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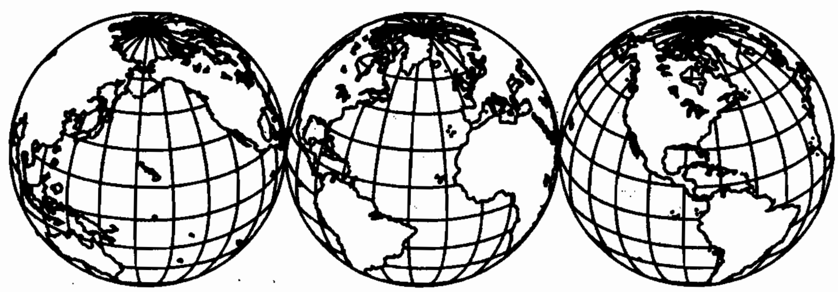

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The Japanese Model of Capitalism: A Guide for Russia's Marketization?

Douglas N. Ross

For Russia, the word of the day is transformation. The transforming of Russia's economic system from state-controlled socialism to market-driven capitalism may prove a major accomplishment of the closing moments of the Twentieth Century (if a Russian nationalist coup does not truncate the process). This raises, however, the question: Which "capitalism" of the global triad–American "individualistic," European "statist" or Japanese "communitarian" (Lodge, 1991)–seems the most likely to prevail in the Russian environment?

This article focuses on the complex and successful Japanese model of industrial capitalism. The first section explains the Japanese model; the second provides a framework for assessing the feasibility of the Japanese approach to Russia's transformation from command to market economy. The concluding section addresses the effects on Russian enterprise–former State and emerging business–and on Western firms if the Japanese model were to be adapted to Russia.

JAPANESE-STYLE CAPITALISM: ITS STRUCTURE AND PROCESS

The Japanese model of capitalism operates on three levels: macro-level relationships between national governments and between the Japanese

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government and business; intermediate level relationships among and within corporate groupings; and micro level relationships between a firm and its corporate grouping and between the firm, its industry and the Japanese government. Figure 1 portrays these macro, intermediate and micro levels of Japanese industrial structure.

At the macro level, a government "roof" often shields domestic markets from the competitive incursions of outsiders. Pushing up from the micro level, individual firms usually group themselves into "alliances" (Gerlach, 1987)–an "intermediate" institution known as the Japanese corporate grouping, or group form (G-Form) organization (Ross, 1992). Commonly recognized as *keiretsu,* or *kigyo shudan,* they are at once an institutional bridge between government and business, and a philosophical, strategic and structural context for the Japanese firm. These corporate groupings can be fiercely competitive in Japan, yet cooperate fully in attacking foreign markets. The Japanese model of capitalism cannot be understood apart from this intermediate institution.

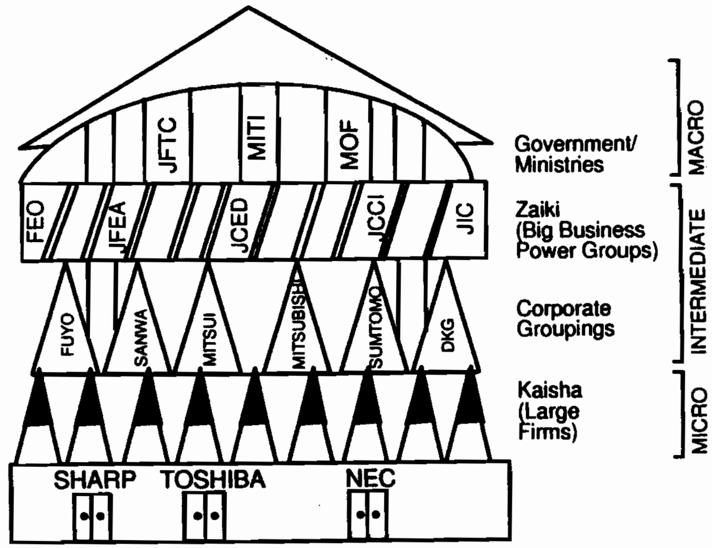
Figure 2 illustrates the interactive processes of the Japanese model. The intermediate organizations of Figure 1 become the important coordinating mechanisms in Figure 2's stages. Figure 2 shows both the several types of coordination–macro, intermediate and micro–and the five principal coordination stages–including business activities and government policies and business activities by businesses themselves (Ross, 1991; Sasaki, 1990). These stages are quite flexible and anything but a lock-step sequence of events.

At the center of the figure, the Government/Business amalgam develops agreement upon and then coordinates the implementation of government policies. Government persuades, facilitates and encourages industry to move in a desired direction through continuous collaboration with industry. This interface gives government great flexibility to utilize fine-tuning measures to help specific industries while not impairing overall competitiveness (Okimoto, 1989). At work here is not the familiar notion of close cooperation between government and business, rather there are "reciprocal relations." For example, the government, in exchange for subsidies, may exact specific performance standards from Japanese firms. Indeed, doing so may counterbalance negatives of administered price regimes which can arise in cartelized industries.

As seen in stage 1, government creates an industrial policy by a kind of national "ringi"–consensual decision making–system in which large business points the direction. Noted former Prime Minister Ikeda, "the government is the captain and the *Zaikai* [big business] the compass of the ship" (Yanaga, 1969, p. 34).

