

THIS REPRESENTS THE TITLE OF
THE THESIS

Japanese Banks' Mergers and Acquisitions: Competitive Advantage &
Organizational Recovery through Strategic Relatedness and Resource
Orientation

by

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Abstract

In late 1990s, diversification was the name of the game for the Japanese banking sector. The problem in the Japanese financial system started on December, 29, 1998 with the burst of the bubble economy which resulted in Yen 75 trillion of non-performing loans among the financial sector. Simultaneously, Japanese policy makers as well as the banking institutions launched a massive restructuring, *risutora* drive. This study, exploratory and descriptive in nature is based on eight interviews conducted in Japan on the five Japanese mega-bank M&As. The motivations, strategic fit and resources that play a critical role towards providing a competitive advantage and organizational recovery for the Japanese mega-bank engaging in the M&A activity are presented in case study style, with a multi-cross case analysis. A conceptual model was derived from the literature, tested through this research and adapted in light of the Japanese bank M&A strategies. The results suggest that the Japanese mega-bank M&As act as a source of influencing a competitive advantage but also in tandem act as a support mechanism in ‘pulling’ the Japanese banking sector out of the crisis mode and thereby providing financial recovery to the system as a whole. The ranking in terms of deriving a competitive advantage among the banks is placed in the following order Bank 1, Bank 2, Bank 3, Bank 4 and Bank 5. More specifically, the competitive advantage can be derived in terms of complementarily relatedness among the combining bank strategic assets; i) markets, ii) products and services; and iii) resource traits, organizational resources including leadership style and corporate culture; and physical traits such as IT systems integration, which rose in terms of cutting costs by reducing unwanted resources. Simply put the integration level, strategic relatedness and the types of resources are classified as strategic inputs and the benefits acquired for a competitive advantage and organizational recovery are defined as strategic outputs. Secondly, the study maintains that with the change in traditional Japanese banking practises, the era of 2000 is defined by diversification i.e. M&A strategy adopted by Japanese banks in terms of strategic fit, and types of resource but also where the resources are derived from. In other words, the source of the resources where the resources are derived from i.e. combining, new and their uniqueness also acts as an imperative indicator for

Japanese mega-bank M&As. Resources prominent among the Japanese mega-banks are i) *keiretsu* (client resources); ii) organizational (management and leadership; knowledge; culture; and human resources); iii) physical (IT systems; branch networks and other real estate assets); iv) strategic (markets and products and services) and v) financial (capital markets and cross-shareholding patterns among *keiretsu* and main bank affiliates). Thirdly, these banks display a unique quality - the 'dual role' that strategic relatedness traits not only act as a combination potential but also act as resources and vice versa. The motivations include government de-regulation; non-performing loans of banks; over-crowding in the banking industry; and size competitiveness and diversification; via capturing markets, increase in profitability; and aligning with the changing needs of the Japanese clients. The research also aims to bridge the gaps in Japanese banking literature by building our understanding on how the Japanese banking sector has distanced itself from the traditional banking culture since the de-regulation wave instigated in Japan in mid to late 1990s. While there has been change in terms of financial cross-shareholdings, the traditional ties in terms of sharing strategic resources continues, introducing out-side directors, breaking away gradually from the *amakudari* systems and the long term employment and seniority based-wage system. The Japanese banking sector learnt from its mistakes and therefore, has not only been able to escape from the sluggish international banking environment of late but has also been able to diversify into cross-border investments and act as a learning source for the global financial institutions which has been in a state of perils since 2008, on the helms of sub-prime losses and failure of major investment banks.

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List of Acronyms and Synonyms

BTM	Bank of Tokyo Mitsubishi
DKB	Dai-ichi Kangyo Bank
FG	Financial Group
FRC	Financial Reconstruction Commission
FSA	Financial Services Authority
FTC	Federal Trade Commission
HLC	Housing Loan Corporation
HEC	Human Ethics Committee
HR	Human Resources
LTCB	Long Term Credit Bank
M&As	Mergers and Acquisitions
MoF	Ministry of Finance
MTFG	Mitsubishi Tokyo Financial Group
MUFG	Mitsubishi UFJ Financial Group
NPLs	Non-performing loans
SESC	Securities Exchange Surveillance Commission
SMBC	Sumitomo Mitsui Banking Corporation
SMFG	Sumitomo Mitsui Financial Group
RBV	Resource Based View
UFJ	United Financials of Japan

Chapter 1

Introduction

1.1. Overview

Banks have been conducting international banking and finance since time immemorial. Globalization and competitiveness, coupled with an increasing interaction between businesses and governments, have strengthened the role of financial markets (Berger, 2000).

Corporate strategy is a domain illuminating the motivations of organizations willingness to diversify in order to keep abreast of the competitive demands of the 21 century. Corporate restructuring presents a platform for financial integration such as mergers, acquisitions, take-overs, amalgamations, divestments, management buy-outs, carve-outs, spin-offs, sell-off, spin-outs (entrepreneurial spin-offs), carve-out, split-up, closure, seizure, relocation and spinouts are important features of corporate restructuring (Berger, 2000). Therefore, globally, corporate restructuring plays a critical role in the growth of banking business.

Japan has travelled through a very successive growth period after World War II. 'Real GDP growth rates averaged 10% from 1955 through the 1960s, 5% during the 1970s, and 4% during the 1980s and 1990s. Throughout this 45 year period the country enjoyed high income, high income equality, low crime rates, low unemployment rates, strong export rates, a strong currency, and a growing current account surplus' (Suetorsak, 2007; pp. 268).

The Japanese financial system has taken many twists and turns since it's inception after the restoration of the Meiji era in 1868 and with the introduction of the National Bank Act in 1872. The Japanese financial system is built around a set of unique characteristics which were carried gracefully up until the late 1990s.

The Japan specific banking traits are, firstly at the industry level, i) extension of plain vanilla loans and cross-shareholdings by the *keiretsu* corporates in their main banks and vice versa upto 5% as defined by the anti-monopoly law; ii) long-term employment system and seniority based wages; iii) *amakudari* system, whereby MoF retired officials

take up positions in the banking system; and, secondly, at the macro-economic level, i) banking sector regulated by the Ministry of Finance (MoF); ii) MoF safety net and convoy system; iii) post-bubble crisis in 1990s with the implementation of de-regulation; and iv) introduction of enhanced M&A structures, and accounting and disclosure laws. In a nutshell, these characteristics provide a distinct platform for the Japanese banking and financial system as compared to other global financial systems.

1.2. Origins of the Financial Crisis

In 1988, Japanese banks accounted for all of the 10 largest banks in the world. It was considered as the pillar of strength of ‘Mighty Japan’ and a symbol of Japan Inc., and often regarded as a model to be emulated by other countries (Chapter 3).

In the early 1990s, the Japanese economy was classified as a ‘bubble economy’ reflecting the strength of the Japanese manufacturing sector, with land and stock prices nearly doubling their value. In 1992 the land myth seemed to have dissipated, losing close to 20% of their value by 1992 and 60% by 1997. On December 29th, 1989, the stock market peaked at Yen 38,957.44 and as the Japanese government increased interest rates, the bubble burst creating an asset deflation mood. Banking sector was heavily entangled with NPLs as loans were extended based on real estate as collateral, and with the market crash, there were no bidders when attempts were made to auction the land (Posen, 2003).

1995 onwards, the ‘tide ebbed’ and the number of Japanese banks counted among the world’s largest fell to 5 of the top 10 (Chapter 3). By 1997, Ministry of Finance estimated 76.7 trillion yen, worth of bad loans, 12% of total bank loans and credits (Patrick, 1998). 30% of which was accounted by Dai-ichi Kangyo bank, Fuji Bank and Industrial Bank of Japan. This was just the beginning; with the collapse of the bubble economy came the failure of several large banks Sanyo Securities, bankruptcy of Hokkaido Takushoku Bank, and Yamaichi Securities in November 1998, and the once-powerful long term credit bank, and the *heisei* recession weakened the banking sector in

Japan (Miyajima and Yafeh, 2003). Moreover, industrial overcapacity, lack of transparency and disclosure, and change in the reduction of the cross-shareholdings among the banks and *keiretsu* affiliates also marked the beginning of the ‘lost decade’ for the Japanese Banks (Hoshi and Kashyap, 1999). The credit rating of Japanese banks was such, that in 1998, they had to pay an additional 1% as compared to western banks in order to borrow dollars on global markets.

The immediate remedy provided by the government was capital injection and deposit insurance of about USD 500 billion alongside USD 200 billion in aid to provide recovery and the collapse of the Japanese banking sector (Bremner; Sep 6, 1999). Japan’s leading banks were forced to allocate a large proportion of their profits towards provisioning of non-performing loans. Appendix 1 provides a timeline of the chronology of events concerning the Japanese financial sector.

Yoshifumi Nishikawa president of Sumitomo Bank explains that Japan is really changing now. ‘The old rules won’t come back now. Old rules? At the start of the decade, the MoF had undisputed control over every bank, broker and life insurer. Major lenders even maintained bureaus that wined and dined MoF bureaucrats to trawl for inside dope on competitors or to lobby to keep foreign players out. Bank lending used to be all about relationships not risk management. The government would be saying to us, well, now its up to you, you’ve got to get your act together, you’ve got to get your costs down, you’ve got to get your balance sheets into shape and that would be an enormous deal’(Bremner, 1999).

December 29th, 1989, with the bubble burst marked a beginning of change for the Japanese banking system, as many Japanese institutions in financial difficulty tended to restructure, *risutora* in order to improve their performance. Traditionally, Japanese companies were alien to the concept of *risutora* as it was often associated with job-losses and redundancies with the lack of systems and experience available in handling the M&A activity.

Consequently, in 1999 with the news of the first M&A consolidation announced among Dai-ichi Kangyo Bank, Fuji Bank and Industrial Bank of Japan, bank stocks soared 20% in the week following the merger announcement. Since then they have formed some of the world's leading and largest financial institutions – Sumitomo Mitsui Banking Corporation, Bank of Tokyo Mitsubishi UFJ, Mizuho Bank, Mizuho Corporate Banks and Resona Bank. Banking analysts predicted that if they continue in a similar vain in redefining the landscape of the banking and financial sector as a whole, then 'Japans sprawling banking industry will be slimmed down to a handful of sleek global contenders and a larger group of smaller banks that focus on domestic business. Hakuo Yanagisawa, head of Japan's Financial Reconstruction Committee, certainly hoped for a major consolidation as he wanted to see Japan's 18 money-centre banks to knocked down into four or five USD 1 trillion behemoths that can compete globally (Bremner, September 6, 1999).

It is widely acknowledged that under PM Keizo Obuchi, in December 1998, Yanagisawa and his team of 50 lawyers and bank examiners carried out a number of bold steps in order to revitalize the Japanese financial sector. They nationalized the two long term credits banks, and shut down four regional banks.

The M&A activity also presents itself as a defensive strategy adopted by Japanese banks in wake of fear that they may encounter foreign invasion or take-over of the Japanese banks. This was partly due to the fact that a number of foreign companies had been taking advantage of the Big Bang (please refer to section 3.4) to enter the Japanese market (Rowley, 1998; pp. 95). However, for the Japanese banks to survive the new competitive environment; Japanese banks had to learn to adjust; impart from the traditional roles of the lending into the new world of capital markets otherwise, it was prophesized that those financial institutions hard hit by the non-performing loans will be unlikely to survive the new domains of the financial system being invested through the reform programs.

1.3. Research Objective

In the context of Japan, the M&A program undertaken by the Japanese mega-banks as a measure to resolve the banking crisis of the late 1990s has given impetus for this research. The exploratory and descriptive nature of this study provides a platform to understand the concepts of corporate strategy and diversification in the context of Japanese mega-banks. Moreover, the motivation for this research resulted from the gap in literature as to what were the deciding factors for the Japanese mega-banks to adopt an M&A strategy, what kind of strategic relatedness and resources provided a competitive advantage to the Japanese mega-banks coming out of a crisis situation as a means of revival for the Japanese banking sector. The qualitative nature of this research is further motivated by the fact M&A research is primarily based on event studies and other quantitative methods, thereby this method based on multi-case study style will provide in-depth insights as to what transpired while Japanese mega-banks were integrating. Therefore, gaps are present both at a theoretical and practical level. A theoretical model was derived from the literature, tested through this research and adapted in light of the Japanese bank M&A strategies based on the findings of this research.

1.4. Research Outline

This thesis is divided into nine chapters, each representing a specific stage of the research process. The content of each chapter is briefly outlined below:

Chapter 1: Introduction

This chapter briefly provides an overview to the research, with the origins of the financial crisis in Japan and the objectives underpinning the research.

Chapter 2: Background - Japanese Financial and Banking System

This chapter discusses the growth of the Japanese banking sector, the M&A profile in Japan from 1990 to 2008, structural reforms in the Japanese M&A framework, the economic growth in Japan and the structure of the Japanese financial sector in Japan.

Chapter 3: Literature Review

This chapter presents a review of the literature based on corporate strategy and Japanese business and banking literature. Theories of M&As, strategic relatedness and resource based view are among the main concepts discussed. The Japanese banking literature focuses on the problems of the financial system, the traditional role of the Japanese banking system and *keiretsu* system alongwith the reform process post-financial crisis. These strands of literature lead to the identification of the research gaps and questions to be addressed through this thesis.

Chapter 4: Conceptual Model Building

This chapter presents a conceptual model derived through literature and to be tested through the findings of this research.

Chapter 5: Research Methodology

This chapter discusses the research design and qualitative methodology used for the thesis. The relevance for adopting such a methodology is explained, along with the strengths and weaknesses of this research approach.

Chapter 6: Case Studies

In this chapter, the findings, in a case study style are presented. The chapter provides a brief overview of the M&A characteristics of each bank, the planning strategy, motivational rational; strategic relatedness and resources providing strategic benefits for the Japanese mega-banks.

Chapter 7: Results: Analysis and Discussion

This chapter presents a cross-case analysis of the five Japanese bank M&As and how the findings relate to extant literature. A conceptual model that is developed through the literature review, is tested, and amended in the context of the findings on the Japanese mega-banks M&A activity, with implications for advancing the strategic management and Japanese banking literature.

Chapter 8: Implications and Limitations

This chapter focuses on the implications for the Japanese banking sector, policy makers, bank clients and the international community and M&A specialist. Furthermore, future researches that may be taken up with a set of limitations of this thesis are provided.

Chapter 9: Conclusion

This chapter provides a conclusion, summing up the key points of the research and how it provided a competitive advantage and organizational recovery for the banking sector in Japan.

Chapter 2

Background: Japanese Financial & Banking System

This section is split into five sections; i) the growth of the Japanese banking system; ii) status of M&As in Japan (1990-2008); iii) reform in M&A structures in Japan (1990-2008); iv) structural changes in the Japanese economy; and iv) the major financial institutions in Japan.

2.1 Growth of the Banking System in Japan

Japanese banking system takes roots from 1872 with the setup of the first National Bank Ordinance. The restoration of the Meiji era took place at the same time when Japan had seen itself in a state of transformation from a feudal state into a modernized industrial economy, following the foot-step of the westernized countries (Rowley,1998).

Until the 1920s, Japanese banking system was structured with hardly any regulation. In 1920s, with a series of banking crises taking place, especially the banking panic of 1927, the Japanese Government was pressurized into implementing tight regulations for the banking sector. After World War II the banking system in Japan took a definite shape. In the early 1950s, Japanese banks established overseas presence in the U.S. and U.K., under the supervisory authority of MoF, and therefore, overseas Japanese banking operations were limited and developed at a gradual pace. The main overseas business of the Japanese banks were twofold: i) remittances were sent home by Japanese immigrants in North and South America; and ii) trade finance as a result of the Japanese trading in which payments were settled in U.S. dollars.

In the 1960s, due to the increased demand for US dollar and the instigation of the dollar defence policy by the US government, the Euro dollar market expanded rapidly whereby U.S. bonds were issued by non-American companies to raise funds in the overseas markets. Consequently, the demand for US dollars by Japanese banks was fulfilled through the Euro dollar market, whereby, Japanese banks issued U.S. dollar bonds in order to raise capital and meet financing requirements. Dollars raised at the London branches of the Japanese banks were then sent to the headquarters of the banks in Japan. The U.S. funds then would be transferred to the overseas branches of

Japanese banks for use in the international trade payments. It should be noted that at the time Bank of Tokyo was the only Japanese bank specializing in foreign exchange. In 1970, the then largest Japanese banks in terms of deposits, Fuji Bank ranked nineteenth in Fortune list of fifty largest banks in the world; in 1969, its deposits, Yen 6.2 billion, were only 27% of those of the Bank of America (\$ 22.5 billion). However, the banking landscape in Japan began to change with the subdued effect of the Bretton Wood agreement (whereby international trade was conducted on a fixed exchange rate system) in early 1970s and the liberalization of Japanese direct foreign investment. Consequently, Japanese banks international banking activity expanded as the banks followed a number of their corporate clients overseas in providing them with banking services. In addition, to international trade finance whereby banks provide services to exporters and importers to mitigate their transaction risk, Japanese banks also lend loans to their customers in overseas markets. Simultaneously, as deregulation was taking place in the foreign markets, Japanese banks expansion into foreign markets became more prominent.

In 1980s, the appreciation in the Japanese yen further accelerated foreign direct investment by Japanese firms to North America and Europe, thereby, further boosting Japanese bank operations overseas. In 1986, the Cooke Committee of the Bank for International Settlements (a transnational body based in Basel, Switzerland, organized by ministries of finance and private banks) decided to implement an 8% capital adequacy ratio for all banks. This was designed to curb the international expansion of Japanese banks because Japanese banks were then obligated to reduce lending or raise new capital to meet this capital adequacy ratio to ensure a healthy balance sheet (Economist 1990).

In Japan, by mid-1980s, however, the corporate and banking sector landscape was changing due to the slow economic growth and therefore, corporates and other business entities appetite for financing through banks declined significantly. This behaviour was further accelerated by the fact that major Japanese export corporates had access to the Euromarket. This landed banks, both Japanese and foreign in Japan, in difficulty and therefore, providing an impetus for them to adopt other banking business alternatives in

Japan i.e. leasing, factoring, house financing, and consumer finance. In 1998, after the burst of the bubble economy and banking crisis, however, the landscape of the city banks changed drastically as discussed in section 1.1 of this research.

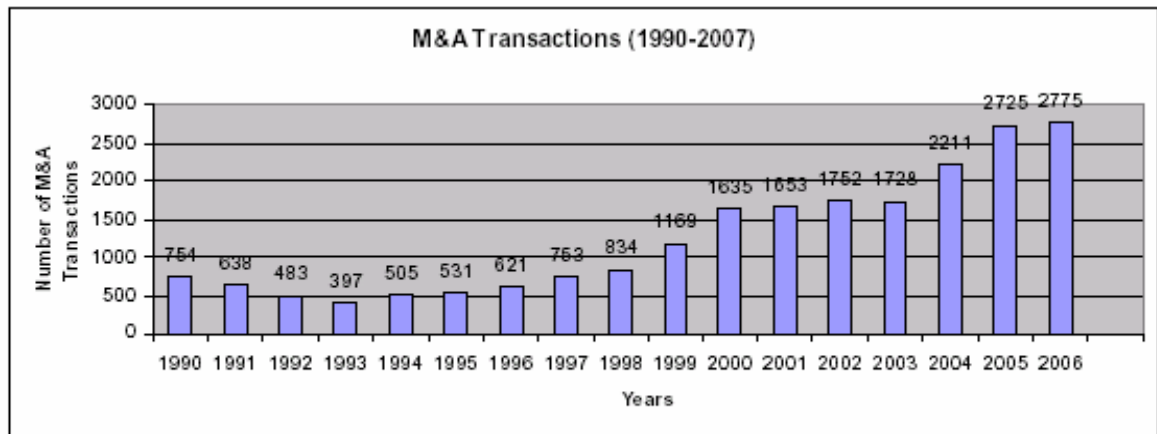
2.2 Status of M&As in Japan

This section discusses the i) current M&A wave in Japan (1990-2008); and ii) the consolidation of the Japanese Banking Sector (1990s to 2008).

2.2.1 Current: M&A Wave in Japan (1990-2008)

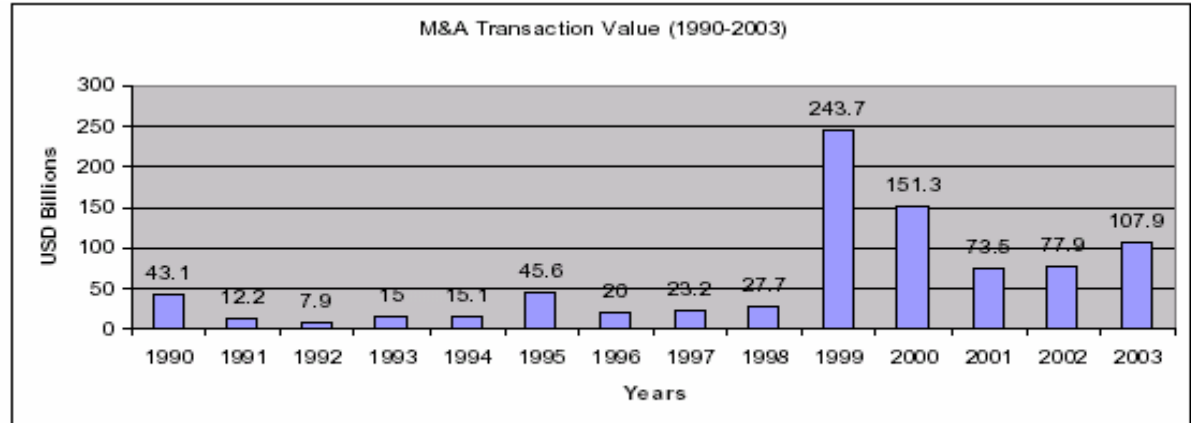
M&A transactions, during late 1990s, grew significantly in the Asian region touching a USD 224 billion level (The Nikkei Financial Daily; 2000). At the sametime, M&As in which both partners were Asian grew 240% to about USD 110 billion in terms of transaction value.

In Japan also during the late 1990s, M&As were seen at an unprecedented level. The M&A activity in Japan started to pick up pace in 1997 and 1998 where it had recorded approximately 200 and 280 M&A transactions respectively. In 1999, the M&A volume increased to 1169 (as is shown in figure 2.1). In 2004, more than 2000 deals were announced, which was considered as a breakthrough from the traditional Japanese business culture, as up until this time, the Japanese M&A market was not considered “mentally mature” to handle M&A transactions. As up until this time Japanese banks and corporates did not possess the mind-set and comfort level to adopt M&As as a diversification/restructuring tool nor were the M&A rules and regulations developed to level where institutions could engage in this activity. Moreover, with the Japanese banks being heavily regulated by MoF in Japan, banks were dependent on MoF whenever any kind of support was required. In 2005 the number reached 2,725 and in 2006 around 2775 M&A deals were announced.



Source: Shimotani (2007); MARR (Mergers & Acquisitions Report)
Figure 2.1

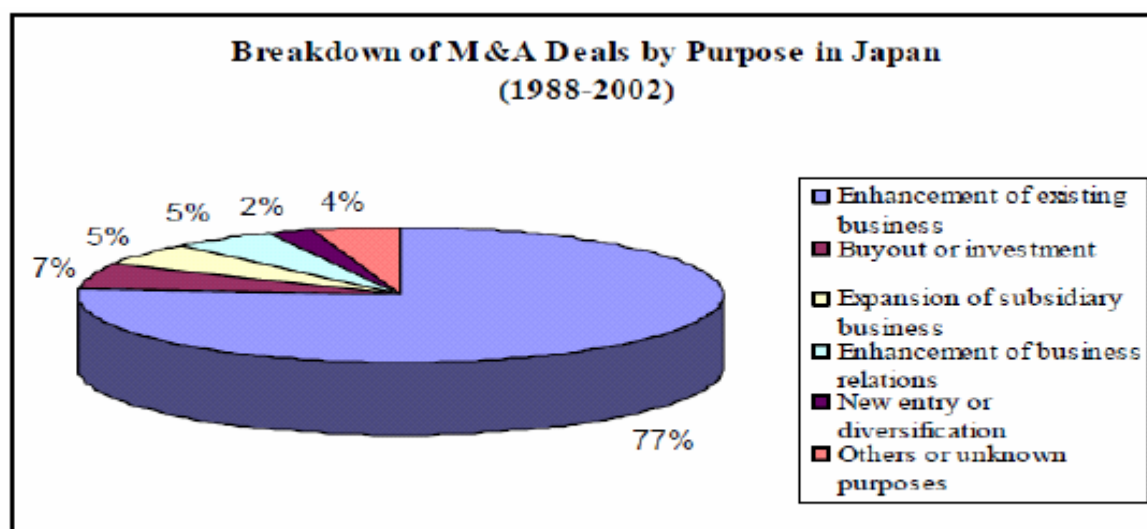
In terms of M&A value, the highest value was recorded in 1999, with M&A deals totalling about USD 243.7 billion. Please refer to figure 2.2 for a breakdown between 1990 and 2007.



Source: Shimotani (2007); MARR (Mergers & Acquisitions Report)
Figure 2.2

In terms of methods adopted by the companies, it is reported that about 35% of the transactions were carried out on the basis of asset acquisition, with an average value per deal of USD 86.3 million. Transaction value in terms of sectors can be split into three segments; financial (36 per cent); manufacturing (28 per cent) and services (26 percent). Moreover, figure 2.3 depicts the M&A deals in Japan by purpose from 1988 to 2002.

Conversely, acquirers from financial industries accounted for 45% of the transaction value and 22 % of the deals and acquirers from the manufacturing sector industries participated in 41% of the deals and 27% of the transaction value.



Source: Annual Report (2003; pp. 193); Japanese Firm's M&A Databook (1988-2002), Recof Corporation
Figure 2.3

Begg and Henning (2008) maintain that the recent M&A activity in Japan has been characterized by a decrease in speculative M&As due to the long lasting recession in Japan, and an increase in transactions related to corporate restructuring and insolvency procedures. In 2006 M&As shift from 'restructuring to troubled companies to strategic selection and concentration type of M&As.' This change reflects improving financial conditions of Japanese companies so that they can afford to allocate more resources to pursue strategic investments.

In Japan from 1990s onwards, with the gradual origination of the M&A wave and structures put in place by the relevant Japanese financial authorities to facilitate the said activity, M&A transactions by foreign country institutions also increased. US companies acquiring Japanese companies in Japan, stood at a value of USD 40 billion, after Japanese companies acquiring Japanese companies stood at a value of USD 742 billion; accounting for 93 per cent of the number of deals and 86 percent of the M&A transaction value during the said period. Consequently, M&A value in Japan, where the

target companies are US companies, stood at USD 62 billion coming in second after Japanese target companies M&As valued at USD 732 billion.

2.2.2 M&As in the Japanese Banking Sector (1990s to 2008)

In 1999, some 40 Japanese commercial banking M&A deals were announced. Ostrom (2000) discusses the city bank deals that started in April 1990, with the integration of Taiyo Kobe Bank Ltd. and Mitsui Bank Ltd. to form Sakura Bank Ltd. Later, in April 1991, Kyowa Bank Ltd. and Saitama Bank, Ltd. merged to form Asahi Bank. Following this activity in April 1996, Bank of Tokyo Ltd. and Mitsubishi Bank, Ltd. formed one of the largest banks, Bank of Tokyo-Mitsubishi.

In November 1997, another city bank Hokkaido Takushoku Bank Ltd., was declared bankrupt and it was absorbed by North Pacific Bank, a second-tier regional bank and Chuo Trust and Banking Co. Ltd.

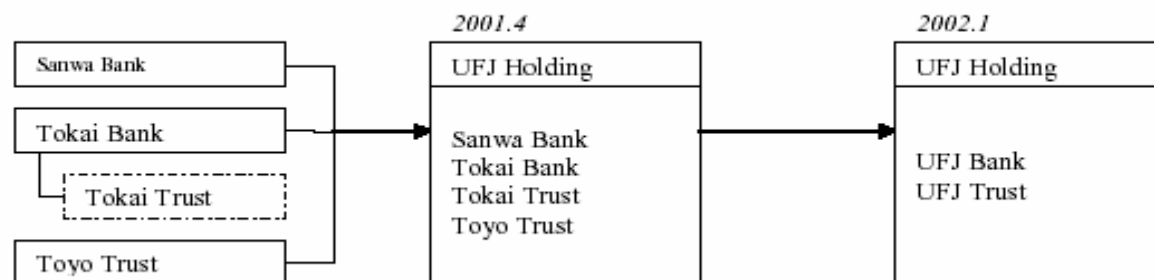
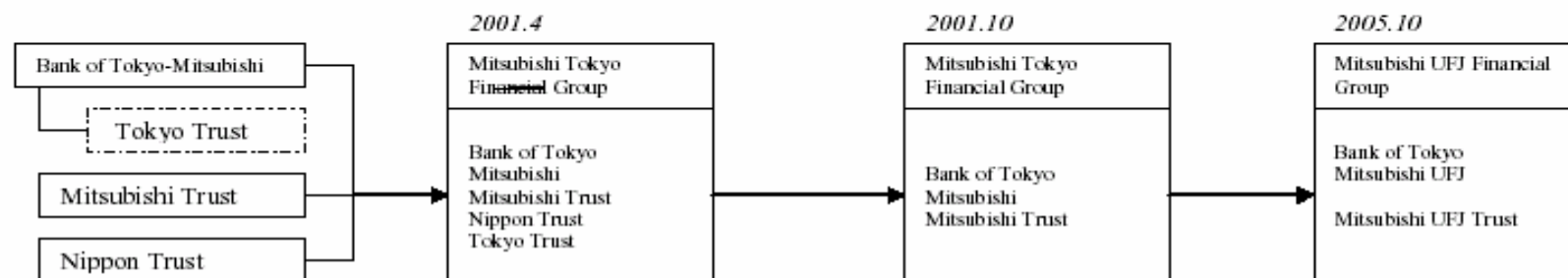
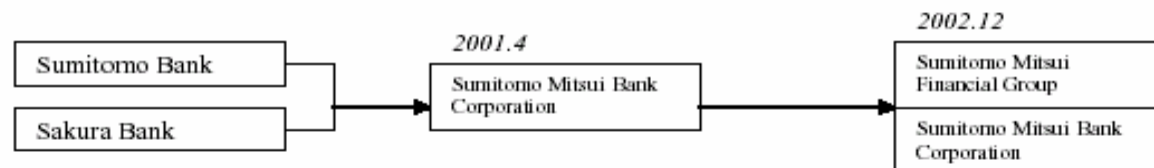
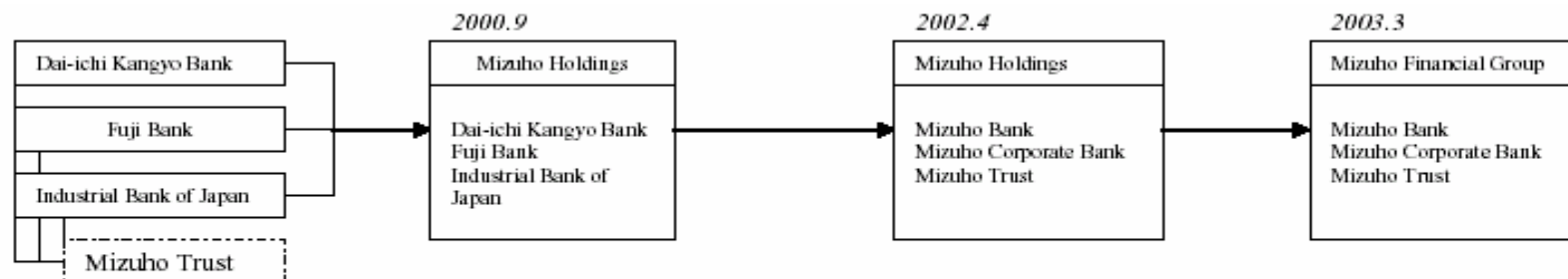
In August, 1999, Dai-Ichi Kangyo Bank, Fuji Bank and Industrial Bank of Japan announced a three-way-tie-up, forming a Mizuho Holding Company in September, 2000. In April, 2002 the three banks were combined to form Mizuho Bank, Mizuho Corporate Bank and Mizuho Trust under the Mizuho Holding Company and then this holding company was converted into the Mizuho Financial Group in March, 2003.

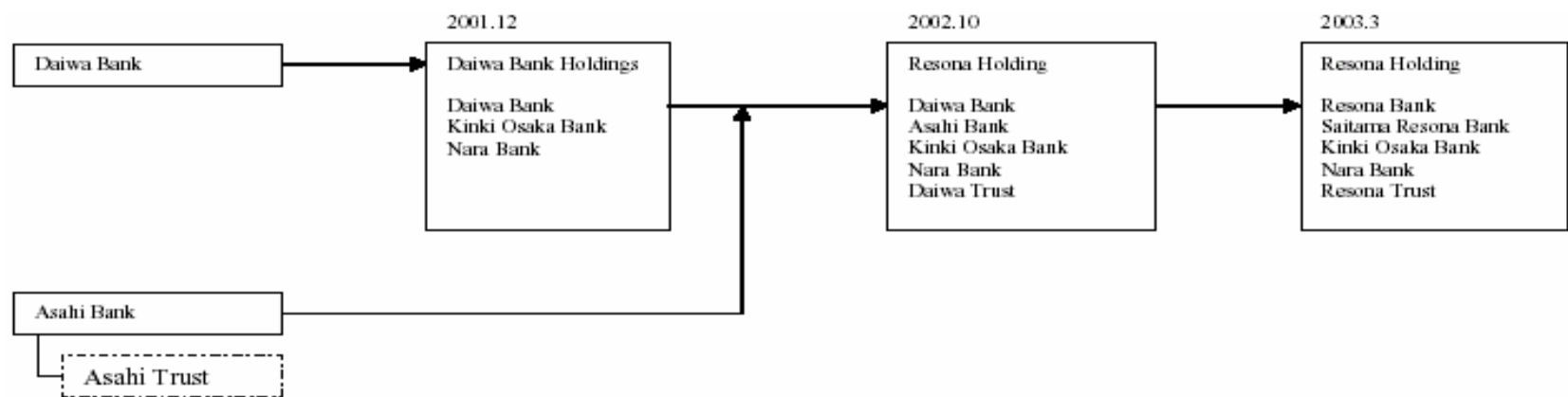
In October 1999, Sakura Bank and Sumitomo Bank decided to consolidate to form Sumitomo Mitsui Banking Corporation (SMBC) in March 2002. In 2003, SMBC was placed under the newly formed holding company, Sumitomo Mitsui Financial Group (SMFG).

In 2001, Sanwa Bank, Tokai Bank and Toyo Trust and Bank, integrated to form UFJ Bank in 2001 and UFJ Holding Company.

In 2002, Daiwa Bank and Asahi Bank combined to form Resona Bank. Asahi Bank had spun-off its Saitama Bank operations before it merged Daiwa Bank. The new bank, Resona Bank was placed under the Resona Group Holding Company. Prior to which Daiwa Bank, Kinki Osaka Bank and Nara Bank had made an alliance to form a holding company, under Daiwa Holding Group. Later Asahi Bank joined the Daiwa Holding Group. Daiwa Holding Group was restructured to form Resona Holding Company.

In 2004, the consolidation of BTM and UFJ Banks was announced for the launch of Bank of Tokyo Mitsubishi UFJ in 2006. The final systems integration for this bank will take place is due to take place in December, 2008. Simultaneously, both bank banks holdings companies, MTFG and UFJ Holding were also merged to form Bank of Tokyo Mitsubishi UFJ Financial Group. A history of the Japanese banks M&As and history of the M&A reforms is provided in appendix 2 and 3 respectively. The Japanese mega-banks M&A Tree is presented in figure 2.3.





Source: Zenginkyo (2006); appendix 4; pp. 17
 Figure 2.4: M&A Tree of Mega-banks in Japan

A summary of the largest deals in terms of value in Japan from 1990 to 2003 is presented in table 2.1. The top league is scored by Japanese banks namely; Sakura Bank and Sumitomo Bank in 1999 (USD 45 billion); Dai-ichi Kangyo, Fuji Bank and Industrial Bank of Japan in 1999 (USD 40 billion); Bank of Tokyo Mitsubishi and UFJ in 2005 (USD billion); Mitsui Bank and Taiyo Kobe Bank in 1990 (USD billion); Bank of Tokyo and Mitsubishi Bank in 1995 (USD 33 billion); Tokai Bank and Sanwa Bank in 2000 (USD 14 billion); Saitama Bank and Kyowa Bank in 1990 (USD 8 billion) and Asahi Bank and Daiwa Bank.

Year	Target & Nationality	Acquirer & Nationality	Amount USD (in Millions)
1999	Sakura Bank (Japan)	Sumitomo Bank Ltd. (Japan)	45,494
1999	Dai-ichi Kangyo Bank Ltd. (Japan)	Fuji Bank Ltd. (Japan)	40,097
1995	Bank of Tokyo Ltd. (Japan)	Mitsubishi Bank Ltd. (Japan)	33,789
1999	Industrial Bank of Japan (Japan)	Fuji Bank Ltd. (Japan)	30,760
2003	Resona Bank Ltd. (Japan)	Deposits Corporation of Japan	16,650
1999	KDD Corporation (Japan)	ODI Corporation (Japan)	15,822
1999	Nippon Telegraphic & Tele Corp (Japan)	Investors Group (Unknown)	15,080
2000	Tokai Bank Ltd. (Japan)	Sanwa Bank Ltd. (Japan)	14,984
1999	IDD Corporation (Japan)	ODI Corporation (Japan)	10,659
2000	Mitsubishi Trust & Banking (Japan)	Bank of Tokyo Mitsubishi (Japan)	10,373
2000	AT&T Wireless Group (U.S.)	NTT DoCoMo Inc. (Japan)	9,805
2000	Nippon Telegraphic & Tele Corp (Japan)	Investors Group (Unknown)	8,760
1999	Saitama Bank Ltd. (Asahi Bank – Japan)	Kyowa Bank Ltd. (Japan)	8,092
1999	RJ Reynolds International (Netherlands)	JT (Japan)	7,832
1999	MCA Inc. (U.S.)	Matsushita Electric Industrial (Japan)	7,406
2000	J-Phone Kansai, Tokai, Tokyo (Japan)	J-Phone Communications (Japan)	6,635
1999	Japan Leasing Corporation (Japan)	General Electric Capital Corp. (U.S.)	6,566
2000	Verlo Inc (U.S.)	NTT Communications Corporation (Japan)	5,694
2003	NTT DoCoMo Inc. (Japan)	NTT DoCoMo Inc. (Japan)	5,630
1999	East Japan Railway Co. (Japan)	Investors Group (Unknown)	5,594

Source: Baba and Hisada (2002)

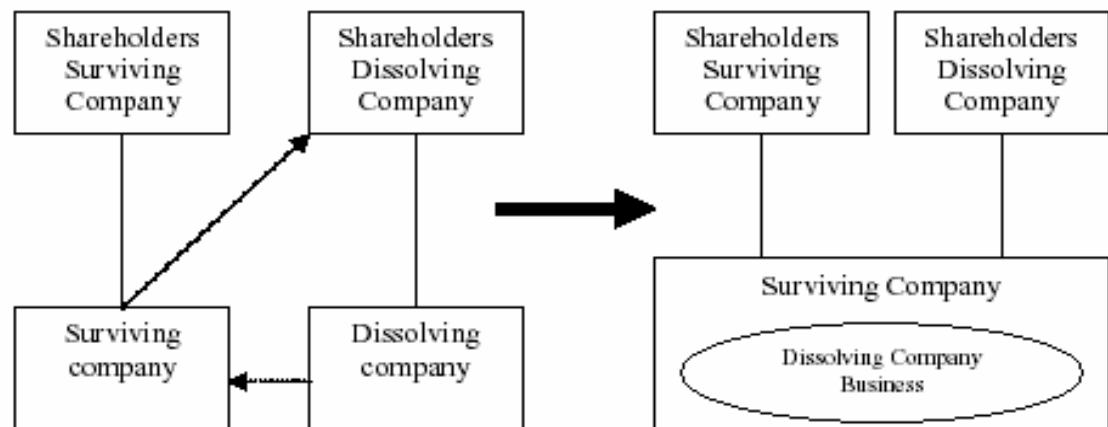
Table: 2.1

2.3 Structural Reforms in the M&A Framework in Japan

The following section discusses the i) structure of the M&A transactions; ii) mode of payment for the M&A structure; iii) benefits of the M&A reforms; and iv) the M&A process in Japan.

2.3.1 Structure of M&As Transactions

In Japan, M&As, are known as *gappei*, when a company dissolves, with its assets being rolled over into another company and its shareholders becoming shareholders in that company (Begg and Henning, 2008). The second company (into and by which the first company's obligations are subsumed and assumed) may be either an existing company or a newly established company. In the former case the consolidation is termed as an 'absorption merger', in Japanese known as *kyushu gappei* and the surviving company in Japanese is known as *sonzoku kaisha*. In the latter case, the activity is termed an 'establishment merger' known as *shinsetsu gappei* and the newly established corporate vehicle is known as *shinsetsu kaisha* (Begg and Henning, 2008, pp. 48).



Source: Begg (2008, pp. 48)
Figure 2.5 An Absorption M&A

2.3.2 Mode of Payment for M&A Transactions

In 1997, the Japanese corporate law rationalizing the M&A regulations was passed, and in 1999 and 2001 the stock swap system (transfer of shareholdings) was introduced to provide a systematic process for M&A activity in Japan. There are two common ways of payment for the M&A transactions, i) cash for stock transactions; and ii) share for share exchange.

- **Cash for Stock Transactions**

The role of the two parties is clear cut and the exchange of money for stock completes a simple transfer of ownership. This transaction is treated as a taxable sale of the shares of the target company. Shareholders of the acquired company take on the entire risk.

- **Share for Share Exchange Transaction**

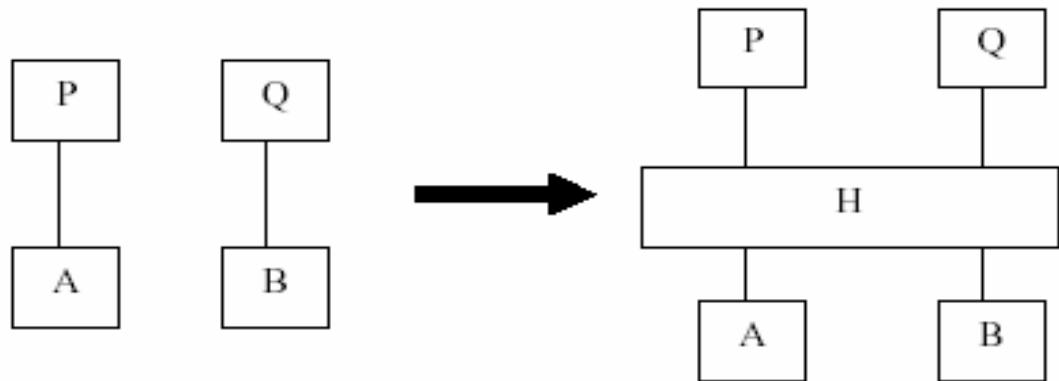
In the context of Japanese banking M&As share for share exchange is further divided into three categories; i) share for share exchange; ii) share switch; and iii) company split.

- **Share- for- Share Exchange - *kabushiki kokan***

Share-for-share exchange referred to as *kabushiki kokan*, as a means of consolidating ownership of an existing company through turning it into a wholly-owned (100%) subsidiary of another company.

- **Share- for- Share Exchange – *kabushiki iten***

Share switch known as *kabushiki iten* system, provide for the establishment of a new company as the 100 per cent of one or more existing companies thereby providing a means of creating a holding company.



Source; Begg and Henning (2008, pp. 54)
Figure 2.6: Share switch (*Kabushiki Iten*)

In a *kabushiki iten* company P has a subsidiary A and company Q has a subsidiary B. A new intermediary holding company below P and Q and above A and B, may be established as a new company H in order to achieve this: P and Q transfer their respective shareholdings in A and B to H, switching their holdings in A and B for new shares issued by H in consideration of the transfers.

➤ **Company Split - *kaisha bunkatsu***

Company split often called *kaisha bunkatsu* system, enables the ‘hiving-out’ of the whole or a part of the business of an existing company to another, which may be either existing or established for the purpose.

The other M&A structures available in Japan are: share acquisition, *kabushiki shutoku*, is considered to be the easiest way to obtain control over a company as it purchases all of its shares; and business transfer, concern the transfer of part or the whole of a company’s business also referred to as *eigyo joto*.

2.3.3 Benefits of M&A Reforms in Japan

The legal reforms discussed above, may yield some benefits, namely; i) the cessation of business or dissolution of some or all of the merging companies; ii) the allotment and issue of new shares to the shareholders of the dissolving company or companies; and iii) the succession by the surviving or newly established company to the assets, liabilities, rights and obligations of the dissolving company. Consequently, in April 2002, a consolidated tax system for corporate groups was put in place, which allows for a group tax relief, instead of subsidiaries being taxed on an independent basis therefore, favouring the holding company set-up. This gives precedence to related operations being brought together into a single division or company and then being spun-off (Begg and Henning (2008).

The M&A mode of payments provide the following benefits; i) no requirement to follow any procedures for transferring any assets as all the pre-merger assets, rights and obligations are acquired by the surviving company (unlike in the case of business transfers or other restructuring measures); ii) mergers can be implemented without arranging for funds as the business of the dissolving company can be transferred to and assumed by the surviving company in exchange for shares issued to the shareholders in the dissolving company. However, the M&A activity also limits the benefits as i) while all assets are transferred to the surviving company, all liabilities and other negative obligations are also transferred; ii) and mergers are only implemented among companies incorporated in Japan (not applicable under the absorption and or the establishment type).

2.3.4 M&A Process: Negotiation and Implementation in Japan

This section discusses the M&A planning process specific to Japanese banks (Begg and Henning, 2008; pp. 19-22).

- ***Nemawashi***

‘*Nemawashi* refers to the pruning and binding of a tree’s roots before it is moved, in order to make the move easier.’ Consultation takes place among the key-decision makers for the proposed M&A activity, and then seeking approval for the said initiative.

- ***Ringi***

This stage produces the document including the project details (*ringisho*) which are then circulated for management approval. If approved the *ringisho* is ‘chopped with the department heads seal’ and then the project can be implemented. Regular discussions take place in the form of *nemawashi* to further fine tune the activity.

- **Middle-up Management**

Japanese management style is more ascribed to middle-up as opposed to top-down. Through the processes of *nemawashi* and *ringi*, M&A activities receive support from both vertical commands from within the department and also horizontally from other departments, before the idea is proposed to the top management. This idea dwells on the ‘confucianism influence’ on Japan, whereby seniority and age are highly respected and go hand in hand. Consequently, Japanese companies promote the rotation of employees among various units allowing them to obtain diversified knowledge instead of being a specialist in a single area.

- **Negotiation**

Negotiations are conducted by a group of staff members and decisions are taken through subsequent meetings or intimated through letters. Once the final draft is negotiated, the *ringi* is then circulated among the relevant management for the approval.

- **Due Diligence**

Until recently, due diligence has been a foreign concept in Japan. Initially, it was used as a tool to determine the price, however, now its role has been diversified to detect problems in order to safe-guard the buyer and to assist the buyer in better understanding the acquired business.

