JSIF

White Paper on Sustainable Investment in Japan 2015

Japan Sustainable Investment Forum

About the Organization

Japan Sustainable Investment Forum (JSIF) started its activities in early 2001 to promote socially responsible investment (SRI) in Japan and was formally registered as a non-profit organization (NPO) in 2003.

JSIF's Sustainable Investment Standards

JSIF defines "sustainable investments" as investments that embody the following two principles:

1. Investments with a view to the sustainability of the earth and society;
2. Investments supported by the disclosure of initiatives pertaining to Principle 1 and the social effects of these investments to suppliers of capital.

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Foreword

The Japan Sustainable Investment Forum (JSIF), which upholds the proliferation of Japanese sustainable investment as its mission, has been engaged in the publication of biennial reports to describe Japanese market trends. We are pleased that in this report, which marks its fifth publication, we have been able to show significant changes toward the growth of sustainable investment markets in Japan.

To date, reports have shown that balances with a focus on individual investors, represented by eco funds and socially responsible investment (SRI) funds, along with impact bonds, have fallen shy of ¥1.0 trillion. This time, however, JSIF was able to observe a genuine commitment to sustainable investment by pension funds and institutional investors, sparked by a series of groundbreaking events occurring over 2014 and 2015: Japan's Stewardship Code was introduced, and the Government Pension Investment Fund (GPIF) became a signatory of the Principles for Responsible Investment (PRI). In fall 2015, JSIF conducted the first sustainable investment survey in Japan aimed at institutional investors.

Responses were received from 28 of the 59 institutions that were asked to participate in the survey. The survey clarified the level of Japan's total sustainable investment balance to ¥26.7 trillion from 24 institutions. As of December 2015, the number of Japan's Stewardship Code signatories had increased to 201 organizations, entities, or institutions. Thus, we assume that the actual sustainable investment figure should exceed this amount. This report describes the content of the survey and provides a concrete outline of sustainable investment initiatives established by institutional investors. We can also observe the influence of such trends on the behavior of shareholders.

In accordance with changes in the circumstances surrounding these markets, the title of this report has been updated, from *Review of Socially Responsible Investment in Japan* to *White Paper on Sustainable Investment in Japan.* Moreover, the report examines not only the progressive movement of large sums of money held by institutional investors toward sustainable investment, but also the movement of smaller sums held by individuals through participation in such initiatives as community investment and crowdfunding. The report also shows the active proliferation of sustainable investment in asset classes separate from equity and bonds, such as green real estate and private equity.

This report includes voluntary contributions from some of Japan's leading experts in various fields. It provides not only statistical market data, but also detailed explanations of circumstances pertaining to these markets. Accordingly, it represents an excellent reference material to aid the reader in understanding the circumstances surrounding various forms of sustainable investment.

2016 commenced with a rocky start as global equity markets continued to plummet. Like the 2008 financial crisis, initial confusion has subsided and, as speculative movements reach a plateau, movements to restore value in equity and bonds have begun to materialize. We believe, however, that the significance of long-term sustainable investment, which upholds the advancement of society as one of its objectives, will be brought into the forefront going forward. In this pressing environment, it is the sincere hope of those who participated in the publishing of this report and JSIF members that it be utilized as a reference when making investment decisions.

We would like to use this opportunity to express our gratitude to Edge International, Inc., for its collaboration in the translation and the production of this report in support of this mission and our enthusiasm. We would also like to thank Ernst & Young ShinNihon LLC and the Development Bank of Japan Inc. for their continued support.

Furthermore, we would also like to extend our gratitude to the investment management institutions and pension funds that cooperated with us in responding to the survey, the main feature of this report.

Finally, we would like to thank our 35 corporate members and 67 individual members for their day-to-day support of JSIF's activities. In addition to our gratitude for their encouragement thus far, we ask for their further support of JSIF's initiatives to bring Japan's sustainable investment into the mainstream.

January 2016

Mariko Kawaguchi
Co-CEO
Japan Sustainable Investment Forum

JSIF Conducts Japan's First Survey Pertaining to the Total Sustainable Investment and ESG Investment Balances of Institutional Investors

According to JSIF totals, the total sustainable investment and ESG investment balances of Japanese institutional investors amount to ¥26.7 trillion and ¥17.5 trillion, respectively.

Since its establishment in 2004, the Japan Sustainable Investment Forum (JSIF) has been regularly calculating Japan's sustainable investment balance and publicizing this information both domestically and overseas. Until recently, the scope of these totals was limited to publicly available figures pertaining to SRI investment trusts and social impact bonds. For a long time, disclosure initiatives pertaining to sustainable investment by institutional investors, including pension funds, were limited, and balances were not publicized. It was therefore not possible to reflect such investments in our calculations.

However, in February 2014, the Principles for Responsible Institutional Investors (Japan's Stewardship Code) were established and, as of December 11, 2015, 201 institutional investors have declared adoption of these principles. Moreover, with the announcement of the Corporate Governance Code in June 2015, ESG and sustainable investment by institutional investors in Japan is anticipated, in addition to ramped up engagement with corporations. Further, in September 2015, the Government Pension Investment Fund (GPIF)—the world's largest pension fund—became a signatory of the Principles for Responsible Investment, which has garnered attention from overseas since its announcement by Prime Minister Abe at the UN Summit.

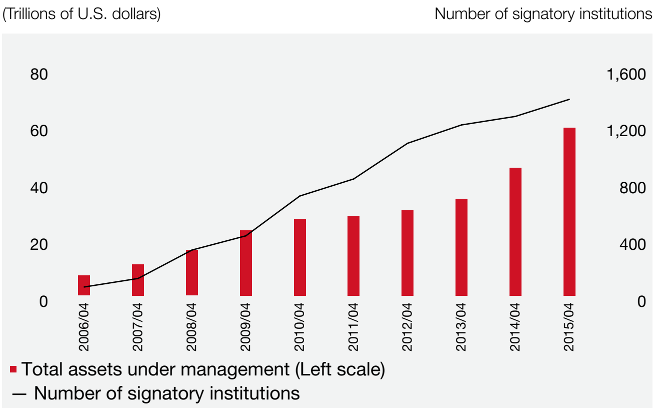
The global sustainable investment balance for 2014 amounted to $21.36 trillion, a rise of 61% from the 2012 figure of $13.26 trillion. Within this amount, there has been a rapid expansion in ESG investment (ESG integration), which has grown 78% from 2012, to $12.85 trillion, and engagement and the exercising of voting rights related to ESG, which has grown 53%, to $7.05 trillion (*Global Sustainable Investment Review 2014*).

Signatories of the UN's Principles for Responsible Investment (PRI), an initiative to promote ESG investment worldwide, totaled 1,453 as of January 11, 2016 (breakdown: asset owners: 301; investment managers: 954; professional service partners: 198), with combined total assets under management of over $59.0 trillion.

	Worldwide	Japan
PRI signatory institutions	1,453	39
Asset owners including pension funds	301	9
Asset management companies	954	23
Information service providers	198	7

Number of PRI signatory institutions and assets under management (as of April 2015)

Total assets: over $59.0 trillion Annual increase of 29%



Source: Produced by JSIF based on PRI data

Furthermore, 12 of the 20 largest pension funds in the world are engaged in ESG investment, and the total assets held by those 12 funds represent 72% of the total assets under management by all 20 (calculated by JSIF based on *P&I/TW 300 Analysis Year End 2014* and PRI data).

Twelve of the 20 largest investment funds in the world are engaged in ESG investment. The proportion of total assets held by those 12 is 72%.

	Fund	Country	Total assets
1	Government Pension Investment	Japan	$1,143,838
2	Government Pension Fund	Norway	$884,031
3	National Pension	South Korea	$429,794
4	Federal Retirement Thrift	U.S.	$422,200
5	ABP	Netherlands	$418,745
6	California Public Employees	U.S.	$296,744
7	National Social Security	China	$247,361
8	Canada Pension	Canada	$228,431
9	PFZW	Netherlands	$215,006
10	Central Provident Fund	Singapore	$207,872
11	Local Government Officials	Japan	$194,696
12	California State Teachers	U.S.	$186,954
13	Employees Provident Fund	Malaysia	$184,697
14	New York State Common	U.S.	$178,252
15	New York City Retirement	U.S.	$158,702
16	Florida State Board	U.S.	$154,657
17	Ontario Teachers	Canada	$133,282
18	Texas Teachers	U.S.	$128,933
19	GEPF	South Africa	$123,204
20	ATP	Denmark	$122,028

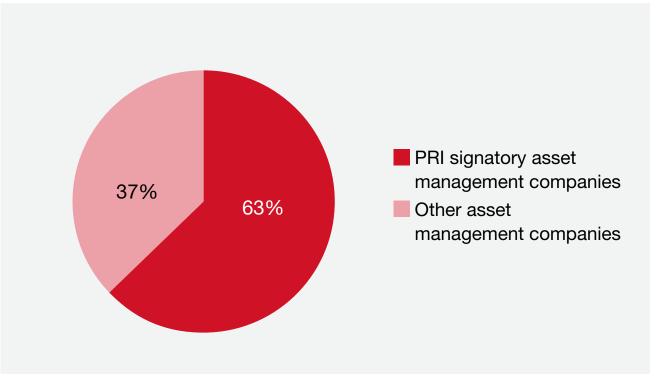
PRI signatories　Engaged in ESG investment but not a PRI signatory

Source: Produced by JSIF based on *P&I/TW 300 Analysis Year End 2014* and PRI data

For 2014, total assets under management by asset management companies that are signatories of PRI accounted for 63% of investment by asset management companies worldwide (PRI data).

Signatories of PRI manage 63% of the assets under management by asset management companies worldwide.

	Market scale: trillions of U.S. dollars (2014)	PRI signatory institutions: trillions of U.S. dollars (2014)	Estimated proportion accounted for by PRI signatory institutions
Asset management companies	74	46.3	63%



Source: Produced by JSIF based on PRI data

Looking at these figures, it is not an exaggeration to say that ESG investment has already become a mainstream concept worldwide. Bearing in mind the changing domestic and global environment that represents a backdrop to sustainable investment and ESG investment, JSIF considers the calculation and publication, both domestically and overseas, of balances that reflect the sustainable investment and ESG investment initiatives of Japanese institutional investors to be a matter of urgency. By requesting the cooperation of 59 institutions that have declared adoption of Japan's Stewardship Code with regard to clear disclosure of their departments responsible for compliance with the Code and participation in the survey, we were able to secure responses from 28 institutions.

This survey examines the status of Japan's sustainable investment, and aims to promulgate a correct interpretation of that status across the country and overseas. The results of totals calculated are to be posted on JSIF's website and announced at a conference jointly hosted with PRI Japan Network and at international conferences. The information will also be widely utilized by public institutions such as the Ministry of the Environment. Moreover, totals will now be calculated every two years, and we intend to reflect the results of the survey in the *Global Sustainable Investment Review*, an initiative started in 2012 through the cooperation of SIFs in countries around the world to calculate and publicize global sustainability investment balances. We hope that this survey will be a useful reference for domestic and overseas pension funds and other institutional investors, NPOs/NGOs, relevant authorities, and Japanese corporations to correctly grasp the status of sustainable investment and ESG investment in Japan and for promoting domestic initiatives such as sustainable investment, ESG investment, engagement, and information disclosure by corporations.

Pension funds and asset management companies that participated in the survey (28 companies in alphabetical order)

Of the 28 respondents, four requested that their group/company name not be published.

- Alliance Bernstein Japan Ltd.
- Amundi Japan Ltd.
- Asahi Life Asset Management Co., Ltd.

- Daido Life Insurance Company
- Daiwa Asset Management Co. Ltd.
- DBJ ASSET MANAGEMENT CO., LTD.
- DIAM Co., Ltd.
- Mitsui Sumitomo Insurance Company, Ltd.
- Mizuho Asset Management Co., Ltd.
- Mizuho Trust & Banking Co., Ltd.
- Nissay Asset Management Corporation
- NN Investment Partners (Japan) Co., Ltd.
- Pension Fund Association
- Resona Bank, Limited
- Robeco Japan Company Limited
- SECOM Pension Fund
- Sompo Japan Nipponkoa Asset Management Co., Ltd.
- Sompo Japan Nipponkoa Insurance Inc.
- SPARX Asset Management Co., Ltd.
- Sumitomo Mitsui Asset Management Company, Limited
- Sumitomo Mitsui Trust Bank, Limited
- TAIYO LIFE INSURANCE COMPANY
- T&D Asset Management Co., Ltd.
- Tokio Marine Asset Management Co., Ltd.

The following four groups/organizations cooperated with JSIF in circulating the survey:

- Principles for Financial Action for the 21st Century, Ministry of the Environment
- CFA Society of Japan
- FTSE Russell (London Stock Exchange Group)
- responsible-investor.com (Response Global Media Limited)

We also received many suggestions pertaining to survey content from the Japan Investment Advisers Association.

Summary of Survey Results

Outline of survey

- Focus period: November to December 2015
- Circulation and number of respondents: distributed to 59 institutions, responses received from 28

Total sustainable investment under management

¥26.69 trillion (24 institutions)

Proportion of total assets under management

11.4% (= 26,661,900 ÷ 232,084,235)

Note: Total assets under management calculated with the exclusion of one institution that did not disclose a figure

Classification of respondent institutions (asset owner/investment manager)

Asset owner	7
Investment manager	20
Asset owner and investment manager (both apply)	1
Total	28

Sustainable investment balance by management method

(¥ Million)

ESG integration	¥17,555,654
Positive (best in class) screening	326,955
Investments based on a theme of sustainability	785,785
Impact and community investment	87,642
Engagement/Use of voting rights	11,709,822
Negative screening	4,573,384
Screening based on international standards	6,075,200

Sustainable investment balance by asset class

(¥ Million)

Japanese stock	¥13,855,308
Foreign stock	2,962,942
Bonds	6,815,325
Private equity (PE)	643
Real estate	435,150
Other	1,147,630

Survey Results

Q1 Please enter the identification code accompanying the guide to this survey.

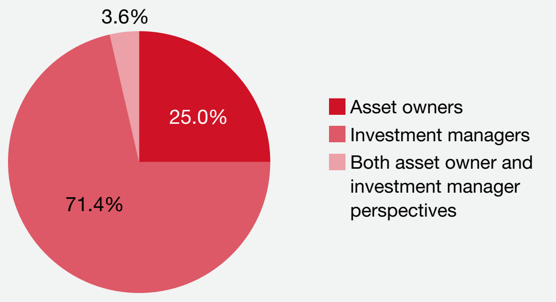
Option	Proportion of responses	Number of responses
Identification code	100.0%	28

Number of institutions that answered this question: 28/28

Q2 Please describe your role pertaining to capital management and capital structure.

Option	Proportion of responses	Number of responses
Asset owner	25.0%	7
Investment manager	71.4%	20
Asset owner and investment manager (both apply)	3.6%	1

Number of institutions that answered this question: 28/28

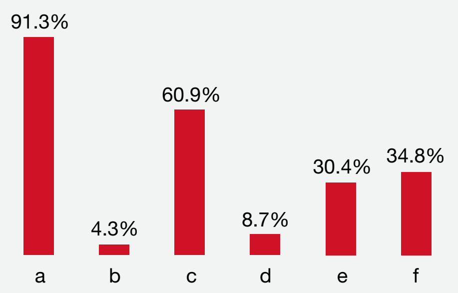


- Seven respondent institutions, or 25%, were asset owners; 20 respondents were investment managers, with a proportion of 71.4%; and one institution indicated that both categories applied.
- Four of the respondent institutions were foreign-affiliated Japanese corporations (all of which were investment managers).

Q3 Which of the following initiatives have you adopted or are involved in?

	Option	Proportion of responses	Number of responses
a	Principles for Responsible Investment (PRI)	91.3%	21
b	Equator Principles	4.3%	1
c	Principles for Financial Action for the 21st Century	60.9%	14
d	Principles for Sustainable Insurance (PSI)	8.7%	2
e	CDP	30.4%	7
f	Other (please specify)	34.8%	8

Number of institutions that answered this question: 23/28

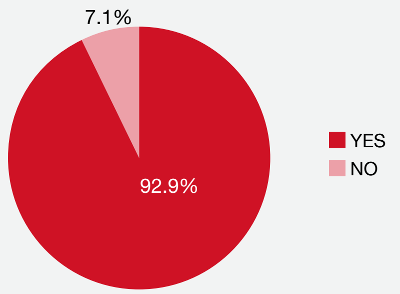


- Twenty-three institutions responded to the question pertaining to their involvement in the main domestic and international initiatives related to sustainable investment.
- Signatories of PRI, which promotes ESG investment internationally, represented the highest proportion, with 21 institutions (91.3%); 14 institutions (60.9%) were engaged in the domestic initiative Principles for Financial Action for the 21st Century; and signatories of CDP, which advocates disclosure of corporate initiatives pertaining to CO_2 emissions, water, and forests, totaled seven institutions (30.4%).
- Furthermore, eight institutions (all of which were investment managers) noted their participation in 24 differing activities both domestically and overseas, including IGCN, JSIF, UNEPFI, the UN Global Compact, and the Montreal Carbon Pledge.

Q4 **Have you declared adoption of Japan's Stewardship Code?**

Option	Proportion of responses	Number of responses
YES	92.9%	26
NO	7.1%	2
For institutions that answered YES, please include the URL of the IR website that describes policies related to each principle.		24

Number of institutions that answered this question: 28/28

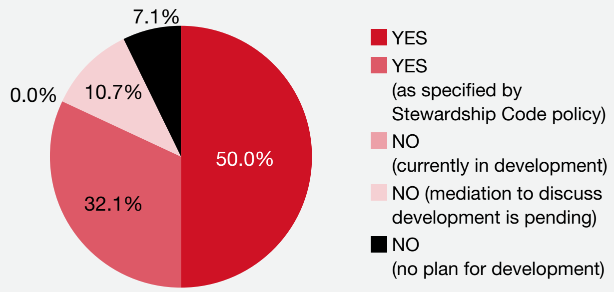


- The survey was conducted with a focus on signatory institutions of Japan's Stewardship Code; 26 respondents (92.9%) reported adoption of the Code.
- Of the two institutions that were not signatories of the Code, one was a domestic asset owner, and the other was an overseas investment manager.

Q5 **Do you have a formal policy pertaining to sustainable investment (ESG investment, responsible investment, SRI, impact investment, eco funds, etc.) specific to your organization?**

Option	Proportion of responses	Number of responses
YES	50.0%	14
YES (as specified by Stewardship Code policy)	32.1%	9
NO (currently in development)	0.0%	0
NO (mediation to discuss development is pending)	10.7%	3
NO (no plan for development)	7.1%	2

Number of institutions that answered this question: 28/28

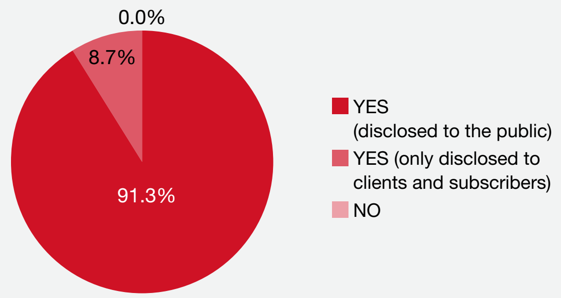


- Fourteen institutions (50%) indicated that they had a formal policy specific to their organization pertaining to sustainable investment, and nine institutions (32.1%) indicated that they incorporated policy as specified by Japan's Stewardship Code, for a total of 23 institutions (82.1%) that answered YES.
- Three institutions (10.7%), all of which were investment managers, indicated that mediation to discuss policy development was pending.
- Of the two institutions that indicated no plan for policy development, one was a domestic pension fund, and the other an investment manager.

Q6 **This is a question for institutions that answered YES to Q4 (pertaining to adoption of Japan's Stewardship Code). Are these policies publicized?**

Option	Proportion of responses	Number of responses
YES (disclosed to the public)	91.3%	21
YES (only disclosed to clients and subscribers)	8.7%	2
NO	0.0%	0
For those who answered YES (disclosed to the public), please provide a URL.		19

Number of institutions that answered this question: 23/28

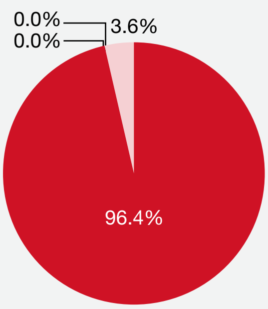


- In response to the question for institutions that have adopted Japan's Stewardship Code with regard to the publication of associated policies, 21 institutions (91.3%) indicated that they made this information available to the public, and two institutions indicated that they disclosed this information only to clients and pension subscribers. Therefore, 100% of respondents answered YES to the question and none of the respondents answered NO. Five institutions declined to respond.

