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Stakeholders and the modern corporation

The Embedded Corporation: Corporate Governance and Employment Relations in Japan and the United States. By Sanford M. Jacoby, Princeton University Press, Princeton, NJ, 2005, 216 pp., $58.00/cloth.

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In his book The Embedded Corporation, author Sanford M. Jacoby compares and contrasts the role of the Human Resources (HR) Department and institutional change in Japan and the United States from the 1950s to the present. He uses the HR function as a vantage point to analyze trends and understand larger issues of divergence and convergence between the two countries.

Japan's corporate governance system emphasizes high levels of coordination between business and government to ensure that the interests of all stakeholders (defined by Jacoby as shareholders and employees) are in balance. For example, Japanese corporations provide employees intensive long-term training programs and job security, even during times of economic downturn. In contrast, Jacoby contends that sovereignty in the United States has trended more and more to shareholders at the expense of employees, beginning with the shareholder movement and the antilabor sentiment it created in the 1990s. He profiles the decline of career jobs and of mutual loyalty between employers and employees, accompanied by a single-minded focus on share price, since that time. In Jacoby's mind, the notion of employees as stakeholders is now "widely repudiated." Corporate governance in the United States, he feels, is out of balance.

Since the end of World War II, Japan and the United States have had an interdependent, but also complex and evolving, relationship. In the 1950s and 1960s, Japanese businessmen and government officials made regular trips to the United States to learn about its ostensibly superior system. Already by the 1980s, however, the economic success of the Japanese system served as a model for the U.S. economy. The key difference was the structure of the HR department. In Japan, labor-management relations, the rotation of managers, and the identification of employees to fill senior management positions were all among the myriad HR duties. HR was thus indirectly linked to corporate governance through the grooming of individuals for board-of-director positions and directly linked through the board of directors' membership. In short, HR took a prominent and prestigious role in all aspects of the Japanese corporate structural hierarchy.

In contrast, U.S. CEOs almost never have a background in HR, and salaries of HR executives tend to be lower than those of other corporate specialists; in fact, until the late 1970s, most HR executives in the United States reported to the vice president of operations or someone of similar rank, rather than to the CEO. Only in a few U.S. firms is there an acknowledgment that "human and intellectual capital are increasingly a company's most important assets." Instead, powerhouse functions inside U.S. corporations have typically been concentrated in production, marketing, and, more recently, finance, with HR executives at the bottom of the managerial hierarchy.

Japan's "stakeholder over shareholder" philosophy represented a long-term commitment: "even in the mid-1990s, 97% of Japanese managers agreed that the company exists for the benefit of all stakeholders and disagreed that shareholders should have priority." But times are changing. In spite of resistance from company workers and the Japanese government, CEOs in Japan are feeling the pressure to conform to the U.S. style of "shareholder first" corporate governance. And many of those CEOs are no longer professing to a belief that stock market–influenced employment practices would weaken corporate HR functions. Meanwhile, HR executives in U.S. companies are struggling to redefine their responsibilities. Gone are the notions of employee advocacy. With finance dominating corporate decision making, HR executives are being forced into becoming strategic business partner, advisor, and contributor to cost cutting. In this new environment, HR has abandoned its traditional role of "pacifying disgruntled employees" in favor of "consulting with internal customers." In spite of lots of buzz words used by corporations in their literature describing what HR executives do, Jacoby insists that exactly what they do as "business partners" remains "something of a mystery."

Jacoby's view is that the HR role in the corporation cannot be understood without an appreciation for the fact that corporations are about more than mechanisms for maximizing profits. They are also about conflict resolution, the pursuit of labor economics, and the decision to invest in human capital. The latter, in particular, has clearly different risk and reward patterns for shareholders and employees. In Jacoby's opinion, the pendulum has swung too far in favor of one stakeholder (shareholders) over the other (employees).

This book is a must-read for anyone searching for a better understanding of the economics of corporate change and social decline. I recommend it.