Spawn-on-kelp Market Study

Part One

Market analysis and Expansion Potential

Edwin Blewett & Associates Inc

November 2001
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Introduction
Fisheries and Oceans Canada, seeking objective, factual information on the spawn-on-kelp industry, has commissioned two studies.

- Part One assesses spawn-on-kelp markets, with particular emphasis on market expansion opportunities.
- Part Two provides information contributing to an understanding of the BC spawn-on-kelp industry’s potential for expansion, and impacts of varying supply scenarios on markets and on existing spawn-on-kelp participants.

Edwin Blewett and Associates Inc, in association with Nelson Bros Fisheries Ltd, has been contracted to furnish both reports.

This Part One report provides insight into past, current, and most importantly, emerging markets for BC spawn-on-kelp production.

Methodology
The short time frame for this study, coupled with the desire of Fisheries and Oceans Canada to maintain the highest possible level of objectivity, led to the decision to enlist additional marketing expertise to complete Part One.

To obtain broad market information under an abbreviated timetable, we enlisted the following sub-contractors to conduct research, probe industry contacts, apply their specialized knowledge, and report their findings.

- Michael Renwick, Renwick & Associates.
- Christina Burridge, Seabridge Strategies Ltd.
- Michael Hopper, Trans Oceanic Seafoods Inc.

Despite applying a team approach to this study, the findings of the consultants were remarkably consistent. We offer this report as a synthesis of the market work conducted by sub-contractors and ourselves as an effort to encapsulate prevailing and expected market conditions, and market expansion opportunities, for Spawn-on-Kelp.

In compiling market information, we and the sub-contractors reviewed market literature and spoke extensively with BC processors, Japanese trading companies, re-processors, and relevant seafood players, as well as observers and participants in fisheries in Asian, European, and North American markets.

1 This report draws particularly heavily on the Seabridge Strategies report, which enunciated nicely a range of market feedback.
Existing Spawn-on-Kelp Markets

Market Demand - Overview

Spawn-on-kelp (kazunoko kombu) is a specialty seafood product composed of kelp covered with herring eggs, produced primarily on the Pacific Coast of North America. Spawn-on-kelp is sold into Japanese markets with a very small percentage (<2%) being consumed in Japanese restaurants in North America. Most, if not all of the product consumed in North America is of lower quality or "off grades" in contrast to product exported to Japan.

We could find no existing markets for spawn-on-kelp outside of Japan and North America. Small quantities of value-added product may be exported from Japan to other Asian or North American markets. In discussing the product with European seafood importers, we found no interest in the product whatsoever. The product seems to fall into a cultural/ethnic niche for seafood products (e.g., dogfish belly flaps which are only consumed in Germany).

The Japanese are the world’s largest per capita consumers of seafood. Spawn-on-kelp, however, is a relative newcomer to the Japanese seafood market, having been on the market only for the past fifty years or so. In contrast, Japan has 400 years of history consuming salted herring roe.

Spawn-on-kelp is considered a luxury food item. To date it is primarily consumed in high-end restaurants or sold in the extensive Japanese gift market. Some spawn-on-kelp is also absorbed into the food service (catering) market and used in home cooking (i.e., sold through supermarkets).

Table 1: Japanese Markets for Spawn-on-Kelp

<table>
<thead>
<tr>
<th>Segment</th>
<th>Quality</th>
<th>Share</th>
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<tr>
<td>Restaurants</td>
<td>Jumbo, #1</td>
<td>50-6</td>
</tr>
<tr>
<td>Gift Market</td>
<td>Higher End</td>
<td>15-2</td>
</tr>
<tr>
<td>Sushi Bars</td>
<td>Mixed</td>
<td>5-10</td>
</tr>
<tr>
<td>Food Service</td>
<td>Medium</td>
<td>5-10</td>
</tr>
<tr>
<td>Home Cooking</td>
<td>Low, off grade</td>
<td>5-10</td>
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Table 1 identifies Japanese market segments for spawn-on-kelp, along with our estimates of quality utilization and market share by

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2 Ballpark estimates, based on weighing information from various sources.

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Segment. Segments are listed roughly in descending order by the quality of spawn-on-kelp demanded. The restaurant trade is the primary user of jumbo and #1 grade spawn-on-kelp. A mixture of grades may appear in the Japanese gift market and food service market. Lower quality, off-grade spawn-on-kelp is consumed in Japanese homes.

As a rare delicacy, spawn-on-kelp's traditional niche has been Japanese restaurants and high-end sushi shops where it was able to command high prices.

The Japanese have a tradition of gift giving in which spawn-on-kelp has played a part as a highly valued, high priced “prestige” product suitable for giving as a gift in Japanese society. The gift market has helped support high prices for spawn-on-kelp in the past.

Consumption of spawn-on-kelp in Japan is concentrated in the Kanto region in and around Tokyo. Japanese demand for spawn-on-kelp is highly regional, reflecting both limited distribution for the product, and highly fragmented consumer preferences (particularly for roe products) throughout the country.

