



Global Investment Research

The Goldman Sachs Group, Inc.

Passive/Active Investment Strategies and Implications for Market Functioning and Corporate Governance

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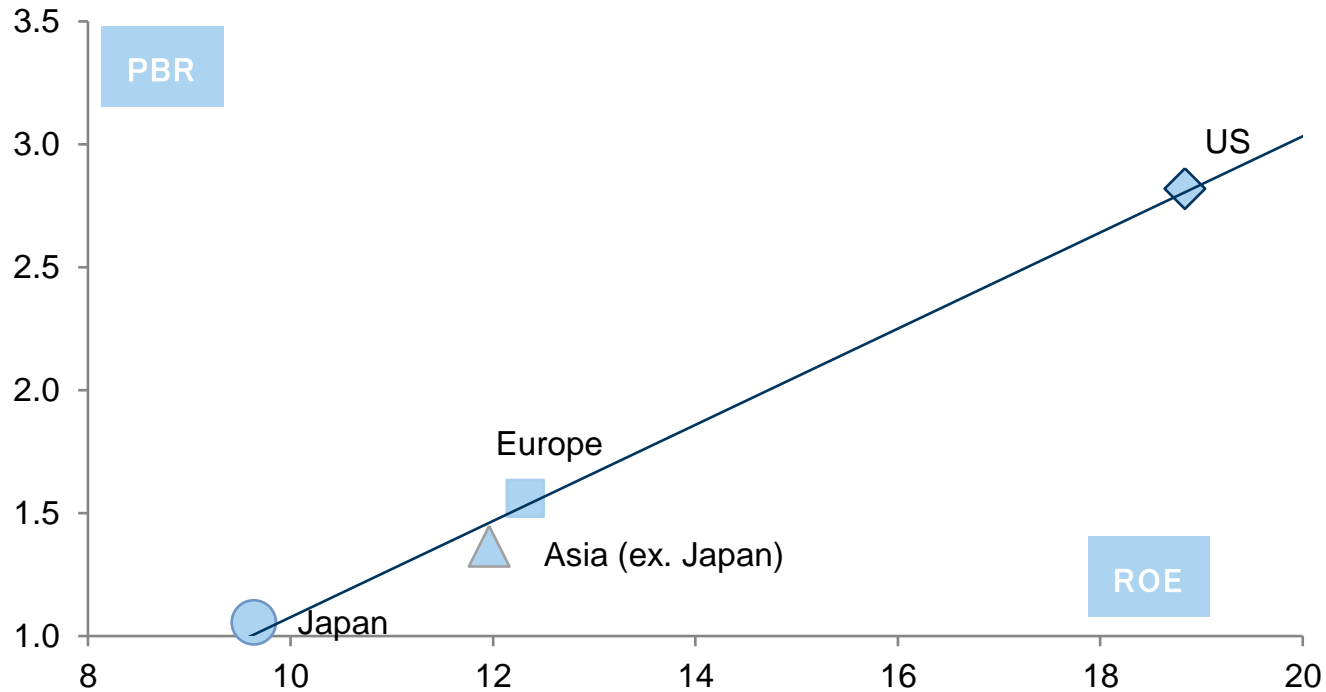
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Japanese Equities: Cheap for a Reason?

