S. HRG. 99-1018

CRACKING THE JAPANESE MARKET

HEARING

BEFORE THE

SUBCOMMITTEE ON TRADE, PRODUCTIVITY, AND ECONOMIC GROWTH

OF THE

JOINT ECONOMIC COMMITTEE
CONGRESS OF THE UNITED STATES

NINETY-NINTH CONGRESS

SECOND SESSION

FEBRUARY 10, 1986

Printed for the use of the Joint Economic Committee

U.S. GOVERNMENT PRINTING OFFICE

62-118 O WASHINGTON : 1987

For sale by the Superintendent of Documents, Congressional Sales Office
U.S. Government Printing Office, Washington, DC 20402

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[Created pursuant to sec. 5(a) of Public Law 304, 79th Congress]

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CRACKING THE JAPANESE MARKET

MONDAY, FEBRUARY 10, 1986

CONGRESS OF THE UNITED STATES,
SUBCOMMITTEE ON TRADE, PRODUCTIVITY, AND ECONOMIC
GROWTH OF THE JOINT ECONOMIC COMMITTEE,
Washington, DC.

The subcommittee met, pursuant to notice, at 2 p.m., in room 2007, Federal Building, San Francisco, CA, Hon. Bobbi Fiedler (member of the committee) presiding.

Present: Representative Fiedler.

Also present: John Starrels, professional staff member.

OPENING STATEMENT OF REPRESENTATIVE FIEDLER, PRESIDING

Representative FIEDLER. The subcommittee will come to order.

We are here this afternoon to seriously explore the possibilities available to United States firms for "Cracking the Japanese Market."

In 1985, the United States ran a merchandise trade deficit of nearly $50 billion with Japan. So, it is very much in America's interest to take advantage of available marketing opportunities, as a growing number of United States firms are now doing to reap well-deserved profits in Japan's dynamic marketplace.

As of late, there has been a volume of rhetoric from the United States bewailing the alleged absence of private sector marketing opportunities in Japan. Clearly, Prime Minister Nakasone is aware of our concerns. And, over the last several years, he has been undertaking strenuous efforts to ensure that American businessmen are afforded the same kinds of entrepreneurial opportunities that Japanese entrepreneurs are afforded in the United States. I have spoken with Prime Minister Nakasone about California's specific aspirations in this regard—as reflected in the superb list of companies and associations who will be testifying before this committee in a few moments.

I am convinced that American firms today have a major opportunity to go into the Japanese marketplace and successfully compete for business.

The challenge for American business is contained in one fundamental message: Success in Japan can be achieved, but only by those American firms who demonstrate a passion for learning those essential cultural, marketing, and—yes—diplomatic skills, which can help ensure a secure place for the "Made in America" label in Japan's economic future.

This Nation confronts a major opportunity in its commercial relationship with Japan. In order to take advantage of that opportunity, we need to understand this relationship in all of its complexity.

Let's begin with trade. It's true that the largest portion of America's recent merchandise deficits have been generated with Japan. It is also true, however, that more than 20 percent of American exports presently go to Japan, making it our second largest trade partner after Canada.

Since 1982, moreover, Japan has provided the goods for America's economic boom just as the United States has, in turn, supplied the appropriate market for Japanese growth.

Put simply, "Japan and the United States are increasingly becoming part of the same economy, an economy equal to a third of the world outputs," says the London Economist.

It is the growing interdependence between the free world's two largest market economies that must be kept uppermost in our minds as we go about the necessary task of cracking the Japanese marketplace.

We need hands-on information that can be used by American firms to help establish themselves in the very competitive Japanese marketplace. For this purpose, I take great pleasure in welcoming our distinguished witnesses from the manufacturing and agricultural sectors who will enlighten us on their experiences in Japan's dynamic marketplace.

May I extend a special thanks to Russell Geiger, president of Delta Electronics of Alexandria, VA, who has traveled all the way to California to share his experiences and insights with us.

We will begin with our manufacturing panel to be followed by our agricultural specialists.

Mr. Okumura, the floor is yours.

STATEMENT OF EARLE T. OKUMURA, DIRECTOR, PACIFIC RIM MARKETING SERVICES, KMG MAIN HURDMAN

Mr. OKUMURA. Congresswoman Fiedler and members of the committee, I am Earle T. Okumura, director of Pacific Rim Marketing Services for KMG Main Hurdman, an international accounting and consulting firm based in their Los Angeles, CA, office.

I am pleased to be able to share my experience with you today relating to exporting to and marketing in Japan. I have over 25 years' experience in marketing and management activities related to Japan.

For over 10 years I managed Max Factor and Max Factor's pharmaceutical subsidiary in Japan, Korea, and Southeast Asia. I have also served as staff vice president of Kimberly-Clark Corp., where I was responsible for analyzing their Japan operations and developing new marketing strategies.

Prior to joining KMG Main Hurdman in 1985, I had my own consulting practice for 10 years assisting United States corporations to enter the Japanese market and control their marketing activities.

I was born in the United States, right here in San Francisco, and raised biculturally and bilingually both in this country and in Japan. I have a bachelor's degree in economics from Waseda University in Tokyo, and a degree from the Graduate School of International Management in Phoenix.

On the issue of marketing to Japan, the following are some of the common complaints voiced by United States companies in dealing with the Japanese. In the last 10 years, I often hear these complaints and I have picked a few here.

"Cannot sell our product or service to the Japanese."

"It takes forever to obtain Government approval."

"Can't find the reason or pinpoint the real problem behind our declining sales in Japan."

"Our distributor is having problems launching the product but we just can't understand why."

The reasons behind these complaints can be found and understood within the historical context of, say, the last 40 years. If I may briefly cover that, I think it will bring to light the real reasons behind these complaints.

After World War II, as we all know, the United States was the only nation capable of supplying the world with sophisticated industrial products and quality consumer goods.

For decades following the end of World War II, U.S. corporations focused their marketing efforts in Europe. Culturally, the European markets were easier for us to identify with and the formation of the European Economic Community encouraged many U.S. firms to direct their resources to the Atlantic trade.

With the exception of Japan, most nations in the Pacific Rim basin did not have the purchasing power until recent years. Except for a handful of multinational firms, such as my former employer Max Factor, it was not economically feasible to launch a major marketing campaign in each of these markets.

Most United States firms who did establish a foothold in these Pacific Rim basin markets, including Japan, did so through the major Japanese trading firms, or other specialized trading companies or importers.

In the sixties, other major United States firms formed joint ventures with Japanese firms to market their products in Japan. And basically, because this was the only way to establish an asset base in Japan.

During this postwar era in Japan, the Japanese partner or distributor gained a competitive edge over their local Japanese competitors by marketing unique American products. It gave them a competitive edge. Meanwhile, United States exporters were content with the extra sales generated in Japan using little or no efforts of their own while they were focusing their attention on their Atlantic trade and the European market.

During the fifties and sixties, Japan exerted an all-out effort to catch up with American quality control standards and marketing techniques. The gurus of modern American management, such as Peter Drucker, were imported to teach the ways of American business and product management. Having studied in Japan between 1958 and 1962 going to Waseda, I know: I had to read all these in English.

Japanese businessmen flocked to visit their United States counterparts. Americans at the time were happy to show off United States ingenuity in manufacturing facilities, resulting in numerous licensing agreements and the beginning of a technology transfer to Japan.

Today, the global business climate that dominated the fifties and sixties has drastically changed. Japan has developed and globally marketed many quality products that compete with United States products.

At the same time, the Japanese market has undergone many changes, especially in the areas of consumer traits and buying trends. While Japanese firms have kept up with these changes, United States firms exporting to Japan in general have not.

Many United States firms have remained totally dependent upon their Japanese importer or distributor to market their products. As a result, these United States firms have lost control over their marketing activities in Japan.

I find many United States firms today trying to enter the Japanese market following the obsolete rules of the fifties and sixties. Americans are caught unprepared to compete directly with the Japanese in Japan.

Because Japanese products are now as good or better than American products, the incentive for the Japanese trading firms or importers to promote United States products as they did in the past has been reduced.

United States firms who were passively dependent upon them for sales, now find themselves insulated from their end users, and without independent resources and a network in Japan to carry out their marketing strategies.

I recall someone telling me that they had five blind men trying to describe an elephant. I would like to share an observation, looking at what I just said from a different angle, if I may.

When we look at markets around the globe, then we see a certain pattern of how we market our products. In developing markets such as Latin America and the Middle East or Indochina, identifying the individual or family or company influential within that industry is key to successful marketing in those markets.

This is because those markets have not matured yet, meaning they are not fragmented, lacking large sophisticated middle-class consumers. And in this type of market, there is very little a U.S. or foreign seller can do to expand sales other than to follow your local contact's advice.

There is nothing you can do in attempting to identify the end user and promoting your product directly to the end user and assisting your appointed distributors from that angle.

However, as markets mature, this mode of market entry no longer becomes effective. In the case of Japan, the major Japanese trading companies and other specialized trading firms assumed this role, taking the initiative to import and market American products.

Now while this served everyone's needs in the fifties and sixties, it has long ceased to be the optimum way of gaining a profitable foothold in a fully matured, affluent 120 million people market.

Japanese firms recognized this market evolution as early as in the late sixties. And most American companies continued to approach Japan the way they had been approaching other premature markets.

I have a book here I brought with me, in Japanese, that was written in 1982. It is entitled "How To Develop New Strategies To Cope Within a Matured Market." The audience, of course, are your major Japanese corporations.

Representative FIEDLER. Is that directed at American companies, or Japanese companies?

Mr. OKUMURA. No; this is addressed to your major Japanese consumer product companies.

Representative FIEDLER. To sell in Japan or to sell here?

Mr. OKUMURA. To sell in Japan.

Representative FIEDLER. All right.

Mr. OKUMURA. I think it reinforces what I discuss here, that the market has matured, and that the United States in any foreign country, short of developing strategies as discussed in this book, doesn't have much of a chance to compete with their counterparts in Japan.

The United States, a country whose marketing is undoubtedly the best in the world, did not apply its own marketing techniques and principles in Japan. And by using trading companies instead of developing their own market research and networking, United States companies insulated themselves from their consumers in Japan.

The United States did nothing as a whole to learn how to work within the Japanese infrastructure or cultural setting. It has not yet made the same cultural commitment to Japan as it has done in Europe or Latin America.

The Japanese, on the other hand, approached the United States market on a cultural level in the late fifties. They were willing pupils for anything American, especially business techniques, eventually incorporating these same techniques to penetrate the U.S. marketplace.

Conversely, the United States must now overcome years of insulation and cultural naivete to reach the level of understanding of Japanese society and markets that the Japanese have of this country. The knowledge gap that exists is a human resource problem that the United States cannot quickly surmount.

I have picked some statistics here to illustrate some of the gap. For instances, while Japanese is not even taught in high school here, English is mandatory from the seventh grade to college level in Japan.

In 1978, we only had 58 registered professional translators. They had over 1,567, which translates to the substantial lack of data source available to U.S. corporations to form a practical market strategy.

While 300,000 tourists went to Japan, over 1 million tourists visited the United States in 1980. And it goes on and on.

If an American corporation wants to train their executives to learn Japanese, I think we are limited to institutions here. Whereas in Japan, their local television, regular programs, teach not only classroom English but how to use that English in the streets.

I would like to discuss next some of the principles for being successful in Japan. To be successful in a major market such as Japan, the same effort and strategies that gained a successful track record in the United States home market must be applied to Japan.

I don't think any California company would expect to sell to a 20 million person New York State market without employing all of their marketing resources and strategy. Anything short of that, I don't think they can expect more in a market six times the size of New York.

The three basic principles to successful marketing in Japan are:

One must have a successful marketing track record in the United States. And I will elaborate on these principles using some case studies.

The second principle is, one must have an extensive network in Japan to assist.

And, third, cross-cultural communication skills to make the Japanese comfortable in dealing with you. Later on I would like to elaborate on what I mean by the word "comfortable."

The following is a definition of what I mean by these three principles. U.S. marketing track record. A successful marketing track record is very important.

A company whose product has a successful track record in the United States has applied the correct marketing techniques to penetrate its marketplace. I will be using the example of one of my clients, Precision Dynamics, who have their headquarters in the San Fernando Valley.

Seven years ago, Precision Dynamics Corp. already had a major share of the U.S. identification band market. These are a plastic band that hospitals use when you enter a hospital—for outpatients as well as inpatients.

They accomplished this by utilizing the same fundamental marketing techniques previously described here. They then identified a new market in the crowd control business, selling identification bands to theme parks, the Kentucky Derby, Indianapolis 500, and so on.

My first task was to understand what contributed to their successful track record in the United States. We then began utilizing those same basic steps in Japan.

My first step in this direction was to replace their Japanese trading company that they had with a distributor specializing in selling disposable medical products directly to hospitals.

I personally made sure that my client invited the owner, Mr. Imamura, to California—it was his very first trip to California—showing him that we had the resources, and more importantly, the imagination and willingness to accomplish the task.

We charted a 5-year program, as I recall, similar to our program in the United States, beginning with the mother-infant identification band in the OB–GYN ward, and gradually penetrating the other wards.

Our next target in Japan was the ambulance business. Today, every public ambulance in Tokyo carries a Precision identification band with blood types of patients on it. This was a strategic step toward the general crowd control market, and resulted in Precision receiving the order last year for 1.5 million bands.

During this time, Precision had complete control of their marketing activities in Japan, guiding their distributor in every step of the way. Today, he continues to expand the identification band market in Japan.

The second principle is having an extensive network in Japan. Here I would like to use the example of Denver Chemical Manufacturing Co., a $16 million pharmaceutical firm on the east coast. One of their specialty lines is a pregnancy test and they had a 60-percent share of the U.S. market then.

I would like to further point out that while we attained a 7-percent share of the Japanese pregnancy test market in 1 year, after gaining Government approval against a formidable Japanese competitor who had a 70-percent share of the pregnancy test market, the foreign exchange rate then was 360 yens to $1.

So, it clearly illustrates that it is not so much the exchange rate. Furthermore, I can now say that our pregnancy test was inferior to the Japanese competition. I was not a consultant then. I was an employee of Max Factor's. I had no choice but to do with what was given me.

What we did was we identified all of the network that made Denver Chemical successful in the U.S. market. The networks are major Japanese pharmaceutical firms. We personally went out and interviewed all of your major prominent Japanese firms to screen a company that would meet our criteria.

We then went to the banks, the Japanese banks, to check their profile and introduce us to the company that I identified as a prospective distributor for us.

We visited the Japanese Ministry of Welfare to find out—directly find out what the requirements were to obtain approval for these products. As a result, we learned that they still required toxicity tests for pregnancy tests which you do not take in orally.

I was fortunate in successfully removing that requirement which would have taken us an additional 6 months to get this product approved.

We then identified a certain Dr. Takeuchi, as I recall, who is in OB–GYN. He was appointed by the Japanese Ministry of Welfare to conduct a study on a disease called choreocarcinoma which one of our products was able to diagnose accurately.

With his help and our network with prominent physicians, we were able to establish our product which was called UCG Titration Test as the only test authorized and blessed by the Japanese Ministry of Welfare.

We also utilized our own network into the major university hospitals to run clinical trials which we were able to use as strategic marketing tools later on.

So by establishing our own network of contacts, we did the legwork for our distributor, thereby making our distributor far more effective. Had we relied on the distributor to do this, it would not have happened.

