# On the Resurgence of Cross-Shareholding—Data from the *Fiscal 2008 Survey of Corporate Ownership Structure*

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*Although the resurgence of cross-shareholding has been a growing concern in recent years, previous surveys have not been able to detect the magnitude of this trend. Based on a careful analysis of the latest data, we clarify the size and structure of the resurgence. Our results indicate that while no discernable rise has occurred in the overall cross-shareholding ratio, a resurgence is underway in the form of expansion of cross-shareholding networks. In addition, the strengthening of cross-shareholding ties is most prevalent among business firms, not banks.*

## 1. Introduction

Cross-shareholding used to be a prominent feature of Japan's stock market until the late 1990s to mid 2000s, when firms began unwinding on a massive scale. However, the tide may be shifting again—recent signs are pointing to a resurgence of cross-shareholding. According to the *Nikkei Shimbun* (August 14, 2009 morning edition), *Yuka Shoken Hokokusho* (securities filings of listed firms) submitted by June 2009 show that new cross-shareholdings have emerged broadly.

Other media reports also indicate that many new cross-shareholding ties have strengthened in recent years. However, no rigorous surveys exist to confirm the size of such cross-shareholdings in the overall market, or what kind of structure they possess. Even our own survey of recent trends cross-shareholding ratios shows no clear evidence of a resurgence of cross-shareholding. [1] As we will discuss below, previous surveys show that the cross-shareholding ratio leveled off from fiscal 2005, and while a lull in unwinding could be confirmed, the fluctuation during this period was small enough to be within the scope of observation error. Even if cross-shareholding had recovered the size of recovery was likely to be small.

However, in recent years, investors and others have become more alarmed about the recovery of cross-shareholding, which is adequate reason to take a serious look. The sense of alarm is fed by the rise of hostile takeovers and activist funds. [2] The essential function of cross-shareholding, which is to eliminate the influence of hostile shareholders, is likely being reviewed. [3] If so, the growth of cross-shareholding signals that current management is resorting to cross-shareholding as a defensive measure, the cost of which investors will undoubtedly reject. Indeed, the possibility of a resurgence of cross-shareholding and the proper understanding of its structure are of crucial importance.

Previous surveys indicate that while stronger cross-shareholding ties have been widely observed, the cross-shareholding ratio has not risen significantly. Three hypotheses have been put forward to explain this apparent contradiction. The first holds that cross-shareholding is simultaneously growing and unwinding, but the preoccupation with strengthening obscures the offsetting effect in the overall stock market. Second, cross-shareholding is growing among certain high-profile but relatively minor corporate groups, and has a small impact on the overall market. Third, cross-shareholding is becoming widespread, but the total impact is negligible because each case is minor.

If cross-shareholding is indeed resurging, another key point is to establish whether it bears a continuity with previous forms (i.e., revival of former cross-shareholding ties), or else represents a discontinuous and new form of tie. Since most of the unwinding in the late 1990s involved ties between banks and business firms, continuity would point to an increase in banks' shareholdings. On the other hand, discontinuity would signal a structural shift in corporate ties based on another key function of cross-shareholding—promoting long-term stable ties between firms.

Which of the above hypotheses is valid? And if a tidal shift has occurred, when did it happen? The answers to these questions are vital to assessing the possible impact of resurgent cross-shareholding. Since previous studies have failed to satisfactorily answer them, we attempt a more refined analysis from a different perspective.

## 2. Trends in Ownership Structure

First we examine the latest data to detect changes in ownership structure at major firms in Japan. For firms listed on the first section of the three major stock exchanges (Tokyo, Osaka, and Nagoya), Exhibit 1 shows the average ownership structure at the firm level. It depicts the average shareholder composition at major companies. The shareholder types shown at the bottom are based on the author's own definitions.[7]

Perhaps the most notable recent change has been the plunging ratio of institutional investors after a sustained surge since 2000. After the Lehman shock in September 2008, foreign institutional investors hastily retreated from the market, causing the ratio to plummet by -2.33 percentage points from 21.29% in fiscal 2007 (yearend) to 18.96% in fiscal 2008.[8] The ratio's decline is particularly significant in light of the perception that institutional investors have helped enhance market discipline of corporate management. In addition, the large sell-off that reduced the ratio also drove

**Exhibit 1 Average Ownership Structure of Listed Firms on the First Section of Tokyo, Osaka, and Nagoya Stock Exchanges**