International ROE vs P/B correlation

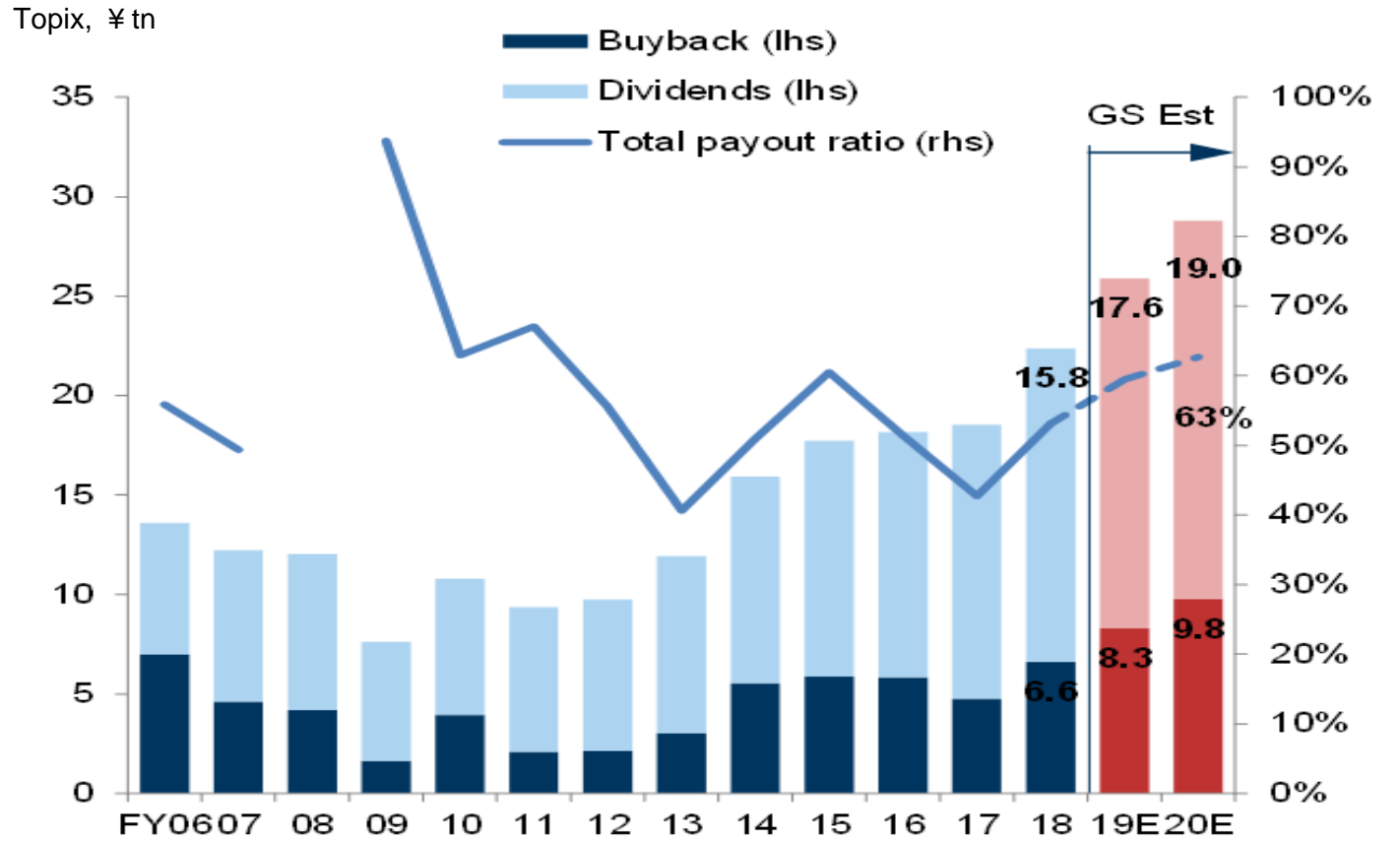


Note: Japanese universe is TSE1. US universe is S&P500. European universe is DJ Stoxx 600. Asia excluding Japan(AEJ) universe is MSCI US\$ basis market index. FY3/16E denotes CY12/15E for US, Europe and AEJ. EPS Growth: GS Global Macro Research forecasts (GSE). EPS Growth and P/E: based on GSE. P/B:GSE for Japan, consensus for US, Europe, and AEJ. EV/EBITDA: excludes financials, based on consensus. ROE and Div. Yield: GSE for Japan, consensus for US, Europe, and AEJ. 10-yr bond yield: Germany's rate used for 10-yr bond yield for Europe. Consensus forecast is based on I/B/E/S, FactSet, Toyo Keizai.

Source: I/B/E/S, FactSet, Toyo Keizai, GS Global ECS Research calculations.

