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Abstract	Most Japanese workers answer "company employee" when they are asked to state their occupation. This is because one's career in Japan is developed within an organization by practices such as . on-the-job training, job-rotation, transfers, promotion' and sending out-and-back. Japanese organizations have been successful in maintaining organizational flexibility and adaptability in the face of a changing environment. Another characteristic of the Japanese labour market is a stable non-rewarding remuneration system, called the "nenko" wage system, which is based on education, years of service, age, and sex. However, Japanese workers today are not satisfied with the present system, and want to have more rewarding systems. What I would like to emphasize is that rewarding systems which are popular in most of the world except Japan, are not conducive to developing organizational flexibility. I suggest another non-rewarding remuneration system based on non-job characteristics. Job characteristics should be accounted for only when jobs are disliked by workers. Even a flat rate may serve this purpose if another way cannot be found. It will become more and more nonsensical to try to measure a worker's individual productivity.
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## WORK AND PAY TOWARDS TOMORROW

by

*Yoko Sano*

### *Summary*

Most Japanese workers answer "company employee" when they are asked to state their occupation. This is because one's career in Japan is developed within an organization by practices such as on-the-job training, job-rotation, transfers, promotion and sending out-and-back. Japanese organizations have been successful in maintaining organizational flexibility and adaptability in the face of a changing environment. Another characteristic of the Japanese labour market is a stable *non-rewarding*

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remuneration system, called the "nenko" wage system, which is based on education, years of service, age, and sex. However, Japanese workers today are not satisfied with the present system, and want to have more *rewarding* systems. What I would like to emphasize is that *rewarding* systems which are popular in most of the world except Japan, are not conducive to developing organizational flexibility. I suggest another *non-rewarding* remuneration system based on non-job characteristics. Job characteristics should be accounted for only when jobs are disliked by workers. Even a flat rate may serve this purpose if another way cannot be found. It will become more and more nonsensical to try to measure a worker's individual productivity.

## *Preface*

Japanese children, like those everywhere else in the world, traditionally dreamt of becoming heroes: baseball players, pilots, singers, and teachers. Nowadays, Japanese children seldom claim to have such dreams, because they know that there are very few professions that they can develop as a lifetime career. The most common way to establish a career in Japan is to enter a company and take whatever job that comes. Therefore, the children's dreams are to become *company employees*, rather than to enter a specific profession such as that of an accountant or a researcher. The only decision a youngster makes concerning his or her career is what level of educational status they wish to achieve: high school, college, or a post-graduate degree.

With the exception of those with post graduate training (such as medicine, law, and engineering), firms look at young graduates merely as either a liberal arts major or a natural science major. Firms put little importance on the knowledge a graduate has in a certain field. Instead, emphasis is on general knowledge and common sense, and therefore students put in little effort in cultivating their specialities. Natural science graduates basically work as plant technicians and engineers, while liberal arts majors (law, economics, literature, etc.) work in offices. However, some areas take people with any background, and due to the lack of computer specialists in Japan a lot of programmers and engineers are not computer majors. General ability is the only talent required, and a flexible mind along with good health, personality, and human relations are also valued. Company workers are hired according to their sex and educational status, and trained, allocated and promoted according to the company's practices. However, promotions usually result from intracompany transfers and high educational attainment.

It should be interesting to note that Japanese ordinary labour statistics show classifications of sex, age, length of service, industry, and location of working place, but not occupation. This means that the occupational category is much less important than industrial or sexual categories in Japan. This is a result of the development of internal labour markets in Japanese firms.

### *1. Origin of the Internal Labour Market*

The theory of the internal labour market summarizes the characteristics of the internal market as follows:

- (1) Skill hierarchy is established in the internal labour market, and ports of entry are open only for the lowest grade; only unskilled workers can enter the firm.
- (2) Workers are mostly trained on-the-job, because required skills are often very firm-specific and cannot be found in the external labour market.
- (3) As workers acquire such firm-specific skills, they tend to be promoted within the firm and paid more as they are promoted.
- (4) As a result, workers have a lower incentive to quit because their firm-specific training investment will not attract as high a wage in any jobs that can be found in the

external labour market, and they are likely to stay at one firm longer because firms want to keep trained personnel for longer.

