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The HRM of Japanese Firms in the Days to Come of Global Competition

Tetsuhiro Kishita

ABSTRACT

Until the 1980s, Japanese firms succeeded with people oriented HRM in favourable business surroundings, but during the 1990s, in contexts of intense global competition, Japanese organisations changed their HRM systems to performance oriented. Arguably, these reforms were not entirely successful. The purpose of this paper is to examine the history of Japanese firms' HRM systems and discuss the strategic HRM system in the environment of fierce global competition. Based on the contingency theory, three conceptual models of HRM systems are analysed for the fitness between the HRM system and the business environment.

INTRODUCTION

Most people understand that quality human resources are a key factor for firms to sustain a competitive advantage in arenas of fierce global competition. Classical contingency theory claimed that an organisation should adapt its structure to the environment in which it exists to achieve and sustain competitive advantage (Lorsch & Lawrence 1970). The theory evolved to insist that an organisation should not only adjust its structure to the environment, but also its organisational processes and the management control system (Galbraith & Nathanson 1978). A human resource management (HRM) system is no exception. Consequently, organisations are likely to be challenged to adapt their HRM system to the business surroundings in order to achieve and sustain a competitive edge.

For three decades from the 1960s to the 1980s, Japanese companies were quite successful. During this period, the management style of the Japanese companies was highly regarded and the overseas researchers and practitioners referred to it as 'the Japanese management style'. Indeed, many researchers insisted that the lifetime employment and seniority based wage system contributed to the good performances of the Japanese companies during that period (Ouchi 1981, Abegglen & Stak 1985). Nevertheless, after the collapse of the assets inflated economy in the beginning of 1990s Japanese companies reported great losses. In response to fierce competition from new entrants, both in domestic and global markets, Japanese companies were compelled to restructure their businesses and reengineered the management systems and processes. These actions are reflected in the great endeavours to adjust HRM systems to the newer environmental variations.

The purpose of this study is to analyse how the Japanese firms adjust HRM systems to changing business environments. Many articles and books have been written (in Japanese) about how the Japanese companies have been reengineering their HRM system in the new business environment since the early 1990s. However, little is written in English about this trend of HRM system transformation, and the consequences of the changes. This paper adds substance to this 'gap' in the literature in three main ways. First, the paper provides a conceptual framework to classify HRM systems into three types. Second, the paper discusses the history of HRM system of the Japanese companies. Finally, this paper suggests how the Japanese companies might structure and operate HRM systems in the contemporary market place, which characteristically features fierce global competition.

FRAMEWORK FOR ANALYSIS

HRM is a business system. A salient objective of these systems is to process and control people in firms so that the employees are better able to contribute to the goals of the firm. A HRM system is composed of four sub systems.

These elements are 1) an employment management system, 2) a working conditions management system, 3) a reward management system, and 4) a personnel evaluation management system. Employers recruit the necessary people, and assign (or sometimes re-assign) them to produce value added outputs. Well designed HRM systems should also develop the faculty of employees and sometimes control the number of employees. Employers should provide good working conditions for employees to perform jobs effectively and efficiently. They should also reward employees for their service with wage, bonus, promotion and recognitions. In addition to these three HRM systems, firms should also set up a personnel evaluation system. A personnel evaluation system provides a basic concept to the other three sub systems of HRM. Figuratively speaking, a personnel evaluation system works as the operating system of a personal computer and the other three sub systems are the application software installed on the operating system. Figure 1 depicts the systemic arrangement of a HRM system.

