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ORIGIN AND EVOLUTION OF CORPORATE OWNERSHIP IN JAPAN: A HISTORICAL REVIEW

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ABSTRACT

This paper is about the origin and evolution of the ownership structures of Japanese firms based on a thorough literature review. Despite several excellent studies, there are several conceptual confusions and debates engendered about why and how the corporate ownership in Japan was originated, shaped, and reshaped over time. Most importantly, there are very few theoretical studies which have addressed this issue comprehensively with chronological order. In this paper, we try to systematically explain the evolutionary stages of corporate ownership from Meiji period to current period. This paper explains the emergence and transformation of different ownership structures of Japanese firms as responses to changing economic, regulatory, and political factors over different eras.

KEYWORDS

Cross-shareholdings, Keiretsu, Ownership structure, Zaibatsu.

1. INTRODUCTION

The world is changing faster than anyone could expect and people are struggling to keep up with the pace of this change. In this ever changing world, too often, we encounter with many conflicting issues that need to be addressed with proper care. Corporate ownership is one of those aspects where most of the researchers are divided in their opinions. One point of conflicts is whether ownership structure of business firm is exogenously determined or it is endogenously determined by other factors. Sometimes, rather than depending solely on empirical investigations, it is useful to look at the history of corporate ownership to address this dilemma. The history of Japanese corporate ownership is always attention-grabbing because Japan is such a unique country where business firms have successively gone through the experiences of concentrated family ownership, dispersed individual ownership, significant corporate ownership, and notable foreign ownership over different eras. In addition, ownership patterns have been changed here more radically and more often than in any other major industrial economy. Despite several excellent studies, there are several conceptual confusions & debates engendered about the issue including its background as well as chronological transformations. Most interestingly, there are very few studies that have addressed this aspect comprehensively with logical and chronological order.

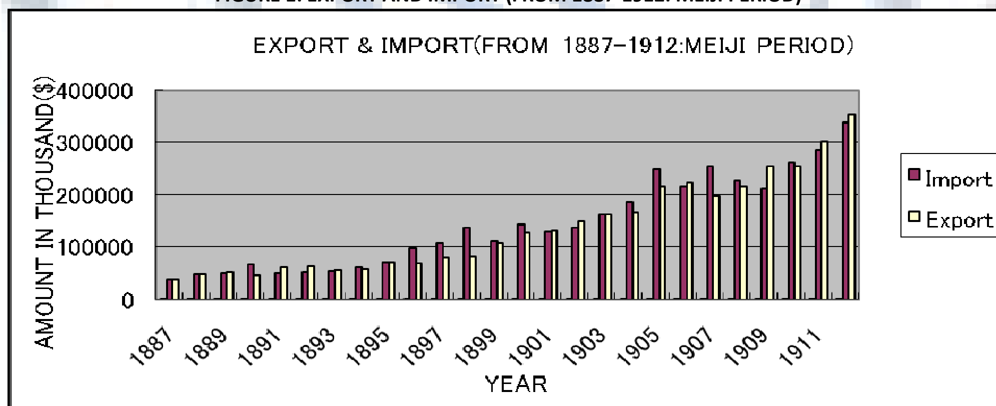
This paper is about the origin and evolution of the ownership structures of Japanese firms based on a thorough literature review. In this part, we make an effort to briefly document the different patterns of corporate ownership being observed in Japan and how those patterns have been shaped and reshaped over time. The explanation also includes concise idea about the changed economic, regulatory, and political systems of Japan over different periods which could sensibly be linked to different ownership structures. We review the sizeable literature on the history of Japanese corporate ownership to attain our purpose. For describing the phenomenon, we try to provide as lucid an explanation as possible, without losing the theoretical rigor.

The paper is organised as follows: Section 2 describes the first phase of corporate ownership structure in Japan after the restoration of imperial rule in 1868(Meiji period). Section 3 describes the second phase of ownership structure after the World War I. Section 4 details the overall corporate ownership and its changes during the American Occupation period in Japan while Section 5 describes the subsequent changes during the post-Occupation period extending up to 1980s. Section 6 reflects the changes in ownership structure of Japanese firms due to financial crisis in 1990s and its current status. Section 7 contains some concluding remarks.

2. MEIJI PERIOD: 1868-1912

During the early part of 16th century, many people started to accept Christianity in Japan not necessarily for the Christian message of salvation by the European missionaries but also for the economic gains and political advantages. As a result, panic of colonization seized the Japanese rulers to such an extent that they subsequently become stringent to stop that phenomenon by issuing *Tokugawa Shogun Exclusion Act of 1639*. Under that exclusionary policy, more than two hundred years, Japan had no political and business connections with rest of the world in true sense. No foreigner was allowed to enter into Japan (except Dutch and Chinese with limited access) and Japanese people were also not allowed to visit outside. Although foreign trade had been prohibited, domestic trade flourished and many merchant families (for example, Mitsui and Sumitomo families) grew wealthy. However, businesses were small in scale and operation. Therefore, the foundation of modern Japanese businesses with large scale of operation, gigantic volume of international trade, and business incorporation were laid on the periods after the restoration of imperial rule in 1868(end of *feudalism*). The first period is called *Meiji Period* which literally means enlightenment period because the country had substantially moved away from closed door to open door policy for rest of the world after 1868. The Meiji government had immediately realised the importance of western ideas of doing business, western technology, and foreign trades. As a consequence, Japan endured significant changes during that period which unified and made Japan a stronger nation, just as powerful as the western countries. Japanese businesses and foreign trades (export and import) had continued to expand steadily (see Figure 1) during the same time.

