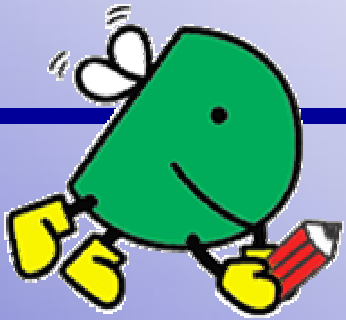


# Corporate Finance and Human Resource Management

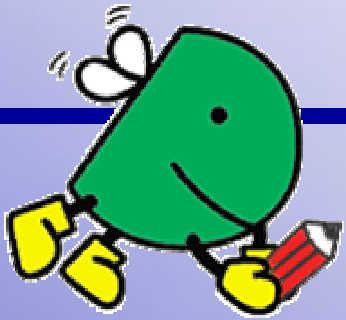
**Masahiro Abe (Dokkyo Univ.)**

**Takeo Hoshi (UC San Diego)**



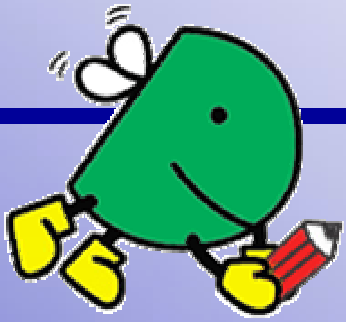
## Introduction

- This paper focuses on two sub-systems of the Japanese corporate governance: one on corporate finance and another on human resource management.
- The various aspects of “CG” are not combined randomly(Aoki[2001]).
- “CG” is a system in the sense that these various sub-systems are integrated to reinforce each other.



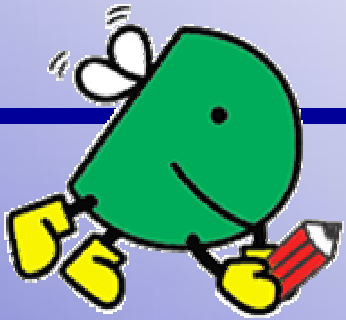
## Related Paper

- Jackson[2004]:close correlation between the corporate finance and labour management practices at country level.
- Ahmadjian and Robinson[2001]:the firms with high foreign ownership and low bank ownership are more likely to downsize their workforce.
- Abe [2002]:the firms with close main bank ties adjust their employment only slowly.



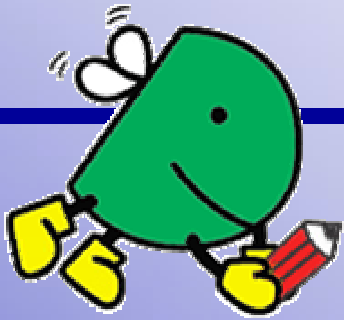
## (Former) Japanese Corporate Governance

- Shareholders seems to play rather a limited role.
- Long-term relationship between the corporation and its many stakeholders; banks, employees



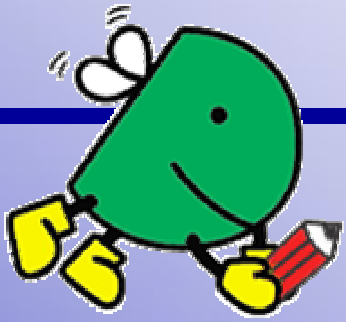
# Changes in Japanese Corporate Governance: Finance

- Deregulation in corporate financing
- Many company increased the bond issues
- Changes in Cross-shareholding
- Foreign investors increased the ownership in the Tokyo Stock Exchange



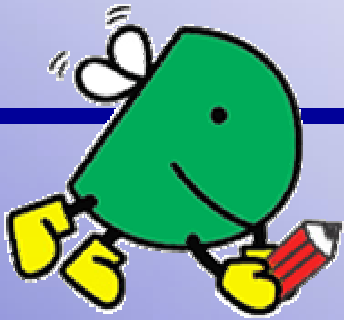
# Changes in Japanese Corporate Governance: Employment

- End (?) of the life time employment
- Increase in the adjustment of labor force through dismissal or early retirement
- Transfiguration of the education and training of worker
- Etc.



