The MNC versus the GTC: Comparison of Their Environments and Strategies

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I. Introduction

Japan established national trading companies during the 1880s as a means of achieving economic independence and in the 1900s used these companies to internationalize its domestic industries. Japaness trading companies served to consolidate and export the products of domestic manufacturers, which otherwise lacked the capabilities independently to penetrate overseas markets. In contrast, manufacturing companies in the US and Europe sought internationalization of

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their operations individually, and only after having established themselves in their domestic markets. Instead of relying on trading companies, the preferred method was direct investment, leading to the emergence of multinational corporations.

Students of western business management have attempted to apply their theories on internationalization[1] to large trading companies in Japan which are commonly called as sogo-shosha. The result has been two opposing schools of thoughts. The first considers the sogo-shosha an "incomplete" or "transformed" MNC and asserts that "sogo-shosha is a New Japan-style MNC."[2] The second view suggests that "sogo-shosha will not become an MNC."[3] The latter differs from the former in that it recognizes fundamental differences in character of the two international business forms. Both viewpoints, nonetheless, evaluate sogo-shosha against previous analyses on MNCs and tacitly assume that an MNC is the only means of promoting internationalization of domestic industries. No consideration has been given to sogo-shosha, the term which has been frequently used as a generic term for a more general term "general trading company(GTC)", as an alternative method for internationalizing domestic industries.

However, GTCs are no longer unique to Japan. Other countries have selected the GTC or a similar organization for their processes of internationalization. GTCs have been established in Korea and Turkey, Large Trading Companies in Taiwan, International Trading Companies in Thailand, and since October 1982, the US has permitted the formation of Export Trading Companies. Given

(1) Most theories on the internationalization process of MNCs are based on various analyses of international movement of capital, international business management practices, the economic environment in host countries, and the industrial structure in the investing countries. The most widely accepted theories on internationalization emphasize industrial structure as the major determinant of foreign direct investment. These include: monpolistic advantage theory, product life cycle theory, oligopolistic theory, and internal market theory.

(2) Isoda Keiichiro, *Japan-USA Trade and Direct Investment in USA*, Yamaguchi University, Economic Research Institute, 1981, p. 76.

(3) Michael Y. Yoshino, *Japan's Multinational Enterprises*, Harvard University Press, Cambridge, Massachusetts, 1976, p. 95.

this increasing acceptance of the GTC as a viable form of international business organization, a general theory of the GTC that is independent of the traditional theories on internationalization based on experiences of the MNCs should be considered.

The modern from of the MNC derives from the US, the GTC from Japan. Before building a theory of the GTC, therefore, this paper attempts to compare the political, economic, cultural, and social environments in the US and Japan, which will help explain the development of the MNC form in the US and the GTC form in Japan. In addition, analysis of the differences in the strategies of the two international business forms will be made.

Each of the comparisons of the business environments in the US and Japan will start with the late 19th century, the initial stage of internationalization in both economies. In the US, internationalization began in the 1880s, with the industrial revolution well in progress. Similarly, in Japan, internationalization got under way after the Meiji Restoration in 1868, with the emergence of national trading companies. Business strategy comparison will focus on the present situation.

II. Comparison of Business Environments in the US and Japan

1. Political Environment

In every society there is a close relationship between the business sector and the government. The range of business activity is often limited by a government's posture toward the private sector. There are three basic models which represent this relationship between the government and the business: the laissez-faire model, whereby the government adheres to a policy of nonintervention, prescribing only minimal regulations; the mercantilistic model, whereby the government actively supports the business sector as a means of increasing national wealth; and the constitutional model, whereby the government, in its capacity as the regulator, seeks to limit socially undesirable conducts of business firms.[4]

Mercantilism first emerged in 16~18th century Europe. After the Meiji Restoration in 1868, Japan also pursued mercantilistic policies, culminating in a close government-business cooperation often pejoratively called "Japan, . Inc." by journalists today. In contrast, the contemporary US economy has exhibited characteristics typical of the constitutional model. Faced with increasing monopoly power of large business entreprises in the early 20th century, the US government instituted antitrust legislations and has since actively maintained its role as a regulator of business activities. Therefore, this section will compare constitutionalism in the US with mercantilism in Japan.

(1) Constitutionalism in the US

After the Civil War in 1865, increased commerce between the agricultural South and the industrial North led to accelerated economic activities and an industrial revolution. At the same time, elements of Adam Smith's "perfect competition" gave way to an increasingly monopolistic economy, as larger companies used their comparative advantage in size to control and absorb smaller competitors.

Rockefeller's Standard Oil Trust was foremost among the period's giant enterprises. Rockefeller early recognized the importance of railroads in the petroleum industry and obtained the trusteeship of railroad transportation. As a result, by charging exhorbitant rates, Standard Oil was able to use its virtual monopoly in land transportation to force potential competitors into mergers or liquidation. Based on its trusteeship of railroad transportation, Standard Oil was able to develop into a fully integrated petroleum company, effectively controlling all stages of the oil process from production and refining to sales.[5]

(4) For a more detailed discussion, see Dong Sung Cho, *Kyungyoung-Jeongchaek-kwa Changki-Jeonryak-Kyehoek* (*Business Policy and Strategic Planning*), 2nd ed., Youngji-Moonwhasa Publishing Co., 1983, pp. 45-73.

(5) During the early 1900s, the only petroleum companies operating independently from Standard Oil Trust were in Texas. At the time, Standard Oil operations were very much limited to the Northern Atlantic states and the Midwest and showed little concern or interest in the Southwest. These independent companies included Gulf, which first started exploring oilfields in Texas, and the Texas Company, now Texaco, which began by transporting Gulf's products.

As Standard Oil's growth continued unabated, concern over its increasingly tyrannical economic power forced the federal government into corrective measures: in 1911 the antitrust law enforced the breakup of Standard Oil into thirty-eight separate, state-wide companies. In addition, the Interstate Commerce Commission, which had been established in the 1880s, began to exert its regulatory power, and further limited these new companies' activities outside their home states.(6)

Faced with increasing government regulations, US entrepreneurs sought alternative methods of pursuing their desire for rapid growth. They found new opportunities abroad, away from direct influence of the US government, and were able to establish themselves in overseas markets through foreign direct investment. The US achieved prominence in the international arena during World War I, and after World War II, sought to exercise its influence as the undisputed global power. Therefore, the US government indirectly, yet vigorously, supported overseas activities of US entrepreneurs,(7) while continuing to regulate their activities at home. The overall effect was to encourage foreign direct investment.

(2) Mercantilism in Japan

Mercantilism in Japan is characterized by public-private cooperation, whereby the economy is managed through collaboration between the government and the business sector. As shown in Exhibit 1, economic policies are formulated and implemented through mutual agreement and cooperation between the

(6) Most of these 38 companies have since developed into some of the largest petroleum companies in the world. Exxon, the largest petroleum company in the US, was formerly Standard Oil of New Jersey. Similarly, Mobil, the second largest, began as Standard Oil of New York. Standard Oil of California is the fourth largest oil producer in the US, while Standard Oil of Indiana is the fifth.

(7) The foreign tax credit provision under the US tax law is an example of indirect government support. In the early 1950s, oil prodcing states in the Middle East started levying a 50% tax on oil revenues of foreign petroleum companies. To ensure continued profitability of US oil companies in the Middle East, the US government allowed US companies to apply their foreign tax payments against domestic tax obligations, thereby avoiding double taxation. The policy also allowed the US to maintain its influence in the Middle East by making the local governments dependent on oil revenues from US petroleum companies.

