

**THE IMPACT OF THE 1990s ECONOMIC RECESSION  
ON JAPANESE MANAGEMENT PRACTICES**

*Dissertation submitted to Jawaharlal Nehru University  
in partial fulfillment of the requirements  
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**MASTER OF PHILOSOPHY**

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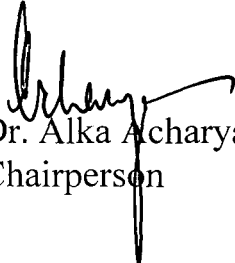
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**CERTIFICATE**

It is certified that the dissertation titled, "**The Impact of The 1990s Economic Recession on Japanese Management Practices**", submitted by **Nishtha Kaushiki** in partial fulfillment of the requirements for the award of the degree of Master of Philosophy, is the outcome of research done by her and has not been previously submitted for any degree of this or any other university.

It is recommended that this dissertation may be placed before the examiners for evaluation.

  
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### DECLARATION

I hereby declare that the dissertation titled, “**The Impact of The 1990s Economic Recession on Japanese Management Practices**”, being submitted to the Centre for East Asian Studies, School of International Studies, **Jawaharlal Nehru University**, in partial fulfillment of the requirements for the award of the degree of Master of Philosophy, has not been previously submitted for any degree of this or any other university. Moreover, analysis and interpretation are my own and I take the responsibility for the same.



Nishtha Kaushiki

*Dedicated*

*to*

*Sai Baba of Shirdi*

*&*

*In the loving memory of my grandfather*

# CONTENTS

|   |                |
|---|----------------|
| <i>Preface and acknowledgements</i>   | <i>i – iii</i> |
| <i>Glossary</i>   | <i>iv – vi</i> |
| Introduction  | 1 – 6          |
| Chapter 1: The Japanese Management Practices: Evolution and Features                | 7 – 32         |
| Introduction  |                |
| Evolution and Development of Japanese Management Practices                          |                |
| Basic Features of the Japanese Management Practices                                 |                |
| Other Features of the Japanese Human Resource Management                            |                |
| ‘Diamond Structure’ of the Japanese Management Practices                            |                |
| Economic Recession and the Burst of the Bubble Economy                              |                |
| Chapter 2: Human Resource Strategies and Employment Relations                       | 33 – 72        |
| Introduction  |                |
| Traditionalism Versus Modern Day Changes  |                |
| Laying off the Inefficient Workers after the recession                              |                |
| Increasing Meritocracy  |                |
| HRM and Economics at Work   |                |
| Shorter Number of Working Hours   |                |
| Production Moved to Offshore Locations  |                |
| Transfer of Excess Manpower to the Suppliers’ Companies                             |                |
| Forced Early Retirements  |                |
| Increasing Number of Job Hoppers  |                |
| Rehiring Retirees   |                |
| Rise of Online Recruitment  |                |
| Hiring of the Non-Regular Employees or the Freeters                                 |                |
| Growing Percentage of the ‘Dispatch’ and ‘Temporary’ Workers                        |                |
| Role of the Labor Unions in Diversified Employment                                  |                |
| Practices due to Economic Recession   |                |
| Management’s Response to the Growing Need for Foreign Workers                       |                |
| Conclusion of the Chapter   |                |
| Chapter 3: Corporate Governance and Changing Practices: 1990s<br>Economic Recession | 73 - 115       |
| Introduction  |                |
| Principles of Traditional Japanese Corporate Governance                             |                |
| Problems associated with the Traditional System                                     |                |
| Economic Recession and the Asian Financial Crisis                                   |                |

Demand-Pull and Policy- Push Reforms  
 Demand-Pull Factors  
 Policy-Pull Factors  
 Reforms Relating to Corporate Law  
 Deregulation of Mergers  
 Hostile Takeovers  
 Share-for-Share Exchanges (Stock Swaps)  
 Corporate Divisions  
 Reforms Relating to the Accounting Matters  
 Reforms Related to the Corporate Governance  
 Reforms Related to the Shareholders' Interests  
 Strengthening Statutory Auditors  
 Changes in the Corporate Pension System  
 Process of Bringing Pension Reforms  
 Basic Structure of the Japanese Pension System  
 Types of Pension Schemes  
 Corporate Pensions and Retirement Allowance  
 1990s and Pension Reforms  
 Reforms in Postal Services  
 Conclusion of the Chapter

|              |                             |           |
|--------------|-----------------------------|-----------|
| Chapter 4:   | Role of Women In Management | 116 – 132 |
|              | Introduction                |           |
|              | Women in Post World War Era |           |
|              | Women in Employment         |           |
|              | Conclusion                  |           |
| Chapter 5:   | Conclusion                  | 133 – 152 |
| Bibliography |                             | 153 - 166 |

## **Preface and Acknowledgements**

The study presents a broad outline of Japan's business practices and the changes brought within the same in the light of the changing economic situation due to the economic recession of the 1990s. The main aim of this study is to have an understanding of the evolving management practices that were earlier unknown to the Japanese society. However, it is essential to point out the fact that most of the practices concerned in the study are confined to the major Japanese corporations. It is construed that these do not find a place in the management practices of small, medium, and family based enterprises in Japan. Further, kept in viewpoint was the fact that Japanese society as such is a traditional one that is immune to sudden changes and this has been the primary reason for the changes being gradual in nature, rather than rapid.

The work contains a critical review of the literature published in English with the focus on the changing Japanese management practices in the context of economic recession. A modest attempt has been made to provide a balanced viewpoint on the same. The methodology used for the study involves analytical and descriptive methods, and also the use of comparative methods for bringing out a distinctive picture of the evolving practices vis-à-vis previous trends.

Due to the restrictions of time and space in the dissertation period, it was not possible to include the impact of the recession on the entire gamete of management: purchase, production, finance, personnel and marketing. Nevertheless, to learn the seriousness of impact two important areas viz personnel and finance (corporate governance) have been covered modestly, with more emphasis having been given for the development and changes taken place during the last decade and the current years of the twenty-first century. Also, access was limited to the books, articles and the primary sources available only in English language due to my own limitation in Japanese language. Japanese terminology has been used in this text as italicized appropriately and Japanese terms have been romanized in the Standard style.

Realizing the fact that women were discriminated against before in spite of the prevalence of the Equal Opportunity Law (EOL), nowadays, their entry and continuation of job have become noticeably high. Thus, the role of women in Japanese management has been included in the dissertation.

A number of volumes came out on all aspects of Japanese style management in the 1980s. Japanese style management was symbol for accounting for higher level of productivity. The low level of industry dispute and low level of workers alienation have been considered as epitome of the success of Japanese. However, recession of 1990s resulted in proclamation in several kind of criticism such as their traditional approach, slow in decision-making, slow in reforms etc. It appeared that the western managers were too impatient for the alteration in the managerial style. The study aims to give a balance view of both positive as well as negative effects of recession on the changes that Japanese society is making in corporate governance as well as HR strategies.

I find myself fortunate enough to be surrounded by helpful people during the course of this work. First and foremost, I take this opportunity to thank my supervisor, Dr H. S. Prabhakar, who spared his precious time and energy in going through my drafts and also suggested improvements and changes as per the need. Working under him has been an enlightening experience and moreover, he has been very supportive and encouraging throughout the period of my M.Phil. Program. Next, I thank Mr. D.L. Sachdeva (Senior Librarian) & Mr. Prakash Gouda (Dy. Librarian), FORE School of Management, New Delhi who were very kind enough to let me use their library facilities.

Further, I thank my aunt (adopting mother), mother and my younger brother Ashish who have helped me a great deal not only with their physical presence but also with their care, love and understanding. In particular I thank Ashish and Mrs. Mamta Bhalla who were very cooperative and kind enough to teach me the computer skills for completion of this work



I also utilize this platform to thank my seniors Mr. Mahendra Prakash, Mr. Shamshad Khan, Mr. Subasis Bera and Mr. Mahesh Sarma who not only advised me on my dissertation, but also supported and helped me. I also thank Nishita who has been supportive of all the friends available not only through the research but also in various phases of my life. Also, Dharmendra has to be obliged because of his support and contribution in the dissertation discussions in spite of the fact that he comes from a very different educational background. I also take this opportunity to thank my classmates Abhay, Nabeel and Varalaxmi who provided me with a very joyful company, intellectual and moral support and further, acknowledgements would remain incomplete without the mention of Mr. M. Narasimha Murthy who was highly encouraging and gave me solidarity when I needed it. Last, but not the least, I thank all my friends whose names do not appear here but who do matter.

I may be forgiven if there are any inadvertent mistakes left in the work.

## Glossary of Japanese Terms

Although the Japanese terms used in the study are defined as and when introduced, yet for the avoidance of confusion, a summary of the terms with brief explanations is given below.

|                          |  |
|--------------------------|--|
| <i>Arubaito:</i>         | Part-time job.   |
| <i>Giri:</i>             | Duty   |
| <i>Gomai Kaisha:</i>     | Partnership company with only unlimited partners.                    |
| <i>Goshi Kaisha:</i>     | Partnership company with both unlimited and limited partners         |
| <i>Godo Kaisha:</i>      | Limited Partnership Company with only limited partners               |
| <i>Ginko Ho:</i>         | Banking laws   |
| <i>Hokengyo Ho:</i>      | Securities exchange law  |
| <i>Haken shain:</i>      | Dispatched workers   |
| <i>Haken rodosha:</i>    | Temporary workers and contract workers                               |
| <i>Ippanshoku:</i>       | Dual track career system   |
| <i>Jidoka:</i>           | Autonomous quality assurance   |
| <i>Kyosai:</i>           | Pensions for civil servants and private school teachers (mutual aid) |
| <i>Kosei:</i>            | Corporate employee pension (welfare)                                 |
| <i>Kokumin:</i>          | Pension for self employed people and others (national)               |
| <i>Kigyo Shudan:</i>     | Corporate group  |
| <i>Keiretsu:</i>         | Business group   |
| <i>Kabushiki Kaisha:</i> | Joint stock company  |
| <i>Kanban:</i>           | Used usually in the context of 'Just in Time' (J.I.T) delivery       |

|                            |  |
|----------------------------|--|
| <i>Kaizen:</i>             | Continuous improvement   |
| <i>Kitsui:</i>             | Difficult  |
| <i>Kitanai:</i>            | Dirty  |
| <i>Kiken:</i>              | Dangerous  |
| <i>Karoshi:</i>            | Death by overwork  |
| <i>Karo jisatsu:</i>       | Suicide by overwork  |
| <i>Kigyō betsu kumiai:</i> | Labor unions post World War II   |
| <br>                       |  |
| <i>Mudadori:</i>           | Time and resource management   |
| <i>Madogiwazoku:</i>       | Employees who are made to sit by the window side and who have nothing to do but look outside the window. |
| <br>                       |  |
| <i>Nikkejin:</i>           | South Americans (Brazilians) of Japanese ancestry  |
| <i>Nikkeiren:</i>          | The Japan Federation of Employers Association  |
| <i>Nenko joretsu:</i>      | Japanese style seniority system  |
| <i>Nemawashi:</i>          | Informal method of managerial communication  |
| <i>Ninjo:</i>              | Tolerance  |
| <i>Nottori:</i>            | Hijacking  |
| <i>Nenkin shingikai:</i>   | Pension Advisory Committee   |
| <i>Nenkin kyoku:</i>       | Pension office   |
| <br>                       |  |
| <i>On:</i>                 | Benevolence  |
| <br>                       |  |
| <i>Paato:</i>              | Low paid part-time workers   |
| <br>                       |  |
| <i>Rengo:</i>              | National Federation of Private Sector Unions   |
| <i>Ringi sei:</i>          | Formal method of managerial communication  |
| <i>Rengo:</i>              | National Federation of Private Sector Unions   |
| <br>                       |  |
| <i>Shojinka:</i>           | Flexible work force  |
| <i>Shushin koyō:</i>       | Lifetime employment system   |

|                            |  |
|----------------------------|--|
| <i>Shunto:</i>             | Spring wage offensive staged by the labor unions |
| <i>Sougoushoku:</i>        | One-track carrier system                         |
| <i>Shakai hoken:</i>       | Employer's health plan                           |
| <i>Shikko yakuin:</i>      | Executive officers                               |
| <i>Shikko yakunin sei:</i> | Executive officer system                         |
| <i>Soikufu:</i>            | Creative thinking                                |
| <br>                       |  |
| <i>Wa kon yon sai:</i>     | Japanese spirit and western technology           |
| <i>Wa:</i>                 | Harmony  |
| <br>                       |  |
| <i>Yugen kaisha:</i>       | Limited Liability Company                        |

## INTRODUCTION

This work presents in broad outline an analysis of Japan's business organization practices popularly termed as 'Japanese Management Practices' by the western scholars at a time when the west was fascinated by the miracle economic growth after the post World War II. The fascination with the same reached a saturation point in the beginning of the 1990s when the economic recession set in. The same practices that were hailed as the chief architect of the economic growth were now being questioned. Further, Japanese corporate governance practices have also been severely criticized as one of the primary reasons for Japan's poor economic performance in the last decade. Facing the prolonged recession since the burst of financial bubble in 1990 Japan has been experimenting with various new policy initiatives both in the public and private sectors. Changes have been brought about gradually in the management practices with special regard to the Human Resource Practices with corporate governance reforms being one of such policy initiatives.

*Chapter 1* titled as "*The Japanese Management Practices: Evolution and Features*" begins by defining the key features of the Japanese management system while tracing their evolution keeping in mind their socio-cultural context. The key Japanese management practices also called the "Three Sacred Treasures of the Imperial House" that developed overtime are lifetime or long- term employment (*shushin Koyo*), the length-of service reward wage system (*nenko*) and enterprise unionism (*Kigyo-betsu kumiai*) have been emphasized apart from the reference given to the other management practices. "The Lifetime Employment System" also called the permanent employment system refers to the period spent by the worker in a firm from the school graduation till his retirement (60 years). However, it has to be noted that this is not a "gentleman's promise" and was directly related to the fact that during the high economic growth era since the profits were unusually high, it did not pinch the pockets of the company even if workers who didn't contribute efficiently stayed back. Companies invest heavily in their human resource by the way of training and in return employees of the job security guaranteed by the above system, they are expected to work hard and display their

sincerity to the company. Further, they also get various types of fringe benefits, and bonuses and pensions.

Another distinctive feature of the Japanese management practices as explained in the same chapter is the system of promotion and reward, popularly known as the seniority system. Wages no doubt begin low but with the gradual increase in the seniority, the former also increases. Thus, there exists an understanding between the workers and management that as the time spent by an employee increases, the wages will also increase by the way of regular promotions.

Correlated to the above two features is the system of bonus which is bargained collectively by the company or enterprise unions which happens to be the third pillar of the Japanese management system. Labor unions are organized on a company basis and they exercise the three primary rights: the right to organize, bargain collectively and strike. They are primarily responsible for maintaining and improving the workers' quality of life and working conditions. They engage themselves in spring wage offensive or '*shunto*' or the annual wage determinant process. The other features of the Japanese management are communication through Quality Control Circles and the Suggestion System (Individual Centered) and *Ringi* and *Nemawashi* (Managerial Communication); The *Ringi Sei* being formal method and *Nemawashi* being informal method; employee welfare programs, involvement and motivation etc.

The features of the Japanese management system are such that they ensure harmony (*Wa*) and avoid unhealthy competition amongst the group members. Further, the features gives a fair chance to the efficient and deserving blue collar employees to move up within the group of white collar employees, the process which is called as *Kazuo Koike*. This happens to be one of the greatest achievements in the field of personnel management since such a provision is totally absent in the western style management. Also, the system encourages leadership based on consensus and not on the power hierarchy relationship.

**Chapter 2** explores the plethora of the changes brought about in the Human Resource Practices and is titled as “**Human Resource Strategies and Employment Relations**”. After the beginning of the economic recession in the early 1990s, there were significant changes in the labor management system at Japanese companies. The reform, which is still underway, is usually called “the introduction of the results-based evaluation and wage system (*jitsuryoku-shugi, seika-shugi jinji seido nodōnyū*).” The reform movement has been driven by employers’ recognition on the financial concern and the necessity of new skills reflecting the liberalization pressure and the industrial structural change as major environmental changes. The economic recession brought about certain internal and external factors for the HR strategies to change. Internal factors include falling profit margins, decreases in white-collar productivity, an aging workforce, and changes in employee attitudes toward work and the seniority system. External factors, on the other hand, include the maturing of the Japanese economy, a decline in large Japanese companies’ international competitive position, and increasing internationalization of Japanese companies’ operations.

Over the last few years, it has been observed that firms have used various means to scale down labor costs. Some of the various techniques followed to cut down on the pay rolls are: overtime reduction, cutbacks in the recruitment of core workers, intra-firm transfers, outplacements to affiliates and subsidiaries, ‘voluntary’ early retirements, and an increasing recruitment of part time and temporary workers by simultaneous gradual departure from the life time employment system to the merit based wages and promotions by explicitly weighting ability and performance over tenure and age in salary decision which contradicts continuation of the inefficient employees of a firm. Further, the firms are administering sophisticated tests and other screening devices to select high quality recruits. Quite a number of firms have adopted the system of online recruiting and have instead adopted direct recruiting in alternate years. The glory of the HR department of being a ‘kingmaker’ was now reduced to a considerable extent. Employee training and welfare expenditures, previously a justification for HR centralization, are being cut. Also, Japanese companies are becoming more cost-focused, as evidenced by “hollowing out”

(the transfer of production jobs to Asia). The changed role of the labor unions has also been focused upon in the chapter.

Moreover, technological changes have revealed some of the limits of traditional practices based on seniority-based wages and on-the-job training. The basic assumption of the traditional system was that workers would become ever more valuable to the company, as they acquired more experience on the job, justifying their steadily increasing wages. However, recent rapid technological developments have surpassed the skills of many experienced workers. The need to fill this gap has increased the competition among firms for promising young workers, not so much because of their relatively lower wages, but because of their adaptability to new technology. Also, increasing competition in product markets requires breakthrough innovations more than incremental adjustments in product development, the latter associated with on the job training. Breakthrough innovations may require more flexible staff policies based on external labor markets rather than internal experienced-based systems of skill formation.

**Chapter 3, “Corporate Governance and Changing Practices: 1990s Economic Recession”** looks at the evolving new practices of the Japanese corporate governance system. Corporate governance comprises the rules, practices, and procedures by which managers are held accountable to those who have a legitimate stake in the enterprise as well as the definition of who those legitimate stakeholders are. Issues of corporate governance include the duties of directors, methods of corporate financing, executive compensation, acquisitions and divestments, and other strategic decisions.

Recent research in the Japanese corporate governance system indicates a direct correlation between the corporate governance and the employment relations. When the management finds it difficult to govern the firm especially in the investments in human capital of the corporate entity, they become inclined to adjustments shifts to employees through various layoff plans. Till the 1990s economic recession, business strategies were resource based with special emphasis on firm based technology and skills. As recession tightened its noose by encircling the entire economy and society, proponents of



convergence point out that, Japanese firms came under heavy pressure from the foreign investors thereby causing major shifts in the corporate strategies.

Also, internal factors such as many banks going bankrupt due to the bad debts that had been accumulated over the years, subsequent unwinding of the dedicated shares held by the banks, and the disintegration of the main bank system etc played a role in the changes in the corporate governance system. .

Some of the changes introduced include the deliberate shrinking of the corporate officer system with a large number of firms having adopted its internal directors in the board of directors and a subsequent addition in the number of foreign directors, thus, the “insider” perspective have been diluted to a considerable extent. Also, the HR executive in many companies is now being denied of any important role in the board. There has been a sharp increase in the number of Merger and Acquisitions (M&A) in the form of ‘hostile takeovers’ in the last few years, something that was considered as an unethical business practice.

There has been a simultaneous adoption of the numerous legal changes in the corporate governance to accommodate a shareholder-oriented approach. For instance the position of statutory auditors have been strengthened. The legal changes in the Commercial Code (CC) shows the acceptance of the government in the changes brought about in the management practices especially with regard to the HR practices and the Corporate Governance. Lately, the focuses of firms have now shifted to the profit-making motive rather than to the expansion motive that was previously held. Pension reforms have also been brought about in the U.S. style thus strengthening the arguments held by the exponents of the convergents.

***Chapter 4, “Role of Women in Management”***, touches upon very sensitive topic- Japanese women in management. While accepting the fact that Japanese society, being quite traditional and gradual to accept changes, this chapter highlights the status, position and the role played by women in management. Infact this chapter deals with the

opportunities extended to women and their acceptance as workers and managers in the society. The Government of Japan has taken certain legislative as well as proactive measures to promote the cause of women as policy makers and also in managerial capacity. Latest developments in this direction have been duly incorporated. Besides that, the large private corporations as well as the multinational companies operating from Japan have also taken some steps in assigning responsibilities to women in the higher position. A brief mention of these has also been made in this chapter.

**Chapter 5, “Conclusion”** sums up the entire summary of the study. It recapitulates the entire findings and observations of the dissertation. The aspects of the Japanese management system that led to the rise of the “bubble” economy have been listed. Further more, the available literature on corporate governance have been evaluated from the viewpoint that it lacks in the interaction between the corporate governance arrangements and the political system. It tends to overemphasize upon the interrelationship between the external finance and the corporate governance arrangements.

The chapter also points out to the charter of corporate behavior released by the Japan Business Federation (*Nippon Keidanren*) in 2004, according to which the member corporations are expected to conduct themselves in a socially responsible manner are supposed to observe both the spirit and the letter of all the laws and regulations while carrying out their activities. Also, vision of the Japan Business Federation (*Nippon Keidanren*) in the form of “JAPAN 2025” has been focused upon. The key areas that have been focused are “made in Japan” policy, new forms of governance, strengthening of the East Asian economy. Thus, the large business corporations have accepted the changes brought about in the Japanese management practices in the light of the economic recession wholeheartedly.

## CHAPTER 1

### THE JAPANESE MANAGEMENT PRACTICES: EVOLUTION AND FEATURES

#### **Introduction**

The earliest settlers of Japan came from the Northeast Asian mainland by way of Korea, and were fused with northward-bound migrants from Southeast Asia who arrived in the Japanese islands by way of the China coast. The island nature of the Japanese geography created a barrier to continuous in - migration and simultaneously promoted the development of a homogenous culture within the islands. Further, the islands being mountainous in nature gave rise to separate village based population and thus strong loyalties to local and regional hierarchies.

The Buddhist missionaries from China further influenced the Japanese indigenous culture, which molded a cultural tradition quite different from the West. The Confucian tradition valued external order and harmony within the society, while at the same time emphasizing the collective aspect of the social order. This has a deep impact on the Japanese managerial practices and thus the individualism in Japan has been overshadowed by the group-oriented behavior. No doubt that some form of individualism does exist in Japan but the Japanese workers do understand the fact that they cannot pursue their individual aspirations openly in the system, and hence they attempt to accomplish it within the framework of the group and the goal of the individual becomes integrated with the firm's goal. In case of a conflict the issue is resolved through an informal gathering. The result being that a group of workers meet to determine and solve their own production problems. Increased identity and esteem amongst the group members lead to increased productivity. Further the most common aim of any Japanese corporation is the "material and spiritual fulfillment" of all the employees in the company and through this successful fulfillment, the objectives and aims of the company are successfully achieved.

The Tokugawa Period (1600 - 1868) came to be identified with a set of values with the virtue of loyalty at the apex. The leaders at that time were the Samurai class, who adopted a code of honor called as the 'Bushido', which had the values of duty (*giri*), benevolence (*on*) and tolerance (*ninjo*) inherent in them. This code did not allow the Samurai class to recognize any authority or obligation other than his Shogun. In a country whose clan structures were strong and cohesive, Bushido superseded even the customs of filial or parental love and responsibility. Samurai class had to be loyal and committed to their feudal leaders and caring for their subordinates.

By 1700, the ideals of group responsibility and loyalty to the authority were directed towards the family unit. It became customary for an entire family to be held responsible for the behavior of each member. Hence group reinforcement, accountability and cohesiveness became matters of necessity and not choice.

Emperor Meiji established constitutional political order with the Meiji restoration of 1868 and a new class of people – the merchants and financiers, who had previously been at the lowest ebb of the society, came to power. The value system was transferred to the managerial class in industrializing Japan. Labor was cheap and the submissiveness of the past did not allow the workers to speak about unions and labor reforms. By the year 1918, the number of factories in Japan had doubled by that of the previous decade and it doubled again in 1924. While the West was suffering from the economic depression of the 1930s, Japan's industrial strength grew by another 50% by the year 1931. The loyalty and commitment that was previously directed towards the feudal lords was now given to the corporations and hence professional development became synonymous with the development of the firm and in return the firm rewarded this dedication with the system of benefits. Gradually this system was adopted in the Japanese society as a whole and hence Japanese managerial system became an outgrowth and reflection of the Japanese historical experience.

Japan being an island country is prone to many natural disasters such as earthquakes and typhoons and thus its history is full of such devastation. The result being that Japanese

usually anticipate the worst and see the arrival of bad times as inevitable. They are also highly adaptable to diverse situations. The psychology of the people is to work hard in a 'sunny day' so that a 'rainy day' can be better managed and this ethos works as stimulus for a work ethics in modern times. Thus a Japanese manager works for longer hours and an example is set before the colleagues and the subordinates.

Patriotism was ignited as a result of the return to the old values of loyalty and conformity and hence Japan jumped into the Second World War with its attack on the Pearl Harbor. With its defeat and unconditional surrender Japan had to re-industrialize itself as a necessity and hence new technology was fused into Japan. Initially Japan started with the borrowed technology of the West but with the hard work, commitment and loyalty of the workers and managers Japan innovated particularly in the electronics that made Japan enter in a 'bubble' period in late 1970s and early 1980s. The Japanese economy grew at an annual rate of 10% from the mid 1950s until the Arab oil shocks of the early 1970s. Also, it represented the largest industrial and consumer market in Asia, and the third largest market in the world. Japanese firms overcame with flying colors, the oil crisis that visited them during the 1970s.

### **Evolution and Development of Japanese Management Practices**

In order to appreciate the meaning of 'Japanese management practices', it is to be made clear what exactly does 'management' mean to the Japanese business entities. Obviously, it will cover the entire gamete of financial systems, relations with government, or methods of management such as industrial relations and labor management, production control, or managerial decision-making and organizations. As already brought out in the preface, the study is aimed at bringing out the changes at the macro-level, rather than at the micro-level. However, it would be desirable to bring out the chronological order of these practices briefly.

After World War II, and till the 1960s, 'Japanese management' was primarily characterized by the three concepts or the so-called "three pillars of imperial house of Japan", which are 'lifetime employment', 'seniority wage system' and 'enterprise unions'

and this was keeping in view the socio-cultural approach to Japanese management. The entire period of the 1970s saw more focus on labor management and industrial relations and hence the term ‘management by collective enterprise for the same’ got subsequently introduced in 1978<sup>1</sup>. Issues such as corporate social responsibilities got a stronghold in the same period and became a part of corporate ownership and management control (as evolved by *Noguchi et al* and *Iwata and Takahashi* in 1974).

The practice of mutual ownership of stocks by corporate bodies, and by ‘enterprise groups’ with banks and general trading companies at their core, and their role in business management generated enhanced interest in research into the managerial structure of Japanese companies. *Okumara* in 1975 evolved the theory of ‘corporate capitalism’ by making research into this practice and *Noguchi* subsequently supported the same.

By the 1980s the culture of Research and Development (R&D), production, purchase, sales, finance and business analysis were made as an integral part of running the business in Japan that gave rise to structural analysis of corporate control by management and enterprise groups. Administrative guidance from such bodies as MITI and other government bodies was so profuse that *Johnson* propagated *Japan Inc.* theory in 1982. From the mid 1980s Western nations started framing their own management styles on these Japanese practices particularly in the production system as a measure of recovery of their economies.

During 1980s, Japanese also started the practice of overseas expansion of markets and also manufacturing that these practices were taken to outside production bases in various countries irrespective of their own culture. The technology transfer or the production package engulfed all the policy matters such as personnel, organization, corporate objectives, management systems and other features making up Japanese management and inter-corporate systems, and, long-standing transaction practices and business connections. This phase was called as ‘universality’ by the economists as well as by the

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<sup>1</sup> Terms used by OECD in 1973 and 1978 respectively.

management experts.<sup>2</sup> The Japanese management practices were paid so much attention that there was a talk of virtual ‘Japanization of foreign management systems’.

In the mid-1980s, there have been more cases using subsystems (even if sometimes divorced from Japanese industrial relations and Japanese culture) of Japanese management, such as JIT (just-in-time) system, multi-skilled workforce system and quality control circles, as rationalization of management in foreign companies (*‘Meditative Japanization’*).

All elements of technology, labor, labor management and industrial relations are important a component of Japanese management systems, yet, there has not been much research either on the general theory on Japanese business management or its synchronization with labor theory of Japanese management.<sup>3</sup>

It was only in the 1990s that attention was paid to the opportunities extended out and the working conditions prevailing for the women workforce that came to be associated with the labor problems and the industrial relations. The anxiety for women was a part of the deepening concern for empowerment of women as a global issue and the social responsibilities of the corporate sector. The lack of equal participation of women in employment as well as management was perceived as some kind of backwardness of Japanese social system by the authors like Iwao, Watanabe and Wolferen<sup>4</sup>.

The late 1990s saw the significance of emerging IT in production, R&D, inventory control in the manufacturing sector as well as information processing. The strength of Japanese management was in automobiles, electrical and electronics, but other countries went far ahead due to their strength in IT. It was evident that the Western management

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<sup>2</sup> Hayashi, Masaki (2002), “A Historical Review of Japanese Management Theories: The Search for a General Theory of Management”, *Asian Business and Management*, Volume 1, pp 1-19.

<sup>3</sup> Ibid.

<sup>4</sup> Nonaka, I. and Takeuchi, H. (1996), *‘The Knowledge Creating Company’*, New York: Oxford University Press, U.K.

theory and methods; new management theories such as ‘competitive advantage strategy’, ‘re-engineering’, ‘virtual management’ and ‘knowledge management’ have overpowered the Japanese management practices.

If the Western theory of F. W. Taylor’s scientific management, divisional organization structure, and management and organization strategy of multinational corporations contributed in the past, the new concepts dating from around 1990, including lean production methods, re-engineering, knowledge management and supply-chain management have taken their cue from research on Japanese corporations, and so the contribution of the Japanese management can not be denied by any country in the world.

In that climate of heightened globalization and networking of information system, the Japanese management style took a backseat particularly when the recession was continuing. It was argued that although Japanese companies have until now achieved profit at the expense of their stakeholders, in order to coexist with foreign industrialized nations such as those of Europe and North America, systems that can only survive at the sacrifice of others must be reformed at the level of both idea and practice. Following this, bodies such as Federation of Economic Organizations (*Keidanren*) and the Japan Committee for Economic Development (*Keizai Doyukai*) came to the fore front and announced the need for concrete reforms in many of the prevailing practices such as employment, personnel, pay and corporate welfare while maintaining universal ideas such as ‘respect for human beings’ and ‘long-term oriented management’. This implied abolishing of the previously ‘gentleman’s promise’ of lifetime employment, and replacing the same by ‘principle of results and performance’.

Critical studies of the reforms have attracted attention, arguing that the introduction of the ‘principle of result and performance’ will mean even greater competition among workers, with a further sophistication of the individually oriented merit system which had already



changed from around the 1970s, with the aim of enhancing competition for the opportunity of education and promotion.<sup>5</sup>

### **Basic Features of the Japanese Management Practices**

European and American scholars coined the term ‘Japanese management practices’ after World War II when Japanese economy had a miracle recovery. Thus, the Japanese followed a principle called as *Wa Kon Yoh Sai*, which means “Japanese Spirit and Western Technology”. After World War II, East Asia was the only region of the world that experienced continual substantial economic growth and no other East Asian country enjoyed more economic growth and prosperity than Japan. International recognition was given to Japanese Management Practices when it reached its zenith in the 1980s. Further, in the same period Japan exported to the world such hi-tech products in electronics such as video recorders and facsimile machines, which only the Japanese were able to manufacture successfully. The West started recognizing the technological presence of Japan and started making in-depth study of the system behind such success.

The terminology ‘Management Practices’ depicts a complete system of working from the shop floor of the manufacturing units to the organization skills covering the policy matters of compensation to the workers for their work and innovation, the spread of the risk relating to the human and financial resources, the transfer of the skills from one organization to the other, interaction among the various interest groups, co-operation of the private sector with the regulating agencies that are essential for the economic growth. These practices cover Industrial Management system including the inventory and industrial relations, Human Resource Development and Corporate Governance. *Muda-dori* (time and resource management) highly valued among Japanese manufacturers, as a general paradigm under which waste, defined both in physical terms and in terms of time, is cut out of the production process became a popular practice in all the manufacturing

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<sup>5</sup> Refer to Masao, Inoue (June 2005), “What has Research into Japanese Industrial Relations Elucidated over 20 Years?” *Asian Business & Management*, Volume 4, Number 2, pp133-156 (23) and, Hasegawa, Keitaro (1987), *Japanese-Style Management: An Insider's Analysis*, Kodansha Publications, U.S.A.

units. It includes just-in-time (JIT or the *Kan Ban*) delivery of parts by both external and in-house suppliers. Japanese words such as ‘*kaizen*’<sup>6</sup>, and English phrases coined in Japan such as ‘Just in Time’ (JIT)<sup>7</sup> and ‘Total Quality Control’ (TQC), entered the world’s dictionary. Japanese companies began to carry increasing weight in the world economy and it continued to chalk up huge trade surpluses.

