Guidebook for Leveraging Foreign Capital to Enhance Corporate Value

(Provisional Translation)

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Ministry of Economy, Trade and Industry

Part 1: Basic Knowledge for Leveraging Foreign Capital

1. Overview of leveraging foreign capital

2. Benefits of leveraging foreign capital for Japanese companies

3. Cautionary points upon leveraging foreign capital and associated risks

Part 2: Five Basic Actions Towards Leveraging Foreign Capital

1. Overview of Five Basic Actions towards leveraging foreign capital

2. Each Stage: Five Points

Successful case studies: Specifics of the Basic Actions taken in actual cases

Introduction

1 Why leveraging foreign capital is important today?

With the pace of change in the market environment accelerating in recent years, companies are finding it increasingly difficult to respond quickly to the changes and achieve business growth solely by using internal resources. In addition, Japan's share of the global market is declining due to its aging population, declining birthrate, and shrinking population. Therefore, for Japanese companies to achieve sustainable business growth in the future, it is essential to capture growing overseas markets.

Against this background, it is becoming increasingly important for Japanese companies that are seeking to enhance their corporate value to capture the vitality of foreign markets and businesses. To this end, the companies should avoid excessive self-reliance and instead promote collaboration with foreign entities and open innovation.

As a form of collaboration with foreign entities, accepting investment from such entities, including foreign operating companies with advanced management know-how, global networks, and advanced foreign technologies and business models as well as foreign private equity funds (hereinafter, accepting foreign investment from those foreign entities is called "leveraging foreign capital" or "foreign capital utilization"), would be an option for Japanese companies. However, Japanese companies tend to face a significant psychological hurdle when considering whether to accept investment from foreign entities, a situation that has kept them lagging behind their foreign competitors in terms of leveraging foreign capital.[1] Therefore, the Ministry of Economy, Trade and Industry (METI) has formulated and published "Case Studies Relating to the Use of Inbound M&A Transactions"[2] and "Case Studies relating to Collaborations and Joint Ventures between Japanese and Foreign Companies in Japan"[3] in order to raise awareness widely about the advantages associated with leveraging foreign capital.

Because of such effort, along with the fruition of investment projects by foreign companies targeting Japanese companies, Japanese companies' awareness of the viability of leveraging foreign capital has been enhanced, but it has been also pointed out that Japanese companies have not yet become sufficiently familiar with specifically how to leverage foreign capital or what kind of cautionary points should be taken into account. In addition, given the intensified global competition to attract foreign capital among countries and the capital market reforms aimed at enhancing corporate value in Japan, it is becoming even more important for Japanese companies to consider leveraging foreign capital.

Therefore, in order to provide a clearer picture of what leveraging foreign capital means and enable Japanese companies to consider specific projects for leveraging foreign capital as one of the options for enhancing corporate value, this "Guidebook for Leveraging Foreign Capital to Enhance Corporate Value" (hereinafter referred to as the "Guidebook") has been formulated based on discussions held by the "Study Group on Leveraging Foreign Capital to Enhance Corporate Value," which was established by METI. The Guidebook is expected to be used by a wide range of people, including executives of Japanese companies, and be helpful for enhancing Japanese companies' corporate value through leveraging foreign capital.

2 Importance of leveraging foreign capital as management strategy

Companies must consider various management strategies in order to enhance corporate value in a sustainable manner in light of medium- and long-term strategies and management challenges. Among those strategies, leveraging foreign capital (foreign capital utilization) can make it possible to incorporate management know-how and foreign networks possessed by foreign investors and advanced foreign technologies and business models. Therefore, leveraging foreign capital can be an effective management strategy option for Japanese companies aiming to achieve overseas business expansion, maintain and strengthen competitiveness, and create innovations in an efficient and effective manner while using external management resources as well.

When considering whether or not to leverage foreign capital, it is necessary for corporate executives to make the decision after giving comprehensive consideration to advantages, cautionary points, risks associated with foreign capital utilization, and potential investors' investment track records, among other factors, and compare that strategy with other management strategies. The key to maximizing the effects of foreign capital utilization is to take the following steps with the involvement, and under the leadership, of the executives: conducting persistent negotiation with foreign investors; carefully providing information to employees and business partners; and implementing business

[1] According to an international comparison of the status of foreign capital utilization, regarding Out-In M&A, which refers to investment by foreign operating companies in domestic companies, both the number and the value of transactions (as a proportion of nominal GDP) in Japan are at a lower level than in other countries. In particular, the value of Out-In M&A transactions (as a proportion of nominal GDP) in Japan is around a ninth of the level in the United States and a forty-fifth of the level in the United Kingdom. (Source: Calculated from UNCTAD World Investment Report, The World Bank)

[2] METI (April 2023) "Case Studies Relating to the Use of Inbound M&A Transactions." Hereinafter referred to as the "Inbound M&A Case Studies."

[3] METI (April 2024) "Case Studies relating to Collaborations and Joint Ventures between Japanese and Foreign Companies in Japan." Hereinafter referred to as the "Collaboration Case Studies."

integration work after the acceptance of investment through dialogue with the investors based on the relationship of trust.

3 Outline of the Guidebook

The Guidebook provides information as follows:

- **Part 1: "Basic Knowledge" that should be gained before considering a specific project leveraging foreign capital**
- **Part 2: "Five Basic Actions" expected of Japanese corporate executives at the time of leveraging foreign capital**

In the Guidebook, leveraging foreign capital refers to accepting investment from foreign operating companies or foreign private equity funds (PE funds), regardless of the investment ratio (both majority investments and minority investments[4] are included).

4 Target users of the Guidebook

The Guidebook is targeted mainly at executives of Japanese companies who are interested in leveraging foreign capital or executives of Japanese companies who are at an early stage in considering leveraging foreign capital. It has also been compiled as a reference for intermediary players that support Japanese companies considering or implementing foreign capital utilization (e.g., investment banks, securities companies, banks, and consulting firms).

Figure 1：Outline of the Guidebook

Part 1: Basic Knowledge for Leveraging Foreign Capital

1. Overview of leveraging foreign capital
Types and trends of foreign capital utilization, structure of players, standard processes, and use of intermediary players

2. Benefits of leveraging foreign capital for Japanese companies
Advantages of leveraging foreign capital
Comparison with other management strategies (business alliances, In-Out M&As)

3. Cautionary points upon leveraging foreign capital and associated risks
Cautions at the time of collaborations
Risk of damaging corporate value
Compliance with the Foreign Exchange and Foreign Trade Act
Responsibilities upon accepting investment
Other cautionary points

Part 2: Five Basic Actions Towards Leveraging Foreign Capital

1. Overview of Five Basic Actions towards leveraging foreign capital
Basic Actions expected of Japanese corporate executives to enhance the benefits of leveraging foreign capital

2. Each Stage: Five Points
(1) Clarify strategies and identify options
(2) Through examination of management strategies that can deliver medium- to long-term value
(3) Proactive and independent negotiation with consideration given to value sources and risks
(4) Dissemination of positive messages to employees and business partners
(5) Trust building and realization of the value through ongoing dialogues

Successful case studies
- Chugai Pharmaceutical Co., Ltd.
- TAKAMI Co., Ltd.
- Kito Corporation
- PLAID Inc.
- Hitachi Metals Techno, Ltd. (currently, SENQCIA Corporation)

[4] Majority and minority investments are terms that represent the percentage of management control of a company in terms of voting rights in the case of M&A transactions. Majority investment refers to control of 50% or higher, while the minority investment refers to control of lower than 50% (source: RECOFDATA Corporation, MARR Online; majority investment: https://www.marr.jp/yougo/detail/175; minority investment: https://www.marr.jp/yougo/detail/174) (Available in Japanese).

Part 1:

Basic Knowledge for Leveraging Foreign Capital

Part 1 describes basic knowledge that should be gained by Japanese companies before considering specific projects for leveraging foreign capital. Specifically, Part 1 explains the types and trends of foreign capital utilization, and the structure of players, standard processes, benefits, cautionary points, and associated risks, among other items.

Part 1: Basic Knowledge for Leveraging Foreign Capital

1. Overview of leveraging foreign capital

1-1. Types of foreign capital utilization

Foreign capital utilization can be classified into the following three patterns according to the size of Japanese companies accepting investment and the parent-subsidiary relationship (investment in a parent or a subsidiary), among other factors: "acceptance of investment by large enterprises themselves," "acceptance of investment by small and medium-size enterprises (SMEs)," and "acceptance of investment by subsidiaries, etc." The overviews of those patterns are as described in Figure 2.

Figure 2: Types of foreign capital utilization

Pattern	Overview
Pattern A **Acceptance of investment by large enterprises themselves**	■ Mainly large enterprises (presumably listed companies) accept foreign capital as part of growth strategy.
Pattern B **Acceptance of investment by middle-market companies and SMEs**	■ Mainly middle-market companies and SMEs (presumably unlisted companies) accept foreign capital for the purpose of business succession in cases where successors are otherwise absent, or in order to achieve further business development by incorporating external capital, rather than on their own.
Pattern C **Acceptance of investment by subsidiaries, etc.**	■ Subsidiaries or business divisions within a group company accept foreign capital. In particular, this pattern applies to business transfer, which refers to selling subsidiaries or business divisions within a group company (carve-out) in order to review the business portfolio or to improve the financial position.

*MBO,[5] which has come into wider use in recent years, is classified as Pattern A.
*Foreign capital utilization[6] by startups is classified as Pattern B.

By investment type, foreign capital utilization can be classified into mergers, acquisitions, business transfers, capital participation, and expanded investment. The overviews of those types are as described in Figure 3.

[5] MBO stands for management buyout. It refers to the acquisition by a company's management team of the whole or parts of the company. In some cases, an MBO project is implemented with funds provided by the management team alone. However, with respect to MBO of listed companies in particular, a large amount of funds is required, so LBO (see Part 1 3-4) is used as an acquisition scheme in many cases. In this scheme, the management team raises capital in cooperation with a PE fund and borrows funds from financial institutions based on the capital thus raised in order to implement the acquisition (source: RECOFDATA Corporation, MARR Online : https://www.marr.jp/yougo/detail/178) <Available in Japanese>). In some cases, a foreign PE fund cooperates in raising capital.

[6] Japanese startups tend to launch business with IPO (see Footnote 16) in mind as an exit option, but it has been pointed out that a strategy that keeps in mind both IPO and M&A as exit options is important. (Source: METI, "FY2023 Survey on Commissioned Industrial and Economic Research Projects <Survey for Growth of Startups>")

Figure 3: Summary of foreign capital utilization classified by investment type[7]

Type of investment	Overview (from RECOF M&A Database)
Merger	• When two or more companies become a single company under a merger agreement. A merger (share transfer/creation of a holding company) is the process of creating a joint holding company through a share transfer and integrating the companies
Acquisition	• Acquisition of more than 50% of shares. This includes cases of 50% or less of share acquisition, if management is controlled. These can also include underwriting new capital, acquiring from existing shareholders, exchanging shares, and granting shares • In the case of a company divesture where the divesting company becomes the parent company of a successor company, or when a merger results in the parent company of a consolidated company becoming the parent company of a surviving company, these may also be considered as acquisition
Business transfer	• The transfer of a "business" consisting of assets, employees, goodwill, etc. The integration of existing businesses between two companies may also be included • In principle, company divestures are classified as business transfers. However, this does not include cases where the successor company becomes a subsidiary
Capital participation	• Acquisition of 50% or less of shares. However, this does not include cases where the company becomes a subsidiary. Capital participation is implemented through underwriting of capital increases or acquisition of shares from existing shareholders. Limited to the first time of acquisition
Investment expansion	• The acquisition of additional shares of 50% or less by the party providing a capital participation. However, if the investor already owns more than 50% of the shares or if the company is a subsidiary, acquisition of additional shares is excluded from the category of acquisition or investment expansion

[7] Source: METI, "Collaboration Case Studies." The source material was prepared on the basis of RECOF M&A Database.

1-2. Trends of foreign capital utilization

Looking at the numerical trends regarding foreign capital utilization, compared with 10 years ago, the number of transactions in which Japanese companies accepted foreign investment (Out-In) has roughly tripled to a record high level and the value of those transactions has become around five times as large (both figures are in terms of the three-year moving average) (Figure 4). Meanwhile, by investment ratio, the number and the value of transactions have increased with respect to both majority investments (mergers, acquisitions, and business transfers) and minority investments (capital participation and expanded investment) (Figures 5 and 6).

Figure 4: The number and value of transactions in which Japanese companies received foreign investment (the three-year moving average)[8]

*The total of majority and minority investments (merger, acquisition, business transfer, capital participation, and investment expansion).