(Percent)

| FY | No. of firms | Cross-shhldg ratio | yoy chg (pp) | Financial institution | Non-financial firm | Foreign firm | Insider | (director) | Holding company | Natl. & local govt. | Institutional shhldr | Other minor shhldr |
|---|---|---|---|---|---|---|---|---|---|---|---|---|
| 1987 | 1,233 | 14.54 | – | 6.56 | 8.19 | 0.66 | 6.58 | (3.07) | 1.21 | 0.11 | 5.85 | 56.30 |
| 1988 | 1,268 | 14.79 | (0.25) | 6.31 | 8.08 | 0.67 | 6.66 | (3.09) | 1.16 | 0.10 | 6.46 | 55.80 |
| 1989 | 1,307 | 14.70 | (−0.08) | 6.18 | 8.12 | 0.61 | 6.81 | (2.84) | 1.10 | 0.09 | 7.73 | 54.66 |
| 1990 | 1,342 | 14.97 | (0.27) | 6.23 | 8.26 | 0.60 | 6.92 | (2.53) | 1.11 | 0.09 | 7.95 | 53.88 |
| 1991 | 1,381 | 14.84 | (−0.13) | 6.22 | 8.46 | 0.56 | 7.09 | (2.54) | 1.20 | 0.09 | 8.64 | 52.90 |
| 1992 | 1,387 | 15.05 | (0.21) | 6.20 | 8.33 | 0.56 | 7.04 | (2.53) | 1.34 | 0.09 | 8.64 | 52.76 |
| 1993 | 1,301 | 15.03 | (−0.02) | 6.27 | 8.12 | 0.58 | 5.95 | (1.98) | 1.31 | 0.09 | 10.08 | 52.55 |
| 1994 | 1,301 | 15.16 | (0.13) | 6.15 | 7.97 | 0.58 | 5.87 | (1.94) | 1.36 | 0.16 | 10.39 | 52.36 |
| 1995 | 1,322 | 14.89 | (−0.27) | 5.80 | 8.21 | 0.58 | 6.02 | (1.93) | 1.45 | 0.15 | 10.85 | 52.06 |
| 1996 | 1,356 | 14.65 | (−0.24) | 5.54 | 8.47 | 0.60 | 6.05 | (2.00) | 1.50 | 0.14 | 11.40 | 51.65 |
| 1997 | 1,393 | 14.29 | (−0.36) | 5.26 | 8.63 | 0.65 | 6.41 | (2.15) | 1.69 | 0.14 | 10.96 | 51.97 |
| 1998 | 1,405 | 13.41 | (−0.88) | 5.22 | 8.88 | 0.68 | 6.59 | (2.30) | 1.91 | 0.14 | 10.49 | 52.68 |
| 1999 | 1,459 | 12.56 | (−0.85) | 4.79 | 9.08 | 0.72 | 7.40 | (2.61) | 2.00 | 0.13 | 11.33 | 51.99 |
| 2000 | 1,523 | 11.64 | (−0.92) | 4.43 | 9.44 | 0.78 | 8.39 | (3.23) | 2.14 | 0.11 | 12.23 | 50.82 |
| 2001 | 1,549 | 11.21 | (−0.43) | 4.20 | 9.41 | 0.86 | 9.05 | (3.44) | 2.21 | 0.12 | 13.08 | 49.87 |
| 2002 | 1,570 | 10.09 | (−1.12) | 4.03 | 9.18 | 0.86 | 9.85 | (3.74) | 2.33 | 0.11 | 13.89 | 49.67 |
| 2003 | 1,594 | 9.75 | (−0.34) | 3.35 | 9.08 | 0.71 | 10.24 | (4.05) | 2.31 | 0.14 | 16.26 | 48.16 |
| 2004 | 1,687 | 8.87 | (−0.88) | 3.07 | 9.40 | 0.72 | 10.43 | (4.29) | 2.20 | 0.14 | 18.76 | 46.40 |
| 2005 | 1,734 | 8.70 | (−0.17) | 2.84 | 9.23 | 0.57 | 10.73 | (4.43) | 2.03 | 0.12 | 21.27 | 44.50 |
| 2006 | 1,768 | 8.65 | (−0.05) | 2.66 | 9.33 | 0.59 | 11.04 | (4.54) | 1.97 | 0.13 | 21.82 | 43.81 |
| 2007 | 1,759 | 8.71 | (0.06) | 2.79 | 9.48 | 0.53 | 11.06 | (4.57) | 2.01 | 0.12 | 21.29 | 44.01 |
| 2008 | 1,740 | 8.61 | (−0.10) | 2.90 | 9.47 | 0.54 | 11.20 | (4.42) | 2.20 | 0.13 | 18.96 | 46.00 |

