



# Master's Thesis

Title of the Master's Thesis

## Market Entry to Japan

The Ideal Entry Mode for a German Consulting Firm from an  
Institutional, a Cultural and a Trust-Based View

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## List of Abbreviations

B2B	Business to Business
BOJ	Bank of Japan
DPJ	Democratic Party of Japan
EU	European Union
FDI	Foreign Direct Investment
GDP	Gross Domestic Product
GLOBE	Global Leadership and Organizational Behavior Effectiveness
JETRO	Japanese External Trade Organization
IFDI	Inward Foreign Direct Investment
Inc.	Incorporated
JFTC	Japan Fair Trade Commission
JV	Joint Venture
LDP	Liberal Democratic Party (of Japan)
LLP	Limited Liability Partnership
Ltd.	Limited
M&A	Mergers and Acquisitions
METI	Ministry of Economy, Trade and Industry
MITI	Ministry of International Trade and Industry
MNC	Multinational Corporation
MOFA	Ministry of Foreign Affairs
n/a	Not Available
OECD	Organization for Economic Cooperation and Development
p.	Page
para.	Paragraph
R&D	Research and Development
RFB	Reconstruction Finance Bank
SCAP	Supreme Commander of the Allied Forces
S.p.A.	Società Per Azioni (Italian: shared company)
UK	United Kingdom
US	United States (of America)

WOS

WW I/II

Wholly Owned Subsidiary

World War I/II

## 1. Introduction

In the course of globalization and markets growing together, market entry becomes a more and more important topic for firms all around the world. Geographical distance loses importance in economic exchange. Multinational corporations (MNC) expand to various markets to increase their customer volume or gain access to low-cost resources. While in the past mainly manufacturing and tangible products selling firms expanded throughout the world, in recent years a shift towards service oriented companies entering foreign markets has begun (Ekeledo and Sivakumar, 2004, p. 69). Following this trend, this thesis will examine which entry mode a German consulting firm should choose in order to enter the Japanese market.

Japan has been and is still today an interesting market. Although, Japan is currently hit by another period of stagnating growth (The World Bank Group, 2015), the Japanese economy is still working on a high level. The most important element is the high price level Japan manages to maintain (METI, 2014). Especially in the service sector, Japanese pricing rewards high quality with comparably high rates (Pascha, 2010, p. 133; Haghirian, 2010, p. 3). Additionally, companies in Japan face a “low risk of payment” (Haghirian, 2010, p. 56) and benefit from a “reliable infrastructure and legal system” (Haghirian, 2010, p. 57). In the past, comparably few firms have entered Japan. Inward foreign direct investment (IFDI) has been low (Dunning and Lundan, 1997, p. 197) albeit various deregulations on an institutional level since the 1970’s (Ito and Fukao, 2001, p. 10; Lawrence, 1993, p. 94). This development leads to the assumption that other intangible barriers remain strong and efforts towards reducing these barriers are needed.

In recent years, Japan faces a demographic crisis. The strongly aging population will soon develop into a serious deficit of skilled workers (Coleman and Rowthorn, 2011, p. 228). Japan’s demand for foreign workforce increases. IFDI can function as a contributor to solving this crisis (Blomstroem et al., 2000, p. 6) In order to shape a more attractive work environment for foreign employees Japan’s organizations may have to undergo drastic restructuring. A foreign consulting firm with experience from its home country can help other companies develop an organizational structure which compromises the traditional Japanese and the modern globalizing components. Concurrently, the firm can provide support to future market entrants from its home country. Thus, the customer volume for consulting firms in Japan is high (METI, 2014; Morschett et al., 2010, p. 62). Lastly, Japan is an appealing

market for a consulting firm since the government tries to attract market entrants in general by providing support to foreign newcomers and lowering hindrances. In 2003 Prime Minister Junichiro Koizumi introduced the campaign “Invest Japan” which includes a council implementing incentives for potential foreign market entrants (Haghirian, 2010, p. 56). In addition, the Japan External Trade Organization (JETRO) provides extensive statistics about various markets, offers legal support and free office facilities for the entrant to use during the entering period, and introduces them to possible cooperation partners. In summary, Japan is an interesting market for a consulting firm to enter.

In the past, many academics researched the market entry to Japan originating in the US. However, during the past ten years Europe has surpassed the US, and also the whole of North America, as biggest investor to Japan (JETRO, 2015a). Hence, this paper takes a closer look at Europe. Within this continent, I decided to focus on Germany. During the 1990s, Germany counted as one of the strongest investors to Japan, yet during the last ten years, the country fell far behind the Netherlands and France (JETRO, 2015a), although Germany is known to be one of the strongest economies in Europe. It is therefore interesting to estimate the obstacles a German firm faces entering Japan. Finding a solution to overcome those could help the exporting nation to extend their investments and become once again one of the main players in Japan.

The main questions addressed in this paper are: Which would theoretically be the optimal market entry mode for this entry? Which factors influence the choice of mode? Which attributes of the Japanese market and the business culture need to be considered? Morschett et al. (2010) have found “cultural distance, market attractiveness, uncertainty of the host country environment, legal environment in the host country, competitive situation in the host country, and culture of the home country” (p. 61) have been considered of highest importance when deciding on a market entry mode. This thesis will focus on three influencing factors: institutional differences, cultural distance, and a trust-based perspective. The first includes the uncertainty and the legal environment in the host country, the second the cultural distance as well as the culture of the home country. Hence, most of the important impacts are covered. Institutional arguments are further important since the Japanese government has averted IFDI in the past. The extent of the remaining restrictions has a significant effect on market entry (Ito and Fukao, 2001, pp. 15-16), as well as the institutional distance does. The possibly surprising result found is that the institutional distance between Japan and Germany is low. Combined with Japan’s secure environment, the elimination of governmental barriers

to the greatest possible extent, and a company's wish to exert the highest control possible over the new subsidiary, the institutional chapter recommends a greenfield investment as entry mode.

The subsequent examination of culture and market entry yields that not just the politically induced formal, but also the culturally influenced, informal uncertainty is crucial to market entry (López-Duarte and Vidal-Suárez, 2010, p. 575). For consulting firms a functioning network and skilled, reliable local staff are of highest priority (Glückler, 2006, p. 376). The cultural and the trust-based perspective help to underline their effect on the choice of a market entry mode. The conclusion drawn from a cultural angle points towards a wholly owned subsidiary (WOS). The need for internal information transfer and the high distance of Japanese and German business culture are decisive. The difficulty of establishing trust between Japanese and Germans further supports the notion of not choosing a joint venture. The final conclusion recommends a greenfield investment as market entry mode. Choosing this mode, the German firm can avoid internal conflicts, exert high control and avoid suspicion towards or from a Japanese alliance partner. However, the great cultural gap between Japanese and Germans will require much attention when interacting with Japanese customers. Therefore, this thesis warns to conduct intensive market research and employ local employees in order to overcome the cultural gap and integrate into the Japanese market.

The thesis starts with a short literature review about market entry to Japan so far. The most important obstacles of entering the Japanese market are introduced. The chapter is followed by a quick recap of the most common market entry modes and their advantages and disadvantages, succeeded by a short introduction to the Japanese economic and political history. This is to deepen the understanding of Japan's current political environment and their cultural uniqueness<sup>1</sup>. The next three chapters explain market entry modes from an institutional, a cultural and a trust-based view and represent the core of this paper. Each chapter derives a set of propositions which suggest a market entry according to certain environmental circumstances. In order to evaluate these propositions, the three subsequent chapters then illustrate the actual institutional and cultural environment in Japan and Germany and the two peoples' views on trustworthiness. Using these findings and applying them to the before derived propositions, chapter 11 analyzes which market entry mode is most suitable for a

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<sup>1</sup> The thesis only focuses on the Japanese history as Japanese business structures and cultural features are known to be unique throughout the world. German customs are similar to other Western nations. In contrast, the Japanese traditions are not simply very specific but also impeding towards market entrants, as chapter 2 explains. Therefore, the historical chapter will help to understand the Japanese set of mind.

German consulting firm expanding to Japan. It first generates a result from the institutional perspective followed by a result from the cultural angle. Lastly, it analyzes the trust-based propositions. Chapter 12 then presents the final result. If the result from the institutional point of view contracts the cultural one, the trust-based result shall induce the final conclusion. If the first two agree, the trust-based analysis only verifies if the findings are viable. The last chapter describes a short conclusion and suggestions for future research.

## **2. Literature Review**

Japan has always been a fascinating market to many scholars. The fascination stems, on the one hand, from the great economic spurt Japan has achieved during the 1970s, but even more so from its otherness. Japan's economic characteristics are very different to most other market in the world and at the same time very distinct. Therefore, especially during the 1980s and 1990s, a variety of books and papers on business in Japan or business with Japan was published (Ford and Honeycutt, 1992; Hall, 1982; Matsuo, 1989). Apart from examining the Japanese market, these essays intensively studied the culture of Japan. During the following paragraphs, the main points academics focused on will be introduced. These include slow decision making by Japanese business partners, tight networks, unwritten cultural rules, differences on the labor market, and suspicion towards foreign products.

In terms of market entry to Japan, most economists concentrated on features hindering a smooth entry. To find these obstructions, they mainly tested their theories on manufacturing firms (Kanemoto and MacLeod, 1990; Ichniowski and Shaw, 1999; Kugot and Singh, 1988; Anand and Delios, 1997; Turpin 1993; Shane, 1994; Larson, 1992; Gulati, 1995). Only in recent years, a move towards service firms has started (Ekeledo and Sivakumar, 2004; Argawal and Ramaswami, 1992; Glückler, 2006; Brouthers and Brouthers, 2003; Erramilli and Rao, 1993). The first difficulty scholars found is the long time to market in Japan. It is very costly to establish an own business in Japan, thus new entrants must provide high monetary resources (Haak and Haak, 2008, p. 74). At the same time, Japanese businesses or customers respectively, before entering business with a new entrant or switching to a new vendor, they follow an extensive decision process (Olaja and Tyrväinen, 2007, p. 700). Hence, a market entering company must be able to bypass this period before diving into active business. The second barrier to market entry in Japan, which concerns mainly the past, was governmental restrictions on foreign ownership. Acquisitions in particular were rendered

almost impossible (Turpin, 1993, p. 11). These restrictions were, however, in large parts lifted during the 1970s and almost eliminated during the 1990s (Ito and Fukao, 2001, p. 10), after the economic bubble burst in Japan<sup>2</sup>. Blomstroem et al. (2000) still portray the governmental rules as nontransparent (p. 19), while Olaja and Tyrväinen (2007) heard from their test firms they felt rather supported by the Japanese government (p. 701). The next argument which leaves many firms reluctant to enter Japan is the continuing stagnation (Haak and Haak, 2008, p. 74). After the bubble economy, Japan entered a phase of economic stagnation. The country was able to escape this development during the early 2000s, however after the economic world crisis of 2008, Japan entered a short period of recession followed again by years of low economic growth (The World Bank Group, 2015). Another challenge corporations expanding to Japan face is the *keiretsu* system<sup>3</sup>. This system is inherent to the Japanese market. It promotes loyalty between manufacturers, buyers, and suppliers and prevents any of its members from being taken over or joining forces with a company outside the web (Lawrence, 1993, p. 102; Blomstroem et al., 2000, p. 19; Olaja and Tyrväinen, 2007, p. 700; Haak and Haak, 2008, p. 74; Kushida, 2010, p. 54). Since keiretsu include plenty of businesses, the group of potential business partners decreases notably. In addition, keiretsu groups sometimes take a monopoly position which prevents competitors from entering the market (Banerji and Sambharya, 1996, p. 91). Another characteristic of the Japanese market are the many unwritten rules, Japanese subconsciously obey, yet a foreigner needs to learn (Haghirian, 2010, p. 58; Turpin, 1993, p. 12; Ito and Fukao, 2001, p. 17). While one might argue that most countries' people follow a certain amount of unwritten laws, Japanese are very keen on everyone obeying to the rules. The Japanese culture takes great pride in their obedience. Thus, to them it is very important even for foreigners to follow the unwritten rules. A popular example of a small detail where those rules begin is how to hand over and to receive a business card. Not taking it with two hands is seen as deeply offensive (Ford and Honeycutt, 1992, p. 5; Sim et al., 2013, p. 81). It is of absolute priority to gain as much insight into the Japanese market as well as the culture and the business culture as possible in order to avoid misunderstandings and be successful (Lawrence, 1993, p. 87; Sullivan et al., 1981, p. 804; Turpin, 1993, p. 12; Haak and Haak, 2008, p. 74; Pucik, 1988, p. 488). Acquiring knowledge about these unwritten rules may be the most difficult. A further aspect is the high costs a firm has to expect when entering Japan. Corporate taxes, as well as rental prices are comparably

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<sup>2</sup> Further explanations about the bubble economy follow in chapter 4.5.

<sup>3</sup> The keiretsu system describes a web of supplier and buyer relations, which spins around financial supporters such as banks and insurance companies and thereby builds perfect protection against external disturbances (Lawrence, 1993, p. 93). Chapter 4.5 provides more detailed explanations.

high in Japan (Blomstroem et al., 2000, p. 19; Haak and Haak, 2008, p. 75; METI, 2014). The highest cost factor is labor costs (METI, 2014; Blomstroem et al., 2000, p. 19; Haak and Haak, 2008, p. 75). High labor costs, among others resulting from the seniority based payment system, are part of the very particular Japanese labor market.

The Japanese labor market in general differs significantly from its Western counterpart (Ballon, 1992, p. 125; Pucik, 1988, p. 488; METI, 2014). One typical characteristic is lifetime employment<sup>4</sup>. Japanese employees usually stay with one employer for their entire life (Kanemoto and MacLeod, 1990, p. 160). This naturally lowers the mobility of the Japanese workforce (Blomstroem et al., 2000, p. 19; Kushida, 2010, p. 54; METI, 2014). Many foreign entrants have complained about the difficulty to find qualified staff (Peterson and Schwind, 1977, p. 48; Olaja and Tyrväinen, 2007, p. 700). Experienced workers are usually not available, because of lifetime employment, and the education most Japanese receive is rather generalized. But not just technical knowledge, also the use of a common language depicts a barrier hard to overcome (Kevenhörster, 2010, pp. 349-350; Olaja and Tyrväinen, 2007, pp. 696-697; Sullivan et al., 1981, p. 804; Haghirian, 2010, p. 59; Peterson and Schwind, 1977, p. 48; METI, 2014). Expatriates sent to Japan usually speak English, yet lack the native language. Concurrently, Japanese do not possess sufficient knowledge of English. In conclusion communication is remarkably hampered. Employees cannot deliver information precisely; superiors cannot explain their plans smoothly (Peltokorpi, 2015, p. 59; Turpin, 1993, p. 12). In addition, they cannot praise their subordinates, which is an important tool to motivate staff (Peltokorpi, 2015, p. 60).

Next to the labor market, there are also many management practices as well as traditions in business unique to Japan (Turpin, 1993, p. 12). Foreigners entering the country often find themselves overwhelmed with the difference in requirements as much as with processes they deem natural which do not proceed. Peterson and Schwind (1977) conducted interviews with foreign managers in joint ventures and international firms in Japan. They often heard that Japanese do not communicate information accurately<sup>5</sup>, they cannot admit to their mistakes, and are not proactive enough (p. 48). This perception may account to the fact that Japanese focus their efforts on different areas than Westerners do. While Japanese embrace the path towards a goal by choosing a stable way and concentrating on harmonious

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<sup>4</sup> Lifetime employment as well as further human resource (HR) customs will be explained in chapter 9.8.2.

<sup>5</sup> As will be shown in chapter 9.8, these complaints are mainly based on incomplete business knowledge. Japanese communicate extensively in different situations than Europeans or Americans would, which highlights the need for a priori cultural research.

teamwork, Western managers prefer to see quick profits (Sullivan et al., 1981, p. 803). Lawrence (1993) contributes that the percentage of greenfield investments as measured by the entire IFDI to Japan are higher than in any other industrialized country. This underlines the internal difficulties foreign entrants have to overcome when arranging the native business culture of Japan and the corporate culture they bring from home (p. 99).

The last big topic in literature concerning market entry to Japan is the Japanese expectations and their reservation towards foreign products. Japanese are known to prefer local goods (Haghirian, 2010, p. 69; Lawrence, 1993, p. 88; Kushida, 2010, p. 54). They are used to high quality and perfect customization for the Japanese needs (Olaja and Tyrväinen, 2007, p 700; Richter and Vettel, 1995, p. 43; METI, 2014). They expect in foreign entrants to adapt their offerings to their taste and to conform to the high standards of service usual in their country. Mastering *keigo*, the Japanese form of speech used in official situations such as business exchanges, is seen as part of showing the willingness to integrate<sup>6</sup> (Ballon, 1992, p. 141). To promote a product and convince the natives of its quality is thus a much bigger challenge for a foreign market entrant than a local newcomer.

Different challenges of the Japanese market have been discussed in great detail. There has, in contrast, been little attempt to apply these findings to certain situations and to find out which risks weigh especially heavy according to which market entry mode. This thesis, therefore, tries to employ the past research to distinguish which particular market entry mode is best for a consulting firm and which risks it entails. The next chapter demonstrates more detailed the advantages and disadvantages of specific market entry modes.

### **3. Market Entry Modes**

When a firm decides to enter a foreign market, it needs to choose a market entry mode. It is “an institutional arrangement that makes possible the entry of a company’s products, technology, human skills, management, or other resources into a foreign country” (Root, 1987, p. 5). A market entry mode helps to plan a strategy: what resources to use, whether to build an alliance, and when to enter the foreign market. There are equity modes, such as joint ventures and WOS, including acquisitions and greenfield investments; and there are non-equity modes, such as licensing, non-equity alliances, and exports (Pan and Tse, 1996, p. 930; Schwens et al.,

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<sup>6</sup> The topic of the Japanese’s perception of foreignness is much wider, and therefore further discussed in chapter 10.4.

2010, p. 330). The latter is especially useful in case of products, technologies, and vendible knowledge. It describes a loose connection with a more flexible character. In case of a consulting firm, a more holistic entry is necessary in order to successfully transfer business practices, which is why this work will concentrate on foreign direct investment (FDI), meaning equity-based entry modes<sup>7</sup>. They include a higher level of internalization, which facilitates the transfer a wide range of information (Dacin et al., 2007, p. 179).

The main goal for firms when entering a foreign market is to develop a competitive advantage and thus secure their long-term profits (Pan and Tse, 1996, p. 931; Anderson and Gatignon, 1986, p. 2). Hence, a corporation needs to carefully choose an entry mode which insures this competitive advantage. There are many equity modes to choose from, however, this work considers only three: joint venture, acquisition and greenfield investment<sup>8</sup>. When deciding between these three modes, the firm faces a trade-off between control and equity based risk (Rasheed, 2005, p. 45). Depending on how much control it deems to be necessary to conduct fruitful business, the company will invest. The more it invests, the greater the risk (Agarwal and Ramaswami, 1992, p. 2; Gao, 2004, p. 39; Rasheed, 2005, p. 42; Pan and Tse, 1996, p. 930), which is why FDI requires a high level of administrative organization (Rasheed, 2005, p. 43). The more equity, and hence control, a company attains, the better it can guide the foreign business in their own interest and the higher is its profit share (Agarwal and Ramaswami, 1992, p. 3; Anderson and Gatignon, 1986, p. 3). However, control is not the only deciding factor. There are many criteria which can influence the choice of a market entry mode, such as expert knowledge which should not leak, the size of a company, prior market entry experience, environmental instabilities (Agarwal and Ramaswami, 1992, p. 5), access to resources and technologies, real exchange rates, market expertise (Wernerfelt, 1984, p. 179; Banerji and Sambharya, 1996, p. 90; Tuppura et al., 2008, p. 484), and institutions, culture and trust. This work focuses on the last three items, since they are especially important for a consulting firm to consider. A consulting firm provides services, needs extensive market knowledge, and good human interaction. The knowledge of the local institutions and culture, and building up trust to local workers and customers are essential. After having gained this knowledge, the company has to integrate the requirements of its environment and their internal processes (Gao, 2004, p. 41; Ballon, 1992, p. 145, Rasheed, 2005, p. 43). In order to

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<sup>7</sup> In the following, businesses alliances shall be defined as equity-based business alliances. In the same manner, the word joint venture will be used as equity-based joint venture, as it is common in the business literature (Canabal and White III, 2008, p. 268; Pan and Tse, 1996, p. 930).

<sup>8</sup> Most literature about market entry to Japan, as well as empirical work about market entry in connection with institutional, cultural, and trust-based views, only regards these three modes, which is why the extension to further modes would not be constructive.

find out which market entry mode plays to this integration process, this chapter provides details first about joint ventures, then acquisitions, and last about greenfield investment.

### **3.1. Joint Venture**

The first entry mode is a joint venture. Among the three to be presented, it contains the lowest equity involvement and the highest power sharing. It is a business alliance where two companies decide to conduct joint business for a set amount of time (Dacin et al., 2007, p. 170). A contract codifies which activities are to be joint, the distribution of power, as well as the distribution of profits. The agreement must clearly state the amount of equity each company contributes, and thus the amount of control they are granted (Hofstede and Hofstede, 2005, p. 347; Parkhe, 1993, p. 308). If one company possesses the bigger share, usually the other firm demands a collateral as proof the former will not ignore their interests (Anderson and Gatignon, 1986, pp. 4-5). Most important for a successful joint venture is intensive communication. It helps the two companies to harmonize their businesses, shows their commitment, and thereby prevents mistrust (Pothkuchi et al., 2002, p. 262).

A joint venture has many advantages. First, it helps to share risk (Contractor, 1990, p. 49). Less equity means less to lose (Agarwal and Ramaswami, 1992 p. 3; Hitt et al., 2006, p. 225). That is why a joint venture is especially popular when entering an economically unstable or recessing country (Meyer and Nyugen, 2005, p. 15, Hitt et al., 2006, p. 226). At the same time, when entering a foreign market and allying with a local company, entry costs are drastically reduced (Hitt et al., 2006, p. 225). A joint venture can help to gain access to specific market knowledge, technological know-how, management competencies, and tangible resources (Anand and Delios, 1997, p. 581; Ballon, 1992, p. 125; Davis et al., 2000, p. 253; Dacin et al., 2007, p. 181; Hitt et al., 2006, p. 226) and may lead to profitable synergistic effects (Haak and Haak, 2008, p. 112; Anand and Delios, 1997, p. 582). It is a very fast way to market, since the firm does not need the time to establish its own premises and processes (Contractor, 1990, p. 46; Haak and Haak, 2008, p. 111) Furthermore, a company can use its partner's brand name and gain access to customers which paves the way for a smooth entry (Ballon, 1992, p. 125, Contractor, 1990, p. 46). A joint venture is recommended in case internalization is not feasible (Meyer and Nyugen, 2005, p. 15) or simply when there are institutional barriers preventing an acquisition or a greenfield investment. Also, the unsure value of a potentially profitable firm may suggest a joint venture instead of an acquisition (Hennart and Reddy, 1997, p. 3). Last, a business alliance

contributes significantly in case the new market is network-based (Meyer and Nyugen, 2005, p. 16).

On the other hand, there are also disadvantages when entering a joint venture. First of all, there is the loss of control, which however is not a definite sign for failure (Ballon, 1992, p. 125; Meyer and Nyugen, 2005, p. 16). Sharing business leads to information asymmetry and provides possibilities for opportunistic behavior, especially concerning long-term transactions (López-Duarte and Vidal-Suárez, 2012, p. 2253). Contracts are usually incomplete, particularly since not all future developments can be foreseen and included (Brouthers, 2002, p. 205). It is not easy to monitor the partner which increases the danger of one firm leaking vital information to third parties (Haak and Haak, 2008, p. 112; Parkhe, 1993, p. 308). Two firms need to conquer the challenge of building a relation of trust. Therefore, both try to act in a trustworthy manner and provide the skills they promised (Haak and Haak, 2008, p. 112; Davis et al., 2000, p. 253; Ballon, 1992, p. 125). However, developing trust is impeded by differences in language, culture, and geographic distance, which lowers the frequency of verbal exchange (Hofstede and Hofstede, 2005, p. 347; Davis et al., 2000, p. 250; Haak and Haak, 2008, p. 112). Some companies may feel difficulty to agree on distribution channels or product usage, as well as HR practices (Davis et al., 2000, p. 250; Ballon, 1992, p. 125; Estrin et al., 2009, p. 1174). The collaboration may thus be restricted to certain selected areas. Last, future environmental changes may induce a change of direction in the development of one firm which lets the partners drift apart and the joint business be of short-termed nature (Haak and Haak, 2008, p. 113). The end of a joint venture is often defined by a buy-out of one partner by the other, when he feels the need to take control (Porter and Fuller, 1986, p. 329; Ballon, 1992, p. 125). But there are also modes of entry which promise exclusive control right from the beginning, which are described in the following two chapters.

### **3.2. Acquisition**

An acquisition describes the process, where one companies buys another one (Hofstede and Hofstede, 2005, p. 347). This involves a much higher investment and thus exposes the company to a higher risk, but at the same time grants the buyer sole control of the acquired firm (Agarwal and Ramaswami, 1992, p. 3). In comparison to a joint venture, this mode promises more control, as well as a lower risk of sensible knowledge leaking to third parties (Hitt et al., 2006, p. 227). It also erases the danger of one partner behaving opportunistically (López-Duarte and Vidal-Suárez, 2012, p. 2253). Further advantages are the

incorporation of technologies, the sharing of resources and production which can prevent duplication (Davis et al., 2000, p. 252), and the access to new clientele, as well as necessary resources (Hitt et al., 2006, 227; Contractor, 1990, p. 32; Wernerfelt, 1984, p. 175; Davis et al., 2000, p. 243). The latter describes not simply tangible resources, but also skills, competencies which help overcome internal obstacles, and tacit knowledge reaching from market knowledge and cultural expertise to the point of an entire organizational set-up which can be copied or learned from (Anand and Delios, 1997, p. 582; Hitt et al., 2006, p. 227; Hennart and Reddy; 1997; p.2). Buying a local brand may also facilitate the market entry (Wernerfelt, 1984, p. 175). Generally, acquisition is a very fast way to market. The buyer can simply continue and adapt the ongoing business (Hitt et al., 2006, p. 228; Hofstede and Hofstede, 2005, p. 347).

Despite all these advantages, acquisitions also lead to negative consequences. First, in comparison to a joint venture, the high equity commitment complicates a market exit (Hitt et al., 2006, p. 228). Therefore, acquisition requires a careful selection process and should be used mainly in high-potential markets. Furthermore, acquisition represents in most cases a hostile takeover which leaves a bitter aftertaste. This may result in a bad reputation externally, if media reports negatively. But more so, internal dissatisfaction is likely to occur. The local staff will probably meet the new management with great suspicion (Hofstede and Hofstede, 2005, p. 347). The buyer must hence calculate whether to renew the management or keep the current, balance local and home culture, and find a path to integrate the former and the new workforce (Davis et al., 2000, p. 253; Hitt et al., 2006, p. 227). Last, because of asymmetric information the appraisal of a firm is often difficult. Thus, the price negotiations do not always pass smoothly (Anand and Delios, 1997, p. 582). In summary, the acquisition provides an easy access to market with high control, yet the integration of the local workforce depicts a great risk for a successful market entry. This can be omitted by choosing a greenfield investment, further explained in the following chapter.

### **3.3. Greenfield Investment**

A greenfield investment describes the process where a firm sets up an entirely new subsidiary in a foreign country using staff from home as well as hiring local employees, if needed (Hofstede and Hofstede, 2005, p. 347). This type of entry mode has the advantage of being completely independent from any other company (Hitt et al., 2006, p. 228; Haak and Haak, 2008, p. 115). No cultural balance between the local staff and employees or

management from home is needed. New local workers can be hired as they are willing to integrate in the proposed corporate culture (Hofstede and Hofstede, 2005, p. 347). The company can steadily develop and integrate interests from home and local availability of resources, customers, and staff (Estrin et al., 2009, pp. 173-1174; Meyer and Nyugen, 2005, p. 16). It might even be able to use the differences between home and host country and gain a competitive advantage local companies do not have access to (Hennart and Reddy, 1997, p. 2). The parent firm solely decides its future goals and siphons profits gained from its own assets and expertise (Agarwal and Ramaswami, 1992, p. 3). Thus, it plans its strategy and finds a way to extract the maximum benefits from the assets it provides to the subsidiary (Haak and Haak, 2008, p. 116; Lu, 2002, p. 19). Involving no unfamiliar firm, the company has little risk of leaking information (Agarwal and Ramaswami, 1992, p. 4).

Nonetheless, greenfield investment also include a few negative aspects. First of all, the greenfield investment is the most costly, both from a temporal as well as from a monetary point of view (Haak and Haak, 2008, p. 115; Hofstede and Hofstede, 2005, p. 347). The high resource commitment raises the risk in case the market entry fails (Agarwal and Ramaswami, 1992, p. 3). There is no partner to seek help from in times of crises. Finding competent and skilled local staff may be a long and difficult process. Concurrently, the firm may have trouble to integrate the locals' way of thought and the corporation culture. Depending on the amount of natives hired, the staff and the management may not agree on how to conduct business, because of their cultural difference (Haak and Haak, 2008, p. 116). However, since there is no alliance with a local partner firm, the entering company may be dependent on local workers in order to gain enough market knowledge. Coming from a foreign country, the corporation needs to research the new market well and collect as much inside information as possible (Hennart and Reddy, 1997, p. 2). Being a foreigner entails a lack of knowledge both on the company's as well as on the customer's side. Thus, understanding the local way of thought as well as convincing local clients is crucial to entering the market<sup>9</sup>. Having prior market entry experience may facilitate this process (Hitt et al., 2006, p. 228).

In conclusion, the three above presented market entry modes each have their advantages and disadvantages. Joint venture helps to gain local market expertise and reduces equity risks but also claims a loss of control and needs trust between two unfamiliar firms; acquisition provides control and local expertise but demands for integration of the home and the local culture after a possibly hostile buyout; greenfield investment also offers sole control

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<sup>9</sup> Chapter 6 includes further details on the effects of cultural distance on the choice of a market entry mode.

and less integration of local and home staff but contributes no local expertise which the company has to attain itself. This presentation of pro and contra arguments will help to analyze which market entry mode is best for the German consulting firm entering the Japanese market. The following chapter details the economic history of Japan, to give a better understanding of the country's current economy, culture and institutional set-up.

#### **4. Economic History of Japan**

Japan's historic development had a great influence on its current economic situation as well as its attitude towards foreign market entrants. Since the Meiji period, Japan's opening towards Western countries has started. Japan went through vast political as well as economic changes. Especially during the past 40 years, Japan has seen periods of strong economic boom as well as deep recession. However, on an institutional level a movement towards attracting IFDI has started. Regulations were loosened and diplomatic efforts strengthened (Ministry of Foreign Affairs of Japan, 2014). As numbers show, these efforts were only partly successful. While public obstacles were lessened, those on a cultural level are still sturdily present. An overview on Japan's history will give helpful clues why these hindrances have not faded, even today.

