OCCASION

This publication has been made available to the public on the occasion of the 50th anniversary of the United Nations Industrial Development Organisation.

DISCLAIMER

FAIR USE POLICY

CONTACT

Please contact publications@unido.org for further information concerning UNIDO publications.

For more information about UNIDO, please visit us at www.unido.org

UNITED NATIONS INDUSTRIAL DEVELOPMENT ORGANIZATION
Vienna International Centre, P.O. Box 300, 1400 Vienna, Austria
Tel: (+43-1) 26026-0 · www.unido.org · unido@unido.org

D03853

United Nations Industrial Development Organization

Distr.
LIMITED

ID/WG.138/1
13 October 1972

ORIGINAL: ENGLISH

Expert Group Meeting on Industrial
Reorganization and Mergers

Vienna, 7 - 10 November 1972

POLICIES AND INSTITUTIONS TO PROMOTE INDUSTRIAL REORGANIZATION AND MERGERS: THE EXPERIENCE OF JAPAN [1]

by

Takeshi I ayama
Assistant to the Director
Planning and Policy Division
Ministry of International Trade and Industry
Japan

1/ The views and opinions expressed in this paper are those of the author and do not necessarily reflect the views of the Secretariat of UNIDO. This document has been reproduced without formal editing.

id.72-5945

I. The changing structure of the industrial sector

1. With the rapid growth of the Japanese economy, the industrial structure has gradually approached the pattern prevailing in the advanced Western countries. During the period from 1955 to 1969, the share of the primary sector (agriculture, forestry and fisheries) in total national product declined from 21% to 8%, while that of the secondary sector (mining, industry and construction) increased from 32% to 42% and that of the tertiary sector (transporation, communication, public services, commerce and utilities) rose slightly from 47% to 50%.

2. Within the secondary sector, one may note the growth of manufacturing industry, whose share of total product rose from 29% in 1955 to 32% in 1969.

3. An examination of the individual manufacturing branches shows a marked increase in the output of the heavy and chemical industries. While total manufacturing production rose 8 times from 1955 to 1969, the output of heavy and chemical industries (metals, machinery, hcemicals, petro-products, etc.) expanded above 11 times and that of the light industry sector (textiles, foodstuffs and others) increased only 6 times. As a result, the share of the heavy and chemical industries in total manufacturing production rose from 45% to 60%.

4. The machinery industry has played the biggest role in the growth of heavy and chemical industries. Machinery production in the period considered increased 16 times and its share in manufacturing production rose from 15% to 32%. Particularly marked were increases in such equipment as machine tools, electrical motors, electrical motors, electrical generators, buses, trucks and steel vessels as well as durable consumer goods such as passenger cars, radio and television receivers, and electric refrigerators. During this period, production of capital goods and that of durable consumer goods increased 12 times and 22 times, respectively.

5. Through these transformations of the industry, the present structure in selected branches of industry is formed as follows in terms of concentration (percentage supplied by the first 6 firms in 1969).

- Textile industry	26%
- Iron & steel industry	73%
- Petro-chemical industry	63%
- Automobile industry	85%
- Camera industry	62%
- Watch & clock industry	57%

6. The branches of industry in which changes in the structure have been most pronounced in the last five years from 1964 to 1969 are:

(i) More than 30% increase of grwoth of share supplied by the first 6 firms;

- Silk yarn	38%	→ 95%
- Spring	34%	→ 55%
- Parts of motor vehicles	16%	→ 26%
- Yarn of animal hais	38%	→ 53%
- Kitchen utensil	49%	→ 68%
- Staple fiber	31%	→ 43%
- Soap	42%	→ 56%

(ii) 20 - 30% increase of growth of share supplied by the first 6 firms;

- News-print paper	53%	→ 67%
- Telecommunications apparatus	42%	→ 53%
- Glass bottle for thermos	45%	→ 56%

7. The trend in industrial reorganisation in terms of the number of merger applications considered by the Fair Trade Commission in recent years has been as follows:

- 1957 - 1961: 400 to 600 cases annually
- 1962 - 1967: 700 to 1,000 cases annually
- 1968 - 1971: more than 1,000 cases

II. Policies affecting industrial reorganization and mergers

8. Japanese industrial policy seeks to promote structural development in the three following directions*:

* See Chap III in detail.

(1) An increase in the unit or scale of production, investment and equipment to an international level. In particular, specific efforts are being made to raise production scales or units in the automobile, oil refining, petro-chemical, iron and steel, and ammonium processing industries.

