Opinion **Inside Business**

Japan Inc wakes up to investor activism in its own backyard

Recent hostile battles show how woefully unprepared companies are for insurgent shareholders

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Kana Inagaki in Tokyo AUGUST 27, 2019

A spate of hostile takeover battles has raised hope among investors that corporate Japan is finally embracing shareholder activism.

But for companies that were spooked by foreign buyout groups, dubbed *hagetaka* (vulture) funds by the domestic media in the early part of the past decade, recent deals show they are facing a new opponent: the once-friendly Japanese corporate owners who have turned belligerent in their pursuit of higher returns and growth.

Last week, travel agency HIS abandoned a hostile takeover of hotel chain operator Unizo Holdings following a white knight counter-offer from SoftBank-owned Fortress. A month before, SoftBank-backed Yahoo Japan ousted the chief executive and three independent directors of stationery supplier Askul, saying it was unhappy with the company's financial performance. In March, Itochu amassed a 40 per cent stake in Descente through a hostile bid, giving the trading house more say in the management of the sportswear group.

The rise in unsolicited offers and proxy fights has coincided with breakthrough private equity deals by the likes of Bain Capital and KKR, which in turn have sparked renewed interest from Third Point, Elliott Management and other activist funds. But it is the emergence of more aggressive domestic acquirers that has convinced longtime investors in Japan such as David Baran, chief executive of Symphony Financial Partners, that the tide has really turned.

"This is about Japanese corporate owners saying I have to grow my business," said Mr Baran.

For decades, big Japanese investors have generally sought to protect the companies they invested in — often due to historical business ties — from outside intervention. When Japanese businesses were targeted in the past by activist funds such as Steel Partners, the investors were criticised for seeking short-term returns rather acting in the interests of the company.

Now, as some large Japanese investors turn combative against businesses that they see as poorly managed, companies face a dilemma. They can defend their management strategy and lament a breakdown of trust with shareholders, but it is no longer acceptable to simply criticise a hostile strategy nor can they rely on sympathy from other investors.

Both the corporate governance code for Japanese companies and the stewardship code for institutional investors call for engagement and pursuit of higher investment returns. Domestic shareholder activism is widely supported by Prime Minister Shinzo Abe, who has bolstered his governance campaign with changes in merger and acquisition and tax rules to make it easier to do all-stock deals.

Still, the way some of these deals have played out shows how woefully unprepared some Japanese companies remain.

Unizo has successfully staved off the hostile takeover approach by HIS, but it may have opened itself up to a bidding war in its search for a white knight. Its top shareholders now include Ichigo Asset Management, a value-focused Japan investor, and activist fund Elliott Management. Having exposed itself as a massively undervalued company with a coveted property portfolio, it is unlikely investors will be satisfied with Fortress's counter offer of ¥4,000 ($38) a share.

A UBS calculation, based on unrealised gains and book value, estimates Unizo has a pre-tax net asset value of closer to ¥10,000. If a bidding war erupts, it is unclear if Unizo will end up in the hands of a friendly shareholder.

In the case of Yahoo Japan's overthrow of Askul's management, the battle could not have turned uglier. The dispute originally stemmed from a clash over the future of their ecommerce joint venture Lohaco, but it quickly became a governance disaster after Yahoo Japan sought not only the removal of the chief executive but also of three external directors. The campaign was widely seen as an improper exercise of power by a controlling shareholder, reinforcing the view that parent-child listings should be eradicated, since the structure is ripe for abuse of minority shareholders and conflict of interests.

As a shareholder with a 45 per cent stake, Yahoo Japan has a legitimate right to seek action to fix Askul's financial performance to increase the company's value, but its implementation was simply misguided.

Masayoshi Son, SoftBank's founder, later waded in, expressing his disapproval at Yahoo Japan's behaviour. But his comments, and subsequent remarks by other SoftBank executives, were uncalled for. They should have stuck to their argument that the campaign was an independent decision made by Yahoo Japan's management, instead of a laboured lament about how parent-child listings are not unique to Japan — a point that, while true, is irrelevant to the debate.

Japanese companies may find it uncomfortable dealing with their newly aggressive domestic investors, but it is a reality that is fortunately here to stay, so they may as well get used to it.

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