

Approach to the Smooth Implementation of the "Select and Focus" Strategy

- Selected and Well Focused Development of Management Resources -

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I. Background

1) Stagnation of corporate profits

During the asset-inflated bubble period, many Japanese companies focused on their market shares and all-round business operations on the assumption that the Japanese economy would continue to grow without interruption. As a result, their profitability has remained low since the burst of the bubble. The return on total assets (ROA) of Japanese companies (except financial institutions) has been hovering in the 2% range for the past several years, indicating just how low their profitability has remained. (Fig. 1)

3) Factors of lower potential growth rate

The long-term trend of economic growth is determined by the growth of potential gross domestic product (GDP). The growth rate of Japan's potential GDP began to slacken even during the bubble economy, and further lost its tempo after the burst of the bubble. This trend has continued to this day. Growth of potential GDP is determined by the combination of labor input volume growth, capital stock growth and total factor productivity. Up to the high growth period, Japan maintained a growth pattern characterized by mobilization

of resources and higher productivity will be essential for the Japanese economy to sustain growth. However, the growth rate of Japan's productivity is below the average growth of member countries of the Organization of Economic Cooperation and Development and has remained stagnant.

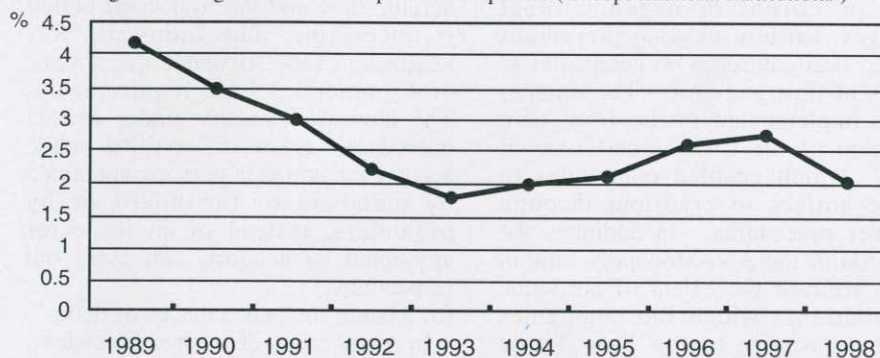
II. Necessity of the "Select and Focus" Strategy for Upgrading Productivity

The Japanese economy remains highly important in the eyes of the world as is seen in remarks made at the G-7 summit and other international meetings held last year. On the other hand, as already mentioned, the Japanese economy remains in a severe condition due to low productivity, among other reasons.

If Japanese companies are to surmount their difficulties and upgrade productivity, they will have to make good use of manpower, capital, information and other management resources, and focus on their niche areas. At the same time, it will be important for them to strategically restructure their businesses in such a way as to expand into potential growth sectors.

In the United States, companies thoroughly restructured their businesses by divesting unprofitable units and focusing on core businesses in the 1990-1991 recession. (Fig. 3) To supplement the measures, U.S. companies invested a vast amount of money in the information sector and made good use of outsourcing. This enabled them to boost their profitability and productivity in a relatively short time. With each company striving to upgrade profitability through the "Select and Focus" Strategy, the U.S. economy began to turn around in the first half of the 1990s. Stock prices have

Fig. 1 : Changes in ROA of Japanese companies (except financial institutions)



Source : Annual Corporate Statistics, Ministry of Finance

2) Stricter corporate evaluation

As the capital market has been globalized on the back of faster diffusion of information, global money flows into companies with potential for high profitability. At the same time, the credit ratings of companies by rating agencies have become so strict as to affect their profits and their stock prices. It is becoming increasingly important for companies to focus on profitability, if they are to raise funds smoothly to maintain sustainable growth.

of resources and higher productivity. In other words, increases in capital stocks and higher total factor productivity led to high GDP growth. Abundant manpower and the high savings rate supported Japan's high growth. But a declining birthrate, the aging of the population and a decrease in the savings rate will inevitably remove these favorable conditions for the Japanese economy. Further growth in the labor input volume and capital stock can no longer be expected. Accordingly, higher pro-

Table 1: International comparison of productivity growth (%)

	Japan	U.S.	Germany	France	U.K.	OECD average
1970 - 79	1.9	0.5	1.8	2.1	0.5	1.5
1980 - 89	1.6	0.8	1.2	1.7	1.6	1.1
1990 - 98	0.3	0.8	1.3	0.6	1.3	1.1

(Source : OECD Statistical Working Party)

continued to soar and the U.S. economy has maintained stable growth up to now.

III. Moves of the Industrial Sector

Japanese companies, for their part, have launched initiatives toward the "Select and Focus" Strategy in an effort to increase their competitiveness in the global market. Alliances across national borders, like Nissan Motor Co.'s capital tie-up with Renault of France, and combinations of industrial complexes by oil refining and chemical companies, represent these moves.