Q7 Are you engaged in sustainable investment (ESG investment, responsible investment, SRI, impact investment, or eco funds)?

Option	Proportion of responses	Number of responses
YES	96.4%	27
NO (currently making preparations)	0.0%	0
NO (mediation to discuss implementation is pending)	0.0%	0
NO (no plan for implementation)	3.6%	1

Number of institutions that answered this question: 28/28

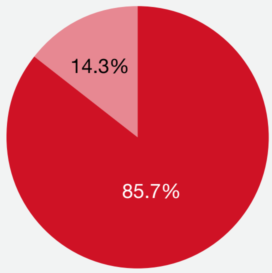


- Twenty-seven respondents (96.4%) indicated that they were engaged in sustainable investment. Only one institution indicated that it did not plan to implement sustainable investment. (This institution explained that it was not engaged in asset management in line with sustainable investment guidelines because analysts use this information as non-financial information to evaluate corporations.)

Q8 Are you able to disclose to us your sustainable investment balance under management?

Option	Proportion of responses	Number of responses
YES	85.7%	24
NO	14.3%	4

Number of institutions that answered this question: 28/28



- Twenty-four institutions (85.7%) indicated that they were willing to disclose their sustainable investment balance under management.
- Four institutions indicated that they were not willing to disclose this information. Of these respondents, two were asset owners, one was a domestic investment manager, and one was an overseas investment manager.
- Of the two asset owners that answered NO, one was a pension fund. The same fund was also not a signatory of PRI.

Q9 This question pertains to institutions that answered YES to Q8. Please tell us your total sustainable investment balance under management (to the nearest million yen).

(¥ Million)

Amount indicated (average)	Total of amounts indicated	Number of responses
¥1,111,969	¥26,687,256	24

Number of institutions that answered this question: 24/28

- Twenty-four institutions responded to the question pertaining to total sustainable investment balance under management, the combined sum of which amounted to ¥26.69 trillion.
- The average total for each institution was over ¥1.1 trillion.

Q10 Please tell us when the balance indicated in Q9 was recorded.

Amount indicated (average)	Total of amounts indicated	Number of responses
Date/month/year	100.0%	24
Number of institutions that answered this question: 24/28		

Q11 If possible, please tell us about your total asset balance under management at the same time the amount indicated in Q10 was recorded (to assess the proportion of total funds under management categorized as sustainable investment).

(¥ Million)

Amount indicated (average)	Total of amounts indicated	Number of responses
¥10,090,618	¥232,084,235	23
Number of institutions that answered this question: 23/28		

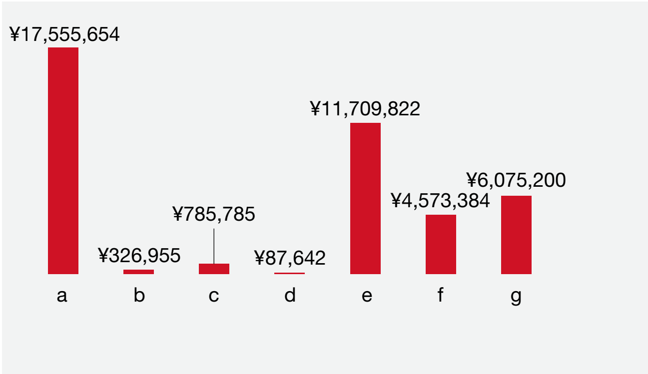
- Responses pertaining to total balance under management were provided by 23 of the institutions that responded to Q10, with the exception of one institution (a pension fund). The total of amounts indicated came to ¥232.08 trillion.
- 11.48% of the [combined] total balance under management was categorized as sustainable investment (calculated with the exclusion of the aforementioned pension fund).

Q12 If possible, please tell us about the proportion of the amount indicated in Q9 allocated to each of the asset management methods* listed below.

(¥ Million)

	Option	Amount indicated (average)	Total of amounts indicated	Number of responses
a	ESG integration	¥1,097,228	¥17,555,654	16
b	Positive (best in class) screening	29,723	326,955	11
c	Investments based on a theme of sustainability	78,578	785,785	10
d	Impact and community investment	14,607	87,642	6
e	Engagement/ Use of voting rights	975,818	11,709,822	12
f	Negative screening	762,230	4,573,384	6
g	Screening based on international standards	1,215,040	6,075,200	5
	Number of institutions that answered this question: 23/28			

(¥ Million)



Note: As multiple responses were received, figures are not aligned with the total for Q9 (¥26.69 trillion).

* Definitions of asset management methods:

a. ESG integration
Investment that systematically incorporates ESG (environment, society, corporate governance) factors in regular management processes

b. Positive (best in class) screening
Investment in selected sectors and corporations by using financial and ESG screening (e.g., eco funds, etc.)

c. Investments based on a theme of sustainability
Investments that reflect sustainability themes, including renewable energy, environmental technology, and agriculture (e.g., renewable energy funds, etc.)

d. Impact and community investment
Investment that prioritizes impact on society, the environment, and the community (e.g., vaccine bonds, green bonds, etc.)

e. Engagement/Use of voting rights
Working with corporations as a shareholder (including use of voting rights) based on ESG engagement policies

f. Negative screening
Abstention from investment in specific industries or corporations for ethical or religious reasons

g. Screening based on international standards
Investment based on international standards set in place by international institutions (OECD, ILO, UNICEF, etc.) (e.g., Oslo Convention —> abstention from investment in corporations affiliated with cluster munitions)

The definitions detailed above were deliberated at a meeting between the JSIF steering committee and members of the PRI Japan Network Working Group, with reference to definitions set out by the Global Investment Alliance (a global network of SIFs), Eurosif, and PRI.

- Twenty-three institutions responded to the question pertaining to the proportion of sustainable investment by asset management methods.
- ESG integration reflected the largest proportion, with a total of ¥17.56 trillion from 16 institutions.
- Engagement/Use of voting rights amounted to a total of ¥11.71 trillion from 12 institutions. Although some institutions indicated that this management method accounted for their entire sustainable investment balance, some institutions did not respond at all.

Caution from JSIF:
Although it is reasonable to assume that all institutions conduct engagement/use of voting rights to some extent, institutions that did not answer this question may have abstained from doing so due to reasons related to the extent of their initiatives and their fundamental beliefs pertaining to what constitutes engagement. (One of the reasons that engagement and use of voting rights are bundled into a single question is due to the fact that this survey used the classifications of global surveys as a reference point. However, for Japan, it may be more appropriate to treat these as separate categories in the future.)

- Negative screening amounted to a total of ¥4.57 trillion from six institutions, and screening based on international standards totaled ¥6.08 trillion from five institutions.
- Furthermore, impact and community investment amounted to ¥87.6 billion from six institutions; investments based on a theme of sustainability totaled ¥785.7 billion from 10 institutions; and positive (best in class) screening was ¥326.9 billion from 11 institutions.
- We can see that a wide range of sustainable investment initiatives are being implemented in addition to ESG investment. However, there is still a significant difference in the proportion of investments deemed sustainable when compared to overseas. We may assume that this is a reflection of the fact that there are differences between the historical and cultural backgrounds of every country and region.

SRI classifications and the rapid expansion of ESG investment
World SRI [totals] ¥21.4 trillion

($ Billion)

Classification	Outstanding amount
1 Negative screening	$14,389.5
2 ESG investment/ESG integration	12,853.7
3 Engagement/Use of voting rights	7,044.6
4 Investment based on themes	5,5342
5 Positive screening (best in class)	992.1
6 Sustainable theme	165.9
7 Impact and community investment	108.6

Source: *Global Sustainable Investment Review 2014*, Global Sustainable Investment Alliance

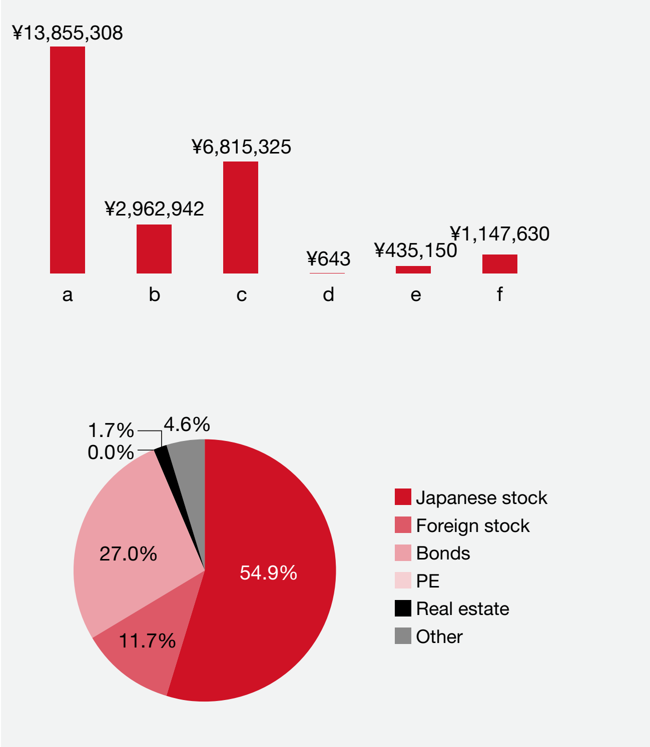
Q13 If possible, please tell us about the proportion of the amount indicated in Q9 allocated to each of the following asset classes.

(¥ Million)

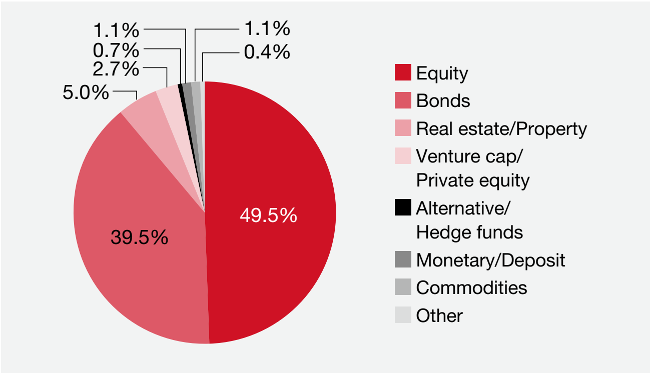
Option	Amount indicated (average)	Total of amounts indicated	Number of responses
a Japanese stock	¥659,776	¥13,855,308	21
b Foreign stock	296,294	2,962,942	10
c Bonds	757,258	6,815,325	9
d PE	91	643	7
e Real estate	62,164	435,150	7
f Other	143,453	1,147,630	8
Number of institutions that answered this question: 23/28			

Notes:
1. The number of institutions that answered includes institutions that indicated an allocation of zero.
2. As one institution declined to answer, the sum of these figures is not equal to the total amount indicated in Q9 (¥26.69 trillion).

(¥ Million)



European and Canadian allocation of sustainable investment by asset class



Source: *Global Sustainable Investment Review 2014*, Global Sustainable Investment Alliance

(The numbers of institutions below do not include institutions that indicated an allocation of zero.)

- Japanese stock represented ¥13.86 trillion of class-specific assets (21 institutions including one foreign-affiliated institution). Two of the responses were given by pension funds.
- Bonds amounted to ¥6.82 trillion (eight institutions), foreign stock to ¥2.96 trillion (six institutions), and “other” to ¥1.15 trillion (six institutions). Moreover, two institutions indicated that they are engaged in real estate investment, and one institution is engaged in investment through PE. All of these institutions were investment managers.
- Eight institutions are engaged in sustainable investment through foreign stock. Of those institutions, five were Japanese and three were foreign affiliates.
- Of the six institutions engaged in investment through bonds, four were Japanese and two were foreign affiliates.
- Of the two institutions engaged in real estate investment, one was Japanese and the other a foreign affiliate.
- There was only one institution engaged in PE investment. This institution was Japanese.
- Four out of six institutions with other assets were Japanese, and the remaining two were foreign affiliates.

Q14

In the past year, how many companies have you engaged with in “purposeful dialogue,” as stipulated by Japan’s Stewardship Code? If possible, please indicate specific companies.

Option	Number of responses
	23
Number of institutions that answered this question: 23/28	

- Twenty-three institutions indicated that they conduct engagement (purposeful dialogue) with companies and, of the five institutions that did not provide an answer, two were pension funds, and the remaining three were investment managers.
- One institution indicated that its scope for engagement was 5,400 companies; one indicated a scope of 3,000; three a scope of 1,000–1,500; two a scope of 600–700; 13 a scope of 120–350; and three a scope of 15–47.
- Although there were many cases where the scope of engagement included a large number of companies, we may assume that there were also cases where engagement was directed toward a more specific focus group.

Q15

Please provide us with some commentary within the possible scope for disclosure pertaining to the systematic evaluation processes used in managing the amounts indicated in Q9–Q13 (e.g., “ESG is implemented by the ESG evaluation team;” “screening is conducted by using outside assessment bodies or analytic data,” etc.). Alternatively, please provide a URL that gives access to disclosure materials.

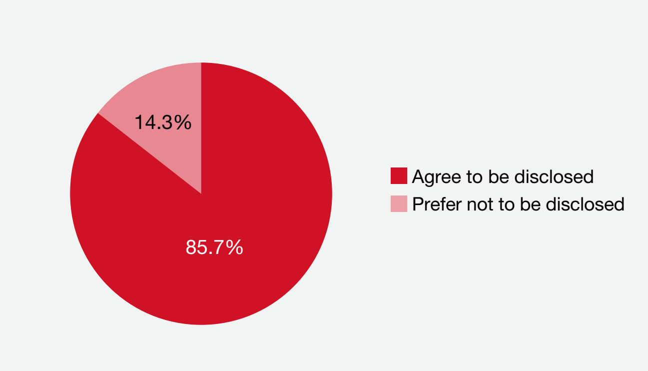
Option	Number of responses
	21
Number of institutions that answered this question: 21/28	

- Twenty-one institutions responded to the request for commentary within the possible scope for disclosure or provided a URL that gives access to disclosure materials pertaining to the systematic evaluation processes used in managing the amounts indicated in Q9–Q13.
- Of the seven institutions that did not respond, three were asset owners (pension funds), one was a foreign-affiliated investment manager, and three were Japanese investment managers.

Q16

The names of companies and funds that cooperated with this survey are to be disclosed at the end of the report for this survey. Please let us know if you prefer that this information not be disclosed.

Option	Proportion of responses	Number of responses
Agree to be disclosed	85.7%	24
Prefer not to be disclosed	14.3%	4
Number of institutions that answered this question: 28/28		



- Two of the institutions that indicated “please do not publish” were pension funds, and two were Japanese investment managers.

Japan Sustainable Investment Forum (JSIF)
JSIF Chair: Masaru Arai

Executive Summary

The *White Paper on Sustainable Investment in Japan 2015* contains new information pertaining to the influence of trends in responsible ESG investment in Japan over the last two years. This summary focuses on the movements of the Japanese markets over the last two years, and I have endeavored to pre-sent the information in a concise way to make it more accessible to the busy reader. For more detailed information, please refer to individual chapters.

Chapter 1 discusses the trends of institutional investors. The Japanese responsible investment market started with a single fund back in 1999 and, following a long period of stagnation, began to show signs of expansion once again following the introduction of Japan's Stewardship Code in 2014. Japan's Stewardship Code and Corporate Governance Code, which was introduced shortly thereafter, are like two wheels on an axle, and have the role of guiding the relationships between Japanese investors and corporations toward change. One of the authors featured in Chapter 1, Mr. Kanai, explains, "for a long time, corporations and investors in Japan have shared relationships based on mutual non-interference." Japanese corporations have long held a reserved stance toward the procurement of funding from capital markets, and investors experience little sense of "ownership," to the point where the relationship between the two can be described as a tacit policy of non-interference. The extent to which Japan's Stewardship Code may be able to change this, therefore, is a highly anticipated topic. Of course, the addition of the Japanese Government Pension Investment Fund (GPIF), the world's largest pension fund by assets under management, to the list of Japan's Stewardship Code and Principles for Responsible Investment (PRI) signatories, is sure to exert an influence on Japan's responsible investment markets, which have been left adrift by global tides. Moreover, the stance expressed by the U.S. Department of Labor regarding the U.S. Employee Retirement Income Security Act (ERISA), stating that "where ESG is directly related to the economic and financial value of investment, it should be taken into consideration in the management of assets," is also likely to have a significant influence on Japanese institutional investors. This is because, according to ERISA's interpretation of fiduciary duty to date, and as the author has expressed, "Socially Responsible Investment (SRI) has traditionally been seen as the enemy to disciples of ERISA," and the traditional interpretation in Japan was "fiduciary duty has represented a dark cloud that has covered over the heads of ESG advocates." GPIF's signing on to PRI is expected to be instrumental in lifting this cloud in Japan, and it has been emphasized that standards are now in place to allow public and corporate pensions to start making a genuine commitment to responsible investment. If we take into account the actual state of Japanese pension funds, however, we can see that there are many issues that are yet to be overcome. Going forward, these pension funds, which do not manage funds directly, will be faced with the challenge of to what extent they are able to select asset management institutions with a penchant for ESG investment processes as partners, as well as monitor and manage these institutions. They must also take on the challenge of changing their traditional interpretation of ESG as one form of active investment, and instead work toward the incorporation of ESG into their investment processes through "ESG integration."

This chapter introduces various examples of ESG integration at Mitsui Sumitomo Trust Bank and responsible investment initiatives at Resona Bank, presented by Resona Bank's Minoru Matsubara, as case studies of initiatives at Japanese asset management firms. The chapter also features a column by Takeshi Mizuguchi, a professor at the Takasaki City University of Economics who has spent many years researching sustainable investment, which discusses the perspectives of overseas observers pertaining to trends in sustainable investment in Japan.

Chapter 2 explores the trends of individual investors in terms of Japanese SRI investment trusts. The chapter is a focal point of this JSIF white paper, which represents the only one of its kind in Japan by presenting data related to the trends of SRI investment trust markets over the last 16 years, adding analysis, and making this information available to the world. We encourage the reader to examine the chapter while considering these market trends. SRI investment trusts were established in Japan in 1999 and, by 2007, their total investment balance had surpassed ¥1.0 trillion. This was reduced by half in the aftermath of the 2008 financial crisis, and since the second half of 2011, the figure continues to fluctuate between ¥210.0 billion–¥260.0 billion. In the two years since the end of September 2013, however, the SRI investment trust balance experienced an 11.5% decline, from ¥244.0 billion to ¥216.0 billion. In terms of the investment scope of SRI investment trusts, the percentage of net assets allocated to domestic stocks at the end of September rose to 54.5% from 42.4% two years ago, while the percentage allocated to international stocks fell from 50.0% to 40.2%. In terms of evaluation criteria, funds under the evaluation criteria of environment represented 58.6% at the end of September 2015, down from over 70% two years earlier. Although the funds invested in international stock under the evaluation criteria of environment still represent the largest proportion of net assets, the composition has been gradually diversified.

If we examine newly established and amortized investment trusts, we can see that the number of SRI investment trusts peaked at the end of June 2010 at 94 before falling into a trend of decline. This trend later subsided and, as of September 2015, there were 74. For over three years from the first half of 2011, there was a continuing trend of no new establishment. However, from the second half of 2014, we can see that newly established trusts have come to exceed amortized trusts. When we observe trusts in terms of evaluation criteria, we may note the characteristic that, over the last two years, six out of ten newly established SRI investment trusts have been womenomics-focused. If we examine the capital flows of SRI investment trusts, we can see that net capital inflows are continuing to decline. Until 2007, capital inflow was consistent with the establishment of funds. However, following the confusion of the global financial crisis, capital flows have continued to demonstrate net losses since 2010, regardless of trends pertaining to new fund establishment or amortization. This net decline has continued even since the second half of 2014, when the number of funds began to rise again. Recent years have seen the investment environment remain relatively favorable, and we can see an increase in the net asset balance as a result of investment. However, this increase has been offset by the capital outflows from cancellations and redemptions and, on the whole, the total net asset balance has remained stagnant with little to no increase or decrease. The analysis featured in this section was contributed by the author, Masaru Otake, and various data were provided by QUICK Corp.

