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**7-ELEVEN Japan Co., Ltd.:  
Reinventing the Retail Business Model**

**Kei Nagayama and Peter Weill**

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**Title:** Seven Eleven Japan: Reinventing the Retail Business Model

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**Abstract:** This case study describes how Seven Eleven Japan (SEJ) has successfully established an innovative business model that is changing the retail industry in Japan. The case describes the information-based strategies that have helped SEJ become a top performing retailer in Japan, selling high quality products through an industry-wide supply chain network. With its strong capability to analyze customer requirements, SEJ pursues an integrated strategy, supported by innovative use of information and IT, to control the marketing, merchandising and manufacturing of original products. The case also describes SEJ's development of an integrated retailing information strategy and associated systems. The company's policy of outsourcing most IT capabilities to partners and pursuing advanced IT initiatives has provided SEJ with substantial advantages over competitors. Strategic IT, human and information assets such as store councilors, item-by-item real-time control, industry-wide IT network, and a sophisticated analysis system have contributed to SEJ's success. The case addresses the challenges of remaining innovative while sustaining current core competencies.

Key words: Retail, business model, IT and information management, IT enabled strategy, outsourcing.

*22 Pages*

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**Massachusetts Institute of Technology  
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**7-ELEVEN JAPAN CO., LTD.**

***Reinventing the Retail Business Model***

Toshifumi Suzuki, CEO of Seven-Eleven Japan (SEJ), the world's largest convenience store (CVS) chain, describes Seven-Eleven stores as:<sup>1</sup>

*“Stores where you can find a solution for any of your daily life problems. We always try to plan and design a store in such a way that our store neighbors, in particular, can get whatever they need at any time they want.”*

Today, SEJ is not just a place for customers to shop but has become a place for relaxation and entertainment (Exhibit 1).

SEJ, headquartered in Japan, leads the world wide Seven-Eleven<sup>2</sup> chain, which had 24,912 stores in 18 countries in March 2003. In a 2003 ranking of retailers by market value, SEJ was number one in Japan and the eighth largest retailer in the world (Exhibit 2). Since its establishment in 1974, SEJ has never experienced a fall in income or profits.

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<sup>1</sup> Some parts of this case are drawn from Bensaou, B., Uchino, H. & Noishiki M. “Seven-Eleven Japan: Managing a Networked Organization,” Insead Euro-Asia Centre, 05/7-4690, May 1997.

<sup>2</sup> “Seven Eleven” includes the franchiser SEJ and its franchisees.

With 9,757 stores as of May 2003, SEJ is the largest CVS chain in Japan. Its stores feature the same basic designs: e.g., a large, highly visible sign in green, red and orange, a large store window, much brighter than average lighting and a spotlessly clean store. SEJ identifies their customer orientation, offering not only a rich assortment of products but total comfort to customers, as the source of SEJ's rise to the top of the Japanese retail industry.

**Industry Background**

**The Japanese Distribution System**

Some Western experts view the Japanese distribution system as a major barrier to trade. Traditional Japanese retailing consists of a conservative, multi-tiered system that combines large numbers of small wholesalers and retailers into complex exclusive networks. These networks are not based solely on economic efficiency but also on tight human relationships.

The W/R ratio, which compares sales volumes at both wholesale and retail levels, is a measure of the number of layers within the distribution system. Japan had a much higher ratio, 2.3, in 1998 than the

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This case was written by Kei Nagayama, Management of Technology Program Class of 2003 at MIT Sloan School of Management, working with Dr. Peter Weill, the Director of the Center for Information Systems Research at the MIT Sloan School of Management. This case is for the purpose of management education, rather than illustrating or endorsing any particular management practice. The authors would like to gratefully acknowledge Mr. Toshifumi Suzuki, CEO, Mr. Makoto Usui, Managing Director, and Ms. Yuka Ozaki, Mr. Usui's assistant, at Seven-Eleven Japan, Co., Ltd., in completing and publishing this case. This case may be reproduced free of charge for educational purposes provided the copyright statement appears.

U.S., 0.98<sup>3</sup>, had in 1992. Although the development of information technology in the industry has gradually improved the efficiency of the distribution system, small-to-medium-sized retailers owe their existence mainly to the multi-tiered and vertically integrated structure. In 1973, when SEJ was established, products typically passed through three or more levels of wholesalers—national or primary, secondary and local levels.

The system was historically established by manufacturers to ensure total support for their products and marketing strategies, as well as to exclude rival manufacturers from the channel. The long-term, secretive nature of the negotiated rebates has increased a manufacturers' power in channel activities.

### **Retail Business Environment**

The Japanese retail sector is still dominated by small retailers. Firms with one to four employees make up about 70% of the total number of stores (Exhibit 3). In these small shops, CVS still accounts for only 3.2% of all stores and only 5% of total sales.

Because of Japan's small land area, most Japanese retail stores have too little space to maintain a wide assortment of products in either the store or inventory. These small, local "mom-and-pop" stores typically lack both managerial know-how and planning skills. In addition, given their limited size, they are often unable to bear large inventory risks and thus have to rely on manufacturers and wholesalers to bear part of that burden. To protect them from large stores, the Japanese government enforced in 1974 the Large-scale Retail Store (LRS) Law which regulated the business hours of larger outlets. Initially applied to stores over 1,500 m<sup>2</sup>, it was later extended in 1979 to stores with an area of over 500 m<sup>2</sup>. The law mandated that stores close by 7 P.M. each day and remained closed at least 30 shop days per year. Fueled by heavy pressure from abroad, the deregulation trend caused the LRS law to be changed in 1990 and practically abolished in 2001. Although the law had a positive effect on small retailers by deterring large retailers from opening stores, it also blocked modernization of small retailers ultimately weakening their

competitiveness.<sup>4</sup> Ironically, large retailers have been gradually overwhelmed by CVSs which evolved under the protection of the LRS law. While operating its large stores under the LRS law, Ito-Yokado, a parent company of SEJ, launched a new retail business based on small regional stores, which can effectively co-exist with large stores. As a result, CVS chains prove that small stores can compete against larger retailers by improving the efficiency and productivity of their franchise and continually striving to meet customer needs.

The lengthy Japanese recession brought hard times to the retail industry by causing a downturn in sales and a difficulty in expanding the store network. The result is that the number of small stores (with one to four employees) has decreased dramatically. The leadership role in Japanese retail was held for a long time by department stores, then by super markets and has finally been assumed by CVSs. Because of the density of the store network, CVS chains are not only places to sell products, but are also becoming an important part of the social infrastructure.

### **Seven-Eleven Japan**

Ito-Yokado, a parent company of SEJ, was founded by Masatoshi Ito in 1964 as a 66-square-foot family clothing store in Tokyo. After starting a new chain of super stores offering a range of food and clothing products, he expanded his business into other distribution areas such as restaurants, department, discount and convenience stores. By 2002, the Ito-Yokado group was one of the largest retail groups in Japan with ¥5,574 billion (\$41.6 billion) in sales and 114,600 employees.

It was during negotiations in the late 1960s with the U.S. restaurant chain, Denny's, that Toshifumi Suzuki, Executive Manager of Ito-Yokado's New Business Development division, first discovered a new style of retail business which were, at the time, very popular in the U.S.—the convenience store. He came to realize that bringing small and less productive retailers into a well-organized franchise network of convenience stores would both provide the small shop owners with the management and merchandising skills they were lacking and provide customers with the benefits of the traditional neighborhood retailer.

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<sup>3</sup> Ministry of Economy, Trade and Industry, "White Paper on Small and Medium Enterprises in Japan," 1997 and 1998 (in Japanese).

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<sup>4</sup> Toshihiko Sato, "Daikibo-Kouri-Tenpo-Hou ga Motarashita Mono (What LRS Law brought about)," SRIC Report, Mar. 2001 (in Japanese).

