

THE STRATEGIC CHOICE MODEL AND INDUSTRIAL RELATIONS IN JAPAN

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Abstract

The strategic choice model in industrial relations advanced by Kochan and his colleagues in 1980s has been the subject of considerable attention. In this paper, I apply this model to understand Japanese industrial relations. After introducing the basic framework of the strategic choice model, I illustrate the historical background of Japanese industrial relations and the transformation of corporate strategies, human resource practices and labor relations using the strategic choice framework. I conclude that the strategic choice model, originally developed in the U.S., can also be applied to Japanese industrial relations.

INTRODUCTION

Since mid 1980s, the strategic choice model in industrial relations advanced by Kochan and his colleagues has been the subject of considerable attention (Godard, 1997). In the field of industrial relations study, the emergence of this model is highly significant for mainly three reasons. First, this model tries to explain the transformation process of U.S. industrial relations by providing a new perspective. As a result, it is successful in understanding the anomalies such as the decline in union membership that traditional industrial relations theories could not provide a good explanation. Second, this model focuses on the dynamic process among management, labor and government as well as the importance of environmental factors. While traditional theories tried to explain industrial relations primarily by environmental conditions, the strategic choice model adds the concept of decision-making in different levels and interaction among players to the old theoretical framework. Third, this model brings the subject of management practices and policies back into the industrial relations research. It promotes a cross-fertilization of research between industrial relations and organizational behavior and human resource management (Kaufman, 1993). In summary, the effort of establishing the strategic choice model is a trial of the paradigm shift in the field of industrial relations research.

Turning our eyes to Japan, its industrial relations are changing. For example, many of large Japanese firms are trying to replace older seniority-based practices with performance-based pay and promotion systems. The number of contingent workforce (i.e., part-time, temporary, and contract workers) are increasing, reflecting the Japanese firms' increased use of externalized workforce. Union membership is declining year after year, and the traditional practice of industry-wide wage negotiations called "shunto" or the spring wage offensive is losing its influence in wage determination among Japanese firms. These changes were accelerated by the long-term recession after the collapse of "bubble economy." However, it also seems that a fundamental structural transformation in Japanese industrial relations had already occurred before

the bubble economy.

Studies on Japanese Industrial Relations were conducted using various approaches including the classical culturalist approach, descriptive institutional approach, functional approach, and neoculturalist synthesis (Shimada, 1983). However, to my knowledge, few studies have explained the recent transformation of Japanese industrial relations using the strategic choice approach. Therefore, in this paper, I apply the strategic choice model (Kochan, et al., 1984; Kochan, Katz, and McKersie, 1986) to understand Japanese industrial relations.

THE STRATEGIC CHOICE MODEL

The strategic choice model was developed when industrial relations in the U.S. were changing rapidly. Because most of the popular theories at that time were generated during periods of relative stability in U.S. industrial relations practices and consequently were overly static, they had difficulty explaining situations when the basic parameters of the system appeared to be changing. For example, Dunlop's systems model (Dunlop, 1958) was widely accepted in 1960s and 1970s. But there were some anomalies in that model. First, the model could not foresee the declines of union membership after that time. Rather, conventional models including Dunlop's model assumed that labor unions were a permanent participant in their employment relationships. Second, conventional models assumed that there was a consensus ideology. But based on the models, we could not tell whether or not managerial values, strategies, and behaviors in industrial relations could change. Third, the traditional industrial relations models treated management as reacting to union demands, pressures, and initiatives. But there could be many managerial initiatives and changes that affected the transformation in U.S. industrial relations.

Given the limitations of the previous industrial relations theory, Kochan and his colleagues add a more dynamic component by developing the concept of strategy, or strategic choice. Based on this, they try to demonstrate that industrial relations practices and outcomes are shaped by the interactions of environmental forces, union leaders, workers, and public policy decision makers. They argue that the significant changes in the American industrial relations system that began in the 1970s were caused by new firm policies dealing with human resource management and labor relations. The most basic change they identify is the more active involvement of senior line management in the formulation of industrial relations policies.

