

The Japan's Economic Future –From a Financial Sector Perspective–

30th August, 2023

Shigeru Ariizumi

Vice Minister for International Affairs

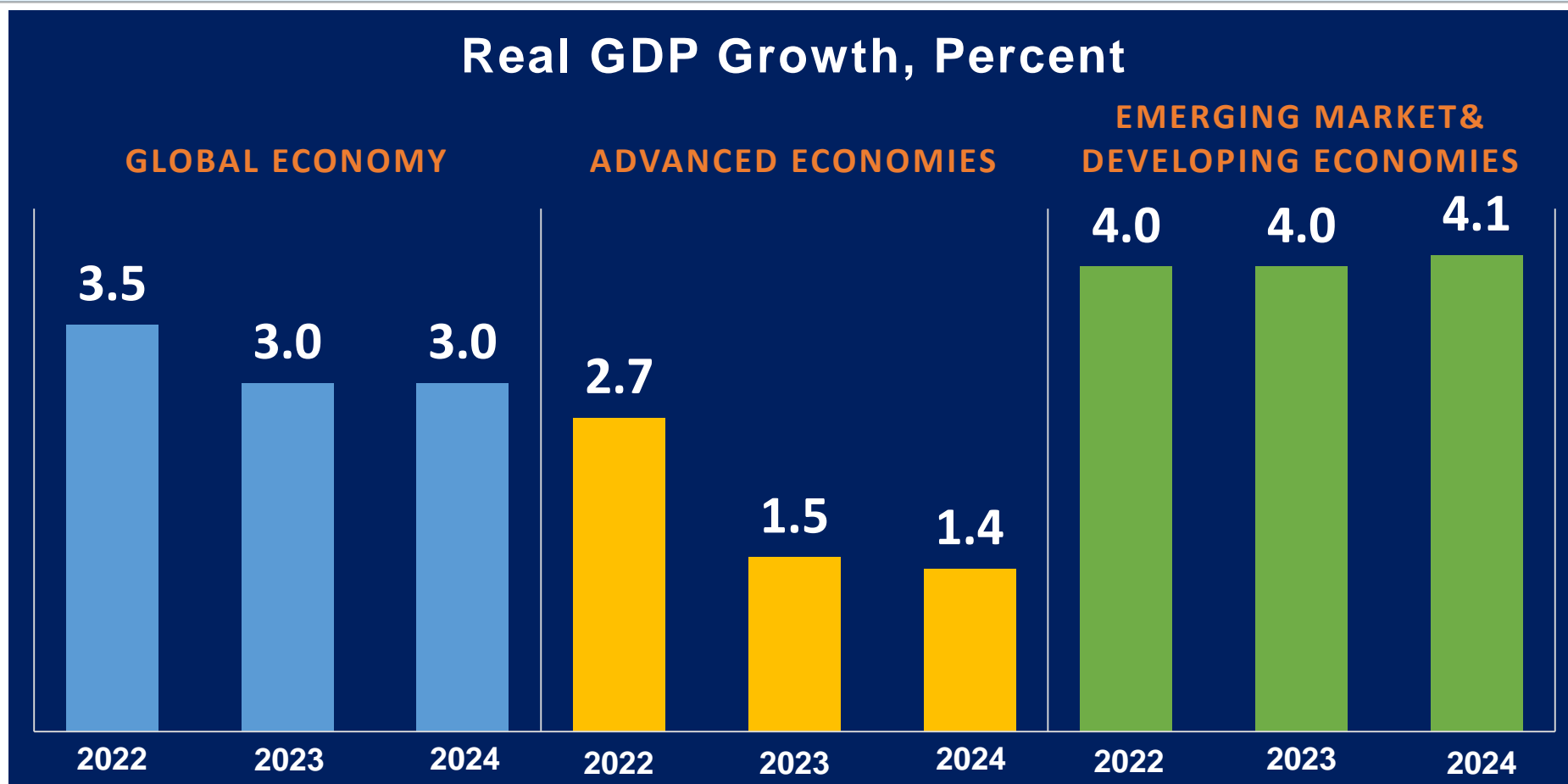
Financial Services Agency,

Government of Japan



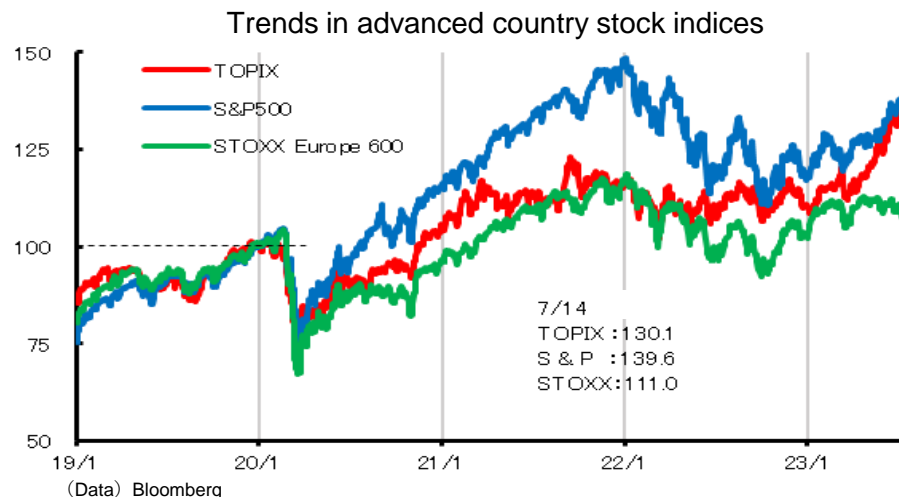
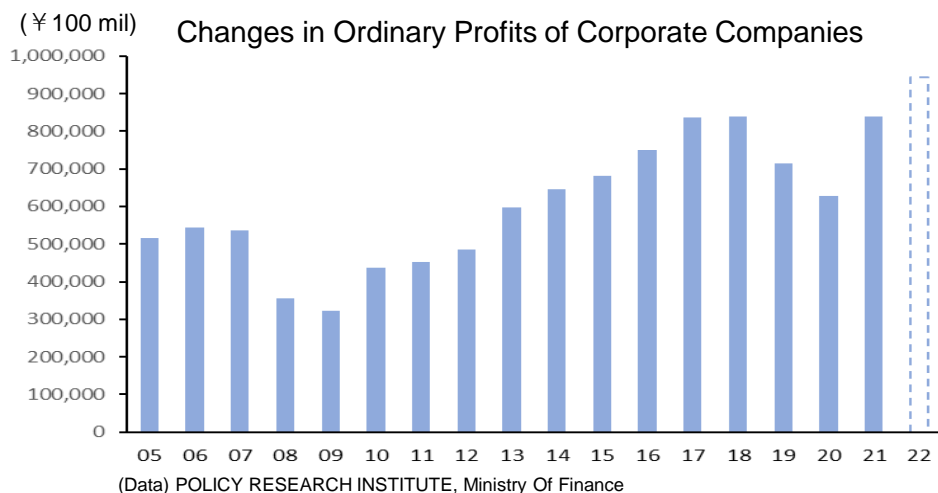
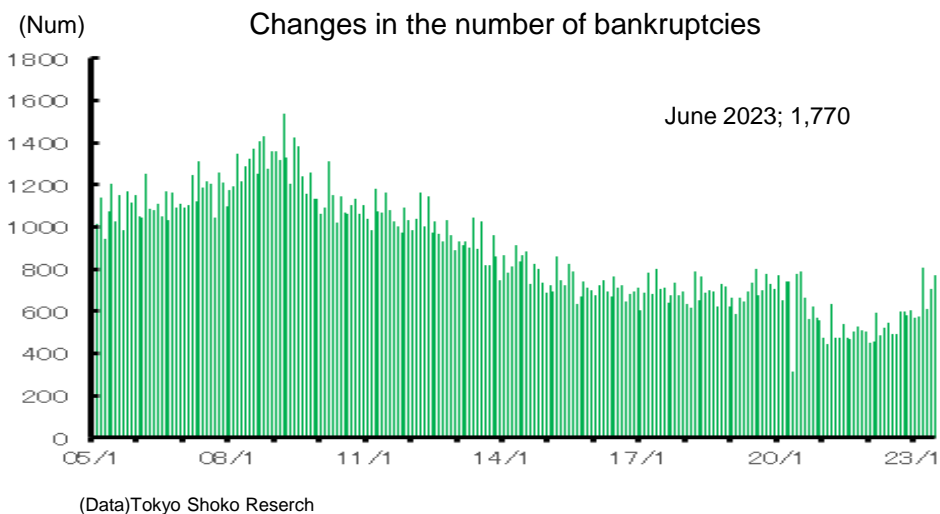
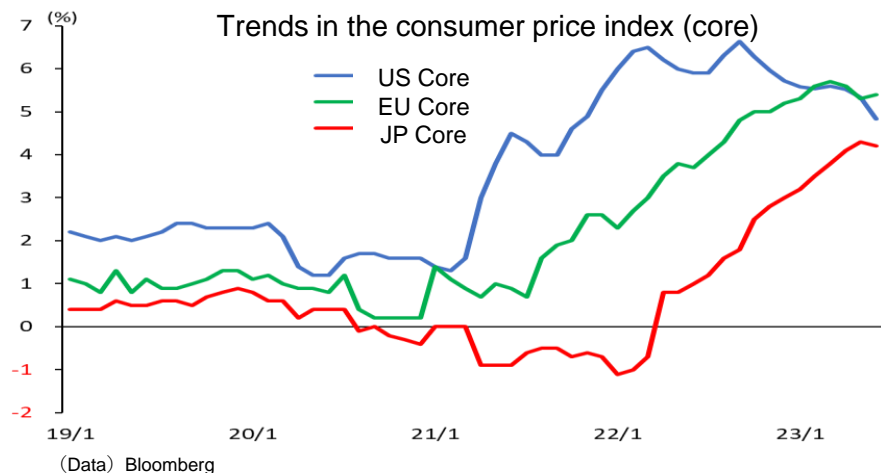
Disclaimer: The opinions expressed in this presentation and on the following slides are solely those of the presenter and not necessarily those of FSA.

