Ten Biggest Financial News Stories of '96

By Sakamoto Sakae

In December of last year, *Jiji Press* announced its selections for the top 10 financial news stories of 1996. They included two stories related to macroeconomics, such as interest and foreign exchange trends— "Bank of Japan (BOJ) continued low– interest policy" and "Strong yen takes root as surplus falls and interest rates remain low." Three were related to financial and insurance system reforms—"Prime Minister Hashimoto announces Japan's own 'Big Bang' plan," "Advisory body to the prime minister submits report on BOJ Law revision" and "Life and nonlife insurance firms enter each other's business turf."

The other five stories were connected with winding up the post–bubble economic situation. "Cleanup of *'jusen'* housing loan companies begins," "Resolution and collection Bank (RCB) set up to take over failed financial institutions," "Bank failures continue," "Bank scandals take place one after another," and "Illegal U.S. bond trading forces Daiwa Bank to withdraw completely from the United States."

The BOJ's official discount rate hit a historic low of 0.5% in September 1995. Though a year and four months have passed since, the BOJ maintains its "extreme low interest rate policy" as economic recovery still remains clouded. But the anxiety brought on then by the "deflationary high yen" has been completely overcome and there has been talk in financial circles about raising the extreme low interest rate to an ordinary low rate. Modification (raising the interest rate) is becoming a mainstream opinion even in the BOJ because lowering the interest rate to 0.5% was an emergency safety measure against deflation and because the fear of deflation has already subsided.

Politicians too are speaking out in favor of raising interest rates as interest on savings and the like were near 0% without exception which put pressure on pensioners. In the past, politicians have usually demanded lower interest rates in consideration of business operations while the financial authorities have opposed rate cuts. This indicates that the current rate of 0.5% is extraordinarily low and we can expect that an interest rate increase will come shortly.

In April 1995, the going rate of the yen reached an all–time high of ¥79 to the dollar. By October 1996, it had come back down to about ¥115. Primary factors of the drop include a reduction in Japan's external surplus, maintenance of the extreme low interest rate policy, the stance of the U.S. monetary authorities to welcome a higher dollar and the healthy U.S. economy and stock market. Some market sources predict that the yen would fall to the order of ¥120 or ¥130 to the dollar on the ground that Japan's surplus would continue to drop and the extremely low interest rate policy would be maintained for the time being. Nevertheless, there are those of the opinion that "currency adjustment will take a breather and the exchange rate will move around ¥110 to the dollar for now."

As reasons for this view, they cite an increase in Japanese exports caused by a cheaper yen, U.S. export industries' concern over the current yen–dollar exchange rate and subtle changes in the Japanese and U.S. monetary authorities. Keidanren (Federation of Economic Organizations) Chairman Toyota Shoichiro (president of Toyota Motor Corp.), in perceiving these changes, states that "currency exchange at ¥100–110 to the dollar reflects Japan's actual economic power."

2001 eyed for Japan's own 'Big Bang'

The second Hashimoto Administration (the first was a coalition, while the second is formed solely by the Liberal Democratic Party) that started after the general elections last fall announced in mid–November the outline of financial system reform, which would make the Tokyo market as liberalized as the London and New York markets by the year 2001. After the major financial and securities market reforms in Britain, the Japanese mass media calls his reform plan "the Japanese version of the Big Bang."

Prime Minister Hashimoto's primary thought is this: "To maintain vitality in the Japanese economy as it faces an aging population in the 21 century, it is imperative that the nation's assets be used more profitably, and funds be supplied to growth businesses that shoulder the next generation. And, in order for Japan to make due contributions to the world, the country needs to supply funds smoothly to the world. To this end, it is necessary for the financial market, which governs the flow of the lifeblood of the economy, to fully play its primary role of ensuring optimum allocation of resources."