During the Tokugawa period (1603–1868), Japan was split into various mostly self-governing domains. Although loosely tied by a central government, the country was characterized by internal conflicts. The Emperor lost his power to the Shogun, a military leader who reigned Japan in a dictatorial way. He decided Japan's absolute seclusion from the rest of the world. Only little trade with China and Korea was allowed (Flath, 2005, p.26). Foreign interest in Japan, conversely, started to grow at the beginning of the nineteenth century. The US government sent Matthew C. Perry who came to Japan in 1853 in order to convince Japan to open its market. They were mainly interested in Japan's coal supplies as well as it becoming a base to refill stocks on American vessels. In 1858, Perry was able to convince the Shogunate to sign the Treaty of Amity and Commerce. It allowed for trade in certain cities such as Yokohama and Kobe. Unfortunately, the treaty included an exchange rate unfavorable for Japan. At that time, the country had to accept this since its military outfit was not yet prepared to risk a war with Western countries. (Banno, 2014, p. 19) Consequently, further treaties with similar conditions with countries such as the Netherlands, Russia, Britain and France followed. The Shogun's acceptance of such critical agreements led Japan's

*Daimyōs*<sup>10</sup> to intensify their resistance against the ruler which eventually led to the end of the Tokugawa period in 1967 (Flath, 2005, p. 28). The first intensive contact with foreign forces was not one of amity, thus an up and down of rapport ensued during the following decades. After the Tokugawa period however, the Meiji period (1868-1912) promised change. Japan's leaders of this age looked positively on foreign forces, and therefore an era of exchange with other nations began, albeit Japan's government made sure Japanese knew and treasured their national identity (Kevenhörster, 2010, p. 239).

#### **4.1. Meiji Period**

The Meiji period was an era of existential change in Japan. The dictatorship of the Shogun ended, the economy started to grow and Japan opened up towards the Western world. New technologies were introduced and the government thereby paved the way for the later following era of industrialization. Ralston et al. (2008) name this era as the beginning of Japan's "capitalistic philosophy"(p. 12).

In 1867 lower-ranking samurai managed to overthrow the Shogunate. They rearranged Japan's subdivision and established today's prefectures (Banno, 2014, p. 52). The Emperor's power was reinstated although, even at that time, his power was of a symbolic nature and the actual legislative force lay upon a group of now reigning samurai. In 1889 a constitution was introduced and in 1890 the first parliament inaugurated. Rich landlords voted the members of the House of Representatives from two main parties. The Emperor was granted a veto power (Banno, 2014, p. 109). Nonetheless, the Emperor maintained a characteristic of supremacy which led the people to rarely challenge the deity's decisions and contributed to Japan's unity. (Iriye, 1998, p. 33) All prefectures were subject to one unifying regime. This regime introduced a new direction of thought. Japan was to become a strong country and a world-respected power hence the country's leaders decided to renew Japan's political and economic organization geared to Western countries. (Banno, 2014, p. 55)

As early as 1881 academic members of the government promoted a new constitution based on the German one (Banno, 2014, p.57). Furthermore, the government implemented a nationwide currency and helped private banks open across the country (Sasada, 2013, p. 23). In order to push the economic development, the main goal was a fast process of industrialization. First, the government imposed new taxes so as to shift income from the

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<sup>10</sup> Daimyōs were the leader of the subdomains of Japan (Flath, 2005, p. 2).

agricultural sector towards the industrial sector (Iriye, 1998, p. 31). Second, it engaged in extensive investments with the purpose of supporting infrastructures vital to industrialization. Most famously, after they won Russo-Japanese War (1905-1906), Japan was able to gain the necessary financial and territorial resources to increase spending and expand their railroad system (Nakamura and Odaka, 1990, p. 8). These investments were, however, mostly of short nature. The acquired firms were resold soon after, due to a lack of successful management. Nonetheless, in private hands these companies contributed to Japan's economic spurt.

Next to investing itself, the government also tried to encourage private investment. The regime's most important goal was the introduction of foreign technologies. They achieved this by purchasing technologies, hiring European engineers, as well as dispatching expatriates to learn in Western enterprises (Sasada, 2013, p. 24; Iriye, 1998, p. 31). By enhancing technological progress, Japan hoped and achieved to become capable of competing on international markets. During the Meiji period Japan turned into an export-led economy. While a lack of natural resources hindered Japan from becoming entirely self-sufficient, it still managed to substitute large parts of import by producing goods locally, in industries such as paper and pulp, chemicals and transport machinery and at the same time improved already successful manufacturing such as textiles and machinery to export to Europe. The only obstacle for Japan's successful export during the first half of the Meiji period was the *unequal treaties*<sup>11</sup> still pending over Japan which prevented it from introducing appropriate import tax. In 1906, after the Russo-Japanese war, they were abolished which led Japan to strongly increase tariffs (Nakamura and Okada, 1990, pp. 6-7). Another important development after the war is the beginning of formation of joint ventures with European companies. The foreigners showed interest in long-term oriented investments in Japanese industries and were welcome to do so during this period of internationalization in Japan (Nakamura and Okada, 1990, pp. 10-11).

The Meiji period had transformed Japan from a closed country, shaken by internal conflicts, exchanging almost only with other East Asian countries, into a competitive nation engaging in international trade, yet with a strong sense of national identity. In 1897 Japan joined the gold standard, thereby gaining the ability to hold a sturdy exchange rate to other

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<sup>11</sup> Academics regard the unequal treaties in two different ways. One direction sees them as unfair and harmful to Japan's economic development. Others treat them as trigger for Japan to become a country of high quality produce. This obstacle made Japanese manufacturers develop quicker and become more efficient (Nakamura and Odaka, 1990, p. 7).

currencies (Nakamura and Okada, 1990, p. 8). The following years during WWI and the interwar years, Japan was able to maintain and improve its economic progress.

## **4.2. WWI and the Emergence of Zaibatsu**

The years of the First World War helped the Japanese economy to take another big leap. Exports increased sharply and Japan achieved international recognition and acquired its position in international politics. The famous zaibatsu families accomplished to spread their influence and power by diversifying their business portfolio. The economic boom which had started during the Meiji Era continued and even intensified.

As Japan had been in a constant conflict with China since its decision to become independent of the previously Chinese ruling of East Asia, it allied with the British forces during WWI. In 1914 it declared war, but in fact Japan was able to maintain the position of a bystander and hardly engaged in actual warfare. Instead, it became a supplier of goods Europe now struggled to produce since all the Western countries' spending was directed towards warfare. Japan's export of metals, machinery, and silk skyrocketed. The country was not just able to stabilize its financial situation but also its political recognition among other world powers. It joined the European nations as a political rival in pursuit of empire (Flath, 2005, pp. 43-45).

Before WWI, Japan had accumulated a lot of foreign debts in order to finance its wars against China and Russia. The country now managed to move its status from a debtor to a lender. And when the Yen depreciated exports strongly increased. During this period Japan's GDP grew by 3-5% (Flath, 2005, p. 46) and for the first time income tax revenues were higher than those gained from land tax (Banno, 2014, p. 161). Various sectors profited from technological progress.

One type of business which managed to successfully use the economic boom of WWI is the zaibatsu business conglomerates. "Each zaibatsu (lit. 'property agglomeration') was a set of interrelated and interlocked commercial enterprises, closely held by the same family." (Flath, 2005, p. 46) Before the First World War, most businesses belonged to several small shareholders. Withal, even then family-owned businesses formed an important part of the Japanese economy. They mainly operated in industries such as mining, shipbuilding, trade or banking. Those industries thrived throughout the war years, which helped these family businesses to widen their portfolio. They acquired large shares of other companies or created

family ties in order to expand into other business areas, all the while keeping close control of their core business. These new business conglomerates were called zaibatsu (Flath, 2005, p. 49). They often used managers who were not family members in order to run their business, and more often than not, these managers were integrated into the family through marriage or adoption (Chen, 2004, p. 140). In many cases zaibatsu achieved almost monopoly status within their industry. Only rarely, government officials tried to hamper them. The most famous zaibatsu at the time were: Mitsui, Mitsubishi, Sumitomo, and Yasuda.

### **4.3. Interwar Period**

The interwar period led to fundamental political changes in Japan. The emergence of zaibatsu did not only shape the Japanese economy but also influenced the regime. This influence was diminished, though, when military leaders took over command as conflicts with China aggravated. Apart from institutional change, Japan was struck by natural catastrophes as well as discontent of the people. Japan's economic growth slowed noticeably compared to the war period yet it never fully ceased.

During the Meiji period, former samurai managed to uphold their political power. However, after the First World War, party politicians replaced them. These party politicians were mainly direct or indirect zaibatsu family members. The business conglomerate owners had a strong interest in improving as well as preserving politically favorable conditions. They achieved this by infiltrating the government with their member in various ways. Marriages to important politicians' or business partners' children were arranged, capable managers adopted, political positions taken over and bribes were paid (Sasada, 2013, pp. 34-36). The zaibatsu system displays one very important feature of the Japanese culture. As soon as a person was integrated into the family, the zaibatsu's head trusted that person. And the new family member usually rewarded this trust with trustworthy behavior. The notion of trust for in-group members is a very important characteristic of the Japanese society and will be further explained in chapter 9.2.

The party politicians implemented a reign of laissez-faire (Sasada, 2013, p. 90). The power went to the businesses. Generally, this helped the Japanese economy. Especially during the early 1920s, Japan was able to extend its economic growth; specifically the export-led industries such as textiles and machinery could develop generously. Later, the heavy industry, electricity and chemicals were added to the most successful business activities. Urbanization

and town planning commenced in Japan. The absence of any antitrust regulations paved the way for zaibatsu to spread their influence into any business sector without obstruction in order to lower local obstruction. However, the technological development entailed by the advancing industrialization and the self-seeking behavior of the zaibatsu families triggered a new labor movement across Japan. Labor unions sprung from most industries to help settle heavy labor disputes (Nakamura and Okada, 1990, pp. 20-31). Discontent started to grow among workers.

In 1923 the Great Kantō Earthquake destroyed Japan's second largest city and one of the main ports, Yokohama, as well as large parts of the capital, Tokyo. The country had to cope with more than 100.000 casualties (Flath, 2005, p. 55). This fatal catastrophe naturally hampered but never stopped Japan's economic development. The Bank of Japan provided financial help to local banks so that loans to private customers and small businesses could be extended (Nakamura and Okada, 1990, p. 18). Soon the government faced the depletion of its reserves of specie and its monetary base, and therefore needed to borrow money internationally. While the US as well as most Western European nations readapted the gold standard system soon after WWI ended, Japan now encountered the Yen's strong depreciation against the dollar. Businesses of international trade now had to deal with the absence of expected income (Flath, 2005, p. 55; Banno, 2014, p. 191).

In 1929 the Great Depression began in the US and spread across the world. Japan's exports went down quickly since one of the country's main buyers, the US, lost its purchasing power (Sasada, 2013, p. 86). Despite this international financial crisis, the Japanese Minister of Finance, Junnosuke Inoue, decided to return to the gold standard at prewar conditions at the beginning of 1930, causing a severe appreciation of the Yen against the dollar and a deflation of the Yen within Japan. Export immediately further plummeted due to the high costs of Japanese goods and local manufacturers turned to international suppliers profiting from low cost foreign goods. The agricultural sector, still representing one of the most important suppliers of work within Japan, took a strong hit. Japan entered the era of the so-called Showa Crisis (Flath, 2005, p.57; Nakamura and Okada, 1990, pp. 34-38).

Within the same year, the Japanese government changed and Japan once again left the gold standard in 1931 (Banno, 2014, p. 191). From that moment on, Japan was able to return to a prospering economy. Export intensified anew, local industries managed to substitute import goods and the population started to move back to rural areas (Nakamura and Odaka, 1990, p. 53). At the same time, a political change announced itself. Zaibatsu families now faced the military bureaucracy challenging their institutional power. The public was deeply

discontent after the depression of the 1920s and looking for a change in leadership. A period of institutionalization began in Japan. The country's political parties represented different strains of thought including liberalism (favored by zaibatsu families) which idealizes the government to refrain from economic interference, Marxism (favored by supporters of communism) which in turn supports an entirely planned economy, and national socialism (supported by the military bureaucrats) which limits the capitalist power yet not as much as communism does. The most dominant party was the *Tozai Keizai Ron*, a reformist bureaucrats' party, which benefited from strong support by intellectuals. They denounced the zaibatsu's greed as the cause of the Showa Crisis and promised to move from a "profit-seeking to an output-seeking" (Sasada, 2013, p. 92) economy. They proclaimed the Soviet Union as their idol since the country was the only one being spared from the Great Depression. Following their role model, Tozei Keizai Ron wanted to implement a long-term plan to enhance the Japanese economy (Sasada, 2013, pp. 92-102). They succeeded in establishing a Planning Board. At the same time, the conflict between Japan and China flared up again, which served as the last impulse for the military bureaucracy to take over the Japanese government (Sasada, 2013, p. 118).

The economic recovery of the early 1930s, however, was soon to end. The conflict with China escalated and Japan entered a state of war. During the Second World War Japan took over a very active role in warfare and redirected all its resources towards the combat. The years to come strongly shaped Japan's economy as well as society and its perception of and attitude towards foreigners.

#### **4.4. WWII and the Era of Occupation**

Japan's economic boom ceased with the beginning of WWII and could only be retrieved after the American occupation ended. Heavy warfare and the two atomic bombs which hit Japan in 1945 precipitated the country and its people into a state of devastation and struggle. The American occupiers then tried to rebuild Japan, however on their own terms.

The conflict between Japan and China never fully vanished. Although Japan had to make several territorial concessions to China after WWI, the state of Manchuria and the two countries' wish to prove their power and to extend their borders resulted in aggressive tension.

The incident at the Marco Polo Bridge<sup>12</sup> triggered another outbreak of combat in 1937. From that moment on the Japanese government deeply interfered with the economy. Manufacturers were forced to stop their usual production and exclusively produce weaponry. Labor unions were prohibited in order to secure smooth manufacturing (Nakamura and Odaka, 1990, p. 338). Resources were directed towards warfare only. Exports decreased and imports focused on material needed for arms production. Japan's alliance with Germany and the entailed war against the US and most West European countries further aggravated Japan's situation. Considering that the US and the UK were Japan's main buyers as well as suppliers, Japan's foreign trade crumbled. The country could not export anymore, and soon imports did not suffice to supply manufacturing sights and as well as civilians suffering from sudden poverty. The atomic bombs on Hiroshima and Nagasaki marked the defeat of Japan. On September 2<sup>nd</sup> 1945, Japanese representatives officially signed its surrender to the US. The era of the American Occupation began.

Post-war Japan was characterized by a great lack of food supply, poverty and destruction. Civilians suffered from hunger and malnutrition (Hein, 1998, p. 48; Sasada, 2013, p. 135). Many companies had been forced to direct their production towards warfare essentials which is why regular manufacturing did no longer suffice (Nakamura and Odaka, 1990, pp. 88-89). The US government used the situation to reconstruct Japan according to their own ideology. Their ultimate goal was to democratize Japan (Flath, 2005, p. 72). In doing so, America hoped to lessen Japan's aggression against the outside world (Nakamura and Odaka, 1990, p. 341) and create another close ally for the US. In order to recompose Japan, the occupying force implemented various drastic measures which were executed by the Supreme Commander of the Allied Powers (SCAP)<sup>13</sup>. The US government left the current diet<sup>14</sup> in power, however, purged any military-related person from institutional positions. It further dissolved the imperial army in order to take Japan's ability to engage in war activities (Sasada, 2013, p. 140). In 1946 the SCAP drafted a new constitution on Japan which included a clause about Japan being only able to engage in warfare for reasons of self-defense. One year later, this constitution came into effect (Flath, 2005, p. 73; Hamada and Mimaki, 2011, p. 137). The prime minister at the time, Shigeru Yoshida, additionally promised to place the economy above all and direct all government efforts accordingly (Hein, 1998, p. 51). The

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<sup>12</sup>Through a conspiracy by the Japanese military, army members stationed at the Marco Polo bridge lured the Chinese counterforce to open fire on July 7th, 1937. This is known as the beginning of the Sino-Japan War (Crowley, 1963, p. 281).

<sup>13</sup>From August 1945 until April 1951 General Douglas MacArthur took over this position, April 1951 until April 1952 General Mathew B. Ridgway replaced MacArthur.

<sup>14</sup>Chapter 8.1.1 contains further explanations of the Japanese diet.

second measure the SCAP realized was reinstalling labor unions (Flath, 2005, p. 77; Nakamura and Odaka, 1990, p. 338). Third, the US government was eager to dissolve all zaibatsu groups. The business conglomerates were believed to have too much political power as well as suspected to have ties to the former military-led government (Sasada, 2013, p. 140). Therefore, the SCAP enforced the Anti-Monopoly Law in April 1947 and the Law for Exclusion of Excessive Concentration of Economic Power in December 1947 (Nakamura and Odaka, 1990, p. 88). The zaibatsu main holding companies were dissolved and the shares in the remaining companies resold. Members of the management were dismissed (Flath, 2005, p. 75). The fourth and last important change was the land reform. Landownership was transferred to tenants who actually used it (Nakamura and Odaka, 1990, p. 88; Flath, 2005, p. 73). A redistribution of wealth was to further support the main goal of democratization and the establishment of a “liberal democratic state” (Sasada, 2013, p. 139).

The US government actively pursued Japan’s economic recovery. Right after the end of the war, the Reconstruction Finance Bank (RFB) was founded. It provided subsidized loans to companies so they could resume their pre-war production or enter the market for the first time. The RFB itself was entitled to loans by the BOJ. In addition, the SCAP established the Board of Trade within the Japanese government. This new agency and the US government handled all trade between Japan and the US. The Board of Trade would buy goods from Japanese manufacturers at elevated prices and sell them to the US at market price and in turn buy on the international market and sell it in Japan for less (Flath, 2005, p. 82; Nakamura and Okada, 1998, p. 92).

This institutional interference in the Japanese economy both contributed to the recovery but at the same time resulted in an unstoppable inflation and dependency on foreign financial aid. As tensions during the Cold War grew and the US had to fear an escalation in Korea, its attitude towards Japan changed. In 1949, the government decided to reverse course and turn Japan into a base it could use in case of war. For this, Japan needed to become independent from financial aid from the US. The economist Joseph M. Dodge was sent to Japan and introduced new policies, later known as the Dodge line (Nakamura and Okada, 1998, p. 92; Sasada, 2013, p. 145). The RFB was closed down, as well as the subsidies for international trade through the Board of trade ended. Japanese companies had to accustom to face national as much as international competition again (Flath, 2005, pp. 83-84; Sasada, 2013, p. 141). The Ministry of International Trade and Industry (MITI) was founded in 1949. Although governmental interference with the economy was to stop, MITI still engaged in

long-term economic planning. Hence, it enforced rationalization policies to direct corporations toward investments in research and development (R&D) and infrastructure, among others, and in selected industries MITI also ensured reduced competition to protect small firms<sup>15</sup> (Sasada, 2013, pp. 123-129).

The Meiji Era and the period after the Second World War have been vital to shaping the organization of firms and the cultural development of Japan. The Meiji period represents the first important step of Japan opening towards the Western world. During the American occupation, many new business practices came to Japan, such as lifetime employment, seniority-based pay, and job rotation<sup>16</sup>. Market regulation was no longer conducted by the zaibatsu groups but by the government. Nonetheless, after the dissolution of the zaibatsu groups, a new kind of cartel-like business conglomerate emerged, called a keiretsu. At its center was a main bank providing loans as well as management advice, monitoring all business activities and interfering in case of inefficiency (Flath, 2005, p. 283). The main bank system ended during the 1990s banking crisis, yet keiretsu still exist today and by holding cartel-like positions (Flath, 2005, p. 286), create challenging environments for market entrants as already discussed in chapter 2.

Aside from economic influences, the American occupation has also introduced certain cultural values to Japan and thereby shaped the manifold cultural attributes of the Japanese people. The following decades until today help to explain the perception of foreigners in Japan why a market entry to this country is still difficult.

#### **4.5. 1950s until Today**

The Korean War (1951-1953) ultimately restored Japan's economy. The American demand for supplies during the war boosted exports and Japan accomplished the transition from a suffering, dependent country to a flourishing economy. In April 1952, Japan regained its sovereignty (Flath, 2005, p. 86). The real economic spurt, however, occurred after 1960. Facilitated by measures such as the revision of the Anti-Monopoly Law to less strict regulations, the introduction of high quality control, which enhanced the international image of Japanese manufactured goods, and the development of the Toyota Production System, which eliminated "muda (waste), muri (overloading), and mura (inconsistency)" (Odaka,

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<sup>15</sup> Japan was still in a phase of dire need to widen production in order to supply national as well as export needs (Sasada, 2013, p. 129).

<sup>16</sup> These practices are further explained in chapter 9.8.2.

2011, p. 94) Japanese companies enjoyed great success during the 1960s. Prime Minister Hayato Ikeda (1960-1964), who first suffered from a disreputable image due to his defense of the Yoshida Doctrine,<sup>17</sup> succeeded by putting great effort in enhancing the Japanese economy and workers' conditions. Industrial policies included among others social welfare within firms and a steep increase of government spending towards education and less income disparity between different regions of Japan (Hein, 1998, p. 56). The average income rose rapidly, therefore spending increased and the economy benefited from a further push. The upward spiral came to a sudden end with the first oil shock in 1973<sup>18</sup>. Yet, Japan remained the world's biggest creditor (Hamada and Mimaki, 2011, p. 138). In 1979, Japan had to endure the second oil shock, but again, during the 1980s, by allowing for heavy and chemical industry-related IFDI (Blomstroem et al., 2000, p. 18), Japan managed to recover and revive its economic growth, albeit not as high as before (Kingston, 2013, p. 15).

During this period of growth a change occurred in the Japanese people's perception of foreigners. Considering their own success and observing the struggles of foreign capitalist countries, Japanese recognized their own economic capabilities. They started to see themselves as superior and attributed their success to traditional values and diligence. Resentment against Americans for bringing capitalism into Japan spread across the country (Hein, 1998, p. 60).

The era of Japan as the miracle economy made the country a role model for many Western countries. Nonetheless, this ended during the 1980s. 1987-1990 were the years of Japan's bubble economy. The bubble built up in two assets, Japan's stock market and land prices. The Nikkei Index, measuring the development of Tokyo's stock market, almost doubled, and land prices quadrupled (Kingston, 2013, p. 15). Investing and spending flourished throughout the country. However, this period could not hold out for long. At the beginning of the 1990s, the bubble burst (Flath, 2005, p. 132) and Japan has not been able to fully recover ever since. Wages decreased and the unemployment rate increased (Kuroda and Yamamoto, 2005, p. 26). Japan's strategy was to infuse businesses with loans to prevent closing. Because of the keiretsu system, this occurred with little regard to profitability. Banks tried to save the members of their keiretsu (Blundell-Wignall et al., 2008, p. 15). This and the

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<sup>17</sup> According to the Yoshida Doctrine economy was placed above all governmental matters. The Japanese army can only be used for defense reasons and no more than 1% of the GDP can be spent on the military. While Yoshida himself had only accepted these rules during the American occupation as temporarily, Ikeda now did not retreat although the era of occupation had ended.

<sup>18</sup> In 1973 the Arab countries blocked oil trades which raised oil prices all around the world. Japan's economy, with the country being a big oil importer, took a strong hit (Flath, 2005, p. 97; Kingston, 2013, p. 15).

government's slow response to the burst prolonged the economic predicament (Bordo, 2008, p. 16). Adding Japan's drop in productivity led to the 'lost decade', ten years of economic stagnation (Hayashi and Prescott, 2002, p. 220). In 2004, Japan's economy managed a return towards positive growth (Kevenhörster, 2010, p. 45). The world financial crisis in 2008, however, once again guided the country towards another period of stagnant growth, from which Japan has not fully recovered until today. Currently, Japan faces a severely aging population and thus a labor deficit, continuously high saving rates, high governmental debts, a need to raise consumption tax, and little increase in productivity (Feldstein, 2010, p. 1; Hoshi and Ito, 2012, p. 14). Additionally, every few years Japan has been shaken by natural disasters such as the Great Hanshin earthquake in 1995 and the tsunami in 2011 (Foljanty-Jost and Hüstebeck, 2013, p. 10). Albeit these challenges, Japan remains one of the world's biggest economies with an exceptionally high living standard (Flath, 2014, p. 1). Combined with the lack of workforce, the country becomes an attractive market to enter. The next chapter provides an overview of the most important market entry modes.

## **5. Institution and Market Entry**

When entering a foreign market, different influence factors can facilitate or impede the entry. Not simply the factors themselves but also their dynamics render certain modes of market entry more recommendable according to certain environmental and internal situations. One very important type of influence is institutions. Researchers have intensively explored how the institutional structures modify market entry possibilities. The most important concept from this research is the concept of legitimacy (Yui and Makino, 2002, p. 667). Depending on how well a firm is accepted by external and internal institutions, its market entry can go smooth or meet many obstacles. The first part of this chapter will describe how market entry modes can help gain different types of legitimacy. In the second part it moves on to explaining which type of legitimacy induces which type of entry mode. It will establish the first propositions on entry mode choice which will help later to decide which type a German consulting firm entering Japan should choose.

### **5.1. Institutional Influence and the Concept of Legitimacy**

When researching market entry modes multiple types of institutions need to find consideration. Intuitively the word institution describes governmental or other public

organizations. However, the word actually includes many more influential entities. Societies, interest groups, laws, professions, organizations practicing in the same industry, and also other unities within a firm expanding into a new market, such as the parent and sibling firms, are a few of the entities which categorize as institutions (Davis et al., 2000, p. 241; Oliver, 1991, p. 147). Their impact unfolds both in a useful as well as a hindering way. On the one hand, institutions create clear structures in an economy. Thereby, they reduce uncertainty. Governmental regulations facilitate contracting; societal values render business partners' behavior predictable. Thus, institutions reduce transaction costs (Meyer, 2001, p. 358). On the other hand, they shape the host markets environment in one way, yet concurrently develop the corporation's culture, its conduct of business and its employees' philosophies of life in a possibly very different way. When entering a foreign market, the company faces the clash of its own institution and that of the new location resulting in external as well as internal "isomorphic pressure" (Yui and Makino, 2002, p. 667; Davis et al., 2000, p. 242). Concerned internal and external institutions expect the new office to adjust. At this point, the theory of legitimacy takes effect. Dacin et al. (2007) define legitimacy as "a generalized perception or assumption that the actions of an entity are desirable, proper, or appropriate within some socially constructed system of norms, values, beliefs, and definitions" (p. 171). In order to legitimize a corporation, institutions expect a certain behavior. They provide the notion of right or wrong (Davis et al., 2000, p. 241). Sometimes the pursuit of legitimacy breeds inefficient strategies which firms are forced to accept (Yui and Makino, 2002, p. 670). However, it is their task to find a balance, how much to adapt to the host environment and how much to maintain its own business practices. Which part of its corporate culture can be kept and which part needs adjustment is to be decided. The larger the institutional difference the more difficult it seems to find the right path (Kostova and Zaheer, 1999, p. 71). Most researchers found, though, that external conformity is more essential than the internal one. Gaining external legitimacy not only facilitates the market entry but also stabilizes the companies' business in the new country. As a result, firms which build their competitive advantage on specific business practices face the biggest challenge (Xu and Shenkar, 2002, p. 614, Oliver, 1991, p. 149). Competitive advantage from special resource access or efficient usage, in contrast, has proved to be easier transferred (Oliver, 1991, p. 149). To find out which kind of institution emits which kind of effect, this chapter will categorize institutions according to their type of influence and list a few of each category's actors. The next chapter will then demonstrate which mode of market entry is most recommended according to which type of legitimacy.

Researchers distinguish three categories of institutional influence on the market entry mode and general international management. First, there is the “regulatory pillar” (Kostova and Zaheer, 1999, p. 69). It includes laws, rules and regulations. The main actors of this pillar are governments and other political institutions (Yui and Makino, 2002, p. 671). Typical means of guiding market entry are the lowering of tax rates and the abolition of performance requirements in order to attract foreign market entrants, and in contrast the selected emission of business licenses, the limitation of access to real estate and the prohibition of certain entry modes in order to distract foreign market entrants<sup>19</sup> (Meyer and Nyugen, 2005, p. 68). Another effective method is competition laws. The government can both loosen these to protect local businesses or strengthen them to avoid local cartels. Often, when strengthening them, not just foreign but also smaller firms profit by gaining an opportunity to enter and survive in the market and the general economy stabilizes (Kee and Hoekman, 2007, p. 856).

Another interesting fact about the regulatory pillar is that it not only guides entering firms, but it is based on reciprocal opportunities to influence. For example, many firms together may display a need for certain rules in order to facilitate their interactions (Meyer and Nyugen, 2005, p. 69). If the demand is articulated by a broad mass, the state may take required actions. Laws help to shorten contracts and the government can provide the necessary laws. Further, powerful firms tend to use lobbying in order to enforce their own interests (Meyer and Nyugen, 2007, p. 68). This shows the interplay of the regulatory pillar. Also, it is important to note that regulatory impact is not limited within one country’s borders. In case of the European Union (EU), the same regulations apply to several countries (Phillips et al., 2009, p. 342).

The regulatory differences between the host country and the hosted firm’s home country are comparably easy to notice, understand and interpret since they are usually in written form (Kostova and Zaheer, 1999, p. 69; Meyer and Nyugen, 2005, p. 70). Being the easiest to understand, they are also the easiest to determine whether a firm can oblige to them, or find a compromising way to bypass them; and what kind of market entry mode is possible.

The “cognitive pillar” (Kostova and Zaheer, 1999, p. 69) is concerned with what kind of behavior a society expects of the entering institution. Main actors of this pillar (and the normative pillar) are societies, peer-groups within and outside the company, interest groups,

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<sup>19</sup> As an example here, many countries do not permit IFDI with 100% foreign ownership, as it was the case in Japan in the past. In such a situation, the regulatory institution, here being the government, clearly rules out the possibility of setting up a WOS.

agencies and professions. Within a society a certain way of thought, certain practices as well as a set of background knowledge is taken for granted (Yui and Makino, 2002, p. 670; Phillips et al., 2009, p. 341). It is described by how people perceive their environment, make sense of it and then transfer their understanding into behavioral schemata (Yui and Makino, 2002, p. 671). The “normative pillar” (Kostova and Zaheer, 1999, p. 69) proceeds one step further and examines the congruence between the values a firm embraces, and those assumed by society (Kostova and Zaheer, 1999, p. 69). A group of people, here the members of a country’s society, share specific values, norms, beliefs and understandings (Yui and Makino, 2002, p. 670). The normative pillar examines to which degree the entering firm conforms to society’s expectations (Dacin et al., 2007, p. 176; Phillips et al., 2009, p. 341). The degree of conformity decides the degree of legitimacy achieved. A company entering a new country seeks to achieve the highest level of legitimacy possible. Hence, they must research about local values to fulfill the society’s expectations. The characterization of the normative and the cognitive pillar emerges from socialization and education (Kostova and Zaheer, 1999, p. 69). A corporation should thus be familiar with the local education system, traditions, and customs. To know these a profound understanding of the local culture is necessary. The firm has to overcome the psychic distance which the institutional differences create (Meyer, 2001, p. 360). Kostova and Zaheer (1999) conclude that the cognitive and normative pillar have a deeper impact on market entry than the regulatory one (p. 70).