## Complementarity: A simple Model

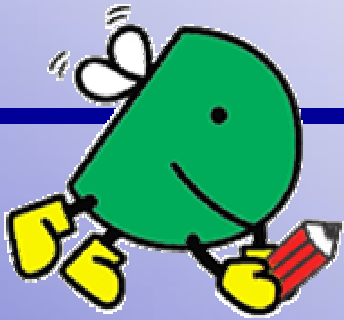
- This section presents a simple model by Hoshi[2002] that implies such a complementarity between corporate financing and human resource management.



## Model: Financial Aspect

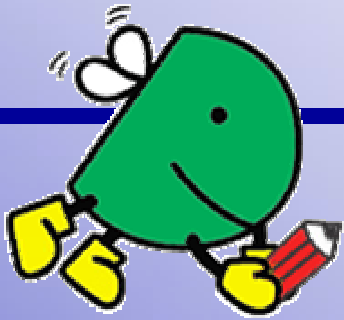
- Two type of project: Good and Bad project.
- Both projects require the initial investment of  $I$  and yield  $R(>I)$  if successful.
- The probability of succeeds is  $P_h$  for good project and  $P_l$  for bad one.
- The bad project bring private non-monetary benefit of  $B$ .
- The manager is endowed with her fund of  $A(<I)$





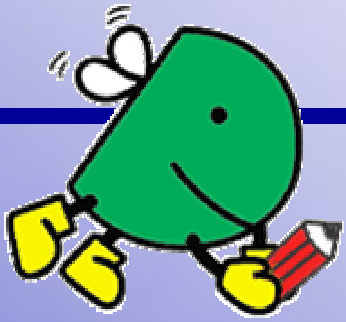
## Model: Financial Aspect

- The choice of project is private information of the manager, which creates a potential moral hazard problem.



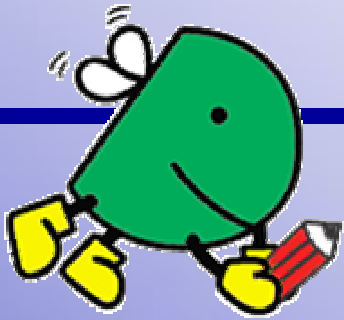
## Model: HRM Aspect

- The manager needs to hire one worker to complete a project
- Good project need a skilled worker.
- If an unskilled worker is assigned to good project, the probability of success falls from  $P_h$  to  $P_m$  ( $P_h > P_m > P_l$ ).
- For bad project, the worker's skill is no important.



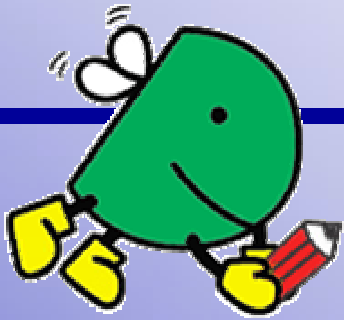
## Model: HRM Aspect

- To acquire the skill, workers need efforts(E).
- A worker's skill and the efforts to acquire the skill are assumed to be private information, which create a potential moral hazard problem.



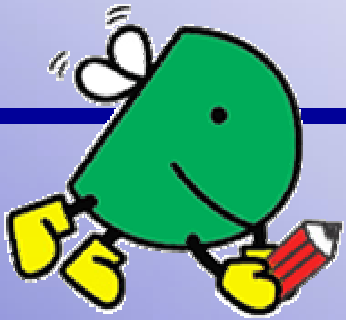
# Result of the Simple Model

	Bank	Stock Market
In-house training	$p_H \left( R - \frac{b}{p_H - p_L} \right) - w^* - e - c_b$ $\geq I - A$	$p_H R - q_H \frac{B}{q_H - q_L} - \frac{w^*}{q_H} - e$ $\geq I - A$
Self training	$p_H \left( R - \frac{b}{p_H - p_L} \right) - \frac{w^* + E}{r_H} - c_b$ $\geq I - A$	$p_H R - q_H \frac{B}{q_H - q_L} - q_H \frac{w^* + E}{r_H}$ $\geq I - A$



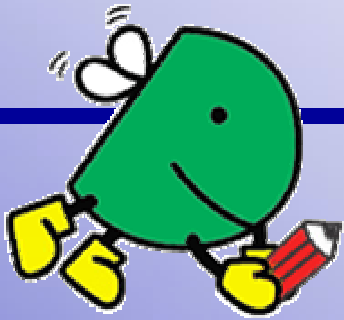
## Result of the Simple Model

- Bank monitoring dominates stock market financing if the workers acquire the skill through in-house training.
- Stock market financing dominates bank monitoring if the workers acquire the skill through self-training.



