

Entrepreneurship in Japan

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■ Entrepreneurship

❖ Definition

- **Entrepreneurship** refers to the **creation of new value** by an existing organization or new venture that **involves the assumption of risk**.
- **New value** can be created in **many different contexts** as follows: (1) Start-up ventures, (2) major corporations, (3) family-owned businesses, (4) non-profit organizations, & (5) established institutions.

❖ ‘3’ Key Factors in New Value Creation

1. Entrepreneurial **opportunity**;
2. Entrepreneurial **resources**; &
3. Entrepreneurs’ **ability & willingness** to undertake the opportunity.



■ Discussions

Why is Japan Lagging in Entrepreneurship?



■ '5' Critical Causes of Japan's Entrepreneurship Gap

❖ Cultural Factors

- The **Japanese culture** is one that **discourages risk-taking behaviors** or the **pursuit of unexploited opportunities**.
- ... tends to focus on the importance of **rules, tradition & customs**.
- ... emphasizes **conventionality, consistency, community, & relative risk aversion**.

❖ Societal Factors

- The **social status of entrepreneurs** in Japan is **not high**.
- The **typical Japanese parent** often does **not support** his or her child's aspiration of becoming an entrepreneur.
- They wish their children to **go to an elite public university & join the bureaucracy or a major *keiretsu***, such as *Mitsubishi* or *Mitsui*.
- This conservative mindset is linked to **life-time employment**.

Source: Knowledge@Wharton. (2013). Finance: The Entrepreneurship Vacuum in Japan: Why It Matters & How to Address It.



■ ‘5’ Critical Causes of Japan’s Entrepreneurship Gap

❖ Educational Factors

- **Limited educational institutions** prepare students to be entrepreneurs.
- *“No more than 1% of the students were engaged in entrepreneurship”.*

❖ Legal Factors

- **Bankruptcy laws** should be modified because **debt is transferrable** –
The family is still liable for the unpaid debt even if the founder dies.

❖ Financial Factors

- **Banks are unwilling to lend money** to entrepreneurs. Even if they did, banks tend to **impose harsh conditions** on start-ups.
- US-based venture capitalists view **Japan** as to its **small market**.
- Many **Japanese domestic venture capital firms** are **conservative** since they are managed by **salary men**.

Source: Knowledge@Wharton. (2013). Finance: The Entrepreneurship Vacuum in Japan: Why It Matters & How to Address It.



■ How to Promote Opportunity-Driven Entrepreneurship?

❖ The Israel Model

- Generation of a **robust venture capital & entrepreneurship** by **encouraging FDI**;
- Promotion of **open immigration policies**;
- Reallocation of **government spending**;
- Strengthening of **private-sector incubators**;
- Alignments of **research institutions, the military & aspirational entrepreneurs**; &
- Special emphasis on **entrepreneurship in schools** across the country.

Source: Knowledge@Wharton. (2013). Finance: The Entrepreneurship Vacuum in Japan: Why It Matters & How to Address It.

Ahmadjian & Robbins (2005). “A Clash of Capitalisms: Foreign Shareholders & Corporate Restructuring in 1990s Japan”, *American Sociological Review*, 70(3), 451-471.

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A Clash of Capitalisms in Japan



■ Questions

Q1: What characterizes **Japan's stakeholder capitalism** in comparison with the **Anglo-American system**?

Q2: Why & how do **foreign investors** affect **Japanese firms**?

Q3: Explain the underlying **rationale** for the **moderating effects** of **financial institutions & business groups** on the association between foreign ownership & firm strategy.

Q4: Do you think that **Japanese firms** are prone to **adopt** the **Anglo-American capitalism**? If yes, why? If not, why not?

Q5: Discuss **potential pitfalls & weaknesses** of this paper.



■ The Core Argument of This Article

❖ Research Goal

- To address theoretical questions about **interactions between different business systems**.
- Is the **Japanese business model** being **dismantled & adopting** the **American shareholder system**?

❖ Why Important?

1. This study has implications for a broader understanding of **institutional change**.
2. There is a **dearth of research** on the potential **mechanisms** by which **business systems change or continue**.
3. Relatedly, this study adds value to the **convergence-divergence literature** by investigating the **condition** under which **foreign investors** exert **pressures** to **firm strategy**.

