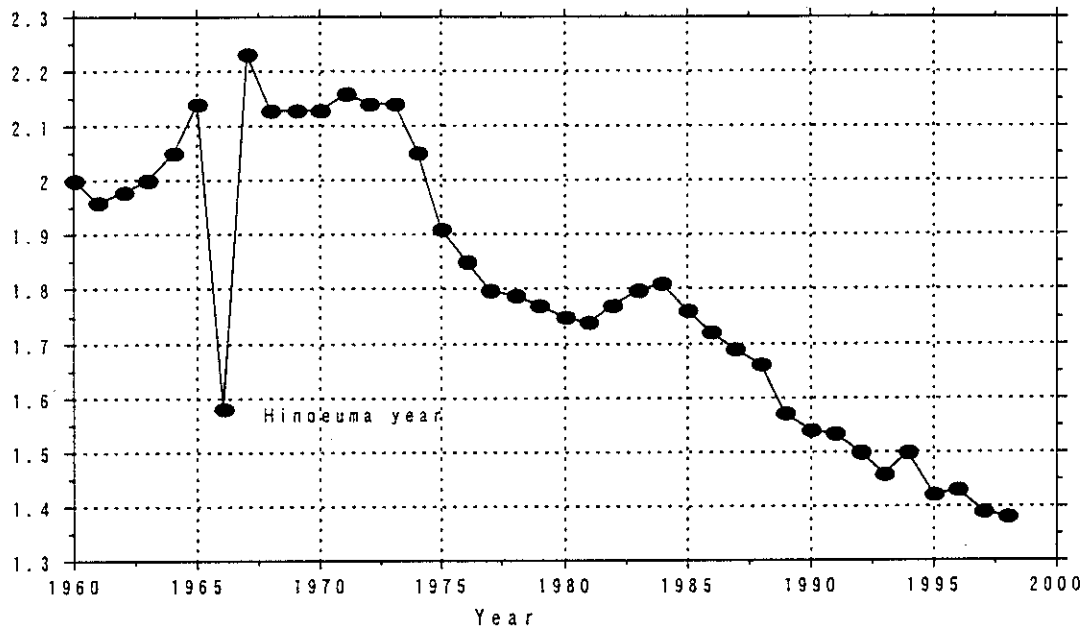


data of 1960~98 suggests that the ratio of female employees is positively correlated with the age at the first marriage of the woman, and the age of marriage is negatively correlated with total fertility rate.

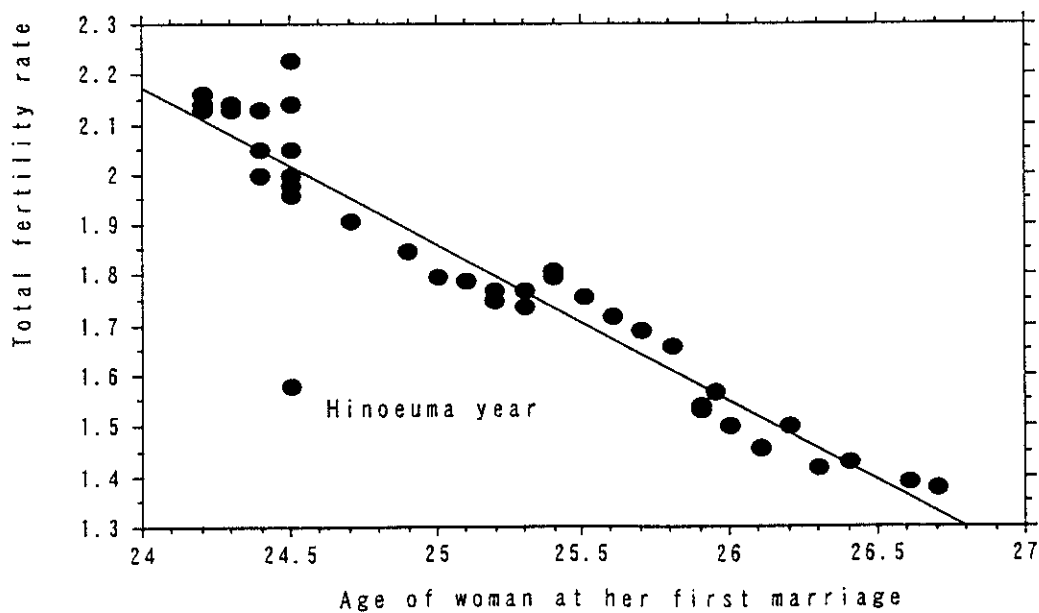
**Chart 6 Total Fertility Rate, Japan**



Source : Ministry of Health and Welfare

If this conjecture is correct and if these relations do not change, the total fertility rate will decline further, for the labour participation ratio of woman is expected to increase, though these relationships are not inevitable.

**Chart 7 Relation Between Female Employment and the Age of the Woman at Her First Marriage**



Source : Ministry of Health and Welfare

The experience in Sweden suggests that active family policy may be helpful to coincide the increase of labour participation ratio with recovery of fertility rate.

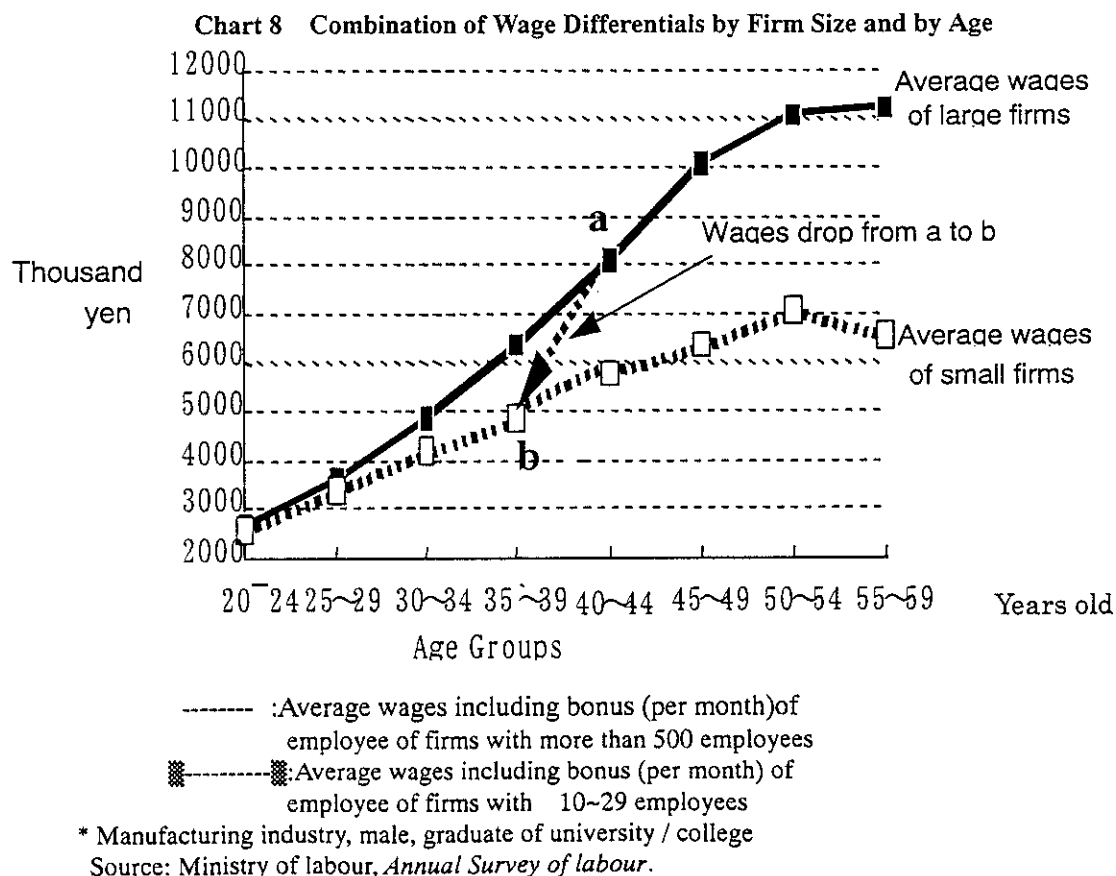
Based on these arguments, the Equal Employment Opportunity Act and maternity leave with income compensation for female employees were introduced in the 1990s. Day care facilities for children are being reformed to cater for working women. Though the wage replacement ratio during maternity leave are still low (25 % of wages from employment insurance funds and social insurance contribution from employers), they are expected to improve in future.