VI. Government Response

Under such circumstances, the government shifted the weight of its policy to bolstering the supply side of the economy and kicked off various initiatives.

The government will focus on the independence of private business operators and on the market principle, and improve the environment for the promotion of the "Select and Focus" Strategy of management resources in an effort to enable business operators to gradually shift their manpower, capital and other management resources to high profit sectors. As part of such measures, the government adopted on June 11, 1999, an emergency measure for promoting employment and strengthening competitiveness. A government council on competition, chaired by the prime minister, examined various measures and recently incorporated some of them into the Special Industrial Revitalization Law.

(1) Versatile corporate structures

From the viewpoint of effective use

of management resources, companies should focus on maintaining versatile organizational structures not only for themselves but also as a group and through mergers and acquisitions. As the business world is increasingly globalized and information is gaining more weight, the government should maintain the versatility of organizational structures to help companies to promptly implement adequate distribution of management resources. Specifically, the government has taken the following measures:

- The government reviewed procedures for corporate mergers to enable prompt corporate organizational changes, because existing procedures placed heavy burdens on companies in terms of time and cost. The changes were implemented in the form of a revision of the Commercial Law in 1997, which enabled companies to issue notices to creditors through simpler procedures. In addition, the revision of the Anti-Monopoly Law in 1998 reduced the extent of corporate acquisitions, which the companies have to report to the Fair Trade Commission. This in turn reduced the clerical burdens on companies.

- Removal of the ban on holding companies, and other measures

Holding companies were totally banned under the Anti-Monopoly Law, but the 1997 revision of the Commercial Law removed the ban on holding companies with the exception of cases where the controlling power of the companies involved is excessively concentrated. In addition, the revision of the Commercial Law enabled the creation of 1) a system under which stocks can be transferred for the creation of a holding company, and 2) a stock swap system which

made full ownership of affiliates easier. These measures will promote diversification of the organizational structure a company can choose and will streamline the shift to a new structure.

- Simplified procedures for divestiture (Exemptions of Commercial Law requirements were taken under the Industrial Revitalization Law enacted in October 1999)

- (a) Simplification of inspector requirements

It is often pointed out that the appointment of an inspector and subsequent inspections take considerable time and the inspection period is uncertain. The Industrial Revitalization Law stipulated exemptions of Commercial Law requirements. The law specifies that under certain procedures, a lawyer, certified public accountant or other persons appointed by members of the board or by promoters, instead of an inspector appointed by a court, can carry out inspections.

- (b) System for bulk transfer of debts

In many cases of business transfers, transfer of assets is accompanied by a transfer of debts resulting from business operations. In such transfers, acceptors are supposed to win the consent of each creditor, if they directly owe debts to creditors and exempt original debtors from debts. The Industrial Revitalization Law incorporated provisions for the full protection of creditors to make it easier to transfer debts to original debtors.

- (c) Exemptions regarding full transfer of business rights.

Under the current Commercial Law, the full transfer of business rights is subject to approval at a general

meeting of stockholders. The Industrial Revitalization Law incorporated a special provision on the full protection of creditors and made it easier to transfer debts from the original debtors. This is because there are cases of transfer of debts having little impact on stockholders, e.g., in the case of the full transfer of stocks of a small company.

- Securitization of debts (The Industrial Revitalization Law incorporated a provision on securitization of debts)

When a financial institution securitizes debts as part of the process of debt recovery, it may prefer to

stock options can be granted up to one-tenth of the total of issued stocks, though beneficiaries are limited to executives or employees of the company involved.

As measures for streamlining organizational changes, such as divestiture, the Industrial Revitalization Law grants executives and employees of an affiliate the right to receive stock options of its parent company if the affiliate owns 95% or more of its own issued stocks.

- Introduction of a corporate split-up system

Divestiture is a system under which a new company is established through

whole will increase. The introduction of a consolidated taxation system, under which tax is imposed on an entire corporate group, instead of each group company, will ensure greater neutrality of taxation in connection with a company's choice of its corporate structure and facilitate the choice.

(2) Smooth corporate reorganization premised on continuation of business operations

This is aimed, from the viewpoint of efficient use of corporate resources and efficient corporate structure, at promptly liquidating and restructuring deadlocked businesses and paving the way for

Table 2 : Examples of corporate restructuring in the U.S.

Companies	What was done
Monsanto	Streamlining of chemical division. Expansion into bio-agricultural chemicals and pharmaceuticals sectors
IBM	Buy-out of Lotus
AT&T	Acquisition of Telecommunications Inc.
Exxon	Merger with Mobil Corp.

acquire stocks with no voting rights, instead of ordinary stocks, if it has no intention of participating in management but only wishes to maximize profit. Under the Industrial Revitalization Law, the upper limit of the issuance of non-voting stocks will be raised to 1/2 of the total of outstanding equity, instead of 1/3 as provided for in the Commercial Law, in case 1) securitization of debts is essential for the continuation of business operations of the company involved, and 2) the owner of the company, who was recognized as having a clear agreement with creditors in accordance with the requirements of related ministerial ordinances, issues non-voting stocks for the securitization of debts for the company's reorganization.

