

CHAPTER 1
JAPANESE DISTRIBUTION:
BACKGROUND, ISSUES, EXAMPLES

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Chapter 1:

Japanese Distribution: Background, Issues, Examples

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Abstract: Prepared as an introductory chapter to a forthcoming book on the distribution sector in Japan, this essay introduces the basic structure of the industry. We note the way competition drives consumers, sellers, and manufacturers to select distributional arrangements that minimize total costs, and the way that this distributional equilibrium will depend both on patterns of consumer demand and on production technology.

To illustrate the way that cross-national distributional practices vary less than often thought, we compare automobile distribution in Japan and the U.S.

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Chapter 1: Japanese Distribution: Background, Issues, Examples

by Yoshiro Miwa and J. Mark Ramseyer

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Call it the bad boy of the Japanese economy. A sultry worker, it refuses to perform at the levels of its manufacturing peers. A sore loser, it stays in business by buying politicians, manipulating bureaucrats, and cheating every which way. A poor player generally, it struts and frets its hour upon the stage -- and then is heard from again and yet again.

Follow the usual intellectual press, and that is pretty much what one reads about the distribution sector in Japan. Take James Fallows, writing for the *Atlantic* in 1994:

Anglo-American economic theory can explain why Japanese prices are so high: the retail system is full of cartels and monopolies. A network of laws, contracts, and commercial agreements in Japan discourages discounting and price competition. Until it was relaxed in the 1990s, Japan's famous *dai ten ho*, or "big store law" effectively outlawed supermarkets...

Outlawed supermarkets? One wonders where Fallows bought his groceries when he lived in Tokyo. Yet to be fair, Fallows is not alone. He does accurately capture the gist of the conventional wisdom about Japanese distribution. The trouble is, the conventional wisdom is wrong -- and in this book the several authors explain how it is wrong.

We use this Chapter 1 to introduce the basic themes in their collective research. We start with a short background to the distribution sector, and then use examples to illustrate several basic points that will recur throughout the book: that firms choose their distribution arrangements subject to constraints imposed by the product they sell -- constraints keyed both to patterns of consumer demand and to manufacturing technology; that notwithstanding those constraints, firms generally retain room for variation and experimentation in distribution; and that superficial differences in distribution across countries can mislead profoundly -- at root, Japanese and American distribution differ less than most observers have noticed.

Structurally, we follow a short overview of Japanese distribution (Section 1) with four short and one quite long non-randomly selected examples. In Sections 2 and 3, we outline the distribution practices for several firms in the apparel, sporting-good, cosmetics, and detergent industries. Through the first two industries, we show how patterns of consumer demand and manufacturing technology can sometimes cause wholesalers to integrate either backward into production or forward into retailing. Through the last two, we show how those constraints imposed by demand or technology can still leave firms room to experiment with alternative distribution arrangements. In our much longer Section 4, we use the distribution arrangements in the automobile industry to illustrate the way Japanese and U.S. distribution practices may differ less than usually thought. Like the other authors in this book, we focus on empirics and keep the theoretical apparatus to a minimum.

1. INTRODUCTION

1.1 *Background*

Critics may see the Japanese manufacturing sector as modern and productive, but they routinely dismiss the rest of the economy as obsolete. The distribution sector they dismiss as egregiously so. If they have the story right, consumers incur huge costs. Suggestive evidence of such costs is easy to find (as Fallows' comment reflects). In Table 1.1A, we reproduce a recent survey of price differentials among several cities. By these numbers, food in Tokyo is 77 percent more expensive than in New York, and nearly double the price in London. Apparel similarly costs nearly twice as much as in New York or London. Because price comparisons depend heavily on volatile exchange rates, in Table 1.1B we use purchasing-price-parity measures to compare factor productivity. Given the limited data available we examine real value-added in 1987, but the conclusion is just as stark: in distribution, Japanese productivity is half that of the U. S. and Germany.

According to many observers, not only Japanese consumers but foreign manufacturers suffer too. Through the early 1990s Japan imported "usually" low volumes of finished goods, they explain, and much of the reason lay in the distribution sector. Only through draconian barriers against competition did the obsolete distributors manage to stay in business. With 18 percent of total employment (1994), by staying in business they wasted human resources on a massive scale.

Table 1.1: Distribution Costs

A. Prices in Tokyo Relative to Selected Cities, 1995

	New York	London	Paris	Geneva
Total	1.59	1.52	1.34	1.02
Food	1.77	1.99	1.78	1.24
Durable Goods	1.47	1.15	0.94	0.93
Apparel, Shoes	1.93	1.81	1.50	0.93

Note: Exchange Rate -- Annual average. \$1 = 94.06 yen, £1 = 148.47 yen, 1 franc = 18.84 yen, 1 Swiss franc = 79.54 yen.

B. Productivity in Distribution (Purchasing Power Parity)

	Labor Productivity	Total Factor Productivity
Germany	0.96	0.97
U. K.	0.82	0.86
France	0.69	0.71
Japan	0.44	0.55

Note: 1987 -- U.S. = 1.

Source: Panel A -- Economic Planning Agency, ed., *Price Report* table 3-1-2 (Tokyo: Economic Planning Agency, 1996); Panel B -- McKinsey Global Institute, ed., *Service Sector Productivity* (Washington D. C.: McKinsey Global Institute, 1992).

1.2. *Issues*

Observers have suggested several cumulative reasons for these phenomena. At the outset, many argue that Japanese wholesaling contains too many levels. In moving from manufacturer to retailer, they note, a product can travel through primary, secondary, and tertiary wholesalers. In the process, they continue, it will accumulate massive wholesale margins. If eventually sold through one of the many small stores, it will incur high retailing costs besides.

In competitive markets, of course, such a system would not survive. If wholesalers and retailers acted inefficiently, other firms (including foreign firms) could earn large profits by replacing them. For the inefficient firms to survive (and for foreign firms to stay out), some aspect of the Japanese institutional framework must exclude more efficient rivals.

To “solve” this logical problem, analysts jumped on the Large-Scale Retail Stores Act. The Act imposed costly barriers against new large retailers. Clearly, it raised consumer prices (as discussed by Tsuruta and Yahagi in Chapter 6, and by Nishimura, Tachibana and Tsubouchi in Chapter 2). Just as clearly, it excluded large foreign *retailers*. What is less clear is why it would have excluded foreign *products*.

One potential explanation lay with the “keiretsu.” Japanese manufacturers, some observers explained, excluded foreign manufacturers by locking up existing distributors in their keiretsu. Through these networks, they maintained extraordinarily opaque relationships characterized by customary norms involving trade support, price concessions, return policies, and even seconded employees. Through these networks, they imposed contractual terms that excluded rivals foreign and domestic.

