THE STRATEGIC MANAGEMENT OF KOREAN AND JAPANESE BIG BUSINESS GROUPS:

A Comparison Study between Korean General Trading Companies and Japanese *Sogo Shoshas*

by

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A thesis submitted to
The University of Birmingham
for the degree of
DOCTOR OF PHILOSOPHY

Department of Management
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August, 2009

ABSTRACT

This research is an in-depth study of Korean GTCs (General Trading Companies) and Japanese *Sogo Shoshas* (the Japanese version of General Trading Companies), which are unique big business conglomerates but not well-known in Western countries. It investigates and compares several of their features, such as their history, characteristics, functions, organisational structure, corporate culture, human resource management, their impact on national economic development, strategic management and decision-making process.

First, it examines a wide range of literature to show the functions of Korean GTCs and Japanese *Sogo Shoshas* as transaction intermediaries, information gatherers, project organisers, international marketers, financial providers, etc. With these varied functions, they have played significant roles not only from the macro aspect, but also the micro aspect. To rationalise their theoretical existence, they are approached from four perspectives: transaction cost economics, informational economics of scale, international marketing, and as financial intermediaries.

Second, many elements were examined to scan the general management system within the two groups. Compared to Western countries, both Korea and Japan traditionally have a collectivist culture with low individualism. However, there have been transformations in the culture in terms of employee values, attitude, behaviour and management style. These cultural changes have been reflected in human resource management practice. Traditional human resource management practices lost their effectiveness, as they proved to be unfit for the changing business environment.

Traditional features such as lifetime employment, seniority-based pay and recruitment patterns have been changing since the slower growth of these economies in the 1990s. Corporate governance and ownership structure were also examined. In Korea's case, control power has been centralised to group owners and their excessive power over ownership has caused problems, especially in the decision-making process. But ownership and management in Japan have traditionally been separated.

Third, as a main purpose of this research, a field survey was carried out to examine the strategic management of the two groups by analysing the relationships between the business environment, competitive strategy, organisational structure and performance. As in the previous literature, this research also found that the variables are not independent, but interdependent with the other variables. Environment influences a firm's competitive strategy and strategy affects its organisational structure. Then, performance is influenced by strategy and structure. For instance, a firm's employment of differentiation strategy is positively associated with environmental uncertainty and complexity. A differentiation strategy is positively correlated with organisational decentralisation. Consistent with the previous literature, a cost leadership strategy is statistically positive with organisational formalisation. A hybrid strategy and new market development are positively correlated, since the main purpose of this strategy is to offer high-quality products or services at lower prices than competitors do. The research also found that organisational decentralisation motivates and encourages employees' satisfaction and retention.

Fourth, the decision-making process within the two groups was compared. Top executives in Korean GTCs still play important roles in the decision-making process, whilst, team leaders and middle managers are positioned as main bodies in Japanese *Sogo Shoshas*. As primary factors influencing decision-making, ownership and corporate culture are the most important factors in Korean GTCs, whilst corporate culture is a primary component in Japan. Korean decision-makers tend to be individualistic, but Japanese decision-makers practice collectivism. There have been significant changes in decision-making both in Korean GTCs and Japan *Sogo Shoshas* since the 1990s.

Fifth, in totality, some differences in the general management system were found between the two groups. These may be caused by cultural differences, history, organisational size and/or the degree of business scope and diversification.

ACKNOWLEDGEMENTS

I wish to thank the many people who have encouraged, or assisted in, the preparation of my PhD. thesis. This work would not have been possible if it had not been for the help and support of many people. In this short preface I am not able to acknowledge everyone by name.

First and foremost, I would like to express my deep and sincere thanks to Professor Jim R. Slater, who has supervised my study for the past three years. His expertise in Strategic Management, as well as his assistance in many other phases, was especially beneficial in completing this dissertation. No amount of words can express my gratitude to him. My special thanks and gratitude are extended to Professor David Bailey. I am greatly indebted to him for his endless efforts and warm assistance in clarifying and refining this dissertation. The useful comments he has given me on Japan-related research were particularly helpful.

For my field survey, I am indebted to many people. I especially thank the contact people in Korean GTCs and Japanese *Sogo Shoshas*, in particular, Mr. Ki Sung, Cho, a manager of Lotte Group, and Mr. Keisuke Sasaki, a senior manager of Tomen Corporation. I also thank all the respondents who participated in my field survey. Most of them gave their total support and encouraged me.

I would also like to acknowledge my gratitude to my family. Without their devotion and sacrifice, I could never have finished all my academic journey in the U.K. I especially thank my mother, Gae Soon, Lee, and my brothers and sister, Hong Woo, Young Woo, and Gae Sun, who have given me their emotional and financial support over the years. Finally, I should not forget my only daughter, Eun Chae, who has given me emotional encouragement during my study. With all my heart, I dedicate this dissertation to my family.

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LIST OF ABBREVIATIONS

AOPC	American Office of the Property Custodian
APEC	Asia Pacific Economic Cooperation
BODs	Board of Directors
BOJ	Bank of Japan
BOK	Bank of Korea
BSC	Balanced Score Card
CEOs	Chief Executive Officers
DKB	Dai-Ichi Kangyo Bank
EBO	Employee Buy Out
ECGD	Export Credit Guarantee Department
EPB	Economic Planning Board
EPS	Earnings per Share
ESB	Economic Stabilisation Board
EU	European Union
EXIM Bank	Export and Import Bank
FDI	Foreign Direct Investment
FKI	Federation of Korea Industries
FOB	Free on Board
FY	Financial Year
GATT	General Agreement on Tariffs and Trade
GDP	Gross Domestic Product
GNP	Gross National Product
GTCs	General Trading Companies
HRM	Human Resource Management
IMF	International Monetary Funds
JETRO	Japan Trade Organisation
JFTC	Japan Foreign Trade Council
JIT	Just in Time
JPY	Japanese Yen
KITA	Korean International Trade Association
KOTRA	Korea Trade Investment Promotion Association
KRW	Korean Won
LC	Letter of Credit
M & A	Mergers and Acquisitions

MBA	Master of Business Administration
MBO	Management Buy Out
MCI	Ministry of Commerce and Industry
METI	Ministry of Economy Trade and Industry
MITI	Ministry of International Trade and Industry
MOCI	Ministry of Commerce and Industry
MOF	Ministry of Finance
MOFE	Ministry of Finance and Economy
OECD	Organisation for Economic Cooperation and Development
OJT	On-the-Job Training
R&D	Research and Development
ROA	Return on Asset
ROE	Return on Equity
ROI	Return on Investment
ROS	Return on Sales
SBU	Strategic Business Unit
SCAP	Supreme Command of the Allied Powers
SCM	Supply Chain Management
SMEs	Small and Medium-sized Enterprises
SPSS	Statistical Package for Social Sciences
SRS	Simple Random Sampling
SWOT	Strengths, Weaknesses, Opportunities and Threats
TT	Telegraphic Transfer
VW	Volkswagen
WTO	World Trade Organisation

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CHAPTER 1. INTRODUCTION

1.1. Research Background

Before the financial crisis of 1997, Korea was routinely hailed as a textbook example of successful economic development and its economy came to be widely regarded as a possible “role model” to be followed by other newly industrialising economies. (Rowley, Bae and Sohn, 2001). However, the financial crisis in 1997 shattered this image. It began with a surprise announcement by the government in late 1997 that the country was in financial crisis and required support from outside. The Korean government had to ask for a combined International Monetary Fund (IMF) rescue package at the end of 1997, which totalled US$55billion, the biggest IMF rescue package ever.

It is difficult to explain Korea’s financial crisis from any single perspective or cause. Instead, the crisis should be seen as the result of a combination of factors. The origin of Korea’s financial crisis can be traced to three sectors; government, financial institutions and the *Chaebol*[1], which means the big business conglomerates owned and managed by family members. Among these three causes, the *Chaebol*, in particular, are

[1] The Korean term, *Chaebol,* can be defined as “a big business group consisting of large companies which are owned and managed by family members or relatives in many diversified business areas.” *Chaebol* refers to Korea’s business conglomerates. The Korean word means business group and is often used as “Big Business” is used in English. *Chaebol* refers to the several dozen large, family-controlled Korean corporate groups, assisted by government financing, which have played a major role in the Korean economy since the 1960s. Some have become well-known international brand names, such as Samsung, Hyundai and LG. Hyundai has even played a role in the slight thawing of relations between North and South Korea since 2000. As of April, 2008, the top 10 largest *Chaebols* in Korea by total revenue were Samsung (US$114.28 billion), KEPCO (US$36.07 billion), Hyundai Motor Company (US$60.00 billion), SK (US$49.13 billion), LG (US$51.70 billion), Korea National Housing Corporation (US$4.72 billion), Lotte (US$22.64 billion), Korea Highway Corporation (US$2.39 billion), POSCO (US$22.95 billion) and Korea Land Corporation (US$4.94 billion) (Fair Trade Commission, 2008).

not free from responsibility for the crisis. The *Chaebol*, in many instances, simply made poor decisions in their management. According to Shim and Steers (2001), short-sighted executive decisions based on limited financial and strategic analyses led companies to the brink of bankruptcy with mounting debts and excess production capacity.

Most Korean *Chaebols* have General Trading Companies (GTCs)[2]. These are positioned at the heart of the *Chaebol*; Korean GTCs played an important role in the process of the *Chaebols'* development and they were functioned as financial resources rather than their primary functions of trading, distribution, risk hedging and providing information services. Albaum, Strandskov and Duerr (2002) argued that GTCs are engaged in a far wider range of commercial activities than simply trade and distribution. They play a central role in such diverse financial areas as insurance, capital investment in joint ventures, extending credit and providing loan guarantees to customers. In fact, it is the range of financial services offered that is a major factor distinguishing GTCs from others. However, Korean GTCs amassed huge amounts of capital, often borrowed heavily in international capital markets and supplied them to headquarters for internal use.[3] Thus, the GTCs were heavily criticised for being no more than sources of finance for the *Chaebols* and they were at the centre of Korea's financial crisis.

[2] The GTCs have originated from the Japanese concept of general trading companies, *Sogo Shoshas*. These are unique organisations which perform not only trading activities but also a variety of functions such as financial services, project organising activities, information-gathering activities, distribution function and business coordination function. Seven GTCs in Korea are the Samsung Corporation, Daewoo International Corporation, Hyundai Corporation, SK Networks Co., Ltd., LG International Corporation, Hyosung Corporation and Ssangyong Corporation (The Handbook of Korean GTCs, 2005).

[3] The GTCs' primary financial services are extending credit, making loans, providing loan guarantees and developing venture capital to both buyers and sellers. In many cases, however, Korean GTCs diverted the funds internally for the purpose of letting the *chaebols* operate (The Handbook of Korean GTCs, 2005).

The GTCs system in Korea was established in 1975, based on a Japanese general trading company model. The model of the *Sogo Shoshas*[4] was used as a means of overcoming Korean export stagnation and achieving economic internationalisation after the oil crisis in 1973. Under the motto "from a noodle to a satellite", Korean GTCs progressed rapidly in scale and outcomes as they dealt with various products. Shin (1984) argued that Korean GTCs have played an unusually important role in export, import, domestic trade and third country trade. In the 1970s in particular and even in the face of a worldwide recession and strict import controls in industrialised countries, the GTCs have recorded an astonishing export growth rate average of over 40% a year. In 1982, the GTCs' total exports were US$15billion and their share accounts for more than 48% of Korea's total exports. Engaging primarily in exporting, importing, financing and operating in or doing business with worldwide networks, Korean GTCs were the growth engines of Korean business in their move toward multinationalisation.

Korean GTCs have led Korean economic and export growth since the 1970s and maintained a positive reputation before financial crisis in 1997. However, business volumes conducted by the GTCs were starting to gradually decrease from the early 1990s due to the changes in the internal and external business environment, such as organisational restructuring, high competition among the existing GTCs, abolition of assistance by government and the secession of manufacturers. For instance, in order to be internationally competitive, most Korean manufacturers pursued direct export or

[4] A Japanese term, the *Sogo Shoshas*, refers to the Japanese version of the GTCs. Many scholars and business people prefer to use "*Sogo Shoshas*" instead of the GTCs. In this thesis, the term "GTC" or "GTCs" will be used for the Korean General Trading Companies (i.e. the Korean GTCs) and the term "*Sogo Shosha*" or "*Sogo Shoshas*" will be used for the Japanese General Trading Companies (i.e. Japanese *Sogo Shoshas*). The major Japanese *Sogo Shoshas* are the Mitsui Corporation, Mitsubishi Corporation, Marubeni Corporation, Sumitomo Corporation, Itochu Corporation, Toyota Tsusho Corporation and Sojitz Corporation.

import by themselves rather than through the GTCs, since they had easy access to global markets and easy acquisition of information. As a consequence of these factors, the total export volumes conducted by seven major GTCs as of January 1997 before the financial crisis decreased by 19.1% compared to the previous year. In addition, most Korean GTCs were affiliated companies of the *Chaebols* and they were heavily dependent upon their parent company as export and import agents on its behalf. Furthermore, the financial crisis significantly affected Korea's industries including the GTCs industry. The collapse of major *Chaebols* and organisational restructuring on the advice of the IMF threatened the GTCs' future businesses.

In contrast, the history of the Japanese *Sogo Shoshas* dates back to the *Meiji* Restoration in the mid-19th century. Before the *Meiji* period, Japan had been closed to the outside world and had no merchants with experience in international trade. Until the *Meiji* period, Japanese goods were traded through foreign merchants. For example, by the second half of the 19th century, European traders dominated Japan's import market. For the purpose of protecting the national economy from Western invasion, the *Meiji* government recognised the need for Japan to have its own trading organisation. The *Meiji* government encouraged traditional *Zaibatsu*[5] families, such as Mitsui and

[5] A Japanese term, *Zaibatsu* (literally "financial cliques") means the diversified family enterprises which rose to prominence in the *Meiji* Era. They are the great family-controlled banking and industrial combines of modern Japan. The leading *Zaibatsu* (called "*Keiretsu*" after World War II) are Mitsui, Mitsubishi, Dai Ichi Kangyo, Sumitomo, Sanwa and Fuyo. They gained a position in the Japanese economy which has no exact parallel elsewhere. Most *Zaibatsus* developed after the *Meiji* restoration (1868), when, by subsidies and a favourable tax policy, the new government granted them a privileged position in the economic development of Japan. Later they helped finance strategic semiofficial enterprises in Japan and abroad, particularly in Taiwan and Korea. In the early 1930s the military clique tried to break the economic power of the *Zaibatsu*, but failed. In 1937 the four leading *Zaibatsus* controlled directly one-third of all bank deposits, one-third of all foreign trade, one-half of Japan's shipbuilding and maritime shipping and most of the heavy industries. They maintained close relations with the major political parties. After Japan's surrender (1945) in World War II, the break-up of the *Zaibatsu* was announced as a major aim of the Allied occupation, but in the 1950s and 1960s groups based on the old *Zaibatsu* re-emerged as the *Keiretsu*. The decision on the part of these groups in the post-World War II era to pool their resources greatly influenced Japan's subsequent rise as a global

Sumitomo, to participate in the trading business. For example, by 1918, the *Zaibatsu* had captured 80% of Japan's total import volume with the support of the government. These *Zaibatsu* organised vertical and horizontal combinations of companies, in banking, marketing and manufacturing, among others and dominated Japanese industry and the finance sector prior to World War II. After World War II, Japanese *Zaibatsus* were required to resolve ownership in their holding companies by anti-monopoly legislation. This resulted in the appearance of great number of specialised trading companies such as Marubeni, Tomen, Nissho-Iwai and Nichimen. The dissolution of the *Zaibatsu* was halted in 1949 and the Korean War in 1959 gave the *Zaibatsu* great opportunities for re-grouping and re-growth. Naturally specialised trading companies and *Zaibatsu* type trading companies were transformed into the contemporary *Sogo Shosha*.

As engines for promoting industrialisation and economic development in the modern age and positioned at the heart of the *Keiretsu*[6] together with the banks, the Japanese *Sogo Shoshas* have played an unusually important role in facilitating

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business power. However, despite the forced dissolution of the *Zaibatsu* after World War II, three of the famous names – Mitsui, Mitsubishi and Sumitomo – have survived and are now known as *Keiretsu*. (Hidemasa, 1992; Kang, 1996).

[6] A *Keiretsu* is a Japanese conglomerate like a *Chaebol* in Korea. The most common Japanese meaning is something close to the English verbs "link", "affiliate with" or "connect to." The prototypical *Keiretsu* are those which appeared in Japan during the "economic miracle" following World War II. Before Japan's surrender in 1945, Japanese industry was controlled by large conglomerates called *Zaibatsu*. The Allies dismantled the *Zaibatsu* in the late 1940s, but the companies formed from the dismantling of the *Zaibatsu* re-interlinked through share purchases to form horizontally-integrated alliances across many industries. Where possible, *Keiretsu* companies would also supply one another, making the alliances to some extent vertically-integrated as well. Each of the major *Keiretsu* was centred on a GTC and a bank, which lent money to the *Keiretsu's* member companies and held equity positions in the companies as well. Each central bank had great control over the companies in the *Keiretsu* and acted as a monitoring entity as well as an emergency bail-out entity. One effect of this structure was to minimise the presence of hostile takeovers in Japan, because no entities could challenge the power of the banks. Although the divisions between them have blurred in recent years, there are six major postwar *Keiretsus*: Mitsui, Mitsubishi, Sumitomo, Fuyo, Dai-Ichi Kangyo and Sanwa (Miyashita and Russell, 1994)

international trade between Japan and the rest of the world. They exist at the centre of Japan's global economic effort and serve as intermediaries for half of their country's exports and two-thirds of their imports; S*ogo Shoshas* handle more than half of Japan's total foreign trade and much of their domestic transactions. In 1984, for example, the largest *Sogo Shosha*, Mitsubishi Corporation, had total sales exceeding US$69billion, making it the biggest company in Japan and third largest in the entire world. According to Shao and Herbig (1993)[7], the *Sogo Shoshas* have three basic functions; seeking export opportunities, securing necessary imported materials and acquiring technology for industrial development. Traditionally and still today, they are concentrated in high volume, low margin commodities. They handle importing, exporting and trading for over 20,000 items – including metals, machinery, energy and chemicals, textiles, foodstuffs and general merchandise. They are also actively involved in raw materials extraction, creation and discovery through multiple stages of production, fabrication and distribution, downstream to the end user. Besides the above functions, the *Sogo Shoshas* serve a multitude of functions, such as financial services, information services, organisation and coordination services, risk reduction services and communication services.

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[7] They also examined the SWOT (strengths, weaknesses, opportunities and threats) associated with the *Sogo Shoshas*. i) Strengths: One of the apparent strengths of the *Sogo Shoshas* is the chance for employees to travel overseas, since the trading companies' role is to spot business trends and opportunities throughout the world. Another strength is that the groups encourage specialists rather than generalists and move employees into new jobs every five to seven years rather than two or three years in most Japanese companies do. Having strong local managers who have special knowledge of the local market is also one of the strengths of the *Sogo Shoshas*. ii) Weaknesses: Japanese *Sogo Shoshas* are highly vulnerable since their expertise is in commodities, not technically-oriented products. Some manufacturers undertake many of their own domestic and international marketing activities (Sony, Honda, etc.). As Japanese manufacturers gain experience in exporting, they need to rely less on the expertise of trading companies. iii) Opportunities: Besides their basic roles, a new role is coming to the *Sogo Shoshas*, that of manager and coordinator of projects, plant exports, financial accounts, information and other services. iv) Threats: The *Sogo Shoshas* are involved in ill-conceived or poorly implemented new businesses. For example, they have diversified into real estate and housing in Tokyo where real estate is not healthy.

Despite *Sogo Shoshas'* continuous development, their future is not likely improve, due to several factors. Shao and Herbig (1993) identified the factors as follows. First, Non-*keiretsu* companies, such as Honda, Sony and Toyota are setting up their own direct exporting network rather than exporting through the *Sogo Shoshas*. Thus, the *Sogo Shoshas* handle less of Japan's exports. Second, the growth potential inside Japan is limited, due to the large share of the *Sogo Shoshas*. Third, the rise of other countries' GTCs will threat the *Sogo Shoshas* in the global market. For instance, Korean GTCs have become substantial in scope and size. Some trading companies in Europe, Hong Kong, Brazil and Thailand operate efficiently. Last, the *Sogo Shoshas* will face greater competition in international trade from manufacturers, smaller specialised trading companies and foreign companies.

At the same time, the birth of World Trade Organisation (WTO) in 1995 made Korean GTCs and Japanese *Sogo Shoshas* confront new business environments. The WTO deals predominantly with the actions of governments, establishing discipline over trade policy instruments such as tariffs, quotas, subsidies or state trading (Hoekman and Kostecki, 2001). The launching of the WTO means that the world trade system enters into infinite competition by reducing tariffs for imported materials or eliminating tariff barriers and ultimately establishing a tariff-free trade market. Moreover, China's entry into the WTO in 2001 made Korean GTCs and Japanese *Sogo Shoshas* encounter many challenges. In particular, Korea's exporters of textiles, electronics, home appliances, autos, plastics and machinery equipment, among others, stand to benefit handsomely from falling tariff and non-tariff barriers in China. By contrast, however, the Korean economy will probably run into a number of challenges, as the Western multinationals and the rapidly growing Chinese manufacturers are expected to further intensify competition for a bigger share of the liberalised Chinese market. Further, according to the Korean Ministry of Foreign Affairs and Trade (2001), Korean and Japanese firms may suffer setbacks in profitability amid fiercer competition from the rising ranks of Chinese manufacturers and expansion-minded Western companies in China.

As reviewed above, the rapidly changing external and internal business environments have threatened the future business of Korean GTCs and Japanese *Sogo Shoshas* and their future does not look bright. Accordingly, both of them are in need of strategic management to lead a revolution which will best position them to capitalise on the opportunities and threats of the global markets. Despite the growing significance of Korean GTCs and Japanese *Sogo Shoshas* in the national economic system and in world commerce, there has been no major study of them in English. This study is an attempt to introduce Korean GTCs and Japanese *Sogo Shoshas* for the first time to the outside world. It seeks to carefully examine several aspects of Korean GTCs and Japanese *Sogo Shoshas,* such as their nature, functions, characteristics, history and development, management system (i.e. organisational structure, corporate culture, decision-making process, ownership, corporate governance and human resource management), financial performance, strategic management and decision-making process.

1.2. Research Objectives and Questions

This research studies Korean GTCs and Japanese *Sogo Shoshas* in some depth. It, therefore, examines several things about Korean GTCs and Japanese *Sogo Shoshas*, organisations which are unique and little-known in Western countries. The reasons that Korean GTCs and Japanese *Sogo Shoshas* were chosen as study targets are as follows: i) both have played important roles in Korean and Japanese national economic development; ii) they are completely unique organisations with varied functions and characteristics; and iii) the nature of the GTCs and *Sogo Shoshas* provides an adequate package for research, for example, their strategic management, export and import activities, financial activities, human resource management, global networks and business group linkages, etc.

The main purpose of this research is to examine the strategic management and decision-making process within the Korean GTCs and Japanese *Sogo Shoshas*. First, the objective of looking at their strategic management is to examine the structural relationship between the business environment, a firm's strategy, organisational structure and performance. In order to achieve the objective, the following sets of research questions is derived:

1) How much do environmental variables affect competitive strategies?

2) Is there any correlation between competitive strategies and organisational structure?

3) How much do competitive strategies influence a firm's performances?

4) How far is organisational structure associated with a firm's performances?

With respect to the decision-making process within the GTCs/*Sogo Shoshas*, the study investigates i) the main bodies in the process of decision-making, ii) the major factors affecting decision-makers and their sources of power and authority, iii) whether corporate cultural differences exist in the decision-making process between Korean GTCs and Japanese *Sogo Shoshas* and iv) the current trend of decision-making processes within their organisations. In order to meet these objectives, the following research questions are addressed:

1) Who are the main bodies in the decision-making process within the GTCs/*Sogo Shoshas*?
2) What are the major factors influencing decision-makers and what are their sources of power and authority in the decision-making process?
3) Are there corporate cultural differences in the decision-making process between Korean GTCs and Japanese *Sogo Shoshas*? and
4) Has there been any significant change recently in the decision-making process within their organisations?

Another objective of this study is to examine the nature of Korean GTCs and Japanese *Sogo Shoshas*, for example, their background and development from a historical perspective, functions and characteristics, management style (including organisational structure, corporate culture, decision-making process, ownership and corporate governance and human resource management), financial performance and their roles in the process of national economic development.

1.3. Methodology and Data Sources

Data for this research are derived from primary and secondary materials. The main parts of this thesis, Chapters 5 and 6, are based on primary data which include a questionnaire field survey of employees in seven of Korea’s GTCs and eight of Japan’s *Sogo Shoshas* and intensive interviews with team leaders and senior managers. With respect to the questionnaire field survey analysis, it adopted some quantitative statistical techniques such as Multiple Regression Analysis, Correlation Analysis, Frequency Analysis and Chi-square Test.

The introductory and background parts of this research, Chapters 2, 3 and 4 are mainly based on secondary materials. The secondary data sources include statistical and historical data, various books and articles released by the Korean and Japanese governments, statistical and historical data, reports and documents from Korean GTCs and Japanese *Sogo Shoshas*, private research institutes, such as Samsung Economic Research Institutes, Nomura Research Institutes and LG Research Institute, government-sponsored institutes, including the Bank of Korea (BOK), the Bank of Japan (BOJ), the Korean International Trade Association (KITA) and the Japanese Trade Organisation (JETRO). Data have also come from Korean and Japanese government ministries, such as the Ministry of Commerce and Industry (MOCI), the Ministry of International Trade and Industry (MITI), the Ministry of Finance (MOF) and other international organisations, including the Organisation of Economic Cooperation and Development (OECD) and the European Union (EU).

1.4. Organisation of the Thesis

This study is composed of seven chapters together with this introductory chapter. Following this introduction, Chapter 2 reviews the nature of Korean GTCs and Japanese *Sogo Shoshas*, including their characteristics and major functions. It also theoretically reviews the rationale for their existence from a number of different perspectives, including those of transaction cost economics, informational economies of scale, international marketing and distribution and finance.

The next two chapters, 3 and 4, are devoted to describing the Korean GTCs and Japanese *Sogo Shoshas and* their impact on national economic development. Since the ultimate purpose of this thesis is to examine the strategic management of Korean GTCs and Japanese *Sogo Shoshas*, the description of these two chapters provides a background for the subsequent chapters. Chapter 3 examines several things about Korean GTCs, such as their origin and development, details of the current GTCs, management style, financial performance and the relationship between *Chaebols*, GTCs and the national economy. In particular, it investigates the management system within Korean GTCs, such as organisational structure, corporate culture, decision-making processes, ownership, corporate governance, cross shareholding and human resource management. The final section discusses the relationship between the GTCs, *Chaebols* and Korea's economy. Chapter 4 examines overall aspects of the Japanese *Sogo Shoshas* using the same organisation as Chapter 3. It investigates the origin and development of Japanese *Sogo Shoshas*, details of the current *Sogo Shoshas*, management style, financial performance and the relationship between the *Keiretsu, Sogo Shoshas* and the Japanese economy.

(Figure 1.1. Organisation of the Thesis)

Chapter 1. Introduction

Background, Objectives, Methodology and the Organisation of the Thesis

Chapter 2. The Nature of the GTCs/*Sogo Shoshas*

Definitions, Characteristics, Functions, Rationales of their Existence

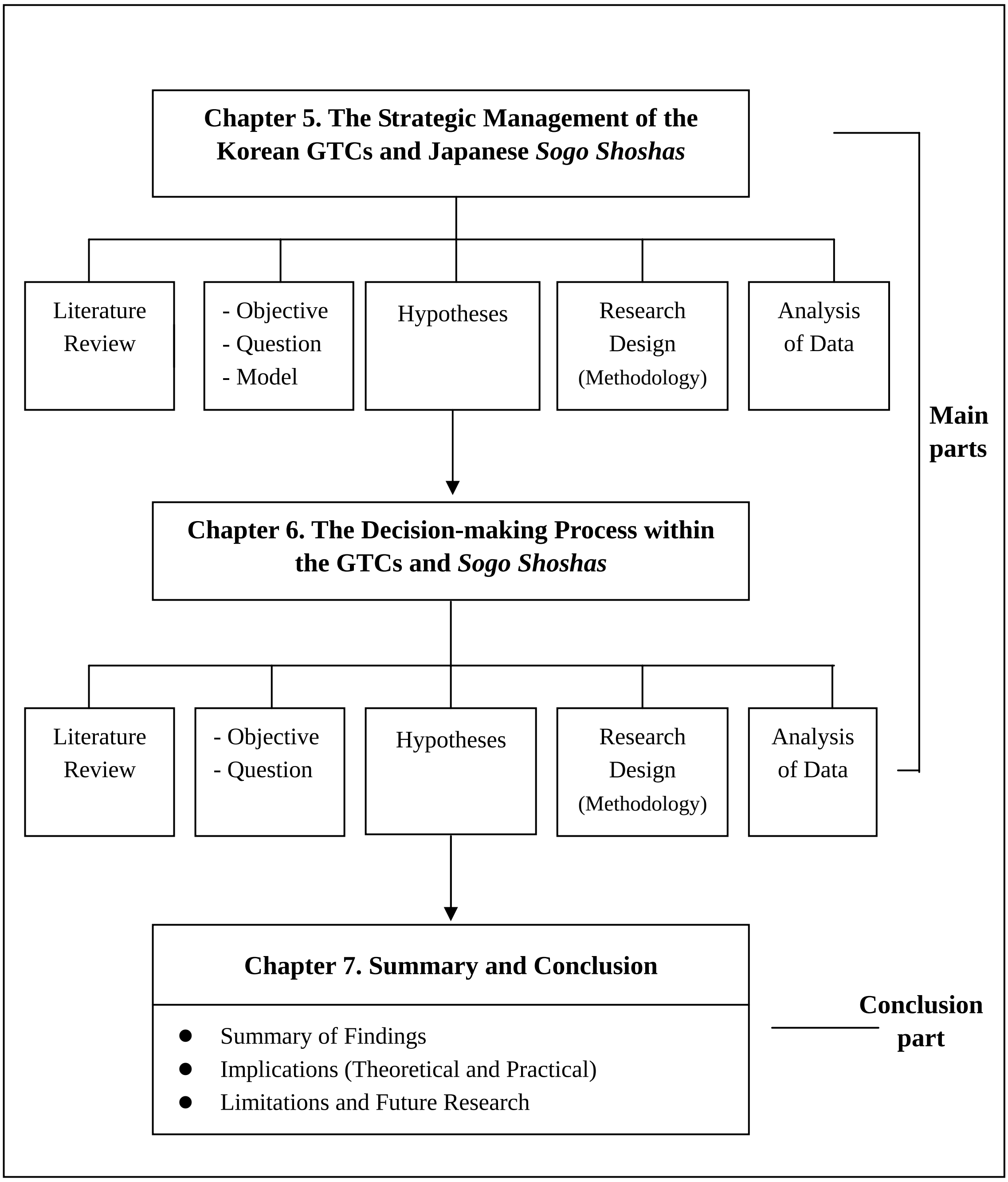
Chapter 3. The GTCs and the Korean Economy

- The History and Development of the Korean GTCs
- The Present GTCs in Korea
- The Management System in Korean GTCs (Organisational Structure, Corporate Culture, Ownership, Corporate Governance and HRM)
- The Financial Performance of the Korean GTCs
- The GTCs, *Chaebols* and the Korean Economy

Chapter 4. The *Sogo Shoshas* and the Japanese Economy

- The History and Development of the Japanese *Sogo Shoshas*
- The Present *Sogo Shoshas* in Japan
- The Management System within the Japanese *Sogo Shoshas* (Organisational Structure, Corporate Culture, Ownership, Corporate Governance and HRM)
- The Financial Performance of the Japanese *Sogo Shoshas*
- The *Zaibatsu*, *Keiretsu*, *Sogo Shoshas* and the Japanese Economy

Introductory and background parts



The strategic management of Korean GTCs and Japanese *Sogo Shoshas* is examined in Chapter 5, which is the main part of this thesis, together with Chapter 6. This chapter starts by with presenting various theories from the literature and previous studies of strategic management within organisations. Based on this literature survey, it presents a research model and establishes several hypotheses, to examine the relationship between the business environment and a firm's strategy, organisational structure and performance. First, it examines the relationship between the business environment (variables: uncertainty and complexity) and the firm's strategy (variables: differentiation, cost leadership and hybrid strategy). Second, it analyses the linkage between a firm's strategy and organisational structure (variables: centralisation and formalisation). Third, it investigates the relationship between strategy and performance (variables: financial and non-financial performance). Last, it examines the correlation between organisational structure and performance.

Chapter 6 investigates the decision-making process within Korean GTCs and Japanese *Sogo Shoshas* through a field survey. The chapter begins by presenting theories from the literature on decision-making within organisations. Existing theories are shown to be inadequate to explain the decision-making within Korean and Japanese firms. It is, therefore, suggested that the decision-making process within Korean and Japanese firms along with relevant cultural factors should be examined. Several things are considered, such as the main body in the decision-making process, major factors affecting decision-making and sources of power (i.e. power and politics, corporate culture, ownership and corporate governance), cultural differences in the decision-making process between Korean GTCs and Japanese *Sogo Shoshas and* recent changes in the decision-making process.

Finally, Chapter 7 summarises the major findings of the empirical research and considers its implications for the future strategic management and decision-making process within Korean GTCs and Japanese *Sogo Shoshas*. It also discusses the limitations of the thesis and offers recommendations for further research.

CHAPTER 2. THE NATURE OF THE GTCs/*SOGO SHOSHAS*

2.1. Introduction

This chapter examines the nature of the GTCs/*Sogo Shoshas*. First, it summarises some definitions of them in previous studies. Second, it reviews their characteristics and various functions. In the last section, the rationale of their existence is examined from the perspectives of transaction cost economics, informational economies of scale theory, international marketing and distribution, and finance.

2.2. The Nature of the GTCs/*Sogo Shoshas*

2.2.1. Definitions of the GTCs/*Sogo Shoshas*

General Trading Companies (GTCs) is the literal translation of the Japanese word *"Sogo Shosha."* When this term was first used, there was no exact definition of what the term meant. In Japan, many scholars prefer to use *"Sogo Shoshas"* instead of "GTCs." There are hundreds and thousands of ordinary trading companies in Korea and Japan today, but only a few hundred are engaged in trade with foreign countries. Among them there are only seven firms called GTCs in Korea and eight firms called *Sogo Shoshas* in Japan, as of 2006. According to Young (1979), the GTCs/*Sogo Shoshas*, unlike ordinary trading companies, can be defined as being "huge wholesale intermediaries that exist between large manufacturers and small producers. They supply large volumes of raw materials and distribute goods from large manufacturers to smaller distributors to numerous retailers". Yoshino and Lifson (1986, p.2) clearly explained the GTCs as follows:

> *"The Sogo Shosha (Japanese version of the GTC) is like no other type of company. It is not defined by the products it handles or even by the particular services it performs, for it offers a broad and changing array of goods and functions. Its business goals are equally elusive, for maximization of profits from each transaction is clearly not the major goal, at either the operating or philosophical level. There are really no other comparable firms, although important business and government leaders in the United States and elsewhere have become convinced that there should be. The six (major Sogo Shoshas)*[8] *affect the lives of most participants in the world economy. From the oil used to cook French fries at a local fast food restaurant to the subway cars running beneath our streets, products passing through their hands are all around us. Collectively they are accounting for four percent of world trade and influencing the jobs and fortunes of people all over the world"*

Yamamura (1985) stated that "the GTCs are economic organisations whose functions consist of minimising risks involved in transactions through their ability to distribute risks, reducing transaction costs via their ability to take advantage of economics of scale and making efficient use of capital." Miyashita and Russell (1994) argued that the *Sogo Shoshas* are uniquely Japanese institutions which are vital to the operations of the *Keiretsu.*

As reviewed in the above, there have been various definitions of the GTCs/*Sogo Shoshas* these are shown in Table 2.1.

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[8] Japan's major six *Sogo Shoshas* are Mitsubishi Shoji, Mitsui Bussan, Marubeni, Itochu (or C. Itoh), Sumitomo Shoji and Nissho Iwai.

(Table 2.1. Definitions of the GTCs/*Sogo Shoshas*)

Scholar (s)	Year	Definitions of the GTCs/*Sogo Shoshas*
Kunio, Y.	1982	The *Sogo Shoshas* are Japan's organisational innovation – an innovation necessitated by the problems the country faced in international trade. It is a unique Japanese organisation that employs hundreds and thousands of people, maintains a network in the major cities of the world and handles such diverse products as iron and steel, chemicals, textiles, foodstuffs and machinery.
Yamamura, K.	1985	The GTCs are economic organisations whose functions consist of minimising risks involved in transactions through their ability to distribute risks, reducing transaction costs via their ability to take advantage of economics of scale and making efficient use of capital
Lee, S. H.	1986	The GTCs combine international and domestic trading with finance, communication and resource development for a single primary purpose; to support their buying and selling functions that constitute the core of the GTCs business.
Shao, A.T. and Herbig, P.	1993	The GTCs are large traders and suppliers and sales intermediaries, not manufacturers or financial institutions, although they are giant financial intermediaries for purposes of credit extensions.
Miyashita, K. and Russell, D.	1994	The *Sogo Shoshas* are uniquely Japanese institutions which are vital to the operations of the *Keiretsu*.
Cho, D.S.	1997	The GTCs are large corporations that display a synergy effect by coordinating the work among products, geographical areas and financial functions.
Albaum, G., Strandskov J. and Duerr E.	2002	The GTCs are engaged in a far wider range of commercial and financial activities than simply trade and distribution. They also play a central role in such diverse areas as shipping, warehousing, finance, technology transfer, planning, resource development, construction and regional development, insurance, consulting, real estate and deal making in general.
Japan Foreign Trade Council (JFTC)	2008	They are involved in and contribute to each value added process in all phases of the flow of business, namely, from natural resources upstream to finished products downstream, from the purchase of materials to the sales of products.

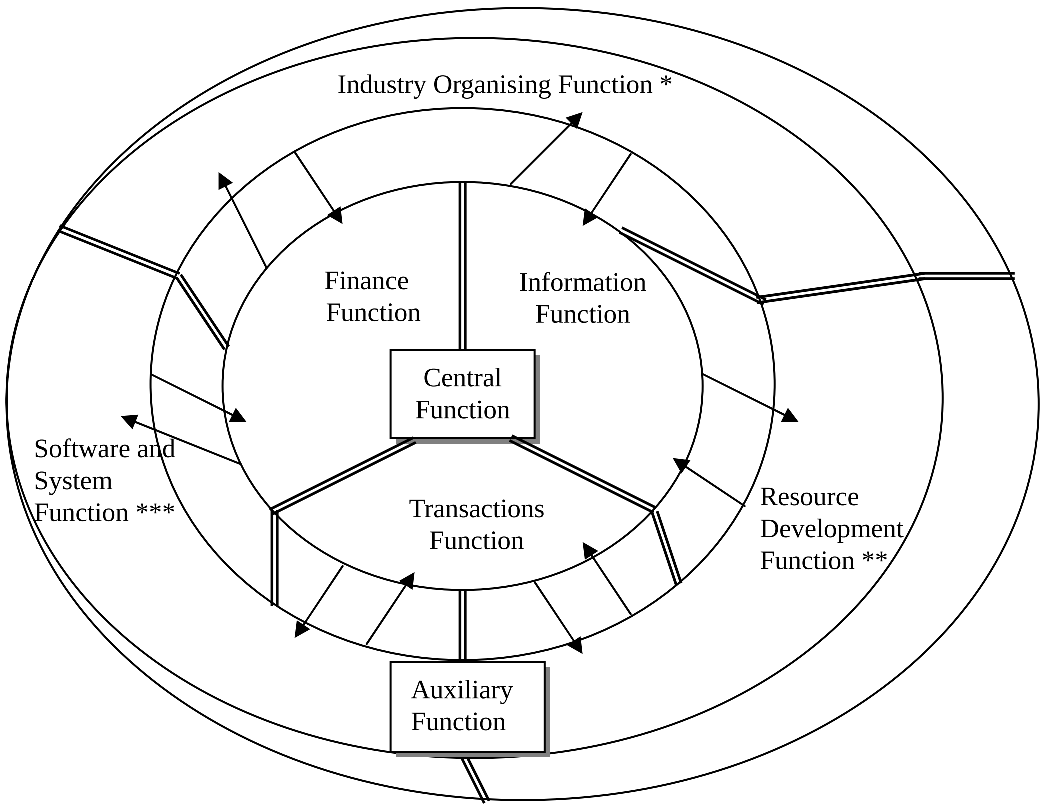
2.2.2. The Characteristics and Major Functions of the GTCs/*Sogo Shoshas*

The GTCs/*Sogo Shoshas* handle a wide range of products in most types of industry. Originally the *Sogo Shoshas* were known as trading companies, before the term evolved to mean general trading companies. They have now expanded and diversified their functions and business fields to include trading, but also investment, as well as services and industry development (JFTC, 2008). Thus, it is obviously difficult to explain the GTCs'/*Sogo Shoshas'* functions systematically, since they undertake extremely variegated activities. However, the various studies all agree on certain salient and common features shared by most of the GTCs/*Sogo Shoshas*. Shao and Herbig (1993) argued that they typically tend to have the following characteristics and serve a multitude of functions including: i) financial services, ii) information services, iii) risk reduction services, iv) organisation and co-ordination services, v) auxiliary services, vi) human resources, vii) financial resources, viii) global commercial networking and ix) communications systems. Besides the above functions, the GTCs also have intermediary or simple broker functions, middle-term credit offering and business project adjusting functions and information processing functions (Yamaji, 1991). A research institute of the *Sogo Shoshas* in Japan (1981) noted that the *Sogo Shoshas* have as central functions: a transaction function, finance function and information function and as auxiliary functions: industry organising functions, resource development functions and software and system functions. Putting all the functions of the GTCs/*Sogo Shoshas* together, they can be summarised as follows:

- Trading and Transactional Intermediation Function: This is the primary function of the GTCs/*Sogo Shoshas* in export, import and third-country (offshore) trade intermediation. They work as intermediaries between sellers and buyers and match them through diverse products, from instant noodles to satellites, in a long-term contractual relationship. They are involved in all phases of transactions from upstream to downstream in almost every kind of industry: machinery, plants, communications equipment, metals, minerals, energy resources, chemicals, textiles, foodstuffs and food products. Through global market-based activities, they take risks, expand markets and control the balance of demand and supply of the products that they handle. Space and time are the two dimensions in which they operate and they profit from the movements of goods and services. Although they perform many functions, trade intermediation is their major source of income (Kojima and Ozawa, 1984).

- Financial Services Function (the Quasi-Bankers): To be an organiser, a GTCs/*Sogo Shosha* must also be a financer. These organisations offer unique financial facilities distinct from those of banks or other financial institutions. They have a close relationship with commercial banks and extend credit, make loans, provide loan guarantees to both buyers and sellers and develop venture capital. They are also involved in acquiring funding, fund management, project finance, credit support, international settlement, currency exchange, insurance arrangements and other risk hedging. They can borrow from the most advantageous sources in international capital markets and channels. They also can act as a risk buffer by absorbing the financial risks for clients, but secure competence and hence profits in foreign exchange handling and investment fund operations. They also provide other financial facilities in relation to Mergers and Acquisitions (M & A), Management Buy-Outs (MBO) and Employee Buy-Outs (EBO). (Marubeni Corporation, 1978; The Handbook of Japanese *Sogo Shoshas*, 2005).

(Figure 2.1. A Diagram of the GTCs'/*Sogo Shoshas'* Functions)



*: New Industry Organising
**: Natural Resources Development
***: Logistics Management System and Business Management System

(Source: *Shin Jonghap Sangsaron* (The New Theory of the *Sogo Shoshas*) (1981), Research Institute of the *Sogo Shoshas*, Japan, p.26)

- Information and Intelligence Gathering Function: Speedy and highly reliable information is important not only to develop new business opportunities, but also to build a good relationship with customers domestically and abroad. For this purpose, all GTCs/*Sogo Shoshas* make efforts to gather firsthand and high quality information to equip the worldwide information network. Through their global networks, they collect and analyse a wide range of information from all over the world and utilise it for corporate strategy and management planning, as well as for promoting their daily business activities. This information includes worldwide political and economic conditions, industrial and corporate trends, advanced technology information, marketing data and changes in the legal and taxation environment, etc. Additionally, they furnish their customers and clients with useful and timely information to support their business and improve business performance. With the recent information and technology revolution, these capabilities have been greatly improved both quantitatively and qualitatively, resulting in increased value-added and speedier service (JFTC, 2008). According to Shin (1984), the information services of GTCs/*Sogo Shoshas* are not confined to economic and business information of immediate practical value; they extend to the global political, legal and social environment and to any trends that are likely to have an impact on the Korean and Japanese economies. They develop a globally extensive information-gathering infrastructure and each GTC/*Sogo Shosha* has spun a vast web of information gathering. They collect not only economic but also social and political information.

- Logistics Function: They take part in the creation and running of logistics information network systems. They also participate in the operation of such logistics facilities as warehouse and distribution centres. As a further goal, they are striving to offer a comprehensive and optimised logistics system which will meet the customer's needs at every stage of the cargo flow, including air, sea and land transportation, storage, processing, sorting and distribution (JFTC, 2008).

- Organisation and Coordination of Complex Project Function: They combine and organise three basic functions; trade intermediation, financial intermediation and information gathering. These enable them to act in a unique way as organisers and coordinators of entire production systems on an international scale (Dicken and Miyamachi, 1998). In promoting such large-scale projects as the construction of oil refineries, petrochemical plants, steel mills and natural resources development, they put together packages combining their various capabilities, such as information collection and analysis, planning for projects, scheme proposal, the selection of appropriate partners, formation of consortiums, arrangement of project funds, procurement of material and equipment, consignment of the construction, insurance arrangement and market promotion (JFTC, 2008; Marubeni Corporation, 1978).

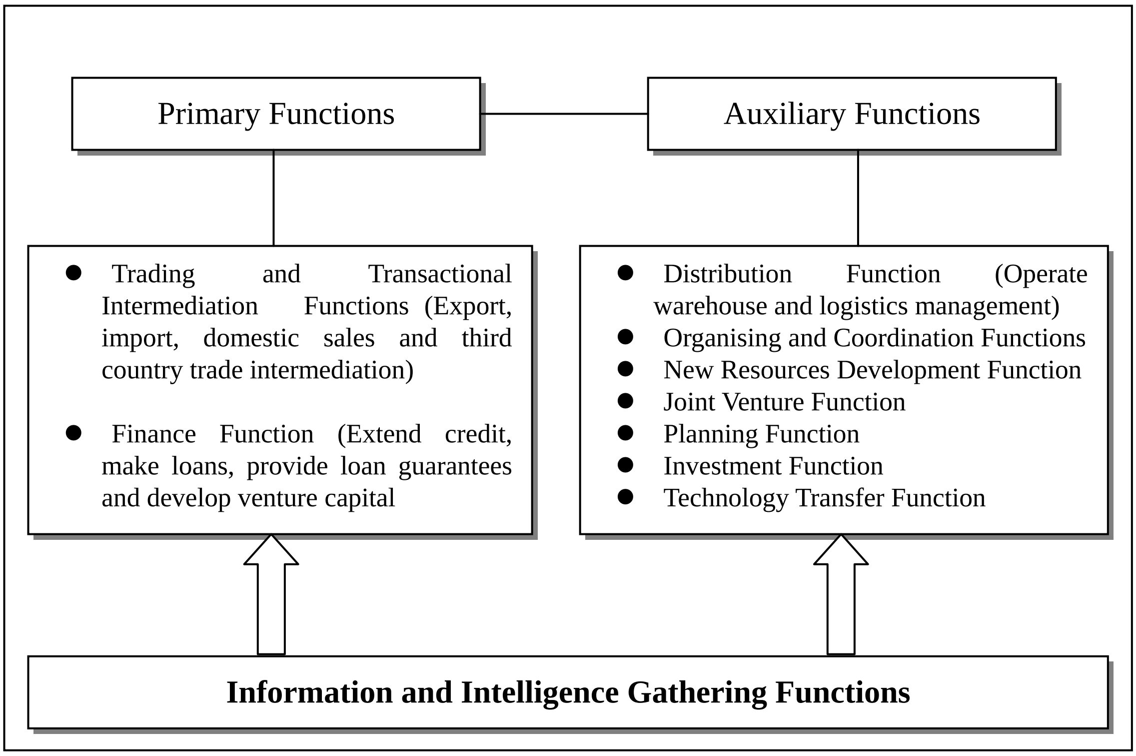
- Risk Management: In their daily business transactions, they utilise a wide range of know-how and management resources acquired over the years to keep various associated risks to a minimum. They are in particular capable in minimising risks in businesses requiring more refined risk management, such as large-scale projects in developing countries and venture businesses in new growth fields. Specifically, they make full use of their deep reservoir of know-how and expertise to minimise risks in such matters as the selection of appropriate partners, the formation of consortiums, the sharing of responsibility and the assurance of collateral; and in such other risk-hedging practices as currency exchange transactions, forward contracts and insurance coverage (JFTC, 2008).

- New Resources Development Function: They have been investing for a long time to develop foodstuffs, fuels, raw materials and natural resources; these are essential for economic growth (The Handbook of Japanese *Sogo Shoshas*, 2005).

- Joint Venture Function: They establish joint venture companies throughout the world in order to develop and stimulate regional economic growth (The Handbook of Japanese *Sogo Shoshas*, 2005).

In the meantime, information and intelligence have become increasingly important in modern business. Information processing capability can improve an organisation's strategic capability in several ways, since a large part of business activity is concerned with processing and transmitting information within and between organisations (Johnson, Scholes and Whittington, 2005). Among various functions of the GTCs/*Sogo Shoshas*, information and intelligence gathering functions are vital in the fast changing modern business environment. The author presents a new model of their major functions as follows:

(Figure 2.2. A New Model of the GTCs'/*Sogo Shoshas'* Major Functions)



(Designed by the author)

2.3. The Rationales of the GTCs'/*Sogo Shoshas'* Existence

2.3.1. Transaction Cost Economics Approach

One of the most plausible explanations of the GTCs/*Sogo Shoshas* from the microeconomic perspective is the transaction cost economics approach[9]. The GTCs/*Sogo Shoshas* can be regarded as mediators to promote transaction activities between sellers and buyers. As mediators, one of the most important factors in displaying their functional ability is the capacity to minimise transaction cost, such as may arise during transactions between sellers and buyers. The economist Mansfield (1988) explained the concept of middlemen (like the GTCs/*Sogo Shoshas*) with the transaction cost approach. He argued that middlemen play an important role in some real-life markets by providing a variety of services both to seller and buyer. In compensation for these services, the middlemen receive a share of the price paid for the good. The costs of these middlemen's services are often called transaction costs. Bradley (1995) also stressed that transaction cost analysis must be carried out, since one

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[9] A Typical Example of Transaction Services and Costs Structure (Chemical Product Export from Korea to the EU)

Items		Unit Price (US$/MT)	Remarks
The GTC "A's" Buying Price from Korean Manufacturers		1,200	FOB
Transaction Costs	Marine Insurance	5	
	Ocean Freight	60	US$1200/Container
	Inland Transportation	25	
	Storage and Warehousing	25	
	Preparing Trade Document	3	
Total of Transaction Costs		118	
Import Tax		108	FOB Price x 9%
The GTC "A's" Commission		20	
The GTC "A's" Selling Price to the EU Customers		1,446	

As seen in the above table, the GTC "A" buys a product at US$1,200 from a Korean manufacturer and sells it to his EU customers at US$1,446, which includes US$118 of transaction costs. However, one of the manufacturers located in the EU, which produces the same product, sells its product to the EU customer at US$1,242, which does not include import tax (import tax is exempted for the EU members) and some transaction costs such as marine insurance, ocean freight and storage charge. Thus, the GTC "A" needs to minimise transaction cost to overcome the price difference of US$204 (US$1,446 – US$1,242) and to have competitive advantage in the market.

purpose of business is to reduce business costs over time. The transaction services and costs during the business undertaken by the GTCs/*Sogo Shoshas* vary from providing relevant information to both buyers and sellers, arranging finance, covering marine insurance, transportation, distribution, storage and warehousing, to the preparation of trade documents and payment and the management of troubleshooting.

However, much neoclassical theory treats transactions as costless (Himmelweit, *et al*, 2001). According to neo-classicists, market exchange is determined by relative prices without regard to the costs of trading activity and there exists only production cost. In opposition to neoclassicism, some economists (new institutionalists) have become interested in the impact of the transaction costs on the pattern and level of economic activity. According to them, the ideal market which neo-classicists assumed is non-existent and any transaction activity generates costs for a number of reasons. Coase (1937), who is the pioneer of new institutionalism, argued that the transaction costs involved in transactions on markets are the price to be paid for using the price mechanism in a market system. In other words, when a person carries out economic activity by using the price mechanism, it generates various costs, called the transaction cost; these include the information costs, administrative costs and legal costs associated with finding transaction partners, negotiations and the final contract agreement. Thus, the cost of negotiating and concluding a separate contract for each exchange transaction takes place in a market and must be taken into account.

Hennart (1991) emphasised that if knowledge were perfect and individuals perfectly honest, market transaction costs would be zero. However, markets are never fully efficient and market transaction costs are positive. This is because humans have bounded rationality and a tendency towards opportunism. Bounded rationality refers to "the cognitive limits of economic agents in relation to the complexity of the problems with which they are confronted." Bounded rationality normally exists due to economic agents' limited capacity for computation and information (Pearce, 1983).

However, opportunism is defined as "self-interest seeking with guile in relation to choosing between alternative contractual relationships" (Williamson,1975). Williamson's (1979) study showed that transaction costs arise from the bounded rationality and opportunism of all interacting parties'. In other words, the external environment and the limited information restrict each party's rational behaviour, even though it tries to act reasonably. Moreover, each party distorts and provides wrong information in the pursuit of its own profits. Consequently, each party's bounded rationality and opportunism causes the transaction costs. With bounded rationality, the value of the goods and services exchanged will never be perfectly measured; hence prices will provide flawed signals and a price system will not maximise the social product (Hennart, 1991). Furthermore, Williamson stressed that the transaction costs can change according to the frequency of the transaction and investment (asset) characteristics of the transaction and these are major factors influencing the market governance structure.

(Table 2.2. Market Governance Structure)

		Investment (Asset) Characteristics of the Transaction		
		Non-specific	Mixed	Specific
Frequency of the Transaction	Infrequent	Market Governance (Classical Contracting)	Trilateral Governance	Trilateral Governance
	Recurrent	Market Governance (Classical Contracting)	Bilateral Governance	Unified Governance

(Source: Williamson, O. E. (1979), "Transaction Cost Economics: The Governance of Contractual Relations", *Journal of Law and Economics*, Vol. 22, pp.233~261)

The GTCs'/*Sogo Shoshas'* role of lowering transaction cost can be applied to this framework. Within this framework, when the investment characteristic of the transaction is non-specific, the governance structure is market governance, regardless of the transaction frequency. This is a characteristic of classic contracting. In this case, many sellers and buyers are normally involved in the transaction and therefore, the GTCs'/*Sogo Shoshas'* market arbitration function is unexpected, because there is no transaction distinctiveness. However, if the investment characteristic of the transaction is specific and the frequency of the transaction is infrequent, the transaction is made under the trilateral governance structure. In this case, the transaction distinctiveness exists and it generates huge costs to reach any complex agreement between the seller and the buyer. In this situation, the GTCs/*Sogo Shoshas* can minimise transaction costs by playing the part of arbitrator between the seller and the buyer.

In conclusion, it is obviously important for firms to reduce the transaction costs involved in their transactions in the market. As one of the strategic ways to overcome transaction costs, the use of the GTCs/*Sogo Shoshas* can be an alternative measure. They, as arbitrators between sellers and buyers, should be able to minimise transaction costs in all cases, in order to display their functional ability, and rationalise their existence.

2.3.2. Informational Economies of Scale Theory Approach

Another microeconomic rationality for the GTCs'/*Sogo Shoshas'* institutional existence is capitalising on informational economies of scale. Whether it needs to make a profit or not, every firm needs information to survive in the competitive business environment and information increasingly becomes one of the major factors to increase a firm's competitive advantage in this environment. The concept of informational economies of scale is the method by which firms enjoy increasing returns from information. Wilson (1974) argued that the value of information may be smaller against the unit cost, which is invested to gather such information, under a certain threshold level of operation scale. The implication here is that most small-and medium-sized enterprises (SMEs), which do not meet a certain threshold level of operation scale, may have difficulty in acquiring necessary information because such information in their position is imperfect and asymmetrical. In such circumstances, the GTCs/*Sogo Shoshas* can be alternative means of gathering information for SMEs.

The GTCs/*Sogo Shoshas* can be regarded as information intermediaries who are economic agents supporting the production, exchange and utilisation of information in order to increase the value of the information for their end-user or to reduce the costs of information acquisition. Rose (1999) stressed that the central function and service of information intermediaries is the matching of end-user specific information needs with the information available in any resource or information depot. The information intermediary reduces the end-user's search cost, including, for example, costs for communication, contact costs, costs for evaluation and in particular opportunity costs of time.

As manufacturing firms allocate their funds to research and development to develop new products or improve the quality of existing ones, it is essential for the GTCs/*Sogo Shoshas* to invest their funds for gathering information. Although it is obviously difficult to explain about the GTCs'/*Sogo Shoshas'* functions in simple terms, one of the major functions that they carry out concerns information. They explore not only the basic information related to the market, such as market trends, competitors' movements, market share and customers' tendency, but also widespread and unquantifiable information related to politics, economics, culture and history. For instance, Mitsubishi Corporation spent 0.041% over the total sales amount on communication expenses (only at headquarters) to gather information in 1990 and Sumitomo Corporation spent 0.023% (Yamaji, 1991). They normally gather information through regular intra-firm communication channels, their global network, publications, broadcasting, public meetings and so on. In addition to these, the GTCs/*Sogo Shoshas* also accumulate what may be called "human-embodied knowledge" (Kojima and Ozawa, 1984) in the form of individual employees' expertise. Hence, labour costs are the largest component of their total operating costs.

Lynch (1997) explained strategically the importance of information. From a strategic point of view, firms can reinforce competitive advantage with information resources and information technology. Specifically, information technology may influence competition in three ways: i) a change in industry structure, for example, the ticketing of airline tickets from any place with a computer network; ii) the creation of competitive advantage by lowering labour costs through automating manual tasks; and iii) the ability to reach new customers with the creation of the Internet and the development of new forms of telecommunications. Hopf (1983) stressed that information can be treated as an economic commodity. To be profitably sold in a market, information must possess some requirements common to all economic commodities; information goods have to directly or indirectly satisfy a human need, they should be limited and their production should compete for scarce resources with other information and economic agents (such as the GTCs/*Sogo Shoshas*) must have property rights on information goods, which must possess an exchange value.

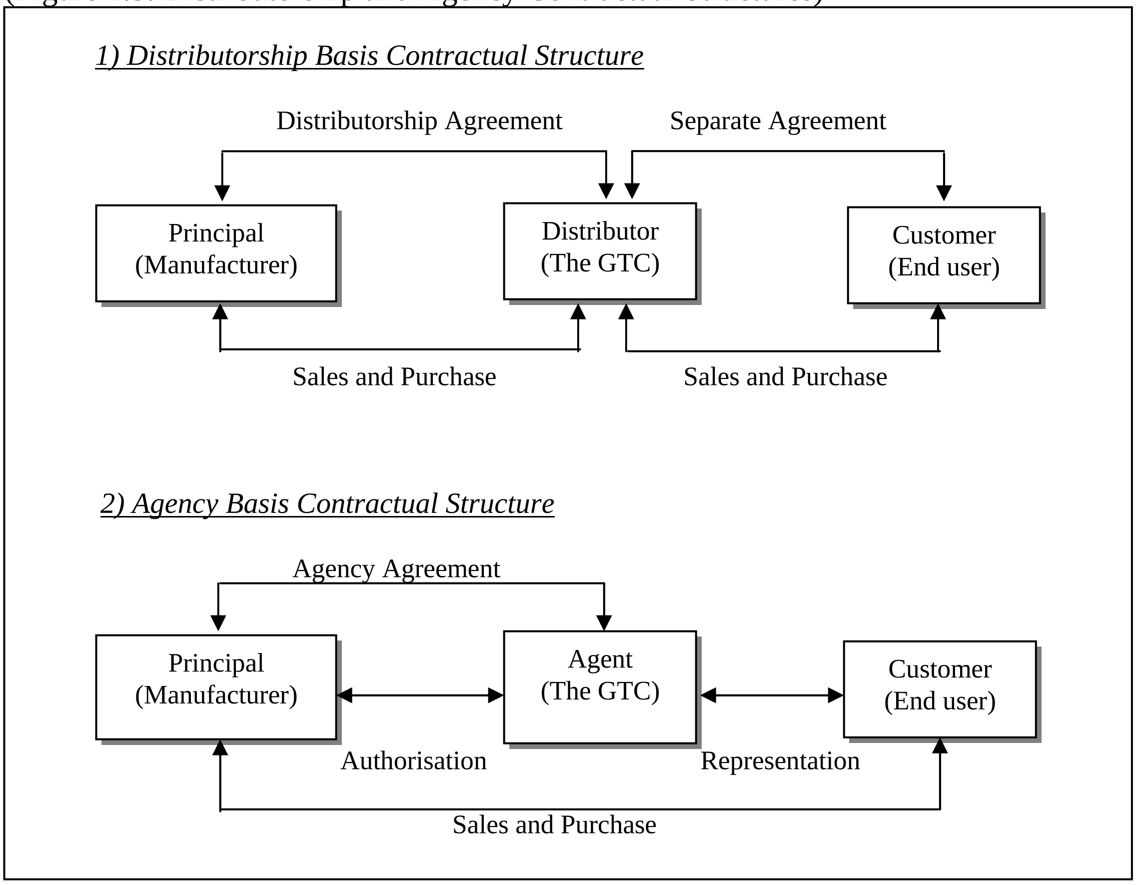
2.3.3. International Marketing and Distribution Perspective Approach

People all around the globe are more connected to each other than ever before. Goods and services produced in one part of the world are increasingly available in all parts of the world. This phenomenon has been entitled 'globalisation' (Katsioloudes and Hadjidakis, 2007). In such a business environment, it is very difficult for small manufacturers who wish to be international firms but do not have international marketing experience to introduce their products abroad and to establish business relationships with foreign customers. Albaum, *et al.*, (2002) defined international marketing as the marketing of goods, services and information across political boundaries. The process of international marketing is typically much more complex and interesting than domestic marketing. The international marketer must deal with a number of key factors in foreign environments which differ from those in domestic environments. Kotler and Armstrong (1997) argued that international markets often vary greatly in their economic development levels, cultures and customs and buying patterns. In this situation, the most appropriate alternative method of setting up a business for small manufacturers is to develop it through intermediaries, such as general trading companies, export trading companies, export brokers and sales representatives. Onkvisit and Shaw (1993) noted that even a good product may not be accepted by a market if it is not properly distributed through a competent channel. Although a manufacturer can sell directly to end users abroad, this type of sales channel is generally not suitable for most consumer goods. It is common for a product to go through several parties before reaching its final consumers.

Among many international business-related companies, the GTCs/*Sogo Shoshas* play a unique role in international business, unlike that of other ordinary trading companies. Young (1979) argued that the GTCs/*Sogo Shoshas* are wholesale intermediaries which exist between large manufacturers and small producers. They supply large volumes of raw materials and distribute goods from large manufacturers to smaller distributors to numerous retailers. Shao and Herbig (1993) stated that the GTCs/*Sogo Shoshas* have three basic functions; to seek export opportunities, secure necessary imported materials and acquire technology for industrial development. They handle importing, exporting and trade in various items – including metals, machinery, energy and chemicals, textiles, foodstuffs and general merchandise. The advantages of using intermediaries are many (Baker, 1991). First, manufacturers may enjoy cost advantages such as minimising the cost of a field sales organisation, eliminating warehousing and local delivery costs, reducing the risk of loss through inventory obsolescence and minimising inventory financing charges. Second, the use of intermediaries allows the producers to reach all potential users without having to incur the fixed costs which would arise if direct selling were used. Lastly, intermediaries can provide immediate availability and the necessary information associated with market trends, competitors' movements and customers' tendency.

At the same time, the GTCs/*Sogo Shoshas* promote business on the basis of two types of contractual structure: distributorship and agency contractual structures. A distributor is a merchant who takes title to the principal's goods, whereas an agent is a representative, who acts on behalf of the principal. Under the distributorship contractual structure, a sales and purchase contract is made between the principal and the distributor and a separate contract is made between the distributor and the end-user. This means that the principal does not have a legal right to be involved in the business between the distributor and the end-user.

(Figure 2.3. Distributorship and Agency Contractual Structures)



(Designed by the author)

However, under the agency contractual structure, the contract is made only between the principal and the end-user and the agent represents and acts on behalf of the principal only. Regarding the method of compensation, a distributor can take income from the difference between its purchasing price from the principal and its selling price to the end-user (trade discount guaranteed by the principal), whereas an agent is compensated on the basis of a commission from the principal. The GTCs/*Sogo Shoshas* are normally involved in transactions with the distributorship contractual structure, which enables them to make higher profits than the agency contractual structure would.

One of the key features of the GTCs/*Sogo Shoshas* is that they normally have their own warehouses in major seaports throughout the world. They keep enough inventory in warehouses and distribute them to markets by periodically checking the status of the demand and supply balance. Operating warehouses has two major objectives. First, the GTCs/*Sogo Shoshas* may expect stable income through quicker and on-time delivery to the end-user as soon as they receive an order. Second, they can maintain a long-term relationship with customers through the constant supply of the product. Besides pursuing their own profits, one of their ethical missions is the constant supply of goods once the relationship is established. Most employees of the GTCs/*Sogo Shoshas* bear in mind that it is their responsibility to supply raw materials to manufacturing firms to allow the continued operation of the plants.

2.3.4. Financial Perspective Approach

One of the important reasons of the GTCs'/*Sogo Shoshas'* existence is their financial role as quasi-bankers through providing various financial services, ranging from extending credit, making loans and providing loan guarantees and project finance both to sellers and buyers, in particular to small and medium-sized firms (Yamaji, 1991). The banks both in Korea and Japan traditionally abhorred the risks involved in making loans to small and medium-sized companies by demanding unfair collateral, checking their financial status and vetting their current business performance and future prospects.

The major reason why banks insist on a conservative lending policy to small and medium-sized companies is that the government supervised the banks. The Japanese government does not want the experience of a bank's bankruptcy, such as occurred in the pre-war period and the Korean government also does not want to see a repetition of the financial crisis period in the late 1990s when many banks went bankrupt. According to Miyashita and Russell (1994), the *Sogo Shoshas* in Japan played an extremely important financial role in Japanese business by providing credit to small- and medium-sized firms. Without the *Sogo Shoshas* to act as financial intermediaries, these firms would have to deal directly with the giant city banks.

Kunio (1982, pp. 215~217) described the GTCs'/*Sogo Shoshas'* financial role for SMEs as follows:

> *"If small- and medium-sized companies had been satisfied with growth using their own funds, there would have been no financial role for trading companies (e.g. Sogo Shoshas) to play, but as it was, the latter functioned as conduits for the flow of money from banks to small-and medium-sized companies. These companies could borrow a certain amount from banks on their own by offering their assets as collateral … But banks were not willing to lend money beyond a certain percentage of the value of the collateral. One problem for banks was that they were supervised by the Ministry of Finance … Trading companies borrowed money from banks and lent it to the small- and medium-sized companies which had high growth potential"*

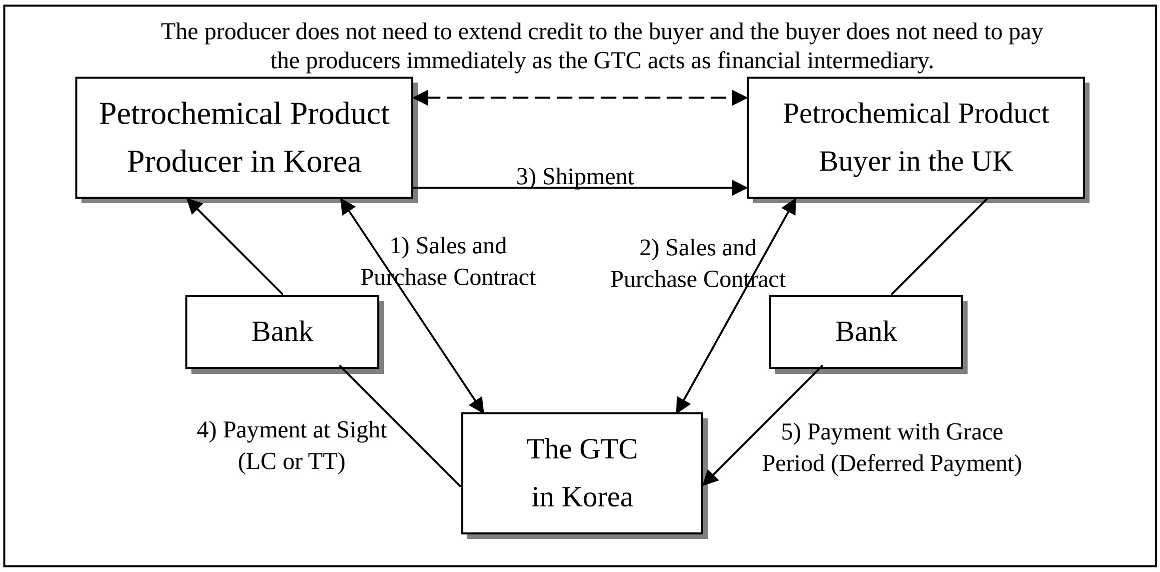
Still, the *Sogo Shoshas* played an extremely important financial role by providing to Japanese firms in the early stage of Japanese international trade development with medium-term financing, a credit with a maturity of 90 days to five years, which is a typical and indeed constitutive credit in a commercial economy. This became available very early in the form of the instruments developed in Europe and remained almost undeveloped in Japan. Drucker (1975) stressed that general trading companies (the *Sogo*

Shoshas) are the one way in which the Japanese economy manages its medium-term credit problems. They create their own money pool, or what bankers called a "float"– a reservoir of money which can be used whenever the need arises. From this point of view, he said, "in many ways, the *Sogo Shoshas* are not trading companies, but finance companies."

Of the various financing instruments, from short-term to long-term financing, provided to customers by the GTCs/*Sogo Shoshas*, the most frequently provided is the granting of a grace period for payment in trading transactions. Albaum *et al., (*2002) emphasised that financing and payments are issues directly tied to export pricing and that export prices are not set in isolation but must take into account how payment is to be made. Generally, the exporter would prefer the most secure payment method, while the importer would prefer the least expensive. Since the extremes for each are at opposite ends of the ordering, it is obvious that some form of compromise will be needed. In this situation, the GTCs/*Sogo Shoshas* can be arbitrators who solve any conflict arising from payment arrangements between exporters and importers.

The following figure presents typical examples for particular cases and it clearly shows the GTCs'/*Sogo Shoshas'* role as financial intermediaries. The process is as follows: one GTC located in Korea makes a sales and purchase contract with a producer in Korea payable at sight payment terms. Then the GTC makes a separate contract with the buyer in the United Kingdom (UK) with deferred payment terms, which grants a grace period in payment. After the producer's shipment to the buyer, the buyer does not need to pay the GTC immediately, because of the grace period that has been granted. However, the GTC does need to pay the producer immediately according to the contracted payment terms of at sight basis after shipment. Through its intermediation of the transaction, the GTC removes the producer's major burden of extending credit directly to the buyer by absorbing their payment default risk which could arise due to the insolvency of the buyer.

(Figure 2.4. Financial Service Provided by the GTCs in Trading Transactions)



(Designed by the author)
(Note: LC: Letter of Credit, TT: Telegraphic Transfer)

The GTCs/*Sogo Shoshas* also participate in project finance, which is often used for capital incentive facilities such as power plants, refineries, telecommunication facilities, toll roads and industrial plants (Davis, 1996). The Export-Import Bank (EXIM bank) in Japan and Korea, the Export Credit Guarantee Department (ECGD) in the UK, Hermes in Germany and SACE in Italy have organised special project finance units. However, sources of funding have recently expanded to the GTCs/*Sogo Shoshas*, banks and insurance companies. In huge projects, most foreign buyers prefer to pay on an instalment basis over several years or on a pro-rata basis according to the progress of the project. However, the exporter (the constructor) normally does not want to accept such a payment scheme, mainly because of the foreign exchange risks involved. In this situation, the GTCs/*Sogo Shoshas* can organise the payment problems by arranging financing for the foreign buyer and making it possible for the exporter to obtain immediate payments. In the process of arranging financing for foreign buyers, the GTCs/*Sogo Shoshas*, with their high credit reputation and financial standing, use foreign banks located around the world to borrow funds.

2.4. Conclusion and Discussion

This chapter examined the nature of the GTCs and *Sogo Shoshas* in terms of definitions, characteristics, functions and rationale.

In this review, it is generally understood that the GTCs and *Sogo Shoshas* are unique organisations which have a wide range of activities from trading transactions, financing and information gathering to organising and coordinating projects. With respect to their raison d'être, the most applicable theory lies in transaction cost economics: that the GTCs and *Sogo Shoshas* act as intermediaries not only to promote transaction activities but also to reduce transaction costs between seller and buyers. They also pursue informational economies of scale as information intermediaries by providing customers with micro-level information as well as macro-level information such as the political situations, legal systems and social environments of certain countries. International marketing and distribution activities are their primary businesses on behalf of small manufacturers or their affiliate companies. Another activity – financing – makes them distinctive organisations compared to ordinary trading companies. They extend various levels of credit, short-term, medium-term and long-term, not only to sellers but also to buyers as quasi-bankers. In particular, their participation in huge projects for industrial facilities or infrastructure construction also justifies their existence.

Although it seems that many multinational enterprises or big ordinary trading companies such as the Volkswagen (VW) Group in Germany or the ICC Trading Corporation in the United States (US) carry out similar activities to those of the GTCs and *Sogo Shoshas,* fundamentally they are quite different. First, when we look at the foundation of the GTCs and *Sogo Shoshas*, both of them were artificially established by the government in order to protect the national economy from Western (as in the case of the Japanese *Sogo Shoshas*) or to promote national economic growth (as in the case of Korean GTCs), whereas most multinationals and ordinary trading companies in other countries are purely established on the basis of the market principle of pursuing their own profit maximisation and are therefore free from government intervention. Second, unlike the GTCs and *Sogo Shoshas*, multinationals and ordinary trading firms concentrate their businesses on one industry only or a few products or services with quite limited functions. For instance, the VW Group focuses on the automobile industry[10] and the ICC Trading Corporation puts its emphasis on chemicals or petrochemical businesses. Another example is financing. The VW Group, for instance, has 17 financial services divisions around the world. Although the Group carries out financial activities, they are quite unlike those of the GTCs and *Sogo Shoshas*.[11]

[10] As of 2008, VW Group has 51 automotive divisions, including nine brands, namely, VW, Audi, Skoda, Bentley, Seat, Lamborghini, VW Commercial Vehicles, Bugatti and Scania (Internet Web Page of VW Group, 2008).

[11] The author contacted Mr. Andreas Buchta, a manager of the Public Relations of the VW Group in Germany through e-mail and telephone. According to him, VW Group has no close relationship with the German government. Thus, the government has no right to intervene in VW's business. Although VW has many sales companies around the world, it has no specialised trading firms as the GTCs or *Sogo Shoshas* have. VW's two major fields are automobile and financial services. Financial services include banking work, cash management, etc. and its function is quite different from that of the GTCs and *Sogo Shoshas*.

Moreover, it is very rare for a single company (e.g. a GTC or *Sogo Shosha)* to take part in a huge industrial project (e.g. project financing) as merely a financial intermediary.

Why then do other organisations not adopt the system of the GTCs and *Sogo Shoshas*, which is unique? The important thing to recall here is that the phrase “Unique organisations or business system” does not mean “Successful organisations or competitive business systems” which other organisations should adopt. Both the GTCs and *Sogo Shoshas* were established not only to pursue macro-level tasks (i.e. national economic development), but also to pursue micro-level activities (i.e. company-level business). From the internal standpoint, it was very difficult for small ordinary trading companies to meet the requirements stipulated by the government needed to get GTC status in Korea. For this reason, only a few big business groups (i.e. the *Chaebol* groups) could apply for this GTC status and it was granted by the Korean government to only 13 companies, which all were big business conglomerates. Furthermore, pursuing macro-level tasks to meet the government’s intention or policy required abundant capital and resources which normal companies hardly ever possessed. From the external standpoint, the reason why many organisations in other countries do not choose the GTCs system is associated with various factors, to do with the historical, political, economical, legal and socio-cultural environments. For instance, the historical background and cultural and business environments differ between Korea and European countries in many ways. In particular, the relationship between the government, banks and business groups in European countries is much weaker than it is in Korea. In Korea’s case, a closer tie between the government and big business groups was one of the major factors allowing the rapid growth of the GTCs in quantitative terms for the past two decades. For these reasons, other organisations in foreign countries would not easily adopt the GTCs system and it remains unique.

CHAPTER 3. THE GTCs AND THE KOREAN ECONOMY

3.1. Introduction

This chapter aims to investigate the nature of the Korean GTCs and their impact on Korea's national economy. Since the process of national economic growth started in the early 1960s with the implementation of a series of Five-Year Economic Plans, the GTCs have played an important role in various areas. First, the chapter reviews the history and development of the Korean GTCs. Second, the present GTCs in Korea will be reviewed. In this section, their strategy, major business areas, financial performance, number of employees and number of overseas branch offices will be examined. Third, the management system within Korean GTCs, such as the organisational structure, corporate culture, decision-making process, ownership/corporate governance and human resource management, will be considered. Fourth, the GTCs' recent financial performance, such as revenues, profitability and stability, will be reviewed. Last, the relationship among the GTCs, *Chaebols* and Korean economy will be described.

3.2. The History and Development of Korean GTCs[12]

The GTC system in Korea was modelled after that of the Japanese *Sogo Shoshas*. The GTC system in Korea began with its promulgation by the Ministry of Commerce and Industry (MCI) in MCI Notice No. 10607 in April 30, 1975. However, long discussions about the necessity of the GTC system had taken place since the mid-1960s, because Korea's economy had grown rapidly since the early 1960s with the

[12] This part is summarised from "The Handbook of Korean GTCs, 2005"

implementation of a series of Five-Year Economic Plans. In the process of national rapid economic growth, there had been many problems due to a heavy reliance on a variety of governmental supports offered to many ordinary export companies. First, the government was not able to give financial support to all ordinary export companies. It could not continue to support both the increasing number and size of ordinary export companies with an increasing volume of subsidies. Second, the government was not able to give the proper incentives to make ordinary export companies self-sufficient. This lack of government incentives resulted in the ordinary export companies lacking the strength to manage export marketing. Third, the government's support to these companies with participation of small-scale manufacturers in the same international markets caused over-competition between them. The over-competition cut export prices, thus decreasing profitability.

In this situation, the government policy-makers had to renovate the export system to keep pace with the rate of increasing exports. They recognised the needs of expert companies in overseas markets and decided to adopt the Japanese *Sogo Shosha* system: a powerful engine of the export-led economic growth of Japan. According to Han (1990), the Korean government expected the GTCs to have three basic functions. First, the GTCs had to have strong international marketing skills. In order to overcome the protectionism of industrialised countries, the GTCs had to be able to approach the consumers in industrialised countries and exploit untapped potential. Second, the GTCs were meant to help produce exports from those manufacturers who had already shown their inefficiency in exports through unnecessary over-competition, dumping, or through the complications arising from the presence of too many exporters. Third, in order to overcome the problems mentioned above, the GTCs had to be large in size and limited in number.

The MCI promulgated the procedures and a set of formal requirements for GTCS to meet for in April, 1975. The minimum requisites initially set by the government for the designation of the GTCs were as follows: i) minimum capitalisation of one billion Korean Won (KRW), ii) an annual value of export per year of US$50 million, iii) ten overseas branch offices, iv) a minimum of ten countries with an export value of US$1million each, v) seven product categories with an export value of over US$500,000 each per year and vi) a public offering of the GTCs stock. Because the GTCs were founded by the government, the government came to specify minimum export targets, capitalisation requirements, number of export items, number of overseas branch offices and the extent of public share ownership for each GTC. Samsung was designated as the first Korean GTC in May, 1975, followed by Ssangyong, Daewoo, Kukjae and Hanil in the same year. Six more companies were designated as GTCs in 1976: Koryo, Hyosung, Bando, Sunkyoung, Samwha and Kumho. In 1978, Yulsan and Hyundai were added, bringing the total number of Korean GTCs to 13. However, Yulsan went bankrupt in 1979, resulting in the liquidation of the Yulsan Trading Company. Again Hanil, Samwha and Kumho failed to retain their GTC status, due to their not achieving a 2% share in Korea’s total exports, which was a requisite for GTC designation.

During the period 1975~1981, the ordinance governing the Korean GTC system underwent a series of amendments due to changes in the economic environment and government policies. The table below shows the changes in requirements for GTC designation.

(Table 3.1. Changes of Requirements for GTC Designation)

	1975	1976	1978	1980	1981~83	1984	1987~
Annual export (US$ million)	50	100	Two percent of total Korean exports				
Capital (KRW 100 million)	10	15	20	Not required			
Export items over US$1 million	7	10	5	5	Not required		
Export countries over US$1million	10	15	Not required				
Number of overseas branch offices	10	15	20	20	Not required		
Public offering of stocks	Mandatory						Not required

(Source: Ministry of Commerce and Industry)

Most Korean big business groups (*Chaebols*) were eager to get GTC status after the foundation of the GTC system in Korea, because of the many incentives given[13]. First, GTC status can enhance the business group's credibility both in Korea and in the world markets. Second, with GTC status, the business group can increase the probability of obtaining government concessions on various government-initiated projects, such as heavy and chemical plants. In addition to those psychological rewards, the GTCs had many government-offered incentives, for instance, as in trade and administration, financial, foreign exchange and tax. In terms of trade and administration

[13] Most of this section part draws on Chung, G. Y (1993), *"The Korean General Trading Companies: Analysis of Process, Performance and Prospect"*, DBA dissertation, Golden Gate University, San Francisco, California, pp.74~76

incentives, the GTCs were preferentially treated in international bidding offered by the government and they found it easy to access the import of raw materials for their own use. In financial incentives, they had priority in obtaining bank loans based on past export performance. Incentives were also given them in the areas of foreign exchange and tax. The government allowed the GTCs to increase the limit of foreign currency holdings by overseas branches and exempted them from business income tax. Beside the above direct incentives, some indirect incentives were also given. Each GTC had regular meetings with other GTCs and regular consultations with government agencies.

3.3. The Present GTCs in Korea[14]

After the adoption of the GTC system in Korea, many companies were designated as GTCs, the total number reaching 13 in 1978. However, some companies failed to retain their GTC status and went bankrupt. At present, only seven companies have retained GTC status and are still running. This section investigates these seven GTCs including a brief history, strategy, major business areas, financial performance, number of employees and number of overseas branch offices.

3.3.1. Samsung Corporation

The Samsung Group was started in 1938 by Lee Byoung Chul under the name of Samsung *Sanghae*. The Samsung Group is the first and largest *Chaebol* in Korea in terms of total assets, consisting, as of 2008, of 59 affiliated companies. The Group's main businesses are electronics, trading, heavy industry, chemicals, financial services,

[14] This part is summarised from various publications, including each company's "Company Brochure, Annual Report, Internet Website and the Handbook of Korean GTCs."

home appliances, engineering and construction and hotel operations. The Group's management philosophy is to devote its human resources and technology to creating superior products and services, thereby contributing to a better global society. Samsung Group's management philosophy represents its strong determination to contribute directly to the prosperity of people all over the world.

Samsung Corporation is a parent firm of the Group and was designated as the first GTC in May, 1975. It played an important role as a GTC in the process of its Group's development. The Company was awarded a US$10billon Export Tower in 1994 and a US$15 billion Export Tower in 1998. In 2007, its total revenue was US$10,753 million, gross profit was US$1,049 million and net income was US$538 million.

Regarding organisational structure, the Company in 2008 has 3 administrative departments and 12 business departments. Under the business departments, there are 30 different divisions dealing with a number of products and services. It has 736 employees and 85 overseas branch offices worldwide. Samsung Corporation's management philosophy and long-term business plans include risk management and human resource management (HRM). Detailed action plans and strategies in risk management are the prevention of risks in all areas. It also adopted HRM as a main business plan through the acquisition and development of core human resources and talent-oriented management.