The spawn-on-kelp and herring roe markets are quite distinct. Spawn-on-kelp and herring roe are not considered substitute products. Spawn-on-kelp is not as well established in the Japanese market as herring roe. Neither does it have the historical/traditional/spiritual connection that herring roe enjoys. However, spawn-on-kelp has product attributes making it attractive to Japanese consumers.

Supply

Herring spawn-on-kelp is produced primarily in Canada and Alaska (with some minor production from the San Francisco area). In recent years, other countries such as Russia, Finland and Norway have contributed minor amounts to global supply of herring spawn-on-kelp.

Spawn-on-kelp is produced by two methods: open pond and closed pond. Open pond methods generally produce a thinner egg layer, while closed ponds produce a thicker layer that corresponds to top quality. Spawn-on-kelp produced by both methods yields a wide range of grades that are sold in “raw” form primarily to re-processors in Japan.

BC spawn-on-kelp is exclusively a commodity export. Raw product is trimmed, salted or brined on the grounds, then graded and packed into 32-37 lb plastic pails by a BC custom processors for export to Japan or domestic sales. There is little if any additional processing in BC. Intermittent attempts at adding value on the BC side have proven unsuccessful and were abandoned as being too risky.
Thus, the bulk of processing is done in Japan. Pails of spawn-on-kelp are purchased by Japanese re-processing companies, either directly, or via importing/trading companies. Most spawn-on-kelp is handled by two or three re-processors who slice and pack the product for seasonal and year-round distribution. The largest, Taniya, accounts for perhaps 75 per cent of BC production and re-processes some portion of its imports in China. Other significant re-processors include: Marugen, Chugai and Koei.

The distribution system in Japan, from raw material purchase (BC spawn-on-kelp), to trading company to re-processor, to wholesalers and major channel players is both lengthy and costly, and has not been simplified for this product.

The supply of spawn-on-kelp is relatively small compared to other seafood imports and food products in Japan. Low volume results in a reluctance by channel players below and including the re-processors to spend much time and/or marketing funds on channel expansion, regional distribution expansion or internal promotion. Under current economic conditions, this difficulty is aggravated by the positioning of spawn-on-kelp (BC’s in particular) as a high priced/luxury product.

Spawn-on-kelp is not differentiated in the Japanese marketplace by country of origin. Japanese marketers have created their own brand recognition for spawn-on-kelp that has helped them to obtain high prices. Brands are extensively used by re-processors, importers, food distributors and retailers in Japan to build awareness and consumer preference.

**Market Dimensions**

**Table 2: Japanese Imports of Herring Roe on Kelp (tonnes)**

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<td>521</td>
<td>512</td>
<td>710</td>
<td>800</td>
<td>631</td>
<td>869</td>
<td>586</td>
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</table>

Japanese imports of spawn-on-kelp over the last half decade are summarised in Table 2. Total Japanese imports and prices paid to Canadian producers in yen terms are illustrated in Figure 1.
Since 1994, Japanese imports from all sources have ranged from 500 tonnes to 870 tonnes. Recent years (1998 – 2000) show a confusing trend although imports from Canada have been relatively stable; it is imports from the USA and other (minor) suppliers that have caused the volatility in total imports at the end of the decade.

Canadian spawn-on-kelp accounts for 54 to 81 per cent of total Japanese imports since 1994. Taking an average of Japanese imports of spawn-on-kelp from Canada and other (non-USA) countries over the past four years, and an indicative supply from the USA (250 tonnes), we can summarise the make up of Japanese imports of spawn-on-kelp as 61 per cent Canadian, 31 per cent American and 8 per cent from other sources.

Prices paid to Canadian and US producers over the last half decade are illustrated in Figure 2. Prices paid to Canadian spawn-on-kelp producers have dropped from lofty heights in the mid-1990s to around 2,000 yen/kg by the end of the decade. Prices paid to US producers have hovered around the 2,000 yen/kg mark during the past half decade. The erosion of prices paid to Canadian producers has brought them more into line with those paid to American producers.

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3 Japanese imports of spawn-on-kelp from the USA were abnormally low in 1998 and 2000. To summarise the make up of Japanese imports of spawn-on-kelp, we have chosen 250 tonnes as a figure indicative of spawn-on-kelp imports to Japan from the USA.
The combined effect of variable supplies and falling prices has resulted in an overall decline in the value of spawn-on-kelp imports to Japan in recent years. This is illustrated in Figure 3.

Market Trends
In this section, we investigate market trends and identify opportunities for increasing sales of spawn-on-kelp in various market segments.
Japanese Economic Conditions

Any consideration of trends in the Japanese market for spawn-on-kelp must occur within the context of the recent history of the Japanese economy.

