The Japanese Beer Industry: Driven by Innovation

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Abstract

The Japanese beer market is an oligopoly dominated by two major players, Asahi and Kirin, who account for 75 per cent of the domestic market. Despite their market dominance, a range of demographic and other factors such as stagnant domestic demand, rising health consciousness and a declining population undermine their prospects for sustained growth. In this climate, the major brewers have introduced a wave of innovative products in recent times. While the major global brewers have focused on their core competencies, Japan's brewers have instead opted for diversification. This paper offers an overview of the Japanese beer market, with a focus on the innovative products developed, the main features of market competition among the Big Four brewers, and a summary of their strategic directions.

Introduction to the Japanese Beer Market

Japan's beer market, like many other Japanese markets, is an oligopoly. Two major brewers – Asahi and Kirin who vie for market dominance – and Suntory and Sapporo, dominate the industry; together they account for around 97 per cent of the market. (Automobiles, convenience stores, cosmetics and consumer electronics are examples of other markets with power concentrated among a few players.) Imported beer accounts for less than one per cent of the market with boutique brewers representing a similar amount (Parsons 2007, p.5). Reflecting Japan's beverage industry's powerful distribution system, major international brewers produce and/or distribute their beer through agreements with the Big Four: Kirin produces Budweiser under license in Japan and has exclusive importing rights for Heineken and Pilsner Urquell; Sapporo imports Guiness, Asahi imports Miller 'Special', Bass Pale Ale and Tsingtao and brews Lowenbrau under license.

Kirin was the overwhelming and unchallenged market leader until 1980s. (In 1979, for example, its market share was still 60 per cent (Aaker, 2011, p.25).) However the launch in 1987 of Asahi's 'Super Dry' beer triggered an assault on Kirin's dominance, and although it took Asahi another several years to surpass Kirin, today Asahi and Kirin battle for market share dominance with shares hovering around 37 per cent each (Parsons, 2007, p.33; Datamonitor, 2011b, p.3). Unlike their global competitors, Japanese beer manufacturers have a diversified product portfolio. All produce non-alcoholic juices, canned coffee, and sports drinks: ranging from 60 per cent of all sales of Suntory to nine per cent of Sapporo's. Asahi and Kirin both produce pharmaceuticals, accounting for four per cent and 10 per cent of sales in 2010, respectively (sourced from 2010 annual reports and corporate information of the Big Four).

Market maturity, the world's fastest ageing population and tighter consumer spending have seen Japan's beer market stagnate, and then decline in recent years. This trend has been forcing the country's Big Four brewers to look elsewhere for growth. By 2012, the total scale of Japan's beer-type beverages market is likely to contract by around 3 to 4 per cent compared to 2009 (Datamonitor, 2010, p.6).

Market Dynamics

Like many product categories in Japan, competition in the Japanese beer market is driven by product innovation, or what Czinkota and Kotabe (1990) refer to as 'incrementalism'. Aaker (2009) has portrayed the market over the last three decades as "hypercompetitive", with roughly four to 10 new product introductions each year, underpinned by aggressive advertising, packaging innovations, and sales promotions. (Price competition is almost non-existent, with prices for standard beers identical across the major brands.)

Over the past twenty years, three new subcategories have been developed and one repositioned. The first innovation to shake up the sector was 'dry' beer, first marketed as a distinct new segment by Asahi Breweries. Kirin was traditionally associated with a rich, somewhat bitter taste of its flagship pasteurized beer. The introduction of Asahi's *Super Dry* in 1987 offered a beer with a sharper, more refreshing taste, and less aftertaste. The new product, which contained more alcohol and less sugar than lager, and a special yeast, appealed to a new, younger generation of beer drinkers willing to experiment with new tastes. Dry beer quickly became a market phenomenon in Japan. In less than a decade, as the other brewers scrambled to enter the market, dry beer captured almost a third of Japanese beer sales. (As Aaker (2009, p.4) notes, light beer took 18 years to gain 25 per cent of the U.S. market.) Sustained first-mover advantage in the subcategory and aggressive brand protection allowed Asahi to own 'dry beer' as their product. By 1998 Asahi was the sole brewer in the dry-beer category.

