



‘Japanese Management 20 Years On: The Contemporary Relevance of Japanese Management Practices’

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Japanese Management 20 years on

The contemporary relevance of Japanese management practices



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The Advanced Institute of Management Research (AIM) develops UK-based world-class management research. AIM seeks to identify ways to enhance the competitiveness of the UK economy and its infrastructure through research into management and organisational performance in both the private and public sectors.

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- Working in cooperation with leading international academics and specialists as well as UK policymakers and business leaders...
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- Engage with practitioners and other users of research within and beyond the UK as co-producers of knowledge about management

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Current AIM research projects focus on:

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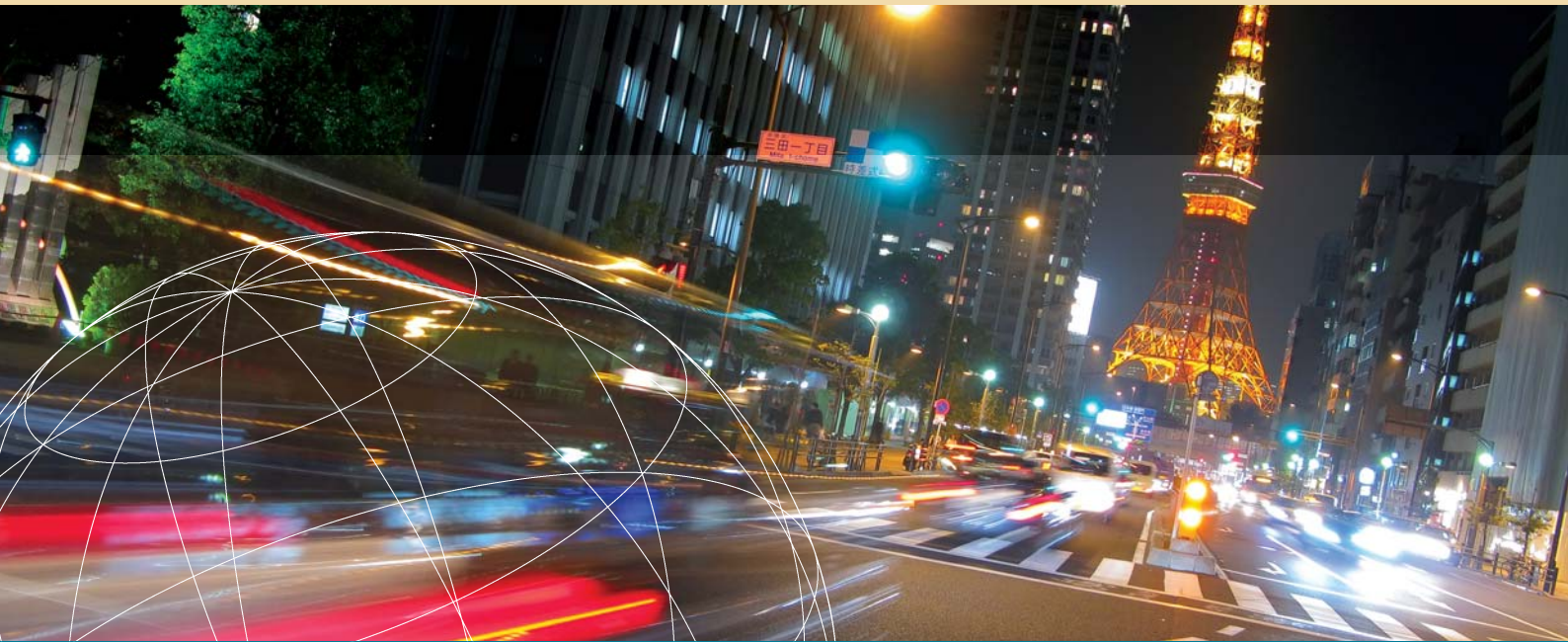
How can UK policymakers evaluate and address concerns surrounding the UK's performance in relation to other countries?

National productivity has been the concern of economists, government policymakers, and corporate decision-makers for some time. Further research by scholars from a range of disciplines is bringing new voices to the debates about how the productivity gap can be measured, and what the UK can do to improve the effectiveness of UK industry and its supporting public services.

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How can UK managers disseminate their experience whilst learning from others?

Improved management practices are identified as important for enhancing productivity and performance. The main focus is on how evidence behind good or promising practices can be systematically assessed, creatively adapted, successfully implemented and knowledge diffused to other organisations that will benefit.

This report discusses the contemporary relevance of Japanese management practices to managers, policymakers and academic researchers. In the 1980s, a period marked by strong performance of the Japanese economy and the emergence onto the global stage of a number of leading Japanese corporations, managers and management academics in the UK and other Western countries studied Japanese management with great interest. There was widespread recognition of the efficiency and competitive advantage afforded by certain management practices and several features of the 'Japanese model' were adopted by companies in the UK, continental Europe and North America. However, two decades of weak economic growth have undermined this belief that Japanese management can serve as a role-model for Western firms.

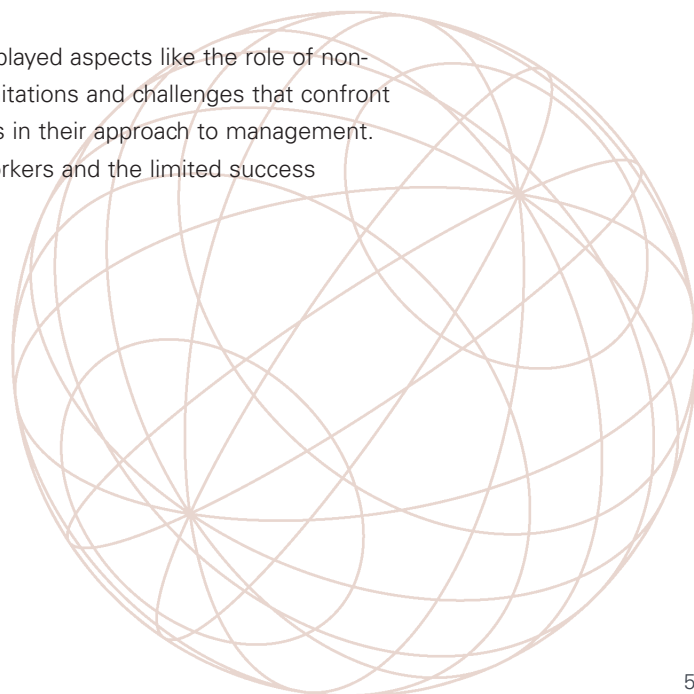
There was widespread recognition of the efficiency and competitive advantage afforded by certain management practices...