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■ Background & Theory

❖ Key Points

- A national economy is a configuration of actors – The state, corporate elites, labor, capital – whose interests are shaped by both formal rules & informal norms (Aguilera & Jackson, 2003).
- Q: **WHY** don't business systems converge even in the development of global markets for capital, products, labor & ideas?
 - i. There is **no one best way to organize an economy**.
 - ii. **Powerful actors who shape institutions to advance their own preferences are likely to resist change** (Fligstein, 2001).
- The **globalization of financial markets & the emergence of foreign investors** to invest in distant economies can be a **political process** by which **new actors with different interests** enter an economy.

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■ ‘2’ Distinctive Business Systems

The Japanese System

- > A wide range of stakeholders (*i.e.*, **employees, banks, customers, suppliers & shareholders**) influence firm strategy.
- > **Long-term relationships.**
- > An assurance of **permanent employment & steadily rising wages for cooperative labor relations.**
- > **Strong norms against downsizing** since dismissing employees indicates **an emotional issue.**

The US System

- > **Shareholding** is a vehicle for investment.
- > “*Investor capitalism*” = “*Maximizing shareholder value*”.
- > **Agency theory:** Shareholders (**principles**) & managers (**agents**).
- > **Institutional investors** > individuals.
- > Pension fund managers **could be sued** if they do not act in the interests of beneficiaries.
- > **Firms that downsized** often are **rewarded by the stock market.**

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■ Foreign Institutional Investors Come to Japan

❖ The Rise of Foreign Ownership of Japanese Firms

- Between **1990 & 2020**, foreign ownership of Japanese shares soared from **4.2% to 30.2%** of all listed shares.

❖ Which Foreign Investors Dominate?

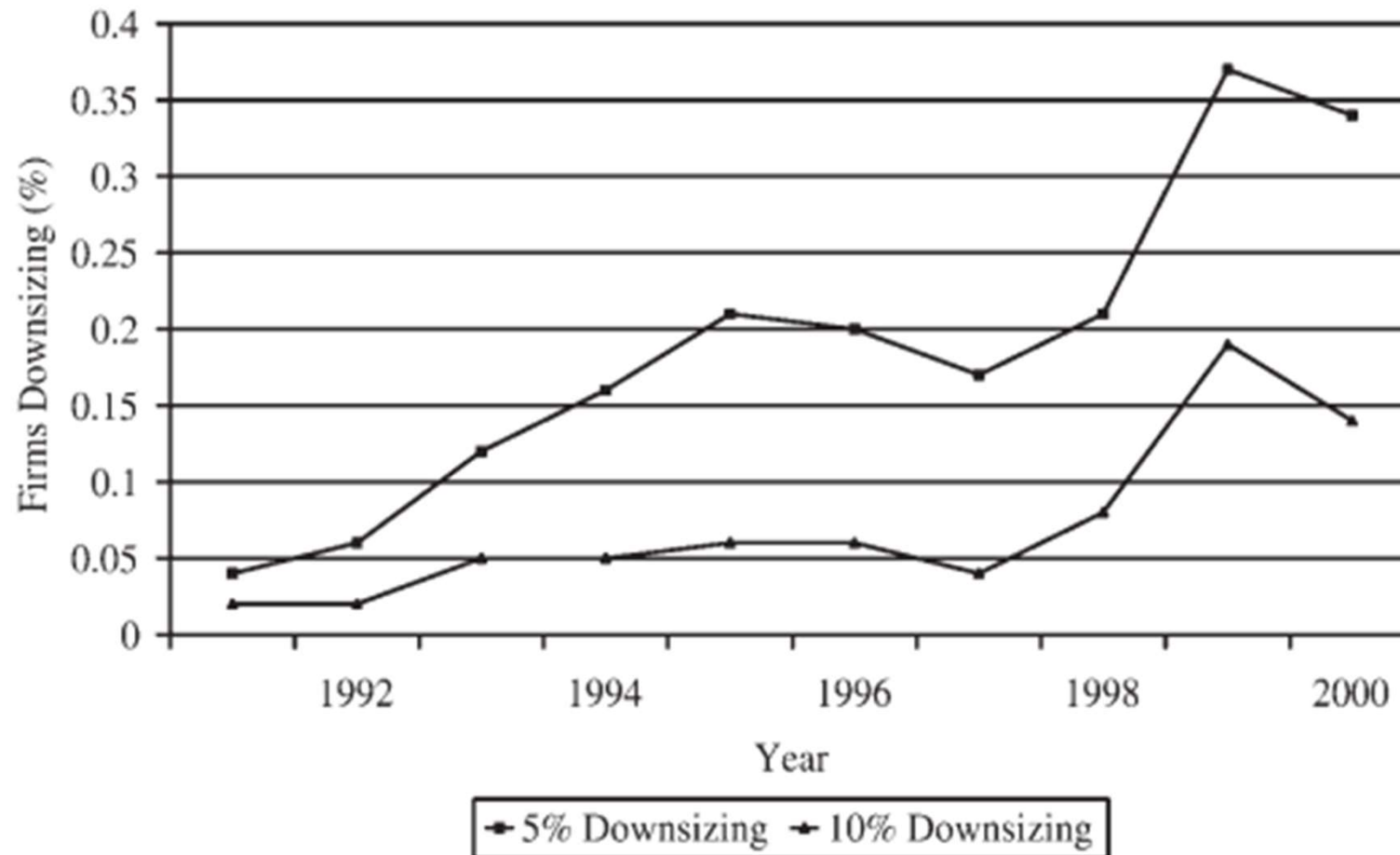
- The **top shareholders** of each firm were overwhelmingly **United States or United Kingdom based**.
- Other foreign investors included **offshore funds (Bermuda) & German funds** (*e.g.*, **Deutsche Bank**).