Basic Framework of Strategic Choice Model

The basic framework of strategic choice model (Kochan, et al., 1984; Kochan, Katz, and McKersie, 1986) is derived from the paradigm that integrates the traditional theories of industrial relations systems with the literature on corporate strategy, structure, and decision-making. The model starts with the consideration of relevant forces in the external environment that affect employment relationships. A changing external environment induces organizations to make adjustments in their competitive business strategies. In making these adjustments, the range of options considered are filtered and constrained so as to be consistent with the values, beliefs, and philosophies engrained in the mind of key decision makers. As choices are also embedded in particular historical and institutional structures, the range of feasible options

available at any given time is partially constrained by the outcomes of previous organizational decisions and the current distribution of power among government agencies, corporations, unions, and other organizations. In this way, industrial relations processes and outcomes are determined by a continuously evolving interaction of environmental pressures and organizational responses. The relative importance of either the environment or the organizational responses can vary over time. Therefore, labor or product market changes do not have an independent effect or operate in a unique or deterministic fashion. Then, choices and discretions on the part of labor, management, and government affect the course and structure of industrial relations systems. Moreover, history plays an extremely important role in shaping the range of feasible strategic adaptations.

Three-Tier Industrial Structure

The framework of the three-tier industrial structure is one of the core components of the strategic choice model. This framework divides the activities of management, labor and government into three tiers: (1) a top tier of strategic decision making, (2) a middle or functional tier of collective bargaining or personnel policy making, and (3) a bottom or workplace-level tier where policies are played out and affect individual workers, supervisors, and union representatives on a day-to-day basis. In this framework, the middle tier encompasses the most traditional terrain of industrial relations, since it focuses on the practice of collective bargaining and personnel policy formulation and on the development and administration of the key public policies governing labor-management relations. The tradition of business unionism that dominated the American labor movement made it appear that few important strategic choices or ideology-driven decisions were being made at the top tier. However, the basic decisions involving such things as what businesses to invest in, where to locate worksites, whether to make or buy various components, and the organizational arrangements used to carry out basic strategies all affect industrial relations at lower levels of the system and therefore are central to analysis of industrial relations. Strategic choices that are relevant to the bottom tier are those most directly associated with the organization of work, the structure of worker rights, the management and motivation of individuals or work groups, and the nature of the workplace environment.

The three-tier framework helps identify an important development that previous industrial relations systems theories did not specifically address: the apparent inconsistencies and internal contradictions in strategies and practices occurring at different levels of industrial relations within firms. This framework recognizes the interrelationships among activities at the different levels of the system and helps explain the origins of any prevailing internal contradictions or inconsistencies among three levels. This framework also considers the effects that various strategic decisions exert on the different actors in the system. The three-tier framework encourages analysis of the roles that management, labor and government play in each other's domain and activities.

APPLICATION OF THE STRATEGIC CHOICE MODEL TO JAPANESE INDUSTRIAL RELATIONS

In the following part of this paper, I apply the strategic choice model to Japanese industrial

relations. First, I briefly describe the historical background of Japanese industrial relations in order to understand the important historical factors that affect strategic choices of the players. Second, I examine the recent changes of the corporate strategies by large Japanese firms and analyze their strategic choices from various viewpoints including changing in product and labor markets. Third, I illustrate recent changes in human resource management and labor relations practices in large Japanese firms, which is considered to be influenced by the strategic choices made at the top tier level of the industrial structure.

Historical background of Japanese Industrial Relations

In this section, I describe a very brief summary of the history of Japanese industrial relations based primarily on Nishinarita (1998). Overall, the characteristics of Japanese industrial relations have been viewed as “three sacred treasures” of seniority-based wages, lifetime employment, and enterprise unions. The view was introduced by the 1973 OECD report. Seniority-based pay is explained with livelihood guarantee (people with higher age need much money) and the degree of specific skills (people with longer experience have high skills). Lifetime employment should be accurately expressed with long-term stable employment within the firm. The formation of co-operative attitudes of enterprise unions took place from the 1960s onwards.

Industrial relations in occupied Japan, 1945-9. After the passage of Labor Union Law in December 1945, a number of labor unions were formed and by the end of December 1947, 45 percent of the workforce were unionized. The majority of unions were enterprise-based and comprised of both blue- and white-collar workers. The labor organizations developed a very powerful workers’ movement in opposition to managerial authority. However, the powerful position of workers was destroyed by the Labor Union Law Agreement of June 1949. In that period, a wage system was created for the purpose of securing a livelihood for the people. For example, industry unions and employers in the electrical sector developed so-called the “electrical industry-style” wage system in which payments for security of livelihood accounted for the largest proportion of the total wages.

