Transformational CEOs

Leadership and Management Success in Japan

Kimio Kase
Francisco J. Sáez-Martínez
Hernán Riquelme

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To Mercedes and to the memory of Gabriel.

To Ángela, Lucía and Juan.

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Kimio Kase

IESE Business School, Spain

Francisco J. Sáez-Martínez

Universidad de Castilla-La Mancha, Spain

Hernán Riquelme

RMIT University, Australia

Edward Elgar

Cheltenham, UK • Northampton, MA, USA

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Foreword

These are interesting times for scholars of management. Companies are facing unprecedented strategic and organizational changes, but their capacity for responding to these challenges is limited by the lack of generally accepted management models or consensus over appropriate managerial responses to common organizational circumstances.

This is a contrast with previous decades. During the last quarter of the 20th century, a substantial degree of consensus existed over the management approaches that best matched the conditions of the time. During the late 1970s and throughout the 1980s, the outstanding international success of Japanese corporations – Honda, Toyota, Matsushita, Komatsu, Canon, and YKK – meant that Western executives and business-school academics looked to Japan for lessons on management. The Japanese management model comprising commitment to global market share, continuous improvement (*kaizen*), total quality management, participative work groups, and just-in-time scheduling were seen as offering the potential for a hitherto unprecedented combination of low cost, high quality, and employee satisfaction.

By the 1990s, the appeal of the Japanese model had been severely dented by the increasingly sclerotic performance of the Japanese economy. The fact that the problems of the Japanese economy could be attributed primarily to the ineffectiveness of government policies towards macroeconomic management, monetary, and banking regulation, and that the international performance of many leading Japanese companies continued to be strong, had little impact on the shifting ground of management thought. During the 1990s, the geographical center of management swung back to the United States where new financial theories – agency theory and valuation techniques – together with US entrepreneurial vigor and US leadership in many digital technologies, encouraged increasing deference to a management model founded upon the single-minded pursuit of shareholder value. The shareholder value maximization model was also associated with the UK, Canada, and Australia – hence the term 'Anglo-Saxon capitalism' became used to emphasize not just its association with English-speaking countries but also a hint of rapacious barbarism too.

Rigorous pursuit of shareholder value resulted in major changes in corporate strategy. 'Core-business focus' replaced diversification; outsourcing replaced vertical integration; the primacy of profitability over growth led to

the downsizing of many major corporations as underperforming assets were divested and costs were pruned. These strategies were successful, not just in boosting profitability and laying the foundation for the stockmarket boom that continued from 1988 until 2000, but also creating a productivity boom that was unprecedented both in magnitude and duration.

Early in the new century, the Anglo-Saxon shareholder-value model began to unravel. The dot-com collapse of 2000 ushered in the stock-market meltdown of 2001–02 and coincided with host of corporate scandals – which included several of the exemplars of the shareholder-value model and New Economy based on digital technologies: Enron, WorldCom, Marconi, Adelphi Communication, and many more. By 2002 it was clear that we had entered an era where we lack any dominant management paradigms.

In this new era of uncertainty, the refocusing upon Japanese management by Kase, Sáez-Martínez and Riquelme is timely. Since the Japanese stock-market collapse of 1990 and the southeast Asian financial meltdown of 1998, Japanese companies have faced the most difficult conditions of the postwar era, and yet many have consolidated and extended their international leadership. Particularly interesting, is the finding that the management styles of the companies studied by Kase *et al*. are less distinctively Japanese than the picture of Japanese management painted by Pascale, Aoki, Ohmae, and Morita in their books of the 1980s. The prominence of several non-Japanese CEOs – most notably Ghosn at Nissan and Stringer at Sony – is just one indicator of this. More significantly, the styles of management that Kase *et al*. discover, are striking in their similarities to those of successful companies in Europe and North America. To begin with, Kase *et al*.'s focus upon chief executives gives a 'view from the top' that is familiar to students of Western corporations and distinctively different from the picture of managerial patriarchs, consensus decision-making and distinction between ceremonial leadership and real decision-making authority that was once observed in some Japanese companies.

Most interesting however are the management models of successful companies that Kase *et al*. discern. In their 'proto-image of the firm' (PIF) and 'profit-arithmetic' (PA) models, Kase *et al*. identify approaches to top-management leadership that echo styles that have been observed in a number of Western companies. The role of vision is central to Kase *et al*.'s PIF model. This links closely with a stream of empirically based observations that extend from Peters and Waterman's *In Search of Excellence* to Collins and Porras's *Built to Last.* The PA model similarly focuses upon a metrics-based approach to management that concentrates upon establishing quantitative goals based upon strategic and operational variables that are directly linked to bottom-line results. Again, a stream of Western management techniques that extend from 'management-by-objectives' (MBO) some half a century ago to 'balanced scorecards' today represent a parallel line of development.

My objective in these comments is not to downplay the novelty of Kase *et al.*'s findings, but rather to emphasize that their findings may be viewed within the broad context of the development of management thought. They point to a fundamental dichotomy in organizational leadership: the inspirational, future-orientated leadership associated with the conceptualization and articulation of a vision; as compared with the disciplinarian, results-based management of organizational performance through setting and monitoring performance goals. These two aspects of leadership form a central tension in the role of chief executives. One of the most valuable findings of Kase *et al.*'s study is to suggest which of these models is appropriate to different circumstances. The direct management of financial performance through the PA model presumes that the drivers of profitability are known and manageable. Its use is particularly suited to situations where a firm's financial performance is suboptimal and there are strong short- or medium-term pressures to increase profitability through cost cutting, asset redeployment, market repositioning, or similar strategies. Such an approach is particularly suited to sectors of comparative stability where technological change and other sources of market discontinuity do not disrupt the relationships between managerial action and profit outcomes. Conversely, the visionary leadership associated with the PIF model can be followed in companies where short-term financial pressures are moderate, and is particularly suited to guiding the long-term evolution of businesses in situations where market boundaries are fluid and where the firm's business portfolio is subject to change.

Robert M. Grant
Professor of Management
Georgetown University
Washington, DC

Acknowledgements

This book finds its roots in the arrival of Kimio Kase in Japan when he took up a faculty position at the International University of Japan (IUJ) in 2002. It was in that position that we started a research project into the causes of failures or success of Japanese firms after the burst of Japan's bubble economy in the 1990s. Many people have contributed to our work since then.

Special acknowledgements are owed to Sony's Mr Katsuyoshi Kutsuwada, who wrote under K. Kase's supervision his Masters dissertation on Sony's product development strategy and management in compliance with IUJ's requirement. His findings and thinking greatly influenced the development of our theoretical framework.

We want to acknowledge the valuable contribution to the research made by the chief executive officers (CEOs) whose business approach we studied and who kindly allowed us to use and cite materials drawn from their writings. Although we did not incorporate his case in this book, we are very grateful to Shinsei Bank's Mr Masamoto Yashiro for his comments and observations on a case centred on him. We certainly benefited from them a great deal.

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Kimio Kase
Francisco J. Sáez-Martínez
Hernán Riquelme

1. Management success in Japan

1. INTRODUCTION

Japan, during the 1970s and 1980s looked to be invincible. A symbol of American capitalism, the Rockefeller Center, had been acquired by a Mitsubishi Group real estate company. The NUMMI[1] project in California, Toyota's and General Motors' (GM) joint venture, helped GM learn their partner's just-in-time production system.

Japanese firms were reducing their costs substantially and building quality advantages through pioneering management practices such as Total Quality Management and Continuous Improvement. Bookshops were crowded with texts eulogizing Japanese management strategies (Abegglan and Stalker, 1985; Dunphy, 1987; Hatvany and Pucik, 1981; Marsland and Beer, 1983; Monden, 1985; Ouchi, 1981; Ouchi and Jaeger, 1978; Pascale and Athos, 1981; Trevor, Shendel, and Wilpert, 1986; Tsurumi, 1981).

Of course, the Japanese economic bubble burst. Since then, Japan seems to have lost its edge. In fact, Japan watchers have called the 1990s the lost decade (Porter, Takeuchi and Sakakibara, 2000).

Establishment names in the Japanese economy such as Nissan and the Long Term Credit Bank of Japan almost collapsed. The turnaround often had as a focus newly appointed foreign managers or even overseas trained Japanese managers.

The contrast between the invincible Japan of the 1970s and 1980s and the past-the-best-period Japan of the 1990s is stark. Many macroeconomic factors certainly exist. While the source of the Japanese bubble economy was the credit expansion and excessive liquidity based on speculative land prices, it ended with the instability of Japan's financial industry and bankruptcy for Sanyo Securities, Hokkaido Takushoku Bank and Yamaichi Securities, among others. However, it is also clear that the change in business environment and resulting mismatch for many Japanese firms' business style cannot be ignored.

2. OBJECTIVES OF THE BOOK

During the 1990s not all Japanese firms failed, many survived and some even

flourished. This book's main purpose is the analysis of causes and factors which lead to these companies' success. To this end, a number of successful Japanese firms were identified as displaying management 'best practices'. Best practices which were identified as being applicable to other countries and business environments. In-depth analyses of these companies were conducted to identify common factors which helped them to succeed when so many others failed.

This book therefore focuses on leadership of successful Japanese corporations, a topic not usually considered by Western managers and business academics.

Some authors emphasize middle management as the main source of transformation, namely, constant and continuous adaptation to a changing environment (Kanai, 1991; Kanter, 1983; Nonaka, 1988a, 1988b). But we posit that the CEO's role is far more important to the transformation process – namely, the process of ongoing adaptation. The development or re-establishment of an organizational strategy depends on leadership, and companies' CEOs are the leaders.

This book is concerned with the value business leaders create. Value creation from the centre, especially by the businesses' leaders, is too often overlooked in Japanese firms. The trend in Japan seems to be to regard the bottom-up process as more important than the top-down process. Consequently CEOs are even seen as *expendable* or *fungible* leading to appointment of people with hackneyed ideas, often preferring to imitate competitors' strategy. This strategy comes from the belief that if everybody imitates everybody else and all fail, little blame could accrue to them. This has been predominant in Japanese banks, due to the highly protected nature of the industry, together with managers having limited manoeuvrability.

Throughout the book we discuss two distinct value creation approaches for business leaders. The first focuses on processing data and information through a mental model which enables identification of the levers which will pull profit and which will not. The second approach centres on the essence of shared values (or the image one has of the firm) to pass judgment on new business endeavours. When a new business project does not fit the corporate image, it is dropped.

Throughout this book we will be working to answer the following questions:

1. What common traits do the successful firms possess?
2. Are there some distinctively different approaches to business?
3. How do the different approaches differ in effect? Is one approach more successful than the other?
4. Why do these different approaches exist? Can they co-exist in the same

company?
5. Do the two different approaches add value to a business? How?
6. How can firms continue their success even if there are leadership changes?

To answer these questions, four Japanese companies and their business leaders were studied. The methodology and case study elaboration is discussed in the following sections. Based on the case studies of four business leaders in Japan trying to cope with the adaptation required for their new business environment, we developed a number of propositions explained in Chapter 5. We found differences between business leaders who successfully turned around and adapted to their changed and changing environment and those who did not. We also found an imperative (1) to question all business assumptions and (2) to count, therefore, on a leader free from the old mind-set to conduct business. The cases illustrate this imperative.

3. FOUR COMPANIES AND FOUR CEOs

An in-depth case study was conducted between 2002 and 2003. Sample companies were chosen mainly from Nihon Keizai Shimbun's[2] market capital increase ranking. The Nihon Keizai Shimbun ranks the increase in capital market capitalization of the firms since the current CEOs took charge. From these we selected four Japanese companies which had increased their value over the last decade.

We chose outstanding firms from different industries to give us a wide range of environments. The companies selected were (see Table 1.1):

- Nissan: This automobile company was close to bankruptcy a few years ago and has successfully recovered.
- Shin-Etsu: Is reputed to be one of the few chemical companies in Japan which will survive competition.
- Yamato: Has revolutionized cargo and parcel transportation in Japan.
- Sony: A top-ranking Japanese consumer electronics firm with high quality standards.

The first three firms are included in the Nikkei Shimbun (2002) and have increased their market capital over 34 per cent. Yamato and Shin-Etsu are also considered to be excellent Japanese companies (Niihara, 2002a, 2002b, 2002c, 2002d). We selected Sony as a globally recognized firm in the consumer electronics industry. Above all, we selected these firms based on their reputation and achievement, as well as the fact that their chief executive officer (CEO) was accessible to us.

Table 1.1 Companies studied

Company	Industry	CEO
Nissan	Automobile	Carlos Ghosn
Shin-Etsu	Chemicals	Chihiro Kanagawa
Yamato	Transportation	Masao Ogura
Sony	Consumer electronics	Norio Ohga

When Carlos Ghosn arrived at Nissan, the company was strapped for cash, and unable to undertake needed product line investments. Nissan's problems were variously attributed to excess capacity, appreciation of the yen, overseas transfer of production etc. Ghosn launched the three-year Nissan Revival Plan (NRP) composed of a number of concrete objectives, promising he would resign if these objectives were not achieved in the set time. The results achieved were exceptional.

The second CEO studied is Shin-Etsu Chemical's Kanagawa. During his 12-year presidency his firm's market capitalization reached ¥1598 billion in October 2002, up ¥1142 billion from August 1990.[3] Shin-Etsu Chemical's ordinary profit was 9.16 per cent on its 2001 sales and its net worth to total capital ratio reached 63.03 per cent (Niihara, 2002a). Jack Welch (2001), General Electric's (GE) retired CEO, identified, in his autobiography, Kanagawa as one of the many excellent top managers in Japan courageous enough to push forward their companies' continual renewal.

The Sony case centres on Norio Ohga, under whose steersmanship Sony grew from a ¥1 trillion company in 1982 to a ¥6 trillion company in 1999. The case study describes his personal and professional history as it entwines with Sony's growth.

Finally, we address the question of how Masao Ogura turned around a haulier with a slipping ranking, and in the process revolutionized Japanese haulage.

Much of the personal data (e.g., background, training, career paths), came from the *Watakushi no Rirekisho* column in the Nihon Keizai Shimbun. This column gives a CEO's first-person narration of their firm's decision-processes and implementation.

Overall this sample represents four top business leaders in Japanese firms with remarkable track records. Company performance data for the last six years is shown in Table 1.2.

In the next section we present the methodology and case study elaboration. Studying these four excellent leaders allowed us to identify two business approaches which will be examined more deeply later.

Table 1.2 Sample companies' performance

Name	Nissan	Sony	Yamato	Shin-Etsu
Sales (millions of yen)				
2003	6828588	7473633	975135	797523
2002	6196241	7578258	932120	775096
2001	6089620	7314824	906944	807484
2000	5977075	6686661	812354	678858
1999	6580001	6794619	767655	642795
1998	6564637	6755490	751357	693274
Operational profit (millions of yen)				
2003	737230	185440	56818	122149
2002	489215	134631	53189	114723
2001	290314	225346	52026	112677
2000	82565	240627	44250	87465
1999	109722	338649	39876	86322
1998	84346	520210	34051	82079
Net profit (millions of yen)				
2003	495165	115519	48501	73015
2002	372262	15310	27512	68518
2001	331075	16574	−4181	64505
2000	−684363	121835	20417	48229
1999	−27714	179004	17275	43362
1998	−14007	222068	16208	42027

Sources: Based on Toyo Keizai (2001, 2002, 2003), *Kaisha Shikiho*

4. CASE STUDY ELABORATION

The methodological framework (used in this book to draw the conclusions presented in Chapter 5) is both inductive and deductive, as can be seen from Figure 1.1. Data from many sources, including the researchers' own experience, was analysed, as explained later in this section.

Case studies and primary data from previous investigations and a review of the literature are used as inputs in an inductive process leading to several propositions presented in Chapter 5. It is complemented by a deductive approach. These facts and case studies allowed the two mental models developed, namely the Proto-Image of the Firm (PIF) and the Profit-Arithmetic (PA) which will be further explored in the chapters following.

Case study elaboration followed the scheme laid out in Figure 1.2. As

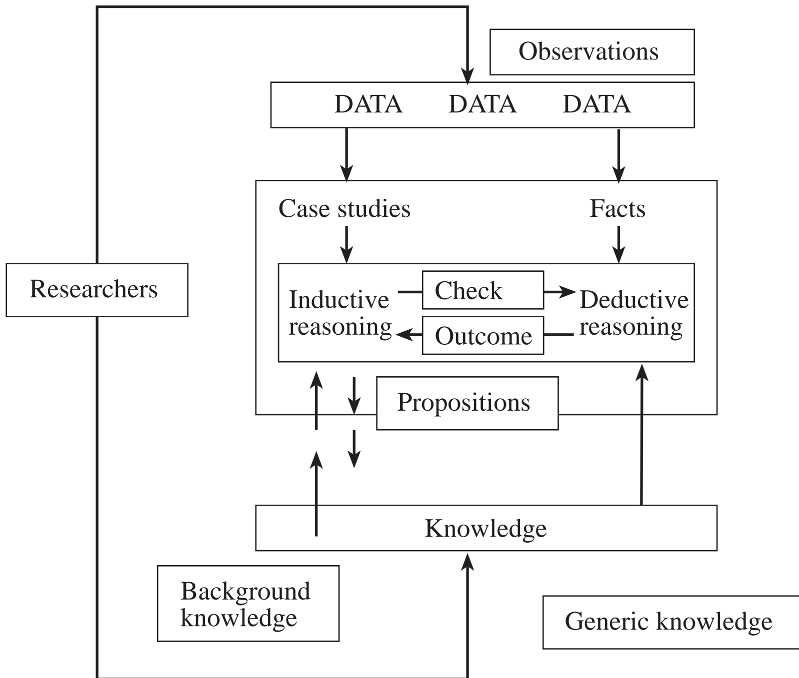


Figure 1.1 Methodological approach

illustrated, several information sources were used. Archival data including magazine and newspaper articles were reviewed and analysed. For more timely information, several Japanese business journals, such as *Diamond Harvard Business*, *Nikkei Business*, *Weekly Diamond*, *Gekkan Keieijoho*, *Shuukan Toyo Keizai* and *Forbes Japan*, among others, were surveyed. Various web sites with interesting information, such as financial information, were checked. Companies also disclose timely corporate events through press releases and their archives, and these were also investigated.

To capture personal insights into the firms, CEOs' autobiographies, books and articles were also significant information sources (e.g. Ghosn, 2002; Kanagawa, 2002; Ogura, 2001; Ohga, 2003). As previously mentioned, the *Watakushi no Rirekisho* column was one of the main sources of information on CEOs' personal data, as it gives the first-person narration of the decision-process and decision-implementation.

To correct possible personal bias in interpretation of the column, draft reports were sent to incumbents of these firms through their public relations department, a window used to contact companies in Japan. When no review came from incumbents or authorized units, telephone or face-to-face

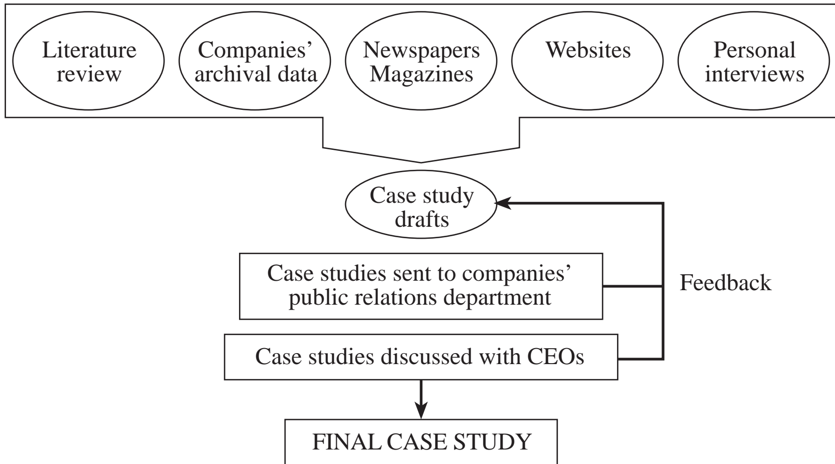


Figure 1.2 Methodology for case study elaboration

interviews were sought with the firm's public relations departments. Unlike their European and American counterparts, Japanese firms' public relations units are usually the first contact point for researchers. Staff normally are well-informed and trained.

To uncover more detailed information, personal interviews were conducted. Interviews targeted those who worked in a variety of positions inside the companies.[4] These interviews' purpose was gathering inside information on how top management dealt with problems faced by the firm.

Once all information was gathered, including their own first-person testimony, cases were drafted. These drafts were mailed directly to their focus individual – the CEOs – for correction of evident misrepresentations. For example, Nissan's President's Office checked the draft on Carlos Ghosn's instructions.

Some case studies were discussed with their focus. For example, the Nissan case was discussed with Carlos Ghosn and students from the International University of Japan, ESADE – Barcelona, Spain – and HEC – Paris, France – by video conference[5] co-ordinated by one of the co-authors of this book.

This feedback helped focus the final case study which constitutes the core of this book.

5. SUMMARY OF THE FOUR CASE STUDIES

In this section we present a briefing of the four case studies of successful

Japanese companies. Full case studies are located in the Annex. The purpose of this section is to give a general overview of the four companies' history, their CEOs as well as their managerial and leadership style.

5.1 Nissan: the Ghosn Era

The announcement in March 1999 that France's Renault would take a controlling stake in Japan's Nissan shocked the automotive world. Symbolically it heralded the end of an age, where Japanese companies had been singled out as a unique force in competition.

People questioned the need for Nissan to seek collaboration with Renault. They wondered what happened to Japanese management which had served as a template during the 1970s and 1980s with the world learning Japanese management techniques such as just-in-time, quality circles and target costing.

One factor deeply affecting Nissan was the burst of the Japanese economic bubble. The company was acutely short of liquidity to meet both its own requirements and requests from subsidiaries which banks had started to withdraw credit from. The firm saw only two alternatives to overcome the situation: (1) to float bonds or (2) seek an alliance with a foreign automaker.

In fact Nissan was excluded from the first alternative. Due to huge debts on its balance sheet and overall poor financial performance Nissan's classification for long-term bonds and commercial papers had fallen to junk level which made it prohibitive for Nissan to resort to this option.

The only way out for Nissan was to find a foreign partner for a tie-up. Ford's CEO, Jack Nasser immediately stated in unambiguous terms that such a tie-up was a non-starter for them. Eventually Nissan started negotiations with Renault.

The European market formed the mainstay of Renault's revenues in 1997, representing 85 per cent of total sales, a third of which came from France. In the same year Renault's world-wide market share was 4 per cent. The merger of Daimler with Chrysler announced in May 1998, convinced Renault that for its survival it needed to look for a partner. It realized it was too small to compete on the world stage, and it was handicapped by being limited to the European market.

Renault considered associating itself with BMW, various Korean car makers, Nissan, Mitsubishi, etc. They eventually rejected Peugeot Citroën as a merger partner, and Fiat was seen as a poor fit with Renault. Ultimately Nissan surfaced as a possible partner. It operated globally and enjoyed a strong base in the Asian and US markets where Renault has no presence. The conclusion was that individually both Renault and Nissan fell short of being major global players, but in combination they could be a significant force.

On 27 March, Yoshikazu Hanawa, Nissan's CEO, and Louis Schweitzer, his Renault counterpart, signed an agreement on the global alliance. Renault would acquire a 36.8 per cent stake in Nissan for US $5.4bn (¥643bn). It was also stipulated that Renault could increase its stake to 44.4 per cent. In turn, Nissan could acquire a stake in Renault under the original agreement.

The agreement included the appointment of a chief operating officer (COO) from Renault to take charge of Nissan's restructuring process. CEO Hanawa would manage external relations including those with the government. He would be also be responsible for alliance issues with Renault. The COO would concentrate on internal activities and operations. Carlos Ghosn, Renault's number two, was chosen as the COO by Louis Schweitzer. Hanawa also saw him as an appropriate person for the position.

Ghosn recalled the day when he arrived at Nissan:

> I don't know how I should express my feeling when I took charge of the post as Nissan's COO. Déjà vu? Sychronicity? Or was it a trick of my imagination? I could not get away from the impression that I was here before.
> 'Here' does not mean the 'place' but the 'situation'. The lack of profitability, excessive penchant to market share, chaos, ambiguous responsibility. There were numerous problems. However, all these problems were familiar to me. I sat in my office and thought as follows.
> 'What I have done so far was for me to get trained and prepared for this moment. The restructuring, reorganization, transformation of the employees' mind-set, merger of two different cultures, and cross-cultural management. If I don't look at the difference in the dimension, I have done all these things.'" (Ghosn, Rivas-Micound and Carvel, 2001, pp. 155–6)

When Carlos Ghosn arrived, Nissan was strapped for cash, and was unable to make needed product line investments. There was excess capacity, the yen was appreciating, production transfer to overseas countries, etc., were all presented as causes of Nissan's troubles.

Ghosn had a different opinion. For him external circumstances such as the economic recession and market fluctuation could not explain why other auto makers including Toyota and Honda were doing well in the face of Nissan's poor performance. He concluded that the difference was management capability.[6] Nissan's management, opined Ghosn, had lost its bearings and not taken necessary steps to make profit a priority. Also, employees had not been given a clear long-term vision.

Carlos Ghosn identified two key problems. First was Nissan's continuous decline in market share: globally eight years in a row and domestically 28 years in a row. Second was dismal performance devoid of profit.

Upon landing in Nissan, Carlos Ghosn took immediate action to redress its profit and loss and balance sheet, boost staff motivation, organize cross-functional teams (CFTs) to review all Nissan's activities, and to restructure the

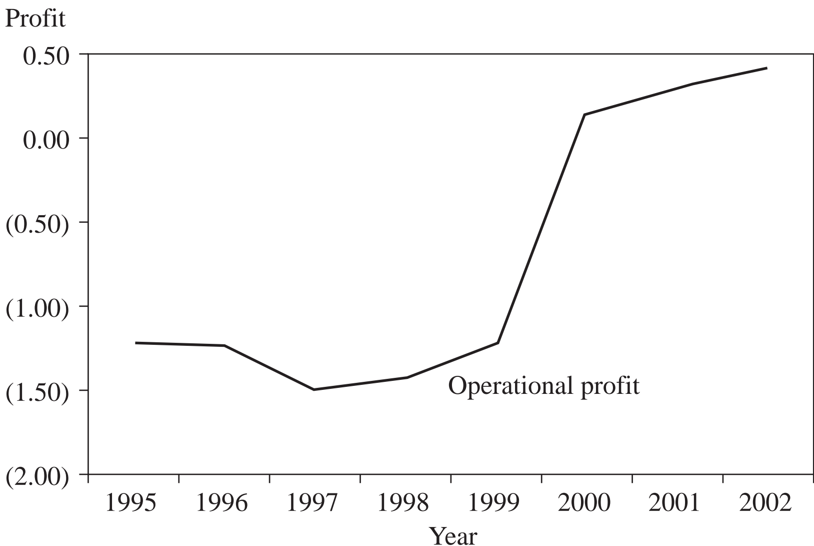
sanctum sanctorum of Japanese management: the relationships with *keiretsu* suppliers, etc.

He launched a three-year plan known as the Nissan Revival Plan (NRP), identified some concrete objectives, and promised his resignation if these objectives were not achieved in the time set. The results of his decisions can be seen in Figure 1.3.

Nissan's success is largely thanks to the cost cutting at the level of SGA (sales, general and administrative expenses), where Carlos Ghosn's previous experience at Michelin and Renault helped him make the right decisions. In his favor too was the realization across Nissan's staff that something had to be done for the firm to survive. Ghosn focused on relevant elements to yield immediate effects such as renegotiating component prices with suppliers.

Another important decision was the widening of information and initiative sources through CFTs, which also served as a communications channel. Within a month of Ghosn's arrival, nine CFTs covering business development, purchasing, manufacturing and logistics, research and development, sales and marketing, general and administrative, finance and cost, phase-out of products and parts complexity management, and organization areas were set up.

> CFT tends to seek change, contrary to incumbent management members. CFT therefore needs to be filled up with intelligent and change-making personnel. If



Source: Based on Gold *et al*. (2001, p. 103) and Toyo Keizai (2002), *Kaisha Shikiho*

Figure 1.3 Nissan's operational profit (in ¥ trillions)

> CFT is too strong it will be jeopardized by management. On the contrary, if management is too interfering, CFT will lose interest in pursuing change. So, striking a balance between these two forces is the key to the success of CFT. (Ghosn *et al*., 2001, p. 173)

Ghosn had the credibility of having achieved good results before. Nonetheless, his forceful personality must be a good reason for Nissan's turnaround. He knew exactly what to do and did it, and moreover, made anyone in Nissan trust him.

5.2 Shin-Etsu Chemical's Chihiro Kanagawa

Jack Welch (2001), GE's retired CEO, in his autobiography,[7] identified Shin-Etsu Chemical's Kanagawa as one of the many senior Japanese managers courageous enough to push forward their companies' continual renewal.

Kanagawa's remarkable performance as Shin-Etsu's president supported Jack's praise. Over his 12-year presidency the market capitalization of his firm reached ¥1 598 billion in October 2002, up ¥1 142 billion from August 1990.[8] Shin-Etsu Chemical's ordinary profit was 9.16 per cent on its 2001 sales and its ratio of net worth to total capital reached 63.03 per cent (Niihara, 2002a).

This is an outstanding feat of managerial creativity in the chemical industry which is a commodity based low-technology industry. Traditionally Japan has not been outstanding in this industry which is dominated by Dupont, Dow Chemical, BASF, and Bayer. With 16456 employees in 2002 Shin-Etsu was comparable to these Goliaths in terms of market capitalization.

The case focuses on Chihiro Kawagawa, the wonder worker in an industry where Japan had not produced a world-class competitor, and who continued to record performance in the middle of recession in Japan in the 1990s and 2000s.[9]

Kanagawa was appointed president of Shin-Etsu Chemical in 1990. Since then the company has outperformed all its Japanese competitors. By February 2002 its market capitalization was ¥1.8 trillion, greater than the market capitalization of Mitsubishi Chemical, Mitsui Chemical, and Sumitomo Chemical combined together (Shimizu, 2002).

Shin-Etsu is the world's number one in silicon wafers and vinyl chloride, number three in silicon resins, and number two in materials for optical fibers. Clearly the firm only focuses on producing and marketing products in which it can successfully compete.

This focus is supported by perseverance and determination. In February 2001 Shin-Etsu invested ¥70 billion on the installations for the production of 300 millimeter diameter silicon wafers. In view of falling demand for semiconductors, other companies thought better of it and would not spend money on expanding production. But Kanagawa went forward with the

investment plan on the view that semiconductor producers would demand 300 millimeter diameter silicon wafers due to the halving of production costs. The decision gave Shin-Etsu ten months' head start over its competitors (Shimizu, 2002, pp. 41–2).

Kanagawa sees the present business environment as characterized by constant change. If managers want to survive in this fluid environment, they have to be ready for any change which may arise. If they are prepared for the worst case, this will be even better.

When in 1999 the US vinyl chloride market was overheated, Kanagawa believed the trend would turn and instructed his staff to renegotiate customer contracts for a longer term and with a price increase. Such renegotiations usually took place late in the year, but Kanagawa wanted to take advantage of the seller's market and have them completed before the summer. Product was in short supply and customers were willing to pay more. Kanagawa predicted the demand would fall in the following year.

While Kanagawa does not deny the need to develop a longer-term plan his view is that long-term vision is the accumulation of daily works. In development of a new business a lack of such a plan will lead to failure. However, when the CEO focuses on short-term daily issues this leads to a bias towards the future influencing their long-term plan. There is one caveat though, the market will never ever move in the direction one prefers.

Kanagawa bases his forecast on the market but is shy of making a plan based on it. Even as he makes one, he tries to foresee a worst case scenario in relation to his forecast. He then maps out a plan to deal with those possible situations.

His ideas about finances are simple:[10] (1) minimize interest-bearing debts;[11] (2) keep the dividend as low as possible, after all in shareholders' interest the company needs long-term steady growth; (3) keep a ROE (Return On Equity) of 10 per cent compared to the current 9 per cent (he does not deify the 10 per cent figure nor is it his intention to increase its treasury shares); and (4) see net income as the clearest indicator of company achievement, on the basis that everything depends whether the firm grows in its quarterly net income constantly or not.

Kanagawa opines that there are two prerequisites for a person who manages to change his firm: (1) he must have clear objectives regarding how to change it, and (2) he must be capable of analyzing the reality.

In his case the first prerequisite was complied with since his objective was clear: to strengthen the firm's financial structure so it could survive any economic downturn. The force working against the 'restructuring' or strengthening the firm was bureaucracy and inherited customs – working by rote and observance of precedent. Combating this force is where the second prerequisite was necessary.

To address the problem of eliminating bureaucracy and inherited vices which were many in a firm established in 1926, Kanagawa, upon becoming president, started to work to change people's mind-set: to call into question accepted wisdom.

In 2003 Chihiro Kanagawa was 76 years old. Shin-Etsu's share price was thought to include the 'Kanagawa premium' (Mayumi, Nishigashira and Tomioka, 2002). Therefore, in the near future Shin-Etsu will face the problem of finding a successor to Kanagawa.

5.3 Yamato: Masao Ogura's Haulage Revolution

The Japanese haulage world has experienced a sea change over the last 30 years. Nobody carries skis or golf bags anymore when they travel to a ski slope or golf club. Shinkansen (the bullet train) travelers move around comfortably without suitcases since they would have been sent already to their destination by a home delivery service such as Yamato Transport's *Takkyubin* service.

Yamato, the inventor or innovator of this new haulage system, had 45 per cent market share in 1996 with 640 million parcels handled (Kon, 1997). In 1997 its market share shrank to 44.6 per cent but it was still a leader in the home delivery service, followed by Pelican's (Nippon Express) 25.2 per cent and Footwork's (Zen Nihon Ryutsu) 9.1 per cent (Yanagihara, 1997). This haulage revolution came about as a brain child of Masao Ogura. This case addresses the question of how a single man could turn around a haulier whose ranking had slipped, bringing about a haulage revolution which changed how Japanese people travel inside their country. The next-day delivery service currently covers almost all of Japan, enabling high-value added articles such as accessories for mobile phones to be manufactured in any plant location.[12] Which signifies another drastic departure for traditional plant selection criteria.

Masao Ogura wanted Yamato to be the best haulier for customers, that is, a company which would transport any quantity to anywhere in Japan. He had the idea of the *Takkyubin* (home delivery service). He was not entirely sure the new business would succeed, but it was clear that Yamato lacked a competitive edge in commercial corporate haulage. Yamato was an underdog, and its only survival strategy was to break new ground in a new business.

He personally drafted a proposal for starting home delivery services and managed to get board approval, though most directors did not support it when asked individually.

In September 1975 a ten-member task force was set up. Ogura and Tsuzuki, the senior managing director, and younger staff and labor union representatives spent two months working out the detail to inaugurate services by January 1976. The distribution network was designed after airlines' hub

and spoke system. In every prefecture the airport was considered to be the hub which would be provided with a distribution centre and depot. From there parcels would be distributed, passing through three stages before their final destination.

As scheduled, in January 1976 the *Takkyubin* service was inaugurated. To begin with the Kanto area, namely Tokyo and its surrounding prefectures, was covered with the next-day delivery service. If a truck had to go to a household there was a surcharge of ¥500. Otherwise there were no surcharges except for freight.

The first month saw only 9000 parcels. Ogura was scared and concerned but decided not to pressure his employees to make money. Instead he emphasized the importance of service quality. His motto then was 'first the service, then the profit'. He was aware that the expansion of the Takkyubin would require a huge amount of money to set up new offices and hire new employees. He also believed that if he emphasized the investment aspect his employees would focus on service quality.

For him drivers were the primary focus. This is why Ogura proposed drivers operate as sushi cooks. Sushi cooks prepare sushi, attend customers, calculate bills, etc. This means that Sushi restaurant performance is largely dependent on the sushi cooks. They have to make their own decisions. So drivers were known as sales drivers (SD). To help SDs a special vehicle called a walk-through vehicle was designed and manufactured by Toyota (Yanagihara, 1997).

The *Takkyubin* service's reputation spread like wildfire. Drivers were initially not keen about collecting money, delivering parcels, etc., which they believed was not their responsibility. But the thank-you from customers and their warm reception gradually altered their opinion. The *Takkyubin*'s positive sides became clear: (1) housewives did not try to negotiate tariffs, unlike corporate customers, and (2) freight was paid for in cash, which gave a breathing space to Yamato's treasury, since corporate customers only paid by bills of exchange.

As soon as their competitors saw *Takkyubin* was a lucrative service, new entrants emerged. Yamato's trademark was the Black Cat (*kuroneko Yamanto*). Others adopted Pelican, Red Dog, Small Bear, Lion, Giraffe, etc., as their trademarks. At one time there were 35 trademarks. This was known as Animal War. Ogura welcomed the competition. He was sure Yamato's service quality was better than competitors.

In 1981 he started a three-year campaign (*Dantotsu Keikaku* – Plan to keep the clear top position) to extend the next-day service area. Over the next nine years, the campaign was renewed twice. Believing any service could be beaten and rather than simply dwelling on the next-day service, Yamato launched a delivery service based on when there was somebody to pick up the delivery.

Many times parcels were not delivered because nobody was at home. Ogura considered it important to shed the logic which favored the haulier, to adapt to the customers' needs.

At the end of March 1990 the campaign concluded after nine years, by then coverage by Yamato's delivery network was 99.5 per cent and 99.9 per cent in terms of area and population, respectively. Next-day delivery comprised over 90 per cent of total deliveries. Yamato had won the Animal War.

In 1991 Ogura resigned as chairman, becoming a special councilor. However, labor unions told him some branches hid accidents and did not report them to head office. Thus in June 1993, Ogura again assumed the chairmanship to 'clean' the organization of the malpractice. He realized that the personnel evaluation system should include concepts such as 'high-mindedness' and 'lofty personality'.

After two years Ogura was unsure whether to continue or not. He consulted H. Miyauchi, then president and encouraged him to exert more leadership. Miyauchi commented that in board meetings people gave more attention to Ogura than to him, which shocked Ogura. This piece of information was decisive and Ogura resigned.

5.4 Sony's Fifth President: Norio Ohga

In 1995 Sony's president Norio Ohga made it public that his successor would be Nobuyuki Idei. His selection was not based on Idei's past achievement, which Ohga thought rather poor. Idei was not successful as head of Audio division; his attempt at entering the home computer business had failed. Ohga was adamant on this: his selection was not based on the past but the potential Idei offered.

Ohga's ideal man to lead Sony was somebody who would dazzle the world with his resplendence.[13] Ohga himself strove to make Sony a company that would dazzle people with its brilliance.[14] Therefore his successor had to be a person who understood Sony's uncommon quality, to outshine its competitors (Takagi, 2001).

Such is the philosophy of a man under whose steersmanship Sony grew from a ¥1 trillion company in 1982 to a ¥6 trillion company by 1999.

The case study describes his personal and professional history entwined with Sony's growth.

In September 1959 Ohga joined Sony at the age of 29. At his request he was appointed senior manager of the second production department in charge of development and manufacture of broadcasting equipment and devices. He immediately took a dislike to Sony's logo and suggested it be changed.

On taking charge of Sony's corporate image ranging from new product development to publicity, Ohga decided the corporate image should be

coherent. At that time Sony's industrial design left much to be desired. Ohga's idea was to give their products the look of luxury goods by combining black and silver. The product body was to be molded in die cast to which a heat-treated coating would be applied. Then part of it would be polished to produce the silver tone.

Believing standardization would need world-wide deployment, Ohga decided to co-operate with Philips. Its Asia representative (V. Decker, later to become the firm's president) insisted on collecting license fees from Sony, as the Japanese firm's stance was that no such payment should be needed if Philips and Sony were to collaborate. A compromise was reached by a free cross enabling the two firms to use each other's magnetic recording technology for free. Inside Philips there was strong opposition to the compromise but Decker persuaded his firm on the grounds that (1) the standard war should be as quick as possible and (2) Sony's support was important.

In 1964, at 34 years of age, Ohga was appointed to Sony's board. Five years had passed since he joined the firm. He was convinced records and audio equipment were like the wheels of a vehicle and complemented each other. In 1965, CBS and Sony set up a joint venture for production of records. By March 1968 CBS Sony officially started with ¥72 million capital and Akio Morita as president. There was a scuffle over whether Sony's or CBS's name should come first. Sony let CBS's name precede its own and kept management control of the new company. Actually conducting the business fell to Ohga as the new firm's senior managing director.

Ohga promised himself that in ten years the new firm would be number one in Japan and should build itself a headquarters building as soon as possible. He was appointed president in 1970 and moved to the company's new headquarters in Ichigaya in 1973. Sales eventually topped industry rankings by 1979. This success was a great help when Sony later launched compact discs (CDs).

In July 1978, a Philips engineer showed Ohga an 11.5 centimeter CD and proposed to make it and an optical disc the world standard. The CD's diameter was the same as the compact cassette. Ohga immediately subscribed to the proposal, believing the record industry must launch a better product than LPs, and saw CDs as such a product. Philips also excelled in optical video disc technology and owned PolyGram. For its part, Sony excelled in audio signal treatment technology and owned CBS Sony. The two companies were an ideal combination.

Co-ordination between the two firms was not without difficulties. Philips insisted on 60 minutes recording time. Sony, led by Ohga, was of the opinion that maximum duration should be determined by considering the music's duration. At that time an LP could not accommodate, for example, the whole

of Beethoven's Ninth Symphony. Based on this, Sony argued a CD should be 12 centimeters in diameter and play for 75 minutes.

Ohga was appointed Sony's president in September 1982 at the unusually young age of 52 for Japan. Ohga, upon taking charge of the firm, promoted CDs.

CD players were sold by 11 manufacturers inside and outside Japan. Due to prices being beyond the reach of many consumers (Sony's CDP-101 cost ¥168 000) initial sales were sluggish. CBS Sony in turn launched many CD items, which helped diffuse CDs.

In autumn 1984, CD sales started to take off, with Sony's D-50 selling at less than ¥50 000, at the behest of Chairman Akio Morita. The industry wisdom saw ¥50 000 as the line below which electrical appliance sales shoot up, but Sony's people were unsure if it would break even. Demand began to exceed supply. Software, namely CDs, began to sell. By 1986 CD sales overtook LPs.

The combination of the software and hardware harmonized nicely due to success in music and film industries. However, Ohga believed Sony needed a further pillar on which to base the firm's performance, and saw that a video game device would fulfill such a need.

The PlayStation (PS) video game device was launched in December 1994, one month after reporting a ¥300 billion loss due to the Columbia Pictures acquisition. At this stage Nintendo dominated the video game industry which is why, with the exception of Ohga, Sony's management had been against entry into this market.

The video game business grew, contributing ¥1 trillion in 2002 between software and hardware.[15] If third-party software is included, PS-related business exceeded ¥ 2 trillion world-wide.

In April 1994 Ohga divided the company into eight divisions each headed by a president – this was the introduction of the business group system with each division called a company.[16]

Ohga resigned from Sony's board on 29 January 2003. He had been chairman of the board since June 2000 after his resignation as chairman of the company. His 'testament' was that (1) Sony should educate new leaders knowledgeable in the software-related business; (2) it should develop new products for the next five years, and (3) it should focus on its brand equity.

6. WHAT'S COMMON AMONG ALL THESE FIRMS

The analysis of these case studies showed several factors common to these 'best performers'. In this section, we present the main common features characterizing these firms, their behavior and their practices. Moreover, in

Chapter 5 we make several propositions developed from analysis of these firms and which need to be empirically contrasted in subsequent research.

6.1 Operational Effectiveness

Operational effectiveness is defined by Porter (1996, p. 61) as ‘performing similar activities *better* than rivals perform them’. It refers to faster product development, defect reduction and any other practice allowing a firm to use its inputs better. Lean production, just-in-time processes and total quality management (TQM) are such practices.

As for many other Japanese companies, the four case studies show firms which have successfully implemented, even pioneered, management practices such as TQM and continuous improvement. These practices led them to gain cost reductions and quality advantages, mainly during the 1970s and 1980s.

One key aspect of Japanese firms is their excellence in operational effectiveness (OE). Our tenet is that these Japanese firms excel in OE due to their handling of information flow inside their organization. This flow enables all components of the organization to share information, skills and resources. This is consistent with existing literature (Nonaka, 1988a, 1988b, 1991; Takeuchi, Sakakibara, Kagono, Okumura and Nonaka, 1986). Our in-depth analysis showed these firms as structurally well supported by operationally excellent middle and lower management. On arrival at Nissan, Ghosn referred to the excellence of Nissan’s middle management.

