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“Inward entry of Japanese banks
into the Russian market”

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Abstract

The paper represents a case study of Japanese banks operating on the Russian banking market. We particularly analyze motivation, organizational representation, entry modes and strategies of Japanese banks. We argue that in case of Japanese banks both the specificity of the home country (Japan) (relationship banking, main bank system) and host country (Russia) indeed plays an important role in expanding their businesses abroad. The shares of Japanese banks in total banking assets, deposits and lending rate of the Russian banking sector remain low, and in general Japanese banks in Russia might be regarded as “followers” of the Japanese business in Russia. Meanwhile, we also provide evidence that PULL factors are the driving forces providing reasoning for the exceptions from this rule in the behavioral patterns of Japanese banks. The paper summarizes history of foreign expansion of Japanese banks into the Russian market and aims to conduct analysis under the framework of the multinational banking theory.

Keywords: *foreign banking, Japanese banks, motivation, entry modes, strategies*

JEL Classification numbers: F21, F23, P31

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1. Introduction

Japanese banks actively conduct international businesses such as foreign exchange operations, lending, securities, trusts, leasing businesses, foreign currency, derivatives operations (future, swaps and options), trade finance and others. In the mid-1990s Japanese banks were reducing their overseas businesses as a part of their restructuring programs that resulted in a decrease of foreign branches of Japanese banks from 437 to 130 as the end of March 2006. However, some signs of recovery have been appearing recently. At the end of March 2009 it was reported that the number of overseas branches was amounted to 144¹⁾. Meanwhile, interest of Japanese business in BRICs economies is also an on-going process facilitating the entry of Japanese banks into these countries.

In the present paper we try to summarize the issues related to foreign expansion of Japanese banks into the Russian market as one of the potential market among emerging economies.

Firstly, some remarks should be made on the object of the present study. We selectively not comprehensibly try to investigate the activity and behavioral patterns of Japanese banks entering into the market of a *host country* (Russia). The paper endeavors to shed light on motivation, organizational representation, entry modes and strategies of Japanese banks on the Russian market. We also add issues of host and home country specificity to our study.

Secondly, the subject of the present study are *locally (domestically) incorporated institutions* established in Russia by Japanese banks and the scope of their activity on the Russian market. We consider both *banking* (subsidiary, branch, joint-venture (JV) with a Russian bank, minor shareholder participation) and *non-banking* (representative offices) locally incorporated institutions.

Thirdly, the literature review on the issue of motivation, organizational representation, entry modes and strategies of the Japanese banks in Russia is scarce. There are no detailed studies tackling this topic. Nevertheless, issues of foreign expansion of Japanese banks into other countries are widely discussed in the existing literature: Yamori (1997, 1998), Duser (1990), Hall (2009), Slager (2005), Marc Von Der Hur (2005) and others.

In general we aim to provide answers to major questions. Are Japanese banks “followers” of the Japanese business on the Russian market? And how and to what extent the home country and host country environmental context (macroeconomic, microeconomic, institutional environment) predetermines the behavioral patterns of Japanese banks on the Russian market.

The structure of the paper is as follows. Introduction explains the subject of the present research and shapes the methodological issues. In Section 2 we outline evolution of foreign expansion of Japanese banks and briefly define market specificity of Japan as a home country. Section 3 provides an overview of the history of foreign expansion of Japanese banks into the Russian market. Motivation for entry, organizational representation, entry modes and strategies of Japanese banks are analyzed in Section 4. In Section 5 we try to evaluate the scope of activity of locally incorporated banking institutions established by Japanese banks in Russia by analyzing their balance sheets and reports on profits and losses. The Conclusion summarizes major findings of each section.

¹⁾ <http://www.zenginkyo.or.jp/en/banks/principal/index.html>. Accessed in November 2012.

2. Evolution of foreign expansion of Japanese banks and contemporary trends of development

Before analyzing the situation of foreign expansion of Japanese banks in Russia, let us briefly introduce the general outline of Japanese banks' foreign expansion. The problems of foreign expansions are extensively covered in the existing literature in studies of Yamori (1997, 1998), Duser (1990), Hall (2009), Slager (2005), Marc Von Der Hur (2005), Wan, Hoskisson, & Kim (2008), Orr (1990) and others. In multinational banking theory Japanese banks are often regarded as a typical example of "*following the customer strategy*", while recently there are studies concluding that Japanese banks "*lead*" international business. Traditionally for Japanese banks, FDI in the manufacturing sector are considered to be the determinant factor in location choice of their financial institutions. Below we summarized several stages of development of foreign expansion of Japanese banks: post-war period, "flourishing" period of rapid growth in 1980s- early 1990; slow-down caused by domestic problems on the Japanese banking market; slow signs of recovery and new wave of expansion in late 1990s-early 2000s; present stage of expansion.

Though Japanese banks had their institutions established abroad even after the WWII²⁾ we start our analysis with the 1980s which are considered to be the flourishing years of Japanese banks' foreign expansion. Rapid foreign expansion during this period made Japanese banks the object of studies in multinational banking theory.

1980s were the period of active expansion of Japanese banks. Duser (1990) states that "japanese banks are the winners in the process of internationalization, emerging as the biggest financial institutions of their kind in the world in the second part of the 1980s". During this period Japanese banks constructed worldwide operations and became very important players in several countries as well as on international financial markets. The primary question of interest is what were the driving forces behind the motivation of Japanese banks that allowed them to create such an extensive international network?

Duser (1990) states that deregulation of the Japanese financial system in parallel with growing "securitization" trend in financial markets and slow-down in economic growth fully explain the motivation of Japanese banks during this period. He generally concludes that both PUSH and PULL reasons accounted for the motivation of Japanese banks. Yamori (1996) analyzed activity of Japanese banks in USA from 1951-1994 and his result is generally consistent with the hypothesis that demand in the manufacturing sector was a crucial factor for Japanese banking FDI in USA, but he also found some reasoning that location of Japanese FDI was partially determined by local banking opportunities. During 1980s positions of Japanese banks on the USA market were rather strong. Orr (1990) states that Japanese banks were in TOP 10 leading banks during this period, while American City bank was ranked only in the TOP 20. On USA domestic market 60% of business loans were provided by Japanese banks, 2/3 of which with the direct participation of Japanese banks. Orr (1990) identifies the driving forces of this extensive foreign expansion of Japanese banks by increasing volume of USA trade, growing consumption rates in USA and excessive saving rates in Japan, favourable generally national treatment of Japanese banks in

²⁾ In 1950-1955 there were 13 branches, 3 subsidiaries and 4 representative offices of Japanese banks abroad, 1970 the number of overseas offices increased to 54, 37 and 125 accordingly.