The third principle is cross-cultural communications skills. The ability to make the Japanese comfortable with your firm is a communication skill that a company should be well versed in from its dealings in the United States. That comfort factor is the basis from which all good business deals are made.

It is no different from doing business in this country. Your firm must have representatives who can show the Japanese that your firm is both flexible and stable, and willing to sit down and negotiate with mutual respect and understanding. Your company must be able to demonstrate the ability to separate myth from reality.

This skill complements and interacts directly with the previous two principles of successful U.S. marketing track record and networking. Although each is not wholly dependent on each other for success, they cannot be exclusive from one another and still guarantee success.

International Marketing Affiliates, Inc.'s president was Mr. Russ Simmons. I have a letter from him to me which I believe will best illustrate how cross-cultural communication skills is an important principle for successful marketing in Japan. May I just quote part of that letter:

As president of an automotive accessory manufacturing company, I was successful in marketing our products in the United States, Western Europe, South America, and Australia. In numerous attempts to enter the Japanese market, my only success was building large expenses and my own frustration.

The "proven formula" just would not work. I faced polite Japanese businessmen who were generous with their time, desired volumes of information, but never allowed anything close to a closing situation to come about.

Further, a nontariff trade barrier made it virtually impossible for one of my products to be installed in a car and pass Japanese vehicle inspection.

The nontariff trade barrier is a requirement that every model be structurally tested after a sunroof is installed, costing the distributor approximately $700 per model.

We used our cross-cultural communication skills and our local network to its fullest advantage to successfully eliminate the need to retest the vehicle after installing a sunroof.

How did we do that? First, we identified every key player in the Government as well as in the private sector. Then we learned about the relations between the key players. We were sensitive to the fact that retirees from the Department of Transportation man those inspection stations. Fully prepared with a TUV report—a structural testing report from Germany—which is much more rigorous and strict than the Japanese requirements and the U.N. tests that my client had, we negotiated with these key players in a strategic order. Like a chess game, we moved in certain strategic order. At the end of 2 weeks, our distributor whom we screened out of many, was able to take advantage of our effort.

In the end we appointed a distributor whom we—Russ Simmons, my Irish client and myself—introduced to their own government office for administrative guidance. I also used his name when I returned—I was a speaker on one of the Department of Commerce activities—to demonstrate that in certain areas the Japanese Government is indeed trying to help.

I believe it was that time in May 1982 when—I believe it was a subcommittee, and please correct me if I am wrong, of Congress had a special session on exporting to Japan. It was televised. That helped, immensely.

In concluding, I would like to say that the barriers facing United States companies wishing to export to Japan are primarily a result of historical factors, as we discussed earlier, and the broad cultural differences that exist between East and West.

To successfully market in Japan, American companies must follow the three principles we have discussed. They must have a successful track record in the United States. You have to have an extensive network in Japan independent of your customer or distributor. Certainly cross-cultural communication skills are not going to hurt. And the purpose is to make your buyer comfortable.

I would like to add, the attitude is different between buyer and seller in Japan. The Japanese have a great advantage over us when they attempt to sell products to us, because the seller serves the buyer. You are asking the buyer to part with hard-earned money and you would do anything and everything to please the customer.

If you go to a Japanese department store, you feel guilty walking out of that department store without spending anything. I think it is the reverse in our country. Japanese from Japan have often told me that the first culture shock that they go through in the United States is when they go to a department store or any of our shops to buy something. They are treated equal. In Japan, buyer and seller are not equal.

However, I do appreciate the fact that many United States firms, other than the major multinationals, may not have the human resources to extend their successful track record to the Japanese market. Governmental agencies to date have not effectively remedied this situation.

To accomplish what needs to be done more quickly, U.S. firms have two basic options. First, to employ qualified bicultural individuals and, second, to engage outside consultants qualified to do the job.

However, any individual American companies that engage, should meet the following criteria. I have seen many situations where they have come short of the following criteria:

First, they should have an extensive network in Japan in industries, banking, and government. Second, they must have an extensive line—and I emphasize the word "line" instead of "staff"—management and marketing experience in both Japan and the United States. It helps—it not only helps, I believe it is a must to have those doors slammed on your face and then have the sense of humor to go back in again both in the Japanese business environment and the United States.

Last but not least, one must have the capabilities in the United States to prepare a preliminary strategic marketing plan that is practical to implement in Japan. Meaning, a full data-source base here in home market.

The Japanese business system is based on long-term commitment between buyer and seller. Japan is now reaping the profits of their commitment to the United States market. The opportunity for American companies in Japan has never been better.

But success will still hinge on how well a company structures its business activities to coincide with the cultural intricacies of the Japanese economic system.

The Japanese market holds great profit for those companies who are willing to make the long-term commitment.

Thank you.

Representative FIEDLER. Thank you. I must say that is as comprehensive a statement as I think I have ever heard on the subject. Don't go away because I want to talk with you for a few minutes.

You know, I think the last statement you made regarding the long-term commitment between buyer and seller is a very telling thing.

Mr. OKUMURA. Yes.

Representative FIEDLER. Because my own background is in small business—I handled both pharmaceutical items as well as cosmetics. And it seems to me that generally in the United States there is not that kind of long-term commitment either in terms of profits, that is how much profit is shown each year to the stockholders, as well as the long-term dynamics of the economy.

And that I think is a very significant point that you have raised here. I guess the question that comes first to my mind in light of that is, how dynamic is the Japanese marketplace? How committed do the people of Japan actually get to the products and services compared to the American market?

Could you just expound a little on that?

Mr. OKUMURA. Within their own marketplace in Japan?

Representative FIEDLER. Yes.

Mr. OKUMURA. First of all, in Japan when they talk about long-term commitment, long-range strategies, they mean businesses that plant and seed and reap profits 10 or 20 years later.

This results in expanding market share, even at the cost of immediate profit. Of course, we have to realize that the shareholders are structurally different—most of the shareholders are institutional, including your banks, who are more interested in long-term growth and expansion of market rather than short-term profit.

Representative FIEDLER. How much capital investment is available to the average Japanese business compared to the United States?

Mr. OKUMURA. If you have a viable product—project, literally unlimited. This is why every New Year's you find Japanese executives visiting their banks. To drink tea, but also to discuss long-term projects.

Because while it is changing, the equity-debt ratio is about 70 to 30, 70 debt in long-term borrowings from banks. And the banks encourage capital investment.

Representative FIEDLER. To what degree is indebtedness a problem or an asset to Japanese business?

Mr. OKUMURA. Well, recently, there was a move toward decreasing the dependencies on banks. To give you an example, Toyota has absolutely no debt borrowings, but for most other companies they still borrow very heavily from banks rather than enjoy the equity share that is common among American corporations.

The interest rate does hurt them, the bottom line. When American businesses go through a recession period, it becomes a burden on the companies. But I believe this problem with interest rates is offset by other factors such as innovative marketing, hard work.

You see, I go to Japan six times a year. I point out to my clients in the back streets of Ginza that the white collars all working until 11, 12 o'clock midnight. And they are not getting paid during those hours.

Representative FIEDLER. One of the points that you made that I would like to explore just briefly with you—and unfortunately we don't have an unlimited amount of time. I wish we did, because I am sure everyone who is going to testify today is deserving of much more time than we can give to it.

But I wonder if you could tell me a little bit more about the distributors. You almost sounded as if you were describing a situation where the company coming in has to sell the distributor on becoming a distributor.

So tell me a little bit about the necessity of persuading the distributor that you are a viable company. What is the psychology of the distributor in that situation?

Mr. OKUMURA. It's no different from doing business here in the United States. When you attempt to ask a distributor or a Japanese company to sell your products, I am a strong believer in basic market research. You must approach that distributor—I would even say it is an insult to approach that distributor without knowing the potential of that market for your product. It is best that you know more about the marketplace—the Japanese market—than the distributor.

Then you have earned your right to ask him to reach a certain sales level for the first year, second year, third year, and support that request by documented proof that the market is viable for your product.

Representative FIEDLER. Do you have to go through the distributor to sell in Japan?

Mr. OKUMURA. When you say distributor, there are many innovative ways to sell products.

Representative FIEDLER. Can you sell from the United States directly to the retail outlet?

Mr. OKUMURA. Yes, but you can sell directly to department stores but I don't think you want to sell directly to—considering the logistics of export—the 10,000 cosmetic and drug stores that Max Factor is currently selling.

One Japanese distributor told me that anything between the manufacturer and the end user—in the case of cosmetics, of course, it's the lady who buys the lipstick—is called an unnecessary evil. But it's necessary for the distribution of the product.

But there are many innovative—and this book does illustrate the different avenues a manufacturer can take to sell the products innovatively. There are many channels, multichannels—there's direct sales.

Representative FIEDLER. I have to ask you one last question. I can't let you go without asking you this. Having been a small business person myself, it sounds to me that for a small business that it would be very difficult to crack that market.

Because if you need to have the cross-cultural experience——

Mr. OKUMURA. Yes.

Representative FIEDLER. If you need to be able to bring the distributor over to the United States to show them that you are a viable business, if you need to take the time to develop a relationship, all of that is extremely expensive.

Small businesses cannot afford to invest that kind of capital not having an immediate return, not having access to unlimited capital, with capitalization being one of the biggest problems of small business.

So, could you just address that for a few minutes? Because that obviously concerns not only myself. Since the base of our economy is small business, we need to know whether it is possible to break in successfully without drowning yourself in costs to do it.

Mr. OKUMURA. Well, this is why I started this practice 10 years ago, to offer these small businesses a way to get in, an alternative, where the client—the manufacturer is the captain, I'm the pilot, hoping that it's the most efficient way to get them into Japan based on network.

I finally waited for my hair to gray. I'm 48 years old, which means all my classmates from Waseda University are in middle and upper management.

Representative FIEDLER. We are a matched pair in that sense.

Mr. OKUMURA. Is that what we are? And they are only a telephone call away from me. That's efficiency. Identifying the need, the product, I can call upon these hundreds of colleagues based on where they're coming from in an open and frank manner.

Depending on the budget of that firm, we could custom tailor the marketing strategy from finding one department store or chain of boutique shops. And after finding out a complete—doing a financial and operational profile on that chain, confirming that it's the right party, to contact them—which is not a big problem, a phone call, a telephone would do it, and just bringing the two together.

I would probably have to go—I certainly recommend that the manufacturer take the trip. And I coach them every step of the way, so that they can establish themselves in the comfort level I discussed earlier in the eyes of the Japanese potential—prospective buyer.

Representative FIEDLER. I thank you very much for the time you have given us this afternoon. Your entire statement will be in the record. I am certain there will be other opportunities for us to talk about this more in depth. But I found it extremely enlightening and I appreciate it very much.

Mr. OKUMURA. It was a pleasure and I am honored to have had this opportunity. Thank you.

Representative FIEDLER. If I ever get back into small business again, you may be hearing from me.

Mr. OKUMURA. All right.

Representative FIEDLER. John Zysman, is this timely for you?

Mr. ZYSMAN. I will be brief.

STATEMENT OF JOHN ZYSMAN, PROFESSOR, UNIVERSITY OF CALIFORNIA AT BERKELEY

Mr. ZYSMAN. Congresswoman Fiedler, it is a great pleasure to be with you. It is always a pleasure to testify and this issue amongst many in my view is of particular significance and importance.

I am a professor at the University of California at Berkeley where I direct a program called the Berkeley Roundtable on International Economy, which for marketing reasons has an acronym of BRIE.

We were concerned that people would remember the name, whatever other jokes might be made about it. It is a research and public policy program and we have done a wide range of studies on United States-Japanese competition, amongst other things.

We did the background studies for David Packard's United States-Japan Trade Advisory Commission from the American side. We have done a substantial part of the background papers for John Helm's Commission—the Presidential Commission on Industrial Competitiveness.

Outside of the university, a number of us from that group have a fairly extensive practice in helping American companies and Japanese and European companies, I might say, work out international trade and production strategies.

So that our experience is both based on sort of an analytic perspective and research perspective, and on hands-on perspective with a number of companies.

Rather than repeat a number of the things that the first and excellent witness has said, let me begin by saying that the problem is also part in this case of the solution.

The single, in my mind, most important step for American firms to begin to be successful in the Japanese market is to recognize that the Japanese market is not a marginal market. It is not a marginal source of additional profit.

It is rather a strategic market. It is a market in which if you succeed, you will probably be able to hold onto your American market. And in which if you fail, you are likely in the end to be fighting the same battle on worse terms in the American market.

And I think that is true now for three reasons, and it was not true 10 or 15 years ago. Though someone with great prescience might well have been able to see it. But it was for most companies not the case.

The first is that of the sectors where American industries have been literally overrun by successful Japanese companies, all of those industries follow a common pattern. An enormous mature market in Japan in which Japanese firms have honed their products, and even more importantly than the products, their production processes in a volume market, brought those products into the American market—sometimes not the identical products, but off of that product base—and used their production advantages in the American market to give them a price and quality leverage.

Now quality costs something. But sometimes the cost of that quality can be lowered through clever manufacturing and intelligent use of production resources. But in many cases, the production advantages are used for quality.

So that for American firms for the most part, unless they encounter that competition in Japan, they are going to face it here. In many cases, they won't see the products coming. They won't understand what the competitive advantages of the Japanese firms are.

Equally important, in many cases, they will fundamentally underestimate the technological advantages that the Japanese firms have.

I should say that the particular areas in which my program at Berkeley works, and I have worked over the last years, are in high-technology sectors, a large part in electronics. Our experience has been that many of the American companies that we have worked with have not in many cases known what components for their systems were available in the Japanese market and underestimated therefore how much of a technological advantage they would have.

So, my first emphasis is, once you have made a decision that it is a matter of life or death, all sorts of things become easier.

There is one small Seattle firm that—an electronics firm—has told us it spends $5 to $6 million a year marketing its product in Japan. It loses $2 or $3 million a year on that effort, and considers it a good investment for the reasons that I have outlined.

It feels that only—it doesn't feel at this point that I want to try and broaden it, but it feels only its presence in the Japanese market can keep it abreast of those conditions.

Now, I will come back to some of the ways in which some of those costs can be lowered and more effective strategies can be adopted.

Having said that, I would also—as I said to you in the moments before the hearing began—say that it is also true that only a consistent and supportive set of policies to open the Japanese market will permit American firms across the board to be successful.

We will always have success stories. But only with a consistent set of policies—and in some regards, I should say, some of the activities of the Special Trade Representative's Office in the high-technology sectors over the last couple of years have been I think quite admirable in that regard.

But we have a double phenomena in the areas like telecommunications where there is a deregulation-privatization that is really a reorganization of the Japanese market without a real loss of government control. New opportunities are clearly being opened for American firms, there is no question about that.

At the same time, many of the obstacles of entry are still there and many of the concerted techniques to, in essence, strip the technology off of the American companies and use the domestic market remain.

I mean, there is a moving band of protections, if you will, in Japan in which the areas in which the Japanese would like to establish advantage and those areas in which they have lost advantage are more insulated than in areas such as, if I may say so, cosmetics, consumer goods of certain kinds, which are not considered of the same strategic rewards.

But having said that, let me emphasize that the American firms that have had success over the last years—have had large and real success—have generally been firms that made the decision to go into the Japanese market in the 1950's and 1960's, and to make a massive investment in building a command of those markets, a command of the distribution networks, and the like.

