An uneasy start in a crowded market
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on a newly privatised entity still trying to find its way Japan's crowded banking sector, already struggling to boost profits in a difficult market, is having to make room for a massive new member.

Last autumn, amid considerable anxiety and antagonism, Japan Post Bank, Japan's largest bank by assets, with Y212,149bn, was unleashed on to the market as part of the privatisation of Japan's post office.

A lumbering giant, JP Bank, which has more than Y181,000bn in deposits and 24,000 post offices at its disposal all over the country, is a worrying presence for its smaller rivals who fear its public image as a government-linked entity, along with its massive network, give it an unfair advantage.

JP Bank's debut as a private bank was given a cold reception by rivals that regard with suspicion its plans to become a leading operator in the retail market, targeting mortgage lending and credit card businesses, and its ambitions to expand fee-generating businesses, particularly investment trust sales.

When the bank, which has had limited experience in lending, solicited partners for its new mortgage business, Suruga Bank was the only one that raised its hand to offer mortgages through JP Bank's network.

Another reason the privatisation of JP Bank is regarded with concern is the challenges it poses for the bank itself. For one thing, its strategy to use cheap funding through deposits to provide loans and generating fees by selling investment products will not be an easy task for the former public entity.

"How are they going to raise profits?" Tsutomu Okubo, an Upper House member of the opposition Democratic Party of Japan, asks. The PO Bank "doesn't have a viable business model," he says.

Until recently, it parked most of its funds in Japanese government bonds. Of its Y212,149bn in assets, Y172,532bn was in securities and just Y3,771bn in loans at the end of March, 2008. And of its securities, more than 90 per cent is comprised of Japanese government bonds, making it one of the largest buyers of government debt.

The problem is, with interest rates at historically low levels, JGBs do not provide much in the way of returns. Futhermore, as interest rates rise in an increasingly inflationary environment, the bank's depositors, who have endured low interest rates for more than a decade, are likely to shift their savings into higher-yielding products.

The worry for JP Bank is that, while its funding is short term -the bulk of its depositors are able to opt out after six months - its investments in JGBs are long term. Those who are pessimistic about JP Bank's outlook say that, in a worst-case situation, the bank could find itself forced to sell JGBs at a loss as it faces a deluge of depositors pulling money out of their accounts.

What is more, any large-scale selling by JP Bank would wreak havoc on the JGB market, leading to even further losses. "If interest rates rise, JP Bank could default," says Mr Okubo, whose party is calling for a review of the post office's privatisation. "We do not envisage a situation in which we will have to sell a large amount of JGBs," JP Bank says.

Even if this worst-case outcome does not arise and JP Bank is able to make a relatively smooth transition from "a JGB fund", as it has been dubbed, to a more normal bank, there is widespread concern that it is unlikely to become profitable enough to be listed as scheduled. JP Bank must be listed by fiscal 2010 and be completely privatised by 2017.

Yoshifumi Nishikawa, president of JP Bank's holding company, Japan Post, appears determined to turn the bank into an important force in the financial industry, capable of generating respectable, if not superior, returns from banking operations.

One big driver of this growth is expected to be the sale of investment trusts. However, sales are unlikely to be sufficient to support a bank the size of JP Bank, whose deposits are larger than the combined deposits of its closest competitors, Mitsubishi UFJ Bank and Sumitomo Mitsui Bank.

JP Bank has taken a step into the mortgage market and credit cards, but these are businesses that much more experienced rivals in the private sector have also targetted as future pillars of growth.

In its desperation to win loan business, the concern is that JP Bank will resort to offering lower interest rates than its competitors, thereby triggering a debilitating interest-rate war.

What is more, since JP Bank has virtually no experience in lending, it risks taking on bad debts, particularly as the economy enters a weak phase.

JP Bank's plans to invest in overseas assets as another way to improve returns also have their limits, given the bank's lack of expertise. To overcome the problems JP Bank faces, Mr Okubo has an ambitious proposal. JP Bank should swap its JGBs for the US dollar assets that comprise Japan's nearly $1,000bn in foreign exchange reserves, he says. This would allow JP Bank to earn better returns, granted with the help of market professionals, while offloading some of the government's debts. Even the determined Mr Nishikawa might feel daunted by the task.

Fonte: Financial Times, London, September 12 2008, Caderno Especial Japan Banking, Finance & Investmnet, p. 5.