Since the emergence of the Japanese model in the 1980s, important changes have been made in the management practices of Japanese firms. A major factor has been the effort to control costs of production in a global economy where the influence of China as a centre for cheap manufacturing has undercut many competitors. In addition, the ability of countries like South Korea and Taiwan to develop cheap, fashionable and fast moving consumer electronics and telecommunication goods has challenged Japanese hegemony in this area. Japan has therefore faced the problem of how to adapt to the new era of globalisation whilst carrying forward the legacy of the 'lost decade' of the 1990s.

Developments like the introduction of performance pay and a greater use of non-regular employment are indicative of a move towards a more market-oriented and diverse Japanese economy that could cheapen overall labour costs. This has been accompanied by significant off-shoring to China and other parts of Asia of segments of the manufacturing process, again in order to reduce costs.

At the same time, there is an important continuity behind the changes and the nature of the management practices remains specific to Japan. It suggests the emergence of a new, or revised, Japanese model which differs from its predecessor in various ways. It stresses the increased diversity between industries and firms, in part due to differential rates of internationalisation.

The new model acknowledges previously underplayed aspects like the role of non-regular employment. It recognises important limitations and challenges that confront Japanese firms in seeking to shift the emphases in their approach to management. Examples include the position of non-regular workers and the limited success in certain knowledge-intensive industries.



Study of Japanese management remains relevant to British policymakers, managers, and management academics.

This model no longer offers the same promises of success as 20 years ago. However, it offers more detailed insights into the diversity, tensions and challenges of management. As such, it can provide important lessons. Not least amongst these is the recognition of the locally created and developed character of management practices. Also important, particularly at this time of economic difficulty throughout the mature economies of the West, are the insights that can be gleaned on how firms can tackle recessionary pressures. In this sense at least, the practices of Japanese firms continue to offer lessons for others.

Key findings

- Japanese management practices have changed considerably since 1990 as firms have followed certain international trends like the introduction of performance-related pay and a greater use of non-regular employment. This has not only increased the role of market forces but also resulted in new diversity between industries and firms.
- Some Japanese firms are becoming more international in terms of their production processes and this has had impacts on the nature of their management, their ability to learn from abroad and their role in the home Japanese economy. Internationalisation has also created challenges for Japanese firms in managing their supply chains.
- At the same time, the outcomes are specific to Japan as practices like lifetime employment remain strongly supported. The 'Japanese model' has shown a persistence and flexibility which belies earlier predictions of its collapse.
- Examination of the practices found in Japan offers alternatives to the dominant approach to economic recession found in the UK and other Western economies. For example, given Japan's economic difficulties over the past two decades, the unemployment rate remains much lower than one might expect. Firms' approaches to employment relations and their commitments to employees help explain this.
- While there are key continuities, understanding of the new Japanese model differs substantially from that of its predecessor. It acknowledges greater diversity between industries and firms and also highlights previously underplayed and negative aspects like the conditions of competitive success and the position of non-regular employees.
- Study of Japanese management remains relevant to British policymakers, managers, and management academics. The new model can offer more detailed insights into the diversity, tensions and challenges of management and can provide important lessons and inspiration accordingly. Moreover, the development of this model over time underscores the importance of understanding the locally specific and contingently emergent nature of management practices contra a universal one-size-fits-all approach.

The Japanese management system

By the late 1980s, Japanese companies had gained a competitive advantage over their American and European counterparts in a number of technology related industries, from consumer electronics to automobiles. So significant was the advantage that some observers predicted that the Japanese economy would overtake the United States economy's position as the largest in the world by the 21st century. Much of Japan's success was attributed to a distinct management style which became known as the Japanese model of management.

Unsurprisingly, other developed economies were soon clamouring to discover more about Japanese management methods. Western scholars and executives were eager to learn the lessons of Japan's success and Business Schools incorporated courses on Japanese management. Corporations actively sought to copy from their Japanese counterparts in the hope of matching the Japanese competition.

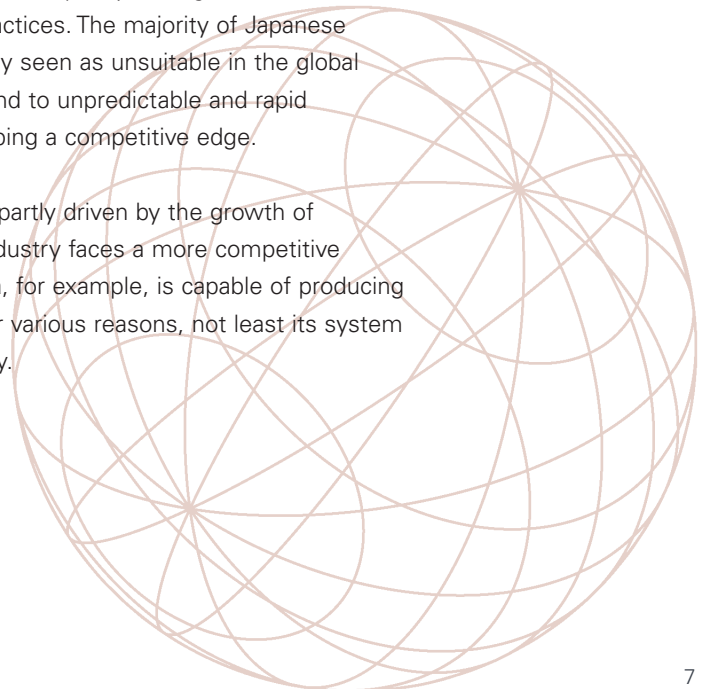
A spate of publications on Japanese management appeared. Management bookshelves grew heavy under the weight of titles such as *The Art of Japanese Management* by Richard Pascale and Anthony Athos, *Kaisha: The Japanese Corporation* by James Abegglen and George Stalk, and William Ouchi's *Theory Z*. One particularly influential work was *The Machine that Changed the World* by James Womack and colleagues, which presented Japanese 'lean production' as a new universal standard for the management of manufacturing operations.

