

Who Runs JAPANESE BUSINESS?

**Management
and
Motivation
in the Firm**

Edited by

Toshiaki Tachibana

in association with RIALS

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Professor of Economics, Kyoto Institute of Economic Research, Kyoto University, Japan

IN ASSOCIATION WITH THE RESEARCH INSTITUTE FOR
ADVANCEMENT FOR LIVING STANDARDS (RIALS)

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Preface and acknowledgements

The aim of this book is to investigate the issues of promotion, corporate governance and related subjects in Japanese firms. Questions are raised concerning who becomes department heads (middle management) and chief executives (top managers); who governs the company; and in what ways business is managed.

In order to examine these issues we conducted two comprehensive surveys: the first was a survey of white-collar employees in several large enterprises, and the second was a survey of executives/board members, in large listed corporate firms. These surveys are explained in more detail in the introduction.

We believe that we have obtained some very interesting results, demonstrating the essence of Japanese business, which will help readers to reach a better understanding of the ways in which Japanese business is conducted.

In Japan, the issues of promotion, corporate governance and business management can be summarized in a few words, which have been adopted as the title of this book: *Who Runs Japanese Business?*

The editor would like to express his gratitude to all the contributors, who have been enthusiastic and cooperative participants since the beginning of this project, and to Professor Sei Kuribayashi, Director of RIALS, who has given his full support to this enterprise.

TOSHIAKI TACHIBANAKI

Introduction

Toshiaki Tachibanaki

1 MOTIVATIONS FOR THIS BOOK

Many business people desire promotion, preferably to the most important position in the firm. The advantages of a higher rung on the hierarchical ladder are not only a better salary but also greater responsibility and leadership. Since individuals often prefer a position where they can supervise other people rather than one in which they are supervised, the degree of satisfaction is higher if they occupy a higher position. There are, however, various levels of high-status position in the firm. The most capable and ambitious person aspires to become the president (that is, Chief Executive Officer, or CEO) of the company. Most people do not want the job of top executive (that is, to be a board member), but would prefer one which is more suited to their capabilities and lifestyle. A significant number of people do not enjoy fierce competition, which is one of the necessary conditions for being promoted, and they may simply say that they work to ensure a decent standard of living, without wishing for any promotion.

The purpose of this book is to examine various issues related to promotion in the firm, such as the reasons and motivations for it, and the characteristics and lifestyles of the people who are promoted. Although the principal tool used here is based on economic analysis, some tools from the disciplines of psychology, sociology and education are also employed, to reflect broader factors associated with promotion.

In this book, the two main targets for promotion are top executives (or board members) such as presidents, vice-presidents, chief and managing executives, ordinary executives and auditors, and department heads (a description which encompasses a wide range of positions). These two ranks can be regarded as symbols of promotion, namely the highest position and middle management. It is not an exaggeration to say that people aspire to these two symbolic positions when they desire promotion. The ultimate winners in the promotion race, whose numbers are extremely small, are the top executives. In other words, most people are unable to attain such a position regardless of their wishes. The position of depart-

ment head includes various elements. For some people it is the final goal in their career, while for others it is merely the intermediate rung on the ladder. We should also not forget those who are unable to attain middle management, whether they want to or not.

We shall investigate in depth the question of who are promoted to these two positions. The following related issues will also be investigated: the degree of desire for promotion; working style, lifestyle and expectations; and the reward of promotion among the winners in the promotion competition. The effects of a university education, including the name of the university and the speciality studied, the assessment of individual performance by managers, opinions concerning competition, and related issues will also be examined. We shall also investigate the economic incentives behind the fierce competition for promotion, both theoretically and empirically, and study what kind of effort incentives are offered by the firm. Accordingly, we shall evaluate whether or not the seniority and/or the merit system has worked well for the determination of both wages and promotion.

Finally, in Japan, these issues of promotion, corporate governance and business management can be summarized in the few words which have been adopted as the title of this book. Questions such as 'Who is promoted to department head and top executive?', 'Who governs the company?', and 'In what way is business managed?', are all related to the question 'Who runs Japanese business?'.