| Shareholder type | Definition |
|---|---|
| Cross-shareholder | Cross-held shares on both sides are counted in the cross-shareholding ratio |
| Financial institution * | Banks, life insurers, and non-life insurers with at least 3% ownership; excludes cross- |
| Listed firm * | Publicly listed companies with at least 3% ownership; excludes cross-shareholding and financial institutions, but includes non-listed companies affiliated with listed holding companies |
| Foreign firm * | Foreign-registered business firms with at least 3% ownership |
| Insider: director | Executives and auditors; includes directors' stock ownership plan |
| domestic private firm * | Domestic-registered private firms with at least 3% ownership |
| foreign priv. firm & large indiv. | Foreign-registered private firms and individuals with at least 3% ownership |
| Stock ownership plan | Stock ownership plans of employees and business partners |
| Govt. & public institution * | National and local government entities with at least 3% ownership |
| Institutional investor: domestic | Pension trust, investment trust, life insurance special account |
| foreign | Foreigners excluding foreign-registered firms and large foreign individual shareholders |
| Other minority shareholder | All other shareholders |

Note: * denotes that only shareholdings in excess of 3% are counted.

stock prices sharply downward.

On the other hand, no significant change was observed among other shareholder types. For example, the cross-shareholding ratio edged down by only -0.10 pp from 8.71% in fiscal 2007 to 8.61% in fiscal 2008. Thus the large sell-off by foreign institutional investors was absorbed not by cross-shareholders or major shareholders, but by small individual investors. In fact, the ratio of other minor shareholders, which aggregates the shareholdings of small investors, rose 1.99 pp from 44.01% in fiscal 2007 to 46.00% in fiscal 2008.

With regard to our main concern of the long-term trend of the cross-shareholding ratio, the ratio stabilized at around 15% until the end of fiscal 1996, but plummeted from early fiscal 1997 to the end of fiscal 2004 mainly due to unwinding by banks. Since fiscal 2005, despite concerns of resurgence, the ratio has remained at around 8.7%.[9] Even the latest aggregated data reveals no evidence of resurgence.

For reasons beyond the scope of this paper, it is very difficult to present clear evidence of a resurgence based on cross-shareholding data regardless of the aggregation method used. For example, our sample from the three exchanges has undergone a significant turnover since 1999 due to new listings and delistings. Assuming that cross-shareholding is of more importance to long-established firms than to new firms, we narrowed the sample and recalculated Exhibit 1 for firms listed as of fiscal 1987. Even so, the cross-shareholding ratio edged up by only 0.39 pp, from 11.02% at fiscal 2004 yearend to 11.41% at fiscal 2007 yearend, and subsequently fell to 11.26% in fiscal 2008.[10] In addition, from firm level data we found that the distribution of change in cross-shareholding ratio clearly confirms an unwinding trend from the late 1990s to mid 2000s, but only a very limited resurgence thereafter.

## 3. Our Analytical Strategy

However, the above analysis does not tell us whether the resurgence of cross-shareholding is a minor and isolated phenomenon with no major significance for the overall market. If the third hypothesis is true—that cross-shareholding is strengthening on a widespread basis, but that each case is so small that the total effect is negligible—then corporate behavior could deviate significantly and have important implications for the market without a commensurate rise of the cross-shareholding ratio. That is, the cost of enhancing cross-shareholding ties may not be justified by the benefits, which are often unclear or unpersuasive.[11]

