

Topic-Setting Program to Advance Cutting-Edge
Humanities and Social Sciences Research
(Global Initiatives)

Progress Report
(Summary of Final Report)

[Empirical Comparative Analysis of Corporate Governance in Japan:
Ownership, Strategic Choice and Performance]

Core-Researcher: Hideaki Miyajima

Institution: Waseda University

Academic Unit: Graduate School of Commerce / Institute for Advanced Study

Position: Professor / Director

Research Period: FY2013 – FY2016

1. Basic information of research project

Research Area	Global Transmission on Corporate Governance of Japanese Companies
Project Title	Empirical Comparative Analysis of Corporate Governance in Japan: Ownership, Strategic Choice and Performance
Institution	Waseda University
Core-Researcher (Name, Academic Unit & Position)	Hideaki Miyajima, Professor, Graduate School of Commerce, Director, Institute of Advanced Study
Project Period	FY2013 - FY2016
Appropriations Plan (¥)	FY2013 6,000,000 JPY
	FY2014 10,000,000 JPY
	FY2015 8,400,000 JPY
	FY2016 5,520,000 JPY

2. Purpose of research

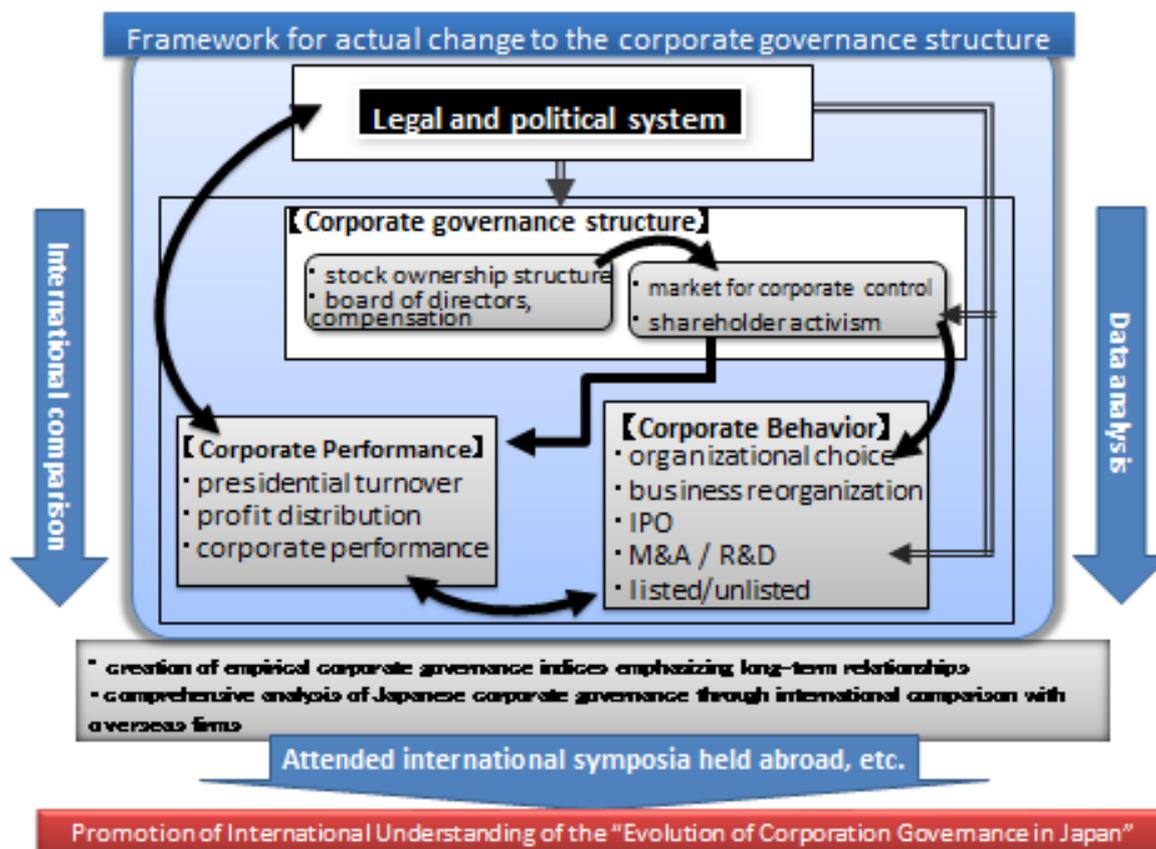
Motivation: The governance structure of Japanese corporations, formerly referred to as the “Japanese model” of governance, has undergone major changes in recent years, spurring a lively debate over whether or not these changes signify a convergence on the U.S. model of governance. The core researcher and fellow researchers have shown, by constructing a long-term data set that spans the 20th century, developing a system for evaluating corporate governance (Cges), and applying the data set and Cges to the empirical analysis of changes in corporate financing and ownership structure, and board composition, that the corporate governance of leading corporations has hybridized since the banking crisis, combining market-based governance and relational-based internal organizations and employment systems, and thus has greatly diversified since the 1980s (Aoki et al. 2007, Miyajima 2011). Consequently, the core researcher and his fellow researchers have emphasized that the challenges which listed corporations in Japan faced have become more complex, and that when redesigning a corporate governance system, there can be no “one size fits all” solution that suits all corporations. However, the characteristics of the above-noted hybrid structure (its benefits, and its costs such as the loss of systemic effects and adjustment expenses), and the causes of the diversification of corporate governance have still not been fully elucidated. Furthermore, no consensus has emerged regarding the influence that the changes in the governance structure, acting via corporate strategic and organization choices, have had on slumping corporate performance during what are now referred to as the “lost two decades.” Furthermore, even as governance structures have evolved in various countries through globalization, a clear picture of the international characteristics of the reshaped corporate governance in Japan has yet to emerge.