2 TOP EXECUTIVES

First, we shall consider the promotion of top executives (that is, board members). They were obviously the winners in the cut-throat competition for promotion. The following questions will be addressed: 'Who are the winners?', 'Does the name of the university matter?', 'Did they study humanities or sciences at university?', 'What kind of career pattern did they have?' and 'Have they frequently changed their job and position in the firm, or did they have a broad or narrow career?'

It is useful to know the conditions under which top executives achieved their promotion in spite of stiff competition. Was it achieved because of the merit system, or through the influence of superiors, or simply as a consequence of luck? At the same time, we shall investigate what kind of working style and lifestyle top executives had before achieving such a position. In other words, whether they worked conscientiously for the firm and whether they were involved exclusively in company life became central issues.

The managerial principle relating to top executives, that is, their role in the firm, is vital in determining the future of the firm because the highest decisions are made by top executives. Therefore it is important to understand the role of top executives. This role is closely related to the following questions: 'Who owns the firm?', 'Who governs the firm?', 'Why does the firm exist?' and 'What is the relationship among shareholders, top executives and employees?'. These issues are simply called 'corporate governance'. Corporate governance is still an open question in Japan, and therefore its understanding will be enriched by the results obtained in this book.

One controversy in this field in Japan, is whether firms are owned by share-holders or by workers (that is, labour-managed firms). The labour-managed firm hypothesis, is more popular in Japan than the shareholder hypothesis, at least for Japanese firms, although it is true that corporate firms are legally owned by shareholders. Some specialists emphasize the intermediary role of top executives between shareholders and employees. This book intends to examine these issues carefully, and to give an answer to these questions.

One novel feature in this book is that we are concerned with the differences among various levels of top executives, such as presidents, vice-presidents, chief and managing executives, ordinary executives and auditors. It will be possible to identify the different level and range of responsibilities which they undertake, and such differences will reflect different managerial principles, lifestyles, and naturally, salaries. Also, we shall be concerned with the influence that the name of a particular university may have on the possibility of achieving the position of top executive.

Another interesting concern in this book will be to investigate the effect of both internal and external experience in the development of the managerial role of top executives. Although many of the top executives surveyed here were promoted internally, several executives were appointed by financial institutions, or parent companies in the case of subsidiary firms. Consequently, they have had longer external experience in other firms. This difference between internal and external experience may provide a new insight into our understanding of corporate governance in Japan.

3 WHITE-COLLAR EMPLOYEES INCLUDING MANAGERS

The next subject to investigate will be the promotion process to middle management, that is, department head. More broadly, the work incentive, and treatment of white-collar employees in general, will be examined.

The following comments reveal attitudes towards the middle manager position as a symbol of promotion in Japanese firms: 'I would like to be promoted at least to department head during my career', 'I desire to be promoted to a higher position than a department head', 'The position of department head does not suit my personal taste', 'I do not want to be promoted because supervising subordinates is worrying and uncongenial', 'There is no chance of promotion for me because of my qualifications', and so on. Impressions from managers that business people regard middle management as a symbol are complex and mixed. It will be interesting and valuable to investigate who are promoted to department heads, and in what way.

The investigation on promotion probabilities to department head will enable us to collect useful information, such as wage determination and promotion in general, for the understanding of the treatment of white-collar workers. In other words, we shall be able to find out how employers evaluate the ability and performance of individual employees, and in what way they utilize such information for the determination of wages and promotion. The most crucial policy goal of human resource management for firms is to provide the highest incentive for employees, and to design the most efficient human resource allocation. It will be interesting to examine whether or not such a goal has been achieved in Japanese firms.

We shall investigate the firm's system of assessment of its workers' ability and performance. In other words, we shall investigate when the firm starts to differentiate promotion possibilities among employees who entered the firm in the same year. Also, we shall investigate the extent of the maximum range in wage rates between the most and the least productive employee. This differentiation in promotion and wages implies that the firm will respond positively to the high contribution of productive employees, or will raise their incentive levels. This is a rational assessment system because it is important to maintain strong incentives for productive employees. A difficult and controversial subject will be to evaluate the degree of work incentive for less productive workers, when favourable treatment of productive workers seems excessive. It is said that Japanese firms do not have a very wide wage differential between productive and less productive workers, or an early promotion policy (which implies that promotion is determined at a relatively young age) because they are afraid that this would be a poor incentive for less productive workers and would lead to shirking and uncooperative behaviour. For three recent international comparisons on this subject, see Tachibanaki (1994), Ohashi and Tachibanaki (1998) and Tachibanaki (1998). This book will investigate the relationship between work incentives and the assessment system in several large firms, both theoretically and empirically.