Moreover, Chapter 2 also touches upon the trends of social impact bond markets. In Japan, the first social impact bonds for individual investors were made available in March 2008 and, in 2014, aggregate total sales exceeded ¥1.0 trillion. The total sales and issue balance as of the end of September 2015 were ¥1.121 trillion and ¥564.2 billion, respectively (calculated at the exchange rate when figures were published; excluding balance decline due to incomplete sales). In comparison with figures from the end of September 2013, total sales rose by ¥327.9 billion, the issue balance rose by ¥89.6 billion, and, even after seven years since they were first introduced in 2008, social impact bonds continued to show a trend toward growth. Moreover, in November 2013 the International Finance Corporation (IFC) issued the “Banking on Women Bond,” which represented the first gender-themed social impact bond to be issued in Japan. The author of the chapter, Ken Tokuda, highlights three elements that are central to the renewed growth and movement of social impact bonds: 1) alignment with stakeholders; 2) a simple composition and high interest currencies; and 3) the promulgation of “best effort” management. Meanwhile, if we consider the issue and sale of bonds by institutional investors, we can see that life insurance companies in particular have begun to use investment in social impact bonds as a form of growth investment, reflecting positive movement on this front also. Green bonds have also started to be issued by Japanese banks, including the Development Bank of Japan (DBJ) and Sumitomo Mitsui Bank, and we can see model cases arising from the perspectives of both investors and issuing bodies.

Chapter 3 touches upon shareholder advocacy. Japan’s Stewardship Code was established in February 2014, and at the end of November 2015, 201 institutions, including overseas institutions, were signed up. Most of the main asset management companies in Japan are signatories, in addition to asset owners such as public pension funds including GPIF, corporate pension funds, life insurance companies, and other associated institutions. Meanwhile, Japan’s Corporate Governance Code, which targets listed companies in Japan, took effect on June 1, 2015, and emphasizes that companies listed on both the first and second sections of the stock exchange have a duty to comply with, or otherwise explain their actions relative to, each principle. The style of corporate governance reports has changed in line with the introduction of the Code and, from June 2015, corporations are required to provide reports in the new style within six months of annual shareholder meetings. As of the end of November 2015, a total of 1,089 companies—approximately 30% of listed companies—have been submitting reports in the new style. However, the Code is not enforced by law, and while the principle-based British system emphasizes the concept of “comply or explain,” Ms. Yamasaki stresses that “until now, most Japanese corporations have operated on a rule-based system where regulations are decided and subsequently complied with. Consequently, there are many Japanese corporations that are simply not used to the concept of explanation yet.”

The concept of “engagement,” a theme common to both codes, is also arousing anticipation. Change continues to be apparent in the use of voting rights for ESG proposals by shareholders and at general assemblies, which represents one form of constructive dialogue. For example, in recent years, proposals by individual shareholders acting autonomously, institutional investors, and major shareholders (individuals, investment companies, and municipal bodies) have become increasingly common. Many of these proposals aim to increase the involvement of shareholders in company management by enhancing transparency pertaining to the election and dismissal of outside directors/outside corporate auditors and corporate management. Constructive, purposeful dialogue by Japanese investors, or, in other words, dialogue that elicits change by enhancing corporate activities or structure is therefore a topic of rising anticipation.

Chapter 4 is entitled "Sustainable Finance" and discusses the emergence of various approaches to sustainable finance in Japan, including financing, community investment, environmentally friendly real estate, and private equity.

According to Keisuke Takegahara, who provides us with an introduction to principles for financial action, as of September 2015 the number of institutions signed up to the Principles for Financial Action for the 21st Century had expanded to 195, which extend across a wide sphere, from major banks, securities companies, and insurance companies, to regional and trust banks all over the country. In this way, a formal foundation, which straddles the borders between industrial sectors, has been established to develop ESG-considerate investment and financing. To further develop ESG investment going forward, however, it is going to be necessary to work on encouraging financial institutions to take anonymous action, while addressing the issue of varying degrees of enthusiasm between signatories.

As stated by the author of "Community Investment and Crowdfunding," Shunji Taga, there were 25 NPO banks in Japan as of December 1, 2015, and as of the end of March 2015, the aggregate total of financing provided by those 25 NPO banks rose to ¥3.2 billion. From a regulatory standpoint, the 2014 revision of the Financial Instruments and Exchange Act deregulated micro-investment funds, or investment crowdfunding, that utilize collective investment schemes, and from January 2016, discussions aimed at forming legislation pertaining to the use of dormant deposits are continuing to take place at regular Diet sessions. According to a bill submitted at an ordinary Diet session in 2015, supporters of community investment represent "fund distribution organizations" for these dormant deposits. This section also includes a column by Masayuki Oki, which draws on his experience of investing in micro funds.

Environmentally friendly real estate is an area that is garnering attention from the sustainable investment sector. Until recently, there were hardly any buildings or projects in Japan that had been recognized by global real estate certifications (LEED, etc.). According to Hiroki Hiramatsu, however, there are now a number of projects in Japan that have successfully acquired such certification. The environmental performance—energy efficiency, for example—of buildings in Japan is generally good. However, verification of this by globally recognized certification systems is appealing because it reflects the expansion of new opportunities to invest responsibly.

There are 3.86 million companies in Japan, and as listed companies only represent 3,500 of these, the remaining 99.9% are unlisted. Some of these may well be selected to form part of investment portfolios, however, as Shunsuke Tanahashi emphasizes: "69.4% of all Japanese workers are employed at small- and medium-sized businesses, and these businesses are responsible for creating 53.3% of total added value. We can naturally assume, therefore, that thinking seriously about investment in the private equity segment is akin to thinking about the sustainable expansion of the Japanese economy." Japan's responsible investment is still primarily focused on investments in listed stock, and this section discusses points to be taken into account when engaging in private equity investments to ensure the proliferation of responsible investment in this field.

Minako Takaba

1 Trends of Institutional Investors

1. Responsible Investment of Pension Funds

(1) The Significance of Stewardship Code Introduction

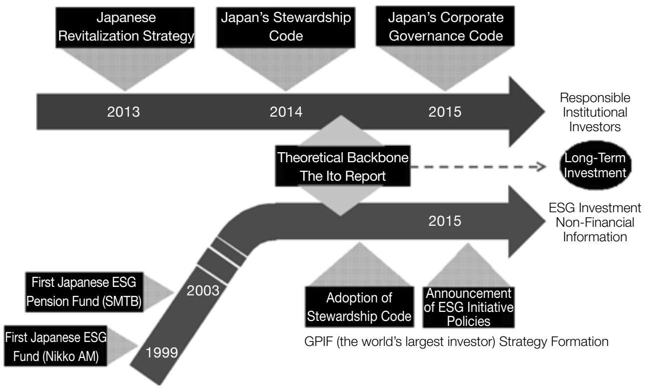
Years from now, 2015 will probably be seen as the year that represented a turning point for Japanese responsible investment. Japan's first SRI fund was established in 1999 and the responsible investment markets continued to expand steadily until the blow dealt by the 2008 financial crisis, which caused them to shrink and remain sluggish for a number of years. In 2015, however, responsible investment began to show signs of a reemergence, which we may attribute to the introduction of Japan's Stewardship Code (SSC).

Following the adoption of the SSC, in 2015 the Corporate Governance Code was introduced, which represents a key policy in the Japan Revitalization Strategy outlined by Prime Minister Abe's cabinet in 2013. The objective of the Code is to "bolster the earning power of Japanese corporations" through "aggressive governance." In addition, it also serves as a policy to resurrect the Japanese stock markets, which have been sluggish since the economic bubble burst in the early 1990s. So what does this mean?

For a long time in Japan, corporations and investors have shared relationships based on mutual non-interference. Japanese corporations have traditionally held a reserved stance toward the procurement of funding from capital markets and tend to dislike it when outsiders (investors) encroach on managerial affairs. Conversely, the sense of corporation "ownership" felt by investors is all but absent, and the leverage held by corporations in transactional relationships has led investors to hesitate in confronting them. In other words, these relationships may be described as acquiescing to a tacit policy of mutual reticence. As a consequence, investors feel little responsibility to protect the markets and are often plagued by a sense of indifference. Over the last ten years, corporate pensions and other funds have been consistently limiting the proportion of investments in Japanese stock, which has accelerated the negative spiral of stock price stagnation. The SSC, however, sent a signal that the stock markets, which even domestic investors had turned their backs on, had begun to change.

On September 27, 2015, Prime Minister Abe announced at the UN summit that the Japanese Government Pension Investment Fund (GPIF)—the largest pension fund in the world, with pension reserves equivalent to $1.0 trillion—had become a signatory to the UN's Principles for Responsible Investment (PRI), and that this would represent a significant contribution to the realization of Japan's sustainable development going forward. The conservative GPIF was also swift to adopt the SSC last year, with its distribution of ESG surveys indicative of a change in its attitudes toward responsible investment. It was even more surprising then, when those with connections to the fund indicated that remarkable changes were in fact yet to materialize. "Key Policies Related to ESG Initiatives," released the next day, highlighted that "ESG initiatives will be reinforced as a key element in the execution of stewardship responsibilities." Although the backgrounds surrounding the establishment of the SSC and PRI are different and, even in the UK where the SSC originated, financial authorities are striving to prevent confusion of the two, both emphasize the concept of raising the long-term value of investee corporations. Conceptual integration of the two is, therefore, not inappropriate. The expression of progressive thinking by GPIF, which is the world's largest asset owner, has been received with favor, and it also has the potential to be a driving force for change in the Japanese markets, which have been left adrift by global tides. In this way the SSC has opened up a pathway toward ESG.

Figure 1.1.1



(2) Influence of the U.S. Department of Labor's New Stance on Pensions

The U.S. Employee Retirement Income Security Act (ERISA) was established as law in 1974 with the objective of protecting the rights of corporate pension recipients. The scope for the act was corporate pensions, but its influence extended to the U.S.'s enormous public pensions in addition to having a substantial influence on pension markets in Europe. Socially responsible investment (SRI), unlike modern investment theory, excludes investment in companies deemed to be unethical, and has traditionally been seen as the enemy to disciples of ERISA. In fact, U.S. corporate pensions have rarely pursued responsible investment in managing their funds. Japanese pensions diverge little from this example; in 2003, which marked the dawn of a new era for responsible investment, SRI was universally loathed by experts, and we cannot deny the fact that this was a major cause of the subsequent slump in the markets. The expansion of responsible investment overseas, however, was sparked by public pensions and, more specifically, European public pensions, which could not be further removed from ERISA.

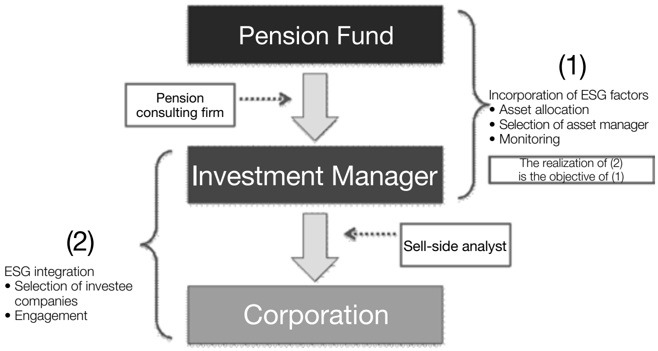
When we take into account these circumstances, the stance expressed by the U.S. Department of Labor, which oversees ERISA, on October 22, 2015, stating that "where ESG is directly related to the economic and financial value of investment, it should be taken into consideration in the management of assets," may well be considered revolutionary. We may, however, interpret this to mean that, in the midst of rapid expansion in the responsible investment markets, the Department has simply become unable to maintain its traditional stance. Although to some this announcement may seem to be a little too late, and to simply represent no more than a return to baseline following a long history of lost opportunities, the dark cloud that has hovered above the heads of ESG advocates for many years has unarguably been lifted. Moreover, as this occurred at the same time GPIF became a signatory to PRI in Japan, we can speculate that the foundations have been laid for public and corporate pensions to start seriously implementing responsible investment.

(3) The Decision-Making Process and Responsible Investment of Pension Funds

The management of pension funds is usually based on independent management policies, and the establishment of a basic asset allocation plan based on the results of pension asset liability management (ALM), among other factors, represents the first step. Small and medium-sized funds often outsource their fund management on a discretional account basis to an investment manager at this stage. Larger funds will decide on the active and passive proportion per asset and, for the active portion, a investment style combination. Investment managers are then selected for each style on the advice of a pension fund-consulting firm, and mandates are settled. The asset owner subsequently has a responsibility to check periodically that the investment manager is managing in accordance with this mandate. Through such monitoring, investment managers that fail to produce the results anticipated can be dismissed and replaced. "Results anticipated," however, does not simply refer to performance. There are areas for periodic evaluation that are separate from performance and, if management is not being implemented in accordance with the asset owners' trust policies, institutions may have their contracts revoked even when performance improves.

Japanese pension funds, with the exception of a part of the Pension Fund Association, do not manage funds directly, and generally outsource management, including the use of voting rights, to a dedicated investment manager. Responsible investment is handled in the same way, through investment managers that specialize in ESG investment. There is a tendency for the role of pension funds, which represent the actual asset owner, to be emphasized more than is necessary. The use of voting rights, such as in investment based on ESG evaluation and engagement, is the role of the investment manager (asset manager). Therefore, the role of the asset owner ultimately depends on the extent to which it presses the asset manager to fulfill its role. In other words, asset owners must select an investment manager that incorporates ESG into the investment process and effectively engages in constructive dialogue with corporations, while periodically monitoring the investment manager to ensure that such activities are taking place.

Figure 1.1.2

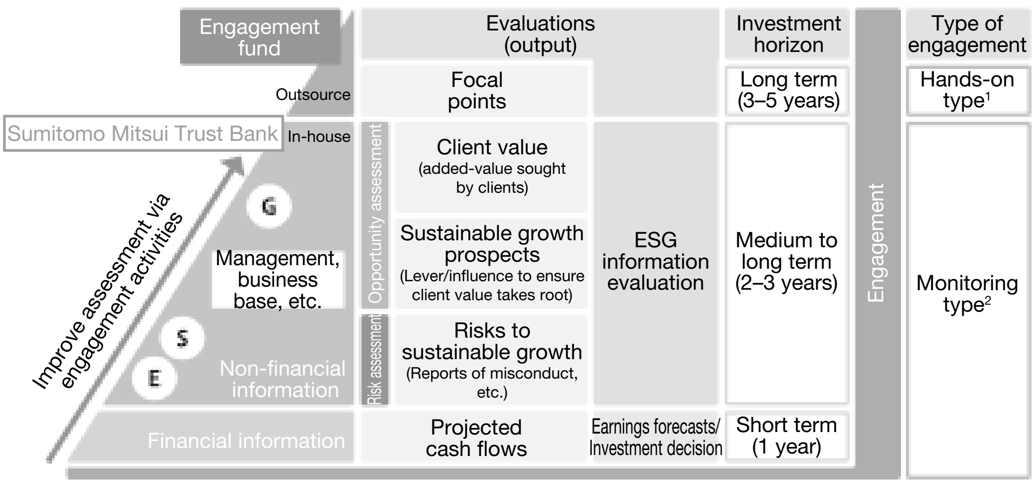


Investment managers aim to improve the performance of actively managed funds by incorporating ESG in the investment process. However, there is currently no clear standard pertaining to the time frame over which pension fund evaluations should be implemented. Long-term management denotes the evaluation of corporate value from a long-term perspective, but does not necessarily mean that a fund will hold onto an investment in a particular company for a long period of time. However, the evaluation of investment managers based on short-term performance may bring about investment behaviors based solely on purchasing stocks that rise in value. It has therefore become necessary to establish evaluation methods that reflect the new role of capital markets—a fact also applicable to SSC evaluation.

Although responsible investment by Japanese pension funds began in 2003 (with KDDI and Shinsei Bank funds), until recently most have been limited to the settlement of mandates with responsible investment funds that specialize in Japanese stocks. In other words, although one style of active management for responsible investment has been established, it still only reflects a very small portion of pension fund assets overall. Consequently, responsible investment balances have not risen.

Meanwhile, Sumitomo Mitsui Trust Bank (SMTB), which has a wealth of experience in fund management, has been conducting ESG integration in its normal active management (¥2.0 trillion) investment process since 2015 (SMTB also conducts engagement based on a theme of ESG). More so than the resultant increase of the responsible investment balance under management, however, the move was significant because it set a precedent for all analysts and investment managers at active funds to work toward incorporating ESG.

Figure 1.1.3: ESG Integration at Sumitomo Mitsui Trust Bank, Limited



E: Environment
S: Social
G: Governance

1. A hands-on engagement-type approach seeks to secure a commitment from investee companies to implement business growth measures, etc.
2. A monitoring-type approach seeks to support independent management decision-making at investee companies via debate on share price impacts, etc., from improving IR activities to rebalancing business portfolios.

In responsible investment markets overseas, a negative screening-type investment has significantly increased, followed by integration- and engagement-type investment. When we take into consideration the Japanese mentality, it is difficult to imagine that negative screening will increase. Integration-type investment, however, has a strong affinity with the fundamental asset management objective to pursue share value, and has a high probability of becoming a predominant trend going forward. Moreover, the incorporation of ESG elements in engagement principles established by the SSC is relatively straightforward, so this is likely to become common practice in the future. On the other hand, it is difficult to conjecture that specialized responsible investment funds will diminish. GPIF also highlighted in its "Key Policies Related to ESG Initiatives," that "regarding ESG-aware smart beta and active management, we will continue to conduct research while taking into consideration past performance and focus on the establishment of a strong foundation to bolster the earnings that have come to be expected of us."

The subject of whether engagement based on ESG themes will be incorporated into passive management is controversial. It has been pointed out that low-income passive management cannot offset the costs of engagement. In Japan, however, purely passive houses are scarce, and, in the case of funds that offer both styles, it can become difficult to distinguish whether engagement is being implemented in active or passive management. Sumitomo Mitsui Trust Bank conducts in-depth engagement activities with investee companies that form part of its actively managed portfolios. However, it also has a policy of conducting engagement with companies that do not fall into this category (companies that are only included in passive funds) but which are considered to have problems.

(4) ESG or GSE?

Sustainable Investment Forums in every region are going to significant lengths to urge institutional investors to work toward the incorporation of responsible investment. Recent circumstances have shown that these efforts are coming to fruition. However, more time is probably going to be necessary in regard to the incorporation of important sustainability themes such as global environmental problems. I would like to address this as my last point.

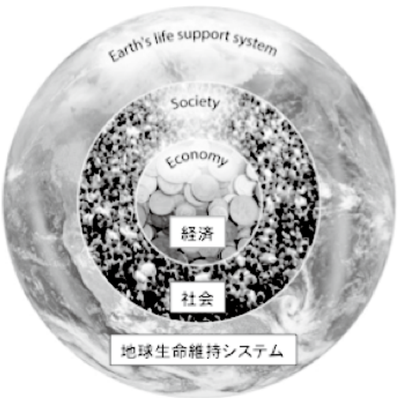
Of the three elements that comprise ESG, the one that holds the most significance for corporate value is corporate governance, including risk management and compliance. In addition, social issues, in particular themes relating to human resources or employees who directly support corporate value creation, are extremely important. As such, these themes represent an area that ESG research agencies place emphasis on. From a corporate management perspective, these non-financial matters (intangible assets) are obviously important. However, as these matters are difficult to evaluate and have a time lag compared to business performance, they have not been of high importance in active management. That being said, there is a possibility that mainstream investors may establish evaluation methods for these non-financial matters and prioritize the pursuit of active returns. Therefore, when listed in order of priority, ESG becomes GSE.

Despite its potential to influence the internal performance of corporations, the UN did not establish PRI simply to encourage investors to evaluate non-financial data. Recently, there has been an international movement to redefine the concept of sustainable development as "development that fulfills the needs of the current generation, while protecting the earth's life support systems that are and will continue to be relied upon by the generations of today and tomorrow." The diagram in Figure 1.1.4 conveys a concept advocated by Australian professor David Griggs, among others, which mirrors the "six forms of capital" diagram (Figure 1.1.5) included in the IIRC's International Integrated Reporting Framework. Natural capital is synonymous with the earth's life support systems, including elements of the environment, and a loss of this would not only affect corporate activities but also jeopardize the basis for all human existence.

When we consider things from this perspective, we have to assert that it is ESG, not GSE, which is most important in the long term. It will probably be some time before mainstream institutional investors are ready to adopt this view. However, with the promulgation of PRI around the world and the SSC across Japan, the foundations may well have been laid.