**Exhibit 2 Trend in Cross-Shareholding Networks**

| FY | No. of cross-shareholding cases | | | | | As percent of total sample | | | | | |
|---|---|---|---|---|---|---|---|---|---|---|---|
| | No change | Buying | Selling | Not known | Total | No change | Buying | Selling | Not known | Net increase | |
| 1987 | 16,063 | 5,371 | 1,919 | 386 | 23,739 | 67.7 | 22.6 | 8.1 | 1.6 | 14.5 | |
| 1988 | 16,017 | 6,982 | 1,611 | 530 | 25,140 | 63.7 | 27.8 | 6.4 | 2.1 | 21.4 | |
| 1989 | 16,546 | 7,736 | 2,035 | 677 | 26,994 | 61.3 | 28.7 | 7.5 | 2.5 | 21.1 | Strengthening |
| 1990 | 20,387 | 5,955 | 1,424 | 507 | 28,273 | 72.1 | 21.1 | 5.0 | 1.8 | 16.0 | |
| 1991 | 23,384 | 3,892 | 1,375 | 528 | 29,179 | 80.1 | 13.3 | 4.7 | 1.8 | 8.6 | |
| 1992 | 25,010 | 2,695 | 1,095 | 411 | 29,211 | 85.6 | 9.2 | 3.7 | 1.4 | 5.5 | |
| 1993 | 24,671 | 1,903 | 1,637 | 606 | 28,817 | 85.6 | 6.6 | 5.7 | 2.1 | 0.9 | |
| 1994 | 25,125 | 2,117 | 1,300 | 557 | 29,099 | 86.3 | 7.3 | 4.5 | 1.9 | 2.8 | |
| 1995 | 25,770 | 2,041 | 1,434 | 359 | 29,604 | 87.0 | 6.9 | 4.8 | 1.2 | 2.1 | |
| 1996 | 25,854 | 2,408 | 1,271 | 487 | 30,020 | 86.1 | 8.0 | 4.2 | 1.6 | 3.8 | |
| 1997 | 25,379 | 2,581 | 1,785 | 756 | 30,501 | 83.2 | 8.5 | 5.9 | 2.5 | 2.6 | |
| 1998 | 23,786 | 2,453 | 2,526 | 668 | 29,433 | 80.8 | 8.3 | 8.6 | 2.3 | −0.2 | |
| 1999 | 18,994 | 1,848 | 4,355 | 2,245 | 27,442 | 69.2 | 6.7 | 15.9 | 8.2 | −9.1 | |
| 2000 | 14,131 | 1,801 | 2,398 | 1,293 | 19,623 | 72.0 | 9.2 | 12.2 | 6.6 | −3.0 | |
| 2001 | 13,327 | 2,410 | 2,301 | 941 | 18,979 | 70.2 | 12.7 | 12.1 | 5.0 | 0.6 | Unwinding |
| 2002 | 11,796 | 2,586 | 2,924 | 1,092 | 18,398 | 64.1 | 14.1 | 15.9 | 5.9 | −1.8 | |
| 2003 | 12,173 | 1,165 | 3,193 | 1,251 | 17,782 | 68.5 | 6.6 | 18.0 | 7.0 | −11.4 | |
| 2004 | 13,003 | 1,357 | 2,034 | 791 | 17,185 | 75.7 | 7.9 | 11.8 | 4.6 | −3.9 | |
| 2005 | 12,742 | 2,281 | 1,580 | 816 | 17,419 | 73.2 | 13.1 | 9.1 | 4.7 | 4.0 | |
| 2006 | 13,671 | 1,909 | 973 | 743 | 17,296 | 79.0 | 11.0 | 5.6 | 4.3 | 5.4 | |
| 2007 | 12,958 | 2,393 | 792 | 966 | 17,109 | 75.7 | 14.0 | 4.6 | 5.6 | 9.4 | Resurging |
| 2008 | 12,698 | 1,756 | 677 | 1,179 | 16,310 | 77.9 | 10.8 | 4.2 | 7.2 | 6.6 | |

Since conventional analysis cannot sufficiently test this hypothesis, we need a different approach that carefully tracks changes in each cross-shareholding relationship (referred to below as cross-shareholding network). In the following analysis, we construct a database of confirmed trends in cross-shareholding transactions, and then analyze how cross-shareholding networks have transformed over time. To determine whether a transaction has occurred, we look at whether the number of cross-held shares has changed by at least two units, against the backdrop of capital movements and organizational restructuring. A cross-shareholding network is determined to be "unchanged" if holdings have not changed from the previous year, "buying" if purchases are confirmed, and "selling" if sales are confirmed. If no transactions can be reasonably determined from the data due to disclosure limitations, the network is categorized as "not known."

In counting the number of cross-shareholding networks, since the cross-shareholding of each firm is counted as one case, each network consists of two cases in principle. However, the number of cases does not necessarily add up to an even number because cross-shareholding ties may exist with firms outside our sample of the three major exchanges. Moreover, since cross-shareholding cases are counted if they can be confirmed in the current or previous fiscal year, a case will be counted in the total even if it has been completely unwound in the current fiscal year.

## 4. Magnitude of the Cross-Shareholding Resurgence

From the above data, we next confirm whether cross-shareholding has resurged in recent years and the size of the resurgence. The cross-shareholding network trends in Exhibit 2 confirm that a resurgence phase began in fiscal 2005.[12] However, although the cross-shareholding ratio has not moved significantly since then, it is clear that cross-shareholding purchases have far exceeded sales, marking a sharp departure from the unwinding phase from fiscal 1998 to 2004. Actually, the ratio also moved sluggishly in the strengthening phase of the bubble economy from fiscal 1987 to 1992, which was much more pronounced than the current resurgence phase. Thus the ratio apparently does not respond strongly even when network strengthening can be clearly confirmed. In this respect, the ratio's large drop in the unwinding phase of the late 1990s attests to the magnitude of unwinding.