Alas, all this still did not a competitive equilibrium make. Saying that incumbent politicians increase their electoral odds through inefficient industrial policy is one thing. Saying that manufacturers in competitive markets increase profits through inefficient distribution systems is quite another. Suppose one electrical appliance manufacturer locked up a set of retailers in its network of dedicated small stores. A new entrant could not sell through those retailers, granted. It could still sell through existing large stores -- which, after all, were never part of a distribution keiretsu. It could also do what the incumbent did, and simply build its own network of small stores.

Given these logical problems, the various authors to this volume propose alternative, more straightforward explanations for Japanese distribution practices. Depending on the industry, for example, any apparent inefficiency may be a transitional phenomenon; may misdescribe the facts; may reflect different consumer preferences in Japan; may reflect attempts structurally to mitigate agency problems in distribution; or may reflect technological constraints in manufacturing. This book is about those many alternatives.

2. CONSUMER DEMAND AND EFFICIENCY¹

2.1 *Apparel*

Distribution is not a service independent of the products distributed. Instead, it depends fundamentally both on consumer demand patterns and on the manufacturing technology involved. To see this, take a representative firm -- call it A Co. -- in the apparel industry. Although primarily a wholesaler, A is much more. On the one hand, it has integrated backward into manufacturing. To be sure, it still buys apparel other firms have made at their own initiative. Yet it also commissions products that it thinks will sell, and makes some items on its own. On the other, it has partially integrated forward into retail. Of its 9,000 employees, it has seconded many to assorted retailing firms that handle its products.

Suppose, hypothetically, that foreign firm F decided to compete with A. Toward that end, it approached one of the department stores where A sold its goods. It asked the store to handle its goods as well. What would F Co. likely find? Primarily, it would find the department store maddeningly obtuse. First, because A Co. sold its products on consignment, it would find that the department store could not evaluate merchandise. It

¹ The examples below are based both on publicly available data and on interviews with company personnel.

had no capacity to evaluate because it had little need for one. A sent its products on consignment, and even supplied the sales force. Fundamentally, A rather than the department store bore most of the business risk involved.

Second, F Co. would find the department store extremely demanding. Given that the store would likely want F to offer the merchandise on consignment too, it would promise no minimum purchases. It would demand that F Co. take back unsold merchandise. It would expect F Co. to provide much of the sales force.

Because it lacked the skill to judge F Co.'s unfamiliar merchandise, suppose the department store demanded that F work through a wholesaler. To F Co., the distribution system would now seem multi-tiered and needlessly inefficient. Given that A Co. would still be selling directly, it would also seem biased against foreigners.

Turn then to representative firm B Co., a firm that makes designer-label clothing for young women. Begun as a buyer for clothing manufacturers, in the late 1970s it moved into the designer-label business in the market for young women's apparel. By 1990, it ran a chain of 600 retail shops, employed 1,200 workers, and had sales of 40 billion yen on 14 labels. A had sold to a broad range of retailers. By contrast, B sold through its own network of dedicated retailers.

B succeeds because its vertical integration speeds the transmission of market information from consumer to producer. Speed matters because of the peculiarities of this segment of the apparel market. Given the short lifespan for products in the young women's apparel market, apparel firms cannot use the past sales to determine future production. By the time they learn whether a given product sold, consumers have moved to something else.

Accordingly, firms survive in this submarket only if they can translate consumer demands into production more rapidly than their competitors. B Co. integrated into manufacturing and retail precisely to increase that speed. A had not, because it competed primarily in submarkets where change proceeds more deliberately.

2.2 *Sporting goods*

Now take C Co., a sporting goods manufacturer. Although nominally a wholesaler, like A Co. C develops and produces its own products. It sells primarily to a single chain of 230 retailers.

C integrated backward into manufacturing for reasons close to those that led B to integrate forward into retailing. Traditionally, manufacturers in this industry independently decided what to produce. Wholesalers then chose from among those products the goods they thought they could sell to retailers. In this environment, a wholesaler might well know best the goods local consumers wanted, but it would have no ready channel by which to induce a manufacturer to supply them. By integrating backward, C could respond more quickly to consumer demand.

Note, however, the implications of these discussions for assessing efficiency. Given the retail market constraints in the industries involved, distribution channels could not plausibly stay inefficient. Any firm that relied on an inefficient distribution network would simply -- and promptly -- go out of business.

3. DISTRIBUTION VARIETY AND EXCLUSION

3.1 *Cosmetics*

In the cosmetics industry, firms making similar products use very different distribution channels. Some firms maintain their own exclusive distributors who sell to non-exclusive retail chains: Shiseido, Kanebo, and Max Factor. Shiseido, for example, employs about 5,000 workers in R&D and production. Yet, it additionally operates twelve distribution subsidiaries that collectively employ 15,000.

Other firms sell door-to-door through their own sales force: Pola, Menado, and Noevia. Still others sell through general wholesale and retail channels: Kao, Lion, Mandom, and Kiss-me. Although one could (and some observers do) try to distinguish among the firms by clientele, one can exaggerate the distinctions. Largely, the cosmetic firms sell interchangeable products. Crucially, they distribute them through fundamentally different channels.

3.2 *Detergents*

If some observers try to partition the cosmetics market by clientele, no one does for detergents. Yet here, too, manufacturers selling interchangeable products distribute them in radically different ways. Three major producers compete in the market: Kao, Lion, and Proctor & Gamble. They sell their products through 300,000 retail stores.

Each of the three producers uses its own distribution scheme. Kao distributes to retailers through a distributor who handles only Kao products. Lion and P&G sell through wholesalers who handle a variety of household products. Lion, however, sells to some 300 primary distributors who then sell to 1,400 secondary distributors. P&G simply focuses on 50 distributors.

Note now the implications this poses for claims about exclusion. Most basically, these radical distributional differences make any talk about the distribution system excluding foreign manufacturers a non-starter. In an industry like cosmetics or detergents, the distribution sector could not plausibly exclude -- for firms can too easily circumvent existing channels.

4. DECEPTIVE DIFFERENCES: AUTOMOBILES

4.1 *Introduction*

As in many other discussions of the Japanese economy, observers of the Japanese car industry have focused less on function than on form. They focus less on those functional attributes to distribution. They focus more on apparent Japanese peculiarities. They focus less on the common problems that manufacturers and dealers everywhere face. They focus more on the way Japanese distribution channels exhibit apparent idiosyncrasies.

In fact, U.S. and Japanese automobile distribution practices resemble each other closely. That they do should not surprise. In both countries, the industry involves similar manufacturing technology and similar consumer preferences. The distribution sector simply ties that technology to those preferences. To be sure, the technology is not identical. If Toyota sells a car it makes in Aichi to a New York consumer, it cannot produce the car to order and deliver it in 10 days. If it sells the car to an Osaka consumer, it can. Neither are consumer preferences identical. A suburban St. Louis consumer who

uses a car for his 20-mile daily commute may want a different car from a Tokyo businessman who uses it for family outings on Sunday.²

In the rest of this Chapter 1, we use generally available data and simple micro-economic logic to show the essential similarity between U.S. and Japanese automobile distribution practices. We start by surveying the U.S. (Section 4.2) and Japanese markets (Section 4.3), and describing how one buys a car in Japan (Section 4.4). We then turn to four common misperceptions about Japanese automobile distribution (Section 4.5).

