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Chapter 7: Trade and Project Financing

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How Do I Get Paid (Methods of Payment)

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There are a number of methods used to settle payment in Japan: cash in advance, letter of credit used in conjunction with a documentary draft (time or sight), promissory note, documentary collection or draft, open account and consignment sales. As with U.S. domestic transactions, a major factor in determining the method of payment is the degree of trust in the buyer's ability and willingness to pay.

Because of the protection it offers to the American exporter and the Japanese importer, an irrevocable letter of credit (L/C) payable at sight is commonly used for settlement of international transactions. As large Japanese general trading companies often serve as intermediaries to small and medium-sized companies, L/Cs are often issued in their name rather than in the name of the end user of the product. With the trading company taking on the risk of the transaction, the U.S. firm is protected from the possible bankruptcy of the smaller company.

Another payment option is the use of documentary collection or open account with international credit insurance that, unlike the letter of credit, allows the importer's line of credit to remain open. At the same time, this option protects the exporter if the buyer goes bankrupt or cannot pay. International credit insurance can be obtained from the Export-Import Bank of the United States or private insurers.

A payment method widely used in Japan but sometimes unfamiliar to U.S. companies is the promissory note (*yakusoku tegata*). Promissory notes are IOUs with a promise to pay at a later date, typically 90 to 120 days. Banks will often provide short-term financing through discounting and rollover of notes. Factoring and other forms of receivables financing (whether with or without recourse) are not common in Japan, and more conservative businesspeople find such arrangements a violation of the "relationship" between buyer and seller. It should be noted that, domestically, it is not uncommon for the buyer to request, and be granted an extension of the term of the *tegata* if there are cash-flow problems.

How Does the Banking System Operate

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While financial system deregulation and international competitive pressure has drastically changed the face of Japanese banking (the consolidation of 19 banks into four mega banks), the connection between corporate finance and banking institutions and non-financial corporations remains much tighter in Japan than in the United States;

and extends far beyond simple lender/borrower relationships. Much corporate banking business is rooted in either *keiretsu* or regional relationships, and Japanese banks are frequently shareholders in companies that conduct banking business with them, although there are signs of changes.

This unique relationship between a company and its bank has been long-standing; until recently, a Japanese company rarely changed its primary lender, although it would occasionally "shop around" for better credit arrangements. Even when credit is loose, companies sometimes borrow in excess of their need in order to maintain good relations with their bank and to ensure that funds will be available in leaner years. Banks are often large shareholders in publicly traded corporations, have close relationships with both local governments and national regulatory agencies, and often play a coordinating role among their clients. The collapse of the asset price "bubble" and the consequent worsening of bank balance sheets since the early 1990s, as well as corporate borrowing outside of traditional channels, has increasingly caused borrowers to tap international capital markets, and placed traditional banking systems under considerable strain. However, it remains safe to say that the Japanese commercial bank system is much more relationship oriented than the transaction-based U.S. system.

While large corporations with suitable credit ratings (especially export-oriented firms) can rely on corporate bond issues rather than banks for financing, bank lending continues to be the primary financing method for small and medium sized companies. However, after the "bubble" economy of the late 1980s and early 1990s, Japanese banks had a harder time maintaining strong capital positions, and consequently became more restrictive, leading to a credit crunch. In November 1996, the Japanese government embarked on a "Big Bang" financial reform initiative and in December of 2007 announced a plan to improve Japan's global competitiveness in financial services. While the actual long-term market impact of this liberalization still remains to be seen, the psychological impact in raising awareness of the potential effects of deregulation is now apparent.

Japanese banks offer regular and time deposits and checking accounts for businesses. Checks are negotiable instruments that are in effect payable to the bearer (rather than to the order of the payee, as in the United States). This limits the usefulness of checks, and in fact, most payments are made by electronic bank transfer (which costs a few hundred yen on average), or by sending cash through the postal system. The banks (and now investment/securities firms) historically waged an uphill battle against the recently privatized postal savings system for consumer deposits, but now that postal savings bank must pay taxes and deposit insurance, in addition to losing its implicit government guarantee, increased competition in the banking sector has already begun.

Personal checking accounts are almost unknown in Japan. Most individuals use electronic bank transfers to settle accounts. Cash settlement is also very common and the Post Office has a mechanism for payment by "cash envelope" which is widely used in direct marketing and other applications. Many Japanese banks now operate 24-hour cash machines (as do some credit card companies). Bank and other credit cards are easy to obtain and are widely accepted. The consumer credit card market reached nearly 15 trillion yen in 2004, equivalent to 5.3 percent of personal consumption. Some bank credit cards offer revolving credit, but in most cases balances are paid in full monthly via automatic debiting from bank accounts.