While a number of factors are said to be behind the Japanese success, Japanese Management Style was seen as distinct from the Western Style of Management and thus gained a stronghold amongst the researchers. The Japanese Management System is a general term for management practices or managerial styles commonly adopted by Japanese enterprises. Apart from being “Human Resource Centric” Japanese Management Techniques aimed at reducing costs of production through the economies of scale and also at “Low Price High Quality Products”. Further, apart from the cultural aspects embedded within the business, ‘Iron Triangle’ and ‘*Keiretsu*’ was seen as an effective tool to harness human resource. In the manufacturing units patronized by Japanese, *Jidoka*<sup>8</sup> (Autonomous quality assurance), *Shojinka* (Flexible work force)<sup>9</sup> and *Soikufu* (Creative thinking) became trendy practices.

The salient features of Industrial Management under Japanese Management Practices prevailing till 1990s are as follows<sup>10</sup>:

1. Lifetime Employment System (*Shushin Koyo*),
2. Seniority System of Wage and Promotions (*Nenko joretsu*),
3. Company/ Enterprise Unions (*Kigyo-betsu kumiai*),

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6 Means Continuous improvement that is possible through work organization, operating practices and new improvement opportunities.

7 A technique for the organization of work flows, to allow rapid, high quality flexible production while minimizing manufacturing waste and stock levels.

8 *Jidoka* (autonomation) is a framework of quality assurance. It recognizes the disruption and costs caused by defective units flowing on to subsequent processes and thus provides for an autonomous status to defect control. This means that every worker is vigilant about quality and has an autonomous power to stop the whole assembly line if necessary to prevent a defective unit flowing into good production

9 It implies (i) multi-process holding; and (ii) multi-skilled worker.

<sup>10</sup> Sai, Yasutaka. (1996), *The Eight Core Values of the Japanese Businessman: Toward an Understanding of Japanese Management*, Haworth Press, New York, U.S.A.

4. Communication through Quality Control Circle and Suggestion System (Individual Centered) and *Ringi* and *Nemawashi* (Managerial Communication); The *Ringi Sei* being formal method and *Nemawashi* being Informal method, and
5. Compensation Package (Wages and bonus System).

Life Time Employment System, Seniority based Wage Structure and Enterprise/ Company Unions are considered to be the three pillars of the Japanese Management upon which the whole corporate activities take place. The OECD (Organization for Economic Cooperation and Development) called these features the “Three Sacred Treasures of the Imperial House” of Japan that helped the country to be a phoenix.

#### **Lifetime Employment System (*Shushin Koyo*)**

It means that a person when becomes an employee of a particular firm (generally upon school graduation) is allowed to work for the company till the retirement age (typically between the age of 55 and 60), which was determined by the government. Japanese academic calendar runs from April through to March. Similarly, the fiscal year of most Japanese companies begins in April and ends in March. As a result, almost all the regular employees are recruited one time and join the company simultaneously in April.<sup>11</sup>

The company does not fire its employees except on the ground of serious misconduct and in return the company successfully gets the loyalty, commitment and hard work. A company invests good amount of money for the training of its employees considering that any other firm or competitor will not hire his employee. Further, once an employee reaches the age of retirement, he is usually re-hired again and hence he continues in the same company office or is transferred to another subsidiary though not in the same

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<sup>11</sup> Selmer, J. (June 2001), “Human resource management in Japan - Adjustment or transformation?”, *International Journal of Manpower*, vol. 22, no. 3, pp. 235-243(9)

position or with the same pay scale. Thus he can work with the same company as long as he lives. Thus the concept of Life Time Employment got coined with ‘virtual guarantee of job’.

An important dimension of the labor-management system of the typical Japanese consumer electronics factory is the stratification of production workers on the basis of the type of contract held with the firm. The lowest stratum of production workers consists of a group of fixed-term, contract (temporary) workers. Above the contract workers is a stratum of regular shop floor workers who are hired on a long-term basis (Kenney, 1995; Nakamura, Demes, & Nagano, 1994). The distinction between contract workers and regular workers influences the type of work performed, as well as wage levels. Contract workers tend to perform simple, routine assembly tasks requiring minimal skills and are paid relatively low wages, whereas regular workers are paid higher wages and perform higher level work tasks (Kenney, 1995; Nakamura et al., 1994). Even though they were officially defined as contract workers, these employees were relatively permanent workers in practice because their contracts were almost invariably renewed. Although assembly work was organized on the basis of teams, regular workers did not typically perform any assembly tasks. Instead, regular workers primarily engaged in supervisory and control duties. During this entire process, regular workers are receiving on-the-job training across a broad scope of work activities.

During this process, regular workers also tend to receive opportunities for off-the-job training, whereas contract workers do not. Off-the-job training represents a more substantial investment compared to on-the-job training because workers are not producing for the factory while they are getting the training. There are various levels of off-the-job training. First, there are plant-level training courses in robotics, integrated circuitry, and various other technical topics taught by senior factory personnel (Kenney, 1996). There are also company-wide training courses. Finally, there are courses offered by outside organizations. Overall, the training component for regular production workers plays a central role in preparing these employees for the internal job ladder.

The Japanese companies hire new graduates as general employees rather than as specialists. Then, the company gives a variety of internal education programs to train the new graduates. The in-house education can be divided into on-the-job training and off-the-job training. In order to cash in on increased seniority, employees work under a virtual "lifetime" incentive to perform satisfactorily and to acquire the additional training required for upgrading continuously their skills and capabilities. Japanese system permits training to be delivered to the individual in small increments and mainly on the job -- just in time for the employee to assume each new responsibility calling for additional skill otherwise. Since production workers in Japanese factories are trained for depth as well as breadth, management can involve the workers in decision-making on the shop floor and avoid the more rigid division of labor between supervision and operation and among workers generally found in factories in the western system. A versatile and deeply trained work force, thus, can produce the same output with fewer people than a work force of highly specialized workers. This system of Japan results in a lower fixed-cost liability to management.

The above concept of lifetime employment system reflects an era, which prevailed during years of high economic growth that began about 1955. It also reflects the social ideas generated by labor unions' resistance to mass dismissal during the preceding decade, as well as court decisions to restrict employers' right to dismissal due to business difficulties. Lifetime employment thus has been a long-established practice in large Japanese firms. However, it is a "gentlemen's agreement" and is not guaranteed by statute or collective bargaining agreement.

Although lifetime employment had some negative effects, it had in the past provided Japanese companies with workforce security. Guaranteed employment and a secure salary served to promote employee loyalty, thus protecting the significant investment companies pour into employee training. Employment security within the firm got converted into a source of employee efficiency and adaptability and also into a source of national economic stability. Throughout the course of employment, employees were also able to establish strong relationships with their colleagues and superiors, reinforcing a

sense of good management and harmony within the company. Lastly, workforce security and lack of employee turnover helped to ensure the confidentiality of company information transmitted to an employee.<sup>12</sup>

### **Seniority System of Wages and Promotions (*Nenko joretsu*)**

Rise in the salary of an employee runs parallel to the amount of his years spent (service) in the firm. This is subject to the age and level of education at the time of the entry. The wage can be divided into performance wage and life wage. The performance wage is rated as a result of individual performance. However, the performance wage often increases according to the length of service on the assumption that people gain ability along with the length of working. The life wage is rated in consideration of the changes in employee's life. This life wage also increases according to the years of service, because it is generally believed that the living cost will increase according to the years of service. The wages of an employee continues to accumulate according to the length of the service with only minor adjustments to reflect employee performance. Since Japanese Management Practices inculcate group harmony and fairness to all in the same group which is in sharp contrast to the Western Management Practices encouraging individualism, promotion of an employee cannot be considered in isolation, thus it is the group which progresses and quick or early promotions are not encouraged and rather taken as favoritism towards certain employees. This system of management results in the following: -

- Lack of clear demarcation between the white collar and blue-collar employee and the provision of a blue-collar employee having considerable chances of moving up into a white-collar job due to his abilities and caliber, and,

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<sup>12</sup> Benson, J.; Debroux, P. (2004), "The Changing Nature of Japanese Human Resource Management The Impact of the Recession and the Asian Financial Crisis", *International Studies of Management and Organization*, vol. 34, no. 1, pp. 32-51 and, Shiimizu, T. (October 2002), "The longevity of the Japanese big businesses", *Annals of Business Administrative Science*, Vol.1, No.3

- Only a very few, efficient and deserving make it to the board of directors.

However, it is important to point out that the traditional Japanese employment system was well suited to the building of a modern industrial society. It provided a stable and skilled resource base for manufacturers as they expanded production during the decades of strong economic growth prior to 1990. However, two key elements of the system—lifetime employment and seniority-based wages—functioned best in a growing economy as that of Japan in the past. Since the burst of the ‘bubble’ and the economic hardships that followed, the lifetime employment and seniority-based wages has proved to be extremely difficult to sustain in.

### **Company / Enterprise Unions (*Kigyo-betsu kumiai*)**

Japanese labor unions basically have a “triplicate structure.” That is, (1) enterprise labor unions organized at each business, (2) industrial trade unions organized as loose federations of enterprise union members gathered by industry, and (3) national centers (a typical example being the Japanese Trade Union Confederation) made up of the industry trade unions gathered at the national level.

Enterprise labor unions are Japan’s dominant form of labor organization because each enterprise union exercises labor’s three primary rights: the rights to organize, bargain collectively, and strike. Each enterprise union has most of the staff, funding, and other material necessary to exercise labor’s three primary rights. Labor unions play the role of maintaining and improving workers’ quality of life and working conditions. In order to do so, they engage in three primary activities: activities with management, activities within the unions, and activities outside the organization. First of all, as individual unions, enterprise unions maintain and improve working conditions and participate in management through collective bargaining and consultation with the management. Next, as for activities within the unions, enterprise unions not only deal with organizational operations but also provide their members with services through various kinds of mutual aid activities. Finally, when it comes to activities outside the organization, enterprise unions individually seek to provide benefits to their members by using their influence for

various policies on the regional, industrial, and national levels concerning employment and working conditions as well as quality of life of their members.

As a matter of fact these enterprise labor unions are geared towards harnessing only the permanent staff or the regular workers employed at the concerned companies and the peripheral employees are not included. The enterprise union is a mixed union organized as a single trade union for all permanent employees, without distinction between white-collar and blue-collar employees.

Industrial trade unions support their member unions' actions against business owners by consolidating requests concerning chief working conditions such as wages and working hours on the industrial level, collecting and providing information and basic material, and coordinating negotiation strategies. In terms of activities within the organization, industrial trade unions provide their members with a variety of services through mutual aid activities, including life insurance, pension, medical insurance etc. In addition, industrial trade unions participate in the decision-making processes of national industrial policies, consult with economic organizations and develop international cooperation among the labor unions.

National centers (mainly *Rengo*—the Japanese Trade Union Confederation) provide members with support for actions against business owners. The most important role played by them is their participation in the national policies. They also maintain cooperative relations with the various political parties.

The relationship between the company and the enterprise union is close and cordial. The Union functions at two levels: -

- '*Shunto*' or the spring wage offensive is a united campaign, mainly for higher wages, launched in each spring by labor unions for each industry. Established in 1955, the main aim behind its establishment was to compensate for enterprise unions' lack of bargaining power as individual entities and to distribute wage



increases proportionately across companies and industries through simultaneous wage negotiations. Taking the wage increase rate set by the top firm in a major industry (or pattern setter) as the standard, the influence on wage increases spreads to the other large companies in the concerned industry, followed by large firms in other industries, government agencies, medium- and small-scale businesses, and finally to workers who are not union members. Wage levels are thereby standardized nationwide. *Shunto*, the annual wage determinant process, represents a significant economy-wide mechanism that restrains inflationary wage pressures. Each year a pattern emerges from lead negotiations in a small group of major firms, which is then diffused through the remainder of the economy.

- Joint Consultative System where the top level management and the union meet to discuss a number of issues such as overseas expansion of the activities of the firm, adoption of the new technology, future plans of production, investment and manpower adjustment. It is at this level that some of the major decisions of the company are made and hence a conflict within the firm after a decision has been taken is avoided and time is saved along with the promotion of harmony within the firm. It is mainly due to this reason rarely we come across enterprise unions going on a strike against the top-level management.

#### **Communication within the Firm**

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Quality Control Circle is a group oriented and the suggestion system is individual centered where an individual drops his suggestions in the drop box and the best suggestion gets an award and certain other morale enhancing benefits. "*Ringi Sei*", a system of communication, is a bottom up communication where a proposal gets approved through vertical, horizontal and diagonal circulation of the proposal to the concerned members of the company. The very first idea comes from the person in charge of the project. He or she draws up the original plan for the project in a written form called *Ringi* i.e. circular. The plan is sent from manager to general managers, and then to top

executives for final approval. It consists of four steps viz proposal, circulation, approval and record.

“*Nemawashi*” on the other hand is an informal method of communication that helps immensely to arrive at a consensus. The negotiations take place informally through discussions at dinner or more likely at bars and nightclubs. In fact this is a more diplomatic way to get the opinions of the concerned employees about a proposal. “*Ringi Sei*” and “*Nemawashi*” work together to take a unanimous decision and hence are another example of participatory method of decision making to smoothen the process of implementation of a decision.

### **Compensation Package (Bonus)**

Regular Career progression is highly predictable, regulated, and automatic. Compensation for young workers is quite low, but they accept low pay with the understanding that their pay will increase in regular increments and be quite high by retirement. Compensation consists of a wide range of tangible and intangible benefits, including housing assistance, inexpensive vacations, good recreational facilities, and, most important, the availability of low-cost loans for such expenses as housing and a new automobile. Regular pay is often augmented by generous semiannual bonuses. Members of the same graduating class usually start with similar salaries, and salary increases and promotions each year are generally uniform. The purpose is to maintain harmony and avoid stress and jealousy within the group.

Japanese companies have traditionally paid their employees a 'divide-by-12' salary plus bonuses with 1/12th of annual salary paid on the 25th of each month and semi-annual 'summer' and 'winter' bonuses traditionally equivalent to 3-months salary (each) paid in June and December. In recent years Japan's economic recession had caused the summer and winter bonuses to reduce and many companies were paying their junior employees just 1-month salary in each bonus with some paying no bonus at all.

To Japanese employees that do receive summer and winter bonuses, especially at larger companies, the bonuses have become almost institutionalized and, though the bonuses are linked to the company's overall performance (no profits = no bonus), they are not linked to individual employee performance. An indication of the almost institutionalized nature of these Japanese employee bonuses is that until recently, Japan's welfare (state) insurance contribution rates were significantly less on bonuses than on regular monthly salary. Also, many Japanese mortgages are structured with relatively low monthly payments and larger summer and winter payments.

Bonus is given twice in a year and is looked forward to by the employees and is also seen as a symbol of profit making by the company. Also, the one time recruitment benefit is another feature of the compensation package. Many Japanese companies make little distinction between salespeople and other employees, so the 'guaranteed' bonuses are also paid to many Japanese salespeople unlike their counterparts in the U.S.

The socially sensitive culture of Japan is also reflected in its management practices. Under the traditional Japanese Management style the social and economic development are inter-related and so the profit motive does not take priority over the Human capital. Society, government, employees of both private and public sector are so much inter-dependent upon each other that sometime the Western Scholars sarcastically name the collective decisions relating to corporate governance as "Japan Inc." Japanese traditional values have been that society, government, employees or for that matters consumers of services or goods are not dependent on some particular business; rather business depends upon support from all the various sectors. This is possible only when the best potential of human element is utilized most effectively. Management skills and practices have to prove relevance to the society, which primarily consists of Human beings with potential of different nature and generates human capital as complementary to each other.

## Significance of HR department

A key element in the Japanese system was the value attached to HR department, which administered employment and labor relations. Among its myriad duties, the HR department was in charge of rotating managers around the company and winnowing out people for senior positions. HR was linked to corporate governance indirectly—by grooming people for the board of directors, comprised of management insiders—and directly through the board membership of the senior HR executive. HR headquarters for the senior managers was a place to network with other managers. It ranked about halfway down the list of functions that were precursors to a senior executive promotion—behind marketing but ahead of engineering, R&D, and others. On the company board, the HR executive voiced employee concerns to other executives and served as the advocate of the *seishain*—the career employees—in strategic decision-making.<sup>13</sup> Thus the HR function ranks high in the corporate hierarchy and influences strategic decisions related to executive careers and payroll allocation.

On the other hand in the USA, the senior HR executive traditionally was low and thus the function's low status was reflected by a relatively high proportion of women in HR positions and relatively low pay for HR executives. For the past fifty years or more, the powerhouse function of the U.S. Corporation has been finance. In the United States, HR continues to be a specialty more open to women than other executive functions.<sup>14</sup> 43 % percent of the HR executives are females. In traditional Japan, women did not receive many opportunities – economic or otherwise. While they did hold a special place in the privacy of the home yet they were not given importance in the corporate world.

As Japan moved into the phase of economic growth of 1980s, women's education in all spheres witnessed a sharp increase. Japan signed the United Nations Declaration on Women and consequently passed the 1986 Equal Employment Opportunity Law that opened more job opportunities to women. The Equal Opportunity Act on becoming law

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<sup>13</sup> Ibid.

<sup>14</sup> Ibid.

contained provisions that companies must voluntarily endeavor to not discriminate in recruiting, hiring, assignments, and promotion. The law also had provisions to prohibit discrimination in retirement, dismissal, fringe benefits, and training. To comply with the principle of this law, companies created a two-track system and women were employed virtually in every field. One track (*sougoushoku*) led to possible managerial positions and, the other track (*ippanshoku*) to routine work with limited promotion potential. In theory both men and women had equal opportunities in both the tracks. Further, hiring decisions had to be made by educational and other work-related criteria, and not gender. However, in practice the majority of women were in routine work and virtually all men on the *sougoushoku* track. The law, however, was merely advisory in nature: It had no penalties for non-compliance and no affirmative action components. The prohibition on late night work for women and other protective legislation remained in effect.<sup>15</sup> The situation today more or less remains the same and hence senior management—regardless of function—is still an all-male preserve. Women, in Japan, account for only 8.2 % of corporate managers.

### **Other features of the Japanese Human Resource Management**

The other characteristics of the Japanese HR practices have been listed as follows:

#### **Employee Welfare Programs**

Another feature of the Japanese Management System is an emphasis on employee welfare programs. Many Japanese companies provide a wide range of fringe benefits and welfare programs for employees. Many companies have hotels, sanitariums or accommodation facilities in health resorts in order for employees to enjoy their vacation. Further, benefits are also provided for recreation and leisure activities, such as athletic competitions, employee excursions, and so on. Employees also have access to the facilities for hobbies, including sports, reading, and board games. As for other benefits, companies offer special

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<sup>15</sup> Please refer to: Brinton, Mary C. (1993), "*Women and the Economic Miracle: Gender and Work in Postwar Japan*", Berkeley and Los Angeles: University of California Press.

allowances in addition to the basic salary, company-owned housing, dormitories for single workers, and various health benefits.

Most employers enroll their workers in the Employer's Health Plan (*shakai hoken*). Under this system, insured employees pay approximately 10% of the cost for medical services, dental treatment, and medicines, while their dependents are charged approximately 30% of the cost of outpatient services and 20% of inpatient or hospitalization service costs. Under this plan, the employer and employee contribute each contribute 50% of the monthly premium, with the employee's share deducted from payroll.

### **Involvement and Motivation**

Quality control circles (QC circles) are small group activities in which, typically, assembly line workers share ideas about how to solve minor problems on their lines, gathering data from the line that can be analyzed using simple statistical techniques tests ideas. "Circles" are based on the intuitive logic that a worker who is thinking could probably make valuable suggestions regarding how to work more productively. In the process of participating in circles, workers are assumed to become more interested in their jobs and more committed to their colleagues and the company. While there are variations in Japan, QC circles regularly meet once or twice a week near the shop -floor, after work, for 30-40 minutes. Workers are not paid for their participation.

Collective or Family-oriented Culture: Some scholars or analysts stress that the cultural aspect of Japanese society is a key to success of Japanese Management System. Japanese society is very homogeneous. Japanese are generally collective and family-oriented. They prefer group-oriented Management to individual leadership. Japanese think that the company belongs to its employees. Thus, Japanese corporate Paternalism is itself a fairly advanced concept in study of Japanese Management Practices.

## **‘Diamond Structure’ of the Japanese Management Practices**

The phrase ‘Diamond Structure’ of the Japanese Management Practices means that the practices are so well knitted with each other and are so interrelated that the entire system has the potential to collapse even if one of the characteristic is missing from the Japanese society.

All of the characteristics work effectively on the condition of lifetime employment. Seniority system is based on the assumption that employees' ability will increase along with the length of service and experience. In-house education also depends on the lifelong employment because the company can gain the benefit of education only when employees work for a long time. Enterprise union is necessary when people work for only one company. One-time recruitment is the other side of lifetime employment. The importance of employee welfare programs is obvious if the employee works within a company for a long time. The other characteristics such as bottom-up decision making system and family-oriented management are the results of lifetime employment. In addition to high levels of coordination between business and government, Japan distinguished itself for having a mode of corporate governance that balanced different stakeholders—shareholders, customers, banks, and employees—rather than, giving exclusivity to shareholders.<sup>16</sup>

## **Economic Recession and the Burst of the ‘Bubble Economy’**

The bubble started because of the enormous amount of liquidity available to borrowers implicit in very low interest rates. The structure of the ensuing bubble basically revolved around the practice of using the rising value of property as collateral for speculative borrowing. Much of this speculation was directed towards equity and property markets, thus intensifying the process of borrowing and speculation. Valuations in these markets reached staggering levels; at the height of the bubble Japanese real estate represented one

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16 M. Jacoby, Sanford and Saguchi, Kazuro (December 2002), “The Role of the Senior HR Executive in Japan and the United States: Companies, Countries, and Convergence”, For the 13th World Congress of the International Industrial Relations Association (IIRA), Berlin, September 2003.

third of all wealth in the world and the capitalized value of the stock market stood at 42% of world stock market value.

Japan's GDP shrank 5.3% during the first quarter of 1998 and unemployment reached a new high of 4.1% in April 1998. Japanese banks are burdened with over \$500 billion in bad loans.<sup>17</sup> In particular, the bankruptcy of a major city bank, *Hokkaido Takushoku* Bank, and dissolution of a big four securities firm, *Yamaichi* Securities, shocked the Japanese public. From 1981 to 1991, Japan recorded an annual growth rate of about 4% in its real GDP. By contrast, the average growth from 1992 to 2001 was less than 1% (0.9% to be precise).<sup>18</sup> Thus, while the pace of the economy was remarkably brisk in the earlier period, it remained practically at a standstill during the latter years. The recent slowdown was so marked that it forged a view that the last ten years of the 20<sup>th</sup> century was a lost decade for the Japanese economy.<sup>19</sup>

A recession, as termed by the National Bureau of Economic Research, of USA is “a significant decline in activity spread across the economy, lasting more than a few months, visible in industrial production, employment, real income and wholesale-retail trade.”

Economists had plenty of theories about why the Japanese business cycle had flattened such as Cheap credit and inflated profit expectations causing both over investment and “mal investment” in the wrong kind of capital i.e. the mismatch between saving and investment, or in terms of real business theory in terms of productivity shocks or, strangely enough, even the policy mistakes. Obviously it was disappointing not only in

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<sup>17</sup> [Online Web] URL <http://www.pacificbridge.com/Publications/JapanFall98.htm> downloaded on 5th Dec.2005

<sup>18</sup> [Online Web] URL <http://www.tcd.ie/Economics/SER/archive/1999/essay16.html> Accessed on 7th December 2005.

<sup>19</sup> Keunho Lee (2003), “An Alternative view of Japanese Economic Slowdown”, Northern State University, Aberdeen, South Dakota, Prepared for the Western Economic Association International meeting of January 9-12, 2003, Taipei, Taiwan, [Online: Web], Accessed on 26th August 2005, URL <http://www.northern.edu/ois/Japan9.htm> And, Ribault, T (ed) (1999), *Japanese Management in the Low Growth Era: Between External Shocks and Internal Evolution*, Secaucus Publishers, Germany



comparison to other advanced economies, such as the United States and the European countries, but also in relation to its own past.

One of the major reasons for the economic slowdown has been the high savings rate. When a boost of consumer spending was greatly needed in the aftermath of the asset bubbles, it was argued that the high savings rate held it in check, leading the economy downhill in subsequent years. Further, The less-than-sound lending practices of Japanese banks, namely the high debt-equity ratio factored in lending, is another reason for the economic slump. Generous debt-equity ratio is a useful leverage in normal circumstances but a highly risky one in abnormal environment. In a competitive market and in a risky environment the result was that the banks were paralyzed with bad debts, leading to a virtual financial disaster in the entire economy. Also, the financial crisis in Asia a few years later delivered another blow to the banking sector, undermining its ability further. Modern monetary economy is founded on financial intermediation. Since banks are the primary agents for it, a healthy banking sector is an essential ingredient for a healthy economy. Thus the collapse of the banking sector has been one of the major reasons for the economic slowdown. The hesitation of the Ministry of Finance to respond quickly to the changing situation has also been cited as one of the instances that have added to Japan's problems. However Japanese economy remained the second largest in the World despite such recession and a simultaneous wave of overseas investments of large magnitude made Japan emerge as the world's largest creditor nation by the end of that 'lost decade'.

Due to the collapse of major financial institutions, the Asian currency crisis and decreased consumer demand, Japan's economy has struggled since the early 1990's. However, Japan experienced a mild recovery period in 2003 with a 2.7% GDP. Nevertheless several economic reports released at the end of 2004 show that the country's economy is once again on the decline with a decrease in industrial output, increase in the unemployment rate, and decline in household spending. The struggling industrial sector has led to an increase in the country's unemployment rate. In 1999, the numbers of people according to the BBC report were estimated to be at around 3.42

million, at the unemployment rate stood at 4.8%, highest since records began in 1953.<sup>20</sup> According to the CIA world fact book, the rate of unemployment stood at 5.4%.

Economic, social and cultural changes have affected the Japanese Management System today. A decade-long economic recession has compelled both the Japanese Government and the corporate sector for review of the traditional practices from all angles such as intervention by the Government through the corporate governance so as to sustain the economy. The social and demographic changes, that is, a falling birthrate and the ageing of the population have also made it more difficult for the Japanese companies to maintain the traditional organization hierarchy. Thirdly, the System was affected by the change in the life style and value of especially younger generations and that of women that want to change their jobs more frequently.

In the past few years, there have been some articles and books written on the related subject. For instance, *“Japanese Labour and Management in Transition: Diversity, Flexibility and Participation”<sup>21</sup>* edited by Mari Sako and Hiroki Sato explores the changing face of Japanese industrial relations. It not only outlines recent trends in Japanese labor markets, labor law and corporate strategy, and explores the responses of both management and labor to pressure posed by these trends, but also, analyses the interaction between the state, management and labor, considering both the macro and the micro levels. It focuses on specific categories of labor such as: white collar workers; women workers; foreign workers; and older workers. Topics such as the public sector and privatization; collective bargaining and joint consultation; and labor-management relations in small firms have been included to throw light on the plethora of the changes taking place in the Japanese management practices.

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<sup>20</sup> “The Record Unemployment Rate in Japan”, Business Economy, [Online: Web], Accessed on 12<sup>th</sup> September 2005, URL [http://news.bbc.co.uk/1/hi/business/the\\_economy/357780.stm](http://news.bbc.co.uk/1/hi/business/the_economy/357780.stm)

<sup>21</sup> Sako, Mari and Sato, Hiroki (1997), *“Japanese Labour and Management in Transition: Diversity, Flexibility and Participation”*, Routledge Publishers, London, United Kingdom.

***“Japanese Management: In Search of a New Balance Between Continuity and Change<sup>22</sup>”***, edited by Rene Haak and Markus Pudelko analyzes the degree to which the Japanese management model is changing in order to regain its competitiveness. A broad variety of management areas such as strategy, corporate governance, globalization, organization, finance, HRM, production, innovation, organizational learning and retailing are covered.

***“The Changing Face of Japanese Management<sup>23</sup>”***, by Keith Jackson although presents that Japanese companies are likely to remain as a dominant global player for at least another human generation, but brings out a very disappointing picture of the present due to the ongoing changes and the insecurities directly related to it about the future. The changes that have been accounted are changes in terms of expectations of lifelong employment and of loyalty as expressed in a 'social contract' with politicians and families and a 'psychological contract' with employers. The authors brings out a direct correlation between the continuing changes in the HR practices on the university or college graduates seeking employment, middle-level managers seeking promotion, and the women managers at all stages of their career. Working mainly with interview material, the book gives 'voice' to managers whose task it is to interpret changes in the Japanese working environment and implement change in the workplace.

Another book that highlights the changes brought about in the changed management practices is the ***“Japanese Business Management; Restructuring for Low Growth and Globalisation<sup>24</sup>”***, by Glenn D. Hook. The areas covered include the changes made in management itself inside Japan and also how it is adapting itself when transferred overseas. There are also chapters on the formation of regional markets, technology transfer, the subcontracting system, ownership, work practices and industrial relations. In

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<sup>22</sup> Haak, Rene and Pudelko, Markus (2006), *“Japanese Management: In Search of a New Balance Between Continuity and Change”*, Palgrave Macmillan Publishers, U.S.A.

<sup>23</sup> Jackson, Keith (2003), *“The Changing Face of Japanese Management”*, Routledge Publishers, United Kingdom.

<sup>24</sup> Hook, D Glenn (1997), *“Japanese Business Management; Restructuring for Low Growth and Globalisation”*, Sheffield Center for Japanese Studies, Routledge Publishers, London, United Kingdom.

a nutshell, this book explains as to how traditional Japanese-style management is responding to changes.

***“The Japanese Finance: Corporate Finance and Capital Markets in Changing Japan<sup>25</sup>”*** by J.J.Choi and T.Hiraki, gives an elaborate account of the various aspects of the Japanese finance and the changes brought hitherto in its twenty-one papers. The corporate finance structures of Japan and the West have been compared and this can be seen as a comparative study for the corporate governance.

***“The Kyoto Model: The Challenge of Japanese Management Strategy Meeting Global Standards<sup>26</sup>”*** focuses on the Kyoto high tech companies that have captured the leading market share with globally preeminent technologies and yet have been able to maintain their robust profitability even under the ongoing current economic recession. It includes the case studies of the management systems of *Kyocera Corp.*, *Omron Corp.*, *Murata Manufacturing Co.*, *Rohm Co.* and *Horiba Ltd.* It emphasizes upon their management attitude giving priority to corporate philosophies, their organizational management, the emphasis they put on R&D management and production technologies, their personnel management, and finally, their philanthropic activities.

Since Japan’s Human Resource Practices played a central role in the strong economic growth that the country achieved in the second half of the 20th century, a change in the economic conditions brought about by the recession has had a considerable impact not only on the Japanese management practices, but also on the corporate governance system. How have both the practices changed and what are their further implications is what this study proposes to attempt.

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<sup>25</sup> Choi, J.J and Hiraki T. (2003), *“The Japanese Finance: Corporate Finance and Capital Markets in Changing Japan”*, J.A.I. Publishers, Elsevier Ltd, United Kingdom.

<sup>26</sup> Ishikawa, Akira and Tanaka, Koji (2005), *“The Kyoto Model: The Challenge of Japanese Management Strategy Meeting Global Standards”*, World Scientific Publishing Company, European Union.

## CHAPTER 2

### HUMAN RESOURCE STRATEGIES AND EMPLOYMENT RELATIONS

The weak aggregate demand for labor in the 1990's is a result of the languishing macro economy. The languishing macro economy was not caused by what structural problems may have existed in the labor market. Instead, it resulted from weak aggregate demand for final products and the slow progress in structural reforms in various sectors of the economy. The lack of convincing progress in structural reforms helped perpetuate the pessimistic assessment of the future of the Japanese economy, thereby discouraging investment in both physical and human capital. Thus, the growth of employment has become less and less responsive to upward swings in the economy.