The Government financial plan for social security is based on the assumption that the total fertility rate will recover from 1.38 in 1998 to 1.61 in future. Assuming the population estimate, the proportion of the elderly to the total population in 2025~2030 is forecast to increase to 28.0. If the total fertility rate recovers more than that, the future prospect of the financial situation of pension and social security funds will be brighter.

As the financial balance of social security depends much on welfare benefits recipients /cost bearers ratio as well as replacement ratio of social security benefits, those policies that promote employment of women and the elderly will have positive effects on the balance.

#### 4 . Dual Wage Differential System: Combination of Differentials by Seniority and by Firm Size

It has become fashionable among economists to show that the seemingly irrational practices at Japanese companies can be logically explained by micro-economic analysis. For example, it is possible to say that the Japanese wage system is a well-devised combination of two kinds of wage differentials. They are wage differentials by age and by firm size. The wage differentials by firm size are not so unique, but the combination of these two wage differentials as shown in Chart 8 is unique and it worked as an effective incentive system for employees of large firms.



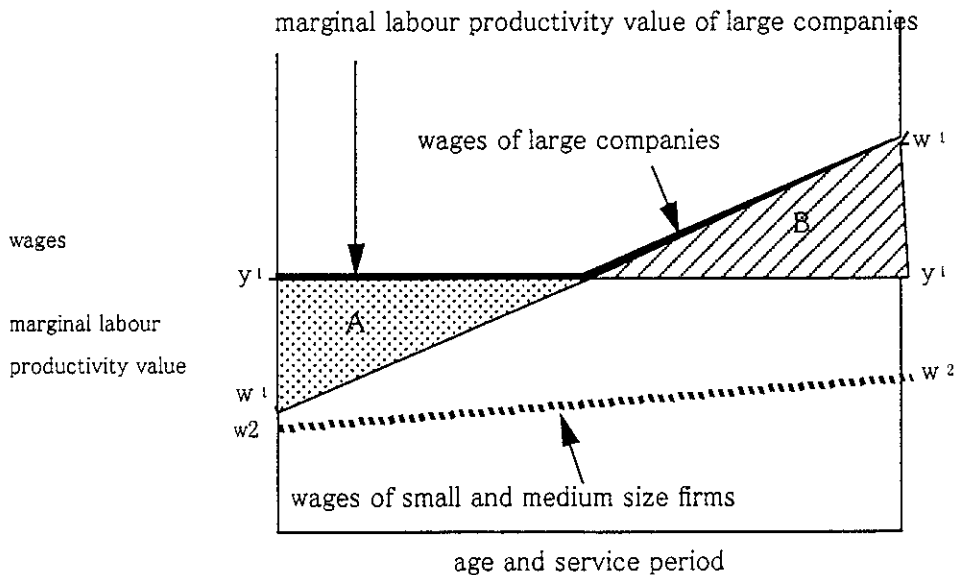
As the efficiency wage theory suggests, it is more profitable for management to maintain relatively high wages for their employees. By keeping higher wages and better fringe benefits, the large

companies can recruit better workers, prevent quitting and shirking, and can stimulate the morale of the employees (Akerlof,1986). In Japanese large firms these effects are reinforced by the seniority wage profile. Under this dual wage differential system, the economic situation of a worker who quits a large company deteriorates seriously. The longer the length of his service years, the larger the loss of his wages including fringe benefits. His wage including fringe benefits will, say, drop from 'a' to 'b' in Chart 8, if he quits the large company after working there more than several years (Maruo,1989). Employee's loyalty to their companies and relative high efficiency of large firms in Japan may partly be explained by this fact.

### Efficiency Wage Theory, Share Economy and Seniority Wage System

Though this system is not fair from the viewpoint of equal pay for equal work, this well-devised incentive system has contributed to improve labour productivity of large firms. As the efficiency wage theory insists, it is efficient for large companies to keep relatively high wages. High productivity in large Japanese companies seems to support the hypothesis of the efficiency wage theory in this respect. However, contrary to the hypothesis that was introduced to explain persistent unemployment, the unemployment rate has been low in Japan, where the wage differentials between firms are larger than those in other industrialized countries. This inconsistency between theory and fact should be explained. The inconsistency between the efficiency wage theory and the share economy hypothesis (Weitzman, 1984) should also be considered. The former tries to give a microeconomic foundation for persistent unemployment and the latter hypothesis insists that a share economy reduces unemployment. As Chart 11 suggests, large Japanese companies have a distinguished feature of efficiency wage system. Their wages and labour productivity are apparently higher than those of medium and small firms. On the other hand, large Japanese companies have an essential feature of the share economy as well, for wages of new employees are usually smaller than the marginal labour productivity value. It seems difficult to reconcile these two theories. However, this seeming contradiction can be explained if we assume that the large company sector in Japan has an essential feature of the share economy while in the rest of the sector market clearing competition prevails.

**Chart 9 Wages, labour productivity value at Japanese Firms**



$y_1 > w_1$        $A=B$  at present value.

Fringe benefits are included in wages.

In the former sector, where the Japanese seniority wage profile is notable, the wages of a new employee are usually lower than the marginal value of labour productivity, for most new employees

of large firms are young workers because of lifetime employment practices.

Still the wages of large firms including fringe benefits are usually higher than those of small and medium sized firms. The relationship between wages and marginal labour productivity value of large and smaller firms is illustrated in Chart 8.

If the relation between wages and productivity in the Japanese wage system is as shown in Chart 8, employers of large firms will have an incentive to employ young workers, while the merit of efficiency wages at large companies will be maintained at the same time.

It is interesting to note that J.E. Meade's model of labour stock scheme assumes a similar income ---wages + income from shares---curve to that of the Japanese seniority wage system. In both systems the wages of new employees are smaller than their labour productivity.

### Lifetime Income Maximization Hypothesis (Future Pie Theory) and Optimum Share of Wages

Moreover, under the Japanese management system employees and employers are likely to agree to keep the share of wages at a relatively low level expecting to receive larger pie in future. In fact the share of wages and the ratio of dividend (the payout ratio) in profits at large companies in Japan have been low. These practices appear irrational in the short run for both employees and shareholders. However, in those companies where the typical Japanese practices of management are introduced, there is a good possibility that both the management and employees will agree to choose a relatively low share of wages and low payout ratio as well. This is because employees, who are promised lifetime employment at the companies, want to maximize the present value of employees' lifetime compensation (including fringe benefits such as employee pension and retirement pay). They will choose to have a larger pie in future, if they think that the implicit contract on the following conditions is reliable.

- (a) Lifetime employment is promised and secured.
- (b) Fair distribution of the "future pie" as a result of the higher rate of productivity increase is guaranteed.
- (c) Employee participation and communication through joint consultation systems<sup>1</sup> and informal contact is introduced.
- (d) A large portion of profit will be reinvested to improve productivity by keeping the dividend ratio low.