The Japanese economy is very fragile, with prospects for improvement in the near future extremely unlikely. The following litany of observations characterize the bleak state of the Japanese economy:

- Government bond values are sinking.
- The national insurance industry is in chaos.
- Banks are on the verge of financial collapse.
- Unemployment is at record levels.
- The Nikkei average has dropped almost 2/3rds.
- Auto production is down.
- Land prices are down.
- Business confidence continues to decline.
- The new mega-banks are as unwilling as the old banks to deal with bad loans.

The Japanese Chain Store Association and the Japanese Department Store Association continue to report declines in sales. In 2000, expenditures on food declined by 1.9 per cent, the first real decline in a decade. The precariousness of the retail sector is illustrated by the filing for bankruptcy protection in September 2001 of Japanese grocery giant Mycal Corp.

Given widespread economic malaise, recovery of the Japanese economy will take considerable time.

The impact of recession on the seafood business has been substantial. Across the board, the wholesale price of high-end products has dropped dramatically. Imports of “international” products (crab, shrimp, some salmon) have dropped as a result of competitive demand. Wholesale prices of virtually all expensive items (lobster, shrimp, salmon, crab, herring roe, abalone, sea urchin roe) have dropped by at least 40 per cent and often as much as 75 per cent since 1997.

Exacerbating lower price levels is restricted access to credit by Japanese seafood companies following consolidation in the banking sector and the demise of institutions such as the Hokkaido Taku-shoku Bank. Soft markets and limited access to credit contribute to a diminished tolerance for risk among seafood players. As the Japanese seafood sector’s appetite for risk declines, suppliers are obliged to assume a greater proportion of the business risk associated with distribution of finished product. Often, “risk sharing” means accepting a lower price for suppliers of raw material.
Spawn-on kelp is a relatively new product for the Japanese consumer and is considered a high-end or luxury food item. Because of the deep recession affecting the Japanese economy during the last few years, consumers have tended to forgo such luxury food items, causing a decline in demand and price.

**Japanese Consumption Pattern Shifts**

Compounding the impacts of a weak economy on Japanese seafood markets are shifting consumer preferences. The following observations, indicative of fundamental shifts in consumption patterns, are provided.

- Older Japanese—whose taste shaped the development of the spawn-on-kelp market—are deferring expenditures, and saving heretofore disposable income.
- A growing proportion of disposable income is in the hands of the young who prefer to spend it on faster food, cheaper food, more international food; in short, on eating out as inexpensive entertainment.
- Concerns about health are growing and many traditional products—especially the time-consuming, heavily salted ones—are declining in prominence.

Consumption of beef, pork and poultry have increased dramatically in Japan during the past 10 years consistent with the changes in demographic makeup and an appetite for western foods. From 1990-1997, meat consumption increased 13 per cent per annum while seafood consumption increased only 3 per cent per annum. The recent “mad cow disease” scare in Europe has spread to Japan. The short-term impact is a dramatic decline in beef consumption but to date, no associated increase is seafood consumption has been noted.

While a weak economy, coupled with shifting consumption patterns, present formidable challenges to the Japanese seafood sector, change invariably brings opportunity. Regardless of the state of the economy, people must eat. As consumption patterns change, new prospects will replace those in decline. Japanese consumers still expect quality, they just want it at a reasonable price. Products deemed to provide good value offer the best potential under shifting market conditions.

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4 As one supermarket buyer put it: “everyone talks about price destruction but this doesn’t mean that Japanese consumers will accept poor quality products just because they’re cheap. It didn’t work for Daiei and it won’t work for any other supermarket chain. We want good quality at a reasonable price and if Canadian suppliers can give me this I am happy to buy from them.”
The High-End Restaurant Market

The restaurant market for high quality (and high priced) spawn-on-kelp has shrunk considerably as a result of economic decline in Japan. Other seafood items traditionally commanding premium prices in this segment such as sashimi tuna, abalone and sea urchin roe have been similarly affected. Before the economic meltdown, the high-end restaurant trade was primarily supported by expense account and business entertainment dining out.

In the current economic climate, there is no prospect of a recovery in the foreseeable future in this kind of generous expense account business.

On visits to Japan, for example, North American exporters were accustomed to being lavishly entertained; they now find themselves in inexpensive sushi bars going “Dutch” (or watching television in their hotel rooms) instead. This impact is not of course limited to spawn-on-kelp.

The Gift Market

The gift market was an early casualty of the economic decline. Gift giving in Japan falls into two categories: corporate and personal. Both are concentrated at the end of the year and during the summer Obon/Golden Week period. Spawn-on-kelp, like top quality salted herring roe, has been a staple of gift packages. This market has shrunk dramatically since 1995.

Lavish corporate gift giving is largely a thing of the past both as a cost cutting measure and because of a change in mores. Corporate gift giving was closely associated with the construction industry—a sector noted both for corruption and as including a large number of “deadbeat” companies on the verge of bankruptcy—and the powerful bureaucracies of MITI and MOF (trade and finance). Public opinion has turned sharply against overt dealing in favours and the gift business has felt the effect.

