

## When NOT to Learn: Misguided Teaching in the DCX-MMC Strategic Alliance (Part II)

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Keywords: DaimlerChrysler Corporation (DCX), Mitsubishi Motors Corporation (MMC), equity alliance, learning alliance, inter-firm learning, organizational capabilities

*Special Introductory Note: This article is the second installment of a two-part academic paper. Part I was published in 2016, also in *Yokohama Business Review* (Yokohama Keiei Kenkyu, Volume 37, Issue 1, pp. 55-72). At the time, MMC was facing a scandal-related severe management crisis and was finalizing a strategic alliance whereby Nissan Motors acquired a 33.4% equity stake in the company. Buoyed by the successful completion of this alliance and the managerial assistance received from Nissan, the financial and market positions of MMC stabilized. Part II presented here discusses the theoretical and practical implications of the DCX-MMC case.*

### 4. Discussion

Using the teaching/learning framework introduced in the literature review presented in Section 2, this section analyzes the strategic alliance (presented in Section 3) between DaimlerChrysler (DCX) and Mitsubishi Motors Corporation (MMC) that existed from 2000 to 2005. The paper closes with Section 5, which contains the conclusions and managerial implications from the case. First, the following two research questions are examined:

- (1) Was the relationship between these two automakers a learning alliance?
- (2) Did any teaching occur in the alliance and, if so, how and why did it occur?

As an initial step to answering the first research question, the paper explains why the equity-based relationship that existed between DCX and MMC can be considered an alliance and not a takeover. Then, using Hamel's (1991) concepts of intent, transparency, and receptivity, the paper shows that while the strategic alliance was indeed a learning alliance, it was one with limited reciprocity of learning and therefore weak in what may be considered a fundamental characteristic of a healthy learning alliance.

After examining learning in the DCX-MMC alliance, the paper probes the teaching (i.e., actively facilitating another's learning) that occurred in the alliance and finds that misunderstandings caused much misguided teaching. However, it is shown that sufficient independence at MMC and the automaker's

confidence in its own organizational capabilities and managerial strengths prevented much misguided learning from happening. This lack of learning was a humbling result for both sides, yet in the end it allowed each company to emerge from the alliance better able to thrive on its own. As such, it is reasonable to state that something good did come out of what was by all measures a bad alliance.

#### 4.1 Was the DCX-MMC relationship a learning alliance?

In the real world, the dividing line between an alliance (i.e., an inter-firm relationship) and a takeover (i.e., an intra-firm relationship) can at times be rather blurry. The DCX-MMC relationship may be considered a case in point. Due to certain rights granted under Japanese commercial law to a shareholder with more than a 33.3% ownership stake, acquiring equity that exceeds this threshold will give the owner effective control of a Japanese company, without having to cross the psychologically and legally significant line of acquiring a majority ownership position (Heller, 2003). Obtaining only a minority stake, even if it is in effect a controlling stake, can produce positive motivational benefits in the firm that is acquired. It can allow the acquired company to be perceived as independent and in control of its own capability building (Heller, Mercer, and Fujimoto., 2006) with a distinct organizational identity (Albert and Whetten, 1985).

In 2000, DCX obtained a controlling equity stake of 33.4% in MMC and dispatched more than twenty executives and managers to its alliance partner. The leader of this group of dispatchees was Rolf Eckrodt, who began as COO but was later promoted to CEO of MMC. Throughout the period during which the two companies were allied they did not merge any of their operations or brands. Instead they related to each other as separate and distinct entities with independent decision-making bodies, which placed real limits on DCX's control over MMC (Begley and Donnolly, 2011), limits that went well beyond those that are typically found in a headquarter-subsidiary relationship. As such, it is reasonable to consider the DCX-MMC relationship to be an alliance and not a full takeover.