- ❑ The global economy continues to gradually recover from the COVID-19 pandemic and from Russia's invasion of Ukraine, yet the balance of risks to global risk remains on the downside.
- ❑ As a baseline scenario, global growth is projected to be 3.0% in 2023, falling from 3.5% in 2022. Economic growth of advanced economies is expected to be 1.5%, with sharp contrast to EMDEs and developing economies. Japan's growth is estimated at 1.4% in 2023 increasing from 1.0% in 2022, supported by pent-up demand and the continued monetary easing policy.



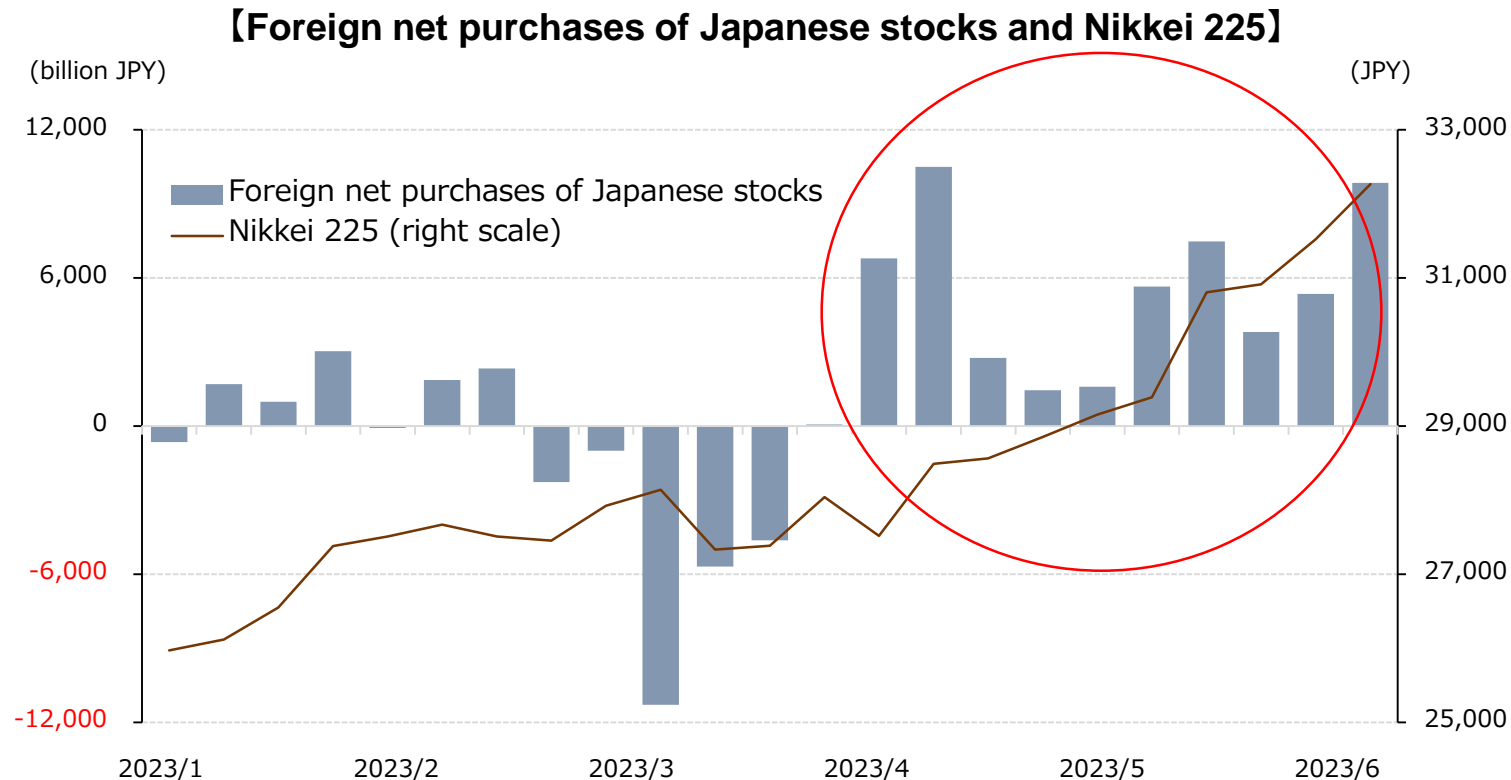
The Japanese Economy and Financial Markets

- ❑ The Japanese economy continues to moderately recover as the normalization of economic activities from COVID-19 has progressed. Inflationary expectation has shown some upward movements through year on year increase of CPI is slower than a while ago. Corporate earnings remain strong and the number of bankruptcy remains low by historical standards.
- ❑ Japanese equity prices have been strong compared to other major economies, and the Nikkei Stock Average has recently reached its highest level since 1990.



The Japanese Equity Market

- ❑ The Nikkei index has been rising since this April, mainly due to the increased foreign net purchases.
 - Strong corporate earnings and future potentials
 - Weaker inflationary pressure and accommodative monetary policy
 - Geopolitical reassessment of Asian Markets
 - Various reform measures