- **Documentation**

Drawing up the contract and finalizing the deal is the final stage. The contracts are based on the Japanese rules and regulations and agreed upon by both parties before the deal is closed.

2.4 Structural Changes in the Japanese Economy

This section discusses the structural changes in the macro-economic policy since World War II and its significance to the Japanese economy.

The Japanese post-war economy is divided into three stages: the pre-1973 period of high growth (average real growth rates of GDP/capita of close to 10%), the period of 1973-1991 of moderate growth of about 4%, and the period 1991-present of low growth of about 1% (Fukao, 2003).

Japan has experienced six major booms in asset prices in the post-war period: Korean War boom, November 1951-January 1954, 27 months; *jimmu* boom, October 1954-June 1957, 33 months; *iwato* boom in the 1950s, July 1958- December 1961, 42 months, the boom of Prime Minister's Tanaka's 'remodelling the Japanese archipelago' project; Profitless prosperity, November 1962 – October 1964, 24 months; *izanagi* boom, November 1965-August 1970, 58 months; and the *heisei* boom in the late 1980s to early 1990. During the *heisei* boom, asset prices increased dramatically under long-lasting economic growth and stable inflation. One factor that misled Japanese Banks, during

the bubble period, into making speculative investments in real estate business to less reliable borrowers than the blue-chip industrial corporations they had served in the past.

World War II pushed the Japanese economy back to boom conditions, even though it lay devastated at the end of the war. Japan's postwar economy, was considered to be the age of technological progress coupled with the large share of human capital in primary industries. This was achieved by the accumulation of capital due to the high savings rate on one hand, and the investment in equipment and production facilities by the private sector.

Up until the 1980s, the Japanese economy grew at 3.8%, with low inflation of 2.5% for the CPI and 2.3% for the GDP deflator, but slipped into a long period of stagnation in the 1990s, which resulted in the *heisei* recession (Shiratsuka, 2003). With an appreciating yen exchange rate, the Bank of Japan had adopted a loose monetary policy until the spring of 1989, when it shifted to a tight monetary policy. Prior to this MoF emphasis was placed on stabilizing the appreciating yen rather than focusing on asset price stability and the overheating economy (Fukao, 2003). Due to the overheating of the economy and asset price inflation, the official discount rate was raised five times, going from 2.5% in 1987-1988 to 6% in 1991. This monetary tightening was deemed partly responsible for the collapse of the bubble in 1990-1991 (Kawai, 2003).

Fiscal policy has also been altered during the 1990s. This is due to the increase in fiscal spending that rose from 32% of GDP in 1991 to 39% in early 2000s. Meanwhile, fiscal revenues declined from 34% of GDP in 1991 to 31% of GDP in 2003 (Kashyap, 2002). Every year, supplementary budgets have been put in place to stimulate the economy, which has resulted in a budget deficit and, hence, government debt has risen sharply.

2.5 Japanese Financial Institutions

In this section the three Japanese financial institution categories of importance to this research are discussed, namely; i) FSA; ii) *Zenginkyo*; and iii) banking sector.

2.5.1 Financial Services Agency

Up until 1998, MoF was the responsible authority for bank supervision and inspection. In June 1998, reforms were designed to mimic the twin trends of liberalization and globalization, thereby, allowing for transparency in reflecting the true and fair value of the problems facing the Japanese financial institutions. It took a while before MoF realized it should not guarantee all banks against failure. Its supervisory capabilities have been weak; therefore, in June 1998 the government established FSA under the direct control of the Cabinet Secretariat (Patrick, 1998), and MoF and BoJ, had to relinquish their supervisory roles and opaque ties with the banks. FSA also has a separate Securities and Exchange Surveillance Commission (SESC), which supervises the market and inspects securities companies.

2.5.2 Federation of Bankers Association (*Zenginkyo*)

Zenginkyo is the principal banker's association in Japan, acting as an umbrella organization for 149 leading banks in Japan and 72 regional banking organizations. The Tokyo Bankers Association acts as secretariat for *Zenginkyo*. In addition, there is the regional banks association of Japan and several others associations. *Zenginkyo* conducts financial and economic research, and formulates industry perspectives for the banking and regulatory institutions. Regional bankers associations, on the other hand, perform specific tasks i.e. cheque and bills clearance on behalf of their members. Chairmanship of the *Zenginkyo* is assumed by the chairman of the Tokyo Bankers Association - a position which rotates annually among the presidents of five leading banks (Rowley, 1998).

2.5.3 Japanese Banking Structure

In Japan, the financial system is divided into three categories; a central bank; private banking institutions '*koko kinko*' set-up for special clientele; and the public financial institutions. The government financial institutions focus on financing in areas where the private sector banks are not allowed, i.e. providing loans for domestic and overseas development purposes. This category is composed of the Japan Post in order to promote small volume personal savings in Japan. The following section briefly discusses the role of BoJ, and some private banks that relate to the nature of this study.

- **Bank of Japan**

The Bank of Japan was established on October 10, 1882. It was originally licensed for a period of thirty years, and one-half of its capital was supplied by the government. The charter of the bank was extended for another thirty year term in February 1910, and February 1942, the present bank of Japan Law was enacted, which transformed the bank from a joint-stock company into a special cooperation.

In April 1998 a new law was passed to make the Bank of Japan a 'nucleus' of an integrated financial system and departure from the traditional role and structure where the MOF had regulated the system. The new Bank of Japan law includes three new features; i) ensures the independence of the Bank of Japan Law in deciding and carrying out monetary policy and acting as a central bank as Japan's sole issuing bank; ii) ensures the transparency of and accountability for monetary policy; and iii) reinforces the functions of the policy board. BoJ is not a supervisory body *per se* but it does conduct on-site examinations for bank branches that have current accounts with BoJ.

- **Private Sector Banks**

The Japanese private banks composes the second category of financial institutions in Japan; i) ordinary banks; ii) specialized financial institutions; iii) insurance companies; and iv) security companies and others. This research focuses only on the ordinary banks and the specialized banks as they pertain to this study.

- **Ordinary Banks**

There are three ordinary banks i.e. city banks, regional banks and regional banks II. Foreign banks and the growth of other financial institutions in Japan are also considered as ordinary banks. A brief description of each bank category is provided in the subsequent section.

- **City Banks (*Toshi Ginko*); Mega-Banks and Super-Regional Bank**

City banks are considered to be the largest and most influential group of banks in Japan. Their headquarters are mostly located in Tokyo and Osaka regions, with major banking presence in Tokyo, Osaka, Kobe, Kyoto, Nagoya, and Yokohama. Some city banks are also referred to as main banks that maintain shareholdings in the *keiretsu* and vice versa. City banks account for about 30% of deposits placed with private financial institutions and around a 27% share of the entire loan market by the end of 2005. City banks average about yen 37.1 trillion each in deposits (Zenginkyo, 2006). From 1999, most of the city banks merged to form the four mega-banks and one super-regional bank organized under the holding company structure (discussed in section 2.3.2).

In 1980s there were twenty city banks, reduced to thirteen by 1990s; Bank of Tokyo, Dai-ichi Kangyo Bank; Sumitomo Bank, Mitsubishi Bank, Fuji Bank, Sanwa Bank, Tokai Bank, Taiyo-Kobe Bank, Mitsui Bank, Kyowa Bank, Daiwa Bank, Saitama Bank and Hokkaido Takushoku Bank; following the merger of Mitsubishi Bank and Bank of Tokyo in April 1996 and failure of Hokkaido Takushoku Bank in November 1997, only 11 banks remained.

City and regional banks are distinguished on the basis of the head-office location and how they are positioned in terms of their banking portfolios.

➤ **Regional Banks (*Chiho Ginko*)**

Regional banks of which there are 64 are often concentrated in prefectures and tend to be smaller than city banks in terms of assets. Their clients are mostly small regional companies which have a capital base less than 10 million yen and local public utilities with almost half of their deposit balances represent individual deposits and almost three-fourths of them are time deposits. As of March 2005, a regional bank on average had about yen 2.9 trillion in deposits with 106 branches (Zenginkyo, 2006).

➤ **Regional Banks II (*Sogo Ginko*)**

These are regional banks, based on the former *mujin* banks (mutual banks), which had stricter limits on exposure to individual borrowers. There are 48 banks under this category serving smaller companies and individuals than regional banks. An average regional bank as of March 2005, composed of yen 1.1 trillion in deposits with 66 branches (Zenginkyo, 2006).

➤ **Foreign Banks**

As of December 2005, there were 69 banks, composing only about 3% gross assets and 1% loans with branches in Japan subject to a license available from the Prime Minister under the Banking Law.

➤ **New Banking Entries**

In late 1999, a number of companies stated venturing into banking business such as settlement banks and internet banks. The Japan Net Bank, in October 2000 started functioning as Japan's first internet bank, followed by IY Bank (corporate name was changed to Seven Bank in October 2005); Sony Bank and eBank Corporation. Other banking activity includes financing for small businesses i.e. Incubator Bank of Japan launched in April, 2004.

- ***Specialized Financial Institutions***

Banks under this category are classified as long term financing institutions, financing institutions for small businesses, agriculture, forestry and fishery.

- **Long Term Financial Institutions**

The long term credit banks and trust banks form the long term financial institutions category as discussed below.

- **Long Term Credit Banks (*Chogin*)**

LTCB was re-established in 1952, under the Shigeru Yoshida government, providing long-term working capital to corporates based on loans, guarantees, and by purchase of government bonds, and other securities. From 1950s to 1970s, LTCB was involved in shipbuilding and steel industry financing but as the manufacturing sector requirements decreased for external resources, the clientele for LTCBs shifted towards the oil, electric power, and non-bank and leasing companies (Rowley, 1998).

In 1998, both LTCB and Nippon credit bank were nationalized and re-organized to form Shinsei Bank and Azora Bank, respectively. In 2000, LTCB was sold to a US-based company, Ripplewood Holdings. Consequently, in 2000, Nippon Bank was also bought by a group of investors led by Softbank, Orix and Tokio Marine & Fire Insurance Co. In 1999, the Industrial Bank of Japan, merged with DKB and Fuji Bank to form Mizuho Financial Group. As of December, 2005, there is only one credit bank; Azora Bank but with a unique business model it seems that the LTCB system is in the midst of ending (Zenkinkyo, 2006).

- **Trust Banks (*Shintaku ginko*)**

As of December, 2005, there were only 24 trust banks, with a total of Yen 49 trillion in total funds with only 46 domestic branches on average per trust bank. Four of the trust banks were established prior to the 1960s; eight were established by foreign banks after 1985 and twelve new ones were established under the Financial System Reform Law of 1992. The traditional business was to supply funds to corporations and receive deposits from trusts; however, recently their business scope has shifted to asset management.

- **Small Business Finance Institutions**

This category of specialized banks is composed of six types of financial institutions providing financing to the small businesses in Japan, namely; *shinkin* banks; *shinkin* central bank; credit cooperatives; *shinkumi* federation bank; labour banks and *rokinren* bank. This section will only discuss *shinkin* banks as they relate to this study.

- **Shinkin Bank (*Shinyo kink*)**

As of March 2006, there were 292 *Shinkin* banks also known as credit cooperatives. On average a bank has Yen 360.5 billion in deposits and 26 branches. They derive a minimum of 80% of all deposits from owners and workers in smaller companies. Members take a stake in these companies and share in profits, to a limited extent with the owners (Zenginkyo, 2006).

Chapter 3

Literature Review

The review will present a platform for this study based on the literature and the gaps identified through it. This chapter is developed as follows; i) corporate strategy and M&A literature; ii) strategic relatedness; iii) resource based view; iv) Japanese business and banking literature; v) linkages; and vi) research questions.

3.1 Corporate Strategy: Concept and Theories of M&As

The following section discusses the i) concept of M&As; ii) M&A theories; iii) M&A strategies as a means of providing a competitive advantage and organizational recovery for Japanese banking sector.

3.1.1 Concept of M&As

The global economy has witnessed an unprecedented amount of M&As, often defined as ‘complex, diverse and multiple causation’ of an organizations business strategy, shaping market structure (Trautwein, 1990). Schular and Jackson (2001) define M&As as the end option in corporate restructuring after licensing, alliances and partnerships and joint ventures. Licensing, is characterized as the least complex mechanism of business operations whereas M&A are a combination of complex variables such as size of investment, control, integration requirements, pains of separation, and people management issues (Hit et. al., 1991). Andrade and Stafford (2002) suggest that M&As play both an ‘expansionary’ and ‘contractionary’ role in restructuring and are difficult to manage.

Epstein (2005, pp. 38) define ‘mergers of equal’ as ‘two entities of relatively comparable stature coming together and taking the best of each company to form a completely new organization.’ ‘In a merger, the parties negotiate how relative value will translate into the amount of ownership each party will have in the new company (Mastracchio and Zunitch, 2002; pp. 39).’

In an acquisition, one company buys the assets of another and administers it in accordance to the acquirer's needs (Schular and Jackson, 2001). Mastracchio and Zunitch (2002, pp. 39) explain that 'in an acquisition, the parties negotiate how the relative value contributed to the new enterprise will translate into the purchase price.' Therefore, in an acquisition, a company can buy another through cash, stock, or a combination of two, leaving the target with cash and possible debt, if the target owned debt before the acquisition.

In a nutshell, there is an unambiguous distinction between the two types of corporate combinations. Acquisitions are supposed to take place when size asymmetry exists, while mergers are referred to as equals. M&As can also be considered the different steps of the same process: the acquisition refers to the transfer of a controlling stake, while merger applies to the legal combination (pooling of assets and liabilities).

3.1.2 Theories on Mergers & Acquisitions

M&As being a complex phenomenon suggest that a single motive tends not to do justice in explaining why organizations are opting for such a corporate strategy (Trautwein, 1990).

Theoretical research on M&As tends to focus, both on macro-economic and micro-economic perspectives. Subsequently, the financial and economic domains suggest value addition for shareholder's based on empirical and event studies (Seth, 1990). The industrial organization perspective translates market conduct into performance and market power (Demsetz, 1973). The strategic management literature provides insights into why companies diversify and what synergistic benefits can be derived from M&As (Barney, 1991). Table 3.1 provides an in-depth analysis on the concept of M&As. The ones relevant to this research are diversification and synergy theories. To further complement this research theoretical models of M&As are presented in appendix 4.

Stream of Research	Theory	Claim (benefits /gaps)
Finance and Economics	Disturbance theory	M&As take place in the form of M&A waves due to economic disturbances that cause changes in individual's expectations and increase the level of uncertainty, thus generating discrepancies in asset valuation (Gort; 1969).
	Macro-economic change theory	Auster and Sirower (2002, pp.217) suggest that M&A waves occur due to macro-economic changes within the national context with M&As reported simultaneously in many industries where this activity intensifies at an increasing rate with sharp rise in transactions, both in frequency and monetary value and then declines rapidly.' Thus, an important implication of M&A wave is that the environment is packed with inexperience; either inexperience with any kind of deal or inexperience with the new pace and size of transactions.
	Financial Motivation	Use of tax shields, lowered expected bankruptcy costs may induce M&A (Linter, 1971; Lewellen, 1971; Brown, 2003).
	Information Hypothesis	Acquiring firm's views that the market valuation of the target firm does not reflect all relevant information (Brown, 2003).
	Inefficient Management	Merger tends to eliminate mismanagement of the target firm (Lu, 2005; Manne, 1965).
	Management Self-interest Hypothesis	Assumes positive correlation between firm size and management compensation and gratification from managing a larger firm (Lu, 2005; Brown, 2003).
	Hubris Hypothesis	Acquiring firm overpays for target resulting in transfer of wealth from acquirer's shareholders to target's shareholders (Brown, 2003).
	Empire Building Managerialism Theory (Seth et. al. (2000).	This approach takes its roots from Berle and Means (1933) study on the separation of ownership and control in the corporation. The theory explains that managers tend to seek higher growth in assets rather than in profits; create a diversified portfolio to maximize their own value instead of their shareholders' value) as manager compensations are based on the amount of assets they manage (Vennet, 1996; Mueller, 1969). With technological change, swiftness of product life cycles, increasing costs of new product development, and formidable

		barriers to entry, M&As maybe the key in acquiring the critical size, in order to compete in today's challenging environment.
	Raider	A person who causes wealth transfers from the stockholders of the companies they bid for. These wealth transfers include greenmail and or excessive compensation after a successful takeover (Trautwein, 1990).
	Valuation	Managers have access to information about the target firm and its value more than the stock market and therefore, want to acquire the company as they can attain a better bargain as financial market efficiency exists (Ravenscraft and Scherer, 1987). Henderson (1999) states this as the information hypothesis as the manager of the bidding company have unique information about possible advantages to be derived from the combining the target's business with their own.
	Winners curse	Overpaying for target company, as a result of bidding wars (Cantwell and Santangelo, 2002).
	Over-estimation	Over-estimation of the ability to manage large organizations, deal with unfamiliar markets and technology and integrate efficiently by exploiting synergies; and misjudging competition policy restrictions (Cantwell & Santangelo; 2002).
Industrial Organization	Monopoly Theory	Demsetz's [1973, as quoted by Brown, 2003] in 'The Market Concentration Doctrine' suggests that M&As are carried out to achieve market power, by strengthening their competitive position in their home markets. Trautwein (1990) suggests that products can be cross-subsidized as profits from one market can be used to grow and sustain market share in another market, thereby, imitating a new market strategy to re-price products. If competition decreases as a result of M&As, all competitors in that industry benefit as products and services can be re-priced.
Strategic Management	Synergy theory or efficiency theory	M&As provide growth and value addition (Trautwein, 1990). Synergies are created when the combined value of the two entities is greater than the sum of the individual entities (Bradley et. al., 1998). Consequently, synergy may arises when two entities combined together operate efficiently with lower costs and effectively

		utilize the scarce resources when combined together then apart, under a given environmental constraints (Lubaktin, 1983). Synergistic benefits may provide a drive for the organizations to incur the expenses for the consolidation process, as a result of which their competitive position is improved and earn a premium for the shares being purchased from the target company's shareholders (Haspeslagh and Jemison, 1991).
	Diversification theory (linked with transaction theory Williamson (1975) and Coase (1937))	Diversification acts as an internal market for capital, thus enhancing efficiency and providing financial benefits (Teece 1982). In the 1990s, this concept shifted from diversification to core competencies and capabilities (Teece et. al., 1997). Amit and Zarowin (1989) claim that diversification may be a desirable alternative to selling off access capacity when there is some failure in the market such as high transaction costs.

Table 3.1.M&A Theories

3.1.3 Type of M&As strategies

According to the Federal Trade Commission (FTC), as quoted in Seth (1990, pp. 434) the two main M&A strategies are defined as; i) related M&A i.e., non-conglomerate horizontal M&As, non-conglomerate vertical M&As and conglomerate: product extension and market extension acquisitions; and ii) unrelated M&A i.e., conglomerate M&As.

In banks, M&As occur through the inter-linkages created by the formation of correspondent networks, syndicates, shared-access networks, or alliances in which the production or distribution of services is collectively shared or parcelled out. Production of financial services may include underwriting of financial contracts, intermediation, risk management, payment processing, and other back office operations. On the other hand, distribution suggests direct contact with customers, including sales, marketing, provision of services and other front-office operations (Berger, 2000, pp. 3). Table 3.2 shows the main strategies prevalent in the banking M&As.

Type of Integration	Example
Scale Integration	M&As of similar organization, allows for the consolidation of production or distribution of financial services into fewer, larger organizations and often defined as a 'primary and natural goal of horizontal mergers.' Scale integration also suggests that economies of scale exist prior to the M&A activity, whereby the firms are not operating at their full potential.
Scope Integration (integration of multiple categories)	M&As among commercial banks, investment banks and insurers. Scope integration gives rise to the diversification of services produced or distributed by financial institutions to become a universal type institution i.e. investment banks, commercial banks, insurance and so on. This form takes place when institutions indulge in M&As and want to move from a single product category to a multiple product category in a single organization.
Geographical Integration	Cross-regional M&As take place when production or distribution of services occurs in an expanded set of locations or set-up of offices or subsidiaries.
National Integration	Consolidation of financial institutions of single product category within national boundaries. M&As maybe the means involving scale integration and sometimes scope and geographical integration.
International Integration	International integration of firms expanding across borders through M&As. It involves the institutions to adapt to different cultures, languages, currency, regulatory and supervisory structures, geographical distances and so on. It also involves for higher risks in terms of political, social and economic infrastructures of the new international location and foreign exchange risk.
Horizontal Integration of distribution systems	Offer 'one-stop shopping' for multiple services in a single location
Horizontal Integration of production systems	Share information in underwriting loans, securities and insurance
Vertical Integration of production and distribution systems	Underwriter shifts from independent agents to direct distribution of services

Conglomerate	Two organizations of completely different industries merge and therefore, are considered more risky in nature as their failure rate is significant
Concentric	Mergers between firms with interrelated, but not identical lines of business creating a 'common thread'

Table 3.2 Level of Integration (Berger, 2000)

In simple terms horizontal mergers occur when two competitors combine to engage in the same industry to increase its market share by achieving geographical diversification (Evans, 2000). Kitching's (1967) refers to horizontal mergers as 'tactical acquisition' with a motive to capitalize on economies of scale and existing marketing skills (Taqi, 1987). Porter (1985) maintains that most horizontal mergers are only successful if they capture an element of competitive advantage across strategic business units. Green and Berry (1991) maintain horizontal M&As can be a success if i) skills and competencies are applied to a partner's business; and ii) the ability to capture the horizontal or relatedness opportunities presented by the new asset of the acquired unit. Horizontal integration may also take place between institutions distributions systems offering a 'one-stop' platform for multiple services in a single location.

Vertical integration can be classified as market extension M&As; 'two companies selling the same products in different markets; or product-extension M&As; 'two companies that sell different products but related products in the same market (Seth, 1990).' Vertical mergers are usually characterized as 'complex' and 'expensive' and occur as a means of gaining 'competitive advantage' within a market.

Conglomerate mergers, also known as 'economic diversification' consists of all mergers which are neither horizontal nor vertical. Two organizations of completely different industries merge and therefore, are considered more risky in nature as their failure rate is significant (Kitching, 1967). As there are fewer synergies and economies of scale; thus there are fewer options to limit downward risk and provide more consistency in long-term growth. Mature organizations which show poor prospects for growth usually indulge in M&As to diversify their businesses as they are not blessed with growth

options within their existing fields. Epstein (2005, pp.38) suggests that large organizations are combined together without any clear attempt to ‘create synergies’ or ‘meld strategies, keeping them separate to provide the advantages of decentralization and autonomy’.

Concentric M&A is a combination between firms with interrelated, but not identical lines of business creating a ‘common thread’ in the relationship between firms, which in turn generates business synergy and reducing corporate risk (Lubatkin and Lane, 1996). Lubatkin (1987) maintains that concentric mergers can both be horizontal or vertical, and tends to reduce a company’s vulnerability when competition increases in a market and companies are becoming more susceptible to industry-specific shocks. Kitching (1967) introduced two kinds of concentric mergers, namely; concentric marketing merger and concentric technology merger. According to (Pandugtin 2003; pp.28) concentric marketing mergers are mergers that ‘have the same customer, but different technology.’ In a similar vain, concentric technology mergers are mergers where ‘both partners have the same technology, but different customer groups.’

3.1.4 Conclusion

This section provides a critical evaluation on the concept of M&As and how the different theories on M&As have evolved over time. In banking and finance M&As hold a very responsible position as a number of banks internationally have adopted M&As as a means of diversification and restructuring. The theories highlighted here are discussed in the context of Japanese mega-banks and how relevant this activity has been during the restructuring of the Japanese financial system in providing a competitive advantage and organizational recovery to the mega-banks in Japan.

3.2 Strategic Relatedness of Mergers and Acquisitions

Strategic management literature dwells on the combination potential among combining banks based on the concept of relatedness. This chapter is split as follows; i) planning stage; ii) concept of relatedness; iii) importance of relatedness; and iv) empirical studies in deriving a competitive advantage.

3.2.1 Planning Stage

M&As suggest that acquiring is a balancing act between exploiting existing opportunities and exploiting for new ones (Hayward, 2002). While firms are combining, some fundamental changes may take place in terms of how they utilize their resources and capabilities yielding different benefits for the resulting entities. Schmidt (2000) suggested that during the pre-deal the challenge is to find a partner with a good strategic fit. Nahanvandi and Malekzadeh (1988) suggest that M&A strategy and motives are discussed during the planning stage. In turn the implementation strategy determines to what extent the firm's activities will be combined.

In the pre-acquisition stage, potential partners begin to assess the business nature through the due diligence. 'Activities occurring at the initial planning phase include identifying business strategy, defining acquisition criteria, identifying target markets and companies, selecting target, issuing letter of intent and developing an M&A plan' (Waght, 2004; pp. 158). The due-diligence includes finance, people, cultural, legal, environment and operations during the initial M&A stage. Wright et. al. (1999) define due diligence as a fundamental responsibility of the organization on behalf of its investors to investigate the target companies general management team, resources, and trading performance. Following the first two stages, rapid integration process begins. The integration plans are used as process maps to accelerate the integration process. It can include finalising and executing integration plans on organisations, people, process and systems (Waght, 2004). An audit team, that provides continuous monitoring and evaluation, and adaptation of the integration process, monitors the evaluation of the process.

Ashkenas et. al. (2001) suggests the assimilation stage includes evaluation and adjustment of long-term plans; development of common tools; processes, and languages; and utilization of a corporate education centre.

3.2.2 Concept of Relatedness

So what is the concept of Relatedness? Rumelt (1986, pp.11) defines relatedness as common skills and resources, market production technologies, distributions systems, and purposes between combined firms. According to Singh and Montgomery (1987, pp. 377) relatedness is associated with the transfer of ‘functional skills between businesses.’

Relatedness can be reflected through strategic fit or complementary and organizational fit or compatibility of the firms and their various divisions and provides insights to understand synergy realization. Organizational fit or compatibility concepts reflect on similarity of organizational cultures and management practices (Shelton, 1988).

Strategic fit or complementarity define ‘the proper fit among the firm’s strategic factors: leadership, style, climate, size, environment, technology, strategy and the firm’s structure (Burton and Obel, 2004). Consequently, Lee and Pennings (1996, pp.2) maintain strategic fit is for a firm to have ‘balanced bundles of resources across resource dimensions that will perform better since they maynot have underutilized resources (Black and Boal, 1994).

3.2.3. Importance of Relatedness

Why, is the concept of relatedness considered critical in defining the M&A strategy? Relatedness between acquiring and target firms has been widely recognized as a critical strategic means for M&As because it provides important source for cost savings from economies of scale, scope or revenue stemming from resource reconfiguration between two firms (Seth, 1990). Following this line of argument Barney (1988) maintains that’s relatedness does not contribute to abnormal returns for bidding firms but does generate

synergistic cash flows and thus positive returns for shareholders. Combination potential or success of integration in M&As is usually conceptual in terms of degree of relatedness (Kusewitt 1985). Shelton (1988) maintains that synergies are achieved through economies of sameness (similar operations) and economies of fitness (combining different but complementary operations). Markides and Williamson (1994) maintain that related businesses provide stronger prospects of growing business and achieving economies of scale and scope, than unrelated businesses.

Jemison and Sitkins (1986) explain that although strategic fit is an important element that aids towards the M&A performance, it not the only condition. If strategic relatedness exists between the firms involved in the M&A activity, synergistic benefits may only exist if the post-merger integration is conducted effectively. Finkelstein and Halebian (2002; pp. 38) maintain that ‘during the post-acquisition integration, the process shifts to organizational fit – the extent to which acquiring and target firms have compatible organizational systems.’ Furthermore, Buono and Bowditch (1989) add that ‘the more compatible these systems are the higher the probability of successful M&A integration.’ Hitt et. al. (2001) maintains that M&A relatedness provides opportunities for complementary managerial and knowledge assets.

3.2.4 Competitive Advantage Created through M&A Strategies

This section discusses the research in terms of i) industry relatedness; and ii) multiple M&A activity relatedness that may be considered imperative in reaping a competitive advantage for diversifying firms.

- **Industry Relatedness**

Salter and Weinhold (1979) draw the linkages between the acquisition of key skills, products and or market positions aiding towards value creation. They suggest that the more the products, markets and technologies of the combining organizations overlap, the greater the expectation of synergistic returns, but the greater the potential of

acculturative conflict, because synergies generally require a high level of integration of human resources. Furthermore, Salter and Weinhold (1979) maintain that diversification in unrelated M&As may result in positive gains if the ability to analyze and manage strategies of widely different businesses are available. The study classifies purely related-complimentary fit as vertical integration while a pure related-supplementary fit as horizontal fit. They maintain that the two concepts of related supplementary; to get more of those resources that a firm already possesses and related complementary, get resources which combine effectively with those you already have will provide value addition.

Shelton (1988) based on Salter and Weinhold's (1979) related-complementary and related-supplementary concepts, suggests that strategic fit is based on the relatedness of firms' products and markets, whereby, each asset class shows a mix of different levels of value creation. The study further maintains that 'diversification into related industries is best when a company has the ability to export or import skills or resources useful in its competitive environment (pp.87). The study also concludes that related acquisitions are more successful than unrelated M&As and there is a positive relationship with the size of the acquired firm.

Lubatkin (1983) conducted research based on two questions; do mergers provide real benefits to acquiring firms and if mergers do not provide real benefits, then why do firms continue to merge? The research maintains that i) M&As do not provide any real benefits as managements may either make the mistake of mis-evaluating their candidates for acquisition or seek to maximize their wealth at the expense of the shareholders of their firms. Secondly, M&As may provide real benefits, but the presence of certain conditions have prevented researchers from detecting such benefits. The study cites differences in managerial styles, threats of layoffs, initial inequities in compensation, authority superimposed on an acquired company, and increase in size of an acquiring company as administrative factors that may negate the potential benefits of the merger.

Lubatkin and Lane (1996; pp. 31) discuss relatedness of two partners with combination potential in physical commonalities such as markets, products and channels. The research suggests that in related M&As the closer the products, markets and technologies of the two businesses overlap, the greater the potential for conflict. This is because synergies usually mean the closing down of some facilities, uprooting people, and breaking apart work groups. Synergies also mean that the people from the two organizations are forced to come in close and frequent contact with each other, and close contact can heighten sensitivities to and intolerance for differences.

Palich et. al. (2000) suggest that moderate levels of diversification produce higher levels of performance than limited or extensive diversification, thus creating a curvilinear relationship between relatedness and performance. The research maintains that related diversification may yield higher returns than unrelated M&As as there are more contacts and overlaps between firms' value chain, resulting in higher potential for operational synergies (Palich et. al. 2000). They suggest three different models; linear (market power and internal market efficiencies); curvilinear, inverted U model (single and multiple business lines); and intermediate model (related versus unrelated business lines). The research supports the curvilinear model that is performance increases as the firm shifts from single business strategy to related diversification. What makes this research unique is the fact that while discussing diversification and performance linkages the authors split the results according to accounting based measures, market based measures and performance based measure.

Lubatkin and Chatterjee (1994) suggest that relatedness allows firms to push some of the burden of dynamic market uncertainties onto their less related rivals. Their findings maintain that the relationship between corporate diversification and both forms of stock return risk generates a U-shaped graph. This suggests that corporations may minimize risk by diversifying into similar businesses rather than identical or distinct business domains. This, according to Wyatt and Kieso (1969) suggest that horizontal and vertical M&As have a high expansion risk since they are directed into markets characterized by the same cyclical volatility and the same stage of development that faced the company prior to the combination.

Seth (1990) posits that value is created either by the realignment of operations and strategic changes during the planning stage or simply because a combination has taken place. The study maintains when two firms are competing in the same market, they possess a high potential for market-power related gains than two firms completing in dissimilar product-markets. Value addition is provided through a change in operating decisions, as the underlying economic motivation for change can be derived through economies of scope, economies of scale or market power in input or output markets. Financial synergy in related M&As results from achieving a lower cost of capital due to an increase in size or risk diversification.

Kusewitt (1985) maintains that six M&A variables, determine the success of M&A strategy; relative size, acquisition rate, industry commonality, timing, type of consideration, acquire profitability and price paid. The performance of the M&A is affected by all the measures discussed above except for price paid. Industry commonality and acquirer profitability positively affect performance whereas, strategy, size, rate, timing and type of consideration negatively impact performance. These variables can be used as a means of improving the effectiveness of the M&A program.

- **Multiple M&A Activity Relatedness**

Research since 1980s has proven that multiple M&A experience and performance are related. Organizations can learn from their previous M&A experience which tends to provide useful insights as to how and when firms should integrate and therefore, possess a higher level of internal variation (Lee and Penning 1994). They may face a number of problems while integrating since staff members from different organizations have their own values and business philosophies. Without proper integration of these contradicting cultures and routines, it is hard for the firms involved in the M&As to be integrated competitively. Firms that overcome there integration problems are more likely to achieve a higher growth momentum.

Finkelstein and Haleblan (2002) conduct a study based on transfer theory at an organizational level of analysis and define both positive and negative transfer effects in combining organizations. Consequently, based on negative theory of past acquisition knowledge, second M&A tends to under-perform first M&A particularly, when first and second targets are from different industry. This study also postulates that acquirer-to-target similarity increases the likelihood of positive transfer. Moreover, routines and practices established in prior M&As transferred to new M&As depends on the similarity of the industry.

Haleblan and Finkelstein (1999) offer insights that a failed M&A activity may create valuable insights in order to enhance the overall performance of combining firms through improved M&A capabilities. Therefore, in subsequent M&As they tend to avoid negative situations from arising based on their past integration experiences. The tendency to make correct inferences improves therefore, the performance level also increases during the time of the M&A activity.

Hayward (2002) maintains that the companies engaging in the M&A process may sometimes have the opportunity to learn from previous experience, but often do not realize it. The study highlights organizational learning as an iterative, dynamic process in which firms i) engage in experiences; ii) draw inferences from them; and iii) store the inferred material for future experience (pp. 22). One explanation maybe that learning relates to quality rather than the quantity of a firm's experience. Acquiring a series of highly similar businesses promotes specialized learning about those businesses, but prevents learning about that business. Conversely, entering into dissimilar business streams may help firms to discover new knowledge and expertise, however prevent specialized learning about any one business (Hayward, 2002; pp. 24). Sometimes firms may lack the skills to effectively select and implement M&As that exploit an existing market position or other capabilities. Therefore, both type of M&A experiences maybe considered detrimental to selecting a focal M&A partner irrespective of the nature of that M&A.

Schipper and Thompson's (1983; pp. 85) study is based on a set of conglomerate acquirers evaluating the impact of acquisition activity on firm value by segregating various merger events and programs of acquisition activity. The research highlights that significantly positive performance is associated with the announcement of acquisition programs and alternatively, significant negative performance is associated with some institutional changes of 1967-1970 relating to acquisition activity (the Williams Amendments, the 1969 Tax Reform Act, and APB Opinions 16 and 17). The results suggest that acquisition activity had a favorable ex ante impact on the value of firms announcing an intention to engage in acquisitions, and that some of the institutional changes reduced the expected profitability of future acquisitions activity.

Amburgey and Miner (1992) conclude that i) the occurrence of M&As tend to increase the rate of mergers of the same type (repetitive momentum); and ii) organizational decentralization increases the rate of diversifying M&As (contextual momentum). The decentralized firms use their ability to aggressively displace incumbent management teams in the market for corporate control and thus perform a 'capital market policing function.' Product market diversification was found to increase the probability of product extension mergers but not conglomerate mergers, only partly confirming positional momentum. They also maintain that M&As arising from risk reduction or imitation would produce a negative relationship between current level of diversification and diversifying M&As.

Laamanen and Keil (2008) test whether the frequency pattern affect acquirer performance and whether firm level influences moderate the relationship between the acquisition frequency pattern and acquirer performance. The study concludes that a high rate of acquisition and a high variability in the rate are negatively linked with performance suggesting the more M&A activities one goes through negative impact can be alleviated. They further maintain that negative performance effects are alleviated by an acquirer's acquisition experience, size and the scope of its acquisition program. Moreover, the study suggests that 'increase in efficiency' and reduced mental load maybe important determinants of performance when a firm carries out multiple M&As in a short period of time (pp. 665).

Haunschild et. al. (1994) suggests that firms maybe unable to generate meaningful inferences from very recent M&As. M&As that take place swiftly one after the other does not all managers to have enough time to carefully evaluate the first M&A activity nor have they had enough time to learn from the first M&A activity in order for them to implement best practices for the subsequent M&A activity. Preoccupied to engage in another deal these managers forego the experience learnt or to be learnt from the prior M&As and therefore, these inferences raise doubts about the merits of the focal M&A.

Homberg and Bucerius (2006) conduct a study by suggesting that during the integration process speed can be considered both as being beneficial and or detrimental, depending upon the magnitude of internal and external relatedness between the combining organizations. They conclude that speed is beneficial when external relatedness is low because it minimizes the amount of uncertainty among members of the combining firms. However, they also conclude that speed is detrimental in case of low internal and high external relatedness. Therefore, they suggest that there is no simple means of defining a quick or a slow integration process during the M&A activity. This study yet again, provides a different perspective into accessing the competitive advantage derived during an M&A activity based on the speed and timing variables.

Olie (1994) suggests that a slow integration process can be appropriate as it can reduce the amount of conflict and tension between the merging partners. In a similar vein, Ranft and Lord (2002) conclude that a slow integration can enhance trust building between the merging organizations employees. These investigations are purely qualitative in nature and do not offer any statistical insights between the relationship of speed of integration and success.

3.2.5 Conclusion

This section provides a reflection on the strategic management literature in the context of how the various aspects of M&As in terms of relatedness tend to provide a

competitive advantage for the combining Japanese banks. It opens doors for the types of research gaps present in extant literature and what is appropriate to study in the context of Japanese mega-banks during their M&A combination stage. To consolidate the large domain of literature on strategic management not only the concepts of relatedness and their importance is discussed but also the empirical and conceptual research is analyzed and presented in a succinct manner.

3.3 Resource Based View Concept

What are resources and why are they important in deriving a benefit for firms seeking to diversify? This is a concept which dates back to the seminal work conducted by Edith Penrose in 1959. Penrose (1959) maintains that a benefit maybe derived during the M&A process when resources are utilized competitively. Wernerfelt (1984, pp. 172) maintains that a resource can be characterized ‘as anything which can be thought of as a strength or weakness of a given firm.’

Barney (1991, pp.101) suggests that firm resources include ‘all assets, capabilities, organizational processes, firm attributes, information, knowledge etc. that enables the firm to conceive of and implement strategies. They maybe physical capital resources; technological resources used in a firm, a firms plant and equipment, its geographical location and its access to raw materials; human capital resources, training, experience, judgement, intelligence, relationships, and insights of individual managers and workers in a firm; and organizational capital resources, a firm’s formal reporting structure, its formal and informal planning, controlling and coordinating systems as well as intra and inter informal relations among groups and those surrounding it.

Chatterjee and Wernerfelt (1991) identify three types of resources, namely; physical resources (plant and equipment), intangible assets (brand names or innovative capability), and financial resources (used to buy other productive resources). Hall (1992) defines resources into tangible and intellectual property kinds, which are allocated by the firms on a semi-permanent basis (Caves 1981). Examples of such resources are; brand names, in-house knowledge of technology, employment of skilled

personnel, trade contacts, machinery, efficient procedures and capital. It is hard to imitate these resources especially, in a short span of time. Amit and Schoemaker (1993) split resources as follows; i) R&D resources such as technological capacity, R&D capacity, and product development speed; ii) manufacturing resources, such as product cost structures; and marketing resources; brand management, distribution channels, buyer-seller relationship, user base, customer services, and business reputation. Carow et. al. (2004) explain that ‘M&As provide firms with an expedient tool to close their resource gaps, allowing for a much faster reconfiguration of the products yielding higher profits as compared to internal development’.

3.3.1 Resource Based View

Resource Based View (RBV) can be a significant driver of strategic competitive advantage (Barney, 1991). Moreover, Eisenhardt and Martin (2000) define RBV as bundles of resources that are heterogeneously distributed across firms and that resource configuration differences persist over time (Amit and Schoemaker, 1993). Bowen and Wiersema (1999) maintain that the RBV provides a firm to perform better based on its ability to possess a distinct and sustainable advantage which is derived from the utilization of unique, non-imitable, non-transferable firm specific resources. Moreover these resources and their relatedness may provide some form of competitive advantage. Barney (1986) define resources as VRIN resources and posit that for resources to create and sustain a competitive advantage they must be i) valuable; ii) rare and causal; iii) imperfectly imitable; and iv) have no equivalent substitutes. Resources can be characterized in terms of ‘distance between resources’ which suggests the difference in resources due to the distinct nature of their development path (Teece 1986). Moreover, ‘environmental uncertainty’ due to markets and technological uncertainty, if unresolved puts the value of the specific resources and capabilities into question.

RBV often provides some key insights into the firms that are diversifying, such as; i) which of the firm’s current resources should be used for diversification?; ii) which resources should be developed through diversification?; iii) in what sequence and into what markets should diversification take place?; and iv) what types of resources will it

be desirable for this particular firm to acquire (Wernerfelt, 1984, pp. 172)? Teece et. al. (1997) explain that dynamic capabilities approach to the RBV focuses on how firms acquire, adapt and integrate internal and external resources, skills and functional competencies to capitalize on a changing environment.

The resource portfolio is also defined based on ‘exploit and develop’ and resources used as ‘stepping stones.’ Resource diversification can be evaluated in terms of their short-term and long-term balance effects functioning as stepping stones for further expansion. This strategy is often used to describe the Japanese business as their indigenous strategy. Table 3.6 provides a glimpse of some of the strategic assets as defined by Connor (2007).

Strategic Assets – Characteristics	
Tangible Assets	More Easily Competed Away
Intangible Assets	Less Easily Competed Away
Features	Inimitable Non-tradable Tacit Durable Competence Capability Institutional Complementarity Metaphysical insights Competitiveness an internal paradigm

Table 3.6 The Principal features of strategic assets
Source: (Connor, 2007)

3.3.2 Competitive Advantage Created through Resources

Penrose (1959) maintains that larger size means more resources can be invested in managing more pre and post M&A activities. Large firms also possess highly sophisticated managerial and financial resources that allow them to engage in more complex M&A strategies versus their smaller counterparts. Larger firms tend to develop specialized personal processes and establish dedicated teams to manage M&A processes and hire a pool of M&A specialist. Smaller firms, constrained due to number of personnel therefore, have to choose either between managing their day to day business operations or being involved in the M&A process.

Barney (1988) maintains that acquirers create a valuable and non-imitable combination of their assets with those of the acquired firm to earn positive abnormal returns on their investments. Although relatedness is an important element in synergy creation it is not the only condition, as performance is also dependent on how the M&A activity is planned and carried out.

Singh & Montgomery (1987) maintain that value is created through the 'reinforcement of skills or positions critical to the success of related M&As.' The study maintains that an acquirer has to create a uniquely valuable and inimitable combination of its assets with those of the acquired firm to earn positive abnormal returns on its investment. Although many acquirers may possess resources related to those of the target, the unique condition provides a much more stringent criterion for value creation. Furthermore, while controlling the type and degree of strategic relatedness between bidding and target firms, M&As tend not to generate abnormal returns for stakeholders of bidding firms.

Harrison et. al. (1991) extends the traditional product based concept of relatedness; thereby, posit that synergistic gains are envisaged in terms of operations, finance and R&D. They also maintain that dissimilarities between target and bidders on various resources allocation variables aid towards positive gains in post-merger performance than do similar resource allocation. Finally, their results maintain that acquiring firms may have the opportunity to satisfy unmet needs in their existing business portfolios through acquisitions.

Wernerfelt (1984, pp. 171) explains that 'resources and products are two sides of a coin. Most products require the services of several resources and most resources can be used in several products. By specifying the size of the firm's activity in different product markets, it is possible to infer the minimum necessary resource commitment. Conversely, by defining a resource profile for a firm, it is possible to find the optimal product-market activities'.

Black and Boal (1994) maintain that the relationship between bundles of assets produce a sustainable competitive advantage as compared to possessing a large number of intangible assets. The combination or 'factor networks with specific inter-resource relationship confer an edge over the competition.'

Lubatkin et. al. (2001), suggest that horizontal M&As depend on four competitive factors; i) the characteristics of the product-market in which the firm competes; ii) the influence of firm, industry and population vary over time; iii) firms are not equally capable of benefiting from horizontal mergers; and iv) both relative market share and relatedness among the merged products influence success. Furthermore, resources for various products differ in terms of competitive constraints.

Larsson and Finkelstein (1999) argue that the traditional concept of relatedness does not take into account complementary resources of synergy such as matching products and services, market access or know-how. The empirical tests reveal that there are several critical factors that affect M&A performance; i) the presence of complementary operations increase the probability of synergy realisation; ii) organizational integration is the single most important factor in explaining synergy realization; iii) M&As that depend on gains from combining similar products and market operations tend to face more resistance from employees than M&As focused on realizing complementary benefits.

Data et. al. (1992), recommended that resources model strategic factors to gain a better understanding of why some M&As perform better than others. The research maintains that target firm's shareholders gain value while bidder firm's do not. Furthermore, the use of stock in terms of financing the M&As provides significant impact on both the acquirer and targets shareholder values. Other variables such as multiple bidders and the type of acquisition influence the bidder's return, while regulatory changes and tender offer influence targets returns.

Chatterjee and Wernerfelt (1991) maintain that 'firms can gain competitive advantage if they have skills or resources that they can transfer into the new market (pp.384).' The

research maintains that excess physical resources, most knowledge-based resources, and external financial resources are associated with related diversification and internal resources are associated with unrelated diversification. They also define resources as flexible resources, whereby most resources can be utilized in more than one end-product; and inflexible resources which are considered to be firms own resources that are end-product specific. They also maintain that in a related market the flexibility of physical resources is considered low, whereas the highest flexibility for related markets is in financial resources such as equity capital and junk bonds and unrelated market resources include financial resources such as internal funds and low risk debts.

Chatterjee (1986) concludes that firms attain market power by increasing size. In this research three broad classes of resources are examined, namely; i) cost of capital (financial synergy); ii) cost of production (operational synergy); and iii) price related (collusive synergy). The resources stemming from financial synergy tend to create more value as compared to the ones originating from operational synergy. Complementarity can exist in horizontal M&As because firms within an industry vary in their capabilities across diverse resource dimensions e.g. strong in technology and market distribution. However, due to the limited nature of sample size employed, further research needs to be conducted to validate the present findings.

Taqi (1987) maintains that differences between business practises usually deteriorate performance. The differences maybe based on; i) accounting principles and practises; ii) salary and benefit differentials; iii) resistance to reporting relationships; iv) values and psychologies (big spenders vs. nitpickers; egalitarians vs. elitists; censuses seekers vs. individualists; customer-orientated philosophies vs. production-orientated ones; and v) understanding business practises when cross-border M&As take place.

Capasso and Meglio (2001) maintain that M&A's are an effective tool to implement deliberate corporate strategy or provide the unique occasion to shift towards an emergent one. They can either allow a firm, to adjust its product-markets portfolio, at a speed not achievable through internal development; or provide the ability to gain all

benefits from pooling assets and sharing capabilities, in a way not obtainable through partnerships.

