Summary Results of the Corporate Excellence Research Project

June 21, 2002

RIETI

(Research Institute of Economy, Trade and Industry)

1. The Research Institute of Economy, Trade and Industry, (RIETI), an independent administrative institution (headed by President and Chief Research Officer Masahiko Aoki, Professor of Stanford University) implemented the Corporate Excellence Research Project (conducted by Senior Fellow Hiroaki Niihara), a study **to analyze the common factors of some Japanese enterprises that achieve excellent performance** even under adverse economic circumstances, in order to obtain the optimal direction for the development of Japanese companies as a whole.

2. The project "Go Nippon!" is being promoted as part of the government's economic policy formulated at the Council on Economic and Fiscal Policy (chaired by Prime Minister Junichiro Koizumi) to revitalize the nation's economy.

   The Corporate Excellence Research Project was placed as a part of the project "Go Nippon!" at the request of the council and is expected to encourage wide public discussion. Launching nationwide campaigns will be considered, including symposiums in many parts of the country, held by the Cabinet Office and RIETI , as soon as the project's results are published.

   This paper summarizes the results of the project submitted at the Council on Economic and Fiscal Policy on the evening of June 21, 2002.

3. In the Corporate Excellence Research Project, we selected typical Japanese enterprises performing very well in terms of profitability, stability, and growth potential, in order to identify the common factors that distinguish them from unsuccessful companies.

   Example: The ordinary profit ratio of general pieces of capital

   Toyota Motor: 5.72% (Industry average: 4.17%)

   Canon: Unconsolidated, 13.04%; consolidated, 9.92% (Industry average: 6.21%)

Kao: 14.59% (Industry average: 10.52%)

Mabuchi Motor: Unconsolidated, 13.03%; consolidated, 11.94% (Industry average: 2.54%)

Shin-Etsu Chemical: 9.51% (Industry average: 5.28%)

Nintendo: 19.21% (Industry average: 6.90%)

Yamato Transport: 8.15% (Industry average: 3.83%)

Shimano: 6.30% (Industry average: 3.47%)

Honda Motor: 7.29% (Industry average: 4.17%)

Seven-Eleven Japan: 20.24% (Industry average: 5.68%)

The analytic results of our research, expected to aid in business management of other Japanese companies, will be published in a 150-page final report in the near future.

The following is a summary of our research:

4. In the first place, the following two unique characteristics of successful companies which are inconsistent with general understanding were identified:

(1) Successful companies are **not necessarily part of fast-growing forefront industries.** Excellent companies can be found in any industry, regardless of whether the industry is thriving. In other words, **what matters is the competitiveness of an individual enterprise, not the competitiveness of the industry of which the enterprise belongs.**

[Example]

Mabuchi Motor (ratio of ordinary profit to net sales at 20% to 30%):

→ Produces consumer small magnet motors; average unit price: ¥72; matured technologically

Shimano (international market share of approximately 70%):

→ Bicycle parts, etc.; low-technology products

Shin-Etsu Chemical (the world's fifth largest in terms of market capitalization, following Dupont, Dow Chemical, BASF, and Bayer):

→ Products in the chemical field, in which most Japanese companies allegedly

have weaknesses

(2) Successful companies do not necessarily belong to industries that handle tradable commodities, and are therefore not necessarily faced with direct international competition. **Some successful companies employ business models targeted at domestic demand.**

[Example]

Seven-Eleven Japan, Yamato Transport, and Kao (only 12% to 13% of profit from overseas operations)

Many export-oriented businesses started operation with business models aimed at domestic markets.

[Example] Nintendo

5. **Successful companies have the following six features in common.** We started this research with the assumption that profitable companies introduced U.S.-style management indicators and ways of management. In fact, U.S.-style concepts were found in both successful and unsuccessful enterprises. Thus, we judged the introduction of the U.S.-style management itself was not an important factor in business success.

(1) Range of businesses—**Making a distinction between what they do and what they don't**

The activities of thriving companies **constitute single, consistent, and coherent concept. They are capable of explaining their concept clearly. And based on that concept, they determine what they should do as a business and what they should not do.**

A group of closely associated concepts composes their corporate philosophy, and that philosophy is effective in determining what they should **not** do.

Currently, most Japanese companies, whether or not thriving, stress the importance of limiting types of business and just concentrating on them whether or not thriving.

An important factor differentiating successful from unsuccessful companies is **whether**

a company can make clear distinctions regarding what it does not do, what it should stop doing, and what it should not do. In our survey, when we asked about certain types of business many successful enterprises asserted, "We aren't involved in that sort of business."