The following chapter will draw up propositions which mode of market entry the regulatory, the cognitive and the normative pillar, respectively, induce.

## **5.2. The Three Pillars and Market Entry Mode**

This chapter will develop the first propositions how to choose a market entry mode depending on the type of legitimacy that is sought for, beginning with the regulatory pillar. As will be seen, not just the institutional gap but also specific laws and the market entry mode chosen by previous market entrants guide the method a market entrant should choose.

### **5.2.1. Regulatory Pillar and Market Entry Mode**

Most researchers have recognized the regulatory pillar as the least influential one which limits the research on specifically regulatory impact on market entry. Generally, companies will show conformity within the regulatory environment and abide by the law. Hence, legitimacy is comparably easily achieved, as described above. Yet, in case there are

ownership restrictions for market entrants WOS may become impossible (Xu and Shenkar, 2002, p. 614, Yui and Makino, 2002, p. 671). This narrows the corporation's number of choices.

*Proposition 1: Restrictions on ownership level for foreign entrants will limit the entering firm's choice of market entry mode.*

Generally, a smaller regulatory gap is favorable for companies. In this case, most business practices a company employs at home will also be legal in the entered market. Dacin et al. (2007) call this the "market legitimacy" (p. 172), which becomes easily attainable. The firm can choose an equity based mode of entry without too great a risk. In contrast, if the regulatory gap is wide the company should consider a market entry mode of low equity involvement. As mentioned above, obedience to the external environment is essential in market entry. Yet, if the local regulations contradict with the business practices which define the corporation's competitive advantage, and thus render it uncompetitive, they need to find a new way to achieve legitimacy. In this case, a joint venture may be helpful. The corporation can use the partner's market knowledge as well as legitimacy and avoid internal change (Xu and Shenkar, 2002, p. 614; Yui and Makino, 2002, p. 671).

*Proposition 2: Small regulatory distance suggests a wholly-owned or majority-owned market entry mode. High regulatory distance in contrast suggests the choice of a joint venture.*

Within the regulatory pillar, another factor of influence requires consideration. In recent years, academics have started to focus on the interdependency of entry mode and changing institutional environments (Meyer, 2001, p. 358; Meyer and Nyugen, 2005, pp. 74-75; Phillips, 2009, p. 340), mainly concerning the regulatory environment. On the grounds of the institutionalization theory, researchers moved away from the notion of legitimacy and concentrated on the resulting heightened transaction costs caused by institutional change. Therefore, the regulatory pillar has two ways of influencing the market entry choice.

The institutionalization theory examines how far along a country is in the institutionalization process, how institutional structures change and describes the features of the old and the new institution and the resulting change of influence (Tolbert and Zucker, 1996, p. 186). The moment of the institutionalization process contributes highly to the choice of a market entry mode. A country going through the process of institutionalization undergoes fundamental changes both on a normative level but especially on a regulatory level. A country's coordination system transforms into a new one. Transactions in the country are

loosely regulated. Both, external as well as internal participants are not yet familiar with the new environment. Stable laws and regulations are generally missing and law enforcement does not take place yet. Corruption easily spreads across the economy (Meyer, 2001, p. 358). Phillips et al. (2009) call this the “institutional uncertainty” (p. 340). This uncertainty strongly complicates a market entry in a foreign country and heightens the investment risk. A business used to clear cut rules and regulations and a protection of its business exchanges by law will especially struggle to succeed in a less regulated market. Therefore, institutional uncertainty affects institutional difference and its influence. (Phillips et al., 2009, p. 341) In addition, changing economies often focus on an internally successful economy which culminates in governments introducing laws which support and protect local companies (Meyer and Nyugen, 2005, p. 75). If firms enter countries with changing institutions they are best advised to choose a JV over a WOS. This way, they can reduce uncertainty and the entailed transaction costs (Davis et al., 2000, p. 245). They can avoid the interaction with immature rules and regulations and risky investments. Another important point is that lacking institutionalization leads to an uncertain market potential. Firms are generally willing to make larger commitments to markets with higher potential (Meyer and Nyugen, 2005, p. 74). Hence countries which are already institutionalized and built up a strong promising economy characterize a more attractive target for a WOS.

*Proposition 3: When entering a country going through the institutionalization process, a company should choose a JV as a market entry mode. The further the institutionalization has progressed the more likely becomes a successful WOS.*

As mentioned before, the regulatory pillar is recognized as the least influential one. The theory of institutionalization strongly supports this conception. A changing economy and fuzzy legislation force market participants to rely on cognitive and normative institutions in order to regulate their interactions. The following chapter will study the influence of the latter two pillars.

### **5.2.2. Cognitive and Normative Pillar and Market Entry Mode**

The cognitive and the normative pillar are a lot more difficult to grasp in comparison to the regulatory one. Thus, their influence is more complex. For the cognitive pillar most researchers came to the conclusion that the majority of firms choose to copy previous entrants' choice of mode and follow their pattern of success. Another idea was for the company to

repeat its own process of entry which it had chosen before for the same<sup>20</sup> or another country, respectively (Lu, 2002, p. 22; Yui and Makino, 2002, p. 672). In the cognitive pillar companies are mainly concerned with expected behavior. A known schema will be predictable for the hosting society and therefore appreciated. By repeating the behavior the corporation can be sure to fit in the societies' expectations and therefore gain legitimacy.

*Proposition 4: In a cognitive distant market, the need to fulfil the local market participants' expectations and thereby gain external cognitive legitimacy suggests to choose the same mode of entry other firms of the same industry have used in the past.*

The above described relations mainly concern external legitimization. In order to gain internal cognitive legitimization, firms can resort to choosing a form of strategic alliance. Finding a profitable alliance partner helps to convince other entities within the corporation to view the investment in the new country as efficient. Dacin et al. (2007) call this "investment legitimacy" (p. 177). They also define "alliance legitimacy" (p. 173). It is the goal for the entire company to accept the newly formed alliance as important, so everyone will contribute to its endurance.

*Proposition 5: The need for internal cognitive legitimacy suggests a JV as market entry mode.*

The normative pillar represents the most complex pillar of influences. Chapter 6 will look deeper into cultural effects on market entry mode choice which is part of the normative pillar. But this chapter will provide an overview of the combined influences by normative forces. As explained above, the normative pillar contains beliefs, values, understanding and the culture a group of people shares. This results in an even higher difficulty of balancing company wide and environmental legitimacy. As described above, companies need to weigh the importance of internal and external isomorphism. Businesses whose competitive advantage rests upon a certain business practice or the access to specific resources are compelled to stay internally consistent. In contrast, if customers are won separately from the mother firm, and R&D, as well as marketing, is conducted individually, the internal pressure loosens. Differences in language and culture, higher risks of selling and new ways of product usage intensify external pressure to adapt. Customers of the local market expect the corporation to communicate in their language and conform to their cultural values. This is the viable case for consulting firms. These being service firms depend on functioning networks

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<sup>20</sup> In this study only first-time entrants to Japan shall be regarded, which is why this pattern can be omitted.

and the local firms' trust (Glückler, 2006, p. 388). In this case researchers recommend a low-control mode of market entry (Davis et al., 2000, p. 252), in particular a joint venture (Yui and Makino, 2002, p. 671; Xu and Shenkar, 2002, p. 611). The market entrant can profit largely from the new alliance partner. Local experts can obtain or may have already obtained the needed degree of legitimacy and transfer this on the market entrant. Dacin et al. (2007) emphasize the importance of "social legitimacy" (p. 176) as well as "relational legitimacy" (p. 173). Social legitimacy describes the firm's need to be accepted by customers, interest groups and the public. Relational legitimacy hints at the need for further business partners to trust the market entrant. This is crucial for B2B business such as consulting firms conduct. Alliance partners can help the hosted corporation by sharing their own legitimacy and provide expert knowledge. The entering firm needs to learn about the local mind, respect the traditions, bow to norms and exert a certain behavior worthy the local expectations Meyer (2001) measure this as the "psychic distance" (p. 359). Normative institutions define the psychic distance between two countries. The smaller the psychic distance, the easier it is to train local staff, work with the local mentality and transfer the own knowledge. Yet, if the psychic distance is high, a JV facilitates the interaction. In addition, the company needs to overcome stereotyping and gain access into the group if the hosting country is a very ethnocentric country. It needs to alleviate the "liability of foreignness" (Dacin et al., 2007, pp. 173-176; Yui and Makino, 2002, p. 671), which further supports the choice of a JV.

*Proposition 6: High normative distance suggests a JV as efficient market entry mode. Low normative distance suggests a WOS.*

So far, cognitive and normative distances guide firms towards a low-equity, low-control entry mode. Nonetheless, there may be instances in which a company still favors a high-control entry mode. In the case a corporation pursues a global management strategy it cannot defer from, Xu and Shenkar (2002) have examined the choice between an acquisition and a greenfield investment and concluded the best choice is the latter. From an internal point of view, the confrontation of home country and host country workers with very different mentalities, as the normative gap is wide, can easily lead to conflict. Further, the local employees may not enjoy the change of business conduct as they are used to certain patterns on a cognitive level. And last, the acquisition entails a taste of loss and invasion which complicates the entry (p. 613).

*Proposition 7: Among high-control modes, high cognitive and normative distance, suggests to choose a greenfield investment above an acquisition.*

According to different premises, institutional differences suggest different types of market entry. Generally, high distance suggests low-equity over high-equity market entry and the cognitive and normative distance have a deeper impact than the regulatory has. Therefore, the next chapters take a further look at cultural differences and the notion of trust as a part of the normative pillar. Evaluating the seven propositions of this chapter and the propositions of the chapters to come, chapter 11 will determine which market entry mode realizes the minimum number of obstacles, taking the institutional differences of Japan and Germany into account.

## **6. Culture and Market Entry**

One critical factor to decide on a market entry mode is culture. In the past, academics have extensively discussed in what way culture facilitates or hampers certain types of market entry. There are theories which emphasize the national culture distance, some which focus on the organizational culture distance, and then others which stress the national culture of the home country. Before exploring the various findings, this chapter will first recapitulate the definition of culture and its dimensions. A broad description of the past empirical findings follows throughout which propositions are derived, under which circumstances what market entry mode is favorable. These propositions will serve as decision framework how the German consulting firm should enter the Japanese market.

### **6.1. National Culture - Definition and Dimensions**

First, it should be mentioned that culture is not defined by country boundaries. Values and traditions can vary within one country as much as they can be the same in several different countries. Nonetheless, people of the same country tend to think and behave similarly (Tihany et al., 2005, p. 270), so we can derive that culture is taught by the institutions around. Hence, this thesis examines the national culture assuming that the people of one country share the same culture.

In the past, most academics based their research in the cultural field on Hofstede's five cultural dimensions, "power distance (...), collectivism versus individualism, femininity versus masculinity, (...) uncertainty avoidance" (Hofstede and Hofstede, 2005, p. 23), and "long-term versus short-term orientation" (Hofstede and Hofstede, 2005, p. 31). However,

lately economists have questioned the accuracy of these and started looking for more comprehensive models. The Global Leadership and Organizational Behavior Effectiveness (GLOBE) project is one popular, very extensive cultural research project. Many scientists used this study which investigates whether culture can influence the type of leadership managers apply. It examines whether the type of leadership induced is especially effective or simply preferred by the actors of one country (House et al., 2002, p. 4). In several stages, the GLOBE project developed nine cultural dimensions, uncertainty avoidance, power distance, collectivism I (societal collectivism), collectivism II (in-group collectivism), gender egalitarianism, assertiveness, future orientation, performance orientation, and humane orientation (House et al., 2002, pp. 5-6). The first six of these were derived from Hofstede's model; the following ones go further beyond (House et al., 2002, p. 6). Being an extension of Hofstede's model and thus containing more details, the GLOBE project has often been utilized to test the results derived by adopting Hofstede's model. Interestingly, most results were confirmed, even if sometimes with a reduced significance (Estrin et al., 2009, p. 1181; López-Duarte and Vidal-Suárez, 2012, p. 2256). Additionally, most findings introduced in the following chapters are based on these five dimensions. In conclusion, Hofstede's model can still be taken as viable structure to study cultural frameworks. Hence, when exploring culture, this thesis will mainly focus on Hofstede's dimensions.

Hofstede distinguishes between national culture and organizational culture. He defines national culture as "certain patterns of thinking, feeling, and acting" (Hofstede and Hofstede, 2005, p. 3) which a specific group of people shares and thus uses to differentiate themselves from others. Culture contains among others shared values, traditions, mindsets, customs as well as way of thought (Tihany et al., 2005, p. 271). People are not born with but into a certain culture. They are taught by their surrounding institutions such as families, schools, friends and even the government, how to think, how to react, what to treasure in life and thereby grow into their surrounding culture (Hofstede and Hofstede, 2005, p. 4). Culture is known as a very steady system. It only evolves slowly from one generation to another (Ralston et al., 1997, p. 9). Hofstede subdivides culture into five dimensions.

### **6.1.1. Power Distance**

The first dimension is power distance. This dimension describes the relationship between superior and subordinate. It explains what kind of leadership style is used between the two. There is the autocratic/paternalistic form as well as the consultative form. In order to

determine which leadership style the superior can employ, the subordinate's mindset is essential. Superiors can only successfully lead in a way, subordinates accept to be led. Hence, the measure of how power distant a culture is mainly depends on the subordinate (Hofstede and Hofstede, 2005, p. 46).

If a country has a high level of power distance subordinates perceive their superiors to come to decisions without considering their subordinate's opinions. The subordinates are heavily dependent on the superiors' guidance but there is no reciprocal interaction. Often, subordinates are even scared of stating their mind. Along with this perceived autocratic style, there is a desired leadership style. Subordinates of high power distance countries either appreciate and promote this structure, or desire for the absolute opposite system, a democracy where the majority decides and not a single person (Hofstede and Hofstede, 2005, p. 45).

In a country of low power distance, superiors and subordinates interact far more in order to reach a decision. Superiors consult with their subordinates who in turn feel comfortable to state their own opinion. The system is based on mutual advice and dependence (Hofstede and Hofstede, 2005, p. 45).

### **6.1.2. Individualism versus Collectivism**

The second dimension distinguishes how people identify themselves, as individuals or as part of a group. In a culture characterized as collectivist, people learn to identify themselves with a group and to value this group. The first group they get to know is the family, including the extended family such as aunts, uncles and even housemaids. They later grow into new groups which they feel they belong to and which become their new in-groups. A feeling of integrity and loyalty is deeply rooted within the people. They are sure never to betray their in-group members. In terms of work, collectivism leads people to prefer working with in-group members. They only trust people they have integrated in their group to be loyal and valuable working partners (Hofstede and Hofstede, 2005, pp. 74-75). In addition, collectivist workers appreciate intensive training on the job as well as the opportunities to use the skills they have and acquire. Lastly, they treasure comfortable working conditions which may be attributed to the superiors who care about their subordinates as part of their group (Hofstede and Hofstede, 2005, p. 76).

In individualist cultures, people grow to focus less on the group around them and more on themselves as individuals. Except for their immediate family, their parents and brothers and sisters, they feel less need for loyalty towards other members of society (Hofstede and

Hofstede, 2005, p. 75). At work individualists treasure the chance to work at their own pace, have as much responsibility as possible and along the freedom choice and decision as well as the opportunity to challenge themselves. Since the only in-group they feel a sense of belonging to is the close family, they treasure their personal time outside of work (Hofstede and Hofstede, 2005, p. 76).

Looking at today's worldwide distribution of collectivist and individualist nations, countries with a national collectivist culture prevail (Hofstede and Hofstede, 2005, p. 79).

### **6.1.3. Femininity versus Masculinity**

The third dimension is the only dimension which produced a significant difference in answers between men and women which is why it was labeled femininity versus masculinity. Gender roles vary quite vastly between different countries. Jobs which are associated to be male dominated in one country are known to be a woman's job in another (Hofstede and Hofstede, 2005, p. 118), such as hair stylists are mostly male in Japan, while they are female in Germany. Yet, in all cultures certain character traits are attributed to being naturally female and others to being typically male. The female ones include the wish to take care, protect and make good relations with the people around them. This stems from women having been the ones to take care of the children and elderly from very early times. Men, in contrast, are on average more goal-oriented and challenging. Their past is focused on hunting and defeating their opponents (Hofstede and Hofstede, 2005, p. 117). Translated into a work environment, these characteristics make a female national culture more focused on the work environment. Workers of such cultures emphasize a good relationship to coworkers, successful teamwork, a workplace favorable for a comfortable family life outside of work, and a secure job. On the contrary, members of a masculine society treasure high wages, status, career opportunities, and chances to challenge themselves (Hofstede and Hofstede, 2005, pp. 118-119). In conclusion, female cultures are content if the professional life itself is enjoyable while masculine societies gain happiness from successful results of their work.

### **6.1.4. Uncertainty Avoidance**

The fourth dimension describes the people's uncertainty avoidance. It is a description of how well they cope with unknown or ambiguous circumstances. When a person stumbles upon a new situation which he has neither been in nor learned how to deal with, the person will experience a feeling of anxiety. How strong this feeling is, depends on his culture. People

adapt their level of uncertainty avoidance to their environment. They learn how much to fear the unfamiliar and how to react in the moment of confrontation. In order to reduce the ambiguous and the unexpected, people have installed laws and regulations (Hofstede and Hofstede, 2005, pp. 165-166).

Transferring this dimension to the professional life, there are several characteristics people of a highly uncertainty avoidant society share. First, they treasure their rules and regulations which help to decrease moments of anxiety. Second, they value their employment and will try to stick with one company as long as possible since it provides them with a sense of security and predictability. Third, in contrast to the former very positive point, they tend to experience a higher level of stress at their work place. Unexpected situations can never be completely canceled out. Thus, individuals who are inclined to feel tense in such instants will still feel a lot of pressure at work (Hofstede and Hofstede, 2005, p. 167).

#### **6.1.5. Long-Term versus Short-Term Orientation**

A few results from his survey, especially concerning Asian countries, Hofstede could not explain using the above described four dimensions. Hence, he later introduced a fifth dimension concerning long-term and the short-term orientation, respectively. It describes whether a person focuses on quick results or long-term effects of the actions he undertakes. Most Asian countries belong to the latter category (Hofstede and Hofstede, 2005, p. 210). People of long-term oriented cultures are prepared to show perseverance in all their doings over a long period of time in order to achieve a final, sustainable goal. They treat their disposable resources economically and are willing to put in all their effort to work towards their goal. If circumstances change and demand for adjustment they are quick to adapt. The future is the center of effort distribution. In contrast, short-term oriented cultures are much more concerned with traditions, upholding standards associated with their social rank and efforts being rewarded with immediate outcomes. The present and the past are the center of attention (Hofstede and Hofstede, 2005, p. 212).

After explaining the different dimensions of the national culture, the following chapter examines its influence of market entry.

## **6.2. Different Types of Culture and the Choice of Entry Mode**

Culture can benefit as well as obstruct a successful market entry. Therefore, it is crucial to consider cultural factors in order to choose an appropriate market entry mode. When expanding into a new market, a firm needs to manage internal cultural differences between local employees and expatriates, as well as external cultural differences between employees and customers. The latter has particularly gained importance throughout the last couple of years. Most developed countries experience an economic shift from the second towards the third sector, meaning expanding service industries which demand for a much closer interaction between personnel and clients (Hitt et al., 2006, p. 224). Hence, managers must prevent internal as well as external cultural conflicts.

Culture is usually seen more important than the regulatory framework of a country (Kostova and Zaheer, 1999, p. 70). As described in chapter 5.2.2, culture influences the normative as well as the cognitive structure of a country's institutions. These are known to be much more persistent than the formal regulations. Even though, laws and regulations in a society may be changed, it takes much more time to change all the society's members' personal views (Estrin et al., 2009, p. 1175; Hofstede and Soeters, 2002, p. 12). Thus, if a firm enters a market and conducts business in a way which does not comply with the local culture, it will be difficult for the company to gain legitimacy (Kostova and Zaheer, 1999, p. 69). A market entry requires adapting to local cultures and knowing customer needs (Hitt et al. 2006, p. 224). This can be achieved by hiring local staff, which may lead to the question of internal cultural conflicts, or learning about the local culture, which in turn can be difficult because of many invisible cultural traits (Estrin et al., 2009, p. 1175). In conclusion, culture amplifies management costs as well as uncertainty (Brouthers, 2002, p, 204). Furthermore, there is what Kostova and Zaheer named the "liability of foreignness" (Kostova and Zaheer, 1999, p. 73). Usually, when entering a foreign market, locals are not familiar with the entering business and tend to face it with suspicion. In order to gain a clearer idea about the firm, they resort to cultural stereotypes which can be beneficial or impede a successful entering. In any case, a foreign market entrant needs to overcome this suspicion and invest much more in convincing locals than a local market entrant does (Kostova and Zaheer, 1999, pp. 73-74). A corporation can achieve this for example by proving their social responsibility or by obtaining enough human as well as relational capital in order to blend in with the local society (Kostova and Zaheer, 1999, p. 74; Hitt et al., 2006, p. 223).

In summary, a foreign market entrant needs to choose a mode which helps to overcome cultural differences and agrees with the local as well as the home culture.

### **6.2.1. National Culture Distance and Market Entry**

Cultural distance measures the difference between two cultures (Mitra and Golder, 2002, p. 352). Many academics have examined the influence of cultural distance on the choice of market entry mode in the past. Interestingly, they came to different partly contradicting conclusions which have become known as the “cultural paradox” (Brouthers and Brouthers, 2001, p. 177). Some academics observed that a heightened cultural distance leads to the preference of a JV; others saw a relation to the choice of a WOS. Morschett et al. (2010) as well as Tihany et al. (2005) have tried to solve this paradox by testing past research for a result in one or the other direction. However, their results were insignificant (Morschett et al., 2010, p. 67; Tihany et al., 2005, p. 276), which emphasizes that no conclusive implication can yet be drawn. Tihany et al. (2005) emphasized that results may be distorted by moderators, such as the home country of the investing firm or the industrial sector the study was conducted in, and thus became insignificant (p. 277). López-Duarte and Vidal-Suárez (2012) conducted their own study and derived that cultural distance on its own has no clear influence on the choice of a market entry mode, yet if it coincides with another factor such as language distance or country risk it guides the company towards a certain mode (p. 2258). Pothukuchi et al. (2002) suggest it is necessary to examine the values of the single dimensions instead of a general national cultural value. For example, they found a positive impact of high distance in the dimension of masculinity on JV performance, and in contrast negative influences from all single dimensions on the staff satisfaction of a JV (p. 256). More importantly, however, the researchers found that it is crucial to differentiate between the national and the organizational culture in order to find reliable results (Pothukuchi et al., 2002, p. 246). It seems viable that cultural distance impacts market entry in different ways depending on the interaction with various environmental circumstances. To overcome this complexity, this chapter will give a broad overview over past research, first concerning JVs, and then WOSs, differentiating between greenfield investments and acquisitions. It aims to derive several propositions, which connect cultural distance with certain prominent objectives, and thereby later help to choose the most efficient entry mode for a consulting firm coming from Germany entering Japan.

### **6.2.1.1. Cultural Distance and Joint Venture**

There are various factors which support the choice of a JV as a market entry mode in case the cultural distance of the targeted market is high. This chapter will develop several scenarios in which a JV is the preferable mode of entry. In the end, it will conclude that the most important point is the need for a sophisticated understanding of and conformity with the local market.

First of all, one of the main uncertainties of a JV is finding the right partner, negotiating a resourceful contract and enforcing this contract. A low local country risk can reduce this uncertainty. The country risk describing national changes which influence the partner's behavior can endanger the long-term strategic alliance (Brouthers and Brouthers, 2001, p. 183). This risk being small, managers can more feel more at ease when choosing a JV.

The second factor is a high investment risk. If the political environment tends to change commonly, the economy is not stable and the cultural distance is high as well, the success of an investment is very unpredictable. The market entrant is confronted with many uncertainties. In this case, a flexible mode with less equity commitment, which allows a sudden exit, seems beneficial (López-Duarte and Vidal-Suárez, 2012, p. 2258; Brouthers and Brouthers, 2002, p. 207; Agarwal and Ramaswami, 1992, pp. 5-6).

*Proposition 8: High cultural distance and insecure foreign investments suggest a JV as market entry mode.*

One very important part of entering a foreign country is obtaining local market resources, one of these being market knowledge. This knowledge is a public good usually easy to access for local market entrants yet often difficult to fully understand for foreigners (Hennart, 1988, p. 371; Morschett et al., 2010, p. 61). Market knowledge includes information about economic developments but also about the local culture along with the needs as well as unacceptable business conceptions. One very efficient way of attaining this knowledge is a JV. The partner firm can contribute local expertise and handle critical situations (Tihany et al., 2005, p. 272; Makino and Neupert, 2000, p. 707). Besides, since this partnership is mutually wanted, the alliance partner will gladly contribute to a successful relationship by providing information and in addition try to avoid internal conflicts because of cultural differences (Kogut and Singh, 1988, p. 414).

The following benefactor concerns the liability of foreignness. As describes above, foreign market entrants are often confronted with unfamiliarity and suspicion. Especially, members of ethnocentric cultures are reluctant to easily accept new entrants. As a result, these companies become easy targets for interest-groups, such as environmentalists or human rights groups. A local partner with local popularity can help overcome this cultural hindrance (Yiu and Makino, 2002, p. 671; Kostova and Zaheer, 1999, pp. 73-74). By forming a JV the corporation not just gains market knowledge but also relational capital. Local clients will feel more comfortable conducting business with the new entrant when a familiar, trusted party is involved in the transaction. Thus, a local partner can be the fast and efficient way to attain a positive image (Hitt et al., 2006, p. 226). In summary, a JV can prevent external conflict. The market entrant engages in “external isomorphism” (Davis et al., 2000, p. 245), shows effort to adapt to the local culture and to conform to local rules. The firm tries to emphasize its social responsibility and can thereby gain social legitimacy (Dacin et al., 2007, p. 176). The JV partner unites the firm with the local market.

*Proposition 9: High cultural distance and the need for local expertise as well as external isomorphism suggest a JV as entry mode.*

On the contrary, high cultural distance can also complicate the formation of a JV. The first task is to gain internal legitimacy (Kostova and Zaheer, 1999, p. 67). If the partner conducts business very differently because of different cultural values, the two firms need to find a way to compromise. The second problem is the successful negotiation of and compliance with the contract. Different cultures embrace varying styles of negotiation and levels of trust. In addition, language barriers can greatly hamper communication and easily leads to misunderstandings or loss of information (López-Duarte and Vidal-Suárez, 2012, p.2258).

Furthermore, the transfer of knowledge can be greatly obstructed (Hitt et al., 2006, p. 226) in particular with varying degrees of individualism and power distance. Members of a very individualistic culture emphasize and retain information which concerns themselves. When analyzing received input, they look at the piece of information itself and tend to omit the context and contextual interpretation. They employ a very logical, rational and straightforward approach. In contrast, members of a collectivist culture focus on information which concerns the institution or group they belong to. When evaluating information, they always respect the context and look at the historical development, if possible. They use a very holistic approach to communicate. Additionally, they generally prefer to communicate with

in-group members. In terms of power distance, cultures which prefer strong hierarchies tend to exchange information solely among the top stages. In case concerned managers do not possess the necessary background knowledge to efficiently process the input, information may be lost. Similar levels of individualism and power distance may hence facilitate a successful JV (Bhagat et al., 2002, pp. 210-212).

*Proposition 10: High cultural distance and the need for a high level of internal legitimacy as well as extensive knowledge transfer suggest not choosing a JV as market entry mode.*

Last, when negotiating the contract of a JV the company must make sure not to reduce its desired flexibility. One of the reasons to choose a JV is the possibility of a comparably easy way to exit the market. If this becomes impossible and additionally the partner expects a certain behavior and thereby limits the corporation's free conduction of business, a JV may not be the optimal choice (Hitt et al., 2006, p. 226). Thus, the foundation and maintenance of a JV can be a daunting task.

In conclusion, although a JV has a few disadvantages, it is generally beneficial in a situation where cultural distance is high and strong external conformity and local market knowledge are needed.

#### **6.2.1.2. Cultural Distance and WOS**

Academics still dispute which market entry mode should be chosen in case of high cultural distance. This chapter will portray the opinions which support the choice of a WOS (López-Duarte and Vidal-Suárez, 2010, p. 585). It will conclude that the intensity of internal knowledge and competency transfer as well as internal orthodoxy is essential for successful business.

Many firms base their success on a competitive advantage derived from their business practices. When entering a new country, it is essential to transfer these competencies with as little distortion as possible. It is therefore crucial for employees in both countries to communicate and get along as unhindered as possible (Schwens et al., 2011, p. 344). Furthermore, the local employees need to accept the firm's traditionally successful critical patterns. When entering a culturally distant market, the local workforce's views and values may conflict the home business structure. Creating a WOS reduces this conflict and enhances the absorptive capacity for the essential knowledge (Morschett et al., 2010, p. 62). Sending

expatriates and using the gained control can help to implement the traditional business arrangements and maintain the competitive advantage (Tihany et al., 2005, p. 271). A functioning management which is trustable and knows the own business culture can try to integrate the home customs with local business practices and thereby to decrease the risks concerning a continuous successful business conduction (Hennart and Reddy, 1997, p. 10). This works particularly well with a greenfield investment since local staff can be chosen according to the desired culture and competencies (Xu and Shenkar, 2002, p. 613).

A WOS also deletes the problem of moral hazard which two partners in a strategic alliance need to take into consideration. First, the two firms need to negotiate the equity as well as the power distribution. After the contract was concluded, they need to make sure the partner attends his obligations. This does not exist in a WOS. Especially in case of a greenfield investment, the corporation does not even need to worry about unmotivated local staff or integration of the old workforce, which reduces the principal-agent dispute (Kogut and Singh, 1988, p. 414). Moreover, a WOS depletes the danger of information being disclosed. When working with a partner, sharing dire information is always critical. Essential knowledge might be divulged to third parties. Thus, a WOS can be a means to protect data contributing to one's competitive advantage (López-Duarte and Vidal-Suárez, 2012, p. 2253; Agarwal and Ramaswami, 1992, p. 20; Schwens et al., 2011, p. 344).

