Sanyo's accounting woes big blow to shareholders

By Jay Alabaster and Hiroyuki Kachi
Last Update: 9:28 PM ET Feb 25, 2007

TOKYO (MarketWatch) -- Sanyo Electric Co.'s (6764.TO) admission Friday that authorities are investigating its accounting practices sent its share price down by almost a third and could be a major blow for Goldman Sachs Group Inc. (GS) and other large investors in the company.

The Osaka-based electronics firm said it has been approached by the Securities and Exchange Surveillance Commission about its past accounting. The timing couldn't be worse for investors like Goldman, which has invested more than $1 billion in the company and was close to being able to make a massive profit on the deal.

"We are fully cooperating with an inquiry" by the SESC and provided documents and explanation, said Sanyo, without elaborating.

A spokesman at the SESC declined to comment, adding the securities watchdog won't comment on individual matters. A Goldman spokeswoman said the U.S. securities firm is committed to supporting Sanyo "for the long-term."

The Asahi Shimbun reported in its Friday morning edition that Sanyo was suspected of misrepresenting losses in its results for the fiscal year ended March 2004. The company had considered processing some Y190 billion in losses, mainly from struggling subsidiaries, but in the end only wrote off Y50 billion worth of losses during that period, the report said.

If Sanyo had booked a more appropriate amount of losses, the company would likely have fallen into the red for that business year, the paper said.

Goldman paid about $1.1 billion for preferred shares in Sanyo that can be converted into about a quarter of Sanyo's common stock, the biggest investment in Japan for Goldman since it spent $1.3 billion for a chunk of Sumitomo Mitsui Financial Group Inc. in 2003.

Shares of the embattled electronics firm ended Friday trading down 21% at Y181 on the Tokyo Stock Exchange, after hitting an intraday low of Y163, down 29%.

Goldman and partner investors Daiwa Securities Group Inc. (8601.TO) and Sumitomo Mitsui Financial Group Inc. (8316.TO) together paid roughly Y300 billion for preferred shares that can be converted into common Sanyo stock.

Their agreement with Sanyo is set up so that the preferred shares cannot be converted and transferred to third parties until March 13. Sanyo shares were up 53% from late last year before the plunge Friday.

A spokesman for Daiwa Securities SMBC Co., a unit of Daiwa Securities, said the report on Sanyo Electric's accounting doesn't affect Daiwa group's support for the electronics maker.

Traders said a wider issue is what this says about accounting practices in Japan and the role of auditors.

"We've already had a patch of problems with Chuo Aoyama and at Nikko Cordial, and now Sanyo. What is going to weigh on people's minds is whether all this can snowball into a Japanese Enron," says Motomi Hiratsuka, head of sales trading at BNP Paribas.

Japan's third-largest securities broker Nikko Cordial Corp. is in the midst of correcting past financial statements to properly account for a deal involving its private equity unit. Nikko's internal probe team concluded last month that the company's former top management was involved in the accounting scandal.

Nikko's then auditor, Chuo Aoyama, which is now Misuzu Audit Corp., was also ordered last year to suspend business for two months after it was found to be part of a massive earnings fraud by Japanese cosmetics maker Kanebo.

Chuo Aoyama was Sanyo's auditor for the period during which the reported accounting problems occurred.

Hit by falling prices of consumer electronics products such as mobile phone handsets and digital cameras, and an unprofitable semiconductor business which it spun off in July, Sanyo suffered a group net loss of Y205.66 billion for the year ended in March 2006.

But the company has showed signs of recovery. Sanyo predicts a group net loss of Y50 billion on sales of Y2.3 trillion, and in the latest October-December quarter its operating profit climbed 31% from a year earlier.

As reports of its possible accounting troubles spread, credit protection for Sanyo became sharply more expensive. Credit default swap spreads on Sanyo changed hands at 150, and then 250, up sharply from indications of around 70-90 in recent sessions. Sanyo Electric CDS last traded at 112 on Jan. 17.

Sanyo's shares also face the risk of being delisted if accounting problems are found, analysts say.

"We can't deny the possibility of a share delisting," Credit Suisse analyst Koya Tabata said in a report. In the past, companies such as Livedoor Co. have been delisted by the Tokyo Stock Exchange for inaccurate financial statements.

A spokesman from the exchange said it will monitor SESC's inspection of Sanyo Electric's past accounting.

-Edited by Kenneth McCallum