

THE FISCAL INVESTMENT AND LOAN SYSTEM

Susumu Fukuda

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Mr. Fukuda is an official of the Japanese Ministry of Finance. He was a visiting scholar at the Center on Japanese Economy and Business during the 1988-89 academic year. The opinions expressed in this paper are the personal views of the author and do not represent the official views of the Ministry of Finance.

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I. Overview

1. Structure

The Fiscal Investment and Loan System (FILS), can be viewed in terms of fund collection and fund disbursement. The FILS collects funds from a variety of national institutions, taking advantage of the popular confidence in government-related financial institutions such as Postal Savings. These funds are then disbursed for investment and other activity in accordance with the objectives of national policy.

There are two principle categories of fund disbursement: direct credit allocation to various quasi-governmental agencies, which corresponds to the Fiscal Investment and Loan Program (FILP); and the subscription of government bonds.¹

2. Sources of Funds

There are four different sources of public funds in FILS: the funds of the Trust Fund Bureau (TFB);² the reserves of the Special Account for Postal Life Insurance and Postal Annuity; the funds of the Industrial Investment Special Account; and bonds and other borrowings guaranteed by the Japanese government.

3. Uses of Funds

These public funds are selectively allocated for the purpose of promoting public goals in coordination with other fiscal and monetary policies. Funds that are not used for the subscription of government bonds are directed towards the National Special Accounts, the Finance Corporations, the Public Corporations and the local government authorities. Plans for the use of these funds (strictly speaking,

¹Subscription of government bonds by the trust fund bureau has occurred every fiscal year since the issuance of public bonds began in 1965. However, it is especially since the very large-scale issuance of government bonds began in 1975 that the funds of the Trust Fund Bureau have played an important role in assuring their smooth absorption.

²The FILS assumed its present shape in 1953. The history of the Trust Fund Bureau, which is the core of the FILS, goes back much further, however, and can be traced to the early Meiji period (the 1870's).

those long-term plans which exceed five years)³ are decided every fiscal year.⁴ These plans comprise the official fiscal investment and loan program (FILP, known in Japanese as *zaiseitoyushi keikaku* or *zaito keikaku*, for short). The flow of FILS funds is shown in Chart 1 at the back of the text.

4. The Diet Deliberations

In this way, the FILP is intimately related to the General Account Budget in a complementary fashion; it determines the management and use of public funds which do not fall under the control of the General Account Budget. It is a vital part of the planning and execution of fiscal policy, and is often called "the second budget".⁵

The FILP program is approved by virtually the same procedures as the regular budget. Each of the FILP's four sources of funds separately undergoes Diet deliberations as a part of the total Special Account Budget.⁶

5. The Functions of the FILS

Generally speaking, fiscal policy serves three economic functions: income redistribution, resource allocation, and macroeconomic adjustment. The FILS is a tool of Japanese fiscal policy in all three respects. It brings together all the interest-

³At first, the FILP did not have to undergo Diet deliberations. However, a law was passed in 1973 which determined that the long-term plans (over 5 years) of the FILP would be subject to Diet approval. This was in line with the growing realization of the importance of FILP funds and that, in view of the importance resource distribution plays in public economic life, the appropriate and effective use of these funds would be served by greater public scrutiny.

⁴The Japanese fiscal year begins on the first of April and ends on March 31st of the next year.

⁵When it was launched in 1953, the scale of the FILP was around one-third that of the general account budget. Since 1970, however, it has grown relatively more important: its scale moved over 50% that of the general account budget during the 1970's, and more recently it has approached 60% (in 1987 the proportion was 57.5%; in 1988 it was 58.4%).

⁶As with the budget, by August 31 each Ministry must present to the Ministry of Finance a request for funds from the FILP for the next fiscal year. After receiving the appropriation requests, the Ministry of Finance conducts an examination from September through December of the FILP requests which parallels the examination of budgetary requests. Usually, the formal government proposal is completed by the end of December, presented to the Diet in late January and, if approved, enacted in April.

bearing funds under direct government control and distributes these funds to various sectors according to government plans. The FILS aims to contribute to the country's economic development by encouraging activity such as capital formation and acts as a mechanism for resource allocation. Furthermore, the FILS, along with the General Account Budget, is utilized as a tool of macroeconomic policy and often responds to current macroeconomic conditions.

