

Exploring Co-operative strategies between India and Japan: A view on Banking Industry

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Abstract

The importance of co-operative strategies can never be over emphasized particularly in the context of developing economies where open markets economy has provided them opportunities to serve at the international scale. Indian Banking industry has taken huge strides in shaping up the development of country and has grown immensely over the last decade; still it is yet to make a mark on the global financial map. While most of our international association regarding banks is limited to America and Europe, efforts are being made to develop stronger bonds with Japan which may serve as a gateway to one of the important economic hubs of the world. An attempt has been made in this paper to review trends and opportunities of India-Japan collaboration for banking firms

1. Introduction

Japan and India are two super economies in Asia. According to the latest World Development Indicators, Japan's Gross National Income (GNI) (estimated based on purchasing power parity) for the year 2007 was \$4.4 trillion while its GNI (PPP) per capita stood at \$34,750. Japanese GDP grew at 2.1 per cent in 2006-07 after registering an average growth rate of 1.7 per cent

from India to face the emerging challenges. A study of history of India Japan banking linkage has been made. Reality of trade interactions between the two countries, banking in particular has been reviewed. The key findings have been discussed and reasons for those findings have been tried to be examined. Areas of possible collaboration have been explored for the leadership role of the two countries to enhance the business propositions for both the countries.

Keywords: Co-operative strategies, collaboration, Banking, Japan, Developing economies

Conference Topic/ Sub-Theme:
International Competitiveness

during the period 2000-07. Comparative figures for India stood at \$3.08 trillion, \$2,740, 9.1 per cent and 7.8 percent respectively. Japan's rapid growth in competitiveness during the 1950s has built up a strong base on which leading Japanese firms achieved international attention in the 1980s. Back in the late 1940s, Toyota and other Japanese auto majors realized the potential of innovation: to match the productivity of American auto makers on

smaller volume, with less capital, and with fever (but more permanent) workers (Doz and Hamel, 1998). The results are sustained for decades with stream of cooperative innovations under names such as TQC, JIT, TPS, lean. Human capital, technology, innovation and knowledge, with several overlapping elements, are recognized as key ingredients of competitiveness (Sushil and Momaya, 2001; Takeuchi and Nonaka,

2004; Herstatt et al., 2006). India, started the industrial revolution at the same time, but it was slow at leveraging technology and innovation for competitiveness (Momaya, 2001). Despite some remarkable achievements across industries, it still struggles on many basic issues such as education, economic growth with equity, environment (just 3 Es for example).

2. Interactions between India and Japan

India and Japan celebrated the year 2007 as the Year of Friendship. Japan gives 30 per cent of its overseas development assistance (ODA) to India and remains committed even in the period of the global economic downturn.

Nevertheless, the economic part of the relationship remains far below potential. Two way trade between India and Japan (\$10,177 million in 2007-08) has risen in the last five years, but the figure still remains way below China-Japan trade (\$2,37,193 million) or even trade between India and China (\$37,931 million in 2007-08). Similarly, Japan's foreign direct investment in India for April 2007-March

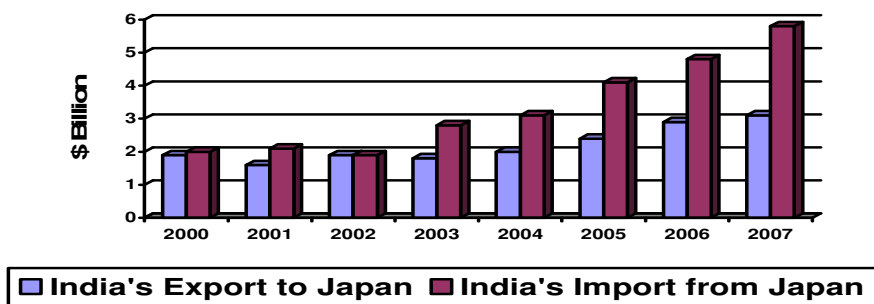
2008 (\$815 million) is still low when compared to Japanese investments in smaller Asian countries such as Vietnam (\$411 million), not to mention China (\$1899 million). (Geethanjali, 2010)

2.1 India-Japan Trade in Goods

Bilateral Trade

In 2007-08, Japan ranked third amongst India's trading partners. The bilateral trade between the two countries has been rising since 2003. The Confederation of Indian Industry (CII) estimates that the trade volume could touch \$15 billion by 2010 if issues like trade facilitation and non-tariff barriers were addressed.