Toshifumi Suzuki negotiated directly with Southland, then owner of Seven-Eleven, to bring the convenience store concept to Japan. President Ito and others at Ito-Yokado were convinced that it was too early to introduce the concept into the Japanese distribution system, which was already saturated with a very large number of small retailers. In spite of the commonly held skepticism and negative opinions from academia and retail experts, Suzuki proceeded with his plans and in 1974, opened the first Seven-Eleven convenience store in Kohtoh-ku, an Eastern suburb of Tokyo. He later explained:

*“At the time, I was young and very eager to find a way that both small and large retailers could prosper together. I was convinced that a convenience store franchise was the best solution.”*

After the contract was signed, Suzuki realized that the Southland convenience store concept had to be adapted to the Japanese market—American operational know-how could not be directly transferred to the Japanese distribution system context. In particular, the differences in consumer behavior between the U.S. and Japan made American methods a poor fit in the Japanese market. Japanese consumers were generally more sensitive to product and service quality, more fickle and less price-sensitive. Therefore products had to be fresh, and the turnover rate very high. To meet such customer requirements within the constraint of limited shelf and storage capacity, it was necessary to forecast customers' demand by the time of purchase, the store location and the weather. Providing the customer with well-targeted, differentiated products 24-hours a day, 7-days-a week was critical. Suzuki said: <sup>5</sup>

*“A CVS is only a small store. Therefore we have little choice but to focus on high-quality products meeting the customer needs and to emphasize convenience.”*

Winning the patronage of customers by constantly meeting their needs, SEJ has generated a strong record of growth and profitability since its establishment in 1973. As of 2003, SEJ is the largest convenience store chain with ¥2,213 billion (\$17.5 billion) revenue and 5,061 employees. Its market value of \$21,721 million and consolidated net

income of ¥82,825 million (\$690 million) are the highest in the whole of Japan's retail industry (Exhibit 4).

## **Strategy**

### **Company's principles**

After graduating in economics from Chuo University, Suzuki worked for Tokyo Shuppan Hanbai, one of Japan's largest book wholesalers. At 31, he was noticed by Ito-Yokado and asked to join SEJ. While working in sales promotion, human resources management and public relations, he came to realize the gap between changing consumer tastes and the one-sided approach to customers used by retailers at that time. His fundamental belief in the importance of customer satisfaction was repeatedly reflected in each of his policies throughout his career. In particular, his obsession with customer satisfaction was at the origin of SEJ practice of continuous item control and well-organized delivery system, and the heavy use of information technology (IT). To get an objective assessment of customer needs, he respects the opinions of non-experienced people. In his view:

*“Merchandising consists of identifying customer needs ... and experience or expertise might contaminate a manager's judgment.”*

Unlike many retail executives, he rarely visits stores. His approach is more analytical—hence his faith in a high-tech computer system to keep in touch with customer tastes and examine SEJ's forecasts of potential customer demands.

The basic mission of an SEJ store is to provide solutions for all the problems of everyday life. Each store offers a variety of high-quality products and services that are required daily or on an emergency basis to make life easier and more “convenient.” Suzuki found that the two main reasons for the failure of existing retailers. They ignored: 1) the importance of convenience to the customer and 2) the quality of the products and the service. Under Suzuki's leadership, SEJ developed some key principles to define a quality convenience store.

*Reduction of lost opportunity:* A missed opportunity to sell an item because it is out of stock is one of the most serious problems in retail business in terms of disappointing customers as well as missing the actual profit. Suzuki therefore encouraged the

<sup>5</sup> “Seven-Eleven Katsu! Ronri-Shiko” (SEJ: Go Win! Logical Thinking), Weekly Toyo Keizai, April 12, 2003 (in Japanese).

development of operational processes to reduce this opportunity cost.

*Effective Item Control and Well-Planned Product Supply Management:* The American practice of keeping large inventories of a wide variety of products could not be applied in convenience stores in Japan where shelf and storage space are limited and maintaining a large inventory is prohibitive. Therefore SEJ pursued a strategy of supplying products in high demand with a rapid turnover rate and eliminating dead or slow-moving products through item-by-item analysis. The well-organized analysis and frequent replacement contributes to SEJ's high product supply efficiency.

*Commitment to Customer Satisfaction with Original Product Development and Friendly Service:* SEJ not only sells manufacturers' products but also researches customers' potential needs. SEJ uses this research to provide original products at reasonable prices (such as a lunch boxes and prepared foods). Well-trained store clerks also contribute to a friendly store atmosphere, which then leads to customer satisfaction.

### **Merchandising**

The store space available for a Seven-Eleven franchisee is, on average, only 110 m<sup>2</sup>. Year to year, 70% of the product lines in a given store will be new items. The items kept in stock and on the shelf are precisely selected for the targeted customers and product quality is kept high. Product turnover is high, and goods are always new and food fresh. For instance, 'bento' lunchboxes are delivered three times a day just before peak hours. The product life cycle of branded drinks is short and tightly follows fashion. Stores can quickly switch from slow-selling brands to the more fashionable ones according to sales data and market trends. Strict product management has enabled Seven-Eleven to reduce the average stock turnover from 25.5 days in 1977 to 8.7 in 2003 (Exhibit 5).

SEJ discovered that customer loyalty was driven more by specific items than by item categories. To meet the demand and achieve such tight item-by-item control, SEJ implemented the POS (Point of Sale) system in 1982, whereby storeowners could identify customer trends and enhance product differentiation. Originally introduced in the U.S., where the employee turnover rate is relatively high, the POS system was used to increase the productivity and reliability of cashier operators, as it reduced the employee training time and the

possibility of fraud. SEJ introduced its POS systems to collect sales data used to improve merchandising and the item-by-item control process. For instance, the cash register would not open until the operator pushed the account button indicating the gender and estimated age of the customer. This information from the POS system was used for consumer trend analysis. Suzuki emphasized:<sup>6</sup>

*"POS is a tool to seek out not hot-selling goods but dead or slow selling products. If you pursue only dollar spinners with the POS system, your business will slowly contract."*

Focusing only on hot-selling items via the POS system allows consideration of only in-store items rather than potential goods. Refilling missing current items does not develop new product ideas that will satisfy potential customer needs. Seven-Eleven forecasts future trends and creates a "hypothesis" of potential hot-selling products based on the analysis of various information. Seven-Eleven uses the POS system as a tool to create and test sales promotion hypotheses.

SEJ has also formed "team merchandising" development tie-ins with major raw material and packaging manufacturers to provide original products. While there is generally a certain distance between companies, SEJ has successfully created a close relationship with these manufacturers as if they were one company, enabling them to effectively share the same goals and to collaborate. Suzuki explains SEJ's enthusiasm for its original products.

*To produce the best original products with higher quality than any competitors, we continue to create a hypothesis, test it, make another hypothesis, and examine it over and over, believing that the taste and quality of the product must satisfy customers. SEJ executives repeatedly sample original fast-foods everyday so that the quality of these products can be improved before they are sold.*

In addition to directly responding to the changing needs of customers, original items are highly effective in differentiating stores because they cannot be purchased anywhere else. SEJ provides customers mainly with fast foods such as rice balls, sandwiches and delicatessen items. They also partner with manufacturers to improve the quality of

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<sup>6</sup> Tomoyuki Ogata, "TANPIN KANRI (Item-by-Item Control)," East Press, Sep. 2000 (in Japanese).

foods and the efficiency of production (Exhibit 6). Since original product development can reduce the costs of marketing and advertisement as compared to other general products, even in Japan's deflationary environment, SEJ can maintain competitive prices rather than be forced to price them as cheap commodities. In 2003, 50% of total sales consisted of original items including soft drinks, instant noodles and confections.

### Store Network Expansion

SEJ considers its market dominating strategy of high-density, clustered store openings to be the key to efficiency and stability. Although SEJ has opened approximately 10,000 stores in 32 of the 47 prefectures in Japan, the company believes there is still room for further expansion (Exhibit 7). The advantages of the market dominance strategy are:

- Improved brand awareness
- Increased customer visits to the stores
- Boosted distribution efficiency
- Enhanced productivity of franchisee-support services
- Improved advertising effectiveness

Rather than aiming for simple expansion, SEJ emphasizes the business factors that will ensure each and every store's success. Some 135 factors are analyzed in new store decisions, based on data related to locations and sales amassed at approximately 10,000 stores, including location, market area, number of households and population density. New store establishment plans are based on analysis of the proposed stores' profitability, with strong emphasis on ROI. This process helps generate an average daily sales of approximately ¥656,000 (\$5,467), exceeding the industry average by about 35%.

### Franchise Strategy

From the beginning Suzuki did not invest in American style 'greenfield' stores, where the franchiser buys the 'walls' or builds the store from the ground up. Approximately 60% of SEJ stores were modified from old family owned stores (e.g., liquor or rice stores). The relationship between franchiser and franchisee is one of reciprocal obligations. The franchisee is an independent business which gives SEJ royalties and a long-term commitment, and concentrates on the tasks of selling and effectively managing inventory. The royalty that the franchisee pays to the franchiser is 43% of its gross profit. Although high compared to competitors, it covers many items such as the trademark licensing fee, 80%

of utility costs, advertising fees, fixtures, computer systems and product supply services (Exhibit 8). SEJ also guarantees a minimum gross profit for poor performing stores in order to support owners.