When the DCX-MMC alliance was announced in March 2000, the complementary geographical and market segment positions of the companies were presented as the principal rationale for the agreement. However, just one month after the announcement of the alliance, MMC fell into an acute scandal-induced crisis due to its cover-ups of quality defects in its vehicles. DCX took some time to negotiate a decrease of 10% in the purchase price of the equity stake in MMC that it had contractually agreed to acquire, because of the lower market valuation of MMC following the scandal.

On the one hand, it can be argued that DCX showed trust toward MMC by giving the company time to put its ethical issues in order on its own. Yet, on the other hand, while rationally justified in negotiating down the purchase price, DCX acted in stark contrast to what had happened just two years earlier in the Renault-Nissan alliance.<sup>1</sup> With so many parallels between the two cases, the decision by DCX to engage in such seemingly opportunistic behavior is, at a minimum, puzzling.

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<sup>1</sup> Renault decided not to take advantage of an opportunity to lower its initial offer made in 1998 to acquire a controlling equity stake in Nissan. Renault made its offer to Nissan when DCX and Ford were both also considering making their own offers to Nissan. Subsequently, these two other firms dropped out of the bidding for Nissan. At this point, Renault knew it was well within its rights to resubmit a lower offer. However, Louis Schweitzer, who was the head of Renault at the time, has stated that he chose not to lower Renault's offer because he knew that such an action would destroy the hard-won trust that had been built up at Nissan toward Renault (Ghosn, 2002).

The scandal at MMC created an opportunity to improve quality at MMC through learning from DCX, a firm with a reputation for industry-leading quality through its Mercedes-Benz brand. Upper management at MMC embraced this opportunity. Yet, it took some time for a reciprocal learning orientation to take root at DCX. It was not until more than three years after the DCX-MMC alliance began, in November 2003, that a quote from an executive at DCX appeared in any major English language media outlet that mentioned the opportunity to learn production efficiency and flexibility from MMC.

Prior to 2003 there do not seem to be any other prominent instances at DCX of the existence of such a recognition or intent to learn from MMC. Thus, although there was a long time-lag and the breath of such an intent within DCX was rather limited, the intention to learn from an alliance partner can be found on both sides of this case. Thus, returning to Hamel (1991), we find that the first characteristic of a healthy learning alliance, the *mutual intention to learn* from a partner, was present in the DCX-MMC alliance.

The nature of the alliance with its controlling stake and large number of dispatchees at both executive and middle managerial levels that were sent into MMC would seem to guarantee DCX sufficient access, or following Hamel (1991), transparency into the managerial systems at MMC. Such transparency could explain the apparent evolution of DCX's understanding of the organizational capabilities at MMC. Upon his arrival at MMC, Eckrodt said that there was the need for more production flexibility at MMC. Over time DCX better understood the high level of production flexibility and high manufacturing productivity that had long existed at MMC and the opportunity for DCX to learn these organizational capabilities from its partner.

There was less transparency for MMC into DCX, since MMC had no equity stake in DCX and therefore a limited basis from which to obtain formal access to DCX. Nevertheless, there was some movement of MMC personnel to DCX through project-based cooperation. A severe lack of organizational slack at MMC probably also limited increasing DCX's transparency. The perpetually strained human resources at MMC had to deal with a severe organizational crisis at the start of the alliance. In similar alliances at this time (e.g., Ford-Mazda and Renault-Nissan), the Japanese side's transparency into its Western partner also increased over time (Heller, 2003). Thus, while the degree differed, it can be concluded that there was at least some level of *transparency at both DCX and MMC*, although it was rather unbalanced with DCX being much more able to see into MMC than vice versa.

The receptivity, or ability, of the two companies to learn from each other is addressed next. The concept of relative absorptive capacity (Lane and Lubatkin, 1998) is used to examine this point. Did the alliance partners share commonalities in their knowledge bases (including basic skills, shared language, ways of thinking, etc.), organizational structures, and dominant logics that could help them learn from each other?