USA, “*keiretsu system*”³⁾ and preferences of Japanese managers to retrieve banking services from compatriot banks with whom they have extensive relations in Japan. In his later study Yamori (1997) also highlights the idea that Japanese banks had financial resources superior to their competitors and by analyzing motivation of banks during 1977-1984 concludes that Japanese banks proved to be “followers” in Asia and Oceania where they had competitive advantages, “leaders” in the Middle East and “escaped” domestic Japanese regulations in order to penetrate to USA markets. Yamori (1997) advocates for the idea that internationalization of Japanese banks and their expansion to USA and Europe in 1980s was also driven by the motivation to learn new banking technologies. Duser (1990) also supports the idea that expansion of Japanese banks to Europe was driven by the aspiration to learn new technologies and acquire cheaper financing.

The situation drastically changes in 1990s after the collapse of the bubble economy. This was a slow-down period of the so-called “Japan premium”, namely the situation when interest rates of Japanese banks were extremely higher than that of foreign banks. It became more difficult for Japanese banks to withstand the competition. In addition, many Japanese banks experienced the problem of non-performing loans and some implemented restructuring programs. As the result, many Japanese banks withdrew their international businesses from abroad and oriented on domestic franchise⁴⁾. Introduction of Basel principles put new barriers for Japanese banks as many of them experienced a problem of capital adequacy (Nozaki, 2008). Hall (2009) analyzed financial condition of Japanese banks from 1995-2002 and concluded that “the performance of Japanese banks was dire due to collapse of Japan’s assets price bubble and stagnation in the real economy”. Hall identifies years of net losses of Japanese banking sector: 1995, 1997, 1998, 2001, 2002. Conversely to the behavior of banks, foreign expansion of Japanese companies was relatively moderate.

In the latter 1990s and beginning of 2000s many Japanese banks could restore their financial stability and retrieved the competitive spirit. Nevertheless, the domestic demand for financing has not improved as it had been expected. As the result, domestic competition intensified and led to emergence of large banks (city banks) that actively started implementing foreign expansion. We refer to this period as slow signs of growth and new wave of expansion when Japanese banks were pushed to search for new market opportunities abroad.

The present period of expansion is characterized by following trends: redistribution of management resources of major European and American banks; shift to Asian markets, China in particular; growing interest in BRICs.

The first trend revealed after the financial and economic crisis of 2008 when many American and European banks bore severe losses and there were cases of investments into charter capital by Japanese banks that less experienced consequences of the crisis⁵⁾. General level of trust towards Japanese banks increased, share of financing in foreign currency decreased opening opportunities for Japanese yen.

³⁾ Orr (1990) argues that *keiretsu* representing a cozy relationship between banks and Japanese enterprises let banks participate in the growth management of their clients and provide below-market loan rates. Banks accumulate huge amounts of hidden assets on the books of Japanese banks.

⁴⁾ In 1994 53 Japanese banks had 373 branches and 361 representative offices in 36 countries, but the number of overseas offices was decreasing in the latter 1990s and beginning of 2000s.

⁵⁾ Mizuho Bank invested in Merrill Lynch (USA) and Sumitomo-Mitsui Bank participated in the charter capital of Barclays Capital (UK).

Shift to Asian markets is explained by various factors. Yukimoto (2002) names high profit expectations, growing presence of Japanese business in the region, relatively high level of trust to Japanese banks as the main driving factors of foreign expansion. Yukimoto (2002) points out interesting fact that while the general trend with overseas offices of Japanese banks during late 1990s and beginning of 2000s was negative, in case of China the number of branches, representative offices was actually increasing.

As for the BRICs countries, the volume of economic transactions with these countries increased, therefore more and more Japanese companies show interest in the growing emerging markets where they can get high profits. Profitability is also a motivation for expansion for Japanese banks. According to the Bank of Japan, loan balance of Japanese banks to BRICs as of March 2005 amounted to 1.5 billion yen, 2/3 was invested to China. Japanese banks show interest in small and medium enterprises and some European companies operating in China and not simply “following” Japanese business.

The presence of Japanese banks is abroad still an on-going process, but some researches point out that off-shore business of Japanese banks is not sufficient enough (Nozaki, 2008). Japanese banks are strong at project financing and scope of syndicated loans in the Middle East and Europe and have leading positions here (SMFG, Mizuho FG), but inferior to competitors in the total level of advisory services on M&A. Foreign expansion of Japanese banks developed in several stages and at present it is shifted towards Asian and BRICs countries. Previous studies have shown that Japanese banks applied “follow the customer” approach in expanding their international business, due to the fact that domestic banking system of Japan is based on the so-called “*main bank*”⁶⁾ system and extensive system of “*keiretsu*”. This system of relationship banking provided access to extensive financial resources and increased assets of many Japanese banks and was considered to be the crucial factor in foreign expansion in 1980s. The new wave of expansion of Japanese megabanks in the beginning of 2000s partially might be explained by these “market specificity” of the Japanese banking industry and business relations. Meanwhile, as viewed above there are some studies advocating for the change in behavioral patterns of Japanese banks, showing a shift towards local business opportunities in foreign countries. In Section 3 we consider the history of foreign expansion of Japanese banks into the Russian market and later on try to evaluate the motivation of Japanese banks on the Russian market.

⁶⁾ The present literature is overwhelmed with definitions of the main bank system, but generally it is understood as a system of intensive relationship between the banks and the firms in terms of reciprocal shareholding, monitoring, providing information, managerial and banking services. The main bank is the largest single lender to its corporate client and its larger shareholder among other banks. This system emerged in Japan in the early period of uncertainty and difficulty following the World War II and grew rapidly in the high growth era (Dilli Ram Pokhrel,). Aoki et al. defines the main bank system as a nexus of relationship comprising a multitude of financial, informational and managerial ties between the firms and their partner banks, a unique reciprocal relationship between the regulatory authorities such as Ministry of Finance or Central Bank. In their analytical study Aoki and Patrick (1994) explain the main bank system as an informal set of regular practices, institutional arrangement and behavior that constitute a system of corporate finance and governance.