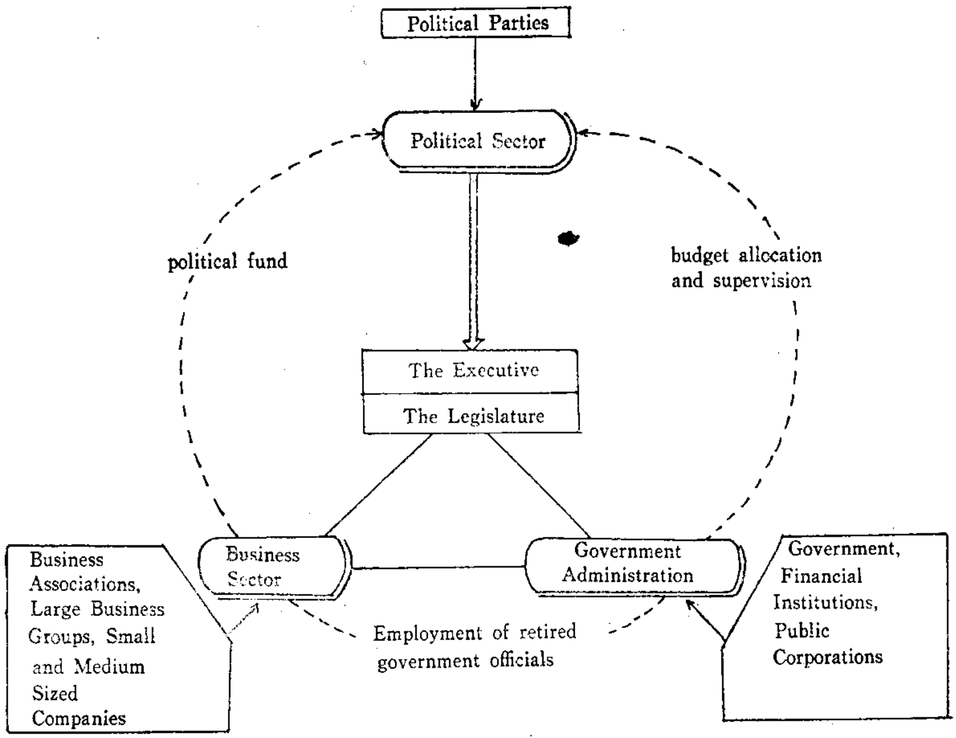


Exhibit 1: Public-Private Cooperation in Japan

political sector, including the executive and the legislative bodies, the business sector and the government administration.(8) The result has been a coexistence of strong government directives(9) with support and incentive programs, which has allowed Japanese entrepreneurs to aggressively pursue business opportunities.(10) In return, entrepreneurs were often expected to take a national perspective, even participating in the development of national economic policies both in official and unofficial capacities. Such public-private cooperation was not new to Japan. In the Edo Period, for example, there had been cooperation between the Shogunate and the merchants.(11)

(8) Shincho Tsuda, *Nihonteki Keiei No Ronri* (*The Logic of Japanese Management*), Chuokeizaisha, Tokyo, p. 281.

(9) There are two major laws which regulate business activities of private firms; *Juyo Sangyo Toseiho* which promotes cartelization and self-control of private industrial sectors; *Kokka Sowdoinho* which facilitates government's direct control over private activities.

(10) Shincho Tsuda, op. cit., p. 281.

(11) Ibid., p. 286.

A similar collaboration between government and business occurred in the internationalization of the Japanese economy. Within a few years after Japan opened her doors upon the arrival of Commodore Perry in 1854, foreign trading companies began to dominate the Japanese import market. Alarmed with this dependency of Japanese economy on foreign traders, the new Meiji government since 1868 sought to promote its economic independence. However, domestic industries proved to be incapable of competing with foreign imports, and the government was forced to seek indirect protection of domestic markets by supporting the growth of domestic traders. The result was the establishment of national trading companies, such as Mitsui and Mitshibishi, which became the foundation of present-day sogo-shosha. These companies initially concentrated on import substitution,(12) but subsequently engaged in exports in order to secure capital resources necessary for continued industrialization.(13) This was the first step in Japan's internationalization process.

2. Economic Environment

(1) Industrialism in the US

The Civil War accelerated industrial development in the North. A small group of entrepreneurs, early founders of modern industry often called the "Industrial Valiants," continued to lead US industrialization, rapidly accumulating wealth and strengthening their market position in the process. Ever seeking new business opportunities, they continued to move westward and soon dominated the entire domestic market. At the same time, they began to realize that any further attempt to increase market share would simply result in undesirable price competition and surplus industry capacity. Therefore, when overseas opportunities appeared in the early 20th century, it was inevitable that US entrepreneurs would apply their tireless frontiermen energy to the expansion of foreign markets through direct investment in manufacturing.

(12) Import substitution refers to an economic policy which encourages domestic production in order to reduce imports and establish an independent domestic economic base.

(13) Keiichiro Nakagawa, *Hikaku Keieishi Josetsu (Introduction to comparative Business History)*, Tokyo Daigaku Shuppankai, Tokyo, 1981, pp. 313-315.

(2) Commercialism in Japan

Concerned with increasing influence of Western colonial powers, the Meiji government attempted to enforce political unity and economic independence. However, backward Japanese manufacturers proved to be incapable of meeting the task, and the government was forced to rely on the traditional merchant class from the Edo Period to promote economic indendence. Under govenment tutelage, Japanese merchants used their extensive domestic commercial network to concentrate scattered national capital resources into few large groups, creating new industrial powerhouses known as "zaibatsu."

The zaibatsu responded to the government's expectations handsomely, rapidly recapturing the leadership in the Japanese import market from foreign traders. However, during the subsequent industrialization process, zaibatsu realized that they could not continue to compete successfully with Western powers, given their rudimentary technology. To overcome this deficiency, zaibatsu began to import advanced technology, relying on increased exports to the colonies to provide necessary capital for its payments. For Japanese companies, which began exports as a means of augmenting domestic capital resources, poor capitalization remained a major concern. Therefore, instead of adopting profit maximization as the prmary strategic goal as in the US, Japanese companies sought to maximize growth in an effort to increass their working capital.

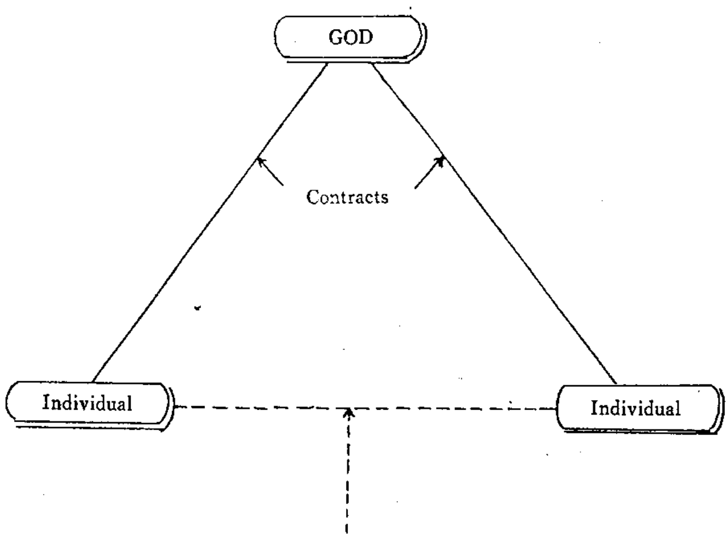
Capitalism in Japen, therefore, was the product of a collusion between the government and the merchant class which allowed the emergence of zaibatsu. With government protection and support, they spearheaded Japan's colonization process prior to World War II. Capitalism in Japan was based on commerce rather than industrial production as in the US. Hence, in the internationalization process, foreign trade became a natural extension of Japan's domestic capabilities. In contrast, US manufacturing firms could more easily export their production capabilities through foreign direct investments.