First, the history of links between the companies is examined. Although there were some cooperative ties between Daimler Benz and Mitsubishi in the 1990s, they never developed into major initiatives. Chrysler, on the other hand, had a long history of deep cooperation with Mitsubishi, which implies shared knowledge bases at the companies. The fact that one of the two top lieutenants of Eckrodt at MMC came from Chrysler, would seem to be an attempt to build on the existing relational capital between the two organizations.

Yet, it seems reasonable to infer that the rapid succession of departures from DCX of executives who

hailed from the former Chrysler organization severely limited the extent to which the existing relational capital could be exploited in the alliance. As argued in Heller (2001), personnel turnover erodes the ability of firms to use their alliance relationships to aid learning from a partner and obtain the benefits of teaching. When key personnel leave the company it prevents tapping the long-term inter-firm ties such people possess.

Although negatively impacted by the exodus of Chrysler's top managers from DCX, it is reasonable to expect that there would still remain a relatively high degree of shared dominant logics at Chrysler and MMC, since both sold most of their vehicles in the mass market. However, the same cannot be said for the Mercedes-Benz passenger car division, which sells its light vehicles in the premium market. Mercer's (2001) analysis of five automotive M&As in the 1980s suggests that premium and mass-market automakers have fundamentally different approaches to the auto business, which makes it difficult for them to work together and cooperate successfully at least in the short- and medium terms.

In contrast with its passenger car division, Mercedes-Benz' truck division shared dominant logics with MMC's truck business. However, the latter had to remain untouched from the announcement of the DCX-MMC alliance in March 2000 until June 2001 when MMC's preexisting alliance with Volvo Trucks was dissolved. Thus, this potential high receptivity between DCX and MMC was initially untapped. Nevertheless, this potential seems to have been quickly realized, especially from January 2003 when MMC spun off its truck and bus division to become a separate company, Mitsubishi Fuso Truck and Bus Corp.

Overall, with regards to mutual learning, the two companies would seem to have possessed *partial receptivity in the car business*, which contrasts with *high receptivity in the truck business*. This asymmetry in receptivity would seem to have contributed to the existence of only limited reciprocity of learning in contrast to what is commonly seen in a healthy learning alliance. While the push for MMC to learn from DCX has been clearly established from the beginning of the alliance, the alliance ended before the DCX side began to pursue learning from MMC in earnest. The need for an additional financial injection and a second major scandal were apparently too much for DCX to accept, especially with the company having successfully acquired a majority stake in Mitsubishi's truck and bus company from March 2003.

To sum up, the first research question may be answered in the affirmative that the DCX-MMC was indeed a learning alliance, albeit heavily weighted to learning on the MMC side. A clear learning intent, high transparency, and some receptivity on the MMC side has been established. On the DCX side there appears to have been limited intent, limited transparency, and limited receptivity, with both intent and receptivity increasing over time. Thus, reciprocity of learning in the alliance was not as high as in similar learning alliances between Western and Japanese automakers at the time (Heller, Mercer, and Fujimoto, 2006).

## 4.2 Teaching in the alliance

Next, the second part of this discussion examines the second research question, which addresses the issue of teaching in the alliance. What teaching occurred in the alliance? If teaching existed, how and why did this teaching occur? Of particular attention will be an inquiry into whether teaching was done based on

correct evaluation of the relative strengths and weaknesses of the alliance partners.

The comments by Eckrodt in January 2001 at his introductory address when he began his tenure at MMC shows the starting point of his (and by extension DCX's) view of the reform needed at MMC. It is highly surprising that nine months after the alliance was agreed upon, a time during which MMC and its stakeholders suffered greatly from the aftereffects of its major scandal, corporate ethics was not mentioned as a specific target of the reform proposed by Eckrodt.