Theme: Thus, while our research project on the one hand has developed a new method for understanding governance structure by adopting a perspective that emphasizes long-term relationships based on trust and commitment between various stakeholders, we aim to carry

out a comprehensive analysis of corporate governance in Japan by making a comparison with overseas firms and explicitly adopting a comparative corporate governance perspective. To this end, we have established a dynamic framework that looks at how actual changes have altered the legal and political systems related to corporate governance (summarized in the chart below), and aim to internationally disseminate our analytical results related to the reality, function, and characteristics of the corporate governance structure in Japan.

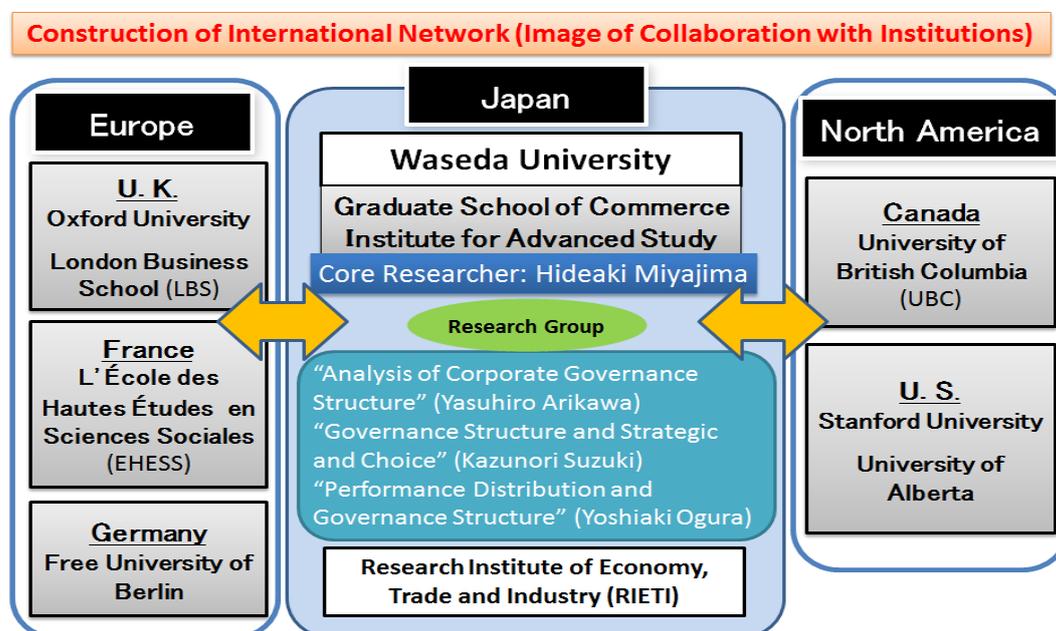
Our empirical research is focused on the following three issues.

