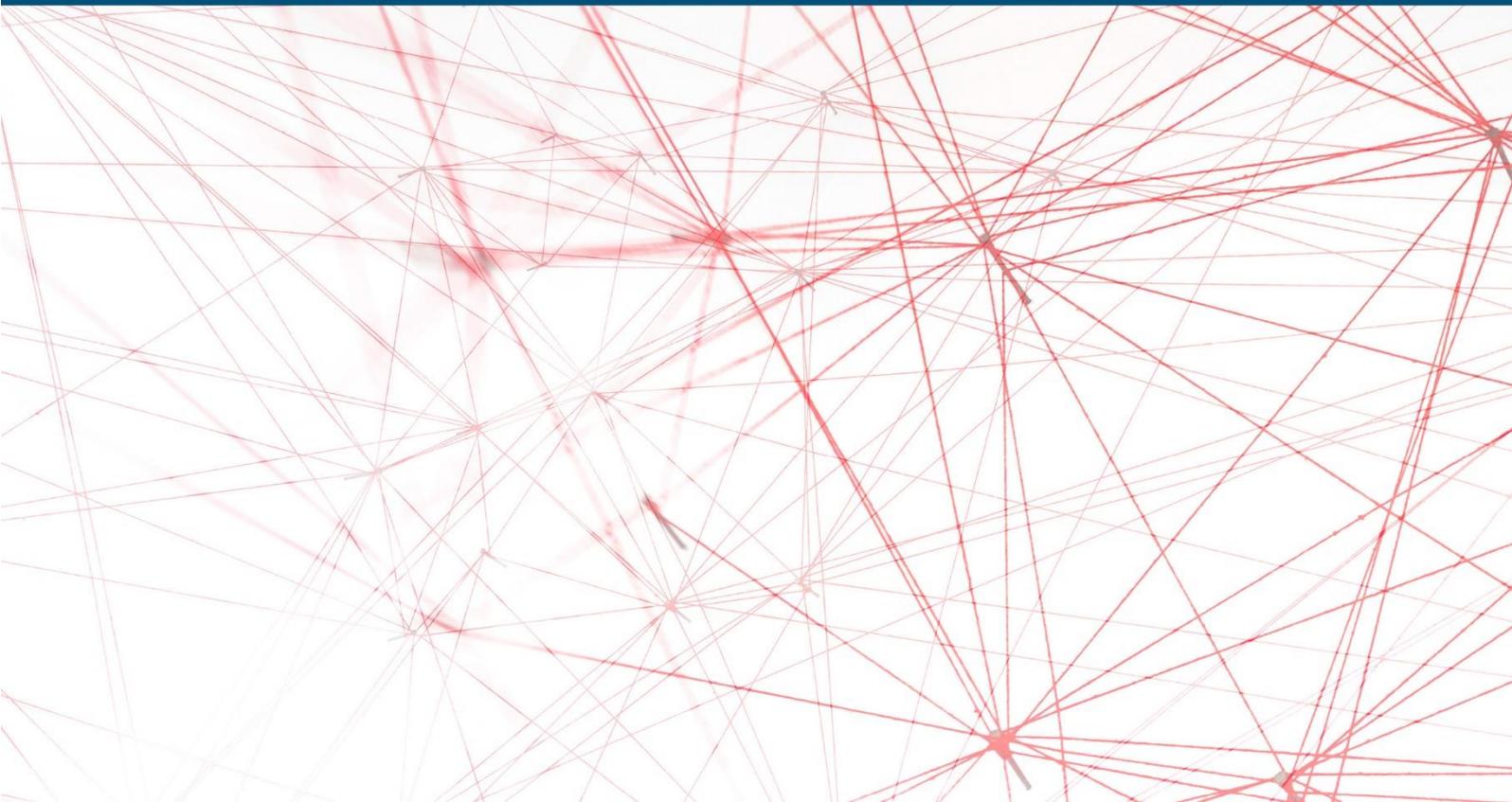




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JAPAN-AUSTRALIA M&A: 2020 REVIEW AND FUTURE TRENDS

4TH EDITION - MARCH 2021



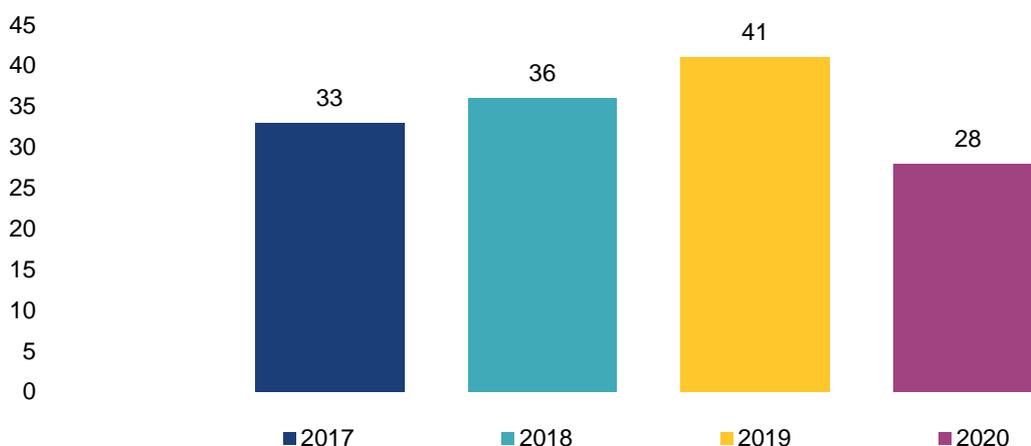
COVID-19 impacts on investment were immediate and significant

What review of 2020 could start without starting with COVID-19? This is our fourth annual review of the transactions and prevailing trends comprising Japan and Australia's investment relationship. Our March 2020 3rd edition covered 2017 to 2019 and was titled "*More good news - more deals, more dollars and more sector diversity*".¹ The expectation was that, as the identified trends continued to develop, there would be increasing investment and expansion of this relationship in 2020 and beyond.

However, last year's report was published on the eve of the COVID-19 pandemic. Who could have predicted, weeks before the closures of borders around the world, just how fundamental its impacts would be on the international economy, travel and trade?

The pandemic had a profound and immediate effect on Japanese investment in Australia. 2020 saw a slight decrease in the number of announced or completed transactions in comparison to the previous three years and the absence of a "mega-deal" (deal value greater than A\$1 billion).

