Financial Conglomerates in Japan
Is Japan heading for a universal banking system?

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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
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)

<table>
<thead>
<tr>
<th>Country</th>
<th>Cash &amp; Deposit</th>
<th>Mutual funds</th>
<th>Stocks</th>
<th>Bonds</th>
</tr>
</thead>
<tbody>
<tr>
<td>JPN</td>
<td>54%</td>
<td>2%</td>
<td>7%</td>
<td>5%</td>
</tr>
<tr>
<td>US</td>
<td>11%</td>
<td>12%</td>
<td>34%</td>
<td>10%</td>
</tr>
<tr>
<td>UK</td>
<td>23%</td>
<td>5%</td>
<td>13%</td>
<td>1%</td>
</tr>
<tr>
<td>CAN</td>
<td>27%</td>
<td>-</td>
<td>28%</td>
<td>3%</td>
</tr>
</tbody>
</table>
### Emergence of mega banking groups (March 2004)

<table>
<thead>
<tr>
<th></th>
<th>vs. domestic deposits</th>
<th>vs. domestic deposits + postal savings</th>
<th>vs. major banks’ deposits</th>
</tr>
</thead>
<tbody>
<tr>
<td>Mizuho FG</td>
<td>13.6%</td>
<td>9.6%</td>
<td>25.4%</td>
</tr>
<tr>
<td>SMFG</td>
<td>11.8%</td>
<td>8.4%</td>
<td>22.2%</td>
</tr>
<tr>
<td>MTFG</td>
<td>10.4%</td>
<td>7.4%</td>
<td>19.5%</td>
</tr>
<tr>
<td>UFJHD</td>
<td>10.3%</td>
<td>7.3%</td>
<td>19.4%</td>
</tr>
<tr>
<td>MTFG+UFJHD</td>
<td>20.8%</td>
<td>14.7%</td>
<td>38.9%</td>
</tr>
<tr>
<td>SMFG+UFJHD</td>
<td>22.2%</td>
<td>15.7%</td>
<td>41.5%</td>
</tr>
</tbody>
</table>
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