— *Chapter 14* —

CULTURE CLASH

These days I feel like one leg is in the old-LTCB, but the other leg—or the other half of my body—is in Shinsei management! Sometimes it is like being pulled in two.

—Hidebumi Mori; Senior Managing Director, Shinsei Bank

As Yashiro settled into his new office on the nineteenth floor, the bank staff nervously wondered what would happen next. About 2,000 former LTCB employees—or two-thirds of the staff—had stayed on at the bank, demoralized and defeated, but glued to their places by intense bonds of mutual loyalty. During 1999 wild rumors had regularly swept the bank that Ripplewood was about to unleash some dreadful things, including sacking workers. The speculation became even more intense when a local television station screened a fictional drama about a Japanese company taken over by foreigners, which showed women in senior management roles—bossing men around. "We all watched that program and talked about it," confessed Takei Tamiwa, a former LTCB "office lady." "I wondered if that would happen to us as well—a company with a woman in such a leadership job! It was a very shocking TV program."

Most of the staff had little real idea what to expect, however, since nothing like Ripplewood had ever been seen before in Japan's banking

world. So, as they waited they feared for the worst, but tried to hope for the best; they were ready to give Yashiro a chance.

It did not take long for the shocks to start. A few days after he arrived, Yashiro announced to the staff that he planned to attack two of the most hallowed pillars of the Japanese corporate world: the planning and human resources departments. To build a modern bank, Yashiro believed he needed to change not only the strategy but also the corporate culture. The old LTCB—like almost every other large Japanese company—had been a homogeneous and hierarchical place, where rank and salary was largely decided by age. Bankers had traditionally been assigned to their roles by a centralized human relations department, which rotated the staff every two to three years, creating a culture of generalists. Moreover, the direction of business strategy had been set by a centralized planning department, which created policies based on what the bank wanted to offer—rather than what customers demanded.

Yashiro, backed by the Shinsei investors, wanted to create a flat, decentralized organization, where business development was driven by the needs of customers. So he effectively abolished the corporate planning department and emasculated the human relations department; in the new bank, staff would be appointed to positions on the basis of merit, rather than age, and each department would be encouraged to develop its own team. Then Yashiro attacked two more taboos. Two hundred new specialist outsiders were hired, including Americans, Indians, Chinese, and Koreans, marking the biggest single incursion of "outsiders" that Japanese banks had ever seen. The old rigid boundaries between female clerical clerks—or so-called "office ladies"—and the male bankers were also eliminated. For the first time in any Japanese bank, Yashiro declared, all women would be allowed to apply for managerial jobs, if they wanted. "Just like the television drama!" Tamiwa noted, with awe. She, at least, was impressed. She was doubly amazed when she herself was appointed to a management job a year later; that was something she had never, ever dreamed of seeing in her lifetime.

In the early summer, Yashiro summoned the bank's chief financial controller to his office. He knew he needed an effective flow of information. So a good place to start his reforms was with the data systems.

"Did we make money last month?" he asked the controller, one of the former LTCB bankers who had stayed on at the new Shinsei bank.

"We don't know," the controller replied.

"Why don't you know?"

The controller explained that when the bank was called LTCB it had never attempted to collect profit and loss data on a monthly basis, since it only ever looked at the figures every six months. That was the usual practice in Japan. Since the corporate planning department drew up business plans on a five-*yearly* basis, nobody saw the need for monthly data.

"Can you give me your best guesstimate?" Yashiro asked. A few days later the controller complied, with a number for profits in April.

"What's the confidence level in this number?" Yashiro asked.

"Maybe twenty percent, or thirty percent, up or down," the hapless official replied.

Yashiro was appalled. "We have got to know where we are making money!" he bellowed in frustration. "What products with which customers, how much and what risk we are incurring!"