National policies actively seek to insure the domestic profitability of

FIGURE 1. Three Tiers of the Japanese Model of Capitalism



ZAIKAI: BIG BUSINESS ASSOCATION	GOVERNMENT/MINISTRIES
Federation of Economic Organizations Japan Federation of Employers Associations Japanese Committee for Economic Development Japan Chamber of Commerce and Industry Japanese Industrial Club	Japan Federal Trade Commission Ministry of International Trade and Industry Ministry of Finance

Japanese companies, which provides the financial support for their international expansion. In stage 2, for example, the Japan Fair Trade Commission (JFTC) may pursue antitrust measures with some flexibility so as to prevent "overcompetition" in the domestic market. Thus, cartels may be formed to the benefit of the producer and the detriment of the consumer, since Japan's economy is a "producer" not a "consumer" economy (Thurow, 1992).

Political Economic Coordination

In stages 2 and 3, the Ministry of International Trade and Industry (MITI) may apply "administrative guidance" to encourage more efficient

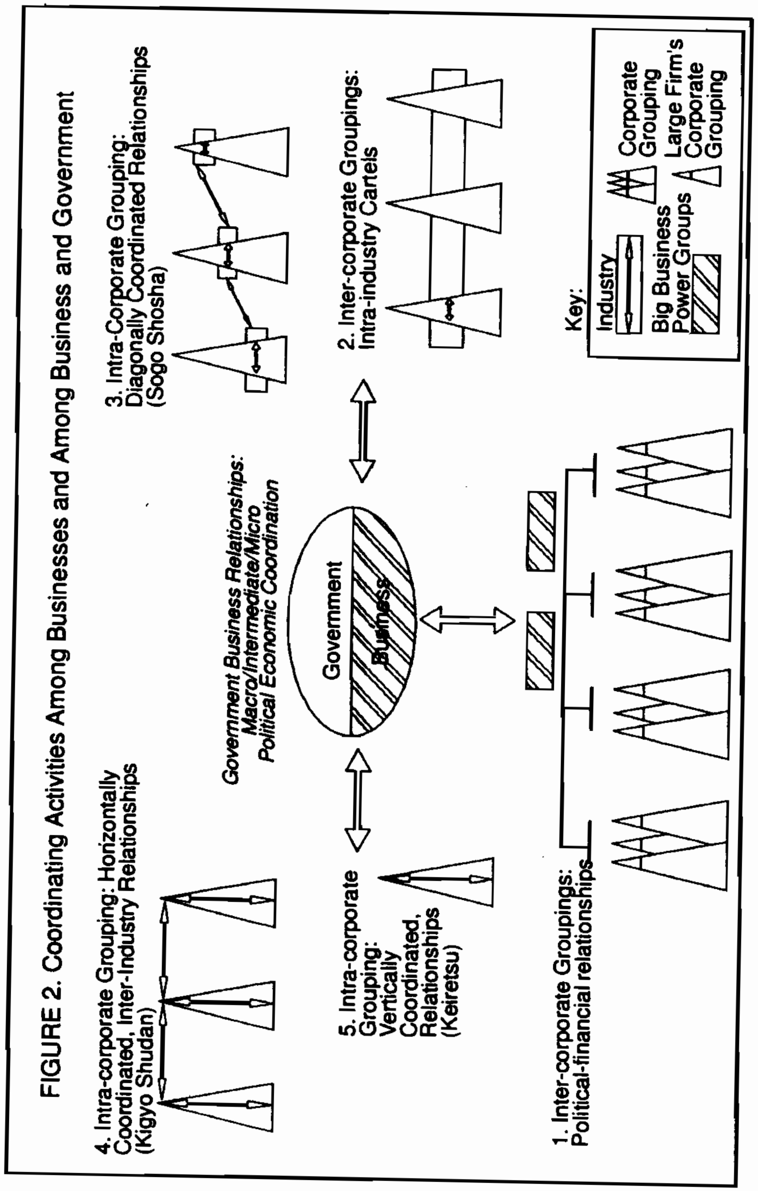


FIGURE 2. Coordinating Activities Among Businesses and Among Business and Government

national allocation of resources based upon specific priorities relating to target industries. (Guidance also affects *keiretsu* relationships of stage 5 because these are typically related to one major industry.) When national priorities are at stake, MITI may encourage firms to seek efficiencies beyond their corporate groupings. For example, the world's largest steelmaker, New Japan Steel, sells its output to a dozen trading companies. In turn, the trading companies may assist in acquiring iron ore for New Japan, in selling steel, or in selling steel products such as ships domestically and internationally. Abroad, MITI promotes open markets and free trade.

The largest six *sogo shosha* (trading companies) with assets in excess of $50 billion, both connect their *keiretsu* members to the global market and bring market opportunities to their *keiretsu*. Currently, they have some 70 Eastern European offices, including those in Russia. Markets, however, may be at any link in an industry's value chain. These relationships serve to "internalize" many intermediate product and labor markets and tie foreign countries and companies into Japanese corporate grouping networks.

The trading companies' distinctive competence is the matching buyers and sellers of diverse products and the playing of many different roles (Yoshino and Lifson, 1986). For example, Mitsui & Co. helped develop Japan's cotton spinning industry by, first, procuring foreign spinning technology and machinery. As domestic cotton supplies were depleted it found stable foreign sources and then stimulated the weaving industry by buying the products for distribution at home and abroad. Seldom do the *sogo shosha* engage in one time transactions; more usually they prefer multi-stage involvement in vertically integrated commodity systems and in such products as textiles, steel, metals, chemicals and food. Often ancillary services such as financing are provided.

In stages 4 and 5, a large firm's vertical corporate grouping (*keiretsu*) is linked to an inter-industry *kigyo shudan*. As seen in Figure 1, the government provides a protective shield for domestic competition between these strategically-coordinated and bank-related inter-market groupings. Further, government banks and agencies provide stable sources of long term expansion capital and market information and support for Japanese firms (*kaisha*) and corporate groupings when they attack foreign markets.

