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## **CHANGES IN JAPANESE HUMAN RESOURCE MANAGEMENT SYSTEM PART I: CHANGES IN THE POST-WAR ERA**

***Abstract:** Lifetime employment, seniority system, Ringi system of decision making, and company trade unions are considered the typical characteristics or features of the traditional Japanese approach to management. In reality, majority of these features are related to human resource management practice in Japan. The paper deals with changes in Japanese management practice in both the post-war era and the lost ten years' era. The post-war era includes about three decades since the 1950's till the end of 1980's. Period of the 1990's till the beginning of the 21st century is regarded the lost ten years' era in Japan. It makes sense to separate these periods as large industrial Japanese companies operated in different business environments in both periods. Changes that occurred in the Japanese management practice during both periods, of course, reflected these differences. Accordingly, the paper is published in two parts. The first part deals with changes in the post-war era.*

***Key words:** American management, human resource management, Japanese management, kanji, management theory, management practice, Ringi procedure*

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### **Changes during and after the Lost Ten Years' Era**

The lost ten years' era is a name frequently used for describing the Japanese economy development in 1990's. The adjective "lost" is aimed to express the stagnation of the Japanese economy during that period. The financial sector's loan policy is considered the main reason which caused the economy to stagnate. Along with the loan crisis, there were some other factors such as stagnating domestic demand in Japan that destabilized the business environment at that time. There could be a number of reasons for the domestic demand stagnation but in the case of Japan the declining birthrate is considered the most important cause.

A declining birthrate as a trend of demographic development is closely associated with human resource management and employment practices, as its consequence is a decreasing size of the workforce. The size of the workforce in Japan, which in general means the country's working-age population, began to fall in 1996 and slightly continues till today. Human resource management systems in large Japanese industrial companies have to reflect the demographic development trends in their employment practice and the human resource management policy.

The beginning of the lost ten years' era in Japan more or less coincides with the beginning of what is now known as the globalization process. Since the Japanese economy found itself in trouble at that time, some experts believe that large Japanese industrial companies "overslept" the incoming globalization. At the same time, it is believed that the Japanese approach to management after that lost its prestige – at least to some extent. Because of that, discussions about necessary changes and a more flexible model started. However, the Japanese economy has sustained its growth since the beginning of 2002, while the sustainable growth is the result of both changes that occurred during the lost ten years' era and the ongoing changes.

In the following text we will briefly describe the most typical changes in the Japanese approach to management, human resource management and employment practices that occurred during that period. In view of the changes in the Japanese business environment, innovations in the field of human resource management and employment practices will be described in the context of the globalization process.

The Japanese traditional model of management as an integral part of the Japanese version of capitalism ran into trouble at the beginning of the lost ten years' era – i.e. at the beginning of the 1990's. Large Japanese industrial companies realized that a traditional approach to management no longer fitted the changing environment requirements. After that, the Japanese government introduced political and corporate reforms that led to the economy revival. As an integral part of these reforms, the Japanese commercial code was amended in 2002. According to the amendment, Japanese companies were given a choice between the traditional Japanese model and an alternative model of corporate governance.

The traditional Japanese model involves a compulsory audit required by the statute. An alternative model requires separate audit, remuneration and nomination committees with majority of outside directors. The alternative model is in reality a Japanese version of the American approach. Because of this, it is clear that reforms were aimed to give large Japanese industrial companies a chance to adopt the American approach to corporate governance<sup>7</sup>. A lot of large Japanese industrial companies have taken the advantage and tried to adopt the Anglo-Saxon model as the American approach is often referred to.

This change in the Japanese business environment is considered very significant, even if it is clear that the Japanese model could not be simply replaced with the American one for a well-known main reason – the different environment

in Japan. Apart from this, there are business leaders in Japan who traditionally oppose such changes, especially after the revival and the sustainable growth of the economy since 2002. To avoid difficulties, large Japanese industrial companies try to adopt the American model but in a Japanese way. They try to find a compromise between the traditional industrial paternalism in the company as a social institution and profit-making company that serves to satisfy and meet the expectations and interests of shareholders. This compromise results in a combined model that includes elements of both approaches – the traditional Japanese and the American ones.