However, operationally excellent middle and lower management is a necessary, but insufficient, condition for a firm’s success. Eventually a company can outperform its rivals only if it can establish a difference which can be preserved. Thus, constant improvement in OE is necessary to achieve superior performance, however, it is not usually sufficient by itself (Porter, 1996). Most Japanese companies competed successfully on the basis of OE over the 1970s and 1980s, however, rapid diffusion of best practices, supported by consultants, made staying ahead of rivals harder every day. This meant that many OE-excellent companies faced diminishing returns.

Thus, company competitiveness must be based on managerial skills as well as on operational effectiveness. The former is related to top management’s ability to devise and implement strategies and companies which do not qualify as superior performers have problems with managerial skills rather than operational efficiency (Niihara, 2002c).

Hence, our four objective companies have, in addition, added to their operational effectiveness, managerial skills which led them to decide which industry changes the company would respond to and which customer needs the firms will work to fulfill. These companies have leaders, CEOs who make choices and guide their employees to make choices.

The important role these leaders play is broadly treated in the next sections and chapters of the book.

6.2 Breaking the Promotion System

The Japanese employment system and its characteristics have been studied extensively. Life-time employment fostered the view that a person would stay in the same company for their whole professional life (Blumenthal, 1984; Hanami, 1979; Hirakubo, 1999; Leibenstein, 1984; Sullivan and Peterson, 1991).

Due to the life-time employment system (Dore, 1973; Hanada, 1979; Nonaka, 1988a), job rotation is undertaken periodically to produce generalists (Ouchi, 1981; Ouchi and Jaeger, 1978). Levine and Kawada (1980) found how and why Japanese firms set up internal systems for key workers, to build a highly versatile, loyal core of permanent employees. Standardized training is given to ensure everyone has at least average competence,[17] essential to job mobility.

Against this backdrop, Niihara (2002a, p. 5) argues that:

> The personnel policy at Japanese companies thus far has generally been to promote those who have produced exceptional business results in some divisions – the 'hard chargers' – to executive position as a reward for their efforts. Company managers are professional specialists in the field of management. However star players do not always make star team managers.

The common element to the four companies studied is that all of them broke the Japanese tradition of rewarding more operationally excellent middle managers with senior positions. Traditionally in Japan, CEOs are promoted from within, staying at the same firm for their entire careers.

Operational effectiveness as an internal promotion criterion does not apply to the business leaders we studied. As an example, Carlos Ghosn came to Nissan from another firm – Renault. Chihiro Kanagawa joined Shin-Etsu from another company – Kyokuto Bussan – and when appointed president of Shin-Etsu Chemical in 1990, he was CEO at Shintech. Surprisingly, Norio Ohga was a professional opera singer when he joined Sony and pursued both jobs in parallel for three years.

The interesting point is that our CEOs are against this Japanese tradition. To illustrate, Chihiro Kanagawa thinks sending managers with potential to subsidiaries as their top people serves nicely to nurture future leaders. This departs from traditional Japanese personnel policy where managers who had fallen out of competition for the top position used to be sent to subsidiaries (Maeda, 2002). Kanagawa maintains that even if sizes are different, running a firm is not qualitatively different between parent and subsidiary companies.

6.3 Calling into Question the Traditional Way of Doing Business

Corporate failures or collapse can be a consequence of failures to alter response vis-à-vis environment change (Staw, Sanderlands and Dutton, 1981). The ways organizations cope with environmental change influences their survival prospects (Pfeffer and Salancik, 1978).

Nelson and Winter (1982) contend organizational routines – the regular and predictable activity patterns comprising sequences of co-ordinated actions by individuals – can be performed very efficiently with near-perfect co-ordination, but the same organization may find it very hard to respond to novel situations.

A general tendency has been found for individuals, groups, and organizations to behave rigidly in critical situations, this is threat rigidity (Staw *et al*., 1981). In such cases an organization may fail to make sense of the situation (Weick, 1979, 1996, 2001). Commonly this will be displayed as group think or the use of accepted industry recipes (Spender, 1989).

An important feature of firms analysed was they all had an outsider who called into question the company's traditional way of doing business and improved on it.

When assumptions on which the organization has been built do not fit reality – the theory of the business – the organization faces a crisis (Drucker, 1994). A successful company, when faced with a crisis, refuses to confront it. Senior managers may tend to suffer from 'rigidity' and follow a previous decision-pattern, and as a result their firms are likely to suffer draw-backs.

The four CEOs in this study never accepted unconditionally, conventional wisdom or commonly held views. They constructed their own logic, using experience gained from peripheral departments or even another firm to avoid unconditional acceptance of accepted views.

As already mentioned, Carlos Ghosn and Chihiro Kanagawa each joined their firm from another company and Norio Ohga was head of CBS Sony before being appointed to Sony's presidency. This offshoot experience let them view the firm as an outsider which facilitated them questioning the accepted wisdom or traditional way of doing business.

Ogura revolutionized transportation while CEO at Yamato. Ohga's vision of what Sony should be changed the company's corporate image, its advertising strategy, even its product design. One of the toughest problems Chihiro Kanagawa faced at Shin-Etsu was the elimination of bureaucracy and the firm's inherent vices. On the way he had to change people's mind-set. In the same way, one of the main contributions of Carlos Ghosn to Nissan was the change to the firm's business culture.

These business leaders' previous experience in subsidiaries, peripheral departments or other firms helped them to introduce these changes in their

firms and avoid rigidity. This offshoot experience has also been found in similar studies. Niihara (2002b) found being outside the mainstream allowed Fujio Mitarai, the president of Canon USA a chance to observe from outside. When his cousin, son of the firm's founder, died at 59, Fujio was called back to head office to become Canon's president. As an outsider living away from the *curia romana*[18] or headquarters he was not bound by the firm's accepted wisdom, and felt free to (1) sell off unprofitable businesses; (2) withdraw from personal computers, word processors and FLC (ferroelectric liquid crystal) displays, and (3) restructure Canon's divisional structure.

Therefore, one factor common across CEOs we analysed was that all of them were able to reverse how either their company or even industry did business. This meant the role played by these companies' CEOs is critical to these firms' success.

6.4 Transformational CEOs

All these firms have an outstanding 'transformational' CEO with an unambiguous understanding of the scope of his business. That is, they have a clear mental model guiding their decisions. These CEOs clearly have reversed how the firms had been managed. Transformational leaders exert great influence by broadening employees' goals and instilling in them the confidence to perform beyond expectations (Dvir, Eden, Avolio and Shamir, 2002). The four CEOs studied have shown both charismatic behavior and transformational leadership. A transformational leader can motivate followers so that their main goal is to satisfy their self-actualization needs (Burns, 1978). The CEOs analysed also contributed to employees' development of new ideas and questioning of outmoded company operating rules. These attributes support calling them 'transformational CEOs' following Bass (1998).

Courtney, Kirkland, and Viguerie hold that the uncertainty surrounding businesses has four levels: (1) a clear enough future in which managers can develop a single forecast and their strategy; (2) alternative futures with few alternate outcomes; (3) a range of futures, and (4) true ambiguity. 'The clear-enough future used to be a normal circumstance. The information required for decision-making is "inherently knowable"' (Courtney *et al.*, 1997). Based on it, operationally excellent managers can make decisions quite well (Elenkov, 1997; Kono, 1984; Takahashi and Takayanagi, 1985). However, if uncertainty increases, past experience can be more of a hindrance than a help. A prediction based on one's experience could be far from actual events. Judgment on future action at higher uncertainty levels is more safely made based on either intuition or a clear mental model allowing clearer reading of the situation.

Excellent CEOs have an unambiguous understanding of the scope of their business, and construct a new business logic, turning a critical situation to their own advantage.

The top management of these firms knew quite well what value-adding they would create and how they would do so. In terms of corporate-level strategy they knew when they contributed corporate (Collis and Montgomery, 1997) or parenting advantage (Goold, Campbell and Alexander, 1994).

In a similar way, Niihara (2002b, p. 2) contends:

> In the minds of these managers, the company as a whole has become a single concept … this concept serves to narrow the scope of the business that the company should undertake … When these top managers were presented the name of a new line of business and asked if their company would be branching out to this new line, they rejected straight out any line diverging from their company's concept as 'not our company's job'.[19]

The basic argument supporting how these presidents make decisions is, as in Niihara's contention, that they have a 'single concept' of the whole firm. We state that successful CEOs have a clear mental model to guide their decision making.

Nikkei Weekly, cited by Factiva (2002) and *Nihon Keizai Shimbun* (2002), point to a feature common across excellent presidents, which is their ability to articulate a powerful message to the firm's staff, customers, and investors alike. This message has impact due to the president's personality. The conclusion is that these top managers come to embody the image of their firm or brand.

The mental model these presidents have, helps simplify complex situations. This simplified image then helps them in their analysis and decision making. As this is done individually, any decision or analysis conducted carries the force of personal conviction. Employees, customers, and investors are thus willingly persuaded.

This is the main contribution of our book. Due to our in-depth case studies we found two equally successful approaches to doing business: the Profit-Arithmetic approach (PA) and the Proto-Image of the firm approach (PIF). The former operates on processing data and information through a mental model allowing discernment of which levers pull profit and which do not. The second approach centres on the essence or shared values to pass judgment on new business endeavors. These two approaches are explained in the following chapters.

NOTES

1. New United Motor Manufacturing.

2. Popularly named Nikkei.
3. Nihon Keizai Shimbun, 15 November 2002.
4. For the Sony case study, interviews were conducted by Kutsuwada (2003).
5. 25 September 2003 at 16.00–18.00 at Nissan's headquarters in Tokyo.
6. 'In 1995 … the labour cost per car was ¥200,000 compared with Toyota's ¥140,000. On paper (Nissan) had 15,000 people in excess if it wanted to lower its cost to Toyota's level.' (Kai, n.d., p. 27).
7. Published by Nihon Keizai Shimbun's *Watakushi no rirekisho* column between 1 and 31 October 2001.
8. Nihon Keizai Shimbun, 15 November 2002.
9. Sawato (2000) predicted in the chemical industry Japan's survivors under competition from international competitors would only be Shin-Etsu Chemical, Fuji Film, and Mitsubishi Chemical.
10. 'I look at performance figures everyday myself. Figures are the lifeline of a firm. You don't need managers who don't take the trouble of analysing them … Apart from figures, you have to use your sense of smell. When a bad situation is reflected in the figures, it's too late. You have to strain to detect it before it becomes too bad' (Yamagata and Tawara, 2001, p. 61) [translated by the authors].
11. 'When I took over as president the equity ratio was 38 per cent on a consolidated basis. In 2002 it was 63 per cent' (Kanagawa, 2002, p. 38) [translated by the authors].
12. One of the authors' personal conversation with Mr H. Nagasawa, president of Reudo, manufacturer of accessories for mobile phones located in Matsunomae-machi, Niigata-ken, which receives four metres of snow in winter.
13. Ohga cited the Chinese character *san* or *can* as an explanation of this concept. *San* means brightness, brilliance, radiance, dazzling, glittering, etc. (Takagi, 2001).
14. For Sony's history see www.sony.net/Fun/SH/1-36/h.5.html
15. Contrary to this success in video game equipment, Sony's struggle in the computer industry was strenuous. Sony entered the computer industry in the 1960s with a desktop calculator, the world's first of its kind, but was eventually forced to exit. In the 1980s it had a brief success with MSX home PC and NEWS workstation but was again forced to exit the market.
16. For Sony's history see www.sony.net/Fun/SH/1-36/h.5.html
17. This does not mean Japanese firms do not foster a group of elite employees. Hanada (1993) discovered elite staff are chosen by the time they have reached the position of section manager (*kacho*) and groomed for a career in the firm.
18. 'The papal court; the government departments of the Vatican' (*Oxford Concise Dictionary*, Ver. 1.1).
19. Translated by the authors.

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2. Mental schemes of successful transformational CEOs: PIF and PA approaches

1. INTRODUCTION

In Chapter 1 we formulated a question, and in an attempt to answer it advanced several findings from our in-depth case studies. The question being that since the Japanese economy and its enterprises which seemed invincible in the 1970s and 1980s appeared to have faltered, why were some Japanese firms doing well, and what were their common factors? We wanted to know what outstanding business leaders were doing either in turning around their firms or maintaining their excellence.

Chapter 1's findings derived from the point that in a drastically changing business environment the firms needed to appoint CEOs whose mind-frame is not hidebound by accepted wisdom or routines and who could bring about a new business approach. We showed that the main factor underpinning these companies' success over the past decade was the presence of an outstanding CEO with a clear mental model guiding their decision making. When these managers confronted a new situation, they recalled their mental model to resolve the problem successfully.

In this chapter we present the two mental models identified in our study, namely Proto-Image of the Firm – PIF – and Profit-Arithmetic – PA – approaches. In the next section we settle the logical grounds and theory behind our arguments. Basically, our reasoning is based on the cognitive perspective of strategic management literature. Therefore, in the next section we briefly introduce that stream of research and its fundamentals. Then, we present the two managerial approaches identified and compare them with well-known frameworks in strategic management literature. Finally, we conclude the chapter comparing our findings with Niihara's study, another piece of research based on Japanese outstanding firms, to seek generalization of the PIF and PA models.

2. THE COGNITIVE PERSPECTIVE OF STRATEGIC MANAGEMENT

Academics and consultants usually advise managers to undertake an objective, rational and exhaustive analysis of competitors and industrial environment as well as an internal analysis to identify organizational strengths and weaknesses together with key resources. While this is an important part of the strategy formulation process, sometimes the information obtained with these analyses is ambiguous and insufficient and, in any case, it must be interpreted and a judgment made to reach a decision.

The stream of research within strategic management which tends to understand how managers use information and their own knowledge to make decisions is called the cognitive perspective of strategic management.

The cognitive perspective is used to study ‘perceptions’ or how managers obtain and process information, it is used to study ‘conceptualization’ or how strategy is formulated, and ‘re-conceptualization’ or how strategy changes and why. It is also used to study ‘management style’ or how managers differ in their cognitive orientations (Mintzberg and Waters, 1985). This stream of research tries to analyse how managers conceptualize strategic problems, how they develop their own rules and heuristics, and how this influences decision making (Schwenk, 1995).

Strategies are strongly influenced by two kinds of forces (Anderson and Paine, 1975): perceptions of the degree of environmental uncertainty and the vision of a change in the business. Managers do not perceive the same degree of uncertainty and this has implications for the strategy formulation process (Daft and Weick, 1984). The cognitive perspective flows from denial of the assumption that managerial decisions can be correctly analysed using notions of rationality, well-defined objective functions and logical election processes (Eden and Spender, 1998).

The mind of the strategist, therefore, is the main unit of analysis in the cognitive perspective of strategic management. Due to limitations in information processing, human beings can only pay attention to a limited amount of information (Miller, 1956). These limited capabilities of processing data or bounded rationality (Simon, 1957) are used to process a huge amount of ambiguous information (March and Simon, 1958). Managers, aware of this fact, must rely on experience and learning to help them choose which information should be used and attended to, and which not. Managers, then, use their memory as well as new information when taking decisions.

Managers have to rely on simplified representations of the world to make sense of it (Kiesler and Sproull, 1982). Sense making is concerned with such things as placement of items into frameworks, comprehending, constructing meaning and integrating in pursuit of mutual understanding (Weick, 1995).

According to Walsh (1995) two types of information processing characterize strategic thought: 'bottom-up' and 'top-down'. The former is information-driven, that is a manager, confronted with a new situation, from the 'bottom-up' will gather all available information and analyse it, considering all possible options before making a decision. This process tends to be rational, however, it is time-consuming and speed is key to strategic decision making.

In contrast, 'top-down' information processing is 'theory-driven'. When a manager is confronted with a situation, they will recall their own theories of how the world works, accumulated through learning and experience, and will make a decision based on their own theory. These personal theories are called 'mental schemes' or 'mental models' (Johnson-Laird, 1983). These mental models are simplified, generalized and abstract representations of the world. When recalled for a new situation, mental models often help identify relevant information and influence subsequent behavior. However, a mental model can be applied unconsciously (Dutton, 1993).

Top-down and bottom-up processing are not mutually exclusive; both modes can operate in any given situation. However, top-down processing of information is quicker and usually helps to fill information gaps, it therefore is likely to predominate in managerial situations (Walsh, 1995).

Figure 2.1, adapted from Daniels and Henry (1998, p.314) shows the two approaches identified by Walsh (1995).

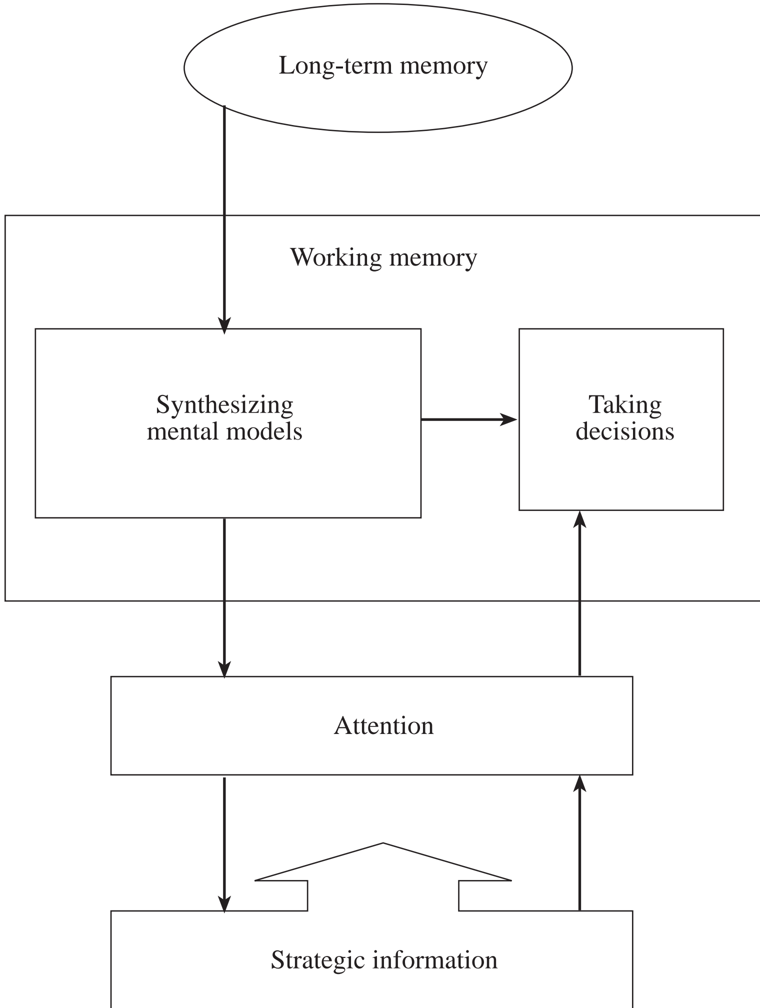
As mentioned in the previous chapter and the introduction of this one, the four cases' commonality was that they were all managed by an outstanding CEO with a clear mental model to guide their decisions. All four CEOs had a clear theory, what we call a mental scheme to guide their decision making.

In Japan, traditionally, most firms were managed on a bottom-up or information-driven basis (Aoki, 1988; Bower, 1974; Kanai, 1991, 1993a, 1993b; Kanter, 1983; Nonaka, 1988a, 1988b; Ouchi, 1981; Pascale, 1988; Shimzu M., 2002; Shimzu N., 2001; Shimzu R., 1986). In contrast, we found these outstanding firms to be managed on a top-down basis, which is closer to strategic thought. These CEOs manage their firms based on their understanding of their business's scope. Their mental model guides their decisions, so when confronted with a new situation they recall their mental model to solve the problem.

In our study, we found two different approaches or mental schemes which we will discuss in the following sections.

3. TWO MANAGEMENT APPROACHES: PROTO-IMAGE OF THE FIRM AND PROFIT ARITHMETIC

The four in-depth case studies on front-rank business leaders allowed us to



Source: Adapted from Daniels and Henry (1998, p. 314)

Figure 2.1 The process of strategic thinking

gain an insight into these leaders' workings, which led us to identify two different, equally successful, business approaches. We called these the Proto-Image of the Firm (PIF) and the Profit-Arithmetic (PA) approaches.

In this section we will define these approaches and analyse their applicability, as well as their significance in the strategy literature. Further implications for corporate-level strategy will be also discussed.

3.1 Explanation of the PIF and PA Approaches to Business

The four cases on Japan's excellent CEOs (Nissan's Ghosn, Yamato's Ogura, Sony's Ohga, and Shin-Etsu's Kanagawa) provide superb examples of the thought-process of outstanding top managers.

On the one hand Sony's Ohga has a clear image of what the essence of Sony is, or should be and on the other, Shin-Etsu's Kanagawa acts based on his extraordinary business acumen which allows him to discern what levers should be pulled if profit is sought. Both succeed despite the differences in their business approaches.

It goes without saying that Ohga does not ignore profit levers entirely nor that Kanagawa lacks a corporate image against which he compares decision alternatives to check their fit.

We call Ohga's way of basing his judgment on a specific image of a firm the Proto-Image of the Firm (PIF) approach.[1] By contrast Kanagawa obviously operates on the basis of processing data and information through a mental model which enables him to discern which are profit levers and which are not. This we call the profit-arithmetic (PA) approach. The resulting question becomes, how do these approaches operate? Daft and Weick (1984) regard organizations as interpretation systems. There are four interpretation modes and each one is determined by management's beliefs about the environment, and organizational 'intrusiveness' – the degree to which proactive interaction with the environment is enacted.

In essence, people and organizations must make sense of every situation they face. This involves simplifying the situation (Bateman and Zeithaml, 1989; Calori, Johnson, and Sarnin, 1994; Ginsberg, 1990; Schwenk, 1984; Stubbart, 1989; Zajac and Bazerman, 1991). Our thesis is that the simplification takes place in the mind of business leaders[2] using one of the two approaches – PIF or PA. Graphically this process may be represented as follows (see Figure 2.2).

Factual phenomena are perceived to be complicated but their complexity is greatly reduced when the mental filter is applied to simplify and then to make sense of them by placing them in a meaningful context. Business leaders follow this thought-process many times without realizing it.

Which of the approaches is applied depends on the leader's training, experience, character, business environment, etc. A switch from one approach to the other cannot be done at a point in time, since its adoption is rooted deeply in the mind-set of the person applying it.[3] A change, either gradual or sudden, in the business environment, drastic restructuring, imminent demise of a firm due to near bankruptcy, etc., may make the switch possible or even inescapable.

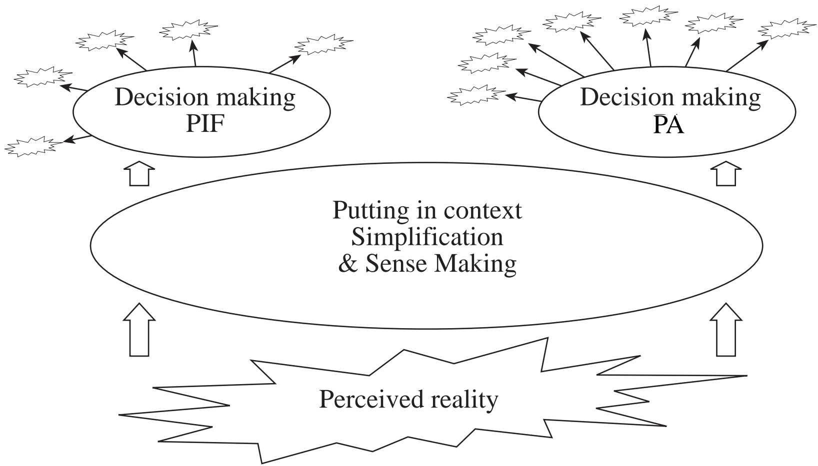


Figure 2.2 Simplification process

3.2 Proto-Image of the Firm Approach

PIF is an idiosyncratic concept relying on the manager's mind. While it is a personal theory, it could be codified, made explicit, and be transmitted to other people. When a firm is created, its founder has, most times, an image, a proto-image of what their firm is, should be or what they want it to be.

The founder's PIF guides the formation of the firm's culture and ideology. When a new CEO comes to the firm, becoming part of it, they build their own PIF of the company. In the process, several factors contribute to development and shaping of a proto-image.

First, the new CEO's personal and professional background clearly influences their vision of the firm they have just joined. Previous experience in other companies, industries or departments will help interpret what the firm is or what it should be according to their personal judgment.

Secondly, organizational culture strongly influences the way a PIF is developed and shaped. The stronger the firm's culture and ideology, the greater the chances that a new CEO's PIF will be similar to the founder's.

Finally, when a new employee joins a firm, a socialization process starts. In this process, this new member develops an idea of what the company is. Some companies have institutionalized this process in which the individual receives information on the firm's products, markets, organizational structure, culture, philosophy and ideology. Obviously, this process is also present when a new CEO is contracted and the process strongly influences how this individual shapes their proto-image of the firm.

Therefore, there is an important institutionalization process in how a PIF is developed and shaped. Socialization inside and outside the company deeply influences how a PIF is shaped. The stronger the firm's business culture and the stronger the socialization process, the greater are the chances that other members will share a similar PIF of the firm. A strong company's culture could explain, for example, why there is convergence among individual PIFs in the board of directors at Sony.

Moreover, educational programs and the existence of 'interoganizational macrocultures' (Abrahamson and Fombrun, 1994) also help the similarity of PIFs among individuals. However, it should be clear that a PIF, as a mental model, is a cognitive idiosyncratic vision of what the firm is or should be that is in the mind of an individual.

Personal and professional background plays an important role in PIF formation, as well as social and institutional influences (Figure 2.3).

A PIF, as a mental model, can be considered as an interpretive mode of an organization (Daft and Weick, 1984). It is therefore determined by the CEO's beliefs about the environment, and the degree to which proactive interaction with the environment is enacted. Hence, environment plays an important role in how a PIF is shaped.

PIF is an abstract vision of the firm which does not necessarily need to account for resources and capabilities, as some CEOs, while aware of their PIF may not know what resources and capabilities there are, or at least, may not think in those terms. Some CEOs may have a PIF based on core competences, some on key capabilities and some others on a market domain. In any case,

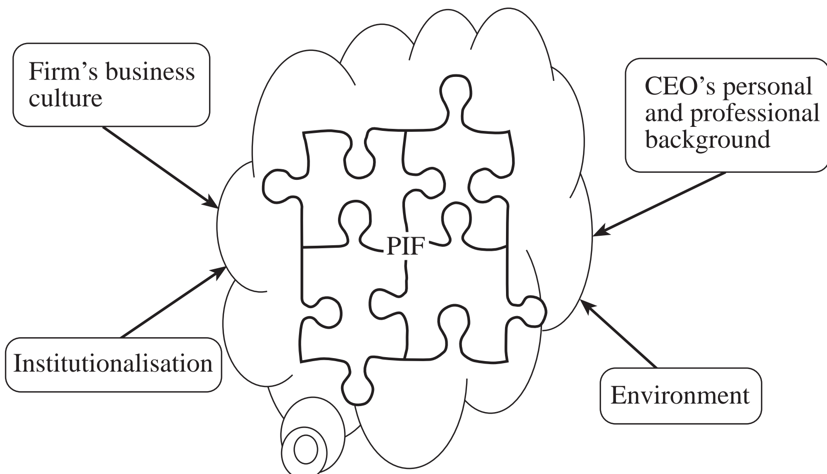


Figure 2.3 Proto-image of the firm approach

CEOs with a PIF approach clearly know what their firm is, should be or could be in the future, and this proto-image guides their decision making.

In Figure 2.3 we have presented PIF as a piece of a puzzle. This helps us to understand how this approach works. When the CEO faces an investment opportunity, this decision is contrasted against their PIF. If the new investment matches or fits their PIF, then the investment occurs.

By contrast, if the new business opportunity does not fit with the CEO's proto-image of the firm, the investment does not get approved. This does not mean no profit-and-loss analysis is made, however, the principal criterion in investment selection is whether it matches the CEO's PIF. Profitable or potential opportunities will be misestimated due to their poor fit with the PIF. Obviously, *a priori* non-profitable business moves will not be undertaken even if they fit the PIF. However, if this is the case, long-term profits will be considered and the CEO will be comfortable with initial losses in the conviction that 'it is part of what the firm should be in the future'. In the same way, if more resources are needed to make the investment profitable in the future, the CEO will accept it as soon as it matches their PIF.

PIF business leaders make sense of their situation by analysing and contrasting it against their model. The fit with the proto-image of the firm is the starting point. Associated variables around the PIF are selected *a priori*. They are ordered by importance and facilitate simplification of the situation. Go or no go then is just a question of fit.

A PIF is not static. The proto-image is influenced by several factors including personal background, the firm's culture, institutionalization and environment, as mentioned already. Hence, a PIF usually evolves as the environment does, and according to the CEO's perception about the way the environment is evolving. Therefore, the PIF reacts actively to environmental changes. In changing business environments, firms must adapt to them by renovating existing businesses, developing new products, and/or entering a new business domain through vertical or horizontal integration, or geographical expansion. A PIF approach to business can help managers successfully guide their firms in this process.

Unfortunately a business-domain change may deal a fatal blow to the firm's performance since, despite management's initial enthusiasm, the corporate structure, organization, etc., may not provide enough support. A strong PIF which is translated to employees through the firm's culture could help the organization react as its leader wants.

3.2.1 PIF, ideology and culture

Collins and Porras (1996) held that the companies which had outperformed the general stock market by a factor of 12 since 1925 had a vision of their own. One of the most popular concepts in the 1980s was that of culture; specially

after Peters' and Waterman's book *In Search of Excellence* (1982). The authors claimed successful organizations were rich in culture, at times used interchangeably with ideology.

An ideology consists of core values and purposes permeating the organization. The former refers to a system of guiding principles and tenets, and the latter to the organization's reason for being. Ideology converts an expendable organization into an institution with a life of its own (Selznick, 1957). That is, institutionalization implies infusing the organization with value. Mintzberg (1983) adds that an ideology 'ties individuals to organizations', generates an 'esprit de corps', a 'sense of mission'.

Collins and Porras (1996), in an interpretation of Sony's values, define core values as a company's essential tenets. According to them, Sony's values are reflected in:

- elevation of the Japanese culture and national status
- being a pioneer – not following others; doing the impossible
- encouraging individual ability and creativity

These same authors cite Sony's core purpose (namely, a company's reason for being) as:

- to experience the joy of advancing and applying technology for the benefit of the public.

The differences between ideology and the PIF concept reside mainly in two aspects: (1) a static versus dynamic view of the firm, and (2) its capability to enact a firm's development.

First, a common criticism of the ideology framework is that it runs the risk of culturally locking in firms or an individual (such as the CEO) resulting in their inability to change corporate culture in the face of clear market threats (Foster and Kaplan, 2001). The CEO is shackled by the chains of the organization's ideology. However, companies consistently turning a profit are those which re-invent themselves continually to outperform the market (Mirazita, 2002).

PIF, by contrast to the ideology concept, encourages firms to re-invent themselves.[4] Furthermore the role of the PIF lies within the individual rather than the organization. This PIF, a mental schemata, is not an inner state individuated independently of cultural context. Instead the PIF approach grows from the individual's experience, of contact with similar businesses, staff meetings, conversations with other executives, news, business comments, etc. It must be realized that, in contrast to the ideology perspective, the PIF is not limited by the organization's culture or ideology. While the organization

can have an identity of its own (with staff sharing beliefs, values, etc.), it is the schemata of the CEO which prevails in terms of the organization's dynamic.

The PIF approach is conceivably a mental prototype, a sort of universal generalization about the image of the firm. A prototype has the advantages of embodying a whole range of complex generalizations and co-occurring features about an organization and at the same time it provides the flexibility that is precluded in the strict universal generalization (Churchland, 1991). The PIF is not representational in that it does not stipulate the existence of underlying symbolic representation in the person's mind. Rather, it assumes the substrate of cognitive activity to be a large neural-like associative network. It assumes operations in connectionist models are not ones of symbol manipulation, but rather parallel distributed patterns of activation in the network. Although we have explained the PIF as a form of schemata, we use the term metaphorically. In other words, the PIF is a set of connection strengths which, when activated, implicitly have in them the ability to generate states that correspond to instantiated schemata.

The challenge in determining the PIF is posed as to what constitutes a PIF, and how to determine the features around this central concept. The first challenge refers to specifying what make the very basic, constituent elements of the PIF. The second refers to how the PIF is formed around features which come close together to form the core PIF and what constitutes closeness enough to be part of the core. In this regard, we can use the connectionist theory to explain the PIF phenomenon. This theory can guide us to understand and recreate the PIF by which CEOs approach companies and decision-making processes.

The second major difference with ideology is that the PIF, when enacted by the CEO, as shown in the analysis of Sony, drives the firm to a continuous assessment of its theory of the business and acts as direction setter of its corporate renewal. In the case of ideology the company seems to run because there is an integration of individual and organizational goals (Mintzberg, 1983), it brings about the same effect as Campbell, Devine and Young's (1990) 'sense of mission'. A sense of mission is an emotional commitment, which occurs when there is a match between the values of an organization and those of an individual. In the case of the proto-image of the firm, the CEO reviews their theory, and uses this mental structure to direct his or her decisions. An ideology by itself is not enacted except through the leader; and under the ideology concept, the organization has a life of its own which develops and reinforces through several mechanisms. This concept leaves little room for the individual, the CEO, to make decisions, unless they fit the ideology of the organization. In our review, we also see CEOs having an independent understanding of the firm and acting on their own proto-image to give the firm new directions.

3.3 Profit-Arithmetic Approach

PA is, like PIF, an idiosyncratic concept relying on the mind of an individual. CEOs with a PA approach guide their decision making not on the base of their image of their firm, but on the possibility of making profit.

Their mental model is more analytical and rational than the PIF. They base their decision making on their knowledge of the industry, of their firm's resources and capabilities, strengths and weaknesses or, sometimes, on their own 'sense for business'.

An important factor playing an important role in how a PA approach is shaped, is context. A PA CEO knows what levers should be pulled to make profit or what gears will make returns from an investment. The profit levers are not always the same ones. They depend on the environmental situation the firm and industry are facing.

CEOs with this approach base their decisions on analysis and their own knowledge and previous experience. Analysing a situation involves a simplification process. This simplification takes place as a consequence of

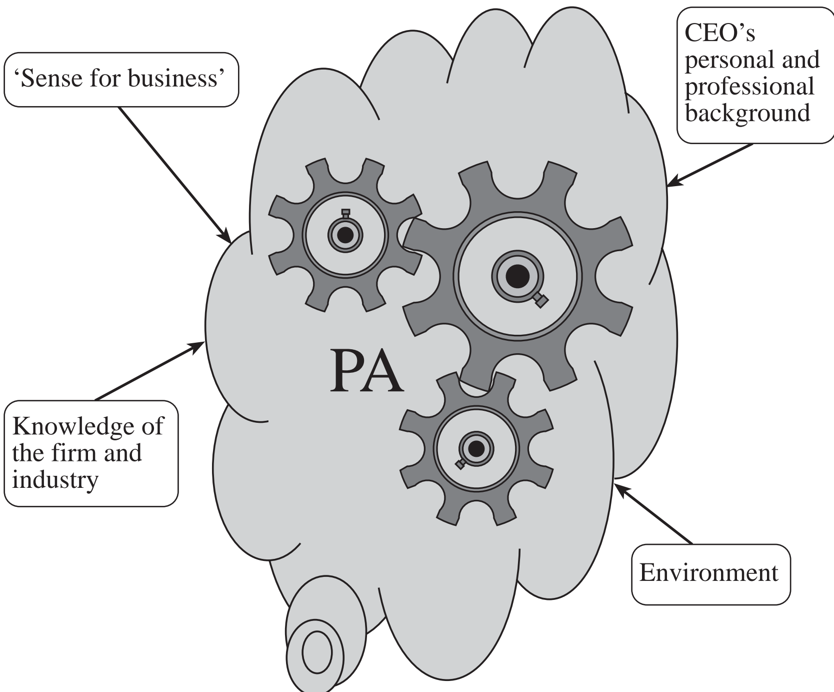


Figure 2.4 Profit-arithmetic approach

classifying the situation into a pattern business leaders have lived in the past. Therefore, experience is key to this approach. Short-term, feasibility analysis is more important in the PA approach than in PIF. However, this does not mean that loads of information are needed to make a decision. A PA manager knows what kind of information is relevant for every case and will demand that information.

Therefore, the factors shaping this approach are the CEO's professional and personal background, their knowledge of the firm and its industry, their 'sense for business', and the environmental situation (see Figure 2.4).

PA business leaders make sense of the situation they face by looking for similar prior situations. Patterns learnt in the process of their business career have taught them how to endow meaning. Prior success or failure experience guides them in their analysis leading to feasible alternative solutions. The selected solution's goodness of fit is a function of the richness and variety of their experience.

However, when uncertainty is high or when the situation is completely new, PA managers make a decision based on their sense for business.

A 'sense for business' is an important component of the PA approach. Kanagawa, consistent with existing literature on the resource-based view of the firm (Barney, 1991), holds that there are things one cannot do anything about – will and effort cannot change them.

Inspiration and luck are two of those things. A manager with a 'sense for business' is the one who has been lucky and inspired in key moments and has been able to take advantage of this.

CEOs' internal and external knowledge is key in a PA approach. A CEO must be aware of profit levers, that is, where there is waste which should be cut, where value is created and which areas need prioritizing. This knowledge allows them to take the right decisions.

As well as in PIF, personal and professional background also shapes a PA mental model. However, the way professional background affects PA is different than for the PIF. Throughout their professional career, a manager gets impressions from different firms, industries, management settings, sometimes even different countries or geographical locations. This experience helps build the PA, identifying profit drivers through different situations. Sometimes profit levers can be similar, sometimes not.

CEOs with a PA approach focus their attention on everything which may enhance the firm's profit potentiality. They tend to concentrate on profit levers such as cost cutting and on actions relating more to daily operations. A *grand design* for the future does not interest these business leaders. Diversification or new product launches are shirked as involving too much risk. But if pursued, risk is diminished by only taking up options the business leader can see as profit generators.

3.4 PIF and PA Compared

In order to differentiate between the two approaches, in this subsection we will explain the main differences between them regarding their time-frame, applicability, etc. The comparison of PIF and PA is summarized in Table 2.1.

As we have tried to make clear in the previous subsections, the essential element of a PIF approach is the 'image of the firm', an abstract conceptualization of the business which guides a CEO's decision making. In contrast, a PA approach is more pragmatic, where actions oriented to profit levers are key.

The constituent factors of each mental model are also different. PIF is shaped and influenced by the CEO's professional experience, environmental situation, firm's business culture and ideology and institutionalization process. The first two factors also shape a PA mental model; however, as explained before, their influence is different. The other elements shaping a PA approach are a CEO's knowledge of the firm and the industry in which it operates and their 'sense for business'.

A PIF approach needs the manager to possess previous knowledge or familiarity with the firm, its culture, tradition, etc. This is essential if a CEO is to manage it effectively. As we have mentioned, a PIF is shaped by the firm's business culture, however, it does not mean they are identical. A PIF in a transformational new CEO may be quite different from the actual situation of the firm, and may imply change is needed in its business culture and routines. In this case, familiarity with the firm is essential as employees will have to change their own image of their firm to adapt to the new CEO's PIF. The fact that decisions will be based on the CEO's abstract image of the firm will make then harder to understand for other company members. If the CEO is familiar with how things were done previously, they will be better able to explain their approach and new practices needed to accomplish it.

Although desirable, familiarity with the firm's culture and ideology is not essential for a PA approach. Business leaders with a PA approach may have few problems changing firms as they know key industry success factors. Their short-term orientation and the quick results flowing from their decisions make them more trusted by their employees. Moreover, the fact that their decisions are based on a clear 'profit-seeking' basis will make the decisions more understandable to staff.

In terms of the time-frame, the PIF approach focuses more on a mid- to long-term time-horizon, while PA is more action- and operations-oriented, focusing more on short-term results. Apart from business leader personalities, this difference may derive from the firm's balance sheet, and profit-and-loss situation. If a firm is short of cash or is losing money, it must prioritize cash flow. In any case, a PIF manager will not be in a hurry to build their image of

Table 2.1 Comparison of PIF and PA approaches

	PIF	PA
Essential element	Image of the firm	Actions oriented to profit lever
Shaping or constituent factors	Professional background, environment, firm's business culture and institutionalization	Professional background, environment, knowledge of firm and industry and 'sense for business'
Familiarity with the firm	Necessary	Not so essential
Time frame	Focus on mid- to long-term	Penchant for short-term
Domain	Wide, new competences and products are fostered	Narrow, existing portfolio
Cash-flow position	Affluence required	At the time of crisis, the only option is to survive
Explicit or implicit instructions from the top	Implicit, second-guessed	Explicit
Applicable when changing firms?	Difficult	Possible
Succession	Relatively easy to find a person with a similar approach, if they share the belief	Imitability or replicability low
Combination with the approach	PIF – top management PA – lower management	If PA at the top, PIF other not possible at lower levels

the firm. They are aware it will take time and all decisions must be focused on a long-term orientation (see Figure 2.5).

In contrast, a PA manager does not need to fulfill any image of their firm. Moreover, they are profit-oriented; therefore, any time-frame will be shorter than for the PIF approach. This does not mean PA managers do not think ahead nor consider long-term results. A PA approach will accept short-term losses, certain that there will be mid- to long-term benefits.

In terms of domain scope, the PIF approach is more inclined to domain selection (Bourgeois, 1980). New product development, new business

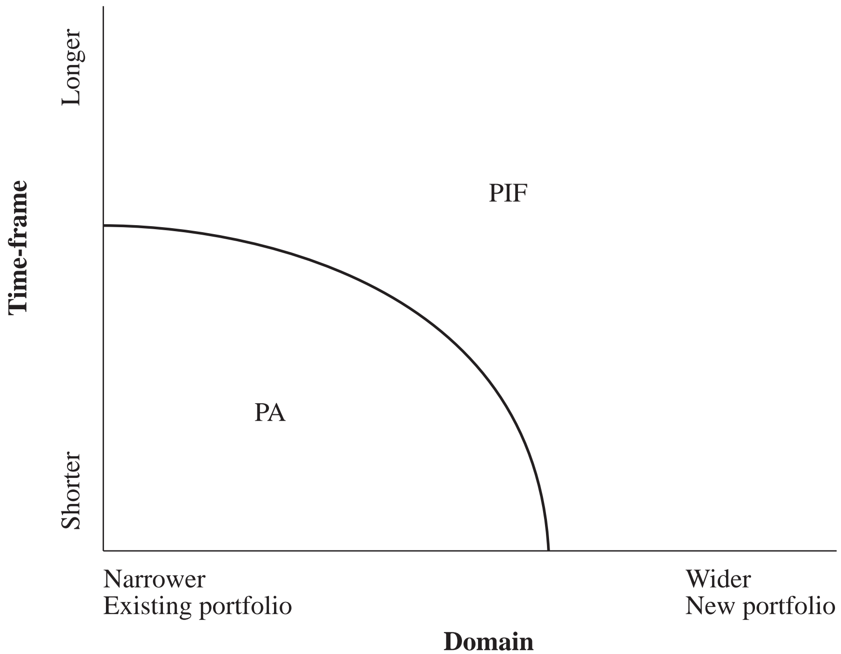


Figure 2.5 PIF and PA approaches compared

exploitation, fostering new core competences, etc., are its main concern. PA is in this sense more centered on domain navigation (see Figure 2.5).

A PIF manager requires cash flow to fulfill their idea of the firm's potential. This may imply new investments, acquisitions, vertical integration, etc. For a PA manager cash-flow generation is essential if the firm is losing money or is short of cash. Therefore, cash-flow position for a PA approach is more dependent on numbers, while the firm's actual situation, compared to the CEO's PIF, is important to the other approach.

Staff can better second-guess top management's intention with a PIF approach when it is accepted by organization members. If the CEO has 'imposed' their image of the firm throughout the business culture, employees fully understand what is expected of them, and know what they should and should not do. This also means that if a CEO (who, for example, is somebody who came from outside) wants to have something done which does not fit the firm's previously shared values, they will find themselves utterly impotent. Their intentions will be sabotaged actively or passively unless they effectively transmit their image to the other staff. Therefore, when a CEO's PIF is effectively transmitted to employees and their own vision corresponds, top management instructions do not need to be explicit, as members can interpret them using their own PIF.

