# "VENTURE BUSINESS" BOOM IN JAPAN

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## Preface

Only several years ago most of Japanese businessmen wondered what "venture business" was, but this word has now emerged in the high school textbook. During the recent nine months (Nov. 1982– July 1983) many venture capitals were established and this phenomenon is called the "second venture boom."

The purpose of this paper is to give an outline of this boom and to consider its perspective. Chapter I will treat the first venture-boom which appeared in 1972–4, and explain the background and some features of it. The second venture-boom we see now, will be discussed in the next chapter. In the final chapter I will point out some problems encountered in this boom and will express my opinion about some conditions for the development of venture capitals from now on.

## I. The First Venture Boom

Largely speaking, many kinds of Japanese booms after World War II were imported from U. S. A., and this principle may also be applied to the venture boom.

In only two years (Nov., 1972~Aug., 1974) eight venture capital companies were established. This matter was apparently influenced by the second venture boom in the U. S. A. where many big banks showed great concerns in the venture capital business and made many subsidiaries to invest to small businesses with high technologies or new management ideas (The companies of this kind are called "the venture business" in this paper. The word, "venture business" was originally stemmed from Japan but is now used in the U. S. A.)

Readers can see names, shareholders, dates of foundation and authorized capital of eight companies in Table I. In the feature of the first venture boom in Japan we can pick up the fact that both banks and security houses including "big four"* took part friendly in this boom, and in some cases

* The big four are Nomura, Nikko, Daiwa, Yamaichi and their total amount of financial resources may be match for that of the big banks.

TABLE I. VENTURE CAPITALS IN THE FIRST BOOM

| Name | Date of Foundation | Authorized Capital: ¥ mil. | Shareholders | | Remark |
|---|---|---|---|---|---|
| | | | Main | Sub | |
| Kyoto Enterprise Development | Nov. 1972 | 300 | Kyoto Keizai Doyukai | | March 1930 dissolutioned |
| Nippon Enterprize Development | Nov. 1972 | 900 | Long Term Credit Bank of Japan | Daiwa Security Co. | |
| *Sogo Finance | Dec. 1972 | 500 | Sumitomo Bank | | Changed to Factoring Co. |
| JAFCO[1)] | Apr. 1973 | 1,000 | Nomura Security Co. | Sanwa Bank | |
| Universal Finance | Dec. 1973 | 600 | Yamaichi Security Co. | Industrial Bank of Japan, Fuji Bank | |
| Central Capital | Jan. 1974 | 600 | Nikko Security Co. | Tokai Bank | |
| Tokyo Venture Capital | Apr. 1974 | 600 | Daiichi Kangyo Bank | Kangyo Kakumaru Security Co. | |
| Diamond Capital | Aug. 1974 | 500 | Mitsubishi Bank | Mitsubishi Trust Bank | |

* The former name is Nippon Venture Capital.
1) Japan Associated Finance Co.

TABLE II BALANCE SHEET OF A VENTURE CAPITAL
APRIL 1982 (¥ MILLION)

| Assets | | Liabilities and Capital | |
|---|---|---|---|
| Current Assets | 17,547 | Current Liabilities | 17,536 |
| Money at Call and Short Notice | 754 | Borrowing from Banks | 6,420 |
| Securities | 197 | Other Short Term Borrowing | 10,800 |
| Short Term Loans | 16,440 | Other Current Liabilities | 316 |
| Provision for Doubtful Debt | 109 | Capital and Reserves | 1,200 |
| Other Current Assets | 265 | Capital | 600 |
| Fixed Assets | 48 | Reserves | 600 |
| Investment | 1,141 | | |
| Investment to Securities | 1,043 | | |
| Other Investment | 98 | | |
| Total | 18,736 | Total | 18,736 |

Note: Compare short term loan with investment, you can find this company was not venture capital but money lender.

together established their companies.

This boom was a remarkable matter in those days, but their actual activities were not vigorous until the recent second boom. As a matter of fact they only had a few achievements in venture capital and instead offered financial services, factoring, leasing and discounting bills. This was only done as a side-businesses, and from the profit made by these side-businesses they made venture finance. Readers can see the matter above mentioned in Table II which is the copy of the balance sheet of a venture capital. If Readers compare "investment" with "short term loan" in Table II, it is clear that this company is not a real venture capital but merely a money lender. In many cases the biggest customers of these venture capitals were personal loan companies.

The disolution of the Kyoto Enterprize Development (KED) in 1980 and the diversion of the Nippon Venture Capital to the factoring proper company were symbolic matters of the first venture boom in Japan. KED was established by 31 local companies, 31 banks located in Kyoto and all the 63 members of Kyoto Stock Exchange Market. But 125 shareholders were apparently too many for such a small fund ¥300 millions to make single decision. In Japan too there is a proverb similar to "Too many cooks spoil the broth," "Too many captains lead the ship to the mountain" this was perfectly applicable in the case of KED. By reason of this boom's misfire we have to refer to the oil shock in 1973 in which most of venture capitals were confronted with great difficulties in finding possible customers. Replying to my question, a general manager of a venture capital said, "We opened our office and hoped to find venture businesses but we could not and our result was namely, much cry and little the wool."

In addition to this economic background, there was no general recognition of the roll of venture businesses in regenerating Japanese economy and little intention of banks to finance them. In those days big businesses still showed high demand for bankers' finance and there was no need for banks to seek new outlet of money.