4.2 *Foreign cars in the U.S.*

The automobile industry has been a major part of the U.S. economy, and it has not been doing well. The problems were a long time in coming. American consumers began their switch to foreign cars with the Volkswagen beetle in the 1960s. In 1960, Americans had bought 444,000 imports. By 1970 they bought 2.0 million.

Unable to replicate the success of the aging bug, Volkswagen began to wane by 1970, but Toyota, Nissan, and Honda continued where it stalled. As of 1960, Japanese manufacturers produced 165,000 passenger cars, and exported (to any country) only 7,000. By 1970, they produced 3 million passenger cars and sold 312,000 in the U.S. -- 3.7 percent of the American market. By 1980, they had 19.8 percent of the American market, by 1990 27.8 percent, and by 1998 31.9 percent.³

4.3 *Foreign Cars in Japan*

Early years. Although U.S. car makers had dominated the Japanese automobile market before World War II, when they returned after it they found a different reception. Throughout much of the 1950s and early 1960s, they faced formidable import and foreign-exchange restrictions. By 1965 the last of those barriers had disappeared (Shinomiya, 1998: 241), but outside the commercial vehicle sector the restrictions had probably been redundant anyway. Most Japanese simply lacked the money to buy cars of any sort. Much less did they have the money to buy the relatively expensive cars from the U.S. (Table 1.2A).

Of the cars that Japanese consumers did buy in the early 1960s, many would have shocked American visitors.⁴ Where the typical U.S. sedan sported a 4,000 cc (250 cubic inch) six-cylinder engine and weighed 3,000-5,000 pounds, Japanese consumers turned to

² Reflecting those different preferences and more, in 1999 Toyota manufactured in Japan 52 models but sold in the U.S. only 20 (Toyota, 2000: 24). It offered Japanese Corolla buyers a choice among 1,300 cc, 1,500 cc and 1,800 cc engines, but sold in the U.S. only the 1,800. It produced 121,000 Siennas in 1999, but offered Japanese consumers none. In turn, Honda offered Japanese consumers both a small (called the Odyssey) and a large minivan (the Lagreat), but sold only the large (still called the Odyssey) in the U.S. And so one could continue, producer after producer.

³ Watanabe (1999: 12, 14, 16). Note that even in 1998 the Japanese manufacturers were not primarily "export-oriented." Their principal market remained Japan. That year, they produced 8.1 million passenger cars, but exported only 3.7 million globally. They sold 2.6 million in the U.S. *Id.*

⁴ Prior to the mid-1950s, most Japanese automobile production had been oriented toward the taxi market. Toyota introduced the Crown, however, for the passenger market in the mid-1950s. Both it and Nissan self-consciously targetted the full-size (albeit much smaller than U.S. full-size cars) market, while companies like Subaru entered through the "light" car market.

800-pound micro-cars with what were essentially 360 cc (22 cubic inches) two-cylinder (often two-stroke) motorcycle engines.

The Japanese government had long offered various regulatory advantages for these “light” cars. In the late 1960s, it capped “light” car engines at 360 cc; today it caps them at 660 cc (Tsuji, 1990: 104-06). Since the early 1960s, however, the fraction of cars catalogued as “light” has held constant at about 15-25 percent of the market: 97,000 of the 587,000 passenger cars sold in 1965, and 947,000 of the 4.1 million sold in 1998 (Watanabe, 1999, 324).

Later changes As Japanese grew richer, they did eventually buy more and bigger cars, but not the ones Detroit wanted to sell. In 1970, they constituted the second largest automobile market in the world. They bought 2.4 million passenger cars (compared to 8.4 million in the U.S.; Table 1.2A), but only 19,000 foreign passenger cars (less than 1 percent of the market). By 1980, they bought increasingly bigger cars, but still only 46,000 foreign cars (1.6 percent of the market). This combination of loyal domestic consumers and a growing export market made cars an important part of the Japanese economy, and there it has remained: 7-13 percent of aggregate manufacturing production, and 5-8 percent of manufacturing employment (Table 1.2D).

Nor did foreign exchange shifts do much to help U.S. producers. From 1984 to 1987, the dollar plummeted from 251 yen to 125. One might have thought (and many observers did think) Japanese consumers would now buy foreign cars. Not so. By 1990 they still bought only 251,000 imported cars (4.9 percent of the market), and by 1998 only 269,000 (6.6 percent; down from 439,000 in 1996).

German cars. To make matters worse for Detroit, when Japanese consumers did begin to buy foreign cars, they did not buy from the big three. In 1990, 62 percent of the imported cars came from Germany, and only 13 percent from the U.S. Of the latter, nearly half were the U.S.-made cars produced by Japanese firms (Nomura & Booz, 1994: VII 10). Nor was this likely to change anytime soon. In one 2000 consumer survey of 700 potential buyers, the BMW 5-series came in as the most desired import; the 3-series came in second. Various Mercedes Benz, Volvo, Jaguar, and Volkswagen models rounded out the top-10 list -- but no cars from Detroit (Nihon keizai, 2000).

German producers have done well in Japan. In 1998, Japanese consumers bought only 25,383 GM cars, 8,800 Chryslers, and 5,300 Fords. Yet they bought 50,500 VWs, 40,000 Mercedes Benz, and 30,200 BMWs.⁵ During the same year, VW imported 86,800 cars to the U.S., Mercedes imported 127,100, and BMW imported 110,946. Given that the U.S. passenger car market is twice that of Japan (Table 1.2A), VW effectively had 1.16 the market penetration in Japan that it had in the U.S., Mercedes had .63, and BMW .54.⁶

⁵ And 23,800 cars produced in the U.S. by Japanese manufacturers. Toyota (2000, 72).

⁶ If one adjusts market penetration by total new vehicle sales rather than new passenger cars (16.0 million in the U.S.; 5.9 million in Japan), VW has 1.58 the market penetration in Japan that it has in the U.S., Mercedes has .86, and BMW has .74. The current popularity in the U.S. of SUVs (classed as light trucks) arguably makes the focus on total vehicles more appropriate than passenger cars.