(Unit: number of transactions) (Unit: 1 billion yen)

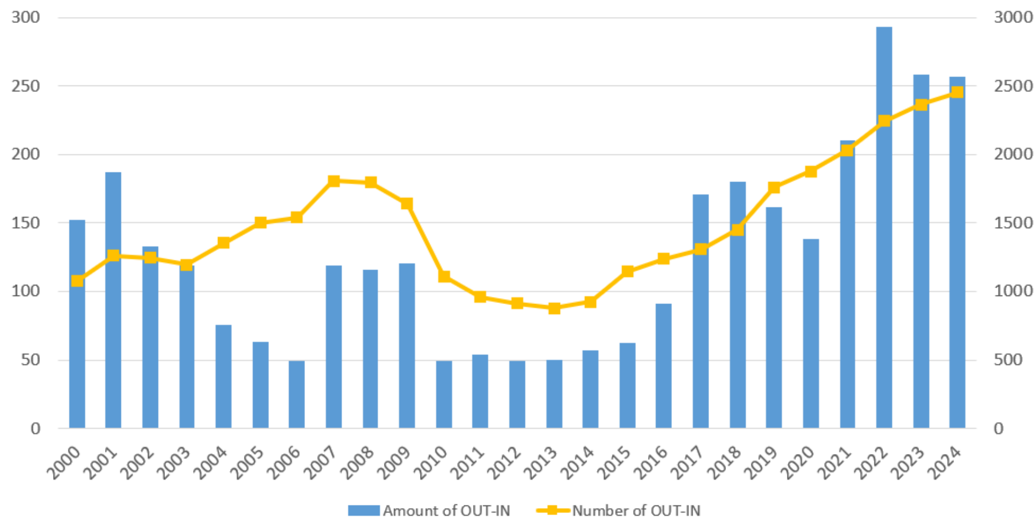
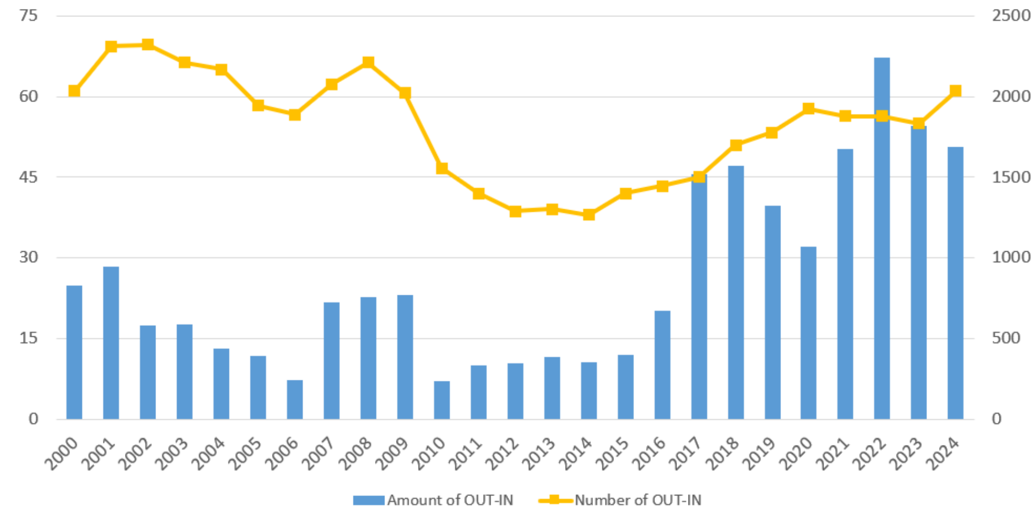


Figure 5: The number and value of transactions in which Japanese companies accepted foreign investment (the three-year moving average)

*The data below cover only majority investments (merger, acquisition, and business transfer)

(Unit: number of transactions) (Unit: 1 billion yen)

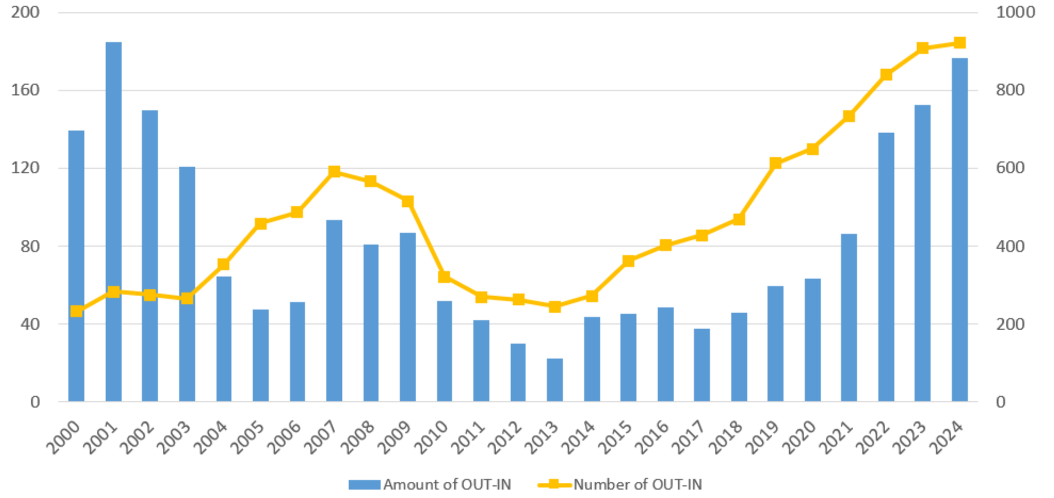


[8] Source: Prepared from RECOF M&A Database (excluding the sale of foreign subsidiaries by Japanese companies; including projects whose transaction value has not been disclosed). The annual value of transactions may vary from year to year depending on the presence or absence of large-scale projects, so the three-year backward moving average was used. The three-year backward moving average represents the value obtained by adding to the average for the relevant year the averages for the two previous years and by dividing the value thus arrived at by the number of years, that is, 3. (e.g., the three-year backward moving average for 2024 represents the average for the three years from 2022 to 2024). The same metric was used in Figures 5 to 9.

Figure 6: The number and value of transactions in which Japanese companies accepted foreign investment (the three-year moving average)

*The data below cover only minority investments (capital participation and investment expansion)

(Unit: the number of transactions) (Unit: 1 billion yen)

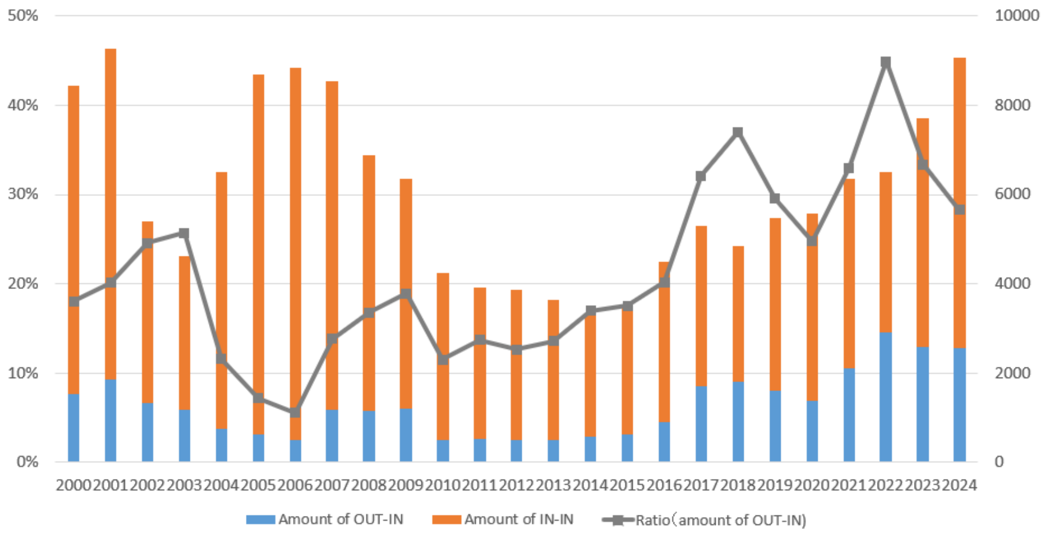


Of the total value of transactions[9] regarding Japanese companies' acceptance of investment, the share of the acceptance of foreign investment by Japanese companies (Out-In) has likewise increased compared with 10 years ago.

Figure 7: The value of investments accepted by Japanese companies and the ratio of foreign investment (the three-year moving average)

*The total of majority and minority investments (mergers, acquisitions, business transfer, capital participation, and expanded investment)

(Unit: %) (Unit: 1 billion yen)



[9] This number represents the total of the value of investments accepted by Japanese companies from other Japanese companies (In-In) and the value of investments accepted by Japanese companies from foreign investors (Out-In).

Figure 8: The ratio of foreign investments to the total value of investments accepted by Japanese companies (the three-year moving average)

*The data below cover only majority investments (mergers, acquisitions, and business transfers)

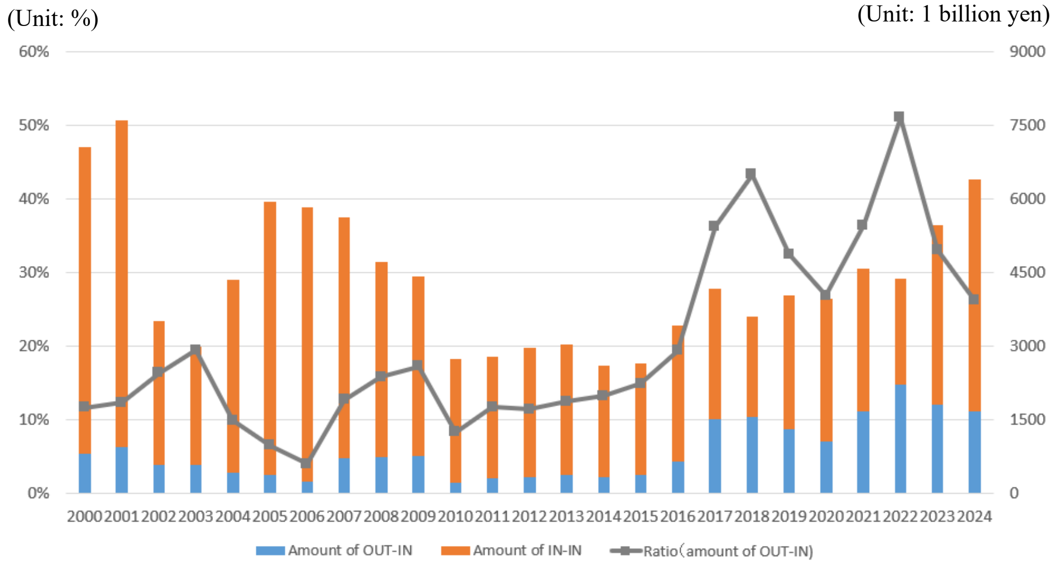
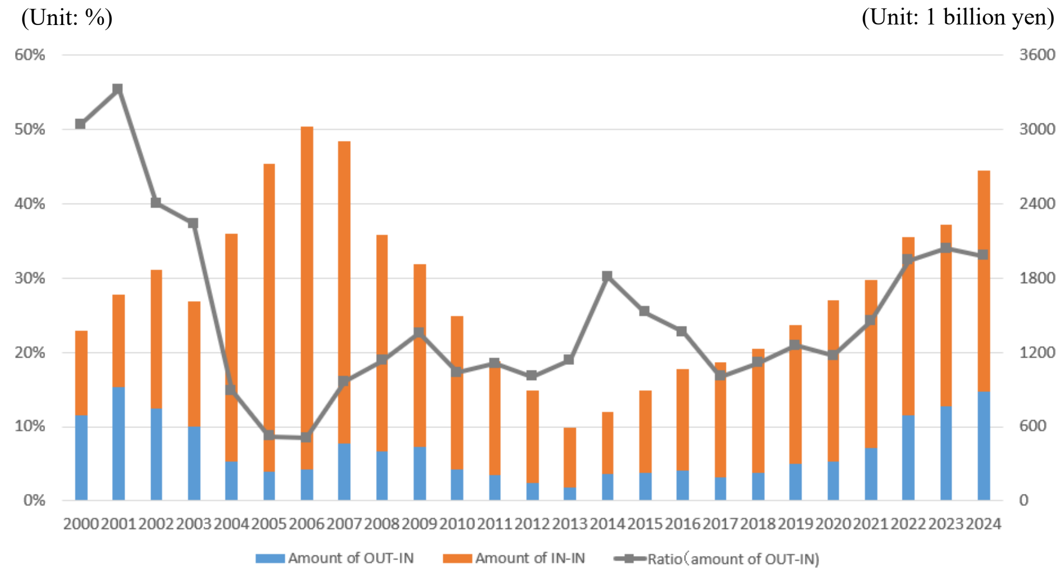


Figure 9: The ratio of foreign investments to the total value of investments accepted by Japanese companies (the three-year moving average)

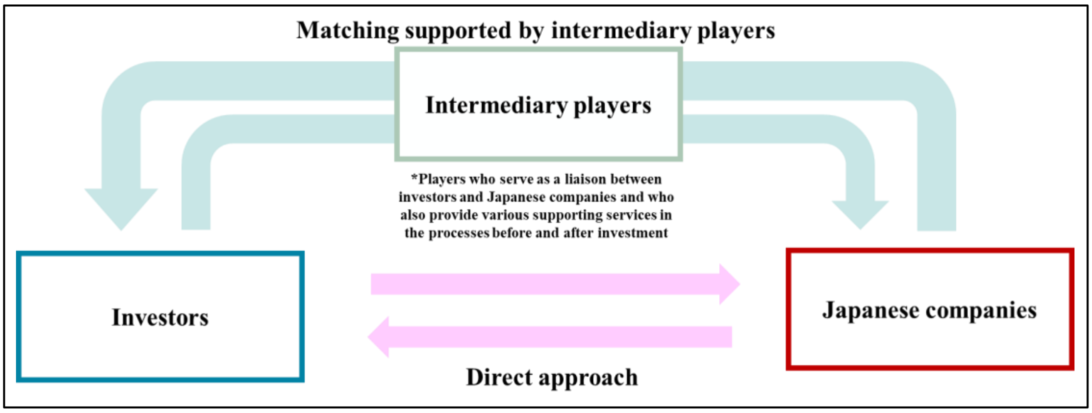
*The data below cover only minority investments (capital participation and expanded investment)



1-3. Players involved in foreign capital utilization

Among the major players involved in foreign capital utilization are investors (foreign operating companies and foreign private equity funds), Japanese companies, and intermediary players (e.g., investment banks, securities companies, banks, and consulting firms). This section describes the overviews of those players, including differences as to the roles they play in foreign capital utilization.

Figure 10: Overview of players involved in foreign capital utilization



1-3-1. Investors

Investors involved in foreign capital utilization can be classified broadly into "foreign operating companies" and "foreign PE funds[10]." Hereinafter, foreign operating companies and foreign private equity funds are collectively referred to as "foreign investors."

In order to smoothly implement the processes of foreign capital utilization and maximize the effects, it is important for Japanese companies to engage in collaboration after understanding the characteristics and the investment purposes of foreign investors.

■ Foreign operating companies

<Overview>

- Foreign operating companies as referred to in the Guidebook are companies whose headquarters function for practical business affairs is located outside Japan (including companies which have accepted investment from foreign investors and which have obtained corporate registration in Japan (so-called foreign-affiliated companies)).
- Foreign operating companies would invest in Japanese companies with the aim of achieving their own business expansion and increasing their own corporate value and on the premise of holding shares in the long term.

<Investment strategy>

- The two major purposes of investment in Japanese companies by foreign operating companies are (i) obtaining sales channels in the Japanese market and (ii) utilizing assets, services, technologies, brands, etc. possessed by Japanese companies.
- <Obtaining sales channels in the Japanese market> Foreign operating companies aim to provide their own goods and services by obtaining sales channels in Japan that are possessed by Japanese companies through investment in those companies.

