



Japanese Mini-Banks: Retail Banking Services through Convenience Stores

William V. Rapp^a and Mazhar Islam^b

^aSchool of Management, New Jersey Institute of Technology, University Heights, Room CAB 3020, Newark, NJ 07102, USA.

E-mail: rappw@adm.njit.edu

^bCarson School of Management, University of Minnesota, Room 3-365, Twin Cities, 321 19th Avenue South, Minneapolis, MN 55455, USA.

E-mail: mislam@csom.umn.edu

This paper analyzes how leading Japanese convenience stores (CVS) have organized themselves over the last two decades to offer services more typical of retail banks. These stores act as mini-banks and offer loan repayments, utility bill collections, online purchase payments, funds transfers and credit cards. In addition, most stores offer more sophisticated financial services through automated teller machines and multimedia kiosks, often leveraging partner relationships. The main drivers in the evolution of mini-banks are CVS' strength in the strategic application of information technology, opportunities in the Japanese financial sector resulting from a series of government-initiated reforms and the continued weakness of many Japanese banks following the collapse of the Bubble. Leading CVS have strategically combined these drivers in developing their mini-banks, while exploiting their 24 × 7 advantage. This mini-bank model creates value for CVS in three ways. First, it generates commissions from financial transactions. Second, it increases store traffic. Finally, it enhances customer loyalty through unique services for which customers come back to a particular CVS chain. This different business model thus potentially offers an interesting banking paradigm that could be replicated in other parts of the world if similar environments and opportunities exist. 7-Eleven appears to be experimenting with this in the US.

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Introduction

Japanese convenience stores (CVS) are neighborhood nerve centers where locals often congregate. These stores not only sell food, snacks and stationery but also offer a range of services to customers, including many financial

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services typically offered by traditional retail banks. In recent years, these financial services have become quite sophisticated and in some ways have changed the structure of Japanese retail banking.

To study the evolution of the CVS mini-banks, we need to look at the underlying economic drivers that have influenced the creation of this business model. Three major drivers emerge as the main forces behind their strategies. First, a number of services in the financial sector were liberalized for competition in recent years through a series of legislative and regulatory reforms. These reforms led to a more open financial services industry where both foreign and non-financial firms can now enter and operate. Second, the collapse of Japan's bubble economy weakened many major Japanese banks, creating a marketing vacuum. Third, the leading CVS have employed and managed information technology strategically to develop their internal strengths and efficiently provide these services. These CVS have been at the forefront of using information technology to integrate a network of stores with suppliers, including suppliers of financial services. Acting as real-time portals, CVS mini-banks have thus evolved from the strategic combination of opportunities and strengths. Other factors contributing to the development of the mini-banks include the CVS's capability to form alliances with related as well as unrelated businesses, their experience in non-financial services and their management's visionary leadership.

This paper is organized as follows: In the next section, we present a brief assessment of Japan's post-war financial system and how its structure has changed and evolved, given a series of reforms to support mini-bank development. In the third section, we offer a short overview of CVS in Japan and the logic behind its mini-banks. In the fourth section, we study the information technology initiatives of the leading Japanese CVS, since IT as a core competency helps support their evolutionary growth into retail financial services. In the fifth section, we present an analysis of how the leading CVS have been successful in strategically combining external opportunities and internal strengths in offering various financial services. In the last section, we discuss possible analytical contributions of this study to an understanding of the retail banking industry. Then, because this is an evolutionary and continuing process, in the concluding section we present some ideas for future research.

Post-War Japanese Financial System

Japan's financial system has gone through dramatic changes since World War II. The US Occupation dismantled the *zaibatsu*, the industrial groups that dominated the economy in the pre-war period. American reform policy was



aimed at the democratization and demilitarization of the wartime economy and the elimination of economic concentrations. It initiated a series of dissolution measures, including the enforced sale of holding companies' shares to the public, prohibition of inter-corporate stockholding among *zaibatsu* firms, etc. (Choi, 1999).

These sweeping changes had major impacts on Japan's financial system that persisted even after the reversion of sovereignty and ultimately helped the emergence of the mini-banks. First, Japanese regulators decided to segment financial services based on the type of financing or financial instrument each firm provided. For example, long-term credit banks could issue debentures and provide long-term loans, while trust banks could finance and manage certain real estate transactions. Second, they restricted price and non-price competition among participants in each segment. Third, they restricted firms' ability to raise capital. Two policies that made raising capital particularly difficult were requiring issuers of public debt to have a high capital base and forcing substantial disclosure of corporate information.

Still, the prewar *zaibatsu* firms progressively re-established their links with the major *keiretsu* financial firms, facilitated by a revision of the Anti-Monopoly Law in 1953. As Japan grew over the next two decades, so did its financial markets, but by using indirect finance that was mainly bank-based. Stock and bond markets were deliberately underdeveloped. The structure of the banks remained stable and the different types of banks continued to be segmented by function and size of customer. There were no new entries, and virtually no bank failures or mergers. In essence, the regulatory regime guaranteed that banks would not fail, effectively protecting management, stockholders and depositors (Patrick, 1998). However, this meant virtually no competition or innovation, as management was insulated from outside pressures.