*Proposition 11: High cultural distance and the need for unobstructed, complete information transfer suggest a WOS as an entry mode.*

*Proposition 12: Among high control modes, high cultural distance and the need for unobstructed, complete transfer of information suggests a greenfield investments as market entry mode.*

A high country risk which forces the partner to take unpredictable actions also renders a WOS more beneficial. The company can react on it without having to account for the uncertainty of partner behaviors (Agarwal and Ramaswami, 1992, p. 6; Brouthers and Brouthers, 2001, p. 183). Furthermore, the language barrier also suggests a WOS. Speaking different languages may hinder the efficient communication between two partners. In a WOS instead, the company can make sure business is conducted the way the managers desire it to be (López-Duarte and Vidal-Suárez, 2012, p. 2258).

Lastly, an acquisition can be favorable in case the liability of foreignness poses a big obstacle for a firm. When acquiring a local firm, the buyer can use the local firm's reputation as well as the current employees' market knowledge (Kostova and Zaheer, 1999, p. X)

*Proposition 13: Among high control modes, high cultural distance and apart from high internal consent the need for external conformity suggest an acquisitions as market entry mode.*

There are, in turn, a few conditions, which render a WOS less preferable. Generally, it is more difficult to gain external legitimacy (Kostova and Zaheer, 1999, p. 67). While it is easier in case of an acquisition, since the local staff knows how to operate in the local culture, an acquisition often still carries the bitter taste of loss which may displease patriotic members of society. In addition, an acquisition usually implies that the firm continues to employ part of the local work force which can lead to the difficulty of knowledge transfer (Hitt et al., 2006, p. 227). The cultural difference between the home and the host office may continue to impede smooth communication. Furthermore, diverse cultures complicate the integration of the local management (Hitt et al., 2006, p. 228; Kugot and Singh, 1988, p. 414; Schwens et al., 2011, p. 333) as well as the motivation of the local staff (Hennart, 1988, p. 372). Different values require different incentives, different perception of power distance requires different types of hierarchy, and different customs require different types of communication. These points provide further support for *Proposition 12*.

A greenfield investment, on the other hand, challenges a company to gain all the knowledge about the local market on its own (Hitt et al., 2006, p. 228) and additionally have very limited access to public goods (Hennart, 1988, p. 371). This further underlines *Proposition 13*.

Estrin et al. (2009) describe the impact of culture depending on the degree of distance in an arch. First, when the cultures of two countries are fairly similar, one can choose a strategic alliance or an acquisition as market entry mode. It is fairly easy to integrate internal divisions and at the same time, the company can enjoy the benefits of the locally experienced partner. With increasing cultural distance, the internal integration becomes more difficult which guides the market entrant towards a greenfield investment. If, however, the cultural distance reaches the point, where the foreign company, albeit great efforts, is not able to access local resources, tangible as much as intangible, it should move back to a partnership

(Estrin et al., 2009, p. 1176). In summary, the effects of high national cultural distance vary according to additional conditions and goals.

### **6.2.2. Organizational Culture Distance and Market Entry**

Lately, more voices call for the inclusion of the organizational culture in the examination of cultural distance (Pothukuchi et al., 2002, p. 246, Estrin et al., 2009, p. 1177). In contrast to the national culture which builds on values, morals and ideals, organizational culture focuses on “symbols, heroes, and rituals.” (Hofstede, 1994, p. 9) Hence, it influences how a company conducts business, what their goals are and whom the management portrays as ideal worker, whom they choose as role model. Organizational culture works independent of national culture (Pothukuchi et al., 2002, p. 257). Up to a certain limit, it varies within one country, which is why we can find various organizational structures within one nation. Nonetheless, organizational culture bears certain tendencies within one country. A good example is the HR system which is likely to contain certain features across one nation, as will be demonstrated in chapter 9.8.2. Countrywide tendencies exist due to the fact that organizational culture is mainly shaped by the top management which belongs to a certain national culture and chooses a business structure which fits their values and ideals (Kogut and Singh, 1988, p. 414). Yet, naturally the structure must also correspond to the employees’ ideas, since they can join an organizational culture voluntarily. As a result, the organizational culture is based on the management’s concept within certain boundaries set by the workforce. Thus, an MNC can take their organizational culture to another country, but they might have to overcome certain obstacles (Hofstede, 1994, p. 9; Ralston et al., 1997, p. 8).

The organizational culture plays a big role in case of a JV. If the two business cultures are very different, it becomes more difficult to communicate and to integrate business procedures. Similar to the national culture, varying corporate cultures can lead to misunderstandings and complicate decision making. Especially, different HR structures obscure which hierarchical levels should exchange information, who has the decision making power, how independently lower hierarchical levels can operate and how often employees change positions which confronts the JV partner with a new correspondent to work with. In short, different HR systems can hamper strategic alliances (Ballon, 1992, p. 129). A greenfield investment would be a good option to overcome this obstacle since no integration of home and host country staff is required (Estrin et al., 2009, p. 1177).

*Proposition 14: Extensively varying organizational cultures, and particularly HR structures, suggest a greenfield investment as market entry mode.*

### **6.2.3. Home Country's National Culture and Market Entry**

As much as cultural distance matter, the home country's culture can also predispose a preferable market entry mode. In case, the home country is characterized by a very power distant culture, companies tend to favor strictly hierarchical structures. Hierarchically high positions are supposed to be in charge of decision making which yields a centralized power of decision (Morschett et al., 2010, p. 62; Makino and Neupert, 2000, p. 706). This system hints at a WOS as a market entry mode. The mother firm can keep tight control of the subsidiary and plan and organize it in sync with the original company.

*Proposition 15: A power distant home culture suggests a WOS as market entry mode.*

The second highly influential cultural dimension is uncertainty avoidance. Corporations acting according to this stigma prefer clear structures and written rules. Tight supervision provides a feeling of being able to manage the unexpected. A central management can react in case of unpredicted market changes (Kogut and Singh, 1988, p. 424; Makino and Neupert, 2000, p. 706). This dimension, too, proposes a WOS as entry mode.

*Proposition 16: An uncertainty avoidant home culture suggests a WOS as market entry mode.*

The chapter about cultural influences on market entry concludes with the result that the types of influences are manifold and it is not easy to examine culture on its own but in interaction with other factors. The derived eight propositions will guide the analysis which market entry mode a consulting firm should choose from a cultural point of view. The next chapter will detail findings about trust and market entry mode choice.

## **7. Trust and Market Entry**

The third factor discussed in this paper, which contributes to the choice of entry mode is trust. Doney et al. (1998) "(...) define trust as a willingness to rely on another party to take action in circumstances where such action makes one vulnerable to the other party." (p. 604) Trust describes the faith one has, the other will behave in one's best interest, will refrain from exploitation, assist in times of need, put in their best effort, keep their promises, and to display

consideration and honesty at all times (Doney et al., 1998, pp. 603-604; Yamagishi and Yamagishi, 1994, p. 131). Trust allows two companies to show their weaknesses since they can expect benevolent behavior from each other (Huff and Kelley, 2003, p. 82; Doney et al., 1998, p. 603). It renders the partner's behavior more predictable. A company can trust the other to choose the best option and thus forecast their actions (Sako, 1998, p. 5). While greenfield investments do not require any trust, business alliances can benefit greatly from the faith two partnering firms have in each other. Transaction costs are reduced, capabilities enhanced, and relationships prolonged. Barney and Hansen (1994) have defined three different types of trust, the weak form, the semi-strong form and the strong form (p. 177). If a firm manages to form a business alliance based on the strongest form of trust, it will gain access to important resources, social capabilities, transaction cost benefits, and ensure a long-lasting collaboration. Hence, a trust-based business relationship is very desirable. In business terms, building a trusting relationship can be depicted as an investment which bears a certain risk but promises high returns on investment in the end (Sako, 1998, p. 6). In the case of a consulting firm entering a foreign market, the question of trust becomes especially interesting. In order to conduct successful business, it is essential for consulting firms that their customers trust them. A company seeking advice will only choose a consultant they trust. Therefore, trust between the firm and its client is of the highest priority. Generally, people trust the known rather than the unknown. Thus, if a German firm enters the Japanese market, the company can facilitate its entry by forming a strategic alliance or acquiring a local company. The Japanese organization can then help to gain the client's trust. Therefore, in contrast to the previous two chapters, rather than examining which entry mode trust suggests, the following paragraphs will try to find out which mode trust renders possible. With no trust involved, a greenfield investment seems best, since there is no risk of exploitation. However, in case a firm aims for another form of entry, trust can reduce costs as described below.

This chapter starts by presenting the benefits of trust, continues by describing different levels of trust and how to achieve them, and end with an elaboration on the interaction of trust and culture.

### **7.1. The Benefits of Trust**

The benefits of trust have been examined under various theoretical approaches. The first and most common approach is the theory of transaction cost economies. When entering an alliance with a firm, the two parties involved both risk being exploited. Information

asymmetry paves the way for adverse selection, moral hazard and hold-up problems (Yamagishi and Yamagishi, 1994, p. 136). To avoid these, the companies need to draw up contracts which include behaviors, permissions, prohibitions, and guidance for certain situations. However, these contracts tend to become lengthy, expensive and are hardly ever fully comprehensive (Ireland et al., 2002, p. 427). A solution to these risks is trust. When two firms trust each other, there is no need for extensive contracting. Firms can risk revealing their own vulnerabilities without having to fear being exploited. This enlarges the number of possible partnering candidates. All those transactions, which are impossible under non-trusting circumstances since contracts are insufficient to eliminate all exploitation opportunities, turn into possible scenarios. At the same time, loose contracts enable firms to maintain a certain flexibility to react to market changes and adapt to environmental developments (Gulati, 1995, p. 107). Furthermore, trust enhances the quality of information delivery. Believing in the partner's reliability lets the informant speak freely which helps an elaborate communication and supports the correct factual transaction (Katsikeas et al., 2009, p. 134; Griffith et al., 2006, p. 22). This effect is especially large in case of interdependent resources (Luo, 2002, p. 677). Trust stabilizes and facilitates a business alliance (Parkhe, 1993, p. 307). It contributes sustainability and is most suitable to a long-term project (Yamagishi and Yamagishi, 1994, p. 132). A trustworthy partner grants a sense of security which both parties will try to maintain. Once a trusting relationship the costs of losing this relationship become very high. The return to non-trusting, often short-termed alliances is a great fear for businesses (Yamagishi and Yamagishi, 1994, p. 138). They prefer the security, which entails several advantages. To keep their partner, companies show willingness to commit and to adapt to their preferences (Yamagishi et al., 1998, p. 171). Simultaneously, the partner is prepared to guide and support the company's adjustments (Larson, 1992, p. 96). A customized business exchange for the two particular firms develops. Usually, the change of business as the partnering firm demands entails lower costs than changing partners, which is why alliances generally consist of mutual adaptations and fast resolutions of difference of opinions (Ring and Van de Ven, 1994, p. 98). Also, the desire to continue joint business in the long run motivates companies not simply to fulfill the partner's expectations but to exceed them (Larson, 1992, p. 96). Hence, trust may lead to enhanced performances. Concurrently, monitoring costs are lowered or eliminated since both firms can rest assured of the other's efforts to contribute successfully (Madhok, 1995, pp. 120-121; Sako, 1998, p. 6). The last advantage in relation to the sense of security is the assurance that a firm has a partner company to rely on in times of crisis. As a result, both firms are able to conduct investments

of higher risks which promise high returns (Sako, 1998, p. 7; Luo, 2002, p. 677). Another interesting product of trust is that a professional business relationship often transforms into a personal one. A kind of friendship develops which renders the alliance even more valuable and the trust even more profound. Inhibitions to end transactions are raised dramatically (Ring and Van de Ven, 1994, p. 7). In conclusion, trust can reduce transaction costs and secure a long-lasting, non-exploitative relationship.

Another approach to analyze trust is from a social capital dimension. In a business alliance two firms are bound to share delicate information. It is absolutely essential for the two parties to be able to be sure that the partner will not leak any facts to a third party. Firms will only be willing to engage in knowledge exchange if they can trust their partner will handle the received data confidentially. Therefore trust is indispensable for a successful business alliance (De Wever et al., 2005, p. 1534). A similar view emerges from the social network theory. Finding long-term partner corporations reduces social uncertainty. Once two firms found each other, they will work hard to continue the relationship since fewer new acquaintances equal decreased risk (Yamagishi et al., 1998, p. 171). In order to build up a wide and well-functioning network, a firm needs many companies to put their trust in them. Having achieved this goal a firm attains access to a wide-range of information which can help to develop their skills and strategies. Complementary capabilities leverage firms to unimagined competitive advantage (Wu et al., 2008, p. 534-535, Katsikeas et al., 2009, p. 146). In addition, as further explained below, a well-developed social network can help convince more firms of one's trustworthiness, and thereby further widen the network (Wu et al. 2008, p. 535; Li, 2008, p. 427; Trapscott, 2006, p. 2; De Wever et al., 2005, p. 152). Trust triggers an upward spiral possibly leading firms towards fast and great success.

The following approach, which will be explained in most detail, is based on a resource-based view. It is a very import concept, since it explores the sharing of information and the resulting advantages, one of the major goals of service firm entering a business alliance.

## **7.2. Three Forms of Trust**

Researchers suggest there are three types of trust, the weak-form, the semi-strong form, and the strong form (Barney and Hansen, 1994, p. 177). The following chapters will examine,

which level of trust can be achieved in what manner, so that later analysis can derive which entry mode is attainable for a German consulting firm expanding to Japan.

### **7.3. The Weak Form of Trust**

The first form of trust is the weak form. It describes a situation where both partners of a transaction have no possibility of exploitation. Therefore, they can trust each other. Such an environment might establish in a highly competitive market. The resources the two firms share are not rare, easily accessible, and can be attained from relationships with various different corporations. Usually, in case of a business alliance, the competitive advantage gained is not as big, yet favorable for the two parties. If one party chooses to behave opportunistically, and betrays the partner's trust, the partner can easily form an alliance with a different party and end the relationship. In other words, there is no reason for either firm to behave in an untrustworthy manner. The resource at stake is not exclusive enough to render a betrayal profitable. The second situation, in which such an endogenous form of trust is established, occurs in case the quality of the exchanged information is easily verifiable. In this case, the two transaction partners can avoid information asymmetry (Barney and Hansen, 1994, p. 177). If both parties share the exactly same amount of knowledge, trust is automatically entailed. In summary, the weak-form of trust is endogenous. The environmental circumstances induce trust. However, as soon as these change, the trust triggering setting disappears and the relationship based on trust is over (Li, 2008, p. 420). In case of a consulting firm, the situation of perfectly observable resources or an extraordinarily high competitive market are both unlikely, which is why the weak-form of trust will not be further regarded.

### **7.4. The Semi-Strong Form of Trust**

The semi-strong form of trust is just as the weak-form endogenous (Barney and Hansen, 1994, p. 178). It describes a situation where trust can be induced by governance. There are three types of governance which can assure two transaction partners of each other's integrity. The first is market-based governance. In order to be successful in a market, firms require a good reputation and a functioning network. If a firm once decides to show betraying behavior, this network may suffer severe damages (Trapscott, 2006, p. 2). The new negative image can easily prevent the firm from future business offers (Gulati, 1995, p. 93). Firms enjoying a wide network will therefore refrain from unfaithful behavior (Barney and Hansen,

1994, p. 178). The fact that in today's society of informational technology, news about companies spread all around the world in an instant, market-based governance's effect is comprehensive and sustainable (Trapscott, 2006, p. 2).

*Proposition 17: Market-based governance suggests the possibility of a JV.*

The second kind of governance is a contract. A contract can include both desired behavior as much as prohibited behavior for the time of the partnership (Barney and Hansen, 1994, p. 178). However, this kind of governance seems questionable, since contracts are incomplete. They cannot contain every possible scenario and the wider they are, the more expensive they become. A solution to such high costs may be to create hierarchical structures (Barney and Hansen, 1994, p. 179).

*Proposition 18: Contractual governance suggests the possibility of an acquisition*

The last form of governance is social governance. This kind of governance is intertwined with culture. In case, in a society, the betrayal of a partner's trust (either the betrayal itself or the actions taken in order to break the trust) is viewed upon as immoral and socially and ethically unacceptable, the partner may refrain from dishonesty (Barney and Hansen, 1998, p. 178). Again, the reputation of company contributes to the argument. This time, it is not the image on a business level, but the image on a societal level which suffer damages. The negative reputation can lead to sabotaging clients, opposition by interest groups or again missing business offer. As can be seen, market-based and society-based governance are tightly intertwined (Barney and Hansen, 1994, p. 178). As society's views do not change quickly, societal governance can also be recognized as a lasting opportunity.

*Proposition 19: Society-based governance suggests the possibility of a JV.*

## **7.5. The Strong Form of Trust**

The third form of trust is the strong form. It is the highest and most sustainable level. In contrast to the previous two categories, it does not emerge from certain environmental settings (Barney and Hansen, 1994, pp. 179). It is based on the belief of two firms that it is right and necessary to conduct sincere business. It relies on moral behavior and personal principles (Li, 2008, p. 420). In such a relationship, both parties highly value trustworthy behavior. They will take the partner's interests into consideration and refrain from exploitation. Both firms have vulnerabilities but treat them openly, since they are certain the

partner will not take advantage of the situation. The trust is deeply embedded in both minds. Therefore, the trust will last throughout several different business exchanges and not simply one transaction. Environmental changes have no impact on the trustworthiness of either partner, which imparts a sense of security to both parties and thus motivates them to contribute earnestly to the partnership. The trust is exogenous (Barney and Hansen, 1994, p. 179). One difficulty of forming a strong form trust relation is the number of people involved in a business exchange. While it appears rather easy to develop trust between two single persons (Yamagishi and Yamagishi, 1994, p. 137), in case of two companies joining business, a great number of individuals need to trust each other (Barney and Hansen, 1994, p. 180). Therefore, a firm must find a mean to induce trustworthy behavior among its staff which ascertains its opposite company and motivates them to reciprocate with the same sincere behavior. One way of convincing employees is the leadership method. The leader should act as a virtuous role model whom the staff can follow (Li, 2008, p. 429). This works especially well in group-oriented societies. Individual employees are interested in developing a good relation with peers and superiors. Therefore, they are ready to adapt their behavior and conform to the moral principles acted out within the company. Another method is to set incentives. Leaders can reward trustworthy behavior which motivates subordinates to put effort into sincere business (Barney and Hansen, 1994, p. 181).

The strong form of trust is neither dependent on establishing some form of governance, nor does it rely on other environmental settings which cancel out options of opportunistic behavior. It is durable and profound. As long as the morally sincere mind-sets of the companies do not change, the trusting relationship does not face the risk of an end. Both corporations share a strong interest in maintaining the alliance since the costs of finding such a business partner are high. Both partners must truly honor each other's trust and resist chances of opportunistic behavior (Madhok, 1995, p. 121). In the past, researchers have found four effective ways to build a relation of trust. The most secure way is passing time. Continuing business relationships let two firms gain experience. They get to know each other, collect information about each other, verify whether their interests and their moral principles match, can slowly start to engage in transactions bearing vulnerabilities, and thus develop a partnership of trust in the long run (Ireland et al., 2002, p. 439; Gulati, 1995, p. 92; Bachmann and Inkpen, 2011, p. 285). Joining forces to conquer obstacles connects two companies (Sako, 1998, p. 11). However, usually market entrants do not have the opportunity of starting with a superficial business exchange entailing only small vulnerabilities on each side. They need to

find other ways to show a targeted firm that they are trustworthy, and at the same time, decide parameters to evaluate the potential partner.

The second path, researchers have suggested is to show four key values of trust, which are “honesty”, “accountability”, “consideration of others’ interests”, and “transparency” (Trapscott, 2006, p. 1). Signing a contract in advance and similar signs of commitment show a firm’s commitment (Barney and Hansen, 1994, p. 187). Flexibility, forecasting and integration of the partner’s wishes, honoring the other party’s requests, and adapting to their needs demonstrates consideration of the other’s interests (Wu et al., 2008, p. 535; Li, 2008, p. 427; Das and Teng, 1998, p. 505). The constant delivery of high quality reassures the partner (Sako, 1998, p. 2). Open communication is most essential to prove honesty and transparency. Correspondence helps to clarify both sides’ interests, their plans for the future, and their world view. It is a good mean to avoid misunderstandings. Communication additionally assists to early uncover discontentment on either side, which both parties can then work to improve (Das and Teng, 1998, p. 504). Lastly, openness towards auditing contributes to show one’s sincerity (Barney and Hansen, 1994, p. 187).

Another important sign of trustworthiness is reputation (Wu et al. 2008, p. 535; Li, 2008, p. 427; Trapscott, 2006, p. 2; De Wever et al., 2005, p. 152; Bachmann and Inkpen, 2011, p. 285). When looking for a partner firm, it helps to examine his network and research whether other companies affirm the firm’s trustworthiness (Das and Teng, 1998, p. 504). The more corporations vouch for a potential partner’s sincerity, the higher are the chances the company is actually trustworthy. Yet, one has to keep in mind reputation is not a perfect proof of trustworthiness. An enterprise might pretend to be trustworthy and behave accordingly until a highly profitable opportunity of exploitation opens up. On the other hand, the longer the company conducts business, the less likely it is it will pass by opportunistic possibilities. Every time, it lets such a chance slide, it has to account for the resulting losses. In contrast, a firm which does not believe in opportunism and exploitation of other firm’s vulnerabilities does not take possible wins from betrayal into account, and hence does not bear any losses. Thus, only trustworthy companies can continue non-exploitative behavior over a long period of time without regretting great losses (Barney and Hansen, 1994, p. 187) In conclusion, the more sincere business transactions a firm has conducted in the past, the more likely it is for it to be trustworthy. Every corporation should therefore try to build up a wide social network in order to signal trustworthiness. At the same time, it should of the partner candidate’s business

relations (Li, 2008, p. 428). Reputation is a suggestion but not a proof of a firm's trustworthiness<sup>21</sup>. Another indicator can contribute certainty.

Academics have found one more efficient mean to induce trustworthiness. Putting faith into a relationship and showing one's own trust trigger a feeling of responsibility and the wish to reciprocate within the potential partner firm (Das and Teng, 1998, p. 503). Sharing delicate information and slowly revealing one's vulnerabilities might motivate the partner company to uncover its own weaknesses (Ireland et al., 2002, p. 439; Sako, 1998, p. 14). This notion also applies to networks. Companies joining a web of trusting relationships, experiencing the faith other firm have in them, may feel more willing to participate in free communication (McDermott and O'Dell, 2001, p. 82).

When considering which kind of trust relationship a firm desires to establish with its potential partner, the company should compare the costs of introducing a type of governance and those of finding a trustworthy partner. One must note, though, that the sustainability of strong-form trust bears obvious advantages. It opens doors towards a long-lasting alliance.

*Proposition 20: The strong form of trust suggests the possibility of a JV.*

Having established four proposals concerning trust, the task now is to find out what kind of trust is most likely to occur in Japan and Germany. In case both countries' members are willing to trust strangers a collaborative entry mode would be facilitated. If, in contrast, mistrust prevails, a joint venture would be greatly impeded (Ballon, 1992, p. 125). Whether trust is possible is substantially dependent on the two country's cultures. As the next chapter will present, trust and culture are closely intertwined.

## **7.6. The Interaction of Trust and Culture**

The notion of trust is perceived quite differently in Japan and Germany; how fast one can trust, how sustainable trust is, in which situations trust is required. To find out how likely Japanese are to trust in Germans and vice versa, this chapter will examine the trust behavior induced by culture. Chapter 10 will then highlight some country specific aspects of trust.

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<sup>21</sup> Interesting to note here is that building up reputations and a wide network has changed during the last decades. While in the past, many long-term alliances were established over time, the fast moving markets, the high mobility, the rapidly changing environment, and the fast distribution of information forces firms to trust faster. The reliance on a well-established reputation is not as easy as in the past (Yamagishi and Yamagishi, 1994, p. 138).

Whether two firms enter an alliance is heavily dependent on the individuals' position towards trust. The management may try to induce trustworthy behavior, yet a generally trusting mindset facilitates an alliance significantly (Huff and Kelley, 2003, p. 82). In order to inspect the interaction between culture and trust, Hofstede's dimensions function as basic principle. The first dimension is power distance. High power distance indicates a society of low trust. In a firm where everyone puts in their best effort without much supervision, strong hierarchies would be redundant (Shane, 1994, pp. 628-629). Thus, only a corporation which needs to keep a strict eye on its employees should automatically lean towards high differences in power. In such an environment, the staff will do as told until a chance of opportunistic behavior opens up, which they will be sure to take. Trust among colleagues, as well, is comparably low and in case a situation of dissatisfaction occurs, workers do not shy away from confrontation since they do not have a trusting environment to lose (Doney et al., 1998, pp. 612-613). If, in contrast, the power distance is low, workers and management collaborate on a friendlier level. Every individual is treated as equal and tries to contribute which leads to trust towards subordinates, coworkers, and superiors. Supervisors feel less need to establish strict rules or to exhibit their power (Doney et al., 1998, pp. 613-614; Shane, 1994, pp. 629-630).

In terms of feminine and masculine cultures, members of the feminine one are more likely to trust. They believe in a harmonious, supportive attitude. Masculine cultures, in comparison, emphasize individual success. They would only commit as long as their own profit is secure. Hence, members must expect their partners in business to take exploitative opportunities. Trust is less easily established (Doney et al., 1998, p. 610).

High uncertainty avoidance also indicates trust to be easily accomplished. First, individual who fear the unknown will put their best effort into maintaining their relationship. They prefer to collaborate with opposites they know. In addition, their risk avoidance narrows their behavioral choices, which makes them predictable. Low uncertainty avoidance displays the opposite effect. They do not shy away from short-term alliances and have a wide variety of choices which action to take (Doney et al., 1998, pp. 614-615). Thus, high uncertainty avoidance indicates high between two avoidant societies and low trust, as soon as individuals of low uncertainty avoidance are involved.

The dimension of collectivism and individualism seems to be the most important as it has been the most mentioned in the literature. Collectivistic cultures are known to be more trusting (Doney et al., 1998, p. 610). Individuals of such societies are used to consider other

people's benefits and to work for the group's good. Whether this is an inherent way of thought or their behavior results from the fear of being expelled from the group they belong to (Huff and Kelley, 2003, p. 84; Shane, 1994, p. 628) varies among individual persons. Nonetheless, their behavior induces trust. Peers can be sure an individual will be honest and act in their best interest. They will let any exploitative opportunity pass by (Shane, 1994, p. 628). In a business alliance instead of detailed written contracts, relational contracts are deemed superior (Gelfand et al., 2004, p. 457). Members of individualistic cultures, in contrast, focus on their own benefit. Opportunistic behavior is more likely to occur (Doney et al., 1998, p. 610; Gelfand et al., 2004, p. 457). The collaboration with a firm of a collectivistic culture thus seems perfectly preferable. However, the trusting behavior of collectivistic people only applies to their own in-group. In contrast, if out-group members are involved, they develop strong suspicion (Yamagishi et al., 1998, p. 166). On the one hand, they fear a lack of integrity from members of an individualistic culture. On the other hand, the sanctioning mechanisms, inducing conform and committing behavior, do not apply in a scenario involving an out-group (Huff and Kelley, 2003, p. 86). Yet, if an out-group member manages to develop into an in-group member, he will easily gain the entire group's trust (Griffith et al., 2006, p. 7).

Gaining trust, especially between firms of different origin, is a daunting task. Understanding the thoughts and expectancies of the party can help to comprehend what behavior to display and what to communicate in order to facilitate the development of trust. This chapter has presented how the strongest form of trust benefits business alliances the most, the most important means which support trust, and how culture, in particular the dimension of collectivism and individualism, drastically influence trust. The following chapters will now study the institutional, cultural, trust-based features of Japan and Germany in order to support the concluding analysis.

## **8. The Institutions of Japan and Germany**

This chapter is going to introduce the institutional systems of Japan and Germany. For a smooth analysis of the impact of institutional differences, which are divided into regulatory, normative and cognitive, this chapter focuses on the regulatory parts of institutions. The normative and cognitive will be covered in the chapters about Japan's and Germany's culture and their perception of trust. Hence this chapter first provides a rough overview of Japan's political structure, the main actors of law making and its economic policy. It continues with

an introduction to the German political outline and its economy. The chapter concludes with an immediate comparison of the two systems and finds Japan and Germany to be similar in terms of institutional characteristics.

## **8.1. Japan's Institution**

First, the chapter will describe Japan's institutional set-up. This should help to compare the Japanese to the German political and economic organization as well as introduce regulations impeding to foreign market entrants. After a general description, the special interconnection between government, bureaucracy and companies as well as the Japanese law will be the points of focus.

### **8.1.1. Political Structure of Japan**

Japan's political structure is a parliamentary monarchy and very similar to the British system. The head is the emperor, the so called *Tennō*, however his role is merely representative; he possesses no political power. The legislative is called the diet. The diet consists of the upper house, the house of councilors (*Sangiin*), whose members are elected for six-year terms, and the lower house, the house of representatives (*Shugiin*), whose members are voted for four-year terms (Gauder, 2011, p. 4; Yamamoto, 2014, pp. 172-173; Kevenhörster, 2010, p. 239). One of their main tasks is policy drafting. For this, they closely work with the bureaucracy, who provides information about reforms needed. If the two houses are in conflict over a bill, usually the upper house holds the superior power (Fukai and Fukui, 2004, p. 227; Yamamoto, 2014, p. 172). The lower house, on the other hand, elects the Prime Minister. He and his cabinet make up the executive. Their main task is the adoption of laws. The Prime Minister also has the power to dissolve the lower house. Further power and influence even on the legislation he gains from his extensive network. The Prime Minister usually fosters close relations not just with his own party member but also with members of the bureaucracy which helps him to indirectly impact policy making. However, lately, due to inner-party conflicts the support for Prime Ministers within their own party has been lacking which resulted in frequently changing Prime Ministers (Kevenhörster, 2010, p. 239; Gauder, 2011, p. 4; Yamamoto, 2014, p. 174).

Today's institutional framework of Japan was established according to foreign models. The first Western influence started during the Meiji period when Japan's politicians and political advisors travelled to Europe and started to import ideas. Japan wanted to authenticate

their modernity and their position in world politics. Hence, Japan became the first East Asian country to introduce a voted parliament. Concurrently, the government at the time tried to impart a very strong feeling of patriotism to its people. A sense of national identity flooded Japan which incorporated deep admiration and absolute recognition of the emperor, who gifted his people with a constitution, as well as the adaption of Confucian beliefs. This strong kind of nationalism entailed skepticism towards foreignness. A controversy developed in Japan. On the one hand, the Western political system was idealized and partially imitated, which led Japan to its very unique structure being a mix of national traditions and foreign modern standards, yet simultaneously national pride triggered a conviction of Japan being superior to other countries. The government, nonetheless, made good use of this unquestioned trust later, as for example it served as justification to engage in warfare. (Kevenhörster, 2010, pp. 238-247; Er, 2014, p. 16) In current society in contrast, politicians try to alleviate this mistrust towards foreignness, as much on a political as on an economic level. It starts with intensified exchange of students and young politician, through the strengthened attraction of IFDI, and reaches as far as efforts towards a permanent membership of the United Nations Security Council (Kevenhörster, 2010, pp. 349-350; Ministry of Foreign Affairs of Japan, 2014). During these efforts parliament will continue to struggle with the reconciliation of national identity and acceptance of foreignness.