3. Cultural Environment

This comparison of cultural environments in the US and Japan examines the effects of religion and ethnic composition on personal and social value systems. "Universalism" generally characterizes the social value system in the US. In contrast, "particularism" must be considered to be the underlying cultural current in Japan.(14)

(1) Universalism in the US

A major, perhaps the major, influence on social behavior in the US has been Christianity. In this monotheistic religion, God is the only acknowledged possessor of absolute authority, and its followers believe that their ultimate obligation is to God. Furthermore, their personal values are derived from the teachings of the religion; as shown in Exhibit 2, Christianity has provided guidelines which strongly influenced interpersonal relations. Universally applied social values in the US, such as freedom, equality, independence and humanitarianism, ultimately can be all traced back to Christian belief system.



Social contracts within the
limits of contractual obligations to God

Exhibit 2: Social System in the US

(14) "Universalism" and "particularism" are borrowed from Talcott Parsons, *The Social System*, Routledge and Kegan Paul, London, 1951, pp. 58-200.

Another cultural determinant in the US has been its diverse ethnic composition and the relationship between ethnic groups. From the colonial days until the end of the Civil War, the US cultural environment centered on the social values of WASPs, White, Anglo-Saxon Protestants. However, beginning in the late 19th century, large waves of immigrants started arriving in the US, each group of immigrants bringing with it a distinctive culture and social value system. Due to this ability to accept and assimilate large number of ethnic groups, the US society has often been referred to as the "Melting Pot."(15)

Familiarity with numerous ethnic cultures at home allowed US entrepreneurs to operate abroad without experiencing much of a culture shock in many foreign markets. Further, cultural diversity at home allowed US entrepreneurs to take a geocentric view of their operations,(16) to consider the whole world a potential market and aggressively pursue foreign direct investments as a strategy for growth.

Due to the diversity of ethnic groups, social order in the US had to rely on general rules which could be understood by, and satisfy the needs of, all members of the society. However, consensus suffers from an inherent resistance to change, since the society can react only after its members agree on a new course of action or a new system. A similar weakness is revealed in US business firms. A major concern in almost every strategic planning in a US company, is the impact a new course will have on the various units in the firm, and precaution is taken not to unduly compromise the special interests of the various units. Therefore, the system itself is more conducive to one-time commitment and gradual changes, such as foreign direct investments, and less adaptable to rapid and constant changes in demand and outlook, whick is an avoidable part of international trade.

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(15) The term came into vogue after Israel Zangwill's play, "The Melting Pot," opened on Broadway in 1908.

(16) Heenan and Perlmutter identified four basic geographic orientation of business operations: the ethnocentric view, the polycentric view, the regiocentric view, and the geocentric view. For further details, see David A. Heenan & Howard V. Perlmutter, ***Multinational Organization Development***, Addison-Wesley Publishing Co., Reading, Massachusetts, 1979, pp. 17-21.

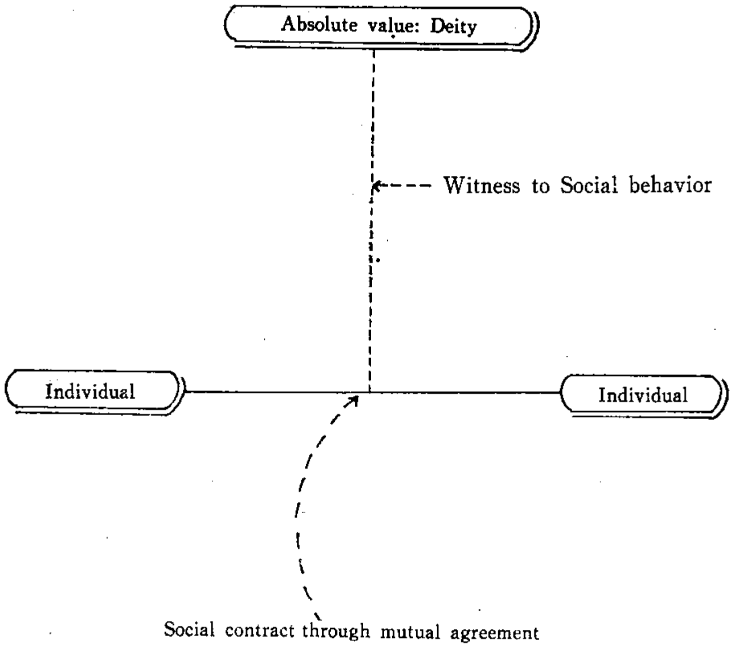


Exhibit 3: Social System in Japan

(2) Particularism in Japan

In contrast to the US, there is a total separation of social and religious values in Japan. As a result, there is no universal principle of social behavior based on religion. Instead, as shown in Exhibit 3, social order is established solely through mutual agreement between individuals within the society. The result is a relatively flexible social system which allows the society to progress by assimilating foreign cultures and values. Not bound by an absolute value system, Japan could easily import a foreign culture, modify it to her own environment, and eventually make it a part of her own.

The Japanese value system is composed of a unique set of values borrowed from both foreign and indigenous cultures. Japan borrowed Confucian ideals from China, creating a rigid, vertically-oriented society constructed around the samurai during the Edo period. Scientific ideals from the West provided elements of individualism and industrialism which permitted the emergence of a progressive managerial class. In addition, Japan adhered to a local brand of realism, which stressed nationalism as the means of survival. The resulting social and personal values have become the driving forces behind Japan's industrialization process since the Meiji Restoration.

Japanese business firms similarly show a willingness to accommodate and learn from others. As a result, they can rapidly adjust to changes in the business environment. At the same time, like the Japanese society itself, Japanese firms have been far less willing to reveal their internal operations. By pursuing foreign trade, rather than foreign direct investment, Japanese firms could operate abroad without being totally exposed to the scrutiny of others.

4. Social Environment

We can compare the social environments in the US and Japan by examining individual behavioral patterns in each country.

(1) Individualism in the US

The US is a society which values and rewards individualism and independent spirit. It is a society based on the premise that rivalry inevitably exists among its members, and that a community is formed by reconciling such rivalries through competition and negotiation. As a member of a community, an individual is subject to certain contractual rights and obligations. Further, the individual has a specific position in the community to perform an assigned function and role[(17)] depending on his ability and his contribution to the community process. Those who contribute more to the community are rewarded more. Since individuals' abilities differ, it is inevitable that individuals are rewarded at different levels.

The US society is characterized by competitive relationships between individuals, which often takes the form of sectional antagonism.[(18)] Such antagonism was manifest in the Civil War between the Confederate and Union supporters and is still apparent in disputes over conflict of interests between the state and federal governments.

In any organization which presumes competition among its members, it is

(17) Ryushi Iwata, *Nihonteki Keiei No Hensei Genri* (*Structural Principles of Japanese Management*), Bunshindo, Tokyo, 1978, pp. 42-43.

(18) Hans Kohn, *American Nationalism*, the MacMillan Co., New York, 1957, p. 93.

necessary to clearly define the competitive goal. This is no less true of US business firms: US business firms clearly define the reponsibility and the authority of their employees, and the organizational structure is formalized. Further, rewards for successful competition must be tangible in the form of increases in pay or promotion. Such rewards can be assessed only on short-term achievements based on superficial and visible criteria. The evaluation system does not allow the managers to take a long-term view on market shares or product develpment. Instead, US executives are subjected to quarterly or yearly evaluations based on their ability to maintain high levels of return on equity or stock price. Similarly, the need to show short-term achievements makes mergers and acquisitions more attractive as a strategy for growth, compared to long-term growth based on internally generated funds.

(2) Collectivism in Japan

The basic unit in Japanese society is the clan rather than the individual. This is not to suggest that the Japanese society discourages independent thinking or individual efforts. Instead, the society demands that individual efforts be accomplished through the clan.[19] Similarly, "harmony" is more valued than independent spirit. Such harmony is not attained through simple coorperation or coordination. It comes from the ability of an individual to translate his goals into the clan's and achieve that goal through the collaboration between all members of the clan.