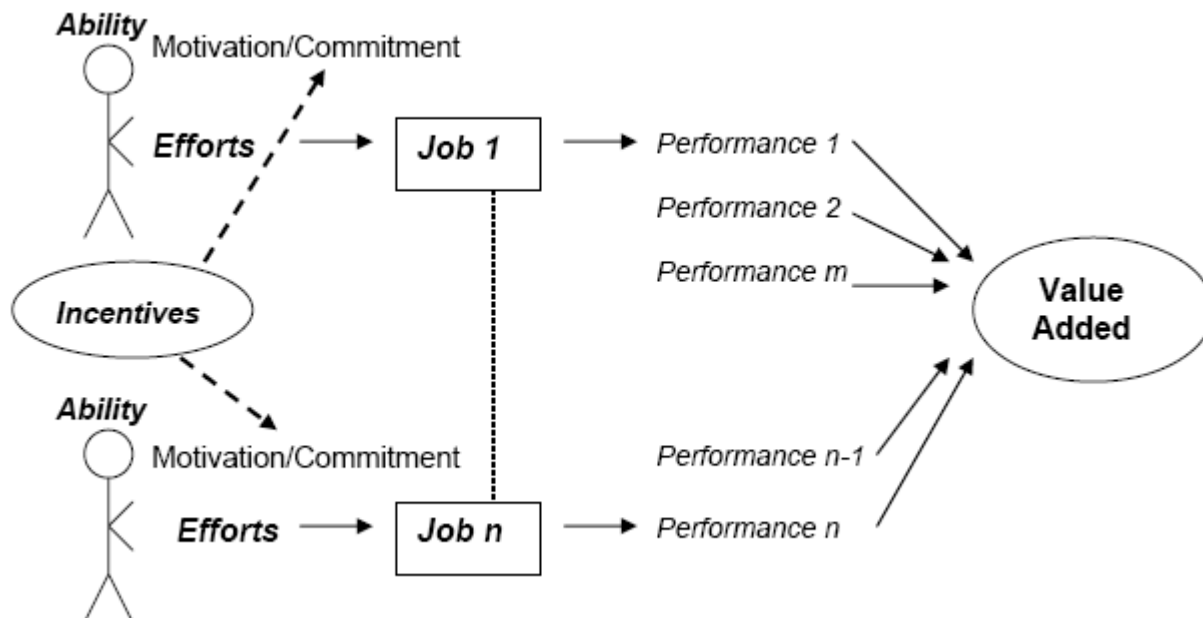
Figure 1 Human Resource Management System

Employment	Working Condition	Reward
<ul style="list-style-type: none"> Recruiting & Assignment Faculty Development Retirement or Dismissal 	<ul style="list-style-type: none"> Working Time & Place Welfare Programmes Labour Union 	<ul style="list-style-type: none"> Wage & Bonus Raise & Promotion Recognition
Personnel Evaluation System		
People centred	Job oriented	Performance oriented

The pattern of HRM depends on a personnel evaluation system. A personnel evaluation system provides a basic concept to grasp the significance, or the value of the human resources. Given that something that has input and output is referred to as a system, a job can be considered as a system – one in which input is the effort of the employee and output is the performance achieved. Employees exert efforts for their jobs and their job performances integrate into the organisational performance chain.

Employee contributions are the embodiment of their physical power, skills and knowledge. These employee attributes are called ‘ability’ and the capacity of an employee’s effort will depend on their abilities. Nevertheless, the extent of efforts that an employee actually exerts will depend on his or her passion to achieve the job assigned, or on his or her enthusiasm (e.g., motivation) to contribute to the organisation for which he or she works. It is likely that stronger motivation will link with a greater effort, and more intense commitment to organisational goals. Simultaneously, this stronger motivation and intensive commitment is likely to enhance ability because learning skills and knowledge are associated with performing their jobs. Employers can enhance this motivation or commitment with appropriate rewards, not only monetary rewards such as wages and bonuses, but also non-monetary rewards such as recognition from other organisational members (Imano 1998). The various input variables included in an organisational performance chain, conceived at a systemic level to produce value added outputs, are illustrated in Figure 2.

Figure 2 A Job as a System to Produce Value



Personnel evaluation systems exist as three main types (Imano & Sato 2002). The first type of personnel evaluation system is the one that puts a focus on inputs, that is to say, efforts or abilities. The reward system that depends on this type of personnel evaluation system is referred to as ability based payment, and this is the people oriented system that Japanese firms took advantage of from the 1960s until the 1980s. The second type of personnel evaluation system is a job oriented system, one that puts an emphasis on the job. The incentive system dependent on this type of the personnel evaluation system is pay, and U.S. firms and European firms have made the most use of this system. The third arrangement is a performance oriented system. More often than not, professional baseball players or professional soccer players are evaluated on their performance, and indeed, their annual payments are based on their performances for the season. The incentive system based on the performance oriented is called pay for performance. In business, payment of employees, such as sales people and lawyers, is often on a performance outcome basis.