(Table 3.2. Samsung Corporation's Management Philosophy)

Name of the GTC	Management Philosophy	Promoting Strategy
Samsung Corporation	Risk Management	● Prevent risk in all business areas ● Take precaution against risks
	HRM	● Acquisition and development of core human resources ● Talent-oriented management ● Respect customers, shareholders and employees
	Reinforce Organisational Competitiveness	● Strengthen the unity of the organisation

(Source: Annual Report of Samsung Corporation and the Handbook of Korean GTCs)

The Company consists of four groups, namely, a Trading Group, an Engineering and Construction Group, a Housing Development Group and a Retail Business Group. Samsung Corporation's 1996 merger with Samsung Engineering and Construction and the1997 opening of the Samsung Plaza Department Store were both important milestones in Samsung Corporation's emergence as a global company, in terms of scale and capabilities. The Company's major business areas are trading, project organising, overseas investment and skyscraper construction. The Company's synergy comes from three things: a global network, decades of project management know-how and world-class financing and marketing capabilities. The Company's main business is trading in numbers of products, for example, petrochemical, general chemical, steel, fibre/fabric products and so on. The Company's project organising services offer a prime example of this synergy in action, delivering total solutions encompassing consulting, financing, technology and construction. Samsung Corporation is also enhancing its production and distribution capabilities through strategic direct investment. For example, in 1997, it took charge of the privatisation of the struggling Romanian stainless steel producer Otelinox, helping the company to increase profits by over 1000% in just three years. Skyscraper construction is a new business area of Samsung Corporation. The Company's project management information system, through the planning and engineering staff, have met the technology, experience and manpower requirements for erecting the world's tallest buildings, such as Taiwan's Taipei 101 tower.

3.3.2. Daewoo International Corporation

Daewoo Group was founded in 1967 as a textile trading company by Kim Woo Choong. Since then, the Group has become one of the world's largest industrial enterprises, being listed 18th in the 1998 Fortune Global 500. The Group's main businesses are vehicle manufacturing, trading, shipbuilding, engineering and construction, securities, consumer electronics, home appliances and hotel operations. As of August, 1998, before its collapse, Daewoo Group was the fourth largest *Chaebol* in Korea in terms of total assets, consisting of 33 domestic companies and 372 overseas subsidiaries. However, Daewoo Group announced details of its restructuring plan, featuring a reduction in the number of its core business operations and a drop in the number of its domestic companies in August, 1998 under the IMF plan.

Daewoo International Corporation (formerly Daewoo Corporation) is the GTC within the Group; it was established in 2000 as a result of a spin-off plan of Daewoo Corporation. Since its foundation, Daewoo International Corporation has been growing as a special trader and overseas investment company all over the world under the banner of a "Global Trading and Investment Company." Daewoo International Corporation was the driving force for the trade and overseas investment of Korea in a variety of businesses, including trade, manufacturing, sales, distribution and resource development with about 6,000 clients world-wide, by collecting and using the optimised information of the global business network based on its information and technology infrastructure.

In 2007, its total revenue was US$8,637 million, gross profit was US$102 million and net income was US$96 million. As of 2008, the Company has 4 administrative departments and 12 business departments. Under the business departments, there are 43 divisions which deal with a number of different products and services. It has 1,704 employees and 72 overseas branch offices worldwide. The Company's corporate culture focuses on "Creativity, Challenge and Trust." The Company believes that its employees must be creative and innovative for both personal and corporate success. The spirit of challenge gives ample opportunities for everyone. A corporate entity must offer clients, partners, shareholders and society in general ample trust and reliability. Corporate and public prosperity depend on honesty and transparency, as well as efficiency and excellence in all operations.

The Company's management philosophy and medium-and long-term business plan is to strengthen commodity trading and core competence, selection and concentration on a strategic market, natural resource development and project related business. The table below shows the Company's business plans and strategies.

(Table 3.3. Daewoo International Corporation's Management Philosophy)

Name of the GTC	Management Philosophy	Promoting Strategy
Daewoo International Corporation	Strengthen Commodity Trading	● Concentration on core commodities trading (Steel, chemical, metal and textile)
	Strengthen Core Competence	● Undertake HRM plan (Result-based evaluation) ● Establishment of a knowledge-based management system
	Selection and Concentration on Strategic Markets	● Business expansion in the China market ● Establishment of Task Force Team for strategic markets (China and the EU)
	Natural Resource Development and Project related Business	● Investment in overseas natural resource development (Energy, gas and crude oil, etc) ● Participation in project-related business (Infrastructure-related projects, such as power plants and road construction, etc)

(Source: Annual Report of Daewoo International Corporation and the Handbook of Korean GTCs)

The Company's main businesses are trading, project management and overseas investment. Trading business deals with a number of products such as steel, metal, chemicals, automotive and component parts, general commodity and energy-related products. The Company has around 50 overseas networks. The overseas corporations which Daewoo International Corporation has invested in are divided largely into the trading corporations which provide the comprehensive trading services, such as local marketing, financing, logistics and others and the investment corporations which undertake the product manufacturing, power generation, transportation and other services including cement, paper, textile products, plywood, pharmaceuticals and others. Among these overseas investment corporations, the major fields of involvement may be the cement company in Shandong, a paper company in Mudanjiang, a cotton company in Uzbekistan, a sewing company in Indonesia and a pharmaceutical company in Sudan.

3.3.3. LG International Corporation

In 1947 Koo, In Hwoi started the LG (Lucky Gold Star) Group business under the name of *Lak Hui* Chemical Industry (currently LG Chemicals Ltd.). The Group's main businesses were electronics, chemicals, trading, telecommunication and services and home appliances.

Lak Hui Chemical Industry changed its name to Bando Corporation (currently LG International Corporation) and started its trading business in 1956. In 1976, the Company was designated as a GTC and awarded a US$100 million Export Tower. In 2007, its total revenue was US$5,924 million, gross profit was US$65 million and net income was US$53 million. Regarding organisational structure, the Company in 2008 has 2 administrative departments and 8 business departments. Under the business departments, there are 28 different divisions, which deal with a number of products and services. It has 659 employees and 52 overseas branch offices world-wide.

The Company's medium- and long-term business plans are risk management, portfolio management and its management philosophy is the strengthening of organisational competence. The table below shows the Company's business plans and strategies.

(Table 3.4. LG International Corporation's Management Philosophy)

Name of the GTC	Management Philosophy	Promoting Strategy
LG International Corporation	Risk Management	● Strengthen the ability of risk prevention and management ● Intensify information-sharing between headquarters and overseas offices ● Strengthen the system of mutual assistance of business among business units
	Portfolio Management	● Selection and concentration strategy ● Allocation of management resources to core businesses
	Strengthen Organisational Competence	● Acquisition of core human resources ● Raise organisational productivity

(Source: Annual Report of LG International Corporation and the Handbook of Korean GTCs)

The Company's main businesses are trading, development and investment in overseas resources, project organising and domestic sales and distribution. With regard to the trading business, the Company deals with petrochemical products, metal and coal products, foodstuffs, energy-related products, machinery and aviation and fashion clothing products. The Company is participating in numbers of overseas resources development and investment enterprises to secure a long-term, stable supply of major raw materials for industrial use. For instance, it was involved in the development of the Ensham bituminous mines in Australia in 1993 and of the Erel bituminous mines in the Sakha Republic of Russia in 1996. Now, it is supplying bituminous coal to Korea and exporting the coal to Japan, Taiwan and other countries. LG International Corporation also participated in a gold copper mine development project in Rapu-Rapu, the Philippines in 2003 and is concerned in currently operational oil fields.

The Company is armed with qualities which differentiate it from its competitors, namely, its strengths in financing, information and networking, thus exercising organisational abilities which enable the company to create synergies in conducting its business and earn highly profitable orders. For example, in 1998, the Company secured a US$ 700 million refining plant order in Qatar, which was a symbolically significant project because it came at a time when Korea's sovereign credibility was suffering. This achievement also attracted the attention of the Middle East's plant market. Thereafter, the Company continued to strike deals on huge plant construction projects in the Middle East.

3.3.4. Hyundai Corporation

Hyundai Group started its business as *Gyungil Sanghwoe* in 1937, founded by Chung Ju Young. The history of the Hyundai Group is the history of the modern Korean economy. The Hyundai Group stood at the centre of the "Miracle of the Han River" and made tremendous contributions to the establishment of Korea's economy. The Group's main businesses were vehicle manufacturing, engineering and construction, shipbuilding, logistics, chemical, trading and so on.

Hyundai Corporation is the GTC within the Group and was so designated in 1976. Hyundai Corporation was founded in 1976 as a trading company and was awarded a US$300million Export Tower on the 14th anniversary of Export Day. The Company has been growing since its designation as a GTC in 1978 and was awarded a US$25billion Export Tower in 2000. In 2007, its total revenue was US$1,844 million, gross profit was US$66 million and net income was US$49 million. Regarding organisational structure, the Company has 2 administrative departments and 6 business departments as of October, 2008. It has 267 employees and 34 overseas branch offices worldwide.

Hyundai Corporation's management philosophy and long-term strategies are value-based management, customer satisfaction management and talent-oriented management. Its mid-range business strategies are selection and concentration and portfolio strategy.

(Table 3.5. Hyundai Corporation's Management Philosophy)

Name of the GTC	Management Philosophy	Promoting Strategy
Hyundai Corporation	Value-based management	● Provide specialised products and services customers need (Specialisation) ● Increase value through brand globalisation of products and services (Brand strategy) ● Create new value responsive to market change
	Innovation-driven Management	● Innovate existing business structure ● Selection and concentration strategy (Concentrate corporate resources to four strategic fields; Information and communication, iron and steel, natural resource development and local business) ● Extend value chain ● Portfolio strategy (To diversify income sources, advance into new businesses)
	Talent-oriented management	● Fair compensation for the performance and efforts of the employees (Economic compensation) ● Constantly motivate employees' self-development efforts and provide a sense of achievement (Sense of achievement) ● Provide vision with clear and precise goal

(Source: Annual Report of Hyundai Corporation and the Handbook of Korean GTCs)

The Company’s main business areas are trading, overseas investment, resource development and shipbuilding business. In its trading business, the company deals with machinery, automobiles, steel, chemicals, ships, plants and so on. On the basis of marketing know-how, financing capability and the global business networks acquired during 30 years of general trading activities, Hyundai Corporation has successfully undertaken a wide variety of overseas investment businesses around the world, including shipbuilding, steel processing and distribution, as well as real estate development and overseas energy resources development. Resources development aims to bolster profitability by continuing to invest in high value-added business and will continue to be actively engaged in natural resources development projects, making the most of its vast experience and know-how. In accordance with the Company’s policy securing a stable profit foundation and diversifying it, the Company has started to participate in the Drayton coal mine development in Australia in 1979 and carried out several successful projects, such as the Marib oil project in Yemen. Steering its business portfolio to something more stable in the long term, the Hyundai Corporation has sought to secure a manufacturing and distribution business base to take a great leap forward and become a world leader as a trading company.

Since 2004, the Hyundai Corporation has set up five strategic new businesses, including a shipbuilding business, in an effort to transform the current business structure, which had been dependent on intermediate trading and export business, into a more value-added one. After acquiring the 30-year-old Qingdao Lingshan Shipyard located in Jiaonan City, Qindao, Shandong in China and establishing a joint venture, Qingdao Hyundai Shipbuilding, the Company has embarked on a shipbuilding business. This is significant because Hyundai Corporation is thus the first general trading company to set up a business in a manufacturing industry. Eventually, this will accelerate the Company's business diversification and lay a solid foundation for the Hyundai Corporation to become a world leading company.

3.3.5. SK Networks Co., Ltd.

The SK Group, founded by Choi Jong Kun, started its business under the company name of SunKyong Textiles Ltd. in 1953. The Group's main businesses are telecommunication, trading, chemical, gas and energy, construction, life insurance, securities, shipping and so on and it is now Korea's fourth largest conglomerate and one of the leading business organisations in Asia, with 64 affiliate companies.

SK Networks is the GTC within the Group and was designated as such in 1976. Founded as the parent company of the SK Group in 1953, SK Networks (formerly SK Global) functions as a marketing arm of SK affiliates, handling some 50 products which it distributes under ten brands via as many as 6,000 distribution channels. In 2007, its total revenue was US$19,543 million, gross profit was US$1,466 million and net income was US$653 million. Regarding organisational structure, as of 2008, the Company has 7 business departments, which are divided into 13 different divisions dealing with a number of products and services. There are 40 overseas branch offices world-wide.

With respect to management philosophy, the Company introduced the SK Management System (SKMS) in 1997; this is an all-inclusive management development strategy based on respecting the dignity and creativity of each employee. The details of

SKMS are i) to instill vision, values and goals in employees, ii) encourage people to achieve high performance, iii) bring together diverse groups of individuals and achieve consensus, iv) find, develop and reward the unique talents of all people and v) foster understanding and acceptance of business principles including the priority of maximising growth.

(Table 3.6. SK Networks' Management Philosophy)

Name of the GTC	Management Philosophy	Promoting Strategy
SK Networks Co., Ltd.	HRM	● Respect the dignity and creativity of each employee ● Make lively organisational working conditions ● Encourage people to achieve high performance
	Strengthen Current Business and Develop New Growth Engines	● Strengthen the competitiveness of current business by driving productivity maximisation for information and communication, energy, export, import and fashion businesses ● Increase the number of loyal customers by exploiting the existing customer data base and channel it to develop new growth engines
	Focused on Globally Localised Marketing	● Develop integrated marketing ● Carry out customer-centred marketing and secure a wide range of products and global brands

(Source: Annual Report of SK Networks and the Handbook of Korean GTCs)

SK Networks' main business is divided into two areas: global business and domestic business. In global business, the Company is involved in the following global activities: resources and energy, chemicals and steel businesses. Resource and energy businesses are the Company's main business and it revolves around oil and gas trading, coal trading and resources development. In regard to chemicals, the Company specialises in the import, export and domestic sales of various chemical products, including aromatic compounds, synthetic resins, chemical textile materials, solvents such as methanol and phosphate fertilisers. The Company also supplies global buyers with various domestic and foreign steel products. In regard to their domestic business, the Company is involved in information and telecommunication and fashion and convenience stores.

3.3.6. Hyosung Corporation

The Hyosung Group was founded with the company name of Hyosung Corporation as a textile exporter in 1957 by Cho Hong Jae. Since its foundation, this Group has grown as one of the most prestigious conglomerates in Korea. The Group's main businesses are textiles, chemicals, trading, construction, information and communication and power and industrial systems. Hyosung Corporation is a parent company of the Group and was designated as a GTC in 1976. In 2007, its total revenue was US$5,995 million, gross profit was US$762 million and net income was US$184 million. The Company has a harmonised combination of 7 Performance Groups and 23 Performance Units, with 23 overseas branch offices worldwide as of 2008.

The Company's management philosophy is to ensure customers' satisfaction and happiness. Thus, the Company puts human value first. With respect to promoting strategy, in its management philosophy, the Company adopts risk management, marketing innovation and HRM.

(Table 3.7. Hyosung Corporation's Management Philosophy)

Name of the GTC	Management Philosophy	Promoting Strategy
Hyosung Corporation.	Customer Satisfaction	● Respect the value of customers ● Intensify risk management capability in order to achieve customer satisfaction ● Innovate marketing strategy ● Respect the value of employees (HRM)
	Development of New Growth Engines	● Foster professionals equipped with information and knowledge ● Gradually convert conventional businesses into new functional businesses
	Creating High Spirits Corporate Culture	● Respect employees' creativity and autonomy

(Source: Annual Report of Hyosung Corporation and the Handbook of Korean GTCs)

3.3.7. Ssangyong Corporation

The Ssangyong Group was officially founded as a cement business by Kim Sung Kon in 1962. The Group's main businesses are the production and sale of cement and ready mixed concrete, trading, recycling of waste and other environment-related business and chemicals. Ssangyong Corporation is the GTC and it was designated as such in 1975. In 2007, its total revenue was US$1,161 million, gross profit was US$54 million and net income was US$11 million. Regarding organisational structure, in 2008 the Company has 4 administrative departments and 13 business departments. It has 392 employees and 21 overseas branch offices world-wide

Ssangyong Corporation's management philosophy is to continue its growth and prosper through profitable corporate activities under the slogan (i.e. the corporate culture) of "Reliability, Innovation and Harmony." With respect to promoting a strategy, its management philosophy is aimed at a business with solid profitability and sound financial structure, one which gives priority to the environment and safety, complying with laws and ethical standards and making a contribution to society and one which seeks effective cooperation between labour and management.

(Table 3.8. Ssangyong Corporation's Management Philosophy)

Name of the GTC	Management Philosophy	Promoting Strategy
Ssangyong Corporation.	Re-creation of the Company	● Focus on further growth and prosperity ● Achieve solid profitability and maintain a sound financial structure ● Comply with laws and ethical standards
	Innovation of Corporate Culture	● Have a 'Can do spirit' ● Infuse with a sense of responsibility ● Innovate employees' consciousness and behaviour ● Put emphasis on employees' creativity and initiative

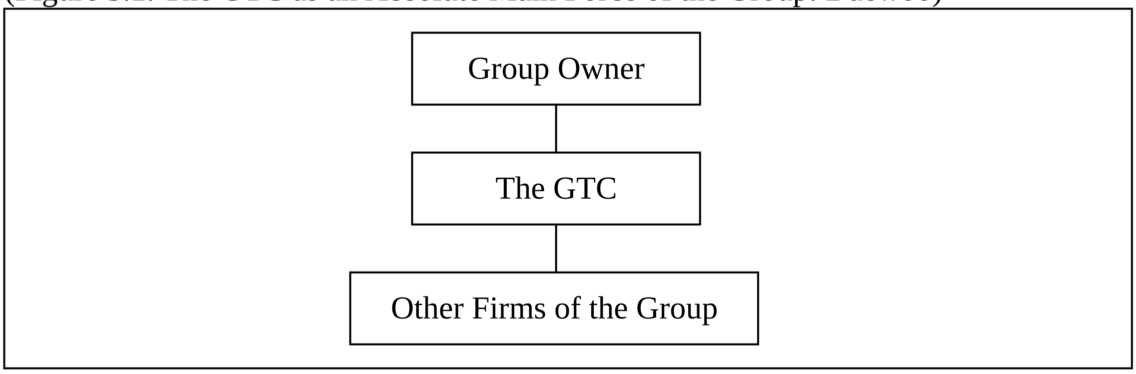
(Source: Annual Report of Ssangyong Corporation and the Handbook of Korean GTCs)

3.4. The Management System within Korean GTCs

3.4.1. Organisational Structure

All Korean GTCs, then, were parts of large conglomerates (*Chaebol* Groups). In most cases, the GTCs were the main force of their Groups. However, each one's importance in its Group was different. The roles of the GTCs in their Groups can be divided into three types: the GTC as an absolute main force of the Group, the GTC as one of the many forces of the Group and the GTC as a supplementary force of the Group. The first type is the GTC as an absolute main force of the Group. In the case of Daewoo Group[15], the GTC (Daewoo Corporation) was a main force firm within Daewoo. It directed and controlled other firms' activities in the Group. Thus, the GTC had great influence over the activities of other firms within the Group. The organisational structure of Daewoo Group is shown below.

(Figure 3.1. The GTC as an Absolute Main Force of the Group: Daewoo)



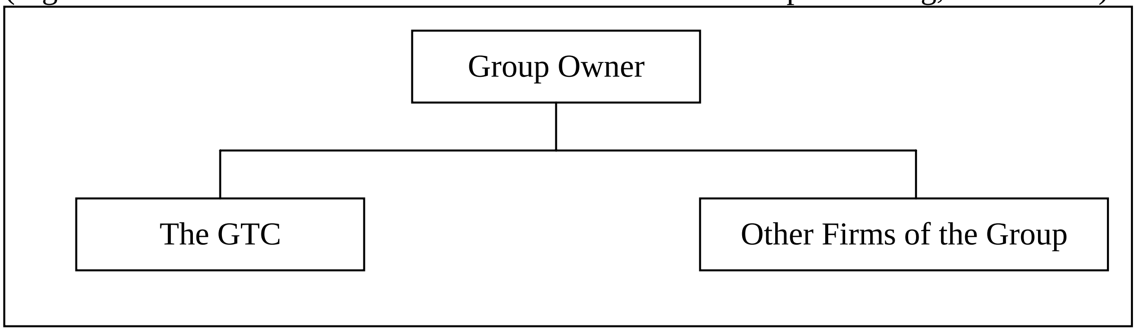
(Source: Adapted from Han, K.H. (1990), "Comparative Analysis of Factors related to the Success of the US Export Trading Companies and Korean GTCs", D.B.A. Dissertation, United States International University, p.45)

The second type is the GTC as one of the main forced in the firm. For example, such GTC as Samsung, LG and SK are one of the many main force corporations in their

[15] The Daewoo Group collapsed in August, 1998 after the Korean financial crisis. Thus, the GTC (Daewoo Corporation) became an independent firm with a new company name, Daewoo International Corporation, after this collapse.

Groups. Therefore, their influence over the other firms within the Groups is somewhat less strong than that of Daewoo over its Group.

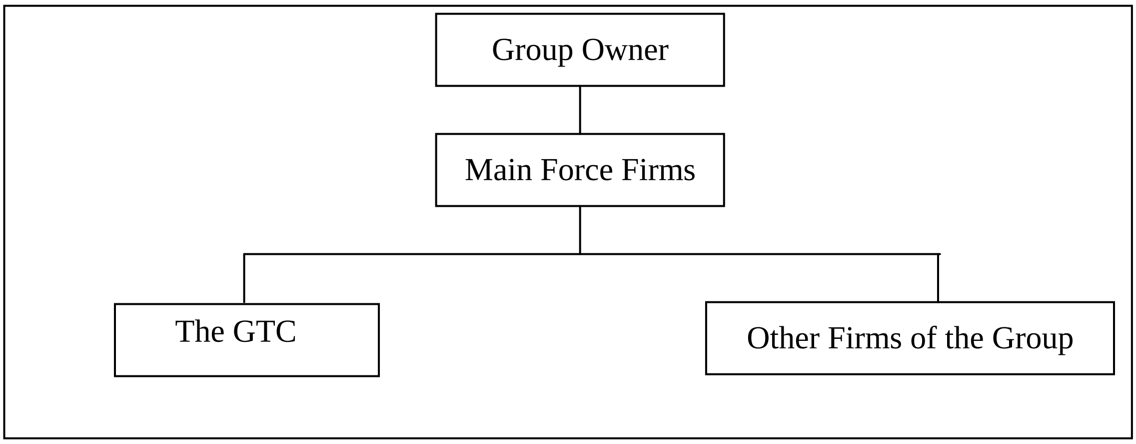
(Figure 3.2. The GTC as One of the Main Forces of the Group: Samsung, LG and SK)



(Source: Ibid, p.45)

The third type is the GTC as a supplementary force in its Group. Such GTCs as Hyundai, Hyosung and Ssangyong are merely supplementary forces in their Groups. In these latter Groups, manufacturing companies (Hyundai Group: Automobile, Chemical, Electronic, etc., Hyosung Group: Chemical, Ssangyong Group: Automobile) are the main forces of their Groups. The GTC helps only with the export and import functions of the manufacturing firms.

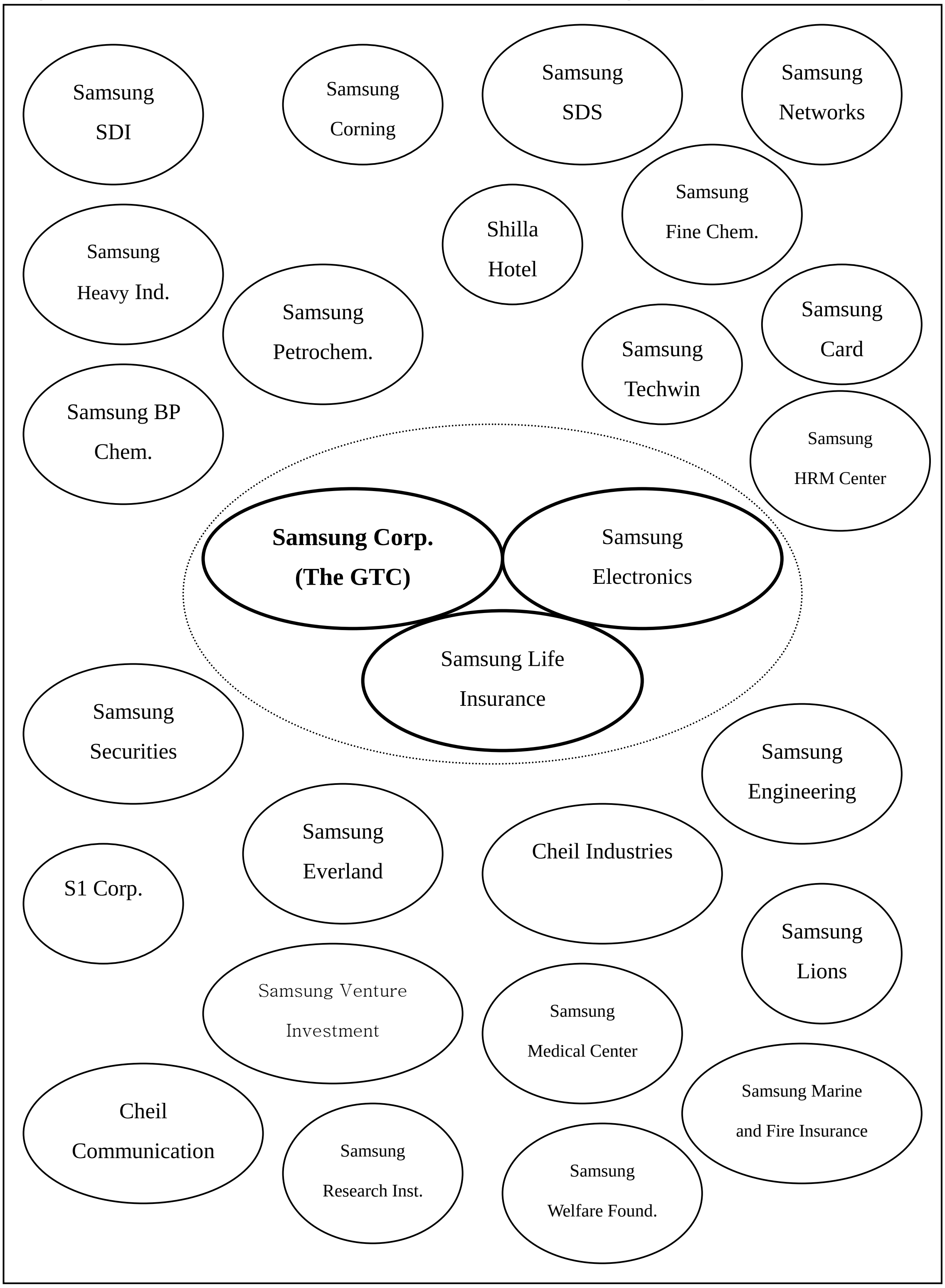
(Figure 3.3. The GTC as a Supplementary Force of the Group: Hyundai and Hyosung)



(Source: Ibid, p.45)

The following figure clearly shows the GTC as one of the main forces within the Group (Samsung Group)

(Figure 3.4. The GTC as One of the Main Forces: Samsung Group)



(Source: Adapted from Samsung Group Internet Web page (2008), www.samsung.com)

We have reviewed the Korean GTCs' organisational structure and their position and role within their Groups. Now, we examine the GTCs' internal organisational structure, apart from their Groups. Most of Korean GTCs' organisational structure is divided into administration departments, business departments, domestic branch offices, overseas branch offices and factories. Administration departments include planning/strategy, accounting/finance, HRM, logistics, purchasing and so on. In all Korean GTCs, most of the staff members are assigned to business departments. In business departments, most members are again assigned to export activities rather than import or domestic activities. This is because sources of business of most Korean GTCs come from exports rather than import and domestic businesses.

The current organisational structure of Daewoo International Corporation, for example, consists of 4 administrative departments and 12 business departments. The business departments are again divided into 43 different divisions. Basically, Daewoo has adopted an organisational system which is structured fundamentally on the basis of geography, not product lines. Daewoo divides the world into ten geographical regions: Asia, Japan, the Middle East, Europe, East Europe, North America, US, Central America, Africa and Oceania. Reporting relationships are maintained between the product and geographical sides of the firm.

The table below shows the organisational structure of the major Korean GTCs: Samsung, LG and Daewoo, by the number of departments or employees.

(Table 3.9. Organisational Structure of Korean Major GTCs in 2008)

	Samsung	LG	Daewoo
Number of Administrative Departments	3	2	4
Number of Business Departments	12	8	12
Number of Divisions within the Business Department	30	28	43
Number of Employees including Executives	736	659	1,704

(Source: Annual Report of Each GTC, 2008; E-mail Communication with Managers at GTCs, 2008)

Nonetheless, information-gathering is very important for the operation of the GTCs. In most GTCs, the strategy and planning department gathers information about overseas and domestic markets. Overseas branches also play important roles as information networks for overseas markets. Overseas branches are under the control of the headquarters in Korea. The table below shows the number of overseas branches and employees in major Korean GTCs.

(Table 3.10. Number of Overseas Branches of Major Korean GTCs in 2008)

		Samsung	LG	Daewoo
Number of Overseas Branches		85	52	72
Number of Employees	Resident Representatives	170	N/A	N/A
	Local Employees	2,426	N/A	N/A

(Source: Annual Report of Each GTC, 2008; E-mail Communication with Managers at GTCs, 2008)

3.4.2. Corporate Culture

Management literature suggests that national culture influences people in general and, eventually, the management style and corporate culture in most countries. Before examining any Korean firm's corporate culture, it is important to review the national culture of Korea.

The perceptions among Koreans and foreigners of Korea's national culture include family orientation rather than community orientation, the "Rush" spirit, educational connection, an extreme pattern of top-down decision-making, favouring seniority and tenure, growth orientation, a "can do" spirit and big business groups' domination of the national economy. Cho and Yoon (2001) suggest that the six key components of Korea's traditional cultural legacy are Confucianism, emotional harmony, hierarchy, discrimination against out-groups, networking and high context orientation. Of these, the dominant influence on Korean national culture has been Confucianism. Endorsed by this ethical norm, most interpersonal relationships are defined in terms of social status: gender, age and position in society. Confucianism emphasises five cardinal human relations: between the king and his subjects, between husband and wife, between father and son, between older and younger and between friend and friend (Chung, Lee and Jung, 1997). It is possible to say that Confucianist relations also exist within the organisation: between the corporate owner and its subordinates. Confucianism also places a strong emphasis on harmony, which enables Korea to be one of the strongest collectivist countries in the world. Hofstede (1991) suggested that Korea is the strongest collectivist country and the corporate culture is even more collectivist than that of Japan[16].

[16] Cho and Yoon (2001), however, took a quite different view of this. They suggested that Korean corporate culture, while deemed the most collectivist by Western people, is seen as more individualistic by the Japanese. To explain this, they proposed the theory of 'dynamic collectivism'. An elaboration of the traditional notion of collectivism, dynamic collectivism applies collectivist norms for in-group members and individualistic norms for out-group members. As a result, it tends to reinforce the boundary between in-group and out-group and to intensify competition between the two groups, which in turn presents Korean society as more dynamic and competitive.

Rowley and Bae (2003) summarised the way in which national or social values directly impact on corporate culture within Korean firms, as follows.

(Table 3.11. Impact of Traditional Social Values on Corporate Culture)

Traditional Social Values	**Impact**	**Corporate Culture Characteristics**
Absolute loyalty of subjects to sovereigns		Owner's authority and paternalism
Close relationship between father and son		*Inhwa* (harmony), belongingness and kinship-based relations
Separate roles for men and women	→	Devotion to the company (in particular for male workers)
Precedence of elders over younger people		Hierarchical system among members and seniorityism
Mutual trust among friends		Trustworthy relations among colleagues and collectivism
Favouring eldest son, ancestor worship and emphasis on family members		Kinship-based ownership and succession, *Yongo* (blood, geography, education –based connections)

(Source: Rowley, C. and Bae, J.S. (2003), "Culture and Management in South Korea" in Warner, M. (ed.)., "*Culture and Management in Asia*", RoutledgeCurzon, p. 194)

The two basic features of Korean corporate culture are dynamic collectivism and the family and military adoption system (roots in the family and military). Dynamic collectivism is multidimensional. Its three dimensions are in-group harmony, optimistic progressivism and the hierarchical principle. Another important feature of Korean corporate culture is that Koreans have adopted a paradigm in which organisations are like families and also like armies (Cho and Yoon, 2001)[17]. Moreover, Chung, Lee and

[17] Cho and Yoon argued that the combination of in-group harmony, optimistic progressivism and the hierarchical principle creates internal dynamics for the in-group which run alongside the dynamics

Jung (1997) place their emphasis on shared values, as seen in the Korean term *Sahoon*, one of the major features of Korean corporate culture. *Sahoon* is what reflects the cultural values, personal values and beliefs of the founder and top management. *Sahoon* basically deals with employee attitudes and behaviour related to collectivism, harmony and order. *Sahoon* is the formal statement of the managerial values which a Korean firm considers most important. Unlike Western companies, which generally emphasise their values in terms of functional and technical performance, such as customer service, innovation and product excellence, *Sahoon* in Korean firms traditionally emphasises the attitude and behaviour expected of employees among themselves, toward the company and to society. The following table shows the S*ahoon* of the Major Korean GTCs.

(Table 3.12. *Sahoon* of Korean Major GTCs)

Korean GTCs	Shared Value or Official *Sahoon*
Samsung Corp.	Respect for Individual, Pursuit of Technology and Empowerment
Huyndai Corp.	Diligence, Thriftiness, Trust and Affection
LG International Corp.	Value Creation for Customers, Respect for Individual and Empowerment
Daewoo International Corp.	Creativity, Challenge and Trust
SK Networks	Humanism, Rationalism and Realism
Hanwha Corp.	Trust, Credibility, Modesty and Excellence

(Source: Company Brochures of GTCs)

between in-group and out-group. In-group harmony is the most important and forms the keystone of corporate culture. For the sake of in-group harmony, people often sacrifice their own goals for collective ones. Another important feature is optimistic progressivism. The expectation of progress is shared as a social context within the organisation. Almost all companies set high growth targets and global visions. Optimistic progressivism creates an atmosphere of strong competition with out-group companies. Employees value hierarchical order and the leadership of superiors within their organisations. Another important feature of Korean corporate culture is that Koreans have adopted a paradigm in which organisations are like families and also like armies. The Korean family is the source of social bonds and it values higher education. Family life is the single most important way in which Koreans learn Confucian norms. These generate notions of proper behaviour among unequals and in running organisations. Moreover, all Korean men have to serve the nation in the military for at least a couple of years. Their exposure to military life reverberates over their whole careers. The organising principles of family and army reinforce in-group harmony, optimistic progressivism and hierarchy.

Another striking feature of Korean corporate culture is the high total of working hours. Traditionally, Korea has been regarded as a nation of workaholics who rarely take holidays. According to the OECD (2008), Korean labourers' working hours are on a steady downward trend, but their hours remain the only ones to exceed 2,000 per year. At the same time, the absolute wage of Korean workers is grouped among the lower ranks, at a mere 60% level of the OECD average, which showed that wages are unsatisfactory compared to the number of hours worked.

Korean workers' annual average working hours have been steadily declining: 2,447 hours in 2001, 2,390 hours in 2003, 2,351 hours in 2005 and 2,266 hours in 2007, but among OECD members they are the only ones to remain above 2,000. Such working hours are a minimum 200 hours to a maximum 900 hours longer than those of other OECD members. Thus, Korea combines the longest working hours among OECD countries with wages rank in the lower range and below the average, reflecting that Koreans receive low wages for the amount of work done. According to Maeil Business Newspaper (2008), the average wage of a full-time working-status Korean worker in 2006 was an annual US$25,379 per person, only 64% of the OECD member average of US$39,743.

Since the financial crisis in 1997, many Korean businesses have initiated a corporate transformation. Korean businesses have broadly achieved spectacular growth since the 1960s and in the process they have developed strong corporate cultures. These cultures favoured corporate growth through diversification and suited the business environment of the past, characterised by a closed home market and strong governmental support for business.

As a result, many big business groups in the country now find it difficult to abandon their growth-oriented strategy through diversification. Park (2002) argued that the strong corporate culture which once led companies to grow quickly has become a source of new problems. For Korean *Chaebols*, cheap labour costs, top-down decision-making and the government's special treatment are no longer sources of international competitiveness for them.

Transforming an organisation by a new culture and making the changes in employee values, attitude, behaviour and management style necessary for high performance is relatively difficult and time-consuming. This argument was supported by Bae, Rowley and Sohn (2002), who stressed that there are wide gaps between the old and the new paradigms and traditions. They argued that the Korean economy, for example, needs transformation in many areas including leadership, corporate culture, organisational structure and HRM. But Korean firms' efforts to change their culture, for example, have not brought desirable outcomes. This was probably caused by the gaps between the new paradigms and traditional notions.

Park's research (2002, p. 106) on these efforts by Korean firms to change the corporate culture found that their efforts were not successful, for several reasons, as follows:

> *i) inappropriate understanding of the concept of organisational culture, ii) lack of professional knowledge and skills among campaign managers, iii) hastiness in culture change movement, iv) failure in eliciting employees' interest and participation, v) lack of linkage between strategy and culture change efforts and vi) lack of linkage between culture change efforts and other business innovation activities.*

Recently, Korean firms have increasingly recognised that they must transform corporate cultures to maintain growth in the rapidly changing business environment. However, as Park (2002) argued, the culture transformation is closely linked with corporate strategy, other business innovation activities and the business environment. In sum, the success of Korean firms' culture change may depend on their efforts to better reconcile the environment with their strategy, structure and culture.

3.4.3. Ownership, Corporate Governance and Cross Shareholding

Ownership and management are not separated in most Korean business groups, including the GTCs. This results in management by the family, although the proportion of professional managers has been increasing steadily. As a result, top-down decision-making is common. The Korean business groups, *Chaebols*, are typified by a "one-person decision-making structure."

(Table 3.13. Insider Ownership of Major *Chaebols*) (Unit: %)

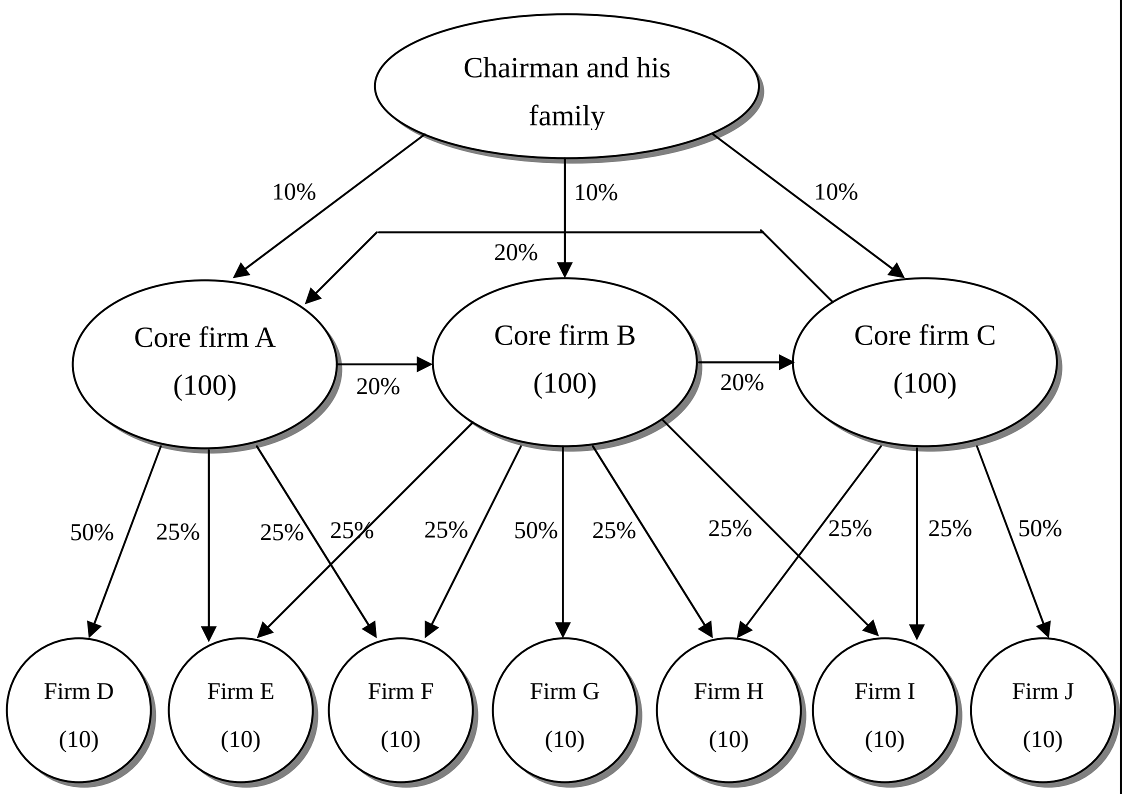
	2000				2002				2006			
	F	R	M.C	T	F	R	M.C	T	F	R	M.C	T
Samsung	0.60	1.21	41.38	43.19	0.45	1.54	38.03	40.02	0.29	0.56	48.52	49.37
Hyundai	0.92	2.87	36.00	39.79	0.99	0.63	26.20	27.82	0.82	1.36	16.96	19.14
LG	0.43	4.17	36.20	40.80	0.61	4.89	36.07	41.57	1.21	3.97	32.19	37.37
SK	3.13	1.21	51.56	55.90	2.51	0.70	51.60	54.81	0.71	0.34	60.32	61.37
Hanwha	3.35	0.84	40.09	44.28	2.96	0.77	45.98	49.71	1.91	0.61	39.02	41.54
Hyosung	6.94	9.08	18.99	35.01	7.16	11.20	22.43	40.79	7.00	16.57	24.76	48.33

(Source: Fair Trade Commission, 2008)
(Note: F (Founder), R (Relatives), M.C (Member companies), T (Total))

The *Chaebols'* owners and their families held, on average, only 5.79%, 5.73% and 5.89% of shares in 2000, 2002 and 2006 respectively (Fair Trade Commission, 2008). However, they exercised full power of control over group-wide management. This system, according to Jeong (2001), can be called “a controlling minority structure” with a low rate of shareholding of major shareholdings on their own, but a high rate of insider ownership.

Nonetheless, within the *Chaebols'* ownership structure a unique system of cross-shareholding exists. The following figure illustrates how a cross-shareholding scheme works to help *Chaebol* owners and their families, despite their small shares, to control the whole group. In the below example, a business group has three core companies, A, B and C, each with an equity of 100 billion won and smaller affiliates D,E,F,G,H,I and J with equity of 10 billion won each. The chairman and his family own only 10% each of the core companies of A, B and C. Thus, company A owns 20% of company B, company B owns 20% of company C and company C owns 20% of company A. As a result, the chairman effectively owns 30% of each of A, B and C; these stakes are sufficient to control each firm. Moreover, A owns 50% of D, 25% of E and 25% of F, while B owns 25% of E, F, H and I and 50% of G. In sum, the chairman and his family control all the group’s affiliates with a total investment of 30 billion won, although this is only 8.1% of the group’s total equity.

(Figure 3.5. An Illustration of Cross-Shareholding in Korean *Chaebols*)



- Numbers in parentheses are equity capital in billion Korean won.
- The core firm in the *Chaebol* is usually the GTC. For instance, Samsung Corp. (the GTC) is the core company of Samsung Group.
- Equity owned by *Chaebol* family is only 30 billion (8.1% of total equity) out of total equity capital of 370 billion.

(Source: Chang, S. J. (2003), "Financial Crisis and Transformation of Korean Business Groups: The Rise and Fall of *Chaebols*" Cambridge University Press, p. 166)

3.4.4. HRM

Under the influence of Confucian culture, the underlying corporate culture in Korean firms, to which workers were brought up from infancy, had been harmony-oriented. These cultural traits are reflected in HRM practice. Traditional Korean HRM is characterised by seniority-based rewards, mass recruitment of new graduates and lifetime employment (Rowley and Bae, 2004). Such traditional HRM policies were useful for the rapid growth of Korean firms in the 1960s and 1970s.

However, these traditional HRM practices lost their effectiveness, as they proved to be unfit for changing business environments due to globalisation; this requires internationally accepted labour standards (Kim and Kim, 2003). Furthermore, the financial crisis of 1997 also accelerated the pace at which Korean firms adopted new HRM practices, characterised as an efficient and flexible utilisation of human resources.

According to Rowley and Bae (2004), as one of the reconfiguration processes within the *Chaebol* groups, many ideas have been propounded in connection with HRM, for example, to reduce 'rigidities' and foster 'flexibilities.' They include the eradication of lifetime employment and seniority-based rewards, which helped to form the basis of the traditional HRM system[18].

- **Recruitment and Selection**

Traditional employee recruitment and selection in Korean firms used to be based on educational achievement and *yon-go* (personal) relations. In these, *Yon-go* relations play an important part in employment decisions; graduates of elite universities or applicants from certain regions are favoured over others (Chung, Lee and Jung, 1997). Big business groups pursue the mass recruitment of new college graduates twice every

[18] Rowley and Bae (2004) argued that lifetime employment and seniority-based rewards were once regarded as strengths within Korean organisations, but now they are viewed as weaknesses. For more details, see Rowley, C. and Bae, J. S., (2004), "Big Business in South Korea: The Reconfiguration Process", Asia Pacific Business Review, Vol. 10, No. 3/4, Spring/Summer, pp. 302~323

year through newspaper advertisements, TV commercials and school placement centres. Graduates from the top universities, such as Seoul National University, *Yonsei* University and Korea University are preferred.

However, these traditional recruitment patterns have changed from the mass recruitment of new graduates to recruitment on demand and from a generalist orientation to a specialist one (Rowley and Bae, 2004). Recent dynamic changes in the business environments have made varied demands and many Korean firms have adopted this new recruitment method.

Another feature of the new selection pattern is that experienced workers with special skills or expertise are preferred to new college graduates (Lee, 2005). In the past, most jobs were assigned or substitutes found internally according to the rigid organisational culture (Park and Noh, 2001). But as Korean businesses have expanded, large firms have also adopted more open and systematic recruitment methods. The *Chaebols* have recently increased the number of people recruited from abroad for both domestic and foreign deployment.

- **Training and Development**

According to the traditional training and development programme, once new employees become members of a company, they are put through an intensive training programme. Employee training and development have played an important role in Korea's economic success during the past four decades. The traditional training and development focused on the instillation of core management values such as harmony, teamwork and loyalty. The typical training and development methods practiced by Korean *Chaebols* are education-based training, new employee orientation, teamwork building, cultural indoctrination, and overseas training. Employee training and development programmes in most *Chaebols* are well organised and systematically designed, covering all functional areas, such as strategic management, marketing, production, accounting/finance, HRM and international trade. Korean *Chaebols* also have many special training programmes, for example in foreign languages, in-house MBA and overseas training. Employees can learn foreign languages, in particular English, Japanese and Chinese, in private language institutes after work with financial support from their companies (Chung, Lee and Jung, 1997).

With the increased emphasis on 'performance' in HRM, training and development is also under the influence of the current performance-based HRM trend. Noh, Kim and Kim (2002) asserted that many big business groups in Korea now consider training, developing and nurturing specialists with specific skills related to corporate strategies, rather than producing generalists. They operate training programmes which are planned to create a specialist pool, reflecting the organisation's vision and core competence. As a result, the new pattern of training and development increases the employability of workers and contributes to the improvement of employee satisfaction and firm performance for companies, by linking the purpose of training to corporate strategic goals.

- **Performance Appraisal and Compensation**

Most Korean firms have a formal system of performance evaluation and compensation. Performance evaluation is taken seriously because it relates to promotion and to wage increases, whereas in traditional systems for performance evaluation and compensation, seniority is more important for promotion than official performance appraisal. These systems also tend to be group-oriented rather than stressing individual differences in performance (Chung, Lee and Jung, 1997). With regard to compensation, the wage structure is composed of basic pay, allowances and bonuses. The basic pay consists of the starting wage, annual increments and the annual increase. The starting pay for graduates at any level is generally determined by the external market rate. The annual increment is determined by age, length of service and merit. The annual increase is usually determined by the increase in the cost of living (Lee, 1999).

Since the financial crisis, performance appraisal and compensation is the area in which the most significant changes have been taking place in Korean firms (2005, Lee). Traditionally, not much attention was paid to performance appraisal, as performance ratings hardly affected promotion and compensation decisions. However, Korean firms began to apply evaluation results directly to both employee development and compensation decisions. As a result, the overall direction of the change in the compensation system, once seniority-based, is now performance-based. For instance, in March 1999, Samsung SDI's labour and management agreed to implement a profit-sharing programme. During the 1999~2001 period, individual employees received profit-sharing bonuses every year roughly equal on average, to 20% of a year's salary (Kim and Bae, 2005).

However, according to Jung *et al* (2003), 56.6% of Korean firms still have a *Ho-Bong* system (wage table which reflects seniority) and the fixed wage determined by this system accounts for 65.7% in the total wage plan. This result implies that seniority is still one of the major factors in the compensation practice of Korean firms.

- **Transformation of HRM**

Some Korean *Chaebol* groups began to transform their HRM system before the economic crisis in 1997 (Bae, 1997). For instance, from 1994, LG Electronics adopted a merit-based HRM system which replaced the traditional seniority-based one (Kim and Bae, 2005).

But many radical structural changes within areas of Korean firms have arisen since 1997, HRM being no exception. Since then, many firms have recognised that human resources are a critical source of competitive advantage (Bae and Lawler, 2000).

The main direction of the changes in HRM has converged on ‘performance-based HRM’ (Lee, 2005). The following comparison table shows the key characteristics of pre-and post-financial crisis HRM within Korea’s big business groups.

(Table 3.14. Traditional and Newer Characteristics of HRM within Korean Big Business Groups)

Area	Traditional Characteristics	Newer Characteristics
Core Ideology	Organisation first, Collective equality and Community orientation	Individual respected, Individual equity and Market principle adopted
Human Resource Flow	Mass recruitment of new graduates, Job security (lifetime job) and Generalist oriented	Recruitment on demand, Job mobility (lifetime career) and Professional development
Work System	Tall structure, Line and staff and position-based	Flat structure, Team system and Qualification-based
Evaluation and Reward System	Seniority, Pay equality, No appraisal feedback and Single-rater appraisal	Ability/performance, Merit pay, Appraisal feedback and 360 degree appraisal
Employee Influence	Limited involvement and Restricted information sharing	Involvement of workers and Information sharing

(Source: Re-quoted from Rowley, C. and Bae, J. S., (2004), “Big Business in South Korea: The Reconfiguration Process”, Asia Pacific Business Review, Vol. 10, No. 3/4, Spring/Summer, p. 319, the original version: Rowley, C. and Bae, J. S., (2001), “The Impact of Globalisation on HRM: The Case of South Korea”, Journal of World Business, Vol. 36. No. 4, pp. 402~428)

However, Kwon’s research (2006) on recent changes in Korea’s business environment from a foreign perspective revealed that 63 foreign respondents were generally of the view that HRM in Korea had changed little. The average score on six types of possible change in HRM[19] was 2.730 on a five-point Lickert scale. Foreign respondents generally agreed that lifetime-employment practices were disappearing with a score of 3.156, whereas they disagreed that changes biased towards merit-based promotion and compensation (2.615), recruitment by merit (2.462) and disappearance of the seniority system (2.394), which were all rated below 2.700.

[19] The six types of possible change in HRM were i) disappearing lifetime employment, ii) increase in the lay-off of workers, iii) merit-based promotion and compensation, iv) willingness to hire foreign workers, v) recruitment by merit rather than by personal connections or university background and vi) disappearing seniority system.

Similar views were also suggested by Chen (2004); wages are generally based on seniority, but bonuses may be awarded on thee basis of performance in many Korean firms. Although a growing number of companies utilise the performance criterion in reward decisions, seniority still remains an important factor in most company decisions.

From the recent research on HRM within Korean firms, it can be inferred that although some HRM practices, such as lifetime employment, are disappearing, other conventional HRM practices are changing little and it will take more time for Korean firms to fully adopt internationally accepted HRM standards.

3.5. The Financial Performance of the Korean GTCs[20]

3.5.1. Sales Volumes

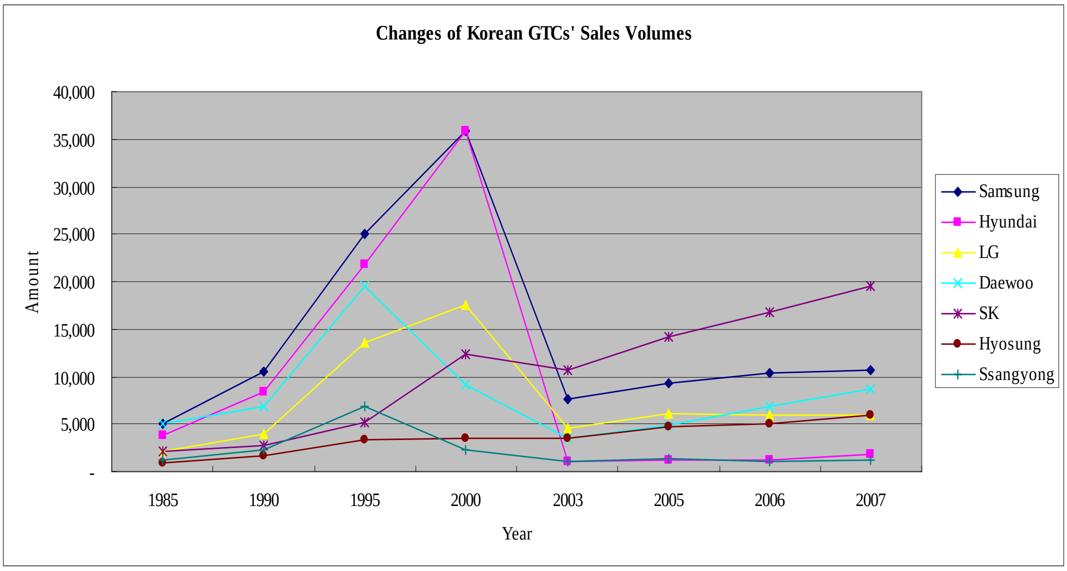
Korean GTCs have concentrated on quantitative growth since their formation, by putting their emphasis on sales volume in order to take a competitive advantage and capture shares in the market. They understood that sales volume was an important indicator to present their credit rating to the outside world. From 1985 to 1995, Korea's seven GTCs achieved constant growth in sales volume, thanks to the government's preferential treatment. In comparison with other industries, this allowed easy growth which was quantitatively aligned with the national economic growth policy, based on the export drive policy. Their quantitative growth was regarded as an important indicator to present their credit rating but an unjust way of gaining various privileges from the government; such as the extension of trade finance or credit limits from the bank and reduced or no import taxes for imported goods.

However, the GTCs' stable growth trend started to decline from 1997 and, since the national financial crisis in the same year, this situation has continued. The average value of the sales by the seven GTCs in 1985 was US$2,874million and in 1995 was US$13,627million. During this decade, they were able to maintain their constant growth, but have since shown a gradual decline. The fundamental reasons for this loss of sales volume can be summarised as: i) the disposal of non-profit business units and ii) the separation of inefficient business units in order to survive under the national economic depression and financial crisis.

[20] Most financial data in this part are summarised from "The Handbook of Korean GTCs" and each GTC's Annual Report.

(Figure 3.6. Changes of Korean GTCs' Sales Volumes)

(Unit: US$ million)



GTCs	1985	1990	1995	2000	2003	2005	2006	2007
Samsung	5,002	10,463	25,053	35,846	7,616	9,262	10,380	10,753
Hyundai	3,754	8,327	21,785	35,943	1,103	1,197	1,182	1,844
LG	2,140	3,960	13,595	17,498	4,544	6,134	5,951	5,924
Daewoo	4,973	6,902	19,550	9,119	3,482	4,932	6,811	8,637
SK	2,175	2,678	5,265	12,366	10,662	14,266	16,842	19,543
Hyosung	872	1,676	3,317	3,447	3,556	4,658	5,105	5,995
Ssangyong	1,206	2,309	6,824	2,219	1,012	1,415	999	1,161
Average	2,874	5,188	13,627	16,634	4,568	5,981	6,753	7,694

(Source: The Handbook of Korean GTCs (2005), Annual Report of Each GTC (2005, 2006 and 2007))

- Currency Conversion Rates: 1985: KRW760.00/US$, 1990: KRW760.00/US$, 1995: KRW768.53/US$, 2000: KRW1, 133.78/US$, 2003: KRW1,186.39/US$, 2005: KRW1,043.00/US$, 2006: KRW937.20/US$, 2007: KRW904.98/US$ (The Interactive Currency Table: http://www.xe.net)

- Simple intermediary businesses were excluded from 2003 because of the changing 'Accounting Standard'

Regarding Korean GTCs' sales structure, they, unlike the Japanese *Sogo Shoshas*, originally focused on exports only and have developed abnormally since their foundation. This caused the government's export-dive policy with a view to accelerating national economic growth. As a result, the sales structure of the Korean GTCs did not balance their exports, imports, domestic sales and offshore dealings properly, but mostly centred on exports. For example, in 1980, Korean GTCs' exports shared 88.2% out of total sales, imports shared 6.9%, domestic sales shared 4.6% and offshore dealings shared only 0.3%, while the Japanese *Sogo Shoshas'* exports shared 19.1%, imports shared 24.3%, domestic sales shared 46.4% and offshore dealings shared 10.2 % (Hur, 1983). However, the sales structure of Korean GTCs started gradually to diversify to imports, domestic sales and offshore dealings in their development stage. In 1992, for example, exports still shared 65%, but imports shared 29.1%, domestic sales shared 3.1% and offshore dealings shared 2.7%, while Japanese *Sogo Shoshas'* exports shared 13.8%, imports shared 16.4%, domestic sales shared 45.1% and offshore dealings shared 24.7 % respectively (Kim and Kim, 2000).

With respect to the major items composing Korean GTCs' sales, they are centralised to a few items, such as electrical and electronic equipment, industrial machinery and automobiles[21], while Japanese *Sogo Shoshas'* sales are well diversified with machinery and construction, fuel and chemicals, metals, foodstuffs and textiles. This has meant that Korean GTCs are heavily dependent on their affiliates' products. For example, Samsung Electronic Ltd. and LG Electronic Ltd. produce various kinds of electrical and electronic appliances and Hyundai Automobile Company produces automobiles. Then, the GTCs, such as the Samsung Corporation, the LG International Corporation and the Hyundai Corporation deal with the above items as their major products and act as the export agents of their affiliates.

[21] In 2001, these three items shared 75.4% of all Korean GTCs' dealings.

3.5.2. Profitability

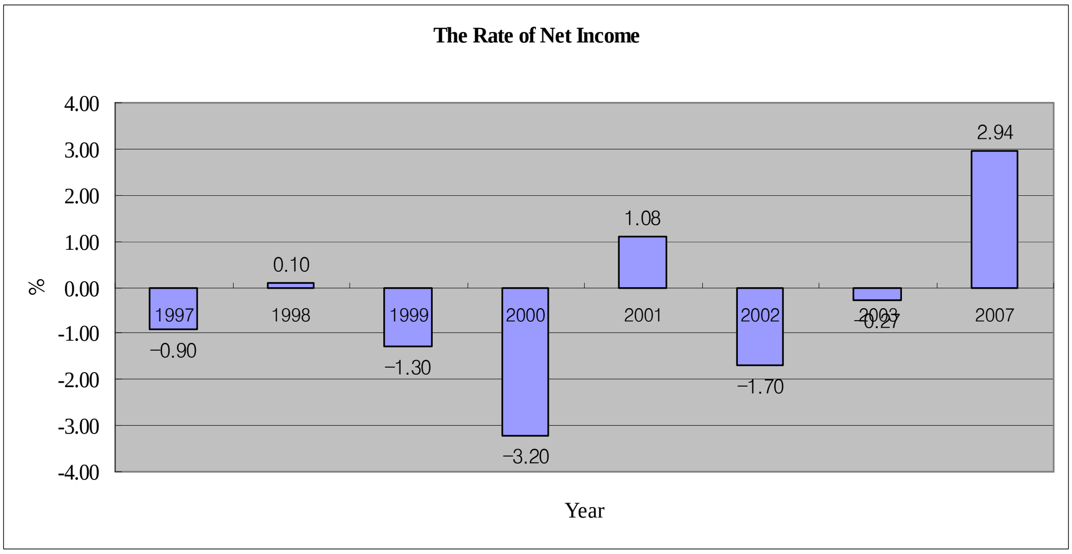
One notable feature of Korean GTCs' business is that profitability is significantly low in every sale. Their low profitability has probably resulted from the following factors. The first may be their deep dependence on intermediaries, or the simple broker function between sellers and buyers. The first earning source of GTCs is dependent on the function of their intermediaries. They obtained a commission fee for this function. The commission fee may occupy even now the largest part of the revenue earned by the GTCs. The Commission fee is usually decided between the GTCs and the confronting firms on the basis of numerous factors, such as types of product, quantity, final destination, quality of the products and the business relationship between two firms. The second is, on the surface, a purely technical accounting issue (Yamaji, 1991). In reality, the GTCs usually record as sales the trading amounts which they made for the tariff procedure in substitute for the manufacturing firms. Hence, the sales amounts of the GTCs do not always represent the real business activities. Unlike manufacturing companies, the GTCs' profitability is affected by numerous factors. Factors affecting the GTCs' profitability include the type of product and service, geographical diversification, ratio of export items manufactured by the GTCs group firms and affiliates and degree of domestic business operations.

In 2007, Korean GTCs achieved a gain of 2.94% of net income over revenues. But they showed a 3.20% deficit in 2000 and a 1.70% deficit in 2002 over revenue. These results denote that Korean GTCs have difficulty in achieving constant profitability. However, most GTCs have by restructured their organisations and changed their management strategies from quantitative growth to profit-based and cash flow-oriented businesses since the financial crisis. For example, Samsung Corporation and Daewoo

International Corporation adopted cash flow-oriented management as their management strategy and Hyundai Corporation and LG International Corporation focused on profit-based management.

(Table 3.15. Profitability of Korean GTCs in 2007) (Unit: US$ million)

Name of GTCs	Revenues	Gross Profit	**Net Income**
Samsung (Profit rate)	10,753	1,049 9.75%	**538** **5.01%**
Hyundai (Profit rate)	1,844	66 3.56%	**49** **2.63%**
LG (Profit rate)	5,924	65 1.09%	**53** **0.89%**
Daewoo (Profit rate)	8,637	102 1.18%	**96** **1.12%**
SK (Profit rate)	19,543	1,466 7.50%	**653** **3.34%**
Hyosung (Profit rate)	5,995	762 12.70%	**184** **3.07%**
Ssangyong (Profit rate)	1,161	54 4.64%	**11** **0.91%**
Average (Profit rate)	7,694	509 6.61%	**226** **2.94%**



(Source: Annual Report of each GTC, 2007)

- Currency Conversion Rates: KRW904.98/US$ (2007))

3.6. The GTCs, *Chaebols* and the Korean Economy

3.6.1. The Relationship between the GTCs and the *Chaebols*

One of the most significant measures taken by the Korean government in the export drive was the creation of the system of GTCs, which were the major source of the *Chaebols'* growth. Most Korean GTCs belonged to the *Chaebols* and they played a vital role in the operations of the *Chaebols*. It is essential to consider the *Chaebols* in order to understand Korean business and the country's economic growth. They featured a variety of distinctive characteristics, such as a family controlled business, dominance of the domestic economy, rapid expansion and diversification through close ties with the Korean government and financial institutions. It is, therefore, crucial to review the relations between the GTCs and the Korean *Chaebols* before examining Korean business and economic affairs.

In its Chinese character, the *Chaebol* is identical to the well-known Japanese *Zaibatsu* and is a combination of the character expressing "wealth" or "finance" and the character for "clique." The Japanese pronunciation of these two characters is *Zaibatsu*, which is defined as a system of highly centralised family control through holding companies. The word *Chaebol* is the only word which has migrated to Western countries from Korea, apart from *Kimchi*, a Korean dish made of vegetables. Both quickly became naturalised as words in the English language. In the academic arena, several definitions of *Chaebol* are available. For instance, Oh and Park (2001) defined it as "a resilient organisation that tries to retain its main characteristics of family ownership and control, centralised decision-making mechanism, highly diversified structures and highly complex network of subsidiaries and suppliers." Hattori (1986) suggested that there are two requisite dimensions inherent in the various conceptualisations of the *Chaebol*; ownership by family and diversified business operations. Other characteristics typically associated with the Korean *Chaebols* are i) quantum growth stemming from unrelated diversification, ii) a monopolistic position in the marketplace, iii) close relations with government, iv) a highly centralised structure with top-down decisions, v) low formalisation and standardisation, vi) flexible lifetime employment practice and vii) paternalistic leadership practices. Yoo and Lee (1987) also defined the *Chaebol* as a business group consisting of large companies which are owned and managed by family members or relatives in many diversified business areas. Thus, to be a *Chaebol* or a *Zaibatsu*, an organisation should satisfy two conditions: i) it should be owned by family members or relatives and ii) it should have diversified business operations.

Besides academic definitions, there are some technical definitions of the *Chaebol* for the purpose of policy regulation (Kang, 1996). Beginning in the early 1980s, the term *Chaebol* acquired technical connotations as the government decided to i) restrict big business groups' undisciplined expansion through interlocking and cross-shareholding structures and ii) control the growing concentration of bank credits in big business groups. To address these two major concerns over the *Chaebols'* activities, the government and the central bank defined the *Chaebol* as follows. First, the government defined a *Chaebol* in terms of combined total assets including those of its subsidiaries. The threshold level is 400 billion Korean won (equivalent to US $550 million). Second, the central bank defined the *Chaebol* in terms of combined bank credits (i.e. borrowings and guarantees). Business groups with combined bank credits in excess of 150 billion

Korean won (equivalent to about US $200 million) are ranked on the basis of combined total assets and the top 30 such groups are put on a credit control list.

(Table 3.16. The Top 30 Korean *Chaebols* in 2008) (Unit: US$ billion)

2008 Ranking	Biz. Groups	No. of Affiliate Firms	Assets	Equity	Debt	Debt – Equity Ratio (%)
1	Samsung	59	90.09	60.28	29.81	49.45
2	KEPCO	12	80.11	50.44	29.67	58.84
3	Hyundai Motor	36	50.75	25.85	24.90	96.31
4	SK	64	51.00	25.60	25.39	99.17
5	LG	36	40.64	23.19	17.46	75.29
6	KNHC	2	36.38	7.95	28.43	357.52
7	Lotte	46	30.28	20.46	9.81	47.96
8	KHC	4	27.62	14.93	12.69	85.00
9	POSCO	31	27.36	20.35	7.00	34.41
10	KLC	3	23.72	4.49	19.23	428.31
11	GS	57	22.09	9.56	12.53	131.09
12	Hyundai Heavy Ind.	9	21.22	7.36	13.86	188.35
13	KT	29	19.19	9.87	9.32	94.37
14	Kumho Asiana	52	18.72	6.63	12.09	182.51
15	Hanjin	27	18.71	6.81	11.89	174.52
16	Hanwha	40	11.70	4.69	7.01	149.36
17	Doosan	21	11.95	4.23	7.72	182.68
18	Hynix	8	10.67	6.45	4.21	65.30
19	KRC	15	10.32	5.90	4.42	74.87
20	KGC	3	9.02	2.76	6.26	226.30
21	STX	15	7.75	2.87	4.88	170.28
22	Shinsaegae	15	7.62	3.53	4.09	115.85
23	CJ	66	6.88	3.48	3.40	97.55
24	LS	24	6.80	3.25	3.55	109.35
25	Dongbu	29	5.97	1.80	4.17	231.50
26	Daelim	14	6.41	3.09	3.32	107.67
27	Hyundai	9	5.33	2.07	3.26	157.71
28	Daewoo Shipping	8	6.15	1.34	4.81	358.75
29	KCC	7	5.70	3.60	2.10	58.41
30	GM Daewoo	3	5.68	1.99	3.69	185.74
Top 30 Average		25	22.53	11.49	11.03	146.48

(Source: Fair Trade Commission, 2008)

- Currency Conversion Rates: KRW1,405.80/US$ (Average value of 2008)

3.6.2. The Evolution of the *Chaebols* and Korean Economy

i) 1945~1960: The Birth of the *Chaebols* with Primitive Accumulation of Wealth

The origin of some *Chaebols* is traced back to the late *Chosun* dynasty before Japan's annexation of Korea in 1910. However, many of the biggest *Chaebols* of today began their first ventures after Korea emerged from Japanese colonial occupation in 1945. Following Korea's independence, the Korean War (1950~1953) destroyed the entire industrial base of the country. War damage to industrial offices, plant and equipment, public facilities, private dwellings and transport equipment in South Korea cost approximately US$3billion. This was almost equal to the estimated Gross National Product (GNP) for 1952 and 1953 combined (Frank et al., 1975). After the war, the Rhee Sung Man government immediately made plans to rebuild the infrastructure and industrial facilities which had been destroyed. The reconstruction project after the Korean War was a good opportunity for some business groups to turn themselves into *Chaebols* by being involved in various projects, in particular in the product manufacturing sectors.

Although the post-war reconstruction project helped some business firms to gain wealth, the Rhee government's offer of political privileges to a small number of entrepreneurs was a decisive factor in their accumulation of wealth within a short period. The government's special policies for this privileged minority can be summarised as i) a preferential disposal of vested properties owned by the former Japanese and ii) a license to trade in imports and preferential access to bank loans and iii) the unfair allocation of aid funds and materials (Kang, 1996).

- ***Disposal of Vested Properties Owned by the Former Japanese***

Among the most important sources of the *Chaebols'* wealth in this period were the vested properties which had belonged to the Japanese during their colonisation of Korea (1910~1945). Frank *et al.* (1975) argued that the Korean economy became highly dependent upon Japan for capital, technology and management under colonial rule. Of the total authorised capital of business establishments in Korea, the Japanese owned approximately 94% in 1940. After Korea gained independence from Japan in 1945, Korea came to acquire 166,301 assets which had been Japanese possessions. These vested properties, which included 3,551 operating plants and firms, land, infrastructure and inventories, accounting for approximately 30% of the nation's total wealth – were first entrusted to the American Office of the Property Custodian (AOPC) and were later distributed to Koreans (Kang, 1996). By 1948 the AOPC had disposed of 2,268 items of vested properties, including 513 firms and 839 land items. The rest of the vested properties, which accounted for 21.6% of the total number of factories, 80% of the large corporations hiring more than 30 employees each and 59.6% of the nation-wide employees, were passed over to the Rhee government in August, 1948 and the distribution work continued until 1957 (Lee, 1995).

In the process of this disposal, a few entrepreneurs who had political connections with the Rhee government became beneficiaries. The disposal price was fixed at the pre-1945 book value, which was remarkably lower than the real value at the time and some items were disposed of at an even lower price than book value. Moreover, the government granted generous payment terms with a long grace period (15-year deferred payment of 90% of the total amount). Therefore, the beneficiaries could acquire properties with only 10% of their own capital. Given the hyperinflation of 600% between 1945 and 1950, it was nearly a free distribution.

- ***License of Import Trading and Preferential Access to Bank Loans***

After Rhee was elected as the president in 1948, he launched an import substitution policy. The government invested most of its aid funds in import substitution industries such as fibre, sugar, cement, flat glass and milling and these industries were completely protected by the government, with lower tax rates, interest and preferential finance. For instance, *Cheil* Textile and the *Cheil* Sugar Company, the predecessors of Samsung, founded by Lee, Byung Chul achieved remarkable profits and became emblems of success in the import substitution industries (Kim, 1998). To foster these industries, the government allowed only raw materials to be imported. At this time, the Korean won was not convertible to other currencies and the government allocated foreign currency paid as aid funds only to those who held import licenses. Thus, such import licenses from the government were an important source of profits. Any firm could apply for an import license, but the government allocated them mostly to those who had political linkage with the Rhee regime.

Moreover, there was a continuous shortage of finance in the 1950s due to the high inflation and the low interest rate policy. In this situation, any entrepreneur who acquired a bank loan was able to earn profit from the negative real interest rate[22]. During this period, the Ministry of Finance, according to macro-planning, determined the priorities in the allocation of industrial credit and bank loans. In this process, the

[22] The real interest rate between 1954 and 1957 was as follows: 1954: - 13.5%, 1955: - 43.8%, 1956: - 15.7% and 1957: - 3.9% (Lee, 1995).

Chaebols enjoyed a preferential allocation of bank loans and industrial credit, a situation which reached its peak in 1956 (Lee, 1995).

- ***Government's Unfair Allocation of Aid Funds and Materials***

In addition to the government's allocation of vested properties to a small number of privileged capitalists, the Rhee government's unfair allocation of aid funds and materials was also one of the easiest ways of accumulating wealth. Since the volume of Korean exports in the 1950s was small, Korea acquired foreign exchange, which was needed for imports, mainly from the inflow of foreign aid from the US and the United Nations (UN). During 1945~1965, the US and the UN provided economic aid worth US$3.8billion to the Korean government.

Acquiring such aid funds and material from the government was at the time an important element in turning a few private entrepreneurs into *Chaebols*, because Korea had a severe shortage of material and capital in the 1950s. When the government began to allocate foreign aid, the beneficiaries of these funds were able to build plants or manufacturing facilities using only 15%~25% of their own capital. However, many of those entrepreneurs who made enormous profits from the government's unfair allocation of foreign aid and material were accused by the Park regime in 1961 of acquiring wealth unlawfully from this preferential treatment (Kang, 1996).

ii) The 1960s: The Consolidation Period with Economic Development Plans of Park's Military Regime

Korea's rapid economic growth began after the launch of the military government headed by Park, Chung Hee. He was a general who succeeded in a military coup d'état on 16th May, 1961. The Park government's primary concerns were to stabilise the people's livelihood through developing the economy and strengthening the national security, following the tragedy of a civil war (1950~1953) which destroyed two-thirds of Korea's productive capacity and killed almost a million civilians. After Park's inauguration, the government, to ensure Park's political legitimacy, immediately concentrated on the national economic development as its priority.

- ***Preparation of a Foundation for Driving Economic Development***

In order to achieve the ambitious goal of national economic growth, the centralisation of power became Park's primary political concern and he resolutely took the following measures to achieve it. First, the government established the Economic Planning Board (EPB) to reinforce centralisation in policy making and granted the EPB absolute power not only in planning and budgeting but also in inspection and mediation of other government administrative organs. Second, the military government carried out financial reform. It established the National Agricultural Cooperative Federation to enhance the social and economic status of member farmers and founded a small and medium-sized Industrial Bank to promote the growth of SMEs. In particular, the government planned to invite foreign capital through the Korea Development Bank for the sake of national economic development.

The government also made it clear that it would use the BOK as a financial resource to safeguard any deficit in the process of economic development. Third, the government tried to make take over some commercial banks through the redemption of the shares of heavy shareholders (the *Chaebols*). Through such a reform of administrative structure, the military government prepared a foundation on which to execute mighty policies for economic development.

- ***Treatment of Illicit Wealth Accumulators***

Another issue which the Park government faced was to meet the public demand that illegal wealth accumulators under the Rhee government should be punished. To this end, the government arrested some entrepreneurs, including Lee, Byung Chul, the founder of Samsung Group and the best-known entrepreneur at the time, together with government and military officials who were accused of illicit wealth accumulation under the Rhee government. After Lee's arrest, he had an opportunity to negotiate with Park over three things. First, the government was to lift the restriction, stipulated in the anti-corruption law, on the movement of the accused businessmen, by protecting their right to free movement. Second, the fine for their illicit accumulation of wealth was to be adjusted significantly downwards. Last, in exchange for this adjustment, the entire adjusted fine would be invested in key industries. The government had only to identify the key industries and the businessmen would be free to coordinate the division of the resources according to their specific capabilities, in order to get the key industries going. (Lim, 2002)

Park realised soon after the meeting that it was essential to cooperate with the *Chaebol* owners if it wanted to achieve its ambitious goal of national economic growth. As part of Lee's proposal, Park modified the restrictions to the *Chaebol* owners, for example, extending the deadline for paying the fine and reducing the amount of the fine to almost half the original amount (from 8,312 million hwan[23] to 4,228 million hwan) (Shim, 2002).

(Table 3.17. Convictions by the Park Regime for Illicit Wealth Accumulation)

(Unit: Million hwan)

Founder and Business Group	Amount of Fine		Reasons for Fine			
	Planned	Adjusted	Tax Evasion	Kickback	Property-related Scandal	Others
Lee (Samsung)	2,400	800	736	64	-	-
Chung (Samho)	1,000	361	349	102	66	-
Lee (Gaepung)	550	387	125	153	109	-
Seol (Daehan)	330	481	272	39	62	108
Lee (Tongyang)	170	128	-	40	-	88
Kim (Goldstar)	240	143	119	24	-	-
Park (Hwashin)	97	10	-	10	-	-
Koo (Lucky)	-	96	96	-	-	-
Kim (Samyang)	-	36	36	-	-	-
Lee (Dongah)	400	211	201	10	-	-
Other 20s	3,125	1,575				
Total	8,312	4,228				

(Source: Shim, J.S. (2002), "The Evolution of the Korean Economic System", PhD Dissertation, The School of Public Policy, The University of Birmingham, p.124)

After laying a foundation for the nation's economic development and an appropriate compromise with the *Chaebols*, the government launched the first Five-Year Economic Development Plan in 1962. During this period, the *Chaebols* were able to build up huge amounts of capital by playing a major part in implementing the government-led policies for economic development.

The following seven factors enabled the *Chaebols* to achieve rapid quantitative expansion and diversification. First, Park's lifting of the restrictions on the *Chaebol*

[23] The currency unit "hwan" was used between 1953 and 1962 before the Park government's currency reform to "won"

owners allowed them to develop rapidly and become major players in Korea's industrialisation. Through this decision, the *Chaebols* were able, through joining various projects, to achieve quantitative expansion and diversification during the first Five-year Economic Development Plan (1962~1966) and the second (1967~1971). The released *Chaebol* owners formed the Economic Development Promotion Committee (it later became the Federation of Korea Industries (FKI), which still exists), which selected 6 key industries: synthetic fibre, cement, electricity, chemical fertilizer and steel and oil refining. They concentrated on these industries with strategic financial support from the government. Between the government and the FKI, a communication system was established. The FKI regularly reported their processing of projects and made requests to the government. The government mostly accepted the FKI's requests and used their suggestions as footholds in the government's policy decision-making. In an interview with *Sisa*-Journal (7th May, 1992), Jung, Ju Young, the former chairman of the Hyundai group, said, "the government selected most industrial policies in consultation with the *Chaebols*." Second, the government's special favours accelerated the *Chaebols'* capital accumulation. The *Chaebols* were given incentives such as the preferential allocation of resources, bank loans with lower interest rates and priority in the allocation of foreign capital. The *Chaebols* could borrow money at a 5~6% interest rate when the domestic interest rate was 25~30%. Third, the government also supported the *Chaebols* with various measures in taxation and tariffs to promote the country's exports. The government's preferential financing policy to export firms enabled the *Chaebols* to become export-oriented firms. Fourth, the *Chaebols* accumulated capital through a profit monopoly in the incomplete market of their underdeveloped country. Fifth, special procurements took place due to the Vietnam War. This war let the *Chaebols* accumulate foreign capital in particular in the transportation and construction industries

(Lee, 1995). Domestically, the construction industry was prosperous due to the expansion of social overhead capital. Sixth, the *Chaebols* were able to make extraordinary profits from the rapid rise of real estate caused by high inflation. Last, the geopolitical environment for Korea at the time was also favourable. The US provided it with significant aid and Japan also loaned it funds after they re-established a diplomatic relationship in 1965. The government thereupon set up ambitious targets and allocated foreign loans for investment (Chang, 2003)

iii) The 1970s: The Expansion Period for Heavy and Chemical Industries and the Formation of the GTCs

There were two impetuses in the early 1970s for the accelerated growth of Korean *Chaebols*. One was the government's policy emphasis on heavy and chemical industries and the other was the establishment of the GTC system in 1975 using the Japanese *Sogo Shosha* as a model in order to expand Korean exports worldwide and achieve economic internationalisation after the oil crisis in 1973.

- ***Emphasis on Heavy and Chemical Industries***

During the third Five-year Economic Development Plan (1972~1976), Park's government tended to achieve economies of scale. It therefore focused on a small number of the *Chaebols* with preferential financial assistance and designated heavy and chemical industries (steel, petrochemicals, machinery and shipbuilding) as "strategic industries". From 1975 to 1979, the Korean government allocated 70% of its economic development funds to these industries. According to Chang (2003), the Korean government allocated licenses to only a few *Chaebols* in order to achieve economies of scale. For instance, Hyundai and Daewoo were chosen to develop power plant facilities and Hyundai, Samsung and Daewoo to build ships. As a result, from 1971 to 1979, the proportion of heavy equipment and chemical industries to total manufacturing shipments increased from 39% to 55% while the proportion of exports to GNP increased from 16% to 36%.

During this period, the government encouraged large-scale projects through planning and subsidisation (Kang, 1996). Thus, there was fierce competition in the private sector to participate in these projects. As a result, large corporations were able to grow rapidly as the main beneficiaries of projects planned by the government, whereas SMEs remained unaffected by them. In these circumstances the *Chaebols* undertook to achieve unprecedented expansion and focused on borrowing money in order to do so. In this process, the *Chaebols* gained the disgraceful nickname of “Octopus Legs”[24] (Kim, 1998)

- ***Formation of the General Trading Companies***

In addition to the emphasis on heavy and chemical industries, the government also began to sponsor the creation of the GTC system in order to devote its total strength to exports. Korean GTCs, modelled on the Japanese *Sogo Shosha,* were officially launched in 1975.

[24] This denotes that the *Chaebols* recklessly diversified their businesses into all industries and areas. As octopuses spread out their many tentacles in search of food, so the *Chaebols* expanded their businesses into all areas in order to make more profit. This earned them their shameful nickname.

In the initial stage after establishing the GTC system, the primary roles of the GTCs were i) to expand national exports, in particular heavy and chemical products, ii) to enter into new markets, iii) to provide a more rational export channel for Korean SMEs, iv) to increase the size of exporters in order to achieve economies of scale and v) to shift some of the burden of export assistance from the government to the *Chaebols* (Chung, 2000). To tell the truth, the GTCs devoted themselves to the economic growth of Korea after their formation and their export performance was impressive. For instance, the GTCs' share of all Korea's exports increased from 12.4% in 1975 to 41.0% in 1980 (Handbook of Korean GTCs, 2005).

(Table 3.18. The Amount of Exports made by the GTCs) (Unit: US$ million)

	1975	1976	1977	1978	1979	1980
Samsung	205	333	390	493	772	1,237
Ssangyong	106	101	117	264	422	642
Kukje	64	194	297	472	564	744
Hyosung	36	106	153	338	584	764
Bando (LG)	31	134	199	330	469	493
SK	52	107	176	283	322	430
Hyundai	-	-	323	260	493	1,028
Koryo	10	17	24	31	51	67
GTCs Total (a)	671	1,329	2,177	3,434	5,102	7,177
Korea Total (b)	5,427	8,115	10,046	12,711	15,055	17,505
a/b (%)	12.4	16.4	21.6	27.0	33.9	41.0

(Source: Lee, S.H (1986), "The Role of the Korean GTCs as an Export-Window for the Korean Economy", The Department of International Trade, *Kyoungbook* National University Press, Korea, p. 37)

iv) The 1980s: The Structural Adjustment Period with Diversification and Entry into Financial Sectors

The 1980s in Korea began with a military coup d'état by Chun, Doo Whan, just like the previous president's, Park, Chung Hee. Park was assassinated by his close associate Kim Jae Kyu, the Director of the Central Intelligence Agency in 1979. Upon its inauguration, Chun government proposed economic policies which were very different from those of the preceding regime. The government, first, enacted the Anti-Trust and Fair Trade Act in 1980, to monitor collusion and unfair behaviour by firms. Second, it set up the Fair Trade Commission which was to be supervised by the EPB in 1981. Third, it introduced the Consumers' Protection Law. Last, as Shim (2002) noted, the government introduced import liberalisation and tariff reduction in order not only to improve the *Chaebols'* structure but also to raise their competitiveness in the world market. However, the external environment also constrained the Korean economy. According to Woo (1991, p. 57):

> *"The IMF and the World Bank pressured the Korean government to reduce government expenditures, tighten the money supply and pursue economic stability. Korea, at that time, was one of the largest foreign debtors and the international financial community were concerned about its financial health. Furthermore, because of its economic success, Korea became a target of US trade wars. Faced with pressure from the US, the government had to open up its barriers to imports and foreign direct investment"*

The changes in the internal and external environment, such as the government's several attempts to regulate the *Chaebols*, as advised by the international financial community and the pressure from the US made the *Chaebols* adjust their structure as follows.

- ***Qualitative Growth through Diversification***

Unlike the 1970s, the *Chaebols* emphasised qualitative growth in the 1980s rather than visible quantitative expansion. Although the *Chaebols* also achieved remarkable quantitative growth in the 1980s, it was crucial for them to seek qualitative growth because the Korean economic structure was becoming mature. There was little change in the number of the *Chaebols'* affiliated companies in the 1980s, although the 1970s had shown a remarkable increase. For instance, there was only a 10% increase in the number of top 10 *Chaebols'* affiliated companies from 242 in 1980 to 266 in 1987. The *Chaebols* attempted to diversify through expanding business areas within the existing affiliated companies, rather than through increasing the number of affiliated firms. During this period, the *Chaebols* exerted themselves in high-tech industry, producing such things as semiconductors, new materials, precision instruments, fine chemicals, computers, aero and space engineering and telecommunications. As a result, Research and Development (R&D) expenses for these high-tech industries increased dramatically from US$109 million in 1980 to US$2,463 million in 1990 (FKI).

- ***Foray into the Financial Sectors***

The government in 1980 began financial liberalisation and started privatising banks which had been owned by the government for the past two decades. Then the *Chaebols* enlarged their business to financial sectors and their share in the commercial banks increased. Although the *Chaebols* were forbidden to own more than 8% of any one bank's shares[25], it was enough to give them influence in the banks' decision-making.