At the public presentations of MMC's Turnaround Plan in early 2001, which was presented first in an outline form in February and later as full plan in March, reforms to corporate culture, which can be understood as a euphemism for ethical reform, were covered by Takashi Sonobe, the president of MMC, not Eckrodt, the COO. While related issues were covered by Eckrodt, such as changes for streamlining decision making and improving clarity of managerial responsibilities, it seems that corporate ethics was not a focus of teaching by the managerial team dispatched from DCX. Instead the matter seems to have been intentionally left to the Japanese management team.

The primary focus of the post-alliance changes made at MMC centered on addressing quality issues through the introduction of the quality-gate approach used at Mercedes-Benz. The teaching by DCX related to improving quality does not seem to have been made with any clear understanding of the fundamental approach of Japanese management in a manufacturing firm, where quality is built into a product throughout the production process (Heller and Fujimoto, 2017). In other words, rather than ensuring quality through inspections at specific intervals in a production process, every work station in a production line and every step in the development process can be considered a quality gate. In the mass-market passenger car business, the inspection-based method taught by DCX conflicted with the shorter lead-times and higher productivity requirements faced by MMC.

Mercedes-Benz' methodical and deliberate new product development processes are highly regarded in the industry. Such an approach has served the brand well over the company's long and storied history. However, unlike Daimler, which sells in the luxury segment under the Mercedes and Smart brands, MMC sells its vehicles in the mass-market segment of the automobile industry. MMC's success and the strong shop-floor organizational capabilities of its plants has been established in the literature (Orihashi 2000, 2007; Orihashi and Fujimoto, 2003).

By necessity, MMC's plants in Japan had industry-leading flexibility, since the company's full line-up of vehicles had to be produced in its small number of plants meaning that each model had low production volume (Orihashi 2008). Perennially low production volumes meant that the company's resources were continually stretched very thin. On the one hand, it seems this chronic resource shortage contributed to a pride in product development at MMC in being able to get the job done, including introducing critically acclaimed vehicles, like the Mitsubishi Lancer Evolution series, and numerous new technologies, such as Active Yaw Control.

On the other hand, resource scarcity in product development may have caused the company to rely more heavily than other automakers on its plants and even its service providers (dealers) to cover any product development shortcomings. A reactive corporate culture seems to have developed where problem solving by attacking root causes lagged problem solving through workarounds and where recall cover-ups could become a chronic issue.

This line of reasoning strongly suggests that the problem at MMC was not in essence strictly a quality issue. Quality problems, recalls, and even a reluctance on the part of automakers to issue recalls have long been an unfortunate reality in much of the industry throughout the world. MMC's serious problem was its systematic covering up of quality issues that should have triggered vehicle recalls. Thus, the problem at MMC was primarily ethical not technical.

For decades prior to the alliance with DCX, a culture had been allowed to take hold inside MMC that permitted hiding issues and addressing them out of sight. Without appropriate checks and balances within the company, advocacy for the user became slanted, allowing problems to be solved secretly rather than openly. After the alliance with DCX fell apart, the new president Osamu Masuko aggressively addressed this very issue. However, the emissions scandal of 2016-17 showed that the process had not yet been finished. This latest scandal suggests that decades of bad corporate habits may require decades of diligent pursuit to completely root out the problem.

The issue at MMC that urgently needed to be addressed was insufficient ethical integrity. Product development must have been complicit in the recall cover-ups to at least some degree, as it is difficult to see how the product development organization could not have been involved in or at least made aware of product remedies that dealers were implementing. Product development, or at least some set of the people in product development, were likely called upon to engineer solutions to the products that failed in the market. Improved internal governance, especially in product development, was the area where reform, and DCX's teaching, was most needed.

Eckrodt's push to increase the power of styling and marketing by elevating their status and bringing in an outside executive may have helped to increase checks and balances within the company. However, such a purpose was not given as a reason for the moves. In fact, Eckrodt clearly stated that past issues were "the past" and would not be addressed. In addition to giving DCX time to renegotiate its purchase price, the long period from April to December of 2000 may have been given to MMC as a time for the company to get its house in order, prior to Eckrodt and his team's official start inside MMC in January 2001.