Emergence of Japanese industrial relations, 1950-59. During this decade, both permanent workers and temporary workers were employed by Japanese firms. The number of temporary workers increased after Korean War broke in June 1950. Japanese firms continued to cut staff including permanent workers and thus employment conditions became extremely insecure. There were significant labor disputes in major enterprises, through which the enterprise union system began to emerge. In the middle of the dispute, alternative workers’ organizations were founded representing more the management point of view. The co-operative enterprise unions were born in this period. Enterprise unions had several weaknesses including weak bargaining power and lack of a universal impact across the industry or nation. To compensate for these weaknesses, union leaders devised a unique wage determination system called “shunto” or the spring wage offensive in 1955.

High economic growth and formation of industrial relations, 1960-73. Co-operative unions were established after following events. First, as the result of the defeat of Miike dispute of 1959-60, the unions lost the effective control of the workplace and labor disputes in the

essential heavy industries disappeared. Second, it became clear that the workplace struggles were to be subordinate to the union's unifying function. Third, federations of co-operative enterprise unions were founded in 1964. The formation of co-operative enterprise unions rendered collective negotiation meaningless. As a result, collective negotiation was transformed into the joint management-labor consultation exercises. This trend allowed a sense of enterprise community to emerge.

Low economic growth and establishment of unionism, 1973-89. In this period, contemporary Japanese industrial relations were formed. After the first oil crisis in 1973, management based upon individual ability began to operate in practical terms. Because the high growth period came to an end, enterprises pushed thorough slim-line management such as dismissing temporary workers or offering temporary leave, natural wastage, encouraging voluntary redundancy, and the development of job displacement and temporary or permanent job transfer. Temporary transfer played a significant role in the context of in-firm long-term secure employment. On the other hand, the number of temporary, or part-time workers increased, which cause the decreasing of the union organization rate. The number of strikes fell dramatically and co-operative enterprise unions were formed in the smaller companies.

Long-term recession after the collapse of bubble economy, 1990-present. To cope with the long-term economic downturn and increasing international competition, a growing number of Japanese firms have adopted performance-based pay and promotion systems for their core employees while increaseing the use of contingent workforce such as temporary, part-time and contract workers. While the aim of these changes is to increase productivity, such diversification of employment and individualization of labor relations have caused various labor problems such as the declining unionization rate, the widening wage gaps among various types of workers (e.g., between regular and non-regular employees), and the increasing number of individual labor disputes.

In summary, the foundation of postwar Japanese industrial relations were emerged, formed, and established by the high economic growth period. Then, it seems that the structural transformation of Japanese industrial relations took place in the low economic growth period, and such a trend has continued to the present, although several environmental changes have accelerated the transformation process.

Transformation of Japanese Corporate Strategies

According to the strategic choice model, Japanese industrial relations systems are a product of the dynamic interacting process between management, labor, and government. That is, the fundamentals of today's Japanese industrial relations were established because of the strategic choices of management and labor as well as government in response to the changes of economic and social environment. In the following, I illustrate the changes of corporate strategies of large Japanese firms, important strategic choices that have influenced other strategic choices made at lower tier of the industrial structure, namely, human resource practices and labor relations.

Market share and growth-oriented strategies. In the high growth period of Japanese economy, Japanese firms obtained competitive advantage in the world market. Abegglen and

Stalk (1985) suggest that Japanese firms or “Kaisha” were market-oriented and concentrated on growth for obtaining competitive advantage. Japanese firms could seek growth recklessly in the expense of profit because they could access to seemingly unlimited source of borrowed funds and they could ignore their shareholders. Japanese firms could take financial risks by increasing financial leverage because of the relationships they had with their financial institutions called “main banks.” Their main banks could reduce their financial risks by establishing close relationships with their clients through shareholdings and access to better information. Also, Japanese financial institutions could lend much money to the high leveraged companies because of the governmental monetary policy that aimed to maintain low interest rates and to avoid a liquidity crisis.