On a PA approach, top management instructions are more explicit and staff members do not have to apply their own vision to interpret them.

A PIF approach is inherent to a particular firm. That is, it is a particular vision an individual has of a company. Therefore, when this individual leaves the firm and joins another company they build their own image of this new company. A CEO with this approach who changes to a new firm must build their PIF of the new one. In this process, previous experience may help shape the new PIF, however, as it is indivisible from the firm, the proto-image of the new firm will of necessity be different from the old PIF even if both firms are in the same industry.

A PA approach does not necessarily depend on the particular situation of a firm or its tradition. Moreover, a PA approach usually benefits from experience. In this sense, PA managers are more 'versatile' and their mobility is higher. This approach is easily applicable to different firms from different industries if profit levers are similar.

It is also an interesting point to consider in which of the two approaches it is easier to find a successor. As discussed, with the PIF approach, effective management presupposes full understanding of the firm's shared values. If a successor has imbibed these values succession should be less of a problem. Therefore, though more abstract and conceptual, a PIF approach can be better codified and made explicit, thus it should be easier to find a successor, either inside or outside of the firm, with a similar PIF.

Conversely, a PA CEO will have learned the approach, cultivated it intentionally based on their individual experience and business sense. Less observant successors may be unable to comprehend the intricate mental scheme of their predecessor.

It is also important to remember that 'you cannot have a longer view than your boss' (Goold and Campbell, 1987a). At the beginning of this subsection we compared the time-frame within which the two approaches work, arguing that PIF has a longer time-orientation than PA. It is understandable therefore, that PIF CEOs can be more tolerant than their PA counterparts over quarterly results and may allow more staff maneuverability. In contrast, subordinates of a CEO with a PA approach who views their issues long-term may run the risk of being defenestrated from the firm. The models can be combined in a firm as long as PIF is at top management and PA at a lower level. The other way round seems very unstable.

4. CORPORATE STRATEGY AND THE TWO BUSINESS APPROACHES

This book is concerned with study of an organization from the view point of

strategy. Strategy is, following Chandler (1962), the determination of the enterprise's long-term goals and objectives, together with adoption of courses of action and allocation of resources needed to carry out these goals. The assumption underlying strategy is that the primary goal of the enterprise is to be profitable over the long term.

Strategic management involves answering two questions:

'What business or businesses should we be in?', and
'Within a particular business, how should we compete?'

The answers to these questions define the two major areas of a company's strategy: corporate strategy and business (or competitive) strategy. In this book we bring to a point the first question from the perspective of value creation from the top of the firm.

Strategic decisions at the corporate level are related to the scope of the business in terms of markets and industries (Grant, 2002). Corporate strategy decisions include diversification investments, vertical integration, acquisitions, new ventures, and resource allocation among different activities of the firm.

PIF CEOs will tend to undertake investment projects if they fit their proto-image of their firm. These investments can be aimed at diversification or at vertical integration. No clear pattern can be expressed *a priori*; it depends on the PIF. A CEO with this approach will always think of the company as a whole, which means resource allocation decisions are made on this basis. Non-rational investments can be made, on expectations they will lead the firm to the CEOs' PIF.

It should be clear that PIF CEOs do analyse and consider the potential of an investment before undertaking it. However, this analysis is not crucial, although it has its weight in the final decision.

On the other hand, corporate strategy decisions by a PA CEO are based on analysis of their potential to contribute to profits. PA CEOs require a deep analysis of business opportunities or investments before undertaking them. If the potential is not in doubt, then the decision is made. Of course sometimes deep analysis cannot be conducted due to limited time, in this case, the CEO's experience and 'business sense' guide the decision.

Two major studies have thrown light on the value-creation role played by the firm's corporate center. One of these is Porter's (1987b) typology of defining corporate strategy in terms of how corporate management creates value in a diversified company. The other is Goold and Campbell's (1987b) study on corporate management styles in large diversified British firms. In the next subsections we compare both studies with the findings presented in our research on outstanding managerial leaders.

4.1 Porter's (1987) Study on Corporate Strategy and the Two Models

Porter (1987) identified four generic corporate strategies – portfolio management, restructuring, transferring skills, and sharing activities. The center creates value differently in each of these strategies.[5] In this subsection we analyse each of these four strategies and see how value is added from the two different business approaches presented in this book (see Table 2.2).

In a *portfolio* strategy the center creates shareholder value by using its expertise to spot attractive acquisition candidates. Fund-raising ability at the center is another source of value creation. Banking and reviewing are main roles. The company identification is based on its adjustment or fit with the proto-image on a PIF approach, while it is profit-based on a PA approach.

Another difference among the two approaches regarding this corporate strategy is that on a PA approach, the corporation exerts strict financial control over the business units. This financial control is looser on a PIF approach.

The *restructuring* strategy identifies underperforming firms. The center changes their management team, shifts strategy, or provides them with new technology. It may build a critical mass by acquiring companies in a similar industry. The center may sell off a business unit when it cannot add further value. The restructuring can be carried out on a PIF approach to adjust the newly acquired firm to the PIF. While on a PA approach, the restructuring is always focused on increasing profit levels.

Table 2.2 Porter's corporate strategies and PIF and PA approaches

	PIF	PA
Portfolio strategy	* Company identification is based on proto-image * Loose financial control	* Company identification is profit-based * Strict financial control
Restructuring	Can be accomplished to adjust the new acquired firm to the PIF	Efforts aimed to increase the profit levels
Transferring skills	It is more accurate on a PIF model	When profit levers are similar among businesses
Sharing activities	* Strong feeling of corporate identity * A clear mission that pinpoints the importance of integration among business units	* Financial incentives that prime cooperation among businesses * Multifunctional and multibusiness working groups

Transferring skills strategy consists of creating value through company relationships with each autonomous business unit. The center exploits synergies among them, such as similar buyers, channels, or value activities. This value creation can be one-time or ongoing. On a PIF approach, this skill transfer is almost guaranteed as investment decisions are based on a proto-image which looks for commonalities among businesses. On a PA approach, skills transfer is sought when profit levers are similar among business units.

The strategy based on *sharing activities* in the value chains is supported, for example, by a common physical distribution system and sales force. Sharing can help to lower cost or raise differentiation. On a PIF model, this strategy can be better implemented through a strong feeling of corporate identity. The sharing of the values of members of a firm guided by a PIF CEO is a mechanism to help sharing of activities among different business units. Moreover, on a PIF approach, a clear mission pinpointing the importance of integration of activities among different business units also contributes to this strategy's success.

Mechanisms used on a PA approach to secure the sharing of activities are different. Two of these mechanisms are financial incentives among business units, and prime co-operation and establishment of multifunctional and multibusiness working groups.

4.2 Ashridge Study

The second study, as mentioned, is that conducted by Ashridge Strategic Management Centre's Michael Goold and Andrew Campbell (1987b). They researched 16 UK firms regarded as successful, state-of-the-art organizations in quest of the role of the corporate center regarding how it created or subtracted value. They identified the center's roles as being (1) planning and allocating resources; (2) controlling and auditing performance, and (3) providing corporate services. The last of these three roles was discarded due to difficulties in outsourcing.

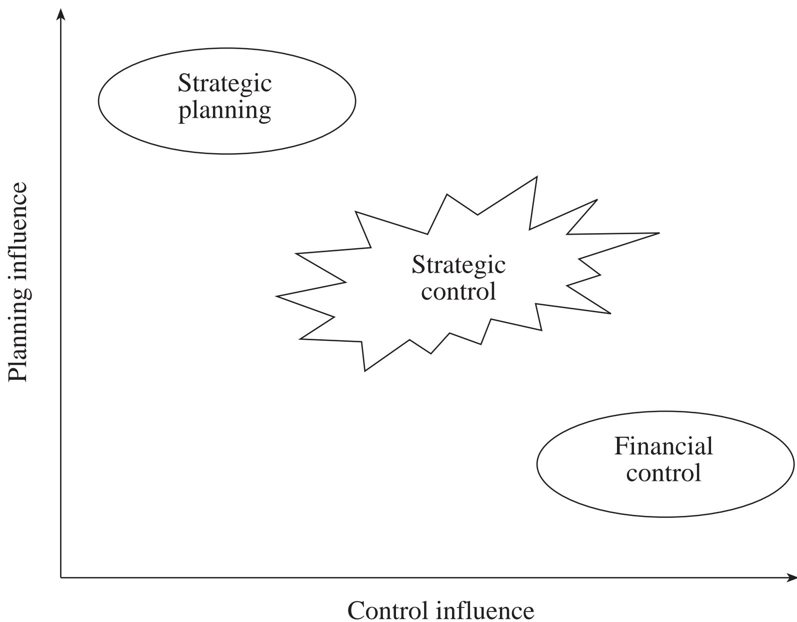
By combining planning and controlling dimensions the center provides different value creation levels. Goold and Campbell identified several *strategic management or parenting styles* by using these dimensions. For each different strategic management style the center contributes to value creation. This process was named parenting (Campbell and Goold, 1998; Campbell, Goold and Alexander, 1995; Goold and Campbell, 1998, 2000, 2002; Goold, Campbell, and Alexander, 1994a, 1994b; Goold, Campbell and Luchs, 1993; Goold and Luchs, 1996). The corporate-level advantage derived from parenting is called parenting advantage or corporate advantage (Collis and Montgomery, 1997, 1998). Corporate advantage is to corporate strategy what competitive advantage is to competitive strategy. Accordingly, strategic

management styles have come to be known as parenting styles too. As to positioning of different strategic management styles in the dimensions, see Figure 2.6.

Three styles – namely, strategic planning, strategic control, and financial control – were found to be most common. Characteristics of each of these styles are shown in Figure 2.6. There are two basic styles and a third one (strategic control) is a hybrid of the other two (strategic planning and financial control).

Strategic planning: the center works with business unit managers to develop strategy. It establishes extensive planning processes, makes contributions of substance to strategic thinking, and may have a corporate strategy or mission guiding and co-ordinating developments across business units. Less attention is given to the control process, with performance targets being set in broader, more strategic terms. Furthermore annual financial targets are seen as being less important than longer-term strategic objectives.

Strategic control: the center prefers to leave the initiative in plan development to business-unit managers. The center reviews and criticizes plans, but uses the reviews to check the quality of business-unit manager thinking, rather than as an opportunity to give direction. This means the



Source: Adapted from Goold and Campbell (1987b, p. 36)

Figure 2.6 Strategic management styles

control process is an important influence mechanism for the center. Targets are set for strategic objectives such as market share, as well as for financial performance, and managers are expected to meet the targets. On the other hand, financial targets can only be missed when important strategic objectives are at stake. Strategic control companies combine moderate planning influence with tight strategic controls.

Financial control: the center's influence is exercised mainly through the budget process. Corporate management's role in developing strategies is limited, and long-term plans are not formally reviewed by the center. Instead, the center focuses on a close review of the annual budget. Profit targets are set when the budget is approved, and careers are at stake if budgets are missed. Financial control companies combine a low level of planning influence with tight financial controls.

Table 2.3 compares our two models with the Ashridge framework. Although some assumptions are different, as are some key variables among the two frameworks, some comparison can be made.

The assumptions on which our frame is based are that leadership is the lynchpin of organizations. Whether a firm is doing well or not depends on whether it can count on a unique business leader with a clear vision and who sets direction to staff.

Ashridge's frame assumes different strategic management styles are a consequence of diverging basic conflicts or tensions in organizations. These inherent tensions force business leaders into choosing from among different trade-offs responsible for each style's strengths and weaknesses.

Key variables addressed in our frame are business domain and time-frame in which business decisions are taken. The PIF approach is more inclined to domain selection (Bourgeois, 1980). New product development, new business exploitation, fostering of new core competences, etc., are its main concern. PA is in this sense more centered on domain navigation; in terms of time-frame PA centers more on a shorter term than PIF.

Comparing the two basic management styles described by Goold and Campbell (1987a) and our two management approaches on the two key variables which define them, we can see the difference between them (see Figure 2.7).

The key variables in the Ashridge frame are control and planning influence. Flexible strategic control, tight strategic control, and tight financial control define the three main strategic management styles.

Comparing both frameworks, we can state that the PIF approach is similar to strategic planning in the sense that the PIF of the CEO at the corporation is used as a base for strategy formation at the business level. However, both styles – PIF and strategic planning – differ in their business domain, with the former being wider. Strategic planning management style should be applied on

Table 2.3 PIF and PA frameworks vs Ashridge framework

	PIF/PA approach framework	Ashridge framework
Assumptions	Business leaders motivational or mental scheme	• Personal motivation structure (autonomy versus intervention from the center) – balancing of tensions • Consonant remuneration/ compensation
Environment	Organizations and systems contingent on business environment (fast-growing, mature, etc.)	Organizations and systems contingent on business environment (fast-growing, mature, etc.)
Key variables	Business domain Time-frame	Control and planning
Focus	Business leaders	Corporate-wide, systemic co-ordination

a narrow scope of business with strong relationships, while the PIF approach tends to extend the portfolio seeking for new competences.

In the same way, we can assimilate a PA approach to the financial control strategic style. Both focus on the short term and in both cases financial analysis and budget procedures are essential. However, both differ in their business domain. Financial control tends to be adequate for multiple businesses in different industries and with low relationships among them. A PA approach, on the other hand, has a propensity to stay within the existing portfolio or in a reduced number of businesses with similar profit levers.

This focus differentiates our and the Ashridge frames. As explained in 'Assumptions' in Table 2.3, we emphasize the business leader, where Ashridge pursues more corporate-wide, systemic arrangements between the center and lower management in terms of planning and budget systems, remunerations, enforcement, etc.

5. LEADERSHIP AND THE TWO BUSINESS APPROACHES

The challenge of developing a clear strategy or re-establishing one depends on

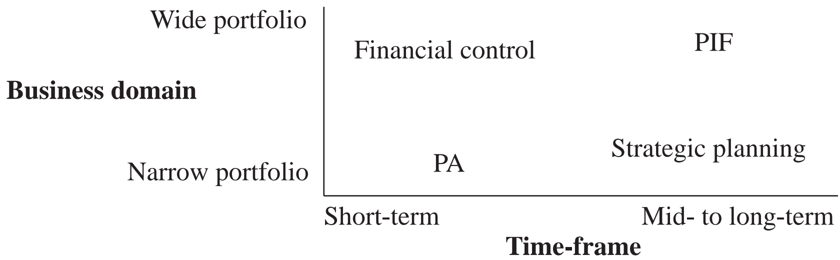


Figure 2.7 Ashridge's management styles and PIF and PA approaches

leadership and a clear intellectual framework is needed to guide strategy (Porter, 1996). Leadership goes beyond efficiency when it sets the organization's basic mission and when it creates a social organism capable of fulfilling that mission (Selznick, 1957). The four CEOs analysed are clear examples of business leaders who think strategically. Leadership is essential to our framework, because the role of a leader is to define and communicate the firm's unique position and forge fit among activities. It involves the continual search for ways to improve, extend and reinforce the firm's position.

Strategic fit among different activities is fundamental to competitive advantage and to the sustainability of that advantage. It is relatively easy to replicate a product feature or to copy a process technology, however, it is harder to match a bundle of interlocked activities. Strategic positions that are built on systems of activities are more sustainable than those built on individual ones (Porter, 1996).

The role of CEOs involves making positioning choices. These decisions imply which activities a company will perform and how they will be configured, and, more importantly, how activities relate to one another. Porter (1996) describes three types of fit:

- first-order fit: a simple consistency among different activities and the firm's overall strategy
- second-order fit: occurs when activities are reinforcing
- third-order fit: optimization of effort.

According to Porter (1996) co-ordination and information exchange across activities to eliminate redundancy and minimize wasted effort are the most basic types of effort optimization. The role played by business leaders in this task is key.

CEOs can use their PIF as a framework to secure fit among activities. Moreover, if the PIF is correctly defined, an investment decision will seek third-order fit – optimization of effort. The way this match is intended to rely

on the CEO's PIF, is what makes it extremely difficult to imitate or copy from outside the company. Even if rivals are able to identify relevant interconnections among activities, guessing the PIF, they will have difficulty replicating it.

A PA approach does not, *a priori*, seek fit among activities as it is not based on an image that should be accomplished. However, third-order activity fit can be achieved indirectly. PA managers always seek cost-reduction activities and make investments trying to increase profit levels. This decision making is based on analysis as well as on the CEO's previous experience and knowledge. The profit-arithmetic approach, if correctly developed, will deeply analyse investment decisions considering the entire system of activities – the company as a whole – and will seek co-ordination, elimination of redundancies and minimization of wasted effort.

Therefore, both approaches developed by our outstanding business leaders provide the right decisions for strategic fit among activities, creating competitive advantage and superior profitability.

Leadership is pursued through a PIF approach by insulating the manager's proto-image through the firm's business culture and shared beliefs and influencing employees' PIF. On a PA approach, leadership is gained due to rapid results of decisions made by the CEO. Their short-term orientation and quick improvements in financial statements will make them trustable. Their industry knowledge and business sense will be appreciated by employees who will respect them.

6. ENTREPRENEURSHIP AND THE TWO BUSINESS APPROACHES

The two business approaches briefly explained before are not limited to large companies' CEOs. These models are also applicable to small-business managers and entrepreneurs as we will explain.

An entrepreneur's decision to start a new venture can flow from unemployment, business opportunity identification, development of an invention, a desire to be one's own boss, etc. (Cooper and Art, 1995; Naffziger, Hornsby and Kuratko, 1994; Robichaud, McGraw and Roger, 2001).

A PA entrepreneur usually starts a business due to its potential profit-making opportunity. This can be identified through deep analysis and is translated into a business plan. The entrepreneur's previous industry experience allows them to have a feel about whether the business project will be successful or it may be the result of a hunch about a business opportunity. It would depend on the factors computed into the PA mental model – knowledge, experience or sense for business. In any case, the

venture's profitability will be the main decision criterion for a PA entrepreneur.

This kind of entrepreneur, if their business falters, would probably quit and start another venture. As the main motivation for the venture is not present anymore, there is no necessity to stay. Profitability will be sought after at another venue. Thus PA entrepreneurs tend to start several business ventures within their professional life.

PIF entrepreneurs meanwhile create their company in search of an idea or 'dream'. This kind of entrepreneur is more stuck on the idea of their firm/business. Hence, when a PIF entrepreneur creates a company, they tend to stay with it even when things are going badly. PIF entrepreneurs are more committed to their venture and, if successful, they stay with it to the end. If unsuccessful, or if profit expectations are not achieved, PIF entrepreneurs will do their best to keep their business alive. This means the psychological exit barriers are greater for a PIF entrepreneur than a PA one.

7. THE TWO BUSINESS APPROACHES AND NIIHARA'S STUDY

Niihara's studies (2002a; 2002b; 2002c; 2002d) deal with Japanese companies which achieved remarkable results even under poor economic conditions. From our four case samples Yamato is included. Defining 'superior' companies in terms of profitability, security, and growth, Niihara (2002c) listed several points common to these companies in Japan:

- top management has an unambiguous understanding of the scope of business in which the company is engaged
- top management is logical
- many members of top management seem to have spent some time on an offshoot during their careers
- top managers are capable of turning crises into chances
- superior companies engage in investment and R&D within the scope of cash-flow management
- superior companies have discipline, and have corporate cultures that emphasize constant discipline among both company managers and employees. The simple belief is shared that the key to corporate governance is a sense of mission and not the system.

In this section we try to extend our findings to other contexts by comparing them with Niihara's companies.

7.1 An Unambiguous Understanding of the Scope of Business

According to Niihara (2002d), the CEOs of the companies he analysed have an unequivocal understanding of the scope of their business, they have a 'single concept' of the firm as a whole. This single concept or what we call 'proto-image of the firm' helps them not to conduct businesses they know they cannot understand. In other cases, this single concept of the firm as a whole lets the CEO apply their own profit-arithmetic to make a decision.

Mabuchi Motor, when asked by Braun, a German electric appliance manufacturer, to provide it with a new type of motors, suggested the Japanese firm would rather stick to its core product – namely, small (200-watt or less) consumer-oriented steel-core DC magnetic motors with brushes. These are used for toys, household appliances, audio equipment, and automotive equipment. Somehow, there is a PIF that guides decision making at Mabuchi.

In Shimano's case, this abstraction reaches a higher level. The firm, a manufacturer of bicycle parts, views its essence in terms of production technology rather than products *per se*. Advanced metal-processing technology, namely, cold-forged manufacturing technology enabling metal to be treated at room temperature, is used to produce the utmost in performance. This is another example of PIF.

Kao, household goods manufacturer, managed to imbue its employees with its proto-image of the firm – PIF. Its products include hair-care goods, laundry detergent, paper nappies or diapers, etc. They share something in common such as the distribution channel and are narrow in scope, which helps their staff understand each other's business. Because of this narrow scope, T. Goto, its president, can hold discussion with all the company's divisions since the product concept is very clear for him. Employees understand, on their part, what is expected of them. They know that Kao is a firm 'dissatisfied with its status quo'. Here the PIF is a driving force behind employees' behavior.

Faced with opposition from inside and outside his company, Toshifumi Suzuki, chairman of Seven-Eleven Japan, when trying to reach an agreement in 1973 with Southland Company, owner of the US Seven-Eleven, used the argument that productivity, not economies of scale was the factor behind the success of Japanese electric equipment manufacturers against giant US and European companies. If this was so, said Suzuki in his exposition, convenience stores would successfully compete against supermarket chains. Suzuki based his business judgment on his understanding of profit levers or arithmetic. This is a clear example of the PA approach.

7.2 Offshoot Experience

Accepted wisdom, unquestioned assumptions in the theory of the firm

(Drucker, 1994), etc., are dangerous. They might lead to doing business by rote. Seven-Eleven's Suzuki, as cited by Niihara (2002c, p. 4) cautions:

> Observing other companies in the same industry and reading books will lead to failure as one ends up imitating someone else. Human beings often get caught up in their own experiences and examples of success … they tend to extract only the positive aspects … .

Niihara (2002c) conjectures that 'offshoot' or outsider experience gives the opportunity to examine the firm objectively from outside, and to find inefficiencies unnoticed by the people inside.

As already mentioned previously, the CEO's personal and professional background is an important factor in PIF and PA configuration. In a PIF approach, the offshoot experience lets the manager see the firm from outside, helping them to develop their own PIF free from internal routines and commonly accepted and hackneyed ideas.

In a PA approach, the mental model is configured through the experience gathered from different firms and industries which, together with the right information and knowledge, let the CEO know what the profit levers are and how to pull them.

7.3 Investment within the Generated Cash Flow

Financial discipline is observed among superior companies. They pursue autonomy not bound by the capital market. Ultimately this leads to risk management (Niihara, 2002d).

This way of thinking is typically reflected in Canon's Mitarai. Upon taking charge of the presidency Fujio Mitarai estimated the total investment amount at ¥130 billion and depreciation at ¥80 billion. Canon needed, Mitarai reasoned, ¥50 billion net profit to cope with investment needs. This net profit amount was considered to be equivalent to ¥100 billion in ordinary profit, a figure he decided to target.

Nintendo's Yamauchi, the former president, believed strongly that his company should hoard abundant ready cash because the game software business was risky – needing a long lead time before investments were repaid since software was developed not against an order but based on a forecast, then produced and kept as inventory based on projected demand. Yamauchi cited Atari, which shocked the industry in the 1980s. The US firm went bankrupt after a sudden market downturn, which shrank 90 per cent in one year. For Yamauchi it was essential to keep sufficient liquidity on hand.

These two examples further illustrate the PA approach which guides CEOs in setting a feasible goal (Canon's case) or preparing them for a sudden change in the market (Nintendo's case). Its basic principles are simple and easy to

understand. Complicated realities are reduced to a simple cause–effect relation.

7.4 Sense of Mission and Adherence to the Business which CEOs can Understand

The proto-image of the firm can lead to a sense of mission (Campbell et al, 1990), if its ethical aspect develops. On the other hand sharing a strong sense of mission certainly strengthens the existing image or concept of the firm among its employees and management.

Niihara (2002d) supports the linkage between a sense of social mission and excellence in the economic and financial achievement of a firm. It understands profit seeking does not justify all its acts, profit instead is viewed in a long time-frame. Short-term profit maximization may lead to debacles such as Enron and WorldCom.

The secret to successful corporate governance lies in the sense of mission not in a given system (Niihara, 2002c). The sharing of a sense of mission among employees helps to avoid their falling away from a firm even during a crisis. This sense of mission motivates staff and generates a belief that their work at their firm contributes to improvement of the society in which they live.

Niihara (2002d) reports Yamato Transport's Ogura distributed *dorayaki*, a sweet popular in Japan, among his staff every time the firm's sales hit a record. The monetary significance was far less than stock options would have been, but as a motivator it was stronger than stock options.

The proto-image of the firm also helps firms decide whether a course of action fits the firm or not.[6] In a complicated situation this is a strong drive for CEOs to reduce it to a simple relation of one or two variables.

Niihara's findings and the two approaches identified in our study are compared in Table 2.4. As it can be seen, both approaches accomplish Niihara's findings.

Both kinds of mental model give an unambiguous understanding of the scope of the business, one is based on image of the firm – PIF – and the other on knowledge of the profit levers – PA. Both approaches to business imply a logic and strategic thinking. PIF and PA managers think about things long and hard themselves. However, both models benefit from an offshoot experience and both models can be used to turn crises into chances.

Moreover, financial discipline is strongly observed in a PA approach. And shared beliefs among firm's members are a sign of a correctly applied PIF approach.

In the next two chapters we will explain each of the two managerial approaches presented in this chapter. Chapter 3 deals with the proto-image of

Table 2.4 Comparison of Niihara's findings and PIF and PA approaches

Niihara's findings	PA	PIF
Scope of business understood	Yes	Yes
Logical thinking	Yes	Yes
Offshoot experience	Yes	Yes
Crises into chances	Yes	Yes
Cash-flow and R&D	Yes	?
Belief shared	?	Very much so

the firm approach while Chapter 4 examines the profit-arithmetic approach to business.

NOTES

1. When Sony's Ohga had to find his successor as Sony's president, his selection criterion was not the past achievement. For him it was more important to find somebody who could guide Sony toward the next century. Ohga's criterion was more deeply set in Sony's corporate image than values, mission, or vision. See the case study.
2. Daft and Weick (1984) argue that the interpretation of the environment is done by strategic-level managers. They cite the observation recorded by Aguilar (1967) in the sense that 'below the vice president level, participants are not informed on issues pertaining to the organisations as a whole.'
3. 'Values are integral to companies' sense of who they are, what they represent, what they want to achieve, and how they intend to achieve it' (Grant, 2002). The approach taken depends on values.
4. 'Sony is not afraid of change. Change is its hobby. Our culture appreciates it' (Hashimoto, 1998, p. 302) [translated by the authors].
5. Currently the common understanding is that 'generic strategies' (namely, a reduced set of strategic patterns applicable to any industrial situation) at the level of corporate strategy do not exist as they do at competitive strategy level (Collis and Montgomery, 1997).
6. In a conversation with a Sony staff member one of the authors heard the reference to '*rashisa*', appropriateness. When a decision is to be taken, Sony people are concerned whether it will be appropriate to Sony. This *rashisa* concept presupposes that among them there is a primal concept or image of how Sony is and should be.

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3. Proto-image of the firm approach to business

1. INTRODUCTION

In the preceding chapter we discussed two different approaches to business observed among successful firms in Japan, namely, the Proto-Image of the firm (PIF) and Profit-Arithmetic approaches (PA). In this chapter we will focus on the proto-image approach by examining how it is created, how it influences launching new products and diversification decisions and even how it affects the succession process. We will explain how a PIF guides managerial decisions to cope with change in its environment.

In this chapter we aim at illustrating how (1) Sony renewed itself by launching new products and entering new activities. We claim the PIF approach was an important driver of Sony's strategy since it enabled the firm to concentrate on products and activities it could cope with; (2) Sony's leaders directed the renewal process through a review of their theory of the business. That is, how new products and new activities gave a chance to Sony's management and staff to re-examine assumptions on which their theory of the business was founded.

Before we do that, we will explain how a PIF, as a cognitive structure, is created in the mind of a leader. In doing so, we will analyse Masao Ogura's professional life to see the facts which helped him to build his proto-image of Yamato. Moreover, we will describe Sony's founders' vision of his firm and how this vision influenced Ohga's PIF.

We believe that a PIF-type CEO has a clear image of what their firm is and where they want it to be and that this image guides every managerial decision. In this chapter, apart from studying how Ohga's PIF influenced Sony's diversification decisions and its product evolution, we will show how succession decisions of a PIF-type CEO are strongly based on their PIF.

We will finally end up the chapter by analysing managerial styles and roles in the PIF approach to business.

2. THE ORIGIN AND SHAPING OF A PIF

Several factors contribute to the development and shaping of a proto-image of

a firm. First, the CEO's personal and professional background clearly influences their vision of the firm. Previous experience in other companies, in other industries or in other departments will help interpret what the firm is or what it should be according to their personal judgment.

Secondly, organizational culture strongly influences the way a PIF is developed and shaped. The founder's PIF guides formation of a firm's culture and ideology in their organization and this proto-image permeates to other members' cognitive structure. In this section we will explain this process showing Sony's founders' PIF and how it influenced Ohga's vision of his firm.

A PIF is also strongly influenced by the environment. In this section we will also explore Yamato's Ogura's PIF analysing how his professional experience and the environment shaped his vision of the company he manages.

2.1 Sony Founders' Idea and Ohga's PIF

In October 1945 Masaru Ibuka and his friends set up a business which would develop into a firm known later as Sony (Kase, 2002).

Ibuka's business repaired radios and made short-wave converters or adapters to help convert medium-wave radios into super heterodyne or all-wave receivers. The demand for these devices was so high that a newspaper published a report on it. Akio Morita, who was to become Sony's president later on, read it, got in touch with Ibuka, and ultimately joined the business (Morita, Reingold and Shimomura, 1986).

On 9 May 1946 the business was incorporated as Tokyo Tsushin Kogyo, Sony's predecessor with an initial capital of ¥190 000.

In what follows, we posit that PIF is a cognitive structure residing in the leader but which permeates a company's belief system and underlies its core values and core ideology. Table 3.1 provides a few elements of the founders' prospectus which formed the base for Sony's 'essential and enduring tenets' – core values, and marked Sony's 'character as an organisation, namely, its consistent identity' – core ideology (Collins and Porras, 1996) and reflect part of this cognitive structure.

Ibuka emphasised in the prospectus that the firm's purpose was to serve as an ideal factory for engineers to exercise their technological skills to the highest level (Sony Corporation, 2003).

Their objective was not to imitate competitors' products. A fierce pioneer spirit can be seen in this prospectus. In essence it expresses:

- the pursuit of uniqueness
- the avoidance of imitation
- the acceptance of technological and commercial challenges
- ferocious independence of mind

Table 3.1 Sony founders' prospectus

Purpose of Incorporation	Management Policies
To establish an ideal factory that stresses a spirit of freedom and open-mindedness, and where engineers with sincere motivation can exercise their technological skills to the highest level	We shall eliminate any unfair profit-seeking practices, constantly emphasize activities of real substance and seek expansion not only for the sake of size
To reconstruct Japan and to elevate the nation's culture through dynamic technological and manufacturing activities	We shall be as selective as possible in our products and will even welcome technological challenges. We shall focus on highly sophisticated technical products that have great usefulness in society, regardless of the quantity involved. Moreover, we shall avoid any formal demarcation between electronics and mechanics, and shall create our own unique products uniting the two fields, with a determination that other companies cannot overtake
To promptly apply highly advanced technologies which were developed in various sectors during the war to common households	We shall carefully select employees, and our firm shall be comprised of a minimal number of employees. We shall avoid to have formal positions for the mere sake of having them, and shall place emphasis on a personís ability, performance and character, so that each individual can fully exercise his or her abilities and skills

- not one of the mass.[1]

Akio Morita reminisced about this spirit years later:

> Sony is a pioneer and never intends to follow others.[2] Through progress, Sony wants to serve the whole world. It shall be always a seeker of the unknown … Sony has a principle of respecting and encouraging one's ability … and always tries to bring out the best in a person. This is the vital force of Sony. (Morita, Reingold and Shimomura, 1986, p.58)

Morio (1998, p. 70) evaluates this Sony's PIF in the following terms:

> [We] may say that it was Sony that created the audio video industry. Tape recorder, CD, transistor radio, home-use video, etc., were developed by Sony … Why do we insist on developing products that fit Sony's image (*Sony-rashii shohin*)? It's because the values Ibuka and Morita instilled at Sony's inception are still vividly shared among the firm's staff.[3] The moment you start to imitate competitors, you will have lost Sony's spirit… .[4]

This is what Sony's founders had in mind and this image of their firm deeply influenced Ohga's PIF. In order to describe his PIF we will use Nathan's (1999, pp. 142–3) account of Ohga's view of Sony:

> Sony must always be extraordinary. Mr. Ibuka and Mr. Morita were extraordinary people. They were a pair of geniuses. I did my part to grow Sony in their footsteps, and I always asked myself what was essential to the company. Recently, I find myself thinking about the Chinese character '*san*', which means to shine dazzlingly like the sun – *san-san to kagayaku*. It's not simply a matter of brightness. '*San*' means an extraordinary radiance. Ever since I became involved with the company, I've worked hard to ensure that Sony would shine with that blinding light. It's been my main focus and my theme.

For Ohga, Sony represents something shining to dazzle the people. He worked hard to keep up this image which we call the proto-image of the firm (PIF) for himself and for his staff. This PIF is a logical extension of the founder's idea with even more emphasis on the uniqueness and 'aloofness'.

2.2 Masao Ogura's Haulage Revolution

In this subsection we will review Masao Ogura's professional life and the environmental facts that contributed to the development of his PIF at Yamato Transport.

Japanese haulage has experienced a sea-change over the last 30 years. Yamato Transport's home delivery service known as the *Takkyubin* service played a vital role. This haulage revolution was brought about as a brain-child of Masao Ogura, the president of Yamato between 1971 and 1987.

Masao Ogura was born in 1924. Ogura's father, Yasuomi, founded in 1919 what was to become Yamato Transport. In September 1948 Ogura joined Yamato Transport and was assigned to the general affairs department.

In 1956 Ogura was put in charge of transport for department stores. This was a period when labour unions staged several strikes. In May 1957 Ogura signed a transport contract with Sogo's Yurakucho branch in Tokyo. He wanted an exclusive relationship, since Yamato had monopolized cargo handling for Mitsukoshi before World War II.

In the 1960s annual revenue amounted to ¥3 300 million with operational

profit of 3.1 per cent. Problems largely consisted of regular truck transportation not breaking even.

In March 1971 Ogura was appointed the firm's second president.[5] Two years later the first energy crisis occurred. Concentration on large-lot haulage impacted the firm's performance negatively. In 1974 cargoes fell by 25 per cent compared with the previous year.

Ogura asked labour unions to accept a pay cut in exchange for a promise of maintaining employment. Directors' executive compensation was also cut. Ogura even commuted to work by train. Between 1973 and 1975, of 6500 employees, 1000 were laid off – see the case study in the Annex.

The large-lot haulage operations were kept, because Ogura thought his competitors were doing the same. While traveling to Osaka he found out one competitor actually handled lots with less than ten items. He knew at Yamato less than 10 per cent of its invoices included lots with less than ten items. On average Yamato's invoice covered lots with over 50 items. He realised loading trucks just with large-lot cargoes without including small-lot cargoes had contributed to the company's poor performance.

In 1975 the return on sales was as low as 0.7 per cent. Drastic measures were needed or the company would risk going out of business.

Ogura repeatedly asked himself what characterised the best haulier for customers. The answer he got was: a company which would transport any quantity to anywhere in Japan. However, he observed the Yoshinoya chain which specialized in beef-meat served with rice increased its profit when it decided to focus on one menu item and exclude all others. Ogura realized it was a non-starter to try to become the ideal haulier. They could only offer a focused service.

The second hint suggested itself when his family planned to send old clothes to relatives in Chiba prefecture. It so happened that hauliers only handled cargoes from corporate customers. There was no way for Ogura, even as president of Yamato, to send the items to their destination.

How would these hints translate into the haulage business? First of all, the focus must become housewives who would buy door-to-door delivery services, a segment largely ignored until then. The typical haulier customer was male. If housewives were to be targeted service content needed to be simple and clear. Regional tariffs should be uniform, with no need to pack, next-day delivery, parcel reception and delivery to anywhere in Japan, etc., should be offered.

One difficulty was that corporate customers can guarantee steady cargo flow on specific routes. Household demand seemed random and sporadic. There was no way to know where parcels would be collected or delivered. Every order would include just one parcel.

Ogura however tried to visualize from a bird's-eye view the flow of cargoes

between Tokyo and Osaka or Nagoya. Individual parcels might reach you randomly but overall there should be a flow.

He advanced the ‘density’ concept to explain cargo profitability. This emphasized dilution of fixed and indirect costs through the volume of cargoes handled in a given square kilometre. It helped to understand haulage operations could make a loss at the beginning due to low cargo density but as density increased, operations would break even.

Ogura was not 100 per cent sure of the success of the new business. But it was also clear Yamato could not enjoy any competitive edge in commercial haulage for corporate customers. Yamato was an underdog. Its only strategy for survival was to break new ground in a new business.

The distribution network was designed after airlines’ hub-and-spoke system. In every prefecture the airport was considered to be the hub to be provided with a distribution centre and depot. From there parcels would pass through three stages before their final destination.

Yamato’s office network would not be sufficient to attend to household demand. Liquor shops were chosen as Yamato’s agents.[6] Due to the monopolistic handling of liquor sales for tax reasons, liquor shops were present in every town in Japan.

As scheduled, in January 1976 the *Takkyubin* (home delivery) service was inaugurated. To start with, the Kanto area, namely Tokyo and its surrounding prefectures, was covered with a next-day delivery service.

The first month saw only 9000 parcel deliveries. Ogura was scared but emphasized the importance of service quality. His motto then was ‘first the service, then the profit’.

For him drivers were the primary force. So drivers were called sales drivers (SD). To help SDs a special vehicle called a walk-through vehicle was designed and manufactured by Toyota (Yanagihara, 1997).

The *Takkyubin* service’s reputation spread like wildfire by word of mouth. Drivers were initially not keen to collect money, deliver parcels, etc., which they thought was not their task. But the thank-you from customers and their warm reception gradually changed their opinion.

Over 1.7 million parcels were being handled by fiscal year 1976 (April 1976 to March 1977) – see the case study.

Positive aspects of *Takkyubin* became clear: (1) housewives did not try to negotiate the tariff, unlike corporate customers, and (2) freight was paid in cash, which gave a breathing space to Yamato’s treasury, since corporate customers only paid by bills of exchange.

Yamato Transport withdrew in November 1978 from the haulage business for Mitsukoshi department stores in the light of unreasonable requirements from Mitsukoshi’s new president, Okada.

The Mitsukoshi incident psychologically marked the departure from the old

Yamato days to the *Takkyubin* era. In 1979, Yamato further rescinded the contract with large-lot haulage customers. Ogura's judgement was that Yamato could not pursue two lines of business: large-lot haulage and *Takkyubin* business.

Dropping the large-lot haulage resulted in a loss in the financial year 1979. However, *Takkyubin* business grew exponentially, reaching 33.4 million parcels handled in the financial year 1980, equivalent to cargoes handled by the National Railway. The return on sales topped 5 per cent as ordinary profit more than trebled compared to the preceding year. After five years the *Takkyubin* finally broke even.

Takkyubin delivery involves things such as golfbags and clubs and skis. In the case of golf bags Yamato got them six or five days before the game. These items were expected to arrive at their destination a day before play. The haulage of suitcases for overseas travellers when traveling inland in Japan was also an important service. The *shinkansen* – bullet trains – do not have space to accommodate suitcases.

In 1988 Yamato inaugurated the Cool *Takkyubin* for the haulage of chilled cargoes. Its technological development and investment in premises cost Yamato ¥15 billion. The training of employees was also very important but nowadays it is one of the main service menu items at Yamato. However, that year turnover reached ¥300 billion with ordinary profit of ¥10 billion.

This is an example of how a leader builds his PIF, how past experience and environment shape it and how it influences their managerial decisions. Yamato dropped large-lot haulage and concentrated on the *Takkyubin* business due to Ogura's image of his firm.

In the next section we will examine how a PIF guides product and diversification decisions as we have already seen at Yamato. We will analyse Sony's product evolution in the period when Nohrio Ohga was at Sony to explain our view.

3. PIF APPROACH, PRODUCT EVOLUTION AND DIVERSIFICATION DECISIONS: THE OHGA ERA AT SONY

Our thesis is based on the proto-image of the firm (PIF). Fostered and nurtured by its leaders a firm develops and evolves its product/market and its activities to become a world-class enterprise.

Conceptually this can be graphed as Figure 3.1. The proto-image of the firm is at the very center, guiding corporate renewal and diversification or contraction activities. Successful companies grow not only by diversifying but also by becoming smaller.

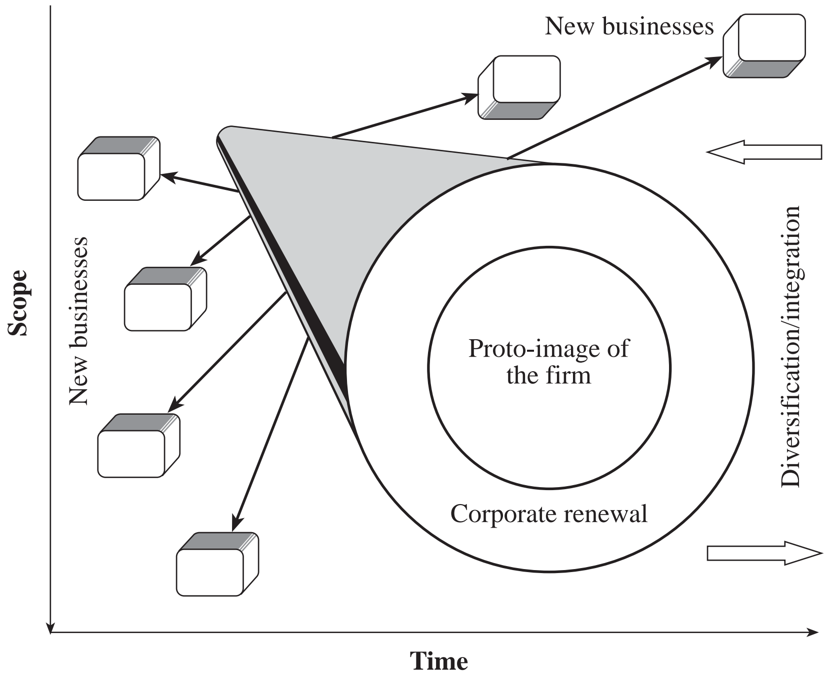


Figure 3.1 PIF and corporate renewal and diversification decisions

To exemplify that statement we review Sony's history during Ohga's leadership.

3.1 Proto-Image of Sony and its Product Evolution

Since its inception, Sony had been led by the founders, namely Ibuka and Morita. In the decades we refer to, for the first time Sony appointed professional managers without a large shareholding. Whether or not this change affected how they think and behave at Sony is an important issue.

Over these decades competition inside and outside Japan became fiercer as exemplified by the VCR format battle between Sony and JVC/Matsushita. The external general economic conditions such as the appreciation of the yen as a consequence of the Plaza Accord in 1985 and the bursting of Japan's bubble economy tried their leadership.

We posit that a firm with a strong PIF, shared in common among its staff and management, will reinforce the brand's importance since it symbolises the basic image of the firm or PIF.

Ohga was convinced that brand image was very important and defined the

brand as the common value of Sony.[7] So he personally changed the design of the firm's logo and set standard templates for different sizes of newspaper ads in which the position of Sony's logo, the catchphrase, etc., were clearly indicated.

Together with developing the company's brand image, Ohga also emphasized product development and planning.

He emphasised products should be worthy of the Sony logo or image, since they might or might not please their customers. If product design was unattractive, he would not allow the Sony logo to be used. The underlying belief was that attractive design and ease of maintenance were hallmarks of Sony's good industrial design.

