Japan's Corporate Governance Reforms: Effects on Corporate Dynamics and Labor-Related Repercussions

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List of Abbreviations

AGM – annual general meeting

BoJ – Bank of Japan

CFROI – cash-flow return on investment

CG – corporate governance

CME – coordinated market economy

CVA – cash value added

DBJ – Development Bank of Japan

DOI – degree of internationalization

DPJ – Democratic Party of Japan

DPS – dividends per share

EP – economic profit

EPS – earnings per share

EVA – economic value added

FAS – Financial Accounting Standards

FSTS – foreign sales as a percentage of total sales

GAAP – generally accepted accounting principles

GB – government bond

GDP – gross domestic product

GPIF – Government Pension Investment Fund

HMFN – hierarchical market-firm nexus

HRM – human resource management

HRM – human resource management

IAS – International Accounting Standards

IB – international business

IFRS – International Financial Reporting Standards

ILO – International Labour Organization

IMF – International Monetary Fund

JACD – Japan Association of Corporate Directors

JCC – Japan's Commercial Code

JCGC – Japan's Corporate Governance Code

JETRO – Japan External Trade Organization

JILPT – Japan Institute for Labour Policy and Training

JRS – Japan Revitalization Strategy

JSC – Japan's Stewardship Code

LDP – Liberal Democratic Party

LME – liberal market economy

LMM – linear mixed model

M&A – mergers and acquisitions

MBS – main bank system

METI – Ministry of Economy, Trade and Industry

MHLW – Ministry of Health Labour and Welfare

MOF – Ministry of Finance

MOL – Ministry of Labour

MVA – market value added

NI – net income

NTT – Nippon Telegraph and Telephone

OECD – Organisation for Economic Co-operation and Development

OLS – ordinary least squares

OPEC – Organization of the Petroleum Exporting Countries

PBR – price to book ratio

ROCE – return on capital employed

ROE – return on equity

ROI – return on investment

RONA – return on net assets

RQ – research question

SMEs – small and medium enterprises

SDP – Social Democratic Party

SPD – serious psychological distress

SV – shareholder value

TA – total assets

TSE – Tokyo Stock Exchange

TSR – total shareholder return

VoC – Varieties of Capitalism

Chapter 1: Introduction

During the last three decades, Japan has experienced sluggish economic growth. The relational corporate-finance setting needed drastic reforms in the face of massive damage caused by non-performing loans in the early 1990s. The crisis was particularly felt by *keiretsu*-affiliated[1] banks that lost many of their partner-companies since they gradually became more equity-oriented around mid-1980s. Many of the new corporate clients failed to pay back the credits, which triggered the 1990's bubble burst. Furthermore, as the Bank for International Settlements severed its debt-to-capital ratio, banks had to massively sell off the shares of their affiliated companies (Montgomery, 2005). The Bank of Japan's lack of timely support for companies and banks during the early 1990s, and the lack of determination for corporate restructuring led to a prolonged economic crisis (Mikitani & Posen, 2000, pp. 15-16; Patrick, 2004, p. 19). As the share prices of Japanese companies dropped, foreign institutional investors took advantage of this situation by acquiring large proportions of stock.

Before the 1980s, the Japanese financial sector was highly regulated due to the presence of financial intermediaries that generated stable sources of indirect finance (i.e., bank loans) for the firms (Toya & Amyx, 2006, p. 104). Most of the funds earned by banks were accumulated through household deposits. Until the early 1980s, close and lasting partnerships between corporate and financial institutions called the main bank system (MBS) provided means for corporate survival. However, following the oil crises of the 1970s that substantially raised the prices for imported crude, many firms switched to direct (i.e., equity) finance, thus breaking the old business-finance scheme. Having accumulated substantial surpluses by the 1980s, numerous companies started to abandon their partnerships with the main banks. Thus, the latter had to search for new borrowers. While the monitoring system of that time was relational, banks did not possess sufficient information about their new clients, many of which later appeared to be insolvent. This resulted in the creation of a bubble with the subsequent collapse of stock and equity markets in 1989-92. Companies, on the other hand, have also faced significant losses due to improper investments. Due to changes in accounting rules in early 1990s that made companies report the shares not at purchase but at market value, the process of cross-shareholdings' unwinding has unfolded (Ahmadjian & Robbins, 2005, p. 455). "The ratio

[1] *Keiretsu* – large enterprises notable for their subcontractors' vertical chains and/or horizontal links with partner-banks coordinated by the Bank of Japan (Inoué & Yamada, 2002)

of cross-shareholdings… plummeted from 15.3% in 1996 down to 9.2% in 2006" (Miyajima, Hoda & Ogawa, 2016, p. 7). Simultaneously, the ever-growing proportion of outsider shareholders that made use of devaluated Japanese stock by purchasing it, has started to claim monitoring credentials to ensure adequate returns to their investments (Yoshikawa & McGuire, 2008, p. 12).

During the postwar period, shareholders in Japanese public companies did not have the capacity to directly monitor their investee firms. In turn, the monitoring function was carried through the MBS. As corporate finance was becoming more equity- rather than bank-based, shareholders have claimed more transparency for linking corporate performance with market indices. Hence, the need for corporate management to be accountable to corporate owners for solving the "agency problem" has become a cornerstone in recent Japanese corporate governance reforms (Nakamura, 2011, p. 190). The agenda for enhancing shareholders' rights in Japanese listed firms has been largely shaped by the government (Nakamura, 2011) and foreign institutional investors that advanced the constitution of market as a legitimizing agency for publicly traded companies (Ahmadjian, 2007). The implementation of corporate governance reforms has however been greatly affected by the entrenched institutional legacy.

The kind of change the government and foreign shareholders have argued for, had to be promoted within an adverse environment. Namely, execution and monitoring have mostly been unseparated under the stakeholder model of corporate governance. The stakeholder model is preoccupied with "a variety of firm constituencies – including employees, suppliers and customers, and the communities companies are located in – enjoy 'voice' in the firm and whose interests are to be balanced against each other in management decision-making" (Vitols, 2001, p. 337). Unlike the "Anglo-Saxon" disciplining by market evolving through a possibility of a hostile takeover, monitoring of Japanese firms is known to be relational and trust-based. Thus, in order to subject managerial behavior to outside instance, such as minority shareholders, policymakers had to ensure managers that the drift towards market-based discipline would firstly be inevitable, and, secondly, evolve as a non-compulsory initiative.

RQ 1. What have been the effects of the ongoing corporate governance reforms in Japan on the corporate dynamics?

Literature gap 1

During the postwar period, the relational bank system was geared towards national support of key industries. However, as the bubble burst in early 1990s depleted the assets of companies and banks, the new recapitalization channels for Japanese companies had to be discovered. Against this background, "government's support for Japan's industry-led postwar model switched to actively trying to dismantle it…, and… a neoliberal, financial view of wealth generation steadily gained influence" (Whittaker, 2017, p. 10).

While it has not been an easy task to shake the relational principles of running a Japanese company, the government effectively used the influence of foreign investors to promote arm's-length shareholder-oriented corporate governance reforms. "Increased board independence, disclosure and transparency, downsizing and asset divestiture occurred in response to an increase in foreign portfolio investment in Japan" (Ahmadjian, 2007, p. 145).

Thus, the corporate governance reforms in Japan have aimed to introduce arm's-length monitoring over incumbent managers that have traditionally acted as both executives and monitors (Itami, 2005; Patrick, 2016). The motivation behind this was not the irresponsive behavior of CEOs, as in the case of the U.S. (Jackson, 2017) but rather the need to become accountable towards increasingly influential shareholders as the new major capital providers.

If judged by the number of adoptees of the U.S.-originated corporate governance model (TSE, 2018), one can conclude that there has been hardly any influence of the ongoing reforms on the corporate dynamics. However, the pace of corporate government reform would suggest the entrenchment of shareholder-oriented discourse. Yorozu (2015) applies the concept of "narrative management" to Japanese companies to show how their communicative strategies have been reoriented towards the boosting of shareholders' confidence starting from the late 1990s. Drawing upon the article of Ovsiannikov (2017), I also argue in Chapter 4 that the corporate governance reforms have been consistently shaping the discourse favoring managerial alignment with shareholders.

Another important gap in the literature is the missing analysis of shareholder value enhancement in Japan as a part of the corporate financializaiton process. In other words, it is important to show, whether the growing attention to shareholder value causes decreased returns to ordinary employees. Yamada & Hirano (2015) mention that while before 1990s, the main managerial concern was the establishment of cooperative relations with workers, during the recent decades the CEOs of large Japanese companies have been mostly

concerned with meeting shareholders' expectations. Jackson (2016) suggests approaching the enhancement of shareholder value in Japan as a display of corporate financialization: "More recent research is needed to examine how (partial) financialization is linked to other concepts like hybridization or dualization" (p. 7). Lechevalier, Debanes & Shin (2016) characterize the post-1990s development of the Japanese economy as the transition from the stage of "financial containment and mobilization" to "financial empowerment and disconnection". In other words, the financial sector has become increasingly market-oriented and, although playing a major part in country's macroeconomic trends, is no longer subordinated to the industrial needs as it was under the main bank system. Lechevalier (2016, pp. 69-70) adds that the neoliberal policies in Japan have brought about financialization, which, in turn, contributed to inter-firm diversity. I address the issue of corporate financialization in Chapter 5.

RQ 2. How have the corporate governance reforms impacted on the labor situation at Japanese companies?

Literature gap 2. The link between shareholders' rights enhancement and decreased labor bargaining power has been extensively highlighted in the literature employing "institutional complementarity hypothesis". The above-mentioned application of this argument to Japan by Aoki (1994) is a part of a general argument about the fact that "functionality of an institutional form is conditioned by other institutions" (Höpner, 2005, p. 331). The idea of a "companyist compromise" (Yamada, 2002), which is central to this study, has also originated from this hypothesis. More and more authors emphasize the interconnectedness between financial and labor deregulation (Watanabe, 2015). Moreover, Shibata (2015) demonstrated that the category most vulnerable to neoliberal reforms in Japan is temporary workers[2]. Existing studies have also extensively covered the normative labor deregulation – from 1999 amendment of the Temporary Work Agency Law until 2015 revision of the Worker Dispatch Act – due to which, temporary employment was allowed for all occupations and sectors.

[2] Apart from being a common trend for the countries characterized by the strong protection of core-workforce (such as France and Italy), the rise in temporary employment in Japan further contributes to a perceived job insecurity among workers (Kuroki, 2012). There is a number of studies showing the perils of the "job flexibility". Kachi, Otsuka & Kawada (2014) have equalized nonregular employment with precarious and demonstrated that the involvement of the Japanese middle-aged males into it increases their risk of getting serious psychological distress (SPD). Tsurugano, Inoue & Yano (2012) observed the similar detrimental effects of involvement into full-time jobs under nonregular employment.

Whereas the impact of shareholder-oriented policies has proven detrimental for blue-collar-workers' remuneration, its relation to the growing number of nonregular workers in Japan has not been highlighted sufficiently in the existent literature. The most likely reason for that is the limited data on nonregular employees in major financial databases (Lechevalier, Dossougoin, Hurlin & Takaoka, 2014, p. 19). Differently from the established link between shareholder-oriented policies and reduced labor costs irrespective of the institutional context, this research argues for the following. The diminishing bargaining power of Japanese labor displays itself not only as contracting labor costs, but also as a creation of two distinct labor camps of regular and nonregular employees. While I mostly concentrate on the issue of labor stability, I also touch upon the wage policies as a part of the discussion on financialization. Here, I follow the statement of Lechevalier (2016, p. 63) who considers the separate treatment of these two problems in most of the literature as a drawback.

From the political economic perspective, the labor bifurcation in Japan is caused not by shareholders' pressure exclusively, but also by politics, according to which "public action is oriented towards the satisfaction of demands coming from the most politically powerful groups" (Amable, 2016, p. 93). Palier & Thelen (2010, p. 121) come up with a related explanation that "emphasizes… the political-coalitional underpinnings that drive political outcomes in France and Germany, including under governments of different stripes". Hence, within the context of coordinated market economies, the nexus between management and regular employees often acts as a powerful institutional impediment to a full-fledged labor deregulation desired by shareholders. On the other hand, however, it reinforces more pronounced bifurcation between core and nonregular employees, thereby undermining industry-based labor movements.

The related stream of scholarship pays attention to the inequalities occurring within companies. Dore (2007), Jackson (2007) and Miura (2008) provide an evidence of the growing intra-firm disparities, whereby directors' bonuses and shareholders' dividends rise exponentially compared to salaries of regular employees. I follow their line of argument in the Chapter 6 by showing that the same tendency holds true for the period between 2010 and 2017. Kubo (2014) concentrates at the role of outside shareholders in the process of Japan's financialization. He points that, in theory, the ongoing changes in Company Law make it easier for institutional investors to acquire shares at Japanese companies. On the other hand, the author notes that the low actual M&A rates among Japanese companies are due to entrenched rights of employees (Kubo, 2014). Kubo & Saito (2009) also note that

contrary to the M&As in the U.K. and in Western Europe leading to significant layoffs, Japan's M&As are instrumental for avoiding the dismissals of core employees and even lead to their higher remuneration. The authors, however, do not specify that, although the interests of regular employees are relatively well protected during restructurings, this is only possible due to the existence of nonregular employees serving as long-term buffers.

Argument (Figure 1): Japan's corporate governance reforms have increasingly promoted shareholder-oriented discourse and contributed to the process of corporate financialization, manifested in the intensified shareholder value pursuit. While the reforms have originally aimed at delivering higher returns to shareholders, the rewards to investors have been also accompanied by stagnant salaries for ordinary workers.

In addition to the growing wage gap between managers and workers, the increased shareholder value returns have been achieved at the expense of the growing labor bifurcation, whereby the share of nonregular employees has drastically increased. The increase of the proportion of temporary workers has been a negative externality of the sociopolitical coalition that has been strengthening since early 2000s. This coalition is composed of the government, management and core employees, as well as foreign shareholders. The cross-class alliances between these actors contributed to deeper divisions within the Japanese labor market.

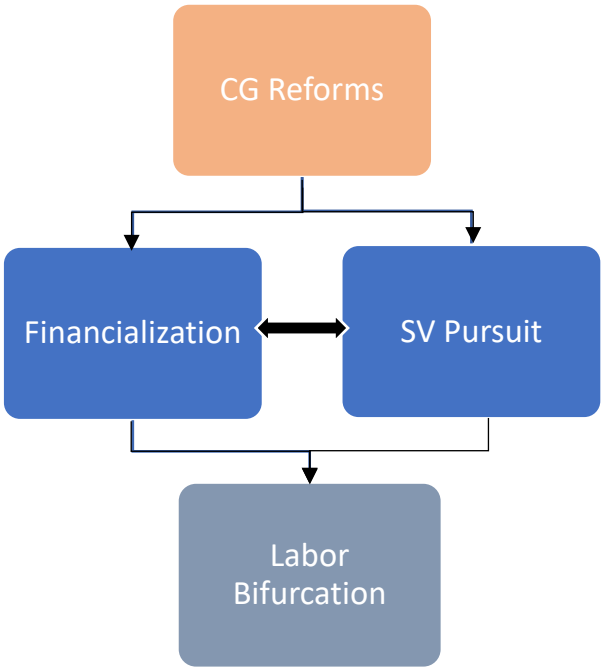

***Figure 1**. Scheme of the Argument*

Theoretical framework. The major theory used to analyze the link between Japan's corporate governance and labor policies is Varieties of Capitalism (VoC). VoC is a political economic theory "that regards companies as the crucial actors in a capitalist economy" (Hall & Soskice, 2001, p. 6). Whereas neoclassical economists mostly perceive firm's aim as maximization of its share value, VoC scholars alter this position. In addition to shareholder scheme, there is a different model of corporate governance called *stakeholder model* that regards the interests of employees, suppliers and customers as vital as the ones of shareholders (Vitols, 2001). The Japanese corporate model belongs to the stakeholder type, however currently adopting some elements of shareholder model (Jackson, 2005). Hall & Soskice (2001) build their typologies of capitalism based on *institutional complementarities*. Their distinction between liberal market economies (LMEs) such as the U.S. and the U.K. and coordinated market economies (CMEs) such as Germany and Japan, results from postulating the respective complementarities between profit-oriented finance and individually acquired skills for LMEs on one hand, and, between committed finance and firm-specific skills for CMEs on the other. According to the authors, "two institutions can be said to be complementary if the presence (or efficiency) of one increases the returns from (or efficiency of) the other" (Hall & Soskice, 2001, p. 17).

The VoC framework is suited for institutional analysis of corporate governance reforms. It is rooted in historical patterns of local capitalist development, and, hence, provides more versatile criteria for defining the success or failure of reforms, as compared to the neoclassical approach. By placing the firm in the center of its analysis, the VoC builds "bridges between business studies and comparative political economy, two disciplines that are all too often disconnected" (Hall & Soskice, 2001, p. 5). Contrary to the VoC, the mainstream economics are preoccupied with the "agency theory", whereby managers are merely shareholders' agents. In this case, the interests of stakeholders other than shareholders are not taken into account. Since Japanese companies have traditionally respected the interests of their stakeholders, particularly employees, it not enough to confine the criteria of their profitability with shareholder value returns. Based on this, I consider the VoC approach more suitable than the neoclassical in respect to the researched case.

At the same time, Japan's ongoing corporate governance reforms pose a challenge to scholars applying the VoC theoretical framework. While operating with dichotomies, it is often not sufficient for capturing institutional change (Deeg & Jackson, 2006, p. 150).

The latter can well lead to hybridization and subsequent blurring of coherences that constitute certain types of capitalist economies (Vitols, 2004). However, differently from early VoC that would view the implementation of alien institutional features as a distortion of a given institutional setting, more recent "institutional complementarity" scholarship provides a detailed account of the types of institutional coexistence that might also be beneficial despite their heterogeneity (Crouch et al., 2005; Witt & Jackson, 2016). There exists a clear research gap in addressing the issue of institutional change for Japan's corporate governance. Therefore, following methodological recommendations of Jackson (2016), current study aims to approach Japan's corporate governance from a less deterministic view of early VoC, but from the political economic perspective that considers institutions primarily as projects aimed at power accumulation (Amable, 2016, p. 93). This approach is close to the one called "actor-centered institutionalism" applied by Aguilera & Jackson (2003, p. 448). Aguilera & Jackson (2003) present a company as a coalition between management, labor and capital. Although the state is not explicitly mentioned in the model, according to the authors, it is present "at the institutional level, by virtue of asserting public interest agendas and mediating conflicts among stakeholders" (Aguilera & Jackson, 2003, p. 450).

The "institutional complementarity" theory is an essential extension of VoC that looks at institutional mechanisms constituting coordinated or liberal market economies. "It suggests that nations with a particular type of coordination in one sphere of the economy should tend to develop complementary practices in other spheres as well" (Hall & Soskice, 2001, p. 18). The relevance of "institutional complementarity" for this research is based on its capacity to capture the links between aspects of a firm that are usually viewed separately from each other. For example, it is famous for pointing at nexuses between debt finance and long-term employment on one hand, and equity finance and high labor turnover on the other (Hall & Soskice, 2001). This theory was coined by Aoki (1994) and further developed by Aguilera & Jackson (2003), Crouch et al. (2005), Höpner (2005), Jacoby (2005), Abe & Hoshi (2007), Amable et al. (2005), Amable (2016). The original concept of Aoki (1994) was based on his observation of Japanese economy in the postwar period, successfully sustained through an institutional fit between lifetime employment, coalition-like relations of labor and management and patient capital provided by partner-banks. The detailed account of finance-management and labor-management complementarities or compromises at Japanese enterprise by the Régulation school (Yamada, 2002; Boyer, 2005) is also built upon the arguments of institutional complementarity (Amable, 2016, p. 82).

The latter is generally conceptualized in terms of a link between capital-labor relations and forms of market competition (Boyer, 2005).

Methodology. The research employs mixed methods. Quantitative method of analysis is based on the data provided by the Nikkei NEEDS FinancialQUEST database, as well as the yearly securities reports produced by Nikkei Index 400 companies. The panel data analysis was preceded by the data gathering and data preparation. I used R software (R Core Team, 2017) that includes various statistical packages to analyze and visualize the data.

Nikkei Index 400 was envisaged by the 2013 (revised in 2014) Japan Revitalization Strategy (JRS) formulated by the Japanese government. Its introduction in 2014 has been expected to foster the alignment of shareholders' and managers' interests. The constituencies of the newly created index are companies that succeeded in enhancing their shareholder value through introduction of outside directors (Miyajima & Nitta, 2014). JPX-Nikkei 400 index is composed of "companies with high appeal for investors, which meet the requirement of global investment standards, such as the efficient use of capital and investor-focused management perspectives" (JCGC, 2015, p. 2).

Qualitative method of analysis of the Japan's political economic strategy aimed at pursuing corporate governance reforms is based on the texts of Japanese corporate governance legislations from the 2002 Commercial Code reform till the 2015 Japan's Corporate Governance Code, Japan's Revitalization Strategy (2013-2016), Keidanren (Japan Business Federation) documents, Keizai Dōyukai (Japan Association of Corporate Executives) and Japan Association of Corporate Directors (JACD / 日本取締役協会) discussion papers. The analysis of labor policies is based on such primary sources as: Labor Standards Act (労働基準法 – amended in 2012), Worker Dispatch Act (労働者派遣法 – amended in 2015), Ministry of Health, Labour, and Welfare (Kōsei-rōdō-shō) as well as Ministry of Economy, Trade and Industry (Keizai-sangyō-shō) papers, Japan Institute for Labour Policy and Training (JILPT / 労働政策研究・研修機構) and Japanese Trade Union Confederation (Rengō) reports. Furthermore, this research relies on OECD, ILO World Bank and IMF documents that frame international corporate governance and labor regulations.

Outline of the dissertation. I start the next chapter with the discussion of the main theories applied in this research. I discuss the major theory used in the dissertation, which is the Varieties of Capitalism. Then I explain the pitfalls of this theory when applied to the analyzed case and argue for the merits of using the Regulation school theory and the institutional theory.

The dissertation proceeds with the literature review on Japan's corporate governance reforms and their effects. Among the impacts, I pay the particular attention to the intensified labor bifurcation between regular and nonregular employees. In addition, I analyze the existing scholarship highlighting the link between the shareholder value pursuit as one of the effects of corporate governance reforms, and the labor bifurcation.

The following chapter 3 provides a background to the institutional changes within Japanese corporate milieu. It describes institutional *nexuses* (using the terminology of Regulation school) in Japan's postwar political economy. It argues that the "companyist compromise" framework that was used to describe the Japanese economy from the 1960s till 1980s has undergone substantial changes. These changes were brought by the bubble burst that occurred in the early 1990s. The resulted economic crisis raised the question about management and financial reforms as key to macroeconomic recovery. Due to institutional complementarities existing between different domains of Japan's corporate governance, changes in corporate finance have triggered the shifts in managerial and human resource fields. The resulting corporate governance reforms reflected the attempts to accommodate these systemic changes.

Chapter 4 analyzes the series of corporate governance reforms from the 2002 Commercial Code amendment to the 2015 adoption of the Corporate Governance Code. It intends to resolve the seeming contradiction between the formally weak pace of the reforms' implementation on one hand, and the entrenchment of the pro-reform discourse on the other. The epitome of this discourse has been the general agreement on the need to enhance the shareholders' rights. The reason for that is the increasing activity of outside institutional investors, especially foreigners, that claim monitoring credentials proportional to the shares in their investee companies. As providers of the capital, they are also viewed as mediums of Japanese companies' reorientation from the relational bank-based finance to the arm's-length market-based finance[3].

[3] In this chapter, I include the parts from my published article (Ovsiannikov, 2017) without citing it each time.

Chapter 5 proceeds with the analysis of the intensified labor bifurcation at Japanese joint-stock companies. It moves from the discussion of nexuses to the discussion of institutional *hierarchies*. This chapter discusses the issue of hierarchy in regard to the phenomenon of labor bifurcation. It argues that the gap between regular and nonregular employees can be attributed to the modified sociopolitical coalition, whereby financially-oriented (mostly foreign) shareholders have gained more political power to advance their agenda. In this respect, corporate governance reforms promoted by the government, pushed managers to achieve higher shareholder value returns, often at the expense of employees, above all – nonregulars. This has been possible due to low unionization rates of temporary employees. Although, during the recent couple of years, the wage and the unionizations gaps between core and flexible employees have somehow narrowed, the labor bifurcation remains a significant social and economic problem for Japan. The altered relationship between directors, management and employees no longer fits into the cooperative postwar framework. In other words, although stakeholder foundations of a Japanese firm are still intact, its bifurcated labor tells that the "companyist compromise" has been breached. Hence, tackling the issue of labor bifurcation is likely to contribute to Japan's sustainable recovery.

Chapter 6 investigates the externalities of the shareholder-oriented policies that are increasingly pursued by Japanese joint-stock companies. In particular, it argues that Japan's corporate governance reforms have resulted in the expanded levels of financialization. Financialization is understood here as an increased priority given to the stock market evaluation as well as higher profits to shareholders compared to the benefits allocated to other stakeholders. Japanese corporate governance model has been traditionally described as a "stakeholder model" that considers returns to employees, customers and suppliers at least as important as returns to shareholders. Hence, the financialization process at Japanese companies significantly altered the institutional foundations of the local stakeholder model. The special attention given to shareholders has led to wider wage gaps between white- and blue-collar workers, having also contributed to labor bifurcation between regular and nonregular employees. The panel data analysis adds further credence to this claim[4].

The last chapter presents the conclusions.

[4] This chapter is based on the article by Ovsiannikov (2018).

Chapter 2: Literature Review

This chapter presents a literature review of the main theories employed in this dissertation. It concentrates on the Varieties of Capitalism (VoC), Regulation theory and institutional theory. It proceeds with the review of the literature on the two major topics of this research, which are: corporate governance reforms and labor bifurcation. Lastly, it concentrates on the previous scholarship that encompasses these two aspects.

2.1. Varieties of Capitalism (VoC)

VoC is notable for its focus on institutions influenced by national political economies (Hodgson, 1996, p. 400). Unlike the uniform neoclassical approach, VoC singles out different regimes of capital accumulation (Ebbinghaus & Manow, 2001). There are two main types of capitalist economies: liberal market economies (LME) (e.g. U.S., U.K., Canada, Australia) and coordinated market economies (CME) (e.g., Germany, Japan, Sweden, Austria) (Hall & Soskice, 2001). Japan, which belongs to the latter group, is the focus of this research.

Within a CME framework Japan is linked in a stylized way to Germany, being contrasted to the LMEs such as the U.S. and the U.K. "Japan and Germany are societies where classical market contracts are replaced by long-term commitments: transactions are coordinated by relational banking and trading, relational employment, and relational regulation by government resulting in a specific mix of competition and cooperation" (Groenewegen, 2001, p. 1056). On the other hand, LMEs are characterized by arm's-length transactions and more short-term commitments motivated by competitive concerns. One should admit that such "varieties" are quite abstract types used for classification, whereas empirical models vary from country to country (Ahlering & Deakin, 2007, p. 877). In the case of Japan, the CMEs' derivatives are classified as "Asian capitalism" (Singh, 2002) or "welfare capitalism" (Dore, 2000). Furthermore, there is an internal variety between large Japanese companies embedded into financial and subcontractors' networks called *keiretsu* on one hand, and SMEs on the other.

Despite the abovementioned degree of abstraction, VoC has an advantage of explaining institutional coherences between different elements of national economies. For example, in the corporate sphere, bank-centered finance is compatible with lower employees' turnover, whereas the opposite holds true for companies relying on equity funding (Höpner, 2005). The former type of relational transactions is peculiar to CMEs and

is conceptualized as a “stakeholder model”, whereas the latter, inherent to LMEs, is called a “shareholder model”. While this research operates with such dichotomy, it follows the VoC argument that change in one domain of corporate governance is likely to trigger transformations in others as well. Moreover, the competitive rationale of introducing novel elements to a national economy is likely to be counterbalanced by the existing institutional legacy. This consideration is important when analyzing cases such as adoption of LME-originated corporate governance reforms by CMEs.

Of relevance to this research from the VoC point is the “*institutional complementarity*” concept. Aoki (1994) developed it based on the example of Japan. The essence of the observation is that, differently from market-based corporate finance complemented by high labor turnover in the West, Japanese companies achieved high level of productivity in the postwar period due to complementarity between the main bank system, the imperfect labor market and the team-oriented production (Aoki, 1994, p. 658). This encapsulates two corporate aspects: finance and labor. On a finance side, main bank plays a role of not only a capital lender, but also of an information provider and a last-resort rescuer in case of company’s financial distress (Aoki, 1994b, p. 21). The task of long-term corporate growth and, ultimately, survival, is further substantiated by high levels of cross-shareholdings, which enhances equity value and provides leverages against hostile takeovers (Aoki, 1994b). On a labor side, employee-management relations are also driven by strategic rather than short-term interests. In particular, enterprise unions enhance cooperative rather contested relationship between management and labor, which allows both parties to prioritize corporate growth rather than to argue for a pursuit of a higher value added or increased labor costs respectively (Aoki, 1994b, p. 29).

According to institutional complementarity argument, for Japan, coherences between financial and labor policies along the line of a coordinated market economy contribute to a national competitive advantage. Following this logic, if any of these elements drifts toward the LME, this would undermine country’s institutional foundations. Thus, the VoC does not pay enough attention to institutional change exemplified by introduction of LME elements into CME environment. The critique of VoC is motivated by the lack of consideration regarding the possibility of beneficial complementarities between two capitalist systems. While the early VoC framework is suitable for explaining institutional path-dependency, its weakness lies in the limited capacity to capture institutional change (Amable, 2016, Poon & Ng, 2017). Because of globalization and intensified competition, firms are inevitably subjected to influence from imported parts.

"This may explain why, in reality, some degree of change is possible without endangering the system of existing "positive", system-reinforcing, complementarities" (Amable, 2016, p. 89).

The only "acceptable" change from the institutional complementarity point is the systemic one, i.e., the departure from the CME to the LME or vice versa (Amable, 2016). However, successful changes that go against conventional understanding of institutional complementariness are not explained by this theory. While early VoC scholarship related comparative institutional advantage to coherency between institutions (for LMEs, transactions should be arm's-length, for CMEs – relational), more up-to-date findings prove the possibilities of beneficial complementizes between elements of LMEs and CMEs (Witt & Jackson, 2016).

2.2. Regulation Theory

The Regulation school offers a less static analysis of institutions by focusing on interactions between actors of a capitalist economy. It is also different from the semantically related neoclassical concept of "regulation" that operates with an ideal equilibrium model. The latter "is the exact opposite of French and European *régulation* theory, which deals with the dynamics of an economy with a wealth of institutions and organisations that do indeed interact through markets, but which are by no means limited to this type of interaction" (Boyer & Saillard, 2012, p. 4). Hence, instead of neoclassical equilibria, regulation school operates with "dynamic processes", instead of determined influence of international regimes on national economy – with "institutional arrangements" and, instead of a rational "homo economicus" – with "situated rationality" (Boyer & Saillard, 2002, pp. 40-41).

From the Regulation school perspective, firms are embedded both into global and national regimes of accumulation, which makes their operations dependent upon these changing broader frameworks. Thus, the first (1) nexus is the interaction between corporate human resource management (HRM) and market called "companyist compromise", and the second (2) is corporate inclusion into the hierarchy of existing institutions that is influenced by a composition of a current sociopolitical bloc (Boyer, 2007, p. 4).

Regarding the first aspect, although companyist compromise describes the management-labor and management-finance relations in the period of Japan's economic heyday – from 1960s till 1980s – its application can come useful while analyzing the "post-

companyist" institutional environment from early 1990s until nowadays. Except Lechevalier (2014, 2016) and Yamada & Hirano (2015), no other authors has addressed the phenomenon of post-companyism in Japan. As regards second aspect, Regulation school focuses on the relations between a corporation and a state and therefore shares the concerns of the political economic approach. This approach defines institutions as "political compromises among different interest groups that form sociopolitical coalitions to advance their interests" (Aguilera & Jackson, 2003). Lechevalier, Debanes & Shin (2016), Yamada & Hirano (2015) and Jackson (2016) have demonstrated the merits of using this analytical tool for addressing the issue of institutional change in Japan. This study intends to follow their arguments while answering the question of Japan's corporate governance reforms' effects.

2.3. Institutional Theory

While VoC and the Regulation theory are concerned with answering the question "how" institutions complement each other, institutional theory answers the question "why" complementarities emerge. VoC argues that institutional complementarities are formed because of deliberate engineering along the lines of "coordinated" or "liberal" coherences. However, "if the changes in subsystems occur or are imposed from outside, the result may be unintended change in other, interrelated, spheres of political economy" (Höpner, 2005, p. 334). Hence, the source of change might not necessarily be internal, but also, possibly, drawn from external experience, particularly in situations of internal crises. In the attempts to conceptualize institutional change driven by concerns of legitimacy rather than economic benefits, Meyer & Rowan (1977) and DiMaggio & Powel (1983) came up with an important concept of "institutional isomorphism".

According to Meyer & Rowan (1977, p. 343), "many of the positions, policies, programs, and procedures of modern organizations are enforced by public opinion, by the views of important constituents, by knowledge legitimated through the educational system, by social prestige, by the laws, and by the definitions of negligence and prudence used by the courts. Such elements of formal structure are manifestations of powerful institutional rules which function as highly rationalized myths that are binding on particular organizations". Here, the authors draw an important distinction between *institutional isomorphism* aimed at attaining ceremonial goals for the sake of public approval, and *competitive isomorphism* leading to output controls and subsequent convergence (Meyer &

Rowan, 1977, p. 354; DiMaggio & Powel, 1986, pp. 149-150). Particularly at times of crises, organizational actors seek empowerment by drawing from successful experiences of their counterparts in order to attain legitimacy. By referring to already institutionally established practices, they immunize themselves from likely accusations of being ineffective or inefficient (Meyer & Rowan, 1977, p. 361).

Japan can be considered a case where implementation of new business practices draws from disappointment with own system against the background of economic downturn, rather than from a coherent path-dependent logic (Dore, 2007, p. 209). Amid this loss of self-confidence, the promotion of Anglo-Saxon practices appears to be in line with so-called "*institutional isomorphism*" that arises from the will of organizations to compete for institutional legitimacy and political power rather than for an improved performance (DiMaggio & Powell, 1983). While notion of "convergence" points at functional homogeneity that stems from competitive concerns, "isomorphism" describes a uniformity of institutional pressures on organizations, which follows *reputational* logic (Meyer & Rowan, 1977; Beckert, 2010). The avenue for the application of "institutional isomorphism" concept towards modern Japan was set by Jacoby (2005) and recently developed by Nagayoshi, Kawabata & Nakamura (2015) and Jackson (2016). However, there is a clear gap in the studies addressing the dynamics of institutional change in Japan that this research intends to address.

2.4. Corporate Governance Reforms: Shareholders' Rights Enhancement

Overview. On one hand, as Japan's postwar industrial system was centered on large enterprises (Yamada, 2002; Amable, 2016), their departure from relational finance and monitoring towards arm's-length finance starting from 1980s, set a new benchmark for Japan's political economic strategy. On the other, coordinated regulatory framework sustained by Japan's government and central bank in the postwar years has established entrenched institutional criteria for subsequent deregulation. Hence, the state has played an important role in framing the new corporate agenda that has become key to recently-initiated "structural reforms" (Lechevalier, Debanes & Shin, 2016). As Japan's economy experienced low growth during the post-bubble period of 1990s, politicians, business groups as well as the Ministry of Economy, Trade and Industry (METI) envisaged corporate governance reforms as an insurance against possible failure of fiscal and monetary policies (Gilson & Milhaupt, 2004, p. 14). According to the governmental agenda,

Japan's corporate governance reforms that started from the 2002 Commercial Code amendment, have aimed to "reform corporate managers' mindset" (Japan Revitalization Strategy, 2014, p. 5) by inculcating a proactive attitude and compliance with market-based accounting standards. This should, in turn, lead to the enhanced international competitiveness, more efficient usage of shareholders' equity and increased levels of investment and M&As (Japan Revitalization Strategy, 2014).

Japanese companies faced major internal and external problems in early 1990s. Firstly, they accumulated large amounts of debt from partner banks and needed to repay it due to the decay of the main bank system (Keizai Doyukai, 2009). To do so, they needed proper monitoring over investment activities that required paying closer attention to market peculiarities (Shishido, 2001). Secondly, enterprises faced increased international competition, especially from China and South Korea, and, hence, needed to optimize their accounting systems. Growing reliance on outsider shareholders has been regarded as a mean to solve these two issues. However, favor comes at a price: outside shareholders invest in companies for pragmatic reasons, claiming financial gains in return for their capital. This mercantile exchange is very different from the postwar main bank system that was based on trust and long-term obligations which were uneasy to quantify. In view on this, Japan's corporate governance reforms have been designed as a platform for managers and increasingly influential shareholders to find a tradeoff between corporate profitability and respect towards institutional legacy of Japanese companies.

The very fact of outsider shareholders' strengthening led to automatic selection of "good companies and bad companies" by the capital market (Shishido, 2001, p. 670). The substantial lowering of litigation fee for shareholders in 1993 was the first step in a long series of legal concessions to outsider investors. Subsequently, shareholders started to exercise monitoring rights by exit or by voice (Shishido, 2001). By now, this was the last "policy pushed action" in the row of subsequent corporate governance reforms (Shishido, 2001, p. 672, Gilson & Milhaupt, 2004, p. 13). Differently from the international experience of market-oriented corporate reforms (e.g., in post-Soviet states or in South Korea), Japan chose an enabling or "demand-pulled" strategy for the firms to incrementally adopt their institutions to shareholders' demands (Gilson & Milhaupt, 2004). "In general, the choice may be part of a signaling strategy, allowing the corporation to credibly inform outsiders of its future plans" (Gilson & Milhaupt, 2004, p. 3). Although the trajectory of corporate governance reforms in Japan has been moving towards a stricter enforcement of shareholder-oriented strategy, the soft "comply or explain" principle (TSE, 2004) has

remained relevant until today. Policymakers have acknowledged the yet-unresolved conflict between path-dependent Japan's institutions that rely on long-term commitments and relational networks, and the growing role of market finance that implies arm's-length monitoring (Yoshikawa, Tsui-Auch & McGuire, 2007).

The next step in corporate governance deregulation was the introduction of stock options in 1997, whereby directors were allowed to hold shares of their companies, thus allying themselves with investors. In the same year, the 1947 Antimonopoly Law was revised by lifting a ban on holding companies, thus opening a way to creating subsidiaries wholly owned and governed by parent entities. Furthermore, the 1997 is known for the start of a board reform which essence has been the reduction of board members and clearer separation between execution and monitoring. The executive officer system (*shikkō-yakuin sei*) was introduced as an institute called to effectively represent numerous sectional managers that previously had seats on a board (Miyamoto, 2017, p. 8). It was pioneered by Sony in 1997 and was followed by numerous listed companies.

The year of 2002 was notable for the Commercial Code reform that provided listed companies with an opportunity of choosing an alternative U.S.-style model with committees constituted of outsiders' majority. At the same time, the companies were provided with an opportunity to retain an old relational monitoring system. Its main characteristic is a supervision by a so-called "statutory auditor" or *kansayaku* that carries an advisory function, not being a member of the board. In 2005, as a part of the enabling strategy, the Companies Act amendment introduced a compulsory demand about the majority of outsides at the board of audit (a former "statutory auditor") (Gilson & Milhaupt, 2004, p. 8). Thereby the legislators acknowledged the possibility of carrying out corporate governance reforms within existing institutional tracks.

Due to a general unwillingness of listed companies to adopt a U.S-style "three-committee" system, in 2014, the new softer system of "companies with an audit committee" was introduced. "This system is expected to adopt a position midway between the system that uses a board of company auditors and the three-committee system" (Ueda, 2016, p. 20). It provided a legal mechanism for outside auditors to become members of the board, leaving at the same the issues of nomination and remuneration to the discretion of insider-promoted directors. Lastly, the 2015 Corporate Governance Code mandated the appointment of at least two independent outside directors. Although those directors do not have to constitute board's majority, as in case of Anglo-Saxon system, the increasing number of companies with independent directors – 97.2 percent in 2018 as opposed to 31.6

percent in 2010 (JACD, 2016, p. 4; TSE, 2018) – demonstrates incremental institutional change taking place within Japanese corporate environment.

Despite the legally declared aim to enhance transparent outside monitoring (Japan's Corporate Governance Code, 2015, p. 3), from 2003 – the year of Commercial Code reform coming to effect – until 2018, the number of companies that applied US-style committee system only increased from 44 to 72 (JACD, 2017; TSE, 2018), constituting only two percent of all listed firms. Most of the reformist companies (62) belong to the Tokyo Stock Exchange (TSE) 1st section (comprising large companies), constituting however only three percent of it. In general, the US-based model was applied in a highly selective way, with stock prices not being significantly affected by the committees' introduction (Gilson & Milhaupt, 2004). Companies have clearly opted to remain within the terrains of the old "statutory auditors / audit & supervisory board" (*kansayaku*) system, which limited outsiders' direct interference with corporate control. The idea about a virtually absent market for corporate control in Japan is supported by the evidence of insider-dominated boards of directors. Hence, even the largest outsider investors cannot fully exercise their voting rights in the boardroom (Aguilera & Jackson, 2003, p. 453).

At the same time, it cannot be said that corporate governance reforms did not yield any results. Amid the skepticism regarding the necessity to introduce outsiders to the board, companies have become much more aware about the need to meet shareholders' claims. In turn, foreign institutional investors seem to have embraced the concept of stakeholder value pertinent to Japanese companies. The currently evolving tradeoff between conservative management and financially oriented investors has been formed around recently promulgated Corporate Governance Code (2015) and Stewardship Code (2014).

While institutional investors take formal steps to acknowledge Japan's stakeholder model, local managers' mindsets shift toward favoring shareholders. Against the background of increasing reputational pressure from outside investors, CEOs of listed companies have become overwhelmingly preoccupied with corporate share value, which provides evidence of "intensification of market discipline" (Roberts, 2001). Under conditions of market authority becoming ever more apparent, even those managers (executive directors) less eager to implement corporate governance reforms have been associating their own performance with share value (Jacoby, 2005, p. 61; Yamada & Hirano, 2015, p. 9). At the same time, the higher share value does not automatically lead to higher long-term profitability. In fact, the excessive attention to market evaluation can lead to social externalities from the stakeholder point of view (Darcillon, 2015). Hence, this

research aims to conceptualize the contested effects of Japan's corporate governance reforms.

1) *Aims*. Most of the existing scholarship concurs with the official objective of corporate governance reforms. Firstly, the reforms aim to tackle current demographic challenges within the Japanese society, such as ageing and decline of the working population. To alleviate these, firms need to improve their profitability and productivity (JRS, 2014, p. 5; Mihaupt, 2017, p. 3). Secondly, amid the shrinking domestic market, corporate governance reforms should enhance international competitiveness of Japanese companies and encourage more risk-taking attitude among managers (JRS, 2014, p. 5). Risk-taking means more investment as opposed to cash-hoarding – the aspect also underlined by the IMF (Aoyagi & Ganelli, 2014). Likewise, according to the OECD principles, the reforms should prompt "companies with high cash holdings to find ways to proactively use their retained earnings for new capital investment" (OECD, 2015, p. 2).

Some authors hold an opinion that the reforms' rationale is to enhance arm's-length control over executive mangers to eventually converge with shareholder-oriented corporate governance model (Komiyama & Masaoka, 2002). Senechal (2003) argues that the nonseparation of executive and monitoring functions of directors at Japanese firms is a deficiency: "Whereas American corporations rely on a clear separation of board and executive officer functions, Japanese firms combine the two and concentrate decision-making power in the hands of a representative director" (p. 544). This phenomenon occurs because directors of Japanese companies are mostly promoted from within and are therefore foremost loyal to their corporate heirs while arguably underestimating the interests of outsiders. IMF also sets an example of developed western countries for Japan to encourage more outsiders, women and foreigners to be present on boards, to lift the restrictions for M&A activities and to pressure managers to act in shareholders' interests. (Aoyagi & Ganelli, 2014).

Itami (2005, p. 9), mentions that the true purpose of the ongoing transformations is "to establish a vigilant watch on corporate management", which is not a mean to promote shareholder value but rather the goal in itself. While in the postwar period the monitoring function was carried by banks, by 1990s their supervision substantially weakened due to unwinding of corporate-financial partnerships. As companies are increasingly relying on outside shareholding, corporate management needs to pay closer attention to market. Hence, outside directors can potentially serve as market mediums and whistleblowers for CEOs

from the perspective of agency theory. “Every Japanese company... has its own, strong, self-replicating corporate culture based on insiders, often with ambiguous or weak internal checks and balances. Reform is needed because corporate management is entrenched, autonomous, and powerful” (Patrick, 2016, p. 15).

In addition to economic reasons for implementing reforms, Japanese companies strive to formally adhere to Anglo-Saxon rules in their attempts to regain legitimacy as their finance changes from bank-based to equity-based (Yoshikawa & Phan, 2001). This is an explanation given by the institutional theory. It “rejects rational choice as the motivator of firm behaviors but instead puts a greater emphasis on the *appearance* of rationality as a path to legitimacy” (Yoshikawa & Phan, 2001, p. 188). From this perspective, the declared commitments to enhance shareholder value might not be economically viable but can legitimize corporate governance in the eyes of potential investors.

There exists another rather unconventional view on the aims of the corporate governance reforms in Japan which also operates with institutional theory. Milhaupt & Pistor (2008) assert that the adoption of the US-originated norms of corporate law like Delaware takeover jurisprudence have served as a tool of institutional reinforcement. For example, the lifting of ban on holding companies in 1997 can enable subsidiary companies to have formally outside directors on their boards who, at the same time, can be employees of a parent company (Shishido, 2007, p. 317). Moreover, the formal presence of outside directors on boards of Japanese companies is likely to help in fighting off possible litigations from hostile bidders, to prevent infamous cases of Livedoor (2005), Oji Paper (2006) and Steel Partners (2007) (Miyajima, Hoda & Ogawa, 2016, p. 7).

