



Reforming Corporate Japan —The Next Chapter

Executive Summary

- The Ministry of Economy, Trade and Industry's recent publication of its "Guidance for Growth Investment" and July's revision to Japan's Corporate Governance Code are the latest milestones in a decade-long program of reforms that have transformed the practices of listed Japanese companies.
- These reforms and an awakened market for corporate control have begun to unlock the value that has long resided on Japanese balance sheets. Along with macro factors, including the end of deflation, the normalization of monetary policy, and a weaker yen, they have contributed to the re-rating of the Japanese stock market.
- From growth prioritization to enhanced board independence, Japan's governance revolution is ongoing—actively engaged investors can help drive further change.

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Investors lacked the mechanism to unlock the value hiding in plain sight on the balance sheets of corporate Japan.

Japan's M&A market has reached unprecedented levels of activity and value.

Tough Love Revisited: Value Trap or Value Opportunity?

In our [Tough Love](#) paper, published in November 2020, we argued that Japan's many high-quality, cash-rich companies trading below their liquidation worth were not permanent value traps but trapped value.¹ We further posited that a decade of governance reforms combined with a slowly awakening market for corporate control would begin to close this value gap. (See Appendix 1 for a timeline of Japan's key corporate governance reforms since the reform program effectively began in 2014.)

2020: Japan the Outlier

As research for our 2020 paper, we ran a screen of stocks trading on global developed markets. These screens were designed to identify companies that met the liquidation criteria of the legendary value investor Benjamin Graham.² Our screen found many more Japanese companies trading below their liquidation value compared with companies in other developed markets.

Why was Japan such an outlier at the start of the decade? We argued it was because investors lacked the mechanism to unlock the value hiding in plain sight on the balance sheets of corporate Japan. Although enterprising investors could theoretically take over these companies and realize their value, the country's weak market for corporate control had historically prevented them from doing so.

To understand why the market for corporate control was underdeveloped, we need to consider the corporate governance landscape of post-war Japan. It was one defined by stable shareholders and insider-dominated board structures. This undynamic combination protected underperforming management teams from the external discipline instilled by a well-functioning market for corporate control.

The presence of strategic shareholders (also referred to as cross-shareholders), who held other companies' shares for business relationship purposes rather than purely for investment returns, was the hallmark of this cozy corporate club. Such investors hindered the market for corporate control as they owned a sizable portion of the Japanese stock market and reflexively backed management teams. Hostile takeover bids were rarely launched. And when they were, they almost never succeeded. In short, the machinery for disciplining underperforming management simply did not function. As a result, Japanese equity valuations languished, with the TOPIX Index trading at just 1.4x tangible book value in 2020, a fraction of the market valuation multiples for the US and Europe.³

Change was coming, however. Corporate governance reforms implemented prior to 2020 had already begun to shift management behavior and empower engagement and activist investors. In time, investor engagement would become a powerful tool in helping to unlock trapped value.

2026: Record M&A Activity and Unsolicited Bids

Over half a decade on, evidence of this change is widespread, not least in Japan's M&A market, which has reached unprecedented levels of activity and value. Driven by corporate restructuring and the pressure for capital efficiency created by governance reforms, deals totaled an all-time high of approximately \$386 billion in 2025, a 33% increase from the previous year.⁴

The Ministry of Economy, Trade and Industry's (METI) introduction of takeover guidelines in 2023 has been an important policy driver of this changed corporate control market. Adopting a culturally friendly tone, METI reframed hostile bids as socially acceptable "unsolicited" bids. While not legally binding, the guidelines substantially increased the pressure on boards to fulfill their duty to consider fully all credible bids. Corporate buyers now launch contested and unsolicited takeover bids that increasingly succeed.

