

# COMPARATIVE STUDY ON INTER-ORGANIZATIONAL RELATIONS BETWEEN KEIRETSU AND PARTNERING

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**ABSTRACT:** Partnering has taken root all over the world as a remedy for the adversarial relation between parties concerned with construction projects. It is deemed to be derived from Keiretsu in Japan where parties related cooperate with one another as a team gaining reputations for completing projects on schedule and budget while maintaining high standard of quality. However, Keiretsu is now being weakened in proportion to the economic recession and there is an important change that needs to happen in the industry. The aims of this study are to find out the essence of Keiretsu by comparing Keiretsu with Partnering and to look for the direction of the reform plan.

*Key words :* Keiretsu, Partnering, inter-organizational relation, partnership, alliance

## 1. INTRODUCTION

Keiretsu is one of the relations among the enterprises in the management system of the Japanese type. It is pointed out that competition is obstructed, and that dealings are shut by Keiretsu, whereas Keiretsu is evaluated as having fairly good economic rationality. In other words, the Japanese manufacturing industry can get worldwide competitiveness by the existence of Keiretsu.

As for the construction industry, Keiretsu exists as well. Keiretsu brought high ability of cost control, schedule management, and quality control, and that is the reason why the people of the worldwide pay attention to construction management in Japan.

The stakeholders in construction industry in Western countries have hostile relations, which brings inefficient control, such as cost overrun and schedule delay. There are specially too many disputes and suits, which is considered to be a serious problem.

So, partnering was introduced as cooperative relations, and the solution was planned in the Western countries. It brought a good result, and partnering has been used widely. It is deemed that Keiretsu in Japan spread abroad as partnering.

The domestic construction market of Japan is sluggish in recent years. General contractors and specialist subcontractors are now exhausted by the excessive competition of the price. They have the serious risk to go bankrupt. It is also the clients' risk that an excessive burden is applied to the contractors, because VFM (Value for Money) and the ability to keep the period of construction work may not be assured in such cases.

A change has been occurring in Keiretsu, which is the

source of the competitiveness of the Japanese construction industry, such that Subcontractors' groups stop working. It is necessary to reform the relations among the stakeholders.

## 2. KEIRETSU IN JAPAN

### 2.1 Keiretsu

Keiretsu in the construction industry means only the relations between the vertical enterprises such as certain big general contractors and their subsidiary companies and the subcontractors. It doesn't necessarily have direct relevance as for the group of the enterprises. Therefore, keiretsu is divided into two types: one is the vertical affiliation which includes Keiretsu in production system and in procurement; another is Keiretsu in the markets which are equal to the Japanese corporate group.

### 2.2 Financial conglomerate

Financial conglomerate had been developed from the end of 19<sup>th</sup> century. It is the enterprise group with the layered structure around the holding company. The big 4 (*Mitsui, Mitsubishi, Sumitomo, Yasuda*) had big financial power around before World War II. They were dismantled as a part of the economic democratization reform after the war.

Only as few general contractors have extension with the financial conglomerate and most of them are founded by individuals.

### 2.3 Corporate group

Corporate group generally includes the relations made from the financial conglomerate, e.g. *Sumitomo-Mitsui, Mitsubishi*, and the relations around a bank, e.g. *Mizuho*

(former *Fuyo* and *Dai-Ichi Kangyo*) and *UFJ*.

The member of the corporate group is evaluated by the right to attend the presidents' meeting, the ratio of the stock combination and the loan dependence on the main bank. It is important in the corporate group in construction industry to deal within the group.

**2.4 Finance loan affiliation**

A financial affiliation is composed by the bank, including the financial agency other than bank, and the main loan customers. That is considered to be an aggregate of the financial relations with the bank and the enterprise. Relations between the borrower enterprises which have the same main bank are included in this affiliation.

A bank has very intimate relations with general contractors. Therefore, as for the construction industry, dealings are often closed exclusively in the same financial affiliation by the leadership of the main bank.

**2.5 Production affiliation**

A production affiliation is formed around a certain company in the cases as follows: the group of enterprises which are merged by the main company, a newborn group of subsidiary companies by the spin-off strategy of the main company, supply dealer and subcontract enterprises.

The subcontractor's meeting and the layered structure of subcontract organized by the general contractor is deemed to be a kind of production affiliation in the construction industry. There is the one that is related to the capital between the enterprises in the subcontractor's meeting, and there also exists the one that has no capital relation remaining in dealings and the relation in the technology. Therefore, Keiretsu in the construction industry can be classified as follows:

- Special command order to general contractor by enterprise that belongs to the same corporate group
- Deal among enterprises that belong to the same finance affiliation.
- Special command order by capital relation in corporate group.
- Regular relation among general contractor, specialist subcontractor and supplier in subcontractor's meeting

**3. KEIRETSU IN CONSTRUCTION INDUSTRY**

**3.1 Keiretsu in market**

Keiretsu in market was historically approved because of the relation between the owner and the general contractor.