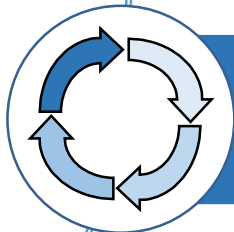
I . Corporate Governance Reform



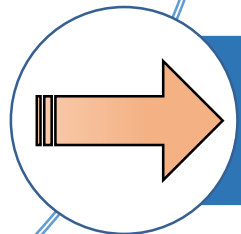
A Public-Private Initiative



Growth-oriented Governance



Periodic Review and Follow-up



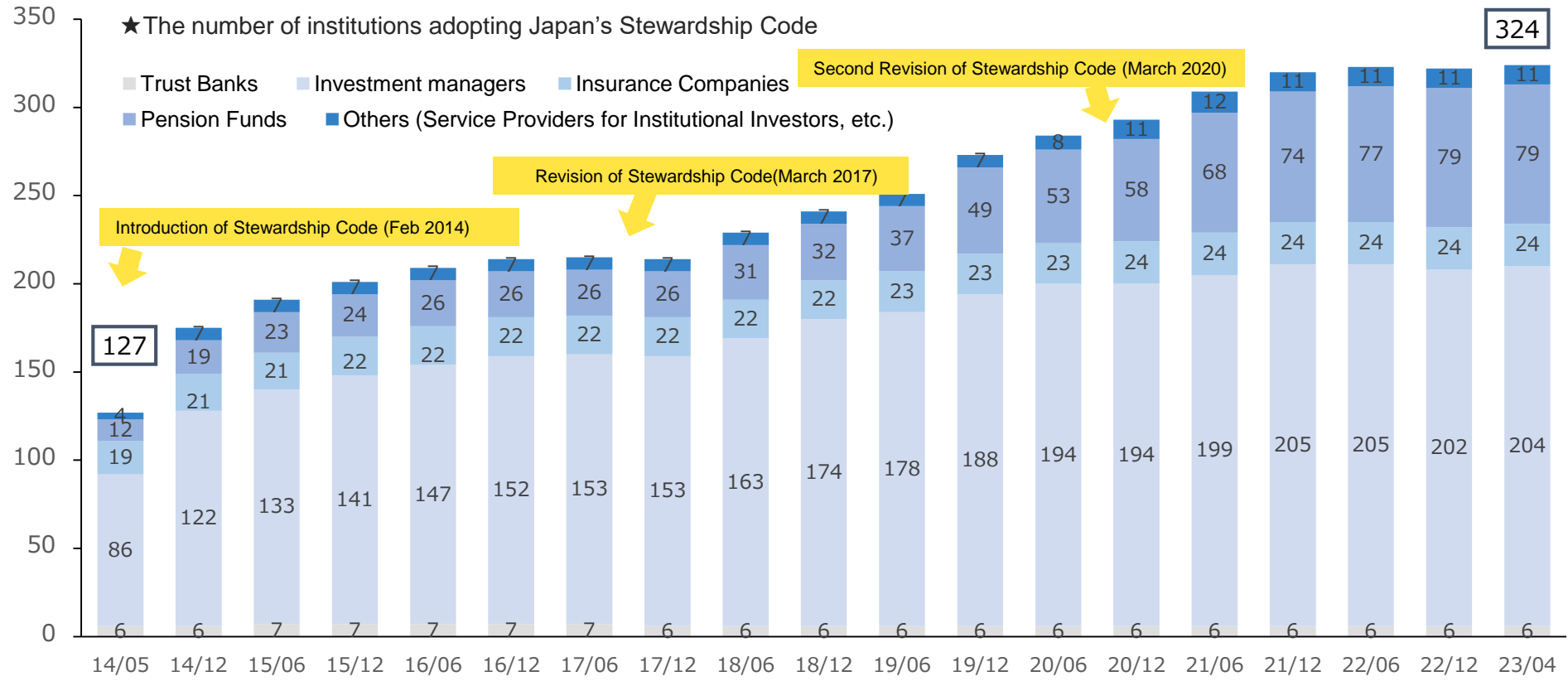
From Form to Substance

Japan's Corporate Governance Reform



Institutions Adopting Japan's Stewardship Code

- ❑ Institutions adopting Japan's Stewardship Code has continued to increase. As of end of April this year, 324 institutional investors have adopted the Code.
- ❑ Out of the 324, 297 institutional investors* have adopted the upgraded 2020 revised version of the code. (*6 trust banks, 184 investment managers, 24 insurance Companies, 73 pension funds, 10 others)

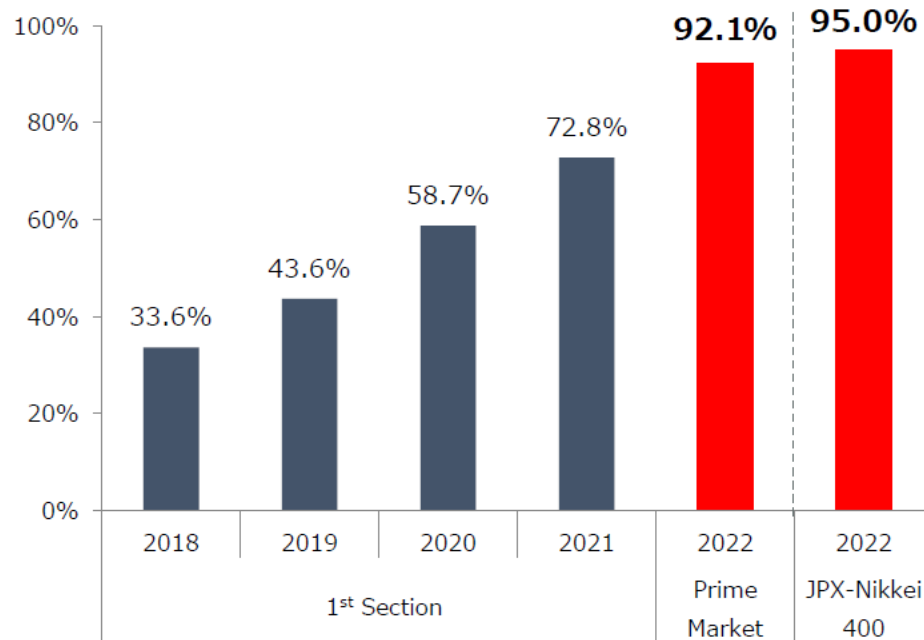


Source: Prepared by FSA

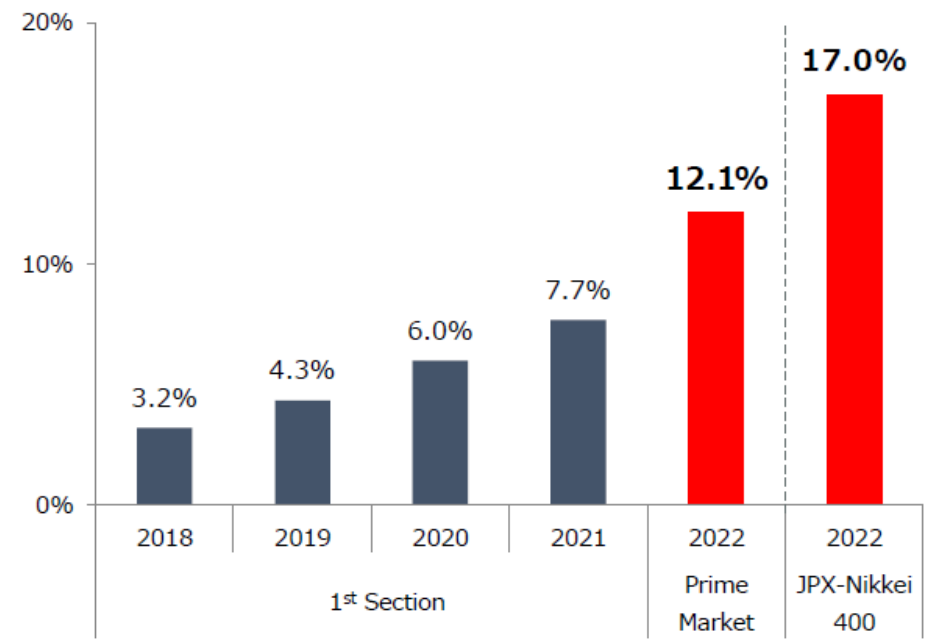
Independent Directors in JPX Listed Companies

- ❑ In **Over 90%** of Prime Market listed companies, **1/3 or more** of their board members are independent directors.
- ❑ In **17%** of JPX Nikkei 400 companies, the **majority** of their board members are independent directors.

【Companies with independent directors making up 1/3 or more of their boards】



【Companies with independent directors making up the majority of their boards】

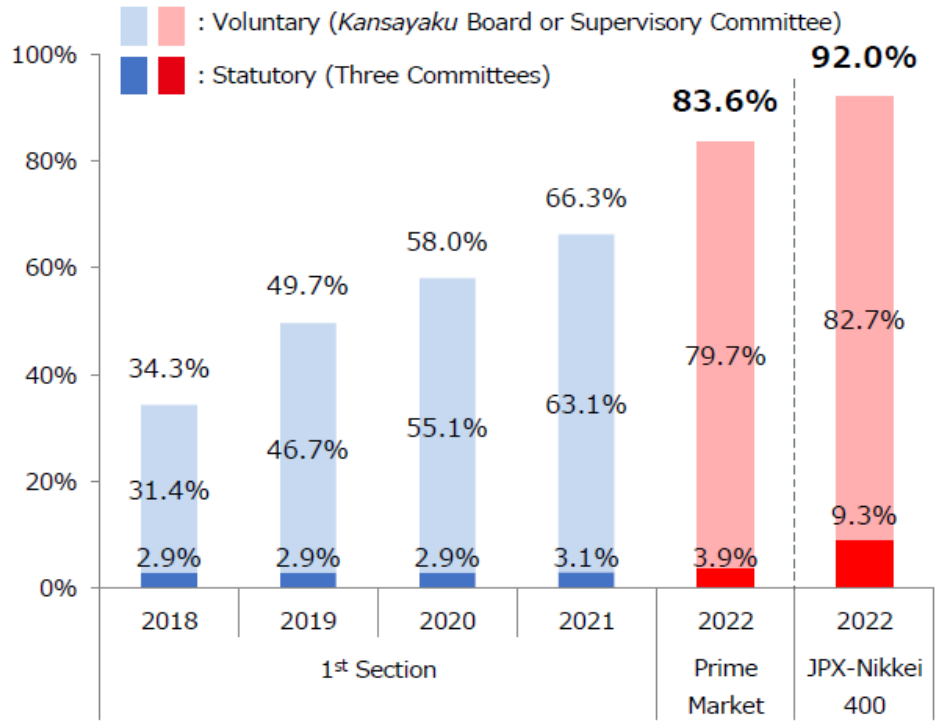


Source: Excerpts from “Response of Listed Companies regarding Revised Corporate Governance Code (As of July 14, 2022), Tokyo Stock Exchange, Inc. August 3, 2022,” partially processed by FSA

