

Control and coordination of Japanese Subsidiaries in China – Problems of an Expatriate-Based Management System

Jochen Legewie

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Abstract

This paper analyzes the international management control (IMC) system that Japanese multinational companies (MNCs) employ to coordinate the activities of their subsidiaries in China. It focuses on the role of Japanese expatriates in this IMC system and assesses their performance. In the process, it offers a comprehensive evaluation of the organizational fit of the Japanese IMC model within the current Chinese business environment. Taking Japanese firms as its the subject, the analysis identifies areas of incongruity explains the underlying reasons for problems with the IMC model. In doing so, this paper argues that the Japanese expatriate-based control system in China (as in many other parts of the world) continues to be characterized by an ethnocentrism that prevents a real internationalization of overseas operations in the ‘transnational’ sense.

1 1 Introduction

The control and coordination of overseas subsidiaries is a permanent task all multinational companies (MNCs) face regardless whether they are from Japan, Europe, the US, or elsewhere. Defined as a means to achieve common organizational goals, international management control (IMC) directly relates to the general global-local dilemma of internationally active companies. MNCs must find the optimal mix between centralized and decentralized decision-making while they employ various control and coordination mechanisms. Following Bartlett (1986), Prahalad and Doz (1987) and, Bartlett and Ghoshal (1989), most authors describe company strategies at either the headquarters or subsidiary level by differing between advantages from *integration/coordination/globalization* on one hand and advantages from *differentiation/responsiveness/localization advantages* on the other.

Attempting to solve this dilemma, recent international management theory suggests that MNCs move toward a kind of loosely coupled network organization (see *e.g.* Galbraith and Kazanjian 1986; Hedlund 1986; Porter 1986, Prahalad and Doz 1987; White and Poynter 1990). The final outcome is often described as a ‘transnational’ company (Bartlett and Ghoshal 1989). Within such an organization, the management of human resources obviously is very important. Coordination shifts from formal to more informal and subtle mechanisms (Evans 1986; Martinez and Jarillo 1989).

Within such an indirect control and coordination system, the employment of expatriates plays a crucial role (see *e.g.* Child 1984; Edström and Lorange 1984; Kobrin 1988; Daniels and Radebaugh 1989; Evans 1991; Roth and Nigh 1992). Most authors draw on the observations of Edström and Galbraith (1977) who were among the first to find different patterns of expatriate employment in the overseas subsidiaries of otherwise similar MNCs. Echoing Wiechmann (1974), they conclude that expatriates provide an alternative to formal control mechanisms and centralization creating a control and coordination system based on socialization and informal communication.^{1[1]}

Japanese MNCs are well known for the concentration of expatriates in their overseas subsidiaries (Tung 1982; Negandhi and Welge 1984; Kopp 1994).

^{1[1]} For a more detailed introduction to the topic of international management control and the use of various control mechanisms by MNCs from both a theoretical and empirical background, see Harzing (1999).

Based on the numbers of expatriates alone, many authors claim that by international standards Japanese MNCs show a high degree of centralization in decision-making (Agarwal 1993; Harrison et al. 1994; Jain and Tucker 1995). By contrast, an equal number of studies have arrived at the exact opposite conclusion, *i.e.* US and most European companies tend to exert more centralized and formalized control over their overseas affiliates than their Japanese counterparts (Otterbeck 1981; Negandhi 1987; Kriger and Solomon 1992; Wolf 1994). Ferner offers a key to understanding these contradictory findings. He describes the Japanese approach as ‘strong but informal centralised co-ordination of foreign operations, highly reliant on establishing an international network of Japanese expatriate managers’ (1997, 21–22). Clearly, Japanese expatriates play a crucial role within any Japanese international management control (IMC) system. What remains is to further explore the real degree of formality and centralization of the Japanese system of international management control and its specific suitability in different environments.

This paper does exactly that. However, it does not attempt to tackle this question in a general manner but rather focuses its analysis on the control and coordination of Japanese subsidiaries in China. Drawing both on empirical research in China and Japan and the relevant secondary literature, the author presents an overview of the specific expatriate-based control system Japanese MNCs currently employ in China and evaluates its organizational fit. The analysis here concentrates exclusively on Japanese firms and identifies areas of incongruity and explains the underlying reasons for problems with this specific IMC model in China. Doing so this paper demonstrates that the Japanese expatriate-based control system in China continues to be characterized by a special kind of ethnocentrism. It is argued that this ethnocentrism will prevent a fast shift to international operations in the ‘transnational’ sense though such a shift will become necessary for a rising number of Japanese firms over the next years.