Then Yashiro tossed the problem over to two senior Indian executives he had just hired to work at Shinsei. Both men already had long experience of managing information systems at banks. Equally importantly, both men had known Yashiro well since his Citigroup days. In the 1990s, the American bank had employed a large number of Indian systems experts in the bank's global operations (a group sometimes called the "Indian mafia"), and Yashiro got on unusually well with these Indians. When word later leaked out that he was recruiting for Shinsei, three of them secretly approached Yashiro. One was Dvivedi—known as "Jay" to his friends—who had run the IT operations for Citigroup in Tokyo, New York, and Singapore. Another was Sajeeve Thomas, former treasurer of Citigroup in Tokyo and latterly head of risk management at the global corporate division. The third was Janak Raj, a skilled operations man who had been working for Citigroup for twenty-five years.

When the Citigroup executives found out that the Indians were planning to desert, they were furious, particularly since the Indians were threatening to take their entire teams as well. Deryck Maughan, the international chairman of Citigroup, called Tim Collins to complain and faxed a list of the men who Yashiro had "poached." "This has got to stop!" Maughan declared. He felt doubly irritated, since back in 1999 Maughan had lobbied on Ripplewood's behalf, to help it buy the bank. Yashiro tartly replied that he was *not* poaching the Indians.

Either way, the talented systems men provided an important boost for Yashiro. He had always preferred to work with respectful acolytes, and his team of Indians offered a level of loyalty that was unusual in the international banking world. "When I worked with Yashiro-san [at Citibank] I realized that he is truly one of the most extraordinary men I have ever met," said Dvivedi, explaining why he had moved across to Shinsei. "He is a very powerful blend of Japanese thinking and American experience—he thinks long term."

Thomas and Dvivedi set to work, trying to put Yashiro's orders into practice. Dvivedi's first task was to get the information technology systems up to speed. In the past, LTCB—like other Japanese banks—had run its IT operations on "mainframe" systems, managed by a closely linked subsidiary of the bank. The computers themselves were always bought from Fujitsu, a traditional borrower from LTCB. The system was fifteen years old and the bank maintained two expensive old computer networks, one of which was used for exchanging data and the other for accounting. The two systems could not talk to each other and could not offer real-time analysis. Worse, customer accounts were processed branch by branch, meaning that there was no central database. "This was the type of system that American banks had twenty years ago," Yashiro declared.

The usual technique to change such a system was to replace an old mainframe with a new one. But as Dvivedi looked at the problem, he developed a grander plan to discard the mainframe *completely*. Indian software developers had recently linked lots of small pieces of software into one large matrix via the Windows operating system. Flexcube, an Indian company partly owned by Citigroup, was at the forefront of this development and Dvivedi believed their system would be cheaper and faster to introduce since much of the work could be subcontracted to Indian software specialists. "In every sense," Dvivedi later explained, "this made more sense."

Dvivedi took over a large "planning space" on the fifth floor of the bank's headquarters and called a meeting to announce his plans to the former LTCB bankers. They were appalled. No large company in Tokyo had ever tried to abandon a mainframe system before, or been bold enough to change an entire computer system in just a few months: the normal time frame for change was *years*. More shocking still, no large bank had hired outsiders to install the systems. The final straw came when Dvivedi coolly told the former LTCB staff that he planned to bring new teams of Indians into the bank. "In the beginning we had lots of problems because the foreigner and Japanese didn't understand each other at all," said Michiyuki Okano, an IT manager at Shinsei.

There was a subtler cultural problem, too. Back in the old days of LTCB, the senior managers had generally not attempted to implement a policy by simply issuing orders. Instead, the usual pattern was to execute policies by *nemawashi*, or the traditional Japanese process whereby a middle manager would create a consensus in an organization *before* implementing any action, by lots of private debate and discussion. This process gave considerable power to middle managers. "In the past what happened was that the senior managers heard our opinion, and then it was presumed to be OK for us to do it," Okano said. "Of course the managers showed the goal for us, but after the former management had shown up this goal, the middle and junior people would create a report based on their discussion, which might be different from what the management thought."

It was now clear that Yashiro had no intention of running Shinsei like a democracy. Nor did Dvivedi. After he received his orders from Yashiro, Dvivedi then issued orders to his staff. Sometimes, to save time, he did this via the Indian subcontractors.

