Ongoing Transformation in Japanese Management

By Yosuke Naito

Keizai Doyukai (Japan Committee for Economic Development) published its fiscal 1985 "white paper on Japanese corporations" in January 1986. This annual report, entitled "Progress in the Globalization of Japanese Corporations," describes progress and problems in corporate internationalization, and was based on a summer 1985 survey of corporations listed on the Tokyo Stock Exchange. (Respondents to the poll numbered 604.) The report provides an eye-opening look at how the "dematurity"* and globalization of Japanese corporations are interacting with each other in transforming traditional Japanese management practices.

Globalization gains momentum

In terms of stock, Japan's globalization still lags considerably behind international standards. For example, the balance of foreign direct investment is less than 3% of GNP, compared with 7% for the United States, 20% for Britain and 6% for West Germany. The per capita foreign direct investment balance is $270 in Japan against $964 in the United States and $1,618 in Britain. Japan's overseas production as a percentage share of domestic production also remains at a relatively low 3% (1982), compared with 18% (1976) for the United States and 23% (1971) for West Gemany. The low levels of foreign direct investment and overseas production show that Japanese corporations trail in overseas activities.

In 1985, however, a number of external factors combined to accelerate Japanese corporate globalization. One was the intensification of trade friction between Japan and some of its major trading partners, particularly the United States. Japan experienced trade friction in the early 1970s over textiles and steel, and in the latter half of the 1970s over home appliances. More recently, however, the scope of friction has widened to include cars and electronics. These trade tensions have forced Japanese producers to establish factories abroad.

The sharp appreciation of the yen is another external factor contributing to globalization. The yen has appreciated rapidly against the dollar since the G-5 monetary conference in September 1985. The current yen rate greatly exceeds the level at which Japanese corporations can cover the negative impact through internal efforts. According to a questionnaire survey conducted by Keizai Doyukai in late March 1986, many of 93 executives polled replied that their organizations would put greater emphasis on products with higher value added and high-technology items, and over the longer term transform their business structure to cope with the higher yen. However, the replies of basic materials industries differed from those of processing and assembly industries. The former emphasized high-value and high-technology products and structural change. In contrast, the latter gave priority not only to high-value products but also to parts procurement from abroad and expansion of overseas production bases. The continuing yen appreciation is expected to promote the globalization of Japan's processing and assembly industries.

Present state of globalization

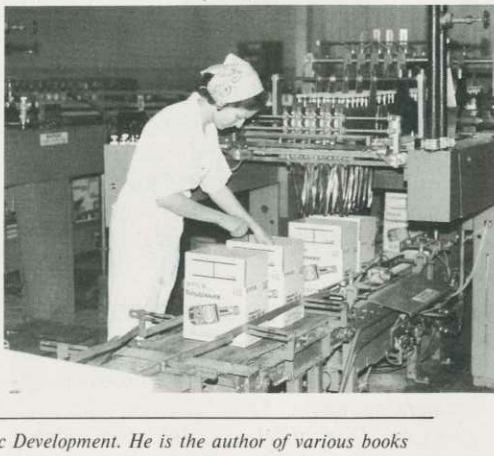
The globalization of Japanese corporations has generally followed three stages. In the first stage, export was the main form of overseas activity. Business activities consisted mainly of manufacturing and marketing in Japan. At this stage corporations relied heavily on technology introduced from abroad. General trading companies and banks also played a large role in the globalization of Japanese corporations during this period. It was also the period during which Japanese manufacturers were able to concentrate on innovation in their production lines.

In the second stage, Japanese corporations began shifting part of their domestic production overseas, although the primary responsibility for management remained with their head offices in Japan. It is also notable that management separated overseas and domestic activities.

Many Japanese corporations are now in the second stage of globalization. Much progress has already been made in the partial transfer abroad of their domestic production divisions and factories. But it has also been pointed out that Japanese corporations are good at management stressing front-line activities, but lack the ability to define company-wide strategy. Corporations in this stage are having some difficulty in maintaining integral control of their production bases as they spread around the globe.

