Research on SOGO SHOSHA:
Origins, Establishment, and Development

— Summary of the final report from Japan Foreign Trade Council, Inc. Special Research Committee on Sogo Shosha Principles Report

October 2012
Japan Foreign Trade Council, Inc.
Summary

1. The purpose of this book is to reveal the following three points: 
   a) What is SOGO SHOSHA, and how is it different from similar overseas business categories? 
   b) What are the conditions under which SOGO SHOSHA can be established, and why are they only established in Japan? 
   c) How are SOGO SHOSHA changing?

2. SOGO SHOSHA, the general trading company, is a term which appeared in the postwar period of Japan, and Japanese people started using it from around 1955. In this book, I will not predefine SOGO SHOSHA but, for the purposes of this discussion, I consider 10 companies as SOGO SHOSHA which appeared just before the high economic growth period after the World War II: Ataka & Co., Itochu Corporation (C. Itoh & Co.), Kanematsu-Gosho Ltd., Marubeni Corporation, Mitsubishi Corporation, Mitsui & Co., Ltd., Nichimen Corporation (Nichimen Co., Ltd.), NisshoIwai Co., Ltd., Sumitomo Corporation (Sumitomo Shoji Kaisha) and Tomen Corporation (Toyo Menka Kaisha Limited). People started using the term of SHOSHA, or trading company, in the same meaning as today around the postwar period; but currently there is no definition with a consensus even in the academic world of commerce and business administration studies. As a matter of convenience, we will consider “wholesalers which mainly engage in export and import trade” as SOGO SHOSHA in this book.
3. After opening the ports to foreign vessels at the end of the Edo era, initially, trade business was mainly conducted by foreign merchants or traders from the western countries, but gradually Japanese trading companies developed and replaced them. Subsequently, in the modernization period of Japan, some trading companies as parts of family-run conglomerates called Zaibatsu, showed development like “SOGO SHOSHA” until the end of the World War II. A typical example was the old Mitsui & Co., Ltd., and it set its form as the origin of SOGO SHOSHA by the 1890s in the middle of the Meiji era. Out of the World War I boom, some general merchants and traders such as the old Mitsubishi Corporation, Suzuki & Co., Iwai & Company, Limited and Okura & Co., Ltd. grew rapidly and successfully followed the same path. During this time, giant specialized trading companies such as Japan Cotton Trading Co., Ltd., Toyo Menka Kaisha Limited, and Gosho Company also developed independently.

4. The following four points can be raised as the required conditions for setting the prototypical SOGO SHOSHA and running such establishment from Meiji until the end of the World War II.
   a) Prewar trading started at the time of opening the country under unequal treaty with western countries.
   b) Japan was a developing country which locates halfway around the world, in the Far East.
   c) Economy grew rapidly under the circumstance of encouraging new industry.
   d) The Zaibatsu, the industrial and financial business conglomerates, developed progressively.

We can note the following four points as the basic characteristics of the prototypical SOGO SHOSHA.
   a) They dealt with a variety of products.
   b) They targeted various regions for trading.
   c) They had established some kind of institutionalized modern business management system for risk management on wholesale distribution and business expansion of branches.
   d) They had strong ties with the domestic industry and invested substantially in various kinds of business.

5. Postwar trade started with one controlled by the government based on policies of the American occupation. However, private trade was gradually permitted, and operations of trading companies accelerated as free trade resumed in 1950. The SOGO SHOSHA was being formed during this time. As the old Mitsui & Co., Ltd. and the old Mitsubishi Corporation, the prewar twin jewels of the prototypical SOGO SHOSHA, were broken down by the order of dissolution from the occupation forces, at first fabric-specialized trading companies in the Kansai area started to take another form of SOGO SHOSHA through improving and restructuring non-fabric departments within the company and expanding their business domains through mergers and acquisitions. Next, steel-specialized trading companies came up and followed the same path. Following this, the subdivided Mitsui & Co., Ltd. and Mitsubishi Corporation each achieved grand mergers, where they brought together companies that had been affiliated with the former family group. Additionally, Sumitomo Shoji Kaisha (Sumitomo Corporation) began operating as a trading company of the Sumitomo Group. As such, 10-major
SOGO SHOSHA framework was established around 1960 in the beginning of the high growth period.

6. The following four points can be raised when you consider the necessary conditions which enabled and promoted the formation of the SOGO SHOSHA in the postwar period, taking into consideration the conditions for setting the prototypical SOGO SHOSHA and running such establishment in the prewar period (aforementioned “4”).
   a) Postwar trading started under the rule of the occupation forces, and underwent the transformation from controlled trade to free trade.
   b) Export items were low-technology non-differentiated products, and export destinations had different commercial practices.
   c) Economy recovered and grew rapidly.
   d) The relationship within corporate groups did not break down completely and went through postwar reforms.