Governance Reforms Prompt Higher Shareholder Returns

Shareholder returns at all-time high

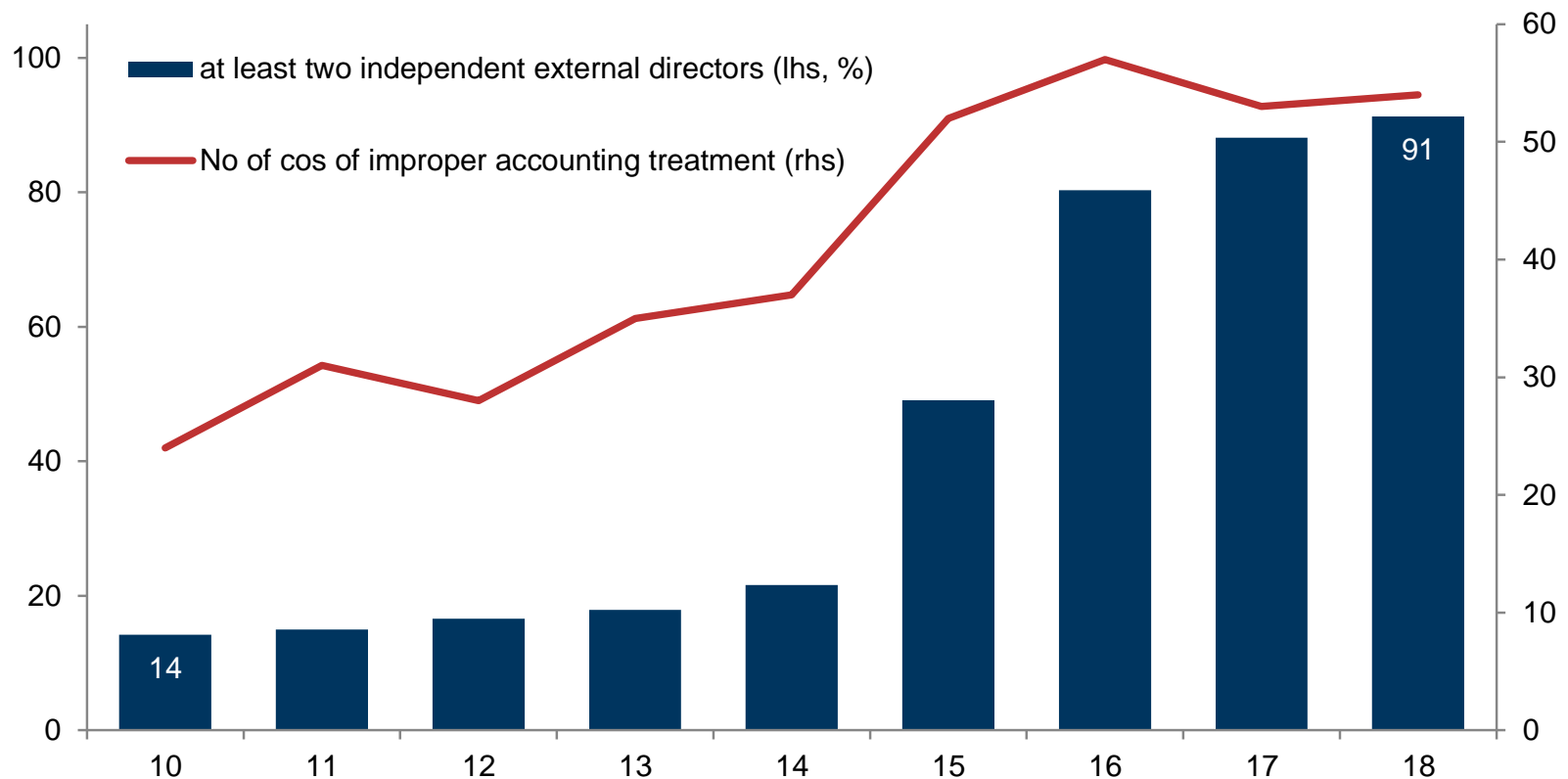


Source: Company data, Goldman Sachs Global Investment Research

Board Independence No Longer an Oxymoron

Rise in Japanese cases of improper accounting treatment coincides with increased board independence