## 2. *Assumed Results of Internal Labour Markets*

It is usually argued that development of the internal labour market together with enterprise unionism, brought about the following tendencies:

Firstly, workers' jobs have been secured. It should also be pointed out that subcontracting and a temporary workforce are utilized as buffers to protect 'inside' workers from less favorable working conditions. However, the idea of lifetime employment is popular, and such policies are often followed by smaller and new developing companies. If any regular worker dies before retirement, his widow is hired instead as a regular worker, despite it being very rare for middle-aged women to be hired by large-sized firms. Similarly, deceased workers' sons are often hired as they graduate from schools.

Secondly, the wide differences in status and compensation between production workers and office workers have been narrowed. The differences were quite large before World War II, but democratic and egalitarian ideas were adapted by management and trade union people, and the differences disappeared at least on the surface. Another outcome that is often pointed out is that the difference in wages between management and unskilled workers is remarkably small as compared with other countries, although the difference between young and senior workers is large among production workers and among office workers. This is called the "nenko" wage payment system.

Thirdly, stable and peaceful industrial relations have been maintained. This is rather an outcome of prolonged industrial struggles immediately after World War II, and especially cooperative relations were established during the post-oil-crisis adjustment of spring wage offensives. Different from the formal way of consultation system often seen in Europe, Japanese management and unions within the firm share more common interest to support maintenance and development of the company. Industrial peace has been accomplished even during the hard times after 1975.

## 3. *Some Doubts about the Assumed Results*

It should be stated that the above view is very commonly held among Japanese specialists. I have some doubts about it. The view derives from human capital theory, which explains the origin of the internal labour market in a rational and economic way. *Skill hierarchy* and *firm-specific skill* are the core of the theory. But if any one looks for counterparts in the real world, he or she will be lost.

(1) In the internal labour market, ports of entry tend to be restricted to the lowest grade of workforce, but there is no evidence to show the existence of *skill hierarchy*. It is usually recognized that *skill* is difficult to define and the level of skill is difficult to measure. Some economists assume that wages reflect productivity, that is, level of skill. It seems to me that there is no evidence to show the close relationship between them since there is almost no way to define skill level.

(2) It is true that Japanese workers are trained on the job, because it has been better for firms to do so than rather to recruit skilled personnel. But it is difficult to identify the reason because the required skill is firm-specific.

(3) Workers are promoted and paid higher on the basis of seniority according to several promotion routes, roughly speaking. But there is no evidence that they are promoted as they accumulate specific human capital. The remuneration system is surely a hierarchy, but again it is difficult to test whether the level of wages is related to the level of skill.

(4) The human capital theory states that trained and skilled workers have no incentives to move, because they are more highly paid than they would be anywhere else. Firms which have invested in workers are afraid of losing them and so wages vary depending on the cost of training, and its return (profits) to the firms. Such firm-specific capital investment is regarded as the origin of the long-term employment system in Japan. But there is another possible way to explain the system: if all the firms do not open *the ports of entry*, no worker can leave a firm, and so every worker has to stay at one firm all through his or her working life. Within the firm, workers are apt to move from job to job, and from place to place, but mobility among firms comes more from the reduction of workforce in times of least favorable business conditions.

#### 4. *How to Solve Redundancy*

The strong doubt about the skill hierarchy comes from the fact that Japanese firms, especially in manufacturing and related industries, have introduced new technology continuously through the past century. Large and progressive firms have always been interested in development of technological competitive power. In such situations the labour force was not available in the external labour market, and had to be trained inside. The important point is the “continuous changes in technology” which means “continuous needs for a newly equipped work force.” Old skills are often made obsolete when another technology is introduced. In the internal labour market workers that were not at the skill-frontier were treated in several ways.