Deal count by year



Fundamentals of the investment relationship endured the pandemic

COVID-19 had an early and significant impact on Japanese investment in Australia in 2020 but the pandemic did not solely define the year or redefine the underlying trade and investment relationship. The fundamentals of the Japan-Australia relationship are deep and enduring, and make it well-positioned for a strong recovery in investment more promptly than many other jurisdictions around the world.

The exciting news is that there was a continuation of the sector diversification that we expect will further expand once business travel restrictions are relaxed. Japanese companies are becoming increasingly sophisticated in both the way they invest and implement post-merger integration. The positive investment outlook is further facilitated by the recent removal of a majority of Australia's restrictive foreign investment rules which were imposed on 29 March 2020 as a direct result of the pandemic.

While the return to more positive trade and market conditions at the end of 2020 help to explain the returning strength of the Japan-Australia investment relationship in the latter half of 2020, there are also longer-term geopolitical changes beginning to emerge. 2020 was a pivotal year in international trade and relations, and some of the changes we saw may prove to be the start of some seismic shifts in the global order.

Specifically, 2020 saw an increasing focus on climate change targets, trade disputes with China, BREXIT, change in leadership in Japan, and a new Biden administration in the US that together have raised questions about the future of trade and investment policies. These events have caused Australians to reflect upon the importance of a trading partner in the region that shares Australia's democratic and egalitarian values and its adherence to an international rules-based trading system. Japan fills this role perfectly.

The value of the Japan-Australia relationship is therefore more deeply understood and respected now than perhaps ever before, and our mutual confidence in each other as economic and political partners and allies may well form the basis of new investments and trends as we look to weather the post-COVID investment environment.

¹ <https://www.herbertsmithfreehills.com/latest-thinking/Japan-Australia-M-A-Review-and-Trends-2017-2020>.

2020 Observations about Japan-Australia M&A

Japanese investment in Australia during 2020 can be characterised by the following overarching trends:

- None of the underlying macro-economic factors that previously have driven investment have changed.
- Very few new entrants to the Australian market, which is not surprising given the difficulty in undertaking due diligence and negotiations without being able to physically visit Australia.
- An acceleration in implementing mid-term business plans, which resulted in a mixture of divestments in traditional areas and an increased focus on investment in new emerging sectors.
- Global trends toward decarbonisation (“zero net carbon”) and against carbon-emitting industries are having a very strong and swift impact, especially for listed Japanese corporates.
- “New Energy” becoming a very attractive investment opportunity and being strongly supported by the Japanese and Australian Governments, financiers, energy companies, engineering firms, trading houses and funds.

Prediction

Our prediction is that our 2020 headline of “*more deals, more dollars and more sector diversity*” will return in 2021 and be even more pronounced within the next 18-24 months.

We have already seen an active start to 2021, and we predict this will continue – particularly from those who are able to take advantage in the short to medium-term of an established network in Australia, as they continue to invest in new sectors as part of their mid-term business plan to diversify revenue sources. We look forward to reporting on this trend in next year’s report. Assuming international business travel between Australia and Japan will have resumed by the end of 2021, we also expect there will be a significant number of new entrants coming into the Australian market, continuing the trend we saw emerging during 2017 to 2019.



Japan-Australia M&A: 2020 Review and Future Trends

MARCH 2021

Japanese M&A

Deals and value both down

There were 391 domestic Japanese M&A transactions (with a total value of US\$160 billion), representing the lowest deal count since 2015.

Japanese cross-border M&A also declined. 2020 saw 179 transactions with a total value of US\$34.11 billion which was a significant downturn from 2019's 348 transactions with a value of US\$95.97 billion.

New entrants markedly absent

International travel restrictions imposed around the world had an impact on Japanese corporates who had limited abilities to have face to face meetings with the counterparties' management. Even though video conferences largely replaced physical meetings in 2020, Japanese management continue to prefer face to face meetings. As such, Japanese corporations with presence on the ground were able to manage this issue and continue with business, albeit with interruptions and uncertainty, but very few deals involved new entrants to outbound destinations.

Australia-Japan relationship

Fundamentals unaffected by 2020 global uncertainty

Against this backdrop of subdued Japanese cross-border investment and global uncertainty, it is notable that the fundamentals of the Australia-Japan relationship showed their underlying strength in 2020.

The two countries share basic values in democracy, market economy, respect for human rights and the rule of law. Japanese investment in Australia continues to be welcomed by the Federal and State Governments in Australia. After the events of 2020, Australia's relationship with Japan is arguably even more important than ever, both economically and politically.

Diplomatic ties strengthened and emphasised

In 2020, security and economic bilateral talks continued notwithstanding the COVID-19 pandemic, including the Australia-Japan Ministerial Economic Dialogue in January 2020 in Australia. In September 2020, newly appointed Japanese Prime Minister Suga held his first talks by phone with Australia's Prime Minister Scott Morrison. Significantly, in November 2020, notwithstanding the need to quarantine on his return, Mr Morrison visited Japan to meet Prime Minister Suga, his first and only

2020 overseas destination since the COVID-19 pandemic began. This sent a clear message of the importance placed on the Japan-Australia relationship.

As key members of the Comprehensive and Progressive Agreement for Trans-Pacific Partnership (**CPTPP**) and the Regional Comprehensive Economic Partnership (**RCEP**), Australia and Japan are in a prime position to work together to promote further economic development in the Indo-Pacific region. These multilateral relationships add a further incentive to deepen our bilateral ties and create new opportunities to develop new and resilient supply chains.

Investment is strong and growing

Japan remains one of the 3 largest investors into Australia with A\$109 billion of direct investment and is the largest in our region. Only the United States (A\$205 billion) and the United Kingdom (A\$127 billion) have higher values invested.

The scale and significance of Japan's investment in Australia has only increased in recent years. This is best exemplified by INPEX's Ichthys LNG project in the Northern Territory. The project – a joint venture between INPEX, Total, Tokyo Gas, Osaka Gas, Kansai Electric Power, JERA, Toho Gas and Taiwanese entity CPC Corporation – commenced production in July 2018 and involved:

- a total capital cost of US\$37 billion (the largest ever overseas investment undertaken from Japan).
- a loan for US\$5 billion by the Japanese Government (through Japan Bank for International Cooperation (**JBIC**)), together with a large banking syndicate. This is the largest ever loan made by JBIC.
- the creation of nearly 8,000 jobs in Australia.

