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GENERAL SURVEY

2001 Unemployment Rate Exceeds Five Percent

On January 29, the Ministry of Public Management, Home Affairs, Posts and Telecommunications released the average unemployment rate for 2001, together with the results of the December *Labour Force Survey*. The annual average unemployment in 2001 exceeded five percent for the first time since commencement of the survey, with the number of unemployed totalling a record high of 3.4 million. The monthly unemployment rate also marked a new record, 5.5 percent in December 2001.

The survey showed that the annual average number of workers in 2001 declined by 340,000 people to 64.12 million, the fourth consecutive annual drop. The magnitude of the decline was greater than in the previous year, when it was 160,000. The number of male workers declined by 340,000, while that of female workers remained the same as the previous year. Of all workers, the number of employees was 53.69 million, and the number of self-employed and family workers was 10.18 million. In 2001, the two types of workers represented 83.7 percent and 15.9 percent of the total respectively, compared with 78.5 percent and 21.2 percent in 1991, illustrating the tendency for the number of self-employed workers to decrease.

By industry, workers in the service sector accounted for 28 percent (17.68 million) of all workers, followed by wholesale, retail, and eating and drinking establishments at 23 percent (14.73 million), manufacturing at 20 percent (12.84 million), and construction at 10 percent (6.32 million). Conspicuous here is the substantial expansion of the service sector and the shrinking of the manufacturing and construction sectors.

Among the 53.31 million employees engaged in the non-agricultural sector (an increase of 90,000 from the previous year), the proportion of regular employees declined whereas that of temporary employees and day laborers increased. By size of enterprise (excluding the public sector), 17.29 million workers (32%) were in firms with one to 29 employees, 17.84 million (33%) in firms with 30 to 499 employees, and 12.48 million (23%) in firms with 500 or more employees. Of the three categories, firms with 500 or more employees alone saw a decrease in the number of employees (a drop of 260,000), illustrating the dismal employment situation among large firms.

Turning to the unemployment situation, the number of jobless people increased by 200,000 from the previous year to 3.4 million (2.09 million males and

1.31 million females). The 2001 annual average unemployment rate stood at five percent (5.2% for males and 4.7% for females), the worst figure yet. By age, the unemployment rate was the highest, 10.4 percent, among males aged 15 to 24, followed by seven percent among males aged 55 to 64. Among female unemployed workers, those aged 15 to 24 accounted for the largest proportion, 8.7 percent, followed by those 25 to 34 (6.9%). Thus the tendency for high unemployment among young workers and middle-aged and older male workers persisted. Concerning families, 930,000 unemployed people were heads of households and 420,000 were spouses of household heads, 1.54 million were other family members, and 510,000 were single householders, showing that just under 30 percent of unemployed people as a whole were heads of households.

A comparison of the reasons given for needing to find jobs in 2001 and 10 years before, in 1991, reveals that the proportion of unemployed people answering "as a result of my quitting a job involuntarily" increased from 23 percent to 31 percent, totalling 1.06 million; the proportion of those answering "as a result of my quitting a job voluntarily" declined from 40 percent to 35 percent (1.18 million); the proportion of unemployed answering "no suitable vacancies since graduation" increased from four to five percent (170,000); and the proportion of those choosing "other reasons" dropped from 27 to 25 percent (850,000). These changes clearly indicate a trend towards less voluntary and more involuntary unemployment.

The *Special Labour Force Survey* conducted every February detailed the change in the length of time people were unemployed between 1991 and 2001. The percent of those unemployed for "less than three months" dropped from 49.3 percent in 1991 to 39.3 percent last year; the figure for those out of work for "three months or more, but less than six months" increased 0.5 percent to 14.5 percent; those unemployed "six months or more, but less than a year" also grew, from 18.4 percent in 1991 to 19.5 percent in 2001; and the number of those responding they had been unemployed for "one year or longer" jumped from 17.6 percent to 26.1 percent. While the proportion suffering short-term unemployment of less than three months declined by 10 percentage points, the proportion suffering long-term unemployment of one year or more increased by close to nine percentage points, clearly indicating the current state of structural unemployment due to labor supply-and-demand mismatches.

WORKING CONDITIONS AND THE LABOR MARKET

Number of Dispatched Workers in FY 2000 Jumps 30 Percent from Previous Year

According to a compilation of business reports from worker dispatching businesses from the Ministry of Health, Labour and Welfare at the end of fiscal 2001, the number of dispatched workers in fiscal 2000 increased by 30 percent over the previous fiscal year to

Statistical Aspect

Recent Labor Economy Indices

	January 2002	February 2002	Change from previous year (February)
Labor force	6,611 (10 thousand)	6,604 (10 thousand)	-66 (10 thousand)
Employed	6,362 (")	6,371 (")	-106 (")
Employees	5,321 (")	5,321 (")	-76 (")
Unemployed	355 (")	357 (")	38 (")
Unemployment rate	5.3%	5.3%	0.6 (%)
Active opening rate	0.51	0.50	-0.14
Total hours worked	138.4 (hours)	p151.5 (hours)	-0.1 (hours)
Total wages of regular employees	(¥ thousand) 296.9	(¥ thousand) p282.5	(¥ thousand) p-0.6

Notes: p: Preliminary figures

US\$1=¥133 (April 1, 2002)

Source: Ministry of Public Management, Home Affairs, Posts and Telecommunications, *Rōdōryoku Chōsa* (Labour Force Survey); Ministry of Health, Labour and Welfare, *Shokugyō Antei Gyōmu Tōkei* (Report on Employment Service), *Maitsuki Kinrō Tōkei* (Monthly Labour Survey).

approximately 1.39 million. Ever since the implementation of the Worker Dispatching Law in 1986, the number of dispatched workers has grown, and this sharp increase of 30 percent shows the active use of such workers by enterprises which are simultaneously cutting back on the number of regular employees.

The report, a compilation of reports submitted to the ministry by 10,330 dispatching agencies, shows that the total number of workers actually dispatched to workplaces in fiscal 2000 was 1,386,364. Of these, “registered” workers, those who are employed by dispatching agencies only when a job is available, totalled 1,250,913, and “regular-base” dispatched workers, those employed continuously by agencies, totalled 135,451.

By job type, 44.8 percent of the “registered” workers operated office equipment, followed by 13.3 percent in financial clerical field, and 7.6 percent in filing. Of the “regular-base” workers, 34.1 percent were engaged in software development, 28.0 percent in machine design, and 19.2 percent in operating office equipment.