Employers, too, will accept the above conditions, if it is effective to persuade employees to keep cooperative labour-management relations and a modest share of wages. Besides, as most Japanese managers are implicitly promised lifetime employment at their companies or related companies, they are more interested in making their companies grow than to receive larger dividends now. Moreover, it is sometimes pointed out that as Japanese companies have extensive cross share holdings, a high payout ratio is not always favourable for employers. Therefore, they are likely to choose to maximize the present value of profits (including capital gain) and their salary not in the short-run but in the long run taking future pie into account.

We may assume that the share of wages that maximizes the present value of lifetime wages including fringe benefits is optimum and fair for the employees, if above conditions (a)-(d) are satisfied. "The three principles of productivity movement of the Japan Productivity Center" intend to guarantee conditions (a)-(c). Condition (d) has been implicitly accepted (for a mathematical explanation, see Maruo, 1989).

## 5 Restructuring Japanese Management towards a New Model

### Cooperative Labour-Management Relations

Japan has won a reputation not only for employment security and cooperative labour-management relations but also for well-devised incentive wage systems. However, the Japanese style of company

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<sup>1</sup> More than 90% of Japanese large firms with more than 1,000 employees have their joint consultation systems.

management and labour-management relations are now faced with difficult problems and require reform. The Japanese model of business management worked well when the average age of employees was low and the economy and companies were growing steadily. With Japan's workforce ageing and its economic growth rate low, the Japanese model does not work well. Globalization of markets is another factor promoting the restructuring of the Japanese style of business management.

(1) First, the seniority wage and promotion system has become difficult to maintain when the number of older employees increased.

(2) Second, large wage differentials between male and female workers and between large companies and small firms cannot be justified. If condition (1) and (2) are discontinued, the incentive functions of the Japanese wage system will disappear.

(3) Third, the group oriented trade practices that tend to treat outsiders differentially cannot be justified in the international market.

(4) Fourth, the Japanese method of policy management proved efficient when the economy was at the catching up stage, but is unsuitable for encouraging the creative activities of employees. Lifetime employment, seniority wage system and firm specific employees' education and fringe benefits have to be reformed without losing their merits.

(5) Under the Japanese seniority wages and promotion system, creative and distinguished talents are not rewarded and, therefore, are not suitable for technical progress. Foreign companies recruit those talented workers at higher wages.

(6) Restrictive practices in financial institution are required to replace to free market mechanism.

The weak points of the Japanese model of management, then come to the fore.

To overcome these weak points, it seems necessary to reform the Japanese model of management in the following ways.

a) The labour force reserve, mainly the elderly and women with children, must be more efficiently employed. The government has introduced active labour market policy them to support their employment,

b) Productivity in the low productivity sectors must be increased. The low productivity sector is another important potential productivity asset which must be developed. Deregulation is a possible effective policy to strengthen the sheltered low productivity sector.

c) New incentive systems for productivity increase to supplement the Japanese model of incentive system are necessary. Employees share-ownership plan and participation in management and information are possible ways to make employees feel that the company is also 'theirs'. If the labour stock scheme suggested by J.E. Meade (Meade, 1989) is introduced, the essential merit for employment incentive will be maintained, for the <wages + company share> of new employees will be kept smaller than that of senior employees and, therefore, there is a good possibility that the wages that have to be paid for a new employee will be maintained less than the marginal labour productivity value. About 90% of the listed companies in Japan have employee share holding schemes. The schemes may be developed for the purpose. Introduction of a stock option scheme to all employees in principle is one of the possible methods of employees share ownership. The ESOP (employees share ownership plan) mainly developed in the United States is another possible plan.

d) Many Japanese companies have begun to introduce a dual system of employment to maintain the merits of the Japanese model of management on the one hand and American meritocracy on the other hand. One system is a traditional Japanese model where employees are implicitly secured lifetime employment and seniority wage and promotion systems are applied. Another system is an American meritocracy system that rewards talented workers with high annual income. Japan Productivity Center for Economic and Social Development recommends the dual system.

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## Chapter 4 Changing Japanese Labour Markets: internalisation and Externalisation of Labour Markets, and Public Policies

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### 1. Introduction

The Swedish economy and labour markets attracted considerable attention as a model of the welfare state in the latter half of the twentieth century. Similarly, the Japanese management and industrial relations systems attracted considerable attention in the 1970s and the 1980s, because the efficient working of labour markets has been credited to Japan's employment practices. Still, it is not uncommon these to be some misunderstanding of Japanese employment practices among people studying Japan. One stereotype, for example, asserts that, under the lifetime employment practice in Japan, most redundant employees are kept on the payroll of firms, with the result that Japan's unemployment rate is always low relative to other developed countries, even in times of recession.

It is true that many employers in Japan do not easily lay off or dismiss employees thanks to the *long-term employment practice*. Indeed, the unemployment rate has been low in Japan even after the bubble economy crashed in the 1990s, because employers are committed to the practice. However, the practice itself is followed mainly at large firms and the public sector, whereas the majority of workers in Japan are employed at small firms, where this practice hardly applies.

Large firms in Japan usually depend on their internal labour markets. That is to say, most large firms and government offices in Japan recruit applicants who are fresh from school to start work at the bottom of job ladders, and upgrade them within their organizations until they reach the age of retirement once a short probationary period is over. Many medium-sized firms follow the practice of this long-term employment.

In contrast, such nonregular employees as contract workers and part-time workers have traditionally been widely used as a buffer so that employers can adjust the size of their workforces to suit fluctuations in demand for labour. The buffer ensures that employers can economize labour costs while providing core employees with stable employment. This nonregular employee segment of the labour market has long been regarded as a dark side of the economy. Therefore, some labour market policies aim at protecting this sector of the workforce.

Recently, however, a new type of workforce has been increasing in this sector. Married women and students prefer to participate in external labour markets *voluntarily* as part-time or contingent workers. In addition, many firms are more likely to utilize part-time, contract, or temporary workers than they used to be, their aim being to maintain flexibility in their employment. Job opportunities and the needs of job seekers come together in labour markets to bring about an increase in short-term, unstable employment.

The globalization of the Japanese economy tends to expose Japanese employers to an uncontrollable business environment. The growth of the service sector in the economy generates job opportunities in the nontraditional, less stable segment of the labour market. In addition, the rapid aging of the population means the aging of Japan's workforce, which in turn may make it difficult for Japanese

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<sup>1</sup> I would like to express my gratitude to Professor Naomi Maruo for his helpful comments. Special thanks are due to Professor Shozo Inouye who revised my first draft and translated it into English to complete this chapter.

employers to maintain internal labour markets that rely on applicants fresh from school as a source of the workforce. Thus, there will be very pressing needs for new labour market policies that cater for the needs of nontraditional work relations. This paper aims at describing structural changes in the Japanese labour markets with the view to elucidating some new directions in Japanese labour markets policie.

## 2. The Structure of Japanese Labour Markets

Many studies of labour market structure have found the characteristics of labour market segmentation, describing them by such notions as primary vs. secondary labour markets, and core vs. peripheral (or marginal) labour markets (e.g., Averitt (1968), Odaka (1984), and Rosenberg (1980)). In dual labour market theories, jobs in a primary (or core) sector are characterized by good working conditions; high wages and salaries, stable employment, and abundant opportunities for advancement within internal labour markets. The secondary (or peripheral) sector, in contrast, is characterized by, among other things, low wages, poor working conditions, unstable employment, and poor training and promotion opportunities. Labour markets in the real world are composed of multiple layers of stratified segments, as the dual labour market theorists assert.

The dual labour market theory would be an apt description of the structure of Japanese labour markets in the 1950s through the 1970s. In the 1950s and 1960s, when Japan's postwar economy was at an early stage of development, its economic structure favoured a dual structure, with the heavy and chemical engineering industries at the top, and their supporting small firms at the bottom. Subcontracting between parent firms and their affiliates characterized the relationships between the primary and the secondary sectors. The capital-intensive large firms enjoyed high labour productivity, while labour-intensive small firms did not. Labour market characteristics were associated with the dual economy: workers in large firms enjoyed better wages and working conditions while those in small firms did not. It is safe to include governmental and non-profit organizations and universities in the primary sector, but most small firms and self-managed undertakings belonged to the secondary sector.

