

Will “Diversity” Save Japanese Companies from Long-Time Stagnation?

By Naoyuki Haraoka



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Introduction

The Japanese economy has been struggling to exit from two decades of stagnation and it has now been recognized that structural reform could provide the solution. Structural reform generally means creating a more accommodative business environment to enhance competition and thereby increase economic efficiency. Deregulation and trade liberalization would be good policies to help achieve this, as they could both lead to the optimal allocation of resources through full utilization of market mechanisms.

But it is not only the government but also businesses that should bear the burden of the work of structural reform. Corporate management should also pursue reform of the existing management system in order to revitalize business firms' competitiveness. Having new corporate governance guidelines to encourage firms to use ROE as an indication of their business performance and more independent directors among their board members to evaluate the company's performance objectively would be useful in achieving this. Increasing the transparency of the management through assessment by objective criteria would also enhance the board members' motivation to boost the company's business performance.

However, this is not the only way to achieve structural reform of business management. Today we expect that more women or foreigners engaging in management decisions or joining the workforce in a company will lead to an improvement in its business performance. This is called “diversity” management. Such diversity will not only complement Japan's workforce, which is declining due to aging and depopulation, but will also be crucial in stimulating the “animal spirit” of capitalism through a wide variety of thoughts and ideas.

It is probably true that for most nations in the world diversity in this sense should already be a reality and not a target to be fulfilled. Even so, it might still be useful for our non-Japanese readers to discover how such diversity could improve a Japanese company's business, assuming that this Japanese adoption of diversity as a new criterion for innovation could lead to the creation of a new post-industrial capitalist system. This is because I believe that a marriage between traditional Japanese management and this new diversity management could have a broader and crucial impact on our knowledge-based economy in the future and could improve the performance of companies all over the world. I will try to explain why and how I believe this to be so in this brief article.

Creativity & Diversity

Creativity is a key to promoting innovation, the principal source of a firm's competitiveness today. Diversity within a business or R&D team could create new opportunities or technology, since the wide range of backgrounds of the members would invite a greater variety of views than otherwise and new ideas could be born from a synergy among those views.

LIXIL Group Corp., a Japanese housing industry company, is actively promoting diversity among its employees by sex and nationality in pursuing the internationalization of its business. It aims at producing unique products or localizing products for each sales region or country, and a high degree of diversity could certainly enable it to achieve such a business goal.

However, without good leadership and teamwork, diversity could provoke serious conflicts among employees rather than creativity and innovation. In order to achieve its goals, companies will need leaders with confirmed beliefs and strong commitment to reform and innovation. The structure of the management of a company is therefore important in turning it into a creative business. A diversified management team could be a catalyst in producing creativity through the synergy of a variety of views. One way of acquiring diversity in products and technologies as well as in management from outside the company is through M&As. Cisco Systems Inc., an IT network equipment giant, is known to have achieved significant growth through the mergers of many IT ventures with creative technologies.

Diversity can be considered an absolute necessity to meet the need for new technology. High speed Internet, Big Data technology, Artificial Intelligence, 3D printing technology – these new technologies are starting now to get into our offices and will facilitate new jobs and new working styles. Flexible workers such as freelancers or parallel workers doing jobs for several companies at the same time would be an absolute necessity for a company to maximize the benefits of these new technologies. Companies may not need so many people working full time and will try to recruit non-permanent technology experts from all over the world for each specific project while keeping a minimal management team and staff as permanent employees. This would be the least expensive way of running their business, since developing the professional skills required to deal with the new technologies in a company would be more costly and time consuming, and thus companies may not be

able to keep up with the high speed of new technology development.

Expansionary use of information and communication technology (ICT) in companies is also changing the working style of employees, whether they are permanent or non-permanent. As the cost of information transmission in companies declines thanks to the spread of ICT, horizontal communication among employees will be enhanced and direct communication between CEOs and employees at particular business sites will also improve, and thus each worker will feel more empowered. The middle rank of management could be minimized and a company's structure could become less hierarchical. Such a flat-type management structure would make it easier for a company to manage a diversified workforce, as it would only require a competent CEO eager to achieve reform and innovation.