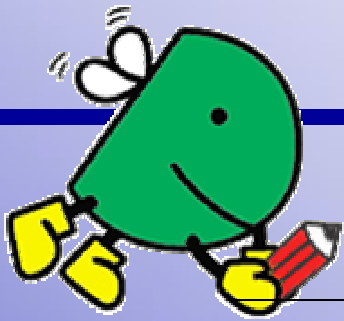
## Result of the Simple Model

- In-house training dominates self-training under bank monitoring.
- Self-training dominates in-house training under stock market financing.
- We find the complementarity between financial arrangement and human resource management.



# Empirical Analysis

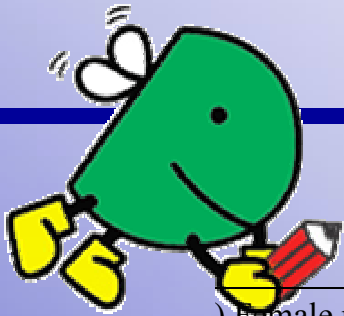
- Data
- “Human Resource Management Systems Survey”
- “Corporate Financial Databank”
- “Directors Handbook”
- For 58 firms, we have been able to collect all the information.



# Empirical Analysis

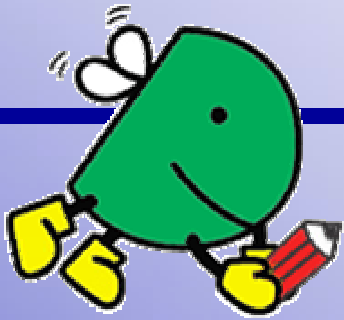
		Bank ownership		Foreign ownership	
actice	Adopted?	1995	2000	1995	2000
) Annual salary system	Yes	0.3474	0.3368	0.0808	0.1082
	No	0.3774	0.3243	0.0819	0.0746
) Bonus linked to achievement	Yes	0.3651	0.3349	0.1031	0.0898
	No	0.3762	0.3274	0.0774	0.0850
) Irregular working hour stem	Yes	0.3931*	0.3434*	0.0906	0.0908
	No	0.3204*	0.2645*	0.0567	0.0634
) Length-of-service awards	Yes	0.3801	0.3228	0.0787	0.0704**
	No	0.3323	0.3459	0.1042	0.1336**
) Training for evaluators	Yes	0.3843	0.3500*	0.0823	0.0599
	No	0.3457	0.2804*	0.0803	0.0972
) Company sponsored ucation program	Yes	0.3891	0.3820*	0.1038	0.1414***
	No	0.3682	0.3062*	0.0727	0.0625***
) Education abroad program	Yes	0.4436**	0.4063***	0.1267**	0.1421***
	No	0.3501**	0.2905***	0.0662**	0.0581***





# Empirical Analysis

) Female managers	Yes	0.3746	0.3695**	0.0959	0.1259***
	No	0.3738	0.2926**	0.0618	0.0506***
) In-house venture system	Yes	0.3697	0.5388***	0.1015	0.1685
	No	0.3745	0.3169***	0.0807	0.0811
0) Permanent <i>shukko</i>	Yes	0.4060*	0.3460	0.0869	0.0871
	No	0.3467*	0.3141	0.0773	0.0845
1) Financial assistance for lf-training	Yes	0.3895	0.3320	0.0941	0.0842
	No	0.3474	0.3220	0.0601	0.0882
2) Exam to advance to a higher nk	Yes	0.3309	0.2884	0.0522	0.0248
	No	0.3793	0.3322	0.0852	0.0914
3) Exam to advance to a higher b grade	Yes	0.4139*	0.3433	0.0744	0.0769
	No	0.3518*	0.3163	0.0860	0.0928
4) Fast tracking	Yes	0.4684	0.3351	0.0557	0.1677**
	No	0.3692	0.3276	0.0832	0.0762**



## Conclusion

- The companies that show high level of foreign ownership were more likely to have human resource management practice that deviate from the traditional Japanese practice.
- However, the foreign ownership cannot explain all the changes in the HRM practices.