Collectivism in Japan can be better understood by examining three essential qualities of interpersonal relations in the Japanese society. First, a clan originally belonged to a village. In Japan, the most traditional and established communities were rural villages. Security was provided through a continued and harmonius relationship between the village and the clan. As the relationship continued, the clan came to represent and defend the village as its own. In modern Japanese industry, such predilection for security based on long-term relationships

(19) Kunio Ohshima, ***Kokusai Hikaku Keieiron*** (***International Comparative Management***), Moriyama Shoten, Tokyo, 1978, pp. 200-201.

can be found in the policy of life-time employment and seniority system. Further, Japanese executives feel personally compelled to maintain the reputation and prestige of their business firms by sustaining corporate growth. Therefore, the primary strategic concern lies in long-term goals of increasing market share and product develpment.[20]

Second, there is a clear distinction between insiders and outsiders. Therefore, a firm with a great deal of internal unity tends to be isolationist and xenophobic. Indeed, the insiders deliberately stress their own internal virtues, thus accentuating the discrimination against the outsiders. As a result, a new employee, regardless of his particular function, is put at the bottom of the organizational ladder.[21]

Third, the social attitude in Japan facilitates vertical personal relations more than horizontal relations. In Japan, antagonism does not arise out of disagreement between the management and its employees. Instead, the contest is primarily between one company and another.

Japanese business firms have retained the traditional social structure: the rural village was a community created out of convenience through long-term relationships among its members.[22] Japanese firms themselves became small universes made up of groups of employees which work as a team. In such a collectivist society, personal goals are subordinated to the more clearly defined community goals. Corporates goals are pursued throgh collaboration and support between groups of employees, rather than by a rigid assignment of responsibilities to individual employees, and the employees are evaluated as a team rather than individuals.

Japanese society stresses internal harmony over external competition. As a result, there is a strong tendency to make an organization into a self-sufficient,

(20) Tadao Kagono, "Nihon No Keiei—Beikoku No Keiei (Japanese Managment—American Management)," *Keizai Seminar*, January, 1981.

(21) Chie Nakaso, *Tate Shakai No Ningen Kankei* (*Japan's Social Structure*), (translated by Seong-Kil Choe), Hyungsul-Choolpansa, Seoul, 1982, pp. 50-56.

(22) Junki Itoh, *Nihonkeki Keiei No Genjou To Tenbo* (*Current State and Future Prospect of Japanese Management*), Hakuto Shobo, Tokyo, 1979, p. 8.

complete unit, thereby avoiding direct contact and competition with the outsiders. Zaibatsu, with their wide range of products, are an attempt to achieve such self-sufficiency. Similarly, in the internationalization process, Japanese firms shied away from revealing their own technology level, trademark, quality, and financing ability through foreign direct investment, and instead opted for trade of manufactured goods.

5. Business Environments Summarized

Exibit 4 summarizes our observations on the political, economic, cultural and social environments in ths US and Japan.

	the US	Japan
Political:		
Domestic	constitutionalism	mercantilism
International	globalism	nationalism
Economic	industrialism	commercialism
Cultural	universalism	particularism
Social	individualism	collectivism
Internationalization Strategy	Foreign Direct Investments	Import and Export of Manufactured Goods
International Business Form	Multinational Corporations	General Trading Companies

Exhibit 4: Business Environments in the US and Japan Compared

III. Business Strategies of The MNC And The GTC

The previous section compared the different environmental pressures in the

US and Japan which led to the two different forms of internationalization, foreign direct investment in the US and foreign trade in Japan. This section examines the differences in specific business strategies which allowed the development of the modern forms of MNCs in the US and GTCs in Japan.

1. Internationalization Strategy

(1) US-Based MNCs: Foreign Direct Investment

To US entrepreneurs, the large domestic market initially seemed to offer an almost limitless opportunity for expansion. As a result, US entrepreneurs showed very little interest in overseas markets until late in the 19th century, when they found in foreign markets an opportunity to sustain high levels of growth.

Traditionally, and especially since the 1950s, the primary strategic concern of US entrepreneurs was to increase their domestic market shares. Therefore, to increase price competitiveness of their products, US entrepreneurs sought to reduce production costs. Their initial solution was found in post-war Europe and Japan, where labor costs were substantially lower. When European and Japanese wages showed sharp increases during the 1960s, they turned to the less developed countries.[23] To take advantage of production efficiency offered by lower labor costs, US entrepreneurs transferred factors of production abroad, including capital, machinery, and technological know-how, and imported finished goods in return. The result was to increase the level of foreign direct investment.

(2) Japanese Sogo-Shosha: Foreign Trade

In Japan, the small domestic economy rapidly limited opportunities for growth. Japanese trading companies, therefore, started exploring overseas markets as soon as they were able to reestablish dominance in the domestic market. During the early 20th century, their efforts were facilitated by Japanese imperialism, which allowed companies to rapidly increase exports of finished goods to colonies.

(23) Such a relocation of production sites can be explained by the product life cycle theory, originally stated by Raymond Vernon.

Even after World War II, export activities continued to receive active government support. However, the government's goal was more than simply expanding export volumes. Recognizing the need to maintain low production costs to assure future competitiveness in foreign markets, Japan sought to reduce the cost of raw material imports. The government's solution was to delegate raw material import rights to a limited number of large trading companies, rather than to allow each firm to import its individual needs. Such purchasing rights were given to sogo-shosha. The buying power of the resulting monopsony served to effectively lower import costs, and sogo-shosha came to play an increasingly prominent role in the Japanese economic process, both as major exporters of finished goods and importers of raw materials.

2. External Growth Strategy

(1) US-Based MNCs: Mergers and Acquisitions

The growth of US-based MNCs can be attributed to both the accumulation of capital provided by secular sales increases and the concentration of capital through mergers and acquisitions. It was generally the latter which allowed the rapid development of US companies into large-scale MNCs. A recent study, for example, showed that two-thirds of the 100 largest US companies in 1969 were products of mergers and acquisitions.(24)

The series of mergers and acquisitions in the US can be divided into three periods. The first stage, begun in the late 19th century, saw horizontally-oriented mergers of companies in the same industry. By the 1890s, increased industrial productivity had led to excess supply of manufactured goods. Faced with surplus capacity and increasingly fierce price competition, US entrepreneurs collaborated to ensure profitability, effectively forming cartels by fixing prices and dividing up the domestic market. Such collusions were soon broken from within, as larger companies found the means to dominate other companies in their industries. Standard Oil, for example, was able to gain effective control

(24) *America Keieishi, Joge* (*American Business History, I and II*), (translated by Kinichiro Toba, et. al.), Toyo Keizai Shinposha, Tokyo, 1977, p. 369.

over smaller petroleum companies after forming the Trust. Subsequently, in 1899, when the revised commercial code in New Jersey allowed the establishment of holding companies, Standard Oil Trust reorganized into Standard Oil of New Jersey, effecting the legal merger of all related companies under the Trust into one giant corporation. Similarly, such mergers allowed US Steel and General Electric to emerge as dominant companies in their respective industries. Three major factors facilitated mergers in this period: the recessionary business environment which made smaller companies particularly vulnerable; completion of a railroad network across the entire US, which made geographic expansion more manageable; and an active financial market, which encouraged capital investments.

The second stage was characterized by vertically-oriented acquisitions of companies in related industries. At the end of World War I, US entrepreneurs again found themselves with surplus capacities in their traditional industries. They sought diversification as a long term strategy for growth, and began to pursue both forward and backward integration. At the same time, they adopted a decentralized management structure, organized by industry segments, and began to expand overseas operations as a part of a diversification strategy.

