Nomura Institute of Capital Markets Research

NOMURA

Financial Conglomerates in Japan

Is Japan heading for a universal banking system?

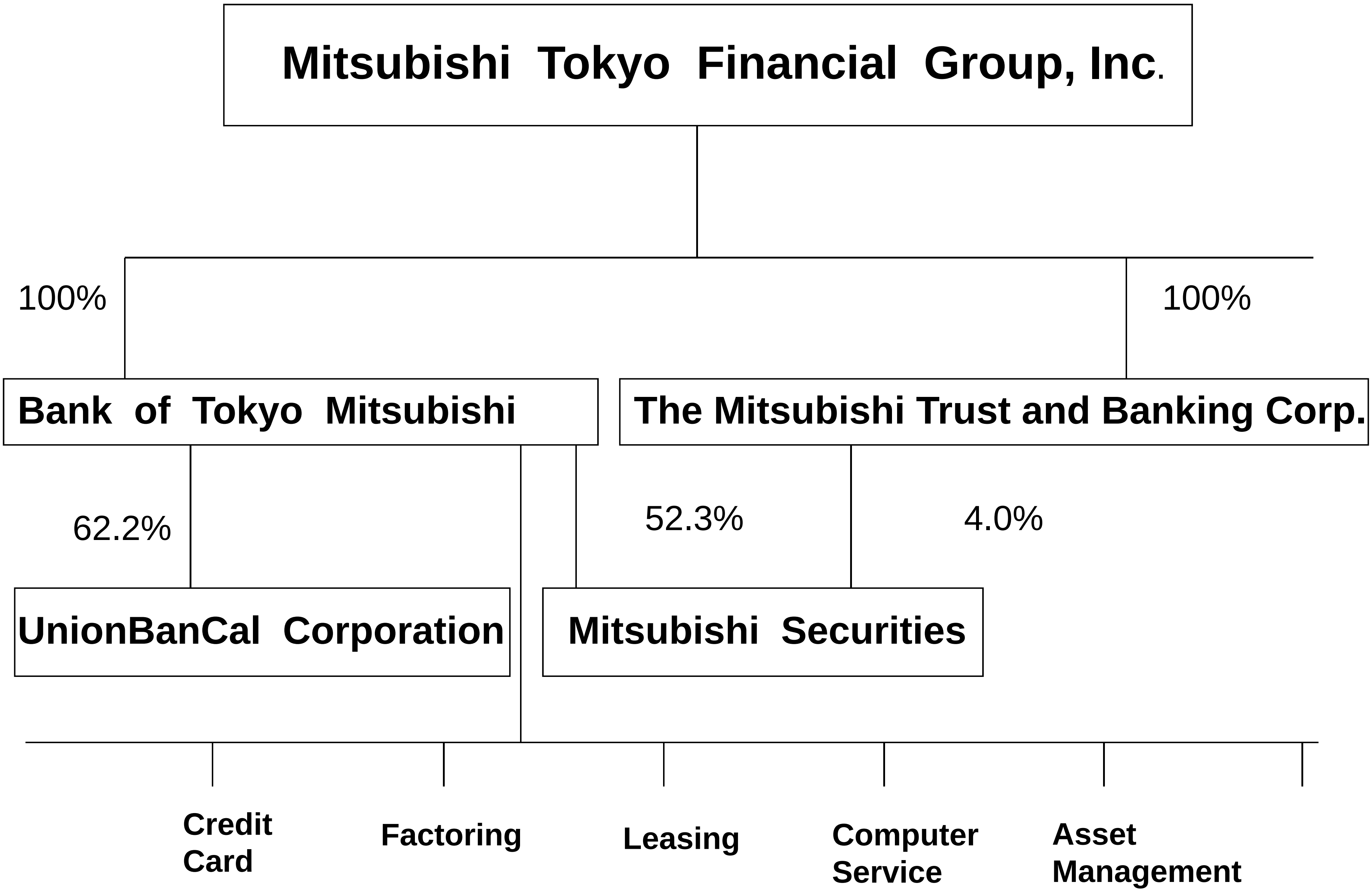
Nomura Institute of Capital Markets Research

