### State Intervention and Private Enterprise: Japan, the U.S., and China

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#### Introduction



#### Kazuhiko Toyama

#### **CEO and Representative Director of IGPI**

<Former COO, Industrial Revitalization Corporation Japan, Inc. (IRCJ)>

Graduated from the University of Tokyo (BA in Law) in 1985. Passed the national bar examination in 1984. Joined the Boston Consulting Group in 1985. In 1986, joined establishment of Corporate Directions, Inc. and assumed an executive role of overseeing operations including strategic planning, development of client service concepts, implementations and monitoring, etc., for a wide range of industries. Graduated from MBA and Public Management Program at Stanford University in 1992.

In 2001, became CEO of Corporate Directions, Inc. Actively led revitalization planning and implementations ranging from large-scale failure cases to medium-sized ones. In April 2003 appointed as Executive Managing Director and COO of Industrial Revitalization Corporation of Japan, a government-backed restructuring fund, whose primary mission was to facilitate coherent revitalization of industrial and financial sectors as well as promote the development of business restructuring market in Japan. In 2007, established Industrial Growth Platform, Inc. which aims to support our clients to achieve long-term and sustainable enhancement of enterprise value.

Services also Expert Member of Council on Economic Fiscal Policy (MOF), Member of The Tax Commission(CAO), Vice Chairman (Executive Director) of Japan Association of Corporate Executives.

#### 3. Industrial Revitalization Corp. of Japan ("IRCJ") - ¥ 10 Tri. (US\$110billion) Japan's SWF



【Koizumi Initiative for Revitalization of Japan】

Mr. Jun-ichiro Koizumi

Prime Minister and the Head of Cabinet Office

#### Dr. Heizo Takenaka

Minister of State for Economic and Fiscal Policy Minister of State for Financial Policy Minister of State for Privatization of the Postal Services

#### Mr. Sadakazu Tanigaki

Minister of Finance Minister of State for IRCJ

Mr. Shoichi Nakagawa Mr. Toshihiro Nikai Mr. Akira Amari Minister of Economy, Trade and Industry

**Business Consultants** Investment Bankers Accountants Lawyers **CEOs** Government Officials

### IRCJ

Organization to Complete the Policy's Mission Industrial Revitalization and Return On Investment "

- Investment capacity: ¥10 Tri for debt purchase ,lending and equity injection
- Duration: 4 years (Planned: 5 years) April 2003 – March 2007
- 200 Professionals
- Result: Invested to 41 companies (disposed about 4 Trillion Yen (book value) NPLs) Profit: 120 Billion Yen

Daiei Kanebo Kanebo Cosmetics Misawa Homes Usui Department Store Phenix Co., Ltd. Kyushu Industrial Transportation Kvushu Industrial Transportation Logis. Kanto Jidosha Dia Kensetsu Matsuya Denki Meisei Shokai Tsu Matsubishi Mitsui Mining Yagami Shoji Fujiyugyo Osaka Marubiru Kimmon Manufacturing Kinugawa Grand Hotel Fre' c Okawaso Taiho Industries Shikisai Hotel Miyano Machinery

Skynet Asia Airways Amex Kyohan Toshigi Hikaku OCC Corporation Hattori Gangu Shoren Corporation Daikvo Incorporated Sankei Asaya Hotel Kinsei Tanakava Tamano Consultants Aviva Japan Ogura Co., Ltd. Kinugawa Onsen Mivazaki Kotsu Okunikko Konishi Hotel Kanaya Hotel Kanko Kamava Rvokan

# **Three Types of State Intervention**



	Type① Privatization	Type② SWF	Type③ Government-owned Fund			
Public Sector	Entity/ State-owned enterprise	SWF	Government owned fund			
	Privatization Investment Investment					
Private Sector	Private Company <u>Japan Post</u>	Private company/ securities, etc. GIC, CIC	Private company  IRCJ, TARP			
Purpose	<ul> <li>✓ Improve efficiency, service level and transparency</li> <li>✓ Reduction of the national burden</li> </ul>	✓ Increase the national wealth	✓ Substitution and restoration of market function			
Key Issues/ Risks	<ul> <li>✓ Pressure to private enterprise</li> <li>✓ Fair competition problem including monopolization issue</li> </ul>	<ul><li>✓ Political Concerns on the investment targets</li></ul>	<ul> <li>✓ Criteria for determining intervention</li> <li>✓ Risks of pressure to private enterprise</li> <li>✓ Government-owned funds vs.</li> <li>Private funds</li> <li>✓ Supported companies vs. Other competitors</li> </ul>			

