Japan Buyout Monthly

July-September 2012

Sushiro Exit and the Opportunities for Foreign Funds

At the end of August, **Unison Capital** announced that it will sell its entire 81% stake in **Sushiro,** Japan's top-selling belt-conveyer sushi restaurant chain, to **Permira**. Permira's press release said that it was valuing Sushiro at approximately USD 1 billion, nearly 4 times larger than the company's EV in 2007 when Unison first acquired a stake in Sushiro.

Unison bought a 20% stake in 2007 after some of Sushiro's founders had sold their holdings to Zensho Group. Zensho, back then, owned a 30% stake in Sushiro's stronger competitor Kappa Create Co.. In 2008, Unison and the management acquired a 90% stake in Sushiro through a TOB, which was announced in the immediate aftermath of the Lehman collapse. The purchase price was set with a 61% premium, but it was still as low as 4x EBITDA. The company was eventually delisted in April 2009. After going through a tough time during 2008 and 2009, Sushiro was selected as the restaurant operator with the highest customer satisfaction in Japan in 2010 and it took over Kappa Create as the highest sale of any sushi chain in 2011.

At USD 1 billion EV, the sale of Sushiro will bring approx. JPY 55 billion (USD 700 million) in profit to Unison's second fund, which was established in 2004 with JPY 75 billion (USD 960 million). According to a source, Sushiro will have paid back all LBO loans before the sale, its EBITDA has increased by a few times and the exit will bring a **return of 8x** to the Unison fund.

The Sushiro deal well-illustrates the current Japan buyout market. In the past few years, most large buyout deals have been consummated between Japanese sellers, mostly funds, and foreign fund buyers.

Year	Company	Seller	Buyer
2009	Bell Systems 24	Nikko Principal	Bain
2011	Tsubaki Nakashima	Nomura Principal	Carlyle
2011	Skylark	Nomura Principal	Bain
2012	Jupiter Shop Channel	Sumitomo Corp	Bain
2012	Sushiro	Unison	Permira

Historically, securities company's principal investment arms, such as Nomura Principal and Nikko Principal, as well as larger local funds, such as Unison Capital and Advantage Partners, were taking deal opportunities away from the foreign mega funds in Tokyo. However, in the past few years, Nikko and Nomura closed or substantially shrunk their investment activities and the investable capital at several larger Japanese funds has depleted. This has created a "vacuum" in the large cap sector in Japan. Those who used to take deals away from foreign funds are now supplying deals to them to cash out existing investments.

Japanese strategic buyers - extremely cash rich and hungry for acquisitions - could be a strong contender, but it looks like they are currently focusing on foreign companies or Japanese companies with established foreign businesses. As a result, their appetite for domestic consumer business seems to be modest, enabling secondary buyers to obtain a reasonable entry price.

A company that has a strong desire to develop overseas business may find a global or pan-Asian fund as an ideal partner, particularly if their experience with a Japanese GP has made them comfortable to work with a foreign fund. A foreign fund will also find some security in investing in a portfolio company of a Japanese GP. The post-buyout cooperation with the management would be more predictable and there would be less chance of a big surprise.

In short, **Japan today is a much better place for foreign funds.** The recent developments should bring very interesting opportunities to funds with ample dry powder. If they do not have a local team, they could possibly consider teaming up with a local fund. An increase in secondary deals should favor foreign funds in general.

However, the opportunities will not hung as low as they were in late 90s. As you can see from the articles in below, **state-backed funds have emerged as a supplier of large buyout capital.** They could fill the void created by the lack of private funds' interest. They could also compete against private funds under certain circumstances.

Buyout Deals **(Up to late-September)**

(June)

Unison Capital announced a TOB to acquire a 41.5% stake in **Nexcon Technology** (038990:KS) through a Korean special purpose acquisition company. The JPY 8.2 billion (USD 105 million) TOB was a part of a MBO by Nexcon's management and its largest shareholder. The TOB premium was set at 34.3% over the weighted-average stock price of the past 1 month or at 60.5% over the price for the past 6 months. Nexcon manufactures battery management system products for secondary lithium-ion batteries. The TOB was completed in July.

(July)

Polaris Capital Group acquired a 30% stake in **Myland Real Estate Co.** by investing in slightly over JPY 2 billion (USD 25 million) through a private placement. Myland buys existing homes, renovates and sells them to first-time homebuyers. It has agencies in 46 of Japan's 47 prefectures and takes in about JPY 30 billion (USD 375 million) in annual sales. It was reported that Myland aims to go public in a few years.

