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The Need for a Grand Design for Industrial and Corporate Revitalization

— The Integrated Revitalization of Finance and Industry —

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Overview

I. The Essence of the Non-Performing Loan Problem

The essence of Japan's non-performing loan problem lies in the excessive debts and low profitability at the industrial and corporate levels. Overcoming the non-performing loan problem will require the reduction of excessive debts at both industrial and corporate levels and the enhancement of corporate profitability through business restructuring. A closer examination of the excessive debts facing companies in terms of the ratio of long-term debt to cashflow reveals the following facts:

- Although steady progress is being made with the reduction of excessive debts, their total amount is still higher than the average level recorded in the 1980s, currently standing at ¥61 trillion for all industries.
- At the individual company level, the cashflow ratio of small- and medium-sized companies is rising, and it is important to realize that excessive debt is not limited to a few industries or major corporations but is also a serious problem for small businesses.

II. An Evaluation of the Industrial Revitalization Corp. and Issues for Further Consideration

The establishment of the Industrial Revitalization Corp. (IRC) incorporated in the recently announced “anti-deflation package" is praiseworthy in that it is a clear signal of the government stance that the revitalization of the financial sector and the restoration of industry are two sides of the same coin. The effectiveness of the IRC, whose mission is to stabilize the financial system and support industrial and corporate revitalization, depends on the following:

- The IRC must not become a "company screening mechanism", nor yet a "company life-extension mechanism". Its role should be to enhance the potential for rebuilding of companies whose survival is judged to be of value to society. To ensure the objectivity of the criteria used to decide which companies should be rehabilitated, a scoring system, incorporating non-financial indicators as well as financial indicators, should be adopted, but the main effort required for the rehabilitation of companies should come from the private sector.
- The scope of loans qualifying for buying-up operations should include not only loans "requiring control" where the borrower is a major corporation, but also loans to borrowers in danger of failure, including small- and medium-sized companies, and other borrowers "requiring caution". To assuage public fears over the stability of the financial system, the partial buying-up of non-performing loans from main banks as well as non-main banks, should be allowed. The loan acquisition prices should be based on an effective book value reflecting the value of the company's survival.
- The role of the IRC should include facilitating the supply of funds, credit enhancement of borrowers, and the support of business reconstruction. Besides investing in and forming business tie-ups with corporate rehabilitation funds established by private-sector financial institutions, it should make full use of private sector know-how and human resources relating to funding and corporate revitalization, including foreign funds, such as private equity funds and buyout funds. It is to be hoped that the IRC will play a leading role in the fostering of an ABS market and a market for the securitization and trade of non-performing loans by securitizing the debts and assets it buys up and selling them on to the private sector.

As to the scale of the buying-up funds commanded by the IRC, assuming certain conditions, a funding framework of a maximum of ¥15 trillion should be established.

III. The Need for Comprehensive Measures for Industrial Revitalization

To enhance the effectiveness of the industrial and corporate restoration functions of the IRC, comprehensive measures for industrial revitalization should be compiled. This should involve:

- the expansion and strengthening of the industrial revitalization law and the creation of an "industrial reorganization program" aimed at resolving the excessive debt-excessive supply structure of specific industries,
- as an interim measure for the next two years, the creation of a special budget framework to help revitalize industries and assure employment, with a total value of ¥5 trillion (four strategic industries including the IT sector, urban renewal projects and an employment safety net), and
- the introduction of a range of taxation measures to support the integrated revitalization of finance and industry. Specific measures required include preferential tax treatment to support reorganization, a strengthening of measures to foster venture businesses and support the establishment of new enterprises, and measures to help speed the disposal of non-performing loans.