

For commercial banks, their direct equity holdings in particular firms are typically quite small. There is no evidence to suggest that banks are breaking the 5% rule. The relationships banks have with other *keiretsu* firms are based on high debt/equity ratios, interlocking directorates and close inter-corporate operational links.

In *keiretsu*, it is unusual for more than 10% of any firm's outstanding shares to be owned by another single firm.⁵² Normally, member firms purchase between 2% and 5% of each other's shares.⁵³ In total, cross shareholding (also known as mutual shareholding, or inter-corporate shareholding) accounts for 15% to 30% of member companies' stock.⁵⁴ In addition to cross shareholding, companies enter into "stable shareholding" agreements with other large institutions. The result is that 60% to 80% of *keiretsu* company shares are never traded.⁵⁵

In the theory of the firm, whenever there is a separation between ownership and management, there is a potential "principal-agent problem" in which the interests of the principals (shareholders) and agents (managers) differ. Owners are interested in profitability, whereas managers can get sidetracked, focusing instead on such concerns as maximizing market share or enlarging the firm. It has been argued that the close relationships between Japanese banks and non-financial firms, which are characterized by cross shareholdings that are rarely traded and high levels of corporate debt, can reduce the incidence of the principal-agent problem.⁵⁶ Banks, acting as principals, closely monitor the activities of related firms and, by extending loans to

⁵² See E. Razin, *op. cit.*, p. 370.

⁵³ See M. Anchordoguy, *op. cit.*, p. 58.

⁵⁴ See M. Anchordoguy, *op. cit.*, p. 59; R.L. Carson, *op. cit.*, p. 453; and R.L. Lawrence, "Efficient or Exclusionist? The Import Behaviour of Japanese Corporate Groups", in *Brookings Papers on Economic Activity 1*, W.C. Brainard & G.L. Perry, eds. Brookings Institution, Washington, D.C., 1991, p. 312.

⁵⁵ See M. Anchordoguy, *op. cit.*, p. 59. A Canadian study indicates that only 5% of the stocks traded on the Toronto Stock Exchange could be characterized as widely traded, 35% are moderately traded and 60% are infrequently or thinly traded. See R.J. Daniels and J.G. MacIntosh, "Toward a Distinctive Canadian Corporate Law Regime", in *Osgoode Hall Law Journal*, Vol. 29, No. 4, Osgoode Hall Law School of York University, Downsview, Ontario, Winter 1991, p. 877.

⁵⁶ By holding both debt and equity, Japanese banks are well placed to monitor affiliated firms and ensure that their own interests, as owners, are served. See S. Prowse, *op. cit.*, pp. 1128-9.