It has been true in cosmetics, of course. It is also true with a company like Hewlett-Packard which—and it is important to note here, we will come back to it—was able to use an ever-changing product advantage to fill its product line in Japan with product that the Japanese couldn't effectively imitate. It ran away from the production problems by continuously innovating.

The problem is, not all firms can do that. Not all firms in the American market are in the market position that Hewlett-Packard is. Du Pont was a company like that. It established an on-going set of relationships.

Equally, it was companies such as Coca-Cola which was willing to play the game on Japanese terms. That is, Coca-Cola invested in Japan when only yen-based companies—that is, a company that was not operating in convertable currency. Coca-Cola could put its money in but it couldn't take its money out for 10 years.

It made the decision to go in anyway. It had a greater freedom of operation because it went in on that basis.

But even having said that and even having emphasized that there are a good number of success stories, one has to emphasize that companies like IBM, which around the world does not have a small share of the computer market, has in Japan found itself seeing its share of the market shrink steadily.

Even a company with the resources and the mastery of a company like IBM faces serious and severe problems from a mix of sides, both intense Japanese competition and encouraged competition. We will call it that.

Having said that, and rather than simply lingering on some of the past success stories which, I would agree with the last witness, do not indicate very much about what it will take to be successful in the future, let me make some remarks as to what I think companies need to do over the next years.

Let me—I agree with the emphasis you put, we will make a distinction here between what large companies need to do and what smaller companies need to do. Because the level of resources and the character of their position is substantially different.

The first thing which I think is true for both is that there are now a wide range of opportunities to enter the Japanese market in association with the actual business form to take a variety of arrangements—be it a joint venture, be it an association, a technology-sharing arrangement—but a set of arrangements with outsider Japanese firms. That is, Japanese firms which are not the dominant or major players in their industries.

Let me call your attention to one recent such arrangement which I think is quite a good one. LSI Logic in this part of the world hired the American head of NEC to lead its venture into Japan. Mr. Yumata did not simply leave on a whim; there was another piece to the story. It was because he had great entrepreneurial drive and was very effective.

Kawasaki Steel had invested into that venture as part of its strategy of moving out of the steel industry and using its managerial strengths to build upon its electronics basis. Quite a contrast with United States Steel buying Marathon Oil, which was simply a financial arrangement.

Kawasaki was in fact beginning to try and move its technology people out of steel and use the resources it had built up in the production of steel and try and apply them in this new area.

Now, Kawasaki Steel does not lack for its own contacts in the Japanese market. It is not a major player in the electronics business. As a result, the kind of deal that LSI Logic could strike with Kawasaki is quite different and is one in which, if it is intelligently managed, could give it an enduring position in that market.

If not intelligently managed, Kawasaki will learn the technology and sidle off into the sunset. But that is, I think, a good single instance.

The second element for large companies—large companies in many ways are better able to play those games. Because in Japan what is evident from the history of industrial experience is, you had best play from a position of real strength. If you are not in a position of real strength, it is very easy to be squeezed and pushed out.

The other element though that I would emphasize is that American firms that want to enter that market, whether they want to enter through a distributor arrangement and produce in the United States for export, or whether they want to produce in Japan, must give over the resources to matching the Japanese production innovations.

The real advantage the Japanese have built, which is sometimes understated in a discussion—in many discussions—is that in complex manufactured goods, that is goods with a lot of parts, a lot of components, that have to be assembled, there is a staggering cost advantage across the board for Japanese producers.

In the long run, the American companies—whether they be companies like Hewlett-Packard, whether they be companies that have more standard product—will not be able to survive in competition with those firms unless they make those adjustments.

Representative FIEDLER. How big is this advantage?

Mr. ZYSMAN. Well, a good instance—a concretization of it is that most of my friends in the automobile industry can see on a small car a $2,000 cost advantage to the Japanese——

Representative FIEDLER. Is that a result of labor costs?

Mr. ZYSMAN. No, it's not labor. The emphasis here is, the more parts it takes to assemble the product, the greater the Japanese advantage because over the last years product organization has been—production has been reorganized, production lines have been trimmed, overhead costs are dramatically lower, materials handling costs are lower. And in fact, in the end, flexibility and product variety is easier to handle in the reorganized lines.

The production advantage is not labor. It is labor—it is wage bill costs——

Representative FIEDLER. You are talking about management.

Mr. ZYSMAN. Right, it is management of production. It is not hourly labor costs. The wage bill in many cases is lower. But that is because in many cases the number of hours of labor required to produce has been cut dramatically. Usually by cutting overhead hours.

Now, if those advantages are not matched, the rest of the story in the end becomes secondary.

Representative FIEDLER. Could I stop you just there for a moment?

Mr. ZYSMAN. Please.

Representative FIEDLER. Can you tell me whether labor unions have an impact in this?

Mr. ZYSMAN. Well, in Japan the manufacturing innovations—and it would take some time to lay out why that was possible. The rapid growth in the markets in which they were copying foreign technologies taught the firms to rapidly alter production lines, to rapidly absorb changing production when they were simply catching up.

In that period, a strong relationship between management and workers was crucial. It is important that it is not simply an issue of the presence or absence of labor unions. Similar kinds of things can be found—in not quite such a dramatic way—in Germany, and can be found in certain parts of Scandinavia.

Where in fact there is production flexibility, because there are broad definitions of jobs. The narrow definitions of jobs of the sort that American management and unions have wanted are the problem. If you have very narrowly defined jobs that are reinforced by——

Representative FIEDLER. Then you have an investment in the status quo.

Mr. ZYSMAN. And you can't change. It is very difficult to change rapidly. In England where that's at its worst, or was at its worst, automobile companies were unable to make product changes quickly because of that set of problems.

Again, I emphasize, it's not simply a matter of whether or not we have unions and it's not just that unions are bad guys, because in many cases in the United States management has wanted to narrowly define job structures and has been willing to pay in the form of higher wages to get them in order to have control of the shop floor.

It is a——

Representative FIEDLER. I am just trying to understand the dynamics there. I think you have hit on what is a really vital difference in the flexibility aspect.

Mr. ZYSMAN. Absolutely. Levels of skills of the workers, which is increasingly—if I may make an aside—over the next 10 or 15 years is going to be a problem also.

As Japanese literacy rates are now extraordinarily high, our literacy rates are relatively low. The Japanese are educating their populace for the kinds of skills that the next generation of production will require. And we are not.

I think that will be, in terms of flexibility, only highly educated and skilled workers can really inbed that kind of flexibility in the sophisticated production lines.

I would hate to see us end up in a relatively weaker long-term position. But with that said, for large firms there is that possibility.

For smaller firms—and I include when I say "smaller firms" such billion dollar corporations as National Semiconductor or Advanced Micro Devices—simply do not have the resources to muscle their way into the Japanese market.

In that case, what I think we are going to need to see is not simply sophisticated marketing, although that, of course, is necessary. But the emergency of what I would call a group of high-technology trading companies. Let me emphasize this—a standard product in the United States so there is no clear product advantage is going to have a very difficult time getting into the Japanese market.

Because if it is made there, distribution networks are already full. This is not, to put it mildly, a developing economy. As a result, most of the firms that will lead the way in will have some form of a technology or product advantage.

The product advantage may be consumer identification. It may be—but many of them will be high technology firms. In many of those cases, a number of the problems will have to be solved jointly, whether it be real estate problems, whether it be problems involving how to test their products as they come into the market. There are a range of kinds of things which I think will be done in that way—under the label of trading companies.

Because it will also take substantial cash.

Representative FIEDLER. It's interesting that you mention that. I made a note as you were talking, before you raised this point, on the issue of pooling resources by small businesses. That is essentially where you are heading with this concept.

Mr. ZYSMAN. That's right. The initiative will have to come I think from some of the larger financial institutions. That is, simple consulting firms will not succeed at this. They just don't have the muscle.

One of the problems is, where do you get people to run these kinds of things who have had experience operating in Japan from a position of power. There are very few.

Representative FIEDLER. Consulting firms?

Mr. ZYSMAN. Well, consulting firms don't really—what I mean is, if you look at the Japanese firm deciding to go into a new market area, you know, you will find the firm willing to commit billions of dollars to that operation.

The question of what you can gain by pulling together and using strength is not obvious unless you play the game. I know very few Americans who have ever been in the position to play in the Japanese market with the kinds of resources that are available to Japanese firms.

Their view of what you do is quite interesting and quite different than that of others. That is, how you can use substantial resources to build a permanent position for yourself?

Other kinds of firms will have to do joint efforts, as I say. Not just trading companies, joint manufacturing operations and, in some cases, joint distribution operations.

But in order to reach the need, the decision to do that, those firms will have to be convinced of two things. One is that these markets are strategic and critical. And, second, that they can't do it alone.

I think once they reach those two conclusions, we are starting to see a number of discussions leading in this direction. That is, leading toward the notion of trying to assemble resources.

I think I have said enough. I would like to stop. So if there are any questions you would like to ask me before I have to run off, with your permission?

Representative FIEDLER. First of all, thank you very much for being here. Again, you provided a different perspective, a different thrust to your comments. It is just a tremendous opportunity for me, I must say, to have a chance to hear your insights, as well as Mr. Okumura's comments, and those of the speakers to come.

You mentioned one thing that I would like you to elaborate on briefly because it is one of the things I can do something about as a Member of Congress, and I hope as a Member of the U.S. Senate.

You talked about a consistent and supportive set of policies in the United States. Would you just touch on some of those policy positions that you think are essential? What kind of timeframe you are talking about, recognizing the political dynamics in which we work?

Mr. ZYSMAN. Let's take one——

Representative FIEDLER. If you had your choice?

Mr. ZYSMAN [continuing]. Specific area, an area like telecommunications. That is, by making this concrete, I am simply making the general point clear.

In Japan, there is some willingness to begin to open the telecommunications markets. At the same time, even within an organization like NTT, or even within the Ministry of Post and Telegraph which officially regulates the system, there are sharp differences in which those who would like to see liberalization of the system and those who would like to see an opening of the markets are often pitted against, in bureaucratic fights, those whose positions are more traditional.

One can see it in the telecommunications area in which there have been some quite spectacular fights, visible fights, when certain kinds of American gear were not certified. In some cases it was joint ventures in which the Japanese partner's gear which was American and which was not certified required additional pressure from the top of the organization.

Consistent American political pressure and spotlighting of these kinds of activities can, in my view, help those in the Japanese Government who would like to see these markets opened.

Equally, I think one of the elements that is important is, we shouldn't throw away the trade assets that we have. Let me give you an instance, again in the same arena, of what throwing them away means.

When we deregulated the American telecommunications markets, which was a choice and probably a good one, we also opened up the American market to foreign competition in telecommunications without asking for any quid pro quo from anyone else.

Now, there was no necessity of automatically opening our market without saying, fine, we're going to now—the deregulating means that there will be a competitive market, and if you want to have access to that market we would like to make that an issue of open trade negotiations.

I think we—in hindsight, it's not just this administration. It's the previous administration. We should have seen that. I think increasingly, with a greater sensitivity to the international issues, we should use those kinds of cards in a way that provides us a chip in a bargaining arrangement.

Representative FIEDLER. Don't you think though, the reality is that in the political environment in which we function in the United States, there tends to be very much of a crisis mentality in managing problems. So that until a crisis occurs, there is not sufficient attention given to a problem as it develops.

I think in the trade situation, we see the perfect example. And, of course, with constantly changing political dynamics—not just in terms of parties because there is such a broad range of opinion within the Democratic and the Republican Parties—that constant change in approach lends a distinct advantage to a country like Japan, that has a common culture and a common thread running through basic business practices that provides for a continuity that isn't provided for in the United States?

Mr. ZYSMAN. I think that is certainly true. I think we will continue to pay a substantial price as long as we don't——

Representative FIEDLER. For the next decade.

Mr. ZYSMAN. Well, we don't have decades. I think that is the real problem. I think we are going to have to in the trade arena make sure that some of the agencies and institutions have the resources, for example, to deal with these issues on other than a crisis basis.

Representative FIEDLER. And a commitment.

Mr. ZYSMAN. And a commitment, that's right.

Representative FIEDLER. That is one of the things that I have seen for a number of years now. When I first won election, I won in a very urban area. It was reapportioned to include agricultural as well as urban interests.

And representing a large number of citrus growers as well as other ag interests, I became involved in the trade issue that way. One of the first things I saw as I began to explore trade problems—in the broad sense, not just a single commodity or single product—was that there had been no continuity.

I put together a bill, which I won't bother going into here, to try to deal with the longer term interest in it. But, unfortunately, politically it tends to be a case of trade this year. It is something we are looking at because it represents a political problem.

But when it is not a political problem, it gets neglected. Politics is such that they are now looking at something else, because this year it is something else that is important.

So there is no continuity in addressing these problems. I see that as a big liability when you are trying to break into a market where you have substantial cultural differences, substantial differences in consumer practices, and obviously in trying to establish a consistent policy over a long period of time, which is the thrust of your comments.

Mr. ZYSMAN. Well, I agree. The question is, how to do it?

Representative FIEDLER. Identifying the problem is one thing. Identifying the solution is another.

Mr. ZYSMAN. Well, it's—in the end, that's an executive branch choice.

Representative FIEDLER. Well, it is also important that that is understood. It is just as you have to go over and market under certain conditions in the Japanese market, uniquely different, let's say, from marketing here. We, too, who are part of the political process, have to understand the dynamics of the environment in which we are working to devise policies which can be as dynamic as they have to be in the marketplace.

Mr. ZYSMAN. I agree with that.

Representative FIEDLER. That is a different kind of challenge.

Mr. ZYSMAN. Well, meeting the Japanese competitive challenge is going to be a strategic problem for the United States in general. I would encourage everyone who is in a position to do so to give great points to making sure that the institutions and resources of the Government to provide the sustained leadership on that or——

Representative FIEDLER. You can be sure that there is one member that will.

Mr. ZYSMAN. Good.

Representative FIEDLER. I thank you very much for your time and your testimony. I know, on a busy day for you, this has been a bit inconvenient. We appreciate your being here.

Mr. ZYSMAN. It's been a pleasure.

Representative FIEDLER. Your statement will be entered into the record and I am sure that all of the witnesses today will receive a copy of the final version.

Mr. ZYSMAN. Thank you very much.

Representative FIEDLER. Thank you.

Next, Russell Geiger, president of Delta Electronics, from Alexandria, VA. Thank you very much for coming.

STATEMENT OF RUSSELL E. GEIGER, PRESIDENT, DELTA ELECTRONICS, INC.

Mr. GEIGER. Thank you for inviting me, Congresswoman Fiedler. There have been remarks made about gray hair. Now you are looking at gray. There have been remarks made about small business. Now you are going to hear about really small.

That remark about the $6 million in promotion in one market, last year was the first that Delta topped $6 million in gross sales worldwide. So, you have some idea how small we are.

By way of personal background, I remember during the AT&T divestiture proceedings the term "plain old telephone" came into use to describe telephone service as most people know it. I think I've spent my life in plain old radio.

I was about 5 or 6 when my dad brought home our first radio, put headphones on my head, and I heard someone say, "This is WGY Schenectady." I don't think I have ever taken those headphones off, figuratively speaking.

After a college education which lasted from 1939 to 1947 because of World War II, I graduated from Ohio State with an electrical engineering degree. I came to Washington, where I was convinced everything important happened, and worked for several years as a consultant in radio and doing some classified assignments for the military and intelligence communities.