Symbols of progress in the market for corporate control have included Nidec's purchase of Takisawa Machine Tool Company after an unsolicited 2023 bid. The acquisition by the Kyoto-based electric motor maker, widely seen as a member of Japan's corporate elite, marked the first

successful bid by an acquirer holding no prior stake. Another milestone was Dai-ichi Life's successful competing offer for HR services leader Benefit One in 2024—its rival bid eclipsed M3's prior offer. This move established that a blue-chip Japanese incumbent could outbid an agreed deal.

Not Fully Open Yet

Progress in the market for corporate control has not been entirely straightforward, however, particularly in relation to recent foreign bid activity.

In 2025, Alimentation Couche-Tard's (ACT) unsuccessful approach for Seven & i, owner of the 7-Eleven store chain, marked a notable bump in the road to a fully open market for corporate control, given it would have been Japan's largest-ever foreign buyout. This tense, high-profile takeover saga ended after the Canadian retailer eventually withdrew its offer, citing Seven & i's failure to engage constructively with its bid—Seven & i rejected this criticism, and our understanding is that it considered the proposal on multiple occasions.

Seven & i has since adopted a strategy of divesting its supermarket and department-store businesses and focusing on its convenience-store operations. However, the company still appears to have some way to go in delivering a meaningful improvement in corporate value, with the share price currently sitting materially below ACT's offer price.

This year has brought another high-profile indicator that the market for corporate control is not yet fully open. In June, the Japanese government effectively blocked the acquisition of machine-tool maker Makino Milling Machine by South Korean private equity firm MBK Partners on national security grounds, due to the Japanese defense industry's heavy use of Makino's machine tools.

While disappointing for shareholders, at least in Seven & i's case, it is worth putting these recent isolated setbacks in perspective. After all, the market for corporate control did not develop in a linear fashion in the US or Europe either.

When set in a historical international context, we believe these frictions look less like backsliding and more like a normal evolution. In our view, the likely final shape of Japan's corporate control market will not be the maximally open, highest-bidder-wins ideal. Instead, we believe it is likely to be a hybrid settlement: open enough to discipline management yet tempered by board discretion and strategic-sector protection. In that sense, it will likely be closer to the European model than to the pure Anglo-American one.

METI's own July 2026 restatement of its 2023 M&A guidelines reinforces this reading. Rather than revising the guidelines, METI reaffirmed that Japanese boards are not bound by a US-style Revlon duty to maximize short-term price on a sale, and that a higher offer price does not necessarily constitute a more desirable acquisition.⁵

A Surge in Shareholder Activism and Private Equity Activity

The revolution in the market for corporate control has had clear consequences. Japan has evolved into the world's second-most active market for activist shareholders after the US, marked by a substantial increase in public campaigns and shareholder proposals. By 31 July 2026, Japanese companies had received 190 shareholder proposals at this year's annual general meetings (AGMs), up sharply from 61 in 2020.⁶ Lazard's own "H1 2026 Review of Shareholder Activism" corroborates the surge in activism from a different angle: Japan recorded a new high of 52 activist campaigns in H1 2026 alone, up 53% year on year, and was the main driver of a record number of activist campaigns in the Asia Pacific region.⁷

Global private equity firms now regard Japan as one of the most attractive markets outside the US.

While few motions passed at these AGMs, there was a notable increase in proposals concerning director appointments/removals, majority independent boards, governance reforms, and measures to boost capital efficiency and shareholder returns. We believe this trend will continue and will motivate boards to take measures to enhance corporate value.

Based in part on recognition of these governance and control changes, private market deal flow has also increased as Japanese companies exit non-core businesses. Global private equity firms now regard Japan as one of the most attractive markets outside the US. This is reflected in deal flow. Private equity deal value in Japan reached ¥4.8 trillion in 2025, the fifth consecutive year that annual deal value passed ¥3 trillion.⁸

Changed Corporate Behavior and Increased Shareholder Returns

This newly invigorated market for corporate control, combined with a raft of other corporate governance reforms implemented over the past decade-plus, has had other noteworthy effects:

A steady decline in strategic shareholdings: The value of Japanese companies' domestic equity holdings as a percentage of their market cap has dropped from 13.3% in December 2022—a few months before the Tokyo Stock Exchange (TSE) introduced reforms requiring companies trading below their book value to disclose specific plans to improve capital efficiency—to 9.6% as of 30 June 2026.⁹

This unwind has accelerated lately, particularly in the case of the megabanks and insurers, which typically had the highest levels of strategic shareholdings. Regulation has partly driven disposals in these sectors. The Financial Services Agency (FSA) introduced rules

Governance reforms and pressure from the government to improve capital efficiency and shareholder returns have led to a surge in shareholder distributions.