However, the first liberalization in a series of deregulations came after the oil crises of the 1970s. The Japanese Diet amended the Foreign Exchange and Foreign Trade Control Law in 1980. This allowed some of Japan's large accumulated savings to flow across the Pacific to the US to earn a higher rate of return, helping to finance the expanding trade deficit between Japan and the US, as a weaker Yen led to more exports. The Japanese government further reduced capital controls by implementing the US–Japan Yen–Dollar Accord in 1984 (Radin, 1999), leading to a step-by-step deregulation of interest rates and a much greater opening of Japan to foreign financial firms.

Liberalization gave a big boost to Japanese financial markets and financial services firms. Indeed, during the 1980s, the economy went through unprecedented expansion, now referred to as the 'Bubble'. Trade and current accounts increased enormously during this period and financial institutions experienced a huge inflow of funds. As a result, the government



did not initiate any key structural reforms during the latter half of the 1980s, except to develop a futures market for government bonds and stock indices that played a role in the Bubble's spectacular collapse from January 1990 (Rapp, 1999).

In response to the Bubble's collapse, the government initiated the Financial System Reform Act of 1993. This drastically deregulated the financial system by allowing institutions to cross lines that were previously segregated, such as banking, securities, and insurance, paving the way for universal banking, and it intensified competition in consumer financial services. While evolutionary in nature, this deregulation process between 1980 and 1993 was often helped along by external pressures, but after the Bubble's total collapse with no substantial recovery, the government felt it had to develop a more radical deregulation program for all financial services. In late 1996, Prime Minister Ryutaro Hashimoto pledged a 'Tokyo Big Bang', modeled after the 1975 Market Day reforms in the United States and the 1986 Big Bang in Great Britain (Nakamura, 2002).

Its main goal was progressive financial sector reform that would bring Japan's financial markets and institutions on a par with those of New York and London by 2001 by making them 'free, fair and global'. While a huge provider of global capital in the 1980s, by the mid-1990s Tokyo greatly lagged behind New York and London as an international financial center. In fact, it had started losing market share to other Asian financial centers, notably Hong Kong and Singapore.

Patrick (2001) describes the post-'Big Bang' status of the Japanese financial system as follows: 'the old post-war, convoy-style, highly regulated system with all its inefficiencies no longer exists. Deregulation, the Big Bang package of capital market reforms and real competition in financial markets has gone a long way to the creation of a free, open, market-based financial system in which capital markets are playing an increasing role'. The 'Big Bang', therefore, changed the structure of Japan's financial system far more than earlier reforms. In particular, a wave of mergers and acquisitions led to the formation of large universal mega-banks. Further, a number of foreign banks and financial institutions entered the market to take advantage of the emerging opportunities. As a result, competition intensified. In addition, non-financial firms such as CVS entered into financial services. For example, in less than a year between 2000 and 2001, four banks were launched by non-financial firms, all heavily dependent on information and communication technologies (Table 1).

Ito-Yokado (IY), the largest supermarket chain, and its subsidiary Seven Eleven Japan (SEJ), the largest convenience store (CVS) chain in Japan, established IY Bank, the first non-branch Japanese bank to be granted such a license. Besides SEJ, Lawson and FamilyMart, two other leading CVS chains,



Table 1 New types of banks in Japanese market

| <i>Bank</i> | <i>Launch date</i> | <i>Activities</i> | <i>Promoters and partners</i> |
|----------------|--------------------|---|---|
| Japan net bank | Oct. 2000 | Internet banking | Sumitomo Mitsui Banking Corporation Fujitsu Nippon Life Insurance am/pm convenience store chains |
| IY bank | May 2001 | ATM Convenience stores as outlets Money transactions | Ito-yokado Seven Eleven Japan |
| Sony bank | June 2001 | Internet banking ATM Savings, loans, financial products for individuals | Sony Corporation Sumitomo Mitsui Banking Corporation JP Morgan am/pm convenience store chains |
| eBank | July 2001 | Internet Banking Mobile Phone Banking | Japan Telecom Co. Ltd. Itochu Group Mitsui Marine & Fire Insurance |

Source: Authors' compilation from various news media.

have been providing some financial services and have now started to offer additional ones.

These initiatives are based on the fact that Japanese CVS have been aggressive users of information technology (IT) to offer new services, increase efficiency and improve product offerings. Indeed, for the leading CVS, such strategic use of IT is now a core competency, since they have used IT strategically to link stores, franchise owners and management before their counterparts in other countries. Moreover, all leading Japanese CVS have been providing some financial services for some time, such as collecting utility bills, selling money orders, and collecting insurance premiums, all based on the efficiency of their IT systems and their links to various companies. Therefore, IT infrastructures and experience in financial payment services gave these leading CVS the capability to efficiently offer an expanded array of consumer financial services when the 'Big Bang' reform opened doors; and traditional banks, reflecting their historically passive approach to strategy, failed to aggressively solicit customers. In the rest of this paper, we examine how these CVS have combined their strengths with the opportunities offered in a deregulated financial system to develop what we call 'mini-banks'. However, to understand the strategic goals behind the mini-banks and the related efficiencies, beneficial externalities, and core competencies supporting them, it is critical to first appreciate the large Japanese CVS's basic business model.