But then, in the 1990s, everything changed. The runaway Japanese economy hit the buffers in the early 1990s. Since then Japan, despite its position as the world's third largest economy (after the US and China), has experienced stagnation and minimal growth.

Perceptions of Japanese management have fundamentally altered. Following the country's downturn in economic fortunes, many Japanese practices have been criticised as outdated and suitable for a developing rather than a mature economy. Some features, such as kaizen, just-in-time, and total quality management, have been adopted into mainstream management practices. The majority of Japanese management practices, however, are increasingly seen as unsuitable in the global knowledge economy, where the ability to respond to unpredictable and rapid advances in technology is a key factor in developing a competitive edge.

Criticism of Japanese management methods is partly driven by the growth of new competitors in world markets. Japanese industry faces a more competitive environment than it did in earlier decades. China, for example, is capable of producing goods much more cheaply than Japan, which for various reasons, not least its system of lifetime employment, is a high wage economy.

Corporations actively sought to copy from their Japanese counterparts in the hope of matching the Japanese competition.



Other countries, such as South Korea, for example, have increasingly found ways of combining incremental innovation with low costs of production and rapid speed to market, allowing them to grow rapidly in the consumer electronics markets that were dominated by Japan in the 1980s.

It would be wrong, however, to see the Japanese management model as largely unchanged since the 1980s. The tendency to view Japanese management in a negative light today ignores important changes that have taken place in the last two decades. Japanese firms and successive governments have responded to the difficult economic circumstances by making important adaptations to many existing management practices that are considered fundamental to the Japanese model.

If anything, it is time for a reassessment of the Japanese management model that takes into account both the changed practices and the wider circumstances in the Japanese economy. This report aims to provide such an assessment. It is a timely reappraisal given the major challenges facing the mature economies of the West and their corporations in this current period of global economic difficulties.

The tendency to view Japanese management in a negative light today ignores important changes that have taken place in the last two decades.



The origins of the Japanese model of management that found so much favour with Western commentators can be found in the institutional settlements that became fully established in the country after World War II. The shape of the Japanese business landscape in turn led to key characteristics in management. In the heyday of the Japanese economy, Japanese management consisted of a collection of practices that emphasised long-term over short-term goals, and collective over individualist principles.

The Japanese business landscape

At the time of the Japanese management miracle Japanese business had a number of distinct characteristics:

Main banks – The majority of Japanese firms did not use capital markets to obtain funding. Instead, they secured their capital from the banking system. Most firms had a relationship with a ‘main bank’ that extended credit to the corporation at preferential rates and performed an important monitoring role.

(Horizontal) keiretsu relations – A traditional feature of Japanese business, a *keiretsu* is a group of companies. This group is characterised by close affiliations between the various members of the group – and usually shares the same main bank. Examples of horizontal keiretsu include Mitsubishi, Mitsui, and Sumitomo.

Supply chains – Many of Japan’s leading manufacturers also developed vertical keiretsu, supply chain networks with tiers of dedicated subcontractors. Toyota, in particular, revolutionised supply-chain management featuring long-term and intimate collaboration, particularly through its just-in-time and lean production systems.

Mutual shareholding – Firms tended to have cross shareholdings with their main banks, fellow firms within the same keiretsu, and selected suppliers. This prevented takeovers and supported stable growth.

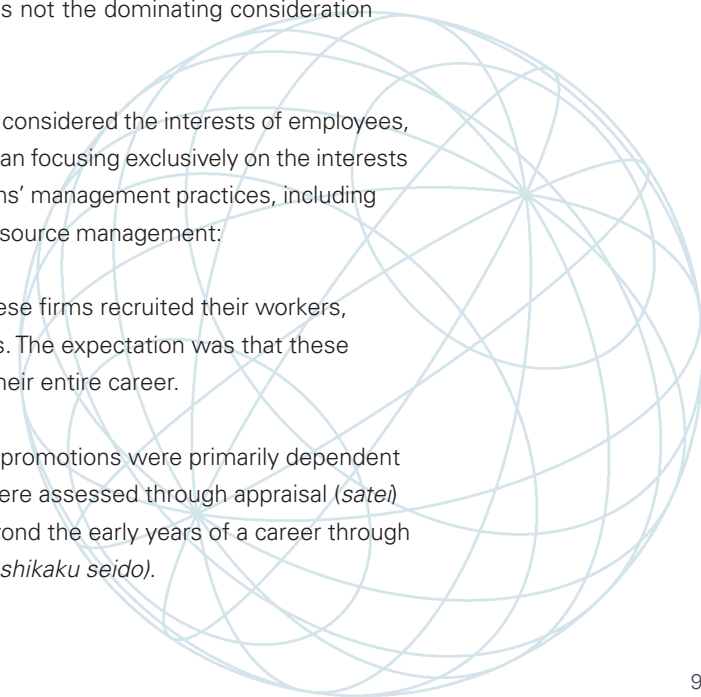
A long term approach

The characteristics of Japanese corporate life detailed above enabled Japanese firms to focus on improving productivity and expanding market share, favouring long-term growth over short-term profits. Unlike the Anglo-Saxon corporate model, a primary concern for the position of the shareholders was not the dominating consideration of Japanese corporations.

Instead, when making decisions managers often considered the interests of employees, members of the keiretsu, and suppliers, rather than focusing exclusively on the interests of shareholders. This provided the context for firms’ management practices, including the so-called ‘three pillars’ of Japanese human resource management:

Lifetime employment (*shūshin koyō*) – Japanese firms recruited their workers, mostly men, from the country’s elite universities. The expectation was that these employees would work for a particular firm for their entire career.

Seniority wages (*nenkō jōretsu*) – Wages and promotions were primarily dependent on seniority. Individual skill and achievements were assessed through appraisal (*satei*) and influenced remuneration and promotion beyond the early years of a career through a so-called ability qualification system (*shokunō shikaku seido*).