In 1951, I began 15 interesting and very rewarding years with Radio Free Europe, first as Deputy Director and then as Director of Engineering.

In 1966, I came back to the States and joined Delta which had been started a few years earlier by friends of mine. I have been there ever since as executive vice president and now as president.

Delta is a 100-percent employee-owned small business located in Fairfax County, VA, just about 15 minutes from downtown Washington, DC. The firm, which employs 75, was founded in 1962 with the goal of becoming a profitable and rewarding—let me use that word again—rewarding operation through the development, manufacture, and sale of proprietary products for professional use in broadcasting, communications, and allied industries.

This plan has been followed over the years, though from time to time inhouse development has been supplemented by the acquisition of patents and the execution of licensing agreements to obtain additional know-how in our field.

Delta's founders had backgrounds that included extensive technical experience in international radio broadcasting and communications, so from the outset it seemed perfectly natural to sell abroad as well as domestically.

In recent years, these export sales have ranged from 18 to 43 percent of our sales total.

Representative FIEDLER. Would you describe your product?

Mr. GEIGER. Yes, indeed I will. They generally fall into two categories. One is a group of measuring, monitoring, and test equipment which are used by radio and communications stations throughout the world.

The other major product area is in high-power radio frequency transmission line switching—a long expression, pardon me, for coaxial cable switches, in so many words. Not the size that you find in the TV production studio, but rather cables that are 3, 6, 9 inches in diameter.

Without making an exhaustive study of our sales records, I can recall more than 60 countries in which we have managed to find customers. We have equipment operating on all six continents including, I think, three devices in Antarctica.

My firm's experience with selling to Japan has probably been different from those that you hear about in many businesses that come to your attention. We haven't made any particular effort to target Japan as a market, and we have done nothing particularly different from the approach we have used in other areas.

Most probably because of the nature of the products we manufacture, we've encountered no visible restrictions on importation, no reluctance to buy from a non-Japanese source, and no requirements for formal marketing agreements.

As a result of our efforts—or perhaps I should say noneffort—it—the Japanese trade—has been a steady contribution to our annual sales.

Representative FIEDLER. Could I just ask you a question in that area?

Mr. GEIGER. Yes.

Representative FIEDLER. How much competition is there for what you manufacture?

Mr. GEIGER. Well, that is precisely the point. We have attempted to confine our efforts both here and abroad to areas where the competition is least.

Representative FIEDLER. Thank you.

Mr. GEIGER. As I pointed out, the dollar volume of our sales to Japan has been quite modest, never representing more than a few percent of our total sales.

For that reason I would like to think of the following comments as a sort of general sales philosophy for export, rather than a customized approach to any specific country or area.

The most important factor in our successful selling, both at home and abroad, has undoubtedly been our ability to identify products which do not have to be marketed in intensively competitive situations.

That old admonition, "If you can't lick 'em, join 'em," holds true. But I might like to add, "And if you don't want to join 'em, at least avoid 'em." In other words, more simply stated, "compete by not competing."

You will recall that I mentioned that Delta's game plan involves products for professional use. There are no consumer items in our line, nor is it expected that there will be any. Many of our products may have a lifetime production quantity of a few thousand—maybe even a few hundred pieces.

This is not an attractive arena for those firms that are geared up to produce and market hundreds of thousands or millions of an item.

There is, of course, the possibility that some other small businesses will identify the same limited requirements and create competition. But at least that is competition among equals.

If I may use one more frequently heard expression, getting there "fustest with the mostest," as the old general said, often helps discourage these would-be sharers in the limited market.

One of the advantages of manufacturing to meet small, specific market needs is the relative ease of identifying the customer base. As an example, most of Delta products fall into the two areas that I mentioned earlier, products which are used by broadcasting stations, by communicators, the third-party traffic—or public-traffic handlers of the world, the telecom administrations, and so on, and military activities concerned with medium- and long-range communications.

Both actual users and the contractors who build capital facilities for them can be identified and approached using conventional marketing methods. Since most of the people we need to reach are professionals—scientists, engineers, and technicians—it's possible to obtain good exposure through advertisements and occasional feature articles in trade magazines and newspapers, professional society journals, handbooks, and other printed matter.

English is widely used, of course, but on occasion we have had promotional material translated for regional publications. Spanish and Chinese come to mind as recent examples.

Another common and certainly productive marketing approach is exhibiting at trade shows and conventions. The major world-class shows do indeed draw visitors from all over the world.

In our industry, the annual conventions and equipment displays of the National Association of Broadcasters and the Armed Forces Communications and Electronics Association fit into this category.

There are generally many visitors from Japan and other countries in the Orient. While their primary interest may be in major equipment items, they also are interested in specialized products of the kind that Delta makes.

We have for years exhibited regularly at home and abroad. We have not as yet shown equipment in Japan, but we have definite plans to do that within the next 2 years.

Delta depends heavily on leveraged marketing. Most Delta products are made to be used in conjunction with other equipment as part of a sizable technical installation.

If you were to hand the user a Delta product all by itself, he would say, "It's quite nice, I like that shade of gray. It blends in with the scenery. But what do I do with it?"

Well, it makes sense therefore to become acquainted with and work with those prime contractors who build the broadcasting and communications facilities and with the manufacturers of major items such as radio transmitters.

These organizations are, in general, inclined to rely on dependable outside sources for peripheral and accessory items rather than to develop their own in-house capability.

By becoming such a dependable source, and by showing a willingness to work fairly and consistently with larger firms in the preparation of bids and proposals, we are able to promote our products as part of a larger, more comprehensive marketing effort than we could ever mount by ourselves.

Here, again, we have an example of cooperating, not competing, with the larger players in the game.

I haven't mentioned the use of agents or distributors. Delta prefers to deal directly with the end user, or through a prime contractor as described above. In many cases, because of distance, language problems, or local custom, this is not practicable.

In some countries, it is even mandatory that the sale be completed in the name of a designated local agent. In these cases, we attempt to locate a firm or an individual with sufficient technical knowledge to understand the applications of our products in the market.

They must also have the disposition and the patience to promote the products over what may be a lengthy introductory period and to persist for literally years in getting equipment specified and purchased for major capital facilities programs.

We maintain a full-time representative in London to provide this function for the European area, but in other parts of the world we either work directly or share representation.

In Japan, we have informal and nonexclusive arrangements with two technically competent firms who keep alert to market opportunities. We also sell directly to major manufacturers on occasion.

Finally, I should acknowledge that some of our best promotion comes from our customers. We have been fortunate in having our products in service in many showcase installations at home and abroad. Visiting broadcasters and communicators see Delta equipment in an operating environment and think of us when specifying for their own future requirements.

Reviewing my remarks, I can't help but feel that there really is little if anything original in them. The most important consideration, in my opinion, is to find a market niche where you are comfortable with your technical competency, your manufacturing capacity, and your financial resources.

Find ways to work with, rather than against, potential competitors. Find ways to use other, larger companies' marketing experience and capabilities by becoming suppliers to them. Try to avoid confining, exclusive marketing arrangements.

Ideally, on a major radio construction project with a requirement for Delta equipment, we like to be included in all of the would-be contractors' proposals. This requires discretion, fair dealing, and the confidence of those parties that you will not reveal their individual strategies.

In dealing with Japan, we have used, as appropriate, all the approaches mentioned. I am certain there is a much greater market for our products there, and within the limits of our resources we will be directing our attention to that market.

Those were my prepared remarks. Listening to what went before, I am tempted to add just a few more comments. First of all, it sounds like we have a pat formula here for sales. That is not the case at all. I wish we did have a pat formula.

But there is more competition—perhaps competition of a different kind. It's a little like going from Washington to New York. If you want to take a train, you have Amtrak. But you can also fly, drive your car, ride the Greyhound, or whatever.

To some extent, that sort of competition we are always up against—other methods, other ways of doing it. So we still have to get out there and scratch.

We also have taken on more and more complex, innovative, technically advanced designs as time goes on.

We find ourselves now, I guess, inviting more competition by moving into the military markets with military specification equipment and things of that sort.

But it is a matter of walking before you run. We feel we can start to run a little bit at this stage of the game.

We have not done a lot of what I suppose you would call cultural accommodation. To be frank with you, the people we deal with from Japan and other countries generally meet with us on a sort of technical level where perhaps the product is sold more by what it does than its appearance, the way it's presented or such factors.

Representative FIEDLER. To what degree do you have hands-on influence on the sales aspect of this? It sounds to me like you really have a strong leadership position in your company.

Mr. GEIGER. Well, we do. Almost everybody in the company has to be a salesman when you're that small. Our marketing—we have a marketing manager, he has two assistants and an order taker. But all the officers sell, our engineers sell, even the man who goes out to do an installation. He is expected to leave behind goodwill or perhaps prepare the way for some equipment or accessory or something of the sort.

I think the reason we like to work with our end customers is we feel that's the way they will be most satisfied with what we sold them. As pointed out earlier, commitment to reliability and competence and what have you is very, very important.

Representative FIEDLER. That brings me to another question. How often does your product need replacing? Could you explain that?

Mr. GEIGER. Yes, I wish there were more of it.

Representative FIEDLER. Is this something they can expect to replace in 5 years, 25 years?

Mr. GEIGER. You're closer the second time. Most of our products—well, they would probably work indefinitely but we assume that about 15 to 20 years down the line most people will be rebuilding their plants and using a new-broom approach, or there will be sufficient advances that things will start to become obsolete.

But replacement is indeed a problem. Once you have sold, you either sell something different to the same customer or move along and look for new customers.

Representative FIEDLER. How much R&D do you do? That is, how much change is there in your products? If you have a product that is going to last 25 years, are they going to need that product for 25 years or are they going to be needing something different because of the changes in technology 5 years from now or 7 years from now?

Mr. GEIGER. We try to prepare for that, of course. About 8 percent of our budget annually—8 percent of sales is budgeted for development of new products. And we keep quite a staff just busy thinking up new ways to do things better in entirely new products.

Representative FIEDLER. What is your profit margin?

Mr. GEIGER. Well, let's see. Let's take this last year. Let's say sales of about $6 million. I guess income before taxes was about 10 percent of that, a little more. After taxes, something less.

Representative FIEDLER. That's pretty good.

Mr. GEIGER. It's been reasonably profitable. We do indeed try to have a replacement on hand for each major product which we feel is approaching obsolescence. And in many cases because of the small numbers involved, we have continuing evolution of the product. Frequently we can upgrade a customer's device and bring it up to modern standards.

Representative FIEDLER. One more question for you. Could you please tell me how long it takes from your initial contact to the time you actually sell the product? You described rather a long and involved leadtime.

Mr. GEIGER. Right. In many cases, there is. The other extreme are the emergency calls that come by telephone and say, I need a new so-and-so piece of test equipment, and you ship it out by air that day if you can.

But the big-ticket items, the things that go into capital installations, they do indeed take a lot of time. Under the best conditions, probably 2 or 3 years is the shortest. I think about 2 years ago we finally started to meet deliveries on one equipment project that was begun in 1966 when I first came with the company. It had a period of gestation of approximately 16 years. That's the other extreme.

Usually there are many years involved in the planning of a major facility.

Representative FIEDLER. So you are talking about an ongoing business relationship that permits you to plan ahead that distance.

Mr. GEIGER. Yes.

Representative FIEDLER. I can only assume from that that there is a great deal of stability within your company management.

Mr. GEIGER. We like to feel that is the case. The people who started the company back in 1962, there are I guess four still around. Of our middle and upper management, there's only one person who has had less than 15 years with the company. And that individual is a replacement for someone who retired and had to be brought in from the outside.

Representative FIEDLER. It sounds like a good success story.

Mr. GEIGER. We try to be. Thank you for the opportunity to tell you about it.

Representative FIEDLER. Thank you very much. And thank you for taking the time to come out here and give us your insight from a different angle on this problem.

Continued success to you. I look forward to seeing you back in Washington. I'm sure we will be doing more of this.

Mr. GEIGER. Thank you.

Representative FIEDLER. Thank you very much.

Let's go to the agricultural panel. Steven Easter, California Almond Growers.

STATEMENT OF STEVEN EASTER, VICE PRESIDENT, CALIFORNIA ALMOND GROWERS EXCHANGE

Mr. EASTER. I will state again, my name is Steven Easter. I am with the California Almond Growers Exchange. I am vice president of that organization.

I am here really to talk not so much about the exchange but about the exchange's effort in the Japanese market. But I would like to tell you a little bit for the record of what our organization is.

We are an agricultural marketing cooperative that handles almonds grown in California. All of the almonds in the United States are grown in California. We handle about 60 percent of the production that comes from some 5,600 grower-members in the State of California, and we market them worldwide.

Currently, about 70 percent of our production is marketed in the international market, making almonds the leading food export in California. It is from that basis that we look at the Japanese market as an integral part of our total marketing effort and as a very important part of the overall market for California almonds.

Now, the Japanese market is one of our fastest growing markets, and it is one that we look to as a very integral part of our total marketing operation and not as sort of surplus disposal operation or anything else of this nature.

But it might be of interest to look a little at how we started there. I don't come here as an expert on Japan, nor as an authority on how everyone else is going to get into the Japanese market. But I do come here to express a little bit of the successes we have had there and perhaps someone else can draw on that.

The testimony that I have provided for the record really is an item that was prepared for us in Japan—I shouldn't say "for us," it was on us I should say—as an illustration of a company that has been successful in the Japanese market from outside, you might say.

However, I think the key to what's happened to us there is that it didn't happen overnight. We have been in that market since about 1955, at which time we started looking at it as a long-term market for us, as one that would provide growth and stability as far as an outlet for our product.

It has ended up doing all that. But we have had to change some of our ideas as we progressed in the marketplace. What's happened to us roughly there was that, as I say, we started in 1955 selling a few thousand pounds of almonds for the candy trade.

At that time the almond was virtually unknown except for the candy trade in that market. So we had to build it from that point. We began building it by using the traditional trading company distributions systems by selling through a trading company.

We soon found that that wasn't progressing nearly as rapidly as we would like. So we expanded it to take it away from the exclusive arrangement and divided it among some seven different trading companies; which proved adequate to distribute to some of the trade in the confection industry and a little bit in the bakery area. By 1967, I'll put it, it became obvious for us to truly develop that market we were going to have to make a larger effort.

So, we entered into an arrangement of establishing our own market development office and began exploring various opportunities in the Japanese market.

That market development office is staffed by Japanese. We do not have a manager in Japan that comes from the home office. The manager who has very successfully operated that office is Japanese and has had a great deal of latitude to operate in the Japanese market.

We have grown from the point in 1967 to the present where we have an office that completely supervises all of our marketing activity in Japan, including developing new programs for market, and does consist of some 55 people in that market.

During this period we've grown from—in 1967 when we started—a sales in terms of millions of pounds—we'll put it in that kind of a context, rather than dollars—of about 5.9 million pounds of almonds that were sold in 1967, to the last complete marketing year which ended last June 30 we sold some 34 million pounds.

So, in that period we've seen substantial growth. And we have done it because of approaching the market through this somewhat different marketing and developing effort.

One, we have taken our personnel and put them into a position where they could meet with the trade there and look at some of the unique methods of distribution and unique tools—I guess you might say—that were available in Japan.

For example, we have a fairly large staff of cooking demonstrators that work with the Japanese cooking schools to demonstrate our product and show them how to use almonds in the various cooking applications.