Table 1.2: Automobile Industry -- Selected Statistics

A. *Passenger Car Purchases (x 1000 units)*

	Japan	U.S.	Germany	France	U.K.
1960	145	6,577	970	639	820
1970	2,373	8,388	2,107	1,297	1,127
1980	2,854	8,761	2,426	1,873	1,514
1990	5,102	9,103	3,041	2,309	2,009
1998	4,093	8,142	3,736	1,944	2,247

B. *Passenger Car Production (x 1000 units)*

	Japan	U.S.	Germany	France	U.K.
1960	165	6,703	1,817	1,116	1,353
1970	3,179	6,550	3,528	2,245	1,641
1980	7,038	6,376	3,521	2,939	924
1990	9,948	6,077	4,661	3,295	1,296
1998	8,056	5,554	5,348	2,582	1,748

C. *Passenger Car Imports into Japan:*

	Total Imports	% of Purchases
1960	3,500	2.4
1970	19,000	0.8
1980	46,000	1.6
1990	251,000	4.9
1998	269,000	6.6

D. *Automobile Industry*

	Share of Japanese Industrial production	Share of Japanese Industrial employment
1965:	7.5 percent	5.0 percent
1975:	8.1	5.3
1985:	11.9	7.0
1995:	12.9	7.5

Sources: Tsuyoshi Watanabe, *Jidosha sangyo hando bukku 2000 nenban [Automobile Industry Handbook, 2000]* 14, 62, 234, 222, 214-15 (Tokyo: Nikkan jidosha shimbun sha, 1999).

4.4 *Buying a Car in Japan*

Consumers buy cars somewhat differently in Japan than they do in the U.S. In the U.S., the manufacturer produces cars with the specifications that match the demand it expects. It sends the cars to its franchised dealers. They in turn stock them in massive parking lots. The quintessential consumer then visits several dealers, probably pretends to know more than he does, drives a few cars around the block, haggles over price, obtains a loan, and drives his new purchase home.

Japanese consumers do sometimes buy from inventory. They do sometimes visit showrooms. Yet quintessentially the consumer does none of this. Instead, about 60 percent of the time he buys a car from a salesman who visits him at home (Morita & Nishimura, 2000: 16). Fully half the time, moreover, he does not buy from inventory.⁷ Instead, he chooses the model, color, and options he wants. The dealer sends the order to the manufacturer by computer; the manufacturer relays the order to the appropriate factories; the factories incorporate it into their production plans; and the car arrives in a week or two.

All this has several obvious implications for distribution. Most obviously, dealers stock fewer cars. Japan being the size of California, even the furthest point is an easy haul from a domestic Nissan or Toyota factory. If consumers can obtain exactly the car they want from the factory in 10 days, dealers have less reason to fill parking lots with cars made on spec. A Toyota outlet in Tokyo might have as few as 3 cars in stock; an outlet with more space might have 5-6. Consumers are also less likely to comparison-shop before they buy the car. With less information, they are more likely to pay suggested retail.

This distributional process involves more than the dealer. Before a consumer can order a car, he must know about it. Toward that end, someone must determine what sort of car what sort of consumer is likely to want. Someone must translate that information about consumer preferences into automobile design. Once designed, someone must advertise the car. Someone must produce the requisite dealership pamphlets. Someone must approach the customer and see that he obtains the information.

Once a customer orders a car, the manufacturer must produce it. Toward that end, someone must translate his order into sub-orders for the requisite parts. Someone must assemble those parts. Someone must contact the consumer and tell him when he can expect the car. And someone must eventually haul the car back to the dealer.

All this is distribution, yet all this involves far more than the dealer upon whom most discussions of distribution turn. Here as with the examples earlier, the producers that thrive are the producers who effectively monitor distribution. They are the producers who use distribution most effectively to learn consumer preferences and translate them into production.

4.5 *Automobile Distribution in Japan and the U.S.*

Introduction. In cross-national comparisons of automobile distribution, observers commonly propose several stereotypes about Japan:

⁷ The industry mean is deceptive. A much higher fraction of high-end cars are made to order than low-end. Of all 12,000 Celciors (base price: 5.4 million yen) ordered in September 2000, for example, fully 7,000 were individually spec'ed. Of all 17,000 Corollas (base price: 1.1 million yen), only 400 were.

- (a) Japanese dealerships are bigger than U.S. dealerships;
- (b) Japanese dealerships have relationships with the manufacturer that are more exclusive than do U.S. dealerships;
- (c) Japanese dealers typically bundle with the cars they sell a larger package of services than U.S. dealers; and
- (d) Japanese dealers maintain longer-term relations with manufacturers than U.S. dealers.

Although superficially true, these generalizations also badly mislead. In the rest of this chapter, we discuss some of the ways they do.

Preliminarily, note that as of about 1990 nine Japanese car makers sold their cars through 3,800-odd franchised dealers (3,148 dealers in 1999). These dealers sold 3.8 million units through their own outlets. They sold another 680,000 to some 60,000 independent outlets who sold the cars to the public. These independent dealers act as agent for the customer, and obtain the car the customer wants from the car's authorized dealers. Out of deference to Japanese industry practice, references in this chapter to "dealership" include only the authorized dealers, and exclude these 60,000 independent outlets (Nomura & Booz, 1994: III 4-5).

As of about 1990, foreign producers sold their cars through 36 importers, who in turn sold to 600-odd franchised dealers maintaining 1000-odd outlets. Total sales through this route came to 120,000 units. In addition, 2,000 parallel importers bought directly overseas, by-passed the authorized dealers, and sold another 23,000 units (Nomura & Booz, 1994: III 4-5).

Size. Typically, U.S. dealerships have been small. They are still smaller than Japanese dealers, though the smallest have been steadily disappearing. In 1970, there were 30,842 franchised new-car dealerships in the U.S. selling 8.4 million passenger cars.⁸ By 1980, only 27,900 dealers remained, and by 1998 only 22,600 (selling 8.1 million passenger cars; 16.0 million total vehicles). More to the point, from 1980 to 2000, the number of dealers selling fewer than 150 units fell from 10,602 to 4,161. During the same time, the number selling 750 or more units a year climbed from 3,906 to 5,896 (NADA, 2000: p. 7).

By contrast, Japanese dealers traditionally have been large. Manufacturers began the 1950s with few dealers, and often assigned each an entire prefecture (there are 47 prefectures in Japan). As the market for passenger cars grew, those dealerships added outlets, but the manufacturers only sporadically added dealers.

When Japanese manufacturers did add dealers, they rarely shrank the geographical scope they assigned the existing dealers. Neither did they introduce directly competing dealers in the same territories. Instead, they did what Honda did when it introduced Acura in the U.S. or -- more obviously -- what GM did with Chevrolet and Cadillac: they segmented the market by product line (Table 1.3A).

For example, in the 1950s when Toyota sold almost no cars, it already had multiple dealership networks. As sales grew through the 1970s, it steadily added dealers (Table 1.3B). Since 1980 the number has held relatively constant. As of 1999, Toyota and Nissan both had five lines of dealers (309 Toyota dealers and 196 Nissan dealers).

⁸ 10.2 million total vehicles. Shinomiya (1998: 260); Watanabe (1999: 222).