[10] Other foreign investors include, for example, foreign government-affiliated investment funds and family offices (a family office is an organization that provides asset administration and investment services to wealthy families that own an amount of assets higher than a certain level).

- <Utilizing assets, services, etc.> Foreign operating companies seek to utilize assets, services, technologies, brands, etc. possessed by Japanese companies through investment in those companies. The Japanese companies can provide their own goods and services globally by utilizing foreign sales channels possessed by the foreign operating companies.

<Methods of research and approach>

- In many cases, foreign operating companies present investment proposals to potential investee companies after conducting independent research focusing mainly on large enterprises (presumably listed companies), for which a relatively large amount of disclosure information is available.
- Some foreign operating companies look for potential investee companies among middle-market companies and SMEs (presumably unlisted companies) when synergy effects[11] are expected.
- In some cases, foreign operating companies approach potential investee companies through investment banks or other intermediary players, which compile a list of potential investee companies after receiving from the foreign operating companies information such as their image of investment target companies and investment criteria.

<Type of involvement in deal-making>

- At many foreign operating companies, global headquarters have the decision-making authority regarding investment. On the other hand, in some cases, their Japanese subsidiaries propose potential investment target companies in a bottom-up process, followed by a meticulous investment feasibility study by global headquarters and implementation of investment. Therefore, executives in charge of negotiation at foreign operating companies are mainly Japanese who belong to Japanese subsidiaries or global headquarters, or foreign nationals who belong to global headquarters.[12]

■ Foreign PE funds

<Overview>

- PE funds invest in companies (mainly for the purpose of acquiring management control) based on funds collected from domestic and foreign institutional investors, among other investors, while leveraging funds borrowed from financial institutions, etc. and enhance the companies' corporate value through various measures during a medium-term investment period of around five to seven years. Among the specific measures that may be taken to enhance corporate value are, for example, monitoring investee companies (setting key performance indicators and identifying the respective effects of individual measures on EBITDA),[13] reinforcing the management team, hiring personnel with professional skills, developing a governance system, designing a compensation incentive system, and business transformation.[14]

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[11] Effects generated through integration between companies and between business divisions.
[12] At Japanese subsidiaries of foreign operating companies, a division or section responsible for conducting negotiations with Japanese companies as potential investee companies has the decision-making power regarding consultations about investment in some cases but does not have that power in other cases. In the former cases, consultations about foreign capital utilization tend to proceed relatively smoothly. When approaching or consulting with a foreign investor about possible investment, it is worth considering in which part of the organizational structure of the investor the decision-making power lies.
[13] EBITDA stands for Earnings Before Interest, Taxes, Depreciation, and Amortization. This is a profit metric calculated by adding interest expense and depreciation cost (tangible and non-tangible) to pretax profit. EBITDA, which represents cash income during a certain year, is used for the evaluation of corporate value in relation to M&A transactions.
[14] Ogura, Motohiro, and Yamamoto, Keisuke (2023), *Konsaru Ga 'Tsugi Ni Mezasu" Pii Ii Fando no Sekai*, Cross Media Publishing (Impress), and Hako, Fuminari, Yamada, Yusuke, and Matsushita, Akira (2018), *Seicho to Shoukei no Tame no Pii Ii Fando Katsuyo no Kyokasho*, Toyo Keizai Inc.

- PE funds, whose shareholding period is not fixed, ultimately sell shares at the so-called "exit" stage after enhancing the corporate value of investee companies. Profits are distributed to investors out of funds collected through the sale of shares in investee companies. The main methods of share sale are selling to other businesses or other PE funds,[15] and listing on a stock exchange.[16]
- In the Guidebook, PE funds whose headquarters function is located abroad are referred to as foreign PE funds.

<Types of foreign PE funds>

- Foreign PE funds conducting activity in Japan can be classified into the following three types: (i) "Japan-specific funds," whose portfolio (the group of investee companies) is comprised exclusively of Japanese companies; (ii) "Asia funds," whose portfolio is comprised of Asian companies, including Japanese ones; and (iii) "global funds," whose portfolio is comprised of companies operating globally, including in Japan.
- Different foreign PE funds have expertise in different sectors (e.g., digital technology and health services) and possess networks in different countries and regions.

<Investment strategy>

- Usually, foreign PE funds make investment decisions from the viewpoints of (i) investment size per project, (ii) projections for growth, stability and investment returns, and (iii) risks.
- Foreign PE funds compile a list of hundreds of potential investee companies (long list) from the abovementioned viewpoints and based on their own strict investment criteria and narrow down the long list to a list of dozens of potential investee companies (short list) after several rounds of screening. They make investment decisions after approaching short-listed Japanese companies.

<Methods of research and approach>

- Like foreign operating companies, in many cases, foreign PE funds directly approach Japanese companies that are under consideration as potential investee companies. Not only large enterprises but also middle-market companies and SMEs may be potential investee companies.
- Foreign PE funds look for potential investee companies in Japan using networks possessed by their individual investment officers as well as by banks, securities companies and other intermediary players.
- In some cases in recent years, Japanese companies made the first move to approach and consulted with foreign PE funds about possible deals such as going private and selling individual business divisions.

<Type of involvement in deal-making>

- Many foreign PE funds operating actively in Japan have Japanese business establishments and employ Japanese workers. Therefore, in many cases, executives in charge of negotiation on the side of foreign PE funds are Japanese, and in that respect, there is no difference from the case of domestic PE funds.

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[15] Sale from one PE fund to another is also a frequently observed scheme (so-called secondary buyout).

[16] This scheme is usually called an initial public offering (IPO). IPO refers to the transition from a situation where a stock company is owned by a small group of shareholders, including its owner, and where free transfer of shares is restricted (private company) to a situation where the company is owned by a large and unspecified number of people as a result of listing on a financial product exchange and where its shares may be freely traded on the stock market. (Source: Japan Exchange Group)

✓ <Column 1> Assessment of the Japanese market by foreign PE funds

Usually, foreign PE funds make investment decisions from the viewpoints of (i) investment value per project, (ii) projections for growth, stability and investment revenue, and (iii) risks. Their assessment of the Japanese market from those viewpoints is as follows.[17] Generally speaking, while the investment value per project is small, the Japanese economy is relatively stable and can be regarded as an attractive investment target when the balance between the investment revenue and risks is taken into consideration.[18]

<Investment value>
The Japanese economy is the fourth largest in the world, but the investment value per project is small in Japan compared with those in the United States, the United Kingdom and other major economies.

<Growth, stability and investment revenue>
While many Japanese companies are facing challenges such as business portfolio reforms,[19] expanding abroad, and strengthening the management base, PE funds encourage the enhancement of corporate value by making available measures to address those challenges. For PE funds, Japan is a market from which investment revenue can be expected because there are many Japanese companies with significant growth potential.

<Risks>
Amid the growing international geopolitical risks, the relative stability of the Japanese economy and society compared with other countries is attracting attention.

1-3-2. Japanese companies

Strategies that Japanese companies as classified by corporate size are expected to adopt when leveraging foreign capital are shown below. When Japanese companies formulate management strategy, they rarely focus on foreign capital utilization from early on. Usually, Japanese companies consider leveraging foreign capital in parallel with various other management strategies, including accepting investment from other Japanese companies or domestic PE funds.

■ Large enterprises

<Strategy for leveraging foreign capital>

- Large enterprises (presumably listed companies) leverage foreign capital through the following two strategies in many cases.

(i) Accept investment from foreign investors for purposes such as executing management strategy by incorporating advanced management resources of those investors or going private with consideration given to the cost of maintaining listing.

(ii) Implement business transfer by selling subsidiaries or business divisions within groups (carve-out) in order to transform the business portfolio or to improve the financial position.

[17] Source: Prepared with the results of interviews conducted by METI as a reference.
[18] It has been pointed out that Japan's PE market is attractive for foreign investors for the following reasons: the market has achieved growth in recent years and has room for further growth; Japanese companies have large room for improving their business performance; and the valuation of corporate value of Japanese companies is relatively low. (Source: "Overview of the Private Equity Market in Japan," (Japan Private Equity Association))
[19] A business portfolio refers to the mix of businesses which a company operates while allocating management resources to it.

<Methods of research and approach>

- Some large enterprises proactively approach foreign investors, including business partners.
- In some cases, large enterprises are approached by investment banks, securities companies and other intermediary players as well as by foreign investors who are existing business partners because such enterprises disclose corporate information more widely than middle-market companies and SMEs.

<Type of involvement in deal-making>

- In some cases, large enterprises have designated divisions/sections focusing on implementation of investment in other companies and are therefore well-experienced in investing in foreign operating companies.

■ **Middle-market companies and SMEs**

<Strategy for leveraging foreign capital>

- At many middle-market companies and SMEs (presumably unlisted companies), founders and executives sell their own shares in order to ensure business succession in cases where successors are otherwise non-existent or to achieve business expansion by leveraging investment from other companies, rather than on their own.

<Methods of research approach>

- Some middle-market companies and SMEs proactively approach foreign PE funds through securities companies, for example.
- In many cases, middle-market companies and SMEs are not within the targeted scope of search for potential investee companies by investment banks, securities companies and other intermediary players, so they may be approached for potential investment only in relatively few cases.

<Type of involvement in deal-making>

- In few cases, middle-market companies and SMEs have designated internal divisions/sections focusing on implementation of investment in other companies.

1-3-3. Intermediary players

In foreign capital utilization, intermediary players such as investment banks and securities companies serve as a liaison between investors and Japanese companies. In some cases, intermediary players also conduct the following various support operations (hereinafter “advisory services”) in the processes before and after investment on behalf of companies considering or implementing foreign capital utilization: helping to develop management strategy, selecting potential investee companies; providing advice concerning the evaluation of corporate value (enterprise value); proposing appropriate investment schemes; and assisting the development of strategy for contract negotiation. Japanese companies would be able to obtain a clearer picture of what leveraging foreign capital means through those support services by intermediary players and their awareness-raising activities (holding of workshops and seminars). This section explains the characteristics of major intermediary players and their roles in leveraging foreign capital.

■ **Investment banks**

- Investment banks provide companies, mainly large enterprises that would consider accepting or implementing investment, with advisory service regarding large-scale projects.

■ **Securities companies**

- In some cases, securities companies have an investment banking division that provides advisory service to companies, mainly large enterprises that would consider accepting or implementing investment.

■ **Independent advisors**

– Independent advisors are players who do not belong to any particular financial institution group. In some cases, independent advisors provide advisory service to companies, mainly large enterprises that would consider accepting or implementing investment.

■ **Large commercial banks**

– Some large commercial banks have a designated division/section focusing on investment that provides advisory service to companies that would consider accepting or implementing investment. In some cases, large commercial banks provide investors with loans for the investment purpose (including leveraged buyout (LBO) loans)

■ **Regional banks**

– Some regional banks have a designated division/section focusing on investment that provides advisory service to companies that would consider accepting or implementing investment. Similar to large commercial banks, regional banks provide investors with loans for the investment purpose (including LBO loans) in some cases. On the other hand, regional banks have limited points of contact with foreign investors compared with other intermediary players.

■ **Consulting firms**

– Consulting firms provide consulting services in the processes of foreign capital utilization. The area of expertise differs from one consulting firm to another. For example, some consulting firms have an advantage in supporting strategy development, while others excel in providing IT- and human resource-related support in the post-investment integration process.

1-3-4. Other professionals

In the field of foreign capital utilization, there are professionals who provide various support services in the processes before and after investment. This section explains the characteristics of those professionals and their roles in leveraging foreign capital.

■ **Law firms**

– Law firms provide advice in the process of investment from the selection of potential investee companies to post-merger integration, including advice related to investment schemes (investment types) and legal advice throughout the investment process. They also engage in contract negotiations relating to the investment and prepare a draft investment contract, among other services. When the investment value is large, law firms also provide advisory services related to takeover bids, auctions, and foreign legal systems.

■ **Financial advisors and tax accountant firms**

– In the due diligence (DD) process that is explained in the later section herein, financial advisors or tax accountant firms often conduct the examination of those Japanese companies that would consider accepting investment from the viewpoints of financial and tax affairs. Moreover, in the post-investment integration process, financial advisors or tax accountant firms often support integration from the viewpoints of financial and tax affairs.

1-4. Basic processes of foreign capital utilization

This section explains the basic processes of foreign capital utilization. Broadly speaking, the main processes are strategy development, matching, negotiation, agreement in principle, due diligence (DD), final agreement/deal closing, and post-merger integration (PMI). The outlines of the main processes are as shown in Figure 11.

While the periods of time required for the processes may differ on a case-by-case basis, it can be said that the period from the start of negotiation to final agreement takes approximately six months to one year.

Figure 11: Basic processes of foreign capital utilization
(as seen from the viewpoint of Japanese companies)[20] [21]

Involving the management team	Strategy development	Develop medium- to long-term management strategy for realizing value creation management and conduct an analytical comparison of foreign capital utilization and other management strategies.
Involving a limited group of members within the company	Matching	An investor and a Japanese company are matched through an intermediary player or other professionals. In some cases, one party approaches the other party directly, without using an intermediary player.
	Negotiation	When a potential investee company has been chosen through matching, decisions are made regarding basic contractual matters, including the terms, such as the price, the assets to be sold, the treatment of employees, and the scheme of the deal (e.g., the transfer of shares or business divisions) in accordance with the objectives of each party.
	Basic agreement	When agreement has been reached through negotiation on general terms, such as the price, the assets to be sold, and the treatment of employees, a basic agreement incorporating those terms would be concluded.
	Due diligence (DD)	The investor thoroughly examines the actual status of financial and legal affairs and business of the Japanese company, confirms the matters covered by the basic agreement, and assesses business risks while using professionals. Regarding the results of examination and assessment, the Japanese company may be required to provide representations and warranties in some cases. In other cases, the Japanese company may similarly conduct due diligence concerning the actual status of the investor.
	Final agreement/ deal closing	Negotiations are conducted once again regarding the points assessed in due diligence or the matters over which decisions were reserved at the time of the basic agreement, followed by the conclusion of a final agreement.
Involving many employees	Post-merger integration (PMI)	The investor and the Japanese company implement integration works in order to maximize the effects of foreign capital utilization. Specifically, the work includes reviewing and revising the Japanese company's governance system and the provisions concerning the responsibilities and authorities (matters required to be reported and approved) and addressing management affairs (e.g., personnel and labor affairs, accounting and financial affairs, legal affairs, and IT systems). The degree of involvement of the investor may vary according to the investment purpose. For example, the investor may be directly involved in the management of the Japanese company in order to realize synergy in some cases, while in other cases, the investor's purpose may be to earn financial revenues and may therefore be involved little in management. Moreover, the Japanese company may be required by the foreign investor to conform to a different mindset and culture, in terms of key performance indicators (KPIs), quality standards and decision-making process, for example.