FIGURE 1: EXPORT AND IMPORT (FROM 1887-1912: MEIJI PERIOD)



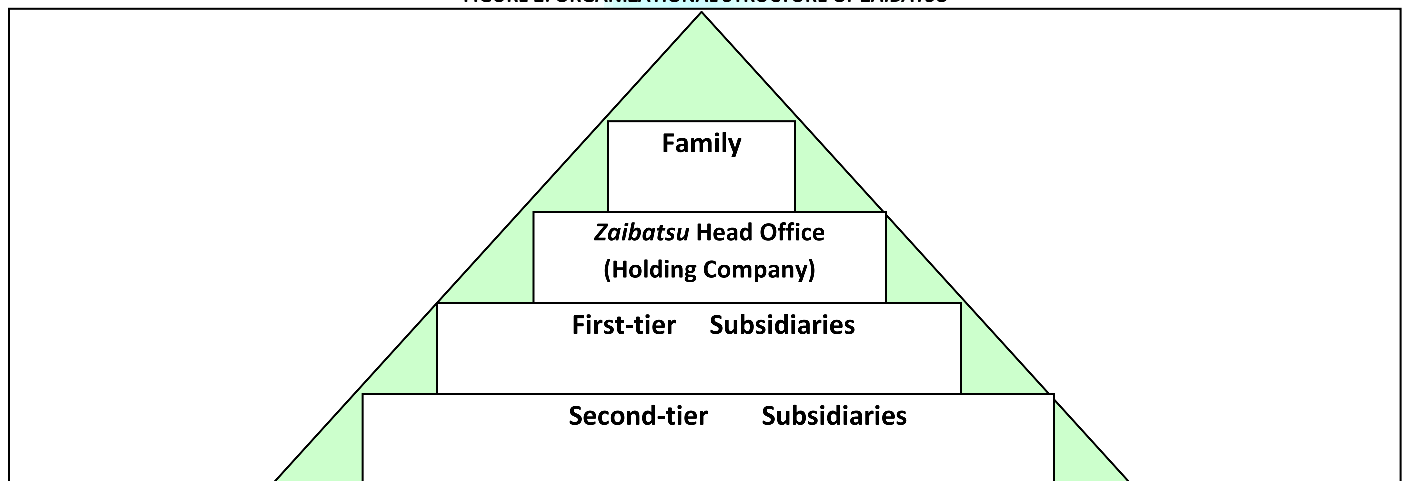
Source: Data compiled from the appendices of GHQ monograph, 1951.

Even though the speed of economic development was slow[1] at the initial stage but it was accelerated[2] at the later part of the 1890s. The notable expansion of Japan's industrial productive capacity after the *Sino-Japanese war (1894-1895)* favoured a rapid growth of businesses and foreign trades. As the economy was being shifted from agrarian economy into a developed industrial one, businesses were becoming bigger in size and incorporations were increasing sharply.[3] Those businesses were, particularly owned by few wealthiest families[4] in Japan, widely known as "*Zaibatsu*". Historically in Japan, the roles of few families were very dominating in various social, economic, and political aspects. Bisson (1954) summarized this point, "In Japan, under the old regime, privileged groups had exercised despotic power in every phase of economic life. Whether one looked at agriculture, labor, industry, banking, or trade, the picture was the same. A few great family combines dominated the business world was merely one aspect of a general situation" (p. 3).

The Meiji government also unswervingly supported the prospering of the businesses of those large and powerful families due to their significant contributions to the emerging economy of Japan. In a nutshell, family businesses were dominating and representing the industrial part of Japan. By utilizing their influences, they established banks (for example, Mitsui bank and Yasuda bank) at that period and thus, each *zaibatsu* substantially owned a bank. In pre-war Japan, as the business firms (mainly small and medium) could not raise enough capital through stock markets[5], they had to borrow from those *zaibatsu*'s banks. And for getting bank loan, they had the only option of making alliance to those wealthy families which helped those families to build massive industrial empire or combine individually.[6] Existing literature substantiates these realities of large business families during Meiji era. For example, Miwa and Ramseyer (2006, p. 39) documented that the *zaibatsu* built themselves the powerful empires through their lock on finance that dominated pre-war Japan. In explaining the role of *zaibatsu* owned banks, Hadley(1970, p. 29) also contended that banks gave combine firms preferential interest terms and were slow to extend credits to outsiders who challenged or might challenged an important subsidiary of *zaibatsu* in a particular field(as cited in Miwa and Ramseyer 2006, p. 40).

In order to describe the structure of *zaibatsu*, Morck and Nakamura (2005, p. 376) and Yafeh (1995, p. 155) mentioned that each *zaibatsu* had pyramidal structure where a family owned holding or partnership controlled a set of directly owned subsidiaries by owning majority of their shares,[7] which then controlled other firms, which then controlled yet other firms (if any), and so on (see Figure 2). Horizontal ownership and personal ties between group firms were also common.

FIGURE 2: ORGANIZATIONAL STRUCTURE OF *ZAIBATSU*



On the other hand, the expansion of ownership among the wider public was very limited and the role of newly established stock exchanges had remained relatively insignificant for the same (Francks, 1999, p.250).[8] Industrial advancement was mainly based on textile businesses. The textile industries grew faster and remained the largest Japanese industries until the World War II in terms of production volume or sales revenue.[9] However, Meiji era is always considered as the founding period for the establishment of modern institutional and legal frameworks for businesses.[10] The period came to an end with the death of the emperor Meiji in 1912 and subsequently, the World War I began which continued from 1914 to 1918.

