Changing Choices in Individual Financial Assets

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In advance of the re-introduction of the so-called "Pay-off" system (the measure capping the guaranteed amount of compensation on deposits to ¥10 million) planned for April 2001, much attention is being paid to how individuals' choice of financial assets will change.

This report aims to examine recent trends in personal financial assets and to consider what the future holds in store.

1. Recent Changes in the Personal Savings Market

1) Halt in Flow of Funds to Postal Time Deposit Savings Accounts

One of the major recent changes in the individual savings market has been the halt in the inflow of funds to the "Teiki" time postal-savings deposits (generally referred to as "New Teiki"), that had been growing steadily since January 1997. Net growth of ¥1,433.6 billion in atime savings during the month of December 1998 was followed by a net decline in the 3 months from January to March 1999 as ¥521.6 billion flowed out of these accounts.

The amendments on January 4th 1999 made to the Postal Savings Regulations Article 100-2, relating to funds invested in atime savings would have much to do with this. Essentially this abolished the previous system whereby investments were separated into small lots of ¥1,000 each, and allowed deposits of any amount over ¥1,000 in multiples of ¥1,000. For example, a deposit of ¥6,000 would, under the previous system, have been treated as 6 lots of ¥1,000 each, whereas now it is a single ¥6,000 deposit.

Figure 1 Amendments to Postal Office Savings Regulations

<Deposit Amounts>

Only amounts of the following 8 types can be deposited (Post Office Savings Regulations, Article 100-2):

- ¥1,000
- ¥5,000
- ¥10,000
- ¥50,000
- ¥100,000
- ¥500,000
- ¥1 million
- ¥3 million

-- EXAMPLE –

- A deposit of ¥6,000 would equal six separate ¥1,000 deposits

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<Deposit Amounts>

- Can be any amount of ¥1,000 or over, in denominations of ¥1,000 (Revised Postal Office Savings Regualtions Art.100-2)

-- EXAMPLE --

- A ¥6,000 deposit is a single ¥6,000 deposit.

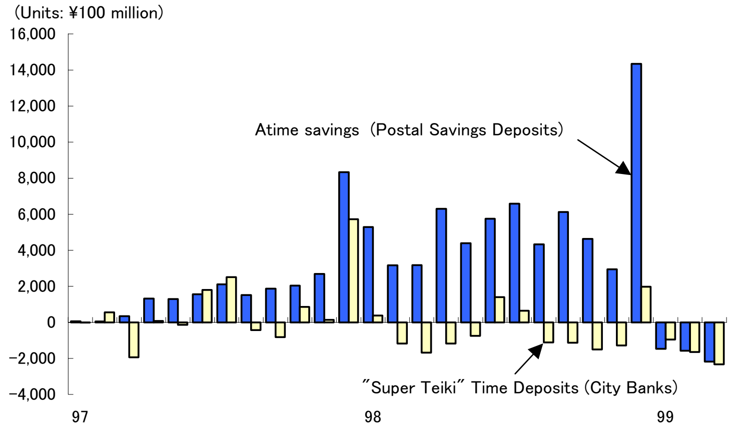
(Source: Ministry of Posts and Telecommunications)

As a result, the loophole in the regulations that allowed an annual yield of 1.2% p.a. on 1-month time deposits (with an advertised rate of 0.15%, as at end December 1998) has been closed, and now the actual yield is the same as the advertised rate, i.e. an actual return on deposits of only 0.15%. With rates of the comparable “Super Teiki” 1-month time deposit accounts of the city banks standing at 0.10% (as at end March 1999), this revision to Post Office Savings law moves their interest rates closer to those of private institutions.

The influx of funds into postal savings time deposits was originally sparked off by various money magazines introducing their readers to their benefits at a time when investor anxiety over the general financial situation in Japan was evidenced by a preference for safer assets.

In fact, the ¥521.6 billion outflow of funds from the postal savings time deposits after they had lost their interest rate advantage (the period Jan. to Mar. 1999) was greater than the ¥491.1 billion leaving the comparable Super Teiki’s operated by the city banks. Roughly the same amount of money flowed out of postal savings and city bank accounts in February and March. This change in the flow of funds despite there being no change in the safety of postal savings indicates that individuals are looking for more choice in financial assets.

