How Companies View Their Ties With Financial Institutions

The Sixth NLI Business Climate Survey Reveals Expectations for the "Big Bang"

by the Industrial Research Dept.

Introduction

The Sixth NLI Business Climate Survey was conducted in January and February 1998 by Nippon Life Insurance Co. in cooperation with NLI Research Institute. The survey mainly covered second-tier and small and mid-size companies nationwide (4,808 responses were received), asking corporate managers their views on recent changes in the financial environment, and on the "Big Bang" reforms slated to begin on April 1.

The survey results reflect the bleak financial conditions companies are presently struggling with: (1) interest in the Big Bang was still limited to a portion of companies, with small and mid-sized companies outside the metropolitan areas not fully aware of its implications; (2) companies that are already aware of the Big Bang (mainly large companies with city banks as their main bank, and small and mid-sized companies in strong industries) predict that the Big Bang will lead to greater diversity in banking transactions and increased transactions with specific financial institutions; (3) while competition among financial institutions is expected to intensify, companies do not expect the competition to yield many benefits, and only 4 percent predict lower financing costs; and (4) nonetheless, almost 80 percent of companies seek lower financing costs from financial institutions.

1. Difficulty Acquiring Loans and Rapid Deterioration in Cash Management

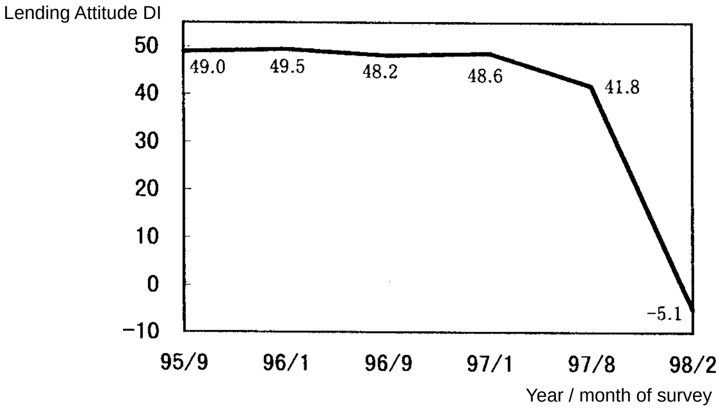
(1) Lending Stance of Financial Institutions Tightens Rapidly

The most conspicuous change from the previous survey (August 1997) is the tighter lending stance of financial institutions. In a marked change from the past five surveys, the present survey reveals the severity of the credit situation for the first time.

According to the survey, the proportion of companies reporting a tight or somewhat tight lending stance among financial institutions rose to 29.8 percent from 5.2 percent in the previous survey, while the proportion reporting an easy or somewhat easy stance was only 16.3 percent, down substantially from 55.8 percent in the previous survey. This caused the diffusion index

(DI) for lending stance, or the proportion of companies reporting an easy stance minus those reporting a tight stance, to plunge from 41.8 in the previous survey to -5.1 (Figure 1).

Figure 1 Lending Attitude DI

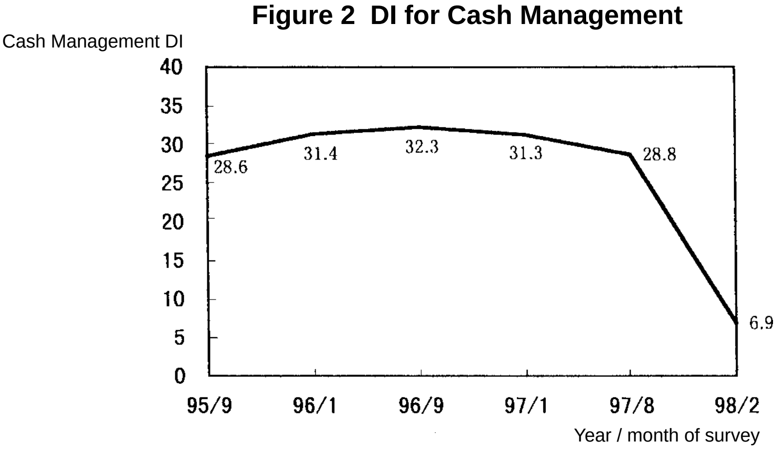


Note: The DI is calculated as follows.
(% companies reporting "lenient attitude")
+ (% reporting "somewhat lenient" x 0.5)
- (% reporting "somewhat strict" x 0.5)
- (% reporting "strict").