In 1990, Kirin responded to the dry beer phenomenon with an innovation of its own: Kirin *Ichiban* ('number one'). It used a new, expensive brewing process that used more malt, filtering at low temperature, and, most critically, used only liquid from the first pressing of the malt. The resulting taste was milder and smoother than Kirin Lager. The prohibitive cost of the process, Kirin's strong brand equity, and its distribution power presented major obstacles to competitors. *Ichiban* halted the decline of Kirin's overall market share during the first half of the nineties, before Asahi eroded its market share by, in 1996, repositioning dry beer as the draft leader.

In 1998, under increasing pressure from Asahi, Kirin halted its market-share erosion thanks to a third innovation in the industry in a decade. 'Happoshu' (low malt) beer was a subcategory introduced by Suntory in 1994 but with only marginal success and little fanfare at the time. It contains significantly less malt than other Japanese beers, and thereby qualifies for a significantly lower tax rate. The subcategory grew dramatically in 1998 when other brewers entered the market, most notably Kirin with its *Tanre*i brand. Tanrei helped Kirin maintain its market leader status spot as Japan's top brewer from 1998 to 2000 as overall sales of happoshu increased to about a fifth of the overall beer market by early 2001. Asahi entered the segment in 2001, but Kirin remained leader in the segment.

The arrival and subsequent popularity of happoshu was a reflection of Japan's tax regime for alcoholic beverages. Traditionally, beer having a high malt composition, is taxed at a higher rate in Japan, and thus sold at high prices. For instance, if the malt content was 67 per cent and above, then the company needed to pay a higher tax than if the malt content was 25 to 50 per cent, or less than 25 per cent. While regular beer costs about $1.75 for a 350-milliliter can – of which 66 cents is tax – happoshu with less malt than traditional beers - sold for about $1.25, including 40 cents of tax. Japanese authorities responded, albeit slowly, by raising the tax rate on low-malt beers. The result has been that 2011 has witnessed Japanese brewers scaling back production of happoshu. Suntory and Sapporo breweries are set to halt the production of low-malt beers in 2011, while Asahi has announced plans to reduce its production by 20 per cent (Business Monitor International, 2011b, pp.52-53). The fourth innovation in recent times is so-called ‘third beer’ (also known as *shin janru* or ‘new genre’). In order to counter tax changes that reclassified the malt content of beer and subsequently raised the price of happoshu, this beer-like beverage contains no malt, instead using pea, soya, or wheat spirits. Third beer costs just $1.10 per can (including roughly 24 cents of tax). Price is not the only factor behind its growth, however. It also taps into the rising health trend, emphasizing a good taste profile to break the stereotype that healthy options are a compromise on flavour.

Growth and Diversification Initiatives for Japanese Brewers

According to the Kirin Institute of Food and Lifestyle (2010), domestic consumption of beer and beer-like drinks in 2009 was 5.98 million kilolitres, down 16 per cent from 10 years earlier. Meanwhile, global beer consumption in the same year was 177.27 million kilolitres, up by 34 per cent over the previous decade (ibid, p.22). Domestic market conditions could hardly be worse for Japan’s Big Four: the domestic beer market is saturated, recessionary pressures are making consumers wary, health consciousness is on the rise, consumer tastes are diversifying, and the population has been declining since 2005.

Against this background, Japanese beer makers are seeking growth opportunities offshore. Like all global brewers, Japanese companies hoped to expand into China but have been unable to take leading positions there as a result of the price battles. Industry giants like Belgium's Anheuser-Busch InBev, Britain's SAB Miller, Netherlands' Heineken and Denmark's Carlsberg dominate the international beer market. Anheuser-Busch held a 20 per cent share of the global market in 2009, compared to just over 2 per cent each for Kirin and Asahi. In April 2009, the latter acquired a stake in Tsingtao Brewery, one of China’s major brands with a strong overseas presence.

