

Transforming Human Resource Management and Governance/Corporate Strategies

Summary

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(Note: Titles are as of March 2005.)

Research Period

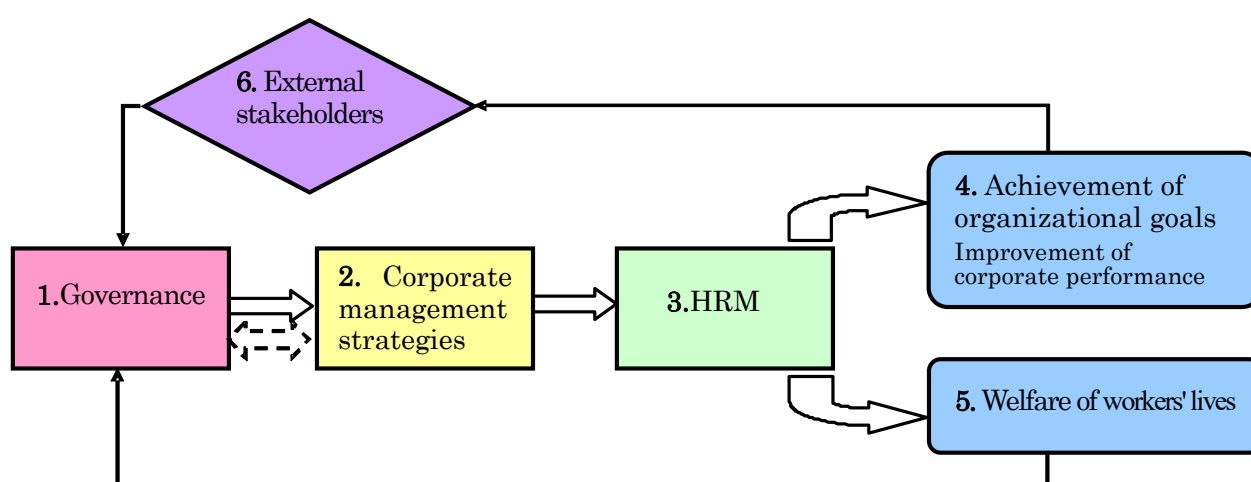
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Objective of the Research

To comprehensively analyze the Japanese companies' significantly changing corporate strategies and personnel treatment systems and to raise issues related to their future corporate management and labor, the JILPT has set down "research on comprehensive analysis of corporate strategies and personnel treatment systems" as a research topic in our medium-term project from FY 2003 to FY2006. In FY 2003, after surveying preceding studies, we identified issues regarding the following four points: "human resource management (HRM) that contributes to corporate management," "progress in performance-based personnel management," "shift in employment towards non-regular workers including part-timers," and "HRM reform and governance reform." We summed up these issues in "Identification of Issues for Research on Corporate Strategies and Personnel Treatment Systems" (JILPT Research Report No. 7) and "Part-timers in Workplace: Literature Survey Based on 'Core Labor Force Formation Model'" (Labor Policy Report No. 1).

In FY 2004, we conducted a company questionnaire survey : “General Survey on Corporate Strategies and Human Resource Management” focusing on “achievement of organizational goals (improvement of corporate performance)” (Item 4 in Figure 1), and an employee questionnaire survey : “Survey on Career Design and Human Resource Management Evaluation in a New Era” focusing on “welfare of workers’ lives” (Item 5 in Figure 1). This report contains the analyses of the company questionnaire survey data. The analyses of the employee questionnaire survey will be later compiled in another report.

Figure 1: Entire Image of the Research Project



Prologue: Framework of the Research Project and Method of the Company Questionnaire Survey

<Issues and the framework of the research project>

In conventional labor studies, issues related to corporate governance structure and corporate strategies have often been dealt as matters other than labor issues. However, the changes in the governance structure, from the management strongly controlled by the main bank to that devoted to shareholders, as well as in corporate strategies, could also significantly affect the method of HRM. Also, we still do not know exactly what kind of influence such changes in HRM have on corporate performance and productivity.