(1) When firms develop in size, they devote more forces to new plants or new areas in a plant. For example, when the Japanese steel industry developed rapidly in the 1960's, large firms established giant, newly automatized steel mills on one hand, while on the other hand they continued to operate old mills to keep up with demand. The new mills were operated by young new workers together with transferred skilled workers from old mills. The core of the manpower in the new mills was a skilled workforce equipped with knowledge of new technology, who were engineers and technicians rather than traditional skilled workers.

(2) A theoretically ideal way is to retrain workers to adapt to the new technology. When the Nippon Telephone and Telegram Corporation (a state-owned organization until 1984) abolished wireless communication, they retrained all the wireless operators to be computer programmers and system engineers. This case of retraining used-to-be core workers to convert to another core group, is quite unusual because it is costly.

(3) The most common way is to transfer elder workers to the area which faces a shortage

of manpower. In large manufacturing firms production workers are to be reduced in number and to be equipped with more and more modernized technology. On the other hand, marketing and sales areas are a growing sector in terms of manpower. When a large newspaper firm introduced a total electronic system several years ago, many workers were freed from editing and printing sections. The management wanted to transfer those mostly middle-aged and old-aged people to the sales sections, but, faced with the trade union's opposition, it decided to spread redundant workers over all the other sections. Especially the printing workers opposed the proposal very strongly.

(4) Not so common, but more often used than is generally thought, is to fire or lay off redundant workers. Transferring workers happens usually at growing firms. But if firms face shrinkage of product demand, they resort to voluntary leave, early retirement, and sending workers to related firms after reducing part-time workers and subcontracted workers. A motor cycle maker recently laid off a large number of employees, but it was difficult to decide whether the situation was caused by automation or by business recession.

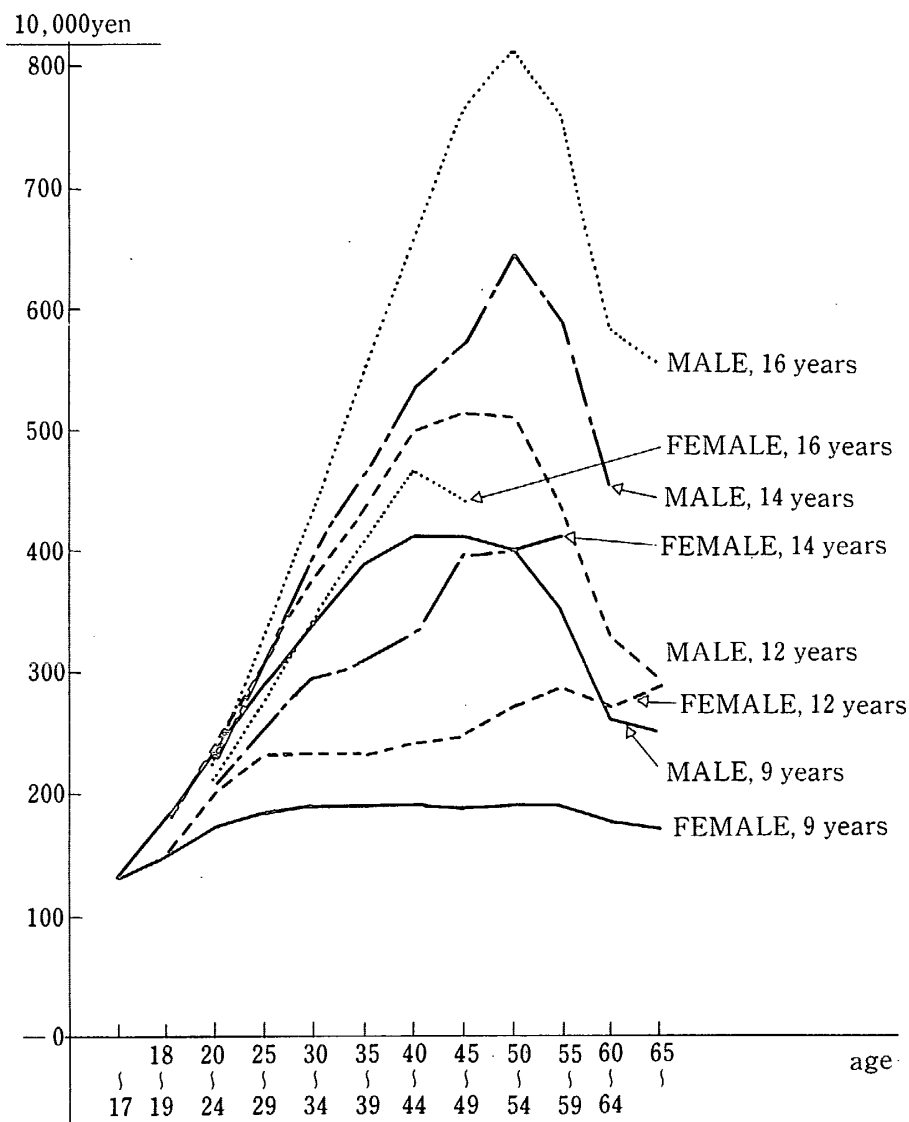
### ***5. Non-Rewarding Wage Payment System***

