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The Transformation of Governance in Textile, Apparel, and Fashion Value Chains, 1950–2020

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Ph. D. Thesis

The University of Osaka

Graduate School of Economics

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ABSTRACT

This dissertation bridges business history with theoretical perspectives, particularly those of Transaction Cost Economics (TCE), while also drawing on insights from international business, strategic management, marketing, and retailing. The central analytical question concerns how Japanese firms have demonstrated resilience amid the evolution of global capitalism and the development of GVCs. Japan provides an ideal setting for this investigation: its institutional profile has shifted from that of an emerging economy to that of an advanced economy; it has undergone profound industrial transformation in the postwar era; and the keiretsu networks long regarded as a source of Japanese firms' competitiveness largely withered at the turn of the twenty-first century. To trace how these external shifts affect firm-level dynamics, I examined the textile, apparel and fashion sectors, one of the most longstanding, globalized, and dynamic industries. Within this context, I focus on two key actors—sōgō shōsha (highly diversified general trading companies) and department stores.

Originating from institutional foundations laid during the Meiji era, sōgō shōsha, repeatedly redesigned their product, location, and governance portfolios, and continuously negated and reconstructed their historical identity in anticipation of—or in response to—shifting external environments. By contrast, Japanese department stores, whose traditions date back to the Edo period, illustrate the capacity to "not to change" even amid the deepening and widening integration of global capitalism. They have preserved the gaishō clienteling system to sustain credibility and long-term trust with clients. Together, these findings underscore the significance of a dual capacity of adaptive flexibility and structural continuity.

Methodologically, it adopts a history-to-theory approach, which remains uncommon in Japanese business history research still dominated by the Chandlerian paradigm emphasizing managerial hierarchies, or corporate functions. By integrating historical contextualization with the analytical rigor of TCE and employing Bhaskar's critical realism (CR), this study positions history not as a passive narrative backdrop but as an analytical laboratory for theory-building. This method enables the identification of underlying "mechanisms" and causal "forces" shaping governance and strategic decision-making.

Theoretically, this dissertation contributes to the operationalization of TCE in four key ways. First, it deploys TCE dynamically, tracing intertemporal changes in governance rather than treating governance choice as a static, one-off decision. Second, it extends the unit of analysis is extended. By conceptualizing the GVC as a bundle of interdependent firm-level transactions, rather than isolated dyads, the analysis clarifies how firms co-develop governance mechanisms and manage complex interdependencies across actors. Third, it refines key TCE constructs, such as credible commitments (Williamson, 1996), by showing how these are manifested and enacted within multi-actor GVC interdependencies. Finally, the dissertation broadens TCE's scope to the B2C domain by conceptualizing transaction costs at the firm–customer interface as "dream costs," thereby extending TCE's applicability to relational and symbolic exchange contexts in luxury and retail sectors.

CHAPTER 1
INTRODUCTION

1.1. THE CHALLENGE OF GOVERNING GLOBAL VALUE CHAINS

Since the 1960s, global value chains (GVCs) have shaped how production, distribution, and consumption are organized across borders (Cattaneo et al., 2010; Gereffi, 2014). Participation in GVCs has allowed emerging economies to gain easier access to foreign knowledge, technology, and better management practices, which has supported their productivity growth, technology diffusion, and income convergence. These chain-level shifts unfolded within broader transformations in global capitalism—successive waves of trade and investment liberalization and the financial deepening that redefined how multinationals (MNEs) organize, control, and finance international business (Jones, 2005; Dunning & Lundan, 2008; Donzé & Yongue, 2024).

Today, a new round of change is again reshaping GVC governance (Neilson et al., 2015; Kano, 2018). Intensified cross-border linkages and deepened interdependence have accelerated shock transmission, exposing countries and firms to greater uncertainty (Cigna et al., 2022). Under such conditions, firms confront dual behavioral constraints—bounded rationality and bounded reliability—that increasingly determine how governance mechanisms in GVCs are designed and sustained (Kano et al., 2022; Verbeke, 2025).

Within this global context, Japan offers a distinctive vantage point for exploring how firms adapt or innovate governance structures and strategies under uncertainty. Its post-war rise occurred within a complex domestic system (Buckley, 1985), often described as

exhibiting “institutional voids” (Khanna & Palepu, 1997), including multi-layered distribution channels (Yahagi, 2000; Larke & Davis, 2007) and regulatory constraints (Mason, 1992). These conditions created distinctive incentives and constraints for both domestic firms and foreign MNEs, producing governance choices that diverged from those in more liberal market economies and mature institutional environments (Buckley, 1985). At the same time, East Asia’s comparative advantage evolved following the Flying Geese (FG) pattern of industrial upgrading (Akamatsu, 1962; Kojima, 2010; Ozawa, 2011). Japanese manufacturers relocated production abroad to capture market opportunities and manage costs. From the 1990s onward, structural changes—including deepening capital markets, prolonged economic stagnation, and the gradual erosion of business groups or keiretsu networks—often criticized as impediments to market openness—(Shimotani, 2006; Lincoln & Shimotani, 2009), further altered the governance landscape, compelling Japanese players to rethink coordination and control mechanisms across global networks (Donzé & Yongue, 2024).

1.2. TEXTILE, APPAREL, AND FASHION VALUE CHAINS

The textile, apparel, and fashion sectors provide analytically rich contexts for tracking how firms adapt organizational arrangements or innovate governance solutions in response to shifting external environments. These industries are among the oldest, most global, and most structurally dynamic in the world economy (Gereffi & Frederick, 2010). Apparel manufacturing has long served as a springboard for export-oriented development because fixed costs are relatively low and production is labor-intensive (Adhikari & Yamamoto, 2007). Textile production (yarn and fabric) is less so, and upstream segments such as synthetic fibers and machinery are more capital- and technology-intensive, requiring higher investments (Gereffi & Memedovic, 2003; Gereffi & Frederick, 2010). Such heterogeneity in investment requirements across stages of the chain creates differentiated governance

challenges. The finely sliced and geographically dispersed nature of modern value chains amplifies the strategic importance of both location and governance choices (Buckley & Ghauri, 2004; Mudambi, 2008; Buckley, 2009b; Dicken, 2015)

Alongside these conventional segments, two parallel trajectories accelerated in the 1990s as industry logics shifted. First, luxury fashion houses from France moved from family-led maisons toward conglomerate ownership capable of rapid internationalization by leveraging financial and organizational scale (Kapferer et al., 2017; Donzé & Fujioka, 2018). Many Italian "Mittelstand" companies, characterized by entrepreneurial models, also showed convergence (Colli & Merlo, 2007; Merlo, 2018). Japan became a pivotal consumer hub for these Western luxury brands, with Japanese department stores tailoring distribution to local preferences (Donzé & Fujioka, 2018; Isozaki & Donzé, 2022). Second, fast fashion expanded on the back of regional upgrading, using China's liberalization to reconfigure sourcing for improved speed-to-market (Mehrjoo & Pasek, 2016; Cattaneo et al., 2010). The 1997 handover of Hong Kong to China further integrated logistics and supply networks, opening new opportunities—and new governance challenges—within reoriented value chains. Dragon multinationals—notably Hong Kong's Li & Fung (Mathews, 2002)—and Japan's sōgō shōsha linked global buyers, regional suppliers, and local subcontractors, leveraging network connections for advantage (Jones, 1998; Dunning & Lundan, 2008).

Against this backdrop, this dissertation focuses on the co-evolution of governance structures and strategies in these interconnected value chains, exploring how lead MNEs and non-lead actors jointly shaped organizational innovation and adaptation under conditions of deep uncertainty. The central analytical question concerns how Japanese firms have demonstrated resilience amid the evolution of global capitalism and the development of GVCs. Extant governance research largely centers on powerful MNEs from advanced economies (Cuervo-Cazurra & Pananond, 2023), notably from the West, often presuming the

entire GVC control via power asymmetries that render suppliers "captive" (Gereffi et al., 2005). The strategic roles of peripheral actors remain underexplored. Dialogue between this literature and TCE-informed governance research (e.g., Anderson & Gatignon, 1986; Brouthers & Hennart, 2007) has also been limited, partly due to the methodological challenges of differing units of analysis between GVC-level and firm-level inquiry (Benito et al., 2019). To address these gaps, I foreground sōgō shōsha—typically operating behind the scenes of lead MNEs—and department stores, which have anchored luxury distribution in Japan from the high-growth era to the present (Fujioka, 2013; Donzé & Fujioka, 2018).

The study thus pursues two interrelated objectives. First, it historically traces how firms—a lead MNE and pivotal non-lead actors—have coordinated and governed transactions amid rapidly changing contexts. Second, using a theoretical lens, it analyzes firms' boundary decisions and identifies the mechanisms and conditions shaping their strategic decisions. In doing so, it challenges lead-MNE centric assumptions and shows that governance innovation frequently emerges through co-creation at the interstices of firms, sectors, and institutions—rather than through unilateral command by MNEs.

1.3. HISTORY-TO-THEORY APPROACH AS ANALYTICAL METHOD

This dissertation adopts the view that business history can contribute to theory development (Buckley, 2009a; Jones & Khanna, 2006). As Donzé and Uemura (2025) note, in the Japanese context, business history has traditionally been shaped by a Chandlerian paradigm, with relatively limited methodological discussion and theoretical engagement (see also Kikkawa, 2006; Kurosawa, 2014; Fujioka, 2022). While this functionalist tradition has produced rich empirical accounts of organizational structures and managerial practices (Abe, 2019), it has been less explicit in explaining why particular governance structures emerged, persisted, or changed under evolving institutional and global conditions—or how firms

interacted strategically with external partners within developing GVC configurations (Abe, 2016; Langlois, 2025).

At the same time, at the international level, Decker et al. (2015) highlight the vibrant plurality of directions that shape "new business histories." They argue that methodological pluralism captures both the multiplicity of productive research pathways and the potential for dialogue among them. Within this pluralistic landscape, the "history-to-theory" perspective (Kipping & Üsdiken, 2014) provides a useful framework for using historical evidence to refine, contextualize, and extend theoretical understanding (Argyres et al., 2020; Bucheli et al., 2023). Parallel developments in strategic management and international business likewise recognize the importance of historical inquiry as a means to examine organizational adaptation and governance transformation over time (Rowlinson et al., 2014; Welch et al., 2022). Nevertheless, ongoing debates remain concerning the scientific validity of case-based reasoning and the appropriate balance between contextual richness and theoretical generalization (Ragin, 2009; Fischer et al., 2022).

Against this background, this dissertation integrates historical reconstruction (Decker, 2022) with established theoretical frameworks (e.g., TCE and flying geese theory), building on critical realist (CR) foundation (Bhaskar, 1979, 1993). CR provides a meta-theoretical basis for identifying causal mechanisms, often latent or unobservable (Fletcher, 2017; Sakakibara, 2008). The application of CR has gained recognition in both strategic management (Nonaka & Toyama, 2002) and international business (Welch et al., 2011) as a means of bridging empirical observation with theoretical abstraction.

Building on this methodological foundation, the analytical process begins with conceptual frameworks derived from existing theory, which are then iteratively confronted with historical evidence from case studies. Through successive reasoning cycles, these initial frameworks are refined and extended as new mechanisms and contextual contingencies

emerge. This abductive reasoning process supports the development of context-sensitive theoretical constructs and propositions that explain when, how, and why particular governance mechanisms evolve. Although the empirical focus varies across chapters, this analytical logic remains consistent throughout the dissertation.

1.3.1. Data Collection

Events are observed at the empirical level using two complementary data types: (1) extensive data: statistical series, industry directories and reports, policy documents, corporate filings, and systematic news reviews that establish macro-level patterns and trajectories; and (2) intensive data: in-depth interpretive materials (e.g., interviews and firm narratives) that illuminate decision rationales, inter-firm relations, and field-level practices. Triangulating these sources (Fiss, 2009; Yin, 2018) enables the identification of demi-regularities (Fletcher, 2017) for further analysis and theory building.

1.3.2. Analytical Lens

This dissertation adopts Williamson's (1985, 1996) Transaction Cost Economics (TCE) as its primary analytical frame, complemented—where industry-level shifts are central—by Akamatsu's (1962) Flying Geese (FG) paradigm. In combination with historical analysis, these lenses help surface mechanisms of efficient governance.

1.3.2.1. Transaction Cost Economics (TCE)

TCE is one of the most influential theories in management research and has illuminated a wide range of organizational phenomena—from diversification and the MNE to alliances and supply-chain relationships—while expanding the set of factors that predict governance choice (e.g., Cuypers et al., 2021). In TCE and its extensions, organizations choose among market, hybrid, and hierarchy to minimize the joint costs of production and transactions under bounded rationality, and bounded reliability including opportunism

(Hennart & Verbeke, 2022). Three parameters organize the analysis: asset specificity, frequency, and uncertainty.

Following Benito et al. (2009) and Bucheli et al. (2023), I apply TCE dynamically: governance choices are evolving adaptations, not one-off decisions. As firms learn, counterpart capabilities change, and institutions mature, organizational boundaries shift. To link firm-level governance with regional industrial transformation, Chapter 3 integrates TCE with the FG paradigm. FG captures the spatial and temporal relocation of production and comparative advantage across East Asia (Ozawa, 2011), while TCE explains how firms adjust governance in response. The combined lens yields a multi-level explanation: industrial shifts generate new coordination problems, to which firms respond by reconfiguring governance boundaries or innovating governance solutions.

1.4. DISSERTATION ARCHITECTURE

This chapter defines the research problem and outlines the methodological approach. Chapters 2–5 constitute independent yet conceptually connected studies (see Appendix A for an overview). Each chapter applies an abductive research design within the history-to-theory program, collectively addressing how lead MNEs and Japanese firms—particularly sōgō shōsha and department stores—have co-governed transactions under conditions of high uncertainty and high asset specificity within GVCs. The final chapter synthesizes the empirical findings and highlights the dissertation's theoretical, methodological, and practical contributions, followed by directions for future research.

Chapter 2 – "Dominance versus Collaboration Models: French and Italian Luxury Brands in Japan" examines the governance mode transformations of foreign luxury firms operating in Japan over seven decades. It traces how French and Italian brands transitioned from local partnerships to fully integrated ownership models as institutional and market

knowledge deepened. French firms adopted the dominance model (unified ownership) early and consistently, while Italian firms typically passed through a transitional collaboration model with local partners before reaching full control. This chapter establishes a foundational understanding of lead firm- non-lead actor interactions in luxury retail, setting the stage for later analysis (Chapter 5) of the marketing channel choice.

Chapter 3 – "Evolutionary Pathway of Sōgō Shōsha in the Textile and Apparel Industries" examines the long-run evolution of Japan's general trading companies (sōgō shōsha) in textile and apparel global value chains across East Asia. It traces seven decades of portfolio transformation in two archetypal sōgō shōsha: Mitsubishi Corporation and ITOCHU Corporation. The analysis reveals that the evolution of sōgō shōsha has been shaped by the complex interaction between external forces and internal factors. This complexity is synthesized into a three-phase hypothetical model that captures changes in product, location, and governance portfolios in textile and apparel value chains and introduces a TCE-informed governance dimension largely absent from prior work.

Chapter 4 – "Governing under High Uncertainty: The Strategic Role of Sōgō Shōsha" investigates the role of Japan's sōgō shōsha in multinational enterprise (MNE)–led global value chains (GVCs). It conducts a comparative case analysis of DuPont and Fast Retailing, both of which entered China in the early 1990s—a period of deep political and policy uncertainty—through partnerships with Mitsubishi, a leading sōgō shōsha. This chapter contributes to entry mode research and GVC governance studies in two main ways. First, we advance understanding of entry into highly volatile transition economies by developing four propositions on the entry process and by elaborating a causal–temporal diagram of governance sequencing. Second, we contribute to the structural–relational mechanisms debate by identifying a proto-governance mechanism, facilitated by a non-lead

MNE, that operates before formal governance structures crystallize and relational mechanisms fully take hold.

Chapter 5 – "Flagships and Department Stores: How Dream Costs Shape Luxury Distribution in Japan" explores foreign luxury brands' channel choices in Japan—directly operated flagships versus department stores. It builds on Chapter 2's insights regarding foreign luxury brands' governance transformation in Japan. This study makes two contributions. First, it extends luxury research by applying TCE logic to a luxury B2C setting. Integrating a value logic in luxury literature with a cost logic in TCE offers a more complete picture of marketing channel choice and the mechanisms underlying firms' decision making. Second, it specifies conditions under which department store intermediation coexists with flagships, highlighting Japan's gaishō clienteling mechanism as a distinctive, cost-economizing governance device that shifts the cost calculus.

Overall, the findings challenge lead-firm–centric assumptions. Using a theory-driven approach, the papers advance the current trend toward a "history-to-theory" program (Kipping & Üsdiken, 2014) within business history.

Appendix 1-A.

Overview of papers

Ch.	Paper Title	Main Actor		Context	Uncertainty Type	Analytical Focus	Core Mechanism
		Lead MNEs	Non-lead MNEs	Spatial and Temporal			
2	*Dominance versus collaboration models: French and Italian luxury fashion brands in Japan*	French & Italian luxury brands	Sōgō shōsha; Japanese department stores	Japan, 1950s–2020s	Psychic distance under Japan's institutional voids context	Market entry mode and its configuration	Tension between collaborative model and dominance model
3	*Evolutionary pathway of sōgō shōsha in the textile and apparel industries*	Various MNEs leading textile, apparel, and fashion GVCs	Sōgō shōsha (Mitsubishi, ITOCHU)	East Asia, 1950s–2020s	Institutional voids in emerging economies	Firm strategy evolution driven by institutional changes and industrial transformation	Ability to align logics among different institutions, and flexible adoptability, continuous negation of historical identity
4	*Governing under high uncertainty: the strategic role of sōgō shōsha in early GVC formation*	Mature American MNEs (DuPont) and emerging Japanese MNE (Fast Retailing)	Sōgō shōsha (Mitsubishi)	China, 1990s	Political risks; technological leakage risks	Entry into politically volatile environment	Credible commitments (proto-governance mechanism), and temporary externalization of orchestration functions
5	*Flagships and department stores: How dream costs shape luxury distribution in Japan*	Foreign luxury brands	Japanese department stores	Japan, 2010s–2020s	Consumer behavior uncertainty	Channel choice (direct vs. intermediated format)	Gaisho clienteling system as a firm-customer cost-economizing mechanism

Note. Prepared by author.

CHAPTER 2
DOMINANCE VERSUS COLLABORATION MODELS: FRENCH AND ITALIAN LUXURY FASHION BRANDS IN JAPAN [1]

Abstract

This paper examines the entry strategies of luxury brands in Japan. It uses the global value chains framework and the literature on international business to discuss the entry strategies adopted by European brands on the Japanese market during the last seven decades. Two different business models, the dominance model and collaboration model, which are exemplified by French and Italian companies, respectively, are identified in our analysis. The findings of our analysis suggest Italian luxury fashion brands initially used the collaboration model to enter Japan; however, this approach caused conflict over time, which eventually resulted in the adoption of the dominance model and convergence with the French model. This paper demonstrates that when entering markets with a large psychic distance, Western luxury brands are more likely to face the paradox that the dominance model can only be achieved in a specific set of circumstances through a transitional collaboration with local partners. In our conclusions, we detail the managerial implications for practitioners in the luxury sector.

[1] This is an Accepted Manuscript of an article published by Taylor & Francis Group on behalf of © 2022 Korean Scholars of Marketing Science in *Journal of Global Fashion Marketing* on August 15, 2022, available online: https://www.tandfonline.com/10.1080/20932685.2022.2085596.

2.1. INTRODUCTION

Japan played a major role in the global expansion of luxury fashion brands. It was the first primary non-Western market where European companies experienced a growth based both on selling volume at high prices and propelling the democratization of luxury goods ushered in by lower entry prices and accessories (Donzé & Fujioka, 2018). Accessing a new market, however, is challenging. As Kapferer and Bastien (2012, p. 233) argued, "Luxury is in the distribution," while "distribution is luxury's weak link (241)." Hence, distribution represents the core luxury strategy that can be fully controlled by brands for protecting their brand equity. Simultaneously, foreign brands need to be entrusted to local partners (whether accompanied by the transfer of capital or not) for the management of their operations in a psychically and geographically distant market.

This paper discusses the transformation of the various strategies adopted by French and Italian fashion brands that have entered the Japanese market since the 1950s. Based on the international business (IB) literature and drawing on the global value chains (GVCs) framework, this qualitative study analyses the evolution of the relationships between European brands and local partners in Japan. The paper identifies two different business models: the *dominance* model and *collaboration* model, typically exemplified by French and Italian companies, respectively. In the dominance model, a foreign fashion brand strictly controls the implementation of brand management by Japanese partners. In contrast, the collaboration model is characterized by the relative autonomy of the brand's local representative. However, achieving collaboration is difficult due to the different interests of the partners involved. Consequently, the main research question addressed by this paper is, *how do fashion companies balance the need to protect brand equity with the need to maintain growth and profitability in a market where psychic distance is important?* Through its

historical investigation over seven decades, this study demonstrates that the collaboration model saw a full convergence to the dominance model, a fundamental principle of luxury.

2.2. LITERATURE REVIEW

Our research builds on two major kinds of literature: IB studies and works on GVCs. We use scholarly works in IB to discuss the expansion of European luxury retailers in the Japanese market and to develop our argument for the dominance versus collaboration model. Additionally, to analyze the market entry and expansion of luxury fashion brands in Japan, we draw on the GVC framework.

2.2.1. International Business (IB) Studies

There are two main classical theories addressing foreign market entry. One comprises the new institutional theories and the other is the Uppsala model.

2.2.1.1. New institutional theories

Many of the new institutional economists have tackled the reasons why multinationals have expanded overseas while simultaneously being subject to the inherent disadvantages of foreignness (Hymer, 1960, published Hymer, 1976)—for example, inadequate local market knowledge and discrimination by the governments and institutions of the host country. Hymer (*ibid*.) and Kindleberger (1969) initially asserted that the presence or absence of a firm's specific asset (ownership advantage) provides an explanation for this. Buckley and Casson (1976) then identified that transaction costs (Coase, 1937; Williamson, 1971, 1975) determine how firms choose their modes of operation in a foreign country (internalization advantage). This theory was further developed by Hennart (1993, 2000), who examined opportunism and bounded rationality-based transaction costs. Accordingly, a theoretical

framework was built by Dunning (1993), which offered a comprehensive understanding of why, where, and how firms crossed the border. According to his eclectic paradigm, multinationals attempt to maximize their total profits by linking their ownership, location and internalization advantages. Based on the eclectic paradigm, particularly the internalization advantage, this paper categorizes entry methods into the following three types: exporting/wholesaling, technology transfer (i.e., licensing and franchising), and foreign direct investment (FDI; wholly-owned subsidiaries [WOS], joint ventures [JVs], flagship stores and free-standing stores). These are not mutually exclusive methods – that is, according to international retailing scholars, retailers may use more than one method to develop their international operations. As for the choice between international JVs and WOSs, Buckley and Casson (2010, p. 180) summarized the necessary conditions for JVs as follows: "(i) The possession of complementary assets; (ii) opportunities for collusion, and (iii) barriers to full integration – economic, financial, legal or political." The abovementioned IB theories are practically applied to the historical analysis of the entry mode choice into Japan presented in this paper.

2.2.1.2. Stages model of entry

The Scandinavian "Uppsala" model (Johanson & Vahlne, 1977), is commonly used among luxury retailing scholars. This model suggests a stepwise pattern of entry into successive new foreign markets, which intensifies the commitment level according to the expertise gained in each market. It is closely associated with the notion of "psychic distance," which attempts to measure the cultural gaps at the country level (Buckley & Casson, 2010). The qualitative research conducted by Moore and Burt (2007) showed that luxury internationalization follows the stages model, and, in turn, has initiated internationalization from the countries with cultural and geographic similarities and through mid or low-cost/control entry strategies such as wholesaling and/or exporting. In the context of the entry

into the Chinese market, the study by Bai et al. (2017) indicated that Western luxury firms instead adopt a high-cost/control entry strategy – that is, a market entry through direct retailing.

2.2.2. Other Studies on Fashion Retailing

Several other scholars have identified a wide variety of entry modes for fashion retailers based on their empirical case studies. Within the context of luxury retailing, Kapferer and Bastien (2012) noted that a brand should only sell in its own stores. In particular, flagship stores play a pivotal role not only as a communication device but also as a market entry mechanism (Moore et al., 2010). However, fashion retailers may initially build their brand presence through exporting or wholesaling before making a fully-fledged market entry via store presence (Alexander & Doherty, 2009). For entry into the Japanese market, Okuma (2014) clarified that the intermediate forms of organization formed by Japanese licensees and sublicensees eventually led French luxury firms to direct control over the Japanese market. These various works provide insight into strategic decisions on entry modes; however, it is also necessary to discuss the causes of the evolutionary change in more detail by focusing on the nature of the relationships between luxury brands and local partners. This is what we propose in the model based on the dominance-collaboration dichotomy.

2.2.3. Global Value Chains (GVCs)

The “value chain” concept was first proposed by Porter (1985) and represents a means for firms to gain a competitive advantage over their rivals by adding value in each stage of the activity within a single firm or among different firms. In the 1990s, Gereffi and others built on this concept and generated the GVC framework, which makes it possible to examine a complex international system of production, trade and investment, as well as value-creation

mechanisms by focusing on chains or organization networks rather than a single firm in a specific country. GVC analysis offers two main concepts for scrutinizing the global economy (Gereffi, 2014, p. 1) the governance of the chain, which refers to the asymmetric power relationship between leading firms and other actors in the chain or within inter-firm networks; and 2) the upgrading in GVCs, known as an action of moving up into higher value-added activities. According to Gereffi (1994), with regard to the governance structure of GVCs, there was growing importance of "big buyers" in the 1990s, including retailers, brand marketers, and traders, all of whom exercised significant power and influence over chain actors, even if they had no direct ownership. Gereffi described this value chain as "buyer-driven", which is in stark contrast to the vertically integrated or "producer-led" chains often seen in capital-intensive sectors.

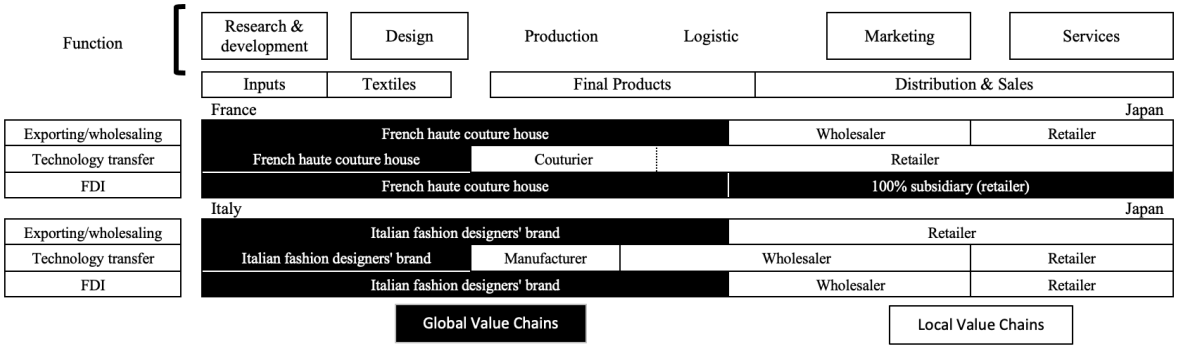
2.3. METHODOLOGY

The development of the model presented in this paper is inspired by new institutional theories (Buckley & Casson, 2010; Hennart, 1993; Williamson, 1975, 2005). Williamson's model (Williamson, 1975) predicts that markets and firms (hierarchies) inhabit the polar ends of the entire spectrum: there are arm's length transactions at the one end, and at the other end there is typically "consolidated ownership". There exist JVs and other arrangements, such as informal long-term contracts between the two. As a product of compromise, and because it allows firms to gain some internalization benefits from behavioral constraints as well as market mechanisms (price constraints) without suffering from the additional costs for vertical integration (Hennart, 1993), this intermediate form of organization – or hybrid – is becoming dominant today (Williamson, 2005). The power relationships between various partners within these different organizations vary greatly and impact how fashion products are manufactured, distributed and sold in a foreign market. In our analysis, we predominantly distinguish

between organizational forms in which the European fashion company owns the majority or even 100% stake in the foreign-based company (which we call the "dominance model") and other forms of cooperation, ranging from licensed production to JVs with a minority shareholding ("collaboration model"). Combining this model with the GVC framework based on the work of Gereffi and Frederick (2010), the paper analyzes the organizational form, which shifts across the spectrum, and discusses the expansion of Italian and French luxury fashion brands in Japan (Figure 2-1). The vertical axis represents the three entry methods these firms adopted, and the horizontal axis represents the six functions in an apparel value chain. The area inside shows the actors in Italy, France, and Japan. The colors clearly distinguish between the GVCs (Italy/France) and the local value chain (Japan; black represents the European brands on the left side and white represents Japan on the right). We apply the term "local value chain" used by Merlo (2018, p. 62), which corresponds to the Italian textile and apparel industry. To indicate the actors in the local value chains, we categorized them into manufacturers, wholesalers (general trading companies ("GTCs"), along with specialized trading companies), and retailers (department stores and specialty retailers).

Figure 2-1

General model, Reproduced with permission of Taylor & Francis © 2022



Note. Drafted by authors.

The sources for our research are articles in newspapers published by Asia's leading business media group, *The Nikkei: Nikkei Shimbun* (financial newspaper), *Nikkei MJ* (marketing journal), *Nikkei Ryutsu Shimbun* (distribution newspaper), *Nikkei Sangyo Shimbun* (industrial newspaper), online fashion magazines, directories of foreign firms in Japan (*Nikkei Shimbun*, Affiliates and Offices of Foreign Corporations in Japan), a comprehensive directory published by *Toyo Keizai* (1986), and reports by market analysts. We selected our luxury brands on the basis of the top 60 largest foreign luxury brands in a ranking published by one of Japan's biggest marketing research firms, Yano Research Institute Ltd (2007). Of these, we selected the Italian (Gucci, Prada, Bottega Veneta, Armani, Fendi, Bulgari, Ermenegildo Zegna, Salvatore Ferragamo, Valentino, Versace, Loro Piana, Moschino, Dolce & Gabbana) and French (Christian Dior, Yves Saint Laurent, Louis Vuitton, Chanel, Hermès, and Cartier) fashion brands dealing in fashion and accessories. Our analysis takes a holistic approach that synthesizes IB theory and the GVC framework, which allowed us to analyze and identify the drivers of the changes across time, space, and function. The focus lies on the shifting roles of economic actors, their relationships, governance modes in particular, licensing arrangements for manufacturers, which stand at the intersection of two connected value chains across the countries and contain inherent contradictions between their complementarity and conflict.

2.4. Entry and expansion of Italian and French fashion brands in Japan

This section discusses the development of Italian and French luxury fashion brands in Japan. Based on the analytical framework described in the previous section, we identify three distinct periods mainly from the viewpoint of GVC development, and the transition from collaboration to dominance.

2.4.1. Dawn of the Luxury Era: The Birth of the Japanese Luxury Fashion Market (1950-1965)

In the post-war years, until the mid-1960s, the Japanese Government strictly controlled foreign trade and FDIs (Mason, 1992, p. 203), making it difficult for Western fashion brands to access the Japanese market. Luxury products were not regarded as essential goods for the Japanese economy at that time. Thus, certain department stores, for which a special quota was allocated from the Government, represented the sole window for the domestic distribution of foreign luxury fashion in the 1950s (Donzé & Fujioka, 2018, p. 136). Daimaru, first and foremost, signed an exclusive contract with Christian Dior in 1953 to reproduce its couture line using the pattern-cutting designs they were granted (Okawa, 2008). This agreement represented an innovative and crucial starting point and contributed to the rise of Japan's luxury industry. The model relied on the creation of fashion design in France, its adaptation by local Japanese couturiers, and marketing and sales by department stores. Based on internalization theory, which explains firms' entry-mode decisions, there are three entry types: wholesaling/exporting, technology transfer, and FDI. The entry mode was virtually limited to technology transfer under government control – whether explicit or implicit – over those two decades post-WWII. Collaboration with local partners was mandatory for new entrants; thus, foreign brands were not permitted strategic choice on how to enter. In the mid-1960s, after trade liberalization, wholesaling/exporting was added to the list of options. Consequently, nearly all the Western fashion brands that wanted to enter Japan followed the Dior model.