2) *Results*. On one hand, statistically, only two percent of Japan’s listed companies adopted a U.S.-based committee system that requires the presence of a majority of outside directors at corporate board (TSE, 2018). On the other hand, 97 percent of listed companies nowadays have at least one outside director, which is a significant reformist development compared with 31.6 percent in 2010 (JACD, 2016; TSE, 2018). So, have the reforms succeeded? The authors applying the “agency theory” mostly give a negative answer. Granting the difference between Japan’s stakeholder model and shareholder-oriented reforms, they regard Japanese institutions as merely costs for implementing effective international practices (Demirbag, Glaister & Tatoglu, 2007; Slangen & Beugelsdijk, 2010). Hence, they view fragmentary and slow implementation of shareholder-oriented reforms as an unaddressed “agency problem”, whereby stockholders incur losses caused by

managerial underestimation of shareholder value. This corresponds to a "thin" understanding of institutions as constrains to business decisions (Jackson & Deeg, 2008, p. 542).

There is, however, another group of scholars who take institutions more seriously. This view fits with the VoC, which framework operates with a "thick" notion of institutions in a sense that they fundamentally matter as resources that "determine actors' strategies, but can also be the object of such action" (Deeg & Jackson, 2007, p. 159). From this point of view, the process of corporate governance reforms in Japan is a case of incremental institutional change. The retention of control by insiders "was neither a delay nor an insufficiency in corporate governance reform because Japanese firms intrinsically did not intend to become more like their US counterparts" (Miyamoto, 2017, p. 9). Thus, the board reform, whereby the number of directors decreased, and the proportion of outside supervisors increased, is an evidence of a substantial institutional development.

Although major industrial associations such as Keidanren and Japan Association of Corporate Executives (*Keizai Doyukai*) initially opposed the delegation of power from managers to shareholders (Jackson & Miyajima, 2007, p. 16) they eventually realized the irreversibility of reforms and chose to follow the strategy "if you can't beat them, lead them" (Rear, 2016). Given this conservative resistance, the reforms focused on the improvement of statutory auditors' independence and motivating managers to take more efficient and unorthodox decisions (Jackson & Miyajima, 2007).

While it can be said that the corporate governance reforms improved monitoring of Japanese management, there is no solid evidence suggesting that these changes enhanced corporate profitability and productivity (Chizema & Shinozawa, 2012). Even more so, Dore (2000) holds an opinion that "Anglo-Saxon" corporate governance reforms have been carried out in Japan because of superficial admiration with the "shareholder model" (p. 53). Had it been contrasted to Japan's postwar "employee-sovereign" model, stresses Dore (2000, p. 53), structural reforms would not have concentrated on corporate governance.

3) *Effects*. Jacoby (2005, p. 16) argues that the choice of a dominant model is often shaped by admiration of a present-day economic success that might well be transient. Moreover, in Japan, instead of a stylized homogeneity possibly converging towards a dominant model, one rather sees at least two different institutional setups for large export-oriented enterprises and SMEs (Jacoby, 2005). Miyajima (1998) as well as Ahmadjian & Robbins (2005) also present arguments against convergence theory, suggesting that despite

the irreversible character of corporate deregulation, an emerging market-based discipline will be affected by the legacy of the Japanese stakeholder model. This view stresses the necessity of institutional transformations for the legal changes to take place.

The increasing role of foreign investors that acquired large portions of Japanese companies' devaluated stock during 1990s led to growing awareness about shareholders' interests in running a company (Ahmadjian, 2007, p. 145). The rise of equity finance compared to debt finance for large companies has pressed management to pay more attention to relatively short-term profitability rather than to long-term growth. According to the "institutional complementarity" hypothesis, bank finance provides patient capital, which exerts less pressure over management, thereby leaving room for strategic planning. Contrary to that, stock finance requires immediate decisions from incumbent managers who can be fired if they fail to meet shareholders' demands. In this case, the so-called whistleblowers for executives are outside supervisory directors that embody shareholders' arm's-length control.

The Japanese corporate governance has been traditionally characterized by the minimal influence of outside directors. In other words, Japanese managers have been subject to relational rather than arm's-length control which provided them "with a high degree of insulation from capital market pressures, rewarded them with high levels of job security, and the many benefits of a well paying, secure and high-status position" (Milhaupt, 2017, p. 14). The substantial increase in non-stable shareholding amid the unraveling of cross-shareholding ties (*mochiai*) during 1990s did not translate in what it would seem a logical increase in arm's-length monitors (Dore, 2007, p. 382). This, however, does not mean that Japan's corporate governance reforms pushed by foreign shareholders and governance did not change the way the local companies are being run.

Although the actual proportion of outside directors did not grow, corporate managers have become increasingly aware of the market evaluation of their companies represented by stock indices. Thereby, the new shareholder discourse has become a part of CEOs' consciousness (Ovsiannikov, 2017). Japanese managers have mimicked their counterparts while enhancing a market for corporate control in a reputational race between stock-listed companies. This resonates with one of the objectives of Japan's Corporate Governance Code that calls for "a corporate self-discipline" of managers on their path of becoming "healthy entrepreneurs" (JCGC, 2015, p. 3). Jackson (2016) develops his own findings (2007) and that of Dore (2007) about the growing returns to shareholders by

encouraging to venture into the research linking partial financialization in East Asia with the growing disparities between managers (aligned with shareholders) and employees.

The commitment of large Japanese companies to annually disclose corporate information to the public has been key to the imposition of a market-based regime. This "voluntary" disclosure can be viewed as a substitute to a presence of outside directors on corporate boards. In fact, shareholders' representatives do not have to personally participate in annual general meetings (AGMs) to spot a corporate misconduct. It is usually enough for them to refer to unified accounting reports (Aglietta, 2000, p. 149)[5]. Since modern accounting systems are biased toward the shareholder value creation, managers tend to resort to drastic restructuring to get "right" figures in their annual reports (Roberts, 2001). "The shareholder value discourse in integrally related to the ability of managers to engage in major and rapid organizational restructuring in order to quickly respond to 'poor figures'" (Morgan & Takahashi, 2002, p. 174). The CEOs have also increasingly engaged in a so-called "narrative management", by reaching out to shareholders via PR channels (Yorozu, 2015).

Despite the growing attention to shareholders, Japanese corporate governance is still considered as a case of a "stakeholder model" (Miyamoto, 2017). Japanese companies tend to pursue socially responsible policies in relation to customers, suppliers, wider community and employees (Vitols, 2001). From the Regulation school perspective, the postwar "companyist compromise" is still intact, although in a modified way (Lechevalier, 2013, p. 67). On a labor side, management and employees still engage in cooperative rather than contested relations, which results in the retention of social benefits for core employees and a minimal number of labor strikes.

Some authors describe the resulted combination as a "hybrid" (Yoshikawa, Tsui-Auch & McGuire, 2007) or a "syncretic" (Kushida & Shimizu, 2013) model. The reformist side that argues for the shareholder-oriented reforms are the "foreign investment banks, securities firms, insurers and some new Japanese entrants" and the traditional is represented by regional banks (Kushida & Shimizu, 2013, pp. 339-340). In a more general sense, the ongoing neoliberal reforms are being mediated through a so-called Japanese-style management (*Nihon-teki keiei*) which attributes cultural and socioeconomic importance to lifetime employment (Rear, 2016). Thus, it is not surprising that managers and core

[5] In 2014, the revised Japan Revitalization Strategy issued by the Cabinet Office Since recommended companies listed at Tokyo Stock Exchange to adopt the International Financial Reporting Standards (IFRS).

employees have been resisting the shareholder-oriented policies and labor reform that would put more emphasis on performance rather than seniority (Milhaupt, 2017, p. 14). However, the mindset of Japanese managers has been gradually changing through the so-called "discourse interventions" by such policymakers as *Keidanren* and *Keizai Doyukai* that gradually stressed such institutionally novel categories as "diversity" and "independent-style employee" (Rear, 2016). The changes in labor policy that have been arguably boosted by corporate governance reforms are discussed below.

2.5. Labor Bifurcation

Overview. The argument about labor dualization or bifurcation originates in the scholarship that relies on the VoC. Its essence is the following: differently from the "liberal market economies" such as the U.S. and the U.K. that have deregulated labor arrangements for both regular and nonregular employees, the "coordinated market economies" of continental Europe and Japan have loosened employment conditions for temporary employees, while keeping previous social guarantees for core employees (Watanabe, 2017, p. 3). Rueda (2006) came up with the thesis that divisions between insiders (core employees) and outsiders (flexible employees) are reinforced by social democratic governments that enjoy high levels of support – for example in Scandinavian countries. Thereby, corporations and a state ally with unionized insiders, preventing a potential full-fledged labor movement.

Later, Emmenegger (2009) argued that the insider/outsider theory centered around the claim about the support of insiders by social democratic parties via job security enhancement is empirically inconsistent. Instead, he concludes that "labour market outsiders can be expected to be as supportive of job security regulations and of Social Democratic parties as labour market insiders" (2009, p. 141). Among the main reasons for outsiders' support of job security, Emmenegger (2009) mentions "household relationships, the power balance between capital and labour or the volatility of one's own position in the labour market" (p. 141). Palier & Thelen (2010) also challenged Rueda's argument, but for different reasons. Authors state that "dualist trends are far more pronounced in the continental European countries than in the Nordic countries, where social democratic parties are stronger and in some cases near hegemonic" (Palier & Thelen, 2010, p. 121). Instead of looking for the causes of labor bifurcation among political ideologies of ruling parties, the authors analyze political-economic foundations of coalitions between state,

business and labor, concentrating on "industrial relations changes, labor market policy, and welfare state reforms" in Germany and France (Palier & Thelen, 2010, p. 121). Hassel (2014) observes similar trends developing within the German corporate environment since 1990s, whereby, amid the pertaining protection of core employees, "firms tended to push for these [irregular employment] alternatives as flexibility buffers to protect permanent employment" (pp. 66-67).

Thus, the political-economic approach modifies the original VoC view of the institutional change in a following way. While most of the VoC scholars would argue that strengthening of alliance between policymakers, managers and core employees serves as a socially necessary barrier to neoliberal deregulation, the political-economic approach maintains that "precisely the intensification of cooperation between labor and management in some firms and industries has paradoxically had deeply *destabilizing* collateral effects that have undermined or are undermining these systems as they were traditionally constituted" (Thelen & Kume, 2006, p. 14).

Among the theories that address labor dualization the one called "dual labor market hypothesis" (Doeringer & Piore, 1971) deserves attention. According to this hypothesis, labor market is divided into internal and external niches. The former, in turn, is further subdivided into two tiers, with the first one composed of a highly qualified workforce that enjoys stable employment and high remuneration. The lower tier has skills mostly acquired through on-the-job training, which makes it more dependent upon employers' requirements. This results in lower mobility and compensation for this labor segment. While internal market is characterized with long-term career opportunities, external market is composed of workers that are hardly provided with any training and whose skills are less valued. The workers belonging to this cohort are mainly involved in simple services, manual work and retail. While it can be disputed whether such a segmented market is a structural display of workers' abilities, it certainly serves to employers' purpose: "Employers like to divide the labour market into the internal and external markets, since they want a buffer against the fluctuation and uncertainty of product demand and since they need to restrict the number and power of internal workers in order to suppress wage costs and need to maintain the flexibility of labour management" (Ishikawa, 2002, p. 248).

The dual labor market hypothesis is quite relevant for this research. However, differently from the VoC, it does not account for national institutional differences. While the hypothesis was originally based on the observation of the U.S. labor market in the postwar period, it could also be applied to the Japanese economy before 1970s. During that

time, Japan's dual labor market reflected the differences between large enterprises and SMEs, where the former was mostly composed of internal and the latter – of external workforce (Teruyama & Toda, 2017, p. 2). In other words, dual labor market was a part of an industrial agenda both in the U.S. and in Japan. However, the post-1970 era has marked more pronounced differences between liberal and coordinated market economies. On one hand, in case of the U.S. and the U.K., the gap between internal and external labor market has been increasingly diluted through deregulation of core employment. On the other hand, the economies of continental Europe and Japan have faced sharper distinctions between the two employee categories due to pertaining institutional legacy of core-workers' protection. In view of this, the recent developments influenced by the encroachment of neoliberalism show that employers' reasoning goes far beyond the claims of neoclassical "rationality" that should be ultimately concerned with employees' welfare. The dual labor market hypothesis shares this assumption. These days, however, the view of a company as an utmost source of profits for its shareholders has become rooted within both liberal and coordinated market economies. But importantly, the way the shareholder ideology fares, depends on local institutions. VoC is designed to explain these differences.

Japan's case. In Japan, like in other coordinated market economies, the labor deregulation has mostly targeted nonregular employees, while the core employees have retained their social guarantees. Although the link between their remuneration and seniority (the so-called "seniority wage system") weakens, regular workers are still mostly well-protected against layoffs. At the same time, there is a growing institutional divide between larger firms that remain devoted to core employees, and SMEs, where both regular and nonregular workers are subject to deregulation, against the logic of the "coordinated" legacy. "An emerging important new divide among core firms in the Japanese economy is between stronger firms (such as Toyota) which have been careful to preserve some of the essential strengths of the traditional system by intensifying their relationship with core workers (even as they may adopt more flexible wage systems), and weaker firms which have moved away from traditional practices (including laying off workers) in a straightforward effort to reduce labor costs" (Thelen & Kume, 2006, p. 32).

In addition, despite the overall commitment to the system of lifetime employment for core employees, some of them fell victims to the restructuring policies toward the late-1990s. Notably, the divide appeared to be mainly gender-based: "the burden of downsizing during Japan's prolonged stagnation fell disproportionately on women as opposed to men and on high-school graduates as opposed to college graduates. The biggest 'losers' appear

to be female regular employees over age 30 with relatively short tenure working in large firms" (Kambayashi & Kato, 2009, p. 25). Reflecting this decrease in women's regular employment as well as self-employment, the current composition of nonregular employees in Japan shows the overwhelming predominance of females, which is different not only from the continental Europe but also from the geographically close South Korea (Lee & Shin, 2017). On the other hand, the proportion of regular male workers (defined as regular employees on indefinite contracts) "actually rose from 58.3 in 1992 to 58.9 percent [of total male population aged 18-70] in 2002" (Kambayashi & Kato, 2013, p. 13).

1) *Causes*. Most of the authors attribute the increase of the nonregular employees' share to the post-bubble strategy of the Japanese companies that significantly limited the hiring of regular workers (Ishiguro, 2008, p. 5; Asao, 2011, p. 13; Gordon, 2017). Since the regulars used to have long-term contracts and various social benefits, lower proportion of core workforce against flexible workforce has been believed to help cutting labor costs during economic downturns (Kuroki, 2012, p. 562; Asano, Ito & Kawaguchi, 2013, p. 362). Following development adds credence to this view. A pay-per-performance system (*seikashugi*), primarily designed for temporary workforce, has been increasingly applied towards regular employees starting from early 1990s, thereby altering the seniority-wage principle (*nenkō joretsu*). For example, in the manufacturing sector, it mostly concerns white-collar workers, for it is problematic to make individual assessments of blue-collars under team-work production peculiar for Japanese firm's shop floor (Thelen & Kume, 2006; Vogel, 2006, p. 123). As a result, the implementation of pay-per-performance system, initially meant to bring some internal labor mobility, has eventually served as a concession for preserving a lifetime employment system (*shūshin koyō*) for core employees (Jacoby, 2005, p. 63; Vogel, 2006, p. 121; Jackson, 2007, p. 289; Keizer, 2009, p. 1530; Uni, 2013, p. 97).

Protection of a lifetime employment system means the following: instead of possible layoffs, companies have tended to almost entirely substitute hiring of new graduates – potential core employees – for nonregulars (Lechevalier, 2014). Thereby, two almost equal institutional arrangements have been created: the first one for temporary and the second – for lifetime employees. The argument about the sharpening duality of Japanese labor market as a peculiarly local feature is also supported by Gottfried (2008) and Fong & Tsutsui (2015). Keizer (2009, p. 1529) concludes that the possibility of virtually infinite contract extensions for the flexible workers has made their hiring an essential prerequisite

of corporate profitability rather than a temporary buffer, as intended originally. The Japanese Institute of Labor report specifies that nonregular employees have become major labor-force in retail and food industries as well as one of the key contributors to the manufacturing industry's competitive power (JILPT, 2010, p. 105).

Other possible factors behind the increase in nonregular employment include the growing determination of women, youth and retired workers to find employment opportunities. Since the standard options are limited, temporary employment often evolves as a second-best option. In addition, due to the contraction of self-employment, those who worked in this niche mostly move to nonregular positions (Rebick, 2005).

The existing literature, however, tends to overlook another factor behind the intensified labor bifurcation that is related to shareholders' pressure and to the changes in the way Japanese companies are run. In short, the growing proportion of nonregular employees is also a negative externality of the departure from the stakeholder model of corporate governance. While this model has not been completely abandoned, nonregular employees appear as "outsiders" whose interests are put in jeopardy in order to maintain the protection of "insiders" that include regular employees.

Although managers of large Japanese firms continue bearing monitoring functions, which protects them from immediate market-caused distortions, they also tend to become more focused on corporate profitability at the expense of growth. Managers have partially lost their immunity provided by relational bank supervisors and have become increasingly subject to shareholders' pressure. In the resulting attempts to guarantee high share value returns to investors, managers have tended to resort to corporate restructuring (Morgan & Takahashi, 2002; Miyamoto, 2017, p. 14). Restructuring is a part of a labor market deregulation meaning lowered salaries for ordinary employees and increasing reliance on flexible workforce. This can lead to two types of labor bifurcation. Firstly, as managers, through mechanism of stock-options, are eligible for premiums reflecting higher shareholders' dividends, their remuneration can grow disproportionally as compared to non-managerial workforce (van der Zwan, 2014). Secondly, nonregular employees can become not only a temporary solution to external economic shocks, but an integral corporate reserve that can be promptly adjusted to meet abrupt market demands.

The first kind of labor bifurcation has entered Japan's corporate scene after the introduction of stock options and share buybacks in 1997 (Dore, 2007). This growing gap between white- and blue-collar workers is mostly attributed to the alignment of CEOs with shareholders and to their resulting alienation from ordinary employees. In contrast, the

second type of labor bifurcation has become pronounced in Japan since early 1990s. It was linked to social turbulences that occurred after the 1990's bubble burst. Because of economic crisis, many workers lost their positions and had to look for temporary occupations. The decrease in family income also prompted women to look for jobs, thus challenging the traditional model of a male-breadwinner (Gordon, 2017). Steadily, the niche for nonregulars has also been expanded for men and is currently an all-inclusive category constituting 37.3 percent of a total workforce (Labour Force Survey, 2017). The concept "nonregular employee" encompasses following working categories (from the largest to the smallest): part-time workers, temporary workers (so-called *arubaito*), contract employees, dispatched workers, entrusted employees and others (Asao, 2011, p. 4).

The institutional peculiarity of Japan is that the growing wage gap within the cohort of regular employees is accompanied by their falling proportion against the nonregulars. These are related, albeit different processes, as the increasing proportion of flexible workforce does not seem to be a cause of growing wage-gap between managers and ordinary employees belonging to the group of core workers (Uni, 2012, p. 102). This point is further substantiated by the Ministry of Health Labor and Welfare Survey that demonstrates the narrowing gap between regular and nonregular employees' remuneration, which are still correlated at a 2:5 ratio (2015, p. 48). Furthermore, amid the reduced hiring of regular employees, the proportion of flexible workforce is growing drastically. Although the current research mainly deals with the labor duality between regular and nonregular employees, it inevitably touches upon the bifurcation between directors and employees. While the widening gap between managers and workers is an example of an *intra-firm* bifurcation occurring *within* companies, it is harder to classify the bifurcation between regular and nonregular employees. "Both explanations, rising intra-firm inequalities and rising inter-firm inequalities are not exclusive from each other" (Lechevalier, 2016, p. 63).

During the period of the rapid economic growth of 1950s-60s, Japan's *inter-firm* bifurcation reflected the dual industrial structure represented by large manufacturing companies with well-protected workforce, and the smaller subcontractors with less privileged employees (Teruyama & Toda, 2017). During 1960s, the wages at SMEs went up compared to large enterprises, which alleviated inter-firm differences (Lechevalier, 2016, p. 64). The inter-firm differences *between* capital- and labor-intensive industries, however, remained. Therefore, the increase in nonregular employment has mostly occurred in the service sector (retail, food) that needs low-skilled labor and is dictated by employers'

determination to cut labor costs. Thus, the *inter-firm* bifurcation between regular and temporary employees is determined by educational and industrial factors (Takahashi, 2016).

There is also an *intra-firm* dimension of the bifurcation between regular and nonregular employees. The gradual reform of the Labor Dispatch Law from 1985 till 2015 has eventually allowed all industries to employ nonregular workers. Also, nowadays, there is no correlation between the firm size as well as wage level, and the tendency to hire temporary employees (Takahashi, 2016). Although nonregulars are predominantly employed in the service sector, the currently predominant neoliberal ideology encourages employees to build individual portfolios, flexibly adjusting to the demands of different employers that are more likely to offer short-time contracts (Takahashi, 2016). Thus, bifurcation between regular and nonregular employees becomes a matter of concern *within* many firms regardless of industry and size.

Although labor deregulation seems quite common for other developed states, in Japan, the temporary workforce does not have adequate institutional representation. The postwar labor model was essentially firm-oriented, meaning that the bargaining tools were confined to the corporate realm. This was caused by the so-called *companyist compromise* that implied long-term relations of trust and cooperation between management and labor along with high costs of occupation change. It was centered on the acceptance of unlimited job duties by employees in exchange for the provision of job security by management (Yamada, 2002, p. 21). In other words, "entering the company" (*shūsha*) was more important than entering an occupation (*shūshoku*). The company-centered employment system has been supplemented by enterprise unions, geared towards so-called "lifetime employees". However, those labor unions were not designed for external workforce. Therefore, under conditions of the rapid expansion of the nonregular employment, none of the existing institutions could bear the function of representing this segment of labor (Fujimura, 2012, p. 10).

There are several reasons for the declined labor unions' militancy in general and the inability to argue for the nonregulars' rights in particular. Among the ones listed by Dore (2007b, p. 212) are "the institutional incorporation of enterprise union leadership into managerial career development tracks and the ideological dominance of the 'reform = acceptance of global standards in the interests of national competitiveness' rhetoric". In addition, the unionization rate at Japanese enterprises fell drastically – from around 30 percent in 1980s to 17.3 percent in 2016 (Basic Survey on Labor Unions, 2016). Another noteworthy development is that under the reduced CEOs' board called the corporate-officer

system (*shikkō yakuin*), there is no longer a reserved seat on the executive board for the HR department representative (Jacoby, 2005, p. 60). Since the latter has traditionally been an advocate of the labor-union's position, with the loss of the seat on the board, it has become much easier for other CEOs to bypass unions' claims when formulating corporate financial strategy. In this way, weakening of an HR department and thereby of a labor union, brings about the shift in balance from employees to shareholders.

Against the background of the declining unionization rate[6], labor unions which are members of Rengō (Japanese Trade Union Confederation) tend to represent the interests of core employees, but not contributing to the protection of the temporary workforce (Ishiguro, 2008; Fu, 2015). Along with the enterprise-centered model legacy kept intact for core employees, Japanese government has been promoting occupational orientation primarily for flexible or temporary workforce (Fu, 2015). Thereby, the creation of two almost equal and mutually dependent institutional arrangements has been supported (Fong, 2015). According to the MHLW survey (2016, p. 30) and Labour Force Survey (2017), the average possibility for males to move from nonregular to regular employment in the first quarter of 2016 was six percent, and for females – 2.7 percent. These extremely low figures tell that instead of serving as a temporary buffer in times of economic distress, nonregular employees make up a large cohort of precariat without clear prospects for future.

Recently, however, Watanabe (2017) came with the argument that the dualization perspective is too simplistic for the Japanese case. He notes that "labour unions allowed the LDP government to attempt to reform regular employment in a way to increase its flexibility, and the working conditions of regular workers have deteriorated" (Watanabe, 2017, p. 2). Thereby, the state and the business have been supporting the creation of intermediate forms of employment, however, to a lesser extent through delegating rights to nonregular employees, but rather through dismantling regular working arrangements. "While dualism still exists…, the Japanese labour market has become more 'diversified', rather than simply remain dualistic, as a result of reduced power resources of unions and more flexible use of regular employment" (Watanabe, 2017, p. 2).

According to Lee & Shin (2017) "dualization" is still a relevant conceptualization of the recent labor market developments in Japan. It is compatible with the segmentation version of the story: "the remarkable proliferation of non-regular employment [has been]

[6] Although, the percentage of part-time worker membership in labor unions has increased from 5.6 percent in 2010 to 7.5 percent in 2016 (Basic Survey on Labor Unions, 2016, p. 4), the overall proportion of part-timers during this period also grew from 34 to 38 % (Labour Force Survey, 2016).

intensifying labor market segmentation" (Lee & Shin, 2017, p. 18). Furthermore, "in the Japanese context, what is remarkable is that the term dualism (*nijū kōzō*) has been preferred to the one of segmentation (*bundanka*)" (Lechevalier, 2016, p. 63).

Turning back to the dual labor market hypothesis (Doeringer & Piore, 1971), the internal segment is composed of two tiers, meaning that relatively less qualified core employees are subject to deregulation, which brings them closer to the external segment. For example, Kambayashi & Kato (2013, p. 6) provide examples of "regular" Japanese workers being employed on a fixed-term contract – against the image of a "core employee" enjoying an indefinite term of service, and, of "nonregulars" being offered an open-ended contract (which does not, however, improve their job quality). In addition, the "dualization" concept underlines the virtually absent mobility between regular and nonregular employment. "Thus, if workers were hired in non-regular jobs at the beginning because of adverse economic conditions, employers might only offer them opportunities of non-regular employment afterward" (Teruyama & Toda, 2017, p. 10). In a nutshell, terms such as "dualization" or "bifurcation" do not reject the idea of further segmentation within each of the main employment categories, but rather map a pattern of major structural differences within a labor market.

2) *Corporate governance and labor*. Operating with the "institutional complementarity" hypothesis developed by Aoki (1994), an extensive scholarship analyzes possibilities of beneficial coexistences within market-oriented and relational corporate governance systems (Höpner, 2001, 2005; Jackson, 2005). As opposed to uncritical proponents of shareholder value enhancement (Friedman, 1970; Jensen & Meckling, 1976; Rappaport, 1986; Stewart, 1991), the advocates of institutional complementarity stress that there is no "right" model of corporate governance *per se*. They argue that the shareholder model has originated in the Anglo-Saxon world known for its adherence to the market model (Lazonick & O'Sullivan, 2000). On the other hand, the continual Europe and Japan have historically developed a relational stakeholder model (Jürgens, Naumann & Rupp, 2000; Fiss & Zajac, 2004). Corporate governance model is not as isolated phenomenon – it coexists with other institutions evolved around labor and finance. Therefore, the predominance of stable, firm-specific involvement of labor within the relational model and participatory, portable involvement of labor within the market model are no coincidence (Aguilera & Jackson, 2003; Höpner, 2005).

The literature on corporate *financialization* establishes a link between the relative growth of financial profits on one hand, and the widening income gap as well as the absence of wages' increments on the other (Palley, 2007). As the goals of companies become more finance-oriented, managers tend to concentrate on short-term market-based criteria, while neglecting firm-specific intangible assets (Gospel & Pendelton, 2003, p. 567). This is likely to result in the lack of attention to human resource development. Stockhammer (2010) mentions the increase in so-called "rentier income" that includes interest, dividend payments and bonuses, which is associated with the decline in labor costs. Darcillon (2015) also states that managers commonly resort to restructuring through labor cuts in their attempts to raise shareholder value.

The original hypothesis for Japan postulated complementarity between bank-oriented finance, contingent governance and firm-specific skills that imply long-term contracts (Tohyama, 2012). However, with the changes in financial system, whereby shareholders have gained more weight as compared to banks, employment system is also likely to partially transform from employee-centered to the one prone to restructuring in the name of shareholder value pursuit (Abe, 2002, p. 685; JILPT, 2010). This view points at contradictory interests of workers, whose welfare is protected under traditional for Japan stakeholder model, and interests of investors, who view employees' wealth merely as production costs that are subject to cuts during periods of economic distress (Dore, 2007b). "If the main-bank system of financing and long-term stable employment system are… complementary, the reassessment of cross-shareholding and the weakening of the main-bank system of financing should have a measurable influence on the Japanese employment system" (Abe, 2002, p. 685).

Even under current piecemeal transformations, the board reform (reduction of directors and introduction of executive officers) promotes restructuring and, thereby, undermines employment stability (Miyamoto, 2017, p. 14). According to Dore (2007, p. 376) the reforms "have had very limited effect in promoting 'good' corporate governance. Rather, they have contributed—along with other factors—to a shift in managerial objectives and priorities, specifically a downgrading of employee interests and an upgrading of shareholder interests". Waldenberger (2017) concurs that the reforms so far have little to do with corporate profitability – the situation which is exacerbated by the unwillingness to create liquid labor market (Milhaupt, 2017).

Shareholders' pressure results not only in labor dualization, but also in decreased wages and shortened contracts of employees regardless of their status. Dore (2008, p. 1108)

asserts the link between the growing shareholders' power and the decreased employees' tenure resulting from the intensified pressure from investors. Those Japanese companies that have been most eager to implement shareholder-oriented policies since 1990s, have loosened employment guarantees due to ascendance of shareholder value along the hierarchy of corporate priorities (Jacoby, 2005, p. 65). Whereas in the postwar period "the relationship between workers and managers was primary, and that between shareholders and managers was secondary", this order has been reversed from the late 1980s (Yamada & Hirano, 2015, p. 14). Against the economic slowdown in 1990s that followed the bubble burst, employers and business have eventually pushed for abandoning the annual negotiations with labor through *shunto* rounds (Uemura, 2012, p. 120), which caused steady decrease in welfare spending (Tohyama, 2012, p. 86).

After Japan's bubble burst in early 1990s, its financial system was liberalized by lifting restrictions on foreign shareholding and providing incentives for managers to prioritize shareholder value. Concurrently, corporate governance reforms have started since 2002, aiming to grant more credentials to outside directors and outside shareholders in the attempts to minimize agency costs. Against this background, Abe (2002), Abe & Shimizutani (2005, 2007), Noda (2013) and Morris, Delbridge & Endo (2018) have studied the repercussions of corporate governance reforms on labor policies. Abe & Shimizutani (2005, p. 14) conclude that "outsiders are more motivated to commit to wage cuts and layoffs, and to increase voluntary (early) retirement, while insiders are more inclined to commit to decreases in new hiring". Noda (2013, p. 395) confirms the association between the reforms and downsizing: "Japanese firms were more likely after 1997 to take downsizing actions earlier than had been the case before 1997, due to changes in Japan's corporate finance and ownership structure".

Moreover, in the context of foreign investors pushing the reforms' agenda, Ahmadjian & Robinson (2001), Ahmadjian & Robbins (2005), Yoshikawa, Phan & David (2005) and Nakano, Otsubo & Takasu (2014) found out that foreign shareholding is positively correlated with downsizing and the cutting of labor costs at Japanese enterprises. Okamoto & Matsuura (2015) corroborate the negative impact of foreign shareholding on unionization rates and, thereby, on the average employment tenure. Recently, however, Kubo (2018) came up with the argument that foreign shareholding and outside directors enhance firms' decent work practices measured according to the corporate social responsibility (CSR) criteria. Although this finding is contrary to my line of argumentation,

it nevertheless points at the relevance of the research that links corporate governance and labor policies in the context of Japan.

Jackson (2005) reminds us that from the institutional complementarity point, it is not sufficient to explore the influence of one variable (corporate governance) on another (employment system) assuming the *ceteris paribus* – one must look at the whole set of institutional conditions instead (p. 421). In this respect, the empowered financial markets are more likely to affect employment system when combined with dispersed ownership and high M&A levels (Jackson, 2005, p. 421). Hence, it is easier to explain why, despite the growing role of outside shareholders, the system of long-term employment for core employees in Japan has not been jeopardized (Kubo & Saito, 2012). Possible answer is: because the shareholding of Japanese companies remains relatively concentrated and the M&A levels are low.

Existing analyses of the link between corporate governance and employment only accounted for regular employees, not paying attention to flexible workforce. This undermines the robustness of measuring cuts in regular employment, since, especially from 2000s, major change has been the drastically growing number of flexible workforce, due to which the downsizing of regular labor could be halted (Lechevalier, Dossougoin, Hurlin & Takaoka, 2014, p. 19). Jackson (2009) and Morris, Delbridge & Endo (2018) mention the connection between corporate governance reforms and shrinking core workforce, however, do not touch upon the issue of nonregular employment explicitly. While addressing this significant gap, current study makes use of institutional complementarity hypothesis by arguing that *the shareholder-value enhancement alone is not enough to change the employment system for regular employees in Japan, but it is enough to intensify labor bifurcation between regular and nonregular workers*.

3) *Political aspect*. Existing studies have extensively covered the normative aspect of labor deregulation – from 1999 amendment of the Temporary Work Agency Law until 2015 revision of the Worker Dispatch Act – due to which, temporary employment was allowed for all occupations and sectors. Whereas scholarly opinions differ on the merits of labor deregulation as such, there exists a shared concern about the emerging labor bifurcation or dualization in Japan (Jackson, 2016; Lee; 2016). According to Watanabe (2012, p. 25), the rapid increase of the nonregular employees' share at Japanese enterprises during the last two decades goes against the explanations of institutional fit and incremental change. In turn, the author attributes it to the shift in political deliberations, whereby the

employment policies have moved from the jurisdiction of the Ministry of Labor (MOL) to the governmentally established Deregulation Committee in the mid-1990s (Watanabe, 2012, p. 31).

Due to the possibility of systematic corporate restructuring for regaining international competitiveness, both business (*Keidanren*) and labor unions (*Rengō*) agreed upon the need for maintaining guarantees for permanent employees (Yun, 2015, p. 5). Moreover, *Keidanren* has been one of the major opponents of implementing compulsory American-style corporate governance reforms for Japanese companies (Dore, 2007, p. 376). Realizing the institutional complementarity between insider-oriented governance and long-term employment system, *Keidanren* has been advocating to "maintain long-term employment security to achieve technological deepening of the manufacturing sector, while activating the use of alternative workforces to adjust swiftly to volatile labour demand" (Yun, 2015, p. 13). As the first aspect sought logical support from *Rengō*, the increase of non-unionized flexible labor has not caused substantial resistance from the trade-unions' confederation either.

Shibata (2017, p. 2) also sees a root of growing discrepancy between regular and nonregular employees in a short-sighted governmental policy. Mainly, current political-economic course known as "Abenomics" entails a number of fundamental contradictions. This includes the anti-deflationary efforts aimed at increased domestic spending, which are leveled by worsening conditions of the growing nonregulars' cohort (Shibata, 2017, p. 15). A related concern has been voiced by the consequent IMF reports that list governmental policies' demerits, even against the background of a generally positive stance towards labor deregulation by this organization (Aoyagi & Ganelli, 2013, 2014, 2015). In regard to the overall labor trends in Japan, authors express their concern with the declining labor's share of income, which contrasts negatively with the related developments in other G7 countries (Aoyagi & Ganelli, 2015, pp. 109-10). The inability of labor unions to demand wage hikes proportional to productivity increase is therefore a sign of an ultimate decline of these institutions in Japan. Moreover, the rapidly growing share of nonregular employees faces steadily worsening chances of attaining a regular status. This is likely to demotivate temporary workforce, thus slowing down labor productivity (Aoyagi & Ganelli, 2015, p. 111). Finally, deliberate placing of nonregular employees outside of institutionally formed "community company" discourages firms to invest in their on-the-job training (Aoyagi & Ganelli, 2015, p. 116).

It is worth mentioning that since 2012 Japanese government has been promoting an increase of the minimal wage. This rather unconventional policy advocated by the business-oriented cabinet has got a name of the "governmental spring offensive" (*kansei shunto*) (Chiavacci & Lechevalier, 2017, p. 9). One has to understand the institutional features of the management-labor relationship in Japan to comprehend this policy. As it will be discussed in the Chapter 3, the major benefit of being a core employee compared to temporary employee is not a higher minimal wage, but a strong social protection, under which the layoffs of core workforce are virtually impossible. Thus, the governmental initiative to raise minimal wage would imply the likely sacrifice of employment security for regular workers, which fits well with the business-oriented neoliberal model. Therefore, "many [workers and unions] choose job security over pay hikes. Demanding higher wages, they fear, would give companies an excuse to move operations abroad or adopt labor-replacing technologies" (Ito, 2018).

The strikingly unequal treatment of regular and temporary employees in Japan is also evident on the example of a minimal access of the latter group to various social benefits such as health and pension insurance, child care and paid holidays (Gottfried, 2008, p. 191). As Kuroki (2012, p. 564) admits, granting the existing gap between two groups of employees, the legal deregulation alone will not contribute to the improved security of nonregular workers. In a similar manner, Keizer (2009, p. 1532) stresses that without changing the rules of the game, namely, abandoning the practice of lifetime employment for core employees, the labor duality will only be exacerbated. From the institutional complementarity perspective, the political support of labor deregulation is a part of the efforts aimed at sustaining the integrity of a new institutional structure (Crouch et al. 2005, pp. 372-3). It is yet unclear whether the new hybrid proves successful in the long-term perspective, but unless the current internal-external conflicts within a corporate milieu are accounted for, the future of the Abenomics' third arrow remains uncertain.

Literature gap. There are hardly any studies about the influence of shareholder-oriented policies on growing proportion of nonregular employees in Japan. While most of the works that link corporate governance to employment date back to at least five years ago (Abe & Shimizutani, 2005, 2007; Araki, 2006; Conrad, 2009; Watanabe, 2012; Noda, 2013), there is a need to revisit this link and to specify the role of nonregulars amidst their drastically increased numbers. According to the recent article by Morris, Delbridge & Endo (2018, p. 2), "existing research does not provide concrete insights into how corporate governance structures condition employment relations practice over periods of time".

Moreover, recent studies devoted to the increase in the nonregular employment in Japan (Cooke & Jiang, 2017; Gordon, 2017; Waldenberger, 2017) operate with the national and industrial data, while I come up with the firm-level data.

The lack of analysis on the link between shareholder-value enhancement and human resource management has been recently acknowledged by Lechevalier, Debanes & Shin (2016, p. 4). Among the literature in Japanese that undertook a similar analysis is Sato, 2000 (as cited in Inagami & Whittaker, 2005, p. 84). Although he found out that the "reformist" i.e. shareholder-oriented companies tend to put more emphasis on individual rather than collective remuneration and to be less eager to maintain lifetime employment system, overall link between share price, ROE (return on equity), EVA (economic value added) and flexible employment appeared weak. At the same time, Ahmadjian & Robbins (2005) proved an impact of foreign shareholding on the downsizing of listed companies having weaker ties with partner financial institutions within keiretsu chains. According to authors (Ahmadjian & Robbins, 2005, p. 460), the major aspect of downsizing is a cut in the permanent labor force of more than five percent per year. Following the same logic, Waldenberger (2017) argues that labor deregulation and corporate governance reforms have been less successful at enterprises with predominant in-house careers.

I intend to explore the link between the intensified pursuit of shareholder value and the growing proportion of nonregular employees. While the topic of wealth redistribution in favor of shareholders and at the expense of workers is well-researched, the possible causes of labor flexibilization have not been studied sufficiently. This problem matters for Japan, because currently, proportion of nonregular employees there is almost 40 percent, while their chances of switching to regular employment are only 1.7 – 10.3 percent as opposed to 30 percent in the U.K. and 45 percent in Germany (Aoyagi & Ganelli, 2015). Moreover, in Japan "non-regular workers… are paid only 56.8% of what regular employees earn on average as compared with 89.1% in France, 79.3% in Germany and 70.8% in Britain" (Japan Times, 2016, as cited in Ishii, 2018, p. 2). This means that roots of nonregular employment in Japan are not merely economic, but structural, and, therefore, require institutional explanation.

In this respect, the approach of Aguilera & Jackson (2003) who view a company as a *coalition* between management, labor and shareholders can yield promising results. Within this framework, interests of nonregular employees are dependable upon other corporate parties. Since the role of shareholders in Japan has undergone most dramatic changes during the last two decades, their impact on other actors is likely to have grown

significantly as well. The most noticeable change is the growing proportion of foreign investors that mostly represent short-term interests as opposed to strategic interests of domestic financial stockholders. Their influence on Japanese joint-stock companies can either be direct – via exercising a vote at general shareholder meetings or reselling shares to a third party, or indirect – via reputational pressure related to the fact that share value reflects corporate attractiveness to investors.

Jackson (2005, p. 422) describes one of the cases of alliance between "stable shareholders, strong enterprise-based unions and career managers" as an "*insider-outsider coalition*". This description fits the Japanese model well, since the local coalitions have been traditionally centered on enterprises ("insiders"), while the current coalition also involves foreign shareholders ("outsiders"). On the other hand, the coalitions in Japan have not formed along the antagonistic *class* divisions between management and labor or along *accountability* divisions between shareholders and management (Jackson, 2005, p. 422). In fact, the issues of "class" and "accountability" have been encapsulated by the companyist compromise, discussed throughout this dissertation. Although nonregular employees are also "outsiders", they lack power to be included into the current political bloc. "Insiders are defined as those workers with highly protected jobs. Outsiders, by contrast, are either unemployed or hold jobs characterized by low levels of protection and employment rights, lower salaries and precarious levels of benefits and social security regulations" (Rueda, 2006, p. 387). Hence, I hypothesize that the growing proportion of nonregular employees is the externality of a newly formed insider-outsider coalition. I discuss this argument in detail in Chapter 6.

In this chapter, I reviewed the literature on the major theories used in this dissertation. Furthermore, I discussed the previous works on corporate governance reforms and on labor bifurcation in Japan. Finally, I pointed at the literature gap that concerns the research on the link between the enhancement of shareholder value, as a part of corporate governance reform agenda, and the increasing proportion of nonregular employees in Japan.

Chapter 3: Decline of the Companyist Compromise

This chapter discusses a concept of a "companyist compromise" developed by the Regulation school for the case of postwar Japan. While the companyist model was intact during the time of Japan's rapid economic growth from 1960s until the mid-1980, upon the bubble burst in early 1990s, its institutional foundations have been watered down. Below, I discuss the pillars of the "companyist compromise" for the postwar Japan. I conclude the chapter with the analysis of the modified environment, whereby the companyist arrangements remain intact, however, the external marked-oriented actors are gaining influence.

3.1. Institutional Foundations of a Japanese Company

Numerous scholars emphasize that the central feature of the postwar stakeholder model of corporate governance in Japan is "internalism" or "contingent governance" (Aoki, 1994; Buchanan, 2007). That being true does not however imply that main bank finance complemented with relational monitoring is key to understanding the institutional features of Japanese listed companies. The evidence from the beginning of the twentieth century shows the predominant role of stock finance and the accompanying market-based monitoring. This means that the modern "institutional fit" between financial and corporate monitoring systems was merely a result of peculiar historical circumstances (Miyajima, 1998) rather than a display of an inherent "corporate culture" as it is sometimes presented by the apologists of *Nihonjinron* ("theories of Japapaneseness") (Befu, 2001).

"Japan presents a particularly interesting case in so far as there was little legal protection for 50 years at the beginning of the century when there were good institutions in place, whereas strong investor protection was accompanied by an institutional failure to sustain the interests of outside investors in the second half" (Franks, Mayer & Miyajima, 2014, p. 4). The similar feature of the prewar and postwar corporate governance is, in turn, the importance of trust institution for corporate monitoring. Whereas in the first half of the century it facilitated the outsider control, during the modern era it has promoted an insider orientation. In particular, trust and reciprocity have been key aspects for such postwar industrial organizations as *keiretsu*, notable for their close customer-supplier relationships on micro-level and cross-shareholdings on macro-level (Lincoln & Gerlach, 2004). Granting the historical experience of shareholder finance and monitoring, the current market-oriented deregulation is thus not impossible from the institutional perspective. What

matters is, rather, the mechanisms of assuring reciprocity between corporate managers and outsider investors. In other words, according to Okumura, 2000 (as cited in Aguilera & Jackson, 2003, p. 461), Japan's corporate coalitions tend to be insider-based, which explains current institutional skepticism for merits of minority shareholders influencing firms' governance.

The institution of trust has also been fundamental for the management-labor relations. Though the pillars of the so-called "traditional" Japanese labor system that include lifetime employment (*shūshin koyō*), seniority wages (*nenkō joretsu*) and enterprise unions (*kigyō-betsu kumiai*) (OECD, 1973), were formed in early postwar years (Fujimura, 2012, p. 9), its roots go back to the dawn of the century. Nishiguchi (1994, p. 21) shows that the formation of in-house careers started around 1920s and was peculiar to such large-scale manufacturing like shipbuilding and steel industry. Furthermore, the first workers' movements in Japan during the 1920s and 1930s were "not driven by the assertion of class interests as much as the aspiration of being recognized as 'equal members of their enterprises'" (Aoki, 1997, p. 240). All in all, regardless of the corporate finance system, one of the ultimate tasks of a large Japanese company has been to preserve corporate integrity – substantiated both by such institutional pillars as: (1) trust relationship between managers / board and investors, as well as (2) between managers and regular employees.

Regulation school argues that the Japanese stylized corporate governance model can be analyzed on the example of *keiretsu* – large enterprises notable for their subcontractors' vertical chains and/or horizontal links with partner-banks coordinated by the Bank of Japan (Inoué & Yamada 2002, p. 264; Westra, 2003, p. 365). On the labor side, *keiretsu*'s rules of wage-setting were adopted to level corporations' competitive advantage and to relieve both management and trade unions from unexpected tensions. The coordination of wages' provision between labor unions and management became a tuned procedure and thus contributed to mutual benefits during the period of rapid economic growth that lasted until the late 1980s. Although financial and labor-management compromise has been largely undermined due to the prolonged economic downturn of the last three decades, coordinated principles of wage-setting are kept intact at large Japanese enterprises.