Fortress Investment Group, through its SPC, is in the process of acquiring a 100 % stake in **Nissin Servicer Co., Ltd.** (8426) through a 2-step TOB. Nissin, a debt-collection firm owned by NIS Group, Index Holdings (4835), CBS Financial Services, state-backed Resolution Collection Corporation (RCC) and others, has selected Fortress and **Seven Seas Advisors**, a Japanese turnaround advisory firm, as its reorganization sponsor. Fortress has acquired a 81% stake for JPY 0.62 billion (USD 8 million) in the 1st round (completed in August) and the 2nd round will be completed in early October.

(August)

Japan Industrial Solutions, a turnaround fund backed by 3 mega banks, Development Bank of Japan, Mitsubishi Corporation and Deutsche Bank, will purchase JPY 15 billion (USD 192 million) preferred shares issued by **ULVAC Inc.** (6728), a maker of semiconductor fabrication. ULVAC reported a loss of JPY 50 billion (USD 640 million) for the year ended June 2012, which has driven down its capital ratio to a record-low 14.8%. As the preferred shares will bring as much as 84% dilution if converted into ordinary shares, the ULVAC management aims to buy back them within 3 years.

A fund targeting at silver business managed by **ACA** and exclusively invested by **Sompo Japan Insurance Inc.** has acquired 34% of **Cedar Co. Ltd.** (2435) for JPY 1.2 billion (USD 15 million) through a tender offer. The TOB price was set at 54% over the average stock price of the past 3 months. Cedar has 76 aged care facilities across the country and generates JPY 9.6 billion (USD 123 million) in revenue.

Japan Industrial Partners will acquire a 100% stake in **ITX**, a mobile phone sales subsidiary of troubled Olympus Corporation (7733) for JPY 53 billion (USD 680 million). Increase in the smart phone sales brought JPY 230 billion (USD 2.9 billion) in revenue, but operating profit stands at JPY 5.3 billion (USD 68 million). Olympus purchased ITX through a tender offer in 2004.

Permira announced that it will acquire **Sushiro**, the belt-conveyer sushi chain operator from **Unison Capital.** (Please see article above.)

Next Capital has acquired the business of Tokyo-based cooking school operator **Sunrich** and its subsidiary **Homemade Association** for JPY 500 million (USD 6.3 million). Sunrich runs 114 cooking schools plus 150 franchise schools in Japan. Next intends to turn around the 40-year-old pioneer among Japan's cooking schools. This makes the first investment from the GP's second fund, which is currently fund raising.

Fortress Investment Group will acquire the business of **NIS Group** for JPY 3 billion (USD 38 million). Fortress, working with **Seven Seas Advisors** was selected as the sponsor for NIS Group's reconstruction under civil rehabilitation law. The consumer finance company, once owned by **TPG**, has been in financial trouble over several years.

Post Investment Activities

Jupiter Shop Channel, owned equally by **Bain** and **Sumitomo Corporation**, will participate in a TV shopping service JV to be formed In Thailand with 2 Thai firms. Sumitomo Corporation and Jupiter will take a 40% stake, while Thailand's top retailer, Central Group, and a unit of consumer goods giant Saha Group will each own 30% interests. The Thai TV shopping market was worth around JPY 20 billion (USD 254 million) in 2010, but the JV aims for annual sales of JPY 12.5 billion in five years.

Aozora Bank Ltd., the successor institution to failed Nippon Credit Bank majority-owned (in voting right) by **Cerberus Capital Management LP**, said it has agreed with the Japanese government to repay public funds in installments over the next decade on August 27. This deal pushes back the mandatory conversion of the government's preferred shares until 2022. Aozora will make an initial upfront payment to the government of JPY 22.7 billion (USD 288 million) and then pay it JPY 20.49 billion annually until 2022. When the government injected public funds into the bank in 1999 and 2000, the state received convertible preferred shares worth JPY 320 billion (USD 4.1 billion), of which JPY 180 billion worth remain outstanding. Aozora plans to reduce its capital base from JPY 420 billion (USD 5.4 billion) to JPY 100 billion, buy back about 20% of shares issued and boost its dividend payout from 30% to 40% of earnings. On September 27, Aozora Bank has announced that Cerberus will sell some of its approx. 50% holdings in the bank in the planned buyback and may begin selling the remainder in 2012 through the capital market or off-exchange direct transactions.

Intelligence Ltd., a recruiting service company and a portfolio company of **KKR**, will start to provide consulting services to companies with respect to the employment of handicapped workers. From FY 2013, the mandatory employment rate of disabled workers will be increased from 1.8% to 2.0%.