* Companies conduct an analytical comparison concerning various management strategies, including foreign capital utilization, in order to resolve management challenges. Therefore, the "strategy development" and "matching" processes are not always implemented in that order but may be implemented simultaneously in some cases.

* The processes following the "negotiation" stage, which are implemented after the partner (potential partner) for foreign capital utilization has been determined, are implemented in the order described above in principle.

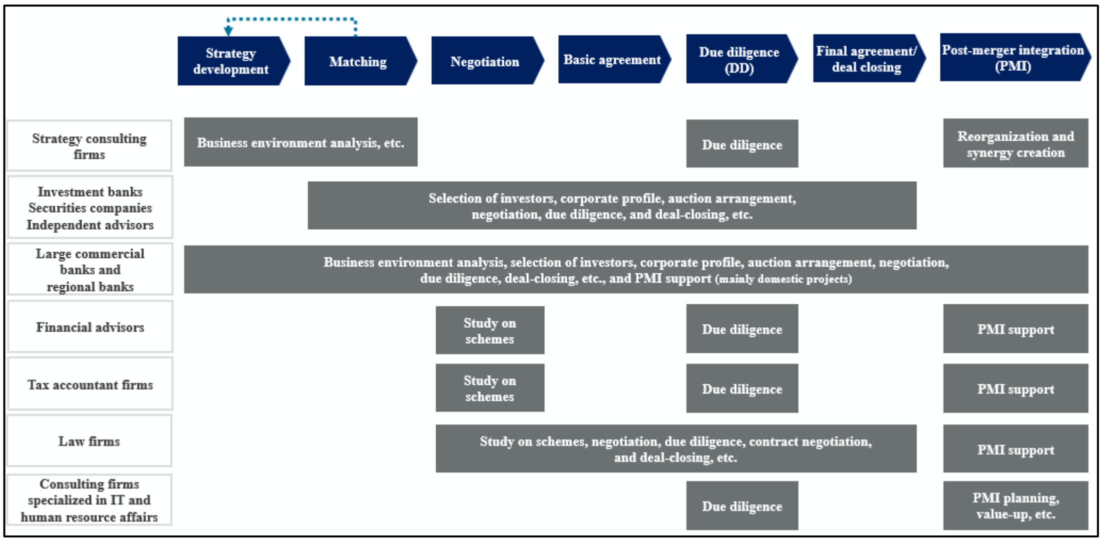
[20] Source: Prepared with the results of interviews conducted by METI as a reference.
[21] Representations and warranties refer to statements and assurances made by one party (Party A) of a transaction to the other party (Party B) to the effect that facts related to Party A and facts related to the specifics of the subject matters of a contract (e.g., businesses, legal position, financial conditions, and other factual statements and legal relationships) that are presented at a certain point in time are true and accurate. There is an insurance product known as warranty and indemnity insurance, which is intended to cover economic losses that a contract party may suffer due to damages demanded for violation of the representations and warranties specified in the contract.
(Source: RECOFDATA Corporation, MARR Online.
Representations and warranties: https://www.marr.jp/yougo/detail/158) (Available in Japanese)
Warranty and indemnity insurance: https://www.marr.jp/yougo/detail/159) (Available in Japanese)

1-5. Employing intermediary players in leveraging foreign capital

As leveraging foreign capital requires expertise in a broad array of areas, it is important for companies considering or implementing foreign capital utilization to proceed with each process while receiving advice from appropriate intermediary players, etc.[22] in such individual process. In particular, regarding processes such as the selection and evaluation of partner companies (matching), negotiation, due diligence (DD), and post-merger integration (PMI), it is important to employ intermediary players, etc. that can provide professional support in light of differences between Japan and foreign countries given that there may be differences in business practices, taking into account that the investor is a foreign entity.

Figure 12 describes the roles of major intermediary players, etc. in the standard processes of foreign capital utilization.

Figure 12: The main roles of intermediary players, etc. (as seen from the viewpoint of Japanese companies)[23]



* Depending on the specifics of the businesses of intermediary players, etc., and the nature and scale of projects, among other factors, the ranges of the roles that can actually be covered may be different from the ones indicated above.

Different intermediary players, etc. have advantages in different areas, regions, sectors, and project sizes and have different track records of supporting activities with respect to similar projects. Therefore, in order to select appropriate intermediary players, etc., it is important for Japanese companies considering or implementing foreign capital utilization to maintain points of contact with various intermediary players, etc. on a regular basis and to grasp their respective advantages, the quality of their executives, and the fee level,[24] among other factors.

After selecting appropriate intermediary players, etc., it is important to engage in periodic communication with them. Japanese companies can obtain useful advice from intermediary players, etc. by holding candid discussions about the direction of their management strategy, internal decision-making process, the terms over which they cannot compromise, cautionary points, and risks, among other items.

[22] In the Guidebook, “intermediary players,” explained in 1-3-3 and “other professionals,” explained in 1-3-4, are collectively referred to as “intermediary players, etc.”
[23] Prepared with the results of interviews conducted by METI as a reference.
[24] The fee level and the fee calculation method may vary from one intermediary to another.

2. Benefits of leveraging foreign capital for Japanese companies

2-1. Advantages of leveraging foreign capital

Leveraging foreign capital could be a particularly effective option for Japanese companies in case of aiming to achieve overseas expansion, maintain and strengthen competitiveness, and create innovations because doing so enables them to incorporate advanced management resources possessed by foreign investors. This section explains the specifics of the advantages of leveraging foreign capital. The explanations classify the advantages into those common to investment from foreign operating companies and investment from foreign PE funds and those peculiar to investment from each of those two categories of foreign investors.

2-1-1. Advantages of leveraging foreign capital for Japanese companies

Below summarizes the advantages of leveraging foreign capital for Japanese companies from the viewpoints of management base, employees, and business operations.[25]

<Management base>

- Advancement of governance and financial management through the acquisition of global knowledge and management know-how and introduction of a governance system

  Japanese companies can advance their governance and financial management and improve their productivity and profitability by acquiring global knowledge and superior management know-how possessed by foreign investors, including an investment approach and business portfolio management that are conscious about KPI[26] management and ROIC[27] and by introducing a governance system.

- Enhancement of organizational systems through personnel support

  Japanese companies can enhance their organizational systems by using extensive networks of personal connections possessed by foreign investors and by incorporating external personnel who may be best suited to resolve the challenges faced by the companies.

<Employees>

- Enhancement of employee motivation by introducing excellent personnel-related systems

  Japanese companies can enhance employee motivation by introducing superior personnel-related systems possessed by foreign investors, including a personnel management system, a highly transparent evaluation system, and stock option programs.

- Training and securing personnel with global skills

  Japanese companies can more effectively train employees to develop a global perspective and mindset by introducing training programs and through exchanges with foreign personnel with global skills. In addition, being affiliated with foreign businesses contributes to hiring personnel with global aspirations.

[25] Source: Prepared from "Inbound M&A Case Studies" and "Collaboration Case Studies." Here, the advantages common to investment from foreign operating companies and investment from foreign PE funds are summarized. For detailed information and example cases, see the relevant case studies.

[26] KPI stands for Key Performance Indicator. KPIs are important evaluation benchmarks to measure business performance. KPIs are set in quantitative terms as interim targets on the path toward achieving ultimate goals.

[27] ROIC stands for Return On Invested Capital. ROIC is an indicator representing the percentage of profits generated through capital invested by a company relative to the amount of invested capital.

<Business operations>

- Expansion of foreign sales channels using a global network

  Japanese companies can expand foreign sales channels and increase their overseas sales ratios and their presence abroad by utilizing networks and brand power possessed by foreign investors.

- Utilization of products, services, and business models in advanced foreign sectors

  Japanese companies can expand the range of products and services that they handle and achieve quality improvement by incorporating technology, know-how, and business models related to products and services in advanced foreign sectors, and information concerning industry trends and competitors.

- Enhancement of growth investment

  By accepting investment from foreign investors, Japanese companies can enhance growth investment initiatives, including progressing capital expenditures, increasing research and development expenses, acquiring financial and human resources and know-how related to implementation of outbound M&As.

Figure 13: Advantages of foreign capital utilization by Japanese companies (common to both types of foreign capital utilization)

Management base	■ **Advancement of governance and financial management through the acquisition of global knowledge and management expertise and introduction of a governance system** ■ **Enhancement of organizational systems through personnel support**
Employees	■ **Enhancement of employee motivation by introducing excellent personnel-related systems** ■ **Training and securing personnel with global skills**
Business operations	■ **Expansion of foreign sales channels using a global network** ■ **Utilization of products, services, and business models in advanced foreign sectors** ■ **Enhancement of growth investment**

* Many Japanese companies may already be conducting initiatives to gain the abovementioned advantages on their own, but leveraging foreign capital would potentially strengthen their implementation capability and accelerate the realization of advantages.

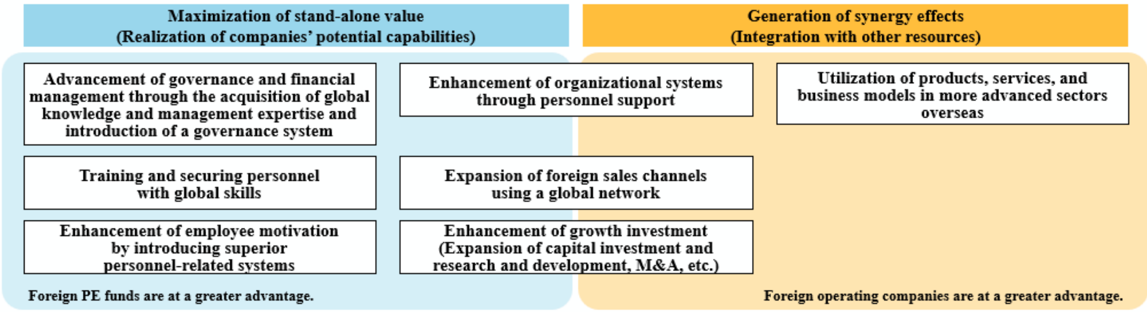
2-1-2. Different effects brought about by different types of foreign capital utilization

The advantages of leveraging foreign capital described above can be classified into (1) the maximization of the corporate value of Japanese companies solely through acceptance of investment from foreign investors (stand-alone value) and (2) synergy effects generated through collaboration between Japanese companies and foreign investors. Such classification can be subject to "whether the advantages represent the realization of the potential capabilities that the Japanese companies inherently possess" or "whether the results achieved through the combination of the management resources of the foreign investors and Japanese companies."

In particular, the expected effects differ depending on the type of foreign capital utilized. Investment from foreign PE funds can be more expected to maximize the stand-alone value of Japanese companies because it can contribute to the advancement of governance and financial management of the companies by enabling them to incorporate management know-how possessed by the PE funds.

On the other hand, investment from foreign operating companies can be more expected to generate synergy effects because it can contribute to innovation creation by enabling Japanese companies to incorporate technologies and business models possessed by foreign operating companies and by integrating the resources of the Japanese companies and foreign operating companies.

Figure 14: Types of foreign capital and effects[28]



✓ <Column 2> Value creation management

Japanese companies must develop business structures that enable them to earn profits globally, rather than continuing business-as-is, with a view to shifting to a growth-oriented economy. From that viewpoint, it is important for Japanese companies to adopt a management strategy that enhances corporate value in a sustainable manner by attracting expectations for growth through the development of strategy that should intensively pursue high added value, such as resolving social challenges, while securing a high level of capital efficiency and profitability (so-called value creation management).

Leveraging foreign capital enables Japanese companies to incorporate foreign capital, technologies, business models, networks and other assets. This strategy may lead to the enhancement of corporate value and the realization of value creation management through the following activities through the following effects:

- Optimizing the business portfolio using foreign capital;
- Improving capital efficiency and profitability through the advancement of management, global expansion, and an increase in growth investment; and
- Implementing growth strategy to thoroughly pursue high added value and fostering growth expectations through global expansion, innovation creation and an increase in growth investment.

Figure 15: Corporate strategies and value creation management

[28] Source: Prepared with the results of interviews conducted by METI as a reference.

✓ <Column 3> Empirical analysis concerning the effects of foreign capital utilization

Previous studies have shown that leveraging foreign capital could lead to the improvement of productivity and profitability for Japanese companies.

For example, Okubo et al. (2017)[29] indicated that among Japanese companies, the higher the foreign investment ratio is, the higher the export ratio is and the more positive the stance toward research and development investment is. That study also pointed out that in regions other than metropolitan areas such as Tokyo and Osaka, the foreign investment ratio also has a positive correlation with the export ratio and research and development investment.

According to an analysis by Iwasaki (2013),[30] which covered Japanese manufacturing companies, the productivity of companies that accepted foreign investment rose and that foreign investment had positive effects on productivity at companies belonging to relevant industries, such as industries to which products were supplied from companies that accepted foreign investment.

Meanwhile, Kimura and Kiyota (2003)[31] showed that the effects on the business performance and the employment situation of Japanese companies varied according to the investment ratio when the companies received investment from foreign investors. Specifically, at companies with a foreign investment ratio of higher than 50%, productivity and profitability growth became apparent faster than at others. In addition, employment reorganization was observed at companies with a foreign investment ratio of 100% but was not statistically observable at companies with an investment ratio of lower than 100%.

On the other hand, some studies, such as Tanaka (2023),[32] found that investment by foreign companies does not necessarily generate positive effects for companies accepting the investment. In short, it is highly likely that the effects vary on a case-by-case basis.

[29] Okubo Toshihiro, Alexander F. Wagner, Kazuo Yamada (2017), "Does Foreign Ownership Explain Company Export and Innovation Decisions? Evidence from Japan", RIETI Discussion Paper Series 17-E-099.