The complementary relationship between financial and labor policies has built a so-called "*companyist compromise*" according to the Regulation theory scholars (Yamada, 2002, p. 20). The first pillar stands for financial compromise, related to the main bank system, under which companies make extensive borrowing, thus expanding own

investment possibilities and supporting related banks by paying an interest rate. In return, companies receive insurance against financial distortions, which is aimed to sustain their long-term survival. Under this system, incumbent management is monitored and protected by main banks. The latter intervene with CEOs' replacement only in exceptional cases. The second pillar represents entrenched exchange, where workers receive life-long protection and guarantees against discharge but agree instead on carrying multifold responsibilities. Thus, "the strong, long-term relations between labour and management, and between companies and their banks… [are the] relations of trust and cooperation that serve as security networks, enabling the economy as a whole to achieve high efficiency" (Yamada, 2002, pp. 27-28).

(1) *Management* ↔ *Finance*. The system of financial support for companies during the post war period secured by the Bank of Japan was called "main bank system" (MBS). "The authorities implemented a 'convoy system' to protect even the most inefficient banks and ensure profitability by imposing severe restrictions on new entries into the banking industry" (Nabeshima, 2002, p. 106). Bond market was toughly controlled by a committee of major banks under Industrial Bank of Japan aegis. It limited the issuing of corporate bonds only to long-term banks so that they could not be resold to the secondary market by non-financial firms (Ueda, 2002, p. 98). In addition, the postwar inactivity in bond market was also due to the low interest rates promoted by the government in order to repay public debt that emerged as a consequence of intensive government-bonds issuing from 1960s on.

The reliance on debt-financing was supported by the fact that the Japanese MBS has been in charge of providing information about firms to fund suppliers (i.e. subordinated banks). "A main bank by definition has especially close ties to its customers through lending, shareholding, and (often) board representation and other personnel placement. This should give it relatively easy access to the same information about the firm's opportunities that the managers making investment decisions have" (Hoshi, 2004, p. 190). Thereby, the screening and monitoring costs have been alleviated for "ordinary" banks. Furthermore, while verifying firms' accounting, main bank as a shareholder has been capable of rescuing operations by protecting companies from hostile takeovers and bankruptcies (Nabeshima, 2002, p. 108).

The system of corporate finance has been formed on the basis of industrial planning at macro-level that has been stressing the role of heavy industries for overall economic advancement. The fit with organizational structure has emerged out of close long-term relations between corporations and partner banks. Firms' obligation to take excessive loans

under minimal interest rates from partner banks without being urged to pay them back has made industrial and financial institutions mutually dependent. Such nexus was established in frames of a state-promoted MBS. Thus, government and the Bank of Japan supported major banks in their relations with firms by guaranteeing potential bailouts and providing them with right to monitor corporate management. Hence, the formally centralized regulation by financial authorities has been based upon long-term relations between firms and banks.

(2) *Management* ↔ *Labor*. According to the institutional complementarity hypothesis employing a political economic logic, the inclusion of non-stable shareholders into the sociopolitical bloc triggers modifications in the related domains of corporate governance such as management and labor. While financial capital usually requires labor flexibility to adjust labor costs to short-term shareholders' claims, Japan's labor force is characterized by the predominance of in-house careers, whereby "top management positions in Japan, including the board of directors, are almost exclusively reserved to employees with a lifelong career in the company" (Waldenberger, 2017, p. 11). Thus, the immunity of core employees is closely linked to non-separation of monitoring and execution. As the separation of these two spheres is key to shareholder-rights' enhancement, their political pressure is therefore being redirected towards the group having the least political capital, which is the nonregular employees. By increasing their proportion and limiting their rights, thus keeping them out of the game, the current sociopolitical bloc supposedly shifts the burden of corporate externalities to marginalized outsiders.

One of the factors that contributed to the overall smooth alignment of management and employees' interests throughout the postwar period was the existence of enterprise unions. Together with the long-term employment, they served as a pillar of firm's social organization (Westra, 2003). Around 90-95 percent of employees of large firms (more than 500 employees) belonged to corporate unions in early 1990s, making this entity inclusive and universal, therefore "superseding traditional blue-collar, white-collar distinctions" (Fruin, 1994, p. 171). Indeed, the nonregular workforce existed in Japan long before 1990s; however, its proportion was relatively low.

While agreeing upon the fact that large business represented by *Keidanren* (former *Nikkeiren*) had a major interest in labor reforms, few attempts have been made to research the corporate privies. Most work concentrates on industries benefiting from accepting growing numbers of temporary employees (Ishiguro, 2008; Keizer, 2009). At the same time, hardly any papers have studied how and why corporate governance reforms can influence

a growing proportion of flexible workforce. In this respect, the Nikkei Index 400 can provide some evidence to illustrate this link. The Nikkei Index 400 can be considered as a political economic project because it was outlined in the governmentally formulated Japan Revitalization Strategy as one of the "initiatives aimed at enhancing the competitiveness of companies" (Japan Revitalization Strategy, p. 76). As an epitome of the current sociopolitical bloc, this index supposedly encompasses the interest of non-stable shareholders, management and core employees to the highest degree. Due to this, the constituencies of the Nikkei Index 400 also, supposedly, downplay the interests of nonregular employees, due to their low political capital and hierarchical standing.

In a nutshell, whereas the non-binding relationship between executive directors and outside investors allows the former to retain control over a corporation while delegating more credentials to the latter, the balance of power between CEOs and ordinary employees has considerably drifted towards the managerial side (Lechevalier, 2012, p. 69). Differently from an overall retained legacy of insider monitoring and management despite growing pressure from outside investors, Japanese labor has become increasingly outsider-composed. Hence, the pre-existing institutional complementarity between contingent monitoring by main banks and long-term employment relations (Aoki, 1994) has been substantially weakened. This has been the essence of a fragmentary deregulation of a stakeholder model with board and management remaining internally-oriented but influenced by shareholders' claims, and ordinary labor being increasingly composed of external workforce. Whereas informal institutions have continuously sustained the image of a "corporate family", those non-affiliated with a company directly have had far less formal institutional tools to argue for their rights.

3.2. Management-Finance Compromise

The postwar system of corporate finance in Japan was embedded into national and international macroeconomic structure. Thus, the understanding of the latter can shed light on institutional foundations of management-finance compromise at Japanese companies. Japan's postwar regime of accumulation was centered on regulated business-finance networks under the main bank system. Operating with the terminology of the institutional theory, *isomorphism* was an internal feature of a system. It was built on long-term commitments and relational monitoring. Under the classification of DiMaggio & Powel (1983), postwar isomorphism was closer to *normative*, i.e. "based on complex processes of

mediation through socialization and professional networks" (Beckert, 2010, p. 157). Relational main bank system also ensured high levels of output controls and even induced US companies to adopt productivity-enhancing techniques from Japan during 1970s-80s (DiMaggio & Powel, 1986, p. 151). Below, I discuss some pivotal developments of the postwar management-finance compromise.

1. *Nixon shock*. The surpluses of Japanese economy peaked in 1969 with an average growth rate of about 10 percent during 1960s (Uemura, 2002, p. 143), but fell considerably at the beginning of the 1970s because of the following international developments. In 1971, the Bretton Woods monetary system, under which countries pegged their currencies to gold, ended with a Nixon shock, whereby the convertibility of dollar to gold was terminated. This gave a start to a system of floating exchange rates, under which the US dollar became a major international reserve currency. Although this led to yen revaluation from 360 yen to about 300 yen per dollar in the aftermath of the Nixon shock, close ties with the US allowed Japan to peg its currency to the American one and thus maintain its exports, despite a significantly slowed economic growth.

2. *Oil crises*. In 1973, the Organization of Petroleum Exporting Countries (OPEC) raised the costs for oil, upon which the Japanese economy was crucially dependent. For the first time in postwar history, this led to a significant inflation and a negative GDP growth (Hoshi & Kashyap, 2004, p. 222). The market-firm nexus managed to structurally modify itself to the new economic conditions. This implied a shift of Japanese economy from the model of "profit-investment-led" to "export-investment-led" growth. The relatively high productivity rates in comparison to other industrialized countries were the consequence of effective modifications of production system, which included restructuring of subcontractors' networks of *keiretsu* enterprises (Uemura, 2002, p. 139). Consequently, although companies incurred losses, the economy entered a stable growth by the end of 1970s, which also allowed for an adjusted reaction to the second oil crisis of 1979.

After the Bretton Woods break in 1971 and until the early 1980s, the Japanese economy was mainly export-oriented, depended on the American markets and maintained low yen exchange rate. During this time "banks dominated the financial system, bond markets were repressed and equity issuance was relatively uncommon" (Hoshi & Kashyap, 1999, p. 134). Like in the US financial system regulated by the Glass-Steagall Act, commercial and investment banks were separated, thus leaving space for the governmental influence (Hoshi & Kashyap, 1999). The latter was carried through the system of main banks attached to partner *keiretsu* and acting in line with governmental entities such as the

Development Bank of Japan (DBJ). The existence of a centralized banking system was essential for the possibility to redirect households' deposits to the industrial sector. Thus, the task of preserving major banks was central to the Japanese financial system. "An extreme version of the pursuit of stability in banking is the so-called convoy system, which allows no banks to fail… When, on occasion, a small, weak bank becomes nearly insolvent, MOF arranged a merger with a stronger bank" (Hoshi & Patrick, 2012, p. 8). The monitoring network was in turn extended by banks upon the borrowers, thereby eliminating moral hazards. "Because the main bank has close ties to its customers and [under *keiretsu* system] is expected by the other lenders to be responsible for its customers, it will have strong incentive to monitor them" (Hoshi & Kashyap, 2004, p. 192).

The three major types of stockholders in the J-firm before 1990s were: individual stockholders, financial-institutional stockholders, and other corporate stockholders (Aoki 1988, p. 116). Though financial-institutional stockholders played a major role in providing corporate capital, the original source of companies' support from banks was welfare capital. Through the channeling of funds from mandatory employees' insurance and pension fund payments to the public finance system via postal savings programs, companies were provided with stable reserve funds (Jackson & Vitols, 2001, p. 184). The long-term cooperation between corporations and financial institutions backed by constant supply of welfare funds built up a system of coordinated market economy: "Japanese corporate pension plans, by law, can only be managed by life insurance companies or trust banks. These financial institutions are subject to numerous regulations by the government as to what they can do with the funds" (Estevez-Abe, 2001, p. 192).

This corporate-finance compromise started to decline from the second half of 1970s. By that time the firms had benefited from the export-oriented economy and managed to accumulate considerable surpluses. Thus, the need for permanent external financing became less acute (Aoki, 1988, p. 127). Consequently, the corporations' fund-raising was gradually reconsidered as a reaction to the unfolding financial deregulation. This implied the usage of stock finance. "Bank borrowing drastically declined from 38.9 per cent in the 1960s to 8.9 per cent of external financing in the 1980s… The percentage of financial assets as a part of total operating assets increased from 25.7 per cent in 1981–86 to 35.6 per cent in 1986–87" (Tohyama, 2012, p. 79). On the other hand, the liberalization of the financial system since the mid-1970s prompted both *keiretsu* and independent firms to start using non-bank finance (Aoki, 1988, p. 102). "In 1980, firms listed on the Tokyo Stock Exchange had nearly 90% of their debt in bank borrowing. This figure had dropped to 50% by 1991"

(Hoshi, 1994, as cited in McGuire & Dow, 2003, p. 379), which triggered a weakening of a bank-centered financial compromise.

From the early 1980s, big companies listed at the Tokyo Stock Exchange started to use direct finance by issuing different kind of bonds like convertible, warrant and straight (Itoh, 2000, p. 84). Corporations that became independent from major banks while changing their capital structure were classified as "nonaffiliated", whereas the ones that continued relying on debt were called "main bank firms" (Campbell & Hamao, 2002, p. 325). From the 1980s on, nonaffiliated companies also started to issue bonds overseas. Though the rules for this activity were the same as for domestic issuing, the Euro-bonds issuing was advantageous, since it did not require a collateral (Campbell & Hamao, 2002, p. 330). "Many large firms had reduced their dependence on banks substantially by the end of the 1980s" (Hoshi & Patrick, 2012, p. 10) by issuing foreign and domestic bonds, thus challenging the monopoly of bank finance.

The 1985 Plaza Accord brought about the sharp devaluation of dollar and thus induced drastic modification of the previously-established export-led Japanese strategy attached to the US markets. The structural changes in the Japanese economy were on the way. The Maekawa Report of the Advisory Group on Economic Structural Adjustment for International Harmony, an unofficial advisory body to then prime-minister Nakasone adopted in 1986, reflected the shift from an "export-led economy" to a "domestic demand-led economy" (Morioka, 1991, p. 19). This gave a start to a full-fledged globalization of financial transactions and further eased the access of companies to financial markets.

Before the financial liberalization of 1980s, the MBS was functioning under conditions when corporations hardly operated with free capital flows, which made supervision quite easy. However, with *keiretsu* gaining independence from debt finance, the main bank was partially divorced from companies' managerial activities. Facing BoJ's eased terms of continuous credit supply "J-firm generated ample equity capital for investing in fixed assets and the surplus of funds was directed toward short-term financial market operations (the so-called *zai-teku)* and speculative investment in real estate" (Aoki, 1988, p. 141).

The overall restructuring as a response to the new economic conditions was backed with parallel rising in stock prices and real estate prices, as well as accompanying expectations about their further growth. Corporations intensively participated in financialization not only because of accumulated funds and new favorable conditions for market finance. They were backed up by the government that despite formal deregulation

considered bank-centered financial compromise to be the cornerstone of the industrial system. Thereby, both banks and big corporations expected support. The Ministry of Finance publicly declared that every potential bankrupt bank would be bailed out (Ozawa, 2005, p. 198). Such "obsolete" policy after the bubble burst in 1990 resulted into the fact that large firms did not react flexibly and promptly to the stock prices' crash (Cargill, 2012, p. 38).

On the other hand, banks also had their motivation to step out of the game. Since the amount of credits issued by banks – and, therefore banks' income – was reduced, this created a disincentive for financial authorities to proceed monitoring these "contracted-out" corporations. By the late-1970s, public debt increased due to economic slowdown and a consequent decrease in tax revenue. Hence, the amount of welfare funds aimed at capital investment significantly dropped. This resulted in intensified government-bonds' (GB) issuing, for which the secondary market (*gensaki*) was created. To compete with GB, banks raised their returns on deposits (Nabeshima, 2002, pp. 111-112). However, their reliance upon the old forms of finance remained unchanged, which illustrated their inelastic reaction towards structural changes of financial markets. "Even after their large customers took advantage of deregulation to start shifting away from bank financing, the banks continued to rely on the traditional banking business of collecting deposits and making loans. Rather than downsizing and moving into new niches, they tried hard to retain their size by finding new customers for loans" (Hoshi & Kashyap, 2004, p. 198).

The deregulation process in Japan has gained momentum rather late compared to the U.S.: 1987 as a turning point to grant the American commercial banks with investment possibilities, and 1993 for Japan (Financial System Reform, allowing banks to enter security business through subsidiaries), marking the new mechanisms to overcome the post-bubble depression (Hoshi & Kashyap, 1999, p. 9). Hoshi (2001) argues that enormous bubble swelling happened mainly due to belated deregulation. This claim, needs further explanation. Deregulation was problematic due to existing companyist compromise that had a form of "convoy system" of state over BoJ, and by BoJ over corporations. Furthermore, the undertaken fragmentary actions favored corporations but left the main lending institutions with their old tools. In other words, major banks as intermediaries between public welfare programs and private industrial entities were bond with the companyist regulation developed since the 1970s. When deprived of their regulatory function in the course of neoliberal policies, they became "stuck in traditional lines of

business while many of their traditional customers changed their financing patterns" (Hoshi & Kashyap, 2004, p. 227).

Upon the emergence of alternative opportunities for the large companies (belonging to *keiretsu* structures) to raise the funds, many banks attempted to fill the gap with alternative options. As the main banks started losing their large clients in the late 1980s, they began lending to SMEs (Ozawa, 2005, p. 198), benefiting from "priced stock market for shares" (McMillan, 1996, p. 154). Whereas earlier, banks' activities were confined to lending to big corporations within *keiretsu* corporate system, by the end of 1980s the main borrowers became real estate agencies, construction firms, specialized housing finance companies (nonbanks that did not receive deposits) and individuals (Itoh, 2000, p. 8). Without having a sufficient knowledge about new clients, banks considered mortgages' issuing to be a priori safe, since the land nominal value did not fall throughout the postwar period.

Due to the lack of information transparency, the fall in land prices in 1992 brought forth an evidence of insolvent loans. At the end, as the hopes for the growth in stock prices were fueled, "government policies and plans contributed to the formation of the inflated expectations, which resulted in massive bad debts" (Iyoda, 2010, p. 76). Moreover, as mentioned earlier, banks lost their monopoly for financial operations, thus opening the road for equity finance. Thus, out of the total amount of loans to real estate market that counted for 120 trillion yens, "major banks owned 59 trillion, and the non-banks – 50-55" (Itoh, 2000, p. 8). Out of these 50-55 trillion of non-banks' loans, the large part was borrowed from banks, which facilitated the bubble creation (Itoh, 2000).

Because of the increased competition from insurance companies and post offices, the major Japanese banks decided to expand their activities abroad. The resulting rapid increase in the Japanese international banking assets in the period from 1985 to 1989 became one of the reasons for the Basel I agreement in 1988. The latter limited own capital of banks by 8 percent of their assets. The need for banks to toughen their loans' rules coincided with the US Federal Reserve Bank interest rate increase (from 5.5 to 7 percent) in 1989, which spurred the BoJ to promote the analogous policy (from 2.5 to 4.25 percent). The latter caused yen depreciation and the fall, first in share prices from 1989 on, and in real prices for housing starting from 1992 (Itoh, 2000, p. 88). With the real-estate prices' crash in 1992, numerous large companies that had their housing possessions, had experienced huge losses. Starting from 1995 "Japanese companies not only stopped taking out new loans, but actually paid back existing ones, despite short-term interest rates that

were close to zero" (Koo, 2011, p. 12). Thus, one could observe demand loss in two ways: "businesses are not reinvesting their cash-flow, and the corporate sector is no longer borrowing and spending the savings generated by the household sector" (Koo, 2011).

Even after the 1992 bubble burst, public expenditure remained at high levels, holding the expectation that during the further yen to dollar appreciation (from 145 yen in 1990 to 79.5 yen in 1995) the bonds issuing will revive domestic demand. The latter did not however ameliorate the situation and led to the public debt increment. In 1997 its ratio against GDP has reached 92.6 per cent leading to gradual Big Bang deregulation (Itoh, 2000, p. 96). Critics point that the BoJ policy should have been more expansionary by further GB issuing (Bernanke, 2003, as cited in Cargill, 2005, p. 314) to combat deflation – a display of depressed internal demand.

In addition, the full-fledged deregulation of Japanese financial markets started only from 1998 on. It targeted the unfavorable asymmetry between companies profiting from equity finance, and commercial banks without access to investment opportunities. The opposition between banks and securities houses was alleviated by allowing banks to involve into securities business, however not in a way of German universal banks, but through subsidiaries (Hoshi & Kashyap, 1999, p. 9). Also, the cornerstone principle of management and stockholding separation was formally abandoned by lifting a ban for holding companies' establishment (Hoshi, Kashyap 1999, p. 5). Finally, the introduction of stock options and share buybacks in 1997 further aligned the interests of managers and shareholders (Dore, 2007).

3.3. Management-Labor Compromise

From the point of Regulation theory, institutions are situated in the heart of an interaction between market and national regime of accumulation (Uni, 2002, p. 54). The most institutionally representative for the Japanese regulation are *keiretsu* enterprises that are characterized with pronounced financial links to partner banks. Regulation theory emphasizes that these large corporations are responsible for creating "structural compatibility" between Japan's industrial policy on the macro level, and labor organization on corporate and micro levels (Isogai et al., 2002, p. 32). Aoki (1997, p. 235) argues that the institutional framework in the postwar years was efficient mainly due to organizational coordination within and between large enterprises.

However, this stylized approach based on large enterprises has certain limitations. Until today, there exists a clear difference between large industrial corporations and small firms in terms of employees' welfare provision. Only large enterprises receive long-term bank-funding with low interest rates and thus provide their employees with social benefits. In the afterwar period, such *keiretsu*-sectors (steel, shipbuilding, chemicals) "were protected from international competition and given time to become sufficiently productive to compete in the international market" (Hoshi, 2004, p. 206). In contrast, medium and small enterprises utilized relatively cheap labor that served as a counterbalance to prosperous core workforce (Miyazawa, 1980, p. 49). Institutional compromise as a leverage for Japanese mode of regulation spreads only across big corporations that employ the minority of local workforce. In the beginning of 1990s, 75 percent of the workforce was employed at SMEs (Levine & Ohtsu, 1991, p. 105). In 2014, the proportion of workforce employed at companies of over-300 employees constituted only 14.5 percent (JILPT, 2017, p. 22). In addition, only a part of employees at big enterprises have a permanent status. Providing this dual structure of Japanese production system, "widely acclaimed IR policies and practices are applicable only to large enterprises and only to regular male employees of the organizations" (Singh, 2000, p. 365).

There exists an academic debate around the question of whether the postwar Japanese mode of regulation can be considered as Fordism. The authors that adhere to this hypothesis do so with certain limitations. Despite the parallel growth in mass consumption and production in the after-war period and until mid-1970s, the first was not indexed to the second with the growth rate of real wages being slower than the productivity growth (Inoué & Yamada, 2002, p. 260). This argument, in turn, leads to the recognition of the fact that the economy of that time was not primarily demand-oriented and therefore Keynesian, but rather centered on the idea of capital profits of big corporations. According to Itoh (2000, p. 4), in order to increase public expenditure in the postwar period, the state did not go into deficit but used natural tax revenue caused by the overall economic growth. Consequently, providing the absence of the specific fiscal policy, the state naturally faced problems during the 1973 oil crisis. Even though the wages' increments during postwar period were already embedded into economic growth cycles, the consensual principle of their provision was central to Japanese management-labor negotiations.

During the postwar period, although capital coefficient rose, the increases in labor productivity due to innovation techniques kept prices relatively low and therefore sustained demand for capital goods at a stable level. From the 1970s on, the Japanese economy

abandoned the patterns of Fordism. It was formally in place in 1960s, when Japanese economy "exhibited vigorous 'profit-investment-led growth' through the mass production and mass consumption of consumer durable goods" (Uemura, 2002, pp. 138-9). This tendency diminished by early 1970s, when, firstly, Japanese households that had traditionally high savings and exhibited relatively low spending, fulfilled their demand in durable goods (Uni, 2002, p. 62). Secondly, capital accumulation in the industrialized countries including Japan rested upon the access to cheap crude, mainly oil. When its price drastically increased, this exacerbated the overall economic performance and led to incomes' curbing. Therefore, during the wage-bargaining rounds after 1973, labor agreed upon modest increases in return for preserving old employment guarantees. Thus, starting from the mid-1970s, Japan ceased demonstrating formerly present Fordist tendencies in terms of labor costs and mass consumption.

The modified management-labor compromise took the following shape in Japan during the mid-1970s. In the stylized Anglo-Saxon corporation, a worker accepts limited number of duties, agreeing in return for the proportional wages' provision. Yamada (2002, p. 21) offers the following scheme for the American industrial compromise: *"The acceptance of Taylorism ↔ The provision of productivity indexed wages"*. In turn, the core of the Japanese compromise lies within the acceptance of unlimited job duties in exchange for the provision of job security for employees. Thus, the compromise looks as follows: *"The acceptance of unlimited duties ↔ The provision of job security"* (Yamada, 2002).

The common Western work ethics implies utilitarian character of labor relations which are part of the rational exchange. A workplace is a space where class and status distinctions between management and labor are materialized into a personal subordination. In contrast, the motivation at Japanese enterprises is of a collectivistic kind, and distinctions between white- and blue-collar workers are blurred. Being an employee of a J-firm (*kaisha*) implies the following: "It does not mean that individuals are bound by contractual re1ationships into a corporate enterprise, while still thinking of themselves as separate entities; rather, *kaisha* is 'my' or 'our' company, the community to which one belongs primarily, and which is all-important in one's life" (Nakane, 1970, p. 3).

Though there is a clear formal hierarchy, it does not significantly affect functional reciprocity between blue- and white-collar workers. "It is important to recognize that Japanese firms have become increasingly competitive not by eliminating hierarchy but by elaborating it" (Fruin, 1992, p. 172). Company members associate their personal benefits with the overall corporate success, due to the system of lifetime employment with in-

company training, seniority-merit pay, and welfare provided by company (Sako, 2006, pp. 15-16). "[This] can be interpreted more clearly as a sense of belonging to the whole company as a place of employment rather than to any specific job… Labor unions are organized into enterprise-based units in which all employees are members, regardless of their occupations of job classifications… The human relations within corporate framework extend to the realm of private life" (Inagami, 1988, pp. 34-35). Within Japanese corporations, submission is symbolically perceived through a common ground. In this regard, Manow offers a hypothesis (2001, p. 30) that the link between wages and welfare regime during an economic growth period represents a motivation of employers to set social rules in a form of wage-coordination, which is likely to reduce their "collective-action" costs. From the point of labor this, however, means, that their wages lag behind productivity, which at the same time does not hurt the overall economy due to a rise in demand for durable goods. In turn, the surpluses are directed into investment and not appropriated by management. Such corporate regulation enabled a successful macro-economic transition from "profit-investment-led" to "export-investment-led" growth model in the mid-1970s.

Close ties that exist between a J-firm and its subcontractors in a capital-*keiretsu* system as well as overall hierarchical ranking support the following fact. Large part of a wealth of de-jure permanent employees consists of potential claims for their future seniority premiums and separation payments that are therefore dependent upon firm's performance (Aoki, 1988, p. 206). Thus, the abovementioned pillars of Japanese corporate labor market are inseparable from the respective industrial structure and therefore provide the following evidence: "The J-firm is a *coalition* of the body of stockholders and the body of employees, integrated and mediated by management, which acts to strike a balance between the interests of both sides" (Aoki, 1988, p. 101).

The main reason why the workers are cooperating with capital while associating their interest with corporate priorities is the importance of status in Japanese society that has to be accounted along with class notion. One of the scholars, who apply Weberian methodology for Japan, notes the following: "Status-inconsistent individuals tend to find it difficult to share coherent class-based interests and class solidarity. Accordingly, the growth of status-inconsistent conditions has led to the decline of clearly demarcated class lines" (Sugimoto, 2010, p. 47-48). Usually status is recognized through belonging to certain corporation. Historically, the first workers' movement in Japan during 1920s and 1930s were "not driven by the assertion of class interests as much as the aspiration of being recognized as 'equal members of their enterprises'" (Aoki, 1997, p. 240). In the after-war

times, it has been not only about a prestige of a firm's name, but also about the number of privileges, primarily during retirement period, which a former employee receives. This includes indexed pension, provision of medical services as well as a possibility for a white-collar worker to "get a post of a director of the enterprise within the same group" (Morishima, 1983, p. 173). Thus, such factors as high costs of changing occupation by core-workforce as well as cultural encouragement of personal devotion to corporate goals were effectively used to sustain firm-based regulation model.

Distinct labor-capital relations at enterprises were based on *shunto* – annual "spring offensive" that came into being in the late 1950s. "*Shunto* can be characterized as a process of dispersed company-level bargaining that brings coordinated results" (Weathers, 1999, p. 963). It has been both an instrument of labor-movement unity achievement (since formally the labor unions are confined with enterprise frames) and "a regulative device that promised to ease the competitive pressures among employers… by leveling wage differentials between the major firms" and thus regulating oligopolistic competition between *keiretsu* (Manow, 2001, pp. 43-44).

The peculiarity of wage-bargaining process in Japan lies in the fact that both unions and management speak not on behalf of themselves but as members of business/industrial groups (*keiretsu*), which leads to decentralization of authority. Hence, the task of nation-wide organizations "is to aggregate the interests of members and mobilize them when trying to reach their goals for the benefit of the group as a whole… Labor emerged as a unified and coherent actor under *shunto*" (Tohyama, 2012, p. 74). Due to the aforementioned devotion of both management and workers to corporate goals, an "enterprise consciousness" as a main social identity has prevailed at enterprises (Sako, 2007, p. 16). "Bargaining is dispersed because the actual wage decisions are made in individual enterprises, but it is coordinated because the decision making preceded months of information gathering and exchange among numerous employers' associations, industrial unions, and other economic associations" (Weathers, 1999, p. 963). This, together with minor influence of market over wage-setting system and minimal external mobility for labor are the main reasons why corporate private-sector unions play major role in Japanese labor disputes.

The corporate system of wage-bargaining became crucial for macro-economic performance after transformations of international monetary regime. With the break of Bretton Woods system in 1971 and the 1973 oil shock, Japanese economy became export-led. The natural growth cycles intrinsic to the after-war economy of scale were no longer reproduced, which led to the searches of new sustainable capital-labor strategies. Due to

the decentralized nature of wage-bargaining that was regulated conventionally by *shunto*, the private-sector unions eventually took an initiative of coordination within this heterogenic system. The commonness of motivation among managers and employees can be observed through the perception of the inclusive character of trade-unions. "The position of president of the union, or other posts among the union's leadership, even came to be regarded as important stops on the road to success within the company. In fact, in many enterprises, the head of the union subsequently became president or director of the company" (Morishima, 1983, pp. 167-168). Around 90-95 percent of large-companies' employees in 1990s used to belong to company union, making this entity inclusive and universal and, therefore "superseding traditional blue-collar, white-collar distinctions" (Fruin, 1992, p. 171).

Due to the abolition of the public right to strike in 1973, the unions' strategy became solely firm-oriented. Their leaders "shared with employers the view that higher wage hikes bring about inflation and have a negative effect on economy as a whole, that wage increases damage firms' international competitiveness and are harmful to maintaining employment" (Tohyama, 2012, p. 75). Such motivation was hardly a display of capitalist hypocrisy but rather reflected the macro-economic slump of Japanese markets after the Bretton Woods system collapse. From 1970s on, recognizing the need to spare, primarily due to the hardships of small firms caused by the imports' price increments, *Nikkeiren* (Japan Federation of Employers' Association) initiated new rules of wage-provision for large companies.

As of the revocation of the public right to strike, one could assume that the workers' welfare was expropriated by the capital. On one hand, workers' bargaining power was significantly undermined. The epitome of this political loss was a defeat of the strike by the public-sector unions of Japan National Railways in 1975 (Watanabe, 2012, p. 29). On the other, asymmetrical power relations did not result in unilateral capital-oriented policy until mid-1990s. As for the 1970s, the common ground for managerial and labor interests was successfully found due to the equal access to corporate plans. This way, the information was not concentrated in the hands of employers, but was instead shared to give credence to wage-level argumentations. This was the reason why the workers did not strike against lower than expected wages. As Morishima argues: "the more the firm engages in information sharing, the shorter and less strike-prone the negotiation process is expected to be" (1991, p. 471).

By the mid-1970s, *keiretsu* accumulated profits that allowed for a growing formal autonomy from bank-finance (Hoshi & Kashyap, 2004, p. 223). Since the management and labor had equal rights within *shunto* rounds, the overall profit growth at enterprises resulted into a stronger bargaining position of unions leading to high (32.9 percent) wage-hikes in 1974. Although the subsequent increase in labor costs was minimal, a uniform wage-setting mechanism among corporate enterprises allowed for keeping wages growing till mid-1980s.

The Joint Consultation Committees (JCC) established to mediate the management-union interests owe their success to the voluntary sharing of information by managers. These negotiations take place within three levels: besides internal enterprise negotiations, the procedure is held for respective industries where the information about general trends is exchanged between management and labor. Furthermore, "at the national level, a tripartite consultation organisation, the Sangyo Konwa Kai (Industry and Labour Round Table Conference), functions as a forum where leaders of the government, the labour and the management, and academic experts meet to discuss policies for industries and labour" (Singh, 2000, p. 371). This triangular compromise was reached after the first oil shock of 1973. "In exchange for employer and government policies to maintain or improve employment security, economic stability, social welfare, and control over inflation, the unions pledged wage restraint, acceptance of technological changes and structural shifts, and avoidance of walkouts" (Levine & Ohtsu 1991, p. 108).

The described system seemed to have won a general consent, at least judging by numbers. According to the 1985 Ministry of Labor survey, "only 3.2% of some 2,700 unions with JCCs reported dissatisfaction with current JCC activities, an unlikely figure if firm management kept using JCCs to deceive unions year after year and information sharing was a gesture lacking provision of valid information" (Morishima, 1991, p. 476). Since JCC was held on voluntary basis, this could ease pressure both for management and employees while discussing burning issues of remuneration (especially during the 1970s' crisis). Consequently, during following formal *shunto* bargaining-rounds both sides could avoid serious tensions. As the tendency towards the fall in productivity (and respectively – in wages) at enterprises has gathered pace in 1990s, to avoid mutual discomfort during *shunto* rounds, more and more emphasis has been put on the JCCs' activity. "Labor disputes continued to decline in number, dropping from about 7000 a year in the early 1980s to below 1300 a decade later" (Taira & Levine, 1996, p. 145).

The formal consent with the established remuneration rules should not divert our attention from the fact that the unionization rate in Japan has been falling consistently after

the 1973 oil crisis (Ministry of Health, Labour and Welfare, 2014). Moreover, the decline of unions' power has been reflected in the gradual decay of the *shunto* negotiations throughout the post-bubble decade during 1990s. This has caused decreased wages during the process of economic recovery that started from 2002 (Uemura, 2002, p. 120). Lower wages, in turn, depressed consumption demand which is a key factor for Japanese economic recovery against strong yen that does not favor export-oriented strategy.

In a nutshell, export-led orientation that was in place during 1970-80s, allowed for a successful integration of wages' coordination into national industrial policy and facilitated channeling of surpluses into investment (Uemura, 2002, p. 139). However, such policy was dependent, firstly, upon households' income and consumption, and, secondly, upon international exchange rates. The 1985 Plaza Accord resulted in yen appreciation and hence – lower corporate profits due to raised costs for exported goods. Accordingly, from 1986 onward, Japanese government initiated neoliberal reforms which promoted lower labor costs and potential employment flexibilization. While employees' remuneration growth started to fluctuate around "zero", households' income and consumption rates went further down[7]. This process was paralleled with a tax-revenue decrease. Providing the absence of efficient fiscal tools, the government eased monetary policy, much in line with neo-liberal recommendations, thus creating space for speculative finance.

3.4. Modified Compromise

The former regulation regime that implied corporate accountability and subordination to state regulatory policy in return for funds' supply was effective during high-growth period. During the postwar time, the extensive usage of welfare funds was naturally compensated by cyclical profits. However, starting from the late-1970s, only large corporations that used to deploy public finance for internal modernization like R&D, could conform themselves to the new mode of accumulation. Facing the decline of MBS monitoring with no other substituting it to manage financial risks, the overall regulation mode was put under question. "To the extent that a monopoly control of credit in the Japanese banks was critical to their power, the rise of alternative credit sources and the growth of corporate retained earnings diminished it" (Gilson & Roe, 1993, p. 880).

[7] The so called "Heisei Boom" of 1989 was driven mainly by relatively prosperous social groups that purchased real estate and other high-priced goods.

The export-oriented strategy, on which the MBS was centered, had to be modified in the aftermath of 1978 Iranian revolution, with the unfolding of a second oil shock. Japanese exports dropped by almost nine percent leading to wages' decrease in manufacturing, further depression of tax revenue and fall in overall demand. Hence, government switched its focus from expansive monetary policy to fiscal austerity measures much in line with Thatcher's neoliberal actions (Itoh 2000, p. 12). Improvements in Japanese economy in the period of 1983-85 were connected to the US macroeconomic recovery. The increased rates of productivity in 1980s were attributed to yen devaluation. The latter allowed for further promoting export-led strategy. The international situation at that time favored it. Under Reagan's neoliberal policy directed at the early-1980s recession overcoming, dollar exchange rate was kept high, which supported Japanese exporters but also contributed to a trade imbalance between countries.

The situation became complicated for Japan with the adoption of Plaza Accord in 1985 that brought yen revaluation against dollar and therefore stipulated companies to expand abroad and take advantage of available financial opportunities rather than to continue maintaining high productive outputs. The higher attention of large multinational corporations to financial profits rather than profits resulting from trade and commodity production can be classified as "*financialization*" (Krippner, 2005).

On a corporate level, financialization is characterized by "a disconnection of wages from productivity growth" and a general widening of income redistribution gap (Palley, 2007, p. 3). This situation has been observed in Japan after the 1985 Plaza Accord, when rising productivity was accompanied by stagnant wages. The former was caused by "fall in the yen-based prices of imported raw materials, by the overseas production of parts, and by the other strenuous efforts of industries to rationalization" (Iyoda, 2010, p. 73). The latter, in turn, can be attributed to disaggregation of the supply chain, whereby a centralized labor-management negotiation system is no longer embedded into a national companyist compromise (Morgan, 2014). Whereas before, the obligations to stakeholders, and, above all, employees, were on top of the companyist compromise, financialization facilitated closer alliance between managers and shareholders, which resulted in higher attention to shareholders' dividends rather than employees' remuneration (Yamada & Hirano, 2015, pp. 17-18). Furthermore, after the 1997 financial deregulation, Japanese stock market has been dominated by foreign investors. Since the latter have pursued financial rather than strategic interests, shareholder returns have become one of the important priorities for Japan's corporate governance (Uemura, 2002, p. 124).

Thus, the task of internal demand restoring is being carried so far through large corporations' support, in hope that lower yen exchange rate, government subsidies and deregulated financial markets would lead to their competitive advantage. New financial options can serve as a leverage for big actors with enough experience in financial operations (Hoshi & Kahyap, 1999, p. 19). The series of corporate governance reforms that started in late 1990s also aim at restoring the competitiveness of strategic export-oriented firms through the increased reliance on shareholders as new capital providers. However, big multinational companies constitute only minor part of Japanese labor market, leaving therefore the question of medium- and small-enterprises' performance open.

The bubble burst in early 1990s made large Japanese companies search for more liquid sources of finance than main banks, especially due to the experience of internationalization and capital accumulation during late 1980s. Notably, the background for change has been different from the postwar period when Japan adopted a path-dependent logic that led corporations to adopt internally isomorphic practices. The crisis of the postwar companyist compromise created a normative vacuum that business and political actors intend to fill by drawing from overseas successful experiences. Thus, the declared "convergence" with the Anglo-Saxon corporate governance model as the one centered on shareholders' rights might serve more to the goal of making Japanese corporations look more *homogenous* with their American counterparts "without necessarily making them more efficient" (DiMaggio & Powel, 1983, p. 147). This type of institutional isomorphism is called "*mimetic*". It often arises from organizational uncertainly (DiMaggio & Powell, 1983, p. 151). Differently from "normative", it is a "form of imitation through which actors react to uncertainty with regard to the effects of institutional rules… Imitation is motivated by disorientation rather than by conviction that the model to be imitated is superior. Since rational assessments for the best institutional design are unavailable, the success of institutions operating elsewhere provides legitimation for using them as templates" (Beckert, 2010, p. 158).

The pitfalls of mimetic isomorphism are evident on a micro-level. Japanese households did not increase their borrowing, despite being provided with better credit opportunities after 1985. This can be explained by traditionally high level of households' savings that have been also used by the state as source of corporate funding. Households' savings rate constituted 15 percent in the period of high economic growth between 1985 and 1990 and reached 23 percent in the middle of the 1990s (Itoh, 2000, p. 84). These rates were once the highest among industrialized countries but have plunged significantly in

early-2000s. Households' burden has been further exacerbated by recent sales-tax lifting from 5 to 8 percent, with the plans of a further increase to 20 percent by 2020 (Reynolds & Mogi, 2013).

Thus, the average Japanese consumption rate remains low. Also, pension programs have been financialized – in 2006 the Government Pension Investment Fund (GPIF), largest pension fund in the world, was created. As seen from the name, the word "investment" implies intensified spending through channeling into secondary market. Moreover, as the most recent news testifies, the further pension deregulation is on the way (Hodo & Hirata, 2013). Against this background, IMF (2011, p. 2) points at the necessity for leveling large corporate savings (that grew from 16 to 21 percent of GDP throughout 1991-2008 period) and small households' savings (that declined from 8 to 3 percent) (IMF, 2011, p. 6).

This chapter discussed the foundations of the postwar Japanese companyist compromise. It rested in two accords: "management-finance" and "management-labor". In the heyday of the Japanese economy during 1960s-70s, the cooperative relationship between management and labor made up the fundament of Japan's stakeholder model of corporate governance. It was contingent on the long-term support from partner banks, which relational supervision allowed managers to offer lifetime employment tracks for core employees. However, as large companies accumulated substantial wealth by early 1980s, they started to diversify their finance, increasingly relying on equity rather than debt. Subsequent revaluation of yen imposed further challenges on export-oriented enterprises. This has triggered changes in labor policies, whereby companies increased the hiring of nonregular employees and limited the number of permanent positions. They became more eager to resort to downsizing as a mean for attaining higher competitiveness at the international level. Starting from 1990s – the so-called "lost decade" – labor costs have been increasingly lagging behind productivity increments. In turn, higher priority has been given to corporate shareholders that have been outweighing main banks as major providers of corporate capital. Thus, the "management-finance" compromise has raised above the "management-labor" compromise along the hierarchy of corporate priorities. The elevation of finance over cooperative HR policies can also be viewed as an introduction of shareholder model elements into the stakeholder institutional setting. The series of corporate governance reforms discussed in the next chapter have been the epitome of this process.

Chapter 4: Corporate Governance Reforms as a Political Economic Project

This chapter discusses the series of corporate governance reforms in Japan that have fared from the late-1990s. Although, judged by formal criteria, the reforms have had a minor effect on the way the Japanese listed companies are being run, they have nevertheless notably impacted the mindsets of local managers. Below, I analyze the major corporate governance legislations and trace their discursive patterns. I view the reforms as a political economic project, largely promoted by the Japanese government and foreign investors. While the reforms started as a voluntary initiative, their articulation has been ever more persistent – up to the point of the mandatory adoption of at least two outside directors, as outlined in the 2015 Corporate Governance Code. As the Japanese corporate governance is still a case of a stakeholder model, the ongoing reforms have contributed to the enhancement of shareholders' rights, and, thereby, facilitated incremental institutional change.

4.1. Institutional Context for Corporate Governance Reforms

The lasting economic crisis has changed the corporate discourse in Japan, so that it started to underline the importance of global standards of corporate governance for publicly traded companies. "Global standards" mostly consider the *shareholder* model of corporate governance as normative. It mainly consists of the enhancement of board independence and managerial accountability in front of shareholders (OECD, 1999). Approached in a stylized manner, contrary to the shareholder model prevalent in Anglo-Saxon world, the *stakeholder* model, peculiar to Japan and a number of continental European countries "provides employment at decent wages, producing safe and reliable products at reasonable prices, contributing to local communities and making economies grow by promoting innovation, increasingly in dialogue with government officials" (Dore, 2008, p. 1102-3).

Stakeholder model features are the predominance of debt finance, concentrated stockholding and "tightly interconnected networks among firms, their trading partners, and financial institutions" (Noda, 2013, p. 369). Stakeholder model is also strategically-oriented, as it seeks to achieve sustainable corporate growth – not only higher profits. It is concerned with "a variety of firm constituencies – including employees, suppliers and customers, and the communities companies are located in – enjoy 'voice' in the firm and whose interests are to be balanced against each other in management decision-making" (Vitols, 2001, p. 337). This view is different from the shareholder model that postulates

that a joint-stock company belongs to its "owners" – shareholders, and thereby its utmost task is the maximization of share value. It is also characterized by disperse shareholding and equity finance. Notably, corporate governance reforms that started in Japan with the 2002 Commercial Code reform, have aimed to incorporate some principles of shareholder model into the local context. In this respect, VoC can be helpful in addressing the possible issues of convergence and hybridization.

Tracing the parallels between national and corporate governance, the stakeholder model implies the utmost importance of a "sovereign" aspect (ethical principles of social servitude) of the firm, whereas the shareholder model reflects the preoccupation with commodified factors such as earnings per share and return on investment (Jackson & Carter, 1995, p. 878). The 1980s' neoliberal shift in the Anglo-Saxon world induced a utilitarian transformation of the "economically inefficient" stakeholder system into a shareholder one. Thereby, the dominant discourse of corporate governance has become centered on the agency approach. It is also called the "principle-agent" approach, whereby managers (agents) fulfil the will of shareholders (principals). In this model, the actions of managers that do not translate into shareholder returns are called "agency costs".

This matters due to the fundamental differences in the structure of social relations at a Japanese workplace compared to Anglo-Saxon context. The former would not satisfy basic assumption of agency theory about the self-maximizing nature of managers and respective firm units that should therefore be checked by means of coercion and compete with each other (Alchian & Demsetz, 1972, p. 795). Though generally lacking outsider supervision, Japanese directors are known for their empathy towards employees and dedication to long-term corporate goals (Ahmadjian & Okumura, 2011). The resulting cultivation of community firm values often means lower returns to shareholders (Miyajima & Nitta, 2014).

