



Transition Finance in Japan and in Asia

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Hideki TAKADA

Director for Strategy Development

Financial Services Agency

Government of Japan

hideki.takada@fsa.go.jp

Sustainable finance developments in Japan

1. Promoting disclosure

- ▶ Sustainability disclosure in corporate financial reporting (from Mar 2023)
- ▶ Introduce Japanese version of “S1” and “S2” (draft by Mar 2024)

2. Enhancing transparency of ESG markets

- ▶ The Code of Conduct for ESG evaluation and data providers (Dec 2022) endorsed by 21 providers so far
- ▶ Supervisory guidelines for ESG investment trusts (Mar 2023)

3. Financing transitions

- ▶ Transition finance guidelines and roadmaps for hard-to-abate sectors
- ▶ Issuance of the world’s first sovereign transition bond (Feb 2024)

4. Promoting impact investment

- ▶ Draft basic guidelines for impact investment (Jun 2023)
- ▶ Establishment of the “Impact Consortium” of stakeholders (Nov 2023)

FSA website on sustainable finance

<https://www.fsa.go.jp/en/policy/sustainable-finance/sustainable-finance.html>

Japan's Policy for Realisation of GX (Green Transformation)

(“GX Promotion Strategy”: July 2023)

- ▶ Realise JPY150tn of public and private investment over the next 10 years
- ▶ Upfront government investment of JPY20tn raised by issuance of the world's first sovereign transition bond: “Japan Climate Transition Bond” starting from Feb 2024
- ▶ Introduction of carbon pricing to give incentives for GX investment and secure financial resources to repay GX Bonds
 - (1) Emissions trading system [from FY2026] + Allowance auctioning for power generation companies [from FY2033]
 - (2) Carbon levy on fossil fuel importers [from FY2028]
- ▶ Mobilise sustainable finance in innovative ways

Japan Climate Transition Bond Framework

- When issuing transition bonds that have received a third-party SPO, it is important to formulate a "framework" that summarizes Japan's transition strategy and the use of funds based on it, and to demonstrate to the market the eligibility and reliability of transition bonds.
- **On November 7, the government released the Climate Transition Bond Framework.**

(1) Items in the framework (based on ICMA Standards)

- ✓ **Issuer's transition strategy**
- ✓ **Use of proceeds**
- ✓ **Management of proceeds**
- ✓ **Reporting** (Allocation reporting + Impact reporting)

<Japanese>



<English>



(2) Decision making process for the formulation of the framework

- **Ministries and Agencies Liaison Conference on GX Economy Transition Bond Issuance**
- **GX Implementation Council (chaired by the Prime Minister)**

Second Party Opinions

Two external reviewers, **DNV** and **JCR**, confirmed that **the Climate Transition Bond Framework aligns with international standards** such as the Green Bond Principles and the Climate Transition Finance Handbook published by ICMA.

[Ref] Certification by the Climate Bonds Initiative



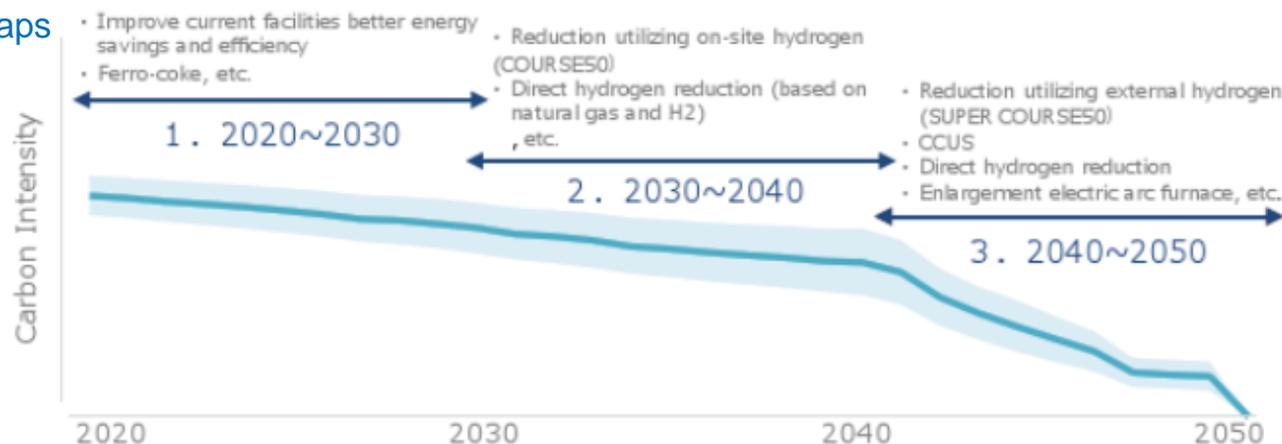
Sean Kidney, CEO, Climate Bonds Initiative, said:
“This bond shows clearly how governments, and others, can raise funds to invest in that transition. It marks a significant milestone in transition finance.”