The members of parliament are elected from various parties. It is important to note that the multi-party system only started to develop during the 1990s. Before that, since 1955, the Liberal Democratic Party (LDP) solely governed Japan. This ended partially in 1993 when more parties emerged, among those the Democratic Party of Japan (DPJ), and furthered diminished during the term of Prime Minister Koizumi (2001-2006) who lessened the power of *zoku*, diet members representing specific interests and pushing for regulations which comply with these interests (Ōtake, 2000, pp. 125-129; Kevenhörster, 2010, p. 294). Nonetheless, the LDP's influence is still strong. Currently, Japan is still controlled by two major parties, the LDP and the DPJ (Yamamoto, 2014, p. 173; Er, 2014; p. 17). In addition, Japan's political set-up is very centralistic. Little responsibility is left to local governments. Especially concerning financial allocations the central government insists on strict regulations. A lack of financial resources on the local level results, among others, in very low civic participation in politics (Foljanty-Jost, 2009, p.11; Pascha, 2010, p.114; Yamamoto, 2014, p. 174).

### **8.1.2. Economic Policy of Japan**

Japan's economy is a free market economy. The country's economic policy can be described as neomercantilism. The government guides the country's economy through rules and regulation as well as financial interference. As introduced in the chapter about Japan's history, during the Meiji period the government started to steer Japan's economy by introducing foreign technologies and improving these within the own country, plus setting up new companies in industries it wished to have and then reselling them to private owners. After WWII the state continued to strongly interfere in order to support the export-led growth which helped Japan to catch up with Western industrialized countries. The government allocated subsidies to exporting industries, loosened competition policies if necessary and provided loans for companies important to foster export (Streeck and Yamamura, 2003, pp. 6-7; Henderson, 1973, p. 202). Despite many academics doubting extensive government interference in a market economy, Japan has achieved great periods of growth. Currently, Japan tries to decrease state intervention, albeit it is prevailing in the country's economy. The agricultural as well as the banking sector enjoy strong protection against international competition. In various other sectors which the government deems essential for Japan's economy subsidies, import barriers, investments and export promotion are not rare (Kevenhörster, 2010, p. 283; Fukai and Fukui, 2004, p. 210). Yet, efforts towards diminishing state interference have intensified especially since the term of Prime Minister Koizumi who strongly supported deregulation. He wanted Japan to move away from neomercantilism towards neoliberalism. He met fierce opposition, though, since many Japanese still embody a deeply rooted group mentality which entails the belief in equality and the caring for each other. The idea of a free market economy under perfect competition clashes with their cultural identity. Japanese highly value a sense of security and therefore a less competitive environment with many businesses protected from failing through governmental aid seems more compatible with their cultural norms<sup>22</sup>. Hence, the move towards a less regulated economy will only slowly if at all realizable in Japan (Kingston, 2013, p. 19).

Another very special feature of Japan is the interplay between political and economic actors. Politicians, bureaucrats and companies representing the state, interest groups and the economy are highly interdependent. Academics call it the "iron triangle" (Fukai and Fukui, 2004, p. 227). In order to be economically successful, companies strive for beneficial laws and regulations. As mentioned in the chapter above, bureaucrats and politicians collaborate on

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<sup>22</sup> A more detailed description of the Japanese culture follows in chapter 9.

legislative drafting. To ensure their interests to be regarded, firms offer high positions to retired ministerial workers as well as financial support for parties and individual politicians campaigning. Moreover, they offer financial favors to bureaucrats. The members of the bureaucracy, who strive for luxurious lifestyle and an affluent life as pensioners, take this money willingly (Rothacher, 2003, p. 117). In turn, they need politicians in order to ensure their political power and opportunities to influence. The politicians rely on the bureaucrats to provide expertise in order to design and pursue their political efforts. At the same time, they need the companies' financial support since in Japan very little money is allocated to campaigning (Streck and Yamamura, 2003, p. 2; Kevenhörster, 2010, p. 291, Rothacher, 2003, p. 110). The three groups depend on each other, which is why a certain level of corruption in shape of financial and political favors has been omnipresent in Japan's politics. In order to avoid being publicly exposed, the groups feel yet more pressure to uphold a very close network. Often, they even include members of the media, since they are the greatest force to investigate cases of corruption (Rothacher, 2003, p. 117). One must keep in mind though, that the general level of corruption in Japan is very low (GAN Integrity Solutions, 2014; World Audit, 2014).

### **8.1.3. Legal Structure of Japan**

Japan first introduced a nationwide law during the Tokugawa period. During the Meiji period, Japanese academics not only tried to economically relate to Western countries but also the legal framework was renovated. Japan then based its law on German and French models with a tendency towards German influences and created a Civil Law (Marshall, 2011, p. 92; Henderson, 1973, p. 164; Kevenhörster, 2010, p. 238). In 1890, the Japanese Emperor introduced Japan's first constitution which he drafted according to the Prussian constitution (Henderson, 1973, p. 167). After WWII, the American system of the Common Law gained influence in Japan's legal structure, yet the law is still more similar to the European versions in being unitary as well as inclined to avoid official trials. In Japan, maybe even more than in its European role models, conflicting parties try to solve their differences outside of court (Marshall, 2011, pp. 92-93; Henderson, 1973, p. 172; Vogel, 2003, p. 308). The highest court in Japan is the Supreme Court. One of its main tasks is to verify for laws and sentences to comply with the constitution (Marshall, 2011, p. 93; Henderson, 1973, p. 174). Furthermore, Japan also established its criminal law following the German design. Interestingly, Japan records five times less offence rates in comparison to Germany. This may be due to Japan's low crime rate or the lower usage of courts. In addition, Japan's law is known to be very

stable. The legal framework only undergoes small changes. However, Japan lately managed to enhance transparency. This started with the Disclosure Act of 1999, which forces the government to deal openly with potential laws and regulations (Marshall, 2011, pp. 97-101).

#### **8.1.4. Competition Policy of Japan**

The competition policy is another important feature of the regulatory institutional framework of Japan. In the past, the Japanese government as well as people did not engage in the idea of establishing a competition policy. Cartels and monopolies were a natural feature of the economy. This paved the way for the huge zaibatsu conglomerates to emerge and successfully continue until the Occupation period after WWII. Under American control, for the first time, monopolies were forbidden and existing ones dissolved. Despite getting to know the idea of unhindered competition, Japan returned to a very relaxed attitude towards cartels as soon as the American occupation ended. Keiretsu emerged. Only during the 1970s, after the oil shock damaged the Japanese economy, a suspicion towards cartels developed which entailed the revision of the Antimonopoly Act. The Plaza Agreement of 1985, which forced Japan to raise the Yen's value as well as strengthen competition in the local market, contributed external pressure on Japan to implement their antitrust law more strictly. During the 1990s the public awareness of the importance of antitrust actions heightened greatly and in 1993 penalties were raised (Sadaaki, 2002, p. 56; Pascha, 2010, p. 133). Nonetheless, many academics view the Japanese antitrust policy to be too lax. In 2005, the country again tried to severe sanctions as well as the government introduced the leniency policy. The Japan Fair Trade Commission (JFTC) engages actively in the prosecution of Anti-Monopoly Act violations in addition to examining large-scale M&A and pursuing the implementation of the current competition policy. All the same, the JFTC struggles to achieve its goals. Many firms violate the laws time and again unwilling to give up their privilege as a monopoly. This often leads to a challenging economic environment for new market entrants (Sadaaki, 2002, pp. 54-60; Pascha, 2010, p. 133).

#### **8.1.5. Impeding Regulations in Japan Concerning IFDI**

Japan has one of the lowest IFDI rates measured relative to the gross domestic product (GDP) among all OECD countries, although it has eliminated most impeding regulations (Bureau of Economic and Business Affairs, 2012, para. 10). Informal obstacle put up a much larger barrier for foreign firms (Ballon, 1992, p. 16-17; OECD, 2003, p. 169). Formal restrictions have been constantly loosened since the 1970s. During WWII, the Japanese

government supported foreign entrants, especially in warfare related industries. Throughout the following period of the American Occupation, the US government pushed Japan to maintain an open yet controlled economy. After 1952 in turn, Japan closed its economy towards foreign entrants fearing to be taken over by foreigners. The government introduced an era of strongly protective policies (Blomstroem et al., 2000, p. 19; Kushida, 2010, p. 4; Suginothara, 2008, p. 842). Foreign entrants were only allowed as non-equity entrants, import was heavily restricted, a state-led centralized bank decided on loan distribution (Pascha, 2010, p. 137; Suginothara, 2008, p. 843). Only during the 1970s, after the impact of the oil shock, Japan started to reopen its economy. In addition, after entering the OECD in 1964, fellow members constantly intensified pressure on Japan, to abandon unfair trade restrictions. Hence, the government lowered import barriers, recognized foreign patent protection and slowly widened permissions for foreign ownership of Japan-based offices (Dunning and Lundan, 1997, p. 202; Porter and Sakakibara, 2004, p. 32; Kushida, 2010, p. 42, Henderson, 1973, p. 237). Still, the state favored local firms, especially concerning the supply of loans (Suginothara, 2008, p.843). Plus, entrants were subject to a strict validation process followed through by the bureaucracy according to the Foreign Investment Law as well as the Foreign Trade Control Law. Foreign market entrants had to prove that their future business would positively contribute to Japan's economy. One must keep in mind though, as described before, the bureaucracy upheld close ties to politicians as well as businesses. Therefore, the validation took an arbitrary nature. Bureaucrats tended to prioritize the interests of their business partners over written laws. In conclusion, obtaining business permission was a very difficult task for foreign businesses (Henderson, 1972, pp. 198-199, 227).

During the 1980s and 1990s, all these processes became subject to change (Flath, 2005, p. 156). First, foreign businesses were released from the validation process and were only asked to inform the Minister of Finance of their intentions prior to their entry. This way the government maintained their loophole to take legal action in case an undesired company tried to enter their market (Ito and Fukao, 2001, p. TF19). During this time, market entrants were still in some way perceived as a threat to Japanese businesses. This perception entirely changed after the bubble burst in 1990. The publics started to doubt the state's protective attitude towards the Japanese market. Foreign entrants became a solution instead of a threat. Multi-national corporations (MNC) could bring new management expertise, technology and job opportunities. Politicians turned to actively attracting foreign businesses. They provided long-term credits as well as amended the reporting regulations. Businesses were now only subject to notify the government ex post their market entry (Kushida, 2010, p. 45; Ito and

Fukao, 2001, p. TF19). Up until today, Japan's Prime Ministers continue to focus on facilitating the market entry to Japan (Kushida, 2010, p. 47). This is mirrored in the numbers of market entries. Japan experienced a very slow increase of foreign entries in the past, but after the bubble burst in 1990 the numbers improved quickly. In the period from 1996 until 2010, IFDI in Japan almost decupled (JETRO, 2015a). Despite this, in an international comparison, Japan score very low concerning IFDI (United Nations, 2015).

From a regulatory perspective, this may have several reasons. First, although regulations were loosened, businesses are still subject to a strict notification policy, having to prove how the Japanese economy will benefit from them. In addition, the state imposes strict administrative guidance onto foreign market entrants which triggers reluctance to choose Japan as a target market (OECD, 2003, pp. 167-168). Moreover, the ties within the iron triangle still exist. Even today, corporations influence politicians to pursue policies in line with their personal interests. Officially, these practices are prohibited since 2000, however, informally still conducted (Gauder, 2011, p. 10; Rothacher, 2003, p. 110). Another characteristic of the Japanese regulatory system, foreign firms tend to struggle with, is the lack of clarity of market entry policies as well as the lack of trained legal support. Especially firms from countries with tight legal frameworks, which create a legal environment easy to understand, do not find it easy to solve disputes in Japan. As mentioned before, Japanese tend to resolve legal issues out of court. This has led officials not to pursue a tight legal system. In order to attract foreign firms, the government thus plans to clarify the legal structures (Pekkanen, 2008, pp. 10-12; JETRO, 2005). One last remaining regulatory obstacle is the granting of visas. The immigration office is reluctant to pass out permanent visas to foreigners (Haig, 2011, p. 225). A wish to keep Japanese a homogenous people (Kingston, 2013, p. 149) and the general perception of foreigner to have criminal tendencies (Kingston, 2013, p. 138) leads the government to refrain from giving out visas. Besides, every foreigner needs to carry his *zairyū* card, his identification card, with him at all times and in addition to always updating the local government of his current place of residency, so the government can keep track of all foreign residents. The state usually tends to distribute limited visas which have to be renewed, yet keeping the option of not renewing it in case of a minor violation (Kingston, 2013, p. 150). Even if a permanent visa is obtained, rights, such as the right to vote, will not be granted to foreign residents (Haig, 2011, p. 225). If a foreign company wants to enter the Japanese market, it needs to be able to bring a few of its own workers to the host country. In case, obtaining a visa is a big struggle, the market entry is hampered. Therefore, MOFA (Ministry of Foreign Affairs) and METI who are interested in improving the Japanese

economy with the help of foreign market entrants, pursue simpler immigration rules (Haig, 2011, p. 252).

In summary, impeding regulations on the market entry to Japan were lowered substantially in the past and are subject to further decrease. As will be seen in the analysis of this paper, in contrast to these regulatory hindrances, difficulties on the operating level impose a much greater obstacle to a successful market entry (Ballon, 1992, p. 16-17).

## **8.2. Germany's Institution**

After introducing Japan's institutional framework, this chapter will take a look at the German structure. A base for a comparison of the two systems should be established. Same as for the case of Japan, the chapter starts with the introduction of the political arrangement and then moves on to the economic policy and the competition policy.

### **8.2.1. Political Structure of Germany**

Germany's political structure is a federal republic. The head is the Federal President who is appointed for a five-year term. He has the power to dismiss federal ministers but very little decisive authority. Therefore, his role is mainly representative (Schmidt, 2007, pp. 176-177). The legislative is made up by the lower house (Bundestag) whose members are elected for four-year terms, and the upper house (Bundesrat) whose members serve for six-year terms. While the members of the lower house are directly voted by the public, the upper house consists of representatives of the sixteen states of Germany. The legislative is responsible for drafting laws and regulations (Allen, 2004, p. 172; Schmidt, 2007, pp. 149, 198). Since neither the lower nor the upper house are supposed to be superior a great deal of cooperation between the two houses is expected. On the one hand, this arrangement supports democratic value, but on the other hand it can slow down the compromising process and may complicate the introduction of new laws (Schmidt, 2007, p. 206). The lower house is at the same time the parliament. Among others, its task is to elect the federal cabinet comprising the Federal Chancellor and the federal ministers. These make up Germany's executive and are responsible for implementing new laws and regulations (Schmidt, 2007, p. 163). The parliament, on the other hand, participates additionally in the election of the Federal President as well as the judges of the federal constitutional court. They make up Germany's judicative power and their main task is to evaluate constitutional violations (Schmidt, 2007, pp. 149, 221). This

way the German legislative has a certain influence in shaping the country's executive as well as its legislative.

Germany is sometimes called a "party democracy" (Schmidt, 2007, p. 173). Political parties in Germany are comparably manifold and more than two parties tend to assert their influence. This way, new policies receive input and shaping from various different parties (Schmidt, 2007, p. 173). Furthermore, Germany is less centralistic than Japan. The central government delegates more tasks to local governments and this way manages to induce more civic participation in political matters (Foljanty-Jost, 2009, p. 11).

### **8.2.2. Economic Policy of Germany**

Germany's economy is just like Japan's a free market economy. The state tries to give only a rough framework within which the private economy should work as independently as possible. Policies are supposed to be seen as goals which corporations and labor unions can aim for together. In comparison to other countries of the EU, in Germany the smallest percentage of the local industry is publicly run (Allen, 2004, p. 151). One topic, however, which the government pursues strictly, is a well-functioning welfare state. Hence, Germany's economic policy is describes as a social market economy. The state as much as the society view the government's task to be a role model for private businesses concerning social welfare and allocate high importance to the matter. This stern persecution of sociality seems to be stable since the upper class of society introduced and still makes an effort to maintain it. Believing in Christian values as well as a fair democracy during the process of nation building, it tried to create a social as well as geographical balance within the country. In summary, the German economic policy is less regulated than the Japanese but at the same time the amount of social spending in Germany has surpassed Japan since the 1990s (Allen, 2004, p. 151; Streeck, 2001, pp. 12-13; Streeck and Yamamura, 2003, pp. 11-12).

### **8.2.3. Competition Policy of Germany**

Germany has a very stringent competition policy which is even more intensified since the country's economy is also subject to the EU's antitrust regulations. The inner German laws include the prohibition of cartels as well as a strict evaluation of intended merger activities. Additionally, the government bans all large firms to take advantage of their market dominance. The federal cartel office enforces these laws rigorously. The EU's regulations are more concerned with state power. They try to lower the government's influence and do not

permit state cartels. The EU fears those to distort competition which creates barriers for market entrants. Their main goal is to secure transnational competition and provide an environment of smooth economic exchange (Kerber, 2002, pp. 37-40).

### **8.3. Institutional Comparison**

After a short introduction of the Japanese and the German institutional frameworks, this chapter will compare certain points of the two regulatory institutional structures. The first part concerns the similarities while second part depicts the differences between the two countries.

#### **8.3.1. Similarities**

Germany and Japan have always been popular to be compared since they are known for their manifold similarities on a political, as well as economic and cultural level. These similarities may partly result from a similar historical development as described below.

Japan and Germany are two populous economically powerful countries, embracing democratic values. Historically, they both started to engage internationally at the beginning of the 20<sup>th</sup> century, entered the phase of industrialization rather late, however, managed to create a strong economy, actively pursuing local as well as international stability. They maintain export-led economies heavily depending on the import of natural resources. On a societal level both countries are facing the challenge of a low birth rate (Coleman and Rowthorn, 2011, pp. 219-220). Concerning international relation both governments ensure close relationships to the US which results from strong American influences after WWII (Sakaki, 2013, pp. 1-2, Kevenhörster, 2010, p. 238).

Japan and Germany are both consociational democracies, trying to include as many actors as possible into political decision making in order to manifest their democratic values (Kevenhörster, 2010, p.311-312). In Germany many different parties and interest groups can provide valuable contributions while Japan ensures the incorporation of different interests through their government officials' close ties to the bureaucracy and businesses. On the other hand, the participation of various players impedes policy making and compromise finding. New policies are likely to meet strong opposition which renders both political systems rather static (Kevenhörster, 2010, p. 293; Streeck and Yamamura, 2003, pp. 36-37). In Germany political leaders have only changed eight times since 1949. In Japan, the Prime Minister has

changed quite a few times more, yet the leading party had not changed except for one period of three years (Schmidt, 2007, p. 163). This again underlines the steadiness of the two countries' politics.

Japan and Germany are two economically strong nations building their success on high quality export. In the past, the lack of natural resources has created high production costs which forced the two countries to resort to a different method than low prices to compete on the international market. Unfortunately, both countries have left the era great success and now struggle to keep their competitiveness and face economic decline (Streeck and Yamamura, 2003, pp. 12-13; Fukai and Fukui, 2004, p. 152; Vogel, 2003, p. 310).

Another similarity of the two societies is their desire for security. In both countries the saving rate is comparably high. This has the very beneficial effect of generating the necessary capital to fund efforts for technological and product improvement (Streeck and Yamamura, 2003, p. 13). Besides, the wish for security produces a society of committed employees<sup>23</sup>. This paved the way for Japan and Germany to create economies resting upon highly-skilled workers. Both nations have managed to develop a system in which workers are extensively trained. Since businesses trust their employees to stay for long period of time they are willing to invest in their workers' skills. In Japan, these skills are mostly firm-specific since most labors take part in lifetime employment (Kanemoto and MacLeod, 1990, p. 162). In Germany, portable skills are more popular since employees tend to change companies a few times during their life, yet not as often as in other industrialized countries. This readiness to contribute by most corporations creates a society of highly-trained workers (Thelen and Kume, 2001, pp. 201-202).

Japan and Germany undergo some changes in their current institutional system; however, they do this concurrently. Both uphold a quite far-reaching social system. Yet lately, they face various challenges, which force them to consider restructuring. Another special feature of Japan and Germany is the main bank system or the Hausbankensystem<sup>24</sup>, respectively. Yet, both nations started to move away from this system of close links between firms and banks. Also, the employee fluctuation rate increases and endangers businesses' willingness to provide extensive training, and lastly both governments try to further

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<sup>23</sup> This effect is stronger in Japan than in Germany, which will be describes in chapter 9.4. In international comparison, however, both countries enjoy a long-term committed labor force.

<sup>24</sup> German Hausbanken are just like their Japanese counterpart, the main banks. They have special relationships to their clients, are usually the biggest shareholders of their corporate client and help in times of need through monetary or informational aid. Commonly, firms do not change their Hausbank (Elsas, 2001, p.12).

deregulate the economic system (Streeck and Yamamura, 2003, pp. 4-5, 16-17). All in all Japan and Germany resemble each other in various points. There are, on the other hand, some important differences. The next chapter presents these in detail.

### **8.3.2. Differences**

Japan designed large parts of its political structure similar to the German system. After WWII both countries received great influence from the US. In spite of this assimilation due to the historical development the two nations also differ in a few points.

The first very important point is how the private sector in Japan influences policy making in an a lot more direct manner because of the iron triangle. In Germany businesses can only trust in interest groups or those politicians who represent their goals to help them guide new policies in a beneficial direction. In Japan, the businesses' influence is a lot more straight-forward since politicians and bureaucrats maintain good relations with large corporations and are willing to distribute favors (Vogel, 2003, p. 308). The iron triangle additionally leads to a high amount of former bureaucrats now working in parliament, which is not the case in Germany (Kevenhörster, 2010, p. 283).

Second, Japan's government still practices more interference into the country's economics, for example by guiding the credit distribution. Germany's government in contrast interferes in particular in order to uphold the level of social welfare. Public spending for social security as well as public transfer payments directed towards pensions and public welfare of children, seniors and handicapped measured relative to the gross national product are almost 10% higher in Germany than in Japan (Fukai and Fukui, 2004, p. 151; Kevenhörster, 2010, pp. 314-316; Vogel, 2003, p. 308).

Further differences concern the organization of unions. In Germany, they are organized on a sectoral level, while in Japan, employees found unions within one firm. In addition, German unions have close relations to politicians and can thereby make their opinion count, while in Japan political ties are held up exclusively on an employer level. The last very interesting variance between the two countries is the avoidance of court cases. While both countries' individuals and businesses prefer settlements out of court, the degree is much higher in Japan (Vogel, 2003, p. 308).

Japan and Germany are two geographically distant countries which seem very different at first sight. This detailed analysis, however, proposes that the two are actually

similar from an institutional perspective. Japan's past orientation towards German law and the two countries' appreciation of an elaborate legal system bring the nations much closer together. The next chapter tests whether this finding is also feasible on a cultural level.

## **9. The Cultures of Japan and Germany**

Since WWII, Japan and Germany have been popular to be compared in economic papers, especially concerning cultural features. In 1940 the two countries, together with Italy, formed the axis powers by signing the Tripartite Pact (Stumpf, 2001, p. 160). Japan and Germany eventually never fought a war together; nonetheless, a bond between the two countries was established. Both countries went through a period of American Occupation, followed by an era of high economic growth. Additionally, on a personal level, both Japanese and Germans are known to value punctuality, compliance with rules, and cleanliness. Both people are stereotypically perfectionists, dedicated workers, not famous for their sense of humor, but rather for serious and precise completion of tasks (Fukuyama, 1995, p. 210). Their historic background as well as their stereotypes makes the two nations interesting subjects for comparison. Hence at first sight, the market entry from Germany to Japan seems rather manageable. Yet, when taking a closer look, the two cultures vary quite a bit on the national level as well as the business level. The latter may be due to Japan's very unique management and HR system.

This chapter will first describe the differences between the two countries focusing on Hofstede's five dimensions. Hofstede compared 74 nations. For each nation he derived a score as well as a rank which helps to compare the different countries' results. Each subchapter will start by giving the scores and ranks for Japan and Germany. After this insight into Hofstede's analysis, the chapter then compares a few more very practical cultural differences to give a more graphic understanding. This should provide information to answer the questions about the level of cultural difference as well as the power distance and uncertainty avoidance in the home country which are needed for the analysis. The chapter then moves on to examining the differences in business culture. It will emphasize the unique traits of Japanese management. These facts should serve as basis to find out the appropriate market entry mode for the German consulting firm to enter Japan.

## 9.1. Power Distance in Germany and Japan

As describes before, the dimension of power distance explains in how far a superior involves his subordinate in his decision making process. Hofstede and Hofstede (2005) derived the following results:

**Table 1: Power Distance Index Values**

	Score	Rank
Japan	54 <sup>25</sup>	49-50 <sup>26</sup>
Germany	35	63-65

Note: Adapted from Hofstede and Hofstede (2005, p. 43)

Japan received a score of 54 and thereby ranks 49<sup>th</sup> to 50<sup>th</sup>. Germany received a value of 35 which places the country on the 63<sup>rd</sup> to 65<sup>th</sup> rank. While Japan's value is greater than 50, so in the upper half of the possible point, both countries rank in the lower half of all the 74 countries. Hence, the power distance is not too large in both nations. This may be especially surprising in the case of Japan. The Land of the Rising Sun is known to employ strict hierarchical structures not just at work but also in society (Ralston et al., 2008, p. 8). Respect towards elderlies and superiors is highly valued, which is expressed in behavior as well as in speech. Deep bows and a whole new form of verbs help to honor higher ranking personalities. Given these attributes of the Japanese society, Japan's power distance index seems quite low. These contrasting results stem from the definition of power distance. While Japanese superiors are indeed in charge of decision making and subordinates rarely dare to challenge these decisions, the former are always eager to choose options which benefit the latter. It is the boss's responsibility to select a path which is in favor of as many of his fosterlings as possible. He is more a parent than a dictator (Hofstede and Soeters, 2002, p. 4). He finds this path by keeping a regular exchange with his protégés. He can use their input and ideas to make up a favorable solution (Hayashi, 1988, p. 115).

Moving over to Germany, the power distance index value becomes even smaller. Germans, just as Japanese, usually believe in hierarchies and in top-down decision making (Hayashi, 1988, p. 115). However, these decisions are not too detailed. German employers exert their best effort when given a framework within which they can operate self-responsibly

<sup>25</sup> The maximum points available for Japan and Germany are 100. Hofstede added a few countries later to his study, which is why there are countries scoring more than 100. However, Japan and Germany were part of the first study, which is why their maximum is limited to 100.

<sup>26</sup> In case there are several nations with the same score, they share ranks accordingly, which is why both Japan and Germany occupy several ranks.

(Hofstede, 1993, p. 83). Germans rarely appreciate the dictatorial instructions what to do and how to do it. They are rather given a goal which they then achieve through their own best effort by choosing the best way themselves or democratically in a group. The German power distance index value is lower than the Japanese. Their scores differ by almost 20 points. Thus, analyzing the first of Hofstede's dimensions, the two countries differ from a cultural point of view.

## 9.2. Collectivism versus Individualism in Japan and Germany

Hofstede's second dimension weighs individualism up against collectivism. This dimension describes how people identify themselves, as individuals or as part of a group. Hofstede and Hofstede (2005) presented the following values for Japan and Germany. The higher the score, the more individualistic is the country.

**Table 2: Individualism Index Values**

	Score	Rank
Germany	67	18
Japan	46	33-35

Note: Adapted from Hofstede and Hofstede (2005, p. 78)

Germany scored 67 and ranked 18<sup>th</sup>, while Japan scored 46 and placed 33<sup>rd</sup> to 35<sup>th</sup>. In conclusion, Germany is a more individualistic country, and in contrast Japan honors collectivistic values. In Japan's collectivistic culture, people grow up to be part of a group. The first group they integrate into is the family. While in individualistic countries family, as a social group, means the close family containing parents and siblings, the collectivistic understanding of family includes grandparents, uncles and cousins. Traditionally, once the children become adults, the eldest son takes care of the family. Thus, the other siblings need to find new families or groups to identify with (Hofstede and Soeters, 2002, p. 6). Japanese need a group to fulfill their feeling of belonging (Ralston, 2008, p. 9; Griffith et al., 2006, p. 8). Once entering a group, they develop a sense of complete loyalty. Success means the group succeeds no matter the individuals' performance (Cousins, 1989, p. 126). They place the group's interests above their own and try to abide to all the group's written or unwritten rules in order to stay a part of the group as long as possible (Kingston, 2013, p. 19; Griffith et al., 2008, p. 7; Hayashi, 1988, p. 67). Members of a group tend to have very little patience for disobedience which is why those who do not comply with the rules are forced to leave the group (Griffith et al., 2008, p. 8). Thus, in order to foster a long-term relationship, group

members work hard for the group. If a group faces a task, they tend not to separate single tasks and distribute these, but work on the entire project as a team (Hayashi, 1988, p. 73). For every Japanese, it is thus very important to belong to a group. Since the eldest son took care of the family his siblings traditionally turned to find their own group of belonging. This group could be at work as much as in the neighborhood (Hofstede and Soeters, 2002, p. 6). This way in Japan strong social bonds develop not just within a family.

One very important result from cultural differences concerning collectivism and individualism is a difference in communication. People from collectivist cultures use a lot more interpretation and construction when transferring information. When receiving a fact they perceive it within its context. They analyze the situation, abstract the information received within its context, in order to find out what exact meaning this piece of information has for them. Japanese consider their past experience and the setting in which they receive the news and then decide on how to understand it (Cousins, 1989, p. 136; Nisbett et al., 2008, p. 296; Bhagat et al., 2002, p. 212). By considering different interpretations and explanations, members of collectivist cultures tend to be less easily surprised. They reflect on different scenarios and try to gain a holistic picture (Nisbett et al., 2008, p. 296). This contextual communication results from Japanese seeing themselves in a group which they transfer to their way of communication.

Germany is a rather individualistic country. People see themselves as individuals rather than as part of a group. If entering a group and becoming a member of a team it is because of categorical bonds. Similar interests, friendship, or a work project and thus a shared goal bind people more than environmentally given relationships such as family, work or place of living (Nisbett et al., 2008, p. 295). For them individual accomplishments, a noble character and efficient performance are signs of success (Cousins, 1989, p. 126), rather than the group's achievements. As mentioned before, unlimited loyalty is restricted to the closest family members, meaning parents, brothers and sisters (Hofstede and Soeters, 2002, p. 6). In summary, Germans perceive themselves as single persons without including the environment. This transfers to the communication style. In Germany, people do not include context into delivering information but see single facts as they are. They convey in abstract words the material they need their counterpart to know (Cousins, 1989, p. 126). Germans use logic to make sense of the data received, and only include context explicitly mentioned during the communication into their analysis (Cousins, 1989, p. 137; Nisbett et al., 2008, p. 296). Individualists approach the transfer of information clearly differently from collectivists. The

same applies to managing dissension. Individualists with a comparably low feeling of power distance, as Germans are, tend to choose the path of direct confrontation. They state their disagreement and try to find a solution on the spot. Collectivists with comparably higher feeling of power distance will try to avoid confrontation and try to reestablish a harmonious relationship without a verbal dispute (Oetzel et al., 2010, p. 255).