Teece and Pisano (1994) argues that the competitive advantage of firms stems from dynamic capabilities rooted in high performance routines operating inside the firm, embedded in its processes, and conditioned by its history. First, it refers to the shifting character of the environment; second, it emphasizes the key role of strategic management in appropriately adapting, integrating, and re-configuring internal and external organizational skills, resources, and functional competences toward changing environment. Firms resorting to 'resource-based strategy' attempt to accumulate valuable technology assets and employ an aggressive intellectual property stance. However, winners in the global marketplace have firms demonstrating timely responsiveness and flexible product innovation, along with the management capability to effectively coordinate and redeploy internal and external competences.

Morrow et. al. (2006) examine outcomes of strategic actions taken by firms lacking behind in marketing experience, from a RBV, valuable and hard to imitate strategy that recombines firms existing stock of resources to create new products, processes or technologies portraying positive influence on organizational recovery as measured by investors perspectives. Furthermore, acquiring new resources through M&As and using existing resources in new ways has a positive effect on investment experience. On the contrary a joint venture or alliance may not affect or lead to decline in performance.

Eschen and Bresser (2005) present a resource-based theory to explain the success and failure of M&As, using a two step model, based on conditions for deriving competitive advantage and financial results for closing resource gaps. The model suggests that if valuable and co-specialized resources are combined then both the target and acquirer benefits from the M&A activity. The first step explores new resources such as factor markets, internal development, and cooperation. In the second stage, financially advantageous M&A strategies are presented.

Moliterno and Wiersema (2007) maintain that firm's resources that are created or modified are based on the dynamic capabilities of the organizations and suggest that in order for firms to achieve competitive advantage, the decision to divest of strategically valuable resources occurs as a manifestation of the firm's efforts to achieve success. By conducting a study on individuals and team franchise, some light is shed on resource divestment as an important firm level resource management tool and more specifically extends our understanding of the rent appropriation mechanism at work in the strategic factors market.

Sirmon et. al. (2007) maintains that resource management involves the set-up of processes that firms use to structure their resource portfolios (e.g making changes to the resources available to the firm), bundle resources into capabilities to create value. Value creation or to achieve a competitive advantage can be created by recombining existing resources and capabilities or by acquiring or accessing new resources externally that are then bundled with existing resources into new capabilities. However, resource management processes carry significant risk, which must be sufficiently motivated to change existing resource portfolios and alter the firms' capabilities.

Connor (2007) maintains that competitiveness is derived from permanent infrastructural characteristics of organizational design providing a source of a continuous stream of temporary strategic assets or successful products, services and process. The study defines RBV along the following lines; i) the firm specific characteristics in providing competitive advantage versus the industry level; ii) intangible assets and capabilities; a focus on the variety of intangible assets and capabilities as a source of unique competitive advantage; and iii) organization structure and adaptability; the structure of the firm provides a key competitive advantage; iv) market and firm processes – asset complementarity and deployment – the way managers combine and deploy strategic assets in the exploitation of opportunities derived from an understanding of the market characteristics; and v) institutional factors and awareness; focus is on path-dependent characteristics of firm culture and the advantages they may provide, together with management of quality as a strategic asset.

Arend (2008) conducts a resource based view study on multi-strategic factors including opposing factors, covering multiple industries in crisis. The research highlights; i) how different SF's can be simultaneously compared; and ii) how the different SF types can simultaneously weighted in a net effect on a firms strategic choice of how to continue after a crisis occurs (pp. 352). They use the strategic assets and strategic liabilities factors as variables and postulate that the top five SA are strong brand, good customer service, specialized knowledge, product differentiation and good executives whereas the strategic liabilities are bad management, bad strategy, financial problems, bad acquisition execution and fraud. The research explores the balance between opposing strategic factors (i.e. beneficial versus detrimental factors) relating to which turnaround outcomes occur.

Eisenhardt and Martin (2002) define capabilities as involving tacit knowledge, they cannot be bought in market transactions rather they are internally developed, obtained through the M&A activity with the desired capabilities or created via a combination of the two processes.

Organizations are often constrained in the context of speed at which they can be developing new resources of knowledge, and market failure hinders the discrete exchange of intangible assets and information (Dierick and Cool, 1989).

Wang and Zajac (2007) conduct a study on measuring two forms of governance structures; alliances and M&As; presenting a dyadic perspective to examine how and why configurations of two firms resources and capabilities affect the costs and benefits associated with each governance structure and thus, the desirability of one structure over the other. They maintain that factors such as; i) the resource similarity and complementarity between a pair of firms; ii) the combined relational capabilities of a pair of firms; iii) the partner-specific knowledge between a pair of firms will affect the likelihood of observing that pair of firms forming an alliance vs. engaging in an M&A.

Bingham and Eisenhardt (2008) develop a typology of strategic logic (i.e. leverage, position and opportunity) that maintain while VRIN resources may be useful for

creating advantage, they maybe neither necessary nor sufficient for competitive advantage to ensue. The linkage of these core resources with one another and with complementary resources is moderate in order to facilitate redeployment of core resources into new combinations that are more appropriate as new markets are entered and existing one change. Position logic; in contrast focuses on building an activity system of resources that are tightly linked in synergistic relationships that occupy a unique, valuable strategic position and opportunity logic focuses on maintaining a few organizational processes (e.g M&As, alliances, new products development and or internationalization) that place the firm in abundant flows of attractive, but often fleeting opportunities, and develop a few heuristics to guide the fast and effective capture of those opportunities yielding the highest payoff.

Zollo and Singh (2004) maintain that the characteristics of the pre-acquisition resources of the target, resource quality, and market relatedness, show weaker explanatory power, with the market relatedness measure showing no statistically significant effect. One interpretation provided can be that companies entering the M&A activity can create or destroy value equally well through cost rationalization, typically prioritized in ‘in-market’ M&As, or through revenue enhancement processes, which become the priority in market extension M&As. The level of integration between the two M&A firms does however, significantly and positively influence performance while replacing top managers in the acquired firm negatively impacts performance, all else being equal. They suggest that M&As are complex, therefore, require more sophisticated and in-depth tools in terms of integration as there are a number of potential overlaps of resources and activities across the organizations and the ‘consequently array of simultaneous, interdependent decisions and actions necessary to accomplish integration.’

Anand and Singh (1997; pp. 101) define RBV as bundles of assets; to some extent some are ‘fungible’ in nature in declining industry and these resources ensure the firm to enter new industry domains, through continuity, survival and stability. They conduct a study based on diversification orientated M&As (diversifying into new markets) and consolidation orientated M&As (consolidating their operations within the industry) in

the declining industry. The research maintains that assets are redeployed more effectively through market mechanisms than within the firm through the acquisition of complementary assets.

3.3.3 Conclusion

This section merits importance because it discusses and highlights the concept of resources i.e. directly linked to the research question as to what types of resources provide a competitive advantage for the Japanese during the M&A stage and also how it facilitates them to come out of the financial crisis. Therefore, this is an imperative section to see where the gaps are in the literature from a resource based view and how they can be filled through the findings of this research. The gaps are discussed later in section 4.2.

3.4 Japanese Business Banking Literature

This section is split as; i) challenges of the Japanese financial sector; ii) traditional role of the Japanese financial system; iii) restructuring of the Japanese financial system; iv) traditional role of the Japanese business and banking system; and v) studies on the *keiretsu* characteristics. This will aid in the understanding of the underlying problems that led to the financial crisis and how the restructuring process was implemented to create a sound banking system in Japan.

3.4.1 Challenges of the Japanese Financial sector

The subsequent section throws light on the problems that led to the financial crisis i.e. non-performing loans; lack of disclosure and transparency policies; competition faced by subsidized financial institutions; lack of technological innovation; banks disproportionate stock portfolio in comparison to their capital base; and lack of profitability associated with high labour costs.

• Non- Performing Loans (1990-2000)

In March 1996, for the first time the non-performing loans were comprehensively disclosed (Horiuchi, 1999). The outstanding amount of risk management loans for all banks by end of March 1998 was yen 29. 7 trillion and by end of March 2001 was yen 32.5 trillion. Table 3.7 below shows a break-down of risk management loans and a proportion of GDP.

Yen Billion

	FY 1992	FY 1993	FY 1994	FY 1995	FY 1996	FY 1997	FY 1998	FY 1999	FY 2000
Risk management loans Cumulative write-offs	12,775	13,576	12,546	28,504	21,789	29,758	29,627	30,366	32,515
Total Proportion of GDP						49,669 (9.78%)	54,247 (10.91 %)	58,551 (11.86 %)	

Source: Adapted from Hoshi (2001, pp. 5)

*Risk management loans consists; i) loans to borrowers in legal bankruptcy; ii) past due loans in arrears by six months or more; iii) past due loans in arrears by three months or more; and iv) restructured loans (March 1998; Zenginkyo).

Table 3.7

Table 3.8 shows the risk management loans and ratio based on each banks loan portfolio.

Yen million

Code Bank	Risk Management Loans	Cumulative write-offs since 1992	Total loans	Bad-loan ratio	Bad-loans plus write-offs ratio	Special loan-loss reserves
Dai-ichi Kangyo	1,471,362	282,132	33,921,107	4.34%	5.17%	1,014,342
Sakura	1,475,401	53,037	34,328,583	4.30%	4.45%	929,928
Fuji	1,692,701	213,889	31,306,818	5.41	6.09	782,636
Tokyo-Mitsubishi	2,250,171	92,607	41,290,834	5.45	5.67	1,317,891
Asahi	994,617	106,491	20,460,087	4.86	5.38	613,647
Sanwa	1,287,580	110,704	32,895,295	3.91	4.25	774,460
Sumitomo	1,469,122	618,445	35,215,195	4.17	5.93	1,114,047
Daiwa	915,784	25,105	10,008,772	9.15	9.40	379,601
Tokai	1,221,628	86,148	19,795,525	6.17	6.61	714,257
Hokkaido Takushoku	2,343,353	134,105	5,857,834	40.00	42.29	1,675,537

Source: Hoshi (2001, pp. 5)

Table 3. 8

Table 3.9 shows the distribution pattern of the government bail-out plan. Together with measures worth yen 17 trillion for dealing with failed banks i.e. Hokkaido Takushoku Bank, the value of the total banking package came to yen 60 trillion or \$ 535 billion (at an exchange rate of yen 112 to the dollar), passed through the Upper House in 1998. This was partly funded through government guaranteed lending from BoJ within the Deposit Insurance Corporation (DIC). The remainder was financed by the issue of yen 7 trillion of special bonds (a type of revolving credit facility) by the government. Consequently, cost of meeting the BIS 8% regulation and clearing bad debts, as much as 67 trillion yen (13% of GDP) was accounted for.

Category of Banks	Cost (trillion yen)
Smaller Financial Firms	7-10
The Major Banks	20-30
Regional Tier I	7-10
Regional Tier II	5-7
Table 3.9	

- **Lack of Disclosure and Transparency**

Hoshi et. al., (2001) suggested the banking crisis may have been due to the unreported, untimely and improper disclosure of the true financial health of the Japanese banks including their loan portfolios. Lack of transparency and accounting problems, inadequate and slow response of the regulatory authorities to take corrective measures to resolve the banking problems in a timely manner; and the overcrowding of the Japanese banking sector maybe some other factors which may have attributed towards the weakness of the banks. Consequently, inappropriate auditing of accounts was presented, as auditors feared that they will be refused if they portrayed the real picture of the company (Kawai, 2003).

It was not only until after the bad loan problems arose, that the Japanese regulatory authorities started to implement the international reporting standards. Since 1993, the banks have included footnotes on their financial statements that classify loans according to the health of the borrowers. *Zenginkyo* has identified the loan amounts that need to be mentioned in the footnotes.

- **Delay in addressing the Banking Problems in Japan**

The financial authorities did not address the banking sector problems efficiently and swiftly as a result the problems grew bigger (Kawai, 2003). The idea was that once the economy picks up the clients would be able to pay back their loans. There was no domestic pressure for the government to resolve the problems due to high per capita income, high savings, zero inflation, relatively low employment, and no social unrest. Furthermore, due to large foreign reserves, no balance of payment problems, and a stable currency the Japanese government was comfortable with the situation. Subsequently, in the absence of adequate legal frameworks for dealing with insolvent institutions, there was hesitation in taking decisive measures for fear that it might touch off a banking panic.

- **Moral Hazard and Information Asymmetry**

The fragility of the Japanese banking sector can be attributed to moral hazard. A situation in which someone insured against risks will purposely engage in risky behaviour, knowing that any costs incurred will be compensated by the insurer. If the project succeeds, the borrower profits a lot and if the project fails, the bank will bear most of the loss, thus creating non-performing assets. In Japan, banks took on greater risk in the expectation that, if they suffer losses, the Ministry of Finance would bail them out. The system offers "rescue packages" therefore, may encourage borrowers and lenders to undertake low-quality or high-risk investments, thus increasing the likelihood of a crisis (Park, 2002). This behaviour is often linked with adverse selection, which has been part of the banking industry of Japan since the 1950s. An alternative to formal liquidation was carved out, as troubled banks were merged, when necessary (Aoki et. al., 1994).

The asymmetric information problem arises when banks or lenders have less accurate information than borrowers regarding potential risks associated with the projects of the borrowers. This asymmetric information often leads to adverse selection, a situation in

which, in the absence of adequate information about borrowers, lower quality borrowers with higher credit risk are the ones finally selected for loans. However, in the *keiretsu*-main bank system this does to some extent mitigate the problem of information asymmetry.

- **Competition faced by subsidized financial institutions**

Private banks in Japan were in direct competition with the subsidized government financial institutions as they offered competitive products at cheaper prices with a large network base i.e. the postal savings system of Japan has 40 times the number of branches as compared to the largest banking group (Fukao, 2003). The extra convenience of the postal accounts, combined with the government guarantee of deposits, represents a major challenge for the banks.

The government-subsidized Housing Loan Corporation (HLC), *Jusen*, non-bank financial institutions founded in the 1970s to complement the banks housing loan schemes, received subsidies from the government and therefore, acted as savings for the customers. HLC loans had lower rates and no prepayment penalties. This compromised the banks' ability to make money through home mortgage loans (Kashyap, 2002).

In 1993, HLC, *Jusen* companies shifted their lending towards real estate developers and ended up in problems due to lack of experience in commercial lending. The losses of the *Jusen* amounted to about yen 6,410 billion which further deteriorated the financial health of the Japanese financial system.

- **Lack of technological innovation**

New technological innovation has been providing cost-cutting services for the Japanese banks. Japanese banks, however, have been unable to take advantage in order to compete aggressively with foreign financial institutions and in foreign markets (Patrick, 1998). This is primarily because Japanese bank employees do not possess the relevant

and required market skills to absorb, learn and implement these technologies and therefore, simultaneously, upgrading their financial technological systems. However, a few major financial institutions in Japan have adjusted to these market realities, at least in their foreign operations, i.e. Nomura Securities Company's New York operations were highly profitable in 1996.

- **Banks stock portfolio too large for their capital base**

Japanese banks hold enormous amounts of stock, compared to industrial companies and foreign financial institutions. Although they are barred from owning more than 5% of the outstanding shares of any one domestic company (Anti-monopoly Law, Article 11), there is no ceiling on the total amount of stock that they may hold as long they invest in a number of different companies.

Previous regulations on large loans looked only at loans and guarantees, not at the credit exposure from security purchases (stocks and bonds) or from off-balance sheet transactions (Kashyap, 2002). This allowed banks to use stocks and bonds, in addition, to lending companies with large loan amounts. As share prices are volatile, banks have an extremely large exposure to price risk. It is estimated that, from 1975 to 1995, the average annual rate of return on stock investments declined to 10.7%, from 21 % in the 1955 to 1974 period. The six years from 1990 to 1995 were particularly bad, with the average rate of return from stock investments at -6.7%.

- **Lack of Profitability and High Labour Costs**

Japanese banks could not earn high profits on their lending, due to the low interest margin relative to their assets, hence incurring difficulties in meeting their operating costs. Furthermore, high labour costs also hindered banks in generating profits. However, the banks have made some progress in reducing salary and wage expenses from about 52% of operating costs to 46% in the 1990s (Kashyap, 2002).

- **International Economy – Globalization**

Japan, especially, Japanese banks holds a major portfolio in the world economy and therefore, due to the sluggish global economy, Japanese banks were hurt drastically, to an extent that they had to retrieve from overseas operations (Aslam, 2005). Therefore, Japan's economic and financial policies are subject to reactive foreign pressures from the United States, Europe and other countries where it holds a significant amount of shareholdings (Patrick, 1998). Secondly, Japan being the world's largest creditor nation, was exposed to foreign exchange risk as well as other economic and political uncertainties. As the Yen appreciated, the cumulative losses were huge, almost of a similar magnitude as the financial system's domestic bad loan losses. Thirdly, as the emerging capital markets evolved and expanded, (such as the Euro market), Japanese companies bought inexpensive bond and equity rather than taking out loans from Japanese banks. The MoF was ineffective in altering this offshore financing activity. Fourthly, continuing deregulation made it attractive for foreign banks, investment banks and similar organizations to compete in the Japanese market, thereby, constraining Japanese banks business in Japan (Hoshi and Kashyap, 1999).

3.4.2 Traditional role of the Japanese Financial System

This section discusses the i) convoy system; ii) safety net system; iii) tax system in Japan.

- **Convoy System**

Bank failures were not significant in the post-war era and the banking sector was considered 'fail safe', as banks were regulated under MoF. Similarly, customers perceived banks to be indistinguishable and 'took it for granted that under the convoy system banks would never fail'. They believed as long as the economy is stable the financial system will also maintain its stability. MoF was acting as a guardian to protect the banking system and if a bank was nearing bankruptcy, it would find a healthier bank

for a merger or an alternative solution for its revival (Fukao, 2003a). At the time interest rates were regulated and thus, there was limited competition among financial institutions in terms of offering favourable rates or products or services. When banks were planning to open, close or relocate branches and or introduce new products and services, they were required to seek permission from MoF. Thus, there was hardly any interest on the banks part to introduce new products and services or streamline profitability as their main priority.

- **Safety Net**

In a provision to provide a safety net for the financial system, the Deposit Insurance System was established in 1971. The safety net is ‘a social system of ex post dealing with distressed banks and of distributing social costs associated with bank failures among related parties. This safety net minimizes the spill-over effect from the failure of banks and other financial institutions on the financial system as a whole (Horiuchi, 1999; pp. 27).’ Based on the confidence that the government had on the safety net, the financial sector lost the function of monitoring and disciplining the bank management. In 1986, after a revision of the law, DIC was provided with two policy options; i) a pay-off in which a failed bank would be closed down for liquidation and a depositor with the failed bank would be protected upto yen 10 million (per depositor). Beyond this threshold a depositor might even recover a portion of the deposit in the liquidation proceeding depending on the remaining value of the bank. The other conduit known as financial assistance, the business (i.e. sound assets and liabilities) of a failed bank would be transferred to an assuming bank. Usually, for a failed financial institution the shareholders capital will be first drawn to cover the losses, then the remaining will be covered by the financial assistance provided by the DIC, which would take the form of a transfer of funds to the assuming bank. The key feature of the financial assistance option was understood to be its flexibility in dealing with a failed bank, without entering into bankruptcy proceedings as in the case of a payoff.

- **Tax System In Japan**

Fukao (2003) discusses that the Japanese tax system was used by wealthy clients for debt financing based on real estate investments. The land transaction evaluation for tax purposes was used at about one half of the market value, and the debt was evaluated at its face value during the bubble period. This allowed for cost savings as the inheritance tax was high; 75% over 500m yen until 1988, and 70% over 2 billion yen. Moreover, capital gains on land were not taxed until the sale, and interest payments can be deducted from taxable income for companies and for those individuals who were investing in condominiums and offices. The property tax was very low, 0.1% of the market value, until 1990s. Therefore, a large number of real estate investments were carried out for tax planning.

3.4.3 Restructuring of the Japanese financial System

This section discusses the i) big bang; and ii) the accounting reform program.

- **Big Bang**

Financial deregulation in Japan started in the 1970s with the issuance of government bonds. Furthermore, in 1980s corporate bonds were issued as a means of alternative sources of financing through capital markets. With the decline in traditional business of retail deposits and commercial lending to large firms, Japanese banks also assorted to middle market business i.e. real estate investment. Bank lending increased for real estate investments based on collateral as it was considered sound investment by bankers. This was because nominal land prices were on the rise since World War II and the pace of land price inflation was higher than government bond interest rates (Fukao, 2003; pp. 368). This caused a shift in the bank portfolios from the manufacturing sector (decline from 25% in 1977 to 15% by the end of the 1980s) to the real estate sector.

In November 1996, Prime Minister Hashimoto initiated the Big Bang agenda to i) align the Japanese banking system with international standards by introducing reforms i.e. law, accounting and supervision system, and transparency in compliance with global standards; ii) strengthening capital markets and offering other financial products for Japanese banks in order to diversify into fee-based business; and iii) provide a market orientated platform for the Japanese banks to invest the yen 1,200 trillion of assets (Fukukawa, 1997). The program was implemented to resolve the bad debt problem.

Big Bang raised a number of questions, as to what degree of impact will trickle down the banking system. Bank of Japan perceived that those banks that are ready to undergo a major restructuring process will be able to handle the big bang and derive benefit from it and those that are not prepared to handle the change will be vulnerable to ‘be liquidated, merged with other domestic bank or taken over by foreign financial institutions.’ Therefore, deregulation in the banking sector is often attributed as the underlying reason for the banking crisis in Japan.

The Big Bang assisted with re-introduction of the holding company set-up and triangular M&As similar to U.S. style M&As which will enable Japanese banks to ‘regroup their activities in a way that is more efficient, both from an operational and taxation point of view.’ Shimotani (2007) also maintains that holding companies serve two purposes; i) to integrate existing companies into one; and ii) to re-organize internal organization of a company. Please refer to table 3.10 for the big bang agenda.

Items	1997	1998	1999	2000	2001
Expanding Options for Investors & Entities Raising Funds					
Full Liberalization of cross-border capital transactions and foreign exchange business	→	April 1998			
Introduction of General Securities Account (CMA)	→	October 1997			
Full liberalization of securities derivatives			December 1998		
Introduction of over-the-counter sales of investment trusts by banks and other institutions			December 1998		
Increased liquidity of asset-backed securities and other debts			September 1998		
Expansion of the definition of securities			December 1998		
Reform of the pension system	→	December 1997			
Improving the quality of services and promoting competition					
Utilization of holding company	→	March 1998			
Liberalization of the restrictions on the business operations of subsidiaries of financial institutions				October 1999	
Switch from a licensing system to a registration system for securities companies		→	December 1998		
Full liberalization of brokerage commissions				October 1999	
Permission for straight bonds and commercial paper issuance by banks				October 1999	
Making markets more user-friendly					
Improvement of exchange trading and abolition of order-flow consolidation for listed securities			December 1998		
Strengthening the functions of the registered over-the-counter market			December 1998		
Abolition of securities transaction tax and bourse tax			April 1999		
Partial elimination of withholding tax on Japanese government bonds			April 1999		
Upgrading the rules and framework for fair and transparent trading					
Introduction of Prompt Corrective Action measures			April 1999		
Enhancement of disclosure systems			December 1998		
Reforms of accounting standards: introduction of mark-to market accounting					March 2001

Source Baba & Hisada (2002, pp. 57)

Table 3.10 Big Bank

- **Accounting Reform Program**

In 1999, accounting systems were revised to reflect transparency and the true value of assets and liabilities of companies. The three important revisions are discussed in table 3.11. In FY 2001, cross-shareholdings were subjected to mark to market valuation of land, building, and equipment as the disclosure of assets at market value was on the increase. This change was already in place since the beginning of 1990s as cross-shareholdings were beginning to negatively influence the performance of companies based on the slow economic growth in Japan.

i.	The consolidation of accounts, through the adoption of substantial control criteria in place of the previous percentage-owned standard for determining which subsidiaries and affiliated companies fall to be included in consolidated financial statements.
ii.	Market-value accounting, which must now be used for certain assets instead of previous method of valuing at either acquisition cost or lower of acquisition cost and market value.
iii.	Pension accounting, through requirements that, for example, pensions obligations must be valued at current market value and make up for the shortfall within 15 years.

Source: Begg and Henning (2008, pp. 16)

Table 3.11

As foreign ownership was increasing with Japanese companies, investors required more information as they may not possess the relevant information unlike stable domestic shareholders (Yoshikawa and Linton, 2000). This suggests that as new banking laws and other restructuring avenues were created many institutional investors may pressure Japanese firms to adopt global standards for corporate disclosure therefore; Japanese companies are placing greater focus on market shareholders interests (Useem, 1998). The introduction of this new reform process suggested parent companies were unprepared to handle the large loan losses from their subsidiaries and therefore, were not prepared to consolidate ill-performing subsidiaries and affiliated companies into their financial statements. Therefore, large scale restructuring was taken up by companies in order to dispose off underperforming units.

3.4.4 Traditional Role of the Japanese Business and Banking System

This section discusses literature dealing with the inter-linkages between the former *zaibatsu*, *keiretsu* and their ‘main banks.’ This is a unique aspect affiliated with the ‘Japanese way’ of conducting business.

- **Concept: *Zaibatsu* (; property)**

Up until the first half of the 20th century, *zaibatsu*’s were referred to as large family-controlled banking and industrial conglomerates. The origins of cross-holdings can be traced back to pre-war Japan, when powerful Meiji families ran large banks that served as financial command centres of closely held family groups known as *zaibatsu*’s organized under a common holding company (Sharpe; 2007). The *zaibatsu* ‘relied on multiple industries, including iron and steel, railroads, oil, mining, and banking, and were managed by new and wealthy entrepreneurs and financial managers (Miyashita and Russell, 1994; pp.22). Each experienced rapid growth as a result of favoured treatment by the government and a special relationship with the military.

The four major *zaibatsu*’s, namely; Mitsubishi, Mitsui, Sumitomo and Yasuda date back to the Edo period. By the end of the war in 1945, the four groups’ alongwith their subsidiaries accounted for 24.5% of the joint stock capital in Japan (Yoshinari, 1992). There were also second tier *zaibatsu*’s, that were formulated after the Russo-Japanese war until the Pacific war, namely; Ayukawa, Asano, Furukawa, Okura, Nakajima, and Nomura, Kawasaki, Shibusawa, Riken, Fujita, Fuyo, Mori, Koga, Michitsu, Nissan, Nisso.

These conglomerates increased in scope and size due to the diversification strategy adopted by focusing on the haulage, manufacturing, distribution and banking industries (Sharpe, 2007, pp.7). One of the advantages of these groups was to concentrate in related industries in the same production location because closeness to competitors and buyers or suppliers allowed faster learning about new products, technology, markets and ideas, reduced costs and improved communication. This circular force, allowed

Japan to maintain its comparative advantage in the manufacturing industry. One of the disadvantages associated with the industrial grouping is the considerable congestion costs and high office rents and wages.

The core of the group consisted of the main bank, general trading company, called a *sogoshosha*, both under the strict control of the holding company. The main functions of the bank were restricted to the granting of loans to group companies. In 1946, the *zaibatsu* were dissolved, and the modern *keiretsu* system developed.

- **Concept: Keiretsu**

In 1952, after the end of the occupation forces, the former *zaibatsu*'s started to re-emerge and reorganized in the form of *kin'yu keiretsu* centred on their respective main-banks, including the setting up of the human structures in the form of executive clubs and federations where company presidents held regular meetings. As a result, many large Japanese firms are now members of *keiretsu*, characterized by a complex web of inter-corporate ownership, a trading company (*sogo shosha*) and a main bank (Morck et. al., 2000).

Keiretsu literally means; series or chain and is divided into three categories; i) corporate group *keiretsu*; ii) supplier *keiretsu*; and iii) distributor *keiretsu*. *Keiretsu* in English means the succession in the sense of a sequence of entities joined together as linked in a chain (Abegglen 1985).

Bird (2002, pp. 96) maintains there are two kinds of *keiretsu*'s; horizontal *keiretsu*, also sometimes referred as horizontal corporate conglomerate or *kigyo shudan* collections of many companies spanning many industries and characterised by cross-shareholdings and a core bank or cash-rich company constituting *konzerns* (financial monopolies); and vertical *keiretsu*, pyramids of suppliers dominated by large manufacturers and constitute trusts. Cross-shareholdings are the glue that binds the horizontal *keiretsu* (Yoshinari, 1992, pp. 198).

Keiretsu used a business group – 6 groups; centred on the large Japanese banks (also called financial groups, financial *keiretsu* or horizontal *keiretsu*). By the 1950s the major industrial groups Sumitomo, Mitsui, Mitsubishi and by 1970s the banking *zaibatsu*'s Sanwa, Dai-ichi and Fuyo were reborn. Miwa and Ramseyer (2001) define a main bank as the bank or institution from which the corporations within the *keiretsu* borrow the most funds. Aoki (1984) suggest that main banks serve as monitors to discipline corporate management. Gerlach (1992: pp 119) suggests that 'the large city banks associated with the six big inter-market *keiretsu* are the main banks for virtually all their group companies.' *Keiretsu*'s are based on *kabushiki mochiai* (cross-shareholdings, mutual aid shareholding), personal ties, internal trading and lending among *keiretsu* member companies and banks and informal communications (Muramatsu, 2000). ' *Kabushiki mochiai* (Bird 2002; pp. 96), specifically dictates the Japanese term for what is known as the cross-holding pattern; that is equity shares that two companies hold in one another. Cross-shareholding in turn is a subset of what is known as *antei kabunushi* (quiescent stable shareholding), which is held in trilateral, multilateral and or otherwise stable arrangements among companies.' The close relationship between the main banks and the *keiretsu* allows for both the allocation of credit and the efficient management of firms (Kim et. al, 2006). Furthermore, Ramseyer, (1998) notes that banks hold stock in their debtors, partly to overcome the moral hazard problem. As firms borrow money, they have an incentive to raise the risk level on the projects they undertake. Second, firms in the same industry invest in each other when relationship-specific investments make contractual opportunism a problem.

3.4.4 Studies on the *Keiretsu* Characteristics

Kim et. al. (2004) conducts research on the horizontal *keiretsu* from the prospective of power-dependence and suggests that benefits differ across member firms, depending on their power in the *keiretsu*. They maintain that powerful *keiretsu* firms are able to place more emphasis on growth in pursuing product and international diversification, whereas less powerful *keiretsu* firms are subject to strong monitoring and emphasize profitability.

Based on diversification strategies this research supports the study's proposition that power dependence relationship in a *keiretsu* influence member firms appropriation of group affiliation benefits.

Aoki (1993, pp. 268) advocates that the corporate governance system in Japan is based on 'decision-making in Japanese companies and is guided by the dual control (influence) of financial (ownership) interests (i.e. main bank) and employee's interests rather than by the unilateral control of the owners interests. In most cases the main banks are both lenders to business corporations as financial institutions and at the same time shareholders.

Bergloef and Perotti (1994), see the equity ownership as a 'hostage exchange' that promotes promissory credibility. Shares held by the banks and by other entities in the group are generally regarded as 'stable shareholdings', and do not show elements of adjustment with changing economic performance (Kang and Shivdasni, 1997). However, Japanese banks' shareholdings are influenced by regulatory changes and Japanese banks, were under the influence of the Bank of Japan up until the deregulation wave was instigated. Until 1977, banks could only hold up to 10% of a firm's outstanding debt. However, in 1977, the Japanese Anti-monopoly act lowered the limit to 5%, upon concerns of banks having too much control over corporations.

Hoshi et. al. (1990) document those Japanese firms with close bank ties tend to grow faster than independent Japanese firms during financial distress, suggesting that this arrangement mitigates the underinvestment problem associated with debt financing. Jensen (1986) also concludes that involvement creates the opportunity for banks to engage in stringent managerial monitoring, thereby improving firm value.

Weinstein and Yafeh (1998) posit that *keiretsu* firms have lower profit rates than do independent firms, and that main banks encourage a tendency to borrow and to maximize sales rather than profits. This is because growth in sale and market share is pretty uniformly more important to Japanese firms than profit or shareholder wealth.

Gerlach (1992) demonstrate that profits of *keiretsu* firms tend to be lower and less variable than other Japanese firms. This is because firms within a group have mutual insurance scheme, which enables firms with a profit in a year to support those with losses in that particular year, leading to a low profit variance for all firms within the group, sometimes; however, industrial groups will allow members to fail.

Isobe et. al. (2006) study is based on the relationship between *keiretsu* membership and firm performance from a risk and return trade-off view. The study shows that *keiretsu* membership has a negative effect on firm profitability, as *keiretsu* membership does not allow firms to reduce risks by smoothing out profitability. Consequently, *keiretsu* are likely to increase the gap between targeted and realized returns, which they refer to as aspiration gap. Firm size has a positive and significant impact on profitability and has a negative and statistically significant impact on firm risk. Firm age is not associated with profitability and does not have a significant impact on firm risk. They also maintain that internal risk sharing mechanism, such as product and geographical diversification do not play a significant role in reducing the risk. The Big Six ties are the fruit of post-war business development policies, referred to as Japan Inc. and spearheaded by the bank of Japan and MOF, through loans, corporates industrial policies, low interest rates, and the relaxation of the anti-monopoly Law.

Japanese banks from a limited comparative advantage have tried to maintain their stake in the retail and wholesale markets for both individuals and corporations, which form their core business, yielding large portions of their operational profits (Kashyap, 2002). Strengthening client relations has been a top priority for the banks and providing customized solutions, through which banks can then become more competitive in the shrinking domestic market. The banks are among the largest in the world, in terms of assets but lack the range of products and services. Recurring patterns has emerged where Japanese mega-banks are late to enter markets or offer new products and, therefore, have faced hurdles in increasing their profitability.

The relational lending, *keiretsu yushi*, acted as a monitoring instrument as well as a financing mechanism. Based on the high demand for loans made by *keiretsu* members,

banks would first screen the loan applications and then decide on the loan commitment to be made to the companies. Side by side, banks were forced to monitor the investments, a protective mechanism on the part of the bank to avoid non-performing loans. On the borrower's side such bank supervision worked as a monitoring device through which the effective functioning of project execution could be assured (Aoki, 2004).

Hoshi and Kashyap (2001a) maintain that the banks acting as main banks repeatedly rolled over loans to their customers, and therefore, the relationship grew stronger as a stable source of long term loans until the 1980s. Moreover, as the commercial banks had an abundant supply of cash, they found every opportunity within or beyond the main bank relational grouping for lending.

Caballero et. al., (2006) maintain that maybe prolonged recession of the 1990s was partly due to the banks lax loan restructuring, in which they had kept lending to insolvent banks. This practise was evident among the banks and *yushi keiretsu* companies. However, many banks were forced to change their relationship and realign according to the health of their respective banks. With the banks adopting more market and performance orientated measures, Japanese banks started to move away from traditional debt financing to equity financing.

Baba and Hisada (2002) discuss the Japanese financial system from the regulators point of view in redesigning and administrating the system. The research suggests that Japanese financial system is characterized by the main bank system and depends heavily on the banks whereas; in the U.S. the financial system is run by capital markets. With changes in the financial markets due to IT innovation, globalization, and financial deregulation, Japanese banks are moving towards capital markets. However, it will be a gradual change as after the financial crisis Japanese banks are submerged in a large share of public finance. The aim is to provide a sound and stable system by ensuring a balance between capital markets and banks.

Tadesse's (2005) study provides an economic rationale for structural changes in the Japanese banking industry based on degree of economies of scale and the dynamics of the technological progress. The study depicts that economy of scale decrease as bank size increases with small banks exhibiting significant scale economies and 'average' and 'large' banks display significant dis-economies i.e. long term and city banks. On the other hand, the evidence shows existence of a technological change that has operated to lower the cost of production, with the larger banks achieving higher cost reductions. This suggests that the underlying technological progress that has swept the banking industry in Japan has been increasing the industry's minimum efficient size – i.e. the scale of production at which total cost is minimized. The consolidation of the banking sector provides the economic rationale as the technological dynamics favour and necessitates large-scale banking, despite the diseconomies of scale. Finally, the study maintains that consumers would favour a concentrated banking industry whereby, they can take advantage of lower costs associated with the banks.

Rose and Ito (2005) discuss M&As of Japanese banks; they posit that, due to the pressures of globalization and the difficult domestic economic environment, some Japanese banks have been restructuring and realigning their business operations, which has included mergers and acquisitions. Japanese banks have reengaged in the practise of M&As, which is refereed to as 'nothing new, but a resurgence of past practise' (Rose and Ito, 2005, pp. 139).

Begg and Hennings (2008) maintain that the nature of Japanese business and its culture may have been associated with the slow acceptance of engaging in the M&A process. Additionally, M&As have been less significant in Japan as compared to the US and European markets. In Japan, historically M&A consolidation has been associated with a 'negative ring, implying unwelcome takeovers or sell-outs (pp. 1). This can be attributed to the fact that Japanese corporate and financial institutions have realized and developed the need towards growth and profitability of their organization and also redeploying poorly or under-utilized resources more efficiently and effectively.

The Japanese banks strategic objectives are (Kawai, 2003); i) gaining maximum market power in a region or a niche market; ii) attaining economies of scale and reduction in

operational costs; iii) generating profits to invest in information systems; and iv) build a critical mass in strategic areas such as investment banking, asset management and so on.

- **Change in the *Keiretsu* – Shareholding Pattern**

With the changing business environment of the 1980s and 1990s, some scholars consider that the ties between banks and companies are changing (Ahmadjian and Lincoln, 2001). Some companies have shifted from the traditional dependence on the main bank for borrowing, to the emerging capital markets, where they can achieve higher growth rates and more competitive products and services (Hoshi and Kashyap, 1999). This in turn, reduces the role that banks have previously played as stable stakeholders for large companies (Posen, 2003). In spite of the declining importance of the bank borrowings, most companies still have a strong desire to maintain tight relationships with a main bank, as many companies expect their main banks to provide emergency funding and assistance during a crisis. In exchange, industrial companies keep unnecessary deposits otherwise known as cooperation deposits concentrate their payments, payrolls, and employee transactions with the bank, and pay high bond underwriting fees. Companies may, however, consider changing their bank if i) the main bank reduces their share-holding; and or ii) the main bank's financial position deteriorates and rating declines to the point that it loses social credibility (Posen, 2003).

As many Japanese firms were required to disclose their true financial health with the introduction of the new accounting rules, they started to reduce shareholdings in affiliated companies (Shimotani, 2006). Moreover, there was mounting pressure on the companies to pay greater attention to their operational efficiency on the utilized capital, due to rising capital market pressures. This in turn has reduced the stable shareholding and reciprocal holdings; stable shareholdings has declined from 45% to 24% and reciprocal holdings declined from 18% to 7% between 1990 and 2003 (table 3.12; Colpan et. al. (2007)).

Year	Stable Shareholdings (%)	Cross-Shareholdings (%)
1990	45.60	18.10
1991	45.60	17.90
1992	45.70	17.80
1993	45.20	17.60
1994	44.90	17.40
1995	43.40	17.10
1996	42.20	16.30
1997	40.50	15.10
1998	39.90	13.30
1999	38.00	10.90
2000	33.10	10.40
2001	30.20	9.00
2002	27.20	7.90
2003	24.30	7.60

Source: Colpan et. al. (2007)

Table 3.12 Unwinding Cross-share holding pattern

With time, a change in shareholders composition has also changed in scope as executive's shareholdings has also increased among Japanese companies. This serves as being critical as executive shareholders align their interests with those of other shareholders and aim for maximization in shareholder value, rather than size or sales of the companies they manage, leading Japanese managers towards a more return-orientated goal (Colpan et. al. 2007). As the financial and corporate sectors unwind their cross-holdings the huge volumes of equities that will come into the Japanese market are expected to be absorbed largely by the personal sector, which has aggressive savings of about Yen 1200 trillion and foreign sector.

Kikkawa (2005) provides a conceptual model, discussing the role of the Japanese financial system in strengthening and aligning it with the requirements of the 21st century. The model is split into three time periods after the oil crisis, namely; i) the success of the Japanese economy and corporations from the mid 1970s to the mid 1980s; ii) bubble economy from the latter half of the 1980s through the early 1990s; and iii) failure of the Japanese economy and companies since 1990s. The argument based on the rebirth of the Japanese economy suggests that the financial and manufacturing system of Japan should not be lumped together rather it should be considered that the

manufacturing system has always flourished and sustained itself under the three phases, whereas, the financial system has been slow and considered a ‘failure’ throughout the three phases. The prescription is based on i) skill-building in the banking sector; ii) overcoming the ‘investment suppression mechanism’ that came into effect after the oil crisis; and iii) shifting to an enterprise strategy combining product power with services in order to increase revenue and building an international division of labour with East Asian economies. Furthermore, the research highlights that the financial system should establish two pillars; i) universal banks with strong international competitiveness; and ii) healthy regional banks with the capacity of meticulous monitoring.

- **Diversification in Long Term Employment System**

Up until the 1960s, Japanese business model was characterized by ‘lifetime employment (*shushin koya*)’, ‘seniority based wage system’ and ‘enterprise unions’ and ‘management by collective systems.’ Hayashi (2002) refers to this as a socio-cultural approach to Japanese management.

In the past seniority based wages were adopted based on age groups rather than on performance as an incentive to maintain life long employment. With changes in the managerial environment, notions such as the superior aspects of Japanese management have fallen into malfunction. Consequently, since the 1990s, with slow economic growth in Japan, companies started to recruit less thereby increasing the overall personal costs ultimately lifetime employment became employment diversification and the seniority system results-orientated (performance based).

Bird (2002), suggests that Japanese firms involved in the restructuring process adopted several measures that stopped short of outright lay-offs. The first was *shukko*, or dispatch of employees either temporarily or permanently to relate to companies. When firms exhausted their options for *shukko*, receiving companies become less willing and able to accept redundant employees, they turned to other methods of downsizing. Many women in secretarial positions were encouraged to retire and were subsequently replaced by soft-drink machines or temporary staff.

Another unique trait was with rejection of groupism, the desire for individual treatment was prompted. According to the ability-based approach, 'there was fresh recognition of groupism as a trait of Japanese ethnicity, with small groups rather than serving as a means of gauging ability.' The groups are aimed at securing flexibility in workforce size are; i) core group: utilizing ability acquired over a long term employment; ii) specialist group: utilizing a high-degree of specialist ability – medium term employment; and iii) flexible employment group facility of labour adjustment. A new element introduced into the Japanese management practise is that of flexi-time in time-keeping; the emphasis on self-help efforts, double-track ability development and employment recommendations in educational training and ability development or the promotion of a cafeteria plan in welfare program (Hayashi, 2002; quoted from Nikkeiren, 1995; pp. 48-49, 55).

- **Composition Change in Governance Structures**

Shimotani (2007) maintain's that in 1997, Sony company was the first to adopt a *shikko yakuin sei* (executive or operating officer system) to move towards a more efficient system based on U.S. governance models. This model split management roles of supervisory control and operational implementation, i.e. separating the executive officers from the board of directors. Moreover, the size of board of directors was reduced in order to make the decision making process more effective and allow the board to concentrate on the supervision of executive officers. Another introduction was the set-up of a U.S. style committee system in which the board establishes three committees – supervisory, nominating and compensation – that are supposed to monitor the functioning of executive or operating officers. Although, the executive officer system became popular, the diffusion of the legally backed committee, in which the operational officer system is integrated is yet limited (Colpan et. al. 2007).

Coplan et. al. (2007) explain that share ownership by performance orientated entities such as foreign investors, trust banks and others portray a positive and significant influence; *yushi keiretsu* shows no significant impact, as a result of which maybe bank

monitoring may have become less effective. Moreso, boardroom reforms in terms of the reduction of board size does not affect financial performance, and introduction of an executive officer system negatively influenced profitability. This was discussed in light of the fact that maybe functional separation of directors and executive officers has not been implemented and many boards still have overlaps and monitoring and execution functions. Further, stock options and executive ownership have remained ineffective as mechanisms to align the interests of senior executives and shareholders. In a nutshell, the study maintains that corporate governance such as shareholder governance and main bank affiliations can be classified as external factors and are supported by the study as having a positive effect on performance whereas, governance factors such as size and functioning of the board of directors and the structure of executive compensation classified as internal factors all reject the hypothesis.

- **Changes in Compensation Schemes**

The introduction of stock options and the transition of executives' salary to performance based system were considered to be a significant corporate governance reform, headed under the commercial code 1997. In 2002, the system only included management and employees of the firm but in 2002 after the revision of the law all stakeholders were also eligible to be granted stock options. Both systems were introduced to promote stockholder conscious management by strengthening the link between executive compensation and firm performance. Executive salaries traditionally were determined based on setting limits to total salary amounts. In 2002, based on a revision made in the commercial code executive salaries were linked with performance rather than setting limits on the total salary.

- **Governance Structure**

Amkudari (literally, 'descent from heaven') as discussed by Aoki et. al. (1994) maintains that regulators have been disciplined to monitor bank management, an informal system in which private banks (and other firms) accept retired government

officials as managers or directors. According to their argument, this system has encouraged regulators to monitor bank management rigorously and thereby faithfully play the role delegated to them by depositors (and or taxpayers). If they fail to do their job as monitors, and bank performance suffers as a result, they may not be able to land good jobs in private banks after retirement. Thus, banks financial soundness may be positively influenced by *amakudari*. If the regulatory authority and private banks bargain with each other over the amount of monitoring and ‘descending,’ the *amakudari* system would undermine the effectiveness of prudential regulation and allow banks to engage in unsound management at the expense of depositors and or taxpayers (Horiuchi and Shimizu, 1998). This agency problem hypothesis predicts that banks accepting *amakudari* officials from the financial authority will show poor performance in terms of soundness.

Some have suggested that the performance of banks accepting *amakudari* from MoF was poor not because MoF officials became part of the bank management, but because MoF officials were sent to badly performing banks. However, as Rixtel (1994) explains, most banks have a long history of accepting *amakudari* officials from regulatory authorities regardless of their performance. There have been cases as well where MoF personnel have been dispatched for the restructuring of management, and revival of distressed banks. However, it is also reported that banks have accepted *amakudari* officials long before their bad performance.

Horiuchi (1999) maintains that the regulatory authorities have been powerless in monitoring bank management. Rather, they tend to help incumbent bank managers to continue their high risk practices. Thus, concluding that the lack of effective monitoring by outsiders has been a traditional feature of the governance system in Japanese banking, which tends to offer weakness in the banks performance. This feature seems to have produced inflexibility on the part of bank management confronted by the serious crisis of non-performing loans since the early 1990s (pp. 34).

Mendenhall and Pudenko (2007) conduct a study on the present Japanese management system and how it is adapting to a more modern and competitive system. Based on

their study they identify Japanese company managers to put forward the following views regarding the Japanese banks; i) are clearly in a crisis; ii) profound strategic re-orientation; iii) opening up to outside influence; iv) major shifts in HRM practises; v) desire versus reality; vi) triggers of management system restructuring; vii) entrepreneurial ventures are so far largely neglected as potential sources for innovation; viii) foreign ownership of Japanese companies, difficult but not impossible; and ix) one's personal situation influences opinions. A comparison of the Anglo-Saxon and Japanese management model is provided (pp. 275).

