

Twenty-Seven Years in Japan – A Report and Personal Account

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I.

I first went out to live in Japan in 1918, as a boy of ten, when my father had accepted the position of Chief Engineer of the Asano Cement Co. at Yokohama. Yokohama had been opened to the West at the beginning of July, 1859, and an international settlement created there. Until July of 1899 foreigners were protected by extraterritoriality laws under which they were tried in consular courts of their own nationality rather than by Japanese judges. Foreigners could not live outside of the Treaty Ports without obtaining specific approval of the Japanese authorities.

The Japanese resented the extraterritorial rights enjoyed by Western powers, as these rights impinged on Japanese sovereignty. In a sense, the international settlements in Nagasaki, Kobe, Osaka, Yokohama and Tokyo were alien enclaves in Japanese territory. The foreign residents had mixed feelings about this extraterritoriality. Although it was comforting to some to be judged by their fellow countrymen, others regarded this as of doubtful benefit. One of the objections to the extraterritoriality laws was that they kept foreigners from establishing factories outside of the international settlements.

In July, 1899 the extraterritoriality laws were abolished by international agreement. On that date foreigners commenced a new life outside the confines of their settlements. The first new firm to be established was the Nippon Electric Company. In 1898 Japanese capitalists and the American owned International Western Electric Co. agreed to establish a joint venture for the purpose of manufacturing telephone and telegraph apparatus; in 1899 it went into business.

The International Western Electric Co. was the manufacturing arm of the American Telephone and Telegraph Co. The patents of Alexander Graham Bell went to this company, and because of its success the Bell System was able to grow rapidly. Investments were made overseas in factories. The Bell Telephone Manufacturing Co. of Antwerp was one. Other investments were made in the United Kingdom, Germany, Spain, France etc. In Japan the International Western Electric Co. owned about 57 per cent of the stock of the Nippon Electric Co.; Messrs. Iwadare and Masujima were among the principal Japanese shareholders. I saw the Nippon Electric Co. many times, because the zaibatsu president, Soichiro Asano, for whom my father worked, had his palace nearby.

In the autumn of 1922 my father decided to quit his position with the Asano Cement Co., and return to the United States. Under his contract he had to give Soichiro Asano six month's notice. The reason for his departure was "fear of a great earthquake". We arrived back in Chicago on August 16, 1923. On September 1st, 1923 the Great Earthquake struck the Tokyo-Yokohama-Odawara axis; about 200,000 people were killed or reported missing, our home in Yokohama collapsed.

When I graduated from college I joined a subsidiary of the American Telephone and Telegraph Co. (ATT). I worked for this company until the beginning of 1946 when I was sent to Japan to aid Mac Arthur in rehabilitating the Japanese telephone and telegraph system. When the Occupation was drawing to a close I returned to the United States and joined the Kellogg Switchboard and Supply Co. of Chicago, then in the process of being merged into the International Telephone and Telegraph Corporation (ITT). The ITT had been founded by a pair of half French half Danish brothers named Behn in 1920 to provide telephone service in the Caribbean Sea countries. When the ATT decided to rid itself of the

International Western Electric Co., the Behns merged it with ITT, and called it the International Standard Electric Co. The Nippon Electric Co. thus came under the control of ITT (in 1925).

I revisited Japan in 1952, 1953 and 1955, and in January 1956, I was asked to go to Japan in charge of the interests of ISE in the Far East.

II.

The Nippon Electric Co. in 1956 was no longer fully controlled by ITT. The percentage of shares held had fallen from 57 to about 33. Still, as shareholder's representative, and a director, I was expected to express my views and do what I could to help the company. No other single shareholder owned more than 6 per cent of the stock, and when shareholders' meetings were held each May and November I found that the shares I voted were approximately half of the total. Many of the small Japanese shareholders did not send in their proxies. Thus ITT's position was stronger than the 33 per cent shareholding would have indicated.

In 1955, the year before I joined the Nippon Electric Co. board of directors, NEC's sales had totalled about \$34,000,000. I have now been on the board for nearly seventeen years, and sales have risen steadily. In this fiscal year (1972) consolidated sales will run about \$900,000,000. Profits have gone up at the same rate as sales. Despite the rises and drops of the business cycle, during these seventeen years the company has earned its dividend in all but one semester. Most of the time net profits exceeded dividends by 100 per cent or more. The surpluses were plowed back into the business.