The number of firms accepting dispatched staff increased by 10.9 percent from the previous fiscal year

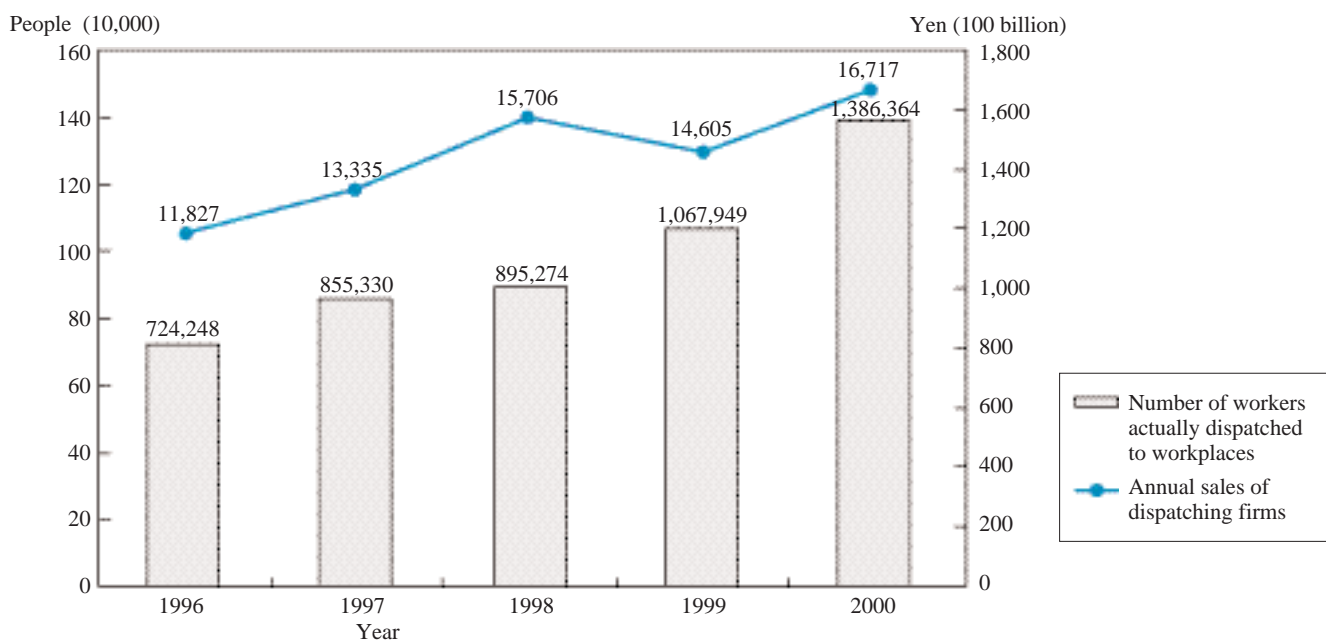
to about 290,000. Of that figure, 269,321 firms made use of “registered” dispatched workers and 23,896 firms “regular-base” workers. Annual sales totalled ¥1.67 trillion, a record high along with the number of firms using dispatched workers.

Fees paid by firms to dispatching agencies averaged ¥16,755 for eight working hours for “registered” workers (a 0.04% drop from the previous fiscal year), and ¥25,100 for “regular-base” workers (a 1.8% drop). By job type, hiring an “announcer” required a firm to pay ¥26,390 for eight hours to the dispatching agency, followed by “interpreter, translator or stenographer” (¥24,037), “secretary” (¥16,875), “financial clerical work” (¥15,413), “operator of office equipment” (¥14,950), “worker engaged in filing documents” (¥14,392), “office cleaner” (¥12,697), and so on. Such costs were higher in many cases involving “regular-base” dispatched workers: “sales engineer” (¥34,900), “software developer” (¥31,162), “worker engaged in research and development” (¥31,530), and so on.

Concerning the job contract period, 70.9 percent of “registered” dispatched workers were contracted for “less than three months,” with 90 percent contracted for “less than six months.” On the other hand, 25.3 percent

Statistical Aspect

Trends in the Number of Dispatched Workers and Annual Sales of Dispatching Firms



Source: Ministry of Health, Labour and Welfare, *Business Reports from Worker Dispatching Businesses*.

of “regular-base” dispatched workers were contracted for “less than three months,” 10.4 percent for “three months or more but less than six months,” 12.9 percent for “six months or more but less than nine months,” 30.8 percent for “nine months or more but less than 12 months,” and 20.6 percent fell into another category, showing the wide disparity of contract periods among such workers.

LABOR-MANAGEMENT RELATIONS

Jichiro Releases Final Report on Series of Scandals

On January 31 and February 1, Jichiro (All Japan Prefectural and Municipal Workers’ Union) held a special conference in Tokyo to finalize a report on an internal investigation concerning a series of scandals that have arisen since the end of last September, and to announce its policies for rebuilding the organization. Jichiro represents about one million workers employed

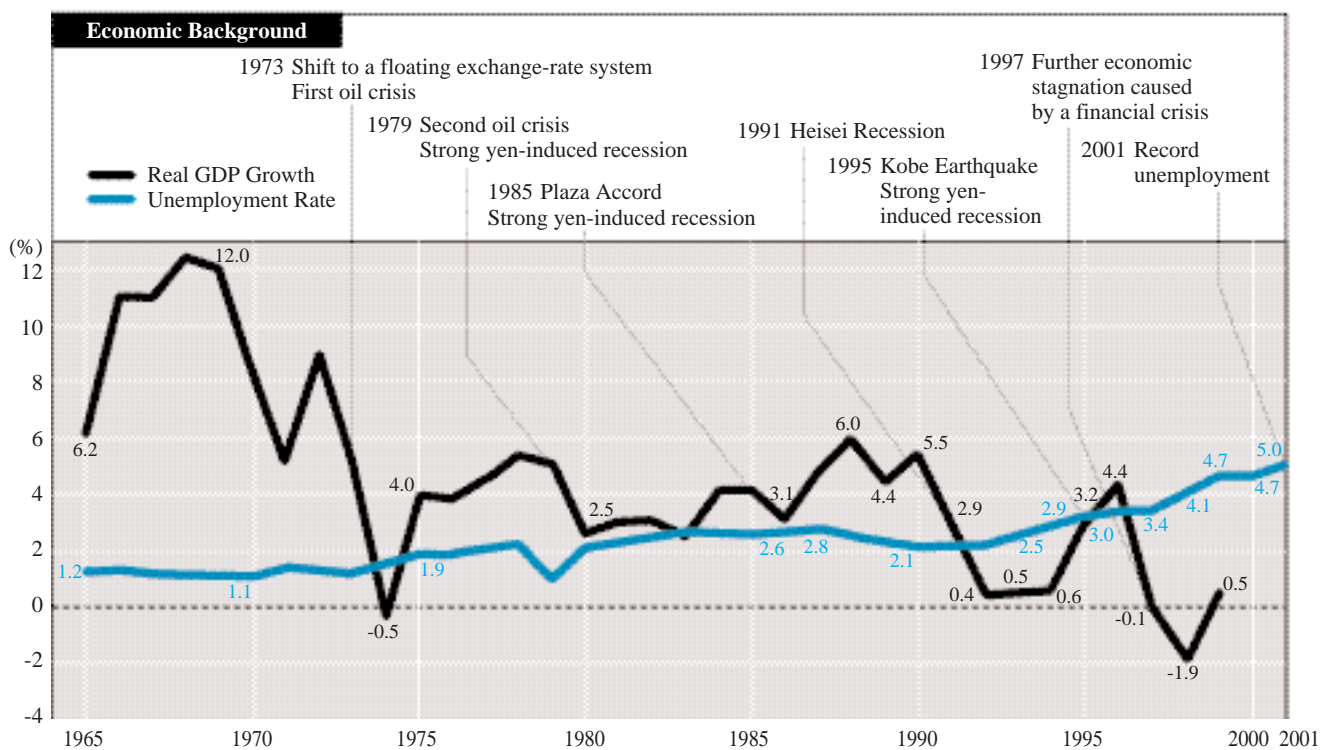
in prefectural and municipal governments and affiliated public bodies across the country, making it the largest industry union in Japan.