In conclusion, just as power distance did, Hofstede’s second dimension also emphasizes how dissimilar Japanese and Germans are. Japan’s score shows its collectivistic culture, German’s score emphasizes its individualism. They vary especially in their perception of individuals, their concept of success and their communication style.

### 9.3. Masculinity versus Femininity in Japan and Germany

Hofstede’s third dimension depicts the gender roles within a society, how equally the two sexes are treated. It transfers these roles onto the work environment, meaning what is valued at a work place. Masculine societies emphasize challenges and efficiency while female societies focus on the work environment and the harmony of a professional and a private life. This dimension is another one which underlines the difference between Germans and Japanese. Hofstede and Hofstede (2005) presented the following scores how masculine Japan and Germany are.

**Table 3: Masculinity Index Values**

	Score	Rank
Japan	95	2
Germany	66	11-13

Note: Adapted from Hofstede and Hofstede (2005, p. 120)

Considering the ranking only, Japan and Germany do not appear too far apart with Japan being the second most masculine country among the 74 Hofstede examined. Germany follows on the ranks 11 to 13. However, the scores show that the two nations are actually almost 30 points apart, with Japan having a value of 95 and Germany one of 66. Japan’s high score indicates how clearly gender roles are defined in Japan. Men are seen to be responsible to earn money, achieve a great professional career, be competitive, and show great skills and a strong performance. In contrast, women are responsible to for a warm family life and a smooth running household. While they are an inherent part of Japan’s workforce, they are not viewed as career potentials. Generally, the inclusion of women in business has developed very slowly (Schein, 2001, p. 680; Trommsdorff and Iwawaki, 1989, p. 491; Steinmetz et al., 2014,

p. 57). Their capabilities are connected to household and family. These clear differentiations make men and women very dependent on each other. One needs the other one's abilities in order to lead a comfortable life (Hofstede and Soeters, 2002, pp. 7-8). Transferring these views of society to their work environments, being a very masculine culture, Japanese emphasize achievement and performance. They strain themselves mentally and physically as much as possible in order to help their company towards success. They feel responsibility to contribute. Death because of overwork seems strange to most cultures, yet is a well-known phenomenon in Japan (Hofstede and Soeters, 2002, p. 7).

Germany in contrast is a lot less masculine. Gender roles are not as clearly defined as in Japan. Both career and household are shared more often than in Japan, a trend which spreads further with years passing by (Steinmetz et al., 2014, p. 57; Trommsdorff and Iwawaki, 1989, p. 486). At work, Germans value a balance between personal and professional life and a comfortable work environment. They make sure to have enough time for human interaction and maintaining their personal relationships (Hall, 1982, p. 132). Nonetheless, Germany still ranks high among Hofstede's examined 74 countries. This may be due Germany's low numbers of women occupied in top management positions (Witt and Redding, 2009, p. 867; Schein, 2001, p. 683). In conclusion, both countries are rather masculine, however, this tendency is a lot more pronounced in Japan both in the professional as well as in the personal life.

#### 9.4. Uncertainty Avoidance in Japan and Germany

The fourth of Hofstede's dimensions is uncertainty avoidance. It describes how well people cope with unfamiliar circumstances. Hofstede and Hofstede (2005) derived the following scores for Japan and Germany:

**Table 4: Uncertainty Avoidance Index Values**

	Score	Rank
Japan	92	11-13
Germany	65	43

Note: Adapted from Hofstede and Hofstede (2005, p. 168-169)

The table shows a very high score of 92 for Japan which places the country 11<sup>th</sup> to 13<sup>th</sup>. Germany's score with 65 is not very low either and places the nation on the 43<sup>rd</sup> rank, in the middle of the nation spectrum. Just like in the case of masculinity and femininity, Japan and Germany both have a clear tendency towards the same end of the spectrum, but because of

Japan's very high value, the two cultures still differ. In order to manage their fear of the unknown Japanese try to introduce many rules which cover most possible scenarios. They need a clear structure within which boundaries they can move without facing unexpected situations. Thus, in Japan people expect fellow Japanese as much as foreigners to honor the set regulations and help to maintain the system of rules. These attributes result in the Japanese desire for conformity and homogeneity<sup>27</sup>, their great respect for traditions and their willingness to adapt customs and rituals (Hofstede and Soeters, 2002, p. 5). Japanese expect the reduction of uncertainty not just on a private but also on a public level. They rely on their government to introduce a strong system of social security which helps citizens in unexpected distress. During the past ten years, Japan has loosened their regulations and cut down their spending on social welfare. The Japanese observed this with a sense of great dissatisfaction (Kingston, 2013, p. 17). They prefer a transparent system of security.

Just like the Japanese, the Germans try to handle their dislike of uncertainty at best possible. They usually resort to detailed planning. A comprehensive plan, which includes various possible scenarios and at the same time information on how to handle these situations, can greatly facilitate life. In Germany, people set great store by following these plans. It is their effort to avoid mistakes right from the beginning, and finally reduce uncertainty (Rauch et al., 2000, p. 30). In conclusion, both Japanese and Germans worry about uncertainty. They exert themselves to anticipate as many developments as possible in order to plot their reactions accordingly by detailed planning and the introduction of an overreaching set of rules. Because of Japan's high uncertainty index value, this behavior is more pronounced in Japan.

### 9.5. Long-Term versus Short-Term Orientation in Japan and Germany

The fifth and last dimension by Hofstede describes whether people of a certain culture focus on long-term or short-term results of their actions. Hofstede and Hofstede (2005) found the values below for Japan and Germany.

**Table 5: Long-Term Orientation Index Values**

	Score	Rank
Japan	80	4-5
Germany	31	25-27

Note: Adapted from Hofstede and Hofstede (2005, p. 211)

<sup>27</sup> Japan as a homogenous people is be further explained in chapter 9.7. It shows how the love of homogeneity can complicate a foreigner's life in Japan.

This dimension contains the biggest difference between the two countries. Japan, with a score of 80, is very long-term oriented, ranking 4<sup>th</sup> to 5<sup>th</sup>. Germany in contrast, with a value of 31, is rather short-term oriented, ranking 25<sup>th</sup> to 27<sup>th</sup><sup>28</sup>. Japanese usually look for a long lasting relationship and are prepared to steadily work towards a greater goal. They excel in patience and perseverance. They do not shy away from hardships. Confucian values are enshrined deep within the Japanese culture. These teach endurance, dedication and determination, which lead Japanese to aim for the greater good as distant as it may be (Hofstede and Soeters, 2002, p. 11). This dimension combined with uncertainty avoidance is also reflected in Japan's unusually high savings rate (Katz, 2015, p. 210). Japanese store as much money as possible to finance their seniority as well as be prepared for any case of emergency. Furthermore, the combination of long-term orientation, uncertainty avoidance and collectivism leads to a very interesting character trait. Japanese plan their actions very detailed and as a group work together for all the plans to be successful, as much time as it may take. If, however, they still happen to fail one day, they struggle much more to find a resolution than a Western person would. Once, Japanese failed, they see themselves to have lost face<sup>29</sup>, which is situation difficult to recover from (Griffith et al., 2006, pp. 10-11).

Germans approach efforts from a much more short-term branded point of view. Fast results are important to show one's success. Long-term achievements can be rather aimed for by defining milestones along the way. Thus, Germans and Japanese contrast highly according to Hofstede's fifth dimension. Japanese emphasize infinite relationships and the great goal at the end, which they work towards as a group. Failure along the way can symbolize the end of the project. Germans in contrast focus on soon to earn profits and short-term beneficial relationships. At the same time, they are flexible in case the project does not follow through as it was planned.

## **9.6. Practical Examples of Cultural Differences**

After comparing the Japanese and the German culture by the means of the five cultural dimensions introduced by Hofstede, the following paragraphs will show a few more detailed

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<sup>28</sup> The seemingly low rank for such a low value stems from the reduced sample Hofstede used for the fifth dimension. In this analysis, he could only include 39 countries.

<sup>29</sup> Face is an East Asian concept, which has its origins in China. It describes a person's position in life, which he derives from his own understanding of himself as a part of the group around him and the expectations his peers have of him. It includes the conformity to society's virtues and rules in order to be accepted as part of this society. Losing face in turn describes that the person was not able to live up to the expectations, in example by violating certain rules. This violation results in losing his peers' acceptance which is a great fear of group-oriented people. Thus, to lose face implies great humiliation in East Asian cultures (Ho, 1976, p. 883).

examples of cultural differences in order to paint an easily comprehensible picture. The first example is the perception of how superiors should behave. On the one hand, Japanese and Germans resemble in that they frown upon powerful people who show their emotions. They prefer absolute objectivity (Mondillon et al., 2005, p. 1117). On the other hand, they differ in that Japanese are stricter than Germans about obliging rules as mentioned before. In addition, Japanese are a peace and harmony loving people who shy away from confrontation. When making a critical decision which requires a compromise between two parties, a mediator first consults with both sides and seeks a solution before the parties actually meet (Hofstede and Soeters, 2002, p. 2). Amicability and cooperation is expected from every member of society. Thus, they expect even influential personalities to always respect social norms and conform to society's rules (Mondillon et al., 2005, p. 1117). Germans in contrast do not believe in the integrity of powerful personalities and hence reckon with them breaking social rules without even facing any repercussions which makes workers often suspicious towards their superiors (Mondillon et al., 2005, pp. 1116-1118).

The second example concerns the structure of society. Both nations emphasize the middle class and try to maintain a small gap between the rich and poor. The governments engage extensively in social welfare and wealth redistribution. Nonetheless, from an economic point of view, Germans hope for a reduction of state interference in order to recover Germany's great economic growth. By introducing more market and less government control they believe to revive Germany's market. Japanese, in contrast, hope for strong leadership which can guide the country's business out of the economic crisis (Witt and Redding, 2009, p. 876). An important part of the two countries' economies is technological progress.

The third example describes the perception of time in the two countries. Europeans tend to focus on the past. They use their experience to determine which processes to use, or which products they want to continue to enjoy in the future. They like stability and continuity (Hayashi, 1988, p. 4). Japanese in contrast emphasize the present. As for the future and the past, they create links to the here and now<sup>30</sup>. Thus, if a problem occurs, they look back and ahead at the same time in order to find the perfect solution. This understanding of time lead to Japan's mix of tradition and modernity. While ancient customs are preserved and taught to the young, Japan keeps on being fast to introduce the newest technology (Hayashi, 1988, pp. 9-10;

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<sup>30</sup> This link is even visible in the Japanese language. There is no differentiation between simple past, the past tense indicating the completion of an action, and the present perfect, indicating an ongoing action. The notion of an action being finished in the past and now being considered of no concern for the present is a concept unfamiliar to Japanese (Hayashi, 1988, p. 27).

Witt and Redding, 2009, p. 875). Germany on the other hand has a very hard time to launch new technologies on the market. The habit of using well-trying tools leads Germans to reject change (Witt and Redding, 2000, p. 872). In conclusion, the Japanese customers are much more open towards new practices than the German buyers, as long as it does not clash with any traditions. The technological market seems much easier accessible in Japan, because of the cultural difference of the perception of time.

The last example depicts a few customs which divide the German and the Japanese culture. Germans highly value of private space. When working in an office, they prefer their door to be closed and work on their own. They enjoy orderliness and the opportunity to work in quiet (Hall, 1982, p. 135). In Japan, in contrast, people have a much more relaxed view on privacy. They often work in huge collective offices where they are separated by small paper walls. In winter, Japanese warm themselves by joining their legs under a heating table which is covered by a blanket and has a heating device attached to it. They do not mind the closeness, nor do they perceive this as an invasion of their private space (Hall, 1982, p. 150). Another cultural contrast of the two nations is their communication. The often examined topic of high-context and low-context culture comes into effect. Germans are a more low-context culture (Campbell et al., 1988, p. 54). They are very straightforward in stating their point and, as mentioned before, include all the information they want to deliver in the actual spoken word. (Richardson and Smith, 2007, p. 480) Japanese, on the other hand, prefer to first orbit the real topic and rather hint at their actual argument (Hall, 1982, p. 151). Japan's high-context culture lets them speak out much less and has their opposite interpret most of the message that needs to be transferred. This way of communication is only possible in Japan, because of their homogeneity. Their similarity allows them to think similarly enough to have all members involved in an exchange of information understand the words in their context the same way (Richardson and Smith, 2007, p. 480). The following chapter will further elaborate on the homogeneity of the Japanese.

## **9.7. The Homogenous People of Japan**

As seen in the chapters above, Germany and Japan are very different. Yet, there is one more cultural feature of Japan to be mentioned, which distinguishes the people of the Land of the Rising Sun strongly from many other countries and thereby makes the country so unique, and at the same time, its market so inaccessible. Japan is culturally very homogenous (Hayashi, 1988, p. 50; Ralston et al., 2008, p. 13, Brody, 2000, p. 165, Haig, 2011, p. 224).

While, to a certain extent, Germany also tries to maintain its intrinsic culture and attempts to avoid becoming a melting pot of cultures such as the US, the country still has a lot of policies to welcome and integrate foreigners. In Japan, there is a strong lack of such policies (Brody, 2000, p. 134), which results in great suspicion towards foreigners and a lack of integration.

Japan's homogeneity can be explained by its geography, its language, as well as its history. First of all, Japan is an island which made the nation more difficult to reach for other migrants (Hayashi, 1988, p. 50; Ford and Honeycutt, 1992, p. 6; Peterson and Schwind, 1977, p. 50). Second, the Japanese language is very difficult to learn (Kevenhörster, 2010, p. 245; Hayashi, 1988, p. 51). Their script demands foreigners to study about 2000 characters in order to participate in their everyday life. Third, as described in the historic chapter, Japan only started to interact intensively with Western nations during the Meiji period. However, when introducing practices and ideas taken from other countries the government was certain to adapt them to comply with Japanese customs and traditions. They never simply copied, but changed and improved (Haig, 2011, p. 224; Hayashi, 1988, p. 105). Japan's leaders were always anxious for their people to keep their identity for them to stand proud and strong. Their effort clearly succeeded in many ways. Not only did Japan manage to protect their heritage but Japan is even today a very ethnically as well as religiously homogenous country (Ralston et al., 2008, p. 13). Moreover, even though Western examples render a few Japanese very uncontentious with their working and living conditions, the vast majority takes pride in its culture and there is no sign of change (Ford and Honeycutt, 1992, p. 6; Hofstede and Soeters, 2002, p. 12; Hayashi, 1988, p. 62).

Unfortunately, the great honoring of their heritage and homogeneity has led many Japanese to mistrust foreigners and to wish to keep their culture and ethnicity pure (Brody, 2000, p. 165; Kingston, 2013, p. 19). Their experience during WWII and the following period of American Occupation has further stabilized this view. They wish for people to be and think equally. They doubt strangers to be able to learn and appreciate their traditions the way they do themselves (Hayashi, 1988, p. 62). They try to avoid purchasing foreign goods but stick to buying as many local goods as possible (Ballon, 1992, p. 122). Other countries' produce is believed to be of lower quality than locally manufactured merchandise (Kevenhörster, 2010, p. 245; Ballon, 1992, p. 139). Thus, it is very difficult for a foreigner to be accepted as a full member of society. An impressive example for the Japanese view on non-Japanese is their attitude towards the so-called *nikkeijin*. They are mixed race Japanese whose ancestors emigrated from Japan and who now wish to return to their home country. Although, they are

related to Japanese, they are seen as strangers. They struggle to find housing, since Japanese prefer purely Japanese tenants, and at the workplace they are discriminated against in terms of employment, wages, and benefits (Brody, 2000, p. 165; Hayashi, 1988, p. 64). Another example is the 2015 Miss Universe Japan who had to endure harassment since she was born a Japanese mother but an African American father (Holley, 2015, para. 3). The Japanese public did not accept her as a winner in a Japanese contest which underlines the on-going devaluing of anything not purely Japanese.

The Japanese desire for equality and homogeneity is a grand obstacle to any foreign market entrant. It prevents the stranger from becoming a part of society and thus gaining the Japanese's trust and their willingness to purchase their services. Firms need to consider this special feature of Japan's public when choosing a market entry mode.

## **9.8. The Business Culture of Japan**

As explained in chapter 6.2, when entering a foreign market not simply the national but also the business culture can influence the success of the establishment of business. Japan has a very unique business culture. Most guide books for business in or with Japan suggest studying these cultural features intensively before entering negotiations. The special attributes range from HR practices all the way to specific actions such as the art of bowing to show gratitude and respect. This chapter will focus on a few main points to show how a German firm will have to prepare intensively to understand which corporate structures are necessary to conquer the Japanese market.

### **9.8.1. General Differences Between Japan's and Germany's Business Organizations**

The first point relates to the institutional set-up of Japan. The iron triangle describes the close relations between government, bureaucracy, and businesses. When entering the Japanese market, a company should try to integrate into the triangle by forming good relations with government officials. One opportunity is to hire retired politicians or ask them to join the advisory board. At the same time, ties to banks just like in the keiretsu system can help to secure financial aid and management expertise. Last, participation in business associations contributes to a wider network, to attain information about the specific industrial sector, and to show one's effort, and thus to gain acceptance among business partners and competitors (Ballon, 1992, pp. 150-153). One element the German and the Japanese business cultures

have in common is strong labor unions. Yet, in Germany, they are much more independent as they work across an entire industry, while in Japan they are established per company and hence are much more intertwined with the respective management (Haghirian, 2010, pp. 26-27; Fukuyama, 1995, p. 218). This feature is emphasized by the structure of working conditions. In Germany, these are mainly set by law and standardized across the country. In Japan, in contrast, just as labor unions operate, they are decided much more on a firm level (Fukuyama, 1995, pp. 217-218).

The next distinction results from Japan's extensive long-term orientation. When setting targets and evaluating actions, Japanese focus on the approach of the distant great goal. The path of achieving this goal is important, with all its highs and lows (Ford and Honeycutt, 1992, p. 4). Current stagnations on a micro level are acceptable as long as progress on a macro-level is visible (Parkhe, 1993, p. 308; Turpin, 1993, p. 15). Germans instead target fast profits and do not tolerate short-term decreases of business. Profits must be secured and reported on a much more frequent basis. They seek for a great distant goal only whilst ensuring sufficient income in the present (Parkhe, 1993, p. 308; Turpin, 1993, p. 12). Furthermore, the two countries' people differ in their approach to problem solving. While Germans do not hesitate to confront coworkers openly during a meeting, Japanese try to find a solution prior to a meeting. Their need for harmony prevents them from triggering an open conflict. They rather speak to their colleagues in private before the meeting so that, during the meeting, only solutions are presented. It helps them not to lose face (Sullivan et al., 1981, p. 804; Saeki and Horak, 2014, p. 1443). Another aspect, which widens the gap between German and Japanese business, is women in business. In Japan, women are not yet seen as natural members of the top workforce (Blomstroem et al., 2000, p. 7). As mentioned before, German society, too, still struggles to integrate women in hierarchically high positions (Witt and Redding, 2009, p. 867), yet the situation is less dire than in Japan. Japanese women are often only hired as part-time workers, their work is evaluated according to different criteria than men's, and they rarely achieve to enter the career track a company offers to its employees. Many women are expected to retire after marrying (Pascha, 2010, p. 226; Blomstroem et al., 2000, p. 8). Even though, these conditions slowly start to change, foreign firms need to calculate the difference in perception when hiring women in higher positions.

### **9.8.2. HR in Japan**

The most significant difference compared to other country's business structures lies in Japan's HR system, which is mainly a product of the American occupation period. It has been studied by many economists since they hypothesized it to be a driving force of Japan's economic success. Japan has established the practice of lifetime employment (Pascha, 2010, p. 226; Haghirian, 2010, p. 16; Kanemoto and MacLeod, 1990, p. 162). After graduating from high school or university, most Japanese find a job in a company and stay with this company until retirement. The practice of internships and changing jobs in search of a new challenge or because the current workplace does not appeal to one's preferences are not very common in Japan. In contrast, it is seen as a virtue to be able to integrate into a firm's staff and to become a valuable member of the workforce. Changing workplace is seen as a weakness (Haak and Haak, 2008, p. 116). A corporation, on the other side, will make its best effort not to dismiss any of its workers. One method to do so is to hire full-time and part-time employees. Only full-timers are seen as genuine members of the workforce who will enjoy all the company's benefits. Per contra, part-timers will be laid off in times of crises. This way, the firm can make sure to provide long-term secure job positions for its full-time staff (Genda et al., 2010, p. 159). Japanese admire continuity and frown upon the rapidly changing executives in foreign firms. They feel a great responsibility towards their employees (Ballon, 1992, p. 148). Another endeavor a company follows in order not to dismiss any laborer is to provide extensive training in various fields. Firms provide on-the-job as well as off-the-job training, the former usually given by an experienced employee to a newcomer, (Ichniowski and Shaw, 1999, p. 718; Kanemoto and MacLeod, 1990, p. 163), which aims at several goals. First of all, in case one part of a firm faces a crisis, the worker can easily be transferred to a different section. Second, it helps to integrate new members into the team (Ballon, 1992, p. 35). Third, it makes sure no individual is unproductive or overwhelmed with his or her tasks. And fourth, it promotes teamwork and friendship among colleagues since the more experienced ones instruct the newcomers. If the trainee successfully merges with the team, the success is accredited to the trainer, which fosters their relationship. Harmony and friendship are seen as essential components of Japanese business (Haghirian, 2010, p. 15; Saeki and Horak, 2014, p. 1441). Furthermore, Japanese value good personal relations not just among colleagues but also to the superior and to business partners (Turpin, 1993, p. 13; Yamagishi and Yamagishi, 1994, p. 153; Haghirian, 2010, p. 45). It is a point where Japan's culture clashes with Germany's which can easily prevent the success of a business transaction. In Germany, personal involvement at work is seen as unprofessional (Saeki and Horak, 2014, p. 1442). The

two customs work in opposite directions. Germans try to focus on skill and separate personal feelings from work while Japanese see openness about one's private life as a mean to improve work relationships.

The desire for close relations may result from Japan's collectivism. It leads to the successful implementation of two further practices. First, extensive teamwork is very important in Japan (Apfelthaler et al., 2002, p. 112; Haghirian, 2010, p. 14; Ichniowski and Shaw, 1999, p. 708). If a team works on a project, in contrast to Westerners, Japanese do not distribute tasks but try to accomplish their goal as a unit (Hayashi, 1988, p. 36). When working together, they constantly communicate with each other to coordinate the process. All participants feel great responsibility to ensure the team's success. The work environment represents a group each employee belongs to. The Japanese collectivism and their uncertainty avoidance lets them put all their efforts into ensuring the firm's success and avoid risky actions as much as possible (Haghirian, 2010, p. 92-93). Further, they engage in frequent and open exchange with the manager of the team (Ballon, 1992, p. 10). In order to enable free communication, Japanese usually share an office with at least all their teammates and in most cases also with the manager (Haghirian, 2010, p. 45). This again is contrary to the German habit. As mentioned before, Germans have a strong sense of personal space and prefer an individual closed office to work efficiently. The second routine, which contributes to Japanese successful business, is mutual evaluation called the *Satai* system. Japanese employees are not simply evaluated by their superiors but also their coworkers and their subordinates, and in turn assess them. Thus, promotions and bonuses are based on how the performance is perceived by colleagues, superiors, and also subordinates. It is essential for Japanese to maintain friendly relations with coworkers, receive positive assessments, and thereby push forward their own career (Pascha, 2010, p. 218; Ballon, 1992, p. 90).

Another important item of the Japanese HR system is job rotation. Japanese do not simply occupy one position within a firm but cycles through various departments. This contributes to the learning process, the interaction with various members of the company, and provides new challenges as an incentive for the employee to stay with the firm (Turpin, 1993, p. 14; Pascha, 2010, p. 218; Haghirian, 2010, p. 28; Haak and Haak, 2002, p. 68). Even managers still rotate. Because rotation trains staff in a variation of skills, the method mainly creates generalists. Japanese firms employ fewer and lesser specialized workers compared to Western companies. Since the number of rotations is handled as a sign of experience and knowledge, it is important during the decision process of promotion (Pascha, 2010, p. 217).

Promotion and salary are based on Satai, experience, and lastly age. The system of seniority-based pay is inherent to Japanese business (Ballon, 1992, p. 35; Pascha, 2010, p. 226; Ichniowski and Shaw, 1999, p. 708; Kanemoto and MacLeod, 1990, p. 162). Experience is seen as an indicator of excellent performance. From the workers' point of view, it motivates them to stay with the firm since they can hope for a high pay during the later years of their service. If they were to change job throughout their career, they face high opportunity costs since they are likely to start at the bottom as they are newcomers to the firm. As noted above, mid-career changes are generally not popular in Japan. Firms suspect a worker who decides to follow a different career to be irresponsible as he or she was not eager to maintain the former position and was obviously incapable to integrate sufficiently (Ballon, 1992, p. 27). The ideal employee merges with the team and participates in *Kaizen* the Japanese system of "continuous improvement" (Haghirian, 2010, p. 4; Ichniowski and Shaw, 1999, p. 705, Apfelthaler et al., 2002, p. 112). Because of rotation, most workers know the entire firm's process. They are expected to always look out for obstacles which hinder a smooth flow and think of solutions. They practice constant quality control (Haak and Haak, 2008, p. 63; Pasha, 2010, p. 215), a trait only possible among the widely-trained Japanese staff.

The next point of comparison among Japanese and German HR practices is education and hiring. Most Japanese graduates share the same level of education. It is common to join an undergraduate program after finishing high school, yet comparably few students enter a graduate program. Education is standardized nationwide, which renders the new entrants to a firm very homogenous and easy to assess for the hiring committee (Ballon, 1992, pp. 4-5; Kanemoto and MacLeod, 1990, p. 163). German graduates vary much more in level of education and set of skills. Another interesting point is that all Japanese students graduate at the same time, in February. They enter working life on the 1<sup>st</sup> of April (Ballon, 1992, p. 24), which highlights Japan's demand for predictability and uncertainty avoidance. In Germany, graduation dates spread throughout the year which gives firms the opportunity to hire as required. The main criterion for hiring are the achievements a student provides, while in Japan the university a student attended is seen crucial (Haghirian, 2010, p. 14).

The last element which underlines the difference in Japanese and German HR is hierarchy. While both countries enjoy strong hierarchies, they take very different forms. In Japanese business a subordinate must pay his superior great respect. At the same time, the superior is responsible for his protégés. He cannot decide on his own but his decisions are influenced by his subordinates as well as coworker's and superiors. This shows that on the

one hand workers have to take orders from their managers, but on the other hand, their scope is much more restricted by their peers. The mutual evaluation lets employees stick to the safe route, avoid risks, and take conventional actions (Hayashi, 1988, p. 115; Hofstede, 1993, p. 83). In Germany, workers, too, must abide to their superiors orders, yet within their task they are given as much freedom as possible. They are expected to be creative and think of new solution, which in turn can bear a greater risk (Hayashi, 1988, p. 115; Hofstede, 1993, p. 84; Saeki and Horak, 2014, p. 1443). Hayashi (1988) describes the Japanese way as hierarchy “from within” (p. 115), while the German one is a hierarchy “from above” (p. 115).

Having examined many different aspects of culture including the national as well as the business culture, this chapter concludes with the finding that Japan and Germany are culturally very different. While they have a few cultural traits in common such as being uncertainty avoidant and rather power distant, the extent of these tendencies and how they show in everyday life, is very different. Also, Japan’s business culture is very unique and shared in few countries around the world. In summary, for the later analysis of how Japan’s and Germany’s cultures influence a market entry, the two countries have to be assumed as culturally distant.

## **10. Trust in Japan and Germany**

After examining the cultures of Japan and Germany, this chapter will move on to depicting the two nations’ attitude towards trust; whom to trust, what expectations come along with a trusting partnership. Trust is heavily influenced by culture (Parkhe, 1993, p. 307). And since the national cultures of Japan and Germany differ significantly, it is natural to assume, so do their views on trust. This assumption is indeed true, yet possibly in a different way than most would foresee. Japan has the image of being a high-trust culture valuing long-term harmonious relationships. While this is correct on a national level, it does not hold on an international level. Germans, in contrast, being of a fairly high-trusting nature as well, even if not as high as Japanese, keep their attitude regardless the nationality of their opposite. This surprising result, as well as, the different methods of signaling one’s trustworthiness will be further elaborated in this section.

## 10.1. History and Characteristics of Trust

Japan and Germany are both characterized as high-trust nations. They promote social values and are rather fast and skilled to form trusting relationships. This is mirrored as much in existing business alliances as in the superior-subordinate rapport (Fukuyama, 1995, p. 29). The Germans' belief in trust roots in their tradition to form communities such as guilds, which are based on mutual benevolence (Fukuyama, 1995, p. 151). Ever since, the German mind has embraced acts of compassion and sincerity. Once they experience trust, they are happy to reciprocate (Willinger et al., 2003, p. 461). German institutions, here meaning an association or organization which represents the views of a larger number of people, strongly support the notion of trust (Bachmann and Inkpen, 2011, p. 285). They set norms how to behave and not to exploit one's partner, which stabilizes trust even more within the German society. On an HR level, labor unions can positively or negatively influence trust. The German economic structure has been characterized by strong labor unions, yet they never rioted enough to damage the trusting relation between workers and management. Thus, Germany is known as fairly high-trusting compared to the nation's neighboring countries (Fukuyama, 1995, pp. 216-217; Willinger et al., 2003, p. 459), yet not as much as the Land of the Rising Sun. The Japanese are predisposed to trust because of the Japanese traditional family structure and their ancient system of feudalism (Fukuyama, 1995, p. 151). They have made many good experiences with their faithful attitudes (Sako, 1998, p. 15) and researchers attribute Japan's economic success partly to their trusting behavior (Hagen and Choe, 1998, p. 589). One very important example is the keiretsu, the trusting system of banks, buyers and suppliers (Sako, 1998, p. 15; Fukuyama, 1995, p. 162; Hagen and Choe, 1998, p. 589; Yamagishi and Yamagishi, 1994, p. 141). They have helped revive and empower Japan's economy, as seen in chapter 4.5. These results fueled by trust have led the Japanese people to deeply embed trust into their mind. When they conduct business, they predict their partner to make an effort in both parties' best interest and to resist opportunistic possibilities. This faithful spirit contributes greatly to successful business alliances. While German partnerships are usually considered horizontally, meaning the different parties to be equal in power, Japanese are structured vertically, following a strict hierarchical order. Nonetheless, Japanese readily confide information in any level of the organization which secures a free flow of knowledge regardless the unequal distribution of power (Maeda and Miyahara, 2003, p. 309; Saeki and Horak, 2014, p. 1433). Even time-consuming communication is welcome to show one cares to transfer information correctly (Turpin, 1993, p. 14). Omitting any kind of material is seen

as a clear sign of dishonesty, which leads to distrust (Kuwabara et al., 2014, p. 44). On an HR level, Japanese trust is reflected in lifetime employment (Yamagishi and Yamagishi, 1994, p. 141). Employers believe in their workers to stay until retirement, to put in their best effort for the company, and to successfully integrate in the workforce. At the same time, the employee can be sure that his company will not fire him, unless there is an unavoidable reason. This contract shows the Japanese faith in mutual good will. The last aspect about trust in Japan in comparison to the western world is concerned with how essential long-term commitment is to Japanese. Researchers found that trust violations are even acceptable at the beginning of a relationship as long as trustworthiness can be proven in the long-run. Later violations have a much deeper impact on Japanese and cannot be forgiven. The alliance will be immediately terminated (Kuwabara et al., 2014, p. 356). In conclusion, both countries have a history of trust yet the Japanese way is much more profound and farsighted. The next chapter highlights the special role of collectivism in terms of trust in Japan.