2.4.2. Period of Complementarity: The Development of Mass-production (1965-1990)

The environment of luxury fashion business in Japan changed drastically during the 1960s. First, the Government gradually liberalized inward FDI in the field of retail (Mason,

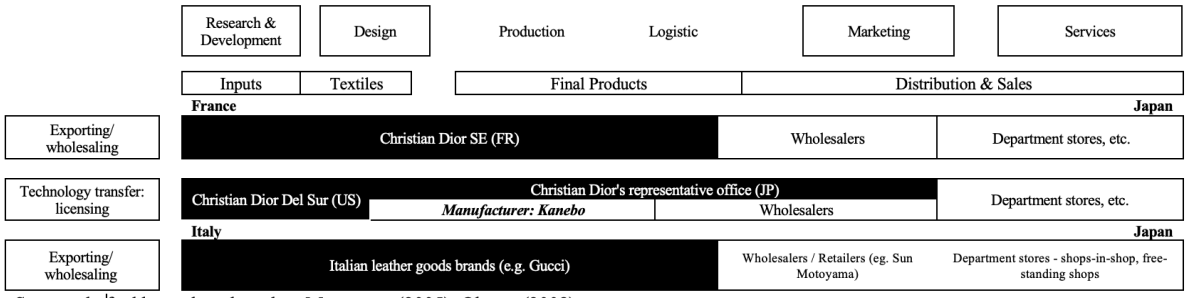
1992, p. 266). In 1975, regulation was abolished and European fashion companies were free to choose their preferred entry mode, based on the degree of expected transaction costs incurred through the adoption of each method. Second, the Japanese economy experienced rapid growth: 9.3%, on average, in real GDP from 1956 to 1972. Many French brands rushed into investment opportunities to leverage Japan's enhanced "location advantage" (Dunning, 1993), regardless of the disadvantages of market uncertainty. Third, the global fashion and apparel industry underwent a major transformation, characterized by the shift from haute couture to prêt-à-porter in Europe and the development of mass-produced Western clothing in Japan. With these industrial structural changes, an important change in power relations took place within local apparel value chains in Japan. A traditional wholesaler called tonya, who controlled the distribution of textiles and clothing, lost their competitiveness to brand-name manufacturers. Textile manufacturers reorganized some sales networks and controlled their distribution channels through a vertical, multi- layered system. Based on complementarity and collaboration between European ion brands and the new dominant actors in Japan, these structural power shifts led to a new organization of the GVCs.

2.4.2.1.New organization of French fashion business in Japan

French brands are an excellent example of the new strategy that firms adopted in the context of these changes. They began large-scale manufacturing licensing businesses with Japanese textile manufacturers. Toray (Yves Saint Laurent) and Kanebo (Dior) used Paris couture's influence to facilitate the market penetrations of their new synthetic fibers (Matsushita, 2020). Dior combined two methods for their fully- fledged entry into the Japanese market: exports of prêt-à-porter from Paris and production licensing in Japan for more affordable items consistent with Japanese sizes and tastes (Figure 2-2).

Figure 2-2

French and Italian fashion brands in Japan, 1965-mid-1970s, Reproduced with permission of Taylor & Francis © 2022



Note. Drafted by authors based on Motoyama (2005), and Okawa (2008).

All the core activities in Japan were under the strict on- site supervision of Dior (Okawa, 2015, p. 24). Dior is a strong example of the pursuit of luxury dominance in its attempts to protect its prestige and authenticity from the early- 1960s when there were regulations preventing direct investment. The case represents the prospect of mutual benefits, which led to successful linkages in Japan of French GVCs with local value chains for the first time. This partnership between them continued for 34 years until 1998.

2.4.2.2.First entry of Italian fashion brands

Export was the first entry mode that Italian leather goods and garment manufacturers adopted. They sold their goods in major department stores and/or free-standing retail stores operated by quality specialty retailers. The challenge was to access retailers without a direct presence in the country. To address this hurdle, Italian fashion brands initially cooperated with traditional wholesalers. Despite the growing importance of textile manufacturers, some wholesalers were still major intermediaries between international brands and department stores (Takaoka, 1997). In 1964, when the Japanese Government completely did away with

trade regulations, Gucci became the first Italian luxury brand to seal a distribution agreement with a Tokyo-based wholesaler, Sun Motoyama.

During the 1980s, in addition to the independent wholesalers, GTCs became the major actors in the luxury fashion market. The decline of the Japanese textile industry made it necessary for GTCs to diversify their activities, shifting to the coordination of the local value chains. Consequently, some aligned with foreign brand holders, and gradually came to exert a strong influence over the domestic apparel industry due to their sales power, a product of their abundant financial and management resources.[2] Mitsui & Co. Ltd. ("Mitsui"), one of the largest GTCs in Japan, was at the forefront of the luxury brand business and established the first JV with Italian fashion brands. From the mid-1970s through to 1990, the JV became the standard form of market entry for Italian fashion brands. Mitsui signed agreements with Valentino in 1974 and Versace in 1981, injecting capital and forming international alliances within the global luxury value chains. The JV exercised a two-way strategy utilizing local licensing production and direct imports. Compared with technology transfer, the JV allows foreign firms to take a step forward in terms of "behavioral constraints" (Hennart, 1993); however, their minority participation has limited their enforcement powers within the boundaries of "collaboration." ITOCHU Corporation ("ITOCHU"), another trading giant, followed suit and came to play a central role in the development of Italian designer brands beginning in the late 1980s, leading the local value chains as the master licensees of the brands.

2.4.2.3.Shifts in governance mode in the 1980s

In contrast to the partnering arrangements of Italian companies, some French luxury firms sought direct ownership in the early 1980s without going through JVs and/or licensing

2 *Nikkei Sangyo Shimbun*, February 20, 1990.

businesses. In 1980, Chanel established a WOS, which is a mode of entry by dominance, a path that Louis Vuitton soon followed in 1981 (Hata, 2003, p. 100). A few years after making its entry, Louis Vuitton Japan was proving a big success, accounting for approximately 30% of the company's consolidated worldwide revenues[3]. Louis Vuitton Japan's success story, which came about without major modifications to the global marketing strategies for Japanese clientele, emboldened other European luxury brands and thereby spurred the acceleration of direct entry by foreign luxury retailers in the 1980s[4].

In contrast to the direct entry of French firms, many Italian brands such as Bottega Veneta and Fila failed their entries into the Japanese market in the mid-1980s[5]. Limited local-market intelligence due to their late entry made it virtually impossible for these Italian brands to achieve a dominance entry mode typically exemplified by the case of Armani, which we look at in the next section.

2.4.2.4.Armani's market entry into Japan

In 1985, Armani first entered the Japanese market through an exclusive distribution contract with Elbis, a retailer of the Saison-Seibu Group. Two years later, in 1987, the company reorganized its presence in Japan with direct investment and the formation of two subsidiaries in the form of JVs: Giorgio Armani Japan and Emporio Armani Japan.

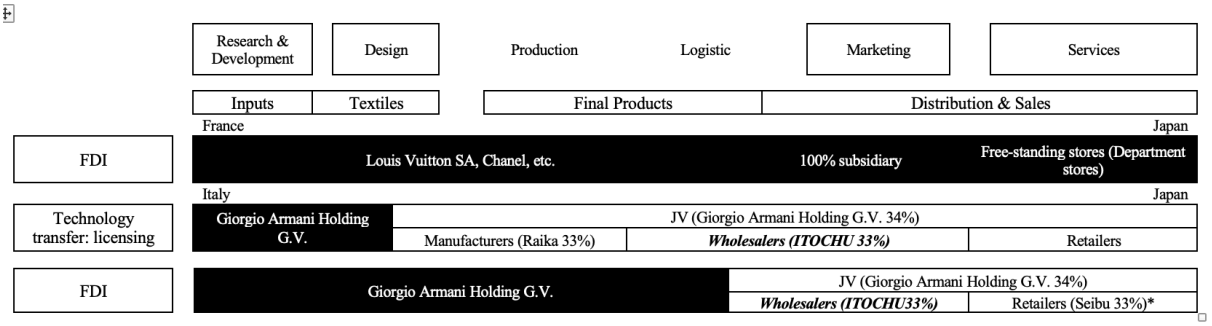
Giorgio Armani Holding G.V. owned a 34% share in both JVs (Figure 2-3). Its fully-fledged market entry, belated in comparison with French competitors, led Armani to begin manufacturing licensing in Japan with local partners. The move was supplemented by direct exports from Italy with a broader range of product lines at different prices for the middle-mass market. The combination of direct exports and local production was adopted by many

3 *Nikkei Ryutsu Shimbun*, November 24, 1988.
4 *Nikkei Sangyo Shimbun*, July 23, 1989.
5 *Nikkei Sangyo Shimbun*, May 26, 1986.

Italian designer brands. It was a necessary approach for many Italian designer brands that had just emerged but sought rapid growth in a distant market. Italian brands, small and medium-sized, mostly family-controlled, and with limited capital, had no choice but to resort to production licensing due to increased operating costs in Japan during the financial bubble of the late 1980s – except Armani, which had gained financial supports from GFT, one of the largest Italian clothing firms (Merlo, 2011). While Giorgio Armani already recognized the vulnerability of local licensing production at the outset of negotiations,[6] he leveraged the solicitation power of the approach in terms of scale to break into the lucrative Japanese luxury market. To execute this strategy, he wanted a solid and trustworthy partner who would make it possible to faithfully represent his brand identity and secure control over the local value chain, populated by complex and multi-layered distribution networks.

Figure 2-3

French and Italian fashion brands in Japan in the 1980s, Reproduced with permission of Taylor & Francis © 2022



*Note. Drafted by authors based on Hata (2003), and Nihon Keizai Ryutsu Shimbun, October 29, 1987. *Sold at department stores, specialty stores, franchise stores, through 100% subsidiaries and partially through the wholesaler Sanki Shoji.*

Eventually, ITOCHU won the heated bidding battle among over ten bidders. ITOCHU acted as an orchestrator for controlling information from downstream to upstream,

[6] *Nikkei Sangyo Shimbun*, August 11, 1983.

handling the various risks dotting the fragmented and complex local value chains. Mitsui had been a forerunner in the domestic luxury brand business at the beginning of the 1980s, but the situation reversed itself and allowed ITOCHU to take the initiative in the industry due to the extraordinary gains from its licensing business with Armani. Intermediaries such as GTCs helped new entrants reduce the high search and information costs, mitigating asymmetric information (Buckley & Casson, 1976). For ITOCHU, and many other domestic channel players, the luxury brand business was becoming the most lucrative source of revenue.

2.4.3. Period of Conflicts: Changes in Distribution Strategies (Since 1991)

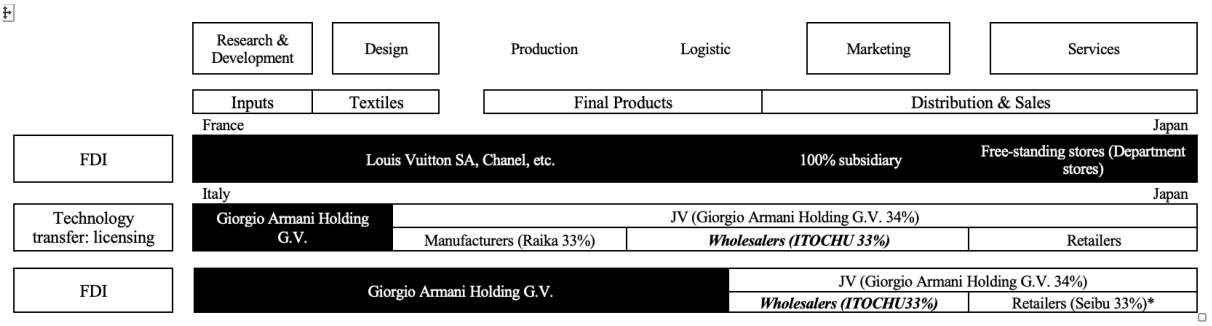
Despite the collapse of the asset bubble in 1991 and declines in household income, the consumption of personal luxury goods, particularly handbags, stayed high in the 1990s. Consumption was fueled by "office ladies, still single and living with their parents" (Kapferer & Bastien, 2012, p. 117). This dynamic also contributed to the democratization of luxury fashion, a new strategy that European firms adopted in the 1990s to enlarge their consumer bases. However, luxury consumption began to decline in the late 1990s due to economic stagnation. It then experienced a second boom during the period 1993–1996, supported by monetary factors (depreciated lira and appreciated yen) and changes in post-market entry strategies: a shift from licensing to direct exports, or a transition into the dominance model that French brands introduced in the early 1980s. Taking back control over the brand became a major issue for most luxury companies around the world. They began to change their distribution strategies, increasing the ratio of exports to enhance the brand equity, which was diluted by licensing. In particular, Armani paid considerable attention to maintaining consistency in its brand image, and striving to strike a balance between high-end lines and diffuse lines, or even more affordable licensed products. Some other brands struggled to rebuild their already diluted brand images in Japan due to the abundance of licensed products.

Italian brands faced not only these types of marketing issues but also many operational challenges in Japan, such as extremely high inventory levels and price collapses due to international price discrimination and, in turn, the flood of parallel imports.[7] The need to strengthen the control of brand management led some companies to establish WOSs. The year 1990, when Gucci took over, marked an important turning point for the Italian brands as they moved towards dominance.

Armani is again an excellent illustration of this new strategy with ties to organizational changes. In January 1995, Giorgio Armani took shares back from the locals and had a 60% majority ownership, with ITOCHU holding 40% (Figure 2-4).

Figure 2-4

French and Italian fashion brands in Japan since the early-1990s, Reproduced with permission of Taylor & Francis © 2022



Note. Drafted by authors based on Hata (2003), Mffashion (1998), and Yahagi (2000, p. 51).

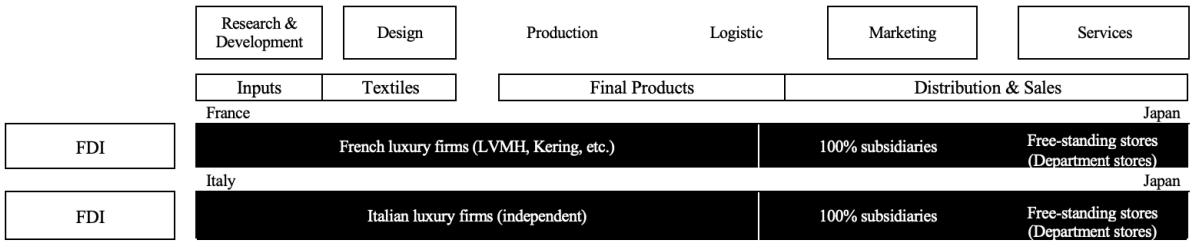
Simultaneously, Armani executed various restructurings by merging its two JVs and closing many unprofitable stores. Next, to eliminate parallel imports, Armani cut retail prices by 20–40%.[8]It also implemented a new business model by gradually shifting from consignment arrangements to outright purchasing to optimize their inventory levels. Most

7 *Nikkei Ryutsu Shimbun*, September 18, 1990.
8 *Nikkei Ryutsu Shimbun*, July 15, 1997 (based on an interview with Jacob Mayor, CEO of Armani Japan).

importantly, Armani refurbished its stores and opened a 1,230 square-meter flagship shop in Tokyo in October 1995 to update its brand image. Flagship shops, as symbolic capital, presented the most extreme form of dominance. The "ownership advantage," especially in terms of authenticity for luxury brands, was supported, enhanced, and realized through Japan's licensing business until the 1980s. However, the need to exert better control over the brand image on the one hand and the rise of value and quality consciousness among Japanese consumers after the bubble economy on the other accelerated the changing strategies (Okawa, 2008). A final point worth mentioning here is that the acquisition of several Italian luxury brands by French conglomerates has had a significant impact on the Italian firms' distribution strategy since the late 1990s (Donzé, 2018). Indeed, these groups adopted full control of their brands early on, verticalizing distribution and putting an end to licensing (Donzé & Wubs, 2017). As shown in the Appendix B and Figure 2-5, the 2000s saw full convergence of Italian brand organizations in Japan with the dominant French model.

Figure 2-5

French and Italian fashion brands in Japan since the 2000s, Reproduced with permission of Taylor & Francis © 2022



Note. Drafted by authors based on LVMH (2003); Bulgari (2009), WWD (2002; 2006); SHOWS (2008).

2.5. CONCLUSION AND IMPLICATIONS

Our paper reveals two different entry modes into the Japanese fashion market. As first movers, French firms sought direct control over the entire value chain from the outset in the 1950s. Italian fashion brands, however, were latecomers and adopted the collaboration model. Limited local-market knowledge due to their late entry and strong growth orientations led Italian brands to rely on intermediaries. However, the collaboration that started with strong complementarity eventually led to conflict. A JV was first successfully set for maximizing joint profits among channel players and internalizing the resources each actor owns. There existed, however, an inherent trade-off between short-term profitability and long-term brand equity. This led to gradual changes in local distribution strategies as firms significantly restructured their retail networks, before causing eventual convergence with the French dominance model. Some brands in Japan have failed to strike the right balance between the two. Conversely, Armani has achieved the best compromise and has managed the luxury paradox through a timely shift across the spectrum from markets to hierarchy.

This paper provides managerial implications to practitioners in luxury business. First, as Kapferer and Bastien (2012) note, “Luxury is in the distribution,” while “distribution is luxury’s weak link.” This is particularly true in the case of entry into countries with large cultural distances and dense networks of domestic ties. The nexus is made up of a wider variety of governance modes that range from arm’s length market transactions to hierarchies and the “swollen middle” (Hennart, 1993) ground in between. As many have suggested, and as this paper also demonstrates, the nexus within the collaborative “middle” contains a host of trade-offs. Thus, managers need to bear in mind that collaboration can only be temporary and that it eventually settles into the ultimate goal of luxury: dominance. Second, when entering markets with a great psychic distance, the dominance model can only be achieved in specific circumstances through a transitional collaboration with local partners. Therefore, the

greater the psychic distance from the home market, the more prevalent the paradox of luxury becomes in the host country. Even in the contemporary world, with the growing importance of online trade and the rapidly increasing presence on social networking sites of luxury fashion actors, the abovementioned challenges remain.

The main academic contribution of this article is addressed to the synthesis of IB theory and fashion business history. The adoption of the dominance versus collaboration model inspired by IB theory allows an analytical explanation of the long-term evolution of fashion brands in distant markets. Our analysis highlights the need to consider the context of entry into distant markets from a dynamic perspective in order to fully illuminate the actions of firms.

This current analysis suffers from several limitations and also offers insight for further research areas. First, the recent phenomenon of artisanal collaborations with local designers (e.g., Prada) has opened up a new avenue as an effective approach to mitigate the disadvantages of "foreignness" (Hymer, 1976) and narrow the psychic distance through the universality of art and culture. Due to space limitations, we could not cover this new strategy of artification, which was initially implemented by French brands in Japan in the 2000s (Kapferer, 2015). Hence, these investigations would provide new insight into the dominance versus collaboration dilemma. Second, our analysis dealt specifically with Japan, one of the major markets for luxury fashion. Hence, future studies should be directed toward other important markets like China, which would help to achieve a more general understanding of the process of globalization of luxury fashion brands.

Appendix 2-B.

Chronological chart of capital investment, Reproduced with permission of Taylor & Francis

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Founded in	Investment type	Shareholding company (stake)	Partners in Japan (stake)
1974	JV	Valentino S.p.A (n/a)	Mitsui Co., Ltd.(n/a), sann frères (n/a), Aoi Co Ltd. (n/a)
1977	WOS	Zegna International N.V (100%)	
1981	JV	Gianni Versace International (34%)	Mitsui Co., Ltd. (33%), sann frères (33%)
1981	WOS	CHANEL S.A. (100%)	
1981	WOS	Louis Vuitton S.A. (99%)	
1983	JV	HERMÈS (50%)	The Seibu Department Stores, Ltd. (50%)
1984	JV	Moonshadow S.r.l (Moschino) (n/a)	Isetan (n/a), Aeffe S.p.A (n/a)
1986	WOS	Bottega Veneta Sarl (100%)	
1987	JV	Giorgio Armani Holding G.V. (34%)	ITOCHU Corp. (33%), The Seibu Department Stores, Ltd. (33%)
1987	JV	Giorgio Armani Holding G.V. (34%)	ITOCHU Corp. (33%), RAIKA CO., LTD. (33%)
1989	JV	Cartier (51%)	Liebermann-Wälchli & Co.,SA (49%)
1990	WOS	Gucci Group N.V. (100%)	
1991	JV	Bulgari International Corp. NV (51%)	Aoi Co Ltd (35%), ITOCHU Corp. (14%)
1991	JV	Prada S.p.A. (n/a)	Efu Maiami Shoji (n/a)
1991	WOS	Loro Piana SpA (100%)	
1992	JV	Salvatore Ferragamo Italia S.p.A (71%)	Aoi Co Ltd (15%), Mitsubishi Corp. (14%)
1993	WOS	Cartier (100%)	
1995	JV	Giorgio Armani Holding G.V. (60%)	ITOCHU Corp. (40%)
1996	WOS	Prada S.p.A. (100%)	
2000	JV	Giorgio Armani Holding G.V. (85%)	ITOCHU Corp. (15%)
2000	JV	Bulgari International Corp. NV (80%)	ITOCHU Corp. (10%), Aoi Co Ltd. (10%)
2001	JV	Fendi S.r.l – LVMH (70%)	Aoi Co Ltd. (30%)
2001	WOS	Dolce & Gabbana (100%)	
2002	JV	Gianni Versace International (n/a)	Mitsui Co., Ltd. (n/a)
2003	WOS	Fendi S.r.l – LVMH (100%)	
2005	WOS	Giorgio Armani Holding G.V. (100%)	
2006	WOS	Gianni Versace International (100%)	
2008	WOS	Valentino S.p.A (100%)	
2009	WOS	Bulgari International Corp. NV – LVMH (100%)	

Sources: *Toyo Keizai Shimposha*, *The Nikkei*, *New York Times*, *LVMH document de référence*, Bulgari consolidated financial statements, *WWD*, *SHOWS*.

CHAPTER 3
EVOLUTIONARY PATHWAY OF SŌGŌ SHŌSHA IN THE TEXTILE AND APPAREL INDUSTRIES

Abstract

This paper examines the long-run evolution of Japan's general trading companies (sōgō shōsha) in textile and apparel global value chains across East Asia. Using a critical realist, history-informed abductive design, it traces seven decades of portfolio transformation in two archetypal sōgō shōsha: Mitsubishi Corporation and ITOCHU Corporation. The analysis reveals that the evolution of sōgō shōsha has been shaped by the complex interaction between external forces and internal factors. This complexity is synthesized into a three-phase hypothetical model that captures changes in product, location, and governance portfolios in textile and apparel value chains and introduces a TCE-informed governance dimension largely absent from prior work. The study contributes to business group and business history research by showing how diversified, non-manufacturing firms in an advanced economy evolve after the original rationale for their existence and competitiveness erodes.

3.1. INTRODUCTION

Japan's general trading houses, or sōgō shōsha, are today the world's most powerful enterprises (Fortune, 2024). Tracing their roots to the Meiji era, sōgō shōsha historically served as the connective tissue linking Japan to the global economy, coordinating finance, logistics, information, and distribution across a wide range of industries (Jones, 2005; Tanaka, 2012b). Domestically, they functioned as core firms within kigyō shūdan (business groups) (Okumura, 1993, p. 175)—dense networks of companies connected through cross-shareholding and other reciprocal arrangements (Lincoln & Shimotani, 2009). Within these groups, sōgō shōsha acted as "nexus of group transactions," particularly in goods trade (Okumura, 1993, p. 166).

Yet their long-run competitiveness remains insufficiently understood in international comparative perspective (Jones, 1996, p. 115; 1998, p. 8; 2000, p. 346). Indeed, their persistence poses two longstanding theoretical puzzles. First, institutional voids (IV) theory predicts that business groups (BGs) including Japan's kigyō shūdan that emerge to compensate for underdeveloped factor markets should decline as markets mature and institutional voids dissipate (Khanna & Palepu, 1997, 2000). Under this logic, once Japan completed its postwar transition from an emerging to an advanced economy, the coordination functions historically performed by sōgō shōsha should have become redundant. Second, classical commercial capital theory similarly predicts their decline: as manufacturers strengthen their bargaining power, intermediaries should be removed from value chains (Hilferding, 1981, p. 209; Morishita, 1974, pp. 66-82). In the late 1990s, Japanese synthetic fiber producers such as Toray and Teijin internalized trading functions and eliminated sōgō shōsha from parts of their supply chains.

The empirical reality, however, contradicts both sets of predictions. By the early 2000s, both vertical and horizontal keiretsu networks had faded (Shimotani, 2006; Lincoln &

Shimotani, 2009); however, sōgō shōsha did not disappear. Instead, firms such as ITOCHU and Mitsubishi became more profitable and more powerful (Appendix 3-A). Their resilience challenges explanations that attribute their persistence and competitiveness either to group affiliation or to the existence of institutional voids (Khanna & Palepu, 1997, 2000; Yagashiro, 2019).

Recent scholarship has called for deeper understanding of how BGs adapt when market imperfections narrow, external factor markets deepen, and institutional transitions are completed—especially in advanced-economy contexts, which remain underexplored (Hoskisson et al., 2005; Carney et al., 2017a, 2017b; Holmes et al., 2018; Aguilera et al., 2020; Lee et al., 2022). Japan offers a rare setting for investigating this neglected stage: sōgō shōsha persist, and have even strengthened despite the transformation of Japan's institutional profile from that of an emerging to an advanced economy, and despite the erosion of the original institutional rationale for business group formation and development.

Addressing these theoretical puzzles requires narrowing the analytical boundaries and moving beyond dominant existing frameworks. The empirical scope of this study is delimited to the textile and apparel sectors, conventional industries in which sōgō shōsha historically played a central role. These sectors have been one of the most dynamic arenas of activity, where product and locational portfolios have shifted rapidly. They also served as a vanguard for business model experimentation within sōgō shōsha, with new practices later diffusing into other sectors, as noted by a former Marubeni director[9]. This setting is therefore an ideal context for an analysis of their business evolution and an identification of survival mechanisms and strategic transformations at the firm level.

[9] *Nikkei Sangyō Shimbun*, 31 January 1981, 繊維２次製品輸出に活路 [Exporting secondary textile products is a way forward].

Extant frameworks typically treat institutional and industrial factors as exogenous or given, and largely adopt an MNE-centric approach (Hennart, 2009). The evolution of diversified, non-manufacturing firms such as sōgō shōsha remains relatively neglected in the international business (IB) literature (Jones & Khanna, 2006; Johanson & Vahlne, 2009). Methodological challenges compound this neglect. Conventional approaches often break the real world down into simplified components and underemphasize process, historical embeddedness, and co-evolution (Cantwell et al., 2010, p. 19), limiting their ability to explain how firms adapt within transforming institutional and industrial landscapes.

To address these theoretical and methodological challenges, we adopt a critical realist, history-informed abductive research design (Welch et al., 2011), which is elaborated in the Methodology section. Historical analysis within this paradigm enables investigation of non-linear trajectories, path dependence, and far-from-equilibrium changes (Cantwell et al., 2010). It also allows the analysis to "zoom in" on specific episodes while "zoom out" to situate them within longer-term industrial upgrading and institutional shifts (Bucheli et al., 2023).

Guided by Japan's postwar institutional trajectory (Shimotani, 2006), the analysis follows three historical phases: Phase I (1950s–1980s): keiretsu-based era; Phase II (1990s–mid-2000s): institutional transformation and keiretsu erosion; and Phase III (mid-2000s–present): post-keiretsu era. Across these phases, we analyze emblematic episodes from two archetypal, but historically distinct sōgō shōsha—ITOCHU and Mitsubishi— to illustrate how they reconfigured their product, location, and governance portfolios in response to shifting institutional and industrial environments. The paper proceeds in two steps. First, it reconstructs a seven-decade historical account of their activities within textile and apparel GVCs. Second, it synthesizes these insights into a three-phase model of sōgō shōsha's evolutionary paths of cross-border activities.

Our historical delineation demonstrates how changes in the external environment influenced firm level decisions for sōgō shōsha and MNEs leading value chains: sōgō shōsha responded to these shifts by repeatedly reconfiguring their portfolios and, in the process, negating and reconstructing elements of their prior historical identity—as textile traders, as forms of commercial capital, and as home-country–anchored GVC coordinators.

The study contributes to BG research by illustrating how diversified, non-manufacturing, BG-derived firms evolve before, during, and after institutional voids diminish. Our findings suggest that the evolution of sōgō shōsha involves a complicatedly interwoven, and multi-layered process shaped by the interaction between external shifts, and micro-level governance challenges. Through an abductive approach, it distills this complexity into a three-phase model that captures changes in sōgō shōsha's product, location, and governance portfolios in textile and apparel value chains, and introduces a TCE-informed governance dimension. These insights enrich BG literature beyond its traditional focus on emerging economies and early-stage institutional development and offers implications for managers and policymakers in countries "climbing the ladder" toward advanced economy status, by illustrating how BG-derived firms can reposition themselves within global industries.

3.2. Literature Review

3.2.1. Theories of Multinational Enterprises (MNEs)

Research on the cross-border activities of multinational enterprises has traditionally been grounded in internalization theory (Buckley & Casson, 1976; Rugman, 1981). This perspective argues that firms expand overseas to internalize cross-border transactions when market failures render external exchanges inefficient. The resource-based view (RBV) focuses on firm-specific resources, capabilities, and skills (Madhok, 2002). It thereby

highlights how firms leverage distinctive internal assets, but provides only a partial account of how those capabilities interact with external governance structures (Hennart & Verbeke, 2022). These inward-looking assumptions are especially restrictive for analyzing organizations such as sōgō shōsha, whose ownership advantages lie in orchestrating intra- and inter-firm linkages rather than in internal resources (Okumura, 1993; Dunning & Lundan, 2008).

Efforts to broaden these perspectives—such as Dunning's eclectic OLI paradigm (1988), which integrates ownership (O), location (L), and internalization (I) advantages and recognizes the value of complementary local assets (Hennart, 2009)—as well as evolutionary perspectives (e.g., Dunning & Lundan, 2008; Cantwell et al., 2010), have enriched our understanding of internationalization. Extensions exploring the interaction between firm-specific and country-specific advantages (FSAs and CSAs) (Rugman & Verbeke, 1991) further highlight how MNEs recombine internal capabilities with external resources to innovate, reduce risks, and manage uncertainty (Gooris & Peters, 2016). Nonetheless, mainstream international business research has focused predominantly on MNEs in high-technology manufacturing sectors in advanced economies (Jones & Khanna, 2006), leaving diversified, non-manufacturing firms such as Japan's sōgō shōsha relatively underexplored.

As globalization accelerated in the 1990s and 2000s, IB research shifted toward network and GVC perspectives. These frameworks recognize that firms increasingly rely on multi-tier coordination across borders (Buckley & Ghauri, 2004; Mudambi, 2008). GVC governance research provides insights into how lead firms coordinate dispersed activities through hierarchical, modular, or relational governance modes (Gereffi et al., 2005), and how they manage upgrading and inter-firm dependence along the chain.

In sum, internalization theory, OLI, RBV, and GVC governance theory illuminate important aspects of firm expansion, capability deployment, and cross-border coordination.

Yet there are some gaps that are particularly salient for this study on sōgō shōsha. First, IB theories and OLI eclectic paradigm devote relatively little attention to non-manufacturing firms. RBV exhibits a strong bias toward internal resources and capabilities rather than exogenous conditions. GVC governance theory typically assumes that cross-border activities are orchestrated by apex lead firms, rather than highlighting co-evolutionary perspectives.

Process-based theories offer a different lens. The Uppsala model (Johanson & Vahlne, 1977) conceptualizes internationalization as a gradual, experiential learning process in which firms increase commitment as they gain foreign-market knowledge. The revised model (Johanson & Vahlne, 2009) introduced "liability of outsidership" and network positions, shifting analytical focus from resource endowments to relational embeddedness. This process-oriented view provides an important alternative to variance-based theorizing (Welch et al., 2016; Vahlne & Johanson, 2017). Yet, significant limitations remain. Critics highlight the model's linearity, noting that internationalization often proceeds through discontinuities shaped by shocks, reforms, or institutional transitions (Håkanson & Kappen, 2017; Santangelo & Meyer, 2011, 2017; Coviello et al., 2017; Aaltonen, 2020; Yoshinari, 2024). Others point to its continued focus on lead firms (Hennart, 2008; Verbeke, 2025). Verbeke (2025) argues that contemporary IB must foreground governance under uncertainty—an area the Uppsala model does not fully encompass.

Attempts to integrate Asian business systems into process theory—such as Kim (1986) and Ellis (2001)—trace the evolution of general trading companies (GTCs). Kim (1986) showed how Japanese sōgō shōsha moved from commodity trading to diversified portfolios across products, locations and functions, while Ellis (2001) introduced the "MNE-trader" typology (investment-to-trade ratio exceeding 50%), and emphasized the functional shift toward investment-based activities of GTCs in general, based on an in-depth investigation of Hong Kong GTCs. Goerzen and Makino (2007) similarly observed sōgō

shōsha transitioning toward differentiated, non-trade activities and increasingly location-specific operations. These contributions help illuminate the diversification path of Asian GTCs. Yet the literature remains largely functionalist and internally oriented. It emphasizes structural diversification within GTCs while offering limited insight into how, under institutional transformation and industrial shifts, these firms reshape cross-border governance mechanisms and strategies with external partners. Recent critiques also underscore this gap. Yoshinari (2024) argues that prevailing process models—including Uppsala—cannot fully explain the strategic complexity underpinning sōgō shōsha's global expansion process.

