

## Japanese cake shops are crazy about Hong Kong – Revealing the reasons behind the Japanese cake shop boom

Have you ever noticed the cake shops while walking on the street? If you pay attention, you'll find that the number of local low price traditional cake shops has decreased, while large-chain Japanese cake shops such as A-1 Bakery, Panash, and Chateraise have been opening frequently. So, what's driving this trend? Let's break it down step by step.

As a cake lover, I've made an interesting observation over the past decade. The price of cakes in traditional cake shops has risen from \$5-\$10 to \$10-\$15 per piece. However, chain Japanese cake shops have maintained an average price of \$30-\$40 per piece. From a relative price perspective, it's easy to see why the cake shop market has changed. Traditional cake shops and Japanese cake shops are in competitive demand. When the price at traditional cake shops increases and the price at Japanese cake shops remains steady, the relative price of cakes in Japanese cake shops decreases. This makes buying cakes from Japanese cake shops more attractive for consumers. Consequently, there's an increase in demand for cakes from Japanese chain shops.



(The photo was taken at the cake shops in Shek Kip Mei.)

In response to this growing demand, numerous Japanese cake shop chains have expanded into Hong Kong. These businesses not only benefit from internal economies of scale due to horizontal expansion but also gain advantages from the unique characteristics of the local currency market. When the Japanese yen depreciates in the foreign exchange market, revenues in terms of other currencies earned by companies in Japan depreciate as well. For these Japanese companies, Hong Kong dollars are a special case as the Hong Kong Linked Exchange Rate System ties the Hong Kong dollar to the US dollar. Whenever the US dollar appreciates or depreciates against other currencies, the HK dollar will follow the US dollar to appreciate or depreciate. Under this system, the value of the Hong Kong dollar will be very stable and the profits earned in Hong Kong won't depreciate as

quickly as the Japanese yen. Therefore, the profitability of opening branches in Hong Kong may exceed that of opening branches in Japan.

The primary reason for product price increases is rising costs, and the common price increase in the bakery industry verifies this. Looking back to before the cakes were made, production of raw materials needed for cake, such as flour, eggs, and fruits, is not entirely under control as these materials are always influenced by environmental factors such as climate change, unpredictable weather, and rampant pathogens. For example, bird flu recently broke out in Japan, leading to a significant decrease in egg production on many chicken farms. The price of eggs, one of the main ingredients for making cakes, soared during this period. Therefore, the average production cost of bakery businesses greatly increased. However, large-chain cake shops usually purchase raw materials from different suppliers in large quantities to support their extensive operations. This approach diversifies supply chain risks, making them less affected by raw material supply crises. When costs change less, their prices remain steady. Meanwhile, small shops that purchase raw materials from a single supplier have no choice but to raise prices due to increased costs.

So, what is driving the proliferation of Japanese cake shops across Hong Kong? They've discovered the secret recipe: keeping cake prices steady. Therefore, the next time you enjoy a Japanese cake, remember that it's more than just a dessert — it's also a representation of economic concepts.

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