Slumping beer consumption has forced the major brewers into ‘unholy’ alliances. Asahi and Kirin are both seeking to improve efficiencies in response to the shipment bottlenecks following Japan’s devastating March 11 earthquake and tsunami. They each have nine domestic breweries, many in close proximity, and have commenced using the same trucking company in joint deliveries that began in Tokyo and three surrounding prefectures in September 2011 (Business Monitor International (2011b), p.9). The two brewers will also use each other's distribution points between factories and wholesalers. The effort is expected to reduce the number of delivery trucks the pair uses in the region by 10-20 per cent and shorten driving distances; the improved efficiency is expected to result in 30 per cent lower carbon dioxide emissions. They are both looking to expand abroad and need to cut costs at home to free up cash for investments. With the rise in ingredient prices, Japan’s major brewers are considering cooperation in procuring supplies as well. (Even before the disaster, Kirin cooperated on deliveries with Sapporo Breweries and Suntory.)

While international beer brewers such as Anheuser-Busch and Heineken have focused on their core business, the Japanese brewers have opted for diversification as their growth strategy. (See Table 1.) Kirin is aiming to enter a fourth product category of health food, which will follow its longstanding presence in alcoholic beverages, soft drinks and pharmaceutical goods (Business Monitor International, 2011, p.7). The large degree of channel power possessed by the major brewers allows them to enter new markets in the food and drink categories.

Table 1: **Sales of Big Four Brewers 2010**

	Kirin	**Asahi**	**Suntory**	**Sapporo**
Alcohol beverages	50%	65%	33%	78%
Soft drinks & foods	29%	28%	60%	9%*
Other business	21%**	7%****	7%	13%***
Beer Market Share	36.4%	37.1%	13.4%	12.3%

Source: Annual reports 2011 **Notes**: * Soft drinks only; ** includes 10% sales in pharmaceuticals; *** includes a 50/50 split in sales between restaurants & real estate; **** includes 4% sales in pharmaceuticals

Strategic Direction

Japan's largest brewers have adopted different growth strategies in recent times. Asahi has a three-pronged strategy for further development. The company is seeking to extend its brand portfolio via launches in the premium sector, in addition to improving its manufacturing facilities, in order to encourage growth domestically and strengthen its business in Japan. It had also changed its pricing strategy, now listing its premium beers at mass-market prices. However, on a wider scale, Asahi is looking to solidify its Japanese operations and use them as a base for expansion throughout Asia, specifically into China. It is also looking to improve its non-beverage product mix to secure against the stagnation of the Japanese alcoholic drinks sector. For the past several years, Asahi has invested 250 billion yen (A$3bn) in acquisitions such as a stake in Tsingtao Brewery Co. of China, Schweppes Australia and Ting Hsin (Cayman Islands) Holding Corp. of China. In July 2011 Asahi announced it bought a controlling stake in Australia's third-largest soft drink maker P&N Beverages Australia for A$188mn (although, at the time of writing, the Australian Competition and Consumer Commission opposed Asahi's bid). On the same day, the company announced it had launched an agreed NZ$129mn ($100mn) bid for New Zealand's Charlie's Group, a juice maker. Despite these overseas investments, however, Asahi remains heavily dependent on *Super Dry* for revenue and profit. Because it has kept its strategic focus on its core beer business, the company has fallen behind domestic rivals in developing profit sources outside of beer.

