PROVISIONAL

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"Achieving net zero: Going beyond the hype and delivering on the goals"
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Keynote Speech

A time to deliver: What are the next steps to ensure that net zero goals are achieved?

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1. Introduction

- Thank you for your introduction. I am Yoshio Horimoto, the Vice Commissioner of the Financial Services Agency (FSA). Thank you for giving me the opportunity to make a keynote speech today at Moral Money Tokyo.

- The international community is making a major shift toward today's theme, the achievement of "Net Zero". More than 150 countries have set a target toward "Net Zero." Japan is no exception. Two years ago, the Government of Japan set its target for carbon neutrality by 2050 and has been accelerating economic, social, and industrial reforms. During these reforms, the importance of finance has been growing to leverage our government's effort to expand economic and social activities for Net Zero in Japan.

- Today, I would like to answer Inagaki-san's questions, by using three key phrases: first, the importance of innovation to achieve both carbon neutrality and growth; second, public-private partnerships for building financial infrastructure; and third, dialogue among financial institutions, investors, and corporations.

2. The Japanese government estimates that more than 150 trillion yen in public and private investment will be required in the next 10 years in order to achieve decarbonization by 2050. How will the government create a framework to promote private investment for green transformation?

□ In July this year, the Government of Japan established the "GX Implementation Meeting" chaired by the Prime Minister Kishida, and plans to publish a 10-year roadmap for this 150 trillion yen investment by the end of this year. While the specific content of the roadmap is still under discussion, it will include five policy initiatives, which spans government, industry, and financial initiatives.

□ Among them, four of them are domestic policies.

□ First is the establishment of the GX Economic Transition Bonds (tentative name), which will be used to raise the necessary government funds, estimated to be 20 trillion yen, in advance of the public and private investments required for GX, and to use these funds to attract private capital. At the same time, the Japanese "Growth-Oriented Carbon Pricing" is also being considered.

□ Second, in order to attract private investment for decarbonization, it is necessary to establish a mechanism to increase the predictability of the return on long-term investment. For example, the recent revision of the Energy Conservation Law requires a new shift to non-fossil energy sources, which may lead to new private investment. We are considering such policy mix of regulations and support.

- Third, we are preparing for the establishment of the so-called GX League for companies that are actively engaged in GX. This GX League will be an opportunity for a group of these companies to discuss their initiatives and practice the creation of new markets. In connection with this, on the Tokyo Stock Exchange, a technical demonstration of carbon credit market was launched last month. In the future, voluntary emissions trading by GX League participants will also be included in this market.

- The fourth point is, as mentioned in the questions, the mobilization of the remaining 130 trillion yen of private funds, excluding the necessary government funds estimated to be 20 trillion yen raised through the GX Economic Transition Bonds. In this regard, we believe that utilization of “new financial method” will be important such as transition finance and innovation finance.

- For this purpose, three authorities, the Ministry of Economy, Trade and Industry, the Ministry of the Environment, and the FSA are working together to discuss systems and environmental improvements, such as:
  - Enhancing government support, such as improving the subsidy program for issuing green bonds.
  - Developing a sector-specific roadmap to facilitate transition financing for high emission companies.

- Establishing a new cooperative scheme to encourage innovation finance in the area of decarbonization, for the purpose of sharing information and discussing risk sharing among industrial companies including startups and private and government financial institutions.

The FSA will continue to strengthen public-private partnerships and consider various initiatives to promote sustainable finance.

3. *The FSA is undertaking various initiatives to promote sustainable finance. What are the current challenges facing Japan?*

- The FSA established the Expert Panel on Sustainable Finance in December 2020 to discuss how domestic and overseas growth capital can be used to realize a decarbonization society in Japan. After one and a half years of discussions, the Panel published its secondreport presenting several challenges. Today, I will explain four of them: enhancement corporate disclosure, stronger market functions, risk management by financial institutions, and impact investment.

1) <u>Enhancement of corporate disclosure</u>

- Appropriate corporate disclosure of sustainability information that contributes to investment decisions is the key for companies' constructive dialogue with investors and financial institutions regarding opportunities, risks and strategies.

- It should be as internationally comparable as possible, and for this reason, cooperation with the international community is also important.