We next consider whether the above network strengthening activity was limited to a small number of firms, or a widespread phenomenon. For an overview of firm activity in the period, we first recalculate the data from Exhibit 2 to reveal movements at the firm level. Then we compare each firm's number of purchases against sales to determine whether the network has posted a net

**Exhibit 3　Firm Behavior Regarding Cross-Shareholding Networks**

| FY | No. of firms | No. of cross-shareholding cases | | | | As percent of firms in sample | | | | | |
|---|---|---|---|---|---|---|---|---|---|---|---|
| | | No cross-shrhldg | No change | Net increase (a) | Net decrease (b) | No cross-shrhldg | No change | Net increase (a) | Net decrease (b) | (a) − (b) | |
| 1987 | 1233 | 32 | 327 | 601 | 273 | 2.6 | 26.5 | 48.7 | 22.1 | 26.6 | |
| 1988 | 1268 | 36 | 292 | 726 | 214 | 2.8 | 23.0 | 57.3 | 16.9 | 40.4 | |
| 1989 | 1307 | 28 | 282 | 832 | 165 | 2.1 | 21.6 | 63.7 | 12.6 | 51.0 | |
| 1990 | 1342 | 24 | 296 | 887 | 135 | 1.8 | 22.1 | 66.1 | 10.1 | 56.0 | Strengthening |
| 1991 | 1381 | 22 | 448 | 728 | 183 | 1.6 | 32.4 | 52.7 | 13.3 | 39.5 | |
| 1992 | 1387 | 20 | 563 | 610 | 194 | 1.4 | 40.6 | 44.0 | 14.0 | 30.0 | |
| 1993 | 1301 | 12 | 537 | 400 | 352 | 0.9 | 41.3 | 30.7 | 27.1 | 3.7 | |
| 1994 | 1301 | 12 | 569 | 449 | 271 | 0.9 | 43.7 | 34.5 | 20.8 | 13.7 | |
| 1995 | 1322 | 12 | 569 | 457 | 284 | 0.9 | 43.0 | 34.6 | 21.5 | 13.1 | |
| 1996 | 1356 | 13 | 520 | 547 | 276 | 1.0 | 38.3 | 40.3 | 20.4 | 20.0 | |
| 1997 | 1393 | 8 | 485 | 522 | 378 | 0.6 | 34.8 | 37.5 | 27.1 | 10.3 | |
| 1998 | 1405 | 1 | 511 | 403 | 490 | 0.1 | 36.4 | 28.7 | 34.9 | −6.2 | |
| 1999 | 1459 | 17 | 437 | 225 | 780 | 1.2 | 30.0 | 15.4 | 53.5 | −38.0 | |
| 2000 | 1523 | 28 | 527 | 354 | 614 | 1.8 | 34.6 | 23.2 | 40.3 | −17.1 | |
| 2001 | 1549 | 32 | 566 | 379 | 572 | 2.1 | 36.5 | 24.5 | 36.9 | −12.5 | Unwinding |
| 2002 | 1570 | 44 | 494 | 339 | 693 | 2.8 | 31.5 | 21.6 | 44.1 | −22.5 | |
| 2003 | 1594 | 80 | 465 | 243 | 806 | 5.0 | 29.2 | 15.2 | 50.6 | −35.3 | |
| 2004 | 1687 | 145 | 638 | 349 | 555 | 8.6 | 37.8 | 20.7 | 32.9 | −12.2 | |
| 2005 | 1734 | 167 | 649 | 598 | 320 | 9.6 | 37.4 | 34.5 | 18.5 | 16.0 | |
| 2006 | 1768 | 192 | 696 | 627 | 253 | 10.9 | 39.4 | 35.5 | 14.3 | 21.2 | |
| 2007 | 1759 | 196 | 715 | 657 | 191 | 11.1 | 40.6 | 37.4 | 10.9 | 26.5 | Resurging |
| 2008 | 1740 | 212 | 776 | 554 | 198 | 12.2 | 44.6 | 31.8 | 11.4 | 20.5 | |

increase or decrease.

Exhibit 3 shows that since 2005, networks at approximately 35% of firms have increased in net terms, outnumbering the 20% with a net decrease. Thus the strengthening of networks has not been limited to a few high-profile firms, but is instead widespread at major firms. Moreover, the firm-level results clearly correlate with the three phases of strengthening, unwinding, and resurgence in the aggregated results of Exhibit 2. These results indicate that the cross-shareholding stance of firms apparently reversed course at fiscal 2004 yearend, and that the magnitude of resurgence is second highest by a wide margin to the strengthening phase of the bubble era.

## 5. Structure of the Cross-Shareholding Resurgence

Does the current resurgence represent a revival of old ties, or the formation of new ties reflecting a structural shift in corporate relationships? Since banks were the principal players in the unwinding phase from fiscal 1998 to 2004, we can confirm this point by determining whether banks or business firms are now most active in the resurgence.