Kirin, for its part, has committed to new product development as the main driver of growth. Acquisitions in new categories are also sought, with the company seeking a stronger presence in more dynamic sub-sectors. Kirin now owns Australian beer market leader Lion Nathan, and holds a 48.3 per cent stake in San Miguel Brewery, and is now looking to possibly take full control. Furthermore, in June 2007, Kirin paid US$2.6bn for Japanese pharmaceutical maker Kyowa Hakko Kogya. In September 2010 the brewer entered an agreement to acquire all its outstanding share in its wine subsidiary Mercian Corporation, giving full ownership and a stronger presence in the wine sector. Although the strengthening of its domestic alcohol business will remain important, Kirin is looking to the soft drink industry and its international alcohol division as the primary future growth drivers, as evidenced by recent expansions in Australia and Russia. Securing Lion Nathan has put Kirin well on course to fulfil its Vision 2015 well ahead of schedule and further consolidates the company's position as a growing force in the Asia Pacific beer market. It is now hoping to generate 30 per cent of its revenue internationally within the next five to 10 years – a big achievement for a previously Japancentric brewer. In July 2010, Kirin acquired a 14.7 per cent stake in Singapore's largest beverage company Fraser & Neave (F&N) as part of its long-term commitment to international markets. This acquisition will provide Kirin with an important foothold in Southeast Asia to revitalize its growth.

Japanese brewer Sapporo is adopting a twin-pronged strategy of geographical and sectoral diversification as the domestic market continues to stutter along. The Japanese brewer is setting aside an investment war chest of JPY125bn (A$1.5bn) for acquisitions and partnerships between 2012 and 2016. Amid domestic demand weakness, Sapporo has embarked on a hunt for overseas mergers and acquisitions (M&A) opportunities as it looks to develop higher-growth assets to revitalise its long-term growth. Vietnam, for instance, marks Sapporo's first major overseas expansion within the last three years as it plans to acquire a 65 per cent stake in a beer joint venture with Vietnam National Tobacco. More interestingly, expansions in North America will be figuring prominently in Sapporo's growth plans as well. The brewer is seeking to acquire a premium beer brand in the US and is contemplating further expansions in its brewing capacity in the country. As a developed market, North America may not be the best place to look for strong growth prospects, but there is certainly scope for a decent level of earnings. Besides geographical diversification, Sapporo is also pursuing expansions in the relatively higher-growth sub-sectors such as soft drinks.

Concluding Remarks

This brief overview of the Japanese beer industry provides three insights into the nature of Japanese industry in general. First is the critical role of product innovation as a competitive strategy, an approach typical of many Japanese market sectors. Such innovation partly succeeds because Japanese consumers are adventurous in their desire to experience new products; brand loyalty mattered for little when Asahi launched *Super Dry* and Kirin ‘loyalists’ deserted the market leader for the innovative upstart. Craig (1995) argues it was the shift by Asahi in the early 1980s from the traditional production orientation to market orientation that produced its phenomenal *Super Dry* in 1987 and triggered a burst in new product development. While, from 1964 to 1984, brewers put an average of 0.76 new beers on the market each year, the new product introduction rate from 1985 through 1993 jumped ten times, to 7.6 per year (Craig, 1995, p.9). In contrast to loyalty associated with domestic automobile or consumer electronic brands, Japanese do not exhibit strong loyalty toward products in the food & beverage segment not regarded as quintessentially Japanese. The second characteristic is the diversified nature of their product portfolio, with strong contributions not only from non-alcoholic beverages by all four major players, but also pharmaceuticals in the case of the Big Two. Strong channel power facilitates this diversification by allowing brewers to leverage existing relationships with wholesalers, convenience stores and through the ubiquitous vending machine that offers everything from rice, batteries, and beer to soft porn and hot coffee. The third characteristic is the focus on the Oceania region and developing markets in Asia such as Vietnam to grow sales, rather than commit to substantial investments in China where it would compete with the major global players. Two factors are at play here: first, most Japanese companies are conservative, risk adverse, averse to price competition, opting instead for innovation or repositioning and, second, Japanese food & beverage manufacturers are uncompetitive in the global marketplace. Beyond autos and electronics, product categories that allow Japanese industry to maximise their competitive advantage in automated assembly line production systems, Japan has been unable to compete on the international market.

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