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Corporate Control and ESG under "New Capitalism" - Next phase of corporate governance reform: Comment

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Too many problems to solve?
(or, don't we expect too much of corporate governance?)

Today, good corporate governance is expected to –

a) discipline management

b) overcome "short-termism" of the capital market and enhance long-term firm value

c) assure "sustainable" development of society

Too many problems to solve?
(or, don’t we expect too much of corporate governance?)

- Structuring corporate governance to tackle all these problems ((a) ~ (c) on the previous page) is a very difficult task
- since taking one governance measure to solve one problem may aggravate another problem

E.g.) Issuing loyalty shares with tenure voting may encourage long-term shareholder engagement and mitigate the problem of short-termism

But it may also increase shareholders who are loyal to managers, which will have negative impact on disciplining management

Too many problems to solve?
(or, don't we expect too much of corporate governance?)

- Considering side-effects in pursuing broader goals, it may be good for corporate governance to focus on a narrow, traditional goal - i.e., to discipline management. (In fact, I am sympathetic with this view.)
- However, more and more people seem to pursue broader goals (e.g. Hart and Zingales (2017)), perhaps for good reasons. Environmental and social issues may be so important that we don't like to leave the (often dysfunctional) political and regulatory process to solve them

Empirical studies are important to analyze costs and benefits of governance measures

- If we want to construct corporate governance system to achieve broader goals, we must be very careful to analyze costs and benefits of various governance measures
- Empirical studies are extremely important to conduct prudent cost-benefit analyses

Comment to "Internal Market for Corporate Control and Stock Repurchase" by Prof. Franks

- An empirical study on Japanese firms' stock repurchases and subsequent uses of treasury shares
- Reporting that Japanese firms often use treasury shares they acquired by quasi-private transactions (through ToSTNeTs and discounted TOBs) in private placements for strategic reasons, and those transactions in combine ("round-tripping") enhance shareholder values on average
- Very interesting, especially because corporate-law scholars (like me) have viewed both share repurchases and private placements with considerable skepticism that they could be motivated by private interests of managers

Comment to "Internal Market for Corporate Control and Stock Repurchase" by Prof. Franks

- This study will contribute to the hypothesis in finance literature that firms serve as "market makers" in repurchasing own shares (Hillert et al 2016; Hong et al 2008; De Cesari et al 2011)
- Market makers fill the gaps between supplies and demands
- When insiders (banks, insurance companies, & other business corporations) of a firm want to sell their shares in the firm, they may have difficulty in finding buyers
- Selling a large block of shares on the market will have negative impact on the market price and cause a loss to insiders, which might discourage insiders from selling their shares in the first place
- In such a case, a firm can serve as a market maker, repurchase its own shares from insiders and hold those shares as "inventory," waiting for the opportunity to use them for future value-enhancing transactions

Comment to “Internal Market for Corporate Control and Stock Repurchase” by Prof. Franks

- Some comments (or cautious views)

(1) Are “round-trippings” really beneficial for shareholder value?

- Quite a few firms use treasury shares in public offerings, which will cause negative CRAs (Table 10, Panel A in the discussion paper [DP])
- Even when firms use treasury shares in private placements, sometimes they allot shares to parties who have already had cross-shareholding relationships with the firms, in which cases CRAs will also be negative (Table 12, Panel B in DP)
- How should we interpret these results? Perhaps some transactions in own shares are motivated to enhance shareholder value, while others motivated by private interests of managers?

Comment to “Internal Market for Corporate Control and Stock Repurchase” by Prof. Franks

(2) [Question for future research] Are private placements for strategic reasons also beneficial for a long-term?

- Some of the cases of strategic alliances discussed in Chap.3 of resulted in a failure DP (Suzuki – Volkswagen)

Comment to "Shareholder Activism in Japan: Quiet v. Public Activism" by Prof. Suzuki

- Conduct research on "quiet" engagement activities by Governance for Owners [GO] and compare them with "public" activism
- Finding: Quiet engagement by GO Japan works well
- - Success rate is (50%) higher than public activism
- - higher BHARs than public activism

Comment to “Shareholder Activism in Japan: Quiet v. Public Activism” by Prof. Suzuki

- A very valuable study on “quiet” activism, which can only be conduced with confidential information (cf. Becht et al 2008 on Hermes UK)
- Data on BHARs are also very helpful

Comment to “Shareholder Activism in Japan: Quiet v. Public Activism” by Prof. Suzuki

- Some comments or questions
- Is “Quiet v. Public” (or “the Sun v. the North wind”) an appropriate way of comparison?
- Are “quiet” activism and “public” one opposing alternatives? Rather, aren’t they **complementary** methods to discipline the management?
- In the US, many activists now reach settlements with firms probably because, if the disputes go public, activists are more likely to win proxy contests with support of institutional investors than they used to (Bebchuk et al 2020, “Dancing with activists”)

Comment to “Loyalty Shares with Tenure Voting: The New Dual Class?” by Prof. Becht

- Very informative overview of loyalty shares, academic debates and practical developments about ESG (sustainability)
- “Inconvenient conclusion”: ESG does not come free (while it can provide new business opportunities), CEMs can entrench irresponsible behavior of management, it is painful to abandon fossil fuels, plastics etc.
- I strongly agree. Pursuing broader goals of corporate governance requires careful balancing of interests, and there is no panacea

Comment to "Loyalty Shares with Tenure Voting: The New Dual Class?" by Prof. Becht

- In Japan, dual-class shares are legally permissible, and loyalty shares with tenure voting are also possible by use of convertible shares
- But uses of them by listed companies are very rare (only CYBERDINE?)
- Negative side-effects (entrenching management) are often emphasized
- On the other hand, dual-class and loyalty shares are more widely used in (some of) European countries (such as France, Netherlands)
- What explains such variety in countries? For economic, political or historical reasons?

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