The Japanese dispatched delegations to Yashiro's office to complain. Dvivedi tried to make amends. He convened face-to-face chats with the staff members, in small groups—complete with cookies and chips—to explain his IT dream. Dvivedi hoped that the snacks would help them relax.

The move backfired. Although they were used to going out drinking with colleagues in the evening outside the bank, the former LTCB bankers had never encountered the idea of talking about business while also eating in an *office*. "We are not accustomed to eat such snacks at a business meeting," Hidehiko Arakawa, general manager in the operations department, explained. "Therefore we tend to say 'no' when they are offered. I know foreigners do such things. But it makes us uncomfortable." Then Yashiro started attending some of the meetings himself. That shocked the staff even more than the cookies; senior bank managers had never appeared without warning back in the LTCB days. "Yashiro-san appears everywhere, even when we least expect it!" explained Arakawa. "Sometimes the junior staff will be meeting and Yashiro will suddenly appear, find out what they are talking about, and express his views and agenda on the spot. We have witnessed that several times and it is absolutely amazing—he says things without prior planning!"

The biggest shock of all was the arrival of the Indians. Men such as Arakawa had never traveled outside Japan in their entire life, let alone *worked* with foreigners. But by the autumn of 2000, several hundred Indians were roaming the bank buildings. These Indians spoke little or no Japanese and though the Japanese tried to communicate with them in English, they found it difficult to understand the English the Indians spoke. In an attempt to be friendly, some of the LTCB staff pointed out that their canteen served "curry rice," the Japanese fast-food dish named after "curry" (though it bore little resemblance to the Indian dish). But the Indians refused to eat it. "They thought our curry rice was horrible!" Arakawa explained. "We learnt that they were vegetarian, so they had to be careful about what they ate."

On the fifth floor of the bank headquarters, next to Dvivedi's IT revolution, a second cultural experiment was also under way. This aimed to create a new retail bank and it was a mission particularly dear to Yashiro's heart, given his past triumph at Citibank. During the postwar years, consumers had been encouraged to leave the vast majority of their savings in bank deposits, which paid virtually no interest. And though consumers had briefly become more adventurous in the 1980s, when the stock market crashed, households rushed back to bank deposits, that on average paid a mere 0.03 percent interest a year. "If you put Y1 million into a bank and left it there for a year, at the end you would only have Y340 interest—not even enough for two bus tickets!" Yashiro liked to say. "Consumers are so badly served in Japan, that there is a mass of opportunity!"

The other major Japanese banks, such as Bank of Tokyo Mitsubishi, already had enormous retail banking operations. But LTCB did not have a retail base. Although nearly 200,000 households owned its debentures, they had bought these in an anonymous manner and the bank had no data about clients. Moreover, the former LTCB bankers had never been trained to deal with customers, since most of the male bankers disdained retail banking. "The entrance of the lavish headquarters was more like a mausoleum than a retail bank. [On] my first day at the bank I walked in at three P.M. one day in March through the empty lobby, that vast glass atrium," Thomas later explained. "I thought: Boy, how can you have a bank with an empty lobby?"

And still Yashiro was undeterred. He reasoned that in the age of the internet, physical branches were less important. The other banks were not offering a good service to consumers, no matter what their size. Moreover, he believed that the old LTCB bankers could be *retrained*. So Thomas and Satoru Katayama, a former LTCB manager, assembled a 100-strong team, drawn from the ranks of the old LTCB staff, to act as the basis for a new retail bank workforce. "We wanted people who could think," Thomas explained. "We kept insisting that we wanted women. Initially none of the branch managers wanted to send any women at all, but Yashiro insisted on it. In this country women control a lot of financial decisions."

The bankers were divided into groups, and asked to write down how they thought a retail bank should operate, nominate companies they admired for customer services, and discuss how Shinsei could copy them. One admired model was Starbucks, the American coffee shop chain that had taken Japan by storm in the previous few years. Other popular choices were 7-Eleven, Uniqlo, a Japanese clothing store, and Sony, the electronics group. On the basis of this debate, the bankers then proposed four new themes for the retail bank: Empowerment; A Unique Identity; Accessibility; and Fun.