Thirdly, Government assistances to foster the venture businesses was not fully arranged and the Board of Tokyo Stock Exchange has not yet shown any concern for reforming the regulation on enlisting companies to the Second Section Market and OTC Market.

## II. Some Aspects of the Second Venture Boom

Since August, 1982 new venture capital companies have found at the pace of one company per month. This rush is a symbolic phenomenon of this time so that many people are discussing on it. However, it is important to recognize that this second boom is consisted of other several factors and is originally only one aspect of small firms finance problems which happened several years ago in many countries. In this chapter I will describe the outlines of some aspects of this boom respectively.

TABLE III. VENTURE CAPITALS IN THE SECOND BOOM

| Name | The Date of Foundation | The Authorized Capital million Yen | Shareholders | |
|---|---|---|---|---|
| | | | Main | Sub |
| Nippon Investment Finance | Aug. 1982 | 1,000 | Daiwa Security Co. | Long Term Credit Bank of Japan |
| Sanyo Finance | Aug. 1982 | 10 | Sanyo Security Co. | |
| Nagoya Capital | Sept. 1982 | 50 | Okatoku Security Co. | |
| Yamaichi Uni-Ven | Nov. 1982 | 50 | Yamaichi Security Co. | |
| New Nippon Finance | Dec. 1982 | 500 | Shin Nippon Security Co. | IBJ |
| Wako Finance | Dec. 1982 | 300 | Wako Security Co. | IBJ |
| New Capital | Dec. 1982 | 10 | Yamatane Security Co. | |
| Marusan Finance | Mar. 1983 | 20 | Marusan Security Co. | |
| Okasan Finance | Apr. 1983 | 100 | Okasan Security Co. | IBJ |
| Kansai Venture Capital | May 1983 | 500 | Osakaya Security Co. | Daiwa Bank |
| Maruman Finance | June 1983 | 100 | Maruman Security Co. | Tokai Bank |
| Nikko Venture Capital | July 1983 | 800 | Nikko Security Co. | Mitsubishi Bank |
| Fuji Investment | July 1983 | 450 | Fuji Bank | Yasuda Trust Bank |

Note: Besides those in this table, there are falling ones in Japan. Techno-Venture, Madoc, Fidelity Japan, Jamile SI Pacific Technology Ventures, Magnam Venture Capital, System International.

## 1. Venture Capitals in the Second Boom

Readers can get some knowledges about the venture capitals established during the second boom (which began in 1982 and continues up to the present) in Table III. At first readers must notice that most of all main shareholders of these companies are security houses, and some banks are in the position of only sub-shareholder. Readers, comparing Table III with Table I, will be aware of a more interesting fact, that is, the shareholders of Nippon Enterprise Development in Table I are the same members of Nippon Investment Finance in Table III. But the order between the main and sub-shareholder is in opposition. What does this fact mean? Everyone will wonder why same members established another similar type of the company. A key to understand this strange matter is to comprehend the present condition of the conflict between banks and security houses. Since a detail description of this conflict might require me to write another paper, I will deal with this briefly.

The distinction between the bank and the security house is strictly defined by the Security Dealing Act, and Section 65 of this Act (a copy of the Regulation Q in the U. S. A.) prohibits banks from doing security-dealing. However with the revolutional change of financial structure, which broke out first in the U. S. A. with some inventions of new financial services like MMF (Money Market Fund) and was imported to Japan a couple of years ago, many banks asked to remove this regulation. At last in May 1981 the New Banking Act was enacted and it allows banks to deal in some kinds of securities. As a result, every banks can sell the Long Term National Debt since April 1983 and the Medium Term National Debt since October 1983. During six months (April-September) the sales amount of the Long Term National Debt by 13 city banks is over ¥200 billion. In addition, since last summer many banks launched a new type of deposit, so-called the National Debt Term Account. This deposit is epockmaking for banks and combines term deposit and the Long Term National Debt. Interest rate is very high, the average is 9.5% and the term is 10 years (the longest term of deposit is 3 years so far). This new deposit contributes to the huge amount as mentioned above.

Obviously this matter is a kind of invasion upon the proper field of security houses and therefore it is quite natural that they asked the Ministry of Finance to give them some counterparts, and they now are able to do security mortgage finance since June 1983.

It might be wrong if Readers think that banks and security houses confront in a wholesale way, because they always conflict in one aspect and at the same time cooperate in another aspect, for instance, in on-line banking service. According to Nikkei newspaper dated June 1, 1983, Mitsui Bank and Nomura Security Co. co-operate with on-line service using DDX (digital data exchange). But the former aspect is getting more serious and the competition for developing new financial commodities like the Medium Term National Debt Fund (so-called Chukoku Fund), which is similar to the Money Market Fund (MMF) in the U. S. A., continues up to the present. Chukoku

Fund was developed by security houses in Jan. 1980 and increased rapidly. The total balance at the end of Sept. 1983 is about ¥3,700 billion and net increase from June to August is ¥1,370 billion. This figure is bigger than 13 banks' total growth of term deposit during the same period.

