

Rethinking the Research of Kao through the Review of MNC Theory by pre-1990

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Rethinking the Research of Kao through the Review of MNC Theory by pre-1990

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1 . Brief Review of MNC theory

1.1 The emerge of FDI and MNC Theory

Basing on theory history review, Jones (2005) suggests that there are two waves of globalization since late nineteenth century; the first globalization wave was formatted during the period of 1880- 1929 through imperial power, but this wave started to retrogress in 1930 for the worldwide economic depression. The second wave emerged in 1950s, the post war era, for the economic recovery and the development of international currency, trade and investment; and it become matured after 1979. Jones and Dunning (1993) agree that before the 1950s the theories of international trade introduced by economists, such as John Williams (1929) or Bertli Ohlin (1933), obtained the fundamental frameworks and provided explanations of state and company's international economic activities. And the research of multinational corporation / company (MNC) had not appeared until the year of 1960 when D. E. Lilienthal, the ex- CEO of TAV, defined the concept of formally. After the first definition of MNC come out, the MNC researches grew and become another critical theory in international business discipline since 1960s.

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In middle 1960s, the product-cycle model was introduced by Vernon (1966) to explain why company goes out and conducts international business. This model basically adopted the data of international trade, and only focused on the patterns of goods flow. Although Vernon’s research has played an important role in international business theory, however, it is agreed that the first MNC research was presented by Hymer (1960, 1976) which explained why company conducts FDI approach instead of international trade or licensing to extend the territory of business, and also propounded the initial concepts of internalization and transaction cost (Pitelis 2006). Moreover, in Hymer’s research, the types of advantages owned by parent company are also introduced to describe why and how parent company can compete with local companies through FDI (Hymer 1960/ 1976, Cave 1971). In brief, according to the theory history, we can see that the concept of MNC emerged formally in 1960s and the related issues are discussed and confirmed in 1970s.

Figure 1: The Theory Map during 1930s-1980s

Period	1930-1950s	1960s-1970s	1980s
Main Issues	International Trade	FDI/ Advantages of Parent Company	Typology: Structure and Organization
Main Researches	Williams (1929) Ohlin (1933)	Hymer (1960/1976) Vernon (1966) Cave (1971) Internalization: Williamson (1975) Buckley and Casson (1976)	Rugman (1981) Levitt (1983) Hedlund (1986) Porter (1986) Prahalad and Doz (1987) Dunning (1988), Bartlett and Ghoshal (1989)
Technology transfer Issue		⇒ knowledge flow within network	
Supplier chain system Issue		⇒ value chain system	

Edited by Tung

Since the 1980s, because of the advancement of transportation and communication technology, the liberalization of the international financial system, and the platform construction of international political and economic organizations, the global society had been formatted more deeply. Thus, scholars, such as Rugman (1981), Levitt (1983, 1990), Hedlund (1986), Porter (1986), Prahalad and Doz (1987), Ghoshal (1987), Dunning (1988), Nohria and Ghoshal (1989), and Bartlett and Ghoshal (1989) began to investigate the content and patterns of new environment and challenges brought by global economy, and classified the types of the adaptation and changes of the organizations and strategies of MNCs. Thus, we can say that the MNC theories become matured in 1980s, and in western, it take about 20-30 years to nurture MNC theories.(see Figure 1).

1.2 The positioning of the research of Bartlett and Ghoshal (1989)

Among the researches in 1980s, the research of Bartlett and Ghoshal not only has great influence on the conception formation of organization and strategy analysis toward MNCs, but also keeps re-print and provide the basic frameworks for students to understand the MNC world in these days. That is because that their work well summarized the fundamental frameworks of MNC theories emerged in 1980s and propounded several integrated frameworks to suggest a new solution, transnational company (TNC), for companies to compete in new age.

