Chambers
Global Practice Guides

Definitive global law guides offering
comparative analysis from top-ranked lawyers

# Private Equity 2021

Japan: Trends & Developments
Shuichi Nishimura and Yasuhiro Kasahara
Nagashima Ohno & Tsunematsu

practiceguides.chambers.com

# Trends and Developments

***Contributed by:***
*Shuichi Nishimura and Yasuhiro Kasahara*
***Nagashima Ohno & Tsunematsu** *** ***see p.6***

## Investment Deal Trends

The private equity market in Japan was very active in 2020, despite the negative impact of COVID-19. M&A activities decreased significantly during the period of the first State of Emergency declared in Japan for COVID-19, from April 2020 to May 2020, including within the private equity market, but the market recovered rapidly after the lifting of this first State of Emergency on 25 May 2020. It is reported that the number of private equity deals for 2020 set a new record. However, the total value of all deals in 2018 remains the highest, as 2020 did not contain any mega-deals like those that occurred in 2018, such as the USD20 billion acquisition of Toshiba Memory Corporation by Bain Capital and its co-investors.

That is not to say that there were no sizeable deals in 2019. Large deals in 2019 include the following:

- the acquisition of Showa Aircraft Industry Co., Ltd. by Bain Capital in March 2020 (reported transaction value approximately JPY83 billion to JPY85 billion);
- the acquisition of Mamezou Holdings Corporation by Integral Partners in March 2020 (MBO) (approximately JPY34 billion);
- the acquisition of Sogo Medical Co., Ltd. by Polaris Capital Group in March 2020 (MBO) (approximately JPY76 billion);
- the acquisition of UNIZO Holdings Company, Limited by Lone Star Funds in April 2020 (employee buyout) (approximately JPY200 billon);
- the acquisition of Nichiigakkan Co., Ltd. by Bain Capital in August 2020 (MBO) (approximately JPY100 billion); and
- the acquisition of Kirindo Co., Ltd. by Bain Capital in November 2020 (MBO) (approximately JPY28 billion).

It is notable that there were at least four MBO transactions involving investments by private equity funds in 2020, and this is reported to be the highest number in the last ten years. Also, there were more hostile takeover deals in 2020 compared to previous years (please see below regarding hostile takeovers). Those trends are expected to continue in 2021.

### *The secondary market and public-to-private transactions*

The number of public-to-private (P2P) deals recovered in 2020, with 11 cases, which is comparable to 2016 and 2017 when there were ten P2P deals in each year. It is likely that 2021 will see the same level of P2P deals, some of which may be due to the reform of various market segments by the Tokyo Stock Exchange (TSE), starting from April 2022. TSE has announced that tighter requirements will be applied for companies to remain in the most prestigious market, called the Prime Market, which is equivalent to the current First Section Market. Such tighter requirements include maintaining a certain minimum level of market capital (at least JPY10 billion) as well as a sufficient number of tradable shares (at least 35% of the shares in the company need to be tradable shares). Due to these tighter requirements, some public companies may choose to become private companies, which in turn may involve investments by private equity firms.

There was also increased activity in the secondary market, in which one private equity firm sold its portfolio company(ies) to another in 2020. This trend continues in 2021.

### *Looking forward in 2021*

Surprisingly, COVID-19 did not have any significant long-term negative impact on investments by private equity firms in 2020 and, after an initial drop, stock prices rapidly recovered to levels that were actually higher than those before the pandemic. At least the same level of investment activities by private equity firms is expected in 2021.

## Exit Trends

In recent times, there have been approximately 40 to 50 deals per year in which a private equity fund or investor exits their investment (exit deals), but it is reported that the number of exit deals in 2020 was well below this recent average. This drop may be related to COVID-19 which, in particular, caused delays in the exit process during the period of the first State of Emergency for COVID-19 (April to May 2020). Given that business activities have recovered to almost the same level as the pre-COVID-19 period, the number of exit deals in 2021 is expected to return to the recent historical average range. It is notable that, despite the decrease in exit deals, there were five IPO exit deals in 2020, compared to three IPO exit deals in 2019. If the stock market continues to be strong, there should be at least the same level of IPO exit deals in 2021 as compared to 2020.

## Recent Amendments to the Foreign Exchange and Foreign Trade Act

Recent amendments to the Foreign Exchange and Foreign Trade Act (FEFTA) have tightened the rules applicable to foreign direct investments to align Japan with the global trend towards strengthening the regulation of foreign investors.

Under FEFTA, when foreign investors (including foreign-based private equity firms) seek to perform certain acts, such as the acquisition of shares in Japanese companies engaged in designated industries, they must file an advance notification to the relevant Japanese Ministry(ies) and wait for the 30-day processing period (which is often shortened to two weeks but may be extended to up to five months in very exceptional cases) to elapse before performing such act.

### *FEFTA amendment*

An FEFTA amendment that came into effect on 1 August 2019 expanded the scope of designated industries by adding certain sectors in the information and communication technology and software development industries. Due to this amendment, the number of transactions requiring a prior notification has significantly increased, including investments into tech start-ups.

A subsequent amendment added certain types of actions that trigger an obligation for foreign-based private equity firms to submit prior notifications to the specified government authority, such as making an affirmative vote to elect a foreign investor (including a foreign-based private equity firm) or its affiliated person as an officer of a Japanese company in the designated industry or proposing the transfer or abolishment of the business in a designated industry.