%, number of firms



Source: TSR, TSE

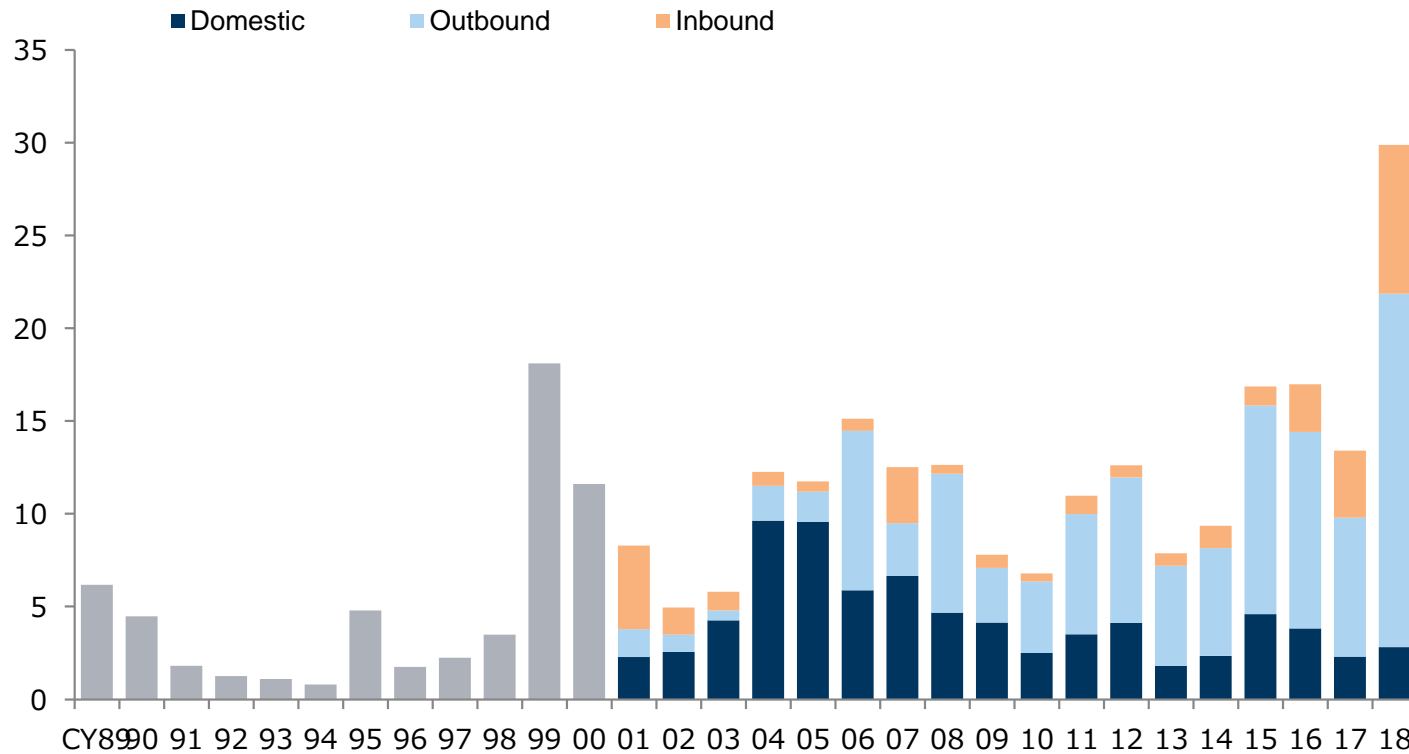
Shareholder-Proposals on the Rise

Date (Reported)	Company	
3/12/2019 5/13/2019	Toshiba (6502.T)	King Street Capital Management announced plans to nominate a number of outside directors to replace a majority of Toshiba's board at the latter's AGM. On May 13, Toshiba announced 12 board nominees that include 10 outside directors (including 4 foreign nationals) for election at the AGM.
5/31/2018 1/11/2019	Olympus (7733.T)	US investment fund ValueAct Capital Management owns more than 5% of Olympus shares. On January 11, 2019, Olympus announced that a partner at ValueAct would be proposed as a board director at its ordinary AGM in June.
10/30/2017 12/21/2018	Alps Alpine (6770.T)	In October 2017, Oasis Management expressed dissatisfaction as an Alpine shareholder in the share exchange ratio underpinning then Alps Electric's plan to turn Alpine into a wholly-owned subsidiary. At Alpine's AGM in June 2018, Oasis called on the company to pay a year-end dividend of Y325 (as opposed to the company's planned dividend of Y15) and to appoint outside directors. The proposal failed to win approval, but nearly 30% voted in support. This was followed by a series of shareholder return measures, including Alpine's September 2018 announcement of plans to pay a special dividend of Y100 post-integration, and parent company Alps also announcing a Y40 bn share buyback after the merger.
2/4/2017 4/21/2017	Panasonic (6752.T)	In September 2016, Oasis Management sent PanaHome a letter saying the homebuilder's stock price was undervalued versus its enterprise value and needed to address this. In December 2016, Panasonic announced that it would turn subsidiary PanaHome into a wholly owned unit via a share exchange. In February 2017, Oasis Management asked for a revision of the share exchange ratio. In April 2017, Panasonic announced the termination of the share exchange agreement and said it would instead make PanaHome into a wholly owned subsidiary via a tender offer (for a total offer of Y92.3 bn, up from Y77.0 bn).
2/10/2015 3/24/2015 4/27/2015	Fanuc (6954.T)	In a letter to investors, US fund Third Point disclosed that it had acquired shares in Fanuc, at the same time commenting that Fanuc's low valuation is in part because it did not communicate with investors and sell-side analysts, so its future earnings potential is unclear. On March 24, 2015, Fanuc announced the establishment of a new SR (Shareholder Relations) department, to serve as a point of contact for dialogue with shareholders. On April 27, 2015, Fanuc announced plans to double its consolidated dividend payout ratio target, from 30% to 60%, and said it also would aim to buy back shares in a flexible manner.
Ongoing		
11/16/2015	Pasona Group (2168.T)	Oasis Management is requesting improvements to Pasona's management, including better cost controls and reforms to corporate governance.
3/14/2019 5/21/2019	Kyushu Railway (9142.T)	Fir Tree submitted six shareholder proposals for JR Kyushu's AGM to be held in June, including a share buyback amounting to 10% of outstanding shares, transition to a company with a three committees structure, election to the board of three outside directors recommended by Fir Tree, and introduction of stock-based compensation. On May 13, JR Kyushu resolved to oppose all six proposals.