Japanese companies remain amongst the highest taxpayers in Australia (especially companies with iron ore investments), are in the top 10 largest exporters of Australian iron ore, coal, LNG, oil, wheat, woodchips and salt, and have long been considered some of our best corporate citizens.

The future is a diversifying investment relationship

Despite the decrease in deal number and value in 2020, the fundamentals of the relationship indicate that 2020 will be seen as a year of continued diversification, realignment and consolidation after record investments in 2019.

This can be seen in the marked shift in strategic approach many Japanese companies have made in relation to Australia: focusing now on “Asset Changeover” from energy, minerals and agriculture to renewables, biomass, post-mine regeneration, hydrogen (blue and green), infrastructure development, healthcare, digital transformation (known as **DX**), circular economy and technology in all forms.

The diversity of new target sectors suggests both the continuation of Japanese inbound investment and an increase in the diversity and sophistication of the Australian economy. It is recognition by Japanese companies of the importance of the relationship with Australia and that demonstrating growing awareness of the breadth of the opportunities for Japanese companies in Australia.

The positive influence of COVID-19

Australia’s attractiveness as a destination for future Japanese investment also benefited from the strong response of Australia and its healthcare system to the pressures of COVID-19, ranking 8th in the world for its response to the pandemic based on the number of cases and the confirmed deaths and testing rates. Politically, the crisis has also been viewed by Japanese businesses as being well-managed.

COVID-19 has caused countries to look locally and to their neighbours in the region to secure food supplies, manufacturing and supply chains as the challenges of a pandemic introduced new and previously unappreciated risks to the globalised, deregulated trade environment.

This reorientation towards regional trade may contribute to greater trade and investment relations between Japan and Australia as the two major economies located in the Asia Pacific Region.

Key drivers for the future

The underlying drivers of Japanese investment into Australia in the short, medium and long-term are:

Short-term	<ul style="list-style-type: none"> Japanese corporates have substantial cash reserves on their balance sheets (US\$5 trillion as at May 2020) and access to low interest finance. Australia, due to its large physical size and relatively small population, has numerous oligopolistic markets which can de-risk an acquisition of the company with an established and profitable client base. Australia is widely considered to have managed its exposure to COVID-19 well and is expected to recover more quickly than other key investment destinations for Japan.
Medium-term	<ul style="list-style-type: none"> Economic growth in Australia driven by both the natural birth rate and steady skilled and business immigration (which improves the demographics as skilled migrants are younger and will need to acquire housing and other services). There are some industry markets which have not been consolidated such as housing (the largest home builder has a 4% market share) and motor vehicle dealerships. These businesses are often family-owned and therefore capital constrained. Japanese investors are able to access finance to consolidate and grow these businesses and extract efficiencies. Japan is in the process of updating its corporate governance code around three pillars – strengthening the role of boards; making core management more diverse; and improving disclosures on the environment. These changes, together with broader macroeconomic factors such as Prime Minister Suga’s 2050 carbon neutral goal, are likely to focus Japanese corporate interest on ESG-conscious investments.
Long-term	<ul style="list-style-type: none"> The aging and decreasing population in Japan will mean that most domestic markets will continue to shrink. Common values in democracy, market economy, respect for human rights and the rule of law. Corporate governance, of ever-increasing importance to Japanese companies and shareholders, is well-accepted and understood. Japan’s transition to a zero emission nation will align with Australia’s endowment of natural resources and renewable energy sources.

2020 Review

Although 2020 was dominated by the impacts of COVID-19, it was also remarkably consistent with our previous observations about the growth and sector diversification of Japanese M&A in Australia, allowing for the immediate impacts of global lockdowns and economic uncertainty. 2020 saw a number of existing investment trends continue in industries which were relatively unaffected by COVID-19, as well as a recovery towards the end of 2020 in industries that were affected.

COVID-19 Impacts

Overall, we observed three key impacts as a result of the pandemic:

1. Existing trends continued at a slower pace, and while deal value remained high in some industries such as financial services, the overall risk appetite of investors was noticeably lower due to the risk of business interruptions caused by the uncertainty of lockdowns.
2. The continuation of international travel restrictions has made it difficult for newcomers to successfully execute acquisitions. Some Japanese companies still struggle to meet the timetable requirements in competitive sales processes when competing against domestic Australian companies. However, with Japanese companies having to adopt new technologies to adapt to remote working, Japanese companies are slowly becoming more accustomed to engaging in competitive sale processes remotely.
3. Japanese companies with an existing presence in Australia overwhelmingly dominated transactions. Perhaps unsurprisingly, Japanese companies with an office in Australia were able to participate in sale processes or bilateral sale negotiations and there were a number of “bolt-on” acquisitions, such as:
 - **Nomura Research Institute** through its Australian wholly-owned subsidiary ASG acquiring Canberra-based professional services firm Group 10 Consulting.
 - **Nomura Research Institute** concluding an agreement to buy 100% of the shares of Australian Investment Exchange (**AUSIEX**) from Commonwealth Bank of Australia.
 - **Kokusai Pulp & Paper** through its Australian wholly-owned subsidiary Spicers acquiring Rojo Pacific.
 - **Kyoshin** acquiring SELC Australia, a language school based in Sydney, after acquiring English Language Company Australia (**ELC**) in 2018.

Continuing M&A activity

Despite the interruptions of COVID-19, the M&A transactions assessed in 2020 continue to support our observations in previous years about the strength of the following trends and sectors in the Japan-Australia investment relationship.

1. Asset recycling

Japanese companies continued to divest from businesses which were no longer aligned strategically or did not meet the financial return threshold. In some cases, the divestments in 2020 brought some of the previous mega deals to a close. Examples of divestments were:

- **Kirin** selling Lion Dairy & Drinks (the last business remaining from Kirin’s acquisition of National Foods in 2007 and Dairy Farmers in 2008) to Bega Cheese.
- **Sumitomo Corporation** selling Emerald Grain to private equity.
- **Japan Post Toll** announcing that it would sell its Toll Global Express business.
- **Mitsui Bussan Woodchip Oceania** selling the hardwood plantation assets of Bunbury Fibre Plantations to New Forests, a forestry investment fund manager. Mitsui is a major shareholder of New Forests, having acquired a 22.5% shareholding in 2016.