6. Distinctions Between the FILS and the General Account Budget

Under the FILS, the government makes loans to various Special Accounts, government-affiliated agencies, public corporations, local governments, and other institutions under the legal requirement that their funds be utilized on a sound and profitable basis to meet public needs. This is because the program is funded from sources on which interest must be paid, such as the postal savings of the general public. In other words, the funds are allocated to revenue-producing projects where the beneficiary can be specifically identified. In contrast, General Account budget expenditures are financed by tax revenues. In less profitable areas, such as social overhead capital formation, however, funds in the FILS program can also be utilized in the form of grants or interest subsidies together with the General Account Budget.

II. Sources of Funds

As stated above, there are four public sources of funds for the FILS. Although each source has a different function, funds are administered as a single unit in accordance with the plan of the FILS.

1. Funds of the Trust Fund Bureau.

The funds of the Trust Fund Bureau make up more than 80% of the entire FILS, and occupy the central position in the FILS.

A. Deposits at the Trust Fund Bureau. Postal savings, and the surplus and reserve funds of the national special accounts, must, by law, be completely deposited into the accounts of the TFB fund. This is called "consolidated fund management", and it has the following merits: 1) A large scale and stable source of funds is ensured. By aiming to utilize these funds consistently with policy objectives, the funds are efficiently distributed to meet the needs of the public economic interest; 2) A timely and flexible use of funds which complements other fiscal and monetary policies is undertaken in response to changing economic conditions. 3) Redundant investment and the unnecessary expansion of administrative structure and personnel is avoided.

B. The Volume of Deposits. At the end of March 1988, the value of deposits at the TFB was 197.3 trillion yen. Of this, postal savings⁷ comprised 59.2% of the total, or 116.8 trillion yen, and pension funds comprised 31.9% of the total, or 62.9 trillion yen. Thus, postal savings and pension funds taken together are the source of more than 90% of TFB funds.

C. The Current Usage of the Funds. The TFB's funding targets are decided by law. Financing of the government is divided into loans towards the government (the special accounts) and the subscription of government bonds. In addition, government funding targets include loans and bond underwritings for finance corporations, public corporations, and other special corporations which carry out public works for the government. Lastly, local governments are financed.

The value of funds in the TFB at the end of March 1988 was 197.2 trillion yen. The principal categories of fund use were the subscription of government bonds (nearly 53.7 trillion yen, or 27.2%), loans toward the Housing Loan Corporation (29.4 trillion yen, or 14.9%), and the financing of local government (27.1 trillion yen, or 13.7%).

⁷The postal savings system was established in 1875.

D. Interest Rates

i. Trust Fund Deposit Interest Rates. The Trust Fund Bureau makes interest payments on the trust funds in pension funds and postal savings. The rates of interest at which the Bureau pays are called trust interest rates, or *yotaku kinri*. These trust interest rates vary depending on the term of the deposit.⁸

ii. Trust Fund Loan Interest Rates. The interest rate for loans to institutions which receive financing from the Trust Funds Bureau (the *yuzu* interest rate) are fixed at the same level as the interest rate on fixed time deposits of duration of 7 years or above; therefore, these deposits are the foundation of the trust fund. The funds of the Trust Fund Bureau, are in principle to be resupplied as loans without any interest rate spread or differential.⁹

iii. Term of Loans from the Trust Fund. The term of loans from the Trust Funds Bureau ranges up to a maximum of 35 years, and is determined by the needs and current business conditions of each borrowing institution.¹⁰

2. Special Account for Postal Life Insurance and Postal Annuity

A. Role of the Account. To make life insurance and pension plans

⁸The following are the trust loan interest rates at the start of the 1988 fiscal year.

<u>Term of Fixed Time Deposit</u>	<u>Annual Interest Rate</u>
1-3 Months	2.0%
3 months-1 year	3.5%
1-3 years	4.5%
3-5 years	4.7%
5-7 years	4.75%
7 years or more	4.8%

⁹The interest rate on loans from the FILP institutions to the general public differ from institution to institution, and from business to business. They also depend on the term of the loan. In some cases the interest rate is equal to the rate of finance from the funds of the Trust Fund Bureau, but it can also either exceed or fall below the trust fund rate.