Nippon Electric Co. has risen to this height through internal growth. It is not common in Japan to merge, although it is done. During these seventeen years NEC has not made any important acquisitions. Growth thus has not come from take-overs or financial manipulation. It has come about through the efforts of the Japanese officers and employees. I have witnessed Japan's amazing growth not as an outsider, but from the vantage point of an insider, a director. I read and hear many theories about the growth. I have my own ideas.

Let us look into the workings of a Japanese company. Kazuo Kitagawa, long time president, and now chairman of the Sumitomo Electric Industries Co. rose to power through his skill as an engineer, so did Koji Kobayashi, president of the Nippon Electric Co. Both men are superbly competent. So is Isamu Sakamoto, president of the Sumitomo Electric Industries Co. A common characteristic of the three is "openmindedness". This is a national trait, and distinguishes the Japanese from some of their conservative Oriental neighbors. Ideas in a Japanese company, for the most part, come from bottom up, rather than from top down. If a young engineer in the Sumitomo Electric Industries Co. learns of a new process for making wire and cable developed in Germany, for example, he will learn as much about it as he can from publications and pamphlets. He will then discuss it with his Kacho (Section Chief). A conference will be called made up of members of the Section. They will consider the process, and decide to delegate responsibility for further investigation to a sub-committee. The sub-committee will explore other sources of information and also discuss it with concerned department of the Ministry of International Trade and Industry. MITI may have a file on the process, but if not, will soon build up one. In time, the sub-committee will have exhausted their local sources, and meet again with the Section Chief. If by now it has been determined that the process is worthy of further consideration the matter will be taken up with the Section Chief's boss, the Bucho (or Division General Manager). Other conferences will be called involving people at higher levels than the Section Chief. Soon word will come down to make direct inquiries of the German firm that developed the process.

The Japanese assigned the responsibility of talking to the Germans will be extraordinarily thorough in their inquiries. Having already researched the subject they will know what questions to ask. They will tenaciously dig into the subject, and in time have a deep understanding. They will want to see the process in operation. They will take copious notes.

Usually the Japanese make their investigations as members of teams rather than individually. There are good reasons for this. One is language. Japanese are not noted for their linguistic skills. When meeting with foreigners, each Japanese will listen intently to what is said, and what the interpreter says, and note this in his note book. After the meeting the members of the team will compare notes. If there are major differences, the matter will be raised at a subsequent meeting.

The Japanese make their investigations as members of teams for another reason. It is in order to make responsibility for decision a collective one, rather than an individual one. In such a case, if the decision proved right the one making it might get swelled headed. If it proved wrong, his job would be in jeopardy. The Japanese do not like for individuals to be singled out either for praise or blame. A part of it comes from Buddhist philosophy. Japanese Buddhists are much influenced by a teaching called *Shujo no on*. This teaching is that each man must feel an obligation to society as a whole for whatever successes he enjoys. Even in the Japanese language, this philosophy is present. It is rare for a Japanese to say "I" or "me" when he is talking. He also deprecates in his speech whatever relates to him. The whole idea is to suppress individual selfishness. This is one of the keystones of Buddhism.

III.

The chief difficulties Occidentals encounter in cooperating with the Japanese are cultural. The Japanese prefer ambiguity to being specific. Their language itself promotes ambiguity. Westerners when negotiating an agreement try to specify clearly who will do what and when and how. The Japanese like to have some margins for changes in circumstances. A contract in Japanese eyes is a declaration of intention based upon known conditions at the time of signing. If conditions change, they feel the contracting parties should be flexible enough to change too. As long as the parties to an agreement are honorable the Japanese philosophy works admirably. But what about an agreement where one of the parties is by nature overly selfish, or unfair? The Japanese answer to that is "don't do business with such people".

In an old country like Japan, where firms have established their reputations through giving good service for a long period, it is possible in many instances to be reasonably sure of the fairness of managements. Japanese and foreigners long resident in Japan learn much about the reputations of companies and individuals in the businesses in which they are engaged. Sometimes all you get is a raised eyebrow, other times you get detailed facts, mostly what you hear is not a condemnation of a company or individual, but a hint. The Japanese language makes hinting an acceptable way of communicating.