[30] Iwasaki, Yuto (2013), “Tainai Chokusetsu Toushi no Sangyoukan Supiru Oobaa Kouka,” Bank of Japan Working Paper No. 13-J-9.

[31] Kimura, Fukunari, and Kiyota, Kozo (2003), “Nihon Kigyou ni Okeru Gaishi Hiritsu to Kigyou Keiei: Paneru Deeta wo Mochiita Jisshou Kenkyuu,” Hanazaki, Masaharu, and Teranishi, Jyuro, eds., *Kooporeeto Gabanansu no Keizai Bunseki: Henkakuki no Nihon to Kinyu Kiki Go no Higashi Ajia*, University of Tokyo Press, pp.159-181.

[32] Tanaka, Kiyoyasu (2023), “Gaishi Kigyou ni Yoru Nihon Kigyou no Emu Ando Ei Kouka,” RIETI Discussion Paper Series 23-J-011.

2-2. Comparison with other management strategies

Leveraging foreign capital contributes to the enhancement of corporate value by Japanese companies, but doing so is merely one of the management strategy options available. Therefore, it is important for Japanese companies to conduct an analytical comparison with other management strategies while giving consideration to the challenges that they face and the constraints on management resources, among other factors. This section provides basic information necessary for analytical comparison with management strategies that may be similar to foreign capital utilization, such as business alliances with foreign businesses and, In-Out M&As.

2-2-1. Business alliances

<Overview>

- Business alliances refer to collaborations between Japanese and foreign operating companies that do not involve capital partnership (e.g., alliance contracts). Through business alliances, foreign operating companies provide management support, including the provision of management know-how, foreign networks, and advanced foreign technologies and business models. In some cases, synergy effects, such as overseas expansion and the maintenance and enhancement of competitiveness, can be expected.

<Characteristics>

- Unlike foreign capital utilization, business alliances do not involve investment, so it is possible to develop alliance relationships quickly. For Japanese companies that feel uneasy about leveraging foreign capital (particularly majority investment), forming a business alliance could become an effective option for examining the reliability and track records of foreign operating companies that may be considered as potential investors and whether or not objectives and visions can be shared.
- On the other hand, as a general rule, there are risks such as the possibility that the commitment to collaboration may weaken because it is easy to cancel alliance relationships and the possibility that decision-making may be delayed because negotiation would be required at each time when a specific collaboration measure needs to be implemented.

✓ <Column 4> Investment ratio in foreign capital utilization projects

When Japanese companies consider leveraging foreign capital, setting a foreign investment ratio is an important factor for consideration. In principle, foreign PE funds would be presumed to seek majority investment, while some foreign operating companies could be presumed to seek minority investment.

As majority investment (investment that provides more than 50% of all voting rights) involves the transfer of management control, the degree of involvement of the foreign investor in the management of the Japanese company accepting the investment (investee company) is larger. Accordingly, the investee company would be able to benefit from advanced management resources possessed by the foreign investor to a greater degree, so the advantage of leveraging foreign capital may be larger.

As minority investment (investment that provides less than 50% of all voting rights) does not involve the transfer of management control, the involvement of the foreign investor in the management of the Japanese investee company may be smaller. Accordingly, the advantage of leveraging foreign capital that could be enjoyed by the investee company may be smaller, but it is possible to reduce the risks that may arise from inconsistencies in strategies between the Japanese company and the foreign investor. Therefore, for Japanese companies that feel uneasy about accepting foreign investment, accepting minority investment could be an effective option for examining whether or not the potential foreign investor will become a reliable partner as a step toward possible acceptance of majority investment in the future.

Even so, as accepting minority investment means that a certain degree of equity stake would be possessed by the foreign investor, a greater involvement of the foreign investor in the management of the Japanese company would be expected compared with the case of business alliances.

2-2-2. In-Out M&As

<Overview>

- For Japanese companies, investing in foreign operating companies (In-Out M&A[33]), rather than accepting investment from foreign operating companies, may also be an option for enhancing corporate value by incorporating foreign vitality. In-Out M&A may enable Japanese companies to incorporate foreign networks possessed by foreign operating companies in which they invest and advanced foreign technologies and business models and use those resources as the driving forces of global growth. In short, In-Out M&A can be expected to generate effects similar to those brought about by foreign capital utilization.
- The number and value of In-Out M&A transactions fell during the COVID-19 pandemic but are back on an upward trend once again.[34]

<Characteristics>

- Through In-Out M&A, Japanese companies can be directly involved in the management of foreign operating companies. However, in addition to allocating a large amount of funds, it is necessary to devote a significant amount of management resources to the investment process and the development and maintenance of management systems after investment. This would set a certain hurdle, particularly for middle-market companies and SMEs.[35]
- On the other hand, regarding In-Out M&A shares many cautionary points common to foreign capital utilization, including the significant difficulty of using its effects to achieve corporate growth due to differences in language, culture, and legal system and the difficulty of finding appropriate partners.

33 METI convened the Study Group for Japanese Companies' M&A Overseas in FY2017 and, together with experts, conducted a study related to M&A-related challenges faced by Japanese companies and summarized points of attention and cases of effective use of In-Out M&A in "Nine Actions for Successful Cross-border M&A." METI also compiled the "Extra Edition" of "Nine Actions for Successful Cross-border M&A," which focused attention on three positions—CFO (chief financial officer), executive officer in charge of legal affairs, and outside director—that, along with the CEO, hold a critical key to taking advantage of cross-border M&A to achieve corporate growth. Based on the contents of "Nine Actions for Successful Cross-border M&A," "Extra Edition" described, in more detail and more clearly, the roles and actions expected of those three positions in accordance with the respective responsibilities and expertise of the positions in order to provide more specifically and practically useful information on how companies should proceed with cross-border M&A.

34 In the period between 2020, when the COVID-19 pandemic started, and 2024, the annual number of In-Out M&A transactions involving majority investment (mergers, acquisitions, and business transfers) increased by 81 and the value of those transactions expanded by around 4.5 trillion yen. In 2024, the number of In-Out M&A transactions involving majority investment (mergers, acquisitions, and business transfers) was 313 and the value of those transactions was 7.9 trillion yen. (Source: Calculated from RECOF M&A Database; there are transactions whose value has not been disclosed.)

35 It is important that Japanese companies, based on their strategies, identify feasible projects that are in accordance with their characteristics (e.g., company size, investment amount, M&A experiences and track records, and the scope of tolerable risks (whether there is the risk that the deterioration of the management situation at an acquired company may have a material impact on the parent company)). If Japanese companies go ahead with In-Out M&A without fully recognizing their own current situation, it is seen as highly likely that they will be involved in transactions involving risks that go beyond the scope of tolerable risks or transactions with an overly high acquisition price. (Source: METI (March 2018; published), A report by the Study Group for Japanese Companies' M&A Overseas)

3. Cautionary points upon leveraging foreign capital and associated risks

Leveraging foreign capital has many advantages, but in order to benefit from the advantages to the maximum possible extent, it is necessary to take appropriate steps, such as sufficiently recognizing cautionary points and risks associated with foreign capital utilization and specifying items that should address those points and risks in a final contract,[36] including the share transfer agreement, while consulting with professionals.

Below explains major cautionary points and risks associated with foreign capital utilization, such as "Cautions at the time of collaborations," "Risk of damaging corporate value," "Compliance with the Foreign Exchange and Foreign Trade Act," and "Responsibilities upon accepting investment." In particular, cautionary points and risks that should be taken into consideration vary according to the type of foreign investors. This section also describes the types of foreign investors (foreign operating companies and foreign PE funds) to which particular consideration should be given with respect to the cautionary points and risks.

"Cautions at the time of collaborations," "Risk of damaging corporate value," and "Responsibilities upon accepting investment" are not only cautionary points and risks to foreign capital utilization but also apply to domestic capital utilization and other types of management strategies.

3-1. Cautions at the time of collaborations

Operating companies/ PE funds

3-1-1. Effects on employment and working conditions

Leveraging foreign capital may have effects on employment and working conditions. For example, foreign investors may call for workforce restructuring associated with reorganization, or important workers and executives may leave the company because of differences in management policy. Despite the above, it should be emphasized that even when Japanese companies have become foreign affiliates as a result of accepting investment from foreign investors, compliance with Japanese labor laws is required.

To mitigate the effects on employment and working conditions, it is important to make as much effort as possible to obtain prior agreement from foreign investors with respect to maintaining employment and working conditions through consultations and negotiations. Such effort includes requesting the retention of employees and measures related to the treatment of important employees and executives (such as key players for the companies).

In addition, upon accepting investment, the Japanese companies would be able to take advantage of foreign capital utilization to enhance employee motivation and to train and secure personnel with global skills, and it is desirable to actively introduce a superior personnel evaluation system and employee training programs for developing global skills that are possessed by foreign investors.

Operating companies

3-1-2. Rationalization of business facilities

In some cases, after Japanese companies have accepted investment from foreign investors, the companies' factories, research and development centers and other facilities may be closed and consolidated with the investors' facilities from the viewpoints of business rationalization and enhancement of corporate value. In particular, when there are redundancies between investors and Japanese companies in terms of facilities and functions, the tendency to implement business rationalization would be stronger.

While leveraging foreign capital sometimes requires a certain degree of business reorganization, some Japanese companies adhere to the high level of their technological expertise through joint research with research institutions, universities, and other organizations in the neighborhood of their facilities in some cases, and thus, from the viewpoint of maintaining and enhancing their corporate value, it is desirable for Japanese companies to thoroughly examine the objectives and validity of facility rationalization plans. In particular, when the investor exercises initiative in rationalization of facilities, the objective is to acquire the technologies, data, know-how, and manufacturing equipment

[36] This refers to a contract with a legally binding power that specifies the contents of a final agreement between the two parties in a M&A transaction. It is sometimes called a formal contract. Examples include a contract on the transfer of shares, a contract on the transfer of business, and a contract on a merger.

existing at the investee company's facilities in some cases. Before accepting investment, it is important to thoroughly examine rationalization plans in cooperation with appropriate professionals and to include, as necessary, a provision for maintaining facilities after investment in a final contract.

3-1-3. Change in and integration of corporate cultures and management policies

Operating companies/ PE funds

Particularly when foreign operating companies invest in Japanese companies, management problems could arise due to differences in corporate cultures, not to mention differences in language, compared with domestic investment in Japanese companies by other Japanese companies.[37]

Therefore, it is desirable for Japanese companies not only to recognize difference in corporate culture and check whether they share visions, including management policies and strategies, with foreign investors but also to build trust so that discussions can be held with a view to resolving challenges after accepting investment, such as coordinating each other's corporate culture,[38] introducing a new personnel management system, and promoting exchange of personnel, including executives and employees.

In some cases, through collaboration with foreign investors, Japanese companies may be required to carry out management reforms with a sense of speed. In that case, it is desirable to ensure careful communication, including explanations from executives to employees about visions, so that employees can keep up with the sense of speed.

3-1-4. Development of a system to seek approval from and report to investors

Operating companies/ PE funds

After Japanese companies have accepted investment from foreign investors, the companies may sometimes be required to develop a system to seek approval from and report to the investors as part of improvement of governance by the investors. In many cases, Japanese companies start consultations and deliberations on the development of such a system with investors before accepting investment.

It is desirable for Japanese companies to clarify as much as possible the matters subject to approval, consultation and reporting through consultations and deliberations with investors and thereby agree with them on the matters over which the Japanese side is granted discretion. Such agreement would lead to a smoother post-merger integration process.

[37] The following are examples of challenges that arise from differences in corporate culture.
(i) In some cases, Japanese companies make decisions outside meeting bodies through informal consensus-building processes, while foreign companies use meeting bodies for substantive discussions. As a result, discord may arise during the decision-making process.
(ii) In some cases, the scope of job duties is not clear-cut at Japanese companies, while it is clear-cut at foreign companies in many cases, and as a result, differences may arise in the perception of the division of work.
(iii) Differences in the attitude toward requests from individual customers may arise between Japanese and foreign operating companies.

[38] When coordinating the corporate cultures of the two sides, it is important to reach agreement with foreign companies on whether to resolve differences in culture through integration, or to respect the differences, and reflect the agreement in concrete actions, for example by providing explanations to employees or by clarifying the agreement in the form of institutional systems.

3-2. Risk of damaging corporate value

Operating companies/ PE funds

3-2-1. Unintended leakage of technologies, etc.

From the viewpoint of economic security, technological superiority is the most essential factor for maintaining Japan's autonomy and indispensability. Currently, for Japanese companies, preventing technology leakage should be treated not merely as a cost but as an investment for strengthening business infrastructure.

In this situation, there is the risk that malicious investors may cause Japanese companies' technologies and data to leak outside, or that an inappropriate licensing contract concerning intellectual property rights may put Japanese companies at a disadvantage.

Even when Japanese companies have accepted investment from foreign investors, intellectual property rights and other assets are not transferred to the investors as a natural course of events unless a comprehensive succession scheme, such as a merger or absorption split, is used. When investors plan to use Japanese companies' intellectual property rights, it is necessary for the Japanese companies to make appropriate judgment as to whether or not to grant rights to the foreign investors and as to the scope of rights to be granted from the viewpoint of technology leakage prevention.

Japanese companies may sometimes be requested to transfer intellectual property rights, etc. (including know-how and technologies that are not materialized into rights). In that case, it is necessary to ensure the value of those assets has been fairly evaluated. Furthermore, as there are cases in which malicious investors send personnel to serve as executives at Japanese companies in order to acquire the companies' intellectual property, it is important for Japanese companies to conduct a thorough investigation in advance as to the existence or non-existence of the right for investors to nominate executives and the scope of access by investors to intellectual property, etc.

First of all, it is important for Japanese companies to figure out whether or not potential foreign investors are appropriate as partners. It is desirable to understand potential foreign investors' investment purposes well and to thoroughly examine investment projects which such foreign investors have executed thus far.

