Mizuho Custody Newsletter

June 2021 | Japan

Contents:

I. Market News

1. Net profit of listed companies increase 26%

Listed companies have almost announced their financial results for their fiscal year ending in March 2021, which is the first fiscal year since the outbreak of the global pandemic. In spite of the shrink of major business activities, net profit for the fiscal year ended March 2021 rose by 26% from the previous fiscal year, the first increase in the past three years, reports Nikkei Shimbun, Japan's leading financial daily. There was a large decline in profit for the first half of the fiscal year, but in the second half, there were a sharp recovery in profits mainly in the manufacturing sector. The rise was supported by brisk demand towards automobiles and smartphones as well as in relation to "staying home" due to coronavirus. Nikkei Shimbun also reports that it was also boosted by the increase in profit of SoftBank Group Corp. (SBG).

According to the Nikkei's research results announced on 18 May, covering 1,683 companies excluding parent-child listed subsidiaries and start-ups, net profit for all industries rose by 26% to JPY 28 trillion, recovering up to the level of about 80% of JPY 33 trillion marked in the fiscal year ended March 2019.

At the end of May last year, nearly 60% of companies were unable to announce earnings forecast for the year due to the pandemic, but business outlook had gradually become clear mainly for manufacturers, and finally, about 82% of the companies performed better than what they had forecasted previously (as at March end). It marked the highest upswing ratio since the global financial crisis.

In the previous fiscal year, 48% of companies increased profits, while 35% of companies decreased profits. Although the companies had a significant increase in their profit, less companies achieved profit increase than in the past in the whole picture. For example, in the fiscal year ending March 2018, when the profit increased by about 30%, the ratio of number of companies with profits increase was 64% (30% of those with profits decrease). In the fiscal year ending March 2014, when the profit increased by about 80%, the ratio of number of companies with profits increase was 71% (22% of those with profits decrease). The industries such as electric machinery and automobiles made recoveries in their performances, but on the other hand, industries that involves human mobility such as railways, airlines, leisure and restaurants are having tough time, and consequently bipolarization in the financial results became clear.

Many companies went into red ink. 17% of the companies (about 290 companies) ended in the red, the highest in 11 years since it recorded 21% in the fiscal year ended March 2010, when many companies recorded deficit after the global financial crisis.

It was remarkable that many companies showed "sales decreased and profit increased" for the first time in 4 years, since the fiscal year ended in March 2017. Overall sales in the previous fiscal year decreased 7% to JPY 576 trillion. Among the 36 industries, 32 industries saw a decline in sales, except for telecommunications, land transportation, insurance, etc. However, they managed to keep profit by various cost cutting including travel expense, personnel expense, entertainment expense, etc. Net profit margin rose by 1.3 points to 4.9% compared to the previous fiscal year. Manufacturers posted 35%

increase in net profit despite 8% decline in sales. Many companies strengthened their earning power by streamlining their business, and they started to gain profit as aggregate demand recovers.

This is clear by comparing what happened in the first half and the second half. The net profit of all listed companies in the second half (October 2020 - March 2021) was JPY 17.92 trillion, which was 3.1 times higher on a year-over-year basis. The semi-annual growth rate was the highest since it recorded 3.2 times in April-September 2010, when the economy recovered sharply after the global financial crisis. There have been cases in the past in which profitability of companies increased in one half and decreased in the other, but it has been extremely rare that significant increase in profit in the second half covers 39% decrease in net profit in the first half (April-September 2020), resulting in “V-Shaped recovery”.

Manufacturers are the driving force, which gained the net profit in the second-half by 3.6 times of that of the first half. The semi-annual growth rate was the highest since the global financial crisis. In particular, automobiles industry fell 94% in the first half of the fiscal year and surged 7.2 times in the second half.

The non-manufacturers’ net profit in the second half was also 2.7 times than that of the first half (first half was 28% down).

The uptrend is expected to continue in the fiscal year ending March 2022. In 1,476 companies that released earnings forecast, net profit (excluding undisclosed SBG) is expected to rise by 30% compared to the previous quarter. A director of an automobile company says, "The break-even point has been steadily getting lowered," and manufacturers have been streamlining their businesses. A senior economist at a research institute comments, “It is expected that the global economy, including the U.S., will continue to recover, which may create a business environment where companies relying on overseas demand can pass it on to their product prices.”

On the other hand, business outlooks for non-manufacturers remain unclear. At this point, some companies may be affected by the declaration of state of emergency and the expansion of the semi-emergency measures for the pandemic. Their performance may depend on external factors such as vaccination coverage.