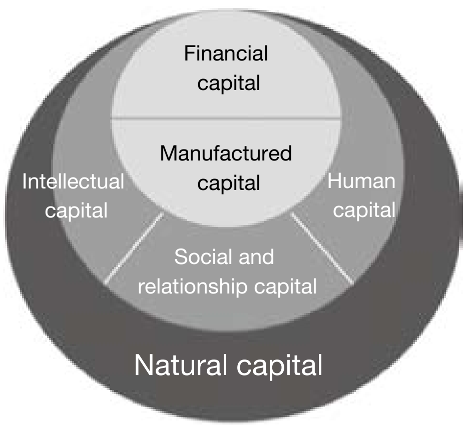
Tsukasa Kanai

Figure 1.1.4



Source: Griggs, David, et al., 2013

Figure 1.1.5



Source: International Integrated Reporting Framework

2. Responsible Investment: Initiatives at the Resona Bank Asset Management Division

(1) Foreword

In May 2008, Resona Bank became a signatory to the UN Principles for Responsible Investment (PRI), and since then, it has been earnestly engaged in responsible investment initiatives. Moreover, in April 2014, the Company announced its approval of Japan's Stewardship Code and published its course of action.

To summarize this, we have established a "basic policy for responsible investment" as part of the "code of conduct pertaining to asset management activities" and are working hard to communicate our intentions and spirit as a responsible institutional investor.

The basic policy is made up of three concrete pillars: the incorporation of environmental, social, and governance (ESG) factors in the investment decision-making process; constructive dialogue with investee companies; and the appropriate use of voting rights as a trustee.

I would like to use this opportunity to explain the thought processes behind and significance of these policies.

(i) Incorporation of ESG in the Investment Decision-Making Process

As society increasingly expects corporations to adopt a "from shareholder to stakeholder" arrangement, the incorporation of ESG evaluation is gradually coming to represent a standard by which corporate value and its sustainability can be evaluated from a multifaceted, long-term perspective. Against this backdrop, coupled with its history as a long-term institutional investor, the Company is working to promote ESG integration initiatives in its stock portfolios. In concrete terms, ESG serves as a catalyst to improve non-financial factors with the potential to impact investment performance, or in other words, overall product quality, in all judgment-based, actively managed domestic stock funds.

By fixating on the term "ESG," there can be a tendency for it to be misunderstood as an extremely specialized investment method. In evaluating corporations today, however, the analysis of non-financial factors including ESG, as opposed to only financial aspects and figures relating to performance, is extremely important. As specific criteria and theories pertaining to the evaluation of ESG are not widely established at this time, we may conjecture that a diverse range of approaches toward ESG will begin to present themselves going forward. This diversity, however, is significant because it is diversity itself that allows for differentiation.

(ii) Constructive Dialogue with Investee Companies

The Company has two reasons for emphasizing the importance of dialogue. The first is the rebuilding of relationships of trust between shareholders and corporations. Although equity investments serve the function of financial intermediary to provide corporations with capital, we cannot expect such investments to materialize if there is no initial trust between lender and borrower. However, as of late, the stock market's function as an "arena for trading" has been strong and, although there have been concerns that relationships of trust between shareholders and corporations have weakened, dialogue with corporations is expected to contribute to the improvement of such circumstances. Provisions to improve the environment so as to encourage such dialogue are steadily being introduced. These include approaches such as the February 2014 establishment of Japan's Stewardship Code in addition to the June 2015 application of the Corporate Governance Code as an additional prerequisite to Tokyo Stock Exchange's Securities Listing Regulations, the latter of which represented a notable shift in the function of the market. Many established corporations are currently finding that opportunities to procure capital from the stock markets are scarce, and we can see many examples in which internal reserve capital and cash flows borne out of corporate business activities are being used to fund investments in future growth. If we consider this from the perspective of market function, we can see that the distribution of funds within the corporation itself is becoming more and more important. To this end, investors must be willing to engage with corporations in dialogue pertaining to the appropriation of income in the same way that they scrutinize the corporations they choose to invest in. This represents a crucial element of investment management.

(iii) Appropriate Use of Voting Rights as a Trustee

Resona Bank considers the improvement of investee corporations' corporate governance policies as one of its responsibilities as an institutional investor and understands that, through its investee corporations, it has the potential to significantly impact the environment and society. Moreover, we understand that, conversely, environmental and social change may have significant impact on our investment performance.

When engaging in responsible investment, the Company places a high level of importance on managing the autonomy and functionality of its Board of Directors, director compensation, performance, and risk, both social and environmental. These elements form the focus of dialogue and, depending on the circumstances, the Company may also exercise voting rights. As a precursor to this, however, we make a point of promulgating the mutual understanding and sharing of information pertaining to issues that may impact these elements.

The three items described above represent the Company's main activities in promoting responsible investment. I would also like to specifically touch upon the concrete ESG initiatives we incorporate into our investment decision-making process, and the Responsible Investment Committee, which represents our internal mechanism to support the plan-do-check-act (PDCA) cycle.

(2) Examples of Concrete Initiatives

(i) Incorporation of ESG in the Investment Decision-Making Process

Resona Bank has been pushing forward with responsible investment initiatives since signing on to the UN Principles for Responsible Investment in March 2008. The incorporation of ESG into the investment decision-making process for our active funds represents a concrete example of such initiatives. In this way, we are working hard to pursue stable added value over the medium to long term.

Through its many years of experience in investment management, the Company believes that, although ESG information does not necessarily affect stock prices in the short term, it can represent a determining factor in stock prices over the medium to long term. With this in mind, we have used ESG primarily as an item to assess risk, whereby the pros and cons of investments and, in turn, investment ratios, are decided based on the assessment of this risk. Moreover, with our adoption of the Stewardship Code in April 2014, we consider ESG to represent an important element in the expansion of corporate value through sustainable growth of sales and profits, and we engage in various discussions and experiments with the objective of reflecting the results of these evaluations in the selection and determination of investee corporations and investment ratios.

The Company manages a number of active funds that employ multiple strategies. Where ESG information is emphasized and analyzed, when it is used in the selection of investee companies, and how it is weighted depends on the concept behind each strategy. Here I will introduce four typical strategies and give an overview of how they use ESG information in investment decision-making.

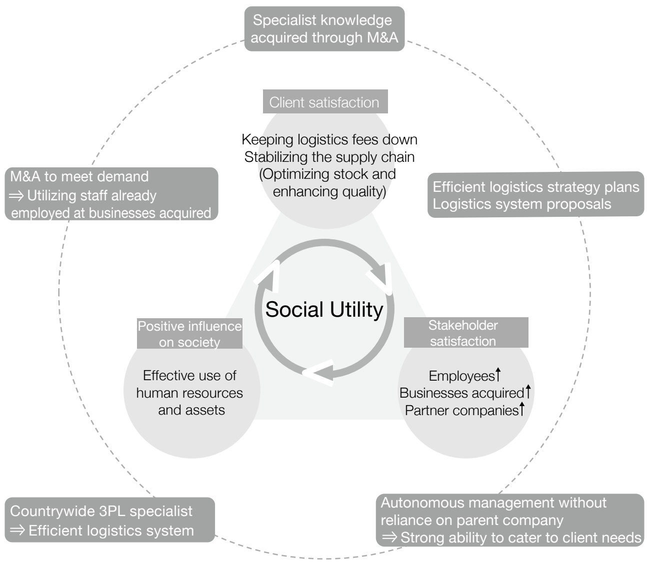
"Market-oriented" funds consolidate ESG factors to build a unique evaluation process that is used to improve accuracy in judging investments and thus expand the funds' returns. From a social perspective in particular, this type of fund emphasizes the analysis and evaluation of a fund's "ability to consistently generate shareholder profits through the realization of social utility." The Company is working hard to select corporations that, through their business activities, have the capacity to generate stable profits as a contribution to the healthy growth of society.

"Social utility" pertains to a synergy between the following three elements: client satisfaction, the satisfaction of stakeholders other than clients, and a positive impact on society. Corporations with a high potential to generate social utility are proficient in activating this three-element loop, and we can expect them to achieve sustainable growth in tandem with society. The Company allocates a larger proportion of investment to companies with an outstanding ability to create social utility, and this is reflected in its portfolios.

As an example of this, I would like to cite the analysis of Company A, a comprehensive logistics company (Figure 1.2.1). In the logistics industry there has been a [gradual] movement toward 3PL (third-party logistics), which endeavors to realize an efficient logistics strategy by building a logistics system that involves outsourcing operations to multiple consigners. Through an efficient logistics system, 3PL is capable of realizing social returns in every area: client satisfaction, controlling the consigner's distribution expenses; satisfaction of stakeholders, improving the satisfaction of staff and consumers; and a positive impact on society, ensuring the mitigation of labor shortages, among other benefits.

Through M&A, Company A has acquired a diverse knowledge pertaining to workflows across the industry and resources including workers and logistics facilities; it has gained further trust from clients by expanding its scope of activities and—through this synergy—is achieving significant growth. M&A is therefore a key factor, but it was the "results dialogue" with Company A to ascertain why so much of this M&A had been successful that led us to judge that it had high potential to achieve sustained growth going forward.

Figure 1.2.1: Social Utility Loop—Company A



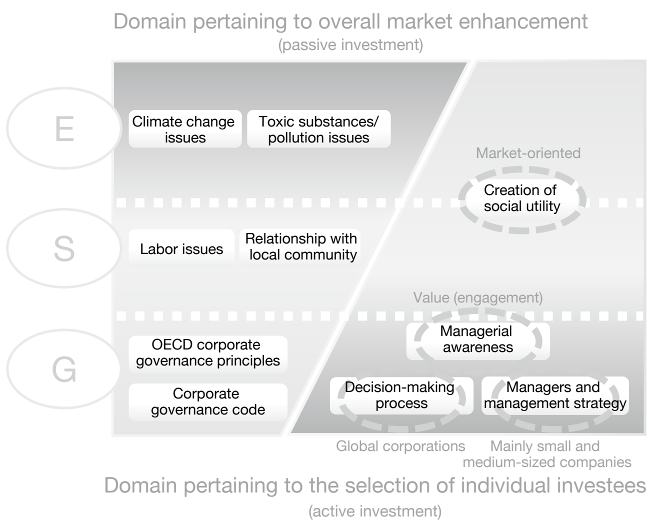
The "Japan Select" fund assesses whether a corporation's decision-making process is functioning effectively to maintain and improve its competitiveness, primarily through the analysis and evaluation of corporate governance. The fund concretely assesses: the circumstances, the processes, what kind of people are making decisions, and what kind of decision was made. It then works to identify the governance structure that each corporation has used to tackle changing environments in the past, and how it intends to deal with changes going forward. Through this process, the fund is able to ascertain an idea of the strengths and weaknesses pertaining to a corporation's decision-making and strategy-building, judge the integrity of its corporate management, and reflect the results of such evaluations in portfolio investment ratios.

Value funds (research [α]) that are in the process of selecting corporations in which to invest evaluate and analyze potential investments by first identifying whether management has correctly interpreted the cause of falling prices, for example, and then determining whether this underlying cause can be addressed by planning and executing policies with a high probability of realization. In this way, governance-focused evaluations, in addition to dialogue with corporations pertaining to the enhancement of corporate value, represent important tools in making investment decisions.

Small-cap funds often target small market capital companies such as newly listed companies and companies where the founding family is a major shareholder. The organizational structures of such companies are therefore seen as more vulnerable in comparison to those of large corporations, as there is a [higher] possibility that their corporate value may be inadvertently damaged by management decisions forced through by the founding family. Therefore, the Company advocates the selection of investees following efforts to implement analysis and evaluations with a focus on "G" from a risk perspective. These small-cap concentrated investment funds, which make concentrated investments in carefully selected stocks, however, do not stop at governance-focused risk assessment. Rather, these funds go one step further to allocate a high proportion of investment to corporations with trustworthy and exceptional management staff who recognize that "companies are a public entity of society."

In this way, the Company is working hard on a daily basis to refine its investment decision-making processes in order to pursue stable added value over the medium to long term. We consider the incorporation of ESG information to be a powerful solution in this regard and, going forward, will continue to work toward effective use of such information.

Figure 1.2.2: Overall View of ESG Initiatives at Resona Bank



(ii) The Role and Activities of the Responsible Investment Committee

The Responsible Investment Committee works to deliberate whether appropriate actions are being implemented to honor the Principles for Responsible Investors and the UN's PRI. This is achieved by discussing and reporting on the Company's activities, and on the statuses of the three concrete initiatives outlined above, which represent our basic policies pertaining to responsible investment: the incorporation of ESG factors in the investment decision-making process; constructive dialogue with investee companies; and the appropriate use of voting rights as a trustee. It subsequently works toward consistent innovation in and improvement of these activities.

The Responsible Investment Committee comprises presiding directors and department/section chiefs from trust asset management departments and, to offer insight from the perspective of internal controls management, presiding directors and department/section chiefs from trust asset management departments. These members leverage their experience and knowledge to make proactive, appropriate contributions.

The Responsible Investment Committee was established in April 2014 and convened 19 times as of September 2015. The meetings mainly discussed and reported on the three concrete objectives outlined above.

More specifically, the Committee discusses changes in standards pertaining to the use of voting rights, deliberates proposals for which resolution has been challenging, reports on the status of incorporation of ESG in the investment decision-making process for active funds and on the content and results of dialogue with corporations, and discusses the improvement of initiatives going forward. Based on the content of these discussions and opinions pertaining to improvement, the Committee works to enhance dialogue initiatives and activities, including the use of voting rights going forward, and functions to foster a higher level of stewardship responsibility.

As epitomized by the Japanese philosophy of *sampo-yoshi*, which emphasizes the notion of "good for the seller, good for the buyer, and good for society," corporations and society share a mutually interdependent relationship.

We may assume that "encouraging the growth of corporations," as emphasized by Japan's Stewardship Code, is achievable through simultaneous "realization of sustainable growth" by corporations, investors, and society, coupled with the support of various stakeholders, in the spirit of mutual prosperity. To realize this vision, institutional investors are expected to embody the role of stringently controlled "unsung heroes," and I believe that Resona Bank, as one of these long-term institutional investors, should be striving to reflect this.

Minoru Matsubara

THE PERCEPTION OF JAPAN FROM OVERSEAS

I was able to ascertain a glimpse of Japan as observed by those overseas through a one-year stint in London. As I am Japanese, however, this perception may well be biased. For example, while attending symposiums such as “RI Europe” in June and “PRI in Person” in September, I would often be engaged in conversation about Japan:

“I hear Japan has also introduced a Stewardship Code.”

“Has it had a big influence?”

“Japan seems to be quite passionate about integrated reporting!”

Then, after October 2015, I was also approached with “I hear GPIF signed on to PRI.” Obviously, my peers were simply aware that I was Japanese and were deliberately directing the conversation toward the subject of Japan; to think that everyone was keeping a particularly close eye on Japan would be a misinterpretation.

That said, it stands to reason that the conversations directed at me were indicative of an increase in positive signs. If I had been there two years ago, there would have been no talk of stewardship codes. Even if we suppose that Japan is not, indeed, the center of attention, such discussion does seem to suggest that the country warrants closer attention. But is that enough?

So what kind of country is Japan, anyway? If we consider it in terms of nominal GDP for 2014, Japan ranks third in the world, at $4.6 trillion, behind the U.S. at $17.4 trillion and China at $10.4 trillion. In terms of CO_2, Japan is responsible for 3.9% of global emissions and is the fifth-largest producer of CO_2 emissions in the world after China, the U.S., India, and Russia. So what about pension assets? Financial media publisher Pensions & Investments and HR consulting firm Towers Watson publish a list of the world’s 300 largest pension funds by assets held. The world’s number one, of course, is GPIF. Ranked second is the Norwegian Government Pension Fund. In terms of the number of pension funds listed in the top 300, Japan is ranked at number five. However, if we look at its ranking in terms of total assets held, Japan is the world’s number two, with 11.6%, behind the U.S., which is number one with 37.6% (see Table 1). In terms of responsible investment, however, Japan’s presence can hardly be thought of as appropriate to this amount of capital.

For example, if we compare countries in terms of the number of PRI signatories, Japan has nine signatory asset owners and 22 signatory investment managers, ranking it number 11 and number 13 in each of these categories, respectively. Japan may hold the top spot in Asia, but in comparison with the U.S., as well as the U.K., the Netherlands, Australia, and other Western nations, its number of signatories is still low (see Table 2). Responsible Investor, which publishes net-based news on the subject, compiles an annual survey of annual reports produced by over 1,000 pension funds and commends the best examples of reporting on responsible investment at the RI Reporting Awards. For the last three years, the awards have been dominated by European institutions in the Netherlands, France, Sweden, the U.K., and Norway. The awards system is based on English-language reports, so the fact that Japanese pension funds are not included speaks for itself. One of the reasons Japan fails to stand out, then, is its lack of English-language publications, and so there certainly seems to be a language bias at work here. However, the reasons may extend beyond that as well. For example, if a Japanese pension fund were to, theoretically, produce an English-language report, is the pension fund likely to be commended as an exceptional example of responsible investment reporting?

Reports that really assert a sense of presence in this field are exemplified by the communication of a special “something,” such as the publication of a survey on climate change, or conducting engagement pertaining to supply chain or human rights issues. Japanese PRI signatories are undoubtedly earnest in their everyday incorporation of ESG in corporate evaluations; but that is not going to be enough to gain recognition on the world stage.

I am not trying to say that standing out is more important than anything else; ultimately, the real “returns” for long-term investors are manifested by the realization of a sustainable, healthy society. So, what do we need to do to achieve this? We might say that the answer to this lies in scale-appropriate contributions that target common returns for the responsible investment community as a whole. Is that not really what is being assessed here? When I look at Japan from the perspective of overseas observers, it is this difference in “execution” that really hits home.

As a result of GPIF becoming a signatory to PRI, Japan has significantly bolstered its weight in terms of capital, and the introduction of its stewardship code has also been recognized. Going forward, Japan may well be set to assert its presence within the global responsible investment community. So with these systems in place, where is Japan headed from here? We can certainly say that the world is waiting with anticipation for an answer.

Takeshi Mizuguchi

Table 1: Top 300 Pension Funds Around the World

Country	Number of funds listed in the top 300 (parentheses indicate global ranking)	Proportion of total assets under management (percentage of overall share)
U.S.	128 (1)	37.6%
Japan	15 (5)	11.6%
Netherlands	13 (6)	6.9%
Norway	1 —	5.8%
Canada	19 (3)	5.6%
U.K.	27 (2)	5.4%
Australia	16 (4)	3.4%
South Korea	3 —	3.0%
Denmark	8 (9)	2.2%
Sweden	7 (10)	2.1%

Source: Pensions & Investments and Towers Watson (2015), *P&I/TW 300 Analysis Year End 2014*

Table 2: PRI Signatories by Country (as of November 9, 2015)

Asset owners		Investment managers	
U.K.	43	U.S.	183
Netherlands	37	U.K.	133
Australia	34	France	118
Canada	25	Australia	74
U.S.	24	Switzerland	44
Brazil	17	Netherlands	43
Germany	17	Canada	33
Sweden	16	South Africa	32
France	11	Brazil	29
Finland	11	Germany	28
Japan	9	Sweden	27
New Zealand	8	Finland	23
Spain	8	Japan	22
Switzerland	7	Spain	19

Source: Produced by the author based on information available on the PRI official website (http://www.unpri.org/)

2 Trends of Individual Investors

1. Investment Trusts

This section mainly covers the trends of SRI investment trusts—a financial product for individual investors that is geared toward sustainable investment—over the two-year period from the publication of the *2013 Review of Socially Responsible Investment in Japan* until the end of September 2015.
(Please see inside cover: JSIF's SRI Standard regarding the scope of calculations in this report.)

(1) Current Circumstances Pertaining to SRI Investment Trusts

Sixteen years have passed since the birth of SRI investment trusts in 1999. At one point in 2007, the net asset balance of these trusts expanded to exceed ¥1.0 trillion, but since the second half of 2011, it has been fluctuating between ¥210.0 billion and ¥260.0 billion. Over the last few years, a relatively favorable investment environment has continued, and the number of individual investors with a positive attitude toward asset management is growing. According to statistics from the Trust Companies Association of Japan, the net asset balance of public investment trusts (excluding public bond investment trusts) was ¥62.425 trillion in September 2013, and as of September 2015, this had risen 23.5%, to ¥77.0807 trillion. On the other hand, the net asset balance of SRI investment trusts fell 11.5%, from ¥244.0 billion to ¥216.0 billion over the same period.

If we classify SRI investment trusts in terms of investment scope and evaluation criteria, we can see that, in terms of investment scope, the proportion of the net asset balance allocated to domestic stock funds has risen from 42.4% to 54.5% compared with figures recorded at the end of September 2013, and the proportion allocated to international stock funds has fallen from 50.0% to 40.2%.