In a different category to the above transactions, **Asahi Beverages**, as a result of the conditions imposed by the Australian Competition and Consumer Commission (**ACCC**) on its acquisition of Carlton & United Breweries, sold the Australian rights to Stella Artois and Becks beer brands and the cider brands, Strongbow, Little Green and Bonamy’s to Heineken.

2. Coal

The concept of thermal coal as a necessary “transition” fuel is no longer accepted by environmental and shareholder activists. In this context, trading houses have accelerated the divestment of their interests in thermal coal mines and coal-related infrastructure. For example, **Sojitz Corporation** sold its 10% interest in the Moolarben coal mine to Yancoal and there is speculation regarding **ITOCHU’s** exit from Australian thermal coal after the sale of its shareholding in a major Colombian thermal coal project.

A number of other coal divestments have been undertaken confidentially without any public announcement by either the buyer or the seller to avoid scrutiny. Conversely, **Mitsui Matsushima** acquired a 17% shareholding in coal mining company, Square Resources.

Moreover, the expected replacement of trading houses in thermal coal projects by end-users of thermal coal has not materialised, as ESG considerations raised by shareholders and activists make it difficult for listed Japanese Power Utilities (**JPU**) to invest in coal assets – even though JPUs continue to purchase large quantities of thermal coal to meet Japan’s domestic energy needs.

To date, investments in coking coal have not had the same level of scrutiny from activists, as there is no immediately available replacement in the steel-making process. Even though differentiating the use of thermal coal and coking coal is becoming increasingly difficult, Japanese trading houses continue to actively look for coking coal opportunities, meaning there is strong competition for a limited number of quality projects.

3. Oil & Gas and LNG

In contrast to thermal coal, despite commentary regarding oil & gas and LNG commodities as unacceptable carbon intensive industries, there were limited divestments by Japanese companies in 2020, as these commodities are regarded as essential to a balanced energy mix for Japan in the medium to long-term. In fact, with the significant reliance on Australian LNG as a source of Japanese energy (currently approximately 40% of total energy imports), investments in 2020 continued and include:

- **Mitsui & Co** developing the Waitsia Gas Project in Western Australia.
- **JERA** signing a letter of intent to acquire a 12.5% interest in the Barossa LNG Project from Santos to advance partner alignment with the Darwin LNG Project (Final Investment Decision for the project expected in mid-2021).
- **Mitsubishi Corporation** signing a 10-year contract to supply 1.5 million tonnes per year of LNG from the proposed Barossa Project.

One divestment (being the exception to the investment trend) has been the sale of **JERA's** 19.9% and **Marubeni's** 30.1% interest in the Australian-Japanese joint venture, Australian Industrial Energy (**AIE**), to Squadron Energy (a subsidiary of Fortescue Metals Group). AIE is the consortium behind the Port Kembla LNG import terminal.

4. Real Estate

Companies adapted to the changed working conditions, allowing a larger portion of the workforce to work remotely with video conferencing as a method to attend meetings. This led to many companies reconsidering their use of office space. However, with low interest rates remaining in place, investments are expected to continue into commercial real estate that offer high quality office design (such as reduced occupational density and improved technological capabilities) and office amenities (to accommodate the different commuting patterns of workers) which create a more attractive working environment.

In 2020, the two notable real estate transactions were:

- **Mitsubishi Estate** continuing its investment in Australia through the acquisition of a 25% interest in the One Sydney Harbour Residences One (OSH R1) project in Sydney from Lendlease.
- **NTT Urban Development** making its second major commercial investment through its acquisition of 200 Victoria Street from Australian Unity's diversified property fund. This follows its 2019 acquisition of a 50% interest in 121 Marcus Clarke Street in Canberra.

5. Financial Services

Australia remains a highly attractive market for financial services. It is the leading financial services exporter in the Asia Pacific, has a stable and favourable regulatory system, and has the world's fourth-largest pension (superannuation) market, valued at US\$2.1 trillion. Importantly for Japanese investors, it is also a fairly consolidated and mature market where businesses are looking to divest non-core businesses, particularly in the banking sector as a result of the Royal Commission into Misconduct in the Banking, Superannuation and Financial Services Industry.

Some of the higher value transactions in 2020 fell within this sector, and Japanese banks, general insurers and life insurers have been active bidders for traditional financial services businesses, as well as new Fintech businesses. Recent investments include:

- **Daido Life Insurance**, Leadenhall Capital Partners and Schroder Investment Management invested A\$43 million in Integrity Life. This follows Daido's A\$13 million initial investment into Integrity Life in 2018.
- **Nomura Research Institute** concluded an agreement to buy 100% of the shares of Australian Investment Exchange (AUSIEX) from Commonwealth Bank of Australia.

- **Nippon Life Insurance** and National Australian Bank jointly provided A\$650 million in additional equity to MLC Life.
- **Mitsubishi UFJ Lease & Finance** establishing a joint venture, “Vestone Capital”, with Macquarie Capital for the leasing of information technology and energy assets.
- **Kanamoto**, a construction equipment rental company, acquired Madica, Porter Group, and Porter Utilities.

It is expected that new investments in life insurance will slow, with the increased capital requirements and costs of regulatory compliance as a result of the Royal Commission making Australian insurance businesses less attractive, and Japanese companies already having a large market share.

There was one significant exit, with **Mitsubishi UFJ Trust and Banking Corporation (MUTB)** selling its 15% shareholding in AMP Capital to AMP Limited for A\$460 million. The exit comes after MUTB first acquired its shareholding in AMP Capital in 2012 for A\$425 million and allows MUTB to realign its focus on the recently acquired Colonial First State Global Asset Management.

6. Technology

Japanese companies are actively looking for investment opportunities in technology such as carbon capture and storage and other emissions reduction technologies, as well as other technologies such as software, data analytics, DX, Blockchain and advanced lightweight materials. Examples include:

- **Mitsubishi Corporation** and Santos signed a Memorandum of Understanding (**MOU**) to jointly investigate opportunities for carbon neutral LNG from Barossa. These include collaborating on opportunities relating to Santos’ Moomba carbon capture and storage project, pursuit of carbon neutral LNG, bilateral agreements for carbon credits and potential future development of zero emissions hydrogen.
- **Hitachi Zosen’s** Swiss-based subsidiary **Hitachi Zosen Inova AG** announced the delivery of its first energy-from-waste (EfW) plant near Perth, Western Australia, which commenced construction in January 2020 with full operation targeted at the end of 2022.
- **Yamaha Motor Ventures** completed a A\$11 million funding to Sydney-based agricultural tech firm The Yield, making it one of Australia’s best-funded agricultural technology start-ups. The funding will be used to further develop its Sensing+ product, which measures inputs such as barometric pressure, light, wind, salinity and

leaf moisture to help irrigate, feed, plant, protect and harvest.