Moreover, the *Chaebols* diversified their business in non-banking financial institutions (the so-called second-tier financial sector) such as insurance, securities, short- or medium-term financing and investment trusts. As Kang (1996) argued, the *Chaebols* which owned non-bank financial institutions used them not only as an

[25] This was to prevent the *Chaebols* from ever becoming as formidable as the pre-World War II *Zaibatsu* of Japan, which owned both financial institutions and industrial enterprises (Shim, 2002).

effective means by which to mobilise funds but also as an effective means by which to expand the *Chaebol* structure by circumventing government regulations.

(Table 3. 19. The *Chaebols'* Ownership of Commercial Banks in 1997) (Unit: %)

Bank		Hyundai	Samsung	Daewoo	LG	SK	Top 5 Chaebols
Nationwide Commercial Bank	Choheung	1.24	3.05				4.29
	Commercial	0.97	6.91				7.88
	Cheil	0.16	0.18		0.19		0.53
	Hanil	2.73	4.90		2.48		10.11
	Foreign Exchange		1.24			0.44	1.68
	Kookmin	2.02	0.96	0.42	0.40	0.48	4.28
	Shinhan	0.42	3.49				3.91
	Koram		18.56	18.56			37.12
	Hana		3.61				3.61
	Boram		1.16	0.21	7.57	0.24	9.18
	Korea Peace	0.37	1.28	0.82	0.73	0.92	4.12
	Housing		0.55				0.55
Regional Bank	Daeku		5.30				5.30
	Pusan		1.31				1.31
	Cheju		2.17				2.17
	Chunpuk		1.50				1.50
	Kangwon	11.89	1.54		0.63		14.06
	Kyungnam		2.68				2.68
	Chungbuk		0.92				0.92
Government-owned Bank	Long-term Credit	0.12	5.31		1.82	0.67	7.92

(Source: Ministry of Finance and Economy, Korea)

- ***The Three Lows***

Besides the *Chaebols'* diversification and their infiltration into the financial sector, the changing external environment in the 1980s also promoted their growth. First, due to an appreciation of the Japanese yen against the US dollar after the Plaza Accord[26] in

[26] This was an agreement signed on 9th September, 1985 in the Plaza Hotel, New York, US, to increase the value of the Japanese yen. An agreement reached by the United Kingdom, France, Germany, Japan and the US to drive down the price of the dollar. By 1985, the dollar had reached an all-time high relative to

1985, Korean products competed against Japanese products, including TVs, VCRs, chemicals, cars, ships and steel, and they remained internationally competitive in the world market *(the low US Dollar)*. Second, the low oil prices, due to an international economic downturn, were favourable to the *Chaebols'* growth *(the low oil price)*. Last, the low interest rate was also one of the important elements in the *Chaebols'* growth *(low interest rate)*. Thanks to these three lows, Korea achieved a trade surplus of US $4.6billion in 1986 (Lim, 2002) and the *Chaebols* were able to gain international competitiveness with their products in the world market.

v) 1990~1996: The Liberalisation and Globalisation Period of a Widening Domestic Market and Foreign Direct Investment

Until 1985, the Korean government had been lukewarm about the execution of an import liberalisation policy, even though it had prudentially debated this as part of economic liberalisation since early in the 1980s. However the rapid changing international environment forced Korea to open its trade and capital markets. For instance, Korea's surplus in the international balance of payments attributed to the Three Lows (low US dollar, low oil price and low interest rate)[27] and a trade surplus with the US from 1986 pressured the Korean government to put the import liberalisation policy into operation (Ministry of Finance and Economy (MIFE)). At this, the Roh

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many major currencies and the US was experiencing a large trade deficit. The coordinated efforts by these countries resulted in a 30 percent decline in the dollar over the next two years. With this agreement, the exchange rate of the Japanese yen to the US dollar in January, 1988 was adjusted 260 to 1 (JPY260/US$1) and the rate was decreased (i.e. the value of the Japanese yen increased) 127 to 1 (JPY127/US$1).

[27] The late 1980s were the most prosperous days in Korean history. Due to the Three Lows, the Korean economy achieved an annual average growth of 12.8% from 1986 to 1988. Between 1986 and 1987, it recorded US$10 billion of trade surplus. Moreover, Korea improved its position in the international market by holding the Asian Games in 1986 and the Olympic Games in 1988 (MIFE)

government rapidly put the policy into action by drastically reducing the import restriction items and simplifying import procedures with confidence, having the Three Lows on his side. However, many economists criticised the Roh government's execution of the import liberalisation policy before eliminating the Three Highs (high prices for commodities, high wages and the high price of land), which impaired Korea's international competitiveness, tended to damage the national economy and was taken by the *Chaebols* as unpatriotic. Although the *Chaebols* were discontented with the government's policy, they had to try to seize any business opportunity that was created by the import liberalisations.

In contrast, Roh Tae Woo, who became the 13th Korean president with only 30% of the lower political support ratio in the presidential election, tried to capture the support of the middle class to ensure his political legitimacy (Lee, 1999). To do so, the government enforced a strong policy of restricting the *Chaebols'* economic centralisation by prohibiting mutual investment and cross payment guarantees between or within affiliated companies[28], the strengthening of fair trade, control of credit and the disposal of non-commercial real estates. However, due to the Roh government's impetuous decision to liberalise imports liberalisation and strict regulation of the *Chaebols*, the Korean economy promptly plunged in 1989[29] with a record US$2billion deficit in international payments and receipts in 1990 (BOK).

[28] Cross payment guarantee: When one firm borrows money from a financial institution, another firm guarantees its payment if the former becomes is insolvent. Under this system, the *Chaebols* were able to maintain their scale through payment guarantees from their affiliated companies. However, this system interferes with the withdrawal of insolvent enterprises from the market and causes a series of bankruptcies once one firm becomes insolvent.

[29] In 1989 Korea's annual economic growth crashed to 6.5% from an annual average growth of 12.8% from 1986 to 1988. Additionally, the market share of Korean products in the US decreased to 3% in 1993.

In Kim Young Sam's inauguration speech in 1992 as the 14^{th} president, he proclaimed thorough political and economic reforms without exception under the motto of "New Korea Construction". As a part of its political reform, Kim's government eradicated the corruption and illegality of former politicians and broke the power of the military, which had dominated Korea politically and economically for the past 30 years. In this process, the previous presidents Chun and Roh were imprisoned for building up slush funds during their years of office. In connection with economic and *Chaebol* issues, the Kim government enforced the Real-name Financial Transaction System[30] to block various financial abuses caused by transactions under unregistered or assumed names. It also executed political revenge on Jung Ju Young, the chairman of the Hyundai group who had fought against Kim during the presidential election in 1992. Approximately 100 of Hyundai's employees and executives were accused in 1993 of violating the election law.

In the early stage of Kim's government, it achieved a surplus both in the trade balance and international payments and receipts. However, the Korean economy began to decline after 1994, mainly due to the crash in the price of semiconductors, Korea's major export item[31] and the *Chaebols'* overlapping investment in the same industries (BOK). In these circumstances Kim tried to overcome the national economic slump and

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[30] In August 1993, the Kim government enforced the Real-name Financial Transaction system. Previously, individuals or enterprises in Korea made many financial transactions such as opening bank accounts, transferring money or investment in securities under unregistered or assumed names. This enabled the *Chaebols* to maintain closer ties with the government by supporting these huge amounts of illicit funds in unregistered or assumed names.

[31] Korea recorded a deficit of US$4.5 billion in 1994, US$8.9 billion in 1995 and US$23.7 billion in 1996 in international payments and receipts. The semiconductor price also slumped from US$50 to US$4 during this period (BOK).

to recover his plunging political support ratio through lifting various regulations on the *Chaebols* which involved half of the national economy. As a first step, Kim declared the Globalisation Plan for Korea in the meeting of Asia Pacific Economic Cooperation (APEC) in 1994 and provided a base for the *Chaebols* to achieve quantitative growth. As Stephan and Mo (1999) noted, the Korean Development Bank increased loans to the *Chaebols* by 26.1% in 1994 and by 24% in 1995. Consequently, the *Chaebols'* investment in the manufacturing sector significantly increased and it reached a 38.5% annual growth rate between 1994 and 1996. However, the *Chaebols'* excessive overlapping investment, in particular their debts in car manufacture, petrochemicals, steel and electronics worsened their financial structure. Moreover, the government's impatient opening of financial and capital markets to foreign countries without enough preparation led Korea to face the financial crisis of 1997.

- ***Increasing of Foreign Direct Investment***

During this period, the *Chaebol* began large-scale Foreign Direct Investment (FDI) to overseas markets by raising huge loans from both the domestic and international capital markets. The history of Korean FDI has been rather short. It began in 1968 with a forestry development project in Indonesia. From 1968, the modest growth of FDI continued until 1986, when Korea's first balance of payments surplus was achieved (Sakong, 1993). However, since the middle of the 1980s, when Korea first experienced double-digit economic growth, its investment has significantly increased. For instance, Korea's outward investment increased 62.4% to US$5.8 billion in 1997 from US$3.5 billion in 1994. Among many *Chaebols*, Daewoo was the most active participant in the

FDI. It built motor and electronics manufacturing facilities in foreign countries including Poland, Rumania, India, Vietnam and Sudan.

(Table 3.20. Korea's FDI by Destination) (Unit: US$ thousand)

	1994	1995	1996	1997	Cumulative Share (%)
Southeast Asia	1,684,920	2,455,389	3,076,893	2,483,018	44.4
Middle East	164,904	3,591	41,462	49,323	2.97
Europe	638,676	705,754	1,322,526	1,046,463	15.8
North America	824,820	1,438,949	1,195,755	1,207,973	25.77
Latin America	96,208	246,179	421,578	627,805	6.0
Africa	132,186	20,448	37,325	184,201	2.0
Oceania	39,368	78,227	122,448	220,399	3.13
Total	3,581,081	4,948,537	6,217,986	5,819,181	100

(Source: MIFE, Various Years)

At this time, the *Chaebols* were free to issue bonds and stocks (Chang, 2002) and were able to raise funds in overseas markets on their own credit without a payment guarantee from the government. Banks also became free to borrow short-term money from international money markets. Thereby, the foreign supplies of funds to Korean enterprises and financial institutions rapidly increased and these enabled the *Chaebols'* to participate in the FDI. Moreover, the excessive competition among existing *Chaebols* also stimulated FDI. However, the *Chaebols'* excessive borrowing in overseas markets and the high competition between them became one of the most important causes of their collapse.

- ***Emergence of Derivative Chaebols***

In the 1990s, many new derivative *Chaebols* were born. For instance, the Halla, Kumkang and Sungwoo Groups branched off from the Hyundai Group and Hansol and

Shinsegae came from the Samsung Group. In the course of the spin-off, ownership passed down to the second and third generation of the founders. Although the new owners of derivative *Chaebols* achieved visible quantitative growth with aggressive diversification before long, some new *Chaebols* brought collapse upon themselves because they mainly relied upon imprudent borrowed monies from international capital markets. For example, Chang Jin Ho, a son of the Jinro group's founder, led the group to bankruptcy through irrational diversification of its business to construction, distribution and electricity rather than investing in its core business of liquor manufacturing. Kirk (2000) argued that its figures were the worst of any *Chaebol*. With assets totalling KRW3.8 trillion, it had shareholders' equity of KRW99 billion for a ratio of debt to equity of an astonishing 40 to 1. Jinro's collapse was only the start. Followed by Jinro, Sammi, Haitai and Newcore, Daenong and Halla went into insolvency file by file. As a result, 16 *Chaebols* out of the top 30 Korean business groups suffered the most disgraceful fate in their group's entire history through bankruptcy and legal management. After the collapse of the minor groups, the gap between the Big Three (Samsung, LG and SK) and the minor *Chaebols* steadily widened. For instance, the Big Three in 2000 achieved a net profit of KRW11 trillion whereas the 30 minor *Chaebols* recorded a deficit of KRW8 trillion (Dong-A Daily Newspaper, 2001).

3.6.3. The *Chaebols* and Korean Financial Crisis

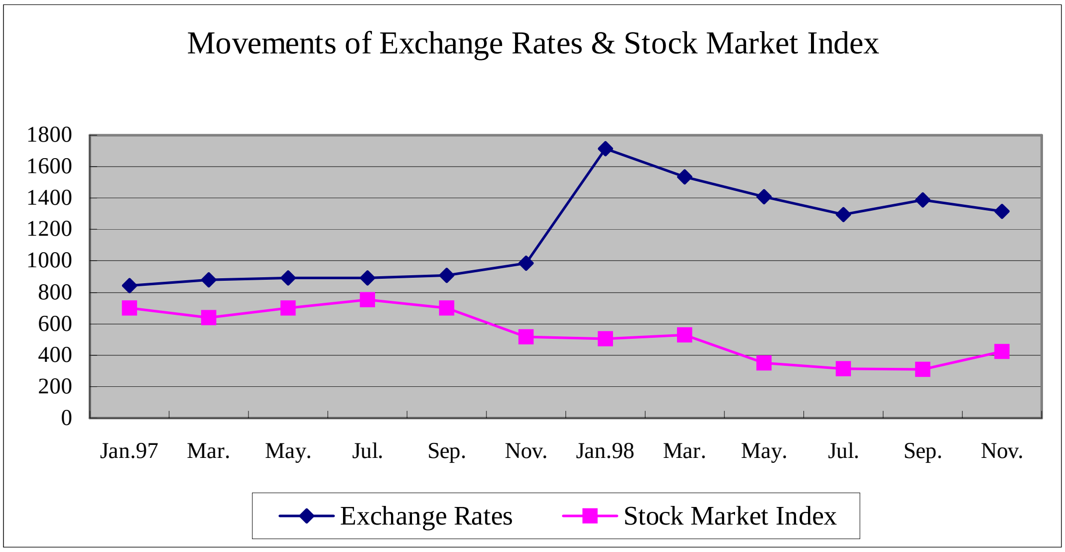
Before the financial crisis in the late 1990s, many countries had paid keen attention to the miraculous economic success of certain East Asian countries, such as Korea, Indonesia, Singapore, Malaysia and Thailand. However, the great Asian crisis which hit the major East-South Asian industrial countries between 1997 and 1998 was already a record, notwithstanding what was to come. According to the Financial Times (1998), Thailand's economy was expected to shrink by between 5% and 8% in 1998 whereas Indonesia's national income was likely to fall by 12~13% in the same year. Krugman (1998) stressed in Fortune Magazine that Asia was nowhere near having hit bottom; even when the region's currencies seemed to have stopped plunging for the moment, its real economies were getting weaker, not stronger. Hong Kong announced that its economy had shrunk by 2.8% in the first quarter of 1998, its worst recession since World War II. Economists predicted that Indonesia's Gross Domestic Product (GDP) would fall an astonishing 15.1% in 1998. And it turned out that Japan's bad bank debt was not US$550 billion, as previously reported, but the immense sum of US$1 trillion.

Every crisis may be unique and each country within a region may have unique factors that no other country in crisis has. However, one can find some common factors and a logic of development to explain why the Asian financial crisis developed as it did. Lee (1998) argued that the common factors involved in the development of Asian crisis were; i) excessive short-term borrowing in international markets, ii) misallocation of investment, in particular in speculative real estate, iii) weak domestic financial systems, iv) irrational pessimism or herd mentality, v) relatively small economies exposed to disruptive international market forces, vi) government guarantees of loans, vii) excessive rapid financial liberalisation without a commensurate strengthening of regulation and supervision and viii) lack of transparency and inaccurate information.

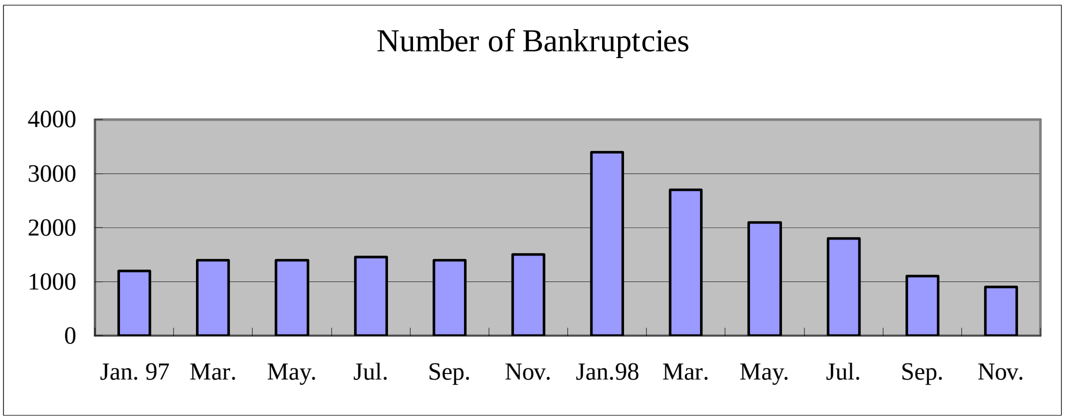
The crisis began in Korea with a surprise announcement by the government in late 1997 that the country was having financial problems and required support from outside.

This announcement plunged Korea's economy into great chaos. Foreign exchange rates soared from 848 Korean won per US dollar (KRW848/US$1) in January 1997 to 1,715 Korean won per dollar (KRW1,715/US$1) by January 1998. The Korean stock exchange index tumbled from 699 in January 1997 to 310 in September, 1998 and the number of Korean companies going bankrupt increased from 1,000 per month to 3,500 per month (BOK).

(Figure 3.7. Movements of Exchange Rates and Stock Market Index and Number of Bankruptcies)



(Source: Korea Stock Exchange)



(Source: BOK)

The Korean financial crisis was the product of a combination of accumulated economic structural problems and several short-term trigger factors. One of the major causes of the crisis was *Chaebols'* excessive investment and over-expansion, called *Dae Ma Bul Sa*[32]; a Big Horse Never Dies. Steers (1999) argued that there were several common characteristics among Korea's most successful business leaders during the 1970s and 1980s. They are as follows: i) clear-cut vision and goals, ii) considerable foresight, iii) strong ambition, iv) rapid decision-making and implementation, v) commitment to the national interest and vi) communal spirit. However, regardless of these abilities, Korean *Chaebols* seldom succeed on their own in any culture; they require outside support and opportunities through close ties with government and banks. The close ties between the *Chaebols*, the government and the financial institutions enabled the *Chaebols* to pursue their "*Dae Ma Bul Sa*" policy. Due to this, loans and investments were determined not by decisions on the economic profitability of businesses, but rather by favouritism and short-sighted executive decisions. In many instances, Korean *Chaebols* simply made poor decisions (Shim and Steers, 2001). For instance, the decision by both Samsung and Ssangyong to build luxury passenger cars in a market that was already glutted was based more on the whims of corporate leaders than on any real need for or competence in such automobiles. Short-sighted executive decisions based on limited financial and strategic analyses led both companies to the brink of bankruptcy with mounting debts and excess production capacity.

[32] In Chinese characters, *Dae Ma Bul Sa*, denotes " a big horse never dies". It is close to the English phrase "too big to fail." This consensus among the *Chaebols* surged in the three decades before the financial crisis in 1997. Under this policy, most *Chaebols* focused on external growth through closer ties with the government and financial institutions. However, after the bankruptcies of some *Chaebols*, such as Hanbo, Jinro, Kia, Daewoo and Dongah, the consensus began to fade.

Lee (1998) argued that Korean government has been a major navigator in the credit allocation to certain industries and even to particular companies. The Korean government has held its power over big businesses (i.e. the *Chaebols*) by maintaining permission and license rights and other complex regulations. The allocation of resources became increasingly distorted in favour of the *Chaebols*, while the financial sector remained underdeveloped and heavily influenced by government and political decisions rather than market forces. This created symbiotic relations between the government and the *Chaebols* and as the *Chaebols* got bigger and bigger, it became increasingly hard for the government to stop intervening in the market whenever a particular *Chaebol* got into financial trouble. This relationship created the myth that Korean *Chaebols* were "*Dae Ma Bul Sa*". The Western press (The Economist, 1998 and Business Week, 1998) and the financial community (IMF, 1998) blamed the *Chaebols* for being the main culprits of the Korean crisis. The Economist (1998) said that the excesses of Korea's conglomerates had helped to bring its economy to near-collapse. The IMF's assessment (1998, p.1) also identified as the root cause of the crisis in the unholy alliance of the debt-ridden *Chaebols* with financial institutions. It said;

> *"In 1994~1996, Korean conglomerates undertook an aggressive investment drive financed by large increases in borrowing from domestic banks, which, in turn, sharply increased short-term external borrowing. During 1997, an unprecedented number of highly leveraged conglomerates went into bankruptcy as the build-up in capacity proved unviable owing to the depreciation of the yen, a sharply adverse movement in Korea's terms of trade and the slowing of domestic demand in 1996. The bankruptcies resulted in a severe deterioration in the balance sheets of Korean financial institutions"*

Korea's high performing exports in the 1990s were led by semiconductors, steel, automobiles, petrochemicals and shipbuilding. The *Chaebols* in these industries enormously expanded production and investment and as a result their financial structure weakened. The *Chaebols* also increased their investment in foreign countries. Financed by foreign credit, the *Chaebol's* investment, mostly in Southeast Asia and Europe, expanded by 33% in 1995 and 36% in 1996. With these over-borrowings by the *Chaebols*, the external liabilities of domestic firms amounted to US$35.6billion, of which US$22 billion was short-term at the end of 1996. The external liabilities of domestic firms increased to US$42.3 billion (US$24.7 billion short-term) by the end of 1997 (Fair Trade Commission).

(Table 3. 21. Total External Liabilities of Korea) (Unit: US$ billion)

		1994	1995	1996	1997
Mid- and Long-term External Debt	Financial Institutions	13.9	19.6	27.7	50.4
	Private Firms	9.0	10.5	***13.6***	***17.6***
	Public Sector	3.6	3.0	2.4	18.0
	Sub-Total	26.5	33.1	43.7	86.0
Short-term External Debt	Financial Institutions	19.4	29.7	39.9	43.8
	Private and Non Financial Sector	11.0	15.6	***22.0***	***24.7***
	Sub-Total	30.4	45.3	61.0	67.4
Total External Debt		56.9	78.4	104.7	154.4

(Source: Fair Trade Commission)

3.6.4. The Restructuring of *Chaebols* and Korea's Economic Reforms

After the Korean government applied for emergency funds from the IMF, the guidelines imposed by the IMF and the World Bank greatly influenced the Korean government's subsequent restructuring policies. The IMF rescue loans were not without price. The IMF's conditions for financial support ranged from macroeconomic policy frameworks to structural policies including both financial and corporate sector reforms.

According to article 32 and 37 of the agreement contracted between the Korean government and the IMF, the IMF required the Korean government to implement the followings things. First, the IMF demanded liberalisation of foreign investment in the Korean equity market by increasing the ceiling on aggregate ownership from 26% to 50% by the end of 1997 and to 55% by the end of 1998. Second, the IMF demanded an improvement in corporate governance structures, that the government should adopt international accounting principles to enhance the transparency of the Korean accounting system. Third, the IMF ordered no government interference with banks' business operation and lending decisions. Fourth, the IMF demanded a reduction of debt levels among Korean firms. Fifth, the IMF demanded changing to the system of mutual guarantees within *Chaebols* to reduce the risk which these guarantees entail (IMF, 1997).

The government's response to the crisis, which embraced the restructuring of the government, corporate sector and financial sector, was swift and impressive in its depth and extent.

- **Corporate Sector Reform (*Chaebol* Reform)**

Corporate restructuring was the most urgently needed move, deemed formidable by domestic as well as international economic specialists, given the tight relations of the government with the *Chaebols* and their powerful position in the Korean economy.

The *Chaebols* have been always at the core of the economic problem. Thus, unless the *Chaebols* are reformed, the Korean economy can hardly be restored to international competitiveness. For this reason, Kim's government immediately followed the IMF demands to streamline the *Chaebols'* ever-expanding businesses, acknowledging that they had been principally to blame for the nation's economic crisis (Lee, 2000).

As a means of restructuring the *Chaebols'*, financial restructuring and business reforms were recommended. Financial restructuring has focused on five main reforms: i) reducing debt-equity ratios to less than 200%, ii) eliminating cross-debt guarantees among their affiliates, iii) improving management accountability, iv) enhancing management transparency and v) improving smaller *Chaebols'* financial structures through corporate workout programmes (Chang, 2003; Lee, 2000). The government has stipulated that the five rules are pivotal in any full recovery from the country's economic crisis and that they will be a platform for transforming the corporations into globally competitive firms.

Under the government-led corporate restructuring plan, substantial progress was made in reducing bloated corporate debts. During this period, the top five *Chaebols* reduced their average debt-equity ratios from 477.9% in 1997 to 329.5% in 1998 and 144.9% in 1997. In 2008, the ratio was finally reduced to 80.06%, which is a significant trend over the past ten years (Fair Trade Commission). The following statistics show the dramatic reduction of debt-equity ratios over a short period.

(Table 3. 22. Changes in the Debt-Equity Ratios of the Top Five *Chaebols*)

- 1997

	Hyundai	Samsung	LG	Daewoo	SK	Average
Debt-Equity Ratios (%)	576.6	370.4	504.7	469.2	468.6	**477.9**
Number of Affiliates	62	61	52	37	45	51

- 1998

	Hyundai	Samsung	LG	Daewoo	SK	Average
Debt-Equity Ratios (%)	484.0	252.6	316.5	353.8	240.4	**329.5**
Number of Affiliates	57	62	48	36	41	49

- 1999

	Hyundai	Samsung	LG	Daewoo	SK	Average
Debt-Equity Ratios (%)	152.0	146.0	147.8	Bankrupt	133.7	**144.9**
Number of Affiliates	35	45	43		39	41

- 2008

	Hyundai	Samsung	LG	Daewoo	SK	Average
Debt-Equity Ratios (%)	96.31	49.45	75.29	Bankrupt	99.17	**80.06**
Number of Affiliates	36	59	36		64	49

(Source: Fair Trade Commission)

- **Big Five Reform**

The president Dae Jung Kim convened a meeting with the heads of the top five *Chaebols* (Hyundai, Samsung, LG, Daewoo and SK) on January 13, 1998, to come to an agreement on “Five Principles” of corporate restructuring: i) enhancing the transparency of corporate management, ii) clearing cross-debt guarantees and cross-ownership, iii) improving the corporate financial structure, iv) focusing on core competent businesses and encouraging cooperation among businesses regardless of their size and v) tightening the control on major shareholders' accountability (Kim, 2003).

Furthermore, from September, 1998, the government implemented the "Big Deal Programme" in seven major industries, namely, oil refining, semiconductors, railroad vehicle, aerospace, power generation equipment, ship engine and petrochemicals.

(Table 3. 23. Big Deals Programme in Industries)

Industry	Big Deal Programme	Date of Completion
Oil Refining	Hyundai Oil Co. took over Hanwha Energy Co.	June, 1999
Semiconductor	Hyundai Electronics Co. took over LG Semiconductor Co.	July, 1999
Railroad Vehicles	Hyundai Precision and Industries Co., Daewoo Heavy Industries Co. and Hanjin Heavy Industries Co. were unified into one company	July, 1999
Aerospace	Samsung Aerospace Industries Co., Daewoo Heavy Industries Co. and Hyundai Space and Aircraft Co. were unified into one company	October, 1999
Power Generation Equipment	Korea Heavy Industries Co. took over Samsung Heavy Industries Co. and Hyundai Heavy Industries Co.	November, 1999
Ship Engines	Korea Heavy Industries Co. took over Samsung Heavy Industries Co.	November, 1999
Petrochemicals	The Merger and Acquisition plan between Samsung Chemical Co. and Hyundai Petrochemical Co. failed due to the failure of hosting foreign capitals	

(Source: Jeong, J. I. (2006), "*Yaehwanwegi Ehoo Giupgujojojeongwe Tooja mit Goyongae Michin Younghyang* (A Study of the effect of the Korean Firms' Restructuring Programme on Investment and Employment after the Financial Crisis, Press Release Report, The Bank of Korea, p. 5)

The purpose of this programme was to reduce dual investment within the same industry and to enhance international competitiveness. The programme began with the mutual agreement between the *Chaebol* groups and their creditor banks; six industries out of seven successfully completed the programme by the end of November, 1999 (Jeong, 2006).

As a result of unprecedented corporate restructuring, Korea was praised by the IMF and the World Bank as an exemplary model of successful reform. With a remarkable turnaround in one and a half years, Korea's vulnerability to external factors seemed to improve greatly: the government strengthened the institutional framework for regulating *Chaebols'* activities as well as controlling reform processes and financial conditions and the corporate structure of the *Chaebols* also improved.

- **Financial Sector Reform**

In addition to the reform of the *Chaebols*, the financial sector also had to be restructured. No matter how difficult or how long it would take, restructuring had to be done under market mechanisms between financial institutions and business firms (Lee, 2000).

Before the crisis, Korea's financial institutions were vassals of the authorities and acted as the private cashbox of the *Chaebols*. It was the creditor banks that Kim's administration used to implement the reform of the *Chaebols*. In 1998, the government required the *Chaebols* to sign the "Capital Structure Improvement Agreements" with their main creditor banks. But this policy was doomed from the start to fail, in particular vis-à-vis the chief *Chaebols* such as Hyundai and Daewoo. The creditor banks were themselves in serious trouble and they were the targets of Kim's other reform, financial sector restructuring (Lim, 2003).

According to the Committee of Public Fund Management, an affiliated firm of the Ministry of Finance and Economy (2008), from November 1997, the government started to channel public funds to the financial sector, including commercial banks and second-tier financial institutes such as merchant banks, security firms, insurance firms, trust banks and savings banks. At the end of October 2006, the total public funding infused into the financial sector was KRW168.5 trillion (equivalent to about US$147,081 million).

The government transferred public funds in various ways. For instance, the government transferred a total KRW86.9 trillion (equivalent to about US$75,808 million) to banks in the following ways; investment KRW34 trillion (equivalent to about US$29,660 million), donations KRW13.9 trillion (equivalent to about US$12,126 million), purchasing of assets KRW14.4 trillion (equivalent to about US$12,562 million) and the purchase of bad loans KRW24.6 trillion (equivalent to about US$21,460 million). This helped the financially sound commercial banks to exceed the "Banks for International Settlement (BIS)" ratios of 10%, which is the international standard.

(Table 3. 24. Infusion of Public Funds to the Financial Sector: November, 1997 ~ October, 2006)

(Unit: KRW trillion)

		Investment	Donation	Paying Deposits (on behalf of)	Purchase of Assets	Purchase of Bad Loans	Grand Total
Bank		**34.0 (U$29,660m)**	**13.9 (U$12,126m)**	-	**14.4 (U$12,562m)**	**24.6 (U$21,460m)**	**86.9 (U$75,808m)**
The Second-tier Financial Institutions.	Merchant Bank	2.7 (U$2,355m)	0.7 (U$611m)	18.3 (U$15,964m)	-	1.5 (U$1,309m)	23.2 (U$20,239m)
	Security	10.9 (U$9,509m)	0.3 (U$262m)	0.01 (U$9m)	1.9 (U$1,657m)	8.5 (U$7,415m)	21.6 (U$18,852m)
	Insurance	15.9 (U$13,871m)	3.1 (U$2,704m)	-	0.3 (U$262m)	1.8 (U$1,570m)	21.2 (U$18,407m)
	Trust Bank	-	-	4.8 (U$4,187m)	-	-	4.8 (U$4,187m)
	Saving Bank	-	0.4 (U$349m)	7.3 (U$6,368m)	0.6 (U$523m)	0.2 (U$174m)	8.4 (U$7,415m)
	Sub-total	29.5 (U$25,735m)	4.6 (U$4,013m)	30.3 (U$26,433m)	2.9 (U$2,530m)	12.0 (U$10,468m)	79.3 (U$69,178m)
Financial Institutes located in Foreign Countries		-	-	-	-	2.4 (U$2,094m)	2.4 (U$2,094m)
Grand Total		63.5 (U$55,395m)	18.5 (U$16,139m)	30.3 (U$26,433m)	17.3 (U$15,092m)	39.0 (U$34,022m)	**168.5 (U$147,081m)**

(Source: The Committee of Public Fund Management, Ministry of Finance and Economy, 2008)

- Currency Conversion Rates: KRW1,146.31/US$ (Average values from 1997 to 2006)

3.7. Conclusion and Discussion

This chapter examined the nature of Korean GTCs, the *Chaebols* and their impact on Korea’s national economic development. Indeed, the Korean GTCs – the growth engines of the Korean *Chaebols*, with a number of unique characteristics and a variety of functions – played an important part in the process of national economic growth.

In the process of Korea’s national economic development, mention of the Korean GTCs is inevitable. Since the early 1960s, exports have been a primary growth engine for the Korean economy. During this period, the GTCs have complied quite successfully with the Korean government's goal of achieving rapid export growth. The reason for their success is that most of them were functioning as trading firms when they were appointed as GTCs. Thus, they had already accumulated substantial know-how and experience in export operations.

The initial goal of the Korean government was to develop the GTCs as giant enterprises pursuing economies of scale with highly diversified products and services in the world market. Since their foundation, Korean GTCs have met the government's specification and, as a result, they have enjoyed a great reputation, receiving various preferential treatment from the government. Despite their devotion to the national economic growth for the past three decades, however, they together with their parent companies, the *Chaebols*, have been criticised as a cause of the national economic crisis which occurred in 1997.

The national economic crisis in 1997 was a turning point for most Korean big business groups, including the GTCs. In particular, many *Chaebol* groups undertook organisational reconstruction in accordance with the guidelines imposed by the government. The GTCs were no exception. External and internal conditions also threatened the GTCs future business. In view of their situation, now is the right time for the GTCs to retrieve their reputation through strategic management, including effective decision-making.

CHAPTER 4. THE *SOGO SHOSHAS* AND THE JAPANESE ECONOMY

4.1. Introduction

This chapter aims to investigate the nature of the Japanese *Sogo Shoshas* and their impact on Japan's national economy. First, it reviews the history and development of the *Sogo Shoshas*. Second, the present *Sogo Shoshas* in Japan will be reviewed. This section will investigate their strategies, major business areas, financial performance, the number of their employees and the number of their overseas branch offices. Third, it reviews the management system within the Japanese *Sogo Shoshas*, such as the organisational structure, corporate culture, the decision-making process, ownership/corporate governance and human resource management. Fourth, the *Sogo Shoshas'* recent financial performance, for example, their revenues, profitability and stability, will be reviewed. Last, it studies the relationship between the *Zaibatsu*, *Keiretsu*, *Sogo Shoshas* and the Japanese economy.

4.2. The History and Development of the *Sogo Shoshas*[33]

The origin of the *Sogo Shosha* dated back to the early days of the Meiji Era (1868~1912)[34], when Japan was about to transform itself from an aging feudal state to a

[33] This part is summarised from "The Handbook of Japanese *Sogo Shoshas*, 2005"

[34] The Meiji period denotes the 45-year reign of the Meiji Emperor, running from 8 September 1868 to 30 July 1912. During this time, Japan started its modernisation and rose to world power status. It was a time of rapid modernisation and Westernisation. Feudal domains were abolished and replaced with prefectures; daimyo and samurai were relieved of their special privileges. To secure a strong central government, a national army was formed and universal conscription was enacted. A new agricultural tax was instituted to finance the new government and a decimal currency was introduced. Eager to encourage economic growth, the government aided the textile industry, established railways and shipping lines and founded an ironworks industry. Education was also reformed and compulsory coeducational elementary schools were introduced. Economic reforms included a unified modern currency based on the yen, banking,

modern nation. With the change from the Edo period to the Meiji era in 1868, Japan started to enter international markets. Before this time, Japan had been closed to the outside world for nearly 200 years, because there had been no merchants with experience in international trade. In those two centuries, Japanese goods were traded through foreign merchants; thus, trading was often disadvantageous to the Japanese (Yoshihara, 1987). The European traders first reached Japan toward the beginning of the 17th century. The East India Companies of the Dutch and the British arrived in Japan in 1609 and 1613 respectively. By the second half of the 19th century, European traders dominated Japan's import market. In order to protect the national economy from Western invasion, Japanese government policy makers and business people recognised the need for Japan to organise its own trade.

Competing with Western traders was not easy, but with the blessing and active assistance of the government, Japan's first trading firms found ways to improve their competitive skills. One of the main strategies employed was to concentrate trading functions in a limited number of specialised companies. Major business interests, such as Mitsui and Mitsubishi, established specialised trading houses to master the techniques of international trade and by so doing fulfilled one of the most important tasks of the time, namely the importing of modern technology, plants and equipment in order to raise Japan's profile as a modern industrial state. To compete with foreign

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commercial and tax laws, stock exchanges and a communications network. Establishing a modern institutional framework conducive to an advanced capitalist economy took time but was completed by the 1890s. By this time, the government had largely relinquished direct control of the modernisation process, primarily for budgetary reasons. The government was initially involved in economic modernisation, providing a number of "model factories" to ease the transition to the modern period. After the first twenty years of the Meiji period, the industrial economy expanded rapidly until about 1920 with inputs of advanced Western technology and large private investments. Stimulated by wars and through cautious economic planning, Japan emerged from World War I as a major industrial nation. After the death of the Meiji Emperor in 1912, the Taisho Emperor took the throne, thus beginning the Taisho Period (Japan Reference, 2006).

merchants, trading companies had to be large in scale. Government assistance and protection were offered to willing merchants. Therefore, the Meiji government encouraged the traditional *Zaibatsu* (large Japanese conglomerates controlled by powerful families) to participate in founding trading companies. Three *Zaibatsus* complied with the government's offer. They were Mitsui, C.Itoh and Suzuki Shoten. They established trading companies in 1876, 1872 and 1877 respectively. The result was entirely satisfactory to the government. By 1918, the three companies had captured 80 percent of Japan's total import volume. With the support of the government, these *Zaibatsus* organised vertical and horizontal combinations of companies, including banking, marketing and manufacturing. Control of these conglomerate-style business groups resulted in family ownership of firms through holding companies. Some of the companies concentrated on one or a few sectors, such as textiles, metals, or mining: others, such as Mitsui and Mitsubishi, expanded to include a variety of industries and activities. These *Zaibatsus* dominated Japanese industry and the finance sector until World War II.

However, after World War II, the *Zaibatsu* were dissolved through anti-monopoly legislation. In 1946, holding companies were declared illegal by the Allied Occupation Authorities as incompatible with a free market economy. The *Zaibatsu* were required to dissolve their ownership in their holding companies. This produced a great number of specialised trading companies, such as Marubeni, Tomen, Nissho-Iwai and Nichimen. The dissolution of the *Zaibatsu* was halted in 1949 and the Korean War in 1959 gave the *Zaibatsu* great opportunities for re-grouping and re-growth. Specialised trading companies and *Zaibatsu* type trading companies were naturally transformed into the contemporary *Sogo Shosha*.

Cho (1987) and Murofushi (1998) analysed the evolutionary process of *Sogo Shoshas* after World War II in terms of function, as follows:

i) The 1950s (Period of Growth):

The Korean War revealed Japanese trading companies' vulnerability to sudden changes in the external economic environment and confirmed the importance for their future of widely-based internationalisation. Continued stagnation in the trade sector forced the Japanese government to contemplate public support programmes. The result was the implementation of various government subsidies for Japanese trading companies in 1953. Active government support programmes helped the *Sogo Shoshas* to rationalise their traditional operations and to increase their product range (Cho, 1987).

ii) The 1960s (Period of Decline):

Due to the manufacturing firms' direct participation in trading, as well as diseconomies of scale resulting from too diversified product ranges, the *Sogo Shoshas* experienced a sharp decline as trading institutions. To stop this decline becoming permanent, the *Sogo Shoshas* searched for a new function. Mitsui and Mitsubishi are examples of functional diversification (Cho, 1987).

iii) The 1970s (Period of Criticism):

There was, first, a slowdown in the rate of growth of the Japanese economy. Second, there was a shift in the economic and industrial structure of Japan. Third, export activities after the fluctuation of currencies in 1971 made exports less predictable. Increased competition among the *Sogo Shoshas* fuelled inflation in Japan. As a result, they became the subject of public criticism (Cho, 1987).

iv) The 1980s (Period of Uncertainty):

Small and medium sized companies and technology-intensive industries in Japan started gaining direct access to financial institutions and international markets, effectively undermining the traditional role of the *Sogo Shoshas*. Many, though not all, changed their strategic decisions by emphasising third-country trade, foreign direct investment and investment in research and development (Cho, 1987).

v) The 1990s (Period of Management Reform for Globalisation):

The *Sogo Shoshas* came to grips with the task of reforming their management structure. They shared the agenda items of giving the company a constitution which would ensure profits even at times of low growth, building a management system adapted to the hyper-information society and globalisation and refining their capabilities and functions (Murofushi, 1998).

4.3. The Present *Sogo Shoshas* in Japan[35]

4.3.1. Mitsui and Co., Ltd.

Mitsui Group is one of the largest corporate conglomerates (*Keiretsu*) in Japan and one of the largest publicly traded companies in the world. It was founded by Takatoshi Mitsui (1622–1694), who was the second son of a shopkeeper in Matsuzaka. His father originally sold miso, a fermented soybean paste and ran a pawn shop. Later, the family built a second shop in Edo (now called Tokyo). Takatoshi moved to Tokyo when he was 14 years old and was later joined by his elder brother. He had shown outstanding business talent even when very young. But his brother's jealousy sent him back to Mie

[35] This part is summarised from various data such as Company Brochures, Annual Reports, Internet Websites and "The Handbook of Japanese *Sogo Shoshas*"

when he was 28 years old. He waited for 24 years until his older brother died before he could take over Echigoya. He opened a new branch in 1673; a large gofukuya (kimono shop) in Nihombashi, a district in the heart of Tokyo. Later the Gofukuya division separated from Mitsui and is now called Mitsukoshi. In 1683, Takatoshi opened a money exchange in Tokyo. Soon the shop began providing dry goods to the government of the city of Edo. At the time, the Edo authorities had struck a business deal with Osaka that it could pay its land tax by selling crops and other materials. The money was then sent to Edo – but moving money was dangerous in feudal Japan. The “exchange shop” facilitated transfers without the risk. In July, 1876, the Mitsui Bank, Japan’s first private bank, was founded, with Takashi Masuda (1848 -1938) as president. The Mitsui Bank, which after a merger with the Taiyo-Kobe Bank in the mid-1980s became part of Sakura Bank, survives as part of the Sumitomo Mitsui Banking Corporation. The group currently associated with the Mitsui family includes Mitsui and Co. Ltd., Mitsui Construction Co., Mitsui engineering and Shipbuilding Co., Mitsui Mining and Smelting Co., Mitsui Mining Co., Mitsui OSK Lines Ltd. and Mitsui Petrochemical Industries Ltd.

Within the Mitsui Group, Mitsui and Co. Ltd. is the *Sogo Shosha*, which was established in 1947 under its original name of Daiichi Bussan with a capitalisation of JPY195,000 and 37 employees. In 1949 it was listed on the Tokyo Stock Exchange and throughout the 1950s contributed significantly to Japan’s postwar economic recovery through its advances into foreign trade. In 1959, the Company integrated with other trading companies and changed its name to Mitsui and Co., Ltd. It now has almost 6,000 employees and a total of 158 branch offices around the world.

In 2007, its revenue was US$99,367 million, gross profit was US$1,857 million and net income was US$1,033 million. Its major stockholders are the Master Trust Bank of Japan, Japan Trustee Services Bank, Mitsui Life Insurance Company, Sumitomo Mitsui Banking Corporation, The Chuo Mitsui Trust and Banking Company, State Street Bank and Trust Company and Nippon Life Insurance Co., Ltd.

The Company's main businesses include sales, manufacturing, exports/imports and international trade and services in the following fields: metal products and minerals, machinery, electronics and information, chemicals, energy, consumer products and services (retail), foods, textiles and fashion, general merchandise and various services, financial markets and logistics and transportation. Mitsui Co., Ltd. is also diversifying services, exploring and developing natural resources, making commercial investments, developing technologies in new businesses and much more.

With respect to its medium-term management plan and management philosophy, the Company adopted in 2004 a new medium-term management outlook for the next three to five years. The key elements of the approach outlined in the new plan are i) building a business portfolio which meets the needs of customers and of society, ii) leveraging business engineering across the Group and optimising the allocation of resources and iii) prioritising the development of human resources. The table below shows the Company's management philosophy.

(Table 4.1. Mitsui and Co., Ltd.'s Management Philosophy)

Name of the *Sogo Shosha*	Management Philosophy	Promoting Strategies
Mitsui and Co., Ltd.	Portfolio Strategy	● Selection and concentration ● Reorganisation of business units (old and new business units) ● Investments in strategic areas (core areas: mineral, energy and plant project, key area: foods and retail business, lifestyle related business and motor and vehicle related business) ● Reallocation of human resources (reallocation within Mitsui group and among business units)
	Value Chain Strategy	● Optimise value chain ● Value chain integration among upstream, middle stream and downstream
	Human Resource Policy	• Cultivating the next generation of global executives and leaders • Offering managerial training opportunities • Development of regional human resources

(Source: Annual Report of Mitsui and Co., Ltd. and The Handbook of Japanese *Sogo Shoshas*)

4.3.2. Mitsubishi Corporation

The Mitsubishi Group, Mitsubishi Group of Companies, or Mitsubishi Companies, all refer to a large grouping of independently operated Japanese companies which share the Mitsubishi brand name. While the companies are autonomous, they share the brand name and trademark, as well as a common legacy. The first Mitsubishi company was a shipping firm which Yataro Iwasaki established in 1870. In 1873 it took the name Mitsubishi Shokai. The name Mitsubishi has two parts: "mitsu" means "three" and "bishi" means "water chestnut" and hence "rhombus", which is reflected in the company's logo. Another translation is "three diamonds". The company bought into coal mining in 1881 by acquiring the Takashima mine, using the produce to fuel their extensive steamship fleet. They also diversified into shipbuilding, banking, insurance, warehousing and trade. Later diversification carried the organisation into such sectors as paper, steel, glass, electrical equipment, aircraft, oil and real estate. Mitsubishi's broadly based conglomerate played a central role in the modernisation of Japanese industry. At the start of the 20th century the company, which by itself accounted for over half of the Japanese merchant fleet, entered into a period of diversification that would eventually result in the creation of three entities: a) Mitsubishi Bank (now a part of the Mitsubishi UFJ Financial Group. After its mergers with the Bank of Tokyo in 1996 and UFJ Holdings in 2004, this became Japan's largest bank, b) Mitsubishi Corporation (founded in 1950, Japan's largest *Sogo Shosha*) and c) Mitsubishi Heavy Industries.

Within the Mitsubishi Group, Mitsbishi Corporation is the *Sogo Shosha*, which was established in 1950. It now has almost 5,500 employees and 123 branch offices around the world. In 2007, its revenue was US$94,861 million, gross profit was US$1,666 million and net income was US$1,570 million. Its major stockholders are the Master Trust Bank of Japan, Japan Trustee Services Bank, Tokyo Marine and Nichido Fire Insurance Co., Ltd., Meiji Yasuda Life Insurance Company, Mitsubishi Heavy Industries, State Street Bank and Trust Company, the Bank of Tokyo-Mitsubishi UFJ, the Chase Manhattan Bank and the Nomura Trust and Banking Co., Ltd.

Mitsubishi Corporation is involved in a broad and diverse range of businesses. These include domestic and overseas transactions of products in the fields of energy, metals, machinery, chemicals and living-essentials. The Company also provides diverse types of business services in the areas of information, financing, logistics and others, while investing in business projects on a global scale. With respect to its medium-term management plan and management philosophy, Mitsubishi Corporation announced its plan, “Innovation 2007: opening up a new era”. The main goal of this plan was numerical targets and investment plans.

(Table 4.2. Mitsubishi Corporation’s Management Philosophy)

Name of the *Sogo Shosha*	Management Philosophy	Promoting Strategies
Mitsubishi Corporation	Strengthen Core Business	● Natural resource development (gas, crude oil, metal) ● Financial services ● Automobile operations ● Foods
	Develop Human Assets	● Motivate employees and enhance their business sensitivity ● Nurture and retain human resources ● Revise personnel evaluation system (performance-based evaluation)
	Portfolio Management	● Selection and concentration strategy ● Low risk and medium return strategy
	E-commerce Strategy	● Establishment of business model integrating IT (information technology), FT (financial technology), LT (logistics technology), MT (marketing technology)

(Source: Annual Report of Mitsubishi Corporation and The Handbook of Japanese *Sogo Shoshas*)

The following is an outline of the key points of the Company’s revised plan: i) three basic concepts (grasp change and open up a new era for Mitsubishi Corporation, develop human assets and reinforce internal systems), ii) consolidate net income of at least JPY400 billion or more in the fiscal year ending March 2009 and onward to the subsequent “jump” period, iii) an Return on Equity (ROE) of 15% over the medium and long terms, iv) investing JPY1,200 billion over the 2-year period covering the fiscal year ending March 2007 and the fiscal year ending March 2008, mainly in strategic fields, v) investment assets of within 1.5 times the shareholders' equity and vi) a consolidated payout ratio of 15% or more. The table below shows the Company's management philosophy.

4.3.3. Sumitomo Corporation

The Sumitomo Group is a family of related Japanese companies, or *Keiretsu.* It is named after its founder, Masatomo Sumitomo and started as a store selling medicine and books in 1630. Masatomo Sumitomo's brother-in-law, Riemon Soga, who ran a copper smelting and smithing business at the time, soon developed a new smelting technique called Nanban-buki which extracted the silver from raw copper. Tomomochi Sumitomo, the eldest son of Riemon Soga, disclosed this technique to other copper smelters and made a name for the Sumitomo family as the origin of the Nanban-buki technique. This gave Sumitomo the ability to rise to the top in copper mining and refining until the late 1800s when the company began to enter other industries, such as banking, warehousing, electric cable production and more. Today, the Sumitomo Group is still run according to the "Founder's Precepts" written by Masatomo Sumitomo in the seventeenth century. The Group consists of 44 companies (chemicals, machinery, finance and insurance, steel, nonferrous metals, commerce, mining, warehousing and transportation, ceramics, construction, rubber products, electronics, electric equipment, services, real estate, etc.) and the main firms of the Group are Sumitomo Corporation (*Sogo Shosha*), Sumitomo Bank and Sumitomo Metal Mining Co., Ltd.

Sumitomo Corporation is the *Sogo Shosha* within the Group; it was founded in 1919. It now has around 5,000 employees and 122 brach offices around the world. In 2007, its revenue was US$49,935 million, gross profit was US$1,669 million and net income was US$612 million. Its major stockholders are the Master Trust Bank of Japan, Japan Trustee Services Bank, Mitsui Sumitomo Insurance Co., Ltd., Sumitomo Life Insurance Company, Dai-ichi Mutual Life Insurance Company, The Chase Manhattan Bank and Nippon Life Insurance Company. Sumitomo Corporation aims to be a global organisation which constantly stays a step ahead in dealing with change, creates new value and contributes to society. Its management philosophy is threefold: i) 'to achieve prosperity and realise dreams' through sound business activities, ii) to place prime importance on integrity and sound management with the utmost respect for individual and iii) to foster a corporate culture full of vitality and conducive to innovation.

With respect to the Company's business activities, the Sumitomo Corporation engages in diverse business activities throughout its world-wide network. These include various domestic and overseas transactions and the import and export of a wide range of goods and commodities and also a wide range of services and investments, in such fields as metals, transportation and construction systems, machinery and electricity, the media, electronics and networks, chemicals, mineral resources and energy, consumer goods and services, materials and real estate and finance and logistics. In addition, the Company has been selecting its core businesses for high profitability and growth potential since 1988. It has engaged in downstream retailing directly to consumers and in the communications business, Portal services and Electronic Commerce as strategic business areas.

Regarding the Company's medium-term management plan, the Sumitomo Corporation launched its two-year medium-term management plan (FY2005 ~ FY2006) in 2004, named the "AG Plan."[36] Under this plan, the Company set quantitative targets of i) a risk-adjusted return ratio of over 7.5% and ii) net income of JPY230 billion. In addition to pursuing these quantitative targets, in order to build a foundation for sustained growth, Sumitomo Corporation adopted a set of basic policies to implement on a globally consolidated basis under the AG Plan, namely, i) the expansion of its earnings base through dynamic growth strategies, ii) implementation of human resource strategies matching its growth strategies and iii) the pursuit of soundness and efficiency.

(Table 4.3. Sumitomo Corporation's Management Philosophy)

Name of the *Sogo Shosha*	Management Philosophy	Promoting Strategies
Sumitomo Corporation	Expansion of the Earning Base	● Strategic move to the future by maximising 'integrated corporate strength' ● Exploring and developing various businesses ● Tackling new technology, potential market and region
	HRM	● Optimal configuration of human resources ● Utilising management and human resources to the fullest extent
	Enhancing Corporate Strength	● Enhance corporate strength with efficiency and soundness ● Efficient group operation on a global basis ● Advancing risk management

(Source: Annual Report of Sumitomo Corporation and The Handbook of Japanese *Sogo Shoshas*)

[36] "AG" is short for "Achievement and Growth."

4.3.4. Marubeni Corporation

The Marubeni Corporation was founded in 1949. It now has over 5,000 employees, 13 domestic offices and 48 overseas branches and offices and 23 overseas corporate subsidiaries with 73 offices for a total of 121 offices in 72 countries. In 2007, its revenue was US$54,754 million, gross profit was US$1,075 million and net income was US$400 million. Its major stockholders are the Japan Trustee Services Bank, the Master Trust Bank of Japan, Sompo Japan Insurance Company, The Chase Manhattan Bank, Tokyo Marine and Nichido Fire Insurance Co., Ltd., Nippon Life Insurance Company and Goldman Sachs International.

The major activities of Marubeni Corporation's business group are sales and trade in a wide range of products and commodities. In addition, the Company offers various financing and project-organising services to customers and also works in diversified businesses such as natural resource development and investment in leading-edge technologies. The Company breaks its operating segments into 12 segments, identified by product and service, agric-marine products, textiles, forest products and general merchandise, chemicals, energy, metals and mineral resources, transportation and industrial machinery, power projects, information and communication, plant, ship and infrastructure projects, development and construction and finance, logistics and new business.

With respect to Marubeni Corporation's medium-term management plan and management philosophy, it announced its "G Plan" in 2005. "G Plan" is a two-year plan (FY2006 ~ FY2007) for Marubeni to accelerate its growth toward further achievement.

(Table 4.4. Marubeni Corporation's Management Philosophy)

Name of the *Sogo Shosha*	Management Philosophy	Promoting Strategies
Marubeni Corporation	Commodity Trade	● Advancement and combination of trading house functions (organising, planning, financing, logistics, etc) ● Quick response to change in industrial structure
	Project Solution Services	● Offer solution services to customers with accumulated and integrated expertise as an organiser, developer and consultant ● Promote superior new projects and increase related businesses ● Arrange structured finance or third-party partnerships ● Organise first stage of feasibility study
	Portfolio Management	● Selection and concentration strategy ● Allocation of management resources with priority (expansion, growth, support, restructuring and withdrawal)
	Cash Flow Management	● Increase net profit ● Reduction of working capital ● Prevention of bad debts ● Reduction of fixed assets

(Source: Annual Report of Marubeni Corporation and The Handbook of Japanese *Sogo Shoshas*)

While it firmly maintains a position of "defence" through refining its management system, through the G Plan, the Company will shift to the "offence" posture by expanding its business domain, further sophistication and diversification of their function as a *Sogo Shosha* and aggressive investment in strategic fields. The Company achieves sustainable growth, with its diverse human resources challenged positively and vitally. While maintaining a balance between "offence" and "defence", the Company works to selectively apply management resources in priority fields (through a new investment of JPY500~600 billion over two years), to continue thoroughly implementing portfolio management, strengthening risk management, promoting human resource deployment and education and leveraging overall strengths through lateral collaboration (collaboration between divisions, etc.) The quantitative targets are to limit risk assets to within the size of shareholders' equity, achieve a two-year consolidated net income of JPY220 billion, a risk-return of over 10%, an Return on Assets (ROA) of over 2% and total assets of approximately JPY5trillion. The table below shows the Company's management philosophy.

4.3.5. Itochu Corporation

Itochu Group, formerly C. Itochu, was initially founded as a kimono retail store in 1858 by Chubei Ito. It gradually evolved from pure buying and selling to manufacturing, supplying, exporting and investments. After various mergers and acquisitions, it was incorporated in 1949. It now ranks as one of the largest *Sogo Shosha* companies in Japan and among the world's largest companies; it has 1,027 subsidiaries and associated companies operating in over 80 countries. Itochu Corporation currently has seven major divisions or business groups: textiles, foods, grain and canned goods, aerospace, electronics and multimedia, financial, realty insurance and merchandise services, such as foreign exchange and leasing, petroleum and nuclear energy.

Within the Group, Itochu Corporation is the *Sogo Shosha* founded in 1949. It now has over 4,000 employees, 18 domestic offices and 135 overseas branches and offices around the world. In 2007, its revenue was US$51,699 million, gross profit was US$1,367 million and net income was US$824 million. Its major stockholders are the

Japan Trustee Services Bank, the Master Trust Bank of Japan, Mitsui Sumitomo Insurance Co., Ltd., Nippon Life Insurance Company, Tokyo Marine and Nichido Fire Insurance and Nipponkoa Insurance Co., Ltd. The major activities of Itochu Corporation's business are engaged in the domestic trading, import/export and overseas trading of various products such as textiles, machinery, information and communications-related products, metals, products related to oil and other energy sources, general merchandise, chemicals and provisions and food. With respect to Itochu Corporation's medium-term management plan, it pursues the three principles of "Challenge, Create and Commit."

(Table 4.5. Itochu Corporation's Management Philosophy)

Name of the *Sogo Shosha*	Management Philosophy	Promoting Strategies
Itochu Corporation	Development of New Earnings and Growth Engines	● Expand earnings and develop new businesses ● Gradual shift to new businesses for future ● Focus on 'Super Powerful and Attractive Business Areas' such as IT and the media, natural resources, solutions, synthetic fibre and foodstuffs
	Solid and Sound Management	● Greater financial soundness ● Enhancing the capacity for risk management ● Setting up transparent corporate governance
	Flexible HRM	● Motivating and encouraging employees ● Providing employees with appropriate rewards ● Optimal configuration of human resources

(Source: Annual Report of Itochu Corporation and The Handbook of Japanese *Sogo Shoshas*)

The Company's major strategies are i) a shift to aggressive business (expand earnings and creating new business) and ii) establishing solid management (further improvement of financial position, enhancement of risk management, establishment of highly transparent corporate governance and reinforcement of internal control).

4.3.6. Sojitz Corporation (Nissho Iwai and Nichimen)

The Sojitz Corporation is a *Sogo Shosha* created through the merging of Nichimen Corporation and Nissho Iwai Corporation in 2003, both of which had over a century of trading history. The Nichimen Corporation was founded in 1892 and the Nissho Iwai Corporation in 1928. It now has almost 2,000 employees, 8 domestic offices and 64 overseas branches and offices around the world. In 2007, its revenue was US$24,680 million, gross profit was US$567 million and net income was US$183 million. Its major stockholders are the Japan Trustee Services Bank, the Master Trust Bank of Japan, Morgan Stanley Japan Securities Co., Ltd., Lehman Brothers Asia Capital Company and the State Street Bank and Trust Company. Sojitz's business activities are wide-ranging, covering machinery and aerospace, energy and mineral resources, chemicals and plastics, real estate development and forest products, consumer lifestyle-related business and new business development.

With respect to its medium-term management plan (FY2006 ~ FY2008), it announced the fundamental policy of a new stage to deliver sustained growth through specific measures which included i) further enhancing growth strategies, ii) accelerating capital and financial strategies and iii) upgrading risk management.

(Table 4.6. Sojitz Corporation's Management Philosophy)

Name of the *Sogo Shosha*	Management Philosophy	Promoting Strategies
Sojitz Corporation	Growth Strategies	● Reaching a stage of sustained growth by leveraging the company's strengths to expand functions and business investment
	Capital and Financial Strategies	● Speeding up financial restructuring and further stabilising the funding structure
	Upgrading Risk Management	● Enhancing and upgrading the company's risk management structure and maintaining a high-quality portfolio

(Source: Internet Web Site of Sojitz Corporation, 2008)

4.3.7. Tomen Corporation (Toyota Tsusho Corporation)

The Tomen Corporation started its business in 1920 as Toyo Menka Kaisha Ltd. by spinning off the cotton division of Mitsui & Co., Ltd. The Company merged with the Toyota Group and changed its name to Toyota Tsusho Corporation in 2006. However, the name Tomen Corporation is widely used in Japan as well as in overseas markets. The Company engages in business activities in a variety of fields across the globe. These business activities include sales transactions relating to a broad range of products and also the manufacturing, processing, investing and servicing of such products. Tomen Corporation's business activities are wide-ranging, covering metals, machinery and electronics, automotive, energy and chemicals and foodstuffs.

In 2007, its revenue was US$36,558 million, gross profit was US$1,004 million and net income was US$292 million. With respect to the Company's management strategies, it aims to make further growth by creating next-generation businesses in six business domains, namely, metals, machinery and electronics, automotive, energy and chemicals, food and consumer products. In order to implement its management strategies, it announced 'Three G Values' – Global, Growing and Generating.

(Table 4.7. Tomen (Toyota Tsusho) Corporation's Management Philosophy)

Name of the *Sogo Shosha*	Management Philosophy	Promoting Strategies
Tomen (Toyota Tsusho) Corporation	Global	● Development of the Company's activities on the global stage
	Growing	● Sustaining a healthy yet growing morale and passion
	Generating	● Constant generation of new businesses

(Source: Internet Web Site of Toyota Tsusho Corporation, 2008)

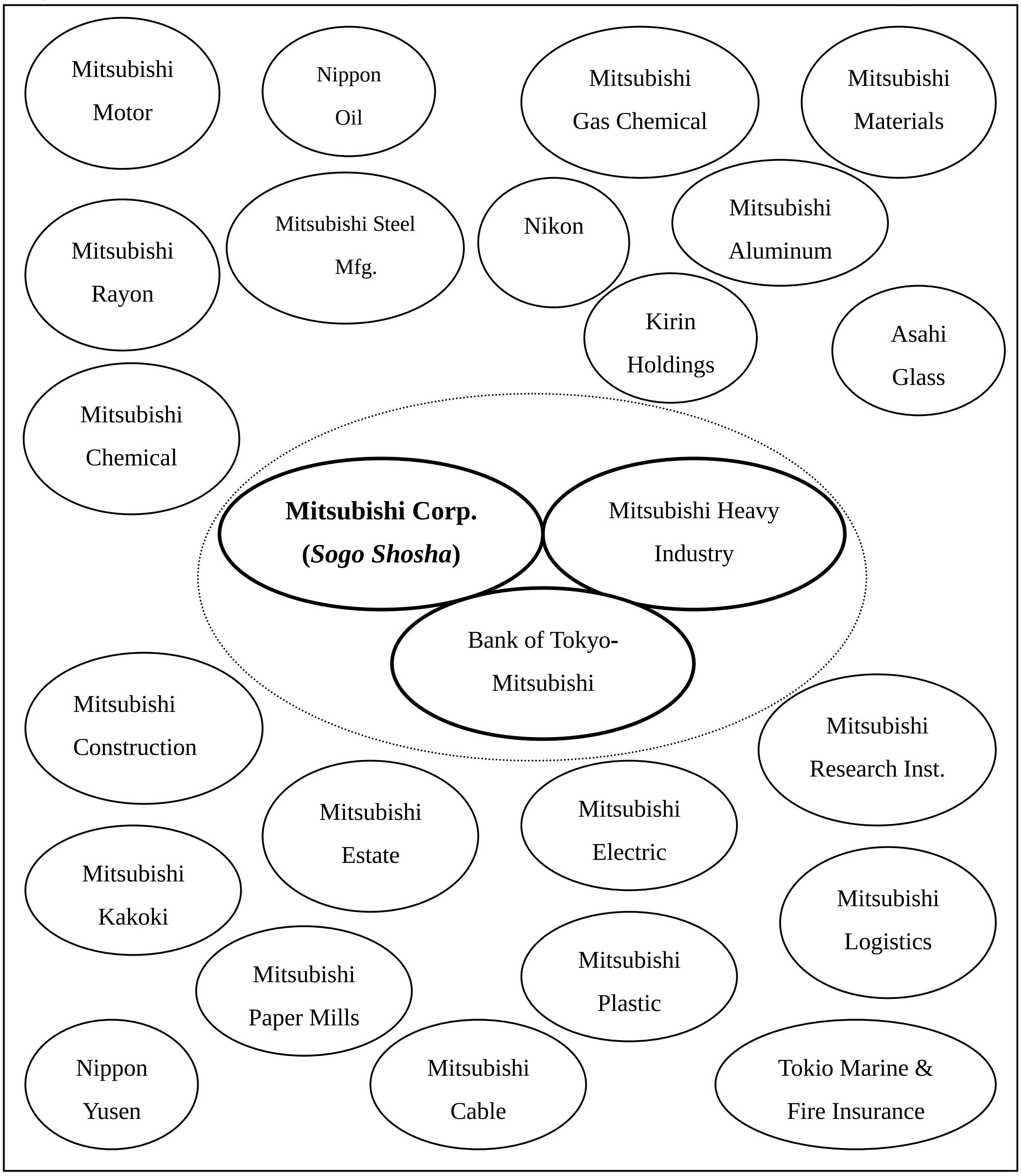
4.4. The Management System within the Japanese *Sogo Shoshas*

4.4.1. Organisational Structure

Before examining the organisational structure of the Japanese *Sogo Shoshas*, it is essential to review the position of the *Sogo Shosha* in its *Keiretsu* group. Each *Keiretsu* has one *Sogo Shosha*, which is positioned at the heart of the *Keiretsu*. Most *Sogo Shoshas* are considered so important that they are part of the nucleus of the group, together with the main bank; in the Mitsui Group, indeed, the *Sogo Shosha* was traditionally more influential than the bank. In all six *Keiretsu* groups, the *Sogo Shoshas* play the same critical role, helping to coordinate group activities through every aspect of commerce. In the Mitsubishi Group, for example, there are main three firms: Mitsubishi Corporation, Mitsubishi Bank and Mitsubishi Heavy Industry. Mitsubishi Shoji – in English, Mitsubishi Corporation – is the *Sogo Shosha*.

In their organisational structure, all *Sogo Shoshas* are divided into administrative and product departments. The former are engaged in support activities (finance, shipping, etc) and housekeeping activities (accounting, auditing, etc.). The latter undertake business operations. Their number varies somewhat from one *Sogo Shosha* to another, but most *Sogo Shoshas* have 10 to 15 departments (iron and steel, textiles, non-ferrous and light metals, machinery, energy, chemicals, etc.). Each department is further divided into divisions, for example, the chemicals department is divided into inorganic chemicals, organic chemicals, fine chemicals, plastics, etc. (Kunio, 1982).

(Figure 4.1. The Position of the *Sogo Shosha* in the *Keiretsu*: Mitsubishi Group)



(Source: Internet Web Site of Mitsubishi Group, 2008)

In most *Sogo Shoshas*, all products departments are profit centres and the head of department manages a department as if it was an independent company. Departmental heads are responsible to either executive managing directors or vice-presidents and the president presides over all. Thus, the chain of command runs from the president to the executive managing directors or vice-presidents, to departments heads and then to division heads. This organisational structure of the *Sogo Shosha* is the structure which Mitsui developed for itself at the beginning of the twentieth century. Certainly, the number of products handled and the volume of trade have increased and the organisations have become much bigger, but the essential organisational features have remained the same.

The current organisational structure of Sumitomo Corporation, for example, consists of 5 corporate/administrative groups and 8 business groups. The business groups (for metal products, transportation and construction, machinery and electrical goods, media and network, chemicals, mineral resources and energy, consumer goods and services, and finance and logistics) make up 37 departments or divisions. The table below shows the organisational structure of the major *Sogo Shoshas* by the number of departments or employees.

(Table 4.8. Organisational Structure of Japanese Major *Sogo Shoshas* in 2008)

	Sumitomo	Mitsubishi	Mitsui
Number of Corporate/Administrative Groups/Units	5	N/A	N/A
Number of Business Groups/Units	8	6	14
Number of Department/Divisions under Business Groups/Units	37	37	N/A
Number of employees including executives	5,008	5,454	5,869

(Source: Annual Report of each *Sogo Shosha*, 2008)

With respect to global networks, most *Sogo Shoshas* divide the world into seven geographical regions: Japan, Asia, the Middle East, Europe, the US and North America, Central America and South America and Oceania. The table below shows the numbers of *Sogo Shoshas'* overseas branches and employees.

(Table 4.9. Number of Overseas Branch of Major Japanese *Sogo Shoshas* in 2008)

		Sumitomo	Mitsubishi	Mitsui
Number of Overseas Branches		122	123	158
Number of Employees	Resident Representatives	786	588	758
	Local Employees	593	1,212	1,152

(Source: Annual Report of each *Sogo Shosha*, 2008)

- Note: Number of employees according to data of 2005

4.4.2. Corporate Culture

The underlying Japanese societal culture is that Japanese people believe the self to be deeply embedded in social relationships. Hamaguchi (1988) argued that there is little confidence in the power of the individual to devise, control and execute his or her own destiny, in particular if the planning runs counter to the prevailing external social and structural norms and conditions. Debroux (2003) further stressed that social structures have generated a durable cohesion in all periods and places throughout Japan's history. As Hayashi (1988) suggested, from an historical perspective, Japanese management can be regarded as an evolutionary product of the 'rice culture'. Group effort, diligence and consensual decision-making can be regarded as practices which have evolved out of Japan's rice culture. In the interaction between national/social values and corporate culture, the Japanese corporate culture is based on its societal culture. In the company, members can count on the mutual support of the others with a high degree of interdependence (Debroux, 2003).

The Japanese corporate culture is based on collectivism and wholism (Hofstede, 1991 and Ouchi, 1981). According to Hofstede's survey (1982, 1983 and 1991) of five major dimensions of culture in various countries, Japan placed low value on individualism, but high value on power distance, masculinity, uncertainty avoidance and long-term orientation. The low value on individualism entails, in other words, the high value on collectivism. Relating to wholism, Ouchi (1981), in his book of Z theory, argued that Japanese organisations form inclusive relationships between employees and employer (wholistic concern for people). A set of mechanisms provides the social support and emotional release necessary for emotional equilibrium.

(Table 4.10. Five Major Dimensions of Culture: Japan, Korea and the UK)

Factor Country	Power Distance	Individualism	Masculinity	Uncertainty Avoidance	Long-term Orientation
Japan	High	Low	High	High	High
Korea	High	Low	High	High	High
UK	Low	High	High	Low	Low

(Source: Summarised from Hofstede, G. (1982), "Culture's Consequences", Sage Publications, Abridged Edition, Hofstede, G. (1983), "The Cultural Relativity of Organisational Practices and Theories", Journal of International Business Studies, Vol.14, No.2 and Hofstede, G. (1991), "Cultures and Organisations: Software of the Mind", McGraw-Hill Book Company)

The distinctive differences between Japanese firms' corporate culture and that of the West which are often cited are lifetime employment, job rotation, promotion based on seniority, group consensus, just in time (JIT) and *Kaizen.*

Lifetime employment brings job security, job enrichment and the career development of employees. The organisation demands loyalty of its employees and in return it offers job security for so-called "organisation men" (Chung, Lee and Okumura, 1998). The candidate takes a significant risk in betting his future on a particular company. If a Japanese leaves in mid-career or is fired from a large company, he will have a much harder time than his Western counterpart (e.g. American or English) in being hired by another large company (Chen, 2004)[37]. Job rotation in Japanese firms is valued as the best means of increasing the motivation of the workers, improving their performance and thus achieving better efficiency and productivity[38] (Kahal, 2005). In the process of decision-making, the starting point in a typical Japanese corporation is input on the bottom line of the organisation. Since everyone at all levels is involved, the system ensures their commitment (i.e. group consensus decision-making).[39]

JIT, a system developed by Tai Chi Ohno, vice-president of Toyota, is a Japanese management philosophy and culture, which has been put into practice since the early 1970s in many manufacturing companies. The primary objective of this system is to meet consumers' demand with minimum delay. From the *Sogo Shosha's* perspective, although JIT is quite difficult to apply there; the system is appropriate for manufacturing organisations, even though the objective is in accord with the one pursued by the *Sogo Shoshas*. Another important concept in Japanese corporate culture is *Kaizen* (improvement). The basic concept of *Kaizen* is that everyone's way of life (e.g. working life, social life or home life) deserves constant improvement. Thus, this concept can be applied to every aspect of everyone's activities (Kahal, 2005).

As in Korea, another feature of Japanese corporate culture is the longer working hours than other OECD nations show. Although the number of working hours has

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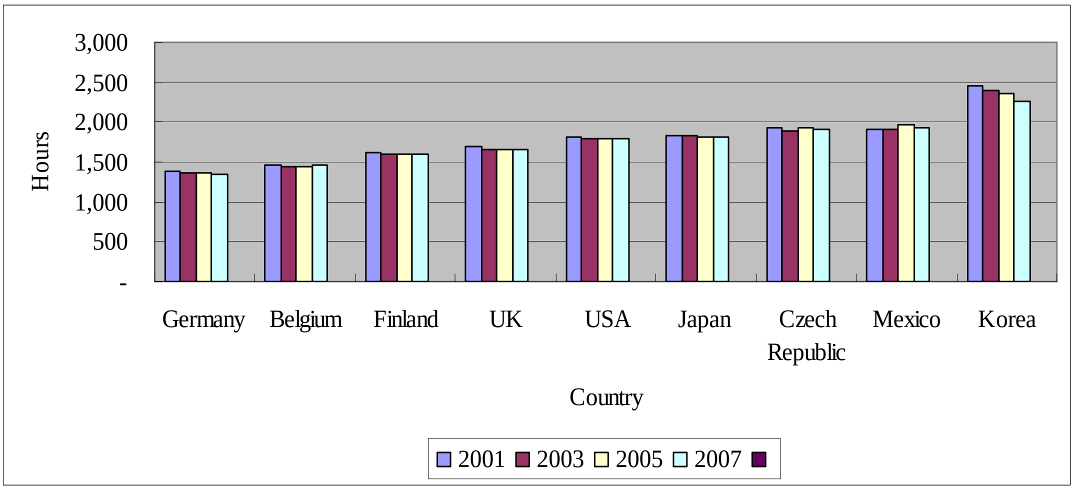
[37] Although lifetime employment is the most distinctive feature of Japanese culture, it is now under pressure to be modified. For more details of this, see the next section, 4.4.4. HRM.

[38] Kahal (2005) pointed out that the drawback of the job rotation system is the potential de-skilling of the workforce itself. Workers may be gaining new expertise in various fields, but these are often limited to the company's specific operations and production techniques and may not be valuable for employment elsewhere. This restricts workers' chances for a career move outside the firm.

[39] For more details of the decision-making process within Japanese firms, see Chapter 6

recently dropped, Japan was ranked higher than most European countries, including the UK and Germany, in the average hours worked per year. According to the OECD's statistical data (2008), Korea ranked as the nation with the longest working hours (2,266 hours in 2007), followed by Mexico (1,933 hours in 2007), the Czech Republic (1,914 hours in 2007) and Japan (1,808 hours in 2007).

(Figure 4.2. Average Annual Working Hours per Worker)



(Source: OECD, 2008)

Paton (2006) argued that Japan has a notorious corporate culture which can make it difficult for employees to ask for more time off than their bosses, who are themselves often stuck in the office. For white-collar employees, it has become harder to take holidays than before because of the tight work schedules since companies cut down on staff to save on costs in recent years. Thus, the Japanese government has long tried to encourage workers to take their holidays in the hope they will spend more on leisure activities and boost the economy. The country's Ministry of Health, Labour and Welfare is proposing a law which would force companies to encourage people to take their full vacation allowance. One unique feature of Japanese corporate culture among salary men is the drinking culture which prevails after working hours. According to Hofstede (1991), these men have the outlet of getting drunk along with colleagues or superiors after work. At such times, men release their pent-up aggression, even towards superiors[40], but, the next day business continues as usual. Such drinking bouts represent one of the major institutionalised places and times for anxiety release.

(Table 4.11. Comparison of Corporate Culture and Management System: Korea, Japan and the West Firms)

	Korea	Japan	The West
Overall Corporate Culture	Collectivism, humanism, familism, abilitism and efficiencism	Collectivism, rationalism, traditionalism and efficiencism	Individualism, rationalism and equalitarianism
Decision-making	Individual decision-making centralised in one leader	Group decision-making with shared information	Individual decision-making or decision by majority
Employment	Lifetime employment	Lifetime employment[41]	No specific guarantee of employment
Settlement of Problem	Settlement with authority and power of superiors and leaders	Arbitration of problems in advance and emphasis on harmony and loyalty	Perfect and thorough discussion when there are problems
Loyalty	High	Very High	Low
Collectivism and Individualism	Collectivism and individualism	Collectivism	Individualism
Relationship with the Government	Intimate and collaborative relationship	Intimate and collaborative relationship	No direct relationship
Reward System	Combination of seniority system and performance-based system	Seniority system	Performance-based system
Overall Management Mode	Leadership-driven authoritarian mode	Environment-driven adaptive mode	Structure-driven mechanistic mode

(Source: Adapted from Chang, C.S. (1983), "Comparative Analysis of Management System: Korea, Japan and the USA", Korean Management Review, Vol. 13, p. 99 and Chung, K.H, Lee, H.C. and Okumura, A. (1988), "The Managerial Practices of American, Japanese and Korean Firms", Journal of East and West Studies, Vol. 18, No. 2)

[40] The same drinking culture exists within Korean corporations as well. However, the big difference between Japan and Korea is that inferiors in Korea hardly ever release their pent-up aggression towards superiors.

[41] According to Bailey (2004), one of the traditional strengths of the Japanese economy is lifetime employment, with the interaction of the main bank system, the *Keiretsu* system and the higher education system. Approximately 33% of Japanese firms guarantee lifetime employment to their employees.

Corporate culture and the management system, including decision-making, in Korean, Japanese and Western firms can be summarised as the above table.

4.4.3. Ownership, Corporate Governance and Cross Shareholding

Although Korean *Chaebols* and Japanese *Zaibatsu* were both big business groups dominated by their founding families, in most Japanese business groups ownership and management are normally separated. According to Shim (2002), the best-known Japanese *Zaibatsu*, the Mitsui and Sumitomo families, do not participate actively in management but entrust it to professional managers. The separation of ownership from management has continued in present-day *Keiretsu*. In both *Zaibatsu* and *Keiretsu*, most decisions are made by professional managers rather than shareholders, in particular, the dominant families.

A unique system in Japanese firm's ownership structure, however, is cross-shareholding. In his book, "*Cross Shareholding in Japan*", Okabe (2002, p.2) argued that

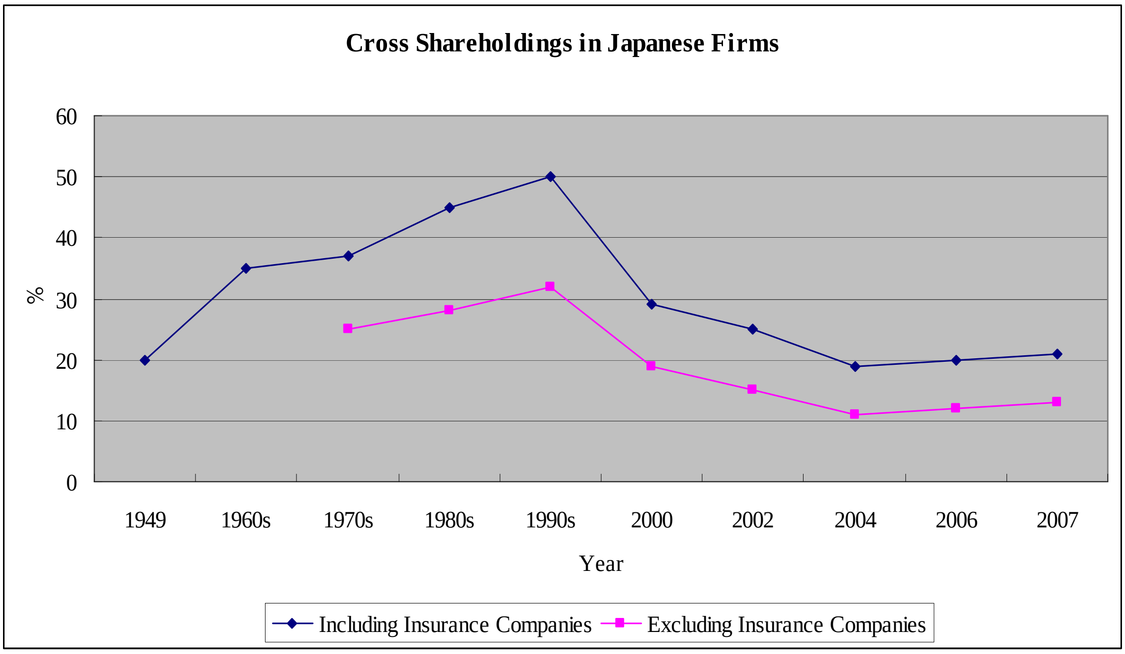
> *"One of the distinctive features of corporate ownership in Japanese firms is that Japanese firms have a strong tendency to have their equity owned by the counter party corporation with which the firm has business transactions, on the one hand and to own the equity of the counter party corporation, on the other. That is, two companies hold stakes in one another, by way of mutual shareholding or cross shareholding"*

This being so, how do Japanese firms see the benefits of cross shareholding? The survey result conducted by the Japanese Economic Planning Agency in 1999 gave a clear answer to this question. A survey of 1,361 non-financial Japanese business firms listed on the Tokyo, Osaka and Nagoya Stock Exchanges in 1998 indicated that Japanese firms regard the benefits of cross shareholding as i) long-term stability of the share price (69.9%), ii) stability of the firm's transactional relationship (52.3%) and iii) the prevention of hostile takeovers (33.0%)[42].

However, critiques of cross shareholding have emerged since the 1990s, because many business leaders and politicians believe that the long-term Japanese economic depression is fundamentally attributable to the mistrust of corporate governance. According to Narusawa, Emori and Ohmori (2001) in the Nomura Research Institute, the change has been occurring in the governing structure in Japanese firms and the shareholder composition of Japanese companies has been rapidly changing over the past few years. One important factor accelerating this trend has been the rush by banks and related companies to shed cross-held shares and back away from the practice altogether. Japanese companies, including insurance firms, have been trying to dissolve such relationships since 1995 and the ratio of cross shareholding to total holdings has declined to 21% in 2002. However, after falling for a decade, the level of cross shareholding has crept up since 2004. Cross shareholdings make it harder to work with firms outside the circle, reinforcing the inflexibility of Japan's business environment (The Economist, 2008).

[42] This survey also showed the costs of cross shareholding. The three major costs related to cross shareholding are i) the possibility of incurring hidden losses when the share price decreases (58.6%), ii) a decreasing liquidity of funds (37.8%) and iii) a decreasing efficiency of capital by weakening the awareness of the cost of funds (11.5%) (quoted from Okabe, M. (2002), "Cross Shareholdings in Japan: A New Unified Perspective of the Economic System", Edward Elgar, pp. 37~40).

(Figure 4.3. Changes in the Cross Shareholding Ratio among Japanese Firms)



(Source: The Economist (2008), "Criss-crossed Capitalism: Japanese Firms' Tradition of Cross Shareholdings is Causing Problems", The Economist Internet Edition, 06/11/2008)

Since the crash of the bubble economy, Japanese firms have been working to overcome their indolent performance through reforms in management strategies. As one of the corporate structural reforms, the reform of corporate governance became increasingly important. According to Tsuru (2000), Japanese corporate governance is in transition. The bubble crash and long-lasting stagnation of the Japanese economy in the 1990s have prompted criticism of the effectiveness of the existing Japanese corporate governance system, in particular the main bank functions.[43] Komiyama and Masaoka

[43] Tsuru argued that the main bank mechanism has been out of order, to an extent. Ever-increasing non-performing loans and a decline in the net worth of banks over the past several years have caused significant changes in lending behaviour. The growth of total bank loans has remained weak and scarce funds have increasingly been allocated to high-quality borrowers. Some banks gave up rescuing and rushed to withdraw their funds from financially distressed client firms, who had maintained a long-term business relationship with them. The change in the behaviour of a main bank might be a rational response to its deteriorating asset quality, but this may also create negative externalities. Because a borrower and other banks would reasonably understand this as a breach of trust, once reputation as a main bank has been lost, it is not easily recovered. Therefore, a long-term relationship between a main bank and a borrower, which gives a strong basis for the main bank governance, might have been significantly weakened. The recent rapid dissolution of cross shareholding between banks and business groups may well explain such a phenomenon.

(2002) further stressed that corporate governance in Japan is undergoing dramatic changes which reflect the transformation of the capital market, such as globalisation and borderless capital markets. As a way of reforming corporate governance, many proposals have been introduced recently and finally an amendment to the Japanese Commercial Code[44] was passed in April 2002. The main feature of this amendment was to introduce a new corporate governance regime modelled on the American-style board of directors (Executive Officer System) and to permit Japanese firms to choose either the conventional or the new approach. A new corporate governance system will be called "companies with three committee boards (Audit, nominations and compensation)". Additionally, in order to expedite management decisions, provisions are made for the establishment of a decision-making subcommittee regarding major assets, which can be mandated to consider some of the issues hitherto assigned solely to the board of directors (Hashimoto, 2002)[45].

But in a corporation where ownership and management are separate, as in most large firms in the West and Japan, there is always the possibility of agency problems – conflicts between shareholders (principals) and managers (agents).