In Exhibit 4, Panel A shows the transaction trends of cross-held shares of banks since fiscal 1996. Banks unwound cross-shareholdings from fiscal 1997 to 2004, after which purchases and sales have balanced out. In particular, their transactions stagnated from fiscal 2006, with approximately 85% of cross-shareholding ties maintaining status quo. Thus banks appear to be tentatively done reviewing their cross-shareholding ties, and are not involved in the current resurgence.

On the other hand, the transaction trends of business firms Panel B confirm that the current resurgence stems from the strengthening of cross-shareholding networks. Even when the overall market was unwinding from fiscal 1998 to 2004, business firms participated in only two years—in fiscal 1999, when mark-to-market rules were introduced for the valuation of cross-held shares, [13] and

**Exhibit 4 Cross-Shareholding Transaction Trends of Banks and Business Firms**

Panel A: Banks

| | No. of cross-shareholding cases | | | | | As percent of total sample | | | | |
|---|---|---|---|---|---|---|---|---|---|---|
| | No change | Buying | Selling | Not known | Total | No change | Buying | Selling | Not known | Net increase |
| 1996 | 3,909 | 472 | 156 | 146 | 4,683 | 83.5 | 10.1 | 3.3 | 3.1 | 6.7 |
| 1997 | 3,996 | 244 | 403 | 174 | 4,817 | 83.0 | 5.1 | 8.4 | 3.6 | −3.3 |
| 1998 | 3,873 | 146 | 486 | 181 | 4,686 | 82.7 | 3.1 | 10.4 | 3.9 | −7.3 |
| 1999 | 3,458 | 172 | 586 | 120 | 4,336 | 79.8 | 4.0 | 13.5 | 2.8 | −9.5 |
| 2000 | 3,202 | 154 | 745 | 100 | 4,201 | 76.2 | 3.7 | 17.7 | 2.4 | −14.1 |
| 2001 | 2,361 | 455 | 1,079 | 197 | 4,092 | 57.7 | 11.1 | 26.4 | 4.8 | −15.2 |
| 2002 | 1,266 | 1,069 | 1,931 | 150 | 4,416 | 28.7 | 24.2 | 43.7 | 3.4 | −19.5 |
| 2003 | 1,994 | 143 | 1,131 | 119 | 3,387 | 58.9 | 4.2 | 33.4 | 3.5 | −29.2 |
| 2004 | 2,208 | 124 | 668 | 193 | 3,193 | 69.2 | 3.9 | 20.9 | 6.0 | −17.0 |
| 2005 | 2,057 | 473 | 509 | 162 | 3,201 | 64.3 | 14.8 | 15.9 | 5.1 | −1.1 |
| 2006 | 2,398 | 182 | 159 | 103 | 2,842 | 84.4 | 6.4 | 5.6 | 3.6 | 0.8 |
| 2007 | 2,391 | 128 | 128 | 74 | 2,721 | 87.9 | 4.7 | 4.7 | 2.7 | 0.0 |
| 2008 | 2,250 | 94 | 162 | 105 | 2,611 | 86.2 | 3.6 | 6.2 | 4.0 | −2.6 |

Panel B: Business firms

| | No. of cross-shareholding cases | | | | | As percent of total sample | | | | |
|---|---|---|---|---|---|---|---|---|---|---|
| | No change | Buying | Selling | Not known | Total | No change | Buying | Selling | Not known | Net increase |
| 1996 | 21,519 | 1,876 | 1,032 | 320 | 24,747 | 87.0 | 7.6 | 4.2 | 1.3 | 3.4 |
| 1997 | 20,980 | 2,235 | 1,314 | 561 | 25,090 | 83.6 | 8.9 | 5.2 | 2.2 | 3.7 |
| 1998 | 19,508 | 2,198 | 1,974 | 463 | 24,143 | 80.8 | 9.1 | 8.2 | 1.9 | 0.9 |
| 1999 | 15,143 | 1,612 | 3,661 | 2,094 | 22,510 | 67.3 | 7.2 | 16.3 | 9.3 | −9.1 |
| 2000 | 10,625 | 1,590 | 1,574 | 1,175 | 14,964 | 71.0 | 10.6 | 10.5 | 7.9 | 0.1 |
| 2001 | 10,685 | 1,888 | 1,151 | 711 | 14,435 | 74.0 | 13.1 | 8.0 | 4.9 | 5.1 |
| 2002 | 10,247 | 1,464 | 882 | 915 | 13,508 | 75.9 | 10.8 | 6.5 | 6.8 | 4.3 |
| 2003 | 9,828 | 990 | 1,930 | 1,113 | 13,861 | 70.9 | 7.1 | 13.9 | 8.0 | −6.8 |
| 2004 | 10,456 | 1,179 | 1,223 | 571 | 13,429 | 77.9 | 8.8 | 9.1 | 4.3 | −0.3 |
| 2005 | 10,269 | 1,782 | 1,004 | 628 | 13,652 | 75.2 | 13.1 | 7.4 | 4.6 | 5.7 |
| 2006 | 10,855 | 1,699 | 751 | 623 | 13,928 | 77.9 | 12.2 | 5.4 | 4.5 | 6.8 |
| 2007 | 10,176 | 2,233 | 609 | 875 | 13,873 | 73.4 | 16.1 | 4.4 | 6.3 | 11.7 |
| 2008 | 10,127 | 1,642 | 447 | 1,051 | 13,267 | 76.3 | 12.4 | 3.4 | 7.9 | 9.0 |