At the press conference introducing Eckrodt in January 2001, the fact that it was MMC's president Takashi Sonobe, not Eckrodt, who mentioned the need for ongoing reform of MMC's corporate culture suggests that DCX had largely delegated this task to the management team of MMC proper. Eckrodt emphasized that the partnership would be forward looking. Yet, it may have been overly optimistic to think that the root causes of a cover-up scandal that had lasted for more than twenty years could be fixed in less than a year.<sup>2</sup>

Precisely due to the recall cover-ups having begun so many years earlier, the sources of such a deep-seated problem were what needed to be addressed. Eckrodt emphasized that processes to prevent any re-occurrence would be put in place. While it is unclear what precisely Eckrodt included within the word processes, a process is typically directed at influencing behaviors. To change wrong thinking, changes must be made to the higher-order organizing principles that underlie corporate processes (Kogut and Zander, 1992).

The thinking at MMC that led to the recall cover-up scandals may have had its roots in the

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<sup>2</sup> Even after ten-years of reform at MMC since the DCX-MMC alliance was dissolved, the 2016 scandal at MMC clearly shows that systemic unethical behavior at MMC persisted.

company's post-war history of independent units. MMC's Japanese passenger vehicle manufacturing facilities and R&D Center were all located far away (at least 300 km) from MMC's Tokyo headquarters, which was near only the Fuso truck and bus R&D Center and truck plant in Kawasaki, a city next to Tokyo. MMC's headquarters seems to have been unable to exercise enough control over the company's productive facilities, which led to MMC repeating its 2001 recall cover-up scandal again in 2004 at the Mitsubishi Fuso Truck and Bus Corporation, with the second scandal being the trigger that ultimately precipitated the complete dissolution of the DCX-MMC alliance in 2005.

Following the dissolution of the alliance, Mitsubishi Group stepped in and Osamu Masuko was dispatched to MMC from Mitsubishi Corporation, the Group's trading company. Masuko sought to eliminate the root causes of the decades long acceptance of lying to consumers and the government. Post-2005 MMC created an ethical advisory committee to find the root cause of the systemic cover-ups. This committee pushed various broad-reaching initiatives within MMC that seem to have produced significant organizational change in the company, although the 2016 scandal reveals that their work was insufficient.

Resource sharing between DCX and MMC was also targeted in the Turnaround Plan. This decision may be viewed as DCX teaching strategic decision-making to MMC. However, the initial aims and the subsequent results were rather modest, namely one small car platform shared between Mitsubishi and Smart, and one small engine shared by Mitsubishi, Smart, and the Chrysler brands. Until it was dissolved in June 2001, the pre-existing alliance between MMC and Volvo Trucks prevented the expansion of resource sharing into the area where DCX and MMC had the most receptivity to each other, namely large trucks.

Ultimately DCX's decision to break off the alliance with MMC to focus on its majority-stake acquisition of MMC's truck business can be seen as a natural outcome. At the same time, it is precisely this good fit in the truck business that leads an observer to question the authenticity of DCX's denial in 2000 that the alliance with MMC was not about the truck business. This denial allowed DCX and MMC to prevent AB Volvo from exercising the rights granted by its 5% equity position to try to prevent the DCX-MMC alliance. However convenient the denial, it certainly constituted ethically borderline behavior.

The ethics of Daimler's acquisition of Chrysler in 1998 was also widely questioned (Vlasic and Bradley, 2000). Faced with such questions about the ethics of its own behavior, it is understandable that DCX took a hands-off approach to ethical reform at MMC. However, since it turned out that MMC was not able to address its ethical shortcomings on its own, this lack of teaching from its partner in this critical area meant that the root cause of MMC's quality problems were not sufficiently addressed, with the ultimate result being the alliance's dramatic failure.