The combined model in practice means that large Japanese industrial companies try to *change* their traditional model but *not replace* it with the American one. While doing so, company management should decide what traditional attributes should be kept in order to fit the Japanese environment; at the same time it should find the way to make the combined model more compatible with the American approach. Of course, it is a challenging task as the limits of how far they can move are unknown. Consequently, large Japanese industrial companies that are considered progressive owing to their efforts to change their traditional approach to management and bring it closer to the American approach have retained many traditional attributes. At the same time, these companies have introduced several changes that are clearly reflected in their human resource management policies and employment practices. To some extent, these changes affected almost all “traditional pillars” of the Japanese management such as lifetime employment practice, seniority system of compensation and career management, the trade union’s role in the company management, as well as the Ringi system of decision making. The most significant changes in the field of human resource management and employment practices that are considered the result of the Japanese – Anglo-Saxon combined model could be specified as follows:

- First of all, the labour market in Japan has become more flexible. In reality, it is a result of changes in the lifetime employment practice. At the beginning of the lost ten years’ era, large Japanese industrial organizations with their long history of lifetime employment practice, i.e. which involves permanent or regular and mid-career or non-regular employees, have solved their economic difficulties by combining two main measures. One measure was to cut wages and salaries of regular employees; the other was the “break” in hiring of new permanent employees. Instead, in order to keep the necessary number of employees, they started to hire more non-regular employees. It was the way to cut costs, since we already know that according to the seniority system of compensation non-regular employees are hired for a lower pay than the regular employees. The labour market became more flexible as the total number of non-regular employees has increased. The increased number of non-regular employees means a higher workforce mobility.
- There are two main consequences of these measures that could be observed today. First, the “break” in hiring of new permanent employees in the 1990’s gave

birth to a young generation of non-regular employees, who in reality had no chance to get lifetime employment, even they were willing to get it. According to Japanese newspaper Asahi Shinbun, this generation of young people is a “lost generation” because during the lost ten years’ era they lost the chance to get lifetime employment and become regular employees in large Japanese industrial companies. As we can remember, the lifetime employment practice is offered exclusively to fresh graduates. Second, there is another category of the workforce in Japan today that is known under the name *freeter*. The origin of this word is unknown but it sounds as a mixture of Japanese and English pronunciation. It is probably a kind of a Jinglish word as some Americans call the English language that is spoken in Japan. The word *freeter* refers to a person who has no specific occupation, and when occasionally employed on a part-time basis they seldom work for the same employer. Freeters belong to the “lost generation” as most of them are young people but their lifestyle is about their private life preferences rather than about lifetime employment, company or loyalty.

- Freeters are in contrast with the *dankai* generation, i.e. the post-war baby-boom generation. In the Japanese language, the word *dankai* literally means “a big agglomerate of different things”. It refers to the post-war generation of people who personally experienced a very difficult post-war period in Japan; people who worked hard and loyal employees; people who have built the second biggest economy in the world, but also people who remember Hippies and the Beatles. It is a generation of the people that have just now reached their retirement age, and as they believe, they have no followers in the young generation, as it is a “lost generation”. Besides this, some young people in Japan do not wish to stay in one company throughout their lives. They prefer to get experiences from more companies including the foreign ones.

- *Seika-Shugi* human resource management system in large Japanese industrial companies is a new system that is aimed to improve the traditional seniority system of compensation and career management. This system was introduced in some companies during last ten or fifteen years, and it is more performance-oriented than the traditional seniority system. The word “more” should be stressed because it is not the same system of compensation that is known, for example, in American companies. *Seika-Shugi* system is a step towards Western compensation systems. Under this system, performance assessment and rewards are based on business results and individual performance rather than on seniority. However, Japanese human resource managers do not usually believe that performance-based pay is the most important change that their traditional compensation system requires. They feel that such a dramatic change in the compensation system would harm the harmony in the company. Because of this, they try to keep the performance-based elements in the compensation system’s structure rather small in comparison with the Western systems. Instead, they focus on talent management, although it is clear that talent management and performance-based compensation are not identical. They believe it is more important to make sure that each talent in the company is assigned to the

most appropriate position according to their personal skills. But as we are familiar with the traditional seniority system, this does not seem to be a brand new approach in Japanese human resource management practice. We can remember that one of the primary rotation's main objectives under the Japanese traditional system was to find the most suitable initial job for each new recruit.