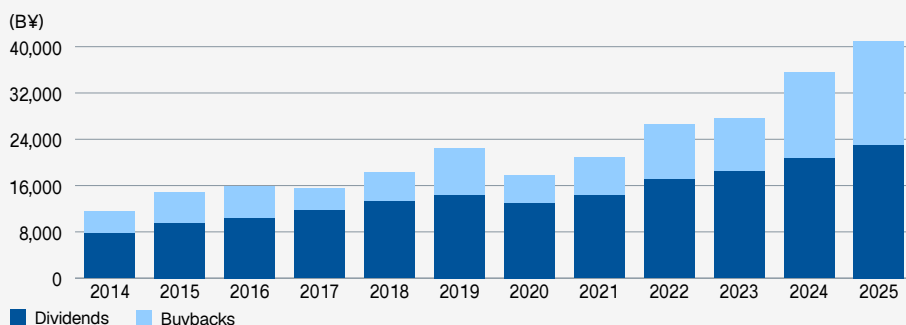
in 2024 preventing insurance companies from holding shares for commercial relationship purposes. As a result, both life and non-life insurers have sold their strategic shareholdings. In response, other financial institutions, including banks, have reduced such cross-shareholdings. The need to comply with Basel III risk-weighting rules has served as another reason for banks to divest.

Reduced strategic shareholdings have been reflected in voting patterns at this year's AGMs. With fewer compliant shareholders, the number of votes cast against the re-election of representative directors has risen.

Increased shareholder distributions: The TSE's aggressive governance reforms and pressure from the government to improve capital efficiency and shareholder returns have led to a surge in shareholder distributions since the start of the decade. Share buybacks and dividends have reached successive record highs, hitting ¥41 trillion in FY 2025, up from ¥18 trillion in FY 2020 (Exhibit 1).¹⁰

Exhibit 1

Cash Back—The Acceleration in Shareholder Distributions



As of 30 June 2026

Source: Bloomberg, TOPIX

A Market Re-Rating but Still Lagging Internationally

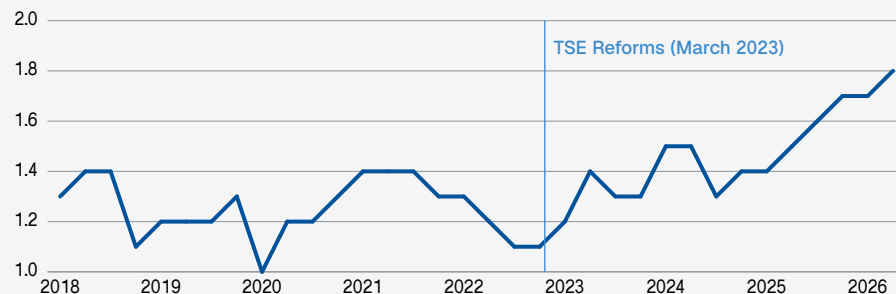
The positive developments outlined above have contributed to a significant re-rating of the Japanese market in recent years:

- The price-to-book ratio of the broad TOPIX Index has climbed from around 1.0 at the start of the decade to 1.8 (Exhibit 2).

