CASE SECTION

Boardroom Battle at Otsuka Kagu: The Shareholder's Dilemma

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Abstract

Japan's oldest furniture retail chain, Otsuka Kagu Ltd. witnessed significant turmoil in 2015 with the company's founder and Chairman Katsuhisa Otsuka (Katsuhisa) and his daughter and President of the company, Kumiko Otsuka (Kumiko), fighting for boardroom control. Both of them differed over the strategy of the company with Katsuhisa favouring the business model developed by him, catering to the affluent customer base in Japan. But Kumiko contended that the business model was not in tune with the times and was leading to losses for the company. She pushed for the discontinuation of the old membership-based business model and opened small and cheaper outlets to boost the sales. The fight for boardroom control between the father and the daughter had spilt over to the public domain, with both blaming the other for the company's misfortune. In a shareholder meeting, both of them prepared contrasting strategies for the company and presented them before the shareholders. The shareholders now had the onerous task of deciding who should be given control of the troubled company. The case provides an ideal opportunity to the participants for evaluating the two strategic approaches threadbare with the Suitability, Acceptability and Feasibility criteria or using criteria like internal consistency, external consistency and dynamic consistency, as part of a Strategic Management curriculum.

Introduction

"Old man, your daughter is pretty smart. I think she really cares about the company... I would put an ad in the paper, with the two of you shaking hands and saying you're sorry, and promise to sell furniture for the best price," [12] said a frustrated shareholder of Otsuka Kagu Ltd., to Katsuhisa Otsuka (Katsuhisa), Founder and Chairman of Japan's oldest furniture retail chain. It was March 27, 2015, and around 200 disappointed shareholders were in the assembly hall. The meeting witnessed a face-off between Katsuhisa (71) and his daughter and President of the company, Kumiko Otsuka (Kumiko, 47), as they differed over the strategic direction that the company should take. The shareholders assembled at the meeting to decide who should be given the control of the troubled company.

Otsuka Kagu and the Japanese Furniture Market

Otsuka Kagu was founded by Katsuhisain 1969 in Tokyo and since then it had established itself in the market for luxury furniture. Otsuka Kagu operated large-scale retail stores primarily in urban areas through a unique 'membership system' introduced by Katsuhisa in 1993. In that system, when the customer entered the showroom, they were required to fill an information form and sign a membership form at the desk. Then, an attendant who had rich product knowledge, was assigned to each group of the customers to escort them throughout the showroom. The attendant while communicating with the customer determined their needs, introduced the items, and provided advice regarding the purchase of furniture. All the products at the stores were labelled with two prices, member's price and non-member's price - the member's price was guaranteed to be the lowest and competitive price in Japan. The membership card was valid for lifetime and customers could avail heavy discount only if they purchased through card. The rationale behind the membership system was that people bought furniture once in a lifetime. In Japan, when two people get married, the family of bride buys all the furniture. Otsuka Kagu's business model helped the couples to manage their purchase. Due to the membership system approach the company witnessed rapid growth in 1990s. Katsuhisa, firmly believed, that without the membership system the company would be just another store which would not appeal to the affluent consumers.

But as soon as recession hit Japan, the disposable income of youth became unstable; they started looking for other cheaper options. As a result, Otsuka Kagu's business was affected ***(See Exhibit 1 Key Financials of Otsuka Kagu and Exhibit 2 for the Key Statistics Related to its Stores)***. The interior retail market in Japan

[12] "Daughter Bests Father in Feud at Japan Shareholder's Meeting," www.reuters.com, March 27, 2015.

dropped to ¥3 trillion in 2011 from ¥4.5 trillion in 2001.[13] In 1973, the figure of new housing starts was 1.94 million units which declined steeply but was above 1.0 million units in the 1990s. But in 2009, because of the change in the Japan's population structure and global recession the new housing starts figure fell below 1.0 million units.[14] Traditionally, during a marriage, bride's family purchased three-piece furniture set which consists of a wardrobe, a Japanese-style chest of drawers and a dressing table. Due to the shortage of housing space for newlyweds, the demand for the furniture decreased. Simultaneously, the apartment houses started to be developed with closets that could be used for storage purposes. There was also a continuous decline in the marriages in Japan from 798,000 in 2000 to 668,000 in 2012.[15]