(2) Joint investment and efforts to coordinate production between different firms with a view to making the entire industry more efficient. Examples include coordination in the production of machine-tools and joint investment in the refining and smelting of non-ferrous metals.

(3) Industrial concentration, sometimes resulting in mergers or acquisitions. A number of positive efforts have been made in this direction, particularly with respect to smaller business and in the textile industry.

9. The policy making which facilitates and encourages industrial reorganization will be initiated by MITI (Ministry of International Trade and Industry) through the various consultative councils and discussion groups in which representatives of industry and banking as well as qualified disinterested persons join with Ministry officials. On the basis of this preparatory work and discussion, the most desirable scale or magnitude of production and investment in specific sectors is defined and made public by the Government. Private industry cooperates voluntarily in making the structural changes needed to meet these targets and this cooperation is facilitated by the granting of tax and other financial incentives, the precise pattern of such inducements depending upon the particular industry and the objectives sought.

10. Apart from encouragement of structural improvements in a wide variety of industrial branches, specific programmes have been launched under special legislation [illegible] a limited number of industries whose development or adaptation is of particular importance to the national economy. These programmes are briefly described below:

(1) <u>Modernization of the machinery and electronics industries</u>

Special legislation has been adopted facilitating the development and modernization of these industries and providing government financial aid for the purpose.

In the case of <u>machinery</u>, the branches upon which most attention is being concentrated are: machine-tools, chemical processing machinery and materials-handling equipment. The need here is mainly for technological innovation and for rationalization of the industry.

As regards <u>electronic products</u>, while it is true that Japan is a very big producer of consumer electronics, the main promotional emphasis is rather on electronic computers, integrated circuits, etc. In these fields, Japan still suffers from a technological lag, and the Government seeks to encourage greater efficiency, a raising of the technological level, and an increased sophistication of product.

Under special legislative enactment, the Japan Development Bank provides about $30 million annually in financing for the machinery and electronics industries. Credits totalling some $41 million per year are made available to facilitate electronic computer rental arrangements; i.e., the Japan Electronic Computer Corporation, the sole purchaser of computers from the manufacturers, leases them in turn to the users, and these arrangements require very substantial financing. Moreover, the manufacturers are allowed for tax purposes to include up to 15% of their earnings as retained earnings in their profit and loss statements in order to strengthen their financial position against any possible failure to pay on the part of Electronic Computer Corporation.

(2) Adaptation of the textiles industry. This is an industry which developed early and which now has to consider its role in the perspective of the present-day world economy. Government promotion measures are designed to stimulate modernization of the industry by helping sophisticate the processing stages of spinning, weaving and dyeing, and to that end, tax incentives and other financial support are provided. In 1970, the Japan Development Bank is expected to supply $14 million in financing to the textile industry, while some $46 million will be provided to the smaller firms in the sector under the programmes for small and medium-sized businesses. However, this assistance - in the form of credits and loans, not subsidies - is designed only to support "scrap and build" operations, i.e., the scrapping of obsolete equipment and the building of completely new facilities.

(3) Restructuring of the coal-mining industry and redevelopment of coal-mining areas. As part of the "energy revolution", petroleum products have been superseding coal due to their lower cost and other advantages. Coal production has been declining by some 2 million to 3 million tons annually. At the same time, despite the change in the structure of energy demand, Japanese industry, especially iron and steel, continues to have substantial coking coal requirements, only a part of which the coal-mining industry in Japan can meet, and thus much reliance has had to be placed on imports.

It is necessary to restructure and rationalize the Japanese coal-mining industry in these circumstances. But it is inevitable that some mines have to be closed, and it has been necessary to minimise the adverse effects which such closings have on the economy and society.

Thus, on the one hand, programmes have been established with a view to assisting in the reconstruction of the coal-mining industry through government loans and other financial aid. And, on the other hand, there are programmes which aim at (i) alleviating the social harm engendered by mine closings through, e.g., subsidies designed to provide relief to workers who lose their jobs, and (ii) fostering the diversification of the economy in the mining areas through industrial site development and loans to facilitate the establishment of new industries. The various government activities in this field are carried out by specially established public bodies: the Coal-Mining Rationalization Corporation, the Coal-Mining Area Development Corporation, the Coal-Mining Damage Recovery Corporation.

11. On the other hand, the Anti-Monopoly Act acts as an abstacle to industrial reorganization. Under the Anti-Monopoly Act, mergers, transfers of businesses, stock-holding or interlocking directorates are prohibited where they "may substantially restrain competition in any particular field of trade" or where "unfair business practices have been employed".