Internationally the Export-Import Bank of Japan has located recently in Frankfurt with the stated purpose of expanding untied loans to Eastern Europe and supporting Japanese business there. Further, to provide information for Japanese firms seeking joint ventures with East European companies, the Overseas Agricultural Development Association conducted surveys of agricultural resources and food processing industries.

To further national interests, the Japanese model of capitalism provides mechanisms for both encouraging certain types of business behavior and tempering the harsh discipline of external markets. Uniquely Japanese are the across-industry, inter-organization cooperative relationships which occur within the context of national industrial policy.

To what extent are Japanese institutions compatible with changing Russian structure? We turn now to examine the applicability of the Japanese model to Russia, beginning with a comparison between present-day Russia and post-War Japan.

By way of preface to this examination, in 1989, under Gorbachev, the USSR-Japan Business Cooperation Committee, whose chairman was the deputy minister of Foreign Trade (now in jail for corruption) was hosted by the Japan-USSR Business Cooperation Committee, whose chairman was head of both the Keidanren (a major zaikai) and a major trading company. Discussed were not only ways and means of enhancing trade but also how closer institutional cooperation could be achieved. Two prominent members of Russia's Yeltsin government–G. Yaulinskiy, deputy prime minister in charge of economic reform, and B. Fyodorov, minister of finance and deputy prime minister–also were members of the USSR delegation.

ASSESSING THE ADAPTABILITY OF THE JAPANESE MODEL TO RUSSIA

A simple STEEP framework–with Social, Technological, Environmental, Economic and Political segments–serves a twofold function. It provides, first, a structure for understanding the breadth and magnitude of changes assaulting Russia today. As such it is a useful environmental scanning tool for any firm contemplating doing business in Russia. Second, the framework enables a comparison of circumstances in Japan of the late 1940s-early 50s with those in present day Russia. Table 1 summarizes.

Social Environment

Both Russia and Japan possess educated populations, yet their social structures and values differ considerably. Established ways of thinking, such as attitudes toward work and honesty, and modes of decision making

TABLE 1. Steep Framework Comparison: Russia and Japan

	RUSSIA	JAPAN
SOCIAL	high education authoritarian	high education consensual
TECHNOLOGY	mixed	high
ECONOMY	developing/ resource rich	destroyed/ resource poor
ECOLOGICAL	low standards	low standards
POLITICAL	totalitarian/ command econ.	quasi-democ./ quasi-market

among managers and workers have been molded by the communist system in Russia and by a more consensual system in Japan. While both sets of managers are familiar with a process of bureaucratic bargaining, in Russia their main interest was guided by a desire to lessen standards and requirements from the economic center. (This is illustrated by the USSR State Planning Commission in Figure 3A. In should be noted that Yeltsin basically replaced the SPC sign with one for the "Ministry of Economy.") In Japan, managers balance various stakeholder interests. Neither place regards efficiency as the top priority. Thus for Russia comes the challenge of adapting to new values.

Russia: Transforming Values. While Russian managerial and worker attitudes may pose a major challenge (Welsh, Luthans and Sommer, 1993), still an educated workforce and a technical bureaucratic elite exist. These latter are resources that few developing countries had as they began to build the base for their rapid growth. For managers, accustomed to an authoritarian planning regime, the discretionary skills of managing a firm in a market environment need to be developed.

Every juncture involves Russia's elites (*nomenklatura*) in some change and they have yet to work out their roles in a market economy. Much of the turmoil in Russia relates not only to the genuine struggle to build a post-Marxian rationale for individual political and property rights but also to elites jockeying for position. Although private groupings are beginning to form, often what results is a push for deals for special interests. As a consequence, no consensus as to Russia's future direction exists. Indeed, even a valid mechanism for establishing national direction has yet to emerge.