All of these themes seemed alien to Japanese banks. Traditionally, when customers visited a Japanese bank they were greeted by rows of desks, behind which bankers sat counting money or shuffling forms. Thomas decided to abolish this. He remodeled the branches to look like showrooms, with the branch manager standing at the front of the office to welcome new clients, and hired an American design company, which normally specialized in producing plans for shopping malls, to create new interiors for the bank's branches, and logos.

Then he set to work tackling the hardest task of all—changing the way that the old LTCB bankers operated. "One of our biggest challenges was that people believed that the old rules had to stay in the new business," Thomas said. "Traditionally if you came to the bank and deposited Y2 million, for example, the bank staff would count it, and hand it to someone else at the back who could also count it, and then probably hand it to someone else again. That is OK if you have all day. But we didn't. So we had to change the rules. But how do you tell a general manager who had been here for fifteen years to let someone who has just arrived at the bank receive Y2 million? That was a challenge."

In the investment banking division, there was an even bigger cultural battle under way. Yashiro's corporate strategy for Shinsei was predicated on the assumption that the bank would retain most of the old LTCB lending relationships—which covered some 5,000 companies and 900 financial institutions—and use that to sell more sophisticated, higher margin services. It looked like a brilliant idea on paper, if the bank had three things: a team known as "relationship managers" who could maintain the old corporate relations; a group of bankers familiar with the new financial services, or "product" specialists; and—most important of all—a system that would force both teams to work together, happily.

The bank was already full of people who could act as relationship managers, but there was a shortage of product specialists. The former LTCB bankers who had stayed on to work at Shinsei were overwhelmingly those who had previously worked on the *domestic* wing of the bank and most of those LTCB bankers who understood capital markets had left, since they were attractive "catches" for foreign banks. To fill this gap, the

Shinsei investors hoped to hire product specialists from outside the bank. They knew that they could not hope to attract outside employees to the bank if they offered the traditional Japanese pay system, since salary levels had traditionally been far lower than a Wall Street bank would pay. So early in the process, they decided to create two distinctly different salary systems. One system was used for old LTCB bankers, and offered a job for life but a relatively low salary. The second system, which was used for outsiders, offered short contracts with less job security—but the potential for large remuneration via a bonus, like a Wall Street bank. The first set of employees was known as "Ps" ("permanent staff"); the second "Ms" ("market hires"—though some Japanese sourly labeled these "mercenaries" instead).

Flowers had led the search for suitable investment bankers, offering lucrative pay packages as an incentive. One early catch was Brian Prince, the former head of Lehman Brothers distressed debt team in Tokyo. Prince brought the rest of his team from Lehman Brothers with him. Prince took the leap because of the pay packet and the logic of Ripplewood's arrangement. At an American bank such as Lehman Brothers, it had been difficult to build a large-scale distressed-debt business, because foreigners had access to only a small pool of distressed assets in Japan. Shinsei's web of contacts could potentially yield a significant harvest. Prince then telephoned a friend, Robert Sheehy, a genial American who ran a securitization team at Bear, Stearns. "Why don't you come over?" Prince asked. Sheehy agreed and pulled over his team as well. "The frustration of working at a foreign bank in Japan is that it doesn't have an extensive client list," Sheehy later explained. "Here we have the clients and more balance sheet than a foreign bank would have and we have the technical competence."

With these two teams on board, plus a motley selection of other bankers, Shinsei had the kernel of an investment bank. So the bankers started to sniff around for deals in distressed debt or financial engineering. LTCB's old clients were stuffed with distressed assets that they needed to off-load and many were also keen to find ways to raise funds or sell assets, which made them natural candidates to buy capital market products, particularly as an alternative to regular loans.

Prince and the other senior managers set to work trying to create these

synergies. But it proved fiendishly difficult to get the product specialists and relationship managers to work together. The new design of the bank placed the product specialists on the fourteenth and sixteenth floors of the Shinsei headquarters. But the relationship managers sat on a different floor and the two groups almost never voluntarily visited each other. This partly reflected an ideological gap. To the product specialists, such as Prince and Sheehy, it appeared to be overwhelmingly obvious that Japan needed to move away from indirect finance to direct finance. But the former LTCB bankers had spent their entire careers making corporate loans. They did not understand the new products and did not think their clients really needed them.

