State of Corporate Groups in Japan
the 7th survey report

May 18th, 2001
the Fair Trade Commission

1. Purpose of the survey

The Fair Trade Commission of Japan has been conducting surveys of so-called six major corporate groups since fiscal year 1977. The groups of companies maintaining tight-knit relations through capital investment and disaptch of executive officers within group exert great influence to the Japanese economy, affecting competition.

In addition to the points cited in previous reports,the 7th survey aimed also at finding how changing business environment, including the reorganization of the banking sector, affects relations of companies within group.

2. The companies covered by research

The survey was done by questionnaires sent on October 30, 2000 to 180 companies that are members of the meeting of presidents (*shachokai*) of the six groups. The period covered by the research was the latest fiscal year (or the end of the latest year).

3. Findings

The findings of the survey are shown in an attached paper.

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I. Introduction

During the post-war dramatic economic recovery and rapid growth period, Japanese corporations were active in forming corporate groups and six major corporate groups emerged: Mitsui, Mitsubishi and Sumitomo, Fuyo, Sanwa and Dai-ichi Kangyo Bank groups. The first three groups originated on pre-war *zaibatsu* while the last three are those formed around banks.

Led by both banks that provide financing and *sogo-shosha* (general trading companies) that coordinate business deals, the six major corporate groups are made up of leading companies representing key industries of Japan. They are said to be maintaining tight-knit relations through cross-share holdings and exchanges of executive officers within their groups.

The six major groups exert great influence to the Japanese economy, more or less affecting competition so that the Fair Trade Commission of Japan has been conducting surveys since 1977

The 7th survey aimed at finding how changing business environment, including the reorganization of the banking sector, affects their relations within the groups. It covered 180 companies that are members of the meeting of presidents (*shacho-kai*) of six groups. Questionnaires were sent by mail on October 30, 2000, asking them to answer questions based on figures and situations at the end of the latest business year.

To conduct the survey, the commission held seven meetings of the study group between September 2000 and April 2001 that discussed the survey methods and the interpretation of findings.

II. Findings

1. Status of the Six major corporate groups in the Japanese economy

A total of 151 member companies of the Six Major groups, excluding banks, held 13.15 percent of the total capital of the Japanese companies in 1999, down 0.94 percentage points from the previous survey of 1997. Their capital totaled 10,717.7 billion yen. In terms of total assets, they held 11.21 percent with 144,032.9 billion yen, down 0.22 points from 1997. In terms of sales, they were 10.82 percent of the total with 149,755.9 billion yen, down 1.72 points. The figures indicate that the combined business scale of the corporate groups of only 151 companies still remained large in the Japanese. However their status in the Japanese economy has been declining after hitting the peak in 1989.

2. Ties among companies within groups

Companies tied up each other through cross-holding of stocks, exchange of board members, exclusive business transaction and financing within groups. By and large, however, the ties are weakening.

(1) Capital relations

(A) The ratio of member of firms whose stocks are owned by each member company within a corporate group.

One in two companies in corporate groups owned stocks of affiliates in the same group. The survey found that 181 member companies of the six groups, excluding life insurance companies, held stocks of 54.53 percent of the companies within the same group, down 0.56 percentage points. Since fiscal year 1985, the level of shareholding has remained unchanged.

The companies of prewar zaibatsu-origined groups, held more shares of affiliates than those of bank-centered groups. It was found that former zaibatsu companies owned shares of 75.85 percent of the group companies, down 0.26 percentage point, while the latter held shares of only 33.22 percent, down 0.84 points, of the other companies within groups.

It should be noted, however, that city banks, flagships of corporate groups, had capital relations with almost all affiliates within the same group. The survey found that the banks were shareholders of 92.20 percent, down 0.51 points, of the firms of the same group. On the other hand, another leaders, general trading companies had the shares of 69.46 percent, down 5.04 points, of the affiliates within the same group.

(B)The average ratio of intra-group stock holdings per group firm

The companies owned an average of 1.38 percent of affiliates. The ratio remained unchanged from the previous survey. It has been declining since 1977 when an average stock ownership was 2.19 percent.