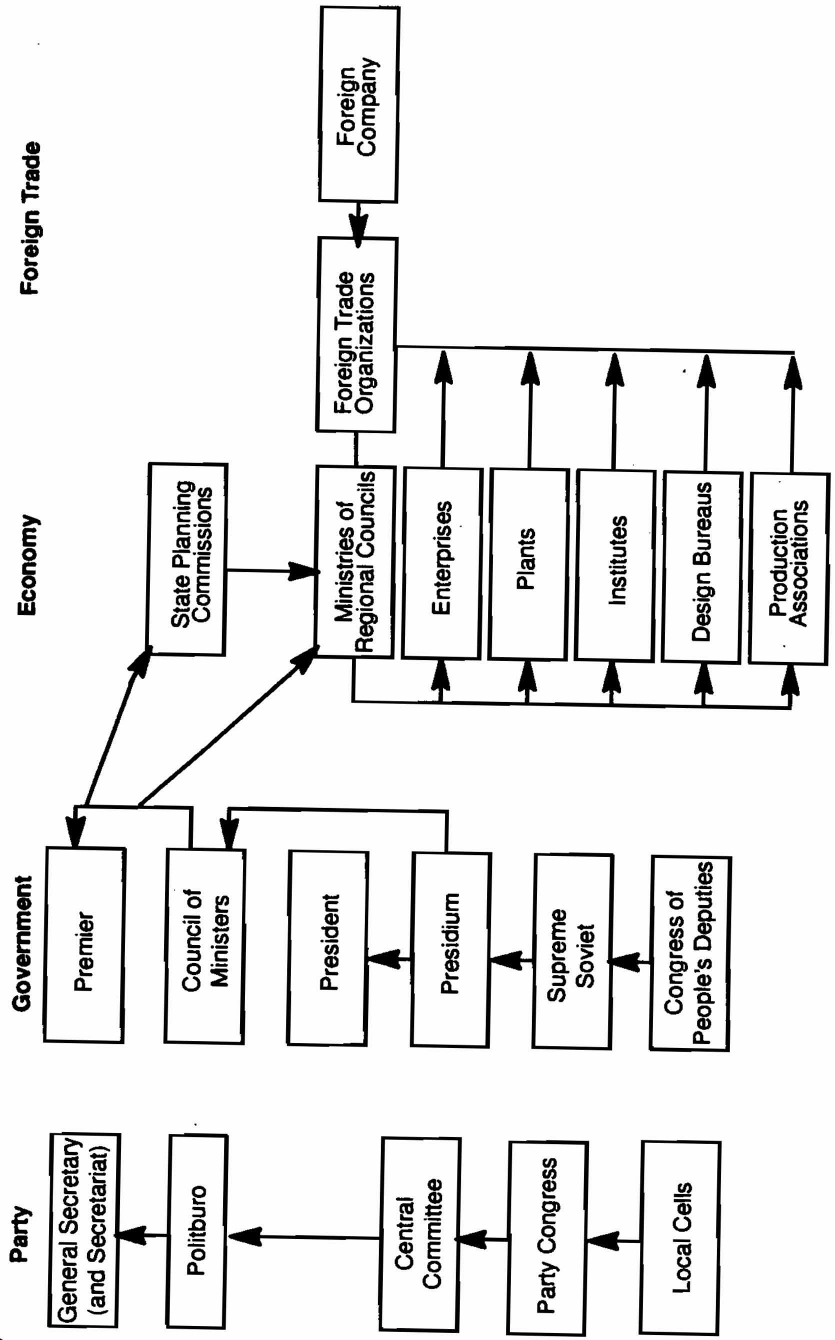


FIGURE3A. Historical View of the Soviet Union's Organization

Russian leaders must walk a tightrope. On one side, invoking the old priority-setting mechanism (the Plan) could simply add new mafia to the corrupted ranks of intermediaries of the planning system. On the other, lurk feelings vaguely reminiscent of Kerensky's 1916–Western bankers' pressure, civil unrest, looming totalitarian coup. Only now there exists a clear alternative capitalist structure and it is one with which Russian leaders have great familiarity.

It is well to note that the Yeltsin government emerged with the support of fledgling Russian entrepreneurs. Indeed, during times of recent instability and hardship, it is they who have kept the politicians on their payrolls so that reforms could proceed!

The challenge is to choose. Somehow, Russia must weave new patterns of efficiency-inducing competition from the old fabric of bureaucratic bargaining. This present lack of a satisfactory priority-setting and implementation mechanism is perhaps the greatest handicap Russia faces today.

Japan: Repairing the Social Fabric. Historically, the Japanese have had an "absence of a formal clearly defined, differentiated structure of decision-making" (Silberman, 1969, p. 347). Even the emperor could descend to personhood without massive social repercussions. Yet Japan is also a rigidly hierarchical society which constrains the consensus seeking process. Japanese managers, with pre-War *zaibatsu* (family-owned corporate groupings) experience and government Wartime control experience, were also used to following dictates of a central command.

General MacArthur's Supreme Command (SCAP) in the Post-War years took several important decisions. Major institutions were shaken; business pursued commercial not military products; the composition of the Diet was altered; and the large *zaibatsu* were broken up which decreased business power and increased government power (in the form of the Ministry of International Trade and Industry role in indicative planning). Then, to Japan's great benefit, along came the Korean War which provided a huge jump start to the revitalization of Japan's economy. As American attention shifted toward containing communism, the Japanese began re-assembling what are today's *keiretsu.*

Thus the social environment presents both broad similarities and marked differences. Similarities include: The fall of a belief system and concomitant turmoil; managers of large enterprise accustomed to central direction but, for Japan, also used to various market-driven competitive forces; and an operative small business sector.

Differences lie not only in areas of social cohesiveness but also in the degree of marketization, that is, the acceptance of the validity of the forces of demand and supply to affect resource allocations. While Japan altered (and continues to alter) the internal relative price structure, still it competed abroad. Russia did not. As a consequence it now experiences shock at moving from an isolated command system to a more open market system. A further difference is in consensus or lack of it on national directions. Whereas the Japanese set top priority on national economic growth, Russian leaders have not or cannot.

Technological Environment

Both Russia and Japan share high technological prowess although Russian capabilities in consumer goods areas have never been great.

Russia: Transforming Industries. The focus of the former USSR on military technology carried a huge cost for consumer products and to some extent for producer goods technology as well. While military productive capability, including heavy industry, undergirded the Russian economy, most other unrelated sectors were allowed to languish. Perestroika took the lid off consumer demand, but the means of satisfying it may be a long time coming.

Even in the key energy and heavy industries many problems exist. Current efforts to raise productive output are being stymied by the years of low investment in facilities and production technology. The steel industry, machinery industry and the electric parts industry all face deteriorating production conditions–shortages of materials, aged facilities, old technology. All are heavily reliant upon the energy sector (until recently the internal price of oil was 40 cents a barrel). Thus linkage effects (Hirschman, 1961) between industries exacerbate the doldrums. No one policy can effect change: many policies must simultaneously be implemented.

The means of supplying basic raw materials and products has a history of reliance upon so-called compensation arrangements between the USSR and Japan. From 1970 to 1985 some $8 billion was invested in Siberia and the Russian Far East by Japanese trading companies. This investment underwrote long term (twenty-five year) contracts for supplies of timber, oil, gas, coal, steel tubes and petrochemicals to Japan. Tied-credits linked USSR purchases of equipment to Japanese suppliers (due in part to intense lobbying efforts of the then-chairman of Komatsu.) The USSR benefitted by getting ten percent of what was produced for its own use.