These limitations suggest the need for a framework that links firm-level governance choices with macro-level institutional and industrial transformations, and that can accommodate diversified, non-lead MNEs such as sōgō shōsha. A more detailed discussion of this theoretical and methodological foundation follows in the next section.

3.2.2. Fate of Large Diversified Firms

Large diversified firms have been extensively analyzed within BG research (Colpan et al., 2010; Lee et al., 2022). BGs are business entities defined as "a collection of firms bound together in some formal and informal ways" (Granovetter, 1994, p. 454). Within this tradition, the institutional voids (IV) perspective (Khanna & Palepu, 1997, 2000) emphasizes how the absence or inefficiency of market-supporting institutions and legal systems shapes corporate strategy (Tan & Meyer, 2010). In emerging economies, such voids often compel firms to internalize market-supporting functions. A well-known example is India's Tata Group, which created internal capital and labor markets to compensate for weak external institutions (Khanna & Palepu, 1999). Thus, BG scholarship conceptualizes diversification as a structural response to underdeveloped institutions (Khanna & Rivkin, 2001).

Much of this literature argues that BGs are transitional organizational forms that should decline as markets mature (Guillén, 2000). Some have indeed disappeared, yet many have persisted—and in some cases strengthened—in countries such as Belgium, Brazil, China, India, Indonesia, Israel, Japan, Malaysia, Peru, Singapore, and Taiwan (Carney et al., 2017b). This tension between theoretical prediction and empirical persistence has motivated a search for BG "survival mechanisms".

Identified mechanisms include the accumulation of proprietary organizational and technological capabilities through internationalization prior to pro-market reforms; product diversification and subsequent refocusing strategies; and "escape" strategies from weak institutions (Guillén, 2000; Holmes et al., 2018; Carney et al., 2017b). In Chile, for example, Bucheli et al. (2018) show that BG survival was enabled partly through the creation of structural market imperfections, in the spirit of Hymer (1960/1976) and Kindleberger (1969).

Empirically, however, the bulk of this work concentrates on BGs in emerging economies (Aguilera et al., 2020). The resulting insights provide a powerful baseline for understanding how large diversified firms respond to institutional change, but offer less guidance on how BG-derived diversified firms behave once their home economies complete major institutional transitions and market-supporting infrastructures deepen. In what follows, we draw on these insights as a point of departure for analyzing sōgō shōsha, while focusing on a different institutional stage and sectoral setting.

3.2.3. Evolution of Sōgō Shōsha

Trading companies are unique entities whose missions, organizational structures, and internal cultures are deeply influenced by the political, economic, and regulatory conditions of their home environments. Similarly, research on this topic is highly context-dependent,

often requiring an examination of the national setting to fully grasp their dynamics (Ellis, 2001; Jones, 1998).

Japan's sōgō shōsha—today represented by seven major firms (ITOCHU Corporation, Sumitomo Corporation, Sojitz Corporation, Toyota Tsushō Corporation, Marubeni Corporation, Mitsui & Co. Ltd., and Mitsubishi Corporation—constitute one of the world's most distinctive organizational forms (Tanaka, 2012b). Tracing their origins to the Meiji era[10], many of these firms emerged from two fundamentally different historical lineages (Tanaka, 2012b)[11]. This divergence partly explains the different organizational cultures, and strategic orientations that characterize ITOCHU and Mitsubishi today (*Toyo Keizai*, 2016): (1) Zaibatsu-originated lineage. Mitsui and Mitsubishi evolved from prewar zaibatsu family-owned conglomerates and benefitted from early state support, privileged access to finance, and vertically and horizontally integrated group structures (Yoshihara, 1987; Jones, 1996). Although the zaibatsu holding companies were dissolved in 1947, the broader "industrial management system" and "invisible links" with affiliated firms persisted (Yoshino & Lifson, 1987; Shimada, 1993). These institutional relationships solidified into kigyō shūdan (horizontal keiretsu), maintained through long-term cross-shareholding and interlocking directorates (Okumura, 1993; Kikkawa, 1995; Shimotani, 1997, 2006); (2) Textile trader–originated lineage. ITOCHU and Marubeni originated as merchant houses dealing in cotton and linen. Their growth was closely tied to the postwar dissolution of zaibatsu, the prioritization of textiles as a strategic industry, and Japan's export-led textile boom (Tanaka,

[10] The term "sōgō shōsha" was not common in the pre-WWII era, but the role of today's sōgō shōsha can be observed in the businesses performed by Mitsui and Mitsubishi during the Meiji era. (Okumura, 1993, p. 173).

[11] Beyond these two archetypes, additional forms exist. Sojitz and Toyota Tsusho: the firms originated from specialized steel and textile trading firms merged and diversified. The Sumitomo group represents a distinct case as Tanaka (2012b) classifies it as a "new entrant": Recognized as Japan's third-largest zaibatsu (Sato, 2025), Sumitomo differed from Mitsui and Mitsubishi in its path and mode of diversification. Initially rooted in mining, Sumitomo expanded into banking and other unrelated sectors primarily through internal capital accumulation rather than government-facilitated acquisitions (Sato, 2025).

2012b). They expanded and caught up partly through mergers and consolidation (Tanaka, 2012b). By the 1960s–1970s, a newer group of kigyō shūdan had formed around large commercial city banks. For example, ITOCHU became a core member of the former Dai-Ichi Kangyō Bank keiretsu (Tanaka, 2012b, p. 99).

Alongside these kigyō shūdan, sōgō shōsha were deeply embedded in vertical keiretsu structures led by Japanese cotton spinners and/or synthetic fiber manufacturers (Uchida, 1973; Yagashiro, 2023). Across both lineages, sōgō shōsha expanded beyond simple trade intermediation toward a multifunctional corporate structure consisting of: (1) commodity and product trading, (2) trade-related services (finance, logistics, information, and risk management), and (3) non-trading functions such as direct investment and project management (JFTC, 2023).

Despite their historical significance in the global economy (Jones, 1998; 2005) and recent calls on more studies about diversified firms in advanced economies (Hoskisson et al., 2005; Carney et al., 2017a, 2017b; Holmes et al., 2018; Aguilera et al., 2020; Lee et al., 2022), few studies have explored sōgō shōsha from an international comparative perspective. Much of the scholarship in business history and management adopts a functionalist orientation (e.g., Shōsha Kinō Kenkyūkai, 1981), offering rich descriptions of functions but relatively limited accounts of why particular governance structures emerged or how sōgō shōsha strategically interacted with external partners under changing institutional and industrial conditions.

Economists drawing on classical commercial capital theory predicted the long-term decline of sōgō shōsha, arguing that they would be disintermediated as manufacturers strengthened their bargaining power and internalized previously outsourced functions (Morishita, 1974). Yet, sōgō shōsha did not fade away. Many commentators in both media and academia attribute their persistence to transformation into investment-driven firms and

deeper involvement in value-chain activities beyond mere intermediation. Indeed, sōgō shōsha become more engaged in non-trading activities over time: in 2009, Mitsubishi became an "MNE–trader" (with investment-to-trade revenues exceeding 51%) according to Ellis's (2001) typology, and ITOCHU followed in 2016. However, such accounts tend to treat this transformation as a static outcome, leaving unresolved the mechanisms underpinning these strategic shifts.

Scholars emphasized that dense keiretsu linkages in the postwar era facilitated transactions among Japanese firms and reduced bounded rationality challenges (Delios & Beamish, 1999). Operating within a bank-centered, relational economy, sōgō shōsha economized on transaction costs by providing credit, monitoring information flows, and mitigating enforcement risks (Imai & Itami, 1984; Buckley, 1985; Todeva, 2005; Dunning & Lundan, 2008). Yet by the 1990s and early 2000s, market liberalization, financial deregulation, and globalization eroded many of the institutional arrangements that had sustained the keiretsu system (Shimotani, 2006; Lincoln & Shimotani, 2009). This shift raises an underexplored question: how did sōgō shōsha sustain and reconfigure their firm-specific advantages once the institutional structures that justified their existence had weakened or disappeared? Few studies address how these firms adjusted their strategies before, during, and after the erosion of keiretsu neetworks, or how they confronted the need to redefine their raison d'être in a more open and competitive environment.

3.3. METHODOLOGY

3.3.1. Abductive and History-Informed Approach

This paper adopts an abductive, history-informed research design grounded in Bhaskar's critical realism. Abduction differs from deduction and induction in that it begins with an initial theory. This approach is particularly suited to phenomena that are strongly

context-dependent and shaped by the interaction of multiple forces, and therefore not easily examined using experimental or cross-sectional designs (Reuber & Fischer, 2022). The strategic behavior of trading firms (Ellis, 2000) and BGs more generally varies significantly across institutional, industrial, and organizational contexts (Cantwell et al., 2010; Carney, 2011; Carney et al., 2017a, 2017b; Holmes et al., 2018), making abductive reasoning especially appropriate for examining sōgō shōsha, given their invisible and context dependent nature.

The abductive process involves continuous engagement with empirical evidence. In our study, we use various historical materials such as trade statistics, corporate documents, news materials, and interviews. Each analytical iteration involved: (1) juxtaposing theoretical assumptions with these evidences; and (2) confronting extant literature to better explain observed governance patterns and portfolio shifts. This iterative movement between theory and evidence enables us to identify underlying causal mechanisms—notably how institutional change and industrial upgrading reshaped sōgō shōsha portfolios over time. This reasoning process culminates in a hypothetical three-step evolutionary model that specifies their transformation.

Among all seven sōgō shōsha, Mitsubishi and ITOCHU were selected as focal cases because they represent distinct historical lineages—zaibatsu-originated and textile-trader-originated, respectively. Their contrasting trajectories make them ideal extreme-case comparisons (Pettigrew, 1990; Fiss, 2009), and enable the examination of *equifinality* (i.e., different paths to similar strategic outcomes) (Welch & Paavilainen-Mäntymäki, 2014).

3.3.2. Data Analysis

The analysis starts from the 1950s—when firms from dissolved zaibatsu groups such as Mitsubishi reunited, and when firms like ITOCHU began transforming from textile traders

into full-spectrum sōgō shōsha (Tanaka, 2012b, pp. 98-105). Given the study's wide temporal scope, analysis proceeds through phase-based triangulation consistent with Japan's institutional evolution:

Phase I: Keiretsu-based era (1950s–1980s): Primary data were scarce, so we relied primarily on secondary historiography and government statistics. Sources included postwar trade statistics, MITI reports, and leading business history monographs, complemented in part by interviews with former managers.

Phase II: Institutional transformation and keiretsu erosion (1990s–mid-2000s): This transitional phase marked the erosion of keiretsu and the rise of GVCs. To reconstruct firm-level decision processes, we conducted retrospective interviews with former managers. To mitigate retrospective or impression-management bias, interview data were triangulated with contemporaneous company reports, METI publications, and trade journals.

Phase III: Post-keiretsu era (mid-2000s–present): Due to confidentiality constraints, access to current executives was restricted. Accordingly, analysis relied on triangulation of public corporate sources—investor-relations (IR) materials, analyst presentations, and reputable business media. These sources provided insight into how sōgō shōsha reconfigured governance portfolios and adapted to post-keiretsu environments.

Across all three phases, we draw on a range of qualitative and quantitative data sources (see Table 3-1).

Table 3-1

Description of data

Data Types	Amount	Use in Analysis
Newspaper articles		
Newspaper articles from four Nikkei-affiliated publications (1979–2024), and *Senken*	245 articles from *Nikkei, Nikkei Sangyo Shimbun, Nikkei MJ, Nikkei Finance Shimbun* ; *Senkeen Shimbun*	Used to construct macro-industry timelines and trace discursive changes in public narratives surrounding sōgō shōsha activities
Industry reports and quantitative data		
Textile and apparel statistics (1950–2023)	Ministry of Economy, Trade, and Industry, *Yearbook of Textiles and Consumer Goods Statistics* , 1950–2023, Japan Chemical Fiber Association (JCFA) *Seni Handbook,* 1959-2023, Statistics Bureau of Japan, *Historical Statistics of Japan* New Edition, vol. 3 2006	Tracked the production, import, and export of goods, including value, quality, destination, and locational shifts.
FDI directories (1978–2020)	Data from Mitubishi Research Institute, 21st Century China Research Institute (1,651 firms, 2,879 entries including Itochu (143), Mitsubishi (35))	Identified FDI patterns in China and assessed the change in governance modes, and the ownership structure
Interviews		
Semi-structured interviews with ex-executives and managers from ex-executive, ITOCHU Italiana S.p.A, ex-vice president, Armani Japan, and ex-director, Mitsubishi China	6 interviews at Tokyo, Osaka, Kyoto, Phone in 2020–2024	Traced firm-level strategic responses and governance adaptation
Company press releases (since 2001)	28 releases	Tracked coporatee and international strategies and business model transformation
EDINET corporate disclosures	Continuous filings	Triangulated investment behavior and validated changes

Note. Prepared by author.

3.3.2.1.Newspaper and trade-journal data

A total of 245 articles were collected from four Nikkei-affiliated publications—*Nikkei, Nikkei Sangyō Shimbun, Nikkei MJ,* and *Nikkei Financial Shimbun*—as well as *Senken Shimbun* (1979–2024). These sources were used to construct macro-level industry timelines and to trace discursive changes in public narratives surrounding sōgō shōsha. Event sequences, reported partnerships, and strategic announcements were coded chronologically, enabling the identification of critical junctures (e.g., trade liberalization, keiretsu erosion, WTO entry of China) that shaped shifts in product, location, and governance portfolios.

3.3.2.2.Industry reports and quantitative trade data

To capture industry-level dynamics, we analyzed extensive textile and apparel statistics from 1950–2023, including the *Yearbook of Textiles and Consumer Goods Statistics* (METI), the Japan Chemical Fiber Association's *Seni Handbook* (1959–2023), and the

Historical Statistics of Japan (2006). These datasets were used to trace changes in domestic production, imports/exports, product quality, and destination patterns. Following the FG model, shifts in comparative advantage and relocation waves were identified by examining changes in the production–import–export structure over time.

3.3.2.3.FDI directories

FDI records from the Mitsubishi Research Institute and the 21st Century China Research Institute (covering 1,651 firms and 2,879 entries, including 143 ITOCHU and 35 Mitsubishi investments) were used to examine the relationship between sōgō shōsha and their customers and suppliers in China. These data allowed assessment of changes in ownership structures, governance modes (e.g., equity JVs, wholly owned subsidiaries), locations, and sequencing of foreign entry strategies as institutional conditions evolved.

3.3.2.4.Interviews

To uncover decision-making processes behind observed patterns, we conducted six interviews (Tokyo, Osaka, Kyoto, and remote) with former executives from ITOCHU Italiana S.p.A., Armani Japan, and Mitsubishi China (2020–2024). These interviews provided insight into firm-level strategic responses, alliance formation, and governance adaptation—particularly in Cases ITOCHU–Armani and Mitsubishi–Fast Retailing. Interview evidence was systematically cross-checked with contemporaneous reports to mitigate retrospective bias.

3.3.2.5.Corporate disclosures and press releases

Press releases (28 items, post-2001), EDINET filings, and investor-relations documents were used to validate strategic shifts identified in other data sources. These

materials clarified the timing of business model transitions, investment decisions, and the evolution of governance structures.

3.3.3. Addressing Author Bias and Reflexivity

As noted by Verbeke et al. (2022), qualitative research may suffer from authorial bias due to selective interpretation or overemphasis on particular causal narratives. To mitigate such risks, the following measures were undertaken: multiple data sources (interviews, corporate archives, industry analyses) were triangulated to identify inconsistencies and corroborate findings (Fiss, 2009; Yin, 2018); quantitative data (financial statements, trade flows, portfolio ratios) were combined with qualitative evidence (interviews, archival documents, and historical analyses). Interpretations were continuously checked against alternative explanations drawn from both Japanese and international scholarship to avoid myopic conclusions.

3.4. Initial Theory

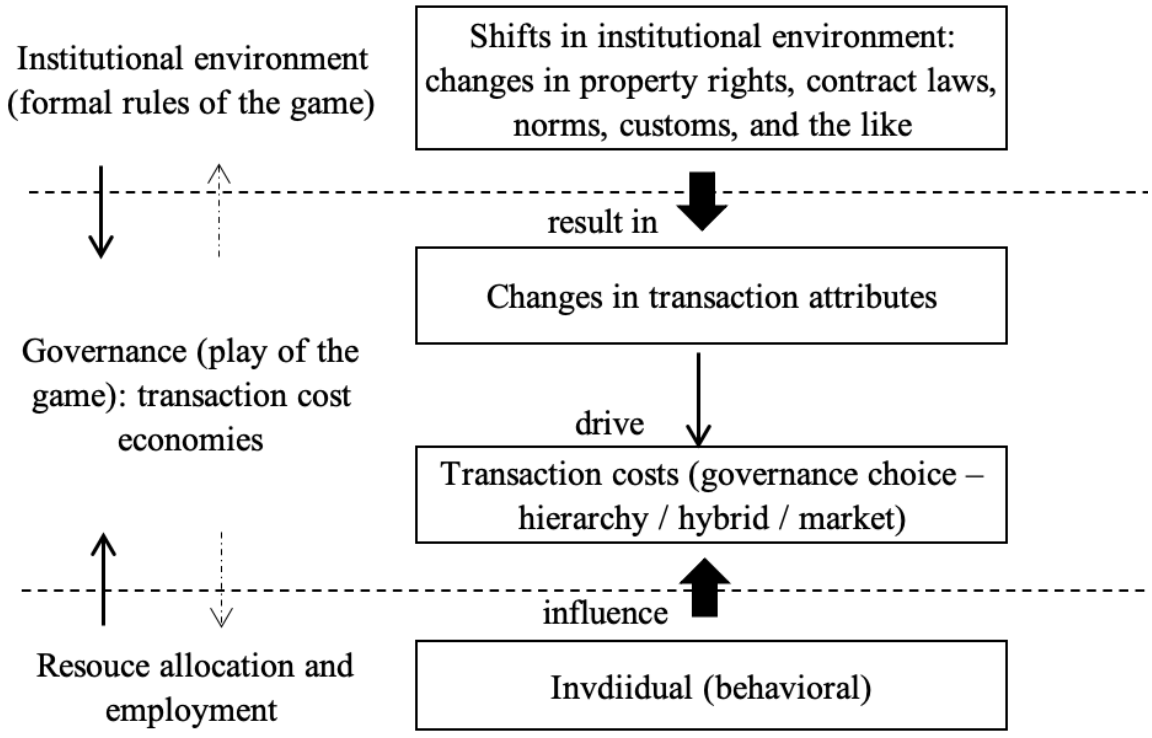
3.4.1. Transaction Cost Economics (TCE)

This study is anchored in TCE and its subsequent extensions, particularly as formulated by Williamson (1996, 2000). TCE provides a useful analytical foundation for examining how sōgō shōsha structure and adjust governance mechanisms in relation to their client MNEs. Historically, sōgō shōsha have operated as supporting rather than lead firms within GVCs, performing coordination, monitoring, and relational intermediation functions alongside (and on behalf of) MNEs. Unlike approaches that focus narrowly on internal resources or assume a lead-MNE–centric logic, TCE explicitly highlights inter-firm complementarities, making it well suited to analyzing the co-governance structures that characterize sōgō shōsha–MNE relations.

TCE rests on the discriminating alignment hypothesis: transactions defined by specific attributes—asset specificity, uncertainty, and frequency—should be governed through structures (market, hybrid, or hierarchy) that minimize the joint costs of production and transacting (Williamson, 1998; Cuypers et al., 2021). Governance choices, however, are not in isolation. As Figure 3−1 illustrates, transactions are embedded in and interact with two interdependent domains: (1) macro-level institutional environments, which define the formal and informal rules of exchange; and (2) micro-level behavioral conditions, rooted in human cognitive and motivational limitations (Williamson, 1996; Verbeke et al., 2023).

Figure 3-1

A Process of Transaction Cost Economizing



Note. Illustrated by author based on Williamson (1996, 1998, 2000); Kano et al. (2020); Verbeke et al. (2023).

Changes in the institutional environment—such as shifts in property-rights regimes, contract enforcement, financial regulation, or informal norms—act as shift parameters that alter the underlying conditions of exchange (Williamson, 1996; Hennart, 1991). The emergence or erosion of institutional voids modifies core transaction attributes, especially environmental uncertainty and the value and vulnerability of asset-specific investments (Khanna & Palepu, 1999). These changes prompt firms to reorganize governance structures, often across borders.

Governance choices are further constrained by two behavioral frictions. Bounded rationality captures limits to cognitive capacity when processing complex, ambiguous, and incomplete cross-border information (Williamson, 2006)—a critical issue for multi-country coordination (Verbeke et al., 2023). Bounded reliability is a broader and more realistic construct than opportunism (Williamson, 1985), encompassing benevolent preference reversals—unintentional deviations from commitments due to shifting priorities, misjudgment, or information overload (Verbeke & Greidanus, 2009; Kano & Verbeke, 2015). These frictions can be mitigated through governance mechanisms, including formal safeguards, relational norms, and entrepreneurship-oriented coordination tools (Verbeke et al. 2021; Verbeke, 2025).

Classical TCE typically treats the industry context as exogenous, because its analytical unit is the individual transaction framed within a buyer–seller dyad. By contrast, this study examines multi-actor broader governance arrangements, where exchange outcomes are shaped by interactions among a wider constellation of actors. In such settings, the "industry logic"—the competitive arena defined by buyers, suppliers, intermediaries, and potential entrants (Porter, 2007)—conditions the types of transaction hazards that arise and the governance challenges that follow. To capture these dynamics, we operationalize Williamson's original formulation by explicitly incorporating industry context and by

adopting the GVC as the unit of analysis. We conceptualize the GVC as a bundle of interdependent transactions. This broader lens is particularly salient for understanding sōgō shōsha, whose strategic trajectories are not purely autonomous or internally driven but are shaped by interactions with repeated waves of industrial restructuring that continually alter transaction attributes and coordination requirements. Over time, firm-level governance adaptations in response to such changes aggregate into large-scale transformations of industry itself.

TCE is sometimes criticized for its static orientation. We view TCE as explaining governance efficiency at a given point in time, while governance outcomes are understood as moving equilibria. Accordingly, we conduct an intertemporal analysis of strategic change by embedding TCE within historical inquiry and pairing it with dynamic theories of industrial transformation, as elaborated in the next subsection.

3.4.2. Industry-Level Dynamics: FG Model

While TCE provides a micro-analytic explanation of sōgō shōsha's governance portfolio, its explanatory power is limited without an intertemporal logic of industrial change. As Williamson (1998) notes, TCE can benefit from being paired with an appropriate dynamic theory that explains how the underlying conditions of exchange evolve over time[12]

We incorporate the Flying Geese (FG) model[13], an industrial development model to situate governance choices within shifting patterns of comparative advantage—across both products and locations—which in turn shape the evolution of sōgō shōsha's product and location portfolios (Akamatsu, 1962; Kojima, 2000; Ozawa, 2011).

[12] Williamson (1998, p. 30) note that "The upshot is that transaction costs economics is very much an intertemporal, adaptive, managerial exercise – although this is not to say that more dynamic theories or more prominent provisions for management are unneeded."

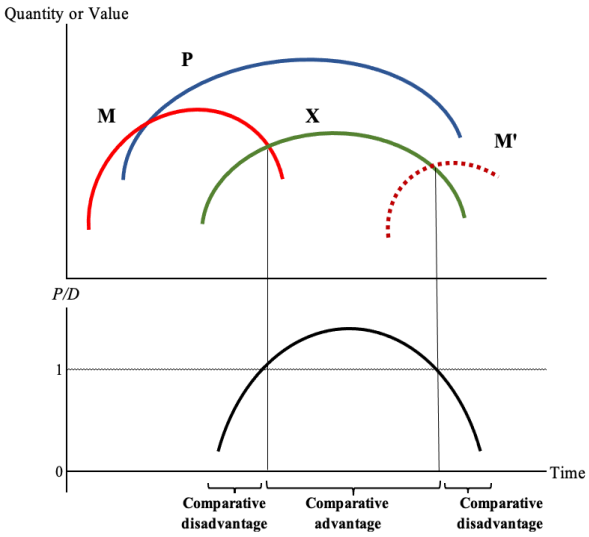
[13] While frequently criticized the FG model as Japan-centric approach (Lin & Chang, 2009; Lin, 2011; Kasahara, 2019), the model was originally conceived with a global perspective, positioning the United States as the lead "goose" (Ozawa, 2011).

As Ozawa (2011) summarizes, there are three industrial trajectories: (1) Pattern A, the *MPXM'* sequence which describes the full lifecycle of industrial activity: beginning with reliance on imports (M), progressing through domestic production (P), reaching export (X) maturity, and ultimately entering deindustrialization as comparative advantage diminishes (M'). Akamatsu's (1962) classic MPX sequence was later refined to $MPXM'$ by Shinohara (1996) to include a re-import phase (M'); (2) Pattern B, *structural upgrading,* refers to the movement from consumer goods to capital goods and/or from simple to refined goods; and (3) Pattern C, *cross-country industrial realignment,* reflects the spatial relocation of production from advanced to emerging economies in pursuit of cost efficiencies.

Adopting this broader interpretation, we use the FG model to trace industry-level transformations across product and geographic dimensions—the context within which firm-level governance adaptations occur. Figure 3-2 illustrates Pattern A, depicting how comparative advantage and disadvantage shift over time.

Figure 3-2

MPXM' sequence and shift in the comparative advantage and disadvantage



Note. Illustrated by author based on Akamatsu (1962), Shinohara (1996), Kojima (2000).

According to the model, the relationship among domestic demand (D), domestic production (P), imports (M), and exports (X) can be expressed as:

$$D = P + M - X. \quad (3-1)$$

Dividing both sides by D yields

$$1 = \frac{P}{D} + \frac{M - X}{D}. \quad (3-2)$$

When $P/D < 1$ and $0 < (M - X)/D$, the industry is in an import-substituting phase, typically reflecting comparative disadvantage. Conversely, when $P/D > 1$ and $(M - X)/D < 0$, the industry is in an export-oriented phase, indicating comparative advantage.

Close attention to industry-level transformation is essential for understanding sōgō shōsha's portfolio evolution—particularly during the postwar decades—because sōgō shōsha handled a substantial share of Japan's and East Asia's import–export flows at least until the 1980s (Kashio, 1964, p. 190; Sugino, 1997).

3.4.3. Sōgō Shōsha's Evolution

For analytical clarity, we conceptualize sōgō shōsha's evolutionary trajectories in textile and apparel GVCs as shaped by the dynamic configuration of three interdependent portfolios: product, location, and governance portfolios. TCE provides the micro-analytic lens for examining changes in governance portfolios, while shifts in product and location portfolios—consistent with the FG model—are largely driven by industry-level dynamics such as changes in comparative advantage and sequential production relocation. The historical analysis that follows traces how these three portfolios co-evolve over time.

3.5. TRANSFORMATION OF SŌGŌ SHŌSHA'S PORTFOLIOS

3.5.1. Phase I: Keiretsu-based Era (1950s–1980s)

Phase I captures how sōgō shōsha's portfolios expanded and diversified through a process shaped by rapidly shifting industry conditions (i.e., evolving comparative advantage across products and locations) under Japan's institutionally distinctive postwar environment.

3.5.1.1.Institutional contexts (1950s–1980s)

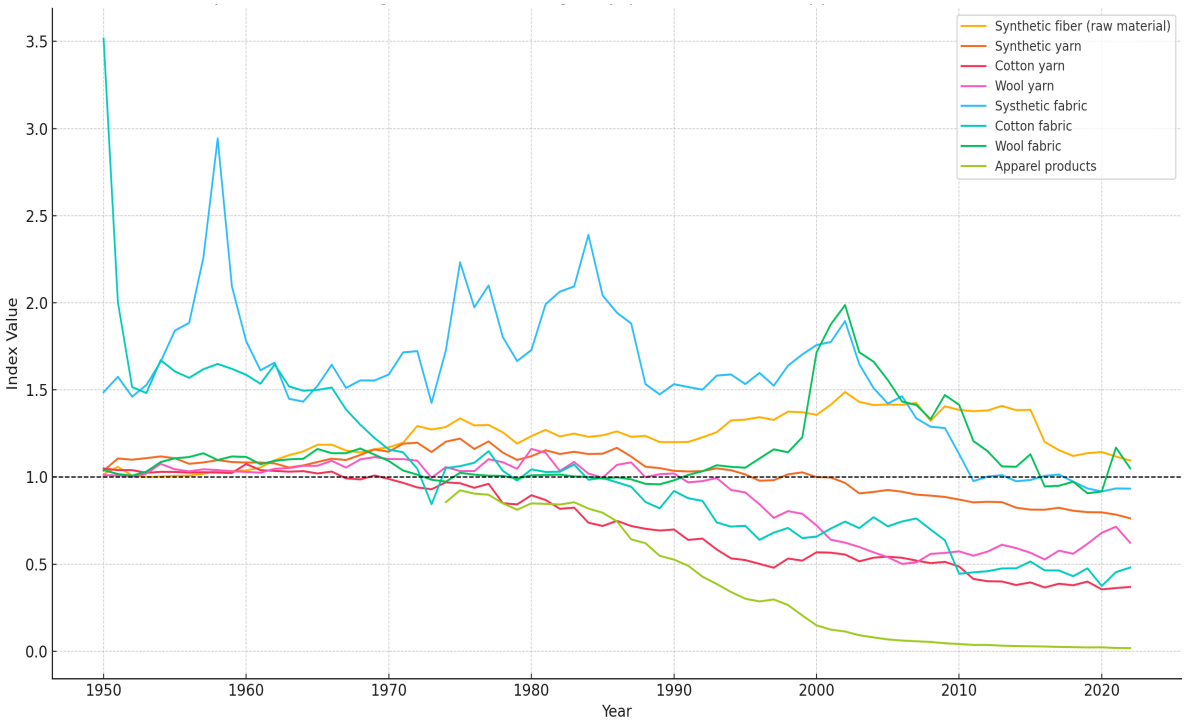
During the 1950s –1980s, within the vertical keiretsu structures led by major manufacturers, production was organized through multi-tier supplier networks comprising numerous small and medium-sized firms engaged in weaving, knitting, dyeing, sewing, and related processes (Ueda, 1973, p. 433). These production stages were tightly interlinked, with intermediaries involved at each step, creating a dense web of reciprocal control and dependence. The result was a highly complex structure of production and distribution (Ueda, 1973).

3.5.1.2.Industrial contexts (1950s–1960s)

In the immediate postwar period (1950s–1960s), Japan's textile and apparel industries were dominated by standardized, low–asset-specific goods such as cotton yarn, basic fabrics, and commodity apparel. As shown in Figure 3-2, the sector's strong comparative advantage lay in cotton and synthetic fabric, followed by woolen fabrics and synthetic fibers. Production was characterized by high-volume and relatively low coordination complexity. Under these conditions, transaction hazards were modest—both ex ante contracting difficulties and ex post enforcement risks were limited.

Figure 3-3

Comparative advantage and disadvantage in Japan's textile/apparel sectors, 1950–2022



Note. Author's calculation using data from the Japan Chemical Fiber Association (JCFA), the Statistic Bureau of Japan, and the Ministry of Economy, Trade, and Industry (METI).

3.5.1.3. Firm-level strategies (1950s–1960s)

This environment allowed sōgō shōsha to manage transactions efficiently through long-term, keiretsu-based relational ties. For textile-origin firms like ITOCHU, cotton fabrics formed the backbone of trading portfolios (Yagashiro, 2023). They sourced raw cotton from the United States, Mexico, and Ecuador and exported Japanese yarn and fabrics to Southeast Asian markets such as Indonesia. The dominant strategic logic of this period therefore centered on cost minimization and scale economies**,** with sōgō shōsha coordinating large volumes of standardized goods and managing globally fragmented location (trade) portfolios.