3. POST WORLD WAR I PERIOD: 1918-1939

World War I was a watershed for Japanese economy in general, and for the *zaibatsu* families in particular, which were provided by war conditions with remarkable opportunities to capture and develop huge new markets in trading, shipping, and manufacturing businesses (Morikawa, 1992, p. 21; Shimotani, 1991, p. 14).[11] The old *zaibatsu* were being able to reap the war boom opportunities by strengthening and expanding businesses in various sectors. Moreover, the situation also facilitated the emergence of new *zaibatsu*.[12] These new *zaibatsu* were different from those so called family centric or subspecies of old *zaibatsu* both in terms of the ownership structure and the range of their business bases. They were genuine holding companies with a relatively large number of stockholders. Franks, Mayer and Miyajima (2007) mentioned that those companies also marketed their shares to the outside shareholders. As a result, the tendency of old *zaibatsu* to control through total ownership did not sustain over these companies (Yamazaki, 1988, pp. 25-26). Whereas the old *zaibatsu* were mainly focused on mining, banking and foreign trade, these new *zaibatsu* were concentrated on heavy and chemical industries. Each of these businesses was led by a person of marked individuality having engineering or chemical expertise rather than so called family support. On the other hand, the distaste of the great business families(old *zaibatsu*) for pooling capital from the outsiders were no longer continued as the need for capital was ever-growing to take the advantage of the post war boom. Families that kept their firms closely-held found this growing need for capital a serious problem and started to issue the shares of their subsidiaries to the public, maintaining the top-tier holdings stable.

The second blow of substantial equity issuance occurred during the 1930s as Japan endured a great depression (*Showa Depression*) with the world economy. Several major *zaibatsu* such as Fujita, Kuhara, and Suzuki collapsed due to that economic crisis (Morikawa, 1992, p. 121). The surviving *zaibatsu* started to sale the shares of their subsidiaries to the public as a way of raising funds. Moreover, after 1937, when the second *Sino-Japanese War* broke-out, production in the munitions industries increased drastically and the *zaibatsu* aggressively sought to reap them. To raise the necessary funds, they had to offer the shares of their first ranked subsidiaries for public subscription (Yamazaki, 1988, p. 32). In addition, Yamazaki (1988) mentioned that the *zaibatsu* also had to raise funds for welfare work and cooperate with state policy in an attempt to appease the anti-*zaibatsu* feelings of the army prevailing at that time. As a consequence, the average number of stock holders increased and the average ratio of stock holdings by families decreased.[13] However, during that time, minority investors' protection was very weak and *zaibatsu* firms were being alleged to involve with share price discrimination and fund mismanagement. Nevertheless, small investors were inclined to buy the shares of *zaibatsu* subsidiaries due to their reputation, stable performance during financial crisis, and good monitoring capacity. Franks et al. (2007, p. 37) confirmed that ownership concentration was decreased during that period and the trend was more or less continued until the period of World War II.

4. OCCUPATION PERIOD: 1945-1951

At the end of World War II, Japan was occupied by the Allied Powers, led by the United States with a contribution from the British Commonwealth Occupation Force. A sequence of far-reaching reforms was initiated by the General Headquarter (GHQ) office of the Allied Command following the end of World War II to change the Japanese regulatory and economic environments. Among the crucial reforms sought by the Allied Command, the measures directed toward the pre-

war *zaibatsu* took high priority (Bisson, 1954, p. 1; Yafeh, 1995, p. 155). In particular, the market power of the *zaibatsu* and the tremendous wealth of the founding families made the dissolution of those conglomerates one of the first and most important targets of the Occupation reforms. This attempt was initialized by "Initial Post-Surrender Policy for Japan" declared by the United States that it would liquidate Japan's large industrial and financial combines. The dissolution program had subsequently been accelerated by issuing several directives and Anti Monopoly Law 1947. For the same purpose, Holding Companies Liquidation Commission (HCLC) was formed which designated *zaibatsu* for dissolution (for example, see Table 1). The number of *zaibatsu* holding companies designated to dissolve was 83 (Yamazaki, 1988, p. 45).

TABLE 1: TEN MAJOR *ZAIBATSU* DESIGNATED FOR DISSOLUTION BY HCLC

Zaibatsu	**Number of Subsidiaries in 1946**
Mitsui	294
Mitsubishi	241
Sumitomo	166
Yasuda	60
Nissan	179
Asano	59
Furukawa	53
Okura	58
Nakajima	68
Nomura	19
Total	**1200**

Source: Morck and Nakamura, 2005, p.375

A few of restrictions on *zaibatsu* firms were as followings- (i) selling all holding shares of *zaibatsu* families and holding companies to public[14] or state (HCLC) on a priority basis; (ii) *zaibatsu* were prohibited to buy-back the shares of their subsidiaries; (iii) pre-war *zaibatsu* family members and managers were purged and prohibited from taking office; and (iv) maximum share ownership ceilings of individual and financial institutions were 1 percent and 5 percent of total shares, respectively. Moreover, share-ownership by ordinary non-financial corporations was, in principle, forbidden and formation of holding companies were made illegal (Okumura, 2000, p. 39).[15] The objective of such restrictions was to make the corporate ownership structure a democratic one and ensure equal opportunity for firms and individuals. In addition, the political cause behind *zaibatsu* dissolution was supposed to be the association of those firms with Japanese military expansion (Kearns, 1992, p. 4; Morikawa, 1992, p. 238; Yafeh, 1995, p. 155). Ozkan (2011) mentioned, "The Americans believed that the Japanese imperial army, rural landlords, and *zaibatsu* were the main actors in Japanese militarism, and therefore their role needed to be eliminated in the future" (p. 1).