Japanese M&A Expanding

Japanese M&A reaches record high

Total value of M&A transactions involving Japanese companies (¥ tn)

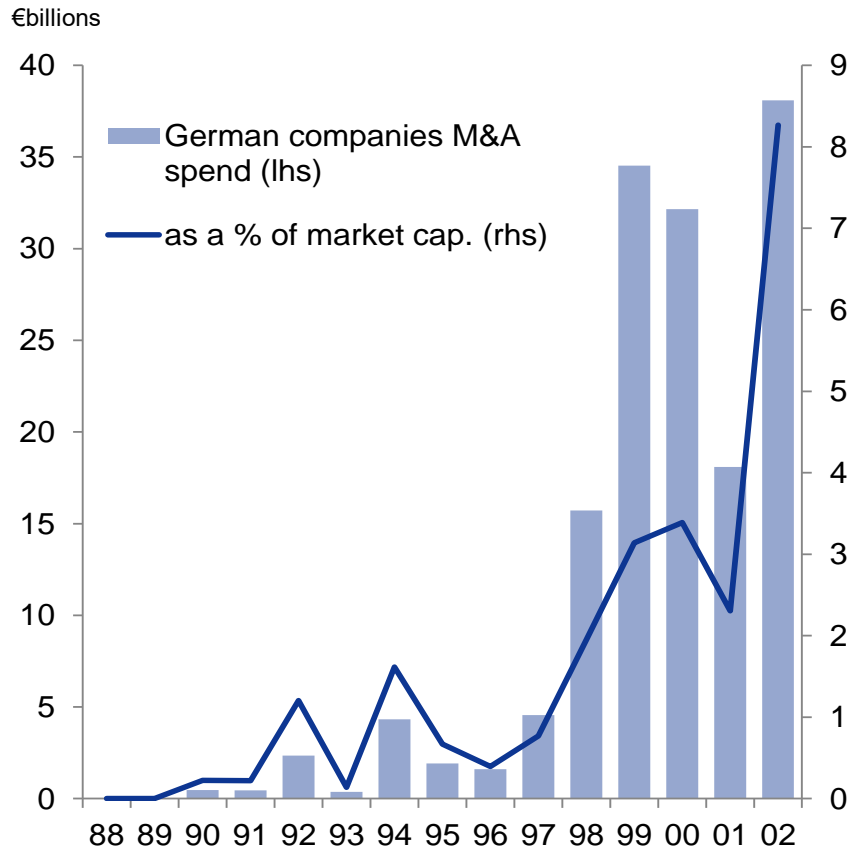


Source: Recof.