Tsubaki Nakashima Co., a maker of ceramic and glass balls and a portfolio company of **Carlyle Japan**, has decided not to float its shares on the stock market. It had planned to relist on the Tokyo Stock Exchange on October 11 and obtained the approval from TSE on September 5.

Exits **(Up to late-September)**

(July)

J-Will Partners sold 2 up-market Japanese-style hotels to **Noguchi Kanko**, a hotel operator based in Hokkaido. The combined revenue of the 2 hotels is USD 23 million.

The Innovation Network Corporation of Japan (INCJ) will invest in **Kureha Battery Materials Japan**, which produces a cutting-edge lithium ion battery material. INCJ, **Kureha Corp.** (4023), **Kuraray Co.** (3405) and **Itochu Corp.** (8001) will jointly contribute JPY 10 billion (USD 127 million) to the JV. Kureha and Kuraray have established processes to produce battery electrode materials that can halve the time required to charge electric and plug-in hybrid vehicles, as well as improve battery durability by 30%.

(August)

Unison Capital has agreed to sell **Sushiro** for approx. USD 1 billion to **Permira.** (Please see article above.)

iSigma Capital will sell its 100% stake in **Gold-Pak**, a fruit juice maker, to **Air Water Inc.**(4088), an industrial gas production company with approx. USD 2 billion market cap. Today Air Water has 2/3 of its revenue generated from non-gas business. Gold-Pak's sales, which had been falling in the preceding years, were stable at around USD 500 million in 2011 and 2012. In January 2011, iSigma spent JPY 4.5 billion (USD 57million) to acquired a 92.6% stake of Gold-Pak through a tender offer. The entry EBITDA multiple was estimated at around 3.5x.

(September)

Rex Holding Co, the holding company of several restaurant chains and a portfolio company of **Advantage Partners**, will become majority-owned by **Colowide Co.** (7616), the parent firm of several chains of Japanese-style pubs. Rex is 32% owned by its founder and 55% or more owned by the funds advised by Advantage Partners. Colowide will acquire a 66.6% stake of Rex through a debt-equity swap. Colowide has agreed to purchase outstanding bank loans from the lenders for JPY 13.7 billion (USD 175 million). Since Advantage funds acquired approx. 90% of the company in December 2006, Rex has been restructuring its business by selling convenience store chain operator am/pm in 2009, Red Robster in 2012 and super market chain Seijo Ishii in 2012.

J-Star has transferred all of the shares of **Iki Iki K.K.**, a mail order business focusing on growing elderly population in Japan, to NK Relations Co., Ltd., a wholly-owned subsidiary of **Noritsu Koki Co., Ltd**. (7744). Noritsu has its origin as a manufacturer of film processing machines, but has been expanding business lines to include medical care, food and environments. J-Star and its co-investor **Macquarie Investment Management** acquired Iki Iki in 2009 for about JPY0.8 billion (USD 10 million) and reportedly sold it for at approx. USD 100 million. No leverage was used for this turnaround investments. According to Noritsu's press release, Iki Iki's revenue, net profit and EBITDA were JPY 0.9, 0.4 and 0.8 billion (USD 12, 5 and 10 million) respectively in FY2012.

Nippon Mirai Capital has sold its holdings of **Gourmet PIA Network Co.**, a restaurant-related information provider, to **Jorudan Co., Ltd.**, a transportation-related information provider. Jourdan paid JPY 330 million (USD 4.2 million) to acquire a 100% stake in Gourmet PIA. Nippon Mirai invested in Gourmet PIA in June 2005.

DRC Capital has sold its investment in **Yumeshin Holdings**, a staffing company specializing in construction workers. DRC invested JPY 920 million (USD 12 million) to acquire a 7.6% stake in the company in February 2007. Since the minority acquisition, DRC guided the company to focus on the core competence and helped restructure the swollen balance sheet. This 5.5 year PIPE investment achieved 1.5x ROI with a gross IRR of 8.3% p.a. while the Nikkei Index fell by 49%.

Japan Airlines Co. (9201) was re-listed on the Tokyo Stock Exchange on September 19 with JPY 690 billion (USD 8.8 billion) market capitalization, which has made it the second largest IPO this year after Facebook. JAL filed for a bankruptcy on January 19, 2010 and received a capital injection of JPY 350 billion (USD 4.5 billion) from **Enterprise Turnaround Initiative Corporation of Japan (ETIC)**. Having wiped out all of the shareholder equity 2.5 years ago, JAL has engaged in substantial corporate restructuring - reducing its flight routes and employees by 40% and cutting pension obligations and the number of subsidiaries by half. It reported JPY 200 billion (USD 2.5 billion) operating profit in FY 2012. ETIC, which owned approx. 96% of the carrier, has sold its entire holdings at the listing and realized JPY 300 billion (USD 3.8 billion) in profit.