On the other hand, resonating with the agency approach, the shareholder model considers managers as interest-seekers who cannot be trusted and thus need close outside supervision ideally carried out by market forces (Lazonick & O'Sullivan, 2000, 16). Shareholder do not necessarily intervene directly with management at annual general meetings. Rather, the main source of subjugation is compulsory disclosure of accounting information that provides investors with corporate prospects. Incentives such as stock options and premiums are called to connect share value returns to CEOs remuneration and employment guarantees. Hence, as in the case of Bentham's "panopticon", managers learn to discipline themselves even in the absence of the eye of the beholder, however, under a

constant fear of a hostile takeover or a plunge in stock prices (Roberts, 2001, p. 1553). Miyajima, Hoda & Ogawa (2016) have observed that in Japan, "one standard deviation increase (decrease) in shareholding (5%) is associated with a 10% rise (decline) in stock returns. Top management's greater concern with stock price is reflected in the increase in IR activities and information disclosure since 2000" (p. 17).

There is a substantial difference between ethically motivated accountability under shareholder model and self-imposed discipline resulting from market pressure. The former is caused by blurred lines between execution and supervision. In this situation, CEOs are not threatened by immediate sanctions in case of occasional misconduct. Hence, they are more inclined to build lasting horizontal networks with stakeholders such as employees and cross-shareholders (Tanaka, 2014). The latter case, on contrary, results from the lack of trust that shareholders have towards CEOs, whose actions are *a priori* perceived as agency costs. Therefore, managers choose an option of share value pursuit, often at the expense of other stakeholders, to prevent shareholders' interference potentially leading to dismissal of incumbent CEOs because of poor financial performance. Thus, described cases rest on two different societal foundations, meaning that corporate governance model is embedded into national context and its reform requires broader institutional analysis.

The drift towards the shareholder model is possible under certain institutional conditions that include individual participation in the stock market as well as the dominant role of equity funding for the national economy (Jürgens, Naumann & Rupp, 2000). According to the World Bank (2016), the market capitalization of Japanese listed companies is one of the highest among developed countries, accounting for 118.7 percent of GDP (Figure 2). On the other hand, as shown in Figure 3, according to the Tokyo Stock Exchange Shareownership Survey (TSE, 2016), individual stock-holding in Japan has been consistently decreasing since the 1970s, currently accounting for 17.5 percent. In contrast, nowadays the largest portion of stock is held by foreign investors (29.8 percent).

Following the direction of Miyajima (2014), the survey infers that stock-market activity in Japan is spurred by "outsiders" represented by "foreigners". On the other hand, high rates of stock-holding by such "insiders" as trust banks (18.8 percent – included in the "financial institutions" category) and business corporations (22.6 percent) illustrate the lasting legacy of cross-shareholding and adherence to bank finance. Thus, applying the criteria of Jürgens, Naumann & Rupp (2000), we are able to conclude that the role of equity finance for the Japanese economy is growing, which is largely due to the activity of foreign investors. At the same time, insiders have a decisive voice in the governance of companies.

Hence, while the reputational role of market-oriented shareholders grows, they face institutional impediments to directly exercise their monitoring rights.

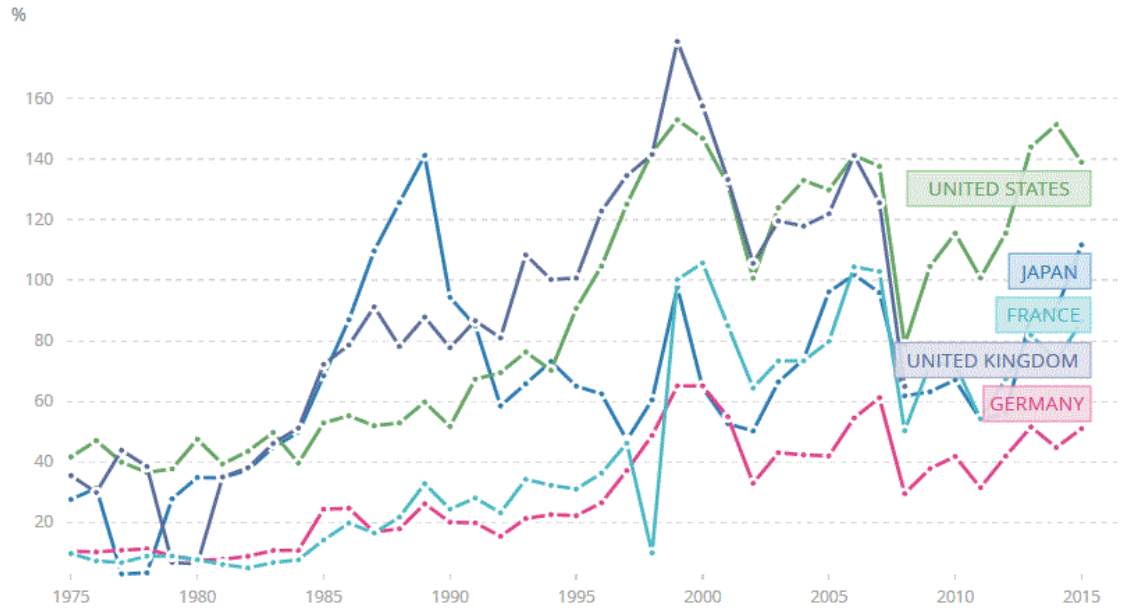

***Figure 2**. Market capitalization of listed domestic companies (% of GDP) (World Bank, 2016)*

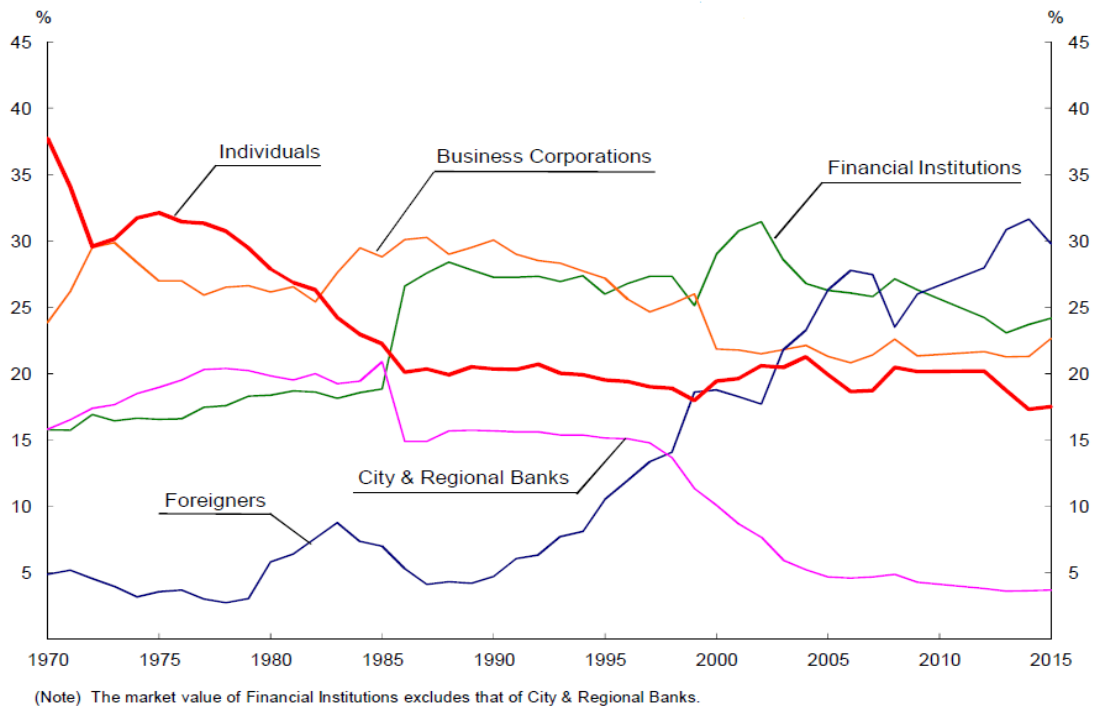

***Figure 3**. Distribution Percent of Market Value Owned by Type of Shareholder. Source: Tokyo Stock Shareownership Survey (2017)*

On the micro level, Japanese households are mostly unwilling to entrust their savings to financial markets. Despite low interest rates they prefer to hold their money as deposits. As a result, their private funds have traditionally supported the entrenched compromise between banks and corporations. In contrast, stockholding has been associated for them with certain risks. According to Aoki (1988, p. 123), "there was on average about a 25 percent chance that individual investors would incur a loss from holding portfolios proportional to the market portfolios over a year". Furthermore, the broker's fee charged by securities companies was rather high, and so was collateral for bond issuing. High commissions on stock trading remained until the 1998 Big Bang launch. In addition, "a range of activities including stock options trading by individuals, over-the-counter trading of equity related derivatives, and trading non-listed stocks through securities firms were prohibited until December 1998. So, prior to the Big Bang it was very costly for individual investors to participate in capital markets directly" (Hoshi & Kashyap, 1999, p. 18).

Amid the growing influence of financially oriented investors and losses incurred by Japanese companies because of the bubble burst, firms have been willing to reform their governance by enhancing accounting transparency and encouraging more active involvement of shareholders. On the other hand, diminishing but still high levels of cross-shareholding and reluctance of average Japanese to participate in stock market have created a rigid institutional environment for the potential establishment of market for corporate control. As a result, corporate governance reforms in Japan have taken a path of incremental change following existing institutional patterns.

4.2. Statutory Auditor ("Kansayaku") System

The traditional Japanese corporate governance model called "statutory auditor" (*kansayaku*) originated in the first Japan's Commercial Code (JCC) that was drafted in 1899 in general accordance with German corporate law. *Kansayaku* is an outside shareholder that monitors board of directors' activity, but is not a part of an executive board. During the US occupation in the postwar period, the JCC was amended in a way that transformed *kansayaku* into a formal body whereby Japanese firms' management was monitored by the board of directors after adoption of the Commercial Code in 1950. This was in line with the separation of management from shareholding and, respectively, holding companies' prohibition. The parallel audit was undertaken by partner banks, which were embedded in the centralized main bank system (MBS) and connected with corporations by cross-

shareholding ties. The latter were, however, symbolic, since both corporations and banks were linked by long-term mutual commitments as members of *keiretsu*[8] unions. From 1974 on the *kansayaku* function has been re-established. Eventually, the 1993 JCC amendment made it obligatory to have at least one outside statutory auditor (Lee & Allen, 2013, p. 5).

The *kansayaku* model is described as a "unique dual monitoring system" (Araki, 2005, p. 30), since it allows for the existence of both supervisory board and statutory auditor (Figure 4). Although this system has been formally based on German civil law, the major difference between two models is that the Japanese auditor bears consulting functions, and thus does not challenge managerial decisions. The German analogue, on contrary, has to represent the employees" position, whose voice is also present within the board of directors[9].

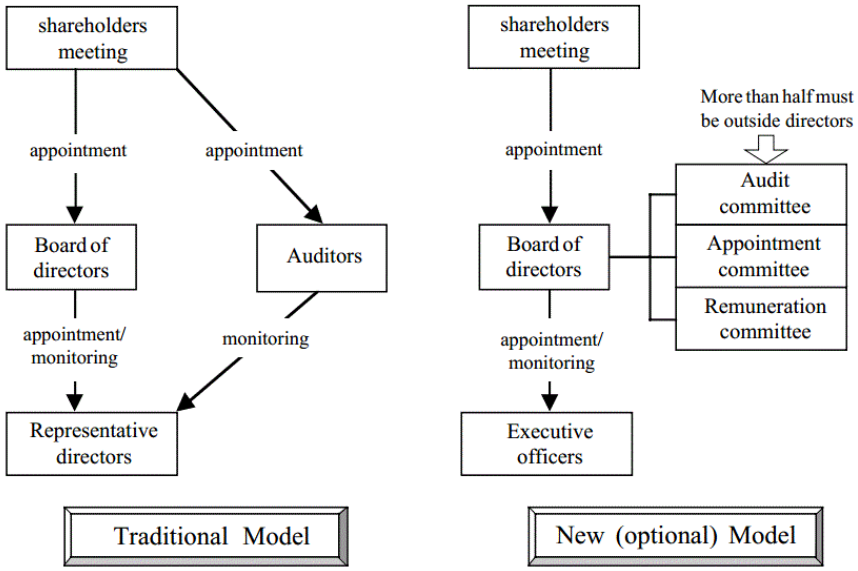

Figure 4. *Two Competing Governance Models (Araki, 2005, p. 31)*

The corporate governance reforms starting from 2002 were explicitly based on the "statutory auditor" (*kansayaku*) system. The 2005 Companies Act formulated a requirement for large companies to have at least three statutory auditors, the majority of which must be outsiders (OECD, 2011, p. 61). Though formally complying with this requirement, in reality that "independent" majority is highly dependable upon internal

[1] Large enterprises peculiar for their cross-shareholding with subcontractors and links with partner-banks coordinated by the Bank of Japan (Westra, 2003, p. 365)

[2] Taking employees' interests into account according to industry-based regulations in German case is referred to as "labor-management codetermination" (Whittaker & Deakin, 2009, p. 4).

corporate policies. Thus, so far, the emerging regime, promoted from above, has had effects different from those expected by the government due to the entrenched nature of Japanese institutions known as "community firm" (Inagami & Whittaker, 2005)[10].

At the same time, enterprise actors themselves have realized the definite pace of shareholder rights' enhancement. This has been apparent due to the gradual reformation of the board of directors from insider-dominated towards one influenced by outside representatives. "The measures show that the statutory auditor system has been flexible enough to realize some of the benefits of the committee system without having to fully adopt it" (Waldenberger, 2015, p. 15). In this respect, *Keidanren* – the Japan Business Federation – has stressed the foundational role of corporate ethics that can preserve an existing corporate order (Nippon Keidanren, 2009, p. 13).

At the end, a contradiction arose between the governmentally declared aims to promote shareholder-oriented corporate governance, and the views of conservative Japanese business actors. Internal reports on corporate governance mention that "Japanese firms have hitherto tended to have other objectives than the simple maximization of shareholder value, but by and large they start from the assumption that the *raison d'être* of business firms is much the same the world over" (Dore, 2000, p. 71).

On one hand, the growing emphasis on the *kansayaku* as outside agents of change showed the consensus over reforming the malfunctioning inward-oriented system. On the other, the fact that the reforms' seed was planted into the old soil demonstrated the longevity of the dual monitoring system. Thus, existent institutional checks induced managers and shareholders to search for a new regime of coexistence that would account both for the growing role of outsiders' expertise and for the common interests of managers and employees in the Japanese "community company".

4.3. Board Reform

Before the actual corporate governance reforms' kickoff, some companies made steps to improve their performance through incremental changes. One of such initiatives was an introduction of a so-called executive officers (*shikkō-yakuin sei)* called to optimize

[3] The segment of Japanese labor market represented by large corporations is constituted by three pillars described in the OECD report (1973). These major organizational standpoints are: lifetime employment (*shūshin koyō*), seniority wage system (*nenkō joretsu*) and enterprise unions (*kigyō-betsu kumiai*). Such favorable policies towards permanent employees are related to stable shareholding: "The J-firm is a *coalition* of the body of stockholders and the body of employees, integrated and mediated by management, which acts to strike a balance between the interests of both sides" (Aoki, 1988, p. 101).

the work of the board by separating executive and monitoring functions. Traditional Japanese boards usually encompassed all unit managers, for whom the promotion to director was a major career incentive (Dore, 2007, p. 374). Thus, Toyota's board, for example, consisted of a record 58 member. Decision-making at such numerous boards was not effective. In turn, most of the procedures were adopted during smaller-format meetings between vice-presidents with CEOs called *jomukai* (Dore, 2007). To underline the task of performance-achievement for every unit, reformist companies delegated executive functions to the group of CEOs comprised of former lower-status directors (Miyamoto, 2017, p. 8). The remaining non-executive directors constituting a new board became much fewer under this model but have got real monitoring credentials that could therefore correspond to formally declared functions of the board. "The board of directors would supervise the business and maintain a holistic outlook on business strategy, while the *shikko yakuin* would pay attention to the operational aspects of business" (Ahmadjian, 2002, p. 71).

The reforms were pioneered in 1997 by Sony and some other firms with relatively large proportion of foreign stockholding (Shishido, 2007, p. 313). By 2005, nearly half of the listed companies adopted the *shikko yakuin* system. Resorting to this step, Sony reduced its board from 38 to 10 members (Ahmadjian, 2002, p. 71). Arguably, this voluntary move laid foundation to the subsequent 2002 Commercial Code reform, which "institutionalized the executive officer system" (Colpan, Yoshikawa, Hikino & Miyoshi, 2007, p. 99). The underlying aim to separate execution from monitoring could be substantiated by the inclusion of outsiders to the board. However, in practice, supervising directors largely remained insiders. Hence, the task of impartial monitoring has been compromised by the reluctance of Japanese listed companies to appoint independent directors (Ahmadjian, 2002, p. 72). Moreover, as the promotion of managers to board members used to be a part of *nenko joretsu* – senior-merit system – the board size reduction could be interpreted as a move toward more performance-oriented system (Ahmadjian, 2002, p. 73).

4.4. 2002 Japanese Commercial Code Reform

The 2002 JCC reform, brought into effect in April 2003, allowed large public companies "to allow outside directors to gain control of the board of directors through committees" in a US-like manner through a "three-committees system" (Itami, 2005, p. 4). Accordingly, the governmental aim has been to promote shareholder governance.

Moreover, contrary to the pre-1990s' restrictions for corporate stockholding by foreigners, the new legislation aimed at paving a more open way of governance. One of the reasons for the pressure extended to local listed firms, particularly from 1990s onwards has been an ever-growing proportion of foreign stockholding in Japan. It reached a record 31.7 percent at the end of 2014, surpassing the holding ratio of 27.4 percent by domestic financial institutions (TSE, 2015). Hence, foreign actors have largely initiated the push towards more transparent shareholder-oriented corporate governance.

The very idea of outside directors holding a majority in the committees and thereby influencing the board of directors originated from Anglo-Saxon corporate governance practices that underline the importance of corporate disclosure and the leading informational role of market indices. The reforms of Japanese corporate governance have been promoted under the supervision of the American Chamber of Commerce in Japan (Poe, Shimizu & Simpson, 2002, p. 75). Initiatives such as the committees' introduction have been directly influenced by the US legislature like 2002 Sarbanes-Oxley Act. According to foreign investors' view, "supervision should be separated from execution to promote objectivity" in accessing managers' performance (Buchanan, 2007, p. 29). In contrast, the Japanese institutional logic has enhanced a "community firm" that implies primacy of contingent governance or internalism (Aoki, 1994). Respectively, executive directors often act as monitors. That is why, until now, many firms have been less eager to introduce separation of execution and monitoring.

Formally, by 2018 only 2 percent of firms listed on the Tokyo Stock Exchange adopted the committee system (TSE, 2018). In general, the US-based model was applied in a highly selective way, with stock-prices not being significantly affected by the committees' introduction (Gilson & Milhaupt, 2004, p. 39). Even in those companies that agreed to adopt the committee system, outside directors are often appointed by the firm's CEOs. As a result, while being formally an independent auditor, an outside non-executive director is likely to feel obliged to the company that hired him for the expressed trust (Buchanan, 2007, p. 31).

The moderate pace of the 2002 Commercial Code Reform implementation within Japanese corporate milieu can also be viewed as a process of a starting institutional transformation. It is reflected in high numbers of firms that chose a path of a gradual change – to appoint outsiders to the board of auditors. By 2016, 97.2 percent of Tokyo Stock Exchange first section companies elected outside directors into their supervisory boards – a rapid progress compared with 31.6 percent in 2010 (JACD, 2016, p. 4). In the case of

companies with a traditional statutory auditor system, this action was voluntary, and mostly caused by market reputational concerns (Shishido, 2007, p. 322).

Another important legislation for Japanese corporate governance was the 2005 Companies Act that systematized firm's management and monitoring issues. From the point of legislative modification of Japanese corporate governance, the 2005 Companies Act that "separated corporate law from the Commercial Code" (Shishido, 2007, p. 328) was the most significant. Though few legal innovations were introduced by the 2005 Act, this codification of desirable corporate governance practices with stress on outside monitoring (Goto, 2013, p. 24) was an important institutional change.

The governmental and foreign-investors' push towards the shareholder model has been motivated by the claimed lack of managerial responsiveness towards investors' demands. From the institutional point of view, the automatic transformation in favor of the outside "committee system" would bear obvious risks. These are due to the fact that outside observers by definition lack information concerning corporate affairs. Therefore, their disciplinary action could interfere with firm's ethical context and thus impede its proper functioning. However, in spite of the low proportion of the firms that switched to the committee system, the numbers of outside directors are growing. Even though non-executives did not form a majority in their committees, the mere reputational role of their presence marked the growing institutional recognition of the market for corporate control.

4.5. "Comply or Explain" Principle

Institutional flexibility inscribed into the 2002 Commercial Code has allowed for a choice between statutory auditor and committee system. Throughout early 2000s, the government allowed the decision of whether to adopt the new scheme of corporate governance to be made by the listed companies. However, on the discursive level, the market-based regime of veridiction has been promoted with ever-increasing intensity. It was reflected in the implementation of the "comply or explain [the non-compliance]" principle by the largest stock exchange in Japan, Tokyo Stock Exchange (TSE, 2004, p. 23).

The policy of underlying shareholders' interests, present in the "Principles of Corporate Governance for Listed Firms" formulated by the TSE in 2004, was left unchanged in the analogous 2009 document (TSE, 2004, p. 7; TSE, 2009, p. 5). At the same

time, the moderate pace of corporate reform implementation left the "comply or explain" principle intact (TSE, 2009, p. 12).

The reason why the introduction of the committee system has remained voluntarily until the present is the lack of institutional compatibility with shareholder-oriented policies described above. However, as presented in the TSE paper (2013, p. 5), such compatibility is likely to grow with the increasing proportion of foreign stockholding (Figure 5). The reverse tendency also holds true. Under reputational pressure for disclosing corporate affairs, some firms with low foreign shareholding, like Daiwa Securities and Ito-Yokado, chose to terminate their listed status (Jackson & Miyajima, 2007, p. 12).

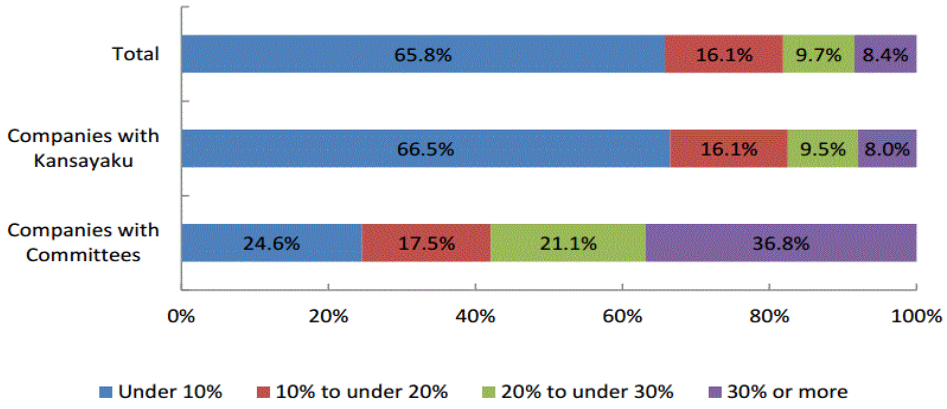

***Figure 5**. Foreign Shareholding Ratio (TSE, 2015, p. 6)*

For the companies that opted to continue their listing at the TSE, there have been no binding sanctions for the non-compliance with the 2002 Commercial Code requirements, mainly, the appointment of non-executives' majority to the board. The requirements have been somehow severed recently, with the 2015 Japan's Corporate Governance Code (JCGC) specifying the mandatory appointment of the outsiders' majority to the *kansayaku* board (JCGC, 2015, p. 26) as well as the presence of at least two independent directors (JCGC, 2015, p. 27). In practice, however, *kansayaku* carry merely advisory functions, with the same holding true for independent directors' minority.

Whereas legal provisions do not effectively stimulate the departure form relational monitoring, the ever-growing disciplinary role is being played by market evaluation (Goto, 2013, p. 24). With market authority becoming ever more apparent, even those managers less eager to implement corporate governance reforms have been increasingly associating their own performance with stock indices (Jacoby, 2005, p. 61). Thereby, the "power of

numbers" has exercised the reputational pressure on corporate managers, inducing them to impose discipline over themselves in order to reward shareholders. At the same time, this self-imposed transformation has been carried out within the old institutional lines of the *kansayaku* rather than the committee-system.

4.6. 2013 Japan Revitalization Strategy: Promoting Entrepreneurship

By giving evaluation authority to market, the reforms of Japanese corporate governance have aimed at empowering managers-entrepreneurs. In order to enhance such framework, it is necessary for government to turn completive motivation into institutional rationale for listed companies. This has become an explicit case of the 2013 Japan Revitalization Strategy (JRS) implemented as part of Abenomics policies under the "structural reforms" (so-called "third arrow") title. "Although both loose monetary policy and expansive fiscal policy can work as economic stimulus measures, they cannot facilitate proactive corporate management or the greater growth potential of the entire Japanese economy. The attitude of risk-taking corporate management is essential to raise potential growth rates" (Kojima, 2014). The shareholder-based view on a firm's main task as profit-maximization has also been set by the JRS that calls for "implementing specific measures to improve companies' earning power" (JRS, 2014, p. 6).

An attempt to instill entrepreneurial motivation is not only due to shareholders' demand, but also because of Japan's macroeconomic strategy aimed at seizing equity-market opportunities. Currently, as envisaged in the JRS, the country's recovery after the crisis is largely dependent on the corporate sector. From the government perspective, the ability to compete globally and discover new markets is inseparable from managers' capacity to act like entrepreneurs, hence – to take risks.

Japanese structural reforms reverberate in the 2014 IMF working paper "Unstash the Cash! Corporate Governance Reform in Japan" (Aoyagi & Ganelli, 2014). It is noted there that Japanese companies tend to hoard cash, rather than invest. Prioritizing savings over investment is a prevailing feature of Japan's corporate governance. Due to this fact, the IMF emphasizes the role of outside directors that can contribute to corporate management's dialogue with shareholders. Unlike CEOs promoted to board members, outside directors might not possess thorough firm-based knowledge. However, they are likely to take risks more frequently and to enhance control based on stochastic market discipline.

The introduction of the JPX-Nikkei 400 index in 2014 was expected to foster the alignment of shareholders' and managers' interests. The constituencies of the newly created index are companies that relatively succeeded in enhancing their shareholder value through introduction of outside directors (Miyajima & Nitta, 2014). JPX-Nikkei 400 index is composed of "companies with high appeal for investors, which meet the requirement of global investment standards, such as the efficient use of capital and investor-focused management perspectives" (JCGC, 2015, p. 2).

Thus, listed firms are likely to view other companies as rivals and strive to raise their share value by inclining towards riskier behavior to secure short-term profits. Such "downsize and redistribute" strategy (Lazonick & O'Sullivan, 2000) already has noticeable repercussions for those labor segments not protected by existing institutional arrangements (Labour Force Survey, 2016).

4.7. JCGC and Japan's Stewardship Code: "Two Wheels of the Cart"

Formally, listed firms were given the possibility to adopt an alternative corporate governance system by the 2002 Japanese Commercial Code (JCC) amendment. However, already in 2005, the principles of firm management and monitoring present in a dispersed way in the JCC were systematized and transferred to the Companies Act. In addition, important notions of "outside" and "independent" director and auditor were further specified[11]. The Companies Act serves as a major guidance for Japanese companies till nowadays. This document was amended in 2014 with a purpose of making the compliance with the previously introduced monitoring system more binding. The respective "comply-or-explain" principle is called to exercise reputational pressure over those companies that chose to stay with old inward-oriented schemes (Sakamoto & Harima 2014).

The insider system pertaining to Japanese firms implies tightly institutionalized relations at a workplace. It is a consequence of the lasting tradition of lifetime employment.

[11] ""Outside Director" means a director of any Stock Company who is neither an Executive Director (…) nor an executive officer, nor an employee, including a manager, of such Stock Company or any of its Subsidiaries, and who has neither ever served in the past as an executive director nor executive officer, nor as an employee, including a manager, of such Stock Company or any of its Subsidiaries; "Outside Company Auditor" means an auditor of any Stock Company who has neither ever served in the past as a director, Accounting Advisor (…) or executive officer, nor as an employee, including a manager, of such Stock Company or any of its Subsidiaries" (Companies Act, 2005, pp. 3-4).

2014 amendment adds to this that "directors, executive officers, and other employees of a parent company, executive directors, executive officers and employees of a sister company, and close relatives of directors and executives of the company would no longer be eligible [or qualify] as outside directors and audit and supervisory board members" (Matsunami & Sugihara, 2014, p. 120).

Japanese corporate culture makes it almost a definite rule for supervisors to be senior to subordinates. “In any age cohort, perhaps – in large companies with Boards of 40 or more – three or four may get to the Board in their early fifties, but only one from two or three adjacent cohorts will make it to the top. Someone likely to abuse power for personal ends is not likely to be that person” (Dore, 2000, p. 80). Thus, it will not be realistic for the Japanese institutional context to require the supervisory board be independent. For, such provisions ought to account for societal attributes of the potential outside directors.

While promoting shareholder value orientation, the 2015 Corporate Governance Code (JCGC) also incorporated the strategy of incremental change: “The board and the management should exercise their leadership in establishing a corporate culture where the rights and positions of stakeholders are respected and sound business ethics are ensured” (2015, p. 8). Mentioning of “corporate culture” and “business ethics” are quite important. Even though the JCGC has an advisory character, its principles are to be incorporated by the Tokyo Stock Exchange (TSE). Hence, listed companies have no other way except to comply with the provisions or explain the abstention. In this regard, the following passage from the Code holds merit: “The Code asks companies to examine whether there are issues in their corporate governance in light of the aim and spirit of the principles of the Code, and take self-motivated actions in response to those issues” (JCGC, p. 4).

In its discussion paper, *Keidanren* has also been expectedly preoccupied with the question of “how to build a corporate management structure oriented towards the long-term growth of corporate value” (Nippon Keidanren, 2009, p. 2). This, according to *Keidanren*, can only be enhanced through addressing the importance of a stakeholder model. The formal right to equally respect shareholders’ rights is also acknowledged by the OECD: “The corporate governance framework also depends on the legal, regulatory, and institutional environment” (OECD, 2004m p. 12). *Keidanren* also stresses the foundational role of corporate ethics that can determine the quality of monitoring, irrespective of the corporate governance model concerned. “It is important for accounting auditors to be thoroughly imbued with professional ethics and for *Kansayaku* to support that through the exercise of their authority” (Nippon Keidanren, 2009, p. 13). However, amid intensified international competition and growing pressure coming from foreign investors, shareholders become prioritized over other stakeholders.

The accountability of corporate management in front of shareholders is not considered a one-sided practice. Providing the fact that, on average, the stockholding composition of Japanese listed companies is diverse, it is logical for firms to require

guarantees from their institutional investors. In this regard, "Japan's Stewardship Code, published in February 2014, [serves] as an important momentum builder for rebalancing in favor of shareholders as investors enhance their monitoring of investee companies" (Miyajima, 2014). Accordingly, for Japanese corporate governance, Japan's Stewardship Code (JSC) and JCGC are called to be the "two wheels of the cart" (JCGC, 2015, p. 4). Acting in line with 2013 (2014) Japan Revitalization Strategy, the Code calls upon institutional investors "to fulfill their fiduciary responsibilities, e.g. by promoting medium- to long-term growth of companies through engagements" (JSC, 2014, p. 1). Thus, strategic aims are considered more important than short-term aims both for management and for shareholders. In other words, unlike companies monitored by shareholders directly, Japanese listed firms aim at keeping distance from outside investors, thereby avoiding the separation of execution from monitoring. "The Code does not invite institutional investors to interfere with the finer points of managerial matters of investee companies" (JSC, 2014, p. 2).

4.8. Alternative Forms of Corporate Organization

Since the initial impetus of the 2002 Japanese Commercial Code – to introduce "companies with committees" system – was realized only by only 2.2 percent of listed companies (TSE, 2013, p. 15), this was an incentive for another institutional compromise to be found. Eventually, it took the form of an alternative corporate organization – "Company with an Audit Committee"[12], introduced in the revised Companies Act in 2014 (Matsunami & Sugihara, 2014, p. 119). "It provides a kind of golden mean between the two former solutions. The audit and supervisory committee is less powerful than the audit committee in the company with committee structure, but members are fully equipped with director rights and therefore have more influence than the traditional statutory auditors" (Waldenberger, 2015, pp. 14-15). Thus, to some degree, while functionally complies with demands to adopt outside directors, this system leaves two crucial committees, appointment and remuneration controlled by insiders.

Here, it would be interesting to trace parallels with German corporate regulations. Its Commercial Code states that "the obligation of the Management Board and the Supervisory Board [is] to ensure the continued existence of the enterprise and its

[12] It is sometimes referred to as "audit and supervisory committee" (Nakamura, 2014), or "audit/supervisory committee" (Whan et al., 2014), or "Audit Etc. Committee Establishment" (Sakamoto & Harima, 2014), or "companies with audit and oversight committees" (JCGC, 2014).

sustainable creation of value in conformity with the principles of the social market economy (interest of the enterprise)" (JCGC, 2014, p. 1). Contrary to shareholder model of corporate governance, a German listed company is viewed as an entity that has to account for its various stakeholders: primarily, by granting employees the right of being represented in the Supervisory Board (JCGC, 2014) and by acting in accordance with company's institutional principles. This relates German and Japanese visons of a corporation, as being not only a mean towards satisfying shareholders' rights, but also an end concerned with social welfare of its constituencies.

For Japan, apart from associating the committee structure with a drift towards shareholder-based monitoring, there is another way to view the possible transformation from the institutional standpoint. As discussed above, Japanese listed companies are mostly disciplined by long-term commitments of their stakeholders. In contrast, US corporate management tends to be disciplined by the possibility of hostile takeovers. Hence, while formally adopting a US-like model of corporate governance, Japanese firms are likely to protect their corporate from direct outside interference. This does not mean that local listed firms refuse to recognize market legitimacy. Rather, those companies are envisaging the role of outside directors as mediators between internal managers and institutional investors. In this regard, their anti-takeover measures seem to satisfy the following OECD principle: "Anti-take-over devices should not be used to shield management and the board from accountability" (OECD, 2004, p. 36). The motivation of anti-takeover measures for Japanese listed companies can be analyzed with the help of the following example.

The 1997 revision of the Antitrust Law allowed stock options for firms, thus lifting the 1947 ban for holding companies' creation. The latter was further simplified by the stock swaps' introduction in 1999 (Shishido, 2007, p. 317). Holding companies formally resemble prewar *zaibatsu* that were managed by respective family-owners (Okazaki, 2004, pp. 398-9). They have "a group structure consisting of subsidiaries governed by a parent company that has its own core business" (Shishido, 2007, p. 316). Currently, as increasing pressure is being put on the notion of "external" – in regard to directors or *kansayaku* – firms might consider it more feasible to adopt the "audit and supervisory committee" system, firstly due to a simple calculation. Under the statutory auditor system, the minimum number of outside monitors is "two-plus-one": at least two in order to form a majority in the *kansayaku* board plus one outside director (whose appointment is not mandatory (TSE,

2013, p. 22) but is considered as a necessary reputational asset for the listed companies[13]). On the other hand, "audit and supervisory committee" system can get along with just two outside directors, providing that they constitute the majority in the committee. Secondly, the outside members of the committee can be employees of a holding company, which would make the monitoring of its constituencies legal. Such scheme would resemble *zaibatsu* governance, with shareholding and management being inseparable. TSE considers this case in particular: "With the recent development of forming a group of companies through the use of a holding company, etc., it is important for a listed company to ensure corporate governance of not only the parent company, but also the corporate group as a whole" (TSE, 2009, p. 3).

On one hand, some firms with a sound vertical organization have found the holding-company structure to be applicable to their institutional context. Sako (2007, p. 420) analyzes the case of Softbank, the Japanese telecommunications and Internet Corporation – as an example of a successful introduction of such structure. On the other – those firms with diversified portfolios that did not have coherent coordination between headquarters and various departments faced difficulties while adopting this model. This was the case of NTT – another telecommunications company (Sako, 2007, p. 421). The reason why it pursued the reforms despite the structural conflict was the fear of possible hostile takeovers that would undermine the corporate community. However, the proportion of firms that voluntarily adopted the holding company structure was not high by the mid-2000s (Shishido, 2007, p. 317). For, such model still presupposes cross-divisional consolidation in a form of a friendly merger. As a result, contextual, tacit dimension pertaining on a shop floor within a department would be subject to changes.

The possibility for Japanese companies to use the reforms not merely to ensure shareholders' rights but to reinforce the prewar *zaibatsu* structure has been debated intensively. "Those who opposed the [1997 Anti-Monopoly Law] revision stressed the danger of a *zaibatsu* revival, while those who were for it, denied the possibility of such a revival" (Okazaki, 2001, p. 243). If the idea of a holding company structure reintroduction gains popularity, this would be an evidence of institutions carrying their peculiar aims, and flexibly adjusting their functions to legal changes. In a somehow emphatic manner the *Economist* (June 6th, 2015) concludes the following: "Before the second world war Japan

[13] Japan Revitalization Strategy functions in line with the aim "to impose accountability on companies having no outside directors" (JRS, 2014, p. 6).

had powerful shareholders, no insistence on lifelong employment and firms were able to lay off staff when times were hard. Forget 'Anglo-Saxon' capitalism. A revived Japanese sort could work just as well".

4.9. Summary

Although, according to the OECD (2004, p. 12), there is no "correct" model of corporate governance, in reality, the current articulation of a shareholder-value discourse in Japan leads to the establishment of market-led regime for corporate institutions that hitherto operated within inward-oriented system. Formal corporate deregulation in Japan has been accompanied with the strengthening of the juridical base for assuring management-investors reciprocity.

The message of this chapter is that the constitution of market as a disciplinary agency has been possible due to governmentally pushed enactments and the ever-growing proportion of foreign investors involved in Japanese stock trading. Due to the increasing weight of outside shareholders, it is becoming less possible for management to ignore their executive demands. Concurrently, large Japanese corporations tend to expand and thus render the participation in financial markets crucial. It is true that some managers also consider the alignment with shareholders as key to corporate success. However, there is a lack of institutional compatibility for the shareholder-value discourse in Japan to become a dominant corporate practice. Firstly, bank finance still plays a crucial role for firms, encapsulating long-term credit commitments and relational monitoring within the framework of the main bank system. Secondly, Japanese households' participation in financial markets remains very limited, which is explained by the decreased (as a result of the crisis) saving rates and the absence of an investment culture. At the same time, the "deviant" character of the shareholder model in Japan does not give us an excuse for ignoring its ever more persistent formal enforcement. The emerging model promoted by the Japanese government and foreign stockholders is claimed by agency theorists to reflect essentialist human nature manifesting itself under equitable market laws.

The recent transformations within the Japanese corporate governance realm give us at least two valuable lessons. Firstly, in spite of the actually slow pace of the reforms' implementation by the Japanese joint-stock companies, the shareholder-value discourse has been manifested in the managerial self-discipline conditioned by the motivation to compete with rival companies for a higher share value, especially within the newly established JPX-

Nikkei 400 Index. Secondly, although market for corporate control ideally requires arm's-length supervision, outside directors at Japanese firms have not been granted executive credentials as shareholders' delegates. Thus, on one hand, the local management tends to increase its transparency in front of institutional investors in the absence of a sovereign controlling instance, following the "panopticon" scheme. On the other hand, the reorientation of corporate performance towards shareholder value in Japan does not imply that companies in focus abandon their institutional foundations on the part of insider-based supervision. Thus, the combination of voluntary subjection to market discipline with the retention of relational monitoring make Japan a promising case for further critical institutional research.

The next chapter proceeds with another aspect of corporate deregulation, which is labor. Like the corporate governance reforms, labor transformations proceeded in a piecemeal way due to the strong institutional legacy, albeit the rules of the game have changed significantly compared to the postwar "companyist compromise".

Chapter 5: Intensified Labor Bifurcation

"*The legal and organizational changes affecting the governance structure of Japanese firms over the last decade, many of which have aimed to increase the intensity of external monitoring, have had very limited effect in promoting 'good' corporate governance. Rather, they have contributed to a shift in managerial objectives and priorities, specifically a downgrading of employee interests and an upgrading of shareholder interests*" (Dore, 2007, p. 370).

This chapter discusses the ongoing process of dualization between regular and nonregular employees that poses a significant challenge for the Japanese society and economy. It discusses the reasons and the dynamics of labor bifurcation by concentrating on the political aspect. Addressing the existing literature gap, the chapter explores the link between the corporate governance reforms and the surge in the proportion of nonregulars. Finally, it assesses the phenomenon of labor bifurcation as a departure from the postwar companyist compromise.

5.1. Introduction

In this dissertation, I define the nonregular employment in Japan in agreement with the explanation of Kambayashi & Kato (2013) that describe nonregular employee as the one who is not termed "*seishain*" or "standard employee". This classification is adopted according to customs of a working place and is therefore considered a *de facto* definition. There also exists a narrower *de jure* view of nonregular employment that refers to "secondary-segment workers… on fixed-term contracts" (Kambayashi & Kato, 2013, p. 5). According to this approach, nonregular employee is the one who is supposed to work less than 35 hours a week and have a limited contract (Rebick, 2005). However, there are two problems with this definition. Firstly, it does not accurately capture intermediate forms of work such as standard employment with fixed-term contracts (which is considered "regular") or non-standard employment with open-ended contracts (which is considered "nonregular") (Teruyama & Toda, 2017). Secondly, it is problematic to acquire data from employers on types of contracts and hours of work (Rebick, 2005, p. 58).

With the current proportion of nonregular employees in Japan reaching 37.2 percent – a tremendous surge compared with 15 percent in early 1980s (Figure 6) – this poses several social and economic challenges to the country (Labor Force Survey, 2017).

Nonregular employment should ideally aim at aiding the economy in times of crisis. Otherwise, flexible employees should have prospects of becoming regular employees. This is not the case in Japan, as the chances of this growing labor cohort to become full members of their companies are significantly lower, compared to other developed countries (Aoyagi & Ganelli, 2015). Flexibilization of labor is not a problem *per se*, if it exists in the environment with low labor turnover costs and representative unions, as in Nordic countries, also characterized by coordinated corporate governance (Witt & Jackson, 2016, p. 795). Contrary to that, Japan has not yet developed robust institutional mechanisms for protecting workforce not affiliated with a company on a long-term basis. Due to emerged gap between regular and nonregular employees, scholars observe rising poverty rate and wage insecurity leading to depressed domestic consumption, which deteriorates private sector accounts (Gordon, 2017, p. 10). Another social consequence for nonregulars that follows is a falling confidence in the future resulting in low degrees of marriage. This has wider repercussions by causing a plunge in birthrates (Gordon, 2017). Finally, as Japanese society ages, lower pay to precarious workers results in diminished social insurance contributions making elderly people more vulnerable (Osawa & Kingston, 2015, p. 58).

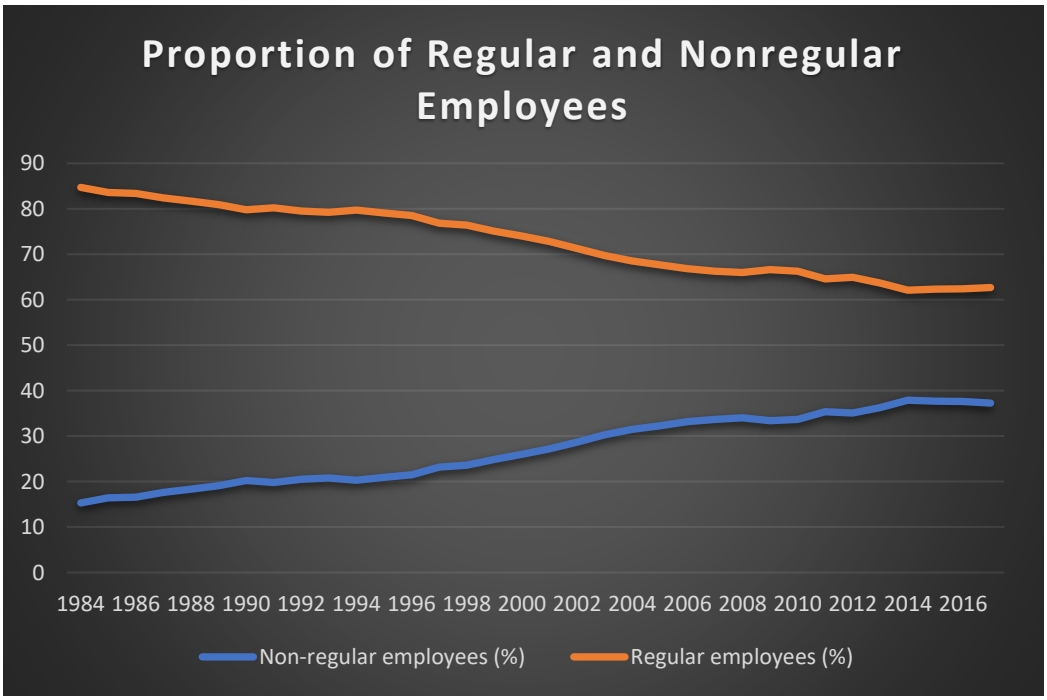

***Figure 6**. Proportion of Regular and Nonregular Employees. Source: Labour Force Survey (2017)*

Before 1984, when the share of nonregular employees in Japan was less than 15 percent, the voice of regular employees in the Ministry of Labor advisory councils (*shingikai*) could be considered as roughly representative of the whole labor segment. However, as temporary workforce has been growing steadily since early 1980s, when their numbers were 6 million, they have reached over 20 million in 2017 (Labor Force Survey, 2017). Nonregular camp is nowadays composed of following categories: part-time workers (49 percent), temporary workers / *arubaito* (21 percent), contract employees (14 percent), dispatched workers (six percent), entrusted employees (six percent) and others (four percent) (Labor Force Survey, 2017) (Figure 7).