Mitsubishi (294 dealers), Isuzu (75 dealers), Mazda (777 dealers; recognizing its over-capacity it was trying to consolidate), and Honda (1,098 dealers) each had three lines.⁹

Although U.S. dealers are smaller than Japanese dealers, the comparison fundamentally misleads. If a U.S. “dealer” does not much resemble a Japanese “dealer,” it does resemble a large Japanese “outlet.” In 1998-99, the 22,400 dealers in the U.S. on average used 48 employees to sell 363 passenger cars (712 vehicles). In 1998, 17,242 Japanese outlets on average used 21 employees to sell 237 passenger cars (341 vehicles). A U.S. dealer is much smaller than a Japanese dealer, but a bit larger than a Japanese outlet.¹⁰ One could restate the contrast in terms of different patterns of integration: in the U.S., the dealer performs only retail services, while the manufacturer has integrated forward into wholesale; in Japan, the manufacturer performs only production, while the retailer has integrated backward into wholesale.

Unfortunately, modest differences in contracting customs fog the data. In the U.S., manufacturers typically use outlet-specific franchise agreements. As a result, a successful U.S. dealer who opens a second outlet will often negotiate a separate franchise agreement (Nomura & Booz, 1994: III-7) -- and appear in the data as two dealers. A successful Japanese dealer who opens another outlet would remain in the data as one dealer.

In any event, there is nothing necessary about these practices. Just as the three detergent makers discussed earlier each use radically different distribution patterns, an automobile manufacturer in Japan could -- if it wanted -- use U.S.-style distribution patterns. Such was exactly the strategy Honda used when it transformed itself from a motorcycle company into a major automobile producer. As Honda began making cars in the mid-1960s, it largely sold them through its existing dealers. Many of these had begun as motorcycle shops. To recruit dealers who would focus exclusively on cars, in 1978 Honda opened a series of 89 “Verno” dealerships. Except for one Kobe dealer with two outlets, each of these dealerships had one outlet. Of the 63 dealerships on which information survives, 50 had exactly 10 employees. Although by 1988 the majority of the Verno dealerships had been successful enough to open multiple outlets, they still remained smaller than Toyota and Nissan dealers (Nikkan, various years).

⁹ Nikkan (1999: 468). This includes the somewhat idiosyncratic Honda Primo (922 dealers, 1,441 outlets, 17,500 employees) and Mazda Autozam line (650 dealers, 704 outlets) of dealers.

¹⁰ Watanabe (1999: 222); NADA (2000: 7); Nikkan (1999: 486). For reasons of data availability at the time of writing, we were forced to couple 1999 dealership data and 1998 sales data for the U.S.

Table 1.3: Toyota Dealerships

A. *Product Lines:*

Products	1980			1991			1999		
	D	O	E	D	O	E	D	O	E
Toyota Century, Crown, Carina	50	674	50	946	26,026	50	1,091	31,304	
Toyopet Mark II, Corona, Corsa	52	794	52	1,015	30,879	52	960	25,579	
Corolla Celica, Camry, Corolla, Tercel	82	1,098	77	1,265	31,787	75	1,335	33,366	
Auto Chaser, Sprinter, Starlet	69	779	66	925	20,251	66	972	20,535	
Vista Cressida, Camry, Tercel	66	237	66	604	10,525	66	653	11,180	

Note: D = Dealerships; O = Outlets; E = Employees

B. *Change in Numbers of Dealerships Over Time:*

	1950	1952	1954	1956	1958	1960	1962	1964	1966	1968	1970	1972	1974	1976	1978	1980
Toyota	47	47	49	49	49	49	49	49	49	49	49	50	50	50	50	50
Toyopet			1	40	51	51	51	53	53	52	52	51	51	51	51	52
Diesel					9	9	9	9	11	11	4	3	2	2	2	1
Corolla							56	65	86	80	84	82	83	82	82	81
Auto										45	62	66	67	67	67	69
Vista																66
Total	47	47	50	89	109	109	165	176	199	237	251	252	253	252	252	319

Sources: Nomura sogo kenkyu jo & Booz Allen & Hamilton, *MOSS jidosha chosa saishu hokoku sho* [Final Report for the MOSS Motor Vehicle Study] IV-10 (unpublished manuscript, 1994); Toyota jidosha hanbai, ed., *Sekai e no ayumi* [Steps Toward the World] 40 (Nagoya: Toyota jidosha hanbai, 1980); Nikkan jidosha shimbun sha & Nihon jidosha kaigi sho, eds., *Jidosha nenkan* [Automotive Yearbook] 486 (Tokyo: Nikkan jidosha shimbun sha, 1999).

Bundled Services. (i) Maintenance. -- By tradition, Japanese dealers are said to bundle a larger package of services with the cars they sell than American dealers do. In the U.S., a consumer faces almost completely different sales and repair staff. He buys the car from the former, and takes it for maintenance and repairs to the latter. In Japan, by contrast, the salesman was traditionally said to intermediate all subsequent services.

For example, when a customer finds that his car needs scheduled maintenance, unanticipated repairs, or mandatory inspections, traditionally he approached the man who made the initial sale. That salesman then arranged the necessary work. When the consumer bought a new car, the same salesman arranged the trade-in. Even contractual structure was said to reflect this practice: U.S. dealers rewarded sales, but Japanese dealers paid their salesmen by rank and experience (Shimokawa, 1997: 224).

(ii) Some doubts. -- And yet, this contrast raises an obvious question: why would these differences in service quality exist? Observers typically posit radical differences in consumer characteristics: Americans are more likely to see cars as everyday tools (and therefore prefer a lower price even if with less service), where Japanese more often see them as status-marking luxury goods (and therefore value the pandering at the shop); Americans know more about cars (and thus need less intermediation), where Japanese know less (and thus want more help at the shop); and so forth.

Still, to the extent that consumers in the U.S. and Japan differ along these dimensions, they differ at the mean. In both countries they exhibit large variations.

Many Americans see cars as status-marking toys (why else buy an SUV from Mercedes Benz?), and many could never find a spark plug (or would look for one in a diesel). Some would not even know how to open the hood. Many Japanese (particularly outside Tokyo) use their cars for daily commutes. Many (particularly young males) could and do perform routine maintenance on their own.

Given this *intra*-national variation in consumers, basic logic suggests that we should see substantial *intra*-national variation in dealership practices. In both countries, we would expect some dealers to price low and service cursorily, while others price higher and bundle better service. Consumer differences may lead to differences in the relative prevalence of the different dealership types, but they should not lead to corner solutions.

(iii) *Service variation across brands.* -- Stereotypes notwithstanding, this *intra*-national variation in service quality is exactly what one sees. As a rough proxy for service quality, consider the number of customers a dealership employee must service. The proxy is obviously imperfect, but the higher the number of cars sold per employee, the less time each employee will have to care for a customer.¹¹ As Table 1.4A shows, the vehicle-sales/employee figure varies widely across manufacturers -- from 11-13 at Nissan and Toyota, to 25-50 at Subaru, Daihatsu, and Suzuki.

Crucially, the variation in service quality correlates with the quality of the cars sold. In general, one would expect the demand for high-quality service to correlate with the demand for high-quality automobiles. Although each manufacturer sells a variety of models, one basic index of average quality is the fraction of cars at the cheapest end of the spectrum -- the “light” cars. Toyota and Nissan sell no such cars, while Daihatsu and Suzuki sell almost nothing else.