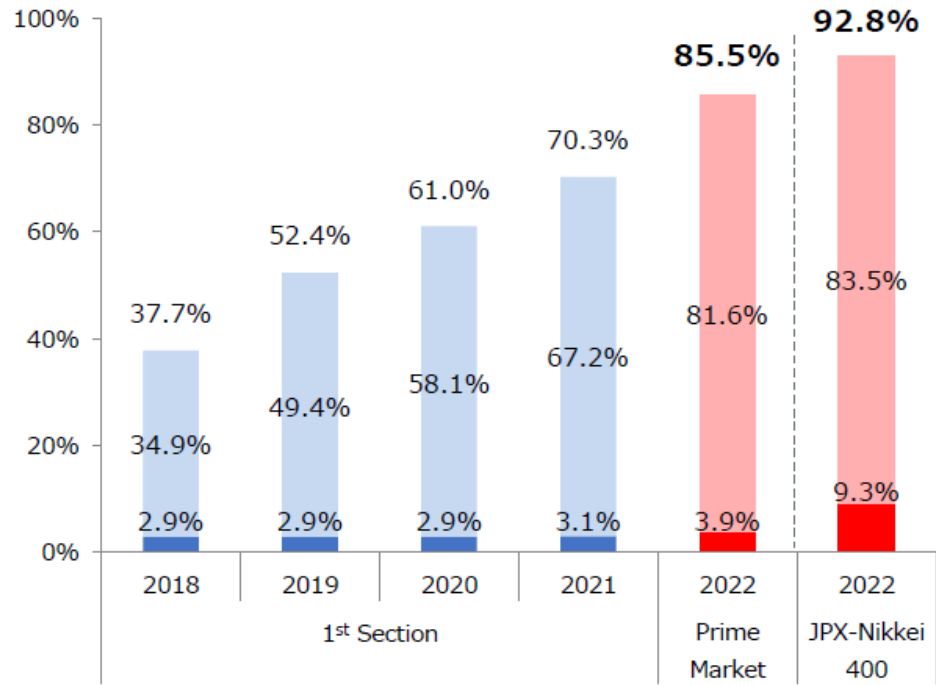
Nomination / Remuneration Committees

More than 80% of Prime Market Corporates have statutory or optional Nomination/ Remuneration Committees.

【Companies with a nomination committee】



【Companies with a remuneration committee】



Source: Excerpts from "Response of Listed Companies regarding Revised Corporate Governance Code (As of July 14, 2022), Tokyo Stock Exchange, Inc. August 3, 2022," partially processed by FSA

From Form to Substance - Corporate Governance Reform Action Program (1)

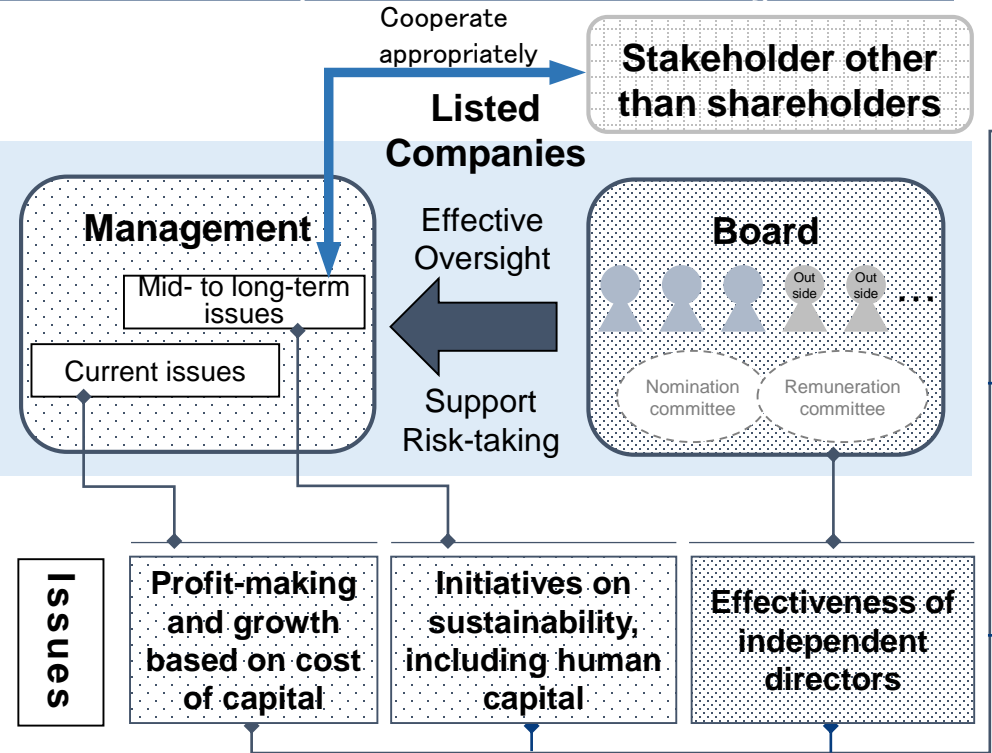
□ The Council of Experts Concerning the Follow-up of Japan's Stewardship Code and Japan's Corporate Governance Code published recommendations regarding "Action Program" as of April 26. The Council will review the implementation status from time to time and consider whether additional measures are needed.

Action Program for Accelerating Corporate Governance Reform: From Form to Substance

Approach to future initiative

- It is vital to move the focus of reform from form to substance in resolving the issues. To this end, it is necessary to create an environment that promotes self-motivated changes in the mindsets of companies and investors, as well as to make the dialogues between companies and investors more productive and more effective.
- It is appropriate to examine the timing of the revision of each Code in a timely manner based on the status of progress from the viewpoint of the effective implementation of corporate governance reform, not necessarily following the review cycle in the past years.

1. Issues for seeking sustainable corporate growth and increased corporate value over the mid- to long-term



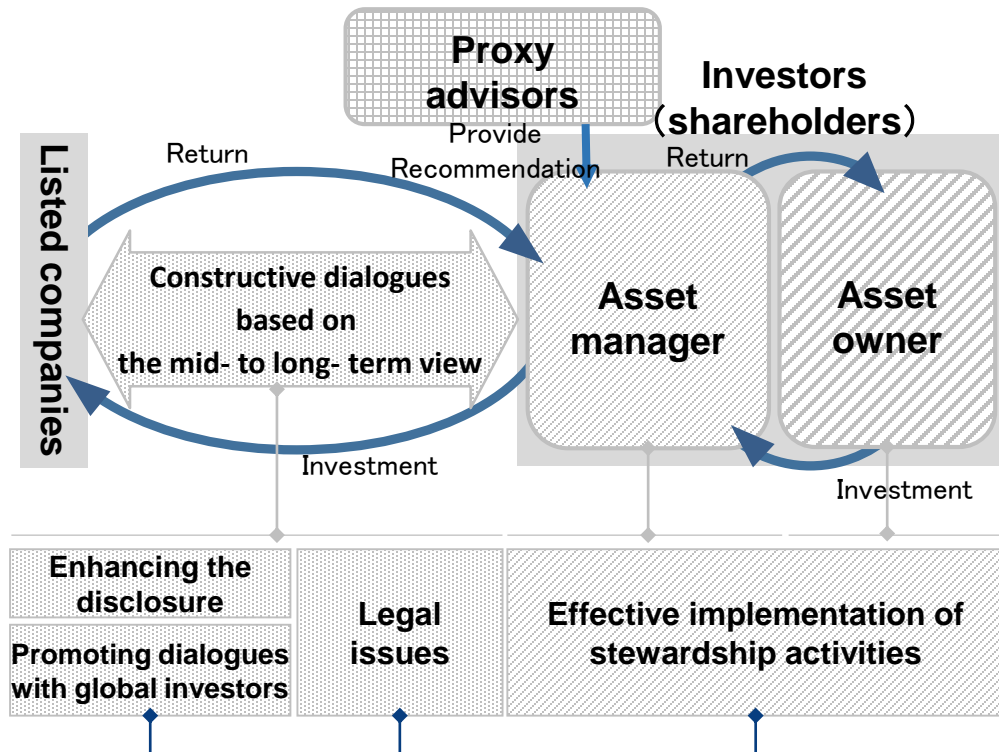
Specific measures

- A) Encouraging the management with an awareness of profit-making and growth**
Encourage the management with an awareness of profit-making and growth based on the cost of capital (such as the proper allocation of management resources toward risk-taking, including a business portfolio review and investments in human capital, intellectual properties and R&D)
- B) Encouraging the management with an awareness of sustainability issues**
Encourage companies to take actions on sustainability through publication of companies' good disclosure practices. Consider measures to improve the diversity of the board and core human resources, such as increasing the percentage of female executives (target of 30% or more by 2030).
- C) Improving the effectiveness of independent directors**
Promote further improvement of the effectiveness of independent directors through compilation and publication of the actual status and examples of a board, nomination committee and remuneration committee, and educational activities to promote understanding of the roles expected of independent directors

Corporate Governance Reform Action Program (2)

Action Program for Accelerating Corporate Governance Reform: From Form to Substance

2. Issues related to dialogue between companies and investors



Specific measures

A) Effective implementation of stewardship activities

Promote the efforts of asset managers and asset owners to deal with the issues relating to the stewardship activities (including allocating sufficient resources, providing incentives for stewardship activities, establishing governance structures of asset owners).

