

Will the TARP Succeed? Lessons from Japan

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Takeo Hoshi

I have just finished a short paper with Anil Kashyap, which reviews the Japanese experience with a series of asset management companies ([CCPC](#) and all that) and evaluates the TARP. [The paper is available as an NBER Working Paper](#). Here is the abstract of the paper.

The U.S. government is hiring asset managers to purchase up to \$700 billion of toxic real estate securities that are the center of the current credit crisis. Buying up assets, if done properly, might address the collective under-capitalization that is the fundamental problem plaguing the financial system. But, experience with financial crises in other countries suggests that success is by no means guaranteed. Japan was the largest other country where the banks were seriously undercapitalized and where asset purchases were a critical part of the government's response to the problem. The U.S. bailout plan is similar to the Japanese approach in that it does not clearly identify the capital problem as critical and instead proposes using AMCs to remove distressed assets from bank balance sheets. When Japan used AMCs, their effectiveness was limited in part because they did not purchase enough assets. AMCs did not help recapitalization, either, and Japan had to come up with different mechanisms to use public funds for recapitalization. Both these risks are also present for the U.S. plan.

Now the TARP seems to be moving beyond an asset management company scheme to include direct bank recapitalization using public funds. Our paper also reviews the Japanese experience of recapitalization using public funds, which was tried after (unsuccessful) attempts of using asset management companies, and identifies several challenges direct recapitalization approach will face.