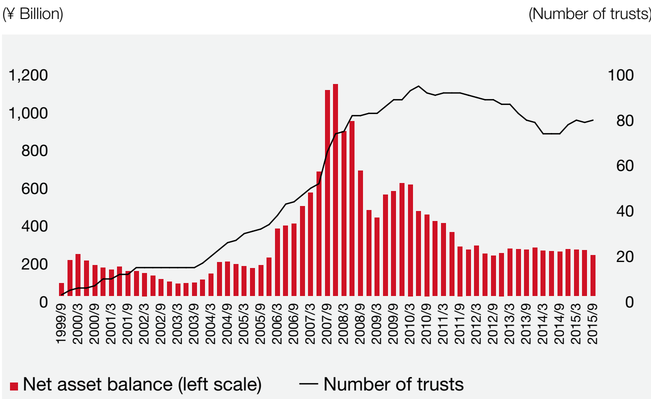
In terms of evaluation criteria, funds that included the environment as one of their evaluation benchmarks represented over 70% of the overall net asset balance at the end of September 2013. This figure, however, had fallen to 58.6% at the end of September 2015. In contrast, the proportion of the net asset balance composed of funds geared toward themes other than the environment or CSR has grown to exceed 10%. These themes include womenomics (as discussed below, many new funds based on this theme have been established over the last two years), employment, health, and sharia compliance.[1]

As ever, the international stock fund/environment combination represents the highest proportion of the net asset balance in terms of definitive totals. The composition of the balance is, however, slowly beginning to change.

(2) SRI Investment Trusts: New Trusts and Trusts That Have Reached Maturity

As reflected by Figure 2.1.2, the number of SRI investment trusts peaked at the end of June 2010 at 94 before falling into a trend of decline. This trend later subsided, and at the end of September 2015 there were 74. To observe this trend in detail, the bar graph in Figure 2.1.3 shows the number of newly established trusts on the positive axis and mature trusts on the negative axis. For over three years from the first half of 2011, there was a continuing trend of no new establishment. However, from the second half of 2014, we can see that newly established trusts have come to exceed mature trusts.

Figure 2.1.2: Trend in the Number and Net Asset Balance of SRI Investment Trusts



Source: Produced by the author using JSIF materials

Table 2.1.1: SRI Investment Trust Net Asset Balance by Category (at the end of September 2015) (¥ Million)

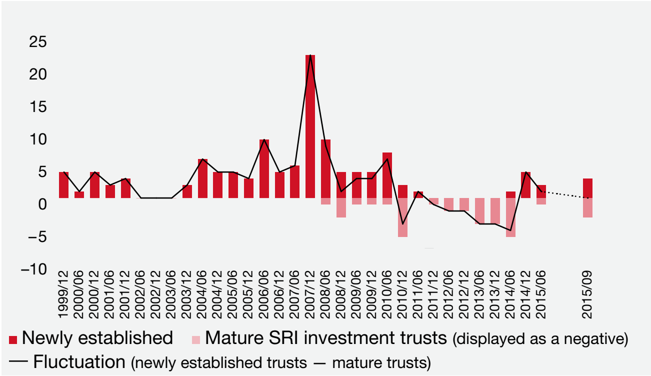
Evaluation criteria	Investment scope						Total	Proportion	Reference values (at the end of September 2013)
	Domestic stocks	Domestic bonds	Domestic compound assets	International stocks	International bonds	International compound assets			
Environment	41,474	—	—	81,326	3,196	536	126,532	58.6%	71.3%
CSR	58,868	—	—	3,087	—	5,513	67,468	31.2%	24.3%
Womenomics	12,218	—	—	—	—	1	12,219	5.7%	1.6%
Other	5,183	—	—	2,433	—	2,124	9,740	4.5%	2.7%
Total	117,743	0	0	86,846	3,196	8,173	215,958		
Proportion	54.5%	0.0%	0.0%	40.2%	1.5%	3.8%			
Reference values (at the end of September 2013)	42.4%	0.0%	0.2%	50.0%	2.5%	4.9%			

Source: Produced by the author using JSIF materials

[1] Investee corporations work to abide by Islamic laws and standards by not being involved in, or making an income less than a specified threshold from, the types of businesses that conflict with Islamic doctrines (which prohibit pork, alcohol, tobacco, weapons, gambling).

Figure 2.1.3: Trend in the Number of Newly Established and Mature SRI Investment Trusts

(Number of trusts)



Source: Produced by the author using JSIF materials

When we observe trusts in terms of evaluation criteria, we may note the characteristic that, over the last two years, six out of 10 newly established SRI investment trusts have been womenomics-focused. The number of these trusts has expanded from one to seven, and their net asset balance from ¥4.0 billion to ¥12.2 billion. Moreover, these womenomics-focused trusts are generally based on domestic stock investment, and, although their influence is still relatively small, they represent one of the reasons for the expansion in the proportion of the net asset balance composed of domestic stock.

The advancement of women as a theme is nothing new, but it does represent one of the policies that the Abe administration is actively working to promote. The "Japan Revitalization Strategy" (June 2013), a key policy of Abenomics' growth strategy, emphasizes that "In particular, it is essential for the 'power of women'—Japan's greatest potential which has not been leveraged fully to date—to be fully utilized. This is critical from the standpoint of securing human resources who will support the new growth sectors amid concerns over the decreasing workforce population due to the declining birthrate and aging population. Promoting women's participation in the labor force and in management roles will lead to the creation of new services and products that will reflect a diverse sense of values more than ever before, and bring vitality to the entire society." This expresses the government's stance to actively encourage corporations to expand the employment and appointment of women, while working toward the advancement of women in general.

Every year since 2013, the Ministry of Economy, Trade and Industry (MITI), in collaboration with the Tokyo Stock Exchange, has been selecting and publicizing listed corporations that have demonstrated exceptional performance in the advancement of women as "Nadeshiko Brands." Moreover, the Cabinet Office has been urging listed corporations to include the status of their initiatives toward the advancement of women in their corporate governance reports. In addition, under the Act to Advance Women's Success in Their Working Life, which came into effect in April 2016, corporations that employ over 301 workers are required to publicize the status of such initiatives, and the Ministry of Health, Labour and Welfare is due to publicize a database comprising a collation of this information.

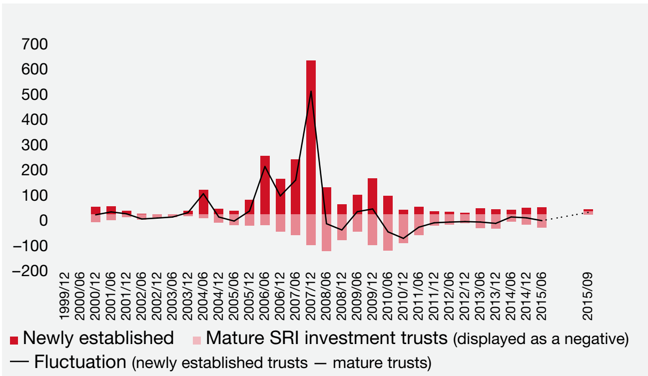
Also, in June 2014 the "promulgation of health management" was added to the Japan Revitalization Strategy, and in 2015, MITI began collaborating with the Tokyo Stock Exchange to select and publicize "Health Management Brands," while working toward the establishment of information disclosure guidance pertaining to health management.

(3) Capital Flows of SRI Investment Trusts

To better understand the finer details of current circumstances pertaining to SRI investment trusts, we can observe capital trends. Figure 2.1.4 shows net capital inflow of SRI investment trusts with repurchase or redemption figures deducted from sales. We can see that from the first half of 2010 there was a continuous net decline in capital, but the scale of this continues to diminish. In the third quarter of 2015 (July–September), however, there were small, consecutive net increases over a period of three months.

Figure 2.1.4: Capital Flow of SRI Investment Trusts

(¥ Billion)



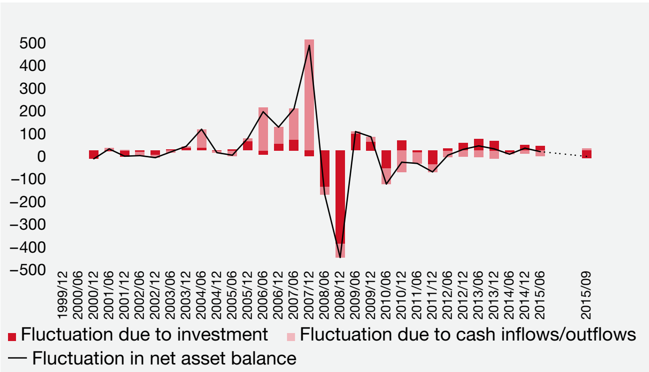
Note: No data is available prior to January 2000.

Source: Produced by the author using JSIF materials

By deducting capital inflow from the increase or decrease in net assets, we can see how the increase and decrease of the net asset balance is affected by investments and the payment of dividends. If we look at these trends (Figure 2.1.5) together with Figure 2.1.3, we can see that until 2007 capital inflow was consistent with the establishment of funds. However, following the confusion of the 2008 financial crisis, capital flows have continued to demonstrate net losses since 2010, regardless of trends pertaining to new fund establishment or maturity. This net decline has continued from the second half of 2014, even when the number of funds began to rise again. Recent years have seen the investment environment remain relatively favorable, and we can see an increase in the net asset balance as a result of investments. However, this increase has been offset by the capital outflows from repurchases and redemptions and, on the whole, the total net asset balance has remained stagnant with little to no increase or decrease. As stated above, capital flows experienced a net increase in the third quarter of 2015 (July–September); however, this has been offset by little or no returns on investment and a decrease in the net asset balance, which we can attribute to a worsening environment, including rising concerns over the Chinese economy.

Figure 2.1.5: Analysis of Causes for Fluctuation in the Net Asset Balance

(¥ Billion)



Note: No data is available prior to January 2000.
Source: Produced by the author using QUICK-provided data and JSIF materials

(4) Conclusion

As outlined above, there has not been significant change in the net asset balance of SRI investment trusts over the last few years. Although the pace at which funds reach maturity has slowed, there have been a few new funds established in the three-year "blank period" since the first half of 2011. Regarding specific evaluation criteria, we have begun to see signs of diversification/dispersion, such as a rising number of funds with a theme of womenomics. In addition to this "renewal," there has also been a gradual dilution of the overemphasis on the "international stock fund/environment" combination. This is due to the continuation of a trend over the last two years, first pointed out in the 2013 report, in which international stock proportions have decreased as domestic stock proportions have increased.

If we now shift our focus to the sales side, including securities companies and other financial institutions, the Financial Services Agency has, in recent years, adopted a rigid stance against commission-focused sales by urging securities companies to change their sales strategies from rapid switch proposals aimed at a limited number of existing clients to a focus on the expansion of their assets under custody and client bases. The "Financial Regulatory Policy 2015," published in September 2015, outlined a policy of "optimizing fiduciary duty" and, in particular, clarified its intention to seek improvement from securities companies, stating that "it has been pointed out that there is a problem with securities companies pursuing commission-based profits by churning investment trusts, a management practice that is counter to client interests."

According to the July 2015 *Financial Monitoring Report*, over 60% of securities companies are already placing more importance on assets under custody and the expansion of their client bases as performance indicators to evaluate sales of investment trusts in comparison to previous years.

Such changes in the approach toward the sale of investment trusts have given rise to a number of trends including an increase in the sale of wrap accounts (discretionary investment management services) and wrap-style investment trusts (a kind of balanced-oriented investment trust). The social aspect of SRI investment trusts may also elicit interest from those who are not particularly concerned with investment, with the added incentive that these trusts also allow for medium- to long-term investment. It will therefore be interesting to see whether SRI investment trusts, with such high marketability, will be able to strengthen their presence going forward.

When referring to net assets in this section, apart from specified instances, non-SRI assets for SRI hybrid investment trusts (investment trusts that are not wholly based on SRI, such as those based on 50% SRI and 50% non-SRI) are excluded.

Moreover, net assets include defined contribution (DC) pension plan specific funds and ETFs. In addition, for comparison purposes, various numerical data has been retroactively recalculated, so please note that some figures do not correspond with those in the *2013 Review of Socially Responsible Investment in Japan*.

Also, various data provided by QUICK Corp. has contributed to the writing of this section.

Masaru Otake

2. Bonds

(1) The Origins of Impact Investment Bonds

Impact Investment bonds are currently showing signs of expansion both domestically and overseas. The origins of this type of financial product, which balances investment returns with social contribution, can be traced back to Vaccine Bonds[1] issued by the International Finance Facility for Immunisation (IFFIm) in overseas capital markets from November 2006.

Of the various Impact Investment bonds that have entered the markets, the Vaccine Bond remains the one thought to be the most transparent in terms of how capital is allocated, and this represents the impetus behind the IFFIm's establishment as an organization. The IFFIm was established in 2006 to procure capital from capital markets to fund the activities of the GAVI Alliance, an organization that conducts vaccination programs in over 70 developing countries. Its primary sources of funding are donations from developed countries, including the United Kingdom and France, although various governments have been making annual donations to the IFFIm for several years. Despite these efforts, many children around the world are still in urgent need of vaccination. To ensure that these children receive the necessary treatment without delay, the IFFIm issues bonds to provide funding for these vaccination programs. All capital invested in Vaccine Bonds can be utilized by immunization programs for children around the world; thus, Vaccine Bonds are thought to have both a high level of transparency and a significant impact investment. In terms of credibility, with a financial base made up of donations bearing legal restrictions from national governments, coupled with financial management provided by the World Bank, the IFFIm has obtained high sovereign ratings from the major rating companies. In Japan, it gained sovereignty in accordance with the Financial Instruments and Exchange Act in 2007 and is seen as a bond with a very high level of credibility. The Vaccine Bond has attracted widespread attention as a model case for financial functions in the development sector.

In 2007, the year following the introduction of the Vaccine Bond, the first environment-themed Impact Investment bond by an international institution entered the capital markets—the European Investment Bank (EIB)'s Climate Awareness Bond[2]. Although the establishment of the IFFIm represented a positive development in social contribution, the EIB is an international institution dedicated to supporting projects that contribute to the advancement of EU policy objectives, and is therefore involved in various businesses. From these businesses, it extracts only future projects that are related to the field of renewable energy and the improvement of energy efficiency. While maintaining transparency regarding the flow of capital to environmental initiatives, the EIB has implemented segregated management of capital procurement with the objective of enhancing transparency to conceive a new kind of Impact Investment bond with a high level of social contribution and transparency in capital flow that is not governed by the precepts of its issuing organization.

Another characteristic of this type of bond is that, in addition to the fact that it is issued with CO_2 emissions credits, returns are linked to indices. Also, it is a type of structured bond that utilizes progressive financial techniques, making it a financial product distinct from the simple product design of the Vaccine Bond.

Subsequently, in 2008 the World Bank introduced its environment-themed Green Bond[3]. Capital procured through green bonds is loaned to the World Bank's development projects to reduce greenhouse gas emissions and mitigate global warming—a prerequisite of green bonds by definition. Moreover, the World Bank adopts a segregated capital management method similar to that used by the EIB. These green bonds are supported by the high credibility of the World Bank and, in addition to having both a high potential for social contribution and capital flow transparency, they also comprise a simple product design similar to that of the Vaccine Bond. The World Bank's Green Bonds can therefore be thought of as the precursor to Impact Investment bonds, which continue to rise in popularity in capital markets both domestically and overseas.

The segregated capital management method used by the EIB and the World Bank is known as "ringfencing[4]." It represents a highly transparent capital management method and has recently been adopted for Impact Investment bonds by a large number of international institutions.

(2) Expansion of Impact Investment Bonds in Japan

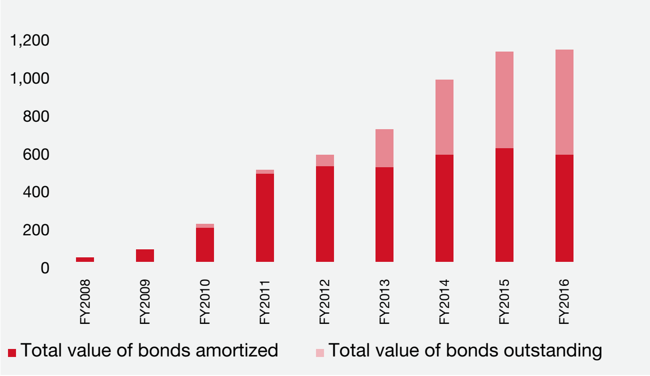
From this point, I would like to explain how Impact Investment bonds have become so deeply rooted in the Japanese capital markets. First, let us take a look at markets geared toward individual investors.

The first Impact Investment bonds available to individual investors in Japan were South African rand-denominated Vaccine Bonds, issued by the IFFIm in March 2008. Since then, the issue and sale of such bonds to individual investors have continued; total sales for 2014 exceeded ¥1.0 trillion, and the total sales and issue balance as of September 2015 were ¥1.12 trillion and ¥564.2 billion, respectively (calculated at the exchange rate when figures were published, excluding the decline of the balance due to redemption before maturity). In comparison with figures at the end of September 2013, total sales rose ¥327.9 billion, and the issue balance rose ¥89.6 billion; and, even after seven years since they were first introduced, Impact Investment bonds continue to show a trend toward growth. In accordance with this increase in total sales, Impact Investment bonds based on a wide variety of themes have come to be issued.

One of the most prominent market trends to come into the fray since the publication of the *2013 Review of Socially Responsible Investment in Japan* is the "Banking on Women Bond[5]," issued by the International Finance Corporation (IFC) in November 2013. This bond allocates capital to the IFC's "Banking on Women Program" in light of the importance of women's prosperity in business. The program aims to enhance financial services geared toward improving access to capital for women business owners, and it became Japan's first gender-themed Impact Investment bond.

Figure 2.2.1: Sales to Individual Investors

(¥ Billion)



Note: Figures for FY2016 reflect sales up to and including September.
Source: Daiwa Securities

It has been seven years since the issue of the first Impact Investment bond in Japan, and new patterns still continue to emerge. Why is it that this kind of bond has taken root so deeply in Japanese capital markets? The background behind this phenomenon lies in three elements: alignment with stakeholders, simple composition and high interest currencies, and the promulgation of "best effort" management[6].

Let us look at the first element, "alignment with stakeholders," from the perspective of investors. When Impact Investment bonds entered the Japanese capital markets in 2008, individual awareness of social issues such as environmental problems was continuing to grow year on year. With the financial crisis, investors began to reevaluate what represents the very foundation of investment—where capital is flowing. This led to a fusion between rising interest in social contribution and Japan's rich source of financial assets held by individual investors, making the establishment of a "social contribution through investment" model a relatively simple process.

If we now consider the issuer's perspective, issuance of Impact Investment bonds has become an opportunity to showcase business activities to a wide range of investors. With a high savings and deposits ratio, Japan's bond market for individual investors has been an important source of capital for overseas bond issuers. The successful entry of Vaccine Bonds and green bonds into this environment therefore drew a high level of interest from other bond issuers.

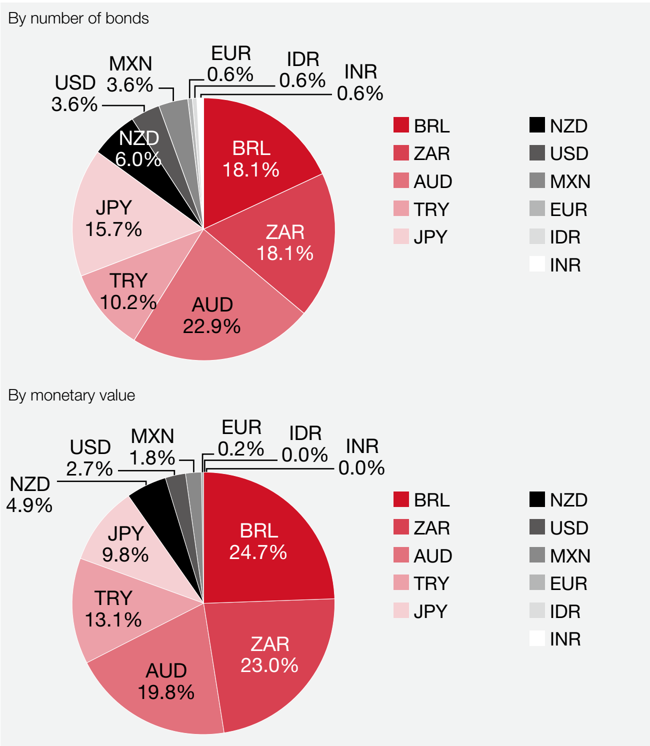
Finally, if we consider sales by securities companies, Impact Investment bonds represent a product that meets the needs of both issuer (borrower) and investor (lender) and, more specifically, can also be used as a product to attract new kinds of investors. Examples of small-scale impact investments, mainly by young people who are greatly concerned by social issues, can often be observed now. There is thus a rising expectation for Impact Investment bonds to act as a new way to encourage the shift from saving to investment.