Table 1.4B gives the correlation between the fraction of its production a manufacturer devotes to light cars (Light/Total) and the number of cars sold per dealership employee (Vehicles/Employee). At .89, the correlation is extremely high: the more a company specializes in the very cheapest cars, the fewer employees it uses to service its customers.

Table 1.4C reiterates the point. The table divides dealers according to the principal cars they sell, by four descending price categories -- large cars, mid-sized & compact cars, “mass market” cars, and light cars. In 1998, profits/sales did not monotonically vary either by price or by sales/employee. Both the number of cars sold per employee and employee wage, however, did vary by automobile quality: as car quality dropped, the number of cars sold per employee increased, while employee wage fell. As we move from the better to the cheaper models, in other words, customers find fewer people to help them, and the people they encounter are less able.

(iv) *Intra-brand service variation.* -- The same correlation between product and service quality appears within firms. Contrast the high-end “Toyota” dealerships with the middle-market “Corolla” dealerships (see Table 1.2.A.). “Toyota” dealers use an average 29 employees per outlet, while “Corolla” dealerships use 25 per outlet. Although we do

¹¹ Of the 177 employees at the mean Japanese dealership in 1998, 65 were in sales, 55 in repair, and 57 in other positions. Nikkan (1999: 533).

not have exact sales per dealership line, we use sales of the various models to estimate dealer sales.

The resulting back-of-the-envelope calculations again suggest that service quality correlates with product quality. On average, the premium “Toyota”-line employees sell 7.3 cars annually. By contrast, the mass-market “Corolla” staff sell an average 11.2 cars annually.¹² The implication is the same: the dealers who sell premium cars bundle them with high-quality service; the dealers who sell cheaper cars bundle them with lower-quality service.

¹² Calculated by excluding sales of models sold by other dealership lines. If one includes such cars, the figure is 12.2 per employee. for the “Toyota” dealers, and 14.3 for the “Corolla” dealers. Watanabe (1999, 123); Toyota (2000).

Table 1.4: Service and Automobile Quality

A. *Sales, Employees, Outlets:*

	Total Sales	Light Total	Vehic . Employee	Vehic. Outlet
Toyota	1664483	0	13.6	332.2
Nissan	773651	0	11.4	254.6
Honda	705902	.41	21.2	306.2
Suzuki	619213	.94	49.6	958.5
Mitsubishi	585707	.47	14.7	748.0
Daihatsu	522524	.98	35.7	754.0
Mazda	315260	.15	15.1	171.2
Subaru	302064	.59	24.6	546.2

B. *Correlation Coefficients:*

	Total Sales	Light Total	Vehic . Employee	Vehic. Outlet
Total Sales	1.000			
Light/Total	-.469	1.000		
Vehic/Emp	-.274	.888	1.000	
Vehic/Otlt	-.212	.861	.784	1.000

D. *Sales per Employee by Size of Primary Vehicles Sold in Store, 1998:*

	Large	Mid-size & Compact	Mass Market	Light
Vehic sales/Employee (monthly units)	0.6	1.5	1.6	2.8
Wage/Employee (monthly, x1000 yen)	376	362	335	333
Profits/Sales	13.1%	15.4%	16.2%	14.5%
Sales/Employee (monthly, x1000 yen)	5,133	4.292	3,518	4,267

Notes: By Japanese regulation, a light car has 660 cc-or-less displacement, and meets assorted size requirements. By custom, a mass-market car is a low-end compact with about a 1,000-1,500 cc engine and a price of 700,000-2,000,000 yen -- the Toyota Corolla and Nissan Sunny are typical examples. See Kosei (1992: 143).

Sources: Nikkan jidosha shimbun sha & Nihon jidosha kaigi sho, eds., *Jidosha nenkan [Automotive Yearbook]* 486, 530-31 (Tokyo: Nikkan jidosha shimbun sha, 1999); Toyota jidosha, *Toyota no gaikyo, 2000 [An Outline of Toyota, 2000]* 69 (Tokyo: Toyota jidosha, 2000).

(v) *Service variation across countries.* -- Return, then to the central cross-cultural stereotype: Japanese dealers offer higher quality service than U.S. dealers. Is this true? Intra-national variation aside, is average service quality higher in Japan than in the U.S.? Consider again the number of cars sold per employee. In Japan, in 1998 the 355,000 employees of franchised dealers sold 5.9 million vehicles -- 16.57 vehicles per employee. In the U.S., in 1998 the 1,081,000 employees of franchised dealers sold 15,971,000 total vehicles -- 14.77 vehicles per employee.¹³

If anything, the basic figures suggest Japanese dealers provide *lower* quality service than U.S. dealers. We will not push the argument that far. We recognize that cars/employee figures only imperfectly proxy for service, and (for reasons discussed below) U.S. consumers may need more repairs per car than Japanese consumers. Nonetheless, the fact remains that a customer at a Japanese dealer will find fewer people to help him than a customer at a U.S. dealer.

Dealership revenues add a curious twist to this discussion: Japanese dealers rely more on new car sales, while U.S. dealers rely more on parts and service. According to Table 1.5 (the revenues and mean value-added at Japanese and U.S. dealers), Japanese dealers generate a higher portion of their total dealership value-added through new car sales (44.4 percent) relative to later service (46.0 percent), than U.S. dealers do (30.2 percent through new cars; 39.5 percent through parts and service). Analogously, dealership value-added is a higher fraction of new car revenues in Japan than in the U.S. (9.6 percent compared to 6.4 percent); it is a lower fraction of parts and service in Japan than in the U.S. (35.4 percent compared to 44.5 percent).

One could posit several alternative (or overlapping) explanations for this. Without purporting to test them against each other, we outline them here. First, perhaps Japanese dealers simply provide less service. After all, as discussed above they do have fewer employees per car sold.

Second, perhaps U.S. dealers provide more parts and service because U.S. consumers drive older cars. After all, North American drivers do own 14.3 times as many cars as they buy each year, while Japanese drivers own only 10.4 times as many (Watanabe, 1999: 4-7). Because of the draconian inspection requirements, Japanese drivers take cars off the road earlier than Americans do, and -- rumor has it -- ship them to Vladivostok.

Last, perhaps Japanese dealers bundle more “after-care” service with the initial purchase. Perhaps both dealers provide comparable service in other words, but in Japan the dealer charges for the later service at the time of the new car purchase. In the U.S. he charges for the car and service separately.

¹³ Japanese dealers sold 4.1 million passenger cars -- or 11.54 passenger cars per employee. U.S. dealers sold 8.1 million passenger cars -- or 7.53 passenger cars per employee. Watanabe (1999: 222) (car sales); Nikkan (1999: 486) (Japanese employees); NADA (2000) (U.S. employees). For reasons of data availability at the time of writing, we were forced to couple 1999 dealership data and 1998 sales data for the U.S..

