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Alpine/Alps: ISS refers to Clarion deal process in its backing of Oasis' views

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- Exploration of strategic alternatives lacking, proxy adviser says
- ISS supports exchange ratio of 0.87, in line with Zecco's 0.86
- Alpine/Alps – a key corporate governance test, former FSA commissioner says

Institutional Shareholders Services (ISS) highlighted the benefits obtained from the process leading up to the recently agreed sale of a majority stake in **Clarion** [TYO:6796] as it recommended shareholders of **Alpine Electronics** [TYO:6816] reject the "low valuation" takeover proposal from **Alps Electric** [TYO:6770], the report issued by the proxy adviser shows.

Valuing Alpine versus a comparable peer like car navigation company Clarion highlights that the Alps' deal "significantly undervalues Alpine", ISS said. "Clarion also sets the ultimate valuation and sale process benchmarks, having agreed to a takeover in cash at 11x EBITDA after getting a bid from a third party," it added.

"The offer for Clarion demonstrates the advantage of running a comprehensive sale process and having a cleaner capital structure. Clarion's takeover multiple implies a value of more than JPY 4,000 for Alpine, well above Alps' current offer of approximately JPY 1,800," ISS said in its report.

In the case of Alpine, "there is no evidence that a full exploration of strategic alternatives was undertaken, nor that market-based evidence of price fairness was actively sought," ISS continued. Furthermore, it noted that "the transaction's strategic rationale does not lead to the conclusion this is a must-do deal that should be pursued at such a low valuation".

The fact that ISS recommended shareholders to vote against the proposed takeover of Alpine at the upcoming EGM was first reported by this news service on 19 November.

ISS' comments were overtly supportive of Oasis Management, the Hong Kong-based activist that is engaged in a battle to reject the proposed takeover of Alpine. Oasis has also referred to the sale of Japanese car navigation company Clarion as a clear indication that Alps' offer price undervalues Alpine, as previously reported.

French automotive parts manufacturer **Faurecia** [EPA:EO] announced on 26 October that it will launch a tender offer for 100% of Alpine's competitor Clarion at a valuation of 11.2x EV/EBITDA. **Hitachi, Ltd** [TYO:6501] has agreed to tender its entire 63.8% stake as part of the offer, as reported.

Using the same valuation multiple would imply a valuation of JPY 4,731 per share for Alpine, or more than 2.5x the amount Alps is offering, according to Oasis.

Alps, an electronic component manufacturer that holds 40.43% of Alpine, said on 27 July 2017 it would acquire the remaining publicly held shares of the automotive components manufacturing subsidiary effective 1 January 2019. The acquisition will be carried out via a share swap with Alpine shareholders receiving 0.68 Alps share for each Alpine share they own.

Oasis, which holds a 9.9% stake in Alpine, has been stepping up pressure on shareholders, urging them to vote against the transaction at the company's EGM on 5 December.

The activist reckons that Alps and Alpine should look for a third-party buyer because there will be multiple third parties who will pay a premium over Alpine's share price, as opposed to the discount that Alps is offering.

Initial "fairness" opinion undercut by Yamada

The proxy adviser said, based on standalone values, without including a takeover premium for Alpine, the exchange ratio between the two companies would be approximately 0.87, much higher than the proposed ratio of 0.68.

ISS's valuation is in line with the valuation analysis conducted by Zecoo Partners, retained by Oasis Management as its advisor to evaluate this transaction.

Based on the numbers presented in Alpine's press release on 27 July 2017 when the deal was announced, Zecco Partners said in its report published in October 2018 that the exchange ratio would jump to 0.86 from 0.68, if SMBC Nikko's assumption of a 0% perpetual growth rate is adjusted upward, and if Alpine's steep upwared revision to its earnings forecast in February 2018 and JPY 30bn of non-operating assets are factored in.

At Oasis' Investors' Day on 7 November, Somitsu Takehara, chairman of Zecco Partners and a certified public accountant, questioned why SMBC Nikko concluded that the exchange ratio would remain unchanged at 0.68 after the upward revision of the company's earnings forecast "even though there was a huge gap in profit-growth rate?"

Takehara also questioned why SMBC Nikko did not add JPY 30bn of operating cash to the share value when it made its DCF analysis, thereby reducing the appraised value of Alpine.

In addition, Takehara argued that shareholders should be paid a so-called control premium even under a share swap. "Under any legal M&A structures, shareholders must be paid a control premium," said Takehara at the meeting.

On the same investor day, Seth Fischer, Oasis' chief investment officer, noted that Yamada Consulting Group, which was appointed by Alpine's third-party committee, has come up with a new "fairness opinion" that is even lower than SMBC's original opinion.

Yamada used a significantly lower discount ratio in valuing Alps than the discount rate for Alpine. This massively inflates Alps' valuation and lowers the share exchange ratio in Alps' favor, Fischer added.

Proxy adviser in favour of special dividend

As reported, ISS also endorsed Oasis' proposal that Alpine pay a cash dividend of JPY 300 per share, subject to the merger agreement being rejected by shareholders.

"A balance sheet analysis reveals that the company still has sufficient cash and equivalents, enabling it to pay dividends in the way requested by the dissident," the report said.

If the shareholder proposal is carried out, a total outlay of JPY 20.7bn (USD 183.9m) will be required. "Given the firm's position in cash and long-term securities, the additional payment should be feasible without causing disruption to the company's day-to-day operations," the proxy adviser added.

To date, there has been only one merger that was vetoed by shareholders in Japan. In February 2007, shareholders of **Tokyo Kotetsu** led by Ichigo Asset Management blocked a takeover by rival steel producer **Osaka Steel** [TYO: 5449] in a proxy fight.

"I think this [Alpine/Alps] case is the most important transaction to test Japan's corporate governance. Oasis's argument and analysis are extremely convincing," Masaharu Hino, a former commissioner of the Financial Services Agency (FSA) and a special adviser to Oasis, said in his opening speech at the Oasis Investors' Day.

Alpine could not be reached for comment as its switchboard was turned off after office hours.

by Norie Hata in Tokyo

Grade: Strong evidence

Value (GBP m): 865.7637

market cap of Alpine

TARGETS

Alpine Electronics, Inc.

Financial advisor
Sumitomo Mitsui Financial Group, Inc.

Lawyer
TMI Associates

BIDDERS

Alps Electric Co., Ltd.

Lawyer
Mori Hamada & Matsumoto

VENDORS

Elliott Management Corporation

Oasis Management (Hong Kong) LLC.

Japan

Industrial: Electronics

Topics: Shareholder Activism, Mergers and Acquisitions

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