

## 日本法研究センター

## SUMMARY REPORT

# M&A in Japan: Reenergized

December 4, 2014

**O**n December 4, 2014, a symposium called “M&A in Japan: Reenergized” was held at Columbia Law School (CLS). Mr. Hidemi Moue, CEO of Japan Industrial Partners (JIP), was the first speaker on this panel, sharing his thoughts on the development of Japanese M&A and current trends. Mr. Jonathan Rouner, the head of International M&A of Nomura Securities International, and Professor Curtis J. Milhaupt, the Parker Professor of Comparative Corporate Law and director of the Center for Japanese Legal Studies (CJLS) at CLS, each shared their perspectives on current and future trends for the M&A in Japan. Professor Hugh Patrick, the director of the Center for Japanese Economy and Business (CJEB) at Columbia Business School (CBS), moderated the event.

Mr. Moue initially compared M&A in Japan to that in the United States and Europe, noting that it accounts for a relatively small percentage of GDP. He discussed the reasons behind this, including Japan’s strong organic post-war growth, the regulatory and social environments, and the small number of M&A success stories.



(Left to right) Professor Hugh Patrick, Jonathan Rouner, Hidemi Moue, and Professor Curtis J. Milhaupt



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Despite the current state, Mr. Moue said that potential for change exists. Twenty years of stagnant economic growth, emerging cases of successful turnarounds, and increasing awareness from senior management of the need to change all are contributing to an increase in M&A activity. Further, the aging of Japanese society is pushing institutional investors to seek both better equity returns and improved corporate governance.

Mr. Moue then discussed case studies. He cited Japan Airlines (JAL) as an example of a successful corporate turnaround. He also mentioned Suntory, Takeda, Shiseido, and Lixil as examples of companies in which top management came from outside of the firms, as opposed to the typical practice of promoting top management from within.



Mr. Moue concluded by describing the opportunity for private equity (PE) in Japan. He said that a confluence of factors is creating an opportunity. However, he cautioned that PE funds must be supported by some percentage of domestic investors in order to build better credibility as the asset class develops in Japan.

Mr. Rouner then shared his views. He echoed Mr. Moue's thoughts on the history of domestic M&A, and then focused on the role of outbound acquisitions by Japanese firms. He pointed out that growth in outbound transactions has been concentrated within the past five years, and

cited the need for growth and new technologies, products, and markets as reasons for this trend.



Mr. Rouner noted how many iconic trading concerns such as Mitsui, Mitsubishi, Itochu, Sumitomo, and Marubeni have been very active outbound investors. While in the past these firms focused on acquiring small, minority stakes, more recently they've shifted to buying controlling stakes on a much larger scale. He also mentioned how the government has begun to support M&A through bilateral financing institutions such as the Development Bank of Japan and the Japan Bank for International Cooperation.

Mr. Rouner finished with a description of the elements unique to Japanese M&A. Transaction types are characterized by acquisitions rather than divestitures. Valuation methods tend to focus on intrinsic methodologies and less on market-based approaches. Finally, he emphasized that timing considerations are important because the process for Japanese corporates tends to be lengthier and requires heavier diligence.

Professor Milhaupt commented next. He began by noting that the legal obstacles thought to hinder M&A in the 1990s and early 2000s had been eliminated, but that M&A remains at a comparatively low level in Japan when viewed in the international context. He suggested that complacency by

institutional investors, labor market rigidities, and the poor strategies of some takeover attempts to date may still be dampening the market. Professor Milhaupt predicted that future growth in M&A could result from the need to realize higher returns on equity, a gradual increase in the number of independent directors, and the sheer need for corporations to make use of the trillions of dollars in cash they are holding. He pointed to two recent institutional developments that may be significant: 1) the promulgation of a Stewardship Code for Japanese institutional investors, which encourages active, constructive engagement with corporate management to increase corporate value; and 2) the pending promulgation of a Corporate Governance Code that will require Japanese firms to either have a specified number or percentage of independent directors or to explain why they do not. Finally, Professor Milhaupt lamented the fact that hostile M&A attempts have thus far been unsuccessful in Japan, and suggested that the potential for such transactions (however small) would be healthy for Japanese corporate governance.