Personal gift giving has changed in a different way. It is still a common, even a growing custom, particularly in the summer but overall expenditures have declined and the range of possible gifts has expanded—spawn-on-kelp is no longer an obvious or necessary choice.

Demographic trends are also at play in the decline in the gift market for spawn-on-kelp. The (previous) importance of spawn-on-kelp in the gift market is largely attributable to older Japanese. The Japanese trade has been concerned for at least the last 15 years that the aging of the population segment most interested in spawn-on-
kelp would have significant impacts on demand, market volumes, and especially prices.5

Changing demographics and interest in spawn-on-kelp being primarily among the older generation has affected corporate and personal gift giving trends. On the corporate side, as decisions about gift-giving fall to younger managers, spawn-on-kelp and herring roe are no longer automatic choices. On the personal side, growth in gifting is coming from younger people who are less likely to choose traditional spawn-on-kelp.

From indications received, we estimate that the importance of spawn-on-kelp in the Japanese gift market is today about one-half of what it was as recently as five years ago. The traditional gift market thus offers little prospect of a recovery in either volume or value.

 Ordinary Sushi Shops, Fast Food and Take-out, and Kaiten Sushi Shops

Ordinary sushi shops are less expensive than high-end ones that have traditionally been the market for spawn-on-kelp. The curtailment of spending by consumers has hit this level hard too, and the consumption of high-priced seafood products (eg, spawn-on-kelp, sea urchin roe, sashimi tuna, abalone) in such establishments is not expected to recover in the near future either.

The main segment of the market where sales appear to have increased over the last five or six years is fast food and take-out. The advent of McDonalds nearly 20 years ago has had a profound influence on the development of this segment of the market, creating the impetus for new chains offering fast, quick foods from different origins, making eating easier, faster and cheaper.

Often this involves taking elements of traditional Japanese cuisine and redeveloping them into fast food items using much cheaper, imported raw materials—the beef bowls at Yoshinoya are a prime example.

Sushi restaurants have not been immune to the trend towards convenience and low cost. Kaiten sushi bars (where diners choose from revolving, made in advance sushi plates) and take-out sushi, both of which do away with the need for highly trained chefs and increase potential volume, have grown significantly. A couple of pieces of spawn-on-kelp sushi in one of these establishments is re-

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5 Stories abound of even top-grade roe gift packages from Ihara Suisan (the market leader) being simply dumped into the garbage because the younger generation does not know how to desalt the product or cannot be bothered to go through the time-consuming process. Spawn-on-kelp is no exception to this trend as it is not perceived as a ready-to-eat product.
ported to cost a mere fraction of the price charged by an ordinary or high-end sushi shop.

For the last few years, the fast food/take out/kaiten sector has been characterized by cost cutting as a primary strategy for achieving market penetration. JETRO’s most recent study of the dining-out market indicates, however, that take-out/fast food prices have dropped as low as they can and that success in this segment depends now on service, quality, better systems, and product differentiation.

This growth in take-out/kaiten shops and the current degree of price stabilization suggest opportunities for spawn-on-kelp, particularly for lower-priced product that may derive from lower quality grades. Lack of consumer familiarity with spawn-on-kelp products in these types of outlets is an obstacle that must be surmounted if these growing segments are to be penetrated.

Reportedly, the traditional Japanese seafood distribution structure—implying a lengthy chain—is still very much in evidence even in newer segments of the market.

**Home Cooking**

Some market participants believe that the future of spawn-on-kelp, especially if production increases, lies in home-use and the development of retail markets. One important trend in this regard is the desire for fast, convenient products. The breakfast market has been identified by at least one marketing firm as an opportunity, with growth in ready-to-eat or pre-cooked items that only need to be dipped in boiling water, cited.

While spawn-on-kelp has always been available in retail shops, it has only recently been identified as a market opportunity. Lack of development to date is likely due to lack of familiarity with the product throughout Japan and limited supply which imposes distribution constraints.

**Bento Boxes**

Bento boxes are compartmentalized lunch boxes of prepared rice, vegetables and small portions of meat or fish. Bento boxes are a fast food staple in Japan at restaurants, department stores, train stations, and take-out shops, with the market estimated at 6-8 million boxes a day.

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6 According to one expert on the Japanese food market, there could be as many as eight or ten middlemen between seafood importer and a take-out sushi manufacturer in Gunma (a 2 million people market to the northwest of Tokyo).
Many of the trends observable in the takeout/kaiten market—particularly the decline in prices—also affect the bento box segment of the market.

Heightened competition, while keeping a lid on prices, is also spurring competition in new product development—the range of acceptable products for bento is growing—and in new technology—microwaveable bentos or shelf-stable bentos. Related opportunities also exist in the B & B (ryokan) and school lunch markets.

Calgary-based Nakodo Consulting, in a recent report, suggests bento box manufacturers as one key avenue for BC seafood producers seeking to take advantage of the growing Japanese market for value-added food products. Nakodo cautions, however, that the market is very competitive, requiring significant new product development and marketing, and needs high volumes of successful products. Its advice is to pick a region, select a niche market, pursue three or four appropriately sized customers, then select one for an 18-36 month development period.