Exhibit 2

The Steady Re-Rating of the Japanese Equity Market

TOPIX Index Price-to-Book Ratio



As of 30 June 2026

Source: Bloomberg

- The share of TOPIX 500 companies trading with a price-to-book ratio below 1.0 has fallen from 44% at the end of December 2022—a few months before the TSE's capital efficiency reforms—to 36%.¹¹

Admittedly, this progress must be placed in a global context: only 2% of companies in the S&P 500 Index and 10% of companies in the MSCI Europe Index currently trade below their book value.¹²

The Next Chapter

Despite this story of genuine progress, Japan's trapped corporate value has not been fully realized; instead, it has moved. It has shifted from the balance sheet restructuring outlined in our Tough Love paper to a comprehensive focus on sustainable growth through management of the business portfolio.

For decades, many Japanese corporations were held back by conglomerate structures that often undermined their returns on equity and market valuations (see “Curse of the Conglomerates?” overleaf). This structural weakness was publicly addressed in 2020 with METI's publication of a document widely referred to as its “Business Portfolio Guidelines”. This influential paper (only available in Japanese) was designed to challenge the cultural taboo among Japanese business leaders about exiting non-core businesses. Its most salient sections encouraged companies to classify their business portfolios using a growth versus return-on-invested-capital matrix and asked them to consider who was the ‘best owner’ of a business unit to maximize its potential.

METI's paper was widely influential. Several companies diligently classified their business portfolios in the suggested format. It also provided a framework for investors to deepen engagement discussions with company management teams. However, METI's proposals were largely defensive in nature. Many companies complied in form but not in substance, as reflected in boilerplate capital-efficiency disclosures and share buybacks announced in lieu of a growth strategy.

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Curse of the Conglomerates?

Conglomerates have long been a feature of Japan's corporate landscape. Indeed, the sprawling nature of many listed businesses has widely been identified as one of the reasons for the country's historically poor record on capital efficiency.

The trend for conglomerates was driven in part by the government-directed, banking-led post-war reconstruction of the Japanese economy. This emphasized corporate diversification to reduce the banking sector's credit risks. It also stemmed from a labor surplus, particularly in white-collar industries, that encouraged overstaffing in a country where societal norms and legal constraints make it hard to fire permanent employees. Adding non-core business lines was a way of finding a home for oversized workforces.

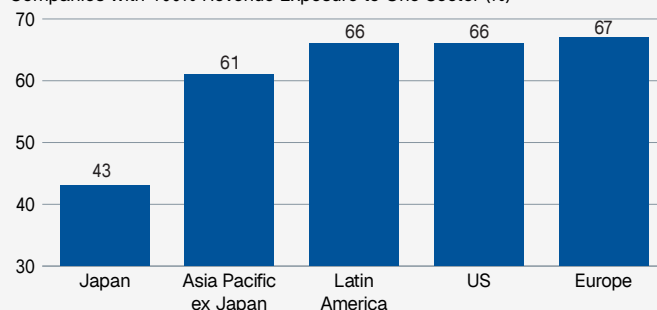
Japan's shrinking labor supply in recent years has altered this latter dynamic. But while progress has been made by many companies in rationalizing their corporate structures, there is still room for improvement: Only 43% of listed Japanese companies are exposed to just one sector. This contrasts with more focused business approaches globally (Exhibit 3).

A diversified business approach can come at the expense of capital efficiency. Companies that concentrate on just one or two sectors tend to generate higher returns on equity and enjoy higher profit margins compared with companies that operate across multiple business lines (Exhibit 4).

Exhibit 3

Japanese Companies are Relatively Less Focused by Business Lines

Companies with 100% Revenue Exposure to One Sector (%)

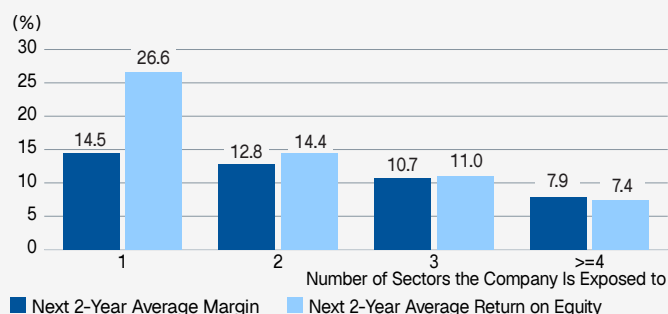


As of 31 July 2026

Source: Jefferies

Exhibit 4

Focus Brings Higher Returns and Margins for Japanese Companies



As of 31 July 2026

Source: Jefferies

METI's "Guidance for Growth Investment"