#### **Traditionalism Versus Modern Day Changes**

Flexibility and adaptability broadly speaking have become key management concepts to develop a sustainable competitive advantage, and successful firms apply them in new organizational strategies that put into question many conventional tenets on organizations and their management. Nowhere was the shift more noticeable than in Japan, a country that served as a model for a struggling U.S. economy in the 1980s and yet again in the 1990s set an example for other countries in region and throughout the globe. A key element in the Japanese system was the Human Resource Department, which administered employment and labor relations. Among its myriad duties, the Human Resource Department was in charge of rotating managers around the company and winnowing out people for senior positions. Human Resource was linked to corporate governance indirectly — by grooming people for the board of directors, comprised of management insiders — and directly through the board membership of the senior Human Resource executive.<sup>1</sup>

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<sup>1</sup> Whitehill, Arthur M. (1992), *Japanese Management: Tradition and Transition*, Routledge Publishers, London, UK.

For the traditional employment practices to be economically rational, certain conditions are required: (1) the age structure of the work force must form a neat pyramid; (2) there must be expectations of steady future growth; and finally, (3) the industrial structure must be stable, making it unnecessary to hastily reallocate labor resources across companies.

Since the 1990s, the environment has changed substantially. (1) Japan's low birth rate and population-aging trends have become more pronounced. (2) Under the influence of these trends, expectations of steady future growth have been eroded and finally, (3) The expansion of other East Asian countries' capacity to supply a wide variety of goods (globalization) and rapid advances in information and communications technologies have raised the pace of change in both the industrial structure and the technologies that generate profits. These kinds of changes in the environment have severely undermined the rationale both for seniority-based wage profiles, which were backed by accumulated firm-specific labor skills, and for long-term employment, which had difficulties in responding to changes in the economic environment. As a result, it is natural that in recent years companies have looked to reduce excess seniority-based wages paid to middle-aged and older workers, and have tried to construct a more flexible employment system. Further change is also because of the pressure on the companies to meet the global standards and thus emphasize more on profitability than ever before. When the balance sheets of the firm started showing reduced profits and even increased debts and other liabilities rather than assets, firms in order to adjust their balance sheets restructured their wages given to the employees.<sup>2</sup>

With the bursting of the economic bubble in the late 1980s and early 1990s, the economy has alternated between periods of recession and extremely low rates of economic growth. For an economy based on and accustomed to high growth, this economic downturn had a serious effect on employment. In 1995, regular employment fell for the first time in

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<sup>2</sup> Watson, D.R.; Sallot, L.M. (Winter 2001), "Public relations practice in Japan - an exploratory study", *Public Relations Review*, vol. 27, no. 4, pp. 389-402. and, Inagami, T and Whittaker D.H. (2005), *The New Community Firm: Employment, Governance and Management Reform in Japan*, Cambridge University Press, UK.

twenty years, and in manufacturing, there was a fall of 1.9 percent from the previous year (Ministry of Labor 1996). Unemployment, which was 2.1 percent in 1991, had risen to 5.3 percent by 2003. In the latter part of the 1990s, much of Asia was affected by what has now become known as the Asian financial crisis. The crisis though initially started in Thailand, swiftly spread to other Asian countries, including Indonesia, Malaysia, Taiwan, Hong Kong, Philippines, and Korea. Many Japanese companies were hard hit as sales of consumer products fell and orders for Japanese capital goods declined.<sup>3</sup>

Although the financial crisis had a severe impact on many of the Asian economies at that time, by 2002 most of these economies had recovered. This was not the case for Japan. A series of financial scandals in the latter part of the 1990s, an increase of 67 percent in the consumption tax in 1997, and a decrease in public spending added to the economic difficulties facing Japan.<sup>4</sup> Thus, an environment was set in the initial years of the recession for bringing about changes in the Human Resource strategies so as to make up for the company's losses.

K. Fazekas and É. Ozsvald in their study titled, "The Triple Segmentation of the Japanese Labor Market: The Impact of Structural Changes on Rising Unemployment and Increasing Elasticity"<sup>5</sup>, have compartmentalized the workers into two major groups and a further division has been made to bring into our consideration that section which is hardly hit by the structural changes because of their traditional practices which they have been following since the good old days of the bubble economy. According to their findings only a very small inefficient workers belonging to the white collared jobs have been

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3 Benson John and Debroux Philippe (Spring 2004), "The Changing Nature of Japanese Human Resource Management: Impact of the Recession and the Asian Financial Crisis", *International Studies of Management and Organization*, Volume 34, Number 1, pp 32-51, M.E. Sharpe, Inc.

4 Ibid.

5 Fazekas, K. and Ozsvald, É, (2001), "The Triple Segmentation of the Japanese Labor Market: The Impact of Structural Changes on Rising Unemployment and Increasing Elasticity", Presented at the Conference of the European Network on the Japanese Economy "Recent Economic Issues in Japan and in Europe", 17/18 March 2001, at the University of Oxford.

affected due to the structural changes brought about in the background of the economic recession of the 1990s.

The prevalent literature, according to them, on the Japanese labor market structure follows a dual segmentation of the employed population. In most cases two groups are distinguished: the group of **core workers**, which includes the regular full time male employees of large firms and the group of **peripheral workers**, i.e. employees of small and medium size firms, female employees, part-time and contract workers, self employed and family workers. It is a well-known fact that the core workers in the Japanese system have a very low probability of the job loss. In the relatively rare cases of separation they can and they do easily switch to another job, i.e. they have also a very low probability of unemployment and the eventually unemployed core workers have shorter than average duration of unemployment. Also, the main characteristics of the Japanese employment practices such as the seniority-based wages, on-the-job training and various forms of employment protection apply mostly to this group. A very small percentage of the ‘core workers’ who are examples of the rising unemployment relate to the category who had in the past not shown any performance and hence took their jobs for granted in the background of the ‘Life Time Employment System’ during the sunny days of the bubble economy. Thus, only the redundant ‘core workers’ were stripped off their jobs.

Peripheral workers, on the other hand, have significantly higher probability of job loss, higher probability and longer than average duration of unemployment. These sections of the workers are the carriers of the flexibility of the Japanese system and who were not in the focus of governmental protection. The majority of Japan’s working population belongs to this group.

Following this dual segmentation it could have been easily argued that the rising unemployment rates were at least partially due to the decreasing share of the core workers in the total employed labor force. Labor Force Surveys however, do not support this hypothesis: Until as late as 1999, the percentage of core workers remained the same as it was in the previous decades. The authors for their convenience in the study have



further divided the Peripheral Workers into Peripheral I (all employees of small and medium size enterprises, female employees of large enterprises, part-time, male employees of large enterprises and part-time government employees) and Peripheral II workers (persons employed in agriculture, forestry and all self-employed and employed and family workers outside of agriculture). The higher the share of “peripheral I.” group on the labor market, the higher the flexibility of adjustment to fluctuation of production and the greater the chances of the separated workforce to become and remain unemployed. This means that the changing ratio of peripheral peripheral II groups and I influences the level of the unemployment rate. The table given below highlights the triple segmentation of the Japanese employed labor force.

**Triple segmentation of the Japanese employed labor force:**

| Core workers  | Peripheral I   | Peripheral II   |
|---|--|---|
| <ul style="list-style-type: none"> <li>• Male, full time employees of large enterprises in non-agricultural industries.</li> <li>• Full time government employees.</li> </ul> | <ul style="list-style-type: none"> <li>• Part time employees of large enterprises in non-agricultural industries.</li> <li>• Female employees of large enterprises in non-agricultural industries.</li> <li>• All employees of small and medium size enterprises in non-agricultural industries.</li> <li>• Part time government employees.</li> </ul> | <ul style="list-style-type: none"> <li>• All employed persons in agriculture and forestry</li> <li>• Self employed in non-agricultural industries.</li> <li>• Family workers in non-agricultural industries.</li> </ul> |

The common characteristic of the peripheral II workers is that the probability of becoming unemployed - similarly to core workers - is quite low. It is not that the peripheral II workers cannot lose their job. What is important here is that after separation they usually do not become unemployed! The traditional behavior of the members of this group after separation is the shift from employment to non-participation. The next table highlights the chances and probabilities of job loss within the three sectors of the workers.

**Probabilities of job loss and unemployment of the three segments:**

| Three segments | Job loss        | Unemployment    |
|----------------|-----------------|-----------------|
| Core workers   | Extremely low   | Extremely low   |
| Peripheral I.  | Relatively high | Relatively high |
| Peripheral II. | Relatively low  | Relatively low  |

The writers conclude in their study that there are hardly any changes in the group of the 'core workers' and all that is being talked about the rising unemployment is due to the above groups. Further, they also hold the view that there are regional differences in the unemployment rate since the core workers are more concentrated in the cities such as Tokyo, etc, where the unemployment rate is low as compared to the gloomy situation in the areas where people belong to the job brackets of Peripheral I and Peripheral II group.

Further, the writers opine that since the changing role and behavior of women and their effect on the unemployment rate were pointed out by Japanese researchers already in the eighties, the long overdue emancipation of Japanese women, their growing educational levels and economic necessity make it very probable that the size of the group of discouraged female workers will shrink further and thus contributing to the increase of

the unemployment rate. Thus, In Japan long-term structural shifts and the changing behavior of certain groups resulted in an increased participation in unemployment.

Since the mid-1990s, wages have also become somewhat more sensitive to economic fluctuations. The high flexibility of wages has been largely attributed to the fact that bonuses, which are highly flexible, make up a significant proportion of total earnings. In the past, the workers usually remained in the parent company till their age of retirement (60 years) and after the retirement the latter got employed in a different branch of the same company or some sister company usually with a little decrease in the wage level. With the continuing changes in the demographic system and the expansion of the life span of an individual with the increase in the number of young people who seek jobs it has really become an uphill task to manage the senior employees in different branches or sister companies with regular wages and on the other hand recruit comfortably i.e. the same number which used to be present in the past. Moreover, the larger the firm, the greater the problem.<sup>6</sup>

### **Laying off the Inefficient Workers after the recession**

The reform, which is still underway, is usually called as “the introduction of the results-based evaluation and wage system (*jitsuryoku-shugi, seika-shugi jinji seido no dōnyū*).” The reform movement has been driven by employers’ recognition on the financial concern and the necessity of new skills reflecting the liberalization pressure and the industrial structural change as major environmental changes. The above mentioned reform system stands in sharp contrast from the seniority based wage and long term employment and consequently bring about more flexible and market oriented forms of employment relations. It seeks to tight-couple wage and performance. By giving employees more responsibility on work results, company is able to achieve more flexible financial structure. Further, it is possible to point out the diversification of the workforce,

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<sup>6</sup> Bai, Gao, (2001), *Japan's Economic Dilemma: The Institutional Origins of Prosperity and Stagnation*, Cambridge University Press, UK. And, Schmidt, R.J. (March 1996), “Japanese management, recession style”, *Business Horizons*. vol. 39, no. 2, pp. 70-76

by which the organization further clarifies the expectations concerning the acquisition of the necessary skills. To achieve the above two objectives simultaneously, the personnel evaluation system tends to be more “objective” based on the detailed report specification, and not on the occupational specification within the organization.

### **Increasing Meritocracy**

The above has been achieved by introducing the concept of “meritocracy” in their management practices which implies that only those efficient workers would be kept in the company who contribute substantially and do not take the traditional management practice of promotions and increase in wage in accordance with the seniority for granted. For this an annual progress of each individual worker is taken into account. The result is what is termed “out of turn” promotions. This has further resulted in the decline of the motivational level of the workers who on the non-fulfillment of the expectation of promotions out of seniority have reduced considerably the very bit they used to perform. In about a third of workplaces, such “out of turn promotions” are claimed to be an “every day” or “frequent” occurrence, are seen with a raised eyebrow, and on the other hand the company has reduced to a considerable extent the number of the recruitment senior employees in different branches upon retirement. Further, in recent years many companies have shifted away from seniority based wage systems, which inflated wages especially for managers, and moved toward annual salary systems. Japan’s seniority-based wage system in conjunction with the aging of its workforce has conspired to exacerbate the problems of higher wages inherent in its employment structure.

More extreme still, major companies started announcing large-scale redundancies as part of their plans to restructure. Some of these redundancies were even "involuntary". In other cases, early retirement opportunities were introduced, offering enhanced early pensions or lump sum severance payments, sometimes to workers as young as fifty years. Recently, the incidence of such “non-Japanese” practices has appeared only to grow. The new managements, that were put in place they were not Japanese, as they laid workers off and, in particular, they operated early retirement programmes. And where they do, take

up has been high. Further, companies are seeking to reduce the number of sub-contracting companies and to enforce greater efficiency upon them and even to source from abroad. In such a case, the small firm sector is particularly threatened by attempts to force the banking sector to reduce bad loans – and their position is made yet weaker by the withdrawal of contracts by the large private firms. Thus, the number of bankruptcies has been rising. Small and medium size firms have been hit twice over – both because the banks were putting their finances under greater scrutiny and because parent companies were seeking to extricate themselves from debt at the expense of sacrificing poorly performing subsidiaries.

Laying off the excess workers have also been achieved by the merger of two-three firms by their respective managements and then finally slashing the number of workers employed to a considerable amount. For example, in the year 2000, *Sanwa* Bank, *Tokai* Bank and *Asahi* Bank announced their merger with one another and decided to reduce 10,000 jobs or 26.6 percent of their combined 37,583-strong domestic workforce.

The downsizing is being accompanied by speed-ups, and excessive workloads—a situation presided over by the unions. These chronic conditions are summed up in a new word that has been added to the Japanese vocabulary— *karoshi*, which literally means death by overwork.

Further, in a number of cases, stress and physical trauma have caused mental disorders as well as triggered heart and other diseases. Another chilling addition to the vocabulary is *karo-jisatsu*, meaning suicide induced by overwork. In 2000, Japan's Supreme Court recognized the *karo-jisatsu* phenomenon. It found that advertising firm *Dentsu* had caused the death of one of its young employees *Ichiro Oshima* by pushing him to work an excessive number of hours, leading to stress and then suicide.

The laying off plans hasn't been easy for the large companies since the newspapers have. Such continuously highlighted these concerns with heart-rending series on downsized employees and their struggle to retain their dignity and economic status while the Elite business organizations called for a new era of "flexibility" in employment. Further,

downsizing in Japan in the 1990's directly threatened the legitimate system of permanent employment. A firm that downsized and signaled to willingness to break with long-held implicit contracts of permanent employment was perceived to be a "bad company" that had neglected its social responsibilities. Such antisocial behavior threatened a firm's reputation with new employees and endangered future hiring prospects.

An alternative to various downsizing techniques has been to 'freeze the hiring activity' of a firm. While employers may have viewed hiring cuts as a means to protect the jobs of existing employees, hiring freezes were nevertheless threats to the permanent employment system in several ways. A hiring freeze meant a gaping hole in a firm's age and promotion hierarchy and threatened the structure of age-based wage and promotion at the foundation of the permanent employment system.

A succession of "deregulation plans" between 1993 and 1996 were intended to facilitate the opening of large supermarkets and department stores – the development of which had been impeded by local governments seeking to protect the livelihoods of small traders – and the breakdown of monopolies in the whole-selling sector – over which domestic manufacturers had an effective stranglehold.

Also, many manufacturing industries, especially those subject to intensifying competition from East Asia, have reduced the number of unskilled workers they employ and have shifted production of low-value-added goods overseas. This has resulted in the decrease of the economic value of unskilled workers, of whom non-manufacturers make greater use than manufacturers. Their wages as a result has headed downwards as supply-demand conditions have become significantly loosened. Also, wages for production workers in manufacturing industries have been weakening in recent years relative to those for non-production workers. This implies that in manufacturing industries, price competition with East Asia has exerted relatively strong downward pressure on wages for production workers, among whom the proportion of unskilled workers is seemingly high. Japan's future employment and wage situation will depend on how the economy evolves and the extent to which new job creation spreads throughout the economy.

In the pre-recession Japan, the labor market functioned perfectly in accordance with the demographic factors. Since the working age population tripled, the seniority-based pay system was in accordance with the structure of the population. The number of older people was relatively small and was in line with the limited number of managerial positions. Further, women participated in the blue collared jobs due to the ‘M’ shaped<sup>7</sup> curve and seldom had aspirations for the managerial posts in the companies. Further, There was an ample supply of young people available to perform the day-to-day operational tasks.

Changes in the Japanese business environment have raised a number of different challenges for management in dealing with their human resources. An aging society, ever widening forms of workforce diversity (particularly employment patterns, generational and gender based), the “Information Technology (IT) revolution,” and globalization are the factors included apart from the 1990s economic recession that have ushered in a series of changes in the traditional employment practices of Japan. The pressure on the Human Resource Department has been to adopt market oriented employment practices that would visibly weaken the traditional Human Resource Department of the Japanese corporations. Some companies for example, have gone for a complete restructuring, such as, Daiwa securities, which in 1998-1999 changed its pay system and by abolishing its seniority system effectively replaced it with the merit based pay structure. Also, further changes have been brought about in the company’s retirement system. Another example could be that of Itochu Corp., a huge Japanese trading company that also revamped its salary structure, providing incentives for exceptional workers. There is no dearth of such example changes, which have already taken place and are taking place because the recession has been too prolonged to wait for sunny days again.

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<sup>7</sup> A typical M-shaped Curve in the figure of the ‘Percentages of Women Workers by Age’ indicates a considerable number of workingwomen leave their jobs between the ages of 25 and 35. The curve ascends to the mid twenties, descends in the early thirties, and swings steadily upward to the late forties, when it finally begins to decline. Sugimoto, Yoshio (1997) *An Introduction to Japanese Society*, p.144.

## **HRM Practices and the Economics at Work**

Links between these environmental factors and HRM systems form the framework within which a new strategic model of HRM is being developed, and a uniquely individual corporate culture is being finally built, for large scale companies in Japan. The final aim of bringing changes in the employment relations is to achieve strategic goals of the company apart from harnessing the human resource talent available with the same.

According to John Benson and Philippe Debroux,<sup>8</sup> the HRM structure of any company consists of the following three tiers given below and the ability to distinguish between the various levels of change is important as it allows for a more refined and considered analysis to be undertaken: --

1. The system architecture or the basic principles and assumptions underpinning HRM;
2. Policies or the guiding principles of HRM; and
3. Practices or the day-to-day strategies designed to achieve the HRM policies.

Since, reform in the existing HRM practices generally require the introduction of supporting mechanisms, such as processes and criteria for measuring individual performance, it is likely that the practice will be modified or disbanded if these conditions are not met And, thus comes into play the increasing role of meritocracy in the Japanese Management Practices instead of the Seniority based system of wages and promotions.

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<sup>8</sup> *The Changing Nature of Japanese HRM: The Impact of the Recession and the Asian Financial Crisis*, International Studies of Management and Organization, 34(1) 2004, in collaboration with Professor John Benson, Melbourne University; *Internal Corporate Governance Discipline and the HRM System in large Japanese Companies*, Asia Pacific Business Review, Vol. 10, Spring-Summer 2004, Number 3-4;



Automatic pay increases based on age and tenure are now seen as incompatible with these planned HRM reforms. Nevertheless, abolishing such a system would not, in the short term, provide the necessary work incentives to boost productivity. As such, companies have begun to restructure the employment portfolio and differentiate pay by linking it more closely to the contribution of each category of worker to corporate performance. *Nikkeiren* (Japan Federation of Employers' Associations) proposed another approach. In their view, Japanese companies need three types of employees to prosper: (1) a core or "elite" group of long-term employees, (2) a "contractor" group of specialists to deal with specific, possibly short-term problems, and (3) a "peripheral" group of employees that concentrate on simple, routine tasks and who do not aspire to a long-term affiliation with the company<sup>9</sup>

Until the early 1990s, a majority of the young people in Japan entered the labor markets immediately after their graduation as "regular employees" with no fixed term labor contracts. Since they were considered as a cheap source of potential and capability, the recruiting companies themselves trained them on the promise that they will continue to work for the parent company indefinitely with full commitment and loyalty. The training was divided into on the job training and off the training. Simultaneously they were treated as the "contemporaries", in line with the seniority system, in the same year they were hired.

In an attempt to curtail labor costs and remain competitive, many companies are reducing the number of core workers in place of peripheral (or "contingent") workers. In 2000, a survey was conducted by the *Asahi Shinbun* Newspaper whose results revealed that as many as thirty-three companies were either currently utilizing, or had decided to utilize, *haken shain* (dispatched workers.)<sup>10</sup> Further, diversification of the work has narrowed the

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<sup>9</sup> *Ibid.*

<sup>10</sup> *Haken Shain* is a dispatched worker from a private agency as defined under the Employment Security Law of 1947 and the Worker Dispatching Law of 1985 both of which were amended on June 30, 1999. [Online: Web] Accessed on 3<sup>rd</sup> January 2006, For further information refer to URL <http://www.jil.go.jp/bulletin/year/1999/vol38-09/06.htm> and <http://www.jil.go.jp/bulletin/year/1994/vol33-08/05.htm>

differences between the two. As the core workers have more discretionary powers in the way they organize their professional life, and outsourcing, outside contractors are being increasingly being brought in, HRM<sup>11</sup> have to deal with a growing complex array of individual work conditions and multi-commitments for the both in the organization.

### **Shorter Number of Working Hours**

The number and spread of working hours declined over the period 1991 to 1995 and continues still further. Medium-sized firms experienced an 11 per cent decline in regular work hours from more than 45 hours/week in 1991 to just over 40 hours/week excluding breaks in 1995 (this is known as "statutory working hours"). The number of these firms working only a five day week rose to over 60 per cent; an increase of 27 per cent over the 1991 figure. A similar trend also occurred in the large firms, although not to the same degree. These findings reflect the general economic conditions and poor product markets.

However, some businesses are permitted to have their employees work up to 44 hours per week at a maximum of eight hours per day. These businesses include retail and beauty services, cinemas and theatres, businesses related to health and hygiene, as well as restaurants and entertainment businesses with less than 10 regular employees.

The decline in scheduled working hours must be seen in relation to the amendments to the Labor Standards Law over the past five years. In April 1991 scheduled weekly working hours were set at 44 hours for all firms from 46 hours in April 1988. Subsequent amendments required large firms to limit the standard workweek to 40 hours by April 1994. Small and medium-sized firms were set the target date of April 1997. These provisions explain some of the 5 per cent decline in working hours for large firms but would explain little of the 11 per cent decline for medium-sized firms.

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<sup>11</sup> Human Resource Management.

Moreover, to reduce the number of working hours, ‘discretionary work scheme’ has emerged for the core employees of the firm under which the research and the planning staff work at their own discretion and work sharing is achieved, by which per capita work is reduced and more than one worker does the same job, thereby protecting employment.

However, the situation is not so comfortable from the management’s viewpoint as it looks from the above. If calculated on an annual basis taking into consideration the "statutory working hours" or 40 hours per week, it amounts to more than 2000 hours of work annually. Target was set previously to reduce the number of work hours to 1800 hours annually. Further, if a comparison is done with other countries Japan as a matter of fact still exceeds even from the industrialized countries of the west, such as, Germany, U.S., and United Kingdom etc. The following table gives a comparative account of the annual number of hours of different countries<sup>12</sup>:

International groupings by annual hours of the work

| Country group                         | Countries              | Annual hours of work |
|---------------------------------------|------------------------|----------------------|
| Countries with relatively short hours | Italy, France, Germany | 1,500-1,650          |
| Countries with medium number of hours | Australia, UK, US      | 1,800-1,950          |
| Countries with relatively long hours  | Japan                  | Over 2000            |

If the above table is interpreted, we can make it out very clearly that Japan, if compared with the industrialized nations of the world, is the top most country whose labor force works the maximum. Its target of being in the bracket of countries with medium number of hours hasn’t been achieved. While the European Union’s developed duo i.e. France and Germany have their labor force working only 1500-1600 number of hours annually,

<sup>12</sup> Mouer, Ross and Hirotsuke, Kawanishi (2005), “*A Sociology of Work in Japan*”, pp73, Cambridge University Press, UK.

U.S. has a labor force which works for somewhere between 1800-1,950 hours annually. Japan, as seen from the table exceeds not only the E.U. duo, but also the U.S.

### **Production moved to Offshore Locations**

One of the techniques followed by the management to reduce their payroll burden is to shift the production facilities to the offshore locations. As new production facilities are needed to add product lines, replace older outdated plans, move to cheaper labor sources, or respond to political pressures to build plants in major export market areas, production and professional employees directly associated with local production facilities have been dismissed. Sony, Matsushita, and Toshiba use offshore production parts and that become the basis for price negotiations with competitive Japanese parts suppliers. No doubt, some Japanese technical assistance were moved to the new off shore sites in the form of supervisors and technical staff, but the fact remains that a vast majority of the plant jobs have been filled by the nationals in the plant area, thus the latter have gained at the cost of the Japanese employees due to a shift in the management practice.

The dominance that Japan built up in production technology has been lost by the relocation of production bases to overseas countries and the shift of attention in Japan toward information processing technology.

It was due to the above cause that in 2000, Japanese investment in China soared for the first time since 1995. Four main factors pushed the Japanese to rush to China. First, it was low cost; second high potential to expand Japanese firms share in the host country; third, to face the domestic competition in Japan by re-exporting the products manufactured in Japanese firms in China, and lastly, to make China as the base for third country exports.

An example of shifting the production bases *Hitachi* shifted its chemical production bases from Japan to Thailand by the end of 2002 due to lower trade costs and brighter trade opportunities, and, completed it's shifting to Thailand of all the low technology

production bases by the year 2003. As of 2004, 60% of newly established overseas operations of Japanese manufacturers were in China, and other parts of East Asia. As a part of the restructuring plan, *Sony Co* announced in January 2006 to cut the number of manufacturing bases worldwide from 65 to 54.

The above trend has been confirmed by the “Survey of Overseas Business Activities,” a quarterly survey of Japanese corporations with overseas affiliates conducted by the Ministry of Economy, Trade and Industry.

### **Transfer of excess manpower to the Suppliers’ companies**

Another payroll reduction technique followed by the management has been to transfer their excess and less efficient employees to their supplier companies. As a matter of fact, these supplier companies are the ones who are small and medium enterprises in the context of their investment, infrastructure etc and also who do not practice the lifetime employment system for their employees. These supplier or the second tier companies work in close association with the large corporations or the first tier companies. Due to the economic recession and their close association with the first tier companies, these supplier companies were no doubt affected from the profit making view point but due to their close dependent relationship with the large companies, they were obliged to add these shifted employees, generally at a much reduced salary structure. The workers who were shifted consisted of workers from the production lines, middle managers over fifty-five years and surplus technical managers. Further, when suppliers were no available, many companies such as ‘Nippon Telegraph and Telephone’ created independent subsidiaries and transferred their employees as the initial staff.

The immediate effect was that the second tier companies immediately stopped their new hiring and recruiting activities and these shifted employees suddenly landed in the pool of uncertainty from the lifetime employment system, which affected them psychologically and hence, their abilities to work competently. This personnel shift away from the lifetime employment is a major change in the Japanese business practices.

Also, with the recession at home having posed dual challenges of finding new buyers and developing alternate products to counter the competition, many suppliers companies were dropped, with the glaring example of that being of the *Tokyo Dietsu Company*. The company had got loan from the National government bank at 2.5% interest rate to shift from the polluting zone to the *Tokyo Bay* (Jenan Tokyo Park), but ironically as soon as they shifted they were dumped by the parent company and as a result they had to make a drastic reduction in the number of the workers employed and simultaneously gave a petition to reduce the interest rate.

### **Forced Early Retirements**

Middle managers over fifty-five years of age are being forced to retire ‘voluntarily’ if jobs are not available for them in the second tier companies. If a middle manager job performance card is poor or not upto the mark due to his taking for granted the lifetime employment system, the corporations have started considering him for early retirements. Further, managers in whom the company believes can improve due to variations in his past performance have been demoted. The personnel department of the firm does this by preparing a list of the managers who have scored in the bottom twenty-five percent in the annual evaluation. Further, new tactics such as giving them jobs or assignments in which the managers have no work experience in the past nor the required specialization or skills, transferring them without their family to the company’s most remotest office, far away from the headquarter, giving them no work at all except to sit by the window side (*madogiwazoke*) and isolating him completely from his work and colleagues have been adopted. Such practices adopted by the management circles have not only made the middle managers question total commitment to their company but also in extreme cases have led to depressions and finally suicides.

Very closely associated to the above two practices have been the informal introduction of the performance based wage system in which the managers and workers are evaluated annually before giving them a hike in their wage structure and also in promotions. This has resulted in the introduction of competitive forces between the employees, which

stands in sharp contrast to the Japanese policy of group cohesiveness and harmony, and thus is common in the western management practices.<sup>13</sup>

### **Increasing number of 'Job-hoppers'**

In response to the changes in employment norms and the fading of lifetime employment, a new group of workers known as "job-hoppers," has evolved. Opposed to seeking out a reliable company after graduating from university and staying with that company for 20 or 30 years until retirement, some Japanese are choosing to change jobs every few years. Therefore, many are exercising options that are better in nature.

Most job hoppers are younger workers, often people who have graduated from university within the past several years. However, job-hopping also exists among older workers, often those who have lost their job due to corporate restructuring, as companies lay off managers and high-salaried workers to save costs. Many job-hoppers justify their frequent shifting of jobs by offering a variety of skills, experiences and knowledge, as opposed to a single focus. However, according to a survey conducted by the Ministry of Health and Labor Welfare earlier in 2004, about 30% of companies would not look favorably upon a job-hopper. These companies view job-hoppers as workers who have no sense of responsibility, no specific or developed skills, and could quit their job at any time.

### **Rehiring Retirees**

According to the Elderly Persons Employment Security Law, employers may not set a mandatory retirement age of below 60; accordingly, nearly 90% of companies have set a retirement age of 60 years old. However, as the number of retiring employees continues to rise, companies struggle with a shortage of experienced workers and an overall lack of manpower.

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<sup>13</sup> Suzuki, N (October 1996), "Middle-aged and older employees in Japanese corporations Their plight during the process of major historic change in employment", *The Journal of Management Development*, vol. 15, no. 8, pp. 8-16

In June 2004, the Japanese government made revisions to the Law Concerning Stabilization of Employment of Older Persons. Under this new revision, companies will be obliged to employ workers for an additional five years (until the age of 65), if an employee requests to work additional years. Even though this revision does not go into effect in Japan until fiscal year 2006, approximately 65% of companies have already extended their employment period for workers, though most set specific conditions. These conditions include requirements such as the employee must have met or exceeded certain company standards.

For example, *Asahi Kasei* Corporation introduced a system for rehiring retirees in 2001. The company cannot afford to rehire all its workers, but if an employee's department has a continuing need for them, the employee may be re-employed in their former department. During the past three years, about 570 employees retired; approximately 190 requested to be rehired. *Asahi Kasei* was only able to rehire 71 of these former employees. The new revision will provide a company with flexibility, as a company will not be required to rehire all employees that request to continue working, but may choose only a select number for rehiring.

*Toyota* Motor Corporation also plans to expand their current rehiring program till 2006-2007. Presently, *Toyota* rehires about 100 of its employees each year, for up to three years. However, *Toyota* will re-evaluate its retirement age (currently 60 years old) and pension system. Another major company in Japan, *Kawasaki* Heavy Industries, has increased its retirement age for non-managerial workers from age 60 to 63 beginning in 2005.

Once this revision is implemented, employees should have less anxiety about their future financial situation, since they will have the option of earning a salary for an additional five years. However, the salary for a full-time job during the re-employed period may drop, even as much as 50%, in comparison to an employee's pre-retirement salary.

The other side of this coin could be the possible outcome that since the older employees would be rehired, there would be a sharp increase in the unemployment rate among the



fresh new graduates when the companies would bring to a halt to the already reduced intake or recruitment since the number of jobs would remain the same. Getting a job for the freshers would become all the more difficult. Japanese management practices will change all the more once the above law comes into effect.<sup>14</sup>

### **Rise of online recruitment**

Traditional, face-to-face recruiting continues as the norm but is no longer restricted to Japan's elite schools. Recently, a number of Japanese companies have established elaborate recruitment web sites in an attempt to recruit new employees online and save the costs of face-to-face interviews, reach a larger audience, use new technology and participate in the future. Recruiting is becoming more and more sophisticated and some companies are developing carefully crafted web sites with questions aimed at those with a special aptitude or training and/or interest in their products or services.

However, while some web sites have had great success, others, which rely too much on traditional practices in their design, have not been successful. Such sites are elaborate and time consuming, forcing visitors to spend agonizing hours slogging through complex, seemingly endless information. Efficiency-minded young people have created electronic short cuts through these sites by making the results available to the public through the web, word or mouth or software. Unfortunately, other good candidates simply leave these sites, deciding instead to apply elsewhere. Overall, however, young thinking is making real inroads into traditional Japanese recruiting and hiring techniques.

