**Hugvísindasvið**

# The Japanese business model, and how globalization is changing it

*Is change necessary for Japanese companies?*

**Ritgerð til B.A.-prófs**

**Daníel Jón Guðjónsson**
**Maí 2009**

**Háskóli Íslands**

**Hugvísindasvið**

**Japanskt mál og menning**

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**Maí 2009**

## Outline of thesis

The Japanese business model is one of the most intriguing aspects of Japanese society in my view due to its ability to export high quality products at low prices. The model's success after the Second World War meant that Japan was the first Asian country to become a first world nation where living standards and longevity were among the highest in the world.

Recently however, it can be said that the model has been changing in order to fit into the emerging global business environment where companies are both manufacturing and marketing their products in many different areas of the world.

Japanese companies used to enjoy the advantage of being able to produce and export products at cheaper prices than their foreign competitors. However because of rising production costs and inefficiency at home, as well as fiercer competition from abroad this is no longer the case. In order to stay competitive maximizing cost efficiency is necessary, and globalization[1] is what makes big companies most cost efficient today. The efficiency changes that are being made in Japan today clash significantly with the traditional business model and that is what makes the topic all the more fascinating.

Globalization has had the effect that export companies are marketing their products to many markets with different types of customers with many different types of needs. Diversifying company staff with foreign and female labor is vital to understanding those customer needs.

The topic leads to the question whether these changes, despite not going hand in hand with Japanese norms, are necessary for Japanese companies to make?

Cheaper labor and manufacturing processes, professionals with specific knowledge and backgrounds and practical business relationships found outside of Japan are things that can improve cost efficiency and innovation at traditional Japanese companies. To most companies it is rather clear that by taking advantage of what the world has to offer instead of just relying on one country's resources[2] is bound to bring a company not only more success, but it is inevitable for survival in today's business environment and the aim of the thesis is to prove just that.

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[1] Globalization: A word used in this thesis to refer to economic globalization, that is, integration of national economies into the international economy through trade, foreign direct investment, capital flows, migration of people and their knowledge, and the spread of technology

[2] Resources: A word used in the thesis to refer to human resources, financial capital, natural resources, supplies, technology and other things that a company needs to reach its objectives.

This thesis comes in four chapters.

The first chapter is a description of the typical traits of the traditional Japanese business model in order for the reader to understand the following chapters. The things that will be discussed in this chapter are isolationism, high-context culture, low foreign investment rate, long-term employment contracts, collectivism, discriminations against female employees, power of corporate management, keiretsu relationships and the role of government.

The second chapter is about the current fundamental changes that are being made throughout the Japanese business world due to globalization. Due to the fact that today's environment is very different from what it used to be only a couple of decades ago the Japanese system has been changing in order to adapt. These changes come in many forms. Examples are western methods of cutting costs and the process of acquiring access to resources outside of Japan in order to recover from the economic downturn of the 1990s and stay competitive against rising global competition. Changes at the workplace will be discussed with focus on the rise of short-term contracts in line with a global business model and promotion based on skill rather the seniority. Other things will be discussed as well such as the rise of female involvement and the increase in foreign staff. Changes in the composition of corporate management, keiretsu relationships, foreign investment, and the role of government will then be made clear.

The third chapter tells the story of the carmaker Nissan after it was bought by French carmaker Renault. Nissan was the first big Japanese company to hire a foreign CEO. Carlos Ghosn changed the corporate organization and culture of Nissan in line with a global standard by reorganizing its staff and making use of global resources. This chapter gives good insight into what globalism can bring to Japanese companies.
The final chapter will be conclusions based on the information at hand. It explains why utilizing global resources are steps necessary for Japanese companies to prosper.

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## Introduction

Japan is a modern economic power as its economy is currently the second largest in the world. This is largely because it has traditionally enjoyed a unique business model that coincided with enormous economic growth in the latter 20th century. The traditional Japanese business model had relied on its own national resources in the form of staff, partners and capital.

Ever since World War II ended Japan had been a nation that relied on its exports for economic recovery. But due to the island country's lack of natural resources, they had to be imported from abroad. However despite this handicap Japan enjoyed an enormous trade surplus from the 1960s to the 1980s as it was exporting for more value than its imports. Due to the trade surplus the economy was growing at an average of 10% a year in the 1970s. In 1960 merchandise exports were valued at US$4.1 billion, but by 1990 they reached a value of $286.9 billion.[3]

In fact the 1980s was the decade when the Japanese economic miracle peaked. Japan deployed its yen reserves outside the country, and quickly became the world´s largest creditor nation.[4]

There was political stability, businesses were profitable, the stock market was booming, prices of real estate soared to record heights and unemployment was kept low. Japanese companies were making high quality products at a lower production cost than elsewhere by commitment of its labor, support of the government and quality inspection- circles. Export companies in Europe and North America were losing market-share to Japanese companies principally because production cost in their home countries was a lot higher than in Japan. Because of lower production costs Japanese companies were able to sell their products at lower prices than their foreign competitors to make a profit.

However, Japan's fortune turned in the early 90s when the economy crashed. Tokyo Stock Exchange lost half of its value in four days and the price of land plummeted thus creating one of the largest asset deflations in history.[5]

Today Japan is the second most indebted country in the world with total public debt of 170% of gross domestic product.[6]

[3] „Trade policy of Japan“ 2009
[4] Nathan 2004: 17
[5] Nathan 2004: 19
[6] CIA 2008

At the same time as this was happening the global business structure was changing. As the Cold War ended in the early 1990s globalization had accelerated as national borders were not as big of an issue for business anymore. Countries were being penetrated with the inflow of foreign investment, people and information.[7]

Today's big and successful companies are more or less using various resources from many countries instead of just their home-country to improve quality and cost efficiency of their production or services. Then these products or services are marketed in many countries around the world by diverse and capable staff with different areas of expertise.

Globalization is changing every country, including Japan. It has been contributing to huge fundamental structural changes of the Japanese business model as many Japanese companies have been looking at globalization as a possible way out of their ongoing economic crisis. Global competition is forcing Japanese companies to cut costs by changing company norms at home and by using resources from countries other than Japan to stay competitive.

However globalization doesn't come without costs. The Japanese are going to have to sacrifice many old traditions and some of their values in order to adapt to it. People on expensive long-term work contracts are losing their jobs and companies are outsourcing activities overseas where manufacturing and other activities are cheaper than in Japan.

