



# CPRC

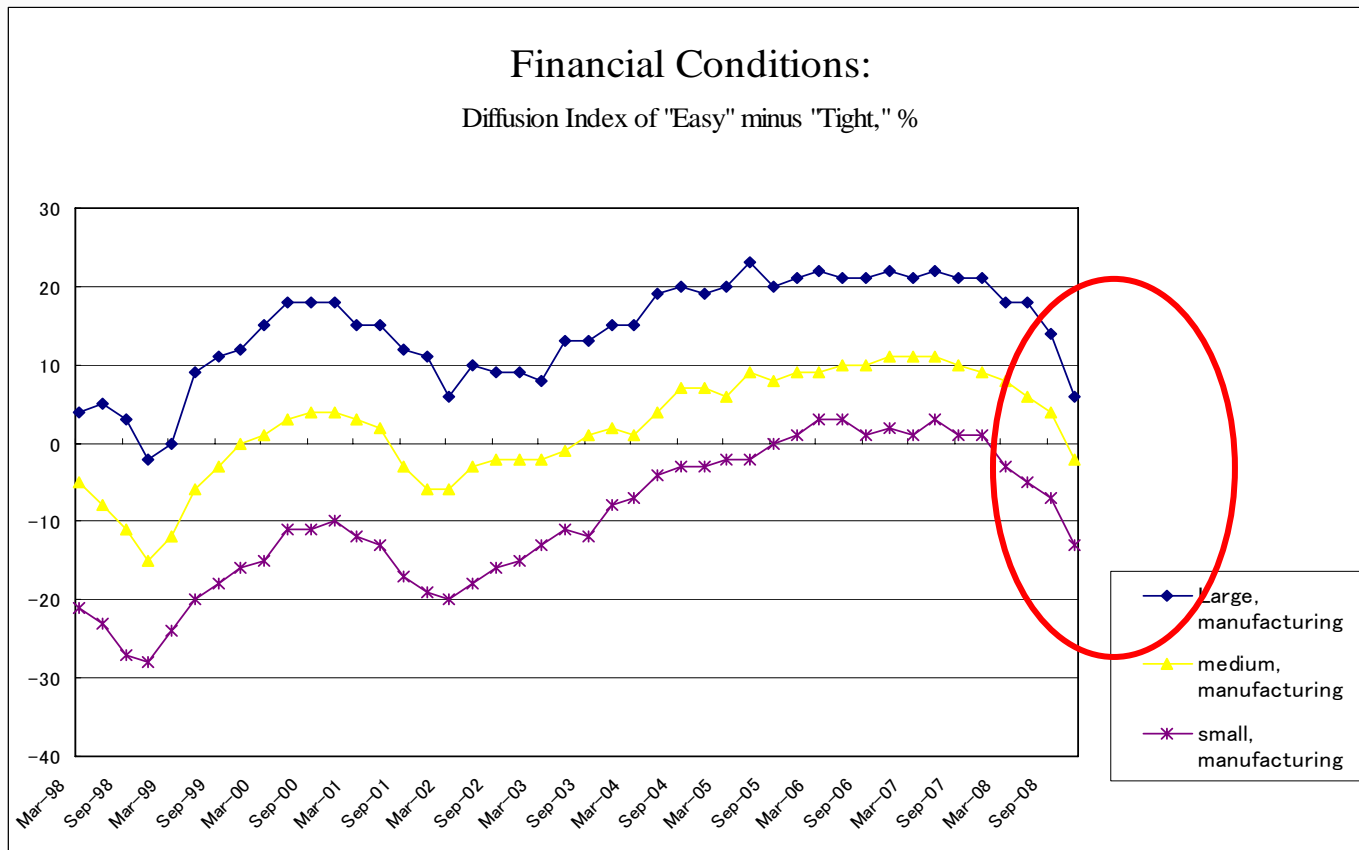
COMPETITION POLICY RESEARCH CENTER  
Fair Trade Commission of Japan