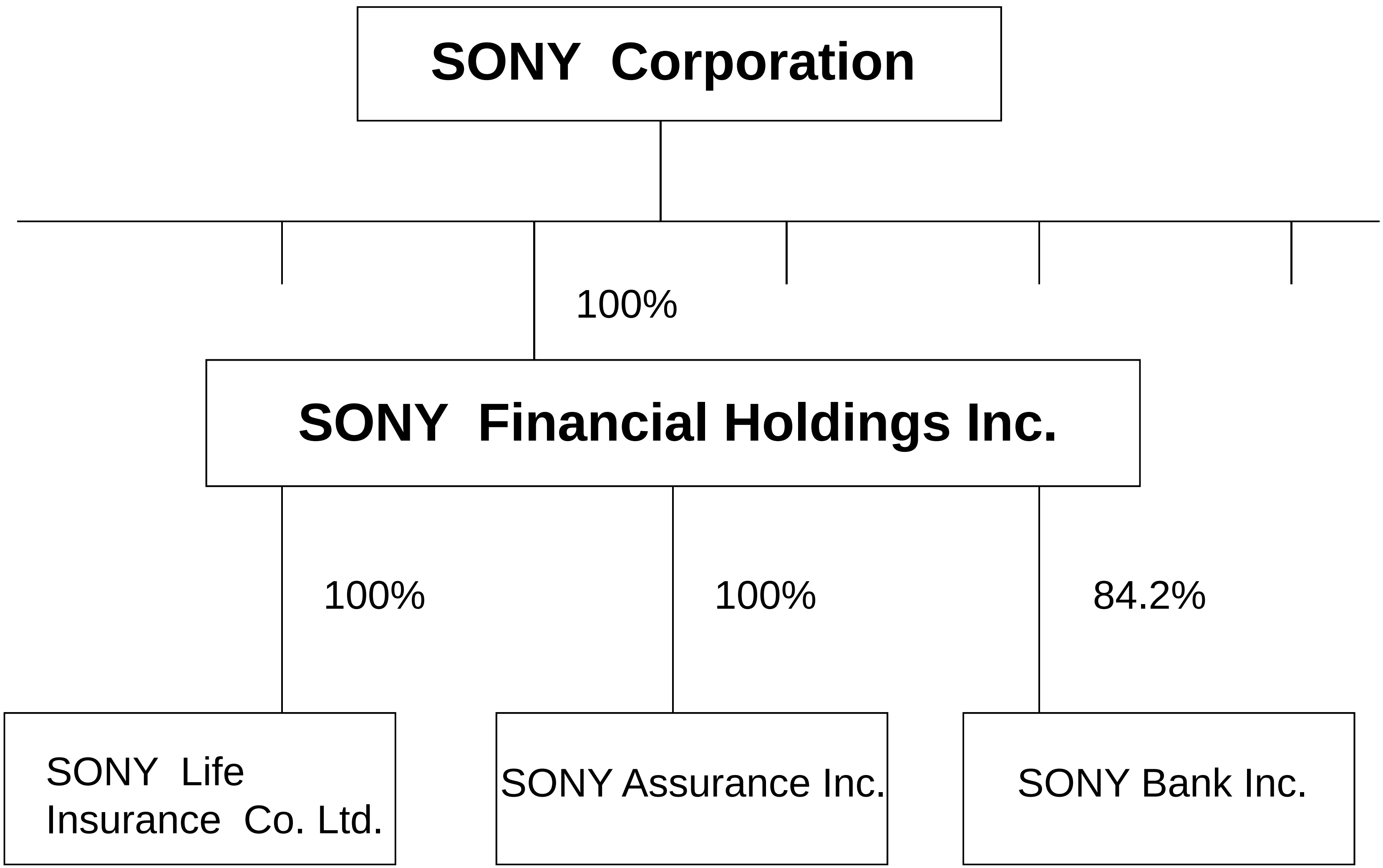
Yasuyuki Fuchita

October 5, 2004

From Separation to Conglomeration- The case in Japan

- 1948: Securities and Exchange Act = GS type regime
- 1983:Banks are allowed to conduct brokerage business of public securities
- 1984: Banks are allowed to conduct dealing business of public securities
- 1992: Financial System Reform Act = Allow entering into other financial business through subsidiaries. Banks started establishing securities subsidiaries in 1993(At first, equity related businesses were banned.)
- 1996: Japanese “Big Bang”
- 1997: Banks’ securities subsidiaries are allowed equity related businesses
- 1998: Establishment of Financial Holding Company is allowed. Banks are allowed to sell mutual funds
- 2004(December) : Banks can sell securities through tie-ups with securities brokers


Mitsubishi Tokyo Financial Group, Inc.
100%
100%
Bank of Tokyo Mitsubishi
The Mitsubishi Trust and Banking Corp.
62.2%
52.3%
4.0%
UnionBanCal Corporation