Ohga attended almost all new product planning meetings in which new products launches were discussed until the beginning of the 1990s. He personally commented on product planning and their designs. He paid special attention to the usage of the Sony logo.[8]

Ohga always insisted Sony products must have a certain, extra something to win over customers (Ohga, 1998). He was concerned as Sony grew larger and its product range became more diverse, the firm might drift away from its philosophy of consistently developing high quality and innovative products.[9]

He was quoted as saying (Sony Corporation, 1996c):

> A consistent product philosophy is the basis of Sony's brand image. With it Sony can expand and globalise, while still maintaining consistency in design over the long-term. From the customers' point of view, there is only one Sony.

The importance of the proto-image of the firm is appreciated when Sony ranked first in terms of esteem, fourth in name recognition, and second in overall ranking amongst US, European, and Japanese firms in 1990 (see Table 3.2). Ohga was said to be particularly delighted (Sony Corporation, 1996c).

Some landmark events, and product development, as well as organisation structure changes are chronologically described in Table 3.3. It shows Sony's product development and evolution during Ohga's leadership at Sony.

Complementary to Table 3.3, we summarize in Table 3.4 several key issues and strategic initiatives during Ohga's steersmanship.

Before Ohga was appointed president, Sony was already one of the most admired firms not only in Japan but also throughout the world. It had already released such popular products as portable radio in 1955, the Trinitron line of television sets in 1968, the Betamax VCR in 1975, and the Walkman in 1979.

Nonetheless, in terms of operations and product line-up strategy Sony could not be said to be a world-class company, since it still relied heavily on single best-selling products such as VCRs.

Accordingly, by the time Ohga took charge of the presidency, some considered Sony's heyday was long past. The battle over the VCR format was

Table 3.2 Top global brands in the world

Image power	Brand	Share of mind	Esteem
1	Coca Cola/Coke	1	6
2	Sony	4	1
3	Mercedes-Benz	12	2
4	Kodak	5	9
5	Disney	8	5
6	Nestlé	7	14
7	Toyota	6	23
8	McDonalds	2	85
9	IBM	20	4
10	Pepsi Cola	3	92

Note: 'Share of mind' refers to the 'shelf space' or 'market share' occupied by a brand in the mind of a consumer among rival brands

Source: Based on www.sony.net/Fun/SH/1-35/h4.html

being lost. In addition, excessive inventories were causing serious financial problems.

In considering the variety of challenges he faced, Ohga must have realised Sony was still a firm in need of more sophistication in terms of operations and strategy. Under such circumstances Ohga had little choice but to seek a way out by developing new businesses and improving management.

Thus, Ohga attempted to outgrow VCR-dependence to become a truly multi-business company. His intention was to rise to a host of challenges to diversify into new products and businesses and to adopt a new organisational system to meet such challenges.

3.2 Corporate Renewal through Diversification at Sony

Drucker (1994, p. 96) argues that the theory of the business is based on the 'assumptions on which the organization has been built and run.' These assumptions are influenced by the environment and capabilities and resources the firm has at its disposal.

In this subsection we review the environment of Ohga's period and how he responded to it through corporate renewal decisions.

The theory of business held prevalent at one time by a leader may become obsolete. Only leaders who continually review their theories can ensure their companies survive. In Sony's case, Ohga's PIF allowed him to review the

Table 3.3 Sony: chronology of Ohga era

Year	New product	Organisation	Businesses initiated	Remarks
1982	*CD player, *Professional VCR 'Betacam', 'Microcomputer SMC series'		Computer	Ohga: COO
1983	*Personal computer 'Hit Bit' Word processor 'Series 35' (Japan)	'Business Unit system'	OEM	
1985	Single-unit 8mm video camera			
1986		Established a battery development subsidiary		
1987	*Digital Audio Tape (DAT) deck, *Workstation 'NEWS'		Workstation	
1988	Electronic still-image camera 'Mavica'	Acquisition of CBS Records		
1989	Hi8 video camcorder CCD-TR 55	Acquisition of Columbia Pictures Entertainment	Films	Ohga: CEO
1990	Colour HDTV 'HD Trinitron'			
1992	Mini Disc (MD)			
1993	Broadcast-use 'Digital Betacam'			
1994	Consumer game 'PlayStation'	'Divisional company system'	Game business	

Source: Based on Sony Corporation (1996a–1996d)

Table 3.4 Sony: activities during Ohga era

Key issues	Strategic initiatives	Implementation
The battle over VCR format	Diversification Development of core components	Entering new business fields PC business OEM business New VCR format (8mm) Acquisitions of CBS Records and Columbia Pictures Strengthening of brand image
Dealing with digital audio technology	Alliance with key players	CD player MiniDisc system
Management of business units	Decentralisation	Business unit systemvarious Divisional company system

Source: Based on Sony Corporation (1996a–1996d)

prevalent theory of the business and reshape it to make Sony a multi-business firm. In order to permeate his proto-image of Sony as the shining firm which dazzles its consumers, Ohga carried out a corporate renewal needed for diversification.

In 1983, a year after his appointment as president, he set about implementing his strategy to consolidate Sony's existing businesses and carry out further diversification.

Vis-à-vis the severe business environment for its existing product at the beginning of the 1980s, Ohga saw it as vital that Sony should develop new businesses in various fields, not only for survival but also to achieve high growth. This diversification required fostering of new core competences (Prahalad and Hamel, 1990; Drucker, 1994).

New products and business ideas and plans were reviewed and discussed to see if they fitted the firm's image staff shared. In a personal communication with K. Kutsuwada, who used to belong to a sales department in Sony, he recalls that one of the key discussion for the launch of a new product was whether it fit Sony's image – Sony *rashisa*.

For the analysis of how Sony diversified and fostered new core competences, we will review some of its products including (1) 8mm VCR format; (2) digital audio products such as compact discs and mini discs; (3) game business, and (4) music and film businesses.

The new products/diversification and development of new core

Table 3.5 Environment and Sony's diversification

Environment	Diversification
Format battle over VCR	8mm VCR format
Digital audio technology	Digital audio products
	Music and film businesses
Games	Game business

competences were answers to the change in the environment. With the battle of the VCRs came development of 8 mm and OEM initiatives, and with development of new digital audio technology new product formats for music were introduced (see Table 3. 5).

3.2.1 8mm VCR format

As set out before, when Ohga became president, there was a smaller product range, though epoch-making products such as portable radio, Betamax VCR and Walkman were constantly released.

These products catered in a timely way to customers' demand, which increased as their income level grew, as did Japan's economy.

The life-cycle of existing products was being constantly replaced by other products. In the event a replacement had not emerged in a timely way, Sony would have had a hard time.

Financial performance clearly reflected such a dangerous phenomenon. While compound annual growth rate (CAGR) of Sony's sales in 1970s was 15.8 per cent, the CAGR from 1980 through 1982 was as low as 7.8 per cent due to lack of new businesses taking the place of old ones. This decrease in the number of new 'hits' led nay-sayers to predict the demise of Sony's growth.

What is worse, Sony failed to make its Beta VCR technology the industrial standard, in spite of having the fundamental technology know-how. This failure indicated that unless the Japanese firm came up with some solutions including new products and organisational renewal, it would not survive as a firm.

Sony officially announced, in New York and Tokyo in July 1980, the launch of the 'video movie', a single unit with the capabilities of a camera and recorder at the same time. This was the start of a new VCR format known as 8mm VCR. An important factor in this product's success was acceptance of the standard. There were two reasons which enabled the format to be accepted as a standard.

First, Sony had formed a group of products with the same format. In April 1984, as a result of the series of negotiations among manufacturers, a set of common standards was finally agreed. Sony released the 8mm VCR in alliance

with 127 companies world-wide, thanks to which over 30 per cent of the initial production was destined for business customers under OEM contracts.

The second reason is that Sony had a competitive edge thanks to the core component it had developed – namely, the charge coupled device (CCD) that substituted tubes for cameras.[10] It is a semiconductor which stores and transfers electric signals. Depending on the voltage applied, an electric signal is transferred in a CCD and the two ends of the CCD act as the entrance and exit for the signal. Sony thus managed to establish its new VCR format as a standard.

In 1989 Sony released CCD-TR55, the world's smallest and lightest video recording and playback unit. Its promotional catch phrase was 'the passport-sized video camera'. Young and old travelers, thanks to the strong yen, carried with them the new video camera, which advertised it gratis.

3.2.2 Digital audio products

During the Ohga era, two waves shook the audio field. The first wave started from the audio player. At Sony, development of digital technology began in the audio field in the 1970s.

Sony's engineers judged it more important to pay attention to recording efficiency than to audio sound quality. Digital recording offered the possibility of storing a large amount of sound. As digital technology developed, attention shifted to the ease of handling.

The desire for digitally recordable media generated the second wave. In the 1990s production volume of audio compact cassettes was fast declining from its peak of 76 million units in 1988.

Therefore Ohga felt the need to replace compact cassettes. Early in the 1980s he had led the establishment of the CD business. CD technology had quickly improved audio technology thanks to its digitally based, high-speed random access and direct search capability. Ohga thought it commercially interesting to make use of this capability to have some product which was rewritable – a kind of disc to replace the audio compact cassette.

Although Sony was developing technology quickly, the success of the compact disc (CD) business might not have been possible if Sony had entered it alone. It owes much to the joint programme with Philips,[11] the Dutch electrical appliance industry giant.

Philips had developed an original audio disc format known as audio long-playing (ALP) disc, whose technology was similar to the one being developed by Sony.

In virtue of the joint programme Philips and Sony released the first compact disc player and Ohga was convinced it would replace the LP record (Sony Corporation, 1996d).

Sony developed CD format in collaboration with Philips and a press

meeting was held in August 1982. Despite initial negative reaction from a record industry afraid of losing its LP sales business, the initiative enlisted the enthusiastic support of Herbert von Karajan, the Berlin Philharmonic Orchestra's conductor, which gave a big push to CD sales – see the case study in the annex.

The CD business success led to development of new digital recordable audio equipment, driven further by the decline in production of audio compact cassettes. The result was the announcement in May 1991 of the mini disc (MD), which was to become a new digital audio standard. To enhance its portability, the disc was housed in a shell.

MD combined the recordable features of a cassette tape and the random access function and high quality sound of a CD. The difference between CD and MD was that the former was to enjoy at home for leisure listening, whereas the latter was for enjoying music anywhere and anytime, much in the same vein as the Walkman.

The partnership was again a success factor for MD. At the time of its announcement Ohga emphasised the importance of calling upon hardware and software manufacturers to endorse the MD system and target the product launch (Sony Corporation, 1996a).

3.2.3 Game business

Ohga's diversification strategy was crowned with the revolutionary game business. This business perfectly embodied Sony's aim of 'dazzling the consumers with its products'.

Personnel from various units of the Sony Group, including broadcast products development staff and Sony Music Entertainment (Japan) Inc. (SMEJ) software staff, were brought together at Sony Computer Entertainment Inc. (SCE), to combine the hardware expertise at Sony and software know-how of SMEJ for development of the 32-bit PlayStation video game system.

With its CD-ROM-based[12] software and the processing power of a computer workstation, PlayStation was far from being a mere toy. The initial stock of 110000 units sold out on the first day of business, and the following six months recorded accumulated sales of over 1 million units.

Following this initial triumph in Japan, SCE launched the PlayStation in the US and Europe in autumn of 1995. By May 1996 the total number of PlayStation units sold world-wide exceeded 5 million. Even for Sony this was the first time a single model had sold in such large numbers in so short a period of time.

3.2.4 Music and film businesses

Two large acquisition operations realised by Sony during the Ohga era were: CBS Records and Columbia Pictures in 1988 and 1989, respectively. The

rationale behind these was that Morita and Ohga believed Sony needed to develop both audio-video hardware and software.[13] However, there are two versions concerning Sony's intention regarding the joint venture with CBS Records.

Nathan (1999, p. 210) describes it thus:

> Ohga had been longing for an opportunity to lose CBS as a partner in the record business. For eighteen years (after the establishment of CBS Records), as he grew CBS Records into the largest and most profitable subsidiary in the conglomerate, he had been fighting with CBS about retained earnings and dividends.

Nevertheless, according to Ohga's autobiography (Ohga, 2003), when Sony heard from a CBS executive in charge of the record division that CBS might be willing to sell its record division including the joint venture for $1300 million, it began the acquisition negotiations at the end of 1986. But to Sony's dismay Tisch beat up the price every time they met and finally proposed $2000 million at which Sony expressed its surprise, resulting in the breakup of the negotiations process.

Eight months later, namely, in October 1987, the US stock market suffered a reverse – 'Black Monday'. The despairing Tisch offered Sony the sale at $2 billion, an amount considered unprecedented in Japan's M&A history. Nobody except for Morita and Ohga was in favour of the resumption of the negotiations. Ibuka's stance was: you take the decision.

Ohga's analysis was that (1) the acquisition of CBS Records signified the obtaining of its world-wide network and plants and (2) the remaining 50 per cent of CBS Records stake would automatically become Sony's. Ohga had a clear picture of CBS Records' cash-flow position in Japan and knew that it was a buy. Thus, Sony acquired CBS Records in January 1988 (Ohga, 2003).

Be that as it may, CBS/Sony Records was established between Sony and CBS on a 50/50 basis. Ohga seemed to have suffered some difficulties due to the lack of an absolute majority in the shareholding.

Negotiations between the two companies regarding retained earnings and dividend payout were sometimes difficult. Thus the first priority in acquiring CBS Records as a sole shareholder would have been more to obtain control of the music company than to get hold of the music rights.

At the time of the CBS Records acquisition, Sony received some criticism that it had paid too much of a premium. The firm, however, recovered 60 per cent of the acquisition cost by offering stock to the public three years later.

Thus, access to music software assets was achieved by the CBS Records acquisition. Ohga's next move was to enter the film industry in search of film rights.

It was thought that Sony's hardware business, namely, sales of its

equipment would be accelerated if the firm acquired a movie company with film assets.

Ohga was deeply convinced that the success of the CD business was owing to the acquisition of CBS Records, because it loaded Sony up with a huge library of discs. Norio Ohga and Akio Morita came to believe that the software and hardware businesses supplemented each other.

Likewise the acquisition of Columbia Pictures was viewed by Ohga as a necessary step to promote its new VCR format, namely, 8mm VCR format and to cope with the forecast diffusion of the high-definition TV format, since access to Columbia Pictures' film library would greatly enhance Sony's bargaining power in the market.

Ohga resolved many problems for Sony and set a new direction in its management, but still he left unsolved some important issues.

Regarding the diversification, for example, the film industry entry uncovered the problem that Sony knew very little about film making and distribution. This problem resulted in difficulties in implementing the desired synergy between hardware and software.

The decentralisation reduced Sony's potential to avail itself of synergistic effects among different businesses. It is true that below the divisional company level it created a certain degree of synergy, but at the upper managerial levels it is undeniable some sectarianism emerged.

The remuneration system for a divisional company president was not coherently designed in relation to their performance (Kutsuwada, 2003). Sony fell short of fully adopting a performance-based pay system. Compared with other competing companies in the IT sector, for example, such a 'lacuna' in the system was obvious.

4. SUCCESSION AND FIRM EVOLUTION ON A PIF APPROACH: IDEI'S ERA AT SONY

In this section we will explain how the succession decisions are taken on a PIF approach and how it influences a firm's evolution. In doing so, we will focus on Ohga's succession and the following years of Sony under Idei's leadership.

In 1995 Ohga made it public his successor would be Nobuyuki Idei. His selection was not based on Idei's past achievement, which Ohga thought rather poor: Idei was not successful as head of the Audio Division; his attempt at entering the home computer business had been a failure. Ohga was adamant on this point: his selection was not based on the past but on the potential Idei offered – see the case study.

Ohga's ideal man to lead Sony was somebody who would dazzle the world

with his resplendence. Ohga himself strove to make Sony a company that would dazzle people with its brilliance (Nathan, 1999; Takagi, 2001). His successor therefore had to be a person who understood Sony's uncommon quality of outshining its competitors. And Idei was such a person with 'gut-level' understanding of the core values.

On taking charge of Sony's top position Idei highlighted the continual and drastic changes taking place in the environment. He pointed out the similarity between the sudden nature of change in the business environment and change in the habitat of dinosaurs caused by the fall of a meteor in the Yucatan peninsula:

> The extinction of the dinosaurs was caused by a huge meteor that crashed into the Yucatan Peninsula 65 million years ago … Today's meteor is digital network technology. It will change the rules of business and create new winners and losers. (Healey and Murakami, 2000, p. 132)

The Internet had come of age and its influence as a communication means could not be ignored. Sony needed to adapt its corporate architecture – organisational structure, product range, service offerings, etc. – to the networked society.

Ohga diversified Sony's businesses and decentralised its organisational structure by empowering lower management. Product and service range was amplified, which allowed Sony to widen its revenue sources and depend less on a single product such as the VCR.

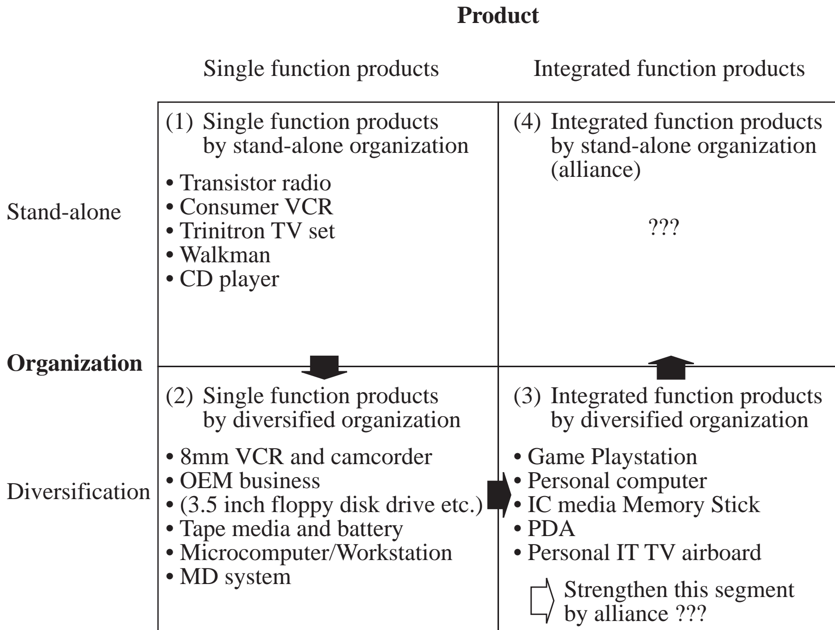
He also introduced first the business unit system and then the divisional company system. However, Ohga's initiatives were centred more on obtaining a competitive edge at the level of business strategy. Idei's efforts focused more on corporate-level strategy.

The clear separation of management and ownership is an example of his efforts. The sheer size of Sony and faster environmental change due to emergence of the networked society made it necessary for Sony to depart from its traditional management style led by charismatic leaders taking care of both business-level and corporate-level strategies.

Figure 3.2 represents graphically the scheme based on which Sony has renewed itself during the past decades including the Ohga and Idei eras.

At its inception Sony had 'stand-alone' units producing single functional products. Activities were not wide-ranging. Founders supervised units and their staff. The centre's role was played by these individual founders. Their proto-image emphasised the uniqueness and not being a copycat, etc.

At this stage Sony produced differentiated products based on unique components such as the transistor and Trinitron cathode ray tube. The founders' product-planning abilities were of primordial importance. Innovative products regularly launched by the firm supported Sony's growth.



Source: Adapted from Kutsuwada (2003)

Figure 3.2 Sony's renewal scheme

Slowing down product launch frequency might mean growth stagnated or even failure of the business.

Another of Sony's weak points at this stage was its unbalanced business portfolio, overdependent on the VCR business. The task for the next leader was therefore to widen its product range.

Ohga's era corresponded to the second stage of the previously mentioned matrix, namely, single functional products combined with a diversified organisation.

Thanks to its effort to consolidate its technological level Sony already had wide-ranging technology. Ohga could use this to diversify into new businesses leveraging on the firm's core competence. To take the market by surprise by offering products which would 'dazzle' consumers was a driving force.

The acquisitions of CBS Records and Columbia Pictures were an extension of Ohga's effort to diversify in terms of products and domain – namely, both domain navigation and selection (Bourgeois, 1980) – to gain economies of both scale and scope. Later it turned out that the synergy effect was more visible in the case of the CBS Records acquisition. The diversification took a heavy toll on the financial structure and Sony's financial plight became precarious.

Towards the end of the Ohga era the Internet age arrived opening the business window of success based on connectivity. Therefore, Ohga's successor would have to address the two questions: finances or financial discipline and the integration of different products in quest of connectivity.

Idei's era ensured Ohga's was the third stage of the matrix, namely, the integrated individual functional products and a diversified organisation.

Idei imposed financial discipline on the organisation by introducing cash-flow management and EVA (economic value added) to run diversified businesses through a 'common thread', namely, cash flow.

He adapted the organisational structure to help to launch more integrated products and services. The connectivity among hardware products and also between hardware and software became an essential success factor.

5. MANAGERIAL STYLES AND ROLES IN THE PIF APPROACH

In the preceding we have described two case studies exemplifying the CEOs' proto-image of the firm as a cognitive orienting structure. In what follows we describe CEOs' managerial styles, roles they have played and their personality traits.

5.1 Sony's Leaders Ohga and Idei

Sony's foundations from inception are characterized by a strong ethic related to the concept of work and employee relations. For example this ethic emphasizes an open mind, freedom to fully realize one's potential, technological advancement, and a sense of commitment to the nation and society in terms of manufacturing and product innovation. From its inception management emphasized technological leadership. The preceding values guided the managerial behaviour of Sony's successive leaders. In Ohga's words, 'Sony must always be extraordinary. Mr Ibuka and Mr Morita were extraordinary people.'

Ohga portrayed his leadership and contribution to these values by maintaining Sony's 'dazing light' to dazzle people. The first step he took was in creating a logo and a brand to focus this shine and by developing new products.

Ohga practiced a hands-on managerial style which showed clear commitment to the firm's values. He attended almost all new product-planning meetings in his intention to diversify Sony, for example, and conveyed explicitly to all personnel what was originally an implicit image of Sony. He ensured that new products were worthy of the image of Sony. Ohga's managerial style was characterized by empowering middle managers. Sony's

diversification and decentralization (the creation of the business unit system and later the divisional company system) attest to this delegation of authority. Having said that, Ohga was deeply involved in business-level strategies.

Ohga, apart from possessing successful decisional acumen, was a visionary. Under his leadership, Sony developed the first PC (though not successfully), compact discs, video games, and acquired a music (CBS Records) and a film business (Columbia Pictures).

Before finishing his reign at Sony, Ohga devoted the utmost care to choosing his successor: Idei.

Idei was selected because of his potential and because he understood the spirit, ethic, and image of Sony.

Idei's managerial style departed profoundly from his predecessor's, Ohga. This may have been due to the role Ohga played in the capacity of a quasi-founder. Idei instead faced the challenge to establish his credibility among his employees as a professional manager.

With the advent of the Internet, Idei envisioned the Sony of the future. He realized for Sony to succeed in the new digital, interconnected world, it had to develop digital products and at the same time relationships with other firms. Given Sony's financial plight when Idei took over, he had to make finance-related decisions. Cash flows were strictly controlled during Idei's era. Notwithstanding this immediate challenge, Idei provided direction and a long-term vision for the company. The vision for Sony relates to a rejuvenation as a 'digital dream kid', his term being 'regeneration'. In this new era, Sony would integrate the electronic and entertainment businesses.

Idei's managerial style emphasized the importance of the corporate center as opposed to Ohga's which emphasized divisional management. Idei's role as a resource allocator and facilitator was clear as he described the corporate center as 'an active investor'. Previously decentralized divisions under the Ohga era had to compete for resources, and while previous leaders created value by focusing on individual innovative products, Idei focused on corporate value. The center became 'professionalised', that is based on a team of managers, mainly the CFO, CEO, COO, and other top executives who took responsibility for providing value to divisions. During Idei's presidency leadership was based on a team concept rather a charismatic individual.

The corporate center, led by Idei, took several critical decisions to consolidate Sony as an international leader. One of these critical decisions was to shift Sony towards digital network-related products. An example was the creation of a device to integrate a television set and a PC.

5.2 Masao Ogura

Masao Ogura's haulage revolution exemplifies how a vision empowers the

development of a company and an innovation. The case of the Home Delivery Service serves to illustrate different angles of Mr Ogura as a CEO; his roles, managerial style, and personality traits.

As with previous cases one important decision of the CEO is the choice of a successor. The case shows one of Masao's activities was to establish a retirement age for CEOs and search for possible candidates. We see in the *Takkyubin* company Masao does not disconnect from his company but continues as a special counselor.

Masao's charismatic leadership so permeates the work of the board that at certain point it weakens the leadership of the new CEO.

Just as posited by scholars, personality traits contribute to leadership (Goleman, 1998; Lewicki, McAllister and Bies, 1998; Kirpatrick and Locke, 1991), however we cannot ignore the importance of the leader's environment. Masao Ogura was born in an entrepreneurial environment, and given his elder brother died young, Masao had to adapt quickly to take the role of the eldest son in the family.

The case illustrates how different environmental events created an imprint in Masao's mind, in particular, his relationship with labour unions, his early school years, and later, his university education. We learn from reading of Masao's life that he was a person of integrity, and the labour force was an important concern for him. This concern for people created support for him when he needed to push for ideas and their implementation.

The integrity aspect also shows in the opportunity he had to take advantage of a friendship his father had with a prime minister, however, he abstained from using that relationship. Masao learned from his entrepreneurial father how to deal with conflict, negotiations, he learned from situations his father faced and dealt with. These situational factors influenced Masao's managerial style later.

Masao's managerial style is characterized as that of a hands-on executive. He would frequently visit the company's branch offices, get to know the processes performed by staff, and identify better or more efficient ways to do them.

Being the son of an entrepreneur his introduction management came at an early time, we know by the age of 29 he was manager of Yamato's subsidiary. In this company he related to several managerial roles, among them the role of planning as the company did not have clear rules or regulations. Masao was forced to be a planner in such circumstances, designing the organization and activities to reverse the company's losses.

In several instances Masao showed entrepreneurial initiatives and develop new ways of doing business. For example, he adopted the relay system in transportation, and use of containers. These are examples of how resilient Masao was and able to adapt to the transport industry's changing environment.

Having said that, when the situation needed toughness he demonstrated that as well. This is seen in the negotiations of licenses with government and the lawsuit initiated against the Minister of Transport.

His major initiative without doubt was starting the home delivery business. In launching this service, Masao displays several capabilities; he is an organizer, strategy designer, and also implementer. In this last role his close relationships with employees and the latter's support helped persuade the company board to take up the initiative. The case study illustrates Masao's managerial life and it is clear that Masao resorted to use of analogies to design new ideas. The home delivery business was designed with the airline's hub-and-spoke concept, for example.

Above all, Masao is an example of a visionary leader. His company's vision was 'a company that would transport any quantity to anywhere in Japan'.

His vision came from an insight that originated from his own personal daily-life experiences and from dealing with day-to-day business. His insight came from synthesizing observations from other transport companies, a meat-chain company, and his own frustration in sending small packages to his own family. This last point highlights the idea that the vision must reflect a need in the market, something of relevance to consumers.

As a hands-on leader, Masao not only articulated the vision but also struggled to make this vision a reality. Masao demonstrated perseverance and communication skills on many occasions throughout his business life and in particular in implementing his vision. The case indicates that the board without exception opposed the vision and he had to organize, plan, and sell the idea to different stakeholders. Moreover, implementing the vision did not come without its problems. Masao had to get permission from government authorities, and prepare drivers to carry his vision under the slogan of service first then profit. Drivers were asked to perform a very different role-set from what they were used to. Masao refered to the analogy of *sushi* restaurant cooks, where they perform all sorts of activities.

Masao's vision took years to implement and develop to the breakeven point, however, in the end he moved his organization from a company fully dependent on large businesses (department stores and the like) to the *Takkyubin* era, or home delivery service.

NOTES

1. Osone (1998) stresses the futility of depending on a market survey, since a new product developed by Sony may not have a market yet. Sony, after all, launches to the market not what customers want but what they may need (namely, needs are untapped by existing products).
2. This intention not to follow others was patent in the word of a CBS/Sony Group's executive.

In 1988, the CBS/Sony Group celebrated its 20-year anniversary. At that time, Ozawa proudly declared, 'The history of our Group has been similar to a painter painting on a blank canvas. And we have been painting our own portrait on a blank canvas successfully for the past twenty years' (Sony Corporation, 1996c). Likewise, Kanoi, Sony's statutory auditor, attributed to Sony's 'world-first spirit' the trend among Sony's engineers to stand up to the seemingly impossible challenges (Kanoi, 1998).

3. Another Sony veteran recognised that at the beginning he had tried to create something new, but later he only tried to create products that fitted Sony's image (*Sony rashii mono wo tsukuro*) (Kihara, 1998).
4. Translated by the authors.
5. In 1969, which should have marked the 50th anniversary of the company, Yasuomi, the senior Ogura, had a stroke. Viewing his father's plight, Masao Ogura became keenly aware of the need to leave the top position at a timely moment. Otherwise CEOs could become a drain on the company.
6. Yanagihara points out that Yamato wanted to have an agent every 500 metres. There were over 280 000 agents by 1997 (Yanagihara, 1997).
7. 'For us Sony's logo is extremely important. The four letters composing Sony's name signify that a product is Sony's … the problem is that if you launch a mediocre product it can charge a premium price thanks to the logo … ' (Kazama, 1998, p. 92) [translated by the authors].
8. A manager interviewed commented that Ohga was product planning incarnate (Kutsuwada, 2003). Another interviewee on 3 June 2003 who worked closely with Ohga pointed out to Kutsuwada that to his knowledge Sony's former CEO never explained to his staff what his proto-image of Sony was (apart from some interviews granted to Nathan, etc.). The proto-image was transmitted and shared among Sony's staff who guessed from Sony's 'legend' what it was, or through formal and informal conversations in which they would try to define what their understanding of Sony (or Sony *rashisa*) was.
9. Ohga (1998) admits he was not enthusiastic over the Walkman. For him it did not signify any technological breakthrough. It was a mere putting together of yesterday's technology. He thought that anybody could do it. As such it was not up to Sony's standard.
10. Sony had been developing the technology since December 1970. The world's first CCD camera was produced in January 1980 for an All Nippon Airways (ANA) jumbo jet to transmit the image of an airplane's take-off and landing to the cabin, acting as the eye of ANA's Sky Vision system.
11. Philips pioneered the optical videodisc system using laser technology in the 1970s.
12. Writing software on CD-ROM was better than doing so on a semiconductor as was the case with Nintendo. Copying software on CD-ROM needed only three days after the order's reception, while writing it on a semiconductor needed three to four months. Therefore the manufacturing of CD was key according to Ohga (1998).
13. Matsushita management thought much in the same way when it acquired MCA in 1990. 'For Matsushita, the strategic benefits of the acquisition seemed clear. The deal would combine MCA's entertainment 'software' – movies, music, and TV shows – with Matsushita's wide range of 'hardware' – TVs, VCRs, CD players, etc. There was much talk about the synergy that would allow Matsushita to revolutionise the marketing of new technologies…The acquisition would also counter rival Sony's push into new product areas' (Inkpen, 1995, p. 340).

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4. Profit-arithmetic approach to business

1. INTRODUCTION

In the previous chapter we explained one successful approach to business observed among outstanding CEOs[1] in Japan, namely the proto-image of the firm (PIF) by reviewing Sony's case supplemented with Yamato Transport's. In this chapter we will explain a second approach: the profit-arithmetic (PA) approach.

Our studies of how successful CEOs approach business decisions seem to indicate their schemata will emphasise (1) profit levers such as cost cutting, (2) daily operations rather than a long-term *grand design*, and (3) priority-setting.

CEOs whose business approach best exemplifies the characteristics of the PA approach are Shin-Etsu Chemicals' Chihiro Kanagawa, and Nissan's Carlos Ghosn.

The analysis will therefore compare the approach of these two business leaders with a focus on the aforementioned three characteristics (points), namely, their use of profit levers, conduct of operations, and setting of priorities. For purposes of clarity we will break down the main concept into its three main characteristics.

2. PROFIT LEVERS

2.1 Kanagawa's Case

PA-type CEOs seem to pay more attention to the actual arithmetic of profit and to how to make individual managers act on the levers to produce the profit than to how each individual manager will behave. Charles Allen from UK's Granada, for example, claimed he was a PVC fetishist (Campbell, 1998). He meant that he focused on price, volume and cost using them as key levers to run the business. Managers were expected to think deeply about how to improve all three levers.[2]

Much in the same vein, Shin-Etsu's Kanagawa concentrates on (1) minimisation of interest-bearing debts; (2) control of the pay-out for dividend; (3) a target of 10 per cent ROE, and (4) a close scrutiny of net income

(Kanagawa, 2002). Despite the unassailable simplicity of these levers one can understand critical factors in the CEO's PA schemata, determining the quality of results in a business.

Apparently concentrating on a limited number of variables may help staff to have a clearer notion of what is expected of them. Also, it presumably helps the CEO to supervise, at a more generic level, drivers with the greatest impact on the value and ultimately survival of the company.

Besides looking at specific levers contributing to business results, we also saw that the CEO needed an explicit understanding of capability sources and their potential impact on a business.

Kanagawa, for example, only fights in the field in which his company can compete successfully – see the case study in the Annex. Thus, his firm focuses on products in which it ranks high globally. These include silicon wafers and vinyl chloride (the world number one), optical fibre materials (number two), and silicon resins (number three).

The focus is supported by determination. In February 2001 Shin-Etsu invested ¥70 billion in installations for production of 300-millimetre diameter silicon wafers in the face of falling demand for semiconductors, their main application. Other companies thought better of it and did not dare to spend money on production expansion. Kanagawa went forward with the investment plan in the belief that semiconductor producers would demand the 300-millimetre diameter silicon wafers as these wafers could halve production costs of semiconductors. The decision allowed Shin-Etsu ten months' head start over its competitors (Shimizu, 2002).

Focus also means Kanagawa steered clear of businesses he thought he could not understand and held on to those he knew well even if they were out of 'fashion'. Some examples illustrate this.

At the time of Japan's bubble economy years (1990s) Kanagawa was presented with a proposal to build and manage a business hotel in Takefu in Fukui Prefecture. The proponents urged him to approve the plan on the ground that everybody including the chairman was in favour of it.

Kanagawa immediately and flatly rejected the plan. He reasoned that Shin-Etsu did not have the know-how or resources to run a hotel business. Run by Shin-Etsu the hotel would be a second-rate or third-rate hotel. Its location would not help, either. It is removed from urban areas such as Tokyo or Osaka. Kanagawa recently guessed that if the firm had taken up the plan it would have lost ¥20 to 30 billion. However, at that time the business atmosphere in Japan favoured such a venture – see the case study.

Kanagawa also prohibited his staff from speculating in financial markets doing what was known as *zaitekku* (financial engineering). He was quite clear on this point: the firm did not have expertise to speculate in financial markets. The *zaitekku* was the nemesis of many a Japanese firm later on.

In referring to the difficulty of success in new products or fields Kanagawa emphasises the value of the old economy – mature businesses – for his firm. The case of Shin-Etsu fertiliser business exemplifies this. It was one of the original businesses with which the firm started. It was relatively small; no brilliant future was predicted for it. Many suggested it should be discontinued or sold off.

Kanagawa resisted the pressure and kept it for 12 years after his appointment as president, showing every year it contributed ¥100–300 million to profit. He sold it as soon as he saw its profit-making possibility seemed to have petered out – see the case study.

Kanagawa's firm belief is that a business should be kept as long as it generates cash flow. Nomura (2002) reports Kanagawa states it takes at least ten years for a new business to start to generate ¥100–200 million profit and it was not easy to be successful in a new business.[3]

Vinyl chloride is another 'old economy' business. It is a low-technology product. Many environmentalists attack it as being a generator of dioxin. Kanagawa is adamant, however, not to shed it since its world market is growing at a rate of 3 to 4 per cent a year. It is also a solid profit generator at Shin-Etsu. So Kanagawa sees no reason to drop it (Kanagawa, 2002).

Vinyl chloride being a commodity means basically everybody produces the same quality. The condition for winning lies in increasing profit by keeping a tight rein on sales and product costs. Kanagawa managed to do so by increasing production without adding more personnel (Nihei, 2002).

To keep cost under control is an important factor for a PA-approach CEO like Kanagawa. He advocates the concept of minimising total cost, while his competitors focus on cost leadership through productivity maximisation, oblivious to the fact that cost reduction is an all-embracing effort including production, distribution, overheads, etc. (Maeda, 2002).

Increasing production capacity may tip the delicate balance in total cost minimisation because it is superfluous, excessive production. In deciding on production capacity increases, Kanagawa's correct reading of the market trend has been an important component.

Minimisation of total cost is pursued in the interest of profit maximisation, which is never sacrificed on the pretext of gaining market share.

He keeps labour cost low at Shintech, Shin-Etsu's major subsidiary in the US, by counting on a chosen few.

Yamagata and Tawara (2001, p. 61) record Kanagawa's opinion in the following terms:

> Business is about how to handle people and get the best from them. You have to let them have a chance to learn. If I see a person is capable, I give him a large assignment. Ten or twenty of them will suffice to change the firm.[4]

Kanagawa (2002) guesses there are 2000 people engaged in production and marketing of vinyl chloride among the nine producers,[5] intermediaries, etc., in Japan. This contrasts with Shintech's 230 staff. Productivity is 8 to 1 in favour of Shintech.

For him vinyl chloride which is almost a commodity item requires severe cost control, which is the only way to survive. Shintech is the only firm in the world generating profit in this product line (Kanagawa, 2002).

No superfluous personnel exist at Shintech. It has only ten salespeople who travel around the world. No unnecessary indirect personnel are to be found at the US firm. Collection and control of accounts receivable are taken care of by Kanagawa's personal assistant. She only got minimum indispensable training: to advise customers ten days ahead of payment-due dates, to chase delayed payments, etc.

Shintech has no financial specialists on its payroll. Kanagawa does not think the US firm needs any financial person to borrow money when the firm's equity ratio is 89 per cent.

It is also true that *errare est humanum*. Kanagawa's heart still bleeds, however, when he remembers ¥4 billion the firm spent on its corporate identity campaign. The spending went to sponsoring motorcycle competitions, TV commercials, etc. Kanagawa's assessment regarding its results is negative. Nothing was got from it. It hurts him to think that with ¥4 billion the firm would have been able to build two research laboratories. His excuse is that he was only a vice president at the time and could not stop his president from doing the spending.

But he learnt. Despite abundant cash on its balance sheet (¥300 billion), Kanagawa (2002) is against moving into a new headquarters building and insists on staying in a rented office building. Apparently what terrifies him is not so much the amount of money but the loss of time and energy for moving – a month spent on it might be better used for the development of a new business.

2.2 Ghosn's Case

Upon arriving at Nissan as its new COO (chief operating officer), Ghosn prioritised actions to lead to generation of profit, which was the issue if Nissan was to survive. The firm was strapped for cash and could not carry out needed product-line investments. Nissan's margin was low due to a poor brand image. Purchasing costs were 15 to 25 per cent higher at Nissan than at Renault (Ghosn, 2002). The plant capacity was in excess of sales by a million or more cars a year. The company's debts amounted to US$11 billion.

Ghosn took measures that would immediately impact its balance sheet and profit and loss account. First, he estimated Nissan's assets at US$4 billion, the

use of which was suboptimal and took immediate action to remedy it. They mainly related to the capital locked up in non-core financial and real-estate investments, especially in *keiretsu* partnership (Ghosn, Rivas-Micoud and Carvell, 2001). The problem for Nissan was that the majority of these investments in shareholding were too small for the firm to have any influence in the companies concerned. A case in point was the shareholding in Fuji Heavy Industries, manufacturer of Subaru cars. Despite its ¥26 billion stake in it representing 4 per cent of total shares, Nissan was not informed beforehand when Fuji entered into the alliance negotiation with General Motors – see the case study. Ghosn sold the stake in Fuji and used the money generated for development of new models. He was sure Nissan as a shareholder and Nissan as a customer have two different statuses and the sale of the share stake would not affect the business relationships.

The second measure Ghosn adopted related to cost cutting. Since 1992, Nissan had undergone several cost-cutting operations including closure of Zama Plant, reduction of personnel from 53 000 to 48 000, secondment of 2500 people to dealers for support, and debt reduction by ¥1 trillion (Kai, n.d.).

In line with these cost-cutting efforts the firm had been busy trying to reduce overheads on different fronts. As examples, a ban was imposed on the use of business-class seats for overseas business travel, and a recommendation on saving in use of paper and office materials was communicated. Also a policy was established whereby the air conditioning had to be turned off after hours.

For Ghosn, these efforts only served to punish personnel and did not have anything to do with the route to recovery let alone did they address the cause of Nissan's ailment. The area contributing a high percentage to the profit-and-loss account was targeted for immediate remedy and action. Procurement was such a priority area, since it represented as much as 60 per cent of cost of goods sold. However, for Nissan's previous management it was a sacred area because of long-standing relationships with suppliers forming a *keiretsu* and nobody dared to touch it. Ghosn took the bull by the horns in this matter by concentrating purchases from fewer suppliers, asking them to cut their prices on the promise that Nissan would purchase more when the business turned around.[6] Accordingly, NRP (Nissan Revival Plan) proposed to cut cost by ¥1 trillion by financial year 2002, of which 60 per cent corresponded to material purchases. The remaining 40 per cent was broken down as follows – 28 per cent to sales and general administrative expenses, 10 per cent to production, and two per cent to other sundry items – see the case study.

More often than not the high purchase cost was due to an excessive specification. Nissan had tended in the past to demand unnecessarily high performance. Ghosn appointed accordingly a 300-member team independent of the purchase department to review procurement specs.

Nissan bent the traditional way of doing business in Japan by breaking away from the habit of buying steel from all five blast-furnace steel mills in a more or less balanced way (25 per cent from Nippon Steel, Kawasaki Steel, and NKK, the remaining percentage from Sumitomo Metal and Kobe Steel). Instead, Nissan would buy 60 per cent of its steel from Nippon Steel, 30 per cent from Kawasaki Steel, and 10 per cent from NKK. The concentration on the two steel mills offered better prices thanks to economy of scale. This clearly marked a departure from the tradition of working with a *keiretsu* company when we consider the fact that NKK (which belonged to the Fuji Bank Group – Fuyo Group – as Nissan) did not enjoy privileged treatment.

A firm such as Kansei, a supplier of electronic control devices, tachometers, instrument panels, etc., decided to face reality by developing the best it could to meet Nissan's requirement. It had to, since the sales to Nissan represented 80 per cent of its total revenue. Nissan and Kansei executives as well as engineers held discussions during several days in a hotel to find a way to reduce cost.[7]

3. PRIORITY SETTING

Sorting out one's priorities is an important management action. CEOs with a PA approach prioritise those decisions and actions directly bearing on the generation of profit.[8]

3.1 Kanagawa's Case

Kanagawa is uncompromising about the firm's purpose being to give a return to shareholders. For him the only owners are shareholders. Therefore the CEO's bosses are shareholders, not employees who are part of the firm. CEOs should not confuse this point: the firm does not exist to cater exclusively and mainly to employees (Kanagawa, 2002).

Kanagawa emphasises the achievement of a firm's objective does not preclude the firm from observing social ethics and a code of behaviour as a social corporate citizen. He stresses likewise that a firm contributes to society by paying corporate tax, but that the contribution to the society is a result, not the objective of the firm's existence. A private firm is for making profit. Shareholders have entrusted managers with handling their money. CEOs are bound to fulfil that trust by contributing a return on their money (Kanagawa, 2002).

In operational issues Kanagawa does not advocate pure drudgery in attaining a goal. This is remarkable in Japan where new recruits are told more often than not (1) to take action rather than to think, and (2) to appeal to the

emotional reaction of customers.[9] He made a point of telling his younger staff that they ought not to attempt to achieve results by dint of mere physical hard work. In its place he emphasises the importance of designing a creative and imaginative plan. He insists on quality, not quantity of labour.[10]

3.2 Ghosn's Case

Nissan's Carlos Ghosn had three times experienced a turn-around situation before arriving at Nissan: Michelin Brazil, Michelin US, and Renault. On each occasion Ghosn stood out because of his capability to put issues in order of priority and have appropriate measures implemented. We will examine what Ghosn did in each of these three situations. The final part of this subsection will review his Nissan days.

First, let us review the Michelin Brazil situation. The Brazilian tyre plant was commissioned in 1981 and was operating under hyperinflation – 1000 per cent a year.