Let's return to the foundation of Nippon Investment Finance, this case exposed severe confrontations typically. NED was originally founded by the Long Term Credit Bank of Japan with co-operation of Daiwa Security Co., but in the course of the confliction above-mentioned, Daiwa needed to make their own subsidiary. It is the same story between the Central Capital and the Nikko Venture Capital, the former was established by co-operation of the Tokai Bank and Nikko Securities. They took part together in the foundation of venture capital but their purposes were different at the first stage. Generally speaking, banks hope to maintain the long term relation with customers but security houses intend to seek short term capital gain.

Securities houses are the leaders of this enthusiasm, on the contrary the banks' attitude is rather cool. This is the most remarkable feature in this time. Accompanied with new foundation of many venture capitals the preceeding six companies have recovered vividly and some of them adopted the partnership system which has been developing in the U. S. A. since Mr. Author Rock had established such in 1969. Already several partnership funds have organized by JAFCO and other venture capitals.* The leadership of JAFCO in this field is very impressive and some leaders of this company say that the first year of the venture capital has just started in Japan. However there are some problems which will be referred to in the last chapter.

Why the enthusiasm of security houses has happened? What is its background? As an answer to these questions we have to point out that the Committee of Securities Dealers has recommended the alleviation of the

* The List of Partnership Funds (July, 1983)

| Managing Partner | Name of Fund | Amount (mil.) | Date of Foundation |
|---|---|---|---|
| JAFCO | JAFCO-1 | 1,600 | Apr., 1982 |
| | JAFCO-2 | 2,800 | July, 1982 |
| | JAFCO-3 | 7,000 | Mar., 1983 |
| | JAFCO-S | 1,000 | Mar., 1983 |
| Yamaichi Uni-Ven | Uni-Ven 1 | 2,200 | Jan., 1983 |
| | Uni-Ven 2 | 1,000 | Apr., 1983 |
| New Japan Finance | NJF 1 | 1,050 | Feb., 1983 |
| Nippon Investment | NIVE 1 | 3,000 | Apr., 1983 |

standard of registration to the Stock Exchange Market. If this proposal is realized, many venture businesses, which were shut out from this market until now, will be able to get the chance of listing their shares. Security houses who have already invested in such hopeful companies will get the opportunities to realize great capital gains. Security houses hope to use this venture boom as a means to overcome the war against banks, and banks naturally intend to make a counterattack which will be covered in the next section.

## 2. Banks' Behavior

As already mentioned the attitude of banks towards new venture capital is rather negative but this does not mean that banks have no concern in venture business. Banks have realized the limitation of cooperation with security houses and are now going to seek their own way to make contact with hopeful "venture business."

"Finantial Revolution" is, I think, one of the results of slow growth economy, in which many big businesses are likely to pay back money to their bank. This tendency emerged first in high profit industries like electronics and car but is now recognized in petroleum and paper-pulp industries. Readers can find recent figures about this matter in Table IV.

TABLE IV. NET INCREASE OF EQUIPMENT INVESTMENT (Breakdown) ¥million

《Petroleum》

| | 1981 | 1982 | 1983 |
|---|---|---|---|
| equity | 42.1 | 10.3 | 0 |
| bond | △ 2.2 | 18.5 | △ 5.9 |
| borrowing | 116.9 | 2.0 | △23.9 |
| self-finance | 250.7 | 304.9 | 301.9 |
| depreciation | 224.1 | 233.4 | 239.5 |
| others | 26.6 | 71.4 | 62.4 |
| Total | 407.1 | 335.7 | 272.1 |

《Paper-Pulp》

| | 1981 | 1982 | 1983 |
|---|---|---|---|
| equity | 5.6 | 16.1 | 0.7 |
| bond | △ 4.7 | 2.1 | △ 0.8 |
| borrowing | △12.1 | △105.8 | △45.1 |
| self-finance | 162.5 | 208.1 | 172.4 |
| depreciation | 127.8 | 131.9 | 131.3 |
| others | 34.8 | 76.2 | 41.1 |
| Total | 151.3 | 120.5 | 127.1 |

Source: Nihon Kin-yu Tsushin, June 13, 1983.

Banks now have to seek other outlets for their leading. Up to now the bank's attitude towards new customers is very strict and conservative but they are being forced to abolish their traditional principle from now on. Already many banks set out new loans for consumers and small businesses. They can find three outlets, personal loan, international finance, and small business loan.

There are many kinds of personal loans in Japan but banks have chiefly engaged in house-loan or concert loan (car-loan, etc.). However these loans have declined recently due to the depression of house building and of car-selling.

In the field of free loan and card loan, banks are in only second position under the predominance of so-called "Sarakin" who provides only consumer-loan at very high rates. To make matters worse some banks distressed with an excess of money are lending huge amount of money to "Sarakin" (it is estimated about ¥1,000 billion). The Ministry of Finance asked banks self-restrain and in May 1983 the so-called Sarakin Act was passed. Although this Act itself has a bad reputation as it recognizes unreasonable high interest rate officially rather than controlling them, since then banks are entering into this business by their own efforts. Many card companies have been founded as direct controlled subsidiaries and some banks have launched some new type personal loan (cf. the Sumitomo Bank set out a new card loan up to 10 million yen at 10.5% rate).

International finance is a very profitable business but is, at the same time, a very risky business. Generally speaking Japanese banks are behind other foreign banks because of the lack of know-how in this field, but recently Fuji Bank has broken onto the horizon by buying Walter E. H. Co., American financial company.