The Japanese Convenience Store Industry

Japanese CVS are very different from their counterparts in other countries. Since they began expanding rapidly about 30 years ago, these stores increasingly have become neighborhood nerve centers. In spaces typically no larger than 100 m² (1079 square feet), these tiny stores now carry as many as 3,000 different items. They also take advantage of their 24 × 7 presence and provide a range of services, such as paying utility bills, making insurance premium payments, offering courier services, paying for online-shopping and Automated Teller Machines (ATM).

CVS were first introduced in the US about 70 years ago. The first in Japan, My Shop, was established in 1969. However, it was in 1974, when Ito-Yokado bought a license from the Southland Corporation of the United States to launch SEJ, that the CVS business there really took off. Since then, the number of CVS stores has continued to grow, reaching 10,000 in 1980 and over 20,000 in 1992. Today, there are more than 40,000 such outlets. Indeed, Japan has, by far, the highest number of CVS *per capita* compared to any other country.

During the 1990s, large CVS enjoyed relatively better performance than general merchandise stores (GMS). While GMS experienced declining sales due to increased competition and the economic downturn, CVS sales rose from ¥3.89 trillion in 1993 to ¥6.18 trillion in 1998. Then, however, they fell slightly in 1999 to ¥6.13 trillion, but again increased, reaching ¥6.71 trillion in fiscal year 2002 despite the general deflation (Rapp and Islam, 2003).

Competition among the large CVS and against other retail sectors having intensified, the time is past when the CVS sector as a whole could enjoy good growth. Rather, future success requires deploying better merchandising strategies, offering more services such as financial services, making greater use of IT, having superior strategic site selection, and providing better franchisee and staff development. Four chains, comprising about three-quarters of CVS sales, dominate the industry. The top three are discussed in this paper. The fourth is Circle K–Sunkus, the result of the three-way merger of C&S, Circle K and Sunkus in 2004.

SEJ is the largest CVS in Japan by both sales and number of stores. It does not operate nationwide, but is heavily concentrated in the Greater Tokyo (Kanto) region, with a strong presence in Osaka. Ito-Yokado (IY), the No. 2 Japanese retailer by sales, but the most profitable supermarket chain in Japan, owns 50.6 per cent of SEJ. The US-based 7-Eleven is managed relatively independently, although IY and SEJ jointly hold 72.5 per cent of the shares and have pushed it to introduce more food items and services. SEJ claims their per store and per square meter sales are at least 50 per cent higher than any major competitor, and it is generally recognized it has achieved this through flexibly supplying its stores with a wide variety of goods and services, especially



with different food items during the day in response to its clients' actual consumption patterns. In turn, it appears to be using its greater efficiency to further increase market share (SEJ, 2004).

Lawson, the No. 2 CVS, headquartered in the Osaka area, is the only chain operating in every prefecture in Japan. The company was established in 1975 as a subsidiary of Daiei, Inc., Japan's largest GMS. Preoccupied with its own troubles, Daiei has been reducing its shareholding, making the company more independent, though it has come increasingly under the influence of Mitsubishi Corporation. Lawson has its own brand and tries to capitalize on it by identifying itself with the quality of its product. In addition, it has organized itself to cater to a particular health-conscious customer segment. For this reason, it launched a line of completely new stores called Natural Lawson, which only sell naturally grown food products. The staff of these stores is qualified to give advice on eating well. Apparently, this strategy is working well for Lawson and it has reported that many customers travel a considerable distance to shop in these stores.

FamilyMart, established in 1981, is the third largest CVS in terms of sales. Stores are primarily in greater Tokyo and Nagoya (Japan's third largest metropolitan area). Formerly a member of the Seibu Saison group, it has been considered part of the Itochu group since 1998. FamilyMart typically does not compete in the low-cost market; instead, it forms alliances with manufacturers to produce exclusive high-end products for its stores. It also differentiates itself from other chains by focusing on excellent customer service and cleanliness of its stores. To implement this strategy, FamilyMart launched a program called Store Staff Total System (SSTS) in spring 2000. This is a systematic program that focuses on attracting, educating, motivating and remunerating store staff.

Table 2 summarizes key data for the leading Japanese CVS.

Table 2 Key data for leading Japanese CVS^a

| | <i>SEJ</i> | <i>Lawson</i> | <i>FamilyMart</i> |
|--|------------|---------------|-------------------|
| Total domestic store sales (¥ billion) | 2,343 | 1,285 | 954 |
| Revenue (¥ billion) | 445 | 246 | 229 |
| Operating income (¥ billion) | 167 | 38 | 29 |
| Number of stores in Japan | 10,303 | 7,821 | 6,199 |
| Average daily sales per store (¥ thousand) | 647 | 484 | 464 |
| Gross margin (per cent) | 30.6 | 30.7 | 28.5 |

^aFiscal years ending last day of February in the following calendar year (here 29 February 2004). NB: company reports vary in terms of the year they cover; so sometimes the 2003 annual report will cover FY 2003 ending February 2004, but sometimes this will be called the 2004 report and the fiscal year 2004. SEJ in particular seems to now refer to the year ending 2004 as FY 2004.