Table 1.5: Average Annual Dealership Revenues

A. U.S. Dealership, 1999 (x \$1000):

	A. Gross Revenue	B. Dealer Val.Add	B/A (%)	B/Total Val.Add (%)
New Car	16,371	1,041	6.4	30.2
Used Car	7,899	1,048	13.3	30.4
Parts & Service	3,061	1,362	44.5	39.5
Total	27,331	3,452	12.6	100.0

B. Japanese Dealership, 1997 (x 1,000,000 yen):

	A. Gross Revenue	B. Dealer Val.Add	B/A (%)	B/Total Val.Add (%)
New Car	5,381.5	516.6	9.6	44.4
Used Car	930.8	110.8	11.9	9.5
Parts & Service	1,509.6	535.1	35.4	46.0
Total	7,822.0	1,162.5	14.9	100.0

Notes: Sums do not total because of rounding.

Sources: Reconstructed from data given in NADA (National Automobile Dealers Association), *NADA Data, 2000* (www.nada.org, 2000); Nikkan jidosha shimbun sha & Nihon jidosha kaigi sho, eds., *Jidosha nenkan [Automotive Yearbook]* 530-31 (Tokyo: Nikkan jidosha shimbun sha, 1999).

Exclusive Arrangements. Japanese manufacturers generally appoint their dealers principal agents for given models within a given geographical area. Traditionally, they assigned a dealer the entire prefecture. More recently, they divide the larger metropolitan areas, but they still assign the smaller prefectures to a single dealer. Generally, these contracts require the dealer to focus his sales efforts within the area, but do not prohibit him from selling outside it (Nomura & Booz, 1994: II 19-21).

Japanese manufacturers do not prohibit their dealers from selling the cars of competing manufacturers. Before 1980 they generally did. In two steps dating from about 1980 and 1990, however, the Fair Trade Commission took an increasingly adamant position against the contracts. By most accounts, manufacturers have since abandoned the arrangements.¹⁴

According to an early 1990s survey, 18 percent of all Japanese authorized domestic car dealers handled the cars of multiple manufacturers, while 22 percent of U.S. dealers did. In fact, however, most of the 22 percent U.S. dealers had negotiated multiple franchises, while only 4-5 percent of Japanese dealers had done so. The rest apparently handled the other cars through their principal domestic franchise agreement. Through 1991, for example, VW sold through Nissan; in 1992, it moved to Toyota. Honda sold Jeeps, Mazda sold Fords and Citroens, Suzuki sold GM and Pugeots, and Subaru sold Volvos (Nomura & Booz, 1994: III 14-19).

Relational Term. By common consensus, Japanese dealers seem to maintain longer-term ties with their manufacturers than do U.S. dealers.¹⁵ They maintain more direct financial ties as well. As of 1991 Japanese manufacturers held equity stakes in one-third of their dealers (foreign manufacturers had equity stakes in only 5 percent of their dealers). In addition, they had loaned funds long-term to 40 percent. Of the dealerships in which the manufacturer had an equity stake, 25 percent were wholly owned subsidiaries; 58 percent were dealers where the manufacturer held a less-than 5 percent stake (Nomura & Booz, 1994: II 5-8).

Unfortunately, the question of relational length is a red herring. Recall that a Japanese dealer is often the exclusive distributor (functionally exclusive, not legally exclusive) for several of a manufacturer's models for an entire prefecture. Given that status, the manufacturer simply cannot let the dealer fail. Toyota cannot afford to lose the only firm that distributes six of its models to an entire prefecture, and neither can Nissan, Mazda, or anyone else. Indeed, when they invest in their dealers they do so exactly by that logic -- for they are most likely to invest in the least profitable distributors (Nomura & Booz, 1994: II 7). Japanese dealers may have dealt with a given manufacturer longer than U.S. dealers have, in short, but they have also been in business much longer. They have been in business longer because Japanese manufacturers cannot afford to let them fail.

¹⁴ Nomura & Booz (1994: II 16-17, 27-28). They now appear to be most common among import dealers.

¹⁵ This is not related to formal contractual length. According to one survey, a majority of dealers work under a franchise contract with no stated term, but 30 percent work under a 3-year term. Generally, the contracts allow the manufacturer to terminate the contract only for cause (failure to pay moneys due, other breach of contract, and so forth) (Nomura & Booz, 1994: II 24-25).

Rather than compare U.S. dealers to Japanese dealers, compare U.S. dealers to Japanese outlets, and consider the impact of demographic change. In any society, people and firms move. As they do, cities change. The government builds new highways, runs new train lines, changes zoning rules. Rural areas become suburban, residential areas turn into office parks. Some roads lose traffic, others gain.

Necessarily, these demographic changes alter the optimal location of new car showrooms. New showrooms open, while others will close. If (as in the U.S.) each showroom is a separate dealer, these changes will yield a data base in which the average length of the dealer-manufacturer relationship is relatively short. If (as in Japan) each showroom is just another outlet for the prefectural dealer (whom the manufacturer cannot afford to let fail), the vicissitudes of demographic shifts will not affect the observed duration of the dealer-manufacturer relationship.

In Table 1.6, we give the total number of outlets for each dealer. Take Toyota -- perhaps the most consistent performer in the industry. Over the past 15 years, Toyota has gained at least 2,190 new outlets, or nearly half its current total.¹⁶ Subaru has added at least 133 (24 percent of the current total), and Suzuki has added 954 (69 percent of the current). Even more astonishing are Honda and Mazda. During the same fifteen years, Honda has added at least 2,479 outlets (more than the current total), and closed 411 (15 percent of the peak total).¹⁷ Similarly, Mazda has added at least 1,572 outlets (85 percent of current), and closed 1040 (36 percent of the peak).

Because Table 1.6 gives only the net annual change per producer it undercounts the true number of new and closed outlets. To illustrate turnover at a more local level, Table 6 gives the number of greater-Tokyo area outlets for several dealer lines for 1979, 1989, and 1999. The "Toyota," "Nissan," and "Mazda" lines are the premium dealer lines for these manufacturers. The "Corolla" and "Sunny" dealer lines are the low-end lines for Toyota and Nissan. Obviously, the table misses any netting effect from outlets added and lost during the intervening years.

Nonetheless, the table again illustrates the impact of demographic change. From 1979 to 1999, Toyota added at least 309 Tokyo-area outlets in these two lines (49 percent of the current total); Nissan added 229 (48 percent of the current total); and Mazda added 42 (48 percent of the current total). Since 1970, Toyota has added at least 417 outlets (67 percent of the current total), while Nissan has added 330 (70 percent of the current). About half of the Tokyo-area outlets, apparently, have appeared since 1970; over two-thirds have appeared since 1970.

¹⁶ Calculated from Table 1.6A as $(4966 - 3699) + (5011 - 4088)$.

¹⁷ $(2652 - 2241) / 2652$.