The question is whether globalization is an opportunity to get out of the current economic slump, or is it only going to deepen the woes of Japanese companies? Are the steps towards globalization necessary for Japanese businesses to take?

[7] Nakamura 2004: vii

## Description of the Japanese business model

This chapter aims to describe the business model that led to the recovery of the Japanese economy and turned it into the second largest in the world. The characteristics of it will be outlined and made clear to further the understanding of the following chapters.

### Isolationism and High Context Culture

As the Tokugawa shogunate took over Japan in the early seventeenth century Japan was sealed off from the international community for more than 200 years. The objective of the shogunate was to keep Japan stable and out of the reach of foreign influences which were regarded as troubling as they could rock an already fragile community. Not until the Meiji period in the late 19$^{th}$ century did Japan open up again, and as it did it entered the international trading community for the first time in its history.[8]

There are still strong negative feelings among many Japanese towards internationalization that is occurring today. This way of thought is actually very common in the business sector even though Japanese companies have for a very long time been exporting their products to foreign markets as well as importing natural resources.[9]

Massive increases in direct foreign investment have contributed heavily to the globalization of the world economy since the 1990s. Most developed countries recognize the potential of acquiring foreign human resources, physical capital, technology and the creation of jobs that comes with it. However in 1999 the world share of Japanese foreign investment in other countries was 6.2% while foreign investment in Japan was only 0.8%.[10]

The Japanese were buying out foreign monuments throughout the 1980s such as Rockefeller Center and Columbia Pictures but foreign investors were not doing the same in Japan.[11] That being said, it seems that either foreigners are not interested in investing in Japan or that the Japanese business environment is hostile towards foreigners.

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[8] Nakamura 2004: 22
[9] Nakamura 2004: 1
[10] Nakamura 2004: 9
[11] Nathan 2004: 18

Throughout the 1980s foreign investors viewed Japanese assets as too expensive. They also believed the Japanese business environment not to be very hospitable to investors as it was flooded with governmental regulations that would limit their influence.[12]

Another reason to why foreign investment is minimal might be because Japanese companies produce very little return on investment capital[13]. An example of this is that only eight big Japanese companies returned above 10% on investment between 1998 and 2003.[14]

Japan also has a 40.9% standard tax-rate on businesses which can scare off potential investors.[15]

The number of foreign laborers in Japan reflects the amount of foreign investment. Official Japanese policy towards foreign workers is that Japan has no compelling reasons to have them. This policy was adopted when Japan was able to recruit new workers from its own expanding workforce in the 1960s. Foreigners have typically only been permitted to perform special tasks by Japanese employers, such as teaching English, or other jobs that require specific skills that are either rare or not present in the Japanese workforce.[16]

Management experts often separate cultures into two categories, low-context cultures and high-context cultures according to a theory started by anthropologist Edward T. Hall.[17] Most western societies are usually believed to be low-context cultures. That means that what is said and written is the most important source of information between two or more parties. Japan on the other hand is often said to be an example of a high-context country like many other Asian countries. That means that nonverbal and situational messages convey primary meaning. In high-context cultures people's official status, place in society and reputation say a great deal about the people's obligations and trustworthiness. It is common knowledge that certain companies in Japan only hire people from certain schools. Conversation simply provides general background information about the other person. Rituals such as the act

[12] Nakamura 2004: 187
[13] return on investment capital: increase in investment value. (new value-old value)/old value
[14] Northroad 2003
[15] Regulation and trade: Japan 2003
[16] Nakamura 2004: 125
[17] Rogers, Hart and Miike 2002: 13

of exchanging business cards is a social necessity, and failing to a read a card you have been given is a grave insult. The other person's company and position determine what is said and how.[18]

The Japanese language is really suited for this, as it contains different levels of humble and honorific ways of talking based on who is being spoken to and the content of the conversation. The high-context culture might very well be one of the reasons as to why foreigners aren't very involved in Japanese business as they don't understand Japanese norms and subtle context messages.

**Collectivism and Long-term fixed employment**

Many believe that the common Japanese way of thought about measurement of success is very different from the western one and this is very apparent in the working environment.

In contrast to western culture, which is usually considered an individualist culture that emphasizes individual rights, roles and achievements, Japanese culture is often thought of as collectively based. Collectivist cultures are cultures which emphasize duty and loyalty to collective goals and achievements. In those types of cultures people tend to feel more comfortably confined in a group, rather than working by themselves. Group goals and shared achievements are paramount to collectivists, while personal goals and desires are suppressed.[19]

A good example of what collectivism can bring to a company is the Japanese system of Total Quality Management, where people in all levels of a company work collectively and continuously on ideas to improve the quality of the company's product.

Because of collectivism, whether something succeeds or fails in Japan, one person is not to be saluted or be held responsible, but the entire group collectively. Individualistic actions are not encouraged and things that stand out seem to be frowned upon.

Japanese corporations provide employees with a basis for identity very much in the same manner as a feudal samurai family. The CEO is the head of the household. Thousands of workers belong to his organization in the sense as one belongs to a family.[20]

[18] Kreitner 2007: 102
[19] Kreitner, 2007: 103
[20] Nathan 2004: 71

When a Japanese person is asked what his job is, he is more likely to say 'I belong to Company X' rather than saying what he actually does there. He relates more with his group than with his own job. People think of 'our' company, rather than a place where they are employed.[21]

Employees traditionally look to their managers for counsel as if they are respected as family elders. Executives often act as go-betweens in arranged marriages and listen sympathetically if their employees have any domestic problems. These interactions often occur after hours, when the manager takes his employees out drinking.[22]

From this it can be assumed that the relationship employees have with the company involves a lot more than financial benefits. Company life can be viewed as something like a social circle as well.