Placing the two sectors at the opposite extremes of a scale, the dual labour market economists called for protective policies for the disadvantaged sector, because workers in it found it too difficult for them to leave it and to climb up to the primary sector.

Ohkawa (1965), in contrast, asserted that wage differentials among enterprises were stratified in association with the firm sizes and that their continuity should be underscored to describe the Japanese economic structure. That is, he asserted that the structure was not divided into two polar sectors but that it included layers whose boundaries were blurred, and that it should be appropriate to call them a *differential* structure. This hypothesis drew attention to the fact that there existed many medium-sized enterprises between the large and small firms, and that they were stable in operation and provided good job opportunities as "Chuken Kigyo" (well-managed, medium firms).

The high economic growth in the 1960s created new demands for labour, and this shifted the labour market from the *unlimited-supply* to the *limited-supply* stage. Maruo (1965)<sup>2</sup> estimated the turning point to be around the years 1960-65. Employers faced the new labour market that gave them an incentive to internalize their work organizations.

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<sup>2</sup> Maruo (1965) shows that the number of self-employed and family workers reached a peak in 1955, then gradually decreased. Breaking down the total number of labour force into two categories: (1) the self-employed and family workers, and (2) all other regular employees, he reported that the latter exceeded the former in 1960. He concluded that it was in the 1960s that the Japanese labour economy structurally transformed from a semideveloped to a developed stage.



### 3. Internalising Japanese Labour Markets in the 1960s-70s

Theoretically, a factor of production, say workers (or capital), tends to move into a more productive (or profitable) sector from a less productive (or profitable) sector. In practice, however, there always are some barriers against mobility between, for example, a core and a secondary sector. Enterprise-type internal labour markets generated by large firms in the 1960s turned out to be a typical barrier against labour mobility. Japanese dual labour markets reorganized themselves into a new dimension to include external and internal labour markets in the 1970s.

One school of thought (Iwata 1989) asserts that the dual employment structure in large firms included both a core workforce that enjoyed a long-term, stable employment, and a peripheral workforce that faced a short-term, unstable employment, and that this originated in Japanese feudal traditions of village communities. Their core sector first included managerial employees, and gradually expanded to include clerical workers and eventually blue-collar workers. It would be appropriate, however, to hold that the employment relations in the primary sector advanced to be a part of the economic system in late 1950s and in the 1960s, when demand for labour in the manufacturing industry increased very rapidly.

Enterprise-type internal labour markets hire new employees from applicants who are completing a higher education and who have not had any previous work experience. Full-time employees in an internal labour market are shielded from direct competition with workers in external labour markets, being under an implicit employment contract that usually guarantees them stable employment until they reach the mandatory retirement age. Their earnings increase in line with the length of service. This upward rising earnings profile corresponds with accumulation of human capital on the part of employees, because employers and employees interact with each other calculating costs and benefits incidental to investing in job-related training. It appears that the earnings profiles are seniority-based, yet one should not regard seniority as an automatic accumulation of length of service at a firm. The length of service reflects the time consuming investment behaviour.

The pay systems motivate employees to upgrade themselves on a career ladder within their firm. It is important to note that the traditional Japanese seniority system does not evaluate employees only on the basis of their ages or their length of service. Koike (1981, 1988), for example, asserted that internal labour markets were not dull work organizations but that covert competition among employees was there to provide the organizations with competitive edge on the basis of human capital. All the employees, including blue-collar workers, are subject to merit ratings. Evaluation criteria not only include job performance, aptitude, and potential, but also such subjective items as "cooperative behaviour." Employees' loyalty to employers may be considered partial grounds for employment security when employees assess their employees in internal labour markets.

Firms are required to screen applicants carefully because recruitment and selection are an important part of investment under the long-term employment practice. To make this investment profitable, employers systematize education and training schemes in the internal labour market with a view to improve labour productivity. Most internal labour markets, therefore, have in-house vocational education and training programs and many large firms have their own training schools.

Moreover, in-service training is not limited to off-the-job formal training; it also includes extensive on-the-job training. Thus, such personnel practices as job-rotation is commonly put into practice to advance employees' job capability through their learning on the job. Evaluating the performance of employees in internal labour markets, therefore, inevitably has a long-term developmental perspective.

Another supporting factor in the primary sector is an extensive use of supplier networks, including subcontracting and outsourcing. Suppliers in Japan are not a short-term, cost minimizing apparatus for the parent firms; suppliers and parent firms are under long-term relationships in which they

collaborate to fix such an issue as parent firms' employment levels in response to economic fluctuations. Thanks to the stable supplier relationships, a number of medium firms grew in size and were included in the primary sector. They joined the club of good employers that extended stable job opportunities to their employees when the economy grew fast in the 1960s and the 1970s. Not all the jobs were good jobs. Figure 1 shows that the longer the length of service of workers, the higher the probability of their staying in the same job. The relationships of the two variables indicate that certain jobs belong to the primary sector while others belong to the secondary sector. Jobs women

Percentage of Employees Holding the same Jobs (%)

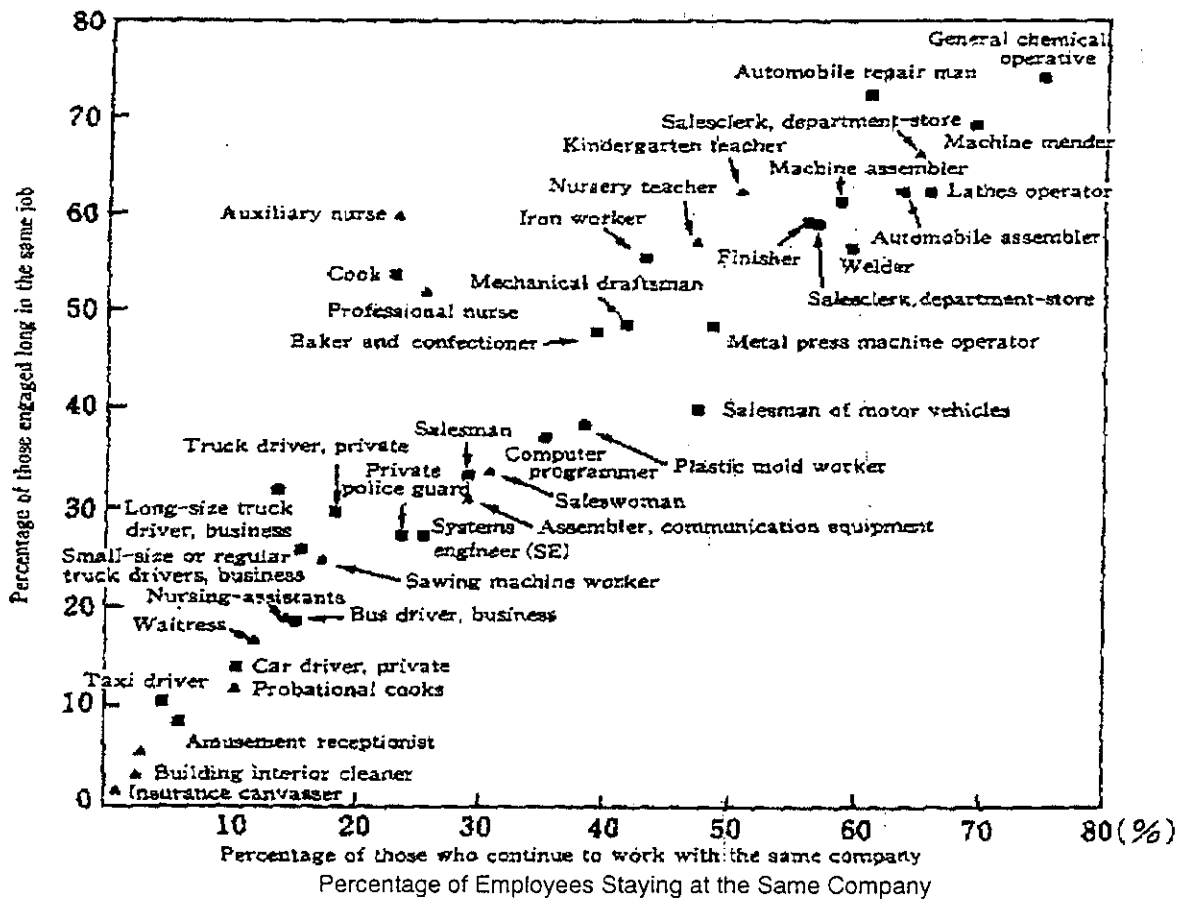


Figure 1. Relationships between the Probability of Employees Staying at the Same Company and Holding the Same Jobs

Source: Estimation by the Ministry of Labour, using the special tabulations of the Wage Census, the Policy Planning and Research Department, Ministry of Labour.