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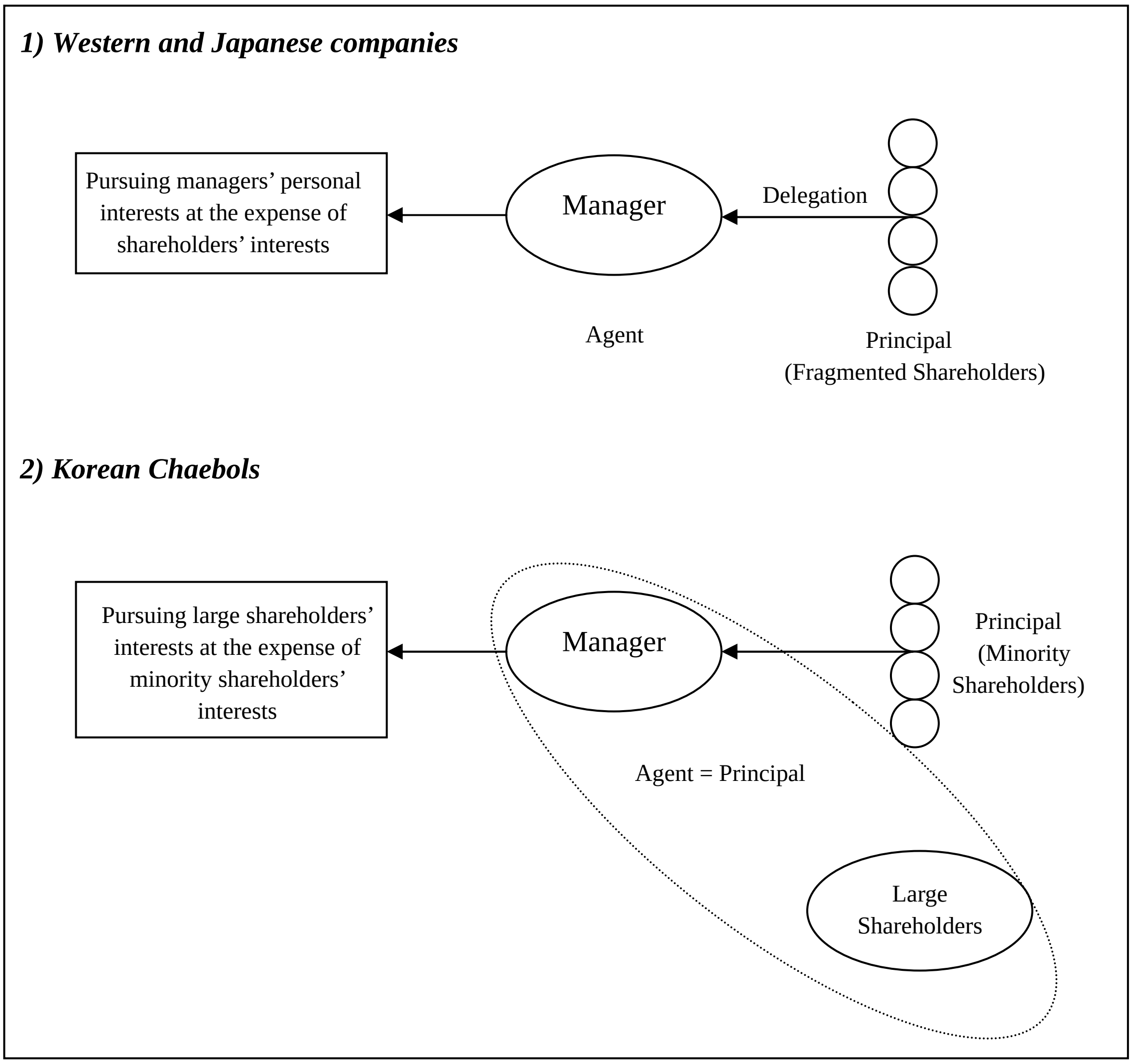
[44] Before the Commercial Code was officially passed in April 2002, the corporate sector had already started to act on the board reforms. The survey on board reforms conducted by the Japanese Economic Newspaper (*Nihon Keizai Shimbun*) in 2001 showed that 35.7% of the companies surveyed had already introduced an executive officer system and 14.1% were studying its introduction. The total for these two groups was close to 50%. Of the companies surveyed, 38.8% had already appointed outside directors and 24.2% were reviewing such appointments (Komiyama and Masaoka, 2002).

[45] For more details, see Hashimoto, M. (2002), "Commercial Code Revisions; Promoting the Evolution of Japanese Companies", Nomura Research Institute, pp. 1~15

(Figure 4.4. Comparison of the Agency Problem)



(Source: Chang, S. J. (2003), "Financial Crisis and Transformation of Korean Business Groups: The Rise and Fall of *Chaebols*" Cambridge University Press, p. 173)

Chang (2003) argued that salaried professional management manages *Keiretsu* affiliates in Japan where ownership and management are separate. However, the situation is somewhat different within Korean *Chaebols*, where the chairman plays the dual role of owner and manager. This is closely related to the nature of *Chaebols'* bank loan-based financing and the government's protection of the *Chaebols*[46]. The chairman

[46] Hong and Ahn (2000) argued that the structure of Korean *Chaebols'* shareholding has not diversified as much, although they have expanded their size very rapidly. This is related to the *Chaebols'* financing method and the state's policy of protecting them. Owing to the centralised financing mechanism supported by the state, the *Chaebols* could finance their funds by loans, which enabled the *Chaebol*

of the *Chaebols* acts as if he were their chief executive officer, even though all the affiliates are legally independent entities with their own boards of directors and presidents. As illustrated in the above figure, fragmented shareholders (principals) in Western companies delegate their authority to professional managers (agents), who sometimes pursue their personal interest at the expense of shareholders' interests. However, large shareholders in Korean *Chaebols*, who are often top managers, play the dual role of agent and principal, sometimes pursuing their own interests to the detriment of minority shareholders. Therefore, principal-agent problems in *Chaebols* do not assume the same form as they do in Western firms.

4.4.4. HRM

The traditional key feature in Japanese firm's HRM is lifetime employment and a seniority-based promotion system. This system was useful when Japan was in the midst of rapid economic growth and companies were competing for new employees for their expanding businesses. However, this system has some drawbacks and has been under increasing pressure to change since the mid-1980s. With slower economic growth, the competitive advantages of the system have declined (Chen, 2004).

As one of their measures, large Japanese firms, from the early 1990s, pursued a multi-pronged HRM strategy with early retirement schemes and growing use of outsourcing and flattening of the organisational hierarchy (Debroux, 2004).

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families to maintain their control with a relatively small amount of investment. Moreover, the government's protection of the *Chaebol*s owners' control rights created the unique system of non-separation of ownership and management. However, the relationship between the government and the *Chaebols* has relaxed since the middle of the 1980s and the *Chaebols* have become independent in their financing and acquisition of information.

The *Sogo Shoshas* also followed traditional HRM policy, as other firms did, and they also faced need to transform their HRM policy. From the *Sogo Shosha's* perspective, human resources are the most precious management resource. It is the people who sell, buy and coordinate the various activities who contribute to the corporate objective. Kuino (1982) argued that, unlike manufacturing companies which are essentially joint ventures between people and machines, people are the sole determinant of the success or failure of the *Sogo Shosha.* This implies that an effective HRM is closely correlated to the *Sogo Shoshas'* performance.

The following section examines both Japanese historical HRM policies and its new HRM practices suited to the global economy.

- **Recruitment and Selection**

In Japan, HR managers traditionally prefer to recruit graduates from high-ranking universities, thereby showing trust not only in the ranking system itself, but also in the long-term potential assumed to exist among graduates. Thus the tradition for graduate recruitment and selection dovetails with the traditional experience of high school and university education (Jackson and Tomioka, 2004).

The *Sogo Shoshas* are no exception to this recruitment pattern. The *Sogo Shosha's* core staff is literally an elite group drawn from an elite group. The firms recruit only from a limited number of universities, all of which are highly selective institutions. The employers who are regarded as most prestigious – a few ministries in the national government, the biggest banks, the large *Sogo Shoshas*, airlines and large newspapers – recruit only from the very top-ranking schools.

The large *Sogo Shosha* receives thousands of applications a year. Both standardised testing and interviewing are used as part of the elimination process. The standardised tests often include both achievement and psychological personality tests. The interviewing process is multistage as well. Candidates are usually exposed to three groups within the company: top management, which devotes an impressive amount of time to interviewing candidates, professionals from the personnel function, who are experts at recruiting and members of line management, in particular those with several year's experience but not yet of executive rank. Thus, it is necessary for a cross section of the firm to approve someone's candidacy before he is taken on. All *Sogo Shoshas* place special emphasis on seeking recruits who will be compatible with their own corporate culture. There are many subtle differences among the *Sogo Shosha* companies. In general, however, their corporate cultures stress initiative – such as is needed to develop new businesses – cooperation and teamwork (Yoshino and Lifson, 1986).

However, the emerging strategic environment challenges the ability of Japanese HR managers to predict what types of staff skills and qualities their organisation will need in the near to mid-term. The recruitment and selection processes thus become more complex. According to Kono and Clegg (2001), current recruitment patterns in Japanese firms show that large companies are becoming more discerning and less general in their recruitment processes. There is an increasing reluctance to offer new entrants a firm prospect of lifetime employment and career progression. The environment for graduate recruitment and selection in Japan is thus undergoing a fundamental shift in values and priorities.

- **Training and Development**

According to human capital theory, human capital is accumulated through formal schooling or on-the-job training (OJT). This theory suggests that workers with more years of education or a longer OJT period accumulate more human capital and earn higher wages accordingly. Debroux (2003) argued that companies have to train new employees systematically and intensively in order to transfer the accumulated stock of knowledge.

The *Sogo Shoshas* have well-organised training programmes. As a first step in their training, for example, all recruits gather at headquarters, where an entire day typically is devoted to entrance ceremonies and lectures on company history and philosophy. Particular emphasis is given to the concept that the recruits are entering an entire new life: no longer are they students, they are members of adult society and part of the "family" of the *Sogo Shosha*. After the initiation day ceremonies, more days may be spent at headquarters learning about company policies, organisation, employee benefits and other basic information. Following this, in one representative firm the recruits spend a week together at a conference retreat located in a relatively remote and isolated area. Team sports and group discussions are the major features of this firm's orientation. Nothing specifically job-related is touched on. The emphasis is completely on building morale and rapport among the recruits. During the first year new members are allowed or required to attend management education courses in such basic business skills as accounting, commercial law and international trade practices. After the first year optional continuing education courses are offered and are usually well attended (Yoshino and Lifson, 1986).

But the main training takes place on the job. In Japanese firms, training is conducted specifically for knowledge and skill acquisition, using OJT to provide the necessary skills for short-term improvement. According to the HRM System Development Centre at the Sanno Institute of Management in Tokyo (2000), OJT activities provide the necessary knowledge, skills and attitudes through daily contact from instructors, supervisors and seniors in the workplace. Most Japanese firms engage in OJT because: i) it is efficient in terms of time and cost, ii) work that is difficult to explain clearly in writing can be learned through observation and iii) flexible OJT can develop staff for the big picture.

Kawaguchi (2006) also emphasised the importance of firm-initiated training programmes by stressing that OJT is more common and intense in Japan than in other countries. Through his research on analysing the relationship between firm-provided training and wages, he found that training participation and wages are positively correlated. This means that workers with stronger educational backgrounds are more likely to participate in firm-initiated training activities. The participation in firm-offered training increases participants’ wage in a causal sense.

- **Performance Appraisal and Compensation**

A traditional feature of Japanese firm's personnel management is the use of seniority as the basis for salary and promotion. In most Japanese companies, the critical factor in determining wages is the age and experience of the worker (Sam and Hiromitsu, 1990).

Japanese firms', including the *Sogo Shosha*, compensation system contrasts with Western practices in a number of ways. A person is hired for lifetime potential, not for specific skills or a particular job slot. The compensation model is based on the amount and pattern of compensation to be received over an entire career. Equal pay for equal work applies to a career but is not necessarily true at any given point. A younger person and an older person doing the same specific tasks will receive very different salaries, due to the emphasis on seniority; but over their career lifetimes they could receive comparable compensation (adjusted for inflation, changes in the standard of living, the rank reached by retirement, etc.). Base salary is the largest determinant of overall compensation. For approximately the first 15 years, an employee's age, position in the hierarchy and base salary are in virtual lockstep. An employee with ten years' seniority will receive approximately double the base salary of a new recruit (Yoshino and Lifson, 1986). However, there is considerable pressure to reduce the influence of seniority on compensation.

The traditional compensation system is under pressure to change. In many Japanese companies the commonly used term of *kyuryo* (salary) is replaced by the term *hoshu* (compensation) which in the past was applied to the directors only. *Kyuryo* has the connotation of pay received automatically by the employee, not relating to performance (Debroux, 2003)

Suda's (2007) research on Japanese firms' pay systems found that they have been changing from organisation-based systems to market-based pay systems since the mid-1990s. He carried out a case study by analysing 10 Japanese firms, all of which had changed their pay system. The most notable change was from a person-based system to a job-based system[47]. Among the ten firms studied, four introduced a job-based system for all employees and three firms adopted the same system for managers. However, compared with the job-based system, market pay is not widespread. Five firms in the study used a market-based pay system for at least some employees. Three firms implemented market pay, using market salary surveys. The main reason is the difficulty in gathering pay data.

- **Transformation of HRM**

Overall, Japanese traditional HRM features such as lifetime employment, seniority-based pay and recruitment pattern have been undergoing transformation since the slower economic growth in the 1990s. Among these, there were considerable pressures on the lifetime employment system to be modified. According to Morris, Hassard and McCann (2006), some Japanese firms were encouraging managers to take

[47] According to Milkovich and Newman (2002), there are two basic types of pay structure; job-based and person-based. In the job-based structure, the pay rates may be determined by reference to relative internal value (established by job evaluation) and external relativities (established by market pat data). Therefore, the job and the market are the factors which determine pay structures. In the person-based structure, personal performance and personal attributes such as skills, knowledge and behaviour determine pay rates and pay structures.

early retirement at a fairly young age, for example, 45 onwards in one company. Another firm offered old managers financial assistance to start up their own business.

There were changes in recruitment pattern, too. Some firms have dramatically reduced their entry-level recruitment numbers. For example, one company's graduate recruitment fell from 80 to 30 per annum. This was to reduce employee numbers and ultimately to save costs. This implies that Japanese firms prefer 'mid-career' employees with specific skills to new graduates with generic potential skills. This was also an attempt to bring in human resources from outside the organisation (Morris, Hassard and McCann, 2006).

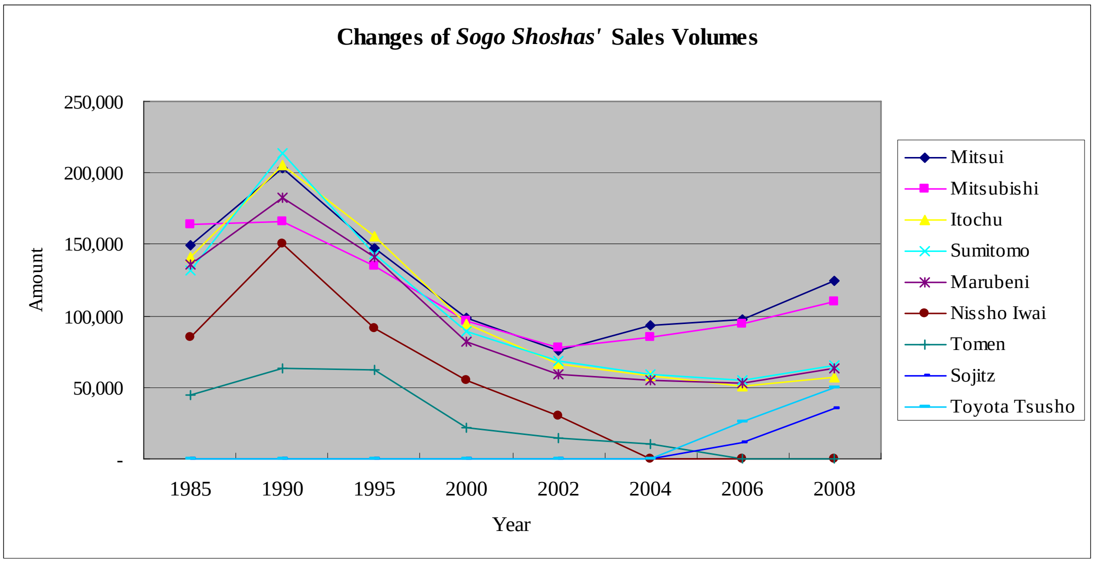
With respect to the compensation system, some firms introduced a performance-related compensation system by reducing age-related pay through direct links between Management by Objective, appraisal and pay. However, after establishing performance-based HRM, some firms had problems because high performers who worked on more difficult tasks than their grade and pay level considered the system to be unfair. For example, the objectives set to higher-grade employees are not necessarily more difficult than those set to lower grade employees, even though the objectives are bases for measuring performance (Suda, 2007). Debroux (2003) suggested that automatic pay increases based on age and tenure are fundamentally incompatible with the planned HRM reform. The only reasonable option is to restructure the employment portfolio and differentiate pay by linking it more closely to the contribution of each category of worker to corporate performance. On this basis, Japanese firms may need to tune the pay distribution by a system covering all employees equally and to design a means of providing appropriate compensation for different categories.

4.5. The Financial Performance of Japanese *Sogo Shoshas*

4.5.1. Sales Volumes

Japanese *Sogo Shoshas* have been concentrating on quantitative growth since their formation by focusing on sales volumes.

(Figure 4.5. Changes of Japanese *Sogo Shoshas'* Sales Volumes) (Unit: US$ million)



Sogo Shsosha	1985	1990	1995	2000	2002	2004	2006	2008
Mitsui	149,001	203,001	147,644	98,248	76,090	93,506	97,156	124,771
Mitsubishi	164,268	166,140	135,203	96,647	78,230	84,602	94,591	109,967
Itochu	140,772	205,327	156,053	94,497	66,499	57,749	51,069	57,104
Sumitomo	131,348	214,036	143,202	89,041	68,479	58,966	54,847	64,856
Marubeni	135,639	182,482	140,674	81,656	59,632	55,305	53,092	62,873
Nissho Iwai	85,524	150,475	90,810	55,273	30,070	-	-	-
Tomen	45,033	63,243	62,100	22,017	14,844	10,304	-	-
Sojitz	-	-	-	-	-	-	11,357	35,331
Toyota Tsusho	-	-	-	-	-	-	25,855	49,357
Average	121,655	169,243	125,098	76,768	56,263	60,072	55,424	72,037

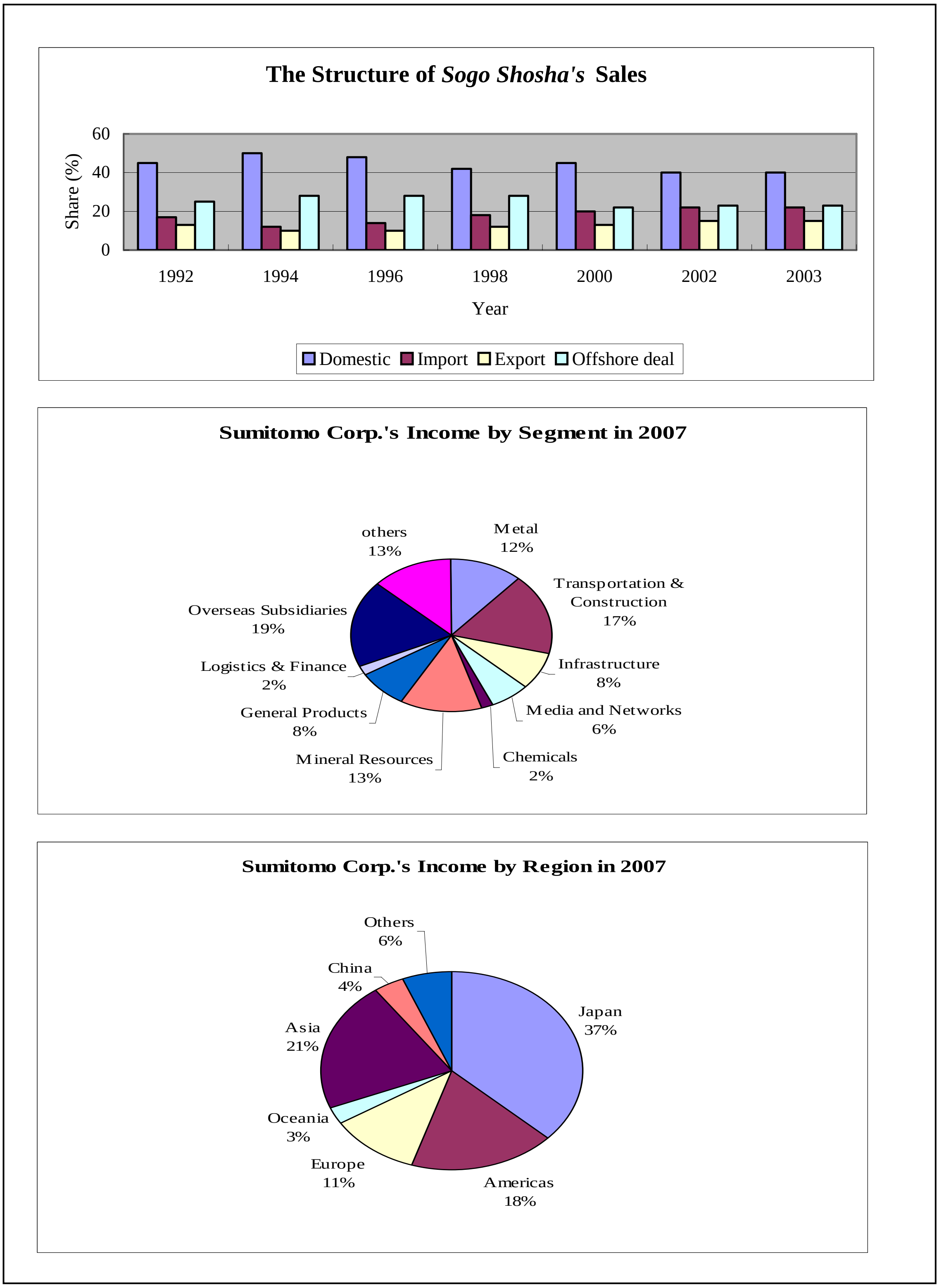
(Source: JFTC (2008), "Financial Results of *Sogo Shoshas*")

- Currency Conversion Rates: 1985: JPY100.00/US$, 1990: JPY100.00/US$, 1995: JPY102.16/US$, 2000: JPY108.49/US$, 2002: JPY122.24/US$, 2004: JPY106.27/US$, 2006: JPY117.12/US$, 2008: JPY98.51/US$ (The Interactive Currency Table: http://www.xe.net)

From 1985 to 1990, seven Japanese *Sogo Shoshas* achieved a constant growth of sales volumes (on average 13.7%) on the back of brisk domestic investment. However, the *Sogo Shoshas'* stable growth trend suddenly headed toward a drastic decline deadlock in 1990 and this situation has continued, due to the collapse of Japan's bubble economy in the early 1990s. The average value of the seven *Sogo Shoshas'* sales volume in 1985 was US$121,655 million. However, it has been gradually declining since 1990 and amounted only to US$56,263 million in 2002. The fundamental causes of the reduction in sales volume were the height of the Japanese yen against the US dollar, disposal of non-profit business units and separation of inefficient business units due to the national economic depression and downturn.

The structure of *Sogo Shoshas'* sales is divided into four areas; domestic sales, exports, imports and offshore dealings (or third country trading). The following figure is the structure of sales from 1992 to 2003. During that period, domestic sales shared 45%, imports shared 17%, exports marked 13% and offshore dealings shared 25%. One notable thing here is that the structure of the *Sogo Shoshas'* sales has been well-balanced and dispersed with domestic sales, imports, exports and offshore dealings since their foundation – a typical sales structure for Japanese *Sogo Shoshas*. Through this structure, the *Sogo Shoshas* gain the advantage of balancing up losses. For example, if there have been big losses in exports, they are compensated by imports, domestic sales and offshore dealings. The income sources, in the case of Sumitomo Corporation from 2007, are roughly divided into nine segments; metal, transportation & construction, infrastructure, media & networks, chemicals, mineral resources, general products and logistics & finance. By geographical region, Sumitomo Corporation's income in 2007 was derived from Japan (37%), Asia (21%), Americas (18%), Europe (11%), China (4%), Oceania (3%) and other regions (6%).

(Figure 4.6. The Structure of *Sogo Shoshas'* Business)



(Source: The Handbook of Japanese *Sogo Shoshas*, 2005; Sumitomo Corporation's Annual Report, 2008)

4.5.2. Profitability

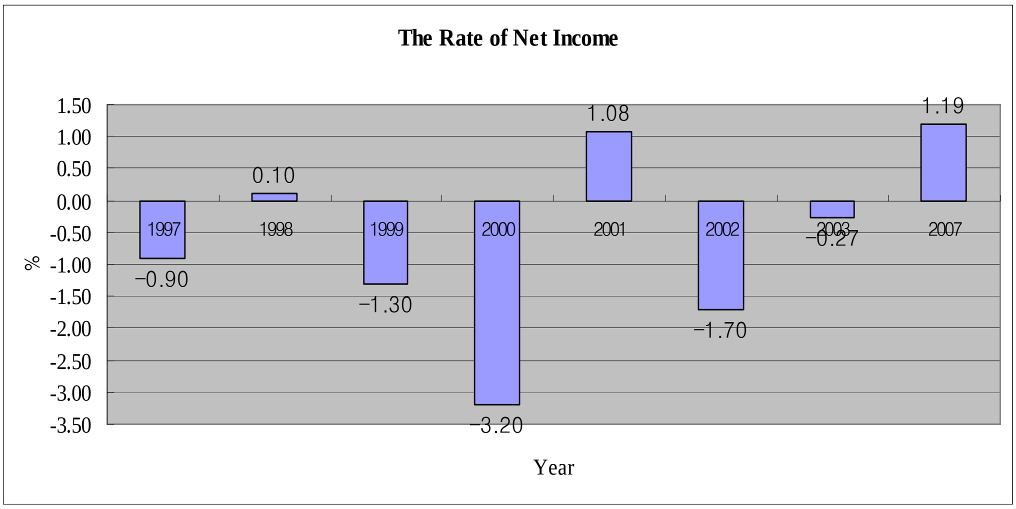
One notable feature of Japanese *Sogo Shoshas'* business is that profitability over the sales amounts is significantly low. This low profitability has probably resulted from the following factors. The first may be their huge dependence on an intermediary or simple broker function between sellers and buyers. The first earning source of *Sogo Shoshas* derives from their function as intermediary, which has been used as the most important one. It earns them commission fees. The commission fee may even now compose the largest part of the revenue earned by trading firms. The commission fee is usually decided between the *Sogo Shoshas* and the confronting firms through numerous factors, such as type of product, quantity, final destination, quality of the products and business relationship between two firms. The second is, on the surface, a purely technical accounting issue (Yamaji, 1991). In reality, *Sogo Shoshas* usually record as sales the trading amounts which they made for the tariff procedure in place of manufacturing firms. Consequently, the sales amounts of the *Sogo Shoshas* do not always represent the real business activities. Unlike manufacturing companies, the *Sogo Shoshas'* profitability is affected by numerous factors. Factors affecting their profitability include type of products and services, geographical diversification, ratio of export items manufactured by the *Sogo Shoshas* group firms and the affiliates and the degree of domestic business operations.

In 2007, the average gross profit and net income of seven *Sogo Shoshas* totalled US$1,316 million (2.24% over revenues) and US$702 million (1.19% over revenues) even though they achieved US$58,836 million in revenues. Moreover, the average net income from 1997 to 2003 was -0.88 % over revenues. The highest was only 1.08% and the lowest one was –3.20% over revenues. These results denote that Japanese *Sogo*

Shoshas still have difficulties in freeing themselves from quantitative growth based on revenues. Some primary factors, such as fierce competition among the *Sogo Shoshas*, changes in the business environment and heavy competition against ordinary trading companies, may cause the profitability of *Sogo Shoshas* to be low. Therefore, they largely tend to expand their revenues at the cost of profitability and commission fee.

(Table 4.12. Profitability of Japanese *Sogo Shoshas* in 2007) (Unit: US$ million)

Sogo Shsosha	Revenues	Gross Profit	**Net Income**
Mitsui (Profit rate)	99,367	1,857 1.87%	**1,033** **1.04%**
Mitsubishi (Profit rate)	94,861	1,666 1.76%	**1,570** **1.66%**
Itochu (Profit rate)	51,699	1,376 2.66%	**824** **1.59%**
Sumitomo (Profit rate)	49,935	1,669 3.34%	**612** **1.23%**
Marubeni (Profit rate)	54,754	1,075 1.96%	**400** **0.73%**
Sojitz (Profit rate)	24,680	567 2.30%	**183** **0.74%**
Toyota Tsusho (Profit rate)	36,558	1,004 2.75%	**292** **0.80%**
Average (Profit rate)	58,836	1,316 2.24%	**702** **1.19%**



(Source: JFTC (2008), "Financial Results of *Sogo Shoshas*")

- Currency Conversion Rates: JPY114.80/US$ (2007))

4.5.3. Stability

A firm's financial stability can be analysed through the reciprocal relationship between assets, debt and equity. A typical method of ascertaining a firm's stability is to analyse the debt ratio, equity ratio and current ratio. Debt ratio indicates what proportion of debt a company has relative to its assets. A debt ratio of greater than 1 indicates that a company has more debt than assets: a debt ratio of less than 1 indicates that a company has more assets than debt. This ratio can help investors determine a company's level of risk.

The equity ratio, for its part, indicates what proportion of equity capital a firm has relative to its assets. A higher equity ratio indicates that a firm's stability is sound. The current ratio, also known as the liquidity ratio, measures a company's ability to pay short-term obligations; it is calculated by dividing current assets by current liabilities. The ratio is mainly used to get an idea of the company's ability to pay back their short-term liabilities (debt and payables) with their short-term assets (cash, inventory, receivables). The higher the current ratio, the more capable the company is of paying its debts.

The following table shows the debt ratio, equity ratio and current ratio of Korean GTCs and Japanese *Sogo Shoshas* in 2007.

(Table 4.13. Comparison of Stability between Major GTCs and *Sogo Shoshas* in 2007)

		Debt Ratio[48] (%)	Equity Ratio[49] (%)	Current Ratio[50] (%)
Korean GTCs	Samsung	101.80	48.50	100.20
	SK	283.00	26.09	77.00
	LG	152.83	39.55	134.26
	Average	**179.21**	**38.04**	**103.82**
Japanese *Sogo Shoshas*	Mitsui	365.02	21.50	133.16
	Mitsubishi	289.22	25.69	130.00
	Sumitomo	472.30	17.47	134.06
	Average	**375.51**	**21.56**	**132.41**

(Sources: Calculated by the author on the basis of 'Balance Sheets' of each company, 2007)

According to this table, the debt ratio and equity ratio of Korean GTCs were much healthier than those of the Japanese *Sogo Shoshas*. But the current ratio was the opposite. In 2007, the average debt ratio of the major *Sogo Shoshas* was 375.51%, which was much higher than the Western management concept. However, the average equity ratio was only 21.56%, which was almost as same as the average equity ratio of all Japanese industries, 20%. With such a low equity ratio, *Sogo Shoshas* had no difficulty in raising funds from domestic and international money markets. In the process of fund raising, most funds are raised by a loan from money markets based on a borrower's level of credit. This capability of raising funds and running effective business activities, with low equity and high credit, may be an intrinsic management

[48] Debt ratio = (debt/equity) x 100
[49] Equity ratio = (equity/assets) x 100
[50] Current ratio = (current assets/current liabilities) x 100

skill of the *Sogo Shoshas*. An extremely high percentage of the liabilities of the *Sogo Shoshas* is composed of current liabilities, in particular, accounts payable, which make up almost half of all liabilities. By carrying such a high percentage of accounts payable, the *Sogo Shoshas* are actually net financiers of trade. What makes it possible, then, for *Sogo Shoshas* to act as financing intermediaries and how do they raise funds from money markets with such a low equity ratio? The reason is their confidence in extending credit stems from the existence of business groups, within each of which is a major bank and general trading company, coupled with their ceaseless creation of diversified new businesses without confining simple intermediaries and broker activities for export and import. In this context, the *Sogo Shoshas* are maintaining financial stability and soundness with a low equity ratio.

With regard to the current ratio, that of the Japanese *Sogo Shoshas* was slightly sounder than that of the Korean GTCs'. The average ratio of the *Sogo Shoshas* was 132.41%, which was slightly higher than the average ratio for all Japanese industries, 110%~120%. The current ratio, as noted above, is mainly used to get an idea of the company's ability to pay back their short-term liabilities (debt and payables) with their short-term assets (cash, inventory, receivables). The higher the current ratio, the more capable the company is of paying its obligations.

4.6. The *Zaibatsu*, *Keiretsu*, *Sogo Shosha* and the Japanese Economy

All Japanese *Sogo Shoshas* belonged to *Zaibatsu* groups (before World War II), or *Keiretsu* groups (after World War II), just as all Korean GTCs belonged to *Chaebols*. Therefore, it will be helpful to review the nature of the *Zaibatsu* and *Keiretsu* and their development, since both of them were developed to discharge the role of *Sogo Shosha*. This section examines several aspects of the *Zaibatsu* and *Keiretsu*, such as their nature, formation, development and characteristics. It also investigates their relationship with the *Sogo Shosha* and its impact on Japan's national economic growth.

4.6.1. The Nature of *Zaibatsu*

- **Formation and Development of *Zaibatsu***

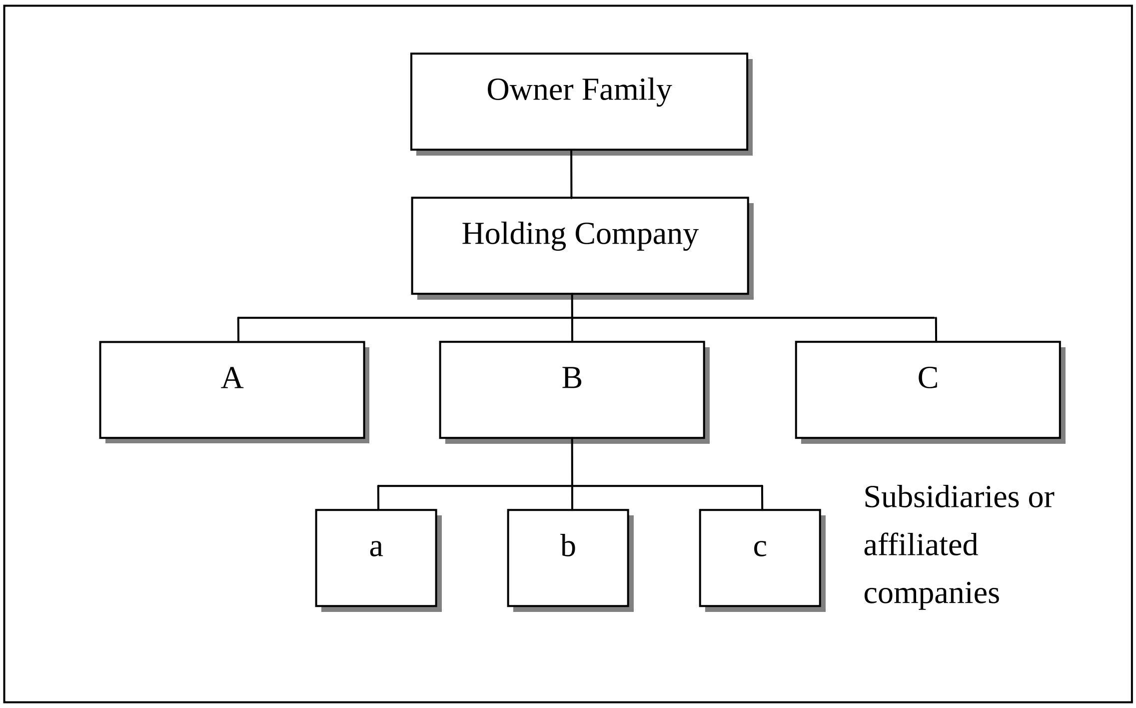
The Japanese term, *Zaibatsu* (literally "financial clique") refers to the great family-controlled banking and industrial combinations of modern Japan. For more than 100 years, Japan's economy was dominated by the *Zaibatsu* and then, after World War II, by the *Keiretsu*. The *Zaibatsu* emerged in the course of Japan's modernisation during the Meiji era and grew rapidly under the patronage of the government. In 1868, the Meiji Restoration took place in Japan, one of the most dramatic turning points in world history. The Meiji leaders noted that in the capitalist nations which they studied wealth was often concentrated in the hands of a few families. As a result, the *Zaibatsu* were able to grow prominently under the patronage of the government. The leading *Zaibatsus* are Mitsui, Mitsubishi, Dai Ichi Kangyo, Sumitomo, Sanwa and Fuyo. They gained positions in the Japanese economy which have no exact parallel elsewhere. Although the Mitsui were powerful bankers under the *shogunate*, most of the other *Zaibatsus* developed after the Meiji restoration, when, by subsidies and a favourable tax policy, the new government granted them a privileged position in the country's economic development. Later they helped finance strategic semi-official enterprises in Japan and abroad, in particular in Taiwan and Korea (Hidemasa, 1992).

In 1937 the four leading *Zaibatsus* directly controlled one-third of all bank deposits, one-third of all foreign trade, half of Japan's shipbuilding and maritime shipping and most of the heavy industries. They maintained close relations with the major political parties. They also contributed to the Japanese war effort in cooperation with the military government from 1931. After Japan's surrender (1945) to the allied forces in World War II, the *Zaibatsus* were eventually dissolved between 1945 and 1947, as part of the resolution of war crimes, but in the 1950s and 1960s groups based on the old *Zaibatsu* re-emerged as the *Keiretsu*. The decision on the part of these groups in the post-World War II era to pool their resources greatly influenced Japan's subsequent rise as a global business power.

- **Characteristics of the *Zaibatsu***

The major *Zaibatsus,* such as Mitsui, Mitsubishi and Sumitomo, have different origins and they also differ in the precise details of their internal constitution and structure. But all were closely linked to the government and military and contributed to the policy of creating a "rich country and a strong army." *Zaibatsu* were the financial face of monopoly capital, whose purpose was to minimise the risks of investment by spreading their capital over a wide and diverse range of industrial sectors rather than concentrating it in a single area of production (Kang, 1996). The *Zaibatsu* had a number of distinctive features which differentiate them from the forms of finance capital in other developed capitalist nations. At the centre of each *Zaibatsu* was the *honsha* or holding company. The ownership structure was that of a pyramid.

(Figure 4.7. The Ownership Structure of *Zaibatsu*: Pyramid Structure)



(Source: Shim, J. S. (2002), "The Evolution of the Korean Economic System: Government, Chaebol, Financial Institutions and the Influence of Japan, PhD Dissertation, The School of Public Policy, The University of Birmingham, p. 97)

Each *Zaibatsu* dominated vertically the business management of its affiliated firms and their subsidiaries through the holding company. The holding company owned most of the stock of the directly affiliated companies and financed them through its own bank. *Zaibatsu* usually owned financial institutions such as banks, trust companies and insurance companies and also the general trading company (*Sogo Shosha*). The financial institutions played the role of capital pipeline for each affiliated firm and the *Sogo Shosha* acted as proxy for the manufacturers in the *Zaibatsu* by purchasing raw materials and by selling products. In group management, even though Mitsui and Sumitomo families participated in company management, the actual power was wielded by professional managers. In the case of Mitsubishi, the heads of families held management power, but the group was also managed by professional managers.

- **The Dissolution of the *Zaibatsu***

Before World War II, the Japanese economy was dominated by four large *Zaibatsus* – Mitsubishi, Mitsui, Sumitomo and Yasuda. They were involved in most key sectors of industries, including steel, banking and international trading and controlled by a holding company which established financial links between the different members (Ito, 1992). However, a dissolution of the *Zaibatsu* was instituted in 1945-7. The main elements of the *Zaibatsu* dissolution programmes were as follows. First, the *Zaibatsu* holding companies and a number of other large holding companies were selected for dissolution. Their stocks were taken over under the occupation policy of the Supreme Command of the Allied Powers (SCAP) and sold to the public. In all, 83 companies were dissolved in this way, including the holding companies of Mitsui, Mitubishi, Sumitomo, Yasuda, Fuji, Nissan, Asano, Okura and Nomura. By offering the stocks of these companies to the public, it was hoped that the *Zaibatsu* would be broken into their component parts, which would then become independent, unrelated companies (Toshio, 1989). Second, members of the old *Zaibatsu* families were prohibited from resuming positions as company officers in the ex-*Zaibatsu* enterprises. This restriction was aimed at breaking the human nexus of semi-feudal control which had lain at the centre of the *Zaibatsu* structure. Third, not only the *Zaibatsu* themselves but even some of their largest component firms were subject to dissolution. For example, the giant *Zaibatsu*-

related *Sogo Shoshas*, Mitsui Bussan and Mitsubishi Shoji were divided into many small enterprises. Last, the 1945 Law Concerning the Prohibition of Private Monopolies and Maintenance of Fair Trade Practice (usually referred to as the anti-monopoly law) was enacted, with the intention of preventing a future rebirth of the *Zaibatsu* (Kang, 1996). After the dissolution of the *Zaibatsu* by the SCAP, six big business groups emerged in their place. They were Mitsui, Mitsubishi, Sumitomo, Fuyo, Sanwa and Dai-Ichi Kangyo Bank (DKB). Each of these firms has vertically or horizontally aligned affiliate and subsidiary firms, a pattern called *Keiretsu*.

4.6.2. The Nature of *Keiretsu*

- **The Emergence of the *Keiretsu***

Notwithstanding the dissolution of the *Zaibatsu*, in 1948 the allied forces realised that they needed a strong Japan to fight the Korean War and international communism. The policy of weakening the Japanese economy was dropped and substantial aid pumped in. Following amendments to the anti-trust laws, many *Zaibatsus* were re-established (Morikawa, 1992). This time, companies grouped round the banks, which were again allowed to hold shares in other companies and this made the establishment of financial links easier (Vohara, 1999). These conglomerates were now called *Keiretsu*. Some (Mitsubishi, Mitsui and Sumitomo) emerged out of the former *Zaibatsu*, but others (Fuyo, Sanwa, DKB, etc.) were just new groupings of companies. Among the big six, Mitsubishi, Mitsui and Sumitomo grew directly out of *Zaibatsu* groups. However, the three other groups – Fuyo, Sanwa and DKB – grew up in the post-war period around prominent city banks; these new groups are sometimes known as the bank groups. Fuyo was built around the former Yasuda Group of companies and DKB inherited many firms from the Fujisawa and Kawasaki Groups. According to Kang (1996), in addition to the “Big Six”, there are also other smaller independent business groups which came into being somewhat later. These include Toyota, Nissan, Hitachi and Shinnitetsu, which are based in manufacturing and Tokyu and Seibu, which are based in the distribution and service sector. These independent industrial and financial groups represent a network vertically integrated in one or more industrial sectors. Independent groups are organised as *Keiretsu*, each consisting of a large, highly successful parent company and vertically aligned subordinate companies. These independent groups developed in the 1950s and 1960s, while Japan’s economy grew rapidly.

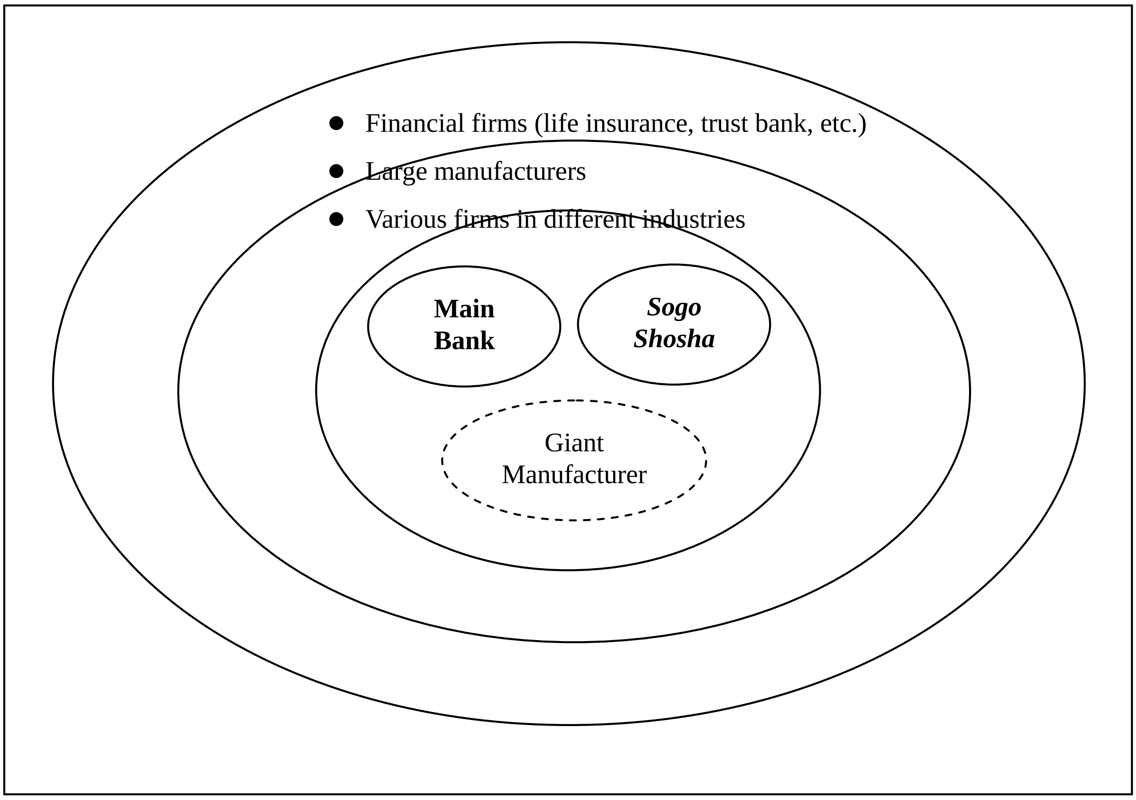
- **Types of *Keiretsu***

There are various ways to classify *Keiretsu*, but the two most common classifications cover all the groups. They are *yoko* (horizontal) *Keiretsu* and *tate* (vertical) *Keiretsu*. A horizontal *Keiretsu* is essentially similar to the structure of the *Zaibatsu*, consisting of a group of large firms in different industries with common ties to a powerful bank, united by shared stockholdings and trading relations. A vertical or pyramid *Keiretsu* is made up of one very large firm and hundreds or thousands of smaller companies subservient to it (Miyashita and Russell, 1994).

i) Horizontal Keiretsu

A horizontal *Keiretsu* is a “financial *Keiretsu*” with horizontal relationships across industries. The Big Six (Mitsubishi, Mitsui, Sumitomo, Fuyo, DKB and Sanwa) belong to this grouping, with close-knit relationships among group members. According to Miyashita and Russell (1994), at the centre of a horizontal *Keiretsu*, there is always a main bank and a *Sogo Shosha* and these are equivalent in influence. There may even be a third firm, a giant manufacturer. Around these two or three giants circle the core members, usually three financial firms – a life insurance company, a non-life insurance company and a trust bank – and one or two very large manufacturers.

(Figure 4.8. The Structure of a Horizontal *Keiretsu*)



(Source: Adapted from Miyashita, K. and Russell, D. (1994), "Keiretsu: Inside the Hidden Japanese Conglomerates", McGraw-Hill, P.84)

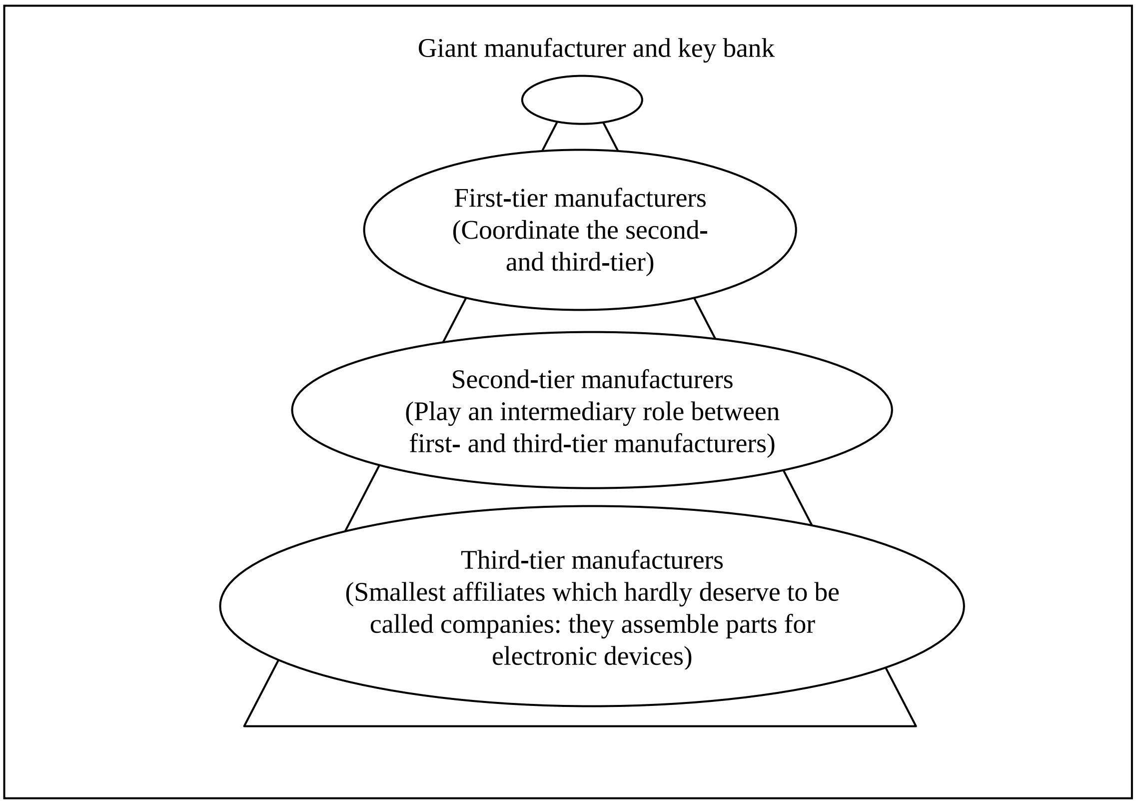
Together, the financial firms, the *Sogo Shosha* and the group's key manufacturers give the *Keiretsu* its identity. In particular, the *Sogo Shosha* is obviously concerned with commerce. It has the vital role of coordinating trade, not only within the group, but among different groups and even with foreign customers. The *Sogo Shosha* also holds equity in many of the group's firms and provides financing in other ways than the banks'.

ii) Vertical Keiretsu

Another form is the vertical or Pyramid *Keiretsu*, made up of one very large company and hundreds or thousands of small companies subservient to it. Generally vertical *Keiretsu* are less influenced by a bank. The advantage of this structure lies in the fact that many subcontractors work as "buffers" for the core firm in economic downturns. According to Miyashita and Russell (1994), vertical *Keiretsu* are more common in manufacturing industries. They are in particular prominent in the electronic and automobile industries, although almost every other field has its own vertical *Keiretsu*, including advertising, publishing, broadcasting and other non-manufacturing businesses.

The figure below shows how vertical *Keiretsu* are organised. In electronics, at the top of the pyramid, there is a giant manufacturer and a key bank, which is more or less equal in status with the manufacturer. According to Shim (2002), the parent firm at the apex of the manufacturing pyramid is responsible for coordinating the vast, complex system of design, manufacture and assembly inside the pyramid and then for advertising the finished products and delivering them to the market. The first-tier subcontractor handles many of the final steps in the production process and also plays an important role in coordinating the second- and third-tier subcontractors. The second-tier manufacturers play an intermediary role between the first- and third-tier manufacturers and the third-tier manufacturers are involved in assembling parts for some electronic devices.

(Figure 4.9. The Structure of a Vertical *Keiretsu:* Electronic Firm)



(Source: Adapted from Shim, J. S. (2002), "The Evolution of the Korean Economic System: Government, Chaebol, Financial Institutions and the Influence of Japan, PhD Dissertation, The School of Public Policy, The University of Birmingham, p. 101)

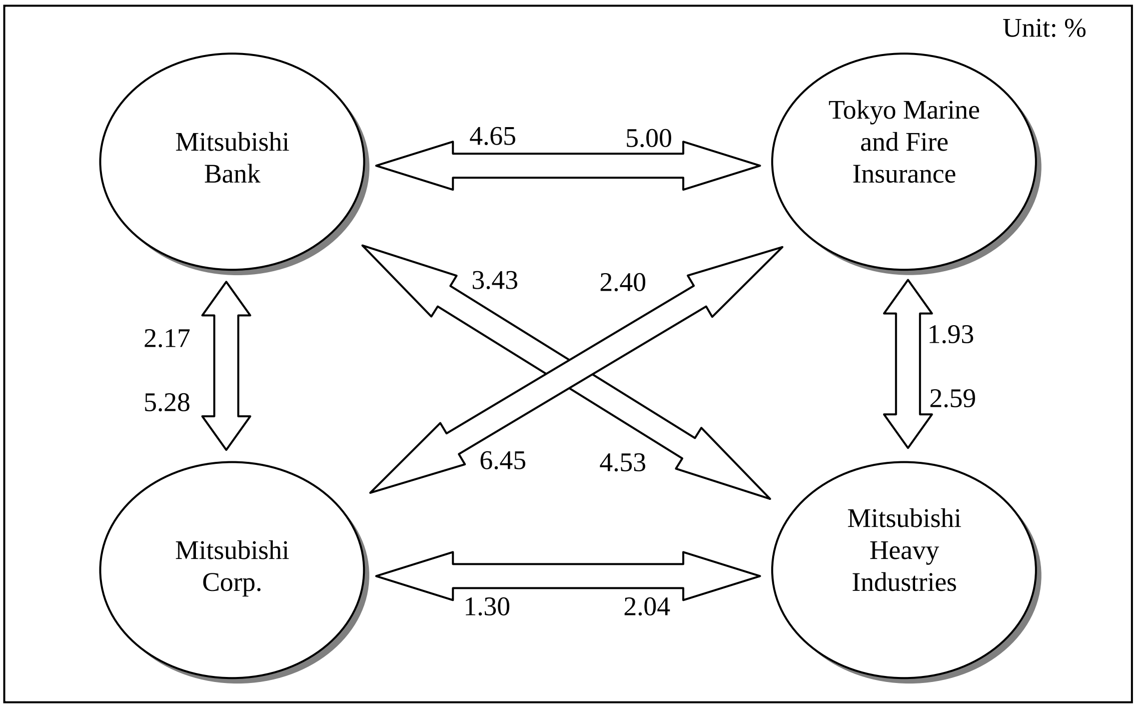
- **The Characteristics of *Keiretsu***

The major characteristics of the horizontal *Keiretsu* are cross shareholding within group members, mutual appointment of officers and key personnel, existence of the *Sogo Shosha* and the formation of presidential councils.

i) Cross Shareholding[51]

A unique system in the *Keiretsu's* ownership structure is cross shareholding. The major objective of cross shareholding is to protect each group company from outside control or takeover threats.

(Figure 4.10. Crossholding of Shares among Four Major Mitsubishi Group Firms)



(Source: Kim, Y.Y. (2007), "Pro-business Policy and Institutional Change of Japan", Korea Economic Research Institute, Research Paper (December), p. 52)

In the Mitsubishi Group, shares of Mitsubishi Corporation (*Sogo Shosha*) are held by its member companies, such as Mitsubishi Bank, Tokyo Marine and Fire Insurance and Mitsubishi Heavy Industries. For instance, Mitsubishi Bank holds 5.28%, 5.00% and 4.53% of Mitsubishi Corporation's, Tokyo Marine & Fire Insurance's and Mitsubishi Heavy Industries' shares, respectively. Mitsubishi Corporation, Tokyo Marine & Fire Insurance and Mitsubishi Heavy Industries hold 2.17%, 4.65% and

[51] For more details of cross shareholding in Japanese firms, see section 4.4.3. Ownership, Corporate Governance and Cross Shareholding

3.43% of Mitsubishi Bank's shares respectively (Kim, 2007). As a result, Mitsubishi Group companies account for about one-third of its total portfolio.

This interlocking shareholding binds Japanese firms into cohesive, horizontal communities. Most of the shares are in the hands of group member firms which are assumed to be cooperative and stable and unwilling to sell the shares to outsiders; if the shareholders were foreign companies, it would be much more difficult to acquire enough shares to gain control of the Japanese firms (Ito, 1996).

ii) Existence of the Sogo Shosha

As mentioned earlier, one of the major characteristics of the horizontal *Keiretsu* is the existence of the *Sogo Shosha*, which acts as the trading arm of the group, achieving huge economies of scale. Not only as a trading arm within the group, but also as a major shareholder of the shares of group members, the *Sogo Shosha* is centred at the heart of the *Keiretsu* together with the bank. In both *Zaibatsu* and *Keiretsu*, one main bank and one *Sogo Shosha* play central roles. The *Sogo Shoshas* originated as trading arms in the international market as well as wholesalers and distributors in the domestic market, due to the huge economies of scale which the *Zaibatsu* and *Keiretsu* could make.

There is one giant *Sogo Shosha* in each of the Big Six *Keiretsu* (i.e. Mitsubishi Group: Mitsubishi Corporation, Mitsui Group: Mitsui and Co., Ltd., Sumitomo Group: Sumitomo Corporation, Fuyo Group: Marubeni Corporation, Sanwa Group: Nissho Iwai Corporation, DKB Group: Itochu Corporation). In all Big Six groups, the *Sogo Shosha* plays the same critical role, helping to coordinate group activities through every aspect of commerce. Most intra-group transactions involve the *Sogo Shosha*. With ties to tens of thousands of Japanese companies, including the *Keiretsu*, the *Sogo Shoshas* play a significant role in Japan's exports and imports, including domestic distribution activities. They are essentially gatekeepers for Japan's economy. According to JFTC's report (2000), in 1993, the nine top *Sogo Shoshas* handled US$124 billion (34.8%) of Japan's exports and US$134 billion (60.8%) of Japan's imports. Their total trade accounted for US$258 billion (44.7%) of Japan's total worldwide trade of US$577 billion. The *Sogo Shoshas*, along with the banks and insurance companies, provide both horizontal and vertical leadership and integrated functions to the *Keiretsu*.

iii) Mutual Appointment of Officers and Key Personnel

The other feature common to the *Keiretsu* is a mutual appointment of officers and other key personnel within the group. Major Japanese *Keiretsus* send their staff members to their subsidiaries and affiliates as top ranking officers. The cross movement of personnel within the group, in particular senior personnel, makes it possible to transfer expertise when member firms move into new areas of operation or occasionally as a source of external discipline (Sheard, 1994). Personnel transfers form a dense and multi-tiered network of labour flows which facilitates information exchange, control, training and learning. Personnel transfers also redistribute labour to balance out surpluses and shortages (Lincoln and Gerlach, 1992).

In addition to capital participation and financing, this system is often used in vertically-integrated groups as a way of strengthening group cohesiveness and control these companies. Horizontally-integrated groups adopt this practice as one of the major centripetal forces. Often, when a member company faces financial difficulty, the major bank of the group sends a member of its staff to the firm as a top executive officer. The average ratio of presidential council members with directors sent by members to the total members varied widely, from just over 40% to almost 100%. The average ratio of directors sent by group members among the six major groups in 1990 was about 60%, with the highest ratio of 97% for Mitsubishi and the lowest of 40% for Mitsui (Dodwell Marketing Consultants, 1994).

iv) Formation of Presidential Councils

The presidents or CEOs within the different members of the *Keiretsu* gather and discuss their business issues in presidential councils known as "*Shacho-Kai*". They convene once a month to exchange information and hear lectures on contemporary topics, such as general economic issues, labour problems, public relations activities, the approval of key personnel appointment at member firms, etc. For instance, 29 company presidents of Mitsubishi group meet every Friday (known as the "Friday Club") (Ito, 1992). However, this council does not want to be a policy-making body for the whole group, a role that the pre-war *Zaibatsu* headquarter or family took on, but instead to be a council which only provides a forum for regular meetings to foster friendship among the presidents of the group. Every member is independent and no one is bound by the decisions or recommendations made by the council (Dodwell Marketing Consultants, 1994).

4.6.3. Japanese Post-War Economic Miracle and the *Keiretsu*

The primary characteristic of Japan's post-war economy is the 15-year period of high growth, beginning in the mid-1950s, which enabled it to catch up with the developed economies of Europe and the US. Japan was a major beneficiary of the swift growth attained by the post-war world economy, under the principles of free trade advanced by the IMF and the General Agreement on Tariffs and Trade (GATT). During this period of high growth, the competitive strength of Japanese industry rose steadily. From the mid-1960s a current balance surplus was achieved throughout the year, with the exception of those years following the oil crisis of 1973. In 1985, with net external assets of US$129.9 billion, Japan moved ahead of the UK to become the world leader (BOJ). During this same period, the US led the world in net external liabilities. Except for 1990, when it was surpassed by Germany, Japan has maintained this position as world leader.

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 success than Japan. The Japanese economic pie grew at an annual rate of 10% from the mid-1950s until the Arab oil shocks of the early 1970s. The Japanese then managed to maintain much more modest but steady growth rates until the early 1990s (Ellington, 2004). Many factors have contributed to Japanese economic growth, such as the international environment, America's contribution, the role of the Ministry of International Trade and Industry (MITI), the role of the *Keiretsu*, state-assisted capitalism, the Korean War, the world free trade boom, the surplus of well-educated workers and a stable political situation. The following are the major contributory factors to Japan's post-war economic growth.

- ***The International Environment of Growth***[52]

Among the many factors of influencing Japan's post-war national rapid growth, the international environment had an extreme influence. According to UN statistics, the volume of world trade tripled between 1955 and 1970, with a growth rate of 7.6%, while it grew at 3.5% from 1870 to 1913 and at only 1.3% in the years from 1913 to 1950 (Maddison, 1964). The worldwide increase in this growth rate had an extremely beneficial effect on Japan's growth. Technological progress and industrial development were of course responsible for the high rate of growth in the world economy. But underlying this was the establishment of the IMF system the purpose of which was to provide infrastructural support for this progress. The IMF system was conceived as a global currency mechanism to replace the international gold standard which had been in use up until that time. The IMF system almost completely correlated with the changes in Japan from the latter half of the 1960s. Japan re-entered the world economy in 1949 and from the time the JPY360/US$1 rate was established until the *yen* revaluation upward in 1971, this rate was consistently maintained. With the JPY360/US$1 rate as the standard[53], Japan's objective at this time was to strengthen its international

[52] Most of this section draws on "The Postwar Japanese Economy: Its Development and Structure" by Nakamura, T. (1981).

[53] One of the major objectives of the IMF was to promote global monetary and exchange stability and it acted as a monitor of the world's currencies by helping to maintain an orderly system of payments between all countries. The main feature of the IMF system was to establish fixed exchange rates between the key currency and the currency of each member country, with a very narrow band within which each of these rates could fluctuate. These fixed rates were not to be changed except for reasons such as a fundamental disequilibrium in the international balance of payments.

competitiveness. During this period, Japan's growth rate gradually rose and it was possible to secure a firm balance of payments surplus.

A further aspect of the international environment beneficial to Japan was the US's contribution. Japan's postwar inflation, unemployment and shortages in all areas seemed overwhelming. It seemed that Japan's immediate economic improvement was not to be achieved on its own. The American government, under the auspices of the SCAP, played a crucial role in Japan's initial economic recovery. SCAP believed that economic development could not only democratise Japan but also prevent the reemergence of militarism. Military hostilities in the Korean peninsula further boosted the economy in 1950 because the US government paid the Japanese government large sums for Special Military Procurement. These payments amounted to 27% of Japan's total export trade. The US also insisted that Japan be admitted to GATT as a temporary member – against British opposition. During the Korean War, SCAP departed and full sovereignty was returned to the government of Japan. Further, a great deal of Japan's trade was with the US, which conducted the largest volume of trade in the world. From the latter part of the 1950s, both export and import trade with the US exceeded 30% of Japan's total export and import trade.

Another aspect of the international environment beneficial to Japan was the availability of cheap and stable supplies of the raw materials and energy needed for heavy and chemical industrialisation. The large-scale development of the most important energy source, oil, began in the Middle East in the 1950s. An adequate volume was taken for granted, for which the price was either stable or falling. Prices of all primary products, in particular iron ore, were also relatively steady. For these reasons, Japan's net terms of trade improved considerably in the latter part of the 1950s, a state of affairs which continued during the 1960s and until the beginning of the 1970s.

- ***The Role of the MITI and Keiretsu***

In the process of Japan's economic development, the MITI[54] was instrumental and it exercised strong administrative leadership over industries in Japan's post-war economic recovery (Nakamura, 1981). The Ministry coordinated various industries, including the emerging *Keiretsu*, toward a specific end, usually toward the intersection of national production goals and private economic interests. In 1954, the economic system which MITI had cultivated from 1949 to 1953 came into full effect. Prime Minister Ikeda Hayato pursued a policy of heavy industrialisation. This policy led to the emergence of over-loaning in which the BOJ issued loans to city banks, which, in turn, issued loans to industrial conglomerates. Because there was a shortage of capital in Japan at the time, industrial conglomerates borrowed beyond their capacity to repay, often beyond their net worth, causing city banks in turn to overborrow from the BOJ. This gave the national BOJ complete control over dependent local banks. The system of over-loaning, combined with the government's relaxation of anti-monopoly laws (a remnant of SCAP control) also led to the reemergence of conglomerate groups called *Keiretsu* which mirrored the wartime conglomerates, or *Zaibatsu*. The *Keiretsu* efficiently allocated resources and became internationally competitive.

Moreover, the distinguishing characteristics of the Japanese economy during the "economic miracle" years included: the cooperation of manufacturers, suppliers,

[54] The MITI was reorganised to the METI (Ministry of Economy, Trade and Industry) in 2001.

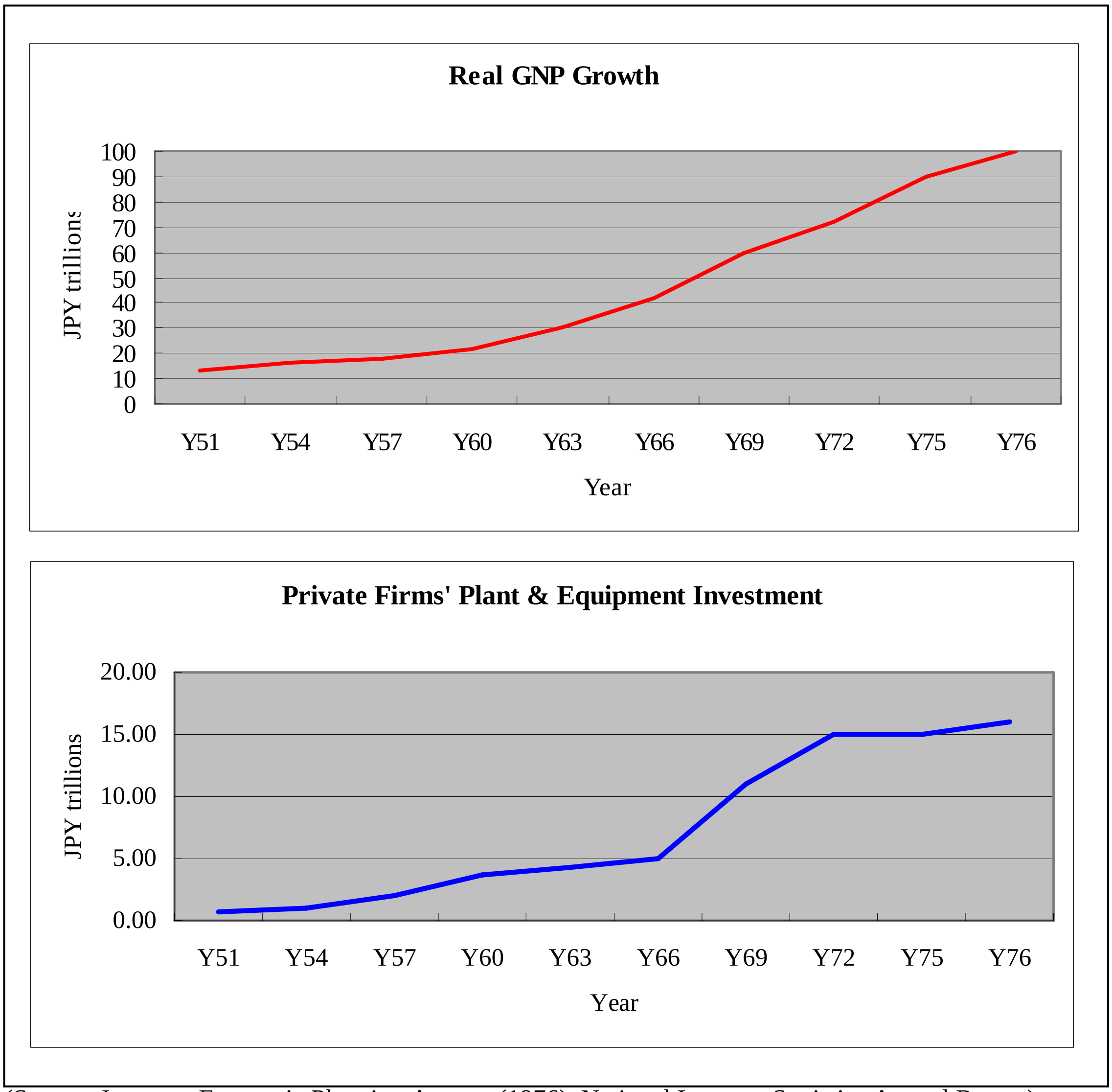
distributors and banks in closely-knit groups called *Keiretsu,* powerful enterprise unions, cosy relations with government bureaucrats and the guarantee of lifetime employment in big corporations. Although some of these reasons are more important than others, many people agree that the *Keiretsu* significantly contributed to Japan's economic rise. The *Keiretsu* are a key feature of Japan's economy, directly or indirectly affecting the economic transactions in both upstream and downstream channels, within and across industries. At the heart of the *Keiretsu* conglomerates' success are the city banks, which lent generously, formalising cross-share holdings in diverse industries. The *Keirestsu* spurred both horizontal and vertical integration, locking out foreign companies from Japanese industries. The *Keiretsu* had close relations with MITI and each other through the cross-placement of shares, providing protection from foreign take-overs. For example, 83% of Japan's Development Bank's finances went toward strategic industries: shipbuilding, electric power, coal and steel production. The *Keiretsu* proved crucial to the protectionist measures which shielded Japan's sapling economy. They also fostered an attitude shift among Japanese managers which tolerated low profits in the short run because the *Keiretsu* were less concerned with increasing stock dividends and profits than with interest payments. Approximately only two-thirds of the shares of a given company were traded, cushioning the *Keiretsu* against market fluctuations and allowing their managers to plan for the long term and maximise market shares instead of focusing on short-term profits.

- ***Rapid Growth Era and Mature Economy***

In the post-war period, the road to economic recovery had begun with the occupation of Japan by the Allied Forces and with the ability of General Headquarters, also known as the SCAP, to exercise indirect control through Japanese government structures. However, when SCAP judged that the Occupation policies could not be implemented through existing government structures, it asked the Japanese government to develop new organisations. The Economic Stabilisation Board (ESB) was thus established in August 1946 and became the "General Headquarters" for economic planning during the critical period immediately after the war. The ESB undertook the tasks of general economic coordination and development of a broad range of policies, covering everything from economic planning, control and prices to food, industry and trade. To begin with, the ESB consisted of five departments and some 300 staff members. But in May 1947, it was expanded to eleven divisions and a permanent staff of about 2,000 and was granted formidable control over the economy (Ishikawa, 1995).

With strong leadership by the ESB, the rare period of worldwide rapid economic growth from the 1950s to the early 1970s was also a period which produced striking changes in Japan's economy, both domestically and in its relationship with the world economy. The following figure shows Japan's real GNP since 1951 and private firms' real investment in plant and equipment. Until the oil shock of 1973, the post-war Japanese economy did not change in an uneven way, but showed virtually a straight line of economic growth (an average annual growth rate of 10%).

(Figure 4.11. Japan's Post-war Economic Growth)



(Source: Japanese Economic Planning Agency (1976), National Incomes Statistics Annual Report)

During this growth period, private firms' investment in plant and equipment showed large increases, growing at a rate of 22% from 1951 to 1973. This was the driving force behind the domestic demand which induced rapid growth and, at the same time, provided the additional productive capacity commensurate with it (Nakamura, 1981). Chemical and heavy industrialisation was, however, the prime mover behind the private firms' investment which supported national economic growth. While chemical and heavy industrialisation itself produced a huge investment demand, it also had a far greater impact than ever before in terms of the derived demand which it generated. Whereas agriculture and light manufacturing had been the mainstay of the economy in the past, this shifted to heavy industry and services. Dominating the industrial sector were iron and steel, ship-building, machine tools, motor vehicles and electronics. With its high economic growth, Japan became the first country in the post-war era to move from “less-developed” to “developed” status. In 1968, Japan’s economy became the world’s second largest, behind only that of the United States. The percentage of Japanese living in cities almost doubled between 1950 and 1970, thus increasing the demands for services. During the 1960s, Japan’s average for exports grew by 18.4% per year (JETRO). This economic growth accompanied tremendous changes in Japan’s industrial structure.

Although high growth rates were predicted for the 1970s, double-digit inflation, the Middle East oil crisis and other factors caused a recession which lowered future growth expectations. This caused a reduction of private investment and economic growth slowed to an average of 3.6% from 1974 to 1979 with, however, a slight increase in the 1980s to 4.4%. In spite of the oil crisis, Japan’s major export industries remained competitive by cutting costs and increasing efficiency. The energy demands were reduced and the automobile industry was able to improve its position globally, by manufacturing lighter and more economical vehicles. The second oil crisis in 1979 created a shift in Japan’s industrial structure from its former emphasis on heavy industry to the development of new fields, such as computers and semiconductors, along with other technology and information-intensive industries.

- ***Bubble Economy and Its Causes***

Following the 1985 Plaza Accord, in the fixed exchange rate system the Japanese yen rose sharply in value over the next few years, to three times its value in 1971. With the increase in the price of Japanese exports, the competitiveness of Japanese products overseas declined, although government financial measures increased demand domestically. Corporate investment rose sharply in 1988 and 1989. New equity issues rose in value as a result of higher stock prices, thus making them an important source of financing for corporations (BOJ). In the meantime, banks sought funds in the outlet of real estate development. In turn, corporations used their real estate holdings as collateral for stock market speculation. A direct result of this was the doubling of land value prices and a 180% rise in the Tokyo Nikkei Stock Market Index. In May 1989, the government tightened its monetary policies to damp down a rise in value of assets, such as land. However, higher interest rates sent stock prices on a steady spiral down. By the end of 1990, the Tokyo Stock Market had fallen 38%, thus effectively wiping out JPY300 trillion (US$2.07 trillion) in value and land prices dropped steeply from their speculative peak. In May 1991, Japan's "Bubble Economy" of inflated land and stock prices came to a crashing halt, sending the country into a prolonged recession from which it has still not recovered (Kojima, 1999).

Now the causes of Japan's economic depression need to be examined. One of the major reasons for Japan's economic crisis is the hollowing out of its manufacturing base (Bailey and Sugden, 2007). Hollowing out[55] (*Kudoka* or de-industrialisation) has been a

[55] For more information about "Hollowing Out", see the book "Crisis or Recovery in Japan: State and Industrial Economy" edited by Bailey, D., Coffey, D. and Tomlinson, P., Edward Elgar, Cheltenham, 2007, pp. 61~81 and 133~156

key feature of Japan's economic depression during the 1990s and early 2000s. The problems afflicting the *Keiretsu* and the hollowing out of Japanese manufacturing have been widespread across the nation; during the 1990s, all industrial sectors experienced a significant decline in real output (approximately 10%), the number of business establishments (a fall of 15%) and employment (a fall of 15%). (Cowling and Tomlinson, 2007).

Opinions differ about the causes of Japan's hollowing out. Ozawa (1996, 1997) sees Japan as suffering from the "Japan disease" caused by excessive government involvement. The problem is seen as something caused by a long-term, sustained rise in the value of the Yen, leading to over-appreciation. This has been stimulated by the export competitiveness of manufacturing sectors, coupled simultaneously with barriers to imports arising from government intransigence against deregulation. Eventually, this has led to outward FDI and hollowing out. Ozawa (1997) argued that an industrial policy aimed at building up manufacturing at home under protection and promotion was ultimately "futile" because this competitiveness drove up the value of the Yen and of wages, eventually making home production less attractive and forcing domestic firms to relocate their production activities overseas.

However, in contrast to the view that the depression was caused by government failures, Cowling and Tomlinson and Bailey (2007) laid the blame on Japan's multinational enterprises, whose strategy failed in the hollowing out process. They argued that Japan's economic crisis was a classic example of the deficiencies associated with transnational monopoly capitalism. The government policy deliberately focused on strategic decision-making in elites within giant firms. These elites were then able to capture aspects of policy in the pursuit of their corporate strategic goals. This allowed firms to become transnational and to shift operations to lower-cost locations, while keeping their home markets protected through import controls. This was what led to the hollowing out of Japan's economy (Bailey and Sugden, 2007).

4.6.4. Future Growth of Japan's Economy

Since the recession bottomed out in 1993, Japan's economy has been making a slow recovery. For the prospect of Japan's future growth, economists and scholars have suggestions both from the government policy aspect and from the industrial sectors aspect.

Katz (1998) suggested that "development state" policies should be avoided. In other words, avoiding strategic failure requires setting in train a framework for developing in a way which reflects broader community interests. According to Bailey and Sugden (2007), the strategy in the interests of Japanese multinational corporations was not in the interests of the wider community or in the public interest. They emphasised the importance of reinforcing a common end-goal, to move Japan away from the government-backed, transnationals-inspired strategic failure experienced through the hollowing out of its manufacturing base, towards an economic system characterised by a more decentralised governance structure, which recognises the positive freedom of varied decision-making. These suggestions need to be consistent with moves to deregulate carefully the inner-dependent sectors, so as to open up to imports and thus to alleviate the problems of perennial trade surpluses and Yen appreciation.

From the viewpoint of industrial sector, Odagiri (2007) suggested the importance to this sector of science-based innovations. As business environments changed, Japanese firms started to realise that it was no longer possible to depend upon technologies imported from abroad and that they had to pursue further growth with their own innovatory products and processes. He further stressed the importance of i) university-industry collaboration as essential for science-based innovation, ii) the promotion of start-ups provided with debt guarantees and subsidies and iii) the need of R & D in, for example, the biotechnology or pharmaceuticals industries.

These suggestions taken together could ultimately contribute to sustainable economic development in Japan.

4.7. Conclusion and Discussion

Like Korean GTCs, Japanese *Sogo Shoshas* have also have devoted themselves from their earliest stages to protecting their country's industry from the West and to further developing the national economy. However, Japanese *Sogo Shoshas* have also been faced with reorganising themselves through strategic management since the collapse of the bubble economy in the early 1990s.

As reviewed, both Korean GTCs and Japanese *Sogo Shoshas* since their foundation have been constantly developing in alignment with the government's economic policy. But rapidly changing business environments did not favour their future business activities. In the case of the Korean GTCs, the national economic crisis treated Korea's industries, including the GTCs industry, harshly. As a step to surviving in such business conditions, Korean GTCs have been forced to restructure their organisational system to increase their competitiveness. Furthermore, the government has not been very much involved in the GTCs business and even small and medium-sized manufacturers were often able to manage their international exports or imports business by themselves and not through GTCs. Similarly, the Japanese *Sogo Shoshas* have been faced with such difficulties since the early 1990s.

As in the introduction and background sections, this chapter, together with Chapter 3, was devoted to analysing Korean GTCs and Japanese *Sogo Shoshas*, for example, their origin, development, characteristics, management system, financial performance and contribution to national economic growth. Since the ultimate purpose of this study is to examine the strategic management and decision-making process of Korean GTCs and Japanese *Sogo Shoshas*, the descriptions in these two chapters provide the background for subsequent chapters.

With this in mind, the next chapter will examine the strategic management of the Korean GTCs and Japanese *Sogo Shoshas* and seek to show how they became competitive organisations in the rapidly changing business environment of the global markets.

CHAPTER 5. THE STRATEGIC MANAGEMENT OF KOREAN GTCS AND JAPANESE *SOGO SHOSHAS*

5.1. Introduction

The modern business environment of the organisations can be described as "uncertain" (Lawrence and Lorsch, 1967; Duncan, 1972; Pennings, 1981; Milliken, 1987; Krickx, 2000) and "complex" (Hage and Dewar, 1973; Lawrence and Lorsch, 1967). Like many other organisations, the Korean GTCs and Japanese *Sogo Shoshas* have been surrounded by environmental uncertainty. Although they devoted various activities to further national economic growth, the macro and micro environmental variables did not favourably influence their strategic management. The major macro environmental variables affecting their business can be summarised as: i) the financial crisis in the late 1990s in Korea, ii) the collapse of the bubble economy which started in the early 1990s in Japan, iii) the globalisation and liberalisation of the national economy and iv) the abolition of assistance by the governments. Micro environmental variables, such as high competition between the existing firms and SMEs' independent business also influenced the GTCs'/*Sogo Shoshas'* management.

The environment for the GTCs/*Sogo Shoshas* does not tend to be stable, but is perpetually changeable. Once the environment changes, the existing strategy and structure may no longer be an effective means for creating competitive advantage over rivals. Thus, a firm's managerial strategy and organisational structure should be re-designed to fit the changed environment. Even if the GTCs/*Sogo Shoshas* have any specific type of strategy for achieving their managerial goals effectively, their success may greatly depend on whether the chosen strategy is fit for the environment at the time.

Moreover, supposing that the strategy is designed to fit the environment, it is crucial to construct a suitable structure to fit the chosen strategy. Lynch (2000) stressed that there needs to be a matching process between the organisation's strategy and its structure and these two elements should be consistent with each other in order for a firm to be economically effective. The characteristics of Korean GTCs' structure are centralisation and formalisation. They are power-centralised, vertically and hierarchically organised entities. Most decision-making power and authority are concentrated in top management. This system may hinder the free flow of opinions and ideas from low-level employees and the centre of the organisation becomes increasingly isolated from the place where decisions are needed and can best be made. These GTCs also emphasise formalisation. Employees within them are controlled by job, workflow and rules.

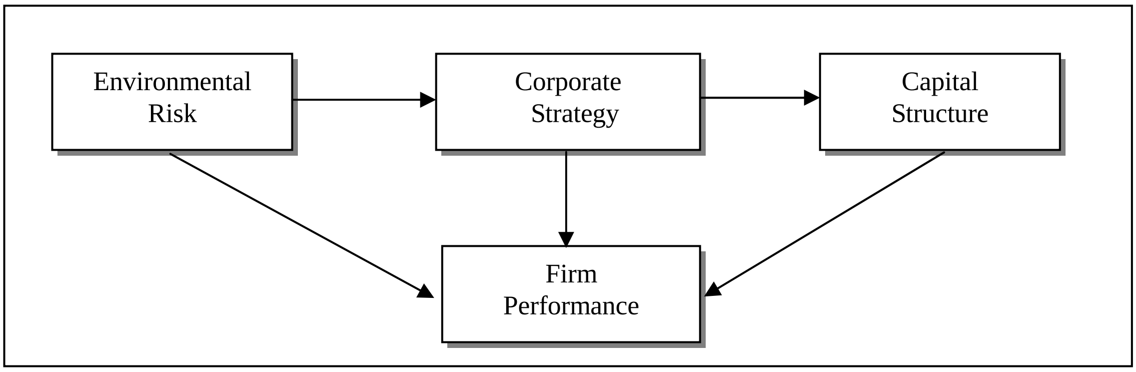
The GTCs'/*Sogo Shoshas'* performance is not, of course, the work of a single factor, but achieved by a combination of diverse elements: the environment, strategy and structure. With this argument in mind, this chapter attempts to examine how Korean GTCs and Japanese *Sogo Shoshas* have become competitive organisations in the global market and how they can achieve their management goals. First, it reviews the theoretical background and literature to establish a conceptual framework of this study. Second, it addresses the research objectives and questions and presents a model. Third, it derives hypotheses based on the literature survey. Fourth, it introduces the research design and methodology. Last, it presents the results of the data analysis.

5.2. Theoretical Background and Literature Review

Analysing the relationship between the business environment, competitive strategy, organisational structure and performance has traditionally been considered one of the main tasks in the area of strategic management. A number of studies have been established to explore the structural relationship of these four elements: between the environment and strategy (Miller, 1988; Govindarajan, 1988; Krickx, 2000), between strategy and structure (Chandler, 1962, Lynch, 2000), between strategy and performance (Gyampah and Acquaah, 2008), the linkages between the environment, strategy and structure and the impact of fit between these three constructs on a firm's performance. (Grinyer, Ardekani and Bazzaz, 1980; Miller, 1988; Chang and Choi, 1988; Kwon *et al*., 1999; Kang, 2002; Chathoth and Olsen, 2007).

Most previous studies have emphasised the importance of strategic fit between all of elements. Strategic fit is developing strategy by identifying opportunities in the business environment and adapting resources and competences so as to take advantage of them (Johnson, Scholes and Whittington, 2005). For a firm to be economically effective, it needs to ensure that all elements are consistent with each other. For example, a firm's performance is not dependent on one element only, but can be achieved through combination of all elements. Chathoth and Olsen (2007) used a co-alignment framework to explain strategic management. Their model postulates that performance is dependent on all such factors as environmental risk, corporate strategy and capital structure. In turn, the environment influences strategy and strategy then impacts on capital structure.