After World War II, conglomerates appeared. US enterprises had accumulated a high level of surplus capital during the war economy. However, the government's stringent enforcement of antitrust laws made any effort to increase market share illegal. Acquiring small-and medium-sized companies in unrelated industries, therefore, uniquely offered the opportunity to both invest surplus capital and maintain high levels of growth. This acquisition strategy was aided by an active and bullish stock market, which made such investments in securities of other companies relatively attractive.[25]

Conglomerates were not driven by the traditional goals of increasing economies of scale or market dominance. Conglomerates became decentralized, market-

(25) Shijo Muramatsu, *Kigyo Gobenron* (*Corporate Merger*), Dobunkan Shuppan Kabushiki Gaisha, Tokyo, 1973, pp. 39-48.

diversified firms, using their comparative advantage in management ability, information capability and relatively easy access to financial markets to compete in diversified market areas with a wide range of products. Less concerned with economies of scale than traditional US manufacturers, conglomerates were willing to penetrate smaller foreign markets. After establishing themselves abroad, conglomerates sought to increase their penetration of local markets by acquiring existing local companies, making foreign direct investment an integral part of their overall acquisition strategy. ITT and Litton Industries were foremost among conglomerates pursuing such a global acquisition program.

(2) Japanese Sogo-Shosha: Formation of Business Groups

Until the beginning of World War II, the Japanese economy was dominated by few large enterprises, the zaibatsu, such as Mitshibishi, Mitsui and Sumitomo. At the end of the War, the US military occupation government dissolved the Mitsui and Mitshibishi holding companies, forcing the breakup of zaibatsu and disrupting business leadership in Japan.

Soon after the end of the US military occupation government, however, there was a rekindling of cooperation between former members of zaibatsu. They were driven together by traditional ties and loyalties, shared values, and the realization that collaboration would lead to increased business opportunities and profits.(26) In order to compete with this increasing power of former zaibatsu group companies, other Japanese firms started pooling their capital resources around major banks, including Dai-Ichi and Sanwa, creating new business groups.

Japanese business groups have followed five basic strategies to strengthen their organizations: (1) each group has a major bank whose role is to channel outside capital to the group; (2) each group has a sogo-shosha which acts as both the sales and purchasing agent for the whole group; (3) each uses outside banks and trading companies to spread political and economic risks and to take

(26) Alexander K. Young, *Sogo Shosha: Japan's Multinational Trading Company*, Westview Press, Inc., Boulder, 1979, Chapter 4.

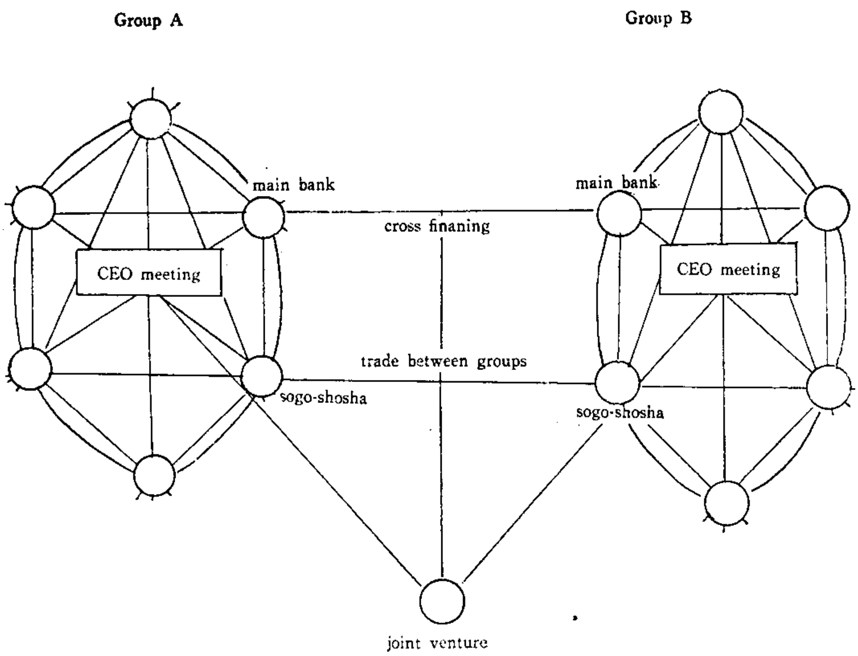


Exhibit 5: Japanese Business Group Structure

advantage of large-scale transactions, including syndicated loans; (4) each creates of new business units within the group through joint investment by other members of the group to strengthen ties through interlocking ownership; and (5) since the early 1970s, each has established joint ventures with other business groups.[27]

The relationship of business units within a Japanese business group and the relationship between Japanese business groups are shown in Exhibit 5. Banks and sogo-shosha are the core units in every Japanese business group. Sogo-shosha, in particular, provide an extensive information gathering capability and an extensive domestic sales network. In return, sogo-shosha profit by exclusively handling the sales and purchases of the other companies in the group. Further, sogo-shosha profit by serving as finder of new business opportunities, undertaking initial investment for the group in new industries.

There are two major sources of income for a sogo-shosha: monopoly profit

(27) Shincho Tsuda, op. cit., pp. 278-279.

from its role as the sales agent, and risk premium for participating in relatively new markets.[28] These profits come from sogo-shosha's ability to perform as the organizer of business activities. Sogo-shosha possess only functional capability and are without capital, technology, or raw material resources, the foundation of most business firms. Therefore, to serve its function, sogo-shosha need the support of and access to financial institutions and manufacturing firms. Similarly, in the internationalization process, sogo-shosha often serve as the pathfinder, leaving foreign direct investment to other companies in the enterprise group.

3. Organization Strategy

(1) US-Based MNCs: Decentralization

As we have already noted, by the 1920s, US enterprises achieved considerable product range and geographic expansion through a series of mergers and acquisitions. At the same time, a centralized, functionally organized management structure was replaced by a decentralized management structure. The old structure had each unit operating under a specific functional charter, such as sales or production. In contrast, the new structure emphasized industry segments, each segment with both production and sales responsibility for a given range of products.[29]

This transition to a decentralized management structure can simply be considered a creative response to changes in the business environment.[30] It was, however, more: roots of a decentralized management can be found in the US social value system. Reassigning decision-making power to a lower level was more suitable in a cultural environment where individual ability and innovativeness are highly valued.

(2) Japanese Sogo-Shosha: Functional Specialization

From the outside, sogo-shosha appear to be organized into units with specific

(28) Gen Kubo, *Sogo Shosha To Sekai Zaibatsugun* (*General Trading Companies and World's Business Groups*), Nunoi Shuppan Kabushiki Gaisha, Tokyo, 1975, p. 35.

(29) Alfred D. Chandler, Jr., *Strategy and Structure*, The M.I.T. Press, Cambridge, Mass., 1962, p. 78.

(30) Shinichi Yonekawa, *Europe, America, Nihon No Keieihudo* (Business Climates of Europe, America, and Japan), Yuhikaku, Tokyo, 1978, p. 130.

product or geographic responsibilities. However, a look at their internal operations reveals that sogo-shosha actually emphasize functional specialization, the nature and range of which are particularly sensitive to changes in consumer demand, since sogo-shosha act as the antenna of Japanese manufacturing firms in foreign markets. Therefore, functional activities of sogo-shosha continuously undergo modifications, and it is difficult to generalize about their organizational structure.

Functional activities of sogo-shosha can be divided into general and product functions. General functions can be further divided into main and support functions. Main functions include trade, finance, and information gathering. Support functions include raw material development, industrial mangement, and software systems, such as project and material management. It is important to note that none of these functions are considered an end in itself. For example, information capabilities are maintained to support trading activities. Similarly, financing capabilities are maintained to provide competitive advantages for the products of manufacturing firms in their groups.

While sogo-shosha's individual functional capability show increasing sophistication, they all serve to support the company's growth through increased trade activities. Therefore, Japanese sogoshosha empasize globlal maximization of profits; less importance is given to internal allocation of profits or the performance of individual units. In contrast, US-based MNCs emphasize local maximization of income, with each business unit operating as a separate profit center.