On taking up his position in 1985, Ghosn prioritised two issues: (1) the definition of what the problems were and what actions were to be taken and (2) putting them in order of priority.

The problems identified were:

- reduction of debts by sale of assets unrelated to business; minimisation of inventory and product in progress
- negotiation with the government to adjust sales price every month
- keeping control of labour costs by monthly adjustments to wages in consultation with labour unions.

In a hyperinflation situation it was hard to know if the firm was making money or not. Ghosn did everything within his reach: inventory management, timely raw materials import, renegotiation of payment conditions, price adjustment, production improvement, quality control, labour union negotiation, employee motivation improvement, etc. The firm's performance improved and it started to record profit in 1987.

The second situation relates to Ghosn's stay in the US where he was seconded in 1989 as the head of Michelin's North American operation. The main task was the merger with Uniroyal Goodrich.

The merger agreement was signed in 1990. Michelin Group went into the red at the same time due to a recession. In the following three years its losses amounted to US$1.85 billion.

Against this backdrop Ghosn identified one hurdle to overcome as being cultural differences between the two firms. Michelin was family-owned and set store by products, technology, and quality. Long-term objectives were

given priority. In the case of loss, owners and managing partners had to support the firm with their own personal equity, signifying these two groups of people had more say in management than general shareholders.

Uniroyal Goodrich attached more importance to short-term quarterly performance. R&D spending was decided according to short-term earnings.

Two key issues were mapping out of marketing and sales strategy and overall restructuring. The cultural difference cropped up in every decision-making situation.

Regarding marketing and sales, Michelin had to switch from a single-brand to a multi-brand policy. Michelin used to have its homonymous brand, whereas Uniroyal Goodrich had Uniroyal, BF Goodrich, PBs (private brands), etc. The positioning of each brand, sales, pricing, distribution channels, etc., required a new decision.

Management decided to unify the sales of all brands and a team was assigned to each different distribution channel such as volume sales, independent dealers, etc.

The second key issue was addressed by organising a cross-functional team (CFT) in view of partisan reactions among initial task teams.

In 1994 Michelin Group recorded a US$247 million net profit. Recovery from economic recession, cost reduction, and success in the multi-brand strategy all contributed.

The third situation took place when Ghosn was headhunted by Renault in 1996 and was appointed vice president in charge of R&D, purchase, manufacturing, engineering, and product planning. Renault lost US$1 billion that year.

Ghosn undertook to cut cost at Renault ('*le cost-cutter*' as he was known). His objective was to cut cost by US$2.4 billion in three years. People were sceptical because of Ghosn's inexperience in the automobile industry. Ghosn, however, was optimistic in his belief that achievement of visible progress would convince people of the need for drastic measures.

The cost cutting was predicated on elimination of excessive production capacity, introduction of product engineering to speed up development of new models, reduction in the number of suppliers from 300 to 150, reduction of main platforms from five to three, and acceleration of product innovation.

Renault's CEO, Louis Schweitzer supported Ghosn's initiative. Plants were closed and CFTs were implemented. Renault came out of the red in 1998.

From the study of Ghosn's decision-making process we came to realize that Ghosn's first reaction in the face of a challenging turn-around task is to identify problems. Secondly he prioritises them in order of importance and urgency in terms of profit generation. Finally, we must add the previous three similar situations prepared Ghosn to face the turn-around challenge at Nissan.[11]

With the expertise gained in the aforementioned situations Ghosn landed at Nissan. Immediately he identified two key problems (Ghosn, 2001): One, the continuous decline of Nissan's market share in both global and domestic markets (eight years in a row in the first and 28 years in a row in the second). The attendant and second problem was Nissan's dismal performance financially speaking.

Ghosn attributed these problems to five reasons. First, lack of focus on profitability. Second, lack of focus on consumers. Third, no collaboration was being pursued in joint tasks across functions and departmental boundaries. Fourth, no sense of crisis was felt among its employees. And fifth, no shared vision existed regarding Nissan's future.

4. A BIAS TOWARDS DAILY OPERATIONS RATHER TOWARDS A LONG-TERM *GRAND DESIGN*

4.1 Kanagawa's Case

Kanagawa is against the argument that CEOs should not focus on daily but on long-term issues, since their task is to set in place a long-term vision and plan – see the case study. He wonders how somebody can plan ahead if they are incapable of sorting out today's problem. He rubbishes a mid-term plan:

> … It's useless to make a mid-term plan. You can prepare a beautiful plan by increasing the sales price and lowering the cost of goods sold on paper. Why can you forecast for three years if you even don't know what will happen next year? (Nomura, 2002, p. 51)

Kanagawa is convinced that a long-term vision comes as an accumulation of daily works. He does not deny the need to develop a longer-term plan. A lack of such a plan offering a time-frame may make it difficult to develop a new business.

The focus on short-term, daily issues tends to lead CEOs to a certain bias on the future and influences their long-term plan. A caveat is that the market will never ever move in the direction one wants it to move.

Kanagawa works out his forecast of the market but fights shy of making a plan based on it. Even if he makes one, he tries to foresee a worse scenario than his forecast indicates. He maps out an action plan in preparation for a worse or the worst situation – see the case study.

The orientation to short-term, daily operations leads to actions. Actions are based on fast decision making. Kanagawa is proud of taking the majority of decisions in 30 seconds. Out of ten proposals he gives an immediate comment

or decision on eight or nine. He never puts off the decision making to consult the board (they meet once every other week).

For tons of documents which find their way to his desk, he spends a few second on each one of them and goes quickly through it. He sets aside those requiring further study. If the explanation on the document is lengthy, he asks the person who has written it to give him a brief verbal explanation.

How this fast decision making may benefit the firm is illustrated in the investment in 300-millimetre diameter silicon wafers referred to earlier in this chapter. The launch to the market of this product in February 2001 led to a ten months' lead over competitors, which enabled Shin-Etsu Chemical to enjoy a 60 per cent global market share.

Kanagawa had been observing a year earlier how quickly the market was heating up, presaging a plateauing-out of demand and then a fall. He judged the boom would not last more than six months and decided Shin-Etsu had to enter the market before it started its downward trend.

Kanagawa did not consult the board of directors for the decision. For him speed was everything and he could not jeopardise the business opportunity by listening to generic discussions. So he gathered some informed opinions and approved the investment under his exclusive responsibility.

4.2 Ghosn's Case

Perhaps because of Nissan's plight (falling market share, mounting debts, consecutive losses, etc.) Ghosn did not have any alternative but to concentrate on the survival plan of the firm in the short term directed towards concrete actions. Be that as it may, he made public the Nissan Revival Plan (NRP) in 1999 covering financial years 2000 through 2002. It comprised – see the case study:

Commitment

1. to become profitable by 31 March 2001
2. to reach 4.5 per cent operating margin on sales by the 31 March 2003
3. to reduce net automotive debt from ¥1.4 trillion to ¥0.7 trillion.

Main restructuring measures

1. to reduce headcount from 148 000 to 127 000, namely, a 14 per cent cut by 31 March 2003
2. to cut production capacity by 30 per cent through the closure of three assembly plants and two power-train plants and reduce the number of platforms from the then-current 24 to 15 by 31 March 2002
3. to reduce purchase cost by 20 per cent and supplier numbers from 1145 to 600 by 31 March 2002

4. to sell off shareholdings in non-core subsidiaries and assets
5. to increase annual investment from ¥210 billion to ¥310 billion.

What may have distinguished Ghosn's determination from his predecessors' was his declaration that he would resign as COO if NRP targets were not achieved. It meant that if Nissan could not come out of the red in financial year 2000, he and his management team would give up their posts (Ghosn *et al.*, 2001).

Likewise Ghosn's 'greatness' consisted not only in fulfilment of the NRP (which he managed) but also in preparing to launch 22 new models by 2002. Bluebird, X-Trail, Primera, Cima, Caravan, Skyline, and Stagea would also undergo model change. This meant he was not a mere cost cutter and turnaround artist but a more profound entrepreneur.[12]

The NRP was ultimately replaced by Plan 180 centred on growth, profitability, and debt reduction. *1* stands for the sales increase by 1 million cars, *8* for the 8 per cent return on sales, and *0* for zero debt – see the case study.

5. PA OPERATIONALIZATION

Previous sections in this chapter illustrated how two CEOs with a PA approach put emphasis on (1) profit levers; (2) daily operations, and (3) priority-setting activities.

The interrelationships among these three components are graphically represented in Figure 4.1.

Excellent business leaders with a PA approach can identify basic essential levers to generate profit. The decision maker is not ambiguous at all about which variables are to be handled and how they contribute to a successful business. Along with identification of levers or variables is the understanding of what resources, namely, tangible and intangible (visible and invisible assets) as well as capabilities (Barney, 1991; Prahalad and Hamel, 1990), are needed to succeed in a particular business (their firm has to help to define the business in which it can be successful). Thus, the focus seems to be on what the firm can cope with and what it cannot. The leader's persuasion that the firm is doing the right thing allows the firm to conduct its business with determination.

Once the business domain is defined as to where the firm has a potential for improvement or competitive edge, it becomes easier to sort out important management actions in order of priority. CEOs with a PA approach prioritise those decisions and actions directly bearing on profit.

As to how the priority is set we have seen two different modes. One is represented by Kanagawa. He works out his short-term and day-to-day actions

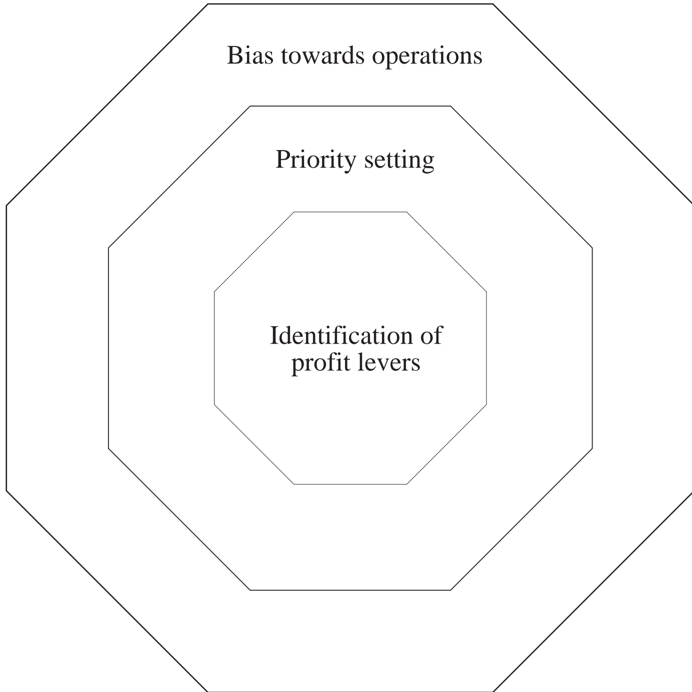

Figure 4.1 Profit-arithmetic scheme

based on his forecast of the market but falls short of making a plan based on it. Even if he makes one, he tries to foresee a worse scenario than his forecast indicates. He maps out an action plan in preparation for the worse or worst situation. The orientation to short-term, daily operations leads to actions. Actions are based on fast decision making. In this mode the framework within which each action takes place cannot be clearly foreseen or discerned. We assume this type of CEO has accumulated enough connections between the results of a business and specific levers and circumstances during their lifetime. These connections are transformed into deep structures through time and become automated. The more experienced the CEO is, the deeper the structures are, and the more complex in terms of ramifications. At the same time the more automated they become.

The other mode is observed in the way Ghosn moves. He provides a general framework setting the stage for each action. His NRP (Nissan Revival Plan) proposed distinct quantifiable objectives, with both a measurable quantity and time-frame, such as profit by 31 March 2001, and measures to take to reach these objectives such as reduction of headcount from 148 000 to 127 000 by the same date.

Overall, identification of profit levers, prioritisation of tasks and operational focus are, we observed in the two leaders, closely interrelated. The clear identification of profit levers facilitates prioritisation of different alternatives by placing high priority on day-to-day actions to result in profits.

When we analysed the PA approach of the CEOs we thought the approach could degenerate into tunnel vision and limit operations to short-term daily actions to the detriment of the long-term sustainability of the firm.

However, evidence indicates that neither of the two business leaders we studied are oblivious to their long-term obligations such as education of the candidates to succeed them, investments in promising new fields, or stashing away profits for future investments, etc.

In an interview cited by Shimizu (2002) Kanagawa stressed he was concerned about selection of his successor and said he had his mind on several candidates. Kanagawa's view is that sending managers with potential to subsidiaries as their top people serves nicely to nurture future leaders, a departure from the traditional Japanese view where managers who drop out of competition for the top position would be sent to subsidiaries (Maeda, 2002).

Carlos Ghosn never gets tired of telling people he will choose, in due time, his successor as Nissan's president, who will most probably be a Japanese. He seems to have some candidates in mind. Ghosn is due to leave for France in 2005 to replace CEO Schweitzer. He emphasises even if he returns to Paris he will watch over the two entities, namely, Renault and Nissan. For a comparison of the Nissan Revival Plan – NRP – with the actual results see Table 4.1.

Focus on daily business never impeded Kanagawa from making a bold move when it is required and the move implies a quantitative and qualitative jump for the firm. A case in point was the 1976 takeover of Shintech, a Shin-Etsu US joint venture subsidiary. The takeover meant disbursement to the US partner of US$12 million (¥3 billion), which was five times Shin-Etsu's ordinary profit at the time. The board was reluctant to go ahead, but thanks to President Odagiri's unyielding support, the deal went through. The US subsidiary is nowadays Shin-Etsu's main profit source.

Ghosn did not ignore the importance of investing in new model development. At the same time as deploying efforts to reduce costs, he prepared an exhaustive plan to launch new models. The plan centred on the three major markets, namely, Europe, Japan, and the US. Table 4.2 shows a list of models due to be launched after 2002.

Kanagawa's efforts resulted in the firm having these past few years ¥130 billion-worth of cash flows every year which has translated into a ¥300 billion-worth cash chest. To take advantage of the cash-rich balance sheet, he is watching out for a new business chance. In his own words:[13]

Table 4.1 Nissan: NRP vs actual results

	FY 99 results	FY 00 results	Actual results in FY 01	NRP Objectivs for FY 02
Operating margin	1.4%	4.75%	7.9%	More than 4.5%
Operating profit	$6.8 m.	$2.4 m.	$3.9 m.	N/A
Net profit (loss)	($5.7 m.)	$2.8 m	$2.9 m.	N/A
Net automotive debt	$11.2 bn.	$7.9 bn.	$3.4 bn.	Less than $5.8 bn.
Capacity utilisation in Japan	53%	51%	N/A	82%
Purchasing cost reduction	N/A	11%	N/A	20%
Number of parts suppliers	1 145	810	N/A	600
Number of employees	148 000	133 800	N/A	127 000

Source: Based on Ghosn (2002, p. 44) and Nissan's press release dated 20th May 2002

Table 4.2 Nissan: plan for new models after 2002

Europe	Japan	US
Primera	Moco	Z-Car
LCV	Elgrand	Murano
	Z-Car	FX45
	Cube	Maxima
	Sedan	G35 Coupe
	Coupe	M45

Source: Based on Nissan's FY 2001 financial results preview: Nissan Revival Plan review and Nissan 180 presentation

> [Unlike] special products that are usually in a seller's market, a commodities producer may only have the chance to control the price once every ten years. Capable managers are those who conclude advantageous deals and from whose attention such a chance does not escape. The decision to increase production capacity must also be based on the reading of the market whether you are in a seller's or buyer's market …
>
> [We] set up in our firm a committee named Z Committee chaired by me presiding over the decisions related to new businesses … Z Committee did not function well … One of the reason for this malfunctioning was that decisions were taken on the basis of majority voting … I changed this system and decided that I would take responsibility for decisions but would not delegate them to a committee … As the decisions on new business affect the future of a firm, they should be a competency of the CEO …
>
> [New business decisions] should not be considered unalterable. We Japanese tend to think foolhardily that once a decision is taken we have to exhaust all means to achieve it …CEOs' role is to judge when to insist on carrying out the decision and when to back off … (Kanagawa, 2002, pp. 120–2).

Does it not depend on the business environment whether PA or PIF is adopted in light of the accepted wisdom that some firms are prosperous because they adjust to their environment? (Goold and Campbell, 1987b; Miller, 1981; Woodward, 1958, 1965; Zajac, Kraatz and Bresser, 2000)

One may be led to believe that because the PA approach is fundamentally oriented to profitability the corporate center would only exercise influence through the budget process rather than in developing strategies.

The belief among PA-type CEOs that they and their corporate center play the vital role in taking care of business performance, was clearly observed in our sample firms.

Their tasks include sanctioning expenditure, agreeing targets, monitoring

performance against targets and taking action to help poorly performing management teams. In this, their style resembles that of Financial Control companies as defined by Goold and Campbell (1987b).

However, their management style contrasts with the characteristics of Financial Control companies described by these authors, namely:

- unlike Financial Control companies the two companies do have formal planning systems
- their concern is not limited to the financial results, nor do they control only against annual targets
- strict short-term (2-4 years) payback could be one of their investment criteria but not to the exclusion of other longer-term criteria.

Overall the motivational structure these Japanese CEOs count on is not based on the trade-off between more or less autonomy and more or less individual performance accountability. Financial Control is supposed to lean on the individuals' accountability in exchange for the autonomy of their actions.

In addition to the influence the corporate centre exerts on the firm, leaders play a key role under the PA approach, perhaps more than under the PIF approach. For example, in both of the PA approach cases, Shin-Etsu and Nissan, financial analysts suspect there is a Kanagawa premium in Shin-Etsu's share price (Mayumi, Nishigashira and Tomioka, 2002). At the time of writing, Shin-Etsu would face in the near future the problem of how to find a successor to Kanagawa who was 76 in 2003.

Likewise it is obvious Nissan's turnaround owes very much to Ghosn and his personality. This management perspective posits that the management of a company is not a science (Chalmers, 1978) but an art.[14] As Rumelt, Schendel and Teece (1994, p. 2) state, 'strategic management may never enter an era of "normal science"' and 'in Kuhnian terms, perhaps strategic management is pre-paradigmatic'.

As each individual business leader has physical limitations to carry in managing a firm, the instability linked to them is unavoidable. The only way out is to systematise education and nurturing of succeeding leaders. We believe by understanding the PA approach governing these CEOs' decisions, we are capable of helping future managers in their endeavours.

When we examined cases and literature material produced on Ghosn and Kanagawa we came to realize the business situation and its environment triggered the PA approach. For example Nissan's mounting debts and falling market share could have invariably motivated Ghosn to opt for the PA approach.

Having said that, whether a leader's approach is PA or PIF seems to depend

to a large extent on their personality, background, training, belief system, etc.

The PA approach better matches a relatively stable business environment. It resembles what Goold and Campbell (1987b) have termed the Financial Control strategic management style. The authors hold that Financial Control companies are most powerful in drawing maximum performance out of established businesses. Other characteristics enumerated by Goold and Campbell (1987a) such as growth by acquisition, individual accountability, etc., do not necessarily present themselves in the PA approach.

Success is commanded when the business leader's PA approach fits the requirement of the business micro and macro environment, namely, the life-cycle stage in the industry, the company's financial and marketing position, and broader economic and socio-cultural trends.

5. MANAGERIAL STYLES AND ROLES IN THE PA APPROACH

An assumption underlying the case studies is that CEOs affected business performance through their actions, personal influence, mind-frames, and charisma. In particular we have emphasized in this book the view that CEOs entertain specific mind-frames guiding their actions, namely a proto-image approach of the firm and a profit-arithmetic approach. These cognitive redefinitions of the firm in the CEO's mind act as the propeller to modify performance within an organization.

Notwithstanding the importance of the cognitive approaches, we believe it is necessary to discuss CEOs' managerial styles, roles, and personality traits since they contribute to strategic implementation together with cognitive approaches. After all strategic leadership is a complex mix of not just thinking patterns, but also effective management (team development, for example) which comes from practical experience and personal characteristics.

We cannot, for example, ignore Carlos Ghosn's early practical experience in Michelin as director of a manufacturing plant in France at 26 and later as COO of Michelin's South American operations in Brazil when just 30. He himself acknowledges this preparation when he assumed his role in Nissan: 'I don't know how I should express my feeling when I took charge of the post as Nissan's COO. Déjà vu? Synchronicity? … What I have done so far was for me to get trained and prepared for this moment.' Ghosn adds in regard to the differences between his previous appointments the following: 'If I don't look at the differences in the dimension, I have done all these things' (Ghosn *et al.*, 2001, pp. 155–6)

Chihiro Kanagawa, Shin-Etsu's CEO, also recognized the importance of his working experience while in Kyokuto Bussan, a food trading company.

Moreover, he was of the view that sending managers with potential to subsidiaries as their top people would serve well to develop future leaders. In fact, Chihiro perceives a CEO's role as to identify potential leaders within a company and give them a fair chance.

5.1 Team Development

Some literature acknowledges the importance of team leadership to the point that teams have been deemed to be the building blocks of organizations (Belbin, 1992; Turner, 1999). Nissan's case study illustrates how important cross-functional teams are, and the pivotal role the CEO plays in forming those teams to promote change within an organization. The CEO's supportive role is reflected in at least two ways in the Nissan case study. First the CEO facilitated the team's capabilities and empowered group members to accomplish their work. This empowerment is clearly exemplified by appointment of leaders at the level of executive vice president for these cross-functional teams. The formation of the teams was also an opportunity for Carlos Ghosn 'to have a close look at the next generation'.

5.2 Managerial Roles

Managerial roles have been used widely in the leadership literature to explain what managers do (Besanko, Dranove, Shanley and Shaefer, 2004; Mintzberg, 1973a, 1990; Schein, 1994). Mintzberg (1973b) classified managerial roles into three categories: interpersonal, informational, and decisional. Activities concerned with interpersonal relationships relate to managers as figurehead, leader, and liaison. The informational role comprises activities aiming at collecting and disseminating information, and portrays the manager as the organization's spokesperson. The third category refers to the decisional role. The manager may act as an entrepreneur discovering problems or opportunities and decide what is necessary for the organization. Other activities under this role are the manager's involvement in handling disturbances originating from unforeseen events, resource allocation, and negotiating.

Other authors have ascribed additional roles to a manager or leader such as the architect, change agent (Kets de Vries 1998).

Nissan's and Shin-Etsu Chemicals' CEOs illustrate the different roles above. Carlos Ghosn's informational role is evident when he sought out information from Michelin and its environment to understand the overall problems the firm faced. He started this search in Michelin's manufacturing division although he had been offered a better position in the R&D technical center. We later know he played this role again as COO of Michelin's South

American operations. The case illustrates that 'Carlos walked around the plants whenever possible, discussed and exchanged opinion with salespeople, factory workers, dealers, etc.' – see the case study. This role is also prominent when Nissan and Renault created the Global Alliance Committee where both companies shared information regarding strategic directions. The monitoring role cannot be easily separated from the role of the disseminator since we presume that as the CEO collected information, he was also transmitting information to others verbally and symbolically (e.g. by gestures).

The Nissan case exemplifies how CEOs are involved in several decisional roles such as negotiating, disturbance handling, and resource allocation. For example, Carlos Ghosn decided on drastic restructuring measures requiring reduction of labour, production capacity cuts, reduction in supplier numbers, and non-core asset sales. All these required not only negotiating abilities but also certain personality traits of effective leaders like extroversion, assertiveness, emotional stability, enthusiasm, trustworthiness, self-confidence, high tolerance for frustration, sense of humour, and an internal locus of control (Craik, Ware, Kamp, O'Reilly, Staw and Zedeck, 2002; Goleman, 1998; Kirkpatrick and Locke, 1991; Lessen and Baruch 2000).

5.3 Managerial Styles and Personality Traits

The interplay of personality traits and decisional roles is well illustrated by Kanagawa's decision to renegotiate a contract with one supplier for a better price while the contract was not due for renegotiation. Chihiro showed determination and an emotional maturity to keep cool in the midst of a potential turmoil caused by the renegotiation conditions. In Chihiro's view leaders must have the judgement to assess information, foresight to predict the future ahead of other competitors, and character. In his view, these are personality traits with which an individual is born. Farsightedness, conceptual thinking, and insight have been referred to in the literature as contributing cognitive factors in leadership (Dubrin and Dalglish, 2003; Kets de Vries, 1998).

Ghosn's experiences also illustrate the combination of managerial style and personality. Ghosn not only decided to reduce the number of suppliers but to break away from a Japanese tradition of dealing with *keiretsu* companies. By doing that, he set apart the relationships between equity and supply chain Nissan had with the *keiretsu*.

He also empathised with employees and allowed them to participate and provide ideas. He believed staff had sufficient ideas to bring Nissan out of the situation it found itself in without the need to hire any consultants. His managerial style was very much of a directive type, he centralized planning but delegated authority to well-defined tasks for the cross-functional teams.

Perhaps a distinctive characteristic of both Carlos Ghosn's and Chihiro Kawagawa's managerial style is their achievement orientation. Both leaders had clear objectives about what needed to be done and achieved in a period of time. Nissan's CEO developed the Nissan Revival Plan which specified benchmarks to achieve. Kanagawa's opinion of a manager is that they should have clear objectives and ways in which to achieve them. Kanagawa's case study reflects several instances of targeted milestones to produce a return for the shareholders.

Finally, after having mentioned the importance of personality traits which accompany managerial styles and roles, one must not forget the importance of luck. Chihiro believes he has been favoured by luck, and the difference perhaps between successful and less successful managers is that he took it when it came.

Carlos Ghosn was also favoured with luck just after graduating as an engineer when he was approached by Michelin. Perhaps if he had continued his education at the Masters or PhD level his trajectory may have been different.

NOTES

1. Nissan's Carlos Ghosn pushed forward his turn-around plan while he was still a COO, but evidence indicates he was the power behind the turn-around more than Yoshikazu Hanawa, the CEO at the time, who gave his total support to Ghosn's plan.
2. As a matter of fact these three components are all major variables in profit-arithmetic. Increase the price (P), sell more (V), and spend less (cost) – namely, do everything in a mature industry – are Allen's message.
3. Contrast this with Sony's continual effort to launch new products described in Chapter 3.
4. Translated by the authors.
5. Sawato (2000) predicted that in the chemical industry Japan's survivors in the global competition would only be Shin-Etsu Chemicals, Fuji Film, and Mitsubishi Chemical.
6. According to Nikkei Business (2000, p. 280), 'The components suppliers were a main pillar for Japanese automakers. Many of them thought that Nissan had managed to launch many of its new models thanks to their technical collaboration. Yoichiro Kaizaki, the president of Bridgestone, for one, expressed his doubt about the feasibility of reducing supplier numbers. Nissan launched an initiative named Quality 3,3,3 to improve on its productive attractiveness, product quality, and sales and service.'
7. Kansei, later to merge with Calsonic, a supplier of airconditioners and radiators, even took advantage of the Nissan–Renault relationship and sent a mission to Paris to sell its components module in search of scale economies (Nikkei Business, 2000).
8. 'The primary goal of the firm is profit maximisation – or, equivalently, maximising shareholder value' (Grant, 2002).
9. K. Kase heard from a company-sponsored student that as a young graduate he had been told by his superior he must learn how to cry in front of his customers to get an order by touching the customers' sentimental emotions. The company is a leading manufacturer of construction machinery. This kind of salesman–customer relations is common in many industrial fields in Japan. People often criticise you if you are too brainy and may tell you that you should behave more viscerally ('*baka ni nare*').
10. See the case study in the Annex.

11. This is eloquently expressed by Ghosn as follows. 'I don't know how I should express my feeling when I took charge of the post as Nissan's COO. Déjà vu? Sychronicity? Or was it a trick of my imagination? I could not get away from the impression that I was here before. "Here" does not mean the "place" but the "situation". The lack of profitability, excessive penchant for market share, chaos, ambiguous responsibility. There were numerous problems. However, all these problems were familiar to me. I sat in my office and thought as follows. "What I have done so far was for me to get trained and prepared for this moment. The restructuring, reorganization, transformation of the employees' mind-set, merger of two different cultures, and cross-cultural management. If I don't look at the difference in the dimension, I have done all these things"' (Ghosn *et al*., 2001, pp.155–6).
12. The media was cautious about how to assess Ghosn's survival strategy plan. In its number in 2002 the *Fortune* magazine cited a financial analyst and expressed its concern: 'Nissan cannot rely on restructuring for ever …'.
13. Translated by the authors.
14. 'In Business Policy should be taught the *art* of doing business, that is, making money by offering a legitimate product or service to society. The knowledge necessary to govern an organization capable of this goal should also be taught. How to structure this governing function, how to institutionalize the group, and how professional commitment should function should also be taught … Another axis in the philosophy of this work is the role of business initiative understood as the capacity of an individual or group to begin to think about doing something and then to do it. It is precisely this that invests organizations with vitality in a fundamental way' (Valero y Vicente and Lucas Tomás, n.d., p. 3).

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5. Conclusions

1. INTRODUCTION

In this book, we have raised and taken up a question concerning the performance of Japanese companies. Since the Japanese seemed to be invincible in the 1970s, and in the 1980s seemed to have faltered, why were some Japanese firms doing well?

Our main purpose was the analysis of the causes and factors that led some Japanese companies to succeed during the 1990s. We were concerned with the value business leaders create, too often overlooked in Japanese firms. Japanese management tradition seems to regard the bottom-up process as more important than the top-down process. Consequently, CEOs are even seen as expendable or fungible leading to appointment of people with hackneyed ideas, often preferring to imitate competitors' strategy.

The objectives of the book, exposed in Chapter 1, were specified in six questions we aim to answer throughout the book. These questions are:

1. What common traits do the successful firms possess?
2. Are there some distinctively different approaches to business?
3. How do the different approaches differ in effect? Is one approach more successful than the other?
4. Why do these different approaches exist? Can they co-exist in the same company?
5. Do the different approaches add value to a business? How?
6. How can firms continue their success even if their leadership changes?

To answer these questions, four successful Japanese companies and their business leaders were studied. We chose Nissan, the automobile company that was close to bankruptcy a few years ago and was successfully brought to recovery by Carlos Ghosn and his Nissan Revival Plan. We also studied one of the few chemical companies in Japan that survived competition, Shin-Etsu Chemicals and the CEO Chihiro Kanagawa, considered by Jack Welch as one of the excellent top managers in Japan courageous enough to push forward his company's continuous renewal. We have also analysed how Masao Ogura has turned around a haulier with a slipping ranking, and in the process revolutionized Japanese haulage. Finally, we studied Norio Ohga, the fifth

president of Sony. Full case studies describing the personal and professional history of these leaders are included in the Annex and they are the basis of the models and findings described throughout the book.

We have found two successful approaches to doing business. One centered on the essence of an image of the firm to pass judgment on new business endeavours, and what we called the proto-image of the firm – PIF. The second approach focuses on processing data through a mental model which enables identification of the levers to pull profit, what we called profit-arithmetic – PA. These two models are explained and compared with other well-known approaches and concepts in Chapter 2.

Chapters 3 and 4 are dedicated to an in-depth development of the two business approaches. Chapter 3 deals with the PIF and explain how it is shaped, its relationship with a firm's product evolution and diversification decisions. It is based on the leadership and managerial styles observed in Sony's Norio Ohga and Yamato's Masao Ogura.

Chapter 4 then focused on the operationalization of PA, and is based on the leadership and managerial styles of Nissan's Carlos Ghosn and Shin-Etsu's Chihiro Kanagawa.

In this final chapter, we proffer our conclusions by revisiting the six questions proposed in Chapter 1 and summarising emerging answers. Therefore, in the sections which follow we will try to answer those questions.

2. WHAT COMMON TRAITS DO THE SUCCESSFUL FIRMS POSSESS?

Courtney, Kirkland and Viguerie (1997) consider four levels of uncertainty: (1) level 1, a clear enough future; (2) level 2, alternative futures; (3) level 3, a range of futures; and (4) level 4, true ambiguity. In the past, uncertainty surrounding the business environment was level 1 where the future was clear enough. Managers could develop a forecast of the future precise enough for strategy development. Past experience, industry knowledge, network, which strings to pull, etc., were the most important elements of strategy. The key to operational effectiveness was cost reduction and continual improvement was key (Porter, 1996; Porter, Takeuchi and Sakakibara, 2000).

If uncertainty increases from levels 2 to 4, experience must become more of a hindrance than a help. Simple quantitative extrapolation may suggest one future direction, while reality may head in quite a different direction. Judgement on future courses of action can, at these uncertainty levels, be better made on the basis of intuition, a clear mental model which facilitates an easier reading of the situation.

Our four objective companies have, in addition to their operational

effectiveness, managerial skills which led them to decide which industry changes the company would respond to, and which customer needs the firm would work to fulfil. These companies have leaders, CEOs who make choices and guide their employees to make choices. All these firms have an outstanding 'transformational' CEO with an unambiguous understanding of the scope of their business. That is, they have a clear mental model guiding their decisions. These CEOs clearly have reversed how the firms had been managed. The four CEOs studied have shown both charismatic behavior and transformational leadership.

Promotion systems in Japan support operational excellence as being easier to evaluate than the more invisible, general management capability of assessing a situation correctly. Thus, operationally excellent managers, richly experienced, may have a better chance to reach their firm's top position. However, the four companies studied have broken the Japanese tradition of rewarding more operationally excellent middle managers with senior positions. Operational effectiveness as an internal promotion criterion does not apply to the business leaders we studied. As an example, Carlos Ghosn came to Nissan from another firm – Renault. Chihiro Kanagawa joined Shin-Etsu from another company – Kyokuto Bussan – and when appointed president of Shin-Etsu Chemical in 1990, he was CEO at Shintech. Surprisingly, Norio Ohga was a professional opera singer when he joined Sony and pursued both jobs in parallel for three years.

The interesting point is that our CEOs are against this Japanese tradition. To illustrate, Chihiro Kanagawa thinks sending managers with potential to subsidiaries as their top people serves nicely to nurture future leaders. This departs from traditional Japanese personnel policy where managers who had fallen out of competition for the top position used to be sent to subsidiaries (Maeda, 2002). Kanagawa maintains that even if sizes are different, running a firm is not qualitatively different between parent and subsidiary companies.

Operational excellence is predicated on knowledge of the accepted way of doing business in industry in general and the firm in particular. How they think in an industry and a firm is a product of many years' thinking of many people. Familiarity with this way of thinking helps to avoid wasting time unnecessarily in the thought process. It can have some unfortunate consequences. For example, a follower strategy has been the most common strategy in Japan. In fact Porter (Porter *et al.*, 2000) has gone further, arguing 'Japanese companies rarely have strategies', as they simply imitate, copying each other's strategy. However, when one faces an unprecedented situation, this does not help. A very new situation because of level 2 to 4 uncertainty requires more than simple rote learning of operations. It requires the ability to call into question accepted industry or company wisdom.

This capability is gained by having been outside the main business or by

having offshoot experience. Japan is a consensus-oriented country, and firms tend to compromise. This makes it hard to question accepted wisdom. Managers from outside the mainstream have had the chance to observe the firm from outside. They feel free to conduct business in different ways and can see inefficiencies unnoticed by those inside.

The four CEOs in our study never unconditionally accepted conventional wisdom or commonly held views. They constructed their own logic, using experience gained from peripheral departments or even another firm to avoid unconditional acceptance of accepted views. These business leaders' previous experience in subsidiaries, peripheral departments or other firms helped them to introduce these changes in their firms and avoid rigidity.

This means firms doing well, more often than not, have 'iconoclastic', maverick business leaders who break the mould which is accepted unquestioningly by 'insiders'.

Promotion and personnel systems in Japan need to be modified. Corporate cultures that shied away from mavericks must start to recognise their value. This will require the traditional methods of future leader selection to be modified drastically.

3. ARE THERE SOME DISTINCTIVELY DIFFERENT APPROACHES TO BUSINESS?

Our main conclusion is that these transformational CEOs are using two different cognitive approaches to guide their managerial actions and help them interpret the managerial task. One approach is profit-arithmetic and the other the proto-image of the firm. We obviously make no claims to completeness concerning the CEOs' cognitive approaches.

In our analysis we cited Niihara's (2000) study on excellent business leaders. He enumerated common features among them: (1) unambiguous understanding of the firm's scope of business; (2) logical thinking or theorisation; (3) offshoot experience; (4) capability to turn crises into chances, (5) investment and R&D within the generated cash flow; (6) discipline and shared belief.

These features are embodied in our business leaders' use of two different approaches to their businesses. Some of them cope with a changing business environment by interpreting and analysing it in terms of levers to make profit, while others stress more a longer time-frame and diversification; a new business domain, product, business activity, etc., are analysed in terms of their fit with the firm's image. We call the first the profit-arithmetic approach (PA), and the second the proto-image of the firm approach (PIF).

PIF is an idiosyncratic concept relying on the manager's mind. It is an

image, a proto-image of what their firm is, should be or what the manager wants it to be. PIF business leaders make sense of their situation by analyzing and contrasting it against their model. The fit with the proto-image of the firm is the starting point. When the CEO faces an investment opportunity, this decision is contrasted against their PIF. If the new investment matches or fits their PIF, then the investment occurs. By contrast, if the new business opportunity does not fit with the CEO's proto-image of the firm, the investment does not get approved.

PA is, like PIF, an idiosyncratic concept relying on the mind of an individual. CEOs with a PA approach guide their decision making not on the basis of their image of their firm, but on the possibility of making profit. Their mental model is more analytical and rational than the PIF. They base their decision making on their knowledge of the industry, of their firm's resources and capabilities, strengths and weaknesses or, sometimes, on their own 'sense for business'.

PA-type CEOs emphasise the identification of profit levers, focus on daily operations and show clear priority setting. CEOs with a PA approach focus their attention on everything which may enhance the firm's profit potentiality.

4. WHAT KINDS OF RESULTS ARE ACHIEVED BY THE DIFFERENT APPROACHES? IS ONE MORE SUCCESSFUL THAN THE OTHER?

Our conclusion is that different approaches achieve different kinds of results. These approaches derive from different business environments, business leaders' past experience and professional background, their beliefs, etc. However, we cannot state categorically whether one approach is better than the other.

The results achieved by the proto-image of the firm (PIF) and the profit-arithmetic (PA) approaches differ. Each approach favours certain time-frames, strategies, results, etc. Once the approach is in place, effective strategy boils down to a limited set of options. The fit with each approach is the essential criterion to decide on a strategy.

PIF leaders build their strategy around their image of the firm. New products and activities are chosen and developed; core competencies are fostered. The cases demonstrate new leaders are chosen when their predecessors believe the successors have understood and assimilated the proto-image of the firm.

While profit making is important for PIF leaders, if faced with a choice of a short-term profit or long-term capacity building and product development, PIF leaders will opt to sow future business chances.

This does not mean that PIF is better than PA. What it means is that PIF-type CEOs are more likely to lead a firm in a technology-driven industry where continual change in product portfolio and business domain is vital to the firm's survival.

However, there is no long term without short term. If the firm goes under, whatever longer-term vision you may have becomes meaningless. The PIF approach, therefore, presupposes that the firm does not face immediate and imminent financial problems. Sony's Ohga says to never forget each new product's contribution to the firm's profit and loss account. However, profit contribution is not the only decision criterion for him. There are others.

In contrast, PA-type leaders pay attention to shorter-term, operations-oriented decisions and their implementation. They build their strategy around actions with results visible in a shorter time-frame. They will not even consider anything which sounds a waste of time and money. Sometimes they are almost 'stingy' in spending as they prepare for a big decision at a critical juncture.

This is made possible by circumstances surrounding their industries. The industries can be technology-driven but their pace of technological change is less hectic. Their technology is established, it may change over time but can be predicted with some certainty. Their products can be commoditised. Many companies try to compete with 'me-too' products simply on the basis of price. Production overcapacity in these industries is fatal since it gluts the market. This means correctly reading market trends and market fluctuations in anticipation of competitors' moves is essential.

Diversification can help, but PA-type leaders know to be successful in a new business is more difficult than in their existing field. Familiarity with a business is key to success. A case of 'Better the devil you know than the devil you don't'. In addition, as CEOs are compensated for their contribution to profit they tend to stick to what they know best.

5. WHY DO THESE DIFFERENT APPROACHES EXIST? CAN THEY CO-EXIST IN THE SAME COMPANY?

Different approaches flow from different assumptions and circumstances. Different emphasis is put on the time–frame in conducting business. Business leaders have different approaches because their underlying assumptions about conducting a successful business come from different experiences, industry characteristics, etc. The difference in approach relates clearly to the business leader's personality, and is rooted in their belief system. Of course, organisational factors such as shared values also influence the successful adoption or failure of an approach.

The leader's belief system and accordingly the business situation determine whether the two different approaches can be enacted in a firm or not. We believe that the PIF approach can exist at the top level to accommodate a profit-arithmetic approach at lower levels. It remains to be researched, however, how this combination actually works. It is quite possible that PA is closer to operational effectiveness – clearly part of the Japanese way of doing business – while PIF is more 'abstract-conceptual', closer to 'strategic thinking' – a view often seen as absent from the Japanese way of doing business.

Commitment to both long-term strategy and short-term operations may seem paradoxical. It can be hard to see how the PA approach could be seen as strategic thinking. It may be a narrow view of the organization's needs, however, by concentrating on a few main issues (linked to profit levers), CEOs can marshal resources and support for their programs.

Once conditions change, CEOs must be flexible enough to reframe their thinking and provide their organizations with stimulating new ventures, new products, all fitting with the PIF.

We believe a PA-type CEO is not oblivious to long-range needs (PIF-type CEO), and vice versa. It is possible both cognitive approaches may be embraced in a leader's conceptual thinking and enacted according to the situation.

6. DO THE TWO DIFFERENT APPROACHES ADD VALUE TO BUSINESS? HOW?

The important issues, and important distinctions between business leaders, concern how business leaders add value to lower management.

Value creation by a business leader is central to any business. We assume variations in company performance in Japan (and globally) are due to business-leader value creation or subtraction (and the corporate center[1]).

The PIF approach excels in helping businesses take up strategies to build long-term competitive and corporate advantages. These advantages come from continual business domain and product portfolio renewal. This renewal encourages re-examination of assumptions on which the firm's past success was founded. This is important because assumptions vary over time and environments change. It is thought that a firm that succeeded in the past was capable of establishing a business model or a theory of the business based on these assumptions. However, because people are reluctant to part with the theory of the business, partly due to inertia and partly due to a lack of impetus to change, firms end up losing their competitive edge. The PIF approach avoids this pitfall.

The simplicity of messages deriving from the PA approach, in part by focusing on just profitability and its levers, harnesses staff and employee energy. Hence, employees will find it easier to buckle down on a few key profit levers as it is easier to prioritise them once they are identified. A good PA-type CEO would recognize how their personnel can contribute to the firm.

7. HOW CAN FIRMS CONTINUE THEIR SUCCESS EVEN IF THEIR LEADERSHIP CHANGES?

We make two suggestions. The first refers to the grooming of future business leaders, while the second relates to the duration of their appointment.

In the first place, we assume operationally effective managers, however excellent they might be, face a quantum leap in their understanding of the nature of strategy. Such a leap, if feasible, demands time, which means a systemic redesign of the current promotion or selection system is urgently needed.[2]

In the system currently operating in Japan, operationally efficient managers, more often than not, benefit from faster promotions. Based on anecdotal evidence, strategically minded managers may not be good at operations (e.g. sales), which means the system needs to be redesigned so that those with strategic potential can be identified and encouraged.

Being given that wider experience, including heading a subsidiary, exposes potential managers to general management sooner in their professional career. Secondments to subsidiaries or overseas branches are valuable in developing their leadership.

Secondly, according to Tanaka and Morishima's survey (2004) between 1960 and 2000 the average tenure of presidents in Japanse firms dropped from 15.6 years to 5.3 years. The implications of this are what Itami (1995) calls presidency in rotation (*shacho no post-ka*), and as shortening of tenure becomes established custom, this leads to incumbents and newly appointed presidents often accepting not to 'ruffle other people's feathers' by taking unusual initiatives. This signifies that presidents rotate in good order as if their positions are just one more career stage.

Rotational or perfunctory presidency differs from the ideal of a leader figure that steers the enterprise based on long-term strategy. Coupled with the trend of newly appointed presidents being on average 60.7 years old in 2000, in contrast to 53.3 years in 1960, shortening tenure jeopardises follow-through of their strategy, if any.

Breaking away from this trend may eliminate some ailments of Japanese firms such as lack of vitality, long-term vision, original thinking in strategy, etc.