Enterprise unionism (kigyō kumiai) – All employees of the firm, with the exception of those in managerial positions above a certain rank, were represented by a single union. These unions tend to have a harmonious relation with management to avoid disruption to the firm's operations. These employment practices created strong ties between the firm and its employees and contributed to employee commitment. Employees were strongly motivated as they competed for promotions that determined the distribution of future wages.

Moreover, the long-term nature of employment in Japanese firms supported the development of firm-specific skills through a combination of job rotation and on-the-job training. These skills enabled workers to handle unusual operations, whether that was dealing with change, or solving problems, to participate successfully in teamwork and kaizen or quality circles, and to share responsibility for the coordination between workshops. Indeed the long-term nature of employment contributed to some of the major strengths of Japanese firms, in particular the many process innovations in manufacturing.

During this period the Japanese economy was able to grow by exporting cheap and reliable products, especially to Europe and the US. In many of the developed Western economies at the time manufacturing sectors had become dogged by high wage costs, low productivity increases, weak innovation processes and poor quality control. Thus the relatively high costs which Japanese firms incurred by maintaining lifetime employment were recouped through the growth of the export markets over the 1970s and 1980s.

Contingencies for success

The lifetime employment model was not universally applicable to all Japanese employees. Indeed, many practices were limited to a minority of leading Japanese firms. Features such as long-term employment and seniority-based pay only applied to the minority of workers in such corporations. Moreover, the success of these organisational and employment practices was dependent on certain factors. For example:

The need for organisational growth – Strong growth enabled the recruitment of many young and relatively cheap workers and, therefore, kept average labour costs low. It also allowed companies to motivate workers by creating new positions for promotion. Without strong growth the efficiency of these employment practices is likely to diminish.

The firm-specific character of skills – These skills were well suited to the incremental innovations that enabled Japanese firms to outperform their foreign competitors. They were less suitable, however, for fast-changing and knowledge-intensive technologies. In the modern economy, specialist knowledge or creative ideas, which have little to do with the length of in-house training, are primary drivers of the competitive strength of firms. The long-term character of skill development may actually hinder a swift and flexible response to new opportunities.

These factors have clearly become more critical in recent years. Both economic growth and the importance of manufacturing in the Japanese economy have declined. Other factors like the rise in white-collar positions, the process of globalisation and the increase in (foreign) competition, and the ageing of the population, have also diminished the efficiency of Japanese practices. For a long time, the impact of these developments was absorbed by the economic successes of the post-war period. However, this changed after its economic bubble burst at the end of 1989, and the subsequent economic malaise proved an important trigger and catalyst for change.

changes in employment and employment practices

To properly appraise modern Japanese management practices we need to consider them in the light of some fundamental changes that have affected the Japanese economy and working life.

Focusing on employment and employment practices, three major developments stand out: the increase in off-shoring of parts of the production process, first to South East Asia, and later from the mid-1990s to China; the introduction of performance-related pay; and the rise in non-regular employment. These developments can be considered a direct response to the rising wage costs in the absence of organisational growth.

1 Off-shoring

In the 1990s and 2000s, Japanese multinationals increasingly moved parts of production out of Japan. This was partly a response to issues of market access and the need to ensure that Japanese industry was behind any potential tariff barriers developed by the EU or NAFTA. Principally, however, particularly in relation to the Asian area, it was driven by plentiful labour, low wages, and other cost benefits (such as the tax benefits offered for investing in certain locations).

...performance-related pay, known in Japan as *seikashugi*, has enabled firms to bring wage costs down as it rewards employees for their direct contribution...



Thus Japanese multinationals moved from being primarily export-based to being increasingly global coordinators of production chains that were partly internalised and partly externalised. Over recent years, this has produced new problems, in particular in relation to maintaining quality standards in foreign contexts (see the discussion on Toyota on page 15). It also confronts Japanese firms with new problems about how to develop a managerial cadre which is international in orientation (and at least in part in origin) and is capable of managing across national borders. Thus off-shoring and outsourcing, which were inevitable responses to the problems of cost faced by Japanese industry, have brought new problems related to management coordination and managerial skills.

2 Performance-related pay

The introduction of performance-related pay, known in Japan as *seikashugi*, has enabled firms to bring wage costs down as it rewards employees for their direct contribution, rather than the long-term productive potential of their skills. Research by the Japan Institute for Labour Policy and Training in 2004 revealed that 57.8 per cent of all firms had introduced *seikashugi*, with this share rising to 74.0 per cent among firms with more than a thousand regular employees. A survey by the Ministry of Economy, Trade and Industry in 2003 found that 77 per cent of firms used individual performance as an element for determining salary (see box opposite for example of performance-related pay).

The introduction of performance-related pay

The character and implications of performance-related pay can be illustrated by focusing on an example, in this case an electrical machinery manufacturer.

Like most other Japanese electronic firms, the company faced difficult economic circumstances in the 1990s and 2000s. The firm introduced performance-related pay as early as 1999, with small adjustments in subsequent years, as part of a strategy to strengthen efficiency.

The current system evaluates employees according to ability and performance. The ability assessment via an ability qualification system has been in place for decades. The assessment of performance, however, is new.

Performance is assessed using management-by-objectives (*mokuhyō kanri seido*). Every half year, the employee and supervisor agree four main tasks for the following six-month period. The objectives depend on the division, function and person. A new objective can be set when a task is completed, when a new task is needed or when priorities change.

Below is a representative example of the forms used. A difficulty rating, (1-5), is ascribed to each objective. Afterwards, the results are evaluated, by both the employee and supervisor, and an achievement rating is ascribed (0-5). The difficulty and achievement ratings are multiplied for each objective and then added together to arrive at a score, with a maximum total of 100 points. In addition, the manager will take the overall job performance into consideration and may award some additional points.

The points do not directly translate into a specific bonus amount but function as a reference for managers to compare their subordinates. It translates into an overall evaluation outcome from 'E2' as the highest to 'B' as the lowest ('E1' and 'A' are the intermediate outcomes). Together with the performance of the division the employee works for, this assessment determines their bonus for the half year under consideration.