Sources: Authors' compilation from company annual reports.



Information Technology in CVS

The Japanese CVS are pioneers in the strategic use of information technology. Led by the industry's leading firm, SEJ, all the top CVS depend heavily on robust IT infrastructures to strategically manage their network of stores. Ishikawa and Nejo (1998) report that during 1997–1998 SEJ's information system was the world's largest retailing network and in 2004, it was still one of the largest retail IT systems globally. In the following sections, we discuss the major IT initiatives that underpin SEJ's mini-bank strategy. Since the two other leading CVS, Lawson and FamilyMart, are typically followers in implementing IT, we limit our discussion to SEJ.

SEJ realized the importance of IT from the very beginning of its operations. Since then it has aggressively invested in introducing IT to create a competitive advantage (Rapp, 2002). The core of SEJ's IT infrastructure is a robust network that it calls Integrated Information System (IIS), developed over the past two decades through an evolutionary process. In November 1997, SEJ introduced its fifth-generation IIS, linking all its stores, headquarters and suppliers through satellite telecommunications and an integrated services digital network (ISDN) (SEJ, 2004).

In 1978, SEJ first linked all stores with headquarters through a simple IIS to establish an efficient ordering mechanism. It also installed an Electronic Ordering System (EOS) that allowed store managers to place orders directly to headquarters. Subsequently, headquarters combined orders from all stores and sent them to particular suppliers through ordinary mail. Unfortunately, government regulators did not then allow different businesses to connect to one another by information systems, so although this IIS improved work efficiency, it was limited to slow and unreliable telephone lines.

In 1982, SEJ was the first CVS in Japan to introduce a Point of Sales System (POS) to collect sale-related information. Stores collected part of the information, such as price and product codes, from barcodes. Sales clerks manually recorded other information, such as customer age and gender, while taking payments. Information from the POS system was sent directly to headquarters, where managers analyzed the products that were selling and those that were not at each store. Only products selling well were ordered for individual stores. This process of elimination that SEJ termed 'item-by-item control' continued until each store ended up displaying only items that were expected to sell well in that store. Other notable developments were Electronic Order Booking (EOB) terminals, replacing the bulky EOS and liquid crystal display terminals with advanced features that reduced order input time. In addition, with a change in government regulations, SEJ could now link its IIS to suppliers so orders could be placed directly. These developments significantly reduced order-placement time.



Competition among Japanese CVS intensified in the mid-1980s as SEJ lost market share. To safeguard its competitive position, SEJ tried to improve IIS by replacing the earlier system. As part of the process, SEJ installed computers capable of graphical display in its stores, which helped store managers analyze sales data more efficiently. In addition, the new interactive POS could collect more information about customers, helping to develop customized products. With the new POS, store managers could directly access the server at headquarters to retrieve information. Thus, for the first time communication between stores and headquarters became truly two-way.

In the early 1990s, SEJ further upgraded IIS. The main feature was a high-speed ISDN line for data communications. This ISDN was built on client-server technology. Other notable features were Graphic Order Terminals (GOT) and Scanner Terminals (ST) that had better interfaces. To improve the ordering process further, SEJ installed STs in each store, enabling store managers to monitor the ordering process. Finally, the POS terminals were improved, becoming easier to handle.

In 1999, SEJ again upgraded its system and implemented its fifth-generation IIS, jointly developed by 12 companies, including Nomura Research (NRI), NEC, and Microsoft. SEJ invested approximately 60 billion yen in the project. This was the first time SEJ used satellite telecommunications besides an ISDN to link stores, headquarters and suppliers. The new system is capable of handling vast amounts of multimedia data at higher speeds than before and has reduced communication costs by about 20 per cent. In addition to the POS, special sensors installed in stores collect customer data, and the more advanced POS can collect a wide range of information about each customer. Moreover, warehousing and data-mining tools help managers to relate and analyze the different information about customers to predict order requirements by forecasting buying behavior. SEJ's IT initiatives have paid off enormously in terms of market share, profit margin and store management, forcing competitors such as Lawson and FamilyMart also to invest in IT infrastructures.

A key strategy for leading Japanese CVS in using IT has been to continually add services to attract store traffic, even if these services do not contribute directly to profits. The store ideally wants a customer to buy some food items for immediate consumption as well as items for later use, while making payments and using the shipping services (Rapp and Islam, 2003). As part of this strategy, in the next section we discuss some financial services that leading CVS have begun to provide in a deregulated financial market utilizing their integrated IT systems. These have gradually evolved into mini-banks.