3. History of foreign expansion of the Japanese banks into the Russian market

Japanese investments into the Russian economy have increased in recent years, though Japan is still far from being the major foreign investor for Russia. According to the data of the Federal State Statistics Service (Rosstat) in 2010 the total volume of foreign investments from Japan amounted to approximately 1.1 billion USD, which is 9 times higher in comparison to 2004. Majority of investments come in the form of other investments and trade credits, FDI are on the second place and portfolio investments are insignificant in number. The volume of accumulated Japanese investments in Russian economy in the end of June 2009 rose to 6.09 billion dollars, up by half as compared with the end of 2008. Nearly 80% of this amount are investments in oil production and refining, 3.4% – in forest and wood, 1.6% – in automotive industry, 2.6% – in the sphere of information and communication technologies.

As for the financial sector, the share of Japanese foreign investments here is relatively low and amounted only to 2.36% in the total volume of Japanese investments into Russia in 2010⁷. Japan, however, has the largest number of locally incorporated banking institutions in Russia from the Asian region: India, China – 2 domestic banks, South Korea, Vietnam, Iran – 1 domestic bank each, while Japan has 4 locally incorporated subsidiaries (plus many representative offices).

The amount of investments that was accumulated by the banking sector of Russia in the form of FDI is difficult to evaluate in the Rosstat statistics, therefore below we analyze Japanese investments into the banking sector through the activity of locally incorporated banks (domestic juridical entities) with Japanese foreign capital participation.

Table 1 summarizes the chronology of foreign entry of Japanese banks into the Russian market. While generally, the expansion of foreign banks from Japan is somewhat restrained in character in comparison to foreign entry of banks from Europe or USA, it is possible to define a few stages in penetration of Japanese banks into the Russian market.

The first wave started right after the collapse of the Soviet Union and can be characterized as a sort of *temporizing period* (1992-1998). This is the period of formation of the banking regulation and banking sector of Russia as the whole, where many foreign banks even from other countries were reluctant to penetrate on the market. Representative office in Moscow of Tokyo Bank (1992) and representative office of Michinoku Bank in Uzhno-Sakhalinsk (1995) were established during this period for the purpose of gathering information on the market, legal framework of the banking sector and social, economical and political situation as the whole. Financial crisis of the 1998 can be regarded as a deterrent factor for entry. While generally the liberalization of the financial sector was gradually implemented during this period, the entry of banks was somewhat slow.

⁷) Author's calculation based on Rosstat data. The average share of Japanese investments into the financial sector in the total volume of foreign investments in Japan for the period 2004-2009 amounted to 0.4%.

Table 1 – History of foreign entry of Japanese banks into the Russian market

Year	List of Japanese banks and their domestic institutions in Russia
1992	Representative office of Tokyo Bank in Moscow
1995	Representative office of Michinoku Bank in Uzhno-Sakhalinsk
1999	ZAO Michinoku Bank (Moscow)
2002	Domestic branch of ZAO Michinoku Bank (Moscow) in Khabarovsk
2003	Domestic branch of ZAO Michinoku Bank (Moscow) in Uzhno-Sakhalinsk
8.2005	Representative office of Mitsui-Sumitomo Bank (Europe) in Moscow
8.2006	ZAO Mitsubishi-Tokyo UFJ Bank (Eurasia) in Moscow (<i>officially started the banking activity from 11.2006</i>)
10.2006	ZAO Mizuho Corporate Bank in Moscow (<i>Mizuho Bank (Japan) acquired 100% of shares of ZAO Michinoku Bank (Moscow), domestic branches of ZAO Michinoku Bank (Moscow) in Khabarovsk and Uzhno-Sakhalinsk were closed</i>)
12.2006	Representative office of Mizuho Bank (<i>officially started the banking activity from 2.2007</i>)
6.2007	ZAO Toyota Bank (Moscow) (<i>5 domestic branches of ZAO Toyota-Bank in St. Petersburg at present</i>)
4.2008	Representative office of ZAO Mitsubishi-Tokyo UFJ Bank (Eurasia) in St. Petersburg
3.2009	Representative office of Hokkaido Bank in Uzhno-Sakhalinsk
4.2009	ZAO Sumitomo Mitsui Rus Bank in Moscow
2.2010	SBI Holdings (Japan) acquired 50% of shares of Obibank (Russia)
9. 2012	Domestic sub-branch of ZAO Mitsubishi-Tokyo UFJ Bank (Eurasia) in Vladivostok
4.2013	Hokkaido bank announced the establishment of a Representative office in Vladivostok

Source: compiled by author

The second wave of activity of the Japanese banks on the market from 1999 – 2003 can be definitely marked as the *pioneer one* actively driven by a regional Japanese bank Michinoku. Michinoku was the first Japanese bank to open a subsidiary (locally incorporated banking institution) in Russia. The subsidiary ZAO⁸⁾ “Michinoku Bank (Moscow)” was opened in 1999 as the result of 10 years lasting strong, cultural and regional ties between the Far East of Russia and Aomori Prefecture⁹⁾. The subsidiary was opened in Moscow under the pressure of Russian authorities, though initially the Management Board of Michinoku planned to established a subsidiary on the Russian Far East. For that purpose a representative office was firstly opened in Uzhno-Sakhalinsk in 1995 and Michinoku company’s office was opened in Khabarovsk. The representative office gathered information about the market. The financial crisis of 1998 didn't influence on the decision of Michinoku to open a subsidiary in Russia and therefore ZAO Michnioku Bank (Moscow) was established as a 100% subsidiary by Michinoku Bank (Japan). In 2002 a branch of ZAO Michinoku Bank (Moscow) was opened in Uzhno-Sakhalinsk and Khabarovsk (2003). Having a reputation of a “Family Bank” in Japan, Michinoku on

⁸⁾ ZAO – Zakritoe Akcionerhoe Obshestvo (Closed joint-stock company)