The following can be pointed out as the basic characteristics of SOGO SHOSHA.
   a) There are various types of trading products.
   b) Fields of trade range from domestic commerce, export and import trade to triangular trade.
   c) Trade volume is enormous in a transaction.
   d) They function as organizer for the industries through provision of products and market development.
   e) They have many subsidiaries and affiliates, and have characteristics like a holding company.
   f) They have modern business management system.

7. When you look at the ranking of trading companies in the world today according to Forbes Global 2000, 11 Japanese trading companies are counted in the top 21 including five Japanese SOGO SHOSHA which dominate the top five (2010 version). Obviously, Japanese SOGO SHOSHA show overwhelming presence in this category. There are 18 companies from Asia including four South Korean companies, and only three companies come from Europe. There are not many giant trading companies in the western world.

8. In mid-1970s, one after another developing countries at the time such as South Korea developed measures to foster general trading companies like SOGO SHOSHA. As a result, general trading companies grew rapidly in South Korea and heavily contributed to its economic development. They have similarities to Japanese SOGO SHOSHA, but also have many differences such as that they couldn’t get out of the role of contact center they played for the chaebol, or the Korean family-run conglomerates, and thus had low import rates in practice. There seems to be similar business entities in other developing countries, but their scales cannot compare with Korean trading companies. However, it is possible that large scale business entities like SOGO SHOSHA may develop in emerging countries such as China in the future. Furthermore, in 1980s the U.S. tried to foster export trading companies as part of measures to dissolve trading deficit, but in vain.

9. When you look back at the history of western developed countries, multilateral trading companies with diversified product
lines similar to Japanese SOGO SHOSHA operated actively in the U.K. from the prewar period and also survived after the World War II until 1970-80s. As a result of being forced by the capital market to focus on businesses with high profitability, however, they were forced to end their development as general trading company. In Germany, trading companies were responsible for exports until around 1910s, but subsequently larger manufacturers undertook to export products directly, and the framework transitioned to one where trading companies took up products from small- and medium-sized companies for export to developing countries. During this time, there were no business entities which developed like SOGO SHOSHA. In the U.S., the role of exports in economic development was small to begin with, and they didn’t have strong interests in marketing for overseas market, hence operations of trading companies were in low gear.

10. The following four points can be noted as we sort out the characteristics of Japanese SOGO SHOSHA when compared to past British multilateral trading companies as well as American or German trading companies.
   a) Exports had significant meaning in the takeoff of the economy and played a strategic role upon request by the government.
   b) Highly educated people assumed and carried out responsibility for top management all the way to bottom level and had established modern business management system from the prewar period.
   c) In the prewar period and the beginning of the postwar period, the product line was mainly low-technology non-differentiated products.
   d) The relationship within the Zaibatsu (pre-war period) and corporate groups (post-war period) ran deep and strong so that they could be sustained by domestic industry.

11. After the establishment of 10-major SOGO SHOSHA framework, the future of profit structure centered on trade (exports and imports, domestic, and triangular traditional trade) did not give SOGO SHOSHA a bright prospect. When the high growth ended, as Japanese economy faced various problems and difficulties, SOGO SHOSHA responded and transformed their business structure. In the midst, a organizational change gradually occurred where new investments in enterprises pursued the aim to increase return on investment whereas existing domestic and foreign investments in enterprises were mainly used for the purpose of securing trade commercial rights.

12. During this time, as SOGO SHOSHA faced the occurrence of crises and new risks, they enhanced risk management system, strengthened corporate governance, and conducted depreciation of non-performing or unprofitable assets which were found in the aftermath of the bubble economy. However, those who could not perform as such on their own were driven out of business, and mergers and realignments took place around 2000. Today, SOGO SHOSHA are the seven companies: Itochu Corporation, Marubeni Corporation, Mitsubishi Corporation, Mitsui & Co., Ltd., Sojitz Corporation, Sumitomo Corporation and Toyota Tsusho Corporation. They currently enjoy unprecedented good performance, as natural resources-related investment income increased among others.
13. The organizational change after the establishment of 10-major SOGO SHOSHA framework (aforementioned “11”) is often considered as “transformation into enterprise investment companies”. Contemporary SOGO SHOSHA not only carry many different consolidated subsidiaries but coordinate them systematically and operate as an entire group in order to foray into some manufacturing businesses and service businesses. On the other hand, what also definitely contributed to earnings was profit from investment in enterprises where they didn’t retain management rights over invested companies. As you can see, the organizational change of contemporary SOGO SHOSHA has two sides which are “foray into some manufacturing businesses and service businesses through consolidated subsidiaries” and “transformation into enterprise investment companies”.