### **Hiring of the Non-Regular Employees or the “Freeters”**

Companies since the economic recession have switched their employment strategies, aiming to seek an increased flexibility in their labor costs, thus, hiring fewer new graduates and have become more dependent on non-regular employees. While many of these non-regular employees are still part-time workers, the number of contract and temporary or part time workers has been rising. Hence, the traditional mechanism “from

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<sup>14</sup> Rowley, C. (ed) (1998), *Human Resource Management in the Asia Pacific Region*, Frank Cass, London, U.K.

school to workplace” has undergone a tremendous change. In terms of the type of jobs, the numbers of non-regular employees or Freeters have been increasing not only in office and retail jobs but also in high value-added professional and technical positions. The definition of the word “*freeters*” includes a major component of the young crowd (in the 15-34 years of age), not including students and housewives, working on an *arubaito* (casual work) or on a part time basis. And one who is an unemployed person looking to work only in part-time job even if a full time job is available. Thus, the distinguishing characteristic of freeters is that they do not aspire to get on the traditional full-time career track, at least at the particular juncture in their life cycle. It is not clear if such an attitude is just a passing phase or a life-long phenomenon.

According to the 2002 Labor Force Survey, the number of *arubaito* and part time workers aged 15 to 34 (excluding married females) was estimated to be at around 1.92 million. These “*freeters*” usually finish the job as soon as possible assigned to them and start a new search for work with some experience at hand. The sudden rise in the number of “*freeters*” is directly interrelated to the fact that the private companies have stopped hiring or have considerably reduced the recruitment of fresh new graduates.

Companies are increasing non-regular employees for the following reasons. First, they find it difficult to change traditional employment practices quickly with regular employees, so they are compelled to increase the weight of non-regular employees to realize their goals of increasing labor cost flexibility. Second, progress in information and communications technologies has made it feasible to use a larger number of unskilled workers. Third, institutional improvements such as deregulation of temporary employment services have made it easier to smoothly match supply and demand in the labor market.

The share of non-regular employees is particularly high in Japan by international comparison. In terms of the relationship between the economy and the overall number of employees, however, the responsiveness of employment to the economic fluctuation in Japan is still much weaker than in other countries such as the U.S. Thus, the flexibility of

Japan's labor market is mainly due to adjustments at the margins and is still low by international standards, although it has increased to some extent. Therefore, it would not be appropriate to conclude that Japan's employment practices have been fundamentally changed.

Such a change in the corporate behavior is the primary factor behind the increase in the unemployment rate among young people, and the increase in the non-regular employees at the expense of the regular employees. With such a situation at hand, there is also a sharp decline in the school career counseling which aims to understand and achieve the nature of various occupations, and, also of themselves, and form ideas about the meaning of work. No doubt, the traditional system of employment was proving a financial burden on the companies but it didn't push the students in the pool of unemployment after graduation. The psychology of the fresh graduates with such a situation is "I want money immediately" rather than "This type of a job will suit me and I could contribute to the company's development". Thus the "*freeters*" can take their jobs in an easygoing manner than the regular employees and with some experience at hand can earn money without excessive efforts and above all increase their vocational ability and thus become a multi-skilled worker who can be suited to do all types of work and thus can adapt efficiently to the changing circumstances.

In spite of the above discussion, it should be kept in mind, however, that Japan is not unique in experiencing the rising part-time work. In many OECD countries, growth of part-time work accounted for a large share of overall employment growth between 1991 and 2001. According to a recent OECD report, rising part-time employment was large enough to more than offset declining full-time employment in Austria (0.2% for part-time vs. -0.1% for full-time), Finland (0.3% vs. -0.2%), and Italy (0.4% vs. -0.2%). The OECD report also mentions that part-time work has been a particularly important factor behind employment growth of women, youths, and to a lesser extent, older workers.

Benson and Debroux opine in their study that the changes within the Japanese HRM have been short term in nature since they are at the practice level and not at the basic structure level of the Japanese HRM. This is because of the general cultural resistance to change and apathy of senior management has created a situation where most of the HRM reforms have not been extended to policy or system architecture.

The most important challenge to the Japanese companies have been to hold on to the most efficient workers while at the same time relieving the inefficient and incapable ones. Companies are looking for solutions to overcome the shortcomings of the seniority-promotion system. Employees are now being differentiated earlier in their career according to their potential or being subjected to more detailed appraisal mechanisms in an attempt to hasten decisions about promotion. Companies are also fixing maximum ages for certain managerial grades in order to create more promotion opportunities for their most promising young executives. In addition, some companies have devised a multi-track career system, where promotion to senior management positions can occur from both specialist and the generalist positions.<sup>15</sup>

### **Growing Percentage of the ‘Dispatch’ and ‘Temporary’ Workers**

Motohiro Morishima and Tomoyuki Shimanuki in their study titled, “Managing Temporary Workers in Japan<sup>16</sup>”, have highlighted the role and the problems faced by the above section of the workers. In their study they have maintained the stance that Supply Agencies provide the necessary number of workers for a term, and bear costs for recruitment, and educational and training. Thus, outsourcing of the personnel

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<sup>15</sup> Masabumi, Tokoro (March 2005), “The Shift Towards American-style Human Resource Management Systems and the Transformation of Workers' Attitudes at Japanese Firms”, *Asian Business & Management*, Volume 4, Number 1, pp23-44,

Richard, A Werner (March 2004), “No Recovery without Reform? An Evaluation of the Evidence in Support of the Structural Reform Argument in Japan”, *Asian Business & Management*, Volume 3, Number 1, pp7-38 and,

Watanabe, T. (April 2003), “Recent Trends in Japanese Human Resource Management: The Introduction of a System of Individual and Independent Career Choice”, *Asian Business & Management*, vol. 2, no. 1, pp. 111-141

<sup>16</sup> Morishima, Motohiro (Professor, Graduate School of Commerce and Management, Hitotsubashi University) and Shimanuki, Tomoyuki (Graduate Student, Graduate School of Commerce and Management, Hitotsubashi University), “Managing Temporary Workers in Japan”

management (recruitment, training, etc.) is done by the supplying agencies, which reduces the cost of the management. Thus, the temporary workers are a great attraction to the firms that considerably aim for cost reduction. They have cited the statistics of the Ministry of Health, Labor and Welfare statistics (2003), according to which, the total number of dispatched workers increased sharply from the mid-1990s on, and reached 1.79 million in fiscal 2002, an increase of 27 percent from the previous year. Further, A series of deregulatory measures – a liberalization in principle in December, 1999, of occupations in which it is allowed to dispatch workers, and a lifting of the ban on dispatch to manufacturing premises, together with the extension of the upper limit on periods of dispatch in March, 2004, have stimulated firms further to make use of temporary workers.

Till a few years back, the companies gave menial work or peripheral work to the dispatched and temporary workers. Simultaneously, these workers have been considered as an efficient ‘buffer stock’ against the fluctuations of demand. However, the trend has been undergoing a tremendous change with the companies having started to recognize their ‘specialties’ and ‘multi-purpose skills’ and have started actively engaging them in the more essential core duties. Today they have started contributing noticeably to the success of the corporate strategies and hence are a natural choice for the human resource management. Thus, their job profile has undergone a considerable change with their status being the same as previous one.

Personnel management of regular employees involves only one actor – the firms which hire regular employees and keep them working in the same firms over the years. While the case with the dispatched workers is different, their personnel management command is in the hands of manpower supply agencies, while the actual relationship involving work assignments arises with the firms taking on temporary manpower. Thus, two actors are present in the HRM of a dispatched worker. Further, contrary to a regular employee of a Japanese company, career development of a dispatched worker is not carried out through transfer, rotation, training and other mechanisms within the firm concerned, it implies low utilization of his abilities with poor career enhancements. This leads to a

mismatch between the job descriptions and abilities required by the firm or company and the workers supplied by the supplying agency. Firms taking on dispatched workers have little information about the ability, skills, outlook, and so on of the workers and the supplying agency do not give importance to the exact credentials of the worker and the exact kind of job desired by him. Further, little interest is taken by the firms and the supplying agencies to resolve the mismatch dispute because of the short-term contract and the nature of job being temporary. In the meantime, the dispatched workers involved discover a gap between their expectations and predictions prior to actual engagement in work on one hand, and the reality after starting to work. Thus, it is hard for the dispatched workers to come to terms with the reality once they are inside the 'pool'. And finally, demoralized, they fail to demonstrate the expected job performances. Work experience at host companies are seen as golden opportunities by the temporary and dispatched workers to apply their acquired ability and skills to practical work environments, and to sustain and improve their quality. Thus both the category of the workers are obliged to adapt themselves once thrown in the 'pool' and perform well.

Remuneration (wages) and rewards are strictly in accordance to the nature of jobs assigned. While the former goes with the job profile and the work done, the latter goes with the improvements in ability and skills, achievement, and other factors but their job being short and temporary in nature, it is not directly reflected in their wages. The only reward expected by them can be a renewal of the contract and chances of being assigned to a different and more high profile host company. Again, the keys of such a reward is directly into the hands of the manpower supplying agencies and does not rest with the host companies. The host company's function is only to monitor the behavior and attitude of the dispatched workers to their jobs assigned and as such have no active role to play in the determination of their wages and rewards, nor drawing up mechanisms for their incentives. This role is being played by the supplying agencies but in the absence of their performance reports with the supply agencies, causes at times a perfect mismatch between the contributions of and the remuneration to the temporary workers, which is hardly resolved due to the shortness of their career.

## **Role of the Labor Unions in Diversified Employment Practices due to Economic Recession**

Mitsuru Yamashita, in her study, “Japanese Labor-management Relations in an Era of Diversification of Employment Types: Diversifying Workers and the Role of Labor Unions<sup>17</sup>” has brought about the causes of the declining rate of the unionization in the Japanese society.

It is the substantial decline in organizing new union members since the mid-1970s, namely the decline in the “birth rate” of labor unions, that is the basic factor behind the decline in the unionization rate. In the present day context, ratio of female employees and the ratio of part-time workers have influenced the declining rate of unionization. Further, the part time workers due to their short tenure in the host company are not eager to unionize themselves. Another common reason cited for low rate of unionization in various studies is the burgeoning of development in the service economy, thereby expanding the importance of commerce and service industries where the rate of unionization has been lower since the beginning. The condition according to the Ministry of Labor, 1998, survey shows that among companies that employ part-time workers, only 4.9 percent companies (totals based on industry and corporate size) unionize part-time workers, and the rest of all labor unions (95.1%) do not treat part-time workers as members. Thus, Unionization is primarily geared toward regular employees and is geared more towards regular employees. It has also been pointed out that if part-time workers are unionized, the unions will have to respond differently to their needs than they do to the needs of regular employees, such as lowering union dues and flexibly scheduling union activities. It appears that regular employees think this will increase the burden on them. Moreover, there are workers who do not necessarily wish to become regular employees, which will be a major challenge to labor unions when they carry out their

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<sup>17</sup> Yamashita, Mitsuru (Winter 2005), “Japanese Labor-management Relations in an Era of Diversification of Employment Types: Diversifying Workers and the Role of Labor Unions”, *Japan Labor Review*, Volume2, No 1, pp. 105-117.

activities. Japanese labor unions have held onto an archaic image of workers —male, regular employees with an awareness of their rights and commitment to their work — and it has been difficult for them to take an active approach toward workers who do not fit this image.

Another study titled as “Formation of the Labor Unions and Responses to the Managerial Crises --- Industrial Relations in the late 1990s” by the Japan Institute of Labor in the year 2002 (October) has highlighted the cause of a decline in the unionization as that since the recession in the 1990s, there has been an increase in workforce restructuring by employers as well as establishment closures and bankruptcies, thus leading to the reduction or dismissal of union members in such companies and establishments. Those union members that have been reduced or dismissed have contributed to the loss of union membership accordingly. According to their report, the late 1990s apart from the economic recession witnessed, a start in the decline of the number of union members. According to their official statistics, in 1999, it dropped below 12 million, then to about 11.21 million in 2001.

The recent development which cannot be ignored is the fact that Individual – Labor management relations such as recent individual personnel treatment, has promoted the individualization of employee’s interests in the recent past have been established. According to the 1997 survey for companies with more than 1,000 employees, approximately 97 percent of the responding companies attempted to strengthen the personnel management based on the achievement and performance of individuals (FUJI Research Institute Corporation, 1997, p. 152). In many cases, superiors dealt with personal grievances and that the managers became busier due to the above reason. Also, companies where labor unions exist, they established ‘Grievance Settlement organs’ or the cells for the same and thus there was a decline in the activities of the unions. Thus, according to some authors there has been successful establishment of the ‘non-union voice machinery’ raising their voices over the decision-making process of individual personnel treatment.



A stark difference is made between the two, i.e. the ‘unions’ and the ‘non-union voice machinery’ (labor-management consultation system and employees’ organizations): the former is superior to the latter in the sense of communication related to the employees’ collective interests, while the latter is superior to the former in terms of communicating the ‘procedural justice’<sup>18</sup> of deciding the treatment of individual personal. When labor unions and employees’ organizations are compared, the former have a higher ability to secure procedural justice, while employees’ organizations have limited influence on information disclosure regarding personnel evaluation system and reform of wage structures. But, in the due course of time when the management practices are itself changing in the background of the continuing economic recession and thus the reduced profits of the companies, one seriously raises doubts over the role performed by the unions in the present day context.

The only role that one can think of regarding the labor union at present is that of the reinforcement of in-house communications and the facilitation of communications with supervisors, as well as the enhancement of employees’ morale and motivation. No doubt even the Japanese management has appreciated this role. However due to business costs, the attitude toward unions may be ambivalent as regards understanding employees’ grievances and dissatisfactions. With regard to the reason for the formation of unions, the number of employers tends to attribute it to the difference of interests between labor and management increased after the union formation and especially against the backdrop of the continuing economic recession.

In the past few years, the issues faced by the unions have diversified because of the economic recession. The priority sequence of needs changed according to age group. The older age group replied that “increased wages” and “extension of retirement age, reemployment system, etc.” were of the highest priority. The middle-aged group responded with “increased wages” and “increased holidays and leave”. The younger age

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<sup>18</sup> ‘Procedural justice’ refers to the fairness of the process or procedures of distributing results, which is used as the contrasting concept of ‘distributive justice’, which refers to the fairness of the results themselves.

group stated that “increased holidays and leave” and “increased wages” were the most important to them. The labor unions keeping in mind the economic situation of the nation and the company thereof, have placed the diversifying in descending order with the demands of the “increase in wages”, “increased holiday leave”, having top most priority. Further, most of unions are not opposed to the application of merit-based or performance-based approaches to the personnel and wage system, however, there is a parallel demand the introduction of some complementary measure since the older and middle aged employees are not accustomed to the new practices which have been brought about by the management. According to the report’s survey approximately 70 percent of all employees felt aggrieved and dissatisfied about their own personnel treatment in the previous year. Moreover the report also mentioned the fact that a considerable percentage of employees gave up expressing their grievances and dissatisfaction because they felt that they had no available channel through which they could express themselves and felt it useless to express them in order to achieve a settlement if a dispute arised due to a change in the management practice. Instead, as a change in the situation, grievances and dissatisfaction about their own personnel treatment were mainly presented to their superiors.

The report laid the duty to protect its employees in advance by grasping the company’s financial position from the cash flow statements and alerting the workers in advance. It was also said that it has now become important to check the real situation when a company’s credit problems are reported in the market. Since management usually would not want to disclose this adverse information to the labor unions, the latter on their part should be sensitive to any information, including that from informal sources. The economic recession had meant that a crisis for the company is directly a crisis for the labor union, thus in order to know what should be agreed in such an emergency, labor unions should infact consult eminent lawyers who are experienced in such matters.

The above requirements, if analyzed, in the environment of the continuing economic recession, stands sharp in contrast to the practices followed by the labor unions in the past. Thus, a change in the management practices and in attitude of the top management has a direct bearing on the attitude of the labor unions. The labor unions are now

expected to be more legally and financially aware of their environment and also gather sources about the financial condition of the company through their own sources. The unions thus, now require not only people who are expert in the field areas but also experts from the financial and legal background so as to secure a future for the workers and to avoid 'reality shocks' in the near future.

A marked shift in the role of labor unions could be seen in the paradigm shift of the aims and objectives of the '*Shunto*' or the spring offensive. In the past, '*Shunto*' was instrumental in raising the low standard of wages in industries and sectors that paid poorly. Annual negotiations between labor and management helped determine an appropriate wage level in the context of changing economic conditions. Consequently, management was able to adjust to those economic changes rather flexibly, and as a result Japan began to enjoy excellent economic performance. The practice of '*Shunto*' has decreased in the recent past firstly due to the poor profit earned by the companies due to recession and secondly, the management (white collar employees) have themselves cut down on their monthly salary structures, thereby, setting up an example to the workers that it is not in favor of their moral obligation to ask for a wage increase when the company is faced by tough economic conditions. Moreover, differences in the business performance of Japanese companies have become conspicuous, a trend hindering the industry wide wage increases that could be expected in the past. Since the huge amount of time and money devoted to '*Shunto*' yield only minor wage increases, there are also cases in which '*Shunto*' is carried out in the alternate years and even multi-year arrangements have been made.

Given today's austere economic climate in which wage increases are difficult, '*Shunto*' has made an extreme deviation from its former policy of wage increase as the highest priority to job security as a matter of utmost importance. Thus, a paradigm shift is clearly visible by the labor unions. Further more, Japan Business Federation is advocating work sharing as an important link in job security, which consists of reduced working hours along with lower wages, and the introduction of hourly wages for permanent employees, and this is being discussed in all fields.

Finally, Japanese business, like its global counterparts, has over the past decade experienced an acute economic and political crisis. Japanese corporations are restructuring their operations to remain competitive. All the past concessions granted to workers are being ripped up with the assistance of the unions. The unions have accepted it with the glaring example of the case of Nissan union in 1999 declaring its support for the company's restructuring plans that costed 21,000 jobs, or 14 percent of the workforce.

### **Management's Response to the Growing Need for Foreign Workers**

Also, the question of ageing population and immigration policy is one of the areas where the management is gearing itself to deal with. Since it is a well-known fact that the Japanese society is homogeneous in nature the question of importing the workforce is very difficult to think of for the Japanese management. Japan's population is projected to become the world's oldest by 2025<sup>19</sup>. The population is projected to continue declining for years to come. Thus, it is expected to decline by almost 14 percent, from 126.9 million in year 2000 to 109.3 million in the year 2040. During the same time period, the prime working age population (15 to 64 years old) will drop by over 29 percent, from 86.4 million to 61 million, and the older population (65 years of age or older) will rise by almost 65 percent, from 22 million to 36.3 million. As a result the ratio of persons 65 years or older to persons of prime working age will rise from 0.25 to 0.59 in this time frame. The prospect of such an increasing imbalance in the age composition of the population raises serious and urgent issues for Japan's long-term prospect, economic and otherwise.

While the falling birthrate is creating acute labor shortages, the young generation is not ready to accept the "3K" jobs (*Kitsui*- difficult; *Kitanai*- dirty; and *Kiken*- dangerous). The term was popularized around 1990, when there was a great demand for foreign workers at the ongoing construction sites and the factories during the period of the bubble economy. Their own preference was obviously on the white collared jobs.

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<sup>19</sup> *Economist*, September 27, 2003

Following the changes in Japan's immigration policy in 1990, the government launched its Technical Internship Training Program (TITP) in 1993. This was designed to be part of a larger effort to facilitate the transfer of technical skills to neighboring developing countries through trainee and technical intern programs while also allowing Japanese employers to avail themselves of a new pool of workers on an interim basis. Today, foreigners entering Japan with a trainee visa can apply for the status of technical intern a year later, and remain in Japan for a total of three years.

At its core, the trainee system is another mechanism for recruiting "unskilled labor." Despite the stated goal of fostering the transfer of technical skills, numerous studies have indicated that the majority of businesses accept trainees to lower personnel costs and to offset labor shortages. While the number of trainees appeared to reach a plateau in the mid-1990s, it increased by 36 percent between 1999 and 2000. According to the Ministry of Justice, of the 36,000 trainees registered at the end of 2000, 61 percent were Chinese, followed by Indonesians (12 percent) and Filipinos (8 percent). Keeping pace with the increase in trainees has been the notable growth in the number of trainees applying for technical internships -- from 5,300 in 1996 to 12,400 in 1998 and then to 16,100 in 2000, according to the Japan International Training Cooperation Organization (JITCO).<sup>20</sup>

Trainees are not protected by labor standards and receive "allowances" that are often significantly lower than the minimum wages. Although technical interns are "workers" in the legal sense, they too have found their wages cut back due to a series of deductions unilaterally imposed by employers. JITCO statistics show that approximately half of the 16,100 prospective technical interns in the year 2000 were expected to receive a monthly wage of less than 120,000 yen (US\$900), and those who could expect 150,000 yen or more accounted for only 3 percent. These figures are substantially lower than the average wages of Japanese workers, aged 20-29, in the manufacturing sector: approximately

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<sup>20</sup> Yamashita, Mitsuru (Winter 2005), "Japanese Labor-management Relations in an Era of Diversification of Employment Types: Diversifying Workers and the Role of Labor Unions", *Japan Labor Review*, Volume 2, No 1, pp. 105-117.

240,000-280,000 yen for males and 190,000-210,000 for females, according to the 2002 Japan Statistical Yearbook.<sup>21</sup>

Will Japan sacrifice its ethnic homogeneity in the prime age population by giving permission to a large number of foreign workers to enter Japan and hence their corporations is the question which has to be dealt effectively both by the Government of Japan as well as the large Japanese corporations. The foreign workers will include both viz the temporary as well as the regular workers. One solution seems to be the retention of the older employees by the company to maintain the existing levels of productivity and profitability. But the dilemma faced by the management is as to how long the older employees can be retained by the companies and what is the guarantee of their efficiency? Will efficiency not decrease with the increase of the physical age of the body? An optimistic scenario can be the assumption that the technological progress is ever continuous in nature so that the ethnic homogeneity is not changed and older employees are retained for a long period of time. But, again the question arises is as to how long the technological progress replace the human mind and body? How will the future management decisions would be taken? Wouldn't they require new ideas keeping in context the changed international levels of competitiveness and levels of quality?

On the other hand, Japan may take a bold and dramatic step and begin accepting a steady increase in the immigration of prime age foreign workers, many of who would be integrated into the mainstream Japanese society. In this scenario, Japan gradually will become transformed into a melting pot, much like the United States, with an increasing ethnic diversity and a more balanced age composition of her population. Prime age foreign workers will help alleviate the difficulties of financing pensions in the face of growing number of retirees. Will the management treat them at par with the Japanese workers? Would the foreign immigrants be granted Japanese citizenship?

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<sup>21</sup> *Ibid.*

As per the law, only the children of the people with Japanese nationality and the third generation Japanese descendants in other countries could legally work in Japan. Further, foreigners wishing to work in Japan in accordance with the law must be from the skilled category. The reality, however, stands in sharp contrast to the above-mentioned requirements. Most of the foreign workers fall within the ambit of the unskilled category, which work illegally by overstaying on their tourist or student visa. And, as expected, they may be treated with contempt and looked down upon. Thus it is necessary on the part of the Government to bring about the required reforms in their laws concerning the immigration of foreign workers so as to amalgamate them with ethnic Japanese regular labor force. This step would be beneficial to both the management and as well as the foreign workers. Management would get labor to do the required work without violating the laws of the land and hence the required level of productivity, efficiency and profitability would be maintained in the background of intense competition created by the ongoing economic recession, globalization and the IT revolution and also the foreign workers would not only get social security schemes so that they are covered as per the international standards but also they would be accepted by the Japanese society with warmth and would not be looked down upon in the near future.

The Japanese Government and the Management have to face the harsh reality that the foreign workers are becoming important members of the nation's labor force and a "closed-door" policy towards them would no longer be beneficial to the economy since both skilled workers and unskilled workers have ample opportunities world wide due to their competence. What the world considers today is the quality and not the ethnic origin of the workforce because efficiency and hence profit is the key to survival in an ongoing competing world.

No doubt, the numbers of foreign workers have increased in the past. In March 2002, the Ministry of Health, Labor and Welfare estimated the number of foreign workers in Japan at the end of 2000 to be at least 7,10,000, i.e. an increase of 6 percent from the previous year and accounting for just over 1 percent of the Japanese workforce. This figure includes approximately 100,000 professionals and other highly skilled workers, as well as

54,000 people holding "entertainer" visas. Excluded are permanent residents such as "old-comer" Koreans and a small segment of Brazilian *Nikkeijin* (Brazilians of Japanese descent). Trends show that Japanese firms have filled lower-paid, short-term jobs with overseas recruits, particularly with South Americans of Japanese ancestry. These new legal laborers, who have benefited from liberalized immigration laws for people of Japanese descent, are rising in number as the population of unauthorized workers, such as visa overstayers, dwindles.<sup>22</sup> Demand for foreign workers who are in the skilled category is bound to increase in labor-intensive service sectors, including those related to the health and nursing care.

In fact, annual Ministry of Health, Labor and Welfare surveys on businesses employing foreign workers show a steady increase in the ratio of "indirect employment" to "direct employment." Indirect, or contract labor, accounted for over 40 percent of the total number of foreign workers included in official records. Also, In addition, some studies have found a decline in monthly earnings by Brazilian *Nikkeijin* due to cutbacks in wages, decreased overtime work, or because they moved to less well-paid, non-manufacturing sectors. In short, the *Nikkeijin's* employment opportunities continue to exist, but the nature of that employment has changed in the current economic climate. By providing a surge tank of flexible labor and accepting less-than-favorable working conditions, the *Nikkeijin* provide a cushion for manufacturing industries and others that need the flexibility to expand and reduce production to cope with unpredictable market conditions.<sup>23</sup>

### **Conclusion of the Chapter**

New Human Resource Management Practices of Japan based on Western model gives altogether different dimensions to employment practices, employer-employee relationships, industrial relations and Job Management Practices that can be considered at

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<sup>22</sup> Kashiwazaki, Chikako (2002), "*Japan's Resilient Demand for Foreign Workers*", Migration Information Source, [Online: Web], Accessed on 17<sup>th</sup> January 2006, URL <http://www.migrationinformation.org/Feature/display.cfm?ID=8>

<sup>23</sup> *Ibid.*



the cost of abandoning the traditional Japanese model of management and focus on the following features: -

- Market orientated employment systems - wages benchmarked on market.
- Contract based employment.
- Introduction of the incentive plans, annual compensation, and competence-orientated payment system.
- Evaluation system has shifted to performance and development.
- *Shokuno-bunruiseido* (classification) shift to task-classification system. (Competence based task role orientated system.)
- Role orientated Job control i.e. HRM adjusts *shikakuseido* and introduces a more task-orientated system.
- Translucent and open HRM practices that strive to gain acceptance by all workers.
- Recognition of Top members of management as pro-active agents in determining work ways with much greater freedom being afforded by management.

One of the immediate after effects of the changes in unemployment relations and decreased Gross Domestic Product (GDP) growth has been a sharp increase in the unemployment rate. The GDP rate in the year 1990 was 4.8% and the unemployment rate was 2.1%. In the year 1997 the GDP growth rate declined to 1.8% and unemployment

rate increased to 3.4%. Finally the GDP growth rate increased due to reforms introduced in the economy to 2.7%, but the unemployment rate increased to 5.3%.<sup>24</sup>

The question is whether the deliberate change in the management practices due to the impact of the recession is long-term trend or opportunistic response? The answer to this question solely depends on whether Japan would ever come out of its continuing economic recession and will there be a second 'bubble' economy in the near future. While economic growth is difficult to predict and is dependent on a range of factors, it is unlikely that the growth rates of earlier years will be regained. Earlier recessions in Japan were followed by periods of strong economic growth and also were of shorter periods. The present ongoing economic recession has not only shown lesser variations but is also continuing since the 1990s. Moreover, Japan now faces more competitive global markets since the process of globalization and the IT revolution accompanied the economic recession. Further, the 1997 Asian Financial Crisis and the subsequent restructuring of the Asian economies and the influence of western economies and firms have been particularly important. Also, the high value of Yen has forced Japanese manufacturers to continue the transfer production to the offshore locations. The recent deregulation has forced firms to be more assertive and aggressive in their production and management practices. Since what matters today is not only the survival of the firm but also marginal profits that the employees' wages can be paid and profits can be retained after that the companies are willing to continue with their changed management practices, the traditional practices which would otherwise not only land the firm in losses but might also force them to shut down. Thus, the traditional rigidities of the past have been broken down with the economic recession having provided only an opportunity to do so.

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<sup>24</sup> The source for Statistics: For Real GDP Growth - International Monetary Fund (2002), Page No. 606–609. For Unemployment Rate - Organization for Economic Cooperation and Development (2001), Page No. 82–83; Organization for Economic Cooperation and Development (2003), Page No. 24–25. For real GDP Growth of 2003 - Cabinet Office 2004 and for Unemployment Rate for the same year - Organization for Economic Cooperation and Development (2004), Page No.16.

While the western scholars call the phase as the ‘slow pace of reform’ and assign the reasons of the integrated nature of the employment system and the Japanese society being traditional and rigid in carrying out the changes, Japanese society is finding even the changes carried out up till now not less than the revolutionary or too fast. The past events in the economy have already influenced the way the firms view their management practices and labor strategies. The management themselves are today evaluating the value of, and their commitment to, the lifetime employment system, and, the workers on their part are questioning in turn their commitment and sincerity to the firm in which they have been employed in the background of the recent changes and the continuing economic uncertainties.

The government, on its part, has taken some bold steps keeping in view the change in management practices job training certifications and job training camps. In a plan issued in September 2004, the Ministry of Health and Labor Welfare has set up around 40 “camps” to provide job training for youths. Within the first five years of the program, Ministry of Health and Labor Welfare intends to train around twenty thousand candidates, as well as provide training for many businesses and organizations. Participants of the program have to spend three weeks in the training with about twenty other candidates and will be taught ethics, self-discipline and work etiquette. The program will also provide support for finding a job.

Further, to make youths more appealing to employers, the Ministry of Health and Labor Welfare has created a certification program to improve the business skills of young people in Japan. The Certificate on Basic Business Skills for the Younger Generation will certify that a person has the skills necessary to perform clerical and sales work in a professional environment. The Certificate will be awarded on one of two levels: (1) on a basic level, equivalent to a high school graduate, or (2) on a practical level, equivalent to a college graduate. Courses for the Certification may be taken at designated vocational schools or job training facilities.

The Certification program focuses on five main areas: (1) communication and interpersonal skills, (2) professionalism and sense of responsibility, (3) academic abilities such as literacy and mathematics, (4) business etiquette and manners, and (5) certification in a specific area, such as accounting or a foreign language. In order to be rewarded Certification, participants must pass the required courses and competency exams. Certificate holders should have an easier time securing a new job, as the Certificate clearly defines the skills, abilities and job training experience of the applicant.

Thus, the government has also indirectly agreed to the changed management practices and is making efforts on its part gradually to make sure at least numbers of people are affected with the changes and also with the changes that are about to come as the time passes. Such a response of the government brings the fact to the forefront that the recession is going to continue for more and the people should be ready wholeheartedly to accept the consequences<sup>25</sup>.

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<sup>25</sup> Refer to Woronoff, Jon (1992), *The Japanese Management Mystique: The Reality Behind the Myth*, Chicago Publishers, U.S.A, Watson, D.R.; Sallot, L.M. (Winter 2001), "Public relations practice in Japan - an exploratory study", *Public Relations Review*, vol. 27, no. 4, pp. 389-402, Selmer, J. (June 2001), "Human resource management in Japan - Adjustment or transformation?", *International Journal of Manpower*, vol. 22, no. 3, pp. 235-243, and, Sarra, J.; Nakaghigashi, M. (October 2002), "Balancing Social and Corporate Culture in the Global Economy: The Evolution of Japanese Corporate Structure and Norms", *Law & Policy*, vol. 24, no. 4, pp. 299-354.

## CHAPTER 3

### CORPORATE GOVERNANCE AND CHANGING PRACTICES: 1990s ECONOMIC RECESSION

For many years Japanese companies have attracted widespread admiration because of their perceived ability to make long-term decisions. This capability has been attributed to various facets of corporate governance Japan-style - in particular to the typical cross-shareholding structure that afforded managerial teams such a sense of security.

According to the OECD (April 1999), “*Corporate governance is the system by which business corporations are directed and controlled. The corporate governance structure specifies the distribution of rights and responsibilities among different participants in the corporation, such as, the board, managers, shareholders and other stakeholders, and spells out the rules and procedures for making decisions on corporate affairs. By doing this, it also provides the structure through which the company objectives are set, and the means of attaining those objectives and monitoring performance*”.<sup>1</sup>

#### **Principles of Traditional Japanese Corporate Governance**

Japan’s model of corporations has conventionally been regarded as relatively ‘society-friendly’ and thus rests on the social presumption particularly when compared with Anglo-American models. This is because of such features as its corporate governance; close coordination with government policy in business strategy; and lifelong employment. Corporate Social Responsibility (CSR) traditionally refers to activity by business that can be said to enhance society, is removed from business for profit activity, and is voluntary and thus not required by law or any other form of governmental coercion. In Japan a company has long been associated with the formation of community, and thus forms the basis of society to which an individual employee belongs. In contrast to an Anglo-American model of community, in Japan both individuals and

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<sup>1</sup> <http://www.encycogov.com/WhatIsGorpGov.asp> Downloaded on 15th October 2005.

companies are members of society and hence responsible to it.<sup>2</sup> There is a visible presence of wider societal and corporate governance norms concerning the close coordination of corporate strategy and national government policy, called as 'reciprocal consent' between business and government.<sup>3</sup>

Commercial Code and Audit Special Exception Code have guided corporate Governance in Japan. The Commercial Code, enacted in 1890, introduced into Japan a financial reporting system modeled after the German Commercial Code oriented towards creditors and tax collection. The Ministry of Justice (MOJ) of Japan administers and enforces the Commercial Code. Every joint-stock company (*kabushiki kaisha*) must prepare non-consolidated (single company) annual financial statements in accordance with Commercial Code rules and must submit these statements for approval at the annual general meeting of stockholders. These statements focus on determining profits available for dividend payments.