In July 2026, METI released an important update, its "Guidance for Growth Investment".¹³ This report estimates that roughly 65% of invested capital in Japan sits in value-destroying segments. It suggests that business portfolio reorganization has so far been too timid. The document goes on to urge a pivot from the defensive restructuring of its 2020 guidelines to an assertive focus on growth. Japanese companies are no longer just being asked to trim the fat; they are being pushed to aggressively redeploy capital into growth.

METI's updated guidance speaks directly to the evolution of Japan's reform agenda. The focus has moved toward scrutiny of excess cash, the allocation of corporate resources to sustainable growth, stronger and more effective boards, and a renewed insistence on capital efficiency as a matter of substance rather than compliance. This is the next chapter in the reform story: the shift from ending value destruction to going for growth.

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METI's recommendations directly align with recent parallel revisions to Japan's Corporate Governance Code by the FSA and the TSE.¹⁴ Together, both publications signal a macro-level transition at work in Japan (see Appendix 2 for additional details).

Qualified Progress Made, Opportunity Ahead

Japan's corporate revolution remains a work in progress. Gaps in governance remain, including around board composition and incentivization. About 30% of Japanese companies have majority-independent boards—versus roughly 95% in the US—not helped by a language barrier that restricts the outside-director talent pool compared with the US and Europe.¹⁵

And while we welcome the progress that has been achieved, we do not claim that the robust performance of Japanese equities over the decade to date is solely due to better corporate control and governance. A weaker yen, the normalization of monetary policy with deflation's demise, and a tentative global reallocation toward Japanese stocks have all contributed to the market's recovery. This macro context matters. The return of sustained positive inflation rates and inflation expectations has underlined the imperative for Japanese companies to close the gap with their overseas peers in terms of capital efficiency and growth.

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Looking ahead, policy reforms by the Japanese government and the TSE have empowered investor engagement and opened Japan's market for corporate control. We believe this has created a significant opportunity for engaged, active institutional investors. Activist investors continue to enjoy high-profile, short-term successes in the Japanese market, usually registered in dividend hikes, more share buybacks, or larger M&A deal premia. But as business strategies shift from defense to offense, the importance of a more constructive, behind-the-scenes active engagement approach based on mutual understanding and trust has increased. This is because achieving the superior returns on investment needed to boost long-term corporate value requires two things: deep insight and a time horizon beyond the focus of many market participants.

Management teams are increasingly listening to institutional investors who can provide a fresh, global perspective and deep industry knowledge, especially investors who can hold these discussions in the Japanese language. Companies realize that engagement is a resource to help them improve their corporate value. Meanwhile, investors understand that engagement enables them to generate alpha for their underlying investors, by benefiting from the rise in corporate value and recognizing the change ahead of the market.

Tough love has helped unlock the value in corporate Japan. But there is still work to be done. We believe actively engaged institutional investors will benefit from playing their part in the next chapter of the reform story.