(2) Sharp Deterioration in Cash Management

As financial institutions toughen their lending stance, companies are left struggling with cash management. The proportion of companies who describe present conditions as unconstrained or somewhat unconstrained has declined, while those experiencing severe or somewhat severe conditions has increased. As a result, the DI for cash management (the percentage of companies reporting unconstrained conditions minus those reporting difficult conditions) plunged from 28.8 in the previous survey to 6.9 (Figure 2).

Figure 2 DI for Cash Management



Note:The DI is calculated as follows
(% companies reporting "unconstrained")
+ (% reporting "somewhat unconstrained" x 0.5)
- (% reporting "somewhat strict" x 0.5)
- (% reporting "strict").

2. Increasing Corporate Liquidity and Ties to Financial Institutions

Amid the series of failures among financial institutions since last fall, 17 percent of companies state that they have either changed the financial institutions they use or are considering doing so (Table 1).

Table 1 On Changing Financial Institution

		Changed or considering changing	Begun considering changing	Quit doing business with some financial institutions	Increased new financial institutions	Changed main bank	No change
All industries		**17.0**	**3.8**	**6.2**	**6.3**	**0.7**	**82.4**
Industry	Manufacturing	15.4	3.4	5.8	5.3	0.9	84.1
	Steel	18.7	1.7	10.2	6.8	0.0	81.4
	Non-manufacturing	18.2	4.2	6.4	7.0	0.6	81.2
	Communications	30.2	2.3	2.3	25.6	0.0	69.8
	Information services	19.1	4.8	7.6	4.8	1.9	81.0
	Specialized services	13.5	0.0	13.5	0.0	0.0	86.5
	Bus., prof., & mgt. services	20.8	2.5	8.2	10.1	0.0	78.6
Company size	Large	21.3	5.9	11.7	3.4	0.3	78.3
	Second tier	17.4	4.0	6.5	6.4	0.5	82.2
	Small & mid-size	16.5	3.6	5.6	6.5	0.8	83.0
Main bank	City bank	18.8	4.1	7.0	6.9	0.8	81.2
	Regional bank*	13.4	2.8	4.5	5.7	0.4	86.5
	Shinkin bank,credit cooperative	22.7	6.2	4.1	12.4	0.0	77.3
	Long-term credit bank, trust bank	21.8	8.0	8.0	5.1	0.7	78.3
	Public financial institution	18.3	2.8	6.6	6.6	2.3	81.7
	Other	18.2	5.1	6.1	4.0	3.0	81.8

Note: Totals do not add up to 100 due to incomplete responses.
＊ Includes member banks of the Second Association of Regional Banks.

Asked about changes in the use of financial institutions amid the recent failures among financial institutions, only 0.7 percent report changing their main bank, while 6.2 percent have quit using some financial institutions, and 6.3 percent have added new financial institutions. Moreover, 3.8 percent have begun considering making a change.

Looking for patterns by industry, we see that specialized services (13.5 percent) and steel (10.2 percent) lead in severing ties with some financial institutions, while new financial institutions have been added most frequently in communications (25.6 percent) and business, professional, and management services (10.1 percent).

By company size, 11.7 percent of large companies have quit using some financial institutions, while only 3.4 percent have added new financial institutions. Among second-tier and small and mid-sized companies, these two alternatives are more evenly balanced.

By main bank, the largest proportion of companies that report making no change in financial institutions are those with regional or second-tier regional banks as their main bank (86.5 percent). On the other hand, a high proportion of companies with credit associations as their main bank have added new financial institutions (12.4 percent).