In early 1990s, the other important theories come out, such as Dinning (1993) which integrated the FDI strategy related theories and suggested “Eclectic Framework-OIL”, or Porter (1990) that indicated the strategic relationship between industrial development and government policy, however those theories have not affected the confirmed status of Bartlett and Ghoshal (1989) in international business and MNC discipline. Therefore, we can position their research as a key research that open more matured research viewpoints for MNC theories as well as influence not only academic but also business area since 1990s.

Even so, the framework of Bartlett and Ghoshal still has some problems in analyzing of Japanese company, and that can be related to the shortages of information and methodology. Thus, the following content will introduce their framework in detail and take the research of Kao for example to point out the problems related to the Kao analysis.

2 . The Framework of Bartlett and Ghoshal¹⁾ (1989)

2.1 Types of MNC organizations

Bartlett & Ghoshal developed a classification framework in dimensions of *dominant strategic requirements of industry* and *dominant strategic capability of company*, and compared three industries with nine companies, including Unilever, Kao, P&G, Philips, Matsushita, GE, ITT, NEC, and Ericsson. By doing so, three MNC types, *multinational company*, *global company* and *international company*, are introduced. (Figure 2); and among nine companies, Unilever, Matsushita and Ericsson (marked in gray) that the dominant strategic capabilities they carried are considered correspond to the dominant strategic requirements of industries, are taken as the successful samples for the industry they belong to. To make the concept of the framework, this paper takes branded packaged industry (marked in **bold**) for example to describe and analyze in detailed.

1) In this section, the specific terms which Bartlett and Ghoshal used are written in *italic*.

In this framework, Unilever of branded packaged industry was defined as a *multinational company*, which developed a strategic posture and organizational capability that allows the company to manage a portfolio of multinational entities and respond to national difference. And Kao was considered a *global company*, which builds cost advantages through centralized global-scaled operations. From the viewpoint of independence and the autonomy of national units, the structure of P&G, an *international company*, is between Unilever (*multinational company*) and Kao (*global company*), which transfers and adapts knowledge or expertise of the parent company to foreign markets, but still retains considerable influence and control in the headquarters.

Figure 2: Industry Requirements and Company Capabilities

<u>Dominant Strategic Requirements of Industry</u>			
Responsiveness (Branded Packaged Products)	Unilever	Kao	Procter & Gamble
Efficiency (Consumer Electronics)	Philips	Matsushita	General Electric
Transfer of Knowledge (Telecommunications Switching)	ITT	NEC	Ericsson
	Responsiveness (Multinational)	Efficiency(Global)	Transfer of Knowledge and Competencies (International)

Dominant Strategic Capability of Company

Source: Bartlett and Ghoshal, 1989, pp21.

Bartlett and Ghoshal note in the case of the branded packaged industry, the capability of *national responsiveness* is important. Unilever is the most able to fit between dominant strategic requirements of the business and the firm's dominant strategic capability. This kind of company is considered to have the ability and flexibility to assist national units adapting to local demands rapidly. However, when diversification of product and region difference became complex, the organization also grew huge and faced problems of enormity and inertia. In this situation, even though *multinational company* can provide rapid responsiveness, it still has to resolve the problems come from inefficient multinational R&D and production operations to prevent the company's loss of competitiveness. In Particular, by the mid-1980s, the force of global integration, local differentiation, and world-wide innovation had become strong and compelling. In order to compete effectively, a company is forced to develop global competitiveness, multinational flexibility, and worldwide learning capability simultaneously. To build these multiple strategic competencies, companies primarily faced an organizational challenge.

According to Bartlett & Ghoshal, Kao, defined as a sample of loser in branded packaged industry, despite it has a highly efficient centralized production system and a sophisticated process technology. Kao owns an extremely strong position in Japanese market, and has been gradually expanded through an extensive overseas licensing program, however by the late 1980' Kao was still not a significant global player. At this point, Bartlett & Ghoshal considered the fundamental problem of Kao was not inappropriate products or marketing strategies, but its inability to understand the differences between markets and adapt appropriately, in their words, Kao lacks *national responsiveness*.

