Consideration about the Way of Balancing Local Finance Institution's Business Model and Local Problem Solution

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Abstract

In this paper, I have examined, from the point of view of PPPs (public-private partnerships), methods for regional financial institutions to contribute to the economy under the effects of regional regeneration. By describing the history of relationship banking (community-based finance) and the changes that have taken place in the environment regional financial institutions operate in, I have also demonstrated the need for regional financial institutions to take part in solving regional issues.

Furthermore, using a "PPP Triangle", made by modifying and expanding the Pestoff Triangle so as to be able to apply it to the current state of Japan's PPPs, I have also shown that there is a relationship between daily business operations and the resolution of regional problems by visualizing the point of contact between regional financial institutions and their respective regions.

Based on the above, as a business model that both solves regional issues and manages financial institutions, the application of business revitalization know-how to the public sector, use of various financial instruments (utilization of securities subsidiaries, sale-leaseback transactions, real estate liquidation, asset-based lending (ABL), and so on), and a collaboration with depositors through crowdfunding has been proposed.

Keywords: Regional Financial Institutions, Relationship Banking (Community-based Finance), PPP (Public-Private Partnership),Crowdfunding

Introduction

This paper examines, through the perspective of PPPs (public-private partnerships), methods for regional financial institutions to contribute to the economy under the effects of regional regeneration.

The first section will cover the history of relationship banking (community-based finance), in which the management supervision of present-day financial institutions has its roots.

Section II will discuss the current state of and issues faced by regional financial institutions (including issues regarding procurement and operation such as the decline in loan-to-deposit ratios, as well as reliance on public bodies for credit), changes in the external environment (such as financial issues faced by public bodies), and so on, under present-day community-based finance, having undergone the events covered in Section I.

Building upon on the contents of Section II, Section III uses the PPP Triangle, which is used at the Toyo University Research Center for Public/Private Partnership of which I am a member, to visualize the point of contact between regional financial institutions and their respective regions and show how daily business operations and the resolution of regional issues are related. To conclude, Section IV will delve into a business model that balances between solving regional problems and managing financial institutions.

I Relationship Banking

1. Background of Relationship Banking Policies

Japan's financial instability after the collapse of the bubble economy started with the managerial crisis and bankruptcy of Cosmo Credit Corporation and Kizu Credit Cooperative, and continued with the collapse of Hyogo Bank, and afterwards of Yamaichi Securities, Hokkaido Takushoku Bank, Nippon Credit Bank, Long-Term Credit Bank of Japan and so on. Japan's unstable financial system continued to be considered an obstacle to its recovery till the late 1990's.

After many twists and turns, including policy differences as regards to what should be done (known as the conflict between the hard landing and soft landing theories), the Minister of State for Financial Services Heizō Takenaka formulated plans to tackle the instability of the financial system. These are described in the "Financial Revival Program - Revival of the Japanese Economy through Resolving the Nonperforming Loan Problems of Major Banks" (Financial Services Agency [2002]) announced on October 30th, 2002 and the "Action Program Concerning Enhancement of Relationship Banking Functions - Securing the Revitalization and Sustainability of Small and Medium Enterprises Financing Toward Solving Nonperforming Loan Problems in Small- and Medium-sized and Regional Financial Institutions" (Financial Services Agency [2003a], hereafter referred to as "Action Program I") announced on March 28th, 2003. The latter is considered to be a concrete, detailed plan formulated in light of a report by the Second Subcommittee, Sectional Committee on Financial System, Financial System Council titled "Toward Enhancing the Functions of Relationship Banking" (Financial Services Agency [2003b]) submitted on March 27th, 2003.

Under these two policies, major banks and regional financial institutions were dealt with through different approaches, and in rural financial institutions, in particular, efforts for credit control and improving profitability were made through the promotion of relationship banking, following the policy outlined in the Financial Service Agency's [2003a] statement, "Setting the two years until 2004 as an "Intensive Improvement Period" for regional finance, each small- and medium-sized and regional financial institution should implement various measures following the recommendations of this report to strengthen the functions of relationship banking, revitalize SMEs, and stimulate regional economies, and this will simultaneously lead to the resolution of the NPL issue."

2. Promotion of Initiatives for Relationship Banking

As explained in the previous section, the Financial Services Agency adopted a different approach from major banks in their administrative methods to solving the nonperforming loan issue in regional financial institutions, and led efforts to improve management in regional financial institutions while adhering to the policies stipulated in Action Program I.

To be specific, as part of the measures taken for the revitalization of SME financing and stimulation of regional economies during the Intensive Improvement Period from 2003 to 2004, the Financial Services Agency required regional financial institutions to develop a strategy for enhancing the functions of relationship banking, annually submit a progress report, as well as publish plans and reports in media such as official websites. In this way, they sought to bring about management reform in regional financial institutions under public scrutiny.

Although intensive efforts were devoted to relationship banking in the two-year period from 2003 to 2004, such measures continued to be taken afterwards as well. The two years from 2005 to 2006 were dedicated to the "Action Program Concerning Enhancement of Relationship Banking Functions" (Financial Services Agency [2005], hereafter referred to as Action Program II), which was devised in light of the policies listed in the "Program for Further Financial Reform" (Financial Services Agency [2004]). In other words, through Action Program I and II, the Financial Services Agency carried intensive reforms for four years, from 2003 to 2006.

3. Report by the Second Subcommittee, Sectional Committee on Financial System, Financial System Council (April 2007)

During the time period devoted to relationship banking mentioned in Subsection 2, the Second Subcommittee, Sectional Committee on Financial System, Financial System Council submitted a report titled "Evaluation of Efforts in Community-based Finance and a Future Course of Action - Accumulation of Regional Information for a Sustainable Business Model" (Financial Services Agency [2007]) on April 5, 2007. This report intended to lay out a plan on where to go after the end of Action Program II.

Although the actions taken up until 2006 succeeded in causing a decline in the nonperforming loan ratio, bringing the emergency situation back to normalcy, the report called for lasting endeavors rather than actions in the form of temporary programs, as well as for continued efforts with regards to improving regional financial institutions through relationship banking and addressing the increase in negative evaluations in the user survey it mentioned earlier.

The three actions equally desired from all financial institutions are directly related to the core of community-based finance: (1) increasing support of client companies in accordance with their life cycles, (2) thoroughly implementing funding methods suitable for SMEs, including financing techniques to assess business value, and (3) making sustainable contributions to regional economies through the accumulation of regional information. How these would be achieved would be left up to the financial institutions themselves (Figure 1).