3. Overwhelming Demand for Lower Cost of Funds

(1) Financing is More Important Than Asset Management

Asked what they seek from financial institutions as a result of the Big Bang, companies expressed concerns that strongly reflect recent tight credit conditions.

The most common result sought by far was for low-cost funds (78.9 percent), followed by provision of comprehensive services including banking, insurance, and securities (40.1 percent). On the other hand, demand was relatively low regarding asset management matters such as the offering of high-yielding financial products (10.4 percent) and expert advice on asset management (8.9 percent). But there was strong demand regarding business support services such as the introduction of customers and business contacts (27.7 percent), and advice and consulting on overall corporate management (20.2 percent; Table 2).

Table 2 What Companies Seek from Financial Institutions

(Multiple response; %)

		Low financing cost	Comprehensive services including banking,securities, insurance	Financial products offering high returns	Expert advice on asset management	Advice and consulting on overall corporate management	Introduce customers
All industries		**78.9**	**40.1**	**10.4**	**8.9**	**20.2**	**27.7**
Industry	Manufacturing	79.0	44.2	10.5	9.1	21.3	20.7
	Materials	81.7	***47.3***	9.7	7.8	19.1	18.6
	Processing	77.7	42.6	10.8	9.7	22.4	21.7
	Non-manufacturing	79.1	37.1	10.4	8.7	19.1	33.4
Company size	Large	77.9	***55.5***	13.1	9.7	15.5	18.6
	Second tier	78.1	43.6	11.1	10.8	19.6	25.9
	Small & mid-size	79.3	37.7	9.9	8.3	20.8	***29.2***
Main bank	City bank	79.1	41.3	10.4	8.7	20.7	27.4
	Regional bank*	80.5	38.3	8.6	8.9	21.7	***29.3***
	Shinkin bank, credit cooperative	84.5	41.2	6.2	9.3	17.5	19.6
	Long-term credit bank, trust bank	***87.7***	42.8	***14.5***	5.8	15.9	18.8
	Public financial institution	85.9	39.0	11.3	6.6	19.7	27.2
Industry conditions	Good (good + somewhat good)	75.2	***45.2***	11.2	10.2	20.8	22.8
	Normal	79.4	41.2	9.5	8.9	18.6	26.1
	Bad (bad + somewhat bad)	79.8	38.4	10.6	8.5	20.7	***29.8***

Note: Totals do not add up to 100 due to multiple responses.
* Includes member banks of the Second Association of Regional Banks.

(2) Smaller Companies Seek Low-Cost Funds

By industry conditions, we note that a high proportion of companies in the stronger industries seek comprehensive services from financial institutions, while a high proportion of companies in ailing industries want financial institutions to introduce customers. The desire for low-cost funds are high in general, but lower among companies in industries that are doing well.

By company size, the desire for low-cost funds increases with smaller company size, while the desire for comprehensive services increases with larger company size. In addition, the desire for introduction of customers and for advice and consulting on corporate management increase with smaller company size.

4. More Transactions with Specific Financial Institutions

(1) Most Companies Predict Diversification of Transaction Types

When asked how they expect their relationship with financial institutions to change as a result of the Big Bang, companies responded most frequently that the types of transactions would diversify (50.5 percent), followed by an increase in transactions with specific financial institutions (34.7 percent). Meanwhile, 16.6 percent expect to use more financial institutions and 10.0 percent expect to use fewer. Thus apparently most companies predict conducting a more diverse range of transactions with specific financial institutions. The proportion of companies expecting no change in their present relationships with financial institutions is 27.7 percent, while only 3.8 percent expect to change their main bank (Table 3).