In exchange for their long-term commitment and royalties, SEJ provides franchisees with service from field representatives called Operation Field Counselors (OFC). Each of about 1,300 OFCs supervises between seven or eight stores, providing (i) advice on store operation and ordering and (ii) information on the portfolio of available items and on sales methods. This person-to-person contact with store managers is a key element of the SEJ franchise system. Each OFC visits each store at least twice a week and spends at least two hours providing advice and information. Such a close relationship not only motivates franchisees but also supports company-wide brand image and promotional strategies.

SEJ spends more than ¥3 billion (\$25 million) per year on bringing together OFCs from all parts of Japan to SEJ headquarters in Tokyo for weekly meetings. Suzuki repeats at each meeting:

*"It is not enough to exchange information. The information has no value unless it is understood and properly integrated by the franchisees and makes them work better."*

Before starting a new store, the new franchisees and their wives are first brought to the central training center for two weeks to understand the corporate principles. Then they go through on-the-job training in one of the regular stores to explain the need for ordering with unique hypotheses and the importance of daily operation and service quality. Suzuki explains:

*"We became successful because we've concentrated on retailing, shared information with staff, and encouraged them constantly to respond to change"*

### Outsourcing Policy

SEJ is known for its outsourcing policy and ability to manage supplier relationships. Since its creation, the company has never directly owned any manufacturing or logistics operations. While its competitors tried to develop their own capabilities to circumvent the inefficiency and complexity of the existing Japanese distribution system, SEJ convinced partner companies for each region to cooperate exclusively with SEJ, ensuring efficient business engagements. In return for



exclusivity, regional partner companies are required to improve their operations and increase their service levels. For instance, strict requirements on product freshness and taste are imposed to ensure quality. Suzuki confides:

*“Selecting and negotiating with the various subcontractors, wholesalers and manufacturers was not easy.”*

The rationalized distribution system crafted by SEJ created conflict within the traditional wholesale system. Over time, however, SEJ’s system has proved highly reliable and efficient, covering everything from raw procurement to product deliveries. Once those standards were met, business partners appreciated the feedback they were getting from the quick and precise sales data. Manufacturers also benefited from an improved understanding of what customers wanted. A salesman with a partner food company said:

*“[Their] information system is so good that we can instantly find out which goods of ours are selling to what types of customers and how much.”*

The collaboration between SEJ and the business partners includes shared information systems and know-how about operations management as well as quality control in the food manufacturers’ factories and delivery centers.

By 2002, the company had built a network of 223 distribution centers and 195 factories dedicated to fast food production, all of them created and operated by wholesalers, suppliers and forward agents.

### **Information Systems Strategy**

Suzuki used to say about information systems:

*“Don’t rely on the POS system. Information technology is merely a tool to achieve business strategy. We shouldn’t use the technology unless we can understand what the information means on paper.”*

Daily, Seven-Eleven stores serve a total of 9.5 million customers, process five million order transactions and send 35 million sales transactions to the information systems center where sales data is collected, integrated and analyzed. The accuracy of the data itself, however, does not guarantee the suitability of the product selection or the appropriate order quantity for strong, sustainable sales. These decisions have to be based on well-analyzed

hypothesis, order and validation. Information technology (IT) for SEJ is merely a method to support the cycle. One SEJ executive said:

*“Even if the POS data is used, it cannot be utilized for the next order unless the hypothesis of potential demand is shared among all store clerks as well as the store owner. Therefore we needed to establish the system that enables store owners and the ordering clerks to create their hypotheses and share them among part-time workers at the store [even if they cannot communicate face-to-face].”*

Although SEJ regards its information systems as just a tool, it is known for proactive investment in IT and outsourcing of its critical systems. Since the implementation of its first total information system in 1978, SEJ has subcontracted information systems management—from development to operation of its systems—to Nomura Research Institute, Ltd. (NRI), the third largest IT service company in Japan.<sup>7, 8</sup> SEJ prefers to outsource most of its information systems management to external service providers due to the speed at which the information technology market moves. This strategy allows the information systems department of SEJ to focus on developing a systems vision that fits with the business strategy, while the rest of the information systems management is outsourced. The department has evolved into a more strategic organization that links needs from stores with top management and proposes innovative system plans.

SEJ regularly explores opportunities to gain first mover advantage by trying out state-of-the-art technologies: the first POS system in Japan in 1982, the first major use of Integrated Service Digital Network (ISDN) in 1991, etc. For example, ISDN allowed data to be exchanged at 30 times faster speeds and thus enabled SEJ headquarters to collect and analyze daily POS data on every single item in each store for use the next morning; a process that formerly took more than a week to complete. This innovation improved the ability to order the right items, thus maintaining shelves of hot-selling products which may be out of stock in competitors’ stores.

In 1996, SEJ introduced a weather forecasting system, enabling store owners and clerks to forecast

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<sup>7</sup> *Computopia*, September 2002.

<sup>8</sup> Nomura Research Institute, “Nihon no Ryutsu System to NRI (Japanese Distribution System and NRI),” *Mirai-Sohatsu* Vo.9, Jan. 2003 (in Japanese).

orders which vary depending on the weather and the temperature. Umbrellas kept in storage can be displayed if rain is forecast. On a sunny weekend, rice products sell well. Five reports a day arrive electronically at store terminals from a total 700 private weather centers, each covering a radius of 20 km (13 miles).<sup>9</sup> This is useful in Japan, where temperatures between towns 40km apart can vary by as much as 5 degrees C and broad TV forecasts are unreliable.

## **Operation Infrastructure**

### **Total Information Systems**

Beginning with its first store system in 1978, SEJ has continued to develop total information systems. In June 1999, the fifth generation total information system, in which SEJ invested ¥60 billion (\$500 million), was released in collaboration with 14 companies including NRI, NEC, Toshiba TEC, etc. (Exhibit 9). The system has four major features explained below.

*High efficiency, maintainability and reliability of the total network system:* The system connects 70,000 computers in stores, at headquarters and at supplier sites through satellite telecommunications, exclusive lines, ISDN and mobile networks via the most appropriate telecommunication technology. The combination of ISDN and satellite telecommunications realizes 45x faster speeds at 35x better cost performance. Terminals are constantly monitored and software and configuration can be updated remotely. The most critical systems such as online ordering and accounting systems are backed up at physically separated locations in Yokohama and Osaka. And in earthquake-prone Japan, satellite telecommunication provides an extra layer of safety. The system, now shared by 10,000 stores, is considered highly reliable due to the crisis management planning and high service levels.

*The store information system which encourages all store staff to participate in ordering:* SEJ provides stores with multimedia information such as pictures, video, audio, text and numerical data, which is used by all employees in Seven-Eleven stores. Each of the total 200,000 store owners and clerks, including part-time workers, is expected to participate in inventory management. This collaboration leads to appropriate orders, optimizes employees'

capabilities and maintains their motivation. The multimedia system helps employees forecast consumer demand by providing POS, products, weather and regional information with sophisticated interfaces and graphics.

*The system platform shared with business partners:* SEJ provides its business partners—vendors, distributors and manufactures—with a common infrastructure consisting of 1,800 terminals at 1,100 locations. The applications on the platform vary depending on the partner's business: raw material ordering system, inventory management, production management, automated sorting system, for example. The broad system infrastructure facilitates collaboration among SEJ allies by improving the efficiency of delivery through the sharing of order, sales and inventory information.

*Sophisticated analysis system which eliminates intuitive decision-making:* The fifth generation total information system provides a highly integrated analysis system which collects enormous quantities of data and creates value-added information for original product development and store support services. The input data includes sales, orders, disposals, and opportunity losses. Most of the data is used to examine hypotheses that each store creates.

### **Electronic Commerce Business**

SEJ categorizes its electronic commerce (EC) business into four major groups: 1) financial services, 2) Internet shopping site, 3) public and regional services, and 4) in-store intelligent copy machines.

*Financial Services (settlement, finance, and card service):* Launched in 1987, Seven-Eleven has developed the payment acceptance service which provides customers with a convenient means to pay their bills 24 hours a day, 365 days a year. Affiliated companies number about 1,500 and the types of payment are mainly utilities: electricity, telephone, water, rent, and mail orders. This business has been successful with 144 million yearly transactions with a total value of ¥1.15 trillion (about \$12.8 billion) and a 20% annual growth rate. Seven-Eleven's desire to create high customer satisfaction convinced Ito-Yokado to establish the group's bank, IY Bank, in 2001. IY Bank mainly provides settlement service for the 5,250 ATMs located mostly in Seven-Eleven stores. The company has rapidly grown into one of the largest banks in Japan with 48 affiliated companies and many contact points with customers.