12. With respect to mergers and transfers of businesses, a prior report to the Fair Trade Commission is required, and such a report is also to be filed in connection with interlocking directorates and stockholding by a company whose assets exceed a certain limit. In all the above-mentioned cases, the Commission may order the entrepreneur concerned to file a report, dispose of the whole or some of his stocks, transfer part of the business, resign from his position as an officer in the companies concerned, or any other measures necessary to eliminate a violation.

13. The Commission may issue a complaint or may make a recommendation with a view to ordering the above-mentioned measures. With respect to mergers and transfers of businesses, it must do so within 30 days after the report has been filed (extension of the period by not more than 60 days is possible with the consent of the companies concerned). Moreover, upon the application of the Commission, the law courts may, where they deem the matter to be of urgent necessity, order the parties concerned to cease the activity suspected of being illegal.

14. A financial company is in principle prohibited from holding stocks in a domestic company in excess of 10% of the outstanding stocks (this is permissible if approved by the Commission), and the establishment of a company which is wholly a holding company in nature is completely prohibited.

15. At the same time, however, the efficacy of the competitive system should be maintained. This objective may sometimes require a partial suspension of the usual competitive conditions in given cases and given sectors. The Anti-Monopoly Act does in fact permit certain forms of cartelization-against business recessions or in order to carry out rationalization - in specific cases approved by the Fair Trade Commission.

III. Government intervention to promote industrial reorganization and mergers

16. The institutional machinery responsible for formulating policy for industrial reorganization and mergers and implementing these measures is Ministry of International Trade and Industry (MITI).

17. MITI's jurisdiction is wide and varied and primary functions are:

(1) The planning and implementation of global, or horizontal, industrial policies which are common to all the sectors; e.g. industrial reorganization, industrial land allocation, distribution and consumer protection, etc.;

(2) The planning and implementation of sectoral industrial policies aimed at promoting the sound development of the industries involved;

(3) The planning and implementation of international trade policies and policies with respect to economic aid and cooperation;

(4) The planning and implementation of the environmental protection against industrial disutilities and mine safety policy;

(5) The administration of the small and medium-sized enterprises;

(6) The planning and implementation of the technological development policy.

18. The role of the MITI in implementing industrial policy is essentially one of persuading, facilitating and encouraging industry to move in the desired directions.

19. Action taken voluntarily by industry on the basis of a consensus arrived at between MITI and industry is the generally sought objective. The close and continuous contacts provide the occasion for thorough exchange of views, the detailed procedures used for reaching consensus being tailored to the characteristics of the particular industry or branch. The guidance and recommendations offered by the MITI are based on the fullest knowledge of the economic situation and trends that on intensive information gathering and processing activity can provide.

20. One source of knowledge of developments in industry is the sustained MITI- business contact. In addition, Japanese firms provide a steady flow of data in submitting various reports and statements required by law.

21. MITI's basic attitude toward industrial reorganization and mergers has been:

(1) Reorganization should correspond with the changes at home and abroad;

(2) Such reorganization should be carried out based on each industry's given conditions.

22. Essentially, industrial reorganization and mergers of an industry will depend on its supply-demand condition, on the management skill, on the level of technology and so forth, and the basic form of reorganization must be seeked for by sector.

23. From that point of view, MITI's policy on this matter might be delineated in the following forms according to types of industry.

(1) Mass-production industry - producer's goods industry;
Such industries as iron and steel, petro-chemical, paper and pulp, etc. require big plants in the production and, hence, can enjoy economies of scale. On the other hand, excessive-investment and excessive-production must be adjusted for efficient management of an industry. Timely replacement of the plant equipment, therefore, will have to be performed. Development of new technology very often makes useless the old production system and a little delay of the introduction of new machines sometimes becomes a matter of life and death of a firm and an industry, eventually. In these industries, therefore, the policy for reorganization should take such forms as invest-in-turn, joint-investment, and mergers.

(2) Mass-production industry - consumer's goods industry;
In the industries like automobile and synthetic fibers where mass-production along with product - differentiation is taking place, the situations to be tackled are more complicated. They must obtain stable and fairly a large amount of demand through quality control, advertizing, dealer - customer royality,

standardization of parts and so forth. In these industries, the cooperative business such as exchange of technology, use of common parts, joint-marketi.g at home and abroad, adjustment of pr duction lines, etc. sh ld be encouraged eforo merger.

(3) Technology-oriented industry;
Such technology-oriented industries as (as electronics, aircraft, nuclear) energy, machine-tool, etc. need a large amount of investment for research and development. But a single Japanese firm is not financially strong enough, and exchange of technology, joint research, joint investment, etc. should be inspired along with mergers.

