

ON WHAT A Japanese Investment Bank's Global Role Should Be

HOW DO you view recent trends in the Tokyo capital market?

Umemura: This past year, the pace of development has been rapid. In keeping with the directions set forth in the report of the U.S.-Japan Yen-Dollar Committee in May 1984, the authorities liberalized the Euroyen market, established a yen bankers' acceptance (BA) market, and further broadened the participation of foreign securities companies in the market—as lead managers of Euroyen bond issues, as participants in syndicates to underwrite government bonds in Japan, and in other activities.

It was also an important year because the terms at which long-term government bonds were being issued more closely reflected yields in the secondary market.

The introduction of a BA market was a significant step toward development of a short-term money market, but this market is only in its initial stage. I believe that a precondition for the growth of the BA market is the introduction of a full-fledged treasury bill market.

A comparison with other countries is revealing. The size of the short-term money market in Japan is only one-tenth that of the United States, although the size of our economy is one-third that of the United States. Even compared with the size of the Japanese capital market, the short-term money market is small. For the efficient functioning of a capital market and the smooth adjustment of interest rates to market forces, the short-term money market must be expanded. Thus, in addition to yen BAs and existing short-term government bonds, Japan needs to create and build a treasury bill market.

WHAT DO you see as the longer-range implications of recent developments in the Tokyo market?

Umemura: As is evident from events of the past year, the rapid pace of deregulation is both diminishing administrative controls and steadily dismantling the previous shelters that have protected many Japanese financial institutions from the full force of competition.

More important, liberalization is presenting us with new business opportunities, and at Nikko, we have moved quickly to rationalize our internal operations and to allocate managerial resources to the most promising business opportunities.

RECENTLY, MANY analysts have drawn attention to the emergence of Japan as the largest net exporter of capital in the world. What is your perspective on these flows?

Umemura: From an economic standpoint, the growth of capital outflows is related to the rising surplus in the current account of Japan's balance of payments. This surplus is projected to be \$39 billion in the current year and \$48 billion next year. It is only natural that Japan reexports its earnings from trade.

Securities investment accounts for approximately one-half of capital outflows. This is

the result of the growth of financial assets in Japan and the desire of investment managers to diversify their portfolios. Over the past year or two, both institutions and individuals in Japan have been attracted by high returns overseas. The trend toward international diversification of portfolios should continue.

I would also note the high level of capital inflows as more international investors diversify their portfolios to include Japanese securities. Thus, although both capital inflows and outflows will continue to grow, I believe that Japan will remain a net exporter of long-term capital for some time.

AS THE Tokyo market expands and capital flows increase, what issues do you see facing Nikko Securities as a global investment bank?

Umemura: There are three strong currents in the financial services industry: deregulation, internationalization, and the growing reliance on information systems. In these currents, we must steer a course that will not only keep us in the lead in our traditional businesses but take us into new waters.

Although we could debate the merits of our strategy, we have chosen to remain a full-service financial institution committed to serving both individuals and institutions. Over the years, our customers have assumed they can come to us for any service, and we will not disappoint them.

In providing a full range of services, we are striving for balance. For example, the ratio of profits from equities-related business and of those from other securities, such as bonds and investment trusts, is now 65:35. We are gradually moving it toward 50:50 by building our capabilities for trading and placing bonds. This has involved adding staff to our bond operations both domestically and abroad. We look forward to the introduction of a bond futures market next month and are prepared to take advantage of the opportunities—for our clients and ourselves—that such a financial futures market offers. There is also talk of launching a detachable warrants market in the near future.

Another means of achieving balance is to make use of our natural strengths. Because we are based in Japan, we believe we have an advantage for yen-linked products as the role of the yen as an international currency grows. And as I just mentioned, we are in an excellent position to help Japanese investors who want to invest abroad.

We also want good geographic balance and already have a solid position in all the major markets. For example, we are very strong in Samurai bond underwritings for Pacific Basin countries. This position is attributable to our long involvement in the region. For years, we have been active in the Republic of Korea. In the People's Republic of China, we recently opened a representative office in Beijing and are preparing for another one in Qingdao.