North America

In North America, markets for spawn-on-kelp are limited to cosmopolitan maritime cities: New York, Los Angeles, San Francisco. The market for spawn-on-kelp in these centres is now about one ton in each city. The total US market is currently in the range of three to four tons.

One of the trends in the North American food service business has been the explosive growth in Japanese restaurants at every level from high-priced sushi shops to noodle and gyoza shops. This growth far exceeds growth in the population of Japanese-Canadians and Japanese-Americans. This growth is generally attributed to two factors—a predilection for Japanese food by ethnic Chinese and its enthusiastic acceptance by affluent Caucasians. Unfortunately, neither group of customers is familiar with spawn-on-kelp or immediately drawn to it.

Conversations with Japanese chefs and wholesalers in Vancouver suggest that most spawn-on-kelp product is local (rather than re-exported from Japan) but that opportunities for expansion are limited to non-existent. They do not believe that lowering the price would result in increased consumption or release of pent-up demand.

At current prices, our market research indicates that North American markets are not likely to grow much if at all. There is currently no “pent up” demand and consumers do not value high grade spawn-on-kelp (much) above that of lower grade product. Expanding North American markets for spawn-on-kelp would therefore be a daunting task and the rewards would likely be lim-
ited given its small size. Market participants estimate that doubling its size would involve a major decline in prices.

Summary of Market Trends

Our review of market trends influencing spawn-on-kelp markets can be summarised as follows.

- Weak general economic conditions in Japan create a daunting environment for the marketing of a high-end luxury product such as spawn-on-kelp.
- A higher percentage of disposable income in the hands of young consumers with a lower predilection to purchase spawn-on-kelp; increased emphasis on nutrition and health; and relative stagnancy of seafood consumption relative to meat; present challenges for marketing spawn-on-kelp.
- Traditional niches for high quality spawn-on-kelp—including high-end restaurants, the gift market, and sushi shops—appear to have shrunk as a result of the poor economy and shifting demographics, with prospects for a rebound deemed poor.
- The growth opportunities for seafood in general, and spawn-on-kelp in particular, are likely in growing market segments for lower cost/high perceived value products: fast food, kaiten sushi shops, home cooking, and bento boxes.
- There is no apparent surge in spawn-on-kelp interest in the North American market, where quantities consumed are now extremely slight.

New Consumers

In this section we investigate opportunities for creating new consumers in existing markets, and in regions not currently consuming spawn-on-kelp.

Regional Expansion in Japan

The primary market for spawn-on-kelp is Kanto (Tokyo region) if only because of the concentrated population and the ease of distribution. Some in the trade take the view that the Kansai (Osaka/Kobe/Kyoto) is potentially attractive because seafood consumers there are more discriminating, willing to pay higher prices, and attuned to the tastes of older Japanese.

In fact, the tiny size of spawn-on-kelp supply and the spawn-on-kelp market mean that it is an unfamiliar product to most Japanese even in metropolitan Tokyo. Market expansion is therefore akin to the introduction of a completely new product. At anything other than a commodity level this is going to take a market development
strategy backed by considerable expenditure. The largest purchaser, Taniya, already estimates its marketing expenses in the Cdn$1 million range—an amount that may sound a lot but is in fact not very much given the cost of marketing activity in Japan.

Regions outside Kanto and Kansai also offer opportunities for new market development for food manufacturers. Kyushu, for instance, has a tightly concentrated population of 15 million (5 million in the Fukuoka area alone) and a handful of regional supermarket chains.

Korea

Korea has a particularly strong Japanese restaurant sector, especially in Seoul. During the buoyant economic times, it expanded dramatically, building on both the desire for conspicuous consumption and a thriving expense account trade with both Japanese and Korean business. Prices were generally reckoned to be at least one-third higher than at equivalent Korean restaurants.

Even so, it does not appear that spawn-on-kelp was a familiar product in these restaurants. There is little evidence to show that it was imported directly although anecdotal evidence suggests that small quantities were available through Japanese importers. Staff at the Canadian Embassy in Korea checked with a number of high-end Japanese restaurants and found that the chefs were unfamiliar with spawn-on-kelp. Embassy staff do not believe that spawn-on-kelp has penetrated the Korean restaurant segment.

Korea has a vibrant seafood trade for both food service and home consumption, but high-end products have been especially hard hit, perhaps more so even than in Japan. As recently as June 2001, Seoul-based Korean importers were expressing interest in availability and pricing of a number of different BC seafood products (though not spawn-on-kelp). In every case, they were looking for prices at least 20% below current levels (even for sockeye salmon which this year hit new lows in landed and wholesale values). Developing a market for spawn-on-kelp would require introducing a new product to a market that is unfamiliar with it. This would require low prices and considerable marketing support. Spawn-on-kelp suppliers in BC do not appear to be in a position to do this.