Tokyo Stock Exchange Survey Recognizes Lazard's Engagement Capabilities

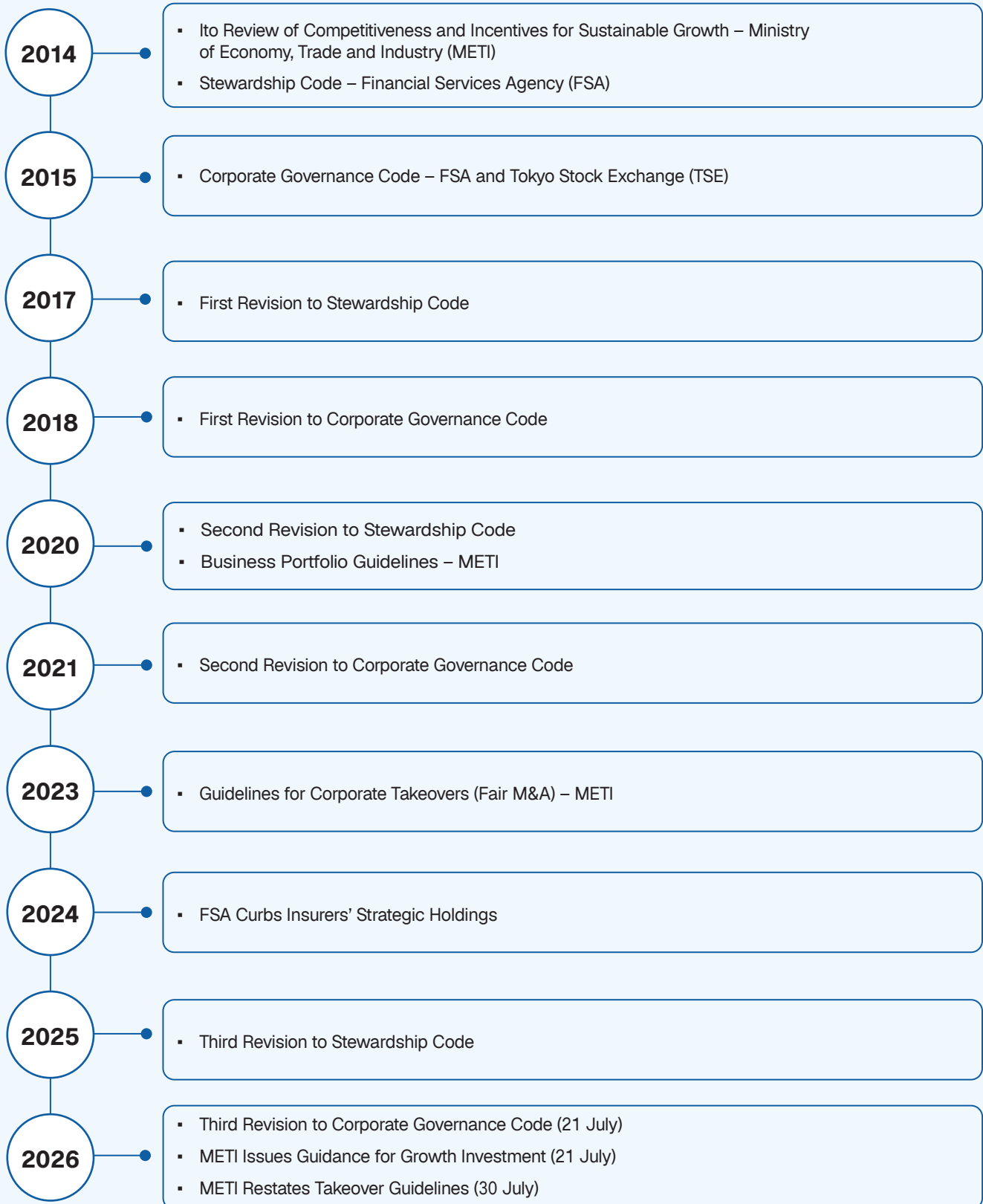
Both the TSE and the FSA have promoted dialogue with shareholders through the Corporate Governance Code, with shareholder dialogue being incorporated into General Principle 1 in the latest revision of the Code.

In August 2026, the TSE published the results of its first-ever survey on shareholder dialogue.¹⁶ A total of 682 companies participated, comprising 395 Prime Market companies, 220 Standard Market companies, and 67 Growth Market companies. The survey asked listed companies whether their dialogue with investors was meaningful and which types of investors provided the most meaningful engagement.