We also have approached directly some of the bakers and other trades that have allowed us then to develop the market in those particular areas.

We have, more and more, widened our distribution channel so that we're not relying exclusively on the trading company's channels of distribution. And one area where we were able to succeed in this was in the distribution of snack almonds, as opposed to almonds for ingredients.

We found that using the distribution system in Japan for snack almonds became virtually prohibitive, price-wise, by the time they went through as many channels of distribution as were necessary traditionally in Japan.

So we were able to develop a relationship with the individual Coca-Cola bottling companies in Japan—there are some 17 of them, and it has taken us about 10 years. But we finally have developed a relationship with all 17 bottlers—in which they take our product and put it into their normal distribution channels which are channels that are much more direct than traditional Japanese distribution channels and more like you are used to here where you are taking your route truck and distributing directly to the retail outlet.

And through that, we have been able to build a rather substantial snack almond trade. And the almond, while not cheap, is still less expensive than it would have been if we had gone through the layers of distribution systems.

So these are some of the methods that we have used. But I think it is important to recognize that we are dealing in a product that is not produced in Japan. We are dealing with a product that because of there being no production in Japan, that there are very few barriers to our product entering the market.

We have very few barriers. There is a 4-percent duty on almonds entering the country. And as a result, the access question has not been a major one with us. We realize this is unfortunately not always the case.

But ours has been a situation where we have been relatively free to operate in Japan and over, as you can tell, a relatively long history have found a successful way to operate in that market.

The barriers that we have now are primarily the tariff, which is lower than it was 20 years ago but even then it was only about 12 percent. So we have had some success both in operation and reduction of tariffs in that market.

I think as far as my statement is concerned, that's probably sufficient for me to stop now and see if there are any questions. Or if you want to go on to the other panel members and then take questions all at once.

Representative FIEDLER. It seems to me that what you have really described here is a ground-up kind of approach to marketing. You started at a very modest level at best and developed a system to enter the market that involved the full scope of marketing techniques.

Mr. EASTER. Well, that's——

Representative FIEDLER. Which is an interesting angle, and different from some of the other comments.

Mr. EASTER. That's true. I was listening to some of the comments earlier about size of the company. Our company is probably 10 times larger today than it was when we started in the Japanese market. So we really started in a relatively small way and built during that period of time.

So we started as a fairly small company, not just in the Japanese market but as a company per se. And there has been tremendous growth over the last 30 years in our company and in the almond industry.

And so we had to start in a fairly small way. But as we were able to grow, we could see progressive steps that could be taken to provide the growth in that market.

Representative FIEDLER. It sounds to me like you probably had good-sized commercial sales as well as retail, is that correct?

Mr. EASTER. Yes.

Representative FIEDLER. You mention bakers, I assume that you are going into hotels, schools, and cafeterias?

Mr. EASTER. That's correct. Actually, in fact, we continue to get as large or larger development in the commercial or bulk area of almond sales as in retail. Retail is a newer phenomenon. We started out in the other areas and then——

Representative FIEDLER. That is newer here in the United States, as well, if I recall.

Mr. EASTER. That's correct. Historically and traditionally, most usage has been in the bulk area rather than a snack item. And a similar development has taken place in Japan.

We still see a lot of very innovative developments. This is one thing we like about giving our Japanese office a lot of autonomy. Because we tend to find a great deal of innovation comes from that market that we can even apply to our U.S. market.

But even beside that, there are differences in taste, differences in culture and so they're able to adapt the almond to products that are desired in Japan.

Representative FIEDLER. Is almond paste a big seller?

Mr. EASTER. It's used there, but it's not a big item. The uses that you find in Japan as far as the bakery and confection uses are probably similar to what you see here. But what we find in Japan is perhaps—well, let me go back a little bit.

When we started in Japan, what we often would do is show them products that were produced here in the United States that they might wish to develop for the Japanese market.

Well, then they got involved in the market, got involved in making confections, and we've done sort of the opposite. We bring a lot of the Japanese products over to this country to show some of the American confectioners the fine Japanese products that are being made.

So it works back and forth from that standpoint. Also, there are a lot of unique products—a recent one that they've put out, for example, is a soy-flavored almond. A lot of the Americans who have tried it like it as well.

But it was developed in Japan for the Japanese market, and has been quite successful there.

Representative FIEDLER. Almonds are a very diverse food, they can be used in many ways.

Could you tell me what impact the strong dollar has had on your sales, if any?

Mr. EASTER. Well, I think it's interesting to discuss that in the context of the Japanese market because as you know, the dollar value has not fluctuated versus the yen nearly as much as it has versus many of the other currencies of the world.

Our Japanese market, because of that, has seen a rather steady development even during this period of a very strong dollar have seen, however, with the recent lowering of the value of the dollar that it has given the Japanese market a bit more of a boost.

But we really see that effect in most other markets more than we do in Japan. Europe, quite dramatically. Certainly it has been a big assist in terms of our overall export efforts.

But the Japanese market, because of the obvious attempt that they have made to keep the yen and dollar more or less in parity, has not been nearly as affected by the strong United States dollar. So our business has been pretty constant over the last several years there. Actually, it has grown.

Representative FIEDLER. I thank you very much for your testimony. I appreciate very much your taking the time to be with us this afternoon.

Mr. EASTER. Thank you. It is a pleasure.

Representative FIEDLER. We will put your prepared statement in the record at this point.

[The prepared statement of Mr. Easter follows:]

PREPARED STATEMENT OF STEVEN EASTER

THE CALIFORNIA ALMOND GROWERS EXCHANGE EXPERIENCE IN JAPAN: A Marketing Success Story

The California Almond Growers Exchange, based in Sacramento, California, increased its annual sales to Japan nearly 15-fold between 1955 and 1984 by creating and cultivating a market for almonds and almond products in a country which had been almost totally unfamiliar with that commodity. A combination of skill, perseverance, patience, creative marketing strategy and a dedicated team effort helped increase sales to Japan from 22,000 pounds of almonds in 1955 to more than 32,000,000 pounds in crop year 1984.

There are many parallels between CAGE's efforts in Japan and its highly successful domestic U.S. marketing strategy.

WHAT IS CAGE?

California Almond Growers Exchange (CAGE) is a cooperative which was formed in 1910 by 230 California almond growers to process, promote and market their almonds under the "Blue Diamond" brand for the best price possible. At the time, in-the-shell sales represented the industry's entire business. Today, due to the innovative efforts of CAGE, shelled and unshelled Blue Diamond almonds are now used in some 2,000 forms and sold to 88 foreign countries.

From the heart of California's almond country in the Sacramento and San Joaquin valleys, all through the Central Valley from Red Bluff in Tehama County to Bakersfield in Kern County, almond orchards are spread over more than 600 square miles. California has the world's largest almond-producing region, and almonds are now the state's leading food export.

One of CAGE's earliest challenges in the U.S. market was to overcome reliance on Spanish and Italian almond suppliers. Innovation, and patient, careful developmental strategies played a key part in the Exchange's success, and by 1938, Blue Diamond shelled almonds began appearing in cans and cellophane packages throughout the U.S., as well as in chocolate bars. With a steady, high-quality supply available domestically, American chocolate manufacturers turned more and more to Blue Diamond almonds.

CAGE has continued innovating, bringing out new forms of almond product both for industrial use and for direct consumption. With record crops and yields, the Exchange is at this time carefully putting in place such innovations as almond butter as part of its effort to further expand domestic consumption of almond products.

ENTERING THE JAPANESE MARKET

Japan and the U.S.S.R. are now the fastest growing major markets in the world for California almonds. Almond consumption in Japan has been steadily rising and the Japanese now consume almonds at an average annual rate of one-quarter pound per person. In 1955, almonds were almost unknown in Japan -- except in the chocolate trade.

When CAGE sent its first almonds to Japan in 1955, it did so as part of an overall export strategy -- not simply to get rid of surplus products, as has been the case with many U.S. agricultural exporters. At the time, CAGE was experiencing record sales overseas because a European crop failure had dried up an important source of almonds. The Korean War had stimulated sales of almond chocolate bars, and many new products such as diced, blanched and slivered almonds had been introduced to consumers, creating strong new domestic markets.

CAGE was able to meet two essential requirements for the Japanese market: quality and assured supply at stable prices. Candy manufacturers were thus able to develop and market new products with the assurance that they would have a sure and consistent supply of almonds. While it is sometimes difficult to supply an agricultural product consistently and in accordance with demand, CAGE made a strategic decision that the Japanese market was worth the effort to commit to that market whatever supplies were necessary -- as with the U.S. market -- before supplying other export markets.

While building its presence in Japan's chocolate market, CAGE also set about to develop the bakery trade. Through assiduous market cultivation, which has included developing and distributing recipes and sponsoring nationwide baking contests, as well as by keeping its supply of almond exports sure and steady, the cooperative was able to construct a market from scratch which today absorbs some 40 percent of California's almond exports to Japan -- about the same amount taken by Japan's confectionery trade.

CAGE's first sales to Japan were made through a trading company, on an exclusive basis. Experience soon taught CAGE that exclusivity did not give the trading company an incentive to promote Blue Diamond products, so "exclusive" rights to market Blue Diamond were given to a group of seven trading companies which specialized in compatible food areas. This technique was adequate for servicing existing market sectors, but did little in terms of further developing or expanding those markets. In 1967, when exports to Japan were at 5,900,000 pounds, a decision was made to set up CAGE's own market development office in Japan. Within four years, almond exports to Japan doubled.

Presently, the CAGE market development office in Japan consists of 54 Japanese staff members charged with coming up with ideas and techniques to develop more almond consumption in Japan. Headed by Masuo Koga since 1969, the employees are divided into teams according to the areas of marketing in which they are involved; those areas include bulk sales, retail snack sales, and advertising and market development.

OVERCOMING DISTRIBUTION HURDLES

Japan produces no almonds, and political problems have not been a hindrance to trade. Today the tariff stands at only four percent for raw product. The

Japanese distribution system, however, was a major stumbling block for CAGE in the early years. CAGE's response has been to use different distribution strategies for their three market sectors: confectionery, baking and snack.

Relying completely on its trading company network to sell almonds to Japan's chocolate industry as it does in other countries, CAGE's general sales manager in Tokyo works directly with Japanese industrial customers, who buy large quantities in bulk. Working directly with the manufacturers has the added advantage of spurring innovation and developing new markets. In fact, an almond soap developed in Japan is now exported to the U.S., where Japanese-developed almond milk may also find a market.

To service the baking industry, CAGE sells its products through a network of trading companies, which in turn resell to large wholesalers. Those wholesalers will supply some users or resell to a smaller wholesaler. The smaller wholesaler will also supply users, as well as resell to distributors who will sell to individual shops. At the same time, CAGE's marketing staff works with bakery associations to promote usage directly by users.

Naturally, with so many links in the distribution chain, the cost of the almond product spirals upward, but because it has a high perceived value and usually represents only a small portion of the value of the finished food product, the cost is bearable.

The nut roasting trade -- in which the almonds represent 100 percent of the finished product -- is quite different. A multi-tiered distribution system would make the cost of packaged nuts prohibitive. To service this market segment, CAGE created -- over a ten-year period -- individual distribution arrangements with each of the 17 Coca Cola bottling companies of Japan. The bottlers distribute the Blue Diamond brand snack almonds directly to their accounts, thereby bypassing the costly distribution channels.

CAGE management wasn't aware of many of the intricacies of the Japanese way of doing business before venturing into the Japanese market. The importance of personal relationships to business decisions, for example, was something Blue Diamond learned by trial and error. The success of CAGE ·ests in large part in its ability to learn from its successes and failures, and steadily build upon them.

PRODUCT PROMOTION

When CAGE strategists learned that many young Japanese women attend cooking school prior to marriage, for instance, their response was to make almond cookery a part of cooking school curriculum. CAGE has several cooking school demonstrators on its payroll who are available to teach classes on cooking with almonds, free of charge, at many of Japan's 700 cooking schools. CAGE has also reached young consumers by introducing almonds to Japan's school lunch program and by providing almond recipes to the program. These have been highly effective forms of advertising and market development for Blue Diamond products, with countless Japanese households becoming familiar with the taste and versatility of California almonds and almond products.

CAGE has not overlooked traditional advertising and promotion techniques, either. In fact, it employs three advertising agencies for print, billboard and radio and television advertising. In addition, a publicity agency sponsors contests and handles general promotion.

Today, California almonds are the largest U.S. horticultural export. The domestic market is also strong, with Americans consuming, on average, one-half pound of almonds per year. But CAGE managers aren't content to rest on their laurels, and are constantly on the lookout for new and improved ways of utilizing almonds in order to increase consumption levels in both domestic and export markets. Indeed, Mr. Koga feels there is ample room for growth in the

Japanese market and he looks forward to increasing average annual consumption of almond products in Japan to one-half pound per person by the year 1990.

Representative FIEDLER. Obviously, the agriculture community needs as much help as it can get right now to make up for some of the difficulties that it has been facing over the past few years. I am sure that other producers will gain some insights from the successes which you have described.

I would like to call Mr. Hughes from Kingpac. Thank you very much, you have been very patient.

STATEMENT OF WILLIAM D. HUGHES, CHAIRMAN AND CHIEF EXECUTIVE OFFICER, KINGPAC INTERNATIONAL, ON BEHALF OF WESTERN STATES MEAT ASSOCIATION

Mr. HUGHES. Congresswoman Fiedler, my name is William Hughes. I am chairman and chief executive officer of Kingpac International located in Carson, CA.

Kingpac is a domestic international sales corporation and the exporting arm of King Meat, Inc., which specializes in the fabrication of high quality U.S. beef. My experience consists of 40 years in the meat business in southern California and 16 years in exporting meat to the Pacific Rim nations.

The company is a member of the Western States Meat Association, and I am speaking here today on behalf of that organization.

Representative FIEDLER. Before you go any further, may I ask you just one quick question?

Mr. HUGHES. Sure.

Representative FIEDLER. Fabrication of meat, what does that mean?

Mr. HUGHES. We take a carcass of beef and cut it up into smaller pieces.

Representative FIEDLER. Thank you.

Mr. HUGHES. Western States Meat Association is a trade association representing meatpackers and processors in the 14 Western States. Among other interests and activities, it has a particular interest in export issues regarding Pacific Rim nations such as Japan, since many members of the association export considerable quantities of meat and byproducts to that market.

Our products are not ones of high technology, but rather high quality basic American agricultural products. Kingpac International is also a member of the U.S. Meat Export Federation, a broad-based trade association working to increase U.S. exports of red meat, particularly beef and pork, through market development, trade servicing, and reduction of trade barriers.

I also serve on the board of directors of the U.S. Meat Export Federation. USMEF has an office in London and in Tokyo, Japan. The Japanese office is staffed with a bilingual director and staff.

The U.S. Meat Export Federation is a unique organization because it is comprised of many other associations. For example, the American Meat Institute, U.S. Farm Bureau, the Kansas Corn Commission, the Western States Meat Association, the National Cattleman's Association, Texas Feed Lots, and so forth. So it is rather broad-based.

Kingpac International is dedicated to the Japanese market. In 1985, we exported about 11 million pounds of high quality American beef to Japan alone, with a market value in excess of $12 million.