- **CapDo**, a business improvement and cloud utilisation consulting service company, provided equity funding to Sazae, a software start-up based in Sydney.

Artificial intelligence (**AI**) is likely to attract greater interest as its business applications gain credibility and visibility. In June 2020, Australia and Japan joined 12 other countries and the European Union to form the Global Partnership on Artificial Intelligence. The forum is centred around common beliefs about how AI is to be used and developed, as well as expertise in the field, which suggests there may be Japan-Australia investment opportunities in the near future.

7. Residential Housing

We expect the vertical and horizontal integration of Japanese housing companies to continue, such as **Asahi Kasei Homes** acquiring the Supaloc steel framing business. As an extension of this trend, it is likely that the logistics and building product suppliers to housing companies in Japan will now enter the Australian market in earnest to continue to support their customers, as well as develop Australian customers. **Daiwa House**, **Sekisui House**, **Sumitomo Forestry** and **Misawa Homes** continue to be active in developing new projects and at least two other Japanese housing companies are exploring investment opportunities.

New sectors and forces driving change

To some extent the following sector and investment trends are not new, but they do represent an evolution or extension of the Japan-Australia investment relationship during 2020.

1. Hydrogen

In last year’s 3rd edition, we noted the momentum of hydrogen fuel was building, with **Kawasaki Heavy Industries** (along with other Japanese and international corporates) working with AGL on a pilot project in Latrobe Valley of Victoria to convert brown coal into hydrogen. The Japanese-Australian consortium is set to begin producing hydrogen from brown coal in a A\$500 million pilot project seen by its architects as the first step in creating one of the world’s first zero-emission energy supply chains, and eventually intends to capture the carbon generated by the process and inject it into under-sea basins in the nearby Bass Strait.

When Prime Ministers Suga and Morrison met in Tokyo in November 2020, hydrogen and the opportunities it presents for the bilateral relationship was a key topic of conversation. The Australian

Federal and State Governments and the Japanese Government (through New Energy and Industrial Technology Development Organisation (**NEDO**) and Japan Oil, Gas and Metals National Corporation (**JOGMEC**)) have all injected a large amount of funding to develop a hydrogen economy, and Japanese corporates continue to make strides to efficiently produce and transport hydrogen from Australia to Japan, helping Australia towards its goal of becoming a global leader in the supply chain of hydrogen energy.

Given this mutual support of commercial hydrogen initiatives, it was not surprising that a number of projects were announced including:

- **Mitsubishi Heavy Industries** investing in Hydrogen Utility (**H2U**) which has been developing green hydrogen and ammonia projects using renewable power sources in South Australia.
- **Kawasaki Heavy Industries** teaming up with Origin Energy on a 300-megawatt electrolyser in Townsville in far north Queensland.
- **Iwatani Corporation** forming a consortium with Queensland Government-owned Stanwell Corporation to progress planning on a new renewable hydrogen export facility in Gladstone, which will also enable the project to move towards a bankable feasibility study and front-end engineering design.
- **Sumitomo Corporation** entering into a front end engineering and design contract with **JGC Holdings** for a green hydrogen project in Gladstone, Australia, with a view on starting production in 2023.
- **IHI Corporation** entered into an MOU with the Queensland Government (via CS Energy) to undertake a feasibility assessment of a renewable hydrogen plant next to the CS Energy's coal-fired Kogan Creek Power Station.

2. Environmental, Social, and Corporate Governance (ESG)

Although the importance of ESG has been increasing year by year, 2020 saw ESG become a major investment consideration / hurdle driving decisions regarding the acquisition of new assets and the divestment of existing assets. Japanese listed-companies are particularly sensitive to reputational risk, and together with the increasing number of external directors this will undoubtedly influence investment decisions and drive sustainability objectives as a major requirement of companies' social licence to operate.

Prime Minister Suga's target of zero net emissions by 2050 will see Japanese corporate strategy and investment seek to align with that target, as shown by **JERA's** "JERA Zero Emission 2050". JERA's strategy in Australia is to establish itself as a long-term provider of Australian-sourced clean energy fuels. In Australia, pressure continues to grow on the Federal Government to declare emission targets for 2050 and the interim period.

Globally, voluntary financial reporting such as recommended by the Task Force on Climate-related Financial Disclosures (**TCFD**) are becoming increasingly commonplace, and many will evolve to become requirements for listed companies.

Most importantly, ESG-linked finance has emerged rapidly in Australia, and is set to grow despite the challenges of COVID-19. As of October 2020, Australia has seen 14 labelled green corporate loans and 7 sustainability-linked loans. There is also much sustainable investment appetite and government support. Japanese banks have played an active and leading role in the market to support ESG related activities, including:

- **MUFG**, assisted Sydney Airport with the world's first ESG-linked US Private Placement (the United States' private bond market).
- **SMBC**, arranged a cross-border syndicated green loan to Macquarie Group, the first green loan arranged for an Australian financial institution from the Japanese market (with three Japanese regional banks) based on the Green Loan Principles.
- **Mizuho, SMBC and MUFG** arranged debt financing for Murra Warra II Wind Farm, the first wind farm in Australia financed through a project finance green loan.
- **Mizuho and SMBC** participated in the refinancing of the Downer Group's debt platform establishing a new A\$1.4 billion Sustainability Linked Loan (**SLL**) facility, the largest SLL in Australia in 2020.

3. Post-Merger Integration (PMI) Governance

Japanese companies are becoming far more sophisticated in the management of the Australian companies in which they acquire either a 100% or majority ownership. This has been assisted by the lateral recruitment of executives with international experience, cultural understanding and good written and spoken English language skills.

Effective PMI governance is predictive of successful business outcomes, which will drive further investment. Good examples are **Nippon Paint** and **Kokusai Pulp & Paper** who have recruited

experienced and sophisticated international bankers in their M&A and PMI teams.

