

system.²⁹ Reform should lead to increased differentiation among banks in terms of size and asset quality. One influential credit rating agency, the ICBA, has concluded that, because of changes in assumptions concerning the future level of systemic support to be given to the weaker banks by the Ministry of Finance, the credit ratings of major banks will be more differentiated in the future, with those of weaker banks more closely reflecting the impact on their financial condition of problematic loan losses.³⁰ Even the Japanese government has recognized the need to modify its convoy style regulation system into one that puts greater emphasis on market mechanisms.³¹

With the demise of the convoy system, the banks' traditional post-war role as "channellers" of individuals' saving into industrial investment might also diminish. The days of the bank being the centre of a cohesive industrial grouping and providing for most of the group's financing needs could be coming to an end. Given the advent of globalization and liberalization in financial markets and with the maturation of the Japanese economy, companies are relying less on their main banks and more on international financial markets.³² Increasing transparency in the activities of the secretive Japanese banks and furthering market liberalization cannot but help level the playing field for foreign banks. The implications of this are positive for foreign banks which might be able to break through the invisible *keiretsu* barriers that have traditionally kept them out of the game in Japan.

Although highly unlikely, one interesting option open to the Japanese government in dealing with weak financial institutions would be to accept mergers with *foreign* banks. This could save public money because foreign banks might be willing to pay a premium to buy a failing institution in order to obtain the right to enter the market.³³ In addition, North American and European banks, which are more

²⁹In the "convoy" system, the major banks reported remarkably similar results year after year. This system might be breaking down. For example, currently the strongest seven banks show an average of 3.9 per cent of problem loans to total loans, while the weakest seven show an average of 11.4 per cent. (*Financial Times*, December 7, 1995, p. 17.)

³⁰D. Iwaasa, Canadian Embassy, Tokyo, "ICBA Note on Japanese Bank Failures", unclassified report, September 15, 1995.

³¹D. Iwaasa, Canadian Embassy, Tokyo, "Japan: Improved Banking Inspection and Supervision", unclassified report, January 20, 1996.

³²*Financial Times*, December 7, 1995, p. 17.

³³D. Ostrom, *op. cit.*, p. 14.