The conference confirmed the resignation of five out of seven senior executives, including the president and general secretary, and elected a new executive with Katsumasa Kitaoka as president.

Jichiro had contracted with a life insurance company via an affiliate company (established in 1988 and liquidated in 1999) for the purpose of administering the welfare benefits of its union members. The first scandal was an alleged violation of the Corporate Tax Law involving a handling charge that should have been paid by the insurance company to the affiliate but was actually passed on to the headquarters of Jichiro. Also in October 2001, an executive director of an data processing company (annual turnover ¥3 billion) with financial backing from Jichiro was arrested on suspicion of embezzlement; he had also served as a special committee member of Jichiro. The subsequent

Statistical Aspect

Real GDP Growth and the Unemployment Rate



Sources: Economic Planning Agency, *National Accounts*; Statistics Bureau, Ministry of Public Management, Home Affairs, Posts and Telecommunications, 1999, *Labour Force Survey*.

investigation conducted by the Tokyo District Public Prosecutor's Office concerning cash flows at Jichiro headquarters revealed the existence of funds in irregular accounts, and of off-the-books debts amounting to ¥3.9 billion borrowed from financial institutions without the decision of the organization.

According to the Jichiro internal investigation, some ¥1.9 billion of the debt was directed toward lobbying activity during national elections and efforts to increase union membership. Jichiro explained that the need for large amounts of money to prepare for national elections was what first prompted the shady accounts. The remaining ¥2 billion or so in debt was borrowed from financial institutions to employ a management consultant to handle their assets with the goal of reducing or repaying existing debts, but it remains unclear whether he will be able to pay this back. Many of the off-the-book accounts (16 in all) opened since the 1980s were theoretically used to win new members in competition against Jichi-roren (National Federation of Prefectural and Municipal Workers' Unions). Jichi-roren split from Jichiro in opposition to joining Rengo (Japanese Trade Union Confederation), a national center which was formed in 1989 and currently has 7.3 million members. Jichi-roren instead affiliated with Zenroren (National Confederation of Trade Unions), another national center with one million members associated with the Communist Party.

The report of the internal investigation admits that these financial transactions were conducted by certain executives without the decision of the organization, and that the union has a permissive attitude towards its finances, allowing individuals to handle funds behind the scenes, with no monitoring against illegal activities.

The "Rebirth Program" that Jichiro decided on at the special conference places priority on the repayment of the ¥3.9 billion in debts immediately, using its regular funds (currently totalling ¥28 billion raised through the ¥200 monthly dues paid by each union member). These funds will be reimbursed within five years by claiming damage compensation against the people who engaged in the unlawful activities, cutting the salaries of union executives at headquarters (by 5 to 10%), and other means. In addition, the union is planning to decentralize the authority currently concentrated at its headquarters and disperse it to prefectural head offices in order to scrutinize those in charge and the union's financial operations. Also, changing the name of the organization, Jichiro (literally, labor unions of self-governing bodies), will be discussed.

Some Jichiro affiliates have withdrawn from the organization, and others are not forwarding membership fees. To regain the trust of affiliates and union members, and the faith of people in general, Jichiro will need to tackle many more tough tasks in the future.

PUBLIC POLICY

Local Governments Tackle Job Creation for High School Graduates

With the annual average unemployment rate marking a record high of five percent in 2001, unemployment among young people — astonishingly high at around 10 percent — is a serious concern from a long-term perspective. The rate of success in finding jobs (as of the end of November 2001) for high school students due to graduate in the spring of 2002 was a record low of 63.4 percent. In order to reverse such unemployment trends among young people, local governments have embarked on a new scheme to hire new high school graduates for a limited period by cutting back on the overtime worked by their staff members.

High school student job-hunting activities are normally coordinated by Public Employment Security Offices and high schools. Firms wishing to employ new graduates are required to submit job-offer documents to the office, and these are passed on to high schools. Students, on the other hand, with advice from their teachers select an offer from among those sent to the school, apply, then sit for the examination the firm conducts in September. Until recently, almost all students wishing to work after graduation were promised jobs, but the situation has changed in recent years: the number of job offers intended for high school graduates has been falling sharply; the ratio of the number of job openings to the number of young applicants stood at 0.98 as of the end of November 2001, resulting in the lowest rate of promised employment, 63.4 percent, since the commencement of the survey in 1987.

The deterioration of the job market for those who leave high school is attributable to the reduction in hiring of new graduates due to the current recession, and to a shift in the interest of firms towards university graduates and others with higher education. The rate of success in job hunting among university graduates (as of December 1, 2001) improved to 76.7 percent, 1.5 percentage points over the same period the previous year, realized at the expense of the job market for high school graduates.

The employment situation affecting high school graduates is much more severe in local areas where job offers are becoming scarce and the opportunities for part-time jobs are limited. It is regional governments in such areas that have taken action in hiring unemployed young people by cutting their own labor costs.

In Hyogo Prefecture, which was the center of the 1994 Kobe Earthquake, the prefectural government has been tackling the employment situation within the prefecture since the earthquake, and since 2000 has been conducting a program whereby the overtime of some 8,000 or so staff members is cut by five percent per year, and the ¥200 million saved is invested in hiring jobless young people. Other local governments see the program as a model.

Hokkaido, where the promised employment rate for high school graduates marked the second lowest figure (29.3%) after Okinawa Prefecture, is to adopt a similar program in fiscal 2002; it will cut the overtime of its civil servants by five percent, and employ some 150 young people under 20 years old as one-year temporary employees. The contract period is limited since the program is designed partly to offer a type of internship before actual job engagement.

Akita Prefecture is also planning to hire some 80 people under 29 years old for one year. Of the 80 vacancies, 44 posts will be offered exclusively to new high school graduates, who will engage in clerical work for four days a week, 30 hours in all, at prefectural offices while learning basic business skills and practices, including computer skills, by helping regular staff members.

With work-sharing drawing attention in the business world, this series of programs launched by local governments is attracting notice as a “public” version of work-sharing, in which public institutions, too, try to cope with employment issues affecting young people, particularly high school graduates.

Number of Consulting Cases Concerning Individual Labor Disputes Sharply Increased

During the three months from the implementation of the Law for Promoting the Resolution of Individual Labor Disputes in October 2001, the number of workers or employers using the “Comprehensive Labor Counselling Desks” dealing with individual labor disputes, which are located in 250 areas across the country, reached 20,000, an increase of 70 percent from the previous year, according to a Ministry of Health, Labour and Welfare survey. Roughly half of the cases were related to restructuring measures

undertaken by companies or dismissals, reflecting the harsh situation in the recent labor market. (Concerning the contents of the law, see the October 2001 issue of the *Japan Labour Bulletin*.)

