"Putting the G20/OECD Principles of Corporate Governance into Practice"

OECD-Southeast Asia Corporate Governance initiative

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I. Opening Speech

１. Good morning, ladies and gentlemen. Thank you very much for the kind introduction. It is a great honor for me to deliver introductory remarks on this great occasion.

First of all, as the Chair of the Corporate Governance Committee of the OECD, I would like to express my sincere gratitude to the Securities and Exchange Commission of Cambodia for hosting this event and also thank you all in this room for your participation and the OECD Secretariat for this good preparation.

20 years have passed since I first visited this great country of Cambodia in 1996 to see, of course, Angkor Wat and Angkor Thom as well. Today I'm surprised to see a dramatic change and development since then.

Today, I would like to start my remarks with the key role of corporate governance, CG, for the economy, and how the Corporate Governance Principles and the Corporate Governance Committee contribute to this dynamism, and then proceed to their specific roles in Cambodia and the Southeast Asian region, which are full of growth potential.

２. Let me start by explaining what role CG is expected to play in society.

The ultimate goal of corporate governance is to support stronger economic growth and a more inclusive society. To achieve this, it helps to build an environment of trust, transparency, accountability and business integrity.

More specifically, it is important to earn long-term "patient" capital to support stable growth. In order to attract such investors from global financial markets, it is indispensable to build a credible corporate governance system consistent with the principles of global standards.

３. Now I would like to introduce such global standards, namely our G20/OECD Corporate Governance Principles. It was first formulated in 1999, revised in 2004 and updated again in 2015 incorporating lessons learnt from the financial crises from 2008 and OECD's peer reviews.

While it has been widely used as an international benchmark for corporate governance since its formulation, the principles were endorsed by G20 summit leaders in 2015, and now serve as the single global standard on CG, also adopted by the World Bank and Financial Stability Board as their key standards.

The principles cover a wide range of corporate governance such as shareholders' rights, institutional investors, disclosure and the responsibilities of the board. However, the principles do not require each jurisdiction or company to be strictly consistent with all the detailed components. It aims to help policy makers evaluate and improve the legal, regulatory and institutional framework for corporate governance, with a view to supporting economic efficiency, sustainable growth and financial stability.

So the principles are not legally binding and do not aim for detailed prescriptions for national legislation. Rather, they seek to identify objectives and suggest various means for achieving them. They aim to provide a robust but flexible reference for policy makers and market participants to develop their own frameworks for CG.

I am confident that OECD Principles will be of great use for countries in this region to further develop their own CG frameworks in a manner consistent with each other, while taking into account the different development stages and unique economic situations in each country.

The principles will need not only to be flexible but also continuously evolve as the economic environment changes. For instance, the recent revision established a new chapter focusing on institutional investors, stock markets and other intermediaries, in order to reflect the growing complexity of the investment chain.

To build a suitable CG system and arrange appropriate implementation, we can also learn from other countries' experiences. This initiative is to serve as a forum for exchanging such experiences and knowledge.

4-1. Now moving on to the application to this region. Cambodia has been showing significant economic growth recently. The average annual GDP growth after the financial crisis has been around 7%, mainly led by the garment and the tourism sectors. Given an expected demographic bonus, Cambodia has great potential for growth if appropriate policies are implemented. CLMV countries altogether also show strong growth such as 7% annually.

To sustain rapid growth for further economic development and raising national welfare, these countries rely considerably on foreign sources of capital.

Now in advanced economies, the interest rate has been low for a while, supported by expansionary monetary policies, although there are some signs of change. These economies have arguably entered into a low-growth stage and the low-rate environment may last even longer. There certainly exists capital searching for yield, in other words, a benefit from the rapid growth of emerging markets.

As long as these are "patient" long-term investments, they will benefit both investors and the companies receiving such investments. Corporate Governance is certainly a key element to facilitate connecting such supply and demand of capital. Good CG will ensure those who supply such long-term capital and other stakeholders that their rights are well protected, which would facilitate companies' access to the capital market.

4-2. The OECD CG Committee has started this Southeast Asia CG Initiative in 2014, which focuses on this region, especially CLMV countries. We have held three successful meetings so far in Myanmar, Viet Nam and Lao PDR.