¹⁰The term of the loan from the FILP institutions to the general public also differs from institution to institution, and from business to business. There are cases when the term exceeds the maximum borrowing term from the Trust Fund Bureau (35 years).

easily accessible, the government operates the postal life insurance and postal pension systems. The Special Account for Postal Life Insurance and Postal Annuity was created to make the management of income and expenditure from these two operations transparent. At the end of the fiscal year, the surplus created by the gap between revenue and expenditure are put into a reserve fund. This fund becomes a source of capital for future payment of insurance claims, pensions, and dividends. The stock of funds accumulates in the Special Account for Postal Life Insurance and Postal Annuity (*kanpo shikin*).

B. Use of Funds. The Special Account for Postal Life Insurance and Postal Annuity is a public fund but unlike other government funds it is treated as an exception to the principle of consolidated management of the government monies in the Trust Fund Bureau because of its particular history.¹¹ More specifically, the majority of the capital from the Postal Insurance and Annuity Account is included in the FILP program and is essentially used in the same manner as Trust Fund Bureau money. One portion of the account money, however, is invested in bank or corporate bonds, or is lent to insurance policy holders. This is known in Japan as *jishu unyo* (roughly translatable as "autonomously managed investment").

In FY1988, for example, out of 5.7 trillion yen in total capital, 4.4 trillion (77.4%) went into the Fiscal Investment and Loan Plan and the remaining 1.3 trillion (22.6%) was used for *jishu unyo*. The year-end balance of the Postal Life Insurance and Postal Annuity Special Account for FY1986 was 32.6 trillion yen: breaking down capital by type of investment, 12.1 trillion yen (37.1%) went to FILP funds for government-related institutions; 6.8 trillion yen (21.0%) went to local governments; and 8.3 trillion yen (25.5%) went to bank, corporate, and other bond

¹¹ The Postal Life Insurance Fund was founded in 1916, the Postal Annuity Fund in 1926. Since then, the government has managed the funds as discretionary operations/on a discretionary basis.

purchases.

3. Industrial Investment Special Account

A. Role of the Account. This special fund uses state funds to promote industrial development and trade. It comprises one part of the Fiscal Investment and Loan Program, and it corresponds to the fiscal investment portion of the program.¹²

There are several sources of capital for the special account: transfers from the general account; income from the issuance of foreign currency denominated bonds backed by this special account; principal and interest from repayment of loans; and dividends on profit from banks and special corporations in which the account makes loans. Recently, neither transfers from the General Account nor foreign currency bond issuance has occurred because of austere fiscal conditions. A 1985 revision of related laws sought to enhance the financing of the account, however. It required that a portion of profits from Japan Tobacco Inc. (JTI) and from Nippon Telegraph and Telephone Corporation (NTT) be remitted to the fund and that dividend income from these corporations should also serve as capital for the fund.

B. The Volume and Usage of Funds. The volume of capital at the end of FY1987 was 2.3 trillion yen. The major categories of investment were 1.0 trillion yen (43%) in capital for the Export-Import Bank of Japan, 0.3 trillion yen (11.6%) in capital for NTT, and 0.2 trillion yen (10.4%) for the Japan Development Bank.

4. Government Guaranteed Bonds and Borrowings

Government guaranteed bonds and borrowings are debt instruments issued by public enterprises, public organizations, and special corporations in which the government guarantees both principal and interest. The debt instruments are governed by a special law and the ceiling on their total volume is set in the budget

¹² The Industrial Investment Special Account was established in 1953. Economic reconstruction was one of the principal purposes of the account at that time.

for each fiscal year.

Unlike the Trust Fund Bureau, bonds and borrowings guaranteed by the government are not financed by government money itself. Rather public enterprises seeking funds to promote business activities procure capital from the private sector under the safety net of government guarantees. In view of this fact, as well as the deep relationship of the instruments with the country's fiscal situation, bonds and borrowings are treated as Fiscal Investment and Loan Program capital; they serve, in other words, as a supplement to government funds.¹³

5. Sources of Funds in FY1988

The total capital for the Fiscal Investment and Loan Program for 1988 is 33,114 billion yen, of which 29,614 billion is FILP resources and the remaining 3,500 billion is bond subscription.