The relationship among trading company, end user and exporter is an important feature of the financing environment in Japan. The Japanese general trading company (*sogo shosha*) is an integrated, comprehensive organization that embraces a range of functions including marketing and distribution, financing and shipping and the gathering of commercial information. It performs functions that in the United States would be carried out by import/export companies, freight forwarders, banks, law firms, accounting firms and business consultants. Thus, U.S. firms dealing with trading companies should familiarize themselves with the financing capabilities of such firms.

Foreign-Exchange Controls

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Foreign exchange regulations have almost no impact on normal business transactions.

U.S. Banks and Local Correspondent Banks

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Besides seven U.S. banks with branches in Japan, many U.S. banks have correspondent relationships with Japanese banks, which themselves have many branches and subsidiaries in the United States.

Commercial Banks in Japan

Resona Bank

2-1 Bingomachi 2-chome, Chuo-ku, Osaka 540-8610

Tel: +81/6/6271-1221; fax: 6268-1337

www.resona-hd.co.jp/index-e.htm

Bank of Tokyo-Mitsubishi UFJ

2-7-1 Marunouchi, Chiyoda-ku, Tokyo 100-8388

Tel: +81/3/3240-1111; fax: 3240-4764

www.bk.mufg.jp/english/

Development Bank of Japan

1-9-1 Ohtemachi, Chiyoda-ku, Tokyo 100-0004

Tel: +81/3/3244-1770; fax: 3245-1938

www.dbj.go.jp/english/

Japan Bank for International Cooperation

1-4-1 Ohtemachi, Chiyoda-ku, Tokyo 100-8144

Tel: +81/3/5218-3579; fax: 5218-3968

www.jbic.go.jp/english/index.php

Mizuho Corporate Bank

1-3-3 Marunouchi, Chiyoda-ku, Tokyo 100-8210

Tel: +81/3/3214-1111

www.mizuhocbk.co.jp/english/

Sumitomo Mitsui Banking Corporation

1-1-2 Yurakucho, Chiyoda-ku, Tokyo 100-0006

Tel: +81/3/5512-3411; fax: 5512-4429

www.smbc.co.jp/global/index.html

Multilateral Development Bank Offices in Japan:

Asian Development Bank
Second floor, Yamoto Seimei Building
1-1-7 Uchisaiwai-cho, Chiyoda-ku, Tokyo 100-0011
Tel: +81/3/3504-3160; fax: 3504-3165
E-mail: adbjro@adb.org or www.adb.org/

Project Financing

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General Availability of Financing

While some large U.S. companies in Japan enjoy strong relationships with the larger Japanese "city banks," most medium and small-sized U.S. firms have stated that it is difficult to secure the specific type of trade financing services needed for importing and distribution. In Japan, credit evaluation is heavily asset-based, and real estate is still favored as collateral despite the collapse of "bubble" era valuations. Moreover, a firm's ability to borrow may also be based on its personal relationships and rapport with bank officials rather than on typical U.S. standards of credit-worthiness. Some smaller firms report that they have been forced to secure needed financing from offshore sources. For U.S. companies with operations in Japan, teaming up with Japanese partners in a joint venture has been effective as a way to receive better treatment from Japanese banks.

While most American banks operating in Japan do engage in lending to subsidiaries of U.S. companies (especially their home market clients), many of them focus on higher value-added lines of business than conventional credit products. When a Japanese bank extends credit to a foreign-owned company in Japan, it generally evaluates the financial status of both the borrower and its parent company. Even in cases where the Japanese subsidiary is financially strong, the parent company is often requested to guarantee the obligation (although a "Letter of Awareness" may be accepted in lieu of a guarantee).

Types of Export Financing and Insurance

The Government of Japan's programs to promote imports and foreign investment in Japan include tax incentives, loan guarantees, low-cost loans to Japanese and foreign investors for import infrastructure through the Development Bank of Japan and other loan programs. Underscoring the Government's emphasis on import promotion, both the Ministry of Economy, Trade and Industry (METI) and the Japan External Trade Organization (JETRO) have established import divisions.

Four major public financing corporations, the Japan Bank for International Cooperation, the Development Bank of Japan, the Japan Finance Corporation for Small Business and the National Life Finance Corporation, now make low-interest loans to encourage imports to and investment in Japan. In addition, the services of the Japan Regional Development Corporation, a government-affiliated institution that develops business parks and provides long-term loans at low interest rates, are available to foreign companies.

The Japan Bank for International Cooperation's import credit program for manufactured goods aims to provide support for the import of manufactured goods from developed countries to Japan. Five-year secured or guaranteed loans up to 70 percent loan-to-value and credit lines at preferential interest rates are available to importers, distributors and retailers incorporated in Japan who plan to increase their imports of manufactured goods excluding food products 10 percent or more over the previous year. Direct 70 percent loan-to-value long-term loans are also available to foreign exporters for the purchase of manufactured goods to be exported to Japan under deferred-payment terms, as well as to foreign manufacturers and intermediary financial institutions for investment in production facilities and equipment to be used to produce goods for the Japanese market.