1. **Determination of the Corporate Governance Structure:** How has the Japanese corporate governance structure, characterized by cross-shareholding and boards comprised of directors promoted from within the organization, changed, and what kind of characteristics does that structure have, when considered from an international perspective?
2. **Governance Structure and Strategic and Organizational Choices:** Do the changes in governance structure have an actual influence on corporate strategic and organizational choices? This question is being analyzed in terms of organizational choices that were made as related to IPOs, M&A, holding companies, and skill formation.
3. **Distribution of Performance and Corporate Governance:** Does governance structure have an actual influence on corporate performance, and moreover, on economic growth, and if so, via what kind of mechanism? In order to shed light on these issues, we analyze the relationship between the distribution of profitability and production, frequency of presidential turnover, and financing policy, and governance structure.



3. Outline of research (Including study member)

As part of the Japan Society for the Promotion of Science's Core-to-Core Program (A. Advanced Research Networks), this project is receiving funding from 2015 to 2018 in order to conduct joint research with overseas collaborating institutions. Through this research project, a group centered on researchers affiliated with Waseda University has been able to augment long-term data related to corporate governance that had been accumulated up to this point, and has used this data to conduct multi-faceted empirical analysis and has made an effort to disseminate research findings internationally. Through these activities, this project has been able to establish a cutting-edge hub for research in this field in Japan. Furthermore, this project has promoted joint research with researchers affiliated with collaborating institutions and has built a network for studying the characteristics of Japanese corporate governance and its functions from an international comparative perspective, and has produced copious findings (See below figure).



Furthermore, this project has dispatched young researchers for short stays at the collaborating institutions noted above. By encouraging young researchers to become involved in joint research from the problem-setting and data-compilation stage, the project aims to enhance competencies in basic research. Moreover, by participating in seminars at collaborating institutions overseas, and acquiring an understanding the nature of overseas interest in Japanese corporations, we have been able to participate in the construction of a database that encompasses the U.S., U.K., continental Europe, and the newly emerging regions of Asia with various overseas collaborating institutions, and have thus blazed a path for participation in joint international research initiatives that will draw on this data in the future. In addition, the funding for this research project has enabled us to purchase data related to ownership structure (FactSets) and CSRI.

Main research topics and corresponding research members are summarized in following table.

Research Team Investigators and Collaborators

Core Researcher:	Research Topic	Investigator	Collaborators
Hideaki Miyajima			
Analysis of Corporate Governance Structure Group leader: Yasuhiro Arikawa	Ownership Structure and Market for Corporate Control	Arikawa	Osano (Kyoto University) Nakamura (UBC) Mayer (Oxford University) Franks (LBS) Hoda (Kobe University)
	Board Composition and Its Redesign	Kubo	Kawanishi (Kumamoto Prefectural University)
Governance Structure and Strategic, Organizational Choice Group leader: Kazunori Suzuki	Listing decision/IPO	Arikawa	Mehrotra (University of Alberta)
	M&A/Business Reorganization	Suzuki and Hirota	Kawamura (University of Edinburgh)
	Organizational Choice (Holding Company and Internal Capital Market)	Hibara	Ushijima (Aoyama Gakuin University) Ogawa (Waseda University)
	Employment Relationship, Labor Market, and Corporate Governance	Kubo	Sako (Oxford University) Jackson (Free University of Berlin) Kotosaka (Ritsumeikan University)
Performance Distribution and Governance Structure Group Leader: Yoshiaki Ogura	Distribution of Corporate Performance, Variation in Heterogeneity and International Comparison	Ogura	Lechevalier (EHESS)
	International Comparison of Corporate Governance and Performance	Arikawa and Hirota	Inoue (Tokyo Institute of Technology) Saito (Keio University)

Analysis of Corporate Governance Structure: We attempted to shed light on the characteristics and function of the ownership structure of Japanese corporations, which has undergone dramatic changes in recent years. This research project advanced the joint international comparison of the evolution of ownership structure that the core researcher had pursued to this point, resulting in the study by Franks, Mayer and Miyajima (2014). Furthermore, the project developed new variables to capture shareholder commitment by taking into consideration ownership ratios and length of ownership, and used these variables to stylize the characteristics of the ownership structure in Japan, while also considering the function of the

ownership structure from the perspective of shareholder activism and the market for corporate control. We approached the topic of board composition not only by focusing on the number of external directors, but also by attempting to develop variables to capture the special features of boards that become deeply involved in strategic decisions (managerial boards), and attempted to clarify the determinants of these features from a perspective that emphasizes stakeholder involvement. The findings resulted in an analysis of the influence of board composition on the relationship between presidential turnover and performance (Miyajima, Saito and Ogawa 2016).