In addition, in consultations concerning intellectual property rights, etc., Japanese companies considering foreign capital utilization should negotiate with potential foreign investors, while cooperating with appropriate professionals so as to ensure reasonable terms with respect to matters such as (i) the scope of licensing (technologies, products and services covered by licensing), (ii) the type of license (exclusive or non-exclusive), (iii) the number of years of license and the regions where the license is granted, (iv) licensing fees, and (v) prohibited activities, such as non-competition, and specify those terms in licensing contracts. The treatment of intellectual property rights may impact the evaluation of corporate value, which is necessary for negotiation. Therefore, it is desirable for Japanese companies to first consider the specifics of licensing terms that they can accept and then start negotiating licensing terms at an early stage in parallel to the price negotiation.

METI has published "Response to Economic Security Challenges (Private-Sector Best Practice Cases),"[39] which describes voluntary initiatives by Japanese companies to address economic security challenges, including technology leakage risk, and "Guidance on Technology Leakage Prevention," [40] which describes specific ways of preventing technology leakage. Japanese companies may refer to those reference materials as appropriate.

[39] METI (March 2025: last revised), "Response to Economic Security Challenges (Private-Sector Best Practice Cases)—Version 2.0—)"
https://www.meti.go.jp/policy/economy/economic_security/best_practice2.0.pdf (Available in Japanese)
[40] METI (March 2025: published), "Guidance on Technology Leakage Prevention Version 1." Version 1 covers measures against (i) technology leakage associated with the overseas expansion of production bases, and (ii) technology leakage through personnels.
https://www.meti.go.jp/policy/economy/economic_security/guidance.pdf (Available in Japanese)

3-2-2. Trade secrets

Operating companies/ PE funds

Japanese companies should implement appropriate information leakage control measures in order to prevent the leakage of their confidential information. For example, when disclosing confidential information to foreign investors to an extent necessary for implementing business operations, it is important to minimize information leakage risk by limiting the scope of confidential information subject to disclosure to a necessary minimum, not to mention by concluding a non-disclosure agreement.

In preparation for possible leakage of confidential information, it is also important for Japanese companies to implement confidentiality management measures necessary for receiving legal protection for trade secrets, so that actions based on the Unfair Competition Prevention Act (e.g., claiming compensation for damage) can be taken.

METI has published "Handbook for Protection of Confidential Information,"[41] which describes effective measures to prevent information leakage, and "Management Guidelines for Trade Secrets,"[42] which describes a minimum level of measures necessary for receiving legal protection for trade secrets. Japanese companies may refer to those reference materials as appropriate.

3-2-3. Non-competition obligation

Operating companies

When Japanese companies have accepted a non-competition obligation under contracts with foreign investors or have become subsidiaries of foreign investors thereby bearing a non-competition obligation as a result, Japanese companies may be prevented from engaging in their main businesses or adjacent businesses in the future, because, for example, particular business activities or businesses in some geographical areas may be prohibited. Therefore, when executing a contract, it is necessary for Japanese companies to examine, together with appropriate professionals, whether or not the contract would prevent them from engaging in such businesses.

3-2-4. Dis-synergies

Operating companies

Leveraging foreign capital may generate not only synergy effects but also negative effects known as dis-synergies. For example, leveraging foreign capital may cause customers to disassociate, or may create a situation where unifying prices for providing goods and services with the ones provided by foreign investors may lead to deteriorated trade terms with customers.

First of all, it is important for Japanese companies to recognize that such dis-synergies could occur. One possible option for Japanese companies is to formulate as concrete a concept as possible of what collaboration should emerge after leveraging foreign capital in the negotiation stage and to include, as contractual provisions, measures necessary for resolving the possible dis-synergies identified.

41 METI (February 2024: last revised), "Handbook for Protection of Confidential Information." https://www.meti.go.jp/english/policy/economy/chizai/chiteki/pdf/21_0127a.pdf
42 METI (March 2025; last revised), "Management Guidelines for Trade Secrets." https://www.meti.go.jp/english/policy/economy/chizai/chiteki/pdf/0813mgtc.pdf

3-3. Compliance with the Foreign Exchange and Foreign Trade Act

As various challenges emerge across the boundaries of national security and the economy, it is necessary for the Japanese government as a whole to strengthen economic security initiatives. When foreign investors make a certain amount of investments in Japanese companies engaging in a certain categories of business, or when Japanese companies export goods or provide technologies to foreign companies or non-residents, it is necessary to implement procedures in compliance with the Foreign Exchange and Foreign Trade Act.

3-3-1. System to review foreign direct investments

Operating companies/ PE funds

Sound foreign direct investments play an important role in the development of the Japanese economy, so it is necessary to further promote such investments. On the other hand, under the Foreign Exchange and Foreign Trade Act, based on the principle of free external trade, Japan implements a necessary minimum level of regulatory measures in certain cases, such as when investment from foreign investors could undermine national security. The regulatory measures include requiring foreign investors to submit a prior notification in such cases.[43]

3-3-2. Security export control

Operating companies/ PE funds

In some cases, when leveraging foreign capital, Japanese companies start exporting goods or providing technologies to foreign companies or executives and employees who are equivalent to non-residents. With respect to exports of cargoes or the provision of technologies that could interfere with the maintenance of international peace and security, it is necessary for Japanese companies to comply with regulations under the Foreign Exchange and Foreign Trade Act, such as obtaining permission from the Minister of Economy, Trade and Industry.

[43] METI, "Control of Inward Foreign Direct Investment by Ministry of Economy, Trade and Industry." https://www.meti.go.jp/policy/anpo/toushikanri/invest-control.html (Available in Japanese)

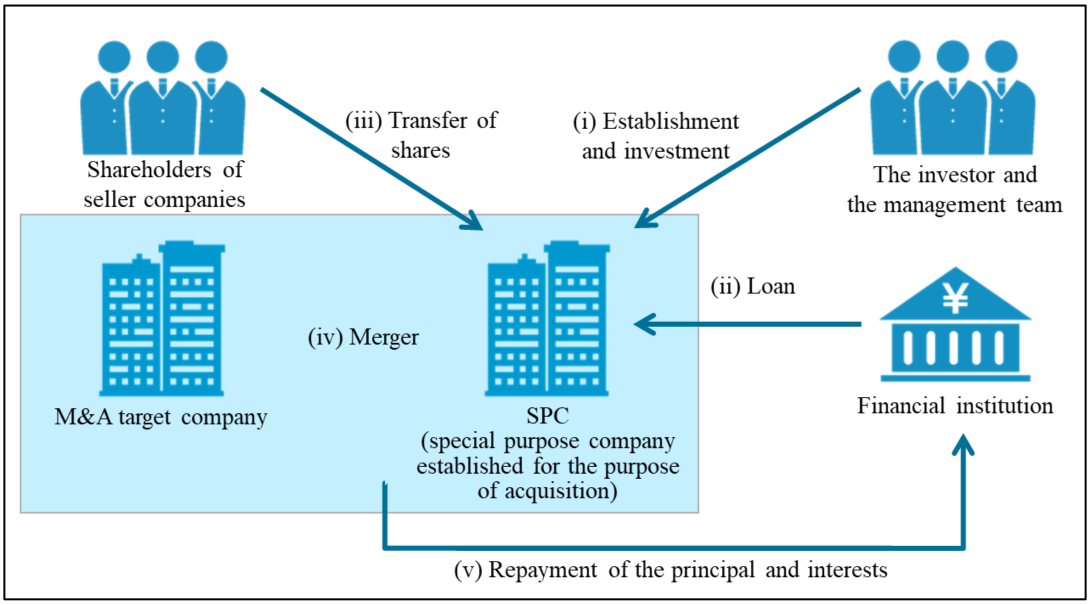
3-4. Responsibilities upon accepting investment (LBO loans)

PE funds

When PE funds invest in companies, they may raise some funds through bank borrowings using investee companies' assets and cash flow as collateral.[44] Such loans are known as LBO loans. LBO loans rely on cash flow generated by investee companies and take advantage of the companies' creditworthiness. As a result, PE funds can carry out large-scale M&A transactions while bearing a small financial burden.[45] On the other hand, the debts thus incurred are ultimately assumed by Japanese companies that have accepted investment.

Japanese companies whose debt ratio would increase should engage in communication with foreign PE funds about the feasibility of debt redemption at the time of negotiation in the process of foreign capital utilization.

Figure 16: LBO loan scheme[46]



[44] This investment scheme is known as LBO (Leveraged Buyout).
[45] Japanese Bankers Association (March 2024) "Report on Challenges Related to LBO Financing in Japan (FY2023)."
[46] Japanese Bankers Association (March 2024) "Report on Challenges Related to LBO Financing in Japan (FY2023)."

3-5. Other cautionary points (responses to laws, regulations, etc. related to investors)

Accepting investment from foreign investors may require Japanese companies to comply with foreign laws and regulations with which the foreign investors comply, such as competition laws in other countries. Moreover, in addition to complying with laws and regulations, Japanese companies may also be required to comply with the "business and human rights" concept,[47] environmental regulations, and diversity management, which have become increasingly important in recent years, at levels different from the levels required in Japan.

[47] In light of the growing social needs related to the relationship between business activity and human rights in recent years, in order to promote respect for human rights in corporate activity, the Japanese government formulated the National Action Plan on Business and Human Rights in October 2020. In addition, from the viewpoint of encouraging further efforts by Japanese companies, on September 13, 2022, the Japanese government formulated the Guidelines on Respecting Human Rights in Responsible Supply Chains, which are based on international standards such as the Guiding Principles on Business and Human Rights of the United Nations, the OECD Guidelines for Multinational Enterprises on Responsible Business Conduct, and the Tripartite Declaration of Principles concerning Multinational Enterprises and Social Policy of the ILO. In April 2023, the Japanese government formulated and published the Reference Material on Practical Approaches for Business Enterprises to Respect Human Rights in Responsible Supply Chains in order to make it easier for companies not yet engaging in the respect-for-human rights initiative, including many SMEs, to do so in accordance with the guidelines.

Part 2

Five Basic Actions

Towards Leveraging Foreign Capital

Part 2 explains the Five Basic Actions expected of Japanese corporate executives to enhance the effectiveness of leveraging foreign capital.

Part 2: Five Basic Actions Towards Leveraging Foreign Capital

1. Overview of Five Basic Actions towards leveraging foreign capital

Part 2 explains the Five Basic Actions expected of Japanese corporate executives to enhance the effectiveness of leveraging foreign capital. Specifically, below explains the key points for enhancing the effectiveness of leveraging foreign capital and actions to be taken in five of the basic processes of foreign capital utilization, namely (i) strategy development, (ii) matching, (iii) negotiation, (iv) final agreement, and (v) post-merger integration (PMI) while citing case studies as well.

Figure 17: Overview of the Five Basic Actions towards leveraging foreign capital

01	Strategy development	Clarify strategies and identify options. *Identify management challenges and consider not only leveraging foreign capital but also various other options in order to resolve the challenges.
02	Matching	Thorough examination of management strategies that can deliver medium- to long-term value
03	Negotiation	Proactive and independent negotiation with consideration given to value sources and risks
04	Final agreement	Dissemination of positive messages to employees and business partners
05	PMI	Trust building and realization of the value through ongoing dialogues

* Companies conduct an analytical comparison concerning various management strategies, including foreign capital utilization, in order to resolve management challenges. Therefore, the “strategy development” and “matching” processes are not always implemented in that order but may be implemented simultaneously in some cases.

* The processes that follow “negotiation,” which are implemented after the partner (potential partner) for foreign capital utilization has been determined, are implemented in the order described above in principle.

In order to understand the Basic Actions more in-depth, there are many situations that require the basic knowledge concerning foreign capital utilization that was described in Part 1. Part 1 also explains the basic knowledge that should be referenced when taking the Basic Actions. Therefore, it is desirable for readers to refer back to Part 1 as necessary.

2. Each Stage: Five Points

Basic Action 1: Clarify strategies and identify options

- Consider strategy for resolving management challenges in order to realize value creation management while examining the company's current situation.
- Consider various options for forward-looking management strategy, such as utilizing external management resources, including foreign capital utilization.

Basic Action 2: Thorough examination of management strategies that can deliver medium- to long-term value

- Thoroughly examine potential foreign investors as to whether they would be partners suited for the company to execute its medium- to long-term management strategy.
- Flexibly change course when the company has determined that other management strategies would be better suited to execute strategy.

Basic Action 3: Proactive and independent negotiation with consideration given to value sources and risks

- Proactively conduct persistent negotiation and dialogue.
- Secure the advantage of leveraging foreign capital for executing strategy and minimize risks and concerns related to cautionary points.

Basic Action 4: Dissemination of positive messages to employees and business partners

- Executives themselves should disseminate to stakeholders, such as employees and business partners, messages outlining the company's strategy and future vision.

Basic Action 5: Trust building and realization of the value through ongoing dialogues

- Share the perspective on PMI strategy with the investor and build trust so that candid discussions can be held in a transparent manner.
- Actively gain synergy effects and carry out organizational and management reforms.
- When the company's opinions conflict with the investor's opinions, work with the investor to figure out an approach better suited to realize value creation management.

Basic Action 1: Clarify strategies and identify options

- **Consider strategy for resolving management challenges in order to realize value creation management while examining the company's current situation.**
- **Consider various options for forward-looking management strategy, such as utilizing external management resources, including foreign capital utilization.**

<Key points for implementing the Basic Actions>

- When developing strategy, does the company hold dialogue with a wide range of stakeholders, including domestic and foreign investors as well as customers and incorporate their opinions?
- Has the strategy developed[48] by the company set numerical goals and timelines and clarified the challenges that must be overcome to plug the gap between the current situation and the goals?
- Is the company considering various options for forward-looking management strategy, such as utilizing external management resources, including foreign capital utilization, rather than tilting toward extreme self-reliance?
- When considering utilizing external management resources, does the company make a decision as to how much management autonomy and independence to maintain?
- Is the company taking into consideration the respective advantages, cautionary points and risks associated with the options and internal management resources and conducting objective evaluation as to which strategy is most feasible?