B) Enhancing the disclosure as a basis for dialogue

Request to disclose the status of dialogues and make clear sufficient and insufficient cases of "Explain". Consider measures to provide investors with the information they need prior to the general shareholder meeting and to promote timely disclosure of corporate information.

C) Promoting dialogues with global investors

Promote dialogues between companies and global investors by "visualizing" companies that willingly and actively respond to the expectations of global investors and further expand the coverage of English disclosure.

D) Resolving legal issues

Consider clarification of "act of making important suggestions" and "joint holders" under the large shareholding reporting rule, transparency of beneficial shareholders, and how to protect minority shareholders in the case of a partial takeover bid.

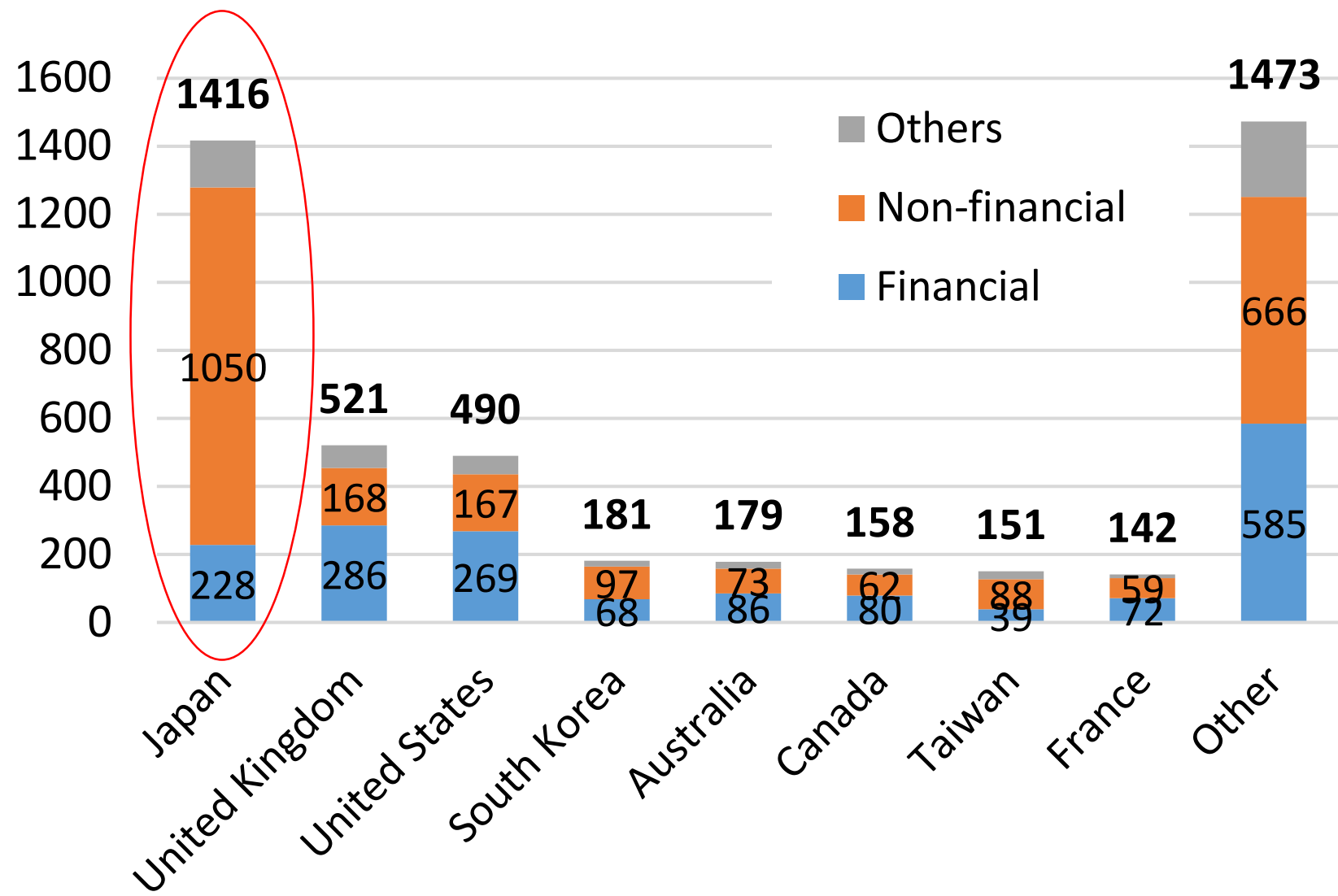
E) Resolving market environment issues

Consider the disclosure and corporate governance issues with regard to quasi-controlled listed companies, follow up on the progress of reduction of cross-shareholdings and consider whether further measures are called for.

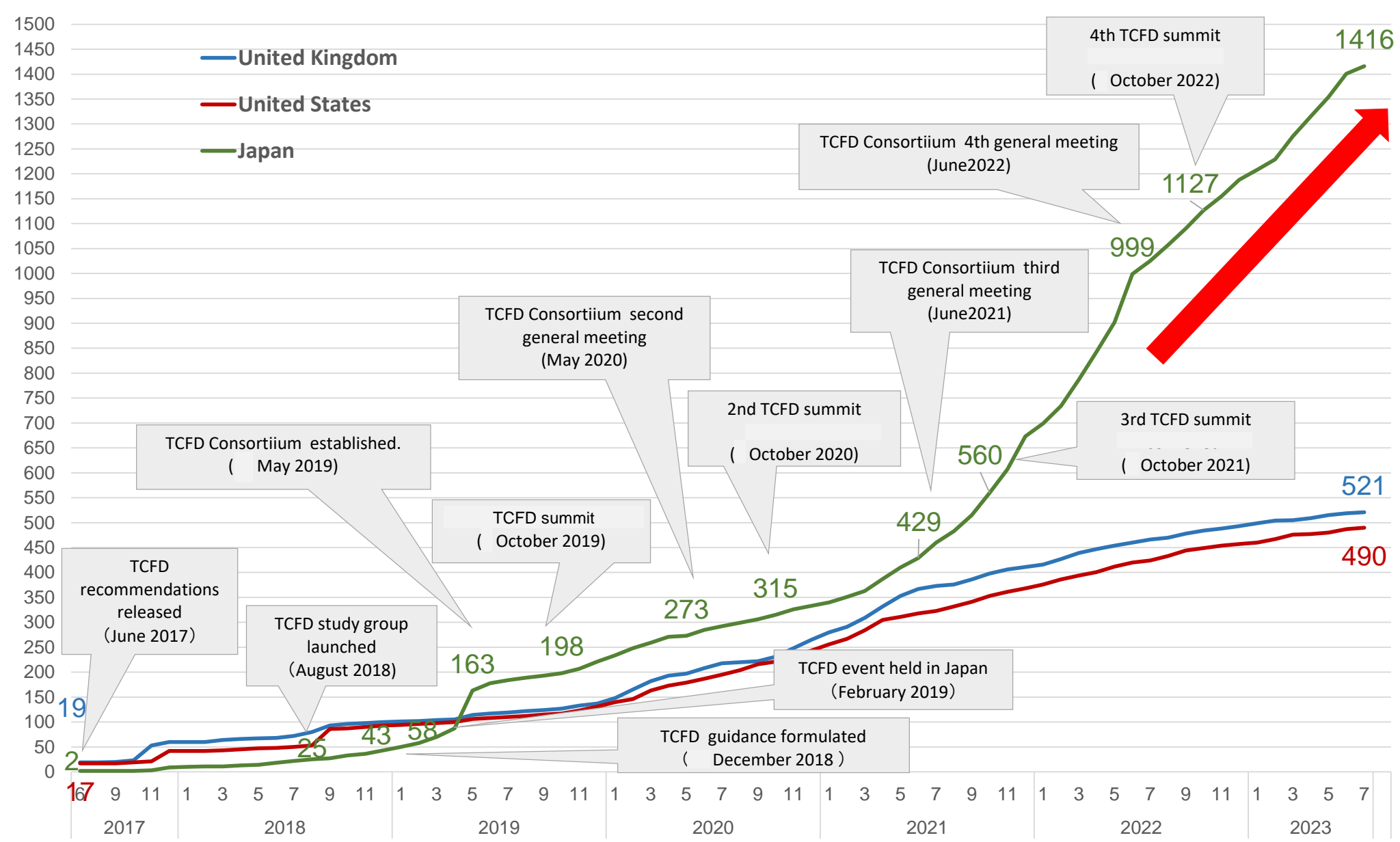
II . Sustainable Finance

TCFD Supporters (As of July 2023)

□ The TCFD has developed a framework to help public companies and other organizations disclose climate-related risks and opportunities.