Good HRM can result in achievement of organizational goals and welfare of workers' lives. From this point of view, HRM should not only be considered as a tool to pursue profits for the company, but it becomes more important to explore a relationship beneficial for both a company and its employees (i.e. a “win-win relationship”), so that it also enriches the lives of those who work. Proposing a HRM mechanism desirable for both employers and employees is one of the most vital challenges in terms of labor policies.

Based on above understanding, we embarked on this research.

<Method of the company questionnaire survey and subject companies>

The subject companies were selected from the company database registry provided by the Tokyo Shoko Research, Ltd. Out of the universe of 18,000 Japanese companies that employ more than 200 workers (excluding organizations in the field of mining, agriculture, forestry, fisheries, medicine, religion, education, social insurance and welfare, as well as cooperative associations, academic institutes, and political, financial, and cultural bodies, defined under the Japan Standard Industry Classification (sub-sectors)) we extracted 11,865 enterprises in descending order of the number of employees. The data collection period was from October 15 to December 24, 2004, and the rate of valid response was 10.8 percent (the number of valid responses was 1,278). However, the data reflected in our study were limited to 1,214 responses which were received by November 30, 2004.

Chapter 1: Elements in Corporate and Human Resource Management Emphasized by Respondent Companies

<Attributes and other characteristics of the respondent companies>

One of the major characteristics of our study is to have covered a diverse range of companies, including middle-sized enterprises. Reflecting this, the composition of the respondent companies by number of employees is as follows: “less than 300” (18.5 percent), “300 – 499” (33.9 percent), “500 – 999” (24.6 percent), and “1,000 or more” (21.6 percent). Categorized by industry, the secondary industry accounted for 41.0 percent (construction: 7.2 percent, manufacturing: 33.8 percent). The shares of more than 80 percent of the respondent companies are not listed on the stock exchange. More than half (52.5 percent) of them have labor unions.

<Business conditions and emphasized corporate management elements>

In response to the question regarding their business conditions in recent years, the respondents answered as follows: “on an upward trend” (20.2 percent), “consistently profitable” (8.2 percent), “on upswing after decline” (23.9 percent), which means more than half (52.3 percent) replied that they were in a favorable financial condition. The corporate management elements which the respondents “have been emphasizing” are, in descending order of the percentage, “reinforcement and expansion of existing operations” (83.5 percent), “further improvement of customer satisfaction” (81.1 percent), “search for new customers” (68.5 percent), “cost reductions in indirect sectors” (64.6 percent), “differentiation of products and services against competitors” (59.1 percent), “corporate social responsibility” (55.8 percent), and “development of new technologies and products” (50.4 percent).

<HRM policies>

Our study also confirmed that these days more and more companies are reducing the number of regular employees and instead increasing that of non-regular workers. The elements which have been “emphasized” with respect to HRM are, “differentiation of treatment and evaluation based on performance and results” (75.3 percent), “communication of management goals and principles to employees” (66.3 percent), “regular employment of new graduates” (64.9 percent), and “employment of non-regular workers and external staff” (63.1 percent). Briefly, though the respondents are premised on performance and achievement-oriented ideas, they also maintain a basic attitude of sharing management goals and principles with their employees. As for the human resource portfolio, they are trying to employ non-regular staff, while constantly hiring new graduates as regular workers.

"The performance-based personnel management system valuing each employee's performance and achievements over his or her age or length of service" is adopted by 57.8 percent of the respondent companies. Two thirds of them introduced the system after 2000. The major reasons for adopting such a system include: "to motivate employees" (77.8 percent), "to make the evaluation and treatment system more accountable to employees" (59.8 percent), and "to clarify individual employees' objectives" (53.6 percent). Many respondents cited as challenges for implementing a performance-based personnel management system as follows: "having different evaluations depending on the evaluator" (70.1 percent) and "having departments/divisions that are having difficulty evaluating performance, including the department of management" (66.1 percent).

