, in which Toyota is an investor, is coming

Like SEJ and Lawson FM noted that currently their B2C activity was a direct extension of their third party payment business which last year amounted to 430 billion yen or about one-half of SEJ’s. Like Lawson they have also signed up members for their service and have introduced a point system so that the customer gets 1.4 points for each 100 yen worth of purchases. After a customer has accumulated 1000 points, they can use the points to buy items at FM. So far they have had 500,000 people sign up for the membership since to actually shop on-line and submit an order via Internet phone, PC or kiosk a customer must be a member. A customer can explore offerings on-line or via the kiosks without being a member, but
to order membership is required. For this they get a magazine that offers them opportunities to buy goods
and services on-line.

FM and PIA produce the magazine and are distributing 700,000 copies each month. The major items they
offer like SEJ and Lawson include CDs, video and computer games, books, tickets (PIA), and travel packages
(JTB). According to FM, 480,000 items are available to the 400,000 famima club members throughout Japan (April
2001), which they aim to increase to 2 million by 2003, greatly expanding FM’s reach to its CVS retail customers
as well as their potential customer base.

This e-Commerce payment and delivery scheme in combination with a catalogue available on-line and in
its stores seems quite similar to SEJ’s and Lawson’s. In fact it is not really clear what the fundamental difference is
between FM’s catalogue and those offered by the latter, except FM claims they offer many more items.
Furthermore, the magazine and Internet sales still rely on roughly the same payment infrastructure such as the e-net
group, in which IBM is a shareholder and the systems integrator, and which supports Internet shopping and the
CVS ATMs. Similarly in emulation of SEJ, FM is offering an m-commerce food delivery service to seniors in a tie-
up with a company that already provides such services to seniors but without current on-line capability. “The tie-up
reflects FamilyMart’s determination to make inroads into the highly promising senior citizen market.” (FM 2001)

As of the summer of 2001, 2000 of all Japanese CVS had ATMs using regional banks that were
members of e-net and of these 70% were in FM shops. (The banks working with FM include: Tokyo-
Mitsubishi, Chiba Bank, Dai-ichi Kangyo, Mitsui Sumitomo, Mitsubishi Trust, Nagoya Bank, Michinoku
Bank, Suruga Bank, 105th Bank, and Sumitomo Trust.) This is thus about the same number as they have
installed multi-media kiosks in their stores, about 1500. Unlike Lawson, however, which is nationwide, or
SEJ, which is focused in Osaka and Tokyo, FM is focused in Tokyo and Nagoya, Japan’s third largest city.
This may be one reason for Toyota’s interest since Toyota’s main plant operations and headquarters are
concentrated in the Nagoya area. By the end of 2002, though, the MMKs and ATMs will be in all FM
stores. This is therefore a much faster roll-out than SEJ’s and should allow FM to challenge Lawson more
quickly. Presumably SEJ’s more measured approach is because it must fund its own ATM expansion and
has about twice as many stores. The internal accounting system and data center (or Computer Resource
Center) for all this is located in Yokohama. The MMKs use a Toyota operated central system, which in turn exchanges data with FamilyMart’s central computer system.

In terms of Toyota’s car navigation system communicating with FM’s e-commerce system it works through NTT, which uses the transportation (ITS) linked satellite system. In the future this may be based on Bluetooth, which is a short-range remote-wireless data communication system. The navigation system will then communicate directly with the kiosk in the nearest FM store and the printer function in that kiosk will print out a coupon that will provide a method for connecting and completing the settlement at the CVS.

A logical extension of this payment concept FM is exploring is the idea of issuing its own credit card. Another area is car rental and sales through Toyota. Presently only a new car sales catalogue is available at FM’s shops but Toyota is considering the idea of rentals through some FM locations. In FM’s catalogue Toyota is also promoting its Gazoo website and quizzes about the new Will car aimed at younger drivers with the car as first prize. In addition, customers can use the MMKs to apply for auto and home insurance from Tokyo Fire and Marine, Japan’s largest casualty insurance company and a part of the Mitsubishi group.

Like Lawson sales through its kiosks are not soaring, averaging only about 10,000 yen per day per kiosk as of July 2001. However, sales seem to be growing much faster since FM introduced travel services. So like Lawson and SEJ, FM is still in an early stage of seeing where opportunities are and what works. However, they are committed to the CVS e-commerce model and business opportunity while using the expertise and strength of their e-retsu partners to develop some proprietary initiatives. So they are meeting SEJ’s and Lawson’s competition in form (kiosks, catalogues and ATMs) while looking for their own geographical and service advantage. They summarize this “bricks and clicks” and partnering effort in their 2001 Annual Report: “As we undertake our E-Retail business, we are using the strengths of FamilyMart’s physical stores to support the e-commerce businesses of companies with which FamilyMart has formed tie-ups. Our e-commerce payment collection agency service permits those customers unwilling to provide credit card information on the Internet to make cash payments at any FamilyMart store. FamilyMart’s Open Cash on Delivery (OCOD) Service also allows customers to pay cash for purchases made on the Internet as well as pick up these items at FamilyMart stores. These services, coupled with
Famiport MMKs and ATMs installed in stores, are underpinning FamilyMart’s efforts to attract new customers. In addition, famima.com members are visiting stores to make payments and collect ordered merchandise, which is also fueling an increase in store sales.”

### Basic Financial Data FamilyMart FY1996-2001 (February)

<table>
<thead>
<tr>
<th></th>
<th></th>
<th></th>
<th></th>
<th></th>
<th></th>
<th></th>
<th></th>
</tr>
</thead>
<tbody>
<tr>
<td>Total Store Sales (yen billions)</td>
<td>543</td>
<td>635</td>
<td>710</td>
<td>758</td>
<td>783</td>
<td>843</td>
<td></td>
</tr>
<tr>
<td>Revenue (yen billions)</td>
<td>129</td>
<td>147</td>
<td>151</td>
<td>148</td>
<td>147</td>
<td>176</td>
<td></td>
</tr>
<tr>
<td>Operating Income (yen billions)</td>
<td>19</td>
<td>22</td>
<td>26</td>
<td>27</td>
<td>28</td>
<td>24</td>
<td></td>
</tr>
<tr>
<td>Number Stores</td>
<td>3965</td>
<td>4496</td>
<td>5039</td>
<td>5286</td>
<td>5546</td>
<td>5813</td>
<td>5814*</td>
</tr>
<tr>
<td>Average Daily Sales per store</td>
<td>491</td>
<td>488</td>
<td>486</td>
<td>484</td>
<td>481</td>
<td>478</td>
<td>479</td>
</tr>
<tr>
<td>(yen thousands)</td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Gross Margin (%)</td>
<td>29.0</td>
<td>28.9</td>
<td>29.0</td>
<td>29.3</td>
<td>28.9</td>
<td>28.4</td>
<td></td>
</tr>
</tbody>
</table>


* They expect to open 450 new stores and close 500.
Bibliography and REFERENCES

Amazon, 2001 Annual Report, Amazon 2002
NTT DoCoMo, Corporate Web Site at www.nttdocomo.co.jp.


Seven-Eleven Japan, Brief Summary of Results of FY2001, Seven-Eleven Japan, Tokyo, 2001.