TCFD supporters (As of 25 July 2023)



Sustainable Finance Initiatives (1)

to June 2023

From July 2023 to December 2023

Corporate Disclosure

Added a new section in Annual Securities Reports, on sustainability information such as climate change and human capital

Standards to be developed by the Sustainability Standards Board (SSBJ). Collect and publish good practices of sustainability information disclosure

Participate in international discussions on ISSB standards development including through publicly communicating Japan's views. Discuss sustainability information guarantee.

Capital market

Data

Provide ESG data including GHG emissions through JPX platforms.

Asset Owners

Identify challenges for institutional investors and assist them on improving effective engagement.

Individuals

Revised supervisory guidelines to clarify expectations for ESG funds

Improve ESG investment trusts accessibility for individual investors.

ESG evaluation

Called for adoption of the Code of Conduct by ESG evaluation providers.

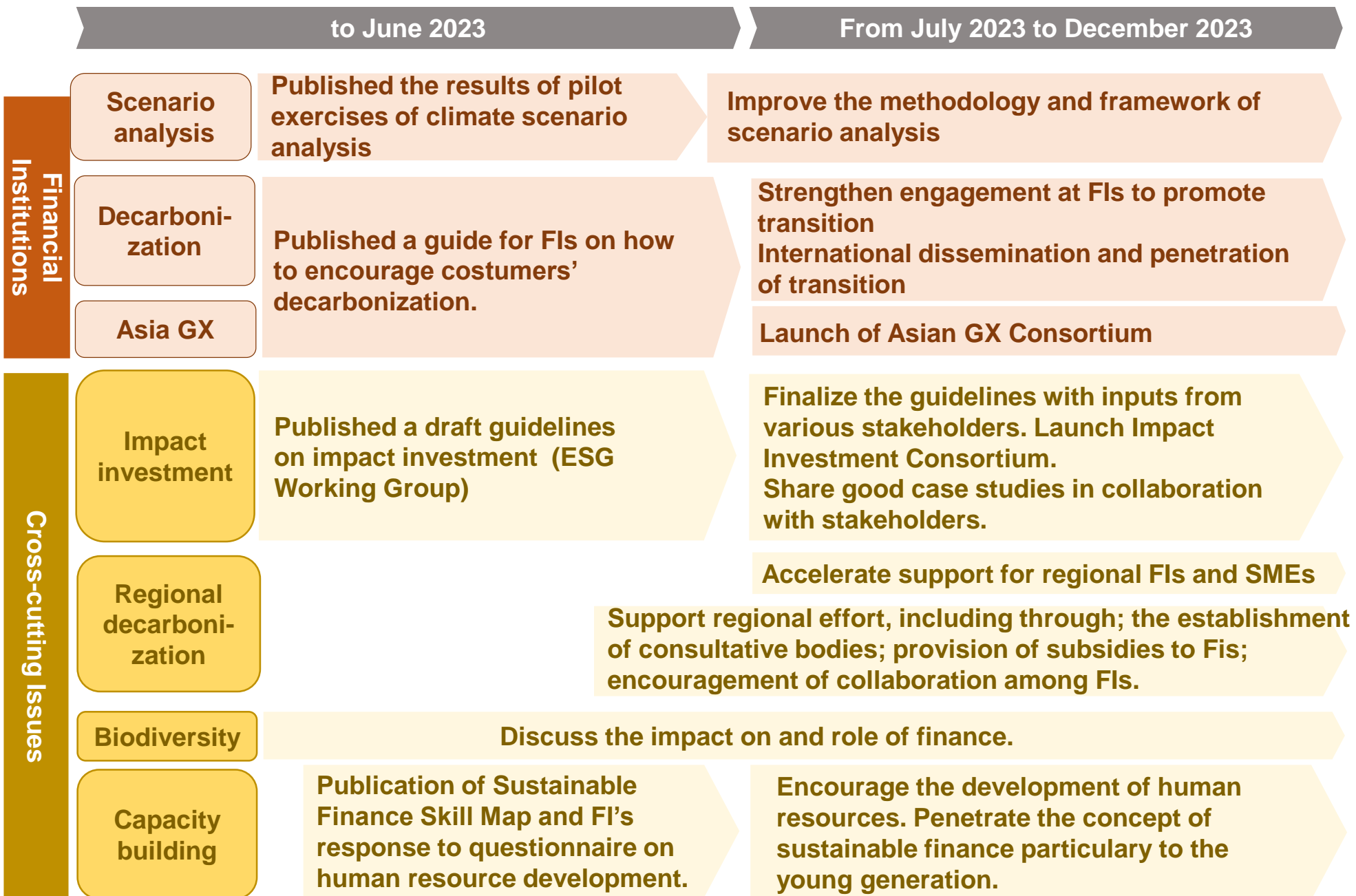
Call for adoption of Code of conduct by ESG data providers.
Improve effectiveness of the Code of Conduct.

CC market

Demonstration testing of market development, etc.

Support market development and credit creation to foster transactions

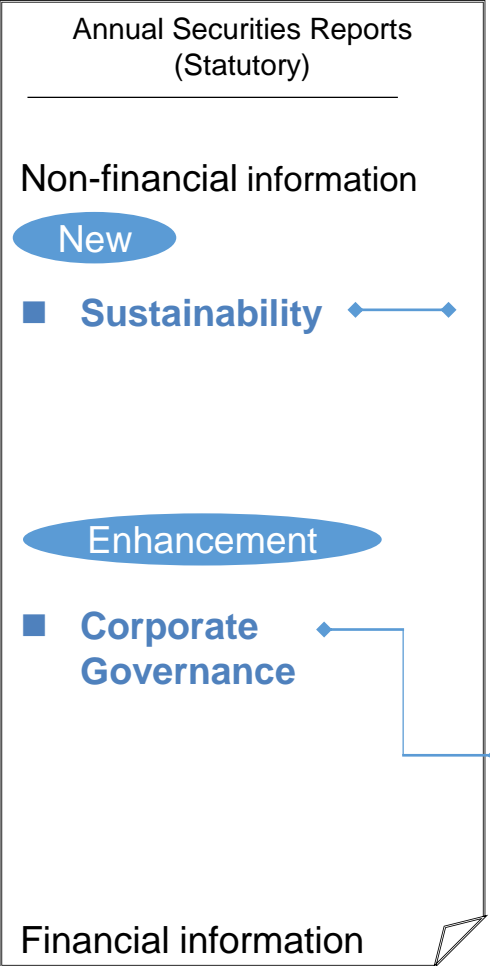
Sustainable Finance Initiatives (2)



New section in Annual Securities Report on Sustainability

Enhancing non-financial disclosure

(Matters of Cabinet Office Ordinance's revisions)



Sustainability

General

- A new section for disclosure of sustainability information will be created
 - "Governance" and "Risk Management" will be disclosed by all issuers.
 - "Strategy" and "Metrics and Targets" will be disclosed under materiality judgement by an issuer.

Human capital

- "Human resource development policies" and "Policies on improving workplace environment" will be added to disclosure items.

Diversity

- "Gender pay gap," "Ratio of women in managerial positions," and "Ratio of male workers taking childcare leave" will be added to disclosure items.

Corporate Governance

Functioning of the Board of Directors

- A new section for disclosure of activities of the Board of Directors, Nomination Committee, and Remuneration Committee will be created.

Asian GX Hub (GX international Financial Center)

□ Support Asian transitions to Net Zero by integrating information, human resources and financial flows.

Data

Aggregate corporate data, including CO2 emissions, on the JPX ESG Bond Information Platform.

Improve access to overseas data in collaboration with Asian stock exchanges.

