

Comments on
“Corporate Finance and Human Resource
Management”
(Masahiro Abe and Takeo Hoshi)
and
“The Challenge Role of Employees in
Japanese Corporate Governance: Participation,
Adjustment and Distributional Conflict”
(Gregory Jackson)

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Abe and Hoshi

- They show, first, the changing features in the Japanese corporate financing and HRM practices.
 - from the dissolution of cross shareholding to the rapid increase of foreign shareholders.
 - from the decline of lifetime employment to the introduction of performance-related pay.
- Second, they present a fine model by extending that of Tirole(2001) and derive from it two kinds of complementarity between finance and HRM system.
- Third, they test such complementarity by using some available data.

Two kinds of complementarity

- Complementarity between sub-systems is confirmed on the basis of the firm's performance or on the building of competitiveness in so far as it could be lasted under the given conditions.
- Abe and Hoshi show this by specifying the financial system to solve the agency problem between manager and investor and by specifying the HRM system to solve the agency problem between manager and worker.
- And they present two dominant patterns of complementarity; one is the combination of bank financing and in-house training (traditional Japanese firm), the other is the combination of stock market financing and self-training (U.S. firm).

Comment 1: Financial approach

- Corporate governance mainly has been argued on the side of “finance”.
- It is yet necessary to shed light on it on the side of “labor”.
- Financial approach is likely to assume that financial change brings about governance change, and which improves the performance of the firm.
- Then, “finance-governance-performance” nexus is supposed.
- However, “governance-performance” nexus is not necessarily confirmed, whereas “finance-governance” nexus is confirmed (Omura and Mashiko;2003, Miyajima; 2003).

Comment 2: Labor view

- As firm's performance rests on the work of "labor", it is important to examine the HRM change under the governance change.
 - from financial view, performance will be measured in terms of profitability, say Tobin's Q.
 - from labor view, performance will be measured in terms of competitiveness, say productivity, although such measuring is difficult.
- Then, "finance-governance-HRM-performance" nexus is supposed.
- Is such a nexus really confirmed under governance change?
- Abe and Hoshi show "finance-governance-HRM" nexus, but "HRM-performance" nexus is left unconfirmed.

Gregory Jackson

- Abe and Hoshi present the alternative model of governance, that is, the U.S. type one, instead of hybrid model.
- By contrast, Gregory Jackson shows the diversity of corporate governance not only across different countries, macro diversity, but also across Japanese firms, micro diversity.
- He categorizes such variations into 4 types in terms of HRM policy.
 - over 85% of sample firms maintain long-term employment (LTE) policy, although employment adjustment is accelerated and the volume of core employees is being diminished.

Variations in the pay policy

- Diversity within J-firms then lies in their pay policy: 1) seniority wage (traditional J-type), 2) seniority plus merit (J-type; 40%), and 3) merit only (J-Hybrid; 40%), respectively hold LTE.
- The rest is categorized as A-type (under 15%), no LTE+ merit wage under the pressure of shareholders.
- Type-2 is likely the firms that introduce PRP (performance-related pay) into competence-rank system, type-3 is likely the firms that introduce the annual salary system.

Diversity within Japanese firms

- Certainly, we can find variations in the changing corporate governance specifically among competitive Japanese firms.
- As for “finance-governance” nexus,
 - under the strong pressure from foreign investors, some firms do not necessarily change its governance structure, particularly, board structure.
 - under the weak pressure from shareholders and banks, some firms can keep its governance effective by means of their internal disciplinary mechanism (Niihara; 2003).
- As for “governance-HRM” nexus,
 - under the governance change, pay and promotion system is changed in some firms, whereas their employment system is not changed (Miyajima;2003).
 - long-term employment practice is not ended, rather maintained (Kato;2001).

Comment 1: Coexistence between LTE and PRP

- It has been argued that LTE and seniority system are complementary factors via firm-specific training in the Japanese HRM.
- By contrast, combination of LTE and PRP becomes dominant pattern, whereas combination of no LET and PRP is still minority.
- The more LTE is highly maintained, the more PRP is eagerly introduced.
- Are they really compatible?
- As predicted by core-periphery model, LTE policy itself is maintained by using increasingly non-regular employees.

Comment 2: Decline of confidence or perception gap

- However, Japanese firms will face a serious problem of the loss of employees' confidence. See JIL(1999)

	Employer		Employee			
	Past	Future	20-29	30-39	40-49	50-59
Employed until the retiring age	80.9	64.5	12.9	25.3	39.0	60.2
Transferred to the related companies	7.8	21.3	8.4	15.8	21.3	17.9
Job change	2.8	5.9	32.5	19.8	11.7	5.4
Unknown	8.6	8.3	46.1	38.8	28.0	15.8

Comment 3: Gradual change

- While radical change is suggested, what actually occurs in HRM change is moderate and gradual in both pay and employment.
 - in so far as PRP is introduced into internal labor market, it really intends to make differentials moderate, meet with the existing competence-rank, and assure implicit contract of LTE.
 - PRP for manager is restrained at least until up to now (Kubo; 2003).
- Pay and employment policy is shaped due to the pursuit for the building of competitiveness rather than the governance change.
- Then, corporate strategy for competitiveness is a key factor in the shape of governance structure.
 - shareholder pressure and market competition will also function to make manager more keen to their competitiveness.