Table 3 Predictions Regarding Change in Relationship with Financial Insitition

(Multiple response; %)

		Type of transactions will diversify	Closer ties with specific financial institutions	Do business with more financial institutions	Do business with fewer financial institutions	Will change main bank	No change
All industries		**50.5**	**34.7**	**16.6**	**10.0**	**3.8**	**27.7**
Company size	Large	***65.2***	***44.8***	16.9	17.9	1.7	12.8
	Second tier	53.1	37.0	15.5	11.8	2.4	25.7
	Small & mid-size	48.3	33.1	16.9	8.8	4.5	***29.8***
Main bank	City bank	52.8	38.3	16.9	10.1	4.2	24.9
	Regional bank*	48.9	31.8	16.8	9.5	2.9	30.6
	Shinkin bank,credit cooperative	47.4	27.8	11.3	14.4	7.2	***33.0***
	Long-term credit bank, trust bank	***54.3***	31.2	19.6	15.2	3.6	26.8
	Public financial institution	47.9	34.3	17.8	8.0	4.7	30.0
Industry conditions	Good (good + somewhat good)	53.3	36.4	***20.2***	8.6	1.8	24.2
	Normal	47.7	32.7	15.4	9.0	3.4	31.3
	Bad (bad + somewhat bad)	50.8	35.1	16.0	10.9	4.2	27.5

Notes: Totals do not add up to 100 due to multiple responses
＊Includes member banks of the Second Association of Regional Banks.

(2) Companies in Strong Industries Expect to Use More Financial Institutions

Company size is positively correlated with predictions of an increase in transaction diversity and use of specific financial institutions. In addition, since the same pattern holds for expectations of using financial institutions, larger companies are apparently more prone to limit the number of financial institutions.

However, among companies in healthy industries, only 8.6 percent predict the number of financial institutions used to decrease, compared to 20.2 percent who predict an increase. Thus we can infer that predictions of using fewer financial institutions are affected by the severity of financial conditions in the future.

By main bank category, we note that predictions of greater use of specific financial institutions are most common among companies with city banks as their main bank, while predictions of greater transaction diversity are highest among companies with trust banks as their main bank. In addition, predictions of no change in present banking relationships are high among companies with credit cooperatives and regional banks as their main bank.

5. Only a Minority Predicts Financial Competition will be Beneficial

(1) One-Third Predict Greater Competition in Financial Industry

When we asked companies how they predict financial institutions to change their stance toward companies as a result of the Big Bang, the most common response was for competition among financial institutions to intensify (33.5 percent), followed by greater diversity of financing methods (20.0 percent), and no change (16.3 percent; Table 4).

Moreover, while 14.4 percent predicts that lending attitudes will worsen, only a small minority predicts that the Big Bang will produce benefits such as enhanced information services (10.0 percent) and lower financing costs (3.9 percent). Considering the earlier result that almost 80 percent seek lower financing costs, this indicates just how bleak most companies see their prospects ahead to be.

(2) Weak Industries Predict a Worse Lending Stance

By company size, predictions of more intense competition among financial institutions are cited most frequently by large companies, while predictions of a more severe lending stance are highest among small and mid-sized companies.

By industry conditions, predictions of more intense competition among financial institutions and of greater diversity in financing methods are highest among companies in healthy industries, while predictions of a worsening lending stance are highest among companies in ailing industries.

By main bank category, expectations of more intense competition among financial institutions and of greater diversity in financing methods are highest among companies with city banks as their main bank (35.5 percent and 21.6 percent respectively), while expectations of a stricter lending stance are highest among companies with trust banks as there main bank (26.8 percent). Also noteworthy is the result that the proportion of companies with credit associations as their main bank who expect lower financing costs (8.2 percent) is over twice the all-industry average of 3.9 percent.

