

East Asian Firms Should Let Employees Have External Networks

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66 *Typical East Asian firms have practices that result in their employees operating in closed social and business networks. This closure increases loyalty and productivity. But globalization and increasing competition having at least some employees who can bridge to external networks. Companies need to find ways to recruit, sustain and rewards such employees.*



The typical East Asian firm has such practices as lifetime employment and seniority-based compensation, work responsibilities that extend into the social sphere, and relational contracting with suppliers and buyers. We would certainly not claim that these practices are uniform across all East Asian countries or that there are no significant differences in the practices of the Chinese family and other businesses, Korean chaebol, and Japanese keiretsu. But they do provide a useful contrast with the practices of typical Western firms.

Advantages of the Closed Network

Compared with Western firms, East Asian firms tend to have (1) a closed and dense network of relationships among employees (2) long-term, often effectively permanent, employment for key employees (3) diffuse patterns of interaction that merge work and non-work relationships, and (4) long-term, personalistic relationships with trading partners and government agencies. As a result, employees tend to have closed networks of relatively long-lived, social ties that have great importance for economic outcome. This more closed network generates higher levels of employee commitment and leads to higher levels of work effort. This commitment also provides incentives for firms to invest in worker skills, thus improving the quality as well as quantity of work.

Lifetime employment tends to generate closed networks because individuals do not circulate between firms over their lifespan and, therefore, develop their network of ties internally rather than externally. Likewise, both formal and informal types of lifetime employment encourage employees to be generalists who will occupy a variety of roles within the firm over the course of their careers. This leads to wide circulation across various departments and, therefore, plentiful opportunity to develop wide-ranging, numerous ties within the firm.

In smaller, family-based firms, the institution of lifetime employment is rarely formalized, but the smaller pool of potential workers such firms draw upon would imply that closure is, if anything, stronger. The prototypical example of this is the small Chinese family-owned firm.

East Asian Model firms encourage internal ties and discourage external ones, thus inducing closure of employee networks by (a) generating material disincentives to the formation of outside ties and (b) taking advantage of or generating identification and shared social norms, making each member's own preferences tied to his/her work in the firm. Indeed, one characteristic of the East Asian Model firm is the

breach of the boundary between work activities and social activities. For larger firms that recruit most of their employees from outside the family, this breach does not occur naturally, so it must be generated by institutional practices such as long hours in the office and after-work socializing, which in turn reduces the amount of time available for external networking.

There are advantages for firm productivity from this type of social norm and behavior. Productivity is increased because individuals devote high levels of effort to group production. This group productivity is enhanced by a coordinating norm that instructs one to cooperate with others who have certain characteristics and causes one to expect cooperation in return from such individuals as well. However, the initial decision to enter into a pattern of cooperation depends in large part on trust, which itself depends on pre-existing social norms.

The specific norms that operate within the Chinese family firm would simply be the adage, familiar to any Chinese person regardless of level of education, that one's primary responsibilities are to one's family members: obedience to one's elder kin, benevolence to one's younger kin, and fraternity with one's kin cohort.

Expanding the Closed Network

In an era of global competition, the renowned characteristics of Chinese family firms may be challenged because, by nature, family firms are limited to grow beyond a certain size. However, Chinese family-owned firms seem to have their own ways to perfectly expand their business scope without jeopardizing the uniqueness of family-centered management. One researcher suggests a concept of "family-ization", in which non-family members can be socialized into the family and develop exclusively closed relations with the family. In his case study, he describes how HKToys, a family firm located in Hong Kong, successfully expanded its business into Singapore by developing family-like trust with a non-family employee (family-ization). By facilitating *guanxi* and developing family-like trust, Chinese family firms can internalize non-family members within the existing family boundaries. In that sense, Chinese family firms can make a breakthrough not only by overcoming the limitation of family, but also by securing the advantage of family firms.

While closed networks promote commitment and work effort by individuals and, thus, higher firm productivity, those individuals within an East Asian Model firm who are able to act for a prolonged period as bridges to external networks tend to receive higher individual benefits relative to effort than their fellow employees. However, their ability to be bridges will be dependent on the firm's willingness to exempt them from the sanctions that are typically used to prevent such attempts at bridging to and exploiting external ties. This willingness increases with a firm's need for individuals with special skills, a condition that is becoming increasingly prevalent as East Asian firms enter an era of globalized competition in information-based technology.

However, within some large East Asian Model firms, there are certain individuals, albeit not large in numbers, who have outside business ties that predate their entry into the company. The existence of such prior outside ties indicate an exemption from normal practice, since recruitment for both family firms and large firms practicing formal lifetime employment policies takes place directly out of secondary or tertiary education, and such firms rarely recruit anyone with substantial prior corporate experience. For those employees who are an exception to the rule, there are reasons to expect that they would receive higher levels of benefits relative to effort than their fellow employees. The economic logic of this is fairly simple: members of an otherwise closed group who have strong preexisting outside ties are more likely to have exit options and can credibly threaten to leave if conditions are not to their liking. Hence, as long as

the members in question continue to offer some positive value to the firm, they can leverage such ties to obtain higher individual benefits or get away with lower levels of individual effort than those who do not. Thus, the social capital characteristics that are beneficial to individuals within a group may be harmful to the group productivity overall. Indeed, the more closed a group, the more powerful the leverage provided to those few members of the group who have exit options.

From around the time of the 1997 economic crisis, Korean firms begin to recruit US MBA students through both official and unofficial channels for the purpose of inducing knowledge workers prepared for global competition. This may be understood as Korean firms' effort to overcome the limitations of their traditional employment systems, which may lack opportunities to gain competent external resources. Likewise, many Japanese companies have tried to recruit Japanese students with degrees from US universities in order to overcome the shortcomings of Japan's stereotypical work environment.

The Future of the East Asian Model

The growing numbers of "cosmopolitans" in East Asian firms, who gain advantages from having external ties but escape sanctions because they provide specialized skills or knowledge that the firms need, raises an obvious question: Will there be a convergence over time that will eventually cause the East Asian Model firm to lose its distinctiveness and become more and more like those in the West? While it is always difficult to make general long-term predictions, logical implications of the evolutionary path of East Asian firms suggests that, while change is inevitable, the end result will be a new form that is different from either the current Eastern or Western Models.

Rather than suppressing or encouraging individuals' external ties, the evolution of the East Asian Model in the era of information-based technology will ensure that ties are maintained, not just between buyers and suppliers, but also between competitors within a sector. This will generate interfirm networks of ties that encompass entire sectors.

This version is based on the full article, "Confucian Capitalism and the Paradox of Closure and Structural Holes in East Asian Firms," *Management and Organization Review*, 2010, 6:1, 5-29. Sun-Ki Chai (sunki@hawaii.edu) is Associate Professor, Department of Sociology, University of Hawai'i. Mooweon Rhee (mooweon@hawaii.edu) is Shidler College Distinguished Associate Professor, Associate Professor of Management, and Cooperating Graduate Faculty of Sociology at the University of Hawai'i.