Representative example management-by-objectives form

Organisation/Division							
Objectives	Assignment/Task (task – deadline – metric – process)		Evaluation Comments		Level of difficulty	Level of achievement	
					Pts.	Pts.	
			EE.		Pts.	Pts.	
			Mgr.		Pts.	Pts.	
				EE.		Pts.	Pts.
				Mgr.		Pts.	Pts.
				EE.		Pts.	Pts.
				Mgr.		Pts.	Pts.
				EE.		Pts.	Pts.
				Mgr.		Pts.	Pts.
	Employee Self-evaluation			Evaluation by the manager			
	Total Score	Difficulty	Achievement	Total	Difficulty	Achievement	Total (a)
		pts.	pts.*	pts.=	pts.	pts.*	pts.=

With some small differences this process for determining bonuses applies to both non-managerial and managerial employees. However, there is an important difference in the impact on wages. In the case of non-managers, the evaluation is likely to bring a 'permanent' or 'cumulative' increase in salary. In the case of managers, however, there is the base salary and each year the evaluation determines how much is added to this salary, so there is not the build-up that exists for non-management employees.

Finally, the decision about promotion is taken in July in accordance with certain rules. These rules are not set in stone but managers, for instance, should have at least three years of an 'E1' assessment to receive promotion. For the top level, at least three years of 'E2' are needed.

Although it provides only a brief description of the firm's practices for performance-appraisal and performance-related management the example illustrates how firms have made the necessary investments to introduce 'performance' as an additional criterion for the evaluation of employees. Performance-related pay is not added as an extra component but integrated in the firm's system for evaluation, remuneration, and promotion.

The example opposite is representative of other firms. Almost all firms use management-by-objectives to assess performance. However, it is important to note that these shifts towards a more individualistic approach to performance management have been interwoven with existing management practices retaining much of the previous character.

This confirms that the local adoption of management practices is not simply a question of the unreflective introduction of a best practice model. Successful implementation requires local adaptation and negotiation. Firms are selective when introducing performance-related pay. They continue to invest in the long-term training of regular workers and have upheld ability and even seniority as criteria for evaluation, especially for younger employees. At the same time, there are also important differences between firms concerning, for example, the types of objectives, the inclusion of performance among other criteria for evaluation, the impact of performance on pay, and the process for evaluation.

3 The rise in non-regular employment

Part-time and *arubaito* employment are two important types of non-regular employment.

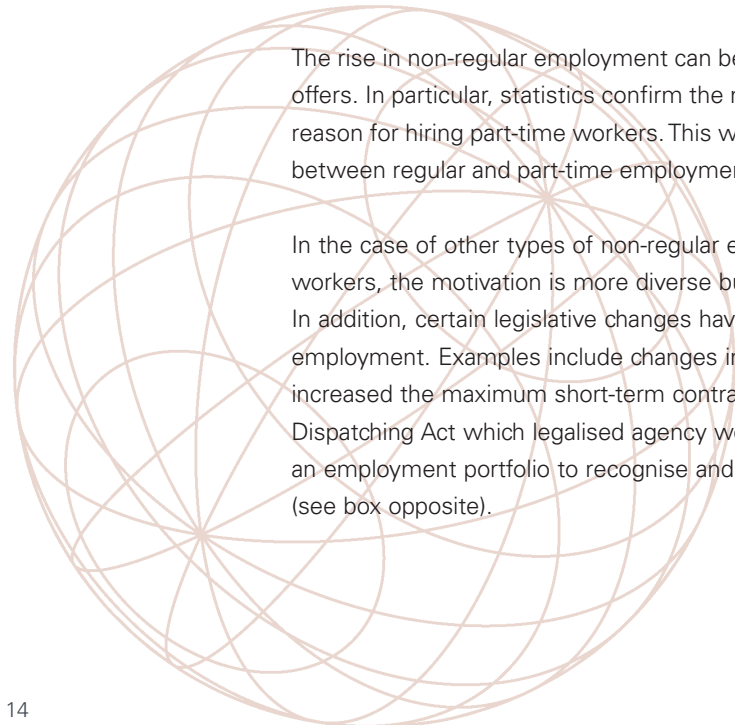
The third major development has been the rise in non-regular employment. This rise has been particularly striking since the 1990s. The overall share of non-regular employment has risen from about 20 per cent in 1995 to almost 35 per cent in 2008.

Part-time and *arubaito* employment are two important types of non-regular employment. Part-time workers are workers whose scheduled working hours are less than those of regular employees in the same workplace. Usually 35 hours a week is taken as the dividing line in this respect. *Arubaito* jobs are taken by someone still in school or with other reasons to work a small number of hours. Other major types of non-regular employment are agency workers and various groups with fixed-terms contracts.

It is obvious that the shift from manufacturing to service industries has contributed to this rise in non-regular employment. In industries like retail and hospitality, part-time employment tends to account for more than 50 per cent. Within specific formats, this share is even higher.

The rise in non-regular employment can be explained by the cost advantages that it offers. In particular, statistics confirm the need to control labour costs as the dominant reason for hiring part-time workers. This was reinforced because cost differences between regular and part-time employment increased during the 1990s.

In the case of other types of non-regular employment, like agency and contract workers, the motivation is more diverse but cost considerations are also important. In addition, certain legislative changes have contributed to the appeal of non-regular employment. Examples include changes in the Labour Standards Act that have increased the maximum short-term contract period and the introduction of the Worker Dispatching Act which legalised agency work. Finally, employers developed the idea of an employment portfolio to recognise and advocate the rise in non-regular employment (see box opposite).



The Nikkeiren employment portfolio

The idea of an employment portfolio was introduced in 1995 by Nikkeiren, an employers' organisation which merged with Keidanren in 2002 to form the main employers' organisation Nippon Keidanren. The multi-track personnel system proposed by Nikkeiren has received a lot of publicity. The proposal argued for a reorganisation of the corporate employment portfolio into three groups of employees:

- 1 a core or elite group of long-term employees
- 2 a group of specialists for dealing with specific problems
- 3 a peripheral group for simple routine tasks

The table below shows how each group has its own type of employment contracts and different rules for promotion, remuneration, training, etc. A crucial difference is between open-ended employment contracts for the core group and fixed-term contracts for the other two groups.