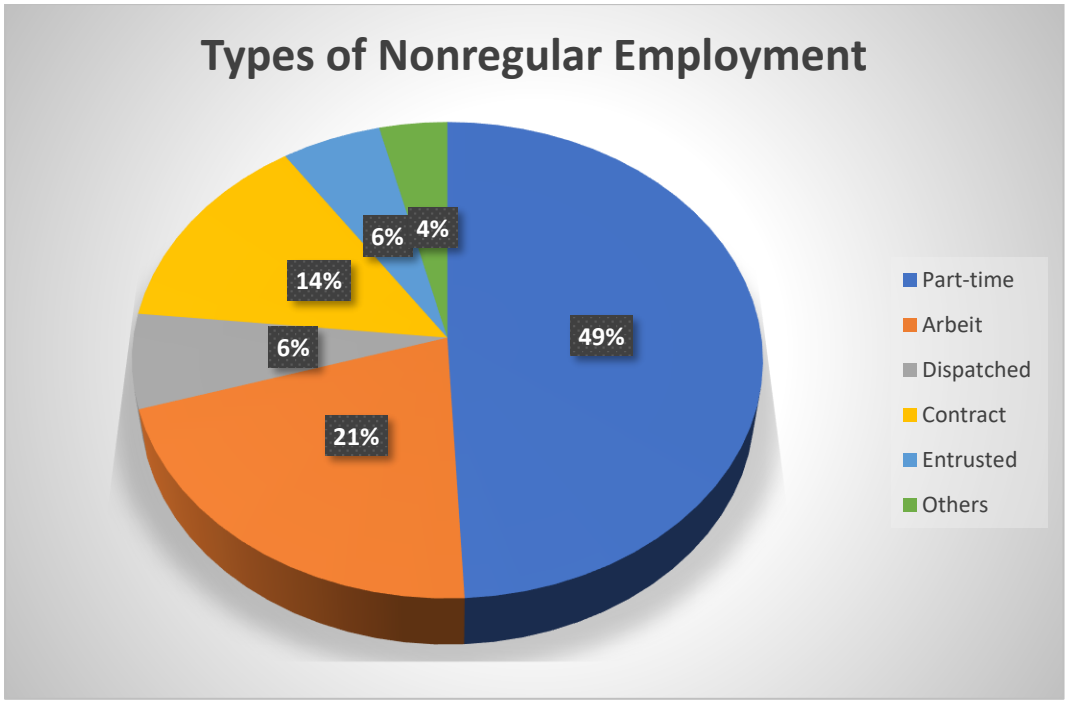

***Figure 7**. Types of Nonregular Employment. Source: Labour Force Survey (2017)*

Concurrently, numbers of regular workforce did not fluctuate significantly – the change has been from 33.3 million in 1984 to 33.85 million in 2017 (Labor Force Survey, 2017). Based on this evidence, Gordon (2017, p. 15) concludes that the overall 35 percent increase in Japan's working population during last 30 years is mainly due to the mentioned 14-million surge in nonregular workforce. This number can appear striking granted the fact that Japan's total population has increased during the same period only by 6.46 million people (from 120.3 to 126.76 million) (Japan Statistical Yearbook, 2017). This seeming paradox can be explained by "a sharp contraction of self-employment and family labor, a rise in the numbers of the elderly and the proportion seeking work, and the increase of job-

seeking women previously not in the wage labor force expanded the supply available for nonregular jobs" (Gordon, 2017, p. 16). Hence, the Japan's labor change over the last three decades can be summarized as the creation of numerous nonregular positions against the freeze in the hiring of regular employees (Lechevalier, 2014).

Under the traditional employment system in Japan, whereby a male's position of breadwinner was substantiated by his well-rewarded and protected job, precarious positions were targeted for women. Although the 1990 bubble burst and the subsequent recession spurred Japanese companies to expand the scope of nonregular jobs, the trend of increased share of females in temporary sector started long before the crisis (Kambayashi & Kato, 2009, p. 17). While before 1997 nonregular employment was mainly designed for women, after 1997 the non-standard occupations were extended to men as well (Kambayashi & Kato, 2009, p. 17). Concurrently, despite the overall commitment to the system of lifetime employment for core employees, some of them fell victims to the restructuring policies toward the late-1990s. The layoffs of core workers also appeared to be gender-based: "the burden of downsizing during Japan's prolonged stagnation fell disproportionately on women as opposed to men and on high-school graduates as opposed to college graduates. The biggest 'losers' appear to be female regular employees over age 30 with relatively short tenure working in large firms" (Kambayashi & Kato, 2009, p. 25). On the other hand, the proportion of regular male workers (defined as regular employees on indefinite contracts) "actually rose from 58.3 in 1992 to 58.9 percent [of total male population aged 18-70] in 2002" (Kambayashi & Kato, 2013, p. 13).

5.2. Labor Duality

Human resource management of large Japanese companies during the postwar period is described by the Regulation school as "employee sovereignty" (Ebbinghaus & Manow, 2001; Boyer & Yamada, 2002). Following comparison can come useful for explaining this classification. Western capital-labor relations historically developed around Fordist regulation, meaning that increase in productivity should be accompanied by proportional increase in wages. De-facto similar situation was observed in Japan before 1975 (Miura, 2008, p. 168). However, from 1975 onward, labor ceased claiming wage hikes proportional to productivity increments and concentrated on maintaining employment security per se. This was the result of an exchange called "developmentalist" (Yun, 2015) or "productivity movement" (Miura, 2008). It has effectively constrained the capital-labor

standoff that could trigger communist movements. In exchange, government and business designed an inclusive framework that allowed employers and employees reach compromises, at least before the onset of the neoliberal era.

"The analysis of the Japanese economy is a deeply problematical issue for those Western analysts who affirm the orthodox economics of the marketplace" (Preston, 2000, p. 106). Namely, wages and contracts in post-1975 Japan were not directly linked to economic fluctuations. Such employee-centered modeled could only exist thanks to close strategic relations between firms and their creditors – main banks (Abe, 2002, p. 685). The mechanism of a long-term exchange between finance, management and labor is called a "*companyist compromise*". In terms of labor organization, it was based upon the principles of long-term employment and enterprise-based unionism (Westra, 2003, p. 365). These principles, however, have been designed to fit team-oriented production sustained by internally-trained employees with long tenure at a same company.

While regular employment encompassed around 85 percent until mid-1980s, employee-centered model could reinforce corporate competitive advantage. In early 1990s, the major part of nonregular workforce was composed of married women doing part-time jobs and students involved in *arubaito*. Thus, these kinds of jobs were regarded as supplementary to regular positions designed for male breadwinners. However, as companies chose to rely on flexible workforce on a larger scale, more and more males above 25 have been working at part-time, contract or dispatch positions (Osawa, 2013, p. 310). According to the Labour Force Survey (2017), significant changes have occurred with the group of males between 25 and 34 years old: among them, the proportion of nonregular employees has grown from 2.8 percent in 1991 to 15.3 percent in 2017. Furthermore, as opposed to 1992, when 20.5 percent of males in the age group between 55 and 64 were nonregular employees, in 2017 their proportion constituted 30.3 percent. Moreover, in 1990, only 52.6 percent of male employees over 64 years old belonged to nonregular camp, while nowadays their proportion is 71.8 percent. For the same age groups, the increase in female rates of nonregular employment has been much more rapid, than those of males. Overall, however, the proportion of men and women in flexible jobs remained relatively unchanged throughout last 30 years, being 32 percent for males and 68 percent for females. Although the proportion remained unchanged, the absolute 14 million surge from 1984 till 2017 is a tremendous number. Hence, growing numbers of nonregular employees have not yet been able to find their institutional niche within a modified companyist compromise framework.

To systematize this duality of Japanese employment, Regulation school comes up with a concept of "hierarchical market-firm nexus" (HMFN). The existing system of incentives for core employees that includes lifetime employment and seniority-merit promotion, functions thanks to buffers that come into play at times of economic downturns (Isogai, Ebizuka & Uemura, 2000, p. 35). In the heyday of Japanese regulation model around 1970s, the main buffer was a system of subcontractors for vertical keiretsu. Subcontractors acted, firstly, as an insurance for core employees at headquarters, by externalizing labor-intensive production which resulted in lower labor costs at subcontractors caused by internal competition. Secondly, along with higher probability of employment cuts at subcontractors, latter have been characterized by higher levels of nonregular workforce. Thereby, SMEs built into the supply chains of large corporations, absorbed workers, thus minimizing national unemployment rates (Isogai, Ebizuka & Uemura, 2000, p. 36). "The flexibility of nonregular workers in various forms makes possible the long-term employment relationship of regular workers by reducing wage costs in a large firm. Therefore, in a sense, the external flexibility of nonregular workers is complementary to that of the internal flexibility of regular workers" (Isogai, Ebizuka & Uemura, 2000, p. 44).

While relatively high rates of flexible employment were peculiar to SMEs until 1990s, their proportion has grown also for large companies from the post-bubble period onward. Hence, contrary to pre-1990s framework, when nonregular workforce was a buffer for sustaining companyist framework, it has recently become an institutional arrangement on its own. Whereas regular employees' relationship with management is characterized by the described companyist framework, nonregular workforce is not embedded into a corporate regulation model. "They are isolated from the career course in the internal labour market, and have no chance to be promoted after taking on-the-job training like regular workers. Therefore, the incentive to continue to work for those workers is mainly their need to sustain a decent standard of living, because they face not only large differentials in wages, retirement pay, and company-based welfare but also relatively poor social welfare and high education costs" (Isogai, Ebizuka & Uemura, 2000, pp. 40-41).

On one hand, traditional Japanese employment system (so-called "lifetime employment") has been subject to criticism from different sides, especially due to lasting economic stagnation and intensified global competition. Hence, the necessity of overall reducing of working hours and provision of decent conditions for small- and medium-enterprises' employees are underlined by the ILO (2013), while IMF (2011) recommends

reconsidering [lifetime] employment policies amid aging population and declining rates of productivity. On the other hand, recent increase in flexible workforce poses another social problem. Large proportion of the nonregular employees in Japan have found themselves in this growing niche involuntarily[14], i.e. not being able to find regular positions (Asao, 2011; Higuchi, 2013; Takahashi, 2016). In addition, whereas according to the ILO standards[15] a part-time employee is the one working no more than 30-35 hours per week, around 30 percent of Japanese part-time workers exceed this limit, being "full-time part-timers" (Higuchi, 2013)[16].

Labor deregulation in Japan started before the 1990s "lost decade". First it was caused by competitive pressures for Japanese companies that started to globalize in early-1980s. To lower production costs, they resorted to increased reliance on flexible workforce (Gordon, 2017). At the same time, internal competition was at least as important factor as globalization, since the largest proportion of nonregular employees has been employed at accommodations, eating and drinking as well as retails, medical and welfare services (Asao, 2011, p. 4) that are not significantly affected by international pressures (Gordon, 2017).

The second upsurge in nonregular workforce was conditioned by the post-bubble economic crisis of 1990s. In order to cope with it, management resorted to cutting labor costs and increasing the pool of nonregular employees. These measures have significantly altered the foundations of the so-called traditional Japanese employment system that implies lifetime employment, seniority wages and enterprise unions (OECD, 1973). First of all, the introduction of performance-related pay (*seikashugi*) for regular workers in early 1990s has thereby modified the seniority-wage principle *nenkō joretsu*. According to Keizer (2009, p. 1524), this step indicated the substantial adjustments in the lifetime employment system (*shūshin koyō)* by prioritizing immediate performance over the skills acquired over a long-term career path. Despite that, institutional framework that implies high cost of occupation change and status affiliation with company proved resistant to the introduction of market-oriented reforms at a workplace.

The deregulation of flexible labor market has unfolded in parallel with retention of institutional preferences for core workforce (Fu, 2015). Thereby, the creation of two almost

[14] "Involuntary part-time workers are part-timers (working less than 30-usual hours per week) because they could not find a full-time job" (OECD, 2014).

[15] According to the ILO Part-Time Work Convention, a part-time worker is an "employed person whose normal hours of work are less than those of comparable full-time workers" (ILO, 1994).

[16] A considerable part of nonregular workforce has continuously extended contracts, which makes them "quasi-regular employees" (Keizer, 2009: 1527).

equal and mutually dependent institutional arrangements has been supported (Fong, 2015). Whereas nonregular employees took a brunt of economic crisis, regular workers incurred relatively minor losses. “Employment protection for insiders remained relatively unchanged in Japan even after labor market reforms, whereas outsiders were exposed to a much higher risk of unemployment, low wages, and poor welfare benefits” (Song, 2012, p. 423). Thus, regular and nonregular employees have come to constitute two distinct camps, with the latter group having few institutional leverages (Gottfried, 2008; Keizer, 2009).

“A typical behavior of Japanese firms facing a drop in their sales has been to reduce hiring rather than firing” (Lechevalier et al., 2014, p. 4). This thesis is consistent with the observation of Gordon (2017, p. 15) who admits that numbers of regular employees did not decrease by much, with the 2012 being “virtually identical to that in 1982”. In turn, the sharp surge in the percentage of nonregular employment is due to a significant increase in wage-earning workforce during the last three decades (Gordon, 2017). In other words, no new regular jobs were created in Japan since 1980s.

One must note, however, that during the recent years there has been some slow positive dynamics in narrowing the gap between the two labor camps. Firstly, according the Ministry of Health Labor and Welfare “Analysis of Labor Economy” (2015, p. 48), the average hourly wage for part-time workers has grown from 1,016 yen per hour in 2010 to 1,058 yen per hour in 2015, which amounts to a growth relatively to regular employees from 52 percent in 2010 to 54.4 percent in 2015. Secondly, although labor unions tend to be overwhelmingly composed of regular employees, the unionization of flexible workers slowly grows – from 5.6 percent in 2010 to 7.5 percent in 2016 (Basic Survey on Labor Unions, 2016, p. 4). This change is quite significant amid the general decline in unionization rates – from 18.5 percent in 2010 to 17.3 percent in 2016 (Basic Survey on Labor Unions, 2016). Against this background, Blind & Lottanti (2014) argue that the expansion of nonregular employment since 1990s represents a growing demand for flexible workforce, albeit the regular employment is not shrinking, which altogether contributes to inclusive long-term development. While authors certainly have their point, economically and socially bifurcated labor market in Japan is a relatively new challenge that needs to be addressed.

In a nutshell, labor duality before 1980s replicated the dual industrial structure, with large enterprises’ employees having more social benefits than those employed at SMEs. Nevertheless, even at smaller firms, nonregular employment was not common. On the other hand, from the mid-1980s onward, labor became bifurcated due to a surge in nonregular

workforce. Although some categories included in the "nonregular" group such as contract workers and part of dispatched workers are full-time employees, their welfare and status is inferior to regular workers, even to those employed at small firms.

5.3. Political Aspect of Labor Deregulation

Labor deregulation in Japan has started from early 1980s under the Nakasone administration and the proposal of deregulation in the Maekawa Report "aimed at expanding private investment" (Watanabe, 2015, p. 417). This document paved a way to a series of structural reforms that led to privatization of some strategic state-owned enterprises, such as "Japan National Rail" and "Nippon Telegraph and Telephone Corporation (NTT)". Notably, many of those companies have been most eager to implement Anglo-Saxon shareholder-centered corporate governance reforms, which is reflected in their inclusion into the Nikkei 400 Index in 2015. During the recent times, these pioneering neoliberal mediums have been increasingly adopting the policy that favored the coexistence of traditional regular jobs and nonregular occupations as two separate institutional arrangements (Fong, 2015). The aforementioned companies, though varying according to their scale and profile, have become an epitome of the deepening institutional gap between core and nonregular employees.

As the labor reforms in 1980s were promoted by the Ministry of Labour (MOL, reorganized into the Ministry of Health Labor and Welfare (MHLW) in 2001), advisory councils (*shingikai*), labor unions and employees had tools to influence policy deliberations. Labor policies were negotiated at tripartite commission formed by academics and former bureaucrats, employers and workers (Miura, 2008, p. 164). On a labor side, Rengō selected seven employee representatives, while on the employers' side, the members were selected based on the following quotas: four picked by *Nikkeiren*, two – by the Japan Chamber of Commerce, and one – by the National Federation of Small Business Associations (Weathers, 2004, p. 434). The third party of the council is the public interest representatives selected by the MOL. This group is composed of "labour academics, lawyers, journalists and former MOL officials" (Weathers, 2004, p. 434). That-time political agenda still followed the postwar conservative and developmentalist stance, whereby LDP leaders recognized Rengō as essential representatives of core labor (Yun, 2015, p. 7). This was one of the reasons why the numbers of regular employees were not cut during the course of the first labor enactments. In turn, the "discretionary work" introduced by the 1987

amendment to the Labour Standards Act was first related to regular employees. It implied the payment for the fixed working hours regardless of the actual working time, thereby legalizing overtime labor (Watanabe, 2015, p. 418).

Regarding nonregular employees, I will discuss the regulation of the "dispatch work" category. It refers to the presence of an intermediary – dispatching agency – that manages employee's contract and negotiates the terms with his/her employer. Although dispatch employment constitutes only 6.4 percent of nonregular camp, the increase in dispatched workers (*haken*) has been most rapid among all types of nonregular employees (Imai, 2004, p. 36). Their numbers grew from just 280 thousand in 1999 to 1.3 million in 2017 (Labour Force Survey, 2017). Furthermore, the total number of temps registered with dispatch agencies amounted to 2.7 million in 2015 (MHLF, 2017, p. 5). According to Weathers (2004, p. 425) and Yun (2015, p. 12), *haken* symbolize the very essence of labor deregulation in Japan. The primary reason for such assertion is the presence of the opposite views on the *haken* phenomenon. The ruling LDP coalition views dispatch workers as a novel solution to flexible needs of employers and an alternative path for individual career pursuit. The opposite, critical position, advocated by DPJ during 2009-2012 when they were in power, is that *haken* constitutes the most precarious camp, while an employee signs a contract with an agency but does have any influence over employers' decision regarding termination, prolongation or changing the contract into the regular type.

The 1985 Worker Dispatching Law was peculiar for legalizing temporary agency or dispatch work, previously prohibited in Japan, first limiting it to 13 occupations (JILPT, 2011, p. 12). In the subsequent legislation, occupations chosen for dispatch work were those where regular jobs required special knowledge and on the job training. Thereby the government wanted to make sure that dispatch workers would not replace regular employees (Watanabe, 2015, p. 418). The 1996 amendment of the Law extended the list of occupations permitted for dispatch work to 26 (JILPT, 2011, p. 13). The next revision of 1999 was notable for substituting of positive listing of occupations allowed to be filled with nonregulars with negative descriptions of jobs not satisfying this condition: the latter belonged to manufacturing, medical, security, dockyard and construction occupational areas (Weathers, 2004, p. 436). Moreover, for the targeted 26 industries, the term of dispatch was extended from one to three years (Imai, 2004, p. 19). The 2003 amendment also extended the maximum period of hiring temps for the newly allowed occupations from one to three years, equalizing it with the original 26 occupations, and removed manufacturing industry from the negative list, setting the employment limit for it to one

year (Imai, 2004). Eventually, hiring limits were canceled by the 2015 amendment that opened the path for unrestricted employment of dispatched workers – so-called *shōgai haken* or "lifelong dispatch" (Okunuki, 2015, Japan Times). Before 2015, employer was obliged either to offer a tenured regular contract to a nonregular worker, or not to renew the current agreement. Nowadays, however, there is a real possibility for having a repeatedly renewed contract without formally becoming a regular employee.

The policy of forming lower-cost nonregular employees' cohort was implemented in the mid-1990s following the recommendations of *Nikkeiren* (Keizer, 2009). In its 1995 report called "The Japanese-style Management in a New Era", the business confederation offered to divide workers into three categories: core workers protected by the postwar companyist compromise, workers with special skills and unskilled workers targeted as a flexible workforce (Yun, 2015, p. 13). This could be done almost unilaterally, without accounting for the employees voices due to the lack of their institutional representation through labor unions. "The unionization rate was a little more than 30% until 1975, but has continued falling annually since then. Since the mid-90s the decrease of union members combined with the rapid increase of nonregular employees to whom enterprise union in the majority of cases have been denying membership, has resulted in a decrease in union density" (JILPT, 2012, pp. 3-4). On the other hand, although the 1995 Nikkeiren report created a space for deregulation among nonregular employees, it remained faithful to the custom of employment protection for core workers. "While this report is often read as evidence that Nikkeiren abandoned its commitment to Japanese employment practices, it is also noteworthy that Nikkeiren sees the first type of worker still as the core of the labor force and essential to Japanese enterprises" (Thelen & Kume, 2006, p. 30).

On a political level, the degree of unions' representation in the ministerial debates on labor reforms was minimized starting from 1995. In that year, at the request of *Nikkeiren*, the LDP-led government established a Deregulation Committee that aimed to bypass negotiations in MOL advisory councils (*shingikai*) for the sake of a smoother liberalization (Watanabe, 2015, p. 419). Subsequently, Koizumi administration completely removed labor representatives from the policymaking process led by the Council for Regulatory Reform (established in 2001; formerly – Deregulation Committee), which was in stark contrast to the labor-inclusive policy led by MOL / MHLW (Watanabe, 2015, p. 420). Whereas before, labor laws were discussed and adopted consensually under MOL's umbrella, the rules were changed under neoliberal government. Firstly, reform plan was offered by the deregulation instance, secondly – approved by the Cabinet Office and only

afterward – forwarded to the MOL councils. Under this order, the tripartite negotiations did not matter much, since they could not substantially alter the governmental position (Miura, 2008, p. 164). The rapid labor deregulation process has been an exception for Japanese political economy characterized by an incremental change (Watanabe, 2012, p. 25). The postwar inclusion of labor into a developmentalist framework historically served a mission of containing leftwing movements (Miura, 2008). However, the 1990s' crisis provided LDP-led government with arguments in favor of limiting general labor rights. Presenting it as an inevitable concession, the party has eventually managed to maintain popular support. Amid this clear infringement, traditionally non-hostile labor unions did not have enough leverages and determination to advocate for anything more than basic guarantees for regular employees.

Against the background of the slumping unionization rates (Figure 8), the labor unions which are members of Rengō (Japanese Trade Union Confederation) tend to represent the interests of core employees, but not contributing to the protection of the temporary workforce (Ishiguro, 2008; Fu, 2015). This can be explained by the entrenched employment duality, where management and permanent employees of large enterprises have traditionally formed coalitions (Aoki, 1988). Before 1990s recession, when employment guarantees have covered vast majority of the Japanese labor market, such companyist compromise was institutionally complemented by the high cost of changing occupation and enterprise-based unions (Morishima, 1984). According to the Ministry of Health, Labor and Welfare survey, the unionization rate in Japan has been declining rapidly – from 30.8 percent in 1980 to 17.3 percent in 2016 (Basic Survey on Labour Unions, 2016, p. 3). However, in absolute terms, the fall in union membership has not been that sharp – from 12.4 million in 1980 to 9.8 million in 2015 (Basic Survey on Labour Unions, 2016). As mentioned above, the number of regular employees has hardly changed during this period. On the other hand, around 14 million of new jobs created are mainly for nonregular employees (Labour Force Survey, 2017). Thus, the drastic fall in unionization rates against gradual decrease in absolute membership can be explained by the fact that regular status is associated with union membership, whereas the opposite holds true for nonregulars.

Due to post-bubble economic crisis, government as well as business community took steps to raise international competitiveness of large Japanese enterprises. In the opinion of Nikkeiren, annual wage hikes advocated by Rengō through *shunto* – spring offensives – was one of the factors that impeded corporate economic performance. Hence, under the pressure of Business Confederation, in 1998, Rengō "agreed to a freeze of the

basic wage rate in exchange for employment protection" (Miura, 2008, p. 163). Since Japanese labor unions traditionally operate on the enterprise rather than industrial level, *shunto* helped to synchronize the claims for minimal wages across various firms. Rengō eventually gave up this function in 2002, unable to resist neoliberal agenda (Miura, 2008). From that time onward, Trade Union Confederation could only seek some political support in the matter of protecting the rights of core employees. As the 1995 Nikkeiren classification was effectively implemented, core workers themselves gave up hopes for requiring wage hikes, having "accepted" the basic status-quo that their shrinking cohort could still enjoy. Contrary to that, "workers with special skills" and "unskilled workers" could not expect any substantial support from unions. Peng (2012) argues that regular employees and major labor unions have been tacitly supporting labor deregulation, as long as it has meant the secured benefits to core employees at the expense of growing number of nonregular precariat.

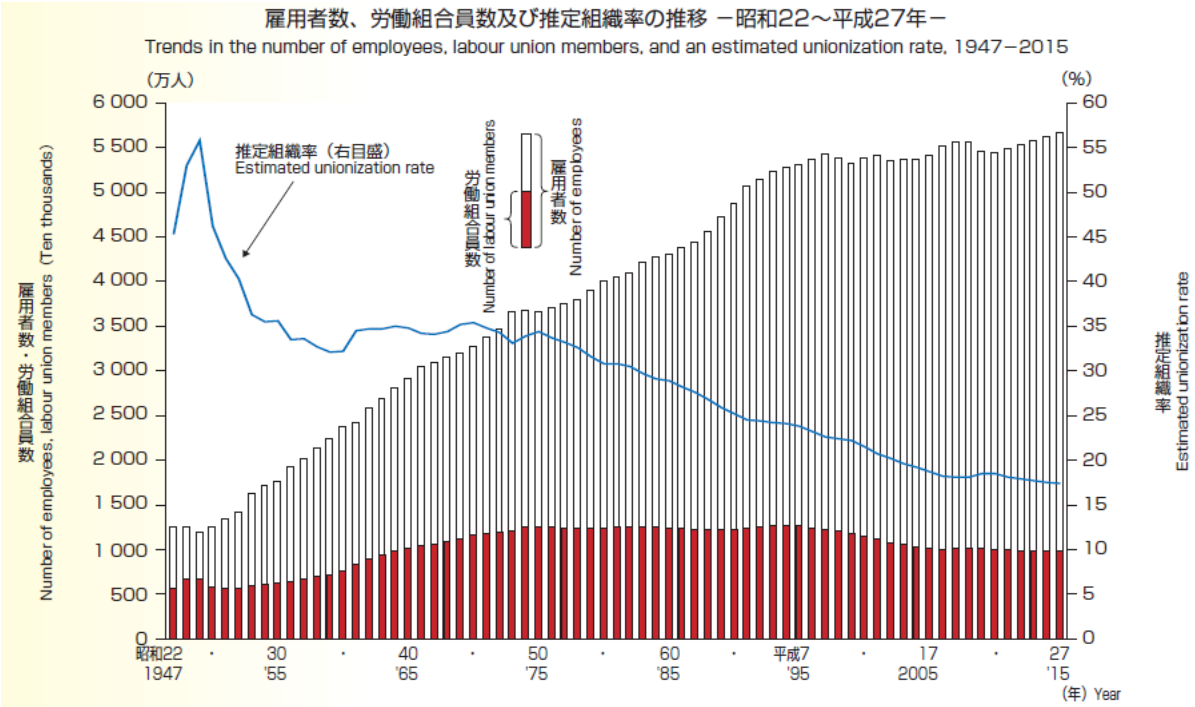

***Figure 8**. Estimated Unionization Rate. Source: Basic Survey on Labour Unions (2015), as cited in Ministry of Health, Labour and Welfare (2015, p. 16)*

In 2007, the Rengō's chairman, Takagi, has explicitly stated that the organization "has turned a blind eye to part-timers", which was believed to allocate additional profits to existing union members (Ishiguro, 2008, p. 15). Eventually, the denial of union membership to nonregulars did not bring wage hikes for core workforce either. Although

the part-time employees' membership in labor unions has increased from 5.6 percent in 2010 to 7.5 percent in 2016 (Basic Survey on Labor Unions, 2016, p. 4), unions still tend to reject most of nonregular employees" applications (Suzuki, 2010; JILPT, 2012, pp. 3-4). This goes in line with the institutional complementarity hypothesis arguing that "In countries with predominantly enterprise-based forms of unionism, labor tends to pursue strategies of internal participation" (Aguilera & Jackson, 2003, p. 456). The flexible workforce representing "external participation" is thus institutionally excluded from the management-labor bargaining process. Okumura (2000, as cited in Aguilera & Jackson, 2003, p. 461) places this problem within the wider context of insider-outsider conflicts pertinent to Japan, whereby "insiders' interests conflict with minority shareholders' interests in greater liquidity and financial returns, as well as the interests of certain employees – for example, mobile professionals and non-core employees".

A consensus over deregulation of nonregular labor has been built between Keidanren and Rengō – two parties with supposedly different views on labor policies. However, the seeming contradiction becomes a regularity if approached from the political economic angle. Both labor unions and business have agreed to advocate insiders' or core-employees' interests, while using nonregular workforce as a long-term buffer. Japanese government facilitated this approach "as nonregular workers did not hold political power as an interest group" (Watanabe, 2015, p. 414). Thereby, ruling party initiated labor deregulation in a way satisfying most politically powerful groups and shifting the emerged externalities towards the member not included into the emerged "coalition".

As mentioned above, in 2003, the Workers Dispatching Law was amended to give more possibilities of workers' hiring from the temp agencies, which was a neoliberal win. But in the same year, Rengō managed to persuade Keidanren and MHLW to revise the Labour Standards Act by including the norms that would complicate the replacement of regular employees by *haken* (Yun, 2015, p. 15). Thus, while neoliberal government succeeded in deregulating nonregular employment, trade unions and business agreed to protect core workforce. Thereby, institutional gap between two labor camps was reinforced politically. "In Japan, political coalitions between conservative policymakers, large firms, and core regular workers were the driving force of the reinforcement of dualism and inequality by shielding labor market insiders from the pressure for regulatory reforms but extensively eroding regulations protecting outsiders for flexibility" (Song, 2012, pp. 416-417).

The 2008 Lehman shock that followed the US-originated financial crisis hit Japanese companies hardly, since the latter are dependent on exports to the US and often place their shares at US stock-exchanges. This had detrimental consequences for the Japanese labor, especially for temporary and contract workers whose contracts where massively terminated (Osawa & Kingston, 2015, p. 60). On the wave of this growing social anxiety, Democratic Party of Japan (DPJ) managed to win a majority during 2009 elections to the House of Representatives, which was only the second time in the postwar history the Liberal Democratic Party (LDP) was defeated. One of its novel electoral promises was the workers-rights' enhancement against a tendency of a growing deregulation favoring big business. The alliance with Rengō was key to achieving this goal (Yun, 2015, p. 8). Moreover, DPJ leaders went beyond the protection of core employees, which is a focus of Rengō, but also advocated the need to advocate rights flexible workforce (Yun, 2015). While securing core positions has been key to Japan's development even against the pursuit of neoliberal policies, the attempt to level the gap between regular and nonregular employees was seen as an encroachment on insider-based management-labor compromise. Hence, both the conservative (MHLW) and pro-business (Committee for Regulation Reform) parties opposed the labor initiatives of DPJ (Yun, 2015). The latter, thus, only managed to advocate the ban for a less-than-1-month temporary dispatch as measure of protecting *haken* (Osawa et al., 2013, p. 324).

As a result of DPJ's failure to deliver its promises, the LDP's hegemony was restored already during the next elections of 2012. The party has traditionally continued to advance a pro-business agenda that allocates only secondary role to employees. "In the battle over Japan's employment paradigm, the LDP is firmly in the employers' camp: 'Abenomics' offers no improvement for the precariat and is likely to expand their numbers under the banner of promoting 'flexibility' in the labor market" (Osawa & Kingston, 2015, p. 61). Increasing proportions of employees are thereby treated as "clients" that consume employment services, rather than "workers" that do their job to earn for living (Miura, 2008, p. 171). The "client" should theoretically be able to individually negotiate terms of contract by letting market rather than a particular employer evaluate his/her skills. However, in practice, employees other than white-collar professionals cannot expect decent conditions, which is further exacerbated by their minimal access to labor unions. In a wider context, the current economic program, so-called "Abenomics", additionally shifts the fiscal burden from large companies to lower-income citizens. Whereas the consumption tax has been gradually raised from 5 percent in 2012 to 10 percent in the upcoming 2019, corporate tax

for large companies has been cut from 40.69 percent in 2011 to 29.74 percent in the upcoming 2018 (JETRO, 2017).

5.4. Corporate Governance Reforms and Labor Deregulation

In the postwar Japan, management-labor compromise occupied a higher place within institutional hierarchy than financial compromise (Yamada & Hirano, 2015, p. 14). The reason for that was the importance of shop-floor labor organization for corporate and national competitive advantage. It resulted in the provision of incentive mechanisms for labor that included the "promotion system, the seniority wage system, the retirement-pay system, and company-based welfare" (Isogai, Ebizuka & Uemura, 2002, p. 34). However, upon the substantial wealth accumulation by large Japanese companies around the early 1980s, traditional HRM policies were overshadowed by financial diversification that implied growing equity finance amid the diminishing role of main banks and cross-shareholding. The 1990's bubble burst further spurred government and management to abandon costly employment practices. In turn, the emerging mean for achieving corporate growth has become a pursuit of shareholder value. This has been caused by growing proportion of financially-oriented investors from the mid-1990s. Under this "post-companyist" framework, incumbent management is no longer secured by main bank and therefore tends to protect itself against shareholders' leverages by rising shareholder returns and lowering labor costs (Isogai, Ebizuka & Uemura, 2002). In other words, CEOs have started to allocate more wealth to shareholders at the expense of employees' remuneration and social guaranties (Aoki, 2007; Jackson, 2007). The described labor deregulation that has favored increasingly financial orientation by Japanese companies, was sanctioned by the Japanese government and the Ministry of Intertribal Trade and Industry (MITI) in particular (Lechevalier, Debanes & Shin, 2016, p. 13).

As described above, nurturing of firm-specific skills among employees of large enterprises was key institutional feature of Japan's postwar industrial development. Such strategic HRM implies long-term contracts for employees backed by senior-merit incentives and high cost of occupational change. This labor-management nexus was not only a societal feature of Japan's stakeholder model, but also a key contributor to country's competitive advantage. Despite two economic crises during 1970s caused by oil shocks, core workforce was protected from downsizing. This was possible due to duality of Japanese production, whereby, large companies' subcontractors absorbed economic shocks

by resorting to labor cuts, wages reductions as well as reception of surplus labor from parent companies (Lechevalier et al., 2014). Although the post-bubble period of 1990s was characterized by higher levels of downsizing, the lifetime employment system has remained, though to a lesser extent, key to Japan's HRM (Noda, 2013, p. 364).

Japan's postwar corporate governance is classified as "contingent" due to its dependence on a main bank system (Aoki, 1994). By providing loans at low interest rates, main banks secured partner firms during financial distress and, by holding large block of shares, prevented hostile takeovers. Under conditions of achieving moderate levels of profitability, incumbent management could secure its positions. However, main banks stepped in if profitability dropped below designed threshold. Still, such interventions did not result in drastic downsizing, but rather relocation and restructuring of human resources. Lower pressure on management compared to shareholder-oriented companies allowed CEOs to pursue HRM policies at their discretion. To achieve high degree of training for attaining firm-specific skills, it was essential to provide long-term incentives to employees. Hence, main-banks' support was key to maintaining employment guarantees even at times of distress. As opposed to financially oriented companies that would consider employment policy as a tool for achieving higher shareholder returns, stakeholder companies in Japan were oriented toward long-term growth and therefore were prone to hoarding labor even during downturns. As a result, when economic situation normalizes, company can again fully utilize its internally-trained high skilled labor to achieve competitive advantage (Abe, 2002, p. 687).

While the postwar corporate governance was contingent upon main banks, the ongoing corporate governance reforms are aimed at empowering minority shareholders. Japanese companies have been gradually abandoning debt finance, seeing the alignment with shareholders as key to their financial success. Hence, even under conditions of a minimal outsider presence at boards of Japanese companies, managers themselves become subject to shareholder-related discipline by committing to disclose accounting information to investors. Whereas under the main bank system, monitors' interference was conditional upon particularly dissatisfying corporate performance, shareholder model links managerial performance to annual financial returns much tighter. Therefore, to secure their own positions, CEOs tend to pay increased attention to financial indices related to share value, while their concern with employees' wellbeing moves downwards along institutional hierarchy (Dore, 2007, p. 387). Hence, although the real effects of corporate governance

reforms on firm performance have not been obvious, they have certainly impacted Japan's stakeholder model.

According to institutional complementarity hypothesis (Aoki, 1994), changes in corporate finance, whereby equity funding grows relatively to bank funding (Hoshi & Kashyap, 2004), are likely to trigger changes in labor policies. Furthermore, while insider-based corporate governance system is contingent upon bank finance, this system is currently moving towards outsider-based governance, hence becoming more compatible with shareholder finance. As a result, increasing pursuit of shareholder value by Japanese companies can be regarded as a step stone for promoting flexible workforce orientation that results from increased market pressure (Amable et al., 2005). The setting of high equity returns as a performance target differs from the vision of long-term growth under a stakeholder model. Hence, the pursuit of equity value alters time horizons and a discipline of poorly performing units (Jackson, 2007, pp. 284-5). In other words, remuneration and employment guarantees become contingent upon relatively short-term financial performance.

The ascendance of business interests relatively to workers' welfare along institutional hierarchy is a part of a macro process whereby the inequality levels have been increasing rapidly since 2001 (Lechevalier, 2016, p. 58). Measured by the Gini coefficient that reveals the distribution of incomes after taxes, the significant change can be observed between the year 1996, when the index was 0.36, and 1999, when it became 0.381 (MHLW, 2002, p. 7). Subsequently, the coefficient peaked to 0.393 in 2005 and slightly dropped to 0.387 in 2014 (MHLW, 2014, p. 6). The indicator before 1996 placed Japan among one of the most equal societies among the OECD countries. However, the post-1999 levels exceeded the OECD average, which caused substantial concern and criticism from this organization (Jones, 2007). The OECD report also mentions insufficient social spending amid aging population as well as the problem of labor market duality between regular and nonregular employees (Jones, 2007).

On a corporate level, the gap between directors and employees is likely to have widened precisely due to increased influence of shareholders that resulted from the process of corporate governance reforms. If we look at the tendencies for the large companies with the capital over 1 billion yen during the discussed period of a sharp surge in Gini coefficient, the similar process will be apparent: "The level of salaries for employees in 2005 was about 90% of that in 1997. In contrast, during the same time period, dividends increased by 237%, salaries for directors by 12%, and bonuses for directors by 295%" (Miura, 2008, p. 166).

This data tells that, on one hand, wage gap between directors and employees did not widen significantly in a strict sense. However, judged by bonuses that mostly display the degree of directors' compliance with shareholders' demands, as well as dividends – a direct result of a rise in equity value, one can realize how the coalition between directors and shareholders brought about a tendency in wealth redistribution that prioritizes shareholder-oriented interests over those of employees.

Although institutional features of Japan's industrial system serve as impediments to labor deregulation, they are also subject to change under the pressure of a newly formed political coalition. One of its emerged powerful actors is foreign shareholders that are certainly inclined towards financial rather than strategic behavior, thus favoring downsizing (Ahmadjian & Robinson, 2001; Ahmadjian & Robbins, 2005). Instead of maintaining long-term employment, foreign shareholders mostly view labor costs' reduction as a mean for raising corporate profitability. The ways they exercise their control over company can be very different from the traditional monitoring system sustained by main banks that was based on trust. The latter was aimed at ensuring corporate survival, for which disciplining by fears like the one of hostile takeovers would clearly be a wrong strategy. In turn, foreign shareholders are mostly concerned with corporate integrity merely as means to make managers pursue shareholder value (Miyajima, Hoda & Ogawa, 2016, p. 13).

Thus, the most widespread way of foreign shareholders' control is the exit option, whereby they sell their shares that can be acquired by entity potentially interested in taking a company over (Noda, 2013, p. 373). The most popular way of shareholder control in the West is the voting at annual general meetings (AGMs). However, the institutional feature of Japanese companies has been the tendency of holding AGMs at the same day and within a short period, so that investors holding shares in different companies could exert as little control as possible (Miyajima & Nitta, 2007, p. 331). Moreover, AGMs have been more of a ceremonial procedure, since most of the issues put on the agenda are resolved beforehand. Therefore, shareholder-initiated discussions at the meeting room are not very welcomed. "The standard defence was the *shan-shan sokai* (smooth and swift AGM), a carefully rehearsed, twenty-minute affair, with shareholder employees forming a claque which passed all resolutions by acclamation and intimidated any opposition" (Dore, 2007, p. 378). At the same time, situation is currently changing, as shareholder activism has become much more pronounced since 2003 (Ahmadjian, 2003, p. 135). Thus, increased presence of foreign shareholders at the AGMs leads to growing opportunities to pursue their interests

through direct voting or initiating discussions in the boardroom (Ahmadjian, 2007, p. 136; Dore, 2007, p. 379-380; Dore, 2007b, p. 210).

On the other hand, stock concentration can mitigate the speed of employment cuts. For example, Abe (2002, p. 698) found out that large stockholdings in the chemical industry companies contribute to lower rates of downsizing in a normal time. However, during crisis, the opposite effect was observed (Abe, 2002). Differently from the Western neoliberal policies that imply encompassing labor cuts, in Japan, core workers still have high degree of immunity to restructuring (Noda, 2013, p. 365). Furthermore, the practice of "lifetime employment" still pertains to regular employees (Jackson, 2007). In turn, growing proportion of nonregular employees amid reduced hiring of regulars seems to be a feature of a new "post-companyist" era.

In a nutshell, corporate governance reforms do not lead to a direct convergence of Japanese employment practices with Anglo-Saxon standards. In this respect, postwar institutional compromise between management, stable shareholders and core employees remains intact. On the other hand, the competitive pressures grow as well. The agents of market are foreign shareholders that own unprecedently large proportion of shares at Japanese companies. While addressing their claims of higher equity returns, incumbent management also tries to prevent possible hostile takeovers. As a result, the M&A levels of Japanese firms, which can serve as a measurement of risk-taking, are significantly lower than the M&A levels of other OECD states (Froud, Haslam, Johal & Williams 2000, p. 105).

Although M&A activity is minimal in Japan, CEOs perceive growing pressure from shareholders linked to financial performance. Hence, to be able to promptly react to downturns, business community together with the government, have been consistently expanding the cohort of nonregular employees targeted to accumulate these risks. Even though the increasing presence of outsiders at boards of Japanese companies does not lead to the break of mutual commitments between management and regular employees, it increases the chances of a company to pursue shareholder value at the expense of nonregulars. These efforts result in accumulation of profits by companies, which, however, does not lead to proportional wages' hikes even for core employees. In this respect, institutions such as labor unions called to effectively challenge neoliberal perils, only act as impediments by building coalitions with politically powerful, but ideologically hostile parties.

5.5. Nonregular Employment Expansion as a Breach of the Compromise

To better understand the overall role of nonregular employment expansion in Japan, let us revamp this concept. "The first definition is based on the specific term (contract length) of each worker's legal employment contract, whereas the second definition is based on a custom/practice in the place of each worker's employment (or how the worker is actually termed in the place of his/her employment). To this end, we can interpret the first and second definitions as *de jure* and *de facto* definitions of the primary and secondary segments of the Japanese labor market" (Kambayashi & Kato, 2013, p. 6). In other words, the first definition originates from the distinction between fixed-term and indefinite contracts, while the second one is motivated by the type of employee's contract within a company ("*seishain*" – a name for a regular employee, remaining types fall under category of nonregular employment). This research mainly operates with the second – de facto – definition.

Sato (2012, as cited in Hirano, 2015, p. 125) lists following four criteria for defining a regular employee: "indefinite operations for utilization, indefinite offices, and locations for transfer, overtime work, and full-time service". In other words, regular employment is embedded into a postwar companyist compromise, whereby, in exchange for labor security, a worker commits to "sacrifices" for the sake of the company. Contrary to that, nonregular employees are subject to individual rather than corporate-specific regulations. They have clearly assigned duties, are not subject to relocation and "voluntary" overtime work and can be hired indirectly by dispatched agency or outsourcing firms (Osawa, Kim & Kingston, 2013, p. 313). While not being formally obliged to fully devote themselves to the company, they also receive much more modest social welfare and are most likely to be subject to employment cuts at times of recession. Moreover, although nonregular employees do not have to work overtime, their regular working hours are equal to those of regular workers in more than 30 percent of the cases (Osawa, Kim & Kingston, 2013).

Although the difference between regular and nonregular employees prescribed by the ILO is based on the 30-35 working hours threshold, length of contract and type of job, in Japan the border between two groups is not that clear-cut. "In reality, it is impossible to differentiate between these employees based on employment period, length of labor hours, and job content" (Hirano, 2015, p. 124). What is clear, however, is a lack of social protection that nonregulars have. As opposed to core employees, flexible workforce does not have unemployment benefits because of not being covered by employment insurance (Osawa, Kim & Kingston, 2013, p. 324). This omission has originally resulted from the

stereotype of nonregulars being students or being supported by a family breadwinner. However, compared to early 1990s, the situation has changed significantly – nowadays nonregular employees often remain within this niche for three years or longer. Furthermore, households' wealth becomes increasingly dependable on the income of precariously employed family members.

According to the MHLW survey (2016, p. 30) and Labour Force Survey (2017), the average possibility for males to move from nonregular to regular employment in the first quarter of 2016 was 6 percent, and for females – 2.7 percent. Moreover, in Japan "non-regular workers… are paid only 56.8% of what regular employees earn on average as compared with 89.1% in France, 79.3% in Germany and 70.8% in Britain" (Japan Times, 2016, as cited in Ishii, 2018, p. 2). These figures tell that the ever-growing share of nonregular employees is an alternative labor arrangement that has lasting consequences. "Non-regular employment in [Japan] does not play a role of a stepping stone to move toward better jobs like regular employment, but that of a 'dead-end' trap" (Lee & Shin, 2017, p. 18).