The exclusive focus on Japanese operations in China has been chosen for several reasons. First, China confronts Japanese MNCs with a unique business environment. It is characterized by both high uncertainty and instability (typical for many developing countries) and a huge domestic market potential and a sophisticated industrial structure in certain areas (typical for many developed countries). This unique combination comes with special requirements for IMC systems. Second, while China is of growing importance for most MNCs it is of special significance to Japanese firms. Being an Asian country and thus lying in the Japanese ‘backyard’,

Japanese MNCs cannot afford to lose out to Western competitors in China if they want to compete against them on a global level.

Third, with regard to this special challenge in China in terms of requirements and importance, a closer analysis of the current situation in China might offer the most telling country-study to arrive at deeper insights into the general functioning of Japanese IMC, its problems and eventual ways to overcome them. Thus findings derived here might offer results applicable to Japanese operations elsewhere too. To facilitate such a broader view, this paper integrates the analysis of Japanese operations in China into Harzing's typology of international control and coordination mechanisms (1999). As such it is the first paper of its kind, hopefully kicking off many other theoretical and empirical studies following this approach that is well-suited for international comparisons.

The paper is structured as follows: Section 2 presents a typology of international control and coordination mechanisms and places the Japanese IMC system in international perspective. Section 3 outlines the characteristics of the current business environment in China that requires foreign firms to simultaneously emphasize local flexibility and cross-border organizational learning. Section 4 describes the current state of Japanese IMC in China and analyzes its most common problems and the reasons for these problems. The final section summarizes the findings and offers an outlook on future development in various industries.

2 2 General characteristics of the Japanese international management control system

2.12.1 Typology of international management control systems

Putting the Japanese IMC system into international perspective requires a typology of control mechanisms. Harzing's classification scheme (1999) is the most convincing of this kind. It accommodates other typologies that have been developed to date, including those of March and Simon (1958), Lawrence and Lorsch (1967), Galbraith (1973), Edström and Galbraith (1977), Ôuchi (1979), Mintzberg (1983), Kenter (1985) and Martinez and Jarillo (1989).

Harzing's typology uses two dimensions 'personal/impersonal' and 'direct/indirect', to generate four distinctive groups of control

mechanisms employed by MNCs. The four different groups are defined as follows (also see Figure 1):

1) *Personal centralized control* denotes the idea of hierarchy. It relates to decisions taken at the center or top level of companies, followed by direct personal surveillance of their execution.

2) *Bureaucratic formalized control*, the other direct behavior control mechanism, is by contrast, impersonal. Written manuals attempt to standardize the behavior of employees by clearly prescribing courses of action to be followed.

3) *Output control* resembles market approaches to coordination by focusing on outputs rather than on behavior (as the other three mechanisms do). The firm measures outputs such as production, sales or financial data. By comparing these results with pre-specified goals, the final output is evaluated and controlled, rather than controlling inputs, *i.e.* the behavior of single employees.

4) *Control by socialization and networks* describes all other control mechanisms; in other words, mechanisms that are not hierarchical, bureaucratic, formal, or output oriented. There are three main sub-categories: a) socialization by sharing organizational values and goals, b) informal and horizontal exchange of information with an emphasis on non-hierarchical information flows between all managerial levels, and c) temporarily formalized cross-departmental relations in the form of task forces or cross-functional teams.

Fig. 1: Classification of control mechanisms

	Personal/Cultural <i>(founded on social interaction)</i>	Impersonal/Bureaucratic/Technocratic <i>(founded on instrumental artifacts)</i>
Direct/Explicit	Personal centralized control	Bureaucratic formalized control
Indirect/Implicit	Control by socialization and networks	
		Output control

Source: Harzing 1999, 21

While personal centralized control and bureaucratic formalized control aim at controlling behavior directly and explicitly, the two other groups do so indirectly and implicitly. Similarly, personal centralized control and control by socialization and networks are based on personal exchange and social interaction. The other two are clearly of

an impersonal and bureaucratic nature (for a more detailed description, see Harzing (1999, 7–31)).

Of course all of these control mechanisms do not work in isolation but rather, interact, as is stressed by Lawrence and Lorsch (1967), Edström and Galbraith (1977), and Martinez and Jarillo (1989). For example, one might see a combination of the first two groups in situations characterized by environmental stability, a low level of technological development and transparent transformation processes. There would be an emphasis on personal, centralized control in smaller companies and bureaucratic, formalized control in larger companies. By contrast, a combination of output and social/network controls is better suited to situations with high environmental instability, complex technology, and limited knowledge of transformation processes. Here, there would be an emphasis on output control if there were measurable outputs and on socialization and networks if there were not (Child 1984, 168).