	Type of employment	Employees eligible	Wages	Bonuses	Basis for promotion/ advancement
Core group of long-term employees (A)	Open-ended employment contract	Managerial career track, core-technical occupations	Monthly salary or yearly remuneration package; ability-based wages; wage increment	Specified rate and sliding scale for performance	Promotion to managerial ranks; pay increase based on job performance qualifications
Specialists (B)	Fixed-term employment contract	Specialist occupations (planning, sales, R&D, etc.)	Yearly remuneration package; performance wages; no wage increment	Sharing of company performance results	Evaluation of performance
Flexible workforce (C)	Fixed-term employment contract	Clerical, technical, sales positions	Hourly wages; Job-based wages; no wage increment	Specified rate	Switch to higher-ranking position

The impact of this portfolio has been debated. In particular, the second group of specialists has not become as substantial as originally suggested. However, Nippon Keidanren has provided continued support and the proposal has played an important role acknowledging the rise in non-regular employment, both its peripheral and knowledge-intensive forms, and re-conceptualising Japanese employment practices.

Recent developments at Toyota

Toyota is the archetypal example of a Japanese global corporation. Its emergence as a leader in the automotive industry has been closely associated with the efficiency and quality delivered by its management practices. Toyota's lean production model has been widely adopted throughout the world. >>>

More recently, however, Toyota has encountered some problems, most notably a series of quality issues that led to major recalls of cars in both Europe and North America. So how has the company responded?

The consensus amongst Japanese experts is that the root cause of the recent quality problems lies with the speed of the corporation's growth and internationalisation. There have also been some specific problems with new product development and testing, both at the carmaker and its suppliers. Akio Toyoda, Toyota's president, publicly acknowledged that the pace at which Toyota has grown might have been too rapid for it to retain the degree of control and quality that has been the company's hallmark.

Rapid growth and internationalisation have strained the traditional employment relations and management practices at Toyota. Dealing with both internationalisation and the global economic crisis has led to increased reliance on temporary employees. At the same time, Toyota undertook a process of delayering to reduce the number of hierarchical positions.

It was not long before the company identified some negative consequences. A director of Toyota's HR department noted, "Toyota's traditional culture in which employees coach each other has decreased" (Nihon Keizai Shinbun, 25 December 2007). The changes undermined the basis and capabilities upon which continuous improvement was founded.

As a result, Toyota and its supplier companies have pulled back from experiments with more individualised HR systems and concentrated on sustaining the established mutual commitment between core employees and employer. Specifically, the company restored the positions of leader and associate leader in its career track and has also redoubled its efforts to introduce new recruits to the corporate culture and history of Toyota in an attempt to secure the commitment to continuous improvement, quality, and efficiency, that have been central to its success.

Indeed, there has been something of a return towards the emphasis on the three pillars of the Japanese employment system in the last few years, both by Toyota and other companies in Japan's motor industry, and more widely across its main industries.

Japanese management practices and innovation: the case of pharmaceuticals

As mentioned earlier, Japan's distinctive employment practices have also shaped the type of technological innovation that Japanese companies pursue. They have specialised in low-risk, incremental innovations and continuous improvement in manufacturing processes. These strengths were borne out of the close coordination of intra-firm departments and the company-specific skills among employees nurtured through job rotation across different departments.

Unfortunately, Japanese organisations have not been adept at responding quickly or flexibly to the rapid, discontinuous, and unpredictable advances in science and technology found in knowledge intensive industries.

This is illustrated by the global pharmaceutical industry where Japan has remained a minor player. The leading Japanese pharmaceutical firm, Takeda, has hovered around 16th in global rankings (by sales) for the past three decades. Japan's pharmaceutical firms have invested less in R&D, and have recorded lower sales compared to leading global firms. The country has remained a net importer of pharmaceuticals and few Japanese drugs are found outside the country. The global pharmaceutical industry is led by firms from the United States, the United Kingdom, and Switzerland, rather than those from Japan.

The distinct features of Japanese management have contributed to Japan's weakness in pharmaceuticals. The system of lifetime employment and keiretsu relationships, for example, made Japanese scientists more risk averse in their research pursuits, as well as reducing opportunities for inter-firm and university-industry collaboration.

Company researchers in Japan were less exposed to fresh ideas, not only from other companies, but also from academic scientists or foreign researchers. Japanese employment practices of hiring fresh college graduates also meant that a lower proportion of Japanese PhD graduates in science were employed in industry.

For many years Japan favoured applied research at the expense of basic research. This research environment had a negative impact on the industry's capacity for breakthrough innovations. The prestige of working at Japan's leading companies with established employment practices encouraged ambitious, talented minds to opt for stable, safe careers rather than pursue entrepreneurship or test new business ideas in the biotechnology sector. Moreover, until the late 1990s, most Japanese academics were not permitted to engage in private sector employment, which prevented the exchange of knowledge between academia and industry.

However, Japanese management practices have evolved over the past two decades. In a more fluid labour market, academics can now establish companies and move between academia and industry, which helps translate the fruits of academic research into innovative pharmaceutical products through collaboration in drug development. An increasing number of firms also welcome mid-career hires and have incorporated meritocratic pay, enhancing incentives to pursue more rigorous research.

New measures to promote entrepreneurship have helped to develop a growing biotechnology sector, which has increased from 102 firms in 1994 to over 550 firms by 2009. The improved incentive structure and cross-pollination of ideas across different organisations have improved Japan's environment for discovering and developing new medicines. Additionally, following deregulation and the harmonisation of Japanese pharmaceutical regulation with those in the United States and Europe, Japanese firms became much more integrated with global markets. In the new economy, the leading Japanese firms have also enhanced their R&D capacities by selectively expanding in more favourable institutional contexts beyond their home country.

updating the 'japanese model'

From long term to short term

The changes in employment practices can be considered part of a wider development; moving from long-term relationships towards a greater marketisation and internationalisation of the Japanese economy set against the backdrop of the prevailing conditions in the global economy.