<sup>9</sup> "E-strategy Brief: Over the counter e-commerce", *The Economist*, May 26, 2001.

*Internet Shopping Site:* 7dream.com, a subsidiary of SEJ, provides the internet shopping site by utilizing SEJ's existing operating infrastructure in its EC activities. SEJ also ties into other internet sites and provides payment acceptance and pick-up service at the retail stores. Goods purchased via the Internet are picked up at stores 24-hours a day or delivered to customers' homes, raising the value of Seven-Eleven stores and enhancing convenience for customers.

*Public, civil and regional services:* SEJ's meals-on-wheels service, named Seven Meal Service, offers prepared meals and cooking ingredients to regional customers. Order can be made via the Internet. SEJ plans to expand its public services at stores via its EC platform so that customers can obtain civil services.

*In-store intelligent copy machines:* Multipurpose copy machines at Seven-Eleven stores are connected the Internet and enable customers to print event tickets and documents created by customers at home as well as to pay for pre-ordered airline tickets.

The current EC business is a new frontier for SEJ, enabling the reinforcement of its existing business at stores. With the capability to attract 1,000 customers per day per store, SEJ is pursuing synergy between the existing retail and EC business units to encourage potential Internet users to visit Seven-Eleven stores and become new customers.

SEJ also provides its EC platform service for EC partners with functions such as authentication, database, settlement, and distribution (Exhibit 10).

### **Temperature-Separated Combined Distribution System**

Since 1976, SEJ has been developing a streamlined distribution system to efficiently integrate product supplies. The company established the Combined Delivery System, whereby the same kind of products coming from different suppliers can be *centralized* into 223 Combined Delivery Centers (CDCs). The combined distribution system allows products from different suppliers to be loaded on the same trucks for delivery to Seven-Eleven stores. Combined distribution consolidates product shipment from manufacturers to stores at similar optimum temperatures. In 22 years, SEJ has reduced the average number of vehicles visiting each store from 70 a day in 1974 to ten a day in 1998 (Exhibit 11). This effort contributes not only to the efficiency of delivery but also reduces truck emissions and traffic congestion.

To meet customer demand, rice products and sandwiches are delivered three times a day: in the morning, at noon, and in the evening, just before peak purchasing times. Items ordered by 10:00 A.M. can be delivered by the evening of the same day.

Delivery routes and time are also well organized to maintain high efficiency. Even in emergency situations such as heavy traffic, other means of transportation (e.g., helicopters or motorcycles) will be used to avoid late deliveries.

### **Competitors**

SEJ is the largest CVS chain in Japan in terms of the number of stores, sales, and net income followed by Lawson, C&S, Familymart, and Ministop. These top-five companies dominate the market with almost 90% market share (Exhibit 12). All four competitors operate franchise businesses with store networks expanding all over Japan.

Competitors are increasingly investing in EC business to compete and establish dominance in a new area. In 1997, Lawson began implementing multimedia terminals in stores to gain first mover advantage. The initiative has been relatively successful with total billing at ¥40 billion. Lawson also tries to differentiate itself in the Internet shopping site named @Lawson by launching new services such as net coupons, which was rare in Japan in 1999.

The downturn of profitability in existing store business is a serious problem to the competitors which cannot rationalize their operation as much as SEJ. Although they have maintained their growth by expanding store networks, such growth is limited in the largely saturated market. Their challenge is to attract potential customers by providing appealing EC services with low costs.

### **Future Vision**

The Japanese retail industry has recently faced severe external pressures: consumer recession, deflation, the threat posed by specialty stores, and vigorous participation by foreign retailers. Can SEJ, which has pursued customer satisfaction for 30 years, sustain its advantage in future?

The company strives to achieve the maxim "the retail business should always keep up with change of customer demands" with three principles.

*Responsiveness to changing customer needs and continuous improvement of customer services:* SEJ's fundamental strategy is to directly respond to the changing needs of customers. Since customers' tastes, market trends, and the industry environment are always changing, SEJ has maintained the agility to address those changes by generating hypotheses of potential customer demands. All store owners and part-time clerks are expected to share this fundamental concept and the methodology of item-by-item product management. In addition, SEJ has emphasized friendly customer service to promote customer loyalty. SEJ has facilitated proactive customer service: e.g., offering shopping advice to customers, changing store layouts based on customers' feedback, and sampling original products.

*Manufacturing retailer:* SEJ has gained capabilities of marketing and original product development, which were held mainly by manufacturers. While expanding the original product development, the company is also exploiting a new Internet-based merchandising strategy. This new network allows SEJ to establish both effective procurement methods such as a reverse auction and another communication channel with consumers. The Internet-based and group-wide shared procurement system is increasingly contributing to the company's merchandising efficiency.

*The combination of demand chain and supply chain management with the common platform:* While supply chain management (SCM) is based on the improvement of efficiency and productivity, demand chain management (DCM) is a more proactive method to stimulate potential customer demands by offering differential products and services in the multi-channel mix. SEJ pursues the synergy of both chain managements to satisfy customer demands as well as achieve co-prosperity with suppliers, believing that the fundamental role of retailers is to link the demands of customers and suppliers by developing and providing reasonable and high quality products (Exhibit 13).

With ten thousand stores open 24 hours a day, 365 days a year and ten million customers daily visiting on average once every two days, this network is increasingly becoming a delivery platform for the services of SEJ's business partners. SEJ believes that this collaboration, based on the mix of existing and Internet channels, could create a disruptive retail business model.

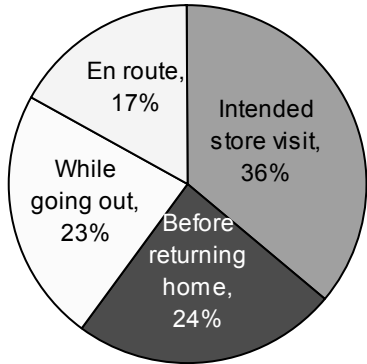
In Hawaii, where there are only 53 Seven-Eleven stores, success comes from the company's fundamental strategies: original product development by the "team merchandising" method, item-by-item control, and store management method. The Hawaii stores' pilot is being applied to other stores in the U.S. mainland. The market share of a CVS store is much lower in the U.S., where the market is heterogeneous and the income gap is bigger than in Japan. Therefore SEJ's approach of targeting a wide range of market segments is considered difficult to implement in the U.S. Despite that concern, Seven Eleven has been successful in the U.S. by effectively maintaining and localizing its principles. James Keyes, President and CEO of 7-Eleven, Inc., of the United States, said:

*"Seven-Eleven of the United States will have a strong potential for success if we learn more about SEJ's item-by-item control and effective delivery system."*

Today, one of SEJ's challenges is how the company can maintain a global strategy and "export" its corporate principles to other countries.

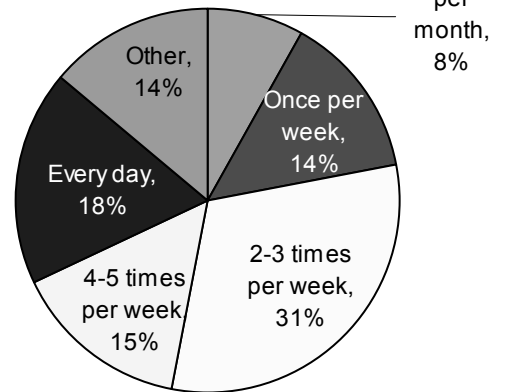
## Exhibit 1 SEJ Customer Profile

**Customer Activities When Visiting Stores**



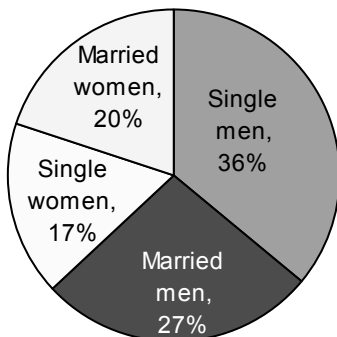
7-Eleven stores are used on a variety of occasions.