Business management utilizing ICT would also enable employees to adopt more flexible working styles, such as working at home, and this would also encourage diversity among employees. Working mothers, for example, would naturally prefer to work at home. Assuming that maximum utilization of ICT will give a company a valuable competitive edge, this trend of increasing diversity in the workforce will be irreversible. But maintaining the high motivation and team spirit among employees that would have been created previously by face-to-face communication will be a crucial point in achieving good management.

Diversity & Risk-Taking Business Behavior

We are living in a world today that is plagued by various rising risks, ranging from low growth in the world economy to all kinds of geopolitical risks. How to manage these risks will be a key to raising a company's growth potential or profitability. According to Japan's new Corporate Governance Code, a company's board is expected to take the business environment into account in making appropriate risk-taking business decisions. Independent directors, as redefined in the Code, are expected to encourage such good risk-taking decisions. Japanese companies' CFOs have been working on daily business decisions on finance up until now, but following the publication of the new Code they must also be working on more strategic business decisions. In particular, M&As with foreign companies seem to be one of the most common business strategies under globalization.

To achieve the best business outcomes, I believe that risk-taking decisions based upon legitimate assessments of the investments and a company's own financial performance will be necessary. Foreign board members or independent directors could encourage such risk-taking decisions on M&As by Japanese companies because they would have a network with the top management of foreign companies. This would be another merit of diversity management.

Apart from the question of M&As, in order to respond well to growing uncertainties worldwide we should in any case maintain diversity among management in the face of an unforeseeable future. Unexpected natural disasters or growing geopolitical tensions could occur quite suddenly. It will be important to have board members

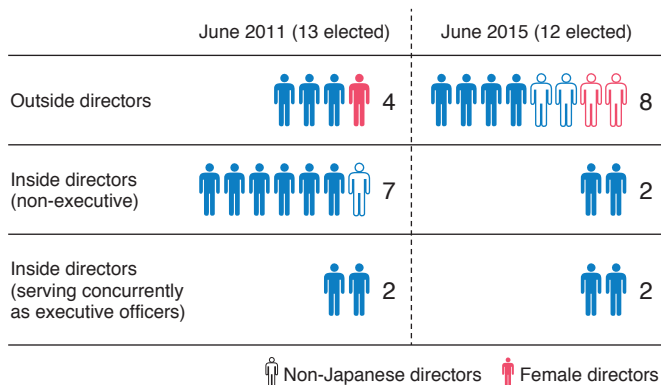
CHART

Increased number of outside directors including non-Japanese; outside directors became majority (June 2012 ~)

Major Aims

- Reflect global, diverse viewpoints in management, further strengthen oversight function

Composition of Board of Directors



Source: Hitachi, Ltd. Annual Report 2015, p. 19

with different business philosophies who could make the most appropriate business decisions in any given situation.

New Japanese Management Model to Lead Knowledge-Based Economy in 21st Century

Diversity will empower businesses, as we have seen. But good teamwork among the various members of a company will be necessary to maximize its benefits. Traditional Japanese management methods, which aim at achieving close human relations among employees as in a family and providing a strong motivation for each employee to work hard for the company, would be effective in such maximization of the benefits of diversity.

In the current world of post-industrial capitalism, a more individual-oriented economic and business system capable of producing knowledge and creating distinctive competencies will come to dominate. In this system, the principal actors will not be products but human beings. As the weight of the service economy increases due to the greater role of computer software, this trend will become more significant.

The traditional Japanese management style, a human-oriented one based on face-to-face communication supplementing communication by ICT, could work well through the marriage of diversity among employees and management to achieve full strength, and thus could show the rest of the world a model for a management system that works well under post-industrial capitalism. **JS**

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