### **Principles To Address Key Issues**



#### Key Issues

✓ Criteria for determining intervention

- √ Risks of pressure to private enterprise
  - √ Government-owned funds vs. Private funds
  - ✓ Supported companies vs. other competitors
  - √ Risks even more serious for the turnaround fund model

#### Principles and Action Guidelines

- ✓ Principle①: Limit response to market dysfunction
- ✓ Principle②: Limit to request of public interest

- ✓ Action Guideline ①: Consider distortion impacting competition
- ✓ Action Guideline ②: Conduct strictly as a market player

### **Principle**(1): Limit Response To Market Dysfunction



- Acute macro market dysfunction: Market dysfunction caused by severe market failure and huge disaster
  - ➤ For example, severe market dysfunction caused or major natural disaster has paralyzed function of market-based economy and government is involved to substitute market function and to restore business through restructuring
  - ➤ For example, financial crisis caused systemic risks for the whole economy system, contraction of risk money has occurred.
- Chronic and structural micro market dysfunction:
  - For example, in Japan there is a chronic market dysfunction in provision of risk capital to ventures and local small-and medium-sized enterprises

### Principle2: Limit To The Request of Public Interest



- ◆ When the companies that play an important public function, such as lifeline, fall into a disorderly bankruptcy, significant public inconvenience will occur.
- ◆ In some cases regarding industrial policy, when the companies involved in significantly important industry face financial crisis, there are risks that related essential technologies are to be dissipated.
  - ➤ However, criteria of whether this industry or company is "significantly important" is unclear.

### **Action Guideline 1: Consider Distortion To Competition**



- Necessary to derive private players to play a more proactive role as equity sponsors from early stage.
- Recovery plan should be
  - generally down-sizing
  - > strengthening profitability and financial structure
  - inhibitory to facilities expansion and sales growth
- Combination of government fund investment and legal liquidation should be avoided as a principle.
- Competitors should also be given an opportunity to bid through a fair process when the equity owned by government fund is sold at an auction.

### Action Guideline2: Conduct Strictly As a Market Player



- ◆ State intervention itself should be suppressive and careful, however once government-owned fund is involved, it should behave as a market player.
- ◆ Being afraid of risk, spreading the governance and delaying the management reforms and restructuring will increase the risk of damage to public funds.
- ◆ Need to sell to private sector after the management reforms are completed.

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### **Case Study ① TEPCO**



On July 31, 2012, Nuclear Damage Liability Facilitation Fund, assumed TEPCO shares (1 trillion yen) based on the comprehensive special business plan.

	Assessment	Comments	
Response to dysfunction of the market		✓ TEPCO racks a huge debt risk in the nuclear power plant accident that is difficult to deal with by only private capital.	
Request of the public interest		✓ Power supply is a lifeline.	
Responding to competition distortion		✓ Distortion to competition is limited as utility company serves as a regional monopoly	
Thorough market player behavior	?	✓ Whether the Nuclear Damage Liability Facilitation Fund can be insulated from political influence will be the key point for the reform.	

### Case Study JAL



- ◆ In January 2010, JAL officially filed for corporate reorganization
- ◆ In September 2012, JAL is re-listed on the Tokyo Stock Exchange First Section
- ◆ Mr. Yasuhisa Shiozaki, member of the Diet, will propose a bill for ensuring fair competition

	Assessment	Comments	
Response to dysfunction of the market		✓ Not the dysfunction of the market, but the difference in management capability compared to ANA is main cause of collapse.	
Request of the public interest		✓ There was a risk of enormously impact on the national economy when it comes to full operation stop of JAL	
Responding to competition distortion	?	✓ No discussion on competition distortion until it is pointed out in the National Assembly.	
Thorough market player behavior		<ul> <li>✓ Governance concentration by Enterprise Turnaround Initiative Corporation (ETIC)</li> <li>✓ Strong leadership of Mr. Kazuo Inamori</li> </ul>	