Although upgrading and re-orienting heavy industry is critical, so also is the development of consumer products and services industries. McDonald's move to Moscow provides a textbook example of Hagen's (1980) theory of development which places primary emphasis on the positive role multinational companies play in technology transfer. It is in these areas that Russians will increasingly find employment and that foreign firms will find future opportunity.

Japan: Linking Industries. Japan experienced negative linkage effects in 1946-47 (Ota, Tanikawa & Otani, 1992). As a result of energy supply bottlenecks, capital scarcity and ruined factories, steel and other basic industry production could not provide for producer-goods industry needs. Japan, however, responded by placing high priority on upgrading technology to increase the production of coal and steel. In turn the increased output of steel was used to rebuild coal mines to increase coal output, thereby making more energy and steel available to other industries and gradually bringing about recovery. Russia might similarly benefit from a priority system.

For reasons of neglect or war, Russia and Japan share the experience of needing to rebuild industrial capacity. But Russia must also create the system to do it.

Ecological Environment

Both Russia and Japan have suffered from the extreme abuse of the ecological environment.

Russia: Transforming Practices. The levels of dust, smoke and sulphur dioxide in Magnitogorsk, for example, are unacceptable (and comparable to those of other developing country cities such as Dehli or Beijing). While in parts of Russia a legacy of ecological destruction remains, to characterize all of Russia as despoiled is incorrect. Mainly the concentration of heavy industry in certain urban areas along with the use of coal has led to pollution levels approximately comparable to those in Western Europe and North America thirty years ago (Hughes, 1991). Low energy prices and old technology exacerbate the challenges of transition.

Japan: Linking Ecology and Technology. Japan has suffered environmental devastations. Yet, while pollution is still a problem in Japan, the Japanese commitment to continuous improvement in technology has led to immense improvement in Japan's physical environment. Further, MITI's industrial location and environmental protection bureau now closely monitors Japanese industry for compliance with stringent environmental standards. Where difficulties occur, compliance is sought through technology upgrading rather than retrofitting. This technology is available to the world. More to point, Japanese industrial policies focused on environmental and energy saving technologies. Any country can choose to do this.

Economic Environment

At macro and micro levels great differences exist. As in Japan, Russia's development of a sense of national direction may be a first step in the transition from command to market system, however, equally important are the many transitional steps. Indeed, the transition process is more a seamless web: structural changes require a price mechanism which sets realistic prices so that decisions about privatization and incentives can be rationally made, all of which require a stronger currency (Lipton and Sachs, 1992).

Yet there is a huge disconnect between macro-prescriptions and micro-realities. Pitfalls, created by the practices of the old Soviet central planning system, await new planner and foreign investor alike. For example, transportation infrastructure needs improving. In the intensive production system of the former Soviet Union, the Ukraine had 10 cable factories each specializing in a specific product and sending 145,000 KM of cable to other Former Soviet Republics (FSR), however it had to bring in 350,000 KM of still different types of cable for industrial use. Rationalizing and upgrading these factories would result in less waste and more efficient transport networks (Ota, Tanikawa & Otani, 1992).

Russia: Transforming People and Habits. Forced from a position of relative isolation to one of extreme economic vulnerability, the new reality for nearly 150 million Russian people has become exposure to macroeconomic forces. Consumer price inflation, at 20% in 1990, soared in the period 1991 to mid-1992 to over 1200% (*Economist*, 1992). As a result, the once stable Russian ruble has collapsed an impressive 99.92% against the U.S. dollar (Sesit, 1993). Producer price liberalization brought ten-fold increases in 1991-92 leading to decreasing industrial production, aging facilities, lack of infrastructure and inaccessibility of resources.

Personal savings, equivalent to 35-40% of Russian GNP, on deposit in savings banks are currently used to cover government deficits, but could be available for investment (Tselichtchev, 1992; Tselichtchev is also a Japanese scholar.) The effect of inflation on savings, however, could be huge. In addition, Russian banks have transferred some $20 billion in private funds abroad which may be available for re-investment.

Wage demands, to combat the decline in real Russian living standards, are increasing. Given the justifiable lack of confidence in the ruble, an estimated one-third of business transactions are conducted on a barter basis, which exacerbates production costs, output and prices (IMF, 1992). And taxes are rising. Private enterprises now are taxed at suffocating 80% rate, which is something of a paradox.

Russian business "profits" have risen, due to the practice of reporting the supposed value of output minus costs, rather than actual sales minus costs. What this means is that business inventories are being built, and goods withheld from the market, in hopes of cashing in at higher prices.

From late-1991 through 1st quarter 1992, in nominal terms retail sales tripled while stockpiled inventories grew eight-fold (*Economist*, 1992).

Thus, some continued state direction of micro-economic activity appears both necessary, in the light of collusive, system-wide withholding of goods and price gouging, and logical, if not inevitable, given 70 years of central planning. The open question, however, is: Can players from the old central planning apparatus nurture new market processes?

If Russian elites opt for a market-oriented economy, then they face a choice between two main alternatives–individualist or communitarian capitalism.

Individualist Capitalism. An International Monetary Fund memorandum (IMF, 1992) adopted as policy by Moscow early in 1992, focused on macroeconomic measures. These include freeing prices, reducing fiscal expenditures, establishing free trade and developing a single foreign exchange rate. Just how to do this without increasing production of necessities and in the face of increasing political unrest at continued decline in living standards remains uncertain. Notes Sergei Khrushchev (1993): "Russia inherits from the old system an extremely concentrated and monopolistic industrial structure. Disruption anywhere spreads havoc far and wide."