Globalization in the third stage involves allocation of managerial resources and conduct of managerial activities on a global scale. Corporations in this stage promote international division of labor

The Wisconsin, U.S.A. Kikkoman soy sauce plant. Like Kikkoman, more than 90% of large Japanese corporations have overseas operations.



*"Dematurity" refers to a phase in the industrial growth stage which is attainable solely by epoch-making product innovation (for example, the change to quartz crystals from springs in clockmaking). It was used by W.G. Abernathy in his 1983 book *Industrial Renaissance* (Basic Books, Inc.) to explain relations between the industrial life cycle from growth through maturity and the number of possible technical innovations in analysis of development processes in the American auto industry.

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within their own organizations by conducting their manufacturing, marketing, R&D and financial activities in the best possible places around the world. At the same time they try to preserve integral control of their strongholds at home and abroad. Moreover, corporations pushing a policy of globalization regard the whole world as a single market, instead of subdividing it into regional and national markets.

Measured against these three stages of globalization, most Japanese corporations may be said to be at stage two. However, some pioneering corporations are already moving toward the third stratum.

The Doyukai white paper on Japanese corporations sheds light on the present state of globalization. Of the 600 corporations which responded to this specific questionnaire, 76% had overseas bases, while 49% planned to establish such bases.

In the case of large corporations with total assets of ¥500 billion ($2.8 billion at the rate of $1/¥180) or more, 91% replied they already have overseas bases, and 73% said they have plans to expand abroad. Some 86% of the respondents were positive about globalization, expressing a desire to move into foreign countries when necessary. They also said they are looking for such opportunities out of a belief that globalization is unavoidable in the long run.

Although 14% replied that they want to avoid overseas expansion if possible because of the many risks entailed, 95% of large corporations said they would expand abroad in spite of risks.

Regarding the relationship between profit margins and overseas expansion, as many as 64% replied they will invest abroad as long as it is necessary to secure markets and raw material resources, even if expected profit margins are small. By contrast, 36% said they will not invest without expectations of high returns, citing the high risk involved.

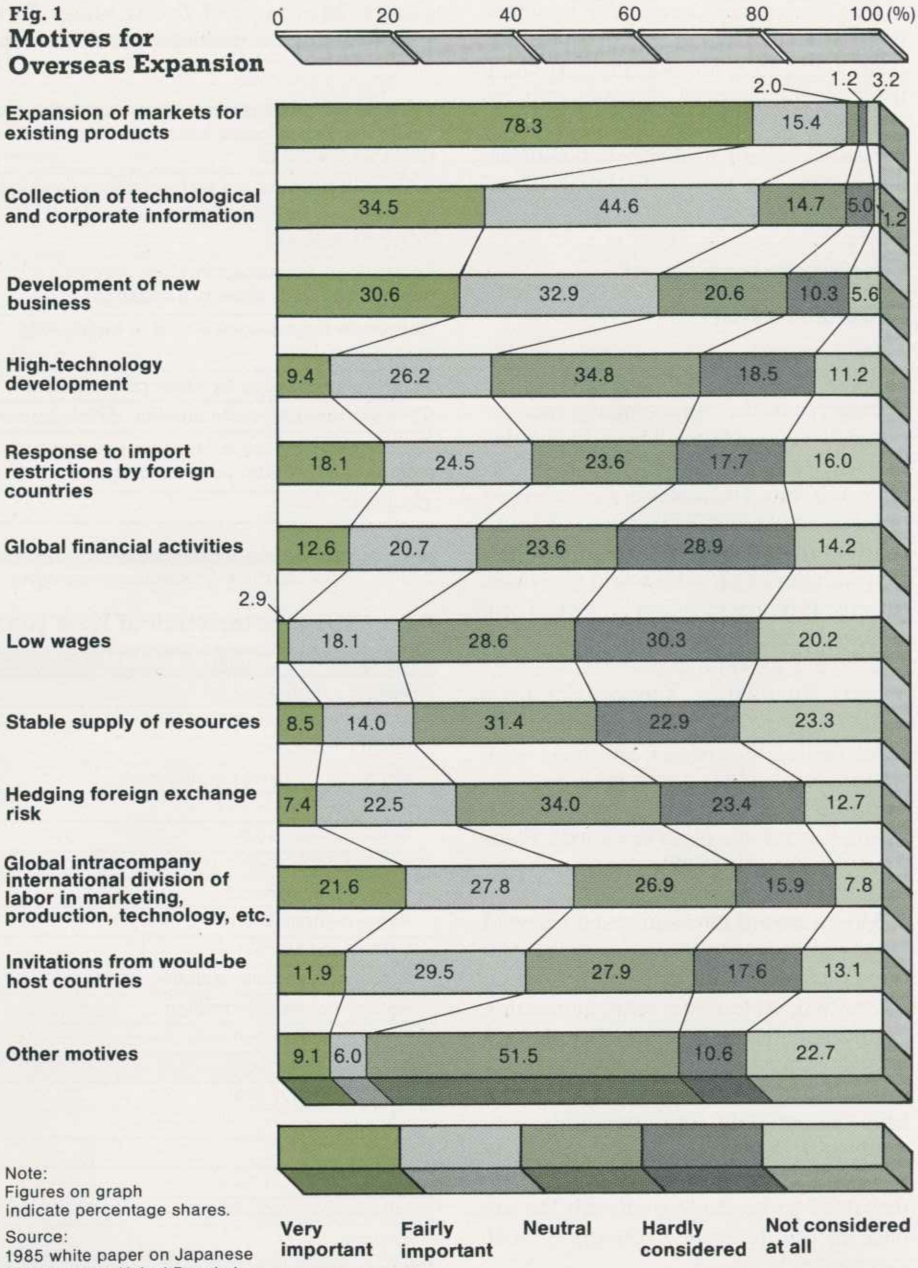
One out of four Japanese corporations with overseas operations is said to operate in the red. It should be noted, however, that the globalization of Japanese corporations is not aimed at making short-term profits, but is meant to promote their international activities over the long term. This view is supported by the survey, which finds that more than 90% of the corporations clearly differentiate portfolio investment and foreign direct investment. Moreover, 57% do not want to withdraw from their overseas bases even if they suffer deficits in the short run.