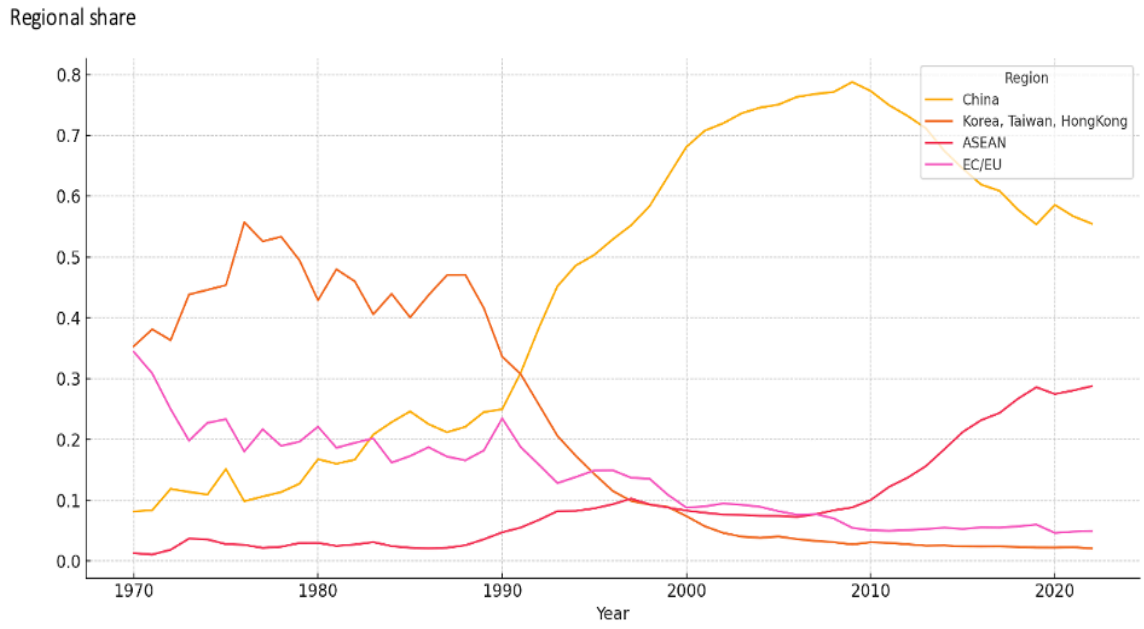
3.5.1.4. Industrial contexts (1970s–1980s)

By the late 1960s and early 1970s, Japan's export-oriented structure came under strain from three converging pressures: (1) rising domestic labor costs, (2) intensifying U.S.–Japan trade frictions, and (3) the yen appreciation following the 1971 Nixon Shock. These forces collectively eroded Japan's competitiveness in cotton textiles, triggering a structural shift. The 1985 Plaza Accord accelerated the erosion of Japan's comparative advantage in labor-intensive manufacturing. By 1991, the apparel industry's P/D index had fallen below the 0.5 threshold as shown in Figure 3-2 (M': re-import phase in Pattern A), indicating that imports accounted for nearly half of Japan's apparel consumption.

Two industry-level transformation unfolded simultaneously: (1) product upgrading: a transition from standardized cotton goods to refined, high–asset-specific synthetic fibers; and (2) locational shift: the offshoring of standardized production to NIEs—Korea, Taiwan, Hong Kong—followed later by China (see Figure 3-3.)

Figure 3-4

Locational transformation of Japan's textile/apparel imports, 1970–present



Note. Author's compilation based on JCFA, Statistics Bureau of Japan, and METI.

3.5.1.5.Firm-level strategies

As Japanese synthetic fiber firms expanded internationally, host economies implemented import-substitution policies. Sōgō shōsha played a central role in orchestrating tripartite joint ventures: Japanese synthetic textile manufacturer offered tacit technology, while the local partner brought in country-specific knowledge (Hennart, 1998). These structures allowed Japanese firms to retain upstream (raw material supply) control, while supporting partner countries' industrial upgrading (Yasumuro, 1998). By the mid-1970s, sōgō shōsha controlled roughly 60% of Taiwan's textile exports—an indication of their central role in orchestrating regional production networks.

For many Japanese SMEs expanding into NIEs, institutional distance and weak contractual enforcement raised external uncertainty. Sōgō shōsha reduced these hazards by

providing relational enforcement, and coordinating finance and logistics. Thus, they became critical brokers linking early-industrialized Japan with late-industrializing Asian economies.

3.5.1.6. NIEs to China (1970s–1990s)

Normalization of diplomatic relations in 1972 opened China to Japanese firms. Prior to this, only designated "friendly firms" could trade with China, forcing sōgō shōsha to rely on dummy companies for intelligence and exploratory exchanges (Noda, 2020). Sōgō shōsha increasingly acted not merely as intermediaries but as strategic catalysts, helping to drive the next Flying Geese wave, which actually surged during the 1990s (see Figure 3-3). Examples include: in 1979, ITOCHU pioneered compensation trade with Chinese SOEs—exchanging machinery for garment output—creating early subcontracting networks in Guangdong and Fujian, regions newly designated as Special Economic Zones[14]. Mitsubishi innovated multilateral trade forms, among British yarn spinner, Hong Kong apparel firms, and Chinese subcontractors[15]. In 1992, ITOCHU became the first Japanese firm granted national treatment in China, establishing wholly owned subsidiaries in Shanghai and Beijing[16]. These illustrate that sōgō shōsha were not simply "following" the regional relocation pattern; they were actively shaping production networks, often ahead of manufacturers.

By the late 1980s, Japan had emerged as a major consumption hub for refined, brand-intensive goods. Increased asset specificity created new governance challenges for foreign entrants unfamiliar with Japan's retail norms. The ITOCHU–Armani case illustrates how governance trajectories are shaped by complementarities between a lead MNE and local

[14] *Nikkei Sangyo Shimbun*, July 26, 1979. 伊藤忠、中国に衣料加工基地、紳士ズボン輸入へ [ITOCHU to establish garment processing base in China to import men's trousers].
[15] *Nikkei Sangyo Shimbun*, September 28, 1983. 繊維２次製品輸出に活路 [Exporting secondary textile products is a way forward].
[16] *Nikkei Shimbun*, December 12, 1993. 伊藤忠商事、対中国ビジネスを強化 [IITOCHU strengthens business in China].

actors, but ITOCHU's organizational logic remained deeply rooted in local relational ties and a home-market orientation even in the 1980s.

3.5.1.7.ITOCHU and the Armani GVC governance: engineering uncertainty

In luxury fashion, competitive advantage derives from symbolic attributes—exclusivity, aspiration, experiential value—that require substantial physical and human asset–specific investments (Kapferer & Bastien, 2012). Such idiosyncratic investments expose luxury brands to "free-riding, opportunism, and brand dilution (Hennart, 1991). Because these hazards threaten brand equity, tight control—often via vertical integration—is considered essential (Kapferer & Bastien, 2012).

Yet, international expansion creates a structural tension between control (to safeguard brand equity) and scalability (to accelerate market entry). Wholly owned subsidiaries preserve exclusivity but limit speed and flexibility. Licensing allows rapid market penetration but frequently results in down-market drift (Kapferer, 2015; Kapferer & Valette-Florence, 2016). Armani confronted this classic industry-specific trade-off when entering Japan, a market characterized by dense retail networks and complex institutional norms.

Armani's transition from a 1984 distribution agreement with Japanese department store Seibu to a more complex governance structure in 1987 was shaped by ITOCHU's intermediation. ITOCHU facilitated two tripartite joint ventures: (1) high-end imported goods: Armani–ITOCHU–Seibu; and mid-market licensed production: Armani–ITOCHU–Raika. In this architecture: licensing JVs accelerated market penetration; exclusive distribution channels protected brand value. ITOCHU's embeddedness in Japan's retail system reduced transaction hazards related to subcontractor monitoring, opportunism, and free-riding. This design allowed Armani to "scale without surrendering exclusivity"—a particularly difficult balance in Japan's multilayered retail environment.

While Armani benefited from ITOCHU's role—enforcing discipline within Japan's retail system—the governance architecture also reflected ITOCHU's logic in this era. Chairman and CEO Masahiro Okafuji's remarks in a 2011 Nikkei interview[17] capture their business philosophy in the 1980s:

"*There are three golden rules in the trader business: Do business with large companies, Keep business simple, and Don't let complaints arise. I said the exact opposite. Traders become unnecessary once clients' business is going well. So first, Do business with small and medium-sized firms. They need traders. Make the business structure as complex as possible, and welcome any problems that arise."*

Although referring to Italian brands Trussardi and Fila rather than Armani, Okafuji's statement reveals the logic underpinning ITOCHU's strategies in the 1980s. By "engineering" uncertainty or, more precisely, exploiting natural market imperfections, ITOCHU amplified its value-added role. Interview evidence further supports this interpretation. As one former ITOCHU executive noted,

"Giorgio was initially hesitant about licensing in Japan; it was ITOCHU that persuaded him to adopt the structure."

Armani's Japan strategy co-governed with ITOCHU demonstrates how governance structures evolve to reconcile short-term expansion needs with long-term brand protection under conditions of high uncertainty and high asset specificity. Armani became financially successful through a license-based, ITOCHU-embedded joint venture. At the same time, the organizational logic guiding ITOCHU's behavior remained strongly home-country oriented

[17] *Nikkei Shimbun*, 5 September 2011. 伊藤忠商事社長岡藤正広氏（下）商社の鉄則、逆張りで勝負 [Masahiro Okafuji, President of ITOCHU Corporation, break the rules: bet against the market].

and exhibited features reminiscent of firms in emerging-economy contexts, which often rely on informal modes of exchange within a formal sector (Verbeke & Kano, 2013).

3.5.2. Phase II: Keiretsu Erosion (1990s–Mid–2000s)

3.5.2.1. Institutional and industry contexts: withering of keiretsu

As Lincoln and Shimotani (2009) document, the 1990s witnessed a weakening of keiretsu networks especially horizontal ones: cross-shareholdings were unwound, main-bank authority diminished, and firms began to unravel under the combined pressures of economic stagnation and external liberalization demands, particularly from the United States (Shimotani, 2006). Vertical keiretsu networks also weakened (Lincoln & Shimotani, 2009). Industry accounts provide evidence of this structural shift. A 1997 January newspaper[18] captures the logic of the era:

"Toray decided to begin local production of polyester raw materials and yarn in China in September 1998… Rather than choosing a trading company as a joint venture partner, the company decided to proceed with sole investment. It is unusual for the company not to rely on a trading company from the start. This unprecedented move is spreading beyond Toray. A sōgō shōsha executive explains, "unless there is a significant risk, manufacturers with accumulated know-how no longer need the help of trading companies."

Simultaneously, sōgō shōsha began making moves that diverged from group-based ties and loyalties. The same report notes that:

[18] *Nikkei Sangyō Shimbun*, January 7, 1997. ニッポンから商社が消える日（４）本社空洞化、繊維が口火――取引の軸アジアに [The day trading companies disappear from Japan (4) Headquarters hollowing out, textiles as the first move - Asia as the center of trade].

"Last year, Marubeni entered India and launched a spinning factory through a joint venture with a Korean textile manufacturer. This disadvantages Japanese manufacturers when the yarn is re-imported into Japan."

This disintermediation trend is also visible in our FDI directory data on Japanese investments in China. From the late 1990s onward, major textile manufacturers such as Teijin increasingly opted for wholly owned investments rather than joint ventures with sōgō shōsha.

3.5.2.2.Firm-level strategies

In January 1990, the annual statements of Japan's major sōgō shōsha collectively signaled a strategic repositioning, reflecting a shared aspiration to shift from home-anchored relational coordination toward outward-looking global engagement. They introduced conceptual anchors such as "global" and "international," signaling this transition. Among them, ITOCHU was historically rooted in the logic of local commercial districts and regionally embedded networks—an orientation that shaped its distinctive trajectory relative to the zaibatsu-origin sōgō shōsha. This shift was codified in the 1992 revision of ITOCHU's mission statement as *"committed to the global good."* Further evidence of this identity transformation appears in ITOCHU's 2019 CSR Report, which retrospectively frames the firm's post–1992 strategy as an effort to dismantle legacy structures heavily tied to local networks, and rebuild the organization as a globally oriented enterprise.

Other shifts occurred in 1997, when ITOCHU began to transfer entire corporate functions such as budgeting, risk management, and strategy formulation in the textile business[19]—the fulcrums for managing its entire portfolio—overseas. For example, ITOCHU established a wholly owned subsidiary in Hong Kong for controlling its entire textile business

[19]*Nikkei Sangyō Shimbun*, January 7, 1997. ニッポンから商社が消える日（４）本社空洞化、繊維が口火――取引の軸アジアに [The day trading companies disappear from Japan (4) Headquarters hollowing out, textiles as the first move - Asia as the center of trade].

and headquarters in Sydney for wool yarn[20]. Collectively, these shifts illustrate how ITOCHU aligned its corporate governance logic with changes in institutions, or formal rules of the game.

Mitsubishi likewise shows how it reoriented strategies by creating and developing new value chains and by solving acute trade-offs MNEs face through governance mechanisms, under institutional and operational uncertainty—particularly with non-keiretsu partners such as DuPont (as detailed in the next chapter) and Fast Retailing (FR) below.

3.5.2.3. GVC governance: Mitsubishi and Fast Retailing

In the 1990s, Mitsubishi created a China-centered supply-chain architecture for Fast Retailing (FR), assuming key orchestration functions including product planning, raw-material procurement, supplier coordination, and inventory management. As detailed in the next chapter, this alliance-based structure mitigated the substantial hazards associated with subcontracting in an underdeveloped institutional environment—specifically, weak contract enforcement and heightened intellectual-property risks in early–1990s China (Schotter & Teagarden, 2014). In the formative phase of FR's value chain, this architecture enabled the firm to capture the flexibility benefits of outsourcing while economizing on the high transaction costs typically associated with externalized production of highly asset-specific, technology-intensive items under politically volatile environments.

Mitsubishi's involvement in FR's value chain can be understood as a governance innovation when viewed against global shifts in fast-fashion governance. Cattaneo et al. (2010, p. 202, Table 5A. 8) document how one leading fast-fashion retailer moved from near-complete vertical integration (with 100% of production in Spain in 1990) to a hybrid global

[20]*Nikkei Shimbun*, July 7, 1998. 伊藤忠や三菱商事、中国で繊維部門強化——現法設立など、対日輸出を拡大 [ITOCHU corp. and Mitsubishi corp. strengthen textile divisions in China, expanding exports to Japan through the establishment of local subsidiaries].

sourcing structure by the mid–2000s: roughly 50% of high-fashion, highly asset-specific items continued to be produced in Spain under tight hierarchical control, while standardized basics (T-shirts, knitwear) were increasingly sourced from China, Bangladesh, and North Africa. This pattern is consistent with the original TCE logic that highly specific products, and design-intensive items should be produced in-house.

In contrast, and ahead of many industry peers and against the economic theory, Mitsubishi facilitated a novel governance architecture that addressed FR's flexibility–control trade-off. Its role exemplifies how, during this transitional phase, Mitsubishi engineered contextually adaptive governance that bridged the structural requirements of fast fashion with the institutional constraints of emerging-market production systems.

3.5.3. Phase III: Post-keiretsu Era (Mid–2000s–Present)

3.5.3.1.Institutional and industrial contexts

Japan's liberalization of finance, corporate governance, and capital markets effectively dissolved the institutional voids that had once justified the existence of keiretsu as relational substitutes for missing market institutions (Lincoln & Shimotani, 2009). At the industry level, this period was driven by China's ascent as consumer market. The policy shift in China in 2004 and its liberalization of wholesale and retail sectors (Yahagi, 2008), permitted sōgō shōsha to operate as fully integrated "general" trading companies within China that encompassed a range of non-trading functions. The result was a profound transformation in strategic posture, as sōgō shōsha began reconfiguring their portfolios, and adopting more globally integrated operational models in the post-keiretsu era.

3.5.3.2. Firm-level strategies

The data on Japan's FDI outflow to China indicates ITOCHU's structural transformation in ownership patterns since the turn of the 21st century (see Table 3-2): the

proportion of ITOCHU ventures majority-owned by Chinese partners rose sharply—from 16 percent before 2000 to 66 percent thereafter—while the share of Japanese-majority ventures declined from 79% to 29%. These patterns signal a deliberate strategic move toward deeper resource commitments to China. Following this shift, ITOCHU further consolidated its position within China's textile and apparel sectors by forming equity-based alliances across multiple stages of the chain. These included partnerships with yarn producers (e.g., Veken Group, Weiqiao Textile), textile manufacturers (e.g., Younger, Luthai Textile), and apparel brand operators (e.g., Qingdao Jifa). By the mid–2010s, ITOCHU had constructed a comprehensive value chain platform in China (see Appendix 3-C), culminating in its strategic alliance with state-run conglomerate CITIC, marked by $5 billion equity investment. This alliance underscored its evolution toward a full-spectrum GVC orchestrator in China. As one ITOCHU former executive noted regarding the firm’s expansion in China, the brand management expertise obtained through the collaboration with foreign brands in Japan was fully utilized in these JV management in China.

Table 3-2

Investment patterns of ITOCHU and Mitsubishi, 1988–2014

Governance mode and investment type			Sōgō shōsha's ownership ratio	Joint venture partners
Wholly owned subsidiary (Holding company, logstics, trading, etc)		**A**	100%	n/a
Wholly owned subsidiary (Apparel manufacturing)		**A'**	100%	n/a
Type of Joint venture	Two-party joint venture	**B**	Majority	Japanese firm
		B'	Minority	Japanese firm
		C	Majority	Chinese firm
		C'	Minority	Chinese firm
	Multi-party joint venture	**D**	Majority	Japanese firms only
		D'	Minority	Japanese firms only
		E	Majority	including Chinese firm(s)
		E'	Minority	including Chinese firm(s)

ITOCHU

	A																	B	C	A+B+C
	100%		50:50 owenership			Majority owned by Chinese firms				Majority owned by Japanese firms								JV	Unknown	**Grand total**
Investment type	A	A'	C'	E'	**Total**	C	C'	E'	**Total**	B	B'	C	D	D'	E	E'	**Total**	**Total**		
Before 2000 (a)	13	0	1	3	**4**		1	11	**12**	1	12	1	3	10	1	33	**61**	**77**	1	**91**
After 2000 (b)	4	10		2	**2**	1	8	16	**25**	1	3				2	5	**11**	**38**	0	**52**
Total (a+b)	17	10	1	5	**6**	1	9	27	**37**	2	15	1	3	10	3	38	**72**	**115**	1	**143**
Before 2000	n/a	n/a	1%	4%	**5%**	0%	1%	14%	**16%**	1%	16%	1%	4%	13%	1%	43%	**79%**	**100%**		
After 2000	n/a	n/a	0%	5%	**5%**	3%	21%	42%	**66%**	3%	8%	0%	0%	0%	5%	13%	**29%**	**100%**		

Mitsubishi

	A		JV															B	C	A+B+C
	100%		50:50 owenership			Majority owned by Chinese firms				Majority owned by Japanese firms								JV	Unknown	**Grand total**
Investment type	A	A'	C'	E'	**Total**	C	C'	E'	**Total**	B	B'	C	D	D'	E	E'	**Total**	**Total**		
Before 2000 (a)	7	0		2	**2**		1	2	**3**		4	2		1	2	7	**16**	**21**	0	**28**
After 2000 (b)	2	1			**0**		1		**1**						1	2	**3**	**4**	0	**7**
Total (a+b)	9	1	0	2	**2**	0	2	2	**4**	0	4	2		1	3	9	**19**	**25**	0	**35**
Before 2000	n/a	n/a	0%	10%	**10%**	0%	5%	10%	**14%**	0%	19%	10%	0%	5%	10%	33%	**76%**	**100%**		
After 2000	n/a	n/a	0%	0%	**0%**	0%	25%	0%	**25%**	0%	0%	0%	0%	0%	25%	50%	**75%**	**100%**		

Note. Author's calculations based on data from Mitsubishi Research Institute and the 21st Century China Research Institute.

Mitsubishi followed a parallel but more decisive trajectory in terms of exiting apparel and fashion, and reallocating capital to higher-value activities. As global competition intensified and FR internalized core functions, Mitsubishi progressively divested from low-margin, asset-specific apparel operations. By the late 2010s, its apparel activities were limited to selected overseas marketing ventures[21]. Between 2024 and 2025, it exited the apparel sector entirely, selling its SPA unit to Muji and its wholly owned subsidiary Mitsubishi Corporation Fashion to World Co.[22] These decisions reflect a deliberate strategy to shed overhead tied to asset-specific OEM operations and to reallocate capital toward higher-value-added sectors and investment-intensive GVCs, thereby supporting an aggressively global corporate footprint (see Appendix 3-B).

[21] *Mitsubishi Corporation*, August 30, 2018, ベトナムにおける合弁会社に関するお知らせ [Notice regarding joint venture in Vietnam]

[22] *Senken*, December 2, 2024, 三菱商事ファッションがワールド傘下に商社 OEM を取り巻く事業環境を象徴 [Mitsubishi Corporation Fashion becomes a subsidiary of World Co.].

3.6. DISCUSSION

Table 3-3 summarizes our historical findings, synthesizing the longitudinal evolution of Japan's sōgō shōsha across three institutional periods—keiretsu-based, keiretsu erosion, and post-keiretsu—and shows how their product, location, and governance portfolios transformed as the institutional environment and industry logic shifted.

Table 3-3

Three-phase transformation of sōgō shōsha's portfolios in textile and apparel value chains

	Phase I General Trading Company	**Phase II** Toward a MNE-trader	**Phase III** MNE-trader
	1950s - 1980s	1990s to mid-2000s	Mid-2000s to present
Institutional environment	Keiretsu-based	Keiretsu erosion	Post-keiretsu
IV theory prediction	Persistence of BG	Disappearance of BG	
Commertial capital theory prediction	Disintermediation inevitably occurs		
Our Findings			
Strategy	Portfolio Diversification	Portfolio Orchestration	Radical Portfolio Reconfiguration
Product	Simple goods to refined goods (since 1970s)	Refined goods	Beyond industry
Location	Home-based	Home-based	Beyond home (highly internationalized)
Governance	Non-lead MNEs	Non-lead MNEs	Non-lead MNEs to lead MNEs (ongoing)

Note. Compiled by author.

3.6.1. Phase I: Keiretsu-based Era: Portfolio Diversification (1950s–1980s)

In Phase I, sōgō shōsha's product portfolios were dominated by standardized, low asset specific goods—cotton and basic textiles. The dominant strategic logic centered on minimizing production costs through scale economies by managing high-volume transactions (Roehl, 1983). As industrial upgrading in the textile–apparel GVC progressed in the 1970s,

comparative advantage shifted from these standardized goods toward more refined, high–asset-specific products. This change in asset specificity gradually increased transaction hazards for Japanese manufacturers leading their value chains and began to create new governance demands.

Location portfolios evolved in parallel. Sōgō shōsha handled a large share of Japan's export and import flows (UNCTAD, 1995; Dunning & Lundan, 2008). Operations were initially home-based and centered on Japanese manufacturers, but sourcing and production steadily expanded from Japan to the NIEs and later to China, consistent with the Flying Geese pattern. These moves into new locations and unfamiliar institutional environments created external uncertainty for Japanese manufacturing MNEs. Sōgō shōsha were not only "riding" these waves; they actively shaped them—pioneering compensation trade, early subcontracting systems, and proto–GVC forms.

Governance portfolios reflected this bridging role. In outbound chains, sōgō shōsha filled gaps between early-industrialized Japan and late-industrializing environments (NIEs, China), orchestrating regional production networks through devices such as tripartite joint ventures. In inbound chains—most notably the entry of Western luxury brands into Japan in the 1980s—the governance problem was reversed: foreign firms confronted high transaction costs in a complex, multi-layered domestic market underpinned by dense social and cultural practices (Dunning & Lundan, 2008). During this period, sōgō shōsha accumulated tacit knowledge by absorbing these costs and mediating between foreign entrants and domestic institutions.

Phase I thus was characterized by the combination of rapid industrial upgrading with the features commonly associated with emerging markets: multi-layered distribution channels, opaque relational networks, and heavy reliance on tacit knowledge and commercial custom. Within this context, sōgō shōsha operated inside dense keiretsu structures, leveraging

their global reach and domestic networks to support both Japanese MNEs expanding abroad and foreign MNEs entering Japan's relationally governed market—consistent with earlier studies that emphasize the advantage of dense local networks (Buckley, 1985; Dunning & Lundan, 2008). Postwar strategies were hence outward-looking in geographic scope but remained anchored in a Japan-centric governance logic, as illustrated by ITOCHU's continued reliance on domestic norms even under growing international scrutiny in the late 1980s.

Recent work by Bucheli et al. (2018) argues that Chilean BGs survived by deliberately constructing monopolistic "structural market imperfections." In contrast, our evidence suggests that in late–1980s Japan, ITOCHU enhanced its indispensability by exploiting—and, to some extent, engineering—uncertainty and bounded rationality at the transactional level, leveraging what IB scholars might describe as "natural market imperfections". Yet it also created complementarities with foreign MNEs. In the Armani–ITOCHU case, ITOCHU resolved acute governance trade-offs—balancing rapid market penetration with long-term brand preservation—by designing innovative governance arrangements that combined multiple entry modes.

BG literature typically explains diversification as a defensive response to institutional voids. Product diversification is seen as protecting affiliates from expropriation (Holmes et al., 2018), while internal capital, labor, and input markets substitute for missing or inefficient institutions (Khanna & Palepu, 1997, 2000). Diversification, under this logic, is a structural response to market failure.

Our findings point to a different mechanism; diversification was driven less by defensive motives than by a structural imperative rooted in Japan's industrial upgrading and by sequential waves of relocation in textiles and apparel. Rapid upgrading and successive shifts from Japan to the NIEs and subsequently to China generated continuous opportunities

for arbitrage and coordination. Sōgō shōsha were not passive beneficiaries of these shifts; they experimented with new trade forms across countries, orchestrated tripartite joint ventures in Taiwan and elsewhere, and designed early subcontracting structures that anticipated later GVC configurations —consistent with portrayals of trading companies as highly entrepreneurial entities (Jones, 1998).

Moreover, diversification was self-reinforcing. As sōgō shōsha expanded into new sectors and regions, they accumulated firm-specific advantages (FSAs) in information-processing, cross-border coordination, and governance design. These FSAs lowered the marginal cost of subsequent expansion and facilitated further diversification. In this respect, we concur with prior research suggesting that BG competitiveness before reforms depends on capability accumulation that later becomes globally portable (Guillén, 2010), while emphasizing a complementary mechanism regarding the way of capability accumulation: by virtue of their role as general trading companies, sōgō shōsha were continually exposed to heterogeneous institutional environments. This exposure enabled capability accumulations.

3.6.2. Phase II: Keiretsu Erosion: Portfolio Orchestration (1990s–Mid–2000s)

In Phase II, product portfolios became centered on refined, high–asset-specific goods, especially in technologically sophisticated apparel ("tech fashion") for Mitsubishi and luxury brands for ITOCHU. These products required tighter coordination and more complex hybrid governance structures for both mature and emerging MNEs. Location portfolios deepened in China as the region became a central node in GVC restructuring: initially dispersed international operations gradually became more China-focused. This evolution aligns with Goerzen and Makino's (2007) observation that sōgō shōsha move from relatively non–location-specific to more location-specific activities over time. Governance portfolios simultaneously underwent significant change. Internally, firms initiated corporate governance

reforms and restructuring, particularly at ITOCHU, which progressively shifted from a Japan-centric to a more globally oriented organizational architecture. Externally, sōgō shōsha developed innovative governance solutions to navigate conflicting institutional systems—for example, bridging subcontracting hazards and enforcement gaps in China—most clearly seen in the strategic alliance between Fast Retailing (FR) and Mitsubishi. Sōgō shōsha increasingly engaged with non-keiretsu firms, constructing governance structures that combined structural safeguards with relational mechanisms.

These portfolio shifts unfolded against the backdrop of keiretsu erosion. As Japan's financial, distribution, and information infrastructures matured in the 1990s and early 2000s, the institutional foundations that had underpinned keiretsu coordination weakened (Shimotani, 2006; Lincoln & Shimotani, 2009). Financial crises further eroded cross-shareholdings and main-bank authority, diminishing the advantages of intra-group coordination. During this period, both overall (Appendix 3-A) and textile-related profitability among sōgō shōsha remained subdued, suggesting that the traditional business model—heavily reliant on domestic relational capital—was reaching its structural limits.

Existing BG scholarship often emphasizes "refocusing" strategies—the shedding of non-core or unproductive assets—as a key survival mechanism during institutional transitions in emerging markets (Hoskisson, et al., 2005; Carney et al., 2017b). Cases such as CEMEX in Mexico, which pursued internationalization while narrowing its product focus in response to liberalization (Lessard & Lucea, 2009), exemplify this pattern. Indeed, the governance structures and legacy assets that previously generated value may become liabilities when underlying industry or institutional logics shift (Suddaby et al., 2020).

Our findings indicate that sōgō shōsha also engaged in selective withdrawal from obsolete product lines and business domains, often at a rapid pace across phases. These reconfigurations involved substantial portfolio pruning. However, sōgō shōsha did not rely on

refocusing or asset shedding alone. In parallel, they embarked on selective recombination, adding new product–location combinations as comparative advantage shifted regionally. Phase II coincided with a major relocation of upstream production such as synthetic fiber from the NIEs to China; Mitsubishi's product–location portfolios were recomposed in ways that supported the emergence of the fast fashion industry.

The Mitsubishi–FR partnership illustrates the nature of this strategic shift. Mitsubishi moved beyond intra-keiretsu relational coordination toward constructing cross-border governance systems capable of bridging heterogeneous institutional environments—Japan, China, Hong Kong, and other economies. These arrangements were particularly important for managing the heightened transaction costs associated with fragmented, fast-cycle fashion production and rising technological and logistical complexity.

The extant literature predicts that as market-supporting institutions mature, arm's-length contracting should become more feasible and the value of BG affiliation should decline (Carney et al., 2017b; Hoskisson, et al., 2005). Our cases are consistent with this prediction in an advanced-economy context and show that sōgō shōsha survive by developing higher-order governance FSAs, forming new hybrid alliances to orchestrate emerging GVCs and to support the creation and development of new industries and business models.

Taken together, these developments suggest that Phase II marked a transitional period in which sōgō shōsha redefined their governance logic both internally and externally. Rather than relying primarily on keiretsu-based relational governance, they began to orchestrate multi-layered governance portfolios suited to a global competitive context. Thus, instead of becoming obsolete, sōgō shōsha reorganized their coordination mechanisms and corporate governance in ways that enabled them to operate effectively beyond the boundaries of the keiretsu system.

3.6.3. Phase III: Post-keiretsu Era: Radical Portfolio Reconfiguration (Mid-2000s–Present)

In Phase III, product portfolios remained anchored in refined, high–value-added goods, but with a marked shift in strategic emphasis. For ITOCHU, brand management capabilities accumulated through collaborations with Italian luxury brands were redeployed in China, in line with IB arguments that inbound FDI can catalyze industrial restructuring and subsequent outward expansion (Dunning & Narula, 1996; Meyer, 2006). Firms moved beyond domestic mediation toward global asset ownership and deeper value-chain integration. By contrast, Mitsubishi's recent moves indicate a deliberate exit from apparel: it progressively withdrew from SPA and OEM activities and eventually divested its remaining apparel-related units.

Location portfolios in this era became highly internationalized. Overseas revenue ratios rose sharply, particularly for Mitsubishi, reflecting a shift toward outward-looking global orchestration. Mitsubishi's consolidated overseas sales ratio increased from 18.5% in 2010 to 41.1% in 2020 and 50.9% in 2024 (Appendix 3-B). ITOCHU's overseas sales ratio followed a more moderate trajectory—25.0% in 2010, declining to 20.9% in 2020 and recovering to 23.6% in 2024—partly reflecting China's economic slowdown (ITOCHU, 2024). Both firms thus moved toward global orientation, with Mitsubishi doing so more rapidly and decisively.

Governance portfolios underwent the most profound change. Sōgō shōsha increasingly shifted from non-lead, supporting roles within GVCs toward more central, orchestrator-like positions in selected segments. This evolution is visible in activities such as acquiring Western brands, building multi-stage JV platforms in China (e.g., ITOCHU's alliances spanning yarn, textiles, and apparel operators), and leading cross-border industrial platforms and multi-country JV structures. Mitsubishi's former chairman Kakiuchi

emphasized the firm's supporting role vis-à-vis client MNEs in a 2016 interview, but subsequent statements by CEO Nakanishi point to a strategic move toward lead-type orchestration rather than pure coordination.

Financial performance mirrored these strategic shifts. ITOCHU and Mitsubishi improved profitability, markedly from the mid-2000s onward (Appendix 3-A), a pattern consistent with Carney et al.'s (2017b) scenario in which BGs reposition themselves as nationally—and eventually internationally—competitive enterprises once institutional voids diminish.

A defining characteristic of Phase III is the pronounced reconfiguration of product, location, and governance portfolios. Mitsubishi's withdrawal from entire apparel-related industries and reallocation of capital toward higher value chain activities exemplify this shift. Whereas both firms traditionally operated as non-lead actors behind manufacturing MNEs, global brands, or major retailers, evidence suggests that they increasingly assumed more central roles in selected value-chain segments.

This emerging role is partly linked to FSAs cultivated in earlier phases: the ability to bridge heterogeneous institutional environments, integrate suppliers across multiple geographies, and stabilize transactions under deep uncertainty. As such capabilities became more valuable in contemporary GVCs characterized by bounded rationality and bounded reliability. They themselves have gradually become diversified global enterprises with orchestration capabilities that, in some contexts, resemble those typically associated with lead MNEs.