Figure 1: Specific action points in report by the Second Subcommittee…Financial System Council (April 2007)

Action Points on How to Proceed Further

1. Increasing support of client companies in accordance with their life cycles

Increasing inspection and support of SMEs in accordance with the various stages of their business growth

○ Recovery Phase
・ Most directly linked to the core of community-based finance for the assessment of business value.
・ Early revival while corporate value is still stable and sustainable business reconstruction after revitalization are of utmost importance.
・ Only regional financial institutions can bring about change in external managers.
・ Further utilization of the SME Revitalization Support Council's funds.
・ New methods with upside potential, appropriate use of DIP financing, and so on.

○ Launch Support/ Support for New Businesses
・ Use of funds, industry-academia-government collaboration, use of a system to guarantee support for renewed efforts, and so on.

○ Support for Management Improvement

○ Business Succession (explicitly declare it the fourth stage of a local enterprise's life cycle and grant support accordingly)

2. Thoroughly implementing funding methods suitable for SMEs, including financing techniques to assess business value

○ Financing techniques to assess business value = thorough implementation of financing techniques that do not overly rely on mortgage or personal surety bonds
・ Improving assessment abilities (especially in MSMEs).
・ Appropriate evaluation of qualitative information, improving quality of quantitative information.
・ Use of ABL (Asset Based Lending), covenants, and so on.

○ Thorough implementation of other financing techniques suitable for SMEs
・ Utilization of funds and investment methods with upside potential, introduction of risk money through the use of equities, and so on.
・ Execution of market-oriented indirect financing strategies, such as CLO and syndicated loans.

3. Making sustainable contributions to regional economies through the accumulation of regional information

○ Comprehensive revitalization of communities
・ Proactive support for devising a vision plan that makes full use of planning and investigative abilities.
・ Proactive participation in efforts for public-private partnerships
— A collaborative effort where the public and private sectors play equal roles, and all community members share the same vision.
— Risk and return, contract governance are highly important. Financial institutions are expected to proactively participate as coordinators.

○ Offering of various services for the revitalization of regional economies
・ Efficient use of senior citizens' assets such as reverse mortgage, the dissemination of financial knowledge, and so on.
・ Contribution to solving the multiple-debt issue, funding and support for communities, businesses, and so on (especially cooperative financial institutions).

○ Making of suitable commitments to regions, regulation of the public sector
・ Tense, formal relationship arising from appropriate cost-risk analyses. Responsible for the regulation of local public body finances.

Source: Financial Services Agency Official Website (http://www.fsa.go.jp/singi/singi_kinyu/tosin/20070405/01.pdf)

A noteworthy role of financial institutions in the stimulation of regional economies is, as previously mentioned, "(3) making sustainable contributions to regional economies through the accumulation of regional information." (Figure 1) In order to achieve this, three major courses of action were proposed: "comprehensive revitalization of communities", "offering of various services for the stimulation of regional economies", and "making of suitable commitments to regions, regulation of the public sector."

While considering the topic of regional regeneration and the role of financial institutions, of particular significance, regarding the "comprehensive revitalization of communities", are the expectations placed on regional financial institutions for proactively supporting the devising of a vision plan that makes full use of their planning and investigative abilities, and for proactively participating in efforts for public-private partnerships, as well as on financial institutions for actively participating as coordinators. In this way, the two were anticipated to be the leaders for the promotion of public-private partnerships (PPP).

As part of measures for the "offering of various services for the revitalization of regional economies", the report calls for the efficient use of reverse mortgages and other assets of senior citizens, and for the financing and support of communities and businesses.

The report also pushes for the "making of suitable commitments to regions" and the "regulation of the public sector". With issues surfacing such as the financial deterioration of local public bodies, and the aging of social capital (public facilities and infrastructure), taken up by all parts of society as an especially serious issue in recent years, coupled with the shortage of financial resources, it is imperative that they take up the role of local public bodies' "main banks" and seek an appropriate, responsible way of dealing with these issues. (Details will be discussed in Section 2.)

As above, the April 2007 report by the Second Subcommittee, Sectional Committee on Financial System, Financial System Council can still be considered to have been an appropriate plan for regional regeneration nine years later, at the time of writing. However, there are unfortunately very few successful cases at present of regional financial institutions taking new initiatives in line with the recommendations of the report. Although, during this time period, regional financial institutions were annually publishing progress reports on their respective "Plan for the Promotion of Community-based Finance" on media such as official websites, as well as making steady progress in the meanwhile, there is a need to take further measures to shorten the gap between what they are capable of and what they should be aiming for.

Moreover, as far as government efforts for regional revitalization are concerned, in recent years it became clear that a collaboration between the industry, academia, government, private companies, and financial institutions would be beneficial. After the establishment of a council or platform for this "industry-academia-government-private-bank collaboration" was proposed as a requirement for receiving support from the government, regional financial institutions are increasingly becoming involved against their will due to requests by their respective regions. Considering the changes in the external environment faced by regional financial institutions, to be covered in Section 2, however, such passive approaches are not expected to yield much result.

Ⅱ Changes in the Environment Facing Regional Financial Institutions

1. Decline in Loan-to-Deposit Ratio

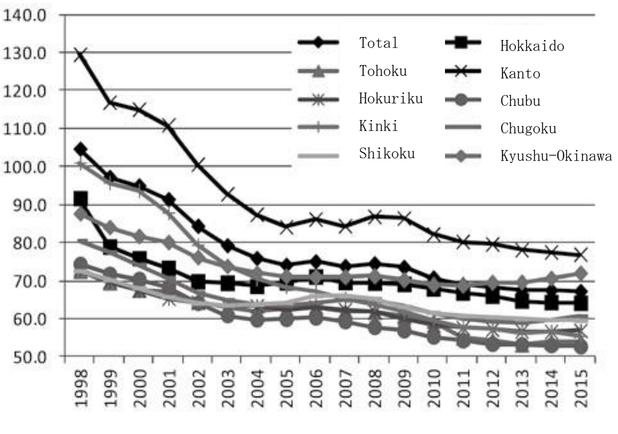
The loan-to-deposit ratio is most indicative of the degree of fund flow and return, and to observe its fluctuation is the first step in observing the changes in the greater environment facing regional financial institutions.