THE HISTORY OF JAPANESE HRM

Japanese manufacturing firms, especially automobile makers, electrical appliance makers, electric equipment manufactures, and precision machinery industries enjoyed a world wide competitive advantage for three decades from the early 1960s to the 1980s. However, after the bursting of the nation's asset inflation 'economic bubble' in the beginning of 1990s, Japanese firms lost their competitive edge. In concurrence with the collapse of the Japanese bubble economy, the Japanese style of management that foreign managers or researchers had revered lost popularity. Subsequently, Japanese firms have been struggling to reengineer their HRM systems.

HRM in the Period of the 1960s to the 1980s

A hallmark of Japanese firms during the successful three decades (1960 to 1980) was the 'people oriented' HRM systems. This framework placed an emphasis on employees' abilities. Employers hired people for a relatively prolonged period and they provided employees with incentives to work earnestly. The Japanese are educated in the six-three-three schooling system, which begins in April and ends in March. After graduating high school, they are university educated for four years. In the successful three decades, approximately one out of three or four high school graduates continued to study in universities. Japanese employers hired high school graduates and university graduates all together in April. Both employers and employees tacitly understood that the employment contracts were to be long term. Notably, it was not the rule for Japanese employers at that time to hire staff with working experiences in other companies.

The employers invested in education and training of employees. Employers preferred graduates who were willing to work for the companies with an emphasis on employing the established university graduates who held membership of sport clubs teams. Employers assumed these graduates were smart in a general way as well as well trained in vertical personal relationships (seniority).

The employers offered several kinds of 'red carpet' benefits to these employees. Many employers provided the employees with company housing and provided them with tours to domestic or overseas resort locations, parties and sporting events (e.g., golf excursions on business trips). The expenses outlaid for employees' welfare were considered a company expense in tax accounting systems. In practice, not only senior managers, but also middle managers enjoyed entertainment (e.g., nightspots) which was charged as company entertainment expenses. In fact, many employees embellished their private lives with abundant company entertainment money. Some critics referred to a Japanese salaried employee as a 'domestic animal of a company'.

Employees were paid and promoted on a seniority basis. A typical Japanese worker was usually paid monthly and given an additional lump sum payment twice a year (in June and December), which the Japanese referred to as a bonus (equivalent to several months' base pay). The normal monthly payment consisted of a basic salary and several kinds of allowances, such as dependent family payment, housing benefits, overtime premiums for non exempt employees, and managerial post allowances for exempt employees. Since a discretionary labour system (free time system) was not a common rule to non managerial workers until the early 1990s, ordinary employees who were not in charge of supervisory positions were principally paid overtime premiums. Although in the successful three decades many Japanese firms paid several kinds of allowances, in the main a Japanese worker was paid a basic wage.

Most Japanese employers paid a basic wage based on the ability of their employee to perform jobs. The assessment system applied to a evaluate worker' abilities was called the ability based grade system. Employers abstracted the abilities to execute the jobs in the companies, and rated and ranked those abilities, and consequently, the amount of basic salary was determined according to each grade. Every employee in a company that introduced the ability based grade system was allocated to a rank, and accordingly given a basic salary. All employees in a company that installed this grade system were evaluated and ranked every year.

The incentive system of Japanese firms in this period (1960s to 1980s) had the appearance of an ability oriented

system. However, the system was actually based on seniority. In fact, Japanese workers were ranked upwards and automatically given a raise each April. In other words, Japanese employers formally introduced the ability based incentive system and operated the system on a seniority basis. Continuing to pay employees on a seniority basis necessitated an expansion of company funds to distribute to employees as they increased in seniority, and thus, they were paid more in successive years. The favourable economic environment of the period enabled Japanese employers to pay so generously.

A major effect of the system was soliciting an employee linkage with their organisation. Most Japanese people in this period recognised that seniority was a fair standard by which to be treated, and tacitly understood that employees could get benefits from a longer service for the company. The HRM system that endorsed a long term employment and seniority based payment worked well in motivating more employees to retain their jobs, but this management style had a problem in that it did not encourage competition among the workers, as treating employees equally and promoting competition among them contradicted each HRM strategy. Therefore, the Japanese employers devised other mechanisms to promote competitive pressures to encourage people to work harder and to climb the corporate ladder. For instance, Japanese employers appointed the employees to managerial positions based on the performance of their work instead of their seniority. In the successful three decades, most managers in Japanese firms were promoted internally after ten years of service. As smart employers did not tell who would be promoted (for this period), almost every employee thought that he (or very rarely she) would have a chance to be selected to higher positions, and thus (he) made great efforts.