There was also a cultural chasm. The relationship managers were mostly Japanese men, who spoke limited English. Prince and some of the other investment bankers spoke limited Japanese. They were used to a brash, aggressive style of working, where bankers debated with each other in an open, frank manner about how to do deals. "All these Americans seemed terribly short-term in their thinking. They just talked about profits and were terribly rude," one Japanese relationship manager later admitted. The distinctions between the pay scales caused added resentment. "It felt like a caste system was developing," one middle-aged Japanese manager grumbled. "At the top were the foreign investors, then the foreign managers at Shinsei, then the Japanese who had been hired from outside, and then us." They were doubly piqued when the bank introduced "swipe cards" to improve security at the bank; though common on Wall Street, it made a mockery of the hallowed idea that companies such as LTCB were "families." "The new investors show they don't trust us. I want to throw away my swipe card," one grumbled. "I hate, hate, *hate* it!"

The Americans found dealing with the Japanese staff equally frustrating and baffling. To them, the former LTCB bankers seemed frustratingly passive and risk-averse. Worse, the former LTCB staff rarely volunteered opinions. For men such as Prince, this was deeply irritating. He was an emotional, passionate man, who had spent much of his career on Wall Street and joined Shinsei because he believed it could offer interesting business opportunities. But day after day, his proposals would be met with just a polite bow; nobody would "bat ideas around" with him. After a few months of working at the bank, Prince noticed that he had become obsessively talkative when he saw his wife in the evenings. It was the only way he could cope with the baffling daytime silences at Shinsei.

In the late spring of 2001, Yashiro was finally ready to open his new retail bank. It seemed a stunning triumph of project management. When Dvivedi had first announced his plans, nobody had believed he could change an IT system in just eight months. But by the spring of 2001, the new system was in place, at a cost of only Y6 billion ($60 million), about a tenth of what Japanese banks usually spent. These dramatic savings came by using the Indian "Flexcube" system and buying cheap computers from the American computer group Dell, instead of using Fujitsu, a "traditional" partner of LTCB. And the switch had gone *so* smoothly that it had even converted some of the former LTCB workers to the idea of reform. "In a typical Japanese corporation," Okano, the IT manager, later recalled, "the idea that you could change something in a month would be impossible. So when we were told things were changing, we could not believe that it could be done that fast! But instead of receiving excuses of why we cannot do it, we got notice up front of when it would happen; division by division we got a list of the dates. When we saw the new PCs arrive on our desks, it was the first real sign for the staff that the new management would be different."

Yashiro's consumer bank also looked impressive. The branches were full of innovative features such as internet banking that allowed consumers to access a whole range of financial services by using a single software program. Although standard in American consumer banks, none of the other Japanese banks were able to provide this service. Better still, the new branches provided tangible evidence of change. In the old days, the 100-foot-high entrance to the LTCB had been as deserted as a mausoleum, decked out in gray walls, glass ceilings, and white marble. The staff was forbidden to enter the building through it, in case they messed up the sense of "order." But by the early summer of 2001 it had turned into a riot of color. The staff had been ordered to use the entrance to create a "buzz" of people, and Thomas's team had placed an enormous Bloomberg terminal in the atrium and a dazzling orange, red, and blue 50-foot picture of a man, reaching triumphantly to the sun. Next to it

stood a banner that summed up the message that Yashiro wanted to proclaim: *Welcome to a whole new world of banking!* A few months later, a Starbucks coffee stall was installed as well as a Yahoo! internet café.

Yet, as Yashiro looked at his new lobby, with its joyous burst of color and life, he did not feel particularly triumphant. On the contrary, although these glossy signs of "success" were striking, they still seemed dangerously cosmetic. Away from the retail bank, a much darker tale had also been unfolding in Shinsei during the first year that could potentially undo everything Yashiro seemed to have achieved.

The same issue that had proved to be the undoing of Onogi and so much of Japan's financial world was still bubbling—what to do about the bad loans.