3.7. CONCLUSION

Akamatsu (1947) conceptualized world economic development as a dialectical process in which followers catch up and leaders respond through further innovation: the

Flying Geese (FG) pattern unfolds through repeated cycles of contradiction, negation, and higher-order synthesis, with each stage resolving tensions from the previous one while laying the groundwork for subsequent upgrading. Sōgō shōsha operated within these cycles as comparative advantage in both products and locations shifted rapidly. Our findings suggest that they did not simply adapt passively to these dynamics. Rather, they actively shaped them by navigating and recombining shifting institutional, industrial, and organizational logics.

The study contributes to IB and BG research by illustrating how diversified, non-manufacturing, BG-derived firms evolve after institutional voids diminish. Our findings suggest that the evolution of sōgō shōsha involves a more complex and multi-layered process than existing studies imply. Our historical delineation makes clear that sōgō shōsha's evolutionary trajectory was far from straightforward or linear. The changes in external environments transformed the context within which diversification, refocusing strategies, and internationalization strategies took place. These strategies occurred concurrently or iteratively.

Through a history-informed abductive approach, we translate this complexity into a three-phase model that captures changes in sōgō shōsha's portfolios in textile and apparel value chains and introduces a TCE-informed governance dimension largely absent from prior frameworks. This model helps enrich BG literature beyond its traditional focus on emerging economies and early-stage institutional development.

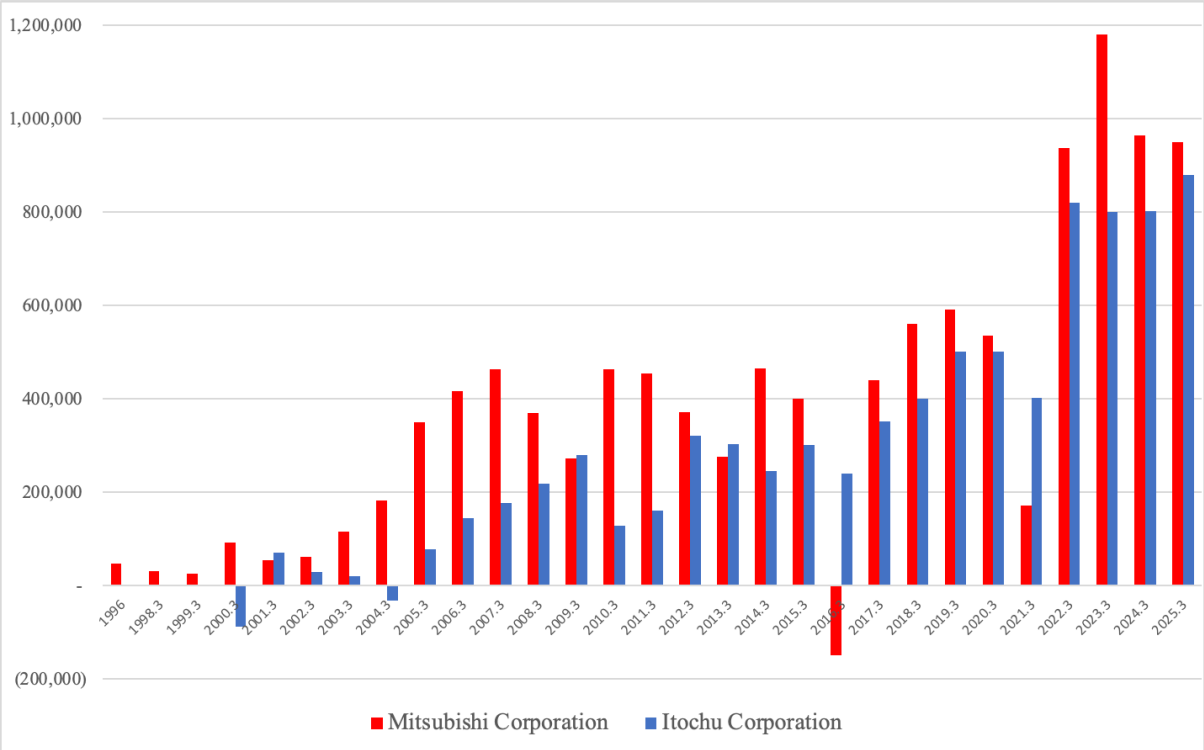
As Welch et al. (2016, 2022) emphasize, understanding processes of change often requires integrating multiple levels of analysis and acknowledging temporal complexity. Aaltonen (2020) adds that more analytical work is needed to specify the most productive combinations of theories and their respective boundary conditions. Through this study, we also concur that to explain the evolution of sōgō shōsha, a more pluralistic, multi-theoretical approach provides a more complete account.

From a managerial perspective, and contrary to the dominant view that diversification necessarily leads to inefficiencies—commonly referred to as the "conglomerate discount" (*The Economist*, 2020; Calhoun, 2020)—our findings demonstrate that, when purposefully managed, diversification can serve as a source of creative advantage. Sōgō shōsha sustained their competitiveness by dynamically reconfiguring product–location combinations and by deploying governance structures tailored to transaction-specific characteristics.

Future research could extend these insights in at least two directions. First, scholars could examine how similar governance transformations unfold across different sectors and geographic settings. Second, further work could investigate the recent strategic moves of sōgō shōsha. Mitsubishi's strategic repositioning under new leadership, for example, suggests that sōgō shōsha may now be transitioning into full-fledged value chain leaders. This raises important questions about how GVC governance and leadership are constructed, contested, and institutionalized in an increasingly volatile and multipolar global economy.

Appendix 3-A

Adjusted Consolidated Profits (Mitsubishi Corporation vs. ITOCHU Corporation)



Note. Created by author based on financial reports (Year Ended March 31, in Millions of Japanese yen).

Appendix 3-B

Consolidated Revenues by Area (Japan vs. Overseas)

Mitsubishi Corporation

Financial year	Revenue by Area	
	Japan	Overseas
2000.3	87.5%	12.5%
2005.3	83.2%	16.8%
2010.3	82.8%	17.2%
2015.3	69.9%	30.1%
2020.3	54.8%	45.2%
2025.3	49.1%	50.9%

Itochu Corporration

Financial year	Revenue by Area	
	Japan	Overseas
2000.3	67.4%	32.6%
2005.3	65.4%	34.6%
2010.3	63.1%	36.9%
2015.3	63.5%	36.0%
2020.3	77.6%	22.4%
2025.3	76.4%	23.6%

Note. Computed by author based on Mitsubishi and ITOCHU's financial reports.

Appendix 3-C

ITOCHU's Joint venture companies in China

	Company name	Ownership structure	Founded on	Business area
Raw Materials	Ningbo Veken Textile Co., Ltd	Itochu Corp (5%), Nisshimbo (25.0%), Vekken Group (70%)	2003	Cotton yarn, Textiles
	Qingdao Nikke Fabric Co., Ltd	Itochu Corp (37.5%), Nikke Textile (62.5%)	1996	Wool yarn
Yarn	Shangdong HengTai Textile Co., Ltd.	Itochu Corp (25%), Weiqiao Textile Co.,Ltd (75%)	2002	Compact Yarn
Textiles	Ningbo Youngor Woolen Dyening and Finishing Co., Ltd.	Itochu Corp (17.5%), Youngor Group Co., Ltd. (75%), HongKong Youngor International Holdings Co., Ltd (7.5%)	2004	Woolen dyening and finishing
	Luthai Textile Co., Ltd.	Itochu Corp (10.2%), Weiqiao Textile Co.,Ltd (75%), local enterprise (14.8%)	1997	Spandex yarn production and distribution
	Younger Knitting Dyeing and Finishing Co., Ltd.	Itochu Corp (19.9%), Youngor Group Co., Ltd.(70.1%), Xin Da Hong Kong (6%), Matsunaga Group (4%)	2002	Kniting, Dyeing and Finishing
	Suzhou Yifeng Dyeing Co.,Ltd.	Itochu Corp (25%), Itochu Service (24%), Suzhou Yifeng (51%)	2004	synthetic linings production and distribution
	Hangzhou Asahikasei Textiles Co., Ltd.	Itochu Corp (30%), Asahikasei (62.5%), Wacoal (7.5%)	1997	Spandex knitting, dyeing, finishing and sales.
	Shanghai Shentang Teng Automobile Machinery	Itochu Corp (20%), Itochu China (10%), SunChemical (40%), Shanghai Car Carpet Plant Co., Ltd (30%)	1997	Nonwoven interior and carpet manufacturing
	Guangzhou Shouteng Automobile Interior Parts Co.,Ltd.	Itochu Corrp (40%), Kotobukiya Fronte Co.,Ltd. (60%)	2004	Automotive Interior Carpet
Apparel	Tianjin Huadao Clothing	Itochu Corp (82.3%), Itochu China (9.6%), Ina Hosei (1.9%), Araki Hosei (1.9%), Unico (4.33%)	1993	Uniforms
	Qingdao Tri-Gents Clothing Co,.Ltd	Itochu Corp (60%), Japanese enterprises (40%), Qingdao Xizhuang Chang (20%)	2003	High-end Men's Suits
	Qingdao Royne Knitting Co.,Ltd	Itochu Corp (45%), Qingdao JIFA Group Co., Ltd. (55%)	1993	Knit wear
	Qingdao TengHua Apparel Co., Ltd.	Itochu Corp (38%), Kondobo (62%)	1997	Innerwear, Sportswear
	Dalian Yawn Underwear Co Ltd.	Itochu Corp (25%), Itochu (China) (3%), Chinese enterprise (72%)	2003	Ladies' Innerwear
	Ningbo Shengzhou Knitting Co., Ltd.	n/a	n/a	Knitting
Wholesale Retail	Renoma (Ningbo) Apparel Co., Ltd.	Itochu Corp (25%), Itochu Textile (China) (14%), Ningbo Shanshan Co., Ltd (61%)	2004	Production, wholesale and retail of 'Renoma' brands
	Ningbo Lecoq Garments Co., Ltd.	Itochu Textile Prominent (Asia) Ltd (10%), Ningbo Shanshan Co., Ltd, Shanshan Brand Management Co., Ltd (30%), Descente Ltd. (40%)	2004	Production, wholesale and retail of sportswear
	Shanghai Sanqianyuan Fashion Co., Ltd	Itochu Textile (Shanghai) (40%), local enterprises (60%)	2003	Men's suits
	Shanghai Encheng Fashionable Dress Limited Corp	Itochu Corp (25%), Onyone (30%), Shanghai Garment Import & Export Co.,Ltd.(25%), Shanghai Nicheng Fashion (20%)	1993	Sports wear
Inspection	Shanghai Baoteng Clothing And Accessories Zhengli Limited Company	Itochu Corp (50%), CI Textile Service (40%), Shanghai Lansheng Logistics Limited Company (10%)	2004	Inspection of apparel products and inspection
Logistics	Shanghai IFS Testing Service Co.,Ltd.	Itochu Corp (25%), Onyone (30.0%), Shanghai Garment Import & Export Co.,Ltd. (25%), Shanghai Nicheng Fashion (20%)	2004	Quality control, testing and inspection of textiles
Services	Aifusi (Shanghai) Enterprise Planning Consultancy Co.,Ltd.	Itochu ModePal Co Ltd. (100%)	2007	Retail consulting

Note. Compiled by author based on IR report (ITOCHU), and MRI data base.

CHAPTER 4
GOVERNING UNDER HIGH UNCERTAINTY: THE STRATEGIC ROLE OF SŌGŌ SHŌSHA IN EARLY GVC FORMATION

Abstract

This study examines the role of Japan's sōgō shōsha in multinational enterprise (MNE)–led global value chains (GVCs). Using Transaction Cost Economics (TCE) and a history-informed abductive research approach, it conducts a comparative case analysis of DuPont and Fast Retailing, both of which entered China in the early 1990s—a period of deep political and policy uncertainty—through partnerships with Mitsubishi, a leading sōgō shōsha. The study advances TCE-informed entry mode research and GVC governance scholarship in two main ways. First, we advance understanding of entry into highly volatile transition economies by developing four propositions on the entry process and by elaborating a causal–temporal diagram of governance sequencing. Second, we contribute to the structural–relational mechanisms debate in GVC governance by identifying a proto-governance mechanism, facilitated by a non-lead MNE, that operates before formal governance structures crystallize and relational mechanisms fully take hold.

4.1. INTRODUCTION

The objective of this paper is to examine the strategic roles of Japan's sōgō shōsha (general trading companies) within MNE-led global value chains (GVCs), and to analyze their governance decisions under institutionally volatile conditions. Recent geopolitical tensions and global disruptions have renewed interest in how firms organize governance and sustain resilience in GVCs under deep uncertainty (Kano & Oh, 2020; Kano et al., 2022; Ryan et al., 2022).

The dominant response in the literature has been to revisit location, ownership, and control strategies in GVCs (Kano et al., 2022). Structural mechanisms, however, capture only one side of governance. A large body of work highlights that relational governance—trust, reputation, interpersonal networks, and historical ties—is instrumental in governing complex, cross-border interdependencies (Dyer et al., 2018; Kano, 2018; Strange & Humphrey, 2019; Lopes et al., 2019), and enhancing GVCs' long-term resilience (Kano et al., 2022). Parallel debates ask whether structural and relational governance act as substitutes or complements (Poppo & Zenger, 2002; Vandaele et al., 2007; Poppo et al., 2016; Benito et al., 2019). The substitution view suggests that strong structural control reduces the marginal value of additional relational safeguards (and vice versa) (Dyer & Singh, 1998). The complementary view instead sees relational mechanisms as embedded within and enabled by structural forms (Benito et al., 2019): well-specified formal contracts, including punishment clauses, provide a stable frame for trust and open-ended cooperation, facilitate information sharing, and reduce monitoring costs (Lazzarini et al., 2008; Poppo & Zenger, 2002).

Both views, however, share implicit assumptions that limit their applicability to today's geopolitical environment. First, they typically assume environments in which uncertainty is moderate and contracts are therefore both writeable and enforceable. Second, they focus almost exclusively on dyadic buyer–supplier relationships (e.g., Poppo & Zenger,

2002; Vandaele et al., 2007; Poppo et al., 2016), leaving underexplored how third parties influence the design and functioning of structural and relational governance mechanisms.

Under deep uncertainty, contemporary MNEs must organize GVCs shaped by multi-actor constellations in which structural mechanisms are costly and incomplete because future contingencies cannot be fully anticipated, and relational mechanisms are fragile, difficult to engineer across borders, or not yet established. GVC governance research often emphasizes the lead MNE's capabilities to orchestrate activities across locations through structural and relational mechanisms. Yet this work often overlooks knowledge supplied by non-lead MNEs such as sōgō shōsha.

Despite their longstanding importance in the global economy (Jones, 1998, 2005; Jones & Khanna, 2006), sōgō shōsha remain theoretically underexamined in governance research. This oversight is partly due to their inherently "invisible" nature (Yoshino & Lifson, 1986): they frequently operate behind the scenes to support client MNEs (Shimada, 1990; *Toyo Keizai*, 2016), often through minority equity positions (Hennart & Kryda, 1998), making their activities difficult to detect in conventional datasets[23].

To address these interrelated gaps, this study examines and compares two governance arrangements—DuPont–Mitsubishi and Fast Retailing–Mitsubishi. Both involve early entry into China in the early 1990s, under institutionally volatile conditions in which sōgō shōsha possessed longstanding political and relational ties. DuPont represents a mature, producer-driven chemical MNE with substantial global experience but limited familiarity with China's institutional environment. Fast Retailing (FR), by contrast, was an emerging retailer MNE in a buyer-driven chain with limited international experience when it began constructing its China-centered GVC.

[23] For example, Directory of Japanese Companies Abroad (TK data) does not capture firms with ownership stakes below 20 percent, nor does it include data on investments made through foreign subsidiary to a local entity or a third-country.

We analyze these two cases using a history-informed abductive approach, iteratively confronting theory with historical evidence and refining theoretical assumptions as analytical patterns emerge (Welch et al., 2011). We employ Transaction Cost Economics (TCE)'s contracting schema (Williamson, 1996; 2008) as our initial framework for two reasons. First, existing GVC frameworks are predominantly lead-MNE centric (Hennart, 2009). TCE, by contrast, explicitly emphasizes inter-firm complementarities. Second, TCE incorporates relational mechanisms in the form of credible commitments (Williamson, 1996), thereby providing a unified lens for analyzing the interaction between structural safeguards and relational governance.

TCE has been criticized for its relative simplicity and its focus on dyadic buyer–supplier relationships that treat the single transaction as the basic unit of analysis. We respond to this critique by taking a sōgō shōsha-coordinated GVC which is defined as a bundle of interdependent transactions, as our unit of analysis, retaining the lead MNE–sōgō shōsha dyad as the analytical building block but situating it within a broader multi-actor constellation.

Accordingly, this paper asks:

How, when, and in what sequence do structural and relational governance mechanisms interact between the lead MNE and non-lead MNEs such as sōgō shōsha in politically volatile county?

Our core argument is fourfold. First, lead MNEs are more likely to temporarily externalize orchestration functions to a non-lead MNE that possesses superior host-country institutional knowledge. Second, if a non-lead MNE (e.g., a sōgō shōsha) perceives substantial long-run strategic value in a project, it is likely to deploy early, unilateral, transaction-specific commitments prior to the formation of formal governance structures.

These commitments are activated under three necessary conditions: where asset specificity is prohibitively high; strong safeguards are thus required; and lead MNE have limited host country institutional knowledge. Third, in multi-actor governance structures, credible commitments may be deployed even within formal governance arrangements such as joint ventures when formal safeguards alone are insufficient to stabilize transactions under double hazard conditions. Forth, as uncertainty declines and host-country institutional knowledge accumulates at the lead MNE, the embedded governance role of the non-lead MNE becomes less necessary and governance evolves toward more conventional forms.

The paper contributes to entry mode research and GVC governance studies in two main ways. First, we advance understanding of entry into highly volatile transition economies by developing four propositions on the entry process and by elaborating a causal–temporal diagram of governance sequencing. Second, we contribute to the structural–relational mechanisms debate by identifying a proto-governance mechanism —one facilitated by a non-lead MNE— that operates before formal governance structures crystallize and relational mechanisms fully take hold.

The remainder of the paper is structured as follows. Section 4.2 reviews prior research of TCE-informed entry mode research under political risk, and structural and relational governance mechanism, and GVC governance studies, and situates sōgō shōsha within this landscape. Section 4.3 outlines the methodology, unit of analysis, case selection, and case analysis. Section 4.4 introduces the analytical framework (initial theory). Sections 4.5 and 4.6 present the Fast Retailing–Mitsubishi and DuPont–Mitsubishi cases and the cross-case discussion that yields four propositions. Section 4.7 elaborates the theoretical implications, and Section 4.8 concludes with directions for future research.

4.2. Literature Review and Theoretical Background

4.2.1. Typology of Governance Relationships

To situate this paper within the broader governance literature, Table 4-1 presents a typology of four dyadic governance configurations, distinguished by whether the lead MNE and its counterpart are sōgō shōsha or non–sōgō shōsha. These dyads serve as basic building blocks for understanding how transactions are organized among GVC participants.

Table 4-1

Typology of governance relationships

	NON-LEAD MNE: NON–SŌGŌ SHŌSHA	NON-LEAD MNE: SŌGŌ SHŌSHA
LEAD MNE: NON–SŌGŌ SHŌSHA	Q1 Dominant studies (e.g., TCE-informed entry mode research; GVC governance)	**Q2 Focus of this study**
LEAD MNE: SŌGŌ SHŌSHA	Q3 GVC upgrading strategy; role transformation among peripheral firms	Q4 intra-firm transactions (parent–subsidiary) or inter-firm transactions between two sōgō shōsha

Note. Prepared by author.

Q1 represents the dominant configuration in existing governance research, comprising transactions between two non–sōgō shōsha firms. This category encompasses two major streams: TCE-informed entry mode research, and GVC governance studies, including work on structural vs relational mechanisms.

Q3 captures a more recent trend in which sōgō shōsha themselves act as lead MNEs—for example, ITOCHU's expansion into global brand ownership. These developments may connect to debates on supplier upgrading and role transformation among peripheral firms (Sturgeon & Kawakami, 2011; Lee & Gereffi, 2015; Sako & Zylberberg, 2019; Lechner et

al., 2020). However, they remain a recent trend in the sōgō shōsha's context and are treated as a promising avenue for future research rather than a core focus here. Q4 pertains to intra-organizational transactions within groups (e.g., parent–subsidiary) and the rare inter-firm transactions between two distinct sōgō shōsha; these also fall outside our analytical scope.

Within this matrix, we focus on Q2: governance relationships between a lead MNE and sōgō shōsha, embedded within a broader, multi-actor GVC constellations. More specifically, we examine this configuration under three boundary conditions: time – the early 1990s; location –China as a transition economy; and context – institutionally volatile settings characterized by high political and regulatory uncertainty. The literature reviewed below is therefore selectively mobilized to illuminate governance under these conditions, rather than to provide a comprehensive overview of all entry mode research and GVC research.

4.2.2. TCE-informed Entry Mode Research (Q1-a)

TCE has long served as a foundational framework for analyzing governance decisions at the transactional level across a wide range of organizational contexts (Hennart & Verbeke, 2022). Within international business (IB), its operationalization—pioneered by Anderson and Gatignon (1986)—established a systematic basis for entry mode research (Gatignon & Gatignon, 2010). From this broad stream, our interest is confined to studies that explicitly address entry into politically risky or institutionally underdeveloped environments.

Early TCE-based entry-mode research treats political risk as a key dimension of environmental uncertainty that shapes the choice between contractual and equity modes. Anderson and Gatignon (1986, p. 14) frame governance choice as a function of control vs. resource commitment; high external uncertainty per se does not always call for high control, but high asset specificity under uncertainty typically favors hierarchical modes. Hill et al. (1990, p. 122) explicitly incorporates political risk into mode choice, arguing that high

political risk often pushes firms toward joint ventures (JVs) or low-commitment modes to hedge against expropriation and policy shifts. In the original TCE formulation, these JVs are framed as transitional solutions that often facilitate an entry into foreign markets (Williamson, 1996)—less efficient than full ownership but preferable in certain contexts. Many other studies support the utility of JVs in politically unstable or institutionally underdeveloped markets, where local partners help mitigate transaction costs, reduce political risks, and align interests with other local stakeholders (Hennart & Park, 1993; Henisz & Williamson, 1999; Meyer, 2001; Brouthers & Hennart, 2007). Henisz (2000) operationalizes political constraints and shows that as political hazards increase, foreign investors face an increasing threat of opportunistic expropriation by governments. He also investigated hazard at transactional level, not only political hazards as country-specific effect, pointing to the possibility that these intra- and inter-firm hazards may be exacerbated by the polity hazard. In this stream, political risk is largely modelled as an exogenous country-level hazard raising the cost of irreversible commitments; entry modes, JVs in particular, are chosen to minimize expected transaction and expropriation costs.

Meyer (2001) and Delios and Henisz (2003) highlight how institutional voids and regulatory risk shape entry strategies in transition economies; JVs with state-owned or politically connected partners can function as political-risk–sharing devices. Here, political risk is not just "noise" but strategically managed through ownership structure and partner choice. Equity sharing is seen as a structural safeguard against state-level opportunism.

Later work adds firm-level capabilities and experience as moderators of the political-risk–mode relationship. Zhao et al. (2004) show that firms with more international experience are more likely to choose wholly owned subsidiaries (WOS), even under political risk, because they can better manage complex operations and hazards. Lee et al. (2020) distinguishes general international experience from host-country institutional knowledge.

Institutional familiarity—often possessed by local partners or intermediaries—can reduce perceived political risk and enable higher-commitment modes. Brouthers and Hennart (2007) reviews the entry mode literature and note that political risk effects are also contingent on industry (service vs. manufacturing), and asset specificity.

4.2.3. GVC Governance Studies (Q1-b)

Two broad governance mechanisms dominate the GVC literature. Structural governance emphasizes formal mechanisms: "the ownership, control, and location of GVC activities (i.e., the what, where, and who decisions)" (Kano et al., 2022, p. 25). Relational governance emphasizes managerial mechanisms that reduce hazards by building interpersonal relational norms, goodwill, trust, reputation (Kano, 2018), elite networks (Lopes et al., 2019), or social capital shared among family firms (Debellis et al., 2024). The central debate concerns whether these mechanisms substitute for one another or complement each other in governing transactions under uncertainty. Some scholars argue that relational governance substitutes for structural safeguards: trust reduces the need for formal contracting (Dyer & Singh, 1998). Subsequent studies find formal contracts and relational governance co-evolve, forming complements rather than substitutes (Poppo & Zenger, 2002; Lazzarini et al., 2004; Hoetker & Mellewigt, 2009; Li et al., 2010; Poppo et al., 2016). For clarity, table 4-2 summarizes these main perspectives.

We narrow our focus to contributions that speak to structural–relational interactions under conditions of institutional volatility, rather than stable, low-risk environments. Modern internalization theory within the GVC governance literature extends TCE (Williamson, 1993, 1996) that explicitly focused on safeguards against opportunism. Verbeke and Greidanus (2009) introduce the notion of bounded reliability, arguing that hazards arise not only from opportunism but from incomplete reliability in fulfilling open-ended commitments. This

literature maintains that relational governance mechanism to mitigate this kind of human fallacy is treated as embedded within formal structures, not outside them: "relational governance is a more fine-grained mechanism within a broader structural governance architecture" (Verbeke & Fariborzi, 2019; Kano et al., 2020, 2022). Thus, trust does not replace structure (Kano & Oh, 2020); it operates within and evolves inside structural frames.

In line with the emerging consensus (e.g., Poppo et al., 2014), this paper adopts the position that structural and relational mechanisms are fundamentally complementary rather than substitutive, especially in volatile institutional environments.

Table 4-2

Structural vs relational governance: key perspectives

Perspective	Structural governance	Relational governance / trust
Core idea	Formal, codified safeguards: contracts, equity, monitoring, incentives, authority	Informal, socially embedded mechanisms: trust, reputation, social capital, norms
Williamson (1993, 1996)	Focus on safeguards against opportunism; governance modes economize on transaction costs given bounded rationality and opportunism	Skeptical about "trust" as an analytic construct in commercial exchange; "true" trust reserved for special relations
Modern TCE / new internalization theory	Governance problems stem from bounded rationality and bounded reliability; structural safeguards are necessary but incomplete and costly (Verbeke & Greidanus, 2009; Kano & Verbeke, 2015)	Trust and bounded reliability shape responses to uncertainty; trust may lower perceived uncertainty but is fragile and context-specific (Kano & Oh, 2020); relational mechanisms are fine-grained tools within broader structures (Verbeke & Fariborzi, 2019; Kano et al., 2020, 2022).
Complementarity view	Contracts and structural devices create a stable frame enabling relational governance (Lazzarini, et al., 2004; Hoetker & Mellewigt, 2009; Li et al., 2010)	Trust deepens information sharing, enables more complete contracting ex ante, and lowers monitoring costs ex post (Poppo & Zenger, 2002; Poppo et al., 2016; Benito et al., 2019)
Substitution view	Strong structural control may reduce the marginal value of additional relational safeguards; in extreme cases, heavy formalization can crowd out relational norms (Dyer & Singh, 1998)	High relational embeddedness may partially substitute for costly control, particularly in long-term or clustered exchanges (Dyer & Chu, 2003; Benito et al., 2019)

Note. Compiled by author.

4.2.4. What is Missing?

The foregoing review highlights several gaps that motivate this study. First, TCE-informed entry mode research and GVC governance studies remain only partially integrated, partly due to differences in unit of analysis (Benito et al., 2009). In entry mode research, the analytical unit is the firm-level transaction, whereas in GVC governance studies it is the network or chain level.

Second, both substitution and complementarity views have paid limited attention to the joint effects of country-level political and institutional risks and transaction-level hazards. We know little about how governance mechanisms work when formal safeguards are costly or incomplete, and when relational mechanisms are difficult to activate because behavioral uncertainties are high. We also know relatively little about how firms with limited institutional knowledge design integrated structural–relational strategies in such high-risk environments.

Third, contemporary GVC literature incorporates TCE and discusses structural and relational mechanisms under high uncertainty (Kano et al., 2022), implicitly assuming that the primary orchestration capabilities reside with lead MNEs. We hence know little about how orchestration capabilities are assembled, shared or internalized within multi-actor GVCs under highly risky environments.

In sum, prior research rarely considers how structural and relational mechanisms are configured among multiple actors, particularly under deep political and institutional uncertainty. We therefore focus on 1990s China as a critical empirical setting in which political hazards, institutional voids, and bounded reliability were pronounced, and in which lead MNEs lacked host-country institutional knowledge. This constitutes the core gap—and

the boundary conditions—that this paper address. To address these gaps, we focus on Japan's sōgō shōsha and, in particular, Mitsubishi's role in the early formation of China-centered GVCs.

4.2.5. Sōgō Shōsha in GVCs and the Value of a History-Informed Lens (Q2)

Japan's sōgō shōsha provide a particularly compelling context for addressing these gaps. Many trace their origins to the late nineteenth century and have persisted as large, diversified enterprises. Historically, they played a pivotal role in connecting Japan to the international economy (Jones, 1998; 2005), coordinating industrial development across sectors and geographies, and supporting both the overseas expansion of Japanese manufacturers and the entry of foreign firms into Japan (Yamazaki, 1987; Yonekawa & Yoshihara, 1987; Yonekawa, 1990; Shimada, 1990; Kawabe, 1990; Tanaka, 2012a; Tanaka, 2012b). Recognized as core components of business groups (kigyō shūdan), many studies attributed their competitiveness to within-group transactions. Sōgō shōsha have traditionally relied on long-term contracts and equity-based JVs to align incentives between Japanese firms and local partners, mitigate hazards, and address information asymmetries (Delios & Henisz, 2003; Hennart & Kryda, 1998). Unlike their Hong Kong or Taiwanese counterparts—where trading functions are dispersed across numerous independent firms—sōgō shōsha bundle trading, financing, logistics, and information services within a single organization (Ellis, 2001; Dunning & Lundan, 2008). Their privileged access to both intermediate and final markets, combined with their ability to coordinate complementary functions, underpins a distinctive set of ownership advantages (Dunning & Lundan, 2008, p. 779).

However, as Okumura (1993) emphasizes, much of their true strength lies in external transactions with non-group firms. It has been well recognized that they leveraged an

international reputation as trust-worthy partners (Buckley, 1985; Jones, 1998; Dunning & Lundan, 2008). Yet the mechanisms through which sōgō shōsha build and sustain these relationships with non-group partners—especially in institutionally volatile environments—remain underexplored.

Recent work in business history advocates moving beyond purely descriptive narratives to uncover the causal mechanisms linking historical trajectories to contemporary organizational phenomena (Decker et al., 2015; Lubinski, 2018; Sakai & Izawa, 2022; Donzé & Uemura, 2025). Sakai and Izawa (2022) in particular call for management research in Japan that traces chains of events and situational contingencies shaping managerial and organizational decisions, rather than treating historical time as a static backdrop. This perspective underscores the analytical value of history-informed case studies—approaches that situate firm behavior within specific temporal, institutional, and industrial contexts in order to explain how strategic and governance outcomes emerge (Rowlinson et al., 2014; Kipping & Üsdiken, 2014).

Following this call, the present paper employs a historical analysis within an abductive approach to examine Mitsubishi's strategic roles in the early formation of GVCs in China during the 1990s. It focuses on how structural and relational governance mechanisms were constructed, sequenced, and adapted under deep political uncertainty, drawing on interviews with former executives and triangulating these with corporate materials and news articles. Sōgō shōsha thus offer a theoretically rich context for examining how structural and relational mechanisms interact in multi-actor GVCs under institutional volatility—precisely research fields under which existing TCE-based and GVC-based studies remain under-specified.

4.3. METHODOLOGY

This study adopts an abductive, history-informed research approach (Bhaskar, 1979; Welch et al., 2011; Fletcher, 2017) to uncover how structural and relational mechanisms emerge. This approach is appropriate when the phenomenon under investigation is context-dependent and an early stage of the development (Welch et al., 2011; Reuber & Fischer, 2022). Rather than testing a pre-specified model, abduction proceeds through iterative confrontation between theory and empirical materials, enabling the identification of underlying causal mechanisms triggered by multiple forces, such as environmental uncertainty and behavioral uncertainty (bounded rationality and bounded reliability). This approach enables us to theorize how governance portfolios are sequenced over time and how structural safeguards and relational mechanisms interact in politically volatile settings. This theory-guided analysis allows us to derive generalizable insights and develop propositions applicable to broader settings (Rihoux & Lobe, 2009; Ragin, 2014).

4.3.1. Unit of Analysis

The unit of analysis is the sōgō shōsha-coordinated GVC, a bundle of interdependent transactions. We retain the lead MNE–sōgō shōsha dyad (the transaction) as the analytical building block but situate it within a broader multi-actor constellation. This unit of analysis enables us to: preserve the micro-analytic rigor of TCE; and examine how structural safeguards and relational mechanisms are combined and sequenced across multiple actors.