Figure 2 shows a graph made using the "Deposit Balance and Loans Outstanding by Region" statistics published by the Bank of Japan. Looking at the trends in loan-to-deposit ratios (calculated using the average loans outstanding and average total deposits for each year) for each region, the ratios are seen to be declining throughout the country with the national average being 67.2 (in 2015) (Figure 2).

The decline of regional loan-to-deposit ratios can be said to be due both to an increase in deposits, the denominator, as well as a decrease in loans, the numerator. Figures 3 and 4 use indexed data with the 1998 average set to 100 as the base value, and although deposits rise up to a national average of 148.1 (in 2015), loans lag behind at a national average of 95.1 (in 2015). While the degree of change differs, a common trend is an increase in deposits while loans lag behind.

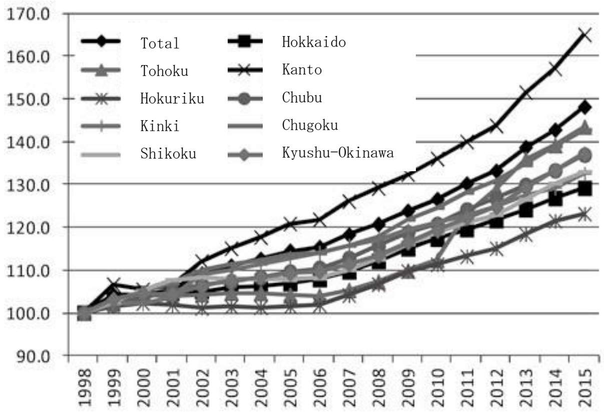
Considering that most regional financial institutions regard contribution to their communities as one of their missions, the regional distribution of loans would be especially desirable. The overall declining trend, however, currently poses a problem (Note 1).

Figure 2: Trends in Loan-to-Deposit Ratios by Region



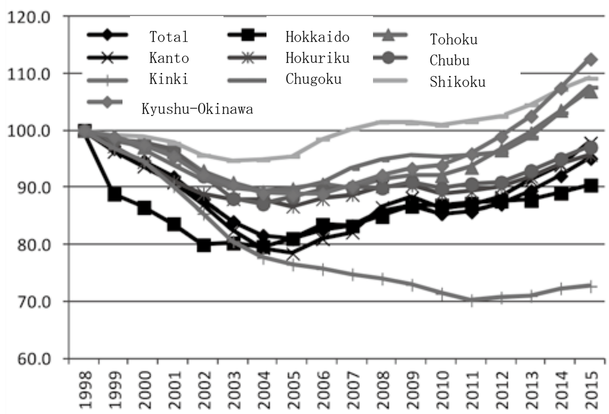
Source: Based on data from "Deposit Balance and Loans Outstanding by Region" by Bank of Japan

Figure 3: Trends in Deposits by Region



Source: Based on data from "Deposit Balance and Loans Outstanding by Region" by Bank of Japan

Figure 4: Trends in Loans by Region



Source: Based on data from "Deposit Balance and Loans Outstanding by Region" by Bank of Japan

2. Increase of Financing to Local Public Bodies

Although it can be concluded from Subsection 1 that there is a mismatch between regional loans and deposits, upon further examination, a clear rise in financing to local public bodies was found. Based on statistics from "Loans Outstanding by Industry" by the Bank of Japan, Figure 5 indexes total loans, loans to local public bodies, and loans to SMEs with the 1998 average set to 100 as the base value, in the same way as the previous graphs. Here we see that loans to SMEs, who are central to the distribution of loans by regional financial institutions, go down by around 30% to

74.6 (in 2015), while loans to local public bodies rise to over a three-fold increase to 317.1 (in 2015) (Figure 5).

Figure 5: Trends in Loans Outstanding of Local Public Bodies and SMEs

	Total Loans	Local Public Bodies	SMEs
1998	100.0	100.0	100.0
1999	99.0	99.5	94.7
2000	95.3	98.6	96.4
2001	91.3	101.7	89.8
2002	86.7	114.8	81.9
2003	92.9	124.4	76.2
2004	80.2	134.5	73.9
2005	79.8	147.5	73.3
2006	81.3	160.5	76.5
2007	82.1	172.6	76.2
2008	84.6	199.7	74.9
2009	84.9	227.7	73.4
2010	83.6	248.4	71.7
2011	83.8	260.5	70.5
2012	85.2	277.7	70.1
2013	87.4	291.3	70.8
2014	90.1	305.6	72.3
2015	93.1	317.1	74.6

Source: Based on data from "Loans Outstanding by Industry" by Bank of Japan

Tokyo Shoko Research, a large private credit reporting company, carries out a continuous questionnaire-based survey of banks regarding loans for local public bodies. According to the "Survey of Loans Outstanding of Local Public Bodies, SMEs, etc." (Tokyo Shoko Research [2016]), "The total loans outstanding of 112 banks to local public bodies for the year ending on March 2016 amounted to ¥28.3708 trillion, increasing by 3.3% (¥926.6 billion) as compared to the previous year, when they amounted to ¥27.4442 trillion. Out of the 112 banks, 71 (63.3%) had increased their loans outstanding to local public bodies over the previous year. These 71 banks composed of 2 major banks, 41 regional banks, and 28 second-tier regional banks. There were 79 (70.5%, 2 major banks, 50 regional banks, 28 second-tier regional banks) such banks in the previous year, decreasing by 8 in 2016.

Loans to local public bodies made up 6.60% of total loans outstanding, increasing by 0.05 over the previous year. Since the start of the survey in the year ending on March 2010, the loan ratio has been surpassing that of the previous year every March for 6 consecutive years, and has reached an all-time high." The survey thus points out the increasing trend in loans to local public bodies. As for banks where a large portion of loans go to local public bodies, the survey states, "Out of 112 banks, there were 57 banks (50.8%) where the percentage of loans going to local public bodies increased as compared to the previous year, which is 4 more banks than the previous year (in which there were 53 such banks).

The bank with the highest percentage of loans going to local public bodies was Aomori Bank at 34.1% (34.5% in the previous year), boasting the highest ratio for the second consecutive year. Following behind Aomori Bank were Hokuto Bank at 32.1% (33.9% in the previous year), North Pacific Bank at 25.1% (24.0% in the previous year), The Bank of Iwate at 23.8% (23.5% in the previous year), and The Fukushima Bank at 23.3% (18.1% in the previous year), listed in order.

