Keiretsu

Keiretsu is the “Japanese form of corporate organization that involves a grouping or family of affiliated firms that form a tight-knit alliance and work to each other’s mutual benefit” (Roy, 2009). It is commonly referred to as a ‘spiderweb’ that is a complicated network of relationships. Through relying on building the relationships between one another, this can help firms to increase competitiveness in the Japanese economy, such as engaging in corporate investment to increase revenue. After the end of WWII in 1945, the Japanese economy underwent major changes in the organizational structure. This prompted an entire restructuring of the Japanese economy from 1945-49. For example, in 1953, the Ministry of International Trade and Industry’s (MITI) Industrial Rationalization Counsel called for trading and manufacturing companies to group in order to concentrate scarce capital in the domestic economy (KWR International Inc., n.d.). Anti-monopoly restrictions were also relaxed during this period of time (KWR International Inc., n.d.). Following which, one of the major changes was the dissolution the zaibatsu which are huge industrial companies that were also family enterprises (Watkins, 2015) during the Meiji Era. Keiretsu hence formed from these reorganized zaibatsu to ensure that they could capture a larger share in the market amidst a stable economic environment. There is also a cultural reason for the keiretsu, which stems from the Confucian tradition of loyalty. Loyalty was a huge factor in maintain the familial relationship among businesses as well as the relationship between the government and the business.

Types of Keiretsu

Vertical Keiretsu

In a vertical keiretsu, the core manufacturing firm and the suppliers are at the centre of the network (Mc Guire & Dow 2009, p. 338). For instance, suppliers can hold small positions in those big firms (Mc Guire & Dow 2009, p. 338). Producers, wholesalers and retailers have a close relationship and each will affect the other through a downward chain. Huge companies can buy shares from one another to maintain this downward chain.

Horizontal Keiretsu

In the horizontal keiretsu, the six industrial giants currently are Mitsubishi (consisting of companies like Mitsubishi Electric, Kirin Brewery etc.), Mitsui (Suntory, Toshiba, Toyota etc.), Sumitomo (Asahi Breweries, Hanshin Railway, Mazda etc.), Fuyo (Canon, Hitachi etc.), Dai-Ichi-Kangyo (Fujitsu, Hitachi etc.) and Sanwa (Hankyu Railway, Toho etc.) (Roy, 2009). Yet, recent mergers by the keiretsu have reduced the number to four. For example, in 2000, Sumitomo and Mitsui merged under Sumitomo Mitsui Banking Corporation. (Mc Guire & Dow 2009, p. 334)

Advantages

Keiretsu will help both parties achieve benefits. Firstly, the access to stable financing, secondly, protection from market pressures, thirdly, reduction of risk, fourth, monitoring benefits and reduction of information asymmetries. Information asymmetries refers to a situation in which “one party in a transaction has more or superior information compared to another” (Investopedia, 2003). Therefore, having a keiretsu will close the information gap between the companies and they can compete on a more equal playing field. Lastly, mutual assistance for each other (Mc Guire & Dow 2009, p.335). Due to mutual help from one another, there are situations when the stronger firms will give financial aid to prop up the weaker firms as in this alliance, both firms will benefit if they are financially well-off. With “vertically integrated alliances between suppliers and manufacturers” (Roy, 2003), this will result in suppliers benefiting such as long term contracts. (Roy, 2003) Finally, the Kanban system which a relay system where the flow of parts were produced according to the same number of demand (Whatlis, 2015), also ensures high quality products, providing a major competitive advantage for a large number of Japanese industries. (Roy, 2003)

Criticisms

Main criticisms of the Keiretsu include the high barriers of entry for foreign firms due to the collusion of the firms with the government. The high protectionist barriers are prevalent in the example of the automobile market. The government also strongly protected businesses to the extent of propping up failing local businesses. The huge financial aid spent on saving these firms instead of letting them go bankrupt was also one of the factors for the collapse of the bubble economy in the 1970s. Due to the vertical relationship of producers, wholesalers and retailers, outside firms will find it challenging to break into the market due to these close relationships (Roy, 2003). Lastly, the Japanese channels take a longer time and are more expensive to operate (Roy, 2003). The additional costs are then imposed on the customers because of the inefficiency generated due to the tedious process of the keiretsu.

Additional short reading:

How the American model of keiretsu differs from the Japanese model of keiretsu

http://www.economist.com/node/14299720

References


