

Asia: Center of World Textile Output

– Technology, Soft Power Propel Teijin's Growth –

Interviewer: Okabe Hiroshi

Japanese textile manufacturers face an uphill battle, with crude oil prices up sharply and Chinese competitors catching up. Despite such a tough business climate, synthetic-fiber giant Teijin Ltd. posted a record profit in the 2005 business year ended in March 2006, thanks to brisk sales of such high-performance materials as aramid fiber and polycarbonate resin. In an interview with Japan SPOTLIGHT, Teijin President and CEO Nagashima Toru discusses his company's growth strategy.



Textile Products Can Evolve Further

The world industrial community is currently hit by waves of merger and acquisition (M&A) deals and of realignment. Japan's papermaking industry saw its top maker attempt to take over a rival firm. In the world's steel industry, Mittal Steel Co. of the Netherlands, which has taken over Arcelor SA of Luxembourg, is reported moving to acquire Japanese or other Asian steelmakers. Do you think such realignment moves will become active in the textile industry? What do you expect will be the future of the industry?

Nagashima: Almost all synthetic-fiber makers are diversifying their business fronts. Their technologies are based on polymer chemistry. In other words, we polymerize raw materials to produce polymers and offer them in the form of fiber, film or resin. There is a wide variety of applications for them, ranging from clothing to industrial products and environmental use such as water purification. In reality, a synthetic-fiber maker produces not simply synthetic fabrics. It also offers a wide range of products and services ranging from film to resin, healthcare, and medications and medical services. Given such realities, any manufacturer wonders how to achieve growth as a company. Synthetic-fiber makers may in the future consider mergers, consolidation of unprofitable



Photo: Kyodo News

Teijin President Nagashima stands in front of kimono made of special fabric that gleams when seen from different angles. Each yarn composing the fabric is made of 61 polyester and nylon layers that gleam at certain angles.

business units, or active investment in promising fields to achieve their growth. But major foreign chemical and textile makers such as Imperial Chemical Industries PLC of Britain, Hoechst AG of Germany and Akzo Nobel NV of the Netherlands did not seek an expansion of scale through mergers but opted to transform themselves by abandoning or selling unprofitable business fields. DuPont of the United States has pulled out of the textile business and is trying to become a specialized biotechnology firm. It is still possible to merge other companies or take over from them some business fields where they are strong. But the time is not yet ripe. I do not think such moves will emerge right away.

Newly emerging economies, notably China, have begun to produce a large amount of textile products with cheap labor costs. And some European and US companies are withdrawing from

the textile business. Do you think Japanese fiber makers face similar structural problems?

Nagashima: The world's textile production is currently centered in Asia. And in Asia, I can say that only Japanese synthetic-fiber makers are promoting investment in research and development to put new products on the market constantly. For example, Japanese makers have worked on carbon fiber for 30 years. European and American rivals were also involved in the development of carbon fiber at first. But they pulled out one by one because of slow demand and no major specific use in sight. Japanese makers continued efforts to develop carbon fiber applications with patience. Those efforts have now produced results. Even for general-purpose nylon and polyester, I am sure Japanese producers are capable of adding fresh functions to them and achieving their evolution.

Product Mix Will Differ from China's

Teijin's medium-term business plan, compiled in February 2006, lists the restructuring of its polyester fiber business as a major theme. What kind of restructuring effort do you imagine for Teijin's textile business, which has been affected by an output increase in newly emerging economies such as China and hit continuously by such cost pressures as crude oil price hikes?

Nagashima: Market trends have a great impact on us. Prices of raw materials go up to offset streamlining efforts. Teijin has been hit by the double hardships of higher raw material prices and the inflow of cheap ordinary products from China. So, we have made it clear that Teijin will never offer similar products to China's. Fortunately, thanks to our technologies that have been accumulated over a long period of time, Teijin can add to products new functions that China has not yet developed. Teijin is still competitive in such technologies as sweat-absorbent or quickly drying textiles. Chinese makers would eventually catch up with us in such technologies. But we have already developed technology to make a nano-size textile that contains as many as 8,000 filaments in a single hair-thin fiber. This textile is very soft. Clothes woven or knit with this textile would firmly stick to the skin. Those clothes would offer users feelings similar to skin. I think they can be used as a part of underwear. They are of very fine texture so they can prevent viruses from intruding into the human body. They can be used as a special filtering material.

High-performance materials such as aramid fiber have become Teijin's key earnings pillars.