The introduction of performance-related pay means that the basis for remuneration has shifted away from the long-term development of skills towards short-term results. The rise in non-regular employment suggests a more short-term relation between firms and large groups of employees. This corresponds to Nikkeiren's employment portfolio, which is indicative of support for a more-market based employment system by Japanese employers. Further support came from the Koizumi government in the 1990s that actively promoted the relaxation of labour regulation.

Moreover, these developments are real and significant. Performance-related pay can be considered a new standard in the management of regular workers among Japanese firms and has introduced important changes to their evaluation and remuneration. Seniority often remains as a criterion for evaluation, but it no longer defines the Japanese wage system.

The rise in non-regular employment suggests a more short-term relation between firms and large groups of employees.



The rise in non-regular employment has been equally significant as it brings major changes to both firms and large groups of workers. Non-regular employment was previously acknowledged as a buffer, to protect the lifetime employment of regular employees, but it now needs to be included as a core aspect of Japanese employment practices because of its increased importance and the cost advantages it offers.

These developments have resulted in a new diversity in employment practices, with important differences across industries and firms. As mentioned, most firms have introduced performance-related pay, but they have followed different strategies to do so. The rise in non-regular employment has given rise to even greater diversity. The ambition to reduce labour costs is widely shared, but regular employment remains dominant in industries like automobiles, where firms' dependence on the specific organisation of work appears to justify and require a long-term investment in the management and skill-development of regular employment.

Change with continuity

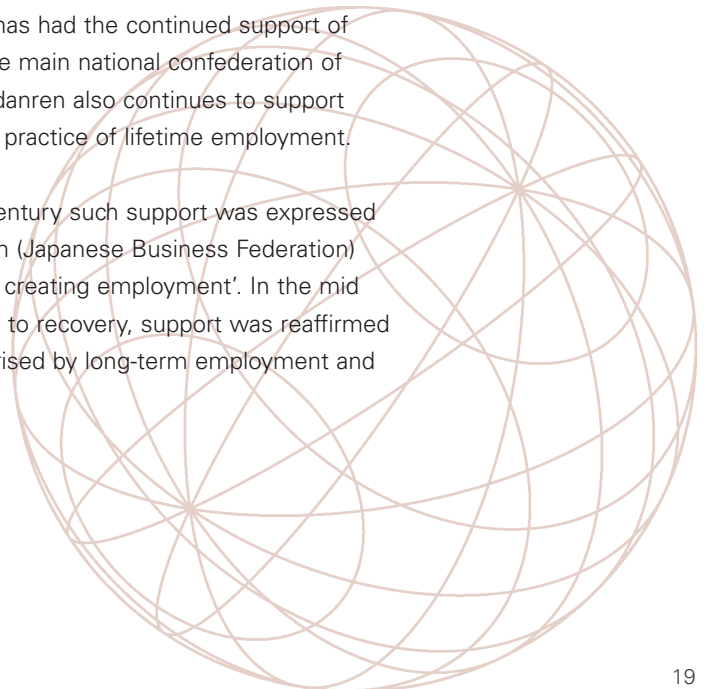
Alongside change there is also important continuity. Most obvious is the continued support for lifetime employment. A study by the Japan Institute for Labour Policy and Training in 2005 found that nearly 90 per cent of companies indicated that they would maintain lifetime employment in its current or partially adjusted form. Moreover, lifetime employment was also favoured by 33.7 per cent and somewhat favoured by 44.3 per cent of employees.

The introduction of performance-related pay can be considered a strategy to reduce labour costs when it is difficult to dismiss workers. However, continued support for lifetime employment has also contributed to the goodwill necessary for change. Moreover, it has enabled the introduction of performance-related pay while maintaining the character of personnel management. Long-term employment remains the sole path to a managerial career and employees remain motivated to compete for promotions.

Lifetime employment is also an important factor behind the cost advantages that non-regular employment offers. It means that firms mostly hire recent graduates. As a consequence, it is very difficult to find regular employment beyond the early years of a career or when one has left the labour market for a number of years. Large numbers of workers therefore have little choice but to accept non-regular employment in spite of the relatively low pay and limited career chances it offers.

Employment security and lifetime employment has had the continued support of employers and unions, including from Rengo, the main national confederation of unions, and employers' organisation Nippon Keidanren also continues to support the importance of employment security and the practice of lifetime employment.

In the economically difficult early years of this century such support was expressed by the employers' organisation Nippon Keidanren (Japanese Business Federation) as a continued commitment to 'maintaining and creating employment'. In the mid 2000s, with confidence somewhat restored due to recovery, support was reaffirmed to 'the Japanese employment system, characterised by long-term employment and in-house labour-management relations'.



Finally, recent research by the Sanno Institute of Management has shown a rising share of new recruits who want lifetime employment. After it declined during the 1990s, the share increased again from around 50 per cent in 2002 to over 70 per cent in 2010. It remains to be seen whether this preference is realistic given the strong rise in non-regular employment but it provides another indication of continued support to the core institution among Japanese employment practices.

The benefits of lifetime employment

The beneficial consequences for Japan as a society of these commitments to maintaining employment can be seen when one reflects on the macroeconomic data on economic growth and unemployment.

The Japanese economy declined sharply from 1990 to 1993 and economic growth has remained low from then on; the average economic growth rate in 1977-1990 was 4.6 per cent, while that of 1991-2009 was only 0.8 per cent. This sharp deterioration in economic circumstances has led to an increase in unemployment. The unemployment rate started to gradually increase from 1990; the average in 1977-1990 was 2.4 per cent, while that of 1991-2009 was 4.0 per cent. However, this compares very favourably to the situation in the UK and is indicative of an alternative approach to handling the consequences of economic downturns.

Japan, then, still retains a distinctive management model. On the one hand it shares with many other countries developments such as the rise in performance-related pay and non-regular employment. However, while these suggest convergence with other countries, the character of these developments and the implications for workers remain specific to the Japanese situation.

Short-term cost considerations have become more important, but long-term employment remains dominant and has not only constrained but also shaped developments. Lifetime employment remains the core but has also become the basis for the introduction of new criteria for evaluation and a greater diversity in employment types. This is a striking development. Many predicted the collapse of the Japanese model, but practices central to the Japanese model have proved persistent, and at the same time flexible.