Their concept of *national responsiveness* is related to the comments on Levitt's argument, and can be used to prove that ignoring national responsiveness, taking global market as a single and universal market, cannot lead to success in the global era. Levitt (1983, 1990) asserts that under the influence of globalization, the world market tends to become flat and standardized, so that to provide high quality and low price products, the MNE/MNC model²⁾ is not applicable anymore, instead the global enterprise model³⁾ will play an important role in the global era. On the other hand, Bartlett & Ghoshal argue that the classic barrier to globalization is always rooted in the differences of national market structures and consumer preferences. International travel and communications might help reduce those differences, but worldwide tastes, habits, and preferences still exist. The demand from different nations is called *national responsiveness* by Bartlett & Ghoshal, and it influences the smooth entrance of market consumer goods.

2.2 The new solution: transnational model

Basing on the above framework, Bartlett and Ghoshal address a transnational model in the concept of *transnational mentality* for companies to adapt to new globalization challenges.

The *transnational mentality* can be described in three key organizational characteristics: (1) configuration of assets and activities are dispersed, interdependent, and specialized; (2) the allocation of organizational roles and responsibilities are differentiated contributions by national units; and (3) the facilitation of multinational learning processes is developed jointly and shared worldwide. In addition, they also propounded three corresponding management tasks for organizing a trans-national organization: (a) legitimizing diverse perspectives and capabilities, (b) developing multiple and flexible coordination processes, (c) building shared vision and individual

2) MNE/MNC model was defined as operate business in several nations to fit local demand, so that their cost is also relatively high. (Levitt, 1990:431)

3) Global enterprise model was defined as one takes global market as a single market and conduct business activities in integrated way. (Levitt, 1990:431)

commitment. (Table 1)

Table 1: Building and Managing the Transnational

Strategic Capability	Organizational Characteristics	Management Tasks
Global competitiveness	Dispersed and interdependent assets and resources	Legitimizing diverse perspectives and capabilities
Multinational Flexibility	Differentiated and specialized subsidiary roles	Developing multiple and flexible coordination processes
Worldwide learning	Joint development and worldwide sharing of knowledge	Building shared vision and individual commitment

Source: Bartlett and Ghoshal 1989; re-edited by Tung

2.3 Contribution and problems of Bartlett and Ghoshal’s framework

So far, the research of Bartlett & Ghoshal summarized the main research results of 1980s, based on those they also provided integrated frameworks to analyze global scale organizations; moreover, their research is also significant as it concerns the characteristics of different industries and is the first in depth comparison of American, European, and Japanese famous companies. In addition, the management tasks and processes of transnational mentality are also good references for constructing a strategic global scale organization; furthermore, the comments on Kao, P&G and Unilever seem being in effect at present.

However, returning to Kao’s case, according to Bartlett & Ghoshal, the main problem for Kao is its inability to offer better responsiveness to overseas markets and persuade efficiency of operation simultaneously. But this statement implies a misunderstanding of Kao’s basic information, and the adequacy of comparison and evaluation of these three companies also needs to be reconsidered. For example, they define Kao as a *global company* without propounding the detailed explanation of its structure and its relationship with overseas subsidiaries. To examine their evaluation toward Kao, this paper adopts historical analysis methods to approve the following hypotheses.

- H1: Pre-1990 is not a proper era to evaluate the performance of Japanese MNCs
- H2: Kao constructed an initial MNC organization by 1990 to assist the R&D capability and composition of product portfolio to compete with rival in Japan market.
- H3: Kao is not a global company that defined by Levitt (1990) for they conduct very few export business.
- H4: Kao, P&G and Unilever have their own types of organizations that fit to the environment

they face and the strategies they adopt. It is dangerous to compare with these companies and evaluate them which one is the loser or winner.