The breakdown of capital resources is as follows: funds of the Trust Fund Bureau, 26,206.6 billion yen (79.1%); *kanpo shikin* 4,409.4 billion yen (13.3%); government-guaranteed bonds and borrowing, 2,406.8 billion yen (7.3%), of which loans account for 6.8 billion yen; and the Industrial Investment Special Account, 91.2 billion yen (0.3%). (See Table 1)

III. Uses of Funds

1. Targeted Institutions¹⁴

While FILS resources are used for the subscription of government bonds and

¹³ FILP organizations depend on the Fiscal Investment and Loan Programs to finance the major portion of their activities; however, each enterprise also has independent means of procuring capital. This is called *jiko shikin* (self-capitalization). In addition to loan repayments and profit raised on enterprise activities, *jiko shikin* also includes bond issuance and borrowings without government guarantees, issuance of foreign currency bonds, and the like. Of course, these sources of funding are outside the FILP plan.

¹⁴ While FILP targeted only 14 areas at its inception (FY 1953), the number had increased to 65 by 1987.

the fulfillment of FILP programs, the FILP program itself can be distinguished in the following way:

A. National Government. Special Accounts are used for operating public enterprises. Public enterprises that have the capability to repay principal and interest through cash income, user's fee, and the like are targeted.

B. Local Governments. Local governments that operate public facilities such as construction, transportation, gas, and waterways are funded through the issuance of local government bonds. The majority of these bonds are FILS subscriptions.

C. Public Policy Companies. These refer to enterprises that are profitable and that have a strong public nature, or to public enterprises established under special laws. These public enterprises rely mainly on FILP for financial resources, and payments on principle and interest are financed through its revenues.

D. Government Affiliated Financial Institutions. Although it is sometimes difficult for private financial institutions to smooth the supply of required capital, it is necessary from a policy perspective to guarantee a secure supply of capital. To supplement private finance, therefore, financial policy institutions were established. A majority of the necessary capital is supplied through the FILP program.

2. Classification

Table 2 illustrates the division of FILP's policy objectives into thirteen categories: housing; water supply, sewers and other environmental facilities; welfare; education; small and medium enterprises; agriculture, forestry, and fisheries; land conservation and disaster relief; roads; transportation and communication; regional development; industry and technology; trade and economic cooperation; and fund operation service.¹⁵

¹⁵Items 1-6 on the classification chart refer to areas that directly improve the nation's living standard. While only 10% of FILP funds were allocated to these areas in 1953, funding has since steadily increased, recently to 70%. In contrast, item 11, which refers to industrial and technological

3. FILP: FY1988

FILP's FY1988 budget of 29.614 trillion yen was allocated to the institutions listed in Table 3.

The FILP program has always been based on current economic conditions and societal needs.¹⁶ In FY1988, the following points were emphasized:

A. Housing and water supply, sewers and other environmental facilities for the purpose of domestic demand expansion and social capital formation.

B. The promotion of economic structural adjustment, small and medium enterprises, and private initiative in the social infrastructure.

C. Deregulation of financial resources for the promotion of capital recycling measures in order to actively contribute to international society.

IV. Future Prospects

Since FILS resources are public funds, its use is aimed at developing national welfare. During the postwar recovery period, FILP funds were directed mainly toward industrial policy. Since then, however, the emphasis has shifted toward standard of living and environmental concerns, such as water supply, sewers, housing, roads and other environmental facilities.

In this way, FILS played a large role during the postwar recovery and high growth period. Even now it is believed to play an important role in the economy, but as the interest rate gap between FILS and the market diminishes, as private financial institutions resources and instruments grow, and as previously public enterprises become privatized, the conditions that surround FILS will change

development, dropped dramatically from 30% to 3% during the same period. It is clear from this example that FILP funds reflect the economic needs of the time and that FILP funds have shifted from an emphasis on industrial to welfare development.

¹⁶Even at the stage of implementation, FILP program can be determined on the basis of the economic conditions following policy deliberation or on changes in the demand for capital resources from FILS.

dramatically. Consequently, the need to disperse FILS resources will be far less than before; to continue using FILS efficiently, and to assure allocation in areas of true need, it will be necessary in the future to rationally reappraise the qualitative and quantitative use of the FILS' system.