Combining Strength and Opportunity: Evolution of CVS Mini-Banks

Competition among the leading CVS has intensified in recent years. Thus, it is absolutely necessary that CVS continuously strive to satisfy customers' changing needs in order to retain them. Failing to do so would be adverse, as customers can always find a different store to get the products or services they need. Therefore, to safeguard themselves, CVS not only sell merchandise but also provide a variety of services that leverage their strength in IT. This strategy has worked well since they first started collecting third-party payments in the late 1980s. As discussed earlier, financial services have been deregulated through a series of reforms over the past two decades, opening the door for the CVS and enabling them to harness opportunities in financial services using their strength in the strategic use of IT. Leading Japanese CVS now offer utility bill collection, third party e-commerce purchase payment collection, insurance premium collection, foreign exchange services, loan repayments, credit cards, etc. In addition, customers can access their bank accounts by using in-store ATMs or multimedia kiosks (now onward kiosk), while conducting various transactions. All these services are typical of retail banks in Japan, which is why we call them mini-banks.

The evolution of Japanese mini-banks has major implications for CVS. First, by establishing mini-banks, CVS create value through economies of scope that are crucial to the successful exploitation of their IT investments. Simply broadening a firm's activities can lead to diseconomies of scope, as many failed conglomerates have often demonstrated. But offering more products or services through the same infrastructure can reduce costs per sale. Second, mini-bank services not only generate commissions and fees, but increase sales through impulse purchases due to greater store traffic. Finally, the services tie a customer segment to a particular CVS chain, thereby creating value through increased customer loyalty, repeat sales and more store visits.

We can categorize the evolution of the mini-banks into three distinct levels based on service sophistication at any point of time. This level of sophistication is the result of two major drivers: internal strength in using IT strategically and opportunities in a deregulated financial services market. We will analyze mini-banks from these two perspectives.

Mini-Bank Sophistication Level I

In the first stage, CVS began collecting utility bills for power, gas, telephone and water companies; SEJ was the first to collect bills for Tokyo Electric Power Company in 1987. Other chains followed and started forming alliances with regional utility companies to provide similar services. Since then this has been a win-win strategy for utility companies and CVS. The former can reach their



customers after regular office hours with low marginal costs, and the latter receive commission from the transactions and the benefit of increased store traffic. The services also bring greater convenience to customers.

CVS then added the sale of money orders in 1995 after that was deregulated. Though selling money orders seems a simple business process, it is significant from the perspective of the CVS because it is a real-money transaction rather than just bill collection as before. This was a paradigm shift for mini-banks.

During this stage, SEJ used its third-generation IIS. This system allowed stores to access the headquarters' servers directly and to transfer data over telephone and SEJ lease lines. SEJ used this two-way communication channel to process its utility payment data. However, in most cases, data were sent to headquarters on floppy diskettes, sometimes taking a week, since telephone and lease lines were slow in transferring large volumes of data.

However, from the 1990s data transfer became both faster and cheaper after SEJ implemented its high-speed ISDN lines. While at that time SEJ was unable to provide additional financial services using this state-of-the-art system, as financial regulators had not yet allowed non-financial firms to fully enter the business, it was still an important change because existing services could be handled more efficiently. This raised the level of mini-bank sophistication by giving the CVS a better understanding of how to handle financial data, creating a solid platform for later introduction of more sophisticated financial services.

Mini-Bank Sophistication Level II

This development positioned them strategically to exploit the 'Big Bang' reforms in late 1996, when Japan's financial markets began to open: 'Opportunity favors the prepared mind'. Thus, the most significant change for the CVS was the opening of financial services to non-financial firms, since this ushered in a new era for the mini-banks where they could offer more and more sophisticated services. Then, in April, 1998, the foreign exchange law was relaxed, allowing non-financial firms to enter into foreign exchange too, and SEJ started offering foreign exchange services. SEJ could handle the necessary real-time data for foreign exchange transactions thanks to their high-speed ISDN lines, and other CVS with similar capabilities followed.

Besides foreign exchange, other types of financial services the mini-banks started to provide were automated teller machines (ATM), kiosks and credit cards. The 'Big Bang' reform slowly opened these services to non-financial firms from the late 1990s. However, CVS needed high-speed networks to support them, and SEJ with its state-of-the-art system was perfectly positioned to do this, whereas Lawson and FamilyMart had to rely on third parties for support.



ATMs are considered bank branches under Japanese banking regulations. So leading CVS chains, other than SEJ, formed alliances with one or more banks to install ATMs in their stores. The banks thus control the ATMs and branching. Since IY and SEJ wanted to control the services available through their ATMs, as well as the number, they decided to establish their own 'IY Bank' in 2001. As such, IY Bank became the first bank in Japan without conventional branches. It operates entirely online through its store-based ATMs, the Internet, and telematics (discussed later). On the other hand, the other five leading CVS, the city banks, IBM Japan and other investors established a new company called e-Net to install ATMs in some other CVS in 1999. The CVS in this alliance are FamilyMart, Circle K Sunkus, Three F and MINISTOP. Similarly, Lawson formed alliances with the four major banking groups and several major regional banks to form LAWSON ATM Networks in 2001. These ATMs can be linked to Loppi, Lawson's multimedia kiosk, to provide a variety of financial services, but these two groups are essentially responding to SEJ's initiatives.