One of the common systems in Japan is called the seniority system, in which both wages and promotion are determined mainly on the basis of the workers' period of employment in the firm. This system has worked fairly well, maintaining a strong work incentive for all employees, and deterring them from shirking. Three of the economic interpretations of the seniority system are called the insurance, human capital and the non-shirking hypotheses. We would like to find out which hypothesis is appropriate for the Japanese system. In other words, we shall be concerned with the economic rationality of the seniority system. The Japanese system also sets a high premium on the role of education and age in the determination of wages and promotion, in addition to seniority (that is, length of employment) in the firm. An overall economic interpretation will be made, taking into account variables such as age, seniority and education.

Although we have talked about assessment of individual performance in business activity, it will not be easy to implement such an assessment in reality. Employees who are engaged in sales activity are easily assessed because their performance can be quantified without much difficulty. Take the example of a car dealer who is engaged in selling cars. Assessment of this kind of activity is easy, and invites no severe criticism. Other types of jobs, however, such as planning, accounting, personnel, general administration, and so on, cannot be so easily assessed. Several types of engineering jobs and jobs in team production are also difficult to assess. If an assessment is judged as unfair by employees, then the degree of dissatisfaction, which is likely to undermine work incentives, may grow. In particular, an assessment which is made largely on the basis of subjective judgement is a risky undertaking.

Although firms try to prepare an assessment system which will minimize such risks, there is no ideal system. A fruitful area of investigation will be to assess how fairness is evaluated by workers. We shall consider the opinion of workers on the concept of fairness, which plays an important role in the actual implementation of assessments of individual performance.

Another worthwhile approach in this book will be to investigate the importance of each individual worker's own assessment of his or her performance. Normally, an assessment is made by other people such as managers, or those who occupy superior positions. If the discrepancy between self-assessment and that made by the manager is large, then trouble will arise. Alternatively, it is possible to understand that self-assessment is more reliable than that made by other people because a person normally knows him- or herself best. Therefore, we shall use the information of individual workers' self-assessment to evaluate the

economic implication of performance on work incentive. The idea is to estimate a possible discrepancy between the current wage, and the potential wage which corresponds to the individual's self-assessed contribution to the firm. The sign and the degree of such a possible discrepancy will enable us to derive the economic implication of work incentives.

This will complete the section associated with the promotion to managers. The information will enable us to discuss the economic interpretation of the relationship between work incentives and promotion for white-collar workers. There are three methods which can be employed for the empirical investigation of promotion in the firm. The first is to conduct statistical analyses from a survey (that is, a questionnaire) completed by workers, and to derive some conclusions. The second is to trace the individual careers of workers from entry into the firm to their current position, and to assess the implications. The third is to conduct frequent interviews of many employees, and to collate the results. Although we use the first method principally, we shall also supplement our examination with the other two.

4 PRESTIGIOUS VERSUS OTHER UNIVERSITIES, AND SCIENCE VERSUS HUMANITIES GRADUATES

A socially controversial and popular concern in Japan is the effect that the name of a university has on promotion in the firm, or more broadly on the success of an individual career. Another interesting subject is the difference between graduates in science and technology, and those in humanities and social science. These factors are relevant only to university graduates, so white-collar graduates will be studied in greater detail.

It is not only in Japan where meritocracy or preferential treatment for the graduates of prestigious universities is observed. Meritocracy here implies that those people will reap the benefits throughout their career in both firms and public institutions. We can cite several examples of these universities: Tokyo and Kyoto in Japan, Harvard and Yale in the United States, Oxford and Cambridge in the United Kingdom, and Ecole Polytechnique and ENA in France. Germany is the only exception among the G-5 countries, as it does not have any comparable universities. We shall investigate whether the graduates of prestigious universities have a higher probability of being promoted to higher office in Japanese firms, and, if this is the case, we shall look for explanations.