The principal objective of the Commercial Code is to protect creditors by ensuring companies calculate the income available for dividends to shareholders in a conservative manner. For example, the Commercial Code requires that asset values be recorded at acquisition cost with no provision for including increase in asset value and so the income available for dividends remains generally low.

Japanese business associations tend not to take on similar governance functions. Unions are organized around enterprise, rather than industry or occupational lines. Coordination across firms takes place on the basis of business groups (*keiretsu*), either vertically (Toyota and their supplier, for instance) or horizontally organized (like in the Mitsubishi group).

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2 Fukukawa, Kyoko and Moon Jeremy (May 2003), A Japanese Model of Corporate Social Responsibility? : A study of online reporting; Bradford University School of Management; Working Paper No 03/10; [Online Web] Accessed on 15th October 2005, URL [http://www.brad.ac.uk/acad/management/external/pdf/workingpapers/2003/Booklet\\_03=10.pdf](http://www.brad.ac.uk/acad/management/external/pdf/workingpapers/2003/Booklet_03=10.pdf)

3 Samuels, R (1987) *The Business of the Japanese State* Ithaca, New York; Cornell University Press.

Corporate Governance System of Japan was based on cross-shareholdings and long-term relationships among a group of firms called as *Keiretsu*. In a large number of cases the main bank in the group exercised the leading role in the *Keiretsu*. According to some authors of management, this corporate governance system or the main bank system, was one of the principal factors that contributed to the success of the Japanese economy from the early 1950s to the early 1990s. By the early 1990s there was substantial concentration of wealth since the entrenchment of very large Japanese corporations, *zaibatsu*, each consisting of a holding company and numerous production companies with their actual strength of less than ten in number controlled nearly 90% of the entire economy. The shareholders of the *zaibatsu* themselves performed the governance functions of the main corporation and its subsidiaries or its related companies and thus it resulted in continued period of high dividends and high employee turnover.

Before proceeding further, it has to be kept in mind that the main bank system is not a legal institution. The main bank's function is not defined in any statute or regulation. Nor are any special obligations to borrowers specified contractually.<sup>4</sup>

*Keiretsu* group consists of a number of companies, of which banks play a central role, that are linked by a stable cross-shareholdings in a sense that each firm owns equity in the other firms of the group such that among themselves, they retain control of the each firm in the group. Hence, *Keiretsu* do not sell their shares outside the group and as a result support incumbent management. The main bank usually holds the largest block of equity and is a major lender to other firms in the group. Therefore, under the main bank system, the banks exercise corporate control and the group's firms are the largest shareholders collectively. Cross shareholding in Japan developed historically as a protection against hostile takeovers and to underwrite long-term business relationships. The behavior of the large corporations has, in the past, not only been attuned to government policies but also coordinated by *Keidanren*, the Japan Federation of Economic Organizations. Moreover,

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<sup>4</sup> Please refer to Aoki, Masahiko and Patrick, Hugh (eds) (1994), *The Japanese Main Bank System: Its Relevance For Developing And Transforming Economies*, Ramseyer, Mark, J. *Explicit Reasons for Implicit Contracts: The Legal Logic to the Japanese Main Bank System*, Page no 231.

these 'national champions' have tendency to maintain close and supportive relations with their suppliers (known as *Keiretsu* or 'affiliates'), which made for relative stability in employment patterns and business relations with particular communities. Further, the bank and debt equity relationships within the corporation are referred to as the corporate group i.e. *Kigyo-Shudan*. Both the *Keiretsus* and *Kigyo-Shudan* performed a monitoring function in terms of protecting the interests of both the equity and human capital investors.

It has been a longtime claim of Japanese companies that, unlike their US counterparts, they have been run largely in the interests of their stakeholders. Indeed, the stakeholder concept has become a fashionable one worldwide but, in the Japanese context, it encompasses a variety of disparate sub-interest groups. These can include employees, trade unions, banks, suppliers of raw materials and distributors of finished products, and of course, the community at large.

Top managers in Japan tend to be internally promoted. Managerial compensation is much closer to that of average employees' schemes and lack strong shareholder-oriented incentives such as stock options. Consequently, managers are often said to be less finance-oriented and focused on long-term product strategy. As a result, managers are able to build corporate governance "coalitions" among stable investors, banks, employees and inside management.<sup>5</sup> Thus according to the Western philosophy of the Management, three characteristics of the Japanese corporate governance system are responsible that lead Japanese managers to produce low returns for shareholders.

- First, insider stakeholders dominate corporate governance. Insider stakeholders held 38% of the shares of the large Japanese firms in the year 1996. These insider stakeholders monitor the firm's managers and outside shareholders have little or no role in the corporate governance. Thus the managers do not focus primarily on profit

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<sup>5</sup> Jackson, Gregory and Moerke, Andreas (May 2005), "Continuity and Change in Corporate Governance: comparing Germany and Japan", *Corporate Governance*, Volume 13, Number 3 pp 351-361.



maximization. Insider stakeholders profit from the return on their equity investments and from their other relationships with the firm. Outside shareholders are hence in a minority.

- Second, institutional investors such as pension funds, mutual funds, and insurance companies, pool the assets of many households are weak and small. They control just 16 percent of household assets, compared with 33 percent in the U.S. Also, Japanese institutional investors do not have a history of exerting pressure on companies to increase shareholder returns. Life insurance companies for example have typically played a passive role in corporate governance. Often life insurers act as inside stakeholders and use their shareholdings to retain the insurance business of a firm and its employees rather than pressuring managers to maximize shareholder wealth. Corporate pension funds, too, are often managed in the interest of the funding corporation rather than the interest of the pension beneficiaries. The small size of institutional investors and their limited role towards shareholders has immensely contributed to Japan's problem of low return on investment wealth.
- And finally, there is no market for corporate control. Some individual shareholders will only take action to force managers to focus on shareholder returns when the cost of the action is small. Many governance mechanisms, such as electing candidates to the board of directors or sponsoring resolutions at the shareholders' annual meeting, are so costly that individual shareholders rarely pursue them.<sup>6</sup> Also, hostile takeovers are thus absent in Japanese corporate. Failing firms were often restructured under the guidance of the main bank, generally resulting in the replacement of the existing management. To prevent hostile takeovers, structural impediment is present in the form of the *Keiretsu*, which is a firmly established social norm. The shared

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<sup>6</sup> For, further references see: S. Gibson Michael, (September 1998), "Big Bang" Deregulation And Japanese Corporate Governance: A Survey Of The Issues, Board of Governors of the Federal Reserve System", International Finance Discussion Papers, Number 624.

understanding that Japanese managers do not sell their companies, particularly to an uninvited bidder, is repeated like a mantra in virtually every domestic and foreign commentary on Japanese mergers and acquisitions. So much so is the social environment against hostile takeovers that in the Japanese Language it is called as “*nottori*” meaning “a hijacking”.

Japanese traditional board system has statutory auditors, who have no vote and are only in charge of ‘illegality monitoring’, have been perfectly fit to Japanese contingent corporate governance system based on company community. In the traditional system, there is little distinction between management and monitoring in the board. Only in the case of bad performance by the company community, main bank or major *keiretsu* shareholders force the company community to accept outside directors.

### **Problems Associated with the Traditional System**

The basic problem in the corporate governance of Japan was the *low level of returns* earned on the Japanese wealth. This problem had to be addressed to maintain a high level of per capita income in the light of two facts. First, Japan’s population is aging rapidly, which will slow Japan’s rate of labor force growth. Second, Japan’s industrial firms are on the frontier of technology, so Japan’s rapid productivity growth of the 1960s and 1970s is unlikely to be repeated.<sup>7</sup>

The success of the main bank system came at the expense of the *non-controlling shareholders*. Although the legal framework provides Japanese shareholders with more rights than the U.S. shareholders, these rights are difficult to exercise in practice. Thus, corporate decisions were taken in order to benefit a number of other stakeholders including the lending bank, customers, suppliers and other firms in the bank group. Thus, profit maximization was not the main aim of the firm. The average excess return on equity in Japan for the period 1980-1998 was 2.4% compared to 8.9% in the U.S.A.<sup>8</sup>

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<sup>7</sup> Refer to Yafeh, Y. (2000), “Corporate governance in Japan: past performance and future prospects”, *Oxford Review of Economic Policy*, vol. 16, no. 2, pp. 74-84

<sup>8</sup> *Ibid.*

Japan's auditing system and practices suffer from several weaknesses. Throughout the 1990s, statutory auditors and the CPA have failed in many cases to identify and disclose financial statement window-dressing and fraudulent acts by company management and employees. Foreign companies have great dissatisfaction with Japanese CPAs since published financial statements lack credibility. This is because of a Japanese company and its CPA auditing firm usually maintain very close relations in good times and bad, so the company expects the auditor to provide help when troubles arise. Although stockholders officially select the company's CPA auditing firm, in reality the company nominates the CPA firm beforehand, and changes in a company's auditor rarely occur. This long, close relationship can lead a CPA firm to overlook and condone improper accounting used by a company to window-dress its financial statements. Further, Lawsuits and compensatory damage claims against CPA firms rarely occur in Japan, and no lawsuit of this type has been successful.

Despite the increase in investments by foreign companies, some investors were not able to satisfy themselves with the transparency level and hence some of the foreign investors were shying away from the purchase of Japanese companies. For example Daimler Chrysler expressed great interest in purchasing Nissan Diesel Motor Company in 1998, but the deal eventually fell through with a principal reason being that Daimler Chrysler had great difficulty ascertaining the amount of debt and contingent liabilities not disclosed in Nissan Diesel's consolidated financial statements.<sup>9</sup>

Further, Japan's competitiveness declined due to the observance of the main bank system, which is evident from the World Competitiveness Report by the International Institute of Management Development that publishes its World Competitiveness Yearbook. During 1986 Japan ranked as number 1 but her position gradually declined to 17<sup>th</sup> by the year 2000 as following:-

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<sup>9</sup> *Ibid*

### Japan's World Competitiveness Ranking 1986-2000

|         |    |
|---------|----|
| 1986-93 | 1  |
| 1994    | 3  |
| 1995    | 4  |
| 1996    | 4  |
| 1997    | 9  |
| 1998    | 18 |
| 1999    | 16 |
| 2000    | 17 |

With the Big Bang financial reforms deregulating the Japanese financial markets and encouraging greater participation by foreign companies, several foreign financial firms have expanded their presence in the Japanese market since 1997. Large financial institutions such as GE Capital Services, Citigroup, Dresdner Bank, and Merrill Lynch have made substantial investments or have established joint ventures with Japanese companies to provide services for specific financial market segments.<sup>10</sup>

Internationalization and Globalization had also created pressures to move toward a more *market-based and shareholder-oriented model of governance*. Japan is increasingly looking upto international capital markets for financing which has resulted in a sharp increase in the foreign investments. Foreign direct investment has increased. They owned 18.3 per cent of stocks listed on the Tokyo Stock exchange in 2002, compared to 4 per

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<sup>10</sup> D. Gordon William (1999), "A Critical Evaluation of Japanese Accounting Changes Since 1997", November 1999, University of Sheffield, School of East Asian Studies.

cent in 1990 (TSE, various years). Foreign companies made unprecedented acquisitions of large stakes in Japanese companies such as Nissan, Mitsubishi Motors or Chugai, as well as bankrupt institutions like the (then nationalized) Long-term Credit Bank of Japan (now the successful Shinsei bank). Finally, the advent of new information technology industries places changing demands on corporate governance.<sup>11</sup> A number of firms are now listing on U.S. stock exchanges thus requiring Japanese firms to comply with disclosure and other Anglo-American securities environments, thus imposing greater transparency obligations on the latter. However, there continues to exist a vast number of companies who continue with their existing norms and governance structures.

### **Economic Recession and the Asian Financial Crisis**

The impressive view of Japanese corporations being ‘society- friendly’ has been seriously tested by the collapse of the bubble economy in the beginning of the 1990s, which has been followed by a long period of economic stagnation for most of the past ten years. Also, the Asian Financial Crisis and the inability of the banks to rescue the corporations that faced an imminent risk accelerated the process of change in the corporate governance norms. The bad loans faced by the banks and the excess capacity in the corporate sector casts doubts on how effectively banks monitored the corporate sector. The concentration of bank loan portfolios shifted then towards medium-sized and smaller corporations whose low credit quality limited their access to securities market. Firms associated with the main bank system went through larger stock prices decline as compared to the more independent ones and thus became less profitable. The previous rescue mechanisms between the banks were no longer possible because of their collective economic vulnerability. Thus the trend that has been adopted by the banks to save their reputation is mergers of banks since in Japan an amalgamation between a bank and a non-bank corporation is not permitted. Further, the establishments of new banks such as the Sony Bank has created normative pressures on the existing banks in terms of their economic viability and hence their existence. The new banks that have been established are not committed to the norms of rehabilitation of the corporate firms. The increased

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<sup>11</sup> *Ibid.*

awareness and realization that profitability has to be restored back has led to the changes in the regulatory environment and business practices aimed at restructuring the corporate structure by improving the corporate governance and shedding excess assets. Also, Corporate Social Responsibility concept has an overlapping with other concepts such as corporate citizenship, business ethics and sustainability, which are themselves contestable, and are in a flux today. Banks thus reduced their monitoring role. But an important point, which has to be mentioned here is that it would be unfair to state that the Japanese Corporate Governance system is dysfunctional. Japan's outstanding performances in the past prove that both the economic structure and its corporate governance system have worked extremely well but it does not lead managers to aim towards profit maximization and that is where the corporate governance system clearly lacks. The Japanese managers have been sensitive to quite a number of issues that have been completely ignored by the American counterparts.

### **Demand-Pull and Policy-Push Reforms**

Reforms in terminology of economics can be classified into two classes---Demand-Pull Reform and Policy-Push Reform. Policy push reforms are those initiated by the legislature in a broad sense to change the practice. The demand-pull reforms are those initiated by the business sectors to enable a new practice that could not be done under the current legal rules. Demand-pull reform of corporate law can be categorized into two types. First, some reforms are based on the interests of management or of human capital providers as a whole, particularly in order to protect their autonomy from intervention by outsider investors. The demands of the business sector for reform come mostly from the management and core employees of major publicly held corporations. They have their own lobbying organization, named *Keidanren* (*Keidanren* is the major management organization for large companies. Generally speaking, they represent the interest of traditional big companies) which has a seat at the Legislative Counsel of the Ministry of Justice. Second, some demand-pull reforms target the interests of shareholders and thus increase pressure on management. In either case, most demand-pull reforms take the form of deregulation of mandatory laws and thus enable new business practices. Policy-push reform is largely developed through the legislative process that involves legal

bureaucrats, who are either judges or prosecutors, and academic lawyers. These corporate law reforms can also be categorized into two types: reforms to improve the monitoring management and reforms to protect the interests of minority shareholders. Most policy-push reforms consist of mandatory regulations that have been introduced either to prevent or require business from adopting particular practices.<sup>12</sup>

Japanese legislature introduced new corporate governance schemes by international, particularly American influence, during the period when the malfunction of traditional Japanese corporate governance system turned to be obvious. The historical significance of these reforms is that the legislature finally intervened in the company community centered governance system, which could not be changed without mandatory law approach, from the point of shareholders' interest. These corporate governance law reforms, in spite of their policy-push nature, are expected to have significant effects on practice because not only they force company communities to change their traditional practice, but also they look like being responded to the hidden demand of business sectors.

### **Demand-pull Reforms**

Since the mid-1990s, Japan has adopted a series of legal and regulatory reforms related to corporate governance. A first series of changes concerns the liberalization of how corporate equity is used, such as share swaps, stock options and spin-offs. In Japan, the post-war ban on pure holding companies was removed. It gave the managers a greater scope to actively manage the stock prices. Further, Japan had creditor-oriented accounting principles that stressed conservative valuation and allowed for substantial building of reserves. The second set of reforms thus included introduction of new market-oriented rules that resulted in much greater volatility into corporate balance sheets, since long-term stable shareholdings are now marked to the market price. A third set of changes concern efforts to promote greater transparency and disclosure, as well as

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<sup>12</sup> URL [http://repositories.cdlib.org/cgi/viewcontent.cgi?article=1090&context=berkeley\\_law\\_econ](http://repositories.cdlib.org/cgi/viewcontent.cgi?article=1090&context=berkeley_law_econ)  
accessed on 9<sup>th</sup> January 2006.

strengthen shareholders' rights through derivative suits or removing voting rights restrictions. Also, various measures were passed to strengthen the independence of so-called statutory auditors. Or perhaps more radically, Japanese law now permits the adoption of a US-style board based on committees for nominations, compensation and auditing that have a majority of outside directors on them.<sup>13</sup>

A principal objective of the reforms is to turn Tokyo into a world-class financial center on par with New York and London. Japan's financial system Big Bang will break down barriers between banks, insurance companies, and securities firms; liberalize brokerage commissions and foreign exchange laws; reform the corporate accounting system; open the doors to foreign competitors and new financial products; and institute other measures to deregulate financial markets.

In October 1993, Japan's Commercial Code was revised to reduce the fees required to file Shareholder lawsuits. Such a suit is filed to influence corporate managers who allegedly cause damage to the company. In the next three months as a matter of fact eighty-four such lawsuits were filed. The system of shareholder lawsuits not only encourage managers to avoid grossly wasteful policies, but also, gives the right to shareholders to pursue redress against corporate mismanagement. Also, subtle change in managers' aims and objectives can be achieved from stakeholders' interests to shareholders' interests.

Until 1995, share buybacks were prohibited in Japan. A share buyback allows a manager to signal that future returns are likely to be high. It also lets a manager return capital to shareholders while avoiding the double taxation of dividends. A firm's share price increases in U.S.A. by an average of nearly 2.5% when an open market repurchase is announced. Moreover, the effect increases with the size of the announced buyback. A stark weakness of the Japanese corporate governance system was its inability to monitor managers of cash-rich firms.

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<sup>13</sup> *Ibid.*



Immediately after the prohibition was lifted, more than 270 firms have announced *buyback plans*, representing 20 percent of Tokyo Stock Exchange First Section firms. From 1997 to 2001, two different methods of stock redemption were made available for publicly held corporations. The formal way required a resolution of annual shareholder meeting, but no limitation was placed of number of repurchased stock. For example, Canon, which has more than 40% foreign shareholders, repurchased shares in 2003 for the purpose of “returning free cash flow to the shareholders.” The less formal way only requires a resolution of board meeting, but repurchased stock was limited to 10 % of issued stock. Finally, in 2001, share repurchases become basically unrestricted within the bounds of profit payable as dividend and subject to a few procedural rules. Even the resale of treasury stock was deregulated. From April 2002 to March 2003, 1652 publicly held corporations voted to authorize stock repurchases within certain limits and 972 companies actually repurchased their own stock for a total amount of more than 3000 billion yen.<sup>14</sup>

Corporate law reforms are most often the products of market pressure. The introduction of stock options in 1997 was a particularly symbolic case, as it was the first corporate law reform initiated by a Diet member. In 1997, *stock options* were introduced to Japan. Initially, stock options remained very restricted. For example, issuing stock options was limited either to directors or to employees. In 2001, stock option was totally deregulated (e.g. no necessity of attaching to bonds) and now can be issued to anybody. As a result, stock options can also be used as poison pills although no such cases can be observed thus far. Stock options can be used to provide additional remuneration, thus serving the self-interest of company insiders. But stock options can potentially also help to resolve agency problems by aligning the interests of managers and human capital providers to the stock market. In any case, stock options have become widely used. From their introduction of 1997 through June 2004, some 1303 companies or 36 % of publicly held corporations have issued stock options. Previously, Japanese companies never utilized this type of equity incentive as a scheme for motivating human capital providers because human capital providers were sufficiently motivated by the company community concept

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<sup>14</sup> Shigemi Ozawa, The Situation of Stock Repurchases in 2002, Shinko Research Institute, Jun. 26, 2003

of the traditional J-model. First, stock options are given very widely, not only to directors and officers, but also to core employees. Second, for directors and officers, stock options remain only a small percentage of their total salary. Third, the gap between option price and current price is small. Forth, option term is relatively short, such as around 4 years. And fifth, companies adopting stock options are mostly market oriented and high performance companies, such as Toyota and Matsushita.

### **Policy-pull Reforms**

Policy-pull reforms can broadly be categorized into two categories: corporate reorganization and accounting reforms. The latter include even the financial matters. Both the corporate and accounting reforms are interlinked and could not fulfill the objective of the transparency by ignoring the other. The then PM Hashimoto in 1996 called for thorough disclosure at all levels, from business accounting to government administration, to ensure fair markets, and he urged changes to the legal system related to derivatives as part of achieving an improved international financial market. Rapid deregulation of corporate law commenced in 1997. In 1997, Sony and other several companies with many foreign shareholders started voluntary reform of corporate governance practice. Younger executive directors were demoted to “executive officers (*shikko yakuin*)” and the number of board members was decreased. Many publicly held companies soon followed this reform of “executive officer system (*shikko yakuinn sei*),” Several leading companies even introduced outside directors and a committee system before the corporate law reform of 2002.

Also, the development and growing acceptance of International Accounting Standards had put much pressure on Japan to reform its financial reporting rules and practices. In response to the increasing internationalization of investing and financing the international financial community had then called for harmonization in accounting and financial reporting practices between countries. Harmonization provides comparable information on companies throughout the world and increases the compatibility of accounting practices by setting bounds to their degree of variation. As a matter of fact, only one

Japanese company viz. Sasebo Heavy Industries in the early 1990s had prepared financial statements consistent with International Accounting Standards and by October 1997 the number of companies reporting with International Accounting Standards had increased to only seven.

### **Reforms Relating to Corporate Law**

Corporate Governance of Japan has been primarily guided by corporations law stipulated in Book 2 of the Commercial Code enacted in 1899, the Law for Special Provisions for the Commercial Code Concerning Audits enacted in 1974 and the Limited Liability Company Law enacted in 1938. Corporate reorganization, both within a single corporate group and between different groups, were pushed by intense product market competition as well as by pressures of the stock market. Since 1997, measures to reorganize corporate groups have been rapidly deregulated and a greater variety of reorganization schemes became available for shareholders and management. Friendly mergers and acquisitions were encouraged. In 1997, procedures for mergers and acquisitions were simplified. The Corporation Law (Kaisha-Ho) was enacted on June 29 2005. The enforcement of the Corporation Law is scheduled for the beginning of May 2006.

Under the existing legislation there are four types of companies: -

1. *kabushiki-kaisha* (KK), a joint stock company that is the most commonly used in Japan;
2. *yugen-kaisha* (YK), a limited liability company that is used for small businesses;
3. *gomei-kaisha*, a partnership company with only unlimited partners; and
4. *goshi-kaisha*, a partnership company both with unlimited and limited partners than KK.

Existing legislation classifies KK as a large company, small company or medium-sized company. A large company is a KK with a stated capital of ¥500 million (\$4.1 million) or a total of ¥20 billion or more stated in the liability section of its latest balance sheet. A small company is a KK with a stated capital of ¥100 million or less.

A medium-sized company is a KK that is neither a large company nor a small company. The new piece of legislation has been drafted to modernize the existing law, and is expected to have a big impact on corporate governance. The Corporation Law consolidates YK into KK and classifies KK as either an open company or closed company. The Corporation Law abolishes YK and adds *godo-kaisha*, which is a limited partnership company with only limited partners. It will be impossible to establish a new YK after the enforcement of the Corporation Law. Existing YK may be given the status of special YK.

An open company is a KK without articles of incorporation that provide that a transfer of every class of shares requires the company's consent. Conversely, a closed company has articles of incorporation that provide that a transfer of every class of shares requires the company's consent whether a company is open or closed has no relation to its listing.

The effect of the changes in the structure of the companies can be summarized in the comparative statement given below<sup>15</sup>: -

|                |        |   |
|----------------|--------|---|
| KK<br>Category | Large  | -board of directors + Board of corporate auditor +<br>accounting auditor, or<br>-board of directors+ committees + accounting auditor  |
|                | Medium | board of directors + corporate auditor (medium sized<br>company may select large company structure in the article<br>of corporation)  |
|                | Small  | board of directors + corporate auditor (only accounting<br>audit authority)   |
| YK<br>Category | -      | - director, or<br>-director+ corporate auditor (only accounting audit<br>authority) or<br>-board of directors, or<br>-board of directors + corporate auditor (only accounting<br>audit authority) |

<sup>15</sup> A special IFLR supplement by Nishimura Corp gov dated 8.12.05 page 30, [www.iflr.com](http://www.iflr.com) downloaded on 14<sup>th</sup> Feb, 06

The effect of the changes in the composition for internal control in terms of Board of directors can be summarized in the following table<sup>16</sup>: -

|                                | <b>Existing legislation</b>   | <b>New corporation law</b>   |
|--------------------------------|---|--|
| No. of directors               | Three or more in case of KK and<br>One or more in case of YK  | One or more (company with Board of directors needs three or more directors)  |
| Limitation of directors' terms | -Two years in case of company with corporate auditor<br>-One year in case of company with the committee<br>-No limitation for YK. | -Two years in case of company with corporate auditor.<br>-One year in case of company with committees<br>-Closed company with corporate auditor may extend the limitation to 10 years in its article of incorporation. |
| Qualifications                 | -Not eligible, if bankrupt, or<br><br>-if in violation of corporation law   | -Bankrupt person eligible if not discharged<br>-Not eligible if violated corporation law securities exchange law or bankruptcy law.  |
| Appointment                    | No need of becoming shareholder   | A closed company can insist that a director be a shareholder in its article of corporation.  |
| Removal                        | Two-thirds majority or the votes at a shareholders' meeting through extraordinary resolution.                                     | Majority of voting rights of attendees.  |
| Liabilities                    | -Absolute law basis (company with corporate auditor) or<br>-Negligence liability basis (company with committees)                  | Negligence liability basis.  |

### **Deregulation of Mergers**

One of the two shareholders' meetings requirements of approving for a merger, called "meeting for reporting shareholders," was abolished. Requirements for notify individual creditors were also abolished. And short-form mergers were permitted, whereby the approval of the acquiring company's shareholders is not required if the size of the acquired company is less than 5 % of the acquiring company.<sup>7</sup>

<sup>16</sup> A special IFLR supplement by Nishimura Corp gov dated 8.12.05 page 32, [Web Online] URL [www.iflr.com](http://www.iflr.com) downloaded on 14<sup>th</sup> Feb, 06

Holding companies have also been used as an important means to implement mergers and acquisitions.<sup>8</sup> In Japan, the concept of “company community” is still strong and members of the company community typically resist the idea that their company will be merged to another company and disappear. Merging through the creation of a holding company together was more easily acceptable by company communities.

According to the corporate value report by the corporate value study group established by the MEITI, the number of mergers and acquisitions increased from about 500 per year in the 1990s to 2211 in 2004. Further, Japanese merger activity was approximately 0.4% of GDP in 1990. By 2002, it was 5.5% of GDP. Economic necessity ultimately drove both the legal changes and the increased merger activity, but these data indicate that Japanese market actors responded predictably and significantly to adjustments in their institutional environment.

### **Hostile takeovers**

The very first example of Merger and Acquisitions under this category is that of the *UFJ-Sumitomo* deal in May 2004 where the *UFJ* bank and *UFJ* trust bank jointly as *UFJ* signed a Memorandum of Agreement to sell the *UFJ* trust bank to *Sumitomo* Trust and its affiliated group, and to enter into the business alliance between the two groups. Some of the other such Merger and Acquisitions include Livedoor- *Fuji* T.V. in January 2005, and the famous *Sony* takeover by the BMG Group. The market players in these deals used previously unheard of tactics to achieve their objectives. M&A Consultant’s use of the proxy fight, *Sumitomo*’s bear hug, Livedoor’s unsolicited bid, not to mention the strategic use of litigation in the contests for *UFJ* and Nippon Broadcasting, all marked major departures from the norm in the world of Japanese takeovers. As such, they generated a welter of controversy by creating the impression that a new brand of “American” capitalism was infiltrating Japan.<sup>17</sup> Some view hostile bids as part of the standard

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<sup>17</sup> Singer Jason (2004), “With ‘80s Tactics, U.S. Fund Shakes Japan’s Cozy Capitalism”, *Wall St. Journal*, U.S.A. April 15, 2004.

corporate governance tool kit, with potential to help revive the Japanese economy by moving assets to their most productive uses; others see an undesirable foreign practice that is inconsistent with Japanese sensibilities, and subject to exploitation in Japan's comparatively underdeveloped corporate and capital markets regime.<sup>18</sup>

The recent takeovers have forced Japan's Ministry of Economy, Trade and Industry (METI) to form a group of experts and business representatives to craft a governmental response to the rising tide of hostile takeovers, which finally resulted in the Takeover Guidelines for Protecting and Enhancing Corporate Value and the Interests of Shareholders as a Whole on 27<sup>th</sup> May 2005. The group conveyed that the aim of these guidelines was "to begin developing a framework for fair and reasonable hostile takeover defensive measures that would enhance corporate and shareholder value based on Western measures that are accepted as a global standard."<sup>19</sup> With the second largest economy of the world embracing Mergers and Acquisitions (M&A) the debate that has grappled the business think tanks is whether corporate law and governance structures around the world are converging on a U.S. shareholder-oriented model. Such events give strength to the convergence theories of corporate governance where they opine that the world is increasingly adopting the U.S. practices and norms of the corporate governance. The rise of hostile M&A can be seen as an amalgamation of corporate law developments and the demands of the market and hence the economy. The corporate law developments include some of the above-explained developments while on the other hand demands on the market side include the rise of foreign institutional shareholders, steady decline in the cross shareholdings of the firm and a modest increase in the number of institutional investors.

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<sup>18</sup> See 2005 Nen Tei Rei Yoron Chosa, 3 Gatsu [March 2005 Public Opinion Survey], [Online Web]. Accessed on 18<sup>th</sup> September 2005, URL [http://www.ntv.jp/yoron/2005\\_03/200503/question.html](http://www.ntv.jp/yoron/2005_03/200503/question.html).

<sup>19</sup> "Kigyo Kachi Kenkyu Kai [Corporate Value Study Group], *Tekitaiteki Baishu Boei Saku* (Kigyo Kachi Boei Saku) *no Seibi* [Preparing Defensive Measures toward Hostile Takeovers (Measures to Defend Corporate Value)]" March 2005, [Hereinafter, METI Interim Report], Accessed on 19<sup>th</sup> September 2005, [Online Web] An English summary of the report is available at URL [www.meti.go.jp/english/information/downloadfiles/Corporate%20Value.pdf](http://www.meti.go.jp/english/information/downloadfiles/Corporate%20Value.pdf).

METI established a Corporate Value Study Group composed of legal experts and business representatives to consider an appropriate policy response to hostile takeover activity.<sup>20</sup> The Study Group's interim report, issued in March 2005 followed extensive research and consultations with experts regarding Anglo- American takeover defenses and legal precedents. The principles that the group kept in mind were as follows:

- Enhancement of corporate values,
- Keeping up to the global standards,
- No discrimination between the Japanese and Foreign firms and finally,
- Expansion of choice.

The report begins by noting that no Western country completely lacks defensive measures, because reasonable defensive measures can enhance corporate and shareholder returns. It authorizes defensive measures in response to a threat to corporate policy and effectiveness, provided the response is proportionate to the threat. Finally, the report discusses incorporation of a rule requiring the board to shift from defenders of the corporate bastion to auctioneers seeking the highest price once the board has reached a decision to sell the firm. The report notes that the establishment of defensive measures recognized in the U.S. and Europe can also be implemented in Japan. The report discusses ways in which to ensure and enhance the reasonableness of defensive measures, including retaining the ability of replacing the board through a proxy contest, participation of independent directors and advisors in the formulation of defensive measures, the use of “chewable pills” and shareholder approval. In short, the report represents a major endorsement of Delaware takeover jurisprudence in the formulation of Japanese policy, down to doctrinal nuances such as disallowance of dead hand pills. The report also notes existing Japanese law offers more flexibility to shareholders in that staggered boards are not used because directors' terms are limited to 1-2 years, and there is no restriction on removing directors mid-term.<sup>21</sup>

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<sup>20</sup> *METI Interim Report* of March 2005.