The lifetime employment system was another mechanism to get more employees committed to their work. The employers, however, could not provide all of them with managerial positions because the number of managerial positions in an organisation was limited. Thus, non managerial staff, with a long service, tended to lose their enthusiasm for jobs. To counter this effect the employers set up some related companies and transferred the employees to those subsidiaries as managers. In other words, the lifetime employment system in Japanese firms was an employment security system within a group of related companies. Most Japanese big companies had (and still have) several dozen, or sometimes several hundred affiliated companies. Some big companies transferred an employee in his or her forties (i.e., those not selected as senior managers in the parent firm) to an affiliated company.

HRM of Japanese Companies in the Global Competition Age of the 1990s

The fierce global economic competition of the 1990s effectively eroded the earnings of the Japanese firms compelling them to reengineer their HRM systems to become more competitive. Some prominent Japanese companies began to introduce 'performance oriented HRM' in the beginning of the 1990s, which provided a foundation for more Japanese companies to adopt this style of HRM in the 2000s. The term performance oriented HRM has become a 'buzz' word in the contemporary Japanese business world.

A consequence of the collapse of the 'bubble economy' was redundancy in the workforce. Despite a reduction in the intake of freshmen, there was still an excessive level of labour, which encouraged employers to abandon the tacit contract of lifetime employment. In the beginning of 1990s, the workforce reduction through attrition and early retirement was insufficient so by the end of the decade employers were obliged to reduce the number of regular employees. One strategy employed by some employers was to outsource the labour force from manpower supply companies, which enabled Japanese employers to control the level of their workforce through the labour market.

A pressing necessity for the survival Japanese companies with declined competitiveness was to reduce costs. Most of the larger Japanese companies, which had provided employees company housing and resort condominium benefits, 'sold off' such facilities to increase company cash reserves. Allowances for business meals and expense for transportation were severely reduced. Many business employees began to take subways and buses instead of taxis, and even the executives who used to take comfortable first class seats were required to take the less comfortable seats in economy class.

The collapse of the 'bubble economy' dramatically changed the incentive system. In the middle of 1990s, some of the larger Japanese firms began to pay more to good performers and less to poor performers in their disbursement of bonuses. Fujitsu Company Limited, for instance, one of the leading companies in electric devices in Japan, introduced the bonus system to pay 10 times more to a super performer than to a poor performer. In addition, the Nikko Securities Company introduced a pay system in which the company promised to pay to all non managerial employees uniformly three hundred thousand yen a month, and a proportionally variable bonus based on the performance of their completed work. While the company promised to pay a super performer 48 monthly salaries (as a bonus), there was a complementary pronouncement to pay a poor performer only a half a monthly salary as his annual bonus. Theoretically, a superior performer had a chance to be able to earn approximately five times more annually than a poor performer.

Japanese legislation also promoted the trend to performance oriented HRM. The amendment of the standard labour law in 2000 enabled white collar employees in the company' headquarters to work with discretion, which

meant that they could decide the way and the time of doing work. In spite of these amendments seeming to be good for workers, (because they had a power to decide the detail about their work) the actual effect of this amendment was to restrict the pay levels of employers. In practice, overtime premiums were not paid to employees in the discretionary labour system. In other words, such employees were paid for the work performed instead of the time they worked, which has been referred to as a 'piece rate' payment.

Consequences of Shift in HRM from People to Performance Oriented

Recently, more and more firms have introduced the performance oriented HRM. When the Japan Management Association (JMA) sent questionnaires about the performance oriented HRM to approximately seven thousand major companies in 2004, they got replies from one thousand ninety eight companies (JMA 2005). The survey results showed that although about 80 per cent of the respondent companies had introduced the performance oriented HRM system, a majority were not able to get the anticipated favourable outcomes. According to the survey, more than 70 per cent of the companies that introduced the system were in fact reviewing the system to ascertain why the performance oriented HRM did not work well. The survey findings revealed the performance oriented HRM system had four significant problems.

