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Establishing contacts without loss of face

The acquisition of a company in itself is a complex and extensive process. However, if the acquisition takes place in another country and cultural differences make matters worse, the right approach is even more important.

By Dr. Ralf Mayer --- Many managers without experience in Japan will wonder if M&A transactions are taking place or are even possible in the Land of the Rising Sun. Often, the media-effective takeovers by Japanese companies abroad are known, such as the acquisition of Sprint by Japan's Softbank or Toll Group by the Japan Post. On the other hand, acquisitions of Japanese companies by overseas investors are rarely recognized, and only the purchase of Sharp by Hon Hai Precision Industry is likely to be remembered by many. However, contrary to the first impressions, the M&A market in Japan is very active and, according to Thomson Reuters, had about 3,600 transactions announced in 2017. By comparison, in Germany about 2,350 takeovers were announced during the same period. However, there is one crucial difference: while well over 850 transactions in Germany were made by foreign investors, the number of announced "inbound" transactions to Japan was well below 200. The question therefore arises as to why the country seems so difficult for foreign investors

Entrance gate to Asian markets

Out of a variety of reasons why to invest in a firm abroad, growth potential, developing new markets, and access to technology and innovation are certainly among the most important. At first glance, Japan's overall economic situation does not seem to be very attractive in this respect: Japan's GDP is growing slowly, if at all, and prices are rising moderately at best. However, one has to keep in mind that GDP remains stable despite a shrinking workforce, which is reflected in a rise of GDP per capita. In addition, Japan's consumers are eager to consume, have a high purchasing power and love high-quality (and high-priced) products. Moreover, the size of the market with 127 million consumers should not be ignored: Japan, for example, is the second largest cosmetics market in the world.

Also, in terms of technology development and innovation, Japan is in the lead in many areas. Robotics, battery technology, and iPS stem cell research are just some of the areas where Japanese companies and universities are at the forefront of development. Acquisitions in these areas can significantly enrich one's own technology development and fill the innovation pipeline, also with regard to the home market. Likewise, the acquisition of a Japanese firm brings a significant improvement in market access, including additional markets all over Asia where Japanese companies are very active.

Build long term trust

As described above, there is quite a lot of M&A activity in Japan. However, this is mainly characterized by intra-Japanese transactions. Two cultural differences from the Western world in particular can serve as an explanation for this. On one hand, profit is not the most important business goal. The well-being of customers and, in particular, of employees, has a much higher priority. On the other hand, the way of building trust as a necessary basis for a successful business relationship is quite different: While in the western world trust is predominantly formed over common intentions, goals and ultimately contracts, in Japan confidence arises almost exclusively through relationship, thus mutually knowing each other. In addition, a divestment is still subject to the stigma of "failure" or "loss of face".
As a result, Japanese companies often acquire foreign firms, but they rarely adjust their own portfolio. And if so, companies are searching for a suitable buyer in their own network, that continues the company for the benefit of employees and customers. The commissioning of an investment bank and divestiture to the highest bidder will take place only in exceptional cases.

First approach via a consultant

However, this also gives opportunities for German companies in particular to present themselves as a suitable buyer. Much of what is important to the Japanese company is also practiced in Germany. For example, many takeovers involve an employment guarantee that excludes operational layoffs for a period of time. Japanese and German labor law are very similar in terms of protection against dismissal and German companies are usually following a long-term strategic goal with company takeovers. For German companies, it should therefore be no problem to accept the corresponding expectations and wishes of Japanese companies. In addition, Germans and German companies enjoy a very good reputation in Japan, which also positively supports their attractiveness as a potential buyer.
With regard to trust, however, only long-term oriented strategy leads to success. Realized takeovers of the recent past show again and again a comparable pattern in the approach:

1. Establishment of contact and start of cooperation
2. First financial, possibly joint investments (purchase of shares, JV)
3. Purchase of further shares and finally acquisition or merger

Examples are Bosch Group (since 1939 cooperation with Zexel, then increase of the number of shares to 30.1% and finally to 50.1% in 1999), Böhringer-Ingelheim (strategic alliance with SS Pharmaceuticals since 1982, acquisition of 9.6% of Shares in 1996, then incremental purchase of further shares to 50.1% until 2001 and full takeover in 2010), as well as the acquisition of Chugai by Roche.

For the first approach as well as for establishing a contact, it is advisable to choose an indirect route via a consultant. This is especially important for companies that do not have a branch office in Japan, as the Japanese appreciate having a contact person ("Madoguchi") located in Japan. In addition, a consultant can help with the selection of possible acquisition objects. Moreover, an intermediary offers the advantage of an anonymous approach as well as the ability to mediate indirectly between the parties, whereby desires, expectations and even disagreements can be communicated without loss of face. The latter are advantages that should also be considered by companies that are already present in Japan. Of course,

the first contact should not take place under the sign of an acquisition, but with the desire of the cooperation, for example, to market Japanese products in Europe (and vice versa) or to jointly develop new products. Once this step has been taken, the others are usually self-evident, such as the acquisition of shares, a joint venture or joint production facilities. Once you have "positioned yourself" that way and established a trustful relationship, a later takeover becomes possible.
A word on hostile takeovers: These are almost impossible in Japan due to the financial interconnectedness of the companies among themselves (so-called "keiretsu"). In addition, there is a special feature in Japanese company law that allows a very large number of "authorized but not issued" shares. These can amount up to three times of the already issued shares. Since these shares are already approved for issue but are still in the possession of the company, the management can sell these in principle "overnight" to a White Knight as a defense measure - and a Japanese White Knight is always found.

Perseverance is necessary
M&A in Japan is possible – if one considers the cultural peculiarities of the country! In particular German companies, which enjoy a high reputation in Japan and have no problem with employment guarantees in a takeover because of similar practice in Germany, can thus expand their presence in Japan and Asia and develop new distribution channels and markets. However, an acquisition in Japan must be part of the long-term strategy and needs time and perseverance.

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