Centrally planned economies have long emphasized stability and long suffered from a lack of technical efficiency. Examples could be materials spoiling because of neglect, labor idling and so on. IMF prescriptions primarily relate to static economic efficiencies. Static efficiency, which subsumes technical efficiency, represents the ideal allocation of resources among all alternative uses at a given time. How a country strives toward this ideal turns upon the operational efficiency of its institutions, including, for example, the degree of centralization of economic decision making, the degree of industry competition, and the nature of the price structure. Hence, the IMF can assert that liberalizing prices, decentralizing decisions and increasing competition are critical to achieving a more efficient allocation of resources, as measured by the availability of goods to Russian consumers.

Presumably richly endowed Russia can avoid the trap of developing countries. Russia has the opportunity to exploit its resource base by liberalizing trade policies. Yet blind adherence to the static efficiency-oriented trade doctrine of comparative advantage can lead to unwelcome dependency and being locked into low end activities on the value chain.

Privatization. Even prior to the collapse of the planning system, the "shadow," or underground private, economy accounted for an estimated 25% of Russian GNP and 15% of the labor force (Treml, 1991). Thus it represents an important, if heretofore illegal, reservoir of "market culture." The challenge facing Russia might even be seen as "expanding the second economy" through privatization and by encouraging more small business creation.

Privatization by itself merely substitutes one bureaucracy for another. It must involve not only the selling off of state assets but also the creating of incentives which encourage a viable market system. These include items often taken for granted by a Western manager such as wages tied to productivity, responsiveness to customer tastes and shareholder pressures, and competition from other firms. Imbedded in the incentives issue is endemic corruption: rigged auctions, contracts for a politician's own company (Brooks, 1993), which undermine the market system. On the other hand, government organizations like the Smolensk Property Fund encourage the startup of private and quasi-private investment companies which are actually bidding against each other for shares of newly privatized companies. Privatization efforts centered in Nizhniy Novgorod (the former Gor'kiy) have been slow for many reasons: difficulty of determining real values, lack of stable currency forcing essentially barter conditions, difficulty in determining who really owns what and jealousy over ownership rights.

The Role of Emerging Financial-Industrial Groups. In a practical sense, the business community is gradually organizing into clusters of firms, centered by main Russian banks. At least in part they have a spiritual connection to the Gorbachev-initiated 1989 visits. These private *finansovo-promishlennie* groupings (FPGs) are concentrated around seven major banks: the Imperial Bank, Incom, Moscow Business Bank, Moscow International Bank (with some percentage of foreign capital from Germany), Stolichnaya, Toko Bank, and Manistap. In the process of privatizing state enterprises, these banks have been acquiring equity positions and then merging the business into coherent groups. While purely macro-economic prescriptions have fallen woefully short of addressing practical transition needs, the FPGs have been able to provide a modicum of stability.

Emerging Dual Economy. Yet privatization is only one aspect of the picture and, in fact, could obscure an important part–the nurturing of new, small firms. Smaller firms typically grow due to product and market innovations rather than cost reductions. Thus longer term economic growth comes from helping small firms expand. Both the FPGs and state firms may have a role in this.

Emerging is a dual economy, including private and state firms, with the former Foreign Trade Organizations (FTOs, still under the Ministry of Foreign Trade) becoming joint stock companies somewhat akin to trading companies. Ownership is held primarily by various Ministries or the Bank for Foreign Economic Relations (ASET, 1992). Today, however, the private FPGs are much more important than the FTO-based companies and each FPG also has a trading house. Recent actions by the Russian Congress (virtually this same Congress of Peoples Deputies governed, then dissolved in 1991, the former USSR) to limit Yeltsin reforms unfortunately underscore the tenuous nature of the support for change.

Japan: Exporting Communitarian Capitalism. Early post-War Japan also experienced inflationary pressures fueled by low commodities production and infrastructure in need of rebuilding. An industrial structure focused on heavy industry–chemicals, aircraft, steel, machinery–to meet military-related production requirements was similar to the Russians. Also, high capital needs, limited access to external sources; large domestic markets (Russia, about 150 million in 1991; Japan, 72 million in 1945) and educated labor forces were similar.

Figures 1 and 2 above set out two critical features of the Japanese model. First, macro level decisions involve consensus-oriented government planning to establish and implement policy. If the Japanese process ended here, then it would be similar to the indicative planning of "statist" Eurocapitalism. It does not, because, second, private sector corporate groupings both act together through the *zaikai* to establish national direction and compete through their member firms. To what extent then can Russia utilize the Japanese model?

As noted above, Japan and Russia have already had exchanges of delegations on both trade and "institutional" topics. More recent discussions have centered on integrating public control over private initiative to create a Russian "economic miracle." A Ministry of International Trade and Industry (MITI/RI, 1992) draft report, relying upon Japan's experience, asserts the need for active guidance of industrial direction by the state. Indeed, the "IMF first seeks macro-economic stability. After that they think the market will decide. From our thinking, this is not enough. Some kind of industrial policy is needed to supplement" (Schlesinger, 1992). This MITI view is shared by eminent Russians and fits more comfortably with Russian bureaucratic traditions. (Even the current IMF plan is to distribute World Bank funds through the former Ministries–to some extent reinforcing the centralized authorities.) MITI's government-oriented approach stresses the need for Russia's planned removal of bottlenecks to increase production while moving toward a market system. For example, Russia now suffers from sagging coal production due to many coal industry engineers leaving. To counter a similar decline in coal production, Japan took steps to keep miners food, housing and wages stable.