⁹⁾ Two regions established cultural and international exchange between citizens of the Far East and Aomori Prefecture. Charter flights were organized for tourists in summer; student’s exchange between junior high schools of both regions. As of end of 2000 more than 1800 Russian junior high school students visited Aomori and about 450 Japanese junior high school students had a chance to come to Russia (Imai, 2004).

acquiring the license permitting operations with Russian citizens in 2001, started consumer-lending business (retail banking). In particular it provided mortgage loans to Russian citizens. From 2003 ZAO Michinoku Bank (Russia) got permission to issue letters of credit to the participants of the Japanese-Russian trade. The bank also participated in financing Gazprom (Blue Stream Pipeline Company) and provided loans to Vneshtorgbank (export of equipment from Japan to Russia). As Imai (2004) shows the success of Michinoku on the Russian market¹⁰⁾ was due to excellent management and personal sympathy towards Russia of the former chairman of the board of directors Mr. Daidoji; strategic move to make a breakthrough on the niche market different from rivals and decisiveness and managerial skills of the board of directors. Notwithstanding these success points, the subsidiary of Michinoku in Moscow was acquired by Michinoku Bank and domestic branches in Khabarovsk and Uzhno-Sakhalinsk were closed.

In 2000s the Russian economy finally moved towards a relative stability and showed signs of high economic growth. Many foreign investors including Japan showed their interest in natural resource and manufacturing sectors. This fact also facilitated the decision of foreign banks to enter on the market. Japanese banks were still going behind the financial institutions of other countries, but even though 2003-2005 were years of *reevaluation of market opportunities and growing interest* in the Russian market by Japanese business. During this time a representative office of Mitsui-Sumitomo Bank (Europe) was established in Russia (2005), two Japanese megabanks stepped into the Russian banking market mostly driven by their domestic clients who started business operations in Russia. Among the three megabanks the first one to start-up the banking activity on the Russian market was Tokyo-Mitsubishi UFJ. In August 2006 it obtained the license of the Central Bank of Russia (CBR) and officially started its activity from November 2006. 100% of shares of ZAO Mitsubishi-Tokyo UFJ (Eurasia) belong to Mitsubishi-Tokyo UFJ Bank (Japan). At present the bank is mostly involved in providing finance to the corporate sector. Mizuho Bank also entered on the market in 2006 through acquisition of 100% of shares of Michinoku Bank. Simultaneously, for the purpose of investigation of the Russian market it obtained the permission (2006) and opened a representative office in Moscow in February 2007. The decision of Toyota Group to establish a plant in St. Petersburg, growing boom of Japanese food and culture in Russia stipulated to some extent the further entry of Japanese business into Russia. Japanese banks traditionally oriented on their customers. Thus, Toyota Financial Group opened a subsidiary in Moscow in 2007. As of end 2007 349 Japanese companies operated in Russia, 2007-2009 many Japanese automotive companies entered on the market: Toyota (2007), Trad (2007), Isuzu (2008), Nissan (2009) and others. Therefore, foreign entry of Japanese banks happens simultaneously with the expansion of Japanese business.

Japanese banks didn't exit the market as the result of the global financial and economic crisis. On the opposite, after crisis years (2009-2012) may be regarded as the *fourth wave* of entry of the Japanese banks. The third megabank Mitsui-Sumitomo Bank that historically had three attempts to enter on the Russian market finally established a locally incorporated banking institution in order to provide assistance to Japanese companies and consultation to Russian and European companies and business. New players such as SBI Holdings showed interest in the development of

¹⁰⁾ Ratings of ZAO Michinoku Bank (Moscow): in terms of capital – 185th place; charter capital – 23^d place; consumer lending – 22^d place; deposits – 17th; corporate lending – 24th

on-line banking in Russia and entered in the form of joint-venture (JV) in 2010. Further expansion of Japanese automotive industry into Russia and recent economic development of the Far East under the guidance of the Russian government stipulated the decision of ZAO Mitsubishi-Tokyo UFJ (Eurasia) to establish a domestic sub-branch in Vladivostok in 2012.

To sum up, it is conditionally possible to define several stages of foreign entry of the Japanese banks into the Russian market: temporizing period (1992-1998); sole pioneering (1999-2004); reevaluation of market opportunities and growing interest of Japanese business towards Russia (2005 – 2008); post-crisis stage and emergence of new players (2009-2012). Meanwhile, the entry of banks on all stages (except perhaps the sole pioneering one) was implemented in parallel with the entry of Japanese companies on the market. In the next chapter we consider the questions of motivation of Japanese banks, organizational representation of Japanese banks on the Russian market, their entry modes and strategies.

4. Motivation, entry modes and strategies of Japanese banks

In the present part we examine the issues of motivation, organizational representation, entry modes and strategies of the Japanese banks on the Russian market. At first, by looking at the motivation for foreign entry, we aim to define the driving forces that stimulate Japanese banks to go abroad (PULL/PUSH reasons).

Notwithstanding the fact that in scientific literature on foreign expansion of banks Japanese banks are often regarded as the typical example of the “*follow the customer*” strategy, there are research studies demonstrating that this tendency is not the sole one applied by them (Marc Von Der Ruhr (2005), Slager (2005)). As **Table 2** demonstrates, in case of Russia “*the follow the customer*” approach might be regarded as common for many Japanese banks, especially for the three megabanks. Thus, the so-called PUSH reasons are the major triggers for penetration of Japanese banks into the Russian market. Foreign entry of many Japanese companies stipulated the foreign entry of Japanese banks. This is often explained by the fact that Japanese banking system is a typical representative of “*relationship banking*”, e.g. through the specific features of the home country. The system here mostly refers to the relationship finance. Traditionally, every large Japanese firm had a strong and often long-term relationship with one bank that served as its “*main bank*”. That bank implemented functions of monitoring of the firm, intervened in its governance through board appointments, acted as a delegated monitor for other creditors, and agreed to rescue the firm if it fell into financial distress. Nevertheless, some researches argue the sustainability of the main bank system, due to the fact that Japan deregulated its financial markets in the 1980s and as the result many Japanese firms prioritized market finance over their relational lenders (Miwa et. al, 2005). In the present paper we do not argue the sustainability of the main bank system, but we do stress that it still has a very strong impact on the Japanese domestic market (home country market), which proves to be one of the specific features of the Japanese banking sector as a whole. Therefore, in case of foreign expansion into Russia, the relation between relationship banking and the “*follow the customer*” approach is somewhat difficult to be neglected.