Figure 1: India's Trade with Japan: 2000-2007 (\$ billion)



(Source: CMIE, India Trades)

2.2 Overview of Japan's FDI

\$450 billion at the end of 2006 and \$387 billion at the end of 2005.

At the end of 2007, Japan's overseas investments stood at \$543 billion, up from

Table 1: Global Trends in FDI Inflows: 1999-2007 (\$billion)

Region/ Economy	1999	2000	2001	2002	2003	2004	2005	2006	2007
World	1086.8	1388.0	817.6	678.8	557.9	742.1	958.7	1411.0	1833.3
Developed Economies	828.4	1108.0	571.5	489.9	358.5	418.9	611.3	940.9	1247.6
Developing Economies	231.9	252.5	219.7	157.6	175.1	283.0	316.4	413.0	499.8
Asia	112.6	146.1	111.9	94.4	110.1	170.0	210.0	272.9	319.3
China	40.3	40.7	46.9	52.7	53.5	60.6	72.4	72.7	83.5
India	2.2	2.3	3.4	3.5	4.6	5.8	7.6	19.7	23.0
Japan	12.7	8.3	6.2	9.2	6.3	7.8	2.8	6.5	22.5

Source: DIPP, Japan Cell (www.dipp.nic.in)

Investment inflows into Japan rose from \$2.8 billion in 2005 to \$6.5 billion in 2006 and further to \$22.5 billion in 2007. However, the story is very different in 2008

and 2009 because of the global economic crisis and its descent into a major recession. Table 1 above shows global trends in FDI inflows including inflows into Japan.

2.3 Japanese Investment in India

According to a survey conducted by the Japan Bank for International Co-operation (JBIC) in 2008, India has become the most favored investment destination for long term Japanese investments. In the portion of the survey dealing with promising countries, China maintained the top position, but the number of companies viewing China as promising is declining. On the other hand, more companies are viewing India, Russia, Brazil, and other emerging countries as promising. The number of companies that view India as promising has increased to a level on par with China.

Table 2: FDI Inflow in India from Japan - \$bn

Year	FDI from Japan	Total FDI Inflows into India	Japan's share in total FDI
2002-03	0.41	3.13	13.15
2003-04	0.08	2.63	2.96
2004-05	0.13	3.75	3.36
2005-06	0.21	5.55	3.75
2006-07	0.09	15.73	0.54
2007-08	0.82	24.58	3.32
2008-09	0.23	21.15	1.07

(Source: DIPP, FDI factsheet, various issues)

The “growth potential of the local market” was listed as the top reason for India being a promising destination.

An analysis of sector-wise inflows from Japan shows that the automobile sector received the maximum FDI during 2000-07, accounting for nearly 41 per cent of the total

FDI inflows. Other sectors included electrical equipment, trading, services sector and telecommunications. These five sectors together account for nearly 72 per cent of the total FDI inflows from Japan. (See Table 3 below for details.)

Table 3: Share of top sectors attracting FDI inflows from Japan
(From January 2000 to November 2007)

Ranks	Sector	Amount of FDI Inflows		% of FDI inflows from Japan
		In Rs mn	In \$ mn	
1	Automobile Industry	36203.8	792.7	40.58
2	Electrical Equipment	16378.0	385.0	18.36
3	Trading	6086.9	145.7	6.82
4	Services Sector	2672.8	59.1	3.00
5	Telecommunications	2440.8	54.8	2.74
Total of the above		63782.3	1437.3	

Note: (I) Amount includes the inflows received through FIPB/SIA route, acquisition of existing shares and RBI's automatic route only.

(II) RBI does not provide country and sector specific data on FDI inflows for the period before Jan 1, 2001

Source: DIPP, Japan Cell (www.dipp.nic.in)

3. Banking & Financial Services

Indian banking sector has seen many positive developments in the last decade. The policy makers, which comprise the Reserve Bank of India (RBI), Ministry of Finance and related government and financial sector regulatory entities, have done a commendable job to improve regulation in the sector. The sector now compares favorably with banking sectors in the region on metrics like growth, profitability and non-performing assets (NPAs). A few banks have established an outstanding track record of innovation, growth and value creation. This is reflected in their market valuation. However, improved regulations, innovation, growth

and value creation in the sector remain limited to a small part of it. The cost of banking intermediation in India is higher and bank penetration is far lower than in other markets. India's banking industry must strengthen itself significantly if it has to support the modern and vibrant economy which India aspires to be. While the onus for this change lies mainly with bank managements, an enabling policy and regulatory framework will also be critical to their success. The failure to respond to changing market realities has stunted the development of the financial sector in many developing countries. A weak banking structure has been unable to fuel continued

growth, which has harmed the long-term health of their economies.