While the government and numerous consulting agencies stress the advantages of newly-created flexible jobs (Clifford Chance, 2012; Muranushi, Itabashi & Hayashi, 2015; UT Group, 2015), one rather sees that many nonregular employees appeared in this camp involuntarily, while their chances to switch to a desired regular job are minimal. The definition of the "involuntary nonregular employment" is "the lack of opportunity to work as a regular employee" (Asao, 2011, p. 13). The MHLW data (2016, p. 25) says that 25 percent of males and 12 percent of females within the group of nonregulars are the ones employed unwillingly. At the same time, the JILPT survey (Asao, 2011, p. 12) found out that only for the group of part-time employees, the choice of the occupation was predominantly voluntary: 39 percent of respondents were motivated by the will "to work during hours suiting the convenience". On the other hand, among fixed-term employees and dispatch workers, the most popular answer was the one corresponding to the definition of involuntary employment (37.1 and 34.9 percent respectively) (Asao, 2011).

Although involuntary nonregular employment is widespread in Japan, statistics tell that most of flexible employees appear in this niche due to reasons other than "lack of opportunity to work as a regular employee". According to MHLW (2016, pp. 24-25) the number of involuntary employed nonregulars in 2015 was 3,15 million people – a decline compared with 3,31 million in 2014 (MHLW, 2015, p. 21). At the same time, the number of voluntary hired nonregulars also fell – from 4,19 million in 2014 to 4,12 million in 2015.

Judged by the total number of nonregular employees (Labour Force Survey, 2017), it appears that there are numerous flexible employees that do not satisfy either of the mentioned two conditions. Asao (2011, p. 12) also presents cases of nonregulars applying for their jobs under the pressure of other circumstances such as "inability to work as a regular employee due to household matter, childcare, nursing care, etc." or physical difficulties related to regular work. Hence, the numbers of nonregular employees that appear to be neither voluntary nor involuntary are 12,25 million (or 62 percent) for 2014 and 12,58 million or (63,3 percent) for 2015.

Based on this evidence, the proportion of involuntarily employed nonregulars (15,87 percent) is only slightly lower compared to voluntary employed regulars (20.75 percent). However, since the arrangements for this labor sector are still at an early institutional stage, the indexes such as conversion from nonregular employment to regular employment, unionization rates and social benefits for nonregular employees can shed the light on a real gap with regular employment. Although the proportion of nonregular employees is growing rapidly, nowadays constituting a social relationship outside the traditional "companyist" framework, there is an indication of slight positive dynamics of the narrowing labor bifurcation. Unfortunately, though, the gap is often closed not by the improvement of the conditions for nonregulars, but by watering down social guarantees of core workers. "As a result of certain deregulation and more flexible use of regular employment, the Japanese labour market has diversified, if not deregulated as extensively as liberal market economies such as the United States" (Watanabe, 2017, p. 14). This process leads to the emergence of intermediate forms of employment that are neither regular, nor nonregular.

The expansion of nonregular workforce can be an efficient response both to the challenge of raising international competitiveness and to the search for optimal work-life balance. However, for Japan, institutional arrangements backed by political power play a significant role in the process of the new coalition formation. In this respect, concessions given to relatively unprotected flexible workforce are proportional to its minimal political leverages. Hence, minor improvements in working conditions of nonregulars can probably be explained by international pressures, to which Japan must respond due to growing dependence of its economy on foreign capital. Apart from that, labor role in political process remains very limited, with neoliberal agenda paving its path at the expense of the most vulnerable layers of society.

This chapter discussed the reasons and the dynamics of the ongoing labor bifurcation in Japan. While the industrial scope and the contract length for nonregulars has been expanding steadily, the core employees segment has preserved its institutional features. As a result, the increasing proportions of nonregular workers have minimal chances to attain regular status. In response to the recommendations provided by the ILO, IMF and OECD, Japanese government has undertaken steps to narrow the gap between these two job categories. However, despite some positive trends like the minimal pay increase for nonregulars and their growing unionization rates, the difference is often alleviated through deregulation of regular employment, which further deteriorates the general labor situation in Japan.

The next chapter analyzes the previously overlooked factor behind the increase in the nonregular employment, which is the enhancement of shareholder value. This explanation complements the existing studies that mostly attribute the increase in nonregular employment to the employers' efforts to cut average labor costs while at the same time preserving the social guarantees to regular workers. In addition, chapter 6 proceeds with the analysis of the corporate governance reforms' effects, namely – with the process of corporate financialization. From the point of labor, financialization has contributed to the widening of the intra-firm gaps between managers and ordinary employees.

Chapter 6: Externalities of the Shareholder Value Pursuit

"A few managers may mutter their dissatisfaction, but after less than two decades of missionary activity, the conversion of Japan to the theology of shareholder sovereignty seems complete" (Dore, 2009, p. 161).

This chapter critically examines the externalities of the shareholder value pursuit at Japanese listed companies. It analyzes the enhancement of shareholders' rights as a part of a corporate financialization process. Although Japanese economy is generally not considered as financialized, the growing profits allocated to directors and shareholders at the expense of employees can be regarded as symptoms of expanding financial influence. Furthermore, I consider the increased shareholder returns being one of the contributors to the progressing labor bifurcation at large Japanese enterprises. Specifically, I test the hypothesis about the positive association between the shareholder value returns and the proportion of nonregular employees.

6.1. Financialization as a Rise of Non-Stable Shareholders

In addition to management-finance nexus, analyzed in Chapter 4, regulation theory is preoccupied with *hierarchy* of existing institutions influenced by a composition of a sociopolitical bloc. "Whereas the notion of institutional complementarity implies… symmetry between two or more institutions, the hypothesis of institutional hierarchy stresses the asymmetry among these institutions" (Boyer, 2005, p. 18). Regulation school is notable for approaching institutions from the political economic rather than the functionalist point of view (Amable, 2016, p. 80). While functionalists underline economic rationality as a cause for institutional complementarities, the political economic approach views institutions as "sociopolitical compromises" (Amable, 2016, p. 93), blocs (Meyer & Rowan, 1977, p. 345) or coalitions (Yun, 2015, p. 5; Lechevalier et al., 2016, p. 6) that owe their place in the existing hierarchy to their political power. This power is recognized and used by the ruling elites to secure their own standing (Amable, 2016, p. 95). Whereas business is normally interested in pursuing competitive strategy, for which financial and labor deregulation are instrumental and complementary, politicians are additionally concerned with institutional rationale. In this respect, I discuss *financialization* as a project that exemplifies the reshaping of sociopolitical hierarchy in favor of financially-oriented groups.

Granting the absence of the required institutional framework for the emergence of a shareholder model in Japan, it is necessary to consider the ways to conceptualize the ongoing corporate governance reforms. Morgan & Takahashi offer a political economic explanation: "The institutional context for shareholder-value discourse has to be created and in some cases engineered into existence" (2002, p. 170). The last decade reflected continuous efforts on the part of the Japanese government (Nakamura, 2011, p. 190) and institutional (mainly – foreign) investors (Ahmadjian, 2007) to orchestrate a new shareholder-value discourse. Dore (2008, p. 1098) indicated that transition from an inward-oriented to a market-based model implies "increasing efforts on the part of government to promote an 'equity culture' in the belief that it will enhance the ability of its own nationals to compete internationally".

The recent corporate governance reforms in Japan have been primarily aimed at granting monitoring credentials of the joint-stock companies to shareholders. Enhancement of shareholders' rights is recognized as an underlying element of financialization by the critical scholars such as Lazonick & O'Sullivan (2000), Duménil & Lévy (2001), Dore (2008) and van der Zwan (2014). Lapavitsas (2011, p. 611) argues that the concept of financialization has become particularly relevant for learning the lessons of the 2007-8 financial crisis, whereby political economists have tried "to relate booming finance to poorly performing production".

In the existing scholarly literature (Dore, 2008; van der Zwan, 2014, Hager, 2015), financialization is understood as: (1) a specific regime of accumulation on the political-economic level where "profits accrue primarily through financial channels rather than through trade and commodity production" (Krippner, 2005, p. 174); (2) ascendance of shareholders' rights on a corporate level and; (3) discursive association of individual merits with ability to participate in financial markets. This study focuses on the second aspect, wherein positioning it within the wider range of critical works on political economy. "Financialization refers to the process whereby the objectives of the corporation have been increasingly narrowly defined as maximizing shareholder value through the treatment of the firm as a bundle of financial assets whose value is expressed solely through market prices at any one point in time. By contrast, stakeholder visions of the firm that see it as a community of fate which has a past, present and future that ties individuals, groups and societies into complex relationships of social and economic interdependence have been increasingly sidelined" (Morgan, 2014, p. 184). The most frequent examples of shareholder value maximization are: the usage of earnings per share as incentive plans for CEOs and

including stock prices and shareholder returns to managers' remuneration plans (Admati, 2017, p. 133).

Financialization regarded as enhancement of shareholders' rights has originated from a so-called "shareholder value ideology". The hegemonic view of respective economic and business-related studies has been centered on managers acting on behalf of shareholders rather than carrying out tasks from the point of firm-specific expedience. However, granting the existence of various types of managers' motivation not limited to maximization of returns to capital, authors such as Lazonick & O'Sullivan (2000), Hall & Soskice (2001), Dore (2008), van der Zwan (2014) and Mees (2015) criticize the agency theory for presenting shareholder model as "one-size-fits-all" and argue for the merits of institutional approach. In the heyday of the Japanese economy from 1960s till 1980s, the local corporate governance model concerned with wellbeing of various stakeholders rather than share value alone, was considered an alternative to the "Anglo-Saxon" shareholder model (Aoki, 1988). But subsequently, since early 1990s, against the background of Japan's financial bubble burst, academia has become overwhelmingly preoccupied with the "principal-agent" or "agency" theory (Dore, 2008).

The most common mechanism of allying managers with shareholders is the delegation of incentive payments to the former as a reward for corporate performance reflected in increased corporate share value. Zalewski & Whalen (2010) as well as Van Arnum & Naples (2013) have demonstrated how in the U.S. financialization understood in terms of shareholder rights' enhancement leads to a significant growth of income gap between top-managers and ordinary employees. Although Japan is characterized by considerably lower CEO compensation rates compared to other OECD states (Jacoby, 2005, p. 13), there is a growing evidence of the adoption of shareholder-centered corporate practices leading to increasing wage inequalities at large enterprises (Dore, 2007, p. 211). This problem has been described in the recent literature as a growing divergence between internationalized export-oriented companies and SMEs (Morgan, 2014, p. 190; Yamada & Hirano, 2015, p. 13). In this regard, the heightened attention to share value as an attribute of financialization is a phenomenon more likely observed at multinational companies integrated to global value chains, rather than at those relying on patient capital and targeting internal markets (Jackson, 2016, p. 7).

Formal realignment of shareholders' and managers' interests in Japan that marked the onset of shareholder-oriented reforms has formally started with the introduction of stock options in 1997 (Shishido, 2007, p. 312) and continued with "the recognition of share buy-

backs in 1998, stock swaps in 1999 and transfers of undertakings in 2001, as well as removal of the prohibition of owning own-company stocks" (Inagami & Whittaker, 2005, p. 73). Since then, share-value pursuit has become one of the top priorities of Japanese management. Furthermore, on the macro level, the level of capitalization of Japanese listed companies in one of the highest among the OECD states, as shown in Chapter 4 (see Figure 2) which shows the key role of shareholders for the national economy.

Despite these developments, most of the studies do not consider the Japanese economy as financialized. The Varieties of Capitalism scholars situate such "coordinated" systems as Japanese and German on the pole opposite to the financialized Anglo-Saxon economies (Froud, Haslam, Johal & Williams, 2000; French, Leyshon & Wainwright, 2011). While in the post-1980s period, the U.S. and the U.K. economies have moved towards finance-dominated regime of accumulation, East Asian newly industrialized countries "underwent only *neoliberal policy adjustments* within the prevailing institutional framework of their respective DSs [developmental states]" (Jessop, 2016, p. 49). As for Japan, it has faced a departure from the developmental state model toward the "knowledge-based economy" characterized by valorization of knowledge, innovation-based competitiveness, flexibilization of wages and eased monetary policies facilitating international capital flows (Jessop, 2016, p. 47).

In addition, Morgan & Takahashi (2002) present an argument about the need for institutional conditions for financializaiton. According to the authors, at time of their research publishing, these conditions were absent in Japan. Epstein (2005) and Dore (2008) also list several institutional requirements for a financialized economy. Notably, such necessary attributes as "growing dominance of capital market financial systems over bank-based financial systems" (Epstein, 2005) and "growth in and increasing complexity of intermediating activities, very largely of a speculative kind, between savers and the users of capital in the real economy" (Dore, 2008) are not characteristic to Japan (Froud, Haslam, Johal & Williams, 2000, p. 105). Jürgens, Naumann & Rupp (2000) also note that financialization is accompanied by individual and corporate participation in the stock market as well as the dominant role of equity funding for the national economy. Applying their criteria, one can conclude that while the overall role of equity finance for the Japanese economy is growing, Japanese households are quite unwilling to entrust their savings to financial markets. Moreover, corporations also remain largely adhered to bank- rather than equity-finance (TSE, 2016).

However, observed from a different angle, the situation during last two decades has changed significantly. One of the major transformations is the decline in cross-shareholding amid the drastic increase in foreign stockholding, as shown in the Tokyo Stock Exchange Shareownership Survey (TSE, 2016). It is not enough to conclude that equity market starts to outweigh bank-based finance (Epstein, 2005), but the proportion is continuously changing in favor of the former. This corresponds to the understanding of financialization by French, Leyshon & Wainwright (2011) more as a *process* than a completed event. Lechevalier, Debanes & Shin (2016) explicitly address the recently-emerged strategy of Japanese multinationals "oriented to maximize its position in global value chains" (p. 25) as a display of financialization. "Japan and Korea have experienced financialization that followed financial liberalization in the 1980s and the 1990s" (Lechevalier, Debanes & Shin, 2016, p. 4).

The presented evidence points at the deficiency of conceptualizing financialization only from the VoC standpoint. An example of the VoC oversimplified classification is the distinction between the market-based financial systems characterized by the dominant role of shareholders (as in case of the U.S. and the U.K.) and the bank-based financial systems characterized by the dominant role of banks as capital providers and monitors (as in the case of Germany and Japan). Such division can misleadingly serve as a sole criterion to ignore the development of financialization within the contexts of CMEs (Karwowski, Shabani, & Stockhammer, 2017). Furthermore, other political economic theories portray financialization as the late stage of capitalism, whereby it can only develop in economies such as of the OECD states. Karwowski & Stockhammer (2017) and Whittaker (2017) counter this assumption by demonstrating the evidence of "premature financialization" observed at companies operating in developing countries. In such cases, financialization is driven by deregulation, often pushed by international organizations such as the IMF and the World Bank, as well as by multinational corporations.

Although the immediate effects of financialization process in Japan may not yet be captured quantitively, by promoting shareholder value it has weakened institutional complementarities between industrial relations and a bank-based financial system (Deeg, 2010, as cited in Lechevalier, 2016, p. 6). "In the larger societal picture, this reduction in institutional complementarities is an important factor that has contributed to rising insecurity and constant questioning of the future of the Japanese way of life" (Chiavacci & Lechevalier, 2017, p. 7). While the idea of market for corporate control has not been accepted by the Japanese corporate environment, the current post-bubble era has marked

the acceptance of the foreign stockholding (Franks, Mayer & Miyajima, 2014, p. 46). According to the Tokyo Stock Exchange Shareownership Survey (TSE, 2016), nowadays, the largest portion of stock is held by foreign investors (29.8 percent). Their tangible presence also means the ability to exercise reputational pressure over executive directors (Dore, 2007, p. 371). Moreover, with the growing proportion of outsider investors like foreign stockholders, the possibility of their shares' selling, causing a potential hostile takeover, also grows (Dore, 2007b, p. 210). Hence, to satisfy shareholders' demands before it comes to an actual conflict, executive directors tend to increasingly prioritize share-value related indices such as return on investment (ROI), often at the expense of employees (Jackson, 2007, p. 301).

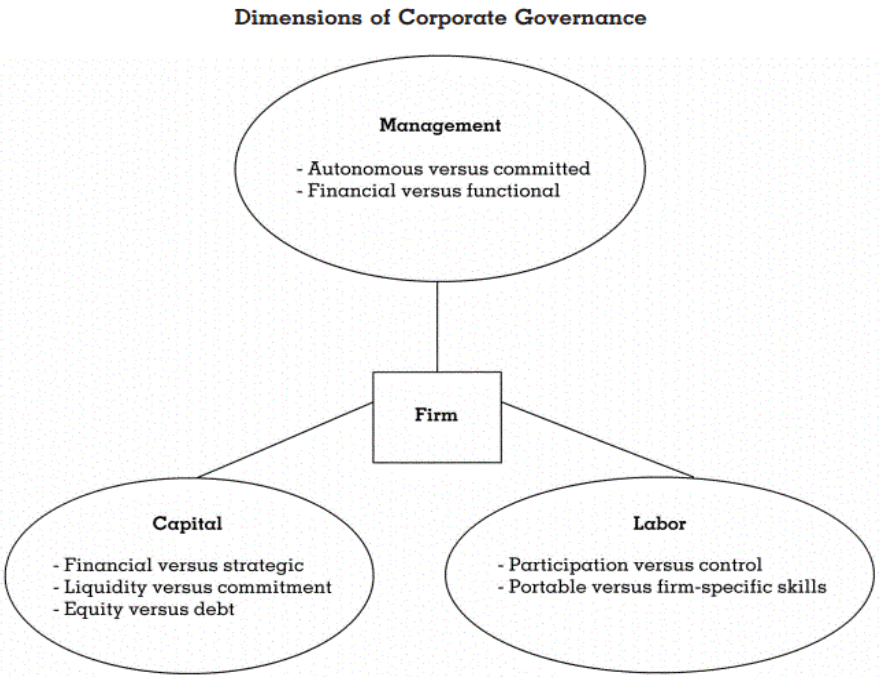

***Figure 9**. Dimensions of Corporate Governance (Aguilera & Jackson, 2003, p. 451)*

Under the influence of the ongoing financialization process, two new subcategories, "non-stable shareholders" (financial domain) and "flexible employees" (labor domain), have been excreting ever growing influence over Japan's companyist compromise starting from the late-1990s. I apply the Figure 6 "Dimensions of Corporate Governance" from Aguilera & Jackson (2003, p. 451) to illustrate the newly arisen institutional incompatibilities against the background of the ongoing changes. They exemplify an incremental departure from strategic and committed capital towards financial and liquid capital. Non-stable, mainly foreign institutional investors have become largest shareholders.

Their interest is short-term, compatible with a motivation to have higher financial returns. This can be assured by arm's-length monitoring of corporate managers by investors through annually published securities reports, the possibility of selling stock to hostile bidders, and, to a lesser extent, by outside independent directors exercising their vote at annual general meetings (Miyajima, Hoda & Ogawa, 2016).

From the institutional point of view, current corporate deregulation seems problematic due to incompatibility with a system of equitable returns to various corporate stakeholders. Throughout the last two decades, the Japanese government (Nakamura, 2016) together with foreign institutional investors (Ahmadjian, 2007) have been consistently promoting reforms of corporate governance and employment. However, the actually slow pace of reforms' implementation has been an evidence of institutional resistance against the attempts to alter the stakeholder model of corporate governance. At the same time, the insider-oriented corporate governance system itself has been clearly unable to properly react to the growing influence of market for corporate control. Consequently, the corporate finance has noticeably moved from banks to shareholders, although the former still play a dominant role (Witt, 2014, p. 4). Moreover, among the shareholders, the largest ones are currently foreigners (TSE, 2016), who belong to the group of "non-stable shareholders" due to their financial rather than strategic interests (Yoshikawa & McGuire, 2008, p. 12; Yamada & Hirano, 2012, p. 19). Therefore, despite low propensity to build institutional complementarities with other domains of corporate governance, their growing socio-economic influence has resulted in the inclusion of non-stable shareholders into current sociopolitical bloc. In a nutshell, compared to the postwar bloc geared towards egalitarian wealth distribution, the current one displays tendencies of favoring financially-oriented groups.

6.2. Decoupling

Although scholars differ in their opinions on the extent Japan's economy can be considered as financialized, they agree upon the fact that the following two distinct features of this process have been in place. Firstly, because of deregulation, the financial sector is no longer geared towards the industrial needs of the state (Lechevalier, 2016). In the postwar period, operations of main banks that provided loans to companies were regulated by the Bank of Japan as a part of a national developmental framework. Large companies, in turn, made strategic investments to enhance Japan's international competitiveness. From

the early 1980s, however, big enterprises have become less dependent on debt finance and diversified their profits by increasing reliance on equity. In turn, from the 1997 onward, the financial system has been deregulated to utilize market opportunities through investment mechanisms. Secondly, as a result, Japan's large multinational companies (MNCs) have become decoupled from the national economy. In other words, financial conditions of the MNCs improved amid the economy's sluggish overall growth (Yamada & Hirano, 2015, p. 13). This corporate cleavage that started from early 1990s, has significantly influenced the main domains of Japan's corporate governance, which are capital, management and labor. There exist different approaches to decoupling, depending on the discipline concerned.

1) From the *public policy* perspective, decoupling refers to a situation, where "the demand and supply functions remain unchanged when a package of policy measures is introduced. There is no change in equilibrium prices and quantities, and there is no difference in the response of the market to any exogenous shock arising on the demand or the supply side" (Cahill, 1997, as cited in OECD, 2001, p. 13). This corresponds to the neoclassical economic view that renders any political interference with economic equilibrium detrimental. In this case, decoupling indicates a "positive" scenario, when market laws are not affected by implementation of certain policies. In a less restrictive sense, decoupling can be linked to asymmetrical reaction of national markets to exogeneous shocks, indicating a decrease in correlation. For example, in the wake of the 2008 US subprime crisis, many developing markets did not experience same deterioration as the American markets did, although they depended on exports to the US (The Economist, 2008).

2) From the point of *corporate accounting*, decoupling indicates the situation when two assets that would have moved together under stylized circumstances, show increasing divergence, whereby the one can increase while the other decreases. One of such cases is a rise of managerial pay, amid stagnant or falling annual profit rates of a company (Tosi & Gomes-Mejia, 1989). Initially, this corresponds to the classical Berlie-Means scheme, whereby managers act as autonomous leaders without enough regard for corporate stockholders. However, since early-1990s, CEOs could enjoy high benefits leading to decoupling *due* to their alliance with shareholders. Thereby, according to agency theory, within the "shareholder (principle) – manager (agent)" contractual system, agency costs are minimized, as it is in agent's interest to partner with a principle. In this case, managers' heightened attention to shareholders' returns can result in higher premiums, regardless of a corporate financial situation, which is a case of decoupling.

Among various cases of corporate decoupling, the one involving shareholder returns on one hand, and labor policies such as employment and remuneration on the other, are of a particular interest for this research. Roberts (2001, p. 1558) argues that the intensified market discipline induces directors to prioritize dividends and share price as indicators of corporate success. Consequently, corporate expenses such as labor costs become subject to "restructuring", favored under shareholder model (Morgan & Takahashi, 2002). Hillman & Keim (2001) also describe decoupling, whereby "social issue participation is negatively related to shareholder value creation" (p. 129).

Under the shareholder model, managers are considered as interest-seekers who cannot be trusted and thus need close outside supervision ideally carried out by market forces (Lazonick & O'Sullivan, 2000, p. 16; Dore, 2007, p. 209). Lazonick & O'Sullivan (2000), Roberts (2001) and Amernic & Craig (2010) underline the manipulative and therefore ideological features of corporate accounting. For example, Roberts (2001, p. 1558) states that "intensification of market discipline produces a heightened awareness in the minds of directors of the perceived interests of shareholders reflected in dividend policy, share price, etc. It encourages directors to identify themselves with these purely financial indices of business success". For many Japanese managers, shareholder-oriented indexes represent reputational rather than competitive assets due to their institutional novelty. Such reputational pressure from an arm's-length instance contradicts to Japan's institutional setting that priorities trust-based and relational monitoring. Hence, as a reaction to institutional pressures, managers are likely to formally adhere to shareholder discipline, while practically continuing to pursue stakeholder-oriented policies. Such deviation of practices from declared aims is also called decoupling.

For Japan, in the wake of the 1990s' bubble burst, employment cuts were accompanied by reduced dividends. Furthermore, wages' reductions encompassed both managers and regular employees. "Since 1997, however, the cumulative volume of dividends paid increased by 180%, compared to a 10% decline in total salaries paid. This change may signal a shift from treating dividends as a quasi-fixed charge toward having a more variable relation with profits and negative relation to employment" (Jackson, 2007, p. 301). Dore (2007, p. 211) presents a similar evidence from 2001-2005 indicating negative correlation between dividends and remuneration: "Over the five years 2001-2005, in Japan's biggest non-financial corporations employing some 7 million workers, average worker remuneration fell by 6% while directors' salaries and bonuses rose by 97% - their reward for raising dividends by 174%. A vastly different story from the last recovery from

recession 1986-1990 when the figures were, respectively, plus 19%, 22% and 2%". Miura (2008, p. 166) comes up with the similar findings: "The level of salaries for employees in 2005 was about 90% of that in 1997. In contrast, during the same time period, dividends increased by 237%, salaries for directors by 12%, and bonuses for directors by 295%".

3) Decoupling is also viewed as a *corporate strategy* aimed at concealing the hardships arising from implementing conflicting claims of stakeholders. Companies pursue it by exhibiting a generally approved behavior and "protect their formal structures from evaluation on the basis of technical performance" (Meyer & Rowan, 1977, p. 357). Thereby, organizations secure their institutional uniformity without necessary demonstrating effective actual performance. The reason for playing this double game is primarily to attain legitimacy by adhering to established rules. Regarding corporate governance of stock-listed companies, decoupling becomes ever more widespread strategy in face of the increasingly important role of reputational assets. For example, Fiss & Zajac (2004, p. 523) measure the degree of German public companies' decoupling by estimating the difference between espousal to and implementation of core practices related to shareholder value management.

Whereas the "market evaluation" is quite an ambiguous term, it displays itself in specific accounting indices that influence corporate stocks and, hence, ensure investors' trust. The rise in stock prices is often accompanied by stagnant dividends and low corporate earnings (Goldstein, 2012, p. 277). Thus, modern companies often downplay long-term effectiveness that relates to corporate growth while concentrating on shareholders' revenue, which merely indicates a short-term profitability. For example, Yamada & Hirano (2015, p. 9) point at the fact that from late-1990s, Japanese companies have been constantly paying attention to shareholders' dividends that did not fluctuate along the changes in net income.

Recent scholarship provides further insights on decoupling in the East-Asian context. Lechevalier, Debanes & Shin (2016) argue that from 1980s onward, financial sectors of Japan and South Korea have become decoupled from the national industrial policy. This has had significant consequences for large corporations. During the postwar period, they were embedded into a relational business-financial system, which provided large export-oriented companies with financial support through a system of partner banks, and, on the other hand, directed their investments into specific niches to contribute to national competitive advantage. With the weakening of this business-finance nexus, large companies became less dependent on a national industrial policy, which allowed them "to allocate resources based on corporate strategy mainly oriented to maximize [their] position in global value chains" (Lechevalier, Debanes & Shin, 2016, p. 25).

Yamada & Hirano (2015, p. 13) also relate the decoupling of Japanese multinationals to their ability to allocate resources worldwide in response to market challenges, which has helped them to alleviate the consequences of the 1990s' bubble burst. On the contrary, internally-oriented companies have been much more dependent on partner banks and less capable of issuing equity, which would potentially improve their accounts. Hence, while MNCs have been increasing their internal reserves by issuing stock and investing overseas, national companies have been mostly concerned with repaying debts, which made their growth almost negligible – much in line with the sluggish growth of Japan's GDP during the last three decades. Thus, amid the falling Japanese exports, the improving accounts of Japanese MNCs provide evidence of their decoupling from the national economy.

6.3. Assessment of Financialization

In this subsection, I make use of different approaches to financialization to test whether Japanese listed companies have been subject to this process. Following the methodology of Dore (2007), Jackson (2007) and Miura (2008), I have calculated the average growth rates of labor costs, directors' bonuses and dividends for the Nikkei Index 400 constituencies. Furthermore, I calculated the proportion of financial to non-financial income. Finally, I measured the productivity growth rates and compared them to labor cost growth rates. I performed these procedures with the help of the *dplyr* R package (Wickham, Francois, Henry & Müller, 2017). I used NEEDS FinancialQUEST database to collect my data. The growth rates are computed throughout the period of 2010-2017. The descriptive statistics of variables used to test the hypothesis about financialization are presented in the Table 1 (built with the *stargazer* R package (Hlavac, 2018)).

Descriptive statistics

Statistic	N	Mean	St. Dev.	Min	Median	Max
Labor Cost	878	462.575	3,409.401	0.0004	1.690	46,062.000
Directors' Bonuses	738	131.154	114.619	1	99	1,101
DPS	1,825	231.515	1,136.208	0.000	30.000	16,000.000
Productivity	1,820	45.561	36.928	4.091	33.844	261.898
Financial Income	1,782	0.056	2.159	−87.984	0.062	14.792

***Table 1**. Financialization Variables: Descriptive Statistics*

The growth rates for the variables indicative of financialization or its absence thereof are following:

Variables	Growth Rates
Labor Cost	-0.02735
Directors' Bonuses	0.227609
DPS	0.146392
Productivity	0.026449
Financial Income	0.123722

Table 2. *Growth Rates*

As seen from the Table 2, while the labor costs have decreased, on average, by 2.735 percent from 2010 till 2017, directors' bonuses and dividends increased by 22.76 and 14.55 percent respectively. These results confirm the hypothesis about the wealth redistribution in favor of investors and CEOs, while the salaries of factory workers remain stagnant or even display a slight negative growth. Selective allocation of benefits to the market-oriented actors is one of the attributes of financialization. Figure 10 summarizes these disparities industry-wise.

Next, I test the definition of financializaton offered by Krippner (2005). She states that the most adequate measure of corporate financialization is the ratio of portfolio income to cash flow (Krippner, 2005, p. 182). I calculated this ratio of financial income based on the financial data of Nikkei Index 400 companies. On one hand, the yearly average proportions of financial income for the Nikkei Index 400 companies have remained around ten percent throughout 2008-2017 (own calculations). Hence, the answer to the question of whether the Japanese economy has become financialized cannot be inferred from this ratio alone. However, as seen from the Table 2, the average growth rate of financial income per company throughout 2010-2017 is 12.4 percent. It shows that listed companies tend to increasingly prioritize financial activities over productive.

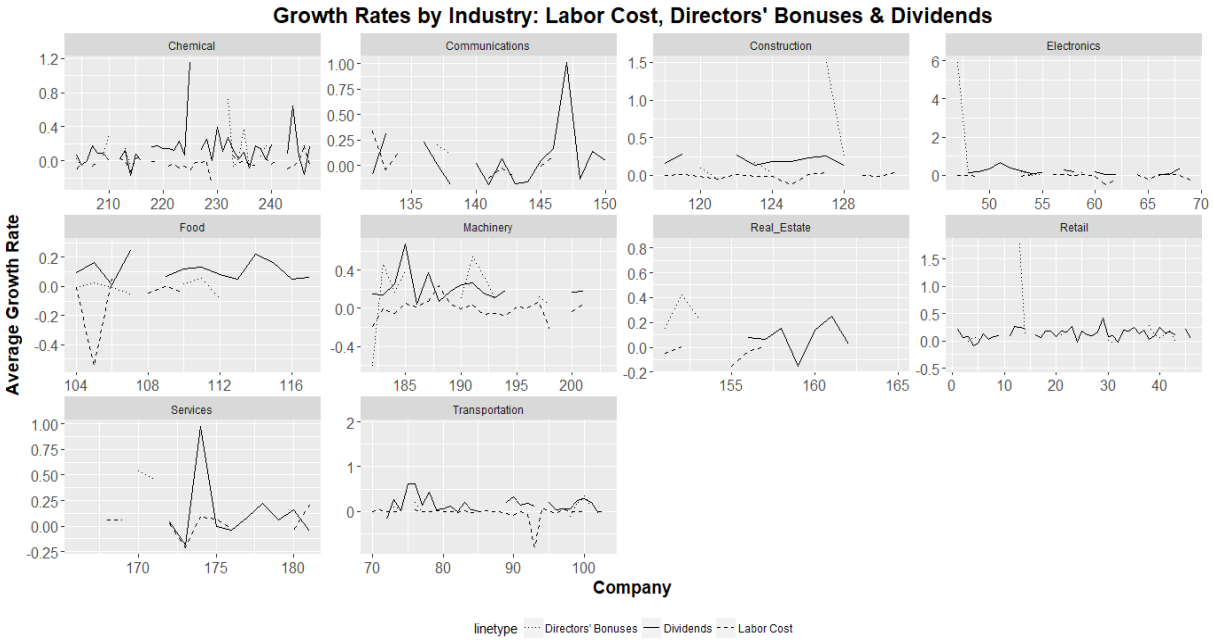

Figure 10. *Growth Rates by Industry: Labor Cost, Directors' Bonuses & Dividends*

Lastly, I compare the growth rates of labor costs and productivity. According to the regulation school, the similarity in the trends of these two variables would show a presence of a Fordist or post-Fordist compromise (Tohyama, 2012). However, as Table 2 shows, the dynamics of labor costs significantly lag behind the productivity increments. This can be interpreted as a decoupling, whereby better average performance by workers (measured as net sales per employee) do not translate in salary increases. In turn, the additional output per employee is counted towards corporate revenue, which can be instrumental for achieving competitive advantage. It is yet another sign of financialization seen as "a disconnection of wages from productivity growth" (Palley, 2007, p. 3). Figure 11 demonstrates the gap between labor costs and productivity pertaining to all industries.

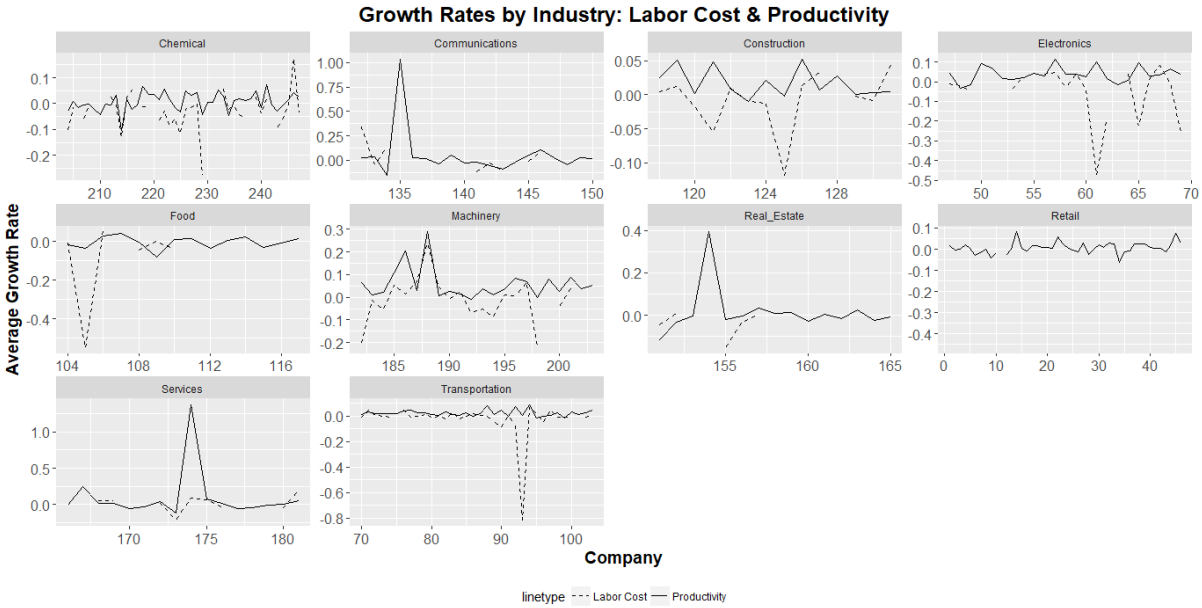

Figure 11. *Growth Rates by Industry: Labor Cost & Productivity*

6.4. Shareholder Value and Nonregular Employment

A systemic view on the simultaneous changes in corporate governance and employment system is provided by the "*institutional complementarity*" hypothesis. According to one of the general definitions given by Crouch et al. (2005, p. 359), it refers to a situation "where components of a whole mutually compensate for each other's deficiencies in constituting the whole". Masahiko Aoki (1994), who was the first to formulate the hypothesis, used it for explaining the institutional fit between contingent monitoring conducted by main banks and long-term employment relations in Japan. It is central to this study due to its ability to capture the link between corporate governance deregulation and labor reform. In agreement with this thesis, the predominance of the in-house careers and the resulting high cost of job loss are institutionally complementary with long-term commitments toward employees and corporate welfare spending (Tohyama, 2012, pp. 85-86).

At the same time, those Japanese companies that have been most eager to implement shareholder-oriented policies since 1990s, have loosened employment guarantees due to ascendance of shareholder value along the hierarchy of corporate priorities (Jacoby, 2005, p. 65). In order to both preserve institutional integrity and pay tribute to shareholders' interests, employers have combined the retained guarantees for the core workforce with increased numbers of nonregular employees. By breaching the formerly encompassing management-labor compromise, directors have thereby

discouraged employees from demanding the expansion of welfare spending (Tohyama, 2012, p. 86). Van der Zwan (2014, p. 109) covered this emerging phenomenon of the "work bifurcation", meaning the growth in managerial rewards is combined with general decline in working conditions.

The Japanese Institute for Labor (2010, p. 106) also highlights the connection between growing shareholders' pressure and incremental change in the human resource management, whereby seniority-merit and long-term employment are likely to decrease. Dore (2007b) comes up with the argument about fundamentally conflicting interests of shareholders and employees resulting from the ongoing reform. Jackson (2007, p. 292) formulates a similar thesis about an increasing role of market for corporate control in the shrinking proportion of core employees. Watanabe (2015, p. 59) applies an integral framework, arguing that financial / corporate deregulation on one hand, and labor deregulation on the other, are inseparable parts of a strategy aimed at "increasing functional flexibility and lowering production costs" (Watanabe, 2015). Abe & Hoshi (2007, p. 272) discover the complementarity between firm-centered employment and bank finance on one hand, and individual-centered employment and stock finance on the other. Conrad (2009, p. 129) considers the possibility of shareholder-oriented reforms resulting in a spread of pay-per-performance system, however does not come up with a definite conclusion.

On the international level, Darcillon (2015) establishes a positive correlation between preferential shareholders' treatment (independent variable) and worsening conditions of blue-collar labor (dependent variable) across OECD states. Dore (2008, p. 1108) asserts the link between growing shareholders' power and decreased employees' tenure resulting from the intensified pressure from investors. Van der Zwan (2014, p. 102) underlines ideological nature of financial reorientation towards shareholders that represents capitalist control mechanism. Aglietta (2000, p. 156) describes a tendency towards labor bifurcation in the US, whereby lower remuneration for core as well as flexible employees is compensated in relation to the former group through stock-options' provision. Through application of institutional complementarity model, Amable, Ernst & Palombarini (2005) link low pressure from capital markets to cooperative management-labor bargaining and vice versa. This view is based on the notion that long-term "company-growth" strategy usually results in lower stock-prices making a firm subject to potential hostile takeovers. Therefore, such strategy is more efficient and safe under low dependence on market, which is the case of bank finance as opposed to equity finance. Contrary to that, shareholder-oriented companies are subject to more immediate challenges that require focusing on

profitability rather than long-term growth. Under these circumstances, management would be less willing to reinvest profits into corporate growth in general and to allocate it to employees (Höpner, 2005, p. 339).

However, as an example of Germany demonstrates, the shareholder orientation strategy may paradoxically be in the interest of labor. Höpner (2005, p. 348) presents an evidence about shareholder-induced accounting transparency being a leverage for the employees in their negotiations with managers. Jackson (2005, p. 423) also argues that "greater checks and balances and better information may enhance the prospects for voice by both investors and employees". According to the 2010 JILPT survey (JILPT, 2010, p. 111), 55 percent of employees, as opposed to only 13.5 percent of managers, welcomed a reorientation towards shareholder-value enhancement.

The difference between Japan and Germany is that the latter has an institutional arrangement called "codetermination". It makes a presence of labor representatives at the supervisory board of directors a rule, as opposed to Japan, which is also considered a "coordinated market economy" (CME) according to the varieties of capitalism (VoC). In this regard, critical studies on institutional complementarities have empirically refuted the VoC basic assumption that only similar-type (coordinate or liberal) synergies can yield positive outcomes (Aguilera & Jackson, 2003). Moreover, Witt & Jackson (2016) have proved that within the CMEs' context, comparative institutional advantage is often achieved through introduction of liberal features. The same holds true for the introduction of coordinated features to LMEs' environment under certain institutional conditions. Some famous examples include combination of strong social protection and external labor mobility in Denmark (Campbell & Pedersen, 2007, as cited in Jackson, 2016, p. 11) as well as coexistence of shareholder orientation with management-labor co-determination at large German companies (Crouch et al. 2005, p. 364).

Although differently from the German "paradox", the example of prewar Japanese companies also refers to institutional complementarity between coordinated capitalism and shareholder-oriented corporate governance. As mentioned in the introduction, Japan's community company has retained some salient features against the change from equity to bank finance during the postwar era. Firstly, although shareholding was dispersed at the beginning of XX century, institutional stockholders were stable, thereby acting as obstacles to potential hostile takeovers (Dore, 2007, p. 378). The postwar increase in cross-shareholding meant as poison pills has had a similar aim. Secondly, the monitoring was predominantly insider-based. With corporate finance and management being unseparated

in the prewar period under *zaibatsu* model, boards' majority was occupied by largest shareholders. The latter also acted as market agents, thereby ensuring trust between corporate management and outside investors (Franks, Mayer & Miyajima, 2014, p. 25). In turn, under the conditions of holding companies' ban in the postwar era, insider monitoring has been ensured by main banks that are also considered as insiders, due to their long-term commitments to partner companies. Likewise, in the modern era, despite a diminishing rate of cross-shareholding and bank finance, boards of Japanese companies are overwhelmingly insider-oriented. Thus, with the growing role of equity financing, market for corporate control has not been excreting its influence through the outsider board majority (Hoshi & Kashyap, 2004).

The above-described coordinated system has been also complemented by long-term contracts with employees aimed at their acquiring of firm-specific skills. However, the nature of a well-known postwar institutional complementarity between patient capital and lifetime employment in Japan was not deliberately engineered but was rather a result of an "unintended fit" (Aoki, 1997). Whereas the main bank system emerged after the World War II as a part of a national developmental strategy, large enterprises have been promoting in-house careers from around 1920s with the purpose of long-term shop-floor training among employees (Amable, 2016, p. 85). Nishiguchi (1994, pp. 21-22) presents evidence of postwar market duality, whereby large manufacturing sectors offered long-term contracts and the rest of the labor markets were characterized by high levels of turnover. Therefore, applying the distinction of Witt & Jackson (2016, p. 781), one can argue that although the postwar institutional complementarity in Japan was organized along the lines of coordinated coherence, the prewar complementarity was based on beneficial heterogeneity. Thus, current ascendance of market for corporate control can potentially be integrated into the coordinated capitalist framework. "The idea is that importing foreign part into a given (productive) system leads to an adjustment of the imported parts and the importing system to one another. In this perspective, hybridisation is not a loss of systemic coherence, but the creation of new complementarities" (Amable, 2016, p. 89).

Granting these specific institutional arrangements, the link between market pressure and growing labor bifurcation at Japanese listed enterprises is not that obvious. To bring it to light, one should account for possible variables indicating the growing priority of corporate profitability over growth. Based on the existing literature, I infer that political pressure and increased foreign shareholding have been crucial factors in this respect. With the account of these control variables, the positive correlation between shareholder value

and nonregular employment would indicate a decline of Japan's stakeholder model of corporate governance. Put differently, the growing proportion of nonregular employees would be a negative externality of the nexus between shareholder finance and entrenched political and business institutions.

6.5. Statement of Hypotheses

Shareholder value (SV) is a concept that is not institutionalized in the corporate law but is rather a display of a conventional view of a company as shareholders' property. If managers fail to deliver substantial shareholder returns, their companies become naturally subject to claims of rival investors that can buy a large enough proportion of devaluated corporate stock to get voting rights at annual general meetings. In case they acquire most of shares without primary consent from other investors and CEOs, thereby acquiring a tool for replacing incumbent management, this move is called "hostile takeover". SV concept originated from the hostile takeover movement that took place in the Anglo-Saxon world during 1970-80s (Deakin, 2005).

In the early 1990s, SV became a dominant managerial ideology representing the departure from the view of managers as public servants bearing social responsibilities, towards the model of managers being merely agents of corporate shareholders (Inagami & Whittaker, 2005, p. 70; Dore, 2008, p. 1103). One of the main features of large listed companies is the separation of management from ownership, according to a famous Berle-Means observation. These authors of the 1932 book "The Modern Corporation and Private Property" pointed at the fact that corporate managers do not necessarily share stockholders' interest in share-value-maximization (Gilson & Roe, 1993, p. 876). Since dominant "agency theory" views shareholders as "principles" and "managers" – as their "agents", managerial actions that cause losses on the side of shareholders are regarded as "agency costs" Therefore, the trade-off between corporate owners and management, where agency costs are minimized, is considered as a key to the "agency problem" for a joint-stock company.

Shareholder-oriented governance is preoccupied with short-term returns, which pursuit can lead to unfavorable wealth redistribution to stakeholders other than shareholders. This is called the "downsize and distribute" regime (Lazonick & O'Sullivan, 2000, p. 18). Potentially seen as lacking social dimension by such firm's stakeholders as employees, this model legitimizes itself through a codified "technique of governance" thereby substituting

the ethics of stakeholder model (Gomez & Korine, 2005, p. 741). It also implies the separation of powers – with executive directors (managers) being monitored by non-executives (outside directors) – to ensure corporate transparency. Arm's-length supervision by outside directors is a well-known mean for minimizing agency costs in the Anglo-Saxon world.

