ASIA WEEKLY: Postcard from Japan

For the Week of August 3, 2012

After spending a week crisscrossing Tokyo earlier this summer to meet with various companies, my general take-away was that the country, as a whole, has managed a rather swift recovery from last year's devastating earthquake. Japan seems to have been able to rebound from its nuclear crisis, showing great resilience. Most of the firms I met with were already plowing ahead to try to make up for last year's losses. Indeed, Japan grew its GDP at a 4.7% rate in the first quarter of 2012, largely fueled by a strong recovery in domestic demand.

While Japan in many ways has a very sophisticated economy with well-developed capital markets, its corporate governance is still less robust than in other developed markets. Whereas most U.S.-listed companies generally maintain a separation between ownership and management, many publicly listed Japanese companies (as with firms in other parts of Asia) are still actively managed by original founding family members who also retain a controlling stake. Good corporate governance involves an alignment in the goals and interests of a firm's management, board and shareholders or other stakeholders. But in Japan, a founding family will often use its controlling stake to keep the succession of top management roles within the family—an arrangement that can bring some potentially significant pitfalls to the underlying business. First, companies may not always have the most capable hands at the helm if management is restricted to family members. In addition, there may be a lack of sufficient oversight of the board of directors who are meant to hold management accountable to all shareholders. Businesses hamstrung by these two factors may be prone to setbacks.

As prime examples of the benefits of focusing on good corporate governance, two companies I met with in Japan this summer saw renewed growth after scrapping their typical succession plans. Both businesses stagnated or deteriorated while run by second-generation family members. To revive business, both companies—one, a snack food firm, the other, a specialty auto retailer—sought external help, bringing in professional managers and handing over the company reins. Business priorities were reset and bold changes were made under new professional management. In the case of the food company, wide-reaching cost-cutting was implemented and an aggressive overseas expansion was set in motion to seek the next stage of growth. In the case of the specialty retailer, its earlier strategy of expanding its own retail store network was abandoned, and its new management decided instead to re-focus the business on a more efficient, higher-return franchise model. Both companies today are seeing marked improvements in their business performance.

Corporate governance is generally considered a "soft part" of businesses. However, as the experience of these two Japanese firms shows, when shareholders and company management realize the necessity of better corporate governance structures—and strive for them—corporate governance can provide a strong catalyst to underlying businesses.

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