The Practical Problem: The above scenario hints that despite much strength, the leading firms in banking industry in India and Japan are not leveraging them effectively. While increasing complexity of customer support, products and markets demands cooperative strategies, firms seem to be lagging behind in forging impactful cooperation. Even when cooperating, their key partners are often in the USA and Europe. Such over dependence is risky, specifically considering the meltdown in financial markets. Let us explore the need and reality of India-Japan cooperation, a high potential area.

4. Why India-Japan Cooperation in Banking & Financial Services Sector?

Considering the vast and growing share for Asia in world economy and the role two largest democracies of Asia, that account for more than 50 % GDP of Asia, can play for peace and prosperity in Asia (e.g. Momaya, 2007), it is assumed that India-Japan cooperation should be quite high or be expanding rapidly. The two prime ministers signed a Joint Statement during the Indian prime minister's visit to Japan in December 2006 to establish an India-Japan strategic and global partnership.

The liberalization reforms are promising many benefits and both countries have decades of experiences and many strengths. Cooperation between India and USA (aka double diamond, Cho and Moon, 2005) has created win-win opportunities for both countries. Similar opportunities can be

created through a double diamond between India and Japan as we explore ubiquitous era. Cooperation between India and Japan in automobile has created several milestones such as sustained market leadership for Maruti-Suzuki and Hero-Honda. Such experiences should inspire India Japan relationships for even bigger goals. (Momaya 2009)

4.1 Japan and India – mutually complementary economies

The Japanese economy is very strong and the services sector accounts for 68 per cent of the GDP in 2007. The industrial sector however now contributes only 30 percent to the GDP which was once the mainstay of Japan's growth while the agricultural sector accounts for one per cent. Similarly, In India, the services sector is the largest contributor to India's GDP, accounting for 52 per cent while agriculture and industry contribute 18 per cent and 30 per cent respectively. The two countries, therefore, share a similar structure, especially with regard to their reliance on the services sector.

In recent years, India and Japan have improved bilateral ties through new initiatives and partnered in programmes ranging from defense and security to economic and cultural linkages. (Geethanjali 2010). In addition, India's 200 million strong middle-class is emerging with strong purchasing power. In addition, there is a difference in the population dynamics of the two countries, with Japan having an ageing society and the India relatively young, which is another dimension that makes the Japanese and Indian economies

complementary. It is thus possible for both countries to enhance their mutually beneficial cooperative relations.

5. Methodology and Data

Considering exploratory nature of the paper, emphasis is more on evolving context than empirical evidence. The research will draw on facts as well as exploratory case study method. Select elements of design and methods of case study research (Yin, 2003) are adapted. Different parts needed different methods. Review of the opportunities in banking sector is largely explored based on secondary data. It also guided the literature review to evolve key constructs. Only quick assessment is done and empirical research for more relevant ones will be explored in future, as cost of research in Japan is very high.

Very limited research and data in India about such international interactions in trade, investment and technology means scope for practical and theoretical contribution at even exploratory stage of this