From collectivism stems one of the most significant characteristics of the traditional Japanese business model, the long-term fixed employment. When a new employee signs on with a company after graduation from college, a personnel manager sits down with him and maps out a career program designed to optimize success all the way to retirement. As a result there is stability and peace of mind which the employee repays with total dedication.[23]

Worldwide, older employees tend to get paid more than their younger counterparts but in Japan this trend is reflected more strongly. Pay levels seem to follow the employee's number of working years more than anything else. Forced retirement between the ages of 55-60, large-sum retirement payments, and twice-yearly bonuses based on a fixed proportion of salary are all systems unique to Japan. In addition to this, under the Japanese promotion system, junior staff within the organization is promoted in preference to bringing in expert staff from outside. This promotion system means that if a worker leaves his job he wipes out years of service. So even if he joins another company his pay and retirement package will be lower. This system promotes the benefits of devoting an entire working life to a single company. Another reason for company loyalty is that it is very uncommon traditionally for businesses to lay-off their

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[21] Nakane 1970: 3
[22] Nathan 2004: 72
[23] Nathan 2004: 70

staff in Japan. If a company is doing badly it tries every option to turn the business around before resorting to lay-offs.[24]

In other words, companies hang on to their staff as long as they can, even if it is unhealthy financially for the company.

**Discrimination against female workers**

When entering the job-market new Japanese female graduates do not have the same job opportunities as their male counterparts. Compared with North America and Europe, there have been very little improvement in Japan in equal opportunity laws. Most upper level managerial positions in Japanese firms are filled by men, with men outnumbering women ten to one.[25]

Average wages between the sexes tell the same story. Japanese men enjoy 50 percent higher wages than women on average for full-time work. One reason for discrimination faced by women in Japan is that employers believe that it is very costly to accommodate periods of absence or reduced work effort from child bearing women.[26]

In a country where working long hours is expected, female workers with children often have to leave work earlier to pick up their children from school or daycare. This is why many of them get turned down for promotion for higher paying jobs.[27]

**The Power of Corporate Management against shareholders**

In America and Europe the common belief is that the purpose of a publicly traded company is to make money for its shareholders. This means an investor decides to use some of his savings to buy stock with the intention of gaining on his investment. He does that with the understanding that the company's board work in his favor as it is their job to increase his share's value.

In Japan it is not that simple. Japanese companies have other goals as well. For example, as mentioned earlier, one of them is keeping labor on board even though by keeping excess staff harms the company financially and therefore also harms the shareholders' interests.

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[24] Okazaki and Okane-Fujiwara 1993: 7
[25] Nakamura 2004: 120
[26] Nakamura 2004: 117
[27] Fackler 2009

The truth is that in Japan shareholders have very little influence over corporate management. This is typically demonstrated in the composition of the board of directors. In most places in the world, the members of the board are thought to work as the representatives of the shareholders. That means that most of board members are usually not affiliated with the company in any other way than sitting on the board and are therefore impartial about how the CEO or management is doing. In Japan this is different. Board members are thought of as regular employees and members have other jobs in the company as well. Because of the Japanese system of promotion, everyone who sits on the board comes from within the company or the company keiretsu. These board members can't be impartial about how the company is doing because they are the same people as those who are working there full time, while nobody on the board represents the external views of the shareholders.[28]

This might very well be because board members aren't really motivated about earnings for their shareholders as their jobs are not at stake.

This lack of motivation effects performance. As mentioned earlier the return on investment is lower in Japan. The average rate of return on equity[29] in Japan from 1900-2007 is 4.3% which is significantly lower than in the United States where the rate stands at 6.5%. Between 2000 and 2007 Japanese equities performed worst of all the developed markets with a decrease in value of 0.7%.[30]

## The Keiretsu System

Keiretsu groupings are big part of today's Japanese business practices. Basically the term "keiretsu" is used to describe a cluster of companies that are all connected together by cross-ownership. Most of Japan's biggest companies are in a keiretsu grouping. Companies within a keiretsu grouping work strategically together in order to advance the interest of the group.[31]

There are two types of keiretsu relationships. First, the smaller picture capital keiretsu relationships that manage the input and output linkages between a single keiretsu company and its satellite companies. A good example of this is the relationship between Toyota and its suppliers of parts for its cars. The second type is the financial keiretsu, or the larger picture keiretsu. The financial keiretsu manages linkages among

[28] Okazaki and Okane-Fujiwara 1993: 9
[29] Rate on Equity: Profit/equity
[30] Dimson, Marsh and Staunton 2008
[31] Jones 2007: 70

many diverse keiretsu companies which usually have at their center a large bank which owns a share in all of the keiretsu companies.[32]

The biggest financial keiretsu groupings have traditionally been Mitsui, Mitsubishi, Sumitomo, Fuji, Dai-Ichi Kangyo and Sanwa.[33]

A particularly good example of how a capital keiretsu network can benefit the companies in it comes from the Japanese car industry. Toyota has been in recent years the most profitable car company in the world. Its cars are constantly ranked among the most reliable, and the company enjoys great customer loyalty. A prime reason for this success is that Toyota controls its part suppliers. Because the car's reliability depends on the quality of its parts, managing their makers is vital for success in the industry today. Toyota owns a 49% minority stake in the companies that manufacture its necessary parts, and therefore can monitor their quality. The inventory system Toyota uses is called the Just-in-Time system. With this system the exact amount of needed parts are delivered from the supplier to Toyota just before they are used. As a result Toyota will not have piles of unused parts in its factory that gradually decline in quality and they are certain to pay only for the amount of parts they need. The manufacturer of the parts also benefits from this because he has constant demand for its product.[34]

Financial keiretsu have benefits as well. If a keiretsu company is having financial troubles it will get a loan through its keiretsu bank with low interest rates. Incidentally the airtight relationship between the bank and the company gets even tighter.[35]

This close relationship is demonstrated in how managers of the dominant companies in a keiretsu will usually sit on the board of directors of the keiretsu bank, and often on the board of each other's companies.[36]

[32] Jones 2007: 70
[33] Melville 1999: 12
[34] Jones 2007: 70
[35] Okazaki and Okane-Fujiwara 1993: 11
[36] Jones 2007: 71