Chapter 2: Changes in Corporate Governance and Human Resource Management

<Changes in governance to emphasize values for shareholders>

The goal of the Chapter 2 is to realize through the questionnaire survey what sort of HRM mechanism Japanese companies are choosing under the changes in corporate governance. Although the influence of shareholders in terms of governance is not very dominant in Japanese enterprises at present, it can be expected for the authority of governance to be reinforced by shareholders and the board of directors, since nearly half of the respondent companies who answered to be listed on the stock exchange have implemented governance reforms including introduction of an operating officer system and have put more weight on enhanced values of shareholders in the last five years, and a significantly increasing number of companies aim to emphasize in the future on capital efficiency as one of their management indices in comparison with five years ago.

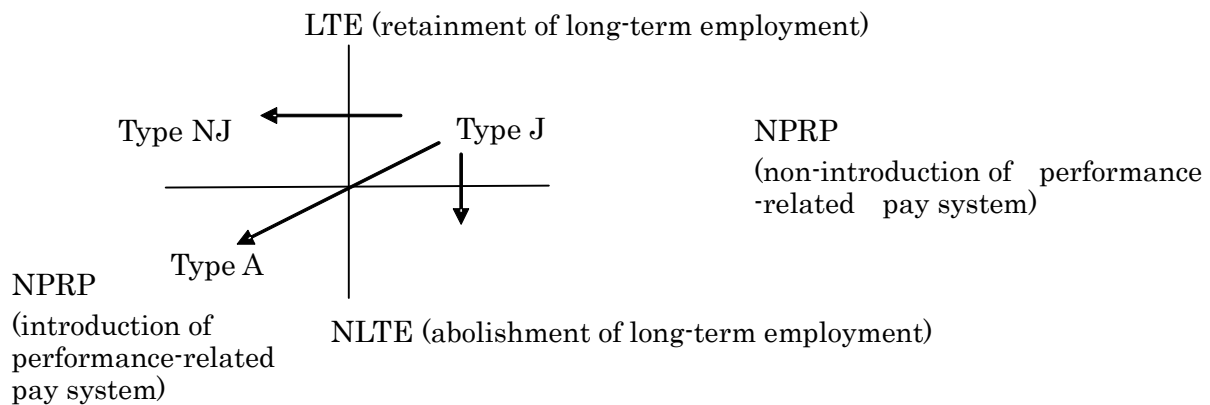
The traditional source of competitiveness of Japanese companies is considered to be their organizational abilities to flexibly adapt themselves to the environmental changes in the market and technology, as well as the system of internal trainings that enabled them to accommodate such changes, which can be conceptualized as functional flexibility. And this flexibility is premised on certain rigidities with respect to adjustment of employment and compensation, which can be seen in the long-term employment practice and seniority-based treatment. In this sense, the conventional system of Japanese enterprises could be comprehended as involving functional flexibility on one hand and quantitative (employment) and financial (compensation) rigidities on the other. What systematically complemented this mechanism was the main bank system. A major question here is whether Japanese companies are going to eliminate their HRM system based on a long-term viewpoint as they head towards shareholder-controlled governance and the complementarity of the main bank system disappears, and how they can

maintain the flexibility in terms of employment and compensation to retain the values for shareholders according to their variable revenues.

<Four differentiated patterns of HRM>

In respect of the flexibility of employment and compensation, we can come up with four HRM patterns, combining “retainment/abolishment of long-term employment (LTE)” and “introduction/non-introduction of performance-related pay (PRP) system.” The vertical axis of Figure 2 represents the distinction between retainment (indicated as “LTE”) and abolishment (“NLTE”) of long-term employment, and the horizontal axis shows that between introduction (“PRP”) and non-introduction (“NPRP”) of performance-related pay system. Applying these classifications to the respondent companies, we obtained the results as follows: Type J (LTE+NPRP) = 29.8 percent (22.3 percent among the listed companies); Type NJ (LTE+PRP) = 39.9 percent (48.4 percent); Type A (NLTE+PRP) = 18.3 percent (20.6 percent); and Type NLTE+NPRP = 12.0 percent (8.7 percent). Among these four patterns, Type J is deemed typical for Japanese companies, and Type A can often be found in the United States.