(Figure 5.1. A Co-alignment Model of Performance)



(Source: Chathoth, P.K. and Olsen, M. D., (2007), “The Effect of Environment Risk, Corporate Strategy and Capital Structure on Firm Performance”, Hospitality Management, Vol. 26, p. 504)

This section reviews some research relating to each element that affects a firm’s strategic management. First, it reviews the literature relating to the concept and process of strategic management, which is the basic framework of this research. Second, literature relating to four elements: the environment, competitive strategy, organisational structure and firm’s performance is reviewed. Finally, some earlier studies will be examined.

5.2.1. Literature relating to the Strategic Management: Concept and Process[56]

First of all, the nature of strategic management in general should be reviewed in order to establish the overall framework before discussing each element of this research – the environment, strategy, organisational structure and performance.

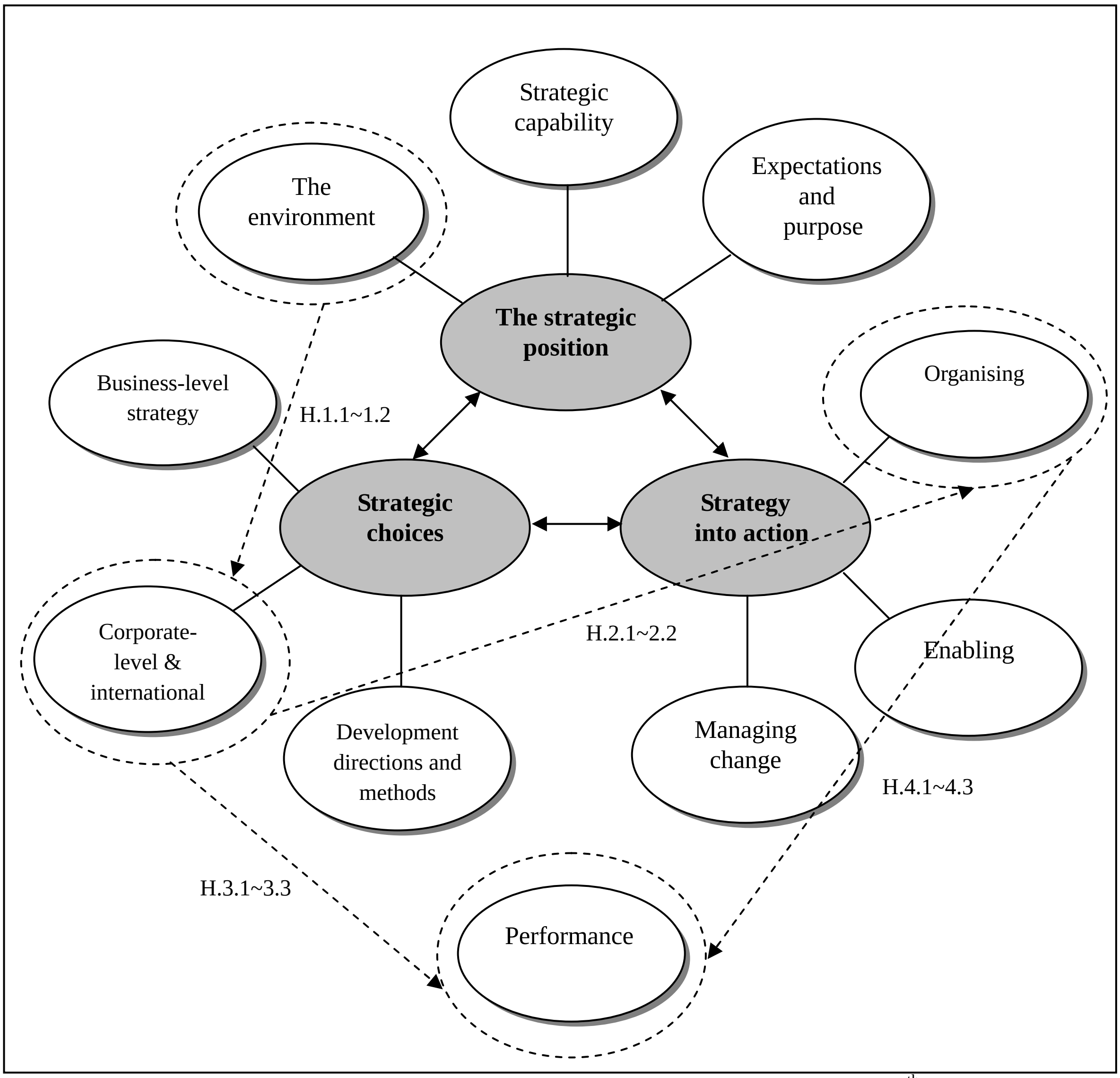
Strategic management is that set of managerial decisions and actions which determines the long-run performance of a corporation. It includes environmental

[56] Most of this section draws on “Exploring Corporate Strategy” (7th Edition, Prentice Hall) by Johnson, Scholes and Whittington (2005).

scanning (both external and internal), strategic formulation (strategic or long-range planning), strategy implementation and evaluation and control. Therefore, the study of strategic management emphasises the monitoring and evaluating of external opportunities and threats in the light of a corporation's strengths and weaknesses (Wheelen and Hunger, 2007). Strategic management includes understanding the strategic position of an organisation, strategic choices for the future and turning strategy into action. It is concerned with deciding on strategy and planning and the way in which the selected strategy is to be put into effect through three basic management concepts: the strategic position, strategic choices and strategy into action.

The strategic position, one of the elements of the strategic management process, is concerned with the impact of strategy on the external environment, internal resources and competences and the expectations and influence of stakeholders. The sort of question which this raises is central to future strategy. What changes are going on in the environment and how will they affect the organisation and its activities? What are the resources and competences of the organisation and can these provide special advantages or yield new opportunities? What is it that those people and groups associated with the organisation aspire to and how does this affect what is expected to be the future development of the organisation?

(Figure 5.2. The Elements of Strategic Management Process)



(Source: Johnson, Scholes and Whittington, (2005) "Exploring Corporate Strategy", 7th edition, Prentice Hall, p. 16)

● Note: Each element circled with a dotted line on the above diagram is a main element in the present study. Hypotheses for each subject are to be derived on the basis of the literature survey. For more details, see section 5.3.2. Research Model.

Strategic choices involve understanding the underlying bases for future strategy at both the corporate and business unit levels and the options for developing strategy, in terms of both the directions in which strategy might move and the methods of development.

There are three levels of strategy in the typical large multidivisional business corporation: corporate-level strategy, business-level strategy and operational/functional strategy. Corporate-level strategy is concerned with the overall purpose and scope of an organisation and how value will be added to the different parts of the organisation. This could include issues of geographical coverage, diversity of products/services or business units and the way in which resources are to be allocated between the different parts of the organisation. Corporate-level strategy typically fits within the three main areas of stability, growth and retrenchment. Carpenter and Sanders (2007, pp. 9~10) argued that this strategy addresses issues related to three fundamental questions; i) In what businesses will we compete? ii) How can we add value to our various lines of business? and iii) How will diversification or our entry into a new industry help us to compete in our other industries?

Business-level strategy, often called competitive strategy, is about competing successfully in particular markets and how to improve the competitive position of a firm's products or services within the specific industry or market segment. Business-level strategy usually operates at the business unit or product level and it emphasises the improvement of the competitive position of a corporation's products or services in the specific industry or market segment served by that business unit. This level of strategy may fit within the two overall categories of competitive or cooperative strategies. Porter's (1980) generic strategies – low price strategy, differentiation strategy and focus strategy – are typical examples of business-level or competitive strategies.

Operational/functional strategy is concerned with the way in which the component parts of an organisation effectively deliver the corporate- and business-level strategies in terms of resources, processes and people. This level of strategy is concerned with developing and nurturing a distinctive competence to provide a company or business unit with a competitive advantage.

Strategy into action is concerned with ensuring that strategies are working in practice. To support successful performance, it is necessary to structure the organisation. This includes functional structures, organisational processes, boundaries and relationships and the interaction between these elements. Strategy very often involves change. Therefore, it is crucial to manage change. This includes the need to change day-to-day routines and cultural aspects of the organisation and to surmount political barriers to change.

From the GTCs' and *Sogo Shoshas'* viewpoint, planning the strategy can become complex and time consuming because they are large and multidivisional organisations. According to Wheelen and Hunger (2007), it often takes slightly more than a year for a large organisation to move by strategic planning from situation assessment to a final decision agreement. Because of the relatively large number of people affected by a strategic decision in a large firm, a formalised, more sophisticated system is needed to ensure that strategic planning leads to successful performance. Otherwise, top management becomes isolated from developments in the business units and lower managers lose sight of the corporate mission and objectives.

So far, this chapter has scanned the nature of the strategic management process, which is the basic framework of this research. Within this framework, it selected four elements – the environment, business-level/competitive strategy, organisational structure and performance – as the subjects of research. These elements are to be applied to Korean GTCs and Japanese *Sogo Shoshas* in order to analyse the structural relationship between them. The following section will focus on reviewing texts which relate to these four elements.

5.2.2. Literature relating to the Environment

The modern business environment for firms can be summarised as uncertain, complex, dynamic, diverse and rapidly changing. Thus, the environment for most organisations will become less predictable in the future. Such uncertainty, degree of complexity and degree of change are threats to all managers attempting to think strategically and the success of an organisation's future will heavily depend on the right and immediate responses to external environmental changes. Wheelen and Hunger (2007, pp. 89~90) explain today's business environment as follows:

> *"Most industries today are facing an ever-increasing level of environmental uncertainty. They are becoming more complex and more dynamic. Industries that used to be multidomestic are becoming global. New flexible, aggressive, innovative competitors are moving into established markets to erode rapidly the advantages of large previously dominant firms. Distribution channels vary from country to country and are being altered daily through the use of sophisticated information systems. Companies learn to quickly imitate the successful strategies of market leaders and it becomes harder to sustain any competitive advantage for very long".*

Environmental uncertainty is the degree of complexity plus the degree of change existing in an organisation's external environment. Wheelen and Hunger (2007) stressed that, as more and more markets become global, the number of factors which a company must consider in any decision increases, making the decision more complex. Environmental uncertainty is a threat to strategic managers because it hampers their ability to develop long-term plans and to make strategic decisions to keep the corporation in equilibrium with its external environment. Yet environmental uncertainty can be an opportunity, because it creates a new playing field in which creativity and innovation can play a major part in strategic decisions. Dynamism or volatility is the frequency of environmental change coupled with the unpredictability of market factors. Complexity refers to the number and diversity of competitors, suppliers, buyers and other environmental actors which firm decision-makers must consider in formulating their strategies (Kabadayi, Eyuboglu and Thomas, 2007).

The effect of uncertainty in organisations was recognised by Barnard (1938), March and Simon (1958). Earlier studies focused on the role of uncertainty in shaping structure and organisational processes (Cyert and March, 1963; Thompson, 1967). More recent work on uncertainty attempted to dimensionalise the concept in order to recognise its complex and multidimensional nature (Krickx, 2000). According to Grinyer, Ardekani and Bazzaz's (1980), who analysed the linkages between the environment, strategy, structure and financial performance in 48 UK companies, a firm's performance is not determined by a single factor, but achieved by a combination of very diverse elements; the environment, strategy and structure. Therefore, the environment surrounding organisations is one of the most important elements in strategic management and it is vitally important to analyse the environment surrounding the firm because environmental analysis helps to develop sustainable competitive advantage, identifies opportunities and threats and may provide opportunities for productive co-operation with other organisations when the firm establishes a specific corporate strategy.

Uncertainty is a key concept for organisation theory and strategic management (Krickx, 2000). The three most common definitions of “environmental uncertainty” cited by organisation theorists are:

1. *An inability to assign probabilities as to the likelihood of future events (Duncan, 1972; Pfeffer and Salancik, 1978; Pennings, 1981),*
2. *A lack of information about cause-effect relationships (Lawrence and Lorsch, 1967; Duncan, 1972) and/or*
3. *An inability to predict accurately what the outcomes of a decision might be (Hickson, Hinings, Lee, Schneck and Pennings, 1971; Duncan, 1972).*

Milliken (1987) identified three types of perceived uncertainty about the environment: state uncertainty, effect uncertainty and response uncertainty. Uncertainty about the state of the environment means that one does not understand how the components of the environment might be changing. Effect uncertainty is defined as an inability to predict what the nature of the impact of a future state of the environment or environmental change will be on the organisation. Finally, response uncertainty is a lack of knowledge of response options and/or an inability to predict the likely consequences of a response choice.

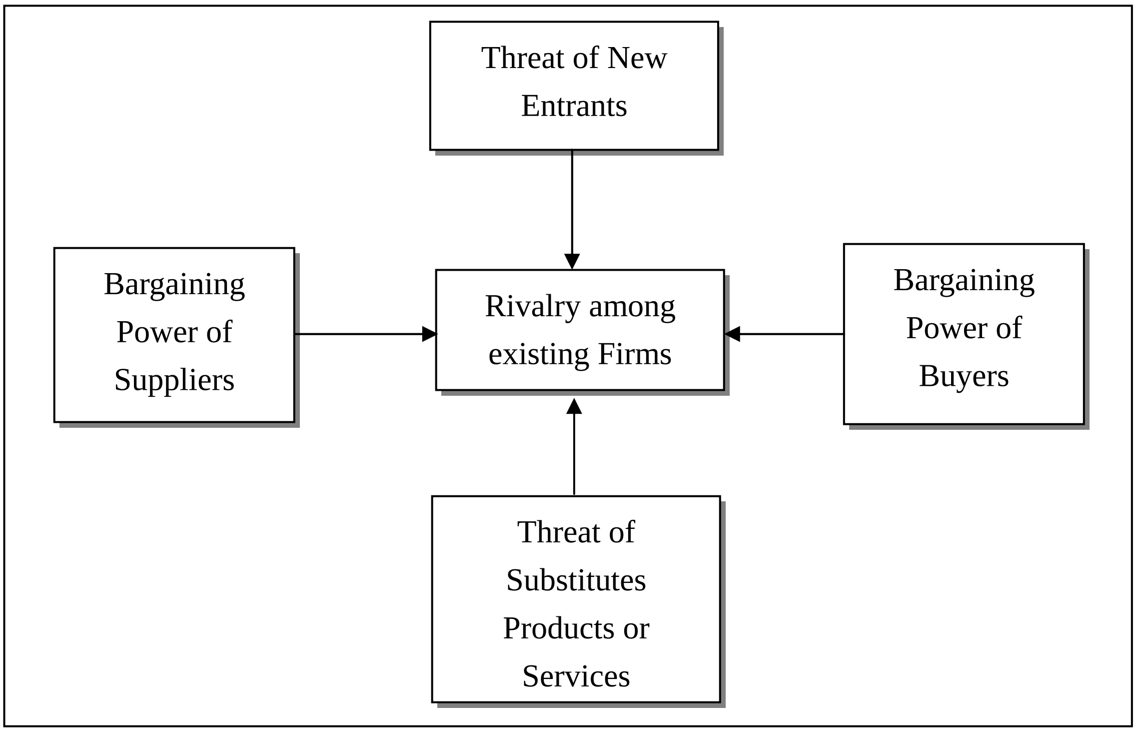
Environmental variables can be divided into two categories: those from the external environment and those from the internal environment. The external environment again consists of two elements: the societal environment, often called the macro environment and the task environment, often called the micro or competitive environment.

External environment scanning is concerned with macro environment analysis, competitor analysis, market analysis, governmental analysis, supplier analysis and interest group analysis. Mavondo (1999) pointed out that the macro environment is generally divided into the demographic, political/legal, technological and natural environment. The basic assumption is that what happens in the broader environment has significant implications for organisational functions. The macro environment introduces a degree of homogeneity in a given industry through similarities in regulatory pressures, strategic alliances, human capital transfers, social and professional relationships and competency blueprints. (Oliver, 1997). Internal environment scanning is concerned with identifying and assessing the strengths and weakness of an organisation. In an internal environment scanning process, the organisation needs to be carefully examined so as to identify and assess resources and capabilities/competences (Slater, 2005).

One of the techniques for scanning the macro environment is the PESTEL analysis, which consists of political, economic, socio-cultural, technological, environmental and legal variables. This helps managers gain a better understanding of the opportunities and threats which they face and consequently aids them in building a better vision of the future business landscape (Carpenter and Sanders, 2007). According to Johnson, Scholes and Whittington (2005), the potential benefits of macro environmental scanning are, *inter alia*, as follows: it increases managerial awareness of environmental changes, it enhances strategic planning by enriching market analysis and it provides time to anticipate changes and develop responses to them.

In addition to the macro environmental analysis, there is a need to focus more closely and move from environmental to industry analysis. Porter (1980, 2008) argued that the essence of formulating competitive strategy is relating a company to its environment and the key aspect of the firm's environment is the industry or industries in which it competes. The state of competition in an industry depends on five basic competitive forces, which are shown in the following figure.

(Figure 5.3. The Five Forces which Shape Industry Competition)



(Source: Porter, M.E. (2008), "The Five Competitive Forces that Shape Strategy", Harvard Business Review, January, 2008, p. 80)

From a strategic management perspective, it is useful for managers in any organisation to understand the competitive forces acting on and between organisations in the same industry. This may inform important decisions about product, market strategy and whether to leave or enter an industry. According to Porter (2008), understanding the competitive forces and their underlying causes reveals the roots of an industry's current profitability while providing a framework for anticipating and influencing competition over time. New entrants to an industry bring new capacity and a desire to gain market share which puts pressure on prices, costs and the rate of investment necessary to compete. Rivalry among existing competitors takes familiar forms, including price discounting, new product introducing, advertising campaigns and service improvements. Rivalry occurs because one or more competitors either feels under pressure or sees the opportunity to improve his position. Moreover, all firms in an industry are competing with industries producing substitute products and buyers and suppliers also compete with the industry by forcing down prices for higher quality goods and services or raising prices for goods of lower quality.

From the GTCs'/*Sogo Shoshas'* point of view, both have been surrounded by macro and micro environmental uncertainty and complexity. For instance, the financial crisis in the late 1990s in Korea and the collapse of the bubble economy starting in the early 1990s in Japan as major macro environmental variables greatly influenced their performance. The globalisation and liberalisation of the national economy and the abolition of government assistance also affected them. Micro environmental variables, such as high competition between existing firms and SMEs' preference for their own independent business also influenced the GTCs'/*Sogo Shoshas'* management.

5.2.3. Literature relating to Competitive Strategy

The ultimate goal of an organisation is to create and retain competitive advantage over its competitors. Competitive strategy, often called business-level strategy, is the basis on which a business unit may achieve competitive advantage in its market and is concerned with developing market opportunities, new products and services. At the same time, there are many sources of competitive strategies to achieve, develop and sustain competitive advantage. The concept of competitive advantage has been examined by many people in the following theories; generic strategy theory (Porter, 1985, 1986), global management strategy theory (Kogut, 1985; Bartlett and Ghoshal, 1998), resources-based theory (Mahoney and Pandian, 1992; Johnson, Scholes and Whittington, 2005; Enz, 2008) and FDI theory (Hymer, 1960; Kindleberger, 1969; Dunning, 1980; Wells, 1983).

- ***Generic Strategy Theory***

To exceed average performance within an industry, Porter (1985, 1986) argued that a firm should possess firm-specific advantages: low cost or differentiation. According to him, the nature of competitive advantage is a function of either providing comparable buyer value more efficiently than competitors (low cost), or performing activities at comparable cost but in unique ways which create more buyer value than competitors do and hence, command a premium price (differentiation). The source of a firm's competitiveness in an industry springs from its specific competitive advantage, which is one of two possible basic types: low cost and differentiation. These two basic competitive advantages originate from a firm's activities and linkages within the value chain.[57] Through optimisation, configuration and coordination within the value chain, a

[57] Porter argued that the value chain provides a systematic means of displaying and categorising activities. The activities performed by a firm in any industry can be grouped into nine generic categories. These generic categories of activities can be grouped into two broad types: primary activities (inbound logistics, operations, outbound logistics, marketing and sales and service) and support activities (firm infrastructure, human resource management, technology development and procurement). Activities in a firm's value chain are not independent, but connected through linkages. The way in which one activity is performed frequently affects the cost or effectiveness of other activities. For instance, if more is spent on the purchasing of a raw material, a firm may lower the cost of its fabrication or assembly.

firm is able to achieve low cost and differentiation advantages. Therefore, a firm must optimise, configure and coordinate such linkages according to its strategy in order to achieve competitive advantage in global strategy. In order for a firm to achieve above-average performance in an industry, the two basic types of competitive advantage are divided into three generic strategies: cost leadership, differentiation and focus.

Cost leadership refers to the ability of a firm to establish a clear cost advantage relative to its competitors. A firm which can produce substantially similar products at lower costs has a significant competitive advantage. With a cost advantage, a firm can sell products for less while still maintaining the same margins as rivals (Carpenter and Sanders, 2007). Porter (1985, 1986) argued that the sources of cost advantage include the pursuit of economies of scale, proprietary technology and preferential access to raw materials. The strategic logic of cost leadership requires that a firm be the cost leader, not one of several firms vying for this position. Differentiation is based on the product itself, the delivery system by which it is sold, the marketing approach and a broad range of other factors. In order to achieve an above-average performance through differentiation in its industry, a firm's price premium should exceed the extra costs. If a firm markets products whose quality, reliability or prestige is higher than its competitors' and if its customers are willing to pay for this uniqueness, the firm has a competitive advantage based on differentiation. Successful differentiation enables a firm to gain market share or raise prices over competitors (Carpenter and Sanders, 2007). The focus strategy is quite different from the others because it rests on the choice of a narrow competitive scope within an industry. A firm can achieve a competitive advantage in its target segments by optimising its strategy for the target segments, even though it does not possess a competitive advantage overall.

Porter's original approach to competitive strategies is that firms can be successful only if they adopt either a cost or a differentiation strategy (i.e. they must choose one of the two). If they mix them, they end up with low perceived value and high price (stuck in the middle). This is another possible competitive strategy but one which, according to Porter, will ultimately fail. Porter made the assumption that a better product costs more to produce, but that consumers will pay more in some market segments for what they perceive as better. This is the basis of the differentiation strategy. In other markets or segments, consumers may be interested only in buying something at the lowest price, subject to some minimum quality. This is the basis of cost strategy.

However, previous researchers have established that Porter's generic strategies are not mutually exclusive – a firm can pursue several simultaneously. It may be true, as Porter argued, that cost leadership and differentiation are generally incompatible, but they are not opposite ends of the same continuum. Hambrick (1983, p. 690) pointed out that a defender, for example, who maintains a stable offering may choose to exploit its stability in the form of low costs (cost leadership), product quality (another form of differentiation), or some combination of competitive weapons. The two typologies are not incompatible. Dess and Davis (1984, p.484) also supported this argument. An important finding of their study was the apparent lack of singularity in strategic orientations which characterises the highest performance group. The group was identified as primarily oriented toward an overall low cost strategy. However, this group also emerged with the highest centroid score on the focus strategy. Given Porter's (1980) caution against being committed to multiple generic strategies, the high performance exhibited by the members of this group may appear inconsistent. Miller's (1988) study also claimed that a firm can adopt more than one generic strategy at once.

He made a study of 89 Canadian firms in order to investigate the relationships of Porter's business strategies to the structures and environment. Miller (1988, pp.284~285) proposed the following hypotheses:

> "*Hypothesis 2: Marketing differentiation will be positively associated with environmental uncertainty.*
>
> *Hypothesis 3: The strategy of cost leadership will be inversely associated with environmental uncertainty"*

Investigators have concluded that the strategies are in fact dimensions on which firms can score high or low (Miller, 1988). Based on those previous researches, this present research also adopts this position.

Now, we examine each element of Porter's three generic strategies from the GTCs'/*Sogo Shoshas'* point of view. The GTCs/*Sogo Shoshas* may use their diverse functions to achieve cost advantage. First, making economies of scale is one of the routes to cost reduction. For example, the SMEs' independent small scale of transactions may incur high cost and is confronted with a limit in the penetration of international markets due to their lack of information, knowledge and personnel. This being so, the GTCs/*Sogo Shoshas* may be efficient at reducing cost for SMEs through their economies of scale. They may overcome such obstacles by organising SME's lack of information, knowledge and personnel together and ultimately succeed in reducing costs. Second, large companies such as the GTCs/*Sogo Shoshas* can achieve cost reduction through marketing. Lynch (2000) argued that large companies are able to aggregate separate advertising budgets into one massive fund and negotiate extra media discounts which are simply not available to smaller companies. Third, the GTCs/*Sogo*

Shoshas also can be a cost leader by rationalising insurance, transportation, storage and warehousing facilities. For example, most Korean GTCS and Japanese *Sogo Shoshas* have their own insurance or transportation companies and are equipped with many storage and warehousing facilities near major seaports in order to meet customers' needs quickly.

The GTCs/*Sogo Shoshas* are also able to create competitive advantage through their differentiation strategy. A typical example of their differentiation strategy is their integrated services: information gathering, organising, coordinating, marketing, financing, transaction and troubleshooting are simply not provided by ordinary trading companies. With regard to the focus strategy, some GTCs/*Sogo Shoshas* may prefer to provide specific services and products to specified regions rather than global markets. They, thus, become niche traders. However, in general, this strategy may not create competitive advantage, because most GTCs/*Sogo Shoshas* are highly diversified in terms of markets, products and services. This is best expressed in their motto of "from noodles to satellites."

- ***Global Management Strategy Theory***

Global management strategy theory presents the concept of a firm's strategic management in a changing environment. In order to obtain and sustain competitive advantage, which is required for global management, a firm needs to cope strategically with the rapidly changing business environment since the source of competitive advantage is continuously changing. Kogut (1984, 1985) established a global management strategic theory by combining comparative advantage (a country-specific advantage) with competitive advantage (a firm-specific advantage). Comparative advantage is normally determined by the difference of factor costs (e.g. wages, materials and capital charges) between two nations, whereas competitive advantage is determined by the difference of technology, brand and information within a firm. Therefore, in order to create competitive advantage it is necessary for a firm to design a global strategy based on the interplay between the comparative advantages of countries and the competitive advantages of firms, because competitive and comparative advantage are not completely independent of each other.

Bartlett and Ghoshal (1998) looked at a multinational firm which used an integrated networks perspective as a means of building competitiveness. By using integrated networks, networks with each specialised unit linked to the others worldwide, a firm can achieve multidimensional strategic objectives of efficiency, responsiveness, innovation and competitive advantage. Bartlett and Ghoshal argued that the strength of this integrated network comes from the following three elements: geographical dispersion of assets, specialised operations and interdependent relationships. A dispersed configuration of assets and resources allows a firm to capitalise on factor cost differentials and still have a chance to access low-cost labour and materials. Dispersed operations are also vital in an international environment where the concentration of assets would expose companies to intolerable political and economic risk. Moreover, today's worldwide competitive environment demands collaborative information sharing and problem solving, cooperative resource sharing and collective implementation.

From the GTCs'/*Sogo Shoshas'* perspective, they create and sustain their own competitive advantage through information management for, as Kogut emphasised, information is vitally important in creating a firm's competitive advantage. Mitsui

Corporation, for instance, focused on "Information Management", which enables the new business opportunities to be created by gathering information about the physical, human and financial flow of each country through its global networks. Regarding the dispersion of assets, as Bartlett and Ghoshal argued, Nissho Iwai Corporation, for its part, selected "Dispersion of Management Resources" as one of its business portfolio strategies for 2003~2006[58].

- ***Resource-based Theory***

A firm's major concern in strategic management is to acquire and maintain sustainable competitive advantage. However, the continued increase of environmental uncertainty over time makes it difficult for a firm to sustain competitive advantage. Consequently, since the 1980s people have started to pay attention to the internal resources of a firm in order to find the source of competitive advantage and this has stimulated the emergence of resource-based theory.

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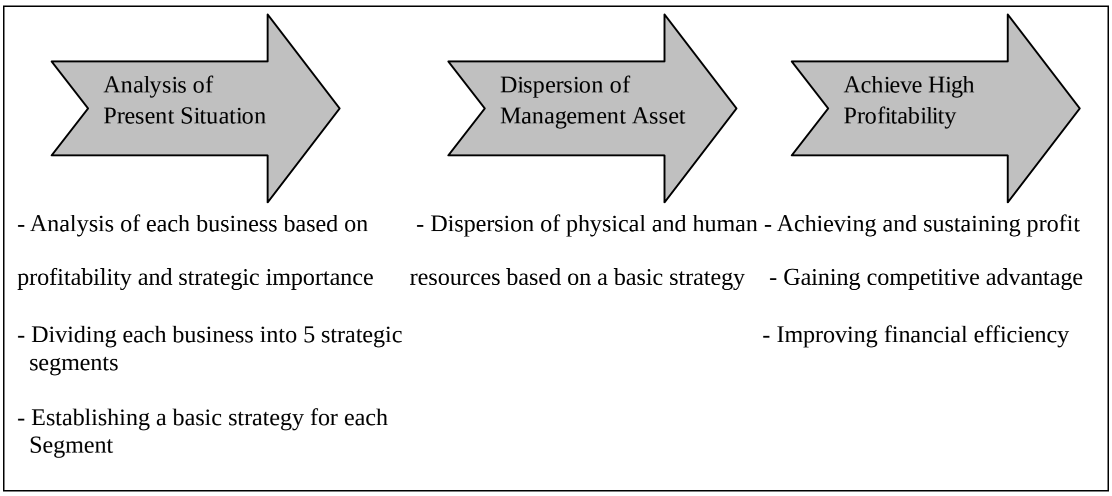
[58] Nissho Iwai Corporation's Business Portfolio Strategies for 2003~2006



(Source: The Handbook of Japanese *Sogo Shoshas*, 2005, pp. 38)

The internal perspective on competitive advantage is often called the resource-based view of the firm. It holds that firms are heterogeneous bundles of resources and capabilities (Carpenter and Sanders, 2007). Resourced-based theory emphasises a firm's physical resources and importantly deals with a firm's human or intangible resources, which were comparatively neglected by previous studies. The idea of looking at firms as a broader set of resources goes back to Penrose (1980). Since her study, the framework of resource-based theory to explain a firm's source of competitive advantage has continued to develop and it has become a new area of research in strategic management.

Among the factors in a firm's growth, resources were used by Penrose (1980) to present a resource-based approach looking at a firm's administrative organisation and collection of physical, human and intangible assets. Penrose stressed that most resources can provide a variety of different services, a fact which is very important for the productive opportunities of a firm; it is the heterogeneity, not the homogeneity, of the productive services available or potentially available from its resources which gives each firm its unique character. Penrose saw a firm as "flesh and blood", consisting of human and non-human resources under administrative authoritative coordination and communication. Human and in particular managerial, resources are the most important of these. Resources provide multiple potential services.

Mahoney and Pandian (1992) also looked at the concept, arguing that a firm's distinctive competence can create competitive advantage. For instance, top management in a diversified enterprise can be a significant and distinctive resource if it uniquely contributes to the sustained profitability of the enterprise. Barney (1991) defined a firm's resources to include all assets, capabilities, organisational processes, information, and knowledge controlled by a firm which enable it to conceive of and implement strategies to improve its efficiency and effectiveness. Barney designated value, rareness, imitability and substitutability as major resources for creating a firm's sustained competitive advantage. In other words, a firm's resources must have four attributes: i) they must be valuable, in the sense that they exploit opportunities and neutralise threats in a firm's environment, ii) they must be rare among a firm's current and potential competitors, iii) they must be imperfectly imitable and iv) there must be no strategically equivalent substitutes which are valuable but neither rare nor imitable.

Johnson, Scholes and Whittington (2005) stressed that unique resources and core competences can generate competitive advantage for a firm. Unique resources are those which critically underpin competitive advantage, whereas core competences are activities or processes which critically underpin a firm's competitive advantage. Unique resources sustain the ability to provide value in the product better than any competitor's resources and are difficult to imitate. At the same time, core competences create and sustain the ability to meet the critical success factors of particular customer groups better than other providers in ways which are difficult to imitate.

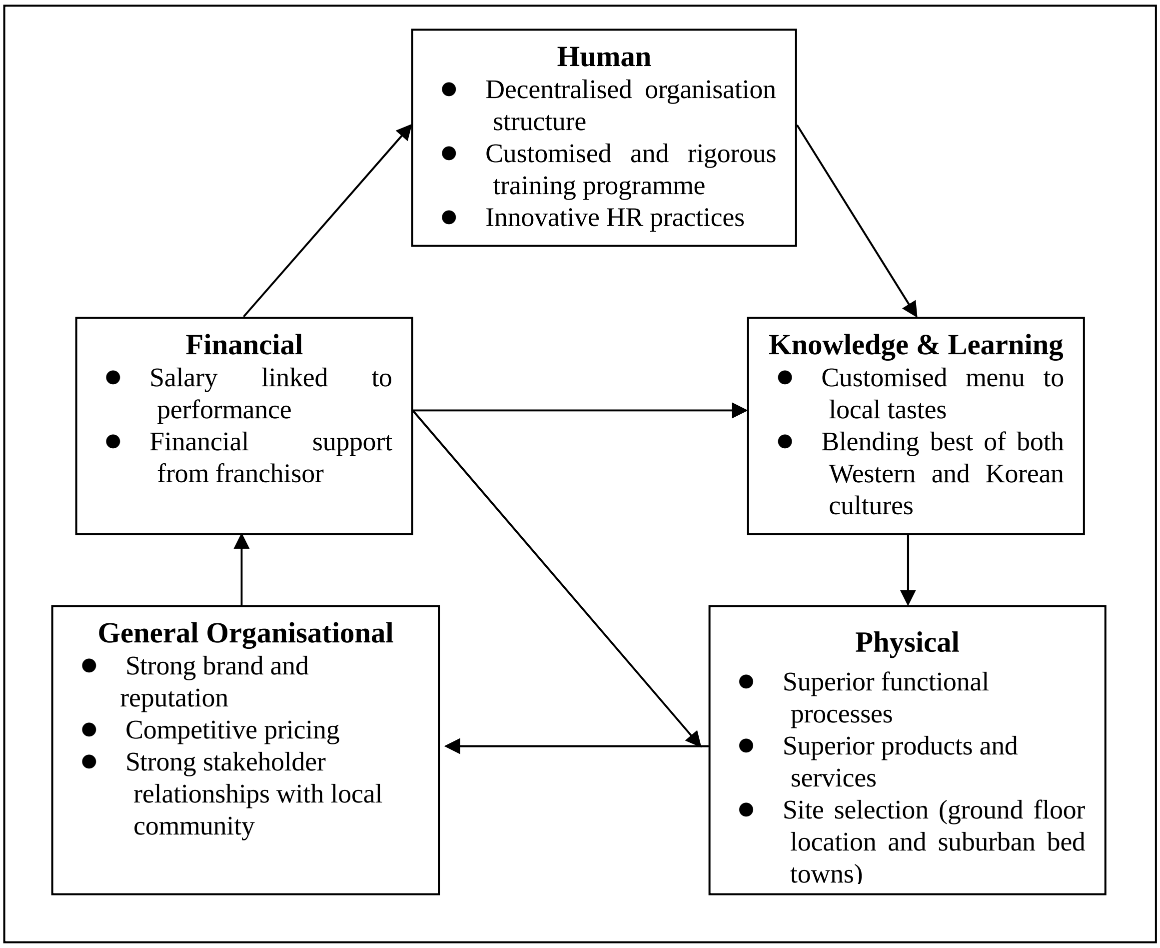
According to Slater (2003), tangible resources may include financial and physical resources, whereas intangible resources may include reputation, technology and culture. Skills and knowledge, adaptability, communication and interactive abilities and motivation are human resources. However, it is better if these resources are unique since unique resources are difficult for competitors to imitate and offer potential competitive advantage. Corporate culture, for example, can be one of the unique resources.

Corporate culture, which is defined as the collection of beliefs, expectations and values learned and shared by a corporation's members and transmitted from one generation of employees to the next (Wheelen and Hunger, 2007), fulfils several important functions in an organisation. According to Slater (2003), corporate culture gives a positive effect or a negative effect according to the situation. Corporate culture may, if appropriate, convey a sense of identity and belonging, generate employee commitment, add to organisational stability and serve as a frame of reference for decision-making. If inappropriate, however, it may give rise to alienation, demotivate employees, destabilise an organisation, frustrate communication and delegation and generate resistance to change. For instance, a Japanese corporation's peculiar culture of a guaranteed lifetime job can be a unique resource for enhancing their competitive advantage.

Enz's (2008) case study of Outback Steakhouse in Korea suggests that firms, in order to sustain competitive advantage, must manage and blend resources in the following five categories; financial resources, physical resources, human resources, organisational knowledge and learning and general organisational resources, including brand names and relationships with stakeholders. A firm's differentiation rests most heavily on such intangibles as human resources and operational processes. If human resource development is neglected, learning and innovation will cease and the organisation will eventually lose its market position.

The following figure shows the bundle of resources at Outback Steakhouse in Korea.

(Figure 5.4. A Combination of Five Resources)



(Source: Enz, C.A. (2008), "Creating a Competitive Advantage by Building Resource Capability: The Case of Outback Steakhouse in Korea", Cornell Hospitality Quarterly, Vol. 49, Iss.1, p. 75)

As regards the GTCs'/*Sogo Shoshas'*, they have hitherto been prone to depend upon external environmental features, rather than depending upon their internal resources to enhance competitive advantage. However, the modern business environment, with its free competition, increased uncertainty, similarity of strategies or policies among the GTCs/*Sogo Shoshas* and market globalisation of market, makes it difficult for them to sustain competitive advantage. Therefore, they need to emphasise cultivating a long-term insight into internal core competences and resources. For instance, Mitsui Corporation selected the "Establishment of a New System of Fostering Competent Employees" as its medium-term business plan.[59]

- ***FDI Theory***

The root of competitive advantage can also be found in FDI theory, because FDI theory examines which competitive advantages are required in order for an investing firm to be successful while competing against locally existing firms, foreign investors and potential competitors in the host country. The concept of competitive advantage in FDI theories was mainly analysed by Hymer (1960), Kindleberger (1969), Dunning (1980) and Wells (1983).

The theoretical base of competitive advantage in FDI theory started from Hymer and Kindleberger, who used the phrase 'monopolistic advantage'. Hymer (1960) stressed that a firm's possession of specific advantage can cause international operations and the origins of monopolistic advantage are the ability to produce at lower cost, knowledge or control of a more efficient production function, distribution ability and product differentiation. To explain monopolistic advantage, which produces FDI, Kindleberger (1969) presented the ability to differentiate products, special marketing skills, retail price maintenance, superiority of management and economies of scale. Dunning's (1980) eclectic theory, however, identified that a firm will engage in FDI if the following three conditions are satisfied: i) A firm must have some firm-specific assets which its competitors do not possess, ii) there should be a reason for the firm to

[59] The specific action plans include: i) promotion of competent employees for global management, ii) confirming a performance-based reward system, iii) cultivating new global leaders with an age range from the late thirties to the early forties, iv) promotion of tailor-made leaders, v) joint ownership and sharing of knowledge with important customers and vi) establishing face to face relationships with important partners (Source: The Handbook of Japanese *Sogo Shoshas*, pp. 24)

use such assets abroad rather than in the home country and iii) the firm must also be induced to internalise such assets. These three are known respectively as ownership-specific advantage (O), location-specific advantage (L) and internalisation (I). Scholars also called ownership-specific advantage monopolistic or competitive advantage. According to Wells (1983), a firm must have some advantages over other firms before it can operate successfully abroad. Such competitive advantages include: technology, marketing skills, ability to collect information and the ability to avoid risk.

5.2.4. Literature relating to Organisational Structure [60]

The purpose of building organisational structure is to generate and develop strategies. Whether strategy comes before or after structure, every organisation needs to formulate an optimal structure in order to achieve its strategic goals. Chandler (1962) defined the structure as the design of organisation through which the enterprise is administered. This design, whether formally or informally defined, has two aspects. It includes, first, the lines of authority and communication between the different administrative offices and officers; and, second, the information and data which flow along these lines of communication and authority. Lynch (2000) argued that the organisational structure should be consistent with organisational mission and objectives. Before considering the possible structures in detail, some basic questions need to be asked: what kind of organisation are we? what is our purpose? which people will carry

[60] Most of this section draws on the following books: “Designing Organisations” (4th Edition, Richard D. Irwin) by Robey, D. and Sales, C.A. (1994), “Exploring Corporate Strategy” (7th Edition, Prentice Hall)” by Johnson, G., Scholes, K. and Whittington, R. (2005), and “Corporate Strategy” (2nd Edition, Pearson Education)” by Lynch, R. (2000).

out certain activities? and which form of control, reporting or supervision is most appropriate?

Robey and Sales (1994) classified organisational structure into two kinds: mechanistic structure and organic structure. Under the mechanistic or bureaucratic structure, every task is well defined by rules, responsibilities are clear, a clear hierarchy of authority exists to control and coordinate the work, rewards are tied directly to job performance and employees are selected on the basis of their ability. However, organic structure adapts more readily to a changing environment. For example, with organic structure jobs are broadly defined, tasks are not governed by standard rules or procedures, responsibilities are somewhat ambiguous, the hierarchy is often bypassed or ignored even if it exists, the formal reward system is little emphasised and employees are selected on the basis of both objective and intangible criteria.

With respect to the basic principles and components in the process of an organisational design, the classical organisation structure designers presented eight principles of organisational structure: division of labour, standardisation of tasks, hierarchy of authority, equal authority and responsibility, unity of command, limited span of control, separation of line and staff and decentralisation. Mintzberg (1979) emphasised the importance of the formalisation of behaviour as a basic element in the organisational design. More recently, Lynch (2000) presented the main elements of organisation design as age, size, environment, centralisation/decentralisation decisions, culture and leadership. The section below focuses on two basic elements: centralisation/decentralisation and formalisation, which are most relevant to the objectives of the present research.

- ***Centralisation and Decentralisation***

As an organisation becomes more diverse in its products or markets, there is a great likelihood that it will need to consider its structure. Specifically, more complex forms of organisational structure may be necessary because the centre becomes increasingly isolated from the place where decisions are needed and can best be made. Separate divisions within the organisation may need to be set up and some power delegated to them. When an organisation changes from being a one-product company to including these more complex elements, it may need to move from centralisation to decentralisation (Lynch, 1997)

When all the power for decision-making rests at a single point in the organisation, we shall call the structure centralised; to the extent that power is dispersed among many individuals, we shall call the structure decentralised. There are some advantages in centralised organisation: it is possible to produce a consistent strategy across the organisation, it allows faster decision-making with less compromise and it facilitates the co-ordination of sub-units. However, a move to decentralisation is necessary when the organisation becomes more diverse. Mintzberg (1979) suggested three reasons why an organisation should decentralise. First, there are too many decisions to be understood at one centre, by one brain. Sometimes the necessary information simply cannot be brought to that centre. Perhaps too much of it is soft or difficult to transmit. Second, decentralisation allows the organisation to respond quickly to local conditions. Third, it stimulates motivation. Creative and intelligent people require considerable room to manoeuvre. The organisation can attract and retain such people and utilise their initiative, only if it gives them considerable power to make decisions.

Wickman (2008) adopts a position of neutrality by suggesting the need for centralisation and decentralisation to coexist. Giving the example of Scotiabank, he argues that firms, to be effective in today's global business environment, are embracing elements of centralisation and decentralisation which allow them to act quickly at the local level while leveraging best practices at the corporate level. A vice-president of the global performance office at Scotiabank says (Wickman, 2008, p. 46);

> *"We are a global company and a highly matrixed organisation. The hybrid model allows us to be nimble enough to respond to the needs of the business quickly and efficiently. At the same time, because we have a centralised unit, we can make sure of economies of scale. We can identify and use synergies wherever possible and it allows us to provide an infrastructure to make the whole thing run."*

The following table shows the balancing considerations between centralisation and decentralisation.

(Table 5.1. The Balancing Considerations between Centralisation and Decentralisation)

Advantages of Centralisation	Elements favouring Decentralisation
It is possible to produce a consistent strategy across the organisation.	Enables a strong response to be made to local circumstances.
The greater likelihood of economies of scale.	When decisions are very complex or localised, centralised decision-making may not be sensible.
It facilitates the co-ordination of sub-units.	It is difficult to provide high-quality customer services from the centre.
Simpler control system than with a decentralisation structure.	Provide opportunities to develop general management talent.
Faster decision-making, with less compromise.	Motivates staff in locations outside the centre.
Limited geographic distance between headquarter and subsidiary.	A more diversified product range.
High degree of inter-relationship between sub-units.	A stable environment.
High technology content.	It is appropriate when a unit is unimportant to the centre.

For GTCs and *Sogo Shoshas*, the centralisation/decentralisation issue is one of the most important to resolve for effective management. A basic dilemma for a multinational corporation[61] is how to organise authority centrally so that it operates as a vast interlocking system which operates a strategy and at the same time decentralise authority so that local managers can make the decisions necessary to meet the demands of the local market (Wheelen and Hunger, 2007). To deal with this problem, GTCs and *Sogo Shoshas* tend to structure themselves along geographic areas, i.e. Asia, West Europe, East Europe, North America, South America, Oceania, Middle East and Africa.

- ***Formalisation***

Formalisation is defined as the degree to which formal rules and procedures govern decisions and working relationships. Rules and procedures provide a means for prescribing appropriate behaviours and addressing routine aspects of a problem. According to Mintzberg (1979), formalisation of behaviour is the design parameter by which the work processes of the organisation are standardised. He classified the behaviour of formalisation in three ways: formalisation by job, formalisation by work flow and formalisation by rules. In case of formalisation by job, the organisation attaches the behavioural specifications to the job itself, typically documenting it in the formal job description. The incumbent may be told what steps to take in his work, in what sequence, when and where. In case of formalisation by work flow, instead of linking the specifications to the job, the organisation can attach them to the work itself. Finally, rather than formalising by job or work flow, the organisation may instead

[61] It is hard to see GTCs and *Sogo Shoshas* as multinational corporations because most of them do not have manufacturing facilities in the local markets where they have offices. However, they have almost same functions as multinational corporations in terms of organisational structure, operating offices in a local market and hiring local people, etc. Nowadays, some GTCs and *Sogo Shoshas* tend to invest in manufacturing business in local markets.

institute rules for all situations – all jobs, all work flows and all workers. These may specify who can or cannot do what, when, where, to whom and with whose permission. As Bjork (1975) suggested, organisations formalise behaviour to reduce its variability and ultimately to predict and control it. One prime motive for doing so is to coordinate activities. The fully formalised organisation is the precise organisation, in which there can be no confusion. Formalisation is also used to ensure the machinelike consistency which leads to efficient production. Tasks are specialised in the horizontal dimension to achieve repetition; formalisation is then used to impose the most efficient procedures on them.

At the same time, according to Kim's study (2007) of a set of best organisational structures for efficient Supply Chain Management (SCM), although excessive formalisation and centralisation of the SCM department within a firm may interrupt the complete integration of the supply chain and performance improvement, a certain range of control by the SCM department is inevitable in building the fundamentals of integrated SCM. Therefore, the temporary pursuit of intensive formal control focused on organisation type, such as integrated line organisation, may be considered, depending on firm characteristics and environmental changes.

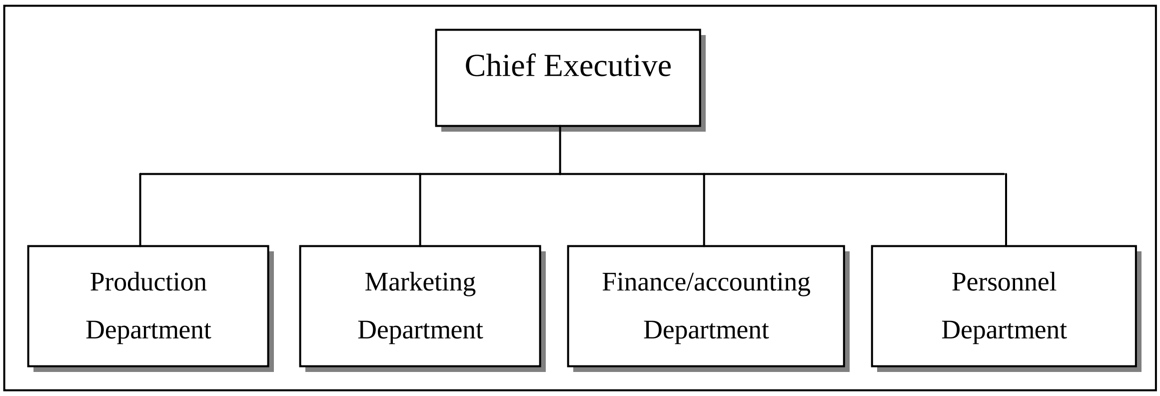
- ***Types of Organisation***

There are many types of organisational structure: simple structures, functional structures, multidivisional structures, holding company structures, matrix structures and so on. Each type of structure has different characteristics. Thus, it is important to be familiar with the strength and weakness of each type when formulating the structure.

First, a simple structure can be thought of as something without formal structure, because the organisation is run by the personal control of an individual.

Second, a functional structure is based on the primary activities to be undertaken by an organisation, such as production, finance and accounting, marketing, human resources and information management. There are some advantages in the functional structure including the fact that it allows central strategic control at a senior level and provides clear responsibilities to organisation members. However, senior managers will be overburdened with routine matters as the organisation becomes larger or more diverse, it will be difficult to cope with diversity and strategic change may be slow.

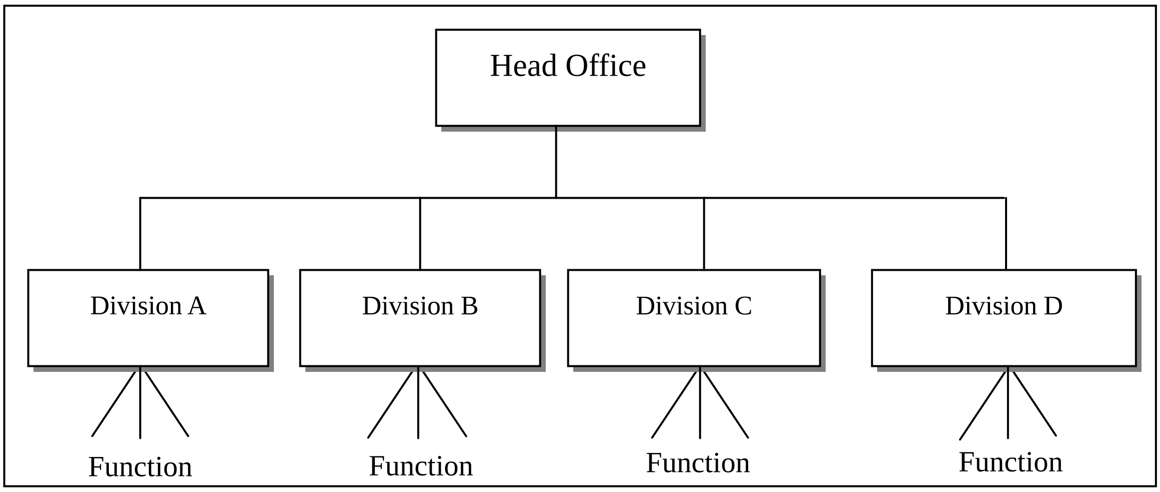
(Figure 5.5. A Functional Structure)



(Source: Johnson, Scholes and Whittington (2005), "Exploring Corporate Strategy", 7th Edition, Prentice Hall, p. 399)

Third, a multidivisional structure is built up from separate divisions on the basis of products, services or geographical areas. As organisations grow, they may need to subdivide their activities in order to deal with the great diversity which can arise in products, geography or other aspects of the business. The major advantages of this structure are: it allows a focus on a particular business area and facilitates the measurement of unit performance. But there will be conflict between divisions when they compete with each other, the complexity of cooperation will increase if there are too many divisions and it is an expensive structure to maintain.

(Figure 5.6. A Multidivisional Structure)

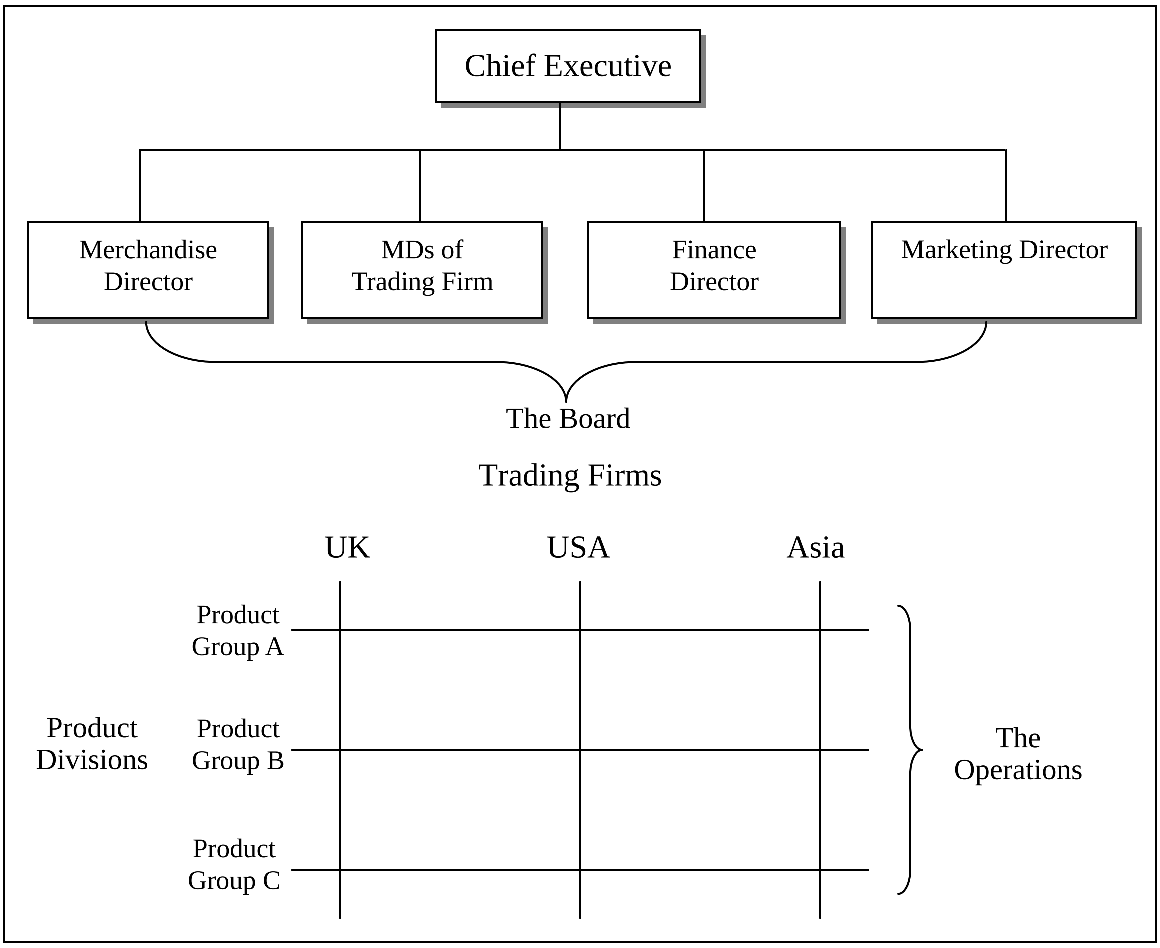


(Source: Ibid, p. 401)

Fourth, a holding company structure is an investment company consisting of shareholders in a variety of separate business operations. This structure may enhance new market entry, spread risk for conglomerates and allow for the complexity of modern ownership. Disadvantages are: there is little control at the centre and problems will arise if two partners cannot cooperate or one partner loses interest.

Fifth, a matrix structure is a combination of structures, which could take the form of product and geographical divisions or functional and divisional structures operating in tandem.

(Figure 5.7. A Matrix Structure: Multinational Organisation)

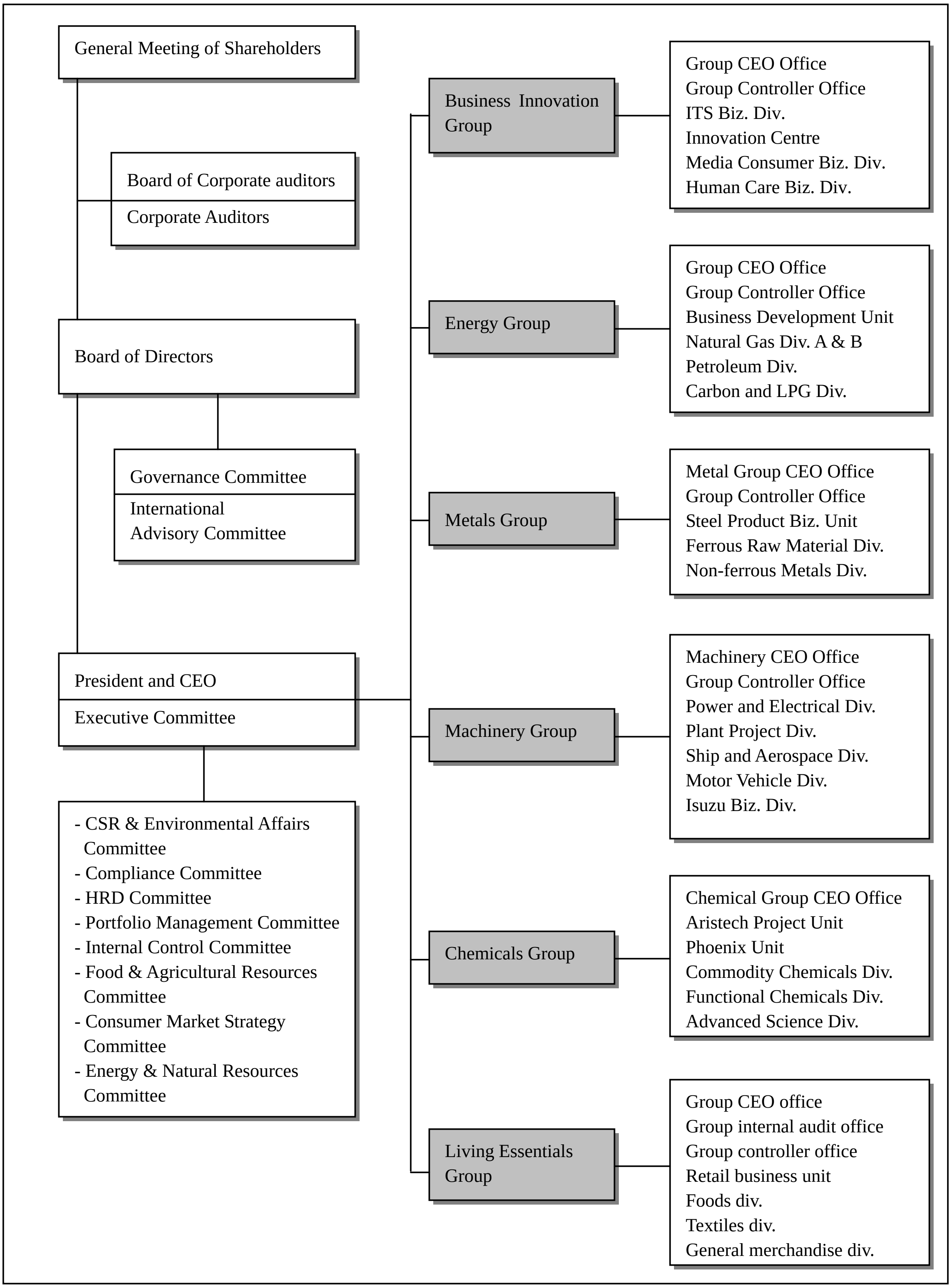


(Source: Ibid, p. 403)

This structure helps quality decision-making where interests conflict and increases managerial motivation through manager's close involvement with organisational issues. However, there is a high degree of conflict and it takes time to make decisions because all participants have to reach agreement.

From the GTCs'/*Sogo Shoshas'* point of view, both Korean GTCs and Japanese *Sogo Shoshas* are highly multidivisional structures. For example, Mitsubishi Corporation consists of six different business groups: the new business initiative group, the energy business group, the metals business group, the machinery business group, the chemicals business group and the living essentials business group. Each group focuses on its core areas. For instance, the energy business group concentrates on natural gas, petroleum and carbon development, while the living essentials business group concerns itself mainly with foods and textiles businesses. This structure allows each group to achieve maximum profits and effectiveness by concentrating on its main business area and it also facilitates the measurement of group performance.

(Figure 5.8. Organisational Structure of Mitsubishi Corporation)



(Source: Mitsubishi Corporation Annual Report, 2008, p. 3)

5.2.5. Literature relating to Business Performance

A firm's performance is reaped from its effective management of physical and human resources. As a tool for measuring a firm's performance, financial performance measurements, such as Return on Investment (ROI), Earnings per Share (EPS), profitability, productivity, growth rate and sales amount, have traditionally been used as key performance indicators. However, it has been recognised that no one performance measure can adequately meet the needs of management in a competitive environment. Brown and McDonnell (1995) argued that the traditional use of profit-based performance measures by many organisations can be criticised on a variety of fundamental grounds – for instance their relative incompleteness and lack of accuracy and neutrality, their encouragement of short-terms and their lack of balance. Moreover, Newing (1995, p. 22) claimed:

> *"In particular, it places too much emphasis on pure profit measures and too little on the customer, staff, risk process and control aspects of the organisation's operations, although these are the key drivers of the financial results"*

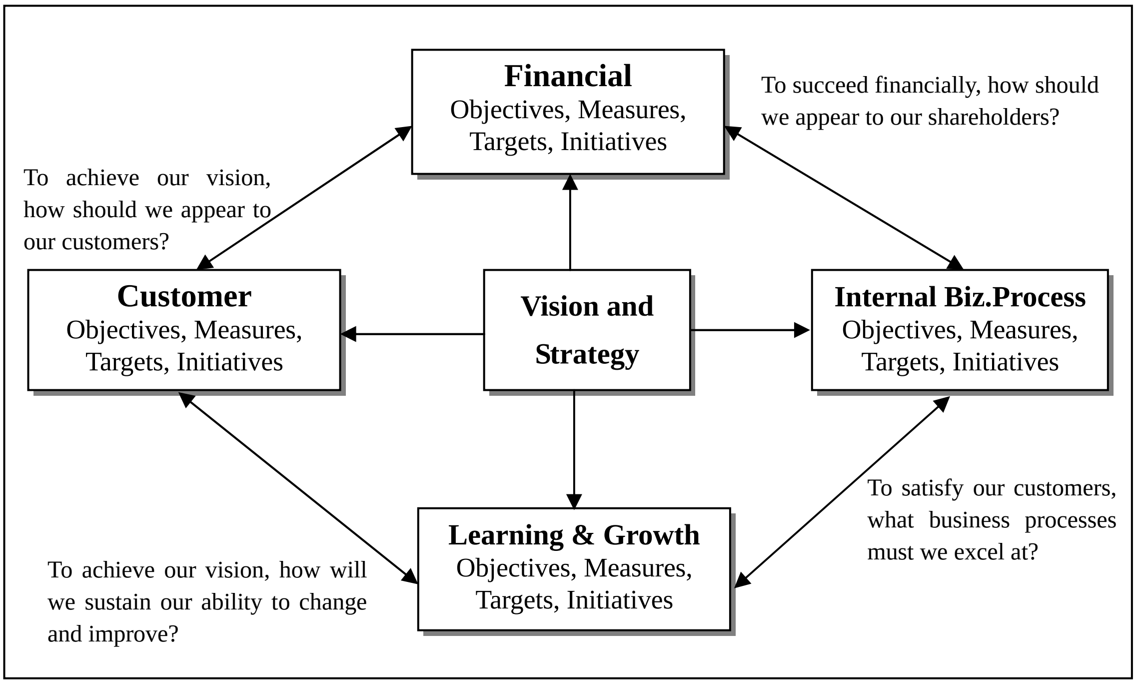
Niven (2008) also pointed out that previous measurement systems have failed to keep pace with the rate of change occurring in the workplace. The performance measurement system focuses almost exclusively on financial measures and more specifically, it relies on counting countable things.

Major limitations of traditional financial performance measurement systems can be summarised as follows. First, they have limitations in forecasting a firm's future performance and its potential to create value, since they are based merely on actions taken in the past, i.e. lagging indicators. They excessively emphasise short-term financial indicators, but tend to ignore long-term potential performance. For example, if firms neglect the driving forces which create future value for them, such as core competencies, R & D and learning, they will ultimately fail to sustain their competitiveness. Second, as Amaratunga *et al.* (2002) argued, traditional performance measurement systems appear not to be providing managers with the information that they need to measure and manage the all-important competencies which drive competitive advantage. Third, they ignore customers and competition. Traditional financial performance measures do not give any information on how customers see a firm, or how a firm creates competitive advantage over its competitors. Fourth, as Kaplan and Norton (1992) argued, traditional financial accounting measures can give misleading signals for continuous improvement and innovation activities in today's competitive and demanding environment.

Due to the reasons mentioned above, many organisations have realised that the traditional financial orientation of their performance measurement systems are no longer adequate and they want a balanced presentation of both financial and operational measures. In 1992, Kaplan and Norton devised a "Balanced Scorecard (BSC)" – a leading indicator of a firm's performance and a new measurement system of both financial and non-financial elements. It includes financial measures which tell the results of actions already taken. And it complements the financial measures with operational measures of customer satisfaction, internal processes and the organisation's innovation and improvement activities – operational measures which are the drivers of future financial performance. The BSC allows managers to look at the business from four important interlinked perspectives – financial, customer, learning and growth perspective and internal-business process. The main aim of the BSC is to address the problem of organisations relying too heavily on traditional financial outcome measures, which tend to focus on past performance rather than on performance metrics to help predict an organisation's future success (Meyer, 2005). By focusing not only on financial outcomes but also on their operational, marketing and developmental inputs, the BSC helps provide a more comprehensive view of a business, which in turn helps organisations to act in their best long-term interests.

The BSC provides answers to four basic questions its four perspectives of the BSC are illustrated in the figure below.

(Figure 5.9. The Four Perspectives of the BSC)



(Source: Kaplan, R. S. and Norton, D. P. (1996), "Using the Balanced Scorecard as a Strategic Management System", Harvard Business Review, Vol. 74, Iss. 1, Jan./Feb. p. 76)

- ***Financial Perspective***

Financial performance measures indicate whether the organisation's strategy, implementation and execution are contributing to bottom-line improvement. Typical financial goals have to do with profitability, growth and shareholder value (Kaplan and Norton, 1992; Carpenter and Sanders, 2007). Smith (2007) suggests that the strategic objectives of financial perspective are maintaining financial integrity, generating revenue, managing budget and managing investments.

- ***Customer Perspective***

Customer perspective captures the ability of the organisation to provide quality goods and services, the effectiveness of their delivery and overall customer service and satisfaction (Amaratunga *et al.,* 2002). To this effect, many firms today have a corporate mission focused on their customers. The BSC demands that managers translate their general mission statement on customer service into specific measures which reflect the factors that matter most to customers (Kaplan and Norton, 1992). When choosing objectives for the customer perspective, firms must answer three critical questions; "Who are our customers?" "What do our customers expect from us?" and "What is our value proposition in serving them?" (Niven, 2008, p. 17). According to Smith (2007), increasing stakeholder satisfaction, promoting a positive image of the firm and enhancing customer communication would be the strategic objective from this perspective.

- ***Learning and Growth Perspective***

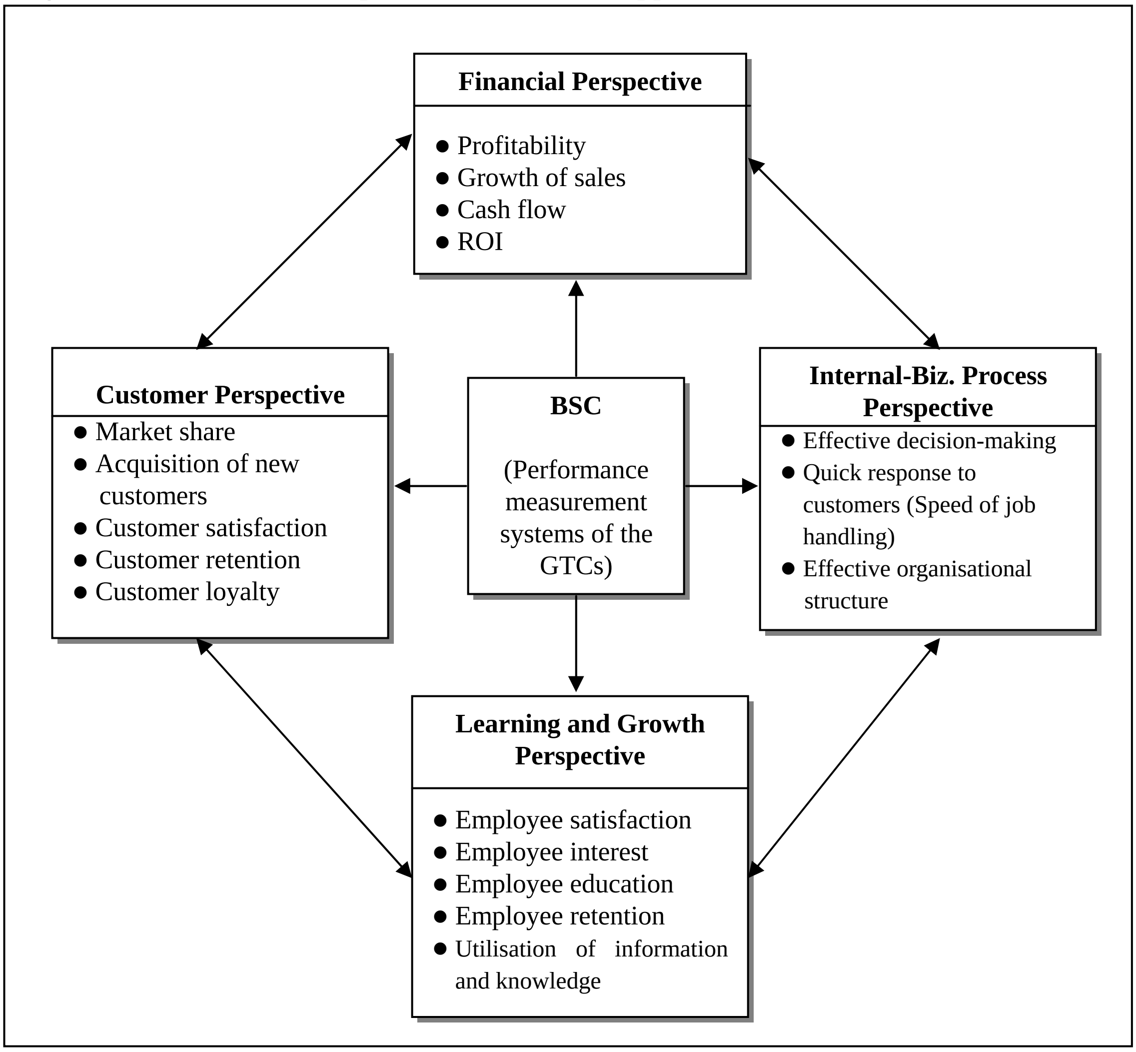
The customer-based and internal business process measures on the BSC identify the parameters which the organisation considers most important for competitive success. But the targets for success continually change. Intense global competition requires companies to make continual improvements to their existing products and processes and to learn to introduce entirely new products which can do more. In this context, the learning and growth perspective looks at such issues, which include the ability of employees, the quality of information systems and the effects of organisational alignment in supporting the achievement of organisational goals (Kaplan and Norton, 1992). Smith (2007) gives some objective examples of the learning and growth perspective; developing a positive culture, improving internal communication and managing technological resources.

- ***Internal-Business Process Perspective***

Managers need to decide which operations, processes, competences and skills their organisations must excel at if customer demands are to be met adequately (Brown and McDonnell, 1995; Niven, 2008). This perspective is primarily an analysis of the organisation’s internal processes. Internal business processes are the mechanisms through which organisational performance expectations are achieved. Customer-based measures are important, but they must be translated into measures of what the organisation must do internally to meet its customers’ expectations. After all, excellent customer performance derives from the processes, decisions and actions occurring throughout an organisation. This perspective focuses on the internal business results which lead to financial success and satisfied customers. Thus, managers need to focus on those critical internal operations that enable them to satisfy customer needs (Amaratunga *et al.*, 2002). Smith (2007) suggests that streamlining key processes and optimising contract management would be a good example for the objectives of this perspective.

From the GTCs'/*Sogo Shoshas'* point of view, the BSC may be an integrated new tool for measuring both financial and non-financial performance. The financial perspective has traditionally been used as a primary indicator to measure the GTCs'/*Sogo Shoshas'* performance. In the stage when they are growing quantitatively, their financial performance is a major performance indicator of their success, without paying special attention to other perspectives, such as customer satisfaction or retention, employee satisfaction or education and effective decision-making, etc. But as the business environment surrounding the GTCs became more intense, they realised that they needed to have a balanced presentation of both financial and non-financial measures. In addition to the financial emphasis, they needed to have a balanced strategic insight as to what was needed by their customers, their employees and the internal-business process. The following figure illustrates four perspectives of the BSC applied to the GTCs/*Sogo Shoshas*.

(Figure 5.10. The Four Perspectives of the BSC applied to the GTCs/*Sogo Shoshas*)



(Source: Developed by the author based on Kaplan and Norton)

5.2.6. Review of Selected Previous Studies

- **A Study by Chandler (1962): The Relationship between Strategy and Structure**[62]

The first study to investigate the relationship between a firm's strategy and structure was carried out by the US strategist Alfred Chandler, Jr. In the early 1960s, Chandler examined how some leading North American companies, including Ford and General Motors, had developed their strategies in the first half of the twentieth century. On the basis of this empirical study, he concluded that it was first necessary for the firm to develop its strategy. After this task was done, the firm should devise the structure to deliver the strategy. As a company grows in size and complexity, the company needed a general office to handle the main planning and co-ordinating work of the various functions of a business, including the marketing, finance, operations and human resources. The general office was concerned with the long-term health of the firm: it devised the firm's strategy. Once the strategy was formulated, the general office then implemented it by designing a suitable organisational structure and allocating capital and human resources to the various parts of the organisation.

Chandler's study was in fact the forerunner for many organisational strategists. However, it is necessary to examine whether its conclusions are still relevant in the modern business environment.

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[62] This part is re-summarised from the book "Corporate Strategy (2nd Edition, Pearson Education)" by Lynch, R. (2000). pp. 717~718

- **A Study by Mintzberg (1979): The Links between Strategy and Structure**[63]

In the process of designing organisational structure, it is necessary to consider the complicated links between strategy and structure. In this regard, Mintzberg provided a process. He argued that the six basic parts of every organisation: its operating core, strategic apex, middle line, techno-structure, support staff and ideology have to be connected together, because between them they add value to the organisation. Furthermore, he presented six co-ordinating methods for linking together the above six parts of the organisation: mutual adjustment, direct supervision, standardisation of work processes, standardisation of outputs, standardisation of skills and standardisation of norms. Using these parts and methods, Mintzberg then developed six main types of organisational strategy and structure which combine the environment, internal characteristics of the organisation and the key part of the organisation for delivering its objectives. The six main types of organisations or strategic configurations are the entrepreneurial organisation, machine organisation, professional organisation, divisionalised structure, innovative organisation and missionary organisation. Using this classification, the organisation's strategy and its likely structure can be interrelated. In this sense, strategy is linked to structure. Although most organisations do not match the six different configurations precisely, they do provide guidelines for linking strategy to structure.

[63] This part is re-summarised from the book "Corporate Strategy (2nd Edition, Pearson Education)" by Lynch, R. (2000). pp. 734~738

- **Research by Grinyer, Ardekani and Bazzaz (1980): The Relationships between the Environment, Strategy, Structure and Financial Performance**

Grinyer, Ardekani and Bazzaz (1980) undertook an empirical study to analyse to test hypotheses relating to the links between the environment, strategy, structure and financial performance. The hypotheses relate to the correlates of strategy and structure; relationships between strategy, structure and environmental hostility; and relationships between strategy, structure and their match and measures of performance. Data were collected during interviews with senior managers within 48 large UK companies. Of the companies, 25% were in service industries, 43% were in manufacturing and 32% were in both.

First, regarding the relationship between strategy, structure, size, sites and dispersion, it found that there were positive correlation between strategy and structure, site and structure and geographical dispersion and structure. However, there was no correlation between the size of company and its diversification strategy. Second, regarding the relationship among strategy, structure and financial performance, it found that there is little support for the view that ROI and growth (Financial Performance) are positively correlated with the degree of diversification (Strategy). Often, growth and diversification were found to have a negative correlation. Furthermore, regarding the structure and financial performance, there is no evidence to support any hypothesis that companies with a divisional structure tend to outperform others in general. Lastly, regarding the relationships between the environment, strategy, structure and financial performance, it was found that diversification has advantages in in particular difficult environments (Environment). However, no significant correlations between diversification and any measure of performance were found. With respect to structure and financial performance, more highly divisionalised companies (Structure) seem to outperform others in terms of growth in sales, capital employed and number of persons employed. However, there was a negative correlation in the growth of ROI.

(Table 5.2. The Hypotheses and Results Summarised)

Hypothesis	Analysis	Result
H.1: Degree of diversification and degree of divisionalisation are positively correlated	Strategy/Structure	Supported
H.2: The number of sites and the degree of divisionalisation are positively correlated	Sites/Structure	Supported
H.3: The geographical dispersion of major sites and the degree of divisionalisation are positively correlated	Dispersion/Structure	Supported
H.4: Size of companies is positively correlated with their degree of diversification	Size/Strategy	No correlation
H.5: ROI and measures of growth are positively correlated with degree of diversification	Strategy/Performance	Little supported
H.6: ROI and growth are greater for divisionally structured companies	Structure/Performance	No correlation
H.7: In unstable environments, ROI and growth are positively and variability of ROI is negatively correlated with diversification	Environment/Strategy/ Performance	Not supported
H.8: In unstable environments, ROI and growth are positively and variability of ROI is negatively correlated with divisionalisation	Environment/Structure/ Performance	Confirmed for growth in sales, capital employed and number employed. Rejected for growth in ROI where correlation is negative

- **Research by Miller (1988) relating to Porter's Business Strategies, to the Environment and Structure: Analysis and Performance Implications**

Miller's (1988) study investigated the relationship of Porter's (1980) business strategies to the structures and environments of Canadian firms. This study dealt with strategy at the top levels of un-diversified autonomous companies, there being no real difference between business and corporate strategies in such organisations. The sample consisted of 89 firms selected randomly from lists published in the magazine "Commerce and Les Affaires", which represent a fairly exhaustive inventory by industry of significant firms in Québec. Most companies were quite small and many of them were tightly controlled by a single owner, a family, a group of partners, or a holding company. A diversity of industries was represented. They included electronics, financial services, home appliances, food and beverages, industrial equipment, construction and mining. Data were collected from the CEO and by the most senior vice president or general manager through the questionnaire. With respect to variables, four of the most commonly researched elements were selected in the part devoted to the environment: uncertainty, unpredictability, dynamism and heterogeneity; three elements emerged in the strategy part: differentiation, cost leadership and focus; and four elements in the structure part: delegation, formal control, specialisation and integration.

The first analysis sought the relationship between the environment and strategy. According to the results, marketing differentiation (Strategy) positively correlated with uncertainty, predictability and dynamism (Environment). However, cost leadership (Strategy) correlated negatively with uncertainty, predictability and dynamism. The second analysis was the relationship between strategy and structure. The result showed that innovative differentiation (Strategy) correlated significantly with the use of liaison devices, technocrats and delegation (Structure). However, there was a low-order correlation between marketing differentiation and the use of liaison devices. Furthermore, the relationship of cost leadership to the use of liaison devices, technocrats and delegation was negative. The third analysis assessed the relationship between strategy, structure and performance. The hypothesis stated that strategies or structures alone – not matched to one another – will not contribute to performance. The result showed that strategy or structure alone actually could influence performance. Thus, it confirmed the hypothesis. The last analysis was the relationship between the environment and structure. The result stated that the relationship between environment and structure was not significant.

(Table 5.3. The Hypotheses and Results Summarised)

Hypothesis	Analysis	Result
H.1: Marketing differentiation will be positively associated with environmental uncertainty, predictability and dynamism	Environment/Strategy	Supported
H.2: The strategy of cost leadership will be negatively associated with environmental uncertainty, predictability and instability	Environment/Strategy	Supported
H.3: The strategy of innovative differentiation will be positively associated with the use of liaison devices, technocrats and delegation	Strategy/Structure	Highly supported
H.4: The marketing differentiation strategy will not be associated with the use of technocrats, liaison devices or delegation of authority	Strategy/Structure	Supported
H.5: The association of strategy and structure with performance will not be significant	Strategy/Structure/ Performance	Supported
H.6: The association between environment and structure will not be significant	Environment/Structure	Supported

- **Research by Kotha and Nair (1995): Strategy and Environment as Determinants of Performance in the Japanese Machine Tool Industry**

This study examined the effect of strategy and environment on performance using data from a sample of 25 Japanese machine tool industries. The result indicated that both firm strategies and the environment play significant roles in influencing performance – in profitability and growth.

First, in the relationship between environment and performance, this study predicted that environmental munificence will be positively related to firm-level performance. Results showed that munificence is positive and significantly related to both Return on Sales (ROS) and growth. It also hypothesised that technological change will be related negatively to firm-level performance. It found that the technological change has no effect on ROS, but has a positive effect on growth.

Second, in the relationship between strategy and performance, it found that cost-efficiency strategy is negative and significantly related to ROS. Moreover, the results showed that a differentiation strategy based on "advertising intensity" is negatively related to ROS. However, even though the relationship between advertising-driven differentiation strategy and growth is positive, it is not statistically significant.

This study suggested the following implications. A firm which matches its strategies with the requirements of the environment will achieve better performance, as many studies argued. Technological change does not always lead to poor performance, but ultimately may lead to superior performance in long-term.

- **Research by Kwon, Kim, Kim and Limb (1999): The Relationships between the Environment, Competitive Strategy and Organisational Structure: Performance Implications**

This research investigated the relationships between the environment, competitive advantage and organisational structure and the impact of this relationship on a firm's performance. Data were obtained through questionnaires from the 250 subsidiaries of 50 Korean diversified enterprises. The study found that a firm's employment of a differentiation strategy positively correlated with the environmental uncertainty. More specifically, it divided the differentiation strategy into two categories: innovative differentiation and marketing differentiation. Both innovative and marketing differentiation strategies were positively associated with environmental uncertainty. However, unlike the hypothesis, the cost leadership strategy also positively correlated with environmental uncertainty, although the result was not significant statistically. With respect to the relationship between the competitive strategy and organisational structure, the results showed that a differentiation strategy was statistically significant with organisational delegation. In addition, the cost leadership strategy was positively associated with organisational formalisation.

Empirical results showed that the fit between the environment, strategy and structure was still important for subsidiaries of diversified firms, even after controlling diversification effects such as resource sharing among subsidiaries. It found that firms with high fit between the environment, strategy and structure performed significantly better than firms with low fit. However, significant performance differences between high and low performance did not exist for bivariate fits (fit between environment and structure, fit between strategy and structure and fit between environment and strategy).

An important finding of this study was that, for subsidiaries of diversified firms, theories of business-level strategy are still applicable and have an important performance implication. It is also important that fit between environment, strategy and structure is not universally applicable for all types of strategy. For example, high performers with innovative differentiation strategy achieved both external fit (environment-strategy) and internal fit (strategy-structure), while high performers with cost leadership strategy pursued internal fit only.

- **Research by Kang (2002): Relationships between the Environment, Competitive Strategy and Organisational Structure and Performance**

This study was carried out in order to examine the relationship between the environment, firm strategy and organisational structure and performance in the Korean hotel industry. The super deluxe hotels located in Seoul participated in this research. This study investigated how the environment and the strategy are related to the formulation of organisational structure, decentralisation, degree of compensation and systematic decision-making and how the influence of the productivity of an industry is different according to its suitability. The results showed that, first, environmental uncertainty had more significant results in differentiation strategy than in overall cost leadership strategy. Second, regarding the relationship between strategy and structure, differentiation strategy showed significant positive influences on decentralisation, degree of compensation and systematic decision-making, while overall cost leadership strategy showed significant positive influences on formalisation. Third, in the relationship between the environment and performance, the results showed that environmental uncertainty does not have direct influence on a hotel firm’s performance.

- **Research by Chathoth and Olsen (2007): The Effect of Environmental Risks, Corporate Strategy and Capital Structure on Firm Performance**

This research, using a sample from the US restaurant industry, tested the simultaneous impact on firm performance of surrogates from constructs identified as part of the co-alignment model, i.e. environment, strategy and structure.

Environmental risk was conceptualised as the impact of the firm's external environment on the firm, from a cash flow and profitability perspective. Corporate strategies were captured by two variables, i.e. growth-related and liquidity-related ones. The capital structure was defined using the resource-based view of strategy relative to the way in which a firm finances its investment using debt and equity instruments. Firm performance is conceptualised from the accounting and finance standpoints.

The relationships between the constructs were tested using the measures of the firm performance construct as the dependent variable and the variables of the environmental risk, corporate strategies and capital structure constructs as independent variables. The main objective of this study was to test if the firm performance-related model which includes the key alignment constructs of environmental risk, corporate strategies and capital structure holds good. The study confirmed that the variables which represent the constructs of the co-alignment model simultaneously help explain a significant variance in firm performance.

According to regression analysis, the full model (environmental risk, corporate strategy, capital structure and firm performance) explained 59% of the variance of the firm's ROE. This clearly was the best model, as compared to other incremental models which explained 35% (environmental risk, corporate strategy and firm performance) and 51% (environmental risk, capital structure and firm performance) of the variance in firm performance.