in fiscal 2003, when unwinding by banks was at the peak. [14] Otherwise, business firms were basically passive toward unwinding. In fact, business firms have been active buyers since fiscal 2005, and the current resurgence is almost fully explained by their cross-shareholding transactions.

A closer examination shows that the current resurgence can be clearly attributed to the strengthening of cross-shareholding networks among business firms (Exhibit 5). Except for fiscal 1999, when firms were preparing for the introduction of mark-to-market accounting rules, cross-shareholding has basically strengthened, particularly from fiscal 2005. Moreover, in conjunction with this trend, we can observe a large increase in cross-shareholding cases from fiscal 2005. [15]

**Exhibit 5 Cross-Shareholding Networks of Business Firms**

| | No. of cross-shareholding cases | | | | | As percent of total sample | | | | |
|---|---|---|---|---|---|---|---|---|---|---|
| | No change | Buying | Selling | Not known | Total | No change | Buying | Selling | Not known | Net increase |
| 1996 | 9,965 | 738 | 525 | 92 | 11,320 | 88.0 | 6.5 | 4.6 | 0.8 | 1.9 |
| 1997 | 9,546 | 1,156 | 648 | 258 | 11,608 | 82.2 | 10.0 | 5.6 | 2.2 | 4.4 |
| 1998 | 9,055 | 946 | 836 | 239 | 11,076 | 81.8 | 8.5 | 7.5 | 2.2 | 1.0 |
| 1999 | 6,165 | 712 | 2,141 | 1,469 | 10,487 | 58.8 | 6.8 | 20.4 | 14.0 | −13.6 |
| 2000 | 4,460 | 741 | 700 | 601 | 6,502 | 68.6 | 11.4 | 10.8 | 9.2 | 0.6 |
| 2001 | 4,588 | 654 | 416 | 374 | 6,032 | 76.1 | 10.8 | 6.9 | 6.2 | 3.9 |
| 2002 | 4,604 | 689 | 381 | 339 | 6,013 | 76.6 | 11.5 | 6.3 | 5.6 | 5.1 |
| 2003 | 4,683 | 656 | 630 | 276 | 6,245 | 75.0 | 10.5 | 10.1 | 4.4 | 0.4 |
| 2004 | 4,902 | 875 | 438 | 302 | 6,517 | 75.2 | 13.4 | 6.7 | 4.6 | 6.7 |
| 2005 | 5,305 | 1,276 | 410 | 356 | 7,347 | 72.2 | 17.4 | 5.6 | 4.8 | 11.8 |
| 2006 | 5,851 | 1,306 | 323 | 373 | 7,853 | 74.5 | 16.6 | 4.1 | 4.7 | 12.5 |
| 2007 | 5,842 | 1,487 | 259 | 511 | 8,099 | 72.1 | 18.4 | 3.2 | 6.3 | 15.2 |
| 2008 | 6,020 | 1,004 | 218 | 595 | 7,837 | 76.8 | 12.8 | 2.8 | 7.6 | 10.0 |

From the above, we can conclude that the resurgence of cross-shareholding is explained not by the revival of ties between banks and business firms, but by the expansion of cross-shareholding networks among business firms. However, we remain skeptical as to whether this represents a structural shift leading to new corporate relationships—because regardless of whether they are strengthening or unwinding ties, cross-shareholders still retain the same basic stance and show no shift in behavior.