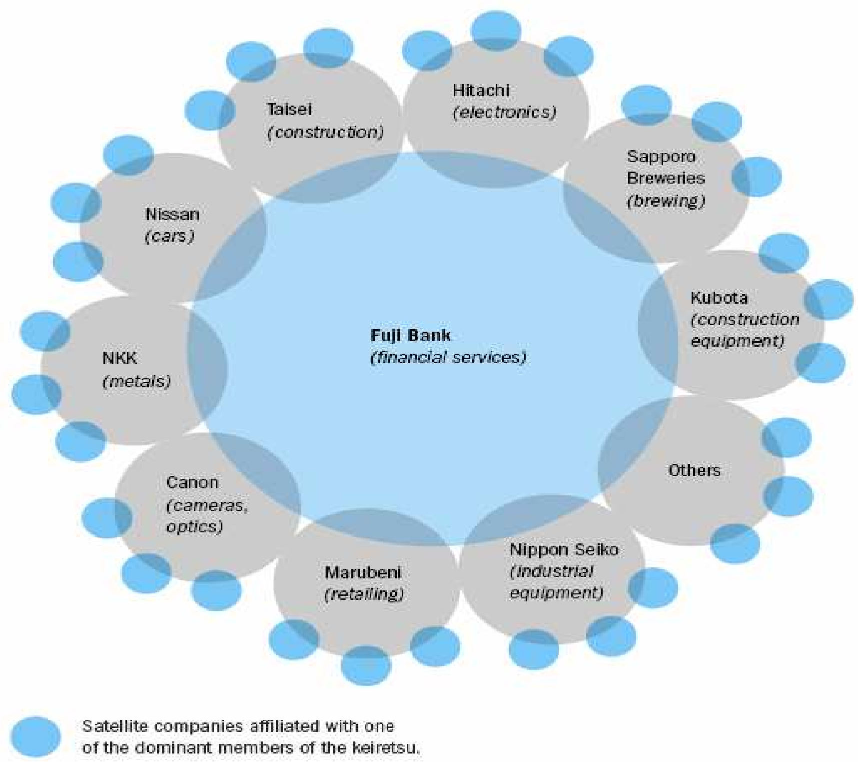


*Figure 1. The Fuji Financial Keiretsu Model. Smaller individual capital keiretsu are the relationship between a unit and its satellite companies.*[37]

**Relations between government and business**

Just like the long-term nature of relations between employers and employees, and between different companies, Japanese businesses and the government enjoy an especially close relationship as well.

In Japan each industry is supervised by a single governmental administrative authority. Examples of these authorities are the Ministry of International Trade and Industry which supervises industrial policy and the Ministry of Finance which supervises policy towards financial institutions. These authorities use a technique called 'administrative guidance' to achieve development and order within the industry. 'Administrative guidance' is the process which occurs when an administrative authority seems to be giving a company a polite tip on what to do and how to do it, when in reality it's a direct order.[38]

[37] Jones 2007: 70
[38] Okazaki and Okane-Fujiwara 1993: 11

Western governments usually tell companies what they can’t do but in Japan the governmental agencies decide what the companies must do. As a result, Japanese college graduates from elite schools, such as the University of Tokyo, are probably a lot more likely to be civil servants than their western counterparts.

Usually the development of an industry comes in three different stages. The first one is the research stage, where new industries that seem to be lucrative are selected by the government and their growth estimated. Secondly, the industries that have been selected and companies that take part in it are given support by the government. That means handing out permits and licenses, low interest loans, tax incentives to the companies to support the development of the structure of the industry. Finally the last part involves the government coordinating the muscles of those companies in order to reach maximum efficiency.[39]

It can be said that this teamwork works both ways. The companies can make huge profits, and the government gets necessary projects done and employment for its citizens.

Because the industries and businesses are so tied together, if something were to fail it could create a domino effect which could bring down the entire system. To minimize the risk of this happening, the agencies have written many regulations to limit competition throughout the industries, covering eligibility, areas of business, deposit rates, and so on.[40]

The Japanese government has also been responsible for keeping the Yen weak in order to help export companies. This was very apparent in the recovery years, from 1949-1971, when the Yen was pegged at ¥360 to a U.S. dollar. This made company production costs a lot cheaper than otherwise.[41]

This very close relationship between the businesses and the government has caught international attention. Nothing emphasizes these close bonds more than the very common act of ‘amakudari’, or ‘descent from heaven’, when retiring governmental officials are offered senior positions at big businesses in order to boost their retirement allowances.[42]

[39] Okazaki and Okane-Fujiwara 1993: 11
[40] Okazaki and Okane-Fujiwara 1993: 13
[41] „What is the Japanese yen (JPY)?“ 2009
[42] Okazaki and Okane-Fujiwara 1993: 13

## Changes in the Japanese business model

The late 1990s were a big growth period for most companies around the world who were doing business globally. In the United States for example the economy grew more than 4% in 1998 and 1999.[43]

In contrast to this the same period was terrible for Japanese business. The burst of the bubble left many Japanese companies in a weak condition. In 1998 the economy shrank by 2% and there was a deflation period from 1999-2006.[44]

In a terrible economic environment like that Japanese companies had to cut costs in order to stay afloat. As mentioned before, from the 1990s and onwards the global business structure has been changing and Japanese companies along with it. Those changes will be discussed in this chapter.

### Changes at the workplace

As Japanese companies face more and more global competition they will have to be just as cost-efficient as other global companies in order to remain viable in the emerging global environment. This applies particularly to employment practices, as they often make up a big part of the company's costs.

As mentioned earlier, wages in Japan have usually depended on seniority. However, a big cost-saving change that is occurring at the moment is that the amount of income based on seniority is coming to an end.

According to the rule of productivity (see Figure 2), when a worker enters a company he is still at the learning the mechanics of his job and thus his productivity isn't very high. Gradually he learns the mechanisms and his productivity increases. By the age of 30-45 he's is in the most efficient period of his life. When the worker is nearing his retirement he is not producing enough for the company to cover his own wages.[45]

If this is taken into account then it can be said that at Japanese companies the most unproductive workers are receiving the most money from it.