- ☐ First, regarding disclosure on climate change, we revised the Japanese Corporate Governance Code in June last year to urge companies listed on the Tokyo Stock Exchange Prime Market to improve the quality and quantity of disclosure. This disclosure should be based on the Task Force on Climate-related Financial Disclosures (TCFD) or an equivalent international framework.

- ☐ In addition, in the mandatary securities report, a new section will be created for the disclosure of sustainability information, including information on climate change. We aim to amend relevant ordinance by the end of this year and begin to apply it from the fiscal year ending March 2023.

- ☐ In July this year, the Sustainability Standards Board of Japan (SSBJ) was established for the purpose of providing input and contributing to discussions on the formulation of international disclosure standards by the International Sustainability Standards Board (ISSB). In the future, the SSBJ will also consider the detail contents of sustainability disclosure in Japan.

2) <u>Stronger Market functions</u>

- ☐ The second challenge is enhancing market functions. In order for the sustainable finance market to develop soundly, it is important that each player in the market, such as investors, asset management companies, and ESG evaluation organizations, fulfills their expected roles.

- ☐ The first issue to be raised is the development of market infrastructure. In July this year, Japan Exchange Group, Inc. (JPX) launched an information platform that consolidates ESG investment information. The platform first targets publicly offered ESG bonds and consolidates (1) basic information, such as issuance amounts and interest rates, (2) management and ESG strategies of issuing companies, and (3) external evaluations of publicly offered ESG bonds. Expansion of the platform is also under consideration.

- ☐ Next, as ESG investment expands, regarding ESG evaluation organizations the use of which by companies and investors is rapidly growing, the transparency and fairness of ESG evaluation methods as well as governance such as the prevention of conflicts of interest may become issues. Therefore, we published a draft of the "Code of Conduct for ESG Evaluation and Data Providers" in July this year. We aim to finalize the Code of Conduct by the end of this calendar year and publish the status of endorsement by each ESG evaluation organization by the end of this fiscal year. This Code not only applies to such evaluation organizations, but also covers the role of investors who use evaluations and data as well as companies with regard to provision of ESG evaluation and data. Please refer to these documents.

- ☐ In addition, this fiscal year, the FSA would like to start to understand the challenges they face in improving the value of assets in trust and to share this information with stakeholders, focusing on efforts by asset owners to improve companies' sustainability.

3) <u>Risk management by financial institutions</u>

- ☐ The third challenge is risk management and demonstrating the roles of financial institutions.

- ☐ In particular, in recent years, there has been a further increase in momentum for mobilizing private capital and for private financial institutions to play a role in facilitating the transition to net zero for society as a whole.

- ☐ As the shift in industrial structure associated with the transition to decarbonization can be a business risk for their client companies, climate-related risks can have a significant impact on financial institutions. Therefore, it is important for financial institutions to manage their own climate-related risks. Compared to traditional risk management and financial policies, climate-related financial risks are pointed out to be long-term, highly uncertain, and non-linear. For this reason, it is important for financial institutions to set various forward-looking scenarios for their own and their clients' businesses and consider how to respond.

- ☐ Last year, the FSA and the Bank of Japan, in collaboration with the three major banks and the three major non-life insurance groups, conducted a pilot exercise on scenario analysis by using the scenarios published by the Network for Greening the Financial System (NGFS). We will continue to discuss with financial institutions how to resolve issues that have emerged from the pilot exercise, such as lack of sufficient data as well as the appropriateness of analytical assumptions and methods.

4) <u>Promoting impact investments</u>

- ☐ Finally, the expansion of an investor base for sustainable finance is also an important issue. In this regard, it is expected that there will be an increase in so-called "impact investments" that aim not only to secure investment returns but also to solve social issues. In Japan, the total amount of "impact investments" is also on the rise, but its scale is still small compared to other developed countries, and its further expansion is a challenge.

□ To this end, the FSA will establish a working group on impact investment under the Expert Panel on Sustainable Finance in order to:

- Analyze the relationship between investment returns and social benefits by each sector and classify impact investments; and
- Consider a kind of practical guideline for selection of target projects, measurement of social benefits, and disclosure when raising funds.