Table 4 Prediction Regarding Changes at Financial Institutions

(% of total)

		More competition among financial institutions	Financing methods will diversify	Lending stance will tighten	Information services will become enhanced	Financing cost will decline	No change
All industries		**33.5**	**20.0**	**14.4**	**10.0**	**3.9**	**16.3**
Company size	Large	***45.5***	18.6	11.7	11.4	2.4	4.8
	Second tier	36.1	22.9	12.7	10.4	2.7	12.6
	Small & mid-size	31.7	19.2	***15.2***	9.8	4.4	18.5
Main bank	City bank	***35.5***	***21.6***	14.0	9.7	3.7	14.3
	Regionalbank*	32.0	19.6	14.0	10.2	4.2	18.6
	Shinkin bank,credit cooperative	28.9	17.5	***20.6***	6.2	8.2	16.5
	Long-term credit bank, trust bank	34.1	20.3	***26.8***	2.2	0.7	12.3
	Public financial institution	33.8	18.3	14.6	8.0	6.1	17.4
Industry conditions	Good (good + somewhat good)	***37.7***	***22.2***	9.5	9.3	3.5	16.2
	Normal	32.9	19.9	10.4	10.3	4.7	20.4
	Bad (bad + somewhat bad)	32.7	19.4	***17.4***	10.1	3.7	14.8

Note: Totals do not add up to 100 due to incomplete responses.
＊ Includes member banks of the Second Association of Regional Banks.

6. 40 Percent are Receptive to Foreign Financial Institutions

Asked whether they would do business with foreign financial institutions if approached with better financial products or services, only 3.7 percent responded with a strong affirmative. However, when combined with those who would consider the matter, we find that almost 40 percent are receptive to the idea (Table 5).

Table 5 Response to Foreign Financial Institutions

(% of total)

		Start transacting with (or considering)	Will start actively	Will consider seriously	Will not start	Don't know
All industries		**38.3**	**3.7**	**34.6**	**17.4**	**43.4**
Industry	Manufacturing	38.8	3.2	35.6	17.7	42.8
	Transport machinery	46.6	1.7	44.9	15.2	38.2
	Electric machinery	44.4	3.3	41.1	14.9	38.2
	Steel	44.1	3.4	40.7	8.5	47.5
	Non-manufacturing	38.2	4.1	34.1	17.0	44.1
	Information services	40.0	8.6	31.4	14.3	45.7
	Personal services	35.0	8.5	26.5	17.1	47.0
	Specialized services	37.8	8.1	29.7	16.2	45.9
Company size	Large	4.6	44.9	13.4	36.7	0.4
	Second tier	2.7	34.2	17.7	45.1	0.3
	Small & mid-size	4.0	34.1	17.6	43.6	0.7

By industry, receptivity to foreign financial institutions exceeded 40 percent for transport machinery, electric machinery and steel, industries in which globalization is advanced. While strong affirmative responses were low in general, proportions were relatively high in service industries such as information services (8.6 percent), personal services (8.5 percent), and specialized services (8.1 percent). By company size, large companies lead in both actively starting business and considering it.

As stated earlier, the proportion of companies that have changed or considered changing their financial institutions is 17.0 percent. Moreover, 26.6 percent of the companies predict an increase or decrease in the number of financial institutions (multiple response). Considering that as many as 38.3 percent are receptive to (foreign) financial institutions offering better financial products or services, it seems reasonable to conclude that as the Big Bang raises the quality of financial products and services, more companies are likely to change their financial institutions.

While we found that only some of the companies seem to grasp the implications of the Big Bang, this can also be interpreted to mean that today's severe conditions have simply diluted corporate expectations regarding the Big Bang.

We can infer that the issues that concern companies most at present are the difficulty in acquiring bank loans, deteriorating earnings, and cash management problems. Thus expectations and predictions regarding the Big Bang tend to reflect efforts to overcome present problems and short-term expectations. Meanwhile, however, transactions with financial institutions are showing signs of greater flexibility, and if this leads to greater benefits, companies will be more optimistic. Thus with the progress of Big Bang, which began in April 1998 with the lifting of foreign exchange controls, long-term perspectives will increasingly prevail in the choice of financial institutions, and companies will shift their attention to fundamental issues such as ways to take advantage of the liberalization of financial transactions.