Figure 2: Four Differentiated Patterns of HRM



Whether or not a company introduces a policy to keep its long-term employment system had a correlation with the increase/decrease in the number of regular employees, but not with that of non-regular employees. This means that an employment policy of regular employees is irrelevant to that of non-regular employees. The decision to retain or abolish a long-term employment system seems to depend not so much on the perspective of corporate governance as on whether the company can retain its regular employees. As for performance-based pay

systems, it is more likely for listed companies to introduce the system compared to non-listed companies, and as the larger the size of the company, the higher the rate of adapting the system. This shows a clear distinction from the case of retention or abolishment of long-term employment system, where such difference is not so evident. Therefore, it can be considered that the influence of corporate governance is most prominently seen, among others, in the presence (or absence) of performance-related pay system in a company.

<Trial and error of Japanese companies hereafter>

The key for a new HRM (either Type NJ (LTE+PRP) or Type A (NLTE+PRP)) that replaces the existing Type J (LTE+NPRP) to succeed is how the performance-related pay system is applied. We assume that Japanese enterprises will have to go through trial and error regarding whether it is necessary to adopt performance-based personnel management more strictly or to maintain a rather moderate system by relaxing the performance-based principle to some extent. If the current performance-based management fails in Type NJ (LTE+PRP), companies will as a result seek for Type A (NLTE+PRP), abolishing their long-term employment system. Or they may result in Type J (LTE+NPRP) by giving up the performance-based pay system. On the other hand, if companies of Type A (NLTE+PRP) which have discontinued their long-term employment system gradually develop mistrust in the performance-based management, they may abolish the performance-related pay system and head for the type of NLTE+NPRP. Or as another alternative, they may resume having the long-term employment policy again and become closer to Type NJ (LTE+PRP).

At any rate, Japanese companies will in the meantime follow diverse routes and experience trial and error under the changes in corporate governance. Regardless of what kind of path each of them takes, the key factors will certainly include the trends of the long-term employment and performance-based pay systems, as well as those of the corporate performance based on these systems. Since this ultimately depends on how employees react, our next important task will be to examine the same issue by analyzing the results of the employee questionnaire survey.

Chapter 3: Human Resource Development, Performance-based Policy, and Organizational Vitality

<"Vitality at workplace" as a deliverable of HRM>

As we assumed that "the vitality in an organization" will be one of the deliverables which a company's HRM provides, we extracted from the data of our survey "the vitality at workplace" as an analyzing tool, which should be considered as a tangible concept that can be measured and

grasped. "The vitality at workplace" is defined as "a concept to capture the state of how members of an organization are highly motivated, proactively utilized as human resources, and inspired to improve themselves." The theme of this chapter is to explore the relationship between such vitality at workplace and HRM.

Based on the results of our factor analysis, we developed the following three scales to measure the vitality at workplace: (1) "morale at workplace" (indicating the levels of willingness and morale), (2) "isolation at workplace" (indicating the loss of atmosphere of the teamwork and development), and (3) "stress and turnover" (the levels of stress and turnover rate).

<Analyzing the respondent companies by the vitality at workplace>

When we analyzed the respondent companies based on the scale of the vitality at workplace, we found that many companies which showed rise in vitality at workplace in the last five years also achieved higher corporate performance, and that those poor in vitality also turned out to be poor in performance. In addition, we realized that highly motivated workplaces can often be found in the companies which have incorporated aggressive corporate strategies. On the other hand, many of the workplaces showing rise in isolation and stress were found in the companies whose performance was in decline, whose competitive environment was insecure, and whose (management) prospects as a business enterprise were difficult to predict. With respect to the stress level, it was low in the companies with a long-lasting tradition, and high in the listed companies and large enterprises. Those which lowered their performance or whose competitive environment was insecure showed high level of stress and clear tendency of voluntary turnover.

<Communication between employees and employers, conveyance of management goals and principles, and vitality at workplace>

The vitality at workplace is more deeply related to communication between employees and employers and conveyance of management goals and principles, rather than to HRM policies including evaluations, treatments, and human resource development. More precisely, these two factors (communication between employees and employers and conveyance of management goals and principles) have positive relations with morale at workplace, and negative relations with isolation at workplace, stress, and turnover. This made us realize that having good communication and sharing management principles and visions with employees are strongly relevant to revitalization of human resources and the organization itself.