Table 2 – Motivation, entry modes and strategies of Japanese banks on the Russian market

Name of the locally incorporated institution (organizational representation)	Main Japanese shareholders	Motivation of entry	Entry mode	Strategy
ZAO Michinoku Bank (Moscow) (1999) (CJSC)	Michinoku Bank (Japan) - 100% of shares	PUSH (historical, non-economic reasons)	Representative office, subsidiary, domestic branches	Organic growth
ZAO Mitsubishi Tokyo UFJ Bank (Eurasia) (2006) (CJSC)	Mitsubishi Tokyo UFJ Bank (Japan) - 99,999% of shares	PUSH (follower)/PULL (later motivation)	Representative office, subsidiary, domestic sub-branch	Organic growth
ZAO Mizuho Corporate Bank (2006) (CJSC)	Mizuho Bank (Japan) -100% of shares	PUSH (follower)/PULL (market potential)	Representative office, subsidiary	M&A
ZAO Toyota Bank (2007) (CJSC)	Toyota Kreditbank GmbH (Germany) – 99.75% of shares, Toyota Leasing GmbH (Germany) – 0.25% of shares (Toyota Financial Group (Japan))	PUSH (follower)	Subsidiary	Organic growth
Representative office of Hokkaido Bank in Uzhno-Sakhalinsk (2009)	Hokkaido Bank (Japan)	PULL (market potential) /PUSH	Representative office	-
ZAO Sumitomo Mitsui Rus Bank (2009) (CJSC)	Mistui-Sumitomo Bank (Japan) – 99.0% of shares, Sumitomo Mitsui Banking Corporation Europe Ltd. (UK)– 1% of shares	PULL (market potential)/PUSH (follower)	Representative office, subsidiary	Organic growth
ZAO Obibank (CJSC)	SBI Holdings (Japan) – 50% of shares; LLC Investment Financial company “Metropol” (Russia) – 46.49% of shares , individual shareholder – 3.51% of shares	PULL (market potential, investment and internet banking)	Joint-Venture (JV)	M&A (JV business)

Source: compiled by author

Meanwhile, in case of Michinoku Bank PUSH factors were strongly dependent on historical and non-economic issues as it was shown in part 1 of the present paper.

Some Japanese banks were attracted to the Russian market as the result of high economic growth of Russia in the beginning of 2000s and its market potential, explaining the motivation of Japanese banks by PULL factors. SBI Holdings entered on the market in order to start online banking, while Hokkaido bank established a representative office in order to search for the market potential (PULL) and provide consulting services to the Japanese companies considering foreign expansion into the Russian market (PUSH). In 2013 Hokkaido bank announced the decision to open the second representative office in Vladivostok, proving the growing interest in doing business in Russia. The entry of ZAO Sumitomo Mitsui Rus Bank is also not solely driven by the PUSH reasons.

Thus, the motivation of Japanese banks on the Russian market to a great extent is explained by the PUSH reasons and many Japanese banks on the market are initially regarded as “*followers*”. They prefer to provide financial banking services and consulting services on doing business in Russia only to the corporate sector of their domestic Japanese clients operating in Russia. There are few exceptions from this rule – the motivation for entry of SBI Holdings (on-line banking both for the corporate sector and retail banking), Toyota Bank (can be regarded as a typical “*follower*”, but is a “*leader*” in retail banking (automobile loans) to Russian citizens), ZAO Sumitomo Mitsui Rus Bank to some extent and Hokkaido Bank. Needless to say, that motivation of the Japanese banks is likely to change over time. Domestic expansion of ZAO Mitsubishi Tokyo UFJ Bank that opened a representative office in St. Petersburg in 2008 and sub-branch in Vladivostok in 2012 is a good example to demonstrate this fact. Representative office of Mistui Sumitomo (Eurasia) in Moscow aims to provide support and consulting services to European companies having connections with Russian business and Russian companies planning to attract finance from the international markets.

In terms of organizational structure, all Japanese banks that established locally incorporated banking institutions in Russia preferred to choose the Closed joint-stock company (CJSC) type and almost in all cases distribute all the shares among the parent banks located in Japan (*Table 2*). The exception here is ZAO Toyota Bank whose main shareholder is a subsidiary of Toyota Financial Services located in Germany¹¹⁾. The example of ZAO Toyota Bank is of some interest, due to the fact that this bank can be regarded both as the “*follower*” and the “*leader*”. In addition, this domestic subsidiary was established by the indirect-FDI or “*expansion under the third country’s flag*” which is a relatively new issue in the theory of TNB (MNB).

Representative offices and 100% subsidiaries (locally incorporated banking institutions) were chosen by Japanese banks as the entry modes into the Russian market. Non-transparency of legislation regarding the property rights, difficulties in finding local partners, views on business in Russia through the “ownership=dominance” prism might be the reasons stipulating this choice. We refer to these restrictive factors as peculiarities of the host country (Russia). In general, the behavior of Japanese banks corresponds to the so-called “*organic growth*” strategy¹²⁾, but SBI Holdings established a JV with the Russian “Obibank” and Mizuho used M&A a strategy and entry mode for their expansion. In general entry modes and organizational structure are similar to the ones applied by other foreign banks operating on the market, but European and American banks recently enter on the Russian market using the M&A strategic approach (Gorshkov, 2011). Institutional barriers like regulation on the foreign share in the capital of the banking sector (50% limit; low level of ownership transparency and protection of shareholders’ rights predetermine the entry form of many bank from Japan as many other foreign banks entering on the Russian market.

In short, Japanese banks are initially driven by the PUSH factors when entering into the Russian market as “*followers*” of their domestic clients, conditionally due to the fact that home country’s institutional context (relationship banking, keiretsu) exert an influence (though it is rather difficult to prove it empirically). They tend to apply

¹¹⁾ In this sense foreign investments from Toyota should be regarded as the German ones, but we consider them as a indirect FDI, as Toyota Financial Services (Japan) is the parent bank for Toyota Kreditbank GmbH (Germany).