### *Pre-deal examinations*

Private equity firms doing deals in Japan should carefully examine whether a company in which it contemplates investing is engaged in any of the designated industries, bearing in mind that such examination may require some time as the classification of the designated industries is not always clear. As mentioned above, the statutory waiting period is generally 30 days, but in practice there is some uncertainty as to whether allowing 30 days for the processing period is sufficient, and a longer period may be required.

After filing such notification, questions from the authority may be anticipated in the examination process, and the 30-day period may elapse before the examination is completed if answers are not provided on a timely basis. In some cases, conditions may be attached by the specified Ministry in relation to a contemplated foreign investment. In these cases, a revised notification may be required to be filed that includes a declaration that the foreign investor will comply with such conditions. In these cases, the 30-day waiting period starts again from the date of filing of the revised notification.

## Fair M&A Guidelines

The "Fair M&A Guidelines: Enhancing Corporate Value and Securing Shareholders' Interests" issued by the Ministry of Economy, Trade and Industry (METI) have influenced M&A practices.

These Guidelines focus on MBOs and the acquisition of controlled companies by controlling shareholders where conflicts of interest and information asymmetries between the buyer and minority shareholders typically exist. The Guidelines stipulate a variety of measures that should be taken by the target company and the acquirer to ensure fairness in these types of transactions, including:

- the establishment of a special committee to assess the valuation and the process of the transaction;
- the retention of independent external advisers;
- requiring market checks (ensuring potential investment opportunities by third parties);
- imposing majority-of-minority conditions; and
- requiring information disclosure.

Although the Guidelines state which fairness-ensuring measures should be taken on a case-by-case basis, and to what extent, it should be noted that the Guidelines emphasise the importance of the special committee in ensuring the fairness of the transaction.

The purpose of these Guidelines is to encourage best practice and, although they are not legally binding, the Guidelines have influenced the MBO practice since their publication. In particular, following the publication of these Guidelines, there is a trend of such special committees becoming more deeply and actively involved at an earlier stage of MBO transactions. It is becoming common to establish a special committee not only in MBOs and the acquisition of controlled companies by their controlling shareholders but also in other public transactions involving squeeze-outs that are not directly covered by the Guidelines.

## Hostile Takeovers

Hostile acquisitions have long been considered taboo in Japan. However, there were a few notable hostile transactions in 2019 and 2020, in which reputable large Japanese companies commenced tender offers without prior agreement with the target companies, some of which ended successfully for the acquirer. The number of hostile transactions is expected to continue to rise in Japan.

Although there has not been any recent transaction where a private equity fund attempted to acquire a target company against the wishes of the target company's management, this trend of increasing numbers of hostile takeovers has greatly affected investments by private equity funds. For example, in 2019, a tender offer launched by Bain Capital against KOSAIDO was blocked by a hostile tender offer by Minami Aoyama Fudosan and Reno, which are associated with a prominent Japanese activist shareholder, Mr Yoshiaki Murakami. Similarly, in 2020, Carlyle Group withdrew its tender offer to acquire Japan Asia Group due to a tender offer at a higher price being launched by City Index Eleventh, backed by Mr Murakami.

In conclusion, together with carefully considering the influence of the Guidelines, any takeover process should be conducted cautiously, with the understanding that deal certainty may be threatened by subsequent tender offers.

**Nagashima Ohno & Tsunematsu** is the first integrated full-service law firm in Japan and one of the foremost providers of international and commercial legal services based in Tokyo. The firm's overseas network includes offices in New York, Singapore, Bangkok, Ho Chi Minh City, Hanoi and Shanghai, associated local law firms in Beijing and collaborative relationships with prominent local law firms in many other jurisdictions. In representing leading domestic and international clients, the firm has successfully structured and negotiated many of the largest and most significant corporate, finance and real estate transactions related to Japan. In addition to its capabilities spanning key commercial areas, the firm is known for handling ground-breaking domestic and cross-border risk management/corporate governance cases and large-scale corporate reorganisations. The firm has approximately 500 lawyers, who work together in customised teams to provide clients with the expertise and experience specifically required for each client matter.

## AUTHORS

**Shuichi Nishimura** is a partner at Nagashima Ohno & Tsunematsu. His main areas of practice are cross-border and domestic M&A, private equity and general corporate. He has vast experience on complex M&A transactions, serving both private equity firms and corporate clients. He graduated with an LLB from Waseda University in 2004 and with an LLM from the University of Southern California Gould School of Law in 2011. He is an Adjunct Lecturer at Aoyama Gakuin University Graduate School of Law.

**Yasuhiro Kasahara** is a partner at Nagashima Ohno & Tsunematsu. His main areas of practice are cross-border and domestic M&A, private equity, joint ventures and other corporate transactions. He has extensive experience in North, Central and South American matters. He graduated with an LLB from the University of Tokyo in 2005 and with an LLM from Columbia Law School in 2012. He worked at Nagashima Ohno & Tsunematsu NY LLP from 2012 to 2014, and has been a Visiting Associate Professor at the University of Tokyo School of Law since 2019.


### Nagashima Ohno & Tsunematsu

JP Tower
2-7-2 Marunouchi
Chiyoda-ku
Tokyo
100-7036
Japan

Tel: +81 3 6889 7000
Fax: +81 3 6889 8000
Email: yasuhiro_kasahara@noandt.com
Web: www.noandt.com