Table 1.6: U.S. Dealers and Japanese Outlets

	U.S. Japan.		Toyota	Nissan	Mitsub.	Mazda	Honda	Isuzu	Subaru	Suzuki
	Dealers	Outlets								
1985	24725	11048	3699	2988	1358	1310	237	608	421	427
1990	24825	N.A.	4529	2977	1289	N.A.	814	571	491	N.A.
1991	24,200	16332	4755	3066	1291	2718	2652	561	501	788
1992	23,500	16538	4755	3176	1319	2762	2652	563	502	809
1993	22,950	16942	4901	3176	1344	2882	2371	565	536	1167
1994	22,850	16355	4936	3099	1374	2412	2246	540	537	1211
1995	22,800	16374	4966	3090	1386	2412	2241	519	536	1224
1996	22,750	15569	4088	3071	1430	2412	2295	501	539	1233
1997	22,700	16170	4977	3048	1430	2106	2295	503	541	1270
1998	22,600	16201	4989	3043	1473	2009	2299	498	551	1339
1999	22,400	16088	5011	3039	1477	1842	2305	480	553	1381

Sources: NADA (National Automobile Dealers Association), *NADA Data, 2000* (www.nada.org, 2000); Nikkan jidosha shimbun sha & Nihon jidosha kaigi sho, eds., *Jidosha nenkan [Automotive Yearbook]* (Tokyo: Nikkan jidosha shimbun sha, various years).

**Table 1.7: Greater Tokyo Area Dealerships --
Outlets for Selected Lines, 1979-99**

Toyota				Nissan				Mazda			
	1979	89	99		1979	89	99		1979	89	99
<u>"Toyota" dealer line</u>				<u>"Nissan" dealer line</u>				<u>"Mazda" dealer line</u>			
Tokyo T	27	40	41	Tokyo N	23	53	52	Tokyo M	10	14	7
Ibaragi T	16	27	37	Shin-Tokyo N	22	0	0	Ibaragi M	2	1	0
Tochigi T	12	15	20	Ibaragi N	11	19	26	Mito M	7	8	11
Gunma T	17	20	20	Tochigi N	10	14	17	Tochigi M	7	10	10
Saitama T	17	27	38	Gunma N	17	18	21	M Auto Gunma	0	10	11
Chiba T	19	27	41	Saitama N	16	18	37	Saitama M	18	22	24
Kanagawa T	27	39	57	Chiba N	19	23	30	Chiba M	16	21	19
				Kanagawa N	25	37	46	Kanagawa M	16	25	6
				N Torakku Kan.	7	0	0				
<u>"Corolla" dealer line</u>				<u>"Sunny" dealer line</u>							
Tokyo C	21	64	66	S Tokyo	27	35	57				
Shin-Tokyo C	15	0	0	S Shin-Tokyo	10	17	0				
Nishi-Tokyo C	14	23	26	S Keio	3	0	0				
C Adachi	4	5	4	S Ibaragi	9	13	22				
C Sugamo	3	3	0	S Mito	7	7	0				
C Takashimaya	3	0	0	S Tochigi	10	12	15				
C Musashino	3	0	0	S S Gunma	14	19	17				
Tokyo T Diesel	5	0	0	S Saitama-kita	10	8	9				
C Ibaragi	11	16	13	S Saitama-min	9	21	29				
C Hitachi	9	12	16	S Chiba	14	16	19				
C Tochigi	14	7	18	S Chiba-kita	7	9	13				
C Gunma	10	13	16	S Kanagawa	17	26	34				
C Takasaki	10	10	12	S Shonan	19	26	30				
C Saitama	18	31	36								
C Shin-Saitama	15	25	32								
C Chiba	17	27	53								
C Keiyo	11	16	0								
C Kanagawa	36	53	61								
C Yokohama	18	18	18								

Source: Nikkan jidosha shimbun sha & Nihon jidosha kaigi sho, eds., *Jidosha nenkan [Automotive Yearbook]* (Tokyo: Nikkan jidosha shimbun sha, various years).

4.6 *Exclusion and Efficiency*

If any aspects of these distribution patterns exclude, we do not see how. This is not an industry that has kept out new entrants. During the early years, Toyota and Nissan did dominate the market. Yet Subaru, Mazda, and Mitsubishi entered it successfully by exploiting the niche for very small cars. Honda and Suzuki entered it by using their background in motorcycles. Mercedes Benz and BMW entered it by using their international reputations for quality.

The distributional requirements in the industry do not demand of the foreign firms tasks they cannot do. Should the foreign firms choose to organize large-scale Toyota-style distribution networks, we know of nothing that would prevent them. Importantly, the Honda example illustrates the way that they need not do so. Firms can survive and thrive with U.S.-style one-distributor-one-outlet networks as well.

If consumers want high-quality service, we know of nothing that would prevent foreign firms from providing it. If they want door-to-door salesmen, we know of nothing that would prevent foreign firms from hiring them. Importantly again, however, the data do not show that Japanese consumers do want unusually high levels of service, and Japanese consumers increasingly buy cars off the showroom floors.

Neither do we see how any of these practices could be inefficient. As foreign firms have discovered to their chagrin, this is a ruthlessly competitive industry. Regulatory strictures do not mandate the distributional patterns in place. Neither do network- and coordination-problems prevent firms from adopting distributional improvements. The arrangements in place might superficially differ from those in the U.S. By all appearances, though, they accomplish much the same results.

5. UNRAVELING DISTRIBUTION

More than a decade has passed since SII and the store wars -- a decade to move beyond negotiation strategy, a decade to unravel distributional practices. For several reasons, it has not been easy. Economic theory provides less help than one might want. For lack of a well-developed theory of distribution, Peter Drucker once called the sector the "Economy's Dark Continent." That is too strong, perhaps, but the contrast with production is nonetheless stark. For the production sector, analysts will find in the economic corpus a well-honed, heavily tested apparatus. About distribution, they will find considerably less.

Not only is the theory relatively undeveloped, the phenomena are diverse. Kao sells detergents through exclusive distributors, while Lion sells on the general wholesale market. Pola sells cosmetics door to door, while Shiseido sells through exclusive distributors to retail chains. Toyota sells to large multi-outlet distributors, while Honda began with a one-outlet-per-dealer strategy. In production, the diversity is less severe. There, each firm in an industry faces more nearly similar, technologically constrained choices. As a result, firms generally choose similar production strategies. Where they do not, observers can usually gauge their relative efficiency.

Reflecting the diversity in distribution across industries, the authors to this book understandably advance diverse hypotheses. In general, however, through their (and our) work, they (and we) stress one of more of the following common themes: that one cannot understand distribution apart from the characteristics of the product distributed -- both the demand patterns and manufacturing technology involved; that even given those

product characteristics, considerable room for diversity in distribution remains; and that distribution practices in Japan are closer to those in other advanced economies than observers have usually noticed. We think the studies clarify the empirics in Japan. We hope they contribute to understanding distribution more generally.

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