**Frequency of Store Visits**



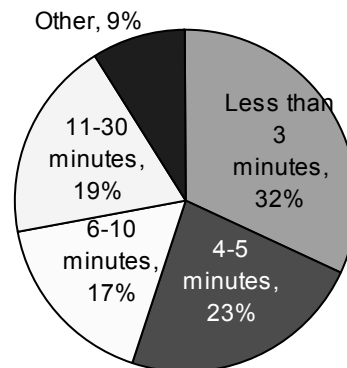
64% of customers visit 7-Eleven stores at least twice per week.

**Gender and Marital Status**



63% of customers are males.

**Time it Takes Customers to Reach a Seven Eleven Store**



55% of customers come to 7-Eleven stores from less than five minutes away.

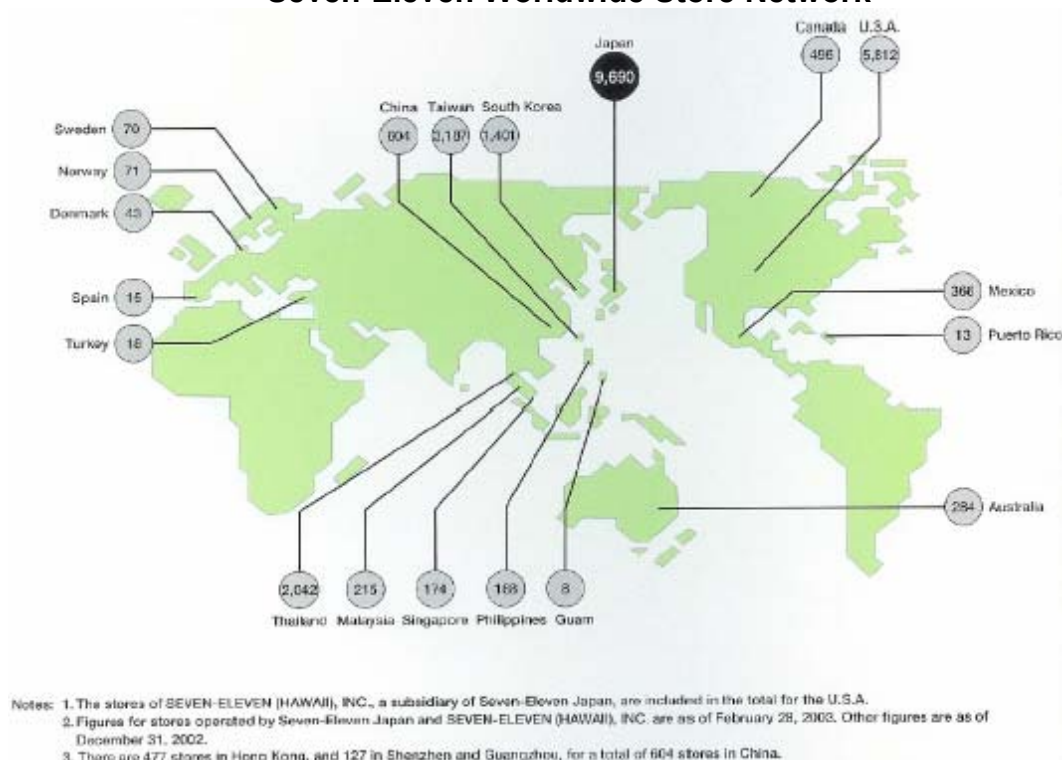
(Source: Seven Eleven Japan, "Corporate outline 2003.")

**Exhibit 2**  
**Top 15 ranked by market value in retailers**

2003 [2002]	Company	Market Value (million US\$)	EPS (US\$)	Sales (2002) (million US\$)	Net income 2002 (million US\$)
1 [1]	Wal-Mart Stores (U.S.)	\$229,658	1.49	217,799	6,671
2 [2]	Home Depot (U.S.)	\$56,655	1.30	53,553	3,044
3 [5]	Lowe's (U.S.)	\$31,878	1.33	22,111	1,023
4 [3]	Walgreen (U.S.)	\$30,214	1.00	28,681	1,019
5 [6]	Carrefour (France)	\$27,124	2.13	75,031	1,500
6 [4]	Target (U.S.)	\$26,591	1.57	39,176	1,416
7 [19]	Ebay (U.S.)	\$26,332	0.89	1,214	255
8 [7]	Seven-Eleven Japan (Japan)	\$21,721	0.83	3,241	689
9 [9]	Tesco (U.K.)	\$20,334	0.19	37,367	1,311
10 [10]	Kohls (U.S.)	\$19,078	1.48	7,489	496
11 [12]	Sysco (U.S.)	\$16,709	1.03	23,351	680
12 [16]	Hennes & Mauritz (Sweden)	\$15,332	0.81	5,369	671
13 [13]	Costco Wholesale (U.S.)	\$13,687	1.54	37,990	700
14 [24]	GAP (U.S.)	\$12,808	(0.01)	13,848	(8)
15 [26]	Inditex Industria de Diseno Textil (Spain)	\$12,100	0.60	3,548	371

(Source: Ito-Yokado Group Investors' Guide 2003)

**Seven-Eleven Worldwide Store Network**



(Source: Seven Eleven Japan, "Corporate outline 2003")

### Exhibit 3 Japanese Retail Industry



(Source: Japanese Ministry of Economy, Trade and Industry, “Census of Commerce”)

#### Number and Annual Sales of Retail Stores in 2002

Business Category	Number of Stores	% of Total Stores	Annual Sales (¥ billions)	% of Total Sales
Department Stores	357	0.0%	8,021	5.9%
General Supermarkets	1,672	0.1%	8,917	6.6%
Specialty Supermarkets	37,037	2.8%	23,631	17.5%
Convenience Stores	41,769	3.2%	6,714	5.0%
Drug Stores	14,673	1.1%	2,496	1.8%
Other Supermarkets	66,163	5.1%	6,808	5.0%
Specialty Stores	1,136,143	87.4%	78,308	58.0%
Other stores	2,229	0.2%	230	0.2%
<b>Total</b>	<b>1,300,043</b>	<b>100.0%</b>	<b>135,125</b>	<b>100.0%</b>

(Source: Japanese Ministry of Economy, Trade and Industry, “Report on 2002 Census of Commerce”)

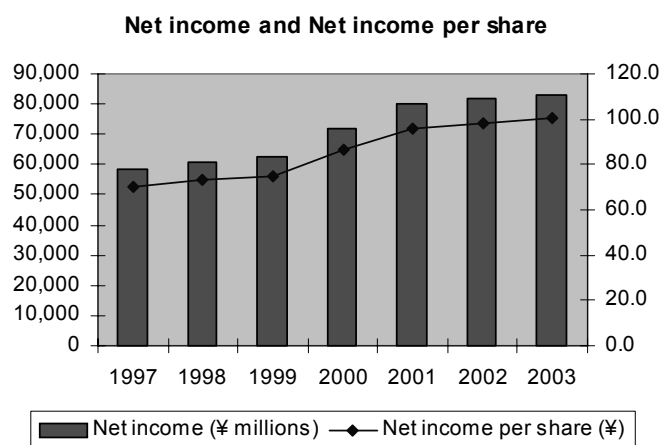
### Exhibit 4

#### Seven Eleven Japan Consolidated Financial Summary

For the fiscal years ended February 28/29	1997	1998	1999	2000	2001	2002	2003
Revenue from Operations (¥ millions)	263,102	286,916	308,903	337,287	358,446	384,416	424,091
Ordinary income (¥ millions)	105,014	112,076	117,211	141,738	148,292	148,507	153,769
Net income (¥ millions)	58,409	61,008	62,390	71,831	80,192	81,716	82,825
Net income per share (¥)	70.1	73.2	74.9	86.2	96.2	98.3	100.6
Number of stores	6,922	7,362	7,780	8,203	8,661	9,116	9,743

For the fiscal years ended February 28/29	<b>2003(Thousands of US dollars)</b>
Total Store Sales	<b>\$18,883,212</b>
Revenue from Operations	<b>3,594,000</b>
Net income	<b>701,915</b>
Capital expenditure	<b>525,754</b>
Depreciation and amortization	<b>233,009</b>