Source: CBI Press Release

Transition finance: basic concept

- “Green finance” applies to low-carbon projects / technologies.
 - However, industries that are currently high-emitting must also be decarbonised in order to achieve a decarbonised society.
 - It is essential to provide finance for such industries to support their “transition” and achieve decarbonisation of an entire economy / society.
 - The Japanese Government (FSA, METI, MOE) published Basic Guidelines on Climate Transition Finance in May 2021 which require an **entity-wide transition strategy**. **Sector roadmaps** are prepared for hard-to-abate sectors (iron & steel, chemicals, electricity, gas, oil, cement, paper & pulp, shipping and aviation).
- ⇒ **sector- and entity-based approach (vis-à-vis project approach)**
- **Transition Finance Follow-up Guidance** was published in June 2023 to promote **continued dialogues** between financiers and fundraisers

Sector Roadmaps
(image)



Transition finance: key points

- ▶ Transition finance focuses on **high-emitting, hard-to-abate sectors**.
- ▶ The recipient of transition finance needs to establish an **entity-wide transition strategy** towards **future decarbonisation**.
- ⇒ **Sector and entity-based approach** (vis-à-vis project based approach)
- ⇒ Transition finance is a **dynamic (forward-looking)** concept (vis-à-vis static concept)
- ▶ Transition finance is **not (must not be)** “compromised green finance”
- ⇒ Needs **rigorous strategy** and **credible pathways**

Private sector initiatives

- ▶ **GFANZ (Glasgow Financial Alliance for Net Zero)**
- ▶ Net Zero Banking Alliance (Japan:6)
- ▶ Net Zero Asset Owner Alliance (Japan:5)
- ▶ Net Zero Asset Managers Initiative (Japan:12)
- ✓ **GFANZ Japan Chapter**, the first country-specific branch of GFANZ, was launched in June 2023.
- ✓ Japanese FIs are very active in GFANZ (e.g. MUFG chairs the Transition Finance work track of NZBA).
- ✓ NZBA published a Discussion Paper on transition finance metrics (Dec 2023).

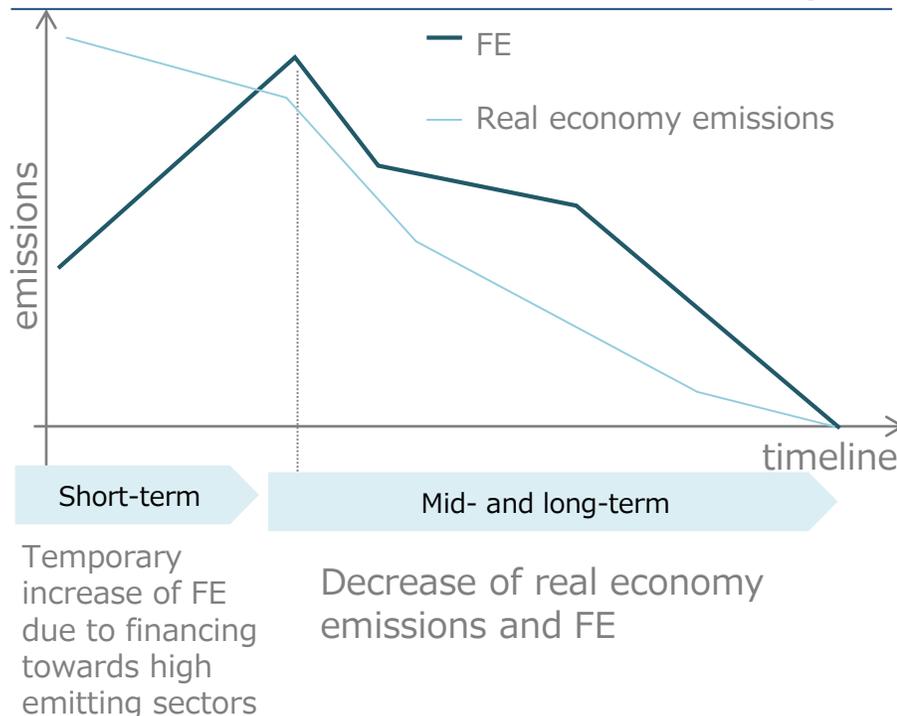
Asia GX Consortium

- ▶ The **Asia GX (Green Transformation) Consortium** was kicked-off to accelerate transition finance in Asian countries.
- ▶ The Consortium will, as a start, gather case studies of transition finance in Asia.
- ▶ The Consortium includes, as a start:
 - ✓ Japan FSA
 - ✓ Private financial institutions (MUFG, Mizuho, SMFG)
 - ✓ Public financial institutions (DBJ, JBIC, JICA)
 - ✓ International bodies (ADB, ASEAN, GFANZ)

Financed Emissions Paper (Released Oct. 2, 2023)

- If investors and FIs are evaluated only by the GHG emissions of their portfolio (financed emissions), they may choose to refrain from further investment (or divest) from hard-to-abate industries, regardless of the status of the portfolio companies' efforts to achieve net zero emissions.
- Calculation/Disclosure metrics must properly reflect the investor/FI's efforts to net zero. The paper covers various potential approaches.

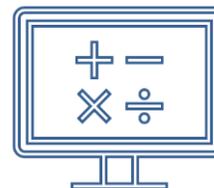
Relationship between Financed Emissions and Emission Reduction in Real Economy



Potential Approaches



- ① **Adjusting methods to calculate/disclose FE**
e.g. disclose FE related to transition finance separately



- ② **Utilizing multiple metrics**
 - Metrics on contributions to real economy transition
e.g. Avoided Emissions
 - Metrics on FI's capability / commitment for decarbonisation

◆ Metrics on contributions to real economy decarbonisation

- Avoided emissions
- Amount or proportion of portfolio aligned with net-zero
- Temperature ratings
- Amount or proportion of finance to companies with transition strategies
- Future reduction effects
- Physical indicators e.g. the generation capacity of RE financed

◆ Metrics on FI's capability / commitment for decarbonisation

- Amount of portfolio covered by key climate policies
- Amount of products and services aligned to net-zero
- Amount or proportion of portfolio companies with climate-related activities
- Number or proportion of employees and board members involved in climate related affairs