According to the findings of the survey, the number of cases brought before Comprehensive Labor Counselling Desks totalled 121,330.

Of these, cases concerning individual labor disputes within the scope of civil procedure (such as dismissals and deterioration of working conditions which do not violate labor law) accounted for 20,470 cases. “Dismissals” accounted for the largest proportion, 29 percent, followed by “deterioration of working conditions such as wage cuts” (17%), “suggested retirement” (5%), “harassment and bullying at the workplace” (5%), “transferring to a related company, or reallocating to a different section” (3%), and “sexual harassment” (2%). Workers filed 82 percent of cases, with employers filing 12 percent. Of the former, regular employees accounted for 55 percent, part-timers or *arubaito* (side-job) workers 16 percent, and fixed-term contract workers and dispatched workers three percent each.

Of these cases, the number of disputes which did not see a resolution on the basis of voluntary discussion between labor and management but required the advice or guidance of the Director of the Local Prefectural Labour Bureau totalled 411. In all these cases, the applicants were workers, with 128 (31%) relating to “normal dismissals,” 47 (11%) relating to “dismissals for the purposes of reorganization,” and 26 (6%) “disciplinary dismissals.” Complaints concerning “deterioration of working conditions” totalled 50 cases (12%).

Of the 411 disputes, 354 cases were completed by December 2001 and were awaiting settlement; 154 cases (44%) received advice and 33 cases (9%) were given guidance, while 89 cases (25%) were withdrawn, and 45 cases (13%) faced “termination of support for dispute resolution,” which occurred when, for example, the facts of the case remained uncertain. Incidentally, 130 cases of the 354 completed cases have been settled.

In terms of the amount of time involved, “less than one month” accounted for 67 percent of the cases, “one month or longer but less than two months” for 20 percent, and “two months or longer but less than three months” for eight percent.

Of all the cases brought before the counselling desks (121,330), 308 called for conciliation by the “dispute adjustment committees,” which were newly established under the Law for Promoting the Resolution of Individual Labor Disputes. The

committees are composed of conciliation members including lawyers, professors, certified social insurance labor consultants, experts on human resource management, and others with experience in administration. Their aim is to reach an amicable resolution of disputes through fair judgment of the claims of both parties, and to offer proposals for solutions. Of 308 cases, 91 (30%) concerned “normal dismissals,” 29 (9%) “dismissals for the purposes of reorganization,” eight (3%) “disciplinary dismissals,” 50 (16%) “deterioration of working conditions,” 15 (5%) “transferring to a related company, or reallocating to a different section,” 19 (6%) “suggested retirement,” 22 (7%) “harassment or bullying at the workplace,” and 12 (4%) “sexual harassment.”

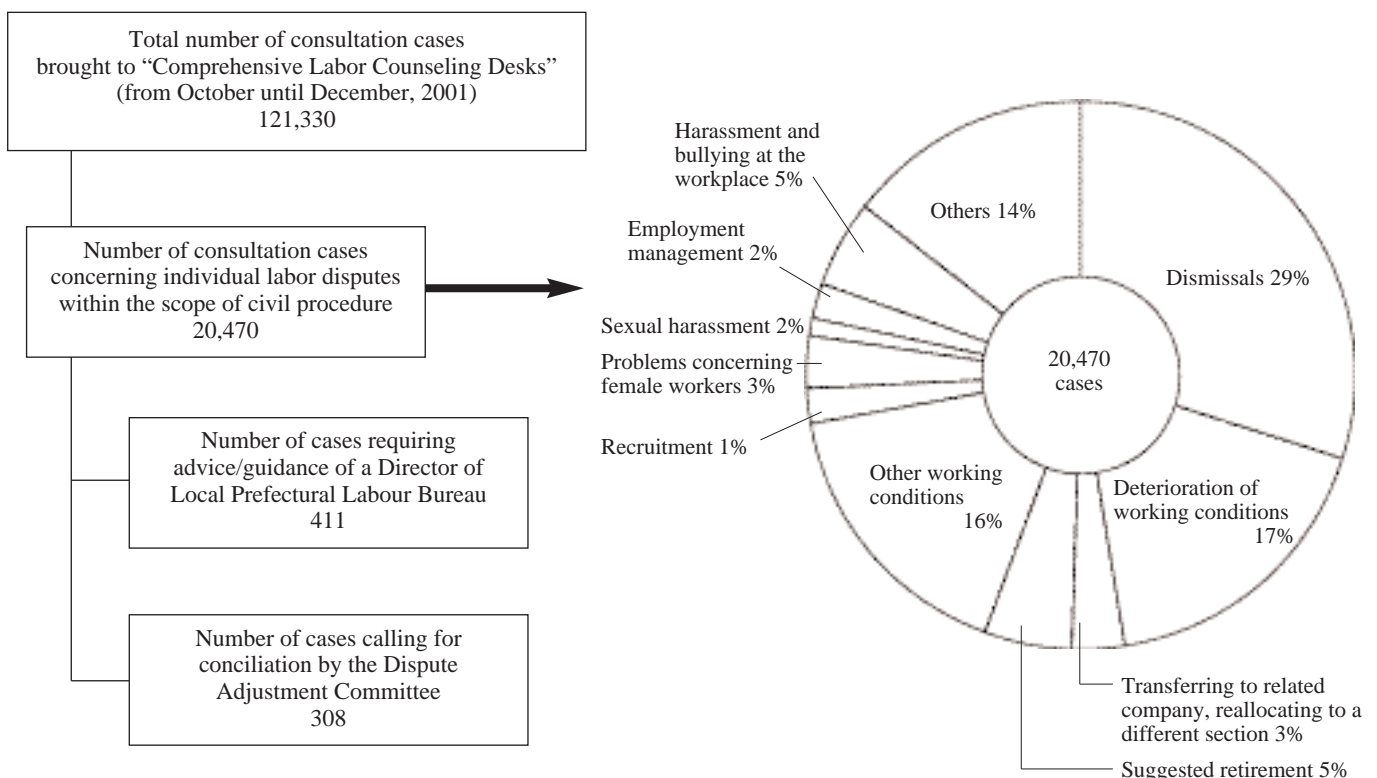
Of the cases handled by the conciliation committees, 147 saw completion of procedures; of these, 57 (39%) effected an agreement between the parties involved, the applications in 41 cases (28%) were withdrawn, and conciliation on 44 cases (30%) was terminated halfway due to, for example, the

absence of one of the parties involved.

Concerning the time required, 83 percent of the cases saw resolution in “less than one month,” 16 percent in “one month or longer but less than two months,” and one percent in “two months or longer but less than three months.”