Note: The probability of staying is calculated as the ratio of workers who stayed at the same firm to total employees, and that of same-jobholders as the ratio of workers who kept the same job to total employees.

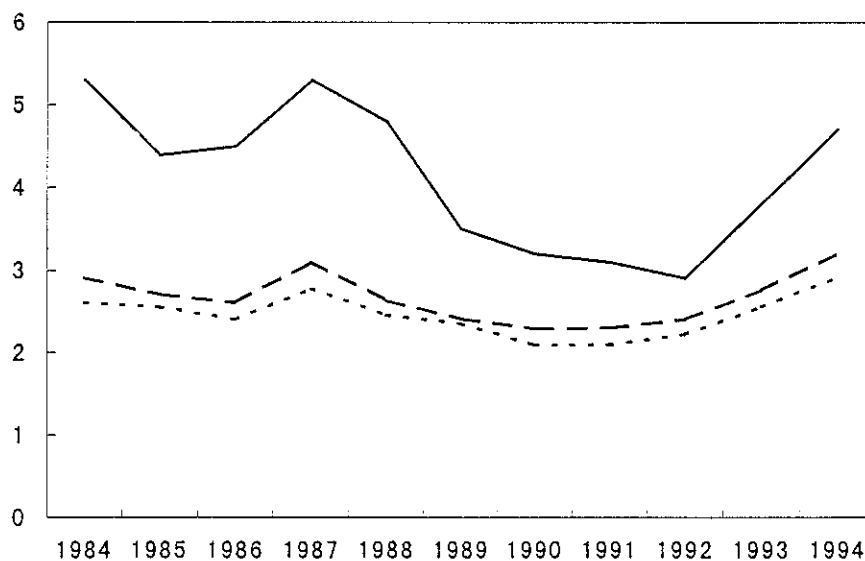
■ indicates male jobholders, and ▲ indicates female jobholders.

held tend to cluster near the origin, reflecting the fact that their length of service, on the average, was shorter than that of men.

#### 4. Structural Changes in the Japanese Economy and the Expansion of External Labour Markets

A characteristic in a secondary (or peripheral) sector is that labour turnover within the sector tends to be high and does not usually cross the sectoral boundary because most jobs are bad and dead-ended. A large part of the workers in this sector are those nonregular employees who are under fixed-term, part-time, temporary, or seasonal employment contracts. Unskilled migrant workers are likely to be in this sector, too. Figure 2 shows that the unemployment rate of nonregular employees (part-time or temporary workers and the like) is as much as two percentage points higher than that of regular employees. The differences in the unemployment rates between nonregular and regular employees are

Figure 2. Unemployment Rates - Nonregular Employees (%)



Source: Statistics Bureau, Management and Coordination Agency, *Report on the Special Survey of the Labour Force*, Tokyo: Ministry of Labour (each issue).

Note: 1) Nonregular employees include part-time workers, temporary workers, and the like.

2) The unemployment rates here refer to the ratio of unemployed persons, who were nonregular workers when they left their jobs within three years before the survey year, to the sum of the regular and nonregular employees at the time.

greater when the companies educate their employees by retraining them in new skills.

The first energy crisis in 1973 impacted very heavily on to the Japanese employment system in the primary sector. The rapid expansion of the economy came to a halt. The economic structure

changed from heavy, resource-eating industries to high-technology, resource-saving ones. Traditional skills became obsolete, while new skills were increasingly needed. Firms found it necessary to secure jobs for their employees by retraining them in new skills.

When the expansion of the primary sectors stopped as a result of changes in the global business environment, firms found that it would, in the short run, be extremely costly to keep redundant employees within their organizations. However, many large Japanese companies made serious efforts to avoid permanent lay-offs, and examined whether they could introduce temporary lay-offs. Their usual method of keeping employees employed was to create empty jobs within their firms or second redundant employees to subsidiary firms. Early retirement plans were also introduced to induce employees to retire voluntarily with an attractive retirement premium, even if it meant that the firms would risk losing good employees. Firms generally maintained the principle of long-term, stable employment until the mid-1980s. Employers anticipated that the Japanese economy would expand under the bubble economy

Independent Variables

Dependent Variables

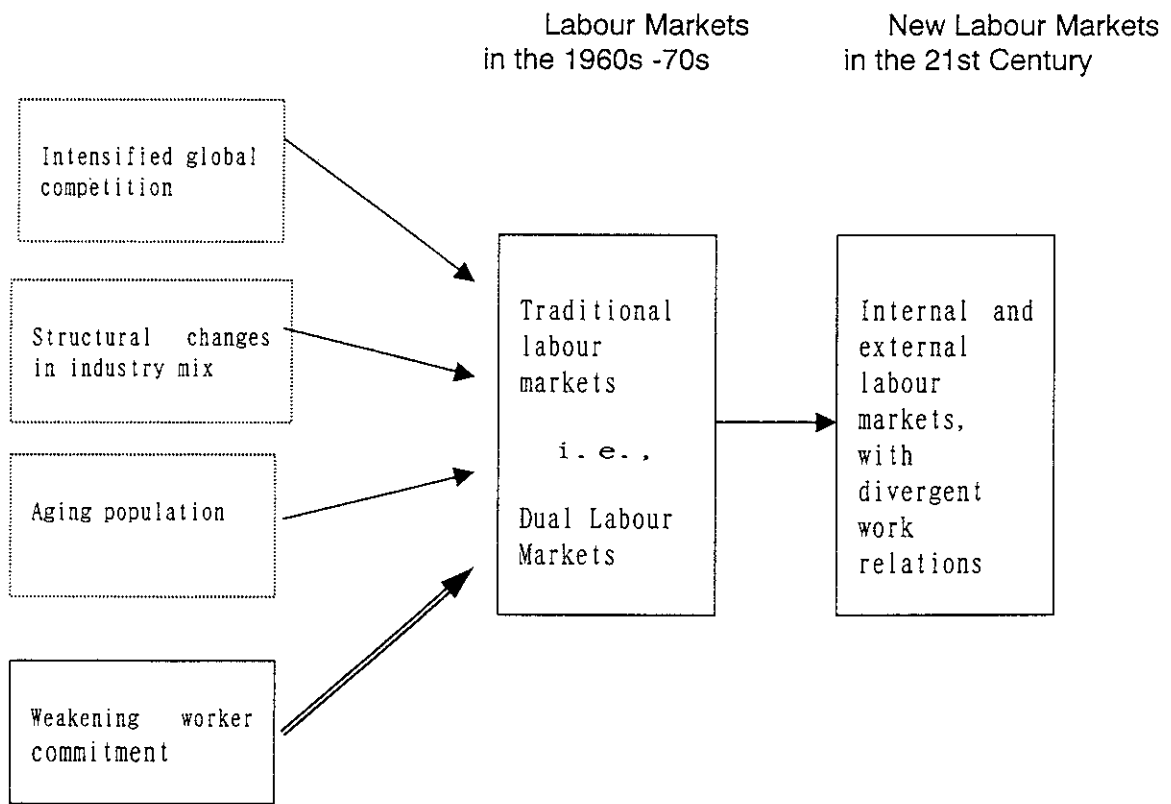


Figure 3. Factors Causing Changes in Labour Market Structure

for the rest of the 1980s and in the 1990s. However, the recession after the crash of the bubble economy has lasted long into the 1990s, thus demanding essential changes in the employment systems.