Human Resources

Train GX financial professionals and assist private sections' effort to set qualification for ESG-related analysts.

Open global GX and sustainable finance courses at Japanese and Asian universities.

Project Development

Establish **Asian GX Consortium** to convene public and private sector participants.

Exchange information on investment strategies on potential GX projects leveraging tools such as blended finance and public-private partnerships.

Support **creating carbon credits** to promote GX investments in Asia.

Disseminate Japan's initiative including through Japan-ASEAN Meetings.

Asian GX Consortium



Ⅲ. Reform of the asset management sector

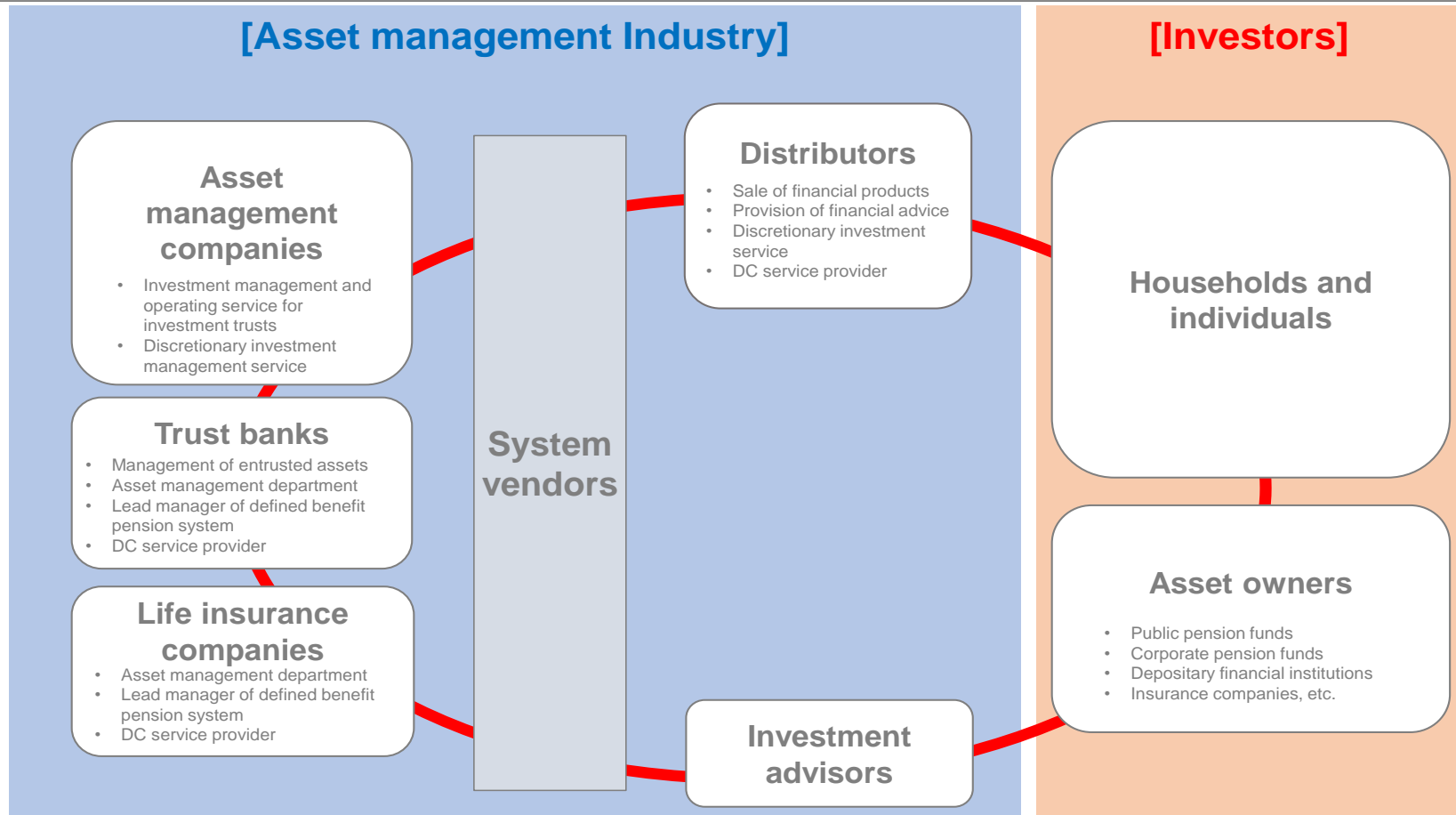
Excerpt from the “Progress Report 2023 - For Enhancing Asset Management Business
in Japan”
(April 2023)

Basic Policy on Economic and Fiscal Management Reform 2023 (Cabinet decision on June 16, 2023)

- . . . In addition, by the end of the year, the government will formulate a policy plan for fundamental reform of asset management sector, etc., that aims at improving the governance and strengthening the structure of asset management companies and asset owners, improving asset management capabilities, and fostering an environment to diversify asset management products.
- . . . the government will work to promote competition by revising Japan's unique business practices and barriers to entry and by enhancing support for new entrants.

Asset Management Business in Japan

- ❑ Asset management firms traditionally has provided full service in-house.
 - This has become a de facto entry barrier;
 - Discouraged competition among individual services
 - Led to distributors exercising strong influence on product development
- ❑ Lack of disclosure and insufficient human resources in asset owners has also been an issue
 - muted market discipline for competition

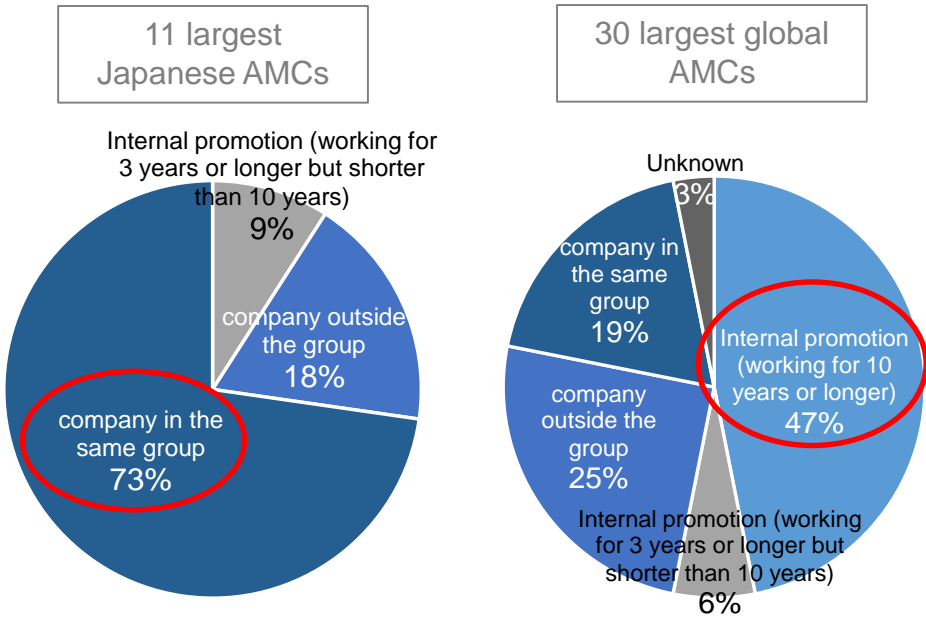
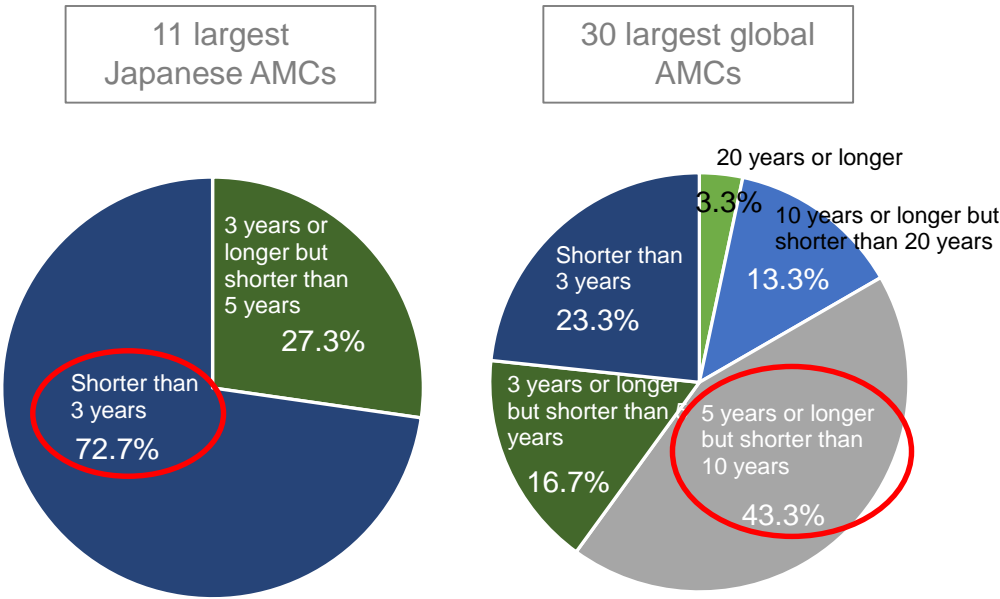


Senior Management of AMC in Japan (1)

- ❑ CEOs of AMC affiliated with large Japanese financial institutions
 - shorter terms in office
 - coming from other companies within the group
- ❑ Investors may be concerned that Japanese AMC is prioritizing internal personnel consideration rather than growth.