4. Personnel Strategy

(1) US-Based MNCs: Short-Term Employment and Merit System

By the late 19th century, the US was able to join the ranks of industrial nations. Continued economic growth demanded an increased labor force, and the US was able to supplement the shortage in local labor supply through increased number of immigrants. Such a policy of "contractual slavery" served the country well as long as the economic growth continued unabated. However, it gave rise to a major social problem during the econonomic depression. Large number of companies started to lay off their immigrant workers and some simply refused to pay their wages. The resulting poverty became a catalyst for the organization of labour unions.

The resistance of US entrepreneurs to unions was not simply for economic reasons: US entrepreneurs saw unions as both an unwanted attempt to share the profits of their business ventures and a challenge to their right to freely pursue business opportunities.[31] The labor movement was considered a renunciation of the right to private property, which was the very foundation of capitalism. Given the prospects of foregoing the right to dismissal, US companies turned toward short-term employment as a more attractive alternative.

Although the US did not have a traditional class structure, Americans are no less class conscious than members of other older societies. In the US, membership in a specific social circle is more valued than company loyalty. Since there is no aristocracy, or other similar traditional hierarchy, social distinction is based primarily on income level. Therefore, increased monetary compensation is the preferred method of reward and cannot be substituted with a simple titular promotion. Higher income not only allows membership to exclusive social circles but permits greater independence and comfort. Therefore, in a society where labor mobility is particularly high, it is inevitable that attractive salary offers are the primary form of inducement for qualified employees.

(2) Sogo-shosha: Life-Time Employment and Seniority System

In the early 20th century, rapid growth of light industries in Japan sharply increased the demand for labor, resulting in both an intense competition between firms for the limited supply and a mass movement of labor force from rural to urban areas. However, the chronic economic malaise at the end of World War I, and eventually the Great Depression, suddenly erased the bargaining power of labor over Japanese business firms.[32]

(31) *America Keieishi*, *Joge*, op. cit., p. 130.
(32) Mitsuo Fujii, et. al., *Keieishi-Nippon* (*Business History-Japan*), Nihon Hyoronsha, Tokyo, 1972, pp. 113-114.

Most small- and medium-sized firms reacted to the depression by reducing the number of their employees. In contrast, large companies negotiated to share the effects of the depression, by retaining their employees in return for reduction in wages. For the companies which survived the depression, this retention program became a permanent part of their policy and the foundation for Japanese labor management. Currently, about one-third of the total labor force works under the benefit of such a life-time employment system, which exists in most large companies including sogo-shosha.

There are two notable elements in this life-time employment system. First, an employee is given an "undefined" reponsibility. For example, an employee is not evaluated as an individual, but as a member of the work team to which he belongs. His responsibilies are whatever is necessary for the team to achieve its given task. Second, an employee's general and social skills are more valued than his specific technical ability. To guard against inertia which could result from a life-time attachment to one specific function, Japanese companies tend to move their employees around the organization, giving them new responsibilities in new areas. The system requires adaptible employees.

The seniority system in Japanese firms is adopted from the Japanese family system, and takes the form of group employment, reassignment, and promotion at predictable and regular intervals.[33] Since hiring is done at regular intervals, there is a particularly close relationship between an employes's age and the length of employment in the company. Promotions are based primarily on these two factors. However, realizing that an overly rigid system could easily lead to a total suppression of individual abilities, Japanese firms have subsequently been more rapidly rewarding the more capable employees through bonuses and assignments closer to the decision-making process.

5. Coordination Strategy

(1) US-Based MNCs: Mechanistic and Contractual

In most US-based MNCs, the function of each management position and the

(33) Ryushi Iwata, op. cit., p. 215.

line of authority in the organization are clearly defined. In an individualistic society, such a clear delineation of responsibility is a prerequisite for the successful participation of each employee in the corporate process. For US business firms, an individual with a predetermined function is the basic unit of operation, and the systematic organization of such units drives the corporation toward its goals.(34)

However, this traditional organization system puts an excessive premium on tangible short-term gains. As a result, internal coordination of activities suffers from mechanistic relations between the members of the organization. The focus on short-term results are an inseparable part of the US business environment, because managements are evaluated primarily by the participants in the stock markets who take ownership in companies only to achieve short-term gains.

(2) Japanese Sogo-Shosha: Organic and Unstructured

Japanese company can be considered as an assembly of numerous small sections, each of which is a self contained entity with a comprehensive coverage of various managerial functions.(35) Therefore, it is not necessary to hire an employee for a specific function or responsibility. Instead, the employee is assigned to a specific job after he becomes a member of a company. As corporate requirements change, employees are shifted around within the firm to meet particular needs; their workload and the nature of their work can vary considerably over time. Further, the company demands collective responsibility of the smaller groups within the organization.

As noted, Japanese companies are driven by the desire for long-term accumulation of capital. The goal is pursued by having all members of the company, through their particular unit, participate in the corporate decision-making process. Furthermore, Japanese companies generally maintain a excess number of employees within the company. Compared to the US, the business environment in Japan tends to be less predictable, the labour force tends to be immo-

(34) Ibid., pp. 174-176.
(35) Ibid., p. 169.

bile, and the capital market is relatively underdeveloped. Therefore, Japanese companies can respond to, and take advantage of, unforeseen business opportunities only by maintaining a "slack" in the internal labor supply.

However, such an organic organization has a tendency to meet all new challenges through adaptive response and suffers from an inability to develop creative responses to new situations. When a new business opportunity appears to be beyond the immediate grasp of their capabilities, Japanese firms often simply forego the opportunity. Similarly, rather than meeting the challenge of overseas opportunities head-on through direct investment, Japanese companies chose foreign trade as the adaptive rather than creative response.

6. Financial Strategy

(1) US-Based MNCs: Internal Funds and Leveraging

US-based MNCs must rely on retained earnings or incur additional external debt to provide the capital for foreign direct investment. However, a company's financial soundness in the US is quite often judged on the basis of its leverage ratio. Hence, the ability to undertake additional foreign direct investment is necessarily limited by the ability of US-based MNCs to maintain an acceptable debt position. As a result, foreign direct investment occurs in stages and tends to be quite selective.

(2) Japanese Sogo-Shosha: Intermediation Between Banks and Manufacturers

The average ratio of net equity to total assets is 3.9% for the nine sogo-shosha. Such a high leverage ratio could not be sustained by a firm in the US; indeed, it would characterize an insolvent company. However, as a member of a business proup, sogo-shosha enjoy the support of the group and have direct access to a major group bank. The financial soundness of sogo-shosha is a function of the strength of support they receive from the groups.

Not only do sogo-shosha have almost limitless access to bank borrowings, they receive the lowest cost of fund possible. It is more difficult for smaller companies operating outside the large business groups to obtain external loans, and when possible, their cost of fund is generally 2～3% higher compared to sogo-shosha. Therefore, sogo-shosha often act as financial intermediaries, providing intercompany loans to smaller firms. The purpose is not simply to make profits by charging a premium on these loans. Providing the loans affords the sogo-shosha an opportunity to gain the right to supply raw materials and distribute the products of the smaller companies.

7. Balance Between Line Functions

(1) US-Based MNCs: Production vs. Sales

Historically, the relationship between the production manager and the outside sales manager has been competitive. In the US, sales people have often challenged production people for the leadership of the whole corporate management.[36]

Even today, most US business firms maintain two basic line functions, production and marketing, and a staff function, which includes, planning, finance, and personnel affairs. In any business firm, the value added from production is realized only when a sale is completed. However, the production has traditionally been the strongest position in US business firms. Production, especially with its extensive research and development capabilities, drives the company toward new products and permits US-based MNCs to maintain their technological edge in worldwide markets.

(2) Japanese Sogo-Shosha: Information and Marketing

Japanese sogo-shosha do not possess any significant production capabilities and purposely rely on the product of other companies. Sogo-shasha base their operations on extensive information capabilities, the way manufacturing firms rely on their production capabilties·for profitable operations. Their value added derives from their ability to match the buyer and seller for any particular product.

8. Diversification Strategy

(1) US-Based MNCs: Selective Diversification

The stages of market expansion and internationalization of US-based MNCs

(36) Dong Sung Cho, op. cit., pp. 227-228.