- Japanese large industrial companies started to hire executives from the external resources – outside directors. There are three issues that should be mentioned in this context. First, some Japanese large industrial companies have moved towards the American model, but it should be stressed that it does not involve an aggressive hiring of executives from external resources. It is now estimated that about 30% of Japanese large industrial companies have outside directors. Second, the meaning of the term “outside director” in Japan slightly differs from that in the West. Japanese outside directors come most of all from associated companies inside the keiretsu or similar groups of companies. They are not real outside directors in the Western's sense of the word. Third, large Japanese industrial companies that have moved towards the American model have retained many of the traditional Japanese management approach characteristics. Put it altogether, there are large industrial companies that have slightly shifted towards the American model but still retain many traditional Japanese characteristics; at the same time there are over 50% of such companies that have no single outside director. A good example for this group of large companies would be the Toyota Motors company.

In order to get the brief characteristic of changes in the Japanese business environment during the lost ten years' era completed, Japanese trade unions should be mentioned, too. Beside the lifetime employment system, seniority system, Ringi system of decision making, the fourth typical feature of the Japanese traditional management – the structure of Japanese trade unions has been changed during the last ten to fifteen years as well. Until the 1980's, there were four main labour federations in Japan that represented Japanese trade unions. By the end of the 1980's they merged, and the National Federation of Private Sector Unions known as RENGO was established in 1989. With RENGO formation the unification of labour unions in Japan has been achieved. It was a long-year dream of Japanese labour union movement, as it is considered a way to strengthening their position.

As for today, Japanese trade union organizations have a three-level hierarchical structure. At the bottom there are enterprise-based unions that monitor corporate activities, provide services to their members, and negotiate such issues as an improvement of working conditions. In the middle of a hierarchy, there are industrial federations composed of enterprise-based unions within the same industry. These deal with the trade union issues related to the entire industry. At the top, there is the RENGO national centre representing the largest trade union confederation in Japan. Because the national centre is made up of industrial federations, it combines the power of individual trade unions.

RENGO is a powerful trade union confederation that can influence also issues related to human resource management and employment practices in Japanese industrial companies. For example, regarding changes in the lifetime employment practice, RENGO suggests that in order to promote development of capable staff and stable employment, *corporate management should not sacrifice lifetime employment* to a flexible labour market. RENGO is also critical of changes in compensation systems and proposes that compensation systems should incorporate both a fair price for work done and securing a stable cost of living. RENGO goes even further by proposing specific wage policy initiatives. RENGO proposals in the field of employee compensation and human resource management in general are heading more or less to the traditional Japanese management systems rather than to the Anglo–Saxon model.

Finally, regarding changes in the traditional Japanese approach to management, human resource management and employment practices, we come to conclusion that large Japanese industrial companies have recognized the importance of changes in the business environment and try to adjust their systems of management to the new requirements. But we should remember that such changes are challenging for a number of reasons.

First of all, we should be aware of the fact that not only in Japan but almost everywhere it is very unlikely for a national character and culture to change dramatically within a decade. Both of them are the result of historical developments taking hundreds and thousands of years. Of course, changes in the management systems cannot take so long; instead they should reflect the changes in environments, both internal and external or global ones. Frequent changes are typical of globalization era; however, these changes are usually not so profound as to bring about a dramatic change in the national character and culture, and change it in a short period of time in the country of such unique history as Japan undoubtedly is. In addition, Western scholars and managers usually suggest and expect such changes in the traditional Japanese system of management that would bring it closer to the Western practices. This seems to be quite unrealistic because such expectations in reality mean the replacement of the system. There are no good reasons to believe that Japanese business leaders are interested in such changes.

Second, changes in the traditional Japanese management system follow the requirements or changes in national and global environments. However, Western companies are in a very similar situation as they have to adjust their management systems to become or stay competitive in global business environment. Because Japanese and Western traditional management systems differ from each other, it would be naïve to expect that both need the same changes to become competitive in global markets. Likewise, it seems naïve to expect that a few Western executives hired by some large Japanese industrial companies could dramatically change the traditional Japanese management system. Instead, it would be more realistic to expect that it will be Japanese business leaders who will perform the role of the “change agents”.