Table 1 Sources of FILP

	(billion yen)	
	FY1987	1988
Industrial Investment Special Account	144.3	91.2
Trust Fund Bureau Fund	24,595.8	26,206.6
Postal Savings	7,900.0	7,900.0
Employees' Pension and National Pensions	4,450.0	3,500.0
Others	12,245.8	14,806.6
Postal Life Insurance Fund	3,941.2	4,409.4
Government-Guaranteed Bonds and Borrowings	2,400.0	2,406.8
Total	31,081.3	33,114.0

Note: These figures include the subscription of government bonds by the Trust Fund Bureau Fund

Table 2 The Fiscal Investment and Loan Program
Classified by Function

	(billion yen)	
	FY1987	FY1988
Housing	6,328.2	6,921.5
Water supply, sewers and other environmental facilities	3,998.7	4,450.9
Welfare	622.7	661.8
Education	784.1	637.6
Small- and medium-sized enterprises	3,985.6	4,030.6
Agriculture, forestry and fisheries	907.8	979.4
Land conservation and disaster reconstruction	493.0	409.8
Roads	2,363.0	2,512.1
Transportation and communication	2,264.1	2,229.9
Development of under-developed regions	657.7	652.2
Industries and technology	630.9	687.2
Trade and economic cooperation	690.5	1,171.0
Fund operation service	3,350.0	4,270.0
Total	27,081.3	29,614.0

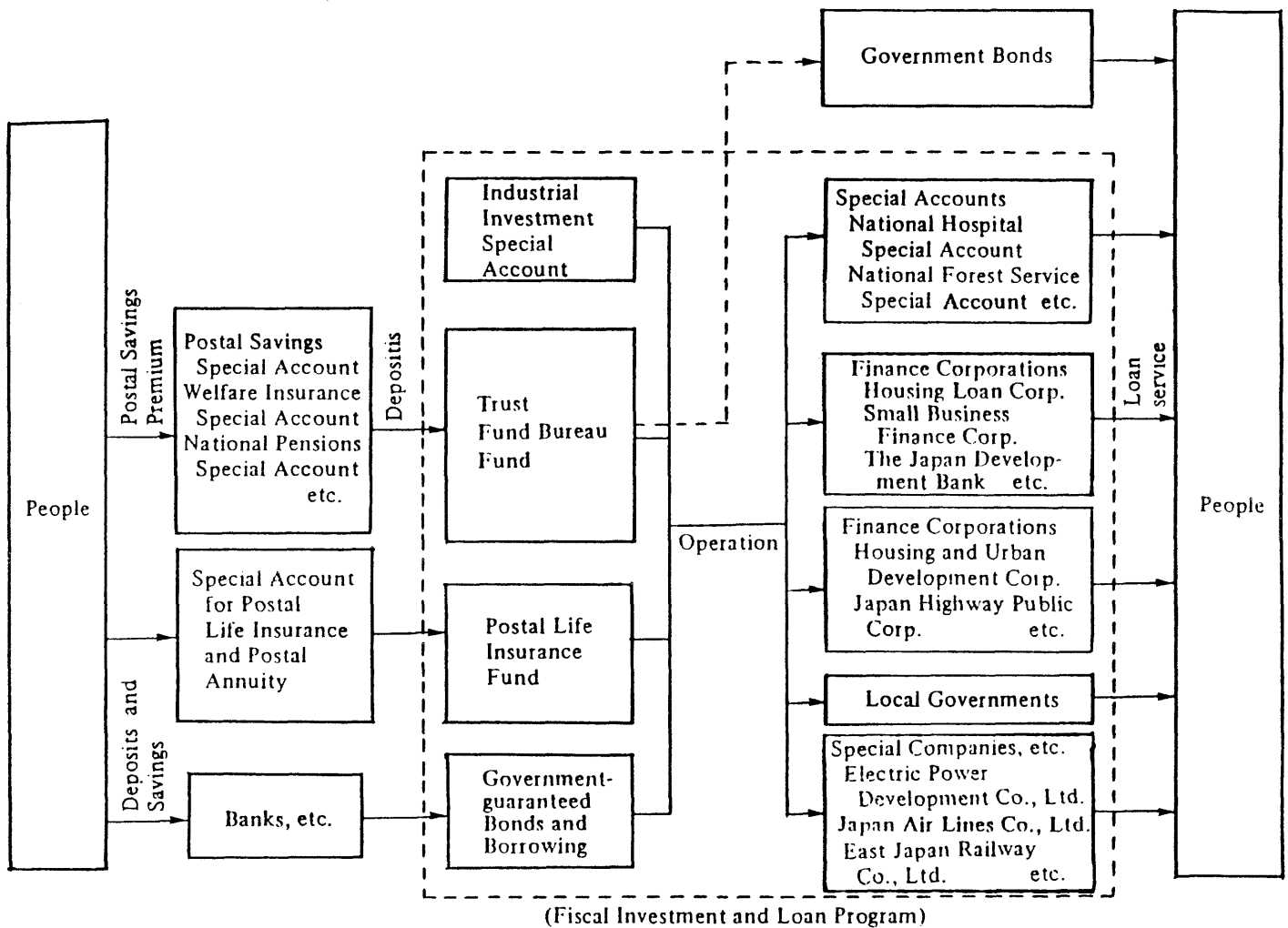
Table 3 Fiscal Investment and Loan Program (FY1988)