## 6. Conclusion

Our analysis leads to the following conclusions regarding the recent resurgence of cross-shareholding. The first critical point is that the resurgence is confirmed not by a higher cross-shareholding ratio, but by the expansion of cross-shareholding networks, which reflects a shift in corporate behavior. Thus unlike the 1990s, when a high cross-shareholding ratio made unwinding a critical issue for Japan's stock market, the current resurgence phase since fiscal 2005 should be viewed as a deviation of corporate behavior. The resurgence implies that more firms have been searching for and negotiating with willing candidates. This raises two issues—whether such behavior is beneficial to shareholders, and whether management can be held sufficiently accountable to shareholders.

Second, the change of players in the current resurgence raises two important points—banks have finished unwinding, while business firms are strengthening their cross-shareholding networks. The resurgence came to prominence because the behavior of both entities changed at the end of fiscal 2004. Thus the lead role of cross-shareholding appears to have shifted from banks and business firms to business firms.

To assess the implications of cross-shareholding in the future, it is crucial that we firmly understand the new structure of cross-shareholding described above.

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## Endnotes

1. See Nitta (2008a) and Nitta (2008b).

2. While no clear definition exists for an activist fund, it generally refers to relatively unregulated private investment institutions whose status as major shareholders allows them to influence corporate behavior with the aim of improving investment return.

3. This view is also corroborated by the growing understanding (following the August 7, 2007 Supreme Court ruling that upheld Bull Dog Sauce's poison pill against Steel Partners) that the validity and effectiveness of a takeover defense depends on a resolution of the annual shareholders meeting. Moreover, after the release of the report by the METI Corporate Value Study Group (2008), the current view holds that a resolution is important to confirm the intent of shareholders, but does not by itself establish a sound takeover defense.

4. A stronger cross-shareholding relationship may be desirable to investors if it achieves new synergies, or helps oust inappropriate shareholders who threaten the corporate value. However, investors are not in a position to clearly distinguish whether management's objective is defensive or otherwise.

5. By banks we refer to banks other than trust banks; by business firms, we refer to listed firms other than banks, trust banks, life and non-life insurance firms, securities firms, and securities finance firms. The same applies throughout this paper.

6. In this period, banks feverishly unwound cross-shareholdings as the stock market's plunge triggered an acute awareness of shareholding risk. At the same time, banks faced new constraints from the introduction of mark-to-market accounting and regulations to restrict banks' shareholdings. For a detailed explanation of the unwinding mechanism, see Miyajima and Kuroki (2003).

7. See Nitta (2008a) for details of the survey.

8. While foreign investors became net sellers in July 2008, the trend was greatly aggravated by the Lehman shock in September 2008. Moreover, almost all of the -2.33 percentage point drop in institutional shareholding ratio is explained by foreign investors, whose ratio dropped -2.28 pp (14.10% to 11.82%), compared to a -0.04 pp decline (7.19% to 7.14%) for domestic investors.

9. Most recently, the cross-shareholding ratio stood at 8.61% at the end of fiscal 2008, down -0.10 percentage point from a year ago. However, this minor decline should be regarded as an observation error rather than unwinding for the following reason. The cross-shareholding status of listed firms is confirmed using the *Database of Major Shareholders* (Toyo Keizai Inc.) and detailed tables of the *Yuka Shoken Hokokusho* (Nikkei NEEDS). In the latter case, firms need not disclose shareholdings that are valued on the balance sheet at less than 1% of capital. Since the Nikkei 225 average fell 35.3% in fiscal 2008, some shareholdings likely fell in value below the reporting requirement and were not disclosed. As the level of disclosure declines, fewer cross-shareholding ties can be observed.

10. As noted in endnote 9, this fluctuation falls within observation error.

11. The main costs are associated with searching for and negotiating with candidate firms, financing the purchase of cross-held shares, foregoing business investment opportunities, incurring market risk of shareholdings, and making management accountable to investors for strengthening cross-shareholding ties.

12. The large jump in unknown cases in fiscal 1999 is due to looser disclosure requirements of the *Yuka Shoken* detailed tables for the period ending March 2000. Under the new disclosure rules, the minimum balance sheet value for reporting of individual securities increased fivefold, from 0.2% to 1% of capital (see also endnote 9).

13. Although market valuation of shareholdings became mandatory from the period ending March 2002, it was allowed starting in the period ending March 2001. Thus the unwinding that occurred in this timeframe can be interpreted as a preparation for the new rules.

14. According to Miyajima and Kuroki (2003), although cross-shareholdings were basically unwound in a harmonious manner based on mutual consent, the unwinding phase from the late 1990s saw an increase in non-harmonious and hostile sell-offs.

15. It should be noted that all cross-shareholding cases are counted if they have been confirmed in the current or previous fiscal year, even including cases that were completely unwound in the current year. The sharp decrease of cross-shareholding cases after fiscal 1999 can be attributed to the relaxation of disclosure requirements (see endnote 12).