[43] Indexmundi 2009
[44] Indexmundi 2009
[45] Nakamura 2004:132-133

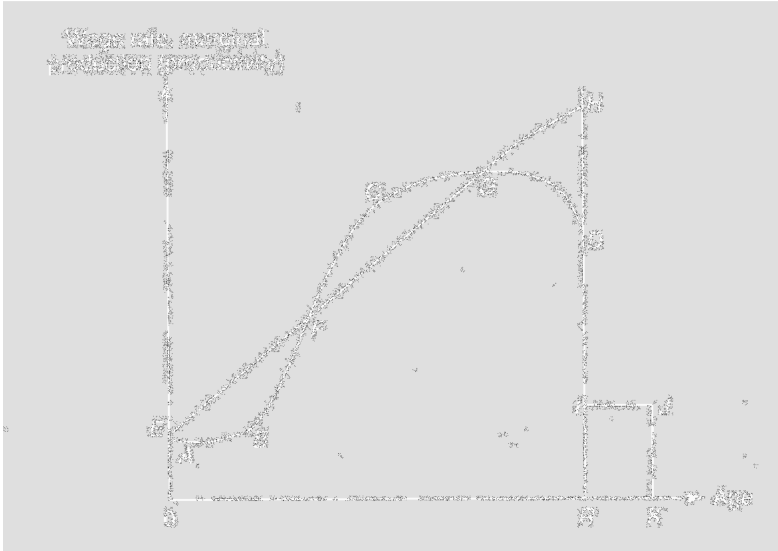


*Figure 2. The rule of productivity according to age. H=wages. The curved line=production rate of the worker. As he enters the later stages of life his contribution to the company doesn't cover his wages.*[46]

Modern Japanese companies are taking measures to cut costs by introducing a new pay-system. This is the same system that is used in most foreign companies, where wages, raises and bonuses will be based almost exclusively on the productivity of the worker. Thus when workers enter midlife their wages will usually reach their peak. This system is becoming more and more common and will probably become dominant in the near future. Life-time employment will therefore die out, as companies will seek to be more productive by getting rid of unproductive staff in favor of younger more efficient staff on short-term contracts. In 1993 31.8 percent of Japanese companies considered long-term employment important, three years later, in the middle of the depression, only 18.9 percent thought so.[47]

One of the biggest hurdles for the Japanese these days is that the population is aging. Basically this Japanese demographic development is characterized by two factors. The first one is prolonged longevity, and the second a reduced birth rate. In fact this is a common development in many Western countries, but in Japan this change is moving more rapidly.
It is estimated that by the year 2015, 25 percent of the Japanese population will be over the age of 65, and by 2050 the ratio will increase to almost 40 percent. At the same

[46] Nakamura 2004: 132
[47] Nakamura 2004: 135

time, the number of people in their twenties will decline from 19 million in 2000 to 12 million in 2015.[48]

This means that by the Japanese system of promotion, as the population gets older the number of managers will increase compared to other employees. If the system is left unchanged it would increase costs as older employees are usually the highest paid group in a company. A normal and healthy company hierarchy looks like a pyramid. This is because the people who have been promoted to the highest ranking positions on top of the pyramid are the smallest group. From there on workers usually increase as their positions within the company become lower. As the population of a country that promotes on the basis of seniority gets older, older higher-ranking workers become a bigger proportion of the companies in it. The company hierarchy then no longer resembles a pyramid, but evolves into an expensive box shape.

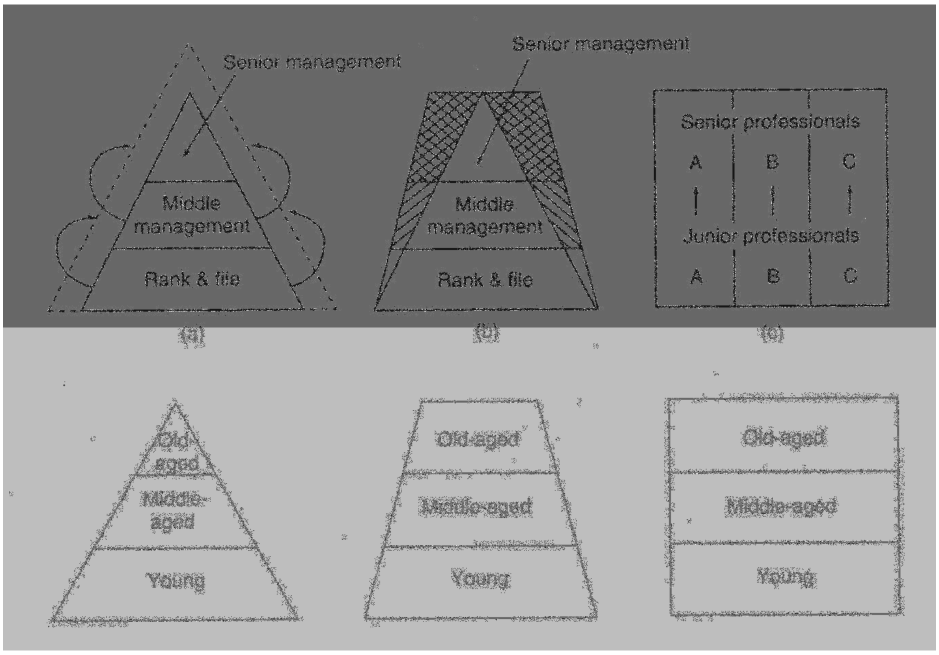


*Figure 3. The development of the Japanese company hierarchy if the Japanese system of promotion is upheld if the current population decrease continues.*[49]

This Japanese system used to work when the population was growing as younger employees always outnumbered older ones. Long-term fixed employment contracts included promises of promotion as the worker got older. When business slowed down in the 1990s many firms had to carry older employees and give them

[48] Nakamura 2004: 129
[49] Nakamura 2004: 134

management titles with no responsibilities just to honor the earlier agreement. This is very costly for the companies and can be lethal for firms going through a major depression like in Japan.

As Japanese companies are trying to adapt to the new environment they have been imposing a new system. In the new system, employees that possess the most or develop superior specialized skills over time will gain promotion just like in foreign companies. Keeping inefficient managers around will become a part of the past. This should cut down costs and increase revenue as management will become smaller, more productive and cheaper.[50]

In 1996, the middle of the depression, only 3.6 percent of Japanese companies thought that seniority was the most important factor for promotion, while most thought the worker's merit was most important.[51]

As a result of the new westernized system of employment, a new class of temporary contract workers called "haken" has emerged. Those employees don't enjoy the same benefits as regular workers. They have lower wages, don't receive high bonuses and don't have the same retirement benefits. This group of people, along with part-timers, has in a short period of time grown to 17.8 million, or one third of the entire Japanese work-force. If lay-offs are necessary temporary contract workers are usually the first victims as they usually don't have any lay-off benefits and therefore it is easier and cheaper for the company to let them go.[52]

Afterwards it is resorted to laying-off normal staff. Lay-offs are something that is very difficult for Japanese managers to do, as cutting off massive numbers of people is something that really hasn't been present in Japanese culture at all. By implementing these changes the tradition of the close patriarchal relationship a manager shared with his employee will probably come to an end. Unemployment rose in 1998 by more than 20% and peaked in 2003 at 5.4%.[53]

In a country where shame is such a big part of the culture these changes are sure to bring drastic results. In the late 90s when these changes were becoming more common, the Japanese suicide rate jumped 35 percent as laid off workers couldn't handle the shame of finding themselves unemployed.[54]

[50] Nakamura 2004: 134
[51] Nakamura 2004: 135
[52] Kageyama 2009
[53] Indexmundi 2009
[54] Nathan 2004: 74

Because work is no longer guaranteed for life it could be argued that competition for various positions will increase because performance, and not seniority, will determine which worker gets promoted. This more competitive reality could change the collectivist ideals at the work place as people will have to think more about themselves and how to advance their own careers.