- Expansion of the extent of beneficiaries of stock options

Under the current Commercial Law,

the split-up of a company division and at the same time stock owners of the former company are entitled to own stocks of the new company. A bill for revising the Commercial Law for the introduction of the system will be submitted to the next regular session of the Diet which will be held from mid-January, 2000 (note: this article was written on December 20, 1999). The current Commercial Law has no provisions about transferring stocks of the new company to those of the former company, which prevents corporate divestiture. The planned introduction of the system will facilitate re-organization of company groups.

- Introduction of consolidated taxation system

Under the current taxation system, losses of subsidiaries cannot be offset by profits of other companies of the same group at the time of divestiture, and so tax burdens on the group as a

creating an environment under which a new business can be developed.

Specific measures

- Introduction of new reorganization-type bankruptcy procedures

The Civil Restructuring Bill, which would serve as general legislation on reorganization-type bankruptcy, was passed into law by the Diet in the previous extraordinary session. The law incorporates acceptance of applications for reconstruction prior to bankruptcy, strong asset preservation measures for preventing the dispersal of corporate assets, and acceptance of debtor in possession (DIP)-type reconstruction. Review of the Bankruptcy Law and the Corporate Reorganization Law will continue.

V. Measures for Employment and Subcontracting

As already mentioned, companies now inevitably must push for business

Table 3 : Recent industrial moves in Japan

Companies	What was done
Sumitomo Metal Industries, Ltd.	Spin-off of bar steel and stainless steel businesses and establishment of new companies
Nippon Oil Mitsubishi Co. and Cosmo Oil Co.	Full tie-up in oil refining and marketing
Mitsubishi Chemical Corp. and Asahi Chemical Industry Co.	Unification of polystyrene business
Teijin Ltd.	Establishment of joint venture with du Pont for production and marketing of nylon textiles
Nissan Motor Co.	Capital tie-up with Renault

reorganization and improve profitability to survive intensified global competition. In the medium and long term, business reorganization would help ensure and even expand employment opportunities. In the short term, however, it could adversely affect jobs at the company involved and even the management of related subcontractors.

In this connection, the government will continue to take various measures for the stability of employment and for the stability of subcontractors' businesses.

(1) Measures for the stability of employment

In reorganizing business operations, each company will inevitably have to pay the utmost attention to the stability of workers' jobs. Accordingly, the government has repeatedly asked the business world to make efforts to ensure and stabilize employment.

The government, for its part, will effectively implement the emergency employment promotion package worked out on June 11, 1999, and strive to build an employment safety net focusing on the smooth transfer of manpower, talent development of individual workers and removal of mismatching in employment.

Specifically, the government will take the following measures:

- give subsidies to companies which accept workers of other companies ("Special Subsidy for the Transfer of Manpower")

The system is aimed at subsidizing

companies which accepted, in the form of reemployment or secondment, workers aged below 60 who were made redundant due to production cutbacks or for other reasons in other companies. The subsidy will cover part of their wages or other costs.

- subsidy to company owners who employed workers in new and growth sectors ("Special Subsidy for the Creation of Employment in New and Growth Areas")

This subsidy is aimed at helping company owners, mainly those in 15 new and growth sectors, who employ middle-aged and older involuntary jobless workers ahead of schedule or provide these workers with practical training.

- licensing more private job placement agencies and job placement information by public employment agencies

Specifically, information on job openings in Tokyo's 23 wards was offered on the Internet.

- Vocational training for jobless workers of their own choice while receiving unemployment benefits (voluntary choice system)

The system is aimed at providing middle-aged and older involuntary jobless workers with vocational training of their choice, at vocational schools or other private educational training institutions, while they receive unemployment benefits.

(2) Measures for affiliated subcontractors

Corporate reorganization could seriously affect contractors, parti-

cularly subcontractors, in the form of reductions in orders and the lowering of unit prices of orders. The government will take measures to support such subcontractors through the cultivation of new customers, financing, innovation, etc., on a case-by-case basis.

Specific measures

The associations for the promotion of subcontracting companies, established in all prefectures, help subcontracting companies find new customers. The associations will expand their activities by helping subcontractors find new customers beyond prefectural borders and sponsoring wide-area business talks for subcontractors.

- Financing system

The Small Business Finance Corporation finances capital investment by small subcontractors affected by changes in parent companies' business operations. The Small Business Finance Corporation, the People's Livelihood Finance Corporation and other public finance organizations offer low-interest loans to cash-strapped small businesses for the stabilization of their operations.

- Support for management innovation

On the basis of the Law on Supporting Business Innovation of Small and Medium Enterprises, small subcontractors are entitled to receive support, such as low-interest loans, tax breaks and subsidies, for new business activities such as the development and production of new products and the introduction of a new production system.