Lazard Asset Management was named as one of 15 institutional investors achieving the highest number of citations for engaging in "meaningful dialogue." We believe this survey result recognizes the constructive and meaningful discussions that investment professionals across our firm have had with Japanese companies.

Appendix 1

A Decade-Plus of Reform: Key Highlights



Appendix 2

The Next Chapter of Reform: METI's Guidance for Growth Investment and an Update to the Corporate Governance Code

July 2026 saw the most recent developments in the Japanese corporate governance reform story: METI's publication of its "Guidance for Growth Investment"—published in Japanese only and therefore we believe perhaps overlooked by many Western institutional investors—and the latest update of the Corporate Governance Code. Both documents promote reforms with the same aim: to move from compliance-based governance to governance targeting growth and capital efficiency.

1. METI's Guidance for Growth Investment

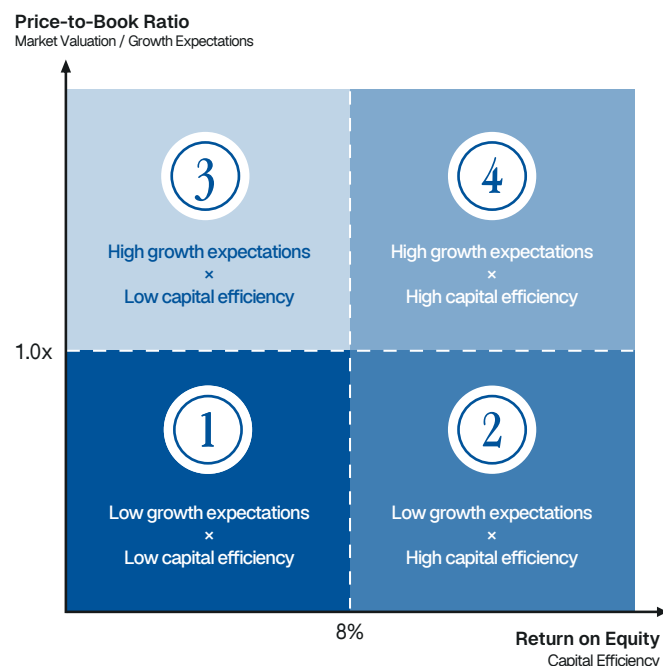
METI's core argument is that capital efficiency has improved since its 2014 Ito Review,¹⁷ yet higher returns have not translated into corporate investment or wage growth. Its proposed solution is not more share buybacks or higher short-term returns but a reallocation of economic profit (returns above a company's cost of capital) into medium- and long-term growth investments.

METI's main observations and proposals:

- The introduction of a new quadrant map plotting price-to-book ratio against return on equity as a guide for companies (Exhibit 5). This updates the 2020 business-reorganization framework incorporated in Japanese business plans. Companies are expected to target the high-return, high-valuation quadrant (upper right).

Exhibit 5

METI's Valuation Framework



Source: Lazard, METI. For illustration purposes only.

- Japanese companies have been too timid in the reorganization or simplification of their business portfolios. As noted earlier, according to METI, roughly 65% of the invested capital of Japanese companies sits in value-destroying business segments.
- The government should facilitate business reorganizations (e.g., spin-offs and M&A) via tax measures and encourage shareholders to engage on the topic.
- Explicit criticism of idle cash, cross-held investment securities, and surplus property.
- Companies should lower their weighted average cost of capital alongside investing and employ credible CFOs with genuine authority over capital allocation.
- Caution against "short-term" share buybacks and cost-cutting as substitutes for investment—although buybacks are accepted where investment opportunities are absent.

2. Revised Corporate Governance Code

The Code remains principles based, requiring companies to adopt a comply-or-explain approach to governance. Although it may not be legally binding, we find that it provides useful leverage in company engagement—we provided a submission to the FSA and the TSE ahead of the Code update as part of their dialogue with stakeholders. In scale, the July 2026 revision is the most significant since the Code's 2015 introduction. The principles subject to comply-or-explain were streamlined from 83 to 30, with supporting detail moved into new, non-binding interpretive guidance, and the Code's five sections were consolidated into four—"Dialogue with Shareholders", formerly its own section, was folded into General Principle 1.

