sector
asset management

Japanese Companies Buying Up Units Helps Hedge Fund’s 30% Return

Sector Zen Fund featured in Bloomberg article

(Bloomberg) -- A shift in the board rooms of Japan’s biggest companies to buy back or sell out of listed subsidiaries has delivered a 30% return for an Oslo-based hedge fund. And it’s betting the pattern will continue this year.

By Jonas Cho Walsgard

Sector Zen, which is a Japanese long/short equity fund, held six companies that were bought up last year. The $170 million fund has returned 9.1% a year on average since starting in 2006, with last year’s 30% return outpacing the 15% gain in Tokyo’s benchmark Topix index.

The type of deals benefiting the Sector Zen fund may gain impetus from efforts by the Tokyo Stock Exchange to improve governance within Japan’s sprawling conglomerates, so-called keiretsu. The exchange sought public comment on its proposals in November, with some changes potentially taking effect in February. The Tokyo bourse’s moves may push the dissolution of parent-subsidiary listings into “full swing” during 2020, Citigroup Inc. analyst Kota Ezawa wrote in December. “It’s the big game changer for Japan,” Trond Hermansen, investment manager for the Sector Zen fund, said in an interview in Oslo, adding that companies have to do more to protect shareholder returns. Buyout news can spur sharp gains in Japanese stocks: Toshiba Plant Systems & Service Corp. jumped 17% in a single session in November, after parent Toshiba Corp. announced plans to make it a wholly owned subsidiary. Toshiba’s Nishishiba Electric Co. surged 76% in two days for the same reason, while unit NuFlare Technology Inc., which Sector Zen held, surged 45% over three sessions. Just last week, Bain Capital offered to buy Mitsui E&S subsidiary Showa Aircraft Industry Co., in which Sector Zen owns a stake, the fund manager said. The stock rose 7.2% in Tokyo trading on Friday and has almost doubled in value since the start of November.

Long Positions

Buyouts tend to unlock increased value in these subsidiaries that isn’t fully represented in their share prices because of assets that investors holding the stock can’t benefit from, Hermansen said. These can include large cash holdings, stock portfolios and property values that aren’t reflected in their balance sheets, he said. Of the 40 long positions Hermansen holds, Hitachi Construction Machinery Co., Hitachi Metals Ltd., Nomura Real Estate Holdings Inc., Cosmos Initia Co. and Kyowa Kirin Co. offer the biggest takeover potential. And he expects to see more transactions this year than 2019, which he described as a “breakthrough” year. “It’s an incredibly interesting investment case,” he said. “Completely unrelated to the macro situation. This is company specific.”

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