Governance Structure and Strategic and Organizational Choices: Previous analyses have attempted to directly tie the characteristics of ownership structure and the presence of external directors to corporate performance. Underlying this approach is the perception that shareholders and the board of directors have the right to appoint top executives, and ultimately determine the level of effort exerted by these executives. However, differences in the degree of commitment to the corporation by the various stakeholders in fact have an important influence on corporate decision-making. Thus, in this project we developed the new variables noted above to clarify the influence of governance structure on corporate behavior. In addition to looking at choices pertaining to M&A, R&D, and holding company structure, and given the decline in metabolism of industry due to sluggish entry and exit behavior, we expanded our perspective to also take into consideration decisions on new IPOs and delistings, business reorganizations, and the function of internal capital markets. Furthermore, considering the possibility that the skill formation mechanism is not applicable to circumstances wherein the technological level continues to rise, we focused on specialists to shed light on the relationship between the choice either to train personnel internally or to outsource, and the governance structure. Based on these results, Kubo was able to prepare a first draft of a study analyzing the choice related to training or hiring of specialists in collaboration with Mari Sako (Oxford University).

Performance Distribution and Governance Structure: This research project analyzes the nature of the corporate governance structure's influence on performance, and produced important findings related to the role of employee stock ownership plans (ESOPs) and presidential turnover. Furthermore, since researchers have often attempted to attribute the laggard performance and risk aversion of Japanese corporations to delays in corporate governance reform, this project attempted a quantitative analysis to determine the degree to which the performance gap can be explained by corporate governance factors (when placed in an international context) and have obtained provisional results. Furthermore, we have also clarified the implications pertaining to long-term trends in the distribution of Japanese corporate performance (heterogeneity), gaps with other countries, causes of variations in distribution, and economic efficiency. While aware that other researchers have sought in recent years to attribute the productivity gap between countries to differences in the efficiency of distribution of resources, we used productivity as an index to examine the real (physical)

implications, and stock price and profitability as indices to examine financing implications.

4. Research results and outcomes produced

By sending the core researcher and investigators on research visits, hosting researchers from overseas collaborating institutions, dispatching young researchers abroad, etc., this project has aimed to carry out a closely coordinated joint international research effort on the three research topics, undertaking tasks that have included the compilation of data, the establishment of analytical frameworks, and the implementation of empirical analysis. Through the construction of an international research network and the pursuit of joint research and efforts to dissemination findings from the research, the results of our research on corporate governance in Japan are being shared with and appreciated by overseas researchers.

This project allocated research funding to purchase a corporate governance and ownership database (NRG Metrics), a CSR database, and data from FactSet Pacific Inc., etc., enabling us to augment the data that had been accrued at Waseda University. In particular, through the use of FactSet's database, we were able to determine the ultimate ownership entities, which thus made it possible to identify external blockholders, and the analytical focus on blockholders resulted in studies such as Miyajima and Ogawa (2016), and Miyajima, Saito and Ogawa (2016). Furthermore, the funding allowed us to hire part-timers who helped to collect and process data pertaining to ownership structure, board composition, etc. This work enabled us to compile new numerical series related to IPOs, and purchases and cancellation of treasury stock, and thus to conduct an analysis of controlling stakes in own-company shares, and to produce the study by Franks, Mayer, Miyajima and Ogawa. In addition, we used original data from the Nihon Keizai Shinbun's Cges (corporate governance evaluation system) to construct a database of Japanese corporations. Furthermore, this work provided feedback for revising Cges, and Cges Ver. 2.0, which was released in October 2016, made good use of the results of our data construction and analyses.

The core researcher used this project to plan and make progress on an English-language manuscript pertaining to the evolution of corporate governance in Japan, written from the perspective of comparative corporate governance theory. Beginning with an overview of the Japanese corporate system from around the 1980s, a period that marked the "golden age" of the Japanese corporate system, the manuscript will attempt to provide a comprehensive analysis of the changes in the ownership structure and corporate finance following the banking crisis of 1997, and of the developments in governance structure reform as well as the reforms following the Lehman Brothers crisis, addressing the vast research on the recent evolution of Japanese corporate governance, following up on the results of Hoshi and Kashyap's *Corporate Financing and Governance in Japan* (MIT Press, 2001), and Aoki et al. (2007). During the duration of this project, we have attempted as much as possible to make good use of the core researcher's empirical research, and of the research findings obtained by investigators as part of this project.