Mitsubishi Securities
Credit Card
Factoring
Leasing
Computer Service
Asset Management


SONY Corporation
100%
SONY Financial Holdings Inc.
100%
100%
84.2%
SONY Life Insurance Co. Ltd.
SONY Assurance Inc.
SONY Bank Inc.

How Japanese system is different from the U.S. system under GLB?

- FHC = not so strict requirements for being well capitalized and well managed
- Banks are not allowed to sell major insurance products (phased deregulations are expected)
- Banks and FHC can be fully owned by commercial companies
- Banks can sell mutual funds
- Banks can sell corporate securities through tie-ups with securities brokers starting Dec. 2004
- Banks can introduce potential clients to investment banks and receive fees

Two characteristics of Japanese system

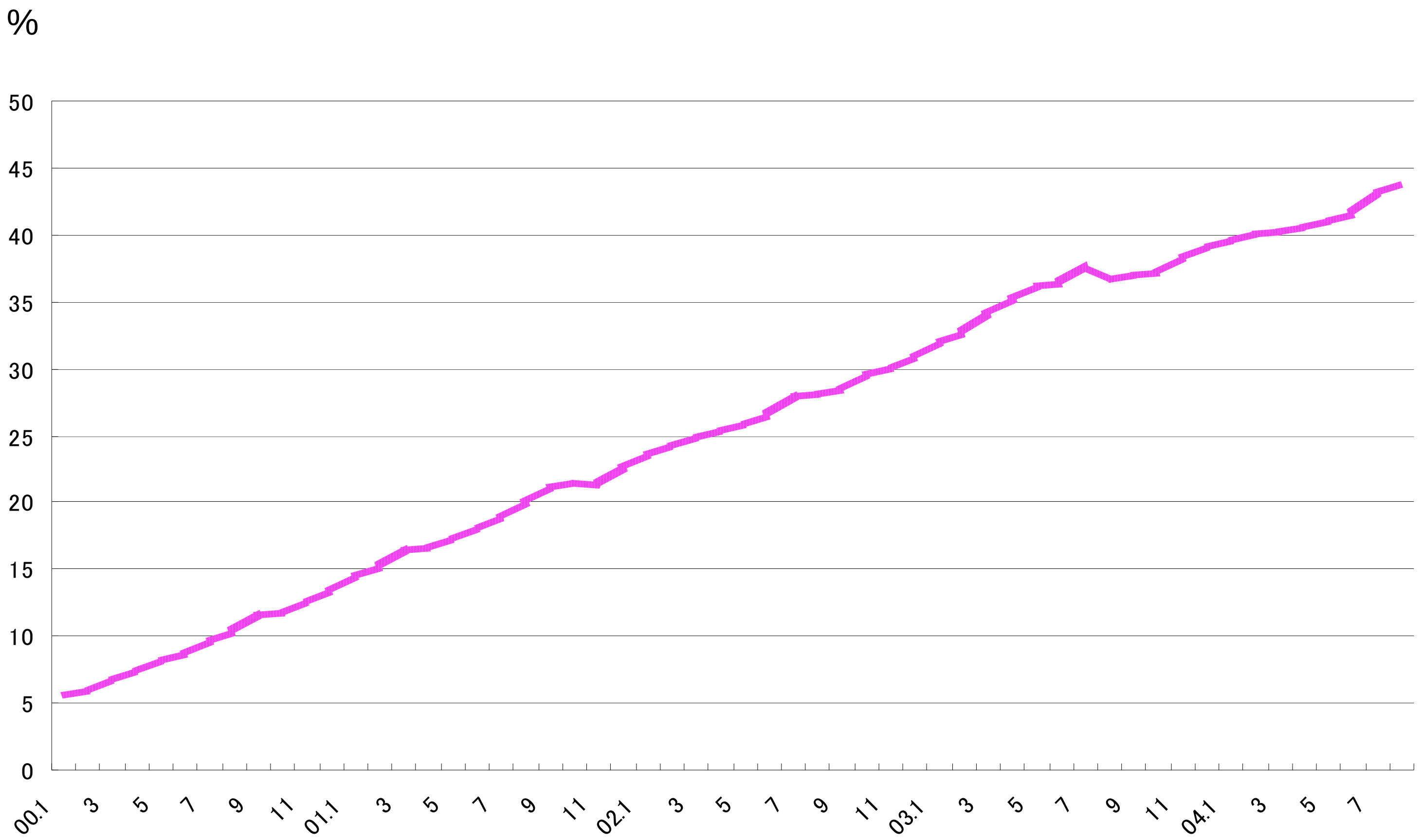
- Banks face less restrictions in doing securities business by themselves
  - Less need to be registered as securities firms
  - Less need to use securities affiliates or subsidiaries