In the CLMV countries, it is commonly the case that security exchanges have recently been established and the first few companies have been listed, and through the process of their listing and other initiatives, corporate governance reform has made a certain degree of progress.

And now we are very pleased to have the 4th meeting here in Cambodia. In this meeting, a number of distinguished speakers will introduce the development of CG frameworks in CLMV as well as other Asian countries. There will also be discussion on various interesting themes such as the investment policies of CLMV countries and progress on ASEAN regional integration regarding CG.

This initiative is not only useful for emerging market countries but also for participants from advanced countries as a CG system is never finalized but needs to always be updated. In Japan, CG reform has been one of the top agenda items for the government as we perceive CG as one of the key elements to enhance corporations' long-term profitability and productivity by promoting active business decisions, the fruits of which will also benefit households. I would be honored to introduce our reform progress in the next session, and look forward to learning from colleagues gathering here.

I expect that this year's initiative will be a great opportunity for all of us to learn from each other through active discussion and that it will contribute to progress in corporate governance frameworks and further economic development both in this region and beyond all over the world.

II. Panel Presentation

(OECD principles and Japanese CG reform)

- I would like to start with the background of Japan's two codes to show their consistency with the global standard, the OECD Principles.
- Japan has formulated its CG Code in accordance with the new G20/OECD Principles of CG which was revised in 2015 and is now regarded as the global standard, by inviting a CG top expert from the OECD to advise our formulating process, while we were actively involved in the discussions of the OECD CG Committee as Vice Chair.
- Japan's Stewardship Code was finalized a little earlier in 2014 and it also corresponds with the OECD principles' newly introduced chapter on institutional investors.
- Therefore, Japan's codes and the OECD principles are mutually coordinated, and Japan's codes are completely consistent with the OECD Principles.

(Japanese Stewardship Code and Corporate Governance Code)

- Japan's Stewardship Code and CG Code work together like the two wheels of a cart and realize a virtuous economic cycle through constructive dialogue between institutional investors and companies, and ultimately lead to the growth of the economy as a whole.

(Overview of Japanese CG reform (1))

- Let me briefly touch upon the history of the recent Corporate Governance Reform by the Japanese Government.
- The Japanese CG reform has been strongly promoted by the present administration. Among the three arrows of "Abenomics", the economic growth strategy package, first priority is put on structural reform, among which CG reform has been one of the top agenda items.
- The first growth strategy of Abenomics published in 2013 stipulates the establishment of principles for institutional investors. Following that, we formulated the Stewardship Code in February 2014.
- Then the Corporate Governance Code was entered into force in June 2015, following the revised growth strategy in 2015.

(CG Reform Progress in Japan (1))

- So far this reform has shown significant progress. Just 2 examples.
- The CG Code has been accepted smoothly by listed companies. Over 80% of all listed companies comply with more than 90% of the principles.
- The number of "full compliance" companies doubled from 216 to 504 since our last meeting in Laos.

(CG Reform Progress in Japan (2))

- Independent Directors substantially increased. Almost all large companies now have at least one independent director.
- And companies with two or more independent directors more than tripled over the last three years.

(Overview of Japanese CG reform (2))

- Although we have seen good progress in CG reform, we consider that we need to continue to monitor and improve CG to achieve reform in substance, not as a mere formality.
- For this purpose, we have established the Follow-up Council for both the Stewardship and CG Codes in August 2015. It has discussed various issues about the role of the board and stewardship responsibilities.

(The results of the Follow-up Council discussion)

- Regarding the role of the board, the council identified the following necessary elements for achieving sustainable corporate growth, namely:
  1. Objective, timely and transparent appointment and dismissal of CEOs,
  2. Independent and objective board compositions,
  3. Board operations emphasizing strategies, and
  4. Continuous evaluation of the board's effectiveness.

- It also pointed out the need for reform on stewardship engagement activities by investors and that asset managers and asset owners should recognize and improve their stewardship roles in the investment chain to promote improvement of CG and long term growth of companies.

