

Activism in Japan

As the markets and economy weaken, has activism in Japan run out of road? Or is the country ready for a revival of hostile campaigns?

These days, activists can get either credit or blame for the slightest thing. Last month, the video game company Nintendo launched the latest iteration of its Pokémon game, Pokémon Go, allowing users to hunt for the “pocket monsters” in the real world using their smartphones. Rapid take-up of the new offering and media attention caused the stock to more than double in less than two weeks. At its peak, a major news organisation traced the decision back to Oasis Management, a Hong Kong-based activist hedge fund that has targeted Nintendo in the past and has recommended the development of games for smartphones, in addition to the traditional consoles and PCs.



“Eventually, Nintendo took our ideas on board. Other companies would say no, then implement some of what you asked for.”

Nintendo’s stock price has since come back to earth, shedding around one-fifth of those gains when the company said it expected the financial impact of the game to be limited. With it, perhaps, comes the reputation of **Oasis**, no longer the genius that inspired a worldwide craze, but another investor trying to crack the corporate business practices of a country trying desperately to undergo a revolution in its thinking.

Speaking to Activist Insight Monthly, Oasis’ Seth Fischer admits that activism in Japan has been “hard-going,” and will continue to be until a few examples break the suspicion that activists are no friends of other shareholders, nor able to get through to management. The truth is more nuanced, he argues. “Eventually, Nintendo took our ideas on board. Other companies would say no, then implement some of what you asked for.”

Activism has been slow to take root in Japan, despite seemingly attracting

more attention than any country outside of the US in recent years. This year, the number of companies facing activist demands broke into double figures for the first time. As of July 29, 13 companies had been publicly targeted in 2016, compared to eight in each of 2014 and 2015. For a sense of perspective, somewhere between 21 and 29 companies are targeted each year in the UK, and last year 410 US companies faced some sort of public demand.

Given that much activism in Japan is conducted behind the scenes, the broader trend may be more impressive, however. Corinna Arnold, Head of **RWC’s** Japan Focus Fund, says the number of potential investments in the pipeline has grown by a factor of five in recent years.

Excitement about activism in Japan has been stoked by the embracing of shareholder value as a concept for the rebooting of Japan’s lagging economy.

Shinzo Abe’s second stint as Prime Minister, which began in 2012, has seen the launch of a stewardship code, governance code, and special index for high-return stocks, as well as monetary easing and fiscal stimulus. Between his election victory in December 2012 and last August’s peak, the Nikkei 225 Index had rallied more than 110%.

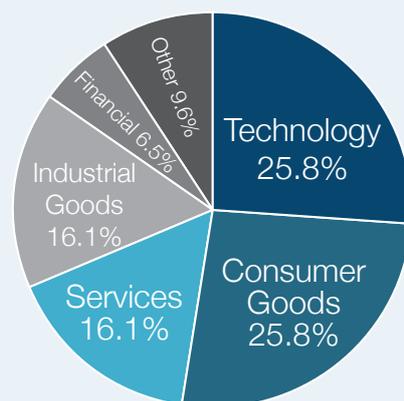
More recently, the economy has slowed and the index is down by 18% in 12 months, but Abe is still winning elections, and governance reforms promoted both by his administration and industry groups are taking effect. According to proxy voting adviser Institutional Shareholder Services (ISS), 83% of the Japanese companies it covers have appointed two external directors, up from 55% a year ago. “All-insider boards, still common until only a few years ago, are on the brink of extinction,” ISS said in a recent bulletin.

That new blood is leading many activists to believe boards will become

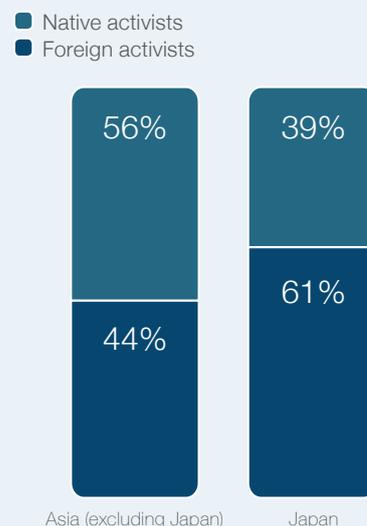
Companies publicly subjected to activist demands by year