By providing the historical data in pre-1990, this paper would like to rethink the Kao research of Bartlett and Ghoshal, to claim that it is necessary to evaluate companies through all kinds of methods, layers and aspects while doing MNC comparison research.

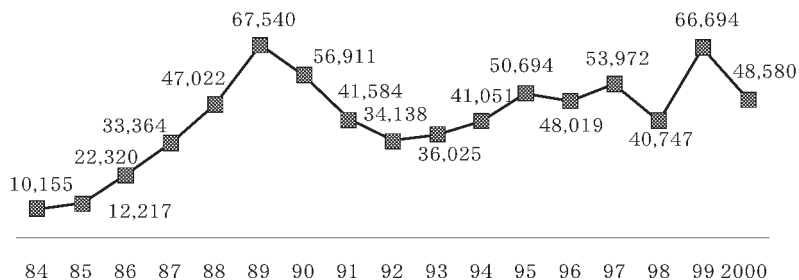
3 . The overseas business of Kao in 1980s

3.1 General information: The outward FDI of Japan

According to Hymer (1976), MNC can be seen as the result of FDI. In western region, the FDI activities become a critical approach for international business in 1950s. However, in Japan, general speaking, after World War II only few industries conducted outward FDI and the dramatic growth of outward FDI emerged in 1985, grew in the period of 1985-1988, and reached the peak in 1989 (Figure 3). Compare with western countries that started to conduct active FDI in 1950s, the FDI activity of Japan is at least 25 years later. Therefore, the better observation period of Japanese MECs should be

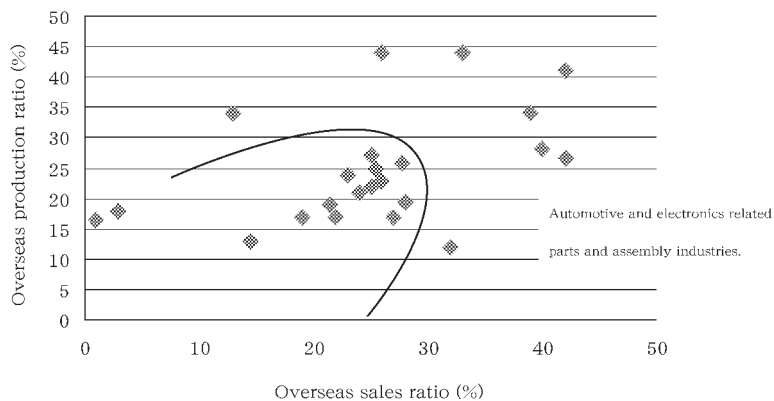
Not only started late, the FDI activity of Japan is also not common in all industries. Until early 21 century, most industries, except automotive and electronics related industries, of Japan operated low ratio of overseas sales and productions (Figure 4). It is said that to catch up with sophisticated western companies, the industries of automotive, steel, electronics, computer, and semiconductor had been protected by Japanese government during initial development period to compete in international (Tsuruta and Ito, 2001 pp.157)

Figure 3: Outward FDI of Japan from 1984-2000 (in million Yen)



Source: Data from Ministry of Finance Japan

Figure 4: The Overseas activities of Japanese Industries (2002 data)



Source: *Journal of Research Institute for Development and Finance* 2004. Fed. p15. Re-edited by Tung.

3.2 The FDI activities of Kao

In 1970s, the Japanese market kept growing firstly after World War II, so P&G started to entrance Japan market during this period. To compete with strong rivals and maintain market shares, Kao started to contract technology alliance through FDI, and this become the main strategies of Kao’s outward FDI since 1970s. On the other hand, Kao kept taking care of Asia markets that started by trade in 1950s and altered to joint ventures since late 1960s (Tung 2010), and tried to find any chance to entrance western markets.