Except for workers who have quit permanently, redundant and transferred workers are paid as much as before, and it shows how loosely wages and productivity are related. This prevents management, unions, and workers from industrial struggles and shows that required skill often changes over the course of one's working life. One's adaptability and flexibility is sometimes appreciated more than one's level of skill.

Thus 'job rotation' became one of the important methods of training people. While the merits of 'job rotation' as a system for training management people are easily understood, they are less obvious in the case of production workers, who are confined to a smaller area. However, the roles of production workers in large firms include supervising subcontractors and parts makers and so it is sometimes said that blue collar workers in large firms are actually white collar workers in a sense. This is clearly illustrated in the construction industry in Japan, which has gradual sub-contracting structure, and in which we find that the larger a firm is, the smaller the proportion of manual workers it has. 'Gene-Con' (Which stands for general construction) means controlling and coordinating but no actual work. One or two supervisors can be seen at the same spot wearing differently designed and colored uniforms and helmets. They are engineers or technical specialists sent from a parent company. The 'general construction' method is an important aspect of firms in Japan, and the only necessary personnel are management and some staff members.

Another point which should be noted is that the remuneration system is different from the skill hierarchy. The payment system in Japan is usually called the 'nenko' system which means a hierarchy based on seniority and age of workers. The widely accepted view is that the payment hierarchy is backed by a skill hierarchy. The 'nenko' system is a sort of rigid hierarchy, and promotion and wages are closely related. (For reference, "age-earnings profiles" are shown in the Figure.)

**Figure** AGE-EARNINGS PROFILES BY SEX AND SCHOOLING YEARS - annual earnings, all industries, 1984, excluding cells which contains less than 10,000 employees



SOURCE: MINISTRY OF LABOUR, *BASIC SURVEY ON WAGE STRUCTURE, 1984.*

## 6. How Workers Look at Their Pay System

A survey was conducted among chemical and public utility workers in 1984, in order to see what the union members' attitudes were in their working lives. A pair of questions asked the union members for their view on the determinants of their wages. One was "what do you think are the important determinants of your present wages?" and the other was "what determinants do you think should be considered more important for your wages?" Two choices were allowed for each question. The survey was designed to show differences among sexes and jobs.

The Table on page 9 shows an interesting comparison between *actual* determinants and *should-be* determinants: every category of workers thinks that their own wages are determined by 'educational attainment,' 'length of service', 'age', and sometimes 'sex'. These are typical determinants of the 'nenko' system. Even male workers in research departments who are mostly graduates of colleges and graduate schools were no exception. Female workers sometimes pointed to the 'sex' factor.

However, all categories of workers expressed their opinion that their wages *should be* determined by 'ability', 'job', 'achievement', and sometimes 'attitude'.

The implication is two-fold. One is that the workers considered the determinants of their wages to be non-job related factors, that is the so-called 'nenko' factors. The other is that the workers considered more important determinants to be more job-related factors. It means that the workers were not satisfied with the present system of wage payment and that they want to have a system which is more closely related with their skill and capability. It shows that the 'nenko' system is based neither on skill nor on capability.