The new scheme seems to be handling well a sharp increase in the number of individual labor disputes, particularly considering it has been only three months since the law was implemented. However, the system still poses potential problems, such as the lack of authority to compel both parties to the conciliation table, the quality of those who are actually engaged in the resolution of disputes, and so on. It will be necessary to monitor the system with an eye toward necessary revisions during implementation of the scheme. (Concerning labor-management disputes, in particular the handling of individual disputes, see the June 1996, October 2000, and June, September and October 2001 issues of the *Japan Labor Bulletin*.)

Consultation Cases Concerning Individual Labor Disputes within the Scope of Civil Procedure



Pay Practices in Japanese Organizations: Changes and Non-changes

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1. Introduction

The serious decline of the Japanese economy and the worst unemployment rate since the end of World War II (5.3% in February) has produced a great deal of speculation among scholars and human resource management practitioners that the Japanese “lifetime employment system” may disappear. Indeed, there are signs everywhere indicating that Japanese employers are attempting to abandon this treasured principle. The number of atypical employees, such as part-time and contract employees, is increasing, and not a day goes by without a major employer announcing an employment reduction plan. There is no doubt that a serious change is in progress with regard to employment of core, full-time workers.

Yet, a change is also being introduced in another aspect of the Japanese employment system, compensation practices. The traditional view is that Japanese employers have followed the principle of “seniority” wages, characterized by a strong link between an employee’s tenure with the firm and his/her compensation. Recently, however, there are signs that Japanese employers have shifted from this wage system based on an employee’s length of service and the highly correlated skill level. The new practice is a wage system based on an employee’s individual performance and the performance of the employing organization. By tying employee compensation to both kinds of performance, employers expect that wage levels will be more flexible in response to changes in individual performance and the economic prosperity of a firm. The new system is also intended to provide incentives for employees to increase their productivity and commitment to the goals of their employing organizations. Lower compensation costs are also on employers’ agenda when they introduce this new system. From an economic perspective, increased intra-firm wage disparity is an expected outcome (Genda, 1997).

In this article, the new system of compensation practices in Japanese firms — often called *seikashugi* — will be described. The focus will be how different this new system really is from the old style of

compensation, both in terms of characteristics and with regard to actual wage determination. In particular, two issues are examined in detail using a variety of data sources: characteristics of this new principle and its impact on employee wages.



Two sources have been heavily used. The first is the Ministry of Health, Labor and Welfare (MHLW) survey conducted in 2001, using a sample 5,321 firms. The sample in this survey is statistically representative of Japanese firms with 30 employees or more, because of the sampling procedure and the high response rate (90.1%). More information about this survey may be obtained at http://www.jil.go.jp/kisya/index_3dtj.html (in Japanese).

The second survey is smaller in scale, conducted by the author in 2001 in the cooperation of MHLW, using the 199 largest employers listed on the Tokyo Stock Exchange. Since the sample was restricted to large employers and the response rate was low (13.3%), the representativeness of this sample is questionable and will be used as a secondary source of information. A full report (in Japanese) of this survey is forthcoming later this year.

It is important to note that the target employee group whose compensation practices are being renovated is white-collar managerial and non-managerial employees. As noted in Morishima (1999), white-collar employees have been the recipient of most of the changes in Japanese human resource management (HRM). In Japan, blue-collar compensation and other HRM practices have generally remained untouched.

2. Is Employee Performance to Determine Compensation a New Idea?

Seikashugi can roughly be translated as “performance-ism” and refers to a set of compensation

(and other HRM) practices that link the performance of an employee and organization to employee rewards and incentives. In Japan, most changes have been in the area of increasing the role of an employee's individual performance in the determination of compensation. This is said to be a departure, as noted earlier, from the previous practice of basing employee compensation on their seniority and skill levels.

Results from the MHLW survey indicate that in 2001, a larger proportion of employers used "employee performance" as a determinant of an employee's base pay than in 1997. Exhibit 1 shows that, for both middle-managers and non-managers, the proportion of employers that use employee performance has increased about 10 percent. In addition, although unreported here, firms employing a large number of people tend to rely more on an employee's performance. The equivalent proportion for employers that have 1,000 or more regular-status employees is almost 80 percent for middle managers and 70 percent for non-managers.

Moreover, when the determination of total cash compensation is considered, instead of simply base pay, about 65 percent of the employers use employee performance for wage determination. One major difference between total cash compensation and base pay is the inclusion of bi-annual bonus payments. It is usually the case that employers use the results of employee evaluation, including evaluation of employee performance, more to determine the amount of bonuses than to determine base pay. Since bonuses

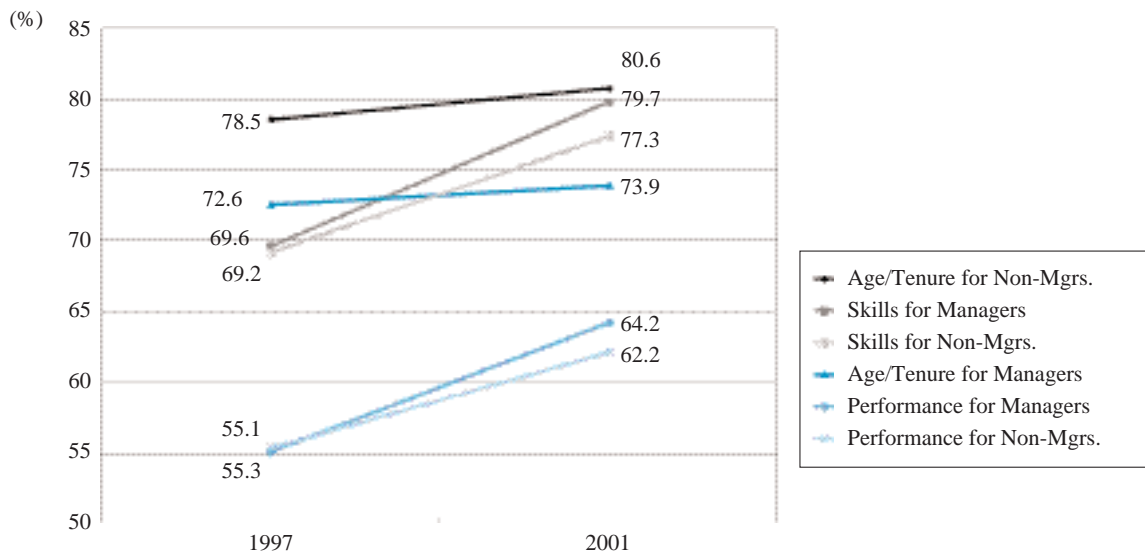
usually occupy more than one-quarter of annual cash compensation, the shift toward emphasizing employee performance has far more weight on the amount of an employee's total wages.

Finally, according to the smaller scale survey conducted by the author, "employee's short-term performance" may be the most important factor used to evaluate employees. For non-management, low middle management and senior middle-management positions, the average weight assigned to this factor is 33.8, 46.8, 51.7 out of 100, respectively. Other factors examined in this question are: employee skills, commitment to work, job content, and age/tenure. In sum, available evidence indicates that employers have begun to place more emphasis on employee performance to determine base pay.