The described shareholder model has not been institutionally rooted in Japan. It is rather characterized as a "stakeholder" (Dore, 2007, p. 211) or "pluralist" (Inagami & Whittaker, 2005, p. 77) model of corporate governance. In line with it, the task of Japanese companies is to maintain long-term commitments to banks, suppliers, employees and customers rather than to simply maximize share-value (Abbeglen & Stalk, 1985). Under this model, accountability can be ensured through relational rather than arm's-length monitoring. Whereas the latter is carried out by outside shareholders, the former, in case of Japan, has been sustained through a main bank system. The main bank monitoring is based on principles of the lasting partnership that ensures mutual trust between corporations and lenders of capital.

However, after the bubble burst in early 1990s, the fall in corporate share-prices led to diminishing rates of cross-shareholding. In turn, foreign investors with financial rather than strategic interests took advantage of a situation by acquiring large portions of stock at Japanese companies. Subsequently, starting from the 2002 Commercial Code reform, government has been consistently promoting shareholder-value orientation for joint-stock companies. Although in practice, Japanese companies have been unwilling to accept new rules of the game, against the background of the unfolding crisis, the gradual reorientation towards outside investors became "reluctantly accepted as inevitable" (Jürgens, Naumann & Rupp, 2000, p. 55). Since institutional foundations of Japanese companies are different from Anglo-Saxon principles, their shareholder value pursuit and resulting externalities requires a detailed analysis.

There are basically two different approaches to shareholder value (SV). One (1), advocated by "*agency theory*" representatives (Friedman, 1970; Jensen & Meckling, 1976; Rappaport, 1986, Stewart, 1991), argues that a joint-stock company is solely a property of its stockholders. Managers are stockholders' agents whose function is to maximize SV under contractual obligations toward principles – stockholders. However, large Anglo-Saxon corporations are characterized by dispersed shareholding, which precludes investors from exercising their rights through general shareholders' meetings. Thus, as managers become more autonomous, they claim higher rewards and credentials. If this is achieved at

the expense of shareholders' returns, their actions are believed to cause "agency costs". To lower them, stock-listed companies must comply with accounting standards, such as U.S. Generally Accepted Accounting Principles (US-GAAP), International Accounting Standards (IAS) or Financial Accounting Standards (FAS) called to enhance corporate transparency (Fiss & Zajac, 2014, p. 514; Yonekura, Gallhofer & Haslam 2012, p. 322). Japanese stock-listed companies have been advised to use International Financial Reporting Standards (IFRS) by the Tokyo Stock Exchange in 2010. As of June 2017, 150 companies have decided or planned to adopt IFRS (JPX, 2017). Hence, even under the absence of direct shareholders' supervision, CEOs are pushed to achieve higher returns to shareholders to sustain a competitive race. Therefore, agency theory emphasizes a dogmatic task of CEOs to maximize SV, which is believed to be a primary task of a joint-stock company.

Since outside directors do not play a substantial role in Japan's corporate governance (only 2.5 percent of TSE 1st and 2nd section companies have adopted a U.S.-style "company-with-three-committees" that requires the majority of outside directors) Japan is a good case study to test the effects of SV implementation through accounting metrics. Japan Revitalization Strategy (2013, p. 5) stresses the foundational role of Return on Equity (ROE) as a crucial index to be pursued by mangers for improving corporate productivity. Inagami & Whittaker (2005, p. 79) found out that Japanese CEOs are giving increasing priority to ROE due its ability to capture the efficiency of capital use against shareholders' investment. Therefore, according to Ito (2014, p. 56), "ROE improvement can be regarded as the core of the third arrow of Abenomics". Although there is a clear awareness of the ongoing prioritization of ROE for Japanese stock-listed companies (Milhaupt, 2017, p. 13), agency theory does not question the implications of growing SV for labor policies. Sato (2000, as cited in Inagami & Whittaker, 2005, p. 84) measured the influence of ROA and EVA (economic value added) on lifetime employment policy but did not touch upon the issue of nonregular employment. One possible reason for the neglect of this aspect is that drastic increase in temporary employment occurred mainly during the recent decade and was quite a novel issue back in 2000. Another explanation is the problem of collecting data about nonregular employment, which is a significant impediment for the labor-related research. Listed companies have started to publish the respective data in annual securities reports only from 2008. Furthermore, it has been included in major corporate surveys and financial databases from 2010 (Lechavalier et al., 2014, p. 18).

Although being empirically contested term, SV matters for market evaluation and, therefore, reputation of a firm. Aglietta (2000, p. 149) argues that shareholders' pressure

exerted over management does not stem from individual evaluations of each company, but is rather a result of market projections. Though the latter are largely of a speculative kind, they produce unified metrics for investors to access the performance of firms included into their financial portfolios. Hence, expectations of profits reflected in corporate stock price, can become more important than the actual profits themselves. In this respect, "institutional isomorphism" (DiMaggio & Powell, 1983) is instrumental for bridging reputational and competitive assets of companies. One should remember, however, that institutional isomorphism brings competitive advantage not in a sustainable way and only by virtue of ceremonial, not actual, performance. It is directly related to corporate strategy of minimizing agency costs through shareholder-oriented corporate governance reforms (Aglietta, 2000, p. 154). While including several measurements for SV used in previous literature (see below), this research is novel for including an additional proxy for SV, which is "stock owned by directors". The following hypothesis aims to link SV with nonregular employment.

H1: *Higher levels of SV are associated with higher proportions of nonregular employment.*

The second (2) view on SV is more critical. According to it, SV has become a highly contested concept due to widespread attempts to adhere to its standards by coordinated market economies (CMEs) of continental Europe and East Asia (Jürgens, Naumann & Rupp, 2000). The pursuit of SV as a primary goal of a public company in the Anglo-Saxon context is very different from the stakeholder model of corporate governance (CG) of CMEs that considers interests of "shareholders, employees, creditors, customers, and the society in which the corporation resides" (Fiss & Zajac, 2004, p. 501). Thus, managerial merits under stakeholder model are not confined to SV returns. Moreover, managers experience less pressure from capital markets: their motivation rather stems from long-term commitments to company. On contrary, CEOs in the shareholder model are mainly disciplined by the threat of hostile takeovers if they fail to meet investors' demands (Deakin, 2005, p. 15; Mitchell, O'Donnell & Ramsay, 2005, p. 475). As a result, while following the task to raise SV, managers commonly resort to restructuring through labor cuts (Darcillon, 2015). Dore (2008, p. 1108) asserts the link between growing shareholders' power and decreased employees' tenure resulting from the intensified pressure from investors. Against these societal externalities, there is a logical question about reasons for introducing shareholder features to stakeholder model. A possible prerequisite is a crisis of a national

CG, which requires an adoption of a popularly-acclaimed alternative. In this case, sufficient analysis of compatibility with local institutions is often missing.

Lazonick & O'Sullivan (2000) emphasize that understanding of the SV concept is impossible without the study of its repercussions in the US context, from which it has originated. Its essence can be described as the departure from "retain and reinvest" to "downsize and distribute" strategy, under which CEOs undertake frequent labor cuts as means to achieve higher returns on equity (Lazonick & O'Sullivan, 2000, p. 16; Goldstein, 2012, p. 272). Otherwise, if employers avoid massive layoffs, they choose instead to cut wages and make employment more flexible (Lazonick & O'Sullivan, 2000, p. 29). Furthermore, SV is driven by "(1) investor dominance and the use of financial markets to discipline corporate activities, (2) financial conceptions of control that stress stock performance and rate of return over alternative performance metrics such as growth, (3) a strategic emphasis on cost-cutting and short-term profits, and (4) streamlined organizational structures and a focus on core competencies" (Goldstein, 2012, p. 270).

Amid a prolonged economic slowdown that started from early 1990s, Japanese government has addressed the issue of corporate governance reforms as a milestone for increased returns to shareholders and thereby – improvements of corporate accounts (Japan Revitalization Strategy, 2014, p. 3). However, it remains unclear how shareholder welfare can bring about corporate and national revitalization. As mentioned above, the original intention of shareholder-oriented corporate governance reforms was to discipline managers who, in their capacity of agents, breached obligations given to shareholders and appropriated part of their welfare. While this was the case of adopting Sarbanes-Oxley regulation in the US in 2002, Japan's corporate governance legislations were mostly aimed at encouraging CEOs to take more risks by aligning with shareholders (Japan's Corporate Governance Code, 2015, Principle 4). Thus, as opposed to the US, corporate governance reforms in Japan are driven not by corporate scandals (Japan's Corporate Governance Code, p. 3), but rather by the lost trust in local institutions and the influence of policy-makers with American MBAs (Dore, 2007b, p. 209).

This gives yet another reason to critically examine the adoption of SV in Japanese case due to salient stakeholder features of the local CG. Several studies confirm negative correlation of the SV pursuit and labor costs in Japan. Those Japanese companies that have been most eager to implement shareholder-oriented policies since 1990s, have loosened employment guarantees due to ascendance of SV along the hierarchy of corporate priorities (Jacoby, 2005, p. 65). Whereas in the postwar period "the relationship between workers

and managers was primary, and that between shareholders and managers was secondary", this order has been reversed from the late 1980s (Yamada & Hirano, 2015, p. 14). Against economic slowdown in 1990s that followed the bubble burst, employers and business have eventually pushed for abandoning the annual negotiations with labor through *shunto* rounds (Uemura, 2002, p. 120), which caused steady decrease in welfare spending (Tohyama, 2012, p. 86).

This research shares the critique of the second approach to SV, however, aims to highlight some missing points. Available analyses of the SV have not come up with robust explanations that would account for Japan's institutional features. In other words, existent literature does not provide a satisfactory answer to the question of why Japanese employers have decreased labor costs not through massive layoffs and overall flexibilization of labor conditions (which is the case of neoliberal policies in the West), but through increasing the proportion of nonregular employees amid retention of preferences for core workers. The basic answer is a tactic of killing two birds with one stone: *preserving institutional integrity while at the same time paying tribute to shareholders' interests*. In order to prove this statement, an appropriate framework is required.

The offered theory is a *political economic* analysis of institutions that employs institutional complementarity hypothesis. It is particularly well-suited for explaining institutional change like the one where elements of shareholder model are adopted in a stakeholder environment (Jackson, 2016, p. 7). Political economic approach defines institutions as "political compromises among different interest groups that form sociopolitical coalitions to advance their interests" (Lechevalier, Debanes & Shin, 2016, p. 6). It is based on the concept of "coalition" developed by Höpner (2001, 2005), Aguilera & Jackson (2003) and Jackson (2005). Recently, Lechevalier, Debanes & Shin (2016) as well as Yamada & Hirano (2015) and Jackson (2016) have linked the institutional complementarity "coalition" concept to political economic theory to address the issue of institutional change in Japan. While their analysis is yet preliminary, current research incorporates and tests the view about the pursuit of SV being a political project aimed at power accumulation (Amable, 2016, p. 93).

As shown in the Table 3, the newly introduced elements of Japan's corporate governance are "non-stable shareholders" and "flexible employees". They are so far characterized by an absent or limited ability to build complementarities with other elements. However, against the crisis of a previous bank-centered system, the role of these parties becomes key for maintaining current sociopolitical bloc. Here, as mentioned in the

beginning of the chapter, institutional hierarchy plays a key role in the formation of a dominant sociopolitical bloc. “For a group, hierarchically superior institutions are those that matter most for their interests… [Their] alteration would imply challenges to the existence of the dominant social bloc” (Amable, 2016, p. 95). In this regard, non-stable, namely foreign shareholders appear on top of the current sociopolitical hierarchy, whereas nonregular employees, although growing in numbers, serve merely as a buffer against distortions threatening the bloc.

		Labor		Management		Finance	
		Core employees	Flexible employees	Executive directors	Non-executive directors	Non-stable Shareholders	Banks
Labor	Core employees		New			New	
	Flexible employees			New	New	New	New
Management	Executive directors					New	
	Non-executive directors					New	
Finance	Non-stable Shareholders						New
	Banks						

Ability to build coalition.

Limited ability to build coalition

Inability to build coalition

***Table 3**. Institutional Complementarities of Corporate Governance in Japan*

To incorporate the political dimension into the analysis of SV repercussions for labor, I inquire, in whose interest the enhancement of shareholders’ rights is. As already mentioned, CG reforms are a part of the governmental agenda, formulated in Japan’s Revitalization Strategy (JRS) (2013). Therefore, CG changes promoted by the Cabinet Office are likely to influence the achievement of higher SV returns. According to the government’s view, the targeted companies are primarily the ones included into the Nikkei Index 400 created in 2014 and described in JRS as one of the “initiatives aimed at enhancing the competitiveness of companies” (JRS, 2013, p. 76). The index is based on such quantitative achievements as: three-years average ROE and operating profit, as well as market value (JPX-Nikkei Index 400 Guidebook, 2016, p. 11). Major qualitative

requirements are: an appointment of at least two independent outside directors, and an adoption of IFRS (International Financial Reporting Standards) (JPX-Nikkei Index 400 Guidebook, 2016). Thus, to account for political influence, I include parameters such as: inclusion into Nikkei Index 400, and the shareholding proportions by various groups. Similar methodology was applied in the studies of Abe (2002), Sakai & Asaoka (2003), Abe & Shimizutani (2005), Ahmadjian & Robbins (2005) and Yoshikawa, Phan & David (2005).

An influential actor that has advocated shareholders' rights is foreign investors. Currently, they hold the largest proportion of stock – 29.8 percent (TSE, 2016). Moreover, Japanese companies with higher levels of foreign stockholding are characterized by higher risk-taking propensity (Yoshikawa, Phan & David, 2005, p. 282; Nakano, Otsubo & Takasu, 2014, p. 21) and downsizing in the attempts to maximize SV (Ahmadjian & Robinson, 2001, p. 630; Ahmadjian & Robbins, 2005, p. 460). Conversely, domestic ownership proportion (*DO*) (Abe & Shimizutani, 2005; Yoshikawa et al., 2005, p. 282) and ownership concentration (*OC*) (Fiss & Zajac, 2004, p. 517; Witt & Jackson, 2016, p. 790) are associated with strategic rather than financial interests. Among others, "cross-shareholding is expected to have a negative influence on the speed of the employment adjustment, as firms with higher cross-shareholding ration feel less pressure" (Lechevalier et al., 2014, p. 13).

H2: *Foreign shareholding is positively correlated with proportions of nonregular employees at Nikkei Index 400 firms.*

Next issue that this study aims to tackle is the repercussions of pursuing SV for sustainable corporate performance. Although higher SV returns are beneficial for shareholders, it remains unclear, whether other corporate actors and national economy can benefit from it. It was mentioned earlier that CG reforms are key to Japan's structural transformations according to the official agenda. However, the evidence suggests that higher levels of SV are not accompanied with comparable corporate profits and wages. For example, Yamada & Hirano (2015, p. 9) point at the fact that from late-1990s, Japanese companies have been constantly paying attention to shareholders' dividends that did not fluctuate along the changes in net income. On the labor side, in the wake of the 1990s' bubble burst, employment cuts were first accompanied by reduced dividends. Furthermore, wages' reductions encompassed both managers and regular employees. However, since 1997 "the cumulative volume of dividends paid increased by 180%, compared to a 10%

decline in total salaries paid. This change may signal a shift from treating dividends as a quasi-fixed charge toward having a more variable relation with profits and negative relation to employment" (Jackson, 2007, p. 301). Dore (2007, p. 211) and Miura (2008, p. 166) present a similar evidence from 2001-2005 indicating negative correlation between dividends and remuneration.

Thus, the reasons for companies to pursue SV might not necessarily be purely economic. Rather, companies aim to "protect their formal structures from evaluation on the basis of technical performance" (Meyer & Rowan, 1977, p. 357). Thereby, organizations secure their institutional uniformity without necessary demonstrating effective actual performance, which is a case of *decoupling*. This strategy is followed to attain *legitimacy* by adhering to established rules. Regarding corporate governance of stock-listed companies, decoupling becomes ever more widespread strategy in face of the increasingly important role of reputational assets. Thus, competitive advantage is achieved not in a sustainable way but by virtue of ceremonial rather than actual performance. It is directly related to corporate strategy of minimizing agency costs through shareholder-oriented CG reforms (Aglietta, 2000, p. 154).

The previous literature accounts for organizational size, age, reputation, wages, foreign ownership (Ahmadjian & Robinson, 2001, pp. 629-30) and board size (Abe & Shimizutani, 2005, p. 19) as key determinants of corporate legitimacy in the Japanese context. This research comes up with yet another proxy for reputation, which is the inclusion into Nikkei Index 400. This index is even referred to as "shame index" for its utmost reputational importance for large companies (Patrick, 2016, p. 16).

The presented evidence about the importance of reputational assets for Japanese listed companies being relevant, requires an important clarification that deals with macro-level. A key economic reason for implementing the CG reforms agenda has been the shrinking domestic market that has induced companies to search for export-oriented strategies (Milhaupt, 2017, p. 3). In other words, internationalization has been regarded as a means for sustainable corporate growth. In order to attract more investment and be able to expand globally, companies need to adhere to recognized accounting and CG standards. However, not all the firms have succeeded to internationalize. With the weakening of business-finance nexus in early 1980s, large multinational companies (MNCs) became less dependent on a national industrial policy, which allowed them "to allocate resources based on corporate strategy mainly oriented to maximize [their] position in global value chains" (Lechevalier, Debanes & Shin, 2016, p. 25). This has helped them to alleviate the

consequences of the 1990s' bubble burst (Yamada & Hirano, 2015, p. 13). On the contrary, internally-focused companies have been much more dependent on partner banks and less capable of issuing equity, which would potentially improve their accounts. Hence, while MNCs have been increasing their internal reserves by issuing stock and investing overseas, domestic-oriented companies have been mostly concerned with repaying debts, which made their growth almost negligible. Furthermore, Yamada & Hirano (2012, p. 20; 2015, pp. 8-9) and Aoyagi & Ganelli (2015, pp. 109-10) corroborate that corporate productivity in Japan has outstripped labor costs, thus breaching former management-labor compromise.

In their similar study, Yoshikawa et al. (2005, p. 287) used return on assets (ROA) as a moderating variable reflecting firms' performance. Other moderating variables include *capital intensity*, measured as proportion of R&D expenses, and the "degree of internationalization" (*DOI*). The proxy for DOI is FSTS (Foreign Sales as a Percentage of Total Sales), which is the most common method used in previous studies (Sullivan, 1994). Capital intensity is supposed to be negatively correlated with proportion of nonregular employees (Lechevalier et al., 2014, p. 12). In turn, DOI is regarded in the literature as a stimulation for labor downsizing due to pressures related to international competition (Lechevalier et al. 2014). However, while more internationalized companies might resort to more frequent downsizing, it is not evident, whether they are likely to increasingly rely on nonregular workforces. Based on this consideration, I offer the following hypothesis:

H3: *DOI and R&D are negatively correlated with nonregular employment at Nikkei Index 400 companies.*

6.6. Panel Data Analysis

Sources: NEEDS FinancialQUEST database and annual securities reports of Nikkei Index 400 companies retrieved from kabupro.jp.

Selection criteria: Nikkei Index 400 is a political economic project outlined in Japan Revitalization Strategy as one of the "initiatives aimed at enhancing the competitiveness of companies" (Japan Revitalization Strategy, 2013, p. 76). The index consists mostly of large companies that are subject to internationalization and thereby decoupling from national economy. It supposedly: (1) encompasses interest of non-stable shareholders, management and core employees to the highest degree while (2) downplaying interests of nonregular employees.

Dependent variable: Proportion of nonregular employees.

Independent variables:

– Shareholder value (SV) proxies:
  - Tobin's Q (*Q* = Equity Market Value ÷ Equity Book Value) (Nakano et al., 2014, p. 21)
  - Total shareholder return (*TSR* = Share price at end of year – Share price at the beginning of the year + Dividends per share) ÷ Share price at beginning of year) (Dobbs & Koller, 2005)
  - *Director ownership*: shows the degree of alignment between directors and shareholder and, hence, the extent of directors' potential compliance with shareholders' clams to raise SV (Gospel & Pendelton, 2003, p. 574)
  - Annual general meeting (*AGM*). Japan's AGMs are often held on a same day and within a short period of time. This measure was introduced to formalize meetings and limit outside shareholders' interference. Thus, I differentiate between companies that chose to hold AGM during the most popular day ("1"), indicating limited shareholders' influence, and the rest ("0"), more opened to shareholders' demands
  - *Foreign ownership*
– Profitability proxy: return on assets (*ROA* = NI ÷ TA, where NI is net income, TA is total assets) (Ahmadjian & Robbins, 2005, p. 461)
– *Domestic ownership* proxy: other companies' ownership + financial ownership
– Size proxy: *total assets*
– *Productivity* proxy: net sales ÷ number of employees (Ahmadjian & Robinson, 2001, p. 632

Control variables:

– *Ratio of Nonregulars* $_{t-1}$. Since the changes in the proportion of nonregular employees are incremental, I include the dependent variable lagged by one year as a control variable.
– Degree of internationalization (*DOI*): exports ÷ net sales
– *R&D intensity*: R&D expenses ÷ net sales

The analyzed panel data sample contains 245 firms belonging to the Nikkei Index 400 with data from 2010 till 2017. Each company's data encompasses the period between two and eight years, which makes the panel unbalanced. I excluded financial companies due to their different accounting standards. Because of the limited availability of information on nonregular employees in the NEEDS FinancialQUEST database, the starting year of analysis is 2010, the final year is 2017, which makes 1762 observations in total. It can be inferred from the Figure 9, constructed by the *ggplot2* R package (Wickham, 2009), that the data encompasses ten industries, with "Retail" and "Chemical" having most of the observations.

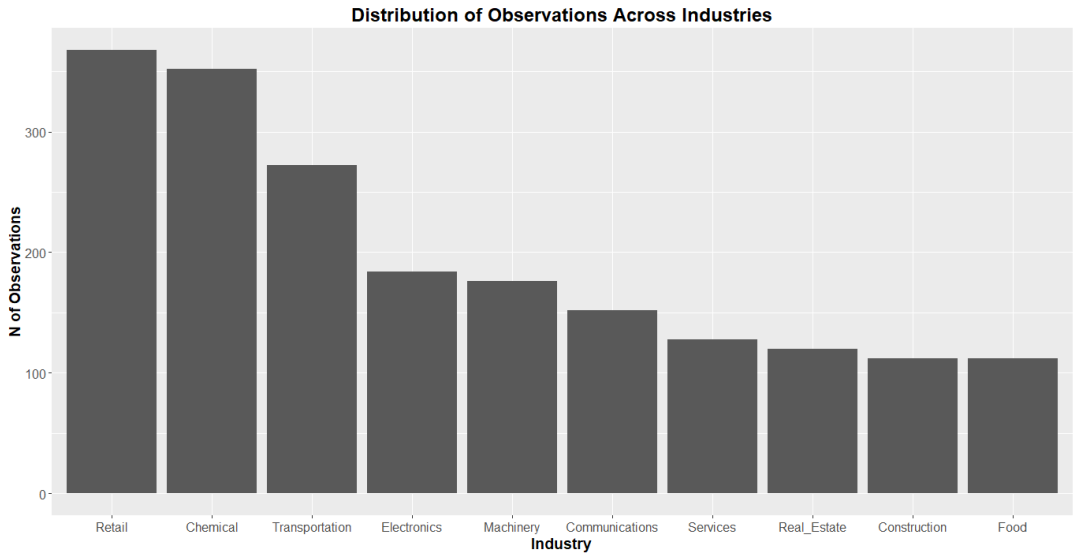

Figure 12. *Distribution of Observations Across Industries*

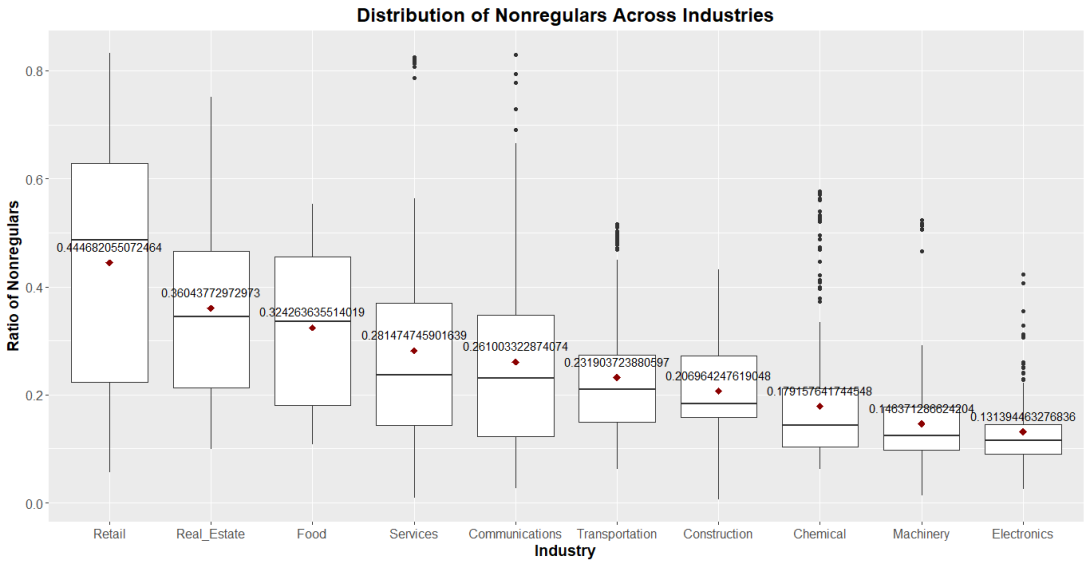

Figure 13*. Distribution of Nonregulars Across Industries*

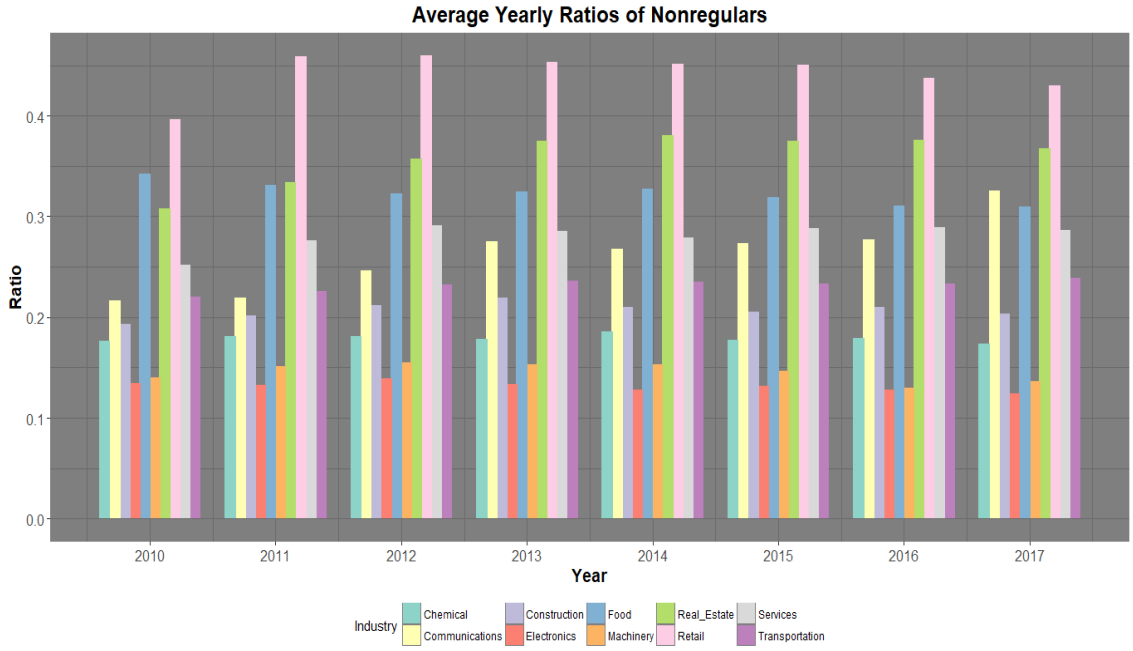

***Figure 14**. Average Yearly Ratios of Nonregulars*

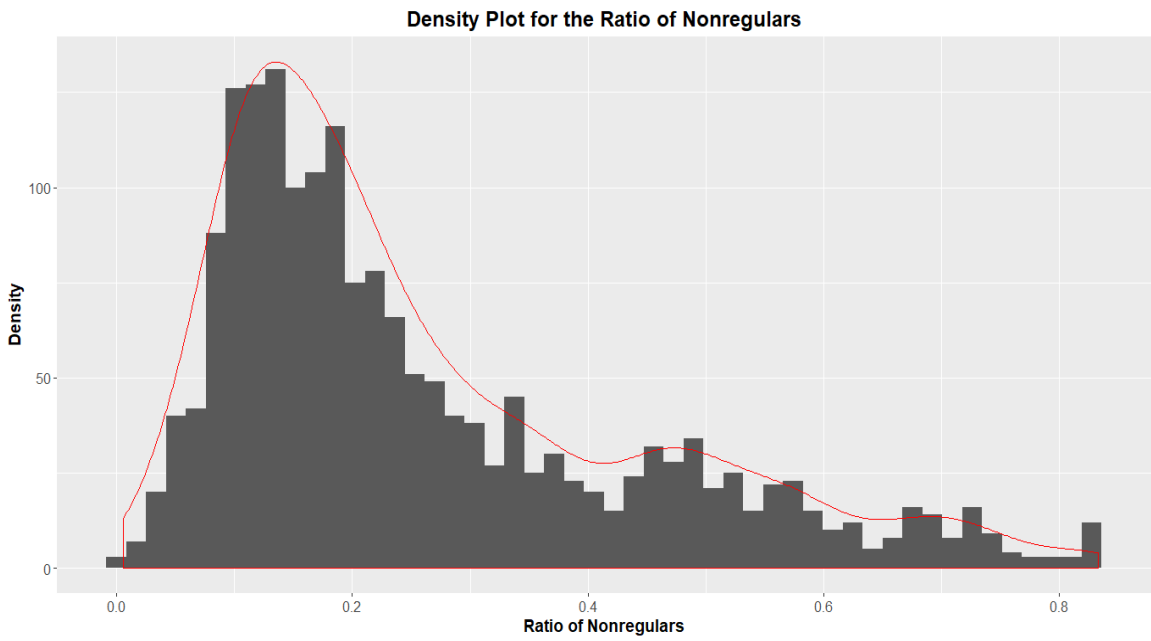

***Figure 15**. Density Plot for the Ratio of Nonregulars*

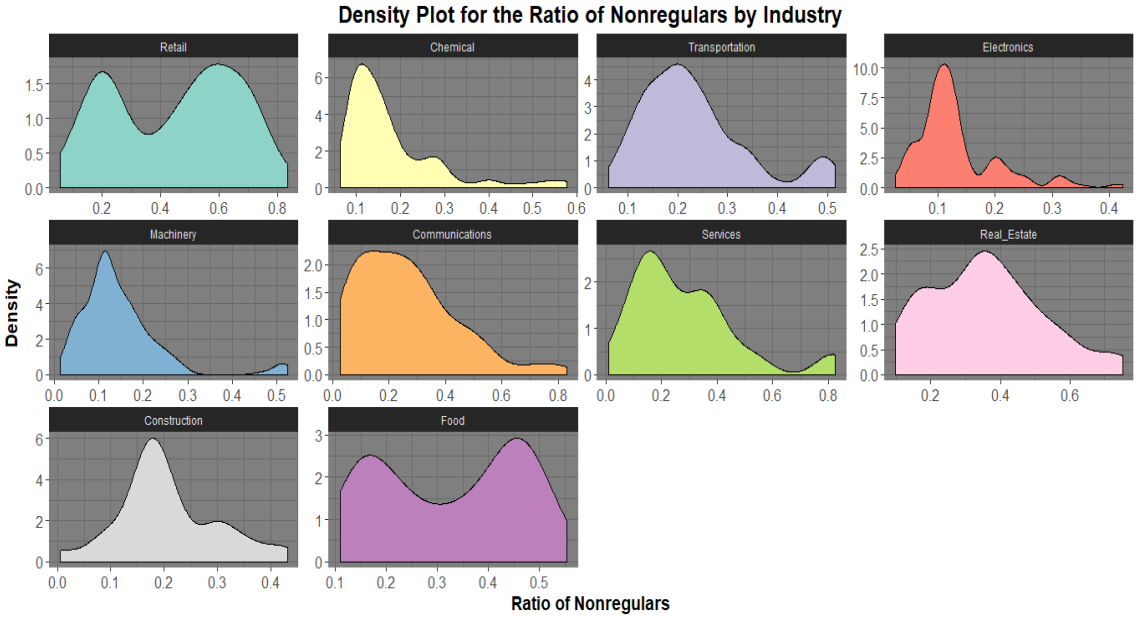

***Figure 16**. Density Plot for the Ratio of Nonregulars by Industry*

Dependent variable: Ratio of Nonregulars

As seen from the Figure 13, built with the *ggplot2* R package (Wickham, 2009), companies belonging to the "Retail", "Real Estate" and "Food" industries have the highest median and average ratios of nonregulars, while "Electronics", "Machinery" and "Chemical" employ the lowest proportions of temporary employees. The same observation holds true for the yearly averages per industry, which can be inferred from the Figure 14. Such distribution is logical, since companies with highest proportions of nonregular employees belong to labor-intensive industries, which means they can improve their balance sheets by decreasing average labor costs. On the other hand, companies belonging to capital-intensive industries have the lowest rates of temporary employees. Their profits are less dependent on human resources, and, hence, there is not much rationale to curb labor cost per employee.

The distribution of the dependent variable "Ratio of Nonregulars" is skewed to the right, as seen from the Figure 15, built with the *ggplot2* (Wickham, 2009). From this type of distribution, we can corroborate that the mean is larger than the median. The descriptive statistics table (Table 4), constructed with the *sjmisc* R package (Lüdecke, 2018) proves this: mean = 0.26262, median = 0.19844. We can also infer from the density plot (Figure 15) that the distribution is bimodal (the third mode can be distinguished towards the right end of the distribution, but it is less evident). That the most common percentage of nonregulars within the first mode is between nine and 14. The next common value is around

19 percent, which is very close to the median value (19.8 percent). The second mode is concentrated around the values of 48-50 percent. It can be corroborated from the Figure 16 that the distribution of nonregulars that closely resamples the general right-skewed bimodal pattern is observed for such industries as: Chemical, Electronics (which also has a third mode), Machinery and Services.

Independent variables

Among the plethora of views on how to measure SV along with discussions on the neutrality of this term, only Uchida (2011), Nakano, Otsubo & Takasu (2014) and Radić (2014) explored the possible determinants of shareholder value for Japan. Moreover, hardly any study analyzes the implications of prioritizing shareholder value for labor policies within the Japanese context. Dore (2007) and Jackson (2007) observed decoupling between shareholders' dividends and average salaries, however, this does not provide enough evidence for considering negative correlation between shareholder value and labor remuneration. According to Froud, Halsam, Johal & Williams (2000, p. 101), under conditions of a "bull market" (when stock prices are rising), shareholder returns are more likely to occur through shares' trading rather than through dividends distribution to shareholders.

Various consulting groups come up with own measurements of SV. Most famous examples of performance metrics are economic value added (EVA) and market value added (MVA) by Stern Stewart, as well as cash value added (CVA) and cash flow return on investment (CFROI) by the Boston Consulting Group (Froud, Halsam, Johal & Williams, 2000). Radić (2014) applies EVA as a proxy for measuring shareholder value creation of Japanese banks. Hillman & Keim (2001) and de Wet (2005) apply MVA as a wealth-based metrics to operationalize shareholder value. Another view stresses a more substantial role of such accounting indices as earnings per share (EPS), dividends per share (DPS), return on assets (ROA) and return on equity (ROE) being drivers of shareholder value. At the same time, EVA is regarded primarily as a managerial valuation tool able to "take into account both the resources used to obtain the profit and these resources' risk" (Fernandez, 2001, p. 9). However, this is not a proper metrics to capture long-term shareholder value creation (Fernandez, 2001). In addition, Froud, Halsam, Johal & Williams (2000, p. 100) argue that MVA is related mainly to stock market fluctuations and thus tends to collapse when bubble burst occurs.

Sato (2000, as cited in Inagami & Whittaker, 2005, p. 84) measured the degree of shareholder-orientation by including both EVA, ROE, as well as share price into his analysis of Japanese stock-listed companies. These indices are positively correlated with pursuing a reformist corporate governance strategy, however, are loosely coupled with employment and industrial policies (Sato, 2000, p. 87). According to survey conducted by Inagami & Whittaker (2005, p. 79), ROE is likely to occupy a leading role as a corporate performance indicator for Japanese companies, outweighing sales and market share. Lazonick & O'Sullivan (2000, p. 18) also associate ROE with shareholder value. The link between ROE and corporate governance was recently acknowledged by the Japanese Cabinet Office: "it is important to strengthen the mechanism to enhance corporate governance and reform corporate managers' mindset so that they will make proactive business decisions to win in global competition for the purpose of attaining targets including globally-compatible level in return on equity" (2014, p. 5). Deakin (2005, pp. 14, 15) mentions that metrics reflecting shareholder returns are mainly EPS, EVA, ROCE (return on capital employed) and ROE. Jürgens, Naumann & Rupp (2000, p. 69) present evidence of the importance of ROCE and RONA (return on net assets) for public companies operating within CME context.

The accounting indices of performance include ROA, ROE, Tobin's Q etc. (Hillman & Keim, 2001, p. 134). On the other hand, measures called to estimate managers' control according to "value-based" systems include: EVA, MVA, shareholder value added, CFROI etc. (Fiss & Zajac, 2004, p. 514). Another classification offered by Dobbs & Koller (2005) is the measure of a long-term and investor-based corporate growth. The former is related to sustainable growth and is less dependent on stock-market fluctuations. It can be measured by combining the return on invested capital (ROIC) with economic profit (Dobbs & Koller, 2005). According to authors, while ROIC drives higher EPS, it is a way less manipulative metrics. However, de Wet (2005, p. 3) mentions that ROIC is included into calculation of EVA (EVA = (ROIC – Weighted Average Cost of Capital) × Invested Capital).

Based on the existing literature and data available, I chose to measure SV by using such accounting metrics as Tobin's Q (*Q* = Equity Market Value ÷ Equity Book Value) and Total Shareholder Return (*TSR* = (Share price at end of year – Share price at the beginning of the year + DPS) ÷ Share price at beginning of year). Jackson Jr. & Milahupt (2014, p. 137) and Kato, Miyajima & Owan (2016, p. 6) offer the Tobin's Q measure for firm performance along with ROA. Nakano, Otsubo & Takasu (2014, p. 21) also suggests using

Tobin's Q as a proxy for shareholder value, along with price-to-book ratio (PBR). Having Tobin's Q means the ROE and MVA measures can affect the robustness of the test since Tobin's Q is positively related on one hand to ROE (Tobin's Q = ROE ÷ cost of capital) and, on the other hand, to MVA (Tobin's Q = MVA ÷ Net Assets – 1) (Aglietta, 2000, p. 148). Regarding TSR, Dobbs & Koller (2005) use it to measure stock market performance of a company reflecting its short-term SV. Next determinant of SV is *foreign shareholding*. It is related to risk-taking (Nakano et al. 2014, p. 21) and downsizing (Ahmadjian & Robbins, 2005, p. 460) in the attempts to maximize shareholder-value seen as a US-originated corporate ideology (Ahmadjian & Robbins, 2005, p. 459). Finally, *director ownership* demonstrates the alignment of CEOs interests with shareholders (Ikeda, Inoue & Watanabe, 2017, p. 22).

To account for the corporate governance reforms in the regression, I confine the analysis with the Nikkei Index 400 companies, who are considered most reformist in terms of applying market-oriented policies. In addition, Sakai & Asaoka (2003) and Ikeda, Inoue & Watanabe (2017) offer the shareholding ratios as proxies for corporate governance. Among the shareholder groups, I include the mentioned foreign shareholders and directors, as well as variable "*domestic ownership*" that includes such stable domestic shareholders as companies and financial institutions (Yoshikawa, Phan & David, 2005, p. 282).

As for corporate performance measurement, Uchida (2011, p. 566) and Ahmadjian & Robbins, (2005, p. 461) argue for the robustness of ROA. Hagel, Brown & Davison (2010) also present arguments in favor of ROA for its capacity to capture operational profitability of the firm, as opposed to ROE. At the same time, Fernandez (2001, p. 12) mentions that ROA is used for measuring EVA, while ROE is used for the calculation of EP (Economic Profit), which is another proxy employed by consulting firms, although both ROA and ROE are criticized by EVA's "founder" Stern Stewart (Fernandez, 2001, p. 2). Despite this, I intend to include ROA into the model due to its capacity to measure long-term SV, particularly in case of Japan. $ROA = \frac{NI}{TA}$. NI – net income; TA – total assets. Ahmadjian & Robbins (2005, p. 461) also recommend including proxies for firm's *size* (measured by total assets). I also include a *productivity* variable calculated as "Net Sales ÷ Number of Employees" (Ahmadjian & Robinson, 2001, p. 632).

Finally, on the labor policy side, I use the proportion of nonregular employees to the total number of employees. According to the hypothesis of this study, higher

proportions of nonregulars are associated with corporate restructuring, which is favored by shareholders (Morgan & Takahashi, 2002, p. 174).

Regression

I initially used the *plm* R package by Croissant & Millo (2008) to perform the panel data tests. The *F test* showed a low p-value (< 2.2e-16), which counts against the null hypothesis that the "pooled OLS model" is adequate, in favor of the fixed effects alternative. The *Breusch-Pagan test* for unbalanced panels showed a low p-value (< 2.2e-16), which also counts against the null hypothesis that the "pooled OLS model" is adequate, in favor of the "random effects model" alternative. Finally, the *Hausman test* showed a low p-value (< 2.2e-16), which counts against the null hypothesis that the "random effects" model is consistent, in favor of the "fixed effects model". Although the "fixed effects model" appears the most appropriate for my data, to demonstrate the similarities/differences in these models and to improve the robustness of the analysis, I include all three of them into the comparative regression tables.

As for the "fixed effects model", I have run two regressions with the "individual" and "two-ways" effects respectively (both have the p-values < 0.01, meaning high levels of significance). While the "individual" effects assume the company-specific differences that are constant over time, the "two-ways" effects assume both "individual" and "time" effects. In other words, the "two-ways" effects imply that differences have been both time-sensitive and company-specific. It is likely that company-specific differences have been time-invariant (since I look at a relatively short period of time, which is eight years), granting the entrenched nature of Japanese institutions and the resulting incremental change within the local corporate environment. Hence, I assume that the "individual" effects are most appropriate for the panel However, it is also possible that changes occurred over time as well, as the proportion of nonregular employees has been increasing from 2010 to 2017.

The main regression model used in this research looks as follows:

$$Nonregular_{it} = \alpha_0 + \alpha_1 Nonregular_{it-1} + \alpha_2 \log(Director)_{it} + \alpha_3 Domestic_{it} + \alpha_4 Foreign_{it} + \alpha_5 ROA_{it} + \alpha_6 \log(Size)_{it} + \alpha_7 AGM_{it} + \alpha_8 Productivity_{it} + \alpha_9 Tobin'sQ_{it} + \alpha_{10} TSR_{it} + \alpha_{11} DOI_{it} + \alpha_{12} R\&D_{it} + \gamma_i + \varepsilon_{it} \quad (1)$$

where $Nonregular_{it}$ is the ratio of nonregular employees to total employees for the company i at time (year) t. γ_i denotes industry- and firm-specific effects, while ε_{it} stands for the residuals or the noise of the model.

The initial OLS regression did not include the time-lagged dependent variable. However, I was not satisfied with the original model since its R^2 value was relatively low (four percent). Although the literature provides examples of low R^2 that does not compromise corporate financial analysis (Beck, Demirgüç-Kunt & Maksimovic, 2006, p. 322), I have experimented with adding the time-lagged dependent variable. This procedure is associated with the risk of suppressing the explanatory power of other dependent variables (Achen, 2001; Keele & Kelly, 2005). In my case, however, the inclusion of the "Ratio of Nonregulars" variable lagged by one year did not change the signs of the coefficients. Furthermore, the significance of other explanatory variables was corrected only marginally (the same effect is not observed if I lag the dependent variable by two years). In turn, the adjusted autocorrelated model has led to a significantly improved R^2 (27 percent) and adjusted R^2 (12.2 percent), which denotes the higher explanatory power of the new regression. This provides an evidence of the dynamic nature of the panel, whereby the Ratio of Nonregulars during the observed year is determined by the "Ratio of Nonregulars" from the previous year.

Next, I considered applying the linear mixed model (LMM) with the help of the *lme4* R package (Bates et al., 2015). I chose to test this model for two reasons. First, it is used when the response variable has a non-normal distribution. This holds true for the "Ratio of Nonregulars" dependent variable, which has right-skewed bimodal distribution, as shown above (Figure 15). Second, the LMM allows to account not only for fixed effects (company and industry) but also for random effects within each unit (company) occurring over time (McCulloch, 1996). In other words, the LMM also captures non-independence that exists between time-observations (years 2010-2017) for each individual company. "The random variables of a mixed model add the assumption that observations within a level, the random variable groups, are correlated. Mixed models are designed to address this correlation and do not cause a violation of the independence of observations assumption from the underlying model, e.g. linear or generalized linear" (SSCC, 2016). When comparing R^2 of the fixed-effects and LMM models, the latter has a clear advantage (marginal R^2 of the LMM is 52 percent, which is almost two times higher than the R^2 of the fixed-effects). Moreover, the LMM has a smaller Akaike information criterion (AIC) estimation (−7,166.45) than the fixed-effects model (−4,489.661) which also confirms that

the mixed-effects model has a better fit (Table 6, built with the *stargazer* R package (Hlavac, 2018)).

I have conducted the t-test and applied the variance inflation factor (VIF) to make sure that there is no multicollinearity among the explanatory variables. Both procedures showed that there is no such a problem. The results of the t-test that computes pairwise correlations between explanatory variables can be seen on the Figure 17. This correlation matrix and the subsequent diagnostic plots (Figures 18-20) are built with the help of the *sjPlot* R package (Lüdecke, 2018b).