**Changes in foreign and female labor**

Many would agree that the need for foreign human resources will increase as the Japanese population decreases even further. However despite this and due to strict immigration laws, only a small number of job-seeking foreigners are admitted into the country. Mostly these foreigners are used to fill up positions that require special knowledge that cannot be found in Japan. This policy was adopted when Japan had a young and growing population and there was no need for foreign labor. However things are changing as there aren't enough people willing to work anymore. In 1984 only about 3000 foreigners were working in Japan and in 1986 it was double that. By now, around 1% of all labor in Japan is foreign.[55]

The problem of the decreasing population could also be addressed in the way of granting more positions to female employees. As it was earlier mentioned women are underused in many levels of employment, especially Japanese management. One of the reasons the Japanese birth rate is decreasing is because women are giving up having babies in order to pursue their careers. Women's rights advocates say that the realities of Japan's shrinking population are slowly forcing changing patterns in hiring practices. They say the need to find talented workers has pushed a growing number of companies to make increasing efforts to hire women as career-track employees, in line for management. Some analysts estimate that about a quarter of career-track hires in recent years have been women.[56]

Globalization has forced Japanese firms operating overseas to face the social structure of the host countries. These host country social structures include equal opportunities for employment, and the protection of pay equity. This has influenced Japanese companies to change their attitude at home too. [57]

[55] Nakamura 2004: 123-124
[56] Fackler 2009
[57] Nakamura 2004: 122

In addition to this the Japanese government implemented equal employment law for both sexes in 1986.[58]

As a result the ratio of female managers has risen a bit, from 6.6% in 1985 to 10.6% in 2005.[59] In Japanese companies where there is full foreign ownership the ratio is 18.1% on average.[60]

Although women are still a minority this is a huge increase that this is largely due to a more globalized environment to which Japanese companies are being exposed to. Utilizing a diverse labor force for companies that are marketing in more than one country and to more than one group is very important for understanding customer needs.

**Shareholders, board of directors and the keiretsu**

As explained earlier, the board of a typical Japanese company was usually made up from senior workers of the same company or its keiretsu partners.

It can be argued that because life-time fixed employment is becoming more or less extinct, the boards of companies are bound to change dramatically as the senior workers will not necessarily be the highest-ranking. Now that the employment contract won't be the same, and people will be promoted on the basis of their skill level and job knowledge, it will certainly mean that the boards of the companies will contain people with special knowledge.

In the 1990s the Japanese government instituted certain changes in the laws governing management structures of firms, so that the Japanese corporate governance would be more in line with that of the USA and Europe. To protect shareholders, consolidated reporting is now required and mandated quarterly reporting is being introduced. In addition, firms are encouraged to have outside directors on their boards.[61]

Keiretsu relationships have also been changing. The financial keiretsu groupings are not as many as previously and have been forced to merge as the downturn in the 1990s left them nearly bankrupt after the bubble burst when they were left with $6 trillion in uncollectable property and building loans.[62]

58 Nakamura 2004: 119
59 Fackler 2009
60 The Japan Institute of Labour 2001
61 Nakamura 2004: 238-239
62 Nathan 2004: 19

Sumitomo and Mitsui merged in 2000 as well as Sanwa and Mitsubishi.[63]

Because of the write-offs of bad loans Japanese keiretsu are not as rich as they were and therefore not as able to lend their keiretsu partners. Therefore, it can be said, that companies are probably more prone to look for capital outside its keiretsu circle.

Huge financial keiretsu can be a burden on the individual companies as managing the interests of the group can slow down the decision making progress and make each company less flexible in responding to the unstable competitive global environment.

The system is also very inconvenient for the smaller members as their influence is a lot less than their bigger keiretsu partners. For example, Toyota bought a huge stake in its suppliers in order to tighten its control over them and promote its own interest. This relationship benefits both parties to a certain degree as there is constant supply and demand, but if there is a conflict of interest Toyota's will probably always come out on top because it is the bigger and more powerful company in the relationship. To shareholders of the smaller companies this is very unfair, as their interests are regarded as secondary to those of the bigger companies.

This relationship can also be a burden on the bigger companies. Japanese manufacturers feel obligated to use keiretsu suppliers despite the fact that production costs can be a lot cheaper from individualized suppliers in the global market. This system means that companies are often propping up less profitable partners. If Japanese companies would continue the trend of using the keiretsu domestic suppliers instead of opting for cheaper and better ones they would find themselves at a huge competitive disadvantage to foreign competitors that don't have to pay these extra costs.

Huge Japanese companies such as Nissan and Sony have shown initiative and cut some of these relationships and looked abroad for inputs which improved the outcome in their balance sheets.[64]

### Changes of Foreign Investment

When globalization started to speed up in the early 1990s, foreign investment was one of its biggest factors. Companies were buying factories in other countries to cuts costs, and mergers between companies from different countries were becoming more common to access market-share and information. This would seem to be the next

[63] „Keiretsu“ 2009
[64] Nakamura 2004: 243

logical step for Japanese companies to take, as they were already participating largely in the global market by both exporting their products abroad and investing in foreign companies.

Although foreign investment is still low in Japan, the rate has been increasing. In the early 1990s the inflow of investment into the country was around ¥500 billion. In 1998 it had increased to ¥1.3 trillion and was 2.9 trillion in 2000. Foreign mergers and acquisitions were rising rapidly in the 1990s, from forty in 1997 to 140 in 2000. The biggest examples of these were when French carmaker Renault bought Nissan in 1999, Ripplewood bought the Long-term Bank of Japan, while British Telecom and AT&T bought Japan Telecom.[65]

There are four obvious reasons for this increase in foreign investment. The most obvious one is that foreign investment has been increasing all around the world, and Japan is only following the trend.