Note, however, that in Exhibit 1, a slightly larger proportion of firms used employees' age and tenure to determine their base pay in 2001 than in 1997! These results seem to show that employers are not simply shifting to a new determinant. They are making their wage determination system more complex than before by considering a larger number of factors. Employees' performance has become important, but other factors, such as employee age and tenure, have not been abandoned.

This trend is even more visible when employers are asked if they have changed over the last five years the relative weight attached to a variety of factors. Close to one-third of the sample (31.4%) increased the weight attached to employee performance. In contrast, 13.7

Exhibit 1. Factors that Employers Use to Determine Base Pay



Source: Ministry of Health, Labour and Welfare survey, 2001.

percent of employers decreased the weight for employee age and tenure, but only 4.7 percent report dropping this factor altogether. This indicates that employee performance is considered in addition to, not in lieu of, employee age and tenure.

Similarly, other data also indicate that Japanese employers are likely to continue the use of the skills grade system, adding the performance component to this system. The skills grade system was introduced around 1960 to promote the idea of evaluating employees on the basis of their skills and capabilities. Close to 70 percent of large Japanese employers now use the skills grade system as a backbone of their HRM.

In the small survey conducted by the author, only 23.9 percent of employers that use employee performance to determine employee wages claim they will discontinue the skills grade system. The similar percentage for those firms that did not use employee performance to determine employees' wages is 21.0 percent. Again, Japanese employers do not appear to have chosen *seikashugi* in place of previous evaluation practices based on skill levels. Performance is simply added to the long list of evaluating factors.

By international comparison, increasing the importance associated with employee performance is likely to produce a system of pay determination that is more complex than that which exists in many foreign countries. The complexity stems from the Japanese pay determination system that formally considers a large number of factors, namely, age/tenure, skill level, performance, and job content. Note that these factors are formally incorporated into the system of wage determination through employee evaluation and reward practices. In addition, the weights attached to these factors change over an employee's career, making the system even more complex. Performance tends to become more important the later stages of an employee's career.

It is perhaps a mistake to finish a discussion on changes in wage determination without referring to the role of market wages. In many Western countries, the role played by market wages or pay offers that employees receive from external employers is said to be significant. In Japan, this has not been the case. One major characteristic of the Japanese compensation determination system is the lack of attention to external market factors. In fact, a survey conducted in 2001 by Recruit Co., Ltd., using a sample of 515 firms indicates that only about 11.5 percent of the employers use "market value" of the employees to determine their pay raise for managers and 6.4 percent for non-managers. The MHLW survey does not even

mention market wages as a factor in wage determination.

Employee removal, not retention, is the biggest issue in Japan now. As the economy recovers from this long recession with a more mobile workforce, another factor — market wages — may be added to the long list of factors for wage determination. As of now, however, market wage is likely to remain a minor factor in the Japanese wage determination system.

3. Intra-firm Wage Disparity: Is it Really Increasing?

The second issue concerns the range of intra-firm wage disparity: Is it really increasing in tandem with the introduction of more performance-oriented compensation practices, according to employer expectation? As argued by organizational researchers (e.g., Pfeffer, 1998), large intra-firm wage disparities tend to imbue competition among employees and increase conflict. Large wage disparity has been considered to be too "individualistic" for Japan and to disrupt organizational performance.

The sluggish economy and the consequent quest for aligning employee wages to productivity, as noted above, however, are expected to change that and increase the degree of intra-firm wage disparity in Japanese organizations. Employers argue that large wage differentiation is necessary to reward those who are performing well and provide incentives to everyone.

Yet, most of the economic studies conducted on this issue fail to find increasing wage disparity in Japanese organizations. Indeed, even according to the MHLW survey mentioned above, only 41.3 percent of employers that practice linking employees' performance (65% of the total sample; N=3,196) report that wage disparity has increased in their firms over the last five years. Forty-one percent may not be low, but considering that one of the purposes of introducing *seikashugi* is to provide incentives through increased wage disparity, the rate seems quite disappointing. A natural question is, why is it so difficult to increase wage disparity in Japanese organizations? Also, a related question is, if employee performance is tied to wages, what is the degree of this linkage?

The MHLW survey can be used to examine these questions. This survey asked those employers who linked employee performance to their pay the rate of average wage increase of middle and non-managers performing at the top, and the rate of average wage decrease for those performing at the bottom in these two groups. Respondents were asked to answer based

**Exhibit 2: Average Wage Increase/Decrease for Those Performing at the Top and Bottom
(Percent of Employers Falling in Each Cell)**

		Wage Increase Less than 5%	Wage Increase 5-10%	Wage Decrease Less than 5%	Wage Decrease 5-10%
Middle-Management	Top Performer	46.8%	28.5%	—	—
	Bottom Performer	—	—	61.5%	16.2%
Non-Management	Top Performer	47.9%	29.5%	—	—
	Bottom Performer	—	—	65.4%	18.0%

on the previous year's actual wage setting. Results are shown in Exhibit 2.

According to Exhibit 2, even when an employee's performance level ranks at the top of his/her peers, almost half of the employers (46.8% and 47.9%) report that wage increases are, on average, five percent. Almost three-quarters of the respondents say that their average wage increase is at most 10 percent.

The wage decrease for those who are performing at the bottom is even smaller. Here, about 60 to 65 percent of the employers report wage decreases of less than five percent and about 16 percent report wage decreases of five to 10 percent. Again, these two categories occupy almost three-quarters of the sample, but the proportion of firms that fall in the five to 10 percent decrease category is much larger than the proportion of firms that fall in the same category for wage increases.

Moreover, results of the smaller scale survey conducted by the author indicates that about one-third of the employers report that they do not decrease middle-manager wages based on performance. This increases to almost three-quarters of the employers when employees in non-management positions are concerned. Thus, decreasing wages for poor performers appears to be more difficult than increasing

wages for excellent performers.

Note, however, that Exhibit 2 shows changes in wages due to performance differences. Wage change and wage disparity are related but not equal, however. For this reason, in the survey I conducted I asked about the wage disparity between the top and bottom performers in a way similar to that used to obtain the results for Exhibit 2. Exhibit 3 shows, in percentage points, the wage differentials between top and bottom performers, relative to the median wage in three job ranks.

Overall, at least one-third of the employers reported that the largest wage differential between top and bottom performers is 10 percent (5% on each side) and some 70 percent responded that the differential was at most 40 percent (20% on each side). Thus, one conclusion is that the majority of organizations have a wage disparity of 40 percent or lower. Unreported results indicate that if one extends the range of wage differentials to 60 percent (30% on each side), it covers almost all the employers in the sample. These differentials are not negligible but appear small.