Anglo-Saxon Management Model	Japanese Management Model
Market regulation	Governmental guidance
Shareholder Interests	Employee's Interests
Capital Markets	Bank loans
Constant Profits	Long-term market growth
Differentiation from Competitors	Imitation of best practises
Embracing Radical Change	Incremental steps towards change
Open, global, geo-centric mindset	Insular, domestic, ethnocentric mindset
Flexible trans-national alliances and supply chain	Rigid, national keiretsu structures
Proactive top-management	Delegation of decision making to middle management
Transparency in corporate governance and financial markets	Behind closed doors insider system of management and control
Clear accountability	Vague sharing of responsibility across people and networks
Flexible labor markets	Life-long or long term employment
Rewards based on performance	Rewards based on seniority
Originality, creativity, individuality, and benefits of diversity	Homogeneity, status quo, conformity and collectivism

Table 3.13

3.4.5 Conclusion

This section has been important as it throws light on the Japanese banking and business sectors including the problems within both the domains that led to the financial crisis of the late 1990s. As the research is based on Japanese banks it is imperative to study this section of Japanese business and banking as it not only discusses the background for this research but it also highlights what kinds of research has been conducted on the Japanese banking sector and where the gaps are to be addressed through this research. The major sections discussed through this research are the i) challenges of the Japanese financial system; ii) traditional role of the Japanese financial system; iii) restructuring of

the Japanese financial system; iv) traditional role of Japanese business and banking system and; v) studies on the *keiretsu* characteristics. These sections will no doubt aid in our understanding on how the Japanese bank M&As influenced a competitive advantage and facilitated in the organizational recovery of the banks overloaded with bad balance sheets and low asset quality.

3.5 Linkages

The literature review has been effective in providing an overview of what kinds of research has been conducted in the past on i) strategic management literature, encompassing the broad concepts of corporate strategy, diversification, M&As, strategic relatedness and resources'; and ii) the Japanese business and banking domains of literature.

The first section of this chapter discusses the relevant themes and theories circumventing around the concept of M&A strategy as a diversification mechanism. Moreover, the theories discuss the competitive advantage and other benefits derived under the umbrella of corporate strategy.

With the initial presentation of the theories on corporate strategy and M&As both from a macro-economic and micro-economic perspective literature on strategic relatedness along with empirical studies is presented. This section is crucial because it highlights the importance of the combination potential between the combining banks, thereby focusing on the competitive advantage derived through various combinations of entities. It circumvents around the concept of relatedness which is a major component of the M&A activity in the strategic management literature. The subsequent section focuses on the resource based view which is also considered to be a highly significant component of the M&A literature as the types of resources and their combination and or utilization in an effective manner promote the idea of competitive advantage and organizational recovery for banks undergoing the M&A activity. Finally, under the Japanese banking and business management framework various challenges, reforms and specific

characteristics of the Japanese banking and financial system are presented in order to discuss the unit of analysis of this research i.e. Japanese mega-bank M&As. This provides the basis for the research at hand. Furthermore, it suggests that Japanese mega-banks M&A activity has not been thus far examined with regards to what kinds of a competitive advantage they provide, if any.

In conclusion, therefore, each section discussed above has a specific placing with regards to this study as it provides a platform in framing the research questions. The research questions are the gaps in the different previews of literature provided above that need attention in the context of the Japanese banking and business literature in terms of Japanese bank M&As. While conducting the literature review a number of important themes that play a pivotal role in deriving a competitive advantage and providing organizational recovery for the banks has also been discussed in the subsequent section. These themes formulate the research questions and also the interview questions outlined in appendix 6 and 8. Moreover, through the literature review and the gaps highlighted, a number of propositions and a model are proposed to be tested through this research. In other words, the propositions are derived from the literature review in order to answer the questions and thereby, fulfil the research gaps in the literature. The propositions are tested through this research in order to validate the model derived from the literature. By fact finding and conducting the interviews the propositions are tested, in turn which classifies a model specific to the Japanese mega-banks. Therefore, fulfilling not only a major gap in the strategic management literature and Japanese banking and business literature but also enhancing our understanding as to what and how M&As present a competitive advantage and act as a source of organizational recovery for the Japanese mega-banks. Propositions are tested and presented in the case studies and a specific model for each Japanese mega-bank is presented. The advancement to the literature and compassion in fulfilling the research gaps from a holistic perspective are presented in the cross-case analysis section in chapter 7. Finally, the final model specific to Japanese mega-banks is also presented in chapter 7.

In a nutshell, after presenting the literature review with the analysis of theories and empirical and conceptual studies and the linkages between various components of this research as discussed above, the rest of the findings of the literature review is presented as follows. Research questions and sub-questions/themes are presented in the subsequent section. The research gaps which are covered by the research questions and the conceptual model derived from the literature is presented in chapter 4. Furthermore, the propositions derived through the literature review to be tested through the research findings are presented with the research gaps in chapter 4. This is the mechanism by which the literature review, research questions, research gaps, and propositions and model to be tested are linked together.

3.6 Research Question

M&As, strategic relatedness and resources advantages are broad concepts and have gained attention in the research arena, as has become evident through this study. However, with regards to Japanese mega-banks M&As providing a competitive advantage hardly any research has been conducted. Furthermore, research is scarcely documented with regards to the strategic relatedness of Japanese banks. Hence, this makes a plausible case for conducting research in this area. This study aims to highlight the relatedness between the combining banks that assisted towards the organizational recovery of the banks. What elements were considered critical in advancing the banks out of financial distress and resulting in a competitive advantage for the combining banks? Consequently, this research aims at understanding the nature of the similarities and differences between the combining banks, and how particular resources played important roles in achieving competitive advantage for the combined bank. It also reflects on how the change in the Japanese business practises i.e. the change in cross-shareholdings patterns has had an impact on the resource allocation among the new banks and how has the traditional *keiretsu* relationships impacted the Japanese banks. The research also aims to provide an overview of the reasons why the M&A activity took place in Japan. On a fundamental level this thesis is a reflection on how M&As

are planned in a new financial system born out of the financial distress. The planning or the initial phase includes the motives and goals and vision of the planned M&A activity.

This research is an investigation into the concept of M&As of Japanese mega-banks. This study looks at the resulting entity i.e. Japanese mega-banks and explains the process of the M&A that led to it, thereby, providing a competitive advantage for the newly formed mega-banks. The broad research questions are:

Research Question One

What were the reasons for the Japanese Banks to engage in the M&A activity?

Research Question Two

What strategic relatedness and resources influenced a competitive advantage for the combining banks and what implications did these have for the recovery of the banking and financial sector?

The study is also unique as these research questions are structured in the following three stages and they can be classified as themes or sub-questions formulating the basis and in providing support to answer the two research questions derived after the literature review:

- i) planning stage during the combining stage of bank M&As and background of banks
- ii) macro-economic and industry based rational for the Japanese bank M&As;
- iii) strategic relatedness phase in terms of products and services;
- iv) resource relatedness and profile
- v) strategic benefits and way forward for Japanese Banking Sector.

Please refer to appendix 6 and 8 for the interview framework, which provides details of the questions associated with each of these stages.

The location of the research is based in Tokyo, Japan. The unit of analysis is the headquarters of the commercial banks, known as city banks in Japan and after the M&A consolidation referred to as mega-banks; as discussed in chapter 2. Throughout this research the term M&A will be loosely referred to where two or three banks integrate to form a new bank.

Chapter 4

Conceptual Model Building

4.1 Background

Theoretical strands such as finance, economics, and organizational as well as strategic management have been dominating the academic streams on M&As. Questions like what types of strategic relatedness influences value creation, synergy realization or performance have received considerable focus with regards to M&A literature. However, research has been bifurcated and it appears that little research has been conducted on the Japanese mega-bank M&As. What research and practitioners have thus, far ignored is what strategic level relatedness existed among combining banks and what resources can drive M&As to reap a competitive advantage in terms of banking in particular the Japanese mega-banks. Has the consolidation process in Japan among the banks, facilitated in the survival of the Japanese banking sector?

This research aims to introduce a conceptual model for identifying competitively advantageous resources acquired through the M&A activity of the Japanese mega-banks and the strategic relatedness that existed among the combining banks. The model (figure 4.2 and 4.3) therefore, aims to extend the diversification theory and resource-based theory and provide insightful measures of why the Japanese mega-banks divulged in the restructuring process. More specifically, the first stage of the model tends to explore why M&As took place on a macro and micro level. Secondly, the research aims to highlight how Japanese banks may have benefited in terms of strategic relatedness and resources, thereby, aiding towards the resilience in the banking and the financial system of Japan, lost during the financial crisis of late 1990s.

This study is an exploratory and descriptive reflection, of the Japanese mega-banks sector. Furthermore, the number of M&As that took place between 1999 and 2005 among the Japanese mega-banks have further strengthened the need for conducting such research. The context of gaps identified for this study are examined in the following relevant literatures; i) M&As literature; ii) Japanese banking literature; iii) diversification and strategic management; iv) resources and competitive advantage; v) geographical context – Japan; vi) theoretical research evidence; and vii) research model.

4.2 Research Gap: M&As Perspective

M&As are a corporate strategy embedded within a string of historical events. M&As add value to the combining banks in terms of market power, operating efficiencies and acquiring strategically valuable resources with the removal of an inefficient management. Subsequently, if the objective is to resolve resource deficiencies, M&As are most likely to result in competitive advantage that benefits all shareholders, if the target possesses and combines strategically valuable resource positions (Lubatkin, 1983). As the number of M&As are increasing globally, more and more emphasis is being placed by corporate and strategic managers in understanding the concepts, value and mechanisms of how to achieve greater value not only through the pre-merger and deal structuring processes. As often M&As result in failure or do not yield the expected benefits as chalked out during the pre-merger stages or in Japanese context *nemawashi* stage.

Capasson and Meglio (2001, pp.15) suggest ‘that M&A is still a puzzle for academic and practitioners, despite the considerable amount of transactions carried out so far, on average, end up with disappointing outcomes.’ Furthermore, M&A outcomes do not confirm as to what asset combination creates value and what type of implications the consolidation process has on the overall combining entity (Lee and Pennings, 1996). Therefore, it is often regarded that literature on M&As complementarity’s and compatibility is bifurcated.

This argument provides impetus for this research in order to identify what kind of asset combinations may create a competitive advantage for Japanese mega-banks based on their recent M&A consolidation activity.

Proposition 1:

Planning is imperative for any business combination arising out of the M&A activity. Different stages take place during the planning stage and the Japanese banking and business domains have a specific set of planning measures that they undergo as explained in chapter 2.3.4. The following proposition is being tested through this research.

The higher the level of planning and strategy the more fundamental and greater the chances for competitive advantage arising as a result of the combining banks and the quicker the organizational recovery

Proposition 2-4:

There are a number of different types and levels of combinations that take place during the M&A stage in the banking sector ranging from simpler to more complex means yielding value addition. Therefore, for this research the following is ascribed:

Proposition 2a: The simpler the level of integration the greater the level of competitive advantage and the quicker the organizational recovery

Proposition 2b: the more complex the integration level the more the competitive advantage however, the chances of problems arising are great and therefore, organizational recovery maybe slow

Proposition 3: Market Power; M&As are a means of strengthening competitive positions by reducing over-crowdedness in home markets therefore, cross-selling products and services and acting as a means of providing organizational recovery.

Proposition 4: M&As are a means of size competitiveness; a means of achieving size in terms of scale and profitability, therefore providing a competitive advantage and a source of organizational recovery

4.3 Research Gap: Japanese Business and Banking Perspective

Japanese banks decided to use the platform of M&As as a diversification tool to overcome the Japanese banking crisis at the turn of the 21st century.

A number of studies have been conducted from a Japanese business perspective i.e. deriving shareholders value from *keiretsu* structures (Weinstein and Yafeh; 1998); and change in the relational banking between *keiretsu* and main-banks (Caballero, 2006); M&A strategies (Rose and Ito, 2005); risk-return (Isobe et. al., 2006); technological innovations (Tadesse, 2005).

Keiretsu affiliations play a significant role in providing and sharing resources among their affiliated companies and main banks. With regards to the Japanese business a number of changes have taken place in terms of their change in cross-holding pattern and governance structures. The change in the *keiretsu* cross-shareholding pattern took place as the shareholding was negatively impacting the banks value due the economic downturn in the Japanese economy of the 1990s. In the context of Japanese banking business, research gaps appear both from a macro-economic and micro-economic level.

With so many changes taking place within the Japanese banking sector, not much research has looked at how the various resources being shared among the companies and main banks that have been affected or changed? Has the change subjected a positive or negative impact on the bank resources? Kim et. al. (2004, pp. 614) maintain that ‘despite recent studies on diversification strategies of Japanese firms, how these *keiretsu* affiliations affect the diversification-performance among *keiretsu* member firms is relatively unexplored.’ Therefore, more studies on the *keiretsu* system may provide insights as to how changes that are taking place within the Japanese banking and

business environment over time might affect the performance and strategy of companies. Moreover, to bridge the gap between studies conducted on Japanese banking sector and diversification i.e. M&As, suggest that the knowledge about performance and competitive advantage are limited in terms of product and international diversification, therefore, they encourage to conduct more studies in this domain.

Proposition 5:

Japanese banks have held a very specific and unique position among the Japanese business sector. They have been acting as main banks for their affiliated group of companies and thereby have held long term relationships with their corporate clients with cross-shareholding structures. However, with the changing trends in globalization, weak Japanese banking and business environment and opening up of capital markets some changes have taken place between the *keiretsu*'s and the main banks. In judging if this change in relationship has had an impact or not on the banking M&A activity the following proposition is being tested through this research:

5a The more the banks are related or belong to a *keiretsu* group, the more the competitive advantage and faster the organizational recovery for the combining banks as many resources are shared.

5b. The change in the cross-shareholding pattern between the banks and affiliated *keiretsu*'s has been changing and displays no sign of change among the competitive advantage that banks can derive from the *keiretsu* affiliates.

Proposition 6:

The Japanese financial crisis took place as a result of a number of different problems in the banking sector. One of the major problems was the large number of non-performing loans on the balance sheets of the Japanese banks. Therefore, while understanding the

problems of the Japanese financial sector and why the M&As took place in Japan, the following proposition is being tested for:

Non-performing loans are considered to be the driving force behind the banking M&A wave and the financial crisis in Japan.

Proposition 7:

As a result of the tight economic and global business scenarios developing during the mid 1990s, Japanese financial regulators started implementing and freeing the Japanese banking sector into a more liberal and de-regulated sector. The big bang program was introduced as a result and a number of new policies were initiated to provide a more stable banking sector in Japan. As a result while testing for the drivers leading towards a competitive advantage for Japanese bank M&A activity the following proposition is tested for:

Big Bang reform did not translate into providing a significant impact on the combining banks and therefore the competitive advantage and organizational recovery for the combining Japanese banks maynot have been so significant.

Proposition 8:

As de-regulation was becoming prevalent in the Japanese banking sector the governance style was mimicking the American management style. Therefore, as literature maintains it would be interesting to note how if any this has influenced an impact on the reasons as to why Japanese engaged in the M&A activity and or derived some value addition. Therefore, the following proposition is tested through this research:

Changes in corporate governance style of Japanese banks management displays a positive impact in influencing a competitive advantage and providing organizational recovery.

Proposition 9:

The Japanese banking sector has been circumventing around a specific set of policies dictated by the Japanese financial regulatory authorities, therefore sometimes there performance has not been as it could be because they were restricted as to what they can and cannot do. One specific policy is the *amakudari* practise whereby retired Japanese MoF officials are placed in the management of the Japanese banks. To see if their experience is positively or negatively associated with the performance of Japanese banks the following proposition is tested:

***Amakudari* practise hinders the performance of the banks therefore, does not yield any competitive advantage or provide organizational recovery for the Japanese banks.**

4.4 Research Gap: Strategic Management Perspective

Diversification in terms of strategic relatedness and performance has received considerable attention over the past five decades. Scholars have discussed strategic relatedness deriving synergistic benefits from a number of different perspectives; economics perspective, Seth (1990); financial perspective, Berger (2000); and corporate strategy perspective, Salter and Weinhold (1978); and Shelton (1988). The strategic management literature has also attempted to extend the ideas by drawing attention to the causes of valuable M&As (Barney, 1998) and some research provides evidence that M&As are important as a means for restructuring firms to increase their performance (Lubatkin,1987). Others yet have focused on synergies and stressed that strategic relatedness is not a sufficient condition for acquirer shareholders to earn abnormal positive returns (Barney, 1988).

Scholars maintain that M&A research has not reached a state of maturity as most research is bifurcated, non-consistent and non-interdependable results released and there is lack of consensus on key relationships (Palitch 2000). The diversification performance concept has been fragmented as it has been studied through many different disciplines. Sirower (1997) presents two problems with M&A relatedness that may explain conflicting or incomplete findings; i) less focus on the degree of relatedness and ii) lack of awareness on what other variables may define performance when relatedness does not have a direct effect. Moreover, Harrison et. al. (1990) suggest's that different results have been concluded due to the nature and methodologies employed. These ideas identified by scholars suggest that conducting research on the Japanese mega-bank M&As may present some insights as to the relationship; motives, relatedness and competitive advantage in the combining Japanese mega-banks. Thereby, adding volume to the depth and breath of the strategic management literature.

Proposition 10a : Diversification is a means of redeploying resources in the market thereby, providing a competitive advantage and organizational recovery.

Proposition 10 b: Diversification is focused on profitability then growth versus the traditional Japanese business practise of focusing more on growth than profitability thereby, providing a source of cost savings in terms of competitive advantage. This in turn acts as a source of cost savings and influences a competitive advantage and provides a means of organizational recovery.

Proposition 10 c: Diversification with regards to long term employment is positively related to reaping a competitive advantage and providing organizational recovery among the combining banks.

Proposition 10 d: Diversification in terms of offering more products and services for customers in order to gain a competitive advantage and enhanced sales provides a quick source of organizational recovery.

Proposition 11:

The concept of relatedness is fundamental to the combining of banks taking on board the M&A activity. It is their level of complementarity that defines the success of the M&A. Therefore, based around the research questions the following propositions will be tested through this research:

Proposition 11a: The greater the level of relatedness in terms of complementarity the greater the competitive advantage and quicker the organizational recovery.

Proposition 11b: The more the strategic fit – relatedness among the combining banks products and services, markets, resources and other combining characteristics the greater the competitive advantage reaped by the new banks and the faster the organizational recovery.

Proposition 12:

As a concept of relatedness and competitive advantage, the number of M&A activities encountered by banks provides them with more experience in handling the subsequent M&A activity, therefore, this concept is also tested in this research.

The greater the number of M&A activity the banks have experienced the skills acquired provide a competitive advantage for the new banks and the quicker the organizational recovery due to the experience and knowledge shared among the combining banks and the opportunity to learn from past M&A experiences.

4.5 Research Gap: Resource Based View

Research on resources based view has been discussed in different contexts; some stress the types of resources and their attributes in creating competitive advantage, some suggest long term competitive advantage and others yet, through light on the effect of resources utilized on the industry and finally some research to see how specific resources evolve over time and their competitive implications over time (Barney, 2001). The resource based perspective, is closely linked to both strategy formulation and strategy implementation, but the use of traditional measures only postulate strategy formulation. Sometimes, synergistic potential of M&As may be over exaggerated and therefore, lack the means of closing resource gaps through alternative methods (Zajac and Bazerman, 1991).

Resources acquired through M&As have the advantage of not being restricted by a firms existing base (Krishnan et. al., 2004), and therefore, there are no limitations concerning the extent to which newly acquired resources can differ from existing ones. In order to acquire some innovative and strategically valuable resources, some disadvantages may also be taken under consideration. It should be noted that the greater the difference between old and new resources, the more difficult it will be to combine such resources.

Eisenhardt and Martin (2000; pp. 1106) suggest that RBV does not necessarily explain why and how sometime some firms have a competitive advantage in situations where there is a rapid and unpredictable change. These markets are often defined as the 'competitive landscape which is shifting, the dynamic capabilities by which firm managers integrate, build and reconfigure internal and external competencies to address rapidly changing environments (Teece et. al. (1997). Some research on market coverage in terms of both domestic and international relatedness has received less coverage from resource theory perceptive. Existing literature is limited, fragmented and anecdotal (Buonoo and Bowditch 1989). All these studies suggest there is a systematic relationship between the type of market a firm chooses to enter and its resource profile. A relationship between resources, type of markets, and the potential for value creation

can be determined. A resource based view of diversification can overcome some of the limitations associated with traditional product – or – market based diversification theory and research (Harrison et. al., 1991).

It could be that the strategies are formulated well, however, maybe implemented inappropriately. Therefore, based on this argument, it would be interesting to see how the Japanese mega-banks benefited from their consolidation process in terms of closing resource gaps. Therefore, the following propositions deserve merit:

Proposition 13:

Proposition 13a: Resources are deemed critical during the M&A activity as it is there combination and allocation that provides value addition and organizational recovery for the combining banks.

Proposition 13b: The types of resources (organizational, physical, strategic and financial resources) play a critical role in reaping a competitive advantage and organizational recovery among the combining banks.

Proposition 13 c: The configuration in the joining of resources also provide a competitive advantage and organizational recovery for the banks. The more closely aligned/similarities exist among the combining bank resources the more the competitive advantage and organizational recovery for the banks.

Proposition 13d: The nature of the resources i.e. its source (combining, new and unique) is a deriving force in drawing a competitive advantage and providing swift organizational recovery for the combining banks.

4.6 Research Gap: Geographical Context – Japan

M&As research has been reported at an unprecedented level by North American and European financial institutions. However, from an academic perspective the M&A research activity has not been as widely studied as compared to the level of M&A transactions taking place in Japan. In Asia, since 2000, especially Japan, M&As have been widely acknowledged as a diversification tool since 2000. Therefore, this leaves ample room for conducting research on the Japanese banking sector, as is evident that in 1980s, 20 city banks were brought down to 4 mega-banks and 1 super-regional bank by 2000.

4.7 Theoretical Research Evidence

In sum, this research is being proposed for the following underlying reasons; i) limited conceptual and empirical investigation on the M&A activity taking place in Japan, especially, in the Japanese banking system; ii) subsequently different M&A waves are a consequence of a number of different reasons however, there is limited information on M&As caused due to the financial crisis and the change in pattern on the cross-share holding pattern among the Japanese banks and their keiretsu affiliated corporates; iii) strategic relatedness has attracted limited interest from academia in the context of Japanese financial crisis and M&As, thus it is imperative to stimulate research interest in M&As in the Japanese banking sector; iv) little research has been conducted using qualitative – case studies on the Japanese Bank M&As, leaving a gap to be filled in terms of detailed understanding of the phenomenon; v) strategic relatedness and resources influence competitive advantage in the context of M&As in the banking sector have not been widely studied; vi) as numerous M&A research has been reporting different outcomes, it is necessary to investigate and validate the extent literature on motivations of M&As; strategic relatedness and resources under the umbrella of competitive advantage and organizational recovery in diversifying banks.

4.8 Overview: Research Model

In a nutshell, the literature review discusses the topic of strategic relatedness, similarities and differences among the combining banks and resources that provide a competitive advantage among Japanese mega-banks, thereby addressing a gap in literature. The roles of various players, and implications for both policy makers and the economy, will also be discussed.

Figure 4.2 and figure 4.3 present conceptual models derived from the literature, to be tested through the findings of this research. Both these models are directly linked with the research questions, that have been derived through the literature, therefore, they will provide the answers to the two questions under review for this research as mentioned in section 3.5. Conceptual model 1 presents the themes that provide M&As a competitive advantage and corporate recovery. The oval boxes narrate the actions and the outcomes whereas the square boxes act as a tool for arriving at the said action, i.e. the Japanese banking crisis provides a catalyst for the Japanese banks to adopt the M&A strategy as a solution based on a number of different strategies, as an outcome to competitive advantage and organizational recovery. Conceptual model 2 builds on the first model in terms of providing in-depth characteristics of the various tools and actions, presented in model 1. More specifically, figure 4.3 is drawn from the findings of the gaps in the literature as discussed above as to why this research will play a significant role in our understanding of how the Japanese mega-banks achieved competitive advantage and organizational recovery of the banks stemming from the M&A consolidation. The framework suggests why the Japanese banks engaged in the M&A activity (determinants); what the strategy the banks adopted (solution) and what characteristics of the combining banks (strategy in terms of relatedness and resources) influenced competitive advantage and organizational recovery for the mega-banks formed out of the M&A process. This model 2 will be tested, amended and then presented for each bank in each case-study (chapter 6) based on the findings derived through the research questions. Then a comprehensive model (chapter 7; figure 7.1) will be amended and presented, as a conclusion and addition to M&A and Japanese banking literature based

on the M&A strategy adopted by Japanese mega-banks in deriving a competitive advantage and providing corporate recovery for the Japanese banking sector (tables 7.1 and 7.6).

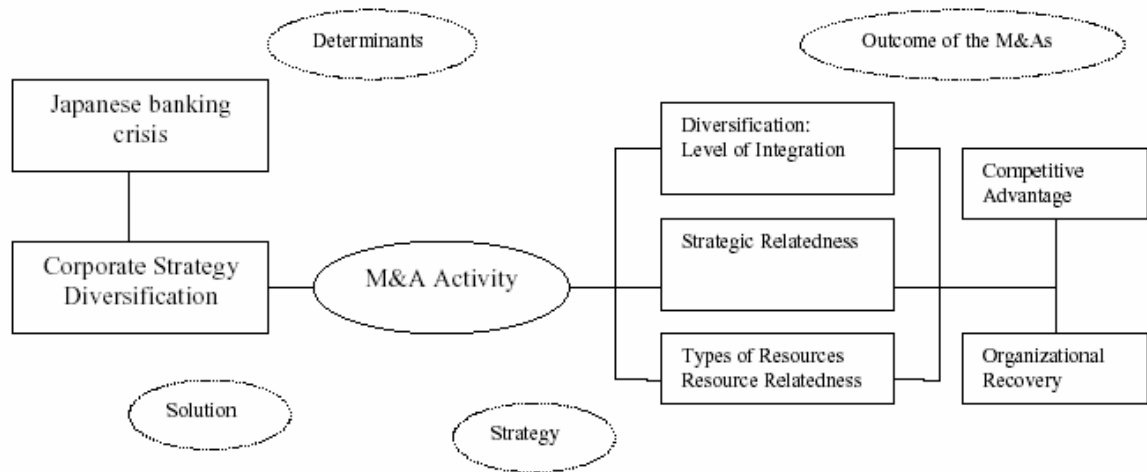


Figure 4.1 Overview: Framework Based on Research Question

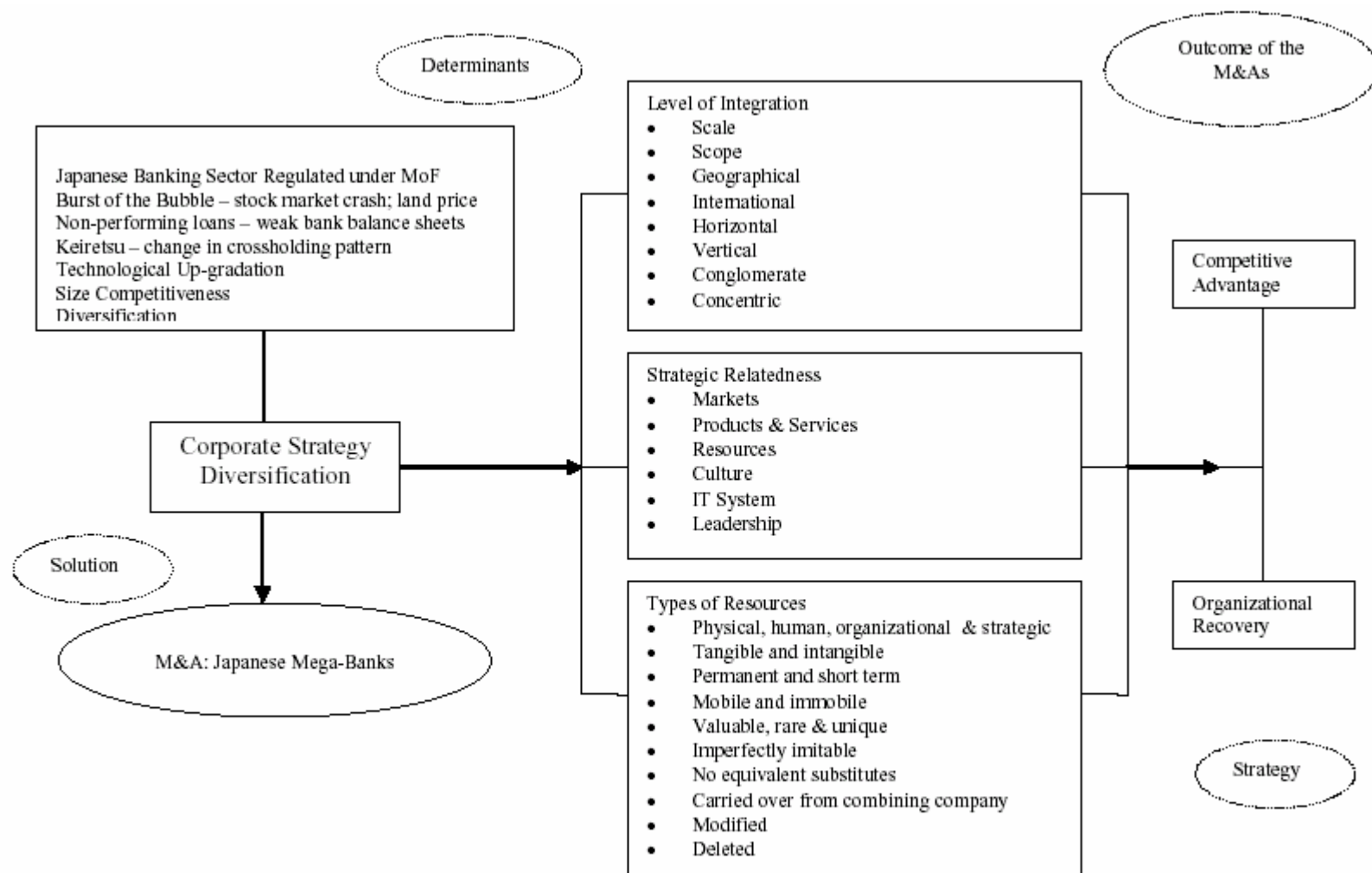


Figure 4.2 Conceptual Model 2 – to be tested on the Japanese Mega-Bank M&As (derived through literature)

Chapter 5

Research Methodology

This research methodology section discusses the i) research approach; ii) research design; iii) research collection; and iv) data analysis stages of the thesis.

5.1 Research Approach

Scholars have divided the research approach into two main categories, namely: qualitative and quantitative research. In this section an analysis between qualitative analysis and quantitative analysis is provided along with what type of approach is used for this research and why?

Research on the banking M&As favours quantitative analysis through accounting, event, dynamic and static studies (Zajac and Bazerman, 1991). It has been highlighted by scholars that research on firm performance has focused on complementary nature of M&As based on event studies mostly with the use of capital asset pricing model (Lubatkin 1987). Consequently, research on compatibility has focused on non-financial measures based on ethnographic methods (Buono and Bodwitch 1989). This is suggestive that less research has been conducted through the qualitative platform.

Research is often depicted as a sequence of planned stages in which research design precedes information gathering, followed by analysis and report writing. Creswell (2007) links three elements of research inquiry; knowledge claims, strategies and methods to present a set of different approaches to research. Knowledge claims according to Creswell (2007) maintain that the research starts a research investigation based on 'certain assumptions' about how they will learn and what they will learn during the enquiry. The research approaches such as qualitative and quantitative analysis are translated into the design process such as questions, theoretical framework, data collection and analysis, write-up and validation. In turn, these three elements can assist with the research approaches.

On a broader level, scholars often maintain that one of the differences between qualitative and quantitative research can be defined as; qualitative research composing of interviews, field observations and documents whereas, quantitative research

including surveys, tests and experiments and or mixed methods? Denzin and Lincoln (2000, pp.8) further maintain that qualitative research ‘emphasize on the qualities of entities and on processes and meanings that are not experimentally examined or measured in terms of quantity, amount and frequency. On the other hand, quantitative analysis studies emphasize the measurement and analysis of casual relationships between variables not processes.’

For this research thesis, a qualitative approach based on case study style has been chosen (Yin, 1994). Some of the major characteristics suggested by Cresswell (2007) are; the research takes place in natural settings, as the researcher goes to the site (home, office) of the participant to conduct the research. This enables the researcher to develop a more fundamental understanding of the phenomenon as to why and how the topic under investigation evolved. Secondly, qualitative research employs multiple methods of research that are humanistic and interactive. It helps to build the rapport between the individual conducting the research and the participant. The data collection methods include interviews, structured or semi-structured; observations; documents and audio-visual material.

Qualitative procedures are described to make use of text and image data, possess unique steps in data analysis and draws on diverse strategies of inquiry. As a number of issues and facts emerge during the data collection phase, the inquirer can refine the ideas and gain in-depth knowledge about the topic under investigation. This includes developing a description of the topic at hand, analyzing data for themes and or categories, and finally drawing a conclusion by making interpretations. This follows theoretical formulations, stating lessons learnt and offering further areas of investigation.

More specifically this research on Japanese Banks M&As is an empirical justification, based on multiple case studies by deploying a triangulation approach. Scholars suggest that when the nature of research is to develop an in-depth understanding and inquiry into the long term effects of resource driven M&As, longitudinal and qualitative research demands merit. Case study and cross-case analysis can cement an in-depth understanding towards the consolidation process of the bank M&As at closing resource

gaps and achieving competitive advantage in Japanese mega-banks. It will illuminate the underlying factors that encouraged Japanese mega-banks to engage in the M&A activity and what kinds of strategies and resources were employed to achieve a competitive advantage through the M&A activity of the mega-banks in Japan. Therefore, testing the theoretical model developed in this research and adapting it to the Japanese mega-bank strategies through the research findings. The study is qualitative in nature as there is hardly any research conducted on the M&A activity of the Japanese mega-banks. Consequently, as the 13 mega banks merged to form only 4 mega-banks and 1 super-regional bank, it is hard to conduct quantitative research on the mega-banks.

It is important, while conducting the research that one recognizes the fact that qualitative data can be interpreted in a number of different ways. Therefore, one needs to make careful consideration as how the data is collected and interpreted (Creswell, 2007).

5.2 Research Design

Research design is a roadmap for conducting the research. This research is an empirical investigation based on primary data collected through interviews and secondary data collected through various sources. The period under examination is from 1990s up until 2008, when Japanese city banks were facing financial difficulties and engaging in a very active race to enter the M&A market to form one of the largest Japanese mega-banks. This is a unique case in time as Japanese banks do not have a strong history of opting for restructuring processes i.e. M&As since the post world war II period. Therefore, it will be interesting to examine such an activity and make credible analysis as to what actually transpired in the Japanese financial system, and therefore, a qualitative study may do justice to this research.

5.2.1 Unit of Analysis

The unit of analysis considered for this activity is the Japanese mega-banks (both combining banks and mega-banks) as the decisions about samples, both sample size and sampling strategies, depend on prior decisions about the unit of analysis to study (Tellis, 1997). This means that the primary focus of data collection will be on what is happening to combining banks in a setting and how they are affected by the setting.

5.2.2 Case Study

This research adopts a case-study style (Yin, 1994). More specifically, this paper conducts case study investigation related with the motives for the Japanese mega-banks to engage in the M&A process, strategic relatedness among combining banks, and resources influencing competitive advantage for the Japanese mega-banks in Japan.

Eisenhardt (1989) noted that the case study method uses multiple sources of information for data collection. Yin (1994) states that 'a case study from a research strategy point of view may be defined as an empirical inquiry that investigates a contemporary phenomenon within its real life context, when the boundaries between phenomenon and the context are not clearly evident, and in which multiple sources of evidence are used. It is particularly valuable in answering who, why and how questions in the management and businesses research.'

The case study allows the investigator to concentrate on specific instances in an attempt to identify detailed interactive processes which may be crucial, but which are transparent to the large-scale survey. Thus, it is the aim of the case study to provide a multi-dimensional picture of the situation. It can illustrate relationships, corporate political issues and patterns of influence in particular contexts.

This fits in well with the investigation on the Japanese mega-banks M&As as it will elaborate on the environment in which M&As took place in Japan and what implications the consolidation process has had on the revival of the banking sector in

Japan. By understanding the Japanese M&A strategy, this research may help other analysts in Japan to understand the strengths and weakness of the M&A activity taken place with the mega-banks and seek knowledge for future M&A activity in Japan.

With the research at hand, on Japanese bank M&As, in empirical terms little is known about what were the drivers, that lead the banks to engage in such a restructuring strategy. Therefore, to understand and gain an in-depth perspective into these questions, the case study methodology is employed at its best.

5.2.3 Multiple Case Studies

This study uses the ‘comparative case study’ or ‘multiple-case study’ approach, where a number of cases are studied to compare the phenomenon across different cases in a systematic way and explore the different dimensions of the research issues. The findings from multiple-case studies can be more robust than those from single-case studies (Eisenhardt, 1991). Multiple-case study sampling adds confidence of the findings and thereby ensures precision, validity and stability (Miles & Huberman, 1994).

The banks analysis will be presented in multiple case study style. There are four case studies presented through this research, while discussing five mega-bank M&As. This is because when Banks E, F and G combined they formed two mega-banks. The case studies are split in the following manner; i) introduction to the banks; ii) planning stage; iii) the motivations behind each bank M&A; iv) strategic relatedness; v) resources; and vi) strategic benefits of the specific M&A. This will be followed by a cross-case comparison of the five mega-bank M&As along with discussion based on the extent literature while adapting the theoretical model and identifying the salient features responsible for value addition in Japanese banks. Tables and figures are created to display the data from individual cases. This will allow the research to develop naturalistic generalizations from analyzing the data, generalizations that people can learn from the case either for themselves or to apply to another case (Creswell, 2007; pp. 163).

5.2.4 Exploratory and Descriptive Research

This thesis is based on exploratory and descriptive research. Case study can be conducted in three kinds; i) exploratory; ii) explanatory and iii) descriptive. Exploratory research deals with questions like “what”, how much or how many, line of inquiry. As discussed by Yin (1994) exploratory research dwells on discovering and exploring what is happening in the environment, to gain an insight, understand a concept and its fundamental basis and how it has evolved and interacts with its surroundings. Furthermore, as discussed by Yin (1994) explanatory research can be used for casual settings. This research is based on exploratory and descriptive methods.

5.3 Data Collection

This section is divided into two parts; i) the method for data collection i.e. triangulation approach; and ii) the types of data collected.

5.3.1 Triangulation Approach

While conducting research scholars often utilize various mix of data collection in order to enhance the quality of the research. One such phenomenon is the triangulation approach which may provide the right balance and mix of information by combining different forms of information in different setting but aiding towards answering the same questions. Tellis (1997, pp. 5) mentions that ‘Not all sources are essential in every case study, but the importance of multiple sources of data to the reliability of the study is well established.’ Yin (1994) highlights six sources: documentation, archival records, interviews, direct observation, participant observation, and physical artefacts.

Denzin (1978, pp. 247) has identified four basic types of triangulation approaches namely; i) data triangulation – the use of variety of data sources in a study; ii) investigator triangulation – the use of several different researchers or evaluators; iii) theory triangulation – The use of multiple perspectives to interpret a single set of data;

and iv) methodological triangulation – use of multiple methods to study a single program or problems.

For the purpose of this research, data triangulation approach suits best, as it will provide in-depth insights on the M&As of the five Japanese banks by using different sources of information i.e. both primary and secondary sources of information as described in the subsequent sections. This approach will also provide credibility to the findings as little qualitative data exists of the M&A motives, strategies and resource competitiveness of five banks in Japan.

5.3.2 Data Collection

According to Creswell (2007) data collection can be defined as a ‘series of interacted activities aimed at gathering good information to answer emerging questions.’ Data collection can be conducted in a number of different ways, however, for the purpose of this study, two broad categories are defined; namely; i) primary data collection through interviews; and ii) secondary data collection through archival resources, databases and annual reports. To collect the data a data collection circle is identified which includes; i) locating site and individuals; ii) gaining access and making rapport; iii) sampling; iv) collecting data; v) recording information; vi) resolving field issues; vii) storing data (Creswell, 2007, pp.118).

- **Primary Data**

Primary data has been collected through eight interviews, with Japanese banks’ senior management (Managing Director and Senior Vice-President level in the range of 10 to 25 years of experience in the financial sector) and banking analysts from credit rating and research institutions in Tokyo, Japan during the week of the 14th to 23rd October, 2008. Some discussions took place with banking analysts in Japan in 2006 from which data was also utilized. In general, everyone interviewed and or discussed this research with had more than 10 years of experience in the Japanese banking system. About 60 to 100 financial institutions were contacted in Japan, including, Japanese mega-banks, Japanese securities firms’, Japanese financial and research institutions, Japanese

libraries, Japanese banks association and the chamber of commerce, Japanese *Keidenren*, Japanese media, foreign banks in Japan, foreign investment houses in Japan, foreign media, and foreign research and credit rating firms. A number of organizations were contacted with the aim to capture different viewpoints on the M&A activity-taking place in Japan including both Japanese and foreign experts.

Five banks are under consideration that were born out of the Japanese mega-bank M&As. Bank names will not be mentioned in the case studies but an alternative mode of identification based on alphabets and numbers is chosen. Bank 1 to 5 are the names of the banks that resulted from the M&As under consideration for this research. Banks A to I are the name assigned to the combining banks.

Based on the qualitative nature of this research with a case study approach interviews seem the best approach as interviews extent the possibility of “verified in-depth exchange between researcher and research at hand’ (Barbour, 2003, pp.113). Barbour (2008) maintains that interviews are often cited as “gold standards” of qualitative research.

The findings of this research will extrapolate in-depth views as ‘interviews yield direct quotations from people about their experiences, opinions, feelings and knowledge on the subject’ (Barbour, 2003). Therefore, by interviewing Japanese mega-banks management and other banking analysts in Japan who have been involved in the M&A activity or monitoring the M&As in Japan have provided insights to what transpired during the M&A activity. This is usually referred to as the snowball or chain sampling approach, by identifying ‘information rich key informants or critical cases’. Semi-structured interviews were conducted as it allows the interviews to capture elicited data on perspectives salient to respondents rather than the researcher dictating the direction of the encounter, as would be the case with more structured approaches.

- ***Human Ethics Committee Approval***

Human Ethics Committee (HEC) approval from the Victoria University of Wellington, Wellington, New Zealand was obtained for conducting the interviews in Tokyo, Japan.

The interview questions along with the purpose of the study were formally sent for approval to the University. Please refer to appendix 5 to 10 for the relevant documents.

- ***Recruitment of Interviewees***

The phenomenon of purposeful sampling is used in qualitative research, suggesting that the researchers select individuals and sites for study because they can infer an understanding into the research problem. Decisions need to be made about who or what should be sampled and how many people or sites need to be sampled.

After receiving the HEC approval, a list of participants to be interviewed was selected after identifying them via organizational charts and by reviewing secondary information obtained via annual reports between 1999 to 2008 and websites, various key departments handling the M&A activity were identified, after which a number of individuals were identified who most suited the profile of being completely or partly engaged in the M&A activity. Initial contact was made via telephone, email or fax in introducing briefly the research scope and requesting for an interview. Scholars maintain that often, while conducting qualitative studies, the researcher faces the problem of gaining access to the organization, identifying the right people involved with the relevant information on the topic under investigation and convincing and building a rapport for individuals to participate in the research (Creswell, 2007). With the Japanese banking system, being a conservation system and highly sensitive area due to the nature of the banking industry and M&A activity, initially it took about 3 to 6 months to establish rapport with the banks and other financial institutions to convince them to participate in this research and make time for the interview. Finally, individuals from within the banks and other financial institutions were selected and interviewed for the research, in order to capture the relevant and true information on the investigation questions. The ethical forms along with the interview questions were sent to the interviewee beforehand in order to introduce them to the research. During the interview consent was requested for the confidentiality of the interviewees name and bank name.

- ***Recording the Interview and Data Storage***

While conducting the interviews with the consent of the interviewee, some of the interview sessions were tape recorded. Simultaneously, notes were taken during the interview. The data was stored in computer with back-up copies and a list of types of information gathered was developed.

- ***Transcription***

The interviews recorded were transcribed to analyze the data collected. The transcription stage appears between the data collection and data analysis stage, whereby it produces scientific knowledge as it captures and freezes in time the spoken discourse that is of interest to the researcher. Edwards and Lampert (1993) as highlighted in Creswell (2007) identify two benefits of transcription, namely; authenticity (the need to preserve the information in a manner that is true to the original interaction) and practicality (the need to respect the ways in which the data are to be managed and analyzed, for example the transcripts are easy to read).

- ***Secondary Data***

Secondary data is collected from professional and academic journals, bank and financial institutions' web-sites and databases, and print media (from various libraries, archival information, bank reports and other documents).

The identification of sources was based on a systematic bibliographic search, using both manual and web-based methods. While the former was more efficient in tracing reference in books, manuals, annual reports, conference proceedings: the latter was appropriate and more suitable for scanning academic and professional journals and various country and company websites. The computerized literature search combined the following databases: Proquest, which provides information on banking and M&A articles published since early 1970s; JSTOR and Science Wiley which also provide

information on similar topics; and Factiva, which provides current information on banks, including statistics such as current market value share. Quick searches were also conducted on the Victoria University's International Business resources internet site and Google scholar and Bloomberg Database facilities in Tokyo, including both international and Japanese new services i.e Nikkei Net, covering the Japanese banking sector from 1997 to 2006 were used. In total, about 250 articles have been examined, of which 125 are empirical studies are, 125 are conceptual articles. All these sources have been used for the literature review, the results and implications sections. It took a total of 6 months to identify, collect and analyze the data. Another source was by visiting libraries in Tokyo, namely; Diet Library, JETRO Library, Zenginkyo Library, and Foreign Correspondent's Club Library.

Data collection primarily included analyzing articles and breaking down the literature into the themes that allude to the M&A and Japanese banking theory. A theoretical model is then presented, to be adapted and presented based on the data collected and analyzed on the Japanese banks behaviour.

5.3.3 Linkages between the two sources of data collection

The data collected both through primary (interviews) and secondary sources (different print and archival sources) present us with the opportunity to understand the complete picture of what substantiated a change for the long term legacy Japanese banks to adopt a restructuring strategy i.e. M&As, what was the background of each bank, how did the planning stage take place, what kinds of strategic and resource relatedness and competitive advantage crop up as a result of the partner banks combining and what kinds of strategic benefits did this M&A activity have on the Japanese banking and financial system and Japanese economy as a whole. To answer all these questions interviews provided with the facts on what actually transpired within the banks and information that was not available through the print or archival data. Therefore, it can be safely said that the interviews answered the research questions and helped with the modification of the conceptual model for each bank. In providing insights the true ground reality as a true reflection of what kind of a competitive advantage and

organizational recovery was evident for each bank under examination. The secondary source of information provided insights into the Japanese financial crisis up until the M&As were initiated. It also fulfilled some gaps into the interviewees presentation of the facts, validated some of the interviewees and most interestingly in some place provided counter-arguments for what actually transpired in the Japanese financial sector. Hard facts about the banks, the type of M&A transaction mode of payment, credit rating and so on were also provided by the secondary sources. In some places the information complemented the interviews and where there were problems encountered during the M&A activity the interviewees information was further backed up with the help of the secondary information. The M&A activity took place between 1999 to 2003 except for one of the banks which started in 2005 and completed at the end of 2008. The interviews took place in October, 2008, therefore, the time gap between the actually activity and interviews is substantial and some information can be lost and forgotten by the interviewees therefore, the secondary data played a pivotal role in re-confirming and validating a lot of the interviews.