### Question and Answer Session

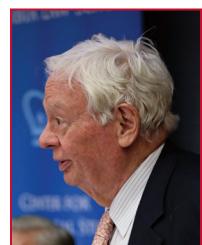


Professor Curtis J. Milhaupt

An audience member opened the Q&A session by inquiring about the difference between M&A and venture capital (VC) activity in Japan. Mr. Moue responded that while PE is tough, VC is even tougher. Though there have been some attempts to induce entrepreneurship, there has not been much success. He emphasized that Japan needs people more willing to take on the risk of starting a new firm.

The next questioner asked how Japanese firms investing abroad manage foreign employees and provide the appropriate incentive structures. Mr. Rouner answered that Japanese corporates focus on well-run companies with strong management already in place. He suggested that, while cultural differences are a hurdle for any global enterprise, differences in organizational cultures are paramount; therefore, successful examples occur when two firms have similar organizational cultures.

An audience member next asked how Japanese firms increase firm value. Mr. Moue responded that he invests for a longer period of time, initially concentrating on the cost structure and then focusing on improving revenue. Professor Patrick offered a follow-on question about how sellers respond to cost cutting by PE buyers and how JIP handles these situations. Mr. Moue said that he evaluates the size of a business and the number of employees necessary; he will only take on the number of people required and will leave the others at the parent company.



Professor Hugh Patrick

Marshall Sonenshine, an adjunct professor at CBS, offered his thoughts and sought commentary. He said that 25 years ago Japanese firms tended

to overpay. However, they have under-participated in M&A over the past 20 years. His thesis was that Japanese firms should “dare to be great” with the cash on their balance sheets; he asked the panelists for their thoughts about this. Mr. Rouner agreed with the thesis and added that firms willing to use their balance sheet are strengthening their position globally, and that other firms in Japan are taking notice. Mr. Moue also agreed that Japan needs outbound M&A due to diminished domestic opportunity. However, he cautioned that firms may still overpay because the decision-making process is bureaucratic and time consuming. Mr. Rouner followed up by saying that sellers desire value, speed, and certainty. Japanese firms may have to increase the price they are willing to pay to offset their slower decision-making process and the uncertainty that results.

An audience member then asked how Japanese firms can become more sophisticated in order to overcome the heavier diligence and longer time frames associated with their M&A process. Mr. Rouner responded that he advises firms to begin earlier in order to compensate. Professor Patrick added that Japanese firms must accept that they are going to embark on an M&A process earlier, and do it before they seek targets. Finally, Mr. Moue confirmed that Mr. Rouner’s comments are in line with the process at JIP. He said that successful cases at his firm have occurred when he has been in touch with a company two years prior to an auction process.

The following question was about the need for outside management and whether a Japanese overlay exists when searching for outside managers. Mr. Moue said that the CEO of Lixil came from GE, the CEO of Suntory from Lawson, and Carlos Ghosn, the CEO of Nissan, from a French auto company. He added that global companies need managers with international experience.

An audience member next enquired about the conservative nature of Japanese society and how it affects outside managers. Mr. Moue responded that, although there may be initial resistance to a change in management style, when positive results start to show, employees become more accepting of change and in fact more motivated by the new management.

The penultimate question came from an audience member who asked where inbound M&A is coming from, given the strengthening dollar. Mr. Rouner replied that U.S. and European companies have a keen interest in Japan. However, many transactions have occurred in distressed situations, such as Nissan.

Professor Patrick concluded the Q&A session by asking Mr. Moue how he funds JIP. Mr. Moue said that the majority of his investors come from outside Japan because domestic investors are still shy when it comes to investing in alternative asset classes.

This event was cosponsored by CJEB and CJLS. Professor Patrick provided closing remarks.

Columbia’s leadership in the field of Japanese law is embodied in the Center for Japanese Legal Studies. The Center initiates and administers a range of research projects, academic exchanges, and informal programs designed to enhance understanding of the Japanese legal system among the Columbia University community and beyond.