City banks, meanwhile, owned more than 4 percent of affiliates' stocks. Some of them controlled nearly 5 percent, the maximum allowed by the Antimonopoly Act. The survey found that the average share holding increased to 4.66 percent from a previous 4.30 percent. The acquisition of Yasuda Trust and Banking by Fuji Bank and that of Kankaku Securities by Dai-Ichi Kangyo Bank contributed to the increase of the average stock ownership of banks the amount of stocks held by affiliates has been decreasing in general, if these case are excluded.

It was 1.46 percent, down 0.03 percentage point, among companies of prewar zaibatsu-origined groups while it was 1.29 percent, up 0.03 points among bank-centered groups, compared with 2.16 percent for prewar zaibatsu-origined groups and 2.22 percent of bank-centered groups in 1977, respectively.

(C)The ratio of stocks of one member company owned by the other member companies within one group

Of the combined outstanding stocks of the six major groups, an average of 20.05 percent, down 1.32 percentage points, were held by companies of the same group. The ratio has been decreasing since 1981 when it hit the peak of 25.48 percent.

The survey found that prewar zaibatsu-origined groups owned more stocks than bank-centered groups. The former owned 24.95

percent, down 1.86 points, of the total outstanding stocks while the latter, 15.16 percent, down 0.77 percent. Among the former, the percentages have been decreasing since 1981 when it hit the peak of 32.21 percent. Among the latter, it has also been declining since 1979 when it hit the peak of 19.14 percent.

(D) Major shareholders

59.97 percent of the principal shareholder, down 2.47 percentage point, of 181 companies surveyed, were affiliates within the same group. Moreover, 56.40 percent of the top three shareholders, down 5.74 percent, were dominated by companies of the same group. Those percentages have also been decreasing since 1992.

Companies of Mitsubishi and Sumitomo groups were found to be owned by affiliates more than other groups. The principal shareholders of 88.00 percent of Mitsubishi companies were affiliates although the figure went down by 4.59 percentage points. Of Sumitomo companies, 73.68 percent, down 21.06 points, had the principal shareholders who are affiliates.

Mitsubishi companies whose top three shareholders were affiliates accounted for 81.33 percent, down 6.32 points, of the total. Among Sumitomo companies, it was 70.18 percent, down 15.78 percent. Compared with the findings of the previous survey, the ratio declined.

(E)Cross-shareholding within groups

According to the NLI Research Institute's "The Fiscal year 1999 Cross-Shareholding Survey," the cross-shareholding ratio of companies affiliated with the six major corporate groups has been declining since 1990. In fiscal year 1999, it fell to 20.25 percent. Yet, it is still much higher than non-affiliated companies whose cross-shareholding ratio was 6.77 percent.

The cross-shareholdings among six major companies unwound minimally. It appears that cross-shareholdings among non-group companies have gradually been unwounded, but those among corporate groups have not.

Meanwhile, cross-shareholdings among all of the publicly traded companies has been declining since fiscal year 1990 when it hit the peak. Particularly after fiscal year 1997, declining accelerated. In fiscal year 1999, the ratio stood at 10.53 percent in terms of value. By and large, companies continued to unwind cross-shareholdings as both banks and business companies (reduced them).

The survey found that as many as 95.9 percent had cross-shareholdings with other companies. But 62.1 percent said that they plan to reduce them, or they intend to reduce them but not completely.

What are priorities when they unwind cross-shareholdings? A total of 64.4 percent said that cross-shareholdings with outsider non-financial companies should be given priority, followed by 46.0 percent who said with outsider financial companies, 18.4 percent who said with insider financial companies and 13.8 percent who said with insider non-financial companies.

(2) Dispatch of executives

Of the six major group companies, 37.17 percent, down 11.43 percentage points, accepted board members sent by affiliates. As shown by Chart 9, the ratio has been decreasing. Prewar zaibatsu-origined groups received more executive officers at their boards from affiliates than bank-centered groups.

Among the board members of the six major groups, an average of 4.17 percent came from affiliates, up 0.45 points from the previous survey.