Secondly, foreign investors became interested because prices had become affordable compared to what they were in the 80s. The Nikkei stock average had declined from its peak of ¥38,915 in 1989, to ¥20,000 by the mid-90s and then to ¥10.000 in 2001. Corporate taxes were relaxed and handling fees for trading stocks in Japan have become cheaper.[66] This sharp decline of prices enabled foreign investors to undertake greater investment than before.

The third reason is the restructuring of Japanese firms. Many Japanese firms were expanding during the bubble economy period, but some of these new operations were later making losses, largely because of the economically unfavorable conditions in the 1990s. To deal with these problems many companies tried to get rid of unprofitable operations. Some foreign firms saw this as an opportunity to expand their business into Japan and acquired some of the Japanese firms' operations.[67]

Finally this increase can be attributed to the change in governmental policies. In 2003 Ex-Prime Minister Junichiro Koizumi made it one of his goals to double foreign investment in the next five years in his policy speech to the Diet. In 2005 investment increased 86% as deregulation opened up more sectors to foreign capital.[68]

As previously stated, before the Japanese governmental agencies controlled competition in the industries by deciding what each company was allowed to do. Now

[65] Nakamura 2004: 187
[66] Nakamura 2004: 188
[67] Nakamura 2004: 188
[68] „Japan Needs to Boost its Inward Foreign Direct Investment" 2005

that these laws have been relaxed somewhat foreign companies such as Toys R'Us are able to compete with similar Japanese companies in Japan.[69]

### Changes in the role of government

As earlier stated, the government's role has been to form and maintain balance throughout the industries. However now that the system is changing from the bottom up as companies are not going by the same norms and principles as they used to, it could be assumed that the governmental agencies' role will change somewhat along with it.

The reason the government had such a tight grip on the industries was because different businesses and industries were so closely connected and dependant on each other and that if only a few of them would fail it could set off a chain reaction which might take down the entire system. Now that companies are becoming more globalized by outsourcing many of their operations close government intervention might not be as necessary.

Also companies are finding it more difficult to work in the favor of the government as they can no longer guarantee a high employment rate. Also it could be argued that now that the companies are thinking more and more globally and not internally, they could be less prone to do favorable local projects for the Japanese government. Furthermore due to the enormous public debt the government isn't the financial muscle it used to be and therefore is far less able to nurture companies. As mentioned previously deregulation of things such as foreign investment has meant the government's influence lessened.

The Yen has also been gaining on foreign currencies in recent years, which is bad news for the Japanese export companies whose production costs go up. In 2009 the price of a U.S. dollar has been in the ¥90-100 range which is a lowest exchange rate for years.[70] This means that products produced in other countries can be sold at a cheaper price than those produced in Japan. The government no longer seems to take the same steps as before to create a helpful exchange rate for export companies.

The Japanese government wants to change its role as many Japanese nationals have become fed up with the system as it is viewed to be prone to corruption. Recently Prime Minister Taro Aso has pledged to put an end the close relationship between

[69] Nakamura 2004: 188
[70] Google Finance 2009

government and business. He has promised that by the end of 2009 the practice of "amakudari" will be banned.[71]

[71] „Amakudari' arrangement to be banned by end of year" 2009

## The Success of Nissan and Carlos Ghosn

A good example of what globalization can bring to a company is the recent story of Nissan.

In the 1990s the giant Japanese carmaker Nissan was in a lot trouble as it hadn't made a profit for almost a decade. A recovery plan introduced by then CEO, Yoshikazu Hanawa, had failed to bring costs under control, and sales had been dropping year by year since the burst of the bubble. It was clear everybody at Nissan that this trend couldn't go on for much longer as the company was edging towards bankruptcy. [72]

In 1999 French carmaker Renault had its controversial take-over offer for the company approved for $5.4 billion. As explained earlier, Japanese companies have been suspicious of foreign investment, so when a foreign firm bought one of its biggest companies it didn't go down well with a lot of Japanese. Renault promised to reorganize the company and make profitable again. In April of 1999 Louis Schweitzer, the chairman of Renault, sent the French/Algerian national Carlos Ghosn to Japan to help rebuild Nissan and make it profitable again. As a result Ghosn became the first foreign CEO of a major Japanese company. [73]

Carlos Ghosn was the child of a Brazilian father and a French mother and spent his childhood growing up in Lebanon. He left Lebanon in order to pursue his education in France where he received his degrees in engineering and economics.[74] It appears that Ghosn himself had grown up in an international environment which probably affected his management style.

Before he arrived in Japan he had earned a notorious nickname from his former job at Michelin, "le-cost killer" due to his unsympathetic ways of cutting costs to achieve results. When he arrived at Nissan he implemented a plan called the "Nissan Recovery Plan" which he believed could turn the company around in a relatively short period of time. He probably ignored Japanese administrative agencies and their advice as he closed down five production plants and many Nissan owned dealerships in Japan, thus making thousands of Japanese people unemployed. He instead invested in manufacturing plants in North and South America where labor costs are cheaper. He

[72] Nathan 2004: 84
[73] Nathan 2004: 84
[74] Nathan 2004: 85

demanded lower prices from Nissan's suppliers and sold its share in Fuji Heavy Industry, to which it was tied to through a keiretsu partnership.[75]

He also restructured the company from within and totally abandoned long-term fixed employment and promotion based on seniority. When Ghosn arrived at Nissan he was 46 years old, and all of the upper company management was older than he was. He replaced a lot of the upper and middle management team with people who he thought had the necessary skills to help him implement his plan. Global knowledge[76] was used to full advantage as engineers and marketing experts were brought in from different parts of the world. When asked about firing senior staff he said "We are trying to reengineer basic processes and basic decision-making approaches, changing the mindset. We promote those who are more capable of working in this mindset".[77]

The percentage of top female managers at Nissan is twice as high as compared to comparable companies in Japan as Ghosn thought it was a good idea to use their expertise. "Companies make better decisions when women are involved in decision-making", he said.[78]