❖ Differences from Domestic Investors?

- Foreign investors set **higher required rates of return** than domestic investors.
- **Rising pressures** to Japanese firms to perform **aggressive restructuring** (*e.g.*, **reinforcing business portfolios &/or liquidating low-profitability assets**)

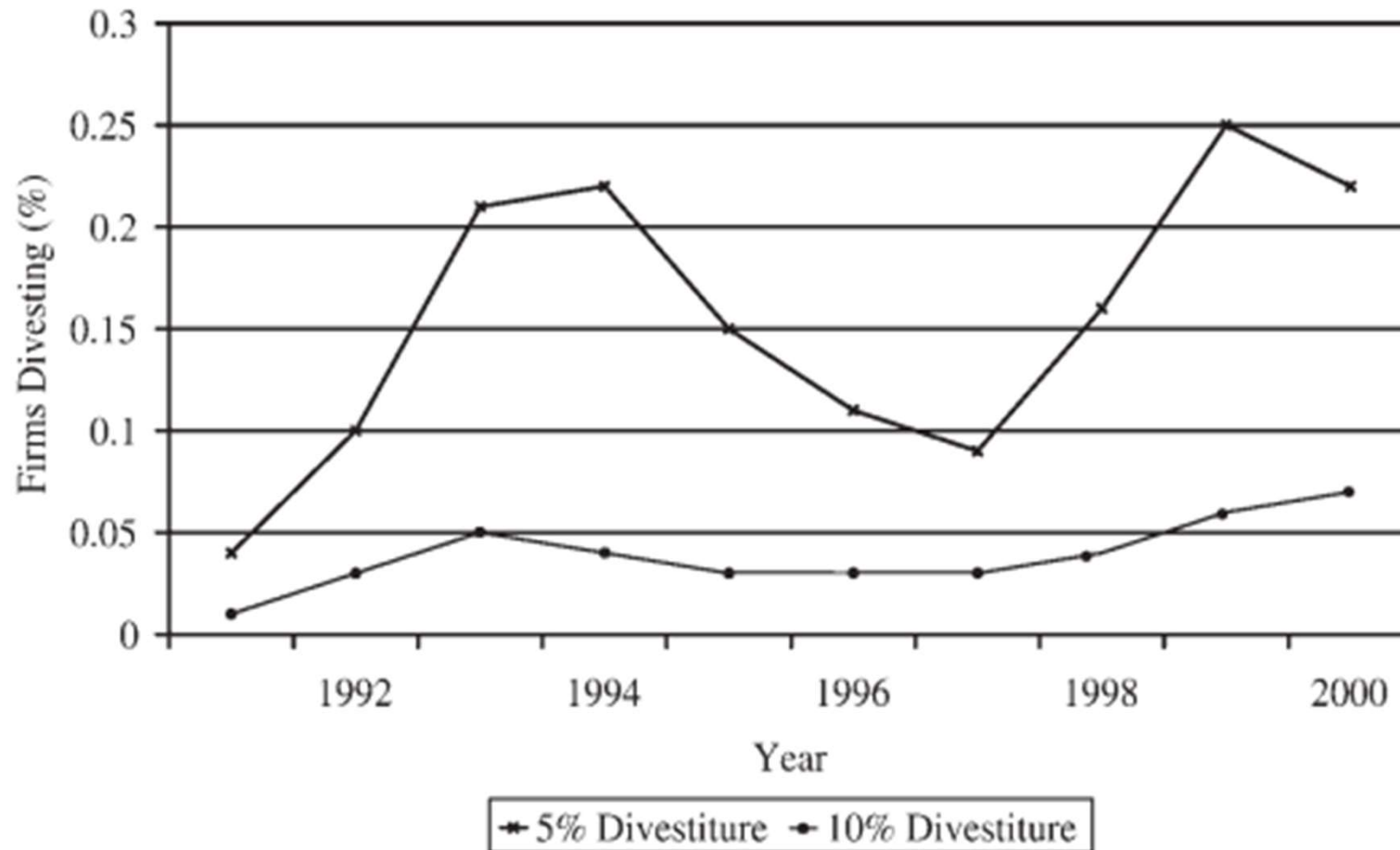
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■ % of Firms Downsizing in a Given Year, 1991-2000