Due to all these efforts, greatest dispersion in Japanese stock markets was being occurred; the minority investor protection was significantly improved and greater managerial independence was ensured. Kearns (1992) noted "In 1949, when the Tokyo Stock Exchange reopened, individuals owned 69.1 percent of all listed shares, securities houses held 12.6 percent, other financial institutions 9.9 percent, non-financial companies 5.6 percent and the government 2.8 percent" (p. 16).

However, as the economy was totally collapsed[16] due to war and the stock markets were not working, bank financing was the only source of additional funding.

5. POST OCCUPATION PERIOD: 1952-1980s

Once Japan regained the democratic power after the end of Occupation period, the scenario of corporate ownership proved unstable and gradually changed to a new trend. Individual ownership almost immediately began to decline and the institutional ownership (both financial institutions and corporations) increased. There were manifold reasons associated with this changing pattern. One of those was the poor operating performance of the listed companies, which discouraged the individual shareholders to continue their holdings. Yafeh (1995, p. 154) documented strong evidence regarding this phenomenon and showed that, other things equal, the greater the percentage of a firm's outstanding shares expropriated and resold by the Occupation, the worse was the firm's performance in the 1950s. That's why, once the stocks markets began to operate, individual shareholders disposed off most of their holdings. On the other hands, the financial institutions (mainly banks) became increasingly interested to buy those sold share as they wanted to take the control of those companies which were burdened with bank loans.[17] Okumura (2000, p. 37) remarked that corporations did not acquire shares on the basis of a calculation of their yields rather as a means of control in their linkages with various other firms. Miyajima (1994, p. 293) argued that, in view of the diffuse post-reform ownership structure and the dissolution of the holding companies, close monitoring by banks as large shareholders became the only mechanism capable of controlling and aligning managerial behaviour with debt and share holders' interests.

At the same time, this changing pattern was also welcomed by the corporate managers due to remain insulated from the external threats of takeover prevailing at that time and keep nettlesome foreign influences out of Japan. Many authors asserted (for example, Miyajima, 1994; Scher, 2001) that low equity prices soon after the war were posited to have many Japanese firms easy target of takeover. Moreover, Scher (2001, p. 4) documented that, during this period, speculators purchased stocks, which management bought back at a higher price (commonly denoted as greenmail). For the same reason, managers discretionarily became involved with fixing the allocation pattern of shares. The common idea of that period was *"Shareholders do not select the company for investment rather company (management) chose the shareholders to allocate the capital" or "Capital is allocated on the basis of who knows whom instead of economic effectiveness".*

These triple urgencies from the three groups (individual investors, financial institutions and corporate management) had made a dramatic change in the pattern of corporate ownership. Okumura (2000, p. 36) denoted this phenomenon as "a reversal of dispersed share-ownership towards its concentration". Aoki (1998) added that the trend was further encouraged by the change in financial institutions' shareholding restriction from maximum 5 percent to 10 percent (as cited in Yafeh, 1995, p. 158). The second stage in the growth of institutional shareholding was precipitated in the wake of the stock markets decline between 1962 and 1965(Goto, 1982, p. 56; Scher, 2001, p. 4). In 1964 and 1965, financial institutions set up two companies, namely, the Japan Cooperative Securities Company and the Japan Security Holding Union to stabilize shareholdings. Between 1964 and 1965, these two institutions purchased 5 percent of the equity of all listed companies (Miyajima et al., 2003, as cited in Franks et al., 2007, p. 20) which was subsequently sold to group interlinked companies. In addition, Section 280 of the Commercial Code was revised so that boards of companies would be able to allocate newly issued shares to specified companies and individuals (Scher, 2001, p. 5). Another factor was Japan's membership of Organization for Economic Cooperation and Development (OECD) in 1964 which required Japanese capital markets to be deregulated for the foreign investors. As Japanese companies were not ready to allow the invasion of foreign owners in the capital structure, they decided to lock their individual shares mutually among interrelated companies. All these above-mentioned facts made the emergence of another trend of ownership structure in the Japanese corporate history commonly called "*Keiretsu*" or corporate cross-shareholdings.

Simply speaking, when two or more than two companies hold each other shares, it is called *keiretsu*[18] or cross shareholdings. The Japanese *keiretsu* are distinct in the way they are being formed and operated. They are mainly controlled by the main banks of the companies often called main bank system where the main banks play the dual role of equity holders and debt providers.[19] Moreover, ownerships are also taken by some mutually unified and same minded companies. The objective of such holdings are less of individual financial benefit and more of group benefit, sustainability and security (from external takeover threats). During 1980s bubble period, more than 60 to 70 percent of total market capitalization was owned by these *keiretsu* firms having limited or no floatation (Scher, 2001, p. 1; Wood, 1992, p. 24). According to Kearns (1992), "By the end of 1980s, corporations owned 73 percent of all listed shares, individuals 22.4 percent, the government 0.7 percent and foreigners 4 percent" (p. 16), which completed the reversal of the occupation period's shareholder democracy. Okumura (2000, p. 38) ascribed this consequence by the phrase the "phenomenon of the corporatization of share-ownership". These interlinked firms not only exchanged

ownership stake but also corporate executives and directorates, strategic plans and policies to ensure the maximum control and performance. Moreover, if a *keiretsu* member got into financial trouble, the other companies would usually bail it out whatever might be the cost.[20]

Keiretsu businesses are different from what we call business conglomerate and cartel, having giant size and structure, being particularly able at providing cheap capital for growth and spreading the economic risk over a broad base of companies working in many sectors of the Japanese economy. Although there is no hard and fast rule as to how they would be structured but two patterns are mainly observed in the Japanese context. One is the horizontal *keiretsu* (Mitsubishi, Mitsui, Sumitomo etc.) which has been formed among companies in a wide range of industries but having parallel interest. In contrast, vertical *keiretsu* (Toyota, Matsushita, Hitachi etc.) has been formed by vertically integrated industries having supplier-customer relationship.