Figure 2 The Post Office “Teiki” and City Bank “Super Teiki” Deposit Accounts



Source: Nomura Research Institute

2) Rise in Non-Resident Yen Deposits and Foreign Currency Deposits

With the revised Foreign Exchange Law coming into effect in April 1998, and the Financial System Reform Law coming into force in December of that year, much attention has been paid to the impact the Japanese Big Bang will have on the individual savings market. Up to now however the clever use of postal savings time deposits has tended to obscure what is happening in the market. With this no longer the case the true state of the personal savings market should be easier to identify.

The first signs have come in the increase in Yen deposits held by non-residents and foreign currency denominated deposits. Outstanding balances in Yen held by non-residents and of foreign currency deposits at city banks rose at all levels between the end of March 1998 and the end of September. Fastest growth occurred in deposits of between ¥10 m. and ¥100m., with a total increase of ¥99.3 billion, exceeding the growth in the “under ¥3 million” group which tends to be individuals making initial trial investments.

In contrast to the strong net increases in ¥3m. - ¥10m. deposits, money has been moving out of the large demand and time deposit accounts of ¥100m. or over. While the proportion of financial assets held by individuals in the form of cash or deposit accounts rose from March’s 58.6% to 59.5% by end September 1998, and on the whole the preference for low-risk Yen-denominated deposits is still pronounced, a recent trend towards foreign currency etc. high-risk savings products is perhaps a sign of changing times.

Table 1 Individual Deposits at City Banks (grouped according to amount)

	Demand Deposits			Time and Saving Deposits			Non-resident Yen Deposits, Foreign Currency Deposits		
	end March	end Sept.	(net increase)	end March	end Sept.	(net increase)	end March	end Sept.	(net increase)
under \3m.	168,786	169,350	564	259,319	258,243	-1,076	1,002	1,314	312
\3m.--> under \10m.	96,363	101,072	4,709	157,539	158,450	911	1,077	1,425	348
\10m. --> under \100m.	74,447	73,252	-1,195	259,182	267,089	7,907	1,766	2,759	993
\100m. --> under \300m	5,583	5,047	-536	30,305	29,589	-716	609	761	152
\300m. and over	3,049	2,942	-107	14,270	14,142	-128	1,021	1,107	86
TOTAL	348,228	351,663	3,435	720,615	727,513	6,898	5,475	7,366	1,891

(Note) 1. 1998 figures
2. Units: \100m.
(Source: compiled by NRI based on Bank of Japan supplied figures)

2. Future Outlook

In predicting how far the current preference for yen-denominated deposits with their low-risk / low-returns will be replaced by investment-type products, the most important factors are undoubtedly the "Payoff" compensation cap to be re-introduced in April 2001, and the problems to be caused by the large numbers of fixed-amount deposits falling due between FY2000 and FY2001. Below I will examine each of these points in turn.

1) Re-Introduction of the Payoffs

With the re-introduction of the compensation cap (the "payoff system" that will limit the guaranteed return of principal to ¥10 million) in April 2000 just around the corner, it is said that savers will be splitting their investments into small accounts of under ¥10 million.

As far as individual demand deposits held at city banks are concerned, between end March and end Sept. 1998 there has been a net rise of ¥527.3 bn. in small deposits of less than ¥10 million , but a ¥64.3 bn. net decline in larger deposits of over ¥100 m. Funds have been flowing into the ¥3 million - ¥10 million band for both demand and time deposits, ¥470.9 bn. and ¥91.1 bn. respectively, which seems to indicate that people are taking into consideration the ¥10 million insurance ceiling.

These statistics include the maximum guaranteed deposit amount of ¥10 m. in the "¥10 million - ¥100 million" section, therefore it is highly likely that savers who are influenced in their investment decisions by the Payoff ceiling are in fact more numerous than the figures for "under ¥3 million" or "¥3 million - ¥10 million" bands would suggest.