As a key part of their retail banking strategies, SEJ, Lawson and FamilyMart have launched credit cards through affiliated companies. JCB, Japan's indigenous competitor to Visa and MasterCard, markets a card jointly with SEJ and IY. FamilyMart uses a 'smartcard technology' that provides both point-award and credit card functions. Besides JCB, FamilyMart's partners are C. Itoh, Toyota Finance, PIA, and NTT Data. Lawson established LAWSON CS Card Inc., a joint venture with Mitsubishi Corp and Credit Saison Co. Ltd, to launch its credit card business in February 2002. All three have integrated their credit cards with their stores' point programs to increase traffic. Customers receive points for all purchases, not just those at the issuing CVS. The cards thus serve the two purposes of building customer loyalty and providing revenue from financial services. It also helps each CVS to collect valuable information about its customers that they can then use for marketing and product development purposes.

Lawson is the CVS leader in multimedia kiosks services. It launched its Loppi (Lawson Online Shopping Print and Pay Information) kiosk in early 1998 and completed putting one in every store by that October. Lawson sourced Loppi, in terms of development and manufacture, from IBM. Loppi has two major features, an entertainment element for purchasing event tickets or downloading game software, and an information platform providing data on events, weather, and suchlike. The system also supports payments, including payments to financial institutions on loans, and is thus part of its mini-bank operation. Logically, Lawson has recently linked the Loppi network directly with its in-store ATMs and started offering financial services like billing settlements and repayment of loans from financial institutions. A major part of the revenue comes from mini-bank bill settlement services.



FamilyMart launched its kiosk, Famiport, in 2001. These kiosks are made by a Toyota–Fujitsu joint venture using a software platform, e-plat, developed by a Toyota–NTT Data joint venture. The ordering and payment system connects to a communications and computer center run by Toyota. NTT Data handles the actual settlement in conjunction with e-net.

SEJ has not been very successful in providing financial services using a kiosk. But, unlike Lawson and FamilyMart, SEJ owns and controls its ATMs, so it may well enhance the capabilities of its ATMs to offer a variety of financial services that its competitors are providing with kiosks, particularly by leveraging its various partnership relations. In this way, mini-banks, after the ‘Big Bang’ reforms, have been able to raise the level of their services as the leading CVS have begun offering financial products that they could not before. Although their strength in IT played a positive role, it was the opportunities offered by a deregulated financial system that led to these more sophisticated financial services.

Naturally credit cards and ATM services were available in Japan long before the CVS launched theirs, but the CVS offered them to an expanded number of customers. Kiosks were introduced initially to provide services such as downloading games on CDs, selling concert tickets, printing digital photos, applying for cellular phones, and requesting hotel reservations. But later, given deregulation, they were linked to the CVS’s ATM networks to provide financial services. Kiosks are thus now an advanced channel for financial services that have emerged in an evolutionary manner in terms of available technology and CVS mini-banks.

Mini-Bank Sophistication Level III

Recently, the leading CVS have begun to provide a further set of financial services. As opposed to financial sector reform, the main driver for the previous introduction of new services, IT and technology, especially wireless-based technology, are the main drivers for these newer, more sophisticated services. Some of these emerging CVS financial services are discussed below.

e-money

CVS chain am/pm started accepting Edy (for Euro, Dollar and Yen) electronic money (e-money) in November 2001. In fact, am/pm was one of the first stores of any kind to accept e-money in Japan. Users of Edy only need to place the card within 10cm of an Edy sensor to have the money debited. Because the money is stored on the card, it is not necessary to check a bank computer or database. Edy cards use integrated circuit (IC) technology and can be charged



from special terminals. Since August 2003, am/pm started installing Edy-charging terminals in its stores. Other leading CVS, including Lawson and C&S, have recently started using Edy on a test basis as well. Japan is considered to be the leading potential market for e-money, because, although it is a wealthy advanced economy, it is still a cash-dominated society and consumers equate debit cards with credit cards, which they use sparingly.

e-brokerage

In September 2003, Lawson announced its strategic alliance with Nikko Cordial Securities (NCS), a Citigroup affiliate, to offer securities services through its Loppi multimedia kiosks. Under the proposed alliance, Lawson and NCS will leverage their complementary resources and know-how to build a security-brokerage business model using multimedia terminals and offering services through ATMs at each other's branches. The alliance initially plans to use Loppi to offer services like opening new trading accounts, trading of securities and government bonds, stock price quotes, and account maintenance. The two companies plan to file a joint business model patent application for a securities brokerage business founded on this basic agreement. The alliance would give rise to the largest securities brokerage network in Japan and is expected to attract more investors by presenting them with a wider range of methods through which they can trade securities.

Telematics

FamilyMart, and to a lesser degree Three F and C&S, have joined Toyota's G-BOOK, a subscription information network designed to link people, cars and society anywhere, anytime. It is primarily aimed at providing interactive information services via vehicle-mounted wireless communication terminals. It can be accessed through PCs, PDAs (personal digital assistants) and cell phones. G-BOOK can also be used to link various G-BOOK compatible functions, such as using a cell phone to determine a vehicle's location or operating status.