The Development Bank of Japan (DBJ) offers loans designed to increase imports into Japan. These loans are available to Japanese companies with at least 33 percent foreign capital or registered branches in Japan of non-Japanese companies for 40 to 50 percent of project costs for the expansion of business operations in Japan.

The Japan Finance Corporation for Small Business and National Life Finance Corporation has expanded their program to facilitate import sales. The program aims to provide support to small-scale retailers, wholesalers and importers in Japan for investments to increase imports to Japan. A program between U.S. Eximbank and the Export-Import Insurance Division of METI (EID/METI) provides for co-financing insurance for U.S. exports to developing countries. EID/METI will also be providing advance payment insurance for U.S. exports to Japan. For additional details on these and other cooperative financing programs, U.S. companies should contact U.S. Eximbank.

No insurance for U.S. exporters is available from the Japanese Government.

Other Financing

Japan has been a member of the Multilateral Investment Guarantee Agency (MIGA) since it was established in 1988. In addition to the investment loan programs from Japanese Government-affiliated lenders described above, prefectures and municipalities offer various incentives, including construction, land acquisition and labor hiring subsidies, special depreciation of business assets, tax deferrals for replacement of specific assets, exemption from special land-owning taxes assessed by municipalities and prefectural and municipal real estate acquisition, enterprise and municipal property tax reductions. In addition, most prefectures offer loan programs to encourage companies to establish local operations.

Japan's venture capital specialist funds are only half the size of those in the United States. Traditionally the top Japanese venture capital companies have acted more like quasi-banks than venture capital firms. Also, Financial Services Agency guidance to brokers to set tough standards for companies seeking to go public results in even the best companies taking up to a decade to get a listing on the over-the-counter stock market – less than 1000 over-the-counter stocks are listed on the nine-year-old JASDAQ, Japan's electronic OTC market.

Types of Projects Receiving Financing Support: In line with the Cabinet Decision in March 1995, the Export-Import Bank of Japan (JEXIM) and the Overseas Economic

Cooperation Fund (OEFC) merged on October 1, 1999, creating a new institution, the Japan Bank for International Cooperation (JBIC).

JBIC is a governmental institution that deals with external economic policy issues such as encouraging exports, securing access to energy resources, promoting direct overseas investments and improving Japan's external imbalances through financial assistance to the trade and investment activities of Japanese companies.

The financial facilities offered by JBIC include export loans, import loans, overseas investment loans and untied loans. JBIC also provides loan guarantees to private financial institutions, short-term loans designed to finance the external transactions of the governments of developing nations (bridge loans), and equity participation in the overseas projects of Japanese companies.

JBIC's international financial operations focus on projects in developing countries where local financial institutions cannot provide financing on their own. As JBIC's mandate is the support of internationalization for Japanese companies, its loans can be distinguished from Overseas Economic Cooperation operations, which targets the economic development of developing countries.

Overseas Investment Loans and Overseas Project Loans: These loans are typically granted via JBIC and extended to Japanese corporations for overseas investment activities and overseas projects. Overseas investment loans can also be made to overseas joint ventures involving Japanese capital and to foreign governments for capital investments or loans to joint ventures involving Japanese capital.

Un-Tied Loans: Extended to foreign governments, foreign governmental institutions, foreign financial institutions (including multilateral development banks), foreign corporations, and so forth for high-priority projects and economic restructuring programs in developing countries. These loans are not tied to the procurement of goods and services from Japan but are restricted to the specific purposes designated for each loan. These loans are managed by JBIC.

Web Resources

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Asian Development Bank (ADB): www.adb.org/

ADB Japan Representative Office: www.adb.org/JRO/default.asp

Development Bank of Japan (DBJ): <http://www.dbj.go.jp/english/>

Export-Import Bank of the United States: www.exim.gov/

Ex-Im Country Limitation Schedule: www.exim.gov/tools/country/country_limits.html

Overseas Private Investment Corporation (OPIC): www.opic.gov/

Japan Bank for International Cooperation (JBIC): <http://www.jbic.go.jp/english>

Japan External Trade Organization (JETRO): www.jetro.go.jp/

Japan Finance Corporation for Small and Medium Enterprise: www.jasme.go.jp

Japan Ministry of Economy, Trade and Industry (METI): www.meti.go.jp/english/

Japan Ministry of Foreign Affairs (MOFA): <http://www.mofa.go.jp/>

Small Business Administration Office of International Trade: www.sba.gov/oit/

U.S. Agency for International Development: <http://www.usaid.gov>

USDA Commodity Credit Corporation: www.fsa.usda.gov/ccc/default.htm

U.S. Trade and Development Agency: www.tda.gov/