Such corporate strategies in the high growth period were connected to the human resource practices and labor relations by large Japanese firms. In such strategies as seeking growth and market share, mass production and process-oriented innovation were the most important. As a result, human resource strategies focused on training and development of generalist workers who were able to absorb and improve existing technologies rather than specialist workers who focused on innovative technology. These human resource strategies could easily implemented because of the stable labor force based on lifetime employment practices and seniority-based pay and promotion. Collaborative labor-management relationship such as joint labor-management consultation contributed to such stable workforce and strategy implementation. Thus, it can be said that the corporate strategies of Japanese firms could succeed because of the consistent policies among companies, financial institutions, government, and labor organizations.

Changes in market and labor conditions. Several important changes in the market conditions occurred in the 1980s and 1990s (e.g., Ornatowski, 1998). First, Japanese economy became matured in terms of both lower growth rates and growth of service sector, suggesting the end of the catch-up economy. As a result, profit margins of Japanese firms had been falling pre-dating the 1990s recession. After the first oil shock, operating margins began to drop before recovering in the 1980s. And they dropped again during 1990s. Second, large Japanese firms’ international competitive position declined primarily due to yen appreciation and firms’ declining ability to squeeze more costs from suppliers and factory production. In addition, the pressures of globalization forced government to deregulate many domestic industries, which accelerated the needs for changing corporate strategies.

Labor market also changed. First, the percentage of total white-collar workers with much slower productivity growth than blue-collar workers increased dramatically from 36 percent in 1970 to 50 percent in 1990. It caused the serious problem of productivity in Japanese firms. Second, workforce has been aging rapidly, with an excess of older workers. Some 20 percent of the Japanese workforce will be 60 or older in 2020 (Ministry of Health, Labour and Welfare, 1999). These factors caused the rise of labor cost because the older workers were given high salary because of the seniority pay system. Third, after the collapse of the bubble economy, the unemployment rate has increased and repeatedly reached new records, hitting 5.4 percent in 2002 (Araki, 2005). These trends increased the need for corporate restructuring.

Shift to new global strategies. As Japanese economy entered into the post growth era,

high profits through expanding domestic markets became hard to guarantee. Nonetheless, large Japanese firms continued to place strong emphasis on both growth and market share as corporate strategies, and put even greater emphasis on product, marketing, and service innovations. The majority of Japanese firms became unable to keep up with the sharp appreciation of yen and acknowledged the needs for restructuring and for setting up operations overseas. Thus, Japanese firms shifted lower-value-added manufacturing overseas while simultaneously introducing performance-based pay and promotion systems in domestic operations to foster greater white-collar productivity and innovation.

One of the global strategies of Japanese firms was to increase direct investment such as plants and factories to foreign countries. This was aimed at avoiding the currency risk that had ever affected the profits of many Japanese firms. Another reason was to resolve the international trade conflict between Japan and other countries. At the same time, Japanese firms took aggressive cost cutting strategies. For example, Japanese automobile companies faced the need of more cost reduction to maintain their competitive advantages in the international market because of the strong yen, which in 1995 broke through 100 yen to the dollar barrier (Ikeda, 1998). Toyota called 113 component manufactures to realize 15 percent reduction in costs by 1997. Nissan also tried to make cheaper cars by setting the goal of upper target of 40 percent for its own cost reductions. Other firms such as Honda and Mazda also followed the cost cutting strategy. As a result, component makers, many of which were the member of keiretsu in the automobile industry, had a hard time because of the strict requirement for cost reduction by automobile manufactures.

Many Japanese firms tried to improve their efficiency by implementing business process reengineering (BPR) in the early 1990s. For example, Omuron Corp. undertook BPR that was aimed at streamlining and integrating its R & D process, product ordering, and demand-forecasting systems (Boyd, 1995). But unlike the typical American approach to BPR, which was usually dramatic and resulted in a downsized work force, Omron was taking each step excruciatingly slowly and only after numerous meetings and reaching a consensus with everyone concerned, including the company's union. "Unlike the U.S., where people might be laid off, it's a matter of not making quick, dramatic changes, because protecting people is a primary concern," one of the Omron's managers said. Another strategy taken by Japanese firms was to make alliances with other firms by conducting merger and acquisition (M&A). Although M&A had not been popular among Japanese firms, the number of M&A transactions in Japan has been increasing in recent years.