The stated shift of the 2026 Code update is from defensive to growth-oriented governance. The main changes include:

- Shareholder dialogue—Directors, including independent directors, should engage with shareholders. Our public comment suggested going further by requiring companies to arrange meetings with independent directors upon request.
- Cross-shareholdings—Companies whose shares are held by another company must not obstruct the seller by threatening to reduce the business relationship.
- Business plans—Business plans must be disclosed while accurately identifying cost of capital, with the inclusion of profitability and capital-efficiency targets that reflect a company's growth stage and the associated opportunity costs. Interpretive guidance adds that boards should persistently review whether cash and real estate are being used efficiently.
- Board independence—Independent directors should make up at least one-third of the boards of Prime Market-listed companies, and a majority where a controlling shareholder exists.
- Minority protection—A recommendation for safeguards around takeover defenses, change of control, and management buyouts. Unfortunately, no specific measures were prescribed.
- Annual securities report timing—The *Yuho* annual securities report should be made public at least three weeks before an AGM, possibly pushing back the timing of the AGM.

Important Information

Notes

1. Source: Lazard. [Tough Love: How a More Effective Market for Corporate Control Will Unlock Trapped Value in Japanese Companies](#), Lazard. November 2020.
2. See Security Analysis, Benjamin Graham and David Dodd. The main filter for our 2020 screening was that current assets minus total liabilities must exceed market capitalization, although we also applied some other liquidity and quality metrics.
3. Source: Lazard and Bloomberg. Data as of 21 June 2020.
4. Source: JP Morgan and Dealogic. Data as of 31 January 2026.
5. Source: METI, [Key Points of the Guidelines for Corporate Takeovers](#), 30 July 2026, Section 5.1. In US corporate law, the Revlon Rule compels the board of directors to seek the highest value in a hostile takeover situation.
6. Source: [IR Japan](#). Data as of 31 July 2026.
7. Source: Lazard, [Review of Shareholder Activism – H1 2026](#), 1 July 2026 and IR Japan meeting material, 15 September 2026.
8. Source: [Bain & Company](#). Data as of 29 June 2026.
9. Source: Jefferies. Data as of 31 July 2026.
10. Source: Bloomberg, TOPIX. Data as of 30 June 2026.
11. Source: Bloomberg. Data as of 30 June 2026.
12. Source: Bloomberg. Data as of 30 June 2026.
13. Source: METI, Guidance for Growth Investment. Published 21 July 2026. [English language summary](#).
14. Source: [Japan Exchange Group](#). Published 21 July 2026.
15. Source: Tokyo Stock Exchange (Data as of 21 July 2026), 2026 US Spencer Stuart Board Index (Data as of 22 September 2026).
16. Source: Tokyo Stock Exchange, Listing Department: [Results of Corporate Survey on Expectations of and Requests to Investors](#), 12 August 2026. (Section 11).
17. Source: METI. [Ito Review of Competitiveness and Incentives for Sustainable Growth — Building Favorable Relationships Between Companies and Investors](#). Published August 2014.

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TOPIX is a free-float adjusted market capitalization-weighted index that is calculated based on all the domestic common stocks listed on the TSE First Section. TOPIX shows the measure of current market capitalization assuming that market capitalization as of the base date (January 4, 1968) is 100 points. This is a measure of the overall trend in the stock market, and is used as a benchmark for investment in Japan stocks.

The S&P 500 Index is a market capitalization-weighted index of 500 companies in leading industries of the US economy.

The MSCI Europe Index is a free-float-adjusted market capitalization index that is designed to measure equity market performance in the developed markets countries of Europe.

The indices are unmanaged and have no fees. One cannot invest directly in an index.

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