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Activist proposals winning support of mainstream shareholders in Japan

- Individual activist proposal wins 48% of vote at Mizuho's AGM
- Activist proposal wins supports if it enhances corporate value
- After codes, activists winning ISS, overseas investor supports

After the adoption of Japan's Stewardship Code, activist shareholders have seen increased support when their proposals are viewed as enhancing corporate value by mainstream shareholders, investors and corporate governance specialists said.

Critics have long argued that overseas and Japanese activist investors have been short term-oriented and acting solely in self-interested motives. This meant their proposals typically failed to gain the support of mainstream shareholders.

But during this year's AGM season, a number of activist shareholders' proposals were broadly supported by mainstream investors. Mitsutaka Yamaguchi's victory at **Mizuho Financial Group's** [TYO: 8411] AGM is the strongest signal yet that activists are becoming agents of change in Japan.

Yamaguchi, an individual activist shareholder, won 48% of the votes for his proposal to amend the articles to restore shareholder authority to vote on income allocation and submit proposals related to income allocation at Mizuho. The vote in favor of the proposal submitted by Yamaguchi with a stake of only 30,000 shares or 0.0001% of Mizuho's outstanding common shares, increased from the previous year's 41%.

"This is a milestone [for activist investors]. Mizuho has no choice but to change its articles next year," said Tsuyoshi Maruki, CEO of Tokyo-based activist **Strategic Capital**. "The company cannot dismiss a proposal with broad shareholder support even if it comes from a small stakeholder," said another institutional investor.

At a 15 June AGM held by **Chori** [TYO: 8014], a leading Japanese textile and chemical company, in which **Toray Industries** [TYO: 3402] holds a 51.2% stake, Strategic Capital won 24.69% of the vote for a similar proposal.

This is also significant because more than a majority of Chori's overseas, trust bank and individual shareholders, outside Toray and its business partners, supported Strategic Capital's proposal. As much as 70% of Chori is owned by so-called stable shareholders -- Toray and the companies with business ties to Chori, according to a company handbook.

In the wake of the adoption of the Stewardship Code, institutional investors are more likely to evaluate shareholder proposals from the standpoint of whether the proposal is beneficial to shareholders instead of judging it based on the identity of the party from whom it originated, said Kengo Nishiyama, research analyst at Nomura Securities.

On top of that, institutional investors are now more likely to be asked to explain why they voted for or against a given shareholder resolution, Nishiyama added.

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In Japan, companies are allowed to stipulate in articles that the board is authorized to determine income allocation without shareholder approval, provided that such article amendments are approved by shareholders.

Mizuho and Chori's articles allow their respective boards to determine the allocation of income and prohibit shareholder proposals on this topic, according to the two companies' articles.

However, if activists' proposals are broadly supported by other shareholders, the companies cannot dismiss the proposals on the grounds that the activists are acting solely in their own self interest, said Nishiyama.

These changes Japan is witnessing have already been occurring overseas, said Michael Davis of Davis Polk & Wardwell. He said passive institutional investors have started taking the Stewardship Code more seriously and a lot more of the activist side recently.

"Institutional shareholders are looking for activists who would work for them because they don't want to be involved in messy public activist campaigns," said Davis. "That is a big change and we have started seeing a lot of successes of activist campaigns," he said, citing the example of activist Nelson Peltz's involvement in **DuPont** [NYSE: DD].

Maruki said Chori is changing; the activist has now been able to have dialogues with Chori's CEO, and Chori board members have started visiting Maruki's office.

The major stumbling block is a parent-subsidary relationship between Toray and Chori, he said. Indeed, institutional investors have been criticizing the Stewardship Code as it has failed to stipulate the right of subsidiary shareholders to carry out dialogues with parent companies' board members.

To this end, Maruki sent a letter earlier this year to the Financial Services Agency's Stewardship Follow-up Committee addressing the need to add a new clause to the code that parent companies' management must carry out dialogues with shareholders of their subsidiaries.

Meanwhile, a spokesperson at Mizuho said: "We are aware that one of the shareholder proposals received strong support from other shareholders at the AGM. The vote in favor of the proposal was indeed significant, but we have not yet taken any steps in response to the result."

A spokesperson at Chori also said the reason for authorizing the board to determine dividends is to keep flexibility in its capital strategies. Chori has been deciding on the dividends it considers appropriate, taking into account shareholder returns as well as managerial and financial stability, the spokesperson said.

Institutional Shareholders Services said in its report that the proxy advisor sees no particular benefit to shareholders in giving the board such discretion to determine income allocation. The fact that the board of Chori is management-dominated, with

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only two independent directors, raises concern that such a board may not look after shareholder interests.

“I was really surprised. In the past, everybody ignored my proposals. Because of cross-shareholdings, I think my proposal won about 90% of the votes of ordinary shareholders at Mizuho, especially those overseas. Yes, Japan’s adoption of the codes has an impact,” said Yamaguchi.

by Norie Hata in Tokyo

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