Out of the top 10 banks with the highest percentage of loans going to local public bodies, 6 banks surpassed their percentage from the previous year. Moreover, excluding The Tottori Bank that comes in 6th place, 9 (8 in the previous year) of these top 10 banks were from the Tohoku and Hokkaido regions. It is possible that being unable to bring about demand for capital in regional companies, their investment of funds shifted towards giving loans to local public bodies instead." It has thus been shown that financial institutions in areas with weak industrial bases depend on the funding of local public bodies, with the ratio in some banks exceeding the average ratio (6.60%, as stated earlier) by almost five-fold.

3. Risk of Financial Deterioration

Subsection 2 covered the increase in loans to local public bodies; however, this will only be considered to have a positive effect on the management of regional financial institutions if both local public bodies and the state providing them credit enhancement are in a sound financial state, and if the government's (the state, local public bodies, etc.) credits are truly low-risk as stipulated in the Basel Accord. According to the Basel Accord, claims on domestic public-sector entities and on the government carry a low risk weight of 0%, so in an environment where it was difficult to allocate rising deposits towards corporate lending, there was no choice but to increase the distribution of loans through investment securities such as government bonds (leading to a decrease in the loan-to-deposit ratio as mentioned earlier) and lend more money to local public bodies.

However, Japan's debt-to-GDP ratio has reached 232.4% of the international average (Ministry of Finance [2016]) and is alarmingly high as compared to the other OECD countries.

Although the credit deterioration (rise in interest rates) of government bonds and the drop in government bond prices that come hand-in-hand with financial deterioration have not surfaced as far as the current interest rates are concerned, in the event that government bonds lose value and Japan faces the risks associated with local public body borrowing, there is no doubt that interest rates will be heavily affected.

4. Fiscal Demands and Risks Associated with Maintenance and Renewal of Social Capital

It is expected that the aging of public facilities and infrastructure will lead to heavy funds being required for the maintenance and renewal of social capital. An appropriate response will require tackling various issues including financial constraints, the development of financial methods, and so on (Nemoto [2011b]).

One instance of an estimation being carried out of the country's total replacement demand is a report published by Toyo University Professor Yuji Nemoto, a member of the PFI Promotion Committee, Cabinet Office of the Japanese Government, as material for the conference held on April 19th, 2010 titled, "The Issue of Shortage of Financial Resources for Renewal Investment Due to Aging Social Capital and a Proposal for the Utilization of PFI/PPPs" (Nemoto [2010b]). According to Nemoto [2010b], "Given the current stock of public facilities (i.e. public buildings, such as schools, hospitals, public housing, government office buildings, community centers, etc.), roads, bridges, waterworks, and sewerage, the total estimated cost of their renewal in 50 years (15 years for road pavement) is ¥337 trillion, or ¥8.1 trillion per year," indicating the significantly large funds required for the state's aging social facilities and infrastructure in the future.

Progressive municipal authorities such as Hadano in Kanagawa Prefecture, Narashima in Chiba Prefecture, and Saitama have published white papers on public facilities, and under plans such as the "Public Facilities Relocation Plan" are being watched closely as they take long-term measures to directly address the issue of aging public facilities and the risk of future burdens.

At the national level, the Cabinet Secretariat formulated the "Basic Plan Against Aging Infrastructure" in November 2013, which was followed by a call by the Ministry of Internal Affairs and Communications in April 2014, with the aim of spurring action amongst local public bodies, for them to lay down a "Comprehensive Plan for the Management of Public Facilities, etc." This demand was not limited to public facilities but extended to all kinds of social capital under the management of local public bodies, including roads, bridges, water and sewage facilities, and appealed for them to take into account long-term trends in the population and finances. Nearly all local municipalities responded (although mostly not to the degree of awareness and planning found in the progressive municipalities mentioned earlier) by recognizing the present state of aging infrastructure and public facilities and the need for relevant long-term policies, and are making necessary efforts towards the realization such policies by implementing facility management (FM) measures such as the reorganization and desegregation of public facilities (Note 2), the reduction of costs through preventive maintenance, and so on.

As can be deduced from the above, regional financial institutions will be depended on to finance local public bodies for the enactment of their respective "Comprehensive Plan for the Management of Public Facilities, etc." Considering the fact that Japan is currently in a difficult financial situation as discussed earlier, regional financial institutions need to take an approach that focuses on the regulation of the public sector. In other words, they need to inspect, assess, and offer advice where necessary from the perspective of feasibility of finances regarding higher-level discussions previously only carried out within conventional local public bodies, such as those concerning the suppression fiscal demands for addressing the aging of public facilities and the utilization of PFI/PPPs as a means for increasing efficiency.

5. The Need to Confront Regional Issues

So far, in this section, we have laid out the issues faced by regional financial institutions, which can be divided into two categories: fund management issues relating to the gap between their loans and deposits (Subsection 1), and those pertaining to the state of credit issued to local public bodies as investment (Subsections 2, 3, 4). We have also seen that there is a significant financial problem as far as the latter is concerned.

This can be linked back to the report published after the end of Action Program II, "Evaluation of Efforts in Community-based Finance and a Future Course of Action - Accumulation of Regional Information for a Sustainable Business Model" (April 5, 2007), that contained guidelines for relationship banking measures. In particular, of the three actions that were equally desired from all financial institutions, namely: (1) increasing support of client companies in accordance with their life cycles, (2) thoroughly implementing funding methods suitable for SMEs, including financing techniques to assess business value, and (3) making sustainable contributions to regional economies through the accumulation of regional information, the third is relevant here. The proposed plan of action for its achievement, described in detail in Section I, included the "comprehensive revitalization of communities" (proactively extending support for devising a vision plan that makes full use of planning and investigative abilities, actively participating in efforts for public-private partnerships, expecting financial institutions to proactively participate as coordinators), "offering of various services for the stimulation of regional economies" (funding and supporting communities and businesses, etc.), and the "making of suitable commitments to regions, regulation of the public sector."

However, seeing the decline in loan-to-deposit ratios, increase in lending to the government (dependence on government and municipal bonds), and so on, it is hard to say that any of these roles are being fulfilled. It is thus necessary to develop a business model that will put into action the three points desired by the Financial Services Agency [2007] ("Comprehensive revitalization of communities", "Offering of various services for the revitalization of regional economies", and "Making of suitable commitments to regions, regulation of the public sector") to succeed in "making sustainable contributions to regional economies through the accumulation of regional information", solve local issues, and manage regional financial institutions.

Ⅲ Visualization of the Point of Contact Between Regional Financial Institutions and their Respective Communities

In this section, we will visualize the point of contact between regional financial institutions and their respective communities to inform the discussion on a business model that balances between addressing local issues and managing regional financial institutions.

