Expat-run Japanese firms miss China boat

Jochen Legewie

One of the most striking characteristics of Japanese firms abroad is their high reliance on expatriates in running their subsidiaries – a management practice for which they have been both praised and criticized worldwide in the past. In China this approach fits well only for some firms.

According to a recent survey by the Japan-China Investment Promotion Organization Japanese export-oriented affiliates in China are quite profitable with only 15% turning in losses. Among local market-oriented affiliates by contrast more than 40% are operating in the red, only few manage to generate substantial profits. By contrast to Western companies the majority of Japanese firms in China is still export-oriented. In 1999 only 30% of Japanese affiliates sold half of their output within China. But the trend clearly turns toward a stronger local market orientation. Hence Japanese firms must urgently address the issue of low profitability. Can this be related to expatriate use?

Three factors are important to be considered here. First, qualified ambitious local workers are difficult to attract and keep for Japanese firms. A major reason for the low popularity of Japanese employers is the insufficient participation of local workers in decision-making and their limited career opportunities that result out of the emphasis on Japanese staff for higher management positions. Still only 10% of Japanese joint ventures in China are headed by a non-Japanese while this share is much higher for Western competitors, especially for firms from the US, the UK or France.

Second, expatriate-run firms often fail to show a quick market response as they come with a clear separation between Japanese top management and local workers. The lack of a middle management layer restricts joint decision-making and hinders information flows bottom-up from the shop floor to top management.

Third, delays and mistakes in bottom-up information flows do not only impede a flexible market response within China. They also limit information flows between Chinese subsidiaries and Japanese headquarters as well as between single overseas subsidiaries. Hence they lead to a limited organizational learning at the global corporate level.

These management problems of Japanese firms are known from other countries as well. Often however, efficiency gains that result from standardization by a centralized expatriate-based control system offset these problems as shown by the successful Japanese transplants in the US or the UK.

But the situation in China is different. This country presents a very unstable and rapidly developing environment in the political, legal, economic and even socio-cultural sphere. At the same time, it promises an enormous market potential. In addition, a sophisticated industrial structure that allows multinationals to increasingly integrate their Chinese production activities into their global production networks is emerging (for example electronics in South China). This combination of uncertainty and instability, a huge domestic market potential and a well-developed industrial structure in some areas makes the business environment in China a unique one. It sets it apart not only from industrialized countries but also from places like Thailand or Malaysia.

The implication for those Japanese firms in China that either aim at the local market or the further integration of local production activities into regional and global networks is clear: reduce the number of expatriates and switch to alternative coordination measures which are formal directives, management by objectives, and control by socialization and networks. A focus on formal and output control mechanisms (typical for US firms) certainly avoids expatriate related problems. Within the highly complex and instable Chinese environment, however, a crucial role must be attributed to control by informal measures and hence socialization and networks.

Hereby we refer for example to the creation of shared values and goals, the informal horizontal flow of information between executives, or the set-up of task forces and temporary cross-functional teams. At home Japanese firms are famous for the successful use of socialization to build up flexible and highly functional business networks. In China they have so far failed to rebuild this strength and perspectives for a fast change remain dim.

The Japanese approach of doing business overseas is still characterized by strong ethnocentric elements. Where socialization and networks have been enforced at an international level they remain biased to Japn. We see this in the lack of strong regional headquarters and the lack of regional board meetings outside Japan. Throughout the 1990s larger Japanese corporations have introduced extensive training programs for Chinese workers in Japan and simultaneously built up personal executive networks. But these efforts also remain bilaterally restricted as they rarely include other Asians.

Without the necessary language skills, namely proficiency in English, such international networking will continue to be difficult for Japanese firms. An even bigger obstacle on the way to real internationalization lies in ethnocentric elements within the Japanese society itself. Over the last few years more and more Chinese have entered the regular career path with Japanese firms in Japan with some being promoted to section chief or head of a joint venture in China. However, over this course quite a few decided to switch to the Japanese nationality citing this to be more convenient for themselves and their families.

Whether we regard this as an example for a persisting ethnocentrism in Japan or deal with it in terms of an insider-outsider mentality is of less significance. Important is the fact that Japanese firms in China still have a long way to go beyond their current export-oriented internationalization stage and to achieve sustainable profitability in local market-oriented business as well.