Flexibility comes at a cost though. This shows in the rising share of non-regular employment, for example, accompanied by relatively low pay and poor career opportunities. It can also become counter-productive because of the reduced training that these employees receive.

The contemporary relevance of the Japanese management system

The Japanese practices that became known as the 'Japanese model' were the product of a specific historical context. Long-term relationships with other firms, either as suppliers or through horizontal keiretsu, and the reliance on bank lending through a main bank, supported the strong growth in Japan during the post-war decades.

Management practices suited for manufacturing and incremental innovation enabled many firms in industries like automobiles and consumer electronics to outperform foreign competitors. The employment practices took advantage of high organisational growth and a rich supply of young workers to guarantee the stable provision of well-trained and motivated workers.

However, the burst of the economic bubble brought various structural developments into the open, until then hidden by economic success, and created a hard landing where it otherwise might have been possible to make more gradual adjustments. The common view was that Japanese practices no longer constituted a model to aspire to, but one that needed overhauling.

Since then Japanese management practices have adapted to the new economic situation with some important changes. Major examples include the introduction of performance-related pay and the rise in non-regular employment.

In arriving at a new updated Japanese model we need to acknowledge a number of points:

- The circumstances in the post-war decades were exceptional. With hindsight, earlier analyses of the Japanese success have probably overestimated the contribution of management practices, and not given sufficient weight to the historical circumstances;
- There is greater diversity than in the past. Marketisation and internationalisation have affected most aspects of the Japanese economy, but to different degrees and this has increased the diversity between firms and industries;
- The boundaries of the Japanese model must be drawn more widely. Consider the importance of non-regular employment, for example. It has always performed a role as a buffer to protect lifetime employment but this was largely ignored in earlier discussions of Japan's success. However, the rise in recent decades underlines the need for its inclusion in our analyses.

The updated model also recognises less attractive aspects of Japanese management practices like the relatively low wages and limited career opportunities of non-regular workers. Moreover, it acknowledges some fundamental challenges that confront Japanese management. An important example concerns the questions about the efficiency of the specific capabilities it develops. In spite of the changes, employees and their skills remain highly firm-specific. This was and continues to be successful for industries like automobiles but has raised doubts about the ability of firms to handle the rapid and discontinuous change in new knowledge-intensive industries. At the same time, the new diversity in practices may provide firms with greater strategic flexibility.

The common view was that Japanese practices no longer constituted a model to aspire to, but one that needed overhauling.

Japan has traditionally been a very introverted society and there is some evidence... that Japanese managers are becoming even less keen on international experience.

Another major challenge concerns the internationalisation of production. The challenges of managing supply chains over large distances, and of transferring Japanese practices and Japanese nationals overseas, has created major issues for Japan's leading corporations. Japan has traditionally been a very introverted society and there is some evidence, e.g. in terms of declining numbers of Japanese studying overseas, that Japanese managers are becoming even less keen on international experience. Given the scale of Japanese investments overseas, internationalising the managerial cadre and its experience, as well as improving its ability to learn from overseas experience, will be of crucial importance for the future success of Japan's major firms.

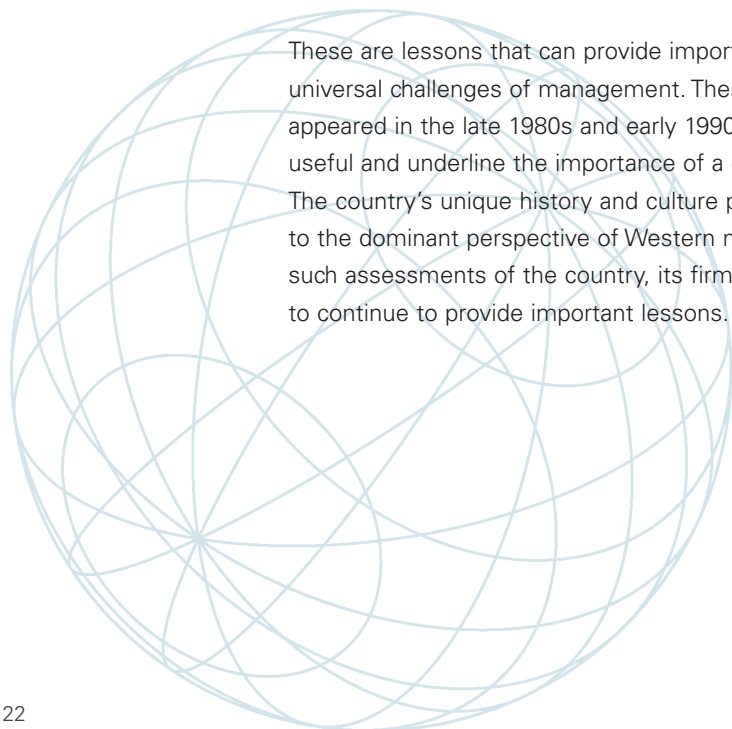
How much inspiration can Japan still offer to UK managers? The Japanese management model clearly no longer offers the same prospects of competitive success as 20 years ago. However, in hindsight, perhaps the lessons offered were never as straightforward as some suggested.

Recent evidence reported here is consistent with other AIM Research on Management Practices which has highlighted the local and specific nature of management practice creation, adoption and adaptation. Instead of easy answers of the one-size-fits-all variety, the new Japanese model offers more detailed insights into the diversity, tensions and challenges of management.

This, for example, concerns the challenges in performance management that confront all firms. The introduction of performance-related pay in the already sophisticated management systems of Japanese firms has resulted in a rich and multifaceted system for evaluation, remuneration and promotion.

Another example concerns the importance of aligning firm strategies with the wider environment. Japanese firms were able to successfully introduce performance-related pay because it fitted the wider set of employment practices based around lifetime employment.

These are lessons that can provide important inspiration to others as they concern universal challenges of management. These lessons are not as easy as they once appeared in the late 1980s and early 1990s. However, the insights may be just as useful and underline the importance of a contemporary focus on Japanese practices. The country's unique history and culture provide the context within which alternatives to the dominant perspective of Western management practices may develop and as such assessments of the country, its firms, and its management practices, are likely to continue to provide important lessons.



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