Factors that are likely to have a profound impact on the working of labour markets in the coming

determination.

First, in general no outstanding changes have been observed so far in employment patterns in Japan. Several years ago the increase in inter-firm job mobility particularly among young workers was pointed out but it is not clearly confirmed yet. This suggests that the once-observed inter-firm job mobility was a temporary phenomenon resulting from younger workers' job-hopping activities and firms' mass employment which were mainly caused by a temporary labour shortage in the period of Japan's *bubble economy* in the late 1980s.<sup>11</sup>

Second, nevertheless, employment patterns in Japan have slowly but steadily shifted in a irreversible way. This is noticed in the fact that attractive job opportunities have been decreasing. This means that a percentage of advantageous regular employees who enjoy "life-time long" employment and seniority-based wage and promotion systems is reduced. See Table 5. It necessarily brings about the expansion of non-regular forms of employment such as part-time workers and dispatched workers. See Table 6.

[Table 5] Decrease in Attractive Job Opportunities

Years	[Thousand;<%>]			
	All Employees	Employees of Big Firms*	Employees of Banks	All Civil Servants
1970	33,400 <100>	3,755 <11.2>	293 <0.9>	4,453 <13.3>
1974	36,380 <100>	3,853 <10.6>	344 <0.9>	4,930 <13.6>
1980	39,970 <100>	3,431 <8.6>	373 <0.9>	5,168 <12.9>
1985	43,280 <100>	3,513 <8.1>	372 <0.9>	4,679 <10.8>
1990	48,820 <100>	3,481 <7.3>	442 <0.9>	4,408 <9.0>
1993	52,130 <100>	3,716 <7.1>	463 <0.9>	4,418 <8.5>

\* Employees of 924 firms listed in the First Section of the Tokyo Stock Exchange.

[Source] The Industrial Relations White Paper 1995, Japan Productivity Centre for Socio-economic Development, Table 10.

[Table 6] Non-Regular Forms of Employment in the Non-Agricultural Sector

Year	[Thousand/<%>]	
	Total Employment	Part-time Employees
1975	36,170	3,530 <9.8>
1980	39,410	3,900 <9.9>
1985	42,850	4,710 <11.0>
1986	43,500	5,030 <11.6>
1987	43,990	5,060 <11.5>
1988	45,070	5,330 <11.8>
1989	46,480	6,020 <13.0>
1990	48,060	7,220 <15.0>
1991	49,720	8,020 <16.1>
1992	50,860	8,680 <17.1>
1993	51,700	9,290 <18.0>

[Source] The Industrial Relations White Paper 1995, Japan Productivity Center For Socio-Economic Development, Table 11.

Third, business managers tend to put more emphasis on job turnover and mid-way recruitment as their employment practices. While the percentage of managers who appreciated "life-time long" employment system was 32% in the 1993 Survey, the percentage drastically reduced to 19% in the 1996 Survey. By contrast, the percentage of managers who never mind life-time long employment practices increased from 15% to 51% in the same period of time.<sup>12</sup>

Fourth, this shift of way of thinking is again shared by the public. Namely, the public tend to consider the "life-time long" employment practices as negative and attitudes toward job turnover as positive. According to the public opinion polls, the percentage of people who thought that the life-time long employment system was good both for firms and workers decreased from 43% to 38% while the percentage of people thinking that it was good neither for firms nor workers dropped from

<sup>11</sup> *The Economic White Paper 1996*, Chapter 3, Section 2

<sup>12</sup> *The Report on the Employment Management Survey 1996*, Table 20, p.25

7% to 11% between the 1987 Survey and the 1995 Survey.<sup>13</sup> Concerning job turnovers, the percentage of people who thought that one had better stay at one firm or place as long as possible dramatically decreased from 52% to 34% while the percentage of people thinking that one might change employers if one is given an opportunity to improve one's own ability increased from 42% to 60% in the same period.<sup>14</sup> These results are also presented in Table 4.

## 2.4 Function of labour unions

First, the number of labour unions has steadily decreased since 1985 in Japan. And the number of labour union membership has been rather stable since 1973 to be just above 12 million. Since the number of employees has been increasing, the ratio of union membership to total employees has reduced from the highest ratio of 56% in 1949 to 24% in 1995.<sup>15</sup> This paper does not intend to analyse why the percentage of unionised workforce has been declining.<sup>16</sup> But a study suggests that a growing share of non-unionised workers does not necessarily lead to less influential position of unions in Japan's labour relations because even non-union enterprises do and have to watch and refer to the wage level and other fringe benefits established in unionised enterprises.<sup>17</sup>

Second, the percentage of the public who responded that his/her enterprise had a union or more remains almost the same from 1989 to 1994 to be around 63-64% according to the individual survey on the labour relations communication. According to it, the ratio of those who responded that their enterprises had no unions and who considered unions positively remains almost the same to be around 50% during the same period.<sup>18</sup>

## 2.5 Resolution systems for individual labour disputes

There are several types of resolution systems for labour disputes in Japan. Perhaps more labour disputes are resolved within firms in Japan than any other countries. But independent resolution systems for labour disputes are also important and are becoming more so than before. Law Courts, Labour Commissions, Watchdogs for Labour Standards, Offices for Female and the Youth Affairs and Prefectural Bureaus for Labour Affairs are considered as independent institutions for labour disputes resolution. Let us summarise the main changes in this area.

First, some shifts in labour disputes are observed through the data collected and compiled by the Ministry of Labour. The following findings are important.

- 1) Total number of labour disputes and the number of disputes both with and without strike actions tend to decline for these ten years. In particular, total number of labour disputes and the number of disputes with strike actions reduced into 20% of the level of ten years ago.
- 2) Participants to disputes with strike actions and work days lost have apparently declined for the last decade.
- 3) The picture may appear little bit different if considering the size of firms. The number of participants to labour disputes and work days lost remained same or slightly increased in 1992-93 in small firms whose employees are less than 100.
- 4) The labour disputes have developed mainly concerning the topic of wages and allowances whose share has about three quarters of all for these three years.
- 5) The performance of resolution systems is fairly good because approximately 90% of disputes have been resolved within a year for the last 6 years. While the share of resolutions by direct negotiations between labour and management has decreased by 20% points, that through the intervention by independent institutions has increased by 5 to 10% points for these years.<sup>19</sup>

Second, the number of civil suits brought into district courts has been increasing since 1990 (764 cases in 1990 to 1,230 cases in 1994). And it is interesting to see that resolutions by voluntary

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<sup>13</sup> *The Public Opinion Poll Monthly* April 1996, Table 6, p.13

<sup>14</sup> *The Public Opinion Poll Monthly* April 1996, Table 26, p.41 and Table 27, pp.43-44

<sup>15</sup> *The Current States of Labour Unions in Japan 1996*, p.25

<sup>16</sup> See Y. Tsuru and J. B. Rebitzer (1995) and T. Muranaka (1996), for instance.