As the core economy in Asia, Japan must play a growing role in assisting its neighbors raise the capital necessary for economic development—and develop their own capital markets. We take this responsibility seriously at Nikko.

WHAT OBJECTIVES will you be pursuing over the next five years?

Umemura: I think the strategy I just outlined points to where we want to be five years from now. By then, we are aiming to have more than 110 offices domestically and more than 20 abroad, all linked as a global network. And we intend to provide a range and quality of service—for individuals and institutions in Japan and internationally—that will give us an edge on other excellent investment banks.



Shoji Umemura

President since 1981, Shoji Umemura has 52 years of experience with Nikko Securities. He is currently serving as Chairman of The Bond Underwriters Association of Japan.

WHAT RESOURCES are required to compete internationally?

Umemura: The answer to that question starts with financial resources. Nikko has an equity base of ¥420 billion, or about \$1.7 billion. This ranks us among the top three securities companies in the world.

Naturally, we must also have the human resources and creativity to best use our capital resources. Quite honestly, Japanese financial institutions do not always compare well on technical skills. Part of the reason is historical. For instance, I think the leading American banks are ahead of their Japanese counterparts in global cash management. But then, Japan has not had a large money market in which to invest liquid assets.

To cite what is both a Japanese and Western maxim: necessity is the mother of invention. The necessity is evident in Japan. The large volume of government debt issues is leading to the rapid development of a secondary bond market. Liberalization of interest rates has forced the design of new savings instruments. Slower economic growth has prompted corporate treasurers to find the lowest-cost capital, thus leading to disintermediation.

Nikko has contributed its share of innovations in the past, and I am confident that we

will continue to in the future. Back in 1961, we were the first to create and offer a bond investment trust fund in Japan. More recently, in 1984, we introduced Home Trade One, the first home brokerage system using a push-button phone to place buy and sell orders.

Our international accomplishments go back many years. In 1961, we were instrumental in setting up the Japan Fund in the United States. This past year, we launched the first Euroyen money market fund, which is based in Luxembourg.

For a company generally recognized as being bound to tradition, I think we have demonstrated we can be effective marketers of innovative services. But they must be services needed by our clients. I am continually saying that we must grow with our clients.

WHAT PARTICULAR services do your clients want from you, and what are you doing to provide them?

Umemura: Since our clients want a variety of services, we are relying on the combined resources of Nikko itself, our overseas subsidiaries, and such members of the Nikko Group as the Nikko Research Center, Ltd.; the Nikko Securities Investment Trust Management Co., Ltd.; Nikko International Capital Management Co., Ltd.; and Nikko Venture Capital Co., Ltd.

One service our corporate clients want is global underwriting. The development of the Euroyen market and the emergence of the yen as an international currency have prompted us to strengthen our international network of 18 offices. We have put additional capital into our American and Luxembourg subsidiaries and are in the process of establishing a merchant bank in Sydney. In Paris, we plan to upgrade our representative office to a subsidiary.

Another service in high demand is global dealing, and we have placed a high priority on expanding our capabilities in this area. To minimize market risk, dealing skills are an essential complement to our brokerage and underwriting skills. We are putting in place a 24-hour dealing system centered on our operations in Tokyo, London, and New York. In another move to help our clients hedge risk, we have become a member of the major financial futures and options exchanges.

Our customers also want fast delivery of, and easy access to, a variety of products. To meet the domestic demand for variety, we recently opened a credit card company and have ventures with other companies to provide particular services. To meet the demand from customers around the world for faster delivery of services, we have been upgrading our data processing and telecommunications systems.

To provide any of these services, we must also invest in people. After highly selective recruiting, we spend considerable time and effort on training new employees. For highly specialized areas—such as bond trading, swaps, foreign exchange, and computer systems—we are structuring our organization to promote specialization. And overseas, we have been fortunate in recruiting top-level individuals for senior positions.

NIKKO

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