

Scandals expose flaws at Japan Inc

Quality control issues, outdated business models see firms struggle to keep up with overseas rivals

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Kobe Steel is one of the many Japanese companies involved in a string of industrial scandals in a nation deemed as a byword for high quality and probity. The scandals betray the weak corporate governance standards at these firms.

Japan's third-largest steelmaker, Kobe Steel, tarnished its reputation due to widespread cheating on product specifications.

Four individuals in Canada, who bought metal products manufactured by Kobe Steel and cars that use the products, have sued the Japanese company. The class-action lawsuits filed in Canadian courts are the first legal actions against the company since it announced the falsifications in October.

Kobe Steel is also being investigated by the United States Department of Justice. Some of its customers have said they plan to recoup costs for making checks and replacing parts that did not meet specifications.

Japanese industrial standards certifications have been suspended or revoked at some plants of Kobe Steel. The company's Shinko Metal Products unit, for example, has had its Japanese industrial standards certifications revoked for its copper and copper alloy seamless pipes because of quality management issues.

The steelmaker has admitted to falsifying data for its products and specifications — including aluminum, copper, steel powder, liquid crystal display materials and special steel products — which were supplied to manufacturers of cars, planes, trains and other products across the world.

More than 500 of Kobe Steel's customers have received products with falsified specifications on strength and durability.

However, no safety issues have been identified so far. Kobe Steel said on Dec 8 that no products required recall.

But the ISO 9001 quality certification from the International Standards Organization has been suspended or canceled at seven plants of Kobe Steel and group companies.

A number of other companies were also caught up in scandals that

tarnished Japan's national brand. Precision electronics maker Olympus was involved in a \$1.7 billion accounting scandal in 2011.

Auto parts company Takata's deadly air bags prompted US congressional hearings in June 2015. The company had to recall its defective air bags in more than 34 million vehicles in the US and millions more worldwide.

Consumer electronics maker Toshiba was involved in creative bookkeeping, it was revealed in July 2015. Yet another electronics company, Sharp, hid contingent liabilities which came to light during merger talks with Taiwan-based Foxconn in February 2016.

In October, both Nissan and Subaru said they used unauthorized quality inspectors.

Mitsubishi Materials Corp, a major nonferrous metal manufacturer, said in November its subsidiaries supplied products with falsified quality data to more than 270 companies. The products were widely used as components of aircraft, automobiles, nuclear power plants and others.

A subsidiary of Toray Industries, a major textile maker, had shipped tire-reinforcement cord and other products with falsified strength test results to 13 clients — including Bridgestone and Yokohama Rubber — from 2008 to 2016.

Confidence at risk

Sadayuki Sakakibara, chairman of the Japan Business Federation, or Keidanren, the country's most influential corporate lobby group, called the data-falsification problem "a serious situation that could adversely affect confidence in Japanese corporations". He added that the lobby group would call on its roughly 1,360 member companies to do in-house checks on governance issues.

The widespread scandals betray the fact that Japan's top executives at those companies leave quality control entirely in the hands of personnel at production sites.

"Japan's manufacturing culture has been built on the advantage provided through the high moral standards of workers at production sites," the *Yomiuri Shimbun* said. "It is important for the industrial sector as a whole to reexamine how corpo-



Hiroya Kawasaki (right), CEO of Kobe Steel, bows during a news conference in Tokyo on Oct 26. Kobe Steel is just one of the Japanese companies involved in industrial scandals in a nation long considered a byword for high quality.

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rations should be governed."

Atsushi Osanai, a professor at the business school of the Tokyo-based Waseda University, attributed overconfidence in technology and the arrogance associated with it to the misconduct issues in Japan's manufacturing industry.

Personnel believe it is fine to slack off a little because the quality of Japanese products is high, said Osanai, who worked at Sony Corp for 10 years before joining Waseda University.

Still, the business models in place at Japan's automakers and electronics firms, Osanai added, have "yet to be converted to match the changing times", such as China's ascent.

Japanese automakers and electronics firms could increase profits by sharpening their manufacturing prowess, the professor said. Now technology alone cannot guarantee Japanese firms an upper hand over Chinese and other foreign firms.

Takashi Sugimoto, a writer with the *Nikkei Shimbun*, said Japanese companies' factory floors have been caught out by a series of irregularities. Japanese companies' models work along these lines, Sugimoto noted: Employees with a good command of factory floors often brainstorm how to achieve technological perfection. These efforts have pushed Japan's manufacturing industry, step by step, to the top of the world.

Now weak links have been found on the factory floors, such as the unauthorized quality inspectors in Nissan. The scandals would deal heavy blows to the capabilities of the

production sites that the Japanese manufacturing sector is proud of, Sugimoto said.

Mo Bangfu, a Tokyo-based analyst, said Japanese companies are struggling to stay in the same league as their high-quality rivals in advanced countries. And China is not too far behind Japan as the quality of made-in-China products continues to improve.

Japan faces the worst labor shortage in more than 40 years. The country's shrinking pool of workers has helped push the number of jobs for every applicant to a ratio of 1.55 in October, the highest since 1973, according to Japan's Ministry of Health, Labour and Welfare. Robots in Japan are stepping in to fill job vacancies.

Survival plans

To maintain round-the-clock operations, a big draw at its stores, Japan's leading convenience store operator Lawson said on Dec 4 that it will introduce unmanned check-out counters at some Tokyo outlets next spring to cope with a labor shortage that threatens its survival.

But there is bad news for Japan as it seeks the talent it needs to compete in the global economy with an aging, shrinking population.

Japan ranks last among 11 Asian nations in its appeal to highly skilled foreigners — behind countries including Indonesia, Thailand and Malaysia — according to the *IMD World Talent Ranking 2017* report released on Nov 20. Worldwide, Japan was

ranked 51st among 63 nations. Singapore ranked first in Asia.

The results published by IMD, a leading global business school, raise questions about Japan's ability to sustain the technological development it needs to cope with a shrinking workforce, said Jose Caballero, senior economist at the IMD World Competitiveness Center. Japan must do more to establish an effective flow of talent in the future, he said.

Recognizing the need to attract outside talent, Japanese Prime Minister Shinzo Abe's government has opened the doors to highly skilled foreigners. To people who meet its strict criteria, the country now offers what it claims is the world's fastest path to permanent residency.

IMD's digital competitiveness rankings illustrate the challenge Japan faces as it seeks to compete with the likes of China and the US in the era of the "fourth industrial revolution".

While Japan ranked 27th globally in overall digital competitiveness, according to results IMD released earlier this year, it ranked near the bottom in the use of big data and analytics in business decision-making.

It could get worse for Japan. The country faces a growing shortage of workers in "frontier IT" — big data, artificial intelligence and the Internet of Things — expected to reach about 48,000 by 2020, and a shortfall of nearly 200,000 information security workers, Japan's Ministry of Economy, Trade and Industry said in a report last year.