¹²⁾ Organic growth strategy is the one aiming the expansion of business and is fully based on the internal resources of a foreign bank. It is normally very costly and takes a lot of time to implement.

green-field investment scheme and establish 100% subsidiaries in the form of CJSC due to the specific institutional context of Russia as a host country. Their behavior is explained by the “*organic growth*” strategy. However, PULL factors should not be underestimated. Some Japanese players are attracted by the conditions of Russia as the home country (PULL factors) and establish trial businesses (ZAO Obibank, ZAO Toyota Bank) or simply explore the market potential by establishing representative offices which are non-banking locally incorporated institutions of Japanese banks. Even the case of megabanks is hard to simply explain by the sole PUSH (followers) factors. In a sense, the host country institutional context might be predominant.

5. Economic and financial analysis of locally incorporated banks with Japanese capital

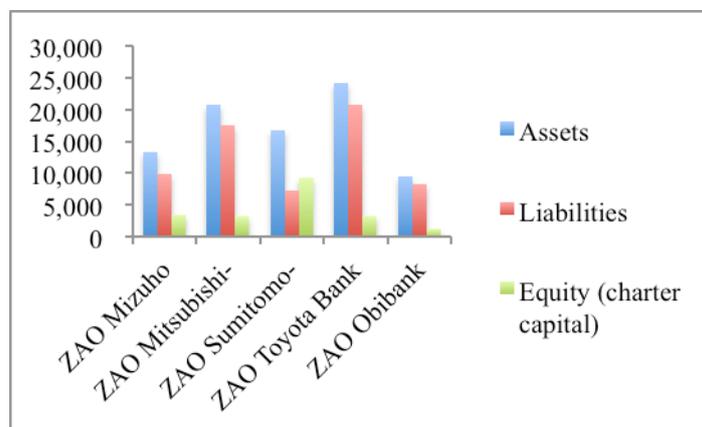
In the present part we briefly introduce economic and financial position of locally incorporated banks with Japanese capital. Based on the CBR statistics, balance sheets of banks and statements on profit and loss, we analyze the dynamics of assets, liability, equity and net profit structure. We also show the position of Japanese banks in the total ranking of Russian banks.

Figure 1 shows the data on assets, liabilities and equity structure. The amount of assets and liabilities generally fluctuates around 12-25 million rubles. The highest indicators has ZAO Toyota Bank, though in terms of equity it is considerably inferior to other banks (except JV ZAO Obibank). The amount of equity exceeds the minimum stipulated by the CBR¹³⁾. Nevertheless, when compared with some other banking institutions in Russia, positions of banks with Japanese capital are not comforting. In terms of rating in assets the best positions belong to ZAO Toyota Bank (103 place) and ZAO Mitsubishi Tokyo UFJ (134th place). Situation with the capital ranking is somewhat better with ZAO Mitsubishi Tokyo UFJ being on the 50th place and ZAO Sumitomo Mitsui Rus Bank on the 63d place. In any case, Japanese banks leave their positions to some European and American banks (Raiffeisen is on the 11th place in terms of assets and on the 10th place in capital)¹⁴⁾. Nevertheless, with almost 1000 banks operating on the market, these ratings of Japanese banks look quite satisfactory.

¹³⁾ For details refer to CBR data. Balance sheet of particular banks. For all Japanese banks as of 01.01.2012 the sufficiency coefficient of capital was higher than the norm stipulated by the CBR.

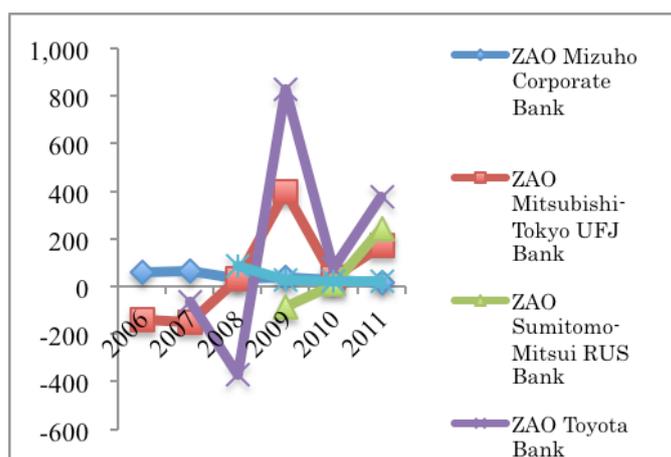
¹⁴⁾ For details on rating refer to Table 1.4 of the Appendix.

Figure 1 – Assets, liabilities and equity of locally incorporated banks with Japanese capital (million rubles) as of 01.01.2012



Source: compiled by author on the base of CBR statistics

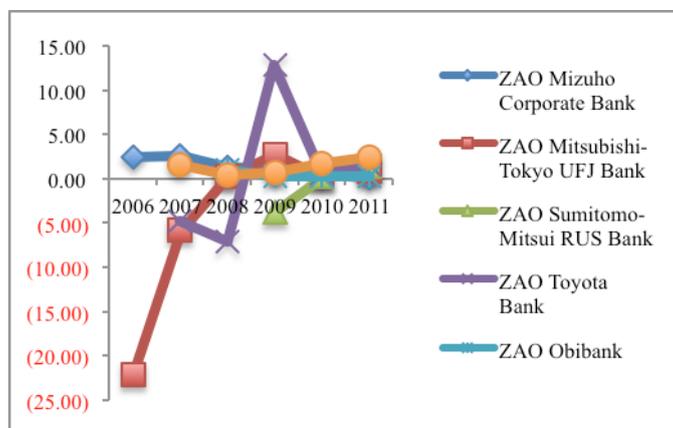
Figure 2 – Net profit of locally incorporated banks with Japanese capital (million rubles) in 2006-2011



Source: compiled by author on the base of CBR statistics

Net profit dynamics is shown on **Figure 2**. In general the first operating year after the establishment of the banking institution in Russia was negative for almost all Japanese banks. For some banks, like ZAO Toyota Bank the negative trend continued even for 2 years fueled by the crisis in 2008. 2009 was quite a positive year for many Japanese banks and they could maintain (ZAO Obibank, ZAO Mizuho Corporate Bank) and considerably increase (ZAO Toyota Bank, ZAO Mitsubishi Tokyo UFJ Bank) their net profits. In 2010 for almost all banks the negative trend continued due to the market fluctuations, but in 2011 the recovery trend was outlined. The structure of assets shows that Japanese banks provide loans to corporate sector and Russian banking institutions (for details see balance sheets of the specified banks).