*Reference points
・<Column 2> Value creation management
・2-1. Advantages of leveraging foreign capital
・3. Cautionary points upon leveraging foreign capital and associated risks
・2-2. Comparison with other management strategies

[48] When developing strategy for realizing value creation management, it is also important to use the Guidance for Collaborative Value Creation 2.0, which is useful as a framework for considering value creation stories. The guidance can be viewed at the following URL.
https://www.meti.go.jp/policy/economy/keiei_innovation/kigyoukaikei/guidance_for_collaborative_value_creation_2.0_en.pdf

Basic Action 2: Thorough examination of management strategies that can deliver medium- to long-term value

- **Thoroughly examine potential foreign investors whether they would be partners suited for the company to execute its medium- to long-term management strategy.**[49]
- **Flexibly change course when the company has determined that other management strategies would be better suited to execute strategy.**

<Key points for implementing the Basic Actions>

- Is the company thoroughly examining foreign capital utilization as an option from the viewpoints mentioned below while employing intermediary players, etc.[50] as professionals as necessary?
- When a listed company is considering how to respond to an acquisition by a foreign investor in particular, is the company considering whether leveraging foreign capital contributes to the enhancement of corporate value and shareholders' common interests in light of the Guidelines for Corporate Takeovers,[51] among other reference materials?
- In the case of a carve-out, is the company examining options, including leveraging foreign capital, in light of the Practical Guidelines for Business Transformations,[52] when selecting the entity most likely to be the "best owner,"[53] which is most suited to realize the sustainable growth of the business to be sold?

Viewpoints regarding thorough examination of leveraging foreign capital (examples)

- The company should examine the suitability of leveraging foreign capital as a strategy for itself, while giving consideration to the advantages, cautionary points and risks associated with doing that.
- The company should examine the validity of leveraging foreign capital based on comparison with all other available management strategies, including going it alone and forming a business alliance.
- The company should consider what the most desirable investment ratio[54] is in view of the direction of its strategy and the purpose of leveraging foreign capital.
- The company should examine the validity of the potential foreign investor as a partner while giving comprehensive consideration to factors such as the type of foreign capital, the investment purpose,[55] the investment period (in the case of PE funds in particular), the details and the results of past investment projects.

***Reference points**
・1-3-1. Investors
・1-3-3. Intermediary players
・1-3-4. Other professionals
・1-5. Employing intermediary players in leveraging foreign capital
・2-1. Advantages of leveraging foreign capital
・2-2. Comparison with other management strategies
・3. Cautionary points upon leveraging foreign capital and associated risks
・<Column 4> Investment ratio in foreign capital utilization projects

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49 Such thorough examination helps to understand the behavioral principles of foreign investors and later facilitates negotiation and smooth PMI.
50 As for which intermediary players, etc. to choose, refer to Basic Action 3.
51 METI (August 2023). This was formulated in order to present the principles and best practices that should be shared on an economy- and society-wide basis with a view to developing fair rules regarding M&A transactions, mainly what actions should be taken by transaction parties in relation to acquisitions that obtain management control of listed companies. The guidelines present the three principles that should be respected in acquisitions of management control of listed companies in general (Principle 1: Principle of Corporate Value and Shareholders' Common Interests; Principle 2: Principle of Shareholders' Intent; and Principle 3: Principle of Transparency) in the "Principles and Basic Perspectives" chapter. Moreover, in the "Code of Conduct for Directors and Board of Directors regarding Acquisition Proposals" chapter, the guidelines describe phase-based approaches to the code of conduct for directors and the board of directors regarding acquisition proposals to obtain management control. In the "Increased Transparency Regarding Acquisitions" chapter, the guidelines describe how transparency in acquisitions should be improved from the perspective of both the acquiring party and the target company.
52 METI (July 2020: published) "Practical Guidelines for Business Transformations: Toward Transformation of Business Portfolio and Organization ("Guidelines for Business Transformations"). https://www.meti.go.jp/policy/economy/keiei_innovation/keizaihousei/pdf/20200731003-1.pdf (Available in Japanese)
53 This refers to a management entity that is expected to maximize corporate value in the medium to long term. (Source: The Guidelines for Business Transformations)
54 In cases where the company is to receive investment from a foreign investor with which it has not conducted any transaction in the past, or where synergy effects are expected to be generated even if the foreign investor is to be a minority shareholder, it is desirable to consider leveraging foreign capital with the possibility of starting collaboration with the investor by accepting minority investment as the first step.
55 Thoroughly examining how the company could contribute to the enhancement of corporate value by the foreign investor helps to understand the purpose of the investor and facilitates price negotiation and smooth PMI later.

Basic Action 3: Proactive and independent negotiation with consideration given to value sources and risks

- ■ **Proactively conduct persistent negotiation and dialogue.[56]**
- ■ **Secure the advantage of leveraging foreign capital for executing strategy and minimize risks and concerns related to cautionary points.**

<Key points for implementing the Basic Actions>

- ➢ Has the company determined "issues negotiable for compromise" and "issues non-negotiable for compromise" in light of its own value sources[57] based on the recognition that negotiation is a process of exploring a middle point where both sides can reach compromise?
- ➢ Is the company clearly explaining its "issues non-negotiable for compromise" to the investor rather than merely giving priority to the successful conclusion of negotiation?
- ➢ Is the company consulting with intermediary players, etc. as professionals in order to address cautionary points and associated risks, including working conditions, such as the maintenance of jobs for employees and the treatment of key players, and the reorganization of production facilities?
- ➢ When selecting intermediary players, etc. as professionals, is the company taking into consideration the following factors?
  - Factor 1: The areas and regions of expertise of intermediary players, etc.
  - Factor 2: The existence or non-existence of track records regarding similar projects
  - Factor 3: Professional knowledge of intermediary players, etc. concerning the industry to which the company belongs.
- ➢ Is the company committed to ultimately making decisions independently, rather than depending entirely on intermediary players, etc., based on the management team's sufficient understanding of the various terms of the whole deal that are addressed in the negotiation or are included among the agreed matters?
- ➢ Do the specifics of the agreed matters (e.g, the price, assets to be transferred, the treatment of employees, and specifics of investment plans after the acceptance of investment) contribute to the developed strategy?
- ➢ In the case of minority investment in particular, has the company negotiated and agreed on the provisions regarding the termination of the partnership?
- ➢ Has the company agreed with the investor with respect to the "direction of collaboration with foreign investors," such as an overall PMI policy, including the degree of the investor's investment in management, the specifics of collaboration, and concrete numerical targets to be achieved after the start of collaboration?

***Reference points**

・1-3-3. Intermediary players
・1-3-4. Other professionals
・1-5. Employing intermediary players in leveraging foreign capital
・3. Cautionary points upon leveraging foreign capital and associated risks
・<Column 4> Investment ratio in foreign capital utilization projects

[56] Patient negotiation and dialogue are also important for figuring out whether or not the investor is a reliable partner.

[57] This refers to important strengths that enable companies to secure their competitive advantage, such as internal infrastructure for creating human resources and technological expertise. As a reference for understanding the "value source", the Guidance for Collaborative Value Creation 2.0 states as follows: "If companies identify management resources, assets/liabilities that serve as the foundation for long-term sustainable value growth, and their relationships with stakeholders that are the key to maintaining their competitive advantages and enhance their efficiency by investing to maintain and strengthen these elements, the sustainability of their business models will improve."

Basic Action 4: Dissemination of positive messages to employees and business partners

■ **Executives themselves should disseminate to stakeholders, such as employees and business partners, messages outlining the company's strategy and future vision.**

<Key points for implementing the Basic Actions>

- Is the company aware of the possibility that employees and business partners may be concerned with changes to be brought about to the company resulting from foreign capital utilization (particularly majority investment) and considering measures to address such concerns based on consultations with the investor?
- After the final agreement,[58] did the company explain to employees and business partners the significance of leveraging foreign capital under its strategy and its future vision for the period after the acceptance of investment in order to remove their concerns?
- Is the investor disseminating information on future strategy and vision to employees and business partners as necessary?
- Is the company considering measures to raise awareness about executives' sense of purpose concerning foreign capital utilization among employees and business partners in order to promote PMI and corporate change after the acceptance of investment?

***Reference points**
・ 3. Cautionary points upon leveraging foreign capital and associated risks

[58] At the consideration and negotiation stages regarding foreign capital utilization, the scope of information sharing is limited to a small group of relevant parties, mainly executives, for the purpose of information control.

Basic Action 5: Trust building and realization of the value through ongoing dialogues

- **Share the perspective on PMI strategy with the investor and build trust so that candid discussions can be held in a transparent manner.**
- **Actively gain synergy effects and carry out organizational and management reforms.**
- **When the company's opinions conflict with the investor's opinions, work with the investor to figure out an approach better suited to realize value creation management.**

<Key points for implementing the Basic Actions>

- Has the company coordinated its overall policy,[59] including the scope and depth of PMI, with the investor's policy in light of the degree of the investor's involvement in management and specified in writing the contents of the agreement reached with the investor?
- Is the company creating opportunities for transparent information-sharing and exchange of opinions with the investor for the purpose of trust building while giving consideration to an appropriate level and frequency of those activities?
- Is the company responding to requests and instructions from the investor after giving consideration to differences in legal frameworks and culture between Japan and the home country of the investor and understanding the backgrounds to the investor's requests and instructions?
- Has the company formulated a specific action plan for gaining synergy effects by levering foreign capital and implementing organizational and management reforms after incorporating the foreign investor's rational and objective viewpoints
- Is the company considering an approach best suited to realize value creation management together with the investor in light of the "issues negotiable for compromise" and the "issues non-negotiable for compromise"?
- Since accepting investment from the foreign investor,[60] has the company continuously considered strategy and future vision?

*Reference points
・1-3-1. Investors
・1-4. Basic processes of foreign capital utilization
・3-1-3. Change in and assimilation of corporate cultures and management policies
・<Column 2> Value creation management

[59] In the case of majority investment in particular, sorting matters into those requiring consultations with and approval from investors when management decisions are made and those over which decisions can be made independently facilitates smooth integration.

[60] In cases where the investor is a foreign PE fund, the investment relationship is maintained only until the PE fund's exit, so it is unlikely that the investment relationship will continue for a long period of time. Even if the investor is a foreign business, the positions of the Japanese market and the Japanese company that has accepted investment under the investor's strategy may change with the passage of time in some cases.

✓ <Column 5> Cases of companies unable to achieve expected effects

While there are cases in which Japanese companies achieved business expansion and other effects by leveraging foreign capital, there are other cases in which expected effects were not achieved. In this column, we describe cases of companies unable to achieve expected effects from leveraging foreign capital as a reference for Japanese companies considering or implementing foreign capital utilization from now on. Measures cited in those cases are important not only in the case of investment from foreign investors but also in the case of investment from domestic investors.

Figure 18: Cases of companies unable to achieve expected effects

Process	Overview	Relevance to the Basic Actions (measures)
Matching	• The company had aimed to expand into foreign markets by leveraging foreign capital, but it failed in overseas expansion because **the "know-how necessary for expanding into foreign markets" that it had expected to incorporate from the investor was insufficient**.	• At the matching stage, **it is important to thoroughly examine** the investor's track records regarding investment, appropriateness as a partner, and the risks involved.
Negotiation	• Although fund-raising for the business reform was realized, **disagreement arose between the company and the investor over management policy**. As a result, it became difficult to implement fundamental business reform.	• At the negotiation stage, it is important to **hold sufficient negotiations and dialogues with the investor, thereby** minimizing frictions that may arise between the company and the investor after leveraging foreign capital and for implementing business reforms in cooperation with the investor.
PMI	• After leveraging foreign capital, the company **introduced the investing foreign company's management strategy as it was** in order to improve management efficiency, but that did not lead to any improvement of business performance. • **The execution of strategy after corporate integration made little progress** due to factors such as **a lack of thorough efforts to carry out long-term cost reform and failure to successfully adapt to Japanese business practices**.	• At the PMI stage, it is important for the Japanese company to **aim for business integration after sufficiently building trust with the investor** and to **continuously consider an approach better suited to realize value creation management, strategy and vision** through dialogue with the investor.

Successful case studies:

Specifics of the Basic Actions taken in actual cases

This section focuses on successful cases of enhancement of corporate value by Japanese companies through leveraging foreign capital, highlighting mainly the specifics of the Basic Actions that they actually implemented.

Chugai Pharmaceutical Co., Ltd.

Case Overview

A strategic alliance with Roche has enabled Chugai Pharmaceutical to make intensive investment in drug discovery based on a stable profit base.

- Chugai Pharmaceutical accepted majority investment from Roche, a major global drug manufacturer, and formed a strategic alliance with it.
- By establishing a stable profit base based on exclusive sales of Roche's new drugs in Japan and by building on the growth in the global market achieved through the provision of its own new drugs, Chugai Pharmaceutical made intensive investment in drug discovery research and early development and achieved leap-frogging profit growth. For example, its revenue and operating profit in 2024 increased approximately 7-fold and 21-fold, respectively, compared with the levels recorded at the time when the alliance was formed.

Specific actions

✓ Chugai Pharmaceutical set a strategy of providing innovative new drugs globally by taking advantage of its expertise in biopharmaceutical drug discovery. On the other hand, the company was facing the management challenge of securing research and development funds and the management resources and infrastructure that are necessary for realizing global promotion of self-developed products.

✓ Therefore, **in order to supplement the lack of management resources and global infrastructure**, which was posing a management challenge, Chugai Pharmaceutical **considered an alliance with a major foreign pharmaceutical manufacturer**. Chugai Pharmaceutical aimed to realize efficient overseas promotion of self-developed drugs by utilizing the management resources and infrastructure possessed by a major foreign drug manufacturer that enable global development and sales. (**Basic Action 1**)

✓ Based on a strategic perspective, **Chugai Pharmaceutical considered its strategic direction and explored and thoroughly examined potential alliance partners that would be suited to the strategic direction while exchanging information through an informal network of connections with executives of global companies that its management team had cultivated on a routine basis**. As a result, the company decided to form a strategic alliance with Roche (Switzerland) as a collaboration partner from which comprehensive synergy effects could be expected, from the research stage through to sales activity. (**Basic Action 2**)

✓ In the negotiation with Roche as an investor, **Chugai Pharmaceutical assessed management independence as an "issue unnegotiable for compromise" in order to maintain the research facilities and production technology functions that constituted its value sources**. In addition, the company explained the Japanese drug pricing system, legal systems related to employment, and other unique features of the business environment in Japan in order to share the perspective on the business environment with Roche. (**Basic Action 3**)

✓ When explaining the capital partnership with Roche to employees, business partners and investors, Chugai Pharmaceutical ensured that the term "strategic alliance" took hold within the company. The company's board of directors was composed of three executive officers each from Chugai Pharmaceutical and Roche and three independent outside directors. By establishing a governance system to realize neutral decision-making that would encompass Roche's intentions, **Chugai Pharmaceutical exercised persuasiveness in the explanations provided to the shareholders and employees about its management independence**. (**Basic Action 4**)

✓ Immediately after the formation of the alliance, Chugai Pharmaceutical and Roche established a joint committee concerning each of the functional divisions, including sales, production, and research and development (currently, the divisions have discretion as to whether or not to establish a joint committee). **By enhancing communications between the two sides at the working level, the companies established a system to enable forward-looking discussions on sharing challenges and incorporating each other's advantages**. Chugai Pharmaceutical is also devoting efforts to personnel exchange and joint training with Roche in order to train employees to acquire global skills. (**Basic Action 5**)

Transaction overview

Company name (Company size)	Chugai Pharmaceutical Co., Ltd. (Large enterprise)
Business overview	Manufacturing and selling prescription drugs
Investor	Roche (Switzerland)
Date of announcement	December 2001
Type of capital utilization	Acceptance of investment by a large enterprise itself (majority investment)
Scheme	Takeover bid
Transaction value (Investment ratio)	122.1 billion yen (50.1%)

TAKAMI Co., Ltd.