## Competition Policy in the Financial Sector and the Current Economic Crisis

Hiroshi Ohashi  
University of Tokyo

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Japan Fair Trade Commission

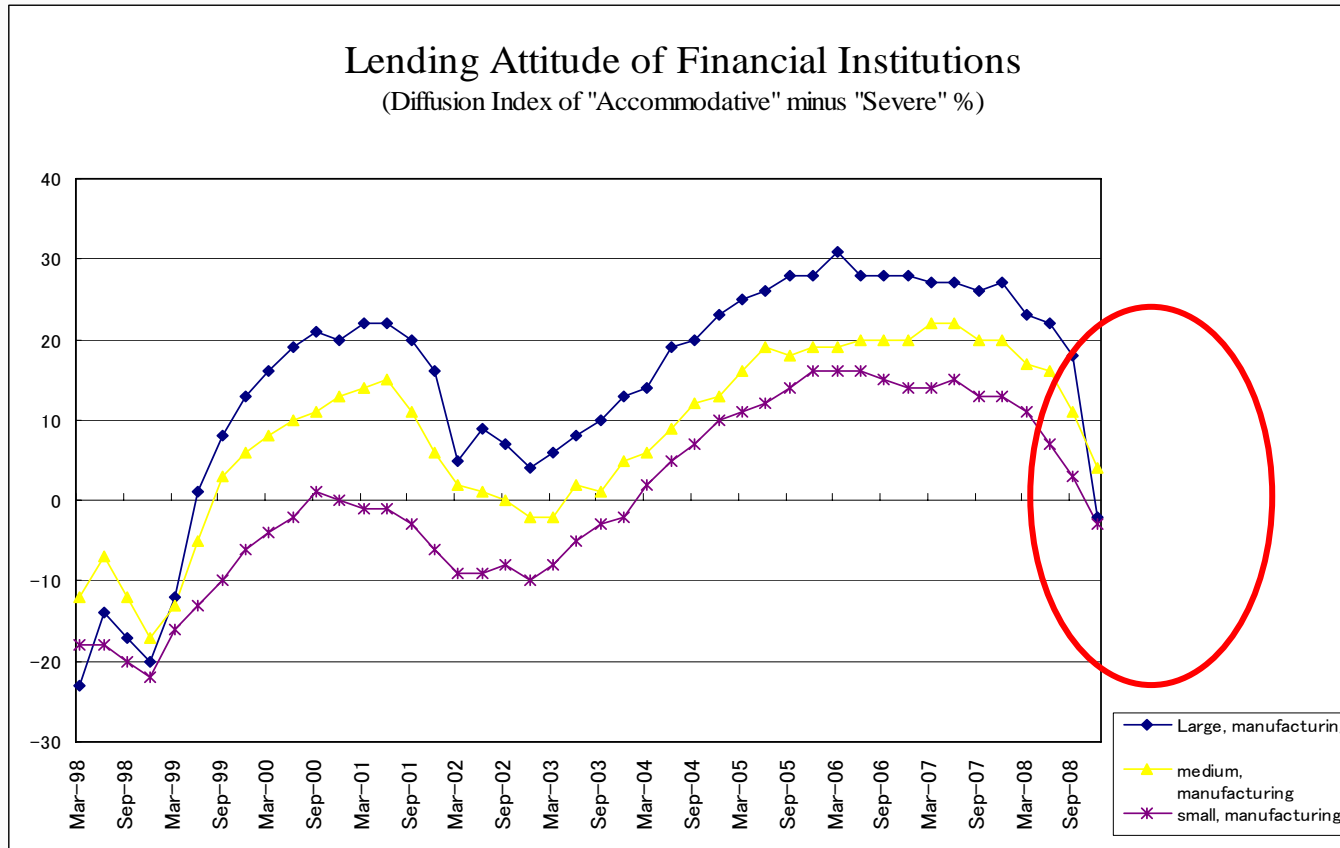
# Financial Condition: Manufacturing Sector



Source: Tankan (Bank of Japan)



# Lending Attitude of Financial Institutions



Source: Tankan (Bank of Japan)



# Main Issues

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1. Role of competition in the Financial Sector
  - Japanese experience after the 1997 Asian Crisis
  - Balance between competition and sector-specific regulation
2. Challenges for competition policy in the Economic Crisis
  - Desirable to use competition policy as a constraint on how regulation is implemented by FSA.
  - Need “Double filter” system both for national and international regulatory oversight.

# Japanese Experience after the Asian Crisis

- Japanese banking sector, at the levels of both retail and wholesale, was heavily regulated in the past.
  - Japanese “Big Bang” in the financial sector, started around 1997, has promoted competition among banking, securities and trust businesses.
  - Competition Policy has also been strengthened in the banking sector. E.g.,
    - JFTC sanctioned on the transactions of interest-rate swap.
    - JFTC reviewed merger cases of large banks.
- ⇒ Competition policy is used to control unregulated segments, while regulation controls the rest.

# Competition policy and Regulation

- It is known that the financial sector exhibits the features of “market failure:”
    - Network Effects, or two-sided market, and Switching Cost (Payment settlement)
    - Asymmetric Information (Liquidity provision; Securitization)
  - Technical issues should be left for FSA. However, it may be a mistake to just throw away competition policy entirely.
    - Indeed, Japanese experience shows that competition has improved the output price (such as interest rates) and enhanced the service quality (accessibility of ATM) at the retail level.
    - Fear of regulatory capture.
- ⇒ It seems to be desirable to have both competition agency and sector-specific regulator jointly oversee the financial sector.



# Challenges for competition policy in this Economic Crisis

- To protect financial stability against systemic risk, state aid may eventually be unavoidable.
  - How about state aid in other industries?
  - Safeguard policy, if implemented, should be committed temporary, for it to be effective.
- Role of Competition Policy
  - The more one values financial stability, the more one has to sacrifice financial innovations.
  - Competition agency should remain to remove inefficiencies, promote innovations, and check against distortion created by state aids or mergers.



# Looking forward

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- After the LB shock, there appear to be mounting calls for tighter regulation on banks.
- In structuring an efficient regulation scheme on banks, it is a key to assign tasks to both competition policy and regulation.
  - Specialized industry knowledge is necessary to regulate the financial sector. But need to recognize inefficiencies associated with regulatory capture.
- Thus, it may be desirable for a nation to use competition policy as a constraint on how regulation is implemented.
  - This “double filter” process would presumably lead to a better scheme for regulating the sector, which avoids harms caused by jurisdictional monopoly.
    - Coordination between competition policy and sector-specific regulation.
    - Coordination between national and international regulatory oversights (to eliminate incentives for regulatory arbitrage and negative spillovers)





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*Thanks for your attention.*

