

construction and the other services rose.⁶⁴ Small and medium-sized enterprises displaced large firms (normally fellow *keiretsu* members with the banks) as the primary customers for bank loans.

One of the factors contributing to the decline of large manufacturing enterprises' share of bank lending was the increased supply of government bonds in the 1970s, and the pressure that caused within Japan to liberalize interest rates on deposits. Depositors had the option of holding higher yielding government securities, so banks had to compete for funds. The banks experienced a decline in net interest margins and shifted lending away from larger customers towards smaller ones, where margins are usually higher.

Since the long-term banking relationships that existed in *keiretsu* were partially due to a lack of efficient alternatives for firms seeking capital, the maturing of domestic capital markets and the fact that many larger Japanese companies have become more global in their operations, have caused firms to rely more on domestic securities markets and international capital markets for funds.⁶⁵ Large manufacturing firms relied on banks for 38.4% of their financing in 1975; by 1989, that was down to 25.2%.⁶⁶

⁶⁴ In 1980, 32.6% of bank lending went to manufacturing and 32.5% went to small business. By 1992, 13.2% went to manufacturing and 50.4% went to small business. See International Monetary Fund, *op. cit.*, p. 10. Lending to the non-traditional sectors has grown along with their overall importance to the economy. The share that the six largest *keiretsu* command of Japan's total assets and net income has fallen in recent years, partly because *keiretsu* firms have less impact on new service-oriented industries. See E. Razin, *op. cit.*, p. 369.

⁶⁵ An indication of the move away from bank debt is the fall in average Japanese debt/equity ratios in the late 1980s. See W.C. Kester and T.A. Luehman, *op. cit.*, p. 132. They quote one study that estimates debt/equity ratios fell by 50% between 1985 and 1989. A similar process has also been underway in the U.S., where commercial banks' share of the assets of all financial institutions has been steadily declining for the last 40 years. See G.G. Kaufman and L.R. Mote, "Is Banking a Declining Industry? A Historical Perspective", in *Economic Perspectives*, Federal Reserve Bank of Chicago, Chicago, IL, May/June 1994, pp. 2-19; and "International Banking Survey", in *The Economist*, London, April 30, 1994, p. 11.

⁶⁶ See R.W. Wright, *op. cit.*, p. 11.