# Case Study 3 Elpida Memory



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- Elpida Memory, Inc. is a major semiconductor (DRAM) manufacturer in Japan.
- In June 2009, it performed a third party allocation of new shares to the Development Bank of Japan (DBJ)

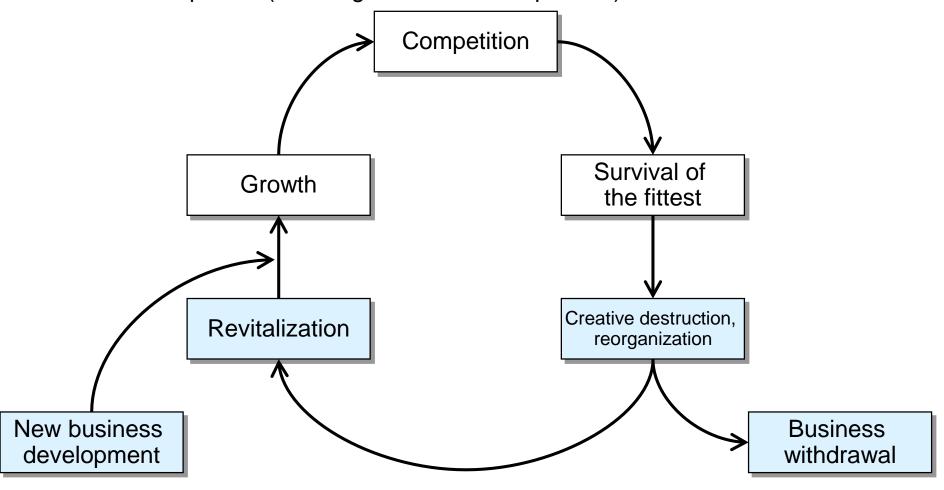
#### Assessment Comments Response to It was necessary to complement the market function dysfunction of the after Lehman Shock. market ✓ "A public request originating from concerns about the dissipation of key technologies and international Request of the public competitiveness decline in important industry" was the interest main logic, but the criteria of whether the industry is "significantly important" or not wasn't unclear. Responding to Collapsed later on. competition distortion Thorough market player behavior

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### Conclusion



Intervention of government owned funds should focus more on metabolism function to provide a healthy market economy rather than life-prolonging support of individual companies (resulting in "zombie companies").



# Appendix: List of Major Government Owned Funds in Japan

Name of Fund	Concerned Authority	Fund Amount	
Enterprise Turnaround Initiative Corporation of Japan (ETIC) (Re-organized to REVIC in March, 2013)	Cabinet Office	2012: 1,699 Billion Yen	
Regional Economy Vitalization Corporation of Japan (REVIC)	Cabinet Office	Same scale as ETIC	
Japan Brand Fund (Cool Japan Promotion Fund)	Ministry of Economy, Trade and Industry (METI)	60 Billion Yen	
Innovation Network Corporation of Japan (INCJ)	Ministry of Economy, Trade and Industry (METI)	280 Billion Yen	
Organization for Small & Medium Enterprises and Regional Innovation, JAPAN	Ministry of Economy, Trade and Industry (METI)	1,114 Billion Yen	
Agriculture, Forestry and Fisheries Fund Corporation for Innovation, Value-Chain and Expansion, Japan	Ministry of Agriculture, Forestry and Fisheries (MAFF)	32 Billion Yen	
Private Finance Business Promotion Fund	Ministry of Land, Infrastructure, Transport and Tourism (MLIT)	310 Billion Yen	
Fund for High-Quality Real Estate Form With Seismic and Environmental Performance	Ministry of Land, Infrastructure, Transport and Tourism, MLIT, Ministry of the Environment (MOE)	35 Billion Yen	
Competitiveness Fund, Development Bank of Japan (DBJ)	Ministry of Finance (MOF)	150 Billion Yen	