In most cases, they received more directors from banks than any other affiliated companies. The numbers of bank executive officers sent to affiliated companies' boards hit an all-time high in 1987 and they have since been decreasing, but the survey found the trend has reversed. The companies having ex-banking officers in their boards accounted for 16.00 percent of the total, up from 12.31 points and the directors sent from banks accounted for 0.83 percent of the board members, up from 0.44 points. Hearings of the polled found that the increases were attributed to the increase of outside directors.

(3) Business relations

(A)Industrial companies

Business transactions among affiliates have been decreasing in general. Among the six major groups, the purchase from insider member companies accounted for an average of 6.44 percent of the total purchase, down from 7.47 percent in fiscal year 1996. Among prewar zaibatsu-origined groups, the ratio stood at 8.09 percent while it was 4.93 percent among bank-centered groups. The major part of in-group purchases were those with general trading firms, but the survey found that the transactions with affiliated general trading firms declined to 5.30 from a previous 6.31 percent. It indicates that the share of general trading companies has been decreasing in business transactions among group companies.

(B) Financial companies

Financial companies extended loans to 73.46 percent of the affiliates, down from 74.53 percent in 1996. The loans to affiliates by city banks also decreased to 85.79 percent from 89.20 percent. Meanwhile, the loans to the affiliates accounted for 3.53 percent of the total, up from 3.27 percent. The loans to the affiliated companies extended by city banks also increased slightly to 2.33 percent from 2.12 percent of the total loans.

The figures indicate that financial companies, facing declining confidence in the country's financial system and following financial contraction, increased their loans to affiliated companies within group while reducing the overall amount of loans. Those city banks which are in corporate groups, for instance, increased their loans to affiliates by 8.1 percent compared with 1996 while decreasing the total loans by 2.1 percent. (Loans by city banks accounted for 46.0 percent of the total domestic loans by banks, while it was 44.6 percent in 1996.)

What the survey found suggests that financing companies became very selective in extending loans even to affiliates in the same group, and intensified relations with selected affiliates.

(4) Alliances

Alliances were not limited to affiliates in the same business group.

Of all the alliances, as many as 96.7 percent were found to be with outsiders. Those within the same business group accounted only for 3.3 percent. Of the collaboration with outsiders, including foreign companies accounted for 16.1 percent.

Within group, no companies are typically in rivalry with others as every member of the group involves in different lines of business. Alliances are usually agreed among companies in the same business field and there are limited number of candidates for alliances. As a result, partners for collaboration tended to be those outside corporate groups.

What types of collaborations were formed with outsiders? Collaborations in sales topped the list with 32.7 percent, followed by technological cooperation (28.3 percent) and cooperation in research and development (19.9 percent). Among affiliated companies, research and development was the major field of collaboration with 31.6 percent, followed by technological cooperation (29.8%) and sales tie-up (18.2%).

It may not be significant to simply compare types of collaboration when there are great differences in the number of cases between the two groups.

In the field of research and development or technology, however, it would probably be easier to collaborate with companies in different business lines, so that there were more cases of cooperation among affiliates in the same groups. Actually, some companies of the meeting fo presidents said to the poll that one of benefits of their regular meetings is finding opportunities to participate in joint research and development programs.

III. Benefits of forming corporate groups

The backbone of corporate groups is *shachokai*, meeting of presidents of the companies in the same group. What are benefits of such meetings? “Exchanges of information” topped the list, followed by “utilization of accumulated business expertise and know-how of affiliates.” Among prewar zaibatsu-origined groups, “enhancing corporate credibility through the common brand” was cited as another major purpose of presidents’ meetings. Actually, a recent merger case of two prewar zaibatsu-origined banks indicated their strong attachment to their traditional brand names as the names of two prewar zaibatsu-origined groups were put together to create the new name of the bank. Raising credibility is included in the purposes of shachokai and its brand committee.

As to corporate management, 19.1 percent of the surveyed said that they have received some sort of approach from their affiliates. Prewar zaibatsu-origined groups were found showing more concern to their affiliates than bank-centered groups; 30.9 percent of the prewar zaibatsu-origined groups replied they have received some kinds of approach from affiliates while 11.8 percent of bank group companies said so.