The words 'examination hell' are common in Japan, implying that very fierce competition is observed among candidates for university entrance, in particular for prestigious universities. Not only higher intel-

lectual capability but also significant effort are required to be able to pass the difficult entrance examinations. Those who graduate from prestigious universities have higher qualifications for their business and professional careers. This success, however, only indicates academic achievements. There should be particular reasons or qualifications other than academic capability, if these graduates are to have a higher chance of promotion. We shall search for such particular reasons and qualifications and, at the same time, discuss whether or not such favourable treatment is socially justifiable.

The next subject will be an investigation into the difference between science and technology, and humanities and social science graduates. There are three common assumptions in Japan about university graduates who have studied science and technology subjects such as mathematics, physics, chemistry, biology, engineering and agriculture. First, the probability of their being promoted to a higher position in the firm is lower than that for humanities and social science graduates. Second, employees who have studied science and technology wish to be specialists rather than managers in the firm for various reasons. Third, there are many people who have completed postgraduate degrees in science and technology, who are in many respects very different from graduates with degrees in the humanities or social sciences. We shall examine whether or not the above three assumptions are true, and provide reasons. In sum, we shall analyse the differences between science and technology, and humanities and social science graduates regarding promotion likelihood, career patterns, lifestyles, and other related factors.

5 SIGNIFICANCE OF WORKING ACTIVITY AND TRADE UNIONS

To conclude this study, we shall discuss a final but very important subject – the significance of work activity in human life. It is natural that employees who have been promoted to a higher position should work hard. There should be no serious problem regarding the motivation of these people. Most workers, however, even white-collar employees, do not achieve the desired promotion because competition is so fierce and, of course, a large proportion of workers do not even seek promotion.

If the degree of work satisfaction among those workers who fail to achieve promotion were higher, it would not be necessary to take any action. It is, however, possible that they are dissatisfied. Therefore, we shall study the important subject: ‘Why do white-collar workers work?’. Is it only for wages (that is, to ensure a basic standard of living), or for

promotion, for job satisfaction, or for other reasons? Finally, the role of the trade unions in achieving the highest satisfaction level for workers will be discussed.

6 SUMMARY

It is useful to present here a brief survey of selected topics which have been discussed in this introduction, and which will be investigated in depth in this book.

1. Who is promoted to the two symbolic positions in the firm, namely top executive (board members) and middle management (department heads)? The mechanism for the determination of promotion, that is, when it is decided, who determines it, and on what ground it is selected, will be carefully evaluated.
2. What is the economic rationality of the seniority system which is a common determinant for both wages and promotion in Japan? There are also other economic theories which can explain the relationship between work incentive and wages or promotion. We shall discuss these theories in the Japanese context.
3. Is it preferable to prepare for broader or narrower careers for white-collar workers? At the same time, the role of professional or specialized, rather than managerial, careers will be discussed.
4. The role or the management principles of top executives will be thoroughly investigated. This is likely to shed light on the understanding of corporate governance in Japanese firms.
5. We shall investigate the role played by 'prestige' universities in the determination of promotion in the firm, and clarify the difference in career, lifestyle, and so on between science and humanities graduates.
6. There are many workers who have no possibility of promotion, whether through choice or not, and therefore it is important to increase their degree of job satisfaction. There will be a full discussion on this issue, including the role played by trade unions.

The overall summary of these subjects is expressed in the title of this book, *Who Runs Japanese Business?*, and we hope that the book will provide readers with some answers.

7 SURVEY DATA USED IN THIS BOOK

Survey of White-collar Employees

This survey was conducted in 1993 for white-collar employees in five significantly large firms. These five firms are, of course, anonymous, but it is possible, nevertheless, to specify the different kinds of business, namely, automotive, electronics, chemical and electric power companies, and a department store. The employees surveyed included both those who had been promoted and those who had not – including section heads, department heads and directors but excluding top executives. The number of questionnaires distributed was 2,100, and the response rate was an impressive 86.5 per cent. Thus, the total number of completed questionnaires was 1,816.

Survey of Top Executives

This survey was also conducted in 1993. We posted questionnaires to 8,000 top executives and auditors, described as board members in a total of 2,128 listed corporate firms which were randomly selected from the data base *Toyokeizai Top Executive Survey*. The survey included 40,800 top executives, who were all appointed at the firms' shareholders' meeting. The selection rate from the original survey was 19.6 per cent, and the response rate was 28.1 per cent. The total number of completed questionnaires was 2,246.

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