## Conclusion

As for today, in the big business of Japan in general, it is difficult to secure its regular employment and lifetime employment. This is due to the increases in non-regular employment. Japanese business-made products tend to be pushed out by the products made in the low-wage countries; and there is an urgent need for Japanese businesses to reduce operating labour costs. At the same time, Japanese businesses move to foreign countries for the cost reduction and the market demand. They have transferred production and selling activities from Japan. As a result, employment opportunities are lost and non-regular employment increases. Moreover, the demand at home does not increase due to the falling birthrate in Japan. Because of the business performance depression, the increase in non-regular employees as well as in overseas production, business in Japan is conducted from a short-term viewpoint and achievement-centre evaluations, which are considered overseas habitual practices. This makes it even more difficult to maintain traditional Japanese management practices which emphasize permanent employment and education from long-term viewpoint.

On the other hand, in the General Election for the House of Representatives in summer 2009, Japanese citizens chose the Democratic Party in place of the Liberal Democratic Party (LDP), which had been in power for fifty years. The LDP political power tried to focus on the market principles and attempted to increase the market value of business, which is a response to the globalization trends. Democratic Party political power opposes the non-regular employment in the manufacturing industry and tries to strengthen restrictions on the companies. The Democratic Party and the posture of the Japanese government aim to recover Japanese traditions, culture, and – of course – the traditional Japanese management. Only the future can give an answer whether this is possible. Our role in the West will probably remain the same – we should be careful students who understand what the Japanese approach to management is about and what kind of changes occur in this system.

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**End Notes****Notes <sup>1-6</sup> refer to part I of this paper.**

<sup>1</sup> It sounds ironic but it is true. Both Christianity and firearms were introduced to Japan at the same time (see: p. 179, line 12 from the bottom, after “there”).

<sup>2</sup> Mentioned typical specific features of the Japanese approach to management, i.e. lifetime employment, seniority system, ringi system of decision making, and Japanese trade unions were usually considered the strong points (see: p. 182, line 11 from the bottom, after “are”).

<sup>3</sup> Staffing the board of directors in large Japanese industrial organizations with full-time executives was a post-war practice. Boards of directors in former Zaibatsu



of the pre-war era included a substantial number of outside directors who were representatives of large stockholders or Zaibatsu families. These directors did not perform operational activities and had no day-to-day managerial responsibilities. As for today, there are similar attempts to get the board of directors staffed also with the “outsiders”. This is considered a profound change in Japanese management inspired by Western management practices. As we can see, it is not a new idea since it was a common practice in the pre-war Zaibatsu already (see: p. 183, line 11 from the bottom, after “organization”).

<sup>4</sup> In general, the decade of 1960’s was exceptional from a global point of view. This decade influenced the mankind history in both positive and negative aspects. To mention just a few of them: it was a decade of the Beatles, the Hippies movement, but also that of assassination of John Fitzgerald Kennedy, the US president in 1963; the era of the Cuban crisis that brought the world to the edge of nuclear war, the war in Vietnam, riots that occurred in one of the most prestigious higher education institution – the Sorbonne University; Civil Rights Act in 1964, the assassination of Martin Luther King, Jr. in 1968; as well as crash of the Prague Spring – the renaissance of Czechoslovakia’s attempt at democracy crashed by the Warsaw Pact occupation forces led by the USSR (see: p. 183, line 9 from the bottom, after “1960’s”).

<sup>5</sup> Former Matsushita Electric (now Panasonic) was an exception as its divisional organizational structure was introduced almost two decades earlier (see: see p. 183, line 6 from the bottom, after “companies”).

<sup>6</sup> Japan Productivity Center (JPC) is a non-for-profit and non-government institution established in 1955 to promote the productivity increase in Japan. For years it was the only institution that offered the management development courses for managers in Japan. By its activities, this institution was a big contributor to both the theory and management practice development in Japan (see: p. 188, line 21 from the bottom, after “Center”).

<sup>7</sup> As we are familiar with the traditional Japanese approach to management as well as with its history, we already know that this is not the first attempt to borrow the Western but most of all the American approach. Similar attempts were known in the early Meiji period and after the end of World Wars I and II. We also remember that all such attempts in the past more or less failed.