One North American seafood exporter, who is a major player in the South Korean market, found a number of Korean importers who were familiar with the product and who expressed interest in it for the food service and restaurant trade. Price would be the key to entering the Korean market. Korean Importers felt a reduction of at least 20% in price would be necessary to penetrate this new market. It is unclear what level of consumption could be attained in the Korean market. Korean importers expressed considerable doubt that spawn-on-kelp could expand beyond a niche product without considerable promotion. They also felt that lower-grade and lower-priced product would dominate the market place.
Europe

European seafood importers, even those trading in European/Asian consumer markets, expressed little or no interest in the product. The product is simply too expensive, even at current market prices. Unlike many other sushi dishes, spawn-on-kelp appears to be in demand only with consumers familiar with the product, and is therefore considered unlikely to gain a wide following with people other than the Japanese.

The market for spawn-on-kelp in Europe is virtually non-existent. One of our market researchers has eaten at a number of sushi restaurants in Paris, for example, yet never seen spawn-on-kelp on the menu or been able to obtain it if asked for. Our market experts consider the European market to be a non-starter at this point.

New Consumers—Summary

With consumption of spawn-on-kelp currently centred almost exclusively in the Tokyo region of Japan, three potential areas for stimulating new consumption were explored: other regions in Japan, Korea, and Europe. Findings are summarised below.

- Other regions in Japan—highly populated pockets of sophisticated seafood consumers are situated throughout Japan; Kansai and Kyushu, for example represent substantial untapped potential. However, penetration into these markets is akin to a new product launch, implying substantial market development expenditures.

- Korea—while a large Japanese restaurant sector offers potential for introduction of spawn-on-kelp, it is likely that such introduction would require both market development investments, and a substantial reduction in pricing vs levels supported in current Japanese markets.

- Europe—little potential for stimulating spawn-on-kelp consumption where none currently exists was uncovered.

Market Expansion Considerations

Understanding the Japanese Distribution System

An oft-repeated criticism of Canadian seafood exporters by the Japanese trade is that Canadians don’t spend the time understanding the Japanese market and figuring out how to adapt to change.

While some Canadians interpret this as a coded criticism of their reluctance simply to lower prices, it’s hard to see how a better un-
derstanding of how the market works can be a disadvantage. It comes down to marketing a product rather than just selling it.

Spawn-on-kelp producers interested in the partnership/vertical co-operation model need to build individual and collective relationships over time with existing Japanese re-processors and potential new ones. Vertical co-ordination or value-chain development really means that each person/company who touches the product sells more of it as a result of personal connections, product knowledge and buyer-seller familiarity.

The early stages of this process should involve exploring how other food exporters have dealt with similar challenges. Spawn-on-kelp producers have the opportunity to play a more effective role in the changing spawn-on-kelp market than they have before. When pre-made, frozen bento boxes from California (using foreign rice, no less) can sell competitively in Japan, then the market is wide-open to new ideas and new ways of doing business.

Quality

Quality is a marketing issue that BC suppliers must face. In Japan, quality is an ambiguous concept. Japanese buyers are the most knowledgeable in the world. They take seriously their job of defining quality and guaranteeing it down the line to the end consumer. Concerns about quality are often used as market codes, however: a reason to pay less for a particular product when market circumstances have changed.

With spawn-on-kelp, the concept is even more confused. For instance, “thick” kelp from closed ponds is generally considered to be top quality whereas thinner kelp, often but not necessarily from open ponds, is lower quality. As markets change, however, quality (in the traditional sense) and demand do not necessarily coincide.

If opportunities for spawn-on-kelp lie in developing everyday uses and consumers at lower prices, then the perceived quality of BC spawn-on-kelp can be an advantage, displacing cheaper product from elsewhere. A parallel exists with herring roe where the better quality, crunchier Pacific roe has to some degree displaced cheaper Atlantic roe in the everyday ajitsuke (flavoured roe) market.

The need for uniform, effective grade standards is one of the common themes in the Japanese spawn-on-kelp trade. Most importers currently re-grade their purchases. BC spawn-on-kelp producers have a chance to solidify their market position in compari-

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8 As one Japanese importer put it, talking of Canadian seafood exporters in general, “if you want to go on selling to us, you have to reduce your costs, improve quality and “freshness,” work with us to develop new products and figure out the stories that will sell consumers on those products.”
son to their competitors by moving quickly to work with Japanese importers to implement grade standards.

The quality issue is raised in virtually every analysis performed on the spawn-on-kelp market.

**Branding**

Spawn-on-kelp is an export commodity: there is no distinction between product by country of origin (or any other identifying attribute for that matter). In Japan, spawn-on-kelp has been relatively undifferentiated although the market ascendancy of Taniya is changing that.

A recent spawn-on-kelp market report identified opportunities for branding BC spawn-on-kelp. BC product does have product attributes that, if combined with a grade standards program, could lend themselves to branding. Together, a branding program for the trade would be relatively inexpensive and could improve the position of BC product within the Japanese market.