As is well known the Japanese language is one of the most difficult in the world for non-Japanese to learn. This is a source of much trouble when Occidentals and Japanese try to co-operate. Whereas in Europe, nationalities such as the Danes, Dutch, Belgians, and Swiss seem to be notably good linguists because they must learn the languages of their neighbors in order to go anywhere or do any foreign business, I have noted that these four have no especial talent for learning Japanese. The reason, of course, is that there are no common cognates in Japanese that they can lodge on. The Japanese have been forced to learn European languages in order to do business outside of the Far East. English and German are the two that have received most attention. However, it is a rare Japanese who really masters a foreign language.

Japanese manufacturers who have grown greatly in the past twenty years have, in a large percentage of the cases, done so partly because of foreign influences of one kind or another. Either the Japanese obtained licenses and patents from abroad, or they purchased foreign machinery and know-how. With this technology they have been able to make improvements and refinements on the Westernmade articles. Then they have found markets abroad. To do all this required knowledge of foreign languages. Although admittedly most Japanese executives don't claim to be fluent in English, French or German, they have learned enough to be able to at least read and understand (though slowly) what they have read. A few Occidentals from the Americas and Europe have learned to speak and

read Japanese too, but far fewer than the other way around. The reason for the Japanese effort to learn a European language was because this knowledge was essential for success in doing business and in investing overseas.

The failure of Americans and Europeans to give as much attention to learning Japanese was predicated on the assumption that there was no especial need to learn Japanese. Japan has enjoyed huge export surpluses for over a half dozen years. In fiscal 1972 the surplus will likely exceed \$9 Bill. In my judgement part of the reason for this high export surplus lays in language study effort. The Japanese have been willing to put forth enough effort to learn the languages of their export market customers. Americans and Europeans have been unwilling to put forth much effort toward learning Japanese. It is difficult to sell in a nation where you cannot speak or read the language.

Americans and Europeans fail in Japan for other reasons too. One is because of unwillingness to learn how the Japanese do business. In Japan it is quite easy for a Japanese to learn how to do business in English-speaking America, or Spanish-speaking America, or in Germany or the United Kingdom. The Japan Productivity Center offers seminars in the major cities on such topics. So do universities and management training institutes. A superb foreign business training center was established several years ago. Each year about 125 young executives go to this school, and spend about twelve months in hard study away from their families. They learn English, German, or Spanish, and learn all that can be told them about doing business abroad in the target area of their interest. I know of no such center in Europe or America¹.

IV.

Many Europeans and Americans feel that Japanese companies are in shaky financial condition because the debt-equity ratio is about 80—20 instead of 40—60 as it usually is in the West. Actually, it is my observation that the debt-equity ratio is really not much different in Japan than in the Occident. The Japanese, under their laws, understate the value of their assets. Land is shown on the books at cost, so is stock of other companies. The price of land has risen eighteen times in the past fifteen years in the metropolitan areas. It is the custom of large Japanese companies to hold substantial amounts of common stock of related companies. Related companies are those which are members of the same capitalist group, the "zaibatsu". Each member of the group owns shares — perhaps 2 per cent or 6 per cent — of each of the others. Then Japanese companies also own shares in suppliers, and in customers too. Share prices have risen dramatically in the past fifteen years. If the real value of land and shares were entered on the books of Japanese firms, their debt-equity ratio would likely be close to 40—60 instead of 80—20. Japanese bankers are fully aware of the understatement of value, and it is in part because of this that they are willing to lend money as freely as they do. Needless to say, it is advantageous tax-wise to understate values as the Japanese do.

The understated values cause some worry, however, when the Japanese are dealing with Occidentals. They fear that Occidental firms will take over their companies, and promptly sell the shares of related and other firms and with the proceeds pay huge dividends — dividends so large that the foreign owners would be able to use them to pay off the bankers who loaned the money for the take overs. To forestall a foreign invasion of capitalists, the Japanese up to now generally forbid acquisition of more than 25 per cent of the stock of an existing concern by foreign interests unless, of course, the permission of the government is first obtained.

The Japanese financial system is, therefore, conducive to growth. I understand that in European countries there are many inventions that are not being exploited because of the fiscal policies of the government, policies designed to restrain inflation. This is not a problem in Japan. First, it must be admitted that the Japanese are not as inventive as are

¹ I am planning to establish one at the University of Texas at Dallas, however, so that the mysteries of doing business with the "inscrutable Japanese" will seem reasonable and explainable.