Sector breakdown** of Japanese companies publicly subjected to activist demands since 2013



Companies targeted by native and foreign activists since 2013



N.B. All data exclude activist short positions unless otherwise specified
 * All percentages are given to one decimal place, and may cause rounding errors
 ** YTD figures as of 31/07/2016 unless otherwise specified

“As companies appoint more and more outside directors, it will change the nature of discussions in the boardroom.”

more open to different ways of creating value. Marc Goldstein, a researcher at ISS who has watched Japanese companies for years, argues, “As companies appoint more and more outside directors, it will change the nature of discussions in the boardroom.” One outside director can be silenced, he says, “But three or four can make much more of a difference.”

“Activist investments have been increasing and will continue to do so for another decade.”

Perhaps as a result of these tailwinds, governance-related activism accounts for one-fifth of activist demands over the past three-and-a-half years. Yet it remains dwarfed by balance-sheet activism, which often involves greater payouts, at an average of 43% of demands. M&A activism, including breakups and straightforward consolidation, has been reduced to little more than one case a year.

That may change in future, however. Companies may become vulnerable to de-listing, bankruptcy or takeovers now that the Abe government is explicitly withdrawing a hitherto implicit bailout promise, argues Arnold. A big difference could then open up between leaders and laggards, creating opportunities both for more short-term and more long-term investors than RWC, which typically works with companies for a few years.

Strategic Capital, a Tokyo-based investment manager that traces its roots back to M&A Consulting, an activist investor founded in the early 1990s, points to another path. It has targeted several companies with large controlling shareholders over the years. In one recent case, **INES**, the parent, had sold down its stake, so Strategic called for its representatives on the board to be replaced and for real estate to be sold to fund a buyback. The company listened, it says, and the activist made a killing. In another scenario, the parent wasn't willing to let the activist dictate to its subsidiary, so bought Strategic's shares.

The pace of change has disappointed some, however, including Hitoshi Sugibuchi, who runs an activist advisory practice at **Sessa Partners**. “Activist investments have been increasing and will continue to do so for another decade,” he says. But they will also grow more slowly than many expected. “People expected faster change thanks to the corporate governance code,” he adds. “A year on, that big story hasn't happened yet.”

In part, this is because activism is seen as a predominantly Western phenomenon. Since, 61% of the companies publicly targeted by activists have found themselves faced with foreign investors. Activism took a knock in 2013, when Sony rebuffed New York-based hedge fund **Third Point Partners'** calls for a breakup. Ever since, Third Point's demands have been more modest, but also more successful—greater transparency and some buybacks at **FANUC**, a robotics company—and a call for a succession plan at **Seven & i**, which might have been helped by the situation within the board room.

Japanese activists do exist, however, and are starting to get livelier.

Strategic Capital told *Activist Insight Monthly* that it considers itself “the only real activist” to be based in Japan, noting that others are largely “engagement” funds that look for friendly management teams before they start their due diligence. That is a slight exaggeration. **Effissimo Capital**, another fund founded by former M&A Consulting stalwarts, is said to be tough behind closed doors, while M&A Consulting's founder, **Yoshiaki Murakami**, made a comeback recently with a proxy contest at **Kuroda Electric**, in which he was defeated. In a sign of how popular activists are, however, both are based in Singapore.

Even Fischer puts Oasis no higher than a six on a sliding scale of aggression, with ten a full blown proxy fight. He has done lots in the engagement mould, he hastens to add, but is unsure shareholders would be willing to back him in a contest. “We've generally asked for reasonable things. In some situations, companies have performed defensive manoeuvres and hurt themselves, and we've sold and moved on.”

Something similar could continue to be the norm in Japan, with its fitful attempts at reform. Activism may remain in a limbo between an openly accepted part of financial markets with its attendant proxy fights, and a softer, suggestive, approach. Most believe there will be a broad range of interactions, and there are signs of an uptick in dissident solicitations. Until that becomes fully realized, it will be up to the descendants of Murakami to fly the flag. [👉](#)



Cultivate your expertise

Activist Insight Monthly

The only online magazine dedicated to shareholder activism

Sign up for a free trial here



Activist Insight

www.activistinsight.com