Our tonnage of meat shipped to Japan has been growing steadily ever since we made our first shipment back in 1971. I have been personally involved in the development of our company's growing trade relationship with Japan and the other Pacific Rim nations.

I, and other members of my firm, have visited this area at least 25 times in the last 10 years to meet with trade representatives or to participate in seminars and trade shows in order to promote our products.

However, I certainly cannot take all the credit for our firm's success in the Japanese market. It has been an effort of a very dedicated team. I am pleased to say that our team was recognized in 1981 when our firm received the prestigious Presidential "E" Award for excellence in exports, the first such meat company ever to receive this award.

We are not a Midwestern company, we are a California company.

Representative FIEDLER. Congratulations on your award.

Mr. HUGHES. It wasn't our volume that was recognized, but our efforts at opening new areas for U.S. meat.

I will direct my comments primarily to the Japanese market because it is our largest market in the Pacific Rim area and because it has the economic ability to purchase United States high quality beef on a continuing and increasing basis.

Japan has been an important beef market not only for Kingpac but for California and the United States as well. Shipments have steadily increased from the United States over the past several years, growing from about 35,000 metric tons in 1978 to 79,000 metric tons in 1984, with an estimated market value of over $400 million.

These figures do not include revenue from related products such as animal oil, hides, and the variety meats. By comparison, the United States' next best foreign customer for beef is Canada, which imported only 12,000 metric tons of United States beef in 1984. Naturally, the majority of all Japan-destined shipments pass through our California ports.

Japan is an extremely challenging market due to a myriad of complexities that do not exist in the domestic marketplace. The solutions to these complexities are as diverse as the problems themselves.

Japan represents, unlike Canada, an utterly foreign culture, with traditions and ways of doing business wholly unlike those of the United States. It has taken me years to learn how to negotiate properly with Japanese customers, and even longer to progress through the complex Japanese business structure, with its associations and quasi-governmental organizations, all of which have a direct bearing on our ability to trade in the meat market.

Culturally, we are selling a relatively new product to Japan. When Buddhism was introduced to Japan in about the 6th century A.D., Japan went from being a minor meat-eating nation to near abstinence. A reversal did not begin until late in the last century, and was not of any consequence until after World War II.

Even today, Japanese per capita beef consumption is less than 7 pounds per year, compared with over 70 pounds per capita per year in the United States. But I feel optimistic about these statistics because they leave a lot of room for growth for United States beef in the Japanese market.

Not all of the challenge of selling beef in Japan is cultural. As in any nation, there are political complexities, too. These complexities come in many forms, but of most importance are quotas and domestic price protection through quasi-governmental agencies.

The Liberal Democratic Party, which has been in power in Japan for a lengthy period of time, relies on the farm vote for the bulk of its support. Consequently, the LDP is very protective of the Japanese farmer.

To this extent, in 1961 Japan constitutionally established a quasi-governmental organization to assure price protection for the Japanese livestock producer. This organization is called the Livestock Industry Promotion Corporation. We refer to it as LIPC.

It is impossible to discuss the beef market in Japan without acknowledging the LIPC, since it is the purchaser of 90 percent of all imported beef. The remaining 10 percent is allocated to specific user groups. I use the term "allocated," since all beef imports are under a strict quota system.

The LIPC uses its 90 percent share of the beef imports to stabilize the domestic market by first determining the floor and ceiling prices, then withholding or releasing product from its inventories to raise or lower prices. The LIPC, not the end user, determines what specific beef cuts it will purchase, and then releases the beef only to authorized beef wholesale dealers. Quite contrary to our method of doing business.

The General Agreement on Tariffs and Trades—the GATT agreement—encourages countries to treat imported product as favorably as domestic product.

The LIPC, however, uses imports to regulate supply, support domestic production, and stabilize prices, and while doing this make a profit and increase the cost of imported beef to the consumer.

Thus, under this kind of system it is difficult for an exporter to build relationships with wholesalers and retailers. An effort to correct this situation was made in 1984 when new negotiations with Japan led to the signing of a beef trade agreement calling for a modest quota increase and the formation of a "simultaneous buy-sell" system of trade.

Representative FIEDLER. I am going to stop you right there just for a few seconds because I happened to be involved in that. I went to Japan and met with Prime Minister Nakasone. As I mentioned before, I represent—then and now—a significant citrus industry.

I was involved with the beginning of the citrus negotiations. Unfortunately, we weren't able to get an agreement as quickly as we would have liked, or raise the quota as we would have liked.

But when they finally did come to agreement, it was as a result of a long-term effort. I am sure you were very intimately involved as well. I had met with Nakasone, and Nakasone had made a commitment to me at that time.

And there were other people with whom I was working who were specifically interested in the beef negotiations. We put together a letter when discussions broke down, stating our side of the issue, and what we were going to do in the event they didn't come to agreement.

And within 24 hours they actually sat down and were willing to sign that agreement. So I watched this very closely and it is interesting to me to hear your testimony on this aspect of the negotiations. Because I know how important it is.

Mr. HUGHES. Well, as you mentioned, it is quite complex and not simple. I sat on the trade negotiations in Honolulu on the beef and citrus issue some 4 or 5 years ago, one of our earlier meetings with the STR's office.

It was the first time trades people had been present during the negotiation. It was quite a shock to the Japanese because they then realized that the beef and citrus industries were available to our negotiators for information and facts.

So it was a unique situation where the several citrus associations and myself representing the beef industry were there at our own expense, to back up our trade representatives.

We have had a little turnaround in recent years from our Government's support of our efforts which we are deeply appreciative of. The slight increase in quota, the SBS system—the quota has been increased but the SBS system is not working. It has worked its way around so it is still under control of the LIPC.

Representative FIEDLER. What you are saying is there needs to be a reevaluation of the results of the agreement?

Mr. HUGHES. Yes; we were asked to be patient by the LIPC. We have been patient. And it is still under their control.

Representative FIEDLER. One of the Japanese's greatest assets is their patience.

Mr. HUGHES. Exactly.

Representative FIEDLER. I often use the term "Stonewalling." But regardless of how you describe it, it is successful.

Mr. HUGHES. Yes; it has been very successful for them, very unsuccessful for the American beef and citrus industries.

Representative FIEDLER. But we are working on it.

Mr. HUGHES. We are making progress.

The challenging nature of the United States and California beef trade with Japan is not due solely to the complexity of the Japanese side of the arrangement. Here in the United States we have also contributed to the problems and misunderstandings.

For instance, ours is one of the very few exporting meat companies that I know of that labels any of its products in Japanese, even though most Japanese people do not speak English, particularly the Japanese blue-collar workers handling the product such as in loading and unloading.

So we take it upon ourselves, along with the use of metric weights, to label our meat products in Japanese.

We have had a little reluctance on the part of the United States beef industry to develop products tailored specifically for the Japanese market. But it really doesn't make much difference because we can only sell those items to Japan that LIPC will buy.

Naturally, we are not going to sell T-bone steaks to Japan. I think any of us in the beef trade realize that you very seldom see a knife on the table. So we sell boneless cuts, smaller portions.

Representative FIEDLER. How about sausage and processed meat?

Mr. HUGHES. Then we get into the Ministry of Health and Welfare. And the list of banned chemicals, nitrates and so forth and so it becomes even more complex. Also they have three or four very large meat companies in Japan that are making sausage.

So, you don't see very much cheese going to Japan, manufactured cheese. Certain chemicals are not permitted on imported products that we traditionally use.

Representative FIEDLER. Those same chemicals can be used in exported products, I understand?

Mr. HUGHES. Yes; you might wonder why we pursue the Japanese market in the face of these cultural, political, and national trade barriers. But we see progress.

Through individual efforts and those of our trade associations, we have exposed the Japanese public to United States high quality beef. And through the efforts of the trade associations, our Foreign Agriculture Service, and especially the STR's office, the quotas have been gradually increased.

The continued positive pressure must be maintained by all concerned, not to force cultural changes, but to educate. Not to politically interfere, but to remove political interference from free trade.

All of this will have an orderly, compounding effect as the quotas increase and the price of our beef will decrease, and at the same time making it even more popular.

I would like to digress just a moment about the popularity of U.S. beef. Many times the Japanese in political positions tell us, well, you must realize beef is a new item to Japan. It is not very popular.

And we rebut that with a particular instance when our Commerce Department—I believe Juanita Krebs held the Cabinet post at the time—negotiated a deal with the Japanese to have a trade show of American goods, and we were given the use of a vessel which toured several Japanese ports with American goods.

American beef was relegated to one of the below deck positions. She received a special quota for this meat. After much negotiation, we got up on one of the upper decks where we could be seen.

The quota, which was supposed to go directly to the Commerce Department, and in turn the meat would be sold at cost someplace in the neighborhood of American meat prices.

In turn, by the time the deal was made, the deal wasn't made. By then the Japanese meat associations got involved. You can't go direct; it must go through one of their members. The association was called All-Japan Meat Association. So it had to go through them.

Originally, the item was to be beef steaks. That was changed. We had to ship some shortribs which are not traditionally a Japanese item. In the meantime, they had near-riots at each port. People selling had to ration the meat.

Naturally, meat isn't popular at $10 a pound. It wouldn't be popular here. You get it down to $4 or $5 and it becomes much more popular. So we take that all with a grain of salt, knowing that with the support of Congress, the STR's office, and so forth, that if we get the quotas increased, we will have no problem selling our product. None whatsoever. It's getting it in.

So we still feel very committed to shipping our meat to Japan. It is the world's finest. We are committed to helping to resolve the trade issues that stand in the way of free and fair access to the Japanese market.

We have found the challenge of the Japanese market really stimulating and fulfilling.

If I may answer any questions, I would be happy to.

Representative FIEDLER. What would be your top priority in United States Government policy development regarding your particular industry and Japan?

Mr. HUGHES. Well, we would like to establish specific targets on the increase of the quota. We have participated in trade shows in Tokyo with 53,000 attendees. Out of the 53,000 attendees, there were probably only 5 who had quotas to buy meat.

It is a little ridiculous to stand all day and display your wares if the customers can't purchase. So we feel the critical item is orderly increase of quotas.

We realize we can't go in and say, "Abolish your quota system." It is too deeply politically involved. We are not that naive. But we think there should be some firm, positive demands on increasing the quota.

We can live with a 25-percent import duty, which is much higher than most of the other Pacific Rim nations. That doesn't stop the movement of the meat. But quota systems are likened to a black market situation. The quota alone has the value of money.

Representative FIEDLER. What kind of leverage do you think we ought to use in increasing those quotas?

Mr. HUGHES. Anything, except a trade war. There are no winners.

Representative FIEDLER. Could you tell me a little bit about how the costs of shipping affect your competitiveness in the Japanese market?

Mr. HUGHES. The cost of shipping are minimal. To give you an example, the freight to Hong Kong is approximately the same as it is to Tokyo, within a penny on a pound.

Our freight runs between 9 and 13 cents a pound, depending upon the commodity. Dealing in a high price steak item of, say, $3 a pound wholesale in California, 13 cents a pound is insignificant. That same piece of meat will sell to a hotel in Hong Kong at $3.75 a pound, and will sell to a hotel in Tokyo for $13 a pound.

Representative FIEDLER. Could you compare the beef that is produced by the Japanese, and the American beef that you export to them?

Mr. HUGHES. That is a little more complex. We hear of the Kobe beef, Matsusaka beef; it is a wagyu breed of which we have a few in this country. We are experimenting with them. The animals are more mature. It takes 4 or 5 years to produce them, where our average beef is slaughtered at 15 to 18 months.

The amount of this high quality Japanese beef, which the Japanese often refer to, is so miniscule it doesn't mean anything. They also slaughter dairy animals. Our beef, our USDA prime grade beef, is probably not as good as this miniscule amount of Matsusaka beef, but it's better than anything else beyond that.

And as a worldwide average—American beef is a standard worldwide for quality beef. In the Hilton Hotel in Berlin or the Hilton Melbourne in Australia or in Hong Kong, this is the standard.

Representative FIEDLER. How much of an impact, if any, do health practices—health and cultural practices—have on the growing interest in beef and the potential market there?

Mr. HUGHES. I don't think health practices have any bearing at all. Most of all—we are very grateful for all of our Japanese tourists. We have an operation in Honolulu also servicing hotels and restaurants. And one of the first things the Japanese like to do is order a nice beefsteak.

I don't think health has anything to do with it. And culture, I think it has very, very little to do with it. Or McDonald's wouldn't be so successful there. Their largest store is in the Ginza.

Representative FIEDLER. Do you supply to McDonald's?

Mr. HUGHES. No. Again, up until a few years ago, the McDonald's hamburger in Japan would not resemble the McDonald's here because of the meat quotas. It had very little beef in it and a lot of everything else.

Currently, McDonald's has standards in this country that demand all U.S. products. So, it is a combination of the trimmings from our fatter cattle, our feedlot cattle, and our cow meat from our culled-out dairies.

In Japan, they use a similar formula. They buy what they call a boneless plate from the United States because it has the flavor in the fat of the meat, and lean meat from Australia. It is now equal in chemical lean content and flavor as the U.S. McDonald's.

Representative FIEDLER. I don't think I have any more questions for you at this time. I am very grateful for your coming today, since I have an interest in this particular area.

As you are aware, I am a candidate for the U.S. Senate, and expect to represent the cattle industry as well as the other agriculture industries throughout the State. I will be working very hard to try to learn more about the economic dynamics.

I am particularly interested in your trade problems. So I appreciate your insights today, and I look forward to working with you more closely in the future. You will probably be hearing from my staff.

Mr. HUGHES. Thank you for listening and thank you for your support.

Representative FIEDLER. My pleasure.

I see a young lady back there saying she is going to represent Sunkist.

Ms. ABBOTT. Yes, I am.

Representative FIEDLER. Where is Bill Quarles today, out fulfilling the rest of the quotas to Japan?

Ms. ABBOTT. He is doing his best.

Representative FIEDLER. Send him my regards. Would you like to introduce yourself?

STATEMENT OF ELAINE ABBOTT, INTERNATIONAL ECONOMIST, SUNKIST GROWERS, INC.

Ms. ABBOTT. Yes, I will. My name is Elaine Abbott. I am an international economist with Sunkist Growers, Inc. Sunkist Growers is a nonstock membership cooperative marketing association representing approximately 6,000 citrus growers with orchards in California and Arizona. Sunkist's principle business activities are the sale of fresh oranges, lemons, grapefruits, and tangerines, and the manufacture and sale of processed citrus juice and peel products.

Last season our sales totaled approximately $837 million. About one-third of our fruit is directed to export markets. The development of the export market has been an integral part of the growth and expansion of Sunkist. Our earliest exports of fresh citrus date back to 1892, with significant volume being first attained in the 1920's. Today, we export citrus products to approximately 50 countries. Japan is our largest foreign market. Last season Sunkist sales to Japan were valued at approximately $96 million.

Development of the Japanese market first requires, of course, access to the market. In 1975, Japan's imports of fresh oranges amounted to 15,000 metric tons. Orange imports this year will be over 100,000 metric tons. It will be up to 126,000 metric tons by 1988 in accordance with an agreement on the expansion of the orange quotas of Japan. The increases in Japan's imports of fresh lemons and fresh grapefruit have been equally dramatic. Japan's imports of fresh lemons have increased from about 17,000 metric tons in 1964 to over 100,000 metric tons annually, while Japan's imports of fresh grapefruit have increased from 6,000 metric tons in 1971 to well over 100,000 metric tons annually.