The success of any branding program will depend on the degree of cooperation afforded by existing Japanese partners and on the ability to access new buyers and distribution channels. With the exception of sockeye salmon, Canadian seafood products are not generally identified by country of origin, whether they are low end (Atlantic herring roe and capelin) or high-end (Gulf snow crab). Atlantic and Pacific herring roe are generally sold as product of Hokkaido. The main Japanese re-processors may be unwilling to extend a BC origin brand beyond the trade, seeing it as jeopardizing their ability to source from different countries and their own brand identity. On the other hand, Canada has an excellent image as a producer of top quality, natural food products and some Japanese re-processors may see an opportunity to capitalize on consumer recognition of this.

Many Japanese re-processors see a role for producers in marketing and promoting spawn-on-kelp. Willingness to contribute to such a process would result in a better dialogue about how to expand markets and set the stage for development of more effective partnership/vertical coordination relationships.

**Analysis of Market Information**

Preceding sections have examined current and potential markets for BC spawn-on-kelp from a variety of perspectives. A host of observations and opinions from industry participants on both sides of the Pacific have been cited. While the focus of this report is to assess

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market expansion opportunities, it is undeniable that much of the intelligence surrounding spawn-on-kelp markets paints a gloomy picture—a picture pointing not to growth opportunities, but to a contracting market and falling prices. While largely negative, the market picture in Japan for BC spawn-on-kelp is by no means “black and white.” Similar information can be used to draw different inferences about the future health of spawn-on-kelp markets, depending upon one’s position and perspective.

We examine three varying interpretations of information presented in this report.

Doom and Gloom

Factors pointing to continued soft, and possibly eroding markets and prices, are summarized as follows:

- The prospects for selling significant quantities of spawn-on-kelp, at prices approaching current levels, to any market other than Japan, appear remote.
- Given continued reliance on the Japanese market, the current state of economic chaos prevailing in Japan presents challenges to any commodity producers exporting to this fragile economy. Spawn-on-kelp producers cannot reasonably expect immunity from a difficult macro-economic environment.
- An estimated 65-80 percent of BC spawn-on-kelp is positioned as a high-priced luxury item in high-end restaurants and the gift trade. These two market segments for spawn-on-kelp have diminished, as business entertainment and gift-giving expenditures have been slashed nation-wide.
- Shifting demographic and consumption trends (younger consumers, less inclined to have developed strong preference for spawn-on-kelp, and eschewing extravagant consumption for value-oriented consumption) exacerbate the decline of the “high-end” market.
- Growth of the seafood market in general in Japan has been marginal in recent years; beef and pork items, meanwhile, have seen explosive growth.
- Because of increasingly volatile commodity markets and reduced access to credit (working capital), seafood companies in Japan are developing increasingly risk averse strategies for dealing with raw material purchases (particularly for high-priced items).
- Many traditional spawn-on-kelp players have exited the business, seemingly unsatisfied by risk/return prospects.
- The seafood market has maintained its stature, or achieved slight growth, in spite of declines in high-end niches, be-
cause of growth of “every day”, value-oriented seafood segments.

- Contraction of the high-end market and growth of the low-end markets are trends that can be expected to continue for the foreseeable future.
- The notion that BC producers may increase production of spawn-on-kelp, for sale into declining market segments, to a rationalizing processing and distribution sector, within a battered economy, while maintaining or increasing prices, is simply unrealistic.

**Mixed Messages**

While the foregoing presents a compelling scenario, Japanese buyers and users of BC spawn-on-kelp nevertheless project numerous mixed messages. While “doom and gloom” discussion abounds, the last 2-3 years in the spawn-on-kelp industry have seen incongruous events.

- Prices received by BC spawn-on-kelp operators, from (Canadian dollar) lows seen in 1998, have firmed slightly in successive years. In 2001, some producers obtained prices substantially higher than they obtained in 2000.
- Although high-end market segments for jumbo and #1 product are seen to be dwindling, the highest prices for BC product are still fetched by operators producing premium quality suitable for high-end markets.
- Efforts by remaining spawn-on-kelp re-processors/distributors to increase market share are seemingly reflective of current or expected profitability.
- Certain players at each link of the distribution chain are desirous of more product, confident that incremental volumes can be “moved” at reasonable prices.

Long before recession struck Japan, the demise of both roe herring and spawn-on-kelp markets because of shifting demographics had been predicted by some. Yet, BC producers inevitably seem to place their product in Japan—sometimes at attractive prices, at other times, not. Commodity markets in Japan have always been subject to speculative highs, followed by “corrective” lows. In the eyes of some, “actions speaks louder than words”, and certain actions of spawn-on-kelp participants are incompatible with the arguments indicating a doom and gloom scenario. Like other seafood commodities in Japan, spawn-on-kelp seems to survive, one year at a time.
A Growth Industry

While high-end product positioning historically provided satisfactory results for the spawn-on-kelp industry, growth in fast food, convenience, and health-conscious segments of the Japanese seafood industry provide long-term opportunities for spawn-on-kelp to achieve sustainable growth.