Terms in office of the CEOs of large AMCs

Former positions of the CEOs of large AMCs



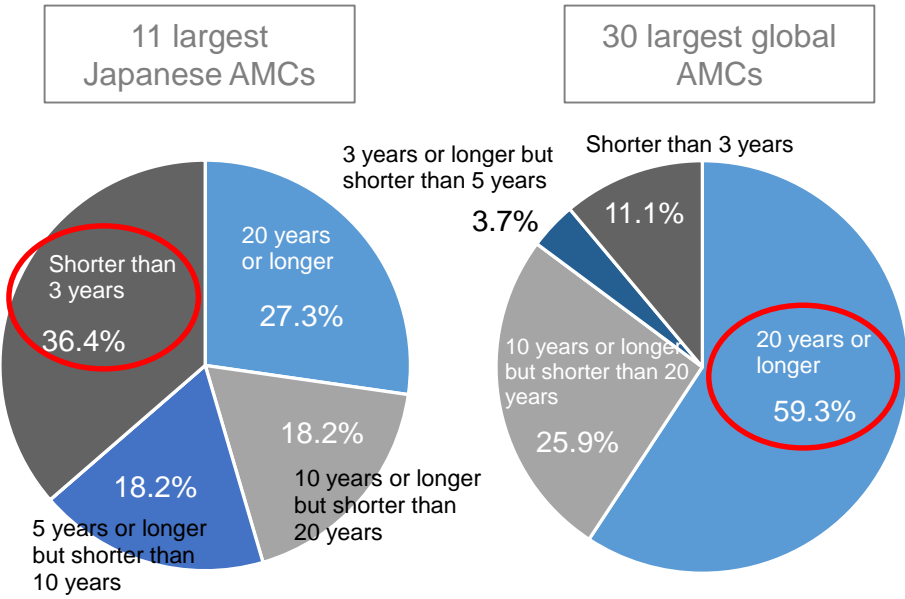
(Source) FSA, based on the data as of the end of December 2022 provided by AMCs for the 11 largest Japanese AMCs and based on the disclosure information on the AMCs' websites and news articles for the 30 largest global AMCs (including one Japanese AMC)

(Source) FSA, based on the data as of the end of December 2022 provided by AMCs for the 11 largest Japanese AMCs and based on the disclosure information and new articles for the 30 largest global AMCs (including one Japanese AMC)
 (Note) Executives who worked for AMCs for three years or longer and were promoted to CEOs, are categorized into "internal promotion."

Senior Management of AMCs in Japan (2)

- ❑ CEOs of AMC affiliated with largest Japanese institutions
 - Shorter working experience for AMCs
- ❑ There is a need, for example, to improve;
 - succession plans
 - provide and explain credible grounds for CEO appointment

Numbers of years working for AMCs before taking over a CEO position



Disclosure of grounds for appointment of CEOs of large global AMCs

- He has 39 years of investment experience, all with our company
- Under the planned succession, he will become our next CEO
- She has a global mindset, and significant leadership experience in all facets of our operations
- He's led our mutual fund department in the Asia-Pacific region, the United States, and Europe
- She has three decades of experience as an analyst, portfolio manager and CIO in the financial sector with global names

(Source) FSA, based on the data as of the end of December 2022 provided by AMCs for the 11 largest Japanese AMCs and based on the information on websites and news articles for 30 largest global AMCs (including one Japanese AMC)
 (Note) The number of years working both for AMCs and a department of management of entrusted assets in trust banks are counted as the "number of years of working experience in AMCs."

(Source) FSA, based on the information on the websites of 30 largest global AMCs

Independence of AMC's Management

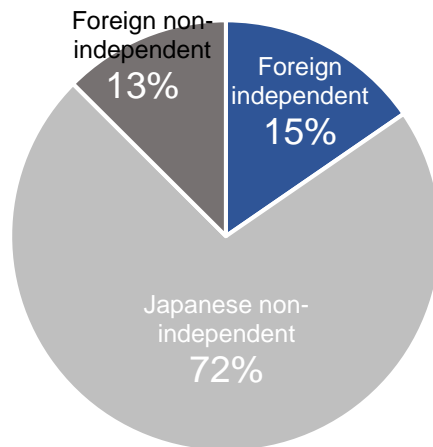
- ❑ In Japan, Independent AMCs have not been dominant players, in sharp contrast to the global trend.
 - A certain survey* indicates that annual performance of independent AMCs is higher than that of non-independent AMCs by 62 basis points.

**source: Affiliated Managers Group, "The Boutique Premium -The Boutique Advantage in Generating Alpha"*

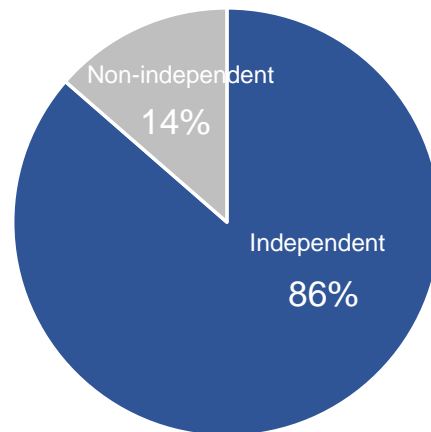
- ❑ Non-independent AMCs should keep an appropriate distance from the parent group, including personnel and remuneration, to ensure necessary flexibility for management to hire external talents.

Share of independent and non-independent AMCs in AUM

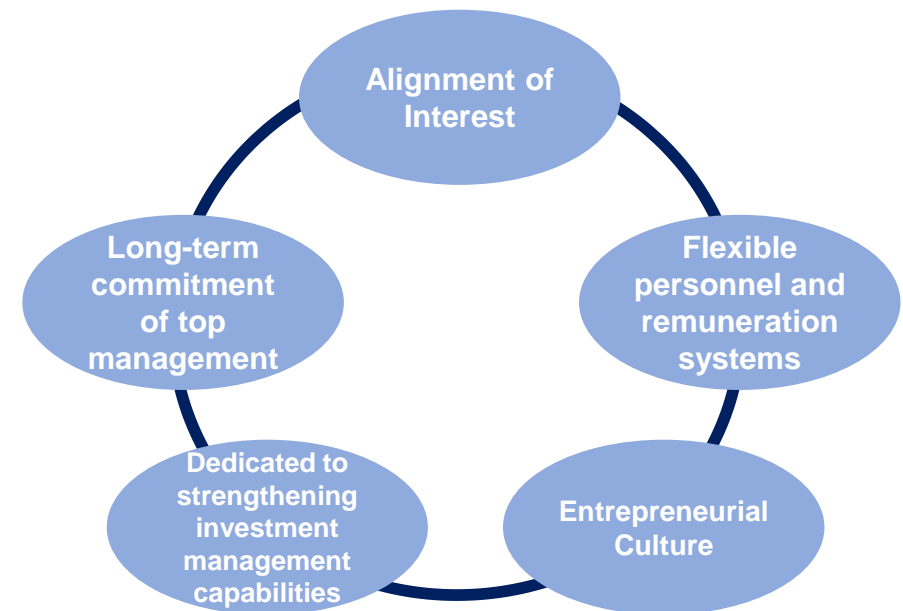
20 largest AMCs in Japan



30 largest global AMCs



Strengths of independent AMCs



(Source) FSA. The pie chart for the 20 largest AMCs in Japan is based on the data as of the end of March 2022 provided by AMCs. The chart covers AMCs that hold domestic publicly offered investment trusts, privately placed investment trusts, and discretionary investment management agreements and are ranked in the top 20 in terms of the total amounts of those entrusted assets. The pie chart for the 30 largest global AMCs covers companies that are ranked in the top 30 in terms of the total amounts of open-end mutual funds and ETFs under their management. Categorization of independent and non-independent is based on the FSA's judgment.

Thank you for your attention.