- The meaning of “Functional Regulation” is different from GLB

Backgrounds

- Policy since 2001
  - Sifting individual financial assets from bank deposits to securities investment
- Purpose
  - Less money flows into banks = less risks in banking system
  - Utilize banks' nationwide networks to promote securities markets

Banks' share in mutual funds sales
(publicly offered stock funds)



Is Japan heading for a universal banking system?

- Some similarities to the initiatives in the UK and Canada in late 1980s
- Any significant problems emerged in the UK and Canada after the reform?
- Important differences = competition among financial industry
  - Banks hold dominating shares in money flow
  - Increasing market shares of mega-banks

Compositions of personal financial assets (2001)

	Cash & Deposit	Mutual funds	Stocks	Bonds
JPN	54%	2%	7%	5%
US	11%	12%	34%	10%
UK	23%	5%	13%	1%
CAN	27%	-	28%	3%

Emergence of mega banking groups (March 2004)

	vs. domestic deposits	vs. domestic deposits + postal savings	vs. major banks' deposits
Mizuho FG	13.6%	9.6%	25.4%
SMFG	11.8%	8.4%	22.2%
MTFG	10.4%	7.4%	19.5%
UFJHD	10.3%	7.3%	19.4%
MTFG+UFJHD	20.8%	14.7%	38.9%
SMFG+UFJHD	22.2%	15.7%	41.5%

Competition policy mitigating LCFIs' problems

- US
  - strict competition policy (ex.10% share)
  - long history of banning interstate business
  - no dominating financial players (except for GSEs?)
- UK
  - relatively effective competition policy
- Canada
  - prohibition of mergers among the Big 5
  - prohibition of mergers between the Big 5 and big insurance firms

Real issue=Emergence of LCFIs in Japanese context

- Limited competition policy
- Policy allowing banks to be more complex
- Insufficient market disciplines and prevalent moral hazard
- Is Japan becoming the country with the Largest and the most Complex Financial Institutions?
- Future policy course
  - Clear policy focus on LCFIs' potential threats over depositors, investors, fair competitions, and financial systems