According to the subsidiaries composition, we can see that during early 1980s, Kao had not conducted a global sales operation through FDI, especially in western regions (Table 2). Therefore, basing on the development history of Kao, the period of 1980s is the construction of R&D capability and the initial period for global business. In this content, the structure and strategy of Kao was not ready for global competition in 1980s, so it is not appropriate to evaluate Kao’s “global management” under this period.

4 . The Problems of Comparison of Kao, P&G and Unilever

Kao, P&G, and Unilever are companies set up in late 19 century, so all have long histories and have generated lots of strategies and structural wisdom to adapt to new environments through time. Usually they are viewed as competitors for originally they started business based on oil chemistry, and were mainly dependant on the income from soap in the initial period. As opposed from Kao, during the same time, P&G and Unilever also produced candles and margarine as part of their business. Although both these products faced the problem of demand decreasing through

Table 2: The Composition of Subsidiaries and Affiliated companies of Kao in 1985

Type	Region		Function				
			R&D	Raw Material	Sales	Manufacturing	Logistics
Subsidiaries (18)	Japan	8	2		3	3	
	Asia	7		1	6		
	Europe	2	1		1		
	America	1			1		
Affiliated (21)	Japan	17			10/2*	3**	2
	Asia	2			2		
	Europe	0					
	America	2***	○		○	○	

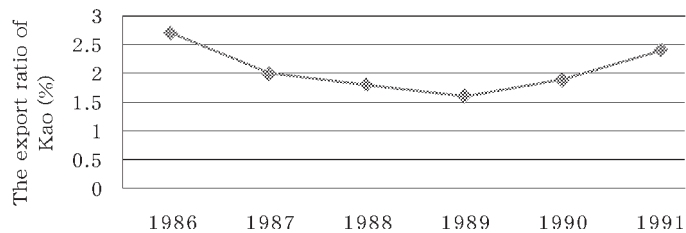
Source: Kao's Annual Report of 1985

* Ten are Japanese Hansha and the other two companies are sales strategic alliance companies that set up in Japan to sell NIVEA products and Colgate's toothbrush in Japan.

** These are industrial chemical manufacturing companies, also technology strategic alliance companies.

*** Set up in Mexico to manufacture and sell products, also a kind of technology strategic alliance.

Figure 5: The Export Ratio of Kao from 1986-1991



Source: Kao's Annual Report of 1987-1991

time, they established their own competence to solve the problem, like P&G empower the research capability, while Unilever build up the foundation of food related business. It is here that the core difference of three companies lies.

4.1 The different composition structure of business

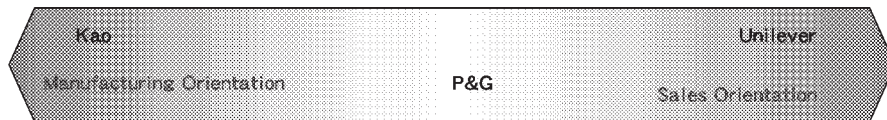
In the composition structure of business, Kao, P&G, and Unilever are different company, although Bartlett & Ghoshal classify them as companies belongs to industries of branded packaged products. Kao is the company that mainly conducts all categories of chemical and cosmetics related business, but only 82% (excludes Gillette and foods business) of P&G's sales and 46% (excludes foods) of Unilever are related to the chemical and cosmetics area. Besides, P&G and Unilever focus on manufacturing consumer products, but on the other hand, the industrial

chemical business unit is also the main business of Kao. These differences define the strategy and structure of three companies.

4.2 The different positioning of strategy and structure

Because of the difference in business, the positioning of strategy and structure are different. Briefly speaking, the positioning of Unilever is close to whole seller which stresses the sales power and constructs the strong partnership with global retailers, such as Carrefour, Tesco, and Wal-Mart. On the other hand, Kao positions itself as a manufacturer with dependent research and development capability, so over sixty percents of staff in the parent company are researchers. And P&G is trying to find the balance between manufacturing orientation and sales orientation, thus it creates a complex but holistic strategy centered in their top layer of organizations.