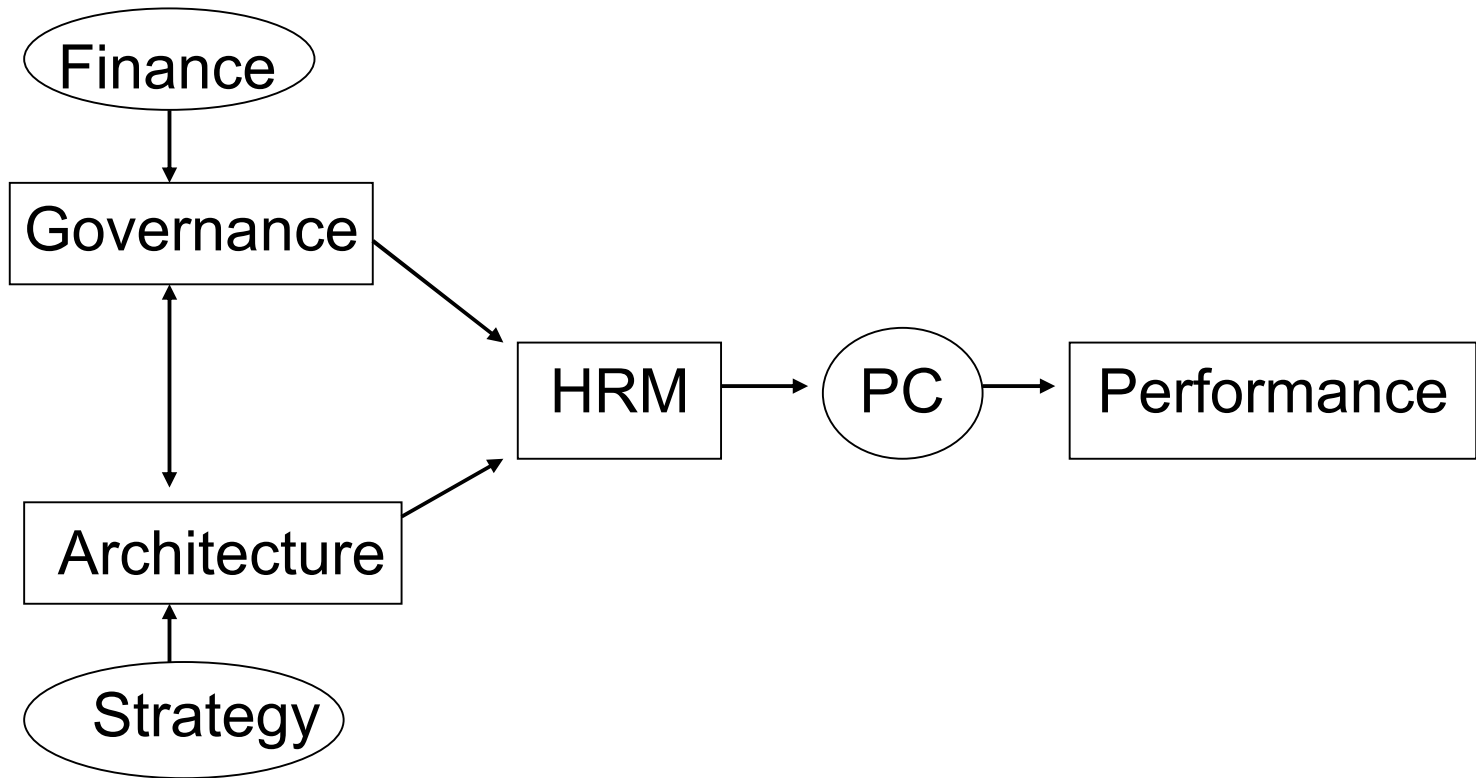
Comment 4: Corporate strategy

- Corporate strategy to build competitiveness shapes its product architecture and organizational architecture, modular or integral (Fujimoto;2003), which determine or correspond with the governance structure(Aoki;2004).
- Then, “strategy-architecture-governance” nexus is supposed in contrast to “finance-governance” nexus.
 - under the strong pressure from stock markets, high engineering strategic firms are likely to block shareholder-oriented governance.
- Corporate strategy also affects HRM to realize its product and organizational architecture.
- Then, “strategy-architecture-HRM” nexus is supposed.

Comment 5: Psychological contract

- As for “HRM-performance” nexus, its performance on the basis of work organization depends on the state of employees’ behavior and motivation under HRM practices, which is critical to the HRM change.
 - while PRP intends to encourage employees’ motivation for work, it is not yet clear whether such an aim is really realized or not.
- This could be shed light on from the viewpoint of “psychological contract”, which is inserted into “HRM-performance” nexus, .
- Then, “HRM-PC-performance” nexus is supposed.

Comment 6: Governance System



Comment 7: Typology of governance

		Finance		
		Market		Bank
Strategy	Modular	Quasi-US (NLTE+PRP)		Traditional-J (LET+seniority)
	Integral	J-Hybrid (LTE+strong PRP)	J-type (LTE+weak PRP)	

Comment 8: Role of union

- In the traditional J-firms, workers were provided with security in both pay and employment, so union or workers representatives are not in the position to express their voice to management.
 - although the joint-consultation is formally established, it is far from German type co-determination.
- However, such security is being removed and the risk of variability is left to individual workers.
- Unions have a role to speak their view on the various aspects of HRM and governance structure, placement, evaluation, opportunity, and board member, but these regulative powers have been too weak in Japan.
- To build such a substantive voice mechanism would be the governance change for workers.