By August 2004, FamilyMart and Three F had installed more than 5,600 and 650 E-Towers, respectively. These E-Towers are linked to G-BOOK. One of the major features of G-BOOK is an electronic account settlement function that accepts major credit cards and prepaid cards. This function enables online settlement of such transactions as payment for basic service fees, purchasing of fee-based services and other e-commerce transactions. By August 2003, Toyota already had 50 vehicle models that could link to the G-BOOK system and it has continued to expand its offerings.



Lawson's 'convenience banks'

In March 2003, Lawson and The Hokuriku Bank, Ltd (HBL) announced the development of bank branches offering convenience store facilities, thus reversing the previous business model. Trial stores opened in Tokyo and Toyama City in July 2003. This alliance will spawn 'Convenience Banks', providing always-available banking services. This new banking paradigm will utilize some existing HBL branches, remodeling them with convenience store services. The Lawson counters and Loppi multimedia terminals will bridge the gap left after regular banking hours. The alliance will also explore a joint Lawson/HBL card combining the functions of a bank cash card and LAWSON PASS (Lawson's own credit card). Lawson plans to develop similar joint stores with nationwide financial institutions, such as regional banks, credit associations and credit unions.

In summary, in the new more sophisticated mini-banks, CVS are thus challenged by how to effectively use various new technologies. In the case of emerging technologies like e-money and telematics, CVS are participating in technology-based consortia, where their role is relatively passive. Typically, these technology-based consortia are pioneers in introducing an emerging technology, but want CVS included in their consortia since through CVS they can reach Japanese society faster than via any other channel. With close to 40,000 stores across the country operating 24 × 7, the CVS have the largest continuously operating consumer-oriented physical retail networks in Japan. We therefore expect this technology-based trend to continue and for the mini-banks to be at the forefront in using emerging technologies to provide an expanding range of retail financial services.

At the same time, the CVS are pursuing their own technology-based initiatives by launching mini-bank ventures such as Lawson's e-brokerage and 'convenience bank'. These ventures can be considered natural extensions of their strategy to develop more sophisticated mini-banks. We predict this trend will continue as well. Table 3 summarizes the different levels of CVS mini-bank development.

Some Analytical Considerations

The structure of retail banking in Japan, as in other developed countries, has changed significantly over the past few decades. With deregulation of financial systems, non-financial firms have entered and begun offering retailing banking services using their specific strategic advantages to compete with traditional banks. The new firms may not have had decades of experience, but many have become competitive on a sustainable basis. This study of Japanese mini-banks, for example, indicates there are several positive and unique aspects to their



Table 3 Evolution of CVS mini-banks

| Features | Level of mini-bank sophistication | | |
|---|--|---|---|
| | Level I | Level II | Level III |
| Period | 1987–1996 | 1997–2001/2002 | 2001/2002 to now |
| Financial services (mini-bank services) | (a) Utility Bill Collection ● Power ● Gas ● Telephone ● Water (b) Money order sale | (a) Automated teller machine (ATM) (b) Foreign exchange transaction (c) Multimedia kiosks | (a) e-money (b) e-brokerage (c) telematics (d) ‘convenience bank’ (Lawson) |
| Japanese financial system | Controlled system | ‘Big bang’ reform (1997–2001) | Competitive open system |
| Information technology use | (a) Point of sale (b) Electronic ordering system (c) Telephone and lease line-based network. (d) ISDN lines — early 1990s | Satellite communications | (a) Short range wireless technology (Bluetooth) (b) Integrated circuit cards |
| Primary drivers | Utility companies to reach customers | Deregulated financial system | Innovation in wireless and communication technology |

Source: Authors’ compilation from various sources.

competitive business model that raise important strategy implications for retail banking generally.

Providing traditional retail banking services has become costlier in recent years. This is especially true of services outside large urban areas or among the less wealthy population. But the above analysis shows CVS-based mini-banks can offer many retail bank services more cheaply than their banking counterparts among more traditional banks. This is because the costs of the mini-bank services are incremental or marginal costs to the CVS, especially in terms of space and IT, whereas in the case of traditional banks it is not. Furthermore, increased store traffic can partially subsidize the cost of personnel, equipment and space used to offer these services.

Scope economies in the use of their IT systems are an example of this. This ability to offer cheaper retail banking services is important in Japan, since historically Japanese retail banks have operated at lower lending margins compared with counterparts in other developed countries. For example, between 1993 and 1997, the average lending margin was 1.11 per cent, approximately one-third of the 3.57 per cent in the US and half Germany’s 2.04 per cent (Kawamoto, 2000). In addition, Japanese banks, wounded by huge



non-performing loans and the collapse of the Bubble, have not had enough resources to serve demand fully. We therefore believe that in other developed countries non-financial firms that, like CVS, have ubiquitous presence may have the potential to replicate the Japanese CVS mini-bank model and reach customers at lower cost, thus challenging traditional retail banks. Wal-Mart, for example, has become a leading supplier of money orders and argues that it can expand into other financial services, since its surveys indicate approximately 20–25 per cent of their customers have no banking relationship.