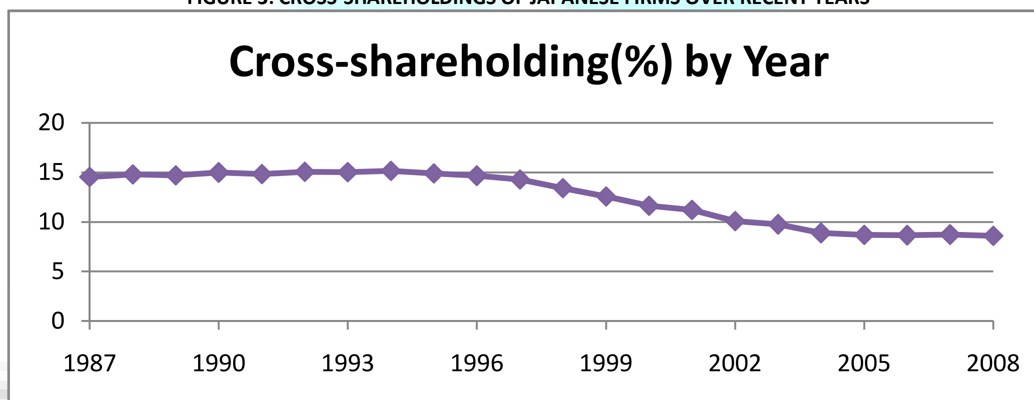
It would be noteworthy to mention here the fundamental differences between pre-war *zaibatsu* and post-war *keiretsu*. Kearns (1992, p. 4) described that the word "*zaibatsu"* as a financial clique evolved as a family dominated holding company and the word "*keiretsu"* as a lineage or a group arranged by interlocking shareholdings around bank and trading company. Shimotani (1991, p. 7) argued that corporate complexes (*keiretsu*) was completely different from the pre-war *zaibatsu*, both in ownership structure and in organizational structure. Ownership and control of the *zaibatsu* resided in the all-powerful family sitting at the top of the holding company pyramid, whereas in case of *keiretsu*, control was shared by member companies connected through interlocking shareholdings. Decisions made by the *zaibatsu* head offices, acting as control towers standing above the members' corporations, were executed by those affiliated member corporations whereas *keiretsu* member firms made their decisions jointly through informal gathering in the form of monthly luncheons. Goto (1982, p. 55) stated that the representatives (senior executives mainly presidents) from members firms of *keiretsu* used to gather once a month in clubs commonly known as "Presidents' Clubs" for exchanging information and coordination, fixing future policies for opening up business opportunities, new technologies, government regulations, foreign market situation, and the granting of permission to a firm to use the group name. Nakagawa (1988, p. 8) mentioned that control exercised by the *keiretsu* banks and trading companies was not as tight and exclusive as the control exercised by the pre-war *zaibatsu* organizations. Though in external form, *zaibatsu* and *keiretsu* do differ in some extent, the basic dynamic force underlying the economic structure of both is same-"*the group having like-minded goal and preferential relationship"*. Many critics claimed that the dispersed corporations (ex-*zaibatsu*) were re-interlinked through share purchases to form horizontally-integrated alliances across many industries (*keiretsu*).[21] In fact, *keiretsu* are the later day heirs of old *zaibatsu* during the pre-World War II (Kearns, 1992, ix). So, it is a debatable issue to justify whether the *keiretsu* formation would be regarded as an efficient market response to an externally imposed inefficient reform or was it nothing more than a resurrection of pre-war group ties in a new guise.

Whatever might be the ownership form either *zaibatsu* or *keiretsu*, historical and statistical evidences support the view that both of them offered Japanese corporations unique competitive advantages and tremendous economic blessings during the twentieth century.

6. CURRENT PERIOD: 1990s AND AFTERWARDS

The dominance of *keiretsu* was confronted to serious challenges due to the financial crisis swirling during the 1990s. When the Japanese economic bubble burst at the beginning of the 1990s, putting Japan into its "lost decade", regulators, investors, even the popular press began talking about the *keiretsu*, the power these groups wielded in Japan, and resulting inefficiency. It is argued that the true nature of crisis was not of the economic system as a whole rather one of the financial system oriented with main bank. Scher (2001, p. 19) claimed that banks had not been especially successful "monitors" of members of the corporate groups during that decade. Kikkawa (2006, p. 112) pointed out the following three factors that were responsible for the 1990s financial crisis: (a) a surplus of money based on trade surplus; (b) a lack of financial know-how among business companies; and (c) a lack of monitoring ability among banks. He added that the crisis triggered the accumulation of bad debts by businesses on the one hand, and bad loans by banks on the other. Even though the crisis affected all listed companies' stock prices irrespective of nature, but the position of banks deteriorated sharply. The price of banks' shares declined more than two-third of it pre-crisis level which forced the companies to sell off their banks' shares sacrificing their long-standing mutual and stable relationship. Wu and Yao (2012, p. 46) found that firms also with more bank borrowings in the late 1980s had more equity losses during the stock market slump in the early 1990s as bank borrowing indicated higher real risk. Banks also reacted in the same way and divested a significant portion of their corporate shareholdings to manage fund for tackling liquidity demand during the financial distress period. As a result, the once *keiretsu* chains, dominated by the major banks, gradually lost their significant influence and control on the Japanese corporate economy by the end the 1990s (see Figure 3).

FIGURE 3: CROSS-SHAREHOLDINGS OF JAPANESE FIRMS OVER RECENT YEARS



Source: Data compiled from survey of NLI Research Institute; Nitta, 2008, p. 4.