Changes in Human Resource Practices

The strategic choices at the top tier level, namely, direct investment such as plants and factories to foreign countries, cost cutting through restructuring and reengineering, and strategic alliance or merger and acquisition, influenced the strategic choices of the other level of industrial structure, and the overall directions of human resource practices and labor relations in Japan.

In response to the transformation of the corporate strategies, it seems that an important strategic choice was made at the human resource practices level. The choice was to protect

employment security by maintaining lifetime employment while giving up seniority-based pay and promotion, both practices had been a part of the traditional Japanese human resource management. Japanese Ministry of Labor (JMOL) survey in 1994 suggests that the general trend among the majority of large firms was to maintain the lifetime employment system, not abolish it. Larger firms, however, gave considerably less support for the future maintenance of the seniority-based pay and promotion systems (Ornatowski, 1998). In fact, the majority of companies supported the gradual weakening of seniority systems and, in many cases, complete abolishment. From 1983 to 1993, the difference between the average wages of older and younger workers decreased, indicating a flattening of the wage curve and thus a weakening of wages based on seniority. Thus, while lifetime employment was to be retained, seniority-based pay and promotion were generally phased out. Also, in order to protect lifetime employment of regular employees in the period of economic downturn, and under the pressure of cost reduction and corporate restructuring, many firms reduced the number of regular employees by not hiring new graduates, by encouraging the voluntary retirement of older workers, and by utilizing external workforce such as part-time, temporary, and contract employees.

Japanese firms also seek to establish more individualized human resource management systems (Watanabe, 1998). In such systems, companies consider diversity of employees and adjust the personnel treatments to their abilities and needs through providing them with several career courses selection. Also, many firms have started to introduce practices that are used in Western countries. For example, many firms are thinking of implementing U.S. style cafeteria plans to meet the individual needs and reduce the total cost of employee benefit.

In summary, recent major changes in large Japanese firms' human resource practices have centered on revisions to the seniority system and not to lifetime employment. As a result, it seems that the seniority system is being replaced by performance-based pay and promotion systems. Individualization and diversification of employment practices are also the major characteristics of the recent transformation of Japanese human resource management.

Changes in Labor Relations Practices

Changes of corporate strategies and human resource practices are also linked to the changes in labor relations. For example, the proportion of workers joining labor unions in Japan has been continuously declining for a long period of time. The estimated unionization rate calculated by the Ministry of Health, Labour and Welfare (MHLW) reached a peak of 55.8 percent in 1949 and hovered around 30 percent from the 1950s to the 1970s. In the early 1980s, the figure fell to the 20 percent level. In 2003, the estimated unionization rate dropped below 20 percent, 19.6 percent, for the first time since the survey began in 1947 (Moriguchi & Ono, 2004).

The popular Japanese annual collective bargaining called "shunto" or the spring wage offensive is about to collapse. Wage increases have been determined through the spring wage offensive. It is industry-wide unified struggle. According to Daiko (1984), the spring wage offensive has taken firm root as Japan's primary mechanism for wage determination and has had the desired effect. But this spring wage offensive will have no significance when the annual increase based on seniority-based pay begins to collapse. Also, in the process of the spring wage offen-

sive, the level of wage has been determined in a way that keeps same level within industries. However, company unions have begun to accept the difference in wage level within industries. That is, they allow the profitable companies to raise wages higher while some companies that are not profitable do not raise wages.

Another change in Japanese labor relations is associated with the increase of non-regular workers (e.g., temporary, part-timer and contract workers). In 1990, non-regular workers made up 20.2 percent of the Japanese workforce, whereas in 2004 this has risen to 31.5 percent (Araki, 2005). This has been caused by the spread of outsourcing practices among Japanese firms. The use of non-regular workers to “buffer” regular workers from market uncertainties is expanding in the current Japanese economy (Lincoln & Nakata, 1997). This is associated with the decline of union membership because traditional enterprise unions solely organized regular employees while non-regular workers remained unorganized. Non-regular workers usually suffer from poor working conditions and are left unprotected and outside of the union organizations. For example, the wage gap between regular and non-regular employees is widening. According to MHLW, if the wage of regular employees is set 100, then the wage gap between female regular employees and female part-time workers was 58.9 in 1990 and 54.3 in 2001 (Yamashita, 2005).