4.3.2. Case Selection

The two focal cases—DuPont–Mitsubishi and Fast Retailing–Mitsubishi—were selected based on their ability to illuminate the mechanisms of interest (Pettigrew, 1990). Both cases share a common empirical context: entry into China in the early 1990s, a period

characterized by profound political and policy uncertainty and institutionally thin markets. In both cases, Mitsubishi coordinated early governance arrangements, allowing for controlled comparison. Despite these shared contextual boundaries, the cases differ along two theoretically meaningful dimensions:

1. Chain type (Gereffi, 1994, 2014): DuPont operates a producer-driven value chain in chemicals and polyester, while FR operates a buyer-driven apparel GVC under fast-fashion logics.
2. Organizational maturity: DuPont represents a mature, globally embedded MNE with formalized routines and deep international experience (Chandler, 2005), while FR was a nascent MNE at the time of entry, lacking established orchestration capabilities.

These differences enable polar-type comparison (Pettigrew, 1990): the mechanism of temporary externalization of orchestration can be examined under contrasting industry logics and firm-level capabilities, strengthening the analytical power of the comparative design. Among the seven sōgō shōsha, Mitsubishi was selected because: its China portfolio in the 1990s was the most diversified among peers and exhibited the highest average investment per project, based on data from the 21st Century China Research Institute (1,651 firms; 2,879 entries); and it spans both heavy industry (DuPont case) and fashion (FR case), allowing observation of governance mechanisms across distinct transaction attributes.

4.3.3. Data Analysis

The analysis proceeded in four iterative steps. First, we began with an initial theoretical framing informed by TCE, and in particular Williamson's (1996, 2008) contracting schema. This provided a starting lens for interpreting governance choices in terms of structural safeguards and relational mechanisms. Second, as empirical evidence

accumulated, this initial framing was progressively refined to accommodate multi-actor governance structures and to identify the sequencing of structural and relational mechanisms. The core data set consisted of news articles, *Nikkei, Nikkei Sangyō Shimbun, Nikkei MJ*, and *Senken Shimbun*; interview material: interviews with a former Director of Mitsubishi Corporation (China), conducted on 6 February 2023 (16:00–21:00), 7 May 2023 (15:00–16:00), and 3 September 2024 (12:00–14:00), supplemented by internal information provided by a former manager in Mitsubishi's textile division in China. These interviews were focused on strategic logic, decision-making mechanisms, and the temporal unfolding of governance responses. Third, we revisited and adjusted the initial framework in light of emerging empirical patterns. This involved comparing across cases to identify similarities and differences in governance responses and moving back and forth between micro-level transaction dynamics and country-level institutional and political risks in order to develop a mechanism-based explanation. Finally, we applied the revised framework to re-analyze the case studies and additional data. In particular, we examined press articles to identify previously overlooked instances of managerial responses. To reinforce internal validity, we triangulated among three types of sources: secondary materials, corporate records capturing formal mechanisms, and interview insights revealing informal logics and decision rationales.

4.4. Analytical Framework: Initial Theory

4.4.1. Classical TCE and the Contracting Schema

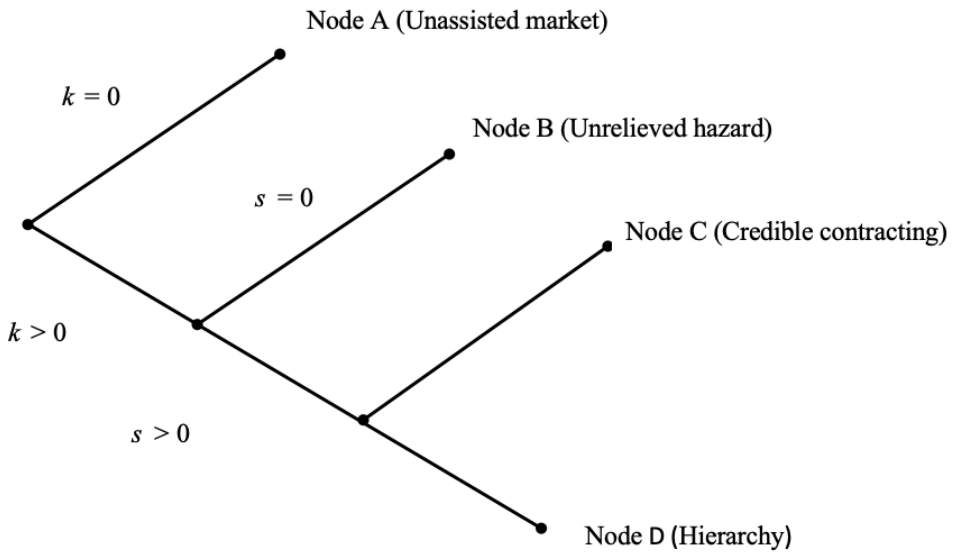
Our starting point is TCE, which explains governance choice as the discriminating alignment of transactions with governance structures that economize on transaction costs under bounded rationality and bounded reliability (Williamson, 1996; Verbeke & Greidanus, 2009). In classical TCE, the unit of analysis is a single transaction between a buyer and a

seller, characterized by two core attributes: asset specificity (k) and uncertainty, which interacts with behavioral assumptions.

Williamson's (1996, 2008) contracting schema classifies governance into four canonical nodes according to asset specificity (k) and the presence of safeguards (s) as illustrated in Figure 4-1:

Figure 4-1

Simple contracting schema



Note. Adopted from Williamson (1996, 2008), illustration by author.

(1) Node A ($k = 0, s = 0$): Market governance

Transactions involve general-purpose assets and require no specialized safeguards. Anonymous market contracting is efficient.

(2) Node B ($k > 0, s = 0$): Governance failure

Transactions entail specific assets but lack safeguards, leaving parties exposed to opportunism and maladaptation. This configuration is unstable.

(3) Node C ($k > 0, s > 0$): Hybrids (credible) contracting

When asset specificity is positive but moderate, hybrids (e.g., long-term contracts, franchising, subcontracting) are efficient. This mode is often supported by credible commitments Credible commitments are reciprocal, often irreversible investments designed to safeguard the relationship ex ante.

(4) Node D ($k \gg 0, s > 0$): Hierarchy

When asset specificity is high and uncertainty is substantial, unified ownership (e.g., wholly owned subsidiaries) is predicted to dominate, as hierarchical authority facilitates adaptive coordination and safeguards vulnerable investments. Although the original schema does not include JVs, we map them on the way to this Node D, based on the TCE interpretation of JVs as "temporary *organizational* forms" (Williamson, 1996, p. 118, italicized by author).

This conceptualization has been widely applied in entry mode research (Brouthers, & Hennart, 2007; Cuypers et al., 2021), where governance is typically conceptualized as a choice among market, hybrid, or hierarchy for a focal transaction in a dyadic relationship. It provides our initial theoretical lens for interpreting governance choices in the DuPont–Mitsubishi and Fast Retailing–Mitsubishi cases. Building on this foundation, we integrate insights from the relational–structural governance literature.

4.4.2. Toward a Conceptualization of Credible Commitment

While powerful, the classical contracting schema is insufficient for analyzing governance in sōgō shōsha–coordinated GVCs under deep political uncertainty, as highlighted in the preceding literature review. Classical TCE (Williamson, 1996, 2008) elaborates relational mechanism, highlighting credible commitments as supporting

mechanisms for hybrids (or credible contracting at Node D) but contemporary debates as to how structural–relational mechanisms in GVC remains weakly connected to this TCE notion. Williamson argues that vulnerable hybrids can be supplemented by credible commitments—specialized, often irreversible investments that signal durability and help stabilize relationships. Yet empirical studies of credible commitments remain scarce (Cuypers et al., 2021; Hennart & Verbeke, 2022).

We hence treat this original TCE (contracting schema) as a necessary but incomplete initial theory. We retain its core logic of discriminating alignment and the k–s framework, but operationalize it along temporal sequencing of structural–relational mechanisms.

4.5. FINDINGS

The objective of the following case studies is not to validate a predetermined theory, but to infer mechanisms and sequencing logic from historically situated decision processes. We treat Williamson's contracting schema as a diagnostic lens that links specific transaction hazards to governance responses, and that highlights when and in what order structural and relational mechanisms emerge under deep uncertainty. Analytically, we trace: (1) the hazard (origin, type, intensity); (2) initial governance response (structural vs. relational); (3) structural complement (equity, JV design); (4) sequencing logic (why that order), and (5) boundary conditions.

The empirical analysis focuses on two cases: FR–Mitsubishi and DuPont-Mitsubishi. These cases are situated within the context of China's economic liberalization following its official transition to a socialist market economy in 1992. While this transition opened significant opportunities for foreign direct investment, it also generated high levels of institutional and environmental volatility. As Montinola et al. (1996) notes, although economic reforms in China were aggressively pursued, institutional reforms lagged behind:

As many pointed out, China at the time lacked critical market-supporting institutions, including robust protection for intellectual property rights, a transparent legal framework for commercial transactions, and an independent judiciary (Montinola et al., 1996; Schotter & Teagarden, 2014). These institutional voids in China heightened the risk of expropriation, arbitrary policy reversals, and opaque regulatory interventions—particularly for foreign firms undertaking transaction-specific investments (Williamson, 1996). The two cases illustrate how the lead MNEs and Mitsubishi addressed the hazards associated with early-stage GVC formation and how their governance arrangements coevolved.

4.5.1. Fast Retailing–Mitsubishi

4.5.1.1. Focal firm and industry context

Fast Retailing Co., Ltd., the parent company of UNIQLO, is a Japanese fashion retailer that opened its first UNIQLO store in 1984. In 1987, it shifted to a specialty retailer of private-label apparel (SPA) model and gradually began outsourcing manufacturing to overseas factories in China and other low-cost locations. International retail expansion started later, with the first overseas store opened in the United Kingdom in 2001 (Fast Retailing, 2024).

During the 1990s, the global fast fashion industry underwent a major governance shift from Node D (vertical integration) to Node C (hybrid/credible contracting), driven by lean retailing, just-in-time inventory systems, and full-package outsourcing (see Figure 4-2). Agility—rapid response, short lead times, and reliable quality—became a critical strategic imperative (Mehrjoo & Pasek, 2016). Competing firms adopted different governance responses.

4.5.1.2. Initial governance challenge

FR's strategic intent was to combine low-cost sourcing with tight operational control over quality and delivery. However, this intent generated a structural tension. On the one hand, fast-fashion transactions are often viewed as relatively standardized and thus low in asset specificity. On the other, Fast Retailing's portfolio included technically sophisticated textile inputs—such as proprietary fibers developed with Toray—which raised asset specificity. At the same time, China's volatile institutional environment meant that contract enforcement and regulatory predictability were far from guaranteed.

In terms of the contracting schema, Fast Retailing faced asset specificity ($k \gg 0$, due to specialized inputs and brand-related risks) and strong safeguard requirements ($s \gg 0$ (given political and regulatory uncertainty). Classical TCE would predict a move toward hierarchy (Node D), yet the competitive logic of fast fashion made full integration—owning factories and logistics assets—too costly and inflexible. The firm needed a way to retain speed and cost efficiency while safeguarding transaction-specific assets in a high-risk environment.

4.5.1.3. Mitsubishi's role and credible commitments

Mitsubishi entered as a multi-functional actor and orchestrator of Fast Retailing's early GVC in China. In the early 1990s, Mitsubishi committed to building and managing FR's regional production, and logistics platform with China as the core manufacturing base[24]. A former Mitsubishi COO recalled:

"In this SPA initiative, we committed to taking full responsibility for two crucial activities for the retailer: product management and logistics. We mobilized a wide array of

[24] *Nikkei Shimbun*, April 5, 2001, ユニクロ商社を走らす[Uniqlo drives shōsha].

our resources to create and develop the value chain—from product planning and raw material procurement to manufacturing and logistics" (Mitsubishi, 2011, p. 136).

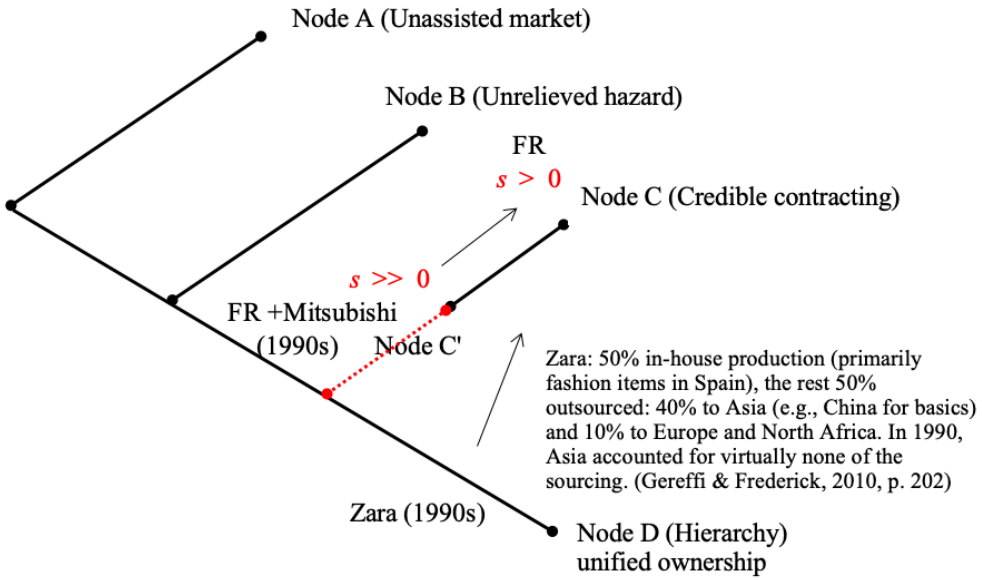
Mitsubishi deployed experienced personnel across China with deep local knowledge and cultural fluency to coordinate factory operations, troubleshoot bottlenecks, and ensure real-time adaptation. As one executive dispatched to China emphasized,

"*A sōgō shōsha's most valuable asset is its people… the key lies in leveraging our portfolio's entirety—across products, locations, and functions—by mobilizing our human assets.*"

Beyond coordination, Mitsubishi also provided financing. It extended credit to undercapitalized local factories that were critical to the uninterrupted flow of goods, effectively underwriting part of the production risk. These commitments in human capital and financing were undertaken before formal long-term contracts fully internalized these arrangements. In TCE terms, Mitsubishi was offering credible commitments ex ante, partially unilateral at first, to stabilize a high-hazard configuration.

Figure 4-2

FR's governance choice



Note. Adopted from Williamson (1996, 2008), illustration by author.

4.5.1.4. Sequencing of governance mechanisms

From a governance perspective, Fast Retailing's trajectory can be understood as a sequence from Node C′—Mitsubishi-embedded credible contracting—toward Node C, that is, direct credible contracting with specialized suppliers. Mitsubishi's role enabled this transition. Industry-wide, governance was moving from Node D (vertical integration, as exemplified by Zara) toward Node C. Fast Retailing was at the forefront of this transition but, because of its limited international experience and China's weak institutions, could not move directly to a pure Node C configuration.

Instead, Mitsubishi created an intermediate arrangement—what we conceptualize as Node C′: a sōgō shōsha–embedded hybrid in which orchestration of production and logistics was temporarily externalized to Mitsubishi. In this configuration, Fast Retailing retained strategic control over product design and branding, while Mitsubishi assumed responsibility

for coordinating multiple subcontractors, managing logistics, and financing key suppliers. Mitsubishi's deployment of specialized personnel and relationship-specific financing functioned as credible commitments that reduced both behavioral and environmental hazards.

As Fast Retailing accumulated host-country experience and strengthened internal capabilities, the need for Mitsubishi's intensive orchestration gradually declined. By the mid-2000s, governance evolved toward more conventional subcontracting relationships (a closer approximation to Node C), with Fast Retailing taking on more direct control over its supplier network while maintaining selected ties with Mitsubishi. Thus, the case illustrates how a non-lead MNE can temporarily substitute for the lead firm's orchestration capabilities, and how this role is gradually unwound as uncertainty diminishes and capabilities accumulate.

4.5.2. DuPont–Mitsubishi

4.5.2.1. Focal firm and industry context

DuPont, founded in 1802 as a gunpowder producer, had become a global chemical powerhouse by the late twentieth century (Chandler, 2005, p. 20). Its large production facilities generated substantial economies of scale, and diversification into adjacent industries created economies of scope. DuPont's international investment strategy has been characterized as cautious and calculated, especially where political risk and protection of proprietary technology are concerned (Casson & Lopes, 2013, p. 38)

In the early 1990s, Chinese local governments and state-owned enterprises (SOEs) faced strong pressure to upgrade upstream industrial infrastructure. While downstream manufacturing had expanded rapidly since the 1980s, upstream operations remained inefficient, constrained by outdated machinery, surplus labor, and volatile input costs (Tsuji, 2000). These conditions created latent demand for advanced chemical and fiber technologies but also posed considerable investment hazards. Foreign direct investment in these upstream

segments remained limited, partly due to weak intellectual property protection, inconsistent regulatory enforcement, and a fragile legal system.

4.5.2.2. Initial governance challenge

For DuPont, entry into China's polyester sector involved very high asset specificity ($k \gg 0$)—large, non-redeployable investments in the use of oil, plants and proprietary process technologies—and very high safeguard requirements ($s \gg 0$) due to political and regulatory risk. Legally, full foreign ownership was not permitted in this sector; standard TCE prescriptions favoring hierarchy (Node D) were therefore infeasible. At the same time, technology licensing without equity control exposed DuPont to severe risks of misappropriation and weak enforcement.

DuPont had several governance options corresponding to different nodes in the contracting schema: (1) License-based JV (Node C) – DuPont would license technology to a JV majority-owned by a Chinese partner, while Mitsubishi and its subsidiary Chemtex would hold minority equity stakes. (This firm was once established in 1993. DuPont granted exclusive rights in its proprietary technologies to the JV, without holding an equity position itself[25], yet the JV never became operational); and (2) 50:50 JVs – A structure successfully used in more stable markets such as Japan (1995), Taiwan (1997), and Turkey (1999)[26].combining DuPont technology with local partners' engineering and distribution capabilities (Karol et al., 2002).

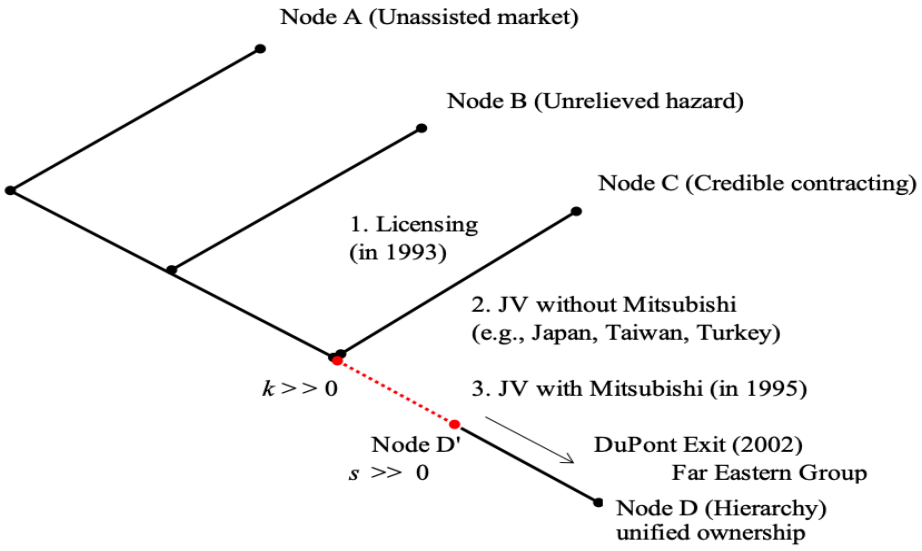
In China, however, both alternatives appeared insufficient.

[25] *Nikkei Shimbun*, August 27, 1993, 三菱商事、中国でポリエステル合弁 [Mitsubishi Corporation to establish polyester joint venture in China].

[26] *WWD*, June 5, 1995. DuPont enters joint venture with Teijin for Nylon in Japan; *WWD*, April 16, 1999, DuPont, Sabanci go 50-50 in foreign polyester venture; Karol et al. (2002).

Figure 4-3

DuPont's governance choice



Note. Adopted from Williamson (1996, 2008), illustration by author.

4.5.2.3. Mitsubishi's role and credible commitments

Mitsubishi's involvement began in 1991 with the acquisition of Chemtex, a U.S.-based engineering firm founded by former DuPont engineers and known for its ability to transfer advanced technologies safely to third parties. This acquisition served as a major credible commitment. It entailed substantial transaction-specific investment by Mitsubishi and signaled a long-term commitment to safeguarding DuPont's technological assets.

Organizationally, Chemtex created an additional structural layer between DuPont and local Chinese partners, and even between DuPont and Mitsubishi. Mitsubishi could oversee project execution and technology transfer through Chemtex, thereby reducing DuPont's direct exposure to potential misappropriation.

Beyond the technological interface, Mitsubishi assumed the critical role of government liaison and financial orchestrator. It brokered regulatory approvals at central and local levels and helped design a JV structure that granted DuPont a majority foreign

ownership stake—unprecedented in China's polyester sector at the time. To enhance legitimacy and impose governance discipline, Mitsubishi invited the International Finance Corporation (IFC), a member of the World Bank Group, into the ownership structure. IFC's presence brought international compliance standards and signaled regulatory reliability to all parties.

Mitsubishi also arranged a syndicated loan from fifteen international private banks, further embedding external oversight. These steps culminated in the establishment of a four-party JV in 1995 with the following equity shares: DuPont 35%, Mitsubishi 30%, Suzhou Chemical Fiber Co. 25%, and IFC 10%[27].

4.5.2.4 Sequencing of governance mechanisms

In terms of the contracting schema, DuPont's China project can be characterized as a move toward a modified hierarchical node, which we label Node D′. This configuration preserved DuPont's strategic influence over technology and key decisions while externalizing orchestration and part of the political-risk exposure to Mitsubishi and IFC. The sequence can be summarized as follows: (1) Ex ante credible commitment by Mitsubishi – Acquisition of Chemtex, prior to any final JV agreement, to signal commitment and provide a technical governance layer; (2) Design of a multi-actor JV structure – Inclusion of a local SOE (Suzhou Chemical Fiber), Mitsubishi as orchestrator and equity investor, and IFC as an international public authority; and (3) Allocation of ownership to manage "double hazards" – DuPont limited its equity stake to 35% to reduce exposure to political risk, while Mitsubishi and IFC together formed a 40% bloc (30% + 10%), which, combined with DuPont, created a majority coalition able to enforce governance and coordinate with the state.

[27] *Nikkei Shimbun*, October 21, 1995, 中国で化学繊維合弁 [Chemical fiber joint venture in China].

This architecture addressed what Henisz (2000) terms a double hazard: simultaneous exposure to firm-level behavioral uncertainty and state-level political risk. Majority ownership could have mitigated behavioral hazards but would have amplified political hazards; a purely minority position would have reduced political exposure but weakened DuPont's control. The Node-D′ solution balanced these trade-offs by embedding DuPont within a coalition of credible allies who shared risk and added monitoring and legitimizing functions.

Over time, as China's institutions evolved and DuPont's strategic priorities shifted toward more R&D-intensive activities, DuPont exited the JV. Mitsubishi facilitated the transfer of ownership to Taiwan's Far Eastern Group, initially retaining a minority stake (DuPont 10%, Mitsubishi 10%) to ensure an orderly transition before eventually divesting as well. Governance thus evolved toward a more conventional hierarchical structure (under Taiwanese owner), consistent with TCE original formulation (Williamson, 1985).

4.6. DISCUSSION

Despite operating under different value chain logics (buyer-driven vs. producer-driven) and different levels of organizational maturity (see Table 4-2), both cases exhibit a common governance logic under the same baseline conditions: high asset specificity ($k \gg 0$), strong safeguard requirements ($s \gg 0$), and limited host-country institutional knowledge (HCK) on the part of the lead MNE. The concrete manifestations of this logic differ, reflecting differences in industry characteristics and hazard types, but the underlying mechanism is shared.

Table 4-3

Cross-case comparison

Feature	Fast Retailing-Mitsubishi	DuPont-Mitsubishi
Industry logic (GVC)	Buyer-driven GVC	Producer-driven GVC
TCE node	Node C' to Node C (credible contracting)	Node D' to Node D (hierarchy)
Organizational maturity	Emerging MNE with limited international experience	Established MNE with global experience but limited local experience/institutional knowledge
Asset specificity	Fast fashion, tech-driven ($k \gg 0$)	Chemicals and fiber, high-tech ($k \gg 0$)
Requisite safeguards	$s \gg 0$	$s \gg 0$
GVC governance mechanism (Mitsubishi's credible commitment)	Mitsubishi-embedded subcontracting (specialized human/physical assets)	Mitsubishi-embedded quadripartite JV (Chemtex M&A and 30% equity stake)
Function of Mitsubishi	externalized production and logistics orchestration	externalized orchestration
Strategic logic for mode choice	reduce both production and transaction costs, while retaining control	manage "double hazards" at state and firm levels

Note. Compiled by author.

Four propositions summarize and extend the foregoing discussion. Consistent with the abductive approach adopted in this study, these propositions are not hypotheses derived a priori from TCE, but theoretically informed generalizations developed through iterative confrontation between Williamson's original contracting schema and the empirical patterns observed in cases. They formalize our extensions of TCE to multi-actor, temporally sequenced GVC governance under political and institutional volatility, and specify the boundary conditions under which these mechanisms are expected to operate. They are offered as conjectural statements that both synthesize the findings of this paper and provide a basis for further empirical examination.

4.6.1. Proposition 1: Temporary Externalization

The two cases reveal a common pattern under the same baseline conditions: high asset specificity ($k \gg 0$), strong safeguard requirements (s $\gg$ 0), and limited host-country institutional knowledge (HCK) on the part of the lead MNE. In both Fast Retailing–Mitsubishi and DuPont–Mitsubishi, conventional governance options—full internalization or direct reliance on local partners—would have implied either excessive risk or excessive cost.

In this context, Mitsubishi stepped in as an orchestrator, temporarily coordinating critical activities (e.g., production/logistics for Fast Retailing; JV structuring and political intermediation for DuPont), while the lead MNEs retained strategic control over their core assets and trajectories. This suggests that given baseline hazards and knowledge gaps, externalizing orchestration to a capable non-lead MNE becomes a comparatively efficient governance response. Hence, we advance:

Proposition 1. *Under baseline conditions ($k \gg 0$; $s \gg 0$; limited HCK), lead MNEs are more likely to temporarily externalize orchestration functions to a non-lead MNE that possesses superior host-country institutional knowledge.*

4.6.2. Proposition 2: Early Credible Commitments

In both cases, Mitsubishi assumed substantial transaction-specific investments at an early stage. Rather than waiting for fully specified contracts or mature relational trust, Mitsubishi moved first with unilateral, asset-specific commitments (e.g., the Chemtex acquisition in the DuPont case; specialized human assets in the FR case).

Importantly, these investments were undertaken prior to the full settlement of formal governance arrangements and without immediate contractual guarantees or reciprocal commitments from the lead MNEs. From a TCE perspective, they exemplify credible commitments: costly, irreversible investments designed to safeguard transactions and enhance reliability under high-risk conditions (Williamson, 1996, 2008). From a strategic

positioning perspective, they reflect Mitsubishi's forward-looking assessment of the long-run strategic value of securing central roles in FR's fast-fashion GVC and DuPont's polyester value chain in China.

Mitsubishi's own framing of this behavior underscores its dual logic. As one executive put it, "It's not that DuPont chose us as a partner. It is crucial to strategically position yourself (to be chosen)." This statement highlights that the initiative for these commitments lay with Mitsubishi itself; the company actively used early, transaction-specific investments both to economize on bounded reliability and to secure durable positions within evolving GVC architectures.

The pattern suggests a conditional mechanism: when *a sōgō shōsha* perceives high long-term strategic value under baseline hazards, it is more likely to undertake early, unilateral commitments. Thus, we develop:

Proposition 2. *Under baseline conditions, if a non-lead MNE (e.g., a sōgō shōsha) perceives substantial long-run strategic value in a project, it is likely to deploy early, unilateral, transaction-specific commitments prior to the formation of formal governance structures.*

4.6.3. Proposition 3: Credible Commitments Inside Formal Governance

The DuPont–Mitsubishi case further indicates that credible commitments do not end once a formal JV is established. Instead, they can be embedded within the formal structure itself: unusually high equity stakes (DuPont's case) under double hazard conditions.

When political and behavioral hazards interact, JV form plus "normal" equity stakes are not enough; additional credible commitments inside the formal structure are required to stabilize the transaction. (For example, Mitsubishi assumed a 30% equity stake within DuPont's JV—substantially higher than the range of 5–15% typically observed in similar arrangements). Such an extensive commitment suggests that, in institutionally fragile

environments, even structurally safeguarded governance forms may require further reinforcement. Hence, we advance:

Proposition 3. *In multi-actor governance structures, credible commitments may be deployed even within formal governance arrangements such as joint ventures when formal safeguards alone are insufficient to stabilize transactions under double hazard conditions.*

4.6.4. Proposition 4: Temporal Unwinding

Across both cases, Mitsubishi's embedded governance role is clearly temporary. Its orchestration and high-level commitments are concentrated in the early phases, when hazards and knowledge gaps are greatest. As political and institutional uncertainty declines and knowledge on host-country institutions accumulates at the lead MNE, governance shifts toward more conventional structures (e.g., direct subcontracting, single-firm hierarchy), and Mitsubishi's equity and coordination roles are scaled back or exited.

This pattern indicates a dynamic outcome consistent with conventional studies: once hazards fall and capabilities increase, the efficiency rationale for externalized orchestration weakens, and governance converges toward standard Node C or Node D forms.

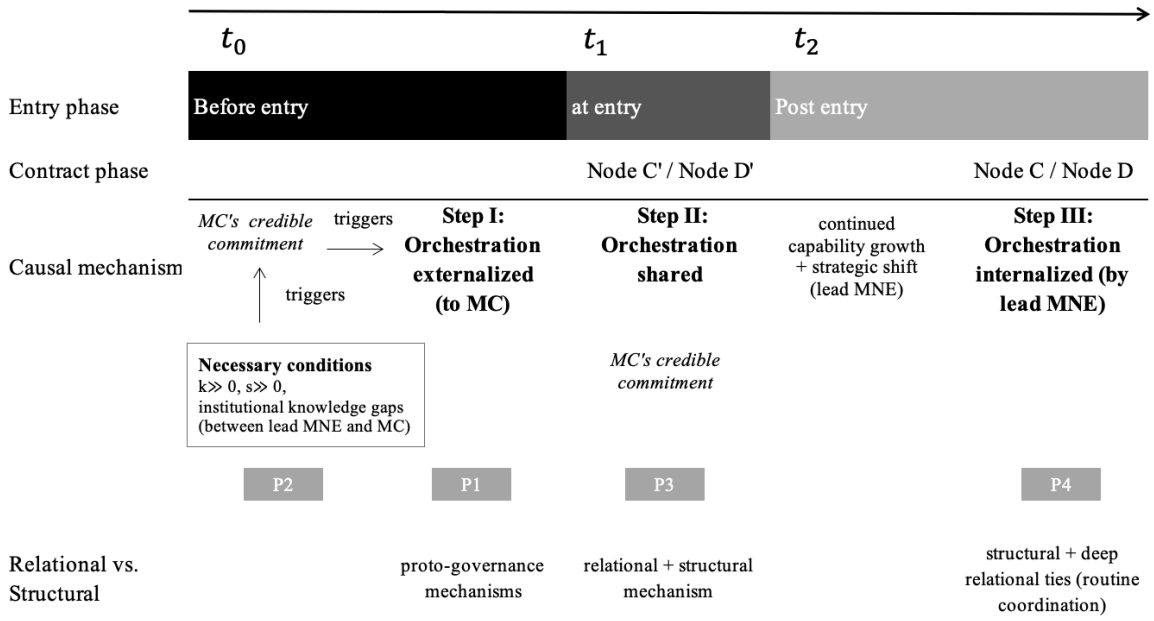
Proposition 4. *As uncertainty declines and host-country institutional knowledge accumulates at the lead MNE, the embedded governance role of the non-lead MNE becomes less necessary and governance evolves toward more conventional forms (Node C or Node D).*

4.6.5. Causal Diagram

Figure 4-4 synthesizes the argument developed above in the form of a causal–temporal diagram.

Figure 4-4

Causal–temporal diagram of governance sequencing



Note. Drafted by author. MC refers to Mitsubishi Corporation. P1–P4 correspond to Propositions 1–4 discussed above.