- Following these suggestions, the group of experts considered a revision of the stewardship code, the draft of which is now under a public comment process. I would like to introduce the essence of the draft although these may be altered after the public comment.

(Effective stewardship activities by institutional investors within a virtuous cycle)

- This slide is to illustrate how a virtuous cycle will work between investors, corporations and households when they all fulfil their appropriate function. Ultimate beneficiaries, namely households, will mandate their assets to asset owners such as pension funds. The asset owners often also mandate assets to asset managers.
- If these asset managers will have constructive dialogues with investee companies, it will help company managers to make the right business judgement with regard to taking appropriate risk from a mid- to long-term perspective. Together with monitoring by the board, this will support mid- to long-term corporate value and returns, which will eventually benefit households.

(Main topics in the Stewardship Code update (1) (Asset Owners))

- So, first on asset owners. Since asset owners, consisting of mainly public and corporate pension funds, have significant investment in Japanese stock through various asset managers, they have an influence and thus responsibility to monitor asset managers in place of the ultimate beneficiaries. In order to fulfil fiduciary duty to the ultimate beneficiaries, asset owners should:

- 1st, Conduct effective stewardship activities,

  It is desirable that asset owners directly engage in dialogues with corporations. If not, they should encourage asset managers to do so.

- 2nd, Clarify what asset owners expect from asset managers vis-a-vis stewardship activities,

  Asset owners should set their own policies when choosing and contracting asset managers. They should not simply endorse asset managers' policies.

- 3rd, Conduct effective monitoring of asset managers' activities.

  Asset owners should monitor whether asset managers follow the asset owners' policies. The owners may well utilize the asset managers' self-evaluation.

(Main topics in the Stewardship Code update (2) (Asset Managers))

- Second, on asset managers. Asset managers are direct counterparts of corporations and thus are expected to carry out effective stewardship activities with deep knowledge of corporations and a long-term perspective.
- In order to fulfil their fiduciary duty to asset owners, asset managers should:

- 1st, Improve governance and manage conflicts of interest,

- 2nd, Possess appropriate management capabilities and experience to fulfil stewardship responsibilities,

  Asset management subsidiaries or departments may face conflicts of interest in proxy voting if the investee companies are clients of their companies or parent companies. They may, for example, set and disclose their policies on managing conflicts of interest.

  Also, they should have the capabilities and experience needed to fulfill their responsibilities, and not simply follow a financial group's preference or voting advisory firms' advice.

- 3rd, Improve proxy voting result disclosure,

  Asset managers often disclose their voting results in an aggregated form by theme. However, in order to improve transparency, asset managers should disclose individual voting results.

- 4th, Engage actively in index funds

  Index investment accounts for 77% of all equity investment. The ratio of index investment has increased over the last three years.

  Along with the increasing importance of index investment, index funds should conduct engagement activities more proactively since they need to hold shares for a long time.

  On the other hand, as index funds have a lot of companies on their portfolio and generally do not have enough resources for engagement, the need for appropriate and effective screening has also been pointed out.

- 5th, Conduct self-evaluation and disclosure of status of stewardship activities

  To continuously improve their own governance structure, asset managers are encouraged to regularly self-evaluate and disclose how they carry out the stewardship code. It will also help asset owners to evaluate and choose asset managers.

- In addition, there are some other new factors which are now explicitly mentioned in the draft revision. I'll take up three points.

- 1st, Collective engagement:
  As one possible method for "constructive engagement" with investee companies, it explicitly states that it would be beneficial for institutional investors to engage with investee companies in collaboration with other institutional investors as necessary.

- 2nd, Proxy advisors:
  It also explicitly mentions what is desirable for proxy advisors as institutional investors often utilize their services. It states that proxy advisors should dedicate sufficient management resources to ensure sound judgement in the evaluation of companies and furnish their services appropriately, keeping in mind that the principles of the Code, including guidance, apply to them.

- 3rd, ESG:
  It also mentions ESG factors explicitly, pointing out not only risks but opportunities arising from social and environmental matters.

- So Japanese experience of CG shows strong consistency with the G20/OECD CG principles and continuing efforts to further improve the framework towards more effective implementation.

Thank you.