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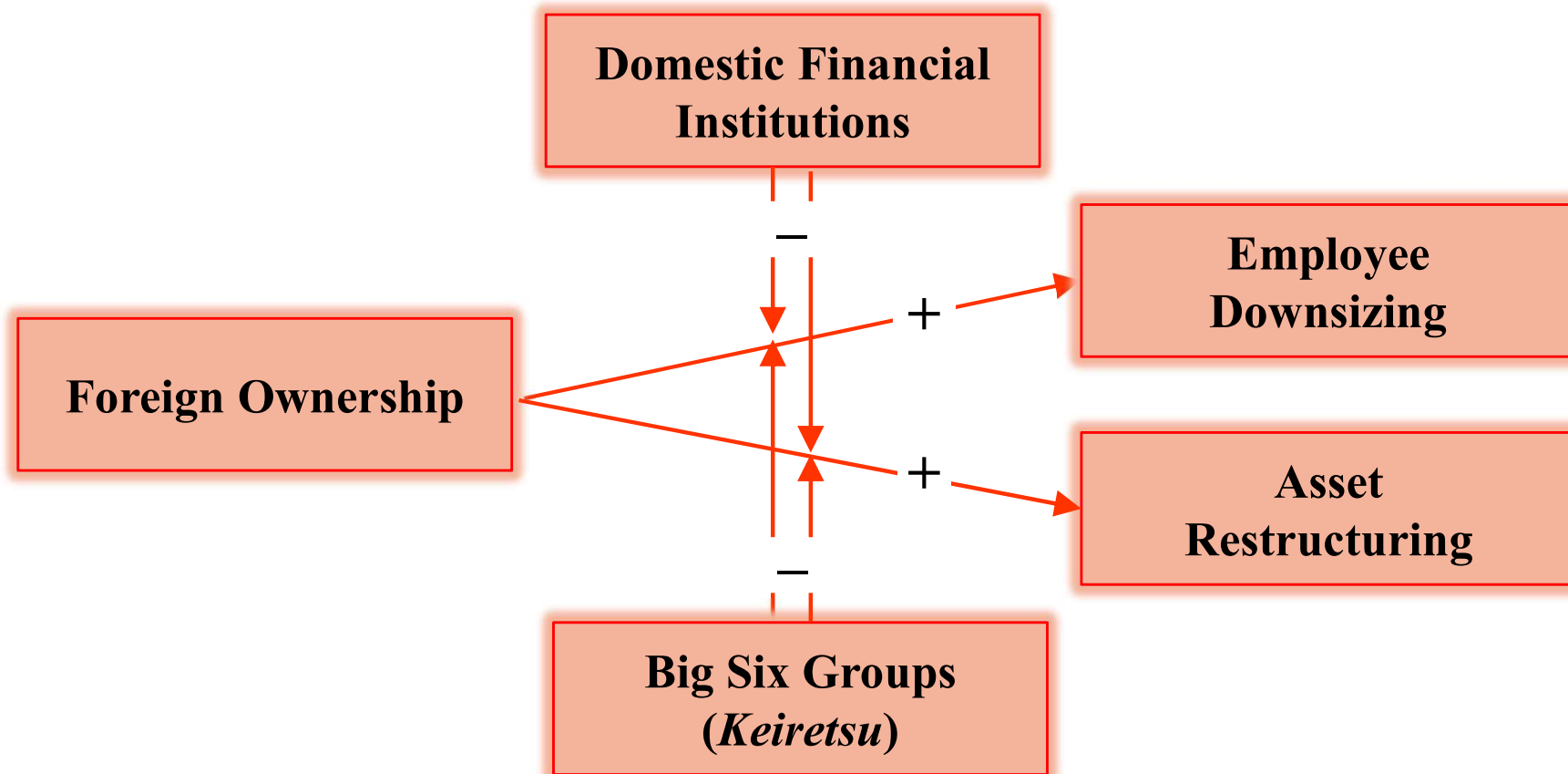
■ % of Firms Divesting Assets in a Given Year, 1991-2000