- **A Study by Gyampah and Acquaah (2008): Manufacturing Strategy, Competitive Strategy and Firm Performance**

This study examined the relationship between manufacturing strategy and competitive strategy and their influence on firm performance. It tested how competitive strategy influences manufacturing strategy and also examined the impact which manufacturing strategy and competitive strategy have on firm performance among Ghanaian manufacturing firms.

First, it examined the relationship between competitive strategy and manufacturing strategy with a hypothesis – that competitive strategy influences manufacturing strategy. The study found significant positive relationships between competitive strategy and manufacturing strategy. It confirmed that all four manufacturing strategies (cost, delivery, flexibility and quality) are means through which a firm can implement its competitive strategies. It also investigated the relationship between manufacturing strategy and firm performance with a prediction – that manufacturing strategy has a positive influence on firm performance. This was also supported. Of the four manufacturing strategy components, only quality was positively linked to market share and sales growth in both the differentiation and cost leadership models.

Second, in the relationship between competitive strategy and performance, it predicted that competitive strategy has a direct positive influence on firm performance.

The study did not find any direct statistical relationship between competitive strategy and firm performance. However, competitive strategy influences firm performance through quality. Quality improves firm performance significantly, regardless of which competitive strategy a firm chooses to emphasise. This is perhaps true because of the impact which quality has on the other manufacturing strategy components.

The implication of this study was that, whether a firm chooses to pursue a cost leadership or a differentiation strategy, an emphasis on quality provides the most benefits with regard to firm performance. An emphasis on quality appeared, for instance, to provide a means by which companies could mitigate the effects of increased competition resulting from the economic reforms within the Ghanaian manufacturing environment.

5.3. Research Objectives, Questions and Model

The previous section surveyed the literature relating to the business environment, competitive strategy, organisational structure and a firm's performance. By reviewing the existing literature, we can see that a firm's performance is not achieved by a single factor, but accomplished through a combination of all the elements or the strategic fit between all of them. In other words, the business environment directly affects a firm's competitive strategy and the strategy influences the design of organisational structure, but at the same time structure can constrain and guide the choice of strategy. Performance, then is directly affected by the strategy and structure. Based on this theoretical foundation, this study attempts to examine the structural relationship between the business environment, competitive strategy, organisational structure and the performance of Korean GTCs and Japanese *Sogo Shoshas*.

5.3.1. Research Objectives and Questions

The objective of this chapter is to examine the strategic management of Korean GTCs and Japanese *Sogo Shoshas.* As a means of accomplishing the objective, it attempts to analyse the structural relationship between the business environment and a firm's strategy, organisational structure and performance. In order to achieve the objective, the following sets of research questions have been devised and methods are presented of finding answers to those questions;

RQ 1. How much do environmental variables affect competitive strategies? ⇒ Analysis of the relationship between business environments and competitive strategies,

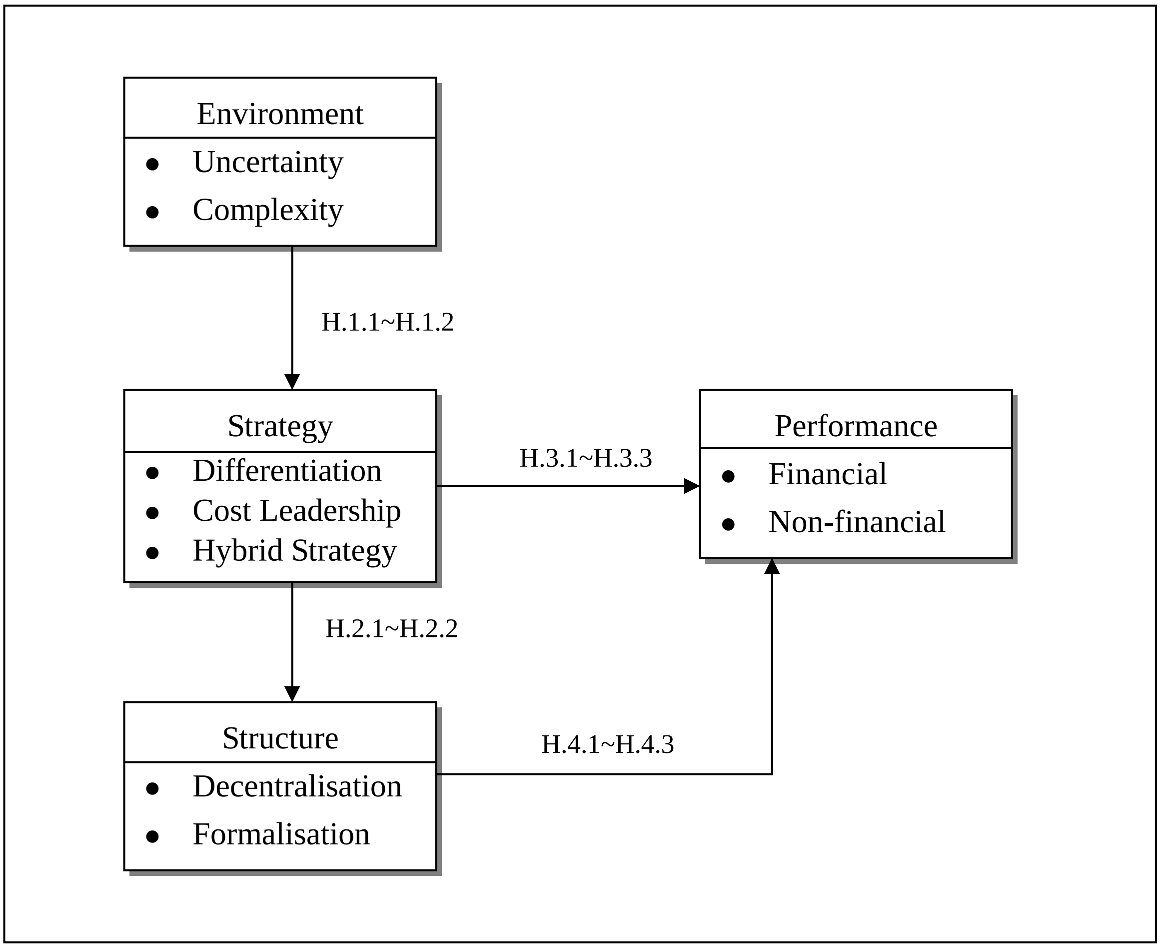
RQ 2. Is there any correlation between competitive strategies and organisational structure? ⇒ Analysis of the relationship between competitive strategies and organisational structure,

RQ 3. How much do competitive strategies influence a firm's performances? ⇒ Analysis of the relationship between competitive strategies and performances,

RQ 4. How far is organisational structure associated with a firm's performances? ⇒ Analysis of the relationship between organisational structure and performances.

5.3.2. Research Model

(Figure 5.11. A Research Model)



The above figure illustrates the model of this study; that is, the relationship between the environment and strategy (H.1.1~H.1.2), strategy and organisational structure (H.2.1~H.2.2), strategy and performance (H.3.1~H.3.3) and organisational structure and performance (H.4.1~H.4.3).

5.4. Hypotheses

5.4.1. The Relationship between Environment and Strategy

Both Korean GTCs and Japanese *Sogo Shoshas* are surrounded by an uncertain and complex business environment. In these circumstances it is crucial for them to choose a suitable strategy in order to create and sustain competitive advantage over their competitors. Based on this argument, hypotheses H.1.1~H.1.2 attempt to analyse the structural relationship between the environment and strategy of Korean GTCs and Japanese *Sogo Shoshas*.

Many people (for example, Barnard, 1938; March and Simon, 1958; Duncan, 1972; Grinyer, Ardekani and Bazzaz, 1980; Pennings, 1981; Krickx, 2000; and Wheelen and Hunger, 2007) argued that environmental uncertainty is a key concept for organisational theory and it has traditionally been considered a significant factor in the process of strategic management. Environmental uncertainty is the degree of complexity and the degree of change existing in an organisation’s external environment. So, it is a vitally important task for managers to make sense of the uncertain world surrounding their organisation. Another issue in organisational management is complexity. Complexity is the number of different occupational specialities and the degree of their heterogeneity and number of elements within the organisations’ environment (Hage and Dewar, 1973). Managers are no different from other individuals in the way that they cope with complexity; they try to simplify what is happening by focusing on those few aspects of the environment which have been important historically. Hence, it is important to find ways to avoid these tendencies when seeking to understand the environment, which are both usable and oriented towards the future (Johnson, Scholes and Whittington, 2005).

However, there are many sources of competitive strategies by which firms may create and sustain competitive advantage. As sources of a firm's competitive advantage, Porter (1980, 1985) identified three generic ways in which a firm can gain a sustainable competitive advantage over other firms in its industry: low cost, differentiation and focus. Kogut (1984, 1985) argued that, in an industry, technology, brand and information will do this and Bartlett and Ghoshal (1998) stressed three other elements for this purpose: geographic dispersion of assets, specialised operations and interdependent relationships. Furthermore, the source of competitive advantage was also reviewed using resource-based theory. Major elements are distinctive competence (Mahoney and Pandian, 1992), value, rareness, imitability and substitutability and unique resources and core competences (Johnson, Scholes and Whittington, 2005).

Of the many ways suggested of creating a firm's competitive advantage, this research chooses to use Porter's generic strategies of low cost and differentiation. However, Porter's original approach to competitive strategies was that firms can only be successful if they adopt either a differentiation or low cost strategy (i.e. they should choose only one of these). If they mix them, they end up with low perceived value and high price (i.e. stuck in the middle). However, both Korean GTCs and Japanese *Sogo Shoshas* are highly diversified enterprises. In the world of business, within diversified firms, a firm or a Strategic Business Unit (SBU) may choose one or two strategies simultaneously from generic strategies according to their own business situation and environment. This research is based on such an assumption.

A number of studies have been established to investigate the relationship between the environment and strategy. Most previous studies (Porter, 1980; Hambrick, 1983; Dess and Davis, 1984; Govindarajan, 1988; Miller, 1988; Chung and Chung, 1997; Kwon, Kim, Kim and Limb, 1999; Kang, 2002) demonstrated that a differentiation strategy is positively correlated with uncertain environments and it is more closely correlated with uncertain environments than low cost strategy is. Govindarajan (1986) supplied the following theoretical argument that the choice of a differentiation strategy rather than a low cost strategy would increase uncertainty in an SBU's task environment. A differentiation SBU, with its primary focus on uniqueness and exclusivity, is likely to engage in product innovation, whereas a low-cost SBU, with its primary emphasis on cost reduction, prefers to keep its product offerings stable over time. According to Miller (1988), the strategy of innovative differentiation is most likely to be pursued in uncertain environments and the strategy of cost leadership is associated with stable and predictable environments. The study by Chung and Chung (1997) of 169 Korean firms (not including the GTCs) also revealed that there has been a positive relationship between the environment and differentiation strategy.

In support of the above sets of arguments, the following hypotheses are formulated:

H. 1.1	The GTCs'/*Sogo Shoshas'* employment of a differentiation strategy will be positively associated with environmental uncertainty and complexity.
H. 1.2	The GTCs'/*Sogo Shoshas'* employment of a cost leadership strategy will be inversely associated with environmental uncertainty and complexity.

5.4.2. The Relationship between Strategy and Structure

First, however, some arguments should be developed concerning strategy and structure. Chandler (1962) recommended that the formulation of strategy be studied before the development of the organisational structure to implement this strategy. However, some organisational theorists have argued that it is incorrect to describe the relationship between strategy and structure as being one-way only. According to them, strategy and structure are more closely interrelated. Thus, structure needs to be considered as strategy is being developed (Lynch, 2000).

Employing the differentiation strategy has many implications for organisational structure. New product development and implementation are highly dependent upon creative ideas from members involved in the organisation (Porter, 1980) and also require the collaboration and close contact of managers from different departments (Miller, 1988). Thus, it is necessary to allow the free flow of ideas from all members rather than centralising the decision-making process. Miller (1988) argued that complexity and changes in product designs create the need to delegate authority to the experts most capable of making critical decisions. Top executives may be too remote from a situation or too untrained to make the necessary judgments. Prior research has found that high decentralisation is an appropriate response to increased uncertainty (Govindarajan, 1988; Kang, 2002). Govindarajan (1988) argued that as a task's environment becomes more uncertain, there will be need for more information. Centralisation is possible at low levels of uncertainty because the information processed does not overburden the organisation's hierarchy. However, as uncertainty increases, more exceptions arise, which must be referred upward in the hierarchy. As more exceptions are referred upward, the hierarchy becomes overloaded. As a result, serious delays develop between the upward transmission of information about the new situation and a downward response to that information. An effective way to deal with such a situation is to move the level of decision-making to where information exists rather than to bring it upward in the hierarchy.

A firm pursuing low cost strategy normally tends to focus on an internal issue of cost reduction and controls. Thus, there will be a strong emphasis on formal profit and budget controls – an aspect of formalisation – in order to keep costs and thus prices, at a minimum (Miller, 1988). According to Porter (1980), cost leadership strategy requires tight control of costs and overheads and a great deal of managerial attention to cost control is necessary to carry out this strategy. Furthermore, Miller (1988) argued that the cost leadership strategy requires that product lines remain rather stable. Unvarying products and procedures allow the division of work into its elementary components, those which are routinised, standardised and ideal for unskilled personnel. Therefore, there is little need for experts such as scientists and engineers who are most useful for handling complex and unstructured problems. Rather, top management can solve most of the administrative problems by themselves without specialists. In this case, liaison devices such as task force teams and cross-functional committees are costly luxuries and most decision-making is centralised upward. Based on the above sets of arguments, the second hypotheses relating to the linkages of strategy and structure are as follows:

H.2.1	The GTCs'/*Sogo Shoshas'* employment of a differentiation strategy will be positively associated with the delegation of power (decentralisation).
H.2.2	The GTCs'/*Sogo Shoshas'* employment of a cost leadership strategy will be positively associated with formal controls (formalisation).

5.4.3. The Relationship between Strategy and Performance

Each GTC/*Sogo Shosha* may select a specific strategy by considering its environment and undertake the selected strategy in order to enhance business performance. In this, their pursuit of performance goal will differ according to the strategy selected. In the process of choosing a specific strategy, some GTCs/*Sogo Shoshas* may fail to achieve any of the strategies that are called "stuck in the middle." Becoming stuck in the middle is often a manifestation of a firm's unwillingness to choose how it will compete. It possesses no competitive advantage and this strategic position is usually a recipe for below-average performance (Porter, 1985). To avoid these situations, each GTC/*Sogo Shosha* may select an appropriate strategy which fits its business situation.

The first hypothesis concerns the relationship between a differentiation strategy and gaining market shares and customers. A firm pursuing a differentiation strategy, in particular a differentiated prospector strategy, may concentrate its efforts on gaining market share and new customers rather than profitability, by exploiting new markets and developing new products or services in order to preoccupy markets at its competitors' expense. This argument was also presented by Miles and Snow (1978). They stressed that the differentiated prospector's prime capability is to find and exploit new markets and products and enact dynamically by continually modifying its product-market domain to take advantage of perceived opportunities and by emphasising flexibility in its technology and administrative system in order to facilitate rapid adjustment. Its growth primarily results from the location of new markets and the development of new products or services. Olson, Slater and Hult (2005) also supported this argument with the contention that differentiated prospectors are the most marketing- oriented of all the types of strategists and the key to their success is the development of new products and entry into new markets.

The second hypothesis concerns the relationship between a low cost strategy and profitability. The main purpose of the low cost strategy is to increase profitability and business effectiveness rather than gaining a bigger market share, based on stable existing markets, accumulated technologies and sophisticated labour power through internal formal budget controls. Miller (1988) argued that a firm tends to undertake low cost strategy under stable and predictable environments with a strong emphasis on profitability by controlling the budget. A similar argument was also presented by Miles and Snow (1978). According to them, low cost defenders typically grow by penetrating deeper into their current markets. This type of growth is facilitated by a narrow and stable domain which allows the organisation to become thoroughly familiar with client or customer needs. Consequently, firms pursuing low cost defender strategy concentrate on profitability rather than gaining market share, by emphasising existing and stable markets.

The third hypothesis relates to a hybrid strategy. According to Porter's original idea (1985), a firm must adopt either cost leadership or differentiation. Achieving cost leadership and differentiation are usually incompatible, because differentiation is usually costly. But reducing cost does not always involve a sacrifice of differentiation. If a firm can achieve cost leadership and differentiation simultaneously, the rewards are great. Bowman (1995) named eight different ways (on a strategy clock) in which managers might think about competitive strategy. They are no frills, low price, hybrid, differentiation, focused differentiation, increased price/standard value, increased price/low value and low value/standard price. The success of the hybrid strategy depends on the ability both to understand and to deliver enhanced value in terms of customer needs, while also having a cost base which permits low prices and is sufficient for reinvestment to maintain and develop the bases of differentiation (Johnson, Scholes and Whittington, 2005). A good example is Japanese saloon car manufacturers' strategy in the late 1980s in the European market. They provided cars to customers with better quality at competitive and reliable prices which were better than their rivals'. The hybrid strategy could be advantageous as an entry strategy into a new market. This strategy could be the strategic approach to new market development which Japanese firms have used in the past.

Based on the above sets of arguments, the following hypotheses relating to strategy and performance are formulated:

H.3.1	The GTCs'/*Sogo Shoshas'* employment of a differentiation strategy will be positively associated with gaining market shares and new customers.
H.3.2	The GTCs'/*Sogo Shoshas'* employment of a cost leadership strategy will be positively associated with profitability.
H.3.3	The GTCs'/*Sogo Shoshas'* employment of a hybrid strategy will be positively associated with new market development.

5.4.4. The Relationship between Structure and Performance

The major dimensions which characterise an organisation's structure are its degree of centralised decision-making, the formalisation of its rules and procedures and structural differentiation (John and Martin, 1984). As subjects of organisational structure, centralisation/decentralisation and formalisation have been treated as major topics in recent studies.

Centralisation refers to whether decision authority is closely held by top managers or is delegated to middle-and lower-level managers. Many studies have been carried out to analyse the relationship between centralisation and performance and three distinct views are evident. Most studies found that there were negative associations (McMahon, 1976; Pennings, 1976; Johnson, Scholes and Whittington, 2005; Olson, Slater and Hult, 2005), or zero association (Stathakopoulos, 1998; Dalton *et al*., 1980) between centralisation and performance. Mintzberg (1979) mentioned that decentralisation can stimulate employees' motivation. The organisation can attract and retain its staff and utilise their initiative if it gives them considerable power to make decisions. Conversely, Hage's (1965) study argued that centralisation increased production, efficiency and formalisation since the centralised organisation tended to very quickly develop a formalised procedure for passing messages. This argument was also supported by Kim (2000), who carried out a study of 47 listed Korean companies. Although decentralisation is positively associated with the increase of employee satisfaction and commitment, it inversely influences the firm's profitability. Tata and Prasad (2004) carried out further study of the relationship between two types of decentralisation, i.e. macro-level decentralisation and micro-level decentralisation[64] and job effectiveness in

[64] According to Tata and Prasad (2004), organisational centralisation/decentralisation can be shown to have two components. Participation in decision-making (macro-level decentralisation) is the degree of distribution of organisational decision-making processes in regard to policy decisions. It describes the extent to which employees have the authority for policy decisions and the power to make decisions about selection, promotion, new policies and new programmes. Authority hierarchy (micro-level centralisation) is the degree of concentration of decision-making in regard to task performance. It describes the extent to which authority over day-to-day task decisions is concentrated in a few hands, with employees having to defer to superiors when making decisions about their jobs.

team-self-management companies. They found that teams with high levels of self-management are more effective in organisations where the authority to make decisions about task performance, i.e. micro-level decentralisation, is distributed. However, the effectiveness is not influenced by the extent to which the authority to make decisions in policies and procedures, i.e. macro-level decentralisation, is concentrated in a few hands.

Formalisation is defined as the degree to which formal rules and procedures govern decisions and working relationships. Rules and procedures provide a means for prescribing appropriate behaviours and addressing routine aspects of a problem. These also can lead to increased efficiency and lower administrative costs (Olson, Slater and Hult, 2005). There have been some arguments over the relationship between formalisation and performance. The first argument is that formalisation is positively associated with a firm’s performance. Without a minimum level of formalisation, role ambiguity may occur. Moreover, role ambiguity may affect members’ attitude and performance (Rizzo, House and Lirtzman, 1970). But a second argument presented the view that formalisation adversely affects a firm’s performance if it is excessive. Formalisation may limit job scope, resulting in boredom, alienation, job dissatisfaction, absenteeism, high turnover and low output (Hackman and Lawler, 1971). Furthermore, Tata and Prasad (2004) found similar results, in that organisational formalisation moderates the influence of self-management on the judgments of team effectiveness. Formalised mechanisms of control restrict team members’ ability to perform a variety of tasks as well as the degree to which they can exercise authority while carrying out these tasks. Consequently, this may cause lower performance. The last argument demonstrated that there is no significant association between levels of formalisation and performance (Dalton *et al.*, 1980; Olson, Slater and Hult, 2005). Putting all the arguments together, it can be concluded that, in order to achieve higher performance, a firm needs an optimal level of formalisation, but not excessive formalisation which may limit job scope and cause job ambiguity.

The GTCs'/*Sogo Shoshas'* are traditionally and culturally centralised and formalised organisations. Although many Korean firms have recently been pursuing decentralisation or de-formalisation, centralisation and formalisation are still dominant organisational characteristics in many companies. As Kim (2000) found, decentralisation in Korean firms is inversely associated with a firm's profitability. It even positively influenced employee's satisfaction and commitment. This implies that a centralised structure would be more effective than decentralised structure, at least in Korea. This result, unlike the majority of studies, may originate from traditional top-down decision-making processes and highly centralised organisational structures. This leads to the three next hypotheses:

H.4.1	The GTCs'/*Sogo Shoshas'* organisational centralisation will be inversely associated with overall performance.
H.4.2	The GTCs'/*Sogo Shoshas'* organisational decentralisation will be positively associated with employee satisfaction and retention.
H.4.3	The GTCs'/*Sogo Shoshas'* organisational formalisation will be inversely associated with the speed of job handling.

5.5. Research Design and Methodology

5.5.1. Data Collection

The principal means of data collection for this study was a questionnaire survey undertaken between September and December 2006 in both Korea and Japan. Data were collected only from the Marketing and Sales SBUs of seven Korean GTCs and eight Japanese *Sogo Shoshas*. Both hand-delivered and mailed questionnaire surveys were conducted. In particular, it was possible to hand-deliver the questionnaires to Korean GTCs, because all of them were centrally located in Seoul. This undoubtedly helped to increase the rate of response to the questionnaires. Further, the personal relationship between the author and the respondents also encouraged an increased response rate since the author had nine years of business experience with them as a marketing and sales manager at a Korean multinational petrochemical enterprise. With the mailed questionnaires, a cover letter was sent explaining the purpose of the study and assuring the confidentiality of the responses. Respondents received return envelopes in which to send the completed questionnaires directly back to the author, in order to minimise response bias.

The questionnaire was designed to survey the strategic management and decision-making process within both Korean GTCs and Japanese *Sogo Shoshas* on the basis of various previous studies. In the questionnaire design, the research followed the typical procedure of developing questionnaires offered by Churchill and Brown (2004)[65] in

[65] They offered the following nine steps to take in preparing a questionnaire. i) specify what information will be sought, ii) determine the type of questions and method of administration, iii) determine the content of individual questions, iv) determine the form of response to each question, v) determine the wording of each question, vi) determine the question sequence, vii) determine the physical characteristics

their book “Marketing Research.” The questionnaire was prepared only in English for both Korea and Japan, because it was believed that a single language would minimise misunderstanding and complications. Another reason was that all respondents or employees in Korean GTCs and Japanese *Sogo Shosha* who participated in the questionnaire survey were good at English. They would have had enough language ability to comprehend the questionnaire, because this ability was one of the most important components when they were recruited. Even though the author was convinced that all respondents both in Korea and Japan were able to comprehend all the questions including their academic terminology, he inserted some explanatory words in Korean and Japanese into the questionnaires before distributing them. This was in order to removing any chance of the respondents’ misunderstanding the full meaning of questions, including their academic terms.

The population and sample of this research was restricted to employees in Marketing and Sales SBUs only. The reasons for restricting the population and sampling to employees associated with marketing and sales SBUs were two: i) one of the aims of this research is to examine only business-level strategy (competitive strategy) and ii) being limited to a single function of SBUs might increase data consistency. When questionnaires were distributed, the job position allowed a division into four groups; general staff, assistant manager, manager and senior manager and the period of working experience allowed another division into four groups: those with less than five years’, five to ten years’, ten to 15 years’ and over 15 years’ experience. In the case of the Korean GTCs, 158 questionnaires in total were distributed on the basis of

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of the questionnaire, viii) re-examine steps 1~7 and revise if necessary and ix) pre-test the questionnaire and revise if necessary (pp. 282~309).

the sample selection calculated from the population (for details of a sample calculation, see the next section). Of the 158 marketing and sales SBU members who received questionnaires, 129 (81.65%)[66] responded. In the case of the Japanese *Sogo Shoshas*, a total of 168 questionnaires were distributed. Of the 168, 77 (45.83%)[67] responded.

(Table 5.4. The Formation of the Sample)

• **Response Rate of Questionnaire**

	No. of Questionnaires Distributed	No. of Questionnaires Collected	No. of Questionnaires Unusable	Response Rate
Korean GTCs	158	129	0	81.65%
Japanese *S.S.*	168	77	0	45.83%

• **Job Position of Respondents**

	General Staff	Assistant Manager	Manager	Senior Manager	Others	Total
Korean GTCs	27.3%	22.7%	25.0%	21.9%	3.1%	100%
Japanese *S.S.*	24.7%	33.8%	23.4%	16.9%	1.3%	100%

• **Working Experience of Respondents**

	Less than 5 years	5 ~ 10 years	10~15 years	Over 15 years	Total
Korean GTCs	38.0%	30.2%	21.7%	10.1%	100%
Japanese *S.S.*	26.0%	24.7%	24.7%	24.7%	100%

[66] According to Churchill and Brown (2004), in Korea, businesspeople are reluctant to answer any survey questions about their company – it is considered disloyal to divulge any type of information to "outsiders." However, the personal relationship between the author and respondents allowed an increased rate of response.

[67] The response rate of the Japanese *Sogo Shoshas* was lower than that of Korean GTCs. However, in an examination of published studies in the field of organisational research in the years 1979~1983, Mitchell (1985) found a range of response rates of 30 to 94% (Bryman, 2004). Furthermore, Churchill and Brown (2004) argued that most Japanese businesspeople are hesitant to take part in surveys during business hours – taking time away from one's work for a survey is like "stealing" from one's employer.

After the questionnaire survey, in-depth interview survey was also carried out to supplement the data collection and as a means of cross checking the questionnaire survey against other sources of data. The purpose of the interviews was to have a more objective understanding of the questionnaire survey results and to learn more about strategic management and the decision-making process within Korean GTCs and Japanese *Sogo Shoshas*.

With regard to the number of interviewees, four manager-level members of staff associated with marketing and sales from Korean GTCs and two senior manager-level members of staff from Japanese *Sogo Shoshas* were interviewed. In order to arrange interview meetings, the author had to make many phone calls to these managers before they would agree to participate in interviews. Around seven Korean managers showed their intention to take part in the interview survey, whilst almost all the Japanese managers in *Sogo Shoshas* politely refused to do so.

In particular, for instance, a manager in Itochu Corporation said:

> *"According to my company's regulation, any individual who has private business is strictly prohibited to visit my office. Even those who have official businesses should report to the reception desk at the lobby of the building before entering the office."*

For several reasons, the author was able finally to arrange interview appointment with only two Japanese managers, but he arranged interviews with seven Korean managers. However, considering the balance of number between Korean and Japanese interviewees, the author decided to select only four managers from Korea.

Although the sample of interviewees was small and maybe not fully representative, they were selected on the basis of a wide range of factors, such as their expertise in business, position and role within their organisations, in order to remove sample error or bias as far as possible. With sufficient time, the author would have tried to arrange interviews with more managers. However, as mentioned earlier, the principal method of data collection for this study is a questionnaire survey, not an interview survey. As the author was fully convinced by the data collected in the questionnaire survey, it seemed to be safe to conduct interviews with only six managers for the purpose of cross checking the questionnaire survey data with the interview survey data.

The interviews were all on different dates. Interviewees were invited to give their comments on the strategic management and decision-making process within their organisations. Before each interview, the interviewee was given interview materials (see Appendix 3) prepared by the author. Interview material was prepared only in English. However, the actual interviews used both Korean and English for the Korean managers, but only English for the Japanese managers. Although the interview was conducted in English with Japanese managers, they had no significant problems of understanding academic or management terms because the author inserted some explanatory words in Japanese into the interview material. Interviewees were given discretion in expressing their feelings by filling up the blanks in interview material in their own handwriting. The theme of the interview was very similar to that of the questionnaire and each interview lasted one to two hours.

In the process of arranging interviews, the author noted the cultural difference between Korean and Japanese businessmen. According to Churchill and Brown (2004), both Korean and Japanese businesspeople are reluctant to answer any survey questions during business hours. Although employees in both countries were reluctant to take part in the survey, the refusal rate of the Japanese businesspeople was much higher than that of the Koreans.

5.5.2. Population and Sample Selection

The population and sample of this research was restricted to employees in marketing and sales SBUs only within Korean GTCs and Japanese *Sogo Shoshas*. In the case of the seven Korean GTCs, it was possible to know the exact numbers of all employees and the total number of marketing and sales employees. This allowed an easy calculation of a sample of the population. There were in total 4,699 employees as of 2005. Of the 4,699, there were 2,224 (approximately 47% of all employees) marketing and sales staff in the seven Korean GTCs. However, when it came to the Japanese *Sogo Shoshas*, it was possible to know only the total numbers of employees, but difficult to find how many marketing and sales staff there were. Thus, the numbers of marketing and sales persons in the eight Japanese *Sogo Shoshas* are based on those in the Korean GTCs. As mentioned earlier, the marketing and sales staff in the seven Korean GTCs occupied approximately 47% of the total. In order to anticipate the numbers of marketing and sales persons in Japanese *Sogo Shoshas*, the same ratio of 47% was applied. It can be seen as reasonable to apply this ratio, because the organisational structure (i.e. the allocation of human resources among different SBU functions) between Korean GTCs and Japanese *Sogo Shoshas* is very similar in many ways since the Korean GTCs were fundamentally modelled on the Japanese *Sogo Shoshas*. Using this ratio, the numbers of marketing and sales persons was calculated to be approximately 13,938. (There was a total of 29,655 employees in the eight *Sogo Shoshas* as of 2005. Of this 29,655, it was calculated that approximately 47% were marketing and sales persons = 13,938 persons).

(Table 5.5. Population Numbers: Total Marketing and Sales Employees within Korean GTCs and Japanese *Sogo Shoshas)*

Korean GTCs		**Japanese *Sogo Shoshas***	
Samsung Corp.	451	Mitsubishi Corp.	2,964
Hyundai Corp.	156	Mitsui and Co., Ltd.	2,944
Daewoo International Corp.	430	Sumitomo Corp.	2,242
LG International Corp.	296	Itochu Corp.	2,046
SK Networks	588	Marubeni Corp.	1,839
Hyosung Corp.	145	Nissho Iwai Corp.	898
Ssangyong Corp.	158	Tomen Corp.	526
Total	2,224	Nichimen Corp.	479
		Total	13,938

(Source: The Handbook of Korean GTCs and Japanese *Sogo Shoshas*, 2005)

Note:

- Korean GTCs: i) Employees in overseas offices are excluded, ii) SK Networks: Employees in domestic regional branch offices are excluded.

- Japanese *Sogo Shoshas*: i) There were 6,307 employees in Mitsubishi, 6,264 in Mitsui, 4,772 in Sumitomo, 4,355 in Itochu, 3,914 in Marubeni, 1,911 in Nissho Iwai, 1,120 in Tomen and 1,012 in Nichimen respectively. Based on these exact numbers, the approximate numbers of marketing and sales persons in each *Sogo Shosha* could be forecast by applying the ratio of 47%, ii) Employees in overseas offices are excluded.

Regarding the sample selection from the population, an Simple Random Sampling (SRS)[68] was used, which is one of the methods of probability sampling. The calculation formula of the sample size in SRS is adapted from the book "Sampling: Design and Analysis" by Lohr (1999, p. 40).

[68] A SRS is a sample selected in such a way that every possible sample with the same number of observations is equally likely to be chosen (Keller and Warrack, 2000).

$$n = \frac{z^2_{a/2} . s^2}{e^2 + \frac{z^2_{a/2} . s^2}{N}}$$ [69]

where;
n: Sample size,
s^2 : Sample variance,
e: Maximum tolerance error,
N: Population number,
$z_{a/2}$: the value that has a/2 area to the right in standard normal distribution and
a: Significance level.

Based on the above formula, the sample size (n) of Korean GTCs and Japanese *Sogo Shoshas* can be calculated as follows:

- **Sampling of Seven Korean GTCs**

$$n = \frac{(1.96)^2 .(1)^2}{(0.15)^2 + \frac{(1.96)^2 .(1)^2}{2,224}} = 158$$

- **Sampling of Eight Japanese *Sogo Shoshas***

$$n = \frac{(1.96)^2 .(1)^2}{(0.15)^2 + \frac{(1.96)^2 .(1)^2}{13,938}} = 168$$

* According to the table of standard normal distribution, $z_{a/2}$ is 1.96 when the significance level (a) is 0.05 (5%), which is the most commonly used level in the social sciences.

[69] This formula is a frequently used equation in scientific sample size estimation. It considers the maximum tolerance error that might occur between population and sample, although it does not consider non-responses. From the statistical standpoint, it is natural to assume non-responses. Furthermore, if the total number of the sample collected exceeds 30, it is classified as a "huge volume of data" and it allows statistical normality. Therefore, the total number of questionnaires collected from Korean GTCs (129,) and Japanese *Sogo Shoshas* (77) both have a significant value as they provide a huge volume of data. Consequently, it was expected that this equation would yield reliable results.

With regard to the sample selection for the interview survey, a judgment or purposive method of sampling was used, which is one of the methods of non-probability sampling. Judgment sampling or purposive sampling is one which hand-picks sample elements, in the expectation that that they will serve the research purpose. In judgment sampling, the researcher selects the sample on the basis of a judgment about the appropriate characteristics required of the sample member. Most typically, the samples selected are believed to represent the population of interest. However, sometimes this selection is not made on this basis, but rather because they can offer the required attributes (Churchill and Iacobucci, 2002).

In the present research, the primary justification for using judgment sampling was that the interview survey was only a supplementary tool for data collection. Another reason was time and cost issues. According to Bryman (2004), social research is frequently based on non-probability sampling methods such as convenience sampling, judgment sampling and quota sampling, since probability sampling involves much preparation and is therefore frequently avoided because of its difficulty and costs.

5.5.3. The Formulation of the Questionnaire

The questionnaire is divided into four sections covering strategic management of the Korean GTCs and Japanese *Sogo Shoshas*. Section one measures the business environment of the GTCs/*Sogo Shoshas* industry. In this study, two factors – uncertainty and complexity – were selected as variables to measure the environment. To measure environmental uncertainty and complexity, 12 items were cited or modified on the basis of previous studies (Olson, Slater and Hult, 2005; Kang, 2002; Sul, 2002) and some of them were developed by the author. Section two is designed to measure the strategy variables.

This study used Porter's (1980, 1985) generic strategies (i.e. a differentiation strategy and a cost leadership strategy) and Bowman's (1995) hybrid strategy (i.e. a mixed strategy of a differentiation and a cost leadership). To measure them, a total of 24 items were designed on the basis of Miller's (1998) and Kang's (2002) scales. Section three measures variables concerning organisational structure. To measure them, 17 items were adapted and developed, on the basis of studies by Olson, Slater and Hult (2005), Govindarajan (1988) and Lee (1998) to measure decentralisation and formalisation. Finally, section four was developed to measure organisational performance. 13 items were developed to cover the variables with respect to performance these were divided into overall performance, financial performance and non-financial performance on the basis of the BSC perspectives.

5.5.4. The Measurement of Variables

- **Measuring the Environment**

The modern business environment for firms can be summarised as delivering uncertainty, complexity and dynamism. The definition of environmental uncertainty is an inability to assign probabilities as to the likelihood of future events (Duncan, 1972; Pennings, 1981). Wheelen and Hunger (2007) stressed that environmental uncertainty is a threat to strategic managers because it hampers their ability to develop long-range plans and to make strategic decisions to keep the corporation in equilibrium with its external environment. Complexity is the number of different occupational specialities and the degree of heterogeneity and number of elements within an organisation's environment (Hage and Dewar, 1973). Within a complex environment, an organisation tends to establish an elaborate information-processing mechanism in order to scan the environment more effectively (Lawrence and Lorsch, 1967). Environmental dynamism has been defined as discontinuous changes within the environment. Hyper-competitive environments tend to be dynamic and their direction of change difficult to predict (Modarres, Beheshtian and Ispahani, 2003).

In this study, two factors – uncertainty and complexity – were selected as variables to measure the environment. To measure environmental uncertainty and complexity, 12 items were cited or modified on the basis of previous studies (Olson, Slater and Hult, 2005; Kang, 2002; Sul, 2002) and some were developed by the author. Olson, Slater and Hult (2005) measured the environment with two items – changes in customers' product preference and customers' tendency to look for new products or services to satisfy their needs. Kang (2002) used ten items to measure the environment with a seven-point Likert scale and Sul (2002) used 11 items with a seven-point Likert scale. In this study, the questions were, however, re-worded to accommodate the use of a five-point Likert scale ranging from ① agree strongly to ⑤ disagree strongly.

The following questions were designed to measure the environment with reference to Korean GTCs and Japanese *Sogo Shoshas.*

(Table 5.6. The Environment Scale)

Variables	Items
Uncertainty	1. It is difficult to predict market trends (A). 2. It is difficult to forecast customer's needs and tastes (A). 3. In our business, customers' product preferences change a lot over time (C: Olson, Slater and Hult, 2005). 4. Our customers tend to look for new products and services to satisfy their needs (C: Olson, Slater and Hult, 2005). 5. Actions of competitors are difficult to predict (R: Sul, 2002). 6. The life cycle of our products and services at present is short (C: Kang, 2002). 7. Competitors' new products and services frequently come to market at present (A).
Complexity	8. In our business, the channel of distribution is complex (A). 9. It is complex for us to develop new products and services (A). 10. The market is highly competitive (A). 11. There are many competing products and services (A). 12. Potential entrants threaten the market (C: Kang, 2002).

(Source: Cited by or adapted from Olson, Slater and Hult (2005), Kang (2002) and Sul (2002))
(A): Items developed by the author.
(C): Items cited or adapted from the previous studies.
(R): Reverse-coded items.

- **Measuring Competitive Strategy**

To measure strategy variables, this study selected Porter's (1980, 1985) generic strategies and Bowman's (1995) hybrid strategy. In a differentiation strategy, a firm seeks to be unique in its industry along some dimensions which are widely valued by buyers. Cost leadership refers to the ability of a firm to establish a clear cost advantage relative to its competitors (Porter, 1985). A hybrid strategy seeks simultaneously to achieve differentiation and a price lower than that of its competitors (Johnson, Scholes and Whittington, 2005).

To measure a differentiation strategy, seven items were designed on the basis of

Miller's (1998) and Kang's scales (2002) and three items were developed by the author. Miller (1998) used six items to measure innovative differentiation. The first, measuring the use of product-service innovation, was scaled from ① = we do not use this strategy to ⑦ = this is a very important strategy. The second item measured annual R & D costs as a percentage of sales, standardised to range over a seven-point scale. The third item measured the annual percentage of sales spent on initiating and implementing product-market innovations. The fourth measured the tendency to beat competitors to the markets. The fifth gauged innovative orientation and the last one measured competitive aggressiveness. In this study, five items were adapted from Miller's scales (1988) to measure differentiation. Kang (2002) used 13 items to measure differentiation on a seven-point Likert scale. In this study, two items were adapted from Kang's scales (2002) to measure differentiation.

With reference to the cost leadership strategy, seven items altogether were designed. Three items were developed on the basis of Miller's study (1998) and four items were developed by the author. Miller (1998) used six items to measure cost leadership. They are: the use of a cost centre for cost control, the use of fixing standard cost by analysing variance for cost control, price cutting for advertising expenditure, minimising advertising expenses, a proclivity for projects and boldness of decisions. In this study, three items were adapted from Miller (1998).

The hybrid strategy attempts to reduce cost while simultaneously improving quality. To measure the variables of a hybrid strategy, seven items were developed by the author on the basis of Johnson, Scholes and Whittington's strategy clock (2005): competitive strategy options.

(Table 5.7. The Strategy Scale)

Variables	Items
Differentiation	1. We use product/service innovations as a means of competing (C: Miller, 1988). 2. Our annual R & D costs for development of products and services are high (R: Miller, 1988). 3. Our annual percentage of sales spent on costs of initiating and implementing product-market innovation is high (C: Miller, 1988). 4. We always try to be ahead of competitors in product novelty or speed of innovation (C: Miller, 1988). 5. We pursue a tough "undo the competitors" philosophy (C: Miller, 1988). 6. We rapidly respond to customers' changing of needs and tastes (A). 7. We develop new products and services to meet customers' needs (A). 8. We invest heavily in advertising, sales promotion and public relations (A). 9. We try to enhance our corporate image (C: Kang, 2002). 10. We frequently analyse competitors' strategy (C: Kang, 2002).
Cost Leadership	11. We use cost centres and fix standard costs by analysing variances for cost control (C: Miller, 1988). 12. We try to minimise advertising expenditures (C: Miller, 1988). 13. We have a strong proclivity for low-risk projects with normal and certain rates of return (C: Miller, 1988). 14. We try to control levels of inventory (A). 15. All employees are appointed to their posts considering productivity (A). 16. We try to cut administrative expenses (A). 17. All employees fully understand the need for cost reduction (A).
Hybrid Strategy (Differentiation and Low cost)	18. We use a high-quality & low price strategy when entering into new markets (A) 19. We offer a wide range of good quality products and services at lower prices than our rivals (A). 20. We always try to find suppliers who offer us high-quality products and services at lower price (A). 21. We maintain long-term relationship with our regular suppliers who offer us high-quality products and services at lower price (A). 22. Our regular buyers purchase our products and services on the basis of high quality and lower price (A). 23. We are able to offer high-quality products and services to our customers based on our competitive distribution channel, logistics and transport systems that reduce costs (A). 24. To deliver high-quality products and services to our customers at low cost, we reinvest in R & D (A).

(Source: Cited by or adapted from Miller (1988) and Kang (2002))

- **Measuring Organisational Structure**

Variables with respect to organisational structure, in total 17 items, were adapted and developed on the basis of studies by Olson, Slater and Hult (2005), Govindarajan (1988) and Lee (1998) to measure decentralisation and formalisation.

Decentralisation is the degree of transferring decision-making power to lower levels. In order to measure it, this study used Olson, Slater and Hult's (2005) and Govindarajan's (1988) scales. Olson, Slater and Hult (2005) used seven items to measure decentralisation. They are i) the degree of decision-making at high levels, ii) the degree of individual decision-maker's latitude, iii) manager's flexibility in getting work done, iv) the degree to which individual decision-making is discouraged, v) the degree of decision-making in small matters and vi) the autonomy of middle- and lower-level managers.

Formalisation is the degree of emphasis on specific rules and procedures in carrying out tasks. To measure formalisation, two items were adapted from Olson, Slater and Hult's (2005) study, two items were developed based on Lee's (1998) study, which also measured all constructs on seven-point Likert scales and three items were developed by the author.

(Table 5.8. The Structure Scale)

Variables	Items
Decentralisation	1. In your company, decisions tend to be not made at a high level (R: Olson, Slater and Hult, 2005). 2. The individual decision-maker has wide latitude in the choice of means to accomplish goals (C: Olson, Slater and Hult, 2005). 3. Middle-and lower-level managers are allowed flexibility in getting work done (C: Olson, Slater and Hult, 2005). 4. A person who wants to make his decision would not quickly be discouraged (R: Olson, Slater and Hult, 2005). 5. Small matters are not referred to someone higher in your company for a decision (R: Olson, Slater and Hult, 2005). 6. Many important decisions are made locally rather than centrally (R: Olson, Slater and Hult, 2005). 7. Middle-and lower-level managers have substantial autonomy (C: Olson, Slater and Hult, 2005). 8. Middle-and lower-level managers are allowed to increase the level of expenditure for advertising and promotion (C: Govindarajan, 1988). 9. Middle-and lower-level managers are allowed to change the selling price on a major products or services (C: Govindarajan ,1988). 10. Middle-and lower-level managers are allowed to increase the number of employees in a business unit (C: Govindarajan, 1988).
Formalisation	11. If employees wish to make their own decisions, they are quickly referred to a policy manual. (C: Olson, Slater and Hult, 2005). 12. Individuals in your company frequently refer to it as a "bureaucracy" (C: Olson, Slater and Hult, 2005). 13. Our company attaches importance to basic principles and all instructions are made through formal documentation (A). 14. Regardless of changing conditions, our company has faith in past management principles which have proven effectiveness (A). 15. The communication channel in our company is very formalised (A). 16. Employees have only restricted access to financial and management information (C: Lee, 1998). 17. Our company persists with the same management style rather than diversifying its management style (C: Lee, 1998).

(Source: Cited by or adapted from Olson, Slater and Hult (2005), Govindarajan (1988) and Lee (1998))
(A): Items developed by the author.
(C): Items cited or adapted from the previous studies.
(R): Reverse-coded items.

- **Measuring Performance**

Variables with respect to performance are divided into overall performance, financial performance and non-financial performance, on the basis of the BSC approach. To measure overall performance, three items, based on Olson, Slater and Hult's (2005) study, were used to ask whether overall performance met expectations, exceeded competitors' and satisfied top management. To measure financial performance, it used typical financial indicators such as sales amounts, profitability and cash flow; three items were developed by the author. To measure non-financial performance, it took three perspectives – customer perspective, learning and growth perspective and internal-business process perspective; and seven items were developed by the author.

(Table 5.9. The Performance Scale)

Variables	Items
Overall performance	1. The overall performance of our company met expectations last year (C: Olson, Slater and Hult, 2005). 2. The overall performance of the business last year exceeded that of our major competitors (C: Olson, Slater and Hult, 2005). 3. Top management was very satisfied with the overall performance of the business last year (C: Olson, Slater and Hult, 2005).
Financial performance	4. The sales of our company increased in the last financial year compared to the previous one (A). 5. The profitability of our company increased in the last financial year compared to the previous one (A). 6. The cash flow of our company is stable compared to last year (A).
Non-financial performance	7. The market share increased in the last financial year compared to the previous one (A). 8. The number of new customers increased in the last financial year compared to the last one (A). 9. Employee satisfaction and retention has increased (A). 10. Employees' speed of job handling has increased (A). 11. Employees are more responsive toward customers (A). 12. Employee empowerment has increased (A). 13. Employee productivity has increased (A).

5.5.5. Statistic Data Analysis Instrument

The instrument of data analysis in this research was largely dependent on statistical methods and used the Statistical Package for Social Science (SPSS) for Windows program. Regression analyses (simple and multiple) and the Pearson coefficient of correlation analysis were mainly used to analyse the questionnaire survey data. In addition, descriptive statistics was also used to check mean and standard deviation. The following table shows the statistical techniques which were used for each hypothesis.

(Table 5.10. Statistical Techniques used for each Hypothesis)

Hypothesis	Variables to be tested	Statistical Tools
H.1.1	● Differentiation/Uncertainty and Complexity	● Correlation Analysis[70]
H.1.2	● Cost leadership/Uncertainty and Complexity	● Multiple Regression[71]
H.2.1	● Differentiation/Decentralisation	● Simple Regression (Korea) ● Correlation Analysis (Japan)
H.2.2	● Cost leadership/Formalisation	● Correlation Analysis (Korea) ● Simple Regression (Japan)
H.3.1	● Differentiation/Market shares and New customers	● Multiple Regression
H.3.2	● Cost leadership/Profitability	● Correlation Analysis
H 3.3	● Hybrid/New market development	● Correlation Analysis (Korea) ● Simple Regression (Japan)
H.4.1	● Centralisation/Overall performance	● Correlation Analysis
H.4.2	● Decentralisation/Employee's satisfaction and retention	● Correlation Analysis
H.4.3	● Formalisation/Speed of job handling	● Correlation Analysis

[70] Correlation, also called the correlation coefficient, indicates the strength and direction of a linear relationship between two random variables. Correlation refers to the departure of two variables from independence, although correlation does not imply causation.

[71] Simple linear regression and multiple linear regression are related statistical methods for modelling the relationship between two or more random variables, using a linear equation. Simple linear regression refers to a regression of one variable on one other variable while multiple regression refers to a regression of the dependent variable on two or more variables. The use of linear regression assumes that the best estimate of the response is a linear function of some variable(s).

5.6. Statistic Data Analysis Results

5.6.1. Descriptive Statistics

The table below shows the value of Mean and Standard Deviation of each variable. Both in Korean GTCs and Japanese *Sogo Shoshas*, the value of the mean ranges from 2.19 to 2.78 and the value of Standard Deviation ranges from 0.46 to 0.83.

(Table 5.11. Mean and Standard Deviation of Variables)

Variables	N	Mean	S.D
Korean GTCs			
Differentiation (present)	129	2.68	0.47
Differentiation (future)	129	2.45	0.54
Uncertainty (present)	128	2.78	0.60
Uncertainty (future)	126	2.62	0.67
Complexity (present)	129	2.19	0.66
Complexity (future)	129	2.37	0.62
Cost leadership (present)	129	2.47	0.48
Cost leadership (future)	127	2.46	0.50
Decentralisation	129	2.76	0.63
Formalisation	129	2.78	0.52
Market share	129	2.58	0.84
Acquisition of new customers	129	2.58	0.70
Profitability	129	2.58	0.90
Hybrid strategy (present)	129	2.45	0.46
Hybrid strategy (future)	127	2.31	0.55
Overall performance	129	2.63	0.77
Employee’s satisfaction and retention	129	2.74	0.73
Speed of job handling	129	2.57	0.69
Japanese *Sogo Shoshas*			
Differentiation (present)	76	2.72	0.46
Differentiation (future)	77	2.48	0.53
Uncertainty (present)	75	2.86	0.59
Uncertainty (future)	77	2.66	0.62
Complexity (present)	77	2.19	0.70
Complexity (future)	77	2.43	0.62
Cost leadership (present)	76	2.54	0.47
Cost leadership (future)	74	2.51	0.47
Decentralisation	77	2.72	0.52
Formalisation	76	2.34	0.62
Market share	77	2.52	0.70
Acquisition of new customers	77	2.49	0.74
Profitability	77	2.32	0.83
Hybrid strategy (present)	75	2.52	0.57
Hybrid strategy (future)	76	2.34	0.62
Overall performance	77	2.54	0.60
Employee satisfaction and retention	77	2.73	0.64
Speed of job handling	77	2.56	0.66

5.6.2. Correlation Matrix

The following tables show the result of correlation analysis between each variable in the matrix.

(Table 5.12. Correlation Matrix: Korean GTCs)

		PRESENT								
		DI	UN	CO	CL	FO	DE	PR	HS	MD
PRESENT	Differentiation (DI)	1.000	0.306	0.315						
	Uncertainty (UN)	0.306	1.000							
	Complexity (CO)	0.315		1.000						
	Cost Leader (CL)				1.000	0.317	0.195	0.105		
	Formalisation (FO)				0.317	1.000				
	Decentralisation (DE)				0.195		1.000			
	Profitability (PR)				0.105			1.000		
	Hybrid Strategy (HS)								1.000	0.252
	Market Devel. (MD)								0.252	1.000

		FUTURE								
		DI	UN	CO	CL	FO	DE	PR	HS	MD
FUTURE	Differentiation (DI)	1.000	0.457	0.293						
	Uncertainty (UN)	0.457	1.000							
	Complexity (CO)	0.293		1.000						
	Cost Leader (CL)				1.000	0.374	0.155	0.125		
	Formalisation (FO)				0.374	1.000				
	Decentralisation (DE)				0.155		1.000			
	Profitability (PR)				0.125			1.000		
	Hybrid Strategy (HS)								1.000	0.140
	Market Devel. (MD)								0.140	1.000

		PRESENT					
		DE	OP	ES	FO	SJ	RC
PRESENT	Decentralisation (DE)	1.000	0.273	0.352			
	Overall Perform (OP)	0.273	1.000				
	Employee Satisf. (ES)	0.352		1.000			
	Formalisation (FO)				1.000	0.063	0.191
	Speed of Job (SJ)				0.063	1.000	
	Response to Customers. (RC)				0.191		1.000

** Significant at the 0.05 level ($p<0.05$), 2-tailed
*** Significant at the 0.01 level ($p<0.01$), 2-tailed

(Table 5.13. Correlation Matrix: Japanese *Sogo Shoshas*)

		PRESENT					
		DI	UN	CO	DE	CL	PR
P	Differentiation (DI)	1.000	0.321	0.352	0.341		
R	Uncertainty (UN)	0.321	1.000				
E	Complexity (CO)	0.352		1.000			
S E	Decentralisation (DE)	0.341			1.000	0.134	
N	Cost Leader (CL)				0.134	1.000	0.053
T	Profitability (PR)					0.053	1.000

		FUTURE					
		DI	UN	CO	DE	CL	PR
F	Differentiation (DI)	1.000	0.392	0.478	0.124		
U	Uncertainty (UN)	0.392	1.000				
T	Complexity (CO)	0.478		1.000			
U R	Decentralisation. (DE)	0.124			1.000	0.140	
E	Cost Leader (CL)				0.140	1.000	0.110
	Profitability (PR)					0.110	1.000

		PRESENT					
		DE	OP	ES	FO	SJ	RC
P	Decentralisation (DE)	1.000	-0.035	0.324			
R	Overall Perform (OP)	-0.035	1.000				
E	Employee Satisf. (ES)	0.324		1.000			
S	Formalisation (FO)				1.000	0.248	0.176
E	Speed of Job (SJ)				0.248	1.000	
N T	Response to Customers (RC)				0.176		1.000

** Significant at the 0.05 level (p<0.05), 2-tailed
*** Significant at the 0.01 level (p<0.01), 2-tailed

5.6.3. Testing of Hypotheses

- **Hypothesis 1.1: A Differentiation Strategy/Environmental Uncertainty Complexity**

Hypothesis 1.1 relates to a firm's strategy and the business environment. (H.1.1: The GTCs'/*Sogo Shoshas'* employment of a differentiation strategy will be positively associated with environmental uncertainty and complexity). It examined not only the respondents' feeling at present, but also their expectations in the future. The results of the Pearson coefficient of correlation for H.1.1 are as follows:

(Table 5.14. Results of Pearson Coefficient of Correlation for H.1.1)

Korean GTCs

	Present		Future	
	Differentiation/ Uncertainty	Differentiation/ Complexity	Differentiation/ Uncertainty	Differentiation/ Complexity
Pearson Correlation (*r*)	0.306	0.315	0.457	0.293
p-value	0.000***	0.000***	0.000***	0.001***

Japanese *Sogo Shoshas*

	Present		Future	
	Differentiation/ Uncertainty	Differentiation/ Complexity	Differentiation/ Uncertainty	Differentiation/ Complexity
Pearson Correlation (*r*)	0.321	0.352	0.392	0.478
p-value	0.005***	0.000***	0.000***	0.000***

*** Significant at the 0.01 level ($p<0.01$), 2-tailed

The significant and positive correlation between a differentiation strategy and environmental uncertainty and complexity found by many previous studies is found here too. With respect to Korean GTCs respondents' feeling at present, the result shows that a differentiation strategy is positively correlated with environmental uncertainty ($r = 0.306$, $p<0.01$) and complexity ($r = 0.315$, $p<0.01$), as predicted. It also examined the respondents' expectations in the future and found that there is no significant difference in respondents' feeling at present and their expectations in the future. As at present, both environmental uncertainty ($r = 0.457$, $p<0.01$) and complexity ($r = 0.293$, $p<0.01$) are positively correlated with a differentiation strategy in the future. In the case of Japanese *Sogo Shoshas*, almost the same result is obtained. Therefore, Hypothesis 1.1 is accepted.

- **Hypothesis 1.2: A Cost Leadership Strategy/Environmental Uncertainty Complexity**

Hypothesis 1.2 also relates to a firm's strategy and the business environment. (H.1.2: The GTCs'/*Sogo Shoshas'* employment of a cost leadership strategy will be inversely associated with environmental uncertainty and complexity). To analyse the data, multiple regression was used.

In Korea's case, the value of Coefficient of Determination (R^2) is 0.237 (23.7%) at present and 0.246 (24.6%) in the future. This means that a regression model explains that a cost leadership strategy is inversely associated with environmental uncertainty and complexity in both the present and the future (Uncertainty Present: Regression Coefficient (R.C.) = 0.331, $p < 0.01$; Uncertainty Future: R.C. = 0.114, $p < 0.01$; Complexity Present: R.C.= 0.138, $p < 0.05$; Complexity Future: R.C. = 0.047, $p < 0.05$).

(Table 5.15. Results of Multiple Regression for H.1.2)

Korean GTCs

	Strategy	
	Cost Leadership	
Independent Variables	Present	Future (square root transformation about dependent variable)
(constant)	1.242 (0.000) ***	1.136 (0.000) ***
Uncertainty	0.331 (0.000) ***	0.114 (0.000) ***
Complexity	0.138 (0.016) **	0.047 (0.014) **
Coefficient of Determination (R^2)	0.237	0.246
Overall F	19.408	20.012
p-value	0.000***	0.000***

Japanese *Sogo Shoshas*

	Strategy	
	Cost Leadership	
Independent Variables	Present	Future
(constant)	1.535 (0.000) ***	1.604 (0.000) ***
Uncertainty	0.218 (0.012) **	0.161 (0.082) *
Complexity	0.164 (0.026) **	0.205 (0.010) **
Coefficient of Determination (R^2)	0.174	0.151
Overall F	7.490	6.137
p-value	0.001***	0.004***

* $p<0.1$, ** $p<0.05$, ***$p<0.01$

In the case of the Japanese *Sogo Shoshas*, the value of R^2 is lower than that of the Korean GTCs' (present = 0.174, future = 0.151). Although the value of R^2 is lower than that for Korea, a regression model also explains that a cost leadership strategy is inversely associated with environmental uncertainty and complexity. (Uncertainty Present: R. C. = 0.218, $p < 0.05$; Uncertainty Future: R.C. = 0.161, $p < 0.1$; Complexity Present: R.C.= 0.164, $p < 0.05$; Complexity Future: R.C. = 0.205, $p < 0.05$). So, Hypothesis 1.2 receives full support.

- **Hypothesis 2.1: A Differentiation Strategy/Organisational Decentralisation**

Hypothesis 2.1 relates to a firm's strategy and organisational structure (H.2.1: The GTCs'/*Sogo Shoshas'* employment of a differentiation strategy will be positively associated with the delegation of power (decentralisation)). For Korean GTCs, a simple regression was used.

(Table 5.16. Results of Simple Regression for H.2.1: Korean GTCs)

	Strategy	
	Differentiation	
Independent Variables	Present	Future (sqrt transformation about dependent var)
(constant)	1.610 (0.000) ***	1.292 (0.000) ***
Decentralisation	0.383 (0.000) ***	0.096 (0.000) ***
Coefficient of Determination (R^2)	0.226	0.119
Overall F	36.866	17.157
p-value	0.000***	0.000***

***p<0.01

The result shows that a value of Coefficient of Determination (R^2) is 0.226 (22.6%) at present and 0.119 (11.9%) in the future. This supports the hypothesis that the Korean GTCs' employment of a differentiation strategy is positively associated with organisational decentralisation in both the present and the future (Present: R.C. = 0.383, $p < 0.01$; Future: R.C. = 0.096, $p < 0.01$)

For Japanese *Sogo Shoshas*, the Pearson coefficient of correlation analysis is used. With respect to the respondents' feeling at present, a differentiation strategy is positively correlated with organisational decentralisation, as hypothesised (r = 0.341, $p<0.01$). However, the respondents expect that there will be no correlation between a differentiation strategy and organisational decentralisation in the future.

(Table 5.17. Results of Pearson Coefficient of Correlation for H.2.1: Japanese *Sogo Shoshas*)

	Present	Future
	Differentiation/Decentralisation	Differentiation/Decentralisation
Pearson Correlation (r)	0.341	0.124
p-value	0.003***	0.281

*** Significant at the 0.01 level (p<0.01), 2-tailed

- **Hypothesis 2.2: A Cost Leadership Strategy/Organisational Formalisation**

Hypothesis 2.2 relates to a cost leadership strategy and organisational formalisation (H.2.2: The GTCs'/*Sogo Shoshas'* employment of a cost leadership strategy will be positively associated with formal controls (formalisation)). For Korean GTCs, the Pearson coefficient of correlation analysis is used. The result shows that a statistical significance is found between the cost leadership strategy and organisational formalisation in both the present (r = 0.317, $p<0.01$) and the future (r = 0.374, $p<0.01$).

(Table 5.18. Results of Pearson Coefficient of Correlation for H.2.2: Korean GTCs)

	Present	Future
	Cost Leadership/Formalisation	Cost Leadership/Formalisation
Pearson Correlation (r)	0.317	0.374
p-value	0.000***	0.000***

*** Significant at the 0.01 level ($p<0.01$), 2-tailed

For Japanese *Sogo Shoshas*, a simple regression was used. The result shows that a value of Coefficient of Determination (R^2) is 0.105 at present and 0.152 in the future. It supports a statistical significance between a cost leadership strategy organisational formalisation (Present: R.C. = 0.330, $p < 0.01$; Future: R.C. = 0.404, $p < 0.01$). So, Hypothesis 2.2 receives full support.

(Table 5.19. Results of Simple Regression for H.2.2: Japanese *Sogo Shoshas*)

	Strategy	
	Cost Leadership	
Independent Variables	Present	Future
(constant)	1.578 (0.000) ***	1.320 (0.000) ***
Formalisation	0.330 (0.005) ***	0.404 (0.001) ***
Coefficient of Determination (R^2)	0.105	0.152
Overall F	8.567	12.738
p-value	0.005***	0.001***

***$p<0.01$

- **Hypothesis 3.1: A Differentiation Strategy/Market Share and New Customers**

Hypothesis 3.1 predicted that the GTCs'/*Sogo Shoshas'* employment of a differentiation strategy will be positively associated with the gaining of market shares and new customers.

In the Korean case, the value of Coefficient of Determination (R^2) is 0.189 at present and 0.179 in the future. It was found that Korean GTCs' employment of a differentiation strategy is positively correlated with gaining a new market share and the acquisition of new customers in both the present and future. (Market Share Present: R. C. = 0.161, $p < 0.01$; Market Share Future: R.C. = 0.204, $p < 0.01$; Acquisition of New Customers Present: R.C.= 0.165, $p < 0.01$; Acquisition of New Customers Future: R.C. = 0.155, $p < 0.05$).

In the case of the Japanese *Sogo Shoshas*, a value of Coefficient of Determination (R^2) is 0.178 at present and 0.133 in the future. Their employment of differentiation strategies is positively correlated with gaining a new market share and the acquisition of new customers at present. (Market Share Present: R. C. = 0.173, $p < 0.05$; Acquisition of New Customers Present: R.C. = 0.153, $p < 0.05$).

With respect to the respondents' expectation for the future, a statistical significance was obtained between the differentiation strategy and the new market share (Market Share Future: R. C. = 0.276, $p < 0.01$). But there is no significance between a differentiation strategy and the acquisition of new customers, even though a statistically significant regression model is obtained (Acquisition of New Customers Future: R.C. = 0.181, $p > 0.1$).

(Table 5.20. Results of Multiple Regression for H.3.1)

Korean GTCs

	Strategy	
	Differentiation	
Independent Variables	Present	Future
(constant)	1.838 (0.000) ***	1.526 (0.000) ***
Market share	0.161 (0.001) ***	0.204 (0.000) ***
Acquisition of New customers	0.165 (0.004) ***	0.155 (0.020) **
Coefficient of Determination (R^2)	0.189	0.179
Overall F	14.652	13.774
p-value	0.000***	0.000***

** $p<0.05$, ***$p<0.01$

Japanese *Sogo Shoshas*

	Strategy	
	Differentiation	
Independent Variables	Present	Future
(constant)	1.898 (0.000) ***	1.782 (0.000)***
Market share	0.173 (0.032) **	0.276 (0.001)***
Acquisition of New customers	0.153 (0.045) **	0.181 (0.138)
Coefficient of Determination (R^2)	0.178	0.133
Overall F	7.881	11.548
p-value	0.001***	0.001***

** $p<0.05$, ***$p<0.01$

- **Hypothesis 3.2: A Cost Leadership Strategy/Profitability**

Hypothesis 3.2 anticipated that the GTCs'/*Sogo Shoshas'* employment of a cost leadership strategy will be positively associated with profitability. To analyse the data, the Pearson coefficient of correlation analysis is used.

(Table 5.21. Results of Pearson Coefficient of Correlation for H.3.2)

Korean GTCs

	Present	Future
	Cost Leadership/Profitability	Cost Leadership/Profitability
Pearson Correlation (*r*)	0.105	0.125
p-value	0.237	0.163

Japanese *Sogo Shoshas*

	Present	Future
	Cost Leadership/Profitability	Cost Leadership/Profitability
Pearson Correlation (*r*)	0.053	0.110
p-value	0.650	0.353

Contrary to what was predicted, Korean GTCs' and Japanese *Sogo Shoshas'* employment of a cost leadership strategy did not correlate with their profitability in either the present or the future. The values of the correlation coefficient in both the Korean GTCs (r = 0.105 (present), r = 0.125 (future)) and the Japanese *Sogo Shoshas* (r = 0.053 (present), r = 0.110 (future)) are less than 0.2, which denotes no correlation between variables. Hypothesis 3.2 is therefore not accepted.

- **Hypothesis 3.3: A Hybrid Strategy/New Market Development**

Hypothesis 3.3 relates to a hybrid strategy and new market development (H.3.3: The GTCs'/*Sogo Shoshas'* employment of a hybrid strategy will be positively associated with new market development). For Korean GTCs, the Pearson coefficient for correlation analysis is used. According to the result, Korean GTCs' employment of a hybrid strategy is positively correlated with a new market development at present (r = 0.252, $p<0.01$). However, there is no statistical significance in the future (r = 0.140)

(Table 5.22. Results of Pearson Coefficient of Correlation for H.3.3: Korean GTCs)

	Present	Future
	Hybrid Strategy/New Market Development	Hybrid Strategy/New Market Development
Pearson Correlation (r)	0.252	0.140
p-value	0.004***	0.118

*** Significant at the 0.01 level ($p<0.01$), 2-tailed

For Japanese *Sogo Shoshas*, a simple regression was used. The result shows that the relationship between their employment of a hybrid strategy and new market development is statistically significant in both the present and the future (Present: R.C. = 0.108, $p < 0.01$; Future: R.C. = 0.362, $p < 0.01$).

(Table 5.23. Results of Simple Regression for H.3.3: Japanese *Sogo Shoshas*)

	Strategy	
	Hybrid Strategy	
Independent Variables	Present	Future
(constant)	1.306 (0.000) ***	1.429 (0.000) ***
New Market Development	0.108 (0.000) ***	0.362 (0.000) ***
Coefficient of Determination (R^2)	0.179	0.171
Overall F	15.926	15.222
p-value	0.000***	0.000***

***p<0.01

- **Hypothesis 4.1: Centralisation/Overall Performance**

Hypotheses 4.1~ 4.3 relate to organisational structure and a firm's performance. Unlike previous hypotheses, these three hypotheses examined only the respondents' feeling at present. Hypothesis 4.1 anticipated that the GTCs'/*Sogo Shoshas'* organisational centralisation will be inversely associated with overall performance. To analyse the data, the Pearson coefficient for correlation analysis is used.

According to the result, Korean GTCs' employment of organisational centralisation is statistically significant for their overall performance (r = 0.273, $p<0.01$). However, in the case of the Japanese *Sogo Shoshas*, it shows that there is no statistical significance between their organisational centralisation and overall performance. Thus, Hypothesis 4.1 receives only partial support.

(Table 5.24. Results of Pearson Coefficient of Correlation for H.4.1)

	Centralisation/Overall Performance	
	Korean GTCs	Japanese *Sogo Shoshas*
Pearson Correlation (r)	0.273	-0.035
p-value	0.002***	0.765

*** Significant at the 0.01 level (p<0.01), 2-tailed

- **Hypothesis 4.2: Decentralisation/Employees' Satisfaction and Retention**

To test Hypothesis 4.2, the Pearson coefficient for correlation analysis is also used. It hypothesised that the GTCs'/*Sogo Shoshas'* organisational decentralisation will be positively associated with employee satisfaction and retention.

(Table 5.25. Results of Pearson Coefficient of Correlation for H.4.2)

	Decentralisation/Employee's Satisfaction and Retention	
	Korean GTCs	Japanese *Sogo Shoshas*
Pearson Correlation (r)	0.352	0.324
p-value	0.000***	0.004***

*** Significant at the 0.01 level (p<0.01), 2-tailed

Consistent with our prediction, both Korean GTCs' and Japanese *Sogo Shoshas'* employment of organisational decentralisation is positively associated with employee's satisfaction and retention (Korean GTCs: $r = 0.352$, $p<0.01$; Japanese *Sogo Shoshas*: $r = 0.324$, $p<0.01$). Therefore, Hypothesis 4.2 receives full support.

- **Hypothesis 4.3: Formalisation/Speed of Job Handling**

The last hypothesis, 4.3, predicted that the GTCs'/*Sogo Shoshas'* organisational formalisation will be inversely associated with the speed of job handling. To analyse the data, the Pearson coefficient for correlation analysis is used.

(Table 5.26. Results of Pearson Coefficient of Correlation for H.4.3)

	Formalisation/Speed of Job Handling	
	Korean GTCs	Japanese *Sogo Shoshas*
Pearson Correlation (*r*)	0.063	0.248
p-value	0.480	0.031**

** Significant at the 0.05 level (p<0.05), 2-tailed

In the case of the Korean GTCs, there is no statistical correlation between organisational formalisation and employees' speed of job handling. However, in the case of the Japanese *Sogo Shoshas*, the result reveals a statistical correlation between their employment of organisational formalisation and employees' speed of job handling (r = 0.248, $p<0.05$). Hence, Hypothesis 4.3 receives only partial support.

5.6.4. Types of Competitive Strategy

Separately, this study also investigated the competitive strategy which Korean GTCs and Japanese *Sogo Shoshas* are pursuing at this moment. The result is as follows:

(Table 5.27. Results of Frequency Analysis for Types of Strategy)

Types of Strategy	Korean GTCs	Japanese *Sogo Shoshas*
Differentiation	10	13
Cost Leadership	45	26
Hybrid (Differentiation + Cost Leadership)	42*	27***
Multi-mixed (Differentiation + Cost Leadership + Hybrid)	32**	11****
Total (N)	129	77

According to Porter's (1985) argument of competitive strategies, firms can be successful only if they adopt either a cost or a differentiation strategy. This denotes that they should choose only one of the two. If they mix them, they end up with low perceived value and high price (i.e. stuck in the middle). However, this survey gave a different result. The result shows that some Korean GTCs and Japanese *Sogo Shoshas* choose more than one strategy at the same time. Of 129 respondents in Korea, 74 (* + **) of them answered that they adopted more than one strategy at once. In the case of Japan, of 77 respondents, 38 (*** + ****) said that they chose more than one strategy at once. Meanwhile, a cost leadership strategy prevails in both groups, followed by hybrid and multi-mixed strategies.

5.7. Interview Results

The function of the interview survey, to allow cross checking, was vindicated by discovering that it obtained similar results to the questionnaire survey, as follows.

- **Hypotheses 1.1~1.2: Business Environment and Competitive Strategy**

i) Korean GTCs

Consistent with our arguments, all the Korean interviewees answered that a differentiation strategy and environmental uncertainty and complexity are positively correlated. Two interviewees, for example, replied as follows:

> *"If there is no differentiation, a company cannot overcome severe competition. It means that consumers will select the product which has attractiveness."*

> *"Basically, I agree that our company's differentiation strategy is positively associated with environmental uncertainty and complexity. I think every differentiation strategy is based on a different environmental uncertainty and complexity."*

With respect to the relationship between a cost leadership strategy and environmental uncertainty and complexity, two interviewees answered that a cost leadership strategy is not always inversely associated with uncertainty and complexity, for example, due to high competition in the market. They answered as follows:

> *"Due to high competition in the market, some of the cost leadership*

strategy that we take is positively associated with uncertainty and complexity, e.g. high volume and low margin."

"I don't agree that a company's cost leadership goes well with environmental uncertainty and complexity. As a General Trading Company, our company would face some obstacles to achieving cost leadership in our business areas."

ii) Japanese *Sogo Shoshas*

Like the Korean interviewees, the Japanese interviewees also felt that a differentiation strategy and environmental uncertainty and complexity are positively correlated. Two interviewees replied as follows:

"Yes. We have many competitors. We have to consider how we can show our functions to customers. So, we need a differentiation strategy when the environment is uncertain and complex."

"The current environment uncertainty and complexity governs market strongly and we also implement our differentiation strategy considering such environmental factors."

- **Hypotheses 2.1~2.2: Competitive Strategy and Organisational Structure**

i) Korean GTCs

All Korean interviewees agreed that their company's differentiation strategy is positively associated with organisational decentralisation, in particular in the decision-making process. Two interviewees replied as follows:

"Yes. In order to respond in time to rapidly changing market

conditions, we cannot always go to top management for a decision.”

“I agree that our company’s differentiation strategy is positively associated with decentralisation. There are many operational divisions/teams in our company. Every division/team should decide something from its own position.”

In the relationship between a cost leadership strategy and formalisation, all interviewees felt that their companies secure cost savings and an efficient work flow through formalisation. Two interviewees, for example, said,

“Yes. Many of our company’s cost leadership strategies have to take necessary procedures to get approval.”

“Through formalisation, a company can get cost savings and an efficient work flow.”

ii) Japanese *Sogo Shoshas*

One interviewee answered that differentiation strategy is positively associated with organisational decentralisation. He also expressed his opinion regarding the relationship between cost leadership strategy and formalisation:

“Yes. In our company, cost leadership strategy and formalisation are carried out at the same time. If our company’s situation gets worse, we try to cut costs and restructure our business portfolio.”

The other interviewee also had a view of positive correlation between differentiation strategy and decentralisation. Regarding cost leadership strategy and formalisation, he replied, *"My organisation is highly developed in terms of formalisation. ~~~~ It is also applied to implement cost leadership strategy."*

- **Hypotheses 3.1~3.3: Competitive Strategy and Performance**

i) Korean GTCs

All interviewees answered that a differentiation strategy is necessary for gaining market shares and new customers. Three interviewees said,

> *"Agree. In the case of one of our business fields where the business model is quite general, differentiation in customer service, like information providing, will gain market share, in particular in the initial stage."*

> *"We set up a differentiation strategy in order to improve our market share."*

> *"We make some non-profitable decision to approach new markets or customers." and,*

With regard to the relationship between a cost leadership strategy and profitability, three interviewees answered that a cost leadership strategy has no meaningful relationship with profitability, as the questionnaire survey did. But one interviewee expressed a different opinion:

> *"I think that our company's cost leadership strategy is positively associated with profitability."*

This was because the interviewee's company has experienced a radical organisational reconstruction since the collapse of its parent group in 1999. Thus, it assumes that a company may use a stable marketing policy by emphasising profitability rather than focusing on an aggressive marketing policy.

Like the differentiation strategy, adopting a hybrid strategy is also crucial for new market development and overall performance. Two interviewees, for example, replied as follows:

> *"Agree that our company's hybrid strategy is positively associated with new market development and overall performance. Especially in these days of severe struggle for existence, a hybrid strategy is essential for new market development."*

> *"It is important to mix two strategies, i.e. have a hybrid strategy, in order to develop a new market properly and at the same time, enhance overall performance."*

ii) Japanese *Sogo Shoshas*

Both two interviewees replied that their companies' differentiation strategy will be positively associated with gaining market share and new customers. Regarding the relationship between cost leadership and profitability, they said,

> *"In the short-time, I agree. But from the long-time perspective, I don't agree."*

> *"Sometimes we are implementing our cost leadership strategy, balancing the expected return at the proper level."*

With respect to the correlation between hybrid strategy and market development, they answered,

> *"Our company can't grow without a hybrid strategy. So, we choose a hybrid strategy to develop new market and make good."*

> *"It has to be considered by each case, but generally hybrid strategy is positively applied for overall performance."*

As we see from this result, most Korean GTCs and Japanese *Sogo Shoshas* mix two strategies (i.e. have a hybrid strategy) in order to develop new markets and enhance overall performance under fierce competition.

- **Hypotheses 4.1~4.3: Organisational Structure and Performance**

i) Korean GTCs

Two interviewees felt that organisational centralisation negatively influences overall performance, whereas another two interviewees felt the opposite. Two interviewees who believed in negative correlation between two variables, replied,

> *"Don't agree that our company's organisational centralisation will be inversely associated with overall performance. Frequently, centralisation makes for efficiency in overall performance."*

> *"Not always, depending on the product and market situation, centralisation is absolutely necessary to enhance work overall."*

With respect to the relationship between organisational decentralisation and employees' satisfaction and retention, all interviewees agreed that decentralisation enhances employees' motivation and, therefore, allowed the company to retain its employees. One interviewee said

> *"~~~Such a big proportion of decisions are endorsed at a lower level to solve each specific situation, in the nature of my company (i.e. a General Trading Company)."*

In the last interview question on strategic management, all the interviewees agreed that formalisation reduces the speed of job handling and response to customers.

ii) Japanese *Sogo Shoshas*

Regarding the relationship between organisational centralisation and a firm's performance, one interviewee said,

> *"Because our company has several business fields like chemical, metal, automobile, basically centralised control is impossible. So, in order to perform well, we need decentralisation. However, we set put company rules in advance and have to follow these rules under decentralisation."*

Regarding the relationship between formalisation and the speed of job handling, both two interviewees replied that two variables are inversely associated. One interviewee, for example, said,

> *"We are considering how to speed up decision- making."*

5.8. Conclusion and Discussion

This chapter investigated the strategic management of Korean GTCs and Japanese *Sogo Shoshas* by analysing the structural relationships between business environment, competitive strategy, organisational structure and performance. To examine this, both questionnaire and interview surveys were conducted. Although there were small differences between questionnaire survey results and interview survey results, they are within acceptability.

First, in the relationship between competitive strategies and business environments, this empirical study revealed that both Korean GTCs' and Japanese *Sogo Shoshas'* employment of a differentiation strategy is positively associated with environmental uncertainty and complexity, as many previous studies have found (Dess and Davis, 1984; Miller, 1988; Govindarajan, 1988; Kwon *et al*, 1999; Kang, 2002). With respect to the relationship between their cost leadership strategy and environmental uncertainty and complexity, it was found that they are inversely correlated each other, as predicted here. However, as in previous studies (Miller, 1988; Kwon *et al*, 1999; Kang, 2002), those relationships do not reach high statistical significance, although a regression model is significant. This result denotes that the choice of a differentiation strategy rather than a cost leadership strategy would increase uncertainty in an SBU's task environment, as Govindarajan argued (1986). The interview results also supported our predictions. All the respondents agreed that their firms' employment of a differentiation strategy has always had a positive correlation with uncertainty and complexity, but a cost leadership strategy is not always inversely associated with them.

Second, the relationship between competitive strategies and organisational structure was investigated. A differentiation strategy is positively associated with decentralisation in the work process. As Porter (1980) argued, the implementation of a new product or market development (i.e. a differentiation strategy) is highly dependent upon creative ideas from the members of the organisation. It also requires cooperation and close contact among them (Miller, 1988). Such assembling of creative ideas and close contact among members can be achieved by organisational decentralisation or a delegation of power to lower levels in the decision-making process. Moreover, consistent with our arguments, a cost leadership strategy is positively associated with formalisation, since a firm pursuing this strategy normally tends to focus on an internal issue of cost reduction and controls rather than the development of new markets. In the interviews, all respondents answered that they do not always go to top management for a decision in order to respond in time to rapidly changing market conditions. This denotes that when they pursue a differentiation strategy, the decision is not always made at a higher level, but is sometimes is made at a lower level according to the situation. In the relationship between a cost leadership strategy and formalisation, all respondents felt that their companies get the cost saving and efficiency of work flow through formalisation.

Third, an analysis was made between competitive strategies and a firm's performance. The result shows that Korean GTCs' and Japanese *Sogo Shoshas'* employment of a differentiation strategy is positively correlated with the gaining of market share and new customers. The functions of differentiation strategy are to secure new markets and customers by diversified products and services (Miles and Snow, 1978). In line with this argument, this study also gained the same result as previous studies. It also found that a hybrid strategy is statistically correlated with new market development since the main purpose of this strategy is to pursue high-quality products or services with lower prices than those of competitors. To support this result, Japanese car firms entering into European market can be cited as a good example. In order to develop markets in Europe, Japanese car firms from the late 1980s pursued a hybrid strategy by producing competitively priced cars which were more reliable and of better quality than their rivals. However, contrary to our hypothesis, a cost leadership strategy is not positively associated with a firm's profitability. Although the main purpose of a cost leadership strategy is to save cost, it is not always correlated with profitability, in particular in such highly diversified organisations as the Korean GTCs and Japanese *Sogo Shoshas*. The interviews here also revealed the same result. One respondent answered that a differentiation strategy in customer service, for example, information providing, would be very helpful for gaining market share at an early stage. In the case of a hybrid strategy, new market development is essential in the modern business environment as the market is so highly competitive. But most respondents felt that a cost leadership strategy has no meaningful relationship with profitability.

Fourth, it investigated the relationship between organisational structure and a firm's performance. In this analysis, some results from the Korean GTCs are different from those of the Japanese *Sogo Shoshas.* With respect to the relationship between centralisation and overall performance, the result shows that there is an inverse association between them in the Korean GTCs, but there is no statistical correlation in the Japanese *Sogo Shoshas*. According to previous literature, there were two views on this subject. The first was a negative or zero association between centralisation and performance (McMahon, 1976; Pennings, 1976; Dalton *et al*., 1980; Stathakopoulos, 1998; Johnson and Scholes, 2002; Olson, Slater and Hult, 2005) and the other was a positive association between them (Hage, 1965; Kim, 2000). The general understanding is that there is a negative or zero association between them. However, according to Hage (1965), organisational centralisation increases production and work efficiency since the centralised organisation tended to very quickly develop into a formalised procedure for passing messages. In the relationship between decentralisation and employees' satisfaction and retention, the result fully supports our hypothesis in both Korea and Japan. It is the general understanding that decentralisation can stimulate employees' motivation (Mintzberg, 1979) and the firm can thus attract and retain its staff. The last hypothesis examined the relationship between formalisation and the speed of job handling. The result reveals that formalisation is inversely associated with the speed of job handling in the Japanese *Sogo Shoshas*, but there is no correlation between them in the Korean GTCs. In the interviews, most respondents felt that centralisation had a negative influence on overall performance, but one respondent answered that centralisation often made work efficient in overall performance. Regarding decentralisation and employees' satisfaction and retention, all agreed that they are positively correlated with each other.

Fifth, it also examined what type of competitive strategy Korean GTCs and Japanese *Sogo Shoshas* are now pursuing as their main strategy. Against Porter's (1985) advice, they both adopt more than one strategy at once. According to Porter's original approach to competitive strategies, firms are successful only if they adopt either a cost or a differentiation strategy. Thus they should only choose one of the two, because mixing them results in low perceived value and high price (i.e. stuck in the middle). This is a third possible competitive strategy, but one which ultimately fails. He made the assumption that a better product costs more to produce, but that consumers will pay more in some market segments for what they perceive to be better. This is the basis of a differentiation strategy. In other markets or segments, consumers may be interested only in getting something at the lowest price, subject to some minimum quality. This is the basis of a cost strategy. This approach was later modified to take account of what was happening in some markets in Japan: through Total Quality Management and the Kaizen philosophy products were getting better and simultaneously coming down in price. This is the basis of the fourth competitive strategy: cost and differentiation strategy (i.e. hybrid strategy). A firm may choose only one of these four generic strategies.

However, this study found that Korean GTCs and Japanese *Sogo Shoshas* can in some cases adopt more than one strategy at a time from the four generic strategies. A similar result was found by Kang (2002) who researched the hotel industry in Korea. Some hotel firms in Korea chose more than one strategy at once. The result of this study implies that the business environment surrounding Korean GTCs and Japanese *Sogo Shoshas* is becoming more uncertain and complex and in consequence it seems that they mix two or more strategies to survive its rapid changes.