Japan does maintain high custom duties on imported fresh oranges. Currently, California oranges are subject to relatively high customs duties which range from 20 percent ad valorem to 40 percent ad valorem, depending on the season. The high duty adds to the cost of the fruit, which means we must work harder to develop a demand for the oranges.

We started to develop the Japanese market for citrus products by utilizing an exclusive distributorship. As business grew, we realized we should sell to all qualified importers. By "qualified," we mean those who are able to handle imports, have a distributorship network and support our efforts in Japan. The establishment of mutual trust and a good business relationship with a distributor is very important in Japan.

We support our sales effort in Japan through chartership arrangements which include weekly shipments to Japan, careful handling, proper storage, and proper unloading in Japan. All this is done under Sunkist's supervision to guarantee good arrival condition of the product. Sunkist has its own inspectors which inspect the fruit before it leaves California and on arrival in Japan.

Our packing houses pack a special grade for the Japanese market because that is what the Japanese demand. The Japanese associate large size with quality. The fruit must look good to the consumer. Cosmetic appearance is very important.

Our home economists participate in the development of the market through visiting major chain stores when there are major promotions, appearing on local cooking school and college programs, doing television and radio interviews, working with the Japanese School Association, the Japanese Institute of Nutrition, the Japanese Housewife Association, and other groups to supply accurate and helpful information about our products. Our initial advertising efforts in Japan were brand advertising programs, but with a significant emphasis on how to use more lemons and, later on, more grapefruit. Our marketing efforts are concentrated on Tokyo, Nagoya, and Osaka where 60 percent of all households are located.

We recently started to develop secondary markets in Japan for imported citrus. Our research indicates that the per capita consumption of imported citrus of the average household in these secondary markets is substantially below that of the average household in the primary markets.

Our advertising and promotional efforts in Japan include the full range of available media and are directed at both the trade and the consumer.

In conclusion, development of the Japanese market requires both access to the market and, like in any other market, meeting the demands of the trade and the consumer.

I would be pleased to answer any questions you may have.

Representative FIEDLER. Thank you, Elaine, very much for being with us. I don't have as many questions for you as for the other witnesses because I have represented the second largest number of Sunkist growers in the country. I have had a chance to become very familiar with the process, all the way from the growing to the selection-separation process.

I have also had the opportunity to represent your interests in my meeting with Prime Minister Nakasone, and helping to shepherd the citrus and meat negotiations to a positive conclusion.

I feel a special pride in Sunkist Growers. You have done an outstanding job. I have had a chance to see some of your marketing promotions, and that is one of the reasons why we wanted you to come and put this testimony in the record today.

So I want to thank you very much for being with us.

I know that your patience and the efforts you put into developing your marketing is paying off over time. I look forward to continuing to work with you toward that end.

Ms. ABBOTT. Thank you very much.

Representative FIEDLER. Thank you.

All right, Mr. King, you are on.

STATEMENT OF RICHARD C. KING, PRESIDENT, RICHARD KING INTERNATIONAL, AND CONSULTANT, CALIFORNIA ASSOCIATION OF WINEGRAPE GROWERS

Mr. KING. Thank you very much, Congresswoman Fiedler. It is nice to be here today. As you know I wear many hats in the business arena, but I have my wine hat on today.

My name is Richard King and I am president of Richard K[illegible] International, an international business consulting firm tha[illegible] about 25 years' experience in working with the Pacific Rim, particularly Japan.

Today I am representing the California Association of Winegrape Growers, which is an organization representing about 1,100 winegrape growers in the State of California, the largest organization of its type in the country.

I might also add that the winegrape growers, with regard to Japan, work very closely with the Wine Institute and the new marketing order recently established called the Wine Growers of California. So you put that all together and you have a lot of people interested in wine.

My particular responsibility for the Winegrape Growers of California is to address the reduction of trade barriers to the export of California wine in the Pacific Basin, particularly emphasizing Japan.

Let me start by saying that Japan is a very, very important market, or I should say potential market, for California wine. When I say California wine, you will have to forgive me because that is almost synonymous with American wine since California produces about 95 percent of U.S. wine.

Under the Trade Act of 1984 and the Wine Equity and Export Expansion Act of the Trade Act, Japan was designated as a major wine trading country and one that we should address in conjunction with the USTR in reducing trading barriers to California wine.

The wine industry is very interested in Japan as a market because of 120 million people who have come to a sense of increasing affluency. They have more money to spend on wine. They have become more familiar with wine.

The exposure of the Japanese certainly to California and the United States has developed a taste on the part of those people. But even in Japan, a greater number of people are switching to wine, becoming accustomed to the tastes, and I must say dry wines which we tend to do a better job on.

At the present time, to give you some idea of the market, Japan is the second largest market for California wine after Canada, and one of the fastest growing.

Our exports to Japan have doubled in the past 3 years and we now have about 7 percent of the bottled wine market—the export bottled wine market in Japan, as compared to about 4.8 percent 3 years ago.

I might add, now don't get overjoyed by that increase. It comes from a very small base. But, nevertheless, some progress is being made.

It is interesting to note that Japan, unlike many other commodities, has an overall trade deficit in wine. They have about a $70 million trade deficit in wine. The reason they do have a trade deficit in wine is the result of a higher consumer demand in Japan. Changing drinking habits are influencing that per capita consumption. They have a small domestic industry to address that market and limited grape acreage.

To meet this demand and to minimize this deficit, the Japanese, of course, import 50 percent of its wine. That deficit is partially alleviated by offering more favorable tariff on bulk wines and virtually no tariff on what we call grape must—which is a combination of the grape and the juice which is set into wine. Those usually come from the GSP countries of Japan, the underdeveloped countries.

So the bulk imports into the Japanese market represent about 60 percent of all imported wine. The bulk, as our Japanese friends know, is mixed with a very limited amount of Japanese wine and called Japanese wine.

Now, the regulations in Japan are if you have 5 percent of domestic product and 95 percent of imported bulk wine, it still can be labeled Japanese wine. The majority of that wine comes from Eastern Europe and has, of course, been a very, very successful export for Eastern Europe to Japan.

Also with regard to this trade deficit, while Japan has an overall trade deficit in wine, they have a trade surplus with the United States of $4.5 million in wine. The reason for that is that the great demand for sake in our country which is considered a wine sort of offsets that thing. The tariff on sake is 25 cents a liter as compared to 70 cents a liter for California wine going to Japan.

So, that is sort of a background to what this market is all about. Now, let me just take about 5 minutes to discuss the concern of barriers and what the California wine industry is concerned with.

With regard to Japan, there are primarily two barriers to the exporting of California wine. One is in tariffs and one is in the area of domestic tax—that is, Japanese domestic tax.

Let me first address the tariff issue. Japan, from the United States point of view, has a rather complicated three-tier tariff system, which I won't go into because it is too complex.

But let me just state that up until April 1, 1985, the tariff on California wine—United States wine—going to Japan was 55 percent ad valorem. Japan announced April 1, 1985, that that would be reduced to 38 percent ad valorem, for which we were very pleased, and while this reduction is encouraging and we are pleased to see it, it gets the tariff down to 70 cents a liter, but it is still a high tariff compared to relative tariffs in the United States and the EEC.

As an example, the United States tariff on wine is 10 cents a liter and the EEC is 12 to 14 cents a liter, as compared to the 70 cents in Japan.

Many people say, well, why isn't the wine industry doing a better job in Japan. I think one of the reasons is that this high tariff has discouraged California wine industry from making an all-out effort to really promote its wine in Japan.

But even with these tariffs, we are making progress. Last year we exported 950,000 gallons of California wine to the Japanese market.

Regarding the tariff again, the wine industry does take the position that it is a discriminatory tariff to the degree that it falls heaviest on the least expensive wines and lightest on most expensive wines.

The California wine industry and the United States wine industry to remedy all this is really asking the Japanese to reduce the tariff to a very simple procedure of one tariff across the board at 10 percent ad valorem. Perhaps phasing that in over a period of years to minimize the revenue impact on the Japanese Government.

I am pleased to say here today that the wine industry is pleased with the fact that the Japanese recently moved up a third tariff reduction which they had planned for April 1, 1987. They moved that up to April 1, 1986, this year, and reduced their tariff further from 38 to 30 percent.

So in essence, in 3 years we have come from 55 percent to April this year of 30 percent. We like that movement in that direction. We feel that if that movement continues, and we get to that 10 to 15 level, that some of these tariff inequities will be alleviated.

The second major barrier is the domestic tax area of Japan. And, Congresswoman, as you well know, there is not much we can really do about domestic tax in Japan except call their attention to the inequity of that tax.

Representative FIEDLER. Could you describe that in more detail.

Mr. KING. Yes, I am going to get into that. It is a serious problem. The excise tax is a national excise tax. The amount of tax that is applied depends pretty much on the type of wine, the value of the wine, the container size, whether it is sparkling or sweet wine, and the alcoholic content.

The purpose of the tax for the value of wine is described in terms of the manufacturer's selling price. That is the basis on which the tax system works, that is the manufacturer's selling price.

Imported wine is taxed on the manufacturer's selling price formula—again, it is a complicated formula. But domestically made wine, that is wine made in Japan, it is our understanding has their option to be taxed on either the manufacturer's selling price or a suggested retail price.

So depending on the value of the wine, it is the feeling of the United States wine industry that the excise tax discriminates against imports and favors the domestic wine industry in Japan.

In response to the wine industry's pressure on that particular issue, we are very pleased to report that just recently the Japanese Government has raised the maximum nontaxable price, as we call it, from 1,020 to 1,080 yen. That again is a move in the right direction.

We call that a luxury tax. So in essence they raised the level of that tax so that medium-priced wine can get in without being taxed.

So these are encouraging trends, but still the tax problem domestically is a problem for the U.S. wine industry.

Finally, in addition to tariff and taxes, we have still a slight concern in a technical area. And that is a matter of what we call sorbates and benzoates in wine. These are chemicals that are a result of the winemaking process.

In Japan, as we know who are very sensitive about health standards, Japan has a regulation that we could not have more than 200 parts per million of sorbate and no benzoates in the wine.

The U.S. wine industry takes the position that that's an unrealistic figure. It should be at least 300 parts per million, and we are working on that.

So in summary, let me just sort of package it for you. The barriers currently facing the California wine industry relative to Japan include:

First, the reduction of the existing 30 percent ad valorem tariff to 10 percent.

Second, the more equitable application of the excise tax.

And third, technical adjustments in the sorbate and benzoate area.

Again, in fairness to the Japanese, they have agreed to lower the tariff to 30 percent effective April 1 this year. They have raised the domestic tax level from 1,020 to 1,080 yen. They have agreed to discuss the sorbate and benzoate issue within the framework of bilateral negotiations.

I would like to add finally here that, just like anything that has been testified here, and I have other clients in this room, reducing the tariffs is one thing. We are concerned about that and some of the policy matters.

The other side of the coin is that all of us have a responsibility in our industry to do a better job in the marketplace. I would just like to take about a minute to point out that barriers are important. But I also feel that the California wine industry—and this is self-criticism—has to do a better job of developing the market in Japan and educating the Japanese consumer to the advantages of California wine.

As many of us know here, the Japanese have been brought up on French wine. As a matter of fact, I believe that almost inherently the Japanese translation for wine comes out like French wine.

So we have to convince the Japanese that California wine can match the French in quality.

Representative FIEDLER. Any day.

Mr. KING. That's right. You must be a good consumer.

Representative FIEDLER. I am.

Mr. KING. So we must do a better job of promoting I think in Tokyo and Osaka. More seminars, more promotion, more generic promotion about California wine to call the attention.

So in conclusion, I would say this. I believe frankly that the wine trade between Japan and the United States can be a very positive influence in the total bilateral relationship. I believe it can help to reduce the tension between our countries.

I believe that wine is slowly but surely getting to have the same symbolic value as beef and citrus, and probably will get into that same category soon.

Also I believe it is significant to point out that the Japanese really don't have a great industry to protect in this area. I think that the Japanese could show some significant breakthroughs to the rest of the world by liberalizing wine.

Further, JETO, the Japan External Trade Organization, points out that according to their prognostication that for at least the next 5 years you are going to see an annual growth in the rate of wine consumption in Japan of 15 percent.

I believe that if Japan and the United States Government cooperate and reduce the tariff and do something about the tax, and we do a better job of administering and promoting, we can have an exceedingly exciting market for California wine.

Representative FIEDLER. Let me ask you a question. The situation that you have described resembles a lot of the problems that we are having worldwide—not just with Japan—in reducing trade barriers.

You have described what is, proportionately, a substantial tariff reduction over a 3-year period.

Mr. KING. Yes, that's right.

Representative FIEDLER. Yet that still leaves it seven times as high as the United States tariff imposed on the comparable Japanese product—sake.

I am not proposing this—I want to make that very clear—but I would like your reaction. If the United States were to sit down with the Japanese Government and say, we are going to keep 10 cents a liter tariff if you will reach that in *x* amount of time.

If it is not reached within that period of time—6 months, a year, whatever—then we are going to put the same tariff on your product as you are imposing on ours.

What kind of an impact do you think that would have?

Mr. KING. Well, that's interesting. That is reciprocity. That has been looked at and discussed in the past and I think that is an area of negotiation.

Representative FIEDLER. It is not my position, I might add.

Mr. KING. Right.

Representative FIEDLER. For me, personally. Nor I believe for you.

Mr. KING. No, right. As you know, I think the whole concept of applying more strict reciprocity in these commodity areas is becoming a more popular concept.

Frankly speaking, I don't believe that is too impressive to the Japanese. We sort of floated that informally.

Representative FIEDLER. Did they think you were serious?

Mr. KING. I believe so. I believe so. Our negotiating posture with the Japanese has been a very positive one. As the gentleman from the beef industry said, we have been patient too and not tried to push too much and make steady progress.

Frankly, speaking for the industry, I would prefer holding those kinds of things in abeyance and see what the Japanese can do in the negotiating posture we are in now.

Now, to get back to your point. If we don't see much progress, then maybe that is the time to try something like that out again. But we find out when you start talking about, well, you know, if you don't reduce the tariff on our wine we are going to up the tariff on your sake—it's not that impressive.

Representative FIEDLER. Just a reflection, a personal reflection. I think that one of our problems has been that we have not been serious enough about our trade relationships in the past. There is a climate right now, at least within the U.S. Congress, if not at the national level, because this is an issue that obviously affects certain industries and certain regions.

But there is a climate right now for applying a great deal of pressure to try to resolve some of these problems. That climate will not be there indefinitely. It is a fluid situation.

I was just curious how you would respond if we were to adopt a very tough negotiating posture. You happen to be the person sitting there. So I am asking you, though.

I could have asked it of any one of the other people who have testified this afternoon. I am concerned that we may lose momentum and lose the opportunity to make continuing progress—which is obviously my personal goal and I am sure the goal of almost everybody sitting here today—by being too patient and not applying what leverage we have to the negotiation process. But I just wanted to raise that question.

Mr. KING. It's a good point.

Representative FIEDLER. This momentum shouldn't be lost just because a step has been made in the right direction.

Mr. KING. Right.

Representative FIEDLER. I would feel very badly, as a person involved in the political arena with responsibility to try to improve the situation, if we became so complacent with the progress we've made that we didn't keep moving aggressively to keep that progress going so that we can achieve the most open market possible in as many areas as possible. Of course, we must recognize that the political dynamics of Japan are no more conducive to massive changes than our own.