This typology of control mechanisms deliberately excludes expatriates as a means of control. Rather, it regards them as an alternative, though one that can ultimately perform important functions. The use of expatriate as a control measure usually takes two different forms. It can strongly substitute or complement personal, centralized control by headquarters and it can assist in the cultivation of shared values and thus facilitate control and coordination through socialization and networks.^{2[2]} Both functions are especially important for Japanese MNCs.

2.2 International management control of Japanese MNC in international comparison

Based on the typology presented above, Harzing conducted a far-reaching international survey in 1995/96 that identified similarities and differences in the subsidiary control mechanisms of MNCs from the US, Japan, and seven European countries. Covering more than 120 MNCs operating in eight different industries and some 1650 subsidiaries in 22 different industries, this survey is by far the most encompassing and systematic to date. The

^{2[2]} There are two other important functions of expatriates. The first is position filling or the transfer of technical/managerial knowledge to subsidiaries abroad; the second is management development for the people sent abroad, *i.e.* to give them international management experience and thus foster international market experience at the mother company level (Edström and Galbraith 1977; Beechler 1993; Harzing 2000b).

results of the study offer the best data base for comparisons of the various patterns of IMC employed by multinationals of different countries, from different industries, and with different organizational models (see Harzing 1999, 2000a).

Fig. 2: Use of control mechanisms in subsidiaries of MNCs of different countries

	Japan	US	Germany	Sweden
Personal centralized control	medium	medium	very high	low
Bureaucratic formalized control	low	very high	medium-high	medium
Output control	very low	medium-high	high	medium
Control by socialization and networks	low	medium	medium	high
Expatriate control	very high	very low	high	medium

Source: Harzing 1999

Here we focus on the so-called country-of-origin effect and compare the characteristics displayed by Japanese MNCs to those of three other countries in Harzing's study: the US, Germany, and Sweden (Figure 2). We have selected these three countries as each stands for a distinctive different IMC model. At first sight we notice a distinctive feature of the Japanese IMC model that sets it clearly apart from MNCs headquartered in all other countries of this study. While Japanese MNCs exhibit a very limited use of the four 'classic' control mechanisms, they nearly exclusively rely on direct expatriate control. German MNCs, for example, that also rely on expatriate, at the same time employ other means of control, especially personal centralized control and output control as well. US companies generally employ an IMC model with a high dependence on bureaucratic, formal control and output control while foregoing the use of expatriates as a means of control. Thus, they constitute the exact opposite of Japanese MNCs. Swedish MNCs fall in between these two extremes, but they too clearly differ from their Japanese counterparts, due to their strong reliance on control by socialization and networks.

Combining the observations by Tung (1982), Kopp (1994) and others as described in section 1 and these findings of Harzing, we can state that generally, Japanese MNCs employ large numbers of expatriates in their overseas subsidiaries and strongly rely on them to control and coordinate

their overseas activities. Looking at the medium score for personal, centralized control and the low score for control by socialization and networks, we can also conclude the following. Expatriate control by Japanese takes the form of a substitution of personal surveillance by the center (headquarters in Japan) rather than a facilitation of control and coordination attempts by socialization and networks.

The main reason for the high degree of centralization applied by most Japanese MNCs is the so-called 'global' organizational model (see Bartlett and Ghoshal 1989). Most MNCs in industries such as automobiles and electronics, industries characterized by standardized consumer needs, price competition, and economies of scale, follow this model. Hence, these industries emphasize highly integrated and efficient production systems over responsiveness to various local markets. Many Japanese MNCs come from these industries, partly explaining their high degree of centralization. Interestingly, most Japanese companies in other industries have also followed this global business model. This has to be seen as the international extension of a domestic business model that is also characterized by centralization and powerful headquarters (see Hatch and Yamamura 1996; Seki 1997).

The high reliance on expatriates can be explained mainly by two factors. First, it reflects the extraordinarily strong personal focus of the Japanese management style at home and thus the influence of the national business system abroad (Ferner 1997). In other words, it is an international extension of the national business system that transfers central decision-making to the MNC (Ferner and Quintanilla 1998). At the same time, it reflects an inability to transfer control mechanisms that work at home abroad. This holds especially true for control and coordination by socialization and networks. This control mechanism is without doubt a specific and important characteristic of the Japanese domestic business system. The very low application abroad, however, suggests major problems with its applicability in Japanese IMC systems in China and will receive detailed treatment in section 4.^{3[3]}

^{3[3]} It can also be argued that expatriate use is cheaper for Japanese firms than it is for US or European MNCs. While Western expatriates tend to bring their spouses and children abroad with them, many more Japanese expatriates go for their overseas secondment alone, leaving their family at home (mainly because of schooling needs). Hence Japanese firms save substantial amounts of money for additional overseas lodging, school fees, and other family related expenses.