In the relation between the owner and the general contractor of Japan, the following consideration exists.

The end of the 19<sup>th</sup> century contract work has become active in Japan. In those days, the contract between the general contractor and the government office was unequal. There were dealings of rule and subordination in the undertaking contract. The government office who was a big client did the construction order while considering humanity. The government office thought construction to be "Gave it", and the general contractor thought construction to be "Get it". The owner was called "*Oseshusama* (Dear Honorable Customer)".

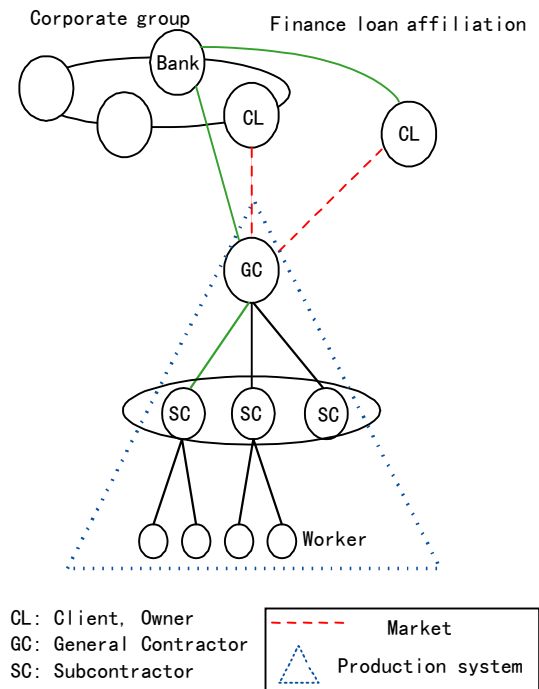
There was a powerful economic support in the succeeding general contractor regardless of government and big private companies. This shows that the owner had big power for the general contractor.

One of the points of the relations is emphasis on the human trust. For example, it was decided that Fujita Corporation yielded a big deficit by the contracted construction due to the rise in price of the price. Client accepts the additional charge as for Fujita Corporation. Though additional payment was taken, the president Ichiro Fujita paid back to the client. Because that greeting was respectable, the client was impressed. Like this, there was an age when the expansion of trust was taken seriously more than loss and gain of the construction cost.

**3.2 Keiretsu in production system**

It is the existence of the cooperation meeting as an exclusive subcontract whom layered subcontract system and the registered owner who faces the special principal contractor of that organized in the center that produces the flexible execution system of the production affiliation.

Construction became large-scale after the second decade of 20<sup>th</sup> century. Before that the production mechanism was: the general contractor - master worker - worker, or the general contractor - subcontractor - dealer - worker. It had changed into: the general contractor - subcontractor - big dealer - dealer - worker, or the general contractor - subcontractor - big dealer - dealer - *boshin* (worker in chief) - worker.



**Figure 1.** Keiretsu in construction industry

The general contractor builder fixed the nominee, and left the labor force procurement, management, and construction to the nominee in this making to the superposition. The general contractor secured the construction demand, the

construction capital, and the construction component. Such a mutual-dependence relation was built. This strong dealings led to organizing of the subcontract.

The main contractor had to select an excellent subcontractor, and to secure it. The main contractor came to start the subcontractor's organizing, and for specific main contractor's cooperation association to be formed centering on the nominee from such a backdrop. Such an activity is done in most main contractors, and the existence of the cooperation association is a general contractor today and a source of special construction trader's regular dealings.

## **4. PARTNERING IN CONSTRUCTION INDUSTRY**

### **4.1 Partnering**

Among the definitions of partnering, CII (The Construction Industry Institute) gives the typical definition as follows [1]:

*Partnering is a long term commitment between two or more organizations for the purpose of achieving specific business objectives by maximizing the effectiveness of each of the participant's resources. The relationship is based on trust, dedication to common goals, and an understanding of each other's individual expectations and values.*

In the United Kingdom there is a definition as follows [2]:

*Partnering is a managerial approach used by two or more organizations to achieve specific business objectives by maximizing the effectiveness of each participant's resources. The approach is based on mutual objectives, an agreed method of problem resolution and an active search for continuous measurable improvements.*

### **4.2 Background of partnering**

Partnering came to be adopted in the United States and the United Kingdom as a possible relief act to the serious problem.