<sup>21</sup> *Ibid.*, pp 12-30.



### **Share-for-Share Exchanges (Stock Swaps)**

In 1999, share-for-share exchanges were introduced to facilitate the creation of holding companies. Stock swaps now give Japanese companies a new convenient tool for mergers and acquisitions. Listed companies can acquire other companies without using cash. A major case using share for share exchange was made between two famous photograph companies: Konica and Minolta in 2003. Sony, and Cannon also took advantage of their high price stock for acquiring other companies. This new scheme can also be used for creating wholly owned subsidiaries by making acquired company's shareholders to be parent company's shareholders without their agreement. Until September 2002, 18 quasi-mergers were either made or announced to be made by creating a holding company together (Miyajima & Inagaki 2003).

### **Corporate Divisions**

In 2000, another new convenient tool for reorganization of corporate groups and mergers and acquisitions was introduced. The newly implemented legal scheme of corporate division, which is German origin, can be used for various purposes: creating wholly owned subsidiaries, creating and dissolving joint ventures, American type spin offs and split offs, transferring a business unit to another company, etc. (Takei & Hirabayashi 2000). Corporate divisions are frequently used for creating wholly owned subsidiaries because the new scheme can skip the inspection by the court on transfer of business to a newly created company, which is ordinary required by the Commercial Code.

### **Reforms Relating to the Accounting Matters**

In 1997, consolidated accounting was required by the Securities Regulation, and, in 2002, it was also required by the Commercial Code. Consolidated accounting was significant change in the Japanese management and investors who used to appreciate the performance of management by individual company basis. In the Commercial Code

Reform of 1999, market-to-market accounting for financial assets was required. This reform had a significant impact towards the dissolving cross shareholding.

Between June 1997 and January 1999, the government announced details of an '*Accounting Big Bang*' that involved sweeping reforms of financial reporting and accounting regulations. Nearly all of these changes were implemented between fiscal years 1999 and 2001. In 1997, restrictions on the asset allocation of corporate pension funds were removed. Management of corporate pension funds is no longer restricted to trust banks and life insurance companies. Also, restrictions on investment in foreign mutual funds have largely been removed. Changes have been observed with the examples of foreign mutual fund companies having established Japanese operations to sell investment trusts. For example, Fidelity opened an office in Tokyo in June 1997 to prepare for direct sales of investment trusts to individuals following deregulation. Japanese and foreign banks and securities firms have set up investment advisory firms to manage pension fund investments and the funds entrusted to these firms have been growing rapidly.<sup>22</sup>

The Business Accounting Deliberation Council issued in June 1997 *a new standard on consolidated financial statements*, which requires that a company's extent of control or influence, rather than only the previously used shareholding percentage, be used as an additional criterion to determine whether a subsidiary must be included in the consolidated financial statements or whether the equity method of accounting must be applied to affiliates. These changes in consolidation accounting rules took effect for the fiscal year ending March 31, 2000. Consolidated financial statements thus replaced single-entity financial statements as the main financial reporting in annual securities reporting as well as registration statement reporting under the Securities and Exchange Law.<sup>23</sup>

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<sup>22</sup> A giant sucking sound," *The Economist*, August 23, 1997, pp. 53-54.

<sup>23</sup> D. Gordon William (November 1999), "*A Critical Evaluation of Japanese Accounting Changes Since 1997*", University of Sheffield, School of East Asian Studies.

In early 1998, the Diet approved *establishment of the Financial Supervisory Agency*, a governmental body independent of the Ministry Of Finance and reporting directly to the Prime Minister's Office. The Financial Supervisory Agency began operations in June 1998 by taking over from the Ministry Of Finance the regulatory functions of supervision and examination of private-sector financial institutions, with the Ministry Of Finance continuing to be responsible for planning and formulating policies for the financial and securities system. The Ministry Of Finance's other responsibilities, such as control of corporate financial reporting requirements remained the same.<sup>24</sup>

In June 1998 the *Laws for Financial System Reformation* were passed, achieving an important part of the Big Bang. These laws amended the Banking Law (*Ginko Ho*), the Securities Exchange Law (*Shoken Torihiki Ho*) and the Law for the Insurance Industry (*Hokengyo Ho*), with a view to promoting market competition and protecting end-users (particularly individual investors) from undue risk. Formally, these amendments were based on reports submitted a year earlier by Ministry Of Finance's prestigious advisory councils.<sup>25</sup>

Today the Japanese banks are very cautious about their clients. There has been ample erosion of the bank-firm relationship in the blue-chip firms rather than the other firms but the market operation of the firms has shifted towards the other sectors and thus the banks are unlikely to regain their past monitoring capacity with regard to very large firms.

### **Reforms Related to Corporate Governance**

Corporate Governance Forum of Japan (1998) is one of the few groups that laid stress on the corporate governance system. Their "Corporate Governance Principles" call for Japanese boards to:

- Include a majority of independent, non-executive directors,

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<sup>24</sup> Ibid

<sup>25</sup> Horiuchi Akiyoshi (2000), "After the Big Bang: Heading for a Transparent Financial System", University of Tokyo, Australia Japan Research Centre, Pacific Economic Papers.

- Be clearly separate from the executive board that is responsible for execution of business activities, and
- Separate the positions of Chair of the Board and Chief Executive Officer.

There are **three major characteristics of the new board system** with committees being compared with the traditional board system with statutory auditors.

First, the new system is much clearer in distinction between day-to-day management and monitoring than the traditional system. While in the traditional system, every management must be a director, in the new system of management, the incumbent of a post, which is called an officer, is not necessarily a director. Second, outside directors, who are never been employees and officers<sup>15</sup>, are expected to play an important role of the corporate governance. Outside directors must be the majority in all three committees: audit committee; nomination committee; and remuneration committee, whose decisions are final and even the Board of Directors cannot change them. And third, management has wider discretion than its counterpart in the traditional system. In the traditional system, the board of directors must decide a lot of business decisions, such as sale of important assets and issuing new stock, because it is the managing board. On the other hand, in the new system, the board of directors can delegate many day-to-day management decisions to the management (officers) and the board can concentrate on major policy decisions, which are indispensable for monitoring management. Therefore, these reforms as a whole, which made outsiders (either as real members or as quasi members) in the board mandatory, were typical policy push reforms.

In November 2002, the statistics indicates that, among 1363 companies, 494 (36.2 %) companies decreased the number of directors, 466 (34.2 %) companies adopted the executive officer system, 388 (28.5%) companies elected outside directors, 54 (4.0 %) companies adopted remuneration committees, and 33 (2.4 %) companies adopted nominating committees.<sup>26</sup>

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<sup>26</sup> According to the interview by mail research by Tokyo Stock Exchange, [Online Web] URL <http://www.twe.or.jp/listing/cg/enquete/index.html> , Accessed on 5th December 2006.

## **Reforms Related to Shareholders' Interests**

To insulate the banks from stock prices volatility, section 3 of the Act of Limitation of Bank's Holdings of Stocks from 30<sup>th</sup> September 2002, placed a limitation on the amount of the shareholdings of banks, banks' subsidiaries, and bank holding corporations. The affiliated ministries in the form of ordinances issued detailed methods of counting and valuation. Unfortunately, this had a depressing effect on the stock market. Banks, thus, have been unable to retain their shareholdings due to the low market price that resulted because of the change in the accounting methods and due to the inability to compete internationally. The solvent corporations to reduce their dependence on banks for the investment capital are shifting their debt to equity ratios. The banks in turn are turning towards developing a greater dependence on relationships with less successful corporations.

Further, the Securities and Exchange Council's report called for full and transparent disclosure through consolidation and fair-value accounting principles in order to provide investors sufficient information to properly assess the risk and return of potential investments. The Council also urged the improvement and strengthening of the review by Certified Public Accountants in order to improve corporate governance. Recognizing the need for investors to easily obtain disclosed information, the Council advocated providing information through the Internet.<sup>27</sup>

The proportion of cross-shareholding has also declined, and ownership by foreign and domestic institutional investors is increasing. Foreign and institutional investors are less concerned about long-term business relationships and are focused more on stock market returns. Moreover, these new shareholders are playing a much more active role in corporate governance. While shareholder activism by foreign institutional investors is well known, domestic pension funds in Japan have also become more interested in exercising voice in corporate governance, as reflected in the surprising increase of "no" votes cast at shareholders' meetings. Further, the center of attraction of the legal reforms

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<sup>27</sup> *Ibid.*

has been the introduction of the committee system that allows firms to adopt a “US-style” board system that uses committees with a majority of outside directors<sup>28</sup> (Commercial Code amendments in the year 2003). The revisions to the Commercial Code became effective since 1<sup>st</sup> April 2003. Through the provisions of the amendments strengthening corporate bonds is to be achieved by increased use of outside directors and other measures to enhance board oversight of Japanese corporations. Amendments as effective of May 2002 had set new limits of director liability, depending on whether a corporate officer is an inside or outside director (Amendment to Commercial Code, 2001).

### **Strengthening Statutory Auditors**

The position of statutory auditor in Japan has a long history dating back to the Commercial Code (CC) enacted in 1890. The CC and SEL require a company’s statutory auditor to review the company’s financial statements and to verify the adequacy of internal controls, but the statutory auditor’s professionalism and credibility are questionable since the law does not require specific qualifications, such as accounting or auditing education or experience, for the position of statutory auditor. In 1993, the CC was amended to require a large company to have at least three statutory auditors, with at least one of them being a person not employed by the company or any of its affiliates within the prior five years. However, even with this requirement, insiders continue to dominate statutory auditor positions, with a company very easily able to nominate ‘outside’ candidates who will suppress their own opinions and follow the company’s direction. The majority of these so-called ‘outside’ statutory auditors come from the ranks of former company directors or employees or from the company’s correspondent banks.

The statutory auditor system was strengthened again in 2001. It is true that the history of Japanese corporate governance law reform was the history of strengthening statutory auditors (Shishido 2001), and the reform of 2001 was the most fundamental changes among them. By this reform, Japanese large companies must have “real” outside auditors

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<sup>28</sup> *ibid.*

who must be at least half of all auditors after May 2005. A Japanese large company has to have at least two outside auditors and provably two inside auditors because the company community would never want an outsider majority auditors board.

### **Changes in Corporate Pension System**

Japan's population is in decline. Deaths have outstripped births for the first time in a period of peace since records have been kept. There is no change in the current fertility rate below 1.3 children per woman of child-bearing age. Experts have predicted Japan's population to be as low as hundred million in the year 2050. Japan is greying at an unprecedented rate. Half a century ago, the proportion of the population over 65 stood at around 5%, well below that in America, Britain, France or Germany. Today, Japan's proportion of elderly, at 19%, is the highest in the world, and is forecast to reach almost 30% by 2025. In particular, an exceptionally large group of Japanese, the baby-boom generation, is making its way towards retirement.

At present, some sixteen million Japanese are in their twenties, many of them children of baby-boomer parents. But the number in this age bracket will shrink by about three million over the next decade. The consequence of all this is, first, that fewer workers will support an ever growing number of non-workers, other things being equal; and, second, that the demographic shape of the workforce is assuming that of an inverted pyramid, with fewer young workers at the base where once there were many. These factors combined lead some commentators to speak of dire consequences: of a national malaise led by a decline in living and even educational standards, accompanied by a government bankrupted by retirement obligations.<sup>29</sup>

The size of Japan's social security benefits was 83.6 trillion yen in 2002, or 23.03% of the national income. Corresponding percentages (based on International Labor Organization standards) were 16.43% in the United States (1995), 37.68% in Germany (1996), and 44.00% in Sweden (1996).

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<sup>29</sup> 'Graying Japan: The Downturn', *The Economist*, 5<sup>th</sup> January 2006.

Corporate firms and the Government have already started replying to the changed demographic situation because with an ageing population and decreased young working crowd, there would be few to contribute to the pension structure and many to avail the benefits. The situation will worsen in the background of the economic recession, where corporates would have less to contribute and same would be the situation of the government. The sub section of the chapter focuses as to how reforms in the pension structure have been brought about to adjust in accordance with the changing scenario and also with the changed management practices in hand.

### **Process of Bringing Pension Reforms**

In Japan, the law requires a regular review of the pension system at least once every five years. This is one of the highly original features of the pension situation in Japan. The process of review and reform is mainly performed by the Pensions Office (*nenkin kyoku*) in the Ministry of Health and Social Affairs. It normally takes two years and follows a timetable that is repeated from one reform to another. It begins with the creation of a Pensions Advisory Committee (*nenkin shingikai*) composed of representatives of the civil service, academics and civil society (in the shape of employers' organizations and trade unions). The idea is that the officials in charge of the review can consult the users; but the former nevertheless retain a considerable degree of control over the process, and in particular produce the final report. Based on this report, and in close liaison with the ruling party, the Liberal Democratic Party (LDP), the Pensions Office drafts a bill for debate in Parliament.

### **Basic Structure of the Japanese Pension System**

The Japanese pension system is multi-tiered, consisting of public and private pension schemes. The distinction between public and private pensions depends on whether the insurer of pensions is the government or not.

The first tier is the Basic Pension (public), which provides the flat rate basic pension of a universal coverage. As a non-income-related pension, it works for income redistribution, and participation is mandatory to all residents. The coverage of the Basic Pension is



universal, i.e. it extends to all residents 20 years old or above in Japan including foreigners. However, the eligibility to receive pensions requires a minimum of 25 years of premium payment. The first tier is operated by municipalities and is called National Pension.

The second tier (public) covers most of employees and provides an income-related payment. It is mandatory to all firms over a certain size, and employers and employees share premium. The second tier i.e. (Employees' Pension Insurance) is managed by social security administration associations within a firm or a group of firms.

For convenience, the first and second tiers for employees are jointly operated by these associations and are sometimes jointly called Employees' Pension Insurance. The Employees' Pension Insurance covers both employees and their spouses. Thus, the National Pension insures either by the Employees' Pension Insurance, or the entire adult population, in principle.

The third tier is an optional scheme for larger pensions. It is private or public and is provided either by private firms (employers) for their employees, or by collective national pension funds for the self-employed with the government as the insurer.

### **Types of Pension Schemes**

Two types of pension schemes exist in Japan: National Pension and secondly, Employees' Pension Insurance. As described above, all residents in Japan between ages of 20 to 60 are eligible and required to become subscribers of the Basic Pension. Whereas employees automatically enroll in the Basic Pension when they subscribe to the Employees' Pension Insurance, the National Pension is for those who are not employees.

The Employees' Pension Insurance forms the core of the income security for retirees. All workplaces with more than 5 employees and their employers are required to participate in this scheme. Both employers and employees contribute 8.68% of employee's salary as premiums (including a premium for the National Pension), and the pension payment is income-related.

## **Corporate Pensions and Retirement Allowance**

A need for corporate governance by pension funds and reforms in the public pension fund scheme was felt with the growing health and medical need of the ageing population, and also with the sluggish performance of the government. Managers of corporate pension funds were lately being expected to take their responsibility to subscribers and beneficiaries in terms of diversifying portfolios and enhancing the value of their assets.

In 1990, the ban on the entrance of financial advisers into trustee business was lifted. Since then, newcomers have rushed into this fields and liberalization of asset allocation has contributed to promoting competition among trustee bodies for their customers' benefits. Among trust banks, life insurance companies and investment advisory companies, competition for trustee business became fierce due to an increase in suppliers as well as stronger demand for more efficient and more transparent portfolio management from pension funds.

With the "Financial System Reform Law" into force since 1993, trust banks and insurance companies became exposed to fierce competition with newcomers on the performance of managed funds. As agents of individuals and pension funds, they had to clarify their policies as trustees and work on behalf of their customers if they have business with corporate pension funds. Thus, pension funds and other leading investors were expected to play a new role in monitoring companies as outsiders in the Japanese corporate governance.

90% of all Japanese firms offer retirement packages for their employees. A retirement package can be either a one-time lump-sum retirement allowance, or a life-long pension, or both. In 1997, about a half (52.5%) of firms with some kind of retirement package offered a pension scheme, while nearly 90% provided a lump-sum allowance. Even though pension style is gradually spreading its share, the traditional style of lump-sum allowance is still the main stream and most employees choose to take a part or whole of retirement money as the lump-sum payment. Thus, public pension, private pension and

lump-sum retirement allowance, all together make up the total income maintenance support for a retiree.

### **1990s and Pension Reforms**

Due to the ongoing economic crisis of the 1990s, the Japanese Government decided in December 1998 to temporarily freeze increases in social security contribution rates for pensions for some years from fiscal year 1999. Also, investment funds were relatively stagnant and significantly decreased throughout the 1990s. Investment funds are especially useful measures for individuals in terms of efficiency of risk diversification and liquidity or tradability in the market. Also, there were regulatory constraints on pension funds. A strict portfolio regulation was put on the corporate pension funds. The fund-managers were allowed to invest only a limited part of their funds into risky assets, including stock-investment funds. Thus, defined contribution pension funds scheme was not introduced in 1990s.

The discussion that Defined Contribution plans were needed in Japan began from the side of employers around 1996 or 1997. Due to the poor investment environment that began with the economic recession, employers had to make additional contributions to existing Defined benefits plans are to cover promised benefits to employees, with the reality being that the employers have difficulties in doing so due to the poor economic conditions. Further, due to the new accounting rules, (similar to Financial Accounting Standard No. 87 in the U.S. that took effect in March 2001) there is a new provision that the under funded defined benefit plans come under the bracket of liabilities on the firm. Besides that the liabilities of book reserve lump-sum retirement plans have ample capacity to downgrade of credit ratings due to the negative effects on the company's balance sheet, which can finally reduce the stock price of a firm considerably. As a result, many employers wanted to replace current defined benefit plans with defined contribution plans so that their problems reduce to some extent. Thus, the employers want to shift the investment risks from their shoulders to that of the employees. Further, with the continuing economic recession and adverse investment environment, the defined contribution plans are considered to suit the needs of the small and medium enterprises.

The Business Accounting Deliberation Council issued in June 1998 its opinion on accounting for pension benefits, which went into effect since the fiscal year beginning after March 31, 2000. This pension accounting standard requires the recording of pension costs and liabilities on an accrual basis, which means companies will record pension expense regardless of the contributions they make to the pension fund. Companies must determine the net pension liability (or asset) to be recorded on the balance sheet by using fair-value accounting for pension fund assets and by employing present-value actuarial calculations on the pension liability. These changes generally bring Japanese pension accounting into line with international accounting standards and will enable meaningful comparison between Japanese companies, although some minor differences exist such as the International Accounting System requiring a maximum of five years for amortization of prior service cost rather than the less stringent 15 years allowed by the Business Accounting Deliberation Council standard.

In July 1999, the government submitted the 1999 pension reform bill to the parliament, which was passed in March 2000. The March 2000 pension reform in Japan focused on the long-term financial sustainability of the country's pension system. The government opted for incremental changes in order to maintain pension solvency through 2060. The change introduced was aimed to reduce future pension funding liability by an estimated one-third.

From the view point of the human resource management, since a large number of companies have given up the seniority based wages and promotions and have in effect switched over to performance based wages and individual evaluation for promotions, the traditional retiring plans favoring the long time workers are not in accordance with the new economic environment. Further with the labor market getting mobile with the change in hiring and recruiting practices, employees with short tenure of service are on the receiving end with the traditional retirement plans since the latter favors the long time workers. Defined contribution plans are said to be the best when a need to attract the new workers was being felt.

The number of corporate pension funds dissolved in fiscal 1999 hit a record high at 3,603. This was attributable, among other things, to a declining yield from fund reserves, and to the increased number of bankruptcies. The numbers of corporate pension plans have been on a continuous decline since 1994, and one reason for this is the increasingly low yield from fund reserves. This has resulted in a shortfall in terms of the benefits that must be paid, and many firms are no longer able to cover the shortfall. Moreover, the amount that private firms have had to pay in premiums to make up such shortfalls totalled a record ¥1.015 trillion in fiscal 1999. A number of corporate pension funds were given up because of increase in bankruptcies.

Such terminations of the pension funds have also been brought about by the new accounting standards that have come into effect which directly require enterprises to reveal their financial affairs so that their capital position is readily apparent. In relation to the specific issue of corporate pension fund, the total liability for pensions will be included in the account for each firm, and poor performance in pension funds will negatively affect firms in terms of their corporate ratings and make it harder for them to raise funds. Accordingly, many firms are making up the deficiency in their pension fund reserves when they can afford it, and dissolve their corporate pension funds when they cannot.

The termination of corporate pension funds means that employees, who in theory participate in the funds, receive upon retirement lump-sum payments whose amount is linked to their tenure, but no extra retirement payments. Moreover, such payments are tax-exempt if workers receive them as retirement pension, while simple lump-sum payments are not eligible for such exemption.

Changes in the pension structure (1999-2000 and 2004) have affected both the changes in the management practices as well as a change in the corporate governance aspect of Japan. A new pension contribution system modeled after the 401(k) plan in the United States was introduced in 2001. This allowed the employees to contribute a portion of their compensation, before income taxes, to a company-sponsored retirement plan. Under

the new scheme, the employees decide how the contributions are to be invested, and continuity is guaranteed when they change jobs. The main provision of the reform was that the normal pensionable age for earnings-related old-age benefits was increased step by step from age 60 to 65 for men from fiscal year 2013 to 2025. The phasing out of earnings-related old age benefits for female employees in their early 60s was delayed by five years starting only in 2018.

Further, an earnings test for those aged 65 to 69 was introduced from fiscal year 2002 and increases in earnings-related old-age benefits for delayed retirement between ages 65 and 69 were abolished accordingly. Also, Employers have been exempted from paying their share of social security pension contributions for their employees on child-care leave from fiscal year 2000. The rebates on contributions for contracted-out schemes have been frozen from fiscal year 1999. Moreover, The benefit/contribution base has to be shifted from monthly standard earnings to annual earnings including semi-annual bonuses from fiscal year 2003. By these measures, aggregate pension benefits will be reduced by 20 per cent by 2025. As a result, the anticipated contribution rate for private-sector employees will peak by 2025 at 25.2 per cent, instead of 34.5 per cent without the reforms.

The defined contribution plan in practice is different from the US provision. There are two types of defined contribution plans, viz., Employer-sponsored Type, and the other is Individual Type. An individual can participate in either of them, and one cannot participate in both of them at the same time. However, not all Japanese can participate in defined contribution plans. Public employees and housewives (to be precise, dependent spouses of employees) are not eligible for participation. Moreover, Private employees are eligible for Employer-sponsored type if their employer sponsors defined contribution plan. The main differences between the Japanese Plan (employer contribution type) and the U.S. plan are as follows:<sup>30</sup>

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<sup>30</sup> Power point presentation of Bank of Tokyo- Mitsubishi on Defined Contribution Plan in Japan on 14<sup>th</sup> December 2004.

|  | <b>Japanese Plan (employer contribution type)</b>  | <b>U.S. Plan</b>  |
|--|--|---|
| Participation:                               | Mandatory. Employer contributes for all employees who meet requirements; employees contribute at their discretion. | Voluntary. Employees may contribute voluntarily, to which employers may add matching contributions.   |
| Inclusion in Expenses:                       | ¥552,000/year for employees not in the defined benefit plan; otherwise ¥ 276,000/ year.                            | 25% of the employee's early salary.   |
| Untaxable limit of Employee's Contributions: | Unable to contribute.  | Upto \$ 11,000/ year.   |
| Early withdrawal (during participation):     | Prohibited, except in the case of death or some serious injury.  | Prohibited, except in the case of death, serious injury, poverty, early retirement (fifty five years of age).   |
| Loans:                                       | Not included, but, probably prohibited.  | Allowed.  |
| Initiation of Benefit Payments:              | After sixty years of age and before seventy years of age.  | After 59.5 years of age and before 70.5 years of age.   |
| Beneficiary Right of Employer Contributions  | Employers are entitled to receive full benefit after three years of employment with the same employer.             | After five years of employment, the employers grant 100%; after five years, 20%, which may increase by 20% each year, until the 7 <sup>th</sup> year of employment. |
| Participant's qualifications:                | All employees under sixty years of age who work for a company, which uses the defined employer contributions.      | Employees over twenty-one years of age who has been with an employer for more than one year.  |

|                                     |            |  |
|-------------------------------------|------------|--|
| Prohibition against Discrimination: | Undecided. | It is required that high-salaried employees be informed that it is not advantageous to them, in terms of contributions before taxes. |
|-------------------------------------|------------|--|

Employer-sponsored Type is similar to money purchase plans in the U.S. Contributions come only from employers, and the amounts of contributions are fixed regardless of employers' profits. Employees cannot contribute to the plan from their pay. On the other hand, in Individual Type, employees or self-employed can contribute to the plan from their pocket money at their discretion. It is similar to 401(k) plans or IRA in the U.S. But employers cannot make matching contributions to Individual Type defined contribution plans. This is the different feature from 401(k) plans.

The main differences between the defined contribution and defined benefit plans are summarized as follows<sup>31</sup>:

|                       | Defined Contribution Plan  | Defined Benefit Plan   |
|-----------------------|--|--|
| Future Benefit Amount | Not fixed in nature and the pension benefits vary in line with accordance with the investment performance. | Fixed in nature and the pension benefits can be calculated in advance.   |
| Investment Risk       | Participants take the risk. Obligations of additional contributions are not on the company's shoulders.    | Company takes the risk. Burden for additional contributions is due to the deterioration of investment performance is on the company's shoulders. |

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<sup>31</sup> *Ibid*



|                                      |   |   |
|--------------------------------------|---|---|
| Monitoring<br>Balance of<br>Accounts | Employees have the power to access their accounts at any point of time in their, even during the middle bracket of their job. | Employees under any circumstances cannot have access to their accounts. |
| Portability                          | Available.  | Not available.  |

The new pension accounting standard provides a hardship exception that allows companies to extend implementation until fiscal years beginning after March 31, 2001. The standard states the exception applies to companies with hardships in applying the standard by the required date because of problems in arranging for actuarial services. However, companies must still publish the pension liability and other details in their financial statement footnotes for fiscal year 2000, even though they are not required to reflect the pension liability on the balance sheet and pension expense on the income statement.<sup>32</sup>

The beginning of the fiscal year since 1 April 2000 saw market- to- market evaluation or accounting for the corporate pension funds. Until the above date, pension fund investment advisors were not evaluated on the performance of the investment they selected. Since the pension funds sponsors didn't mark their portfolios to the market, investment performance was not given ample weightage.

Reforms in the pension sector were again brought about in the year 2004. The 2004 reforms were based on the premise that existing pension programs would be maintained separately. These involve (1) *kosei* (welfare) corporate employee pensions, (2) *kyosai* (mutual aid) pensions for civil servants and private school teachers, and (3) *kokumin* (national) pensions for self-employed people and others. Systemic differences exist in premiums, benefit levels and reserve management.

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<sup>32</sup>*ibid.*

Funding has occupied the most important issue of the latest reforms. The House of Representatives passed “Pension Reform Plan” on 1 October 2004. The 2004 reforms have called for an increase in the government share of contributions to the basic (national) pension fund from one-third to one-half. Extra revenues are to be raised through tax increases. That may not suffice, given the steady rise in the number of pensioners. The reforms in 2004 have tried to address the following issues:

1. Adapting the social security pension schemes to the changing life style of the people, especially that of women,
2. Improving the organizational structure of investing and managing the reserve fund of the social security pension schemes and,
3. Neutralizing the financial relationship between the Employees’ Pension Insurance (EPI) scheme and the contracted out portion of the Employees’ Pension Funds, and increasing the upper limit of contributions to the defined-contribution pension plans.

### **Reforms in Postal Services**

The recent developments in Japan have addressed the question of the retention of the main public financial institution i.e. Postal Services. At present the Postal Services Department contains \$3+ trillion, the privatization of which will have a significant impact on the financial markets. This has been the most ambitious goal of the PM Koizumi who on not being the privatization bill passed in the upper house of the Diet had dissolved it and took the country to the polls. The bill had narrowly passed the lower house of Parliament in a 233-228 vote, amid much disagreement within Koizumi’s ruling Liberal Democratic Party (LDP). Before the polls in September, the Japanese cabinet adopted the basic principles needed to privatize Japanese postal services over a ten-year time frame. Under this plan, Japan Post's four areas of service - mail delivery, management of post offices, savings deposits and life insurance - will become separate businesses in

April 2007. Progressive privatization will then occur over the following decade. Stakes are high since the Postal Savings System (PSS) is currently the world's largest bank. It holds more than 119 trillion yen (US\$1 trillion) in insurance deposits and around 211 trillion yen (close to US\$2 trillion) in savings deposits.

PSS was established in 1875. Before the 1970s, it became the country's strongest player, as the banking and insurance sectors were weak and fragmented. Deposited funds were invested in infrastructure projects, such as building highways, railroads, electric power systems, hospitals, and schools.

After the mid-1970s, Japan's private banking sector matured. Competition lessened the monopoly power of the state-run PSS, and infrastructure projects were able to borrow funds from the private sector. Funds from PSS were used in projects that did not bring real value to the depositors, such as the tunnel bridge across Tokyo Bay; many of these projects will not be able to repay the loans, as there is no substantial income to be expected.

Beginning in 2001, PSS was allowed to control investment of its own funds without political interference, reforms in the same are aimed to be completed by the year 2017. PSS has become obsolete as a funding institution for Japan's infrastructure projects, although it remains strong as a trusted bank for the Japanese.

Privatization of Japan's Postal Saving System can be expected to lead to the development of more sophisticated and efficient financial and capital markets in Japan. This is true because funds that were previously directed into the public sector will then be channeled into the private sector where they can be used to revitalize existing firms and to support the needs of emerging companies.

If the Japanese public abandons the caution fostered by unlimited government guarantees and preferential tax treatment for Postal Saving System deposits, and begins to invest their savings in private banks and other investment vehicles -- the country's economy will never be the same. Huge amounts of pent-up capital would then be moved into private

financial markets. This would help to bolster not only Japan's incipient economic recovery but also, over time, financial markets around the world.

Postal Saving System privatization will also push Japan to more efficiently allocate capital and account for risk. The government will be forced to become more fiscally prudent. Since the postal service would no longer be required to purchase government securities, Japanese Government Bonds (JGB) would have to be sold to private investors. They are less likely to be forgiving about chronic budget deficits and will need to perceive a risk-reward ratio that effectively balances the ability of JGB's to provide stability, liquidity, diversification and Yen exposure with the interest rate that is provided.<sup>33</sup>

### **Conclusion of the Chapter**

The entire world learnt Japanese Management Practices and the corporate governance that were human-resource centric as well as customer oriented. The challenges thrown by Japan's post World War II status were to shift from Command to Orientation proactive collaboration, from Specialization to Multitasking Part-time work, from Individual to Organizational objectives and creation of integrated team networks based on autonomy and flexibility besides achieving innovation creative group synergy. Modern concepts such as motivation, leadership, communication, interpersonal relationships, and development of high-performance, cohesive work teams, collective risk sharing, Quality Circles, multifunctional groups, autonomous teams, task forces, and encouragement of Intellectual Capital have been taken from Japan but the utility of these practices lie in Participative decision-making, continuous consultation, opportunities for dialogue, direct and open communication, suggestion programs, use of meetings and awards ceremonies, more freedom in task selection and the methods to carry them out, group work and teamwork, work schedule options etc. In the new economic order the paradigm shifts are from the Industrial Age to the Information Age, from Restricted Markets to

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<sup>33</sup> For more information on privatization of the Postal Services please see the newsletter released by JETRO, [Online: Web] Accessed on 30<sup>th</sup> October 2005, URL <http://www.jetro.go.jp/usa/newyork/focusnewsletter/focus37.htm>.

Globalization, from Stability to Change, from Intellectual Capital to the Financial Capital and from present to the future. The challenges posed by the new millennium are so complex that online information, real-time projections, remote and virtual work are gradually overshadowing the traditional Japanese Corporate System and compelling them to adopt the western system of corporate governance. Ironically these measures are being called “REFORMS” because the compulsions are to attract the Foreign Investment, to compete globally and to fall in line with rest of the world.

A White Paper from The Business Roundtable in May 2002 clearly states, “It is the responsibility of management to operate the corporation in an effective and ethical manner in order to produce value for stockholders. Senior management is expected to know how the corporation earns its income and what risks the corporation is undertaking in the course of carrying out its business. Management should never put personal interests ahead of or in conflict with the interests of the corporation”, as one of the principles of corporate governance.<sup>34</sup>

According to Akiyoshi Horiuchi in his paper, “After the Big Bang: Heading for a Transparent Financial System” some of the major issues that still remain to be addressed are as follows:<sup>35</sup>

**1. The question of Free Exit:**

A competitive financial system requires not only free entry, but also free exit of inefficient intermediaries. However, the recent mix-up over the procedure for dealing with distressed banks shows that Japan’s financial system is not well prepared for the exit of inefficient financial institutions. Further, unlike in the United States, Japanese law does not differentiate between bank failures and those of other companies. Moreover, there exists no legal principle of giving priority to

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<sup>34</sup> “Principles of Corporate Governance”, May 2002, White Paper from The Business Roundtable, An Association of The Chief Executive Officers Committed to Improving Public Policy.