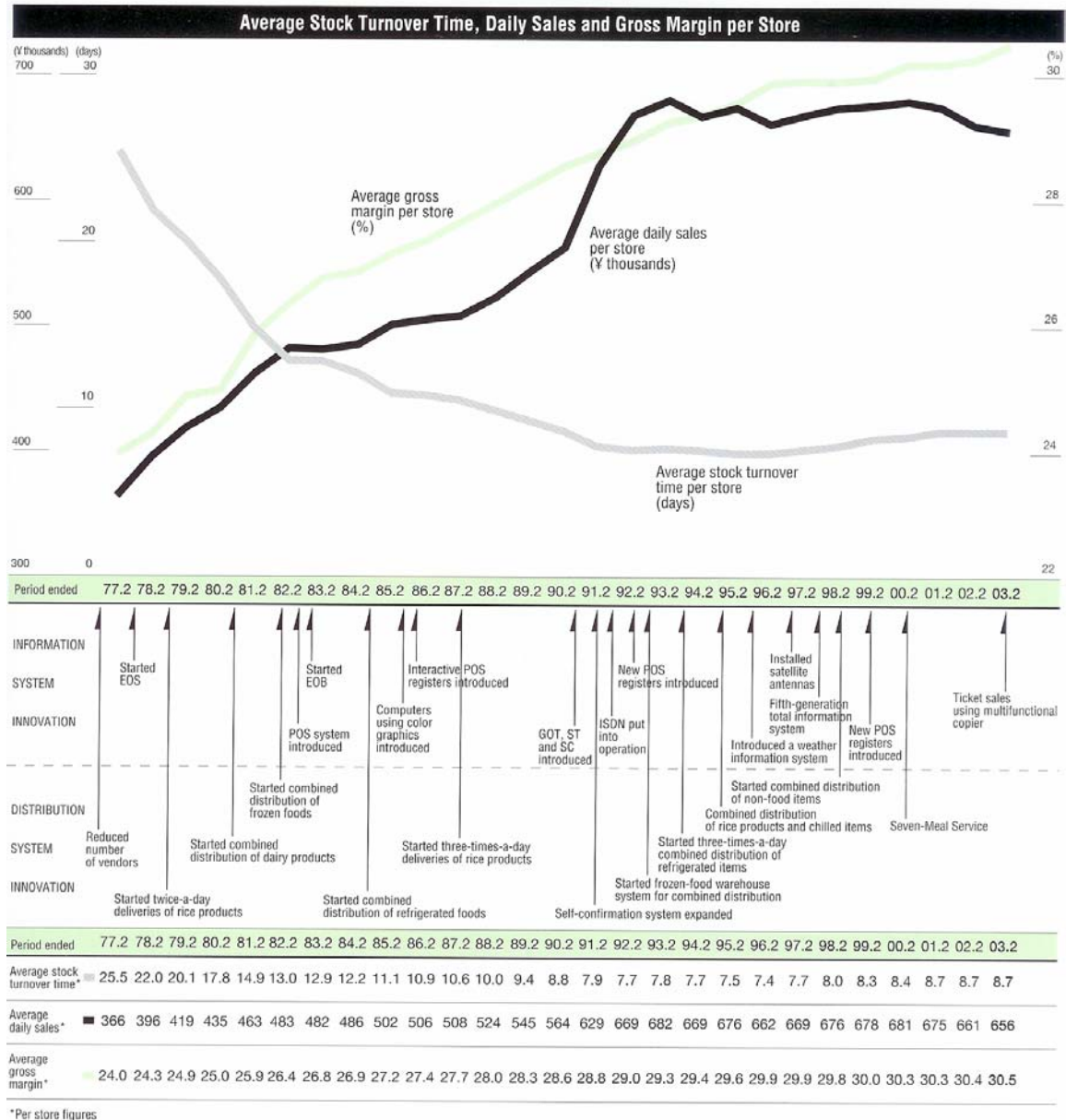
n Eleven Japan, "Corporate outline 2003"  
"Annual Report 2003")



(Source:  
Seven  
and



# **Exhibit 5** **Seven Eleven Japan** **Average Stock Turnover Time, Daily Sales and Gross Margin per Store**



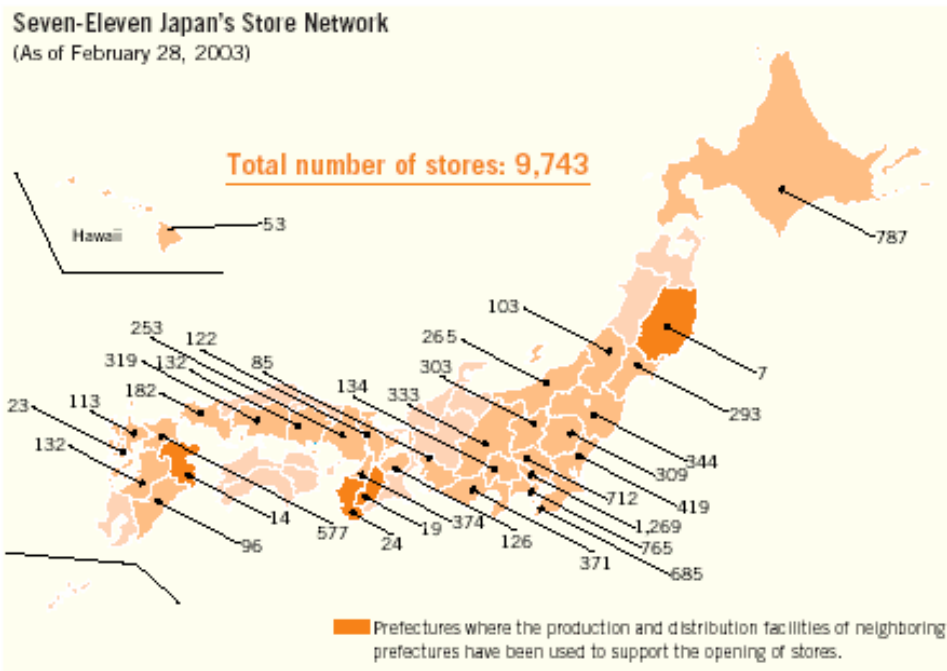
(Source: Seven Eleven Japan, “Corporate outline 2003”)

### Exhibit 6 Original Products by Team Merchandising



(Source: Seven Eleven Japan, “SEVEN-ELEVEN”, 2002)

### Exhibit 7 Store Location and Network

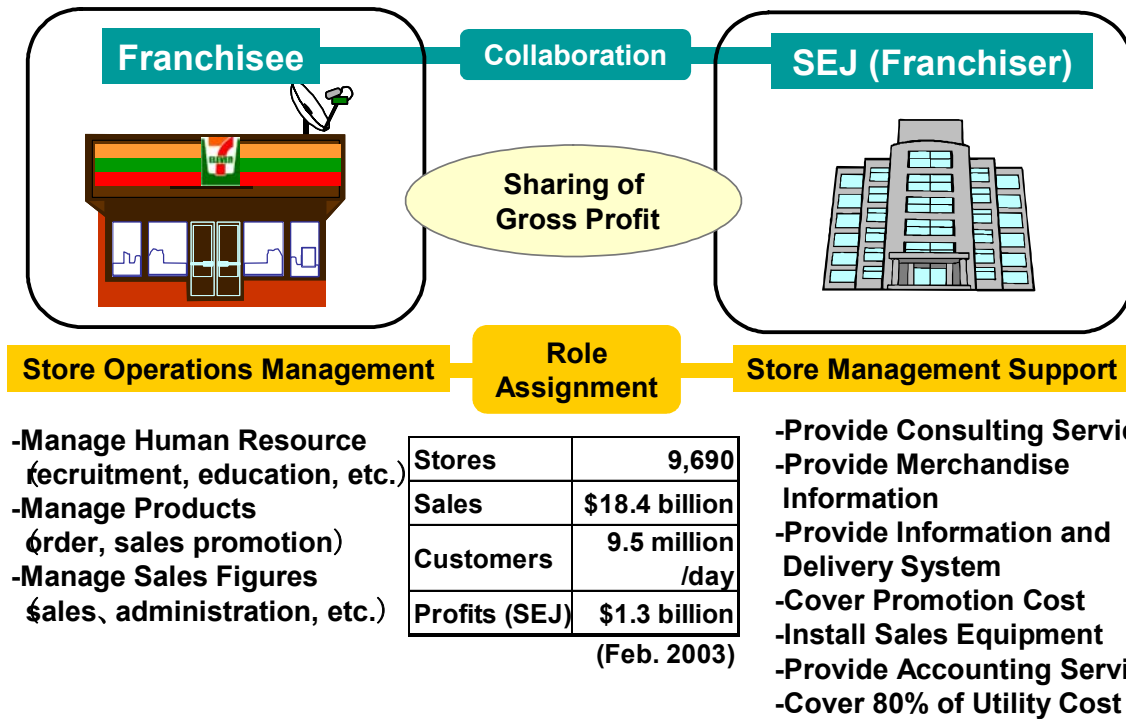


(Source: Seven Eleven Japan, “Annual Report 2003”)