Information compiled from Nikkei Shimbun & Mizuho research

2. The number of M&As by Japanese companies marked record high in January-March 2021

It is now clear that more and more Japanese companies are coming back to M&A market, which had been stagnant due to COVID-19, according to Nikkei Shimbun, Japan’s leading financial daily. In January-March 2021, the number of M&A cases increased by 7% on a year-over-year basis to 1,058, which marked the record high. In March, the number of acquisitions of overseas companies by Japanese companies, increased for the first time in 16 months after a respite due to travel restriction under the pandemic. De-carbonization has been forcing many companies to review their profit structure, and has been reinvigorating their business restructuring.

According to a research by a M&A advisory firm, the number of M&As (including capital contribution) in January-March 2021 was the highest for the period since they began to collect data in 1985. The number fell by 22% to 831 cases in April-June 2020 due to the pandemic, but the situation turned around in July-September 2020 and continued to increase for the three consecutive quarters.

In terms of monetary value, it was doubled up to JPY 3.9 trillion in January-March 2021 on a year-over-year basis.

Domestic M&A deals rose by 10% to 843 cases. In particular, the number of deals rose by just under 30% to 372 cases in March. Companies’ reaction to the next generation environmental technology prompted by de-carbonization now accelerates restructuring of industries. With a view to the planned reorganization of the stock market in April 2022 by Tokyo Stock Exchange, there are moves to dissolve parent-child listings.

The number of M&As by Japanese companies toward foreign companies turned upward in March. This trend is expected to continue as more people get vaccinated worldwide.

On annual basis, M&As cases reached a record high of 4,088 in 2019. In January-March 2021, M&A deals

have been done at a faster pace than 2019. It has been already 422 deals in April, up by 40%. Companies have been still eager to restructure their businesses, and it may make 2021 as the record year for M&A deals.

Information compiled from Nikkei Shimbun & Mizuho research

3. The revised Corporate Governance Code encourages more active use of outside directors and female workforce

On 11 June 2021, Tokyo Stock Exchange (TSE) released and enforced the revised Corporate Governance Code (Code), which outlines the rules on the management of listed companies. Through more active use of outside directors and female workforce, it intends to attract more money from both Japan and overseas by making their governance standards closer to those of Western countries, reports Nikkei Shimbun, Japan's leading financial daily. It also aims to urge companies to deal with internationally recognized issues such as human rights and climate change.

This is the second revision since the Code was introduced in 2015. This revision is closely related to TSE's planned realignment of market segments in April 2022. Companies listed in the "Prime" market, which is practically the nation's top market segment, will be required to exercise high level of governance equivalent to those of major markets overseas, and set the required ratio of outside directors at one third or more.

According to the Organisation for Economic Co-operation and Development (OECD), the ratio of female directors at large Japanese companies is 11%, which is less than one half of the OECD's average of 27%. The revised Code calls to disclose "skill matrix," which lists the experiences and abilities of the senior management.

Companies listed on the Prime market will be encouraged to disclose assumed impacts of the climate changes on them. The revised Code will urge disclosure that is consistent with the recommendations of the Task Force on Climate-related Financial Disclosures (TCFD) established by the financial regulatory authorities of major countries. In Japan, more than 400 organizations support the recommendations.

For the issue on human rights, the Code requires issuers to further tackle these matters in positive and proactive manner.

The return on equity (ROE) of major Japanese companies at the end of March 2021 was about 6%, which is way behind in comparison with 13% in the U.S. The upcoming reform will make clear which companies can cope with international challenges and attract foreign and domestic investors' money. The CEO of International Corporate Governance Network (ICGN) points out that strengthening disclosure of cross-shareholdings and having assessments of the board of directors by external parties will be issues to be considered further.

Information compiled from Nikkei Shimbun, Tokyo Stock Exchange & Mizuho research

4. Preparation for the revision of articles of incorporation towards a full online AGM

A growing number of companies are considering to amend their articles of incorporation to allow shareholders meetings to be held entirely online, reports Nikkei Shimbun, Japan's leading financial daily. In the wake of the coronavirus outbreak, the current Diet session has been discussing a bill to revise laws to allow full online shareholders meetings. Based on this, some companies submitted proposals for amending the articles of incorporation at their AGM in June 2021. This would significantly changes the ways AGMs are held, as it would make it more convenient for shareholders living in remote places. On the other hand, the movements toward full online AGMs also shed lights on some unique issues that are associated with online facility, such as protection of shareholder rights and smooth communication.