To sum up, the term ‘transplants’ – often used to describe Japanese production systems abroad – also seems well-suited as a means for characterizing a Japanese approach toward control and coordination of their overseas subsidiaries. Japanese MNCs rely on expatriates to facilitate the transfer of their specific ownership advantages abroad. Expatriates have helped in the international extension of efficient production systems, especially in the rather stable environments that characterize most industrialized countries (Negandhi and Belga 1982). In the unstable environments of developing countries, expatriates contributed to levels of flexibility higher than those possible under formal, bureaucratic rules or output control mechanisms (Negandhi 1982).

However, this centralized, expatriate-based approach has its limitations. First, there are industries that mainly require local responsiveness and thus are unsuited to the ‘global’ business model. This was best demonstrated by the internationalization failure of branded packaged products leader Kao in the 1980s (Bartlett and Ghoshal 1989). Second, the expatriate-based approach can also lead to problems in other fields that require cross-sectional information exchange and horizontal communication flows that go beyond Japanese dominated structures (Ferner 1997, 23). In broader terms, this relates to the debate over whether or not ‘the innovations pioneered by Japanese corporations ... constitute a discrete package of organizational techniques which can be lifted from its original social and economic context and adopted elsewhere’ (Elger and Smith 1994, 2). This debate raises the question whether Japanese production and management practices are location-specific or of universal relevance. Those that answer in the negative include Dunning (1986), who suggests that Japanese efficiency is location-specific to Japan. Kenney and Florida (1993) argue that an overseas transfer of a wide range of Japanese management practices is possible, but only where ‘functional equivalents’ to the Japanese socio-economic environment exist (also see Taylor 1999). We will return to this point in the next section on current control and coordination problems of Japanese MNCs in China.

3 3 The business environment in China

At present, China presents foreign investors with an environment characterized by high complexity and rapid development. Whether we look at the political, legal, economic, or social-cultural sphere, all areas display both crude and effective complexity to use the terms of Gell-Mann (1995) (see also Napier and Vu 1998, 50–55). Crude complexity describes the

number of elements in a system and the number of connections among them. Effective complexity is the function of the irregularity and unpredictability of a system. By both measures China exhibits one of the most complex business environments with its large numbers of different actors at the various layers of business and politics. This is combined with huge regional differences and general instability (Napier and Vu 1998; Child 2000).

At the same time, China made rapid progress toward clearly defined goals throughout the 1980s and 1990s. Economically, China has displayed impressive growth rates and upgraded the level of technology used in industry and by workers. Politically, the situation has stabilized and transparency has increased. In part, this can be attributed to a legal environment that, in anticipation of the introduction of WTO regulations in the near future, promises greater transparency and stability for business. Finally, there have been substantial changes in the social-cultural sphere. One can see the departure from the 'iron rice-bowl' regime to a more individualistic market-based society, at least in the coastal regions (Warner 1995; Child 2000).

These trends mean that China will continue to rise in strategic importance for foreign companies. This holds true despite the problems that result from the highly complex and unstable business environment. On the one hand, China obviously presents a huge market potential, an argument that needs no further elaboration here. On the other hand, China will become more important as a link in the global production networks of MNCs. Continuous improvements in technology will allow MNCs to use China both as an inexpensive site for simple production processes and as a site for higher value-added activities that can be integrated on a global scale.

This combination of an unstable business environment and the rapidly developing economy with its promise of a huge future market sets China apart both from the developed markets in North America and Europe and from the smaller developing economies as Thailand, Poland, or Brazil. In regard to international management control, this setting presents a special challenge to foreign MNCs. They have to exhibit a high level of local flexibility in the rapidly changing business environment. At the same time, the cross-border integration of their Chinese operations becomes increasingly important. Ultimately, they must achieve both the ability for a flexible market response as well as organizational learning and innovation on a global scale.

4 International management control of Japanese MNCs in China – Current state and problems

4.1 Japanese expatriate use and control in China

Since the early 1990s Japanese firms increased investment in China and stepped up their local presence. As a result, by April 1999 the number of Japanese wholly-owned subsidiaries or equity joint ventures in mainland China had risen to more than 1,400 (Tsûshô Sangyôshô 2000, 6) with some of the large multinational companies (MNCs) like Itochu, Matsushita, or Fujitsu having more than 30 Chinese affiliates each. The control and coordination of these foreign affiliates is a permanent task for Japanese MNCs that seem to rely on expatriates in China in similar ways as they do in other parts of the world (see section 2.2).

The mere numbers of Japanese managers in Chinese joint ventures and wholly-owned subsidiaries confirm the well-known picture of extensive expatriate use. Larger MNCs like NEC, Mitsubishi Electric, Fujitsu, or Matsushita, for example, employ between 100 and 250 expatriates on a permanent basis in China. Data collected by the author shows that expatriates on average account for about 2% of the workforce in Chinese subsidiaries of Japanese MNCs (also see Tôyô Keizai 2000; JETRO 2000) a figure clearly above that for their Western counterparts, especially US and UK firms.