The most serious problem was that the senior management did not adequately explain the purpose of introducing the system. In fact, what the employers publicly stated was completely different from what they intended. They publicly stated that the system was introduced for organisational competitiveness, and that an employee who worked hard should be rewarded based on the performance of his or her work. What employees actually intended, however, was to change the personnel cost from fixed costs to variable costs. In other words, the employers were not open about the public purpose for introducing the new performance oriented HRM system.

Secondly, the management by objective (MBO) system had inherent systematic problems. At the heart of a MBO system is a performance appraisal framework in which an employee is evaluated based on how much he or she will have achieved in terms of the objective criteria that are established at the beginning of the evaluation period, but the achieved outcomes do not necessarily link to the extent of 'value added' company achievements. In fact, staff in a back office of an accounting section may do an excellent job, but cannot earn any value added in markets as the amount of 'added value' produced is determined in the markets where those goods or services are traded. The monetary amount of the 'added value' realised in the market is equivalent to the amount left in subtracting the input value from the price of goods or service realised in the markets. The price of the goods or service is determined depending on the balance of supply and demand, and not necessarily linked directly to the excellence of the jobs that workers have done.

Some other problems in the MBO system are evident. For one thing, when an objective is assigned to each employee, the content of each job is determined by paraphrasing an organisational goal step by step. It is a difficult task, however, to break down an organisational goal to a worker's level without impairing the congruence between them. In addition, given specific objective, an employee tends not to do additional activities than those described in the specific objective. Furthermore, people were reluctant to help others, since the evaluation of an employee depends on his or her individual performance. As a result, these problems in the MBO system lowered the morale of the work team.

The third problem in a performance oriented HRM system existed in the evaluation process. The most important things in an evaluation process are fairness and the consent of the workers to be evaluated. An absolute evaluation, instead of a relative evaluation, is indispensable to evaluate employees fairly, obtain their consent and keep them committed to the organisation. The employers, however, evaluated the employees relatively. The Japanese employers generally set up roughly four or five ranks in evaluation and determined the proportion of each level in advance. Thus, employers evaluated the employees in accordance with such predetermined proportions. The reason why employers predetermined the proportions and evaluated workers relatively was that the funds to be distributed to them were subject to the firms' poor performances. As a result some employees could not get acceptable evaluations for good work performance, and hence, not enough pay, and consequently, these workers lost their enthusiasm for their jobs and expressed lower commitment to the company. Another problem, related to the evaluation process, was that some managerial people could not evaluate their subordinates appropriately because of they lacked evaluation experience.

The fourth problem in the performance oriented HRM system was the extinguishment of informal opportunities for education and training. In the successful three decades when human resources were managed on a seniority basis, elderly employees educated and trained younger people on the job. The elderly people did not have to worry about the fact that their junior fellow would later replace them. Since the treatment of people in companies began to be based on the performance of their work, most elderly people came to think that younger staff in the same company were rivals with whom to compete, as the younger staff had the potential to be paid more and replace them some day. Such anxieties kept the elderly people from educating and training younger people. As a result, the transfer of internal knowledge, technology and expertise, specific to the firm, was restricted.

CONCLUSION

Japanese firms are compelled to compete in global markets. Severe competition in the global markets means that participants are forced to accept the low market rate of returns and high risks of the markets' growth. The issue of how to manage their human resources in the global competition age is a salient challenge for Japanese management.

In the successful three decades, the domestic and foreign market had been continuously growing. In that period, Japanese employers provided long term employment and paid employees on a seniority basis, which drove employees to work hard. Growing markets enabled the employers to make a benevolent cycle in which increased pay based on good firm performance led to high commitment by employees, and in turn, this high commitment led to more pay based on the good performances of firms. In fact, this benevolent cycle, however, just depended on a continuous expansion of markets. Therefore, with the collapse of the 'bubble economy' in the beginning of the 1990s, these traditional HRM arrangements required transformation.