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■ Conceptual Framework



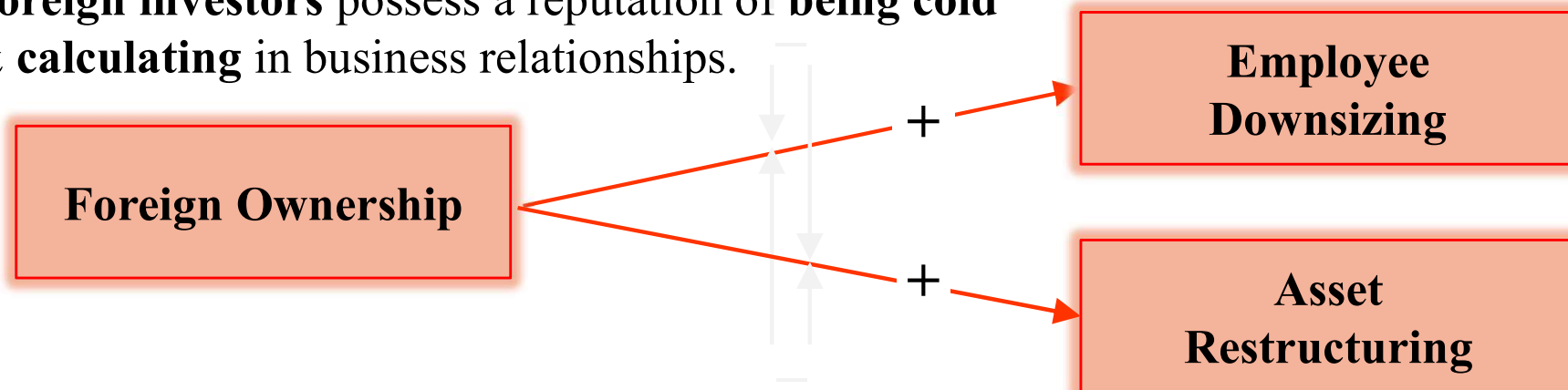
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■ Hypothesis 1

- ❖ Foreign shareholders use **exit & voice** to make their interests clear to management.
- ❖ Foreigners has an **excessive influence on share prices** because they were much more **active in buying & selling shares** than their Japanese counterparts.

- ❖ Foreign investors possess a reputation of **being cold & calculating** in business relationships.



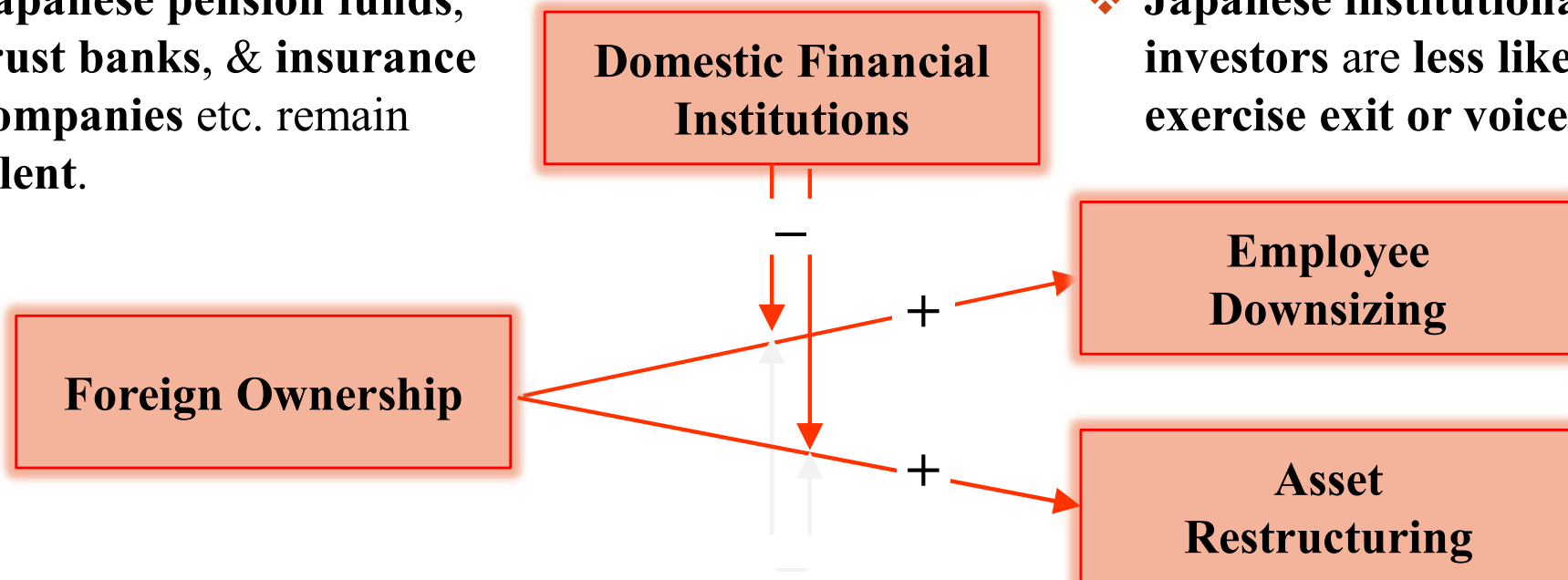
- ❖ *“When Japanese managers see foreign ownership on their share moving from 5% to 10% to 20%, they feel **a strong psychological pressure** (a greater sense of urgency) to pay attention to **corporate governance**.*