A large number of these Japanese expatriates (relatively more than in subsidiaries of Western MNCs) are engaged exclusively in technological transfer and the supervision of production techniques and processes (Taylor 1999, 861). Yet a majority remains in charge of control and coordination of the subsidiary's relations with headquarters. Hence, the IMC model employed by most Japanese MNCs in China follows the Japanese model described in the previous section. Interviews of the author with representatives about 20 large Japanese multinationals regarding the main functions of Japanese expatriates in China confirmed this finding.

Interestingly, these interviews also showed two different patterns of judging extensive expatriate use. One group of Japanese managers did not cite any special IMC problems beside the high costs of sending Japanese employees to China. Most of them belonged to firms with manufacturing operations in China that were highly export-intensive and only little direct exposure to the Chinese market. The other group was made up by employees of companies

or certain division groups with a strong focus on sales to the Chinese market. These managers tended to view the relative high expatriate use of their firm far more critically and sometimes related it to concrete labor problems, especially the problem of securing qualified workers. We will now try to shed more light on these problems and offer explanations for the different perceptions of the suitability of expatriate use in China.

4.2 Problems of Japanese expatriate control in China

The strong reliance on expatriates in China offers Japanese MNCs the same advantages and disadvantages in coordinating and controlling their subsidiaries as it does in other parts of the world. This IMC model is especially well-suited for the large number of Japanese manufacturers that are heavily engaged in export-processing trade. Their plants in China do not only export most of their output under strict control by Japanese headquarters but are also highly dependent on their headquarters in areas such as inputs, financing, or production technology. In these cases, the typical transplant type of business, the Japanese IMC model still provides an efficient way for many Japanese MNCs to control and coordinate their China operations.

However, particularly within a context of a shift in focus toward the Chinese domestic market and improvements in production activities in China, the strong reliance on expatriate control increasingly results in a number of problems for Japanese MNCs. Such problems are described by Leung et al. (1997), Ma (1998), Taylor (1999) or Nakamura (2000) who argue that there are two main problems for Japanese IMC systems in China:

- (1)(1) qualified local workers become frustrated and leave the company because of insufficient participation in decision-making, limited career opportunities and a non merit-based appraisal system; and
- (2)(2) firms suffer decreased ability for flexibility in their response to the market because of limited information flows from the bottom. This is due to a missing layer of middle management and a subsequent lack of joint decision-making of expatriates and local employees.

Ma (1998) describes the unpopularity of Japanese firms as employers among Chinese workers as compared to their US and European competitors. This preference is not only based on the usually higher wages paid by Western firms but also comes as a reflection of differences in the general systems of

appraisal and performance assessment. Nakamura (2000) makes the same point in his description of the dissatisfaction of Chinese employees in Japanese wholly-owned subsidiaries around Shenzhen. All of his Chinese interview partners complain about not being involved in the decision-making process and are generally pessimistic about their career opportunities. A special problem is the wide-spread dissatisfaction of Chinese employees with assessments of their performance by their Japanese superiors. Interviews of the author with Japanese managers in China even suggest that, at times, personnel appraisals become assessments of language ability, rather than evaluations of work performance.

Leung et al. (1997) confirm these observations with their comparative study on job satisfaction in Chinese hotels under Japanese and Western management. They show that employees working with Japanese expatriates were far less satisfied than those who were working with expatriates from the West. Those working with the Japanese perceived that they were rewarded less fairly in relation to their performance and in comparison to other employees in hotels under Chinese or Western management. Finally, the heavy reliance on expatriates also meant limited career opportunities for Chinese managers, constituting the famous 'rice-paper ceiling' of Japanese companies (Kopp 1999). In Japanese MNCs, cases of non-Japanese heading a joint venture in China are very rare. A recent survey by JETRO found that only about 10% of Japanese were headed by a non-Japanese (2000, 24). This contrasts sharply with many US firms and even some German companies (also famous for their high reliance on expatriates). In 1999 for example, out of the heads of nine joint ventures involving the German chemical firm BASF only three were Germans. Managers from Norway, China, Korea, Indonesia, and Malaysia held the post of general manager at the other six.

In total, these factors keep Japanese MNCs in China from attracting or keeping the most qualified personnel. Labor turnover is directly related to job satisfaction and opportunities, as shown by Wong and Law (1999). Fisher and Yuan (1998) confirm this view with their study on employee motivation in China. They show that most Chinese managers prefer salaries and promotions based on individual performance. This requires measurable goals (output control) rather than subjective, personal assessments by expatriates. Older workers, by contrast, tend to prefer job security and hence do not show any preference for Western over Japanese employers. Interestingly, this fact was stressed by many Japanese interview partners of the author linking it to an eventual superiority of the Japanese employment system in the long run.