(Table 5.28. Questionnaire Survey Results Summarised for Korean GTCs' and Japanese *Sogo Shoshas'* Strategic Management)

Hypothesis	Analysis	Result
H.1.1: The GTCs'/*Sogo Shoshas'* employment of a differentiation strategy will be positively associated with environmental uncertainty and complexity.	Strategy/Environment (Differentiation / Uncertainty and Complexity)	Supported in both Korea and Japan
H.1.2: The GTCs'/*Sogo Shoshas'* employment of a cost leadership strategy will be inversely associated with environmental uncertainty and complexity.	Strategy/Environment (Cost leadership / Uncertainty and Complexity	Supported in both Korea and Japan
H.2.1: The GTCs'/*Sogo Shoshas'* employment of a differentiation strategy will be positively associated with the delegation of power (decentralisation).	Strategy/Structure (Differentiation / Decentralisation)	Mostly supported But no correlation in future for Japan *Sogo Shoshas*
H. 2.2: The GTCs'/*Sogo Shoshas'* employment of a cost leadership strategy will be positively associated with formalisation.	Strategy/Structure (Cost leadership / Formalisation)	Supported in both Korea and Japan
H.3.1: The GTCs'/*Sogo Shoshas'* employment of a differentiation strategy will be positively associated with the gaining of market shares and new customers.	Strategy/Performance (Differentiation/Market shares and New customers)	Mostly supported But no correlation in future for Japan *Sogo Shoshas*
H.3.2: The GTCs'/*Sogo Shoshas'* employment of a cost leadership strategy will be positively associated with profitability	Strategy/Performance (Cost leadership / Profitability)	Not Supported in both Korea and Japan
H.3.3: The GTCs'/*Sogo Shoshas'* employment of a hybrid strategy will be positively associated with new market development.	Strategy/Performance (Hybrid/New market development)	Mostly supported But no correlation in future for Korea GTCs
H.4.1: The GTCs'/*Sogo Shoshas'* organisational centralisation will be inversely associated with overall performance.	Structure/Performance (Centralisation/Overall Performance)	● K: Supported ● J:Not supported
H.4.2: The GTCs'/*Sogo Shoshas'* organisational decentralisation will be positively associated with employee satisfaction and retention.	Structure/Performance (Decentralisation / Employee's satisfaction and retention)	Supported in both Korea and Japan
H.4.3: The GTCs'/*Sogo Shoshas'* organisational formalisation will be inversely associated with the speed of job handling.	Structure/Performance (Formalisation/Speed of job handling)	● K:Not supported ● J: Supported

5.9. Difference Analysis between the Two Countries

According to the results, most of the hypotheses are accepted or some of them received partial support. Almost same results were obtained from Korea and Japan. But two hypotheses (H.4.1. and H. 4.3.) show results for Korean GTCs which are different for Japanese *Sogo Shoshas*. Although there were small differences in H.2.1, H.3.1 and H.3.3 between two countries, they were acceptable and understandable without further discussion. Thus, this section discusses why differences in H. 4.1 and H.4.3 should arise between the one country and the other.

- **Hypothesis 4.1.: Centralisation/Overall Performance**

As summarised in Table 5.28, people in Korean GTCs feel that organisational centralisation is inversely associated with a firm's overall performance, whilst Japanese people think there is no statistical correlation between them.

First, the corporate culture and decision-making culture may affect the different results. The typical Japanese firm's decision-making culture is consensus-style decision-making which allows all the people to take part in the entire process of defining, solving and acting upon a problem. Thus, people in Japanese firms may feel that organisational centralisation is not closely associated with a firm's overall performance because most decisions are made on the basis of opinions and information emanating from each of the responsible parties. However, in Korea's case, most decision-making power is concentrated in the higher levels. Due to such a hierarchical system, top executives in *Chaebols* sometimes made poor decisions which led their companies to the brink of bankruptcy. Ultimately, their short-sighted decisions were among the factors in the national's financial crisis, as well leading to the government's decision to restructure the organisation of the *Chaebols*. Consequently, people in Korean GTCs may feel that organisational centralisation has a negative influence on a firm's overall performance.

Second, the external environment may have played a part in the different results for the two countries. Both Korean and Japanese firms experienced rigorous economic conditions in the 1990s, following the financial crisis (Korea) and the collapse of the bubble economy (Japan). For this reason, many big business groups in Korea and Japan slimmed down their structure as part of their organisational restructuring. Although the firms in these countries restructured their organisational system, the extent of change in Japanese firms was much less than in the Korean firms. In Korea's case, the government led the *Chaebols'* organisational restructuring under the special programme named "Work-out ", a very strict regulatory programme determining whether the *Chaebols'* should continue in the market or be abolished. As a result, overall management system of most Korean big business groups was significantly changed by rationalising their decision-making process, decentralising their organisational structure and so on. Thus, employees in Korean GTCs feel that organisational centralisation may affect a firm's overall performance inversely, whilst Japanese people feel that there is no statistical correlation between them.

Third, the size of organisational structure may also have an effect. The organisational structure of Korean GTCs is much smaller than that of the Japanese *Sogo Shoshas*. The results of the result indicate that a smaller organisational structure can adapt quickly to a new business environment in changing business situations. People in both Korean GTCs and Japanese *Sogo Shoshas* may feel the need to decentralise these days, in the interests of greater effectiveness, because they have experienced such drastic environmental changes since the late 1990s. However, although middle-level or lower-level managers in Japanese firms feel that decentralisation is a highly appropriate system at present and one which may benefit a firm's performance, they may find it psychologically beyond them to oppose the weight of the traditional huge organisational structure. Thus, it is possible that people in Japanese *Sogo Shoshas* may feel subjectively that organisational centralisation would not correlate significantly with a firm's overall performance.

- **Hypothesis 4.3.: Formalisation/Speed of Job Handling**

According to the survey result, respondents in Korean GTCs also feel that organisational formalisation is not associated with the speed of job handling, whilst Japanese employees answer that there is an inverse correlation between these two.

First, the corporate culture is one of the main factors to show a different result. According to Cho and Yoon (2001), there have been controversies over the corporate culture of Korean firms. Some Western scholars, such as Hofstede (1991) and Trompenaars (1994), argued that Korea was one of the most collectivist countries in the world and its corporate culture is even more collectivist than that of Japan. But Japanese scholars such as Hasegawa, Watanabe and Kusayanagi take a different view (Chang and Chang, 1994) and declare that Korean companies are more competitive, individualistic and dynamic than Japanese ones. Although Korean corporate culture has been built on traditional collectivism, many Korean scholars disagree about its specific nature. For instance, young managers (e.g. the new generation) in Korean firms often egoistic and instrumental forms of behaviour to deal with their tasks. This argument was supported by Chung, Lee and Jung (1997). They argued that most Korean employees' loyalty and life-time commitment to the company are not as strong now as they were in the past. While most employees respect group opinions, they now want the chance to express their own views. For this reason, these employees nowadays tend to disregard formal procedures in their work process. This, then, affects their response that formalisation has no significant correlation with the speed of job handling.

Second, the different national culture may affect the different results from Korean GTCs and Japanese *Sogo Shoshas*. Because Korea and Japan are located in the same cultural region, there are some cultural similarities between them, such as collectivism, the seniority system and Confucianism. At the same time, there are obvious cultural differences. For instance, one of the features of Korean national culture is the "Be quick" spirit, which is reflected not only in people's personal lives, but also in all the working processes of a company. Thus, most decisions and approvals in all Korean firms tend to be made very quickly. In comparison with Korea, Japanese national culture is very prudent, in particular in business. In Japan, any decisions, changes or modifications occur slowly and carefully, involving in the entire process of decision-making all those who will be affected. In addition, an informal decision-making stage is generally necessary. In summary, employees in Korean GTCs may have a tendency to neglect strict formalisation, although most Korean firms put emphasis on basic principles and all instructions are prepared through formal documentation. Thus, they feel that formalisation is not closely associated with the speed of job handling. However, in Japan’s case, although employees feel the need for informal processes in their work these days, they may find it psychological burdensome to think of opposing a traditionally established formalisation system. Thus, they may feel formalisation is inversely associated with the speed of job handling.

CHAPTER 6. THE DECISION-MAKING PROCESS WITHIN THE GTCs/*SOGO SHOSHAS*

6.1. Introduction

Strategic management encompasses the strategic decision-making within any organisation. In the process of implementing strategic management, a firm may rely heavily for its success on its decision-making processes. Although a firm has a specific type of strategy, a competitive organisational structure and an amicable business environment, its irrational and incoherent decision-making may impede the accomplishing of its managerial goals. Therefore, a firm's successful implementation of strategic management is intimately associated with its decision-making.

The previous chapter investigated the strategic management of Korean GTCs and Japanese *Sogo Shoshas* with theoretical constructs of their environment, strategy, structure and performance. By extending the work of the previous chapter, this chapter examines in particular the decision-making process within the two groups with new constructs, questions and hypotheses. As mentioned, although a decision-making process is a part of strategic management, it is worth carrying out an in-depth investigation and comparison of the two groups' decision-making processes themselves as a separate task. There are two reasons for this; i) both Korea and Japan have unique decision-making cultures which are quite different from those of Western countries and ii) there are cultural differences between Korea and Japan in the decision-making process, even though two countries are in the same geographical region.

This chapter will seek to identify i) who are the main decision-makers within the GTCs/*Sogo Shoshas*, ii) what factors influence the decision-making process, iii) whether there are corporate cultural differences in the decision-making process between the two groups and iv) whether any recent changes have been made in the decision-making process within the two groups.

The organisation of this chapter can be briefly summarised as follows. First, it describes the relationship between strategic management and strategic decision-making and the way in which they are interlinked with each other. Second, it reviews overall theories of organisational decision-making, such as the types, models and steps of decision-making. Third, it examines the major factors in organisational decision-making: power and politics, corporate culture, ownership and corporate governance. Fourth, it reviews some empirical studies relating to the decision-making process within Korean and Japanese firms. Finally, it addresses the research objectives and questions and derives some hypotheses.

6.2. Strategic Management as Strategic Decision-Making

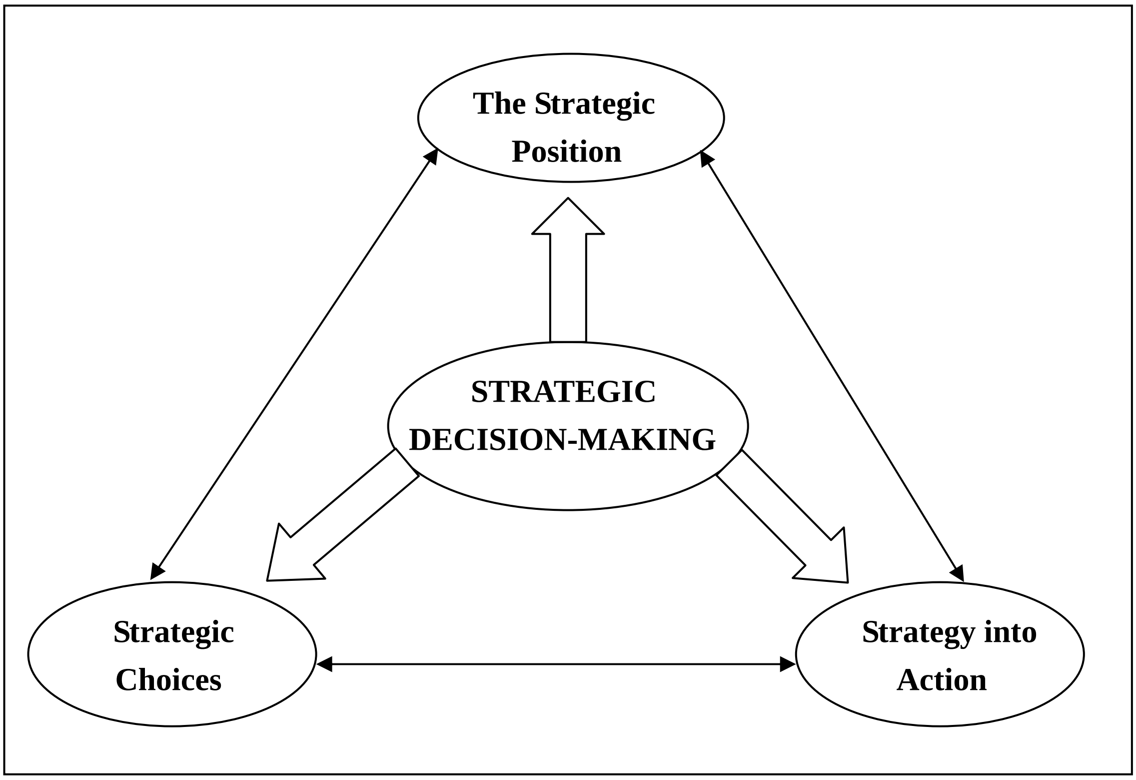
Decision-making is a fundamental activity of strategic management among managers. Managers all over the world must make decisions which significantly affect their organisations (Martinsons and Davison, 2007). Successful strategy emerges from effective decision-making process in which executives develop collective intuition, accelerate constructive conflict, maintain decision pacing and avoid politics (Eisenhardt, 1999). However, today’s rapidly changing business environment complicates decision-making. Nevertheless, managers need to make effective decisions through consultation processes and choices as part of their firms' strategic management.

The distinguishing characteristic of strategic management is its emphasis on strategic decision-making. Strategic decision-making refers to non-programmed decisions typically made by high-level executives regarding the direction which their organisation should take to achieve its mission (Greenberg and Baron, 2008). As organisations grow larger and more complex in more uncertain situations, decisions become increasingly complicated and difficult to make (Wheelen and Hunger, 2007). Strategic decision-making necessitates an integrated understanding of the company's marketing, finance, human resources, R & D and manufacturing functions. These functional areas interact over time and are essential for the successful implementation of a firm's strategic management in the longer term.

Regarding the Korean GTCs, irrational decision-making was one of the major reasons for the failure of their strategic management. Furthermore, the *Chaebol* groups' easy decisions contributed to Korea's economic crisis in 1997; they were not based on the real market situation but instead on company owners' personal preferences or feelings. As decision-making power is concentrated in the top management in most Korean firms, including the GTCs, Korean subordinates are usually reluctant to express their opinions (Chen, 2004). Kahal (2005) argued that in most Korean organisations decision-making, financial decision-making in particular, is centralised and tightly controlled by top executives. As for the *Sogo Shoshas*, they usually use the consensus decision-making style in strategic management. However, this has some drawbacks when it comes to effective strategic management. For instance, as Kahal (2005) argued, consensus decision-making system is a weakness because Japanese people believe that there is always one right answer to a question and that authority should not be challenged. Chen (2004) stressed that the system is too slow and involves many unnecessary meetings.

The strategic management and strategic decision-making within an organisation is never separated. The following figure illustrates the relationship between strategic management and the strategic decision-making process and how they are correlated. In the figure, strategic decision-making is central to the strategic management process and affects all strategic management activities, such as environment scanning, strategic choice and strategic action.

(Figure 6.1. Strategic Management as Strategic Decision-making)



(Source: Developed by the author from Johnson, Scholes and Whittington (2005), "Exploring Corporate Strategy", 7th edition, Prentice Hall, p. 16).

More specifically, in the stage of the strategic position, decision-makers need to consider how the environment will affect the organisation and its future activities and what are the resources and core competence which may create competitive advantages and new opportunities. This process diagnoses an organisations's external and internal environment, deciding on a vision and mission, developing overall goals and allocating human and capital resources to attain the managerial goals. In the strategic choices stage, managers need to make decisions with respect to a firm's overall direction in terms of its general policy toward growth and the management of its diverse businesses and product lines (i.e. Corporate-level strategy). Decision-makers also consider how their company can improve its competitive position in the specific industry or market segment by competitive strategies (i.e. Business-level strategy). In the strategy into action process, managers are required to make effective decisions of ways to execute a strategic plan.

Taken altogether, strategic management and the strategic decision-making process are not separated, but interact with each other in order to accomplish a firm's goals. This relationship between the two elements could be called 'strategic management as strategic decision-making'.

6.3. Theoretical Background and Literature Review

6.3.1. Types of Decision-making

Many researchers (Barnard, 1968; Daft, 2000; George and Jones, 2008; Greenberg and Baron, 2008) classify different types of decision-making. There are in general three types of decision-making: i) programmed vs. non-programmed decision-making, in accordance with established plans, procedures and systems or the lack thereof, ii) personal vs. organisational decision-making, in accordance with the main body of decision-making and iii) decision-making in conditions of certainty, risk, uncertainty and ambiguity created by current circumstances.

- **Non-programmed vs. Programmed Decision-making**

To the extent that decisions are repetitive, routine or made in accordance with an established procedure, they can be described as programmed. Decisions are non-programmed to the extent that they are novel, unstructured and consequential. George and Jones (2008) established that non-programmed decision-making involves searching for the extra information needed to make the right choice. Greenberg and Baron (2008) defined non-programmed decision-making as decisions made about a highly novel problem for which there is no pre-specified course of action. Thus, the decision-maker confronts a unique situation in which the solutions are novel. However, programmed decisions are highly routine decisions made according to pre-established organisational routines and procedures (Greenberg and Baron, 2008). To make a programmed decision, the decision-maker uses a standard sequence of behaviours followed routinely by organisational members whenever they encounter a particular type of problem or opportunity (George and Jones, 2008).

- **Personal vs. Organisational Decision-making**

According to Barnard (1968), personal decisions cannot ordinarily be delegated to others, whereas organisational decisions can often if not always be delegated. In other words, personal decisions are made by an individual within the organisation in order for him/her to achieve a personal purpose, whereas organisational decisions are made in order to achieve an organisational purpose. However, it is quite difficult to distinguish clearly between these two. For instance, if a personal decision contributes to or has the intention of cooperation in order to achieve an organisational purpose, this personal decision is regarded as relating to an organisational decision. In some cases, the purposes are compatible with each other and converge. More often than not, they are incompatible.

- **Decision-making under Certainty, Risk, Uncertainty and Ambiguity**

Daft (2000) classified four types of decision-making: those made in conditions of certainty, risk, uncertainty and ambiguity. Certainty means that all the information needed by the decision-maker is fully available. Risk means that a decision has clear-cut goals and that good information is available, but that the future outcomes associated with each alternative are subject to change. With decision-making in uncertainty, managers know what goals they wish to achieve, but information about alternatives and future events is incomplete. In this case, the manager may have to come up with a creative approach to alternatives and use personal judgment to determine which alternative is best. Ambiguity is by far the most difficult decision situation. In this case, the goals to be achieved or the problem to be solved is unclear, alternatives are difficult to define and information about outcomes is unavailable.

All organisational decisions involve some degree of risk, ranging from complete certainty (no risk) to complete uncertainty (high risk). Thus, one of the managers' important tasks is to try to reduce decision uncertainty. In this context, Greenberg and Baron (2008) argued that decision uncertainty can be reduced by establishing linkages with other organisations. The more an organisation knows about what another organisation will do, the greater certainty it will have in making decisions.

6.3.2. The Models of Organisational Decision-making

- **Rational or Classical Model**

The rational model is an ideal pattern of decision-making; it is applicable to programmed decisions in which the goal and problem are well defined and information on alternatives is perfect. Simon (1976) defined the concept of rationality as one which is concerned with the selection of preferred behaviour alternatives in terms of some system of values whereby the consequences of the behaviour can be evaluated. Rationality is commonly associated with notions of logic, reasoning and sense-making (Stewart, 1994). This model assumes that decisions maximise goal achievement and that people strive to be economically rational. According to Daft (2000), the assumptions underlying this model are that: i) the decision-maker is rational and uses logic to make a decision which will maximise the attainment of organisational goals, ii) the criteria for evaluating alternatives are known and iii) the decision-maker strives for conditions of certainty, gathering complete information.

However, there are in organisations a number of obstacles and limitations to making the best rational decisions. Managers seldom achieve complete rationality in managing. George and Jones (2008) stressed that the classical model is unrealistic. Its assumptions that decision-makers have all the information needed to make optimal decisions bears little resemblance to the conditions facing most organisations. Further, although the decision-makers have all necessary information, they are not often able to use it all.

- **Bounded Rationality or Administrative Model**

As mentioned earlier, organisations present many obstacles and limitations to making the best rational decisions. It is in general unrealistic to expect managers to behave with a high degree of rationality in the organisational decision-making process. This is because many factors – limited information, time, certainty and limits on human intellectual capacities and on the availability of information – prevent such behaviour, even though managers try to be completely rational.

Simon (1958, 1976 and 1979) pioneered the effort to understand how real decision situations are handled by individuals and organisations and in what ways such processes differ from the rational comprehensive model. Simon and March (1958) introduced the concept of bounded rationality – the concept that people have the time and cognitive ability to process only a limited amount of information on which to base decisions – to explain how managers realistically cope with baffling complexity. According to Simon (1979), rationality is bounded when it falls short of omniscience. And the failures of omniscience are largely failures of knowing all the options, uncertainty about relevant exogenous events and the inability to calculate consequences. He further emphasised that managers settle for a satisfactory rather than an optimal solution. Decision-makers have a set of criteria which describes minimally satisfactory alternatives and can recognise alternatives in questions which meet these criteria: this decision mechanism is called s*atisficing*. A satisficing decision is much easier to make than an optimal decision. However, in most decision-making situations, satisficing decisions are acceptable and are more likely to be made than optimal ones (Greenberg and Baron, 2008).

According to this model, decision-makers choose how to respond to opportunities and problems on the basis of a simplified and approximate account of the situation. They do not take into account all the information relevant to a problem or opportunity, nor do they consider all possible alternatives and their consequences (George and Jones, 2008).

- **Political Model**

Challenging the conventional rational model's unitary view of organisations as consisting of well-structured, differentiated subsystems linked through a common goal, the political model regards organisations as pluralistic and divided into various subunits, each wedded to its own goals, interests and subcultures (Varman and Bhatnagar, 1999). The political model is useful for making non-programmed decisions when conditions are uncertain, information is limited and there is disagreement and conflict between multiple actors about what goals to pursue or what course of action to take. This model starts with an assumption that power arises inevitably and is a crucial variable in achieving organisational goals; managers engage in the push and pull of debate to decide goals and discuss alternatives. Viewing an organisational decision-making process from a political perspective started with Cyert and March (1963). According to them, the process of decision-making in organisations is a power game for multiple actors who all want to further their interests. Rex (1961) also argued that if there is an actual conflict of ends, the behaviour of actors towards one another may not be determined by shared norms, but by the success each has in compelling the other to act in accordance with his interest. Power then becomes a crucial variable in the social systems. Etzioni (1967) noted that decisions reflect the interests of the most powerful, since partisans invariably differ in their respective power positions.

Martin and Sims (1983) went further, presenting major elements – alliances, taking counsel, communication and compromising[72] as power tactics in order to reach an organisational agreement among multiple actors. This concept is also described by Jones (1988) and Daft (2000), who emphasise coalition, defined as informal alliances among managers supporting a specific goal[73]. Unlike the rational model, the political model recognises that the preferences and values of managers differ and that conflict between managers and different stakeholder groups is inevitable. Without a coalition, a powerful individual or group could derail the decision-making process.

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[72] Martin and Sims argued that every executive needs closer alliances with other executives, both on his own level and above him, if he is to protect and to enhance his status and to reach an organisational agreement. The executive also needs counsel, but he should be cautious about how he seeks and receives advice. He should take counsel only when he himself desires it, because it is often interpreted as a delegation of power if an executive allows his subordinates to provide advice when he does not specifically call for it. A manager also needs well-dredged communication channels and should accept compromise.

[73] According to Jones (1988), the political model views an organisation as a coalition of different interests, in which decision-making takes place through compromise, bargaining and negotiation between managers from different functions and areas of the organisation. Any solution chosen meets the approval of the dominant coalition, the collection of managers or stakeholders who have the power to select a solution and commit resources for implementing it. Daft (2000) argued that most organisational decisions involve many managers who are pursuing different goals and have to talk with one another to share information and reach an agreement. Under this situation, managers often engage in coalition building for making complex organisational decisions. Coalition building is the process of forming alliances among managers. In other words, a manager who supports a specific alternative talks informally to other executives and tries to persuade them to support the decision. When the outcomes are not predictable, managers gain support through discussion, negotiation and bargaining. Coalition building gives several managers an opportunity to contribute to decision-making, enhancing their commitment to the option which is ultimately adopted.

The characteristics of each of the three major organisational decision-making models, as reviewed above, can be summarised as follows:

(Table 6.1. Comparison of Decision-making Models)

	Rational Model	Bounded Rationality Model	Political Model
Actors	Single or multiple	Single or multiple	Multiple
Goals	Clear-cut and shared	Vague and shared	Conflicting and incompatible
Information	Perfect and full	Imperfect and limited	Ambiguous and imperfect
Decision Behaviour	Problem-solving and making rational choices for maximising outcomes	Constrained problem-solving	Negotiation, bargaining and struggling
Mechanism of the Choice	Maximising	Satisficing	Domination

6.3.3. Factors Affecting Decision-making

- **Power and Politics**

In organisational behaviour theory, it is generally accepted that any decision-making process influenced by power and politics is non-ethical, but should be made on the basis of acceptable boundaries of rationality. However, to speak realistically, power significantly affects organisational behaviour in ways which, though not visible, can change or shift organisational decisions. Since Russell (1938) asserted that "the fundamental concept in social science is power, in the same sense in which energy is the fundamental concept in physics", the concept of power has for decades stimulated intense debate. Simon and March (1958) claimed that politics is one of the organisational reactions to conflicting objectives. When there is inter-group disagreement on goals and bargaining is not used, inter-group conflict is resolved through politics. This mechanism of decision-making has some potentially disruptive consequences. It almost necessarily places strain on the status and power system of the organisation. If those who are formally the most powerful prevail, the result is a more forceful perception of status and power differences in the organisation.

Pfeffer (1992), who placed power at the centre of the organisational decision-making theory stressed that it is essential to understand the decision-making process from a power and politics perspective, since it is hardly possible to reach an organisational decision on the basis of rationality in the real business world. He defined organisational politics as activities which attempt to influence decisions about critical issues. He viewed organisations as pluralistic and divided into various interests, subunits and subcultures. He further emphasised an inseparable relation between power and politics: the organisational politics is the exercise or use of power and power is defined as a potential force.

When discussing power and politics in organisational decision-making, one of the important things to remember is identifying the source of power. Pfeffer (1992) pointed out that an individual's power within an organisation comes from the subunit of which he or she is a member. In other words, the location in the organisational structure is one of the sources of power[74]. Not all subunits are created equal – some are more influential than others. The power of a subunit comes from its ability to act in a unified, consistent

[74] Besides the location within the organisational structure, Pfeffer presented other sources of an individual's power: i) energy, endurance and physical stamina, ii) the ability to focus one's energy and to avoid wasted effort, iii) sensitivity, which makes it possible to read and understand others, iv) flexibility, particularly with respect to selecting various means in order to achieve one's goal, v) the willingness to engage in conflict and confrontation, or, in other words, a certain degree of personal toughness, vi) the ability to submerge one's ego, at least temporarily and play the good subordinate or team player to enlist the help and the support of others.

fashion, from its proximity to critical issues and its ability to cope with those issues and from achieving a position of monopoly by means of its expertise and problem-solving ability. Varman and Bhatnagar (1999) identified seven sources of power: formal authority, rules and regulations, control of scarce resources, ability to cope with uncertainty, knowledge and information, counter-organisations and informal organisations[75]. Cohen and Bradford (2002) stressed that power comes from both position and personal skills – what people know and are able to do. Expertise has always been a source of power, but it will become even more important – and easier to recognise – in organisations where power is widely dispersed. Reputation, which derives from one's character, abilities, collaboration and performance on the job, along with the ability to learn, becomes ever more important. When important tasks are on the line, people will want to work with others who can deliver. Power will accrue to those who deliver the desired results.

- **Corporate Culture**

An important influence on organisational behaviour is culture. Although people may not be consciously aware of culture, it has a pervasive influence over their behaviour and actions within the organisation (Mullins, 1996). Corporate culture, which is defined as the collection of beliefs, expectations and values learned and shared by a

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[75] Detailed explanations of these sources of power are as follows. i) Rules and regulations: they are often created, invoked and used in either a proactive or retrospective fashion as part of a power play. ii) Control of scarce resources: those subunits or individuals within the organisation which can provide the most critical and difficult to obtain resources, come to have power in the organisation. iii) Ability to cope with uncertainty: a player's power ultimately depends on the control he has over a source of uncertainty that affects the pursuit of the organisation's aims and on the importance of this source as compared with other relevant sources. iv) Knowledge and information: these can help a person to systematically influence the definition of organisational situations and create patterns of dependency. v) Counter-organisation: whenever a group of people manages to build a concentration of power in relatively few hands, it is not uncommon for opposing forces to co-ordinate their actions to create a rival power block. For instance, unions develop as a check on management in industries. vi) Informal organisations: friends in high places, sponsors, mentors, coalitions, or people to trade support and favours to further their individual ends and informal networks – all provide a source of power to those involved.

corporation's members and transmitted from one generation of employees to the next fulfils several important functions in an organisation and is one of the main factors affecting corporate decision-making. According to Slater (2003), corporate culture may, if appropriate, convey a sense of identity and belonging, generate employee commitment, add to organisational stability and serve as a frame of reference for decision-making. However, it may, if inappropriate, also give rise to alienation, demotivate employees, destabilise an organisation, frustrate communication and delegation and generate resistance to change.

How much does corporate culture influence organisational decision-making? In his book, *Cultures and Organisations*, Hofstede (1991) stressed that organising always demands the answering of the question: who has the power to decide what? The answer to this is influenced by cultural norms of "*power distance*"[76]. The decision-making process is different in different cultures. Who makes a decision, when it is made and the importance placed on rationality vary in organisations around the world. For example, in high power-distance cultures, such as India, only very senior level managers make decisions. But in low power-distance cultures, such as Sweden, low-ranking employees expect to make most of their own decisions about day-to-day operations. Moreover, because Italians value the past and traditions, managers in that culture will tend to rely on tried-and proven alternatives to problems. In contrast, the US and Australia are more aggressive and now-oriented; managers in these countries are more likely to propose unique and creative solutions to their problems (Robbins, 1991).

[76] Hofstede defined the term Power Distance as "the extent to which the less powerful members of institutions and organisations within a country expect and accept that power is distributed unequally. Institutions are the basic elements of society like the family, school and the community; organisations are the places where people work".

According to Pheysey (1993), there are major cultural differences between West and East. The West has tended to think, for example, that a cause precedes an effect and that things happen one after another. The West tends to perceive things in categories, is oriented towards mastery over nature and bases reality or ultimate truth on science and pragmatism. However, the East tends to perceive things in contexts, seeks harmony with nature and sees reality as more based on revealed truth than on empirical experimentation. Moreover, corporate leaders in the East, in particular in Korea, tend to depend on their intuition when they make decisions.

Korean firms' decision culture is quite different from those in other Western countries. The failure of the Samsung Motor Company offers a good example of a poor decision based on the owner's intuition[77]. The owner of Samsung, Kun Hee, Lee who had an individual taste for collecting luxury cars, had an undue influence on the car industry. His interest in the car industry was one of the main triggers in his decision to invest in a luxury passenger car project and he reached the decision – when the luxury passenger car market was already overstocked – on the basis mainly of his intuition and whim, rather than on any real need for or competence in such automobiles. This same kind of poor decision-making by corporate leaders frequently occurs within the Korean GTCs, as well. For instance, when each SBU within the GTC establishes an integrated international marketing strategy, such as the selection of a target market, choice of market entry mode and of logistics and transportation partners, the decision-making

[77] There is an interesting unrevealed story behind the Samsung Car Project. During the period of the project feasibility study, the owner of Samsung, Kun Hee, Lee, fired many executive members who had opposed the project as unfeasible. These members were held to have betrayed the owner's final decision. Yet when the project failed, Lee again fired most of the executive members who had agreed to the project and made no objection. These were also condemned as traitors who had forced the company to take risks without any managerial foresight.

process tends to rely on a SBU leader's propensity without accepting opinions of all the members involved.

In contrast, the typical Japanese corporate culture in decision-making is collective. Input from the bottom line of the organisational hierarchy is the starting point and this system ensures everyone's commitment and involvement at all levels. The Japanese attach greater importance to implementation, unlike Westerners who give priority to the speed of reaching a decision. The time needed to reach a decision is increased in proportion to the number of people who have to be persuaded.

- **Ownership and Corporate Governance**

The other important factors influencing a firm's decision-making and overall management are ownership, control, or corporate governance. A study by Pitelis and Sugden (1986) relating to the relationship between ownership and control within a firm defined control as "the ability to determine broad corporate objectives despite resistance from others." The percentage shares required for control varies among firms because each firm has specifically placed interconnections between the principal shareholders, employees, directors and other firms (Lee, 1999). Pitelis and Sugden (1986) argued that the percentage of shareholding for control does not require ownership of 51% of the shares. According to them, only 20% of shares is necessary to maintain control, while Cubbin and Leech (1983) argued that well under ten percent, or even 1~2% may be sufficient to retain control.

In this context, Korean big business groups are a good example. Ownership and management are not separated in most Korean business groups and group owners have power much in excess of their shares. As Lemmon and Lins (2002) argued, this structure may cause lower performance when a firm is faces crisis.[78]

6.4. Decision-making Process within Korean and Japanese Firms

6.4.1. Decision-making Process within Korean Firms

The influence of hierarchical traditional family systems in Korea impacts on management behaviours, such as business strategies, organisational structure, decision-making and HRM (Rowley and Bae, 2003). In most Korean firms, decision-making power and authority are concentrated in the higher echelons of managerial hierarchies. However, there is no visible resistance to this decision-making system, because of the Confucian ethical system, which entails paternalism, loyalty and respect for elders and seniors (Chung, Lee and Jung, 1997). Decision-making, in particular, financial decision-making, is centralised and tightly controlled by top executives in most Korean organisations (Kahal, 2005). However, there is the process of establishing informal consensus (in Korean term *sajeonhyupui*) which is similar to the Japanese n*emawashi* (prior consultation), even though Korean subordinates are usually reluctant to express their opinion (Chen, 2004).

In order to get approval from top management, all business issues should be reported in a specific written form in accordance with the strict formal procedure of *Kyuljae* (a strict formal procedure of decision-making) system, which requires much

[78] Lemmon and Lins (2002) argued that when firms' controlling managers or insiders have more power than their ownership rights would justify, the performance of these firms is lower than that of other firms during the crisis period.

time until the final approval. In Korean terms, *Kyuljae*, means formal processing to get approval from those higher up in the firm. The major reason for following this is the unique culture of Korean organisations' decision-making; top-down and centralisation to upper-level management. However, Chung, Lee and Jung (1997) stressed that the formal approval process could provide a mechanism for discussion and consultation among employees and various levels of managers throughout the organisational hierarchy, but it has not been used as such. *Kyuljae* is similar to the *ringi* system in Japanese firms, but the former is considered to be more of a means for exercising authority and control than for requesting consultation and participation which characterise the latter.

- **A Strict Formal Procedure of Decision-making *(Kyuljae)***

No decision is made, even for minor issues, in Korean firms without passing through a strict formal procedure called *Kyuljae*. In Korean terms, *Kyuljae*, means the formal processing to get the approval of those higher up. The major reason for following this system in all Korean firms is the unique culture of decision-making in Korean organisations (i.e. top-down and centralisation to upper-level management). However, Chung, Lee and Jung (1997) argued that a formal approval process could provide a mechanism for discussion and consultation among employees and various levels of managers throughout the organisational hierarchy, although it has not been used in this way. *Kyuljae* is similar to the *ringi* system in Japanese firms, but the former is considered to be more of a means for exercising authority and control than the asking for consultation and participation which characterise the latter.

In accordance with the *Kyuljae* system, five persons are normally involved in any business matter until the final decision is made. The first step in *Kyuljae* is the drafting of report by someone in charge. Once the draft is prepared in a specific written by a person in charge (staff normally has five years of working experience), it is handed over to middle-level management (managers normally have more than ten years of working experience) which plays the most important role during the whole process of the *Kyuljae*. At this stage, the middle-level manager checks the entire draft with scrupulous care from typographical errors to the content of the draft, which help the report to be written accurately. If any inadequacy is found, the middle-level manager sends the draft back to the person in charge for him to revise. Once the draft is approved by the middle-level manager, it is handed over to upper-level management, including the vice president, president and chairman and can be effortlessly approved by them, not rejected[79].

However, the situation is different in the case of reporting major business issues. In this case, the middle-level manager does not have much authority and upper-level management decides most issues. Furthermore, there is a unique institutional device in the *Kyuljae* system for obtaining consensus (the Korean term is *Hapuye*) from various levels of managers and business departments who are not directly connected with the issues reported. In this case, the final decision is made after a normal review by ten or more persons who are directly or indirectly associated. For instance, if a marketing department reports on the annual sales prospects in the EU market, it may need the agreement of some indirectly associated departments, such as strategic planning, legal, insurance and logistics and factory departments as well.

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[79] From the author's 9-year working experience at one of the biggest business groups in Korea, the author is very familiar with the decision-making process within Korean organisations.

- **A Regulation of Mandated Arbitrary Decision**

One of the notable problems of decision-making through *Kyuljae* in Korean firms is the loss of efficiency caused by the strict formal procedure of securing the approval of upper levels of management. Although the general decision-making procedure in Korean firms is quicker nowadays and most firms recognise the need to increase decision-making efficiency, it still takes a significant amount of time for the final approval from the top management to emerge. In some cases, it needs a month or more, even for small issues, to get final approval if a final decision-maker is absent. In order to improve the efficiency of the decision-making process, an institutional device can be used. A typical example is the "Regulation of Mandated Arbitrary Decisions." The purpose of this regulation is to promote work efficiency, increase the speed of work processes and establish a climate of responsibility-management by stipulating the matter to be arbitrated on in each position. According to this regulation, each matter of arbitration should be carried out in accordance with a standard table – a table stipulating details of the range of duties and the person in charge of arbitration.

(Table 6.2. A Sample of the Standard Table of Duty of Arbitrary Decision within Korean Firm)

Job Specification	Duty of Arbitrary Decision	Person of Arbitrary Decision				BOD**
		Mgr. *	Team Leader	Vice President	President/ Chairman	
Strategic Planning	1.Establishment of short medium and long-term strategies					
	1) Medium and long term strategies				O	
	2) Set up management philosophy				O	
	3) Set up long-term vision				O	
	2. New investment and expansion					
	1) Set up short, medium and long-term plans					O
	2) Detailed investment planning				O	
	3) Finance planning				O	
	3. Capital (Stock) Management					
	1) Shareholder and stock price management			O		
	2) Stock option					O
	3) Payment of dividend			O		
HRM	1. Establishment and implementation of employment strategy					
	1) Set up basic policy				O	
	2) Periodic employment				O	
	3) Trial employment		O			
Expenditure	1. General expenses					
	1) Over KRW30 millions				O	
	2) KRW5~30 millions			O		
	3) Under KW5 millions		O			
Marketing and Export	1. Ordering and export-related expenditures					
	1) Issue offer sheet	O				
	2) Issue contract sheet	O				
	3) Fix commission rate		O			
	4) Post settlements	O				

(* Mgr.: Manager, BOD: Board of Director)
(Source: One manager from Korean GTC, 2006)

Once the arbitrary decision-maker approves any business matter with his/her own authority, he/she takes full responsibility for that matter and the decision has the full force and effect of the president's approval. Although this system exists, middle or lower level managers normally do not have much authority to perform their job effectively and to decide major business issues because more than 80% of the authority resides at the upper management level.

6.4.2. Decision-making Process within Japanese Firms[80]

The decision-making process in Japanese organisations is unlike the methods of Western decision-making, in which a quick decision, usually involving very few people, tends to be followed by implementation and then evaluation.

The feature of Japanese firms' decision-making culture is consensus-style and bottom-up decision-making. In most Japanese firms, decisions are made on the basis of opinions and information emanating from each of the responsible parties, which are subsequently collated and used to create what is considered to be the best possible proposal for adoption. The management system features a decentralised internal information structure which facilitates horizontal communication between functional units, whereby teams are able to resolve problems autonomously without the involvement of higher managerial levels (Debroux, 2003).

In the process of decision-making, opinions are formed within the network of information exchange and a number of different pieces of information, judgment and

[80] Most of this section draws on two books, "Decision-making and Japan" by Taplin (1995) and "The Rise of the Japanese Corporate System" by Matsumoto, K. (1991).

opinions are then added to or subtracted from these as part of a process, which could aptly be described as self-refining. In Japan, any decisions, changes or modifications occur slowly, involving the participation of all those who will be affected in the entire process of defining, solving and acting upon a problem. Action or the implementation of ideas takes place before the formal decision is announced. The informal decision-making stage in a Japanese organisation is a continuous process in which information is gathered or discussed. In the process of information gathering, each member of the team must have enough information to be able to determine his own role and position within the team and this information must be used so that all team members have a unified perception of the circumstances in which the team is placed.

- **Informal and Formal Procedure in Decision-making: *Nemawashi* and *Ringi***

Japanese firms have different ways of conducting business meetings. Before a formal meeting starts, participants have already drawn their conclusions about the information to be presented at the meeting. This is what the Japanese term, *Nemawashi*, involves – prior consultation. As with the smoothing of the soil around roots before planting a tree, a secure basis helps the decision to grow. According to Tomlinson (1996), once the roots are secure the rest of the tree may then begin to grow. When the tree reaches maturity, the decision is made and everyone hopes that the outcome will be as desired. This system was developed to avoid discrepancies when taking a decision in formal conditions and to gain agreement from everyone in advance, thus keeping relationships harmonious. The most important feature of *Nemawashi* is that it is used to allow the free flow of ideas between people who might never have the opportunity to speak publicly about a proposal.

Once there has been a great deal of discussion at all company levels at the *Nemawashi* stage, issues are taken forward to top management for formal ratification (*Ringi* in Japanese). *Ringi* is a procedure for conducting administrative operations that has been widely used since before World War II in large Japanese organisations. In particular, in implementing some plan for which the cooperation of a number of divisions is necessary, or the results of which will influence many divisions, a *Ringi* is almost always produced. After being created by the division personnel responsible, the *Ringi* is approved by each division and climbs the ranks hierarchically from the plan initiators through every position of the upper-occupational structure: division chief, managing director, vice-president and finally the president (Noda, 1975). According to Yoshino (1975), the *Ringi* system operates in the climate of the traditional Japanese concept of organisation, characterised by ambiguity and elusiveness, where the group rather than individuals constitutes the basic unit of organisation, where the task is assigned to groups and where the functions and the role of each individual member of the organisation are virtually undifferentiated.

- **Counter Arguments to the Bottom-up system, *Nemawashi* and *Ringi***

There are, however, a number of flaws associated with the *Nemawashi* and *Ringi* processes. Kahal (2005) argued that consensus in the Japanese decision-making system is not a virtue, but a weakness, since, traditionally, Japanese are led to believe that there is always one right answer to a question and that authority should not be challenged. Another flaw with the system is that it is too slow. Too many people and sections get involved. Too many meetings are held with many unnecessary questions and suggestions raised. These may delay a business decision, which often requires a swift response (Chen, 2004).

Thus counter arguments can be set against the Japanese typical decision-making process which is widely known as the bottom-up or consensus style. This involves top management in some Japanese organisations in every decision-making process from the very earliest stages.

Ohtsu and Imanari (2002) studied the decision-making process at the highest level within Japanese organisations with specific reference to the use of *ringi* to analyse how the decision-making power is shared. They obtained data through intensive interviews of those who were members of the board of directors or above and who were directly involved in top-level decisions. Ten organisations were examined – three large companies, three subsidiaries, two medium-sized firms and two family-owned companies.

According to one interviewee who worked as a managing director in charge of the overseas operations of a large diversified synthetic fibre company, although the *ringi* system is used in the decision-making process, its function is very different from what is described in the rest of the literature. It is not a consensus-building process but instead a process of spelling out the plans for implementing a decision which has already been made at management meetings.

Another interviewee who worked in a large retail business replied that when a proposal is approved at the managing directors' meeting, the department concerned prepares implementation plans in the form of a *ringi*. According to the interview (Ohtsu and Imanari, 2002, p. 346),

> *"The decision-making is "top-down," not "bottom-up." Here again, the role of the* ringi *is secondary, in that it is used only for making implementation plans after major decisions have already been made."*

One managing director who worked in a medium-sized company also rejected the argument that Japanese-style decision-making is characterised by consensus and bottom-up decision-making. He said (Ohtsu and Imanari, 2002, p. 356),

> *"Decision-making methods vary according to the issues involved and the circumstances surrounding the issues; therefore, it is wrong to assume that there is a uniform and uniquely Japanese style that is applicable to all cases."*

Ohtsu and Imanari's study, then, rejected the view that a uniform Japanese decision-making style always applies. Although the *ringi* system is used, it appears that it is used for different purposes at different levels. The *ringi* is often used for routine decisions, while a relatively small number of *ringi* are used for non-routine decisions. It is also used to spell out the plans for implementing a decision which has already been made at the top level. In total, the *ringi* plays a rather limited role in making firm-wide decisions at the level of top management. The dominant role, instead, is played by various kinds of executive meeting.

In order to crosscheck and confirm the above arguments, the author had a separate interview with one senior manager from a Japanese *Sogo Shosha*[81]. He said,

> *"It is difficult to say that all Japanese companies follow a bottom-up decision-making process. We just follow a standard table of decision-making which was already prepared and fixed by the planning and strategy department of the company. The standard table already specifies, for example, who makes decisions for asset investment and who makes minor decisions division level. So, it is hard to say that the decision-making system within all Japanese companies is bottom-up. Regarding the Nemawashi* and *Ringi systems, we, of course, use them But they are also controlled by the standard table."*

- **A Standard Table for Decision-making within a Japanese Company**

What is, then, the standard table for decision-making within Japanese firms? The table looks very similar to that of Korean companies. The functions and purposes are almost the same as those in Korea. During the interview, the senior manager briefly showed the standard table to allow the author a short glance through of it. The senior manager was not prepared to give the table to the author, because it is strictly confidential. The following table is based on the author's memory of what he learned in this brief glimpse.

[81] A personal interview was arranged in October, 2008 during the senior manager's business trip to Seoul, Korea. The senior manager has almost 20 years of working experience in one of the famous Japanese *Sogo Shoshas*.

(Table 6.3. An Example of a Standard Table for Decision-making within a Japanese Firm)

Job Specification	Decision-maker					Mutual Consultation Department
	BOD	Top Execut.	Team Leader	Mgr.-level	Staff-level	
Asset Investment						All asset investments need mutual consultation with the financing department
1) Over JPYOOOOOO	Approval	Decision				
				Nemawashi or Ringi		
2) Up to JPYOOOOO	Report	Decision				
3) Less than JPYOOOO		Report	Decision			
Establishment of Business Strategy						Strategy, financing, marketing, insurance department
				Nemawashi or Ringi		
1) Corporate-level		Decision				
2) Department-level		Report	Report	Decision		
3) Division-level			Report	Decision	Draft	

(Source: A manager from a Japanese *Sogo Shosha*, 2008)

(Note: The dotted arrow lines in the above table do not feature in the standard table shown by the Japanese senior manager. The author inserted these lines. This indicates that *Nemawashi or Ringi* are used contrary to a widespread belief, as a top-down device in the stage of making implementation plans)

Overall, it seems that not all Japanese firms follow the principle of bottom-up decision-making. It depends, rather, on how important an issue is. As seen in the above table, the scope of decision-making is already fixed in the standard table, prepared and set up by the company. Some decisions are solely made by the top management and some are made by team leaders or at manager level. When team leaders made a decision on their own authority, they had to report it upwards. However, Japanese firms respect the consensus-oriented decision-making system. They use *Nemawashi* and *Ringi*, but it seems that these systems are more common at the stage of implementation planning after major decisions have already been made, as Ohtsu and Imanari (2002) argued.

6.5. Previous Studies of the Decision-making in Korean and Japanese Firms

6.5.1. A Study of Korean Firm’s Decision-making

Lee (1999) made a survey in order to analyse the decision-making procedures of Korean companies’ investment in the UK. The survey was conducted by mailed questionnaires sent to the 28 Korean manufacturing companies operating in the UK. The purpose of this survey was to identify the following major questions; i) the main driving force leading to investment in the UK, ii) the degree of top management’s involvement during the project investigation and decision-making process, iii) decision-making authority at the board of directors meeting and iv) sources of the top management’s authority and power.

According to the survey, first, the main driving engine of Korean companies’ investment in the UK originated in top management’s drive (61.9% of the respondents answered). This result implies that top management in Korean firms plays a conclusive role in the decision-making processes under a highly centralised hierarchy decision structure. Second, regarding the degree of top management’s involvement in the project, most respondents answered that top executives (chairman, president and CEO) were mainly involved (Mean 5.52 on a scale of 7) and they retained absolute power during the decision-making process of the project (Mean 6.38 on a scale of 7). Third, the survey also examined the decision-making authority at the board of directors’ meeting by analysing the structure of board members of 14 selected sample companies at the Korean headquarters. The result showed that most board members in parent companies were inside directors, who were also members of the owner's family or professional managers employed by the owners. But there were very few outside directors (the average number of board members from 14 surveyed companies was 9.4. Among these, the average number of outside directors in each company was only 1.3). Therefore, the board of directors merely ratified the top management's decisions without real involvement. This result implies that the board members do not discharge their natural duty of supervising the activities and performance of the managers, since they tend to be controlled by the owner. Finally, this survey found that many respondents felt that top management's work performance and contribution to the firm is the most influential factor in the source of authority and power in the decision-making process. Ownership was ranked as the third element, followed by managerial/work-related ability.

Furthermore, Lee also carried out a case study of two Korean *Chaebols*, Daewoo and Kia Groups, in order to identify their decision-making processes. The case study also obtained a similar result to the above in that the important decisions, such as new investments and capital tie-ups with foreign companies, were made by the top management, centring on the group chairman.

Consistent with our argument, Lee's study found that the important decisions are made under a highly centralised hierarchy decision structure at the level of top management within Korean organisations. However, since the financial crisis there have been subtle signs of change in the decision-making processes within these organisations even though the top-down and highly centralisation system is still dominating corporate culture across Korean firms. In this context, Lee's study did not clearly explain this with reliable data, although he emphasised that the Korean government has been trying to decentralise decision-making power by increasing the role of the board of directors. One of the factors accelerating such changes in the decision-making process springs from the emergence of new generations equipped with advanced managerial insight acquired through a higher education overseas. For instance, most Korean *Chaebols'* founders (first generation) withdrew or retired from office by transferring their power of management to their second or third generations. Another force to promote such changes is the government's intervention to improve the distorted structure of corporate governance. As a way of restricting the concentration of economic power in the *Chaebols* and decentralising decision-making power by the few, the Korean government has been restricting the *Chaebols* with institutional devices since the financial crisis. According to the Fair Trade Law revised on December 2004, 49 big business groups were selected as groups with "no mutual investment allowed" – such companies were prohibited to hold cross-shares with their affiliates. Moreover, in order to consolidate the role of the board of directors and supervise the activities and performance of managers, the government changed the regulation in 1998 that all listed firms in the stock market must appoint outside directors (Fair Trade Commission, 2005). Therefore, in conclusion, it is worth examining what significant changes have been occurring in the decision-making process within Korean firms since the financial crisis.

6.5.2. A Study of Korean Middle-level Manager's Decision-making Process

Jun (1996) undertook a study of decision-making among Korean middle-level managers . This research was carried out by direct observation in order to identify how the sample group reaches decisions on designated issues provided by the researcher. In total, 706 middle-level managers from Samsung Corporation were selected as a sample group and divided into 110 small teams, each composed of 6~7 members. The average age of the sample group was 32 years and 98 percent of them possessed an undergraduate degree as educational background.

According to the observation, more than 100 teams followed a similar process in their decision-making which were not compatible with the typical six steps of effectiveness; i) recognition of decision requirement, ii) diagnosis and analysis of causes, iii) development of alternatives, iv) selection of desired alternatives, v) implementation of chosen alternative and vi) evaluation and feedback (Daft, 2000). Most observed teams skipped over one or two of the opening steps in a typical decision-making process. For instance, as soon as they recognised the decision requirement, each member of the teams immediately asserted his own individually preferred alternative or opinion, without diagnosing and analysing causes. They next entered the stage of evaluating and choosing alternatives, which took two-thirds out of the time involved in the decision-making process. One interested finding at this stage was that most individuals persisted in their own alternatives or opinions from the beginning to the end, even though sufficient information and opinion interchanged between attendances, but only 5% (35 managers) changed their original opinion by the end.

In conclusion, this research suggested that Korean middle-level managers' decision-making process was somewhat distant from the process presented in rational decision-making theory. The observed decision-making process of Korean middle-level manager can be summarised as follows: i) recognition of the decision requirement, ii) assertion of individually preferred alternative or opinion, iii) evaluation and choosing of alternatives, iv) re-recognition of the problem through mutual evaluation, v) presentation of revised alternatives and vi) selection of compromised alternatives.

6.5.3. A Study of Korean and Japanese Manager's Ethical Decision-making Behaviour

Park (1998) carried out research with Korean managers to identify how managers sub-divide when faced with ethical dilemmas and conflict in the decision-making process. First, in order to examine the level of Korean managers' ethical consciousness compared with that of managers in foreign countries, the study surveyed the basis of ethical preference among Korean and Japanese managers.

(Table 6.4.The Basis of Ethical Preference of Korean and Japanese Managers) Unit: %

Item	Korean Managers			Japanese Managers		
	Composite	Upper-level manager	Lower-level manager	Composite	Upper-level manager	Lower-level manager
Profits of the firm	61.4	61.3	61.8	42.2	56.0	20.0
Individual ethical value	16.7	17.5	14.7	15.6	8.0	26.7
Depends on situation	21.9	21.5	32.5	42.2	36.0	53.3

(Source: Park, H. J. (1998), "Ethical Decision-Making and Behaviour in Korea *(Hankook Kyungyoungjauae Yoonrijeok Uaesakyuljeongkwa Hangdong*)", The Journal of Yonsei Management Research (*Yonsei Kyungyoung Yeonku*), Vol.35, No.2. pp. 206)

As seen in the above table, Korean managers and Japanese managers have different ethical preferences when faced with ethical decision-making. Over half of Korean managers (61.4%) considered "profits of the firm" as the most important basis of ethical preference, while 42.2% of Japanese managers considered "dependence on the situation" as important as "profits of the firm" (42.2%). This result implies that

Japanese managers tend to follow situationism within the organisation. One notable thing here was that the phenomenon of situationism was found significantly in lower-level managers' groups. No less than 53.3% of lower-level Japanese managers replied that their ethical preference depended on the situations involved and only 20% of them considered "profits of the firm" as the most important ethical preference. However, the situation was totally different in the upper-level managers. Unlike lower-level managers, 56% of Japanese upper-level managers replied that the firm's profit was the basis of their ethical preference, whereas only 36% of them followed situationism. This result implies that lower-level managers tend to take a hesitant stance towards business issues until they become familiar with the organisation, but they become sensitive and loyal to all organisational issues once they have secured a firm position within the organisation.

Second, Park undertook further research with 60 selected Korean managers in order to identify how managers subdivide in this process of ethical decision-making. The sample was selected from various business fields: GTCs (17), financial firms (11), manufacturing firms (12), government-owned firms (6) and other firms (14). The research found that four different types of managers can be observed in the process, namely: blind obeyingists, conscienceists, opportunists and adaptationists.

- **Type- I (Blind Obeyingists)**

Managers belonging to this type considered "the survival of the fittest" as the most important factor in business management. They put special emphasis on the firm's survival and profit. When faced with an ethical dilemma or conflict, they tended to ignore quarrels over the rights and wrongs of the problem by treating them as secondary issues. Most Korean managers belonged to this type and they are called “blind obeyingists” who were pursuing the firm’s survival and profits as a top priority. However, this study does not give any answer as to whether managers are unaware of ethical dilemmas or whether they ignore such dilemmas for the purpose of ensuring the firm’s survival and profits.

- **Type – II (Conscienceists)**

This type of managers considered conscience the most important virtue in business. They have strong power and interest in ethical behaviour and a high degree of ethical recognition. Therefore, they took a positive attitude in both the process of understanding ethical dilemmas and solving them. It is assumed that managers belonging to this type possess a coherent and consistent ethical insight in these situations.

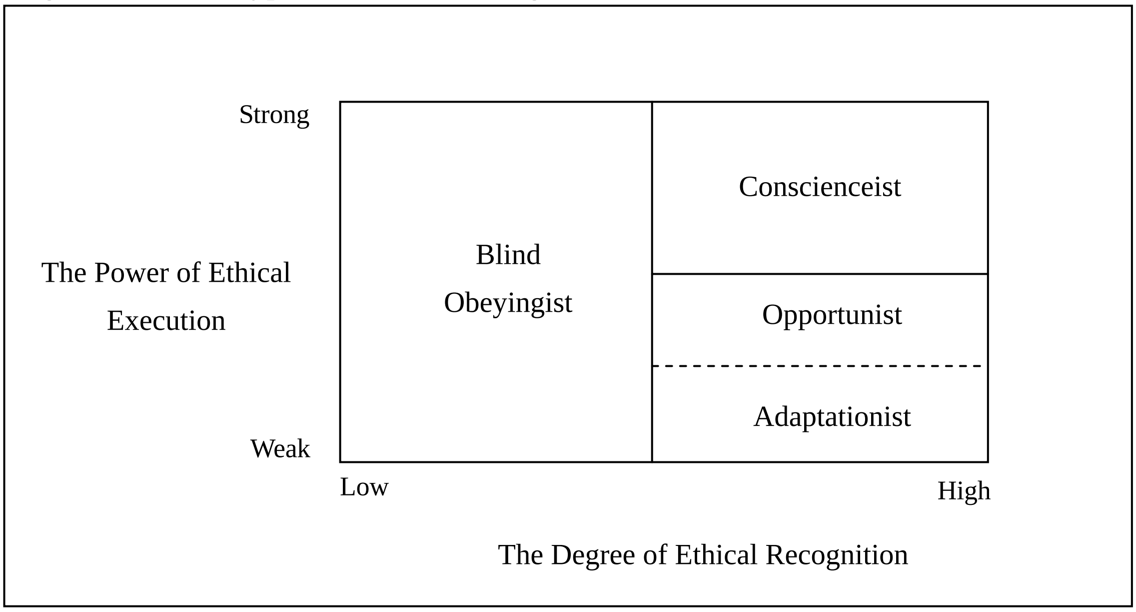
- **Type- III (Opportunists)**

Although managers belonging to this type put special emphasis on conscience and behaviours based on principle, they were passive in addressing ethical conflicts, even if they were well recognised problems. Managers of this type have a tendency towards individualism and can change their attitude according to their personal situation, for example, their desire and intention.

- **Type- IV (Adaptationists)**

A manager of this type was weak in taking action to solve any ethical conflict. He also took negative attitudes and did not have a clear and consistent direction. Although he fully recognised the problem, he lacked the will to settle it, but merely looked at the situation.

(Figure 6.2. Four Types of Korean Managers in Ethical Behaviour)



(Source: Adapted from Park, H. J. (1998), "Ethical Decision-Making and Behaviour in Korea *(Hankook Kyungyoungjauae Yoonrijeok Uaesakyuljeongkwa Hangdong*)", The Journal of Yonsei Management Research (*Yonsei Kyungyoung Yeonku*), Vol.35, No.2. pp. 206)

The implication of this study is that both Korean and Japanese managers' ethical preference and behaviours are not immutable, but tend to change with the situation, even though there were slight numerical differences between two countries. Of the many factors influencing such a change, a manager's individual position within the organisation would be a major factor. For this reason, lower-level managers in both Korea and Japan tend to take a hesitant attitude towards the organisation until they secure a firm position within it. Another factor would be the underlying levels of culture associated with nation, organisation, function and individual (Johnson and Scholes, and Whittington, 2005). Paradoxically, in conclusion, instead of managers devoting themselves to the organisation in order to be able to take a firm position, the tendency of lower-level managers to hesitate in their organisational behaviour would seem to be increasing in the current business circumstances which no longer guarantee lifetime employment.

6.6. Research Objectives and Questions

This section examines the decision-making process within Korean GTCs and Japanese *Sogo Shoshas*. The objectives are to investigate i) the main bodies in the decision-making process within Korean GTCs and Japanese *Sogo Shoshas*, ii) major factors affecting decision-makers and their sources of power and authority, iii) whether there are corporate cultural differences in the decision-making process between Korean GTCs and Japanese *Sogo Shoshas* and iv) the current trends in the decision-making process within the two groups. In order to accomplish these objectives, the following research questions are addressed.

RQ 1. Who are main bodies in the decision-making process within Korean GTCs and Japanese *Sogo Shoshas*?

RQ 2. What are the major factors influencing decision-makers and what are their sources of power to undertake the decision-making?

RQ 3. Are there any corporate cultural differences in the decision-making process between Korean GTCs and Japanese *Sogo Shoshas*?

RQ 4. Are there any recent changes in the decision-making process within the two groups?

6.7. Hypotheses

6.7.1. The Main Body in the Decision-making Process

It is a general understanding that decision-making in Korean firms is, typically, highly centralised in the hands of the top management. Korean firms generally make decisions with few people, because most of them are still run by the owner or founder of the firm and, consequently, decision-making tends to be more centralised. Hence, most decisions made by top management are rarely challenged and they are almost always accepted by all members without visible objection. Previous studies support this argument. Hofstede's survey (1982, 1983 and 1991) of the five major dimensions of culture found that, Korea, not surprisingly, was one of the countries with the highest power distance between superiors and their subordinates. This implies that the decision-making power is not distributed equally to lower-level members, but is centralised to a few upper-level superiors. Lee's (1999) study analysing the decision-making of Korean firm's investment in the UK also found that top executives were involved the most and they retained an absolute power during the process of decision-making for the project.

In contrast, the striking feature of Japanese firms is their structured, hierarchical, group-oriented character, with strong emphasis on maintaining harmony between group members. But Japanese firms are less strongly hierarchical than Korean and are built on the expectation of cooperation amongst all the "core" employees (Whitley and Morgan, 2001). Thus, group-oriented decision-making has been generally described as a bottom-up exercise rather than top-down. Japanese firms prefer to reach a consensus supported by all, but top management are capable of making tough decisions when necessary. However, according to the report of US and Foreign Commercial Service and US

Department of State (2005), family firms founded since World War II and smaller second-tier firms are exceptions to this rule. Most decisions in the large family firms are made by the top executives, but the process is usually managed so that company members have a sense of participation. In the context, this implies that the most important and the most sensitive decisions would be made by top executives, even in the Japanese Sogo *Shoshas.*

Given the above arguments, we can predict that important issues would be made by top executives in both Korean and Japanese firms. From the GTCs'/*Sogo Shoshas'* perspective, such a decision-making tendency would be apparent within the GTCs/*Sogo Shoshas* since most of them are family-based firms and they still emphasise a hierarchical structure. Therefore, the following prediction can be made:

H 1.1	In the process of decision-making for important strategic management within Korean GTCs, top executives (i.e. chairman, president and vice president) may have an absolute power.
H 1.2	In the process of decision-making for important strategic management within Japanese *Sogo Shoshas*, top executives do not have an absolute power, but they may have more decision-making power than team leaders and middle managers.

6.7.2. Major Factors Affecting Decision-making and Sources of Power

Previous studies (Simon and March, 1958; Pfeffer, 1992; Cohen and Bradford, 2002) asserted that power and politics significantly affect organisational behaviour and decision-making. In particular, Pfeffer (1992) argued that it is essentially important to understand the decision-making process from a power and politics perspective because most decisions in organisations are not ideally made on the basis of rationality.

Corporate culture also influences the organisation’s decision-making. There is a big difference in the decision-making process between the Orient and the West. According to Hofstede’s survey (1983), most Oriental countries, such as Korea, Japan, Indonesia, Pakistan, Singapore, Hong Kong and Thailand, tend to have a large power distance with low individualism, while Western countries, such as the UK, the US, Germany, Canada, Denmark and Finland tend to take up small power distance and high individualism. Such differences may be caused by cultural reasons.

Ownership and corporate governance are also important components affecting an organisation’s decision-making. The ideal percentage of shareholding for control is 51% of shares. However, the percentage of shares required for control varies between firms. According to Pitelis and Sugden (1986) only 20% of shareholding is enough to maintain control. Even 1~2% may be sufficient to retain control (Cubbin and Leech, 1983). For instance, the chairman of Samsung Group in Korea and his family held only 1.99% out of the total shares in 2002. With such a small percentage, however, the chairman had absolute power to control and decide all important issues. This example confirms that ownership may not be an essential factor in the control and decision-making of a firm. In the case of Japan, the separation of ownership from management does not allow shareholders and dominant families to actively participate in decision-making. From the example of the two countries above, it can be concluded that ownership and corporate governance may not be major factors influencing the decision-making process in either Korean or Japanese firms.

Where, then, does decision-making power come from? People have different opinions on this question; location in the organisational structure (Pfeffer, 1992), ability to cope with uncertainty, together with knowledge and information (Varman and

Bhatnagar, 1999) and contribution to the firm (Lee, 1999). In particular, Cohen and Bradford (2002) stressed that expertise has always been a source of power and position within the organisation is also important as a source of power. Further, Lee's (1999) study found that decision-makers' work performance and contribution to the firm is the most influential factor in the source of decision-making power, not ownership, seniority or position within the organisation alone.

Based on the above sets of arguments, the following hypotheses, relating to major factors affecting decision-making and sources of decision-making power, are derived:

H 2.1	Within the Korean GTCs and Japanese *Sogo Shoshas*, power and politics may most strongly affect the decision-making process rather than other factors (i.e. ownership, corporate governance and corporate culture).
H 2.2	Within the Korean GTCs and Japanese *Sogo Shoshas*, ownership is not a main source of decision-making power over other factors (i.e. expertise, contribution to firm, managerial and working ability and seniority).

6.7.3. Corporate Cultural Differences in the Decision-making Process between Korean GTCs and Japanese *Sogo Shoshas*

The decision-making process varies depending on the culture. Who makes decisions, how decisions are reached and when they are made differ between organisations around the world. Previous studies found that there have been cultural differences in organisational behaviours between Korean and Japanese firms, even though they are culturally neighbouring countries. The characteristics of a Korean firm's traditional culture are Confucianism, hierarchy, familism and individualism. Regarding individualism in Korean firm, there have generally been two different arguments. One, suggested by Hofstede (1982, 1983 and 1991), is that Korea is a low individualism country with large power distance. The other, suggested by Chang (1983) and Chung, Lee and Okumura (1988), is that most Korean firms tend to take up high individualism centralised to top executives in their decision-making processes. From these two arguments, we can predict that low individualism is a dominant organisational behaviour within lower-level employees, because they do not have their own peculiar power to make decisions, but high individualism is a dominant phenomenon within upper-level managers because they have absolute power in decision-making. This implies that once people within Korean firms are promoted to higher levels, they manifest a high tendency towards individualism.

In contrast, the striking feature of a Japanese firm's corporate culture is collectivism and wholism. According to Ouchi (1981), Japanese firms form inclusive relationships between the employees and the employer. In their decision-making, input from the lower-level employees is the starting point and a consensus of collectivism and wholism allows all members to be involved in this process. Based on the above sets of arguments, the following two predictions can be made:

H 3.1	In the process of decision-making within Korean GTCs, decision-makers may tend more towards high individualism than wholism (i.e. group decision-making system).
H 3.2	In the process of decision-making within Japanese *Sogo Shoshas*, decision-makers may tend to have a more wholistic system than individualism.

6.7.4. Recent Changes in the Decision-making Process

The financial crisis of 1997 fundamentally changed Korea's economic structure as well as management style. The main responses to the financial crisis were two – one was the government sector's response and the other was the corporate sector's. Regarding the government sector, it has tried to implement the IMF programme[82]. The monetary policy recommended by the IMF was to find a total solution for all foreign liquidity, debt and credit problems. As regards the corporate sector, firms have been trying to reduce corporate debt, use transparent accounting, improve standards in corporate governance and decentralise the decision-making power by increasing the role of the BODs. In order to strengthen the role of the BODs, the Korean government amended a regulation that all listed firms must assign outsider directors. Consequently, the consolidating of the BODs' power may restrict the centralisation of decision-making power to a few top executives. Lee's (1999) empirical study also supports this change in Korean firms' decision-making processes. He found that there have been a few signs of change in the decision-making process within Korean firms since the financial crisis through increasing the role of the BODs although the top-down decision-making system is still dominant across Korean firms.

In the case of Japan, the reform of the corporate governance has become an important issue since the crash of the bubble economy. As a way of reform, Japanese government has amended the Commercial Code and introduced a new system modelled after American-style boards of directors. To summarise the above sets of arguments, it is obvious that there have been changes in the decision-making process in both Korean

[82] The implementing of the IMF programme was done over two broad areas – tight macroeconomic policy and structural and institutional reforms. In more detail, the monetary policy recommended by the IMF was to work towards a total solution of foreign liquidity, debt and credit problem. In the area of financial sector restructuring, the programme seeks financial sector reform bills such as the revised Bank of Korea Act and a bill to consolidate the supervision of all financial institutions to be passed at the December special session of the national assembly. As for trade and capital account liberalisation, a timetable was set up in line with WTO commitments to eliminate restrictive import licensing and the schedule for capital account liberalisation was accelerated.

and Japanese firms since the 1990s. Based on this, the following two hypotheses are derived:

H 4.1	After the financial crisis, the BOD's power may increase in the process of decision-making within Korean GTCs.
H 4.2	After the collapse of the bubble economy, the BODs' power in the process of decision-making may increase within Japanese *Sogo Shoshas.*

6.8. Research Design and Methodology

6.8.1. Data Collection, Population and Sample Selection

Like the strategic management analysis in chapter 5, the principal means of data collection for this section was a questionnaire survey and interviews with personnel in Korean GTCs and Japanese *Sogo Shoshas*. Data were collected only from Marketing and Sales SBUs. The population and sample selection procedures were also the same as the strategic management analysis in chapter 5.

6.8.2. The Formulation of the Questionnaire and Measurement of Variables

The questionnaire is divided into five sections. Section one is designed to examine who the main bodies are in the decision-making process. Ten questions were developed to investigate who mainly affects the decision-making process. The variables are top executives, team leaders, middle managers, general staff, boards of directors, labour unions and general meetings of shareholders. Section two measures the factors affecting the decision-making process and sources of power. As variables affecting decision-making, power and politics, ownership, corporate governance and corporate culture were selected on the basis of previous studies, such as Simon and March (1958), Pfeffer (1992) and Pitelis and Sugden (1986). As variables of a decision-maker's source of power, expertise, ownership, managerial and working ability, contribution to firm and seniority are used, on the basis of Lee's study (1999) . Section three attempts to measure cultural differences between Korean GTCs and Japanese *Sogo Shoshas*. Variables are individualism and wholism (i.e. group decision-making). Section four is designed to measure whether there have been any recent changes in the decision-making process. As variables, it uses the degree to which top management changes its mind, the degree of free flow of opinion in the general staff, the degree of decentralisation and the degree of free expression of opinion by the board of directors/labour unions/general meeting of shareholder's. Section five is designed to gather demographic information.

6.8.3. Statistical Data Analysis Instrument

The data analysis of this chapter is also dependent on statistical methods, using the SPSS for Windows. The survey data were analysed by Frequency Analysis and the Chi-square test. The following table shows the variables and statistical techniques used for each hypothesis.

(Table 6.5. Statistical Techniques to be used for each Hypothesis)

Hypotheses	Variables to be tested	Analysis Tool
H.1.1~H.1.2	Main body in the decision-making process within Korean GTCs and Japanese *Sogo Shoshas* (Variables: top executives, team leaders, middle manager, general staff, BOD, labour union and general meeting of shareholder)	Frequency Analysis[83] and Chi-square test
H.2.1	Major factors affecting the decision-making process (Variables: power and politics, ownership, corporate governance and corporate culture)	Frequency Analysis and Chi-square test
H.2.2	Sources of decision-maker's power (variables: ownership, expertise, contribution to firm, managerial and working ability and seniority)	Frequency Analysis and Chi-square test
H.3.1~H.3.2.	Cultural differences in the decision-making process between Korean GTCs and Japanese *Sogo Shoshas* (Variables: individualism and wholism)	Frequency Analysis and Chi-square test
H.4.1~H.4.2	Recent changes in the decision-making process within Korean GTCs and Japanese *Sogo Shoshas* (Variables: the degree of top executives' change of mind, the degree of BOD's power, etc.)	Frequency Analysis and Chi-square test

6. 9. Statistical Data Analysis Results

6.9.1. Testing of Hypotheses

In order to know the ranking of variables in the decision-making process, Frequency Analysis was carried out first. Then a Chi-square test was undertaken to discover the relationship of each variable between Korean GTCs and Japanese *Sogo Shoshas.*

- **Hypotheses 1.1~1.2: The Main Body of Decision-making**

i) Frequency Analysis

[83] Frequency Analysis is the simplest method for analysing categorical data. It is often used as one of the exploratory procedures to review how different categories of values are distributed in the sample.

Hypotheses 1.1 and 1.2 relate to the main body of decision-making within the Korean GTCs and Japanese *Sogo Shoshas*. Hypothesis 1.1 predicted that top executives may have an absolute power in the decision-making process within Korean GTCs. Hypothesis 1.2 anticipated that top executives in Japanese *Sogo Shoshas* do not have an absolute power, but they may have more decision-making power than a team leader or a middle manager. Results of the frequency analysis are as follows;

(Table 6.6. Results of Frequency Analysis for H.1.1~1.2)

Korean GTCs

	Frequency	Percent (%)	Ranking
Top executives	24	18.9	1
Team leader	23	17.7	2
Middle manager	20	15.0	3
General staff	16	12.3	5
BODs	19	14.7	4
Labour union	13	9.9	7
General meeting of shareholders	14	11.5	6
Total	129 (N)	100	

Japanese *Sogo Shoshas*

	Frequency	Percent (%)	Ranking
Top executives	12	16.4	3
Team leader	15	18.4	1
Middle manager	13	17.1	2
General staff	10	14.1	5
BODs	11	14.5	4
Labour union	7	9.2	7
General meeting of shareholders	9	10.3	6
Total	77 (N)	100	

The above result shows that in Korean GTCs, 18.9% of the respondents said that top executives form the main body for decision-making in the process of carrying out important strategic management, followed by team leaders (17.7%) and middle managers (15%). Consistent with our belief, top executives are ranked at the top as the main body of decision-making. But one notable finding is that they do not exercise absolute and decisive power in the decision-making process, unlike our prediction. Another notable thing is that some respondents (14.7%) replied that the power of boards of directors becomes increasingly important in the decision-making process. Yet just a few respondents (9.9%) answered that the labour union influenced the decision-making process. Therefore, Hypothesis 1.1 receives little support.

Unlike Korean GTCs, top executives in Japanese *Sogo Shoshas* are not ranked at the top as the main body of decision-making, but ranked third. 18.4% of respondents replied that the team leader is the main decision-maker, followed by middle manager (17.1%), top executives (16.4%) and the board of directors (14.5%). The respondents felt that labour unions and the general meeting of shareholders were little involved compared to team leaders, middle managers and top executives. Contrary to our prediction, top executives in Japanese *Sogo Shoshas* not only do not have absolute power, but also have no more decision-making power than team leaders and middle managers. Therefore, Hypothesis 1.2 is not supported.

ii) Chi-square Test

In addition to Frequency Analysis, which reveals the ranking of variables, a Chi-square test[84] was also carried out in order to learn the relationship of each variable between Korean GTCs and Japanese *Sogo Shoshas*. Here, not all the tables of variables are presented, only three selected sample tables (e.g. top executives, team leaders and general staff) to see whether they are independent or associated between Korea and Japan.

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[84] The Chi-square test shows whether the variables are independent or whether they are associated with each other.

(Table 6.7. Chi-square Test for Top Executives)

Crosstabulation

		Top Executives					Total
		Influence strongly	Influence	Neither influence nor remain uninvolved	Not involved	Never involved	
Korea	Count	87	28	10	2	2	129
	% of total	67.4%	21.7%	7.8%	1.6%	1.6%	100%
Japan	Count	14	36	25	1	1	77
	% of total	18.2%	46.8%	32.5%	1.3%	1.3%	100%
Total	Count	101	64	35	3	3	206
	% of total	49.0%	31.1%	17.0%	1.5%	1.5%	100%

Chi-square Test

	Value	df	Asymp. Sig. (2-sided)
Pearson Chi-square	50.980(a)	4	.000
Likelihood Ratio	53.777	4	.000
Linear-by-Linear Association	32.190	1	.000
N of Valid Cases	206		
4 cells (40%) have an expected count of less than 5. The minimum expected count is 1.12			

As seen in the above Chi-square test, the Pearson Chi-square value is 50.980 with 4 degrees of freedom (df). In other words, it can be said that top executives' involvement in the decision-making process is different between Korea and Japan (χ^2 = 50.980, df = 4, p (0.000) < 0.01).

(Table 6.8. Chi-square Test for Team Leader)

Crosstabulation

		Team Leader					Total
		Influence strongly	Influence	Neither influence nor remain uninvolved	Not involved	Never involved	
Korea	Count	47	70	7	4	1	129
	% of total	36.4%	54.3%	5.4%	3.1%	0.8%	100%
Japan	Count	25	46	5	1	0	77
	% of total	32.5%	59.7%	6.5%	1.3%	0.0%	100%
Total	Count	72	116	12	5	1	206
	% of total	35.0%	56.3%	5.8%	2.4%	0.5%	100%

Chi-square Test

	Value	df	Asymp. Sig. (2-sided)
Pearson Chi-square	1.810(a)	4	.771
Likelihood Ratio	2.212	4	.697
Linear-by-Linear Association	.008	1	.930
N of Valid Cases	206		
5 cells (50%) have an expected count of less than 5. The minimum expected count is .37			

The Pearson Chi-square value is 1.810 with 4 degrees of freedom (df). This means that the pattern of team leader's involvement in the decision-making process is associated between Korea and Japan (χ^2 = 1.810, df = 4, p (0.771) > 0.01).

(Table 6.9. Chi-square Test for General Staff)

Crosstabulation

		General Staff					Total
		Influence strongly	Influence	Neither influence nor remain uninvolved	Not involved	Never involved	
Korea	Count	5	29	58	28	8	128
	% of total	3.9%	22.7%	45.3%	21.9%	6.3%	100%
Japan	Count	6	18	45	6	2	77
	% of total	7.8%	23.4%	58.4%	7.8%	2.6%	100%
Total	Count	11	47	103	34	10	205
	% of total	5.4%	22.9%	50.2%	16.6%	4.9%	100%

Chi-square Test

	Value	df	Asymp. Sig. (2-sided)
Pearson Chi-square	10.077(a)	4	.039
Likelihood Ratio	10.814	4	.029
Linear-by-Linear Association	5.343	1	.021
N of Valid Cases	205		
2 cells (20%) have an expected count of less than 5. The minimum expected count is 3.76			

The Pearson Chi-square value is 10.077 with 4 degrees of freedom (df). This means that the pattern of general staff's involvement in the decision-making process is associated between Korea and Japan ($\chi^2 = 10.077$, df = 4, p (0.039) > 0.01).

The involvement pattern of other variables – Middle manager ($\chi^2 = 8.097$, df = 4, p (0.088) > 0.01), BODs ($\chi^2 = 6.484$, df = 4, p (0.166) > 0.01), Labour Unions ($\chi^2 = 4.879$, df = 4, p (0.300) > 0.01) and General Meetings of Shareholders ($\chi^2 = 7.736$, df = 4, p (0.102) > 0.01) – in the decision-making process between Korea and Japan is also associated.

- **Hypothesis 2.1: Major Factors Affecting Decision-making**

i) Frequency Analysis

Hypothesis 2.1 examined the major factors affecting the decision-making process within Korean GTCs and Japanese *Sogo Shoshas*. It hypothesised that power and politics may most strongly affect the decision-making process rather than ownership, corporate governance or corporate culture. Results of frequency analysis are as follows;

(Table 6.10. Results of Frequency Analysis for H.2.1)

Korean GTCs

	Frequency	Percent (%)	Ranking
Power and politics	29	22.4	4
Ownership	35	26.9	1
Corporate governance	32	25.2	3
Corporate culture	33	25.5	2
Total	129 (N)	100	

Japanese *Sogo Shoshas*

	Frequency	Percent (%)	Ranking
Power and politics	18	24.1	3
Ownership	17	23.0	4
Corporate governance	20	24.8	2
Corporate culture	22	28.1	1
Total	77 (N)	100	

Contrary to our prediction, power and politics is not a major factor influencing the decision-making process in Korean GTCs and Japanese *Sogo Shoshas*. In the case of Korean GTCs, power and politics received the lowest value of 22.4%. Of 129 respondents, 35 (26.9%) felt that ownership is the major factor affecting the decision-making process, followed by corporate culture (25.5%) and corporate governance (25.2%).

In the case of Japanese *Sogo Shoshas*, 22 respondents out of 77 (28.1%) answered that corporate culture is a main element influencing decision-making, followed by corporate governance (24.8%). As in the Korean GTCs, power and politics is not ranked at the top, but in third place. Therefore, Hypothesis 2.1 is rejected.

ii) Chi-square Test

Only two selected sample tables are presented (e.g. power and politics and corporate culture) to see whether they are independent or associated between Korea and Japan.

(Table 6.11. Chi-square Test for Power and Politics)

Crosstabulation

		Power and Politics					Total
		Influence strongly	Influence	Neither influence nor remain uninvolved	Do not influence	Never influence	
Korea	Count	8	43	54	22	2	129
	% of total	6.2%	33.3%	41.9%	17.1%	1.6%	100%
Japan	Count	3	28	36	9	0	76
	% of total	3.9%	36.8%	47.4%	11.8%	0%	100%
Total	Count	11	71	90	31	2	205
	% of total	5.4%	34.6%	43.9%	15.1%	1.0%	100%

Chi-square Test

	Value	df	Asymp. Sig. (2-sided)
Pearson Chi-square	2.991(a)	4	.559
Likelihood Ratio	3.713	4	.446
Linear-by-Linear Association	.379	1	.538
N of Valid Cases	205		
3 cells (30%) have an expected count of less than 5. The minimum expected count is .74			

The Pearson Chi-square value is 2.991 with 4 degrees of freedom (df). This means that the effect of the pattern of power and politics on the decision-making process is associated between Korea and Japan (χ^2 = 2.991, df = 4, p (0.559) > 0.01).

(Table 6.12. Chi-square Test for Corporate Culture)

Crosstabulation

		Corporate Culture					Total
		Influence strongly	Influence	Neither influence nor remain uninvolved	Do not influence	Never influence	
Korea	Count	14	69	40	4	2	129
	% of total	10.9%	53.5%	31.0%	3.1%	1.6%	100%
Japan	Count	4	58	12	2	1	77
	% of total	5.2%	75.3%	15.6%	2.6%	1.3%	100%
Total	Count	18	127	52	6	3	206
	% of total	8.7%	61.7%	25.2%	2.9%	1.5%	100%

Chi-square Test

	Value	df	Asymp. Sig. (2-sided)
Pearson Chi-square	10.103(a)	4	.039
Likelihood Ratio	10.494	4	.033
Linear-by-Linear Association	1.235	1	.266
N of Valid Cases	206		
4 cells (40%) have an expected count of less than 5. The minimum expected count is 1.12			

The Pearson Chi-square value is 10.103 with 4 degrees of freedom (df). This denotes that the effect of the pattern of corporate culture on the decision-making process is associated between Korea and Japan (χ^2 = 10.103, df = 4, p (0.039) > 0.01)

However, the pattern of influence of other variables – Ownership (χ^2 = 33.022, df

= 4, p (0.000) < 0.01), Corporate Governance (χ^2 = 15.054, df = 4, p (0.005) < 0.01 –on the decision-making process between Korea and Japan is different.

- **Hypothesis 2.2: Major Sources of Decision-making power**

i) Frequency Analysis

Hypothesis 2.2 predicted that ownership is not a main source of decision-making power within Korean GTCs and Japanese *Sogo Shoshas*. Results of the frequency analysis are as follows:

(Table 6.13. Results of Frequency Analysis for H.2.2)

Korean GTCs

	Frequency	Percent (%)	Ranking
Expertise	29	21.2	1
Ownership	26	20.4	3
Managerial and working ability	27	20.9	2
Contribution to the firm	24	18.9	4
Seniority	23	18.6	5
Total	129 (N)	100	

Japanese *Sogo Shoshas*

	Frequency	Percent (%)	Ranking
Expertise	17	21.5	1
Ownership	13	17.1	5
Managerial and working ability	16	20.9	2
Contribution to the firm	16	20.9	2
Seniority	15	19.6	4
Total	77 (N)	100	

In Korea, 21.2% of respondents marked expertise as a main source of decision-making power, followed by managerial and working ability (20.9%), contribution to the firm (18.9%) and seniority (18.6%). However, ownership is ranked third, receiving 20.4%. Almost the same result was obtained from Japan. As in Korea, 21.5% of participants marked expertise as a main source of decision-making power, followed by managerial and working ability (20.9%), contribution to the firm (20.9%) and seniority (19.6%). But ownership received the lowest value of 17.1%, coming last. Therefore, Hypothesis 2.2 receives full support.

ii) Chi-square Test

Only two selected sample tables (e.g. expertise and ownership) are presented as either independent or associated between Korea and Japan.

(Table 6.14. Chi-square Test for Expertise)

Crosstabulation

		Expertise					Total
		Influence strongly	Influence	Neither influence nor remain uninvolved	Do not influence	Never influence	
Korea	Count	33	78	15	1	2	129
	% of total	25.6%	60.5%	11.6%	0.8%	1.6%	100%
Japan	Count	8	57	10	1	1	77
	% of total	10.4%	74.0%	13.0%	1.3%	1.3%	100%
Total	Count	41	135	25	2	3	206
	% of total	19.9%	65.5%	12.1%	1.0%	1.5%	100%

Chi-square Test

	Value	df	Asymp. Sig. (2-sided)
Pearson Chi-square	7.175(a)	4	.127
Likelihood Ratio	7.723	4	.102
Linear-by-Linear Association	2.778	1	.096
N of Valid Cases	206		
4 cells (40%) have an expected count of less than 5. The minimum expected count is .75			

The Pearson Chi-square value is 7.175 with 4 degrees of freedom (df). This denotes that the pattern of expertise as a source of decision-making power is associated between Korea and Japan (χ^2 = 7.175, df = 4, p (0.127) > 0.01).