To conclude, we have illustrated in this book how the two cognitive approaches (PIF and PA) influence how CEOs develop strategic thinking. In two cases we have observed how the PIF approach (1) shapes core image and company ideology, (2) guides company development, and (3) influences succession in some Japanese companies.

The PA approach is posited in this book to be shaped by the company's economic condition and its industry type. Companies in dire straits and a mature-industry environment enact a PA approach. Other elements of the PA approach are profit levers, resources and capabilities which can contribute to implementation of the levers.

Both approaches are active, information-seeking structures directing actions. These approaches encode experiences with cause–effect relationships, which can be used later to make causal inferences.

8. FINAL THOUGHTS

As usual in an exploratory study, we have left more questions unanswered than answered. For example, we have shown how business leaders use each approach. It would be interesting to determine if a manager can shift from one approach to the other and, if it can, how it takes place for one leader. In our cases Nissan's Carlos Ghosn seems to be shifting from the profit-arithmetic to the proto-image of the firm approach. So we wonder, how does this change take place? Is there a connection between these models, which given certain stimuli, triggers the change? If the shift takes place as a consequence of a change in a mental model it would be interesting to investigate how these mental models change. Furthermore, it may also be of interest to determine to what extent these mental approaches can be replicated and how much they depend on the leader's personality. Future research should cast light on these points.

We should also like to determine if the replication of one style is easier than the other, or whether it is difficult to replicate any of them since they depend on the leader's personality. From the resource-based view of the firm (Barney, 1991; Peteraf, 1993), leaders provide more than the capability for resource integration. Capability uses two mechanisms to integrate employee knowledge and skills with capital equipment, technology and other resources both tangible and intangible – rules and directives, and organisational routines (Grant, 2002). Leaders' capability as our cases show goes beyond this role. We differ from this collectively shared capability and refer to more person-specific capability. Therefore, the replication that concerns us is not about developing rules and directives or routines, but rather about how to 'clone' leaders and their capability to manage. There will not be a single answer to

this. However, it is important to systematise succession, and any direction on this, no matter how tenuous, will help.

NOTES

1. The center of a diversified company is, in a sense, an intermediary between the business unit and the capital markets. To exist, it must outperform capital markets: its 'net' added value must be greater than its cost (Goold and Campbell, 1987). As to the mechanisms for corporate coherence used by the centre, see Collis and Montgomery (1997, 1998).
2. Mishina (2004) identified the trend to CEOs becoming more functional managers than strategists. One reason he advances is that the selection and promotion system of managers is based on the judgement of whether they have done well in their previous position and whether they will comply with the requirements of the next new position. This means that promotion criteria are constrained to the performance in specific positions without taking into account whether the person is of general management calibre.

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Annex: Four case studies

A1. Nissan: the Ghosn era

INTRODUCTION

Grant and Neupert (1999) summarised automotive industry trends as follows:

1. Technological and design convergence: cars look more alike. Front-wheel drive and disc anti-lock brakes, suspension, and steering systems are more standardised. Body shapes are increasingly similar.
2. Market segmentation in different countries is growing more consistent: (1) luxury; (2) sport-utility; (3) passenger minivan; (4) mid-size family sedans; (5) subcompacts; etc. The relative size of the segments varies between countries.
3. All major car manufacturers have adopted Toyota's lean production system. Increased flexibility lowers minimum efficiency levels. So, average plant size is 150 000–300 000 units a year.
4. New product development cost increases mean smaller producers become cost-uncompetitive. This means new product development is a critical differentiating organisational capability.
5. Development and supply of sophisticated subassemblies (transmissions, braking systems, and electrical and electronic equipment) increase component manufacturer negotiating power.
6. Cost reduction, driven by increasing competition, is a key success factor. Outsourcing, JIT scheduling, automation, use of low-cost locations, etc., are intensely sought.
7. Excess global capacity: capacity utilisation was around 70 per cent in the US and Western Europe in 1998 against 60 per cent in Asia.
8. Internationalisation: through trade and foreign direct investment the global car market is dominated by US, Japanese and European large car makers.

In this scenario, a shock wave spread in the automotive world in March 1999 at the announcement that France's Renault would take a controlling stake in Japan's Nissan. It was a symbolic event heralding the end of an age when Japanese companies singled themselves out as a unique force in competition with the world powers.

Why did Nissan have to seek collaboration with Renault? What happened

to the Japanese management which served as a model to follow during the 1970s and 1980s with the world learning Japanese management techniques such as the just-in-time system, quality circles and target costing?

INTERNAL AND EXTERNAL FACTORS IN THE CRISIS OF JAPANESE MANAGEMENT

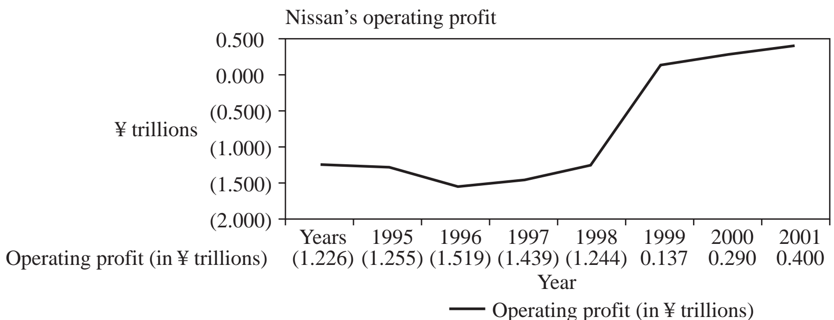
One of the main factors deeply affecting Nissan was the bursting of the bubble economy, which grew from credit expansion and excessive liquidity, based on land price speculation in the 1990s. Japan's financial industry was destabilized as a result. Bankruptcy of Sanyo Securities, Hokkaido Takushoku Bank, Yamaichi Securities, etc., ensued in 1997 and 1998, resulting in a credit crunch.

Nissan's performance during these years was disappointing (see Figure A1.1). Until financial year 1998 it suffered losses for six quarters in a row. What is worse, its consolidated interest-bearing net automotive debts amounted to ¥2.1 trillion as of end-March 1999.

Nissan was in acute need of liquidity to meet both its own requirements and requests from its subsidiaries from which banks had started to withdraw credit. Industrial Bank of Japan (IBJ) and Fuji Bank, Nissan's main banks, were themselves in dire financial straits and could not lend a helping hand to Nissan.

Nissan had only two alternatives left to overcome the situation: (1) float bonds or (2) seek an alliance with a foreign auto maker.

Nissan was actually excluded from the first alternative. The huge debt burden piled on its balance sheet and poor performance meant Nissan's classification was believed to be cut to the junk level[1] for floating long-term



Source: Based on Gold, Hirano and Yokoyama (2001, p. 103) and Toyo Keizai (2002), *Kaisha Shikiho*

Figure A1.1 Nissan's operational profit

bonds and commercial papers. This made it prohibitively expensive for Nissan to resort to this alternative.[2]

Nissan's only option was to find a foreign partner. Ford's CEO, Jack Nasser immediately declared in unambiguous terms that a tie-up was a non-starter for them. Nissan started to negotiate with Daimler Chrysler, however Nissan's eventual rescuer was unexpected, France's Renault.

RENAULT JOINING FORCES WITH NISSAN

In 1997, the European market was central to Renault's revenues, representing 85 per cent of total sales, a third of which came from France (Ghosn, 2001). In the same year Renault's global market share was 4 per cent.

Daimler's merger with Chrysler, announced in May 1998, convinced Renault that to survive it needed a partner. It was too small to compete on the world stage, and being limited to the European market, handicapped (see table A1.1 for a comparison of the top five global automotive groups including Renault-Nissan).

Renault had left no stone unturned. In 1980 it acquired a 46 per cent stake in American Motors Co. (AMC), but had to dispose of AMC's shares later, due to its lack of financial ability to help boost AMC's operations.

In 1992 Renault initiated merger talks with Sweden's Volvo. If the merger had occurred, it would have created the world's sixth largest car maker. The combination was perfect. Renault was strong in southern Europe, while Volvo's stronghold was northern Europe. The latter specialised in large deluxe sedans, while the former excelled in the compact car segments.

Schweitzer cited by Ghosn (2002, p. 37) reminisced:

> Normally the French Government did not intervene in Renault's day-to-day management, but in the case of the merger with Volvo it was up to the shareholder to decide. The Government could not take a quick action. It was very cautious. It was concerned about its political consequences.

The French government's intervention turned public opinion in Sweden against the merger, forcing Volvo's top management to resign. The new management stopped merger talks with Renault.

The French government's concern stemmed from Volvo's poor performance. Renault reported US$1 billion profits, while Volvo's sales had experienced a sharp fall in its domestic market.

Renault reviewed associations with BMW, Korean car makers, Nissan, Mitsubishi, etc. Peugeot Citroën had been rejected as a merger partner, while Fiat was seen as a poor fit with Renault (Ghosn, 2001).

Ultimately, Nissan surfaced as a possible partner. It was a global company,

Table A1.1 Comparison of global automotive groups

Group	Main automakers	Consolidated turnover ($ billions)	Cars sold world-wide (million units)	Market capitalisation ($ billions)
Toyota	Toyota, Daihatsu, Hino	111	5.2	107.6
Daimler Chrysler	Daimler Chrysler	155	4.5	88.6
Ford Motor (US)	Ford, Mazda (Japan), Volvo (Sweden)	174	8.2	69.1
General Motors (US)	GM, Isuzu (Japan), Opel (Germany)	173	9.8	64.6
Renault-Nissan	Renault, Nissan	97	4.8	18

Source: Based on Nikkei Business (2000, p. 229)

with strong Asian and US market bases where Renault had no presence. Both Renault and Nissan were not top-ranked global players, but in combination, they could be a force to be reckoned with (Ghosn, 2001).

In March 1999 Nissan's Daimler Chrysler merger talks collapsed. Two weeks later, Yoshikazu Hanawa, Nissan's CEO, and Louis Schweitzer, his Renault counterpart, signed a global alliance agreement. Renault would acquire a 36.8 per cent stake in Nissan for US$5.4bn (¥643bn). The original agreement stipulated that Renault could increase its stake to 44.4 per cent, while Nissan could take a stake in Renault.

The agreement included appointment of a COO (chief operating officer) by Renault to take charge of Nissan's restructuring. CEO Hanawa would manage external relations including those with the government. He would be also in charge of alliance matters with Renault. The COO meanwhile would concentrate on internal activities and operations.

Carlos Ghosn, Renault's number two, was chosen as COO by Louis Schweitzer. Hanawa also saw him as an appropriate COO.

CARLOS GHOSN: YEARS OF FORMATION

Carlos Ghosn was born on 9 March 1954 in Porto Bello, Brazil, of parents of Lebanese origin (Ghosn, 2001). When he was six, the family decided to

educate him in Lebanon, so Carlos, his mother, and his other siblings moved to Lebanon.

After studying at a Jesuit high school where the language of instruction was French, Carlos applied and was accepted for the French élite school, L'Ecole Polytechnique in Paris. The school belonged to the French Army and students were paid salary during their stay.

Although educated in English as well at the Jesuit high school, Carlos's main languages were French, Arabic and Portuguese.

After the Polytechnique, Carlos entered L'Ecole des Mines, another 'grande école' in the French education system. Before graduation Carlos considered proceeding to an MSc or PhD programme in economics. However, close to graduation Michelin, the French tyre maker approached him in 1978.

Michelin planned a large construction project, tyre and steel cable plants in Brazil and wanted an engineer educated in a French university and who spoke Portuguese.

Michelin offered to send Carlos to Michelin's R&D technical center after the basic orientation period. This was clearly an élite track for an engineer. To the surprise of Michelin's management, Carlos asked to be assigned to the manufacturing division. He thought it would be the best place to see how plant operators, engineers, supervisors, managers and other people worked and to understand larger company problems.

Carlos joined the firm in September 1978, and was assigned to La Puy Plant near Clermont Ferrand, Michelin's hometown. During this stage at La Puy, Carlos became keenly aware of the fact that management tend not to understand that employees want to develop. After a year he was appointed director of La Puy Plant. Carlos was 26 years old and had 700 operators under his supervision.

After appointment in 1984 as director of the R&D center for large car tyres, Carlos was transferred to Brazil as COO of Michelin's South American operations, reporting directly to François Michelin, the firm's CEO. It was 1985 and Carlos was 30 years old.

CARLOS'S BRAZIL YEARS

Michelin's Brazilian tyre plant was commissioned in 1981, in an unstable business environment, with an annual inflation rate of 1000 per cent. Despite a personnel manager's opposition based on Carlos's young age, François decided to send Carlos.

Carlos had three points in his favour: his age which meant he was less concerned with risk, his personal experience of Brazil's hyperinflation, and his command of the Portuguese language (Ghosn, 2001).

Upon arrival, Carlos Ghosn gave priority to two issues: (1) definition of the problems and (2) prioritising them.

Problems were identified and grouped as follows:

1. reduce debt by selling non-core assets. Eliminate inventory and product in progress
2. consult with the government to adjust prices once every month
3. ask dealers to pay Michelin at the moment of product delivery instead of the 30th, 60th day, etc.
4. maintain labour cost control through a monthly adjustment and consultation with labour union representatives.

Michelin Brazil attempted real-time measurement of the situation since, with monthly inflation of 30 per cent, firms could be losing money while believing to the contrary.

Carlos did everything within his reach. Inventory management, timely importation of raw materials, renegotiation of payment conditions, product price adjustment, production improvement, quality control, negotiation with work unions, improving employee motivation, etc., were studied and attempted.

Following his belief in the importance of communication, Carlos walked around the plants whenever possible, discussed and exchanged opinions with salespeople, factory workers, dealers, etc. Hyperinflation, high interest rates, frequent contact with governmental officials for regular price adjustment, and avoidance of governmental micromanagement were his concerns.

Michelin Brazil's performance improved. While losses were reported in both 1985 and 1986, profits flowed in the following year.

CARLOS'S US DAYS

In 1989 François Michelin transferred Carlos Ghosn to the United States to head its North American operations. The main task he faced was the merger with Uniroyal Goodrich.

While Carlos directly reported to François as in Brazil, due to Michelin US's size (representing 35 per cent of Michelin Group sales), he felt he was watched and interfered with by corporate headquarters.

Acquisition of Uniroyal Goodrich was agreed in 1990, to serve as Michelin's US penetration strategy. Nevertheless, the Michelin Group during the 1990 recession lost money and over the following three years losses totalled US$1850 million.

The two companies' cultures differed. Michelin was a family company

based in France, which set store by products, technology and quality. Long-term objectives were given maximum priority. In case of losses, owners or managing partners supported the company with their personal patrimony. This meant managing partners had more say in management than general shareholders.

Uniroyal Goodrich typically attached more importance to short-term profit. R&D spendings were controlled to benefit short-term earnings.

In the 1990s recession former Uniroyal Goodrich people insisted on concentrating on sales of replacement tyres for individual consumers on the basis of greater profitability, where Michelin people emphasised development of tyres supplied to auto makers under OEM (Original Equipment Manufacturer) contracts. For Michelin an OEM operation led to longer-term brand consolidation.

Carlos learnt neither French nor US styles of management were superior to each other, but that the combination was more powerful. Michelin could focus on short-term profit, introducing performance-related bonus payments as an incentive. Uniroyal Goodrich's problem resulted from a lack of due consideration for long-term strategy and R&D.

The new head decided to create a unified organisation by giving the central management team decision-making authority over important issues including overall company policy and objectives.

The management team faced two key issues: mapping out of marketing and sales strategies and overall restructuring.

Regarding marketing and sales, Michelin had to switch from a single-brand policy to a multi-brand policy. While Michelin had only its homonymous brand, Uniroyal Goodrich had Uniroyal, BF Goodrich, and private brands, etc. Positioning of each brand, sales, pricing, distribution channels, etc., needed decisions.

Management decided to unify sales of all brands and a team was assigned to each distribution channel such as volume sales, independent dealers, etc.

The second key issue was addressed by organising a cross-functional team (CFT) to overcome the partisan reactions of initial functional teams. CFT highlighted different issues from different functional angles. Excessive production specification was one issue resolved by discussion among R&D, marketing and production.

In 1994 Michelin Group reported US$247 million net profit. The end of the recession, cost reductions, and success in the multi-brand strategy all helped.

Carlos was then headhunted by Renault in October 1996 and was appointed vice president in December. Renault lost US$1 billion that year. As executive vice president in charge of R&D, purchase, manufacturing, engineering and product planning, cost reduction was Carlos's responsibility.

The new vice president announced cost cuts of US$2.4 billion over three

years. People were sceptical because of Carlos's inexperience in the auto industry, but he was optimistic, believing that visible progress would convince people of the value of these drastic measures. Cost cutting involved eliminating excessive production capacity, introduction of product engineering to speed development of new models, reducing suppliers from 300 to 150, reducing main platforms from five to three, and accelerating product innovation.

Renault's CEO, Louis Schweitzer fully supported Carlos's initiative. CFT was introduced. Plants were closed. Renault came out of the red in 1998.

GHOSN LANDS AT NISSAN

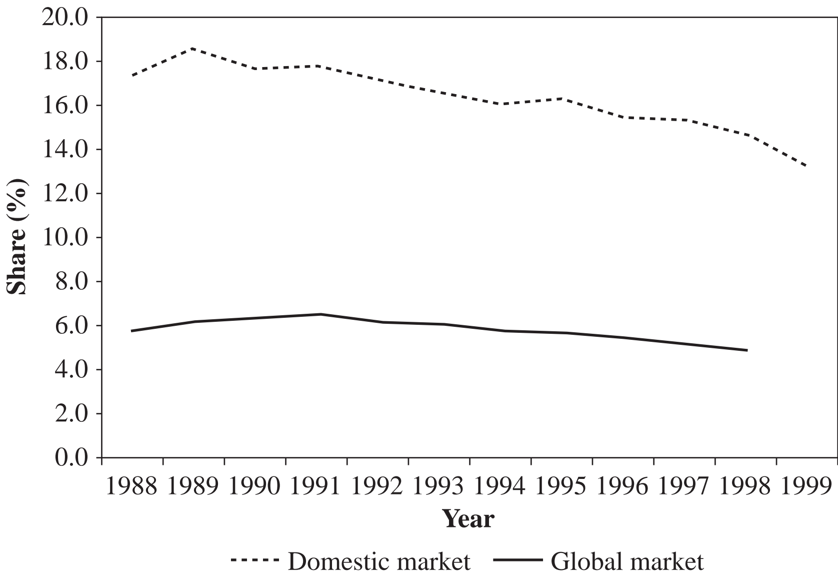
Carlos recalled the day when he arrived at Nissan:

> I don't know how I should express my feeling when I took charge of the post as Nissan's COO. Déjà vu? Synchronicity? Or was it a trick of my imagination? I could not get away from the impression that I was here before.
>
> 'Here' does not mean the 'place' but the 'situation'. Lack of profitability, excessive penchant to market share, chaos, blurred responsibility. There were numerous problems. However, all these problems were familiar to me. I sat in my office and thought as follows.
>
> 'What I have done so far was for me to get trained and prepared for this moment. The restructuring, reorganization, transformation of the employees' mind-set, merger of two different cultures, and cross-cultural management. If I don't look at the difference in the dimension, I have done all these things.' (Ghosn, Rivas-Micoud and Carvell, 2001, pp. 155–6)

When Carlos Ghosn arrived, Nissan was strapped for cash, and could not make needed product line investments. Excessive capacity, currency appreciation, emptying-out of production bases to overseas countries, etc., were given as causes of Nissan's trouble.

Carlos had a different opinion. For him external circumstances such as recessions and market fluctuation could not explain why other auto makers including Toyota and Honda were doing well in contrast to Nissan's poor performance. He concluded the difference was due to management capability.[3] Nissan's management, opined Carlos, had lost its bearing and failed to take measures needed to make profit a priority. No clear long-term vision was offered to the employees.

Carlos Ghosn identified two key problems (Ghosn, 2001). Nissan's market share had been in continuous decline for eight consecutive years globally and 28 years in the Japanese market (see Figure A1.2). The attendant and second



Source: Based on Gold, Hirano and Yokoyama (2001, p. 97)

Figure A1.2 Nissan's market share

problem was its dismal performance devoid of profit.

Nissan's new COO attributed these problems to five causes. First, lack of focus on profitability. Second, lack of focus on consumers. Third, no collaboration pursued joint tasks across functions and departmental boundaries. Fourth, no shared sense of crisis among its employees. Fifth, no shared common vision of Nissan's future.

In concrete terms, Nissan's margins were low because its brand image was poor (Ghosn, 2002). Nissan's purchasing costs were 15 to 25 per cent above Renault's. Plant capacity exceeded sales by a million cars a year, and company debts were US$11 billion.

In spite of its cash shortage, Nissan had capital locked up in non-core financial and real-estate investments, especially in *keiretsu* partnerships. The money, use of which was suboptimal, was estimated at US$4 billion. Nissan's problem was that the majority of these investments in shareholdings were too small for them to have any influence in the companies. A case in point was the shareholding in Fuji Heavy Industries, manufacturer of Subaru cars. Despite its 4 per cent stake valued at ¥26 billion, Nissan was not informed beforehand when Fuji started negotiations with General Motors.

During this period, Carlos confirmed his suspicions that Nissan's operations

were disjointed (Ghosn, 2002). For instance, a director in charge of manufacturing explained to him about productivity gains, but they did not know if there had been an improvement in total cost. Purchase cost was the purchase department's responsibility, and fell outside the manufacturing department's domain.

Carlos discovered priority setting at Nissan was chaotic.[4] The company had been trying to cut overheads, especially in personnel and communications. For overseas business travel a ban was imposed on using business-class seats. Paper and office materials were restricted, and air conditioning was turned off after hours. For the new COO these efforts missed the mark. He was convinced these saving efforts only served to punish personnel and did not impact the real cause of Nissan's ailments.

The area which needed immediate attention formed a high percentage of the profit and loss account, in some cases as much as 60 per cent of the total cost. It was there that management attention should be directed.

The prevailing view was, as Nissan had an equity stake in many suppliers, they would do their best to offer best price and appropriate quality. Carlos decided to separate shareholding and purchaser–supplier relations. He knew even if shareholdings were sold to release capital, suppliers would make a clear distinction between Nissan as customer and Nissan as shareholder (Ghosn, 2002).

Another example of poor priority setting lay in product development. As cash was short, new model development was postponed. Nissan's March model was not renewed for nine years when passenger car models are generally renewed every five to six years. No renewal meant declining sales.

To establish the right priority, Carlos believed in two things. First of all, planning must be centralized, and, second, responsibility must be clearly defined and assigned.

Nissan's COO discovered that his staff had many ideas to help Nissan overcome their difficulties. Eventually, no outside consultants were needed. The advantage was that staff-drafted plans are more acceptable to all concerned.

Thus cross functional teams (CFT) was created. Carlos strongly believed (1) it was important to meet customers' requirements, (2) customers' requirement tend to be 'interdisciplinary', and (3) opinions from different fields must be considered to improve on cost, quality, and lead and delivery time. CFT can bring all members' different perspectives to bear on the issue.

> CFT tends to seek change, contrary to incumbent management members. CFT therefore needs to be filled up with intelligent and change-making personnel. If CFT is too strong it will be jeopardised by management. On the contrary, if

> management is too interfering, CFT will lose interest in pursuing change. So, striking a balance between these two forces is the key to the success of CFT. (Ghosn *et al*., 2001, p. 173)

Within a month of Carlos's arrival, nine CFTs were set up to cover business development, purchasing, manufacturing and logistics, research and development, sales and marketing, general and administrative, finance and cost, phase-out of products and parts complexity management, and organisation areas (see Table A1.2).

To ensure the workability of CFTs the number of members was limited to ten per team. In order for a team to obtain knowledge depth, each CFT formed a set of approximately ten-member subteams. Altogether some 500 people worked across CFTs and subteams. Some 2000 proposals were submitted by CFTs as well as by other staff not belonging to CFTs between 1 July and 18 October 1997.

Authority was vested in CFTs through appointment of two leaders (executive vice presidents) from the executive committee. Between the two leaders a narrow focus was avoided by CFT and they helped the organisation sell ideas developed by CFTs. There was one pilot for each CFT, who was selected by leaders and Carlos Ghosn. CFT members had to sign a confidentiality agreement on information handled by them. No issues were to be disclosed outside CFTs.

> It was also important that the CFT process not look like a corporate-imposed blaming exercise. The team leaders, therefore, took a back seat in the actual operation … one of (the remaining nine) acted as team's pilot, taking responsibility for driving the agenda and discussions. The pilots were selected by the executive committee, and the leaders and pilots together selected the rest of the team. Typically, they were managers who had front-line experience … I took a personal interest in their selection … to have a close look at the next generation … (Ghosn, 2002, p. 42)

CFTs common goals were development of a plan targeted at business development, profitability improvement, and cost reduction. CFTs did not have to take any action other than submit a proposal to be studied and deliberated by the executive committee.

Based on the CFTs' proposals, Nissan publicised its Nissan Revival Plan (NRP) around the time of the 1999 Tokyo Motor Show. The NRP (financial year 2000 through financial year 2002), announced two days before the opening of the Tokyo Motor Show, targeted the following goals:

Commitment

1. become profitable by 31 March 2001

Table A1.2 Nissan: CFT objectives

CFT	Focus	Objectives
Business development	Profitable growth, new product opportunities, brand identity, product lead time	Launch 22 new models by 2002, introduce a mini-car by 2003 in Japan
Purchasing	Supplier relationships, product standards	Cut number of suppliers by half, reduce cost by 20% over 3 years
Manufacturing and logistics	Manufacturing efficiency, cost effectiveness	Close 3 assembly plants in Japan, close 2 power-train plants in Japan, improve capacity utilisation from 53% in 1999 to 82% in 2002
R&D	R&D capacity	Move to globally integrated organisation, increase output efficiency by 20% per project
Sales and Marketing	Advertising structure, distribution structure, dealer organisation, incentives	Move to single global advertising agency, reduce SG&A by 20%, reduce distribution subsidiaries by 20% in Japan, close 10% of retail outlets in Japan, create common back office
General and Administration	Fixed overheads	Reduce SG&A by 20%, reduce global headcount by 21000
Finance and Cost	Shareholding and other noncore planning structure, working capital	Dispose of noncore assets, cut automotive debt in half to $5.8 bn. net, reduce inventories
Phaseout products and parts	Manufacturing efficiency and cost effectiveness	Reduce number of plants in Japan from 7 to 4 by 2002, reduce number of platforms in Japan from 24 to 15 by 2002, reduce by 50% the variation in parts for each model
Organisation	Organisation structure, employee incentive and pay packages	Create a worldwide corporation headquarters, create regional management committee, implement performance oriented compensation and bonus packages

Source: Based on Ghosn (2002, pp. 40-41)

2. reach 4.5 per cent operating margin on sales by 31 March 2003
3. reduce net automotive debt from ¥14000 billion to ¥700 billion.

Main restructuring measures

1. reduce staff from 148000 to 127000, cut by 14 per cent by 31 March 2003
2. cut production capacity by 30 per cent by closing three assembly plants and two power-train plants and reducing the number of platforms from 24 to 15 by 31 March 2002
3. reduce purchase cost by 20 per cent and suppliers from 1145 to 600 by 31 March 2002.
4. sell off shareholdings of non-core subsidiaries and assets
5. increase annual investment from ¥210 billion to ¥310 billion.

Carlos Ghosn staked his continuing as COO on fulfilment of NRP. He promised the audience he and his management team would resign if Nissan could not come out of the red in financial year 2000 (Gold *et al.*, 2001).

He was aware eliminating excess capacity would mean severe human sacrifices for employees whose work places were to be closed and who were to be transferred to other locations. Nonetheless, despite Nissan's plants often enjoying high productivity, even being benchmarked by rival firms, such as the Sunderland plant in the United Kingdom, the difficulty is that high productivity does not necessarily mean high cost efficiency nor operational efficiency, in so far as Nissan's fixed manufacturing structure costs were 50 per cent. Nissan's overall capacity utilization was only 50 per cent in Japan in financial year 1999. So a drastic capacity reduction was vital for Nissan's survival.[5]

Apart from cutting costs, the NRP planned to launch 22 new models by 2002. Bluebird, X-Trail, Primera, Cima, Caravan, Skyline, and Stagea would change models.

THENCEFORWARD

On the day following the announcement of the NRP, Nissan held a conference with its suppliers at a hotel in Tokyo. It was revealed that 60 per cent of the cost of goods sold at Nissan corresponded to materials and components purchase. Accordingly, the revival plan targeted cost cutting by ¥1 trillion by financial year 2002, of which 60 per cent would correspond to material purchase (28 per cent to sales and general administrative expenses, 10 per cent to production, and 2 per cent to others).

Component suppliers were a mainstay for Japanese auto makers. Many

thought Nissan had managed to launch many new models thanks to their technical collaboration. Yoichiro Kaizaki, president of Bridgestone, for one, expressed his doubt about how feasible was reducing supplier numbers (Nikkei Business, 2000). Nissan launched an initiative named Quality 3,3,3 to improve on product attractiveness, product quality, and sales and service (Takahashi, Hosoda and Kodaira, 2001).

More often than not high purchase costs were due to excessive specification. Nissan had tended to require unnecessarily demanding performance. Ghosn appointed a 300-member team independent of the purchase department to review component specifications.

Nissan changed traditional Japanese business etiquette by breaking away from the tradition of buying steel from all five blast-furnace steel mills in a more or less balanced way (25 per cent each from Nippon Steel, Kawasaki Steel, and NKK, and the remainder from Sumitomo Metal and Kobe Steel). Now Nissan would buy 60 per cent of its steel from Nippon Steel, 30 per cent from Kawasaki Steel, and 10 per cent from NKK. The former two mills would offer better prices thanks to economies of scale. This clearly marked a departure from the tradition of working with a *keiretsu* company when we consider the fact that NKK, which belonged to the Fuji Bank group (Fuyo group), as did Nissan, did not enjoy privileged treatment.

Kansei, a supplier of electronic control devices, tachometers, instrument panels, etc., decided to face reality by developing as best it could to meet Nissan's needs. Sales to Nissan formed 80 per cent of its total revenue. Nissan and Kansei executives and engineers held discussions spending several days meeting at hotels to find a way to cut costs. Kansei merged with Calsonic, a supplier of airconditioners and radiators, even taking advantage of the Nissan-Renault relationship to send a mission to Paris to sell its components, searching for economies of scale.

The tie-up with Renault contributed to Nissan an essential element for management: human resources. The traditional Japanese life-time employment system tended to foster managers good at implementing strategy but to quash the creativity of mavericks. In a continually changing environment, business acumen based on creativity was more in demand, but the Japanese system suffered from sclerosis in this regard. The arrival of Carlos Ghosn was more than welcome for Nissan's CEO, Yoshikazu Hanawa. Unlike Japanese practice in which there is no mechanism to train staff in general management skills (Ito, 2001), Carlos had undergone from an early career stage appropriate training as head of Michelin Brazil and Michelin US, and number two of Renault in truly international environments.

Nissan and Renault established the Global Alliance Committee (GAC) in which executive committee members of both companies participate to discuss medium- and long-term strategy and share purchase and information systems.

On 30 October 2001, Nissan and Renault decided to cross-hold their shares.[6] By virtue of the initial agreement Renault would increase its stake in Nissan to 44.4 per cent, up from 36.8 per cent. Nissan would acquire a 15 per cent stake in Renault by subscribing newly issued shares for ¥150 billion. Renault would exercise its option in warrants, spending ¥216 billion. On the surface there would be an outflow of ¥70 billion-worth of cash to Nissan. However, the fact was that the warrant exercise price had been fixed at ¥400, which would yield Renault a ¥82 plus billion-worth profit vis-à-vis the share price of about ¥550. What was more, Nissan's stake in Renault would not be given voting rights. The setting up of Renault Nissan BV was announced on 30 October 2001.

Fortune magazine cited a financial analyst's concern: 'Nissan can't rely on restructuring for ever. There's no question it can't afford to fail with this model' (Taylor, 2002, p. 36). In 2001 Nissan's market share in Japan was just 18 per cent. The March, the first Nissan car to share a platform with Renault, was launched on 5 March 2002. The original monthly sales target was 8000, however by the end of April there were 55 000 orders. Nissan's plan for new model launches is summarised in Table A1.3.

Nissan chalked up ¥489.2 billion as consolidated operational profit in financial year 2001, which was a 68 per cent rise compared to the previous year. Consolidated net sales were ¥6196.2 billion, a 1.8 per cent increase on the previous year.[7] Nissan's global vehicle, passenger car and light commercial vehicle (LCV) sales in financial year 2001 were 2 597 000 units compared with 2 633 000 units in the previous year.

At the presentation of the 2001 financial statements, Nissan's executive committee announced each of the three NRP commitments had been met, one full year ahead of schedule.[8]

Table A1.3 Nissan: plan for new models after 2002

Europe	Japan	US
Primera	Moco	Z-Car
LCV	Elgrand	Murano
	Z-Car	FX45
	Cube	Maxima
	Sedan	G35 Coupe
	Coupe	M45

Source: Nissan's Financial Year 2001 financial results preview: Nissan Revival Plan review and Nissan 180 presentation

Nissan attributed this performance to several factors, including:

- slashed purchasing costs
- reduced capacity and improved productivity leading to greatly enhanced manufacturing efficiency
- thoroughly revamped domestic sales system which reduced sales and administrative costs, and increased efficiency
- world-wide staffing changed in accordance with needs
- non-core assets sold
- increased R&D efficiency
- new Nissan model line gaining global market share.

In early 2002, the NRP was superseded by Plan 180 centred on growth, profitability and debt reduction. Here, *1* stands for the sales increase by 1 million cars by financial year 2004 relative to 2001 figures, *8* for the 8 per cent ROS by financial year 2004, and *0* for zero debt by the end of 2004.

These goals were to be attained by:

- increasing revenue generation
- reducing costs
- increasing both quality and speed
- maximising the alliance with Renault.

Nissan would increase new-vehicle launch frequency. Nine new models were released during the NRP. In financial year 2002 alone, 12 all-new products were to be launched globally. Over the Nissan 180 period, a minimum 28 new models were scheduled to be released.[9]

At the 104th Ordinary General Meeting of Shareholders on 19 June 2003 Carlos Ghosn, president and CEO, reported on their achievement in financial year 2002 ended March.[10]

- In the first year of Plan 180, Nissan achieved two of the plan's three commitments – 8 per cent operating margin, and zero net automotive debt
- Nissan's consolidated operating profit rose 50.7 per cent from financial year 2001 to a record ¥737.2 billion. Operating profit margin was 10.8 per cent
- Nissan's net automotive debt was totally eliminated to be ¥8.6 billion cash-positive at the end of financial year 2002
- Nissan sold 2771000 vehicles globally, up 6.7 per cent from financial

year 2001. With 12 all-new models, Nissan sales in Japan rose 14.3 per cent to 816000 units. Nissan's market share rose to 19 per cent, 1.1 points above financial year 2001.

NOTES

1. Standard & Poors (S&P) lowered Nissan's classification to BBB from BBB+ in 1995. The junk bond (for example, BB in S&P) means the company is in crisis and the bonds may entirely lose their value.
2. Other solutions such as a rights issue or a convertible issue were considered unachievable. One reason could have been that Nissan and its main banks deemed it impractical for a firm with such structural problems to count on subscribers to new issues. Another could be that the banks and existing shareholders shied away from dilution.
3. 'In 1995 … the labour cost per car was ¥200000 compared with Toyota's ¥140000. On paper (Nissan) had 15000 people in excess if it wanted to lower its cost to Toyota's level,' (Kai, s.d. p.27).
4. According to Kai (s.d.), President Tsuji who took charge in 1992 launched a mid-term plan for Nissan's restructuring in 1993. It included cost cutting by ¥200 billion, the closure of the Zama Plant (all personnel were offered a transfer), reduction of personnel (from 53000 to 48000), the despatch of 2500 people to dealers for their support, debt reduction by ¥1 trillion. Despite these efforts another cost-cutting plan was started in financial year 1995.
5. According to Nikkei Business (2000) Nissan's production capacity with two shifts was 2.4 million cars a year at that moment. Viewed against this, the financial year 1999 production forecast at 1.28 million signified only 50 per cent utilization.
6. According to Renault's Annual Report 2002, on 1 March 2002 Renault increased its equity stake in Nissan from 36.8 per cent to 44.4 per cent. Nissan Finance Co. Ltd., a wholly owned Nissan subsidiary, acquired 15 per cent of Renault's capital through capital increases on 29 March and 28 May 2002. Nissan Finance cannot exercise voting rights attached to these shares. The French government reduced its stake in Renault to 25.9 per cent. In addition, each company reinforced its presence on the other's board of directors. The number of Renault directors on the Nissan board was increased to four of nine. An additional Nissan director was appointed to the Renault board of directors, giving Nissan two of 17 seats.
7. Nissan press release dated 20 May 2002.
8. Renault Annual Report 2002.
9. Renault's Annual Report 2002.
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A2. Home delivery service (*Takkyubin*): Masao Ogura's haulage revolution

INTRODUCTION

The haulage world in Japan has seen a sea change over the last 30 years. Nobody carries skis or golf bags when they travel to a ski slope or a golf club. Travelers by the *Shinkansen* (the bullet train) comfortably move around without luggage as they have sent it to their destination beforehand by a home delivery service such as Yamato Transport's *Takkyubin* service.

Yamato, the inventor or innovator of this new haulage system, had a 45 per cent market share in 1996 with 640 million parcels handled (Kon, 1997). In 1997, its market share shrunk to 44.6 per cent but it was still a leader in the home delivery service, followed by Pelican's (Nippon Express) 25.2 per cent and Footwork's (Zen Nihon Ryutsu) 9.1 per cent (Yanagihara, 1997).

This haulage revolution was the brain-child of Masao Ogura, the president of Yamato between 1971 and 1987. This case addresses the question of how one man could turn around a haulier which had been slipping in the rankings and bring about a haulage revolution which changed how Japanese travel inside the country. The next-day delivery service covers almost all of Japan, enabling high-value-added articles such as accessories for mobile phones to be manufactured in any plant location.[1] This signifies another drastic departure for the traditional plant selection criteria.

THE OGURA YEARS

Childhood

Born in 1924, Masao Ogura was practically brought up as the eldest son of the family as his elder brother had died very young.

In 1919 Masao's father, Yasuomi, founded what was to become Yamato Transport, when he was 30. From its inception the company was a joint-stock firm, a rare phenomenon in the nascent age of Japanese capitalism. (See Table A2.1 for Yamato's chronological milestones.)

When he was seven Masao's home was attacked by a Communist Party-

Table A2.1 Yamato's chronological milestones

1919	Company foundation
1929	The transport route between Tokyo and Yokohama was started
1976	*Takkyubin* was launched
1981	Total volume of *Takkyubin* reached 10 million items
1983	Ski *Takkyubin*
1984	Golf *Takkyubin*
1985	Complete Moving Service
	Total volume of Takkyubin reached 50 million items
1986	Express Delivery Service
	Collect Service
1987	Book Service
	UPS *Takkyubin*
	Alliance with UPS (United Parcel Service of America)
	Total volume of *Takkyubin* reached 100 million items
1988	Cool *Takkyubin*
	Yamato sea mail
	Night-time Delivery
1989	Airport *Takkyubin*
1990	Two-Cubic Meter Personalized Moving Service
1992	*Takkyubin* time service
1994	Complete Moving Economy Service
1995	Unaccompanied Baggage Service
	Complete Overseas Moving Service
	Total volume of *Takkyubin* reached 500 million items
1996	Pickup and Storage Service
1997	*Kuroneko* Mail
	Kuroneko Quick Maintenance Service
1998	Package-tracking service on the Internet
	Time Period Delivery
	Golf, Ski and Airport Round-Trip *Takkyubin*
1999	Half-Day Moving Service
	Total volume of *Takkyubin* reached 800 million items
2000	*Takkyubin* Escrow Service

Source: Based on www.kuronekoYamato.co.jp/english/overview/index.html

related labour union. Ogura and his siblings had gone to a spa in anticipation of this. His father's motto became 'labour unions are to be destroyed, where employees are to be loved'. This incident left an enduring imprint on Ogura's mind (Ogura, 1999).

Tokyo High School

In 1937 Ogura passed the one-out-of-twelve entrance exam, to be among the 80 new students in 1937 at Tokyo High School (Tokyo). The seven-year stay at Tokyo incorporated four years for junior high school and three years for high school.

Ogura was deeply impressed by the speech made by the school's principal on the first day, to the effect that from that day on they would be treated as gentlemen and they were expected to behave as such.

Two years later his mother died of a stroke at 45. His father remarried, to a highly intelligent woman who influenced Ogura's intellectual and emotional growth but who sadly died just a few years later.

Tokyo University

Ogura entered Tokyo University's Faculty of Economics in 1943. During his university days he read many classics such as Weber's *The Protestant Ethics and the Spirit of Capitalism*. He was struck by how important ethics were in defining a businessman's behaviour.

Shortly after going to university Ogura was conscripted and chosen as an Army officer candidate, entering officer school in Fukuoka in 1944. During the war he saw how hunger could destroy human dignity. When some soldiers stole, it drove home to him how hunger could atrophy people's ethics and morale (Ogura, 2001).

Joining Yamato and Hospital Life

In September 1948 he joined Yamato Transport and was assigned to the general affairs department. Prior to joining the firm, he had worked with his high-school classmates selling saccharine and had met a girl he wanted to marry but his father opposed this.

Shortly afterwards he fell gravely ill with pneumonia. During his long convalescence, he despaired at ever being useful to himself or society. This almost drove him to attempt suicide, until one night he thought he saw a light and felt relieved. Overall he spent almost five years in hospitals and returned to work in 1953. He joined the Salvation Army shortly afterwards (and converted to Catholicism years later).

Secondment to Shizuoka

In 1954, at a bank's request, Ogura was sent as senior manager of general affairs to Shizuoka Transport, a recent acquisition of Yamato. He was 29 and had just two people to supervise.

The firm had no employee regulations; Ogura was supposed to work them out for himself. The firm was in the red, with an obsolete structure and systems.

One day a senior executive, also seconded from Yamato, asked him to come with him to a warehouse. The senior executive told Ogura to hide behind an electric pole. Shortly afterwards two truck drivers came out of the office to load the truck with boxes. Ogura was told to count them, there were 50 of them.

Three days later when the truck drivers returned from Tokyo they were asked to show the cargo invoice, which was 50 boxes short. Ogura knew then why the Shizuoka subsidiary lost money. Clearly, the firm was morally lax to boot.

Labour safety was another important concern. The firm had been reprimanded again and again by the authorities for poor safety in its operation. Ogura visited a factory famous for its safety regulations. Inside was a poster emphasising the importance of safety before efficiency. It came home to Ogura that if the company was to emphasise all necessary safety, actions must be implemented. At Shizuoka Transport drivers shuttled between Shizuoka and Tokyo in three days, often being requested not to take a day off after these days and continue driving. Ogura decided to insist the day-off rule was observed (Ogura, 2001).

Back to Tokyo and into the Fray

In 1956 after contracting marriage Ogura was called back to the Tokyo head office and put in charge of transport for department stores. Labour unions had staged several strikes. Normally these strikes did not affect cargo for department stores by virtue of an implicit pact between management and labour unions that department stores were valuable customers who should not be bothered by Yamato's labour conflicts. In one year it seemed this pact was not going to be respected. So Ogura's father accompanied him to Mitsukoshi, a major department store chain. His father asked to see Mitsukoshi's president and told him that due to the strike transport might be affected, emphasizing he would not accede to labour union demands because if he compromised, labour union demands would impact prices. His client agreed and encouraged Ogura and his father not to accept unions demands. For Ogura the lesson was that top management should not compromise when they believe they are right.

In May 1957 Ogura signed a transport contract with Sogo's Yurakucho branch. He wanted an exclusive arrangement, since Yamato had monopolized cargo handling for such a major firm as Mitsukoshi before World War II (after the war though the firm had to share cargo transport with Nippon Unpan).

To convince Sogo of the value of an exclusive transport contract, Ogura also pointed out that before the war Yamato had handled all cargoes sent and received by Sogo in Osaka. His father also supported him in his endeavour. Ultimately the transport contract was split between Yamato and Nippon Unpan. Ogura Senior consoled his son saying it was better in the long term for Yamato to have a competitor, as a monopoly would mean less effort was made to improve cost structure and service quality. Ogura saw that a president had to have a longer view of management issues.