Europeans and Americans. They are remarkably good in making improvements on other people's inventions, however. They are also alert to what is going on in foreign countries, and are able to obtain financing from their banks if they can show that the product they want to introduce from abroad has proven successful there. By following a policy of bringing in only the latest and best obtainable from overseas they have managed to modernize their industry to a high degree.

Japanese government planners and industrialists are currently running into some opposition within their own country. As an example, the government has designated a vast area in Yamagata prefecture in northern Japan as a site for factory development. In answer to a questionnaire circulated among farmers made by Yamagata University 44 per cent said that their business would suffer rather than benefit by industrialization of the area. Only 21 per cent felt that their business would improve. The problem is environmental pollution. If Japan slows down in her mad rush for an ever higher Gross National Product it is likely to come from resistance of an outraged people — people outraged because of pollution².

Prime Minister Tanaka, realizing that the long area on the Pacific coast, commencing a hundred kilometers north of Tokyo and stretching south and west through the Inland Sea and into north Kyushu, is overly crowded, and overly polluted, plans to establish new industrial centers in underpopulated areas of the nation. Many ecologists in Japan — and farmers and townspeople too — are protesting that his plan will merely widen the areas of pollution.

If the new factories can be constructed in such a way as not to pollute the countryside, the move away from the cities will be beneficial to all. How to do this is now being studied by the newly organized Environment Agency of the government.

Foreign firms contemplating manufacture in Japan, and prevented from doing so because of the restrictions imposed by the Ministry of International Trade and Industry, may find a welcome from prefectures that are losing population. These are remote from the industrial centers, and are largely in northern Honshu, western Honshu, southern Kyushu, and southern Shikoku. These are prefectures that the Prime Minister's plan wishes to see developed industrially. If the type of manufacture contemplated by a foreign firm is non-polluting, it is in some instances possible for prefectural politicians working with the Prime Minister's office to persuade MITI to change its stand.

V.

This brings up the question of how foreign companies should negotiate. Should they use trading companies to intervene for them, or should they try to work direct. If a trading company can make some money out of intervening, there is no harm in asking for their help. It should be kept in mind, however, that trading companies are not in business to negotiate agreements from the government on behalf of foreign clients. This work is better done by consultants. A trading company is likely to refuse to help unless it is to be a partner in the venture the foreign company is planning to establish in Japan.

The first trading companies established in Japan after the opening in 1859 were foreign. Jardine Matheson, the Scottish firm which exercised much power in Hong Kong and Shanghai, entered Japan shortly after the opening. So did some others, including the American Trading Company. These firms represented many clients, and supported by the commissions of all, rendered valuable service. In time these firms lost nearly all their early clients, but not because of failure to represent them well, but because the volume of business grew so much that it paid to establish direct offices and dispense with the services of the trading companies.

² In my office in Tokyo, on the 23rd floor of a building, there were several days in 1972, when I could not see the street below because of the heavy pollution. Japan, when I first came in 1918, was almost uniformly beautiful. Now, due to over-industrialization, vast areas are ugly and unhealthful. Yet the people have become rich. One wonders if it is progress when people in becoming wealthy destroy the environment that supports them.

As the Japanese learned how the foreign trading companies operated, they entered the business too. They now dominate the trading company business in Japan, however, there are still many foreign firms, including several that have been in Japan over 100 years. When an Occidental company wishes to enter into business in Japan, if it is totally inexperienced it is a good idea to use either trading companies or consultants until the necessary expertise has been gained. If the foreign firm has a product to sell, the trading company may be able to handle it through its own outlets. If a consultant is used instead, he will be able to find the proper outlets and assist in negotiating marketing agreements.

Once a good market has been established in Japan, some foreign firms think that they should investigate whether to manufacture there rather than ship from Europe or the Americas. Japan's position among industrialized nations is unique in this regard. It is so far from any of the others, that there are usually compelling economic reasons for manufacturing in Japan rather than relying indefinitely on exporting from the home country. When wanting to establish direct operation, there are three roads to take. (There is a fourth too — establishment of a branch office, and limited assembly of imported parts but this is highly restricted by the government.) Most common is to license a Japanese firm to manufacture; the second is to establish an equity interest usually in the form of a joint venture; the third is to organize a 100 per cent foreign owned firm.

