



### SHAKING THINGS UP - JAPANANESE STYLE?

For the last 14 years I have been hoping that there might be a significant change in the way Japanese business culture works. It has been a frustrating 14 years because there has been the odd glimmer of hope (particularly around the time of the Koizumi administration) but at the end of the day very few of the changes that I think are necessary to create a dynamic economy and stock-market, have occurred.

Last September part of me began to think that the election of a new DPJ (Democratic Party of Japan) government might be the catalyst for a new beginning.

The new Prime Minister Hatoyama proposed some pretty radical changes. In particular he said that he was going to take on the bureaucrats, the real rulers of Japan. He also talked about defining a new independent foreign policy but the one thing he did not and has not tackled is the “Keiretsu” system.

In all my opinion pieces that concentrate on Japan I do not think I have used the term “Keiretsu” but in reality it is a one word summary for all the things that I think are wrong about Japan. It is a word that summarises all the problems I have described at the large companies at the heart of the economy like Hitachi, Konica Minolta and in particular Asahi Chemical. (Opinion pieces 1 and 7).

As long as “Keiretsu” like companies remain the dominant force at the heart of the economy I remain convinced that Japan is condemning itself to remain a laggard.

This chart of the Nikkei shows just how much of a laggard the Japanese market has been in recent years.



Hatoyama appears to associate Western style capitalism with the cowboy capitalism of Enron, Lehman, Worldcom and AIG (dare I add Anglo!). He does not appear to

acknowledge that it also creates companies like Google, Cisco, Coca Cola, Johnson & Johnson etc.

I would love to be able to take the best of both systems and blend them into a dynamic ethical capitalism but I do not get the impression that the DPJ share this dream. They seem to see the credit crisis as a vindication that their system is better. I am therefore reconciled to the idea that Japan is not going to change in the way I hope for the foreseeable future.



Prime Minister Hatoyama

There are investors that still like the Japanese stock-market even if they think the economy will remain problematic. These investors are usually attracted by the cheapness of the market.

There is no doubt that Japan is cheap on a tangible asset basis. There are plenty of companies with lots of cash, buildings and machinery that sell for less than the value of those assets. This is fairly rare in the rest of the world. It is the reason why companies like Steel Partners went into the Japanese market and it is the main reason why I bought a small position a couple of years ago.

This time last year I wrote about Warren Liechtenstein / Steel Partners and their attempts to unlock that value (Opinion piece 42). They have continued to soldier on despite the setbacks I wrote about.

I am disappointed to have to write that their attempt this year to unlock value at Sapporo Holdings has suffered a major setback. They appear to have done everything right in their attempt to shake up the board of Sapporo. First of all they found Japanese nationals with a background in the food and beverage industry willing to become new directors. Secondly, they managed to get the support of corporate governance consultancy firms like Riskmetrics. Thirdly, they published detailed research on their reasons why they were unhappy with existing management and finally they held public meetings in order to explain their views. Despite all of this they only managed to get 30% support for their proposals and this is in a company 32% owned by foreigners! (You can read the full details at: [www.spjsf.weblogs.jp/en](http://www.spjsf.weblogs.jp/en)) This vote tells me that the Japanese ruling classes have not changed and are still not convinced of the need to use scarce capital wisely. A 70% vote in favour of existing management at Sapporo suggests that all Japanese banks, insurance companies, fund managers and individuals voted against change. They voted for the status quo and I am convinced that this is at the heart of Japan's problem.

Steel Partners say they have not given up yet. (There are other activist investors like TCI that do appear to have given up on Japan). As I mentioned last year I hope they continue to battle on and I wish them the very best of luck but it is a frustrating process.

If Warren / Steel had succeeded at Sapporo I would have seriously considered putting more money into the Japanese market. The fact they failed leaves me in a dilemma. If the market was not so cheap I would definitely sell my small position but the cheapness makes me feel that I will wait until I need the money for something else.