We can recognize some new behavior in banks in small firms finance. The Mitsui Banks issued a new loan for small firms (not especially for venture business), "Neighborhood Loan" in 1982 Jan., and since then five banks have made similar loans which Readers can see below.

The balance of Mitsui loans amounted to about ¥35 billions to about 10 thousand customers at the end of May, 1983.

| Banks | Name of Loans | Size of Loan (¥ million) | Term (years) |
|---|---|---|---|
| Mitsui | Neighborhood Loan | 5 | 3 |
| Tokai | Our Town's Loan | 7 | 3 |
| Daiwa | Non-collateral Loan | 5 | 3 |
| Hokkaido Takushoku | Prosperity Loan | 5 | 5 |
| Dai-ichi Kangyō | Neighborhood Loan | 5 | 5 |
| Saitama | Development Loan | 5 | 5 |

The remarkable feature of these loans is that they do not require any collateral in principle and the necessary procedure is very simple and easy. A banker who promotes this loan said that it is even possible "if you make application in the morning you can get money in the evening."

These loan are not necessarily arranged for venture businesses but we can find some loans and plans specialized for them. In June 1983 the Daiwa

Bank and the Sanwa Bank set out to make new loans for venture businesses which have not enough collateral but show a remarkable growth-power, so to speak, an intangible collateral. In the case of the Daiwa Bank the interest rate will be set rather below the long-term prime rate and the Sanwa Bank intends to do loans without collateral. This movement will spread rapidly to other banks because of excess of lending money.*

The Hokkaido Takushoku Bank announced new plans to assist small businesses to develop new technology in March 1983. This plan has three pillars, the prize for new technology, the loan to develop new technology and equity-investment. According to the report of Nikkei Business, 591 companies of 1,000 which are at very near the stage to listing their shares are the customers of 13 city banks. This matter shows the strong intention of big banks to venture business. It is very important to recognize the next two facts. First, venture businesses whom banks want to contact are not small businesses at the stage of R & D but rather medium sized businesses graduated from the developing stage. Second, the venture businesses boom expressed by banks is not single phenomenon but is only one aspect of their enthusiasm for small business finance.

According to the most recent information, Fuji Bank decided to establish "Fuji Investment" whose main business is equity investment to venture businesses.

### 3. Reform of Stock Exchange Market

It is the most important thing for venture capitals to get capital gain by selling shares in the Stock Market. But both the listing standard of the Stock Exchange Market and the registering standard of Over the Counter Market (OTC) are so severe that the number of listing brands were only 28 in the last year. The OTC Market in Japan is very inactive and the total dealing of this Market was only 33 million in the last year. This figure is much smaller than the per-day average of Tokyo Stock Exchange Market.

On the contrary, there is an active OTC Market in the U. S. A. which is called NASDAQ opened 1971. In the U. K. too we can find the Unlisted Securities Market (U. S. M.) has been successfully operating since 1980.

It is very natural that a spire to Japanese NASDAQ is strongly rising in this venture boom. A clue to this movement was the Commission of Inquiry to NASDAQ in Oct. 1981 and at last the Committee of Security Dealing (an Organ of Ministry of Finance) made the following two recommendations in June 1983.

* Besides city banks, the Japan Bond Credit Bank is promoting a campaign "Developing New Customers" including venture business. And the Hyogo Mutual Bank has opened their original venture business loan.

TABLE V-1. THE CHANGE OF LISTING OR REGISTERING STANDARD OF TSE (enforced from Nov. 1, 1983)

| Listing Standard of TSE Second Section Market | | |
|---|---|---|
| | Old Standard | New Standard (estimated) |
| Capital issued | 500 (¥ million) | 300 (¥ million) |
| Years since Foundation | 5 | 5 |
| Net Assets | 1,500 (¥ million) | 1,000 (¥ million) |
| Profit per Share | First Year ¥15<br>Second Year ¥15<br>Third Year ¥20 | Same as the Old Standard |
| Dividend | ¥5 or 10% during 3 years | ¥5 or 10% during 1 year |
| Audit | 3 years | 3 years |
| Number of Shareholders | 2,000 | 1,000 |
| Percentage of Stable Shareholders | under 70% | 80% |

| Registering Standard of OTC Market | | |
|---|---|---|
| | Old Standard | New Standard (estimated) |
| Capital issued | 100 (¥ million) at the end of Business Year | 100 (¥ million) at the time of registering |
| Years since Foundation | 2 years | no regulation |
| Net Assets | 200 (¥ million) | 200 (¥ million) |
| Profit per Share | ¥10 | ¥10 |
| Dividend | ¥5 or 10% | no regulation |
| Number of Shoreholders | no regulation | over 200 |

TABLE V-2. NEW LISTING STANDARD OF OSAKA NEW SECOND SECTION MARKET

| | |
|---|---|
| Years after the foundation | 3 years |
| Capital issued | Over 100 (¥ million) |
| Percentage of Stable Shareholders | 90% at the time of application<br>30% at the time of listing |
| Net Assets | Over 500 (¥ million) |
| Profit per Share | ¥15, 2 year before listing<br>¥20, 1 year before listing |
| Dividend | No regulation |

(1) Reformation of the listing standard of the Stock Exchange Market
(2) Vitalization of OTC Market

In order to realize the latter purpose the Committee suggested three ways. The first is to make it possible to make the public subscription in OTC that is prohibited under the present condition. The second is to disregulate the rule prohibiting security companies to induce their customers. The third is to create the system similar to NASDAQ in the U. S. A., which will enable securities companies to show a quotation of OTC shares to their customers rapidly.