Naturally Nissan has implemented a mission of maximizing diversity in the company where they try to hire people with as many backgrounds of gender, nationality, culture, education etc. They claim to be committed to increasing diversity to ensure that they meet with the diverse needs of their customers from around the world. Their slogan is "Diversity is our Advantage".[79]

Under Renault, the board of directors of Nissan also changed and shareholders of both companies are represented.[80]

In 2001, only one year into Ghosn's program, Nissan enjoyed its best financial performance in history, posting a profit of $2.8 billion after spending years in the red. Before he took charge in 1999, only four of forty car models were profitable. But by the end of 2003, a large majority of them were making money. At the same time the reduction of the company's debt was 50 percent.[81]

When Ghosn was asked whether the Japanese themselves could have achieved the turn-around that he and Renault achieved his answer was this:

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[75] Nathan 2004: 86
[76] Knowledge: specific information and abilities that people possess that can be shared throughout the company to improve performance
[77] Nathan 2004: 87
[78] „Unfinished business for women“ 2006
[79] Nissan 2009
[80] Nathan 2004: 88
[81] Nathan 2004: 87

> "I can't say whether Nissan would ever have been able to do something about its decline. I can only say they watched eight or nine years of it and didn't take the steps that we have taken. One reason they saw bad performance and failed to act may have been because they thought that even the remaining performance was sufficient. I would say based on my experience here that tolerance for bad performance is higher in a Japanese environment than in a U.S or even a European environment."[82]

It is clear from what he said that he does not believe that under the traditional Japanese management style the same turn-around would have been possible. Japanese management was only following Japanese norms, where things such as lay-offs were impossible and Japanese resources had to be used. This was costly and inefficient and almost bankrupted the company.

[82] Nathan 2004: 91

## Conclusions

The Japanese had for a very long time benefitted from their unique business model. New workers had long and safe careers ahead of them, which guaranteed a stable life and a promotion path for the future. The working environment was friendly as workers enjoyed the fruits of their labor collectively just like a family would.

The companies too enjoyed the benefits. Massive profits were made possible by loyal and capable staff and guaranteed sources of revenue through government sponsoring and loyal and practical relationships with other companies.

However the burst of the bubble and the more globalized environment has forced Japanese businesses to become more practical and efficient in order to be competitive.

Long-term fixed employment can no longer be guaranteed if companies are going to be able to compete with foreign companies who employ cheaper and more efficient labor. Producing through keiretsu circles in Japan is not as efficient as it used to be because of a stronger yen and emerging competing economies such as China that can manufacture products at cheaper prices. This has caught the eye of many Japanese companies who are in desperate need to cut costs.

According to basic economic theory, inward foreign investment can have various impacts on the host country. It leads to the expansion of both output manufacturing and employment. Those expansions increase the income of firms and households, which stimulates investment and consumption, thus promoting economic growth.[83]

So Japan should be embracing foreign investment instead of avoiding it as it improves living standards. Through Renault’s foreign investment Nissan was saved from bankruptcy and turned into one of Japan’s most successful companies.

Nissan’s makeover didn’t occur without a sacrifice. Costs were reduced enormously by making painful changes such as laying off massive amounts of people and terminating close relationships with other companies. However had the company stayed on course it could be said that all of the workers at Nissan would have lost their jobs because the company would have ceased to exist.

As a result Ghosn is an unlikely modern hero in Japan. He won the Father of the Year award, a comic book hero has been dedicated to him, and many books have been

[83] Nakamura 2004: 193

written about him and his management style which have topped the best seller lists in Japan.[84]

Those kinds of books are sure to influence a lot of managers as they look for a new alternative way of doing things.

But just having a foreign CEO of course doesn't guarantee results. The head of Sony, Sir Howard Stringer, hasn't managed a Nissan style turn-around himself. But thinking outside the box, like Nissan did, does make results more likely. Foreign companies have thought outside the box and implemented Japanese oriented ideas such as Just-in-Time and Total Quality Management with much success. Japanese companies should also approach different ideas with an open mind.

In fact Nissan's story is just an example of what is occurring to Japanese business life today as more Japanese companies are realizing the necessity of foreign money, human resources and partnerships and the important knowledge and information it can bring the company.

It is probably not a coincidence that the economy started growing again. From 2004 to 2008 growth averaged more than 2%. Also the inflation rate finally turned positive in 2007. In 2008 unemployment was down to 3.8%.[85] Therefore it can be said that globalization doesn't only benefit companies, but Japanese society in general.

Women and foreigners are very likely going to become a big part of the professional workforce in Japan as the need for skilled labor goes up and the need to understand specific markets increases. Foreign investment is likely increase further as that is what normally happens when economies open up.  As a result shareholders should gain influence over management with time. Utilization by Japanese companies of resources outside of Japan, such as factories, plants and cheaper labor will become ever more prominent in order to cut unnecessary costs.

Globalization can make countries lose some of their unique traits. By relaxing the legal framework the government loses influence. Things such as "amakudari" and "administrative guidance" will probably become a lesser part of business life as the economy continues to open up. Common Japanese business etiquette in the form of collectivism and high-context thinking may also become less important.

[84] Nathan 2004
[85] Indexmundi 2009

Now that the economic condition is worsening again, not only in Japan but globally, globalization is more important than ever before. Japanese companies have been particularly badly hit by the depression as the size of the economy shrank by 12.1% in the last 3 months of 2008 due to decreasing demand of Japanese exports. Nissan has reported that in response to the economic conditions it has decided to slash a further 20.000 jobs, a lot of them in Japan.[86]

Despite being a painful process, cutting costs is inevitable. In a crisis like this it's more important than ever for companies to run efficiently. By taking advantage of what the entire world can offer in the form of foreign capital, technology, staff and information companies should become more efficient as they have more lucrative options to choose from. That not only increases cost efficiency but promotes greater innovation from a diverse group of staff which can lead to future profits.

If Japanese companies want to compete globally they have to do things globally in order to pursue the most efficient way of operating. The theory of evolution can also be applied to the business world as a big company's survival today depends only on how well it can adapt to the global environment. So it's almost impossible to come to another conclusion than that globalization is an absolutely necessary step for Japanese companies to take, not only to stay competitive but to not go out of business.

[86] „Japan Economy Shrank at 12.1% Pace Last Quarter on Export Slide" 2009

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