<The performance-based principle and vitality at workplace>

The morale at workplace has the following two aspects: (1) increase in willingness by

promoting competitions and (2) that by intrinsic motivation (i.e. motivation caused by the work itself which an individual desires to take on). While performance-based evaluations and treatments bring about rise in willingness by promoting competitions among employees, they do not necessarily have positive influences on “motivation caused by the work itself,” that is, intrinsic motivation for each employee. Furthermore, the effect of promoting performance-based principles turned out to be immense in companies that have discontinued the long-term, stable employment system. We can interpret that the reason for this is because workers are more likely to expect to receive clear and short-term evaluations and treatments based on their performance, when long-term employment is not secured.

<Human resource development and vitality at workplace>

While we can often observe the high level of willingness for work in companies which emphasize on human resource development, there is no visible relevance between the emphasis on it and rise in willingness by promoting competitions which can be reinforced by performance-based principles. This outcome indicates that if a company seeks to promote not competitions but intrinsic willingness for work, it should prioritize human resource development over performance-based principles. The reason that human resource development could result in increasing willingness for work might be because it enables individual workers to obtain more compensation by helping them enhance their long-term values as employees.

<Selective career management and vitality at workplace>

Our study found that the emphasis on selective career management, particularly accelerated promotions regardless of age or length of service or consolation promotions following promotional competitions, is useful in improving the morale at workplace, but that it does not affect negative phenomena such as isolation at workplace, stress, or turnover. If implementing a performance-based principle means transition to evaluations and treatments exclusively based on achievements, accelerated promotions or consolation promotions can be regarded as genuinely merit-based approaches (or “abilityism”) in HRM. To properly carry out accelerated promotions or consolation promotions, it is vital to make comprehensive judgments reflecting individual worker’s ability, potential, and level of contribution. If such a mechanism of promotion based on comprehensive judgments can result in improvement of morale at workplace, it means that workers are simply appreciating the merit-based management beyond just a performance-based principle. Regarding this finding, further efforts will be required in the future to deepen the analysis.

Chapter 4: Realities of the Performance-based Principle

<Attributes and other characteristics of companies which have introduced performance-based principles>

The so-called “performance-based principle” has often been perceived as if it were a common concept, though it does not actually have a precise definition. The objective of this chapter, therefore, is to identify exactly what kind of characteristics a “performance-based principle” has, based on the results of our company questionnaire survey.

First of all, let us take a look at the rate of introduction of such principles. “The performance-based personnel management system valuing each employee’s performance and achievements over his or her age or length of service” is adopted by 57.8 percent of the respondent companies. It has a clearer relation with the number of regular employees rather than with that of the total workers including non-regular employees. We found that it is high among companies with 3,000 or more regular employees, while low among those with less than 300 regular employees. By business sector, it turned out to be relatively high in the field of information and telecommunications, construction, and wholesale and retail. Another finding is that it is higher among listed companies than non-listed companies. The presence/absence of a labor union or permanent labor-management consultation body does not have a strong connection with the introduction of performance-based principles. The subjects of such principles are mainly regular workers including department managers, section chiefs, and general full-time staff, while it is less common among the top management such as the president or executives, as well as among employees contracted on a part-time or *arubaito* (casual work) basis.

<The reasons for introduction of performance-based principles>

The reasons that respondent companies gave for introduction of performance-based principles can be broadly classified into the following four factors: (1) to motivate employees (motivation factor), (2) to make the evaluation and treatment system more accountable to employees (fairness factor), (3) to clarify individual employees’ objectives (objective management enhancement factor), and (4) to flexibly adjust personnel costs according to corporate performance and to abolish or reduce benefits in return for long-term commitment to the company (labor costs factor).

Additional findings include: (1) many companies in the field of information and telecommunications value fairness factor, (2) objective management enhancement factor is not given much weight in the finance and insurance industry, (3) labor costs factor is deemed

important in the wholesale and retail industry, (4) motivation, fairness, and objective management enhancement factors are all equally valued in the large-sized companies with 3,000 or more regular employees, and (5) relatively small-sized companies are not putting so much importance on either motivation or fairness factor.