Moreover, the customers' needs were catered by other furniture retail chains which were in their growth phase like IKEA, Nitori Holdings Ltd, and Mujirushi Ryohin (Muji)***(See Exhibit 3 for Otsuga Vs. Key Rivals in the Japanese Market)***. These stores offered all the products made specifically according to the modern integrated in-house style. IKEA re-entered Japan's furniture market in 2002 and opened its first showroom in 2006. It targeted the young customers with less disposable income and increased desire of self-expressions. By 2015, it had eight stores in Japan and by 2020 it planned to open six more stores in the country. According to Minoru Fuduka of Roland Berger Strategy Consultant, consumers now preferred to buy the simple furniture which was appropriate for their lifestyle. Fuduka added, *"When you look at IKEA, they don't just display their products, they show IKEA's uniqueness through the displays, so it interests consumers."*[16] Nitori established its furniture store in 1967 and by 1972 it founded two Nitori wholesale furniture stores. As of 2014, it operated 313 stores in Japan. In comparison to 2009, Nitori generated an increase of 17.3% sales and 39.6% income in 2010, with ¥ 286 billion and ¥47 billion respectively.[17] Muji was founded in Japan in 1980. It believed in 'no brand' strategy.[18] It believed in the simple shopping experience and 'anti brand movement' therefore spent a little amount on the advertising and totally relied on the word-of-mouth.

[13] Philip Brasor and Masako Tsubuku, "Outdated Otsuka Kagu Business Model is at the Root of Family Feud," www.japantimes.co.jp, April 11, 2015

[14] www.asean.or.jp/ja/trade/lookfor/top/market/pdf/Japans%20Market%20for%20Interior%20Furnishing%20Products.pdf/at_download/file (Accessed on December 2016)

[15] "Handbook of Health and Welfare Statistics 2013," www.mhlw.go.jp.

[16] Kazuaki Nagata, "Otsuka Kagu Familial Feud Nears Climax," www.japantimes.co.jp, March 25, 2015.

[17] http://www.nitori-intl.com.

[18] http://www.muji.eu.

Trouble at Otsuka Kagu

Katsuhisahad handed over the position of President to his daughter Kumiko in 2009, while he remained the Chairman of Otsuka Kagu. By 2011, Kumiko renovated the stores and cut the prices of the products. She moved the reception desk to the back and launched a line of stores offering lower-priced products.[19] She implemented strategies to deal with competition aroused by IKEA, Nitori and Muji. She then simplified the expensive policy of the company of appointing sales staff for every customer and dropped the mailed advertising. For cheaper offerings, she opened small shops which specialised in Scandinavian furniture. Some industry observers credited Kumiko with restoring the image and profit of the company by shifting from the high-end business strategy of her father. To compete with its rivals, she emphasized on the need to broaden the customer base, selecting more middle class customers. She further believed that the business strategy 'membership sales model', which her father introduced, was no longer applicable in the changed economic environment. She wanted Otsuka Kagu to be more store like experience rather a more casual business style. She stressed to make Otsuka showrooms handy to the general public without memberships and until and unless customer asks for a staff for help, no staff would be trailing them.[20]

But as she launched the new business model, in July 2014, Katsuhisa dismissed her from the post and appointed himself as Chairman and President of the company as he felt that Otsuka Kagu was struggling under Kumiko. He reintroduced his business model, brought back the membership forms, and reinstalled the big service counters at the stores and closed the low-priced stores. According to Kumiko, her father was also not comfortable with her push for adding independent directors to the Otsuka Kagu board. *"We often had a clash of opinions and I saw that clearly in early 2013 when we were welcoming three directors from outside,"*[21] she recalled.

Katsuhisa insisted that Otsuka Kagu returned its focus to the high-end customer service and membership structure. He considered the discounted prices as the mistake by his daughter.[22] Katsuhisa said, *"Employees*

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[19] http://www.wsj.com/articles/family-feud-splits-japanese-furniture-chain-otsu-ka-kagu-1426715809

[20] Philip Brasor and Masako Tsubuku, "Outdated Otsuka Kagu Business Model is at the Root of Family Feud," www.japantimes.co.jp, April 11, 2015

21 Atsuko Fukase, "Kumiko Otsuka Says Corporate Governance at Heart of Dispute With father," http://blogs.wsj.com/japanrealtime, March 19, 2015.

22 http://www.wsj.com/articles/family-feud-splits-japanese-furniture-chain-otsu-ka-kagu-1426715809

came to me. They think that only I can revive the company."[23] Bearing in mind his old business model, he said, *"It's extremely important that our employees with deep knowledge of such products and customers' purchase history offer proper consulting to our customers."*[24] He contended that the business strategy of IKEA or Nitori was different from the business they were doing and therefore to follow them would be a mistake

In December 2014, Otsuka Kagu witnessed the loss for the first time in four years. Sales declined from ¥56.23 billion in 2013 to ¥55.50 billion in 2014.[25] Looking at the sales figures, in a meeting of Board of Directors in January 2015, the majority of the members decided to re-appoint Kumiko as the President of the company.