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■ Hypothesis 2

- ❖ Japanese pension funds, trust banks, & insurance companies etc. remain silent.



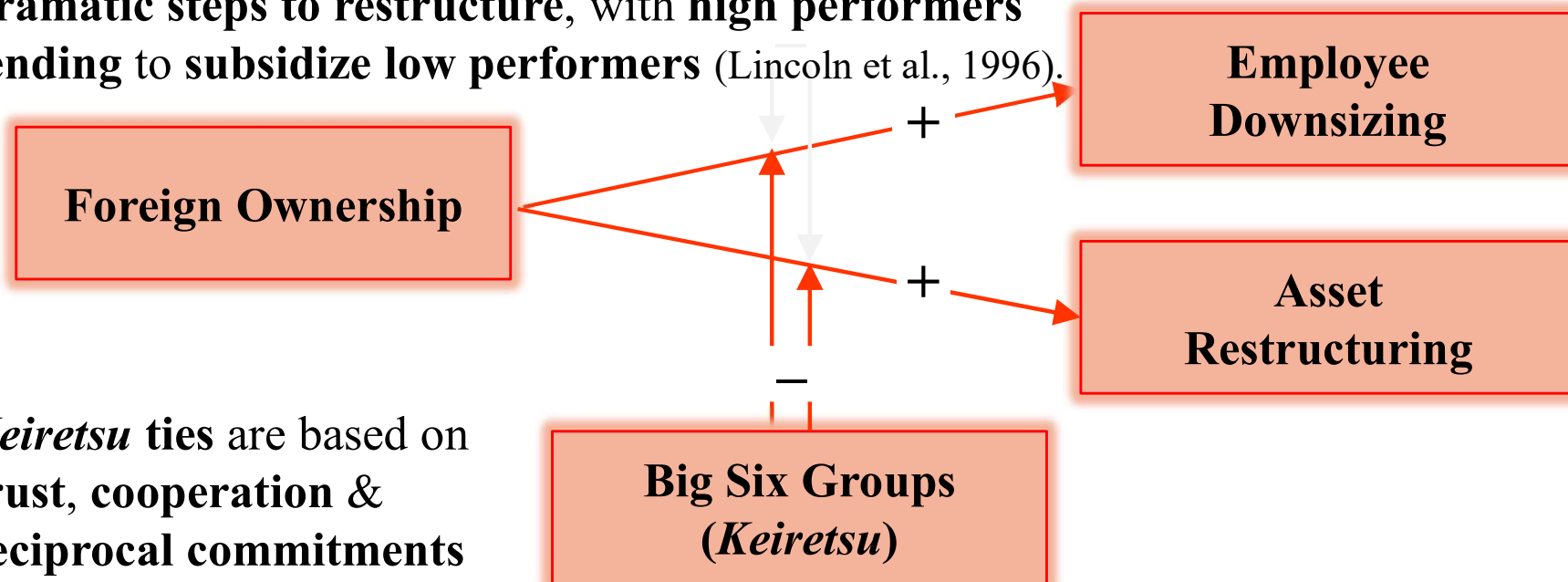
- ❖ Japanese institutional investors vote against an immediate return on their investments in favor of maintaining long-term relationships.
- ❖ *“Bankers try to avoid any drastic divestiture on the part of the clients at the expense of the bank’s own profit because banks should be socially responsible beings.”*