Further, retail banks often target existing customers to cross-sell financial products and services, since acquiring new customers is both time-consuming and expensive. Citibank estimates that the cost of selling to a new customer is a significant multiple of the cost of selling an existing customer a new product (Rapp, 2002). So by targeting existing customers, they maximize business volume within a customer segment. However, market research suggests that successful cross-selling heavily depends on the contact employee's understanding of the customer's perception of the service experience (Beatty *et al*, 1996; Holmlund and Kock, 1996). This paper supports this finding, in that it shows that the mini-banks' success in cross-selling is largely due to their good understanding of their customers through detailed tracking of their purchase habits.

As discussed earlier, Japanese CVS traditionally have been very skilled at collecting and analyzing lots of information about their customers. This is done through a number of mechanisms, such as input from the sales clerks checking out products or services, from electronic sensors installed in each shop and from their 'point reward' credit/debit cards. CVS use this customer information to select the products and services they should carry or offer in a particular store, as well as to develop new products and services. With advances in data warehousing and data mining, CVS are now able to further differentiate and appeal to the different characteristics of their customers and to create and offer customized financial services in their mini-banks.

But they are not alone in this capability. Citigroup has successfully employed a customer life-cycle model in the US and is well towards adapting it in other countries, including Japan (Rapp, 2002). So the success of non-financial firms such as CVS in financial services depends on how successfully they can translate the knowledge of their customers to develop and provide financial services in combination with their basic business model that depends on increasing store traffic and product turnover.

The model also depends on the leading CVS continuing to be successful in forming the alliances needed to provide these services as well as develop new ones. For example, in recent years, they have entered into e-commerce through such alliances (Rapp and Islam, 2003). Such affiliations are particularly important when introducing a new financial service, because through such



alliances each individual participant can bring their resources into the value chain while minimizing investment cost and risk. CVS with their wide experience in managing such alliances are in an advantageous position compared to traditional retail banks used to offering their own proprietary products. Because a key mini-bank goal is to increase customer traffic and retail volume, they do not always have to offer their own products. Indeed, this study indicates that the collaborative approach may be critical for the development of mini-banks in other parts of the world. That is, non-financial firms with considerable experience in forming strategic alliances should have a higher potential for implementing successful mini-bank ventures elsewhere. 7-Eleven, for example, has done this in their pilot project in the US.

At the same time, one needs to recognize that the relative competitive weakness among Japanese retail banks facilitated the mini-banks' emergence. Compared to their US banking counterparts, Japanese banks were first diverted from retail banking between 1950 and the mid-1970s due to government pressures to increase consumer savings and support industry investment. This was followed by the Bubble and finally financial weakness consequent to its collapse. This extended period of weak retail banking created a strategic opportunity, since the normal competitor occupying this market segment was not strong.

At any strategic inflection point, the firm that recognizes the opportunity and has the strategy in place to exploit it will have an advantage. 7-Eleven Japan and other Japanese CVS fulfill this criteria, given that they recognized Japanese banks' weakness and had the ability to move from just processing payments into retail banking services by leveraging their 24 × 7 customer expertise and investment in IT. Therefore, to the extent that retail banks are stronger and more competitive in other developed countries, in such countries non-financial firms will need to carefully consider the competitive context in order to determine the extent to which they can strategically develop mini-banks as easily as the Japanese CVS.

However, to the extent that they share the Japanese CVS advantage of being able to justify banking through capturing network externalities due to improved store traffic, while reducing their risks by emphasizing transactions rather than credit as a revenue source, they should still actively consider this business model. This is because these factors will still give them an advantage over traditional retail banks that should help them sustain their strategy of extending their retailing activities to financial services and pushing more product through their existing customer base. This will be similarly true for the Japanese CVS even if the Japanese banks recover their footing, as they finally seem to be doing. Furthermore, both retail banks and non-financial firms appear to be testing the model in the US. There is the Wal-Mart example noted above and 7-Eleven is testing the extension of such services in Florida.



Moreover, in the New York area Chase has teamed with A&P to offer Chase banking services in several A&P markets, all having extended hours of operation.

Conclusions

From modest beginnings with utility bill payment collection, CVS have developed their mini-banks tremendously over the past two decades in terms of the number and types of services provided. Now a typical mini-bank offers many if not most of the services provided by their traditional retail banking counterparts. Indeed, in cases such as employing new technologies, mini-banks seem ahead of traditional Japanese retail banks. Their differing financial services business model is based on the simple strategic principle of coupling external opportunities with internal strengths (ie core competencies such as IT). However, as such simple strategic principles are often difficult to apply in a real competitive environment for an extended period, it is important to continue to study and monitor these CVS mini-banks and their evolutionary development. Such studies might focus on how they are organized and how they form and maintain key alliances. These will be critical issues in assessing their impact on Japanese financial services' future evolution as well as how they may be replicated or modified in other countries to bring 24×7 convenience, efficiency, and customer orientation to the widest possible audience.

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