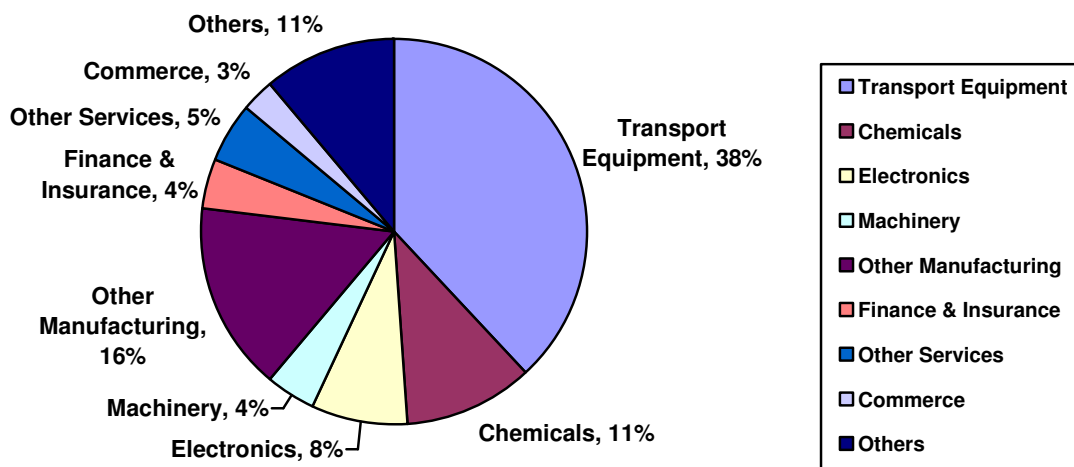
paper. While research and data can be very rich in Japan, they are mostly in the Japanese language. While not very perfect picture can evolve with proxies, it can still provide some clues. Since, the research on India-Japan interactions is so limited, these findings can add some value. Efforts to collect data in such context, evolve a strategic scenario of overall picture and provide alternate perspectives are important contributions of this paper. (Momaya 2009)

6. Review of India Japan interactions in Banking Industry

There have been very limited interactions between India and Japan as far as banking industry is concerned.

The below pie chart says the penetration in BFSI is still a smaller pie. The balance sheet size of Japanese banks in India is still very small as compared to other foreign banks in India. The table 4 below depicts a brief overview presence of operations of major foreign banks in India.

Figure 2: Sector wise break up Japanese Investment in India Total amount from 1991-2004



(Source: Economic Research office, Bank of Tokyo Mitsubishi UFJ)

Table 4: Overview of operations of foreign banks in India

(Amount in Rs. Crore)

Items	2004-05	2005-06	2006-07	2007-08	2008-09	All banks Avg 08-09
Bank of America						
No.of offices	5	5	5	5	5	825
No. of Employees	275	282	283	314	294	12039
Business per employee (Rs. Lakh)	1707.72	1924.81	1920.89	2483.54	2430.57	750.55
Profit per employee (Rs. Lakh)	29.47	51.82	69.09	102.08	110.85	5.60
Bank of Tokyo Mitsubishi UFJ						
No.of offices	3	3	3	3	3	825
No. of Employees	156	159	132	137	150	12039
Business per employee (Rs. Lakh)	663.58	1113.29	1780.52	2613.45	3107.91	750.55
Profit per employee (Rs. Lakh)	6.45	0.20	35.42	60.50	41.57	5.60
Barclays Bank						
No.of offices	1	1	3	5	5	825
No. of Employees	39	45	265	2078	1782	12039
Business per employee (Rs. Lakh)	188.49	148.51	280.54	942.33	1110.13	750.55
Profit per employee (Rs. Lakh)	160.21	271.00	36.28	0.50	1.96	5.60
Citibank						
No.of offices	35	39	40	40	41	825
No. of Employees	2754	3250	5194	4782	4795	12039
Business per employee (Rs. Lakh)	1359.51	1607.92	1360.48	1763.78	1880.10	750.55
Profit per employee (Rs. Lakh)	21.75	21.71	17.33	37.73	45.12	5.60
Deutsche Bank						
No.of offices	5	8	8	10	13	825
No. of Employees	380	678	2250	3500	2005	12039
Business per employee (Rs. Lakh)	1608.93	1016.83	1143.53	1616.74	1434.10	750.55
Profit per employee (Rs. Lakh)	20.31	18.57	20.98	27.54	26.90	5.60
Hongkong & Shanghai Banking Corporation						
No.of offices	39	43	47	47	47	825
No. of Employees	3784	4985	6564	7753	7446	12039
Business per employee (Rs. Lakh)	852.54	975.65	979.68	1012.34	961.81	750.55
Profit per employee (Rs. Lakh)	9.74	12.07	14.32	16.69	16.06	5.60
Mizuho Corporate Bank						
No.of offices	1	1	2	2	2	825
No. of Employees	52	75	83	95	113	12039
Business per employee (Rs. Lakh)	608.21	684.21	918.86	1589.56	2023.79	750.55
Profit per employee (Rs. Lakh)	18.67	8.88	14.60	25.03	38.14	5.60
Standard Chartered Bank						
No.of offices	85	87	82	90	90	825
No. of Employees	5232	6497	6658	8967	7825	12039
Business per employee (Rs. Lakh)	786.36	837.29	924.20	817.35	971.77	750.55
Profit per employee (Rs. Lakh)	11.50	14.50	19.62	20.22	23.82	5.60

(Source: Reserve Bank of India, A Profile of Banks 2008-09)

As can be concluded from the above table, the operations of Bank of Tokyo Mitsubishi UFJ and Mizuho Corporate bank are much smaller than Citibank, Standard Chartered Bank, HSBC and other banks.