<sup>35</sup> Horiuchi Akiyoshi (2000), “*After the Big Bang: Heading for a Transparent Financial System*”, University of Tokyo, Australia Japan Research Centre, Pacific Economic Papers, 2000.

deposit liabilities over other debts in the case of bank failures. Under the current legal system, Japan's pay-off cannot be finished within a few days, as is possible in the United States. A prolonged pay-off would further reduce confidence in the financial system. Thus, to meet its commitment, the government will have to substantially amend the laws concerning bank failures.

**2. The question of efficiency of the new Financial Agency:**

The Big Bang plan assumes that financial markets will work efficiently. However, it does not eliminate the role of the government in the financial system. The separation of the supervisory authority from Ministry of Finance, which now concentrates on fiscal matters, was necessary but the issue remains as to how to motivate the Financial Supervisory Agency to work efficiently. It is probably necessary for the agency to disclose its activities according to a specific format, as this would prevent deviation from its designated role.

**3. Ability of the infrastructure to adapt to the Financial Reforms:**

Financial markets rely on infrastructure such as clearing systems to achieve efficient transactions in financial markets, but some infrastructural problems remain. For example, the clearing systems in Japan's securities markets have been technologically separated. The clearing systems for government bonds, stocks, corporate bonds and commercial paper have functioned almost totally independently from each other. This situation is inconvenient for investors and needs to be rectified if securities markets are to be efficient and competitive.

It will not be as easy as foreigners may expect to establish a unified clearing system covering the entire Japanese securities market. The equilibrium among interest groups that the compartmentalism of the financial system has produced has meant it has been difficult to introduce financial reforms. When attempts were made to introduce a unified clearing system, each interest group tried to build up a clearing system specific to its group, and the current system of narrowly subdivided sections resulted. The Japanese government has been unable to resolve

this issue. Japanese traditions of consensus building and unanimity have prevented a more comprehensive clearing system from being introduced. It is likely to take a long time to resolve this coordination failure.

**4. The question of retention of Public Financial Institutions:**

One of the mysteries of the Big Bang plan is that public financial institutions were not explicitly included. Public financial institutions, particularly the Postal Savings and Postal Life Insurance (*kan'i hoken*) Services, are a major part of the Japanese financial system. It will be difficult to achieve the ideals of the Big Bang when these huge market players are insulated from market discipline.

## CHAPTER 4

### ROLE OF WOMEN IN MANAGEMENT

#### Introduction

Japan is a complex, dynamic society that has undergone enormous change in the past one hundred and twenty five years, converting itself from a feudal state into a modern industrialized nation and an economic superpower. In doing so, the Japanese have absorbed Western technology, science, education and politics, while still keeping their unique Asian cultural identity. The country is an island culture of almost total ethnic homogeneity. Asian common cultural traits such as group centric approach, authoritarianism and protocol are salient ingredients of the Japanese society. Contrary to other Asian countries, the collectiveness of Japanese culture has been carried over to the companies and corporate culture. A job means identification with a larger entity through which one gains pride and feeling of being part of something significant, tying an individual's prestige directly to the prestige of his or her employer. Typically, the company is seen as a provider of security and welfare. Actually, loyalty to the company even surpasses the family bond.<sup>1</sup>

Before World War II, the status of women in Japanese society was very low. The Constitution at that time did not guarantee the equality of the sexes, and women had neither the right to vote nor the right to be elected. Under the Civil Code, wives were regarded as incompetent, and their property and inheritance rights, and their right to exercise parental authority was restricted. After the World War II, the new Constitution that was promulgated in 1946 guaranteed for the first time the equality of men and women under the law. Subsequently, the Civil Code was revised, and a range of domestic laws were enacted, including the Fundamental Law of Education and the Labor Standards Law, which resulted in sweeping improvements in the legal status of women in the family, the workplace and in society generally.

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1. Selmer, Jan, (2001), "Human Resource Management in Japan: Adjustment or Transformation?" *International Journal of Manpower*, Volume 22, No 3, pp 235- 243.



## **Women in Post World War Era**

As Japan moved into the 1960s and its period of double digit economic growth, new family norms developed. However, there were strong legacies from the past, including the social expectations that the happiness of a Japanese woman lay in her successful marriage and the role to be played by her was to be that of a “good wife and a wise mother”. Economic growth and industrial development produced salaried workers, a minority of whom had “permanent” (until retirement) job. Due to rapid economic development the jobs took men outside their local community and neighborhood, which resulted in separate social networks for husbands and wives, and overtime the necessity and opportunity for women to take on community responsibility emerged. All these changes resulted in the increase in the employment opportunities for married women outside the home. They could work in a growing range of occupations including newly developing neighborhood supermarkets, fast food restaurants and the like, participating in the Parent Teacher Association (PTA) and other child rearing organizations, join or found a community related group, and pursue personnel education through courses offered at community centers and women’s centers.

Since 1960s and the entire 1970s, the high growth of the Japanese economy brought rapid socio-economic changes such as rise of living standards and scientific and technological progress. These changes, together with longer life expectancy, lower birth rate, and higher educational standards, affected family life, and particularly the lives of women. Women began to participate in ever-greater numbers in a range of economic and social activities. However, the equality of men and women has not been fully achieved in practice, for the traditional value that women are to stay at home, is still deeply rooted.

The Equal Opportunity Act of 1986, combined with the bubble economy, provided increased opportunity for women who were ambitious and willing to work harder than men to become managers. In spite of the above law being passed, women lagged far behind men in Japan in terms of equal employment opportunities. The public's perception was that women could be managers only in "feminine" industries such as fashion, cosmetics, and retail businesses. Despite advanced industrialization, Japanese professional women had been excluded from responsible positions in most private

industries. Most workingwomen, however, took this differential treatment for granted and view their employment as a temporary stage before marriage or childbirth. This acceptance was primarily on account of two factors: --the high cultural value placed on motherhood and collective goal achievement and second, the housewife's unchallenged authority at home, which discourages women from pursuing an independent career. Since the companies have established a dual track system of employment (Core and Peripheral workers), the management gives preference to only the most brilliant educational background and career oriented women for the core group of workers, and thus indirectly and informally encourages discrimination by admitting majority of the women in the peripheral group or the non-career track system. Also, those companies which do not have a dual track system recognized formally, employ majority of the women in the category of "Office Ladies" whose only work is to greet customers, serve tea, and do some other menial works such as filing of the important documents, data entry and copying. The final result of the above practices is that in the long run only a few women managers emerge.

Education too had the impact on the opportunities. Among new workers in 1989, 37 percent of women had received education beyond upper-secondary school, compared with 43 percent of men, but most women had received their postsecondary education in junior colleges and technical schools rather than in universities and graduate schools. Few Japanese attend graduate school, and graduate training in business per se is rare. There are only a few business school programs in Japan. Companies provide their own training and show a strong preference for young men (rather than the women) who can be trained in the company way.

In 1990 approximately 50 percent of all women over fifteen years of age participated in the paid labor force. At that time, two major changes in the female work force were under way. The first was a move away from household-based employment. Peasant women and those from merchant and artisan families had always worked. With self-employment becoming less common, though, the more usual pattern was separation of home and workplace, creating new problems of childcare, care of the elderly, and housekeeping responsibilities. The second major change was the increased participation of married women in the labor force. In the 1950s, most women employees were young and single; 62 percent of the female labor force in 1960 had

never been married. In 1987 about 66 percent of the female labor force was married, and only 23 percent was made up women who had never married. Some women continued working after marriage, most often in professional and government jobs, but their numbers were small. Others started their own businesses or took over family businesses. More commonly, women left paid labor after marriage, and then returned after their youngest children were in school. These middle-age recruits generally took low-paying, part-time service or factory jobs.

### **Women in Employment**

One of the prominent features of Japanese management is the practice of permanent employment (*shushin koyo*). Permanent employment covers the minority of the work force that work for the major companies. Management trainees, traditionally nearly all of whom were men, are recruited directly from colleges when they graduate in the late winter and, if they survive a six-month probationary period with the company, are expected to stay with the companies for their entire working careers. On entering a Japanese corporation, the new employee were to be trained from six to twelve months in each of the firm's major offices or divisions. Thus, within a few years a young employee will know every facet of company operations, knowledge that allows companies to be more productive. This practice did not suit the dual role of "mother and careerist".

The norms of rewarding continuous employment (that is, promotion and wage based on length of service--*nenko joretsu*) and the stress on group loyalty (as expressed by the long overtime put in by workers and active participation in the company's social activities) virtually denied women an option to combine familial and career roles. The home-oriented majority hinders the formation of effective public opinion advocating fair employment practice, thus perpetuating the status quo of the sexual division of labor. But the fact that was often overshadowed was that they can also be found in a small percentage in the sectors of finance, manufacturing, construction, and transportation.

The Labor Standards Law was also revised to relax overtime restrictions for some women. Originally established in 1947, this law limited overtime for women to two

hours per day, six hours per week, and 150 hours per year. The law also prohibited holiday work and late-night work (from 10 p.m. to 5 a.m.). Under the revisions implemented in 1986, restrictions were abolished only for women in managerial positions and in 14 occupational categories requiring specialized knowledge or technical skills. In 1987 there were 24.3 million working women (40 percent of the labor force), and they accounted for 59 percent of the increase in employment from 1975 to 1987. The participation rate for women in the labor force (the ratio of those working to all women aged fifteen and older) rose from 45.7 percent in 1975 to 50.6 percent in 1991 and was expected to reach 50 percent by 2000.

In 1992, the Child Care Leave Law went into effect, which allows employees, both men and women, to take leave of absence until their children reach the age of one year. Workers with preschool children may also get reduced hours in place of a leave. This law only applied only to fulltime regular employees, and it did not guarantee payment of salary while on leave. In 1995, the law was revised to include family care provisions (e.g., parent care).

The question that comes into the mind of many while analyzing women managers in Japan is whether Japanese women would struggle their way "out of the glass ceiling"<sup>2</sup> or the invisible and artificial barriers created by attitudinal and organizational prejudices, which are often put up to prevent women from reaching top management positions. According to a Japan Federation of Economic Organizations survey in 1996, male personnel managers tend to blame women themselves and the social environment in Japan rather than corporate policy to explain the lack of female senior executives. Common reasons cited in the survey were "possibilities of giving birth," "lack of professionalism on the part of women" and "insufficient public child care facilities."<sup>3</sup> On the management side, 64% of the companies said that they are really focusing on "carefully outlining job responsibilities and giving appropriate supervision when mistakes are found." This was the number one response for the management group. Ironically, the women's group chose the same response, as the area that they thought needed the most improvement in their companies. That is

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<sup>2</sup> The term was coined in the US in the 1970s to depict the attitudinal prejudice against women.

<sup>3</sup> Iwao, Sumiko, "The New Lifestyles of Japanese Women", Ministry Of Foreign Affairs, [Online: Web], Accessed on 25<sup>th</sup> December 2005, URL [http://www.mofa.go.jp/j\\_info/japan/opinion/iwao.html](http://www.mofa.go.jp/j_info/japan/opinion/iwao.html)

women, 48% of them, felt that the companies were doing a lousy job of "outlining job responsibilities and giving appropriate supervision when mistakes are found."<sup>4</sup>

In the same survey, the second item on the managers list was "give women responsible jobs." 54% of the company managers chose that response, while 24% of women chose the same item. This points out the great diversification of interests and motivations of Japanese women. A growing number of women in the country have career aspirations of the highest order, but others are quite content with support roles. Although it is difficult to discuss Japanese women as one group, it is clear that the majority of workingwomen were happy with jobs that have little or no responsibility.<sup>5</sup> Thus it is evident that throughout the 1990s, the number of women in managerial posts in various fields was still small, although it increased annually. According to the Management and Coordination Agency, Population Census, 1995, women accounted for just 14.2% of the managerial workers in the non-governmental organizations.

According to the survey conducted by the Prime Minister's Office, Public Opinion Survey on Gender Equality, in the year 1995, it was observed that 77.1% of people surveyed felt that men received better treatment than women in society's views and customs and 59.3% felt the same way regarding the workplace. The survey also revealed that women feel inequality more strongly than the men. Further, the same survey also revealed that although the traditional concept of roles of men and women is still persisting in the minds of Japanese people, the ratio of those who agree with the traditional idea has been decreasing. In 1995, 22.3% of women agreed with the idea that "man is to work and woman is to stay at home," while 53.9% did not agree.<sup>6</sup> In 1997, the Japanese Diet passed revisions to several laws, including the Equal Employment Opportunity Law, the Labor Standards Law, and other related laws, in order to guarantee employment equality and to improve work opportunities for female workers. The revisions came into effect into effect from April 1999, and effectively abolished legal provisions protecting women employees, which meant that they would now be exposed to the same working conditions as men.

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<sup>4</sup> Ibid

<sup>5</sup> Ibid

<sup>6</sup> Japan Institute of Worker's Evolution, Commentary on the overall situation of women in general, "*Women In General*", [Online: Web] Accessed on 28<sup>th</sup> December 2005, URL <http://www.jiwe.or.jp/english/situation/general.html>

The revision in 1997 not only abolished restrictions on overtime, late-night work, and holiday work, but also made mandatory the Equal Employment Opportunity Law anti-discrimination provisions related to recruiting, hiring, assignments, and promotion, which previously employers only needed to make voluntary efforts in regard to compliance. Enforcement provisions in the revisions were weak, with the only penalty being that violators may have their names made public. Thus the foundations fabled of Japanese management--lifetime employment, the seniority system, and the bureaucratic, tightly knit nature of industrial policy--have served as barriers to women's entry into management in Japan. Institutionalized discrimination against women, while not necessarily written policy, is widespread and accepted. Practices such as restricting women to staff positions, not including them in informal meetings or off-site training sessions, and limited transfers and travel, all serve to restrict their advancement. Attitudes that assign women to decorative and service roles serve as unwritten, but powerful, institutional practices.

With regard to the blue collared jobs, economic recession has reversed the traditional gender pattern with the male unemployment rate being higher than their female counterparts since 1997. This gender reversal in unemployment rate reflects such fundamental changes as the shift of economic activities from manufacturing and construction to service and trade. It also reflects management's increasing reliance on part-time and temporary female workers, underscoring the lack of confidence in the economy's prospect that makes employers reluctant to invest in long-term employees. As manufacturing employment steadily fell, more and more male workers became unemployed but it does not necessarily mean the reversal i.e. more number of women being employed in the manufacturing sector of the economy. Thus, this sector has traditionally been and has still ignored women as the potential employees in the company. On the demand side, this phenomenon is due to the employers' reluctance to invest in human capital of male workers with long-term employment in the environment of grave uncertainty about the future of the economy.

Many companies admit the fact openly that though there are women who have the capacity to become managers in the long run but their service to the company in the form of number of years lags far behind the service rendered by men to the company and thus men are in a advantageous position when it comes to being appointed as a

manager. The management strictly believe that since the Equal Opportunity Employment Law exists, a woman, if wishes to be in the category of the white collared employees must work under the same conditions as men and thus should continue to work as full time employees without any maternity benefits which directly means a greater number of working hours. Yet, as explained above, there still exists a section of the management who believe that women lack the necessary experience, knowledge and judgment to be in the white collared category. To make the matters worse for women, a small minority of the society is biased in favor of men thus having stereotypes and expectations that support gender –stratified work structure.

Contrary to popular opinion and despite enormous obstacles, Japanese women have become successful managers in business, government, and education. Japanese women managers are among the best educated in the world, while at the same time they are the most flagrantly wasted national resource. They number only eight percent of its managers, having increased from six percent a decade ago. They have been exploited as temporary, and therefore less expensive, labor, and cast out at marriageable age for a new, younger crop of female college graduates.

The need to cut costs and increase efficiency due to the economic recession that started in the early 1990s is having a severe impact on employment in Japan. Companies are reducing hiring of new graduates, pushing "voluntary" early retirement programs for older workers, transferring people to lower paying positions, and even resorting to outright layoffs as part of their restructuring efforts. In addition, a growing number of companies are replacing seniority-based wages with performance-based systems. Thus, any effect any one of the three pillars will have a simultaneous effect on the other.

Lately, Japanese women have come to recognize the fundamental problem of the dual role of home-maker and the career and are now hesitating to get married and by improving their English language are able to find employment in the management of non-Japanese companies which unlike the former provide equal opportunities and benefits to both men and women. Thus, women have lately started migrating to other developed companies for career enhancement. The postponement of marriage by women for their career opportunities also explains the demographic changes that

Japan has been witnessing, which will lead to other societal and economic problems in the long run.

On the supply side, it may be partly due to an additional worker phenomenon in which wives of husbands who lost employment enter the labor market to supplement family income and also to maintain the national consumption level. Clearly, women typically have the larger share of part-time jobs than men. One factor to explain this phenomenon could be that since part-time workers suffer from low wages, men could generally be not interested in such work especially when they had a chance of working as a regular employee in a company. Moreover, women find it more convenient to work as part-time employees because it means that they have to work for shorter hours and fewer days while earning to supplement their family income. Also, women with technical knowledge can utilize their knowledge with the presence of part time jobs since it is still very difficult for them to obtain for themselves a regular job because the management still hesitates to give them a regular job keeping in view their maternity relief benefits (average length of women's full time employment in a company is less i.e. 8.2 years as compared to men i.e. 13.1 years in 1996); The large companies tend to hire men first. There is an increase of 4% in the part-time workers in Japan, the second highest among G-7 countries (after Germany). It has to be pointed out that structural reforms have been brought about in the economy of both the countries viz. Germany and Japan simultaneously. As per the government resource the rate of female part-time workers has increased from 31.9%(1985) to that of 51.6% in 2004.<sup>7</sup> This can be interpreted both ways negative as well as positive. Negative inference can be that the women are losing the opportunity to get regular employment in the companies due to the economic pressure of the companies to show the profit by minimizing the cost. The positive inference can be that more and more women are trying to seek employment opportunities besides their family commitments and therefore is a sign of productivity.

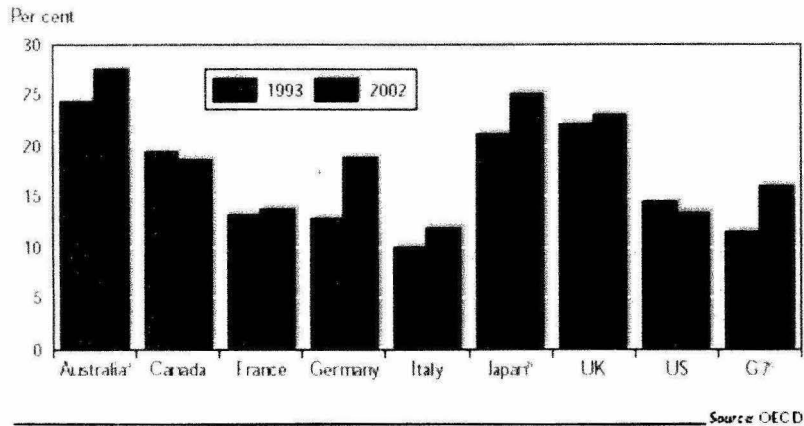
The comparative figure of the part-time workers in the G-7 countries is as brought out in the diagram below: -

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<sup>7</sup> [Online Web] URL [http://www.gender.go.jp/english\\_contents/](http://www.gender.go.jp/english_contents/) accessed on 18<sup>th</sup> February 2006.



**Figure 1** Proportions of part-time workers in selected countries; 1993 and 2002



a. Data for Australia are based on actual hours worked.  
 b. Data for Japan are based on actual hours worked; part time is defined as under 35 hours per week.  
 c. The group of seven countries: Canada, France, Germany, Italy, Japan, UK and USA.

The percentage increase in the women force as regular employees has little impact in Japan as can be seen from the comparative figure given below. This phenomenon as seen from the charts is not only faced by Japan only but from the other countries also with the exception of Germany, where the rise in their labor force is comparatively more than the other countries.

**Figure 2** Proportions of women in the labour force in selected countries;<sup>4</sup> 1993 and 2002

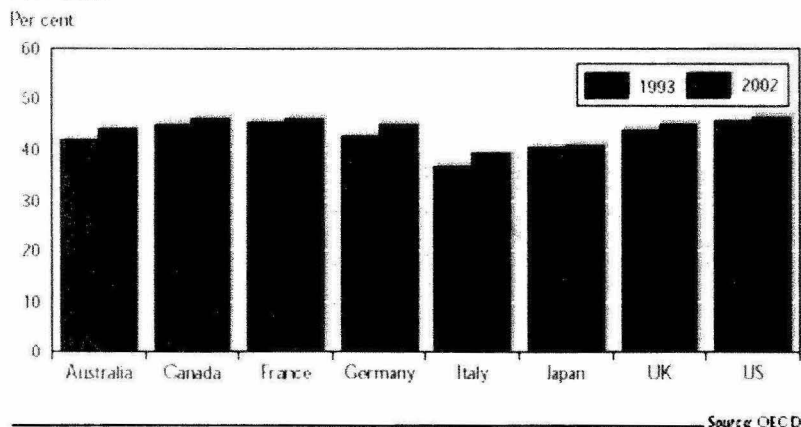
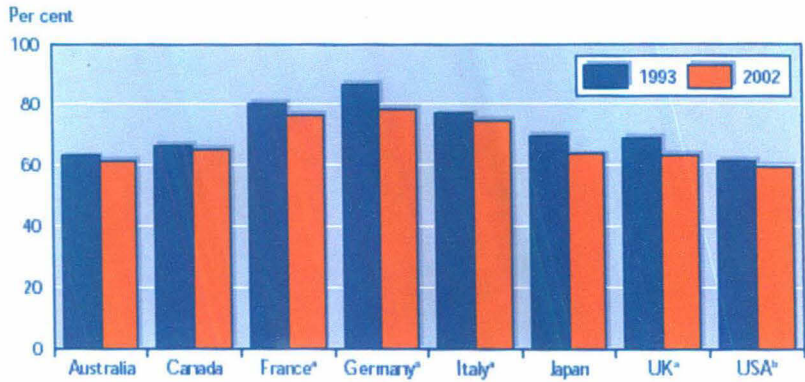


Figure 3 indicates proportion of involuntary part-time workers who are women in selected countries; 1993, 2002. The bar graph indicates that there is decrease in involuntary part-time workers in 2002 and so it implies that most of the women have come to serve voluntarily.

**Figure 3** Proportions of involuntary part-time workers who are women in selected countries; 1993 and 2002

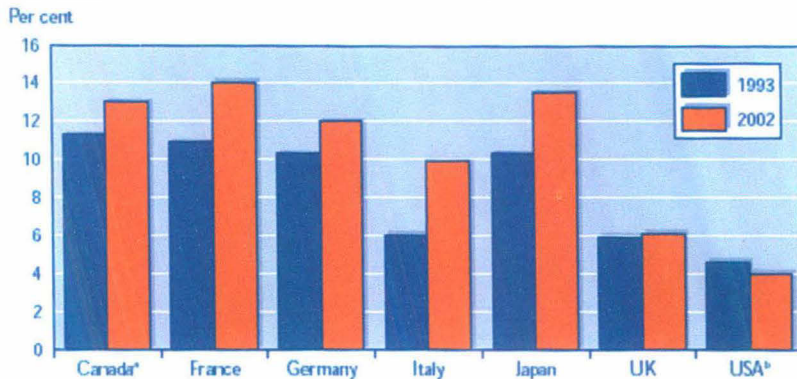


Source: OECD

<sup>a</sup> Data for UK, Germany, Italy, and France are for 1993 and 2001.  
<sup>b</sup> Data for USA are for 1998 and 2002, and exclude those who are self-employed.

Figure 4 however does not give very happy position because there is a tremendous increase in temporary status of women in 2002 i.e. approximately 3.5% as compared to 1993.

**Figure 4** Proportions of people in temporary employment in selected countries; 1993 and 2002



Source: OECD

<sup>a</sup> Data for Canada are for 1997 and 2002.  
<sup>b</sup> Data for the USA are for 1997 and 2001.

There were probably about 300,000 persons actually working as temporary employees (*toroku-gata haken rodosha*) in 2000; the number of persons registered with agencies exploded to a reported 1.39 million in 2001. Women accounted for close to 90 percent of registered temporaries through 1999, and they work primarily in service sector industries in large urban centers. For FY 2004 the data from Ministry of Education, Government of Japan indicates that there is 10-point gap with the OECD

average for university type higher education program and doctoral courses as in Japan only 26% are M.A. holders and 23% Ph.D. among women and in fact when taken into consideration the life science, natural science, agriculture, engineering manufacturing and architect this gap becomes 20-point with the average of OECD.<sup>8</sup> This factor becomes responsible for the lower percentage of women at the higher level.

Revised Temporary Workers' Law<sup>9</sup>, which took effect December 1, 1999 replaces the "positive list approach," which allowed temporary workers to work only in approved occupations, with the "negative list approach," which allows them to work in all but five specifically prohibited occupational areas: dockyards, construction, security, nursing and other medical fields, and manufacturing. Japanese employers seem to be able to pressure women into changing from regular to non-regular employee status, although the acceptability of such practices probably varies by industry. When the original Temporary Worker Law was passed, several companies, especially banks, induced many regular female employees to become temps in their employers' newly established in-house Temporary Service Agencies. Whether or not the companies "forced" the women to change status is murky, but some people believe that they probably gained the women's acquiescence by threatening to subject them to the long work hours and mandatory transfers faced by regular male employees. Such conditions are virtually impossible for mothers, and even regular women employees who perform the same work as men may therefore not receive comparable promotions.. Non-regular workers, including *paato*, contract workers, and temps (*haken rodo-sha*), have increased rapidly over the past decade and now account for an estimated 27.5 percent of Japanese employees.

The temporary services industry also reflects the prevalence of gender segregation and age discrimination in Japanese workplaces, since almost 90 percent of registered temps are women, and companies usually refuse to hire temporary workers over 35 years old. Thus Temporary workers often face a "triple punch" of discrimination on the basis of gender, age, and status. Despite the Equal Employment Opportunity Law, gender segregation is still common in Japanese workplaces, and this is reflected in the

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<sup>8</sup> Ibid

<sup>9</sup> Earliest Temporary Workers' Law came into effect in April 1986. The TWL served in part to help companies circumvent the Equal Employment Opportunity Law, which also took effect in April 1986, by making it easier to shift full-time women to non-regular status.

temporary work force, which is overwhelmingly female. Managers of Agencies on the other hand complain that the revised law's limit of a one-year maximum for temporary assignments has discouraged the use of temporaries.<sup>10</sup>

Temporaries rarely receive bonuses, and few temps receive all of the fringe benefits, social insurance benefits, or travel allowances that regular workers receive. These benefits have been designed primarily for regular workers, and little effort has been made so far to adjust them to meet the needs of non-regular workers. Most temporaries do not receive travel allowances, which are provided tax-free to virtually all-regular workers, and they are thus taxed on the income that goes for transportation expenses. In Japan, where the public transportation system is mostly unsubsidized, the cost to low-paid workers can be substantial.

Japan 's deregulation measures and the influx of temporary, part-time and female workers led the government to revise certain provisions of the Labor Standards Law in December 1997. The maximum length of labor contracts was extended from one to three years (limited, however, to "older employees" and those with "sophisticated knowledge") and the upper limit of flexible working hours was relaxed to allow workers up to 10 hours in one day and 52 hours in one week. These measures aim to fulfill the growing need for diversified contract periods and work patterns, particularly in an increasingly competitive economy. The government is also considering an increase in the upper limit of overtime to 360 hours a year (compared to the 150 hours proposed by labor unions). Japan's Central Labor Standards Council also seeks to strengthen worker protection and clarify working conditions under the Labor Standards Law, which currently focuses on wage-related matters.

Since the 1990s, the environment has changed substantially. (1) Japan's low birth rate and population-aging trends have become more pronounced. (2) Under the influence of these trends, expectations of steady future growth have been eroded and finally, (3) The expansion of other East Asian countries' capacity to supply a wide variety of goods (globalization) and rapid advances in information and communications

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<sup>10</sup> Weathers, Charles (2002); "*Women in Japan's Temporary Services Industry*", Japan Policy Research Institute Working Paper No 85.

technologies have raised the pace of change in both the industrial structure and the technologies that generate profits. (4) Japan's GDP shrank 5.3% during the first quarter of 1998 and unemployment reached a new high of 4.1% in April 1998. Banks got burdened with over \$500 billion in bad loans.<sup>11</sup> In June 1998, approximately 1.05 million Japanese received unemployment benefits, the first time this monthly figure has topped 1 million in 22 years.

The most affected section of Japanese society were women with the burden of taking care of the family and also from the point of view of giving psychological support to the male members of the family who had to lose the jobs due to the policy of deregulation in the several sectors such as energy, telecommunications, housing, finance, and medical devices and pharmaceuticals. These kinds of changes in the economic environment have severely undermined the rationale both for seniority-based wage profiles, which were backed by accumulated firm-specific labor skills, and for long-term employment, which had difficulties in responding to changes in the economic environment. As a result, it is natural that in recent years companies have looked to reduce excess seniority-based wages paid to middle-aged and older workers, and have tried to construct a more flexible employment system. Further change is also required because of the pressure on the companies to meet the global standards and thus emphasize more on profitability than ever before. When the balance sheets of the firm starts showing reduced profits and even increased debts and other liabilities rather than assets, firms in order to adjust their balance sheets restructured their wages given to the employees by making the part-time employment policy. This favors the generation of part-time employment opportunities for women in certain sectors, but not certainly in encouragement for the higher management post as the women may not be in position to put the extra working hours for excelling in the field as per the expectations of the corporate world.

A changing element in international business, particularly in industrialized countries, is the increasing presence of women. In most industrialized countries, women's role has changed during the past 25 years. Increasingly women are more educated and are

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<sup>11</sup> Facts, [Online: Web] Accessed on 28th December 2005, URL <http://www.pacificbridge.com/Publications/JapanFall98.htm>

actively participating in the workforce. In many countries, women have made great strides in assuming positions in firms that in the past had not been attainable for them. As businesses interact across cultures, the likelihood of interacting with a female business partner for men continues to increase and this factor also affected Japan. According to the ILO statistics report of the year 2001, by 1999, women had grown to 41% of the total labor force in Japan. The question that now arises is that how come in spite of the legal reforms in their favor and in their increased percentage of their awareness and degree holders, women still continue to occupy a considerably low number in the high rank files of various large private enterprises? The answer to the question lies in the existence of the Dual Track system of employment (Core and Peripheral workers) practiced by the Japanese Management according to some scholars. Other scholars attribute it to the negative effect of the globalization on the Japanese society particularly women who culturally differ from the field of competition. With legal provisions into force, which favor workingwomen, women have come ahead to solve their household problems during last five years.

### **Conclusion**

Accompanied with the economic recession was the IT revolution, which has increased the job opportunities for women in the specialized fields such as software development, accounting, computer-aided designing and data processing. In their personal lives highly educated and technically sound women prefer to marry men who possess high education and with the latter's income being high, women are satisfied with their part-time jobs to supplement their family income. With these assumptions, a direct correlation is established between the reduction in the employment of regular workers and increase in temporary workers. Much of this problem should disappear once the economy starts growing and management and hence the employers become convinced that the recovery is sustainable and that they should invest in long-term employment.

The basic law for a gender equal society came into force in June 1999, which requires the central and local governments to take the necessary "positive actions" which imply better opportunities to eliminate the gender gap. In December 2000, the cabinet introduced 'Gender Equality Basic Plan' calling for enhancing women's participation

in policy decision making process at central government level and encouraging private enterprises, education research institutions and other organizations to voluntarily take gender equality action. The target is to increase the percentage of female members of society in higher position to 10% in the next ten years. Though the percentage of women in government advisory council members has become 28.2% in September 2004 yet the female public employees account for only 1.5% in the 9<sup>th</sup> grade or higher (directors in ministry HQ. or chiefs of government organization in local area. As regards management officials the percentage stands at 4.9% at prefecture level and 6.4% at cabinet-order designated city level as of FY 2004.<sup>12</sup>

To motivate female employees, the multinational companies like HP and even the Japanese corporate groups like Nissan Motor Co, Sanyo Electric Co., are active in organizing a support group that encourages women to discuss topics like communication skills, English language, time management and balancing work and family life. Some of the well-known top executives such as Carlos Ghosn, chief executive of *Nissan Motor Co*, *Motoko Honma*, H-P marketing specialist, Hitomi Mori of *Sharp Corporation* and Tomoyo Nonaka of *Sanyo Electric Co.* have created the example of success stories in Japan. Under a mentoring program HP that began in 2004, the company aims to raise its levels by one percent each year by promoting more Japanese women to management posts.