Figure 6: The Positioning of Kao, P&G and Unilever



4.3 Re-evaluation of the three companies

In the volume of assets and net sales, as well as the margin of Kao are much lower than P&G and Unilever, but if evaluates Kao with its own positioning, the result is reversed. Here, as Kao is the company that focuses on chemical and cosmetic manufacturing, to measure how much sales and profits it generates from the manufacturing process, the ratio of net sales and net profits of assets are calculated. The result shows that Kao is successful under its strategy and structure positioning. (Table 3 and 4, Figure 7 and 8)

We can see that different comparison data will cause the different evaluation and result come out, thus how to choose an appropriate comparison method is important, and that is also the key mission for future study.

Table 3: The Comparison in Net Profit (2007)

	Kao	P&G	Unilever
Margin	7.3%	12.7%	12.7%
(Net Profit/ Asset)*100%	9.37%	6.29%	6.46%

Figure 7: The Comparison of ROA

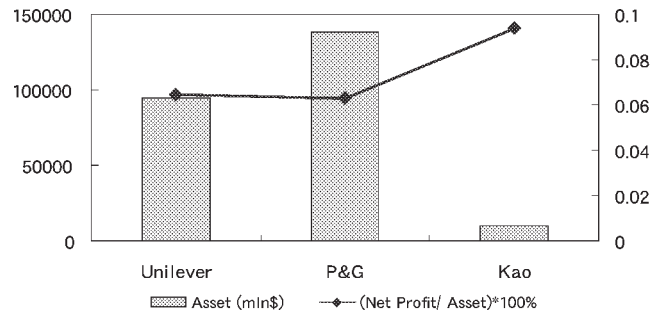
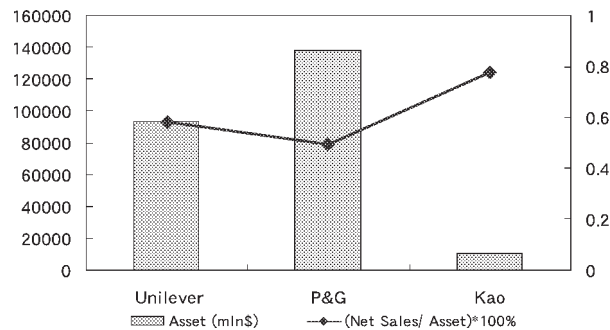


Table 4: The Comparison in Net Sales (2007)

	Kao	P&G	Unilever
Net Sales	8,231	68,222	54,706
(Net Sales/ Asset)*100%	77.87%	49.43%	58.37%

Figure 8: The Comparison in (net sales/ asset)*100%



5 . Conclusion

This paper is basing on the data of pre-1990 for two reasons, one is that Bartlett & Ghoshal used data during the late 1980's and therefore in order to re-examine their research this paper does not adopt the materials after 1990. Secondly, before 1990, Kao was managed under ex- CEO Maruda. After 1990, he handed the right to Mr. Tokiwa, so the year 1990 can be seen as a turning point for Kao.

The ratio of overseas sales shows that Kao is unlike P&G and Unilever which have more income from overseas markets; and Bartlett & Ghoshal contributes this to the insufficiency of

capabilities in localization. However, according to above analysis and Tung (2008, 2010), by pre-1990, Kao had not started to establish global sales networks; instead it focused on technology catch-up to against the intensive competition from rivals and to maintain the Japanese market shares. Moreover, the main problem of weak overseas business might not because the problem of localization, but conversely, is because Kao spends too much effort developing and adjusting products to suit the local markets and graphic environments. However, at present, the environment become more complicated for after 1990s, the strategic partnership with global large scale retailers has become critical, and the shortage in constructing a more competitive manufacture-sales alliance is the main reason for the weak overseas business of Kao and other branded packaged companies.

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