<sup>17</sup> Y. Tsuru (1997)

<sup>18</sup> *The Current States of Industrial Relations Communications in Japan 1990 and 1995*, Table 17 and Table 14 respectively

<sup>19</sup> *The White Paper of Industrial Relations 1995*, pp.160-64 and *The White Paper of Labour Movements 1996*, Appendix, p.102

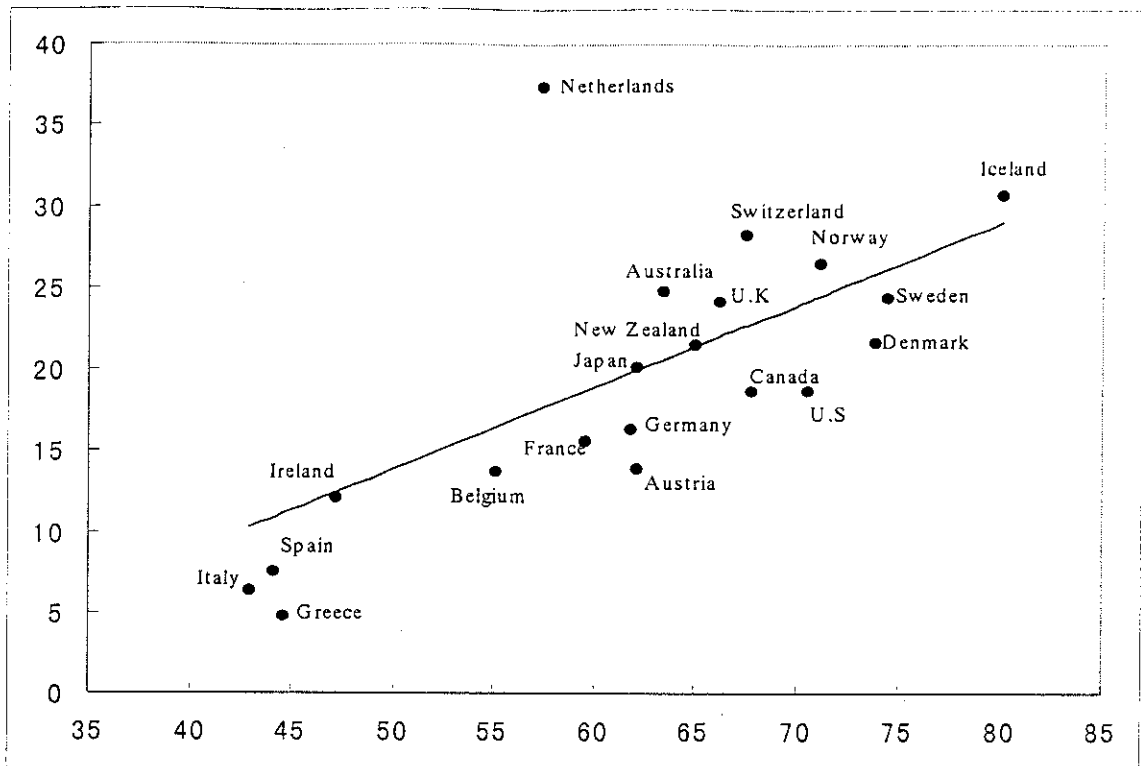


Figure 4. Relationships between Female Labour Force Participation Rates and Part-time Employment, 1994-95 (%)

Note:  $Y=15.65X+0.5657$ ;  $R^2=0.5173$

X: female participation rate (1995), Y: part-time employment as % of total employment (1994)

Source: OECD, *Labour Force Statistics 1975-1995*, Paris; 1997.

It is not only institutional economists who are critical of this neoclassical assumption. Brown (1985), for example, argues that the assumption was unrealistic; it is the families that decide how to provide child-care and meals and that freely switch between the labour market and home production.

Policy targets could be individuals when decisions are made at the level of individuals, as the theory asserts. However, it is better if households are included when it comes to formulating labour market policies. Nowadays, markets provide goods and services that are not readily produced at home, indicating that productive work in labour markets and housework are not interchangeable. Further, wives' decisions to work are not governed primarily by economic efficiency, because the substitution of time for money in housework would not be perfect. Thus, both income and time are needed to sustain family life, and they are not readily interchangeable in the real world. Therefore, policy making in general becomes far more complicated when it aims at household behaviours rather than dealing with individual behaviours.

Policy targets themselves are also becoming diverse. About a quarter of female part-time workers work as part-time workers because they could not find a full-time job. They themselves may feel that they are a secondary labour force, because they would wish to work longer if they could, and also because their current part-time job would probably be unstable, as Wilcock (1957) theorized. Protective policy measures would be in order for them. Still, the remaining three out of four female part-time workers voluntarily choose to be employed under short-term, flexible working arrangements. They are not interested in becoming full-time workers, and switch freely between labour force status and non-labour force status. These women would probably appreciate it very much if a better flow of job market information were made a component of labour market policies.

Even though many female part-time workers choose to remain under a part-time employment contract, their social security measures are inferior to those of full-time employees. Their vocational training

and education opportunities are also limited. There is a need for public policies to support them regarding the issues that part-time workers are unable to achieve on their own.

The majority of large Japanese firms in the primary sector and government offices would try to maintain long-term employment contracts with their employees. Some estimates report that Japanese enterprises have kept approximately 1 to 1.5 million redundant employees in the private sector since the crash of the bubble economy in 1993-94. This figure would keep the unemployment rate figures down by about 1.5-2 percent. Thanks to such generous employers, the unemployment rate has been kept as low as 3.0-3.5 percent until very recently. How long can these generous employers stay competitive?

Shimada (1985) asserted that new job opportunities were found not in traditional industries but in new businesses whose employers were not concerned with the traditional long-term employment practice. Employers in this new growing sector hire and fire workers according to their business needs. This means that the core workforce now includes temporary and part-time workers, for many skilled workers or professionals might prefer a fixed term employment to a permanent one. In July 1986, "Labour Standards on Temporary Workers were introduced. The relaxation of these standards, even now being discussed, would increase unstable job opportunities, although workers themselves might opt for the flexibility in work scheduling. External labour markets in Japan will surely keep on increasing in the 21st century in response to the globalization of the business environment, the growing importance of the service sector in the economy, and the changes in worker commitment to a firm. Labour market policies geared to the traditional primary and secondary sectors would not be sufficient to deal with the new type of work relationships. Strategic perspectives in identifying policy objectives and targets are becoming more important for public policy makers than they used to be.

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# Chapter 5 Industrial Relations and Labour Market Policy in Sweden

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## 1 Characteristics of "the Swedish Model"

Industrial relations in Sweden form a constituent part of the so-called "Swedish model". In order to understand the nature of industrial relations in Sweden one must therefore, in our view, also look at other aspects of the Swedish model which affect the bargaining strength of representatives of workers and the employer at the firm level.

The "Swedish model" has been used by some writers as a concept for describing a distinct type of capitalistic society which combines the efficiency of a capitalistic mode of production with radical, egalitarian redistribution policies and democratic decision making. Such a view of the Swedish society as being especially egalitarian and democratic has, however, been strongly disputed. Moreover, "the Swedish model" is often used in an ambiguous way and the concept has different connotations

Three applications of the Swedish model:

(1) On a macro societal level the Swedish model has been equated with the "Scandinavian" or the "Social Democratic" type of welfare state, claiming to offer a nearby total social security to its citizens.

As van den Berg & Szulkin (1994:162) argues: "Although most of Sweden's welfare policies and social insurance programs can be found in other advanced countries in one form or another, none has implemented a whole system of programs of the comprehensiveness, universality, extent, generosity, and redistributive effect as Sweden has."

The implication for industrial relations at the plant level is that the workers' dependency on the employer for their welfare and social security is decreased since such necessities are provided by the welfare state. In other words, the bargaining strength of the workers tend to be higher in a well-developed welfare state.