For this purpose, the PPP Triangle will be used, which is a theoretical concept developed at the Toyo University Research Center for Public/Private Partnership (Director: Yuji Nemoto, Professor, Faculty of Economics, Toyo University), where I assist as a research partner, to visualize the relationship between the government, the market, and the community, which are the three actors in a PPP. Subsection 1 will explain the concept, and in Subsections 2 onwards the PPP Triangle will be used to carry out visualization.

1. The PPP Triangle

The PPP Triangle was first published in a discussion paper by the PPP Research Director Yuji Nemoto, Professor at the Faculty of Economics, Toyo University, titled "A Study on the Relationship between the Public and Private Sectors in Public-Private Partnerships" (Nemoto [2010]), and has been considered an element of the framework of PPP research in his paper "Consideration of Frame of PPP Studies 2" (Nemoto [2012]). The concept behind the PPP Triangle will be explained below, based on Nemoto [2012].

(1) Defining the PPP Triangle

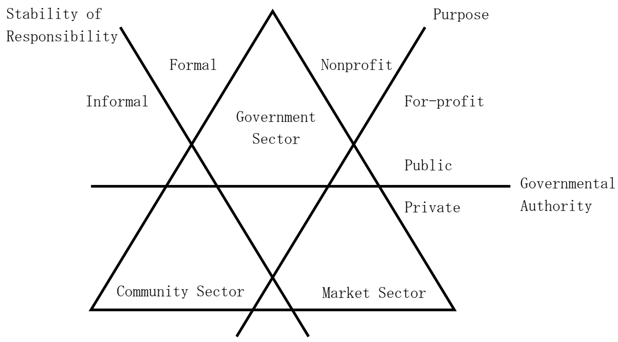
Nemoto [2012] says when defining the PPP Triangle, "One of the tools to determine who is responsible for offering public services and the like is the PPP Triangle. Victor Pestoff, a Swedish political scientist, designed a triangle that clearly described the interrelationships between volunteering within the region, private fee-based services, public assistance by the government, and so on, under the category of social welfare services; the PPP Triangle was developed by modifying and expanding this triangle to be applicable to the current state of Japan's PPPs."

On the benefits of using this triangle, he explains, "This will help one grasp how public services are being carried out in the real world" (Nemoto [2012]).

(2) Structure of the PPP Triangle

The PPP Triangle is depicted as shown in Figure 6.

Figure 6: The PPP Triangle



Source: Nemoto [2012]

The government sector, market sector, and community sector in Figure 6 represent the entities providing public services. The government sector includes all institutions with public power, such as the state, local municipalities, and so on. The market sector comprises of private enterprises. NPOs are also considered to be in the market sector if they carry out commercial activities. The community sector includes self-help within homes, cooperation with neighbours, and volunteering activities. Nonprofit activities by NPOs lie in this region.

The three dividing lines are helpful in understanding the nature of the three sectors, and Nemoto [2012] explains as below:

The horizontal line separates between entities with governmental authority for actions such as lawmaking and tax collection, called "public", and those without, called "private". The government sector has, of course, governmental authority and so is considered to be "public", while the market and community sectors are "private".

The line rising rightwards separates entities according to their purpose; namely, into "for-profit" and "nonprofit" entities. The market sector is for-profit, while the government and community sectors are nonprofit.

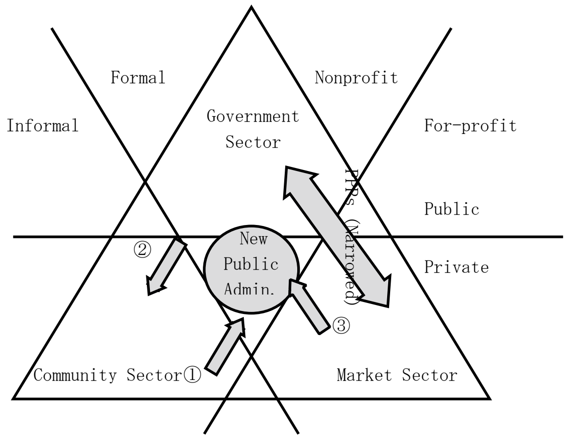
The line falling rightwards separates between formal and informal entities. Specifically, it divides them according to whether or not they are responsible for the steady supply of public services, and especially according to whether they are able to raise funds independently. The government and market sectors are "formal" entities that operate under legal obligations, responsible for continuously and consistently offering services. On the other hand, this is not the case with the community sector, making them "informal" entities. Taking an elderly neighbor along for shopping every now and then is a wonderful act of kindness, but on days they cannot be taken along, one cannot be sued for breach of promise. If one is indeed taken to court, the act must have been considered a paid service (considered an activity by the market sector in Figure 6), which completely changes the nature of the act.

Using these three lines, the three sectors can be classified as follows: the government sector having the characteristics "public, nonprofit, formal", the market sector being "private, for-profit, formal", and the community sector being "private, nonprofit, informal".

(3) Narrowly Defined PPPs

Contractual PPPs such as those under the PFI or the designated administrator system are represented by an arrow between the government and market sectors (Figure 7).

Figure 7: The PPP Triangle (2)



Source: Nemoto [2012]

(4) New Public Administration and a Mutual Aid Society

The inverted triangle in the center is characterized as being "private, nonprofit, and formal". According to Nemoto [2012], it is linked to the New Public Administration movement promoted by the government, and there are three kinds: one arises when the community sector carries out formal activities (such as participating in the PFI or as a designated administrator, indicated by ① in Figure 7), the other is when activities become informal (such as under the Adopt Program, indicated by ② in Figure 7), and the last is when the for-profit market sector maintains the principles of its activities but makes them non-profit (such as social enterprises, indicated by ③ in Figure 7).

With the change of government in 2012, the government has shifted from New Public Administration towards the making of a Mutual Aid Society, but the implications of the PPP Triangle can be thought to be unchanged.