Meanwhile the board of Osaka Stock Exchange presented the original reforming plan, which proposed the foundation of new market section dealing with only venture business stocks, namely Osaka Third Section. A director of this board said that Osaka is the most appropriate place for the venture stock market because there are many hopeful small businesses in Osaka district. This proposal is one of means to stop the relative decline of the Osaka Market compared with the Tokyo Market, but has a sensational influence because of its good timing.

After some discussions among several sections the final plan was agreed between Government and the Association of Security Houses in September 1983 and enforced in November 1. Readers can see in Table V-1 the main reforming points of the Tokyo Stock Exchange. The idea of third section in Osaka Market was finally settled with the formation of New Second Section Market whose standard Readers can see in Table V-2.

Under these new standard, many venture businesses, which were shut out from the Capital Market until now, can get the chance to raise money directly, and security companies who have already invested to such companies will get opportunities for achieving great capital gain. This is the main reason why security companies are showing very positive attitudes towards this boom. Their catch phrase is "Don't miss the bus."

As to this, I can point out some problems. Because of violent fluctuations manipulated by security companies and their irresponsible attitude for customers, the number of individual shareholders has been declining to only 28%. As a matter of fact the stock exchange system is sustained by the mutual share holding of large companies, therefore someone call it "juridical person market." Under this condition is it really possible to make new market?

JAFCO has recently accepted the shares of Sord Computer Co. (a typical venture business in Japan) at the price of ¥70,000 per 1 share. Who can buy such high price shares when JAFCO sell them on OTC Market? Generally speaking the price is higher the fluctuation is more violent and I wonder many individual investors will become the miserable joker of Money

Game. In order to avoid this matter we should arrange some appropriate means for protecting individual shareholders. After all this is a short cut to the foundation of Japanese NASDAQ.

### 4. Government Policies to Venture Business

(a) VEC and Japanese SBIC

Besides the venture capitals above mentioned, there are two kinds of public institutions which provide the money to venture businesses. One is VEC (the Venture Enterprize Center) established by MITI (the Ministry of International Trade and Industry) in July 1975. VEC is a heepsake of the first venture boom and was barely making their business until last year. As Readers can see in Table VI, both the amount of VEC's investment and the number of customers were very small but they have been getting larger since last year.

TABLE VI. THE RESULTS OF VEC'S ACTIVITIES

| | 1975 | 1976 | 1977 | 1978 | 1979 | 1980 | 1981 | 1982 |
|---|---|---|---|---|---|---|---|---|
| The Number of Customers | 40 | 34 | 13 | 10 | 14 | 10 | 22 | 34 |
| The Amount of Finance (¥ Mil.) | 1,012 | 920 | 419 | 210 | 329 | 264 | 670 | 1,389 |

Source: VEC's Annual Report

VEC's main business is the Loan Guarantee which is available to 80% of total loan (max ¥80 million) without any collateral. Gurantee fee is 2% and if the project will get a great success VEC can ask for a bonus. It is the most remarkable thing that under this guarantee a customer company can get special loan (4%) from his banks. The secret of such low rate is the fund which the Association of Bicycle Race lend to banks, at the rate of 0.9%. Bicycle Race is one of public managed gambles and this Association always gets huge profits, part of which is advanced to several public enterprises. For example, VEC guarantees ¥100 million project and then the Association of Bicycle Race advances ¥80 million to a bank at the rate of 0.9%, a bank lends ¥100 million (this ¥80 million with their own ¥20 million) to a customer at the rate of 4%. VEC's guarantee is attractive to small businesses which has no sufficient collateral, but its inspection to projects is not easy. It is interesting to note that the Chairman of VEC's Inspection Committee is Mr Soichiro Honda who is a famous man as a founder of Honda Mortors Company.

Another is the Small Business Investment Companies. These Companies, someone call them "SBIC of Japan," were established in Tokyo, Osaka, and Nagoya under the small Business Investment Act in 1963 which is the copy of SBIC Act of the U. S. A. in 1958. They buy stocks and convertible bonds of the small business as well as provide managerial and technical consultancy until those businesses can raise funds in the Stock Market.

But the appraisals of these Companies is not good to small businessmen, according to their evidences the inspection for applications is so severe that most of small businessmen are likely to resign their hopes. Readers can see the achievements of Three Companies in Table VII. The number of small businesses who could list their shares in the Stock Market by the assistance of these Companies were only 8 during the last 20 years. Investment fund of these Companies is mainly supplied by the Small Business Finance Corporation and the source of this SBIC cames from the savings at the Post Office. Therefore you can see these companies as official institutions although their appearance is private.