These days, firms from banks to auto makers are rushing to launch new programs to train and retain female managers. Sharp, which wants to triple the ranks of women managers by the fiscal year ending March 2008, created a special division last year for that purpose. Sharp Corp., where currently 21 of 3,412 managers are female. Nissan Motor Company plans to fill 5 percent of its management posts with women over the next few years from a current 1.6 percent. Even as more women graduate from university and make up 41 percent of the work force, including part-timers, there may be some improvement in the legacy system. The result of pro-active approach is very encouraging in the sense that while in 1985, only 1 percent of division chiefs at

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<sup>12</sup> Outline of the “FY 2004 Annual Report on the State of Formation of a Gender-Equal Society” and “Policies to be implemented in FY 2005 to promote the Formation of a Gender Equal Society”. The Cabinet Office, 2005, [Online Web] URL [http://www.gender.go.jp/english\\_contents/](http://www.gender.go.jp/english_contents/) accessed on 17<sup>th</sup> February 2006.

Japanese companies of 100 employees or more were women but by 2004, that figure may reach up to 2.7 percent.<sup>13</sup>

Last, it can be said that the implementation of the Equal Employment Opportunity Law has improved the position of women only marginally and women still continue to face discrimination. The strengthening of the dual-track employment system, the long working hours required for career-track employees, and the increase in female non-regular employees have served to restrict true equal employment opportunities for women. The law in-fact has been given into effect from the reverse side and thus Japanese women continue to suffer in spite of the existence of various legal provisions. The Government of Japan has to work further along with the business entities in not only encouraging but also in putting up their case in regular reviews with the help of advisory councils set up for the purpose of women empowerment.

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<sup>13</sup> *Japan's diversity problem: Women command few top posts* by Ginny Parker Woods, The Wall Street Journal, October 24, 2005



## CHAPTER 5

### CONCLUSION

In the beginning of the 1990s Japan witnessed economic recession that is often called as the burst of the 'bubble' economy. It was marked by the *Nikkei* average index declining to one third at the end of October 1998, of what was earlier in late 1989 (On 29 December 1989, *Nikkei* average reached its peak at 38,915.87 points). Also, Prices of land for commercial use and residential use dropped by 70 percent and 45 percent respectively, the result being that many companies landed themselves into bad debts and finally became insolvent and hence bankrupt. Since the economy was a on a virtual collapse, many companies had to cut spending in an attempt to repair their balance sheets.

With the situation at hand not being enough to handle, 1997 saw the Asian Financial Crisis taking the whole of the East Asian region in its grip. The government back home tried to boost its economy by pumping various monetary packages and the Bank of Japan intentionally allowing its interest rates to fall to a historically low level. Japan's economic growth rate declined in steps since the early 1970s, from 10.4 percent in the 1960s to 5.2 percent in the 1970s, to 3.8 percent in the 1980s, and to 1.7% in the 1990s. As a matter of fact, the GDP growth rate between 1992 and 1999 stood to as low as 1.0 percent a year. However, apart from all the factors at work, the decline in the growth rate in recent years could also be attributed to a sharp decline in investment efficiency, as reflected in a sharp increase in the incremental capital-output ratio (ICOR). The rate was further dragged down because both the government and the corporate sector failed to adapt the institutions that had contributed to the economy's past success to a new environment characterized by globalization, aging population, and the transition to a post-industrial society.

Thus, middle of the 1990s proved to be a wake up call when the hopes of timely return of the bright and sunny days that existed earlier died its own death. Led by a comprehensive reform program initiated by the Hashimoto Administration in late 1996,

serious attempts have been made to revitalize the economy by enhancing competition. The six areas of interest focused by him were economic structure, finance and banking, public finance, health and education. Reform of the economic structure, till today continues to occupy the driving seat of the entire reforms because it has a direct impact on the productivity growth. Under this scheme, resources are shifted to the growth areas that encourage employment in the long run.

The corporate sector has responded by changing business practices in both the aspects viz. the HRM practices (to cut back their payrolls, streamline their supply structure in accordance with the market needs, and to focus on the never important area of profitability) as well as the corporate governance practices, with more emphasis on the market mechanism as the guiding principle. In the HRM practices, lifetime employment is giving way to a more flexible one, preference is being given to the individual performances rather than the group performances, seniority based wages and promotions taking a back seat, and finally, the role of the company unions declining to a considerable extent. Thus, the 'three sacred pillars' of the Japanese management are said to be 'crumbling down' and no longer they enjoy the glory of the past. Closely associated with the change in the above two aspects and coupled with a change in the demographic situation is associated the change in the pension structure of the country.

Mergers and acquisitions (M&As) across corporate groups and national borders have become a common tool of restructuring with the Japanese government reducing restrictions that hinders such developments. Japan has brought about a change in their anti monopoly law to facilitate the mergers and acquisitions. The ban on holding pure holding companies (companies with more than half of their assets being the shares of other companies) was lifted in 1997 for the non-financial firms and in 1998 for the financial institutions. Recent examples of M& A being the merger between *Mitsubishi Bank* and *Tokyo Bank* in 1996, *Dai-ichi Kangyo Bank* (DKB), *Fuji Bank*, and *Industrial Bank of Japan* (IBJ) to form the Mizuho Financial Group in the autumn of 2000, *Sanwa Bank* and *Tokai Bank* in the spring of 2001, and *Sakura Bank* and *Sumitomo Bank* in

2002. Thus, Japan's major banks have been effectively consolidated into four major groups.

Merger and Acquisitions have not only been in the domestic industries and firms only. Lately, Japan has become a part of the global wave of M&As in the automobile industry. Glaring examples of which are Renault of France invested \$5.3 billion in *Nissan* in 1998, giving it a 36.8 percent ownership share of Japan's second-largest automaker. This was followed by GM's investment in *Fuji Heavy Industry* in 1999 and Daimler Chrysler's acquisition of 33.4 percent stake in *Mitsubishi* in 2000. As a result, seven out of Japan's eleven major automakers have come under the control of foreign companies. Of the remaining four, *Toyota* now has majority holding of *Daihatsu* and *Hino*, and only *Honda* has decided to go it alone.

Thus, as an overview of the changes in the entire industrial policies, a marked shift can be seen as -- from market-conforming "accelerationism" to market-defying "preservatism". Focus has finally shifted to help out the sinking companies that in turn would decrease if not stop the increasing unemployment rate, and also to see that the workers are maintained with at least the respectable conditions of living. Japanese companies are paying more attention to the rate of return on their investment, with return on equity (ROE) and return on assets (ROA) followed closely by both managers and investors. Further, recession cartels formed under the initiative of the Ministry of International Trade and Industry (MITI) to protect declining industries have reinforced inefficiency. In the name of egalitarianism, members of a recession cartel are obliged to cut production in proportion to their share of the market or their share of capacity. The companies as a major initiative to cut down their wage structure have reallocated their production units to the offshore locations in the East Asian regions, and thus have helped to generate employment in the nations that have been hit by the East Asian financial crisis, at the cost of jobs of their domestic workers.

Japan is still the world's second largest economy after the US, despite being disadvantaged with the natural resources and also the aging population. What contributed

to the so-called economic miracle? The reply to this interesting question perhaps lies in series of answers to the several questions. Was the economic miracle due to the borrowed technology from the West or the funding from US or the inherent potential of Japan? Did Japan remain tied to the Western technology for a long time or did it innovate on her own? Did Japan remained indebted to the West or for that matter to the US perpetually or start to contribute in terms of intellectual wealth? Did Japan adapt to the Western management practices or evolved her own management practices? Cost aware and creative employees, just-in-time production, autonomous quality assurance and an in-built flexibility in the process layout and employee skills, are dominant features of the Japanese management approach which creates a cost aware and quality conscious culture across the organization. It has a flexible outlook, encourages improvement and invests in training multi-skilled employees. Japanese management practitioners are arguably better equipped and well suited to face the open-ended challenges of rapidly changing technology and increasing global competition. These practices have not only contributed to the Japanese economy but also enriched the economies of the other countries of the world wherever the Japanese technology was adopted. Professor Ostubo laid down ten points of distinction between Japanese Management Practices from the Western Management practices. These are: -

1. Market First: Not capturing the market but sustaining it.
2. Long terms commitment to the customer
3. Training and Education
4. Get-in-touch, learning from facts
5. Effort Evaluation - focus on process rather than results
6. Customer first and shareholder last i.e emphasis more on quality rather than profit.
7. Team work i.e. function maximization.
8. Flexibility
9. Quality first and cost last
10. Learn from the best.

Japanese believe that “Manpower is something that is beyond measurement. Capabilities can be extended indefinitely when everybody begins to think”<sup>132</sup>. While the higher relative wages paid by large Japanese firms offer a disincentive to shirking, the firm's internal wage system offers a positive incentive to heightened levels of employee effort and proficiency. In order to cash in on increased seniority, employees work under a virtual "lifetime" incentive to perform satisfactorily and to acquire the additional training required for upgrading continually their skills and capabilities. The steeper age-earnings profiles found in Japanese firms function more effectively as employee incentives than the flatter pay structures prevailing in Western concept, especially under collective bargaining. In large firms on the Western model, a larger proportion of rewards are distributed in the form of general pay increases, and short job ladders and narrow job classifications often characterize pay structures. Japanese management on the other hand had the following advantages:

- Employment security within the firm has been converted into a source of employee efficiency and adaptability and into a source of national economic stability.
- A strongly egalitarian distribution of earned income has been combined with comparatively high rates of economic growth.
- Low unemployment has been combined with low inflation and high growth.
- Productivity of the entire section of the society in which even the women could take part-time jobs at their convenience.
- Avoid the squandering of training resources that occurs in the U.S. "post and bid" system when senior employees bid for new jobs with skill requirements that do not build on their own accumulated expertise. In the job change, valuable human capital is lost.
- Training to be delivered to the individual in small increments and mainly on the job -- just in time for the employee to assume each new responsibility calling for additional skill. A versatile and deeply trained work force can produce the same

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<sup>132</sup> Taiichi Ohno, pioneer of the Toyota Production System

output with fewer people than a work force of highly specialized workers, resulting in a lower fixed-cost liability to management.

- Group activity and cooperative effort, such as work teams and QC circles that emphasizes continuous improvement and lowering costs. Highly trained production workers are capable of discovering ways to improve the production process.
- *Shunto*, the annual wage determinant process, represents a significant economy-wide mechanism that restrains inflationary wage pressures. Each year a pattern emerges from lead negotiations in a small group of major firms, which is then diffused through the remainder of the economy.
- Placing the interests of their employees first amongst their stakeholders concept followed by customers and lastly the shareholders. This is virtually the opposite situation to that found in free market western countries.
- Efficient utilization of human resources through framework of *Shojinka* (flexible workforce) and preventing idle time and boredom by employing the twin strategies of (i) multiprocess holding; and (ii) multiskilled worker.
- Harnessing the creative abilities of employees through *Soikufu* (creative thinking) is a framework for and a recognition of the fact that no one appreciates a task better than the person who performs it day in day out. Through implementations such as Quality Circles and Suggestion Schemes, employees are encouraged to continuously think about improvement. *Soikufu*, thus, is an integral part of the overall *Kaizen* (continuous improvement) framework. The most important difference between Japanese and Western management concepts is Japanese *Kaizen* and process-oriented thinking against the West's innovation and result-oriented thinking.

The recession of 1990s has got both negative as well as positive effect on Japanese Management Practices. There is more focus on hiring of temporary and dispatched workers who take no pains to give their performance either to the organization or to the society. The supply agencies, from which the temporary work force is being hired, are also not taking pains to improve skills and career enhancement, which would have been

possible if they would have belonged to an organization. Since all this labor is disorganized, there is no communication between the employer and employee. This resulting both in psychological set back as well as loss to the society in the matter of productivity and creativity. The Japanese society is gradually getting converted into “*Job hoppers*” and *Freeters*” like youth in European and Western world and it may prove a burden on the government resource in the matter of health and social security. The situation will get aggravated further when the aging process of population becomes faster. According to Japan’s Ministry of Health, Labor and Welfare, if necessary reforms cannot be achieved, the premium rate for employees’ public pension plan is expected to rise as high as 25 percent on annual income basis in 2025 compared to 14 percent today. The Potential National Burden Ratio (Proportion of Taxes, Social Security Contributions, Fiscal Deficit as a percentage of NI), which now stands at 46.9 percent, is expected to soar as high as an unsustainable 80 percent in 2050, security and fiscal problems.<sup>2</sup> According to Japan’s Ministry of law and that Japan should swiftly take some action toward this to expand the potential labor force by attracting women and healthy aged persons into the work force.

The government has also changed its strategy of not letting the financial institutions (banks in particular) go bankrupt, with the government (Ministry of Finance) arranging for its merger with another bank which was in a sound financial health in order to protect the interest of depositors and borrowers. This ‘safety net’ proved to be a bone of contention in the long run as it resulted in the problem of bad debts and a sharp decline in the prices of the real estates, finally the government had to do away with it. Further, steps have been taken to ensure full transparency in the balance sheets of the companies and in order to improve the circulation of money, public works have also been used as tools to create jobs and transfer income (to the construction sector and to the countryside) rather than as investment to yield a return; it has been said that Japan has roads that lead to nowhere. New areas of investment such as the IT development however, continues to be

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<sup>2</sup> [Online Web], , URL <http://www.keidanren-usa.org/publications/currents/docs/economic-currents25.pdf> accessed on 5<sup>th</sup> February 2006

neglected and an overall backward-looking public spending strategy has led to a misallocation of social resources and retarded economic growth.<sup>133</sup>

One of the major developments in the HRM practices has been the “outsourcing” of human resource management responsibility to outside temporary agencies and contractors. Many employers cite “low administrative burdens” as one of the major reasons for using dispatch/temporary contract workers. The use of “non-employed” individuals is likely to reduce administrative costs, but other benefits include reduced responsibility regarding such issues as employment continuity and employee assessment and training. In short, firms can remove themselves from human resource management responsibilities. Many firms obviously consider that this is an attractive benefit. There has been very little research done on the impact that the use of contingent workers has on the attitudes of the core or regular employees. The effect on the attitudes of regular-status employees is an important consideration since it is they who are still likely to staff key strategic positions in organizations and it is, therefore, their morale and their trust in employers that will at least partially determine the effectiveness of organizational performance.

A departure from the traditional practices such lifetime employment and increasing meritocracy at the workplace, sends a signal to the existing regular-status employees that their jobs can be at any point of time be converted into contingent positions. Employees may also conclude that their efforts to learn and to upgrade their skills will not be rewarded in the long run, and hence, they may show less willingness to learn firm-specific skills that are valuable only to their current employers. It can therefore be hypothesized that the increased use of contingent employees would cause regular-status employees to decrease their attachment to their workplace, and would have negative consequences on workplace morale. Moreover, this negative impact will be more pronounced when employers simultaneously decrease the number of regular-status workers in workplaces. To avoid such negative effects, employers may need to manage two kinds of human resources with separate sets of human resource management

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practices, and to differentiate the work allocated to them. As a matter of fact, many of the non-regular workforces that is hired is utilized for the skills that are not available within the firm and that are being constantly needed in an ever changing competing business environment. Thus, employers do not have the incentives to maintain them as part of the internal organizational structure. However, it is important to note that the hiring of non-regular workforce is not only been increasingly adopted in Japan but also in many of the industrialized countries of the west due to the inflexibility and the high costs associated with the internalized mode of employment.<sup>3</sup>

The changes in the corporate governance sector of the Japanese Management practices has brought to the forefront the issues and often conflicts between the management and the shareholders, something which was nowhere to be observed in the pre-recession era. Furthermore, the changes have brought out the question of the identity of the investors to the center stage since full transparency has been encouraged. Also, the questions such as to who monitors the investments, what are their incentives and how are they constrained by the legal framework have gained importance in the past decade. When firms are closely monitored by various agencies and by the shareholders, emphasis shifts altogether from the different governing institutions such as the board of directors, takeovers, general shareholder's meetings to the various devices for redesigning ownership and control, in particular, the use of pyramiding of share holdings and cross ownerships. Further, bilateral negotiations and arrangements to keep the company safe and sound have replaced the agenda of analyzing the capital market activities. With recession and the changing corporate governance, even the small time investors are being given importance. This becomes important with the rise in the number of firms going bankrupt and in the hostile takeovers by the other firms in order to enhance their credentials in the stock market. Moreover, other external factors that have a defacto influence over the firm is to be closely scrutinized.

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<sup>3</sup> Please refer to Blake, Davis, Alison and Uzzi, Brian (1993), "Determinants of Employment Externalization: A Study of Temporary Workers and Independent Contractors.", *Administrative Science Quarterly*, Volume 38, pp 195-223, and Morishima, Motohiro (1995), "*Japanese Human Resource Management: A Learning Bureaucracy*", In Larry Moore and Dev Jennings (eds.), *Human Resource Management in the Pacific Rim: Institutions, Practices and Values*. pp 119-150, Walter de Gruyter, Berlin and New York

Emerging corporate governance paradigm replaces the traditional corporate governance problem of small, dispersed investors attempting to control entrenched managers by a model of multilateral negotiations and influence seeking. This model in practice typically integrates a number of checks and balances. Investor protection has become important since the past days of certainty are over especially in the transition days where strategic investors are needed to restructure the companies.

The available literature on the changed corporate governance is lacking in the interaction between corporate governance arrangements and the political system, and also with the products produced by the firm. The literature tends to over emphasize the importance of external finance and corporate governance and the interrelationship between the two. Aspects such as supply of profitable investment opportunities and ability to mobilize savings, which have a considerable impact on the economic development, are completely ignored in the literature of the corporate governance. The implicit claim, which no doubt is true, is the fact that a financial arrangement in conjunction with the legal framework affects corporate behavior and performance, but the other external factors are completely ignored. Further, the factor of qualitative judgments is completely lacking in the readings. Corporate law only provides a basic outline and thus is only one of the many inputs available to go forward successfully with the management of a firm especially in the conditions of recession at back home. Moreover, the dimension of the methods of investor promotion needs to be given enhanced importance if an all-round protection and further development of a firm is required. Decision-making within the corporate governance structure is another contributory factor that has to be given its due share. Differentiation is also to be done in the types of creditors such as the junior and senior creditors who have at times divulging interests, the law has to be in favor of the both since a law favoring one group may harm the strategic interests of the other. This becomes all the more important when in other countries cases have emerged in which the large shareholders exploit the minority shareholders through diplomatic means. Moreover, the role that has to be played by each group of shareholders has to have importance in the say of the board of directors and hence the policy making decisions. More light still has to be thrown in this area.

It is the corporate law that drives corporate finance and it is not the other way around. The way available literature has given importance to the ways and means to attract corporate finance and thus the laws rotating around it makes us think as to what type of a correlation is being tried to establish between legal origin and financing arrangements. No doubt, the many of the corporate laws shape up the financial institutions but correlation has to be established from both the sides since it is an equal give and take relationship. More information has to be provided in the Japanese corporate law literature about the use of various control mechanisms such as dual class shares, pyramiding and cross-ownership in the case of foreign companies taking over their Japanese counterparts and vice versa, and also in the case of merger and acquisition activities. Investor protection measure along with various enforcement measures should be given importance in the literature so as to avoid future conflicts in the form of legal suits between the management and the investors. Furthermore, ample evidence has to be provided in the literature to show a direct correlation between the corporate laws, financial arrangements and the economic growth. Just a mere change in the corporate laws is not enough to make the economy from recession to the back old sunny days.

The role of women in their household management during the recession cannot be ignored. In 1985, Japan witnessed Diet passage of the Equal Employment Opportunity Law (EEO) following a serious and bitter debate. The law went into effect the following year. The media called the 1990s an era of women, indicating that the women had now increased opportunities to participate in the jobs, and hence their conditions would no doubt increase. The job picture, following collapse of the speculative bubble has swiftly shifted away from that of a severe labor shortage toward that of excess labor in which men are preferred. However, industrial realignment, i.e. a greater share of the services in the economy and sophisticated information technologies and on the other hand, changes in life style-diversifying values and attitudes toward work has given ample opportunities to women to step outside the four walls of their house and contribute to the family income since the wages have now been decreased. This is evident from the fact that in 1987, there were 23.6 million women working, according to the Labor Force Survey conducted by the Management and Coordination Agency, and in 1992, the number of

working women increased to 26.19 million. But the stark reality remains that the largest number of women are engaged in clerical work, accounting for one-third of all female employees. Crafts persons, manufacturing and construction workers, professional and technical workers, sales workers, protective service workers and service workers, follow these. Thus, in particular since 1982 there has been an increase in the number of women doing the menial clerical jobs, but the ratio of women workers tending to rise in all other occupations, the ratio of women in professional and technical jobs, it should be noted, has declined.

Female professional workers have increased in number but have decreased in ratio, suggesting that professional opportunities have proportionally declined. Female managers and officials are extremely small in number and percentage alike. Thus, women have yet to make headway into white-collar jobs. The low ratio of women in managerial positions in Japan is linked to human resource management in Japanese companies. The foremost cause is the difference in assignment and training between women workers, for whom long employment tenure cannot be expected, and men workers. It has been argued that the implementation of the Equal Employment Opportunity Law has given a legal base for the discrimination in recruitment, assignment and training because it requires that both men and women have to work under the same circumstances and thus are expected to do the same work as men do. This becomes almost impossible keeping in mind the natural differences between men and women and thus different situations have to be evolved for them. It is well known that women managers cannot work till late hours not only because of her family commitments but also because of her safety aspect. Further, a woman manager if going into the family way can't be expected to take up the same strains as that of her male counterpart. Thus, the EEOL has made the same work to be done by both men and women as a major point of contention.

There is a need of adaptation of shorter working hours keeping in view the changing demographic situation, creating potential for employment opportunity for women by proactive approach, favorable working condition even for the older work force and engaging the younger generation in fruitful employment. It is not that the Japanese

government is insensitive to all these needs and the challenges encountered at this movement in the context of globalization and slow economic growth. Abandoning the traditional management practices in favor of Western Management Practice will not suit the Japanese society with its economy in the long run.

However, the positive developments can't be ignored. The 1992 Survey on Female Employment Management, carried out by the Women's Bureau, the Ministry of Labor, showed that many companies assign both male and female workers to individual jobs in most areas, but with some exceptions. Over 80 percent of firms replied that they assign both men and women workers to personnel and planning jobs. It is a fact that in corporate organizations, there are still many job areas that are not open to women. Yet women are gradually being assigned to those jobs that are male-dominated. Thus, the job areas to which women are assigned are expanding within the corporate organizational structure. An increase in the number of female managers depends entirely on how women's ability is demonstrated amidst a widening of job fields. Therefore, it is clear from the above arguments that women's advance into the career world has made great strides quantitatively as well as qualitatively in the fact that more diverse job fields are open to them. It was thus confirmed that occupational fields for women are indeed expanding steadily and the "Glass Ceiling" is thus beginning to crack. Finally, from now on, occupational fields in which women have special additions will expand and the extent to which women develop their abilities will depend upon training, skill enhancement and other advancement systems outside of the firm as well as how effectively women are able to take advantage of such systems.

Labor unions could also not remain much behind to contribute their bit to improve the conditions created by the economic recession. Not only they have accepted the changes brought about in the HRM practices, but also they have shifted the focus of their annual spring offensive bargaining or the practice of "*shunto*" from annual increase in the bonuses and wages to the continuance of the jobs of the workers. Also, many labor unions have accepted that instead of holding "*shunto*" annually, it would be held either in

alternate years or after a gap of two to three years. Further, the rate of unionization has been declined to a considerable amount.

A new pension contribution system modeled after the 401(k) plan in the United States has been introduced in 2001, which allows employees to contribute a portion of their compensation, before income taxes, to a company-sponsored retirement plan. Under the scheme, the employees decide how the contributions are to be invested, and continuity is guaranteed when the employees change jobs. This is in accordance with the changes in the employment structure of the country.

For the developing countries and particularly for India, there are few lessons to be learnt by the Japanese experience of the 'bubble economy', the economic recession and how to cope up with the reforms thereafter. First, the economic growth should not depend upon only support from outside either by way of exports or by way of capital support. The real economic growth depends upon the generation of the employment in all the sectors of the economy, the consumption pattern within the country and Human Development Index (H.D.I) covering education, health, and women empowerment. Second, the impact of globalization should not be sudden, but, a gradual process keeping in view the aspect of social security, demographic factor and its effect on the domestic economy. Third, the policy of merging of the 'sick' banks with the 'healthy' ones as a policy of protectionism, as adopted in Japanese corporate governance does not serve the purpose for a very long time. Fourth, transparency and accountability remains the keystone for financial discipline and any amount of government interference at appropriate stage is an integral part of the management practice. Fifth, the role of women in the higher management and decision-making is very significant to ensure better productivity. Sixth, the burden of pension on the government resources can take a heavy toll on the economy and so the pension fund should be utilized effectively while ensuring the social security. Seventh, the interests of the stakeholders are as important as the interests of the employees and both are interdependent. Eighth, reforms should be taken on a continuous basis, i.e. as and when changes occur in the economy, rather than waiting for the entire financial system to crumble down and then hurrying up with the reforms. Ninth, the best

management practices are those that take into consideration the culture, economy and the market constraints into its ambit. Neither universality of western management practices nor the universality of Japanese management practices may serve the dual purpose of both the profit and corporate welfare. Solution lies in incorporation of both.

Very recently, an urgent need is being felt to reform the postal savings system, which also happens to be the largest deposit-taking institution in the world. This state-run system enjoys a competitive advantage over private banks because it does not have to pay any corporate taxes or deposit insurance premiums and it is not subject to reserve requirements. Postal savings are used to finance policy loans (channeled automatically through the Ministry of Finance and then government-related financial institutions) based more on political than on economic considerations. But, here also the irony is the fact that some of these borrowers are public corporations that are running very large deficits, thus, raising doubt over their ability to repay without additional financial support from the government.

Moreover, *Nippon Keidanren* (The Japan Business Federation) had released their charter on the corporate behavior in 2004. According to this charter, member corporations are expected to conduct themselves in a socially responsible manner, observe both the spirit as well as the letter of all laws and regulations applying to their activities both domestically and overseas in accordance with the following principles. *Nippon Keidanren* have a firm belief that corporations exist not only as economic entities designed to pursue profits through fair competition, but also as social entities which must make a contribution to society at large.<sup>4</sup>

- Member corporations by the development and provision of socially beneficial goods and services in a safe and responsible manner shall strive to earn the confidence of their consumers and clients.

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<sup>4</sup> Charter of the Corporate Behavior, Nippon Keidanren, [Online Web], URL <http://www.keidanren.or.jp/english/policy/cgcb3.html> accessed on 5<sup>th</sup> February 2006

- Members shall promote fair, transparent, and free competition between corporations. Further, they will ensure that their relationships and dealings with government agencies and political bodies are of a normal and proper nature.
- Members shall engage in the active and fair disclosure of corporate information, not only to shareholders but also to members of society at large.
- Members will recognize that positive involvement in environmental issues is an essential part of their activities and their very existence as a corporation, and should therefore approach these issues positively.
- As "good corporate citizens," members will actively engage in philanthropic and other activities of social benefit.
- Members will strive to respect the individuality and differences of their employees, to promote safe and comfortable workplaces, and to ensure the physical and mental well being of their employees.
- Members will reject all contacts with organizations involved in activities in violation of the law or accepted standards of responsible social behavior.
- Members will respect the culture and customs of other nations and strive to manage their overseas activities in such a way as to promote and contribute to the development of local communities.
- The highest levels of management within member corporations will assume the responsibility for implementing this charter and for taking all necessary action in order to promote awareness of it among all those concerned. Management will also heed the voice of their organization's stakeholders, both internally and externally, and promote the development and implementation of systems that will contribute to the achievement of ethical corporate behavior. And Finally,
- In the event of a violation of the principles of this charter, management of member corporations will investigate the cause of the violation, develop reforms to prevent its recurrence and make information publicly available regarding their intended actions for reform. After the prompt public disclosure of appropriate information regarding the violation, responsibility for the violation and its effects will be clarified and disciplinary action will be taken which includes the highest levels of management where necessary.



Further, *Nippon Keidanren* has envisioned a vibrant, attractive Japan in the 21<sup>st</sup> Century, in the form of “JAPAN 2025” which seeks to turn the situation of the economic recession or Japan’s “lost decade” around. It aims for economic strength and confidence both at the domestic as well as at the international level. Japan according to “Japan 2025” should become an attractive and dynamic place to people throughout the world. It projects a country where diverse values come together to foster dynamism and creativity. It aims at making Japan a destination for the world not only to spend their leisure time but also to invest their careers, build their assets, and live their lives.<sup>5</sup>

Three key areas have been focused in the above context that are:

1. The economy of the nation must be reinvigorated to provide the energy to drive the remolding of the nation. Keidanren proposes to bring this about by pursuing a “made by Japan” policy, with Japanese business interests positioned in a broader global context, providing Japan’s knowledge and technology to drive economic development around the world, not just on Japanese soil. Further, sustainable development has also been focused upon. Such a society will make full use of its talents and knowledge and hence economic value will be created and personnel achievement would be achieved. Individual’s efforts would be supported by the new principles of corporate governance that will be a shift from the primacy of the corporations to the people in the society. To further this process, new administrative structures would be added in which the people would take the desired initiative.

The phrase “made in Japan” has in the past served as a symbol of quality engineering performed by Japanese in their own nation. But *Nippon Keidanren* sees the key phrase for the country’s economic activities in the twenty-first century as “made by Japan” — symbolizing Japanese involvement in the creation of value on a global basis. The nation will continue to innovate at home, but it

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<sup>5</sup> “Japan 2025”, *Nippon Keidanren*, [Online: Web], Accessed on 5<sup>th</sup> February 2006, URL <http://www.keidanren.or.jp/english/policy/vision2025.pdf>

will make full use of technological resources from around the world, adding value in this process, both for itself and for the global economy.

2. New Forms of Governance -

*Nippon Keidanren* calls on Japanese companies to revamp their policies of governance to help realize this new society. Communities of self-reliant individuals with clearly defined values will form the core of the Japan of 2025, and people must wean themselves away from the business-centered culture that compels uniformity if they are to play a role in these communities. Toward this end, enterprises will create new structures of corporate governance that give people the space to do their personal best and proper rewards for achieving it.

Trust is the most important element to consider when formulating this new governance. Self-reliant people will be aware of the markets through which society operates—labor, capital, goods, and services—and these markets will need to be open to all if they are to inspire trust among the individuals living in communities affected by them. Corporations and their managers may no longer impose conformity through their leadership of society, but they will continue to play a leading role in the creation of the trust underpinning it.

3. The East Asian Economy -

*Nippon Keidanren* believes that Japan must work to ensure regional freedom and cooperation if it is to wear this mantle of leadership. Our vision for 2025 includes a focus on five freedoms—in the movement of goods, people, services, capital, and information throughout East Asia—and on two vital forms of multilateral cooperation, aimed first at boosting regional economic development and second at tackling global problems impacting the region and threatening its progress. The growing wealth of East Asia should be seen not as a rival to Japanese capital but as a complementary force, and Japan should clarify its open attitude toward this force through policies that open the nation to investment, imports, and

immigration. A Japan at the forefront of an Asian free economic sphere will be an integral part of the global community.

Finally, *Nippon Keidanren* by 2010 aims for a reduction of public pension benefits by 11% in fiscal year 2011 and also for creation of global rules making Japanese firm's knowledge and technologies more marketable around the world. In the social structure sector it aims at finalization of a system for bringing foreign workers to work and live in Japan keeping in mind the changes in the demographic rate. By 2015, it aims for the reduction of the consumption tax rate to 10% (assuming that average annual growth is 3.8%) and by 2020 it aims for the reduction of the overall tax burden on the people to below 50%. Further, it aims at achievement of average annual nominal growth of 3.0% and real growth of 2% over the first quarter of the century. It finally envisions an achievement of an economically healthy Japan with strong environmental awareness and deep ties to the rest of the world economy by 2025 along with a vibrant integrated East Asian Economy.

Each sector of the economy from the labor unions to the *Nippon Keidanren* are trying to do its best by adjusting itself to the changed economic environment and hence in the management practices so that the basic minimum levels of standard of living and national prestige is maintained. Everyone, including the common man on the street has fully accepted the fact that the previous glory of the past cannot be retained, and hence everyone is trying at its own level to at least improve the situation considerably if not the retention of the past economic status. It has been duly accepted that apart from the changes in the government policies, changed management practices has become essential to achieve the above goal and hence, change in the management practices have been fully accepted at all the levels of the society and the economy.

Finally, There is no iota of doubt that Japanese management practices helped a great deal in the creation of human capital and intellectual wealth in Japan. The recession of the 1990s had an adverse impact on the Japanese human capital and also on the Japanese management practices. HR practices as well as Corporate Governance practices underwent a change in favor of the Western management practices. In the HR field, the

solution to the problem, keeping in view several factors such as, the unique culture, norms and ethics of the Japanese society, lies in the combination of both i.e. Japanese management practices as well as the Western management practices as per the changing economic environment. The capacity of Japanese to innovate new management practices is anybody's guess.

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