

## Feature Articles

### This month's focus: The Art of Portfolio Strategy: Balancing Diversification and Focus

#### Value Added by Top Management: Functions of Executives in a Diversified Corporation

*Tsuyoshi Numagami*

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Much has been discussed about the role of top management from the perspective of the capital market. However, it is unclear from the viewpoint of executives at diversified corporation how they can claim their unique value added. In today's well-developed capital markets, this paper argues that managers can demonstrate their value by either (1) establishing a strategic control method when the Strategy map and KPIs are not fixed or (2) identifying and developing an underlying structure for the company's business portfolio.

#### Conglomerate discounts in Japan: An analysis of a 25-year period

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Firms diversified across industries tend to be discounted by investors vis-à-vis focused firms operating in the same industry. This article investigates this phenomenon based on a long-term panel of Japanese firms listed from 2000 to 2024. The discount for diversified firms averaged over this 25-year period is approximately 10%. However, the size of the discount varies substantially over time depending on capital market conditions. We also document that the discount is significantly larger for non-manufacturing firms than for manufacturing firms.

#### Capital Allocation and Corporate Value

*Makoto Nakano / Yuriko Takahashi*

In this paper, we conducted a quantitative analysis of the impact of capital allocation on corporate value (PBR) of industrially diversified firms from the perspective of redeployment flexibility, using business segment accounting information. We find that PBR is at a high level when both inter-segment resource allocation flexibility and intra-segment resource allocation flexibility can be balanced. Maintaining a high level of both flexibilities in good balance is likely to lead to a higher evaluation from the capital market. Furthermore, since the value of the redeployment option held by diversified corporation increases when uncertainty is high, the above value creation effect is more pronounced in corporation with high business risk.

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### Strategic Business Portfolio Management and the Value of Focus

*Toshio Tamura*

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A central challenge facing Japanese companies in the formulation of business portfolio strategy is the establishment of a coherent and consistent policy on business separation. Two important concepts in considering business separation are the “best-owner principle” and the “value of focus.” The latter, in particular, is closely tied to the question of why spin-offs—prevalent among Western firms—create value. This paper explores the value of focus through the lens of the theory of the firm, originating with Coase, with specific emphasis on intra-firm transaction costs, especially organizational management costs.

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## Articles

### The Usefulness of Machine Learning for Predicting the Sign of Earnings Changes: Evidence from Japan

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This study examines the usefulness of machine learning for predicting the sign of earnings changes using Japanese listed companies. We employ random forest models to predict earnings direction and compare their performance with management earnings forecasts. Our analysis covers 44,309 firm-year observations from 2002 to 2021, with prediction tests conducted from 2007 to 2021. Results show that machine learning predictions achieve accuracy comparable to or superior to management forecasts, particularly when focusing on high-confidence predictions. Hedge portfolios based on machine learning predictions generate statistically significant abnormal returns, achieving 9.15% annual returns compared to 3.87% for management forecasts. Variable importance analysis reveals that management forecast information plays the central role in machine learning predictions, while traditional financial statement information serves a complementary function. These findings suggest that machine learning can serve as a valuable tool for investment decision-making in Japanese markets.

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