TABLE VII. THE INVESTMENT OF JAPANESE SBIC

| | Tokyo | Osaka | Nagoya | Total |
|---|---|---|---|---|
| Cumulative Number of Customers | 486 | 280 | 511 | 1,277 |
| Cumulative Amount of Investment: ¥ Mil. | 19,648 | 10,803 | 20,192 | 50,644 |
| Number of Customers at Present | 303 | 194 | 344 | 841 |
| Amount of Investment at Present: ¥ Mil. | 13,380 | 7,414 | 13,837 | 34,632 |

Note: In fiscal year from Apr. 1982 to March 1983, Tokyo Company newly invested ¥1,571 million to 32 customers.
Source: Annual Report 1983 of Tokyo SBIC.

As one of incentive policies to the economy Government decided to set out the new loan of SBIC which will provide about ¥1.5 billion to hopeful small businesses. I would rather say that ¥1.5 billion is too small amount for the present condition of small business.

The venture capital companies (private sector), VEC and Japanese SBIC (public sector) are the specialized institutions for venture business finance, and the division of work among them and the partition of customers are going well because private venture capital companies aim at such companies that are in the last stage of the beginning growth, c. f. the nearest stage to listing their shares in the Stock Market. On the contrary, VEC's target is the companies of R & D stage and Japanese "SBIC" is in middle way. From this point we can pick up one of problems. Although the companies at this stage are almost countless (about 800,000), the customers of VEC are only 40 last year. We must appraise VEC's qualitative contribution as a pioneer in this field, but at the same time the amount these special institution provide is too small to bring up small business in Japan. I think MITI's policy for venture business still remains at the stage of lip service because of the fiscal crisis.

Besides these specialized institutions for venture business, there are many institutions for small businesses in Japan. Readers can get an outline of small business finance system in Fig. 1. The Central Cooperative Bank for Commerce and Industry (Choko-chu-kin) is the biggest one. Equity is financed by the Government and member cooperatives half and half, and its total cumulative investment is now over ¥6,000 billion. The Small Business Finance Corporation and the People's Finance Corporation are wholly government-owned banks, former deals with middle businesses and latter with

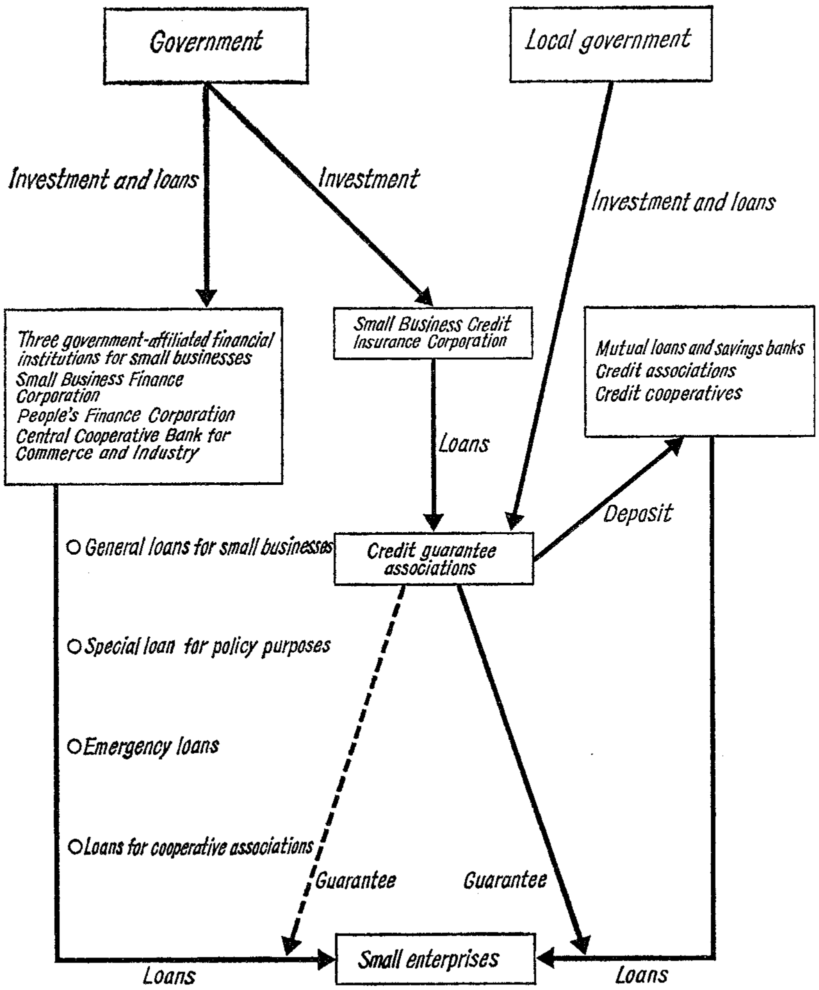


**Fig. 1.** Small Business Financing Policy.

rather smaller businesses. Recently MITI required the Ministry of Finance to open New SBIC loan for venture business in the budget of 1984.

As already mentioned big deposit banks are showing a great concern in small businesses and about 50% of their total lending is financed to them.* This trend has become clearer over the couple of years, partly because the lending to big businesses is declining rapidly. In addition, the local banks and other small "banks" (you can find them in Fig. 1) are lending for small businesses. As mentioned above there are many banks for small businesses in Japan and to some extent they can provide their advances to the venture businesses. This is one of reasons why banks did not show the enthusiasm for the venture capital subsidiary. Not in the form of investments but in the form of advances they have already provided the services to the small businesses.