What Next?

The fight for boardroom control transformed into a public spat between the father and the daughter as they blamed each other for the company's problems. In March 2015, the sales of Otsuka Kagu dropped by 37.8% compared to the March 2014.[26] Otsuka Kagu's shareholders believed that people would be less inclined to buy furniture, which is usually associated with a happy occasion, from a company a father and daughter were fighting over. They expressed anger and dismay over the situation and suggested that the father and daughter work together. In the general shareholders meeting, both Kumiko and Katsuhisapresented their contrasting proposals to the 200 shareholders, as all efforts at reconciliation went in vain ***(See Exhibit 4 for the Strategy and Forecast by Katsuhisa and Kumiko)***. The dilemma before the shareholders was who should be given the reigns of the company.

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23 Kazuaki Nagata, "Otsuka Kagu President Prevails in Bitter Family Feud," www.japantimes.co.jp, March 27, 2015.

24 http://www.wsj.com/articles/family-feud-splits-japanese-furniture-chain-otsuka-kagu-1426715809

25 http://www.corporateinformation.com.

26 Philip Brasor and Masako Tsubuku, "Outdated Otsuka Kagu Business Model is at the Root of Family Feud," www.japantimes.co.jp, April 11, 2015

Exhibit 1

Key Financials of Otsuka Kagu Ltd. (2005-2014)

(In ¥ Million)	2005	2010	2011	2012	2013	2014
Net sales	69,649	56,912	54,366	54,520	56,230	55,501
Gross profit	38,591	31,064	30,551	30,848	31,069	30,598
SG&A expenses	33,240	31,197	29,401	29,664	30,226	31,000
Transportation	1,648	1,636	1,537	1,478	1,521	1,550
Advertising	5,649	3,524	3,036	3,138	3,417	3,860
Personnel	9,551	10,243	10,150	10,402	10,686	11,009
Rents	11,997	11,743	10,735	10,492	10,175	10,161
Operating income	5,350	132	1,150	1,183	843	402
Net income	3,649	255	203	640	856	473
Current assets	29,403	23,867	25,393	25,334	26,595	30,312
Fixed assets	29,079	18,846	16,358	16,390	21,062	16,398
Total assets	58,483	42,714	41,751	41,725	47,657	46,710
Current liabilities	11,399	7,982	8,069	7,849	8,433	9,518
Long-term liabilities	3,960	711	1,015	1,076	2,973	2,527
Net assets	43,123	34,019	32,666	32,799	36,250	34,665
Total number of shares issued and outstanding [1,000 shares]	21,600	19,400	19,400	19,400	19,400	19,400

Adapted from Trends in Business performance,
http://www.idc-otsuka.jp/company/e-ir/e-zaimu.html.

Exhibit 2

Key Statistics Related to the Otsuka Kagu Stores (2005 – 2014)

	2005	2010	2011	2012	2013	2014
Number of employees	1,611	1,678	1,673	1,673	1,749	1,749
Floor Space [m^2]	2,07,060	1,77,590	1,56,796	1,53,751	1,53,751	1,54,055
Number of Showrooms	16	17	16	15	15	16

Adapted from Trends in Business performance,
http://www.idc-otsuka.jp/company/e-ir/e-zaimu.html.

Exhibit 3

Otsuga Vs. Key Rivals in the Japanese Market (FY 2011)

Name	Sales (In ¥ Million)
Nitori	331,016
Nafuko	220,247
Shimachu	158,982
IKEA	67,500
Otsuka Kagu	54,376

Adapted from Global Strategies in Retailing: Asian and European Experiences, 2014

Exhibit 4

The Strategy and Forecast by Katsuhisa and Kumiko

	Katsuhisa	Kumiko
Sales (¥ million)	66,000	59,400
Operating profit (¥million)	2,640	1,900
Strategy	* High value added marketing with premium products * Promoting consulting service while shopping * Having a wide variety of furniture at large stores * More advertising	* Marketing more mid-priced products * Strengthening B-to-B * Large stores and shops designed to sell specific categories of furniture * Making stores more inviting for customers

**The forecast was for 2017*

Adapted from Kazuaki Nagata, "Otsuka Kagu President Prevails in Bitter Family Feud," http://www.japantimes.co.jp, March 27, 2015