The view that spawn-on-kelp is positioned to achieve growth in the marketplace is supported by the following points.

- Current spawn-on-kelp volume is miniscule in the scheme of overall seafood consumption in Japan (about 650 tonnes compared to an overall market of 750,000 tonnes), and this volume is now distributed strictly within a single region (Kanto).
- There is ample potential to expose consumers in other Japanese regions to spawn-on-kelp but a current constraint to market expansion is a lack of product.
- For the majority of Japanese consumers, who are unfamiliar with spawn-on-kelp, this product can be shown to perfectly combine the new and convenient with the traditional.
- Retailers in Japan are competing ferociously to provide consumers in the growing fast food/take-out/kaiten sushi shop/bento box segments with products that are tasty, nutritious, healthy, and new. Spawn-on-kelp meets these criteria nicely.
- Spawn-on-kelp offers similar potential in the home cooking segment.
- By offering spawn-on-kelp in small quantities, as a “luxury” component of an otherwise “ordinary” food-item (ie, along with rice), higher values may be supported for spawn-on-kelp, while strong values are offered to consumers.
- When growth of spawn-on-kelp sales volume is viewed in the context of tiny volumes, if positioned to penetrate distinct and growing segments, in a massive overall seafood market, the notion seems entirely reasonable.

Summary & Conclusions

The preceding analysis generates three distinct outlooks on spawn-on-kelp market growth potential, drawing on a common body of market information.

- A negative outlook—that high-end positioning in a weak market and declining segments spell market contraction and price reductions.
• A “year at a time” outlook—that, while negative talk abounds, the spawn-on-kelp industry annually survives, with participants earning the volatile results characteristic of seafood commodity production.

• A positive outlook—that shifting economic and consumption patterns provide ideal opportunities for penetration of spawn-on-kelp into new regions of Japan.

Many spawn-on-kelp industry participants have adopted one of the extreme positions, and that individual interests may influence how market information is interpreted.

Based on the information presented in this report and considering the varying prospects for spawn-on-kelp markets, we have concluded that the market outlook is decidedly gray, not black and white. In our assessment of market development opportunities, we are influenced by the following considerations.

Difficult Economic Environment

Spawn-on-kelp markets cannot help but be impacted by extremely soft economic conditions prevailing in Japan. The effects of a weak economy have filtered down to virtually all industries and market segments in Japan.

Generally, a strategy targeting both increased output of a commodity product into a weak economy, and maintenance or enhancement of price levels, would not be attempted according to common business practice.

Spawn-on-Kelp Exporters Lack Influence

BC spawn-on-kelp producers (individually and collectively) should be aware that they exert very little influence over how their product is distributed to the Japanese marketplace. With few genuine purchasers of BC raw material, and few players re-processing and distributing finished product within a single region of Japan, the BC spawn-on-kelp sector enjoys few options in selling its products.

Vulnerability to business actions of a very few Japanese firms, coupled with weak economic conditions, makes increase of production an inherently risky strategy for BC producers.

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10 We assume that an implicit objective of increasing production is maintenance of current price levels (and eventually, firming of prices); increased production quantities met with a corresponding reduction in price levels would serve little market purpose.
The Product is Good

With business risks of spawn-on-kelp expansion identified, producers of the product may take solace from the fact that the attributes of the product at the consumer level appear to be strong. While traditional high-end markets for spawn-on-kelp are under severe pressure, the product lends itself to positioning in growth segments of the seafood market. The product seems to be regarded as tasty, visually attractive, and nutritious. Certainly, a good product is the underpinning of a sustainable business.

Marketing vs Selling

Translating strong product attributes into increasing sales and stable or firmer pricing, given the challenges identified, will require more than a “produce it, and it will sell” approach. Achieving broader distribution of spawn-on-kelp in Japan is akin to launching a new product (since most consumers have no experience with it). Such an initiative would require substantial marketing support. Marketing measures include: promotion, advertising, product demonstrations, new product development, and the carrying of inventories to support consistent product availability.

In the absence of a marketing program, the only tool for distributors to achieve new market penetration is pricing, and a low-price strategy is likely to frustrate the objectives of expansion.

With marketing campaigns expensive, and the Japanese spawn-on-kelp sector increasingly risk averse, BC producers will no doubt play a role any marketing effort. Quality and branding initiatives already underway are an excellent start.

Tread Cautiously...

From the foregoing analysis, an outlook of both risk and opportunity emerges. While traditional spawn-on-kelp markets, and the lofty prices they supported, are declining, spawn-on-kelp can be positioned in lower-end growth sectors of a fragile Japanese economy.

To the extent that a market-segment transition is taking place, and that the transition brings substantial potential for eventual market growth, a cautious approach to expansion while the transition takes place would appear to be prudent.
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