(b) Venture Business Investment Act

MITI is going to bring an Act in next year Diet (1984). This Act is consist of two components, the first is the foundation of a recognition-system which will authorize hopeful small businesses as venture businesses. This authorization will be based on several conditions; capital is under ¥100 millions, the number of employees is under 300, the independent business having a short history since its foundation, and the cost of technology-development is relatively high.

Authorized small businesses can easily get all types of loans and investment from public institutions.

The second factor is the tax allowance for venture capitals who invest in venture businesses. We can find similar measures in other countries, cf. Small Business Investment Act 1980 in the U. S. A. and the Business Start-

* Small Business Finance of 12 City Banks
(% to the Total Finance)

| | Daiichi Kangyo | Fuji | Sumitomo | Mitsubishi | Sanwa | Tokai |
|---|---|---|---|---|---|---|
| March 1983 | 46.7 | 47.6 | 47.6 | 50.9 | 51.0 | 47.4 |
| March 1978 | 42.5 | 43.3 | 42.9 | 45.1 | 49.1 | 44.6 |
| March 1973 | 30.8 | 27.2 | 32.5 | 29.3 | 34.8 | 28.1 |

| | Taiyo Kobe | Mitsui | Kyowa | Daiwa | Saitama | Hokkaido Takushoku |
|---|---|---|---|---|---|---|
| March 1983 | 49.1 | 48.5 | 51.8 | 43.9 | 50.6 | 53.0 |
| March 1978 | 46.3 | 41.1 | 50.8 | 41.9 | 48.4 | 48.7 |
| March 1973 | 36.3 | 26.8 | 33.9 | 32.0 | 37.5 | 33.2 |

Up Scheme 1982 in U. K. (this was expanded to the Business Expansion Scheme since April 1983). MITI's purpose is to restrain the side business of venture capitals (huge lending to "Sarakin") and to grow the original business of them. In 1980's the expectation of small businesses has been growing, especially their contribution for technical innovation were revalued and this tendency was spurred by the unwillingness of big businesses to do the innovation. Reflecting this matter, MITI set about nursing the small high-technology businesses and began to regard them as a hope-maker in the depressed economy. Although the budget of the Small and Medium Enterprise Agency (one Division in MITI having the responsibility for the small businesses) was discriminated by about 5%, new budget to assist small businesses developing new technologies was passed smoothly. This can be only a point, where MITI can be proud of small entrepreneurs this year. Roughly speaking, the second boom is one of products of a long depressed economy. It is a typical Japanese phenomenon that Government decides the definition of venture business. It is quite natural that foreigners think Japanese economy is wholly managed by Government policy and they sometimes call our economy "Japan Company." Besides the Act above mentioned, we can find two new measures for developing venture businesses. The Japan Development Bank, which is wholly owned by government, has decided to found a new loan for venture businesses. Interest rate on this loan is 4.3%, about half of JDB's standard rate, and its total amount is ¥16 billions and the period of loan is up to 10 years.

It is the first time in JDB's history to make such a loan and we can recognize it to be epock-making. I can point out as a background of this revolutional loan that JDB is in distress for the excess of lending money under this economic depression.

In June 1983 MITI announced the plan for building three venture business areas which will be composed from four or five venture businesses. MITI will help these areas by establishment of some common facilities like big computer system and some kinds of testing equipment. Half the cost of these establishment will be paid by MITI and venture business can use modernization loan of a public institution (interest rate is only 2.7%). But the total cost per one project is only ¥3 billion and therefore many people wonder at its contribution.

According to current information the 1984 budget for small businesses will be cut down about 6% than previous year. MITI was faced with strong opposition of Ministry of Finance and at last has abandoned the Venture Business Investment Act and presented some new policies for venture businesses. The budget of new policies is as follows ;

Subsidy for Reforming Technologies of Small Business

| | | ( ) previous year |
|---|---|---|
| Total | 1,348 mil. | (1068) |
| Special budget for VB | 200 | ( 0) |
| Common Facilities for Venture Businesses like Computer Centre | 151 | ( 0) |
| Foundation of Venture Cooperatives (some institutions for technological exchange between different-type small Businesses) | 83 | ( 0) |
| Venture Business Symposium | 5 | ( 0) |
| Special Venture Business Loan of Small Business Finance Corporation | 15,000 | ( 0) |

## III. Some Problems in "Venture Business Boom"

In Japan we have a proverb "different dreams in the same bed." It means that men who are performing the same task find different purposes respectively and this proverb can be completely applicable to the venture business boom of this time.

First different dreams are ones between banks and security houses and have already come out immediately after the first boom. This gap is now decisive because only the security houses are showing enthusiasm for the foundation of venture capital subsidiaries, on the other hand banks are seeking their own ways for treating hopeful small customers (II-2). So venture business finance is a new battle field between them.

As already mentioned, the banks' dream is to make a long relation with hopeful customers and in principal banks profit will be successfully derived from the growth of the customer company. Bank and customer should always walk side by side. On the contrary, the security houses dream is to get capital gain in the near future and to get the post of underwriter of new shares. Needless to say the chance to get these merits does not always happens. Metaphorically speaking the bank should be a wife always helping her husband and the security house is a househelper which is needed at very busy time. But it is an absolute fact that banks and security houses are indispensable to the growth of small businesses; therefore if they want to develop Japanese small companies with their business, they should fill this gap rapidly.