## Exhibit 8 Franchise System of Seven-Eleven Japan

### Mutually Beneficial Relationship

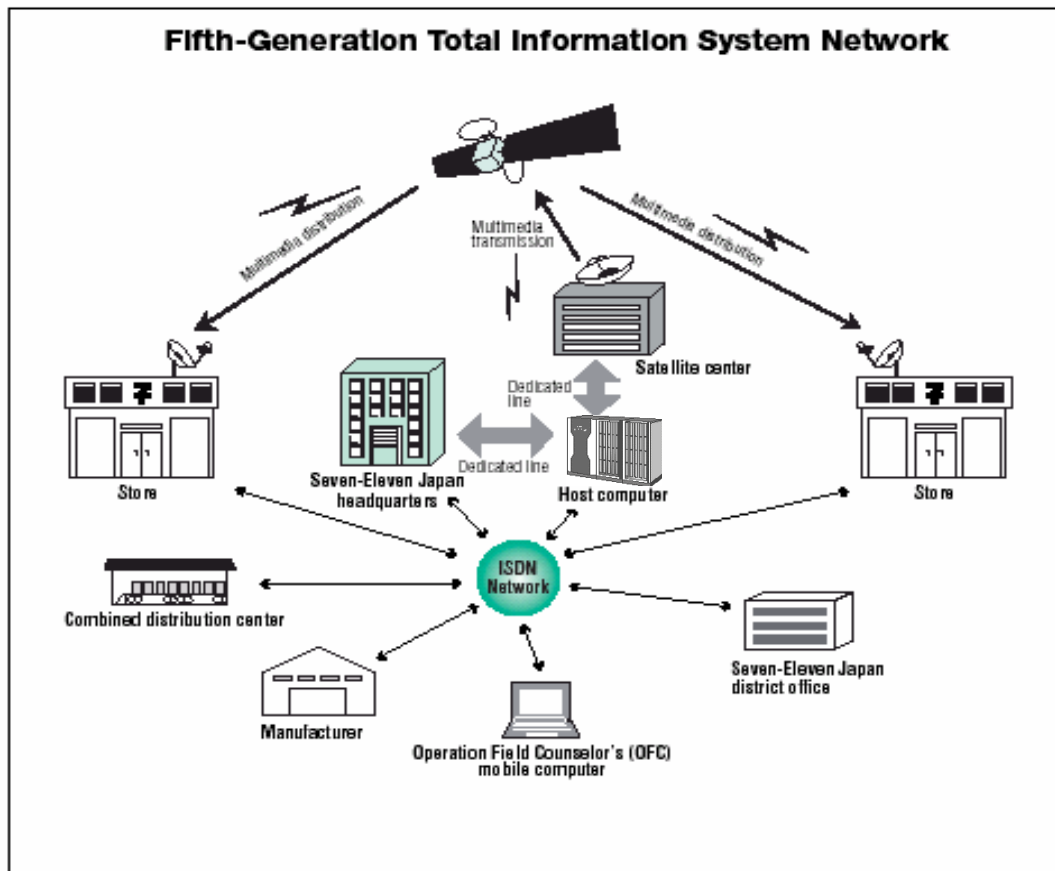
(Source:  
Seven  
Eleven  
Japan)






- Manage Human Resource (recruitment, education, etc.)
- Manage Products (order, sales promotion)
- Manage Sales Figures (sales, administration, etc.)

- Provide Consulting Service
- Provide Merchandise Information
- Provide Information and Delivery System
- Cover Promotion Cost
- Install Sales Equipment
- Provide Accounting Service
- Cover 80% of Utility Cost

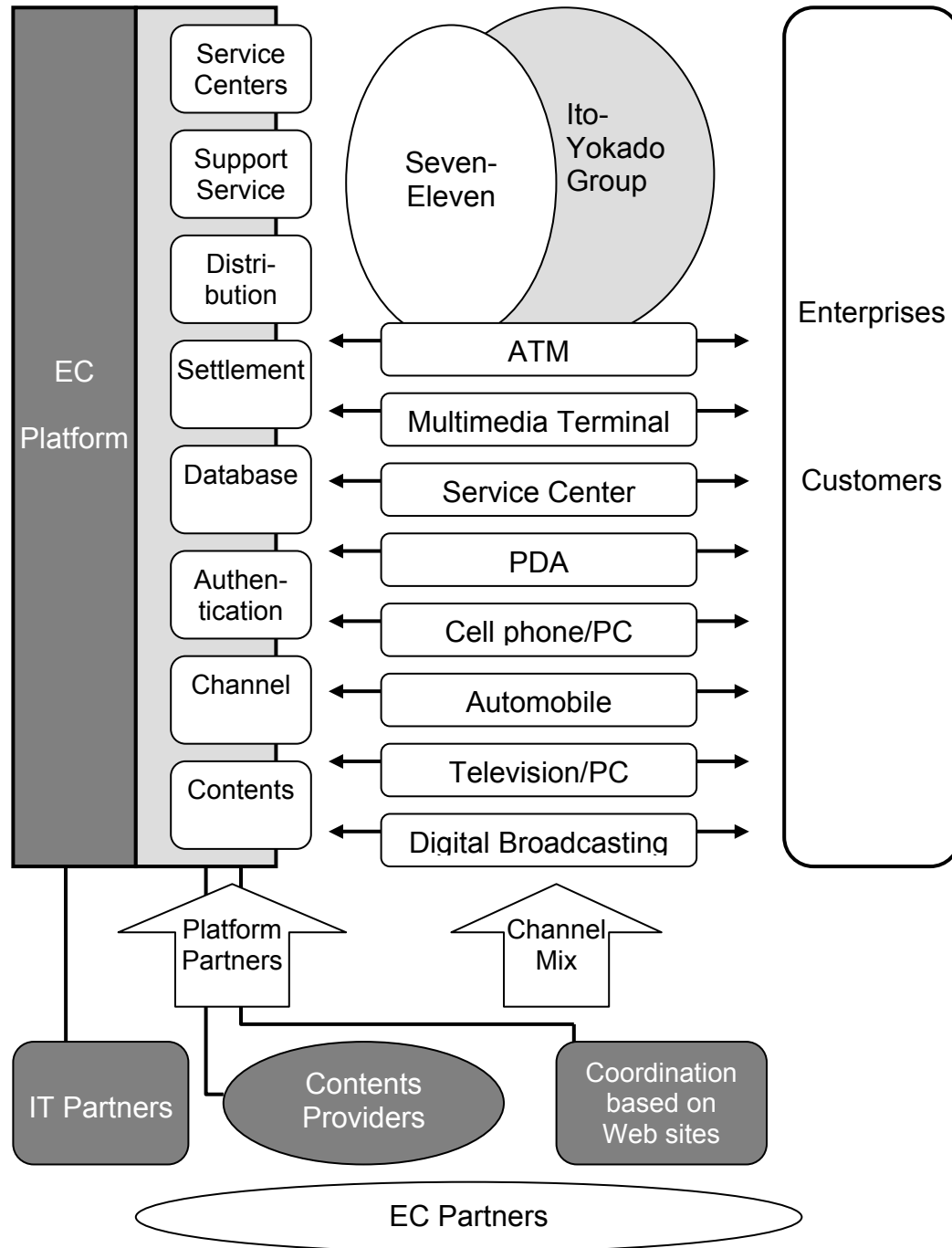
## Exhibit 9 Total Information System



<b>POS Cash Register</b>		<b>Graphic Order Terminal</b>
<b>Customer's View</b>		
<b>Store Computer</b>	<b>Clerk's View</b>	
<div style="display: flex; justify-content: space-around;"> <div style="text-align: center;">  <p>The system enables various information to be easily called up on a color monitor.</p> </div> <div style="text-align: center;">  </div> </div>		<div style="text-align: center;">  </div> <p>Color screen terminals confirm product display orders and out-of-stock items, enabling easy product ordering for employees at each store.</p>

(Source: Seven-Eleven Japan, "Corporate Outline 2003")