Japan's great rise is due to a considerable extent to the wisdom of her leaders in buying foreign technology instead of developing it at home. It is expensive to invent and perfect a product, and the trial and error stage is time consuming too. The Japanese avoided these worries by going straight to foreign manufacturers and buying their perfected technology. Many foreign firms, however, came to have second thoughts about licensing the Japanese to use their patents and know-how. Usually within five or ten years the Japanese were able to manufacture well themselves, and no longer needed the foreign technology. Then the Japanese exported their products back to the homelands of the licensors — and in some instances took their markets.

To avoid this, foreign firms often try to manufacture in Japan itself. Prevented by the government (there are some exceptions) from starting up their own 100 per cent owned businesses, they have sought native partners. Joint ventures have in many cases been successful, but far too many have failed. Failure has come from many causes, not the least of which has been the unfamiliarity with the art of doing business in Japan on the part of the foreign firms.

A common complaint made by foreigners in Tokyo is that the home office people are impatient when things don't move as swiftly as they expected. The home office people naturally become concerned when delays which they do not understand take place. When they react too strongly the Japanese become uncooperative. What is needed in such a case is for someone who knows both the field office and home office problems to play the role of "explainer" for both sides. To be credible, such a man must of necessity have lived in Japan for many years, for otherwise neither side would believe him. It is a rare Occidental firm that has a man like that on its staff.

VI.

The expatriate in Japan, if his duties involve dealings with Japanese (some only deal with the U.S. military), to be successful usually requires a minimum of three years in residence during which he must study everything he can about the Japanese system. During my year as President of the American Chamber of Commerce in Japan, I learned much of the experiences of other companies than my own. It is obvious that part of the trouble of the American firm lay in ignorance about Japan. To assume that staff people from the U.S. could come out and give expert advice on any but technical matters without possessing extensive background knowledge of Japan was unrealistic. The great problem with either joint ventures or foreign owned companies in Japan is that usually there are not enough experienced or trained Occidentals either in the Japan operation or the home office to know how to run them.

When examining the business practices of an old country, one is continually discovering that the origins go far back. Take marketing for example. Although most of the products being distributed and sold in Japan were unknown 200 years ago, the channels of those days — and the weaknesses too — are still present. There are many more layers of middlemen than in the United States, and this adds much to the cost to ultimate consumers. One reason for this is the great number of retail outlets. It is estimated that in Japan there are twice as many as in the United States with nearly double the population.

The vast number of retail outlets serves, however, a useful purpose: it provides jobs. There are many people who gain employment from the small shops who would otherwise be dependent on relief or their relatives. The low level of unemployment in the country — currently about 1.3 per cent — is made possible in part by the large number of small retail outlets.

Foreigners — which means mostly Americans, Australians, Canadians, North Europeans, Chinese and Koreans — in some instances follow the Japanese distribution system, and in a few cases establish their own, copied from that followed back home. I have known many Occidental companies to fail in reaching the Japanese market. In a few instances it was because they insisted upon using their homeland marketing system without modifying it to meet local circumstances. In quite a few cases it was because the people from overseas would not adapt their products to the local market conditions. As an example, a U.S. firm insisted on supplying its product only in color. The local market did not require color, and wanted a black and white product, one which cost about one-third the price of the colored article. The home office in the U.S. refused to accommodate the Japanese, so the firm has never been able to reach the market properly. In the past dozen years it has fired four Occidental general managers in succession. The fault lay in headquarters inflexibility, not in the behavior of these men.

VII.

We in the teaching profession are trying to train foreigners in the art of cooperating with Japan. Ideally, we should have candidates for positions in Japan study in our classrooms for a year before crossing the ocean. Then we should have the home office staff people who will be responsible at a distance for the Japan operation spend time with us learning the techniques, problems, and the mysteries of Japanese operations.

Japanese executives have difficulty in doing business outside of their own country too. Japanese miss many an opportunity to establish factories in the West because they fear the labor unions. American and European universities having business schools should encourage Japanese to attend post graduate courses and learn the technique of operating in Europe and America. If properly trained, I think that the Japanese would feel much more like investing overseas than they do now. Japan, with its 20 or more billion dollar foreign assets reserve, is losing a lot by the slowness with which it is investing overseas.

Perhaps part of the trouble lies with us in the teaching profession. Japan has a labor shortage, and in most other countries there are far too many people out of work. The Japanese have far more foreign exchange than they know what to do with. Surely in a mix like this there are opportunities. The missing ingredient up to now may have been "lack of instruction for Japanese in the technique of investing, managing, and operating in foreign countries".