Exhibit 6: Diversification Process of US-Based MNCs

	Product	Area	Function	Organizational Structure
Regional Corporation	single	regional	single	unstructured
National Corporation	single	national	single	centralized
Integrated National Corporation	multiple	national	single	decentralized
Foreign Market Integrated Corporation	multiple	international	single	head office staff centered
Global Corporation	multiple	international	multiple	head office staff centered
Transnational Corporation	multiple	international	multiple	multiple head offices
Supra-national Corporation	multiple	international	multiple	supra-national

diversification achieved

are summarized in Exhibit 6. US firms began as regional corporations, producing and marketing a single product to the immediate geographic area. After the 1880s, US firms expanded through a series of intra-industry mergers and the rapid development of transportation system in the US, especially railroads, allowed regional companies to become national corporations. During 1920s, series of acquisitions of vertically-related companies led to development of the larger companies into integrated national corporations.

Further, with increasing foreign direct investment after the 1920s, US-based MNCs adopted a decentralized management structure, giving their overseas subsidiaries the profit responsibility for local operations. This geographic diversification resulted in foreign market integrated corporations. Increasing foreign operations led to a wider perspective on business activities, and US entrepreneurs sought to maximize the return on their overseas investment through functional integration into transportation, warehousing, and financing, as well as to strengthen production and sales. The result was global corporations.

The next stage of development led to the emergence of transnational corporations, which showed not only internationalization of operations but also internationalization of ownership. Such companies include Royal Dutch Shell and Unilever. It remains to be seen whether the next logical step of development into supra-national corporations will ever occur. These companies would be characterized by internationalization of the actual management of operations.

As Exhibit 6 shows, MNCs had achieved diversification in all three dimensions —in product, in area and in function—by the time they matured into global corporations. However, diversification strategy of US-based MNCs tended to be selective, and was founded on their monopolistic advantage in established industry segments. Product diversification was generally limited to vertical integration into related industry segments, while area diversification was concentrated within certain regions, usually in other developed countries. Similarly, functional diversification was limited to activities which could immediately increase the profitability of their main manufacturing activities.

The diversification model summarized in Exhibit 6 is derived from the experience of conglomerates such as ITT. More traditional US-based MNCs, however, continue to specialize in limited number of products based on extensive research and development. For example, GM continues to concentrate in automobile production, IBM in computers, and GE in electrical and electronic products. Therefore, US-based MNCs can be correctly characterized as international business enterprises that have achieved selective diversification in geographic area and function, but who remain undiversified in product.

(2) Japanese Sogo-Shosha: Diversification to Achieve Economies of Scale

The diversification process of Japanese sogo-shosha is summarized in Exhibit 7. Japanese GTCs began, in the late 19th century, as domestic trading companies to counter the increasing influence of foreign traders. After establishing

Exhibit 7: Internationalization Process of Japanese Sogo-Shoshas

	Product	Area	Function	Organizational Structure
Domestic Trading Company	multiple	domestic	single	unstructured
International Trading Company	multiple	international	single	centralized
Large Trading Company	multiple	international	single	marketing centered
Diversified Trading Company	multiple	international	multiple	decentralized
Foreign Direct Investment Oriented Trading Company	multiple	international	multiple	local operation centered
Global Competitive Strategy Oriented Trading Company	multiple	international	multiple	head office staff centered

Diversification achieved

their position in Japan's import market during the early 20th century, Japanese trading companies sought export markets for their increasingly wide range of products. The result was the emergence of international trading companies prior to World War II, characterized by both market and product diversification.

After World War II, Japanese trading companies developed into marketing oriented large trading companies. They began to establish foreign subsidiaries and by the early 1960s, formed an extensive international sales network linked by direct presence in major foreign markets. These networks constituted global logistics systems which became the source of comparative advantage for Japan's large trading companies in international trade.[37]

In an attempt to discourage foreign direct investment of manufacturers, Japanese trading companies sought to increase their activities beyond simple exports. The result was vertically-oriented functional integration into numerous support activities, such as raw material exploration and imports, transportation and warehousing; in effect they became truly diversified trading companies.

Even after the oil crisis in the early 1970s, Japan continued to show consistent growth in the midst of the worldwide economic recession. Sogo-shosha continued to be the leading force in Japan's exports. At the same time, Japanese sogo-shosha took on the added responsibility of organizing and undertaking Japan's foreign direct investment in raw material development and economic cooperation in less developed countries. Therefore, present Japanese sogo-shosha can be charaterized as foreign direct investment oriented trading companies.

As the Japanese economy continues to move away from capital and raw material intensive industries into high technology and service industries, Japanese sogo-shosha will inevitably lose their comparative advantage based on economies of scale in the raw material import market. They will begin to face increased competition from foreign producers of raw material and domestic consumers. Japanese sogo-shosha will have to adopt a global competitive strategy, deem-

(37) Shoho Kinugasa, *Nihonkigyo No Kokusaika Senryaku* (*Internalization Strategy of Japanese Corporations*), Nihon Keizai Shimbunsha, Tokyo, 1979, pp. 17–18.

phasizing results in individual foreign markets, while seeking global maximization of profits by offsetting losses in one market with greater profits in another.

A cursory look at Exhibits 6 and 7 could lead to the impression that diversified trading companies in Japan and global corporations in the US have pursued a similar diversification strategy. In fact, there is a fundamental difference in the diversification strategy of the two international business forms. US-based MNCs sought selective diversification. In contrast, Japanese sogo-shosha have diversified without restrictin in terms of product, area, or function in order to achieve economies of scale. Therefore, it is not surprising that phrases like "from missiles to noodles" have been frequently used to describe Japanese GTCs.

9. Business Strategies Summarized

Exhibit 8 summarizes the differences in business strategies of US-based MNCs and Japanese sogo-shosha.

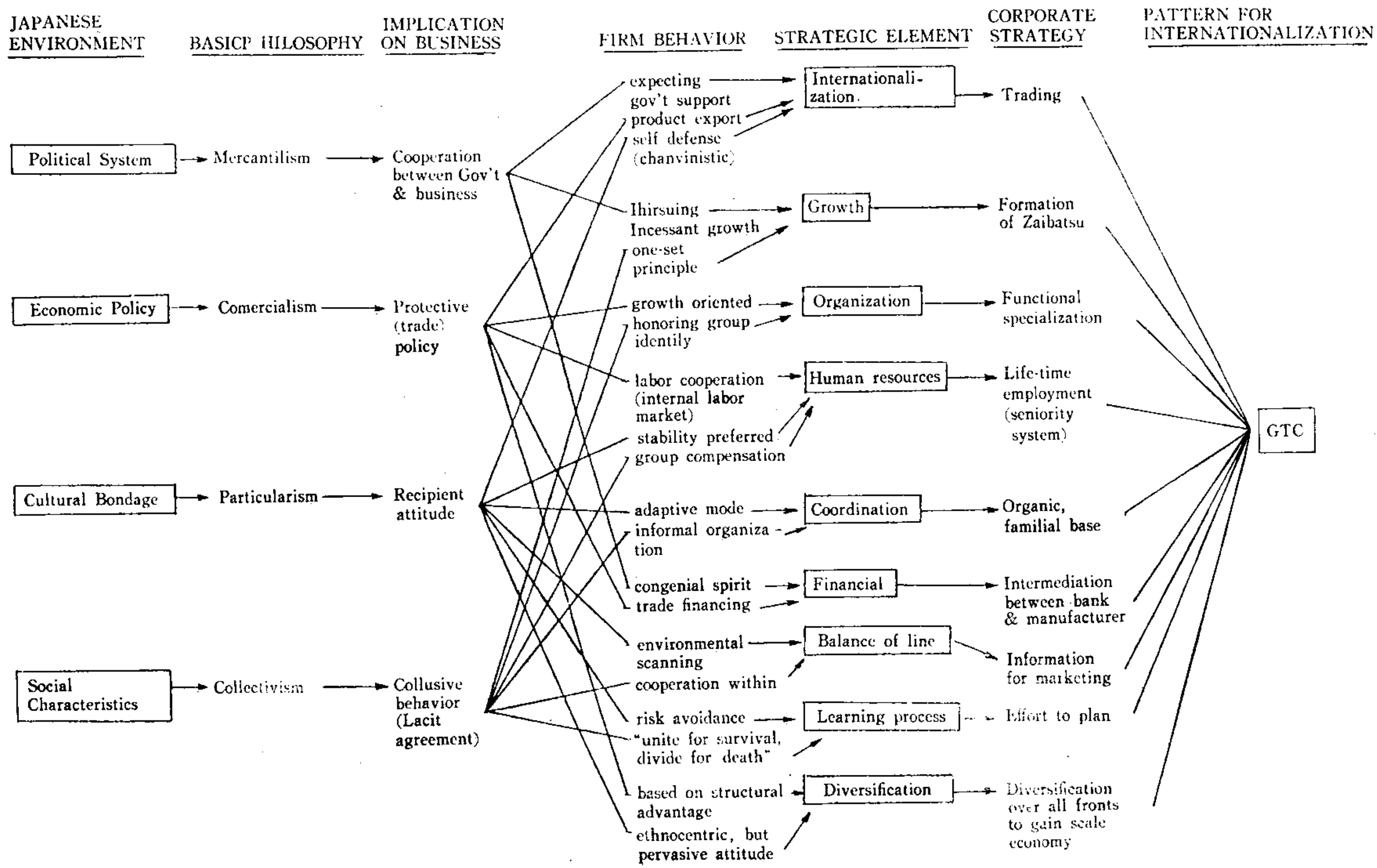
Exhibit 8: Business Strategies of US-based MNCs and Japanese Sogo-Shoshas Compared