2. Visualization of the Point of Contact between Regional Financial Institutions and their Communities

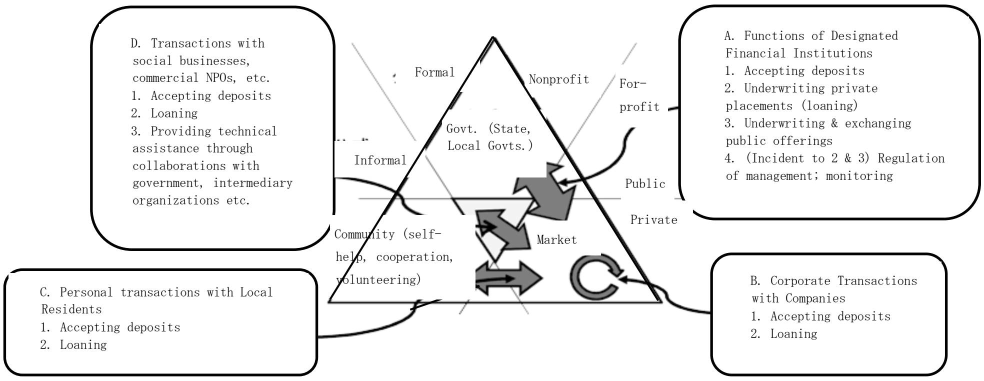
This section will present a visualization of the point of contact between regional financial institutions and their respective regions, based on the PPP Triangle described in Section 1 (Figure 8).

Financial institutions are in and of themselves corporations, and so they are members of the market sector. Their relationships and transactions with the government, community, and market sectors are represented by filled arrows.

Transactions with the government (state, local public bodies) are considered to be the function of designated financial institutions, and include accepting deposits, and underwriting and exchanging municipal bonds. Incident to the latter, they can also be considered to include addressing the financial problems of local municipalities, an increasingly serious issue in recent years, as well as administrative improvement strategies such as monitoring and the regulation of management. The point of contact is thought to be in financial public relations (A in Figure 8).

Transactions with local companies are carried out in the market sector, and include accepting deposits, issuing loans, and so on. The point of contact is thought to be in places of business (B in Figure 8).

Figure 8: Visualization of the Point of Contact Between Regional Financial Institutions and their Communities



Source: Based on Fujiki [2012]

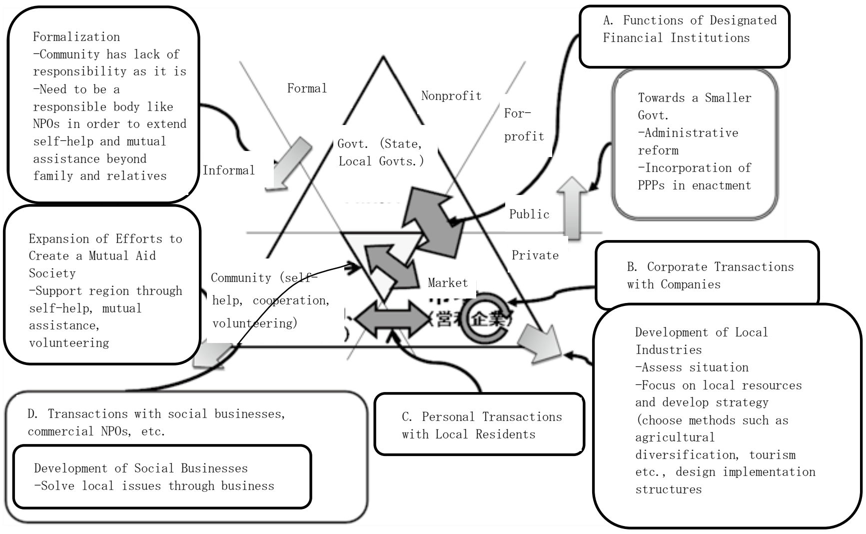
Transactions with the community include, as far as personal transactions with local residents are concerned, accepting deposits and extending loans. The point of contact is thought to be in those in charge of CSR at head offices, and in places of business (C in Figure 8).

Transactions with those pushing for a mutual aid society or for New Public Administration, such as social businesses and commercial NPOs, are considered to be transactions between the market and center segments in the figure (D in Figure 8). If they are operating as informal non-statutory bodies, then these will be transactions between the community and market sector. In this case, while deposits may be taken, issuing loans is a more difficult matter. If we take into account the fact that those promoting a mutual aid society or New Public Administration are generally venture companies with weak financial bases, then an additional function of financial institutions along with lending and taking deposits would be offering technical assistance through collaborations with the government or intermediary organizations.

Some regional financial institutions have think tanks, research centers, or consulting departments; in this case, they can carry out any of A, B, C, or D in Figure 8. Making use of the fact that transactions can be done even when there is no demand for them to be performed as a financial institution, and that they can carry out activities relatively freely without the responsibilities of a financial institution, they can do much more than just raise funds (making identification of local issues to the planning and enactment of their solutions.

Financial institutions are in a position where they tend to be called on to contribute to the region by participating in local projects, and so they often struggle in their response. However, adopting an approach informed by the relationship between financial transactions and the region may help them provide financial solutions to local issues more efficiently. Moreover, by addressing measures for projects aiming for regional regeneration and economic stimulation to reduce business profitability and risk during the planning stage before they are asked for financial advice, and making them more "bankable", options to maintain and expand projects and services with the necessary degree of publicness for the region, as social businesses where local companies and residents cooperate together, open up.

Figure 9: Regional Issues and the Direction of Efforts for their Resolution



Source: Based on Fujiki [2012]

3. Regional Issues and the Direction of Efforts for their Resolution

Figure 9 adds onto Figure 8 the local issues considered critical from the perspective of regional financial institutions and their regions, and the direction of efforts being taken for their resolution.

The problem faced by the government is that of financial deterioration, and this is being solved by working "towards a smaller government". To be specific, the incorporation of PPPs, such as PFIs, designated administrator systems, outsourcing, and so on, in the optimization of and enactment of what is generally called "administrative reform" is the point of focus. Regional financial institutions are hoped to carry out surveys required for the incorporation of these PPPs, and to extend financial support once a PPP is established.

The market faces issues related to the local industry, such as its development. Since implementing support programs funded by taxes will become increasingly difficult due to worsening financial situations, regional financial institutions are expected to accurately assess and understand the current situation, and design promising approaches and implementation structures such as utilizing local resources for agricultural diversification, tourism, and renewable energy (solar, wind, geothermal, biomass, small hydro, etc.).

The problems the community faces relate to the promotion of a mutual aid society, and the development and such of social businesses that aim to solve the region's issues through business rather than taxes. Due to the government's declining financial situation and the increasing difficulty of using taxes to fund countermeasures, there is a widespread need to instead make use of cooperation with local residents, volunteering, self-help, and mutual assistance. In the same way, the community is also expected to solve their issues using business, such as social business. To increase the number of those leading the creation of a mutual society, including social businesses, the socialization of self-help and mutual assistance, and the formalization of those leaders in order to assign them responsibility (an example of which would be incorporation) are challenges to be overcome. Regional financial institutions are expected to provide technical assistance for industrialization as well as financial assistance.