Private Equity Related News

(June)

Tokyo Metropolitan Government appointed **Sparx Group** (8739) and **IDI Infrastructures** as the managers of public-private partnership infrastructure funds that will invest in power plants and other renewable energy facilities in Tokyo area. TMG has selected the 2 managers through a public tender. TMG will invest JPY 1.5 billion (USD 19 million) to each of each fund, while the managers are expected to raise another JPY 18.5 billion (USD 230 million).

(July)

Polaris Capital Group has announced that its 3rd fund had the first closing on July 11th with approximately JPY 20 billion (USD 254 million) commitments from investors. Polaris III aims to raise between JPY 30 to 40 billion. According to the press release, Polaris I has realized almost 2/3 of investments and expects to achieve full exits in a few months. Polaris II is now fully invested.

Defta Partners will establish a VC fund focusing on telecom, healthcare, environments and energy sectors through its Japanese subsidiary, Defta Capital.

The fund size will be between JPY 2 - 3 billion (USD 25 - 37 million).

(August)

Daikin Industries Ltd. (6367) announced that it would acquire **Goodman Global Inc.**, the leading manufacturer of home air conditioners in the U.S., for roughly JPY 296 billion (USD 3.8 billion) from **Hellman & Friedman LLC**. The acquisition would be one of the largest yet this year by a Japanese manufacturer.

In August it was reported that **KKR** has decided to take over management of **Renesas Electronics Corp.** (6723) by spending JPY 100 billion (USD 1.27 billion) to acquire new shares from the troubled chipmaker. According to The Nikkei, KKR declined Renesas' request for JPY 50 billion partial acquisition and, instead, it proposed a majority acquisition with a plan to replace the current management and further reduce employees. Renesas is seeking more than 5,000 voluntary retirements in September and also plans to eliminate up to 14,000 jobs (roughly 30% of its workforce) and shut down or sell (half of) its 19 domestic plants. Renesas' three major shareholders, NEC, Hitachi and Mitsubishi Electric had already agreed to provide a JPY 50 billion (USD 630 million) financing in total and 4 major banks were prepared to lend up to JPY 50 billion (USD 630 million). On September 22, it was also reported that a consortium led by **INCJ** is aiming to acquire Renesas with more than JPY 100 billion capital injection. According to The Nikkei, the consortium is likely to include major manufactures, such as **Toyota, Nissan, Honda, Panasonic, Cannon** and **Fanuc**, whose products heavily depend on Renesas's custom-made chips that cannot be replaced by others. Apparently KKR's plan to reform Renesas as a mass-producer of generic chips made them anxious and prompted the action.

Hiroshima Bank and 9 other regional financial institutions and **Development Bank of Japan** will set up a Hiroshima-region focused fund in anticipation of the termination of SME Finance Facilitation Act in March 2013. It aims to raise JPY 3 billion (USD 38 million).

(September)

Hokuyo Bank, a regional bank based in Hokkaido, announced that it will set up a fund jointly with **J-Will Partners** focusing on SMEs in Hokkaido.

Government Pension Investment Fund, the largest public pension fund in Japan with USD 1.37 trillion AUM, collected proposals from the companies interested in conducting a research on the subject of "a possible alternative investment scheme at GPIF". GPIF had announced a public tender in August and the tender winner is expected to complete the work by February next year.

Atomico, a VC fund established by a Skype founder, has set up a Japanese office and plans to invest in about one local venture a year.

Financial News

On September 19, **The Bank of Japan** decided to increase the size of its asset purchase program, its main tool for monetary easing, to JPY 80 trillion (USD 1.02 trillion) from JPY 70 trillion and extended the deadline of the program by six months to the end of 2013. The BOJ downgraded its view of exports and production. In its August report, the BOJ said that economic activity has started picking up moderately as domestic demand remains firm on the back of post-quake reconstruction. The increased tension between Japan and China will also have a negative impact on both countries' economy, though the BOJ governor said it was not a part of BOJ's decision this time.

The BOJ also announced that the foreign holdings reached 8.7% of all outstanding government debt of JPY 940 trillion (USD 12 trillion), the highest since 1979.

Market Indices

		Monthly change (end of June vs August)	
TOPIX	731.64	-38.36	-4.98%
Nikkei JASDAQ	1302.04	-32.67	-2.52%

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