## 7. *Recent Changes in Internal Labour Markets*

Dr. M. Maurice stated about recent changes in internal labour markets that required skills were multi-dimensional, and that workers should know not only know-how but also know-why. Human resources today are expected to be equipped with more adaptability and flexibility within organizations.

This is the way in which Japanese firms have developed as their internal labour markets. The problem with them has been the lack of flexibility *among firms* through external labour markets.

In addition to the above, there are important tendencies in recent labour markets which arise in studies of various countries. Some of them are: uselessness of present job categories, appearance of new-type career development, dysfunction of skill hierarchy, and decreasing demarcation between manual and non-manual workers. These changes have not been caused only by the new technology, but it is an important factor.

Developments of internal labour markets in Japanese firms might give some suggestions on the future prospects of labour markets in other countries, because most of the above tendencies have already been seen in Japan.

Maurice did not state much about remuneration systems. What I would like to emphasize in this article is the independence of the wage payment system from labour market conditions. In spite of such changes in skill and job organization, the Japanese "nenko" system has been strikingly stable over the past decades.



## Conclusion

Professor L. Thurow claimed that wages were determined by socioeconomic factors and not only by the demand-and-supply mechanism as neoclassical economists expected. This means that the wage structure is rather stable in the face of changes in labour market conditions. Thurow's assertion was strictly against the human capital theory which explains that the internal wage structure is defined by the internal skill hierarchy.

Japanese experiences discussed above do not seem to support the human capital theory nor the internal-labour-market theory merely based on firm-specific skill hierarchy. Japanese organizations have shown remarkable flexibility and adaptability in operating their internal labour markets. The problem with them, is the wage payment system. Japanese workers generally seem to support more rewarding systems rather than the traditional "nenko" system, which is based on educational attainment, length of service, age, and sex. These factors are not considered by Japanese workers as rational and reasonable.

Recent changes in characteristics of internal labour markets in a considerable number of countries sometimes reflect the inappropriateness of the traditional (in the western world) system of rewards based on job content, because such a system does not easily allow workers to transfer, and flexibility cannot therefore be maintained. I should conclude that this is the time to give up measuring individual productivity. People are not always motivated by monetary incentives to work. This is close to the Japanese non-rewarding pay system.

The problem with Japanese workers is that they have an illusion. The illusion is that rewarding pay systems would be better than the present "nenko" system. The new system should be based on workers' characteristics other than education, service years, age, and sex. Job characteristics should be accounted for only if jobs are unstable, unpleasant, dirty, and dangerous. Skill is no more definite. Educational level is becoming higher. Why should the society pay more for illusionary higher skill and for traditionally internalized professions?

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Table Union Members' View about Wage Determinants

present department	number of respondents	determinants perceived as important for their wages*			determinants that should be considered more important for their wages**		
		most popular	second popular	third popular	most popular	second popular	third popular
Male							
production	2,286	educational attainment	length of service	age	ability	content of job	achievement
research	857	educational attainment	length of service	age	ability	achievement	content of job
office	663	educational attainment	length of service	age	ability	achievement	content of job
sales	705	educational attainment	length of service	age	ability	content of job	achievement
computers	344	educational attainment	length of service	age	ability	content of job	achievement
Female							
production	70	educational attainment	age	length of service	ability	content of job	attitude
research	90	educational attainment	sex	length of service	ability	attitude	content of job
office	278	length of service	educational attainment	sex	ability	content of job	attitude
sales	46	educational attainment	length of service	sex	ability	content of job	attitude
computers	80	educational attainment	length of service	sex	ability	content of job	achievement
Total	5,419						

Source: International Federation of Chemical, Energy, and General Workers' Unions, Japanese Affiliates Federation, *Kagaku Energy Sangyo ni miru Rodosha Ishiki*, (a study of workers' attitude in chemical and energy industries), Tokyo, ICEF · JAF, 1985.

\*Question: "What do you think are important determinants of your present wages?"

\*\*Question: "What determinants do you think should be considered more important for your wages?"