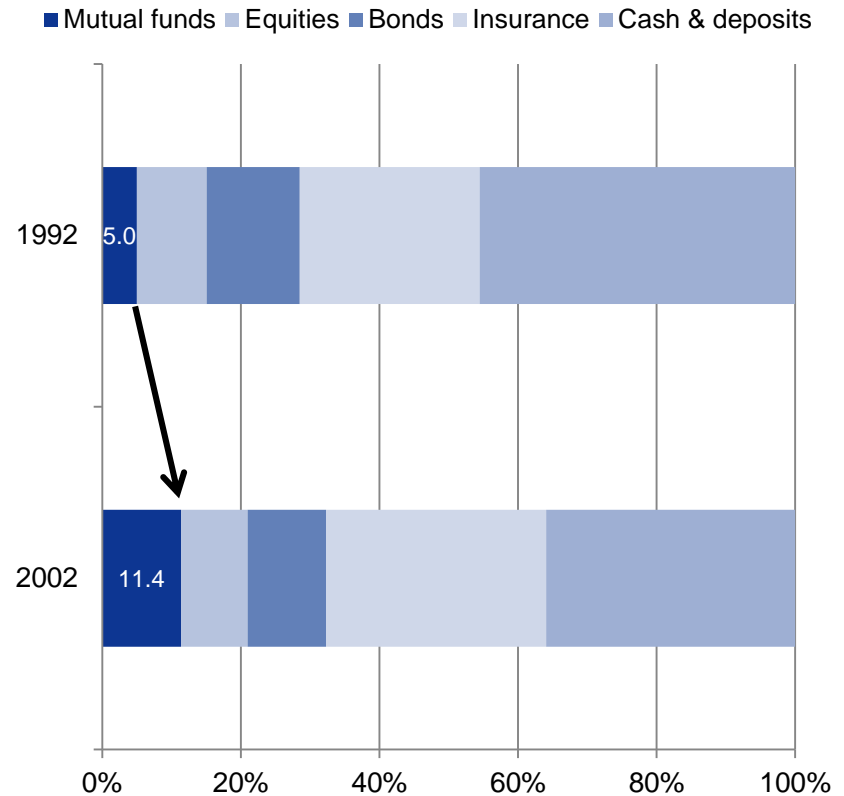


German Example: Governance Reforms → Equity Culture

German companies' M&A spend sharply increased in the late 1990s



Mutual fund share has doubled—breakdown of German household savings



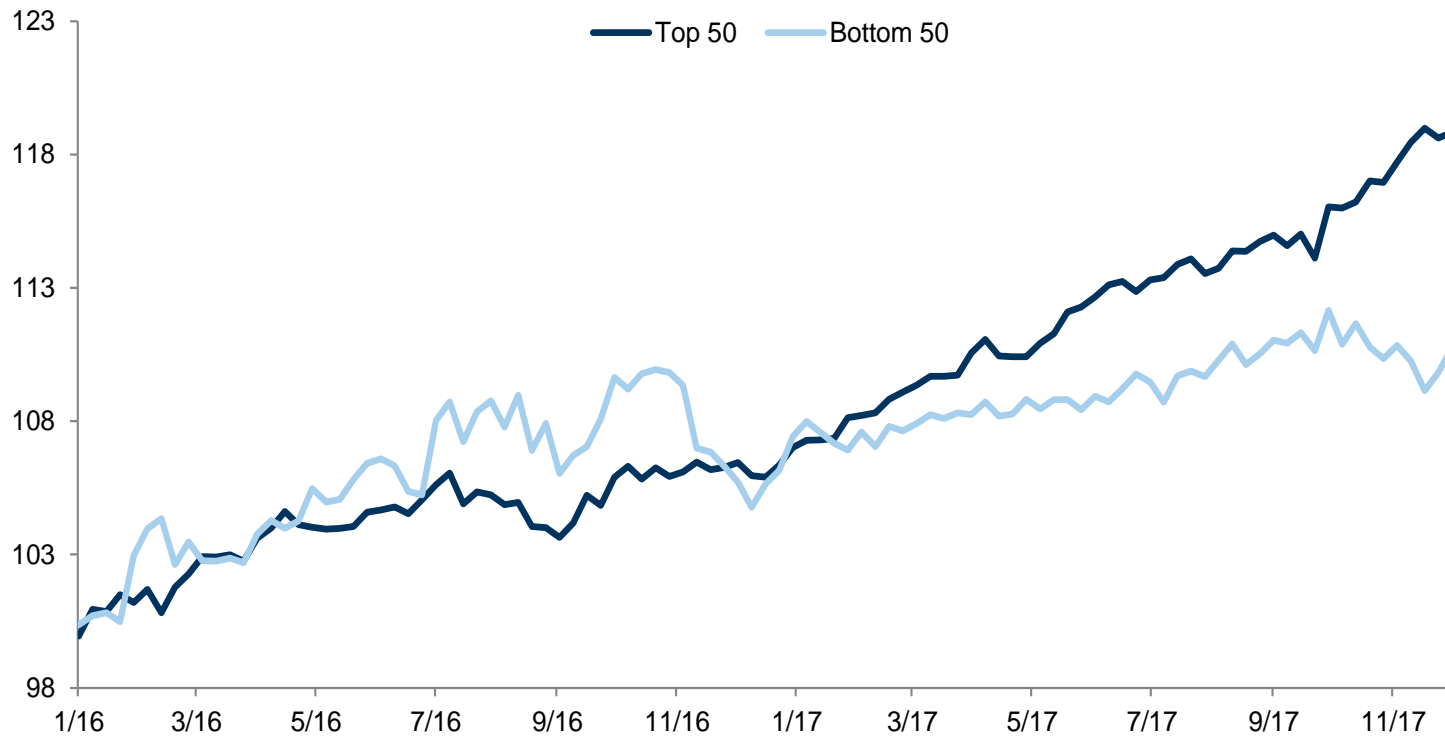
Source: FactSet, Worldscope, Goldman Sachs Global Investment Research.

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Better Corporate Governance Drives Excess Returns

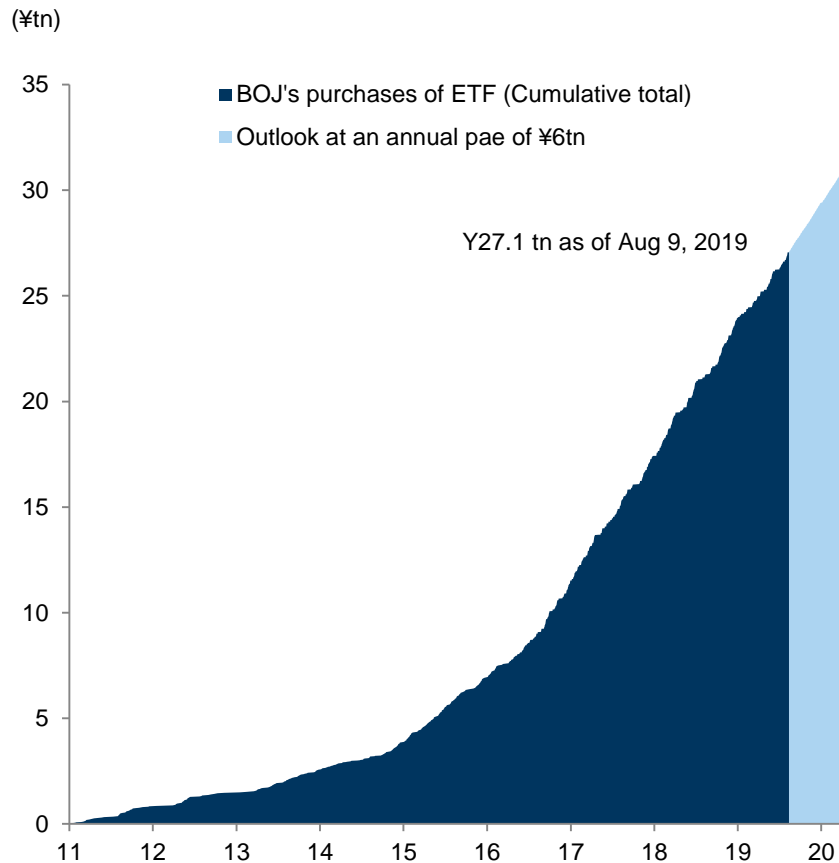
Companies with high scores have outperformed YTD