To make this objective a reality, Hashimoto advocates three principles— "an unrestricted market where the market mechanism works (Free)," "a transparent and trustworthy market (Fair)" and "an international market that is ahead of the times (Global)." Specifically, he cites "promotion of mutual entry into one another's business turf by banks, securities houses and insurance companies," "removal of product regulations based on the separation of long– and short–term finance," "liberalization of stock brokerage and other commissions" and "a review of asset management regulations and thorough implementation of disclosure." The next five years should see reform of Japan's financial system progressing along these lines.

Reaction in the financial world to Japan's Big Bang plan is mixed. Those wanting to protect the established order are concerned about intensified competition with foreign banks and among domestic financial institutions resulting from the removal of the "fence" that lies between long– and short–term finance and financial and securities businesses. Financial circles also express dissatisfaction with the exclusion from a review of public financial services and institutions like postal savings and government–affiliated financial institutions. Protected by regulations, public financing with low cost of funds is becoming the rival of private financial institutions.

Photo: Kyodo News Service

Central Bank Research Committee Chairman Torii Yasuhiko submits report on financial system reform to Prime Minister Hashimoto (November 12, 1996).

Legal reform for an independent BOJ

One of the top 10 stories along with Japan's Big Bang is "Revision of BOJ Law," a move to change Japanese financial policy. The November report put together by the advisory body "Central Bank Research Committee (chairman Torii Yasuhiko, president of Keio University)" to Prime Minister Hashimoto indicates the basic direction for reforming BOJ Law. The report is titled, "Reform of the Central Bank System—Seeking Open Independence." The report points out that the BOJ Law (established during World War II and its purpose was to execute an all–out war) cannot meet the demands of the times due to changes in the economic and financial situations, such as the expansion of the direct financing market, advancement of financial techniques and globalization of economy. It calls for "the BOJ's independence," "transparent policy management" and "open independence" as goals for BOJ reform.

With regard to independence, the report says: "Ensuring the independence of the BOJ is the most important issue. This is only natural in view of the spreading perception that the independence of the central bank is necessary also in the field of monetary policy, which is based on historical experiences and recent theories. In Europe, too, there are moves to review the relationship between the government and central bank in connection with the planned unification of currencies." As for the clarity of policy management, it says: "The approaching 21st century will be marked by advanced information orientation and globalization and emphasis on the market mechanism. In these circumstances, opaque monetary policy management makes it difficult to obtain the global market's understanding of the Japanese monetary policy. Transparency is thus indispensible for Japan's monetary policy to gain confidence of the global market and function effectively." At the same time, the report notes that "the BOJ is required to have transparent independence, i.e. open independence," in order to keep itself from falling into self–righteousness.

The ever-present hold of the Ministry of Finance

Discussions at the Torii committee focused on how to make the BOJ, now virtually a part of the Ministry of Finance, independent (how to separate the central bank from the ministry). As a result, "independence" was incorporated in the report as the top priority issue. But the Ministry of Finance is still trying to keep "general supervisory rights" and the "right to approve the BOJ's budget," and independence should be interpreted as "restricted" independence. Former officials of the central bank are apparently aware of this and one of them says coolly: "It is not realistic to completely remove the government's supervisory rights. It should be enough if the reform serves as an opportunity to arouse public opinion on the BOJ's independence."

The specific degree of independence (currently, they are distanced by a meter, but will that extend to five? Ten meters?) will be decided upon by the Financial System Research Council (advisory body to the finance minister) in January to February this year. In the current schedule, the revised bill is due for Diet submission in mid–March. Nevertheless, how far the BOJ can actually be independent depends on how well it can maneuver under the new law, not the report on the new law.

Management of the post–bubble economic situation was placed on track with the establishment of the RCB, which takes over the assets and debts of failed financial institutions, and an organization to take over housing loan companies (so–called jusen), part of nonbank financial institutions, to recover their loans, It now depends on how financial institutions can write off bad loans without much strain on themselves and how smoothly they can recover loans in arrears. This is a few years of work, and financial journalism's interest in the work is sure to wane.

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