The above analysis of this case shows that DCX incorrectly evaluated its partner's operational capability strengths and sought to teach MMC a quality-gate system that did not fit with the competitive market segments in which the Mitsubishi brand is sold. It is fortunate that MMC did not learn the long lead-time and high-cost product development practices of DCX, which would have severely lowered MMC's competitiveness in the mass-market product segment. Middle-level management at MMC should be praised for not learning what would have made the company weaker.

## 5. Conclusion

In closing, this section draws conclusions from the DCX-MMC case that contribute to the academic literature and presents implications for practitioners who face the difficult task of managing a learning alliance.

Was the DCX-MMC alliance truly the epic failure it has been made out to be? Clearly the alliance did not last long and neither side seemed to learn much from the other. It also destroyed capital for DCX shareholders, and MMC had to cede control and most of the ownership of its truck and bus division to DCX. The alliance does seem like it can be called nothing but a failure. But how bad a failure was it?

First, it must be noted that there were no bankruptcies. Organizationally both sides survived, and both companies even went on to outperform vis-à-vis their pre-alliance positions. At DCX, Schrempf was ousted ending his overly aggressive control of the company, with the fiasco at MMC seemingly hastening his demise. Meanwhile, DCX obtained an 85% equity stake in Mitsubishi Fuso, a heavy-duty truck manufacturer with a strong position in the important growth region of Southeast Asia and in smaller truck segments based on its Canter line. As of 2017, Fuso's sales make up 40% of Daimler's commercial truck sales.

By exiting the commercial truck and bus segment, MMC finally significantly narrowed its vehicle line-up to allow the company to focus its limited but top-class resources on achieving a leading position in newly emerging electric vehicle and plug-in hybrid vehicle segments. MMC was also fully folded into the Mitsubishi Group, where it has prospered. More recently, the company joined the Renault-Nissan alliance, with the new three-way partnership passing the Toyota group to become the second largest auto manufacturing group in the world in 2017, after the VW group.

The DCX-MMC alliance was never intended as a pure learning alliance, where both sides learn from the relative strengths of each other. Learning was thrust on MMC due to its egregious scandal. However, DCX's diagnosis of the learning that was needed at MMC was largely off the mark. Faced with very different competitive dynamics in the mass-market segment, MMC did not need DCX to teach it a slow, stage-gate quality improvement system, but rather needed to return to the basics of Japanese operations management, namely integrated and front-loaded problem solving in product development, and building-in quality at each work station on the production line (Heller and Fujimoto, 2017).

Thus, the alliance should not be considered an epic failure, though it could very well have been one if people at MMC had learned what DCX tried to teach them. Although most corporate executives may not like to hear it or admit it, front-line and middle managers will be the ones who determine if meaningful learning actually happens in an organization or not. Even in cases where the envisioned inter-firm learning in a learning alliance is necessary and timely, the variety of viewpoints that will naturally be found in a healthy organization make it unlikely that everyone will easily see the need or fortuitous timing. Rarely will it make sense for executives to shirk efforts to build the case for and persuade rank and file members of the rationale for learning from an alliance partner.

The MMC-DCX case reminds us that even if executives get it wrong, it is possible for the rest of the people in a company to be a good inhibitor of bad learning. It is the hope of the author that the failed DCX-MMC alliance will serve to help executives to be less cavalier about trying to impose learning on an alliance partner, without first making sure that the learning is really what is needed and that the timing is

right for it. It seems reasonable to expect that widespread efforts to build the case in alliance partners for both teaching and learning can help prevent the type misguided teaching that was found in the DCX-MMC case.

This paper has contributed to the academic literature by introducing a teaching framework for analyzing learning alliances. Using a perspective that incorporates teaching allows for deeper understanding of how learning can be successfully managed in an alliance. In particular, the framework emphasizes the importance of correct evaluation of the organizational capabilities of alliance partner. The analysis of a failure case also provided new insights into how ethical issues can inhibit successful alliance management.

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