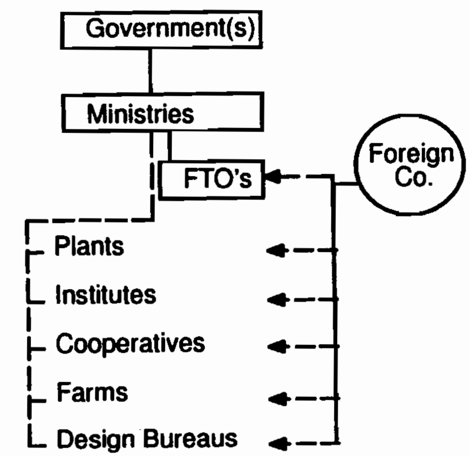
Similarities and Differences. Russia has in place a centralized planning structure, parts of which are roughly similar to Japan's and might be adaptable to a less rigid industrial policy process. The new process must encourage rather than command, promote rather than direct resource flows into critical areas such as developing new oil fields. In a sense then, the government-industry dimension exists and not much stands in the way of Russia's creating a range of policies.

With the rise of financial-industrial groupings, the possibility of establishing indigenous Russian corporate groupings has taken an interesting step forward. Still, at this point, many Russian firms still seem to be operating independently, rather than clustering together. For example, a consortium of German banks enabled AutoVAZ, a recently privatized car maker (Lada, Niva, and Samara lines), to become the first Russian company since 1917 to obtain a Western commercial loan without a government guarantee. To effect this required special exemptions from Central Bank dollar to ruble repatriation rules, which underscores the need for close government connections in any business deal. This is counter-intuitive because under the old system business transactions were primarily relational (as opposed to arms length market) which could have and may still provide a basis for corporate groupings. In addition, the lines of product flow were clearly drawn thus providing a kind of map for internal markets. In *keiretsu,* for example, these internal-to-the-grouping markets can account for as much as 50% of sales, but each group has its own map.

The net effect of changes, however, may leave more control in the hands of a new Russian *nomenklatura*–now becoming hidden owners of enterprise–and less in the hands of non-politically connected entrepreneurs, with consumers again left out of the equation. Russian political leaders are becoming rich: the new *nomenklatura* and entrepreneurs are forming alliances. Out of these alliances are coming the FPGs which are increasing in power and controlling influence. Thus emerging are Russian political-business power groupings which may in the process of creating policies and their mode of implementation, bring in aspects of the Japanese communitarian model, specifically the "intermediate" level corporate grouping.

An alternative to indigenous corporate groupings is linking up with Japanese groupings. Linking into the Japanese system could provide the Russian government with a model for financial intermediation as well as Russian business with access to capital and complete development packages. For example, the Japan Development Bank and the Long Term Credit Bank are government backed institutions that play an important role in supplying capital to other main Japanese banks and industries.

FIGURE 3B. Changes in Russia's Industry and Foreign Trade Structures



Does the Japanese model require close integration of global activities? Or, can a component of the Japanese system be separated from its whole? Whichever answer we might select, Japanese political-business leaders are clear in their aims. In the words of Koichiro Ejiri, former head of Mitsui & Co and now president of the Japan Foreign Trade Council: " . . . the development of the Asian economy with Japan at its center will be beneficial to everyone" (*Fortune*, 1992, p. S-12).

Political Environment

An institutional link between freedom of economic choice and freedom of political choice has yet to be forged in Russia. Yet in Japan, pluralistic power sharing arrangements among groups control both political and economic outcomes to a considerable extent.

Russia: Transforming Institutions. Figures 3A and 3B illustrate pre- and post-perestroika industrial guidance mechanisms and changes in Russian industry and foreign trade structure. Pre-perestroika a foreign company would approach the relevant Foreign Trade Organization (FTO), which would act as a go-between for cooperatives, factories and so on. Because of the foreign contact, FTO's were often staffed by trusted officials. Marketing was straightforward, the purchasers' agenda relatively clear, and business was safe in that great buyer-seller loyalty was established. The difficulty lay in access. Contacts and contracts were long term arrangements.

A foreign company now has many entry points (see Figure 3B for a simplified portrait.) Risk has increased, however, because credit worthiness is now an issue, and laws are in transition. Many if not most of the old players and institutions are still in place. Other political-economic obstacles have been identified (BISNIS, 1993):

- legal and governmental uncertainties including changing officials, regulations, tax policies and ownership laws.
- financial uncertainties including lack of an adequate banking system.
- inadequate information ranging from public laws to potential markets and business partners.
- infrastructure problems including inadequate communications and transportation systems.
- limited trade relationships including the lack of normal bilateral trade agreements between the U.S. Government and Russia.

Japan: Moving toward Democracy. The Japanese pre- and post-War economy flourished under close reciprocal business and government relations within a pluralistic decision process and power structure (at least including large powerful businesses).

Subsequent to World War II, Japan pursued vigorous producer-oriented, mercantilist policies which strongly favored business over consumers. Yet given the example of restrictive but successful Japanese policies bolstered by closed *keiretsu*-type practices in building Japan, a strong case can be made for Russia's following a similar economic model.

A major difference, however, is that the Korean War came along enabling Japan to ramp up its economy based upon U.S. economic demands. Russia, on the other hand, is largely dependent for major stimulus on stopgap international welfare and limited by well-intentioned IMF policies.

Whether the Kuril Islands will prove an insurmountable stumbling block to Russian-Japanese relations is a long term concern. In other words, where political disputes now exist, it is likely that mutual economic interests can prevail.

CONCLUSIONS

Can the Japanese model "marketize" Russia? Put another way, which model of capitalism has been followed by virtually every successful East

Asian industrializing country since 1960? Some parallel exists between conditions in Russia (and even China) today and the East Asian "dragons" of twenty years ago: limited indigenous private enterprise, few people with experience in managing outside the military or state-owned enterprise, and very limited experience with either political democracy or economic markets.