According to 1960s data cargo handling for department stores was about 20 per cent of Yamato's revenue. In the Tokyo area its market share of department store cargo was 50 per cent (Kon, 1997). Another 20 per cent came from transport operations combined with Japan's National Railway. Total revenue was ¥3300 million, and operational profit was 3.1 per cent. The problem was that routine regular truck transport did not break even.

In frequent visits to branch offices Ogura found out that drivers often left some cargo for the next day. After hours, when branch heads left for home, nobody took care of cargo except for these drivers (if they volunteered to do so). So Ogura set a simple rule: if a branch transported more cargo than the standard estimate per day it would be seen as making a profit, otherwise it would be seen as in deficit.

Shizuoka Transport managers, in contrast, paid more attention to each transport operation's profitability. When there was space in a truck managers even called prisons in search of sculptures and other items prisoners made, which, while tariffs were low, were readily available for transport.

Tokaido (Tokyo-Osaka) Route

Apart from cost oversights at the operational level (at branches), the regular truck business losses were due to Yamato's late arrival in long-distance large-lot transport. Yasuomi, the senior Ogura, always insisted on short-distance small-lot transport.

Ogura's father had succeeded due to small-lot transport within Kanto area, namely, Tokyo and surroundings. He believed a truck's radius should be less than 100 km, over which the train was more competitive. This was true of truck technical qualities before the war, however after WWII, both truck quality and road conditions had improved.

For Ogura this was a clear example of a previously successful entrepreneur, who committed an error precisely because of that past success.

The gravest error was missed cargoes from Osaka area to Tokyo area. In Japan's high-growth period (the 1960s) demand for electrical appliances was high. Manufacturers such as Matsushita, Sharp and Sanyo were based in Osaka. This meant merchandise moved from east to west, and Yamato did not have a license to operate on the Tokaido motorway which linked Tokyo and Osaka.

Yasuomi Ogura insisted that beyond the Hakone Mountain were ghosts and they should not go beyond that 'waterfront' if they did not want to be scared by the preternatural beings. By 1957 Masao Ogura had persuaded his father and applied for a license to operate between Odawara and Osaka. In 1959 the license was granted despite opposition from existing competitors and Yamato could start its regular truck transport in 1960, five years after its first competitor had started its Tokyo-Osaka long-distance truck transport.

The five-year delay in arriving in Tokyo-Osaka transport made it hard for Yamato to get customers. When in 1961 Ogura was promoted to the directorship, he instructed his people to rush to enlist a new customer, every time they spotted from the road a smokestack they had never seen. 'Find a smokestack' became their motto.

The Matsushita Electric contract was a windfall for Yamato. Every month from the 20th Matsushita had a large quantity of cargo to send. However, Ogura found the contract was unprofitable. The cause was the tariff structure set by the license-granting authority. Freight was estimated on the basis of decreasing per-unit tariff, meaning the heavier the cargo the less the per-unit freight. Matsushita's cargoes were heavy which made its per-unit tariff below Yamato's cost. Worse still, handling Matsushita cargoes required investment in new trucks and terminals, which ultimately pressured company profits, increasing interest payments, etc.

This situation was a major problem for Ogura who had championed the move to long-distance and large-lot transport. A finance director seconded from Yamato's main bank[2] sent his staff to watch Ogura's every move.

In 1965 sales grew to ¥6800 million but the company's ordinary profit fell to 1.8 per cent.

Ogura decided to decline small-lot cargoes which he thought were cost drivers and concentrate on large-lot cargoes, ultimately this turned out to be a mistake.

Meanwhile he tried many strategies to increase profitability. He used trailers, able to carry a 15-ton cargo instead of 10-ton. Operational efficiency was improved by separating a trailer from a truck and linking it to another. From 1965 to 1975 Yamato purchased 206 trucks and trailers.

In 1967 Yamato adopted the relay system consisting of changing truck drivers from Tokyo in Hamamatsu, mid-way between Tokyo and Osaka. This

meant drivers could go home to Tokyo on the same day instead of spending a night in Osaka. This shortened drivers' working hours.

New Haulage Era Started

The same year saw the first container vessel operating on the Pacific route. Before then transhipment from trucks to vessels and then from vessels to trucks, needed days. Overall, it took a month before cargo arrived at its destination. Containers revolutionised this. They were part of a truck when transported by trucks, and part of the warehouse in port, etc. Labour costs and transport time were cut dramatically thanks to eliminating transhipments. This spelled a logistics revolution.

As the company's productivity was low and declining Ogura studied adopting containers and other measures to improve it. None was achieved, one reason being the structural problem inherent in large-lot transport. Another was labour union radicalisation. Frequent strikes drove away customers. Ogura resented the fact that Yamato, a first-rate haulage contractor before WW II, was now a second-rate player.

Appointment as President and Dark Days

In 1969, which was the company's fiftieth anniversary, Yasuomi, the senior Ogura, had a stroke. Masao Ogura, who had by this time been appointed senior managing director, visited him in hospital every Saturday to report company performance. Seeing his father's plight, Masao Ogura became keenly aware of the need to leave the top position at the right time. Otherwise the CEO could become a drag on their company.

In March 1971 Ogura was appointed second president of the firm. Two years later the first energy crisis occurred. Concentrating on large-lot haulage harmed the firm's performance. In 1974, 25 per cent less cargo was transported than the year before.

Ogura had to ask labour unions to accept a pay cut in exchange for promising to maintain employment. Directors' executive compensation was cut. Ogura even commuted to work by train.

Employees from the countryside were moved to Tokyo for three months. The salary differential between Tokyo and outside was ¥5000 per month per head. Yamato's competitors based outside Tokyo enjoyed a competitive advantage in terms of labour cost, which was 60 per cent of total cost.

New recruitment was stopped. Part-time operators who were housewives and bachelors were dismissed. Between 1973 and 1975, of 6500 employees, 1000 were laid off. Ogura was careful not to dismiss labour union representatives (Ogura, 2001).

Large-lot haulage operations were maintained, as Ogura thought his competitors were doing. Nonetheless, at the bottom of his heart he could not convince himself that, in sticking to a large-lot transport, his competitors could make money. When he travelled to Osaka he secretly observed how Fukuyama Transport, a competitor, was doing in one of its branch offices. A driver came out and packed several cargoes. Ogura counted and realized a lot had less than ten items. He knew at Yamato less than 10 per cent of its invoices had lots with less than ten items. Average Yamato invoices covered lots over 50 items. He saw that loading trucks with large-lot cargoes without small-lot cargoes had been the main cause of the company's poor performance (Ogura, 1999).

Ogura decided to shift from large-lot haulage. But customers who had been driven away due to their small-lot transport needs were slow to return. His competitors knew small cargoes' profitability was better than large ones'. Ogura learnt this the hard way and it was driven home to him that his experience as general affairs specialist did nothing for him in daily business.

In 1975s return on sales dropped to 0.7 per cent. Something drastic had to done or risk going out of business.

HOME DELIVERY SERVICE OR THE *TAKKYUBIN*

Ogura asked himself what was the best haulier for customers. His answer was a company which would transport any quantity to anywhere in Japan.

Suddenly he recalled having read that the Yoshinoya chain which specialized in beef-meat served with rice increased its profit when it focused on one menu item to the exclusion of others. Logic dictates that if you cut the number of dishes offered, the number of customers might decrease as well. The reality was that Yoshinoya ended up with more customers.

Ogura wondered if instead of pursuing the idea of becoming the ideal haulier, Yamato and its customers might be better off if the firm only offered a focused service.

The second hint occurred when his family tried to send old clothes to relatives in the Chiba prefecture. Hauliers would only handle cargo from corporate customers. Ogura could not, even as president of Yamato, send the items.

The only way open to a housewife was parcel services offered by the National Railway or Post Office. Their packaging and weight requirements etc., were stringent and, worse still, it took days for the parcel to arrive at the destination.

The third hint was JAL Pack, a packaged and organized tour offered by Japan Air Lines. Thanks to this, even an old lady with no knowledge of foreign

languages could travel thanks to the package which included air tickets, hotel bookings, town tours, multilingual guides, etc.

The question was, how would these hints be translated into the haulage business? First, housewives would buy door-to-door delivery services. Until then the typical haulier customer was male. If housewives were to be targeted the service content must be crystal clear. A uniform regional tariff, no need to package, next-day delivery, parcel reception and delivery to anywhere in Japan, etc., should be offered.

Corporate customers might guarantee a steady flow of cargo for specific routes. However household demand seemed random and sporadic. Parcels could be delivered and be destined for anywhere. An order would only include one parcel.

Ogura however tried to visualize from a bird's-eye view the flow of cargoes between Tokyo and Osaka or Nagoya. He realised an individual parcel might reach you at random but overall there should be a flow.

He advanced the 'density' concept to explain cargo profitability. This emphasized dilution of fixed and indirect costs based on the volume of cargo handled in a given square kilometre. It helped to understand haulage operations could be a loss maker at the beginning due to low cargo density but as density increased, operations would break even.

In 1973 Ogura travelled to New York to tour his company's branch offices. When in Manhattan he saw four UPS – United Parcel Service- trucks parked on a corner. He realized each block supplied sufficient cargo to a truck. That was why there were four trucks on a corner. The operation of a truck has a fixed cost and will only break even when cargo fills it. UPS's four trucks on a corner confirmed Ogura's belief that this business would be successful (Ogura, 2001).

Putting into Practice the Idea of the *Takkyubin*

Back in Japan Ogura put his idea of a home delivery service to his board. All of them including his own father were opposed to the idea. Their argument was that even cargoes to and from department stores which required little effort were loss makers. How could they break even if they had to collect parcels from households?

The only people who agreed with the idea were labour union representatives. They were sold on Ogura's idea as he had not dismissed any labour union representative during the 1973 energy crisis. Employees who had to stay in Tokyo on a rotational basis wanted to stay at home if they could. They welcomed any job which allowed them to stay at home.

Ogura was not 100 per cent sure the new business would succeed. But clearly Yamato could not enjoy any competitive edge in commercial haulage

for corporate customers. Yamato was an underdog. Its only way to survive was to break new ground in a new business.

He personally drafted a proposal to open home delivery services and managed to get approval from the board although most directors were against it when asked individually.

In September 1975 a ten-member task force was set up. Ogura and Tsuzuki, the senior managing director, and younger staff and labour union representatives spent two months working out the detail to inaugurate services in January 1976.

The distribution network was designed after airlines' hub-and-spoke system. In every prefecture the airport was the hub to be provided with a distribution centre and depot. From there parcels would be distributed, passing through three stages before their final destination.

Yamato's office network was insufficient to match household demand. Liquor shops were chosen as Yamato's agents.[3] Due to the monopolistic handling of liquor sales for tax reasons liquor shops were present in every town in Japan. For liquor shops, handling Yamato's parcels gave them an opportunity to promote sales to housewives handing their parcels in, apart from their commissions.

As scheduled, in January 1976 the *Takkyubin* (home delivery) service was inaugurated. To start with, the Kanto area, namely, Tokyo and its surrounding prefectures, was covered with the next-day delivery service. If a truck went to a household to pick up cargo rather than customers coming to liquor shops to hand them in, an additional ¥500 was charged. Otherwise no surcharges except for freight were collected. (See table A2.2 for Yamato's service-menu items.)

The first month saw only 9000 parcel deliveries. Ogura was scared and concerned but decided not to pressure his employees to make money. Instead he emphasized the importance of service quality. His motto then was 'first the service, then the profit'. He was aware that expanding the *Takkyubin* would require a huge amount of money to set up new offices and hire new employees. He knew that if he emphasized the investment aspect his employees would focus on the quality service.

For him drivers were the primary force. Therefore Ogura emphasized that drivers must operate like a *sushi* cook. *Sushi* cooks prepare *sushis*, attend customers, calculate bills, etc. *Sushi* restaurant performance is largely dependent on *sushi* cooks. They must take decisions on their own. So drivers were called sales drivers (SD). To help SDs a special vehicle called a walk-through vehicle was designed and manufactured by Toyota (Yanagihara, 1997).

To ease cargo handling information the *Hariden* – affixed invoice – system was invented (Yanagihara, 1997). Invoices were issued in five copies, two of

which were stuck to the box. One was given to the parcel sender to acknowledge receipt. Of the two remaining copies one was used to bill the account to large customers not paying cash, and one stayed at the branch office as an accounting document. As soon as the parcel reached the destination region, the branch there kept one of the two invoice copies which came with the box. The SD or driver delivering the box to its addressee would ask them to sign the invoice copy affixed to the box.

Customers First

The reputation of the *Takkyubin* service spread like wildfire. At first, drivers were not keen to collect money, deliver parcels, etc., which they thought were not their task. But with customers' thanks and their warm reception gradually their opinions changed.

By fiscal year 1976 (April 1976 to March 1977) the service was handling 1.7 million parcels.

Positive sides of the *Takkyubin* became clear: (1) housewives did not try to negotiate tariffs, unlike corporate customers, and (2) freight was paid for in cash, which aided Yamato's treasury, as corporate customers only paid by bills of exchange.

A Turning Point: Withdrawal from Haulage for Department Stores

In 1979 there was a milestone event symbolizing the turning point for the management of Yamato. It withdrew from haulage for Mitsukoshi department stores.

Mitsukoshi's new president, Okada, had demanded Yamato pay parking fees for trucks parked on Mitsukoshi premises, plus office space used by Yamato's employees in handling of cargo, as well as reduced freight charges. Initially Yamato accepted these demands. However, when a ¥100 million-plus loss was generated in the Mitsukoshi business Yamato decided to stop operations for Mitsukoshi. In November 1978 the contract with the department store chain was formally terminated.

The Mitsukoshi incident marked, psychologically, the transition from the old Yamato days to the *Takkyubin* era. In 1979 Yamato rescinded the contract with Matsushita and other large-lot customers. Ogura's view was Yamato could not purse the two businesses: large-lot haulage and *Takkyubin*.

Ceasing large-lot haulage lead to a loss in financial year 1979. However, the *Takkyubin* business grew exponentially, reaching 33.4 million parcels in financial year 1980, equivalent to cargo handled by the National Railway. ROS topped 5 per cent as ordinary profit grew 3.3 times over the preceding year. After five years the *Takkyubin* finally broke even.

Table A2.2 Yamato's service menu items

Domestic Parcel Delivery	1. *Takkyubin*	1. *Takkyubin* door-to-door parcel delivery service provides fast, reliable, low-cost delivery to every address in Japan. On call pickup and next day delivery coupled with six delivery time-periods makes *Takkyubin* the excellent choice for all shipments.
	2. *Kuroneko* Mail	2. *Kuroneko* Mail Service delivers magazines, catalogues and product samples to every mail box in Japan. It provides scheduled low-cost delivery with tracking capability.
	3. Cool *Takkyubin*	3. 'Chilled' and 'Frozen', temperature controlled delivery service can be added to *Takkyubin* and it reaches every address in Japan.
	4. Collect Service	4. Collect Service carries out shipping, delivery and payment collection service (C.O.D. service).
	5. *Takkyubin* Time Service	5. *Takkyubin* Time Service guarantees delivery by 10:00 a.m. next day.
	6. Express Delivery Service	6. Same day delivery service for extremely urgent documents and packages. Available in 55 major cities.
	7. Golf *Takkyubin*, Ski *Takkyubin*, Airport *Takkyubin*	7. Delivery service of golf clubs to golf courses, ski equipment to ski resorts and suit cases to airports frees avoids carrying them. Round-trip Service is also available.
International Parcel Delivery	1. UPS *Takkyubin*	1. For critical international shipments, UPS world network guarantees fast and reliable customs-cleared delivery to over 200 countries and territories.
	2. Yamato the Sea Mail	2. Low-cost door-to-door parcel delivery service by sea. Available in USA, UK, Germany, Netherlands, Belgium, Hong Kong, and Singapore.
	3. Unaccompanied Baggage Service	3. Unaccompanied Baggage Service with *Takkyubin* concept. Door-to-door complete package service with Japanese assistance at destinations. Available in USA, Canada, UK, Germany, France, Netherlands, Belgium, Hong Kong, Singapore, Malaysia, Taiwan and Thailand.

Domestic Moving	1. Complete Moving Service 2. Complete Moving Economy Service 3. Two-Cubic Metre Personalized Moving Service 4. Charter Service 5. Half-Day Moving Service 6. Pickup and Storage Service 7. Small Moving Service	1. Packing, delivery, unpacking and cleaning, everything needed for family moving is included in this complete package. The cost of the moving is easily calculated by the number of rooms. 2. Value package of complete moving which includes packing and delivery services. 3. Two-Cubic Metre Personalized Moving Service provides simple moving by specialized two cubic metre container. 4. The manpower, small, medium and large size trucks with drivers available for moving. 5. Short distance moving service to be completed in a half-day. 6. Pickup and Storage Service makes life space bigger. Furniture and personal belongings are safely stored in temperature controlled rooms. 7. One consignment of bed, sofa, desk, TV etc. are safely packed and delivered.
International Moving	Complete Overseas Moving Service	Complete moving service by Japanese staff and operation. Available to USA, Canada, UK, Germany, France, Netherlands, Belgium, Hong Kong, Singapore, Malaysia, Taiwan and Thailand.
International Forwarding and Logistics		International Air and Ocean Freight Forwarding and NVOCC services provide customized operation for imports and exports. Yamato's network creates logistical speed and efficiency.
Products Retails	1. Packing Materials 2. Yamato Brand Products	1. Packing materials are developed and retailed. 2. '*Tokusen-ichiba* Brand' heavy and bulky products, such as water, toilet tissue, etc. are distributed by sales drivers, so they do not have to be carried.

Source: Adapted from www.kuronekoyamato.co.jp/english/overview/index.html

Fight against Officialdom; the Minister Sued

When growth of Yamato's business seemed guaranteed, it faced a hurdle: governmental regulation. Haulage by speedways or motorways needed a license. When Yamato applied for one in 1980 to operate on the Yamanashi route linking Tokyo with the inland prefecture, the Ministry of Transport did not reply. It feared opposition from existing hauliers, who did not want increased competition.

In January 1984 at a public hearing held by the Transport Council Ogura was invited to speak and he argued that commercial haulage and *Takkyubin* targeted different markets, as the latter focused on unspecified customers. The Council agreed and the license was granted in May, four years after application.

A similar obstacle was encountered when Yamato applied for a license for the Northern Tohoku Region in November 1981. The Ministry hinted that the license would be issued if Yamato managed to persuade their competitors.

Ogura fought against this administrative 'slackness'. He argued the Administration was in dereliction of its role if it insisted on there being no objection from existing competitors before granting the license, and not granting it if there was. He thought the Administration should prioritize consumers' needs first, not hauliers'.

In December 1985 Yamato submitted a complaint against the Minister of Transport based on the Law of Complaints against Administrative Measures. The Ministry responded by saying the application was being reviewed and given due consideration, an expected delaying tactic.

In August 1986 Yamato started a lawsuit against Ryutaro Hashimoto, Minister of Transport, for neglecting his obligations. This administrative lawsuit was unheard-of in Japan. The Ministry of Transport compromised by issuing the license in December, after a public hearing in October.

Ogura never doubted winning the lawsuit. But the license concession terminated it. His belief was based on the view that the Ministry of Transport lacked documentation needed to refute Yamato's argument. The law regulating land transport specified the need to review granting of licenses in terms of haulage demand and supply. Ogura thought that the Ministry had never conducted such a study.[4]

Against the Authorities

Yamato during Ogura's presidency conflicted with the Ministry of Transport on both licenses and freight.

The *Takkyubin* had two parcel sizes: the S size for parcels below 10 kilograms and the M size for those up to 20 kilograms. Ogura had chatted with

a college student and she complained the *Takkyubin* rate was too high when she tried to send her classroom notes to a friend. Ogura agreed and applied in March 1983 for a license to set a price for parcels below two kilograms (the P size). The Ministry's rejection of the application infuriated Ogura whose opinion was that the Administration was not entitled to review hauliers' price setting.

The company applied several times with no approval forthcoming. Ogura appealed to public opinion, on 17 May Yamato announced the start of the P-size service on 1 June, in a newspaper advertisement.

When the Ministry did not respond, another advertisement was placed in newspapers on 31 May stating the P-size service would not start on the announced date; in addition to apologising, Yamato explained the delay was due to slow processing of the license by the Ministry of Transport.

T. Sugiura, the vice minister, it is reported, was enraged when he saw the advertisement. However, public opinion was on Yamato's side and the Ministry was forced to grant approval in July.

Friction with government bureaucrats was frequent and incessant. In 1988 Ogura advised on the shift from licenses to approvals for haulage of general cargo in the context of the Administration's restructuring plan. He was informed that if licenses rather than approvals were the basis on which to apply administrative guidance, the number of bureaucrats would grow. Resistance from bureaucrats where their acquired rights were concerned was great.

Ogura never sought political assistance even when confrontation with bureaucrats was greatest. For example, Keizo Obuchi, later to become Japan's prime minister, was a friend of Yasuomi. Ogura refused to avail himself of Obuchi's help. His argument was that if he asked for a politician's help his competitors would do the same and eventually compromises would be sought-after on all occasion even if Yamato's position were right.

A Race for the Top Position

As soon as other competitors saw the *Takkyubin* was lucrative, new entrants were legion. Yamato's trademark was the Black Cat (*kuroneko* Yamato). Others adopted Pelican, Red Dog, Small Bear, Lion, Giraffe, etc., as their trademarks. At one time there were 35 of these trademarks.

This was called the Animal War. Ogura stoically welcomed the competition, sure that Yamato's service quality was better than competitors'.

In 1981 he started a three-year campaign (*Dantotsu Keikaku* – plan to keep the clear top position) to extend the next-day service area. The campaign was renewed twice, lasting for nine years. Remembering that any service could be beaten by new ones, Yamato launched a delivery service when there was

somebody to receive the delivery, to replace next-day delivery. Many times parcels had not been delivered because nobody was at home. Ogura thought it important to shed logic favouring the haulier and adapt to customer needs.

By end-March 1990 when the campaign concluded after nine years, Yamato's delivery network covered 99.5 per cent of surface area and 99.9 per cent of population. Next-day delivery involved over 90 per cent of deliveries.

Takkyubin delivery involves things such as golf bags and clubs, and skis. In the case of golf bags Yamato received them six or five days before the golf game. Items were expected to arrive at the destination a day before play. For both golf playing and skiing transport by *Takkyubin* was a great help to customers due to space limitations on passenger trains. Suitcase transportation for overseas travelers when traveling inland in Japan was an important service for the same reason. In the *shinkansen* – bullet trains – space was hard to get.

In 1988 Yamato inaugurated Cool *Takkyubin* for haulage of chilled cargo. Its development and investment cost Yamato ¥15 billion. Employee training was very important but the service has become a major menu item at Yamato.

Resignation as Yamato's President

Yamato won the Animal War. In 1984, 150 million parcels were handled by Yamato, more than the total number of parcels sent through the mail.

By 1988 turnover reached ¥300 billion with profit of ¥10 billion.

In the latter part of his presidency Ogura started to think about setting a retirement age for CEOs. He thought many companies suffered from CEOs who had passed their prime, but had not retired. His own father stood down from the top position at 81. He realised a dictatorial figure might be appointed and who might not want to resign. Age might dull their business acumen and lead the company to disaster. Ogura believed it was his responsibility to set a rule to avoid this (Ogura, 2001).

It was proposed to set an age limit to the presidency. The board was all in favour, but were unsure about the appropriate age. Ogura tentatively proposed 63, although he thought 65 was the right age. He was surprised when this was accepted by the board. Applying that limit, Ogura resigned as president in June 1987. M. Tsuzuki, the senior managing director, succeeded him.

Post-retirement and Re-appointment as Chairman

In 1991 Ogura resigned as chairman and became a special counselor. However, he heard from the labour unions some branches hid accidents and head office was not informed. He investigated and found it was true.

In June 1993, Ogura again took over the chairmanship to 'clean' the organisation of malpractice. He became aware in the personnel evaluation

system concepts such as 'high-mindedness', 'lofty personality', etc., should be contemplated.

After two years of the second chairmanship Ogura was unsure about whether to continue or not. He consulted H. Miyauchi, then president, encouraging him to show more leadership. Miyauchi commented that in board meetings people gave more attention to Ogura than to him, which shocked Ogura. This was decisive and Ogura resigned.

EPILOGUE

In September 1993, Ogura set up the Yamato Foundation to dedicate himself solely to *causes sociales*. The organisation was to contribute to handicapped causes. Ogura donated 2 million Yamato shares estimated to be worth ¥2.4 billion. He retained 1 million more shares to live on after his retirement. However, in 2000 he donated the remaining shares (estimated at ¥2.2 billion), as his wife had passed away and his daughter had moved to the US. He rented his house to an American MNC and this was sufficient for him to live on.

NOTES

1. One of the authors' personal conversation with Mr H. Nagasawa, president of Reudo, manufacturer of accessories for mobile phones located in Matsunomae-machi, Niigata-ken, where the snow is 4 metres deep in winter.
2. Japanese companies used to work with a bank for finance. Other banks were also made use of but in relatively smaller proportions. During a crisis main banks provided financial support and many times seconded staff to the firm to guide it and, more often than not, keep watch.
3. Yanagihara points out that Yamato targeted to have an agent in every 500 metres radius. There were over 280000 agents by 1997.
4. 'After this lawsuit I gained fame as a man fighting against government officials. That was not my intention. It's only that the Ministry hindered smooth running of our business. I still feel cross when I remember this incident since it took as long as five years for us to get the licence.' (Ogura, 2001, p. 25) [translated by the authors].

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A3. Norio Ohga: the fifth president of Sony Corporation

INTRODUCTION

In 1995 Sony's president Norio Ohga announced his successor would be Nobuyuki Idei. His selection was not based on Idei's past achievement, which Ohga thought rather poor: Idei was unsuccessful as the head of the Audio division; his attempt at entering the home computer business was a failure. Ohga was adamant on this point: his selection was not based on the past but Idei's potential.

Ohga's ideal man to lead Sony was somebody who would dazzle the world with his resplendence.[1] Ohga himself strove to make Sony a company to dazzle people with its brilliance.[2] His successor therefore had to be someone who understood Sony's uncommon quality of outshining its competitors (Takagi, 2001).

Such is the philosophy of a man under whose steersmanship Sony grew from a ¥1 trillion company in 1982 to a ¥6 trillion company in 1999. This case describes Ohga's personal and professional history as it entwines with Sony's growth.

NORIO OHGA THE MAN[3]

Childhood

Norio Ohga was born in 1930 in Shizuoka prefecture into the family of an entrepreneur. Shoichi, his father, ran his own business with branches in Indochina. In 1941, a year before Ohga joined a junior high school, to be exact, Japan's navy attacked Pearl Harbor and the Pacific War started.

In his second year he contracted pleurisy and had to stay home for a year. A neighbor, Ichiro Iwai, whose family owned Iwai Industries, a forerunner of the present-day Sojitz (Nissho Iwai) trading house, took pity on him and volunteered to give him lessons.

Ichiro taught Ohga varied things such as principles on which electrical condensers worked and interpretation of music scores. Thanks to this personal

teaching Ohga could sustain technical discussion with Sony's engineers without problems years later.

In 1947 he attended a concert by Japan Symphony playing Beethoven's Ninth Symphony. Teichi Nakayama, a baritone singer, took part in it and Ohga was deeply impressed. In the following year, preparing for a second attempt at the Tokyo National University of Fine Arts and Music's (*Geidai*) entrance examination Ohga took a private lesson from Nakayama.

In 1949 Ohga managed to enter *Geidai*. There were ten new entrants in the vocal music course and 40 in the chorus course. He was popular among girl classmates who outnumbered men seven to three.

Just after joining *Geidai*, Ohga was enthused by amplifiers for record players. The Williamson amplifier from the USA attracted Ohga who, based on a magazine article, made his own amplifier. He made several more units and gave them to Nakayama and others. As he assiduously visited Akihabara – a quarter in Tokyo with many electrical appliance shops – to buy amplifier parts and components he became well known by shop owners.

As he was known by his classmates as an electrical wizard, a classmate of his introduced him to Hiroki Naganuma, a former Ministry of Finance vice minister, who planned to open a music studio to let as an investment in a premium Tokyo location.

Electrical installations were set in place by Oki Electric. Ohga designed the electric circuitry with Oki. The circuit for tuning recording levels was designed by Ohga, who maximized the dynamic range – the ratio of high and low sound levels – to make recording quality the best possible.

Naganuma paid Ohga ¥100 000 for this service to Ohga. Those days a young office worker barely made ¥5000 a month. Another consequence of this project was that Ohga's existence came to the attention of Sony's Ibuka, one of the firm's founders.

In 1950 *Geidai* decided to buy a tape recorder. Totsuko (that later became Sony) attempted to sell its G-type magnetic recorder and approached Ohga who had championed the idea of buying a recorder and had managed to persuade the Ministry of Education to budget the necessary money.

The device Sony delivered to him for test-listening was unsatisfactory technically. So Ohga listed 10 reasons why it was so and visited Sony to hand over the list. Ibuka took a liking to Ohga and from then on they met from time to time to discuss technical matters related to recorders.

After graduating from *Geidai*, Ohga decided to study abroad on the basis of the ¥100 000 he had earned helping Naganuma. He chose Germany.

The day of his graduation Ibuka sent a car to meet Ohga and he was driven to Sony's office. Ibuka suggested Ohga should sign a contract for advisory services with Sony. Ohga first declined on the basis that he was leaving for Germany, but finally allowed himself to be persuaded by Ibuka. With the

benefit of hindsight Ohga concluded later that the contract was actually a ploy to secure Sony's relations with him.

In 1954 he arrived in Munich, Germany. The following spring he moved to Berlin and was introduced by Michiko Tanaka to Herbert von Karajan, the conductor of the Berlin Philharmonic Orchestra. Michiko had helped von Karajan to escape Nazi persecution in 1945.

During Ohga's stay in Germany he met Honda's Soichiro Honda and Takeo Fujisawa while they toured Germany. Ohga acted as chauffeur, interpreter, and restaurant guide for a week.

Ohga also got to know Gen'ichiro Kawakami, Yamaha's legendary top executive when advising Yamaha regarding its pianos.

In July 1957 Ohga graduated from the National Art University at the top of his class. When preparing for his return to Japan, he received a letter from Akio Morita, Sony's co-founder, asking him to accompany Ibuka during his German tour.

They visited Telefunken's tape-recorder plant. To Ohga's surprise Ibuka showed little interest in tape recorders. However, in a semiconductor plant Ibuka looked truly keen on gathering information. Sony was planning to develop transistors.

In November 1957 Ohga married Midori Matsubara, a pianist he met in Germany. The *Nakodo* (a 'go-between') was Masaru Ibuka. Morita attended the wedding too.

Joining Sony

In 1958 Tokyo Tsuhin Kogyo or Totsuko shed its name and became Sony. It was listed on the Tokyo Stock Exchange in December.

Ibuka and Morita insisted on Ohga's coming to work at Sony once a week. Ohga, meantime, debuted as a professional opera singer.

Ohga's visits to Sony became increasingly frequent, as every time the firm negotiated with foreign companies over licenses, he was asked to be present.

The final decision to join Sony permanently came when Ohga accompanied Morita to Europe in May 1959. Ohga suggested they go from Europe to the US by sea. Transport by luxury liner was available on the Atlantic Ocean route. Morita agreed, as an ex-navy officer, he liked the idea of travelling on board a vessel as fast as a battleship.

They boarded *SS United States* at Southampton, UK. Over the five days of the voyage to New York, Ohga found he did not enjoy swimming in the vessel's pool. The pool water was too choppy due to the cruising speed of 35 knots (65 km/hour). Accordingly, Ohga and Morita spent time discussing management problems. Ohga's opinion was that Sony must catch up with its

European and American competitors, Morita expressed his total agreement and added that Ohga must join the firm.

After returning to Tokyo, Ohga and his wife were invited by Morita and his wife to a famous Japanese restaurant in the posh Akasaka area. Morita encouraged Ohga to join the firm and exhorted him to develop parallel activities both as a Sony executive and an opera singer. Ohga ended up by being persuaded by Morita.

In September 1959 Ohga entered Sony, he was 29. At his request he was appointed senior manager of the second production department in charge of development and manufacture of broadcasting equipment and devices.

CAREER AT SONY

He immediately disliked Sony's logo and suggested it should be improved. Morita agreed and appointed him chief of the design bureau. When Ohga said Sony's newspaper advertisements lacked elegance, he was appointed senior manager of the publicity department. Thus before he knew it, he was senior manager of product development, design and publicity.

The hectic life took its toll. One day Ohga was due to sing the part of the Count in the *Marriage of Figaro* in Hiroshima. He and his staff at Sony had negotiated a deal with a broadcasting station in the city. When they successfully concluded, Ohga headed for the theatre where the opera was on, and went on stage. While he was waiting for his entrance, he fell asleep and failed to appear on the stage at the right moment. Though he managed to conceal his failure, he concluded he would have to make a decision about which career he should pursue: Sony or the theatre.

In 1962 Ohga finally convinced himself it was time to shelve, at least temporarily, his music career.

He revised Sony's logo. The 'S' in Sony was made slightly larger than the other letters and the 'Y', smaller. The visual effect if all letters were the same size was that the 'S' looked small and the 'Y' large. Overall the Sony logo was revised six times and its current design was adopted in 1973.

In parallel to the Sony logo redesign, Ohga persuaded his firm to drop the figure named Atchan, a young male child doll which was placed throughout Sony's distribution network. His opinion was that the homely doll did not support the image of an international firm. Opposition to change was widespread but Ibuka and Morita supported Ohga totally.

Sony Design

On being charged with building Sony's corporate image, covering everything

from new product development to publicity, Ohga decided the corporate image should be coherent. Sony's industrial design left much to be desired then.

Ohga's idea was to make products look like luxury goods by combining black and silver colours. The body of products was moulded in die cast onto which the coating was heat-treated. Part of it was polished and given a silver tone. The die-casting idea was taken from Ichiro Iwai's teachings.

An FM radio set named TFM-110 (popularly known as Eleven) was the consequence of such a design improvement effort. Its shape was perfectly square instead of a traditional oblong. Its black and silver colour combination received high praise. Sony's radio market share shot up and has ever since used this colour combination.

Ohga also intervened in design of the Citation, a compact TV set, and Profile, a TV set without a wooden frame, in the second half of the 1970s when he was a vice president.

From its inception, Sony encouraged its staff to launch products nobody else did and avoid becoming a copycat. For example, in 1968 Sony adopted the Trinitron system for colour TVs unlike other firms using Shadow Mask system. The former's advantage was its brightness, a differentiating feature that gained Sony additional market share. Competitors immediately imitated Sony and Sony's market share fell back to 10 per cent.

The Citation television was developed to launch a totally innovative set with a new design. It departed from the traditional set encased in a wooden box. It had tuning buttons on top of the 13-inch display. Young consumers' acceptance was unexpectedly high and Sony's market share grew to 14 per cent.

Sport was made of the Profile model due to its unique design. Nonetheless, the Tokyo Motor Show decided to adopt it for displays. It was obvious design was gaining ground and becoming a selling point even in electrical appliances. Sony's remote-control devices currently closely resemble each other, as these result from the combination of ease of use and functional aesthetics.

Ohga thought advertisements were essential to appeal to consumers. Accordingly, he and his staff designed standard templates for different sizes of newspaper advertisements with the position of Sony's logo, the catch phrase, etc., clearly indicated.

Until then Sony's newspaper advertisements were designed by agencies. Sony demanded reduced fees now they were provided with designed templates. The agencies revolted but Sony was adamant and the agencies finally accepted it. Sony's corporate brand was thus created and consolidated.

Ohga believed the ultimate ideal of Sony design would be ease of use. For example tape recorders used to need tapes to be manually placed through recorder heads, which was a nuisance for users. Ohga accordingly invented a device called Soniomatic for automatic tape placement. Ibuka did not seem to

support the idea. However, when Sony's other staff raised objections Ibuka protected Ohga.

License Negotiations

License-related issues fell within Ohga's domain. When Telefunken lodged a protest against Sony's quasi-PAL system alleging it resembled the German TV manufacturer's PAL system, Ohga was sent to Germany. Morita's instructions were not to compromise on payment of license fees as the two systems were different. Ohga struck an uncompromising stance on the issue and won Telefunken's agreement.

Regarding tape recorders Sony's position was consolidated when Ohga successfully negotiated with the Dutch firm Philips a free cross-license, which allowed establishment of the standard for compact cassette tapes.

Ohga hit on the idea of cassette tapes, because even Soniomatic could not entirely resolve the problem of manually setting tapes to play. Cassette tapes would easily clear such a hurdle.

In Europe both Philips and Grundig had been struggling to establish their own system as the world standard. Both approached Sony to get its support. Technically Grundig prevailed over Philips. But the latter excelled in global deployment of its technology.

In the belief standardization would require global deployment, Ohga decided to co-operate with Philips. Its representative for Asia (Wisse Dekker who was to become Philips' president and chairman of its board of management in 1982) insisted on collecting license fees from Sony, where the Japanese firm's stance was that no such payment should be made if Philips and Sony were to collaborate. A compromise was reached by a free cross-license enabling these two firms to use each other's magnetic recording technology free. Inside Philips there was strong opposition to such a compromise but Dekker persuaded his firm on the grounds that (1) the standard war should be waged as quickly as possible and (2) Sony's support would be important.

In 1966 compact cassette recorders started to be marketed. It was 15 years since Japan's first home-use magnetic recorder (H-model) had been sold.

Philips' idea was to limit the license-fee free contract just to Sony, but the antimonopoly law forced it to extend the same type of agreement to other manufacturers. With the benefit of hindsight Ohga later realized this eventually drove rapid market growth.

CBS SONY

In 1964 Ohga was appointed a Sony board member at 34. Five years had

elapsed since he joined the firm.

One day he was called by Morita to his office and was told he was to help Morita to start the record business. Morita had just returned from the US after having a conversation with CBS, which had expressed its interest in collaborating with Sony.

Ohga was convinced records and audio equipment were like the wheels of a vehicle and complemented each other as businesses. JVC (Japan Victor) had been active in expanding its business to music software. Sony should follow suit.

His problem was he was overextended working on everything from product planning to publicity activities. Morita, however, did not allow any objection to him working on the music business.

The background to CBS's contact was a news item which raised the possibility of setting up a 50-50 joint venture in Japan (which banned foreign company entrants to many industries) for record production after July 1965. This was one of the measures involved in the first capital liberalization for overseas companies. Trade friction with the US had already built up over ship building and textiles.

CBS was owned by Columbia Records and had recently started to establish its own international network. First CBS approached Japan Columbia to set up a joint venture but it did not receive a positive response. Morita's reaction to CBS's contact was rapid and forward-looking compared with Japan Columbia's.

The problem Ohga faced was recruitment. Japanese record companies pressured the Ministry of International Trade and Industry (MITI) not to facilitate recruitment activities for new joint ventures. Sony, accordingly, inserted a full page advertisement in leading newspapers announcing 'staff wanted for CBS Sony'. The advertisement was designed on Ohga's initiative.

Reaction to the advertisement was slow. On the deadline for applications Sony staff went to the post office to collect two boxfuls of letters and advised Ohga. On the next day a further 7000 responses were received. From these CBS Sony recruited 80 people. Toshio Ozawa who had previously worked with Ohga was recruited from Sony to form the management team. Ozawa had an imperfect knowledge of music. However, Ohga greatly appreciated his management capacity and thought, assisted by his deep understanding of Sony's way of doing business, this would compensate for his lack of experience in the music market.

In March 1968 CBS Sony officially started with ¥72 million capital with Akio Morita as its president. There was a scuffle to decide whether Sony's or CBS's name should come first. Sony preferred to let CBS's name precede its own and retain management control of the new company. Actually running the business fell to Ohga as the new firm's senior managing director.

The majority of CBS Sony's staff lacked any experience in the record industry. Instead of following the industry's accepted custom, the new enterprise set up payment in cash and record returns limited to 10 per cent of purchases. Industry custom had payment by letters of exchange payable at six months. This forced disc shops to accept unwanted records but gave them the right to return as many as they wanted.

Despite Ohga's determination to modernize industry customs in view of its growth potential, disc shops strongly opposed this policy – which was the first hurdle to clear for the new company to survive. It was also rumoured that the new company was not very Japanese with meetings held in English and salaries being paid in dollars. This brought some young staff to tears.

Then there was a *kamikaze*, a divine wind. Simon and Garfunkel's song, *The Sounds of Silence*, sold by CBS Sony became a hit. Disc-shop owners overcame their ill-feelings towards the new business, having to beg the firm to sell them copies, and accepted cash payment. After this breakthrough negotiations with many disc shops and distributors became easier.

Teenage Idol Singers

From its inception it was rumoured that as CBS Sony was run by a professional classical singer it would, perforce, focus on classical music. Contrary to this belief, Ohga, from the start, planned to concentrate on popular genres. The first hit singer was Carmen Maki who belonged to Shuhei Terayama's vanguard theatre movement. Legend says she came to Ohga's office barefoot. Her song, *Sometimes I Feel like a Motherless Child*, was a huge hit and CBS Sony managed to have her participating in the *kohaku uta gassen*, a popular year-end song contest, quite an achievement for a two-year old start-up business.

CBS Sony had a great success in its launching of singers. Saori Minami succeeded with *Seventeen Years Old*, Hiromi Goh, Mari Amachi, Miyoko Asada, Seiko Matsuda, etc., were some names who sold very well. These singers carried off many prizes. Momoe Yamaguchi was another all the rage in the 1980s.

Ohga promised to himself the new firm would be number one in Japan in ten years and it would build its own headquarters building as soon as possible. He was appointed its president in 1970 and moved to the company's new headquarters in Ichigaya in 1973. Sales topped the industry in 1979. CBS Sony's success was a great help when Sony attempted later to launch compact discs (CDs).

Ohga contended CBS Sony should have its own pressing plant. Launching records in a timely fashion was a key industry success factor. Possession of a

plant was therefore seen as essential. While CBS was opposed to the idea, ultimately a plant was built in Shizuoka prefecture[4] in February 1968.

The Birth of CDs (Compact Discs)

Success in standardization of compact discs and CBS Sony widened Sony's business options. However, the second half of the 1970s brought a new wave, digitalization which impacted the sound world.

In 1975 Sony started to sell the Betamax home-video system, and from 1977 its PCM record equipment to digitize sound using Betamax tapes. Ohga, however, thought discs would be cheaper and easier to use than tapes.

Heitaro Nakajima who headed Sony's research laboratory, Chisato Miyaoka, and Toshitada Doi had researched the applicability of such an idea. They had developed a product, the same size as LPs (30 centimetres in diameter), with a recording time of 13 and a half hours.

In July 1978, a Philips engineer showed Ohga an 11.5-centimetre CD and proposed to make it and an optical disc a world standard. The CD's diameter was the same as the compact cassette.

Ohga immediately subscribed to the proposal, believing that the record industry must launch a better product than LPs, and that CDs could be this product. Philips excelled in optical video-disc technology and owned Polygram; Sony for its part excelled in audio signal-treatment technology and owned CBS Sony. The two companies were an ideal match.

Co-ordination between the two firms was not devoid of difficulties. Philips insisted on 60 minutes recording time. Sony led by Ohga was of the contrasting opinion that recording time should relate to the duration of pieces of music. An LP could not accommodate, for example, the whole of Beethoven's Ninth Symphony. Based on it, Sony argued a CD should be 12 centimetres in diameter and play for 75 minutes.

Recording density was another hurdle. Philips supported 14-bit, whereas Sony's Doi insisted on 16-bit, to gain the support of Japan's record industry, 16-bit was finally agreed to.

Further trouble was close at hand. December 1982 was set as the CD launch date, but as it neared, optical pick-up mass production proved technically very difficult. Likewise CD casting proved difficult, with the discs failing to be flat-faced.

A press meeting was held at the end of August in Tokyo in conjunction with Philips, eulogizing the coming digital-audio age. This conflicted with the record industry's negative reaction fearing that the LP business would be jeopardized.

Sony had a strong supporter in promotion of CDs in the person of Herbert von Karajan,[5] the famous conductor of the Berlin Philharmonic Orchestra.

Karajan always supported Sony's endeavours to improve sound-storage methods. In 1981 he gathered organizing staff and industry experts at the Salzburg Music Festival to listen to Sony's CDs. Von Karajan's support was forceful enough to convince the world of the new musical media's excellence.