Nagashima: I was assigned to the aramid fiber development section at the end of 1985. It was upgraded to a business

department but remained deeply in the red every year. Sales were slow while costs were high. The use of aramid fiber was limited. It took considerable time to develop a market and win customers. We repeated tests thoroughly to win orders for the fiber as a belt for automobile engines. Only after finishing the tests could we finally launch pricing talks. I traveled throughout Japan and the world at that time to promote sales. It took about five years to fully grasp the advantages and disadvantages of aramid fiber. And I emphasized its advantages to promote sales. Eventually, it took 10 years to turn the aramid fiber business profitable. Now, its profitability and growth are high. We took over a Dutch aramid fiber firm, greatly contributing to development of that business for Teijin. Our aramid fiber sales continue to grow by 9% annually. We are expanding production facilities, but we are still lagging behind demand. Automakers have begun to use the fiber for tires because it is safe, light in weight and energy-saving, and also as a friction material for automobile brakes because of its strength and heat resistance. Its applications have widened as enforcement materials for optical fibers and bullet-proof vests.

Hostile Takeover Bids Doomed to Fail

The so-called triangular merger framework is to be introduced in May after a one-year moratorium. Foreign firms with immense capital power may launch takeover bids (TOBs) of Japanese companies upon the lifting of the moratorium. Some Japanese businesses are concerned about foreign competitors threatening TOBs.

Nagashima: It is not only foreign companies but domestic firms that may launch hostile TOBs. Looking back on the history of M&As in the United States, there are few cases of hostile takeovers that turned out to be successful. Notably in Japan, I do not think hostile

takeovers will go smoothly due partly to national characteristics. But we have taken defensive measures against hostile TOBs. A general meeting of Teijin shareholders has approved a type of anti-takeover action that allows management to issue new shares if an outside takeover proposal is unfavorable to all existing shareholders. The defensive measure is effective for three years.

Will Teijin launch any hostile TOB?

Nagashima: Japanese corporations have a higher degree of respect for employees than US firms. Such corporate culture has taken root in Japanese society. Japanese companies are managed in a sense as a common destiny. So, after more than two Japanese companies merged into one, the management of the merged firm will be quite difficult if there is a sense of resistance among employees. Of course, Teijin has takeover experience. But it took many years to consolidate Teijin into a purely single firm. This might have come from the Japanese people's DNA. If Teijin is to launch a TOB, we will in advance have in-depth discussions with the top executive of the other party and also decide on future plans for the merged company. It is Teijin's main takeover premise to make use of each other's advantages and to achieve sound and continuous growth for both parties.

Recently, giant investment funds handle an enormous amount of money, and there seems to be a climate in which corporate M&A deals themselves are regarded as a money game.

Nagashima: Teijin is aiming at becoming a sound company trusted in society and will never do anything that goes against that philosophy. Being healthy does not mean either money-first nor short-sighted. I have worried about rising "mammonism" in Japan. Top corporate executives are required to have high levels

of ethics and philosophy. By contributing to society and providing services, only then can corporations post profits. These basics must be in place first of all.

Meeting of Global Teijin Group Managers

Would you brief us on the Teijin group's overseas strategies?

Nagashima: The Teijin group has been globalized, with 40% of its sales and half its profits coming from overseas businesses. The group has production bases in Asia, Europe and the United States, and continues to further globalize. Teijin is seeking to find out what is necessary for a Japanese corporation to turn into a truly global company. The biggest challenge is to secure human resources. This means how many foreign members are on the board of directors. Teijin has begun an annual meeting of top managers of our group firms, starting with one in Singapore in 2005. In 2006, Tokyo was the venue. The get-together is aimed at gathering the heads of group companies across the world and sharing information about Teijin's long-term business policies, medium-term targets and plans, and short-term situations. They will share Teijin's corporate brand and governance along with its corporate philosophy, which ranks higher than the two themes. From a risk-management point of view, Teijin has worked out a code of corporate behavior in six languages and distributed it to all group employees. Modified according to different customs and cultures in various countries, the code makes it clear what Teijin will do and what it must not do.

As for Teijin's policy of rewarding shareholders with profit returns, you have changed it from the conventional practice of long-term, stable dividend payments to dividend payout linked with

consolidated earnings. What is your philosophy behind the policy shift?

Nagashima: Teijin began to tackle in earnest the question of how to better manage group firms around 1996-97 and adopted the consolidated accounting system in the 1999 business year ended in March 2000. In the 2003 business year, Teijin adopted a holding company system. To grow into a healthy group, Teijin basically linked its dividend payments with the group's earnings performance. Parting from the conventional policy of stable dividend payments, Teijin decided to pay out what it can, when it can. But in the three-year period starting in 2006, Teijin needs to aggressively invest to develop its businesses in the years beyond 2009. Teijin will use its funds to achieve that target. It has declared that it will use its funds to achieve growth rather than dividend payments and will set its payout ratio at 20-30% in the three years. We are considering raising the ratio to more than 30% in the future. It is important for a corporation to restrain itself at some point in favor of investment in research and development projects, spend its funds on expanding facilities and promote business alliances or takeovers in promising fields.

¥50 Bil. at President's Discretion for Investment

What are the pillars of Teijin's investment plans for the coming three years?