	US-based MNCs	Japanese Sogo-Shoshas
Internationalization	foreign direct investment: export of factors of production and import of finished goods.	foreign trade: import of raw materials and export of finished goods
External Growth	mergers and acquisitions	formation of business groups
Organization	decentralized by industry segments	functional specialization and coordination
Personnel	short term employment and individual	life-time employment and seniority system
Coordination	mechanistic and contractual	organic and undefined
Financial	internal funds and leveraging	intermediation between banks and manufacturers
Line Function Balance	production vs. sales	information and marketing
Diversification	selective and based on monopolistic advantage	in all fronts to achieve economies of scale

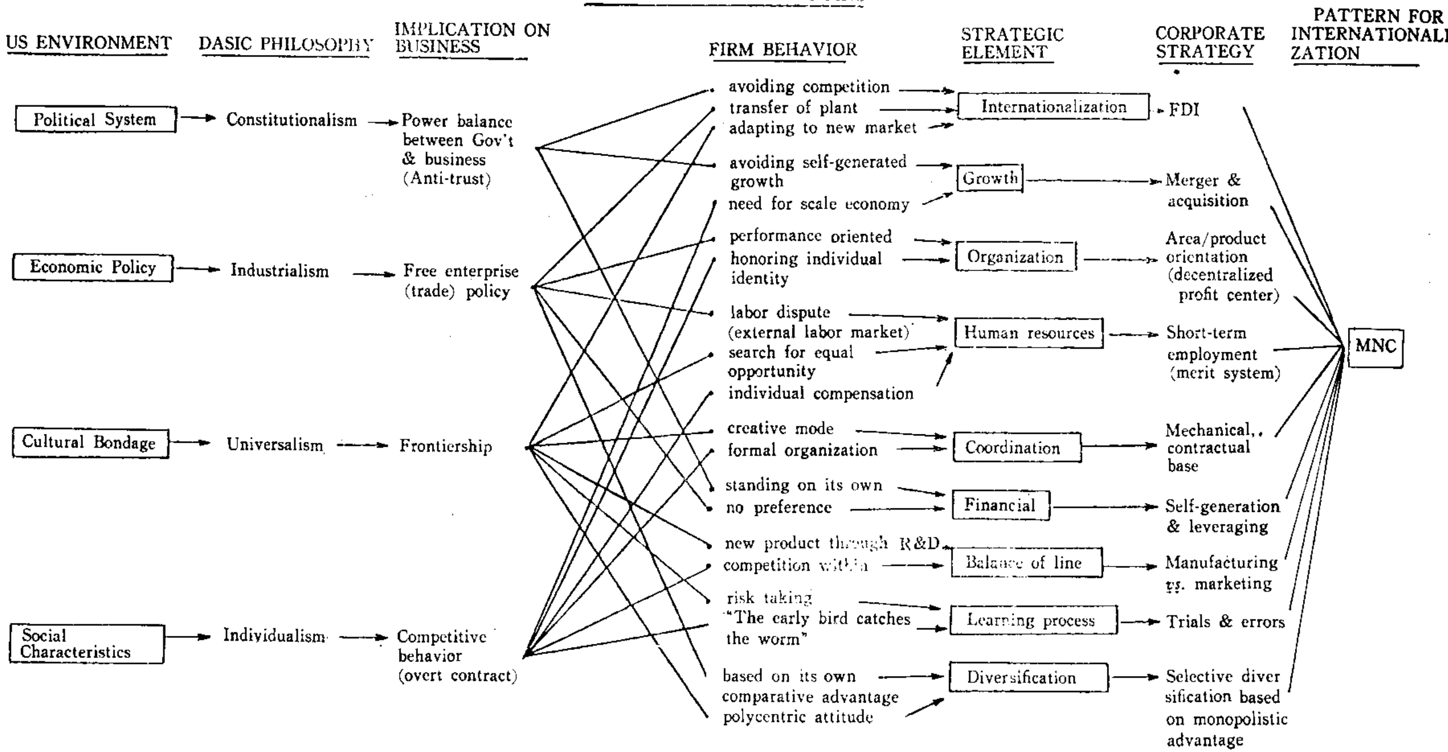
IV. Implications For Korean Gtc

The preceding observations on business environments and strategies are related

Japanese Environment Conducive to GTC



US Environment Conducive to MNC



and summarized for the US in Exhibit 9, and for Japan in Exhibit 10. It is clear that US-based MNCs and Japanese sogo-shosha are two distinctive forms of international business organization and cannot be considered as international business concerns at different stages of maturity. They are the products of the environment in each country. A unique set of political, economic, cultural, and social pressures have forced the choice of the MNC form in the US, and the GTC form in Japan, in their respective processes of internationalization.

Therefore, neither the MNC form nor the GTC form can be easily offered as a corporate growth model for other countries. Different environmental pressures in each country inhibit either international business form or their strategies from being transplanted wholesale. As an example, consider the case of Korea. First, the political environment in Korea cannot be considered purely constitutional or merchantilistic. Authoritarian regimes in Korea both supported the business sector as a means of increasing their political influence and regulated business activities in the hopes of gaining popular support. Second, processes of industrialization and internationalization through trade coincided in Korea. This is not consistent with the experience of the US, where foreign direct investment was pursued after domestic industrialization, or with the experience of Japan, where industrialization was founded on extensive domestic commerce. Third, the cultural environment in Korea is characterized by an unsystematic combination of both weaknesses and strengths from local and imported values, and the underlying cultural current is not easily identified as universalism or particularism. Fourth, interpersonal relations in Korea often results in simple nepotism or sectionalism, and personal behavioral patterns cannot be generalized as individualist or collectivist.

Environmental differences will not allow Korea to simply adopt the MNC form of the US, or even the GTC form of Japan; at least, similar success cannot be reasonably expected. The lesson is no less true for other countries. This does not mean that others cannot benefit from the experience of the US or Japan. While each country will have to establish its own form of international business organization, each may be able to modify and incorporate the strengths of the US or Japanese business strategies.