5.4 Data Analysis

Data analysis is a means of categorized data collected so that it can be presented in a logical manner in the results section. Scholars have identified three key analytical strategies: coding, memoing and integrative diagrams (Creswell, 2007). For this research all these strategies have been employed.

Huberman and Miles (1994) provide more detailed steps in the process such as writing managerial notes, drafting summaries of field-notes, and noting relationships among the categories. The data analysis stage encompasses 'analytical circles' rather than using a fixed linear approach. Basically, there are four stages during the data analysis stages as described below: i) data managing stage; ii) reading and memoing stage; iii) themes and dimensions are identified in order to develop some classification and interpretation to the system; iv) a spiral package that displays the results in form of themes, matrixes, and other kinds of empirical and or conceptual evaluations can be presented.

Coding is a process for both categorizing qualitative data and for describing the implications and details of these categories. Initially one does coding, considering the data in minute detail while developing some initial categories. Later, one moves to more selective coding where one systematically codes with respect to a core concept.

Integrative diagrams and sessions are used to pull all of the detail together, to help make sense of the data with respect to the emerging theory. The diagrams can be in the form of graphics that is useful at that point in theory development. They might be concept maps or directed graphs or even simple cartoons that can act as summarizing devices. Huberman and Miles (1994) maintain that the process of data collection, data analysis and writing the thesis go hand in and hand and can be conducted at times simultaneously. After the findings are presented in case study style, a cross-case analysis is presented, summing up the key findings by advancing the various theoretical strands used in this thesis.

Chapter 6

Case Studies

These case-studies on the Japanese mega-bank M&As, in advancing the understanding on the M&A motives, strategic relatedness among the combining banks and resources providing a competitive advantage and organizational recovery for the banking sector in Japan. The combining banks are referred to in alphabetical order and new banks are identified based on numbers. The case-studies are placed in the order of the banks benefiting the most to the least in terms of competitive advantage.

6.1 Case-Study Bank 1 M&A

In 1999, both Bank A & B, decided to integrate and form bank 1, Japan's third largest bank with Yen 99,000 billion (US 1.37 trillion) in terms of asset size.

In June 2000, at the Annual General Meeting it was decided to launch bank 1 on April 1, 2001 and the consolidation process to be completed by April 2002. Bank A will be the surviving company and bank B will be the dissolving bank as shown in figure 6.1. Bank 1's headquarters' will be in Yurakucho, Chiyoda-ku, Tokyo. In the Kinki area, corporate functions will be housed both in the Osaka headquarters (the former Osaka head office of Bank A) and in the Kobe headquarters (the former Kansai headquarters of Bank B). In December 2002, a holding company, Bank 1 Financial Group was established.

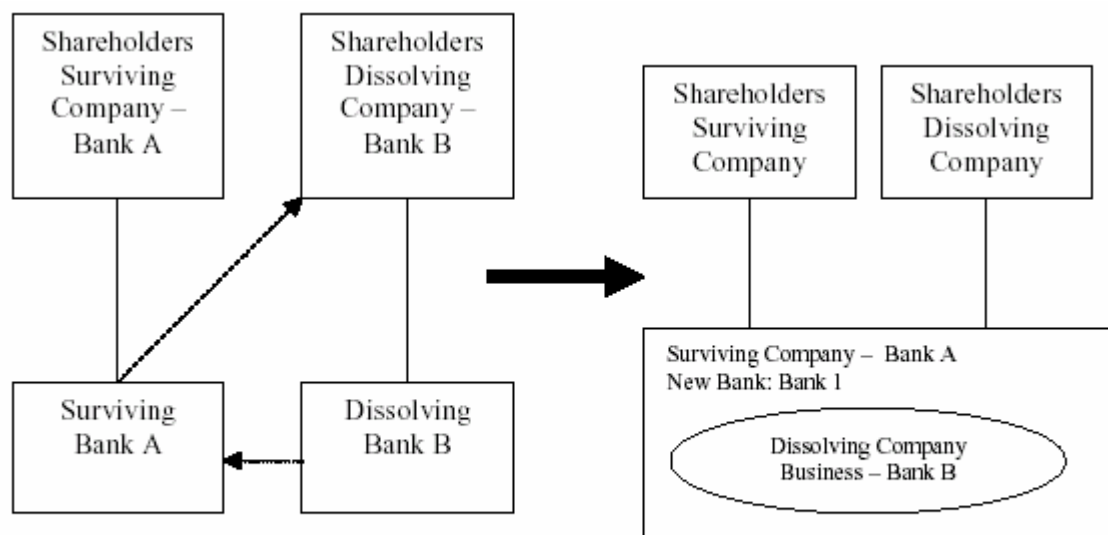


Figure: 6.1 M&A Structure - Bank 1

The merger was based on a merger ratio of 1 share of Bank B's common stock exchanged for 0.6 shares of Bank A's common stock, with a total capital stock of Yen 1,420,9 billion listed on the Tokyo stock Exchange, Osaka Stock Exchange and Nagoya Stock Exchange. JP Morgan was the advisor for Bank B and Goldman Sachs was the advisor for Bank A. Please refer to table 6.1 for a profile of Bank 1 at the time of its establishment.

Characteristics	April, 2001
Head Office	Tokyo
Amount of Capital	Yen 1,276.7 billion
Ordinary Shares	5,612 million
Number of Employees	26,000
Number of Manned Offices	578
Assets	Yen 113,451.3 billion
Consolidated Capital Ratio	10.8% (BIS Guidelines)
Deposit	Yen 59,041.3 billion
Loans & Bills Discounted	Yen 61,747.8 billion
Long term credit rating	(as of June 29 th , 2001)
Moody's	A3
S&P	BBB+

Table 6.1: Bank 1 Characteristics

6.1.1 Planning Stage

In 1999, there was a sudden announcement that Bank A could possibly anticipate a consolidation activity, amidst a series of banking crisis in Japan, especially behind the non-performing situation of banks. There were rumours for Bank A to merge with the Long Term Credit Bank and or Nippon Credit Bank, but it could not be determined who would be the new partner for Bank A. Bank A, to enter an M&A activity was posed with questions for immediate attention; who is the potential partner bank, what will be the new name of the combining banks, where will be the headquarters, who will be the president and chairman, legally which bank will be the surviving bank and which will cease to exist.

The planning stage for both Bank A and Bank B was managed by the senior management of both the banks, including decision making, allocating the task force teams, and determining the strategic fit between the specific partners. It is often suggested that the two major players in articulating the significant integration landscape for Bank 1 were President and CEO Bank A and B, who were good friends. It was therefore, decided from day one that Bank A would take the lead in the articulating this M&A. There was regular monitoring, even adhoc meetings three to four times per week on the performance of the merger by board members to resolve any issues. Some of the major considerations outlined by the management were; i) careful merger preparation and number one in terms of profitability and over-head ratio; ii) merger data; merger accounting to rid of Bank B's unrealized losses and reserved using 'merger surplus' without reducing retained earnings; iii) the first 100 days; revised internal target for further cost reduction for faster and larger merger benefit and group strategy, integration of major group companies; and iv) balance sheet management – asset quality and equity portfolio. President of Bank A mentioned that before the actual merger, the banks would take an unspecified stake in each other, forge alliances in all business areas and integrate computer systems that control deposits and lending (Shimogori, Oct 15, 1999).

The M&A consolidation was on schedule, however, with regards to overseas bank operations management had to decide on a country by country basis keeping in perspective each host country regulations. As an example Hong Kong monetary authority was keeping a close eye on Bank 1 activity and how closely the legal processes were followed.

The level of integration for the merger between Bank A and B is classified as vertical integration, aiming for scale and scope integration. As discussed by one of the banking analysts the idea was ‘scrap and build branch networks, close branches that are located in same areas.

6.1.2 Motivations for Consolidation

There are a number of reasons why Bank A and Bank B decided to take this M&A activity on board, such as; i) macro-economic; ii) industry-based; and iii) international level rationales.

- **Macro-economic level rational**

On a macro-economic level there seem to be two factors acting as catalysts;

- *Deregulation*

Bank 1 wanted to take advantage of the de-regulation process and become more competitive in the Japanese and overseas banking markets. The management wanted to take advantage of the change in the banking business climate stemming from the implementation of the financial big bang and other liberalization measures, and the globalization of the financial sector in Japan.

- ***Banking Crisis and NPLs***

It is widely acknowledged by banking analysts in Japan that, ‘after the Japanese financial crisis many Japanese mega-banks required a strong asset base that had diminished since the burst of the bubble. Therefore, it was imperative and a ‘natural time’ that banks go out and ‘seek partners’ as a profit source.’ Bank B was pressed to find a strong partner, given its fragile financial health and relatively high level of problem loans, estimated at Yen 1.8 trillion at the end of March, 1999 (Shimogori, 1999). The government assistance received by both the banks as of 1999 was about Yen 1501 billion. By improving the financial health of the banks it was perceived that the banks could re-pay the government.

- **Industry Banking Level Rational**

Bank 1’s composition may also be attributed to banking-level rationales as discussed below.

- ***Size Integration***

A bigger size in terms of assets is considered a ‘potent factor’ in the domestic and international banking community therefore, both Bank A and B decided to integrate to increase asset size. With increase in scale, Bank 1 wanted to create a Bank A brand taking advantage of IT investments, develop key infrastructure; such as delivery channels, skilled personnel and other management resources, including a competitive might of both the *keiretsu* groups, which marries the strengths of the Mitsui and Sumitomo brands that have been built over the years to mean reliable and innovative service.

- ***International Rational - Asian Currency Crisis***

Another factor aiding with the consolidation of Banks A and B is based on the Asian Currency Crisis which took place at the same time as the Japanese banking crisis. Japanese banks could not borrow money at LIBOR and had had to borrow at LIBOR plus 25 b.p. to 30 b.p. This made doing business overseas costly for which Japanese banks were required to sell overseas assets and down-size overseas operations. As a result, Japanese banks had to move towards cost-efficiency and adapt the banking system based on the changing financial landscape.

6.1.3 Strategic relatedness

Strategic relatedness between the combining banks was considered critical in deriving a competitive advantage in terms of markets and products and services, as discussed below.

- **Market Relatedness**

Bank A had its strengths in western Japan and Bank B had its strengths in eastern part of Japan, with its ‘economic anchor in Tokyo’, thereby, merging the banks provided some benefit in terms of synergy realization. Bank B was created through a previous M&A activity; therefore, was heavily concentrated not only in Tokyo and Kanto region, but also possessed roots in Kobe region. In addition, ‘for large corporate clients there is a minimal overlap as previously, Bank A clients were *keiretsu* A members and bank B’s major clients were from *keiretsu* B, giving the two banks more room for cross-selling. Therefore, the difference in the banks in terms of providing a regional coverage with a balanced nationwide clientele from Osaka to Tokyo has added to scale and scope economies increasing profitability for Bank1.

- **Products and Services Relatedness**

Bank A has expertise in capital markets and small and medium sized corporates. In fiscal year 1999, Bank A developed a number of strategic initiatives, i) Consumer Banking Group – a new branch terminal system (WIT), enhancement of telephone

banking and establishment of additional centres, Internet banking functions, customer information file system, and updating of ATMs; ii) Middle Market Banking Group – specialize in receiving income fund transfers (virtual branches) only; iii) International Banking Group - new international account system developed; iv) Treasury Group - systems for yen-denominated securities and money, currency dealing support system; v) Others Settlement Group - risk reduction system, credit risk management system, internet settlement service, on-line debit service, adaptation to the Japanese version of 401K developed; vi) e-business division developed to exploit the full potential of new banking technologies, including the electronic settlement of accounts. On the corporate side; i) for small and medium-sized customers, the bank launched a portal site named “NETdeBIZ to help them improve their sales activities; and ii) for larger corporate customers, the bank aims to provide e-banking services, such as electronic banking and account settlements. Meanwhile, for consumers, Bank A has established its own electronic debit service, with plans for launching smart cards and electronic money well advanced (annual report 1999, pp. 11-12).

Bank B, on the other side brings to the table housing loan product, a profitable product and expertise in virtual banking and other areas to provide strength to Bank A’s presence in this area. According to the UBS banking analyst (Tamura, 2005; pp. 54) ‘Bank B created a team of several hundred advisors for wealthy clients more than 10 years ago. It was also one of the first few banks to install ATMs at convenience stores and proved to be a leader in retail operations.’ Therefore, both banks before merging already had a strong retail clientele base.

6.1.4 Resources Combination

The following section discusses the *keiretsu*, organizational, and physical resources as being pertinent to Bank 1 in providing a competitive advantage.

- ***Keiretsu* Resources**

Bank B's President points that 'the alliance of the two banks will enjoy the country's most powerful client base (Shimogori, 1999). We cleared the hurdle of [traditional] corporate group structure in order to create the world's top-class financial firm.' By way of this consolidation, Bank 1 has a larger pool of client resources as the banks cater to the large corporate clients especially, linked with their *keiretsu* member's i.e Bank A Group and Bank B Group. Large corporates such as Sanyo and NEC, Nippon Glass, Sumitomo Chemical, Sumitomo Mining, and Sumitomo Rubber bank with Bank A and Toshiba and Sony, bank with Bank B. Group B supports Toyota Motors, Mitsukoshi Department Store, and Oji Paper; Group A has mining companies (Zielenziger, 1999).

The name of the new bank was decided to be based on their respective *keiretsu* names as combining the brand names would allow Bank 1 to take advantage of its their brand names, as discussed by banking analyst. Brand positioning of introducing and maintaining a high standard for Bank 1 brand was a challenge. But this was handled tactfully and a common brand strategy on a group basis was established.

Recof banking analyst, Mr. Ishikawa maintains 'Group A and B have a 300 year old history. Both groups are strong in manufacturing, car, retail sector and so on and have a large client base. Group B created big players as trading partners, and merged weaker companies. Both have a big influence in the corporate world and will be able to meet the diversified and specialized needs of the clients. Moreover, Brian Waterhouse (Shimogori, 1999) maintains that this tie-up would eventually create one of the largest

financial conglomerates that also include life and non-life insurers and trust banks both are *keiretsu* group A and B. Therefore, the new banking group would not only focus on consolidating corporate relationships but also drive into the lucrative retail sector.

- **Organizational Resources**

The organizational resources that influenced a competitive advantage for Bank 1 include i) knowledge; ii) managerial leadership; iii) cultural; iv) human; and v) legal resources.

- ***Knowledge Resources***

While combining the banks, bank management envisaged that some knowledge expertise was shared and transferred to Bank 1 from the previous M&A activity of Bank B's previous integration.

- ***Managerial Leadership Resources***

Bank 1 had maintained a strong leadership spearheading the M&A by CEO and President of Bank A. This allowed for a smooth integration as the employees of combining banks knew where the orders were coming from and who to consult in case they encounter any problems. Managerial synergies have been achieved through one man leadership. Moreover, both President and CEO of Bank A and B worked together in harnessing the consolidation process.

- ***Culture Resources***

A unique characteristic of this consolidation was the 'generation of a new corporate culture by Bank 1, diminishing the former bank cultures'. Banking analyst Shinichi Tamura (2005, pp. 56-57) describes this as a monoculture strategy, whereby Bank 1

chose the best method for each business unit at the time of the merger keeping in mind ‘customers come first’.

In the beginning, it was hard for Bank 1 to mix employees of branches. There was some resistance from Bank B employees as they were prone to hard work and a gentlemen business style whereas, Bank A staff was known for its aggressiveness, centred towards profitability. The bank ultimately unified the business procedure, earnings targets and personnel evaluation methods in order to reduce friction between the bank staff. It was hard to integrate the corporate cultures of both Bank A and B, especially, Bank B’s culture as it was more closed and conservative as compared to Bank A’s fast-paced culture. Finally, the cultures were fused and one performance system and one reporting line system were streamlined.

The banking language terms differed between the combining banks, so initially ‘there were some surprises when employees visited customers. Bank B language was ‘*homon*’ for visit whereas Bank A used ‘*oho*’ for visit. This was a regular concern therefore; the planning department introduced a glossary of terms.

- ***Human Resources***

HR matters were thoroughly discussed for Bank 1, for about a year based on concerns like who will head which department, branch, what are the terms for reward levels, beneficiary and fringe benefits, how many days for vacation and so on.

With the formation of Bank 1, UBS banking analyst maintains that some 6000 jobs were cut down from 2001 to 2005, reducing from about 26,000 to 20,000. Under the Japanese employment system there is no lay-off system, therefore, some employees were transferred to other affiliated companies of Bank A and B *keiretsu* groups and some opted for voluntary retirement plan, as they were concerned that under the present fifteen year recession period (at the time), the long-term system maynot be sustained for long. New resources such as new staff members were hired from outside, both at a

graduate level as well as professional and senior level in order to enhance the capabilities of Bank 1.

Bank 1 placed staff based on their capabilities, placing the right person for the right job, dis-regarding which bank they came from. In terms of compensation there was a decline for Bank 1 employees based on the longstanding recessionary period of Japan. Bank B employees were not satisfied with this as they had to incur a reduction in their salaries.

- ***Legal resources***

Legal consultants were hired to organize the intensive review of legal documents for the consolidation process, including the notice to customers and stakeholders to succeed the obligation and rights of the consolidation.

- **Physical Resources**

The physical resources prominent in Bank 1 are i) IT systems; and ii) branches.

- ***IT Systems Integration***

Information Technology systems were considered as one of the major resources that played a pivotal role in the smooth and efficient integration for Bank 1 IT systems. Banking analysts at Bank 1 maintain that for domestic operations NEC systems, mainframe systems using a common branch teller system were employed which were previously used by Bank A. Overseas operations in US and Europe made use of former Bank A system's and in Asia and Pacific region Bank B, IBM systems were used. However, this was an extremely time consuming and costly exercise. The problem was that Japanese banks used obsolete IT systems. As one of the bank analysts explains that the 'Japanese IT system is focused on main frame structure or transaction processing system not a diversified system, which is a time consuming affair in terms of

integration.’ IT related strategic investments during and after the consolidation process were estimated to be about Yen 100 billion annually.

Banking analysts maintain that emphasis was also placed on channel systems. Bank B’s delivery channels such as convenience stores, ATMs and the Internet Bank were used as a basis to form other compatible channels. Additional, information sharing systems, risk management systems and database networks were developed for diversification in products and services. Moreover, the bank engaged in alliances with IT specialists for development of contents, networks and client base features, internet banking, international securities and financial portal. Banking analysts maintain that on a technical basis ‘we had to choose the best combination for the new bank.’ Slogan was ‘best practice,’ however; it was not easy to determine which is better than the other. How to integrate customer information was a big question to be addressed. One bank database was fine as it was already in the database but matching the information and consolidating it with the other bank information was a tedious task. Consequently, if Bank B customers had availed a loan facility, it had to be re-paid to bank 1 i.e Bank A customers. Therefore, streamlining these concerns required detailed attention.

- ***Branch Network***

Branches for both bank A and B numbered about 300 each. The size reduction was about 30% by 2002 and by March 2003 the total number of branches was reduced to about 400. As a total number, management reduced about 108 duplicate branches between March 2001 and March 2004, in total some 151 branches were to be shut down in Japan and some 32 branches in the overseas market (Whymant, 1999). The branches that were considered duplicate or redundant were not closed down immediately as the management ‘did not want to hurt the feelings of the customers,’ therefore; they declined gradually over a period of time once clients adjusted to Bank 1. One by one, the bank decided on who will be the new GM, which office building will be retained based on the lease and rental agreements and the landscape and position of the bank branches. Financial Synergy in terms of cost savings for Bank 1 for fiscal year 2001

was about yen 30 billion and for fiscal year 2002, some yen 20.1 billion expenses were reduced with a total banking profit of about yen 100 billion from 2001 to 2005.

6.1.5 Strategic Benefits

By way of choosing specific partners i.e. Banks A and B integration, the model presented in chapter 4 is tested, amended based on this case study and presented in figure 6.2, which is applicable in deriving a competitive advantage based on the M&A motives and strategies adopted by Bank 1.

Long term strategy for Bank 1 dwelled on growth opportunities and to adapt to the new bank structure by reducing the branch network; corporate wide business process re-engineering and reduction of non-marketing staff by restructuring of headquarters operations. In 2003, Bank 1 FG was developed. In 2003 March, Bank 1 acquired a regional A. In June 2008, Bank 1 purchased a 2% voting right stake in Barclays PLC and in future is considering registering on the New York Stock Exchange.

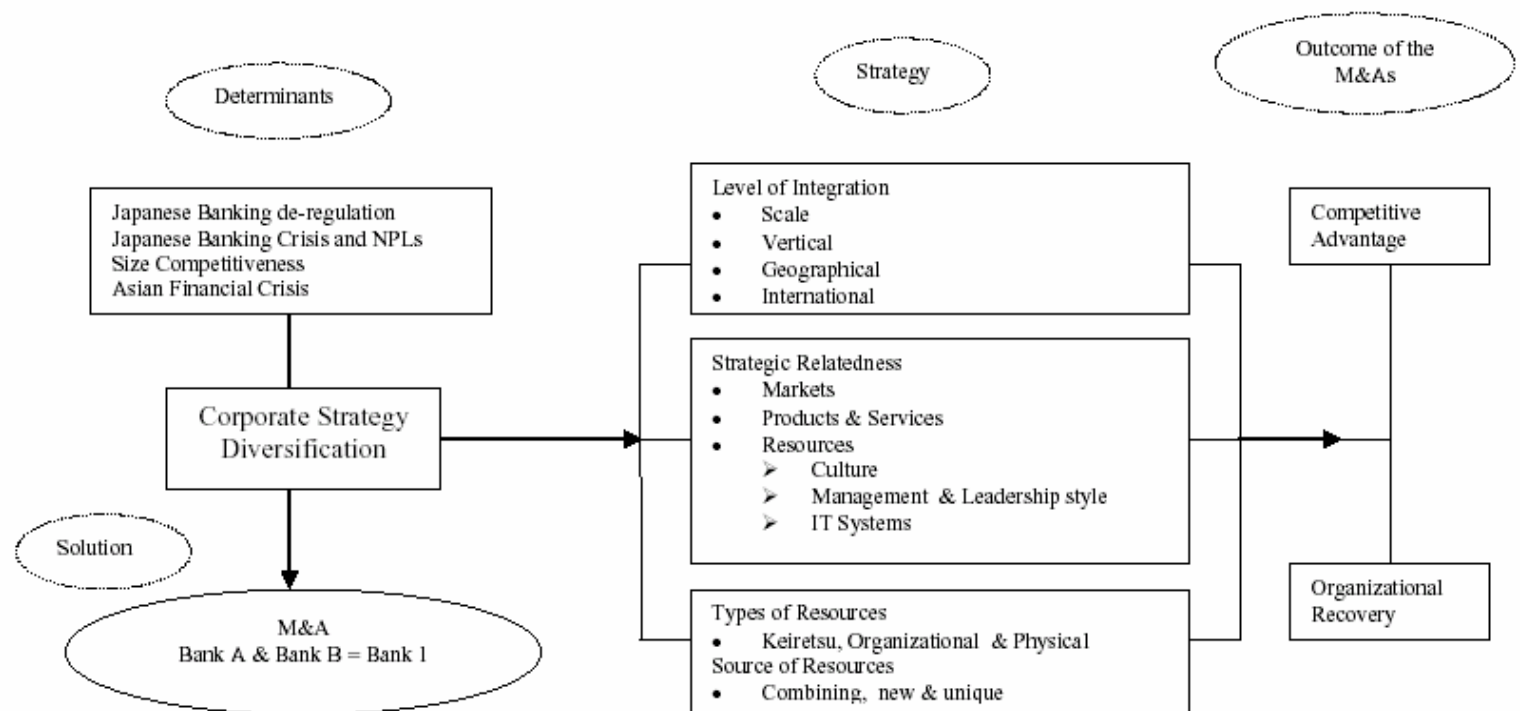


Figure: 6.2 Bank 1 Conceptual Model

6.2 Case-study Bank 2 M&A

On January 1, 2006 Bank C and Bank D integrated to form Bank 2, headquartered in Marunouchi, Chiyoda-ku, Tokyo with total assets of Yen 162, 714.1 billion as of September 30, 2005. Bank 2 formation was scheduled for 1st October, 2005, however later the date was shifted to 1st January, 2006 in order to ensure proper systems integration. Bank 2 was considered second in terms of assets at time of its inception, Bank C was second and Bank D was fourth in Japan among the mega-banks.

The merger ratio was based on 0.62 Bank C shares for one bank D shares. Bank C will be the surviving company and Bank D will be the dissolving company. The bank is listed on the Tokyo, Osaka and Nagoya Stock Exchange and overseas on the stock exchange of New York and London. Please refer to table 6.3 for a profile of Bank 1 at the time of its establishment.

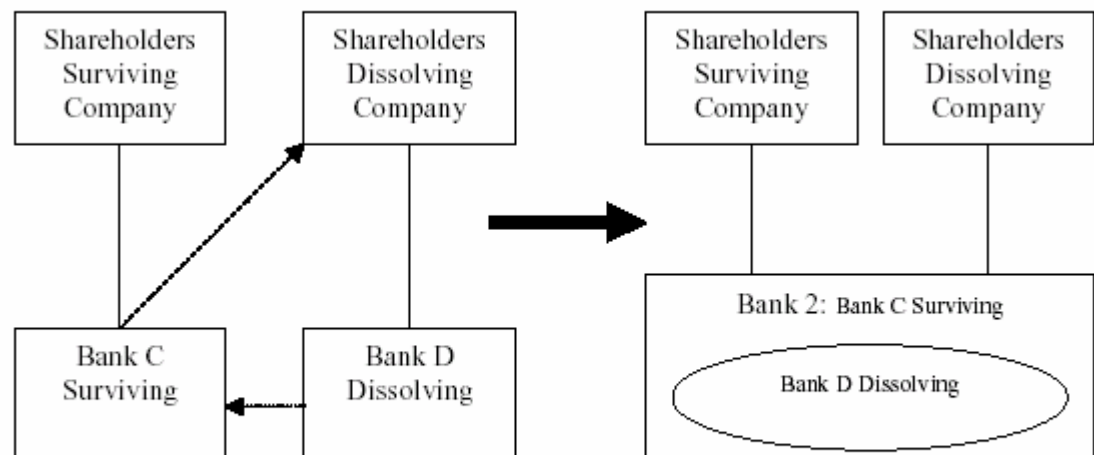


Figure: 6.3 M&A Structure - Bank 2

Characteristics	September 2005
Head Office	Tokyo
Amount of Capital	Yen 996.9 billion
Number of Employees	19,694
Branches	350
Assets	Yen 162, 714.1 billion
Consolidated Capital Ratio	12.48 % (BIS Guidelines)
Deposit	Yen 106,667 billion
Loans & Bills Discounted	Yen 75,293.1 billion
Long term credit rating	March 2006
Moodys	A1
S&P	A

Table 6.2 Bank 2 Characteristics

Bank C Financial Group, Inc. and Bank D Holdings, Inc. to form Bank 2 FG, with Bank C FG as the surviving company and Bank D Holding as the dissolving company. Bank 2 FG is a comprehensive financial group comprising top class credit card, consumer finance, investment trust and leasing companies, and a US bank (UBOC) as well as a commercial bank, securities company and trust bank.

6.2.1 Planning Stage

Banking analysts in Japan, maintain that it was hard to identify which bank takes the initiative to integrate as officially Bank C did not acquire Bank D but practically, it was an acquisition. A bank integration committee was set-up and the president of Bank C was the committee chairman and the president of Bank D was the deputy chairman. Management was meeting on a daily basis and discussed about 10,000 items every week with regards to the integration. Weekly and monthly plans were scheduled, segmented systematically in the form of charts and time frames; alongside mapping out who is involved with what. Staff members from both the combining banks were chosen, to form integration teams, as well as M&A consultants were hired to undertake the planning and consolidating stages. A number of contingency plans were set-up for various scenarios and how to improve and or overcome these arising situations. Questions like what products and services and divisions to keep were addressed by management? The teams decided which service satisfied customers and how was this cost-effective for Bank 2 to retain? Another means of deciding on the business unit was

through a sampling survey that was conducted once a year by a marketing company depending on the nature of the products – short term or long term. Scorecards were used at business unit level not at a corporate level. Risk management was another concern based on Basel II accord as former banks were setup on how to monitor risk including third party involvement.

Bank 2 integration was based on vertical levels, with scale and scope integration. When the management decided to merger, the aim was to have one single bank ‘not to good to have two different systems – as long as we have decided to merge, in principle everything has to be one.’

6.2.2 Motivations for Consolidation

The following section will discuss why Banks C and D consolidated based on a i) macro-economic; ii) banking industry level; and iii) intra-banking level.

- **Macro-economic Rational**

On a macro-economic level, as discussed below, there seem to be two reasons acting as catalysts.

- ***Government Regulation***

The M&A activity in Japan is often cited as being conducted by the financial system for competitive reasons, as it was regulated by MoF. Therefore, sometimes the ‘Japanese bank M&As are annotated as not being real M&As.’ Moreover, government envisaged that the Japanese banking system was behind in terms of the conducting M&As as compared to other financial markets, therefore, enforced the M&As in Japan.

- ***Banking Crisis and NPLs***

Banking analysts also maintain that the M&A activity in Japan was not self-triggered as it was triggered due to the bad debts profile of banks. In bank D’s case, it had a bad debt to asset ratio of about 8% to 9% therefore, the management was under pressure to resolve the bad debt position in line with the BIS regulation as it was having a hard time to survive. If Bank D had not integrated with another bank, it would have gone bankrupt. On the other hand, in 2004, both Bank C and Bank A showed interest in

acquiring Bank D. Both banks were trying hard in aspiring to become one of the largest banks in Japan as well as making their *keiretsu* groups stronger in a short period of time. Finally, Bank C was given the clear signal to combine with Bank D as there was government pressure on Bank C to accept Bank D. Bank D also preferred to merge with Bank C as it had received a better offer from Bank C as compared to Bank A.

- **Industry Level Rational - Size Competitiveness**

Size competitiveness, triggered by banks to become the largest banks in terms of asset size was highlighted as an industry-banking rationale for Banks C and D to combine. Banking analysts at Bank 2 maintain that ‘no preparation or planning was conducted for a long time to change the banking landscape of Japan in terms of compatibility with other global banks. Therefore, banks followed each other in the race of becoming the largest in terms of asset size’. Bank D wanted to secure a bigger bank network and customer base. Furthermore, Bank D would not have to incur capital expenditure in strengthening the international market or deal with global issues such as money laundering as it would inherit bank C’s platform. Subsequently, bank C wanted to get stronger in retail business therefore was interested in bank D due to its strong retail business.

- **Intra-bank level Rational**

The intra-bank level reasons for banks C and D to combine were based on diversification measures as discussed below.

- ***Diversification - Profitability***

Bank D wanted to increase profitability, therefore, wanted to consolidate with Bank C. Bank C had many competitors with each one having their own strategy for integration but bank C wanted to choose a partner based on business segments, customers and core competitiveness. Strategically, both bank C and D could not have chosen better suitors, as any other bank combination would have resulted in duplication for both sides.

- ***Diversification - Customer Requirements***

Customer financial requirements are increasing and changing, therefore, with the combination of the two banks products and services, a more innovative range of products is developed, especially in terms of investment banking and securities services. As one of the banking analysts mentions this M&A can be characterized as ‘responding to customer needs.’

6.2.3 Strategic Relatedness

Strategic relatedness is an important facet in terms of providing a competitive advantage as it helps identify the complementarity of markets and products and services, providing an impetus for the combining banks to integrate.

- **Market Relatedness**

Bank D is deep rooted in Kansai area, around the western and middle part of Japan. Bank D which originated from previous bank M&A; based in western part of Japan, out of Osaka area and Nagoya area. On the other hand, Bank C takes roots from a previous merger which has a strong presence in Kanto region especially, around Tokyo area, with specialized international networks especially in foreign exchange business. Bank D focused on regional areas whereas Bank C focused on city areas.

Difference in scale of clients also possesses a strategic advantage for Bank 2 as Bank C has a diversified range of clients both in corporate and whole-sale business and international markets. Bank D, on the other hand, has strengths in retail banking with small and medium sized industry and individual clients. Bank C benefits accrued to a sizable bank growth in strengthening of retail business which Bank C lacked before which now stands at 400 million retail accounts larger than Bank 1 and Bank 3. This can also be attributed to the fact that one of Bank D’s previous combining banks was known as ‘people’s bank’ as it was involved in retail banking. Bank D benefits in terms of Bank C’s domestic and global bank operations and customer base. Bank 2 has three main markets, Tokyo, Osaka and Nagoya and also the international markets.

- **Products and Services Relatedness**

Bank D excelled in small and medium sized and housing loan products whereas Bank C was present in retail, corporate and overseas business, especially foreign exchange. Retail side of Bank C was deleted and Bank D retail side was taken over as it offered better services. Major difference was that Bank D was customer orientated by international standards, no other Japanese bank operated 7 days a week and providing 24 hours of ATM service. Bank D served clients, 24 hours, opening accounts, remittances and took other steps to help clients, offering friendly situation in serving clients. It was hard to deal with local customers, as banks had a huge position in the domestic market, with different needs, therefore, initially, till all the products and services were not combined, the bank had to make some adjustments.

6.2.4 Resources

Bank 2 takes advantage of the *keiretsu*, organizational and physical resources in order to gain a competitive advantage.

- ***Keiretsu* Resources**

The relationship of Bank 2 has strengthened as the *keiretsu* group can benefit from Bank D products and services such as access to small medium companies in Kansai and Nagoya region. Consequently, Bank 2 has facilitated group companies in changing their way of business since the bank now has a broader range of customers and therefore, stronger networks.

- **Organizational Resources**

The organizational resources that provide a competitive advantage for Bank 1 includes; i) knowledge; ii) cultural; and iii) human resources.

- ***Knowledge Resources***

Bank C's resources could be characterized in terms of 'experience' and 'knowledge' in terms of international business. Bank D has a large base of customers and know-how for providing business to SMEs. These two attributes coupled together provide a stronger base for knowledge and experience to be shared among employees of the bank. Bank D had merged in 2001, therefore, it didn't have much time to adjust its present merger or learn and contribute to the extent that it should have, when it merged with Bank C.

- ***Corporate Culture Resources***

Corporate cultures were different for both the combining banks. Bank C's background due to its affiliation with its *keiretsu* group was perceived to be 'elite' and 'luxurious' with an aristocratic and bureaucratic business culture. Bank D culture, on the other hand, was more aggressive, samurai-type and creative. This is primarily because they didn't have many clients and were always on the go, to look for more clients 'hunt for clients', as one of the banking analysts claims. The creation of Bank C and Bank D was targeted on how to utilize the big-machine, people never seen before was a challenge. Bank 2 compliance policy was based on Bank C policy which was carefully followed by its employees; therefore, a lot of adjustment was required by employees of Bank D as it had to maintain the brand name.

Bank 2 never formed a mono-culture. The culture for Bank 2 is a combination, therefore has a mix effect. Initially, the merger was a benefit therefore, there was easy adjustment.

On another level, one of the reasons, why Bank D employees were willing to combine with Bank C as compared to Bank 1 because Bank D and Bank 1 culture was closely associated with that of aggressiveness, business like and how to generate profits. Bank D people thought that after the merger, more people maybe laid off. In terms of competitive advantage, two different kinds of bank cultures generate a new culture, which is beneficial for merging banks.

- ***Human Resources***

Human resource allocation and shuffling of specialists were important factors of the integration between the two combining banks. Training was provided at a branch level in the operations and to back office staff. During the consolidation, many employees left the bank; they took early retirement or were shifted to Bank 2 Securities or seconded to the *keiretsu* companies. There was some loss of talented people from the banks. Salary scales were also adjusted for the two banks. Bank D increased the bonus and Bank C decreased the bonus, therefore there was some resistance among the employees.

- **Physical resources**

The physical resources prominent in Bank 1 are i) IT systems; and ii) branches.

- ***IT Systems Integration***

The idea of the merger was launched in summer of 2004 and its final main frame integration will be completed and standardized by December 2008. It took a long time for management to decide if main frame or open system should be used. Main frame is a huge system and expensive, not active, not agile and not flexible. Open system cheap and small not good enough. The bank had also learnt lessons from Bank 3 failure of systems, therefore, was being careful and numerous tests were conducted in order to avoid major disruptions. FSA also threw their reservation that Bank 2 network plans are insufficient due to a flawed merger timetable that could lead to systems breakdown and the integrated computer system maynot be able to handle the information-processing load after the merger.

Additionally, in terms of costs it is also costly as the costs are about USD 2 billion and sometimes additional costs are incurred. The integrated operations for deposits, withdrawals and loans will begin Oct 1st, 2005. The core commercial banks were to operate under two separate platforms operating in tandem until mid December 2008.

Bank D had already outsourced the IT division to a joint venture company to maintain the operations and got rid of 5000 people. Bank C has some political reasons due to which it was hard for them to outsource since their president was once part of the IT department, therefore, he did not want to outsource the IT integration. There are 40,000 employees and 15,000 are for IT systems integration to maintain the mainframe.

Two plans were adopted for the integration as discussed below;

- Two separate systems will be maintained, while overseas and market systems including fund settlement; will be integrated into Bank C's system.
- The new bank will sort customer transactions into both banks host systems using the front-end transfer method; a method by which transactions are sorted at the data-entry level, without connecting to both host systems.

For final integration due in December 2008, it will adopt the following measures based on a reliable system developed on mutual compatibility of component of systems:

- Bank C's system will be adopted for basic system, including OS. Bank 2 will incorporate Bank D's positive attributes, which features year-round 24 hour ATM, account transfer system and telephone banking system.
- Relationships will be maintained with IBM and Hitachi groups which are technology vendors for Bank C and Bank D respectively.

- ***Branches***

Initially, it was decided to combine international operations into one unit based on former Bank C units as it had bigger operations overseas and therefore, it will be easier to integrate the branches overseas. For domestic operations, the branches were combined based on their relevance and convenience for customers, and cost-effectiveness. There were a total number of 900 branches now there are 294 domestic branches & 47 overseas branches. A bridge system was developed for bank C and D to portray as one bank for customers. Back-office operations remained separately till systems integration is completed by the end of 2008. Domestic concerns were to settle

various parts of business services such as ATMs, internet and so on, so customers can benefit. The deciding factor for which branch, combining bank takes the company is dependent on the type of client, asset size of the client, profitability level, loans and so on.

6.2.5 Strategic Benefits

At present it is too early to say what the benefits from the M&A will be as systems integration is due to complete by December 2008. By way of choosing specific partners i.e. Bank C and D integration, the model presented in chapter 4 is tested, amended based on this case study and presented in figure 6.4, which is applicable in deriving a competitive advantage based on the M&A motives and strategies adopted by Bank 2.

Bank President maintains that Bank 2 has to be among the top 5 global competitive banks, 'We can cut costs by reducing employees, closing the branches, sometimes branches are located closely, - close one already in process' (2005).

The major competitive advantages as cited by the bank management was to signify Japan's pre-eminent global network and presence in the global business village; provide a strong business foundation based on retail deposits and strong customer base with a strong financial and capital foundation; highly complementary business and networks and strong corporate governance and transparent management appropriate for NYSE listed companies and can make cross-border strategic investments i.e. recently MUFG has purchased a 20% stake amounting to USD 9 billion in Morgan Stanley.

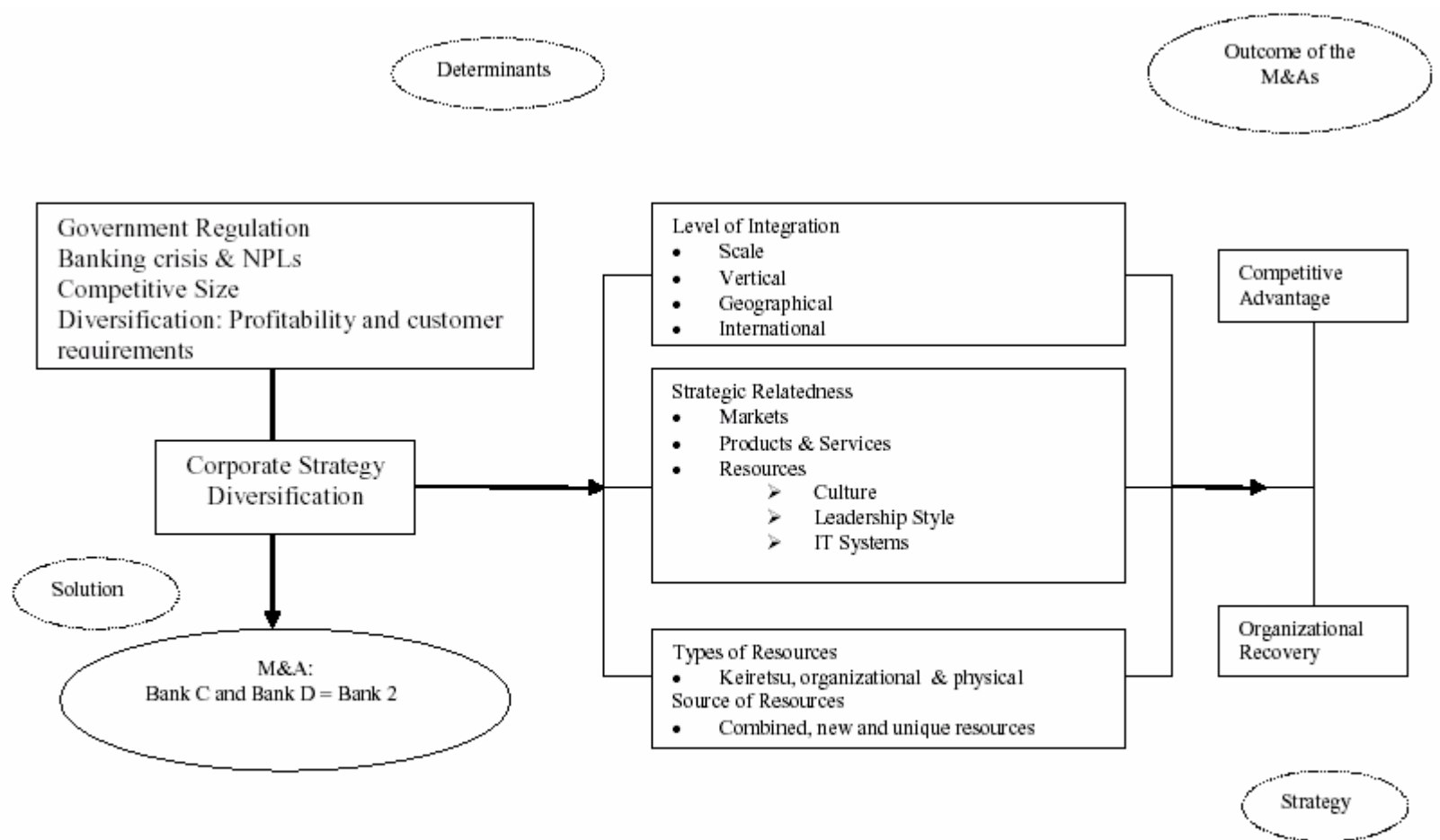


Figure: 6.4 Bank 2 Conceptual Model

6.3 Case-study Banks 3 and 4 M&As

Bank 3 and Bank 4 were born on the 1st of April, 2002, out of a three-way merger among Japanese legacy banks, Bank E, F, and G. It was the largest bank in the world in terms of an asset size of USD 1.3 trillion at the time of the merger. It's headquarters is located in the Uchisaiwaicho district of Chiyoda ward, Tokyo, near the imperial palace, former Bank E headquarters. The building that is currently, Bank F head office was chosen to be the new location for Bank 4 and the Bank E headquarters at the time was chosen to be Bank 3. The headquarters for Holding group will be set-up at Bank G's current head office. It was listed on the Tokyo, Osaka and Nagoya stock exchange. In November, 2006 it was also listed on the New York Stock Exchange. Figure 6.5 shows the formation of banks 3 and 4.

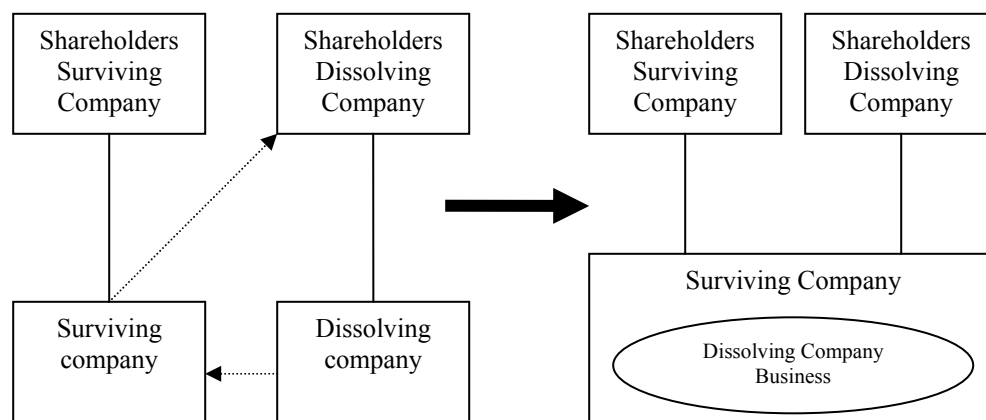


Figure: 6.5 M&A Structure - Bank 3 and 4

On August 20, 1999, the three banks announced their agreement on the comprehensive consolidation of the 3 banks with a formal agreement signed on December, 22, 1999. During the June 2000, ordinary general meeting of shareholder, the three banks obtained the approval for the parent companies into the formation of Financial Group.

The combining banks has bad debts amounting to USD 45 billion (yen 5.5 trillion); and 1998 losses of USD 8.5 billion.

Bank 3 and 4 Holding Group was approved through the stock for stock exchange method (*kabushiki-iten*) method. Under this method, one common share and one preferred share (par value Yen 50,000) in the holding company will be allocated for each 1000 common shares (par value Yen 50) of each of the three banks. The strategy was split in two phases; Phase 1; the period after the establishment of the holding company, the business of three banks will be conducted on an integrated basis through business unit structures. In phase 2, from Spring 2002, the business unit operations of the three banks will be reorganized according to business lines and customer segments subject to the expected legislative and tax code changes for corporate split in Japan. Financial Group; has split its banking operations in two separate subsidiaries; Bank 3 looks after the bigger, blue chip companies and essentially it's a whole-sale bank. Bank E's corporate and investment banking division was transferred to Bank 3 and retail banking division to Bank 4.

Characteristics	March, 2001
Head Office	Tokyo
Amount of Capital	billion
Number of Employees	35,000
Branches	740
Assets	Yen 113,451.3 billion
Consolidated Capital Ratio	10.8% (BIS Guidelines)
Deposit	Yen 59,041.3 billion
Loans & Bills Discounted	Yen 61,747.8 billion

Table 6.3 Bank 3 Characteristics

6.3.1 Planning Stage

A planning department responsible for streamlining the merger process and handling operations was set-up within the holding company and representatives from the three combining banks were appointed for each area. Merrill Lynch was hired as a consultant for planning stage. The planning stage process was managed properly however; the

integration of Bank 3 and 4 computer systems was a problem. It took a long time to recover from this activity.

Vertical integration was achieved through this M&A consolidation process. Bank operations and functions were kept separate, although, ultimately they were combined together in one unified banking operation and function.

6.3.2 Motivations for Consolidation

There are a number of reasons why Bank E, F and G decided to go ahead with this M&A.