(4) Ordered and lotted production industry;
Ball and roller bearing, pressing machines, dyeing and finishing machines, etc. are based on orders and lots in the production. For the efficient production of these specialized areas, therefore, organization of cartels, syndicatos, cooperative business, joint-ventures, etc. should be encouraged for the reorganization of the industry.

(5) Labor-intensive industry;
Such industries as miscellaneous manufactured articles, textile and spinning, etc. are mainly engaged by numerous small and medium-sized enterprises where traditional way of production is still prevailing and labor-intensive. Therefore, the rationalisation and modernization of production through financial incentives for "scrap and build" and pr duct differentiat n through development of new products of higher quality and design should be pr moted.

Based on this recognition, further measures such as cooperative management, tying arrangement, syndicates, mergers, etc. should be invited for more efficient reorganization of an industry.

(6) Distributive trades;
The wholesalers and retailers of all sorts of goods from groceries to automobiles are expected to cope with the stabilization of consumers' prices through simplification and rationalization of trade practices and through reorganization of dealer-consumer system.

For that, mergers, cooperative management and chain-store should be fully encouraged.

24. Upon this basic idea, MITI is employing necessary measures for the promotion of industrial reorganization and mergers.*

* See Chap. II for special sectoral reorganization and mergers' programmes.

25. Fiscal advantages, for example, are accorded to promote modernization, rationalization and reorganization with particular emphasis on the smaller enterprises, as well as to stimulate an intensified industrial research effort and similar goals. And, in some cases, credits and loans are made available from public funds through the Japan Development Bank and other government financial institutions, but these are generally auxiliary to financing by private sources. The role of the JDB is, in fact, regarded mainly as that of a catalyst encouraging the types of industrial development aimed at by government policy, and the bulk of its credit facilities are extended to promote industrial reorganization, the development of desirable new industries, commercialization of new technologies, develoment of stable sources of energy and regional industrial development. In addition, a number of specialized government instituions have been established to help finance, respectively, the adaptation of small and medium-sized enterprises, the development of petroleum and metal resources, the reorganization of the coal-mining industry and the redevelopment of the coal mine areas.

IV. Lessons to be drawn from experiences in Japanese industrial development

26. In the post-war period, the guiding principle of industrial policy has always been to promote economic vitality based on the initiative and ingenuity of enterpreneurs, and an optimal distribution of resources, through the exercise of free competition. The principle of free competition was introduced and gradually reinforced in Japan through the dissolution of the Zaibatsu, the adoption of the Anti-Monopoly Act and the abolition of various economic controls.

27. It should be noted, however, that the post-war performance of the economy has not flowed simply and exclusively from the introduction of free competition. Foreign aid and the positive industrial policy of the Government have played a vital role in the development of a workable system based on free competition. Moreover, some modification of this principle was required for the swift recovery from the ruins of war.

28. Generally speaking, competition in the Japanese economy has tended to develop far more violently than in any other country. This tendency is attributable to an excessively large number of extremely small enterprises, existence of surplus labor, lack of labor mobility, and a close link between leading banks and manufacturing firms.

Such excessive competition has caused deterioration in the financial position of enterprises and obstructed the progress of rationalization. It is for these reasons that some measures were introduced to control competition: e.g., depression cartels, rationalization cartels, agreement among small firms and investment co-ordination. On the other hand, however, it must be noted that the transition from a closed to an open economy had exposed Japanese firms to growing competition from abroad.

29. In the view of the Japanese authorities, the harmonious adjustment of the two objectives involved here - that of strengthening the competitive power of Japanese industry internationally, and that of maintaining effective competition in the Japanese market - has required an appropriate selection of policies for industrial co-ordination.

30. Other forces promoting industrial reorganization have been:

(1) The desi e and need for large pr duction runs to a hieve greater efficiency and lower costs;

(2) The need for large investment in research and development which exceeds a single firm's financial capacity;

(3) The need for standardization of product quality and design in the industry.

31. The main benefits of reorganization have been:

(1) Rationalization of production, including closing down of inefficient units;

(2) Rationalization of distribution and marketing contributing to the stability and decrease of consumers and producers' prices;

(3) Rationalization of research and development to utilize the duplicated fund and skilled personnel;

(4) Rationalization of enterprencurship to meet the deterioration in the financial position caused by excessive competition.

32. The policy framework has not sufficiently excouraged and facilitated industrial reorganization and mergers under private initiative because of the excessive-competition among firms, and each firm has been reluctant to initiate the negotiation of industrial reorganization fearing the loss and decrease of the market share of his own. Therefore, government intervention has been, in most cases, inevitable in Japan.