APPOINTED SONY'S PRESIDENT

When Ohga was appointed Sony's president in September 1982 it was at 52, which is unusually young in Japan. He followed four presidents since Sony's founding.[6] Due to president Iwama's ill health, Ohga had acted as actual president of Sony between 1981 and 1982.

At the press conference to announce his appointment, Ohga emphasized his task as president was to increase Sony's brand equity.

His baptism of fire came in January 1984 during Sony's general shareholders' meeting. Ohga was adamant in not paying racketeers (*sokaiya*), who, in exchange for money, would refrain from voicing awkward questions in general shareholders' meetings. His pugnacious stance induced many of them to attend the meeting to castigate him. The meeting was held in Sony's conference hall, and was uproarious such that presentation of motions was almost impossible.

At the time Sony's Betamax and JVC/Matsushita's VHS were locked in battle and Sony was not on the winning side. The racketeers attacked this point. The meeting had started at 10.00am and lasted until 11.00pm, during which Ohga developed a fever and had to be given an injection. After 11.00pm the racketeers sudden began to disappear. It is unclear what happened but one explanation for this unexpected racketeer retreat was that the chief of the metropolitan police discovered Sony's general shareholders' meeting had lasted over 13 hours due to racketeer sabotage, then phoned the chief of Shinagawa ward police (in whose jurisdiction Sony's head offices were) and the racketeers got cold feet.

Large-scale Acquisitions

Ohga's effort, upon taking charge of the firm as president, was to promote CDs. A CD player and 50 CDs arrived in his office in December 1982. It is reported that Billy Joel's *New York 52nd Street* was one of the first numbers played.

CD players were marketed by 11 manufacturers inside and outside Japan. Prices were beyond the reach of many consumers – for example, Sony's CDP-101 cost ¥168000 – so sales were sluggish. CBS Sony launched many CD items, which helped CD diffusion.

CD sales started to take off in autumn 1984, with Sony's D-50 costing less than ¥50000. Industry wisdom viewed ¥50000 as the line below which sales of electrical appliances shoot up, Sony's people were unsure if it would break even. In fact demand exceeded supply. Software, namely CD, sales began to grow. By 1986 CD titles overtook LPs.

CBS started to demand a higher dividend payout, which drove Sony's management to plan the acquisition of CBS Sony.

From the beginning the firm paid out 100 per cent dividend. CBS's new president, Laurence Tisch, demanded an increased dividend. The payout ratio had increased tremendously thanks to CD sales, so Sony's management saw this demand as improper and started to consider the acquisition of the joint venture.

When Sony heard from a CBS executive in charge of the record division that CBS might be willing to sell its record division including the joint venture for US$1300 million, it began negotiations at the end of 1986. To Sony's dismay Tisch beat up the price every time they met, finally proposing US$2000 million to Sony's surprise, which resulted in negotiations breaking down.

Eight months later, namely, October 1987, the US stock market crashed – Black Monday. A despairing Tisch offered to sell at US$2000 million, an unprecedented amount in Japan's M&A history. Nobody except Morita and Ohga favoured resuming negotiations. Ibuka's stance was 'its your decision'.

Ohga's analysis was (1) acquisition of CBS Records would gain its worldwide network and plants and (2) the other 50 per cent of CBS Sony would become Sony's. Ohga had a clear picture of CBS Sony's cash-flow position in Japan and knew it was a buy. So, Sony acquired CBS Records in January 1988.

The mass media saw the operation as being burdened by an ownership premium. Later events showed Ohga's judgement to be correct – three years later CBS Sony's IPO (initial public offering) of 22 per cent of its shares generated US$1200 million for Sony.

Ohga's idea that hardware and software must harmonize with each other as do the wheels of a vehicle was realized regarding music. The image part still needed to be resolved, which required Betamax, the home video system, to be fixed.

VHS versus Beta

Nobutoshi Kihara, a Sony engineer, developed CV-2000 in 1964, the year of the Tokyo Olympic Games. It was a precursor to the home video system but did not sell well, except for business use. Based on it, the U-standard using cassette tapes was developed.

To make U-standard the global standard, Masaru Ibuka and Akio Morita proposed to Matsushita Electric and JVC – Matsushita's subsidiary – its adoption. During further development of the standard it was agreed each other's license might be used without royalty payment.

Sony concluded if it was to become the home video standard, smaller tapes were needed and Betamax came into being. Again Sony contacted Matsushita and JVC and gave them trial models. Matsushita had been developing its own standard but Konosuke Matsushita was inclined to co-operate with Sony by using its standard.

In this context JVC's launch of the VHS (video home system) was a total surprise to Sony. The system adopted many U-standard ideas thanks to the cross-licensing agreement.

Matsushita was forced to choose from among the three alternatives: (1) Beta; (2) VHS, or (3) its own system still to be developed. The viewing took place at JVC's Tokyo head office in Nihonbashi. Konosuke Matsushita picked up the JVC model, commenting on its lower weight. His reason seemed to point to the convenience of selling lighter electrical appliances. Others thought his judgement was based on the convenience of using its subsidiary's standard.

The major difference between Beta and VHS lay in their recording time. Beta lasted for an hour while VHS initially ran for two hours.

Sony lagged in the competition for licensees for its standard. For example, Hitachi visited Sony to discuss a license but the latter's reply was only half-hearted. Sony's pride in its technology could have led to its hubris in relation to possible licensees. For years Morita grudged Konosuke Matsushita's double-cross, which could explain why Sony did not change ships and adopt VHS.[7]

Despite Beta's failure in the standard war Sony benefited from the license payment for its technology used in VHS.

The Beta debacle taught Ohga that success or failure in image devices depended on image software availability. Thus the idea of acquiring Columbia Pictures was its corollary.[8]

Acquisition of Columbia Pictures

Ohga was deeply convinced that the success of the CD business owed much to the acquisition of CBS Records, because it loaded Sony up with a huge library of discs. Ohga and Morita came to believe that the software and hardware businesses supplemented each other.

They regretted the lack of image software to support Sony's video-standard war.

Ohga cherished the idea of acquiring a US film company. Japan's bubble economy was at its zenith. Everybody was buying real estate. At the time

Ohga, who had been hospitalized due to a heart problem, instructed his US staff to look for a film company.

Columbia Pictures came onto the stage.[9] There were candidate companies. Two criteria were used: size of the film library and sale price. Coca Cola, Columbia's parent company, wanted to sell it because the film company had not produced a hit.

Acquisition of Columbia Pictures in September 1989 required assuming its debts. Sony also acquired Peter Goober's firm to recruit him as the top man of the newly acquired firm. Overall Sony paid US $4800 million including US $3400 million to acquire Columbia.[10]

Unlike the acquisition of CBS Records, Sony could not expect partial amortization of the investment from an IPO. The film library needed a longer time-frame to get the money back. Sony's 8-millimetre video (TR55) was a hit that year and did not need any support from the film library.

Columbia Pictures' performance was good in the year of its acquisition but over the following three years it went downhill. Film-making costs shot up but no hits resulted.

Negative opinions prevailed before the acquisition of Columbia Pictures despite Ohga's conviction that the film library would become a cash cow in future.

In the mid-year report in September 1994 Sony was forced to chalk up a consolidated loss of ¥300 billion to depreciate the goodwill as a result of the gap between the acquisition and the evaluated prices. For Ohga this was necessary to pave the way for his successor.

Eight years later Columbia Pictures had recovered and started to generate cash thanks, for example, to hits such as *Spiderman*.

PlayStation (PS)

The combination of software and hardware was nicely harmonized thanks to success in the music and film industries. But Ohga was aware Sony needed one more pillar to support the firm's performance. The video-game device could fill such a need.

The PlayStation video-game device was launched in December 1994, one month after reporting a ¥300 billion loss, due to the Columbia Pictures acquisition. As the video-game industry was dominated by Nintendo, Sony's management, with the exception of Ohga, was against the entry.

In eight years the video-game business had grown to contribute ¥1 trillion in 2002 between software and hardware.[11] If third-party software is included, PS-related business exceeded ¥2 trillion world-wide. The brain behind this success is Ken Kutaragi, president of Sony Computer Entertainment.

Table A3.1 Sony's purpose of incorporation and management policies

Purpose of incorporation	Management policies
To establish an ideal factory that stresses a spirit of freedom and open-mindedness, and where engineers with sincere motivation can exercise their technological skills to the highest level	We shall eliminate any unfair profit-seeking practices, constantly emphasize activities of real substance and seek expansion not only for the sake of size
To reconstruct Japan and to elevate the nation's culture through dynamic technological and manufacturing activities	We shall be as selective as possible in our products and will even welcome technological challenges. We shall focus on highly sophisticated technical products that have great usefulness in society, regardless of the quantity involved. Moreover, we shall avoid any formal demarcation between electronics and mechanics, and shall create our own unique products uniting the two fields, with a determination that other companies cannot overtake
To promptly apply highly advanced technologies which were developed in various sectors during the war to common households	We shall carefully select employees, and our firm shall be comprised of a minimal number of employees. We shall avoid to have formal positions for the mere sake of having them, and shall place emphasis on a person's ability, performance and character, so that each individual can fully exercise his or her abilities and skills

Source: Adapted from Sony Corporation (1996b)

Sony started by supplying sound chips for Nintendo's Super Famicon™. Nintendo was using cartridges to run software, but Sony suggested CDs be used to improve image quality. An agreement was reached to develop the next-generation game device.

To Sony's surprise, in June 1991 Nintendo announced a new product jointly developed with Philips the day following Sony's announcement of launching compatible equipment driven by CD at a Chicago fair.

For Sony it meant major loss of face. When no compromise was struck between Nintendo and Sony, Sony's management committee decided the following year to withdraw from this business. All committee members expressed their conviction that video games were not Sony's business, except for Kutaragi.

Kutaragi's opinion was based on the belief that combining CDs and high-quality chips meant a three-dimensional image could be obtained. This would lead to Sony's market dominance. Ohga was enthused and before realizing it he hit the desk and yelled: 'Do it!'.

PS's success was attributable (1) to use of CDs for memory storage, the larger information storage led to finer graphic images and (2) to ease of production because, unlike cartridges, CDs could be replicated flexibly and at lower cost. The publication of specifications helped too, as any software developers could join the market.

Another reason was the game controller whose shape allowed it to be gripped by users with both hands. Ohga supported it, because, based on his experience as airplane pilot, he knew holding by gripping could occur in any body position.

Ohga was aware Kutaragi, the product's champion, was in an awkward situation due to his superiors' opposition to its development. To help, Ohga asked Sony Music Entertainment (SME, formerly CBS Sony) to rent him and his team a room in its office building in Aoyama. Ohga guessed that the video-game business was similar to the music business and that contact with CBS Sony SME would help Kutaragi and his team replicate success factors of the music business in the video-game business.

Ohga argued PS would allow Sony to take initiatives which otherwise would be in the hands of Intel and Microsoft. PS would enable Sony to establish its own standard combined with its strength in mechatronics – mechanics and electronics.

A NEW PRESIDENT APPOINTED

On the 12th anniversary of his appointment as president, Ohga began to seriously consider selection of his successor. Ibuka had held the position for

21 years, Morita for five years, and Iwama for six years. Sony's sales had reached ¥4 trillion a year. Ohga was 64, a year below the company's 65 age limit.

In April 1994 he divided the company into eight divisions each headed by a president – this was the introduction of the business-group system with each division called a company.[12]

The true purpose of the new system was twofold: (1) to facilitate quick decision making by empowered company presidents and (2) to select Ohga's successor.

Morita suffered an intracerebral haemorrhage in November 1994 while playing tennis, which made selection of the next president a matter of urgency.

Nobuyuki Idei was nominated as the next president in January 1995. Idei was called to Ohga's office and told about the nomination. The candidate pleaded for reconsideration.[13] Idei had been appointed managing director six months before and his nomination meant he was going to jump over all his seniors.

Ohga resigned from Sony's board of directors on 29 January 2003. He had been chairman of the board of directors since June 2000 after resigning as chairman of the firm.

His 'testament' was that (1) Sony should educate new leaders knowledgeable in the software-related business; (2) it should develop new products for the next five years, and (3) it should focus on its brand equity.

NOTES

1. Ohga cited the Chinese character *san* or *can* as explanation of this concept. *San* means brightness, brilliance, radiance, dazzling, glittering, etc. (Takagi, 2001).
2. For Sony's history see www.sony.net/Fun/SH/1-36/h5.html
3. Mainly drawn from Ohga (2003).
4. Ohga emphasizes the timeliness of buying a corporate airplane in 1968, which allowed Sony's Morita to spot a wide tract of land in Shizuoka when he flew between Tokyo and Osaka. Tajima, then chairman of Sony, opposed such an extravagance as an airplane purchase, but Morita was enthused and convinced the directors. Ohga himself obtained a pilot's license in 1972.
5. Ohga remembers Karajan's last moment. He and his wife visited von Karajan in Salzburg 1989 and chatted with him about a new jet plane recently launched by France's Dassau. During the conversation von Karajan passed away. Ohga himself suffered a heart attack the following day in Colon.
6. His immediate predecessor was Kazuo Iwama who was the force behind development of CCD (Charge-Coupled Device which changes light into electric signals and is used in video cameras as 'Eye of Electron') and semiconductors. When Ohga returned to Sony after his stay at CBS Sony he and Iwama shared the office space for board directors. Ohga's role was to approve the budget presented by Iwama who used to tell Ohga the project would not become profitable in the 21st century. Iwama was appointed president in 1976 but died of colon cancer soon after.
7. Ohga, however, always cherished a fond memory of Konosuke Matsushita who treated him almost as a son.

8. In the meantime Ohga had been struggling against his delicate health. In 1989 he developed a heart problem. That year Rokuro Ishikawa, president of the Tokyo Chamber of Commerce died. Ohga, as a vice president of the chamber, deputized for him to attend a conference in Austria. On learning of Ishikawa's decease he flew back to attend the funeral. On the following day Ohga had a heart attack. Four months later he had another in Cologne on the day following von Karajan's passing. Ohga underwent bypass surgery in 1991.
9. 'The acquisition of CBS Records was the result of more than a year of negotiations. At the end of 1986, under instructions from Morita and Ohga, Michael Schulhof who was then vice chairman of SONAM, began discussions with CBS chairman William S. Paley, CBS president Laurence A. Tisch, and CBS Records president Walter R. Yetnikoff. The negotiations, which covered such issues as the price of the acquisition, continued for almost a year before their conclusion in 1987.

   The formal acquisition process began as soon as an agreement was reached. Toshio Sakai, who was then senior managing director and general manager of the Accounting division, led Sony's team of lawyers and other specialists who negotiated with CBS through the maze of legal and financial procedures. Like Sony, CBS had assembled a large team to conduct the negotiations. Because Sony was acquiring 100 per cent of CBS Records' assets including all personnel, everything relating to the deal had to be worked out in painstaking detail to avoid any problems later. Each team was divided into smaller groups to grapple with specific issues. After a month of exhausting negotiations that often continued through the night, all loose ends were finally tied up, and CBS Records with operations in 40 countries around the world was a member of the Sony family.

   The acquisition of Columbia Pictures took place next. Unlike the CBS Records deal, there was no protracted period of negotiation between the two companies. Once the Columbia Pictures board of directors agreed to the acquisition, Sony made a cash tender offer for all of the outstanding company shares. What did take time, however, was deciding how to manage the movie company once it had been acquired. Purchasing Columbia Pictures cost Sony US $3.4 billion, which was the largest purchase ever by a Japanese company. But when considered in conjunction with the acquisition of CBS Records, this purchase gave Sony control of vast assets in terms of music and motion picture content.'
10. This operation coincided with Mitsubishi Real Estate's acquisition of the Rockefeller Center in New York, which 'sensitized' US public opinion against Japan. *Newsweek* published a special number on Japan's move into Hollywood.
11. Contrary to this success in video-game equipment, Sony's struggle in the computer industry was strenuous. Sony entered the computer industry in the 1960s with a desktop calculator, the world's first of its kind, but was forced to exit. In the 1980s it had a brief moment of success with MSX home PC and NEWS workstation but was again forced to exit the market.
12. For Sony's history see www.sony.net/Fun/SH/1-36/h5.html
13. Takagi (2001) cites Idei: 'I was aware that it would be next to impossible to manage Sony. Sony had been a firm run on the basis of the founders' vision … In other companies there is a separation between the owner's figure and managers'. But not so at Sony. Ohga was not an owner but he had behaved as if he were. His logic had always been that of an owner'.

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Yahagi T. (1996), Sony Kabushiki Kaisha (B) – Sony wo sasaeta keiesha (Sony Corporation (B) – the Top Managers who Supported it), Keio Business School.

A4. Shin-Etsu Chemicals' Chihiro Kanagawa

In his autobiography, Jack Welch (2001) the former CEO of GE, cited Shin-Etsu Chemicals' Chihiro Kanagawa as one of the excellent top managers in Japan who was courageous enough to push forward their company's continual renewal.[1]

Welch's praise was borne out by Kanagawa's remarkable performance as Shin-Etsu's president. Over his 12-year presidency the market capitalization of his firm reached ¥1598 billion in October 2002, up ¥1142 billion from August 1990.[2] Shin-Etsu Chemicals' profit was 9.16 per cent of sales in 2001 and its ratio of net worth to total capital reached 63.03 per cent. (Niihara, 2002).

This is an outstanding feat of managerial creativity in a commodity-based low-technology industry such as the chemical industry. Traditionally Japan had not been able to compete with the giants, namely Dupont, Dow Chemical, BASF, and Bayer. With 16456 employees (consolidated base) in 2002 Shin-Etsu was on par with these competitors where market capitalization was concerned.

This case focuses on Chihiro Kanagawa, the wonder worker in an industry where Japan had been unable to produce a world-class competitor, who continued to achieve record performance during the Japanese recession of the 1990s and 2000s.[3] His management 'philosophy' will be set out below.

CHILDHOOD AND SCHOOL DAYS

Kanagawa was born in 1926 in Korea where his father served as a judge. He was brought up there until he moved to Okayama, Japan, to enter the Sixth High School.

Okayama was destroyed by a US air attack on 29 June 1945. He and his classmates tried to save their hall of residence from incendiary bombs. His roommate was hit directly by a bomb and died. Kanagawa himself was hurt by a shell but survived. He came to believe luck was integral to both personal and business life (Kanagawa, 2002). For him competent managers could take advantage of their luck.

Japan's defeat in World War II shocked him, as with many youths of his age. In searching for an answer to the question of why Japan lost the war and how it should recover, he read many history books.

JOINING KYOKUTO BUSSAN, A TRADING FIRM

In 1950, he graduated from the University of Tokyo with a degree in political sciences and joined Kyokuto Bussan, which had been split from Mitsui & Company because of the demerger of *zaibatsus*[4] by order of the occupying army.

Kyokuto was mainly engaged in trading foodstuffs. Kanagawa still has fond memories of the company as it trained him as a professional and allowed staff to have their own opinions (Nihei, 2002).

Ten years after he joined Kyokuto it merged with Mitsui & Co. Kanagawa worked in the alloyed metal department. He concluded human relations would be complicated in the merged firm as Mitsui's size was ten times greater than Kyokuto's. As larger and stronger merger partners tend to dominate smaller ones, his promotion chances would depend largely on whether he had the right sort of friends and superiors from the winning party.

At 36, after consulting a superior, Kanagawa decided to switch companies and entered Shin-Etsu Chemicals. In choosing a new company, he felt the business he chose should take risks, invest, and manufacture something tangible (Nihei, 2002). Accordingly, he chose a manufacturing firm.

JOINING SHIN-ETSU CHEMICALS

In the new company, he was assigned to manage overseas businesses. At that stage, Shin-Etsu conducted little overseas business, this meant Kanagawa could start from scratch, designing strategy and implementing it himself. Between the 1960s and the 1970s he visited over 100 countries on business, which taught him how difficult it was to compete abroad and the importance of country risk assessment (Nihei, 2002).

It was the 1976 takeover of Shintech,[5] its US subsidiary, which was decisive, laying the foundation for Shin-Etsu Chemicals' current success. Shintech's US partner proposed to sell its stake for between US $12 and 13 million, Odagiri who was Shin-Etsu's president gave Kanagawa unconditional support despite all-out opposition from other board members. Kanagawa, then senior manager in charge of overseas businesses, knew that Shintech could be a 'hen laying golden eggs'.

Shintaro Odagiri was Kanagawa's protector and mentor. Even so, Odagiri's

support was surprising. The proposed price was ¥3 billion at a time when Shin-Etsu's ordinary profit was around ¥600 million. Thus the board's reluctance was understandable. Moreover, the firm was still suffering from the after effects of the energy crisis.

SHINTECH'S PRESIDENT

Kanagawa was seconded to the US in 1978 to be Shintech's president. Upon arriving, he emphasized how important it was to comply with delivery deadlines (Mayumi, Nishigashira and Tomioka, 2002). Vinyl chloride prices were rock-bottom in the 1980s which had driven many competitors away,[6] but Shintech persisted and by 1991 it had become the world's largest producer (Shimizu, 2002). With a 3.9 million-ton production capacity, in 2003 its global market share was 13 per cent, with 26 per cent and 20 per cent of US and Japanese markets respectively (Zaikai, 2002).

Kanagawa saw a future for vinyl chloride, because, though it had become a commodity after 40 or 50 years, it had many uses – pipes and window frames for housing, bags for blood transfusions, syringes, etc. More importantly it had few significant side-effects.

In 1986 Shintech benefited from the Reagan administration's tax cuts, which helped boost the US economy. It was a windfall for the company because the vinyl chloride market which had been depressed since 1980, had started to improve. Corporate US tax was cut from 46 per cent in 1986 to 34 per cent in 1988. By this time Shintech recorded over US$100 million profit, which allowed it to write off all its borrowings (Shimizu, 2002).

Koichi Saito, an analyst at Daiwa Research, commented (Nihei, 2002, p. 103): 'Vinyl chloride is a commodity. Basically, everybody produces the same quality. The condition to win lies in increasing profit by keeping a tight rein on sales and product costs. I admire Kanagawa-san because he managed to do so by increasing production without adding more personnel.[7]

Kanagawa advocated minimizing total costs; competitors focused on maximizing productivity but forgot that cost reduction should also be pursued at the level of production, distribution, overheads, etc. Thus, reduction of per-unit raw materials costs was the goal. The result was that independence from borrowed money was almost complete which reduced the interest burden (Maeda, 2002).

Kanagawa's strategy meant beating off competitors through establishing long-term customer contracts. Increased production capacity was always based on correct readings of market trend so that excess production might be avoided. Profit maximization was pursued and never sacrificed to gain market share.

APPOINTMENT AS PRESIDENT OF SHIN-ETSU

In 1990, Kanagawa was appointed president of Shin-Etsu Chemicals while still holding the position of CEO at Shintech.

Ever since Shin-Etsu Chemicals has outperformed all competitors in Japan. In February 2002, its market capitalization was ¥1.8 trillion, a figure in excess of the market capitalization of Mitsubishi Chemical, Mitsui Chemical, and Sumitomo Chemical combined together (Shimizu, 2002). (See Table A4.1 for Shin-Etsu's main business lines).

Focus in the Business Domain

As Shin-Etsu only produces and markets products in which it can successfully compete, it is the world number one in silicon wafers and vinyl chloride, number three in silicone resins, and number two in materials for optical fibers.

Table A4.1 Shin-Etsu Chemicals' main products

Business	Product name
Organic and inorganic chemicals business	• Polyvinyl chloride (PVC) • Silicons • Methanol • Chloromethane • Cellulose derivatives • Caustic soda • Silicon metal
Electronics materials business	• Semiconductor silicon • Organic materials for electronics industry use • Rare earth magnets for electronics industry use • Photo resists
Functional materials and other business	• Synthetic quartz • Oxide single crystals • Rare earths • Rare earth magnets • Technology and plant exports • Export and imports of products

Source: http://www.shinetsu.co.jp/e/profile/

Kanagawa estimated Japan's production capacity of vinyl chloride to be 2 million tons with demand around 1.5 million tons in 2002 (Nomura, 2002). The price war came from this disparity. Even firms not breaking even pushed the price down. It was his opinion that only the fittest would survive.

His focus is supported by perseverance and determination. Thus in February 2001 Shin-Etsu invested ¥70 billion in installations for production of 300-millimeter diameter silicon wafers. In view of falling demand for semiconductors, other companies were more cautious and did not dare invest in production expansion. But Kanagawa went forward with the investment plan in the belief that semiconductor producers would demand 300-millimeter diameter silicon wafers due to halving of production costs. This decision gave Shin-Etsu ten months' head start over its competitors (Shimizu, 2002).

Kanagawa Premium

Shin-Etsu's looming problem was finding a successor to Kanagawa who was 76 years old in 2003. Kanagawa takes all important decisions about running the show. Shin-Etsu's share price was thought to include the 'Kanagawa premium' (Mayumi *et al*., 2002). The question became, in replacing himself, would Kanagawa prefer to leave team-led management or find a second Kanagawa?

Kanagawa was optimistic regarding this issue. 'I am concerned about the selection of my successor. I have on my mind several candidates I have spotted in the process of our business diversification,' and, 'I may be at the wheel until I am a hundred years old' (Shimizu, 2002, p. 43).[8]

Kanagawa's view was sending managers with potential to subsidiaries as their top people served nicely to nurture future leaders, a departure from the traditional Japanese view (Maeda, 2002). This was also different to traditional Japanese personnel policy where managers who fell out of competition for the top position were sent to subsidiaries. Kanagawa maintained that even if size differed, running a firm was not qualitatively different between parent and subsidiary companies.

CHIHIRO KANAGAWA'S MANAGEMENT PHILOSOPHY

Always Provide for the Worst Case

The current business environment is characterized by constant change. Managers, to survive in this changing environment, have to be prepared for any change which may occur. If they prepare for the worst case, so much the better (Kanagawa, 2002).

Global competitiveness is indispensable for a firm's survival. As mentioned previously, Shin-Etsu is world number one in vinyl chloride and silicon wafers for semiconductors and number three in silicon resins (number one in Japan). This results from constant productivity and technology improvements. Amazingly this productivity excellence at Shin-Etsu has been achieved with just 230 staff.

A significant issue is balanced business deployment. To explain, new electronic and optical fiber businesses may experience rapid growth, however are subject to great variability. This means dependence on them will not provide stable profit levels. This is why Shin-Etsu sets store by old businesses such as vinyl chloride and silicon resins to smooth out fluctuation in new business items.

However firms' top people must be able to read business trends ahead of time and act quickly (Kanagawa, 2002).

CEOs' Only Bosses are Shareholders

For-profit organizations are normally private entities. Their only owners are shareholders. Therefore, CEOs' bosses are shareholders, not employees. The employees are part of the firm, and CEOs should always remember employees are hired people. Otherwise, even CEOs could become confused and might deceive themselves into thinking their firms exist for employees.

Nonetheless, motivated employees are essential for firms to make money and to remunerate shareholders. The company's objective is not to make a huge amount of money for the CEO nor to provide welfare to employees, but to compensate shareholders by strengthening the firm. If employees are unhappy this objective will not be achieved. This requires keeping the means and the objective separate (Kanagawa, 2002).

Achievement of the objective does not depend just on employees. Financing, R&D, marketing, most competitive production technology, environmental measures, product liability (PL) issues, etc., must be duly taken care of by CEOs and management to provide appropriate grounds for the firm to prosper.

Achievement of the firm's objective does not preclude observance of social ethics and a code of behavior as a social citizen. Shin-Etsu has as one of its first principles compliance with the spirit of law.

A private firm that prospers contributes to the society through payment of corporate taxes. Nowadays the effective rate of corporate tax in Japan is 40 per cent but until recently, it was 50 per cent. Accordingly, firms making ¥50 billion contributed ¥25 billion to society.

What one should remember is that the contribution to society is a result, not the objective of the firm's existence. Kanagawa deems it hypocritical of

managers when they hold that the reason their firms exist is for society or employees.

A private firm exists to make profit. Shareholders have trusted managers to handle their money. It is understood CEOs are bound to fulfill their trust by contributing a return on their investment.

Be Cool-headed in the Midst of Turmoil

Kanagawa (2002) is wary of the opinion that his management style is more American than Japanese. He refutes it by citing his habit of keeping a cool head or judgment amidst market turbulence. A case in point is set out below.

In 1999, the US vinyl chloride market was overheated. Kanagawa thought the trend would turn and instructed his staff to renegotiate contracts with customers for a longer term and at a higher price. Such renegotiations usually took place later in the year, but Kanagawa wanted to carry them out before summer during the seller's market. Product supply was short and customers were willing to pay more; Kanagawa predicted demand would fall in the following year.

Kanagawa's idea was to make 'savings' as much as possible while the market allowed it, to prepare for the market downturn. Savings gained meant non-performing customer debts could be written off (Kanagawa, 2002).

The Old Economy is Important

Kanagawa saw a further difference between American and European managers, in their handling of old-economy products.

He believed many US CEOs tend to prefer new and fashionable products while shedding old-economy products in hopes of becoming the hero of the moment.

In the case of Shin-Etsu, the fertilizer business fell into this category. It was one of the original businesses the firm started with. It was relatively small, no brilliant future was predicted for it and many suggested it be discontinued or sold off.

Kanagawa put up with the pressure and kept the fertilizer company for 12 years after his appointment as president, on the grounds that it contributed yearly ¥100–300 million, which meant that in 12 years it added almost ¥2 billion to the bottom line.

If Kanagawa were to sell the business it would be because the business's profit-making possibility seemed to peter out. For him a business should be kept while it generates cash flow. He is keenly aware how hard it is to make money with new businesses.[9]

Vinyl chloride is also an old-economy business. It is obviously a low-technology product and many environmentalists attack it as being the generator of dioxin. All said and done, however, its market is growing 3 to 4 per cent a year globally. Moreover, it is one of the most solid profit-making products at Shin-Etsu. Therefore, Kanagawa (2002) sees no reason to drop it.

Instead of a 100-year Plan, Short-term Daily Issues

CEOs cannot use the economic downturn as an excuse for their companies' poor performance. After a boom period, a recession always follows. CEOs must prepare for the next downturn.

Some argue CEOs should not focus on today's issues but on longer-term ones because their task is to set in place a long-term vision and plan. Kanagawa is against such an argument.[10]

He wonders how somebody can plan ahead if they are incapable of sorting out today's problem.[11] He cites Admiral Isoroku Yamamoto's motto: 'One is always on the battle ground' (Kawashima and Tamara, 2003, p. 86).[12]

While he does not deny the need to develop a longer-term plan, Kanagawa's conviction is that a long-term vision comes as an accumulation of daily works. For development of a new business, a lack of such a plan will make it useless.

However, focusing on short-term, daily issues tends to lead the CEO to a certain bias on the future and influences their long-term plan. A caveat should be made here, the market will never ever move in the direction one wants it to move.

Kanagawa bases his forecast on the market but shies away from making a plan based on it. Even if he makes one, he tries to foresee a scenario worse than his forecast. He maps out a plan to work out actions in preparation for the worse or worst situation.

Indicators for Management

Kanagawa's idea about finances is simple:[13] (1) minimize interest-bearing debts;[14] (2) keep the pay-out rate for dividend as low as possible, since after all it's in shareholders' interest if the company's long-term growth is steady; (3) set a ROE target of 10 per cent, this compares with the current 9 per cent, but he does not deify the 10 per cent figure nor does he intend to increase its treasury shares, and (4) the clearest indicator of the company's achievement is net income, on the basis that everything depends whether the firm's quarterly net income constantly grows, or not.

Generated Cash should not be Wasted

Over the last few years, Shin-Etsu Chemicals has had cash flows around ¥130 billion every year. Kanagawa was pressured to use them for new investment but he is adamant – unless one is cock-sure that success is a high probability, do not waste them on a new business.

Kanagawa also avoids buying back Shin-Etsu's shares to increase ROE and he does not want to have stock options, either. Holding available cash on hand always helps when an investment chance crops up.

Kanagawa is critical of his US counterparts who tend to use up stashed money for M&A operations. It may temporarily increase the firm's share price, say, to US$100 but many times it ends up by falling to the level of US$1, portending a disaster for both shareholders and CEO.

Fast Decision Making

Kanagawa (2002) is proud of taking the majority of decisions in 30 seconds. Of ten proposals he gives immediate comment or decision on eight or nine issues. He never puts off the decision making to consult the board (that meets once every other week).

For tons of documents that find their way to his desk, he spends a few seconds on each one and goes quickly through it. He sets aside those requiring further study. If the explanation on the document is lengthy he asks the person who wrote it to give him a brief verbal explanation.

The case of 300-millimeter diameter silicon wafers was referred to above. The launching to the market of this product in February 2001 had ten months' lead over other competitors, which enabled Shin-Etsu Chemicals to enjoy a 60 per cent global market share.

Kanagawa had observed a year earlier how quickly the market was heating up towards October 2000. He judged the boom would not last more than six months and decided Shin-Etsu had to enter the market before it started its downward trend.

Kanagawa (2002) did not consult the board of directors for the decision. He thought that speed was everything and he could not jeopardize the business chance by listening to generic discussions. Therefore, he gathered some informed opinions and approved the investment plan on his exclusive responsibility.

He instructed his engineers to commission new production facilities in three months. For such a situation Shin-Etsu have several specialized engineer teams who can carry out a plant construction project in a few months covering from the design of the plant layout, purchase of machinery, construction, test-run to the commissioning.

Concentration on Heartland Businesses

At the time of Japan's bubble economy years (1990s) he received a proposal to build and manage a business hotel in Takefu in Fukui prefecture. The proponents urged Kanagawa to approve the plan alleging that everybody including the chairman was in its favor.

Kanagawa immediately and flatly rejected the plan. This was one of the few cases in which he vetoed a business plan. He reasoned that Shin-Etsu did not have any expertise or resources to enter a hotel business. Run by the firm the hotel would be a second-rate or third-rate hotel. Its location would not help, either. It is removed from urban areas such as Tokyo or Osaka. Kanagawa's guess was that if the firm took up the plan it would have lost ¥20 billion to 30 billion. The business atmosphere in Japan favored such a venture and everybody was doing it.

Kanagawa likewise prohibited his staff from speculating in financial markets doing what was known as *zaitekku* (financial engineering). He was quite clear on this point: the firm did not have expertise to speculate in financial markets. The *zaitekku* was the nemesis of many a Japanese firm in later years.

FIGHT TO CHANGE THE FIRM

Prerequisites for a Transformational CEO

Kanagawa (2002) opines there are two prerequisites for a person who manages to change their firm: (1) they have to have clear objectives regarding how to change it, and (2) they must be capable of analyzing reality.

He more than satisfies both prerequisites. His objective is clear: to strengthen the firm's financial structure so that it could survive any economic downturn. The force working against 'restructuring' or strengthening the firm was bureaucracy and inherited customs – working by rote and observance of precedent. Combating this force is where the second prerequisite was needed.

To address the problem of eliminating bureaucracy and inherited vices which were many in a firm established in 1926, Kanagawa, upon taking charge of the presidency, developed an effort to change people's mind-set: to call into question accepted wisdom.

The accepted wisdom regarding work was that hard-working, pure donkeywork or drudgery would pay. Challenged by an important task, his younger staff tended to rush headlong into the fray. Kanagawa made it a habit to tell them that they did not have to attempt to achieve results by dint of mere physical hard work. Instead, he emphasized the importance of designing

a creative and imaginative plan. He insisted on quality, not quantity of labor.

Another component of the accepted wisdom was the observance of established ways of doing business. The turn-around of the domestic vinyl chloride operation was an example.

After successfully turning around Shintech in the US, Kanagawa was requested in 1982 by his president to repeat the feat with the domestic vinyl chloride operation in two years.

The first hurdle was how to persuade his staff to renegotiate the purchase price of chlorine. The purchase contract had been signed with a supplier in the Kashima industry complex. Some felt the need to renegotiate but the majority preferred to respect the agreed-upon terms and price because of personal relations and the belief that an agreement should be honored, rain or shine.

Kanagawa personally visited the supplier several times and stressed that the environment had changed because of the energy crisis and that unless the terms of purchase were changed, Shin-Etsu's operation would be forced to close down. The supplier would not compromise. Therefore, Kanagawa finally decided to fight in the courts. Until the verdict was handed down, Shin-Etsu would not comply with the contract. The supplier ended up by accepting Shin-Etsu's proposal.

Once the chlorine purchase issue was sorted out, Kanagawa undertook to rationalize the transport, and to widen the supply source by importing raw materials, all of which resulted in halving of production costs.

Further measures he adopted included 'focus and elimination' of customers and closure of a plant.

Organizational Structure

The fight against bureaucracy was at its severest in Kanagawa's plan to change how the organization was run, especially, in issues related to personnel because of the sway the personnel department held.

Kanagawa thought it absurd for Shin-Etsu to employ 600 new college graduates every year. The personnel department considered the contracting of new graduates to be their exclusive privilege. For Kanagawa this was a confusion of one's role with one's acquired right.

Kanagawa instructed the divisions to submit their need for new graduates. There again, he found the divisions erroneously thought the number of new graduates reflected their relative importance in the firm. Therefore he decided not to employ any graduates the year he took charge as president to drive home the fact that unnecessary staff would push down productivity and push up personnel cost.

Be that as it may, Kanagawa generally took care not to devolve too much influence to the personnel department. He firmly believed personnel-related

decisions should be handled by line managers who would know their personnel better than the personnel department. The centralization of power in the personnel department was to be avoided at all costs: the department does not know how each individual staff member on the line behaves – because of this, a mere rumor, hearsay, complaint filed with the personnel department against somebody might lead to a poor decision.

Central to the personnel issue is the education of future leaders. Kanagawa is against job rotation for its own sake. He maintains his staff must be professionals. Such professionals can only be trained by letting them stay in a job for a long time. This does not contradict the main purpose of job rotation – to expose somebody to many different positions and tasks – since it will be achieved even if a person is not rotated from one assignment to another. If they are good in a job assignment, they must perforce be good in another assignment. Staying in a job assignment teaches them not only the special knowledge involved in it but also other more universal issues such as judgment, implementation skills, etc.

Only Count on the Chosen Few

Shintech is the world number one vinyl chloride producer, headquartered in Texas. Its production capacity is 2.3 million tons, which is almost equivalent to Japan's total production capacity – 2.5 million tons.

In Japan, Kanagawa guesses there are 2000 people engaged in the production and marketing of vinyl chloride among nine producers, trading companies, wholesalers, etc. This number contrasts with Shintech's 230 staff. The productivity is in favor of Shintech in an 8 to 1 ratio.

An almost-commodity item such as vinyl chloride requires severe cost control, which is the only way to survive. Shintech is the only firm in the world in the industry making money on this item.

No superfluous personnel exist at Shintech.[15] It has only ten salespeople who travel around the world. No unnecessary indirect personnel exist, either. Collection and control of accounts receivable is in the charge of Kanagawa's secretary. She only received minimum necessary training: to advise customers ten days ahead of payment-due dates, remind them of delayed payments, etc.

Shintech does not have any financial specialist on its payroll. Kanagawa does not think the firm needs any financial staff since its equity ratio is 89 per cent. Almost no debt, therefore, there is no need for a financial specialist.

Kanagawa even today regrets the ¥4 billion the firm spent on its corporate identity campaign. The spending went on sponsoring motorcycle competitions, TV commercials, etc. His assessment is negative: nothing was got from the CI campaign. It hurts him to think that with ¥4 billion the firm

would have been able to build two research laboratories. His excuse is he was only a vice president and could not dissuade his president not to do it.

In line with this thought, Kanagawa (2002) is against moving into a new headquarters building and insists on staying in a rented office building the firm has. Thanks to a ¥300 billion cash chest Shin-Etsu may have a new building constructed. What terrifies Kanagawa is the loss of time and energy for the moving – a month spent on it might be better used for the development of a new business.

LEADERSHIP QUALITIES

Five Qualities

Kanagawa (2002) enumerates five leadership qualities; (1) judgment; (2) foresight; (3) decision; (4) implementation, and (5) character.

Judgment is necessary to analyze the situation and reality. Foresight helps to predict the future ahead of competitors. Decision making is indispensable to change the reality, but it needs somebody with skills and capability to implement it.

Kanagawa regards the majority of these qualities as inborn factors, especially judgment and foresight.

Even if a person is blessed with these qualities, without sincerity and warmth towards other people, someone will be a failure as CEO.

Be Afraid of Failures

Kanagawa is critical of Japan's accepted wisdom, which is permissive of failures or errors committed by younger staff.[16] Originally, it meant one had to be daring if one wanted results. It tends to imply, however, that losses are unimportant compared with the value of the lesson learnt.

Kanagawa is not against giving a chance to managers with potential. When he discovers such a manager he gives them an assignment beyond their past experience. The gist of the message is that a CEO has to be capable of discerning people with potential and give them a chance, not to everybody thus risking the company's fate.

Importance of IR (Investor Relations)

Ever since Kanagawa was requested by financial analysts to explain his company some years ago, Kanagawa made it a point to attend as many meetings with analysts as possible. In 2001 he met in total 1200 analysts and

investors. Analysts transmit key information to investors and shareholders. As such they have to be respected.

Luck

Kanagawa holds there are things one cannot do anything about – the will and effort cannot change them. Inspiration and luck are two of these things.

Kanagawa suspects that he was always favored by luck. He applied for entrance to the Army's cadet academy and failed. If he had been admitted, he might have been sent to the battlefield and perished young.

He was hit by bombshells during the war. However, his wound was not fatal unlike that of a friend of his who was hit directly by an incendiary bomb and died instantly.

Kanagawa realized successful managers had been lucky and inspired at key moments and been capable of taking advantage of it. Therefore, luck, inspiration or 'sense for business' are key issues in management for him.

NOTES

1. Nippon Keizai Shimbun, 31 October 2001.
2. Nippon Keizai Shimbun, 15 November 2002. Consolidated ordinary profit estimated at ¥151 billion for the fiscal year ending in March 2005, a 20 per cent increase over the previous year. Sales will be ¥930 billion, up 12 per cent (Nippon Keizai Shimbun, 10 October 2004).
3. Sawato (2000) predicted in the chemical industry Japan's survivors would only be Shin-Etsu Chemicals, Fuji Film, and Mitsubishi Chemical.
4. 'A powerful financial and industrial conglomerate of Japan' (*Merriam-Webster Unabridged Dictionary*, ver. 3).
5. A US joint venture started in 1973 to produce vinyl chloride at Chihiro's initiative. Its partner, Robintech, due to its poor performance, was forced to sell its stake in the joint venture (Mayumi, Nishigashira and Tomioka, 2002).
6. According to Mayumi *et al*. (2002), there were 21 companies producing vinyl chloride in the US in 1974, but only seven of them still in this business in 2001.
7. Translated by the authors.
8. Translated by the authors.
9. 'It would take at least ten years for a new business to start to generate ¥100–200 million profit … It's not easy to be successful in a new business' (Nomura 2002, p. 48) [translated by the authors].
10. 'In entering a new business, you have to be careful not to make mistakes in day-to-day operations. Even if the direction you set was right, the business will not succeed if the day-to-day operations were not correctly conducted. However, if the direction was wrong, then the day-to-day operations would not go well, either … I usually keep a close watch until the business starts to run smoothly' (Kawashima and Tamara, 2003, p. 85) [translated by the authors].
11. '… It's useless to make a mid-term plan. You can prepare a beautiful plan by increasing the sale price and lowering the cost of goods sold. Why can you forecast for three years if you don't even know what will happen next year?' (Nomura, 2002, p. 50) [translated by the authors].
12. Translated by the authors.
13. 'I look at performance figures everyday myself. Figures are the lifeline of a firm. You don't

need managers who don't take the trouble of analysing them … Apart from figures, you have to use your sense of smell. When a bad situation is reflected in the figures, it's too late. You have to strain to detect it before it becomes too bad' (Yamagata and Tamara, 2001, p. 60) [translated by the authors].

14. 'When I took over as president the equity ratio was 38 per cent on a consolidated basis. In 2002 it was 63 per cent' (Kanagawa, 2002, p. 20) [translated by the authors].
15. 'Business is about how to handle people and get the best from them. You have to let them have a chance to learn. If I see a person is capable, I give him a large assignment. Ten or twenty of them will change the firm' (Yamagata and Tawara, 2001, p. 63)
16. In Japanese, '*mukokizu wo osoreruna*' – 'don't be afraid of a scar on the forehead' [translated by the authors].

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