Figure 1 illustrates some motives for expansion overseas and some of the characteristics of the globalization of Japanese corporations. The graph shows that most corporations now attach little importance to low wages and stable supplies of resources—two of the main motives which once drove Japanese corporations to expand abroad. Now the most important reason is to expand markets for existing products. The second most important is collecting technological and corporate information. Next comes high-technology development, followed by global intracompany international division of labor and responses to import restrictions. Last on the list was invitations from would-be host countries.

But these motives look somewhat different when the size of total assets is factored in. In the case of large corporations with assets of ¥500 billion or more, the most important motive remains the same: market expansion. But the development of new business comes second, followed by information gathering. In addition, large corporations place greater emphasis on the global intracompany international division of labor, import restrictions, global financial activities, invitations from would-be host countries and hedging against foreign exchange risk.

Clearly, both the direction and nature of Japan's globalization are changing. Emphasis is placed not only on market expansion and information gathering but increasingly on moves toward dematurity, such as the development of new business and high-technology development

Fig. 1
Motives for Overseas Expansion



Note:
Figures on graph indicate percentage shares.
Source:
1985 white paper on Japanese corporations, Keizai Doyukai

ment. The priority given to intracompany international division of labor, import restrictions, invitations from host countries, global financial activities and exchange risk hedging also indicates a diversification of motives that is bringing a new dimension to the trend toward globalization.

Characteristics of globalization

One notable development in the globalization of the Japanese corporation is progress in the intracompany international division of labor. This is happening in such sectors as automobiles and integrated circuits. Examples of such division of labor abound in American and European multinational corporations. IBM, for example, divides the world into three regions. Product selection and parts procurement are coordinated within each region, but in some cases extend across regional boundaries. Xerox maintains a matrix network of nine special business units (SBU) for copiers, printers, work stations and other product lines with operating units in the United States, Japan, Europe and other territories. Plans formulated by the SBUs are coordinated with operating units.

Moves toward international division of labor within Japanese corporations rapidly gained momentum as trade friction intensified, as can be seen in textiles, home appliances and, more recently, cars and electronics. The fact remains, however, that head office control is not yet fully integrated, and relations with peripheral industries leave much room for improvement. Moreover, further efforts need to be made to absorb the impact on the domestic economy of such division of labor.