However, the speed and volume of off-loading crossly-held shares were not same between financial institutions and business corporations. Mainly, the companies' sold off banks' shares were relatively more pronounced than banks' sold off of companies' shares. Moreover, shareholdings between non-financial companies remained relatively unchanged (Okabe, 2002, p. 35). The process of unwinding of cross-shareholdings also accelerated due to some other reasons (some of them are considered as measures taken to cope up with the economic distress) which came into effect around the time of the financial crisis:

I. BANK SHAREHOLDINGS RESTRICTION ACTS 2001

Bank Shareholdings Restrictions Act 2001(with a targeted implementation date of September, 2004) made the restrictions for banks to invest in shares. Banks' shareholdings were restricted up to 1.5 times of Tier-1 capital, in order to actively dissolve cross-shareholdings, requiring excess shares to be transferred to Banks' Shareholdings Purchase Corporation (BSPC) or to the market. As a result, all the banks had to sell their shares in excess of the limit. Moreover, financial institutional ownership ceiling was reduced from maximum 10 percent to 5 percent.[22] Scher (2001, p. 17) mentions that this ceiling caused the banks to sell off excess shares to bank owned subsidiaries. In addition, revisions to the Commercial Code abolished restrictions on share buy-backs from March 1998, allowing firms to hold their own shares continuously after acquisition (lifting the ban on treasury stock).[23]

II. BANK MERGERS

Bank mergers themselves caused the liquidation of crossly-held shares by the merged banks during the 1990s financial crisis. If each of two merging banks owned shares in a client firm, then the new merged bank should sell off enough of those shares to bring the new bank's total holding down to 5 percent of the firm's equity. Moreover, since the main bank was typically the greatest cross-shareholder among the banks that are part of the firm's stable shareholders, a merged bank that was not the main bank of the firm would have been compelled to reduce its holdings even further to make it less than main-bank holding (Scher, 2001, pp. 16-17).

III. BASEL ACCORD AND RISK SENSITIVITY

At the contemporary time of the financial crisis, the BASEL accord was changed by the Bank for International Settlements (BIS) which requires the banks to consider the investment in shares for calculating risk adjusted assets in determining the tier-2 minimum capital requirement. According to the BASEL accord, an international capital adequacy standard, equities held in a bank's portfolio at historic cost can be revalued to reflect their current value, and 45 percent of the resultant revaluation reserves (latent revaluation reserves)[24] should be included in the capital base (BASEL Committee on Banking Supervision 1988, as cited in Okabe, 2002, p. 36). As a consequence, counting unrealized gain or loss made Japanese banks vulnerable to the price fluctuations in the stock market. This means that when there is a valuation gain accruing to holding stocks, the size of a company's capital expands, thus lowering the return on equity (ROE), an index of great importance for investors. In contrast, fall of stock prices might lead to the erosion of capital base causing financial anxiety to maintain BIS standard of an 8 percent ratio of capital to assets as well as degradation of bank's rating in the market. The collapse of the stock markets during 1990s also collapsed the banks tier-2 capital and put them under the pressure to raise capital. But they no longer could find easy capital to borrow and forced into financially distress condition. Under such circumstance, banks came to realise the real burdens of holding stocks and went for the sale of stocks investment.

IV. DEREGULATION OF INTEREST RATES ON DEPOSITS

Before 1985, banks were not allowed to pay interest on deposits which induced them to extend credits or loans irrationally and immensely[25] as there were no costs of fund in true sense. This culture made the banks peculiarly ill suited to cope with the wrenching change posed by the deregulation of interest rates (Wood, 1992, p. 21). In 1985, the Japanese government (Ministry of Finance) began to deregulate the interest rates on deposits which prompted the banks into fierce competition for deposits as well as interest payments. Moreover, banks did not raise the interest rates of lending to offset the effect of increased costs of deposits. In order to manage the widening hole in their operating profits, they began to sell the shares they owned for a long time and counted the realized capital gains as profit.[26]

V. EASY ACCESS TO FINANCIAL MARKET

Irrespective of the distress market condition during the 1990s, it was easier for the profitable and large companies to collect finance from the share markets rather than depending on bank finance only. So, the profitable firms became enthusiastic to reduce the discretion of main bank by raising funds from the share markets directly. Kikkawa (2006, p. 112) argued that many businesses has changed their financial policies from banks-financing to equity financing as soon as the capital markets became more effective (see Table 2). Thus, the debt for equity swap (the foundation principle of *keiretsu* system) was no longer remained a valid and strong argument to continue the *keiretsu* relationship.

TABLE 2: THE DECLINE OF BANK DEBT IN JAPANESE CORPORATE FINANCE: THE RATIO OF BANK DEBT TO ASSETS FOR LARGE LISTED JAPANESE MANUFACTURING FIRMS OVER SELECTED YEARS

Year	Bank debt to total assets ratio (approx.)
1972	0.39
1977	0.37
1982	0.30
1987	0.23
1992	0.14
1997	0.13

Source: Hoshi and Kashyap, 1999, p. 148

Note: The term 'large' refers to Japanese firms whose assets exceed 120 billion Yen