Unfortunately both banks and security houses are losing sight of their essential part for fostering Japanese small businesses and using the venture capital finance as a weapon in the battle between them. As a result, their target is not small but medium, correctly speaking, hopeful and well managed large medium companies (only several hundred companies). If we consider which factors sustained Japanese economic growth, we realize soon the important role of real small businesses sometimes called subcontact companies.

Second different dreams are ones between MITI and the Ministry of Finance. The main promoter of this venture boom is MITI and its aim is to create original technologies which will break a path to the growth-economy. Spy-Scandal between the IBM and Hitachi which happened last year gave a great schock to MITI and it is one of the motivations to lead MITI in this direction. The attitude of the Ministry of Finance is rather negative to tax allowance of the Venture Investment Act, needless to say, because of the crisis of finance, as you know the balance of national debt is over ¥100,000 billions this June and this figure is about half of GNP. As regarding the reformation of the Stock Exchange Market the policy of the Ministry of Finance is somewhat conservative. They have not abandoned yet the principle of "protecting individual shareholders" and are rather suspicious for the creation of Japanese NASDAQ, therefore, MITI will be forced to make some compromises with the Ministry of Finance.

I hope that the different dreams will not develop to mere dispute over the area of jurisdiction between both Ministries. In relation to MITI's policies there is a criticism that too much emphasis is placed upon hopeful medium companies therefore the majority of Japanese small businesses are left outside the protection. Although the unemployment problem is serious and the number of bankruptcy of small firms got the historical high point in October 1983, LDP Government seems to have very little concern and to ignore these matter consciously. The Venture Business Seminor was held by MITI in Sapporo in November 23, 1983, however, the number of participants was only 120 including 20 bankers and 10 local government officials. At the same time and the same place "the Bankruptcy Seminor, How to Prevent the Connected Bankruptcy" was also held by the Sapporo Chambers of Commerce and over 300 entrepreneurs attended it. This shows what the first thing to do is.

We can recognize a bit of difference between VEC (II-4) and private venture capitals. Because the purpose of VEC in promoting the venture businesses is to generate the revitalization of Japanese economy and it expects the small businesses to develop many new technologies, the target of its assistant policy necessarily goes toward the companies at the stage of R & D. As far as one company is hopeful, even if it is very dangerous and has a great risk, it can become a VEC's customer. As a result the rate of failure of VEC's finance is very high, about "20%." In contrast with VEC's generosity, the security houses are very discreet and the customers whom the security houses try to treat are ones who have already graduated from the

R & D stage. They are apt to seek, so to speak, Sony or Honda of tomorrow. But it is so difficult for them to find such companies that the number of the customers invested by JAFCO (the largest venture capital in Japan) is only 70 at the end of June 1983. The essential matter to overcome the long continued depression is to bring up many candidates who may possibly become to Sony or Honda after ten or fifteen years. This different dream may come out in this boom more clearly.

Finally I have to mention some problems in this venture boom.

Needless to say, financial institutions should keep a kind of soundness in their business. But as already mentioned there is the intimate relation between venture capitals and "Sarakin" companies.* In fact, it is the normal case that "Sarakin" are big customers of venture capitals' sidebusiness, in turn "Sarakin" are main investor of venture capitals and also are members of the partnership fund. "Sarakin" are sometimes blamed for their excessive interest rate or heartless collection, and cause some social problems. If venture capital companies hope to stabilize their position in the financial structure, they need to break off these put-up jobs with "Sarakin" companies. We can find some foreign investors in the list of some partnership venture funds and they are for the most part famous merchant bankers, cf. Baring Brothers, Robert Fleming, Bank Paribas. This matter in itself may be a splendid result of the effort of venture capital leaders but it is a strange scene for me that the most famous merchant bankers sit with the most notorious "Sarakin" companies. At the beginning leaders of venture capitals expected that many domestic investors subscribe for partnership funds but as a matter of fact "Sarakin" and "Foreigner" commanded majority. If venture capitals hope to further the development of the partnership fund they should consider what a desirable component is.

The spirit of the merchant banker is always international but the spirit of MITI promoting domestic small businesses is very national. I am afraid that in relation to the problem of industrial policy this will generate new friction between Japan and other countries. Most of people seem to believe the future prosperity of so-called venture businesses. Really some of them have been showing great profit, but also we can find some examples of breakdown. In some fields big businesses also are going to catch up small venture businesses, for example, in the U. S. A. IBM has just catched up Apple Computer in the field of personal computer, in Japan the Systems Formulate Co. which was one of pioneers in the field of personal computer went bankruptcy in April 1983. The future of the venture businesses will never be tranquil. In the U. S. A. and U. K., the reasons for their bankruptcies were not money problems but the insufficiency of management techniques, so this

* See *Financial Times* dated April 21, 1983.

matter teaches us that the consultation is very important for small businesses. But in this field there are very little experiences in our country. Both in the banks and especially in the security houses we can not find any ample services and knowledges of how to manage small venture businesses. Compared with this Japanese conditions, ICFC (a pioneer of small firms finance) and big four banks in U. K. marched out to the small businesses finance from the system of consultation.

Since the history of Japanese venture capitals has just begun, so we can not make a conclusion of this phenomenon. If we can settle some problems mentioned in this chapter, we can see a real venture boom which will make a great contribution to our economy. (December 1983)