(Table 6.15. Chi-square Test for Ownership)

Crosstabulation

		Ownership					Total
		Influence strongly	Influence	Neither influence nor remain uninvolved	Do not influence	Never influence	
Korea	Count	40	52	25	12	0	129
	% of total	31.0%	40.3%	19.4%	9.3%	.0%	100%
Japan	Count	3	17	46	8	2	76
	% of total	3.9%	22.4%	60.5%	10.5%	2.6%	100%
Total	Count	43	69	71	20	2	205
	% of total	21.0%	33.7%	34.6%	9.8%	1.0%	100%

Chi-square Test

	Value	df	Asymp. Sig. (2-sided)
Pearson Chi-square	48.116(a)	4	.000
Likelihood Ratio	52.480	4	.000
Linear-by-Linear Association	32.488	1	.000
N of Valid Cases	205		
2 cells (20%) have an expected count of less than 5. The minimum expected count is .74			

The Pearson Chi-square value is 48.116 with 4 degrees of freedom (df). This means that the pattern of ownership as a source of decision-making power is different between Korea and Japan (χ^2 = 48.116, df = 4, p (0.000) < 0.01).

The pattern of other variables – Managerial and Working Ability (χ^2 = 7.614, df = 4, p (0.107) > 0.01), Contribution to the Firm (χ^2 = 7.021, df = 4, p (0.135) > 0.01) and

Seniority (χ^2 = 10.731, df = 4, p (0.030) > 0.01) – as a source of decision-making power is associated between Korea and Japan.

- **Hypotheses 3.1~3.2: Corporate Cultural Differences**

Hypothesis 3.1 anticipated that Korean GTCs' decision-makers may be more individualistic than wholistic and Hypothesis 3.2 predicted that Japanese *Sogo Shoshas'* decision-makers may tend to be more wholistic than individualistic. The results are as follows:

(Table 6.16. Results of Frequency Analysis for H.3.1~3.2)

Korean GTCs

	Answer	Frequency	Percent (%)
Individualism	Very high	10	7.8
	High	54	41.9
	Neither high nor low	50	38.8
	Low	9	7.0
	Non-existent	6	4.7
	Total	129 (N)	100

Japanese *Sogo Shoshas*

	Answer	Frequency	Percent (%)
Wholism	Very high	12	15.6
	High	47	61.0
	Neither high nor low	15	19.5
	Low	3	3.9
	Non-existent	0	0
	Total	77 (N)	100

As anticipated, decision-makers in Korean GTCs tend to be more individualistic than wholistic in their decision-making. Of 129 respondents, 10 marked "very high" (7.8%) and 54 marked as "high" (41.9%). In the case of Japanese decision-makers, unlike the Korean GTCs, they make decisions on the basis of a group decision-making system called wholism. Of 77 participants, 12 of them marked “very high” (15.6%) and 47 marked as “high” (61.0%). Therefore, hypotheses 3.1 and 3.2 received full support.

According to the Chi-square test, the value is 16.434. This proves that the corporate culture in decision-making between Korea and Japan is different (χ^2 = 16.434, df = 4, p (0.002) < 0.01)

- **Hypotheses 4.1~4.2: Recent Change in the Decision-making Process**

i) Frequency Analysis

Hypotheses 4.1 and 4.2 examine recent changes in the decision-making processes in Korean GTCs and Japanese *Sogo Shoshas*. Results of frequency analysis are as follows:

The result shows that there have been many changes in the decision-making process within Korean GTCs since the financial crisis. Although the BOD’s free expression of opinions is not ranked at the top, many respondents (16.5%) answered that the BOD’s power increased. In addition to this increase, respondents replied that other changes have also occurred. One of the notable changes was top management’s change of mind. Of 129 participants, 26 (19.7%) felt that there have been changes in top management’s way of making decisions. As a result, the decision-making power was also decentralised (17.5%) from top management to the lower ranks, such as team leaders and middle managers.

(Table 6.17. Results of Frequency Analysis for H.4.1~4.2)

Korean GTCs

	Frequency	Percent (%)	Ranking
Top management's change of mind	26	19.7	1
General staff's free expression of opinion	22	17.3	3
Decentralisation	23	17.5	2
Labour union's free expression of opinion	18	13.6	6
BOD's free expression of opinion	21	16.5	4
General meeting of shareholders' free expression of opinion	19	15.4	5
Total	129 (N)	100	

Japanese *Sogo Shoshas*

	Frequency	Percent (%)	Ranking
Top management's change of mind	15	19.2	1
General staff's free expression of opinion	14	18.2	2
Decentralisation	14	18.2	2
Labour union's free expression of opinion	10	13.2	6
BOD's free expression of opinion	13	17.6	4
General meeting of shareholders' free expression of opinion	11	13.6	5
Total	77 (N)	100	

There also have been changes in Japanese *Sogo Shoshas*. The most significant change was top management's change of mind. Of 77 respondents, 15 (19.2%) felt that there had been a change in top management's decision-making process. The BOD's power was also strengthened. 17.6% of the respondents answered that the degree of freedom in the BOD's expression of its opinion in the decision-making process had increased. Therefore, Hypotheses 4.1 and 4.2 receive partial support.

ii) Chi-square Test

Only two selected sample tables (e.g. top management's change of mind and decentralisation) are presented to show whether they are independent or associated between Korea and Japan.

(Table 6.18. Chi-square Test for Top Management's Change of Mind)

Crosstabulation

		Top Management's Change of Mind					Total
		Totally changed	Changed	Neither changed nor unchanged.	Unchanged	Totally un-changed	
Korea	Count	21	82	25	1	0	129
	% of total	16.3%	63.6%	19.4%	0.8%	0.0%	100%
Japan	Count	9	36	29	2	1	77
	% of total	11.7%	46.8%	37.7%	2.6%	1.3%	100%
Total	Count	30	118	54	3	1	206
	% of total	14.6%	57.3%	26.2%	1.5%	0.5%	100%

Chi-square Test

	Value	df	Asymp. Sig. (2-sided)
Pearson Chi-square	12.000(a)	4	.017
Likelihood Ratio	12.107	4	.017
Linear-by-Linear Association	9.170	1	.002
N of Valid Cases	206		
4 cells (40%) have an expected count of less than 5. The minimum expected count is .37			

The Pearson Chi-square value is 12.00 with 4 degrees of freedom (df). This means that the pattern of top management's change of mind in the decision-making process is associated between Korea and Japan (χ^2 = 12.00, df = 4, p (0.017) > 0.01).

(Table 6.19. Chi-square Test for Decentralisation)

Crosstabulation

		Decentralisation					Total
		Totally changed	Changed	Neither changed nor unchanged	Unchanged	Totally un-changed	
Korea	Count	4	62	59	4	0	129
	% of total	3.1%	48.1%	45.7%	3.1%	0.0%	100%
Japan	Count	1	40	30	5	1	77
	% of total	1.3%	51.9%	39.0%	6.5%	1.3%	100%
Total	Count	5	102	89	9	1	206
	% of total	2.4%	49.5%	43.2%	4.4%	0.5%	100%

Chi-square Test

	Value	df	Asymp. Sig. (2-sided)
Pearson Chi-square	4.250(a)	4	.373
Likelihood Ratio	4.563	4	.335
Linear-by-Linear Association	.377	1	.539
N of Valid Cases	206		
5 cells (50%) have an expected count of less than 5. The minimum expected count is .37			

The Pearson Chi-square value is 4.250 with 4 degrees of freedom (df). The pattern of decentralisation in decision-making process is also associated between Korea and Japan (χ^2 = 4.250, df = 4, p (0.373) > 0.01).

The pattern of other variable such as the General staff's free expression of opinion (χ^2 = 4.199, df = 4, p (0.380) > 0.01) and the BOD's free expression of opinion (χ^2 = 6.654, df = 4, p (0.155) > 0.01) is associated between Korea and Japan in the decision-making process.

6. 10. Interview Results

The interview results for the decision-making process within Korean GTCs and Japanese *Sogo Shoshas* are given below.

- **Hypotheses 1.1~1.2: The Main Body of Decision-making**

i) Korean GTCs

Two out of four interviewees replied that top executives still decide most important issues. One interviewee, for example, said,

> *"Small day-to-day decision will be generated from team leaders and below but short- or mid- and long-term strategic decision-making is mostly influenced by top management."*

However, the other two interviewees answered that team leaders and middle managers have more decision-making power than top executives do. Overall, top executives, team leaders and middle managers have the most decision-making power. It is moreover a general phenomenon that nowadays some portions of decision-making are delegated from top executives to middle management and many subordinates' opinions are also accepted nowadays within Korean GTCs.

ii) Japanese *Sogo Shoshas*

One interviewee answered that the decision-making within Japanese firms depends on the size of the risk.

> *"It depends on risk size. If risk size is big (like investment), the general meeting of shareholders, executive officials or senior managing director are the decision-makers. If it is small, team leaders decide."*

The other interviewee replied that the daily routine decisions are made by persons in charge. He answered,

> *"We put priority for every decision we make. For the daily business decisions, the biggest involvement is put on the person in charge. Team leader's control is limited when the person in charge is keeping the right process."*

- **Hypothesis 2.1: Major Factors Affecting Decision-making**

i) Korean GTCs

Like the result of the questionnaire survey, the interview survey revealed that ownership, corporate culture and corporate governance are major factors affecting decision-making. All the interviewees felt that power and politics are not major factors. One interviewee replied,

> *"Power and politics are not much related to our decision-making."*

ii) Japanese *Sogo Shoshas*

One interviewee ranked corporate culture, corporate governance, power and politics as the main factors influencing the decision-making process. He further commented,

> *"Even if I have a bright business plan which is not accepted by the corporate culture (i.e. not compatible with corporate culture), the plan will be rejected by the management."*

The other interviewee also ranked corporate culture as the most important factor influencing the decision-making process. He replied,

> *"~~~~~~ our corporate culture which especially gives authority to each responsible person in charge can be most influential. Other three factors are evaluated lower than corporate culture."*

- **Hypothesis 2.2: Major Sources of Decision-making Power**

i) Korean GTCs

Here, also, almost the same results were obtained as in the questionnaire survey. Expertise and managerial and working ability and quality of contribution are the primary sources of decision-making power. Seniority is no longer an important component. One interviewee expresses it thus:

> *"After the IMF crisis, more and more decisions are made on the basis of facts and data and no longer driven by the owner's inclination."*

ii) Japanese *Sogo Shoshas*

One interviewee answered almost the same result obtained as in the questionnaire survey.

> *"I think the expertise and the working ability are most influential. Ownership is not mentioned often."*

The other interviewee replied that all decisions within his company are made on the basis of seniority.

> *"Every decision is made on the basis of seniority which is controlled by company rule. But decision-makers, every time, are concerned about expertise and the contribution to the firm."*

- **Hypotheses 3.1~3.2: Corporate Cultural Differences**

i) Korean GTCs

Three interviewees replied that decision-makers tend to be individualistic in the process of decision-making. But one interviewee expressed the following quite different opinion:

> *"Wholism. So not only one individual will be responsible, but the whole group will be responsible, at the same time. This will bring every one involved to strive to reach the goal, thus having the effect of synergy and driving force."*

ii) Japanese *Sogo Shoshas*

Consistent with our arguments, one interviewee answered,

> *"Decision-makers should always consider wholism, because they should stay in their position for a maximum of five years. If they want to find a new position, they have to consider that their decision-making will support the whole company's profit."*

The other interviewee answered that team-based decisions are not always made. He replied,

> *"Team decision-making is not always taken, but the reporting of individual decision to the senior is common."*

- **Hypotheses 4.1~4.2: Recent Change in the Decision-making Process**

i) Korean GTCs

Here, a quite different result was obtained from that of the questionnaire survey. In the latter, 26 respondents out of 129 replied that top management had changed its view of the decision-making process and 23 respondents ticked the answer 'Decentralisation'. However, in the interview survey, three interviewees replied that they did not feel there had recently been changes in the decision-making process. One interviewee, for example, said,

> *"There were no changes in the process of decision-making. Anyway, our company ultimately set a high value on shareholders' opinions."*

ii) Japanese *Sogo Shoshas*

One interviewee indirectly answered that there have been some changes in the decision-making process recently, in top management in particular. He answered,

> *"The company rule for making decision is almost as same as the past. However, in the past top managements in each sales department have come from their original businesses. So, top managements never oppose other departments' business plans. Now, our company has a rotation system for top management."*

The other interviewee replied that there have been no significant changes. He answered,

> *"General staff's free flow of opinions has been existing as a tradition of my company. But there were no recent changes in other areas."*

- **Other Comments and Opinions**

A special space was provided to express comments from the interviewees or opinions related to the decision-making process. There were no additional comments from Japanese interviewees, but two Korean interviewees, for example, expressed the following opinions,

> *"More and more decision-making is changing from mere cascading from top to bottom; now it's bottom-up. But in order for this to be successful, not only do those at the bottom have to make a lot of suggestions, but those at the top also have to be open to hearing what the others have to say."*

> *"Our company sets a high value on shareholders' opinions and tries to listen in their decision-making to the opinion of those who are in practical working positions."*

6. 11. Conclusion and Discussion

This chapter examined the decision-making process within Korean GTCs and Japanese *Sogo Shoshas*.

First, in Korean GTCs, top executives are still key persons and the main bodies for decision-making, but they do not exercise absolute power. Instead, the power of the team leader and the middle manager has notably increased. This means that the structure of the decision-making process has decentralised to lower level managers compared with the past, rather than remaining highly centralised in the hands of the top management. Most previous studies argued that few people in Korean firms generally make decisions, because most of them are run by the owner or founder of the firm. A top-down decision-making system is still dominant in most Korean firms, because of the Confucian culture, which entails paternalism, loyalty and respect for elders and seniors (Lee, 1999). But it is possible for the GTCs to decentralise their decision-making power to lower levels since they are consist of a number of different business divisions or teams. For an effective work process and to meet rapidly changing market situations, it is necessary to decentralise the decision-making power in highly diversified organisations such as the GTCs. Another notable finding is that the power of boards of directors has become increasingly important. This finding supports Lee's (1999) study, which found that since the financial crisis there have been subtle signs of change in decision-making within Korean firms through increasing the role of the BODs. In the Japanese *Sogo Shoshas*, the team leader and middle manager are the main bodies, rather than the top executives. Consequently, the free flow of lower level personnel's opinions in decision-making is possible. This system has arisen probably because of Japanese firms' unique decision-making culture of consensus. In most Japanese firms, decisions are made on the basis of opinions and information emanating from each of the responsible parties.

Second, it examined the major factors influencing the decision-making process and sources of decision-making power. In Korean GTCs, ownership is the main element affecting decision-making, followed by corporate culture and corporate governance. The important implication here is that top executives or owners of firms still dominate decision-making for important issues, even though the decision-making power is decentralised to lower level managers for minor issues. Another main factor affecting decision-making, corporate culture, is ranked second. Each firm has its own unique corporate culture which has a pervasive influence over its employees' behaviour and actions within the firm. In Korean firms, corporate culture is normally associated with ownership, which is best expressed in the phrase 'a system of centralisation to one person'. This result disproves the view that decision-making power and authority in Korean firms are normally concentrated in the higher echelons of managerial hierarchies, as Chung, Lee and Jung (1997) argued. Regarding the source of decision-making power, expertise and managerial and working ability are ranked first and second, followed by ownership. It seems that ownership is an underlying factor in decision-making, but Korean GTCs put emphasis on employees' expertise and working ability to enhance business performance. In case of the Japanese respondents, they answered that corporate culture is a primary element influencing decision-making, followed by corporate governance and power and politics. Unlike the Korean GTCs, however, the respondents said that ownership is not an important element in the Japanese *Sogo Shoshas'* decision-making process. This result clearly supports the existing literature that ownership and management are normally separated in most Japanese firms. As a source of decision-making power, expertise and managerial and working ability are selected as primary and secondary factors.

Third, we investigated the decision-makers' inclination to take up individualism or wholism. In Korean GTCs, contrary to Hofstede (1982, 1991) argument which defines Korea as a country of low individualism, a majority of respondents answered that decision-makers incline towards individualism rather than wholism in their decision-making. This implies that once people in Korean firms are promoted to a higher level, they have a high tendency to prefer individualism, even though they practised low individualism when they were lower level employees. In the case of Japanese *Sogo Shoshas*, the result complies with expectation and conforms to the existing arguments (Ouchi, 1981; Keys and Miller, 1984; Pheysey, 1993). Most people answered that Japanese decision-makers put emphasis on a consensus of collectivism which allows all members to be involved in the decision-making process

Fourth, the result shows that there have been some changes in decision-making process within Korean GTCs. The most significant change is that there has been a change of mind in top management. Other notable changes are increases in the power of the general staff and the BOD's free expression of their opinion in the decision-making process since the financial crisis. Since 1997, there has been growing pressure to reform large conglomerates in Korea. Many people agree that the crisis stems from structural problems within Korean firms, such as the centralised decision-making power. In this regard, the Korean government has undertaken several reform measures, such as the introduction of the outside director system. Furthermore, in order to decentralise the decision-making, the Korean government needs to activate the role of the BOD and to seek diverse ways to grant the BOD the right to control management as a top decision-making body (Lee, 1999). There also have been changes within the Japanese *Sogo Shoshas* since the collapse of Japan's bubble economy. The most significant change was top management's change of mind and the strengthening of power among the general staff and the BODs. Moreover, it found that there also have been changes in the degree of freedom for labour unions and the general meetings of shareholder to express their opinions in both Korean GTCs and Japanese *Sogo Shoshas*. In total, it implies that the financial crisis in Korea and the collapse of the bubble economy in Japan were significant turning points for most business organisations which allowed them to restructure their management style or decision-making system.

Interview survey revealed almost the same as the questionnaire survey did. One difference between two surveys is, however, related to the recent changes in the decision-making process within Korean GTCs. Some of the questionnaire respondents replied that there had been changes in decision-making such as decentralisation and top management's change of mind. However, three interviewees who took part in the interview survey indicated the opposite. But, paradoxically, one interviewee who expressed the opposite answer replied that his company tried to listen to the opinion of people who were in a practical working position.

This result implies that nowadays there is indeed transformation in the decision-making process within Korean GTCs. The traditional decision-making culture (i.e. the top-down decision-making system) always dominated Korean organisations in the past, but it has been challenged since the national economic crisis. Nevertheless, although there have been slight and gradual changes in the decision-making culture within Korean GTCs, there was no likelihood of radical changes because of the underlying national and corporate culture.

6.12. Difference Analysis between the Two Countries

In the surveys of the decision-making process comparing Korean GTCs and Japanese *Sogo Shoshas*, some different results were obtained, as shown below.

- **Hypotheses 1.1~1.2: Main Body for Decision-making**

In Korea's case, top executives are still major bodies in the decision-making although the power of team leaders and middle managers has increased, whilst, in Japan's case, team leaders and middle managers are the main groups. Why, then, are there cultural differences between the two countries even though they are geographically very close? This may be discussed in terms of the macro-and micro-aspects.

First, there are historical socio-cultural differences; then the geographical characteristics of the two countries may affect the result. The Japanese Archipelago consists of four main islands; *Hokkaido, Honshu, Kyushu* and *Shikoku,* each with its own typical cultural features. There are also several races: the majority *Yamato* and some minorities such as *Ryukyu, Ainu, Uilta and Nivkh*. Moreover, Japan forms one nation by combining each race's cultural features and pursuing local diversity by mutual respect. This historical way of thinking would affect the consensus style of decision-making in any organisation, because group consensus decision-making requires respect for each member's contribution to variety and diversity.

Unlike Japan, Korea is a peninsula and it has only one race, the *Han*. Since the beginning of history, Korea has incessantly been exposed to foreign invasions from Mongolia, *Manjujok*, *Yeojin*, *Malgal,* China and Japan, etc. Under these continued external aggressions, the Korean people have putting their emphasis on the spirit of union to cope with the many challenges from outsiders. In order to strengthen the national solidarity, a strong and capable leader may be required to lead people as an effective unity. Such a historical background may affect Korea's socio-culture as a whole, including its approach to decision-making.

Second, corporate-level organisational structure and size may affect the result. Although the basic organisational structure of the two groups is similar, the degree of business diversification, the scope of the business area, the number of people involved and the size of the organisations are quite different. Hence, in Japan's case, Group-level top managements have difficulties in managing, controlling and making decisions for all issues; many previous writers have pointed out that decentralisation is required when an organisation becomes very big. As a result, the functional experts (i.e. team leaders and middle managers) could in most cases be the major decision-makers rather than top management. In contrast, Korean GTCs' business areas are not as diversified as those of Japanese *Sogo Shoshas*. Since the organisational structure of the GTCs more compact than that of the *Sogo Shoshas*, a tight and vertical control by upper-level management remains possible.

- **Hypotheses 2.1~2.2: Major Factors Affecting Decision-making**

As for factors affecting decision-making, the staff of the Korean GTCs felt that ownership is more important than all the others, while the staff of the Japanese *Sogo Shoshas'* answered that ownership is the least important factor of all. This result reflects well on the two groups' basic management philosophy and it may also be affected by the historical socio-cultural difference between the two countries, as mentioned above.

The characteristic of the Korean *Chaebols* is that group founders dominate the all affiliated firms with their minor shares through cross shareholdings; these impede the separation of ownership and management. Another feature is a succession of management power from founders to their blood relatives rather than to professional managers (Lee, 2006). Why is it then that most *Chaebol* owners cling to the succession by their second generation, not only in their ownership, but also in private possessions, to the extent in some cases of breaching the law?

As is well known, Korea's is a profoundly Confucian culture. The influence of Confucius is still felt today and this impacts also on business activity as on every area of behaviour, values and ways of thinking. Korean business groups tend to recruit employees on the basis of kinship from their own clan (*chiban*) or region (Rowley and Bae, 2004), counting on the loyalty of a junior relative to a senior. Moreover, Koreans are among the greatest believers in the importance of blood connections all over the world. For this reason, most Koreans are more reluctant to donate their property to society or the community than people in the developed countries. They seldom donate to society; rather they bequeathe their goods to their sons or daughters. Such widespread traditional practices may influence other social decisions, including management decisions in business firms.

In contrast, ownership and management are generally separated in most Japanese firms. Although founders or relatives involve themselves in the group's general affairs, management issues are assigned to professional managers. Therefore, *Sogo Shoshas'* people felt that ownership affected decision-making least of all factors, while the corporate culture in such features as group consensus, *nemawashi* or *ringi* was the primary element.

- **Hypotheses 3.1~3.2: Corporate Cultural Difference**

Previous writers have generally suggested that both Korea and Japan are collectivist countries with low individualism. But according to the result, almost 50% (49.7%) of participants from the GTCs answered that decision-makers in Korea were individualistic when they made decisions – a quite inconsistent result with the previous literature, whilst 76.6% of the respondents from the *Sogo Shoshas* felt that Japanese decision-makers were wholistic - which echoes what many existing studies have found. This difference may have its origin in the following factors.

Korea's overall socio-cultural environment is collectivist in its emphasis on relationship with regions (*yongo*), schools (*hakyon*) and clans (*chiban* or *hyulyon*). But from the viewpoint of organisational behaviour, including decision-making in business firms or people's family life, the situation is quite different. This may be because of the underlying culture of high patriarchalism in the family and the military. For instance, heads of families in Korea (mostly males) have traditionally managed their family economy with a high degree of exclusive responsibility, based on strong paternalistic traditions. Needless to say, life in the armed forces which most Korean males experience for two or three years, is highly command-oriented. Both from family and military experiences where top-down decision-making and upper person-oriented management is dominant, then, Korean males may unconsciously learn how to adapt their expectations and how to act in an organisation. Such unique traditions and experiences may influence the individualism of Korean managers when they are in a position to make decisions. This is consistent with a previous argument suggested by Chung, Lee and Okumura (1988) most Korean firms when they make decisions tend to adopt high individualism centralised in top management .

In Japan's case, as the previous literature suggests, most decision-makers adopt wholism, collectivism or a consensus decision-making system. Even though the spirit of collectivism prevails in both countries, Japan lacks the dynamic factors that Korea has. Japanese people place more emphasis on harmony than Koreans and are conservative, prudent and slow to adopt a new system. In this context, Japan is a high collectivism-oriented country (Cho, 2001). In contrast, the corporate culture of Korean firms is 'dynamic collectivism' combining collectivism (oriented towards in-group harmoniousness and tolerant of human nature) and dynamism (rapid, aggressive and progressive) (Cho, 2001; Rowley and Bae, 2004).

CHAPTER 7. SUMMARY AND CONCLUSIONS

7.1. Introduction

This final chapter has four main objectives. First, it summarises the principal findings throughout the study. Second, it presents an overall analysis of the difference between two countries in terms of strategic management and the decision-making process. Third, it discusses theoretical and practical implications for business managers, academicians and government policy markers. Fourth, it suggests a possible direction for future research in this area.

7.2. Summary of Findings

This study began by examining the nature of Korean GTCs and Japanese *Sogo Shoshas*. Then it investigated and analysed their strategic management and decision-making process. Therefore, the findings of this research can be summarised under three headings: a general profile of Korean GTCs and Japanese *Sogo Shoshas*, their strategic management and their decision-making process.

7.2.1. General Profile of Korean GTCs and Japanese *Sogo Shoshas*

A wide literature review of Korean GTCs and Japanese *Sogo Shoshas* produced the following findings. First, the GTCs and *Sogo Shoshas* are unique organisations which are not well-known in Western countries. They have a variety of business functions, such as trading and transaction intermediation, financing, distribution, project organising and coordinating, information-gathering and new resource development, etc. With such diverse capabilities and functions, they have played a crucial role not only for their parent companies' growth, but also for national economic development. Their alignment with their parent companies' development and the government's policy has been constantly developed from their foundation until the 1990s.

Second, the financial crisis in 1997 shattered the Korean GTCs' favourable 30-year reputation and image. Korean GTCs, as core members of the *Chaebol* groups, were treated as among the major agents in the national economic crisis, together with the government and financial institutions, because the GTCs acted as the *Chaebols'* financial resources. They borrowed from international money markets to provide their parent companies with funds for internal use. Then the *Chaebols* diversified their business in various fields and even in non-profit areas using the loans taken out by the GTCs to achieve quantitative growth. When the national crisis no longer allowed them to pursue such business diversifications, they were forced to restructure their organisational system, on account of the fundamental problem in the ownership and corporate governance structure among Korean *Chaebol* groups. Although the GTCs have their own unique roles, they tended to act as financial arms of their parent company (the *Chaebol*) rather than focusing on their original functions. With a low rate of shareholding, the *Chaebol* owners exercised full power of control over every aspect of management, in which was called "a controlling minority structure" (Jeong, 2001). As ownership and management were not separated in the *Chaebol* groups, the *Chaebols'* financial providers could only be the GTCs. Even if many Korean firms started to entrust their management to professional managers after the financial crisis, the tendency of the *Chaebols'* owners to be involved in group-wide management still prevailed in most big conglomerates. But to achieve the ultimate goal of having competitive advantage, it is time for Korean firms, including the GTCs, to concentrate on managing themselves, rather than retaining the parent companies' group-wide management.

Third, Japanese *Sogo Shoshas* were a good textbook example for Korean GTCs' development in terms of business functions, management system, organisational structure and strategic planning. Although the Japanese *Sogo Shoshas'* stable growth has suddenly turned into a drastic decline since the collapse of the bubble economy in the early 1990s, the fundamental reason was quite different from that of the decline of the Korean GTCs. For example, ownership and management are normally separated in most Japanese business groups, even though they were dominated by their founding families. Therefore, *Sogo Shoshas* were able to focus on their original functions of trading and transaction intermediation, financing, distribution, project organising and coordinating, information-gathering and new resource development, etc. Furthermore, their financial activities were geared to financing for customers, rather than for internal use by *Zaibatsu* and *Keiretsu* groups.

Fourth, the GTCs and *Sogo Shoshas* are regarded as mediators in transactions between buyers and sellers, by minimising transaction cost. The issue of transaction cost is one of the key components in management (Mansfield, 1998; Bradley, 1995; Hennart, 1991; Williamson, 1979). In modern business, a firm's success or failure greatly depends upon whether it can reduce transaction costs. As one of the strategic ways to save transaction costs, the use of the GTCs/*Sogo Shoshas* is significant. The GTCs and *Sogo Shoshas* are information gathers who are economic agents supporting production, exchange and utilisation in order to increase the value of the information for their end-user or to reduce the costs of information gathering. They also have unique functions as international marketers and distributors for their customers, in particular for SMEs who do not have international business experience. As quasi-bankers, the GTCs and *Sogo Shoshas* also provide various financial services, such as extending credit, making loans, providing loan guarantees and financing projects.

Fifth, since the 1990s both Korean GTCs and Japanese *Sogo Shoshas* have been faced with management difficulties, due to the internal and external business environments. The environmental variables affecting their management difficulties can be summarised as: i) abolition of assistance from the government, ii) high competition among the existing GTCs/*Sogo Shoshas*, iii) manufacturers' preference for their own direct business, iv) the birth of the WTO and v) the rapid growth of the Chinese market. Therefore, the future of the GTCs and *Sogo Shoshas* is not likely to brighten and they now need to retrieve their reputation through strategic management.

7.2.2. The Strategic Management of Korean GTCs and Japanese *Sogo Shoshas*

Through questionnaire surveys and interviews, this empirical study found the following major features in the strategic management of Korean GTCs and Japanese *Sogo Shoshas*.

First, like many previous studies, it found that Korean GTCs' and Japanese *Sogo Shoshas'* employment of a differentiation strategy is positively associated with environmental uncertainty and complexity. With respect to the relationship between their cost leadership strategy and environmental uncertainty and complexity, there is inverse correlation, as anticipated. And, like previous studies (Miller, 1988; Kwon *et al*, 1999; Kang, 2002), it found that these relationships do not reach high statistical significance. This denotes that a firm's choice of a differentiation strategy rather than a cost leadership strategy tends to increase uncertainty (Govindarajan, 1986). However, according to the additional analysis to check the types of competitive strategy being currently pursued by Korean GTCs and Japanese *Sogo Shoshas*, it found that some of them are adopting in their competitive strategy more than one strategy at the same time.

Second, a positive association between differentiation strategy and organisational decentralisation was found. The result is consistent with Porter's (1980) and Miller's (1988) arguments. According to them, creative ideas, a free flow of opinions and a close collaboration among team members are necessary for a firm to carry out a differentiation strategy to secure new markets and customers. These may be achieved by delegating the decision-making power to lower level managers. Consistent with our arguments, a cost leadership strategy is positively correlated with organisational formalisation, since the main purpose of pursuing a cost leadership strategy is to put strong emphasis on formal profit and budget control in order to keep costs down.

Third, this study also found that the employment by Korean GTCs and Japanese *Sogo Shoshas* of a differentiation strategy is positively associated with the non-financial activities of gaining both market share and new customers. As many previous studies revealed, a major aim in pursuing a differentiation strategy is, despite competitors, to develop new markets and customers with diversified products and services (Miles and Snow, 1978). A mixed strategy (i.e. hybrid strategy) is also positively associated with new market development. The success of the hybrid strategy depends on the ability both to understand and to deliver enhanced value in terms of customer needs, while also having a cost base which permits low prices and is sufficient for reinvestment to maintain and develop bases of differentiation (Johnson, Scholes and Whittington, 2005). However, one notable finding is that a cost leadership strategy is not positively associated with a firm's profitability. This means that in highly diversified organisations such as Korean GTCs and Japanese *Sogo Shoshas*, the profit is not achieved by one factor or strategy alone, but by a combination of several factors or strategies.

Fourth, with respect to the relationship between centralisation and overall performance, it found that there is inverse association between them in Korean GTCs, but there is no statistical correlation in Japanese *Sogo Shoshas*. Although there is this difference between Korean GTCs and Japanese *Sogo Shoshas*, the finding is consistent with previous literature (i.e. a negative association and a positive between centralisation and overall performance). Needless to say, it also found that organisational decentralisation motivates and encourages employees' satisfaction and retention, as was our expectation. Regarding the relationship between formalisation and the speed of job handling, the result reveals that formalisation is inversely associated with the speed of job handling in Japanese *Sogo Shoshas*, but that there is no correlation between them in Korean GTCs.

7.2.3. The Decision-making Process within Korean GTCs and Japanese *Sogo Shoshas*

In the part dealing with the decision-making process, this empirical study found some evidence to support the existing literature, the major finding being as follows.

First, top executives in Korean GTCs still play important roles in the decision-making process, even though the decision-making power of the team leaders and the middle managers is stronger than in the past. But unlike our hypothesis, the power of top executives is not decisive, although they still dominate important decision-making. The decision-making power is more decentralised to middle level managers but not altogether; there are two reasons for this. One is Korea's general corporate culture. It is a general understanding that a top-down, highly centralised decision-making system is dominant in most Korean firms, due to the national culture of Confucianism. The other is ownership. Many respondents answered that ownership is the most important factor affecting decision-making, which recalls the fact that in Korean firms ownership and management are not completely separated. Unlike top executives in Japanese *Sogo Shoshas*, they do not play crucial roles, though team leaders and middle managers are positioned as the main bodies of decision-making. The increase of their power may allow the free flow of all members' opinions in decision-making. Considering the characteristics of such highly diversified big business groups as general trading companies, it may not be effective to depend on a centralised decision-making system concentrated in the hands of only a few people, given the number of different operational departments.

Second, as a primary factor influencing decision-making, it found that ownership and corporate culture are the most important elements in Korean GTCs. This result meets our constant belief that one of the most distinctive features of Korean firms is the high degree of centralisation to upper level management or a group owner. In Japan's case, the corporate culture is a primary element influencing decision-making. However, ownership is not an important element here since ownership and management in most

Japanese firms are normally separated. In both Korea and Japan, it was found that expertise and managerial and working ability are primary sources of decision-making power.

Third, this study found that Korean decision-makers are likely to be individualists in the decision-making process. Even if Korea is a low individualistic country (Hofstede, 1982; 1991), people tend to be individualistic once they are promoted to a higher level of management. In Japan's case, consistent with our arguments, decision-makers allow all members to express their opinions or comments by putting emphasis on a consensus of collectivism.

Fourth, there have since the 1990s been significant changes in the decision-making process in both Korean GTCs and Japan *Sogo Shoshas*. The financial crisis in Korea and the collapse of the bubble economy in Japan were turning points for Korea's and Japan's business organisations to consider their strategic management, including their decision-making systems. The most significant change is top management's change of mind over decision-making. Simultaneously, there have been general changes with the strengthening of the free expression of opinion by general staff, BODs, labour unions and general meetings of shareholders.

7.3. Analysis of the Overall Differences between Korean GTCs and Japanese *Sogo Shoshas*

Some differences were found between the two groups both in strategic management and the decision-making process, as mentioned at the end of Chapters 5 and 6. From the results, this research concluded that both macro-and-micro factors influence the differences, as illustrated in Figure 7.1.

First of all, its culture (both national and corporate), which reflects a nation's unique historical tradition and its people's ways of thinking, values, norms and behaviour, is a major factor. Though Korea and Japan adjoin, the geographical position and the formation of the peoples are quite different. As Japan is a chain of islands and was originally peopled by several tribes, people historically recognise and respect heterogeneity, diversity and variety in one another in terms of culture, religion and ethnic. Religion is a good example. For instance, according to the statistical data of religion in 2005, many Japanese have more than one religion, but in Korea this would be an extraordinary phenomenon. The total population of Japan as of 2005 was 127 million, but total number of people who state a religion is 211 million, many more than the total population (Statistics Bureau, Ministry of International Affairs and Communication, 2008).[85] Therefore, the respondents in the *Sogo Shoshas* answered that organisational centralisation has no correlation with overall performance because most decisions are made on the basis of consensus.

With respect to the corporate culture of the two nations, both Korea and Japan regard collectivism as important element in organisation behaviour. But it is a major difference that Korean people are more dynamic than Japanese. Based on "Be Rush" spirit, aggressive attitude and adoption of military practice, Korean firms observe a system of strict order with a more centralised structure than Japanese ones. For this reason, employees in Korean GTCs felt that centralisation has a negative influence

[85] According to the data, total number of Japanese people who have religion in 2005 was 211, 021,000. It divided them into four categories; Shintoism, Japan's native religion, (107,248,000: 50.82%), Buddhism (91,260,000: 43.25%), Christianity (2,595,000: 1.23%) and others (9,918,000: 4.70%).

overall performance. As a result, decision-makers tend to be individualistic and ownership is the most important thing affecting decision-making.

(Figure 7.1. Analysis of Overall Differences between Korean GTCs and Japanese *Sogo Shoshas*)

K O R E A	**Strategic Management**	**Decision-making Process**
	● Centralisation is inversely associated with overall performance ● Formalisation is not associated with the speed of job handling	● Top executives are the main body in decision-making ● Ownership is a major factor influencing decision-making ● Decision-makers tend to be individualistic

Macro Factors
National & Corporate Culture

Micro Factors
Organisational Size & Business Scope, etc.

J A P A N	**Strategic Management**	**Decision-making Process**
	● Centralisation has no correlation with overall performance ● Formalisation is inversely associated with the speed of job handling	● Team leaders & middle managers are the main bodies ● Corporate culture is a major factor influencing decision-making ● Decision-makers adopt wholism, collectivism and the system of consensus.

The second factor is organisational structure in the two countries, including size, business scope, number of employees and business diversification. Most *Sogo Shoshas* started their business in the 1940s, which was around 25 years earlier than the Korean GTCs began. Since their foundation, *Sogo Shoshas* have diversified their businesses in many directions. During the period of Japan's economic booms, *Sogo Shoshas* with their various functions were one of the major beneficiaries, because they acted as a forerunner for national economic growth. As a result, their organisation grew, acquiring many employees and branch offices around the world which required decentralisation for their effective operation. For this reason, the functional leaders, such as team leaders and middle managers, by adopting wholism, play a crucial role in the decision-making process. Korean GTCs' business history, however, is much shorter, their organisations are smaller and the scope of their business diversification is narrower than the *Sogo Shoshas',* making it possible to have a centralising management.

7.4. Theoretical Implications

Substantial data and information about Korean GTCs and Japanese *Sogo Shoshas* have been examined or analysed through the literature and the field survey. As a result, some theoretical implications may be derived, as follows.

7.4.1. The Rationales of the GTC's/*Sogo Shosha's* Existence

The first theoretical implication is related to GTC's/*Sogo Shoshas'* existence as transaction cost reducer, international trader and distributor, financial provider, etc.

To begin with, the GTC/*Sogo Shosha* are intermediaries pursuing transaction cost economies (Coase, 1937; Williamson, 1975, 1979; Mansfield, 1988; Hennart, 1991; Bradley, 1995; Chang, 2006). As the previous literature suggests, middlemen providing a variety of services between sellers and buyers are required for reducing transaction costs from the inefficiency of the market and the imperfections of the individual's knowledge and honesty. In this context, the GTCs/*Sogo Shoshas* have played significant roles as transaction cost reducers. For instance, before establishing the GTC system in Korea, each individual firm's dispersed business activities in international trade suffered increased transaction cost due to its unorganised system, small size and lack of market information. The GTCs consolidated each firm's trading business by reducing transaction costs, such as that of information-gathering, marketing, searching for new markets and customers' expenses (Chang, 2006).

Second, two theories state that economies of scale and informational economies of scale may be applied to the GTCs/*Sogo Shoshas.* Economies of scale are the cost advantages which a firm obtains due to expansion. In many production processes[86], in particular those involving large fixed assets, average costs fall as production increases (Froeb and McCann, 2008). In addition, Wilson (1999) argued that better information justifies a higher scale of operations and vice versa.

The GTCs/*Sogo Shoshas* utilised economies of scale by expanding their scale of purchasing or selling (e.g. bulk buying or selling of goods through long-term contracts), financing (e.g. borrowing money at lower interest rates) and marketing. Each of these factors reduced the GTCs'/*Sogo Shoshas'* long-term average costs of operation and perhaps gave them cost advantages. For instance, Sumitomo Corporation's mineral resources and energy business unit has achieved constant earning by importing huge amounts of copper from Indonesia and coal from Australia under long-term contracts

[86] A theory of economies of scale is normally applied to production industry. However, this theory may also be applied to other industries including the GTC/*Sogo Shosha* industry where inputs (costs) decrease as outputs (productions) increase.

(Sumitomo Corporation Annual Report, 2008). The GTCs/*Sogo Shoshas* have also been pursuing informational economies of scale by matching end-user specific information needs with various information resources. Through highly diversified information sources such as global networks, they provide customers not only with micro information (e.g. information about market, prices, competitors, etc.), but also with macro information (e.g. information about political, social, economic factors, etc.)

Third, the GTCs'/*Sogo Shoshas'* existence may be explained by a theory of international marketing. International marketing deals with differing markets in many different countries. These markets often vary greatly in their levels of economic development, cultures, customs and buying patterns (Kotler and Armstrong, 2008). For many companies, the multinational or global approach is a desirable management objective, But most of them have a relatively low level of internationalisation in terms of business experience and information about different cultures, customs and consumers' buying behaviour, human resources, capital and networks. On their behalf (e.g. manufacturers, SMEs or ordinary trading companies) the GTCs/*Sogo Shoshas* have pursued business activities across national boundaries. Their well-planned and coordinated combination of marketing methods or tools have contributed in many different spheres; national economic development, SMEs' business growth, the nation's international competitiveness and the GTCs'/*Sogo Shoshas'* own business growth. For example, 25.7% of Korean GTCs' sales in the 1980s came from SMEs and 35.3% in the 1990s (Chang, 2006).

7.4.2. Corporate Governance and Ownership Structure

A theory of corporate governance and ownership in organisations may be one of the theoretical implications of this research. It is generally understood that the key elements of good corporate governance principles include transparency, openness, performance orientation, responsibility and accountability, and commitment to the organisation. La Porta *et al.* (2000) argued that the laws of corporate governance and their enforcement are important factors in market development, firm value and investor protection. Lemmon and Lins (2002) suggested that when firms' controlling managers or insiders have more power over their ownership rights, the performance of these firms is lower than that of other firms during the crisis period. Mitton (2002), however, suggested that firm-specific measures of corporate governance for example, higher disclosure quality, a greater degree of transparency and sound ownership structure influence firm value significantly during the crisis period.

From the viewpoint of Korean GTCs, as Lemmon and Lins (2002) suggested, excessive control power from one person (e.g. the *Chaebol* owner) over a company has always caused problems in corporate governance, strategic management, decision-making and organisational restructure. Parties involved in corporate governance normally include the CEO, BODs, management and shareholders. However, in the case of most Korean GTCs, controlling power is centralised in group owners without the appropriate sharing among regulatory parties. As a result, this unfair governance structure became one of the primary factors in the management problems of the GTCs during the financial crisis and even today. This implies the problem may recur unless the current governance and ownership is changed.

7.4.3. Strategic Management in Organisation

First, even in the highly diversified and integrated trading industry (the GTCs/*Sogo Shoshas*), the existing theory works. In order to examine strategic management in organisations, the structural relationship analysis between environment, strategy, structure and performance has received much attention in the literature over time (Chandler, 1962; Mintzberg, 1979; Miller, 1988; Ketha and Nair, 1995; Kwon *et al*, 1999; Kang, 2002; Chathoth and Olsen, 2007). The sample companies of previous research include manufacturing firms, service companies (e.g. restaurant and hotel firms), financial firms, un-diversified autonomous companies, subsidiaries of diversified big enterprises, etc. Consistent with the existing studies, each variable in the present study is found to be not independent, but interdependent with other variables. The business environment influences a firm's competitive strategy and strategy affects organisational structure. Thus performance is influenced by strategy and structure.

Second, an original theory of Porter's (1985) competitive strategies works quite differently in the practice. According to Porter, firms can be successful when they adopt only one strategy out of three generic strategies. However, contradicting Porter's argument, the present research found that both Korean GTCs and Japanese *Sogo Shoshas* adopt more than one strategy at a time. This implies that they may not create and sustain competitive advantage with a single specific strategy in today's highly competitive market situations. As a result, they mix two or more strategies to cope with the rapidly changing and highly competitive business environment. Hence it is the main task of managers to seriously consider their strategic management.

7.4.4. Decision-making Process in Organisation

According to organisational decision-making theories, managers need to make decisions under certainty, risk or uncertainty and even under ambiguity (Daft, 2000; George and Jones, 2008; Greenberg and Baron, 2008). Another theoretical issue is how much decision-makers follow rationality, which is associated with the concepts of logic, reasoning and sense-making (Stewart, 1994; George and Jones, 2008). But it is generally understood that there are a number of interruptions in managers' rationality which lead them to adopt bounded rationality (Simon and March, 1958; Simon, 1979; George and Jones, 2008; Greenberg and Baron, 2008) or the political model. The next important academic theory related to organisational decision-making concerns what kinds of factors are affected. According to the literature, the major elements affecting decision-making or organisational behaviour are of three kinds; power and politics (Russell, 1938; Pfeffer, 1992), corporate culture (Hofstede, 1991; Mullins, 1996; Slater, 2003) and ownership and corporate governance. With this in mind, this research draws the following theoretical implications from the GTCs' and *Sogo Shoshas'* perspectives.

The first implication relates to the decision-making environment for managers. Compatible with the existing organisational decision-making literature, it assumes that managers in both GTCs and *Sogo Shoshas* make decisions under risk, uncertainty and ambiguity[87]. In other words, although managers know what goals they wish to achieve, they are confronted with limited information (e.g. a rapidly changing environment, severe competition among existing rivals, etc.), time and cognitive ability, which

[87] According to the questionnaire survey asking about the business environment in strategic management, most respondents answered that the business environment at present is uncertain. The mean value for Korea is 2.78 and of Japan is 2.86 on a five-point Likert scale (see Table 5.11. Mean and Standard Deviation of Variables).

prevents them from being purely rational. As a result, they tend to behave with a bounded rationality which hardly ever arrives at optimal solutions. For example, in the case of Korean GTCs, ownership most greatly affects the decision-making process, which is far from the model of rational behaviour. As the decision-making power was traditionally centralised in a few people without separating ownership and management, such short-sighted decisions with irrational behaviour led their companies to the edge of bankruptcy in the period of the national financial crisis.

The second implication is related to the Japanese firms' bottom-up decision-making system, which many previous writers have made well known. However, the recent literature has suggested some drawbacks associated with this system, including the *Nemawashi* and *Ringi* processes (Ohtsu and Imanari, 2002; Chen, 2004; Kahal, 2005). For example, these are often too slow, since many people are involved and numerous meetings are held. Another notable issue is that Japanese firms do not always follow bottom-up or consensus systems. Instead, top management is sometimes involved in the decision-making process from the very earliest stages and the *Nemawashi* and *Ringi* are only follow-up systems used for making implementation plans after major decisions have already been taken by top executives. This present research also supports the above argument. According to one manager of a *Sogo Shosha*, most Japanese firms have a standard table stipulating decision-makers for specific actions. From this, it can be assumed that most important issues are made by top executives and such decisions would be conveyed to lower levels for action planning.

7.4.5. Culture

Both national and corporate cultural differences were found between the two groups. Hofstede (1991) suggested that Korea is one of the strongest collectivist countries, with low individualism, and that the corporate culture is more collectivist than Japan. According to more recent literature, Rowley and Bae (2004, pp. 306~307) argued that Korea's corporate culture can exemplify the concept of dynamic collectivism, developed from the nation's traditional view of collectivism. It strengthens the boundary between in- and out-groups by applying collectivist norms for in-group members and individualistic norms for out-group members.

However, this research found that Korean decision-makers tend to adopt individualism in the process of decision-making rather than wholism or collectivism[88]. It seems to have two aspects. A company or top executive requests employees (normally lower-level staffs) to show collectivist norms by sacrificing themselves in order to extend a firm's performance. At the same time, decision-makers (normally upper-level executives) tend to have individualistic norms when they make decisions.

7.5. Practical Implications

Some practical implications may also be derived for government policy makers and business managers.

[88] In the question asking whether decision-makers adopt individualism or wholism, 10 (7.8%) Koreans out of 129 answered "very high", 54 (41.9%) replied "high", but only 9 (7%) answered "low"

The first implication relates to the role of the government and its intervention in Korean GTCs. Korean GTCs were not the natural outcome of the evolution and expansion of Korea's export-oriented trading firms, but were artificially established by the government and modelled on the Japanese *Sogo Shoshas.* Therefore, the main bodies of decision-making in the process of forming and developing the Korean GTCs have been government officials, rather than the management within the GTCs. As they were created to meet the government's objectives, the government came to specify minimum export targets, capitalisation requirements, number of export items, number of overseas branch offices and the extent of public share ownership for each GTC. As a result, their own long-term tasks, such as developing and promoting sustainable resources, building and maintaining a strong marketing position in overseas markets and seeking various functional diversifications are often overlooked in favour of short-term programmes aimed at meeting necessary requirements to maintain their status as GTCs. Although the government's intervention is weaker than before, requirements for designation as a GTC and requirements to maintain its status are still controlled by the government under the Foreign Trade Law. From the standpoint of policy considerations, this study has useful implications for government policy makers. A government-led policy and a short-term orientation programme are likely to hamper the creation, development and sustainability of the GTCs' international competitiveness in today's highly competitive global markets. At this point, the government may need to consider a radical liberalisation of Korean GTCs by relaxing its regulations.

The second implication relates to Japanese *Sogo Shoshas'* management in the future. Their foremost weakness is their high dependence on commodities transactions. Their traditional strengths in commodities businesses are rapidly reaching maturity. The

Sogo Shoshas in the future will not be mere middle-men; they should put investment in other businesses at the core of their activities and also function as global investors. The combination of various investments and the linkage between businesses through the trading business, which may be regarded as their mature main line, will create an overall synergy and support their status as business integrators. To enhance their ability to adapt to change, the *Sogo Shoshas* may be expected to make dynamic adjustments of their business portfolios through ongoing scrap-and-build programmes. At the same time, they should probably be concentrating their resources in several fields of particular strength and working to make their core competence even stronger. In fields where they are less competitive or less confident, they should turn more to outsourcing and expand their ties of global alliance and partnership with other firms. Furthermore, they need to become increasingly diverse by bolstering their activities in fields of special expertise and strength. As a priority, each should discern its field of core competence and allocate management resources to it. As a result of this process, some of them could come to resemble high-tech firms, while others could end up specialising in project engineering or financing business. In this sense, the future evolution of the *Sogo Shoshas* will be diversification in various directions from their conventional business as trading firms.

The third is related to Korean GTCs' reform of their management system. It is necessary for Korean GTCs to adopt a system which substantially separates ownership from management in order to promote effective business management and to meet a global standard. As the owners in the Korean *Chaebols* have absolute authority in their group's management, they have always managed and controlled all the affiliated firms in their groups, including the GTCs. Consequently, the role of professional managers was limited because of the influence of the group owners. All professional managers are reviewed on the basis of their yearly operation results at the annual meeting attended by all the group presidents. As a result, professional managers are highly sensitive about their short-term management performance, which is largely affected by profit maximisation. In this context, this study has an important implication from the viewpoint of strategic management. In contrast to the Korean GTCs, the main bodies of decision-making in strategic management within the Japanese *Sogo Shoshas* are their professional managers, rather than group owners or family members. Hence, effective management may always need a substantial separation between ownership and management and this would be one of the current sources of competitive advantage in the highly competitive markets.

The fourth implication is for organisation designers. Designers of organisations need to pay special attention to building complementarities between their competitive strategy and its structural, environmental and performance context. For instance, a firm which wants to pursue a differentiation strategy may need to adopt organisational decentralisation by undertaking to delegate decision-making power to lower level managers, in order to cope with uncertain and dynamic environments. As a result of the decentralisation process, a firm may perform well, since decentralisation may encourage employees' satisfaction. At the same time, a firm pursuing cost leadership needs to stay in predictable and stable environments with organisational formalisation, since the main way of implementing a cost leadership strategy is to put strong emphasis on formal profit and budget control. Finally, before designing a hybrid strategy, managers need to have the ability both to understand and to deliver enhanced value in terms of customer needs, while also having a cost base which permits low prices and is sufficient for reinvestment to maintain and develop sufficient bases of differentiation.

7.6. Limitations and Further Research

There have been some limitations during this study and the following topics are recommended for future research.

First, the major topic recommended for future research is more profound study of the Japanese *Sogo Shoshas*. This research started with the intention of examining the nature, history, characteristics, functions, financial performance and management system, strategic management and decision-making process of Korean GTCs and Japanese *Sogo Shoshas and* of comparing the two groups. The above research objectives called for vast amounts of factual information and data for both groups. During the field survey, the author could sense significant corporate cultural differences between Korean GTCs and Japanese *Sogo Shoshas*. There have been no significant problems in the process of gathering information and data from Korean GTCs, both through primary sources (i.e. field surveys) and secondary sources (i.e. journal articles, books, government issued reports, etc.). However, there have been some limitations in gathering data and information from Japanese *Sogo Shoshas*, in particular through field surveys, such as questionnaires and interviews. As with Korean GTCs, secondary data for Japanese *Sogo Shoshas* are readily accessible, but the degree of participation in the survey and the response rate to the questionnaire survey was lower than for the Korean GTCs. Although the author followed the necessary steps to improve response rates (see

Bryman, 2004)[89], most Japanese *Sogo Shoshas* refused to allow any individual visit to their companies, or showed a very cautious and conservative attitude to revealing confidential information. It is, therefore, worth recommending that future research on Japanese *Sogo Shoshas* should be undertaken, with more adequate primary data and information.

Second, more profound field surveys are also needed of the executives of the Korean GTCs and Japanese *Sogo Shoshas*. This study dealt with strategy at the business level of highly diversified organisations. There were difficulties in obtaining information and data from the heads of SBUs or divisions (all at the executive or a director level) during the field survey. Most of them were frequently not available at the office for various reasons, such as domestic or overseas business trips and business meetings with customers and some of them were reluctant to participate in the survey. Therefore, data were collected from four classes; general staff (working experience normally less than five years), assistant manager level (working experience normally five to ten years), manager level (working experience normally ten to 15 years) and senior manager level (working experience normally over 15 years). However, previous surveys (Miller, 1988; Govindarajan, 1988; Dess and Davis, 1984) were undertaken with executives such as CEOs, the most senior vice presidents, or general managers. To increase the degree of representation, further research, including surveys of top management, is recommended.

[89] Bryman (2004) suggests some steps to improve response rates to postal questionnaires survey. Frequently suggested steps are i) writing a good covering letter explaining the reasons for the research, why it is important and why the recipient has been selected, ii) accompanying postal questionnaires by a stamped addressed envelope or, at the very least, return postage and iii) providing clear instructions and an attractive layout to improve the response rate.

Third, the survey of this study was undertaken among only the Marketing and Sales SBUs of the Korean GTCs and Japanese *Sogo Shoshas*. As these are both highly diversified organisations, the result of this study is not enough to represent the position of the whole organisation in any of the cases. Future research is thus recommended with different SBUs or with every SBU (i.e. planning, sales, accounting, financing, logistics SBUs). There are numbers of different SBUs and divisions, which have their own unique roles and tasks within Korean GTCs and Japanese *Sogo Shoshas*. However, this study can be called worthwhile, because it dealt with highly diversified organisations, whereas previous studies (Miller, 1988; Olson, Slater and Hult, 2005) dealt only with small or single-business undiversified corporations. Within small companies, structural issues of decentralisation and formalisation are simply not relevant, or there is no real difference between business-level and corporate-level strategies. According to Mintzberg (1979), simple structured organisations are characterised by centralisation and informality, because direct supervision is their key coordination mechanism. This denotes that significant results with such small or un-diversified companies may have limitations.

Fourth, another major topic for future research could be the analysis of Strategic Management with fractionisation and concretisation of the differentiation strategy. The literal meaning of differentiation is comprehensive and wide-ranging. Hence, it was not easy to examine the detailed relationship between the differentiation strategy and other variables. According to Porter (1985), the means of differentiation are peculiar to each industry. Differentiation can be based on the product itself, the delivery system by which it is sold, the marketing approach and a broad range of other factors. From the GTCs' perspective, differentiation strategies may include product differentiation, marketing differentiation, service differentiation, distribution differentiation, financing differentiation, etc. In some cases, a low cost strategy will also be included in the differentiation strategy, as low cost differentiation. It may provide new theories or hypotheses to undertake if future research with more specific types of differentiation strategy. Moreover, future research is required if the types of strategic behaviours are divided into various forms. For example, among firms pursuing a differentiation strategy, or cost-leadership strategy, some may adopt the posture of prospectors and others take up the posture of analysers or defenders (see Olson, Slater and Hult, 2005)[90]. From the GTCs' perspective, the types of strategic behaviours may be divided into various forms, such as prospector with differentiation, prospector with low cost, analysers with differentiation, analysers with lowcost, defenders with differentiation and defenders with low cost.

Fifth, research is also recommended on the decision-making process within Korean GTCs and Japanese *Sogo Shoshas*. Of the many issues, some are related to the BOD and the labour union which play an important role in decision-making process within organisations. However, the survey in this study was of office workers only and we asked them to express their feelings on the BOD and labour unions[91] issues. It will be significant if future research is undertaken including the members of the BOD and labour unions themselves.

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[90] Olson, Slater and Hult (2005) divided the types of strategic behaviours into four categories: i) prospectors who are developing innovative new products and entry into a new market, ii) analysers who bring out either improved or less expensive versions of products which the prospector introduced while defending core markets and products, iii) low-cost defenders who are providing quality products or services at the lowest overall cost and iv) differentiated defenders who are providing premium services and/or high-quality products to select sets of customers who value and are willing to pay for them.

[91] In most Korean private firms, office workers are prohibited from joining the labour union. So, most of the labour union members are factory workers.

APPENDIX 1. COVER LETTER FOR THE SURVEY

THE UNIVERSITY
OF BIRMINGHAM

Dear Sir,

25 September, 2006

My name is In Woo, Jun, a doctoral student at the Birmingham Business School, the University of Birmingham, UK and you have been selected to take part in my research study concerning the Strategic Management and Decision-making Process within Korean General Trading Companies (GTCs) and Japanese *Sogo Shoshas*.

The primary purpose of this study is to compare the Strategic Management of Korean GTCs and Japanese *Sogo Shoshas*. In particular, I am analysing the relationships among environment, strategy, structure and performance. The second purpose of my study is to investigate and compare the decision-making process within Korean GTCs and Japanese *Sogo Shoshas*.

Your cooperation in completing the attached questionnaire is required for my successful research study. Your responses to this questionnaire will be completely anonymous and all the information you give will be kept completely confidential. The final results will not be identified with any individual or firm.

Please read carefully the directions at the beginning of each section and answer all the questions as accurately as possible. Your cooperation would be highly appreciated and will contribute to the growing knowledge about Korean GTCs and Japanese *Sogo Shoshas*.

Sincerely yours,

In Woo, Jun
Doctoral Student
The Birmingham Business School
The University of Birmingham

Jim Slater
Professor, The First Supervisor
The Birmingham Business School
The University of Birmingham

David Bailey
Professor, The Second Supervisor
The Birmingham Business School
The University of Birmingham

APPENDIX 2. SURVEY OF THE STRATEGIC MANAGEMENT AND DECISION-MAKING PROCESS

SURVEY OF THE STRATEGIC MANAGEMENT

SECTION 1. INFORMATION ABOUT THE ENVIRONMENT

This section attempts to gather information about the business environment surrounding your company. The modern business environment surrounding your firm can be characterised by the degrees of uncertainty and complexity. This section consists of two parts; i) your feelings at present about the business environment and ii) your

expectations about the future. **Please tick one number as ∨ in each statement using the following scale.**

① = Agree strongly	④ = Disagree
② = Agree	⑤ = Disagree strongly
③ = Neither agree nor disagree	

- **Present: How do you feel about the business environment at present.**

Uncertainty	1. It is difficult to predict market trends.	① ② ③ ④ ⑤
	2. It is difficult to forecast customer’s needs and tastes.	① ② ③ ④ ⑤
	3. In our business, customers’ product preferences change a lot over time.	① ② ③ ④ ⑤
	4. Our customers tend to look for new products and services to satisfy their needs.	① ② ③ ④ ⑤
	5. Actions of competitors are difficult to predict.	① ② ③ ④ ⑤
	6. The life cycle of our products and services at present is short.	① ② ③ ④ ⑤
	7. Competitors’ new products and services frequently come to market at present.	① ② ③ ④ ⑤

Complexity	8. In our business, the channel of distribution is complex. 9. It is complex for us to develop new products and services. 10. The market is highly competitive. 11. There are many competing products and services. 12. Potential entrants threaten the market.	① ② ③ ④ ⑤ ① ② ③ ④ ⑤ ① ② ③ ④ ⑤ ① ② ③ ④ ⑤ ① ② ③ ④ ⑤

- **Future: How do you feel about the business environment in the future.**

Uncertainty	1. It may be difficult to predict market trends in future. 2. It may be difficult to forecast customer's needs and tastes in future. 3. In our business, customers' product preferences may change a lot over time in future. 4. Our customers may tend to look for new products and services to satisfy their needs in future. 5. Actions of competitors are difficult to predict in future. 6. The life cycle of our products and services will be shorter in future. 7. Competitors' new products and services may come to market more frequently in future.	① ② ③ ④ ⑤ ① ② ③ ④ ⑤ ① ② ③ ④ ⑤ ① ② ③ ④ ⑤ ① ② ③ ④ ⑤ ① ② ③ ④ ⑤ ① ② ③ ④ ⑤
Complexity	8. In our business, the channel of distribution may become more complex in future. 9. It may be complex for us to develop new products and services in future. 10. The market may become highly competitive in future. 11. There may exist many competing products and services in future. 12. Potential entrants may threaten the market in future.	① ② ③ ④ ⑤ ① ② ③ ④ ⑤ ① ② ③ ④ ⑤ ① ② ③ ④ ⑤ ① ② ③ ④ ⑤

SECTION 2. INFORMATION ABOUT THE STRATEGY

This section is about the competitive strategy. Competitive strategy, often called business-level strategy, is about how to compete successfully in particular markets and how to improve the competitive position of a firm's products or services within the specific industry or market segment.

1. This part attempts to classify your company's present strategy. **Please tick one box only as V that best describes the basic strategy that your company is now pursuing.**

Type of Strategy	Features	Tick Below
Differentiation	● We focus on securing new markets and customers with diversified products and services. ● We actively develop new markets and products/services. ● We focus on providing high quality and our pricing is at the high premium end of the market.	
Cost Leadership	● We focus on stable and predictable markets. ● We focus on keeping our existing customers and markets. ● We concentrate on high volume and low margins. ● We compete on the basis of lower price than our competitors.	
Hybrid Strategy (Differentiation + Cost Leadership)	● We combine differentiation and cost leadership strategy. ● We focus on high-quality products and service with lower prices than competitors	
None of the above		

2. This part attempts to measure your feeling on the strategies of differentiation, cost leadership and hybrid. **Please tick one number as ∨ in each statement using the following scale.**

① = Agree strongly	④ = Disagree
② = Agree	⑤ = Disagree strongly
③ = Neither agree nor disagree	

- **Present: How do you feel about your firm's strategy at present.**

Differentiation	1. We use product/service innovations as a means of competing.	① ② ③ ④ ⑤
	2. Our annual R and D costs for the development of products and services are high.	① ② ③ ④ ⑤
	3. Our annual percentage of sales spent on costs of initiating and implementing product-market innovation is high.	① ② ③ ④ ⑤
	4. We always try to be ahead of competitors in product novelty or speed of innovation.	① ② ③ ④ ⑤
	5. We pursue a tough "undo the competitors" philosophy.	① ② ③ ④ ⑤
	6. We rapidly respond to customers' changing of needs and tastes.	① ② ③ ④ ⑤
	7. We continuously develop new products and services to meet customers' needs.	① ② ③ ④ ⑤ ① ② ③ ④ ⑤
	8. We invest heavily in advertising, sales promotion and public relations.	① ② ③ ④ ⑤
	9. We try to enhance our corporate image.	
	10. We frequently analyse competitors' strategy.	① ② ③ ④ ⑤
Cost Leadership	11. We use cost centres and fix standard costs by analysing variances for cost control.	① ② ③ ④ ⑤
	12. We try to minimise advertising expenditures.	① ② ③ ④ ⑤
	13. We have a strong proclivity for low-risk projects with normal and certain rates of return.	① ② ③ ④ ⑤
	14. We try to control levels of inventory.	① ② ③ ④ ⑤

Cost Leadership	15. All employees are appointed to their posts considering productivity.	① ② ③ ④ ⑤
	16. We try to cut administrative expenses.	① ② ③ ④ ⑤
	17. All employees fully understand the need for cost reduction.	① ② ③ ④ ⑤
Hybrid Strategy (Differentiation and Cost Leadership)	18. We use a high-quality and low price strategy when entering into new markets.	① ② ③ ④ ⑤
	19. We offer a wide range of good quality products and services at lower prices than our rivals.	① ② ③ ④ ⑤
	20. We always try to find suppliers who offer us high-quality products and services at lower price.	① ② ③ ④ ⑤
	21. We maintain long-term relationships with our regular suppliers who offer us high-quality products and services at lower price.	① ② ③ ④ ⑤
	22. Our regular buyers purchase our products and services on the basis of high quality and lower price.	① ② ③ ④ ⑤
	23. We are able to offer high-quality products and services to our customers based on our competitive distribution channel, logistics and transport systems that reduce costs.	① ② ③ ④ ⑤
	24. To deliver high-quality products and services to our customers at low-cost, we reinvest in R and D.	① ② ③ ④ ⑤

- **Future: How do you feel about your firm's strategy in future.**

Differentiation	1. We may use product/service innovations as a means of competing in future.	① ② ③ ④ ⑤
	2. Our annual R and D costs for development of products and services may become higher in future.	① ② ③ ④ ⑤
	3. Our annual percentage of sales spent on costs of initiating and implementing product-market innovation may become higher in future.	① ② ③ ④ ⑤
	4. We may try to be ahead of competitors in product novelty or speed of innovation.	① ② ③ ④ ⑤
	5. We may pursue a tough "undo the competitors" philosophy in future.	① ② ③ ④ ⑤
	6. We may rapidly respond to customers' changing of needs and tastes in future.	① ② ③ ④ ⑤
	7. We may continuously develop new products and services to meet customers' needs in future.	① ② ③ ④ ⑤
	8. We may invest heavily in advertising, sales promotion and public relations in future.	① ② ③ ④ ⑤
	9. We may try to enhance our corporate image in future.	① ② ③ ④ ⑤
	10. We may frequently analyse competitors' strategy in future.	① ② ③ ④ ⑤
Cost Leadership	11. We may use cost centres and fix standard costs by analysing variances for cost control.	① ② ③ ④ ⑤
	12. We may try to minimise advertising expenditures in future.	① ② ③ ④ ⑤
	13. We may have a strong proclivity for low-risk projects with normal and certain rates of return.	① ② ③ ④ ⑤
	14. We may try to control levels of inventory.	① ② ③ ④ ⑤
	15. All employees may be appointed to their posts considering productivity.	① ② ③ ④ ⑤
	16. We may try to cut administrative expenses.	① ② ③ ④ ⑤
	17. All employees may have full understanding of the need for cost reduction.	① ② ③ ④ ⑤

Hybrid Strategy (Differentiation and Low cost)	18. We may use a high-quality and low price strategy when entering into new markets.	① ② ③ ④ ⑤
	19. We may offer a wide range of good quality products and services at lower prices than our rivals.	① ② ③ ④ ⑤
	20. We may try to find suppliers who offer us high-quality products and services at lower prices.	① ② ③ ④ ⑤
	21. We may maintain long-term relationship with our regular suppliers who offer us high-quality products and services at lower price.	① ② ③ ④ ⑤
	22. Our regular buyers may purchase our products and services on the basis of high quality and lower price.	① ② ③ ④ ⑤
	23. We may offer high-quality products and services to our customers based on our competitive distribution channel, logistics and transport systems that reduce costs.	① ② ③ ④ ⑤
	24. To deliver high-quality products and services to our customers at low-cost, we may reinvest in R and D.	① ② ③ ④ ⑤

SECTION 3. INFORMATION ABOUT THE STRUCTURE

This section is about the organisational structure of your company. **Please tick one number as ∨ in each statement using the following scale.**

① = Agree strongly	④ = Disagree
② = Agree	⑤ = Disagree strongly
③ = Neither agree nor disagree	

Decentralisation	1. In your company, decisions tend not to be made at a high level.	① ② ③ ④ ⑤
	2. The individual decision-maker has wide latitude in the choice of means to accomplish goals.	① ② ③ ④ ⑤
	3. Middle-and lower-level managers are allowed flexibility in getting work done.	① ② ③ ④ ⑤

Decentralisation	4. A person who wants to make his decision would not quickly be discouraged.	① ② ③ ④ ⑤
	5. Small matters are not referred to someone higher in your company for a decision.	① ② ③ ④ ⑤
	6. Many important decisions are made locally rather than centrally.	① ② ③ ④ ⑤
	7. Middle- and lower-level managers have substantial autonomy.	① ② ③ ④ ⑤
	8. Middle- and lower-level managers are allowed to increase the level of expenditure for advertising and promotion.	① ② ③ ④ ⑤
	9. Middle- and lower-level managers are allowed to change the selling price on major products or services.	① ② ③ ④ ⑤
	10. Middle- and lower-level managers are allowed to increase the number of employees in a business unit.	① ② ③ ④ ⑤
Formalisation	11. If employees wish to make their own decisions, they are quickly referred to a policy manual.	① ② ③ ④ ⑤
	12. Individuals in your company frequently refer to it as a “bureaucracy”	① ② ③ ④ ⑤
	13. Your company attaches importance to basic principles and all instructions are made through formal documentation.	① ② ③ ④ ⑤
	14. Regardless of changing conditions, your company has faith in past management principles which have proven effectiveness.	① ② ③ ④ ⑤
	15. The communication channel in your company is very formalised.	① ② ③ ④ ⑤
	16. Employees have only restricted access to financial and management information.	① ② ③ ④ ⑤
	17. Your company persists with the same management style rather than diversifying its management style.	① ② ③ ④ ⑤

SECTION 4. INFORMATION ABOUT PERFORMANCE

This section plans to gather information about performance. **Please tick one number as ∨ in each statement using the following scale.**

① = Agree strongly	④ = Disagree
② = Agree	⑤ = Disagree strongly
③ = Neither agree nor disagree	

Overall performance	1. The overall performance of our company met expectations last year.	① ② ③ ④ ⑤
	2. The overall performance of the business last year exceeded that of our major competitors.	① ② ③ ④ ⑤
	3. Top management was very satisfied with the overall performance of the business last year.	① ② ③ ④ ⑤
Financial performance	4. The sales of our company increased in the last financial year compared to the previous one.	① ② ③ ④ ⑤
	5. The profitability of our company increased in the last financial year compared to the previous one.	① ② ③ ④ ⑤
	6. The cash flow of our company is stable compared to last year.	① ② ③ ④ ⑤
Non-financial performance	7. The market share increased in the last . financial year compared to the previous one	① ② ③ ④ ⑤
	8.The number of new customers increased in the last financial year compared to the last one.	① ② ③ ④ ⑤
	9. Employee satisfaction and retention has increased.	① ② ③ ④ ⑤
	10. Employees' speed of job handling has increased.	① ② ③ ④ ⑤
	11. Employees are more responsive toward customers.	① ② ③ ④ ⑤
	12. Employee empowerment has increased.	① ② ③ ④ ⑤
	13. Employee productivity has increased.	① ② ③ ④ ⑤

SURVEY OF THE DECISION-MAKING PROCESS

SECTION 1. INFORMATION ABOUT THE BODY OF DECISION-MAKING

This section attempts to know the main body for decision-making in your company. **Please tick one number as ∨ in each statement using the following scale.**

① = Influence strongly	④ = Not involved
② = Influence	⑤ = Never involved
③ = Neither influence nor remain uninvolved	

1. Only for Korean GTCs: In the process of decision-making for carrying out important strategic management in your company, to what extent do you think the following persons influence the decision-making process?	
Top executives (Chairman, President and Vice president)	① ② ③ ④ ⑤
Team leaders	① ② ③ ④ ⑤
Middle manager	① ② ③ ④ ⑤
General staff	① ② ③ ④ ⑤
Board of directors	① ② ③ ④ ⑤
Labour union	① ② ③ ④ ⑤
General meeting of shareholders	① ② ③ ④ ⑤

Please tick one number as ∨ in each statement using the following scale.

① = Accepted without question	④ = Ignored
② = Accepted	⑤ = Totally ignored
③ = Neither accepted nor ignored	

2. Only for Korean GTCs: In the process of decision-making for carrying out important strategic management in your company, to what extent do you think that top executives accept their subordinates' (team leader, middle manager and general staff) opinions?	① ② ③ ④ ⑤

3. Only for Korean GTCs: In the process of decision-making for carrying out important strategic management in your company, to what extent do you think the Board of Directors express their opinions?	① ② ③ ④ ⑤
4. Only for Korean GTCs: In the process of decision-making for carrying out important strategic management in your company, to what extent do you think the Labour Unions express their opinions?	① ② ③ ④ ⑤
5. Only for Korean GTCs: In the process of decision-making for carrying out important strategic management in your company, to what extent do you think the General Meeting of Shareholders express their opinions?	① ② ③ ④ ⑤

Please tick one number as ∨ in each statement using the following scale.

① = Influence strongly	④ = Not involved
② = Influence	⑤ = Never involved
③ = Neither influence nor become involved	

6. Only for Japanese *Sogo Shoshas*: In the process of decision-making for carrying out important strategic management in your company, to what extent do you think the following persons influence the decision-making process?	
Top executives (Chairman, President and Vice president)	① ② ③ ④ ⑤
Team leaders	① ② ③ ④ ⑤
Middle manager	① ② ③ ④ ⑤
General staff	① ② ③ ④ ⑤
Board of directors	① ② ③ ④ ⑤
Labour union	① ② ③ ④ ⑤
General meeting of shareholders	① ② ③ ④ ⑤

Please tick one number as ∨ in each statement using the following scale.

① = Accepted without question	④ = Ignored
② = Accepted	⑤ = Totally ignored
③ = Neither accepted nor ignored	

7. Only for Japanese *Sogo Shoshas*: In the process of decision-making for carrying out important strategic management in your company, to what extent do you think the top executives allow their subordinates' (team leader, middle manager and general staff) free flow of opinions?	① ② ③ ④ ⑤
8. Only for Japanese *Sogo Shoshas*: In the process of decision-making for carrying out important strategic management in your company, to what extent do you think the Board of Directors express their opinions?	① ② ③ ④ ⑤
9. Only for Japanese *Sogo Shoshas*: In the process of decision-making for carrying out important strategic management in your company, to what extent do you think that the Labour Unions express their opinions?	① ② ③ ④ ⑤
10. Only for Japanese *Sogo Shoshas*: In the process of decision-making for carrying out important strategic management in your company, to what extent do you think the General Meeting of Shareholders express their opinions?	① ② ③ ④ ⑤

SECTION 2. INFORMATION ABOUT FACTORS AFFECTING DECISION-MAKING AND SOURCE OF POWER

This section is about the factors affecting decision-making and its source of power. **Please tick one number as ∨ in each statement using the following scale.**

① = Influence strongly	④ = Do not influence
② = Influence	⑤ = Never influence
③ = Neither influence nor remain uninvolved	

1. In the process of decision-making for carrying out important strategic management in your company, to what extent do you think the following factors affect the decision-making process?	
Power and politics	① ② ③ ④ ⑤
Ownership	① ② ③ ④ ⑤
Corporate governance	① ② ③ ④ ⑤
Corporate culture	① ② ③ ④ ⑤
2. In the process of decision-making for carrying out important strategic management in your company, to what extent do you think the following factors influence the decision-maker's source of power?	
Expertise	① ② ③ ④ ⑤
Ownership	① ② ③ ④ ⑤
Managerial and working ability	① ② ③ ④ ⑤
Contribution to the firm	① ② ③ ④ ⑤
Seniority	① ② ③ ④ ⑤

SECTION 3. INFORMATION ABOUT CULTURAL DIFFERENCE

This section is designed to gather information about cultural differences between Korean and Japanese GTCs. **Please tick one number as ∨ in each statement using the following scale.**

① = Very high	④ = A little
② = high	⑤ = Never
③ = Neither high nor low	

1. Only for Korean GTCs: In the process of decision-making within your company, decision-makers may tend towards individualism over wholism (i.e. group decision-making system).	① ② ③ ④ ⑤
2. Only for Japanese *Sogo Shoshas*: In the process of decision-making in your company, decision-makers may tend towards wholism (i.e. group decision-making system) over individualism.	① ② ③ ④ ⑤

SECTION 4. INFORMATION ABOUT RECENT CHANGE IN DECISION-MAKING PROCESS

This section attempts to gather information as to whether there have been any recent changes in the decision-making process in your company. **Please tick one number as ∨ in each statement using the following scale.**

① = Totally changed	④ = Unchanged
② = Changed	⑤ = Totally unchanged
③ = Neither changed nor unchanged	

1. Only for Korean GTCs: After the financial crisis in the late 1990s, to what extent do you think that there have been any changes in the process of decision-making in your company?					
The degree of top management's change of mind	①	②	③	④	⑤
The degree of general staff's free expression of opinion	①	②	③	④	⑤
The degree of decentralisation	①	②	③	④	⑤
The degree of the labour union's free expression of opinion	①	②	③	④	⑤
The degree of the BOD's free expression of opinion	①	②	③	④	⑤
The degree of the general meeting of shareholders' free expression of opinion	①	②	③	④	⑤
2. Only for Japanese *Sogo Shoshas*: After the collapse of the bubble economy in the early 1990s, to what extent do you think that there have been any changes in the process of decision-making in your company?					
The degree of top management's change of mind	①	②	③	④	⑤
The degree of the general staff's free expression of opinion	①	②	③	④	⑤

The degree of decentralisation	①	②	③	④	⑤
The degree of the labour union's free expression of opinion	①	②	③	④	⑤
The degree of the BOD's free expression of opinion	①	②	③	④	⑤
The degree of the general meeting of shareholders' free expression of opinion	①	②	③	④	⑤

SECTION 5. DEMOGRAPHIC INFORMATION

Job Position	① General Staff ② Assistant Manager ③ Manager ④ Senior Manager ⑤ Other (Please specify:)
Working Experience	① Less than 5 years ② 5~10 years ③ 10~15 years ④ Over 15 years
Job Duty	① Sales ② Planning ③ Accounting/finance ④ Purchasing ⑤ Logistics

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I appreciate your time and effort in filling out this questionnaire.
Please check that you have answered all the questions that you should have answered.
If you have any comments or suggestions, please indicate them below.

APPENDIX 3. INTERVIEW MATERIAL

INTERVIEW MATERIAL ON
THE STRATEGIC MANAGEMENT

SECTION 1. THE RELATIONSHIP BETWEEN ENVIRONMENT AND STRATEGY

This section attempts to investigate the relationship between the business environment surrounding your company and strategy that your company is now pursuing. First, the modern business environment surrounding your firm can be characterised by the degrees of uncertainty and complexity. Second, among many strategies, competitive strategy, often called business-level strategy, is about how to compete successfully in particular markets and how to improve the competitive position of a firm’s products or services within the specific industry or market segment. The typical type of competitive strategy is differentiation and cost leadership.

Questions 1.1~1.2. Do you agree that your company’s differentiation strategy is positively associated with environmental uncertainty and complexity? And do you agree that your company’s cost leadership strategy is inversely associated with environmental uncertainty and complexity? If you have any other opinions, please indicate them below.

SECTION 2. THE RELATIONSHIP BETWEEN STRATEGY AND STRUCTURE

The purpose of building organisational structure is to generate and develop its strategies. It therefore is crucially important to examine the relationship between strategy and structure. In this study, two basic elements of organisational structure are selected:

centralisation/decentralisation and formalisation. Centralisation is the process by which the activities of an organisation, in particular those regarding decision-making, become concentrated within a particular location and/or group. Formalisation is to give formal standing or endorsement to make official or legitimate by the observance of proper procedure. Please answer how you feel about the following questions.

Question 2.1. Do you agree that your company's differentiation strategy is positively associated with decentralisation? If you have any other opinions, please indicate them below.

Questions 2.2. Do you agree that your company's cost leadership strategy is positively associated with formalisation? If you have any other opinions, please indicate them below.

SECTION 3. THE RELATIONSHIP BETWEEN STRATEGY AND PERFORMANCE

This section investigates the relationship between strategy and performance. Each firm may select a specific strategy to enhance its overall performance, because a firm's strategy depends highly upon overall performance. On the other hand, business performance can be divided into two elements: financial and non-financial performances. The typical financial performance measurements are ROI, profitability and productivity while non-financial performance measurements are gaining new markets share, acquiring new customers and employee satisfaction and retention etc. Please answer how you feel about the following questions.

Questions 3.1~3.2. Do you agree that your company's differentiation strategy will be positively associated with the gaining of market share and acquisition of new customers? And do you agree that your company's cost leadership strategy will be positively associated with profitability? If you have any other opinions, please indicate them below.

Question 3.3. Do you agree that your company's hybrid strategy is positively associated with new market development and overall performance? If you have any other opinions, please indicate them below.

SECTION 4. THE RELATIONSHIP BETWEEN STRUCTURE/PERFORMANCE

This section is about to examine how organisational structure (i.e. centralisation, decentralisation and formalisation) affects a firm's performance (i.e. financial and non-financial performance). Centralisation refers to whether decision-making authority is closely held by top managers or is delegated to middle- and lower-level managers. Formalisation is defined as the degree to which formal rules and procedures govern decisions and working relationships. Rules and procedures provide a means for prescribing appropriate behaviours and addressing routine aspects of a problem. Please answer how do you feel about the following questions.

Questions 4.1~4.2. Do you agree that your company's organisational centralisation will be inversely associated with overall performance? And do you agree that your company's organisational decentralisation will be positively associated with employee's satisfaction and retention? If you have any other opinions, please indicate them below.

Question 4.3. Do you agree that your company's formalisation (formal control) will be inversely associated with the speed of job handling and of response toward customers? If you have any other opinions, please indicate them below.

INTERVIEW MATERIAL ON
THE DECISION-MAKING PROCESS

SECTION 1. THE MAIN BODY IN THE DECISION-MAKING PROCESS

This section attempts to know the main body of decision-making in the process of carrying out important strategic management in your company.

Question 1.1. In the process of decision-making in your company, how much do you think the following persons are involved in the process? Please rank them and say why. (Top executives (i.e. Chairman, President and Vice-president), Team leaders, Middle managers, General staffs, Board of directors, labour union and General meeting of shareholders).

Question 1.2. In the process of decision-making process in your company, how much do you think that Top executives allow their Subordinates, Board of Directors, labour unions and general meeting of shareholders free flow of opinions?

SECTION 2. FACTORS AFFECTING THE DECISION-MAKING PROCESS

This section examines major factors' influence on the decision-making process and seeks to know the source of the decision-maker's power.

Question 2.1. In the process of decision-making in your company, which of the following factors mostly influence the process? Please rank them and say why. (Power and politics, Ownership, Corporate governance and Corporate culture).

Question 2.2. In the process of decision-making in your company, which of the following factors mostly influence the decision-makers' power? Please rank them and say why. (Expertise, Ownership, Managerial and working ability, Contribution to the firm and Seniority).

SECTION 3. CULTURAL DIFFERENCES BETWEEN KOREAN GTCs AND JAPANESE *SOGO SHOSHAS* IN THE DECISION-MAKING PROCESS

This section aims to understand the cultural differences between Korean GTCs and Japanese *Sogo Shoshas* in the decision-making process.

Question 3.1. In the process of decision-making in your company, do you think decision-makers tend towards wholism (i.e. group decision-making system) or individualism and why?

SECTION 4. RECENT CHANGES IN THE DECISION-MAKING PROCESS

This section is about whether there have been any recent changes in the decision-making process in your company.

Question 4.1. In the process of decision-making process in your company, have there been any recent changes? If so, which of the following things mainly changed? (Top management's change of mind, General staff's free flow of opinions, Decentralisation, Board of director's free flow of opinion, Labour union's free flow of opinion and General meeting of shareholder's free flow of opinion).

SECTION 5. OTHERS

This section is provided to express any of your comments and opinions related to the decision-making process in your company. If you have any comments or opinions, please indicate them below. Any comments and opinions would be highly welcomed.

APPENDIX 4. LIST OF INTERVIEWEES

<table>
<tr><th></th><th>Name</th><th>Company</th><th>Job Position</th></tr>
<tr><td rowspan="4">Korean GTCs</td><td>Mr. Bo Keun, Kim</td><td>Samsung Corporation</td><td>Manager
PTA/MEG Section
Marketing and Sales</td></tr>
<tr><td>Mr. Keun Ki, Lee</td><td>Hyosung Corporation</td><td>Team Leader
Fine Chemical Team
Marketing and Sales</td></tr>
<tr><td>Mr. Young Kyu, Sung</td><td>Daewoo International Corporation</td><td>Manager
Chemical Team 3
Marketing and Sales</td></tr>
<tr><td>Mr. Ki Sung, Cho</td><td>Lotte Corporation</td><td>Manager
Petrochemical Team
Marketing and Sales</td></tr>
<tr><td rowspan="2">Japanese Sogo Shoshas</td><td>Mr. Kazuyuki Sasaki</td><td>Marubeni Corporation</td><td>Team Leader
Chemicals Department
Marketing and Sales</td></tr>
<tr><td>Mr. Keisuke Sasaki</td><td>Tomen Corporation</td><td>Senior Manager
Chemicals Department
Marketing and Sales</td></tr>
</table>

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