In the process of writing this manuscript, overseas collaborating institutions have been asked to schedule seminars to allow the presentation of preliminary drafts of our research, and we have incorporated the feedback provided by participants and attendees to prepare a final edition for publication.

With respect to the three topics, the core researcher, along with Professor Hideki Kanda, had been invited by the Ministry of Finance's Policy Research Institute to edit a special issue of the *Financial Review*, "Corporate Governance III," Vol. 121, and the core researcher has subsequently made further efforts to publish the findings of this project. Furthermore, as part of a research project for the Research Institute of Economy, Trade and Industry (RIETI), the core researcher edited *Corporate Governance and Growth Strategy* (Toyo Keizai Shinposha), also drawing on the results of the current research project (see list of publications). The main portions of this publication were published in English in *Public Policy Research*, Vol. 11, No. 3 (July 2015), contributing to the international dissemination of research findings on Japanese corporate governance.

Furthermore, in relation to the above-noted three topics, the core researcher, drawing on the results of RIETI's Corporate Governance Research Project, edited *Corporate Governance and Growth Strategies* (Toyo Keizai Shinposha). Most of the members of the current research project have contributed to this book, using data purchased with project funding and making use of research grants. The articles contained in this book are Japanese translations of the essential content of the English articles prepared using this funding, as well as articles appearing first in Japanese, and in the future an English edition of this book will be prepared to help disseminate these results overseas.

During the term of this project, the academic contribution of the many English-language articles that were created can be summarized as follows.

1. The research is distinguished by a new perspective that emphasizes commitment, and by the establishment of a framework that systematically grasps the mutual relationships between governance structure, strategic and organizational choices and performance, and thereby makes it possible to analyze corporate governance as an a priori corporate growth problem, rather than as an ex post facto distribution problem, and on the one hand advancing the analysis of the actual conditions of Japanese corporations, but also putting forth a new international perspective on the analysis of corporate governance. For this project, we constructed new variables related to corporate governance, which we then used to analyze the influence of corporate governance on real investment, M&A, and financing and organizational choices.
2. By carefully considering reverse causality, and conducting analysis that clearly controls for firm entry and exit, it is possible to elucidate the degree to which, and through which

channels, governance structure factors exercise influence over the distribution of performance. And in this way, we have been able to contribute to the international debate that has continued since Demsetz (who held that since the optimal governance structure is selected, it does not have an inherent influence on performance) while at the same time we were able to analyze the influence that independent directors, institutional investors, and share-holding by employee stock ownership plans had on corporate performance.

3. Using a long-term international comparative framework, our analysis has been able to newly stylize and standardize Japanese corporate governance's divergence from and convergence with other countries in the period since the collapse of Lehman Brothers, and have been able to contribute to the debate on the diversity of capitalism from the vantage point of corporate governance. We analyzed the actual state of the diversification of the Japanese corporate governance structure and its determinants not simply by addressing legal factors but also by taking into consideration cultural factors, and the characteristics of managerial perceptions of risk.

Appendix

List of Team Members

Core Researcher	Hideaki Miyajima	Professor, Graduate School of Commerce, Director, Institute for Advanced Study, Waseda University	The Evolution of Corporate Governance in Japan
Group leader	Yasuhiro Arikawa	Associate Professor, Graduate School of Commerce, Waseda University	Ownership Structure and Market for Corporate Control
Group leader	Kazunori Suzuki	Professor, Graduate School of Commerce, Waseda University	M&A and Business Reorganization
Group leader	Yoshiaki Ogura	Professor, Faculty of Political Science and Economics, Waseda University	An International Comparative Analysis of Performance Variation
Investigator	Shinichi Hirota	Professor, Graduate School of Commerce, Waseda University	M&A and Business Reorganization
Investigator	Katsuyuki Kubo	Professor, Graduate School of Commerce, Waseda University	The Employment Relationship, Labor Market, and Corporate Governance
Investigator	Nobuhiko Hibara	Associate Professor, Graduate School of Commerce, Waseda University	Organizational Choice (Holding Company and Internal Capital Market)