Relative to TOPIX, Indexed, Jan. 4, 2016=100

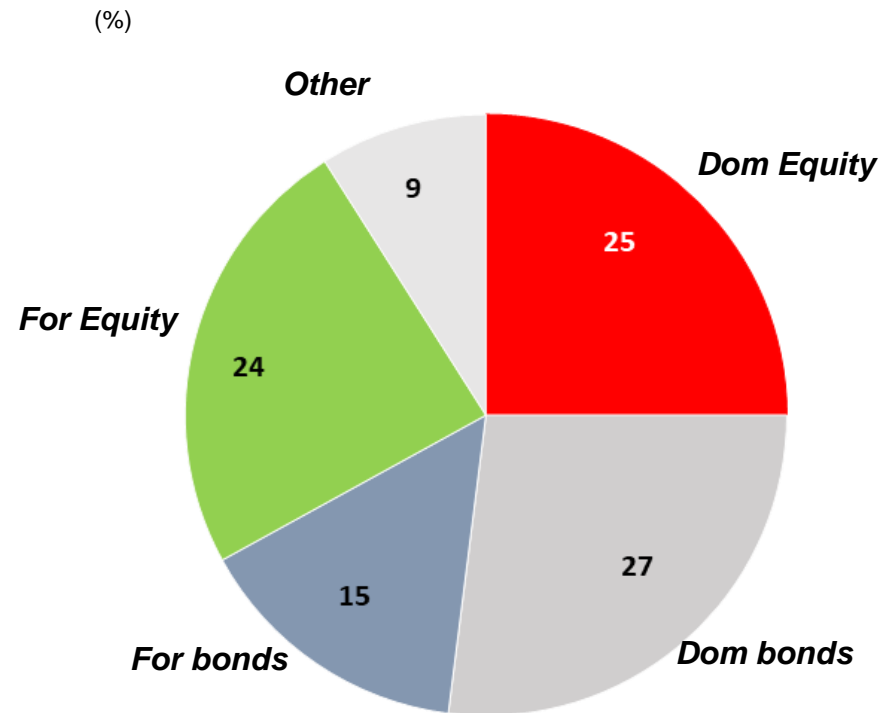


BOJ Owns 5% and GPIF Owns 5%+ of TSE1

BOJ ETF purchases



GPIF-Asset Allocation



Note: As of Aug 9 2019
Source: BOJ, QUICK, data compiled by Goldman Sachs Global Investment Research

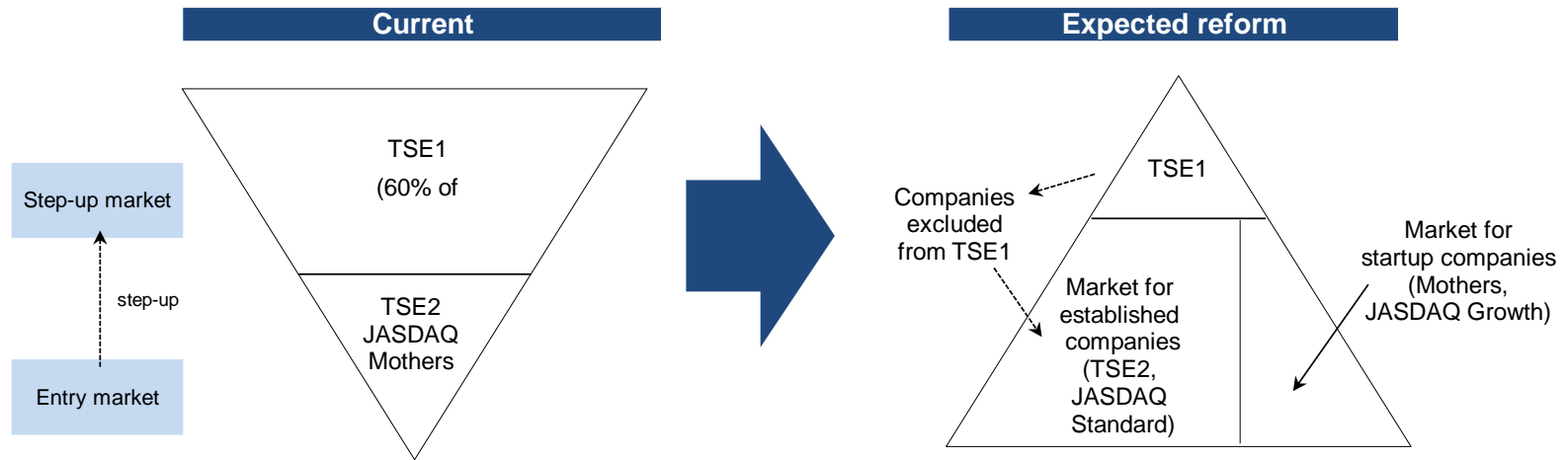
Note: Market cap weightings for indices with ETFs eligible for purchasing, as of Mar 2018
Source: Nikkei Financial Quest, Goldman Sachs Global Investment Research