Let us now consider the second element: "simple composition and high interest currencies." Simplified products are crucial to attracting a wide range of investors, unlike complicated, risky products, which cannot be expected to draw in such wide participation regardless of to what extent they may emphasize social utility. Impact Investment bonds tend to be bullet bonds with fixed rates, a type of bond that individual investors have become accustomed to, and feature relatively low exposure to default risks because they are issued by international institutions and private-sector financial institutions with high ratings, making them easy to invest in.

We must also consider that sales are predominantly made up of bonds in high interest currencies. As interest rates in Japan remain at an all-time low, the potential needs of investors, who favor high interest rates, are high. If we look at Impact Investment bonds sold to individual investors to date we can see that, excluding the Japanese yen, Impact Investment bonds denominated in the South African rand, the Australian dollar, the Brazilian real, the New Zealand dollar, and the Turkish lira accounted for 75% of all bonds sold on a numerical basis and 85% on a monetary basis.

It could be said that these Impact Investment bonds have succeeded in creating new social value by leveraging the high interest of bonds denominated in foreign currencies while focusing the use of capital to address specific social issues, and packaging all of this into a simple product design.

Figure 2.2.2: Impact Investment Bonds by Currency Denomination (total by volume/monetary value at the end of September 2015)



Source: Daiwa Securities

The final element pertains to "the promulgation of 'best effort' management." The aforementioned "ringfencing" capital management method places a considerable administrative burden upon bond issuers. As a result, there have been many cases where ringfencing has become an obstacle to the issuance of Impact Investment bonds. However, the "Microfinance Bond," issued by the IFC in November 2009, adopted a form of capital management called "best effort" management. This method, which does not involve segregated management of capital, significantly reduces the administrative burden placed on the issuing body. The method therefore came to contribute significantly to the expansion of Impact Investment bond themes in Japanese capital markets.

The "best effort" management method has the problem of not being as transparent in terms of capital flows as ringfencing from the perspective of investors. To resolve this problem, bond issuers and securities companies have worked to improve transparency by hosting IR seminars and issuing sales pamphlets with easy-to-understand examples. As a result of these efforts, "best effort" capital management has been widely accepted by individual investors, and as themes have diversified, investor options have expanded, leading to a virtuous cycle where investor attention is focused on new themes.

If we look at the issuance and sale of Impact Investment bonds to institutional investors, we can see that from summer 2010, issuance and sales targeting specific investors, including regional banks, expanded rapidly. Between 2010 and 2012, 20 different types of bonds, amounting to ¥25.5 billion, were issued. From 2013, however, things began to quiet down. Impact Investment bonds in Japanese capital markets have traditionally been focused on individual investors. It may be time, however, to change perspectives and to focus on markets overseas.

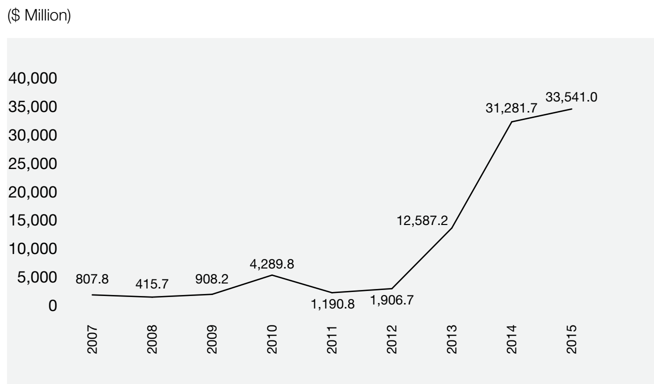
(3) The Expansion of Impact Investment Bonds Overseas

Since the introduction of the Vaccine Bond in 2006, and the Green Bond in 2008, what kind of progress have Impact Investment bonds achieved in overseas capital markets?

The World Bank's Green Bond, issued in 2008, was conceived in part as one aspect of the Scandinavian Pension Fund's socially responsible investment initiatives, as the fund hoped to issue a bond that allocated capital specifically to support the prevention of global warming[7]. These types of public-sector institutional investors tend to favor the transparency offered by capital management methods such as ringfencing. As such, in overseas capital markets, bond issuers often fail to see any upside to the comparatively heavy administrative burden imposed by socially responsible investment, and the number of bodies that issue new Impact Investment bonds have thus become limited. However, as in the model case of the Scandinavian Pension Fund, a public investor, a gradual broadening of attitudes toward social responsibility and ESG in bond investments has led to an increase in the number of investors that incorporate socially responsible investment into their investment portfolios. As the benefit of expanding investor bases has been recognized among bond issuers, the issuance of Impact Investment bonds increased gradually throughout the period between 2012 and 2013.

The most significant turning point in the overseas capital markets was probably the publication of the Green Bond Principles (GBP)[8] in January 2014. This established the definition and composition of green bonds (Use of Proceeds / Process for Project Evaluation and Selection / Management of Proceeds / Reporting), and represented the world's first independent guideline with the objective of enhancing transparency in the expanding green bond markets. Administered by the International Capital Market Association (ICMA), the GBP were produced with oversight from bond issuers, investors, underwriting financial institutions, and environmental experts. Once the GBP had been established, a large number of bond issuers, including private companies, started to issue Impact Investment bonds in the context of improving green bond transparency, and the scale of the market expanded significantly. If we look at the total sales of green bonds alone, over US$30.0 billion worth were issued in 2014. Moreover, 2014 also heralded the issue of the "DBJ Green Bond" by the Development Bank of Japan, the first green bond by a Japanese bond issuer to be issued in overseas bond markets.

Figure 2.2.3: Trend in Issuance of Green Bonds



Note: The total value of bonds classified as green bonds by Bloomberg.
Source: Compiled by Daiwa Securities through Bloomberg

With the publication of the GBP, the number of new theme-based Impact Investment bonds available is increasing. Through a change in capital flows based on the GBP's ethos as a whole, types of high transparency Impact Investment bonds based on themes other than those of green bonds are also being issued. For example, the Education, Youth, and Employment (EYE) Bond[9] was issued by the Inter-American Development Bank (IDB) in September 2014. This bond allocates capital to finance the EYE Bond Program, which contributes to education, youth support, and employment support programs in South and Central America, and in various regions of the Caribbean.

In this way we can see that, although individual investors have traditionally promulgated the bulk of Impact Investment bonds in Japanese capital markets, the opposite trend is true for overseas capital markets, where institutional investors purchase the bulk of such bonds. As a result, we can see that, particularly in recent years, sales of Impact Investment bonds in overseas capital markets have continued to significantly outpace those in Japanese Impact Investment bond markets.

(4) Future Outlook

If we consider Japan from an overseas perspective, we can see that institutional investors are becoming more and more important to the further expansion of its Impact Investment bond markets. As of recently, positive moves toward the realization of this goal are taking place, particularly at life insurance companies. Many life insurance companies treat investment in Impact Investment bonds as a growth investment, and regularly disclose such initiatives in press releases.

In September 2015, the Japanese Government Pension Investment Fund (GPIF) became a signatory to the UN Principles for Responsible Investment (PRI)[10]. The GPIF urges its affiliated asset management institutions to become signatories to PRI and to inform them of their activities pertaining to this. If an institution is not a signatory, GPIF expects to be given an acceptable reason. GPIF's signing on to PRI therefore has the potential to further promulgate the concept of ESG among Japanese institutional investors.

In addition to movement by investors, Japanese bond issuers are also making gradual progress. In September 2015, the DBJ issued its Sustainability Bond, which expanded on the scope of assets included in the DBJ Green Bond, issued in September 2014. At the same time, Sumitomo Mitsui Banking Corporation issued what was to become the first green bond by a Japanese bank.

Examples of model cases, from the perspective of both investors and bond issuers, are gradually beginning to present themselves, and the scene is being set to encourage further acceleration of the trend toward sustainable investment in Japan's capital markets. To strengthen this trend, investors, bond issuers, and securities companies must cooperate with each other, involving the government where appropriate, to expand the markets going forward.

Ken Tokuda

1. Referenced IFFIm's homepage (http://www.iffim.org/)
2. Referenced EIB's homepage (http://www.eib.org/investor_relations/cab/index.htm)
3. Referenced the World Bank's homepage (http://www.worldbank.or.jp/debtsecurities/cmd/htm/WorldBankGreenBonds.html)
4. Ringfencing: by recording capital procured in a separate account from the general account, this method ensures that capital is used for strictly defined purposes. Needless to say, the advantage of ringfencing is that the use of invested capital is transparent. However, this may not be effective for overall capital management if bond issuers have to take the trouble to manage procured capital in different ways.
5. IFC press release (http://ifcext.ifc.org/IFCExt/pressroom/IFCPressRoom.nsf/0/31A3A5FE75BD940C85257C350074093A?OpenDocument)
6. "Best Effort" Management entails investment of procured capital in previously specified fields. These are made clear in sales pamphlets and other materials, but are not legally enforced, and there are no separate accounts. As there is no need for new operations to manage capital, bonds can easily be issued.
7. Referenced the World Bank's homepage (http://www.worldbank.or.jp/debtsecurities/cmd/pdf/WhatareGreenbonds.pdf)
8. ICMA Green Bonds (http://www.icmagroup.org/Regulatory-Policy-and-Market-Practice/green-bonds/)
9. IDB EYE Bond Program (http://www.iadb.org/en/idb-nance/investors/eye-bondprogram,18001.html)
10. GPIF press release (http://www.gpif.go.jp/topics/2015/pdf/0928_signatory_UN_PRI.pdf)

3 Shareholder Advocacy

1. “Abenomics” and Corporate Governance

(1) Corporate Governance Reform as One of the Pillars of the Japan Revitalization Strategy

Since the launch of the “Japan Revitalization Strategy -JAPAN is BACK-,” in June 2013, which represents the third arrow of Abenomics’ growth strategy, the Abe Cabinet has issued revisions to the Strategy every year in June together with renewed three–five year roadmaps.

The Strategy covers a wide range of areas, but one policy seen to have delivered concrete results is the Corporate Governance Reform. The main measures implemented at the end of November 2015 that are significant to this aspect, including pension fund reform and Ito Review, are summarized in the chart below.

Figure 3.1.1: Main Corporate Governance Measures and Related Activities

Year	Government	Stock Exchange/Corporation	Asset Owner/Asset Manager	Other
2012	December: Inauguration of the Abe administration			
2013	June: Japan Revitalization Strategy (Cabinet Office) “Japan is Back”			
2014	February: Japan’s Stewardship Code (Financial Services Agency) “To promote sustainable growth of companies through investment and dialogue” August: Ito Review (Ministry of Economy, Trade and Industry) “Constructive Dialogue toward Sustainable Growth of Companies” “ROE 8%”	January: JPX Nikkei 400 (Tokyo Stock Exchange) “ROE, Outside Director”	March: Manager selection (GPIF) Smart Beta /Index “Selection of active asset managers with distinctive style” October: Change in Asset Allocation (GPIF) “25% allocation to Japanese stocks”	May: Japan Revival Vision (Liberal Democratic Party) “Two or more independent directors” “Reducing cross-shareholding”
2015	March: Corporate Governance Code (Financial Services Agency, Tokyo Stock Exchange) “Sustainable Growth of Japanese Companies” and “Medium- to Long-Term Growth of Corporate Value” May: Revised Companies Act goes into effect	June: Corporate Governance Code goes into effect: Corporations begin to implement disclosure through a new format for Corporate Governance reports (Companies that settle accounts in March required to disclose new reports by December)	February: Investor Forum (institutional investors) “Purposeful dialogue between corporations and investors” and “Open discussion” September: GPIF becomes a signatory to PRI	February: Application of ROE standards (ISS) “Recommendation to oppose the re-election of top management at companies with an ROE average of less than 5% over 5 fiscal years”

Source: Compiled from various reports and articles by author, including websites of the Japanese government, Cabinet Office, Ministry of Finance, and Ministry of Economy, Trade and Industry

(2) Japan’s Stewardship Code and Corporate Governance Code

Each of the above measures has had a significant impact, but it was the introduction of the Principles for Responsible Institutional Investors, i.e., Japan’s Stewardship Code, and the Corporate Governance Code that represented the most significant cause for change in the relationship corporations have with shareholders and investors, primarily institutional investors.

The Principles for Responsible Institutional Investors, the so-called “Japan’s Stewardship Code,” comprise seven principles, and asset owners, asset managers who invest in Japanese equities, service providers, and other providers of capital have become signatories. The principles were established in February 2014, and by the end of November 2015, 201 institutions, including overseas institutions, were signed up. Most of the major asset managers in Japan are signatories. Also, public pension funds such as the Government Pension Investment Fund (GPIF), which is the world’s largest holder of assets under management with over ¥135.0 trillion, as well as life insurance companies and other associated institutions have become signatories.

The scope of the Corporate Governance Code covers listed companies in Japan and was put into effect on June 1, 2015. It comprises 5 general principles, 30 principles, and 38 supplementary principles, for a total of 73 principles. All companies listed on the First and Second sections of the Tokyo Stock Exchange have a duty to comply, or otherwise explain their inability to comply with all of these principles, and those companies listed on JASDAQ and Mothers are only required to comply with the five key principles. The format of corporate governance reports has changed in line with the introduction of the Code, and, from June 2016, corporations are required to provide reports in the new format within six months from the end of their annual general meetings of shareholders. At the end of November 2015, a total of 1,089 companies—approximately 30% of listed companies—have been submitting reports in the new format.

We must bear in mind, however, that the two codes are not legally binding. Both propose principles (or "best practices") and introduce the U.K.-style "comply or explain" framework (when it is not possible to comply, corporations must explain the reasons why). Until now, most Japanese corporations have operated on a rules-based system where regulations are decided and subsequently complied with. Consequently, when suddenly asked to provide explanations as to why, for example, it does not have more than one outside director, a company may not find this to be a necessarily simple task. And as the new system has been put in place fairly recently, there are many corporations that are simply not used to it yet.

"Engagement" is the word that links the two codes together. Japan's Stewardship Code defines "engagement" as "constructive, purposeful dialogue." This implies not only simple communication, but also dialogue to urge improvements and changes to a corporation's activities and structure. The word "engagement" was first used in the context of corporate governance by institutional investors in the U.K.; however, the word has come to be commonly used by investors in the U.S., Europe, and Asia. Corporate governance to date, both domestically and overseas, has focused on compliance related to corporate corruption (legal compliance), and functions to monitor compliance through outside directors, and remuneration for directors and corporate auditors. Corporate governance in the context of Abenomics policy, however, is focused on the enhancement of corporate value; the Code itself includes the following in its preface: "It is important that companies operate with full recognition of the responsibilities they have to a wide range of stakeholders, starting with the fiduciary responsibility that shareholders have entrusted them with. In addition to the fulfillment of companies' accountability in relation to these kinds of responsibilities, the Code aims for 'growth-oriented governance' by promoting timely and decisive decision-making on the condition that transparency and fairness is guaranteed in that decision-making. The Code does not place excessive emphasis on avoiding and limiting risk or the prevention of corporate scandals. Rather, its primary purpose is to stimulate healthy corporate entrepreneurship, support sustainable corporate growth, and increase corporate value over the medium to long term."

2. ESG Shareholder Proposals in Japan

Alongside the widespread adoption of PRI and corporate governance reform as well as other measures, engagement continues to root itself deeper as an important approach by institutional investors, and collective engagement continues to proliferate between multiple investors in Europe and the U.S. Engagement has also garnered attention in Japan, as we can see from the examples of the Ito Review and the introduction of the two aforementioned codes. Proxy voting by institutional investors also garners public attention. However, when it comes to actual investor/corporation engagement, although many corporations have been publishing information in reports and on websites, public arenas allowing for face-to-face dialogue remain very few, and efforts to connect with society are predominantly made up of reports and shareholder proposals.

As described in previous editions of this white paper, for many years in Japan, anti-nuclear groups have submitted shareholder proposals to electric power companies. These kinds of shareholder proposals are generally submitted by groups of individual shareholders that hold relatively very few shares, but who have secured the voting rights to satisfy the minimum threshold to make shareholder proposals. In recent years, however, proposals by individual shareholders acting autonomously, institutional investors, and major shareholders (individuals, investment companies, and municipal bodies) have become increasingly more common. Many of these aim to increase involvement in company management through demands to elect outside directors/outside corporate auditors and enhance managerial transparency.

As items requiring resolution at general shareholders' meetings are determined by the Companies Act, shareholder proposals frequently endeavor to change a company's articles of incorporation. For a changed resolution to be passed, at least two-thirds of the shareholders present, including those who submitted votes in advance, are required to vote in agreement. In the U.S., there are many cases where shareholder proposals are non-binding, meaning that even if a proposal is backed by a majority, it can still be overridden by a rejection from the board of directors. It must be noted that in Japan, however, all resolutions at general shareholders' meetings are legally binding.

Submission of shareholder proposals at general shareholders' meetings between July 2014 and June 2015 (at both regular and special meetings) are summarized in the table below.