Nagashima: Teijin will put ¥210 billion out of the ¥300 billion under our medium-term capital investment plan into such growing fields as medicine, aramid fiber, carbon fiber, polycarbonate resin, and polyethylene naphthalate

resin/film. In addition, ¥50 billion can be used at the company president's discretion to deal with emergencies, which may be an M&A project or an investment in other fields. I see the ¥50 billion as a fund that can be used for investment at the quick decision of the president. Having such an amount of money for the president's discretionary use will never worsen Teijin's financial strength.

Are there any specific business fields Teijin is envisaging for alliance or M&A plans? In the medicine business, Teijin once planned to merge with Kyorin Pharmaceutical Co. But it failed. Do you see medicine is a promising business field for Teijin's M&A strategy?

Nagashima: The failure in the merger talks was a good lesson for Teijin. We continue to keep a close watch on the medicine business both at home and abroad. What we are paying attention to is not simply drugs but a more broad sense of medicine, including home medical care services. We are searching (for a partner to acquire) to save time in developing a new business field.

Do you mean you always have in mind an M&A strategy to save time, not only in the medicine and home medical care fields but other business sectors?

Nagashima: Medicine is not the only promising business field. We are planning to put emphasis on four key fields. They are automobiles/aircraft, information electronics, environmental energy, and healthcare. We will actively consider acquisitions in those fields if there are any good deals.

Teijin's Service Business Originates from Technology

Photo: Teijin

In the medicine/home care business field, Teijin has departed from manufacturing and undertaken home medical care services. Why, as a manufacturer, are you promoting a services business?

Nagashima: There is a history to it. While promoting various polymer businesses, Teijin developed a thin polymer film membrane. Many firms competed to develop technology to produce a thin membrane that filters water or lets air through. Teijin developed technology to extract oxygen from the air through a membrane. Oxygen levels are very high under this method. This technology led to the development of another technology to give condensed oxygen to patients with lung diseases. Then, Teijin began to undertake that business. Patients received treatment at hospitals at first. Later, the Teijin-developed technology made it possible for patients to receive treatment at home. Physicians, patients and we joined hands to develop such a service on a rental basis at any place in Japan. So, Teijin became a pioneer in the field of home medical care services. Recently, we have developed technology to remove nitrogen from the air instead of extracting oxygen from the air. This means technology-based matters can become a service business.

Ethical drugs can be seen as a service for physicians. They are in fact a service that gives doctors full-fledged briefings, follow-ups and various data acquired by us. In the medicine business, we do not merely sell drugs but offer various services. I think service businesses are leading to profits, particularly in advanced countries or intellectual societies. But it requires not only software but hardware. Materials and home instruments cannot work without their supporting technologies. We have concluded that both software and hardware are necessary. So, Teijin came to use two phrases as its brand statement: "human chemistry," which symbolizes technologies in the polymer, chemistry and materials field, and "human

solutions," which means software and service businesses. The Teijin group includes such service business firms as N.I. Teijin Shoji Co., a distribution and retail company, and Infocom Corp., an information technology company. I think Teijin can promote better business activities in the medicine / healthcare, distribution / retail, IT service and environmental service fields.

Teijin's brand statement uses the same word, "human," twice. What kind of philosophy is contained in the message?

Nagashima: There is some meaning in the use of the word "human" twice. The first "human" means attention to humankind and the global environment, and the latter one means that Teijin will continue offering solutions to society and customers. Teijin tells its employees the message in the form of the brand statement and makes it its commitment to people in the world. Software and hardware are inseparable. It does not make sense to sell hardware or materials alone. The brand statement contains the message that software must be added and that more solutions must be offered to customers. I am planning to establish a new business model – that is, not to sell polyester fiber alone, but to add value to it and recover products to reproduce them in a recycling process. It might take time, but we would like to pursue it.

Target: Closed-Loop Recycling Business

What is the environmental-recycling type of business, specifically?



Teijin gathers the heads of group companies across the world for an annual meeting to share information about the company's long-term business policies, medium-term plans and short-term situations.

Nagashima: For example, used clothes such as uniforms and sportswear made of polyester would be crushed at a plant. These crushed materials are broken down to crude original materials of polyester through chemical processes for re-polymerization to produce polyester fiber that is almost new and not degraded. Then, knit and woven products are to be made. We have been successful in developing such a closed-loop recycling type of technology and are now ready to go on to the next step of investment. We started this project around 2002 and it is turning out to be an actual business, gaining support from consumers. The sharp rise in crude oil prices or the limit to resources triggered the development of the technology. What Teijin is aiming at is not a mere recycling of products but closed-loop recycling technology that produces new products of the same quality as the used ones recovered. Mere recycling technology cannot solve the problem of resources exhaustion. We are making efforts, dreaming of the day when the creation of a recycling-oriented society and the development of recycling-oriented technologies will become greater sources of business. **JS**

Okabe Hiroshi is a business news editor at Kyodo News.