A demise of the steady growing market meant an exhaustion of the available funds for distribution. Consequently, Japanese employers introduced the performance oriented HRM system in which they paid more money to those who contributed more to the firms and paid less to those who did less. The Japanese employers naively believed that the principle to pay more for a good job and less for a poor job should work well to motivate employees. Their expectation, however, was completely unfounded. The issue that they should have learnt from the previous fifteen years of workplace experience was not understood. Indeed, a majority of Japanese employees worked hard and performed their jobs well, but most of them were not evaluated proficiently and not paid accordingly to their performance, because the number of the employees to be rated excellently was limited. As a result, most of employees lost their enthusiasm for their jobs and the company performance worsened. In other words, the benevolent cycle in the past successful three decades turned into a vicious cycle in the following fifteen years.

The relative evaluation for employees was certainly one of the factors that prevented the performance oriented HRM from creating another benevolent cycle. Nonetheless, the most important reason why the performance oriented HRM system had a functional failure was that the employers transferred market risk to the employees. Many employers linked the funds to pay to employees as bonuses (lump sum payment) to the performance of the firms. In fact, some employers changed the proportion of excellent employees according to the firm's performance, and other employers paid employees directly based on their contribution to the performance of firms. The linkage between a firm's performance and the employee's wage meant that employees as well as stockholders and corporate managers had to take their share of risk of a company's performance. However, agency theory explains that an employee, who usually is risk averse, would not take share of risk because a risk averter exerts less effort and performs less if risks are imposed on him or her (Milgrom & Roberts 1992).

Additionally, Japanese employers downsized surplus manpower concomitantly with introduction of a pay for performance scheme. Some employers dismissed people based on their job performance. As a result, employees were exposed to two kinds of risks: the income variable risk and the unemployment risk. Employees were forced to work hard for the fear that they might be paid less next time, or they might be fired some day. The employees left in the firms who luckily survived downsizing could not help, but undertake the work of others who quit their jobs. Currently, many overworked Japanese employees are exhausted and hate the performance oriented HRM system. Most workers cannot work comfortably, efficiently and effectively under the fear of unemployment and sudden reduction of wage.

Two hypotheses are proposed. First, Japanese employers adopted a new type of HR initiative with the expectation that these frameworks would lead to more favourable outcomes. Second, their decision to change the HRM system from people oriented to performance oriented was theoretically justified, but poorly operated. Judging from the observations and analyses so far, a reasonable conclusion is that the Japanese employers embraced a system that did not realise their desired objectives.

A performance oriented HRM system was less compatible with Japanese people or a Japanese organisation. The introduced performance oriented HRM system threatened employees into hard work with the exposure to the risks of unemployment and sudden reduction of salary. A system like this is unlikely to either promote the institutional cohesiveness of the group or develop organisational skills. It follows that the Japanese firms are likely to consider changing the HRM from people oriented to job oriented in the future, although this change might be the result of elimination of an unpopular scheme, there are reasons that are more positive. A reason why Japanese management may inevitably change the HRM system to job oriented is that such an arrangement has the potential to provide fairer and clearer criterion to the management of human resources in the global labour market.

Motivating employees is a major challenge for contemporary Japanese managers. Japanese employees now are frightened by exposure to HRM systems with a high risk of dismissal and avenues for payroll trimming. Moreover, in the current Japanese economic climate job security is highly valued. If the employers promise to secure employment, most employees are likely to work very hard for the company. While job security can be a great incentive to make majority of employees committed to their work, what can be an incentive to motivate a few super

performers? Although money can be an incentive, it is just one necessary condition but it is not sufficient reason to make employees committed to their work. Most employees need and appreciate money, but they will not work just for money. Many employees, especially younger employees who will forge the future of firms, expect to get a feeling of accomplishment or fulfilment through jobs well done. Such organisational members long for a solid job through which they can develop themselves. Therefore, the freedom or power to choose a job they want to do can be a greater incentive for those who perform an excellent job. Traditionally, many Japanese people work to get an intrinsic value of work as well as money. Such people are very happy to work enthusiastically if they can make themselves fulfilled through working even if their remuneration is small. The impending challenge for the Japanese manager is how to champion a balance of employer expectations with organisational exigencies.

AUTHOR

Dr. Tetsuhiro Kishita is a doctor of economics and an associate professor in the Faculty of Business, Ryukoku University, Kyoto, Japan, where he lectures in Asian Business. He has published two books, written over 30 articles in Japanese or English. His current research involves incentive schemes, corporate governance and business histories in Asian countries.

E-mail: kishita@biz.ryukoku.ac.jp

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