Mr. KING. It's too bad we don't have 2 more hours. We could really go into this. But let me give you my reaction. And I was told by the committee that I might get involved in general discussion on this subject.

Representative FIEDLER. Yes. In fact, I would like to invite anybody who would like to, to come back up to the panel for a discussion. Please let me hear your comments on any issues you felt weren't raised during the course of this hearing.

[At this point, Ms. Abbott, Mr. Hughes, and Mr. Okumura joined Mr. King on the panel.]

Mr. KING. I think what you are talking about, Congresswoman Fiedler, is a very, very key point. I have some observations based on my 25 years or so with this. You are right, we have a lot of momentum going today that we didn't have before.

International trade, particularly Japan-United States trade, has become a political issue. I am sure you are very aware of that.

Representative FIEDLER. Right.

Mr. KING. A lot of people have jumped on that bandwagon, and a lot of them well intended. Some not too well informed. So I believe what we have is—and this is, of course, present company excepted.

Representative FIEDLER. Of course.

Mr. KING. So we have a lot of cannon on the battlefield. Some are lose cannon and some are well-aimed cannon. I have found that—I am sure there are others who feel the same way—there is a balance between government-to-government negotiations and industry-to-industry reality.

Frankly speaking—and we are here to be frank—I really believe that if we could rely more on industry-to-industry negotiation and perhaps have less interference from governments on both sides, many times we would make much greater progress. Because then the negotiation is on the basis of economic competitors, global competitors.

Now let me just continue, please. When you get the governments in—and the nature of government, of course, is that they are political mechanisms. But then you have the political mechanism, particularly in agriculture and agribusiness, the economics have sort of gone out the window and they become political issues.

Now, that has its plusses and its minuses. We certainly have some political clout. The Japanese have a lot of political clout. As my colleague from the beef industry says, when you are up that LDP in Japan that's pretty tough stuff.

So, I'm not so sure that on the government-to-government negotiating side, picking up on the political mechanism you are talking about, I am not so sure we come out winners in that.

I feel that maybe our Japanese partners are much more effective in that arena than we are. I think on the industry-to-industry side, we hold our own very, very well.

Representative FIEDLER. I think that if that is the case, then we on our end are not doing a very good job on behalf of the industries that we have a responsibility to represent. I would never point fingers, because I can't evaluate anybody else's performance in this area. That is something for the constituency to evaluate.

But I am curious: Are you saying that there would be any advantage in having trade discussions at several layers as opposed to simply government doing it? Perhaps some kind of a mechanism where industries can do it first and try to work it out at that level? And only bring in the government if you need to go further?

Please, if anybody has something to say, you can all make comments. This is a free-flowing discussion. I am just interested in hearing———

Mr. HUGHES. I have to take exception to what Mr. King said.

Representative FIEDLER. All right.

Mr. HUGHES. About industry-to-industry. Because in our business we are fighting a quota which is not created by the industry, although protective of the Japanese meat industry. The Japanese meat industry loves it. They are a protected group.

There was a book written about the Japanese meat mafia. One of the local reporters said it was a very factual book. In the meantime, there is nothing we can do industry-to-industry in the meat business in Japan.

The industry didn't formulate the quotas. We can live with the duty. Twenty-five percent duty, as high as it is, we can live with it. We can't fight a quota established by a government on an industry-to-industry basis. We need your help. We need the STR's help.

Clayton Yuetter is very, very familiar with the situation. He served on our board of the U.S. Meat Export Federation. We are very grateful he is in the position he's in.

Representative FIEDLER. I am very impressed with him.

Mr. HUGHES. A sharp man and a tough man.

Mr. KING. I would like to add that I think we are all very pleased with him. But I would like to make my position clear. I think we have to define terms.

Representative FIEDLER. You are talking about different kinds of advocacies.

Mr. KING. Well, not only that. We are really on the same track. But when I say politician, I don't mean the U.S. Trade Representative Clayton Yuetter and all those folks that he worked with day after day who I have the highest degree of respect for.

When I talk about the political, I am talking about the legislative area. So please understand that differentiation.

Mr. HUGHES. I'm glad, because we met with the Washington——

Mr. KING. Oh, that's very true. Clayton Yuetter and all those people are good friends of ours. I think that they can work very effectively for us if they have industry support and the kind of support they need from the Congress, and so forth.

But to go back, I have to say that sometimes, too many times, that you might be making progress in beef and, as you say, we all know the problems you have to go through and the patience and all that—but just when you really feel you are making meaningful economic progress or competitive progress then, again, some well-intended legislator comes off the wall and gets in there and really sometimes fouls up the act.

Mr. HUGHES. We were warned in Washington very strongly when a task force of meat associations met with eight Congressmen and six Senators, along with Mr. Brock at the time and Mr. Baldrige and someone from the State Department, and, you know, we were quite incensed that we weren't getting support.

We were warned of the same thing. And they said, all you have to do is get one Congressman to introduce a bill that is protective, and it will be, "Can you top this." Because someone will initiate a bill that is more severe and more severe and we will have a trade war, which none of us want.

But 3 years ago, in the 15 years of exporting, did our industry ever get total support from our Government in the past. The Agriculture Department supported us, the Commerce Department supported us, the State Department dumped dirt on us. For the first time, the State Department supported our efforts, the first time in the history of 15 years of exporting.

It was a welcome thing to behold, to be part of. It's great when State and Commerce and Agriculture and the STR's office are all pointed in the same direction. We were very grateful for it.

Representative FIEDLER. What you really need is informed advocacy.

Mr. KING. That's right.

Mr. HUGHES. Yes.

Representative FIEDLER. That is a very difficult commodity to come by in the Congress. Not because people don't care, but because they are heavily burdened with a broad range of different responsibilities.

I will say this: 60 percent of Congress are attorneys. They have no private sector experience. And because of that, there is a great lack of the fundamental understanding of what business is all about, what it takes to succeed.

I think that is really a problem; I really do. I think that there is an imbalance legislatively. I would urge strongly that those of you who have a serious interest, not only in this issue but in lots of other things, work hard to see that people are elected who are capable of understanding your problems.

It is a problem at every level of the legislative process. Maybe I am biased because I happen to be a business person myself. But I really think that when these issues are discussed, there is a lack of fundamental understanding that has nothing to do with the motivations or political philosophies of the people involved.

I think that it is a real loss.

Mr. OKUMURA. May I cite an example? To be competitive with the Japanese, I think we should follow some of the steps of more cooperating effort between the Government sector and the private sector. We know the Japanese do this extensively.

Coming back to my statement on the sun-roof issue, our Embassy—we reported our effort to the Embassy and they couldn't believe that we had accomplished removing that voluntary barrier in 2 weeks' time. That they had been working on it for 2 years, without any success.

I think it's no fault of anyone, simply a lack of this cooperation, informed cooperation between the private sector and——

Representative FIEDLER. But you are also describing a very skilled political effort.

Mr. OKUMURA. Yes.

Representative FIEDLER. But it is such an individual thing. It is the same kind of thing that represents the difference between a very skilled manager versus one who is not so skilled.

I had a question I would like to address specifically to you, if I can.

I would like to know, to what degree you think the savings incentives affect consumer spending in Japan? Because from my limited experience there as a guest of the LDP and Nakasone, and the fact that there is a continuing increase in the savings percentage of GNP there, I am wondering to what degree there is any disincentive—I guess is the right word—to expanding consumer spending?

At the same time, it seems to me that with a high level of savings, there has to be some pent-up consumer spending potential.

Could you reflect on that?

Mr. OKUMURA. Yes, having lived there. First of all, I don't think they are saving as much as they used to in the sixties when there was a big strive to save. I also feel that we should understand that twice a year annual bonus system. The bonus is equivalent to as high as 6- to 8-month equivalent, which means they keep your monthly salary to a minimum level where it sustains your daily and monthly expenditures. And you cannot save from that.

Then twice a year, once in the summer and once in the winter, means that twice a year a big gift-giving spree. Everyone starts—this goes beyond our Christmas gifts. And to give you an idea of the scope of this gift, the department stores that usually employ 3,000, they double that with part-time employees in these peak seasons.

This takes care of your balloon payments, installments, and other——

Representative FIEDLER. You are saying there are bonuses that are given two times a year to employees?

Mr. OKUMURA. Yes. It also has other effects. First, it keeps your wages to a minimum. During recession when the company is going through a rough time, it enables the company to forgo the bonus temporarily, and resume it again when times are better.

Representative FIEDLER. It is something like profit sharing, is what you are saying?

Mr. OKUMURA. In a sense, yes. It is not called profit sharing. It is actually part of the salary.

Representative FIEDLER. Is everybody given this?

Mr. OKUMURA. Yes.

Representative FIEDLER. Everyone? So it is not an earned bonus?

Mr. OKUMURA. No, it's tied into some merit system. But overall profit——

Representative FIEDLER. How does that affect the savings?

Mr. OKUMURA. Twice a year, the family agrees that they will set so much aside for savings, so much for spending, so much for college education, and so on. So they can plan better. It's like a forced savings effort.

Mr. HUGHES. Currently, the Prime Minister is trying to get the banking industry to reduce the savings interest in Japan in order to encourage more consumer spending. That's in current discussion right now and there is some pressure being put in that direction to encourage the Japanese consumer to spend more money by reducing the savings interest.

Representative FIEDLER. What is it right now?

Mr. HUGHES. I think 5 percent.

Mr. KING. It was two digits. But I think it just went under two digits, like maybe 9.

Mr. OKUMURA. I think it did.

Mr. HUGHES. The interest on a savings account?

Mr. KING. No, the percentage of the savings of the Japanese consumer. It used to be up around 16 percent. I believe it's——

Mr. HUGHES. It's declining. The interest being paid is below 5 percent.

Representative FIEDLER. That savings then goes into the pool of funds available for borrowing for the businesses?

Mr. KING. It's a lot.

Mr. OKUMURA. Yes; it's a lot.

Mr. KING. That is another competitive factor the Japanese have. They do have this tremendous pool of financial resources brought about by this savings incentive. It is very interesting. As you pointed out, the Japanese have for years and years had an incentive for saving.

In our system, we have an incentive for indebtedness.

Mr. HUGHES. Right.

Mr. KING. This tremendous pool of low-interest capital available to Japanese firms.

Mr. OKUMURA. The Japanese postal system is quite familiar, makes it very easy. The corner post office has a savings program.

Representative FIEDLER. Explain that.

Mr. HUGHES. It's like a savings bank——

Mr. OKUMURA. We used to have this in the early days of our history, with competitive interest.

Representative FIEDLER. I wonder where we would be if we did that here?

Mr. HUGHES. We'd save nothing. We couldn't stand in line.

Mr. KING. We would compete with the lottery.

Mr. OKUMURA. Credit cards are also trying to catch up with us in the plastic business—in the credit card business. That is becoming more and more popular. Of course, they don't have their checking system yet.

Mr. KING. Could I get back——

Mr. HUGHES. Consumer financing. They are starting to have typical loan companies, like Household Finance and so forth, on side streets. It's still an embarrassment to go in and interest rates are still high, double or triple what ours are here on private consumer financing. From the loan shark, they would be nearly 100 percent.

Ours I think are in the twenties, aren't they, with consumer financing through Bank Americard? Even the authorized ones in Japan are up in the thirties. So there you have deals for very low savings and very high interest on borrowing.

As that gap narrows, it will increase the consumer spending.

Representative FIEDLER. I would like to ask one other question, if I may. I know this may sound strange, but I am just curious because of its impact on the food market.

To what degree do the Japanese entertain, compared to Americans? Do they have large parties? Explain just a little about it.

Ms. ABBOTT. The use of our products, oranges, at least for the most part still is for gift giving. I think that is an area that would be worthwhile to discuss. Oranges for the most part, imported oranges, are used as gift-giving items.

The Japanese people do that to a large extent. They give delicacies, they wrap them up and they exchange these food items as gifts.

Mr. KING. The Japanese—as all of us experts know here—but the Japanese method of entertaining of course is far different from ours. Because the Japanese entertainment is mostly outside of the home, for very practical reasons.

The homes aren't large enough to entertain in.

Mr. HUGHES. Or you might be an hour and a half away.

Mr. KING. Right. So the entertainment, if you look at it from a market point of view, that is an institutional market for commodities.

Representative FIEDLER. What I am trying to find out is how frequently. Is it something the family might do once a month? Or would they do it twice a year?

Mr. OKUMURA. You have to have a strong kidney to survive.

Mr. KING. You have two types. You have business entertainment that goes on every day, every night. Family entertainment is very minimal.

Mr. OKUMURA. Though very recently we have had fast food and family restaurants. Some of the American institutions are very successful in Japan. Family outgoing weekends, catching on rapidly.

Representative FIEDLER. So more people are going out to eat? I am trying to get a sense of comparison.

Mr. OKUMURA. That is a change—was No. 16 or No. 14, I think it's climbing in the ranks of food institutions, McDonald's being at the top.

Mr. KING. But you're going to sell—of course, I guess it's the same thing. As far as our commodities are concerned, you have to look at Japan, at least in my opinion, as niche markets.

There is an institutional market, there's a consumer market, there is a boutique-gift market, there are various niches in that market. As regards to wine, for example, there's all kinds of markets. There's a high-end market, there's a mass market, there's a youth market, there's an elderly market.

So you have to really look at it, I think, in that respect. Find the niches and try to penetrate those niches and dominate those niches. You know, we are never going to—if you go back to wine, we are never going to out compete the French in the high-end wine business in Japan.

But there is no reason why we can't dominate just below that in the mass markets, the pop wines and things like that. So you have to find your niches and dominate them, I think.

Mr. OKUMURA. I had one question regarding Australian beef. I feel our efforts to promote beef and the efforts of the Government are helping the Australians.

Mr. HUGHES. Well, the Australians have a different system. They have a marketing system, the Australian Meat Board, and they have a staff in Japan. They advertise on Japanese radio.

Mr. OKUMURA. That's right.

Mr. HUGHES. They don't have one thing we have, and that's a large volume of high-quality beef. They do have some high-quality beef—when they determined what high-quality beef was, so many days of feed of a certain grain ration. But we are the only ones that can afford to feed grain to animals in the quantity that we do.

So the Australians have a very small part of what's considered the high-quality beef quota in Japan. For the cheaper meat, we can't compete with them anyway. We are buying it from them right now.

Mr. OKUMURA. So we will never eat Australian shabu-shabi.

Mr. HUGHES. Not knowingly you won't.

Representative FIEDLER. Everybody has to have something to look forward to.

All right, thank you all very much for being with us today. I found this extremely enlightening, and I look forward to seeing the testimony.

If anyone here would like to submit written testimony, or supplement their testimony of today, please feel free to submit it to us as quickly as possible.

I want to thank you very much for being with us. I know that the information that has been given will be shared with my colleagues. I will try to help them become better informed about the successes that you have achieved.

I am very proud of what we are doing in our State. I must admit my own bias, but I think we have some of the most talented people in the entire world here.

If we can succeed in these areas under some most difficult circumstances, I am certain that as the conditions improve, you are going to see worldwide markets for many of these products expand in a way that we can't even imagine right now. It will be due to your efforts.

I thank you all very much for being with us.

[Whereupon, at 5:15 p.m., the subcommittee adjourned, subject to the call of the Chair.]

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