Such a view, however, does not help Japanese firms in the current situation in which they compete with other MNCs for young and qualified employees. The seriousness of this problem is clear in the results of the January 2000 JETRO survey of 674 Japanese firms in China (JETRO 2000). While 55% of the respondents cite ‘securing of qualified workers’ as the most important success factor for business in China, 35% report problems related to labor and human resources. The causal relationship between the Japanese IMC system and labor problems becomes even more apparent when we look at the numbers for wholly-owned subsidiaries. Without the interference of a local partner, Japanese MNCs are freely left to implement their own systems of labor management and the story becomes even more telling. Among wholly-owned subsidiaries, 40% of all respondents cite human resource related problems, making them the second largest headache for Japanese MNCs in China after ‘tax and legal problems’ (JETRO 2000, 88–89).

In addition to the problem of securing qualified workers, the second major problem, facing Japanese MNCs is their inability to respond flexibly to the market. Nakamura (2000) and Taylor (1999) describe this challenge well. By dominating decision-making, Japanese managers do more than frustrate Chinese employees. They also hinder a free and constant flow of information from the shop floor to the top management. A study by Taylor of 31 Japanese wholly-owned and joint venture manufacturing plants in China highlights this problem. On the one hand, he finds that some Japanese MNCs have deliberately ceded control of certain organizational functions to Chinese employees, especially in the area of human resource management. On the other hand, however, he detects a ‘tendency to dichotomize between either Chinese or Japanese control, with little attempt to make joint decisions’ (Taylor 1999, 864). This reflects language and cultural barriers between Japanese and Chinese managers but also the fact that most Japanese expatriates are sent to China to do a specific job based on their area of expertise.^{4[4]} Hence, most focus on their specific jobs rather than seeking to cross-fertilize management knowledge and practice. This results in a striking lack of decision-making between locals and expatriates (Taylor 1999 863–865). As a result of the missing middle layer of management, there is also no proper system for monitoring the output of local personnel and channeling their market and customer knowledge to the Japanese members of top management who formulate business strategies.

^{4[4]} Language barriers, however, are slowly but gradually lowered as more and more Japanese expatriates tend to speak Chinese or at least understand a little which was rarely the case 10 years ago.

Kawashima and Konomoto (1999) report exactly the same problem for Japanese subsidiaries in Taiwan, Hong Kong, Singapore and the Philippines. They note a very negative impact on the ability to react to rapid changes in the operating environment. Their observations in these four countries also confirm the findings regarding the negative effect of frustrated local employees described earlier. Kawashima and Konomoto find that Japanese subsidiaries in East Asia display a strict top-down structure dominated by senior Japanese management and headquarters (1999, 21). This allows for an organizational structure that is totally goal-oriented and that has a clear and effective chain of command. In this, it is well-suited to a stable environment. Even so, these firms give their local staff little autonomy and opportunity to channel information to their superiors making a flexible market response under rapidly changing conditions difficult. In China, Japanese operations face exactly the same problem. The complexity of the environment and the speed of changes there are even faster and more unpredictable. Hence disadvantages of the Japanese expatriate-based IMC system count even stronger in China than they do in Taiwan or Singapore.

In addition to problems that arise from Japanese approaches to IMC within China, one must also look at the international level. Section 2 stressed the rising importance of China as both a growing domestic market and an emerging link in the global production networks of MNCs. This situation requires that the correct type of information flow quickly from the Japanese subsidiary to the headquarters in Japan. Information must also flow between subsidiaries in China and other (especially Asian) countries. Delays and mistakes in generating correct information in China resulting from the absence of local hires in middle management that can connect the top level to the factory or shop floor are an important problem. The main problem, however, lies in the inability of Japanese MNCs to generate a continuous, international exchange of information. And it is exactly here where the Japanese IMC system often fails to provide the sufficient structure. By stressing expatriate control over other means, especially control by socialization and networks, Japanese MNCs restrict the international exchange of information nearly exclusively to Japanese employees. Hence they deny chances for additional and valuable inputs by their non-Japanese colleagues that are still not needed by every Japanese company active in China but by an increasing number of industries and firms.