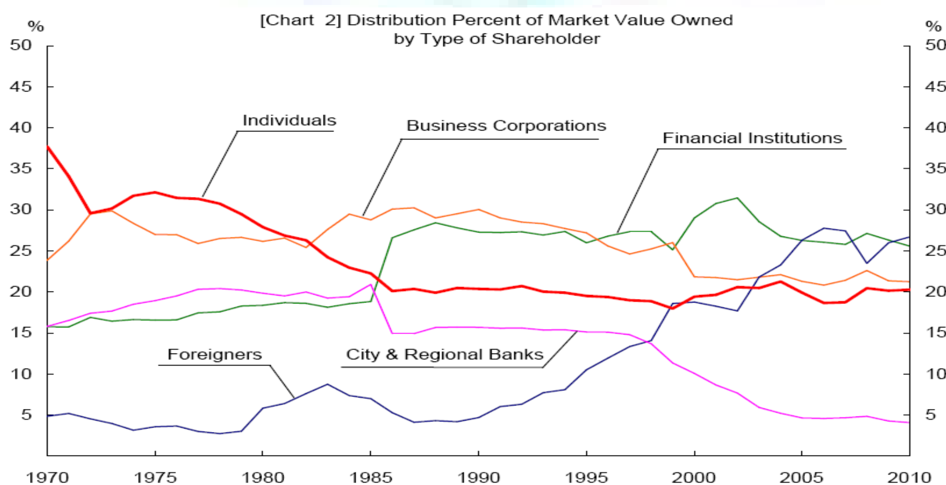
VI. INTRODUCTION OF NEW AND UPGRADED JAPANESE ACCOUNTING STANDARDS

During the period between 1999 and 2001, a radical reform was implemented in the financial reporting system of Japan which is very often referred as "Accounting Big Bang". The objective was to ensure more transparency and international acceptability of the financial disclosures of the Japanese firms. Shiba (2003, p. 7) stated, "Accounting after 1997 has produced a change in the conscious and behavior of the Japanese corporations … the year 2000 points the real start of the new era".

Two major changes in the disclosure system are (1) preparing consolidated financial statements from the fiscal year 1999, and (2) the evaluation of financial assets by the market value replacing the old historical cost valuation.[27] Due to the latter one, it becomes necessary to recognize as well as disclose accrued gain or loss from stock investment as items under capital in the balance sheet, rather than being reported in the profit and loss statement. The complicacy is that when there is a valuation gain, the amount of capital expanded; but when there is a valuation loss, the amount of capital is damaged. And thus, the new change has injected an uncertainty of holding shares and other financial securities. So the financial institutions and business firms have begun to sell off crossly-held shares and tried to relocate the proceeds for other purposes.

Now it is worth asking that if the corporate shareholdings in the form of cross-holdings were reduced during the 1990s and thereafter, then who has bought the shares came into the market. The recent trend of share-ownership answers this more clearly than anything else (see Figure 4).

FIGURE 4: LONG-TERM TREND IN OWNERSHIP STRUCTURE OF JAPANESE LISTED COMPANIES AT MARKET VALUE



Source: Share-ownership Survey-2010

From the above figure, it is evident that during the 1990s financial crisis and afterwards, all categories of shares have either reduced or remained stable but foreign shareholding has increased sharply.[28] According to the share ownership survey of the Japanese listed companies conducted in 2010, the present corporate ownership is dominantly represented by two categories of shareholders-financial institutions and business corporations. Each of these categories is occupying around one-fourth of total outstanding market shares (see Table 2). It is also evident that foreign owners have significant stake in the corporate

ownership of Japan in the twenty-first century.. Among institutional shareholders, since the mid-1990s, the ownership structure of Japanese companies is also featured by the presence of large funds, such as investment trusts and pension funds (Naoki, 2009, p. 2). However, *keiretsu* have not vanished completely, rather many members firm are still managed to maintain their *keiretsu* allegiance at lower scale. Recent surveys conducted by the NLI research institute, a very prominent research organisation in Japan, have confirmed that the level of such cross holdings among the firms is around 8 percent. In a nutshell, the current ownership structure seems to be balanced in compare to any prior periods. Now, it is just a matter of time to see how the Japanese companies perform with this changed control in coming future.

TABLE 3: PERCENTAGE OF UNIT SHARES HELD BY TYPES OF SHAREHOLDERS 2009-2010

Survey year	2009	2010
No. of Companies	3694	3616
	Percentage of unit shares	
(1) Govt. & local govt.	0.2	0.2
(2) Financial Institutions	23.9	22.5
(a) City & Regional Banks	3.1	2.8
(b) Trust Banks	15.1	14.6
(c) Life Insurance Cos.	3.5	3.1
(d)Non-Life Insurance Cos.	1.4	1.3
(e) Others financial Inst.	0.8	0.7
(3) Securities companies	1.5	1.8
(4) Business Corporations	24.5	24.3
(5) Foreigners	22.5	22.2
(6) Individuals	27.3	29.1

Source: Share-ownership Survey-2010

7. CONCLUSION

Any form of ownership pattern is likely to be sustainable only if they are economically and politically viable. Any other forms, whatever is the nature, will not sustain a longer period and will be re-organized into its rational shape soon. Japanese ownership structures starting from Meiji period reflect the same conclusion and can be forwarded as an example to the rest of the world. The frequently changing ownership patterns of Japanese corporations have made us curious and entwined to do research in this field. It is evident that corporate groupings (*zaibatsu*/*keiretsu)* have dominated the corporate ownership structure of Japanese firms except the short Occupation period. The economic viability, political back-up and regulatory changes were more pronounced in explaining those trends than anything else. The recent statistics support that present-day Japan has reduced group bonding significantly. However, according to share-ownership survey-2010, financial institutions and business corporations control around 50 percent (on an average) of total market shares of Japanese listed companies. Moreover, it is also visible that foreign owners are now holding significant stake in the overall market. Simply putting, the control is now supposed to be much more balanced compare to the twentieth century.