<Institutional and actual operational wage gaps>

How much annual wage gap is seen in each of the respondent companies, among “regular employees who equally have a title of section chief in a same department”? In the questionnaire, we asked the respondents to work out indices to indicate the highest and lowest annual salary, setting the average index at 100, in terms of both: (1) annual wage gaps that are institutionally possible, and (2) those that actually exist. As a result, we confirmed that the both institutional and operational wage gaps are generally larger in companies that have introduced performance-based principles, rather than those that have not. In other words, it is understood that the performance-based principles are introduced and put into practice in order to widen the wage gaps among individual workers. We also found that the performance-based wage systems tend to aim not at imposing disciplinary actions by cutting down the compensation for those who did not perform satisfactorily, but at rewarding those who have achieved remarkable results by paying them higher wages, which shows that such wage systems have a more reward-oriented nature than other equivalents do.

The companies that introduced performance-based principles in 2000 or later have established wage systems that allow smaller wage gaps, both institutionally and operationally, compared to those adopted in companies that introduced the principles in 1999 or before. We may label performance-based systems with small wage gaps as “mild performance-based principles.” In many of the companies who have introduced such “mild performance-based principles,” their corporate performance turned out to be strong. Such principles, which are based on achievement yet keep wage gaps relatively small, can be recognized as a new Japan model, referable to as “Japanese-style performance based principles.”

<Introduction of performance-based principles and HRM strategies>

When we conducted a logistic regression analysis, using the presence/absence of the performance-based principle as the dependent variable, as well as the number of regular employees (continuous variable) and dummy variables that represent type of industry, long-term and stable employment strategies, non-regular worker employment strategies, and educational training strategies (both general and selective educational training strategies) as the independent variables, we found that the only factor that was statistically significant was

the selective educational training strategies. To put it differently, among the respondent companies, those which have introduced selective educational training strategies that are selectively applied only to some of their employees have a high rate of introduction of performance-based principles. It is indicated that, as one of the reasons for pursuing financial flexibility in the form of performance-based principles, companies have strategies to intensively educate outstanding staff and to implement differentiation in human resources. So that a company can secure highly competitive and capable employees, it is required to establish a highly incentive oriented HRM mechanism, including performance-based principles.

Chapter 5: Use of External Workers and Corporate/Human Resource Management

<Intention to use external workers>

In the questionnaire, we asked about “the prospect of newly hiring or reducing regular employees” and “style of employment that should be most prioritized in the future” in the following four categories: (1) specialists in certain fields such as accounting, legal work, finance or R&D, (2) clerical staff who mostly engage in routine tasks in the administration and management division, (3) workers with highly technical skills at production sites, and (4) workers who mostly engage in routine tasks at production sites. Many of the respondent companies answered that they are interested in using external workers. The term “External workers” used here means workers who are not employed but utilized by companies such as dispatched workers, outside contracted temporary workers and so on. They also answered that they have intention to use those workers in routine tasks as (2) and (4) above. This result, to some extent, corresponds to the theoretical scheme of Lepak and Snell (1999) that classifies human resources by value and rarity.

The companies that plan to prioritize using dispatched workers and outsourcing the most in either of the above four categories accounted for 44.7 percent of the entire respondents, while those that do not plan to prioritize using dispatched workers and outsourcing the most in any of the four categories accounted for 39.1 percent. We analyzed the both types, categorizing the former as “companies that have intention to use external workers” and the latter as “those that do not have the intention to do so.” The “companies that have intention to use external workers” are often found in the field of information and telecommunications (79.0 percent) and manufacturing of electrical equipment and appliances (71.6 percent). There was no difference observed by size of enterprise. Among the companies that have labor unions, approximately 60 percent have intention to use external workers, while less than half among those without a labor union. This suggests that the increase in employment costs of labor union members may be promoting the willingness to use external workers.