Implications of the Japanese Model for Russian Leaders

Japan has successfully exported its political-business model to many areas of the world. According to Leon Hollerman (1988) Japan has been rapidly moving its older "smokestack" industrial base offshore, especially to lower wage areas, to reduce costs and increase "imports"–firms remain tied to their Japanese corporate grouping. It is in this context that much development has occurred in newly industrializing countries. The economies of Malaysia and Thailand, for example, have been largely integrated into Japan due to close ties to various corporate groupings and to much foreign direct investment. While corporate grouping headquarters remain in Japan, along with most high value added manufacturing, a steel plant may be opened in Brazil, a cement factory in Bulgaria. Products then may serve the local market and be re-imported to Japan. The effects on the developing country are mixed–on one hand it gets much needed industry and jobs, but on the other, it also may get locked into the low end of the value chain.

Still, much Japanese experience is relevant to Russia. Japan saw the need in early Post-War II times to: utilize industrial policy measures to get resources to critical areas; abolish many economic controls and liberalize trade and capital flows; develop a base for competition; create a market for corporate stock ownership and improve managerial skills; convert military industries to civilian uses; encourage capital formation in business through, for example, generous depreciation allowances; enhance industrial technology (for example, establishing subsidies and favorable tax treatment for R & D activities and checking increases in royalties to conserve foreign exchange); promote exports (for example, the government established the Export-Import Bank of Japan in 1951 for export financing and the Japan External Trade Organization (JETRO) in 1954 to carry out overseas market research); and encourage the "soft" infrastructure of the economy (such as the promotion of industrial standards and the creation of laws on patents and trademarks). This same list could belong to Russia.

Yet Russian products are expected to compete head-on in the world economy. Russia is expected to do so in two years when it took Japan twenty. Thus, strong links into world markets are likely to prove critical and these can be provided effectively by the *sogo shosha*, but at a price.

Internally, however, two main implications emerge: the need to foster the development of small business; and the need to encourage the financial-industrial groupings (FPGs). Small business provides the vehicle for the greatest indigenous growth and job creation. Since small business can prosper and grow only in an environment relatively safe from criminal elements, it becomes the government's role to provide that environment along with reasonable rules for commerce.

Curiously, both Japan and Russia have criminal elements which play important roles in business operations. Recent private reports on Russia suggest that 30% of business profits go to "protect" the business.

As noted, however, a major focus of Russian development should be small business creation and this can occur effectively under a communitarian system. It may be that small firm ties to larger firms would provide financial security and market access not available otherwise.

Implications of the Japanese Model for Western Firms. Four main implications emerge: the importance of providing complete "packages" for large deals; the range of market opportunities for smaller firms; the need to overcome many obstacles in the Russian environment; and the importance of political-backing to business negotiations.

Japanese "Package" Deals. The international implications are striking. Many advantages could flow to Russia and its firms. The *sogo shosha*, for example, can package mammoth deals including hardware, software, personnel, infrastructure (transportation, power, communications), financing and markets (Cutts, 1991). The components in the package are drawn primarily from firms within a corporate grouping and often can include special Japanese government dispensations as well. Increasingly, competition is waged between corporate groupings on a scale beyond the capability of even the largest single firm.

Even strategic alliances and international joint ventures fall short of *sogo shosha* clout. To the extent that situation obtains, international managers may suffer barriers to access similar to those into the Japanese market. One response is to create more custom-tailored deals.

From the Russian perspective, however, both Japanese and Western firms are still foreign firms. Thus large turnkey companies, such as Fluor or Bechtel, and service companies which create and enhance indigenous capabilities should find opportunity.

Range of Russian Market Opportunities. BISNIS (1993) estimates that the top three product markets–computer and peripherals, food processing and packaging equipment and medical equipment–exceed $5.5 billion.

The food processing and packaging industry (selected because insufficient data exist for computers) illustrates both problems and market opportunities in Russia. Heavy losses of consumer food products both in pre-processed agricultural products and in poorly packaged goods necessitate construction of modern food processing and packaging facilities closer to production sites. Specific markets for dairy processing equipment ($300 million), meat and poultry processing equipment ($500 million), and beverage equipment ($300 million) suggest real opportunity. BISNIS reports high receptivity to U.S. products, few market barriers but very heavy competition.

Common Obstacles. The STEEP framework provides the underpinnings for a firm's assessment of Russia. Since a company will operate in a host country's STEEP environments, trends there will influence both entry mode and operational decisions and major obstacles exist in them all.

Getting paid presents a special challenge. Since only the highest priority items will be bought for hard currency, most Western firms will have to learn to deal with the intricacies and variations of countertrade. In the commodity countertrade model Western firms accept local currencies for products and services, purchase local goods with local currencies and then sell these goods through international commodity exchanges (White, 1992). Or, in what may be called the "McDonalds variation" Western firms may choose to reinvest in Russia, with repatriation of proceeds well into the future.

The positive thing to be said, however, is that all foreigners face similar obstacles to doing business in Russia. The challenge for the Western firm is to clearly delineate a business strategy for dealing systematically with all aspects of the STEEP environments . . . and to meet Russia's innate need for job creation.

Political-Business Negotiations. Russia's choice of direction is by no means fore-ordained. Business deal making will be within the political context of Russian interests. Western firms are seen as representatives of their countries and thus may be subject to other than economic considerations. For example, just as developing countries once sought aid and military assistance by playing off Soviet and American interests against each other, so also Russia may seek economic benefits by counter-balancing Japanese and Western interests. Foreign governments are likely to be implicit partners, along with foreign and Russian firms, in most large deals. The implication, of course, is that the capitalist model whose firms have close home-government business relations will enjoy a tangible advantage in the political environment.

Assuming a modicum of political stability, international businesses most able to provide real, tangible, deal by deal advantages and the largest potential for job creation will have the greatest chance of success in Russia.

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