Japanese companies are also increasingly recruiting experienced Australian executives to the board of their Australian-owned subsidiaries. Examples include MLC Life (**Nippon Life**), TAL (**Dai-ichi Life**), Asahi Beverages (**ASAHI Group**), Lion (**Kirin**), McDonald Jones Homes (**Asahi Kasei Homes**) and Programmed Maintenance Services (**Persol**).

4. Economic Infrastructure

In Australia, the development of infrastructure is mainly a State Government responsibility supported by the Federal Government particularly in relation to priority investments from a national perspective. As a result of the economic impact of COVID-19, the Federal and State Governments have been working on initiatives to bring forward the timing of major infrastructure projects.

This will create new opportunities for Japanese companies and banks, who have gradually increased their familiarity with Australia's approach to delivering infrastructure, over the next few years. This is in addition to the existing opportunities with the Western Sydney Aerotropolis, Westmead Health and Innovation Precinct and the Sydney Innovation and Technology Precinct.

The New South Wales Government in particular is looking to help identify market opportunities for Japanese investors, and providing incentives such as Jobs Plus (payroll tax rebates for companies adding more than 30 full-time equivalent employees in the next 3 years) for eligible investors.

At the same time, the Japanese Government is strongly supporting an "Infrastructure Export" initiative to drive growth in the Asia-Pacific region in particular, given the decreasing domestic infrastructure opportunities.

Traditionally, Japanese companies found the Public Private Partnership (**PPP**) bidding process expensive, time-consuming and difficult to win due to the alliances between the established Australia construction companies and their European partners. This is starting to change, and **Mitsubishi UFJ Bank** is now one of Australia's four biggest project finance lenders.

Japanese companies are now also looking to bypass the PPP process by partnering in a consortium and submitting an "unsolicited proposal" to State Governments for unique solutions, which if accepted give an exclusive right to develop the Project. We expect there will be some exciting announcements during 2021 regarding successful proposals from consortia with Japanese participants.

LYRO Robotics, a robotics company received seed funding from **Toyo Kanetsu Corporate Venture Fund II** for the purposes of building AI-powered pick and pack robots for a large range of inventory stock in the agricultural sector.

5. Social Infrastructure

Japanese companies (particularly trading houses) have long-invested in Australian economic infrastructure – power, water/desalination, roads, rail and rolling stock. They are now looking to invest in social infrastructure such as hospitals and "Smart Cities" / "Internet of Things" where telecommunications, infrastructure and utilities converge, and data management is the key. **Hitachi Corporation, Urban Renaissance Agency, NTT Urban Development** and **Sojitz** have all been active in this sector recently.

Looking ahead, perhaps the two countries' shared interest in the construction and post-Olympic use of sporting infrastructure will provide a new source of Japanese expertise for Australia, given Brisbane's bid to host the 2032 Olympics.

6. Asset Management

In addition to asset recycling, the creation of an asset management business through the establishment of an investment fund (often seeded with existing assets) is also becoming popular with trading houses. Companies are seeking to attract external investors, such as Japanese pension funds, to inject cash into the investment funds instead of low-return Japanese Government bonds. This strategy both de-risks existing investments by selling an economic interest to the fund and recycles capital for new investments. For example:

- **Marubeni Corporation** established MM Capital Partners, which manages a global infrastructure fund and seeded the fund with existing Australian rail projects (Gold Coast Light Rail and Sydney Metro Northwest) and EII gas infrastructure assets. Subsequently, MM Capital Partners acquired a 9.5% interest in Royal Adelaide Hospital.
- **Mitsui & Co** and ENGIE have established an Australian Renewable Energy Trust which will invest in wind and large-scale solar Projects.

We expect the establishment of such funds to drive further M&A activity both in greenfield and brownfield projects as investors in the funds seek a diversified portfolio of assets. The funds provide an opportunity for Japanese pension and investment funds in particular, as well as corporate investors, to have exposure to the Australian market without having to directly invest in projects. We have seen, for instance, the Government Pension Investment Fund (**GPIF**) of Japan and New South Wales Government's TCorp acquiring a shareholding in Brussels Airport.

Moreover, funds are increasingly forming a core component in corporate "green" strategies. Forestry funds can provide carbon credits to investors and offtake of wood pellets for Japanese bio-mass power projects.

Asset management businesses also provide trading houses with an additional method for gaining exposure and knowledge of infrastructure and real estate. Trading houses are actively seeking to acquire an interest in existing asset management business given Australia's business reputation as having first class infrastructure and real estate fund managers.

Australian fund managers tend to allocate 30-40% to infrastructure. By contrast, Japanese pension/investments funds currently do not regard infrastructure as an "investment" class and so tend to limit exposure to 10-11% of funds. If the allocation increases in the future there could be significant more investment in Australia.

7. Japanese banks

Japanese banks all continue to support Australian projects. The Japanese banks have been active in project finance of key landmark projects, including:

- **Hills M2 motorway refinancing in Sydney:** Transurban's A\$815 million refinancing of the Hills M2 motorway project was supported by a lender syndicate of more than 20 financiers across Asia and Australia, including MUFG Bank (as lead arranger), Norinchukin Bank, Daido Life Insurance, Dai-ichi Life Insurance, Meiji Yasuda Life Insurance, Sumitomo Mitsui Trust Bank and Hyakugo Bank (regional bank based in Mie prefecture).
- **Canberra Light Rail Stage 1 refinancing:** the first operational infrastructure PPP project in Australia financed with a green loan was assisted by, among others, MUFG Bank (as green structuring adviser and financial adviser) and SMBC and Mizuho (as Mandated Lead Arrangers).
- **Ichthys LNG refinancing: INPEX** undertook a US\$8.3 billion refinancing of part of its debt during 2019-2020 which involved 28 commercial banks including **SMBC, MUFG** and **Mizuho** and a number of Japanese regional banks. **JBIC** continued as the major lender.

8. Healthcare

Japanese companies see healthcare as a very attractive market segment in which to invest in due to the steady cash-flow and lack of market volatility. The main opportunity to acquire assets is when private equity exits but the purchase price is usually high and there is a question over how to manage Australian healthcare professionals (e.g. specialist doctors).

Rather than direct investment we expect Japanese companies (most likely trading houses) will take strategic shareholdings in medical service providers to gain crucial operational management experience while, in parallel, looking for opportunities to supply high-end equipment.

9. Critical Minerals¹

Due to high importance of critical minerals to Japan's economy, the Japanese Government and Japanese companies have coordinated their approach to securing their supply. As Australia is a leading producer of many of these minerals, we expect that there will be investments, particularly battery materials which are essential to energy storage in the transition from fossil fuels to renewables.