Another notable development is the search for new business strategies aimed at establishing international networks in the area of technological development. Business strategy immediately after the oil crises of the 1970s concentrated on trimming operations and cutting costs. Around 1980 this defensive posture gave way to an offensive strategy, and around 1982 shifted again to a mix that sought both expansion and efficiency. By 1984 Japanese corporations had entered a dematurity stage where strategic importance was placed on market and technology development. The 1985 Doyukai white paper says they are now reviewing and restructuring their strategies toward further dematurity, with special importance attached to globalization.

In recent years Japanese corporations have stepped up efforts toward dematurity as they have achieved maturity in their main lines of business. Propelled by technological innovations, they have strengthened their desire not only to revitalize existing lines of business but to expand into new fields. To this end, they have developed new strategies and restructured their organizations. The latest survey shows, however, that Japanese corporations are entering new fields primarily through development of existing internal resources, rather than through extra- and intracompany ventures and utilization of external resources such as corporate takeovers. .

Table 1 details methods of technology development and acquisition and shows that in future the weight of technology developed at central research institutes is likely to decrease while that of technology developed by intracompany ven-

Table 1 Methods of Technology Development and Acquisition

	the late 1970s	the mid-1980s	early 1990s
Technology developed independently at central research institute	47.7%	47.5%	44.1%
Technology developed by intracompany venture, entrepreneurial subsidiary, independent business unit, etc.	16.4	18.0	18.0
Technology developed through research commissioned to other organizations	6.1	7.7	9.3
Corporate acquisitions aimed at technology acquisition	0.8	0.7	1.8
Technology licensed by other corporations	20.6	15.4	12.2
Joint ventures for technological development	3.1	4.8	8.4
Capital participation in other corporations for acquiring or monitoring technology	1.2	1.7	2.5
Others	4.0	4.2	3.8
Total	100	100	100

Source: 1985 white paper on Japanese corporations, Keizai Doyukai

Table 2 Characteristics of New Japanese-style Management

Traditional management	New management
Strategic action	
Operation-centered	Strategy-centered
Internal reserves	Maneuverability (use of external resources)
Stress on main lines of business	Related business, diversification
Development research	Basic research
Efficiency-centered	Innovation-centered
Organization	
Hierarchical pyramid	Horizontal division of labor network
Power centralization	Power decentralization
Large head office	Small head office
Stable bureaucratic structure	Dynamic innovation structure
Bottom-up decision making	Decision making by top leadership
Power in production department	Power in R&D department
Systems and practices	
Lifetime employment	(to be maintained)
Seniority	Meritocracy
TQC	(to be modified)
Company labor union	(to be maintained with raison d'être redefined)
Intracompany education	(to be maintained)
Welfare	(to be maintained)
Human resources	
Homogeneous talent	Heterogeneous talent
Collectivism	Individualism allowed
Company loyalty	(to be maintained)
Egalitarianism	Stress on individuality
Missionary-type leader	Revolutionary leader
Mode of behavior	
Incremental	Entrepreneurial

Source: Corporate Management in the 1990s, Keizai Doyukai tures will increase slightly from past levels. The weight of technology licensed by other corporations has dropped considerably. By contrast, technology developed or acquired through the utilization of external resources, such as research commissioned to other organizations, takeovers, joint ventures and capital participation, is increasing in importance.

In international technological development, Japanese corporations have also relied increasingly on external resources, while the scope of such utilization has widened. Specific methods used include commissioned research by foreign universities and other foreign research organizations, joint research or joint ventures with major foreign corporations and foreign venture capital firms, and the establishment of their own research institutes abroad.

Basic research is expected to play a great role in the dematurity of Japanese corporations, as can be seen in the current boom in the construction of basic research institutes. Further improvement in this area is to be hoped for, as dematurity is the biggest single challenge facing Japanese corporations today. Already Japanese enterprises have an integrated system of research and development management ranging from recruitment to education and training, selection of research themes, reward systems, performance rating systems and even organizational alignment. Within this framework, they have trained large number's of researchers and engineers capable of developing commercially viable products.