On the other hand, the Indian banks couldn't take off despite being present in Japan for so many years. Bank of India was the first Indian bank that opened its branch in Japan, after World War II. On 17th May, 1950 Tokyo Branch was opened and on 20th October 1950, Osaka branch was opened. (Source: boijapan.com)

State Bank of India opened a representative office in Tokyo on 26th January, 1978, which was transformed into a full fledged branch on 23rd January 1980. The branch was opened with the objectives, to foster the bilateral trade between India and Japan and to help Indian Corporate to access the financial market in Japan. Another branch in Osaka was opened on 5th September, 1984. (Source: sbijapan.com)

7.1 Key Implications for banking sector

7.1.1 Enhanced bilateral interaction on financial services would facilitate comprehensive exploitation of trade potential between India and Japan. India has opened up to FDI by many of its financial services. The Insurance Regulatory and Development Authority (IRDA) opened up the state monopoly of domestic insurance market to private companies, including foreign companies in 1999. The IRDA issued insurance licenses to fifteen private insurance companies in joint ventures with foreign insurance companies in December 2001. A Japanese insurance company has

already entered the Indian private insurance market through a joint venture with an Indian company.

7.1.2 Regulations on foreign and direct investment in the banking sector were liberalized in March 2001. Foreign investment of up to 74 per cent, including all sources, is now permitted in the private banking sector through the automatic route. FDI and portfolio investment in nationalized banks are subject to overall statutory limits of 20 per cent.

7.1.3 In the case of Japan, many foreign-owned financial institutions withdrew from the Japanese market after the 1997 financial crisis. In some instances, their Japanese offices were integrated following international mega-mergers. However, foreign-owned financial institutions have started entering again since the late nineties. This can be attributed to financial liberalization and improved growth expectations.

7.1.4 Japanese banks based in India mainly support Japanese companies present there. We see the following vicious circle; Japanese banks are not motivated to enter India without a critical mass of Japanese companies. On the other hand, Japanese companies including the manufacturing sector are discouraged from making investment in India due to the very small presence of the Japanese financial sector there.

7.1.5 Other constraints in the financial services area which are currently perceived

by Japanese institutions include the following:

- Japan attaches importance to commercial presence commitments, in particular, the abolition of limitations on foreign equity participation and forms of commercial presence, and the right of establishment.
- However the public monopoly in insurance has been eliminated, it is felt that the limitation of 26% on foreign equity participation in insurance is restrictive compared to other Asian countries. Also, foreign insurance companies can not open direct branches. Changes in both these regulations may facilitate a greater Japanese presence in the sector.

8. Conclusion

India and Japan engage themselves bilaterally to augment their financial markets interaction. Both the countries should make efforts to make adequate presence of service providers in other country's financial sector. The mutual presence of banking, financial services and insurance services of India and Japan would be required by and for trade in goods and other services. Such services should also be encouraged to serve the growing trade in goods and other services. In particular, both parties may co-operate in the field of financial services with a view to promote the regulatory co-operation and share related experiences. It will develop the financial

market and improve the financial market infrastructure. It is also recognized that, improvement of efficiency and competitiveness of the financial markets of the two countries is of great importance. It is thereby recommended that both countries emphasize on the financial guarantee of the state run banks such as EXIM banks for business activities between the two countries, endeavor not to apply any restrictions for transfer of earnings; and work towards meaningful commitments for building commercial presence in financial services. It is also advised that the Financial Services authorities of both sides mutually discuss to increase cooperation in this area. Foreign banks, which need to build a rapport with the Indian customers, may adopt alternative approaches to win the "race for the customer" and build a value-creating customer franchise in advance of regulations potentially opening up post 2009. At the same time, they should also seek potential acquisition opportunities as and when they appear in the near term. Maintaining a fundamentally long-term value-creation mindset will be their greatest challenge.

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Biography

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