Table 3.1.2: Shareholder Proposals from July 2014 to June 2015

Company Name	Securities Code	Market	Section	Month/Year of General Meeting	Proposal
TOWNNEWS-SHA CO., LTD.	2481	JASDAQ		Sept. 2014	1: Dividends of surplus, 2: Repurchase of treasury stock
INTELLIGENT WAVE Inc.	4847	JASDAQ		Sept. 2014	1: Repurchase of treasury stock
MIYAIRI VALVE MFG Co., Ltd.	6495	Tokyo	2nd	Sept. 2014*	1: Dismissal of corporate auditor(s), 2: Appointment of corporate auditor(s), 3: Dismissal of director(s), 4: Appointment of director(s)
Tsunoda Co., Ltd.	7308	Nagoya	2nd	Sept. 2014	Total of 10 proposals including partial amendments to the Articles of Incorporation and election and dismissal of director(s) and corporate auditor(s)
MEDINET CO., LTD.	2370	Tokyo	Mothers	Oct. 2014*	1: Dismissal of 2 directors, 2: Appointment of 6 directors
PRAP Japan, Inc.	2449	JASDAQ		Nov. 2014	1: Appointment of director(s)
USEN CORPORATION	4842	JASDAQ		Nov. 2014	Partial amendments to the Articles of Incorporation: 4 items
Mandarake Inc.	2652	Tokyo	Mothers	Dec. 2014	1: Appropriation of surplus, 2: Repurchase of treasury stock
Alphax Food System Co., Ltd.	3814	JASDAQ		Dec. 2014	1: Dismissal of 4 directors, 2: Appointment of 2 directors, 3: Appointment of 1 corporate auditor, 4: Appointment of accounting auditor(s)
Kyodo Public Relations Co., Ltd.	2436	JASDAQ		Mar. 2015	Appointment of 5 directors
Japan Tobacco Inc.	2914	Tokyo	1st	Mar. 2015	1: Dividends of surplus, 2: Repurchase of treasury stock
Seiwa Chuo Holdings Corp	7531	JASDAQ		Mar. 2015	Appointment of 2 directors
Otsuka Kagu Ltd.	8186	JASDAQ		Mar. 2015	1: Appointment of 10 directors, 2: Appointment of 2 corporate auditors
Tri-Stage Inc.	2178	Tokyo	Mothers	May 2015	1: Appointment of director(s), 2: Abolition of takeover defense measures, 3: Appropriation of surplus
WAKITA Corporation	8125	Tokyo	1st	May 2015	Dividends of surplus
fonfun corporation	2323	JASDAQ		June 2015	Appointment of 6 directors
Pro-Ship Incorporated	3763	JASDAQ		June 2015	Appropriation of surplus
Oji Holdings Corporation	3861	Tokyo	1st	June 2015	Partial amendments to the Articles of Incorporation
FUJI MEDIA HOLDINGS, Inc.	4676	Tokyo	1st	June 2015	Total of 9 proposals including partial amendments to the Articles of Incorporation and election of directors
JFE Holdings, Inc.	5411	Tokyo	1st	June 2015	Dismissal of director(s)
HOKUETSU METAL Co., Ltd.	5446	Tokyo	2nd	June 2015	1: Appointment of 2 directors, 2–3: Partial amendments to the Articles of Incorporation
MITSUI MINING & SMELTING CO., LTD.	5706	Tokyo	1st	June 2015	1: Dismissal of CEO, 2: Appropriation of surplus, 3: Repurchase and retirement of treasury stock
OSAKI ENGINEERING CO., LTD.	6259	JASDAQ		June 2015	1: Repurchase of treasury stock, 2: Appointment of 2 directors, 3–4: Partial amendments to the Articles of Incorporation
KANEMATSU ENGINEERING CO., LTD.	6402	Tokyo	2nd	June 2015	1: Election of 1 outside director, 2–3: Partial amendments to the Articles of Incorporation
Toshiba Corporation	6502	Tokyo	1st	June 2015	Partial amendments to the Articles of Incorporation: 7 items
Japan Digital Laboratory Co., Ltd.	6935	Tokyo	1st	June 2015	Appropriation of surplus
KAWASUMI LABORATORIES, INC.	7703	Tokyo	2nd	June 2015	Repurchase of treasury stock
HOYA CORPORATION	7741	Tokyo	1st	June 2015	1: Dismissal of 6 directors, 2: Appointment of director(s), 3–18: Partial amendments to the Articles of Incorporation
DAINIHON WOOD-PRESERVING CO., LTD.	7907	Nagoya	2nd	June 2015	Appropriation of surplus
Mitsui & Co., Ltd.	8031	Tokyo	1st	June 2015	1–6, 9: Partial amendments to the Articles of Incorporation, 7: Dismissal of outside director(s), 8: Repurchase of treasury stock
Mitsubishi UFJ Financial Group, Inc.	8306	Tokyo	1st	June 2015	Partial Amendments to the Articles of Incorporation: 2 items
Shikoku Bank, Ltd.	8387	Tokyo	1st	June 2015	1: Partial amendments to the Articles of Incorporation, 2: Dismissal of 5 directors, 3: Election of 1 corporate auditor
Mizuho Financial Group, Inc.	8411	Tokyo	1st	June 2015	1–10: Partial amendments to the Articles of Incorporation
Seibu Holdings Inc.	9024	Tokyo	1st	June 2015	1: Appropriation of surplus, 2: Partial amendments to the Articles of Incorporation, 3: Appointment of director(s)
Tokyo Electric Power Company, Inc.	9501	Tokyo	1st	June 2015	1–15: Partial amendments to the Articles of Incorporation
Chubu Electric Power, Incorporated	9502	Tokyo	1st	June 2015	1–8: Partial amendments to the Articles of Incorporation
Kansai Electric Power Company, Inc.	9503	Tokyo	1st	June 2015	1–6, 8–22: Partial amendments to the Articles of Incorporation, 7: dismissal of director(s)
The Chugoku Electric Power Company, Inc.	9504	Tokyo	1st	June 2015	1–5: Partial amendments to the Articles of Incorporation
Hokuriku Electric Power Company, Inc.	9505	Tokyo	1st	June 2015	1–8: Partial amendments to the Articles of Incorporation
Tohoku Electric Power, Incorporated	9506	Tokyo	1st	June 2015	1–4: Partial amendments to the Articles of Incorporation
Shikoku Electric Power Company, Inc.	9507	Tokyo	1st	June 2015	1–2: Partial amendments to the Articles of Incorporation, 3: Dividends of surplus
Kyushu Electric Power, Incorporated	9508	Tokyo	1st	June 2015	1–7: Partial amendments to the Articles of Incorporation
Hokkaido Electric Power Company, Inc.	9509	Tokyo	1st	June 2015	1–6: Partial amendments to the Articles of Incorporation
CHARLE CO., LTD.	9885	Tokyo	2nd	June 2015	Appropriation of surplus

Note: Shaded areas represent examples of where shareholder proposals have been approved.

* Special meetings

Source: Produced by the author using *Shojihomu:* document edition, various reports, and published documents

3. Changes in Japanese Institutional Investors' Attitude toward ESG—A Recent Trend at General Shareholders' Meetings

Japanese institutional investors' attitude toward ESG has changed steadily since publication of the last report. The number of PRI signatories when the last review was published stood at 28 institutions. Since then, a further 13 institutions have become signatories, and subtracting three institutions that have withdrawn themselves, the total number of signatories has expanded to 38. Moreover, with GPIF's signing on to the Principles in September 2015, the number of signatory institutions in Japan looks set to rise further.

Table 3.1.3: Japanese PRI Signatories
(as of December 1, 2015)

Asset Owners (pension funds, insurance, etc.): 9 (5 new, 1 withdrawal)
MS&AD Insurance Group Holdings
Dai-ichi Life Insurance
~~Fuji Pension Fund~~
Government Pension Investment Fund
Kikkoman Corporation Pension Scheme
SECOM Pension Fund
Sompo Japan Nipponkoa Insurance
Sophia University
Taiyo Life Insurance Company
Tokio Marine & Nichido Fire Insurance
Asset Management Institutions (trust banks, investment trusts, investment consultants, etc.): 22 (5 new, 1 withdrawal)
ACA Innovative Investment Management
~~AI Capital~~
Asahi Life Asset Management
Chuo Mitsui Asset Trust and Banking
Daiwa SB Investments
Daiwa Securities Trust and Banking
DIAM Asset Management
HC Asset Management
J-Star
Misaki Capital
Mitsubishi Corp. - UBS Realty
Mitsubishi UFJ Trust and Banking Corporation
Mizuho Trust & Banking
MU Investments
Nikko Asset Management
Nissay Asset Management
Nomura Asset Management
Resona Trust & Banking
Sompo Japan Nipponkoa Asset Management
Sumitomo Mitsui Asset Management
Sumitomo Mitsui Trust Bank
T&D Asset Management
Tokio Marine Asset Management
Tokio Marine Capital
Service Providers: 7 (3 new, 1 withdrawal)
Ark Alternative Advisors
CSR Design Green Investment Advisory
Edge International
~~Good Bankers~~
Integrex
Neural
QUICK
Tsunagiba

Note: Figures in parentheses represent movement since publication of the last report. Shaded areas represent new signatories. Strikethrough represents institutions that have withdrawn from PRI.
Source: Produced by the author from information available on the PRI website

Accompanying this movement, Japanese institutional investors are gradually becoming stricter in exercising voting rights and most of their proxy voting guidelines are approaching global standards. Ten or more years ago, Japanese institutional investors supported all management proposals, but now it is considered reasonable to oppose company proposals and support shareholder proposals instead. In 2011, for example, Nomura Asset Management changed its policy by expressing opposition to takeover defense measures in principle. Institutional investors are also increasingly pursuing engagement with companies, mainly in the corporate governance field. Almost none of the activities described above are taking place publicly, but there is lively discussion on issues related to the independence and skills of outside directors and outside corporate auditors, board diversity, and the status of director compensation and retirement benefits. Through this discussion, corporations are increasingly selecting outside directors with a high level of autonomy, introducing performance-based director compensation, and abolishing retirement benefits systems. Moreover, engagement by institutional investors continues to urge corporations to enhance their corporate governance.

Akemi Yamasaki

4 Sustainable Finance

1. Principles for Financial Action

(1) Principles for Financial Action for the 21st Century

Initiatives geared toward the realization of a sustainable society through financial markets are implemented within the parameters of numerous international frameworks established since the 1990s, and include the United Nations Environment Programme Finance Initiative (UNEP FI), Principles for Responsible Investment (PRI), Principles for Sustainable Insurance (PSI), and the Equator Principles for Project Finance. Japan's version for these activities is represented by the Principles for Financial Action towards a Sustainable Society (Principles for Financial Action for the 21st Century). The Principles were drawn up by a Drafting Committee and established in October 2011. Four years later, in September 2015, signatory institutions had expanded to 194 and extended across a wide sphere, from major banks, securities companies, and insurance companies, to regional and trust banks all over the country. We can therefore say that, at least on paper, a foundation has been established to promulgate ESG-considerate investment and financing, which straddles the borders between industrial sectors. So what can we say specifically about the content of these activities? This article will report on performance between October 2013 and September 2015, and represents a continuation of the activities introduced in the last issue.

First, let us take a look at the principles:

1. Recognize our roles and responsibilities, taking into account a precautionary approach, and promote those actions that contribute towards shaping a sustainable society
2. Contribute to the formation of a sustainable global society through the development and provision of financial products and services
3. Assist the environmental programs of small and medium-sized enterprises from the perspective of regional development
4. Cooperate with diverse stakeholders
5. Take active steps toward reducing our own environmental footprint and encourage suppliers to do likewise
6. Disclose information on our activities
7. Raise awareness of environmental and societal issues with our own board

The principles are made up of the seven preceding precepts defined. A general theme of addressing social issues and aspiring toward value creation through financial services, which represent the main activities of signatory institutions, is prominent throughout. At the same time, the principles reflect a strong awareness of contemporary themes such as precautionary approaches, business opportunities and risk, regional development, and cooperation with multiple stakeholders. The principles allow a diverse range of financial institutions to forge commitments in accordance with their individual circumstances, regardless of their sphere of activities or how much progress they have made in ESG investment and financing activities.

(2) Current Activities

The Principles encourage signatory institutions to engage in activities that deal specifically with the themes described, and three guidelines have been established to correspond specifically to the kinds of activities that an institution may be involved in. Accordingly, a series of working groups (WGs) has also been set up to address each guideline. In addition to the three activity-specific WGs, two more have also been established to deal with crossover themes, and activities are mainly conducted through these five WGs.

Table 4.1.1 shows the activities conducted by each WG since the second half of fiscal 2013, ended March 2014.

Table 4.1.1: Activities at Each Working Group (WG): FY2013–First Half of FY2015

WG Name	Fiscal Year*	Date	Main Theme
Asset Management/Securities/Investment Banking	2013	1: 2013/7/8	Integrated Reporting
		2: 2014/1/17	Attractive ESG Investment Products to Individual Investors
	2014	1: 2014/6/9	Free Discussion Pertaining to Future Direction
		2: 2014/9/11	Response to Japan's Stewardship Code
		3: 2015/1/11	Corporate Value Dialogue and CSV
	2015	1: 2015/9/17	Response to Corporate Governance Code
		2: 2015/12/7	Engagement
Insurance	2013	1: 2013/10/25	Lecture by World-Leading Insurance Intermediary Service Corporation Willis Group
		2: 2014/2/19	Lecture by AXA Life Insurance and NLI Research Institute
	2014	1: 2014/11/18	Resilience and Finance
		2: 2015/1/26	The Role of Finance in Dealing with a Declining Birthrate and Health Problems
	2015	1: 2015/10/17	Dementia Symposium (collaboration with Community Support WG)
Deposit/Loan/Leasing	2013	1: 2013/8/26	Environmentally Friendly Real Estate and Reduction of Energy Use (collaboration with Environmentally Sustainable Property WG)
		2: 2013/10/15	Regional Renewable Energy and Finance Initiatives (in Nagano) with Hachijuni Bank
		3: 2013/11/6	Regional Renewable Energy and Finance Initiatives (in Kagoshima) with Kagoshima Bank
		4: 2014/1/26	Regional Renewable Energy and Finance Initiatives (in Shiga) with Shiga Bank
	2014	1: 2014/10/16	Regional Renewable Energy and Finance Initiatives (in Toyama) with Hokuriku Bank
		2: 2014/11/14	Regional Renewable Energy and Finance Initiatives (in Mie) with Hyakugo Bank
		3: 2014/12/16	The Equator Principles and Evaluation of Environmental and Social Risk: Finance and Regional Growth
		4: 2015/2/6	Regional Renewable Energy and Finance Initiatives (in Okayama) with Chugoku Bank
Environmentally Sustainable Property	2013	1: 2013/8/26	Responsible Property Investment (RPI) and Regional Innovation (collaboration with Deposit/Loan/Leasing WG)
		2: 2014/2/3	Public Facility Management and Infrastructure Investments
	2014	1: 2014/12/3	Finance and the Environmental Impact Assessment of Existing Properties
		2: 2015/2/27	Aging Society and the Management of Public Facilities (collaboration with Community Support WG)
	2015	1: 2015/10/1	Compact Cities
Community Support	2013	1: 2013/9/2	Declining Birthrate and Aging Population in Japan: Present State and Challenges Going Forward
		2: 2013/12/6	Reorganization of Housing and Medical Care Policies in Building a Comprehensive Regional Healthcare System
		3: 2014/1/31	Reforms to Social Security and Care Going Forward
		4: 2014/2/21	Review of Past Activities and Discussion Pertaining to Activites for Following Fiscal Year
	2014	1: 2014/6/23	Comprehensive Regional Healthcare and Regional Financial Institutions
		2: 2014/9/25	On-site Observation: Comprehensive Regional Healthcare (Satte City)
		3: 2014/10/31	The Problem of Care in a Rapidly Aging Society
		4: 2015/2/27	Aging Society and the Management of Public Facilities (collaboration with Environmentally Sustainable Property WG)
	2015	1: 2015/9/1	"Town Guardian" System
		2: 2015/10/17	Dementia Symposium (collaboration with Insurance WG)

* Fiscal year is from April to March of the following year
Source: Produced using data available at MOE "Principles for Financial Action for the 21st Century" https://www.env.go.jp/policy/keiei_portal/kinyu/gensoku.html

As many activities are planned during the first half of the fiscal year, April to September, and implemented in the second half, October to March, it is only possible to reflect a small proportion of the activities that took place recently in fiscal 2015, ended March 2016. However, just by looking at the difference between fiscal 2013 and fiscal 2014, we can see that the range of activities implemented has broadened and that WGs have become more active.

Most notable is the Asset Management/Securities/Investment Banking WG becoming active and gaining extensive participation. This is in part due to the systematic influence resulting from the introduction of Japan's Stewardship Code and its Corporate Governance Code, with timely opportunities to share information pertaining to Japan's direct financing today, against a backdrop of a changing environment where interest in ESG investment has accelerated rapidly. This represents a good example of how the Principles have been carefully adapted to address change from generation to generation and to function as a trigger.

Moreover, as environmental risk, including climate change, exerts a direct influence on business activities, the Insurance WG, which has always been sensitive to issues regarding ESG, has begun to leverage its expertise in the area to diversify the themes it deals with to include resilience and an aging society, among others, thereby expanding the scope of the Principles. At the same time, this WG also represents institutional investors, and going forward, we expect it to expand its collaborative activities with the Asset Management/Securities/Investment Banking WG, centering on life insurance.

The Deposit/Loan/Leasing WG, which has the largest number of Principle signatory institutions, is working to encourage a large number of signatory institutions to participate. Also, rather than broadening the themes it deals with, it deepens specific themes to promote them in regions where they bear significance. More specifically, with the introduction of the Feed-In Tariff Scheme for Renewable Energy, it has been actively engaged in holding regional workshops with the support of local banks representing each region on the theme of renewable energy project finance, which has also garnered significant attention in the world of regional financing. By focusing on themes that are directly applicable to financing operations, this WG is working to encourage participation from signatory institutions to which ESG is an unfamiliar, abstract concept. With the support of the hosts shown in Table 4.1.1, each workshop addresses the unique features of a particular region, and with their efforts they have proven to be a great success. Meanwhile, the Tokyo session functions as a platform for the finance world by hosting discussions on dealing with globalization and other themes applicable to a wide range of business categories. These have included an introduction to the Equator Principles by business managers from three megabanks, and lectures on a company's social value through leasing operations by a major leasing company.

Along with such operation-specific discussions, the Environmentally Sustainable Property and Community Support WGs have ushered in wide participation from signatories engaged in a broad range of business categories. The Environmentally Sustainable Property WG has continued to broaden discussion on new fields related to ESG financing, such as the evaluation of green building, as well as infrastructure renewal and public facility management. Meanwhile, the Community Support WG has been working to shed light on social problems that have resulted from a super-aging society and to offer opportunities to consider the position of financing from the perspective of both opportunity and risk.

In addition to this activation of group-specific activities, the overall function of the Principles was reinforced in fiscal 2014. To be more specific, a significant progression was evident in terms of incentives to encourage signatories to report on their activities; for instance, establishment of a logo for wider recognition of activities requested by a good number of signatories and the introduction of the Environment Minister's Award, in addition to the Good Practice Award, which is awarded based on the number of votes received from fellow signatory institutions. The first highly coveted Environment Minister's Award was given to Daishi Bank, for its Carbon Offset through Green ATMs initiative. Furthermore, closer cooperation with the UNEP FI has also been cited as an objective, and, at the general meeting in March 2015, Ligia Noronha, the Director of UNEP's Division of Technology, Industry and Economics (DTIE) delivered the keynote speech.

(3) Future Outlook

Following these developments, the Principles have continued to see solid improvements, particularly with regard to the activities of WGs. At the same time, functional enhancement initiatives and changes in external environments pertaining to ESG investment have also been influential, and momentum is continuing to build. If we consider the present as a period of "breathing substance" into the Principles, then we can see that progress is, in general, coming along smoothly. Our next challenge is to maintain the stability of current trends and work to elicit the autonomous expansion of activities going forward.

The most important issue lies with the composition of frameworks. Although frameworks reflect initiatives that are implemented by financial institutions, we must also remember that there is a process for the establishment of such frameworks. To date, this process has relied on generous support including the provision of administrative functions by the Ministry of the Environment. Going forward, there are a number of issues that need to be tackled to elicit the shift toward independent implementation of activities by financial institutions. Signatories are going to have to engage in in-depth discussions. When that happens, there may well be some interesting patterns that emerge, such as differences in the degrees of enthusiasm between each institution. Moreover, with the passage of time since an institution becomes a signatory and changes in the persons responsible for compliance with the principles due to reshuffling of personnel, effort will continue to be necessary in discussing and reaffirming the significance and value of participation as a signatory of the principles.

Keisuke Takegahara

2. Community Investment and Crowdfunding

(1) Overview of Community Investment in Japan

Community Investment Activities in Japan

Community investment can be defined as "investment activities with the goal of contributing to local communities." It makes up a division of sustainable finance and a division of traditionally classified SRI. More recently, it is also recognized as a division of social investment.

Although Japan's community investment activities showed signs of activity for some time, we had to wait until the 2000s to see some real progress. However, while the scale of this sector is currently limited, activities among NPO banks, micro-investment funds,[1] microfinance institutions (MFIs), and other organizations have become more vigorous, making it possible to grasp a general idea of overall trends.

In this chapter, we will look at community investment in Japan, describing its current state and the course of its development, with a focus on the trends that have appeared since the publication of the *2013 Review of Socially Responsible Investment in Japan*. This update will reference, in particular, initiatives related to reconstruction following the Great East Japan Earthquake.

Moreover, this section aims to compare trends in Japan with those seen in Europe and the United States. In the same way as for the 2011 and 2013 Reviews, the main focus of this chapter is alternative initiatives in which the main entities behind community investment are citizens (citizen-financed initiatives). The scope therefore excludes the initiatives of governments and traditional financial institutions (microfinance bond initiatives recently implemented by securities companies, etc.). This section also excludes certain types of investment and financing that are classified as citizen financing but cannot be easily interpreted as investments and loans (mutual aid, local currency, etc.). Moreover, although it comprises elements that are difficult to term "investments," we will also examine recent trends in crowdfunding, which is continuing to take hold as a form of Internet-based capital procurement.

(2) Current Conditions Pertaining to Different Areas of Community Investment

NPO Banks

NPO banks are "non-profit financial institutions established by citizens, using funds that originate from citizens, which finance social needs including citizen entrepreneurs." As of December 1, 2015, the number of NPO banks in Japan stood at 25, 14 of these mainly provide funding for social enterprises (see Table 4.2.1), and 11 mainly provide funding to individuals in financial need[2]. As of the end of March 2015, the total financing provided to individuals in need and by the 14 NPO banks that mainly provide funding for social enterprises had risen to ¥3.2 billion.

Although there have not been any new NPO banks established to fund social enterprises since the publication of the last Review, the Community Youth Bank Momo (Momo) did win the Third Nikkei Social Initiative Award for the domestic category, which is worthy of mention. In fiscal 2013, Momo also collaborated with Tono Shinkin Bank (Gifu Prefecture) and Seto Shinkin Bank (Aichi Prefecture) to carry out the Shinkin Pro bono Project. In addition, Momo coordinates other activities through financial institutions to promote financing for social enterprises, including "Social Business Aichi," which was implemented with cooperation from financial institutions within Aichi Prefecture and Japanese governmental financial institutions.

To cite other characteristic initiatives, from 2015 onward, the Mirai Bank has been working to elicit innovative business operations by holding regular public "strategy meetings." Tokyo Community Power Bank also commenced its "100% Tomodachi Financing Group" initiative, which aims to form direct links between investors and financing operations.