## **10.2. Collectivism and Trust in Japan**

Many researchers have tried to find out how Japanese managed to establish such a high level of trust within their society. As described before, one important influence factor on trust is culture. More specifically, the dimension of collectivism eases the introduction of mutual trust. As typical for this dimension, trust is not simply an inherent value of the Japanese mind, led by altruism. The Japanese society is founded on an extensive system of mutual monitoring (Griffith et al., 2006, p. 7; Yamagishi et al., 1998, p. 169). In everyday life as much as at work, people observe each other and scan whether the environment is complying with norms of behavior (Kuwabara et al., 2014, p. 349). As illustrated in chapter 9.8.2, mutual monitoring and evaluation is a common feature of Japanese HR. When actions outside the accepted norms are found, according sanctions follow (Hagen and Choe, 1998, p. 591). Thus, abiding rules and behaving in line with the mainstream is a simple mean to gain and maintain acceptance as part of a group. Members of a collectivistic society value their group highly. They have a strong desire to belong and at the same time believe they can gain from their integration in a society (Yamagishi et al., 1998, p.168). Therefore, they will take any action required to keep their acceptance and to contribute to the group's good. As trust has been established as part of Japan's culture since long ago, Japanese ascertain to display trustworthy behavior in order to show their respect for the group's values. This notion renders trust a stable and deeply-embedded value of Japanese society. It spreads throughout all levels

of hierarchies. As mentioned before, compared to other countries, in Japan even top management members are expected to show their respect for the nation's virtues. Hence, if a high-ranking executive infringes society's norms, he will face appropriate consequences. This system supports the employee's faith in his superior (Hagen and Choe, 1998, p. 592). It adds to a beneficial, harmonious environment at work. Another factor, which benefits the sustainability of trust, is Japan's education system. Japanese students' level of education at the end of high school is comparably similar. They receive a fairly uniform education throughout the country including social standards. They learn to follow the society's rules (Hagen and Choe, 1998, p. 592). Therefore, employers hiring new graduates can be certain of their level of knowledge and integrity which promotes the trust of a superior in his team (Yamamura, 2010, p. 5). In summary, academics attribute the magnitude of trust in Japan to their systems of social monitoring paired with their uniform education and their collectivistic desire to be part of a group.

### **10.3. Signaling Trust**

Generally, both, Japan and Germany, provide a beneficial environment for trust to flourish. They have a strict system of laws which inhibit exploration, paired with the Japanese avoidance of litigation trust is continuously promoted (Hagen and Choe, 1998, p. 591). Further, trust-breaking customs are fairly rare. Corruption, for example, is comparably low in Germany as well as in Japan. Both countries reject corrupt behavior and honor honest values. Existing corruption is mainly limited to the highest levels of politics and economics, such as bribery within the iron triangle in Japan or among high government officials in Germany. There is very little petty corruption (Rothacher, 2003, p. 117; McKay, 2003, pp. 53-55). Both societies lean towards morality and sincerity. However, in order to start an alliance based on trust, both parties first have to ensure each other's trustworthiness. Thus, the next important question economists faced is how to signal trust in different societies. The following three methods have been recognized as most efficient in Japan and Germany.

#### **10.3.1. Commitment**

As explained in chapter 7.5, one way of communicating one's willingness to enter an honest alliance is showing commitment. However, empirical evidence suggests that commitment as a signal of trust only works in Germany (Sako, 1998, p. 19). For example in the manufacturing sector, German firms usually try to reduce their risk by entering business

relationships with several suppliers (Saeki and Horak, 2014, p. 1441). They close contracts on a rather open basis. Yet, if one firm decides to conclude a long-term oriented, big contract with just one firm, it is a clear sign, they believe in their supplier to fulfill his task on a satisfactory level over a long period of time (Sako, 1998, p. 19). In Japan in contrast, long-term commitment to just one supplier is rather expected (Saeki and Horak, 2014, p. 1441). For the uncertainty avoidant Japanese, grouping and commitment are important tools to create a more predictable future (Griffith et al., 2006, p. 9). “Commitment to the group and harmony” (Griffith et al., 2006, p. 23) are two pillars of Japan’s society. Thus, a manufacturer showing commitment towards one single supplier is not a signal of trust but simply customary. Nonetheless, there is a clear connection between commitment and trust (Griffith et al., 2006, p. 8). Commitment facilitates the sharing of information. Especially, in an organization, if one promises to stay with the company for his lifetime, the firm does not need to worry about information leaking to a competitor after the employee leaves the firm. Therefore, the corporation can promote extensive communication among all staff members. Exchange lets people know more about each other, which reduces mystery and enhances trust (Griffith et al., 2006, p. 23). More trust results in more open sharing of personal details. Thus, commitment induces an upward spiral towards trust and is hence, if not as signal then still a contributing factor, essential for a faithful partnership.

### **10.3.2. Reputation**

The next important mean often used in Japan and Germany to show trustworthiness is reputation (Burchell and Wilkinson, 1997, p. 224; Yamagishi and Yamagishi, 1994, p. 139). This can be both a reputation built on the evaluation by other firms, and the reputation which was established during previous, possibly less intensive exchanges. Creating and maintaining a functioning network can be very useful in order to show one’s trustworthiness. Especially in Japan, a wide range of trusting business partners is highly valued. Japanese believe only a truly sincere firm can develop an extensive network. Small firms as much as big firms need to convince many other firms that they can be trusted in order to prove their trustworthiness. In this sense small companies can become equally powerful as big corporations (Hagen and Choe, 1998, p. 595; Kuwabara, 2014, p. 349). Furthermore, because of mutual monitoring not just on an individual but also on a corporate level, a network of allying firms becomes a sanctioning system (Yamagishi and Yamagishi, 1994, p. 139). If a firm betrays the trust of another firm, it will face consequences not simply concerning this one company but it risks to lose touch in its entire network. Thus, in Japan the alliance with many firms increases the

chance of the company to conduct honest business. Germans also appreciate externally provided reputation; however, they prefer internally, self-acquired knowledge about the firm (Burchell and Willkinson, 1997, p. 224). They first investigate about the potential partner firm, its experience, its network. If the firm seems trustworthy, they will enter an alliance. Interestingly, Burchell and Willkinson (1997) found out that firms even after their trust was betrayed do not necessarily cancel an alliance but try to cover for possible future untrustworthy behavior by introducing respective contractual structures (p. 225). This supports the notion that German firms only gain inherent trust through their experience. They observe whether contractual obligations are met, the quality and price of the product fulfills their expectations, and whether the alliance partner shows extra effort to contribute to the joint success (Burchell and Willkinson, 1997, pp. 226-228). In the end, they develop “knowledge-based trust” (Yamagishi and Yamagishi, 1994, p. 153). In conclusion, both Germany and Japan respect reputation, yet in Japan the externally attained reputation is more important while Germans cherish the internally collected information.

### **10.3.3. Personal Relationships versus Professionalism**

The following method to gain trust is one very particular to the Japanese culture. As described in chapter 9.8.2, one typical feature of Japanese business is personal relationships. These are of major importance on the path towards a trusting relationship (Yamagishi and Yamagishi, 1994, p. 153; Saeki and Horak, 2014, p. 1441). In Germany in contrast, they may lead to hampering conditions. When negotiating with a potential partner firm or simply introducing a new member to the staff, Japanese are very keen on establishing not just a business but also a personal connection. During after work activities, they enjoy drinking together, getting to know each other, and sharing personal stories (Saeki and Horak, 2014, p. 1442). When preparing an alliance with a firm, they meet many times before signing a contract not only in company facilities but also in a more private environment (Haghirian, 2010, p. 70). Japanese consider being open about one’s private life to show sincerity and honesty. They project these traits onto business conduction and thus assume the newly acquainted to be trustworthy. For them, business without a personal bond is unimaginable. On the contrary, when entering a long-term alliance, the two parties are bound to become friends also on a personal level as they will share many years of interaction (Saeki and Horak, 2014, p. 1442). Germans in contrast prefer to strictly separate professional and private life. Drunkenness in front of a business partner is a clear sign, this person cannot be trusted. By the same token, drinking in front of a superior is unacceptable (Saeki and Horak, 2014, p. 1442).

Private information is only shared on a need-to-know basis or with colleagues who are also considered friends. For Germans professional skills are a more appropriate signal of trustworthiness (Saeki and Horak, 2014, p. 1444). Considering personal relations, the notion of how to establish trust points towards opposite directions. Thus, it is the most critical part when trying to form a new alliance between a Japanese and a German consulting firm.

#### **10.4. Trust in Foreigners**

So far, Japanese have won the battle of trustworthiness. They are more inclined to trust a new business partner as much as they have a wider range of signals to show their own trustworthiness. This result, however, reverts as soon as foreigners enter the picture. Japanese are very faithful towards their own nationals yet suspicious of foreigners (Yamagishi and Yamagishi, 1994, p. 146) which is why in an international alliance Germans exert a higher level of trust. In Japan trust is tightly connected with in-group membership. If a potential partner belongs to the in-group of a person, he is willing to easily believe in that partner without acquiring much further information. People of one group are usually ethnically similar, share important virtues and respect the same values (Huff and Kelley, 2003, p. 84). In an international alliance, the candidate firm is not even part of one of the widest groups a person can feel a belonging to. Therefore, it is more difficult to trust this person. This applies to the workers and the management of two companies of different nations. It becomes more difficult for them to understand each other's way of thought and predict each other's actions. In addition, Japanese take great pride in their history of producing high quality products but also preserving traditional manufacturing businesses (Haghirian, 2010, p. 69). As a result, they find it challenging to rely on foreign products and services. In addition, when working with out-group members, the sanctioning mechanisms which force Japanese to comply with the rules and exert trustworthy as well as trusting behavior cease. The social enforcement is missing. Thus, the Japanese are not simply suspicious because of the unknown products, but also because they are no longer forced to be faithful (Kuwabara et al., 2014, p. 249). One way for foreign businesses to enter a trusting relationship is become part of the in-group<sup>31</sup> which they may achieve by signaling trust as described above (Griffith et al., 2006, p. 24). In contrast to the Japanese, Germans do not change their level of trust regardless their opposite. Since Germans embody a fairly trusting nature, their faith in foreigners has been declared as

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<sup>31</sup> Between becoming part of the in-group and gaining a firm's trust, it seems difficult to decide which comes first. When trust is attained one should become part of the in-group, when someone is part of the in-group, trust is assured. The two achievements will occur concurrently.

higher than that of the Japanese (Sako, 1998, p. 9). Researchers have discovered that one reason why many Western countries do not distinguish between locals and foreigners in their trust is their mobility. In contrast to Japan, there is no lifetime employment in Europe or America. People change jobs several times throughout their professional life, often voluntarily. The place of living shifts; the circle of friends fluctuates. Every time they enter a new phase of life, they need to adapt to a new place, make new acquaintances, and create new relationships. In order to achieve happiness and feel comfortable in their surroundings most people depend on human contacts and friendship, both at work and in private. Hence, they need to learn to trust faster and have faith in a variety of people (Macy and Sato, 2002, p. 7215; Wang and Leung, 2010, p. 1530). This may be one of the reasons why in an international negotiation, the German party will be better prepared to establish a trusting relationship than the Japanese party who has spent their lifetime under continuous, sustaining circumstances.

### **10.5. Trust Arranges Contracts**

In the case of contracts one can observe very well the dynamic influence of trust and how it varies among different countries. Trust guides how managers draw up contracts, how concrete to describe the content, and is concurrently dependent on the country of origin of the two participants of the transaction. As illustrated above, Japanese are generally supposed to be more trusting than Germans are. Therefore, they tend to design less-detailed contracts. They trust the opposite party will act in all conscience. There seems to be no need to cover every risk of exploitation since they are sure the new partner will have the alliance's best outcome in mind when taking action (Sullivan et al., 1981, p. 805; Ballon, 1992, p. 122). In Japanese style business a contract is preceded by a long period of negotiation which involves not just the top management but many hierarchical levels. During this time, the company can slowly evaluate whether it is willing to enter a long-term commitment with the firm in question (Matsushita and Schönebaum, 1989, p. 47). By the time a Japanese firm decides to sign a contract, the management has made very sure the future partner is credible and responsible. If doubtful acts occur during the negotiations, the attempt to join business will fail (Hayashi, 1988, p. 123). The certainty that the partner will be a firm of honor and virtue allows Japanese firms to accept loser contracts. German companies in contrast value detailed contracts (Ballon, 1992, p. 122). They are used to contracts being one mean among others to protect the firm's vulnerabilities. Germans are faster to conclude contracts although trustworthiness has not

been entirely proven yet, which leads them to demand concrete encoding of all obligations, permissions, and prohibitions included in the alliance. Strict regulations help them in case of a conflict. They can use the written word in court to defend themselves. Japanese tend to avoid litigation and thus rather turn to conferral than arbitration (Sullivan et al., 1981, p. 812). This leads to intensive communication among Japanese alliances (Saeki and Horak, 2014, p. 1442). In addition, in the Japanese mind detailed written explanations are a sign of distrust. This faithful comportment of the people of Japan changes, when foreigners get involved in the transaction. Their knowledge of the Westerner's love of detailed contracts and their mistrust towards foreign products lead them to demand for arbitration (Ballon, 1992, p. 122; Sullivan et al., 1981, p. 805). To safeguard themselves from unfavorable circumstances in case the foreign party decides to induce legal procedures, the Japanese firm banishes its faithful spirit and adapts to the more suspicious Western culture. As mentioned before, it might even become less trusting than its counterpart. In summary, with trust follow loose contracts but the less trusting relationship of an international alliance demands for detailed content within the agreement.

Trust is a virtue honored in Japan and Germany. Yet, it takes different forms, is signaled in different ways, and in the case of Japan changes in case a foreign party is involved in the transaction. Japan's collectivism leads Japanese to be deeply trusting towards their in-group members yet renders them highly suspicious of out-group members such as Germans. Germans in contrast are not as trusting as Japanese yet do not change their attitude according to their opposite's country of origin. This conflict in addition to the very different ways of signaling trustworthiness renders the development of a trusting relationship in a Japanese-German business alliance very difficult.

The following chapters will now use the propositions developed in the chapters 5-7 and the information about Japan and Germany provided in the chapters 8-10 to determine the most efficient market entry mode for a German consulting firm entering the Japanese market.

## **11. Analysis**

The chapters above have systematically collected information about market entry in terms of an institution-based, culture-based, and a trust-based view. Subsequently, they have presented the different features of Japan and Germany. These collections now serve as a base to analyze which entry mode is best for a German consulting firm entering Japan and, when

chosen one, which risks to consider. The chapter separately analyzes the institutional, the cultural and the trust-based perspective, generates a result for each, so that the final analysis can combine the three single findings. Before checking the before derived propositions, however, this chapter will take a quick look at market entry in terms of service firms. In case the three individual findings do not agree, in order to derive a conclusion, it is important to consider which type of influence (institutions, culture or trust) is most significant. Thereafter, the chapter moves on to checking the propositions and finding the most efficient market entry mode.

### **11.1. Service Firms and Market Entry**

Up until now, most studies are based on researching manufacturing firms. The intensification of the third sector induced academics to investigate whether results change when using service firms as sample companies instead. They concluded that they usually do not; however, the points of most influence shift from resource access and technical furnishing towards local market knowledge and effective staff management.

Morschett et al. (2010) tested the results of six different studies conducted on manufacturing firms to find out whether these results would change using service firms. Four studies produced insignificant results, one vouched for no difference, one, in contrast, proved a clear difference. In conclusion, they did not generate clear findings (p. 70). However, many academics emphasize how arguments of choosing a market entry mode change when expanding as a service company (Ekeledo and Siyakumar, 2004, p. 69; Erramilli and Rao, 1993, p. 23). The amount of resources and technical facilities needed decrease. Thus, it is easier, even for a small firm, to enter a foreign market due to smaller necessary seed money (Ekeledo and Siyakumar, 2004, p. 81). Also, less access of local resources renders service firms less vulnerable towards political changes or environmental interest groups (Brouthers and Brouthers, 2003, p. 1196). Nonetheless, in case of a very unstable political or economic environment, a low risk mode, such as an alliance, is recommended, posing no difference to the case of a manufacturing firm (Erramilli and Rao, 1993, p. 32).

In comparison to the above mentioned points, there are also arguments which complicate the market entry of a service firm in comparison to a manufacturing firm. For example, in order to cover a large market share, the service needs to be provided at many

places. Thus, a multiple entry may become necessary<sup>32</sup> (Ekeledo and Siyakumar, 2004, p. 81). Another aspect is highly idiosyncratic services. Erramilli and Rao (1993) define idiosyncratic service “as one which is characterized by ‘high’ levels of professional skills, specialized know-how, and customization” (p. 24). A service firm’s competitive advantage lies in their abilities, their strategies, and their expertise. For the most part, these are difficult to protect by patent, which is why it is of absolute importance, to find personnel who is able to transfer and efficiently use these capabilities (Ekeledo and Siyakumar, 2004, p. 80; Erramilli and Rao, 1993, p. 24; Brouthers and Brouthers, 2003, p. 1181). The integration and management of home and local staff are a highly prioritized task for the HR department. In addition, idiosyncratic services increase the risk of opportunistic behavior which is why extensive monitoring or a relationship of trust needs to be established, either within a WOS or in a JV (Brouthers and Brouthers, 2003, p. 1185; Erramilli and Rao, 1993, p. 25). In summary, internal procedures are an important element for a service firm to consider when expanding into a new market. Even more decisive is, however, the knowledge of the local market. This may result in part from the “non-seperability” (Erramilli and Rao, 1993, p. 25) characteristic of consulting services (Glückler, 2006, p. 375). The service is produced and sold at the same time and place (Ekeledo and Siyakumar, 2004, p. 70). The consultant discusses the client’s needs and with the help of his own and his coworkers’ market knowledge, he finds and implements a solution. Therefore, he has to not simply know the market but requires intuition how to interact with local customers (Anand and Delios, 1997, p. 583; Ekeledo and Siyakumar, 2004, p. 82). The firms should integrate into the local market. Local staffs, as well as creating a network are two important tools to facilitate this process (Anand and Delios, 1997, p. 594; Ekeledo and Siyakumar, 2004, p. 83).

In conclusion, entry mode choices do not differ vastly between manufacturing and service firms. Nonetheless, service offering companies require much more attention towards internal integration and external assimilation. The importance of adaptation to the local customs and the frequent human interaction of consulting firms highlight the effect culture and trust have on the success of a market entry (Brouthers and Brouthers, 2003, p. 1196). This finding leads to the following decision. In the following, the propositions are used to determine the ideal market entry mode. If the results of the institutional analysis contradict those of the cultural analysis, the latter will be taken as viable. This includes the value of adjusting to the local market.

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<sup>32</sup> This point, however, does not apply to consulting firms, since consultants have a habit of travelling to their clients and do not require an office in the immediate vicinity.

## 11.2. Results of the Institutional Analysis

This chapter systematically examines the propositions derived in chapter 5 to find out which market entry is most recommendable from an institutional perspective. The chapters 8 and 9 provide the information for all the comparisons made. The final examination of the institution-based propositions suggests a greenfield investment as most effective market entry mode.

The first proposition of this thesis concerns the restrictions on the ownership level. Such restrictions could narrow the choice of possible modes to enter Japan. In the past, market entries were very restricted, such as the permission of only partial foreign ownership, which rendered WOS impossible. These restrictions were lifted for the most part until 1976 (Ito and Fukao, 2001, p. TF19). The system then changed to requiring prior notification before any type of IFDI could be conducted in order to give the MOFA an opportunity to prevent unwanted acquisitions. But these boundaries were also eliminated in 1992 by introducing ex post notification (Lawrence, 1993, pp. 94-94; Ito and Fukao, 2001, p. TF19). In addition, critical demographics, meaning an aging population and a very low birth rate, force Japan to be more open towards IFDI and incoming labor force (Blomstroem et al., 2000, p. 6). Hence, they strengthen their support for foreign market entrants as well as tighten competition (Blomstroem et al., 2000, p. 9). Obstacles such as the iron triangle, a nontransparent legal system with a lack of legal support and strict visa applications remain. Nonetheless, there are no direct restrictions on IFDI which leads to the first result.

*Result 1: There are no restrictions on ownership level for foreign entrants; thus, the choice of market entry modes is not limited.*

The second proposition requires an examination of the regulatory distance between Japan and Germany. A small distance allows for the company to choose a high control mode, yet if the distance is high a JV will be necessary to overcome regulatory obstacles. As described before, the general set-up of the two countries' economic, political and legal system does not differ vastly. Both nations build their economic success on export of high quality goods. In the past, Japan has taken Germany and France as model to create their law and their constitution. Both countries were influenced by the Americans after WWII. Albeit the influence was stronger in Japan than in Germany, Japan tried to orientate itself towards Europe thereafter. The iron triangle is a feature specific for the Land of the Rising Sun, but proposition 2 is more concerned with the legal framework, whether an action permitted in

Germany would also be permitted in Japan. This can be answered positively because of Japan's gearing towards Germany in terms of legal structure.

*Result 2: The small regulatory distance between Japan and Germany suggests a wholly-owned or majority-owned market entry mode.*

The third proposition examines how far a country has proceeded through the institutionalization process. The further a country is institutionalized the more likely a firm is to choose a high control mode as their investments are less risky. Japan is a fully institutionalized country (Kevenhörster, 2010, p. 290). Although the Prime Minister has changed often, Japan represents a politically stable parliamentary monarchy. Therefore, the third result is easy to derive.

*Result 3: The completed process of institutionalization in Japan renders a WOS likely to be successful.*

The fourth proposition studies which mode previous entrants of the same industry chose. Choosing the same mode can help overcome cognitive distances as locals expect the new entrant to enter through such a mode. Being able to anticipate the newcomer's actions triggers a feeling of security in the locals' mind and leaves them more open towards accepting the new entrant. Unfortunately, there are no exhaustive records on how consulting firms have entered Japan in the past. JETRO has published eleven articles about successful entries by consulting firms from the US, France, Italy, and Australia. Eight of them describe greenfield investments, the other three were joint venture.<sup>33</sup> A first intuition is, therefore, that past entrants mainly relied on greenfield investment. However, this being a very small sample, biased by the fact that they were all projects supported by JETRO, a more complete study is necessary to determine the result of proposition 4. As such an empirical study would go beyond the scope of this thesis, proposition four will be left out at this point and be proposed for future research.

The fifth proposition inspects the need for internal legitimacy. The higher this need the more helpful becomes a JV. From a regulatory point of view, irrespective of the country, the alliance with a local successful firm is a useful tool to justify a market entry. It helps to gain internal understanding and support. When the employees recognize the new partner firm's success, they will be more likely to put their effort in expanding into the new market.

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<sup>33</sup> Appendix I – History of Market Entry to Japan by Consulting Firms presents a table which gives a more detailed overview of the past entries to Japan supported by JETRO.

However, since this thesis scrutinizes the entry of a consulting firm, external legitimacy is prioritized over internal legitimacy. To highlight the difference in priority, I will introduce a difference in wording. Up until this point all propositions “suggest” a certain type of entry mode. The word “suggest” will be replaced by “guide” as these propositions rather than suggesting a market entry mode, only guide the company in a certain direction. During the final analysis, these results will be given lower priority in case of an indefinite finding.

*Result 5: The need for internal legitimacy of a consulting firm guides towards a joint venture as market entry mode.*

The sixth and the seventh proposition explore the normative and the cognitive distance between Japan and Germany. If the normative distance is high, in order to integrate into local society, a JV is beneficial. If, however, a WOS is chosen nonetheless, in case the normative and the cognitive distance are high, a greenfield investment can help to avoid conflicts between the local and the home workforce. As a reminder: the normative distance describes the difference in values and mindset which includes a difference in culture. The cognitive distance labels the congruence between expected and exerted behavior. The steps a corporation takes are characterized by their employees and managers cultural background, traditions, and customs. Hence, in order to estimate the normative and the cognitive difference between Japan and Germany, this chapter will anticipate the following chapter in its cultural analysis. On a societal level the two countries have gone through very different historic developments. The Germans’ traditions and ethics were steadily influenced by Christian values. Japanese were divided into Shinto, Buddhists, and Atheists. Thus, it is no surprise that the two people significantly vary according to Hofstede’s five dimensions. In terms of power distance, both countries scored in the lower half of the spectrum of countries, although both people believe in clear hierarchical structures. In Japan, however, the superior has to consider his subordinates’ and coworkers’ best interest at all times and is hereby restrained in his decision making. The Germans, in contrast, rely on giving orders, yet leaving sufficient scope for action for the subordinate to maneuver independently. In summary, according to the dimension of power distance, the two countries are close on a normative level, as they both trust in hierarchies, yet the superior is limited in his orders. On a cognitive level, in contrast, they differ as the restraints emerge from different behaviors. One considers his peers’ benefits; the other one needs to maintain flexibility in his orders.

In terms of individualism and collectivism, Germany and Japan clearly belong to different ends of the spectrum, with Japan being the group-oriented one. Germans work

towards their own goals and enjoy their individual success. Japanese, in comparison, prioritize the group and are only satisfied when their group profits from their efforts. In addition, this dimension influences communication. While Germans directly speak what is on their mind, Japanese interpret information in a context as they are used to viewing individuals not as single piece but as part of a whole group. To conclude, according to Hofstede's second dimension, Japan and Germany differ both on a normative as well as a cognitive level. They are different in how they view themselves as much as in how they act because of their views.

Considering masculinity, Japan and Germany both show tendencies towards masculinity, albeit the former does so in a much more pronounced manner. Culturally masculine people emphasize challenges and exert themselves as much as necessary in order to achieve their goals. Germans are of moderate nature in that they still try to balance their work and their private life. Masculinity further implicates a belief in conventional gender roles. In Japan, women are rarely seen on a career track within a firm. Germany faces similar developments, again to a lesser extent. In summary, both from a normative as well as a cognitive view the two countries differ in terms of Hofstede's dimension of masculinity.

In light of uncertainty avoidance, Japan scored again one of the highest throughout the world. In order to cope with their fear of the unknown, they resort to rules and regulations. They obey by the law, honor their traditions, and expect foreigners to respect these customs. Germans, also leaning towards uncertainty avoidance, resort to extensive planning in order to reduce risks. In spite of their similar tendencies, Germany scoring much lower on Hofstede's scale infers a great normative gap. Nonetheless, the two people honor similar behavior such as punctuality, keeping promises, and honesty in business, which renders them close on a cognitive level.

Hofstede's last dimension, long-term or short-term orientation, clearly illustrates the difference between Japan and Germany. While Japanese work steadily towards a greater goal, Germans prioritize soon to earn profits. This provides further support for the normative and cognitive distance between the two countries.

Taken all the results derived from analyzing Hofstede's dimensions together, Japan and Germany are evidently different on a normative and on a cognitive level. Chapter 9 provides further details to support these finding. Japan is a homogenous country, valuing peace and harmony and thus shying away from open conflict. Germany, in contrast, is more heterogeneous as well as they do not mind to openly address a difference in opinion. Further,

they are reluctant to accept change in terms of new technologies, while the Japanese are open for new ideas as long as they do not clash with their traditions. Lastly, Japanese appreciate networks much more than Germans do, and see them as indispensable part of the economy. The discrepancy in their cultures, values, traditions, and their behavior serves as deciding factor for the last two propositions of the institutional chapter.

*Result 6: The high normative distance between Japan and Germany suggests a JV as efficient market entry mode.*

*Result 7: Among high control modes, the high cognitive and normative distance between Japan and Germany suggests to choose a greenfield investment above an acquisition.*

In summary, propositions 2 and 3 recommend a WOS; proposition 6 suggests a joint venture. Proposition 5 guides towards a JV, however, since two propositions suggest a high control mode, the alliance in contrast is suggested only once and once only indicated in a weaker form, the institutional chapter suggests a high control mode as most efficient. Proposition 7 then delivers the final decision as it decides on a greenfield investment among the high control modes. In conclusion, a greenfield investment as market entry mode is most recommendable from an institutional point of view. Little regulatory differences and the inexistence of ownership restrictions allow companies to choose a high control mode of entry. The possibility of a high control mode is always beneficial for a company as it can reap the entire profits made. The main risk is the cognitive and the normative distance between Japan and Germany. Those will be more deeply included in the following chapter. However, among the high control modes, they shift the result towards a greenfield investment in order to avoid the clash between local and home workforce, as well as to secure the integrity of the corporate strategy. Therefore, the analysis of the regulatory, normative and cognitive institutional differences finally suggests a greenfield investment as market entry mode.

### **11.3. Results of the Cultural Analysis**

Following the institutional perspective, this chapter inspects the propositions concerning culture. The most important aspect to conduct the following research is the national cultural distance between Germany and Japan. As seen in the chapter before, the two countries can be defined as culturally distant according to Hofstede's dimensions of culture. Practical examples taken from everyday life further support this result. Based on this premise, the following nine propositions guide the German consulting firm to enter Japan by a WOS.

The eighth proposition of this thesis examines the interaction between cultural distance and the security of a foreign investment, meaning as how stable the political and economic environment of the targeted market can be described. Instability in addition to cultural distance suggests a joint venture to reduce the risk of entry. Japan can be characterized as a stable market. As seen in the historical chapter, Japan has not changed much politically since the American occupation period. The economy of Japan, in contrast, is currently caught in an ongoing stagnation. Despite this, Japan still maintains its high living standard, its high price levels, and thus is still a profitable market to enter, as mentioned in the introduction. Hence, Japan's market is stable. At the same time, it is culturally distant. Future coworkers from the home and the host country will have to put effort into working together. Open communication, tolerance, and explaining of one's own premises are of utmost importance (Hayashi, 1988, p. 57). In summary, Germany and Japan culturally seen different, but the Japanese market is stable. Hence, the first proposition concerning culture does not guide a market entrant either way. Secure investments do not induce a preference towards a WOS or a JV.