(2) The Swedish model has also been used as synonymous to the Rehn-Meidner model (named after the two prominent trade union economists Gösta Rehn and Rudolf Meidner), that is a specific program for economic and labor market policy which will be further discussed below.

(3) On the firm level, the "Swedish model" has been used in connection with workplace democratization, job enrichment and the creation of multi-skilled team work organizations, as exemplified by the famous experiments at Volvo's plants in Kalmar and Uddevalla. The fundamental idea is that new technologies and work organizations should be introduced that simultaneously serve the objectives, on the one hand, of industrial policy in increasing the economic efficiency, competitiveness and productivity of the firms and, on the other hand, objectives that is central for the well-being of the workers, such as employment, skill and a high quality of work. A fundamental requisite for this reform movement has been a low unemployment rate and a relative shortage of labor.

These three applications of the Swedish model, although different, have one thing in common, namely that they can all be conceived as historical consequences of a strong, united and centralized trade union movement which has acted in close cooperation with the a politically hegemonic Social Democratic Party.

The political hegemony of the Social Democrats is based on an almost continuous governmental control from 1932 up to the present. The exceptions are brief spells of "bourgeois" governments during two periods - between 1976 and 1980 and between 1991 and 1994.

Although, as will be discussed below, cooperation with the social democratic party has been put under heavy strain during the 1990's and the trade union movement has been weakened, their strength and unity is still impressive.

Trade union organization rate in Sweden was 84 percent in 1994 which is the highest in the advanced capitalist world. Furthermore, although the union density has fallen sharply in many

countries during the past decade, the number of union members has remained relatively stable in Sweden.

The Swedish trade union movement consists of three dominant national confederations. The largest and most powerful is LO (the National Organization) which organizes blue collar workers, and the second largest is TCO (the Central Organization for Salaried Employees) organizing most white collar workers on low and middle levels. The third major organization is SACO (the Swedish Confederation of Professional Associations) which, sometimes in competition with TCO, organizes professionals with a university degree. Moreover, the Swedish employers are also unusually well-organized in the (at least until the end of the 1980's) highly centralized SAF (the Swedish Employers' Federation).

The Swedish trade union movement is characterized by an all encompassing industry type of organization which is combined with a highly egalitarian ideology among the trade union officials.

Thus, historically the Swedish type of labor market policy regime is founded upon, what has been called "an institutionalized resolution of the conflict between labor and capital", the basic and symbolic event being the famous "Saltsjöbad Agreement" in 1938 between LO and SAF which defined a set of ground rules for conflict resolutions without state intervention. In combination with legislation this "historical compromise" formed the basic institutional context for industrial relations in Sweden. Before 1938 the Swedish labour market was characterized by an unusual high degree of industrial disputes and strikes. After the Saltsjöbad Agreement up to the 1970's Sweden instead became famous for her peaceful industrial relations.

### *The Rehn-Meidner Model*

It was in this context that the Rehn-Meidner program was presented at the LO national congress in 1951. The three corner-stones of their model was "solidarity wage bargaining", an "active labor market policy", and a restrictive fiscal policy. The package was intended to secure rapid economic growth and the strengthening of union solidarity while avoiding both unemployment and inflation. The term "solidarity wage policy" was coined during the 1930's. Its more specific meaning was refined and developed during the 1940's by Rehn and Meidner. By central coordination of wage bargaining between different trade unions, the principle of "equal pay for equal work irrespective of the productivity and profitability of the firm" should be achieved.

With the combination of wage pressures through solidarity wage bargaining and a government policy of strict fiscal restraint, it was foreseen in the Rehn-Meidner program that less efficient firms would gradually be squeezed out of business while the more efficient ones would be encouraged to expand faster than they otherwise would. In the long run, Rehn and Meidner argued, this would lead to rapid industrial restructuring, economic growth, and real wage increases for the workers. In the short run, however, such policies might lead to increased unemployment in certain industries and regions. Therefore, solidarity wage bargaining should be combined with an active labor policy - which included an efficient employment service agency, retraining programs and migration subsidies, and, when needed, the active creation of work - in order to facilitate a fast reallocation of workers made redundant in less efficient industries and firms. It should be emphasized, however, that the Rehn-Meidner program was never intended to supplant the capitalistic economic system, but instead to make it function more efficient and more to the benefit of the working class. In other words, it was a program suited for the aims of a reformistic social democratic government in close cooperation with a strong trade union movement.

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## 2 Changes in Industrial Relations

During the heydays of the Swedish model, between 1956 and 1983, bargaining took place at three levels: First, a central framework agreement between LO and SAF (from the early 1970's central agreements were also made between, on the one hand, the two white collar workers trade union confederations TCO and SACO and, on the other hand, SAF). Second, a number of national industry negotiations and, third, followed by local negotiations at the plant level.

On the central level, relations between SAF and the unions became much more confrontational from the 1970s onward. This is probably the most important reason for the more or less collapse of the centralized system of collective bargaining. The turning point came in 1983 when Verkstadsföreningen (the employers' organization in the engineering industry) succeeded to sidestep LO and formed a separate agreement with the Metal Workers' Union. The wage negotiations after 1983 have primarily involved industry-level and not national bargaining. The exceptions being three national central frame agreements during the second half of the 1980's. Furthermore, between 1991 and 1993 a government-promoted voluntary income policy agreement was struck in conjunction with a sharp disinflation policy. Thus, more and more often the government has had to participate in order to keep central bargaining alive, and more and more these efforts have failed. This tendency toward decentralization has clearly reduced the effectiveness of LO's "solidarity wage policy".

Although the Swedish labor market traditionally has been characterized by centralized bargaining, the local trade union also has been a strong force at the firm level which also goes for the electrical industry. Well aware of the bargaining strength of the unions, most employers established a cooperative relation with the local unions. Even though, as mentioned, industrial relations on a central level have been much more confrontational since the 1970's, the spirit of cooperation often seems to have remained stronger at the local level.

Berggren's (1986) conclusion on the basis of a national survey of local union officials and employers was that the corporatist spirit was highly developed. A large majority of employers regarded the local union as a "partner" and as a helping hand when implementing organizational and technological changes. This conclusion is supported by the Swedish Organizational Survey of 1991, according to which as much as 72% of 488 plant managers in the manufacturing industry answered that the participation of the local union in decision making leads to better decisions for the organization, while only 2.3 percent said that it leads to worse decisions. Furthermore, 89 percent of the plant managers thought that the relationship between the local unions and management was characterized by cooperation.

The Metal Workers' Union has been particularly active in the job enrichment movement since the beginning of the 1970's. Van den Berg et al (1996: chapter 6) argues on the basis of case studies in plants conducted in 1991 and 1992 that the local union was a "driving force" behind technical and organizational changes in the telecommunication industry. According to these authors, the metal workers' union was sometimes more energetic in pursuing change than was the management of the plant. Furthermore, they argue that the union clearly was more supportive of change than many of the rank-and-file workers. The white collar union, however, tended to be more resistant to technical and organizational changes since it often encroached on traditional white collar prerogatives.

In a way which van den Berg et al (1996) conceive as a "top-down 'neocorporatist' arrangement", organizational changes which were pushed for by local union representatives had been inspired by the central Metal Workers' Union through regular conferences, study circles, literature, and so on (van den Berg et al 1996:30). This is in line with the declared policy of the Metal Workers' Union to create reformed work organizations in combination with new technology which have the purpose to implement job enlargement and job enrichment for the members (for a policy declaration, see the congress report of the Metal Workers' Union of 1985).

Although there are many arguments in favor of a policy of active participation in company rationalization by the union, it is not without problems if it leads to a reduction in the need for manpower. The upgrading of the blue collar workers' work in the manufacturing industry in recent years is associated with a dramatic loss of jobs. Thus, in spite of the tremendous expansion in for example the electrical industry since the beginning of the 1980's the number of jobs has decreased.