The Companies Act has been interpreted to require companies to set up a physical venue for AGM and to rule out "full online AGMs" at present. During last year's peak season in the midst of rapid spread of COVID-19, companies wanted the events to be held entirely online, but actually, only some AGMs took place in hybrid style, at a physical venue and online. About 100 companies, or 4% of the total, held "hybrid AGMs". About 90 companies, or about 4% of the

total, held “virtual observation type” AGM which can be viewed online, while 9 companies, or less than 1%, held “virtual attendance type” AGM in which shareholders may vote and ask questions online.

As it is time consuming to amend the Companies Act for this purpose, the government planned to achieve the goal by amending the Act on Strengthening Industrial Competitiveness (Act). The amendment of this Act was promulgated on 16 June this year and part of the Act including the section to enable a full online shareholders meetings was enforced on the same day.

Online AGMs are not just for infection prevention. It makes it easier for shareholders living in remote areas to attend the meetings and to attend more than one meeting on the same day. The head of responsible investment group at an asset management company says, "We think it is a solution for both social challenges, digital transformation (DX) and coronavirus crisis.”

On the other hand, there are many issues to be solved. One is the risk of undermining shareholder rights, such as questions to the management. Indeed, a U.S. voting advisory company recommended to vote against a consulting company’s proposed amendment to the articles of incorporation, stating that the amendment may hinder meaningful exchanges between shareholders and the management.

A legal counsel says "Shareholders should be concerned that companies may take advantage of shareholders’ absence at the venue and intentionally select questions they want to deal with." An officer in charge of Responsible Investment at an asset management company says “The online meeting has good and bad points. If it may significantly damage shareholders' rights, we would not support implementation of full online AGM at the election of directors in the following year.”

It is also important to ensure communications infrastructure to work properly during the meeting. Companies should tackle issues such as validity of resolutions that were made while the AGM was in the midst of communication malfunction, which affected the exercise of voting rights, and how companies can ensure proper identity verification to prevent impersonation.

In overseas, full online meetings have gained popularity under the pandemic. An operating system management company based in the U.S. supported 1,957 shareholder’s meetings in 2020, which is 6 times more than the previous year, and 98% of which were fully online. Starting from Delaware in 2000, about 30 states in the U.S. have approved online AGMs. This rapid spread of online AGM is owing to well-organized relevant legislation and deep understanding of both issuers and shareholders in this regard that have existed long before the COVID-19 breakout.

But even in the U.S., the global front runner of online AGMs have some concerns. In July 2020, the Council of Institutional Investors (CII), etc. called on the U.S. Securities and Exchange Commission (SEC) to urge companies to check and review their practices by expressing their concern that companies may restrict the participation of some shareholders, such as not allowing asking questions. One of the largest public pension fund in the U.S. also opined that online meetings should be held only as a supplement to the face-to-face meetings.

Information compiled from Ministry of Economy, Trade and Industry, Nikkei Shimbun & Mizuho research

II. New Equities Listing Approvals

Listing Date	Name of Company	ISIN Code	MKT
Jun-29	OMNI-PLUS SYSTEM	JP5702090001	M
Jun-29	Waqoo	JP3992050009	M
Jun-30	Ogic Group	JP3172280004	P
Jun-30	Plus Alpha Consulting	JP3832700003	M
Jul-01	REFINVERSE Group	JP3974820007	M
Jul-01	Mercuria Holdings	JP3860160005	T
Jul-01	Densan System Holdings	JP3551440005	T / N
Jul-06	BCC	JP3799790005	M
Jul-08	Colan Totte	JP3305920005	M
Jul-14	DN HOLDINGS	JP3548840002	T
Jul-16	LaKeel	JP3967020003	M
Jul-20	ASIRO	JP3118600000	M
Jul-21	LANDNET	JP3968860001	J
Jul-27	CIRCULATION	JP3310050004	M
Jul-28	Brains Technology	JP3831430008	M
Jul-29	Delivery Consulting	JP3549360000	M
Jul-30	AIMECHATEC	JP3105350007	T

**Information compiled based on postings from the TSE (T), Mothers (M), NSE (N)、FSE (F), SSE (S) & JASDAQ (J), Tokyo Pro Market (P)*

***Board lot size is unified to 100*

III. Foreign Ownership Limit Ratio

Click for up-to-date FOL information:
http://www.mizuhobank.com/service/custody/actions.html

Please visit our Custody homepage on the Web at:
http://www.mizuhobank.com/service/custody/index.html