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■ Hypothesis 3

- ❖ Social networks are important in Japan, where a **dense web of ties**, through **ownership stakes, interlocking directorships, groupwide councils, & trading relationships**, links many firms into business groups (Gerlach, 1992).
- ❖ Business groups **buffer firms from needing to take dramatic steps to restructure**, with **high performers tending to subsidize low performers** (Lincoln et al., 1996).



- ❖ *Keiretsu* ties are based on **trust, cooperation & reciprocal commitments** over many time periods.

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■ Empirical Results (Downsizings of 5% of 1,108 Firms)

% Shares held by foreigners (t-1)	-.157 (.260)	1.561** (.562)	.050 (.303)	1.470** (.564)
% Shares held by financial institutions (t-1)	-.258 (.136)	.044 (.161)	-.268* (.148)	-.005 (.164)
1 = Member of big six group	.130* (.054)	.137* (.054)	.296*** (.079)	.252** (.084)
% Foreign ownership * % Financial ownership		-5.320*** (1.524)		-4.588** (1.576)
% Foreign ownership * Member of big six group			-1.956** (.734)	-1.371 (.778)
Constant	-.357 (.420)	-.441 (.448)	-.456 (.449)	-.349 (.539)
Log likelihood	-4326.58	-4321.76	-4315.49	-4318.25
				-4313.91

Note: Random effects probit coefficients with standard errors shown in parentheses; 18 dummy variables for industry significant, not reported.

* $p < .05$; ** $p < .01$; *** $p < .001$ (two-tailed tests).

❖ A group member may be more likely to restructure if it knows that it can send its excess employees to another group member.

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■ Empirical Results (Divestitures of 5% of 1,108 Firms)

% Shares held by foreigners (t-1)	-.023 (.263)	1.836** (.564)	-.011 (.272)	1.878** (.567)
% Shares held by financial institutions (t-1)	-.031 (.136)	.286 (.161)	-.032 (.136)	.305 (.163)
1 = member of big six group	-.021 (.058)	-.014 (.058)	-.009 (.088)	-.067 (.089)
→ % Foreign ownership * % Financial ownership		-5.700*** (1.522)		-6.010*** (1.573)
% Foreign ownership * Member of big six group			-.138 (.780)	.642 (.808)
Constant	-.453 (.441)	-.516 (.470)	-.487 (.471)	-.509 (.472)
Log likelihood	-4165.57	-4165.47	-4158.32	-4165.46
				-4158.01