<HRM in companies that are thinking of use external workers>

The companies that have reduced or at least controlled the number of regular employees are more likely to use external workers, in which we assume that they may have motives for reducing, controlling and avoiding fixing labor costs. With regard to the long-term stable employment system, there was no visible difference in attitude between the companies which were willing to use external workers and those which were not. Maintaining the long-term stable employment system and using external workers (as well as adopting non-typical employment styles) can be considered not at all incompatible but rather mutually complementary.

The companies that have put an emphasis on “use of non-regular and/or external workers,” “flexibilization of labor costs,” and “differentiation of treatment according to each worker’s performance and results” are often found among those that do not hesitate to use external workers. In fact, the companies that have introduced a performance-based HRM system account for 66.1 percent among those that are willing to use external workers, and 48.4 percent among those that are not. The willingness/unwillingness to use external workers showed differences with statistic significance concerning the following four principles associated with employees’ placement and career: “consolation promotions following promotional competitions,” “transfers reflecting intentions of each employee, incorporating the system of self-application or internal recruitment,” “temporary or permanent transfer to a subsidiary or associated company for such company’s management improvement,” and “change in the contractual status from that of a non-regular worker to that of a regular worker.” It is clear that the companies that have intention to use external workers are also actively introducing these HRM programs.

<The companies that are thinking of using external workers and their management environment>

Although the use of external workers is often aimed at controlling or reducing personnel costs, companies that are willing to do so are not necessarily less successful in terms of corporate performance than those that do not. However, the difference in the willingness to use external workers does cause differences in management indices to prioritize. The companies who have intention to use external workers show a clearer tendency to put weight on “productivity and efficiency.” Another difference is seen in the recognition of management environment. The companies that are willing to use external staff tended to answer that the speed of technology renovation and product development was faster in their industry, and that they survived more intensive competitions, having more uncertainties in operational processes, than those in other

industries.

<Use of external workers and corporate/human resource management>

To verify under what kind of HRM principles and corporate strategies the use of external workers is likely to be introduced, we conducted a logistic regression analysis, using the HRM policies and business conditions of the respondent companies as the independent variables, willingness/unwillingness to use external workers as the dependent variable, and corporate attributes as the control variables. The willingness to use external workers showed statistically-significant correlations with increase/decrease in the number of regular employees and HRM policies such as “differentiation of treatment according to each worker’s performance and results,” “career development assistance for employees using career development plans (CDPs), etc.,” “transfers reflecting intentions of each employee, incorporating the system of self-application or internal recruitment,” and “employ regular employees among non-regular workers.” We have once again confirmed that the use of external workers is highly likely to be introduced along with the following policies: (1) reduction or control in the number of regular employees for the purpose of reducing or controlling labor costs, (2) review of the relation between performance and cost covering the entire personnel (including both regular and non-regular employees), and (3) selection of the core staff who play a role to contribute to corporate performance, and efforts for the human resource development, retainment and morale improvement of such core staffs.

We also added certain items regarding business conditions as independent variables to our analysis. Our findings include the statistically-significant relationship between use of external workers and the following two points: (1) the degree of uncertainties involved in the operational structure of the primary business activities and (2) whether the most prioritized business indices in the last five years were related to productivity and efficiency. It is indicated that (1) companies that feel uncertain about their business prospects often use external workers because they are inclined to flexible personnel management, and (2) those that have emphasis on productivity and efficiency are willing to use external workers for cost reduction/control purposes.

Appendix

Contents of the JILPT Research Report “Transforming Human Resources Management and Governance/Corporate Strategies”

Part I: Summary of the Report

Part II: Analyses of the Report

Prologue Role of this Report in the Course of the Research

Chapter 1 Summary of “the General Survey on Corporate Strategies and Human Resource Management”

Chapter 2 Changes in Corporate Governance and Human Resource Management: Changes and Diversity in Japanese Companies

Chapter 3 Human Resource Development, Performance-based Principle, and Vitality of Organization

Chapter 4 Realities of the Performance-based Principle

Chapter 5 Use of External Workers and Corporate/Human Resource Management

Part III: References and Materials

Simple Compilation of the Survey Results and the Questionnaire used in the Research