14. These two movements are both supported by investment in enterprises, but they are conducted in forms such as:
   a) Splitting up and subsidizing existing business of the main body;
   b) Starting up new subsidiary; and
   c) Taking a stake in existing corporation.

In SOGO SHOSHA, when investing in enterprises, management strategy of “divestiture and recycling of assets” is adopted, by which they control the entirety of a group appropriately by increasing consolidated subsidiaries and affiliates through new investments, as well as selling them and withdrawing from unprofitable business. To secure interests in overseas natural resources-related investments, partner selection proves to be very important. Furthermore, value chain strategy is gaining prominent attention which expands opportunities to realize various earnings models at every stage of the field from upstream to downstream by utilizing commercial rights in existing business fields.

15. It is difficult to express in one word current SOGO SHOSHA which experienced two structural changes as we saw in “13”, but I will take the liberty of saying that it is a “General Enterprise Management and Enterprise Investment Company”. If I can make a slight note, it should be added that:
   a) It is conducted by investment from the main body through consolidated management.
   b) Trade business plays a key role as the foundation of business operation and enterprise investment.

The following three points can be pointed out to explain how SOGO SHOSHA differs from simple and common investment companies (investment trust and hedge fund).
   a) It runs its own business and has the function of business formation.
   b) It maintains trade business as its foundation of operation.
   c) It has discerning ability for partner selection.

We can raise the following two points as the positive characteristics of SOGO SHOSHA:
   a) Optimism to face difficulties constructively and “ability to adapt”, and
   b) Clear awareness of its own mission which is to respond to national request and customer’s needs.

16. As we reconsider the conditions for setting of SOGO SHOSHA using “4”, “6”, and “10” as reference, the following four points
can be raised:
 a) Necessity for national policy,
 b) Export structure centered on low-technology non-differentiated products and export destination with different commercial practices,
 c) Rapid expansion of the economy, and
 d) Deep involvement with domestic industry.
 However, these conditions are all becoming vague. On the other hand, emergence of the following three factors can be noted for existence of SOGO SHOSHA, and these are becoming rather stronger.
 a) Risk tolerance through diversified business fields,
 b) Ability to discover source of earnings and realize huge profits by engaging in many business opportunities within one industry sector, and
 c) Ability to discover needs and seeds in order to commercialize a new product and service through information collection and analytical ability formed by being involved in business opportunities across many business fields.
 These characteristics can be considered as being “general” in a new sense.

17. As we look at the future of current SOGO SHOSHA as a “General Enterprise Management and Enterprise Investment Company”, the following four directions can be noted:
 a) Strengthening a “General Enterprise Management and Enterprise Investment Company”;
 b) Strengthening overseas business development;
 c) Maintaining trade as its foundation business; and
 d) Maintaining business relationship with domestic industry.
 Points a) and c) as well as Points b) and d) both have conflicting characteristics. SOGO SHOSHA have taken the course of Points a) and b) up to this day. Although, there is no question that the directions of Points c) and d) characterize current Japanese SOGO SHOSHA, and today SOGO SHOSHA exist on such balance. As we confirmed earlier, it is not feasible for existence of SOGO SHOSHA to be specific drastically and give up “general” in the new sense. It is possible that each company differentiates into a different form of management body in the future depending on what it focuses on, but as SOGO SHOSHA face difficulties constructively and have the “ability to adapt”, it is highly likely that SOGO SHOSHA will continue to develop as a unique management body in the world.

18. Furthermore, SOGO SHOSHA will be needed in the years ahead in the following two points. That is:
 a) to be a step ahead of potential needs of the market and show to the industries in Japan and the other countries while market-oriented system of world economy progresses; and
 b) to be the one to discover and bear true national interest while globalization of politics and economy progresses.
Research on SOGO SHOSHA: 
Origins, Establishment, and Development

A Report of the JFTC Special Research Committee 
on Sogo Shosha Principles Report
Author: Professor Takayuki Tanaka
of the Faculty of Economics, Senhu University

This is published by Japan Foreign Trade Council, Inc.

All rights reserved.
Copyright © 2012 by Japan Foreign Trade Council, Inc.

No part of this publication may be reproduced in any form or by any means, without the prior written permission of the publisher.

Japan Foreign Trade Council, Inc. www.jftc.or.jp