Some unprofitable enterprises, in contrast, gave an endless list of their incoherent operations, which they state as their corporate concept.

Initiating multiple moves or pursuing more than one objective simultaneously tends to thin out corporate power and bring each move and objective out of focus. Although their business models initially produced excellent business results, some companies are suffering from poor performance after they diversified or expanded their operations beyond their initial concept by using up their profits.

We also judged it to be more important than we first thought for a president to realize actual forefront operations. Companies and the people who run them should understand the importance of the forefront and daily operations,—in effect, reality.

The management should divide, throw away, or discontinue any operations they do not fully comprehend. The worst companies were those where the president pretended to know about their operations. The important thing is to divide and delegate, not integrate them as in a merger. (Such as spinning off or selling off a segment, exchanging operations with other companies, or withdrawing entirely from a particular line of business.)

A holding company is one option. Nonetheless, in light of the fact that there are many cases where holding companies failed to solve problems, substantial effort may be required to make one a success.

Our research indicates that sticking to a limited range of businesses and avoiding doing what is outside of it, as well as close associations among the company's technology and products, will **produce a great deal of synergy, bringing spontaneous communication among management and employees.**

The establishment of a long-term business plan had no bearing in distinguishing thriving companies from unsuccessful ones. Even some poorly performing companies had well-established plans, possibly made in an attempt to positively influence the stock market.

(2) Being logical—**Thinking over and over again about their own case** instead of believing commonly accepted ideas blindly or mimicking successful peers uncritically

Thriving companies think logically. They thoroughly think about the reason why they would do something.

Although both successful and unsuccessful companies are acquainted with a variety of management approaches, what makes a real difference is whether the management not only knows management approaches but is also capable of thinking for themselves and devising innovative plans. **Successful executives think and think without sticking to conventional wisdom, while many unsuccessful ones accept their consultants' opinions without question or simply imitate their competitors.**

(3) Second fiddle—**Viewing their own company objectively to find out problems**

Our survey indicated that today's many successful presidents, though it might not sound very good, once "played second fiddle" in their organizations.

In many successful cases, radical reform was implemented effectively by leaders who had been brought back to the corporate mainstream after working in peripheral areas of the company, instead of leaders who had moved smoothly up the promotion ladder. (In successful family-owned companies, some members were selected as president just by luck after they had been left out of the presidential candidates' list. In other thriving companies, those chosen as president had worked for many years in a non-elite group or at subsidiaries.)

How did these presidents succeed in improving the profitability of their companies? These leaders were free from complicated connections with past and existing core business projects, which enables them to make daring decisions on their own.

Moreover, these leaders had had frequent opportunities to observe their companies objectively from outside, and were able to easily detect problems because they had remained for a long time outside of the corporate mainstream.

(4) Converting a crisis into a business opportunity

Many profitable companies found a new field of their business at a time when they were faced with adversity. This means that **they have made the most of a critical period during crisis.**

[Example]

- Mabuchi Motor, which had produced motors only for toys, decided to diversify its applications when the company suffered from heavy loss by the import ban on some Japanese toys because of containing lead poison. This decision to diversify secured the further growth.
- Yamato Transport developed the home delivery market because the company faced a crisis when it lost in competition in the long-distance commercial transportation market due to its belated market entry following World War II.

In this survey, we found another category in which successful companies constantly fostered a sense of crisis in the minds of their employees. **Endeavoring not to slip into self-complacency they were frantically inspiring a sense of crisis among their employees.** In many unproductive companies, on the other hand, employees seemed confident about the survival of their company even during a real crisis.

Thus, we concluded that the existence of a culture in which a sense of crisis is inspired among employees is a key to business success.

(5) **Developing in accordance with their ability and keeping an eye on business risk**

Many excellent enterprises showed independence from the capital market. In other words, they skillfully control cash flows. They were controlling the development of their business within the limits of the cash flows generated.

(6) **Management's encouragement of a sustained culture of discipline**

Flourishing companies embody a **"sustained culture of discipline,"** which embraces

both management and employees, without simply the former disciplining the latter.

It is true that the discipline given by the capital market is important. To succeed in business, however, companies must not only accept market discipline, but also **nurture a culture themselves where management and employees have a strong sense of ethics and their mission.**

Orientation toward the welfare of society rather than to money will be the greatest key to a business's long-term development.

Our survey suggests that successful enterprises **contemplate deeply, avoid overextending their operations, approach their work with uprightness, steadiness and enthusiasm.**