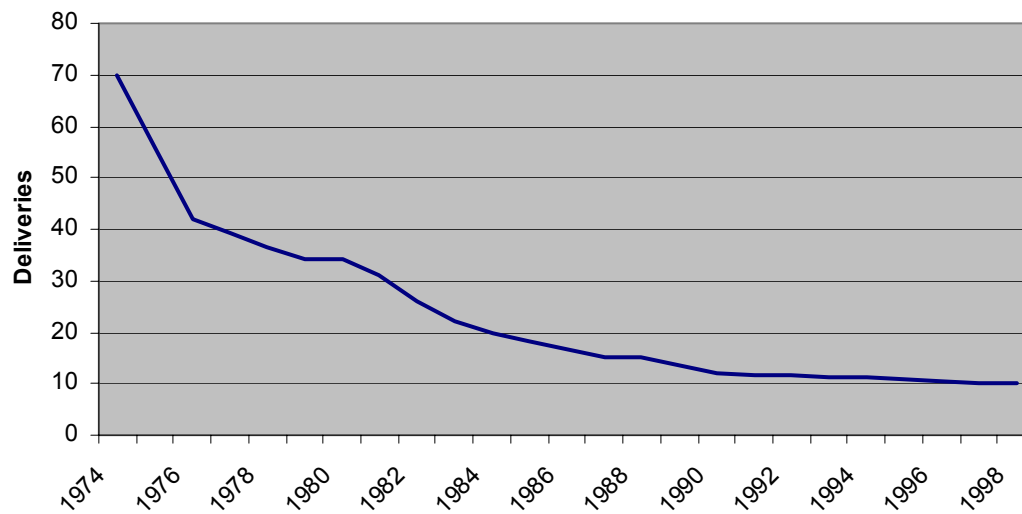
**Exhibit 10**  
**EC Platform**



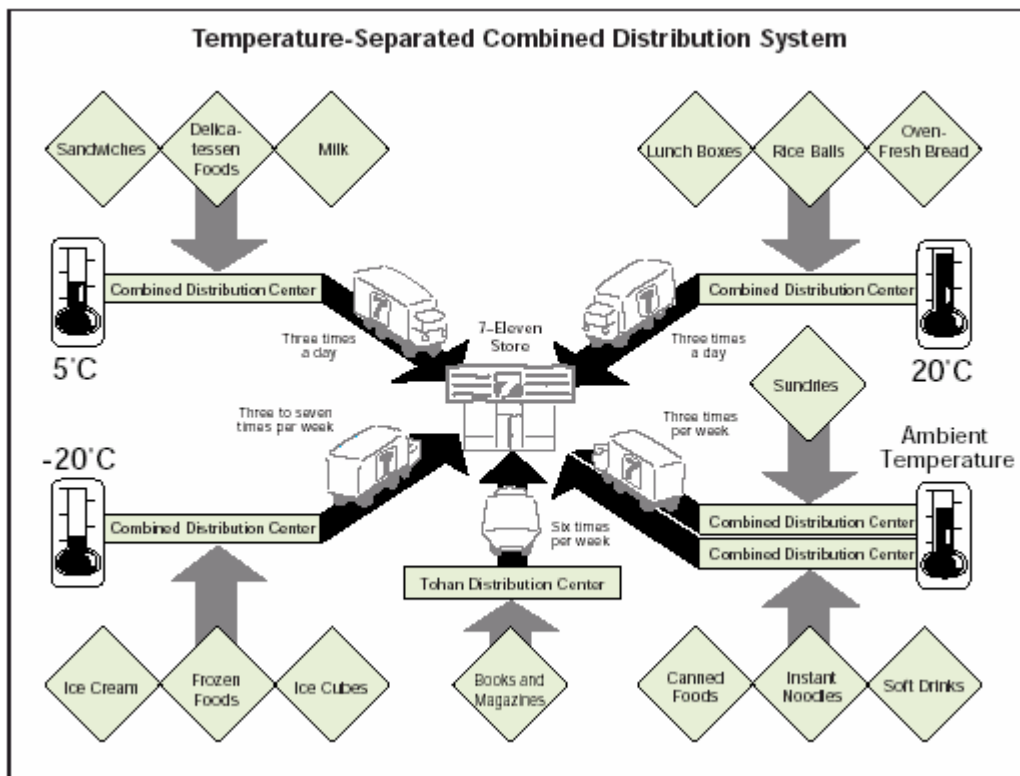
(Source: Seven Eleven Japan)

## Exhibit 11 Distribution System

### Number of Deliveries per Day



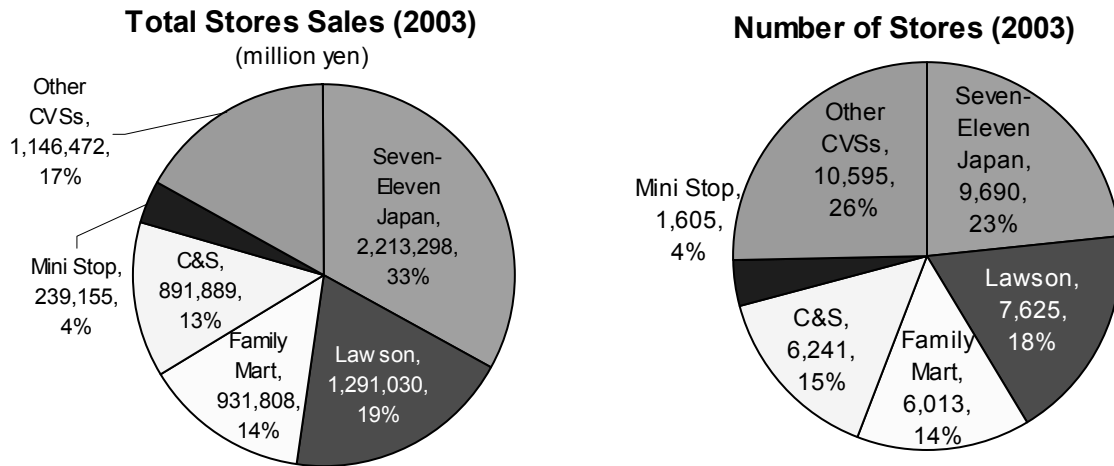
(Source: Seven Eleven Japan, “Corporate outline 2003”)



(Source: Seven Eleven Japan, “Corporate outline 2003”)

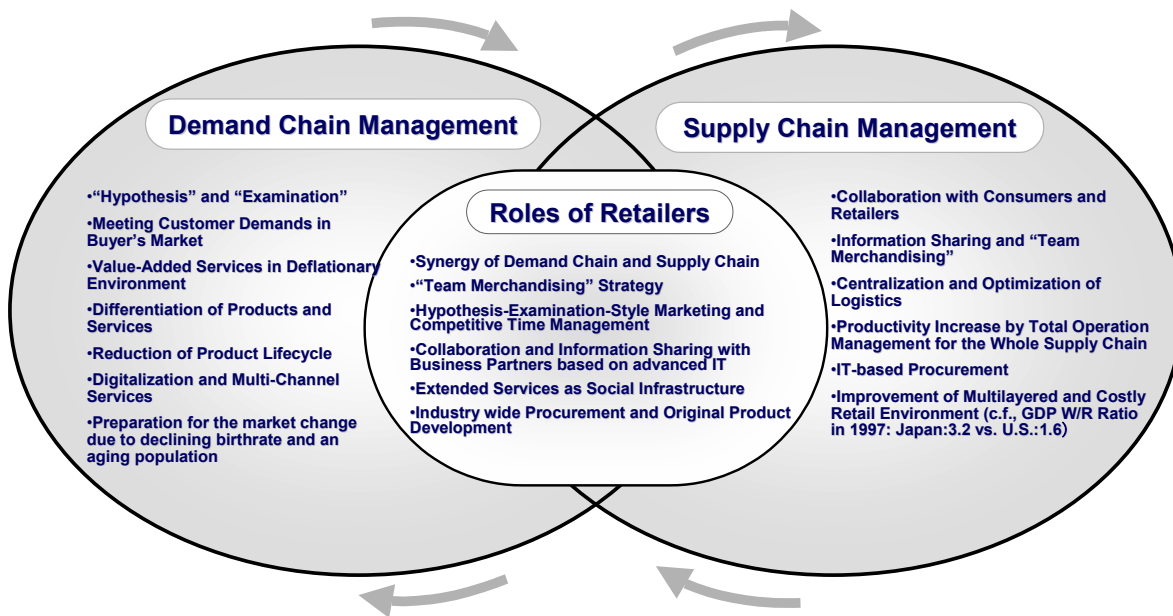


## Exhibit 12 Composition of major CVSs in Japan



(Source: Ito-Yokado Group Investors' Guide 2003)

## Exhibit 13 Synergy of Demand Chain and Supply Chain Management



(Source: Seven Eleven Japan)