(billion yen)

Description	Industrial Investment Special Account	Fund of Trust Fund Bureau	Postal Life Insurance Fund	Government- guaranteed Bonds and Borrowings	Total
Special Accounts ¹	—	3,100.7	41.6	—	3,142.3
Government-Affiliated Agencies					
Housing Loan Corp.	—	4,667.1	40.0	—	4,707.1
People's Finance Corp.	—	1,643.8	240.0	—	1,883.8
Small Business Finance Corp.	4.7	1,345.6	432.7	20.0	1,803.0
Agriculture, Forestry and Fisheries Finance Corp.	—	439.0	33.0	—	472.0
Finance Corp. of Local Public Enterprise	1.0	—	—	1,190.0	1,191.0
The Japan Development Bank	—	853.2	40.8	—	894.0
The Export-Import Bank of Japan	—	649.0	31.0	—	680.0
Others ²	25.3	352.3	56.0	—	433.6
Public Corporations					
Housing and Urban Development Corp.	—	569.4	140.0	157.0	866.4
The Pension Welfare Service Public Corp.	—	2,448.0	—	—	2,448.0
The Environmental Pollution Control Service Corp.,	—	36.0	—	—	36.0
The Japan Regional Development Corp.	3.0	62.3	—	—	65.3
Japan Highway Public Corp.	—	604.9	1,080.0	212.3	1,897.2
Metropolitan Expressway Public Corp.	—	66.7	189.8	—	256.5
Hanshin Expressway Public Corp.	—	57.0	162.1	—	219.1
Japan Railway Construction Public Corp.	—	101.8	—	50.0	151.8
The Overseas Economic Co-operation Fund	—	468.6	22.4	—	491.0
Others ³	48.2	1,356.5	722.0	672.8	2,799.5
Local Governments (Local government bonds and borrowings)	—	3,617.0	1,128.0	—	4,745.0
Special Companies, etc.					
The Shoko Chukin Bank	9.0	119.1	—	—	128.1
Tokyo Bay Bridge Construction Co., Ltd.	—	—	—	2.8	2.8
East Japan Railway Co., Ltd.	—	33.6	15.0	48.5	97.1
Kansai International Airport Co., Ltd.	—	—	—	50.7	50.7
Electric Power Development Co., Ltd.	—	70.0	20.0	—	90.0
Others ⁴	—	45.0	15.0	2.7	62.7
Total	91.2	22,706.6	4,409.4	2,406.8	29,614.0

- Notes: 1. Including Urban Development Loan S.A., National Hospital S.A., National Schools S.A., National Property Special Consolidation Fund S.A., Specific Land Improvement S.A., Postal Services S.A., and National Forest Services S.A., etc.
2. Including the Small Business Credit Insurance Corp., Environmental Sanitation Business Finance Corp., Hokkaido-Tohoku Development Finance Corp. and the Okinawa Development Finance Corp.
3. Including Employment Promotion Projects Corp., Teito Rapid Transit Authority, Japan Private School Promotion Foundation, Water Resources Development Public Corp., etc.
4. Including Central Japan Railway Co., Ltd., West Japan Railway Co., Ltd., Japan Freight Railway Co., Ltd. and The Organization of Promotion for Urban Development.

Chart 1 Fiscal Investment and Loan – Flow Chart of Fund



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