For example, **JOGMEC** signed an MOU with the Government of Western Australia (**WA**) to promote stable supply of mineral resources to Japan and promote investment in WA from Japan and actively exchange information and views on metal mineral resources with WA in the future, particularly with the abundance of critical minerals and base metals found in WA.

Collaborations and Alliances – some observations on non-M&A trends

A number of non-M&A contractual arrangements between Japanese and Australian corporations were mentioned in last year's report, and this has developed into further collaborations and stronger alliances in the Japan-Australia corridor. As with our observations on M&A transactions in new sectors, while these commercial agreements are not new to 2020, they do represent an evolution or extension of the activities reported in previous years.

- The Joint Study Agreement between Transborder Energy and **Kyushu Electric Power** and **Mitsui OSK** in 2019 has led to a multi-party and multi-project Floating LNG Solution (**FLNG Solution**) Framework Agreement for co-pursuing the deployment of the FLNG Solution on a range of stranded offshore gas resource opportunities. Both **Kyushu Electric Power** and **Mitsui OSK** have the potential to become equity investors in the FLNG facility as well as potential offtakers from the project.
- **Eisai** and Cogstate's Business Alliance Agreement in 2019 has expanded such that Eisai's right to develop and commercialise the Cogstate Brief Battery (**CBB**) has expanded from Japan to globally. The CBB is envisioned as a tool for individuals to self-assess brain performance to support healthy lifestyle choices and preventative measures in daily life, as well as a medical device to aid healthcare professionals in clinical diagnosis decisions.

- **J-Power** has signed a development funding agreement with Genex Power to realise the Kidston Stage 3 Wind Project, reaffirming its \$25 million equity commitment to the project.

Despite the disruptions in 2020, new alliances and further strengthening of partnerships were formed:

- **NEC** signed a MOU with the NSW Government to be a founding partner in the development of the Sydney Innovation and Technology Precinct, a place where start-ups, world-class universities, leading research institutions, high-tech giants and the community collaborate. NEC is the second tech giant after Atlassian to set up its office at the Innovation Hub.
- **Hitachi Corporation** established a strategic partnership with BizCubed to deliver initiatives that co-create socially innovative digital solutions for the Smart Agriculture and Smart Cities initiatives. This partnership further affirms Hitachi's commitment to developing world-class digital solution capability in Australia, following the 2019 announcement to establish the "Kyōsō Centre (collaborative creation centre)" within the Western Sydney Aerotropolis.
- **Hitachi Construction Machinery** formed a partnership with Whitehaven Coal for the implementation of an autonomous truck haul system at the Maules Creek coal mine.
- **Kyocera Corporation** entered into a non-binding MOU with ASX-listed Regenus in March 2020, for the exclusive negotiation rights to Progenza for the treatment of knee osteoarthritis in Japan. The companies entered into a licence and collaboration agreement in August 2020.
- **Japan Aerospace Exploration Agency (JAXA)** and the Australian Space Agency entered into a Memorandum of Cooperation in July 2020, strengthening Australia's long-standing space cooperation with Japan with the aim to increase space collaboration.

¹ Critical minerals include: rare-earth elements (REE), gallium (Ga), indium (In), tungsten (W), platinum-group elements (PGE) including platinum (Pt) and palladium (Pd), cobalt (Co), niobium (Nb), magnesium (Mg), molybdenum (Mo), antimony (Sb), lithium (Li), vanadium (V), nickel (Ni), tantalum (Ta), tellurium (Te), chromium (Cr) and manganese (Mn).

Herbert Smith Freehills

Herbert Smith Freehills is a leading global law firm bringing together the best people across our 26 offices in Japan, Australia and worldwide, to meet clients' legal services needs globally. We are the largest law firm in Australia and are consistently ranked No.1 in M&A, both in number of deals advised and value of deals.

Our Australia Japan Practice is a unique team of experienced bilingual and bicultural lawyers, specialising in advising Japanese businesses on their investments and operations in Australia. Herbert Smith Freehills' team has more experience advising Japanese businesses on Australian investments than any other law firm.

Herbert Smith Freehills was involved in 11 of the 28 transactions surveyed for this report (including 3 confidential deals that were not specifically mentioned in the report), more than any other disclosed legal adviser.



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Experience

Ian is a highly experienced M&A and joint venture specialist. He also holds a position as a director or adviser for a number of Japanese and Australian companies. Ian was awarded the Japanese Foreign Minister's Commendation in October 2016 for his service to the Japan Australia relationship in business and sport.

Japanese Language Proficiency

Ian holds Japanese Language Proficiency Test N2 certification.



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Experience

Melissa has a particular focus on advising Japanese investors on farm-ins, joint ventures and other equity investments in the energy and resources and infrastructure sectors.

Melissa has worked with a number of Japanese corporations during her career and she currently advises Japanese trading houses, power utilities and mining companies on their investments in Australia.



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Experience

Tatsuki is an Australian-born and educated solicitor who has worked on cross-border transactions and mergers and acquisitions both for private and public companies. He has experience assisting Japanese trading houses, TSE-listed companies and has advised Australian companies negotiating with Japanese counterparties.

Japanese Language Proficiency

Tatsuki is fluent in Japanese.



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Experience

Damien is a leading Japan-based expert for Australian Corporate / M&A work, particularly in the infrastructure, resources and consumer sectors. He is a Registered Foreign Attorney and has been based in Tokyo since 2011.

Japanese Language Proficiency

Damien holds Japanese Language Proficiency Test N1 certification and is a NAATI-accredited interpreter.



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Experience

Hiroko is a finance lawyer who was previously a member of the Tokyo office of HSF. She has been working closely with Japanese corporations, including trading houses conducting business in Australia. Hiroko was born in Japan and completed her law degrees in Japan and Sydney.

Japanese Language Proficiency

Hiroko is a native Japanese speaker, and is also proficient in English, French and Russian.



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Experience

Edward is a solicitor in the Employment, Industrial Relations and Safety team. As a member of the Australia-Japan Practice, he has worked on various Japanese client matters since joining HSF in 2016. He also has experience working briefly in the firm's Tokyo office.

Japanese Language Proficiency

Edward is fluent in Japanese.