Figure 3 – ROA of locally incorporated banks with Japanese capital and ZAO Raiffeisen Bank (%) in 2006 - 2011

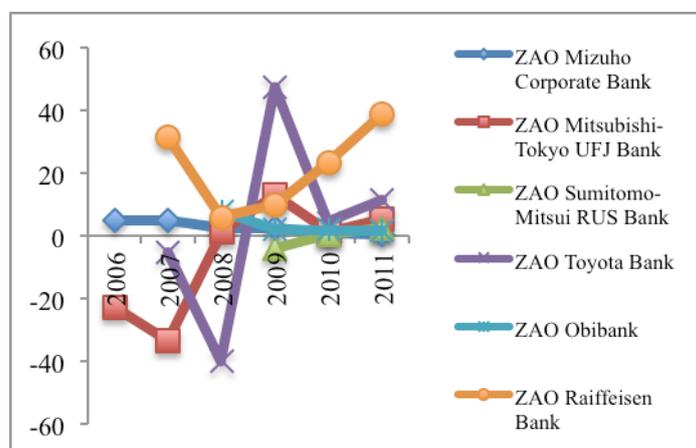


Source: made by author on the base of CBR statistics

Return on assets (ROA) and return on equity (ROE) for Japanese banks locally incorporated in Russia are calculated and presented on Figure 2 and Figure 3. ROA is generally reflecting the dynamics on assets and general trends more or less the same for all banks. Even when compared with ZAO Raiffeisen Bank (Austria) the ROA are on the same level and are in the range of 1-2.5% as of 01.01.2012 (for details refer to *Appendix Table 1.1, 1.2*).

The situation of ROE is slightly different. While there is still possible to distinguish similar trends in ROE dynamics, the gap with other foreign banks here is quite high - up to 30% (ROE of ZAO Raiffeisen is calculated for the purpose of a relative comparison).

Figure 4 – ROE of locally incorporated banks with Japanese capital (%) in 2006 – 2011



Source: made by author on the base of CBR statistics

Table 1.3 in the Appendix shows that Japanese banks are mostly engaged in corporate lending and do not prefer to work with the individual customers. Ratings in

corporate lending for them are better than those for consumer lending or deposits level. ZAO Toyota Bank is an exception here marking the 36th place out of almost 1000 in terms of consumer ending as of 01.10.2012. Retail business of ZAO Toyota Bank (providing automobile loans) stands behind this high-ranking results. Other Japanese banks obviously show no interest in retail business and deposit activity with their ranking positions fluctuating in the range of close to 900th place. This sounds extremely astonishing when compared with the leader on the Russian market among foreign banks – ZAO Raiffeisen Bank that is marked 11th in terms of assets, 10th in capital, 11th in corporate lending, 10th in consumer lending and 5th in terms of deposits from individual households.

Finally we look at the revenue structure of Japanese banks operating on the Russian market. *Table 1.4* provides data on revenue structure in 2010 and 2011. Majority of revenue origins from interest rates with only one exception - ZAO Sumitomo Mitsui Rus Bank which revenue structure is mostly based on commission. Income from foreign exchange operations and reevaluation of foreign currency is also present in the total revenue structure, but with some negative outcomes for particular banks.

To sum up, the scope of activity of locally incorporated Japanese banks in Russia is not that high. Japanese banks are inferior to some other foreign banks operating on the market. The analysis on revenue structure and dynamics of assets and liabilities showed that many Japanese banks are engaged in corporate lending mostly to crediting Russian banking institutions and presumably some services to Japanese business on the Russian market. Retail business and deposit activity are not priority vectors of development on the Russian market for Japanese banks. Therefore, the scope of activity generally corresponds to the initial motives for entry (PUSH), but with gradual changes due to the market potential in Russia (PULL).

6. Conclusion

In the present paper we introduced a case study of Japanese banks operating on the Russian banking market. We analyzed the history of foreign entry of Japanese banks into the Russian market and conditionally defined a few stages of foreign entry. We also raised issues with motivation, organizational representation, entry modes and strategies of Japanese banks.

Foreign expansion of Japanese banks developed in several stages and at present it is shifted towards Asian and BRICs countries. The new wave of expansion of Japanese megabanks in the beginning of 2000s partially might be explained by these “market specificity” of the Japanese banking industry and business relations. Meanwhile, as viewed above there are some studies advocating for the change in behavioral patterns of Japanese banks, showing a shift towards local business opportunities in foreign countries.

The shares of Japanese banks in total banking assets, deposits and lending rate of the Russian banking sector remain low, some Japanese banks in Russia are “followers” of the business of Japanese companies. Meanwhile, there are exceptions from this rule in the behavioral patterns of the Japanese banks. As it was shown in the paper, motivation of entry for Japanese banks to a great extend might be explained by PUSH factors. These include the “follow the customer” approach (Toyota Bank, initial motives of Mistubishi-Tokyo), historical and cultural reasons (Mihinoku), and

decisions on foreign strategy of particular banks. Nevertheless, motivation for entry like high profitability of the market, searching new market niches, consumer lending business, providing services to the domestic banking and non-banking clients and others comprise the so-called PULL factors. And these should not be underestimated as driving forces for banks like SBI Holdings, Hokkaido Bank, recent change of motivation of megabanks.

Thus, generally speaking the idea that Japanese banks are a typical example of “follow the customer” approach advocated by the multinational banking theory in Russian condition is only partially confirmed, due to the existence of PULL factors as well.

Another argument is that in case of Japanese banks both the market specificity (relationship banking, main bank system) of the home country (Japan) and host country (Russia) (property rights, specific structure of the banking sector) to some extent plays an important role in expanding their businesses abroad. Barriers existing in the banking sector of Russia and Russian economy as the whole stipulated the choice of organizational forms such as CJSC and form of entry as organic growth strategy rather than the M&A approach. Japanese market specificity to some extent predefined the limited scope of activity on the Russian market (phobias towards doing business in Russia, low trust in the market quality from Japanese and foreign investors). As the matter of fact, these home and host country specificities are conditional ones. Nevertheless, they partially explain the differences among the foreign entry of banks from other home countries.