Offers of financial assistance at the time of poor financial performances was the most common form of approach from affiliates; a total of 20 companies said that they have received it. Financial assistance included the acceptance of new shares and the extension of the payment due date. It indicates that corporate groups, particularly prewar zaibatsu-origined groups, still maintained the function of mutual support to affiliates facing a financial crisis. Other common supports included coordination and advice to joint projects (10 companies) and coordination and advice on business affiliation involving stock acquisition.

IV Reorganization of the financial sector and corporate groups

The globalization of economy and on-going liberalization of the financial sector promote new entries into the financial sectors from non-financial sectors and abroad, intensifying the competition and accelerating large-scale reorganization of financial companies. The banks spearheading the six major corporate groups were no exception. Actually, Sakura and Sumitomo banks, Bank of Tokyo Mitsubishi Bank and Mitsubishi Trust and Banking (and Nippon Trust Bank), Fuji and Dai-ichi Kangyo banks (and the Industrial Bank of Japan), and Sanwa Bank and Toyo Trust & Banking (and Tokai Bank) have merged.

(1) Impact to corporate groups

As to possible impact of the reorganization of the financial sector, 34.4 percent of the surveyed said that current corporate groups would be maintained. But 18.4 percent said the roles of corporate groups would be weakened and they would eventually remain only in name while the same number said that relations among affiliates would be strengthened.

The perception of possible impacts differs from one group to another. Among DKB and Fuyo groups, it was the dominant perception with 34.8 percent that the role of the group will be declined. Among Sumitomo and Mitsui groups, on the other hand, 40.7 percent said that the current roles of the group would be maintained and 37.0 percent said that the relations among the affiliates would be strengthened.

Such difference may derive from the history of groups. Bank-centered groups were formed by companies that received loans from the same bank. Those companies do not have common trade marks, and their relations are rather loose. Moreover, the banks, flagships of the group, are reorganized after the merger.

On the other hand, many ex-zaibatsu companies think that the value of groups' trade marks would remain unchanged. And the merger of their banks would make the relations of the two groups closer. Particularly, Mitsubishi group; as many as 90.9 percent think that the current group would be maintained. It is partly because the mergers involved only banks within group.

(2) Impact of banking sector reorganization to industrial reorganization

The 70.7 percent of companies surveyed said the reorganization of the banking sector would not trigger the reorganization of the industrial sectors. But 9.5 percent said more partners for joint projects would be introduced, and 7.8 percent said that more improved joint projects would be proposed by banks because they could know more joint prejects. They viewed that the integration of banks would increase options for business affiliations beyond the framework of the traditional groups. As a result, it is probable that following in banks' footsteps, companies seek mergers and affiliations with companies of another group.

What should be noted is that some groups try to reform their groups by, among others, changing the current style of grouping led by banks. Moreover, some banks said that they would not take initiative to strengthen or expand the ties among the affiliates nor to support and promote the integration of the affiliates. We should carefully watch the development.

Conclusion

The status of six major corporate groups in the Japanese economy, as shown by the survey findings, has relatively lowered. By and large, moreover, such bonds as capital, personnel and business relations that bring affiliated companies together has been weakening.

The survey found that exchanges of information is considered the major raison d'être of shachokai or the meeting of presidents of the group. Prewar zaibatsu-origined groups cited that the group’s common brand name contributes to upgrade the credibility of the companies. It also provides support to affiliates, particularly financial support to group companies facing financial difficulties.

Many companies surveyed believed that current corporate groups would be maintained regardless of the reorganization of the banking sector. As to the future of the corporate groups, however, the survey found two opposing views. Many companies under bank-centered groups predicted that corporate groups would lose power while many prewar zaibatsu-origined groups believed that relations among affiliated companies would be strengthened.

As to impacts of the reorganization in the banking sector to industries, many said the mergers of banks would not trigger the reorganization of the industrial sector but the number of possible partners for joint projects would be increased. Some companies try to reform their groups by, among others, changing the current style of grouping led by banks. Moreover, some banks said that they would not take initiative to strengthen or expand the ties among the affiliates nor to support and promote the integration of the affiliates. We should carefully watch the development.