4.3 Obstacles to overcoming current problems in China

The obvious countermeasure to the described IMC problems in China is a reduction of the strong reliance on expatriates and an increase of alternative control mechanisms, *i.e.* formal bureaucratic control, output control and control by socialization and networks. But such a shift faces several obstacles in Japan and China. Space does not allow for a detailed explanation of why such a shift has to include changes in Japan as well. Such a discussion includes, for example, the current debate on corporate governance in Japan and relates to an eventual shift from the strong personal focus in the Japanese business system towards a more formal and output-based system. Resulting changes in the domestic business system will undoubtedly have important repercussions on international business practices and hence IMC systems. A closer look at these effects, however, requires a study of its own (or eventually more than one). Hence, we will here focus our discussion on the situation China.

Among alternatives to reliance on expatriates in China, a stronger emphasis on formal, bureaucratic control might appeal the most to Japanese MNCs. This is the control mechanism generally suited to complement personal, centralized control (see section 3.1) that is already in place in most Japanese subsidiaries. Complexity and instability in the Chinese business environment, however, restrict the effective use of this mechanism to limited areas. By over-reliance on formal control measures, Japanese MNCs, like other companies risk losing flexibility in their response to the market.

The alternative is an increase in the use of output control combined with more control by socialization and networks. The combination of these two mechanisms is preferred in situations with high environmental instability and thus seems well-suited to the current business environment in China. Within such a combination, controls on output target areas where outputs are measurable. Control by socialization and networks targets behaviors that do not lend themselves to measurement (see section 3.1). Hence, an isolated increase of output control does not make much sense in a complex environment like China because there are currently still too many areas that resist any meaningful measuring of numerical goals. This makes control by socialization and networks an important key to the successful coordination of business activities in China. But exactly herein lies the biggest weakness of Japanese MNCs.

Control by socialization and networks largely takes place through three means: (1) the creation of shared values and goals; (2) informal, horizontal communication between executives; and (3) temporarily formalized cross-section relations like task forces or cross-functional teams. Based on

conventional wisdom we might expect Japanese firms to score high in areas (1) and (2). The low overall significance of control by socialization and networks, presented in Figure 2, however suggests otherwise. This can be explained by the following factors.

A high level of shared values and informal communication can be aimed at by expatriate presence but can be better achieved through international training programs and formal international networks of executives (Harzing 1999, 318). Such programs and networks, however, are very rare in Japanese MNCs. Where they do exist, participation is nearly exclusively Japanese. The same applies to board meetings dealing with global or Asia-Pacific matters and strategies. They usually take place at the Japanese headquarters, not somewhere in the region like China.^{5[5]} The fact that foreigners are generally missing on the board of directors at Japanese headquarters completes the picture.^{6[6]}

As a result, chances for socialization and learning between Japanese and non-Japanese employees at the managerial level are fairly restricted. In any case, they are limited to hierarchical, bilateral exchanges between Japanese and Chinese. They do not allow for a cross-border flow of information between subsidiaries of two different countries that bypass Japanese headquarters. The same holds true for international task forces and cross-functional teams. They rarely take place in Japanese MNCs involving managers from more than one other country.

One major obstacle to overcoming these barriers is of course, the problem of language. English is the international business language and is a prerequisite for all kinds of international networking at the formal and informal level. Since the beginning of international operations, lack of proficiency in English has put Japanese MNCs in a disadvantageous position versus firms from other industrialized countries. It will continue to do so until the average proficiency level of the international managers at Japanese MNCs improves enough to allow for a smooth international exchange of ideas at the working level.

Another more abstract, though ultimately larger obstacle to the introduction of effective socialization and networking at the international level lies in the

^{5[5]} A rare exception is Sony that regularly holds board meetings abroad including China.

^{6[6]} Once again the 'untypical' Japanese company Sony was the first among larger Japanese MNCs to break with this unwritten rule some years ago.

persistence of ethnocentric elements in Japan.^{7[7]} Such ethnocentric elements can be found at the concrete company level but also within Japanese society itself. Examples for the former include the preference of Japanese-only boards as described earlier. Examples for the latter are more difficult to find but eventually more important. One such example comes with the increased employment of Chinese nationals by Japanese companies in Japan.

For more than 20 years, Japanese MNCs have used training in Japan to upgrade the technological and managerial knowledge of their Chinese and other Asian employees. In the early/mid 1990s, larger firms have also started to employ Chinese workers in Japan in larger numbers on a permanent basis, offering them regular careers within the mother company. This has increased knowledge about foreign countries and markets in the head offices of the Japanese MNCs. It has also created a pool of 'loyal' Chinese employees that can be sent to overseas postings to reduce the problem of over-reliance on Japanese expatriates. At first sight, this trend seems to constitute a clear example for a shift from ethnocentrism to polycentrism. The author knows, for example, of three cases where native Chinese worked for several years at the head offices of large Japanese MNCs in Tokyo before being promoted to senior positions. One became the head of the China department at headquarters. The two others were sent to China as general managers of existing joint ventures. In all three cases, however, these Chinese took up Japanese nationality during the course of their career.^{8[8]} Such nationality changes have strong repercussions. Even assuming that success in each of these careers is totally unrelated to the switch in nationality, local managers in China might conclude otherwise. With devastating results on their motivation, they might think that such a switch is a prerequisite for