***Figure 17**. Visualized Correlation Matrix*

6.7. Results and Discussion

The hypotheses listed in this chapter look as follows:

1. *Higher levels of SV are associated with higher proportions of nonregular employment.*

2. *Foreign shareholding is positively correlated with proportions of nonregular employees at Nikkei Index 400 firms.*

3. *DOI and R&D are negatively correlated with nonregular employment at Nikkei Index 400 companies.*

The regression coefficients obtained through the application of the LMM model are shown on the Figure 18. Each coefficient demonstrates the change in the response variable (Ratio of Nonregulars) provided we control for other explanatory variables. Excluding the lagged dependent variable, ROA has a highest correlation coefficient with the response variable (0.06), while Productivity, AGM and Total Assets are the only variables with negative coefficients. Among them, only Productivity is significantly correlated with the Ratio of Nonregulars.

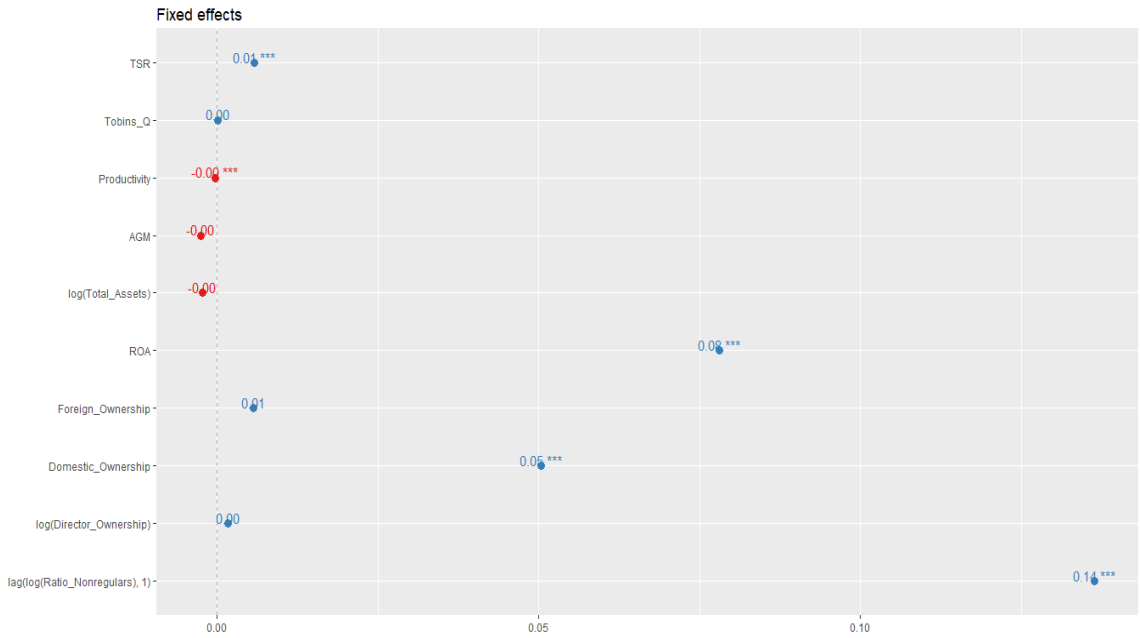

Figure 18. *Correlation Coefficients of the LMM*

Figure 19 shows the overall fit of the model. The actual quantiles are plotted on the x-axis, while the quantiles fitted through a random-effects model are plotted on the y-axis. While dots represent observed values, the line exemplifies the linear model called to capture the given distribution. The overall proximity of dots to the line shows the degree the model represents analyzed data.

Figure 20 demonstrates the relationship between the predictor (red line) and response (blue line) for each explanatory variable. The response is the "Ratio of Nonregulars" that is determined by each of the plotted independent variables within the designed linear regression. Like on the Figure 19, the closer the red line that represents linear model is to the curved distribution of data, the better is the fit. The darker area along the predictor is the 95 percent confidence level interval for predictions from a linear model.

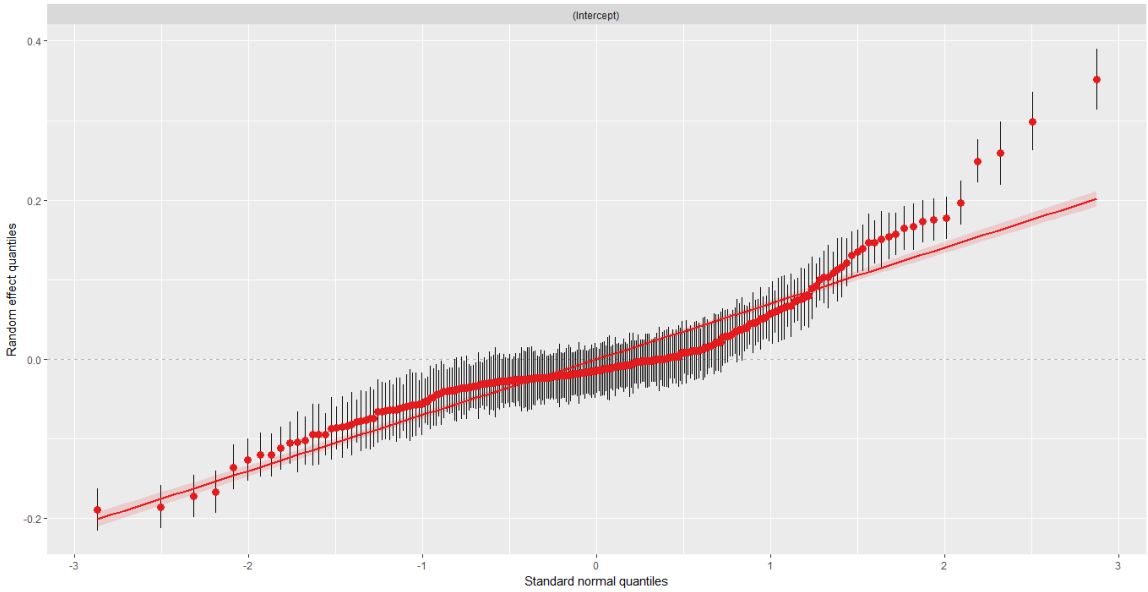

***Figure 19**. Q-Q Plot for Random Effects*

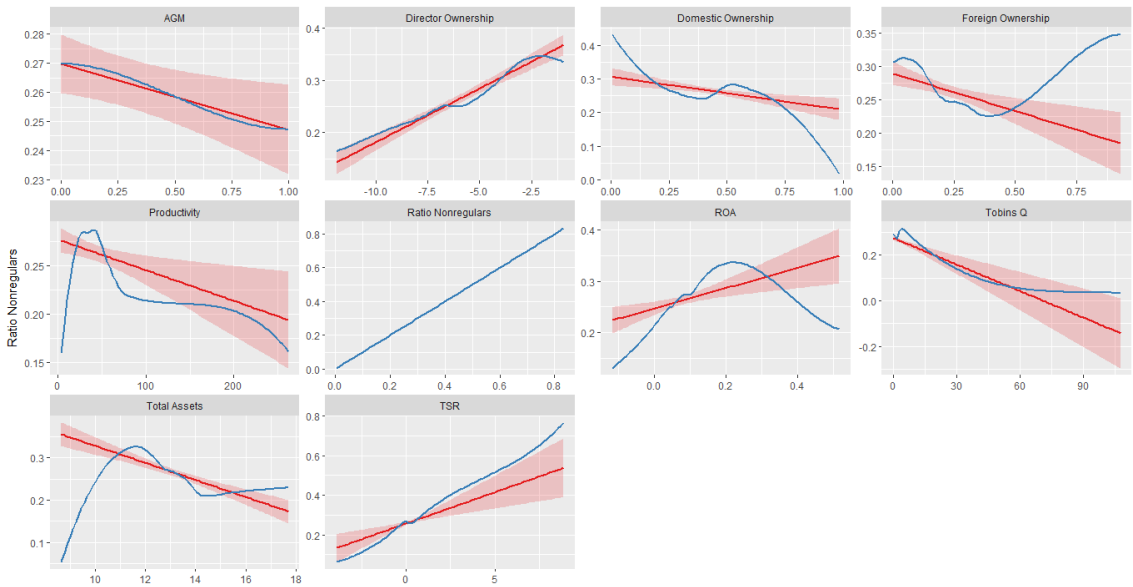

***Figure 20.** Slopes of Coefficients*

On one hand, as seen from the Table 6 (built with the *stargazer* R package (Hlavac, 2018)), Tobin's Q, which is one of the proxies for shareholder value (SV), does not show significant correlation with the proportion of nonregulars. On the other hand, total shareholder return (TSR) – another SV proxy – is positively and significantly correlated with the proportion of nonregular employees. To be more precise, the correlation index

0.006 tells that with the one percent increase in TSR, the Ratio of Nonregulars increases by 0.006 percent, provided we control for the other explanatory variables. Since this coefficient has a low p-value (< 0.01), the chance of TSR and the Ratio of Nonregulars not being correlated is only one percent. Hence, we can reject the null-hypothesis in favor of the alternative hypothesis. In case of this research, the alternative is the Hypothesis 1 that assumes the link between the SV and nonregular employment. Since the TSR variable indicates stock market fluctuations and dividends per share, it is highly possible, based on the regression results, that higher stock prices and higher dividends are associated with downsizing and cutting of labor costs, primarily via the growing reliance on temporary employees.

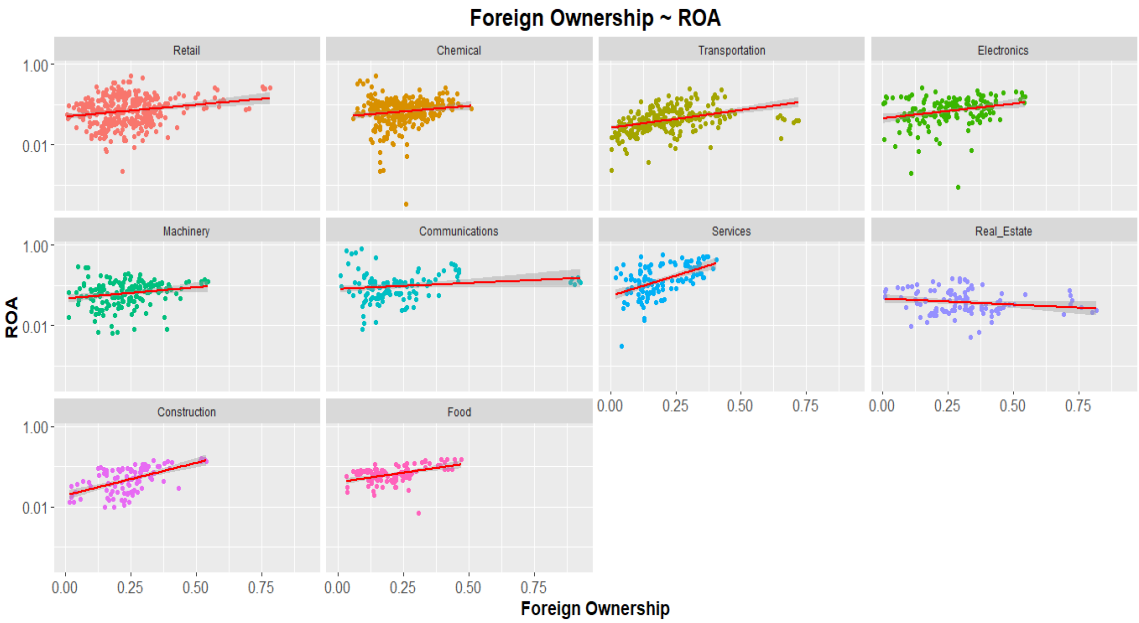

Figure 21. *Correlation Between Foreign Ownership and ROA Across Industries*

Regarding the Hypothesis 2, thus far, the correlation between foreign ownership and nonregular employment is not significant. At the same time, foreign shareholding appears to be correlated with higher profitability measured as ROA (0.39, at the 0.01 significance level) and Tobin's Q (0.001, at the 0.01 significance level), but lower productivity (-0.0004, at the 0.01 significance level) (Table 10). This can be interpreted in a following way: increase in foreign shareholding is likely to be associated with higher corporate revenue, but not with higher efficiency of production. The positive correlation between foreign shareholding and profitability is also valid for linear correlation by industry, with the only exception of "Real Estate" (Figure 21, built with *ggplot2* R package

(Wickham, 2009)). However, Miyajima, Hoda & Ogawa (2016) warn that the reverse correlation can also be true: “Even though a correlation between foreign ownership and high performance could be observed, it is a superficial one. Higher stock returns could simply be a result of their demand for the stock as such, while higher performance may simply reflect foreign investor preference for high quality firms” (p. 16).

While there is no significant correlation between foreign ownership and the ratio of nonregulars, such correlation can be found *between domestic ownership and the ratio of nonregulars*. These variables are positively (0.05) and strongly (at the 0.01 significance level) correlated. Which means, the one percent increase in domestic shareholding is associated with the 0.05 percent in the Ratio of Nonregulars, provided we control for other explanatory variables. This result can be interpreted in a following way. The pertaining institutional compromise between finance, management and regular employees allows core workers to retain their traditional benefits, which comes at price of virtually zero remuneration growth. Ahmadjian & Robinson (2001) and Ahmadjian & Robbins (2005) show that companies with higher levels of domestic shareholding are less prone to downsizing. In other words, domestic ownership is associated with stricter adherence to the companyist compromise. It also shows stronger managerial influence, since CEOs are protected by insider ownership from potential hostile takeovers (Gospel & Pendelton, 2003, p. 574). Most of the large Japanese companies, regardless of their ownership structure, have tended to cut their labor costs during the last three decades to improve their competitiveness. Hence, if a company chooses not to downsize its regular workforce, the only way for it to curb average labor costs is to freeze the hiring of new regulars and to intensify the hiring of nonregulars (Lechevalier, 2014). This also confirms the findings of Abe & Shimizutani (2005) about insiders, represented by domestic owners, being inclined to decreasing new hiring.

The data on degree of internationalization (DOI) and R&D intensity required to test the Hypothesis 3 is provided approximately by the half of the analyzed companies: 145 and 140 firms out of 245 disclosed the information regarding their R&D activity and exports respectively. It can be inferred from the Table 8 (built with the *stargazer* R package (Hlavac, 2018)) that DOI is negatively (-0.028) and significantly (at the 0.01 level) correlated with the Ratio of Nonregulars. This result is in line with the Hypothesis 3. It assumes that companies with higher proportions of overseas sales are the ones less likely to employ higher proportions of temporary employees. This can be due to higher extent of integration into global value chains, which leads to more vigilant supervision of labor standards by

international investors. Since nonregular employment in Japan is associated with relatively inferior status and poor social benefits, more internationalized companies are likely to refrain from over-reliance on nonregulars.

As regards the R&D intensity, Table 9 (built with the *stargazer* R package (Hlavac, 2018)) shows negative (-0.188) and significant (at the 0.01 level) correlation between the R&D intensity and the Ratio of Nonregulars, which also confirms the Hypothesis 3. This coefficient can be interpreted in a following way. Firms that invest more in R&D are overwhelmingly capital-intensive. Hence, they depend less on human resources relatively to labor-intensive industries such as services, retail and food. Since capital-intensive firms have higher entry barrier for their workforce, it is relatively smaller, but, as a rule, composed of more qualified regular employees. On contrary, labor-intensive companies invest less and hence, are less dependent on capital. In turn, their profits are associated with control over labor costs that can be curbed by increasing the proportion of nonregular employees.

The panel data analysis yielded some other valuable results. Firstly, ROA shows positive (0.078) and significant (at 0.01 level) correlation with the proportion of nonregulars. In other words, the one-percent increase in ROA is strongly associated with the 0.078 increase in proportion of nonregulars, provided we control for other explanatory variables. The likely interpretation of this correlation is that nonregular employees are instrumental for achieving higher levels of corporate profitability.

On the other hand, these higher profits are not earned in a sustainable way. As seen from the Table 6 (built with the *stargazer* R package (Hlavac, 2018)), productivity is negatively (-0.0004) and significantly (at 0.01 level) related to the proportion of nonregular employees, provided we control for other independent variables. The possible explanation is: the higher is the share of nonregulars at company, the less is the output per employee. This result confirms previous studies (Jones, 2007; Aoyagi & Ganelli, 2015) that found out that employers are less eager to invest into training of flexible employees. This, in turn, leads to low working motivation among nonregulars as compared to core workers, which explains lower productivity rates for enterprises with higher proportions of nonregular workforce. It can also be inferred from the Figure 22 (built with *ggplot2* R package (Wickham, 2009)) that the negative linear correlation between the Ratio of Nonregulars and Productivity holds true for all industries except “Communications” and “Electronics”.

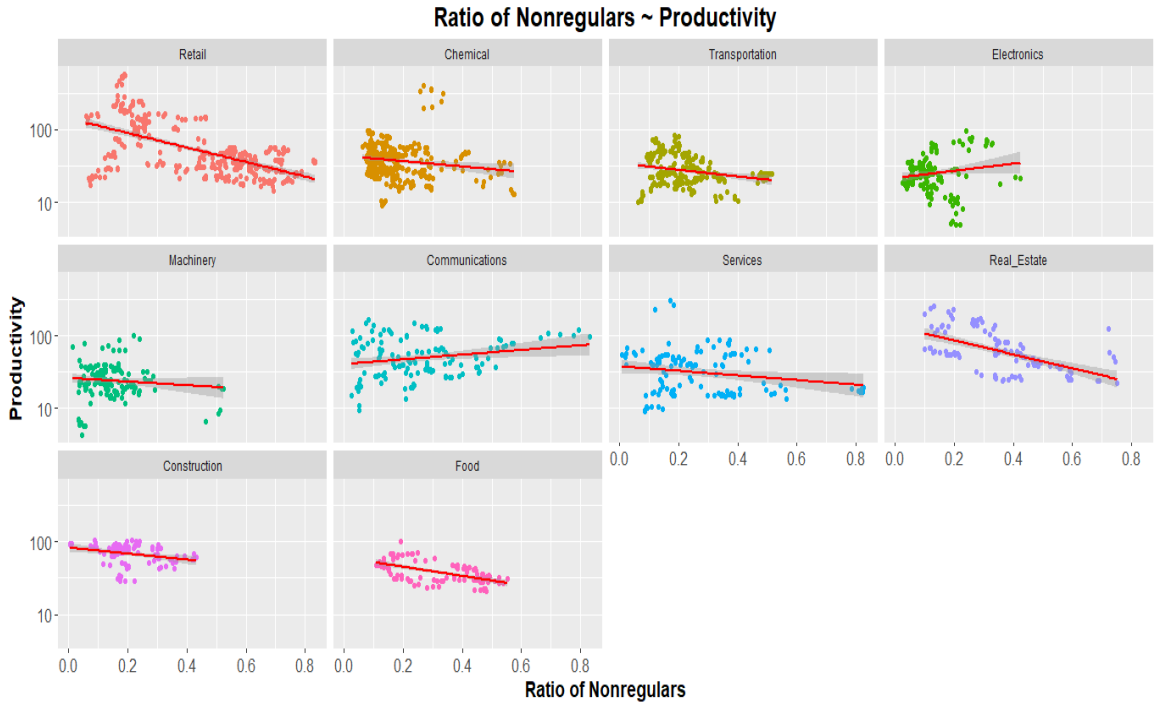

Figure 22. Correlation Between Proportion of Nonregulars and Productivity Across Industries

6.8. Summary

This chapter started with the assessment of the process of corporate financializaton in Japan. It demonstrated that large listed enterprises have tended to curb labor costs while significantly raising directors' bonuses and dividends per share. This is the proof of the unevenness of welfare redistribution that is allocated in favor directors and shareholders, while ordinary salaries remain stagnant. Such tendency is observed against the background of the modest productivity growth that should have driven the labor costs up. However, the associated corporate profits do not lead to improved employees' wellbeing.

The second part of this chapter further explored the relationship between the shareholder value enhancement and the labor situation. It concentrated on the issue of the labor bifurcation, whereby the proportion of nonregular employees has dramatically increased over the last decades, almost reaching the proportion of core workers nowadays. My panel data analysis aimed to shed light on the previously overlooked factor behind such a noticeable change in Japan's labor composition, which is the shareholders' influence. The increase in precarious employment is mostly the feature of such labor-intensive industries as services, real estate and food. Thus, it can be concluded that the growing reliance on temporary workforce is a mean for decreasing average labor costs.

The analysis confirmed the positive correlation between the total shareholder return – one of the shareholder value proxies – and the proportion of nonregulars. Based on the previous evidence of the association between foreign shareholding and downsizing, I assumed that foreign investment can also contribute to the reliance on nonregular employees. While this hypothesis has not been confirmed, I have found out that it is the domestic shareholding that is correlated with large proportions of temporary employees. Companies with higher levels of domestic shareholding are associated with managerial entrenchment. While Japanese managers are known for their strong alliances with core employees, their most likely response to economic turbulences has been the increased hiring of nonregulars as a measure against potential layoffs of regular workers.

The final valuable finding of my panel data analysis is the negative association between R&D intensity as well as internationalization, with the ratio of nonregular employees. It was mentioned that most pronounced labor bifurcation is observed for labor-intensive industries. On the other hand, such capital-intensive industries as electronics, machinery and chemicals rely on temporary workforce to a lesser extent. Thus, it is logical for the companies with higher levels of R&D investment, which is a display of capital-intensive enterprises, to be less dependent on nonregulars. In addition, those companies with higher proportion of exports – the display of internationalization – are, arguably, more likely to adhere to international labor standards. Hence, such firms would be less eager to replace core employees with nonregulars characterized by precarious working conditions.

The presented data analysis contains some limitations. First, my panel data analysis on nonregular employees does not account for dispatch workers (*haken*). However, since their number is relatively small (six percent of nonregulars), this should not significantly affect the results of the research. Second, I only analyze the constituencies of Nikkei Index 400, which are large companies. Hence, my findings might not be generalized for the SMEs as well as unlisted companies. Third, while I only account for the stock market influence on labor bifurcation, the model is likely to be more accurately explained through the inclusion of capital market variables. For example, international competition certainly affects employers' decision on whether to hire more nonregular employees. Therefore, I do not claim that my independent variables solely explain the increase in temporary employment. In turn, I argue that the shareholder value pursuit is likely to *intensify* the labor bifurcation at Japanese joint-stock enterprises.

[**Table 4**. *Descriptive Statistics*]

[**Table 5**. *Correlation Matrix*]

[**Table 6**. *Panel data analysis for the constituencies of Nikkei Index 400*]

[**Table 7**. *Panel data analysis for the constituencies of Nikkei Index 400 (including DOI and R&D Intensity*)]

[**Table 8**. *Panel Data Analysis for JPX-Nikkei Index 400 (Including DOI)*]

[**Table 9**. *Panel Data Analysis for JPX-Nikkei Index 400 (Including R&D Intensity)*]

[**Table 10**. *Panel Data Analysis for JPX-Nikkei Index 400 (Foreign Ownership)*]

Conclusions

The first research question asked about the effects of corporate governance reforms in Japan on corporate dynamics. In this dissertation, I focus on such effects of the reforms as the discursive enhancement of shareholder value and the process of corporate financialization. Nowadays, it is a crucial task for Japanese companies to regain international competitiveness and to attract global capital. To do so, they are required to improve their accountability and to engage more in financial rather than productive activities. Before the rapid international expansion in early-1980s, Japanese companies were not exposed to the market for corporate control. In turn, the monitoring function was carried by the main bank system. It is also called a "contingent" system, since partner banks were interfering into corporate matters only occasionally, mostly to rescue their corporate partners. This provided Japanese directors with a comparatively high degree of freedom. They were promoted from inside, and, upon getting the board position, were becoming relational monitors who profoundly knew corporate matters. However, they were less capable of taking market-oriented decisions that require high degree of entrepreneurship.

While the Japanese multinationals already had an experience of arm's-length monitoring, many other companies had to reform their governance as a result of a sharp decline of the main bank system upon the bubble burst in 1990. In the mid-1990s, foreign shareholders took advantage of corporate devaluated stock and massively purchased it. On one hand, this provided investee companies with a leverage of operating in the open market, rather than within the closed main bank system. On the other hand, these outside shareholders have claimed monitoring credentials proportional to their investments.

The institutional peculiarity of a Japanese joint-stock company is a non-separation of monitoring from execution. In other words, there has been a very critical reception of the idea about mandatory presence of outsiders at the local boards. However, as directors of listed companies realized the need to comply with such shareholder demands as annual accounting disclosure, they have been reforming their own mindsets towards the more shareholder-oriented policies. As a result, enhancement of shareholders' interests has become one of the integral components of the ongoing corporate governance reforms in Japan. As shown in Chapter 4, this has been promoted through a series of corporate governance reforms that started with the 2002 Commercial Code amendment and eventually led to the adoption of the Corporate Governance and Stewardship codes in 2015.

The strengthening of shareholder orientation has been further promoted by such governmental initiatives as Japan's Revitalization Strategy.

In Chapter 6, I analyzed social externalities of the shareholder value pursuit. The main externality is the intensified process of corporate financialization, whereby a company is increasingly perceived as a bundle of financial assets that must be maximized by all means. Such idea clearly conflicts with the Japanese stakeholder model, which provides decent returns not only to shareholders, but also to employees, customers, suppliers and a wider society. Hence, while pursuing shareholder value, Japanese managers have been inclined to protect the institutional compromises with other stakeholders such as employees. Employees, however, have been gradually losing their ground during negotiations about salaries and benefits. From the late-1990s, the joint employer-employee negotiation system, *shunto*, has been in decay, which was justified by employers as a concession that core workers need to give in exchange for preserving their traditional guarantees such as lifetime employment, and, to a lesser degree – seniority promotion, and post-retirement benefits. In turn, the labor costs have been stagnant, or declining, which I show for the period of 2010-2017. Negative growth of salaries for average workers has been accompanied by the sharp surge in directors' bonuses (23 percent) and dividends (14.6 percent). Such welfare distribution in favor of shareholders and directors aligned with them, at the expense of labor cost, is one of the displays of Japan's corporate financialization. It cannot be said that corporate governance reforms have caused this phenomenon, but they have certainly fueled it, by promoting shareholder orientation among Japanese directors.

While the guarantees for regular employees have been overly preserved, their cohort has been steadily shrinking. There has not been much firing of core workers but rather – freeze in the hiring of new full-time employees. In turn, companies, especially in such industries as retail, food and services, have been increasingly relying on nonregular workforce. In the second research question, I ask about the impact of the corporate governance reforms on the labor situation at Japanese companies. Accordingly, I hypothesize that the ongoing reforms have intensified the labor bifurcation, whereby the proportion of nonregular employees has almost equaled the proportion of core employees. I come up with such hypothesis based on the institutional complementarity hypothesis that emphasizes the incompatibility of shareholder orientation (which was enhanced by Japan's corporate governance reforms) and employment security. Hence, I regard the relative and absolute surge in flexible employment as another externality of shareholder value pursuit. In my panel data analysis of Nikkei Index 400 companies I have found out that the ratio of

nonregulars is positively and significantly correlated with the total shareholder return (TSR). Hence, I conclude that higher shareholder returns are achieved at the expense of the growing proportion of temporary workers.

I interpret this result from the political economic point of view. As foreign shareholders gained financial weight in Japanese companies, they entered a power bloc with directors that realized the benefits of aligning with new capital providers. This alliance has been enhanced by the Japanese government that has been increasingly promoting reorientation towards market among Japanese companies. However, due to entrenched institutional legacy represented by such actors as *Keidanren* and *Rengō*, the management-labor compromise has remained intact, although in a modified form. At the same time, the group that has not been able to secure political privileges is the cohort of nonregular employees. Their increasing proportion leading to labor bifurcation is a buffer that the current political economic coalition uses to advance its interests.

The postwar corporate governance in Japan was centered on two compromises: firstly, between management and labor and secondly, between management and partner banks. The pre-1980s hierarchical market-firm nexus prioritized the first compromise, whereby the cooperative relations between directors and average workers were key to Japan's comparative advantage. However, with the unfolding of financialization from the mid-1990s, the management-finance compromise has started to occupy a leading role. As banks have been gradually outweighed by outside shareholders as major corporate investors, companies have started to pay more attention to profitability than to growth. Whereas the postwar "companyist" model was a display of a rather closed "community company", the post-1990 model has partially embraced market orientation. However, with the still relevant "insider-outsider" distinction, modern companies continue to rely on insiders – both as executives and as monitors. For the current labor situation, it means that the growing proportion of nonregular employees, which are "outsiders", is not enjoying same benefits as core workers. Although the unionization rates among temporary employees are gradually increasing, they still lack institutional representation and incentives to become full members of the companies they are formally affiliated with. This is complemented by the results of my panel data analysis: it shows negative and significant correlation between the ratio of nonregulars and productivity. This result suggests that, to increase productivity, Japanese companies need to find ways of narrowing the gap between core and temporary workers. In particular, nonregulars need to be provided with higher chances of becoming regulars, which would boost their motivation and, thereby, productivity.

In a nutshell, the lesson from Japan's ongoing corporate governance reforms can be captured by the institutional complementary hypothesis: the change in one domain triggers changes in relative domains. The Japanese stakeholder model has been known for its complementarities between relational finance and long-term employment. Currently, as the structure of finance and governance is characterized by the increasing domination of shareholders, this logically invokes changes in the employment system. However, as Japan has a strongly enforced legacy of core employment protection, those who eventually bear the cost of shareholder orientation is the newly formed cohort of nonregulars who do not formally belong to any company.

The described externalities of the shareholder value pursuit invoke a broader discussion on Japan's current social problems. Against the background of the aging population and the shortage of labor, companies and government undertake steps for creating more liquid labor markets and for enabling wider cohorts to participate in the economic life of the country. At the same time, corporations face challenges of coping with international competition. This prompts them to review the postwar privileges to core employees that include lifetime employment and senior-merit wages. While not abandoning former guarantees entirely, employers resort to reductions in average wages via increasing reliance on nonregular workforce amid the decreased hiring of core employees.

Even though the growing proportion of temporary employees is a common tendency worldwide, in Japan, nonregular employees have minimal chances of being promoted to regular positions, thus finding themselves in the long-term precarious niche. As shown in Chapter 6, this is likely to be the cause of their low productivity. Hence, even from the purely economic standpoint, companies employing large proportions of temporary employees need to come up with the career incentives that would tackle the inferior status attributed to the nonregular employment in Japan.

Annex

Label	*N*	*Missings (%)*	*Mean*	*SD*	*SE*	*Median*	*Trimmed Mean*	*Min*	*Max*	*Range*	*Skewness*	*Kurtosis*
Ratio of Nonregulars	1848	6.48	0.26	0.18	0	0.2	0.24	0.01	0.83	0.83	1.13	0.47
Director Ownership	1938	1.92	0.03	0.07	0	0	0.01	0	0.54	0.54	3.27	11.57
Domestic Ownership	1942	1.72	0.44	0.15	0	0.45	0.44	0.01	0.98	0.98	-0.19	0.43
Foreign Ownership	1939	1.87	0.24	0.13	0	0.22	0.23	0	0.93	0.93	1.2	3.44
ROA	1917	2.99	0.08	0.07	0	0.07	0.07	-0.12	0.57	0.68	2.43	9.55
Total Assets	1927	2.48	1615144.48	3678650.55	83800.71	512365	835033.09	5741	48750186	48744445	6.58	60.14
AGM	1939	1.87	0.29	0.45	0.01	0	0.24	0	1	1	0.91	-1.17
Productivity	1820	7.89	45.56	36.93	0.87	33.84	38.4	4.09	261.9	257.81	2.6	8.4
Tobin's Q	1901	3.8	3.1	5.69	0.13	1.4	1.76	0	107.59	107.59	6.65	78.42
TSR	1958	0.91	0.19	0.51	0.01	0.1	0.13	-3.91	8.89	12.81	5.3	68.11
Internationalization	940	52.43	0.47	0.23	0.01	0.47	0.47	0	0.98	0.97	0	-0.95
R&D Intensity	1128	42.91	0.03	0.04	0	0.03	0.03	0	0.3	0.3	2.52	8.39

***Table 4**. Descriptive Statistics*

Correlation Matrix

	Ratio of Nonregulars	*Director Ownership*	*Domestic Ownership*	*Foreign Ownership*	*ROA*	*Total Assets*	*AGM*	*Productivity*	*Tobin's Q*	*TSR*	*Internationalization*	*R&D Intensity*
Ratio of Nonregulars		0.150***	-0.074**	-0.069**	0.069**	-0.088***	-0.060*	-0.071**	-0.120***	0.077***	-0.327***	-0.287***
Director Ownership	0.150***		-0.542***	-0.197***	0.448***	-0.128***	-0.064**	-0.039	0.056*	0.061**	-0.169***	-0.027
Domestic Ownership	-0.074**	-0.542***		-0.368***	-0.252***	-0.049*	0.008	-0.035	-0.026	-0.028	0.026	0.032
Foreign Ownership	-0.069**	-0.197***	-0.368***		0.157***	0.174***	-0.046*	0.099***	0.097***	-0.032	0.336***	-0.016
ROA	0.069**	0.448***	-0.252***	0.157***		-0.177***	-0.121***	-0.037	0.229***	0.063**	0.176***	0.008
Total Assets	-0.088***	-0.128***	-0.049*	0.174***	-0.177***		-0.018	0.177***	-0.090***	-0.048*	0.162***	-0.024
AGM	-0.060*	-0.064**	0.008	-0.046*	-0.121***	-0.018		0.011	-0.015	-0.016	-0.093**	-0.049
Productivity	-0.071**	-0.039	-0.035	0.099***	-0.037	0.177***	0.011		-0.134***	-0.009	-0.143***	-0.244***
Tobin's Q	-0.120***	0.056*	-0.026	0.097***	0.229***	-0.090***	-0.015	-0.134***		-0.046*	0.261***	0.219***
TSR	0.077***	0.061**	-0.028	-0.032	0.063**	-0.048*	-0.016	-0.009	-0.046*		0.000	0.014
Internationalization	-0.327***	-0.169***	0.026	0.336***	0.176***	0.162***	-0.093**	-0.143***	0.261***	0.000		0.261***
R&D Intensity	-0.287***	-0.027	0.032	-0.016	0.008	-0.024	-0.049	-0.244***	0.219***	0.014	0.261***	

Computed correlation used pearson-method with pairwise-deletion.

Table 5. *Correlation Matrix*

Panel Data Analysis for JPX-Nikkei Index 400

	Dependent variable:			
	Ratio of Nonregulars			
		panel *linear*		*linear* *mixed-effects*
	(Random Effects)	(Two-Ways Effects)	(Individual Effects)	(Mixed Effects)
$RatioNonregulars_{t-1}$	0.131***	0.077***	0.077***	0.136***
	(0.004)	(0.004)	(0.004)	(0.003)
log (Director Ownership)	0.003**	−0.001	−0.001	0.002
	(0.002)	(0.002)	(0.002)	(0.001)
Domestic Ownership	0.007	0.027	0.025	0.050***
	(0.022)	(0.023)	(0.023)	(0.015)
Foreign Ownership	−0.030	−0.049**	−0.044**	0.006
	(0.021)	(0.023)	(0.021)	(0.015)
ROA	0.068**	0.100***	0.104***	0.078***
	(0.029)	(0.027)	(0.027)	(0.019)
log (Total Assets)	−0.009***	−0.006	−0.007*	−0.002
	(0.003)	(0.005)	(0.004)	(0.002)
AGM	−0.004	−0.004	−0.004	−0.003
	(0.003)	(0.003)	(0.003)	(0.002)
Productivity	−0.0002***	−0.0004***	−0.0004***	−0.0004***
	(0.0001)	(0.0001)	(0.0001)	(0.0001)
Tobin's Q	−0.0002	0.0001	0.0001	0.0001
	(0.0003)	(0.0003)	(0.0003)	(0.0002)
TSR	0.003	0.002	0.003	0.006***
	(0.002)	(0.002)	(0.002)	(0.001)
Constant	0.623***			0.501***
	(0.037)			(0.034)
Observations	1,524	1,524	1,524	1,762
R^2	0.472	0.258	0.264	0.522
Adjusted R^2	0.468	0.106	0.117	
Log Likelihood				3,597.225
Akaike Inf. Crit.			−4,489.661	−7,166.450
Bayesian Inf. Crit.				−7,089.811
F Statistic	135.237*** (df = 10; 1513)	43.993*** (df = 10; 1263)	45.559*** (df = 10; 1269)	
Note:				*p<0.1; **p<0.05; ***p<0.01

Table 6. *Panel data analysis for the constituencies of Nikkei Index 400*

Panel Data Analysis for JPX-Nikkei Index 400 (Including DOI and R&D Intensity)

	Dependent variable:			
	Ratio of Nonregulars			
		panel *linear*		*linear* *mixed-effects*
	(Random Effects)	(Two-Ways Effects)	(Individual Effects)	(Mixed Effects)
$RatioNonregulars_{t-1}$	0.116***	0.078***	0.081***	0.134***
	(0.004)	(0.006)	(0.006)	(0.003)
log (Director Ownership)	−0.0005	−0.004	−0.004	−0.001
	(0.002)	(0.002)	(0.002)	(0.001)
Domestic Ownership	−0.039	−0.020	−0.025	0.006
	(0.025)	(0.033)	(0.033)	(0.016)
Foreign Ownership	−0.042	−0.013	−0.033	0.019
	(0.026)	(0.034)	(0.032)	(0.016)
ROA	0.134***	0.121***	0.112**	−0.038*
	(0.043)	(0.044)	(0.045)	(0.022)
log (Total Assets)	−0.008**	0.004	−0.018**	−0.006**
	(0.003)	(0.011)	(0.009)	(0.003)
AGM	−0.001	0.0004	0.002	−0.001
	(0.004)	(0.005)	(0.005)	(0.002)
Productivity	−0.0001	0.00001	−0.00003	0.0001
	(0.0001)	(0.0002)	(0.0002)	(0.0001)
Tobin's Q	−0.0001	−0.00002	0.00003	0.0001
	(0.0003)	(0.0003)	(0.0003)	(0.0001)
TSR	−0.003	−0.001	−0.002	0.001
	(0.003)	(0.003)	(0.003)	(0.001)
DOI	−0.054***	0.001	−0.028	−0.015
	(0.014)	(0.025)	(0.024)	(0.010)
R&D Intensity	−0.225***	0.002	−0.052	−0.154***
	(0.085)	(0.152)	(0.149)	(0.057)
Constant	0.559***			0.512***
	(0.042)			(0.035)
Observations	664	664	664	763
R^2	0.562	0.295	0.302	0.739
Adjusted R^2	0.554	0.124	0.143	
Log Likelihood				1,875.977
Akaike Inf. Crit.				−3,719.954
Bayesian Inf. Crit.				−3,645.758
F Statistic	69.691*** (df = 12; 651)	18.587*** (df = 12; 534)	19.465*** (df = 12; 540)	
Note:				*p<0.1; **p<0.05; ***p<0.01

Table 7. *Panel Data Analysis for JPX-Nikkei Index 400 (Including DOI and R&D Intensity)*

Panel Data Analysis for JPX-Nikkei Index 400 (Including DOI)

	Dependent variable:			
	Ratio of Nonregulars			
		panel *linear*		*linear* *mixed-effects*
	(Random Effects)	(Two-Ways Effects)	(Individual Effects)	(Mixed Effects)
$RatioNonregulars_{t-1}$	0.120***	0.082***	0.084***	0.140***
	(0.005)	(0.005)	(0.005)	(0.003)
log (Director Ownership)	0.0001	−0.006***	−0.006***	−0.0001
	(0.002)	(0.002)	(0.002)	(0.001)
Domestic Ownership	−0.022	−0.020	−0.022	0.009
	(0.026)	(0.031)	(0.031)	(0.016)
Foreign Ownership	−0.036	−0.015	−0.022	0.017
	(0.027)	(0.030)	(0.029)	(0.016)
ROA	0.210***	0.168***	0.167***	0.023
	(0.040)	(0.038)	(0.038)	(0.021)
log (Size)	−0.004	−0.007	−0.021***	−0.003
	(0.004)	(0.010)	(0.008)	(0.003)
AGM	−0.005	−0.003	−0.001	−0.003
	(0.004)	(0.004)	(0.004)	(0.002)
Productivity	−0.0002*	−0.0003	−0.0003	−0.0002**
	(0.0001)	(0.0002)	(0.0002)	(0.0001)
Tobin's Q	−0.0001	−0.00004	0.00000	0.0001
	(0.0003)	(0.0003)	(0.0003)	(0.0002)
TSR	−0.001	−0.002	−0.001	0.002
	(0.003)	(0.003)	(0.002)	(0.001)
DOI	−0.083***	−0.030	−0.041*	−0.028***
	(0.015)	(0.022)	(0.021)	(0.010)
Constant	0.524***			0.529***
	(0.047)			(0.042)
Observations	777	777	777	897
R^2	0.532	0.328	0.340	0.507
Adjusted R^2	0.526	0.171	0.193	
Log Likelihood				2,125.580
Akaike Inf. Crit.				−4,221.160
Bayesian Inf. Crit.				−4,149.174
F Statistic	79.203*** (df = 11; 765)	27.890*** (df = 11; 629)	29.727*** (df = 11; 635)	
Note:				*p<0.1; **p<0.05; ***p<0.01

Table 8. *Panel Data Analysis for JPX-Nikkei Index 400 (Including DOI)*

Panel Data Analysis for JPX-Nikkei Index 400 (Including R&D Intensity)

	Dependent variable:			
	Ratio of Nonregulars			
		panel *linear*		*linear* *mixed-effects*
	(Random Effects)	(Two-Ways Effects)	(Individual Effects)	(Mixed Effects)
$RatioNonregulars_{t-1}$	0.105***	0.063***	0.065***	0.111***
	(0.004)	(0.004)	(0.004)	(0.003)
log (Director Ownership)	−0.001	−0.003	−0.003	−0.0004
	(0.002)	(0.002)	(0.002)	(0.001)
Domestic Ownership	−0.021	−0.00004	−0.003	0.014
	(0.025)	(0.032)	(0.031)	(0.018)
Foreign Ownership	−0.067***	−0.017	−0.029	−0.010
	(0.026)	(0.031)	(0.030)	(0.018)
ROA	0.091**	0.135***	0.114***	0.015
	(0.039)	(0.039)	(0.038)	(0.024)
log (Size)	−0.003	0.006	−0.010*	−0.0001
	(0.003)	(0.009)	(0.006)	(0.003)
AGM	0.006	−0.0003	0.002	−0.0001
	(0.004)	(0.004)	(0.004)	(0.003)
Productivity	−0.0001	−0.001**	−0.0005**	0.00000
	(0.0001)	(0.0002)	(0.0002)	(0.0001)
Tobin's Q	−0.0002	−0.0001	−0.00004	0.00002
	(0.0003)	(0.0003)	(0.0003)	(0.0002)
TSR	0.001	0.001	0.002	0.002
	(0.002)	(0.002)	(0.002)	(0.002)
R&D Intensity	−0.372***	−0.066	−0.139	−0.188***
	(0.090)	(0.142)	(0.141)	(0.070)
Constant	0.452***			0.402***
	(0.040)			(0.038)
Observations	901	901	901	1,039
R^2	0.473	0.259	0.267	0.564
Adjusted R^2	0.467	0.098	0.114	
Log Likelihood				2,302.440
Akaike Inf. Crit.				−4,574.880
Bayesian Inf. Crit.				−4,500.690
F Statistic	72.581*** (df = 11; 889)	23.518*** (df = 11; 739)	24.619*** (df = 11; 745)	
Note:				*p<0.1; **p<0.05; ***p<0.01

Table 9. *Panel Data Analysis for JPX-Nikkei Index 400 (Including R&D Intensity)*

Panel Data Analysis for JPX-Nikkei Index 400 (Foreign Ownership)

	Dependent variable:			
	Foreign Ownership			
		panel *linear*		*linear* *mixed-effects*
	(Random Effects)	(Two-Ways Effects)	(Individual Effects)	(Mixed Effects)
log (Director Ownership)	−0.019***	−0.018***	−0.022***	−0.020***
	(0.002)	(0.002)	(0.002)	(0.002)
Domestic Ownership	−0.359***	−0.289***	−0.338***	−0.353***
	(0.022)	(0.023)	(0.024)	(0.022)
Ratio of Nonregulars	0.016	0.002	0.004	−0.0003
	(0.022)	(0.026)	(0.027)	(0.024)
ROA	0.388***	0.266***	0.335***	0.390***
	(0.029)	(0.029)	(0.030)	(0.029)
log (Total Assets)	0.050***	0.025***	0.077***	0.055***
	(0.003)	(0.006)	(0.004)	(0.003)
AGM	−0.004	0.001	−0.002	−0.004
	(0.004)	(0.003)	(0.004)	(0.004)
Productivity	−0.0003***	−0.0003**	−0.0004***	−0.0004***
	(0.0001)	(0.0001)	(0.0001)	(0.0001)
Tobin's Q	0.001***	0.001**	0.001**	0.001***
	(0.0003)	(0.0003)	(0.0003)	(0.0003)
TSR	−0.004*	−0.004**	−0.005**	−0.004**
	(0.002)	(0.002)	(0.002)	(0.002)
Constant	−0.402***			−0.465***
	(0.043)			(0.046)
Observations	1,762	1,762	1,762	1,762
R^2	0.372	0.191	0.413	0.412
Adjusted R^2	0.369	0.051	0.315	
Log Likelihood				2,780.763
Akaike Inf. Crit.				−5,535.526
Bayesian Inf. Crit.				−5,464.361
F Statistic	115.489*** (df = 9; 1752)	39.374*** (df = 9; 1501)	118.053*** (df = 9; 1508)	
Note:				*p<0.1; **p<0.05; ***p<0.01

Table 10. *Panel Data Analysis for JPX-Nikkei Index 400 (Foreign Ownership)*

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