The actions listed above to be taken by regional financial institutions are all within the limits of the business activities being carried out at the point of contact with their region, as explained in Subsection 2, and are thus entirely possible to implement.

Ⅳ A Business Model to Manage Both Local Issues and Regional Financial Institutions

As a conclusion to this paper, this section will propose a business model that balances between solving local issues and managing financial institutions.

1. Application of Business Revitalization Know-How to the Public Sector

As we have seen in Section 1, regional financial institutions have gone through large changes in their environment since the collapse of the bubble economy, resulting from the promotion of relationship banking and the promotion of community-based finance after Action Program II by the Financial Services Agency. These called for them to adopt an

Figure 10: Classification of PPPs by the Toyo University Research Center for Public/Private Partnership

	Public Service PPPs	Public Asset Utilization PPPs	Regulatory/Guidance PPPs
Target Businesses	Public Services	Private Services	Private Service
Place of Activity	Principally public land, public building	Principally public land, public building	Principally private land, private buildings
Usual Form	PFI, designated administrator system, market tests, privatization etc. Includes BOT、BTO、DB etc.	Utilization of public land and public buildings	Invitation of enterprises, urban development, revival of shopping streets, promotion of tourism, promotion of local industries etc. Special Zones for Structural Reform, Regional Regeneration, Urban Regeneration
Related Laws and Regulations	PFI Act Local Autonomy Law, Public Service Reform Act	National Government Asset Act, Local Autonomy Law	Special Zones for Structural Reform Law, Three Acts of City Planning, Local Revitalization Act, Act on Special Measures concerning Urban Reconstruction.

Source: Fujiki [2011a]

approach different from that of major banks and make various efforts for strengthening its functions, revitalizing businesses, and stimulate regional economies, so that the issue of nonperforming loans will also resolve itself at the same time.

Although this paper did not go into the details of regional regeneration and the role of regional institutions in order to instead discuss the broader picture, it can be said that through the promotion of relationship banking, regional financial institutions are also gaining expertise on the revitalization of SMEs; in other words, business revitalization. The application of this knowledge to the public sector, and the proposal of and the extending of various kinds of financial support for management reforms to be carried out in local public bodies facing difficult financial situations can be thought of as a business model.

The Toyo University Research Center for Public/Private Partnership divides PPPs into three kinds: Public Service PPPs, Public Asset Utilization PPPs, and Regulatory/Guiding PPPs. This classification, shown in Figure 10, is carried out based on (1) whether the activity in question is a public service or a private service, and (2) whether that activity is to be carried in a publicly or privately owned space (Nemoto [2011a]). These three kinds of PPPs will be discussed in contrast to the general point of view adopted while carrying out the business revitalization of private enterprises. When a private business slumps, the issue is generally addressed by focusing on three things: securing profits by reducing costs, asset restructuring (selling, etc.), and increasing sales. In the case of local municipalities, these become: (A) securing funds from the redemption of local bonds by reducing costs, (B) improving financial structure, securing funds for management reform, and (C) increasing tax revenues (Figure 11).

Public Service PPPs can be analysed with regards to (A). Market testing, PFI, designated administrator systems, and so on come to mind. Public Asset Utilization PPPs, on the other hand, can be analysed with regards to (B). Here, PPPs for the efficient use of public real estate obtained from PRE strategies, relocation of public facilities, and so on come to mind. Lastly, Regulatory/Guiding PPPs can be linked with (C). Maintaining and improving the region’s charm, carrying out measures under industry-academia-government collaborations alongside management reforms already being enacted in each local company is sure to contribute even further to regional economic stimulation.

The implications of these for regional financial institutions are that whichever of the cases (A), (B), or (C) it is of the government, a business opportunity lies in the promotion of PPP projects. In the case of (A), they will be Public Service PPPs, and there will be opportunities to invest in PFI/PPP businesses. In addition to providing financial advice to the government (or local municipality), the contractee in PFI/PPP commercialization during the initial discussion stages, there will also be opportunities to similarly offer financial advice to bidding private companies. In the case of (B), they will be Public Asset Utilization PPPs, and regional financial institutions can assist using their know-how of real estate projects. In PFI/PPP commercialization, the project may have aspects related to both (A) and (B).

On the other hand, PPPs are Regulatory/Guidance when it comes to (C), and so partnerships with not just other financial organizations but also with local public bodies or public organizations that follow them (such as the Chamber of Commerce and Industry) are necessary. Projects arising from formulating an outline and plan of action through the development of project design and the sharing of vision through workshops involving local residents and concerned parties may or may not turn out to be investment opportunities. Therefore, instead of having departments like sales departments, that aim to achieve a certain amount of investment or profit in the short-term, handle things, it would be productive for departments capable of developing a long-term vision for the region, such as the planning departments and think tanks in financial institutions, to work together and become involved from the planning stage.

Figure 11: Ways of looking at PPP Utilization

Central Focuses in Case of Businesses	Rephrasing in Case of Government	Methods of Administrative Reform, Type and Method of PPP	Examples
1. Securing profits by reducing costs	(A) Securing funds from the redemption of local bonds by reducing costs	Use of market testing, PFI, designated administrator system, outsourcing →Public Service PPP	PFI prisons, incorporation of designated administrator systems for maintenance and repair of every town’s roads (26% cut at Kiyosato, Hokkaido), establishment of outsourcing company for city affairs (Takahama, Aichi)
2. Asset restructuring (selling, etc.)	(B) Improving financial structure, securing funds for management reform	PRE strategies (writing white papers on public facilities, relocation of public facilities) →Public Asset Utilization PPP	Invitation of call centers by Yamato Transport (Minamiuonuma, Niigata and Nabari, Mie), privatization of public hot springs, reconstruction of Youtokugakusha in Nara
3. Increasing sales	(C) Increasing tax revenues	Maintenance and improvement of region’s charm, regional revitalization →Regulatory/Guidance PPP	Making of Showa no Machi in Bungotakada, Oita

Source: Fujiki [2012]

2. Employment of Various Financial Instruments

When it comes to methods of financial support, it is entirely possible to extend beyond conventional loans and employ a diverse set of financial technologies.