The Financial Supervisory Agency report entitled "The Current Status Regarding ¥10 million Deposits held by Deposit-Taking Financial Institutions in Japan," [1] deals with the splitting up of deposits into many small accounts. According to this report, out of the total number of accounts held by both personal and corporate customers at the end of March 1998, 99.4% were accounts holding under ¥10 million, leaving a mere 0.6% of accounts holding over ¥10 million. Taking amounts deposited, 50.6% of funds were held in under ¥10 million accounts, while 49.4% were in accounts of over ¥10 million.

In addition, the ¥374 trillion of insured deposits held by both corporates and individuals represented 65% of total deposits. This is 1.2% higher than the 63.8% figure that the Bank of Japan announced at the end of September 1994 for insured deposits. Nevertheless, when compared to the 81.3% of the U.S. this figure is still very low.

Moreover, if we apply the ratio of individually-held deposits as appears in the Total Amounts of Deposits by Depositor[2] (month-end) to these figures, the amount of non-insured deposits held by individuals amounts to ¥118.8 trillion.

1 "Savers Respond to the ¥10 million Deposit Account Cap", Nikkin (Mar. 12th 1999, page 1)
2 "Amounts of Deposits by Depositor," Bank of Japan," Financial and Economic Statistics Monthly

Table 2 Deposits of Under / Over ¥10 million held by Financial Institutions (end March 1998)

	No. of Accounts				Balance of Deposits			
	under \10m.		over \10m.		under \10m.		over \10m.	
City banks	38,340	(99.2)	292	(0.8)	751,506	(38.7)	1,189,505	(61.3)
Long-term Credit Banks	254	(98.5)	3	(1.5)	3,521	(5.5)	60,007	(94.5)
Trust Banks	1,483	(98.4)	24	(1.6)	51,198	(28.9)	126,002	(71.1)
Regional Banks	41,934	(99.4)	247	(0.6)	905,189	(53.8)	777,531	(46.2)
Regional Banks II	11,191	(99.2)	93	(0.8)	335,451	(55.3)	270,807	(44.7)
Shinkin Banks	17,611	(99.2)	135	(0.8)	667,527	(67.8)	316,465	(32.2)
Credit Associations	2,933	(99.0)	30	(1.0)	117,325	(62.0)	71,794	(38.0)
Labour Credit Assocs.	17,102	(99.9)	9	(0.1)	74,108	(72.2)	28,521	(27.8)
TOTAL	130,852	(99.4)	837	(0.6)	2,905,837	(50.6)	2,840,643	(49.4)

	Deposits covered by Deposit Insurance		Deposits not covered by Deposit Insurance			
					(a)	(b)
City banks	1,043,906	(53.8)	897,105	(46.2)	(55.4)	496,548
Long-term Credit Banks	7,411	(11.7)	56,117	(88.3)	(8.7)	4,871
Trust Banks	75,318	(42.5)	101,882	(57.5)	(43.9)	44,685
Regional Banks	1,152,669	(68.5)	530,051	(31.5)	(65.0)	344,639
Regional Banks II	428,711	(70.7)	177,547	(29.3)	(66.8)	118,672
Shinkin Banks	803,377	(81.6)	180,615	(18.4)	(74.7)	134,937
Credit Associations	147,865	(78.2)	41,254	(21.8)	(60.0)	24,752
Labour Credit Assocs.	83,568	(81.4)	19,061	(18.6)	(100.0)	19,061
TOTAL	3,742,917	(65.1)	2,003,563	(34.9)		1,188,166

(NOTES) 1. Covers corporations and Individuals
2. Units: Accounts = 10,000, Balances = \100m. Parentheses indicates share
3. Includes foreign currency deposits, public funds and deposits by financial institutions
4. (a) is the proportion of total deposits held by individuals
5. (b) is individual non-insured deposits
6. Assuming Labour Credit Assoc. deposits are 100% held by individuals, and Labour Credit Assoc. deposits are 60% held b
(Source: Compiled by NRI based on figures provided by the FSA and Bank of Japan)

Table 3 Insured Deposits – Comparison of U.S. and Japan

	Total Deposits	Insured Deposits	Coverage (%)
Japan (end Sept.'94)	4,669,715	2,977,673	63.8
U.S. (end Dec. '94)	3,179,579	2,585,509	81.3