The horizontal axis represents the evolution of governance from the entry phase (t_0) through intermediate governance under Node C′ / Node D′ (t_1) to more conventional Node C / Node D arrangements (t_2). Along this axis, the figure distinguishes three steps in the orchestration of the GVC: Step I: Orchestration externalized to the sōgō shōsha (Mitsubishi), Step II: Orchestration shared, and Step III: Orchestration internalized by the lead MNE. The lower row ("Relational / Structural") indicates how the governance mechanisms change over time. At t_0, governance takes the form of credible commitments offered by non-lead MNE under deep uncertainty. Between t_0 and t_1, these arrangements manifest itself as proto-governance mechanisms that prepare the ground for more formal structures. At t_1, governance becomes relational + structural, as formal contracts (Node C′ / Node D′) are introduced but remain heavily supported by relational devices and/or credible commitments. By t_2,

governance shifts to structural modes with deep, routine relational ties (Node C or Node D), consistent with mature coordination and reduced hazards.

The central panel links this temporal evolution to the four propositions. The box at t_0 summarizes the necessary conditions under which our mechanism is activated: high asset specificity ($k \gg 0$), high safeguard requirements ($s \gg 0$), and a gap in host-country institutional knowledge between a lead MNE and non-lead MNE. Given these baseline conditions, the non-lead MNE (Mitsubishi) offers an early credible commitment (red text), such as transaction-specific investments, which triggers Step I, the temporary externalization of orchestration to Mitsubishi. This first step corresponds to Proposition 1 (externalization) and is causally enabled by Proposition 2 (early credible commitments).

At t_1 (Node C′ / Node D′), Step II is reached: orchestration is shared between the lead MNE and non-lead MNE. Here, in our case, Mitsubishi offered additional credible commitments inside the emerging structural arrangements (e.g., JV equity stakes), which stabilize transactions under double hazards conditions. This phase corresponds to Proposition 3, which extends credible commitments from classic hybrids into complex, multi-actor formal governance structures.

Finally, at t_2 (Node C / Node D), Step III occurs: orchestration is internalized by the lead MNE. Continued capability growth and strategic shifts at the lead MNE make the governance role by the third-party less necessary. Here, governance converges toward more conventional structures—direct subcontracting (Node C) or hierarchy (Node D)—and formal safeguards become sufficient and relational ties are routinized. This dynamic outcome is captured in Proposition 4, which describes the temporal unwinding of Mitsubishi's orchestration role as hazards decline and host-country knowledge accumulates. This move from t_1 to t_2 was consistent with Hennart & Kryda (1998)'s finding that sōgō shōsha often reduce their commitment or equity stakes over time as partners gain knowledge.

4.7. THEORETICAL IMPLICATIONS

The causal–temporal diagram (Figure 4-4) also re-interprets and extends existing theory. This diagram highlights mechanisms that become salient when political risk is prohibitively high and formal governance alone is insufficient. On this basis, it derives theoretical implications for three interrelated domains: TCE-informed entry mode research; the structural–relational governance debate; and GVC governance and orchestration under political and institutional volatility.

4.7.1. Entry Mode Research

Studies in entry mode research often informed by TCE have extensively examined JVs in high-risk environments (Hill et al., 1990; Hennart & Park, 1993; Henisz & Williamson, 1999; Meyer, 2001; Brouthers & Hennart, 2007), and have argued that political risk can be "strategically managed" through ownership and partner choices (Meyer, 2001; Delios & Henisz, 2003). Our analysis is consistent with that view but extends it in two ways. First, it focuses on *double hazards*—the simultaneous presence of state-level political risks and transaction-level behavioral risks (Henisz, 2000). Our case of DuPont-Mitsubishi shows in concrete terms how they are mitigated by multi-actors. Second, it introduces the t_0–t_2 diagram, which makes explicit that, under extreme hazard configurations, governance strategy is better understood as a *portfolio of interdependent safeguards* assembled over rather than as a single, one-off mode choice at a particular moment.

The findings indicate that mode choice needs to be operationalized in explicitly *multi-actor* terms. Prior research has analyzed triparty JVs including sōgō shōsha (e.g., Hennart, 1991; Hennart & Kryda, 1998), and the utility of JVs under politically volatile situations (e.g., Hennart & Park, 1993; Henisz & Williamson, 1999; Henisz, 2000; Meyer, 2001). Yet, the extant studies have paid limited attention to how hazards are mitigated across *linked*

transactions among multiple actors. The DuPont–Mitsubishi case illustrates a cross-link mechanism: Mitsubishi's credible commitment at one link (the Mitsubishi–Chemtex relationship) alters the hazard structure at another link (the DuPont–China JV negotiation) by securing a technology-transfer channel that protects DuPont's intellectual property. This kind of interdependence is difficult to capture within a purely dyadic approach, which typically treats each transaction in isolation.

4.7.2. Governance as a Temporal Sequence Connecting Structural and Relational Mechanisms

The findings also have implications for the structural–relational governance debate (Benito et al., 2009; Strange et al., 2009). Much of the literature has centered on whether structural safeguards can be substituted by relational mechanisms such as trust and reputations (Dyer & Singh, 1998; Dyer & Chu, 2003), or whether structural and relational mechanisms are complementary (Poppo & Zenger, 2002; Lazzarini et al., 2004; Hoetker & Mellewigt, 2009; Li, Poppo & Zhou, 2010; Poppo et al., 2016). More recent work in modern internalization theory, partly building on Williamson's calculative view of trust, tends to conceptualize relational mechanisms as fine-grained instruments operating *within* an already-given structural frame (Verbeke & Fari, 2019; Kano et al., 2020, 2022).

This corresponds to a t_1-t_2 phase in the diagram, in which relational governance and routine coordination are primarily observed inside established contractual or equity-based structures. The cases from 1990s China, characterized by high asset specificity ($k \gg 0$), strong safeguard requirements ($s \gg 0$), and limited host-country institutional knowledge at the lead MNE, point to a previously under-theorized, t_0 phase of governance: (1) credible commitments offered by a non-lead MNE on behalf of a lead MNE, and (2) the temporary externalization of orchestration functions to that third party.

The evidence suggests that under prohibitively high political and institutional uncertainty, governance evolution follows a multi-phase trajectory that precedes the observable t_1 phase: In an initial t_0 phase, pre-contractual credible commitments and proto-governance form emerge. In a subsequent transitional phase between t_0 and t_1, structural safeguards are introduced, and credible commitments become woven into these emerging structures. As uncertainty declines and host-country institutional knowledge accumulates at the lead MNE (t_1- t_2), stronger relational ties can deepen within more conventional Node C or Node D forms.

Seen through this temporal lens, third-party credible commitments become the connecting mechanism between structural and relational governance. What appears cross-sectionally as "relational mechanism embedded within formal structures" can be reinterpreted as the outcome of an earlier t_0 phase of unilateral credible commitments that made those structures viable under severe uncertainty. The theoretical implication is not that prior work is mistaken, but that it largely corresponds to later phases in the sequence; the present analysis makes the earlier phases visible and analytically tractable.

4.7.3. Implications for GVC Governance and Orchestration

Finally, the analysis has implications for GVC governance and the broader theory of orchestration. Existing GVC governance research typically posits that flexibility-seeking MNEs retain control over high-value, knowledge-intensive functions while outsourcing standardized or commoditized tasks such as production and logistics to external suppliers (Buckley & Ghauri, 2004; Mudambi, 2008; Buckley, 2009b). Yet others argued that this division of labor assumes that outsourcing reduces production costs, provided that associated transaction costs do not outweigh these savings (Strange & Humphrey, 2019). This argument raises a central question: how can firms simultaneously reduce production and transaction costs when operational flexibility is traded off against governance control, and when political

and institutional hazards are prohibitively high? The Fast Retailing–Mitsubishi case in 1990s China context, offers one answer in the form of a complementary governance pathway, denoted Node C′**,** in which orchestration is temporarily externalized to a sōgō shōsha prior to the lead MNE's move to Node C (direct outsourcing). Node C′ allows the lead MNE to capture the production-cost advantages of subcontracting while containing transaction costs that would otherwise escalate if it attempted to orchestrate a politically exposed chain directly.

By contrast, The DuPont–Mitsubishi case hence reveals a parallel, more hierarchy-like configuration, denoted Node D′, with DuPont maintains strategic influence over technology and key decisions, but shares orchestration and political-risk exposure with Mitsubishi and an international public authority (IFC). Taken together, Node C′ and Node D′ can be interpreted as early-stage, transitional governance structures under specific conditions before the formal structure that arise at t_1 and then unwind at t_2.

4.8. Conclusion and Future Research

In light of the foregoing analysis, the focus shifts from asking "which mode is chosen?" to asking "how are modes assembled and reconfigured over time?" The abductive, history-informed analysis shows how lead MNEs and sōgō shōsha co-construct governance architectures from t_0 credible commitments, through Node C′ and Node D′ transitional forms, toward more conventional Node C or Node D structures. In this sense, the primary role of the diagram is to reframe existing GVC governance and entry mode research insights as particular phases within a broader temporal sequence, while highlighting the distinctive role of sōgō shōsha as strategic governance actors under extreme political and institutional volatility.

Future research should further conceptualize credible commitments within this temporal and multi-actor perspective. Classical TCE acknowledges the significance of credible commitments and locates them primarily at Node C in a contracting schema and within buyer–supplier relationships, where one party requests safeguards from the other when perceived risks increase (Williamson, 1996; Williamson, 2008, p. 10; Cuypers et al., 2021). However, it offers limited guidance on when credible commitments arise relative to formal structures, how they shape the configuration of arrangements such as joint ventures rather than hybrid contracting, and why they emerge at particular points in the governance sequencing. While the cases identify both the location and the provider of credible commitments under specific context, showing that they are not always confined to classical hybrids, more analytical works are required toward the operationalization of this notion.

CHAPTER 5
FLAGSHIPS AND DEPARTMENT STORES: HOW DREAM COSTS SHAPE LUXURY DISTRIBUTION IN JAPAN

Abstract

This paper examines foreign luxury brands' channel choices in Japan—directly operated flagships versus department stores—through a unified lens of value creation and cost economization. Employing an abductive research design, we argue that department-store channels persist in Japan when savings in supplier "dream costs"—the expenditures required to stage, communicate, and sustain customers' dream value—together with reductions in customer dream costs more than offset the additional brand–intermediary transaction costs, making intermediation an efficient governance choice alongside direct flagships. This study contributes in two main ways. First, it extends luxury research by applying TCE logic to a luxury B2C setting. Integrating a value logic in luxury scholarship with a cost logic in TCE offers a more complete picture of marketing channel choice and the underlying mechanisms of firms' decision making. Second, the paper specifies conditions under which department store intermediation coexists with flagships, highlighting Japan's gaishō clienteling mechanism as a distinctive, cost-economizing governance device that shifts the cost calculus.

5.1. INTRODUCTION

Luxury is inseparable from social and cultural meaning (Kapferer, 2014a). Its management logic reverses conventional marketing rules: rather than minimizing visible outlays (e.g., Brun et al., 2008; Chevalier & Gutsatz, 2020), brands invest in symbols and experiential assets to construct "dream value" that renders brands incomparable (Phau & Prendergast, 2000; Tynan et al., 2010; Kapferer & Bastien, 2012; Kapferer & Valette-Florence, 2016). Directly operated flagship stores epitomize this logic: in response to the late-20th-century legitimacy crisis triggered by over-licensing and mass diffusion (Dion & Arnould, 2011; Dion & Borraz, 2015), global luxury houses expanded regional flagships to concentrate symbolic capital, communicate country-of-origin prestige (Moore et al., 2010; Manlow & Nobbs, 2013; Liu et al., 2016), and stage multi-sensory experiences (e.g., Kozinets et al., 2002; Paton, 2012; Joy et al., 2014; Dion & Borraz, 2015; Sabbadin & Aiolfi, 2019) that enable brands to curate the full "universe" of meanings underpinning willingness to pay (Blazquez et al., 2019).

Over the past decade, this brand building logic has been accompanied by a structural shift away from intermediated channels—especially department stores—toward direct retail (Chevalier & Gutsatz 2020). Performance trends reinforce the shift: direct formats have grown faster worldwide (Chevalier & Gutsatz, 2020), and department stores' share of personal luxury goods sales declined from ~26% in 2014 to ~13% in 2024 (D'Arpizio et al., 2025). From a governance perspective, this trajectory is consistent with a core tenet of Transaction Cost Economics (TCE): when assets—particularly brand-name capital—are highly specific, transaction hazards increase and hierarchical control becomes comparatively attractive (Williamson 1985, 1996; Anderson & Gatignon, 1986). Luxury scholarship similarly stresses that mono-brand control safeguards authenticity and reduces dilution risks in multi-brand settings (Kapferer & Bastien, 2012; Kapferer, 2014b). Taken together, TCE

and luxury theory imply that, as symbolic and experiential investments intensify, luxury houses should increasingly internalize distribution through directly operated stores.

Yet, alongside the global sales decline, intermediation has proved resilient in Japan, mediating a large share of luxury sales; industry estimates (Yano Research Institute, 2016) and our interviews suggest that direct retail (flagships) and intermediation (department store) each account for a meaningful portion of the market. This pattern appears to contradict the integration logic implied by high asset specificity and the global trend toward direct control.

It poses a governance puzzle: *if asset-specific symbolic and experiential investments generally favour internalization, under what conditions does department-store intermediation remain an efficient governance choice for luxury brands in Japan, and why does it coexist with, rather than yield to, directly operated flagships?*

This puzzle is sharpened by two related gaps in existing theory. First, classic TCE and internalization theory give limited guidance at the firm–customer interface. Williamson (2005, p. 6) explicitly prioritized inter-firm transactions, treating complications in firm–worker and firm–customer exchanges as of "lesser importance." Internalization theory likewise centers on intermediate-product transactions and notes that firms cannot "take over" household consumption (Buckley & Casson, 2010, p. 8). Empirical works of TCE such as entry mode and marketing channel research consequently focus on manufacturer–wholesaler–retailer relationships (Anderson & Gatignon, 1986; Anderson & Coughlan, 2002; Gatignon & Gatignon, 2010), leaving the costs borne between firms and consumers under-examined. Second, luxury research richly theorizes dream value—how consumers perceive symbolic, hedonic, and pragmatic value, and how brands create and deliver it through space, service, and narrative—but says far less about the cost side of sustaining that dream.

To address this blind spot, we reconceptualize the firm–customer interface in terms of "dream costs"—the cost-side counterpart to dream value and the analogue, at the firm–

customer boundary, of intra-firm governance costs and inter-firm transaction costs. We define dream costs as comprising two interdependent components: (a) supplier dream costs—the expenditures required by brands or intermediaries to stage, communicate, and sustain customers' dream value in practice; and (b) customer dream costs—the frictions customers incur before and after purchase, including search and evaluation under bounded rationality and bounded reliability, as well as switching and hold-up costs associated with relationship-specific learning (Williamson, 1985; Foss & Foss, 2005; Verbeke & Greidanus, 2009; Wu et al., 2014). This reconceptualization foregrounds the fact that creating and maintaining dream value is costly for both sides of the exchange, and that different channel structures may allocate, share, or economize these costs in distinct ways.

Against this backdrop, drawing on TCE and a critical-realist research design (abduction), this paper explains why department store intermediation persists in Japan's luxury market despite a global shift toward vertically integrated flagship stores. Focusing on foreign luxury brands' use of Japanese department stores versus directly operated flagships, we ask under what contextual and structural conditions department-store intermediation constitutes an efficient governance choice, and through which mechanisms it coexists with direct integration rather than being displaced by it. We argue that department-store channels remain efficient when savings in supplier dream costs—reinforced by reductions in customer dream costs—more than offset the additional transaction costs of using the intermediary, making intermediation at least as cost-effective as direct flagship channel. This argument extends TCE from inter-firm B2B exchange to B2C luxury retail, reframes department stores as dream-cost economizers rather than value dilutors.

This argument advances existing scholarship in two ways. First, it contributes to operationalizing TCE by re-specifying it for a luxury retail context, by drawing a clear line between intra- and inter-firm costs, and firm–customer costs, and by identifying the

mechanism through which costs of realizing a given bundle of dream value are distributed and economized across channels. Second, this paper contributes to luxury literature by specifying conditions under which intermediation (multi-brand store environment) coexists with flagships (mono-brand store environment) and yields two sets of propositions that can be tested in other markets.

The remainder of the paper proceeds as follows. We review the literatures on TCE and luxury theory. After briefly outlining the history of Japanese department stores and their clienteling system, we describe our research design, present our provisional value–cost framework, and develop propositions, before concluding with implications for scholarship and practice.

5.2. LITERATURE REVIEW

5.2.1. Theory of Governance Choice

Transaction Cost Economics (TCE) offers a rigorous lens for comparing the efficiency of alternative governance modes. Building on Coase's (1937) insight that using markets entails coordination costs, Williamson (1985, 1996, p. 379) formalized the boundary-of-the-firm problem by distinguishing (a) production costs (transforming inputs into outputs), (b) the governance costs of hierarchy (coordinating activities inside the firm), and (c) the transaction costs of markets (the frictions of arm's-length exchange, including ex-ante drafting, negotiating, and safeguarding, and ex-post adaptation, haggling, set-up and running, and bonding costs).

A core TCE proposition is that asset specificity shapes the comparative efficiency of governance (Williamson, 1996; Cuypers et al., 2021; Hennart & Verbeke, 2021). When investments are tailored to particular exchanges and difficult to redeploy, market transactions become hazard-prone—exposed to opportunism, hold-up, and costly maladaptation—so

internal organization tends to dominate. When assets are generic, market governance typically prevails (Williamson, 1996). International business research has widely applied this logic to entry mode choice and, in doing so, helped operationalize TCE (Anderson & Gatignon, 1986; Anderson & Coughlan, 1987; 2002; Brouthers & Hennart, 2007; Gatignon & Gatignon, 2010). They argue that in distribution contexts, intangible, human-capital specificity linked to what is sold and how it is sold is pivotal for governance choice (Anderson & Coughlan, 2002, p. 227). Contemporary work in GVC governance and TCE extension emphasizes human frailty—bounded rationality and bounded reliability—as fundamental sources of exchange hazards that firms must mitigate (Verbeke & Greidanus, 2009; Verbeke, 2025).

Despite these advances, costs associated with firm–customer exchange remain underdeveloped in governance theory. Williamson (2005, p. 6) explicitly prioritized inter-firm transactions and Internalization theory likewise limits analysis to intermediate-product transactions (Buckley & Casson, 2010, p. 8). Similarly, the TCE-informed entry mode research has largely examined inter-firm relationships among manufacturers-wholesalers-retailers (e.g., selling through wholesalers versus owned networks) within a supplier-centric frame (Anderson & Gatignon, 1986; Anderson & Coughlan, 2002; Gatignon & Gatignon, 2010). As an international retailing scholar cautions, translating this manufacturer-based transaction cost paradigm into B2C retail context requires care (e.g., Dawson, 1994).

Debates around digitalization consider whether new B2C models reshape conventional governance logics (Rindfleisch, 2019; Banalieva & Dhanaraj, 2019), whether new technologies allow MNEs to diminish implicit costs of internalization (Rangan & Sengul, 2009), and how platform-related frictions influence selling arrangements (Wang et al., 2024). Some contend that TCE remains robust even for digital service multinationals (Hennart, 2019; Hennart & Verbeke, 2021). Others advocate—under new technological

advances—shifting from a cost- to a value-based lens for boundary choices (Madhok, 1997) or adopting a cross-border coordination theory of value creation (Rangan & Sengul, 2009). Yet empirical—rather than purely conceptual—studies that integrate Williamson's comparative-cost logic with value-based analysis remain scarce.

Luxury retail is a particularly apt setting to advance this conversation. Transactions involve multiple forms of specificity—prime locations, architectural façades and immersive interiors, brand-trained human capital, reputational (brand-name) capital, and dedicated clienteling relationships—each costly to redeploy. By focusing on physical channels—and on an early, analog form of platform governance, the department store and its gaishō network—we exploit a context where exchange processes are structurally transparent, enabling a clear view of how value creation and cost economizing interact. Insights from this setting can also inform emerging, digitally mediated governance models that are more modular and granular in design (Rindfleisch, 2019)—that increasingly structure luxury distribution.

5.2.2. Dream Value and Dream Costs

Luxury value creation is not primarily about functional performance (Pine & Gilmore 1998); it centers on eliciting and sustaining a "dream" that justifies price premia and long-term loyalty. Dream value is assembled through fame and narrative, symbolic capital, and a coherent brand "universe," and is enacted in retail through carefully curated encounters with the brand (Kapferer & Bastien, 2012; Kapferer & Valette-Florence, 2016).

Luxury consumption is shaped by individual desires and social signaling (Kapferer & Bastien, 2012), and often governed by competing value logics: (i) distinction—other-oriented signaling of status and taste; (ii) hedonism—self-oriented sensory and emotional payoff; and (iii) pragmatism—instrumental benefits (e.g., Welté et al., 2021; Mandel, 2009; Kapferer &Valette-Florence, 2016; Gladstone et al., 2024). Cultural context shapes these emphases

(Wiedmann et al., 2007): in collectivist settings, distinction motives are especially salient (Shukla & Purani, 2010; Le Monkhouse et al., 2012; Shukla et al., 2015), whereas for Western consumers hedonism and experiential aspects exerts a stronger positive influence on purchase intent (Aliyev & Wagner, 2018). Emphases also vary by gender and generation (Tafani et al., 2024).

Retail is the primary stage on which dream value is realized (Dion & Arnould, 2011). Brands heighten purchase intention by amplifying perceived dream value through experiential marketing—sensorial atmospherics (Kotler, 1973), immersive, aestheticized spaces (Pine & Gilmore, 1998; Dion & Arnould, 2011; Joy et al., 2014), prime locations that confer symbolic capital (Arrigo, 2015), and calibrated scale and assortment that raise salience and choice confidence (Manlow & Nobbs, 2013; Chevalier & Gutsatz, 2020). Authenticity—the sense that the offer is true to a brand's history and craft—further conditions perceived value (Hernandez-Fernandez & Lewis, 2019). Flagships epitomize this logic (Moore et al., 2010; Liu et al., 2016), allowing brands to curate the full "universe" of meanings that underwrite willingness to pay (Blazquez et al., 2019).

While the literature richly documents what dream value is, how it is produced and delivered, it says far less about the costs of producing and sustaining it. We reconceptualize these as dream costs—the cost-side counterpart to dream value—to foreground the expenditures and frictions that must be managed for dream value to materialize in practice. Early attempts to incorporate firm–customer frictions into governance (Sarkar et al., 1995, 1998)—showed that firms adopt intermediaries when the costs of direct coordination with consumers exceed the costs of using intermediaries, and that institutional and social factors can support intermediary survival. However, that work centers on digital markets and does not conduct cost-comparative analysis in symbolic, experiential settings—like luxury—where

asset specificity is high. Hence, our understanding of how costs interact with value dimensions, and how this interaction shapes retail governance, remains incomplete.

Two gaps follow. First, cost-based perspective, TCE-informed entry mode research has focused on inter-firm relations, and B2C e-commerce studies building on TCE typically do not consider the level of asset specificity. Second, while luxury research richly theorizes value, its cost complement remains underdeveloped. The paper integrates these two notions —value and cost—, which enables TCE to travel credibly into B2C retail while preserving its comparative-governance logic.

5.2.3. The Japanese Department Store

As noted in the introduction, department stores' share of luxury sales has declined globally even as intermediation remains resilient in Japan. Explaining this puzzle requires brief attention to Japan's distinctive retail lineage. As Hollander (1960, p. 40) observed, Japanese department stores developed "contrary" to the British–American pattern: rather than beginning as low-margin formats that gradually upgraded, they entered at the high end from the outset (Fukami, 1953, p. 42). Many trace their origins to seventeenth-century drapers (gofukuya) serving elite samurai households (Nida & Mizukoshi, 2013, p. 68), later expanding their customer base while continuing to target affluent consumers (Fujioka & Stobart, 2018, p. 258). This heritage institutionalized norms of exclusivity, long-term trust, and bespoke service (Ito, 2019). Central to this model is gaishō (out-of-store sales), a membership-based clienteling system for privileged customers (Nida & Mizukoshi, 2013; Ito, 2019).

5.3. METHODOLOGY

We adopt critical-realist abductive research approach (Sakakibara, 2008; Welch et al., 2011; Fletcher, 2017). Critical realism (CR) posits that social and economic phenomena are generated by real but often unobservable mechanisms that exist independently of our recognition of them and can be investigated empirically (Welch et al., 2011, p. 748). Rather than predicting regularities, the goal is to identify the contextual conditions under which particular causal mechanisms are activated and generate the observed empirical patterns (Fletcher, 2017, p. 189). This stance is well suited to our focus because the central construct—transaction costs at the firm–customer interface—is still under-formalized in the existing theoretical literature (e.g., TCE and internalization theory). This design allows us to start from an initial theory. Guided by TCE and the luxury literature, we first developed a deductively derived framework for luxury channel choice (see next section). Our framework combines the comparative-governance logic from TCE with the notion of "dream value" from the luxury literature.

5.3.1. Data Collection

Consistent with CR, we assembled two complementary data streams to develop plausible causal conjectures: intensive data and extensive data (Fletcher, 2017). Intensive data consist of in-depth, mechanism-focused narratives that illuminate how actors manage brand–retailer-customers interface in practice. We conducted four semi-structured interviews with experienced practitioners held senior responsibilities in foreign luxury brands and in Japanese department store contexts (Table 5-1). Together, these informants cover: both brand-side and department store perspectives; multiple product categories (fashion, leather goods, watches, jewelry); and roles directly involved in channel management, and clienteling. Our aim is not statistical generalization or saturation of all possible narratives but mechanism

theorization: we treat these interviews as theoretically informative cases that reveal how costs and value are allocated and economized across channels.

Extensive data comprise industry statistics, market reports, annual/financial filings, firm publications, and a systematic news review. These sources establish macro-level trends in channel shares, performance, and organizational practices and provide an independent check on patterns reported in the interviews.

Table 5-1

Data sources and collection

Panel A. Intensive data: semi-structured interviews

Organization (anonymized)	Interviewee role	Modality/ Location	Date	Duration
Italian luxury fashion, independent brand	Former Department Store Manager	In person, Osaka	16-Aug-24	14:00–17:00 (3h)
French luxury conglomerate (fashion, watches, jewelry)	Former Retail Manager	In person, Osaka	25-Jul-24	13:00–14:00 (1h)
Italian luxury leather, independent brand	Former Retail Director	In person, Osaka	31-Aug-24	13:00–14:00 (1h)
Italian luxury menswear, independent brand	Former VP / Sales Director	Phone	22-Apr-21	16:00–16:30 (30m)

Panel B. Extensive data: secondary sources

Source type	Details / period–coverage
Annual and financial reports; press releases	Draper-originated department store groups: ISETAN MITSUKOSHI LTD., DAIMARU MATSUZAKAYA DEPARTMENT STORES CO. LTD. (J. Front Retailing), and Takashimaya Company, Limited; firm publications (various years)

Industry reports	Yano Research Institute; Nomura Research Institute; Japan Department Stores Association; CBRE; Bain & Company (various years)
News articles (systematic review)	158 articles, 1985–present (*Nikkei; Senken*)
Trade magazines / firm data	*Kojima Fashion Marketing*
Prior case materials	Previous case studies conducted by the author

Note. Prepared by author. All interviews were semi-structured, mechanism-focused, and anonymized; local times reported (JST).

5.3.2. Data Analysis

Guided by this CR-inspired design, we conducted an analysis in two steps: First, we used our initial framework to (re)describe the phenomenon, and iteratively compared this initial framing with interview narratives and extensive secondary data to clarify constructs, surface rival explanations (e.g., bargaining power, or pure brand-equity safeguarding), and specify how value–cost dynamics appear across brands, department stores, product categories, and customer segments. Second, we inferred the mechanism that could plausibly generate the observed patterns. On this basis, we formalized a value–cost framework that yields propositions on channel choice and coexistence in Japan's luxury market.

Throughout, triangulation across data sources (Fiss, 2009; Yin, 2018) underpins the analysis: we cross-checked interview accounts against industry statistics, firm documents, and news coverage, using convergence and divergence between sources to refine our theorization. The next section explains theoretical components, and presents the provisional value–cost integrative framework and that organizes the subsequent empirical analysis.

5.4. CONCEPTUAL FRAMEWORK

We first define a typology of value and cost at the brand–intermediary–customer interface. We then assemble these elements into an integrative framework that we later use to interpret the evidence.

5.4.1. Typology of Value

Supplier dream value (SDV and SDV')

SDV denotes the tangible and intangible benefits that a supplier (or its channel) creates to spark customer aspiration and purchase intent (Phau & Prendergast, 2000; Kapferer, 2017, p. 32). In luxury, intangibles such as symbolic capital, fame, authenticity, and a coherent brand narrative render the offer incomparable and support premium pricing and loyalty (Pine & Gilmore, 1998; Kapferer & Valette-Florence 2016; Aliyev & Wagner, 2018). Retail price reflects the monetization of this supplier dream value. In our framework, SDV denotes value created by the brand, whereas SDV' denotes value created by the department store.

Customer dream value (CDV and CDV')

CDV is the consumer's subjective evaluation of worth. Luxury buyers combine overlapping value logics as discussed above in the review—(i) distinction; (ii) hedonism; and (iii) pragmatism (e.g., Welté et al., 2021; Mandel, 2009; Kapferer & Valette-Florence, 2016; Gladstone et al., 2024)—with weights that vary by culture, gender, and generation (Wiedmann et al., 2007; Shukla & Purani, 2010; Shukla et al., 2015; Aliyev & Wagner, 2018; Tafani et al., 2024). These logics shape what customers expect from the retail experience and, ultimately, their willingness to pay (Bowman & Ambrosini, 2000). In our framework, CDV denotes perceived value when the transaction occurs through a direct (flagship) channel, whereas CDV' denotes perceived value when it occurs through a department store channel.

5.4.2. Typology of Costs

Efficiency in luxury retail depends on three cost classes: (i) governance costs of hierarchy (GC), (ii) transaction costs between brand and intermediary (TC), and (iii) costs at the firm–customer interface, which we reconceptualize as "dream costs" (DC). Firms select governance structures that minimize the total costs of organizing exchange. In this analysis, production costs are held constant across channels given the vertically integrated supply chains typical of luxury.

Governance costs (GC) and Transaction costs (TC)

Williamson (1985; 1996) distinguishes internal coordination costs (GC) from "costs of running the economic system" in markets (TC). In luxury contexts, multiple assets are highly specific and create bilateral dependency. Prime flagship sites (e.g., Ginza, Fifth Avenue) and first-floor concessions in prestige department stores embody symbolic capital; once committed, relocation risks eroding reputational capital. Similar specificity characterizes logistics, fixtures, interiors, secure-handling protocols, and service scripts tailored to luxury standards. Such specificity raises both governance and safeguarding burdens and is central to comparative governance choice.

Dream costs (DC)

We treat firm–consumer frictions as dream costs—costs at the interface between brand or intermediary (or its channel) and end customers—distinct from GC and TC. Dream costs have two interdependent components:

Customer dream costs (CDC). Ex-ante search and evaluation burdens under bounded rationality and bounded reliability (limited information and imperfect trust), plus ex-post switching and hold-up costs created by relationship-specific learning (Williamson, 1985; Foss & Foss, 2005; Verbeke & Greidanus, 2009; Wu et al., 2014). CDC can differ across

formats; we denote customer dream costs in the brand's own channel as CDC, and those in department store channels as CDC'.

Supplier dream costs (SDC). Supplier-side outlays to stage, communicate, and sustain customer dream value (CDV). We compare costs in direct channels (SDC) with those when serving through an intermediary (SDC'). Typical SDC/SDC' investments include brand-trained fashion advisors (human specificity), flagship architecture and interiors (physical specificity), and long-horizon clienteling/CRM system (dedicated relational assets). These investments safeguard authenticity and reputation and underpin the ability to charge premium prices.