- **Macro-economic Rational**

On a macro-economic level the M&A activity for Bank 3 and 4 was based on the following reason:

- *Government Solution to the banking crisis*

With the banks carrying large NPLs, the Ministry of Finance was actively engaging in restructuring by encouraging M&As among the Japanese banks to increase their capital base and provide healthier balance sheets. More than yen 10 billion was injected into the three bank by the government, which the banks had to re-pay. At the time the asset debt ratio stood at about 5% (1999-2000) which now has decreased to around 1.2% (2007-2008). Consequently, against a backdrop of problems associated with the three banks M&A was the best solution; ‘Bank E was tainted by scandals over pay-offs to racketeers, Bank F lost USD 3.5 billion in 1998, after making heavy write-offs to a number of owned bankrupt affiliates by the Fuyo *keiretsu* to which it belongs and Bank G the soundest, had lost government guarantees on five year bonds it uses to finance itself (banking analyst).’

- **Industry level factors**

Banking industry level factors also provided an impetus for the banks to consolidate as discussed below.

- *Over-crowding in Japanese Banking Sector*

In 1990s, there was over-banking in Japan with nearly 10 banks, 3 LTCBs, and more than 100 regional banks. Now after the M&A activity only 3 mega banks have emerged and a restructuring program is in the pipelines for the other banks.

- *Size Competitiveness*

The three banks, wanted to rank number 1 in terms of assets, therefore entered the M&A activity. Bank G's president said 'We feel endowed with a mission to become the frontrunner of banks here, so that we will be able to help Japan's financial sector regenerate.' Sometimes the banks would sign deals just to be in the top leagues, forging the 'profitability' sign.

- **Intra-bank Rational – Diversification**

The intra-bank rational for the three banks to combine was based on the diversification benefit of utilizing the present resources among the combining banks, thereby cutting costs, and offering a diversified range of products and services. Bank 3 and 4 also wanted to create a new corporate culture and climate by offering attractive compensation and opportunities for its employees. These benefits would pave the way for Bank 3 and 4 to become competitive in the Japanese and overseas markets.

6.3.3 Strategic Relatedness

In deriving a competitive advantage among the combining banks; market relatedness and products and services relatedness demands merit.

- **Market Relatedness**

Bank E had a strong presence in Kanto, Tokai, Kansai and Kyushu areas. Bank F had operations primarily in Tokyo, Osaka, Yokohama and Kobe areas. Bank G had operations in few but selected industrial regions i.e. Tokyo, Nagoya, Shizuoka, Fukuoka, Nigata, Osaka, Kobe, Kyoto and Hiroshima. Bank 3 is placed in Tokyo and Kansai area. Bank 4 also has a diversified domestic network covering every prefecture and urban area in Japan.

- **Products and Services Relatedness**

Bank E and F were money centre banks and both had strengths in retail banking (individual and small medium sized corporations) with some share of corporate banking. Bank E is a retail bank with a strong branch network. Bank G on the other hand provided long term financing to the industrial sector with major focus on loans, debentures and other investment banking and foreign exchange products.

Bank 3 draws its strength from the breadth of its coverage of transactions with large corporates (2/3 of Japan's listed companies); mainly accounts for about 70% of loans to large corporates and their subsidiaries; 30% to small medium sizes companies and about 20% to overseas institutions. It will provide products and services as; investment banking products; loan syndication; derivatives; support for IPOS, business information support and overseas business support. It has about 10,000 large corporate clients;

1,100 financial institution customers; 300 national governmental clients and about 4500 non-Japanese corporate clients.

Bank 4 covers transactions with individuals and small medium sized companies and maintains about 23% large corporate/public sector lending, 44% SME lending and 33% individual loans. The bank has about 30 million individual accounts; 170,000 domestic company customers and about 5000 local government customers.

6.3.4 Resource Profile

The following resource profile highlights the competitive advantage derived from the resource combination among the three combining banks.

- ***Keiretsu resources***

The combining banks still maintain their relationship with the Fuyo-Yasuda group and Kawasaki group, however there has been a slight change in the relationship due to the decline in cross-shareholdings and also less number of loans made out to the groups.

- **6.3.4.2 Organizational resources**

Bank 3 and 4 have combined in a manner as to utilize their already existing resources more efficiently and relied less on outside resources.

- ***Management and Leadership Resources***

Leadership was a concern for Japanese mega-banks as discussed by banking analysts ‘it was hard to decide on Presidents of the banks, especially, when you are under pressure to cut costs, consolidate business, become competitive and subsequently, you are being pulled in three directions, its hard to move forward.’ It was only under Mr. Maeda’s leadership, did the threat for hotbed formation of faction groups had dissipated.

More specifically, there was an internal struggle between Bank G which had always played a dominating role in Japanese business and finance, therefore, wanted an upper hand in its areas of specialization; Bank E weighted into the dispute of experienced struggles for dominance and position as a way of life of virtue from its previous bank merger; and bank F, accustomed to its leading position as a leading city bank.

GM for different positions was hired from the three combining banks as a means to maintain some kind of balance among the three companies. As examples, GM GTF is from the Bank F; GM Bank E is in another position and GM Corporate Banking is from Bank G. So there is a criss-cross 'taskigake' in relationships that are being maintained, which is a unique resource characteristic. The board of directors is composed of seven directors, including the president and CEO. There has been a 20% decline in terms of board members and executive officers.

- *Corporate Culture Resources*

A unified corporate culture is what the banks were trying to achieve although it was hard initially, as employees would often retain and talk about their affiliation with their former bank. As a measure to make the employees adapt quickly and adjust in the new environment some old employees were retired and then rehired under the holding company. Another unique feature added was that top management would periodically, conduct meetings with Japanese expatriates in English to make them part of the new business model being developed globally.

- **Human Resources**

Human resource is also considered another essential resource for the combining banks. Full range of talent, knowledge, capabilities was transferred from previous banks. There was some overlap of employees in the banks therefore; about 7000 jobs (from a total of 35,000) were cut down with a reduction in compensation by 10%; for management reduction was about 30% in compensation packages. Some shuffling of

employees of the three banks also took place in order to share and promote the business skills. An exchange officer program was initiated whereby, about 300 employees were exchanged in the; human resources; risk management and auditing; business promotion - planning area, and in dealing and trading for foreign exchanges and derivatives area.

In overseas branches new human resources were allocated. Ten non-Japanese speaking GMs have been hired for overseas branches in Americas, European and Oceania operations. Another unique feature is that an Australian lady is heading the Australian operations.

New compensation and evaluation system were developed with over-time system that rewarded employees based on their jobs and performance, instead of basing it on seniority. A unique feature added to bank 3 and 4's profile are; i) basic framework of the personnel system, including rank classifications based on duties and career paths; ii) basic elements of welfare benefit programs, such as health insurance; and iii) design of retirement benefits and pension schemes that allow personnel transfers between group companies. A welcoming party was organized by MHFG whereby 1000 new employees attended the ceremony. The three banks conducted joint recruitment activities through the cooperative partnership program that was established. The three banks had published a joint brochure and created a home page on the internet for recruiting.

- **Physical Resources**

The physical resources prominent in Bank 1 are i) IT systems; and ii) branches.

- *IT Resources*

The existing operations of the three banks were integrated to create one system with strategic related investments amounting to about Yen 150 billion annually, including i) building databases to support market strategies; ii) build global risk measurement systems and systems to support domestic and overseas trading activities; iii) build an e-business model and iv) expand cash management systems for corporate clients to

manage corporate funds efficiently. It was designed in a way to utilize the present IT resources in the combining banks to a maximum. The integration began in January 2000 and was completed by March 2002.

A suite structure is adopted, whereby, the systems of the three banks are reviewed and the most efficient system for each product is reviewed and selected; specifically for the market system (dealing and trading) and for business information systems.

Computer systems for Bank 3 wholesale banking and financial markets and securities business were built around Bank G's existing system while database and other information systems were based on Bank F's systems. Bank F (developed by IBM Japan) and G's computer systems that handle individual deposit accounts were switched over to Bank E's systems which were developed by Fujitsu Ltd. Bank 4 uses Bank E systems. The bank plans to cut Yen 30 to 50 billion annually of their 110 billion yen in IT costs (March 15th 2000).

On the 1st of April, ATM disruptions, delayed fund transfers, debit card settlements, blocked bill payments with a portion of 3 million transactions being processed after April 2nd and till the 5th of April, about 105,000 transactions remained unsettled with both Bank 3 and 4 operations caused due to inadequate integration of networks. Moreover, about 30,000 instances of double debit have been identified in transaction from April 1 to April 5th. ATM disruptions resulted in debit entries in passbooks without receipt of cash in 147 transactions. The trouble was caused due to an error in a program modification to the Relay Computer System. This problem was corrected on April 2nd and the unpaid cash along with corresponding service charge, was re-deposited by April 2nd.

Resources were deployed both on administrative and systems sides to effectuate processing. A project team headed by the Deputy President of Bank 4 was set-up to investigate the cause of the troubles and re-establish appropriate control on systems. Inquiry centres manned by approximately 100 employees to respond to questions from

customers were set-up. On the first day, April 5, the centres had received about 1,500 calls.

- *Branches*

At the time of the merger between the three banks there were 740 branches. After the M&A Bank 3 had 18 domestic offices; 46 overseas offices and 29 overseas subsidiaries. Bank 4 had 664 branches (inclusive of 91 sub-branches and 7 agencies); about 6000 ATM services. By 2005 the bank cut costs by USD 900 million that involves shedding a quarter of their domestic branches and cutting 6000 jobs by 2005. In terms of physical assets, two buildings were sold off from which the cash proceeds were used to clear the NPLs.

6.3.5 Strategic Benefits

By way of choosing specific partners i.e. Bank E, F and G integration, the model presented in chapter 4 is tested, amended based on this case study and presented in figure 6.6, which is applicable in deriving a competitive advantage based on the M&A motives and strategies adopted by Banks 3 and 4. Competitive advantage as argued by Tamura (2005, p. 91) for Banks 3 and 4 starts from the fact that the group has always regarded itself as a superior bank on the basis of 'staff awareness of the role that has been played in the contributing to growth in the Japanese economy (Bank G); origins as the first commercial bank (Bank E) and breadth of client coverage covering extending to two-thirds of all listed companies.

In a nutshell, the three banks plan to accelerate plans to merge or close domestic branches and reduce payroll in order to return there is a total of Yen 2.8 trillion (USD 27.18 billion) in public funds they received in March. The banks were expecting to post a total of Yen 2.25 trillion in consolidated gross operating profit in the year ending March 31, 2006, up 20% from their combined total in fiscal 1998, while slashing just above 10% or 800 billion yen, in costs over the same period (Asia Pulse, December 24, 1999).

According to bank management the new banks aspire to be; i) one of the top five global banks in terms of market power and customer satisfaction; iii) a front-runner in IT and FT (financial technology); iv) No.1 in domestic commercial banking, securities business and investment banking; trust and asset management, and settlement businesses; and vii) a management structure with 'best practices.

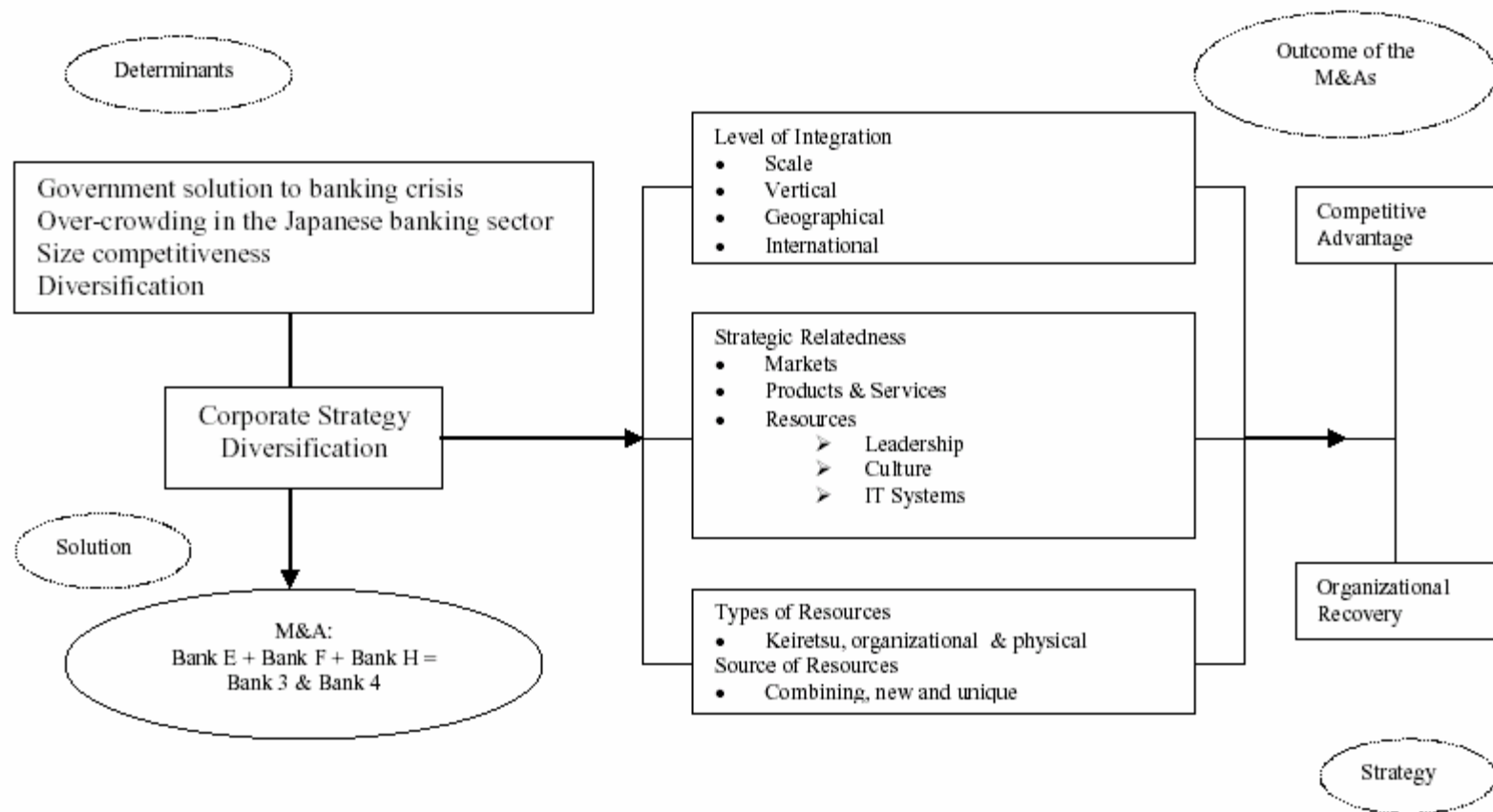


Figure: 6.6 Bank 3 and Bank 4 Conceptual Model

6.4 Case-study Bank 5 M&A

Bank 5 was formed through the reorganization and merger between Bank H and Bank I on March 1, 2003. Bank H is the surviving company with Bank I was the dissolving company as shown in Figure 6.7. The headquarters are in Osaka and Tokyo. It is listed on the Tokyo, Osaka and Nagoya stock exchanges.

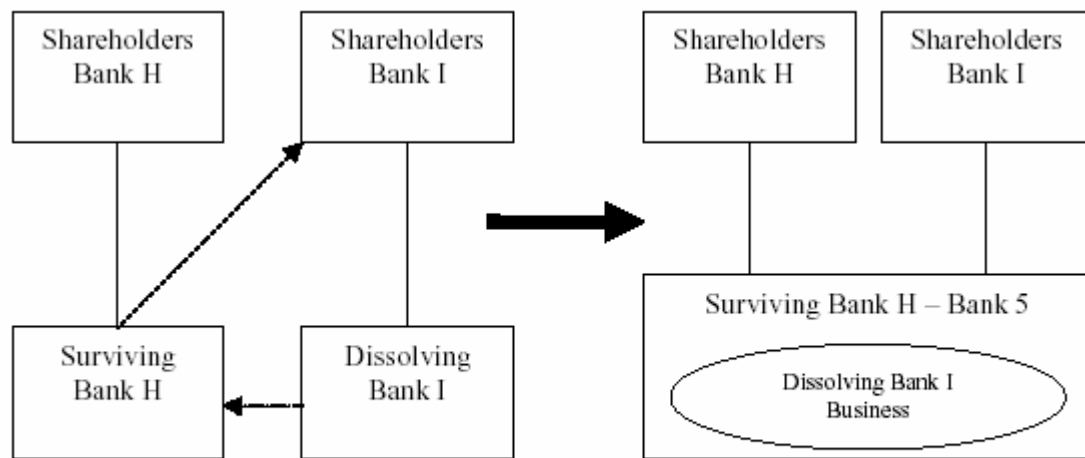


Figure: 6.7 M&A Structure - Bank 5

The change took place on October 1, 2002 after seeking shareholder's approval at the annual General Meeting in June 2002. Bank 5 is characterised as a super-regional bank, 'a federation of regional financial institutions; key member of Japan's banking industry' (annual report, 2001; pp. 7) and therefore, its management style is different from the other banks.

Characteristics	30 September, 2003
Head Office	Osaka
Amount of Capital	Yen 443.1 billion
Number of Employees	13,300
Branches	367
Assets	Yen 29,187,771 million
Consolidated Capital Ratio	12 % (BIS Guidelines)
Deposit	Yen 21.6 trillion
Loans & Bills Discounted	Yen 21.7 trillion
Long term credit rating	30 November 2003
Moodys	BAA3
S&P	BBB-/A3

Table: 6.4 Bank 5 Characteristics

6.4.1 Planning Stage

In the case of Bank H and Bank I consolidation, the group did not have much to in terms of searching for other partners as the aim for Bank 5 Holding Group was to reorganize the four banks within their existing structures into a new holding company. According to banking analysts this was a complex merger as first Bank I had to split – off its Saitama operations to separately form a separate Bank and then Bank H and I combined. Both banks were streamlining both bank businesses into one unified system as they are relatively small banks unlike the city banks. A new business model is being introduced with the organizational structure to be regional orientated, known as the area management system, whereby more authority is delegated to the Area CEO's and the sales front interacting with customers on a daily basis have more responsibility. This makes the head-office structure slim and flat. The first 100 days were deemed critical and was split into four parts; i) minimization of risk factors such as problem loans and reduction in excessive stocks; ii) reduction in operating costs by reviewing cost structures; reduction of personnel costs, retirement benefits and improving efficiency of back office; iii) strengthening of governance and compliance; and reform of corporate culture.

In March 2003, when the banks were planning for the said integration, the auditors gave a notice of a big cut in tax deferred assets, for which the bank had to request for a Yen 2 trillion public funds injection. Other reasons that assisted with the request for a capital injection, included i) clearing problem loans from balance sheet; and ii) write-downs of unrealized losses on stocks, the Program for Financial revival, announced in October 2002.

Moreover, the problems faced by the merging banks at the time were more specific in terms of organizational recovery for the banks i.e. reducing non-performing loans, reducing operating costs; defining a straighter and transparent management and corporate governance system with a more aggressive and open style of doing business.

6.4.2 Motivations for Consolidation

There are a number of reasons why Bank H and I decided to go ahead with this specific M&A.

- **Macro-economic Rational**

On a macro-economic level the banking crisis with the large slate of non-performing loans between the combining banks seemed to be the reason why Bank 5 was formed.

- *Banking Crisis - NPLs*

At the time of the merger, both banks were burdened with non-performing loans with an NPL ratio at 11%. The NPL position for Bank H started to build up in 1996, when Bank H's New York office had incurred a loss of Yen 100 billion. After both banks had received two rounds of public funds in 1998 and 1999, in 2002 they decided to merge in order to strengthen their asset base, through scale expansion while repaying back the public capital and Bank 5 will be in a position to dispose of their claims to 'doubtful' or lower categories of borrowers in the amount of 1.2 trillion yen. As a result of the removal of such claims from their balance sheets, their combined claims to such borrowers will be halved. Balance as of March 31, 2002 is Yen 1,845.7 billion with a final disposal planned in fiscal 2002 (removal from the balance sheet) for approximately Yen 1200 billion, with a balance remaining as of March 31st, 2003 of Yen 870 billion.

- **Intra-banking Level Rational**

The catalyst for the banks H and I to combine on a intra-banking level are discussed below.

- ***Diversification - Profitability and Cost Competitiveness***

With the bank possessing a weak balance sheet bank management focus was on generating ‘profits’ for the banks, ‘through implementing rationalization measures, i.e. increasing loans, nurturing strategic subsidiaries, and realizing synergistic effects from the management consolidation.’ Bank 5’s goal was to develop closer ties with community by measuring up to their requirements as most of the clients are based in regional areas.

- ***Corporate Governance and internal reforms***

It is often cited by banking analysts that primarily the bad debt problem existed due to lack of proper management and governance structures within both the banks. Therefore, Bank 5, while replacing the old management aims to create a highly transparent management system, and introduce other internal reforms.

6.4.3 Strategic Relatedness

The reasons narrated above give impetus for the said consolidation activity on a broader scale. However, there were a number of other similarities and differences in terms of strategic relatedness between the combining banks that were viewed as critically important.

- **Markets Relatedness**

The merger was based on realigning bank H and I based on their regional coverage to cover the small to upper-middle corporate and individual clients. Bank H is based in western part of Japan in Osaka and Bank I is based in Tokyo and Saitama regions. Bank 5 will maintain close links to other group banks, linked through internal regional bank systems in order to share resources with them.

- **Products & Services Relatedness**

Banking analysts maintain ‘ bank H, as a city bank, was unique because it operated on a commercial level mainly in trust banking (monetary claims trust, land trusts and special donation trusts; others like investment trusts, retirement benefit trusts, money trusts and so on will be transferred to The Bank H Trust & Banking Company. Ltd.). With the merged entity of Bank H and Bank I, trust banking business existed from inception and such business will be sold to the client base provided by Bank I. Moreover, trust business, private banking, derivatives, real estate, inheritance, and other trust services will be further developed and closer ties will be developed with Trust and Banking groups.

The merger will benefit Bank 5 to strengthen its retail banking business with focus on small medium sized companies which accounts for about 40% of their business and housing loans which accounts for about 45% of bank 5’s business predominantly coming from Bank H portfolio. Bank H was also offering ‘Retail 48 (West)’ a new type of small-loan product targeted to SMEs that is based on the same scheme as the Bank I existing ‘Retail 48.’ The small loan products will be strengthened based on banks scoring model that reflects the regional characteristics of the Kansai region and Bank 5 will enable the group to extend some Yen 1.5 trillion of housing loans annually.

6.4.4 Resources

A number of resources played a critical role towards creating a competitive advantage for Bank 5.

- **Organizational resources**

The organizational resources that influenced a competitive advantage for Bank 5 include; i) governance and leadership; ii) corporate culture; and iii) human resources.

- ***Governance and Leadership***

The management style adopted at Bank 5 was unique as after the restructuring of the new group, the management was replaced including the removal of the former management and the appointment of independent, outside directors (annual report, 2003; pp. 6). About 142 directors and auditors, including five representatives resigned from group banks and affiliates. It was the first time that a unique corporate governance style was elected based on U.S. style, composed of 10 BOD members at Bank 5 Holdings, six independent directors with various backgrounds, and the CEO was from Japan Railways, from a different field to banking. Others were either dispatched by the government or hired from the private sector. This style facilitated in the cleaning up of its balance sheet, develop business opportunities as a result to provide a profit for Bank 5.

- ***Corporate Culture Resources***

One of the main resources that required immediate attention was the change in the business culture of the combining banks, which were often stated as ‘in-ward looking.’ Therefore, the structure were changed to allow for a more vibrant and open business atmosphere, orientated towards achieving profitability and changing the current conservative atmosphere.

- ***Human Resources***

Banks staff was carried over from the combining bank with a reduction of 1300 employees among Bank 5 group. Starting March 2003, Bank 5 Group adopted a new retirement payment and pension systems such as cash balance plan and pre-paid retirement benefit and so on and also adopt a new salary system that places importance on the roles and specific achievements of employees. In addition, by reducing the level of pension payments Resona Group plans to reduce its retirement benefit liabilities by approximately 40 billion yen and the annual retirement benefit expenses by 2 billion yen.

Some important positions were filled in by the ‘aggressive use of external advisors for finance, risk management and human resources positions and the appointment of Kao Cost Reduction Team as advisor.’ Other form of recruitment was to hire young staff based on full-time and temporary basis to maintain low costs and also ensure a higher level of efficiency. The bank standards and code of conduct was simplified, temporary staff and regular staff was shifted from back office to front office and vice versa. This reshuffling of staff proved to have added value. However, 2002 and 2003 did prove to be very painful years for the employees, as salaries were cut by 30% due to the restructuring phase of Bank 5. A dual responsibility staffing system was applied whereby; staffing was applied to both the divisions of the holding company and bank. The bank will allocate the right staff for the right job regardless of which bank he/she comes from. According to the banking analyst interviews bank 5 implementation process was successful.

- **Physical Resources**

The physical resources prominent in Bank 1 are i) IT systems; and ii) branches.

- ***IT Systems Integration***

One of the new plans for the bank was to implement ‘branch-in-branch’ system, which will enable the consolidation of overlapping branches before integration of computer systems.

IT Systems Integration was used to develop direct banking, CRM systems for database marketing and so on (September 21, 2001, Resona bank website). Bank 5 hired Reuters to implement the Reuters Electronic Trading for Automated Dealing (RET-AD), thereby hosting Bank 5’s foreign exchange dealing internet portal. Bank 5 was the first bank to implement such a system. Nobuyoshi Yamaguchi, Executive Officer, Corporate Business Division, Bank 5, explains ‘by choosing Reuters automated dealing system we will be able to automate existing FX operations, providing more convenient

and faster services to our corporate customers. The new system will allow corporate clients to access and trade on real-time, executable foreign exchange prices by assessing Bank 5's website from any standard browser. Additionally, by choosing Reuters hosted option we will be able to offer a service at a lower cost than if we had developed independently (Reuters, 26 January, 2004).

Business Tie-up was another way for Bank 5 to strengthen its business; bill clearing operations, integration of intra-firm mail delivery systems joint administration of off-premises ATM corners, mutual operating of ATM networks, sales of common products [mutual funds, business loans designed for small and medium sized businesses etc.] tie-up in the field of trust business, exchange of personnel (trust business, private banking business etc.), with a view to deriving benefit from such reciprocal arrangements (September 21, 2001, Resona Bank website).

- ***Branch Networks Other bank assets***

Bank 5 took over all branch offices of the combining banks. There were 573 for Bank H and 367 for Bank I. Company housing and other related facilities were disposed of in order to reduce expenses.

6.4.5 Strategic Benefits

By way of choosing specific partners i.e. Bank H and I integration, the model presented in chapter 4 is tested, amended based on this case study and presented in figure 6.8, which is applicable in deriving a competitive advantage based on the M&A motives and strategies adopted by Bank 5. Bank 5 embarked on a mission to develop itself as a super-regional bank and maintains an open door policy for other regional banks to explore the options of joining in with Bank 5 and Bank 5 Holding Company. The synergies resulted from unified strategies and reallocating resources; well balanced coverage of branch networks; wider array of products and services through know-how integration and integration of systems infrastructure. The M&A resulted in a profit of Yen 500 billion with rationalization effect from the integration of systems is estimated

to be 16.8 billion yen in fiscal year 2005 on a non-cumulative basis (April 12, 2002 Daiwa Bank Holding, Inc.). In 2004, the company managed to turn a profit of about yen 386 billion and the Bank 5 management plan is pay of the yen 868 billion of the yen 3 trillion over the next 10 years.

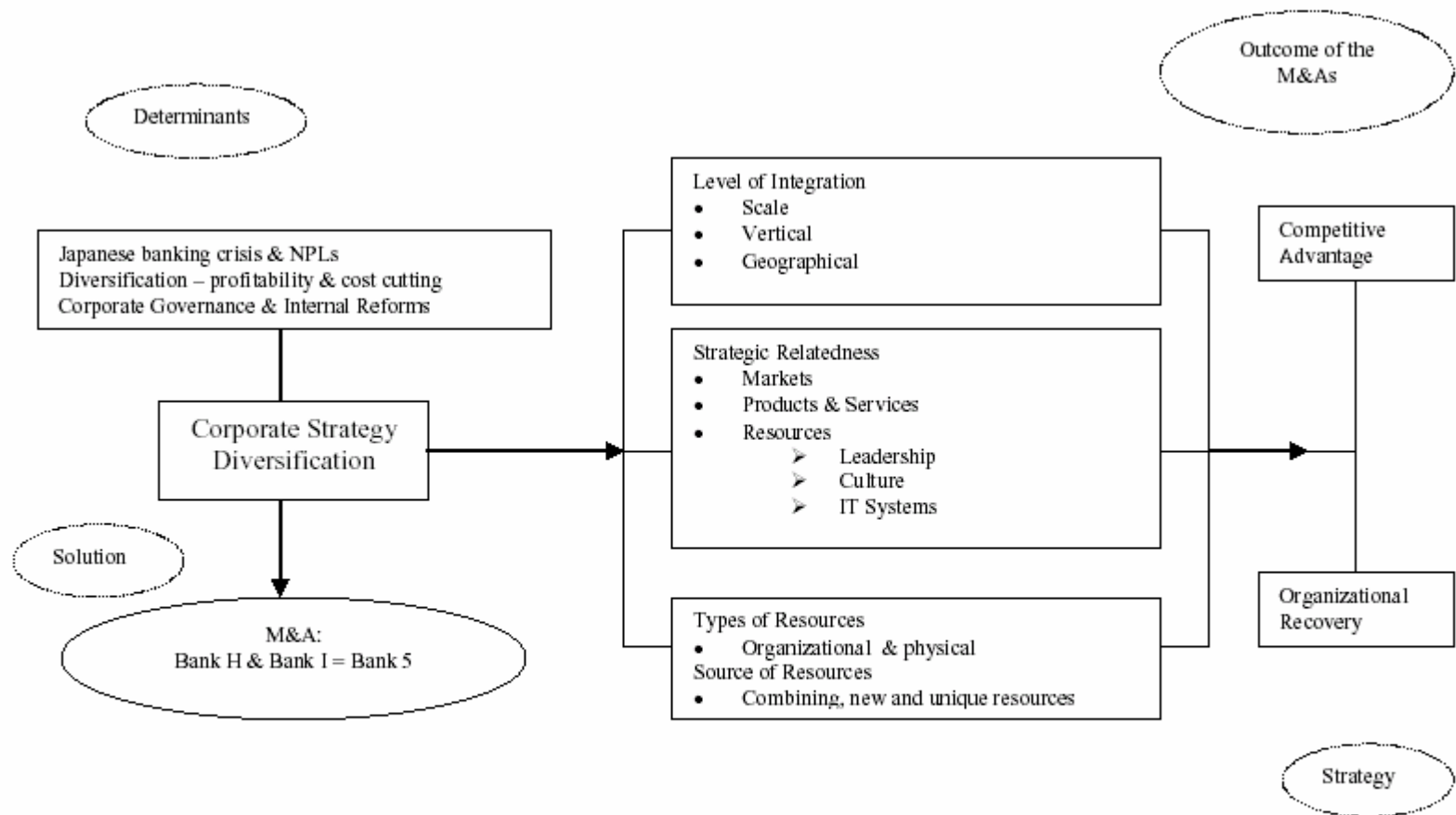


Figure: 6.8 Bank 5 Conceptual Model

Chapter 7:

Results: Analysis and Discussion

This section provides a cross-case analysis and linkages with extant literature based on the findings of the case studies presented in the preceding chapter. Furthermore, the propositions tested through this research are presented with a tested model based on Japanese mega-bank M&As competitive advantage and organizational recovery (please refer to figure 7.1). The subsequent presentation is split into six sections; i) the importance of the planning stage; ii) the motivations for the Japanese mega-banks to adopt M&A strategy; iii) what type of strategic relatedness existed among the combining banks; iv) what types of resources and their source may have influenced the Japanese mega-banks to derive a competitive advantage; v), the role of regulatory authorities; and vi) key implications of this research and advancing the strategic management and Japanese banking knowledge is discussed. Table 7.1 discusses these points in details, pertinent to the five mega-banks under investigation in this thesis.

7.1 Importance of the M&A Planning Stage for the Japanese mega-banks?

The planning stage is fundamental for the Japanese mega-banks, as it is during this stage that the motivations, integration levels and structures, specific partners, and their combining attributes suggest what kinds of benefits maybe derived from the specific M&As. Japanese bank M&As follow some specific business routines that were not presented through the findings of this research. Therefore, proposition 1 has been rejected by the research findings on the five Japanese banks under investigation. This can be argued as the Japanese banking literature presents that; *nemawashi*; *ringi*; middle-up management; negotiation; due diligence; and documentation are imperative stages for the Japanese mega-bank M&As. The findings suggest that the Japanese mega-banks followed some planning and strategy routines however, they did not display signs of following the Japanese business routines therefore, some of the problems envisaged during the combining stage and not realizing the true competitive advantage that could have been achieved otherwise is maybe due to this reason. Moreover, it can be stated that perhaps the planning strategy was not fundamentally considered imperative because the M&A diversification strategy adopted by Japanese

banks was fairly a new idea therefore, causing some hesitation or discomfort for the bank management and staff. One needs to note that the M&A phenomenon was a new concept both for Japanese regulators and Japanese banking management arising after the Japanese financial crisis. Therefore, both from the perspective of the regulators and banking management lacked the relevant and required experience and confidence in implementing an aggressive planning stage. However, they had no choice quick decisions had to be made in order to save the banks from the financial crisis and therefore, they had to adopt this M&A strategy. However, some of the banking analysts maintain that once they have gone through this restructuring phase and at a highly critical time they are confident in submerging and opening up their banking world to more sophisticated restructuring and diversification strategies including overseas business mergers, acquisitions, and other forms of business alliances. Through the interview dialogue with representatives from the Japanese financial sector, it can be stipulated that after undergoing a series of M&A activities among various banks, that now the M&A market is ripe and the banking and financial sector in Japan has achieved a mentally mature state of engaging in future restructuring processes. M&As for the mega-banks maynot be appropriate as the market has already reached saturation point with 3 mega-banks and 1 super-regional bank however, alliances with regional banks and other forms of financial institutions maybe possible in Japan. Other forms of literature conducted in other countries maintain that value is created either by the realignment of operations and strategic changes during the planning and combining stage or simply because a combination has taken place (Seth, 1990). Therefore, it is essential for the Japanese banks to have developed a proper M&A strategy. It was often also cited as a slow process because managers had to put in double the time, on one hand they had to carry out their normal business routines and on the hand they were involved in the planning and implementation of the combining banks. This presented time delays and hurdles in conducting the said M&A routines. Moreso, the banking system in Japan was still adjusting to the de-regulation process and therefore, they required time to handle and adjust to all the policy level initiatives implemented as a result of the de-regulation wave. Even if the banks were experienced in the M&A activity they were still constrained by the number of activities they could conduct by themselves since the traditional Japanese management practises call for all process and

procedures to be approved by the highest authority which was an extremely hard task and definite time delays were experienced.

All Japanese mega-banks adopted the *kabushi-iten* transaction mode of payment, based on absorption M&A style; known as *kyushu gappei* because of simplified procedures and tax benefits associated with it. The banks that remain in business are known as the surviving bank *sonzoku kaisha* and the bank that transfer its business into the surviving bank, is classified as the dissolving bank, as it ceases to exist after the consolidation. The holding company structure was also introduced whereby Bank 1 was first formed and then restructured later into a holding company, in order to strengthen their banking group and also follow the other Japanese mega-banks. With Bank 2; two existing holding companies were integrated to form Bank 2 financial group as their respective banks were combined to form Bank 2. Bank 3 and Bank 4 formed a holding company with the three pre-combining banks and then the FG was formed by spinning off independent entities in retail banking, whole sale banking and other specialized businesses. With Bank 5, the already existing holding company was restructured to form a new holding company at the time when Bank 5 was formed. According to banker's association in Japan, holding company has given posture to the banking sector by providing a means of diversification in terms of efficiency, operational structures, markets, and products and services. Shimotani (2007) suggests it provides a strategic advantage for the Japanese banks by streamlining management into 'creating a source of dynamism for development of the industry and providing brand imaging' (pp. 183). The bank holding companies will deploy their resources towards profitability and return on assets rather than on the maintenance of cozy corporate ties and mutual protection against take-overs.

7.1.1 Integration level

Japanese mega-banks were aiming for complete integration in term of their business segments alongwith with the formation of a single headquarters under a holding company set-up. Thereby, the Japanese mega-banks were aiming for scale, vertical and international integration. Please refer to table 7.1 for the M&A strategies adopted by the

Japanese mega-banks. The level of integration is considered a critical aspect for the mega-banks involved in the M&A activity as a successful integration defines the types of benefits derived from the combination in order to achieve a scale, scope or mix of output that is more profitable (Berger et. al. 1998). Scale integration, the simplest form of financial integration, has allowed the Japanese mega-banks to consolidate the production and distribution of financial services into fewer, larger units. Scale integration sometimes also suggests that economies of scale exist prior to the M&A activity, whereby the firms are not operating at their full potential. This is true for Bank 3 and Bank 4 as they did not acquire any new resources as they wanted to utilize the existing resources of the combining banks to their full potential.

International integration is more complex as it involves the institutions to adapt to different cultures, languages, currency, regulatory and supervisory structures, and geographical distances. It also involves for higher risks in terms of political, social and economic infrastructures of the international location and foreign exchange risk. This is evident from Bank 1 when realigning their operations in overseas markets they had to seek permission from local regulatory authorities to conduct the respective operations. Haspeslagh and Jemison (1991) emphasize that the role of the integration phase is relevant to consider in understanding the performance of the entire M&A process. Therefore, in this case both propositions 2a and 2b are supported and show that all Japanese mega-banks under investigation derived a competitive advantage in terms of cost-saving as complex nature of the integration provided them with more flexibility in utilizing and even deleting some existing resources from the combining banks. Proposition 2b also suggests the more complex the integration the more the chances of problems arising are greater and it is true in the case of mega-banks 3 and 4 as their IT systems integration failed on the day of the launch. Fundamentally, all banks had challenges but with more precise details, fine-tuning and rehearsing of the business operations to be implemented they all managed to overcome their integration problems.

Characteristics * at the time of the M&A	Bank 1	Bank 2	Bank 3	Bank 4	Bank 5
Motivational Factors					
Macro-economic Rational					
Government Deregulation	•	•			
Government Instigated			•	•	
Banking Crisis – NPL problem	•	•	•	•	•
Industry Level Rational					
Over-crowding			•	•	
Size Competitiveness	•	•	•	•	
Intra-Bank Level Rational					
Diversification					
Customer needs - Products & Services		•	•	•	
Profitability & Cost savings		•	•	•	•
Resource utilization			•	•	
Offering competitive environment for staff			•	•	
Internal reforms – management replacement					•
International Rational					
Asian Currency Crisis	•				
Integration Level					
Scale	•	•	•	•	
Vertical	•	•	•	•	
International	•	•	•	Some	Some
Strategic Relatedness					
Market Coverage					
Kanto	•	•	•	•	•
Kansai	•	•	•	•	•
Kyushu	•	•	•	•	•
International	•	•	•	•	•
Products and Services					
<i>Retail</i>					
Individual (home loans)	•	•		•	•
SMEs	•	•		•	•
<i>Private Banking</i>	•	•			•
<i>Wholesale</i>					
Long term Loans	•	•	•		

Capital Markets	•	•	•		
Internet Banking – virtual banking	•				
Resources					
Strategic Resources					
<i>Markets</i>	•	•	•	•	•
<i>Products & Services</i>	•	•	•	•	•
<i>Foreign Exchange Business</i>		•			
<i>Strategic alliance with regional banks</i>					•
Keiretsu Resources					
<i>Clients Resources</i>	Combining to increase	Combining to increase	Combining to increase	Combining to increase	
Financial Resources					
<i>Capital Markets</i>	Strengthened	Strengthened	Strengthened	Strengthened	Strengthened
<i>Cross-shareholdings</i>	Unwinding and decreased in value	No change	Unwinding and decreased in value	Unwinding and decreased in value	
Organizational					
<i>Knowledge</i>	Unique				
<i>Leadership</i>	Carried forward	Carried forward	Criss-cross	Criss-cross	Replaced New Unique
<i>Governance</i>					Changed to new
<i>Culture</i>	Combine to adapt to form new mono-culture Unique	Combine to form mix	Combine to form new	Combine to form new	Changed to more aggressive New
<i>Senior management placement</i>	Unique				
<i>Staff placement</i>	Reshuffled based on expertise in relevant sections Unique	Reshuffled based on expertise in relevant sections Unique	Reshuffled based on expertise in relevant sections Unique	Reshuffled based on expertise in relevant sections Unique	
<i>Employees</i>	Newly hired Laid-off Voluntarily left Shifted to sister companies Early retirement	Newly hired Laid-off Voluntarily left Shifted to sister companies Early retirement	Newly hired Laid-off Voluntarily left Shifted to sister companies Early retirement	Newly hired Laid-off Voluntarily left Shifted to sister companies Early retirement	Newly hired Laid-off Voluntarily left Shifted to sister companies Early retirement
<i>M&A Specialists</i>		New			
<i>Legal</i>	New				
Physical Resources					
<i>IT System Integration</i>	Combined to form new	Combined to form new	Combined to form new Newly hired	Combined to form new Newly hired	Combined to form new Newly hired

	Newly hired	Newly hired			
<i>Branches</i>	Downsized Closed & sold Upgraded	Downsized Closed & sold Upgraded	Downsized Closed & sold Upgraded	Downsized Closed & sold Upgraded	Downsized Closed & sold Upgraded
<i>Bank commercial property</i>			Sold	Sold	
<i>Company houses</i>					Sold
Challenges					
<i>Financial</i>					
Stock Market	•				
<i>Organizational</i>					
Culture			•	•	•
organizational functionality			•	•	
Governance & management					•
workforce harmonization at the branch level			•	•	
sense of unity as a business entity			•	•	
<i>Operational</i>					
Risk management		•			
Brand Positioning	•	•			
Bank Language	•				
Integration of banking divisions					
IT systems	•	•	•	•	
<i>Distance between M&A activity of same banks</i>		•			
<i>International</i>					
Delays in consolidation of Overseas Operations	•				

Table:7.1 Japanese Mega-Bank M&A Characteristics

7.2 Motivation for Japanese Mega-Bank M&As

The case studies narrated above suggest that there are numerous motivations behind the Japanese mega-bank M&As. A cross-case analysis of the motivations is discussed in the subsequent section based on i) macro-economic; ii) bank-level; iii) industry level; and iv) global perspectives.

7.2.1 Macro-economic Rational

The following section discusses the two macro-economic rational for the Japanese mega-bank M&As, namely; i) de-regulation program; and ii) banking crisis and the bad loans profile of Japanese banks.

- **De-regulation Program**

Proposition 7 is refuted in this research as it signifies that the big bang program essentially the de-regulation process did have a significant impact on the Japanese mega-bank M&A activity in providing a competitive advantage. Whereas, all Japanese mega-banks, maintain that the de-regulation process initiated by the inception of the big bang in 1997 meant that Japanese banks could choose to become more competitive by offering a diversified range of products and services. Therefore, in order for the Japanese city banks to become more competitive they took advantage of the Japanese de-regulation policy and started looking for partners. This follows the Japanese banking literature as prior to the deregulation Japanese banks had to seek approval from MoF over introduction of new products and services, opening, closing and relocation of branches and so on (Fukao, 2003), whereas now with the banking sector deregulated they are more at ease in terms of speed of launching new products and services, relocating branches and other facilities, divestments of units and aligning products more towards clients needs then before. As discussed by Vennet (1996), in the context of EU banking sector deregulation provided a breakdown of the functional and geographical barriers similar is the case with Japanese mega-bank M&As. Contrary, Banks 3 and 4 call the M&A activity as ‘government instigated’ suggesting that due to the banking crisis the Japanese government was introducing ways of restructuring the banking

sector and provide the banks with the provision of clearing their bad debt profiles (as discussed below). Therefore, Japanese Big Bang program defined the outlay for Japanese banks to become more flexible and away from the helm of the Japanese bureaucracy, in essence the banks to clean their slate of non-performing loans (Fukao, 2003).

- **Banking Crisis – NPL Problem**

One of the concerns Japanese mega-banks had was the non-performing loan profiles of yen 75 trillion, as a result of which many Japanese banks were facing bankruptcy; credit rating downgraded and required immediate financial assistance. This is supported in this research, proposition 6 that NPLs were the driving force behind the failure of financial sector and therefore, provide an impetus for the M&A activity in the Japanese banking sector. This follows suit with the Japanese banking literature based on the convoy system and safety net provided by MoF, whereby MoF provides assistance in the form of financial bail-out or asks other banking partners to assist the ailing institutions in the form M&As or forming other strategic alliance (Kawai, 2003). The restructuring of the banking sector provided for cost savings and profitability and therefore, banks could improve their financial health.

7.2.2 Industry Level Rational

The following section discusses the two industry level rational for the Japanese mega-banks, namely; i) over-crowding in the Japanese banking industry; and ii) size competitiveness.

- **Over-crowding in the Japanese Banking Industry**

Banks 3 and 4 maintain that the Japanese banking sector was overcrowded with 10 city banks, 3 long term credit banks and a large number of regional banks wrestling, with overcapacity, lingering bad loans, and years of losses incurred during the nation's slump years. After the M&A activity in Japan only 3 mega-banks emerged, with one super-

regional bank and a handful of regional banks. M&As are used as a restructuring tool to make the banking landscape more competitive and therefore, reduce the large number of banks, into a smaller, tighter and more competitive market (Vennet, 1996). Therefore, it can be suggested that proposition one is accepted as by reducing the number of banks a more competitive environment is created, creating more opportunities and more competitive products and services for the clients. This in turn is laying the basis for a healthy banking sector. Demsetz's 1973 monopoly theory, suggests that M&As are carried out to achieve market power, by strengthening their competitive position in their home markets, thereby, providing opportunity for cross-selling of products (Trautwein, 1990).

- Size Competitiveness

Japanese mega-banks wanted to achieve size scale in terms of assets to become more competitive and profitable. Bank 5 did not display such a motivational characteristic, maybe because they are a super-regional bank. Proposition 4 is accepted as achieving size and scale for the Japanese mega-banks and therefore, seeking profitability along the way. In terms of market power, 'big size' has been associated with posing an increase in market share and at the same time decreasing some internal competition for the banks. Auster and Sirwas (2002) maintain 'the race for bigness' is the latest corporate trend in corporate strategy. To survive competitively in an era of rapid technological change, swiftness of product life cycles, increasing costs of new product development, and formidable barriers to entry, many top managers believe that quick purchases or M&As give them the critical size and the nimbleness they need (Auster and Sirwas, 2002). This falls in line with Marks and Mirvis (1988) study that sheer size is often considered as an essential competitive factor and is often the driving force behind M&As.

7.2.3 Intra-Bank Level Rational

The following section discusses the two intra-bank level reasons as to why Japanese mega-banks adopted the M&A strategy based on; i) diversification and ii) internal reforms and governance structures.