V. Experience of interest to developing countries

33. Japanese experience in the industrial reorganization and mergers might warrant attention by developing countries since Japan once shared such problems as excessively large number of extremely small enterprises, existence of surplus labor, lack of labor mobility, etc. And, especially, the following aspects of the experience might induce developing countries' interests.

(1) The basic philosophy toward the maintenance of competitive system;

(2) Joint research and investment in the development of new products and technology;

(3) Standardization of products and parts to attain economies of scale;

(4) Improvement of managerial skill by introducing competition from abroad.

34. However, any kind of national policy cannot be a good policy unless it has concensus supported by people, firms, and industries. And concensus will be reached only when the peculiar conditions in a country are well recognized by them. Simple imitation and introduction of other countries' systems and methods may be easy but sometimes cost more. This might also be a lesson from Japanese industrial development. Japan's outstanding economic performance since the war is attributable largely to the close, purposeful cooperation between government, industry, the financial institutions and labor upon full recognition of each capacity. In this regard, MITI's guidance has been very appropriate and the nation's productive resources have been effectively marshalled towards the achievement of national economic objectives, leading to the build-up of internationally competitive industrial capacity in certain sectors.

35. In sum, industrial reorganization and mergers policy in developing countries will have to be appropriate in the sense that each country has its own development programme by sectors and the programme is prosecuted and supported by necessary measures in accordance with the situation. In this, Japanese experience might be of some help for developing countries and Japan seems to be ready to provide the necessary cooperation.

Annex A: Merger of Nippon Kangyo Ginko (the Hypothec Bank of Japan Inc.) and Daiichi Ginko (the First Bank Inc.)

(1) The product produced;
Banking.

(2) Number of enterprises involved;
two

(3) The reasons why the merger was needed;
To strengthen the procurement power of funds, to adjust regional and seasonal maldistribution of funds, to save the administrative costs, etc.

(4) The time of the merger, the benefits expected and the benefits realised so far;
Two companies were merged in 1971. Nippon Kangyo Ginko held numerous branch offices all over the country while Daiichi Ginko possessed them mainly in and around the three largest cities of Tokyo, Osaka and Nagoya; hence the main benefit of the merger was to consolidate the foundations of the business and transaction of both companies.

(5) Some comments on the merger;
Both companies had conflicts in ordinary banking business (acceptance of deposit, loans, etc.). By this merger, they were to occupy the first place among 14 largest city banks in terms of 1970's record in the balance of savings and in the balance of loans possessing the share of 13.8% and 14.4%, respectively. However, this merger was not regarded to be such that it "may substantially restrain competition in any particular field of trade", since rival companies like Fuji Bank (the share in the balance of savings 11.1%, the balance of loans 11.0%), Sumitomo Bank (10.9%, 10.5%) and Mitsubishi Bank(10.6%, 10.6%) remained still competitive and no substantial restriction was produced by the merger on the competition.

Annex B: Merger of Yawata Seitetsu (Yawata Iron and Steel Inc.) and Fuji Seitetsu (Fuji Iron and Steel Inc.)

(1) The pr duct produced;
Iron and steel.

(2) Number of enterprises involved;
Two.

(3) The reasons why the merger was needed;
Necessity to adjust the supply-demand condition; i.e., the development of large scale production method in iron and steel industry based on technological innovation was likely to cause excessive supply since in the demand side there was little hope to be enlarged at home and abroad.
Requirement to strengthen the technology level to cope with the development of efficient production system contributing to reduction of production costs, and to cope with the development of new products and higher quality seeking for a new market, was another factor to be considered. Demand to consolidate the firms' international competitiveness was another requirement. Facing the capital liberalization, the industry was to be exposed by severe competition with advanced countries' rivals with better management skill and technology in the production.

(4) The time of the merger, the benefits expected and the benefits realized so far;
The merger was approved in 1969, and the benefits expected were (1) efficient investment in equipments and research and development, (2) efficient allocation of raw materials and products through mass-importation based on long term contracts and through standardization of the products, (3) efficient distribution of products by rationalising transportation system and by adjusting the stock for regional difference in demand, (4) Unification of distributive channels by establishing warehouse and service-center, and (5) Computalization of management based on economies of scale in the production.

(5) Some comments on the merger;
The Commission issued a complaint considering the merger might

substantially restrain competition in some fields of trade such as rails for rail-road and hot-coils and also considering it might employ unfair busin ss practices. Th refore, some of the stocks were disposed of and part of the business was transferred to rivals. in the approval of the merger.

23.7.74