Case overview

TAKAMI further strengthened brand development by coming under the control of L'Oreal group.

- As a result of accepting 100% investment from L'Oreal, TAKAMI, which is a skin care brand operator, succeeded in increasing sales by formulating a global sales strategy and by strengthening brand power. After the acceptance of investment, TAKAMI's sales became slightly more than four times as large as the pre-investment level due to the expansion of sales channels and a mindset change among employees.

Specific actions

✓ While TAKAMI set a growth strategy as a luxury brand, major brands were leaders in cosmetics sales at department stores. In light of that situation, **TAKAMI considered various options in order to develop human resources and organizational systems necessary for business expansion**. **While trying a self-approach in developing organizational systems and maintaining and expanding its brand, TAKAMI also continued dialogue with various companies, including foreign companies and intermediary players, etc.** (Basic Action 1)

✓ TAKAMI was approached by various companies about possible investment and **held dialogue with foreign companies and other parties, and during that process, the company understood its advantages and disadvantages once again and realized that the TAKAMI brand had higher value than it imagined and had the potential to achieve considerable growth**. The company set a strategy of developing the TAKAMI brand in the medium to long term and decided to come under the control of L'Oreal, which has an advantage in expanding sales channels in foreign markets and at the domestic department store market. (Basic Action 2)

✓ In the negotiation, TAKAMI struggled with the matters that it was unable to fully address on its own due to differences in the accounting standard between the company as an SME and L'Oreal as a global enterprise. **TAKAMI coordinated with support from lawyers and other professionals and adapted to the kind of advanced due diligence process that is implemented by a global enterprise**. (Basic Action 3)

✓ After TAKAMI's coming under the control of L'Oreal, the two companies developed brand strategy and organizational systems by taking advantage of TAKAMI's brand value and the superiority of its direct-to-consumer model while employees from both sides held discussions repeatedly on the backgrounds to and the raison d'etre of the brands. (Basic Action 5)

✓ In particular, **the former president of TAKAMI, who remained as an executive, clarified policy and intentions concerning PMI and held discussions with the management team of L'Oreal. As a result, the two companies decided to create a new approach by integrating each other's advantages in day-to-day operations**. After accepting investment, TAKAMI continued to cooperate with professionals in proceeding with the integration of its budget management, inventory control and other systems into the business operations systems adopted by L'Oreal's global businesses. (Basic Action 5)

Transaction Overview

Company name (Company size)	TAKAMI Co., Ltd. (SME)
Business overview	Manufacturing and selling skincare products
Investor	L'Oreal S.A. (headquartered in France)
Date of announcement	December 2020
Type of capital utilization	Acceptance of investment by an owner-managed company (majority investment)
Scheme	Acquisition
Transaction value (Investment ratio)	Not disclosed (100%)

Kito Corporation

Case overview

Kito has aimed for business expansion based on the advantages accumulated over many years through two rounds of foreign capital utilization.

(i) Kito, which manufactures and sells equipment to lift and secure heavy load, among other products, accepted investment from Carlyle in 2003 and delisted its stock. Later, in 2007, Kito listed its stock on the Tokyo Stock Exchange once again after expanding foreign business at the same time as carrying out reform of business structure.

(ii) In 2023, Kito has realized business integration with the Crosby Group (hereinafter referred to as "Crosby"), which was under the control of KKR. Kito has aimed to become a global leader as a comprehensive manufacturer of lifting equipment by integrating the advantages and disadvantages of the two companies, which were highly complementary in terms of the regions of business operation and product lineup.

Specific actions

(i) Acceptance of investment from Carlyle

- ✓ Being placed in a difficult business environment due to factors such as the stagnant domestic economy, Kito was facing management challenges such as a severe financial position due to unprofitable businesses and interest-bearing debts. Therefore, **the company set a strategy of accelerating globalization with a view to resolving the management challenges through the advancement of governance**. (Basic Action 1)
- ✓ After accepting investment from Carlyle, in addition to disseminating messages from executives, Kito invited Carlyle executives to **speak in person** at meetings of employees and distributors **about the company's value and possibilities as seen by Carlyle**. (Basic Action 4)
- ✓ **When carrying out corporate reform, Kito held meetings with Carlyle repeatedly and promptly made improvements with respect to matters of concern**. After receiving rational and objective advice from Carlyle, Kito boldly implemented corporate reform measures such as selling cross- shareholdings and unused land on factory premises. Kito also accelerated business expansion by using Carlyle's network in the United States and other foreign markets and generated synergy effects peculiar to foreign capital utilization. (Basic Action 5)

(ii) Integration with Crosby Group

- ✓ Regarding business integration with Crosby, Kito made effective use of support services from the M&A team of a securities company and from a law firm, such as facilitation service, in order to hold effective discussion by a third-party committee. (Basic Action 3)
- ✓ After conducting an analytical comparison of all available capital policy options, Kito selected business integration with Crosby based on the determination as it was the most rational option for executing management strategy. After **assessing capital investment plans for maintaining and increasing long-term value, research and development investment, and maintenance of facilities as "issues non-negotiable for compromise,"** Kito explained the importance of those items in the negotiation stage and made efforts to maintain budget funds.(Basic Action 3)
- ✓ Crosby did not have MVV (*) on a group-wide basis. Therefore, Kito explained the importance of MVV to Crosby and established MVV meetings comprised of representatives from countries where the two countries have business operations. **Kito developed new MVV for the integrated company based on an existing document called "Kito Spirit Manual."** (Basic Action 5)

Transaction overview

Company name (Company size)	Kito Corporation (Large enterprise)
Business overview	Manufacturing and selling material handling equipment
Investor	(i) Carlyle (U.S.) (ii) KKR/Crosby (U.S.)
Date of announcement	(i) July 2003 (ii) May 2022
Type of capital utilization	(i) and (ii) Acceptance of investment by a listed company (majority investment)
Scheme	(i) and (ii) Takeover bid
Transaction value (Investment ratio)	(i) Approx. 5.9 billion yen (100%) (ii) Approx. 56.6 billion yen (100%)

*MVV stands for "Mission," "Vision," and "Value."
The term refers to management policy elements that should be placed at the core of corporate management.

PLAID Inc.

Case overview

PLAID has succeeded in strengthening the functions of its products by accepting minority investment from Google and receiving technical support.

- PLAID, which provides a platform for customer analysis, was highly regarded by Google as PLAID refined its core technology that would be difficult for other companies to emulate, and the company accepted minority investment from the U.S. company.
- PLAID obtained new customers by strengthening the functions of its products and developing new services while receiving support from the investor. The company has succeeded in increasing sales and has also promoted collaboration in consulting service as well.

Specific actions

- ✓ As its strategy, PLAID aimed to further increase new customers by strengthening the functions of its product (KARTE) that takes advantage of a core technology that is difficult for other companies to emulate. However, **in order to achieve further growth, PLAID considered ways of utilizing AI as a new technology that was not available in Japan at that time**. (**Basic Action 1**)
- ✓ As PLAID was using Google's cloud computer service (GCP*) for KARTE, **the company concluded that it would be able to receive technical support for enhancing the product by collaborating** with Google. Google was also paying attention to PLAID, which was providing a SaaS platform using GCP. As a result, PLAID decided to collaborate with Google for purposes such as introducing each other's products and services and receiving technical support from the U.S. company. (**Basic Action 2**)
- ✓ When negotiating the investment contract, **PLAID had to engage in the Western-style tough negotiation with Google**. **PLAID pursued its demands over priority points and remained persistent in its arguments without making concessions over points unnegotiable for compromise, such as matters that could undermine decision-making concerning IPO and other important affairs**. PLAID carefully conducted deliberations to ensure collaboration that is beneficial and significant for both sides, while giving consideration to the complementary relationship of the two companies' businesses and overlapping operations. (**Basic Action 3**)
- ✓ In order to create synergy under their collaboration, **PLAID and Google implemented thorough progress management based on common goals**. For example, the two companies worked together to identify potential customers who may be targeted when introducing KARTE more widely and decided to check the progress in sales activity on a weekly basis. (**Basic Action 5**)
- ✓ In addition, **PLAID has developed a good relationship with Google by being involved with it in multiple aspects and is engaging in close communication with Google in order to collaborate in promoting their businesses**. For example, in addition to collaborating in technology development, which was the initial goal, the two companies are holding consultations with each other on a regular basis with respect to the progress management in sales activity. (**Basic Action 5**)

*GCP stands for Google Cloud Platform.

Transaction overview

Company name (Company size)	PLAID Inc. (SME/startup)
Business overview	Developing and providing SaaS related to customer analysis, etc.
Investor	Google (U.S.)
Date of announcement	November 2019
Type of capital utilization	Acceptance of investment by an owner-managed company (minority investment)
Scheme	Issuance of preferred shares
Transaction value (Investment ratio)	Not disclosed

Hitachi Metals Techno, Ltd. (currently, SENQCIA Corporation)

Case overview

Hitachi Metals Techno, currently known as SENQCIA, has succeeded in achieving considerable growth by realizing a highly productive management system through the integration of external and internal human resources and knowledge.

- While Hitachi Metals, the parent company, proceeded with selection and concentration of management resources based on portfolio strategy, the former Hitachi Metals Techno accepted majority investment from Carlyle because it intended to promote business expansion.
- Since accepting investment, the company, renamed SENQCIA, has achieved considerable growth in both sales and profit by improving employees' sense of independence and also by making efforts to raise the profit margin with support from Carlyle.

Specific actions

✓ Hitachi Metals, the parent company, was considering concentrating management resources on core businesses and selling off Hitachi Metals Techno, which was a listed subsidiary. **The former Hitachi Metals Techno itself intended to promote business expansion in new areas and globally as its strategy**. (Basic Action 1)

✓ In that situation, the former Hitachi Metals Techno held consultations with Carlyle and **came to the view that receiving support from a PE fund might lead to the business expansion of the company, which had many products with a significant market share**. Therefore, the company decided to become independent of the Hitachi Metals group and receive support from Carlyle. (Basic Action 2)

✓ As a result of becoming independent of the Hitachi group, the company needed to shift to a corporate culture that is proactive in new business creation. Therefore, **the company's executives and Carlyle executives visited branches and sales offices in person and explained the need to build trust with new shareholders, to share a future direction after the company's independence, and to take on the challenge of adapting to change and trying new things. Carlyle indicated readiness to provide support to that end**. Through such earnest communications with employees, a mindset change started to take hold among the company's executives, realizing that they hold a strong responsibility to the company's growth and independence, aiming to protect employees simultaneously. (Basic Action 4)

✓ Meanwhile, as some employees felt anxious, in addition to changing the corporate culture, it was necessary to improve employee motivation. Therefore, with support from Carlyle, **the company implemented multiple internal projects and the "100-Day Plan," which involved members selected from within the company through internal public invitation. The company held a rally-style event attended by all employees, announced the new company name, explained its management policy under the new SENQCIA name, and provided opportunities for junior employees to express opinions and present proposals**. (Basic Action 5)

*This was an initiative in which the company invited employees to present proposals for addressing management challenges, including marketing and operational efficiency improvement. Employees selected through the internal public invitation, mainly young people, participated in the initiative and presented proposals to the management team after a period of 100 days.

Transaction overview

Company name (Company size)	Hitachi Metals Techno, Ltd. (currently, SENQCIA Corporation) (Large enterprise)
Business overview	Manufacturing and selling construction materials and equipment (including implementing related construction works)
Investor	Carlyle (U.S.)
Date of announcement	February 2015
Type of capital utilization	Acceptance of investment by a subsidiary of a large enterprise (majority investment)
Scheme	Takeover bid
Transaction value (Investment ratio)	Approx. 29.3 billion yen (100%)

Reference: List of members of the Study Group on Leveraging Foreign Capital to Enhance Corporate Value

(Names listed in the Japanese alphabetical order)

<Members> ◎ Chairperson

・ IWAI Takashi (Executive Manager, Professional for Industrial Policy, External Affairs Department, Chugai Pharmaceutical Co., Ltd.)
・ UCHIDA Kosuke (Executive Officer/General Manager, Strategic Corporate Banking Department, Sumitomo Mitsui Banking Corporation)
・ OTA Yo (Partner, Nishimura & Asahi (Gaikokuho Kyodo Jigyo))
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・ KATO Chihiro (Partner, McKinsey & Company Japan)
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◎ MIYAJIMA Hideaki (Professor, Faculty of Commerce, Waseda University)
・ YAMADA Kazuhiro (Managing Director and Co-Head of Carlyle Japan, L.L.C)

<Observer>

○Industry organization

・ Japanese Bankers Association

○Ministries and agencies concerned

・ Office of Foreign Direct Investment Promotion, Cabinet Office
・ Strategy Development Division, Strategy Development and Management Bureau, Financial Services Agency
・ Industry Creation Policy Division, Economic and Industrial Policy Bureau, Ministry of Economy, Trade and Industry
・ Corporate System Division, Economic and Industrial Policy Bureau, Ministry of Economy, Trade and Industry
・ Innovation Department, Japan External Trade Organization (JETRO)