*Result 8: The high cultural distance between Japan and Germany combined with the security of foreign investments in Japan neither suggests a JV nor a WOS as market entry mode.*

The ninth proposition studies the interaction of high cultural distance and the need for local expertise and external isomorphism. If both are high, a JV can facilitate the market entry. When entering a new country, the entrant is seen as the foreigner, an outsider. He has to overcome the liability of foreignness. To achieve this, he needs to acquire as profound market knowledge as possible and adapt to the local customs and traditions. He needs to fulfill the locals' expectations. These requirements are especially important for a service firm. As described at the beginning of the analysis, for a service firm and particularly a consulting firm, expert knowledge about the local market is indispensable in order to find a suitable solution for the client. Concurrently, the consultant needs to internalize the local culture in order to communicate efficiently with his customers and establish a relation of trust. The liability of foreignness is the biggest challenge a consultant faces. Therefore, he will exert all his efforts in order to blend into society and be respected for his expertise. Learning the Japanese language and integrating into a culture (Brody, 2000, p. 168) which is highly suspicious of foreign products is, nonetheless, very difficult and may take a long time. Therefore, help from locals can be highly advantageous. The combination of a consulting firm's crucial requirement to integrate into the local culture and the Japanese's tendency to reject

foreignness renders proposition 9 as one of the most important aspects of entering the Japanese market.

*Result 9: The high cultural distance between Japan and Germany and the need for local expertise as well as external isomorphism of a consulting firm suggest a JV as market entry mode.*

The four following propositions analyze which effect cultural distance has in combination with the need for internal legitimacy and extensive knowledge transfer. If both are high, a WOS eases the market entry as it facilitates the communication between local and home employees. Depending whether internal or external legitimacy is of higher priority, a greenfield investment or an acquisition respectively may be more beneficial. In case a company's competitive advantage is built on specific business practices and successful business relies on perfect information transmission, an internal mode is recommended. As described before, Japanese, being collectivists, see themselves as part of a group. Thus, they interpret information as part of a context. Germans, in contrast being individualists, see themselves as single person. Therefore, they use only the information they receive and directly communicate their needs. As a result, the exchange of information between the two people can be hampered.

*Result 10: The high cultural distance between Japan and Germany and the need for internal legitimacy as well as intensive knowledge transfer of consulting firms render a JV less preferable as a market entry mode, yet do not suspend it.*

*Result 11: The high cultural distance between Japan and Germany and the need for unobstructed, complete information transfer of a consulting firm guide towards a WOS.*

*Result 12: Among high control modes, the high cultural distance between Japan and Germany and the need for unobstructed, complete information transfer of a consulting firm guide towards a greenfield investment.*

The thirteens proposition is more easily to apply to the case of a consulting firm. The topic is still the interaction of high cultural distance and internal integrity, but this time, this element is set into perspective regarding external integration. A consulting firm needs to transfer its business practices to the newly entered market, yet the knowledge and adaption to the local market are more important which leads to the following finding.

*Result 13: Among high control modes, the high cultural distance between Japan and Germany and, apart from high internal consent, the need for external conformity of a consulting firm suggests an acquisition as market entry mode.*

The fourteenth proposition shifts away from the national culture and turns to examine the organizational culture. While the latter is influenced by the former, its impact needs to be viewed separately. Strongly differing organizational cultures recommend a greenfield investment to avoid the clash of local and home culture. Organizational culture describes characteristics such as decision-making authority, infrastructures, and distribution of responsibility. On the one hand, companies based in Japan and Germany are culturally distant since they embrace very different values and prefer varying structures. Japanese are long-term orientated working towards a greater goal, while Germans demand fast profits. As mentioned before, the language and the type of communication are different, as to how to interpret received information. Japanese try to maintain harmonious collaborations at all costs, while Germans do not shy away from open conflict. On the other hand, the gap between the two nations widens even more because of Japan's unique economic features. These are, for example, the iron triangle or the HR system, including lifetime employment, seniority-based pay and extensive group work. Different hierarchies and distribution of responsibilities can hamper efficient communication and thus complicate a joint venture (Ballon, 1992, p. 125). The Japanese's identification with the workplace, rooting in their collectivist nature, disrupts acquisitions. A change of the company's core may lead employees to lose this feeling of identity, which eliminates their motivation to work efficiently (Lawrence, 1993, p. 92). The specificity of the Japanese economy has begun and will continue to gradually change, because of the demographic situation as well as Japan trying to maintain their position as a global player (Blomstroem et al., 2000, p. 7). However, these predictions will not come true in the near future, which is why proposition 14 produces the following conclusion.

*Result 14: The extensively varying organizational cultures, and particularly HR structures, of Japan and Germany suggest a greenfield investment as market entry mode.*

The last two propositions relate to the culture of the home country, here being Germany. The first concerns Hofstede's dimension of power distance. A company based in a country appreciating hierarchies will try to transfer these distributions of power to the new market and therefore choose a WOS. Germany, however, does not score very high on the scale of power distance. While they benefit from hierarchies, they still appreciate responsibilities and room for maneuvering.

*Result 15: The lack of power distance in Germany neither suggests a JV nor a WOS as market entry mode.*

The sixteenth proposition identifies the level of uncertainty avoidance of Germany. Depending on how well people cope with unexpected situations or events they have never experienced before, one entry mode becomes more suitable than another. Germany counts as an uncertainty avoidant country, yet among these, they belong to the moderate fraction. Therefore, a high control mode may be helpful, nevertheless dispensable.

*Result 16: Germany's uncertainty avoidance guides companies towards a WOS as market entry mode.*

To summarize, the analysis of the cultural perspective on market entry generates a surprising result. Proposition 9, one of the most important propositions since it combines the cultural distance between Japan and Germany with a consulting firm's need for external legitimacy, suggests a JV as most efficient market entry mode. This idea supports a first intuition of an alliance being most preferable as many researchers have pointed out how important it is for a service firm to integrate into the local market. However, the number of propositions indicating a different entry mode is so high, it changes the result. Proposition 10 renders a JV less preferable and propositions 14 and 16 specifically suggest a WOS, the former particularly recommending a greenfield investment. Proposition 11, too, guides towards a WOS. Therefore, just as the institutional analysis, also the cultural research suggests a WOS as most efficient market entry mode. The need for internal legitimacy, organizational culture distance, and the uncertainty avoidance of Germans induced these findings. Among high control modes, proposition 14 recommends a greenfield investment, proposition 13 in contrast indicates an acquisition as most beneficial. While the different organizational cultures and internal legitimacy induce a greenfield investment, the need for local market knowledge pushes to acquire an experienced company. There is no unequivocal result. In conclusion, there is no final finding as if to choose a greenfield investment or an acquisition. Nonetheless, the cultural analysis supports the finding of the institutional perspective to choose a WOS as market entry mode.

#### **11.4. Results of the Trust-based Analysis**

The last of the three factors to influence the market entry choice is trust. Trust contributes significantly in case resources are interdependent (Luo, 2002, p. 677). The main

resources of consulting firms are knowledge and skills. Business knowledge and local cultural knowledge need to be combined, which renders trust indispensable. Moreover, the notion of trust is especially important for joint ventures (Haak and Haak, 2008, p. 112), but can also help in case of an acquisition. When acquiring a firm, former staff can only be kept if the management can trust them to work efficiently for the new owner. In case of a greenfield investment, trust is not as necessary. In conclusion, the mode being most in need of trust is a joint venture. It requires two firms to share resources and information. They need to trust in order to confide in each other. Because of the significance of shared resources, chapter 7 has derived four propositions on a resource-based view. Examining these generates that between Germany and Japan, only the semi-strong form of trust is likely to occur. The strong form of trust will be difficult to establish.

As explained, trust does not suggest a certain market entry mode but can help to facilitate. The first proposition concerning trust is based on semi-strong trust. Two firms can use market-based governance to enter a business alliance. Each firm needs to create a network. If a company can attain a good reputation this way, a potential partner may categorize the company as trustworthy. Japanese strongly value extensive networks. A corporation within a web of trusting alliances will avoid risking its position within this structure, and hence refrain from dishonest business. Thus in Japan, a network serves as a proof of trustworthiness. Germans, in turn, believe in reputation. A large number of firms vouching for the potential partner's trustworthiness are a significant signal.

*Result 17: The Japanese's and Germans' belief in market-based governance suggests the possibility of a JV.*

The eighteenth proposition studies contractual governance. The well-developed legal systems of Japan and Germany support drawing up and enforcing contracts. However, as described in the literature review, the legal section concerning IFDI is not as sophisticated just yet. In addition, Japanese appreciate loose contracts which represent an alliance of trust, while Germans prefer to go into detail in order to cover all eventualities. The German version, however, repels Japanese to commence business, as they favor trusting relationships. Adding the general obstacle of incomplete contracts, contractual governance is unlikely to be successful.

*Result 18: The difference between Japanese and German contracting suggests contractual governance to be inefficient.*

The nineteenth proposition researches about the effect of society-based governance. If lying is generally defied in a society, firms are likely to behave in a trustworthy manner. On the one hand, members of the company are also members of the society, thus valuing honesty. On the other hand, the corporation will not risk of creating a scandal, and hence the loss of market shares, which opportunistic behavior might entail. Both, Japan and Germany are known to be countries of high moral values. They despise dishonesty and betrayal. Their ethics teach them not to exploit. In summary, society-based governance makes Japanese and Germans trustworthy, yet not necessarily trusting. The positive impact on a business alliance, nonetheless, remains.

*Result 19: The Japanese's and Germans' belief in society-based governance suggests the possibility of a JV.*

The twentieth proposition analyzes the strong form of trust. As mentioned, Japan and Germany are both countries of high trust, which triggers a first intuition that the strongest form of trust is easily established between companies originating in these two countries. Japanese and Germans believe in committed, long-term alliances, even if Japanese do so to a higher degree. Their cultures support this notion. Trust and culture are closely intertwined. Even though cultural distance is said to matter only during the trust building process and once two firms trust each other, their home culture will lose its influence (Luo, 2002, p. 686). Culture can still serve as measurement to estimate the potential partner's trustworthiness. As mentioned, power distance is a sign of low trust, as managers believe in close monitoring. However, both countries do not score too high in this category and especially Germans' custom for superiors to cede a certain amount of responsibility to their subordinates demonstrates their trusting behavior.<sup>34</sup> Uncertainty avoidance is also a clear sign of a high trust society. In order to avoid uncertain situations, firms try to maintain business with the partner they are used to. Therefore, they will conduct honest and trustworthy business. Japanese, being highly uncertainty avoidant, but also Germans, leaning towards uncertainty avoidance, both belong to this group. They value continuous, predictable developments, and

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<sup>34</sup> As this chapter follows the order of chapter 6, the dimension of masculinity and femininity should succeed. However, the results would be misleading. The argument of this dimension is that members of a feminine culture are more trustworthy as they look for harmony and peace. As a result, they will refrain from exploitative behavior in order to maintain harmonious relationships. Japanese, being highly masculine, would thus be labeled highly untrustworthy. However, as chapter 9.6 describes, Japanese deeply treasure harmony and amicability and would therefore certainly avoid deceiving their peers. Their high scores on the masculinity scale stem from other features such as their high work ethics and their belief in conventional gender roles. Germans are also on the masculine side, yet not as pronounced as the Japanese. Their high scores in uncertainty avoidance and their moderate points of the other three dimensions support them being trustworthy and trusting, yet not to the extent Japanese are.

hence display integer behavior to secure their alliances. The last dimension to be discussed is the one of collectivism and individualism<sup>35</sup>. Generally, members of collectivist cultures are known to be more trusting. They all work towards the same goal of being accepted in a group and once achieving this goal, from thereon, foster this acceptance. This includes sincere behavior. Hence, all the members of the group can be sure of each other to be trustworthy. At first sight, this presents Japanese as the more trusting people. Germans scoring higher on the individualism scale cannot be as sure of their peers' integrity and thus trust less. However, this result only holds in case of a purely Japanese alliance. As soon as a foreign party is involved, this dimension is the reason for the findings to perform a 180 degrees turn. The trust collectivists exert is only directed towards in-group members. It is not an inherent trust, but a trust fueled by the fear of being expelled from the group and at the same by the security for everyone else to suffer the same fear. These two factors disappear in a transaction with an out-group member. Added the Japanese's fear of the unknown, rooting in their high uncertainty avoidance, and the pride they take in their locally manufactured goods and services, instead of being trustful, they become highly suspicious when entering a foreign alliance. Germans, on the other hand, usually do not distinguish between an alliance with a German or a foreign party. The mobility and their proximity with many different foreign countries have desensitized them. Nonetheless, as they expect corporations from collectivist countries such as Japan to have prejudices against any firm not from their own country, the German's level of suspicion may be heightened as well (Yamagishi et al., 1998, p. 321). The question remains, if there are strong enough tools to develop a trusting relationship despite the heightened suspicion.

As chapter 7.5 illustrated, one task on the path to a trusting business alliance is to convince all the members of a firm to trust the new partner. In a collectivist culture, this can be achieved by the leaders functioning as role models. In an individualist culture, managers need to set appropriate incentives. The greater task is to establish the trust between the two companies coming from different cultural backgrounds. Chapter 7.5 named the first mean to be time. In case of a market entry of a service firm, this is difficult to undertake. There is little possibility to first work together on a loose base, such as exporting, until trust is established. The second method is to maintain a good reputation as a signal of one's trustworthiness for the potential partner. This is again difficult to apply as a German firm entering the Japanese

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<sup>35</sup> There are no empirical findings on the interaction between long-term and short-term orientation and trust. Nonetheless, it can be speculated that long-term orientation is an indicator of a trustworthy partner, as he is interested in maintaining a long healthy relationship. This would again underline Japan's higher propensity to trust.

market would demand the Japanese firm to rely on foreign references. Their suspicion towards strangers might complicate this method. The best option is to exert trustful behavior for the opposite to reciprocate and concurrently to make efforts to prove one's trustworthiness by showing one's "honesty", "accountability", "consideration of others' interests", and "transparency" (Trapscott, 2006, p. 1). The former, however, takes a lot of courage and is only possible if one party is already prepared to trust. Japanese and Germans being both suspicious are unlikely to have this courage. Proving one's integrity thus represents the more useful choice. From a German point of view, commitment is an appropriate signal. Signing a long-term contract is a demonstration of a company's good intentions. In Japan, however, a long-term contract is the norm. Therefore, it is expected and does not function as a convincing argument. In Japan, managers rather rely on building a personal relationship with the responsible representatives of the future alliance partner. This approach, in turn, is not appreciated by the Germans, as they consider personal relationships at work as unprofessional.

To summarize, because of their cultural backgrounds, Japanese and Germans are highly suspicious of each other. In order to overcome this skepticism, companies of the two countries would employ very different techniques. They are improbable to find a common denominator, which significantly complicates the development of the strong form of trust<sup>36</sup>.

*Result 20: The difference between the Japanese's and the Germans' attitude towards trust suggests the establishment of a strong form of trust to be unlikely.*

In conclusion, the semi-strong form of trust is attainable and contributes to an easier implementation of a joint venture. However, the semi-strong form of trust is not as deeply embedded and durable as the strong form; hence a WOS, particularly a greenfield investment, is a possibility to avoid the dilemma of a lack of trust.

This chapter about trust shall conclude the analysis. Having tested all the propositions the following chapter will summarize the findings and extract the final result.

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<sup>36</sup> One must keep in mind that this is a purely theoretical approach. In practice, it is still possible to establish a strong form trust relationship if both parties are willing to have faith. Compared to other two geographically distant countries, Japan and Germany might even have an easier time as they are both known for their integrity. Nonetheless, theoretical findings do not depict an easy path towards the strong form of trust which is why the proposition 20 cannot be answered positively.

## 12. Final Result

After analyzing twenty propositions concerning the institutions, the culture and the trust-based views of Japan and Germany, this chapter draws a final conclusion which entry mode is most suitable for a German consulting company expanding to Japan. Moreover, it points out the advantages and risks entailed by this solution.

As seen above, both the institutional perspective as well as the cultural perspective suggests a WOS as entry mode. Since both recommend the same mode, a final conclusion to choose a high control mode is easily drawn. There are no legal hindrances, thus the German headquarter can exert full control over the new subsidiary in Japan, information transfer is unobstructed, and a conflict between two firms' different corporate cultures is prevented. A WOS goes in line with the trust-based perspective which illustrates that a joint venture based on the strong-form of trust is difficult to realize. While a semi-strong form of trust is possible, this does not facilitate an alliance as much as the strong form would. In terms of which high control mode of market entry to choose, the cultural analysis is inconclusive, however, the institutional study produces a clear sign towards a greenfield investment. This helps to avoid internal conflicts. The company can choose Japanese workers who, although being distant on a normative and a cognitive level, are willing to adapt to the German corporate culture. This finding matches the trust-based view as it omits the challenge of building a trusting relationship. The advantages of this decision are manifold. The consulting firm can bring its own corporate culture to Japan and needs to employ few internal changes. It can find a compromise between the specific Japanese HR system and its own and it can hire local staff which is able to bridge the cultural gap between Germany and Japan. Most importantly, the company does not need to share its profits. Yet the German market entrant has to keep one big risk in mind. The company needs to find a way to adapt to the local market. It needs to convince suspicious Japanese potential clients of its reliability, its trustworthiness, and its quality work. Integration is generally important, yet particularly challenging in Japan. To recapture a few examples, for unobstructed communication, consultants in Japan need to learn the language. An extensive network is needed as business affiliations are highly valued. A network means both a business network, as well as the integration into the iron triangle, which is a substantial part of the Japanese market. In order to build up a network, it helps to hire experienced Japanese managers who have connections and market insights. However to win them over, the consulting firm first has to convince them to leave their position of lifetime employment. In addition, to conduct efficient consulting a deep understanding of how

Japanese businesses work is necessary. The liability of foreignness will remain an important obstacle the market entrant has to calcite. Nonetheless, hiring locals and conducting extensive market as well as cultural research will help to overcome these hurdles.

The final result of this thesis is that a German consulting firm entering the Japanese market should use a greenfield investment as market entry mode. It can benefit from the internal advantages of unobstructed information and little change of the corporate culture, and with these in mind face the challenge of integrating into the local market.

### **13. Conclusion and Future Outlook**

Entering the Japanese market is a challenge but at the same time a chance for German consulting firms. Price levels are high and the demand for foreign investments increases (METI, 2014). Institutional barriers are low; on the contrary, the Japanese government tries to attract foreign entrants. This thesis has studied which market entry mode is most recommendable for a German consulting company which chooses to do so. Three topics, namely institutional differences, cultural distance, and trust-based views were tested in detail. They help to examine, which type of entry mode best balances high control and internal communication with equity commitment and external integration. The final conclusion drawn is to choose a greenfield investment. There are no restrictions on ownership for foreign entrants in Japan, the Japanese market is one of low risk, and the legal structures of Japan and Germany follow similar ideals. Therefore, a German market entrant can use a high control mode. Further, a greenfield investment prevents inner-firm conflicts, which are likely to occur because of Japan's very unique organizational culture. Entering by a greenfield investment offers the chance of balancing the local with the home corporate culture. The entrant can hire locals who are willing to bridge cultural gaps. Lastly, a greenfield investment eliminates the trust-based conflict of members of two different firms. Japanese are highly suspicious of foreign alliance partners. They believe in the superiority of Japanese goods and services, as much as they expect foreigners to display untrustworthy behavior. For these reasons a greenfield investment can be concluded as the most efficient market entry mode for a German consulting firm entering Japan. Concurrently, a greenfield investment entails one important risk. It does not solve the liability of foreignness, which is why the representatives going to Japan will have to intensively prepare their journey. They will have to learn the language and internalize the culture in order to overcome suspicion and distrust. Additionally, hiring

experienced locals is crucial. Considering this risk and putting special efforts into overcoming this liability, a German consulting firm should be able to successfully establish a subsidiary in Japan.

In the future, more intensive research about the service sector is recommendable. Academics still focus on manufacturing when studying market entry (Morschett et al., 2010, p. 71), although a large part of today's international movements occurs in the tertiary sector. Japan joined this development since WWII (Blomstroem et al., 2000, p. 3). Therefore, more elaborate studies on the service sector itself or on whether results between the service sector and the manufacturing sector differ significantly, respectively, could provide further conclusions what market entry mode a service offering firm should choose. In addition, an empirical analysis about past entries to Japan divided by type of industry would support any research related to entry experience. When looking for past entries to Japan by consulting firms, there was little information to be found. Hence, research subdividing types of services could provide information for future case studies as well as give an impression how market entry changes within the service sector. Lastly, an evaluation which type of influence is most crucial when a service firm decides on a market entry mode. This study is based on the premises that institutions, trust and culture are most important for a third sector company as it has to manage intensive human interaction. However, other factors such as the availability of trained personnel or market information, thereby moving back to a more resource-based view, or entry experience may be just as essential. A comparison of these different influencing factors could shed light on which factors to pay most attention to. Market entry will stay an important topic as the world moves closer together which creates much room for future research.

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## Appendix I – History of Market Entry to Japan by Consulting Firms

**Table 6: Past Entries to Japan by Consulting Firms**

<b>Company</b>	<b>Country of Origin</b>	<b>Year of Entry</b>	<b>Entry Mode</b>
Advisory Reseach, Inc.	USA	2012	Greenfield
Sisvel S.p.A.	Italy	2007	Greenfield
Reach Local, Inc.	USA	2011	Greenfield
Carmichael and Fisher International Pty Ltd.	Australia	2010	Greenfield
ZS Associates Group, Inc.	USA	2003	Greenfield
Elanex	USA	2003	Greenfield
Gemba Research	USA	2006	Greenfield
Japan Australia Corporation	Australia	2003	Greenfield
Trend Union	France	2007	JV
IMS Research	USA	n/a	JV
Osha Liang LLP	USA	2008	JV

Note: Adapted from JETRO (2015b, 2015c, 2015d)

## **Appendix II - Abstract**

This study examines which market entry mode is most efficient considering the case of a hypothetical German consulting firm entering the Japanese market. Japan is a very interesting market for its high price level and its need for foreign investments to revive its stagnating economy. Germany, on the other hand, is a strong economy and a worldwide investor. Until the beginning of the 2000s, Germany was one of Europe's main investors to Japan, yet during the past twelve years Germany's investments stagnated. Nonetheless, the Japanese market yields substantial benefits especially in the service sector, as it is the fastest growing with high price standards. Therefore, this thesis considers the case of a consulting firm which belongs to the third sector, and concurrently, can help future German entrants from other industries to be successful in Japan. To find the most efficient market entry mode, the study, on the one hand, examines formal characteristics such as the institutional distance and the legal environment of Japan to clarify limitations on ownership and highlights which actors of the Japanese institution need most consideration. On the other hand, the study evaluates informal characteristics such as culture and views on trust to calculate how well interpersonal relationships between home and host country staff will develop. After deriving twenty theoretical propositions about the interaction between market entry and institution, culture, and trust, the study tests these proposition on the basis of a market entry from Germany to Japan. The analysis of the institutional environment of Japan and Germany yields a greenfield investment to be most beneficial. Almost no restrictions on ownership and the similarity of their institutional set-ups allow for a high control entry mode. The analysis of cultural distance and the great difference in the perception of trust also render a wholly owned subsidiary most beneficial. The cultural dimensions of Japan and Germany are very different, which complicates communication and the development of trust. Thus in a joint venture, employees of two culturally diverse backgrounds have to interact, trust, and exchange sensible information, although they are used to different business cultures as well as communication styles. A wholly owned subsidiary in contrast, and in particular a greenfield investment, allows for the company to hire local staff which fits the corporate culture. This ensures an unobstructed flow of information and avoids conflicts caused by a lack of trust between two business partners. Nonetheless, the results of the analysis caution to apply particular attention to overcoming cultural differences, when dealing with local customers and integrating into the local market. In summary, a greenfield investment is the most efficient

market entry mode for a German consulting firm entering the Japanese market, assuming high efforts to adapt to local clients' needs.

## **Appendix III – Zusammenfassung**

Diese Studie untersucht welche Markteintrittsstrategie sich im Falle eines hypothetischen Consultingunternehmens deutscher Herkunft am besten für einen Markteintritt in Japan eignet. Japan ist ein sehr interessanter Markt. Er hält seit vielen Jahren ein hohes Preisniveau und präsentiert sich aufgrund der stagnierenden ökonomischen Entwicklung attraktiv für ausländische Investoren. Deutschland, auf der anderen Seite, ist für seine starke Wirtschaft und als weltweiter Investor bekannt. Bis Anfang der 2000er wurden viele der deutschen Investitionen nach Japan gelenkt, doch diese Tendenz nahm in den letzten zwölf Jahren ab, obwohl der japanische Markt nach wie vor als ein profitabler für deutsche Unternehmen eingestuft werden kann. Besonders im dritten Sektor glänzt er durch starkes Wachstum und hohe Preisstandards. Aus diesem Grund beschäftigt sich diese Studie mit einem Consultingunternehmen, was zu diesem Sektor zählt, jedoch auch gleichzeitig zukünftigen deutschen Unternehmen aus anderen Wirtschaftszweigen bei ihrem Eintritt in den japanischen Markt helfen kann. Um die effizienteste Markteintrittsstrategie zu finden, untersucht diese Arbeit zum einen formelle Charakteristika, wie zum Beispiel institutionelle Unterschiede und die Gesetzgebung Japans, um mögliche Eigentumsrestriktionen auszuschließen und herauszufinden, welche institutionellen Akteure in Japan besonderer Beachtung bedürfen. Zum anderen untersucht die Studie informelle Charakteristika, wie Kultur und die Einstellung zu Vertrauen, um die zwischenmenschliche Entwicklung zwischen den lokalen Mitarbeitern und denen des Mutterkonzerns einzuschätzen. Um diese Eigenschaften zu untersuchen, leitet die Studie zwanzig theoretische Aussagen über die Wechselbeziehung zwischen Markteintritt und Institution, Kultur und Vertrauen her und testet diese anhand des Beispiels eines Markteintritts von Deutschland nach Japan. Die Analyse der institutionellen Begebenheiten ergibt, dass eine Greenfield Investition sich am besten eignet. Da in Japan Eigentumsrestriktionen fast gänzlich eliminiert wurden und die institutionelle Organisation Deutschlands derer Japans ähnelt, ist eine Neugründung eines Unternehmens unter Lenkung der Muttergesellschaft möglich. Auch die Analyse der kulturellen Distanz und der sehr unterschiedlichen Einstellungen gegenüber Vertrauen empfiehlt eine hundertprozentige Tochtergesellschaft. Die großen kulturellen Unterschiede zwischen Japan und Deutschland erschweren die Kommunikation und den Aufbau eines Vertrauensverhältnisses. In einer Joint Venture müssen Mitarbeiter sehr verschiedener kultureller Hintergründe zusammenarbeiten, einander vertrauen und sensitive Informationen austauschen, obwohl sie sehr unterschiedliche Arbeitskulturen und Kommunikationsstile

gewöhnt sind. In einer hundertprozentigen Tochtergesellschaft und insbesondere einer Greenfield Investition kann die Firma lokale Mitarbeiter suchen, die bereit sind sich der Firmenkultur anzupassen, um so einen ungehinderten Informationsfluss sicher zu stellen, und außerdem Konflikte aufgrund eines unzureichenden Vertrauensverhältnisses zweier Businesspartner zu vermeiden. Nichtsdestotrotz warnen die Ergebnisse der Studie, dass kulturelle Unterschiede bei der Arbeit mit lokalen Klienten und bei der Integration in den lokalen Markt besonderer Beachtung bedürfen. Zusammengefasst schlägt die Studie demnach ein Greenfield Investment als die optimale Markteintrittsstrategie für ein deutsches Consultingunternehmen, das nach Japan expandiert, vor, vorausgesetzt das Unternehmen passt sich den Bedürfnissen der lokalen Klienten an.

## Appendix IV - Curriculum Vitae

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### Education

- 03/2013 – 10/2015 Master in International Business University of Vienna, Austria  
focusing on
- International management
  - Innovation and technology management
- 10/2008 – 07/2012 Bachelor in Global Business Management University of Augsburg,  
Germany  
focusing on
- International management
  - Human resource management
  - Japanese
  - GPA 2.2 (equivalent of an overall “A” grade average)
- 07/2008 Abitur (approximately equivalent to A-levels), Sophie-Barat-Schule,  
Hamburg, Germany
- GPA 1.7 (equivalent of an overall “A+” grade average)

### Work Experience

- 05/2013 – 07/2014 Kursalon Hübner  
Part-time work
- Sold tickets as well as informed costumers about concerts, the restaurant and events at the Kursalon
  - Corresponded with travel agents
  - Office work (event scheduling, internal communication)
- 08/2012 – 02/2013 Nissan Center Europe GmbH  
Internship Human Resources
- Self-responsibly organized and conducted the entire hiring process of other interns
  - Helped attending interviewing candidates
  - Created and introduced a weekly newsletter
  - Drafted reference letters

- 11/2011 – 04/2012 Gran Education Technology and Science Co. Ltd, Guangzhou, China  
Internship
- English teaching
  - Helped during the hiring process by representing the firm at personnel fairs and interviewed candidates
  - Conducted an employee satisfaction survey

### **Foreign Experience**

- 09/2014 – 07/2015 Graduate Exchange Program at the Waseda University, Tokyo, Japan
- 09/2010 – 04/2011 Japan and East Asia Studies Program at the Kwansai Gakuin University, Nishinomiya, Japan
- 07/2005 – 06/2006 EF-High School Year at the Eisenhower High School, Lawton, Oklahoma, USA

### **Language Skills**

German (native)  
English (business level)  
Japanese (speaking: fluent; writing: intermediate)  
French (conversational level)  
Italian (beginner level)

### **Extra-Curricular Activities**

- 08/2011 – 04/2012 Member of the student organization AIESEC
- Participated in internship program
  - Represented interns at events for cooperating firms
- 01/2010 – 08/2010 Member of the student organization AEGEE
- Organized the “Summer University” program for international students
  - Led and trained a group of international students on intercultural understanding
- 10/2008 – 01/2010 Member of the management of the Global Business e.V.
- Introduced and organized the “Social Day” (now an annual event)
  - Appointed to advocate my degree program at various events
  - Proposed and evaluated suggestions to improve the degree program Global Business Management with professors

## **Appendix V - Eidesstattliche Erklärung**

„Ich erkläre hiermit an Eides statt, dass ich die vorliegende Arbeit selbstständig und ohne Benutzung anderer als der angegebenen Hilfsmittel angefertigt habe. Die aus fremden Quellen direkt oder indirekt übernommenen Gedanken sind als solche kenntlich gemacht.

Die Arbeit wurde bisher in gleicher oder ähnlicher Form keiner anderen Prüfungsbehörde vorgelegt und auch noch nicht veröffentlicht.“

Marlen Valerie Nels

Wien, im Dezember 2015