Loaning is a method of financing, found in the upper right portion of the balance sheet (liabilities). It can also be considered support for capital, found in the lower right side (investments), and for the area between capital and liabilities (mezzanine). Investments can be made through the methods directly carried out by financial institutions as well as through methods using securities subsidiaries and funds. Moreover, by making use of “investment-oriented crowdfunding” institutionalized under the revision of the Financial Instruments and Exchange Act of 2014, financial institutions may extend support in conjunction with depositors (details in 5-3).

Additionally, asset-based lending and liquidation of real estate through sale and leaseback transactions and such are becoming increasingly common funding methods that utilize assets, which are found in the left side of the balance sheet.

In light of the grim financial situation discussed in this paper, focusing on assets held by local public bodies and securing their use as public services while at the same time using them a means for funding, such as by the liquidation of real estate through sale and leaseback transactions, will no doubt become a topic of discussion.

Even the use of ABL can be extended beyond simply between financial institutions and existing clients and can be used as a means of supporting regional economic stimulation projects (agricultural diversification, etc.), which can be thought of as new ventures, to expand working capital support for achieving business expansion.

3. Support by Cooperation and Collaboration with Depositors through Crowdfunding

Although regional financial institutions have been the main topic of discussion in this paper, there is a trend among local residents to collect "money given out of goodwill" and establish community development financial institutions and funds, and make investments using private placement bonds and silent partnerships. These are being carried out for the purposes of regional revitalization and the support of enterprises (communities, businesses, etc.) who find it difficult to receive loans from existing financial institutions. There is has also been a rise in recent years of services using the Internet to act as intermediaries for silent partnerships (such as "Securite" by Music Securities, Inc.) and in matching services for donations (such as Readyfor).

Although services such as those mentioned above are being employed in existing financial techniques such as silent partnerships, crowdfunding was declared by the Second Abe Administration as one of the ways to implement their growth strategy. The document outlining this growth strategy "Japan Revitalization Strategy－Japan is Back－" (Cabinet Decision on June 14th, 2013) states: "Conduct a study on and identify institutional reforms which need to be made with regard to a mechanism that will connect new and growing companies, including venture businesses, and investors on an Internet website, and raise small amounts of funds from many investors (crowdfunding) by the end of this year." (p.12) The government took this opportunity to make quick progress towards environmental improvement. The next year, on May 23rd, 2014, the "Amendment of Financial Instruments and Exchange Act, etc." (hereafter referred to as "FIEA Amendment") was approved and enacted at a plenary session of the House of Councillors (the House of Representatives approved it on May 13th). In conjunction with the actions being taken by the Diet, at the government side, the Chief Cabinet Secretary, Regional Revitalization Bureau, Cabinet Secretariat (currently the Office for Promotion of Regional Revitalization, Cabinet Office) established the Furusato Investment Liaison (Cabinet Office [2014]), after which crowdfunding creators, relevant government agencies, local municipalities, regional financial institutions, and the securities industry all gathered to cooperate, and began to formulate a "Furusato (Hometown) Investment" project in which they will collaborate and use crowdfunding to support the stimulation of regional economies.

Crowdfunding is generally classified into three types based on the type of return on investment: donation-based, reward-based, and debt-based crowdfunding. In donation-based crowdfunding, no returns are given to the contributor (such as raising money for donation through websites, sending newsletters to donators, etc.), while in reward-based crowdfunding returns other than money are given (such as developing a product using an advance payment by a contributor, and sending back the completed product). In debt-based crowdfunding money is returned to the contributor (such as investing in silent partnerships between investors and operators through operating companies).

In the FIEA Amendment, there was an easing of restrictions on debt-based crowdfunding; if they are utilized alongside donation-based and reward-based crowdfunding, it will become possible for regional financial institutions to use previously unattainable "money given out of goodwill" to support projects for regional regeneration.

In the areas surrounding the Kansai region where this university is located, there have been instances of the "Furusato Investment" being preceded by in its philosophy since before the institutionalization of crowdfunding, such as the Nishiawakura Shared Forest Fund (having chosen not to merge during the great Heisei mergers, this was for raising funds required for initial investments such as the purchase of high-performance forestry machinery in order to carry out appropriate and efficient forestry management; this 2009 fund was the first case of forest and forestry support in the country) and the Kurokabe Fund (a 2011 fund established by The Shiga Bank that solicited investments from individuals). It is hoped that in present times regional financial institutions collaborate with local municipalities and local enterprises to identify issues, propose and materialize projects, and achieve concrete results.

When that happens, along with the fact that suitable returns will be gained through invested funds, the spreading of the service industry (from agriculture, forestry, fisheries, commerce, and industry to tourism) following the Furusato Investment into the creation of new markets will bring about new demands for investment. As for the issue of a shrinking population faced by many areas, it is hoped that the young generation bearing the future of their community receive enough income to live without worrying about marriage and childbirth, and revitalize (or rebuild) the industrial base of their area so that their children may be hopeful of and proud of their hometown.

Conclusion

Expectations are increasing on regional financial institutions and financial institutions for achieving the regeneration and stimulation of regional economies. As the business environment surrounding regional financial situations is steadily becoming harsher, it is hoped that this paper plays a role not limited to the forming of financial institutions' business logic, but one that extends to the promotion of regional revitalization through collaborations between the administration and the citizens, who are also depositors from the point of view of financial institutions.

Notes

(1) According to various documents and hearings of related organizations, there is a difference in loan-to-deposit ratios when financial institutions are divided into different types. While there is the opinion that city banks should be excluded, in large cities city banks take on the role of regional financial institutions as well, and there are cases of this being intensified through merges (for example, The Kobe Bank merged to become Taiyo Kobe Bank, and merged further to become Mitsui Taiyo Kobe Bank, renamed The Sakura Bank, and is now Sumimoto Mitsui Banking Corporation), so it can be said that there is also a need for city banks to be aware of their relationship with their region, and thus they need to be examined carefully as well.

(2) To mention a leading example of this, the "Hadano Public Facility Relocation Plan" by Hadano (in Kanagawa), the planning of which I was involved in as a member of the committee, was a plan immediately worked on after the publishing of the "Hadano Public Facility White Paper" provided an understanding of the present state of and issues related to public facilities, and aimed to reduce public facilities by around 40% over the span of 40 years. Actions taken after its proposal were praised for bringing about fiscal effects (an effect of ¥1.06 billion in the 5 years of the first basic plan), and the plan won the grand prize at the 16th Japan Association for Planning and Public Management Planning Awards in 2016.

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