There was frequent cost excess because of a severe price competition bid, the relations contracted in opposition, and the non-efficient control. The period of construction work also delayed. It caused excessive number of suits.

Partnering was introduced into the construction procurement first in the United States. When the construction project was executed, lawsuits of an excessive number had been generated in the United States. There was hostile business relationship of the inter-firm behind that. Partnering came to be used in the U.S. military to solve these dealings. It has widely spread to the army, the navy, and the road agency, etc.

There was an excessive price competition in the United Kingdom. There were a term of works delay and a charge increase in the construction project, and the excessive loss became a problem.

Sir Latham proposed the introduction of partnering in the government advisory panel aiming at the cancellation of the conflict of industry segments in 1994 (Latham Report).

In addition, Sir Egan announced "Rethinking Construction" aiming at the quality and the efficiency reform in 1998 (Egan Report). As a result, partnering was promoted

and spread in the United Kingdom.

### **4.3 Partnering and contract**

Partnering, which is deemed to be a way of management, is not a kind of the contract system in the United States. Normal construction contract form is used in the project where partnering is operated.

The standard contract provision (in such cases as NEC, the European Economic Community and the PPC2000 provision) which made partnering which was traditionally different from the contract method a base has been adopted..

### **4.4 Validity of partnering**

A decrease in complaint, a cost cut, period of construction work shortening, improvement in the quality, and so on are shown as the advantage.

On the other hand, it is consistency with the existent system that a legal right duty makes fear to the collusion of the cooperative relations, responsibility by this clear as a disadvantage.

And, penetrability, legal grounds, dispute management are sometimes concerned as a problem.

It can be said that partnering is effective if it is used for the place of the recognition not to be heal-all never, the relevancy.

## **5. RELATIONS IN CONSTRUCTION INDUSTRY**

### **5.1 Keiretsu and partnering**

As for the strong point seen in partnering, it is mostly secured as for Keiretsu as well. Many differences are found at the same time.

A difference is the point to that the procedure is indicated clearly supported by the system and the tool in partnering, whereas Keiretsu is not clear.

The general contractor is valued in the cost management, the VFM achievement, the risk management, the process management, and the innovation activity in Keiretsu. These activities are executed tacit.

On the other hand, the procedure is secured for fairness with the articulation in the partnering. This is especially remarkable in the United Kingdom. In partnering, various tools or systems are used. These are the one customized to suit the system and the business practice there when Keiretsu spreads from Japan to the two countries. The problem was corrected though the merit of Keiretsu had been left as it was. Therefore, the profitable one exists as a means to cancel the problem of the affiliate in the partnering.

### **5.2 Problems in construction industry**

There are some problems around Keiretsu in construction industry in Japan.

The owner concerns less to the project. Cost control, risk management, innovation activities, are often left for the general contractor. As the contract is unequal to each other, fairness should be secured. The organization of subcontractors loses flexibility.

### 5.3 Future relations in construction industry

Keiretsu that was the dealings between subjects in the Japanese style construction production system spread to the United States and the United Kingdom as partnering the recipe to the hostile dealings between subjects. Now, partnering was established as a method natural in the United States and the United Kingdom.

The approach that should be paid attention for the general contractor in Japan exists there. It is necessary to correct the problem of the affiliate referring to the method seen by other systems such as partnering under such a situation.

It fuses Keiretsu in market with Keiretsu in production system by owner's participation. CM, Nominating subcontractors, and the severance order are executed for that.

An open competition is achieved by the diversification of the procurement channel. The net public offering, CALS, and the supply chain construction are introduced for that.

The price, the technology, and the quality are assessed overall, and the technique recognition, ISO, and the Value assessment are used.

Those such as Project Manager and producers who summarize the project fairly are entrusted.

It is necessary for each stakeholder to make the effort to invoke such a method according to the project, and to cancel the problem.

Keiretsu does the basis of the dealings between subjects in the general contractor in Japan in the future. The effort for the amelioration of Keiretsu is extremely important for the owner as well as the general contractor and the subcontractors. It might be able to enjoy such an effort and to enjoy the merit of the affiliate by continuing more.

## 6. CONCLUSIONS

Keiretsu that was the relation between subjects in the Japanese type construction production system spread to the United States and the United Kingdom as partnering the recipe to the hostile relations between subjects.

Keiretsu spreads, and partnering is customized along the system in each country and the introduction purpose, and individual development is made with making use of the strong point which Keiretsu having.

An inter-business relation in the Japanese construction industry must keep evolving to the new system with repeating the discovery, imitation of the new tool and the system due to the interaction with the system that partnering is different.

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