5.4.3. Provisional Value–Cost Framework

Building on TCE, Sarkar et al. (1995, 1998) argued—within e-commerce settings—that firms favor intermediated channels when the governance costs and the costs of directly coordinating with consumers exceed the combined costs of using intermediaries, and vice versa. While their framework was developed for digital markets, the underlying comparative logic is portable. We apply it to a context where asset specificity and experiential staging are central—flagships and department store concessions—and make the following three distinctions explicit to suit this luxury setting:

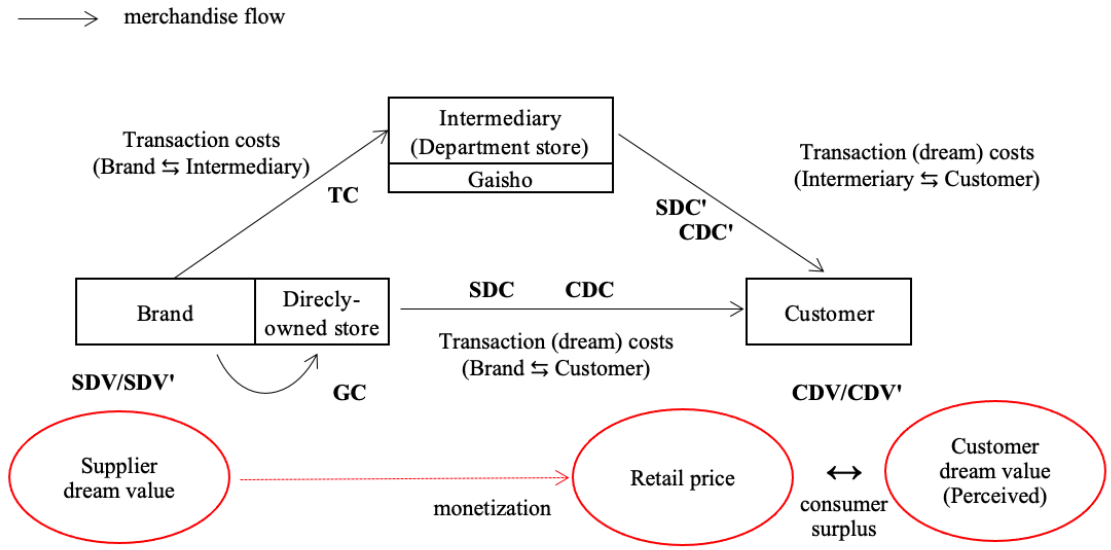
First, as for dream value dimension, supplier dream value created by the brand (SDV) or by the intermediary (SDV') versus customer dream value (CDV) as perceived and realized by consumers. Second, for governance costs, the costs of hierarchy (GC) versus the transaction costs of brand–intermediary market exchange (TC). Third, concerning, dream costs, supplier dream costs in the direct channel (SDC) versus in the intermediated channel (SDC'); and customer dream costs in the direct channel (CDC) versus in the intermediated

channel (CDC'). We also attend to the within-channel pairings (SDC with CDC in direct; SDC' with CDC' in intermediated) because supplier and customer burdens co-move in practice.

Figure 5-1 integrates these elements and serves as the conceptual foundation for the empirical analysis that follows.

Figure 5-1

Conceptual framework



SDV/SDV': Supplier dream value brand or department store creates; CDV/CDV': Customer dream value (perceived) when a transaction occurs through a direct channel (CDV) or a department store channel (CDV')
TC: Transaction costs (i.e., governance costs of market organization); GC: Governance costs of internal organizat
SDC: Supplier dream costs of internal organization; SDC': Supplier dream costs of market organization
CDC: Customer dream costs of internal organization; CDC': Customer dream costs of market organization

Note. Prepared by author, based on Sarkar et al., (1995, 1998); Williamson (1996); Kapferer & Bastien (2012), etc.

5.5. FINDINGS

Guided by our framework, we examined how the value and cost components at brand–intermediary–customer interface operates in practice. We triangulated interview

accounts with secondary sources and interpreted the patterns through the lens of the extant literature.

5.5.1. Customer Dream Value vs. Supplier Dream Value

Consistent with evidence that formats attract different clienteles (Dion & Borraz, 2017, p. 15), each channel cultivates a distinct form of customer dream value (CDV). Consumers combine value logics—distinction (other-oriented status signal), hedonism (self-oriented pleasure), and pragmatism (investment or lifestyle fit) (Kapferer & Bastien, 2012; Welté et al., 2021)—and those mixes shape what they expect from the retail encounter. All formats work to translate supplier dream value **(**SDV**)** into realized CDV, but they do so via different pathways.

For one customer segment, CDV rests on authenticity and symbolic aura. Motivated by distinction and hedonism, these consumers experience "the dream" only when the full brand universe is staged without compromise. As a former retail manager at a French luxury group put it, flagship stores

"*offer immersive experiences... a break from the demands of daily life*," whereas

"*it is sometimes difficult to offer the entire brand universe in department store settings*."

Directly operated flagships thus privilege authenticity and atmospheric immersion, reinforcing supplier dream value in ways that may be hard for department stores to replicate. These interviews results are consistent with prior studies that multi-brand environments are less hedonic than mono-brand stores (Desmichel & Kocher, 2020) and that flagships naturally serve distinction-driven consumers (Dion & Borraz, 2017).

For other segments, CDV is tied to quieter forms of hedonism, and, in some categories, to pragmatic motives. An ex–department store manager observed that some affluent clients—often not "new riches"—

"*prefer shopping at home and visits from department store gaishō rather than visiting stores...purchase is not for showing off but for personal pleasure.*"

A former senior executive at a French conglomerate similarly noted that clients treating high-end watches or art as assets seek

"objective evaluations and integrated, cross-brand information—including financial considerations—rather than recommendations confined to a mono-brand."

Because gaishō operate across brands and categories, they create SDV' through curated assortments, cross-category synergies, and personalized at-home clienteling that mono-brand flagships cannot easily match.

We also observe variation across department store groups. Isetan–Mitsukoshi mobilizes its gaishō network as a full-spectrum concierge, orchestrating services that span fashion, beauty, food, health, and even travel and education; Daimaru–Matsuzakaya blends gaishō expertise with big data analytics to craft highly individualized proposals. Despite different organizational approaches, both rely on gaishō as a relationship-intensive mechanism that converts trust, comparative product knowledge, and cross-category curation into purchase confidence, thereby linking SDV' to CDV.

In sum, formats translate SDV into distinct CDV outcomes because customers weight distinction, hedonism, and pragmatism differently. Flagships create CDV via authenticity and mono-brand immersion; department stores create CDV' via deep cross-category expertise, credibility and integration, with gaishō acting as the relational engine.

5.5.2. Transaction Costs vs. Governance Costs of Hierarchy: Intermediation vs. Internalization

In Williamson's term, the governance costs of hierarchy (GC) and the transaction costs of market exchange (TC) are functions of asset specificity (k), and contextual shift

parameters (x) such as culture, policy, and history—i.e., $GC = g(k, x),\ TC = t(k, x)$ (Williamson, 1996, p. 107).

When assets are generic ($k = 0$), markets dominate ($0 < TC < GC$). As bilateral dependency rises with semi-specific ($k > 0$) or highly specific assets ($k \gg 0$), market governance becomes comparatively disadvantaged ($TC > GC > 0$).

Holding contextual contingencies constant for within-market channel choice ($x = 0$), the level of asset specificity (k) becomes pivotal and shapes comparative costs. Luxury distribution in Japan exhibits multiple forms of asset specificity and thus requires significant investments in site, physical, human, and brand-name capital, and dedicated assets. Against this backdrop, we compare GC and TC across these dimensions; Table 5-2 summarizes the resulting cost patterns.

Table 5-2

Cost comparison

GC vs. TC	Direct Flagship Stores (GC)	Department Store Channel (TC)	Cost comparison
Site specificity	$k \gg 0$—fixed rents to property owner in prime locations	k≫0—sales commissions; indexed to rent-to-sales ratios	$GC_{site} \approx TC_{site} \gg 0$
Physical specificity	k>0— logistics, compliance/miscellaneous costs: lower—direct control avoids additional external compliance costs. k>0—distribution and inventory costs: generic—mitigated by economies of scale; large-scale stores reduce inter-store transfer inefficiencies.	k>0— logistics, compliance/miscellaneous costs: higher—duplicated reporting process, additional costs due to department store safety, service, and quality standards k>0—distribution and inventory costs: generic—small-scale concessions create costly distribution inefficiencies.	$TC\ physical > G\ C\ physical > 0$
Brand name capital specificity	k≫0—limited risk of value dissipation, opportunism, or free-riding	k≫0—higher risk of value dissipation in multi-brand environments	$TC\ brand > GC\ brand \gg 0$

SDC vs. SDC'	Direct Flagship Stores (SDC)	Department Store Channel (SDC')	Cost comparison
Physical specificity	k≫0—architectural façades and interiors designed to display products as if in art institutions; larger store sizes and merchandise volumes enhance visibility	k>0—less focused on symbolic display; smaller store sizes and merchandise volumes	$SDC_{physical} - SDC'_{physical} \approx CDV_{physical} - CDV'_{physical}$
Human asset specificity	k≫0—brand-trained staff required to deliver immersive brand experiences	k≫0—staff are seconded from—and trained by—the brand.	$SDC\ human \approx SDC'\ human \gg 0$
Dedicated asset specificity	k≫0—own loyalty programs to foster repeat purchases	k≫0—Gaisho mechanism providing long-term, trust-based relationships	$SDC\ dedicated > SDC'\ didicated \gg 0$

Note. Compiled from interviews and secondary sources.

5.5.2.1. Site specificity

Flagships require prime, symbolically charged locations; department stores also occupy prime sites and allocate scarce ground-floor space to select brands. Flagships face high fixed rents; department stores levy sales commissions on brands that, according to a former Italian brand sales executive, are

"*more or less indexed to the rent-to-sales ratio per square meter in the direct channel"*.

Site burdens are very high in both channels, and broadly similar. The following comparative-cost relation then obtains:

$$GC_{site} \approx TC_{site} \gg 0. \qquad (5-1)$$

5.5.2.2. Physical specificity

While many physical assets are generic in distribution contexts (Anderson & Coughlan 2002, p. 227), luxury retailing settings exhibit semi-specificity due to bespoke interiors and specialized logistics (e.g., secure handling, premium packaging, and display standards). Smaller in-store concessions frequently face stock/replenishment frictions and duplicate logistics; larger flagships amortize fixed costs and reduce missed sales. As one former sales director put it: "*In Japan, where it costs hundreds of yen to move even a single necktie from one store to another, it is inefficient to have many small shops*." Hence, costs tied to physical assets tend to be higher in the intermediated channel:

$$TC_{physical} > GC_{physical} > 0. \qquad (5-2)$$

5.5.2.3. Brand-name capital specificity

Reputational assets in luxury—prestige, aura, and trust—are highly specific and costly to rebuild (De Vita et al., 2011; Williamson, 1996). In multi-brand environments, protecting this symbolic capital requires more intensive monitoring and safeguarding by the brand. Two hazards are especially salient ex ante: value dilution where proximity to other brands or tiers blurs positioning and erodes perceived exclusivity; free-riding, where service and promotion fueled by a mono-brand channel is appropriated by another channel that closes the sale.

Department stores, in turn, strive for protecting their own institutional reputation. Top-tier stores therefore impose strict compliance on brands—detailed incident reporting, packaging and goods transfer protocols, rigid standards on services, and testing and inspections for quality assurance—burdens all the interviewees described as substantial. Directly owned stores can rely on globally standardized processes that reduce these adaptation burdens. Hence, brand-capital–related transaction costs in the intermediated channel tend to exceed governance costs in the direct channel. The following comparative relation obtains:

$$TC_{brand} > GC_{brand} \gg 0. \qquad (5-3)$$

5.5.2.4. Integrated inference

In Japan's luxury retailing context, $TC > GC > 0$ generally holds, consistent with brands' revealed preference for direct store operations. This sets the stage for incorporating the layer of dream costs into the conventional cost-comparison equation to explain why intermediation nonetheless persists.

5.5.3. Dream Costs

Dream costs are the outlays required to stage, communicate, and sustain customer dream value (CDV). Luxury suppliers undertake specific, hard-to-redeploy investments whose payoff is tightly bound to symbolism and exclusivity (Williamson, 1996; Kapferer, 2017). Accordingly, we examine three sources of SDC (brand-borne dream costs in flagships) versus SDC' (department store channel) —physical, human, and dedicated relational assets— and show how each interacts with value dimensions (CDV/CDV') and customer-side frictions (CDC/CDC').

5.5.3.1. Physical asset specificity

Flagships incur high SDC to stage authenticity and hedonic immersion—façades, gallery-like interiors, and multisensory atmospherics—that elevate customer dream value (CDV) (Dion & Arnould, 2011; Joy et al., 2014). Department store channels typically economize on these elements (lower SDC'), but consequently tend to yield lower CDV', consistent with evidence that multi-brand settings—exemplified by department stores—emphasize comfort and convenience over exclusivity and intense hedonism (Dion & Borraz, 2017; Desmichel & Kocher, 2020). Taken together, the channel gap in supplier dream costs tracks the difference in customer dream value, such that:

$$SDC_{physical} - SDC'_{physical} \approx CDV_{physical} - CDV'_{physical} \qquad (5-4)$$

5.5.3.2. Human asset specificity

Brand-trained client advisors are another form of idiosyncratic investment in distribution and marketing context (Anderson & Coughlan 2002). Their expertise, product knowledge, and service scripts are central to staging dream value. Both formats rely on brand-trained client advisors; in department store concessions, staff are often seconded

from—and trained by—the brand. Training and capability costs are therefore comparable, implying:

$$SDC_{human} \approx SDC'_{human} \gg 0. \qquad (5-5)$$

5.5.3.3. Dedicated relational assets

Both channels also invest in relationship-specific assets to economize customer dream costs (CDC/CDC')—notably search and evaluation—and to deepen trust, loyalty, and personalization. Flagships leverage authenticity and global reputation (Moore et al., 2010; Manlow & Nobbs, 2013; Liu et al., 2016), often via loyalty programs and bespoke clienteling. Department stores, in turn, deploy the gaishō system: Gaishō representatives act as dedicated relationship managers who provide personalized advice and lifestyle support—including in-home consultations. In luxury categories where credibility matters, gaishō mitigates uncertainty throughout the shopping journey and performs high-touch relational work on behalf of brands. Leveraging on their long-horizon relationship capability, and based on the accumulation of tacit knowledge of tastes and risk preferences, Gaishō reduce customers' bounded rationality (through curation and translation of technical information) and bounded reliability concerns (via institutional assurance). By lowering these customer-side costs, suppliers enhance their client's perceived value (Foss & Foss, 2005) and help sustain loyalty (Wu et al., 2014).

The commercial salience is visible in outcomes: at Matsuzakaya Nagoya store, gaishō reportedly account for ~40% of store sales (J. Front Retailing, 2021); at Daimaru–Matsuzakaya (FY2019), gaishō generated 71% of art, 42% of watch, and 29% of luxury fashion sales (J. Front Retailing, 2020)—precisely the categories with the highest search, evaluation, and credibility demands. Interviews mirror this gradient: pragmatic-driven customers and high-stakes, investment (art, watches) or distinction-intensive (watches)

categories elicit stronger demand for objective, cross-brand guidance, whereas hedonically driven categories (fashion, cosmetics) rely more on self-oriented aesthetic judgment and require relatively less third-party assurance. Taken together, these department store dedicated assets provide structural assurance in the product categories where the objective evaluation is required and materially lowers customer-side frictions, realizing customers' dream value in a way distinct from flagship stores.

5.5.3.4. Integrated inference

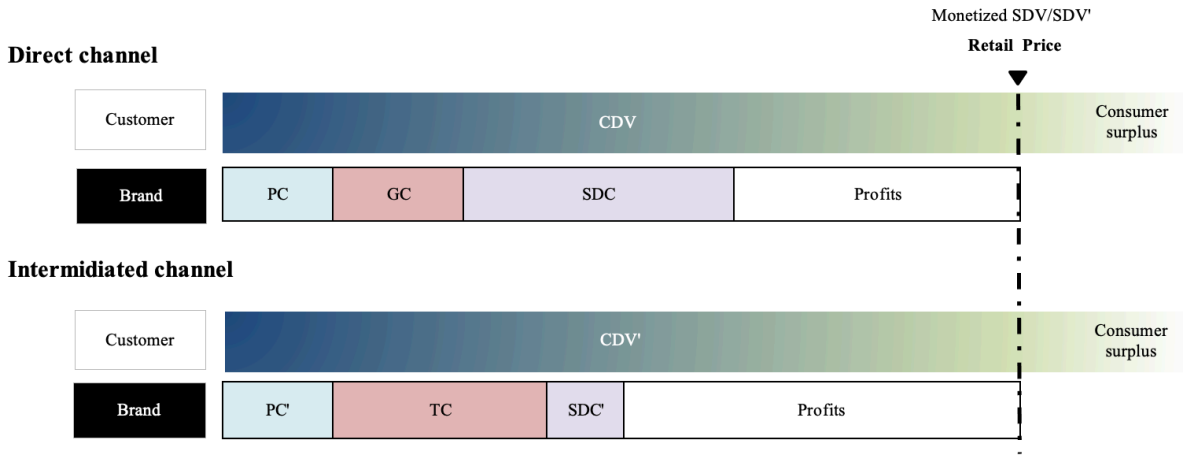
Physical specificity tends to favor flagships on the value side but raises SDC; human specificity is materially similar across channels; and dedicated relational assets simultaneously reduce SDC' and CDC'. These patterns set up the formal value–cost conditions we analyze next.

5.6. DISCUSSION

This section synthesizes the preceding arguments and develops testable propositions by specifying the contextual and structural conditions that shape luxury brands' channel choices in Japan. Building on the preceding analysis, Figure 5-2 applies the provisional framework introduced earlier (Figure 5-1), linking its theoretical logic to the empirical evidence assembled in the previous section.

Figure 5-2

Value-cost integrative model: direct vs. intermediated channels



Note. Illustrated by author.

SDV—Supplier dream value a brand creates; SDV'—Supplier dream value a department store creates; CDV—Customer dream value (perceived); PC—Production costs of internal organization; PC'—Production costs of market organization ($PC = PC'$); TC—Transaction costs (i.e., governance costs of market organization); GC—Governance costs of internal organization; SDC—Supplier dream costs of internal organization; SDC'—Supplier dream costs of market organization.

These costs and value are measured per transaction of a specific luxury good.

5.6.1. Set-up and Primitives

We compare flagships with department store channels—the two formats that dominate core luxury sales. For tractability, we treat directly-owned free-standing stores as weaker variants of flagships and exclude direct outlets/online stores which remain marginal for top-tier luxury brands sales.

Two features of the setting matter: First, luxury brands typically follow a uniform retail price P across formats for core assortments in a host market (e.g., Hermès sells the same Birkin at the same price in flagship or department store). Therefore, monetized SDV and SDV' is equal to the uniform retail price P as shown in figure 5-2. Second, customers'

dream value differs by retail formats ($CDV \neq CDV'$). When willingness to pay exceeds the retail price P, the gap constitutes consumer surplus—heterogeneous and inherently ambiguous—and, as our findings show, each channel attracts customers driven by different value logics. Hence, surplus differs by channel even at the same price:

$$CS^F = CDV - P, \quad (5-6)$$

$$CS^D = CDV' - P. \quad (5-7)$$

where CS^F and CS^D denote customer surplus of flagship and department store, respectively. On the cost side, brands incur two categories of outlays to deliver and stage the offer: First, governance costs for internal coordination in direct channels (GC) vs. brand–intermediary transaction costs in department stores (TC). Second, supplier dream costs borne by the brand in its own channel (SDC) vs. when serving through the intermediary (SDC').

Total per-unit organizing cost is therefore $GC + SDC$ for flagships and $TC + SDC'$ for department store channel. In Japan's luxury retailing context—characterized by high asset specificity ($k \gg 0$) —field evidence indicates $TC > GC > 0$. If these intra- and inter-firm costs were the only consideration, forward integration would dominate; the persistence of department stores therefore requires a cost offset elsewhere.

5.6.2. Reconciling the Paradox: The Role of Dream Costs

Formally, intermediation is efficient when the brand's total organizing cost via the intermediary is no higher than serving the client directly:

$$TC + SDC' \leq GC + SDC. \quad (5-8)$$

Equivalently, this condition can be written as:

$$TC - GC \leq SDC - SDC'. \quad (5-9)$$

Proposition 1 (condition for intermediary persistence)

With uniform within-market pricing and positive asset specificity ($k > 0;\ k \gg 0$), the department store channel persists when its dream cost savings for the brand more than offset the extra coordination costs of using the department store; that is,

$$TC - GC \leq SDC - SDC'.$$

In short, cost differentials—not absolute value levels—govern persistence, and supplier dream costs become decisive in channel choice.

5.6.3. Strategic Collaboration: The Viability of Partial Forward Integration

Why can department stores deliver such savings? Japanese department stores deploy the gaishō system—personalized, out-of-store clienteling for affluent customers—which (i) substitutes for brand-borne, high-touch tasks (lowering SDC') and (ii) reduces customers' search and evaluation burdens through credible, cross-brand curation and objective advice (lowering CDC'). Because part of the customer's dream costs is absorbed by these intermediaries, the brand's residual burden declines. Even where intermediation is efficient for specific categories or client segments, flagships remain essential to safeguard authenticity, stage the full brand universe, and anchor symbolic capital. The empirically observed outcome in Japan is therefore a portfolio solution: direct stores for aura-intensive expression and control; department stores for serving heterogeneous, service-intensive clientele while economizing dream costs on both sides of the exchange.

Proposition 2 (Coexistence condition)

Partial forward integration (coexistence of the flagship store and department store) is strategically viable when the intermediated channel materially lowers both brand-side and customer-side dream costs while flagships perform brand-building and authenticity functions; formally,

$$TC - GC \leq SDC - SDC' \text{and } CDC' \ll CDC.$$

Under these conditions, coexistence, rather than exclusivity, maximizes system performance.

5.6.4. Profit-Margin Corollary

Under within-market price parity, we define per-unit margins as:

$$\pi^D = P - (PC' + TC + SDC'). \quad (5-10)$$

$$\pi^F = P - (PC + GC + SDC). \quad (5-11)$$

$$PC = PC'. \quad (5-12)$$

where π^D and π^F denote conceptual margins (not accounting) for the department store and flagship channels, respectively. If cost-offset condition holds, i.e., $TC - GC \leq SDC - SDC'$, then $\pi^D \geq \pi^F$ follows directly as a reduced-form implication of the framework.

Moreover, the advantage of the department store channel should be especially pronounced in institutional settings where customer dream-cost intensity is elevated (e.g., cultures that demand highly personalized service) or where consumers are more often guided by pragmatic financial considerations than by hedonism or distinction. In such contexts, intermediated channels that economize on both supplier and customer dream costs are more likely to sustain a margin edge despite brands' general preference for integration.

5.7. THEORETICAL IMPLICATION

5.7.1. Firm Boundaries (Cost-based Perspectives versus Value-based Perspectives)

In firm boundary literature, two broad strands shape how scholars think about governance choice. One is cost-based view, and the other is value-based perspective. First, TCE explains boundaries in terms of the comparative costs of alternative governance modes under conditions of asset specificity, uncertainty, and opportunism (Williamson, 1985, 1996). Within this tradition, marketing channel work already recognizes intangible asset specificity—particularly brand-name capital and retailer-specific human capital—and the

associated costs of safeguarding brand equity against opportunism and free-riding (Anderson & Gatignon, 1986; Anderson & Coughlan, 2002;). The primary focus is on the inter-firm interface—manufacturer–wholesaler–retailer relations—and on how monitoring, contractual safeguards, and selective partner choice protect the brand in the presence of asset specificity (Anderson, 2010; Gatignon & Gatignon, 2010). In this stream, frictions related to safeguarding brand-name capital are treated as a specific class of transaction costs between firms.

Second, value-based perspectives building on the resource-based view, such as Madhok's (1998) organizational capability approach, argue for a shift in frame from cost minimization to value creation in boundary analysis. This work highlights the limits of a purely cost-based lens, especially in complex, knowledge- and brand-intensive contexts, and emphasizes how firm capabilities to create and appropriate value shape governance decisions.

Our value–cost integrative framework speaks directly to these two approaches. TCE already has conceptual room to accommodate frictions that arise in transactions between firms and consumers (Williamson, 2005, p. 5), yet classic TCE has prioritized the comparison between hierarchy (intra-firm governance costs), and market (inter-firm transaction costs), offering limited theoretical guidance on the firm–customer interface.

Our study contributes to operationalizing TCE in three ways. First, we re-specify it for a luxury retail context where value is inherently symbolic and experiential. Second, we draw a clear distinction between: (1) intra-firm governance costs (GC) and inter-firm transaction costs (TC), including transaction costs associated with safeguarding brand equity and coordinating with intermediaries, and (2) firm–customer costs, which we conceptualize as dream costs—the supplier's expenditures required to stage, communicate, and sustain customers' dream value, and the frictions customers incur when searching, evaluating, and switching under conditions of bounded rationality and bounded reliability, including

opportunism. Third, we identify the mechanism through which the costs of realizing a given bundle of dream value are distributed and economized across integrated and intermediated channels.

Two theoretical implications follow. First, our framework re-centers costs in the analysis of marketing channel boundaries in a way that is fully integrated with value: the question is not whether value or cost matters more, but how the costs of realizing customer's perceived value are structured across governance modes.

Second, we show that even in high-symbolic contexts, the efficient outcome may be coexistence rather than pure forward integration. Even when inter-firm hazards and brand-equity safeguarding costs push toward full internalization, reallocating dream costs via an intermediary can restore the efficiency of a partially intermediated solution. This offers a nuanced response to calls for a value-based shift in boundary analysis: the value dimension remains central in luxury, but cost offsets in creating and realizing that value still govern the choice between integration and intermediation.

5.7.2. Channel Governance (Intermediation versus Disintermediation)

Within marketing channel research, debates on digital intermediation and electronic markets have centered on whether information technologies that enable direct supplier–buyer linkages will trigger disintermediation. Sarkar et al. (1995, 1998) is a key reference. They challenge simplistic disintermediation predictions by arguing that the Internet can both lower transaction costs for direct exchange and create new roles for "cybermediaries." Their comparative analysis shows that increased outsourcing of channel functions and more complex producer–consumer mediation needs can yield a prominent and persistent role for intermediaries. However, their framework focuses on B2C electronic markets, abstracts from the level and consequences of asset specificity.

Our analysis contributes to this stream by bringing a highly symbolic, physical retail setting—luxury department stores and flagships in Japan—those functions as an *analog* platform. In this context, gaishō act as human "platform operators" who curate assortments, provide cross-brand advice, and orchestrate services across categories. This insight suggests testable hypotheses for e-commerce platform research in luxury, where algorithmic recommendation systems and platform governance may play roles analogous to gaishō in reallocating dream costs between brands, platforms, and consumers.

5.7.3. Luxury Management and Dream Value (Mono-brand versus Multi-brand Store)

Luxury research has developed a rich understanding of what dream value is (Mandel, 2009; Kapferer & Bastien, 2012; Hennigs et al., 2012; Kapferer & Valette-Florence, 2016; Welté et al., 2021; Gladstone et al., 2024), how it is created (Tynan et al., 2010; Choo et al., 2012; Dion & Arnould, 2011), and how luxury value perceptions differ across contexts (Wiedmann et al., 2007; Shukla et al., 2012; Aliyev & Wagner, 2018; Tafani et al., 2024).

What this literature has said far less about are the cost structures that underpin the creation, delivery, and maintenance of dream value, and the implications of those costs for channel choice. Besides, the prevailing assumption in much luxury writing is that department stores dilute dream value relative to mono-brand flagships; the implied trajectory is toward full vertical integration, especially as brands invest more heavily in experiential assets and brand universes.

Our value–cost integrative framework adds two novel elements to this conversation by (1) introducing dream costs as a structured cost complement. This allows us to analyze how different channels not only generate different dream value profiles ($CDV\ vs. CDV'$) but also entail different cost profiles for brands and consumers; (2) reframing luxury channel choice around cost *offsets*, rather than absolute levels of dream value. The key question is not

whether flagships or department stores generate more dream value in the abstract, but whether the savings in dream costs achieved through intermediation are sufficient to compensate for the higher transaction costs of using the market.

5.8. CONCLUSION

This study explains foreign luxury brands' channel choice in Japan by unifying value creation and cost structures within a single comparative-governance model. TCE remains an effective lens—even in luxury B2C contexts, where value creation logic dominates—for examining firm boundaries, consistent with the prior work that reaffirms TCE's centrality to marketing channel strategy (John & Reve, 2015).

Our managerial implication is that brand headquarters should assess not only inter-firm transaction costs (e.g., costs of monitoring, safeguarding, and potential dilution) but also the supplier–customer costs required to stage and sustain dream value. Our evidence shows that, because customers are motivated by heterogeneous value logics, certain segments (e.g., clients who treat luxury goods as portfolio assets or who are guided by pragmatic logics) demand high-touch advising, credibility building, and cross-category curation. Where intermediaries absorb a material share of these functions, the use of an intermediated channel can minimize system-level costs even when market governance is otherwise comparatively disadvantaged. Echoing evidence on the standardization–localization dilemma in China's luxury retail market (Liu et al., 2016), this historically embedded, cost-economizing mechanism cautions against rigid "direct-only" or highly centralized doctrines—especially for entrants designing strategies for Japan.

Our studies invite future work to explore how digital platforms and algorithmic clienteling might play analogous dream-cost economizing roles in online luxury distribution, and under what conditions such platforms complement or substitute for traditional

intermediaries. We focused on physical channels and the traditional business model based on the gaishō network. We exploited this structurally transparent setting to clarify how value and costs interact. Future research should therefore test boundary conditions in digital platform contexts. Furthermore, because our analysis is static by design, longitudinal work, tracking evolving consumer emotions (e.g., Kim et al., 2016) and tracing the governance transformation over time would deepen understanding of how dream value and dream costs interact are interwoven across time and, in turn, reshape the efficient boundaries of the luxury firm.

CHAPTER 6
GENERAL CONTRIBUTIONS AND FUTURE RESEARCH

This dissertation bridges business history with theoretical perspectives, particularly those of Transaction Cost Economics (TCE), while also drawing on insights from international business, strategic management, marketing, and retailing. It aims to identify the underlying mechanisms through which firms sustain resilience amid rapidly changing institutional and industry environments. Japan provides an ideal setting for this investigation: : its institutional profile has shifted from that of an emerging economy to that of an advanced economy; it has undergone profound industrial transformation in the postwar era; and the keiretsu networks long regarded as a source of Japanese firms' competitiveness largely withered at the turn of the twenty-first century. To trace how these external shifts affect firm-level dynamics, I examined the textile, apparel and fashion sectors, one of the most longstanding, globalized, diversified, and dynamic industries. Within this context, I focus on two key non-lead actors—sōgō shōsha (highly diversified general trading companies) and department stores.

The dissertation makes empirical, methodological and theoretical contributions. First, empirically, it offers historically grounded accounts of how non-lead MNE actors have demonstrated enduring resilience in a turbulent global economy. Sōgō shōsha, deeply rooted in Meiji-era institutional traditions, repeatedly redesigned their product, location, and governance portfolios and continuously negated and reconstructed their historical identity in

anticipation of—or in response to—shifting external environments. By contrast, Japanese department stores, whose traditions date back to the Edo period, illustrate the capacity to not to change amid the deepening and widening integration of global capitalism. They have preserved the gaishō clienteling system to sustain credibility and long-term trust with clients. Together, these findings underscore the significance of a dual capacity of adaptive flexibility and structural continuity.

Second, methodologically, this dissertation contributes to the advancement of the "history-to-theory" approach (Kipping & Üsdiken, 2014; Argyres et al., 2020)—a research program still uncommon in Japan, where descriptive historiography remains dominates. Japanese business history has long stayed within a Chandlerian paradigm (Donzé & Uemura, 2025), focusing on internal factors such as hierarchies, internal organization, and firm capabilities (Abe, 2019).

Against this backdrop, the present work integrates historical contextualization with theory-driven analysis. TCE was employed as the main theoretical framework for examining firm-level decision making, and it was partially complimented by the FG paradigm to track the interaction between firm-level changes and industry level transformation. Bhaskar's Critical Realist approach functioned as our philosophical and methodological foundation in this dissertation. This approach is particularly well suited to its research purpose of identifying hidden mechanisms underlying firms' governance and strategic decision-making processes, especially because the topic—notably the activities of sōgō shōsha—is highly context-dependent and many relevant phenomena are not directly observable through conventional datasets.

Theoretically, this dissertation contributes to the operationalization of TCE in four key ways. First, it deploys TCE dynamically, tracing intertemporal changes in governance rather than treating governance choice as a static, one-off decision. Second, it extends the unit

of analysis is extended. By conceptualizing the GVC as a bundle of interdependent firm-level transactions, rather than isolated dyads, the analysis clarifies how firms co-develop governance mechanisms and manage complex interdependencies across actors. Third, it refines key TCE constructs, such as credible commitments (Williamson, 1996), by showing how these are manifested and enacted within multi-actor GVC interdependencies. Finally, the dissertation broadens TCE's scope to the B2C domain by conceptualizing transaction costs at the firm–customer interface as "dream costs," thereby extending TCE's applicability to relational and symbolic exchange contexts in luxury and retail sectors.

Looking ahead, the findings suggest several promising directions for future research. First, geopolitical realignments and supply-chain decoupling are likely to reshape governance structures and boundary decisions. Historically informed, mechanism-based analysis can help identify the conditions under which hierarchical, hybrid, or market arrangements remain strategically viable—and when re-internalization and re-externalization become preferable. Within this context, further studies of sōgō shōsha can illuminate how firms respond to shifting geo-economic landscapes, and resulting GVC configurations.

Comparative historical studies can further test the portability of the mechanisms identified here. Cross-national analysis involving Japanese sōgō shōsha, Korean chaebol trading arms, and Latin American conglomerates could deepen understanding of the governance transformation under differing institutional configurations (Lee et al., 2022). Finally, ongoing research into the transformation of sōgō shōsha from non-lead actors to potential lead MNEs will be vital for understanding their evolving governance functions.

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