Appendix

Table 1.1 – *Assets, liability, equity and profit of locally incorporated banks with Japanese capital (thousand rubles)*

Banks	Years	Assets	Liabilities	Equity (charter capital)	Profit	ROA, %	ROE, %
ZAO Mizuho Corporate Bank	2011	13,312,032	9,864,640	3,430,829	16,564	0.12	0.48
	2010	7,509,100	4,078,271	3,430,829	27,275	0.36	0.79
	2009	3,420,102	2,016,547	1,403,555	35,942	1.05	2.56
	2008	2,849,159	1,526,546	1,367,613	35,284	1.24	2.58
	2007	2,574,587	1,242,680	1,331,907	65,241	2.53	4.90
ZAO Michinoku Bank	2006	2,479,193	1,218,360	1,260,833	60,425	2.44	4.79
	2005	2,451,873	1,254,818	1,197,055	39,800	1.62	3.32
ZAO Mitsubishi-Tokyo UFJ Bank	2011	20,788,228	17,520,835	3,267,393	170,875	0.82	5.23
	2010	15,480,731	12,384,212	3,096,519	38,705	0.25	1.25
	2009	14,236,516	11,178,703	3,057,813	396,512	2.79	12.97
	2008	13,676,653	11,015,351	2,661,302	32,992	0.24	1.24
	2007	2,582,135	2,129,629	452,506	-150,915	-5.84	-33.35
	2006	627,075	23,823	603,252	-138,688	-22.12	-22.99
ZAO Sumitomo-Mitsui RUS Bank	2011	16,652,671	7,285,481	9,367,190	244,517	1.47	2.61
	2010	4,543,651	2,320,978	2,222,673	9,699	0.21	0.44
	2009	2,282,862	69,888	2,212,974	-87,026	-3.81	-3.93
ZAO Toyota Bank	2011	24,107,529	20,821,559	3,285,970	377,708	1.57	11.49
	2010	13,140,164	11,311,902	1,828,262	77,233	0.59	4.22
	2009	6,439,726	4,688,697	1,751,029	827,777	12.85	47.27
	2008	5,238,511	4,315,259	923,252	-370,435	-7.07	-40.12
	2007	1,372,419	107,903	1,264,516	-66,213	-4.82	-5.24
ZAO Obibank	2011	9,437,462	8,234,865	1,202,597	22,236	0.24	1.85
	2010	9,857,342	8,663,624	1,193,718	23,115	0.23	1.94
	2009	9,693,991	8,527,540	1,166,351	24,801	0.26	2.13
	2008	9,050,343	7,981,308	1,069,035	85,236	0.94	7.97
	2007	8,891,856	7,813,945	1,077,911	0	0.00	0.00

Source: Balance sheets of banks obtained from CBR, various years

* ROA (return on assets) and ROE (return on equity) are calculated by author

Table 1.2 – *Assets, liability, equity, net profit and revenue structure of Raiffeisen Bank (thousand rubles)*

Years	2007	2008	2009	2010	2011
Assets	419,738,284	555,142,221	474,435,124	482,906,850	571,916,479
Liabilities	377,490,032	498,005,212	414,875,194	416,186,289	494,605,427
Equity (Charter capital)	21,828,968	36,711,260	36,711,260	36,711,260	36,711,260
Net Profit	6,857,005	2,159,880	3,566,553	8,516,542	14,197,764
Revenue structure:					
Interest rate revenue	31,183,775	45,444,634	48,549,246	35,699,389	40,742,738
Comission revenue	8,414,638	6,272,721	6,762,002	7,489,028	8,952,077
Income from foreign exchange operations	1,714,745	3,177,102	7,969,079	6,515,142	157,961
Income from reevalutaion of foreign currency	2,337,485	-2,848,425	-4,545,782	-556,277	7,111,433
ROA,%	1.63	0.39	0.75	1.76	2.48
ROE,%	31.41	5.88	9.72	23.20	38.67

Source: Balance sheets of banks obtained from CBR, various years

* ROA (return on assets) and ROE (return on equity) are calculated by author

**Table 1.3 – Rating of locally incorporated banks with Japanese capital
Bank and Raiffeisen Bank (place in the total rating) as of 01.10.2012**

Bank	Rating (place) in				
	Assets	Capital	Corporate lending	Consumer lending	Deposits of individual households
ZAO Mizuho Corporate Bank	186	132	156	856	718
ZAO Mitsubishi Tokyo UFJ Bank	134	50	79	866	871
ZAO Sumitomo Mitsui Rus Bank	163	63	137	884	880
ZAO Toyota Bank	103	128	162	36	868
ZAO Obibank	242	227	298	307	N/A
ZAO Raiffeisen Bank	11	10	11	10	5

Source: <http://bankir.ru/rating> (accessed on November, 20th 2012)

**Table 1.4 – Revenue structure of locally incorporated banks with Japanese capital
(thousand rubles)**

Bank	Net Profit		Interest revenue		Comission revenue		Income from foreign exchange operations		Income from reevaluation of foreign currency	
	2010	2011	2010	2011	2010	2011	2010	2011	2010	2011
ZAO Mizuho Corporate Bank	27,725	16,564	158,174	290,410	24,334	59,191	42,002	50,777	3,219	-2807
ZAO Mitsubishi-Tokyo UFJ Bank	38,705	170,875	399,482	503,458	33,138	53,974	-110,051	-18,302	172,556	146,042
ZAO Sumitomo-Mitsui RUS Bank	9,699	244,517	87,307	304,146	371,636	609,534	3,780	-9,123	2,985	19,716
ZAO Toyota Bank	77,233	377,708	1,092,565	2,336,065	1,288	1,378	2,274	12,122	-1,457	-1856
ZAO Obibank	23,115	22,236	677,779	628,390	22,042	28,086	-5,024	105,897	-10,394	-36,768

Source: P/L of banks obtained from CBR

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