(Note) 1. Japanese insured deposits equals the total of time and demand deposits
2. Insured deposits for the U.S. is an FDIC estimated figure
3. Insured deposits in Japan are on a non-consolidated basis
(Source: Bank of Japan)

2) Mass Maturing of Teigaku Savings

One problem regarding postal savings drawing much attention of late is the large numbers of Teigaku savings to fall due in the period from FY2000 to FY2001, representing the ¥106.5 trillion invested in Teigaku accounts from FY1990 until FY 1991. Out of these the outstanding balance as at end March (of principal amounts) was around ¥62.9 trillion[3], meaning some 60% are still outstanding. Furthermore, the exceptionally high interest rates on deposits made between September 1990 and July 1991 of 6.33% meant that in July 1991 alone ¥9.6 trillion of new funds were deposited.

3 "Policy statement of the Bureau Chief of the Ministry of Posts and Telecommunications, regarding the problem of many time deposits falling due in a short period, insurance coverage will not be changed" (Nikkei Kinyu Shimbun 28 July 1998 p.3)

Considering the extremely low interest rates at present, it would be difficult to imagine any serious decline in these balances from now on. If these individual investors do not withdraw their money before the 10-years maturity, then from FY2000 to FY2001 there will be a total of some ¥100 trillion to be paid back (including interest).

Table 4 Monthly Trends in Deposits / Payments on Teigaku Savings (FY1990-91)

FY	Deposit	of which new deposits	of which compound interest	Repayment	Yield (ref. only)	Maturity
1990 4	104,245	99,346	4,899	221,889		Apr. 2000
5	51,239	44,440	6,799	60,850	7.851	May
6	48,197	43,765	4,432	54,693	7.851	Jun
7	40,820	37,246	3,574	39,185	7.851	Jul.
8	31,076	26,388	4,688	31,163	8.648	Aug
9	32,673	27,768	4,905	30,885	8.648	Sep
10	59,580	54,868	4,713	60,681	8.648	Oct
11	80,901	74,880	6,021	90,604	8.648	Nov
12	80,268	76,257	4,012	66,166	8.648	Dec
1	56,873	53,828	3,044	40,685	8.648	Jan 2001
2	44,929	40,711	4,218	33,818	8.648	Feb
3	46,335	41,736	4,598	36,451	8.648	Mar
1991 4	68,624	64,024	4,599	39,338	8.648	Apr
5	48,043	41,074	6,969	26,703	8.648	May
6	40,247	36,140	4,107	24,186	8.648	Jun
7	99,781	96,306	3,475	50,314	8.061	Jul
8	23,319	19,041	4,279	13,346	8.061	Aug
9	23,378	18,338	5,040	13,967	8.061	Sep
10	33,560	28,263	5,298	15,382	8.061	Oct
11	51,685	43,334	8,351	19,229	7.204	Nov
12	41,468	35,361	6,107	21,153	7.204	Dec
1	31,379	27,789	3,590	14,776	6.386	Jan 2002
2	19,505	14,659	4,845	11,207	6.386	Feb
3	25,703	19,187	6,516	15,392	6.386	Mar
TOTAL	1,183,829	1,064,750	119,078	1,032,064		

Notes: 1. Units: ¥100 million, % Yield
2. The yield used is the simple (average) yield calculated by dividing the interest at maturity by the maturity term

Source: Compiled by NRI based on figures supplied by the Ministry of Posts and Telecommunications

In Conclusion

As we have seen, domestic credit fears are showing signs of easing and with the recent recovery in the securities markets the environment surrounding individual financial assets is stabilizing at long last. However into this will be thrown the c. ¥100 trillion of Teigaku Savings (including principal plus interest) maturing from FY2000, and the re-introduction of the deposit compensation cap in April 2001. In reaction to the latter individual investors will split up their funds into many small accounts of less than ¥10 million that are covered by deposit insurance. The amount of deposits held by individual investors that will not be covered by deposit insurance is according to my previous calculations around ¥119 trillion, giving a total ¥220 trillion in funds whose movement will be of major interest.

The ¥1200 trillion Japanese personal savings market is entering a 2 to 3 year period of dynamic change that will be closely watched.