Why is it so difficult to increase and decrease wages for excellent and poor performers, respectively, and introduce larger wage differentials? Most research conducted in Western settings indicates that to derive

**Exhibit 3: Wage Disparity Between Top and Bottom Performers
(Percent of Employers Falling in Each Cell)**

		Wage 5% or Less Below the Median	Wage 5- 10% Below the Median	Wage 10- 20% Below the Median	Wage 5% or Less Above the Median	Wage 5- 10% Above the Median	Wage 10- 20% Above the Median
Senior Middle- Management	Top Performer	—	—	—	33.3%	14.8%	23.2%
	Bottom Performer	38.0%	17.6%	19.4%	—	—	—
Lower Middle- Management	Top Performer	—	—	—	34.3%	16.7%	21.3%
	Bottom Performer	37.0%	16.7%	27.8%	—	—	—
Non- Management	Top Performer	—	—	—	66.7%	11.1%	14.8%
	Bottom Performer	70.4%	9.3%	8.4%	—	—	—

strong incentive effects, organizations often provide wage disparity larger than actual performance or productivity differentials (e.g., Lazear, 1998).

One possibility is the existence of a large number of factors that are used to evaluate employees and determine their wages. As noted earlier, performance is being introduced not in place of previous evaluation factors, but as an addition. Thus, even though employees may be widely divergent in their performance levels, when other factors — such as skill levels, age/tenure, employee commitment — are taken into consideration, the effects of performance by itself may be watered down. The complexity of the evaluation and wage determination criteria may be in part responsible for the smaller wage disparity.

The second possibility is the lack of accurate and fair evaluation. In fact, according to the MHLW survey, only 10.6 percent of the employers report that they have experienced no problems with regard to the evaluation of employee performance. Forty percent report that they have experienced minor problems, and another 33 percent report experiencing major problems. Among the problems most frequently indicated are: “adjustment across evaluating managers is problematic” (63.2%), “managers are not trained to evaluate subordinate performance” (53.5%), and “managers do not spend enough time in evaluating subordinates” (26.7%). These results indicate that managers who are actually in charge of evaluating performance are not accustomed to evaluating subordinates this way and are experiencing difficulties. Since it is easily conceivable that managers play an important role in determining the success of this new method of evaluation, these difficulties experienced by managers could have serious implications.

Thus, employers may have kept wage disparity narrow in order to alleviate problems arising from the lack of experience and commitment of evaluating managers. Employees may not view performance evaluation conducted by these inexperienced managers as fair or accurate and may protest when large wage disparity is introduced based on their evaluation. In the MHLW survey, 32.9 percent of the employers report that their employees are not likely to view the results of performance evaluation in their organizations as fair.

The third possibility is the potential impact on organizational performance. It has often been claimed that the relative equality that existed in the Japanese compensation system is the result of the importance placed on workplace morale, on-the-job training (OJT) and cross learning among employees. Consequently, it has often been argued that the introduction of

seikashugi may hurt the effectiveness of teamwork and on-the-job training⁽¹⁾.

Yet, the MHLW data indicate that these are not strong concerns of the employers at the moment. Among the five possible problems that may be caused by relating compensation to employee performance, concern for decreased workplace morale ranks fourth, with 13.4 percent of the employers choosing this item. Only 2.1 percent responded that OJT at the workplace may be negatively affected. The most common concern was the perception of performance evaluations, as noted above. Thus, from the employers' perspective, lower workplace morale and the impact on OJT are not likely to be a strong deterrent against introducing a large wage disparity. Future research needs to be conducted to determine whether or not this lack of concern on the part of employers is justified.

Similarly, the fourth possibility is opposition from labor unions. Since large wage disparity among individual workers is likely to hurt union solidarity, unions are often said to oppose introduction of individualized employee assessment. Yet, the survey conducted by the author shows that only about one-half (50.8%) of the employers experienced labor union interference when introducing new performance-based employee evaluation systems. Slightly less than half (45.4%) of the employers report that the unions in their firms engage in negotiations with management regarding individual grievance cases relating to evaluation of their performance. In part due to the fact that *seikashugi* was mostly introduced for managerial employees who are not members of labor unions, the labor unions do not seem to be a strong barrier against large wage disparity. (See more on union roles in Morishima, 1999.)

Thus, as far as my evidence indicates, it is not opposition from labor unions nor concern for organizational performance that are preventing more employers from introducing larger wage differentials by employers. It has more to do with the performance evaluation system itself. Japanese employers do not seem confident (yet) that their own employees will accept the system nor that employees will accept a large-scale replacement of employee evaluation factors.

4. Employee Compensation Based on Corporate Performance: Does it Exist in Japan?

Finally, one remaining issue is the existence of compensation practices that tie organizational performance (e.g., firm profitability) to employee pay. This issue is important because in Western settings the

term “variable pay” usually covers compensation practices that tie organizational performance to pay as well as use individual employee performance evaluation to decide wage determination. In the United States, one study indicates that toward the end of the 1990s, almost all private-sector firms have some type of organization-based variable pay, the most important of which is a practice called profit sharing used by about 70 percent of the largest employers (Lawler, Mohrman and Ledford, 1998).

In contrast, Japanese employers have mainly focused their pay flexibility efforts on individual-based variable pay. Consequently, most Japanese employers have not adopted profit sharing or any other forms of variable pay using organizational performance as a base. One survey conducted by the Japan Productivity Center for Socio-Economic Development in 2000 (N=301) shows that 32.9 percent of the employers have this type of variable pay for managerial employees and 18.9 percent for non-managers. Among those firms which do not employ this practice, only about four to six percent are considering adoption in the future.

According to the same survey, the two most often cited reasons were that organizational performance may be affected by external factors that are not under the control of employees or managers, and that there does not exist a good measure of organizational performance. Japanese employers appear to be quite suspicious of using organizational performance measures for determining individual employee wages.

However, in the most recent *shunto* (spring wage offensive) negotiations, some employers and unions have been negotiating a system of tying corporate performance to next year’s bonus payments. Most notably, five major unions in the steel industry have demanded “corporate performance-linked bonus” and are negotiating with management. The impetus for this change is the current recession. Employers want to introduce more flexibility into their overall labor cost, and unions are willing to accept lower pay when times are bad but want to obtain assurance that when employers do better, they can also get more. More employers and unions are likely to follow. Thus, in the future, we may see an increase in the number of employers that have some form of organization-based variable pay⁽²⁾.

5. Conclusion

Japanese pay practices are undergoing change. Most notably, many employers are introducing an evaluation and wage determination practice that takes employee performance into consideration. However, these new types of practices are not necessarily a departure from the old system. This is a reformulation of the evaluation and wage determination system, assigning a larger weight to employee performance, while retaining previous factors such as employee skills and age/tenure. Thus, the system of wage determination is likely to become much more complex in the future.

The second characteristic of the new compensation practice is an increasing wage disparity among employees. Yet, the evidence shown in this article indicates that it will be a while before we may see a substantial disparity. Many system and institutional factors are likely to prevent employers from introducing large wage differentials and wage increases/decreases based on employee performance. Finally, although Japanese employers have been reluctant to introduce organization-based variable pay such as profit sharing, the current recession may change employer and union attitudes on this question.

Notes:

- ⁽¹⁾ Evidence in my data set showed some evidence that when employers decrease employee compensation based on performance, workplace morale and the extent of OJT deteriorates.
- ⁽²⁾ Previous researchers have put forward the hypothesis that Japanese bonuses are a form of profit sharing. However, to date only limited evidence has been found to support this view.