Details of transactions surveyed

No	Buyer	Target/Seller	Description of Transaction	Deal Value (A\$ millions)	Industry	Date Announced / Completed
1.	Toyo Kanetsu Corporate Venture Fund II	LYRO Robotics Pty Ltd	Toyo Kanetsu Corporate Venture Fund II provided seed funding to LYRO Robotics.	Undisclosed	Technology	Announced 14/02/2020
2.	New Forests Pty Limited	Mitsui & Co., Ltd.	Mitsui Bussan Woodshop Oceania sold assets of Bunbury Fibre Plantations to New Forests.	Undisclosed	Agriculture	Announced 2/03/2020 Completed 2/03/2020
3.	Futura Resources	Sojitz	Sojitz agreed to proceed with the Wilton coking coal mine with Futura Resources.	Undisclosed	Energy & Resources	Announced 31/03/2020
4.	Asahi Kasei Homes	Weeks Building Group	Asahi Kasei Homes Corporation acquired the Weeks Building Group, including Supaloc (the steel frame business) through McDonald Jones Homes.	30.27	Property & Construction	Announced 12/03/2020 Completed 30/04/2020
5.	ASG Group Ltd	Group 10 Consulting Pty Ltd	ASG Group Ltd (wholly owned subsidiary of Nomura Research Institute Ltd) acquired Group 10 Consulting.	Undisclosed	Services	Announced 17/03/2020 Completed 17/03.2020
6.	Yancoal Australia Limited	Sojitz Corporation	Sojitz sold its 10% interest in the Moolarben coal mine to Yancoal.	300	Energy & Resources	Announced 27/03/2020 Completed 31/03/2020
7.	Nomura Research Institute	Commonwealth Bank of Australia	Nomura Research Institute acquire Australian Investment Exchange Limited (AUSIEX).	85	Financial Services	Announced 28/04/2020
8.	NTT Urban Development Corporation	200 Victoria Street	NTT Urban Development acquired 200 Victoria Street from Australian Unity's diversified property fund.	72	Property & Construction	Announced 30/04/2020 Completed 3/05/2020
9.	Yamaha Motor Ventures	The Yield	Yamaha Motor Ventures completed an equity investment into agricultural tech firm The Yield.	11	Technology	Announced 11/05/2020 Completed 11/05/2020

No	Buyer	Target/Seller	Description of Transaction	Deal Value (A\$ millions)	Industry	Date Announced / Completed
10.	Mitsui Matsushima	Square Resources Pty Limited	Mitsui Matsushima Holdings acquired a 17% shareholding in Square Resources.	Undisclosed	Energy & Resources	Announced 29/05/2020
11.	Nippon Life Insurance	MLC Limited	Nippon Life Insurance acquired additional equity in MLC.	650	Financial Services	Announced 3/06/2020
12.	Kyoshin	NichiiGakkan	Kyoshin acquired SELC Australia from NichiiGakkan.	0.13	Services	Announced 17/07/2020 Completed 12/10/2020
13.	Bridgestone	Transense Technologies plc	Bridgestone acquired a number of Transense subsidiaries and certain other assets and liabilities from Transense Technologies plc.	Undisclosed	Services	Announced 25/06/2020
14.	Mitsubishi Estate	Lendlease	Mitsubishi Estate acquired a 25% interest in first residential tower at One Sydney Harbour from Lendlease Group.	Undisclosed	Property & Construction	Announced 1/07/2020
15.	CapDo Co., Ltd.	Sazae Pty Ltd	CapDo acquired an equity interest in Sazae Pty Ltd.	Undisclosed	Technology	Announced 28/07/2020
16.	AMP Limited	Mitsubishi UFJ Trust and Banking Corporation	Mitsubishi UFJ Trust and Banking Corporation sold its 15% interest in AMP Capital Investors Limited to AMP.	460	Financial Services	Announced 13/08/2020
17.	Kanamoto Australia	Madica Pty Ltd, Porter Group Nominees Pty Ltd, and Porter Utilities Holdings Pty Ltd	Kanamoto acquired Madica Pty Ltd, Porter Group Nominees Pty Ltd, and Porter Utilities Holdings Pty Ltd from asset management company T&B Porter Group Investment Pty.	74	Property & Construction	Announced 4/09/2020
18.	Daido Life Insurance Company	Integrity Life Australia Limited	Daido Life , along with other investors, acquired an interest in Integrity Life Australia Limited, an Australia-based life insurance company.	43	Financial Services	Announced 1/10/2020 Completed 1/10/2020

No	Buyer	Target/Seller	Description of Transaction	Deal Value (A\$ millions)	Industry	Date Announced / Completed
19.	Mitsui & Co	Australian Renewable Energy Trust	Mitsui and ENGIE formed a joint venture to establish an Australian Renewable Energy Trust.	Undisclosed	Asset Management	Announced 13.10.2020
20.	MM Capital Partners	Royal Adelaide Hospital	MM Capital Partners an infrastructure fund managed by Marubeni , acquired a 9.95% interest in the Royal Adelaide Hospital from Pacific Partnerships Investments.	Undisclosed	Asset Management	Announced 19/10/2020 Completed 19/10/2020
21.	Squadron Energy	Marubeni & JERA	JERA and Marubeni sold 19.9% and 30.1% interest respectively in Australian-Japanese joint venture Australian Industrial Energy (AIE) to Squadron Energy (a subsidiary of Fortescue Metals Group).	Undisclosed	Energy & Resources	Announced 20/10/2020 Completed 20/10/2020
22.	Spicers Limited	Rojo Pacific Pty Ltd	Kokusai Pulp & Paper (through its subsidiary Spicers) acquired Rojo Pacific Pty Ltd.	Undisclosed	Manufacturing & Industrials	Announced 30/10/2020 Completed 30/10/2020
23.	Bega Cheese	Lion Dairy & Drinks	Kirin sold its Lion Dairy & Drinks business to Bega Cheese.	534	Consumer	Announced 26/11/2020
24.	Roc Partners	Sumitomo Australia	Sumitomo Australia sold its interest in Emerald Grain Pty Ltd to Roc Partners.	Undisclosed	Agriculture	Announced 27/11/2020 Completed 27/11/2020
25.	Rakuten	Pop Tech Pty Ltd	Rakuten acquired 100% interest in Pop Tech Pty Ltd.	Undisclosed	Software	Announced 3/12/2020

In addition, there were 3 confidential transactions which were not publicly announced.