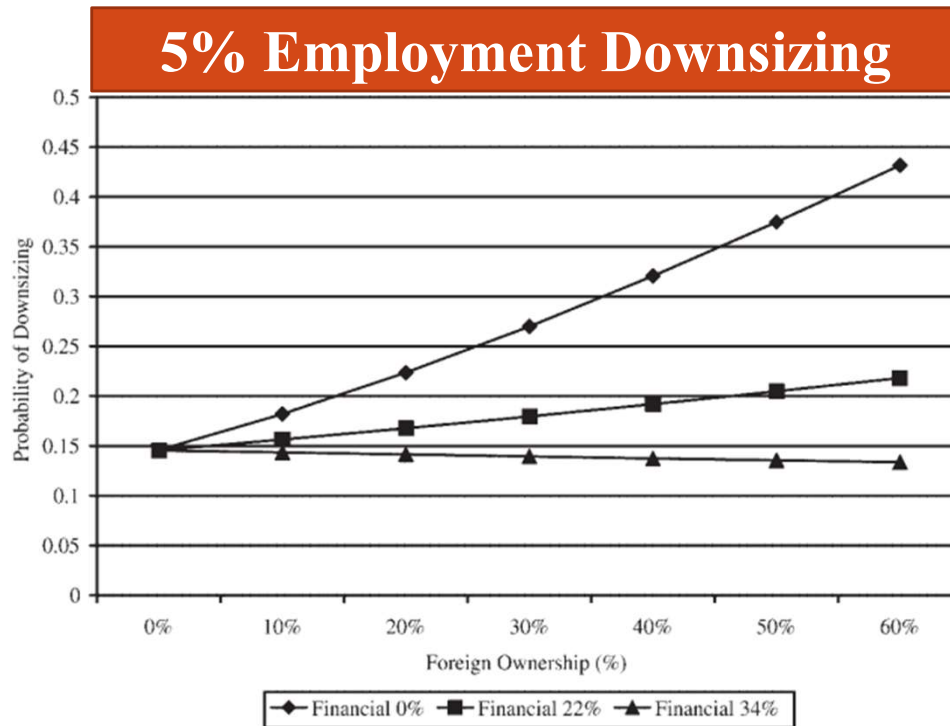
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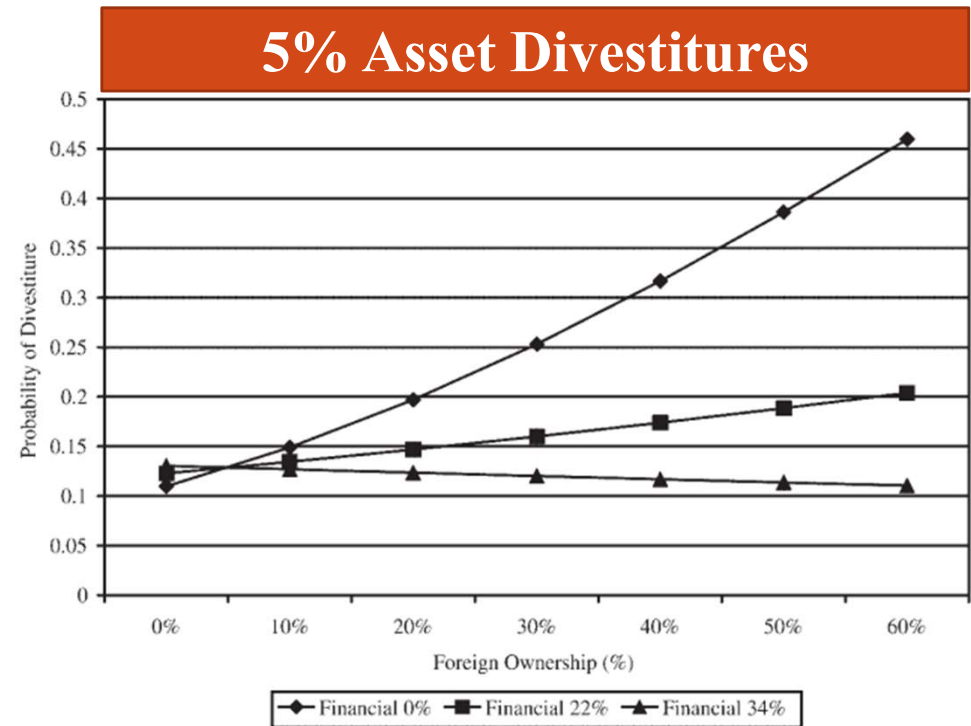
❖ Firms with higher levels of ownership by domestic financial institutions were able to resist the influence of foreigners.

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Foreign Influence × Financial Institutions



- ❖ In a firm with no financial ownership, an increase in foreign ownership from 0 to 60% increases the probability of downsizing from 15 to 45%.



- ❖ Foreign investors are more likely to facilitate asset restructuring in firms less embedded in the existing stakeholder.

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■ Conclusive Remarks

❖ Managerial Relevance

- **Foreign ownership** leads to **increased restructuring** in firms unlikely embedded in the **Japanese stakeholder system**.
- **Foreign actors**, with different interests & incentives, **replaced local shareholders** who were tightly linked to the stakeholder system.
- The **Japanese stakeholder system** was **NOT** overwhelmed by a superior shareholder system.
- **Restructuring** among foreign owned firms may **remove** the perceived **illegitimacy** of **radical strategic actions** & encourage their **spread** to **larger, older, & more prestigious firms**.



■ Conclusive Remarks

❖ Suggestions for Future Research

- Identify **different types of foreign portfolio investors** & their influence: *e.g.*, (1) large index funds (*e.g.*, Black Rock, Charles Schwab, Fidelity, Vanguard), (2) hedge funds, & (3) other actively managed funds.
- The **validity** of this study's results needs to be verified by **comparing the influence of foreign investors** across **national borders**.
- Further research is needed to explore how **foreign investor influence** on changes in many other types of **firm strategic behavior** (*e.g.*, cross-border M&As, divestment etc.).

The End of Today's Lecture



ご清聴有難う御座いました。

Thank you so much!

Vielen Dank für Ihre Aufmerksamkeit!

Grazie mille !

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