- Diversification Strategy

Japanese mega-banks 2,3,4 and 5 wanted to enter the M&A activity in order to diversify; fully utilize resources, thereby cut costs and increase profitability, and offer better products and services, whereas, Bank 1 did not show any sign of such motivation. Proposition 10a, 10b, 10c is accepted by this research as it supports banks 2,3,4 and 5, whereas, bank 1 did not display signs of such behaviour. Proposition 3a discuss's resource re-deployment as a source of competitive advantage for the banks involved in the combining stage. This supports the diversification theory of Williamson (1975) and Coase (1937). It states that diversification may be a desirable alternative to selling off access capacity when there is some failure in the market and the ability to redeploy the firm's assets (Amit and Zarowin; 1989). Proposition 10b suggests that more products and services offered as a result of the M&A activity also provide more profitability for the banks. Diversification takes managers to multi-markets and introduces products and services with the opportunity to negotiate, with or coerce, competitors to act in ways conducive to superior performance (Shelton, 1988). Proposition 3c holds true as the banks following the past traditional business acumen of growth first and profitability later, realized profitability comes first and then growth as it allows for cost-savings as a means competitive advantage which in turn provides a quick organizational recovery. Based on synergy theory M&As provide value addition, as is evident through the Japanese bank M&As that they were able to cut costs, increase profitability and clean the NPLs profile. With the urge to make the business more competitive, the ideology of profitability came first and growth followed suit (Shimotani, 2006) whereas traditionally, the focus was on growth. Finally, in terms of diversification, proposition 3d is also accepted through the findings of this research. Changes in the traditional

Japanese banking practice in terms of long term employment system, that encouraged banks towards profitability was the introduction of stock options and the transition of executives' salary to performance based system that made managers strive for profits for Japanese mega-banks in terms to increase their own share in the pie (Coplan et. al., 2007).

- Internal Reforms – Governance Structure

Bank 5 replaced internal management by a new U.S. corporate governance system aiming for a new more aggressive business culture. This supports proposition 8 that changes in corporate governance style of Japanese banks did display a positive impact in influencing a competitive advantage and providing organizational recovery. Bank 1 to 4 didn't display any sign of internal governance reform and thereby, suggesting that they probably retained and carried forward their management policies and board structures. This follows from the Japanese banking literature as Shimotani (2006) maintain's that in 1997, Sony company was the first to adopt a *shikko yakuin sei* (executive or operating officer system) to move towards an efficient and effective US based governance model. This model was supposed to differentiate and divide the distinctive management roles of supervisory control and operational implementation in Japanese banks. Moreover, the size of board of directors was reduced in order to make effective decision making. However, Copland et. al. (2007) discuss that reduction of board size does not affect financial performance, and introduction of an executive officer system negatively influences profitability in Japanese institutions. This could be as many boards may still have overlaps and monitoring and execution functions. Furthermore, proposition 9 is supported in this research that *amakudari* practise hinders the performance of the banks therefore, does not yield any competitive advantage.

7.2.4. International Rational - Asian Financial Crisis

Bank 1's reason for the M&A can be enforced based on an international factor such as the Asian currency crisis as it had made overseas Japanese operations very expensive due to high borrowing costs 25 to 30 b.p. above LIBOR, as a result of which Japanese banks through the M&A activity were able to target cost-effective operations by consolidating their overseas operations. Japanese banks were actively engaged in foreign lending, thereby exposing themselves to major foreign exchange risk as well as other economic and political uncertainties. As the Yen appreciated, the cumulative losses were huge, almost of the same order of magnitude as the financial system's domestic bad loan losses (Patrick, 1988).

7.3 Strategic Relatedness

While discussing the strategic similarities and differences, it has become evident that the strategic fit aspect among combining banks was important for Japanese mega-banks in terms of markets, and products and services. Relatedness among combining firms is perceived to be important because it creates value for shareholders (Barney, 1988) stemming from resource reconfiguration between two firms (Lubatkin, 1987). Therefore, these findings suggest that proposition 11a is accepted that the greater the level of relatedness in terms of complementarity the greater the competitive advantage and quicker the organizational recovery. This is because M&As also act as a balancing act between exploiting existing opportunities and exploiting for new ones. Proposition 11b is accepted as the greater the strategic fit among the combining banks products and services, markets and resources and other combining characteristics the greater the competitive advantage reaped by the new banks formed. This is further highlighted in the subsequent sections 7.3.1 and 7.3.2. Relatedness among three resources has also become prominent in this research i.e. organizational level; management cum leadership style relatedness, corporate cultural relatedness and physical resource; systems integration relatedness; discussed in section 7.4 of this research.

7.3.1 Market Relatedness

The M&A activity among the Japanese mega-banks provided them with the opportunity to strengthen the market coverage within Japan and overseas markets. Market coverage was concentrated in the Kanto, Tokyo area and Kansai, Osaka areas. Bank 2 had an added advantage of a strong overseas presence in terms of foreign exchange business. Bank 2, 3 and 4 wanted to strengthen their Nagoya, Tokai; Kansai and Kyushu areas, whereas Bank 1 wanted to strengthen its existing Kanto and Kansai operations. This is represented in table 7.2.

Combining Banks	M&A Prior Markets	Strategic Relatedness	Competitive Advantage
Bank A	Kansai – Osaka	Complementarily – Different	Cross-selling of Products & Services.
Bank B	Kanto – Tokyo		
Bank C	Kanto-Tokyo and International	Complementarily – Different	-ditto-
Bank D	Kansai – Osaka Tokai- Nagoya		
Bank E	Kanto – Tokyo	Complementarily – Different	-ditto-
Bank F	Kanto – Tokyo		
Bank G	Kanto – Tokyo		
Bank H	Kansai – Osaka	Complementarily – Different	-ditto-
Bank I	Kansai – Osaka		

Table 7.2 Market Strategic Relatedness among combining Japanese mega-banks

This suggests that strategic fit – relatedness among combining bank markets is highly important. Thereby, aiding with the research questions on how and what types of competitive advantage is provided for the combining Japanese banks. This concept coincides with existing literature whereby a bank combining in a complementary market may add value as the acquisition allows bidders access to new but related markets (Shelton 1988). Based on the work of Seth (1990) this suggests that a related M&A strategy perspective provides for market-power related gains than two organizations competing in dissimilar product-markets. Jemison and Sitkins (1986) maintain that synergies are achieved through economies of sameness (similar operations) and economies of fitness (combining different but complementary operations). Moreover, market extension M&As are based on vertical mergers; two

companies selling the same products in different markets is true for the Japanese mega-banks.

7.3.2 Products and Services Relatedness

This research has provided impetus that Japanese mega-banks have developed strong retail; private; and wholesale banking operations by combining with respective partners (please refer to table 7.1). This suggests that newly leveraged products and services do provide a competitive advantage and a faster organisational recovery for the banks. This is because products and services relate to the level of integration that the Japanese banks were aiming to achieve i.e. vertical integration; product-extension M&A; two companies that sell different products but related products in the same market. All Japanese mega-banks follow Shelton's mode (1988) that the banks were aiming for related complementary (new products and similar clients) and related-supplementary (similar products and new customers) paths. Some elements of overlap in terms of similar products and customers is also evident i.e. Bank A and Bank B virtual banking segments, combining for more enhanced efficiencies. Bank C, especially, took advantage of Bank D's retail business and Bank D took advantage of Bank C's corporate and foreign exchange business. Bank 3 and Bank 4 were created separately to provide corporate banking and retail services, respectively. Moreover, Demsetz's (1973) market concentration doctrine suggests that M&As are carried out to achieve market power by strengthening their competitive position in their home markets. This means that profits from one market can be used to sustain a fight for market share in another market based on monopoly theory. Trautwein (1990) research maintains that products can be cross-subsidized as profits from one market can be used to grow and sustain in another market, thereby, imitating a new market strategy to re-price products. Moreover, as competition decreases as a result of M&As all competitors can benefit as products and services are re-priced. Based on literature, the behaviour of Japanese banks may also be considered counteractive to Lubatkin and Lane (1996) research maintains that the more closely aligned the operations and products and services of two businesses are the more room there is for conflict, arising from choosing which products and services to maintain and develop, or which banks to delete. However, it may

coincide with Bank 2's consideration 'it was hard to decide which product to keep and which to delete.'

7.4 Importance of Resources

Resources are deemed imperative because they are thought of as a strength or weakness for any given entity. Proposition 13 a that resources are deemed critical during the M&A activity in providing a competitive advantage and organizational recovery is accepted through the findings of this research. Resource based view, furthermore, is considered to be a significant driver of strategic competitive advantage. Resource configuration in terms of types, relatedness and source are also considered competitive in terms of Japanese mega-bank M&As. This concept of 'resource' is considered imperative not only from a practical perspective but dates back to Penrose (1959) who first discussed the importance of resources as a means of diversification.

The subsequent section provides a comparison among the five Japanese mega-banks resource structure and strategy profile followed by a discussion based on support or rejection of already existing theory. The discussion is placed as follows; i) combining resource configuration from the previous banks; ii) new resources; and iii) unique resources.

7.4.1 Combining Resources

This section discusses the combining resources i.e. i) strategic resources; ii) *keiretsu* resources; iii) organizational resources; iv) financial resources; and v) physical resources. Basically, the research supports proposition 13b, 13 c and 13d. Proposition 13b is maintained through this research that the type of combining resources in terms of strategic resources, *keiretsu* resources, financial resources, organizational resources, and physical resources all provide a competitive advantage, therefore, swift organizational recovery for the new banks formed. 13 c supports the fact that the configuration in the joining of resources is also critical. Furthermore, proposition 13d is accepted which

suggests that the nature of the resources i.e. its source termed as combining resources because they are carried forward from the previous banks provide comprehensive advantages as is discussed in the subsequent sections. The following section not only provides a cross-analysis among the five Japanese mega-banks of the types of resources but also their source i.e. combining to form new, reshuffled, retained and removed are discussed along with their relatedness aspect (table 7.1 and 7.6).

- **Strategic Resources**

In terms of strategic resources adding more markets and providing a diversified base of products and service was of benefit to the consolidating banks (already discussed in strategic relatedness section).

- ***Keiretsu* Resources**

Another noteworthy resource identified among the Japanese banks was the addition in clients from the combining banks belonging to particular *keiretsu* companies. This supports proposition 5a that the more closely related banks are to group companies or belong to a *keiretsu* group the more the competitive advantage and the faster the organizational recovery for the banks as the resources are shared between the banks and *keiretsu* group companies. Bank 1 increased clients from respective *keiretsu* affiliates; Bank 2 benefited from its *keiretsu* clients by offering bank D products and services and Bank 3 and 4 made use of the *Fuyo* group and *Kawasaki* groups in terms of clients. This adds to the present Japanese banking literature that Japanese mega-banks still maintain close ties with their *keiretsu* affiliates and have significantly benefited from the client resources by offering them more diversified products and services supply that the banks could not offer before. Contrary to the findings of this research, the Japanese banking literature presents that the relationship between *keiretsu* groups and banks is unwinding (Capron et. al., 2006). Proposition 5b is accepted that change in the cross-shareholding pattern between the banks and affiliated *keiretsu*'s have been changing with the diversification the *keiretsu* affiliates and also for them opting for alternative methods of financing i.e. capital markets. However, in terms of resources i.e.

knowledge, capital and other characteristics nothing has changed much infact, the relationship has further developed between the combining banks as the banks have shared their *keiretsu* clients. In spite of the declining importance of the bank borrowings, most companies still have a strong desire to maintain tight relationships with a main bank, as many companies expect their main banks to provide emergency funding and assistance during a crisis (Posen 2003).

- **Financial Resources**

The findings of the research in terms of *keiretsu* clients, links to the financial resources; a decline in the cross-shareholding pattern among the main banks and *keiretsu* affiliates due to the slow economic activity in Japan. This is in line with extent Japanese banking literature that the cross-shareholding in the 1990s started to unwind as they were negatively impacting the banks profitability due to the slow economic growth in Japanese economy more specifically the manufacturing sector. The banks strategy towards profitability has bent them towards choosing diversified clients and rely less on *keiretsu* affiliation (Capron et. al. 2006). Moreover, with the deregulation and capital market structures being offered *keiretsu* groups prefer to use such options rather then rely on traditional main bank financial resources.

- **Organizational Resources**

The organizational resources prominent among the combining banks include; i) management cum leadership resources; ii) knowledge capabilities carried over from previous M&A activity; iii) corporate culture resources; and iv) human resources. Proposition 12 is accepted in this research as the greater the number of M&As combining banks have experienced the more the skills provide a competitive advantage for the new banks and the quicker the organizational recovery due to the experience and knowledge shared among the combining banks to learn from the past experiences. It has become clear through this research that organizational resources tend to play a critical role in Japanese banking due to their long term traditional business culture that has been embedded in their culture dating back to as early as 1870s since the Meiji

restoration. This is one of the major reasons why Japanese organizations and banks have maintained their own business style but after the Japanese financial crisis they realized that they had to align and adopt their systems in line with the changing global business and financial trends in order to sustain and survive their own Japanese systems.

Bank 1's organizational resources include leadership resources which were similar among the combining banks A and B and was retained and reshuffled for Bank 1, knowledge capabilities derived from previous bank B's M&A activity; corporate culture resource, a combination of aggressive and not so aggressive business style led to a mono-culture somewhat of an aggressive nature and employees were reshuffled around business units based on their existing strengths. Some were laid-off in terms of early retirement, some voluntarily left and others were positioned in sister companies of Bank A and B. Bank 1's mono-culture presented an opportunity for the bank employees to amicably adjust to the new culture and continue working progressively with clients.

Bank 2's organizational resources were leadership, old management which was similar in the combining banks was retained and reshuffled; different corporate cultures combined to form a new culture based on a mix of previous bank corporate cultures and employees were reshuffled around different business units in the new bank; some were made redundant, given early retirement, positioned in sister subsidiaries, and some voluntarily retired. Bank 2 employees adjusted quickly to the new culture as the integration itself presented significant benefits to the employees, which they accepted.

Bank 3 and Bank 4 organizational resources i.e. leadership was different in styles among all the three combining banks, but it was retained and adopted into a criss-cross strategy in terms of leadership appointment for the new banks; corporate culture was different and adapted into a new corporate culture which was more business orientated but not so aggressive, and employees were reshuffled around business units based on their existing strengths, some were laid-off in terms of early retirement, some voluntarily left and others positioned in sister companies of the *Dai-ichi* and *Fuyo* groups. Bank 3 and 4, employees had to struggle for the first 2 to 3 years in order to

adapt to the new business culture. Initially, this did impair the synergies and value addition derived out of Bank 3 and 4 M&As.

Bank 5 in terms of resources adopted a slightly different strategy as leadership which was different in both the combining banks was removed and new management took over; in line with the banks initial strategy for the integration. The combining banks had a similar corporate culture, in-ward looking and conservative. Bank 5 developed a new culture, aggressive, more business like and open-minded. Bank 5 employees adjusted gradually, but well in time. Employees were either laid off in terms of early retirement and or left voluntarily. Based on inefficient management theory especially, when the management of the target company cannot replace their employees who are operating below their potential (Manne, 1965). This can be due to i) the firm is not operating at its full potential due to a gap in the vision when management pursuits for growth differ from shareholders desire to maximize wealth; and ii) the acquired may have better management experience than the target.

Combing banks	Culture Characteristics	Relatedness	New Bank New Culture
Bank A	Aggressive towards profitability	Different	Monoculture; aggressive yet business orientated; adapted overtime.
Bank B	Hard working; business style; gentleman orientated		
Bank C	Aristocratic and bureaucratic; 'elite' and 'luxurious' and often referred to as natural flow of business; has open-knowledge."	Different	New culture; no mono-culture; mix of both combining bank cultures. Adapted over time; some initial problems
Bank D	Aggressive, samurai-type and creative; small bank therefore, looking for clients 'hunt clients'		
Bank E		Different	New culture; confusion as constantly changing & 3 separate cultures; Difficult; adapted with time
Bank F			
Bank G			
Bank H	In ward looking; conservative	Similar	New Culture; Different from past. Aggressive and open-minded. Adapted/looking forward
Bank I	In ward looking; conservative		

Table 7.3 Cultural Relatedness among combining Japanese banks

The cross-analysis presented above in terms of pre-existing resources that were combined and carried forward to the new bank or deleted follow the argument that banks can gain competitive advantage if they possess certain kinds of skills or resources that can be transferred into the new market (Barney, 1991) thereby creating value by recombining the resources into new capabilities (Sirmon et. al., 2007). Furthermore, the findings of this research fall in line with Teece et. al.'s (1997) RBV that firms acquire, adapt and integrate internal and external resources, skills and functional competencies

to capitalize in a changing environment which fits in well with the Japanese mega-banks strategy.

The findings of this research in terms of employee lay-offs and shifting to sister companies are in line with the current Japanese banking literature. Prior to 1990s, in Japan unheard phases like downsizing in banking sector were unthinkable. Gradually, with a number of diversification strategies being introduced in the Japanese financial sector, started to include phrases like voluntarily retirement, secondment and even at times plain lay-offs. Moreover, lifetime employment became employment diversification and the seniority system changed to result-orientated, performance based. Bird (2002), suggest that restructuring among Japanese firms tend to adopt several measures that stopped short of outright lay-offs. The first was *shukko*, or dispatch of employees either temporarily or permanently to relate to companies. When firms exhausted their options for *shukko*, receiving companies become less willing and able to accept redundant employees, they turned to other methods of downsizing. Many women in secretarial positions were encouraged to retire and were subsequently replaced by soft-drink machines or temporary staff. A new element introduced into the Japanese management is that of flexi-time in time-keeping; the emphasis on self-help efforts, double-track ability development and employment recommendations in educational training and ability development or the promotion of a cafeteria plan in welfare program (Nikkeiren, 1995; p. 48-49, 55). Based on this research bank staff was placed in the new banks according to their specialized skills. This is contrary to the traditional Japanese literature whereby, in the past employees have rotated around the banks to equip them with a number of different traits rather than specialize in one area (Begg and Henning, 2008).

- **Physical Resources**

All Japanese mega-bank IT systems integration, borrowed the strengths of the combining banks in order to develop a new IT system for the new banks as shown in Table 7.4 which outlines the relatedness of the combining banks and types of IT systems combined.

Combining banks	IT Systems	Relatedness
Bank A	NEC system	Different
Bank B	IBM System	
Bank C	IBM Systems	Different
Bank D	Hitachi Systems	
Bank E	Fujitsu Systems IBM	Different
Bank F		
Bank G		
Bank H		Different
Bank I		

Table 7.4: IT systems relatedness among combining Japanese Banks

The Japanese mega-bank behaviour coincides with Morrow et. al.'s (2006) study. They explain that existing stocks of resources may create new product processes or technologies by providing a positive influence on organizational recovery. IT integration was one of the important aspects of the combining banks especially, as most of the banks were using old IT systems and not only systems were upgraded but also cost efficiency gains were incurred through sharing of 'physical inputs, information systems, databases or other similar means' (Berger, 2000; pp.7).

In the Japanese mega-bank branches were shut-down and reduced where there was an overlap and some were advanced with sophisticated distribution channels to make them more client user friendly. Most of the banks had an extensive network of about 500 domestic branches and anywhere from 2 to 50 overseas branches. After the mega-bank M&As, the number of branches were reduced gradually by about 30% within the first 3 to 4 years of the mega-bank M&As. As discussed by banking analysts, a gradual scale back on the branches allowed for the customers to get used to the new bank set-up and simultaneously, allow for bank employees to use new systems and to strategize based on business segment priorities. Brealey et. al. (2001) and Dettmer (1963) maintain that with closing of redundant branches, consolidation of systems, back office operations and payments takes place as banks are presented with an opportunity to streamline their operations and thus, make huge cost savings. A behaviour like this for the Japanese banks translated into huge amounts of cost savings which were then utilized for clearing off the non-performing loans of the banks.

Bank 3 and 4 sold off commercial bank buildings and Bank 5 disposed off housing estates in order to re-pay some of the public funds borrowed from the government. This fits in well where Moliterno and Wiersema (2007) maintain that organizational capacities create or modify the firm's resources and the decision to divest of strategically valuable resources occurs as a manifestation of the firm's efforts to achieve success. Resource divestment therefore, can act as an important firm level resource tool. The findings of this research take this argument a bit further by suggesting that the competitive advantage derived from selling off the physical assets have been utilized to pay off the bad loans inherited by the Japanese mega-banks.

7.4.2 New Resources

Japanese mega-banks hired new resources to increase the banking capacity and efficiency. This is supported by proposition 13d which presents the notion that the nature of the resource i.e. new resources are positively associated in drawing a competitive advantage and providing a swift means of organizational recovery. The new resources hired by Bank 1 include employees and legal services on an organizational level. Bank 2, 3 and 4 stressed on utilizing the existing resources from the combining banks to their full capacity. Some new staff resources were hired at graduate level to induct fresh blood and thoughts into the system. Bank 2 hired some M&A specialists from its securities company to facilitate the M&A process. Bank 5 placed significant stress on acquiring new resources by replacing old management; a new board of directors was hired from outside the banking sector, something perceived as new and unique to the Japanese mega-banks business as it circumvented around the western style of management. New staff was also hired, both part-time and full-time. In terms of physical resources, all banks hired some-kind IT specialists. Uhlenbruck et. al. (2007) discover that potential M&A benefits to the acquirer arise from new technologies and capabilities for firms pressured to keep up with the competitors. This research supports that competitive pressure requires firms to change their scope of resources to create new opportunities (Penrose, 1959).

7.4.3 Uniqueness

The uniqueness of the resources is another significant trait that provided a competitive advantage for the Japanese mega-banks. Bank 1 explains that it took advantage of the knowledge networks and experience gained from its previous M&A activities. Bank D, on the other hand, could not carry forward the experience from its previous M&A due to a short time gap between Bank 2 and its previous M&A. Bank D's employees also didn't have enough time to absorb and learn from the previous M&As and replicate it in the present M&A with Bank C. Bank D's behaviour sets in well with what Haunschild et. al. (1994) suggests that firms maybe unable to generate meaningful inferences from very recent M&As. M&As that take place swiftly one after the other does provide managers with enough time to carefully evaluate the M&A activities. Bank 1 behaviour is in line with the knowledge based view; that the outcome of an M&A is influenced by the degree to which the acquiring firm develops a capability specific to managing the M&A process (Haleblian and Finkelstein, 1999). Moreover, Haspeslagh and Jemison (1991) identify this knowledge-experience can be accumulated in both explicit forms; such as manuals, blueprints, information systems; and implicit forms; such as human memory. Eisenhardt and Martin (2000) define capabilities as involving tacit knowledge, that cannot be bought rather internally developed, obtained via M&As of institutions. It has suggested the linkages between accumulations of experience in prior M&As carried forward in making improvements in M&A performance as measured by financial variables or survival (Lubatkin 1987). Firms sometimes engage in multiple M&As mutually interrelated aimed at specific strategic targets (Schipper and Thompson; 1983). This in turn can create a strategic momentum that may impact the consolidating companies for several years (Amburgey and Miner, 1992) and create substantial value for its shareholders (Laamanen and Keil; 2008). Bank 2 did not show any signs of learning or carrying over their experience from their previous M&A activity which took place about 10 years back. This could be as many employees involved in the M&A activity may have left the bank or possibly not retained the knowledge from the past M&A activity. Therefore, time may play a significant factor in determining if certain skills and resources can be carried over.

Adopting a mono-culture is another unique resource adopted by Bank 1. The general premise was the ‘generation of a new corporate culture, whereby banks chose the best culture suitable for each business unit at the time of the merger keeping in mind ‘customers come first’. Staff placement based on the right person for the right job – based on their skills and experience, was another unique aspect adopted by the Japanese mega-banks. Bank 5’s unique resource is revamping the structure and introducing U.S. style governance structures. More interestingly, Bank 2 defined a strategic factor such as foreign exchange business as a unique trait. Consequently, strategic resources like regional business and forming strategic alliances with other regional banks is peculiar to Bank 5.

It has become evident that the strategic, organizational and physical characteristics of the combining banks play a dual role, as they not only add value in terms of their relatedness but also play a pivotal role as they maybe considered as resources adding value to the combining entities. The dual role of relatedness and resources can be ascribed to as a unique feature of this research adding to the strategic management and Japanese banking management literature.

7.5 Role of Regulatory Authorities

The role of regulatory authorities in facilitating the M&A activity is housed under different perceptions.

Bank 3 and 4 maintain that the Japanese government encouraged the Japanese institutions to increase its capital base and also clear its bad debts. Bank 2 also maintains that M&A activity received support from the government authorities as government initiated the consolidation but it was never ‘officially’ announced. Bank 5 explains that in the Japanese context; regulatory authorities are very powerful entities; many M&As are in a sense promoted by regulatory authorities. FSA tends to deregulate the banking sector, did prepare the M&A plan and was concerned over the management of the consolidation process which could have been handled in a much better manner. The M&A process was conducted by outside consultants not FSA. Bank 1 suggests that

Japanese over-banking problem existed for a long time but the government sorted this concern by restructuring. In order for Japanese Banks to survive global competition, Bank of Japan had requested Japanese banks to i) define a clear strategy; and ii) improve efficiency in operations and risk management (Rowley, 1998). Often it is maintained that there are two stages to the Japanese banking reforms, namely; i) government's rescue plan whereby, the government injected public funds into the ailing banks; and ii) the restructuring program itself, adopting financial integration of banks in terms of M&As (Defterios and Marchini, 1999). Banking industry needs to become stronger in profit taking and compete with global banking institutions.

7.6 Implications for Strategic Management and Japanese Banking Literature

Based on the theoretical model defined in chapter 4 as a result of the literature, the model is tested and prescribed in relation to the Japanese mega-banks, presented in chapter 6. The subsequent discussion revolves around table 7.6 and figure 7.1 which present the M&A strategies and rational for the Japanese mega-bank M&As, while discussing the importance and specific characteristics that have been adapted from figure 4.3. Therefore, these two sets are critical in contributing and advancing the present theory on strategic management and Japanese business and banks. The research aims to bridge the gaps in M&A literature by proposing the competitive advantage realized at a planning stage for private commercial Japanese banks based on the two research questions discussed in section 3.5. The results, as identified in table 7.6 and figure 7.1 suggest that the Japanese mega-bank M&As not only act as a source of deriving a competitive advantage for the combining Japanese mega-banks but are acting as a support mechanism in 'pulling' the Japanese banking sector out of the crisis mode. This is explained by the strategic inputs (level of integration, strategic relatedness and types of resources) and strategic outputs characteristics of the combining banks.

More specifically mega-banks have derived a competitive advantage in terms of costs saving, financial and managerial synergies, diversified range of products and services. The ranking in terms of deriving a competitive advantage among the Japanese mega-

banks is placed in the following order; Bank 1, Bank 2, Bank 3 and 4 and Bank 5. This study presents the notion that with the change in traditional Japanese banking practises, the era of 2000 is based on diversification i.e. M&A strategy in terms of strategic fit, and types of resource but also sources of resources are equally important, where the resources are derived from.

In terms of motivational level determinants this research enhances the understanding of current literature by suggesting that diversification can take place to clear the bad loans profile of banks as it appears has happened in the case of Japanese mega-banks consolidation. Diversification is also subjected to provide organizational recovery and the recovery of the Japanese banking sector caused due to the burst of the bubble economy which caused yen 75 trillion worth of non-performing loans.

This research advances the resource based view, by proposing that not only specific industry level resources i.e. organization, physical, *keiretsu*, financial and strategic add value to the Japanese banks through this M&A diversification strategy but also resources in terms of their combination potential i.e. relatedness add value for the combining banks. Moreover, these banks display a unique quality the 'dual role' that strategic characteristics of the banks markets and products and services not only act as a combination potential but also act as resources. Therefore, not only the types of resources play an enhanced role in the value addition but their relatedness is considered equally important. The sources of resources are also considered critical i.e. combining, new and their uniqueness in terms of adding a competitive advantage and organizational recovery for the banking sector in Japan. Sometimes banks are capable of not only utilizing and combining their existing resources strategically but they can reshuffle, delete, or create new resources when combining the existing resources from within the consolidating banks.

Extent Literature	Contribution to Literature	
Diversification	Diversification in order to resolve the non-performing loans and provide organizational recovery to the Japanese banking sector	
Strategic Management & RBV	Resources	Organizational: <i>keiretsu</i> clients; knowledge from pervious M&As; leadership; culture, senior management placement; employees
		Financial: Cross-shareholdings & Capital markets
		Physical: IT systems; branch network; bank office buildings & housing.
		Strategic: Products & Services and Markets
	Resource Relatedness	Organizational: Leadership style, culture Physical: IT systems
	Resource Sources	Combining, New, Unique Combining Resources include; modified to form new resources retained reshuffled reduced downsized Strengthened upgraded voluntarily laid off shifted to sister company permanently removed to delete permanently removed i.e sold off carried forward adapted to form new adapted to fully utilize

Table 7.6 Contribution to Literature derived from the Japanese Mega-Bank M&As

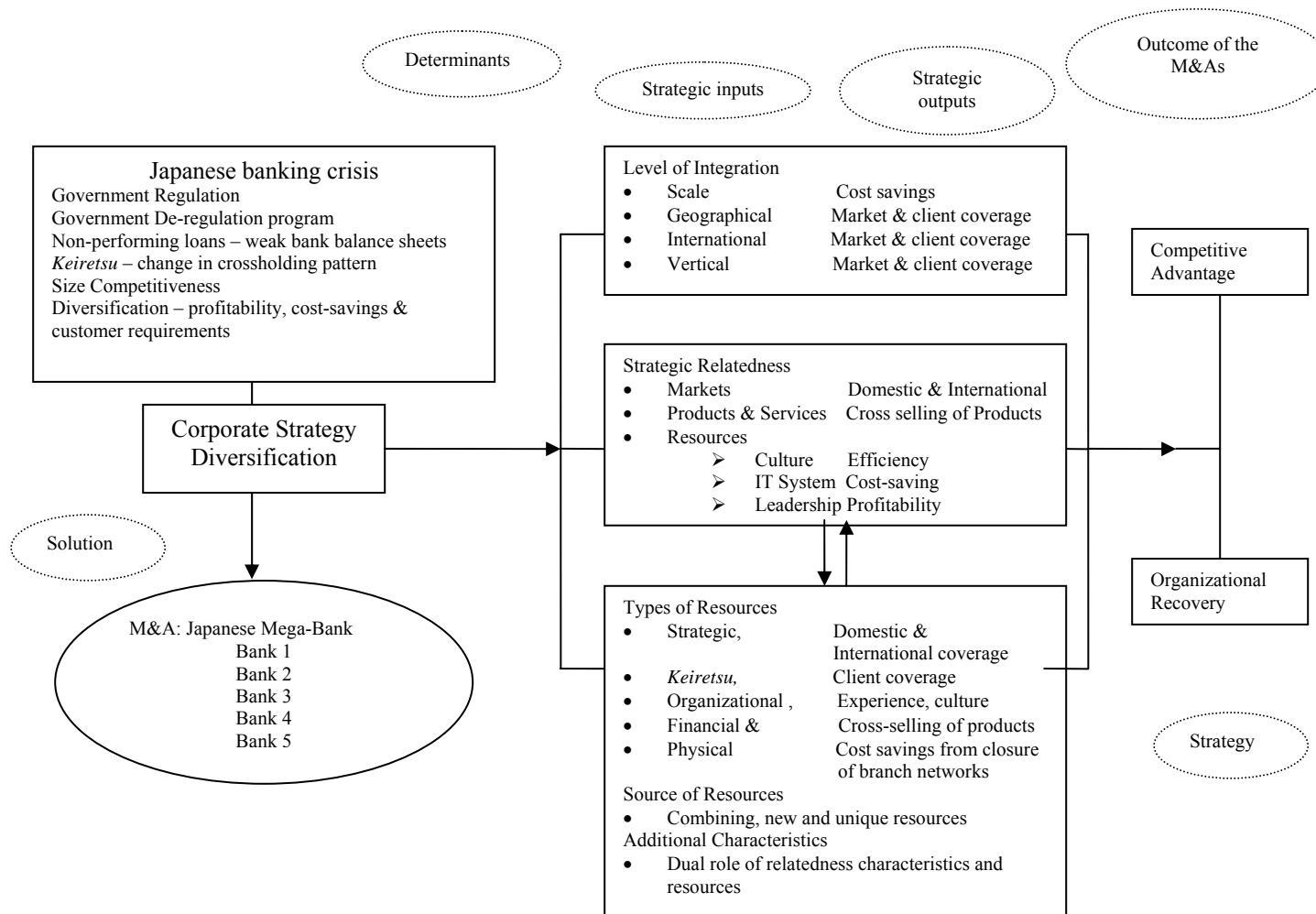


Figure 7.1 Conceptual Model based on the Japanese mega-bank M&As; (derived from theory and tested in this study).

It is postulated that when companies are articulating and fine-tuning acquisition-specific tools they may learn and pick-up the relevant tools in better integrating and conducting the implementation process for the said M&A activity. Location acts as a key competitive factor in terms of cost advantage as it rationalizes branch networks in order to create value. In general, in-market M&As tend to attain cost efficiencies due to economies of scale whereas, out-market M&As tend to rely more on cross-selling opportunities and economies of scope as cost-efficiencies derivable from the rationalization of the two branch networks maybe available. Moreover, many studies suggest that M&As tend to be successful when combining entities cover a diversified geographical region. Therefore, this research would add to the understanding of the value creation literature from a pre-merger combining stage to create value. Products and services were similar but banks wanted to further strengthen their products and services range and also different with an eye to secure some characteristics they are missing from the existing banks. This follows suit that linkages drawn between the acquisition of skills and product markets and technologies of the combining organizations overlap. This aids in our understanding on the diversification theory which suggests that in related mergers higher return is expected than unrelated M&As, due to ‘more contacts and overlap between firms’ value chain, resulting in higher potential for operational synergies’ (Palich et. al. 2000).

The research also builds our understanding of how the Japanese banking sector, has distanced itself from the traditional banking culture since the de-regulation, the change in terms of financial cross-shareholdings, introducing out-side directors, breaking away gradually from the *amakudari* system and the long term employment and seniority wage system. The research also suggests that while a number of changes have taken place both on a macroeconomic and industry banking level, the traditional relationship among the banks and affiliated *keiretsu*’s continues to be maintained and still derive resource benefits and other profit enhancing variables.

Most importantly, in the context of Japan the underlying notion from this research seems to be the mindset change among the Japanese regulators, bank management,

employees and clients. The M&A activity, on the premise of the banking crisis and burst of the bubble economy has provided an impetus for the five mega-banks in perceiving this diversification stance as a positive change, thereby, reviving the Japanese banking system, and economy. Regulators were prepared to implement quick and drastic changes in terms of laws, de-regulations and facilitating a positive change; bank management, towing the line of the regulators, changed their mindset from traditional growth for banks into adopting more profitable techniques for the banks, employees became aggressive in terms of breaking free from the traditional long term employment and compensated based on their performance rather than age and finally the clients started to raise their voice in terms of better and more diversified products and services and leveraging higher profit seeking measures. In a nutshell, table 7.5 (column 3) proposes and builds on the understanding of the changes taking place in the Japanese business and banking world and its importance in providing corporate recovery to the banking sector, deciphered through the findings of this research in chapter 6 as already discussed by Mendenhall and Pudenko (2007; column 1 & 2).

<i>Anglo-Saxon Management Model</i>	<i>Japanese Management Model</i>	Support Rejection of this Research findings
<i>Market regulation</i>	<i>Governmental guidance</i>	Liberalized based on market regulation
<i>Shareholder Interests</i>	<i>Employee's Interests</i>	Shareholders interests as well as management interests
<i>Capital Markets</i>	<i>Bank loans</i>	Capital Markets (increase) Bank Loans (decline)
<i>Constant Profits</i>	<i>Long-term market growth</i>	Profits
<i>Differentiation from Competitors</i>	<i>Imitation of best practices</i>	Diversification; mix of differentiation from competitors & imitation of best practices
<i>Embracing Radical Change</i>	<i>Incremental steps towards change</i>	Change gradual pace
<i>Open, global, geo-centric mindset</i>	<i>Insular, domestic, ethnocentric mindset</i>	Open, diversified, aggressive
<i>Flexible trans-national alliances and supply chain</i>	<i>Rigid, national keiretsu structures</i>	Break away from traditional business practices; unwinding in cross-shareholdings but still maintain keiretsu affiliations in terms of clients and financial resources
<i>Proactive top-management</i>	<i>Delegation of decision making to middle management</i>	Gradual change based on a mix of senior management, middle management, clients requirements and market trends
<i>Transparency in corporate governance and financial markets</i>	<i>Behind closed doors insider system of management and control</i>	Openness, gradual change towards transparency based on new regulatory and accounting laws
<i>Clear accountability</i>	<i>Vague sharing of responsibility across people and networks</i>	Change towards accountability and staff positioned across units based on expertise & skills
<i>Flexible labor markets</i>	<i>Life-long or long term employment</i>	Flexible change being integrated and widely acknowledged
<i>Rewards based on performance</i>	<i>Rewards based on seniority</i>	Based on performance and market based
<i>Originality, creativity, individuality, and benefits of diversity</i>	<i>Homogeneity, status quo, conformity and collectivism</i>	Similar with gradual change, open and diverse

Table 7.5 Mendenhall and Pudenko (2007) conceptual model tested on Japanese mega-bank M&As.

Chapter 8

Implications and Limitations

This section discusses i) implications; ii) future research and iii) limitations associated with the research.

8.1 Implications

The following section discusses the implications on the Japanese banking and financial sector; policy maker's; clients and the international financial community.

8.1.2 Implications of the Japanese Mega-Bank M&As

With the so many changes taking place within the Japanese banking sector, it has prompted a desire among the banking and policy masterminds to carry on with this progressive diversification tool of M&As and other such alliances.

More consolidation is required on a smaller scale with regards to regional banks, trust banks and shinkin banks, as these financial institutions still have many problems in terms of operational efficiency. More restructuring of these institutions and post bank will shape the market. Post bank is the largest retail network and is a 'scary competition for other banks as it is one of the world's largest retail bank.' This is a big change in the Japanese banking landscape with the Japan post being privatized over the past three years. In terms of retail banking the sector had gained strength and Kanto and Kansai markets are well developed however, other areas need more growth avenues.

Mega banks are also pursuing overseas business, especially in Asia-Pacific region. BTMU invested Yen 90 billion in Morgan Stanley. This transaction was possible, because it has a strong capital base, repeated history of M&As; frantically cutting costs; cutting operations, branch offices and rebuilding capital base. Now cross-border M&As have also started taking place (Standards and Poor Analyst). However, at the same time, no high growth measures may be taken due to the low growth in population increase.

8.1.3 Implications for Japanese Policy Makers

Implications for Japanese policy makers fall in two previews; i) with regards to the mega-banks M&A activity, much has been learnt for policy makers as they were liberalizing the banking sector and also introducing new reform measures. More work needs to be done towards regional bank consolidation and other financial institutions integrations processes; and ii) more enhanced measures need to be provided for Japanese banks cross-border M&As and also foreign companies business in Japan with regards to the financial sector. Begg (2008) maintains that with revised versions of the accounting practices in Japan, it has opened up doors for interest by foreign entities in Japanese assets, giving Japanese companies more room and alternatives in diversifying their operations as well as divest their ill-performing units and expand the scope for Japanese banks for cross-border M&As. Other lessons learnt include; proactive and timely regulatory measures adopted and changes in traditional Japanese business practices.

8.1.4 Implications for Japanese banking and financial sector and Japanese Economy

The banking analysts in Japan maintain that a wide range of benefits and prospectus have been provided to the Japanese banking and financial system and Japanese economy. The 1990s was classified as the 'lost decade' as banks were suffering. After the M&A activity, with three mega-banks and one super-regional bank remaining the banking system has become more efficient and so has the financial system. It seems the Japanese mega-banks have achieved competitiveness, globally and if the M&As had not taken place then some banks would have not survived. Starting 2006 many banks have cleared NPLs and are becoming more active in lending. 'Public has been paid and people feel recovery is coming.'

New banks have been created such as 7 bank; Aeon Bank, Jibun Bank mobile company; KDDI. It is however; premature to say where the sector is headed as more work is required in the restructuring of the financial sector.

What happened in Japan towards the end of the 1990s, has transpired in the global economy now where all the banking institutions in the U.S and Europe are facing massive losses due to the deterioration of assets, decline in equity without having external equity, therefore, problems have trickled down into the banking system as well as the industrial sector. With the M&A activity in Japan, the financial sector has been on a road to recovery. According to banking analyst 'top management wanted to do everything and in later stages all seems to be going well.'

8.1.5 Implications for the Bank Clients

The implications for the clients of the combining banks have been based on how they perceive the M&A activity and how they want their banks to grow.

Japanese mega-bank customers have positioned different views on the M&A activity; some have accepted immediately as the new banks will offer them increased business coverage, and clients anticipated a sound and safe banking system based on global, domestic and customer basis; some like Bank 1 customers were surprised in the beginning but then with the new corporate colour; the difference between the two banks got adjusted. Also as the integration was smooth between the 2 banks, customers accepted the business style. With some mega-banks some customers were unhappy because restructuring of business in the short period while closing branches especially, duplicate branches, and consolidating branches was disliked by some customers.

Bank 3 and 4 have had to maintain its branch network as customers prefer to be in close physical proximity of the bank, in order to deposit cash and also meet with financial advisor on a regular basis. Bank offices prefer near corporate clients in order to meet them on a regular basis.

Bank 2's corporate clients were satisfied with the stable financial sector, and perceived the M&A to have brought about advantages for the corporate as the customers were facing difficulty in raising loans from banks. Sound financial system decreased problems for customers. Small sized customers were making complaints as the quality of service declined as they used to have better services before in terms of business relationship in particular regions.

Banking analysts often maintain that for customers this M&A banking activity was ripe at providing convenience; more networks; securities firms; and products such as mutual funds.

8.1.6 Implications for the International banking community & M&A Specialists

The research on the revival of the Japanese banking sector, through the diversification of mega-banks presents a smorgasbord of solutions, challenges, and restructuring mechanism for the international community to learn from and thereby, avoid such crisis within their own barriers. It presents confidence to the banking sectors, globally, that if a tradition bound economy stemming from the Meiji era can accommodate and make amends to its traditional business philosophies especially, those dwelling on a heavily regulated banking sector cushioned and protected by the Ministry of Finance; *amkudari* business practices, long term employment and seniority waged based system, and relational main banking and *keiretsu* affiliations, than any banking sector can opt for a change in their systems in order to produce a sound and stable financial and banking system for their own economies. The learning imparted through the change envisaged in the Japanese banking system is therefore, more fundamental as it is unwinding gradually from its traditional roles, and this gradually unwinding provides a closer evaluation to comprehend and streamline a better banking system. Moreover, the motivations, relatedness and resources will provide credible insights when the managers are involved in other M&A activities seeking for institutional recovery and competitive advantage.

8.2 Future Research

This section is divided into two parts i) future research strands based on Japan specific research and cross-border research; and ii) limitations associated with this research.

8.2.1 Japan specific M&A research

- Replicate this study in other financial sectors and see if this study adds value to the understanding on the Regional banks, Securities and Insurance sector M&A activity versus the banking sector M&A activity and what implications it presents for the Japanese economy? This is of particular importance as it will enable a healthy banking sector and ensure its sustainability.
- Research on the change in the relationship between the *keiretsu* and banks as an outcome of the M&A in Japan, needs to be studied.
- Research on bank holding companies and its implication need to be studied more specifically with regards to the banking and non-banking sector and what advantages it may provide with regards to the revival of the Japanese economy after the financial and banking crisis?
- Research on risk management and how it was positioned during the M&A activity, as this provides the basis for the balance sheet recovery in the banking sector and how it aided with the Japanese banks in their banking sector recovery? What lessons were learnt and how the other banking structures and Japan learn from this?
- A number of M&As took place in a short span of time, the distance between each M&A and the speed of the integration and its affects on the combining banks and the knowledge carried over to the next M&A activity may be considered further.

- The Japanese banking sector has traditionally, been considered to be conservative and regulated, with the deregulation process, a number of changes have taken place including encouraging the role of foreign investors. Research should be conducted on the nationalized banks and later revived on the behest of the foreign investors, what mechanism and resources provided a turn around for those banks and how it compares to the banks owned by Japanese investors.

8.2.2 Cross-border M&A research

- This research to be tested for the overseas banking sectors and other financial sector M&As, especially, U.S. and European M&As especially those economies undergoing banking sector recovery after a financial crisis. This research would be of fundamental importance as it will provide a learning curve for the international banking community, in order to avoid banking crisis; as has been envisaged lately, in the U.S. and Europe.
- Research on the restructuring of other banking centres in order to overcome a financial crisis and compared with the Japanese banking sector in overcoming the financial crisis.
- Discuss resources based on cross-border M&As from an internal and external resources point of view and compare with other banking sector M&As resource profile?
- A comparison of domestic and international bank resources; similarities and differences and how markets can take advantage to better perform the subsequent M&A integration that take on board?

8.3 Limitations

While conducting this study a number of limitations have been encountered as discussed below:

- The sample size was limited to five banks (for the purpose of the case study only four banks were discussed as Bank 3 and Bank 4 were established from the same banks), due to the size of the banking sector in Japan.
- The mega-banks were four and the fifth bank Bank is a super-regional bank, therefore, the sample size is restricted due to the nature of the Japanese private banks. The variation in the types of M&As is limited.
- This study focuses on the single industry study, focusing on Japanese mega-banks M&As. Its application in general terms for the other banking segments i.e. regional banks, trusts banks and so on and financial segments i.e. insurance and securities need to be defined.
- The M&As took place between 1999 and 2005, therefore, by conducting this research in 2008, maintains that a number of knowledge resources i.e. staff who were responsible for the M&A consolidation, were hard to get hold off. Therefore, in terms of data collection, some information may have been limited. Moreover, as the M&As took place a few years back, it was hard for some staff to remember the exact details of the M&A activity.
- Not all senior management interviewed were the direct decision makers and strategy initiators and therefore, could not capture the true nature of what transpired in the Japanese banking sector and measures that aided towards its organizational recovery.

- Only eight interviews were conducted; with five interviews on the banks and three from external consultants, therefore, it limits the information. This was due to the difficulty of getting consent from banking analysts to participate in the study and also the time constraints. However, to overcome this constraint to some extent, four discussions that transpired in 2006 on the Japanese banking sector were also included in this research.
- Based on the limited scope of the master's thesis in term's of word count the details of the M&A activity and other consolidation measures in the formation of Shinsei Bank and Azora Bank and other banking segments recently spurring growth in Japan have not been discussed in this research. Moreover the literature review does not cover the M&A lifecycle stage and the case studies do not discuss the organizational structure as it was out of the scope of this research.

Chapter 9

Conclusions

The thesis has been a reflection of the M&A motivations, strategies and resources providing a competitive advantage and organizational recovery for the Japanese mega-banks. The thesis provides a platform on how M&As work by analyzing the corporate strategy, M&As, strategic management and Japanese business and banking literature. On the other hand, the Japanese financial crisis and non-performing loan profile of major Japanese banks was identified as a problem, based on which the restructuring drive i.e. M&As were initiated for the Japanese mega-banks. A conceptual model was derived from the literature, tested through this research and adapted in light of the Japanese mega-bank M&A strategies based on the findings of this research. This research makes it imperative for us to comprehend what transpired in the Japanese financial sector in terms of financial consolidation, what were the benefits and problems, how they were handled and what can be learnt from this in order to prepare practitioners for future M&As not only in Japan but also globally. How products and services can be aligned to facilitate the global demands of the diversifying client requirements, especially, in Japan where traditionally they have been comfortable with savings and deposits and plain loans. Therefore, this thesis provide a means of advancing our understanding on the M&A concept in providing competitive advantage and organizational recovery for Japanese banking sector.