In summary, changes of labor relations in Japan are characterized as the decreasing rate of union membership, losing influence of shunto or the spring wage offensive in industry-wide wage determination, and increasing number of non-regular workers such as temporary, part-time, and contract employees. It seems that the important choice has also been made at this level. That is, the nature of labor-relations in Japan is changing from the collective labor-management relations to individual-based labor-management relations. This is also associated with the individualization and diversifications of employment practices.

DISCUSSION

I have illustrated the historical background of Japanese industrial relations, recent transformation of market condition and corporate strategies, and changes of human resource practices and labor relations in Japan. Applying the framework of the strategic choice model, it is suggested that Japanese industrial relations systems are a product of the dynamic interacting process between management, labor and government. That is, the fundamentals of today’s Japanese industrial relations were established not just because of the economic situation or other external environments but also because of the strategic choices made by different players.

In 1980s and 1990s, the environment surrounding Japanese firms dramatically changed and it enforced the strategic choices among Japanese firms. The significant changes in the environment were caused by the long recession after the collapse of bubble economy. However, it seems that even before the bubble economy, the structural transformation had already started.

At the top tier of the management level, the main choices made by large Japanese firms were (1) direct investment such as plants and factories to foreign countries, (2) cost cutting through restructuring and reengineering, and (3) strategic alliance or merger and acquisition. The role of top tier of the industrial structure was to decide the corporate directions in the context of long recession after the bubble economy, which also affected the overall directions of human re-

source practices and labor relations.

The changes in human resource practices and labor relations are associated with the strategic choices in the lower tiers of the industrial structure. Because Japanese labor relations have been rather collaborative than competitive, it seems that the interaction between management and labor has reached the way that fits into the recent trend or direction. The basic direction is to protect employment security through the long-term employment practice and to give up the seniority-based pay and promotion. However, the problems of aging population and increasing number of white-collar workers who are less productive may force the further changes of human resource practices such as giving up the life-time employment, too.

Enterprise unions have been the dominated form of unionism in Japan. "The enterprise union seems to employed workers to be the most acceptable and effective form of union organization (Shirai, 1983)." According to the statistics as of 1997, 95.6 percent of unions in Japan are enterprise unions and 91.2 percent of all unionized workers are organized in the same union (Araki, 2005). To compensate for the limitations of enterprise unionism such as the lack of bargaining power, shunto or the spring wage offensive has played a significant role in collective bargaining. However, the spring wage offensive is losing its impact in industry-wide wage determination as a result of the changes of the economic situation and human resource practices. Also, because the number of non-regular workers who usually do not join unions is increasing, the proportion of union membership is declining year after year.

Japanese labor relations have been characterized as collaborative. The joint labor-management consultation is one example. This characteristic is based on the community-like labor-management relationship. However, it is uncertain whether this type of labor-management relationship will continue in the future. According to the strategic choice model, the form of the future labor relations depends on the strategic choices among management, labor and government at the different levels of industrial structure. It is predicted that in Japan, the economic and other situations will become more challenging for all of the parties. Many firms will try to increase productivity through such employment practices as diversification of employment and individualization of human resource practices, but it may further promote various labor problems such as the widening wage gaps among various types of workers and the increasing number of individual labor disputes.

With regard to individual labor disputes or personal grievance, managers and supervisors in the workplace usually deal with personal grievances (Japan Institute of Labour, 2002; Sato, 2000). However, as managers and supervisors become busier as Japanese firms reduce the number of employees to cut labor cost, their capability of handling grievances and their leadership skills is declining (Fujimura, 1999). In this way, for managers and supervisors, the labor relations in the day-to-day operations would become more challenging in the future.

In conclusion, it seems that the strategic choice model can be applied to the understanding of Japanese industrial relations, although historical background and institutional structure are different from those of the U.S. Compared with the previous theories of industrial relations, the strategic choice model is more dynamic, which fits well with Japanese industrial relations that are currently under transformation. However, the strategic choice model does not predict precisely how the future of Japanese industrial relations looks like. Instead, the model suggests

that the future directions of Japanese industrial relations are derived from the dynamic interacting process between management, labor and government, and their strategic choices are somewhat constrained by the historical context and environmental factors in Japan. Some of the symptoms of the future Japanese industrial relations may already be underway today.

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