Stocks with Highest Indirect BOJ Ownership

Stocks with highest indirect BOJ ownership and forecast ownership ratios in one year

	Indirect ownership by BOJ			Market Cap.		Sector	
	31-May-17	31-May-18 (GS Est)	Diff	Ybn			
1	6857	Advantest	16.9%	20.3%	3.4%	395	Electric Appl.
2	9983	Fast Retailing	15.3%	18.3%	3.0%	3,935	Retail
3	6976	Taiyo Yuden	14.4%	17.4%	3.1%	190	Electric Appl.
4	6762	TDK	13.8%	16.8%	3.1%	867	Electric Appl.
5	8028	Familymart Uny HD	13.6%	16.5%	2.9%	788	Retail
6	5707	Toho Zinc	13.0%	15.9%	2.8%	58	Steel & Nonferr.
7	4704	Trend Micro	12.6%	15.4%	2.8%	780	IT & Services
8	1721	Comsys HD	12.3%	14.9%	2.6%	331	Const. & Materials
9	9766	Konami HD	12.0%	14.5%	2.5%	781	IT & Services
10	4021	Nissan Chemical Industries	11.8%	14.4%	2.6%	591	Raw Materials
11	8035	Tokyo Electron	11.1%	13.6%	2.5%	2,592	Electric Appl.
12	6103	Okuma	10.7%	13.1%	2.4%	168	Machinery
13	6988	Nitto Denko	10.7%	13.2%	2.5%	1,545	Raw Materials
14	9301	Mitsubishi Logistics	10.2%	12.5%	2.3%	248	Transportation
15	4272	Nippon Kayaku	10.1%	12.4%	2.3%	281	Raw Materials
16	6971	Kyocera	10.0%	12.4%	2.4%	2,410	Electric Appl.
17	8253	Credit Saison	9.9%	12.1%	2.2%	381	Nonbank Financials
18	3105	Nisshinbo HD	9.9%	12.0%	2.1%	187	Electric Appl.
19	4543	Terumo	9.8%	12.1%	2.3%	1,709	Electric Appl.
20	9681	Tokyo Dome	9.7%	12.0%	2.3%	95	IT & Services
21	6770	Alps Electric	9.7%	12.1%	2.4%	616	Electric Appl.
22	6954	Fanuc	9.6%	12.0%	2.4%	4,442	Electric Appl.
23	7951	Yamaha	9.3%	11.4%	2.1%	706	IT & Services
24	5541	Pacific Metals	9.1%	11.2%	2.0%	56	Steel & Nonferr.
25	2801	Kikkoman	8.9%	11.0%	2.1%	730	Foods
26	2282	Nh Foods	8.9%	11.0%	2.1%	733	Foods
27	9735	Secom	8.6%	10.7%	2.2%	1,889	IT & Services
28	2531	Takara HD	8.5%	10.5%	2.0%	251	Foods
29	5301	Tokai Carbon	8.5%	10.5%	2.0%	128	Const. & Materials
30	3865	Hokuetsu Kishu Paper	8.5%	10.4%	1.9%	178	Raw Materials

TSE Reform Implications: Need for a Better Benchmark Index



Potential changes to TSE1 listing criteria

- A market cap-based redesign of the criteria for new/existing listings is under consideration, with media reports suggesting potential market cap thresholds of ¥25 bn, ¥50 bn, and ¥100 bn.
- Given repeated references to corporate governance in discussions of market structure reform in the advisory group, we think related indicators could be included in listing criteria.

Disclosure Appendix

October 02, 2019

Disclosure Appendix

Reg AC

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