Through this work, we intend to consider specific promotional measures to attract various investors to impact investing.

4. In order to achieve the Net Zero target, it is essential for companies and financial institutions to work together. How will the Government promote collaboration here?

□ As I mentioned earlier, expectations for global financial sector movements toward decarbonization are accelerating. In order for financial institutions to achieve Net Zero in their portfolios, it is important for financial institutions to provide support to their clients so that they can appropriately respond to risk and new business opportunities.

- This is because whether financial institutions’ portfolio companies can adapt to changes in business environment with regard to climate change and transition to a decarbonized society also gives an impact to their own business. In other words, supporting their clients to adapt to climate change not only reduces their risk, but also provides themselves with the opportunities to secure stable revenues.

- Particularly, for companies with high emissions, such as electric power and steel companies, it is not realistic to make the transition to carbon neutrality overnight. For the medium-to-long term transition, it is essential for financial institutions and investors to keep dialogue and engagement with companies, not simply divesting their funds.

- Furthermore, for small and medium enterprises, an approach by regional and local financial institutions is also important.

- From this perspective, the FSA published guidance titled "Supervisory Guidance on Climate-related Risk Management and Client Engagement" in July this year. This guidance is intended to be used in dialogues between the FSA and financial institutions, and summarizes the viewpoints of those supervisory dialogues, with regard to the key points and procedure of the financial institutions’ climate-related risk management and their support for client companies addressing climate change.

- At the same time, international momentum to promote such a transition that brings together financial institutions and companies is increasing ahead of COP27 and the G20 Summit that will be held next month. The recommendation of the report, which is currently being finalized by the G20 Sustainable Finance Working Group, will include measures to develop a framework for transition financing and improve the credibility of financial institutions' commitments.

- ☐ We think that the understanding of the importance of transition and engagement by financial institutions has deepened conceptually. On the other hand, the challenge is how to accelerate the implementation of such practices for both financial institutions and companies.

- ☐ Therefore, the FSA decided to establish a Working Group under the Expert Panel on Sustainable Finance to contribute to the formulation and steady implementation of transition planning by companies and financial institutions. This WG will deepen discussions on:
  - ➢ Points to keep in mind for financial institutions and investors when engaging in dialogue with companies toward decarbonization; and
  - ➢ Practical issues and best practices, especially for regional and local financial institutions, to support SMEs toward decarbonization

  We would like to have a deep discussion among experts consisting of investors, financial institutions, companies, and academics to encourage dialogues with financial institutions and companies and to promote transition finance.

- ☐ The newly-established Working Group is scheduled to begin next week. First, we will strengthen the sharing of domestic awareness of international trends and actual examples related to transition. But we also should keep in mind that a one size–fits-all approach is not appropriate. Depending on the size and characteristics of financial institutions, we will advance discussions on ideal forms of dialogue and engagement by financial institutions.

5. Conclusion

- Climate change and other sustainability issues are globally common, and require continuous efforts across national borders and public-private boundaries. On the other hand, geopolitical risks and soaring energy prices are currently forcing each country to address both the stable supply of energy and the maintenance of economic growth as well as decarbonization in the medium term. Amid this situation, there are concerns about the slowdown of decarbonization.

- However, from the beginning, the transition policy of the Japanese government has been aimed at realizing both economic growth and a sustainable society while taking advantage of the strengths of capitalism. This is an approach that Prime Minister Kishida asserted in his speech at the New York Stock Exchange by linking it to professional baseball player Shohei Ohtani's "two-way performance." Innovation is important to achieve these two goals.

- For this innovation, the wisdom of the private sector and innovative activities are the key. Therefore, we should not only discuss our plans within our government, but also share our goals and information with the private sector support innovative economic business, and embed decarbonization efforts in actual business activities. It is also important for us to promote trial and error as well as accumulation of actual practices in various private businesses.

□ I believe that strengthening such public-private partnership is today’s theme, the important next step to ensuring the net-zero goals.

□ I would like to conclude my remarks by expressing my hope that the discussions at today's conference by investors, companies, the media, and officials will contribute to further coordination on the journey to achieving Net Zero.

□ Thank you very much.