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JIL NEWS AND INFORMATION

Workshop on International Migration and the Labor Market in Asia: Summary

Since 1995, the Japan Institute of Labour — supported by the Ministry of Health, Labour and Welfare, the OECD and the ILO — has sponsored the annual “Workshop on International Migration and the Labor Market in Asia” with the aim of providing a forum for an exchange of opinions and information on the subject. This year marked the eighth session, and specialists and policymakers from 12 countries and regions in Asia, and specialists from the OECD and ILO gathered in Tokyo on February 4 and 5 to discuss international migration and the labor market in Asia.

1. Special Session

During this year’s workshop, a special session was held on “International Migration of the Highly Skilled,” a theme that has become the focus of attention in terms of inter-regional development. With globalization as the background, this session centered on the current situation of international migration patterns of highly skilled workers and the introduction of model initiatives for the region.

The keynote report by Professor Yasushi Iguchi of Kwansai Gakuin University dealt initially with the concepts of “brain drain” and “brain exchange.” Regarding brain drain, Professor Iguchi stated that the harmful effects of this phenomenon could be avoided if appropriate consideration is given to a number of areas given the current remarkably brisk international movement of capital, goods and services as compared to the 1970s when brain drain first became an issue.

In addition, having analyzed the actual situation of highly skilled workers and identified the patterns of those workers, Professor Iguchi raised several points for consideration, including the fact that in Asia, migration of the highly skilled is still dominated by intra-corporate transfers.

On the basis of these considerations, he indicated seven policy options including (i) promoting the establishment of research and development bases to utilize the highly skilled, (ii) the provision of centers of excellence, and (iii) streamlining intra-company

transfer from the perspective of mitigating the risk of brain drain in Asia, and finding ways to strengthen migration of the highly skilled within the framework of regional economic integration. Professor Iguchi also noted the importance of providing sufficient social infrastructure to facilitate the smooth entry of the families of highly skilled workers.

<Panel Discussion>

In the panel discussion that followed, based on Professor Iguchi’s keynote report, various panelists presented reports covering their experiences in Europe and on the actual situation of foreign students. Discussion focused on the following three points: (1) how to evaluate the experiences of individual countries; (2) how to utilize the highly skilled to promote economic development and avoid brain drain; and (3) how to formulate regional policies that respond to external competition in order to acquire highly skilled workers. Furthermore, the status of foreign student mobility and factors determining such movement were addressed by OECD specialists from the floor.

- (1) As to the experiences of individual countries, there were various reports on the substantial differences between those countries that have already determined national IT policies and are taking measures to acquire highly skilled workers, and the countries that have only just formulated such policies. Reports also looked at the emerging trend of one-way migration among students, particularly those destined for the U.S. In addition, the situation whereby students are unable to find work to optimize their skills in their home country due to wage differentials and the low level of domestic technology, known as “brain waste,” was also addressed.
- (2) To prevent brain drain, the following factors should be considered. The growing diversity among foreign students has led to an increase in the number of “non-elite” students. In this instance, it is important to consider the profitability of individual investment in studying

overseas. Consequently, it is important to ensure suitable employment opportunities for returning students.

- (3) Apropos policy options for the Asian region, the panelists and various attendees addressed a variety of subjects, including their experiences in Europe and on incentives being offered to returnees in their respective countries. When considering the affect of international transfers of the highly skilled in Asia, it is important to implement comprehensive educational, R&D, industrial and employment policies because it is impossible to resolve this issue in isolation.

The importance of keeping skilled workers in the country as opposed to merely attracting them was raised in connection with shortages of highly skilled workers. Furthermore, it was noted that this is not just a matter of filling the economic gap between the mother and receiving country, but requires establishing research centers that will attract the highly skilled via international cooperation, and the cultivation of a superior workforce to develop human resources.

The question and answer session addressed the aspects of national stability and cultural integration, as well as immigration issues including human rights, that need to be considered when addressing the issue of the highly skilled.

2. General Session 1

In the first general session, initial presentations focused on the recessions in the U.S., Japan and Europe, the stagnant or decelerating economies of many countries and regions in Asia, and how these affect the labor market.

The impact on foreign workers, however, differs among the various countries and regions. While a number of nations and regions reported that economic stagnation has led to a reduction in the number of foreign workers, other reports revealed no change in these numbers, and some cases saw an increase in the numbers of such workers.

Regarding illegal workers, the situation differs among settlement countries; however, there were reports on the necessity for new measures to address the question of people attempting illegal entry by sea and on the issue of fugitive trainees, which has surfaced in recent years. Problems, including the activities of criminal organizations, were noted, as

was the effectiveness of cooperation among nations.

3. General Session 2

Discussions in the second general session focused on changing policies; which governmental departments are taking policymaking initiatives, and how they are cooperating with relevant ministries; and, what kind of international cooperation is possible.

There were reports on the trend toward developing policy from the perspective of reviewing the system of trainees with employment contracts and revisions to reflect the current needs of such trainees, and the temporary acceptance of more skilled workers from among the migrant workforce. There was also a lively exchange of opinions and information on the current policy status among the sending and receiving nations and on new



movements in industry and business in settlement countries.

There were reports on how several countries and regions are aware of the need to accept the highly skilled as a means to facilitate domestic economic development and alter the structure of industry, and of formulating policies to attract such labor. In this regard, the importance of strengthening the connection between economic policies and immigration policies in sending countries was raised as a means to stop the outflow of the highly skilled, while the importance of adjusting/cooperating between government and nongovernment sectors, and cooperation between sending and receiving nations was also addressed.

Furthermore, from the standpoint of international cooperation, the need to consider policies from a broad range of perspectives, including the need to unify incentives for returnees with development assistance and so on, was highlighted. Reference was also made to drafting agreements between countries that are the main suppliers of workers and the receiving nations, to govern the handling of such labor, and to the need for cooperation between such nations.

There was debate on the growing number of illegal workers and how to deal with the situation. On the one hand, changes are in motion to legalize the position of undocumented workers in the receiving country, while cooperation between sending and receiving nations in the supervision of

illegal workers, etc., and international cooperation is also progressing.

4. Conclusion

To summarize, in spite of the various conditions prevailing in the economies and societies within Asia, all nations are aware of the need to utilize the highly skilled in order to facilitate overall economic and social development of the region. To secure highly skilled workers and to promote their effective movement, more discussion and information exchange between nations is needed to address the specific policy measures raised in the Special Session. Moreover, the potential for and necessity of promoting interregional cooperation was also mentioned. Formulating countermeasures for illegal workers is a crucial issue for policymakers, and, in light of reports of successful international cooperation, interregional cooperation should be promoted. As to measures to promote the acceptance of foreign workers, individual nations must first assess the situation in terms of national development and stability to conceive of an ideal scenario. Apropos the resolution on various problems regarding the receipt and dispatch of foreign labor, from the standpoint of economic and social development across the region to realize orderly labor mobility, it is crucial to maintain a continuous flow of information and opinions using the workshop forum, and to continue to cooperate with the OECD and ILO.

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