However, the establishment of basic research institutes will, and must, have an impact on the traditional management system if it is to achieve its anticipated purpose within the corporation. At the same time, the globalization of research and development, including both basic research and product development, could remake the conventional management system into a more flexible and universal one. It is far more difficult to operate the traditional Japanese management system for research and development in harmony with the cultures and histories of foreign host countries than it is to maintain Japan's distinctive operation-level management system.

In this sense, the rush to establish basic research institutes and the globalization of research and development are closely intertwined, and could add impetus to the further development of Japan's corporate management system. American and European multinational corporations are following positive global strategies for R&D. Companies like IBM and Xerox maintain a global network of basic and applied research institutes in the United States, Europe, Japan and other regions. Moreover, their head offices maintain firm control of these research organizations on a global scale.

Still another noteworthy development is the globalization of financial activities. In this respect, average Japanese enterprises lag considerably behind American and European multinationals. The latest Doyukai survey indicates, however, that some large pioneering corporations in Japan are moving toward constructing a global financial system of overseas bases including financial subsidiaries abroad.

The financial operations of American and European multinationals are under the strong control of their head offices. Or put differently, their business activities are closely coordinated in ways that link them to management goals and programs. These corporations are also eager to develop new methods of coping with exchange rate risks and interest rate fluctuations. Their efforts in this direction have already produced a number of systematic methods which are contributing greatly to their profit position.

In sum, Japanese corporations as a whole seem to be moving from one end of the globalization process to the other, from "multi-domestic strategy" to "global strategy." Under the old multi-domestic strategy, they exported unique products that had first proved a hit in the domestic market, then transferred part of domestic production abroad as international sales expanded. Each foreign country was treated as an independent national market, and dealt with separately from others. In contrast, global strategy seeks to conduct a full range of activities from manufacturing through marketing, finance and R&D under a system of international division of labor—that is, on a truly global scale.

Dematurity and new Japanese-style management

The global deployment of Japanese corporations is bound to have a powerful impact on Japanese-style management. Japanese corporations now in the dematurity stage are moving to shift from their traditional management styles to a new, though still Japanese, management system.

There are two hurdles that must be cleared before Japanese corporations can achieve dematurity emphasizing creative development. One is inherent in Japanese-style management itself. The other is the so-called "big business malaise."

The postwar success of Japanese corporations was the result of Japanese-style management. Strategic importance was attached to rationalizing production lines, a task that was carried out with rigorous thoroughness. Moreover, human resources were managed with characteristic skill.

However, the single-minded pursuit of process innovation also gives rise to a "productivity dilemma." In other words, producers reach a point where they cannot achieve dematurity without product innovation. Traditional Japanese-style management makes it likely that Japanese corporations will come face-to-face with this dilemma sooner or later.

Japan's large corporations today are showing symptoms of big business malaise. These range from rigidity of organizational structure to a deep-rooted tendency to avoid risks, difficulty in achieving intracompany consensus and the overwhelming strength of existing divisions. These characteristics hamper efforts toward business development, which is an essential prerequisite for dematurity.

Table 2 lists the elements of Japanese management which need to be changed in the 1990s and those that need to be maintained. Items requiring change are: (1) the seniority system (to be replaced by the merit system), (2) "bottom-up" decision making (to strategic decision making by top leadership), (3) bureaucratic and rigid organizational structure (to a more flexible structure) and (4) pursuit of short-term profits (to positive management control such as the pursuit of a financial management strategy for R&D investment).

On the other hand, the following items are cited as requiring no change: (1) pursuit of higher operating efficiency, (2) emphasis on human resources, (3) factors contributing to change in the consensual decision-making system and other areas needful of reform, (4) lifetime employment and (5) company labor unions.

As pressures mount at home and abroad, Japanese management clearly faces its greatest challenge in many years. The increasing number of female employees in management posts, increasing labor mobility and employment of foreigners will also inevitably affect the way Japanese companies do business. Yet those corporations that can successfully make the transformation to globalization should emerge in a better position than ever before to cope with today's changing, and increasingly international, business environment. ●