This paper is worthy of attention, and is an important contribution to the continuing dialogue on the Japanese corporate ownership structures. Our attempts in this paper are not to justify which form of corporate ownership structure is better for Japan, rather narrating the facts and the factors that have driven the ownership structures of Japanese companies from Meiji period to present state. We hope this research will definitely benefit a wide range of people in the Japanese financial sectors to comprehend the situation and set the future of corporate control, taking lessons from the history. Finally, this study suggests that this is a fertile area for future study.

ENDNOTES

[1] Due to excessive circulation of inconvertible notes (clan notes), higher commodity price, and unfavourable trade conditions (General Head Quarter [GHQ] monograph, 1951, pp. 1-2).

[2] Due to (a) withdrawal of inconvertible notes by the establishment of "Yen", (b) introduction of silver standard & subsequently gold standard for international trade, and (c) revision of tariff policy & treaties etc.

[3] Out of 4,596 companies during Meiji period, joint stock companies, limited partnership, unlimited partnership comprised 56.2 percent, 36.3 percent and 7.5 percent respectively (Miyamoto 1984, as cited in Yasuoka, 1986, p. 1).

[4] Mainly four families (the Mitsui, the Iwasaki of the Mitsubishi Empire, the Sumitomo, and the Yasuda). Others were Furukawa, Asano and Okura.

[5] Newly established stock markets (For example Tokyo, Osaka) were not so operational & active at that period.

[6] In markets where the individual *Zaibatsu* tended to dominate, its share of the total sales ran as high as 50 or 60 per cent (RMJC, 1946, p. 55, as cited in Bisson, 1954, p.12). Moreover, *Zaibatsu* controlled over a quarter of all capital assets in the economy (Hadley 1970, as cited in Yafeh, 1995, p. 155).

[7] The ratio of such holding was around 80 percent or more in case of Mitsui, Mitsubishi, Sumitomo, Furukawa and Okura in 1928 (Yamazaki, 1988, pp. 24-25).

[8] The numbers of listed companies were between 40-50 in 1905, 108 in 1908, and 262 in 1918 (Franks et al. 2007, p.11).

[9] See Yamazaki (1988, pp. 12-54) for details.

[10] Establishment of banking system, commercial and tax laws, stock exchanges, stock market law, and a communications network.

[11] The war cut-off exports of the manufactured goods by the European nations, an interruption that not only secured the domestic market for Japanese manufacturers but also made an expansion of their share of the Asian market.

[12] For example, Nissan, Nitchitsu, Mori, Nihon Soda etc.

[13] For example, average number of stockholders increased for: Mitsui, from 5,481 to 14,836; Mitsubishi, from 6,374 to 11,106; Sumitomo, from 3128 to 5,862; Furukawa, from 323 to 19,821. Average ratio of stock holding in the same group decreased for: Mitsui, from 51 percent to 31.7 percent; Mitsubishi, from 52.5 percent to35.2 percent; Sumitomo, from 52.9 percent to32.8 percent; Furukawa, from 65.2 percent to 44.5 percent (Yamazaki 1988:33-35).

[14] Giving priority to the officials and employees of those companies.

[15] Holding companies, which were banned by the American occupation forces after the World War II, became legal again in Japan in 1998 (Yafeh, 2000, p. 81).

[16] Massive destructions of war and subsequent poor relationship with neighbouring countries (China, Korea, Formusa-Taiwan) as well as sterling countries caused retarding effect on production, import and export; trade deficit and inflation in the economy (GHQ monograph, 1951, p. 222).

[17] In early post-war period, the stock market initially played a relatively important role as a source of funds for corporate investment in Japan … it soon came to be overwhelmed by bank loans. This was clearly reflected in the ever-declining equity-to-total-capital ratio throughout Japan's high-growth era (1950-1974); for all industries (Ozawa, 1999, p. 353).

[18] Six dominating *Keiretsu* were Mitsui, Sumitomo, Mitsubishi, Fuyo, Sanwa, Dai-chi Kangya Bank (DKB). Each of them had a bank and a trading company.

[19] The main bank relationship between a bank and a business corporation is usually characterized by all or many of the following situations (1) the bank has the largest share of lending of all the banks for the firm; (2) the main bank is the top owner of the business corporation's equity; (3) the bank is the main performer of various financial services beside lending; (4)the bank dispatches its personnel as executives of the business corporation; and (5) when the business corporation faces financial distress, the bank extends various kinds of assistance, including the making of an emergency loan (Okabe, 1999, chapter 1; as cited in Okabe, 2002, p. 30).

[20] For example, Mazda in 1970s.

[21] For example, Mitsui, Mitsubishi, Sumitomo and Fuji (Goto, 1982, p. 54).

[22] In 1977, the upper permissible limit on bank holdings of a firm' shares had been reduced from ten to five percents by Anti-Monopoly Reform Bill, with the banks having ten years to comply (Sheard, 1989, p. 402).
[23] See Miyajima and Kuroki, 2005, p. 14.
[24] Hidden assets.
[25] Bank loans equalled 90 percent of nominal GNP at the end of September 1991 in Japan, compared with 37 percent in America (Wood, 1992, p. 25).
[26] For example, in the financial year ending on March 31, 1989 an average of 42 percent of the reported profits of Japan's city banks came from securities gains (Wood, 1992, p. 23).
[27] Securities held for trading purpose should be valued in the market price from the fiscal year 2000 (April 2000-March 2001) and the other securities (stably-held shares including the cross-held shares) should be valued in the same way (fair value) from the fiscal year 2001.
[28] A study by NLI Research Institute (1998) of 2426 firms reported that stable holdings of their shares fall from over 41 percent in 1992 to 36 percent in 1997. During the same period, foreign holdings of the shares in these firms become double from 6.3 percent to 13.4 percent (Scher, 2001, p. 6).

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