The story of the Japanese mega-banks dates back to late 1990s when the banking landscape started to present gaps within the Japanese financial system. The burst of the bubble economy presented Yen 75 trillion of non-performing loans, alongside reduction in businesses from their major clients due to the change in the cross-holding pattern and clients raising funds through capital markets, overcrowding in the banking sector, banks losing guaranteed profits and niche markets. This allowed the Japanese regulators to adopt diversification strategies thereby, as a means of reducing banking risk and also identifying multiple opportunities for their ‘come back’ and corporate revival.

M&As have been taking place in Japan, at different stages for different reasons, since 1927. As discussed by Rose and Ito (2005) ‘the M&A activity is a resurgence of the past practices’ and with the banking crisis, an influx of M&As took centre stage, which is ‘considered productive for the up-gradation of the banking sector’ (banking analyst).

Berg and Henning, (2008, pp. 50) maintain that ‘the domestic M&A boom is continuing unabated as a growing number of firms, armed with strong balance sheets and bulging war chests are expanding aggressively in the face of mounting pressure from investors to boost corporate value. Economic and social trend like globalization and falling birth-rates are also adding pressure.’

Broadly speaking, banking analysts interviewed in Japan have discussed the rationale behind the M&As from different perspectives; domestic banking level; i) economic and financial downturn at the end of 1990s suggested that the Japanese banking sector consider restructuring and making the sector universally competitive and providing banking sector recovery; ii) banking industry structure is the focus with a comparison of the city banks, regional banks and the Japanese postal banking system; and iii) deregulation imposed based on the big bang in 1996, allowed Japanese banks to rely less on the government and make decisions based on deriving profitability and market share thereby, blurring the barriers between the banking, insurance and securities industries including selling of bonds; domestic industry level; i) comparison of the Japanese banking sector with the Japanese manufacturing sector and its development dating back to world war II; ii) the effect on the banking sector due to the change in the traditional cross-holding pattern among Japanese companies, i.e *keiretsu* groups; and global level; i) comparison of the domestic banking M&A activity versus international M&As in the banking industry specifically, with regards to the US and European M&As. The government instigated some banking and M&A laws imperative for banks and non-banking sector to get involved in the M&A activity.

With the massive diversification strategy setting its mark in the heart of the Japanese banking sector; not only the M&As resulted in a competitive advantage for Japanese mega-banks but also provided a bail-out plan in terms of the organizational recovery for the Japanese financial as well as the banking sector. As time progressed, from 2000 onwards, Japanese banks became more confident to enhance their business profiles and better utilize their resources but also take massive steps of entering the cross-border M&A markets. The motivations included government de-regulation; NPLs of banks; over-crowding in the banking industry; and size and diversification streams; capture

markets, profitability; aligning with the changing needs of the Japanese clients. Complementarily relatedness existed among the combining banks strategic assets; markets, products and services; organizational traits, i.e. leadership style and culture were different among the combining banks and physical traits such as IT systems integration. As highlighted in table 7.6, resources were diverse. Their source in terms of combining resources, new resources and uniqueness was also played a fundamental role and finally the dual role of relatedness factors provided a competitive advantage for the Japanese mega-banks.

This research has tried to identify under what conditions and circumstances, what types of resources and strategic relatedness aids with competitive advantage in Japanese banking industry. M&As like any other diversification tool can facilitate or destroy value and composition for the banks undergoing this strategy, based on the conditions under which they aim to consolidate. It has used the platform of qualitative research (chapter 4), based on a triangulation approach of case study and multi-case study style to present the findings of the M&A activity, which only this methodology could do justice based on its nature of portraying the activity as and how and when it takes place can capture the true activity that transpired among the banks integration at a planning stage. Based on diverse categories identified through the literature review (chapter 3) on strategic management, diversification, resource based view, and Japanese banking literature; the benefits, and challenges discussed; the background on the banking and M&A activity in Japan (Chapter 2); and the case studies and cross-analysis with a discussion on theory building from this research (chapter 6 and 7) provide monumental explanations into the current domains of M&As and banking sector in Japan, thereby building on the preceding research evidence. The strategic inputs yield various strategic outputs as highlighted in figure 7.1 to provide a competitive advantage and organizational recovery to the banking sector activity. Moreover, the limitations and future research associated with this research are highlighted in chapter 8. This research has significant valuable inputs on resource driven M&As, defining methodologies that should be adopted when choosing the M&A strategy to close resource gaps. This research also outlines a proposition for managers undertaking an M&A strategy to learn from the Japanese banking experience and implement that in other banking

consolidation activities; i) gaining insights as to why Japanese banks engaged in this M&A consolidation activity; ii) to highlight the problems of the Japanese financial system, with particular emphasis on the bursting of the bubble economy, regulatory and macroeconomic problems, and the bad loans situation faced by Japanese banks; iii) understanding what kinds of strategic relatedness existed between the combining banks, and what resources played important roles in achieving a competitive advantage for the banks; iv) to develop linkages between strategic relatedness, resources (strategic inputs and strategic outputs) and competitive advantage for the newly combined banks.

An underlying implication arising throughout the course of research of this study was that diversification was the key to the Japanese financial sector problem. Implementing a change may be considered a step forward in the mind set of Japanese regulators but also banking management. What is most impressive is the recent break Japanese mega-banks have been making in the global domains of the international financial sector, which would have not been possible if the Japanese mega-banks had not gone through this M&A drive. Japanese mega-banks have learnt from their mistakes and therefore, have not only been able to escape from the negative impact of the international banking community which has been in a state of perils, on the helms of sub-prime losses and major investment banks failures; i.e. Bear Sterns, Lehman Brother and Merrill Lynch but the Japanese banks have been able to enter alliances with; SMBC and BTMU have entered with Barclays and Morgan Stanley, respectively. What other banking segments have to learn from the recent M&A wave of the Japanese mega-banks and what the international banking arena picks up from the lessons learnt from the Japanese banking crisis are yet to be seen.

This research is timely in providing insights for the banking sector as a whole, when in 2008, the global banking scenario is mimicking what transpired in the Japanese banking sector late 1990s. Now that the mega-banks have been stabilized in the Japanese banking sector more and more attention is being placed on the diversification of regional banks which seek more substantial diversification opportunities. In sum, restructuring has been good for the Japanese economy, its financial system and banking system.

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APPENDIX

Appendix 1

Appendix Table 1. Chronology of Events Concerning the Japanese Banking Sector

Year	Month	Events
1991	June	<ul style="list-style-type: none"> A subcommittee of the Financial System Research Council to the Finance Minister released its final report on deregulating and globalizing Japan's financial system, including recommendations to permit banks and securities houses to enter into each other's businesses through subsidiaries.
	July	<ul style="list-style-type: none"> The Bank of Japan (BOJ) began monetary easing by reducing the official discount rate from 6.0 percent (set in August 1990), the highest level since 1981, to 5.5 percent
	November	<ul style="list-style-type: none"> Interest rates liberalized for time deposits of 3 million yen and over.
	December	<ul style="list-style-type: none"> The government decided to lift the cap on bank loans related to real estate (introduced in April 1990) as of January 1, 1992.
1992	June	<ul style="list-style-type: none"> The Diet approved laws related to the reform of the financial system, lowering barriers between banks and security firms.
	August	<ul style="list-style-type: none"> The Ministry of Finance (MOF) announced new guidelines—"The Present Guidelines for Administrative Management for Banking Sectors"—to help calm anxiety over bank NPL problems.
	October	<ul style="list-style-type: none"> The MOF estimated the total outstanding NPLs of the largest 21 banks (city banks, long-term credit banks and trust banks) to be 12.3 trillion yen as of September.
1993	January	<ul style="list-style-type: none"> The Cooperative Credit Purchase Company (CCPC), established by commercial banks to purchase their bad loans at a discount, commenced operation.
	February	<ul style="list-style-type: none"> The MOF requested private financial institutions to expand loans to SMEs at lower interest rates.
	June	<ul style="list-style-type: none"> Interest rates on time deposits completely liberalized.
1994	April	<ul style="list-style-type: none"> The government decided on liberalization of non-time deposits including the postal savings to be effective in October.
	December	<ul style="list-style-type: none"> The BOJ, private financial institutions, and the Tokyo Metropolitan Government announced an agreement to establish a new bank, Tokyo Kyodo Bank (in March 1995), to take over the assets and liabilities of Tokyo Kyowa Credit Association and Anzen Credit Association.
1995	March	<ul style="list-style-type: none"> Tokyo Kyodo Bank established, which later became the Resolution and Collection Bank to assume the operations of failed credit cooperatives and, from September 1996, other failed financial institutions.
	June	<ul style="list-style-type: none"> The MOF announced a five-year package addressing commercial banks' balance sheet problem—the Deposit Insurance Corporation (DIC) would ensure all deposits in troubled banks to be honored and, within five years, a framework for financial stability involving greater self-responsibility for depositors established. A Financial System Stabilization Committee set up.
	July	<ul style="list-style-type: none"> The Tokyo Metropolitan Government ordered Cosmo Credit Cooperative to suspend operations involving new loans and deposits.
	August	<ul style="list-style-type: none"> The Osaka Prefectural Government ordered Kizu Credit Cooperative to suspend operations. The BOJ announced a plan for the liquidation of Hyogo Bank and the establishment of a new bank, Midori Bank.
	September	<ul style="list-style-type: none"> The Financial System Stabilization Committee of the Financial System Research Council, an advisory committee of the MOF, released an interim report of measures facilitating the early settlement of NPLs of financial institutions.
	December	<ul style="list-style-type: none"> The Cabinet approved measures to resolve the <i>Jusen</i> problem by injecting 685 billion yen. The Financial System Research Council submitted its report on "Measures for the Maintenance of Stability in the Financial System" to the Finance Minister. The MOF announced "Measures to improve bank inspection and supervision."
1996	March	<ul style="list-style-type: none"> The MOF and BOJ announced a plan to dispose of Taiheiyō Bank. The basic deposit insurance rate raised to 0.048 percent.

	June	<ul style="list-style-type: none"> The Diet passed six financial laws, to establish the Housing Loan Administration Corporation (HLAC), strengthen the Deposit Insurance Corporation (DIC) function, and introduce prompt corrective action to ensure the sound management of financial institutions. The additional deposit insurance rate, for the newly established special fund, set to 0.036 percent by a Cabinet ordinance.
	July	<ul style="list-style-type: none"> The DIC created the HLAC to resolve the <i>Jusen</i> problem.
	November	<ul style="list-style-type: none"> The Prime Minister announced a five-year plan for financial system deregulation, the so-called “Financial Big Bang.” The MOF ordered Hanwa Bank to suspend operations.
1997	March	<ul style="list-style-type: none"> Hokkaido Takushoku and Hokkaido Banks announced their merger plan. Nippon Credit Bank presented a substantial restructuring plan.
	June	<ul style="list-style-type: none"> The Diet passed changes in the Bank of Japan Law to strengthen its independence and the transparency of the policy decision-making process. The Diet passed changes in the Anti-Monopoly Law to lift the ban on pure holding companies. The Diet passed a law establishing the Financial Supervisory Agency.
	October	<ul style="list-style-type: none"> Kyoto Kyoei Bank announced its liquidation plan.
	November	<ul style="list-style-type: none"> Sanyo Securities applied to the courts for legal restructuring procedures. Hokkaido Takushoku Bank announced its inability to continue business operations and the transfer of its operations in Hokkaido to Hokuyo Bank. Yamaichi Securities announced closure of its business. Tokuyo City Bank announced its closure and the transfer of its operations to other regional banks.
	December	<ul style="list-style-type: none"> The Diet passed two laws concerning holding companies in the financial sector. The Diet passed the revised Deposit Insurance Law, giving the DIC the right to cover loan losses of merging banks.
1998	February	<ul style="list-style-type: none"> The Diet passed two finance-related laws, which enabled the government to use 30 trillion yen of public money to bail out banks and protect depositors.
	March	<ul style="list-style-type: none"> Twenty-one banks applied for public capital injections, virtually all of which were fully approved by the Financial Crisis Management Committee.
	April	<ul style="list-style-type: none"> The new Bank of Japan Law and the new Foreign Exchange Control Law took effect.
	May	<ul style="list-style-type: none"> Hanshin Bank announced a merger with Midori Bank as of April 1999.
	June	<ul style="list-style-type: none"> The Diet passed four bills to implement “Financial Big Bang” reforms. The Financial Supervisory Agency created, taking over the functions of supervision and inspection of the financial system from the MOF. Long-Term Credit Bank of Japan announced a merger with Sumitomo Trust Bank as of April 1999. (By September, it was clear that the merger would not take place.)
	August	<ul style="list-style-type: none"> Long-Term Credit Bank announced substantial restructuring measures.
	September	<ul style="list-style-type: none"> Nippon Leasing Corporation, an affiliate of Long-Term Credit Bank, applied for the Corporate Reorganization Law with record high liabilities in the post-war era. Tokai and Asahi Banks announced a business tie-up.
	October	<ul style="list-style-type: none"> Long-Term Credit Bank of Japan voluntarily taken over by public administrators for temporary nationalization. The Diet passed eight bills to revive the banking system, creating a Financial Reconstruction Commission to oversee the process and to take over responsibility for financial regulation and planning from the MOF as from January 2000 and allowing the government to inject capital into banks on request even if they are solvent. The Diet adopted the second FY1998 supplementary budget, thereby providing government loan guarantees amounting to 43 trillion yen in total—replacing what remained from the previous 13 trillion yen—on BOJ loans to the DIC to implement bank recapitalization.
	November	<ul style="list-style-type: none"> Fuji and Daiichi Kangyo Banks announced a tie-up in the field of trust banking by setting up a new trust bank to take over the operations of Yasuda Trust Bank.

	December	<ul style="list-style-type: none"> A package of laws for the “Financial Big Bang” reform took effect. The government decided to place Nippon Credit Bank under temporary nationalization. The Financial Reconstruction Commission (FRC) established as a parent body of the Financial Supervisory Agency, taking over oversight of the financial industry until the end of FY2000. Hakuo Yanagisawa appointed as the first FRC Commissioner.
1999	January	<ul style="list-style-type: none"> The FRC published its basic operating policies. Mitsui Trust and Chuo Trust Banks announced their merger as of April 2000.
	March	<ul style="list-style-type: none"> The FRC decided to inject about 7.5 trillion yen in new capital into 15 major banks.
	April	<ul style="list-style-type: none"> The Resolution and Collection Corporation (RCC) formed, under the ownership of the DIC, through merging the Resolution and Collection Bank with the HLAC. The Financial Supervisory Agency released its final report of the working group on the new financial inspection manual. The FRC decided to place the operation and assets of Kokumin Bank under financial reorganization administration.
	May	<ul style="list-style-type: none"> Osaka and Kinki Banks announced their intention to merge as of April 2000. Kofuku Bank applied to the Financial Supervisory Agency for voluntary closure of business after the agency applied the prompt corrective action clauses for the first time.
	June	<ul style="list-style-type: none"> The Tokyo Court formally declared Yamaichi Securities to be bankrupt. The FRC released a basic guideline for capital injections into regional banks, aiming at a capital adequacy ratio of at least 8 percent. The FRC decided to place the operation and assets of Tokyo Sowa Bank under financial reorganization administration. The Financial Supervisory Agency decided to apply the prompt corrective action clause to Namihaya Bank.
	August	<ul style="list-style-type: none"> The Diet passed the Special Law for Industry Revitalization. The FRC decided to place the operation and assets of Namihaya Bank under financial administration. Industrial Bank of Japan, Daiichi Kangyo and Fuji Banks announced joint establishment of a holding company in the fall of 2000 and reorganization of their businesses from spring 2002.
	September	<ul style="list-style-type: none"> The FRC decided to sell Long-Term Credit Bank, still under public management, to an international group of financial institutions led by Ripplewood Holdings. The sale concluded in March 2000.
	October	<ul style="list-style-type: none"> Michio Ochi appointed as FRC Commissioner. Tokai and Asahi Banks announced their intention to speed up their merger and to set up a holding company in October 2001. Sumitomo and Sakura Banks announced their intention to merge by April 2002.
2000	February	<ul style="list-style-type: none"> Teiichi Tanigaki appointed as FRC Commissioner.
	March	<ul style="list-style-type: none"> Sanwa, Tokai and Asahi Banks announced a merger plan through establishing a joint holding company (Asahi Bank later decided not to join this group).
	April	<ul style="list-style-type: none"> A new bankruptcy law, the Civil Rehabilitation Law, aiming to streamline procedures and encourage corporate restructuring, came into force. Tokyo Mitsubishi, Nippon Trust and Mitsubishi Trust Banks announced establishment of a joint holding company in April 2001 and a merger of the latter two banks and Tokyo Trust Bank by October 2001. Sakura and Sumitomo Banks announced speeding up of their merger, to form Sumitomo Mitsui Banking Corporation by a year to April 2001.
	May	<ul style="list-style-type: none"> The Diet passed bills to postpone the lifting of comprehensive deposit insurance by a year, to facilitate the disposal of failed financial institutions. The Diet passed a bill to revise commercial codes to enable corporate splits.
	June	<ul style="list-style-type: none"> Shinsei Bank, ex-Long-Term Credit Bank, started operations.

	July	<ul style="list-style-type: none"> The Financial Services Agency (FSA) launched, integrating the functions of the Financial Supervisory Agency and the Financial System Planning Bureau of the MOF. Kimitaka Kuze appointed as FRC Commissioner and soon replaced by Hideyuki Aizawa. Toyo Trust Bank announced joining a holding company to be set up jointly by Sanwa and Tokai Banks in April 2001.
	September	<ul style="list-style-type: none"> The FRC sold the nationalized Nippon Credit Bank to a consortium comprising three Japanese companies, Soft Bank, Orix and Tokyo Marine and Fire Insurance. The new bank later named Aozora Bank. Industrial Bank of Japan, Daiichi-Kangyo and Fuji Banks jointly established a holding company, Mizuho Holdings.
	December	<ul style="list-style-type: none"> Hakuo Yanagisawa appointed as FRC Commissioner.
2001	January	<ul style="list-style-type: none"> With the abolition of the FRC in conjunction with the reorganization of the central government ministries, the FSA became an external agency of the Cabinet Office, absorbing the crisis response function of the FRC. Hakuo Yanagisawa appointed as Minister for Financial Services. Council on Economic and Fiscal Policy (CEFP), comprising scholars, business representatives and relevant Ministers, formed under the Cabinet to support the Prime Minister.
	March	<ul style="list-style-type: none"> Asahi and Daiwa Banks announced a merger.
	April	<ul style="list-style-type: none"> Full mark-to-market accounting adopted for FY2001 and thereafter. The government decided an Emergency Economic Package, setting a target for major banks to write off existing bad loans over the next two years and new bad loans over three years and also proposing to limit the amount of shares held by banks to within their capital, with a proposal to create a new share purchasing body to absorb such shares. Bank of Tokyo Mitsubishi, Mitsubishi Trust and Nippon Trust Banks merged to form a holding company, Mitsubishi Tokyo Financial Group (MTFG). Sakura and Sumitomo Banks merged to form Sumitomo Mitsui Banking Corporation. Sanwa, Tokai and Toyo Trust Banks formed a holding company, UFJ Holdings.
	June	<ul style="list-style-type: none"> CEFP proposed the Outline of Basic Policy for Macroeconomic Management and Structural Reform.
	August	<ul style="list-style-type: none"> The FSA reported that the volume of bad loans would remain unchanged over the next three years due to the projected economic slump, and that it would take another four years to halve the existing amount after its recovery.
	September	<ul style="list-style-type: none"> The Bankers Association (<i>Zenginkyo</i>) and the Federation of Industries (<i>Keidanren</i>) agreed to a code of conduct for debt forgiveness based on the London rules (by INSOL).
	October	<ul style="list-style-type: none"> Mitsubishi and Nippon Trust Banks merged to form Mitsubishi Trust Bank.
	December	<ul style="list-style-type: none"> Daiwa, Kinki Osaka and Nara Banks established a holding company, Daiwa Bank Holdings.
	January	<ul style="list-style-type: none"> Sanwa and Tokai Banks merged to form UFJ Bank, and Toyo Trust Bank became UFJ Trust Bank.
	February	<ul style="list-style-type: none"> The government adopted an anti-deflation package, which includes measures for accelerating NPL disposal and stabilizing the financial system. Chuo Mitsui Trust Bank formed a holding company, Mitsui Trust Holdings.
2002	March	<ul style="list-style-type: none"> Daiwa Bank Holdings absorbed Asahi Bank.
	April	<ul style="list-style-type: none"> The FSA reintroduced limited deposit insurance on time deposits by protecting only up to 10 million yen per depositor per bank, while maintaining full protection of demand deposits. The FSA published the results of the special inspection of large borrowers at major banks. Industrial Bank of Japan, Daiichi Kangyo and Fuji Banks reorganized into Mizuho Bank and Mizuho Corporate Bank.
	September	<ul style="list-style-type: none"> The BOJ announced purchasing equities held by commercial banks at market prices to help them reduce their equity holdings to the level equivalent to their tier-1 capital. Heizo Takenaka appointed as Minister for Financial Services.

	October	<ul style="list-style-type: none"> • The FSA made public the Program for Financial Revival, an ambitious three-pronged strategy to deal with banking sector problems, including reduction of banks' holdings of equities, stricter loan classification and provisioning, and acceleration of NPL disposal. • The FSA announced the postponement of the introduction of a cap on deposit guarantee until April 2005. • Daiwa Bank Holdings renamed to Resona Holdings.
	December	<ul style="list-style-type: none"> • Sumitomo Mitsui Banking Corporation established a holding company, Sumitomo Mitsui Financial Group (SMFG).
2003	January	<ul style="list-style-type: none"> • Mizuho Holdings renamed to Mizuho Financial Group (MHFG), with Mizuho Bank, Mizuho Corporate Bank, and Mizuho Trust and Banking under its control.
	March	<ul style="list-style-type: none"> • Saitama Resona Bank separated from Asahi Bank, and Daiwa and Asahi Banks merged, forming Resona Bank. • The BOJ announced a plan to purchase from commercial banks asset backed securities and commercial papers. The plan went into effect in July.
	April	<ul style="list-style-type: none"> • The postal saving system transformed into an independent corporation, the Japan Post. • The Industrial Revitalization Corporation of Japan (IRCJ) established to promote more effective corporate restructuring and to accelerate the disposal of NPLs. • The FSA published the results of the second special inspection of troubled borrowers of the major banks, showing the gap between the FSA and the banks' own self-assessment had narrowed since the first special inspection. • The Corporate Restructuring Law amended.
	May	<ul style="list-style-type: none"> • Resona Holdings requested the government to inject public funds. • The IRCJ began operation.

Source: OECD Economic Surveys, Japan, 1991-2003, supplemented by information from the Financial Services Agency (FSA), the Bank of Japan (BOJ), and the Ministry of Finance (MOF).

Appendix 2: History of M&As in the Japanese Banking Sector

M&A phenomenon and its importance in Japan dates back to the banking crisis of 1927, following the great depression in Japan (Tatewaki, 1991). In 1927 after the Banking Act Law was passed the number of banks reduced from 1,445 in 1928 to 663 at the end of 1932. Prior to this in the year ending 1918, banks and saving banks numbered 2,033. The largest, Japan's savings bank, became Kyowa Bank, one of the city banks.

By the end of 1945, after World War II, M&A wave swept Japan, leaving only 69 banks, including the prominent city banks: Teikoku, Mitsubishi, Yasuda (later known as Fuji bank), Sanwa, Sumitomo, Kobe, Tokai, and Nomura (later known as Daiwa Bank), Dai-ichi, Nippon Kangyo, and Mitsui bank. In 1952, Long Term Credit Bank was established by merger of two public banks – Kangyo Bank and Hokkaido Bank Colonial Bank. In 1963, Dai-ichi Bank absorbed Asahi Bank. Later on, Teikoku was divided into Mitsui and Dai-Ichi. Besides, Kyowa Bank, three of the former special banks joined the ranks of the city banks, bringing the number to thirteen; Taiyo Bank was given the status of a city bank in December 1968 and Saitama Bank in April 1969. In 1964, Sumitomo Bank absorbed Kawachi Bank, and in 1968 Mitsui Bank merged with Toto Bank. However, these mergers where city banks absorbed local banks did not impact or change the landscape of the banking world in Japan.

On October 1, 1971, Dai-Ichi bank merged with Nippon Kangyo Bank to form Dai-Ichi Kangyo Bank, reducing the number of city banks to twelve. It was the largest merger of the time with Yen 4,056.4 billion in deposits, Yen 3,547.0 billion in outstanding loans, 278 offices and 23,200 employees. About sixty offices were located in the same location with MoFs approval and some new banks were relocated to 15-20 offices in fiscal 1971. This was classified as the new phase of reorganization of Japanese banks. The Fair Trade Commission approved M&As because the combined share of the two banks in the business of the fifteen city banks was 13.8 %, and their share amounted to about 8.3% of all banks deposit balances.

A merger between Dai-Ichi and Mitsubishi bank was proposed on January 1, 1969, however due to resistance from Dai-ichi banks clients and shareholders (strong resistance from Furukawa and Kawasaki groups) disintegrated the plan.

Appendix 3: History of M&A Reforms in Japan

A major development took place on January 7, 1964, when Kakuei Tanaka, the then Finance Minister, in an address to the Federation of the Bankers Association, stressed the need for bank mergers by outlining the following guidelines; (Rowley, 1998; pp. 156) ‘i) mergers of local banks will be approved only if they do not create regional economic problems and if they strengthen the business of the merging banks; ii) mergers of city banks will be approved if they eliminate excessive competition, but no single bank should become too strong and the merger should have no adverse repercussions on the economy; iii) mergers between city banks and local banks are inadvisable because they lead to excessive competition among city banks, but mergers between banks with traditional connections will be approved if the local banks cannot expect further growth.’

In November 1967, the Financial System Research Council cited a need for reorganization of the banking system aimed at resolving the following concerns; i) to ensure that the financial system organized in the beginning of the fifties, would follow its responsibilities to its maximum capacity as the boundaries were perceived to be blurred, as most of the institutions look alike, and they may seem to overlap in terms of their activities i.e. special institutions to provide long-term financing and credit to small enterprises; ii) stop chronic fund dislocation; and iii) to streamline an expansion plan for financial institutions as its lagging behind in terms of growth making them small-scale, high-cost operations; iv) financial institutions must offer new facilities and services to meet the needs, but this kind of adaptation is obstructed by the traditional demarcation of business lines.

Among the recommendations presented, one specific to M&As was that ‘Concerning Mergers and Changes of Status of Financial Institutions.’ This law proposed the merger between different kinds of financial institutions; and also that financial institution be allowed to change their status from one category to another. Subsequently, bank mergers were allowed creating ‘one prefecture one bank’ trend and branch openings

were on the rise. With a few exceptions, branches of local banks were located in the prefectures in which their head-offices were located. The set-up of new branches took place, as a result of which bank branches were outnumbered in old locations than in urban areas. Strategically, located branch network is imperative for Japanese banks as it becomes easier for bank to do business with clients, providing easy access for the deposit of funds for customers, as the basic nature of banking business is collection of deposits from customers, and then on-lending to borrowers. This is why the diversification in individual financial assets created a serious problem for city banks.

Up until 1969, Ministry of Finance, allowed merging banks to retain only one branch in a certain location, other branches in the same neighbourhood had to be closed down. Following the mergers of Dai-ichi bank and Asahi Bank and Sumitomo and Kawachi bank, ten branches had to be shut down. In 1967, the ministry began to allow the transfer of branches; i.e banks could obtain permission to relocate branches from unprofitable locations to more promising neighbourhoods. In 1967 and 1968, the number of branches which banks were allowed to relocate were restricted to two for each bank, but in February 1969, the Ministry of Finance announced a change in its rules. No restriction was put on the number of branches that could be moved, but the ratio of the book value of the real estate used for business purposes to the net worth of the bank must be lower than the standard established by the Ministry of Finance for each kind of bank (the basic ratio for ordinary, long-term credit, and trust banks is 50%; for mutual banks, 70%).

This was considered to be a fundamental law as the city banks were anxious to set-up branches in the new residential developments, which are often used far from the old population centers. In fiscal 1969, the Ministry of Finance authorized the opening of fourteen new branches and the relocation of thirty-two, and, in fiscal 1970, consent was granted to set-up thirteen new branches and re-locates forty-seven. For fiscal 1971, the total new branch offices to be opened by city banks rose to eighty-one, including the relocation of sixty-eight branches (Rowley, 1998; pp. 157).

The mergers among financial institutions for small enterprises made possible by law have increased: in fiscal 1968, there were eight mergers between institutions belonging to the same category and three between those belonging to different categories; the figures were nine and eight in fiscal 1969. From 1968 to May 1971, thirty-eight mergers took place between institutions of the same kind and sixteen mergers between institutions belonging to different categories; three banks became a different kind of financial institutions. As a result of these changes, the number of mutual banks, credit associations, and credit cooperatives decreased from 1,134 in May 1968 to 1,093 at the beginning of 1971. The first mutual bank to take advantage of the new law was the Japan Mutual Bank, which became an ordinary bank, known as Taiyo Bank and then was given the status of the city bank.

Appendix 4: Theoretical Models of M&As

Halpern (1983) has categorized M&A motivation theories into two streams, namely: i) Value maximization theory which includes efficiency theory, informational and signalling theory, market-power and financial motivation theory; and ii) Non-valuation theory considers shareholder and managers, managerial and the free cash flow hypothesis. On another level, external factors such as regulations and laws, globalization, technological progress and economic conditions can also be considered as determinants of M&As.

Trautwein (1990) presented a framework discussing why M&As take place; i) rational choice based on efficiency theory, monopoly theory, raider theory, valuation theory and empire-building theory; ii) process outcome based on process theory; and iii) macro-economic outcome based on disturbance theory.

Merger as a rational choice	Merger benefits bidder's shareholders	Net gains through synergies	Efficiency Theory
		Wealth transfer from customers	Monopoly Theory
		Wealth transfers from target's shareholders	Raider Theory
		Net gains through private information	Valuation Theory
	Merger benefits managers		Empire Building Theory
Merger as process outcome			Process theory
Merger as macroeconomic phenomenon			Disturbance theory

Table 3.5 Theories on Merger Motives

Source Trautwein (1990)

Bower (2001) distinguished five main reasons for the M&As to take place, namely: i) to deal with overcapacity through consolidation in mature industries; ii) to roll up competitors in geographically fragmented industries; iii) to extend into new products or markets; iv) as a substitute for R&D; and v) to exploit eroding industries boundaries by inventing an industry.

Drucker's rule of success for M&As include; (Cantwell and Santangelo, 2002); i) acquire a company with a common core of unity – either a common technology or markets or in some situations production processes (financial ties alone are insufficient); ii) think through your firm's potential contributions of skills to the acquired company; iii) respect the products, markets and customers of the acquired company. There must be a 'temperamental fit'; iv) within approximately a year, you must be able to provide top management for the acquired company and v) within the first year of a merger, a large number of managers of both companies should receive substantial promotions from one of the former companies.

Recof (2003) discuss in the annual report (2003) claim that M&A reasons in Japan fall under five categories; i) bailout, designed to rescue a performance-deteriorating enterprise; ii) sectoral reorganization, an enterprise's ranking within an industry rises to the top-three slot; iii) enhancement of existing operations is to integrate existing business operations; iv) mutual supplementation, combine similar operations; and v) entry into new operations.

Ikeda and Doi (1983) M&A motives; i) increasing market share or market power; ii) increasing efficiency, especially realization of scale economies; iii) increase of research and development; iv) investment adjustment or avoidance of overlapping investment; v) promotion of fund raising capacity; vi) firm growth; vii) reducing risk of business. These are mutually exclusive. Then, the above motives are reduced into; i) increasing market share; ii) increasing efficiency; iii) firm growth; iv) increase of R&D.

In Japan, mergers are represented as defensive measures aimed at consolidating, downsizing and obtaining economies of sale, while avoiding massive lay-offs (Rose and Ito, 2005). Furthermore, it is assumed that merged banks increase their asset size while having the opportunity to close redundant branches and offices.

Appendix 5: Information Sheet for Japanese Banks

VICTORIA UNIVERSITY OF WELLINGTON

Te Whare Wananga o te Upoko o te Ika a Maui



Japanese Banks' Mergers and Acquisitions: Competitive Advantage through Strategic Relatedness and Resources

The Researcher:

My name is Ms. Khadijja Aslam. Currently, I am conducting research on Japanese banks' mergers and acquisitions, in support of the thesis requirement for my Masters of Commerce and Administration degree (International Business) at Victoria University of Wellington, New Zealand. As part of this research, I plan to interview senior executives of the Japanese banks, in their headquarters in Japan. I have identified your bank as a potential participant in this research. I am very interested in interviewing senior management of your bank which may include the Chairman, President, Directors, or Senior Managers.

My Contact Details:

Manners Street, P. O. Box. 11956, Wellington City, New Zealand

Telephone Mobile: +64-21-255-1975, E-mail: aslamkhad@student.vuw.ac.nz

Co-Supervisors:

Associate Professor Val Lindsay, Head of School, School of Marketing and International Business, Room 1101, Rutherford House 23 Lambton Quay, Victoria University of Wellington, Wellington, New Zealand, Tel: +64-4-463-6915, Fax: +64-4-463-5231, E-mail: Val.Lindsay@vuw.ac.nz.

Overview

This research aims at understanding the nature of the similarities and differences between the combining banks, and how particular resources played important roles in achieving competitive advantage for the combined bank. The research also aims to provide an overview of the reasons why the M&A activity took place in Japan.

The results of the interview will be written up as part of my Master of Commerce and Administration (International Business) thesis. There is a possibility that this research will be published in academic journals and professional magazines, and presented at conferences. Ethics approval has been obtained under the VUW (Victoria University of Wellington) research guidelines.

I seek your consent to participate in the study by means of an interview. I would like to record the interview, which is expected to last about 60 minutes. The participating

executive should ideally be someone who has been involved in the M&A strategy and structuring processes.

How will you be affected?

- I am seeking to identify and meet one or more senior executives in your company, who have extensive experience and are willing to participate by speaking with me in an interview.
- The participants' names will not be reported in my thesis, but the company name may be referred to and released if consent is provided by the interviewee (please refer to the request form). Everyone involved in this study will be asked to sign an agreement, to which extra confidentiality conditions may be added.
- You may decide if you want the interview to be taped, or if you prefer that only notes are taken. You have the opportunity to see the notes if you so desire.
- A summary of the results will be provided after the research is completed, if you so desire.
- Seminars /papers may be written for participating companies if you so desire.
- All written material (questionnaires, interview notes, tapes, etc) will be kept in a locked file, with access only to me and my supervisors.
- All data collected will be stored securely and destroyed, two years after completion of this project.
- You have the opportunity to ask questions and have them answered to your satisfaction. You may withdraw yourself and any information you provide from this project, at any time before the data analysis is complete (before December 31st, 2007), without having to give reasons and without penalty of any sort.

Background on Researcher

I hold a BCA Honours in International Business and BCom in Finance, from Victoria University of Wellington and the University of Otago, respectively, and my work experience has been with the United Nations Industrial Development Organization, Pakistan, as Project Manager–SMEs and Gender, on behalf of UNIDO, headquartered in Austria. Furthermore, I have lived in Japan, having graduated from the International School of the Sacred Heart, in Tokyo. Last year, I conducted research on the de-internationalisation of Japanese banks. With this background, I feel that I possess a good understanding of the Japanese business environment, along with some Japanese speaking ability. These skills and experiences will enhance my ability to conduct this research in a professional manner.

This research is being supported by the Sasakawa Foundation, the Victoria University of Wellington School of Marketing and International Business and various other New Zealand organizations.

Appendix 6 Interview Framework

Time required: approximately 0 minutes

This interview framework has been developed to guide the researcher during interviews related to M&As among Japanese banks. It will be taken to each interview. The order of questions will be aligned according to the conversation taking place, in order to maintain coherence.

During the interview, the following forms will be presented to the interviewee: 1) Information Form, 2) Participant Consent Form, 3) Company Consent Form.

Interview starts off with exchange of greetings and introducing the research and its purpose.

Name of Bank:

Name of Interviewee:

Interviewee's Position:

Date of Interview:

Early Planning Stage and Motivations

1. From your perspective, how important was the planning process in advance of this M&A? Do you consider that this process was managed successfully?
2. What made your bank interested in being part of this M&A activity? Why was this 'partner' selected?

Strategic Relatedness

3. I would like to understand about similarities and differences between the combining banks. In your opinion, which of the attributes for both the combining banks were particularly important with respect to creating a competitive advantage for the newly formed bank?
4. What level of integration or combination were you aiming to achieve for the newly combined bank?
5. In your opinion, what kinds of resources were critical for the success of the combined bank? Which of these resources already existed in the separate banks? Were any resources used more effectively in the new bank than in the separate banks?
6. In your opinion, what new resources were required for the combining of these banks, with respect to achieving competitive advantage for the new bank? How were they acquired?
7. What resources do you view as unique to the combined bank, helping it to succeed, relative to other banks?
8. In your opinion, what were the major problems encountered before, during and after the M&A? How were they handled?

Strategic Implications & Future

9. What benefits, in terms of operating and financial synergies, market power and managerial efficiencies, were you hoping to achieve through this M&A activity?
10. In your opinion, how did the customers - individual, corporate and institutional - view this M&A activity?

11. To what extent did the Japanese regulatory authority and FSA assist with carrying out this M&A activity? What could the public sector have done to better support the M&A activity?
12. What impact has this M&A had on the overall banking/financial and economic environment of Japan?
13. I appreciate your giving me this opportunity to interview you today; before I end the session, are there any other comments that you would like to add with regard to M&As in the Japanese banking sector?

Appendix 7: Information Sheet for Non-banks

VICTORIA UNIVERSITY OF WELLINGTON
Te Whare Wananga o te Upoko o te Ika a Maui



Japanese Banks' Mergers and Acquisitions: Competitive Advantage through Strategic Relatedness and Resources

The Researcher:

My name is Ms. Khadijja Aslam. Currently, I am conducting research on Japanese banks' mergers and acquisitions, in support of the thesis requirement for my Masters of Commerce and Administration degree (International Business) at Victoria University of Wellington, New Zealand. As part of this research, I plan to interview senior executives and research analysts of the Japanese banks and other financial institutions, in Japan. I have identified your company as a potential participant in this research. I am very interested in interviewing Senior Financial Analyst, Financial Editor, Director or Senior Manager of your company.

My Contact Details:

Manners Street, P. O. Box. 11956, Wellington City, New Zealand
Telephone Mobile: +64-21-255-1975, E-mail: aslamkhad@student.vuw.ac.nz

Co-Supervisors:

Associate Professor Val Lindsay, Head of School, School of Marketing and International Business, Room 1101, Rutherford House 23 Lambton Quay, Victoria University of Wellington, Wellington, New Zealand, Tel: +64-4-463-6915, Fax: +64-4-463-5231, E-mail: Val.Lindsay@vuw.ac.nz.

Overview

This research aims at understanding the nature of the similarities and differences between the combining banks, and how particular resources played important roles in achieving competitive advantage for the combined bank. The research also aims to provide an overview of the reasons why the M&A activity took place in Japan.

The results of the interview will be written up as part of my Master of Commerce and Administration (International Business) thesis. There is a possibility that this research will be published in academic journals and professional magazines, and presented at conferences. Ethics approval has been obtained under the VUW (Victoria University of Wellington) research guidelines.

I seek your consent to participate in the study by means of an interview. I would like to record the interview, which is expected to last about 60 minutes. The participating

executive should ideally be someone who has been involved in the M&A strategy and structuring processes.

How will you be affected?

- I am seeking to identify and meet one or more senior research analysts or senior executives in your company, who have extensive experience and are willing to participate by speaking with me in an interview.
- The participants' names will not be reported in my thesis, but the company name may be referred to and released if consent is provided by the interviewee (please refer to the non-bank consent form). Everyone involved in this study will be asked to sign an agreement, to which extra confidentiality conditions may be added.
- You may decide if you want the interview to be taped, or if you prefer that only notes are taken. You have the opportunity to see the notes if you so desire.
- A summary of the results will be provided after the research is completed, if you so desire.
- Seminars /papers may be written for participating companies if you so desire.
- All written material (questionnaires, interview notes, tapes, etc) will be kept in a locked file, with access only to me and my supervisors.
- All data collected will be stored securely and destroyed, two years after completion of this project.
- You have the opportunity to ask questions and have them answered to your satisfaction. You may withdraw yourself and any information you provide from this project, at any time before the data analysis is complete (before December 31st, 2007), without having to give reasons and without penalty of any sort.

Background on Researcher

I hold a BCA Honours in International Business and BCom in Finance, from Victoria University of Wellington and the University of Otago, respectively, and my work experience has been with the United Nations Industrial Development Organization, Pakistan, as Project Manager–SMEs and Gender, on behalf of UNIDO, headquartered in Austria. Furthermore, I have lived in Japan, having graduated from the International School of the Sacred Heart, in Tokyo. Last year, I conducted research on the de-internationalisation of Japanese banks. With this background, I feel that I possess a good understanding of the Japanese business environment, along with some Japanese speaking ability. These skills and experiences will enhance my ability to conduct this research in a professional manner.

This research is being supported by the Sasakawa Foundation, the Victoria University of Wellington School of Marketing and International Business and various other New Zealand organizations.

Appendix 8: Interview Framework

Time required: approximately 60 minutes

This interview framework has been developed to guide the researcher during the interviews related to M&As among Japanese banks. It will be taken to each interview. The order of questions will be aligned according to the conversation taking place in order to maintain coherence.

During the interview, the following forms will be presented to the interviewee: 1) Information Form, 2) Participant Consent Form, 3) Company Consent Form.

Interview starts of with exchange of greetings and introducing the research and its purpose.

Name of Media Agency/Government/Consultancy

Name of Interviewee:

Interviewee's Position:

Date of Interview:

Economic Environment of Japan

1. What are the most important ways in which the Japanese financial sector has changed after the bursting of the economic bubble?
2. What are your views regarding the Reform Program, such as the government-initiated 'big-bang'?
3. What motivated the banks to engage in the M&A activity? Why were these banks selected for combination?

Strategic Relatedness

4. One important consideration when choosing partners for M&A activity is the extent to which their resources and strategies are related and aligned. In your opinion, which aspects of these firms, their similarities and differences, were crucial for this M&A?
5. What kinds of resources were critical for the success of the combined bank? Which of these resources already existed in the separate banks? Were any resources used more effectively in the new bank than in the separated bank?
6. What were the major problems encountered before, during and after the M&A? How were they handled?

Strategic Implications & Future

7. What kinds of benefits, in terms of operating and financial synergies, market power and managerial efficiencies, were achieved through this M&A activity?
8. In your opinion, how did the customers - individual, corporate and institutional - view this M&A activity?
9. To what extent did the Japanese regulatory authority and FSA assist with this M&A activity? What could the public sector have done to support the bank's M&A activity?
10. What would you suggest that the future holds for Japanese banks and M&A activity?
11. In your opinion, what impact has this M&A had on the overall banking/financial and economic environment of Japan?
12. I appreciate your giving me with this opportunity to interview you today; before I end the session, are there any other comments that you would like to add with regard to M&As in the Japanese banking sector?

Appendix 9: Consent for Japanese Banks to Participate in this Thesis

VICTORIA UNIVERSITY OF WELLINGTON
Te Whare Wananga o te Upoko o te Ika a Maui



Japanese Banks' Mergers and Acquisitions: Competitive Advantage through Strategic Relatedness and Resources

- This is a research agreement between you and the researcher, Khadijja Aslam.
- Your name will be kept confidential; that is, your name will not be used, but your company's name may be referred to in the thesis, if you give your consent. However, if you are concerned about lack of confidentiality, then this study will adopt an alternative approach that does not identify companies

() I allow the company name to be used in professional and academic literature.

() I would like the researcher to adopt an alternative approach that does not identify the name of the company.

- You have the option to decide if you want the interview to be tape-recorded or if you prefer me (or the interpreter) to take notes (please indicate your preference below). You may see the notes if you wish to do so.

() Yes, I consent to having the interview tape-recorded.

() No, I do not consent to having the interview tape-recorded.

- All written material (interview notes, tapes, etc) will be kept in a locked file, with access only available to the researcher and the supervisors.
- You have the opportunity to see the notes if you so desire, please tick below.
() Yes, I would like to review the notes/transcripts.
() No, I do not wish to review the notes/transcripts.
- The research results may be published in professional and academic journals, and presented at conferences/seminars. The finished thesis will be held in the Victoria University of Wellington library.
- If you would like to receive a summary of the research results, please tick below.

() Yes, I would like to receive a summary of the results of this research when it is completed.

Participant's Statement

I am satisfied with the information provided regarding the research. I realise that I have the option to decide not be involved at any time, without having to specify why, at any time prior to the data's being analysed.

Please write in any additional comments or conditions:

I, _____ (print participant name) agree to take part in this research and interview on _____ (date).

Signed _____

Researcher:

Khadijja Aslam

School of Marketing and International Business, Victoria University of Wellington, New Zealand

Address: Manners Street, P. O. Box 11956, Wellington, New Zealand

Email: aslamkhad@student.vuw.ac.nz; Telephone: +64-21-255-1975

Appendix 10: Consent for Non-banks to Participate in this Thesis

VICTORIA UNIVERSITY OF WELLINGTON
Te Whare Wananga o te Upoko o te Ika a Maui



Japanese Banks' Mergers and Acquisitions: Competitive Advantage through Strategic Relatedness and Resources

- This is a research agreement between you and the researcher, Khadijja Aslam.
- Your name will be kept confidential; that is, your name will not be used, but your company's name may be referred to in the thesis, if you give your consent. However, if you are concerned about lack of confidentiality, then this study will adopt an alternative approach that does not identify companies

() I allow the company name to be used in professional and academic literature.
() I would like the researcher to adopt an alternative approach that does not identify the name of the company.
- You have the option to decide if you want the interview to be tape-recorded or if you prefer me (or the interpreter) to take notes (please indicate your preference below). You may see the notes if you wish to do so.

() Yes, I consent to having the interview tape-recorded.
() No, I do not consent to having the interview tape-recorded.
- All written material (interview notes, tapes, etc) will be kept in a locked file, with access only available to the researcher and the supervisors.
- You have the opportunity to see the notes if you so desire, please tick below.
() Yes, I would like to review the notes/transcripts.
() No, I do not wish to review the notes/transcripts.
- The research results may be published in professional and academic journals, and presented at conferences/seminars. The finished thesis will be held in the Victoria University of Wellington library.
- If you would like to receive a summary of the research results, please tick below.

() Yes, I would like to receive a summary of the results of this research when it is completed.

Participant's Statement

I am satisfied with the information provided regarding the research. I realise that I have the option to decide not be involved at any time, without having to specify why, at any time prior to the data's being analysed.

Please write in any additional comments or conditions:

I, _____ (print participant name) agree to take part in this research and interview on _____ (date).

Signed _____

Researcher:

Khadijja Aslam

School of Marketing and International Business, Victoria University of Wellington, New Zealand

Address: Manners Street, P. O. Box 11956, Wellington, New Zealand

Email: aslamkhad@student.vuw.ac.nz; Telephone: +64-21-255-1975