5 Economic Analysis of the ‘Loan-Concentration’ Mechanism

5.1 INTRODUCTION

This chapter examines the ‘loan-concentration’ mechanism, often referred to as financial dual structure, dual structure in the flow of funds and financial burden shifting. The loan-concentration view asserts that a de facto mechanism in the Japanese financial sector directed loans to large firms rather than small businesses, thereby harming the financial interests of small business. Loan concentration is closely related to keiretsu loans, main banks and corporate groups, and has been accepted as a serious phenomenon since the second half of the 1950s. Together with the dual-structure view, the loan-concentration view has been the basis of small business policy, especially in the 1960s.

The basic questions I ask about the loan-concentration view are: (1) What is the reality behind the term? (2) Has the view been logically consistent and coherent over time? (3) Has the existence of the loan-concentration mechanism been proved persuasively? (4) Who created and maintained this mechanism and why? (5) Does the loan-concentration view take into consideration market forces, which often constrain the choice sets of economic agents? Examination of representative academic literature, such as Shinohara (1961) and Kawaguchi (1965, 1966), leads me to answer these questions in the negative for the decade beginning in the mid-1950s. I also present reasons why the loan-concentration view is unpersuasive. The loan-concentration mechanism is a component and for some the basis of the dual-structure view; thus the argument in this chapter is directly related to that of Part I.

Section 5.2 defines the problem: representative treatments and their place in the literature are explained and Section 5.3 lays out my seven reasons for their rejection. Section 5.4 examines the reality of the ‘loan-concentration’ mechanism, that is, the long-run structure and the short-run dynamic process over the course of trade cycles of loan concentration. Section 5.5 discusses the reality of the ‘adhesion relationship’ (yuchaku kankei) between large banks and large firms or keiretsu loans, which form the basis of the loan-concentration view. Section 5.6 examines the empirical evidence supporting the conventional argument. Section 5.7 offers concluding remarks.
5.2 DEFINITION OF THE PROBLEM

In a joint volume, Yamashita (1985, p. 231) declares at the outset of the section entitled 'The Nature of Small Business Financial Problems': 'we recognize small business financial problems as serious since they are rooted in the dual structure, one of the basic features of Japan's economy'. Teranishi (1974, p. 51) also begins his 'Loan-Concentration, Credit Rationing, and Credit Limit' by arguing: 'we can sum up the main features of the financial side of the postwar Japanese economy with “the loan concentration to large firms through the predominance of indirect financing”'.

Our first concern is how deeply the loan-concentration mechanism has taken root in the dual structure and whether loans have been made to large firms rather than small businesses. I thought this mechanism never existed. No literature totally denies the existence of this mechanism and its relation to the dual structure, but little of the literature proves its existence clearly with careful investigation and hard evidence. Like the dual-structure view, a wide variety of views exists in regard to the loan-concentration mechanism, and sharp controversy over the various aspects of interpretation rapidly developed. Nobody denies Kawaguchi's position as the most influential promoter of the loan-concentration view. I take Kawaguchi (1965) as representative of the field.

Because of the dominance in Japan of dogmatic Germanic theory, mentioned in Section 1.1, the literature and debates over the Japanese economy have been dominated by focus on financial factors, such as financial phenomena like loans and shareholdings, financial institutions like banks, and financial markets like loan markets and stock markets. This literature focused on the loan-concentration mechanism. In addition to the five basic questions listed in the previous section, critical examination of the literature leads us also to an anatomy of the underlying traditional, dominant theory, recognizing economic phenomena not as a result of exchange by agreement but by coercion. The next two chapters investigate the relationships between financial markets and large firms, the alleged beneficiaries of burden shifting, thereby focusing on the other side of the loan-concentration mechanism. The main-bank view argues that Japanese large firms have special long-term relationships with one or more large banks, and that these pervade the Japanese financial market and therefore influence Japan's industrial organization. Each large bank has such a relationship with a group of large firms, called 'corporate groups' and the corporate-group view asserts that these groups are important for understanding the Japanese economy. If the loan-concentration mechanism never existed, as shown below, these two views lose their foundation. Hence this chapter is a basis for the next two chapters.

As with the dual-structure view, support among both academics and the public for the loan-concentration view had weakened rapidly by 1970. However, just like the keywords for the Japanese economy in the 1950s and 1960s, the loan-concentration view and related keywords are often used to describe Japan's economy today. Some, like Yamashita (1985, p. 232), insist that there has been no change: 'As the financial dual structure takes root in the real economy, it cannot be solved in a short time. It applies in today's