^{7[7]} For different states of mind or attitude of international executives, see the models of ethnocentrism (home-country-oriented), polycentrism (host-country-oriented), and geocentrism (world-oriented) as described by Perlmutter (1969). The ethnocentric attitude implies that management style, knowledge, evaluation criteria, and managers from the home country are supposed to be superior to those of the host country. The polycentric attitude takes the opposite point of view recognizing differences between countries and believing that local nationals are in the best position to understand and handle country-specific affairs. The geocentric attitude draws from a world-wide pool of international managers to be appointed regardless of their nationality. See also Harzing (1999, 54–55).

^{8[8]} Asked for the reasons, all gave, explicitly or implicitly, pressure by the Japanese society as the reasons to have done so. While they denied that their Chinese nationality had any influence on their professional careers, they judged it more convenient for their children at school to have a Japanese family name.

promotion or contributing for quick success at those and other Japanese companies (also see Nakamura 2000).

As such, an indirect form of ethnocentrism that persists in Japanese society stands in the way of building up truly international operations in Japanese firms. Although this social phenomenon can be partly explained by the relatively late development of Japan with the international environment, it nevertheless influences Japanese MNCs in their current thrive to globalize and implement new IMC systems.

5 5 Conclusions and outlook

The IMC system of Japanese multinational companies, with its reliance on Japanese expatriates, faces several problems in China. Most of these issues are not China-specific by nature. But the special business environment of China is exacerbating problems partly known to Japanese firms from other overseas operations. Yet, urgency about finding solutions rises with the growing importance of China and its market for Japanese firms.

Many Japanese MNCs have already realized the organizational incongruities between their IMC systems and the requirements of the business environment in China and other parts of the world. This is expressed in the numerous plans emerging at headquarters in Japan that call for a reduction in expatriates and numerical targets for localization of management of overseas subsidiaries. A simple reduction of the number of expatriates would be a radical change in the IMC system. However, this is neither advisable nor to be expected anytime soon. At least three reasons militate against such a scenario in China.

First, a fast shift to IMC models like those used by US or German firms is not realistic. Japanese MNCs simply cannot develop alternative, effective control mechanisms overnight. Main obstacles is the different domestic business system and its enduring influence on overseas operations (Ferner and Quintanilla 1998).

Second, despite the various problems described for Japanese MNCs, Western competitors similarly face problems specific to their IMC systems. The low use of expatriates in US overseas operations, for example, has increased the fear of insufficient international managerial experience in US MNCs (Kobrin 1988; Wong and Law 1999). Another IMC problem, not uncommon with Western firms in China, is the employment of overseas

Chinese in top management positions. These managers speak Chinese and offer familiarity with the local culture. Yet they are often rejected by local managers who prefer working under Western expatriates as stressed by many of the author's interview partners (also see Leung et al. 1997).

Third, the need for an efficient IMC model differs depending on the type of company. Among Japanese MNCs there are great differences that depend on the type of activity in China. The three plants of Teijin in Nantong, for example, work de facto as subcontractors for the Teijin headquarters in Japan. These plants receive inputs materials, engage in the weaving and dyeing process and then return 95% of their output to Japan. For this they receive a commission. In other words, because they are (still) not targeting the local market, they have very little need for local feedback. Many Japanese plants in China engaged in this kind of export-processing trade in which efficient production is more important than market response or organizational learning. For these companies, the expatriate-based IMC model has worked fairly well and does not require immediate alteration.

Other Japanese firms, however, have totally different needs, especially with regard to a flexible market response. More than one third of all Japanese manufacturers in China sell more than 50% of their output to the Chinese market (JETRO 2000, 72). Other companies in fast-moving sectors like information technology and telecommunication equipment are very dependent on quick and comprehensive organizational learning. They embody another example of internationally active MNCs that require fast, cross-border flows of formal and informal information. This is difficult to achieve in an IMC model that is exclusively expatriate-based.

Hence, Japanese MNCs will attempt to implement new IMC models in response to their specific needs and the specific requirements of the business environment in China. The transfer towards learning organizations and transnational companies in the real sense will, however, in any case be a difficult one, be it in China or elsewhere. The various obstacles along the way will make the shift from ethnocentric to geocentric firms (or more realistically regiocentric firms) a very 'tortuous evolution' (Perlmutter 1969). Whether Japanese firms will succeed in this shift in China, will be of utmost importance for most of them.

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