Concerning NPO banks that provide financing for individuals in need, the Seikatsu Club Co-op, Chiba established and commenced lending activities at the "Seikatsu Club Life and Household Budget Consultation Office," following on from similar activities implemented by Miyagi Co-op.[3] Moreover, from 2015, the National Women's Shelter Net began to register moneylenders and commenced financing activities to support the independence of women affected by domestic violence.

In April 2015, businesses that support individuals in financial need, which work to integrate household budget consultation and finance and originate from trust co-ops in Iwate Prefecture, etc., were formally defined as "household budget consultation and support businesses." However, as these businesses are run voluntarily, they have not yet demonstrated sufficient growth.

1. In this report, citizens funds that provide assistance, contributions, intermediations, etc., are referred to as "citizen community foundations." Citizens funds that invest in businesses are referred to as "micro-investment funds."
2. Trust Co-operatives (Iwate Prefecture, etc.), Life Support Foundation (Tokyo), lifestyle rehabilitation services by Green Co-op (Fukuoka, Kumamoto, Oita, Yamaguchi, and Nagasaki prefectures), Miyagi Co-op, anti-poverty cooperation networks, lending activities by National Women's Shelter Net.
3. Seikatsu Club Co-op, Chiba News Release: http://chiba.seikatsuclub.coop/news/2015/04/post-215.html

Table 4.2.1: Current State of NPO Banks (for social enterprise funding)

(Thousands of yen)

	Established	Type of financing	Subscribed capital	Total loans provided	Loans outstanding	Financing program	Remarks
Mirai Bank	1994	Environment, social welfare, citizen entrepreneurs	¥149,146	¥1,100,014	¥53,747	Interest: 2.0% Max. ¥3.0 million Max. term 5 years	—
Women's and Citizens' Community Bank	1998	Investment groups residing in Kanagawa Prefecture, private (limited targets)	¥114,780	¥588,365	¥66,297	Interest: 1.8%–5.0% Max. ¥10.0 million Max. term 5 years	—
Hokkaido NPO Bank	2002	NPO Group Workers Collective*	¥43,124	¥349,270	¥10,467	Interest: 2.0%–5.0% Max. ¥2.0 million Max. term 2 years	Donations ¥7,100
NPO Yume Bank	2003	NPOs established in principal offices within Nagano Prefecture	¥13,870	¥302,230	¥48,363	Interest: 2.0%–3.0% Max. ¥5.0 million Max. term 5 years	Donations ¥35,180 No interest borrowings ¥30,000
Tokyo Community Power Bank	2003	Organizations active in fields relevant to NPO law annexes within Tokyo	¥105,100	¥307,638	¥54,257	Interest: 1.5%–2.5% Max. ¥10.0 million Max. term 5 years	Total financing includes social investment (subscribed capital) of ¥23.0 million
ap bank	2003	Renewable energy and other environmentally related projects	Undisclosed	¥208,460		Inactive. Total loans provided as of December 2007	
Community Youth Bank Momo	2005	20 divisions of NPOs, sole proprietorships, private organizations, corporations	¥51,598	¥126,340	¥22,788	Interest: 2.5% (Bridge financing: 2.0%) Max. ¥5.0 million (in principle) Max. term 3 years (in principle)	—
Natural House Bank	2008	20 divisions of NPOs, private	¥61,177	¥70,204	¥16,474	Interest: 0%–2.0% Max. ¥3.0 million Max. term 10 years	—
Moyai Bank Fukuoka	2009	NPOs and other social entrepreneurs that operate in Fukuoka Prefecture and surrounding areas	¥12,850	¥35,970	¥6,390	Interest: 1.5%–3.0% Max. ¥ 3.0 million Max. term 5 years	—
Shinrai Zaidan	2009	Private, corporation (without limitation), juridical personality (without limitation), area of activity (country) (without limitation)	0	¥84,570	¥17,306	Interest: 0% Max. ¥3.0 million Max. term 2 years	Donations
Piece Bank Ishikawa	2010	NPOs that are active in the 20 divisions of NPOs within Ishikawa Prefecture, sole proprietorships, private organizations	¥10,969	¥25,507	¥5,061	Interest: 3.0% (Bridge financing: 1.0%–3.0%) Max. ¥3.0 million Max. term 5 years	—
Entrepreneurship Support Program for Refugee Empowerment	2010 (Public interest recognized in 2012)	Projects by refugees residing in Japan	¥3,000	¥2,520	¥916	Interest: 3.0%–7.5% Max. ¥1.0 million Max. term 5 years	Donations and project revenue (subscribed capital column is funds outstanding)
Hachidori Bank Financing	2011 (Operations began December 2012)	Private/Group offices within Toyama Prefecture, private/ group activities related to Toyama Prefecture	¥7,620	¥4,900	¥1,400	Interest: 1.0%–2.5% Max. ¥3.0 million Max. term 3 years	
Mutosu Iida citizen fund	2008	Specified non-profit corporations within Iida city	¥7,001	¥19,090	¥5,600	Interest: 0% Max. ¥2.0 million (Max. term 1 year) ¥1.0 million (Max. term 2 years)	Donations ¥3,000
Total			¥580,235	¥3,225,078	¥309,066		
Compared with previous fiscal year			99.4%	109.5%	115.6%		
Japan Credit Union	1968	Church and church groups, NPOs, religious orders, etc.	¥230,000	Exceeding ¥1.0 billion	¥174,728	New loans have been suspended since January 2013	Continuation of collection services and lifestyle consultations

* "Workers Collective" does not refer to the relationship of employee and employer but rather a cooperative association where workers carry out collaborative investments. Each member of a Workers Collective participates on an equal level as a co-business owner and makes efforts to commercialize products and services needed by local communities as a collective "citizens' business."

Micro-Investment Funds

In micro-investment funds, "Securite" by Music Securities Inc., continues to be widely utilized, with the latest statistics reflecting total financing of ¥5.9 billion. Moreover, micro-investment funds for renewable energy businesses have also been widely utilized following the establishment of feed-in tariffs (FIT).

In addition, the 2014 revision of the Financial Instruments and Exchange Act relaxed regulations, redefining micro-investment funds (investment crowdfunding) that utilize collective investment schemes as "Dealing in electronic offerings."

Microfinance

NPO banks that fund individuals in financial need are continuing to push ahead with domestic microfinance activities, as previously described.

Organizations such as ARUN LLC, Oiko Credit Japan, and Kiva Japan are also continuing to implement solid microfinance activities overseas. Moreover, social investment activities implemented in Cambodia by ARUN LLC have been evaluated highly, and the organization was awarded the Third Nikkei Social Initiative Award in the overseas category.

(3) Current State of Crowdfunding

Over the last two years, crowdfunding seems to have taken root as a fund procurement method for projects geared toward the solution of social issues, test marketing of manufactured products, and entertainment content such as films and games.

According to the Yano Research Institute, the scale of the domestic crowdfunding market has expanded to ¥19.7 billion.

(4) Trend of Policies Pertaining to Community Investment and Crowdfunding

Over the last two years, policies concerning community investment and crowdfunding have continued to be approached from various perspectives, including social investment and impact investment.

In October 2014, the Japan Fundraising Association put together *A Roadmap to Building a Social Impact Investment Market*. On June 1, 2015, the G8 Social Impact Investment Taskforce put together a proposal with the objective of promoting social impact investment in Japan.

Moreover, from January 2016 activities with the objective of forming legislation pertaining to the use of dormant deposits have continued to take place at regular Diet sessions. According to a bill submitted at an ordinary Diet session in 2015, supporters of community investment are categorized as "fund distribution organizations."

(5) Future Prospects and Challenges

Soliciting Support

As previously described, over the last two years community investment has continued to raise anticipation in society; however, the number of people willing to invest has not increased enough to warrant such anticipation. The fact that efforts to lobby such investors are insufficient is cited as the reason for this.

Makers University, a school established by NPO organization ETIC, which aims to seek out young social entrepreneurs with a focus on university students, includes "finance" as one aspect of its entrepreneurship course. The school aims to seek out and support people of various backgrounds, including graduates of the course, who aspire to set up their own business through community investment. It is going to be necessary, however, to increase the number of people willing to provide financial support for community investment.

Encouragement of Supporters

Providers of capital for community investment often struggle with issues related to a lack of managerial resources, such as adequate staffing and funding. In the U.S., the government has put in place the CDFI Fund, which targets the proliferation of Community Development Financial Institutions (CDFIs), and the expansion of their cooperation with regular financial institutions. In Japan, the aforementioned dormant deposits are expected to embody a similar role to the CDFI Fund. The time may have come, however, to consider the creation of a Japanese version of the CDFI Fund in the private sector by harnessing the power of citizens.

Shunji Taga

MICRO-INVESTMENT: INVESTING SMALL, ENRICHING JAPAN'S FUTURE

1. Discovering Micro-Investment

I first heard about micro-investment in 2008, and I became interested in it after reading an article about the procurement of funds to purchase rice as an ingredient to produce sake.

Although sake takes three years in a cellar to mature into great-tasting liquor, any money lent from a bank has to be paid back in monthly installments. For producers then, who cannot sell the product until it has matured but must continue to make payments on their loan before they see the fruits of their labor, this is a significant obstacle, and many producers simply do not have the time to allow it to mature despite a desire to produce high-quality sake.

On the other hand, those who enjoy a drink are happy to wait three years if that's what it takes to produce delicious sake. Furthermore, if the sales of this fine sake are good and money is made, with investors seeing a return on their investment, their wallets wind up happy too. Moreover, as the sake producer also sends some of its product to the investor as a token of appreciation, investment represents killing not two, but three birds with one stone. Even if their sales are not good, they send a bottle of premium sake to compensate.

This system attracted my interest because it keeps all parties happy—investors, producers, and consumers. As the deadline for applications had already passed by the time I read the article, I decided to invest in micro-investment funds from the following year.

2. Understanding the Usefulness of My Own Money

The attraction of micro-investment is being able to watch how investments with your own money are used to make products that materialize before your very eyes.

A producer of organic cotton towels in Imabari, Ehime Prefecture was forced to undergo civil rehabilitation* procedures after its wholesaler went bankrupt. The towels were of premium quality, having won such honors as a New York Trade Show award, yet the company could not apply to the banks for financing due to its status pertaining to civil rehabilitation. That's when it decided to adopt a micro-investment fund.

The money procured from the fund was used as capital to purchase organic cotton from Tanzania. As ordinary cotton is cultivated as a crop that is not consumed as food by humans, large quantities of agricultural chemicals are used in its production. When the cotton is collected by machine, a chemical to wither the leaves is sprayed on the crop to prevent the green leaves from staining the cotton fiber. In India and other cotton-producing nations, there have been incidents where farmers who cannot read have used too large a quantity of these chemicals and, in failing to implement adequate protective measures, have become ill. The organic cotton used by the company in Imabari requires more work to pick, but it avoids the dangers of agricultural chemicals. Moreover, the cotton is fair trade, so the compensation for these farm workers is better than it would be for an ordinary cotton farmer.

When I first felt one of the towels at a trade fair, I could feel the weight of my contribution in the quality of the finished product, and I couldn't help but feel moved. There was such a sense of satisfaction in realizing that you have contributed to making something special, feeling that cannot be replicated by money.

The fund provided a positive return on my investment, but the joy I felt had really nothing to do with money. I subsequently fell in love with the company to the extent of earning a qualification as a towel sommelier.

* A bankruptcy law in Japan allowing a company to force a lender to change the terms of the loan in order to help alleviate the company's bad debt.

3. Witnessing Investee Activities

The sense of closeness between investor and producer is another attractive feature of micro-investment. I am fortunate enough to have participated in a tour for investors after investing in a local business engaged in the revival of forests in the village of Nishiawakura, Okayama Prefecture.

Unlike unkempt (or neglected) forests seen in many other parts of Japan, Nishiawakura's "100-year forest" is a beautiful, well-kept forest. This made me realize the issues that forestry is facing and what the village was striving to achieve.

Moreover, rather than selling lumber from forest thinning on the raw timber market, the village has developed a system to process the material into a final product to increase the income of the woodland owners. By observing how logs are used to make chopsticks on a production line, how wooden floorboards are produced, and how logs not wide enough for lumber are not wasted but used to make various products in innovative ways, I was able to fully appreciate the scope of this operation. Many people who choose to invest in micro-investment funds do so because they feel some level of affinity for a company's business operations or have a special desire to support them. Through the nature of this investment, a connection is forged between those living in the city and those living in rural environments, and this connection allows for the inbound flow of capital from cities that stimulates rural economies.

By visiting investees, investors can experience a world that they have never seen before. It feels like a sociology field trip for adults, and participants on such tours tend to be highly impressed with the experience. By going to see things for yourself, you get to view what's on the surface as well as experience the deeper aspects of these activities, which strengthens the connection you have with them.

4. Sending Money with Love

Funds to support the reconstruction of small and medium-sized businesses impacted by the Great East Japan Earthquake are half donation, half investment. As a result, returns are nearly always negative from the moment you invest. Despite this fact, funds of this type have amassed a total of ¥1.1 billion.

If we consider only the financial returns of these funds, it is almost a given that they will be negative, and, what's more, of course, the target company has already been seriously affected by natural disaster. In the worst-case scenario, investors may not get a single penny back. In the beginning, affected business owners thought it folly that investors would even consider investments in companies that were in such a state, let alone put their money into a fund where half of it is sourced by donation.

The accumulation of such a large amount of money despite this scenario can therefore be attributed to the fact that the characteristics of micro-investment, which allows investors to see their money delivered to recipients, are well matched to the investors' desire to encourage business owners to triumph in the face of adversity and work toward recovery. Disaster relief funds were launched on April 25, 2011, just a little over one month after the earthquake. Such investor activities do not stop simply at the donation of money, but extend to the joy of hearing that a new factory has been completed and, further, to the formation of strong bonds with the business by visiting the area and purchasing products.

Investors that spend a long period of time getting involved to support affected businesses are, to business owners working toward reconstruction, not simply providers of capital but also providers of emotional support.

5. Issues Associated with Micro-Investment

In May 2014, it was pointed out that the parent organization of a civil fund for investment in renewable energy was failing to adequately implement the segregated management of its investment capital, and was ordered to improve its operations by the Ministry of Finance. The business owners running the fund were pioneers in civil energy funds, but as the amount of work involved expanded, the fund suffered, plagued by staff shortages and cases where the segregated management of investor funds was not properly executed. After being ordered to improve its operations, the fund improved its compliance structure and addressed its staff shortages. However, this inability to secure sufficient manpower is an issue often faced by business owners operating small-scale funds, through no ill will of their own.

In 2015, business owners at a fund specializing in social lending to overseas microfinance institutions, domestic renewable energy ventures, and small and medium-sized corporations were ordered by the Ministry of Finance to halt a portion of their activities. This too was the result of a shortage of manpower following rapid expansion. As crowdfunding is growing increasingly popular and microfinancing is attracting more attention, it has become necessary for investors to adopt a financial industry-style stance in assessing whether parent organizations are properly engaged in compliance.

Even in cases where accounts are set up and fund application procedures are completed via the Internet, it is better to engage directly with fund managers before making the decision to invest.

6. Healthy Relationships Between Investors and Businesses

The role of finance is to provide capital to where it is needed from where it is not needed. Banks in Japan began with the objective of creating a river of capital for nation building through the accumulation of small amounts of capital held by the public. Micro-investment funds are a mechanism to deliver small amounts of capital held by the public to small and medium-sized businesses that need it. The amount of money needed varies depending on the recipient, but these funds allow money to be delivered to producers for whom investors have felt an affinity, and in fields that make it difficult for existing financial institutions to take the risk and invest capital in.

Relationships between investors and producers, who represent the investees, naturally give rise to the encouragement of long-term business success and a relationship where both parties strive to satisfy each other's expectations.

In the world of asset management including pensions, institutional investors are encouraged to engage in "purposeful dialogue" to support the medium- to long-term growth of corporations. Interestingly, however, investors and producers are successfully giving rise to positive relationships at the grassroots level. This is not simply down to money, but through a desire of the investor for the producer to create quality products.

In a generation where affluence was reflected by owning the same things as other people, productivity and rationality were held in high regard. However, in a generation where there are now so many products to choose from, affluence has come to be reflected in the ownership of unique items that other people do not have. Contributions of money motivated not only by returns but also by a desire to support development because investors find something interesting, have encouraged the creation of original products.

Although returns are low on the list of reasons for investment in this kind of fund, this does not mean to say that investors are not concerned with financial gain. By simply rearranging their priorities, investors are receiving returns the moment that businesses experience success. Risk is not something to be avoided entirely but to be taken in order to promote success. This represents the basic principle of investment.

In a world where patronage has all but disappeared, micro-investment is a mechanism that allows you to invest small amounts of money in businesses you want to support as an ordinary individual. As Japan continues to become a country where urbanization and standardization have given rise to streets that are lined with the same kinds of shops wherever you go, micro-investors support unique businesses by investing a small amount but make a big difference in giving them a new lease of life.

Masayuki Oki

3. Environmentally Friendly Real Estate[1]

(1) Neighborhood Sustainability Evaluation System LEED ND: Best Practice

World's First Gold LEED ND Certification Realized in Japan

In the real estate industry, Leadership in Energy and Environmental Design (LEED), a system to evaluate the sustainability of buildings, has become synonymous with "environmental performance." The system represents an international standard, which started by evaluating the environmental performance of newly established office buildings based on figures pertaining to design efficiency. It has since expanded to include a range of systems to evaluate the construction of buildings including commercial facilities, hospitals, distribution facilities, data centers, hotels, and schools. LEED O+M (LEED Building Operations and Maintenance), an approach to managing the operations of existing buildings, has also become more prevalent. LEED was originally developed with the primary objectives of reducing environmental impact and improving the quality of indoor environments; however, the criteria it uses to evaluate a space have now been expanded to emphasize human health and comfort, which represent crucial elements to the enhancement of productivity. Moreover, LEED is working to become more than just a system to evaluate environmental performance by incorporating and proliferating social equity perspectives (social common capital—a mechanism to encourage fairness by ensuring that common assets are shared across the whole of society), which includes the idea of "contributing to the community" as a social objective toward which we should aspire. Against this backdrop, LEED ND (LEED Neighborhood Development) is an evaluation system that goes beyond the borders of individual real estate developments to evaluate the sustainability of entire neighborhoods, and movement toward expanding the scope of evaluation in this way has been accelerating around the world.

The U.S. Green Building Council (USGBC), the NPO that develops and manages LEED, has always aspired toward the realization of a sustainable society through market transformation. LEED certification is the system designed to reflect monetary value in the markets by quantitatively evaluating the value added to a project through the enhancement of sustainability. LEED embodies three characteristics to make this a possibility: "quantitative evaluation to ensure quality meets a certain benchmark," "transparency of information pertaining to performance," and "objectivity." All LEED certifications are conducted and granted by Green Business Certification Inc. (GBCI)[2], an independent certification body, to ensure that quantitative assessments are approached from a neutral perspective. This allows the certifications, in which even stakeholders from other sectors place their trust, to maintain their credibility. Failure to link cross-sector collaborations in creating value would mean that initiatives are unlikely to be reflected in the economy and, if initiatives are not reflected in the economy, paradigm shifts are unlikely to occur in existing economic systems; hence, LEED was established to embody these three characteristics. Frameworks aimed at eliciting economic paradigm shifts, including PRI, ESG-considerate investment, and the business-driven "low carbon" initiatives adopted as targets at the 2015 UN Climate Change Conference (COP 21), have also been established in the financial and investment sectors. However, as it is difficult to explain sustainability in quantifiable terms and the value arising from it is only manifested over a long period of time, the characteristics embodied by LEED are going to be instrumental in enabling developers to explain their approaches, which in turn, will lead to the further promulgation of LEED going forward.

As I mentioned previously, LEED ND, which focuses on the development of neighborhoods, has been added to the LEED family. LEED ND has also been adopted in Japan, and in November 2015, a gold LEED ND certification was awarded to the Futako-Tamagawa East area Redevelopment Project in Setagaya, Tokyo. The project acquired the world's 40th preliminary certification in September 2014, followed by the world's fifth official certification in November 2015. It represents the first project in the world to be certified with a rank of gold or above.

The LEED ND evaluation system was developed through a collaboration of three organizations: the USGBC, Congress for the New Urbanism, and the Natural Resources Defense Council. The scope of evaluation for LEED defines its main categories as 1) Location and Transportation/Sustainable Sites; 2) Water Efficiency; 3) Energy and Atmosphere; 4) Materials and Resources; and 5) Indoor Environmental Quality. In contrast, LEED ND specifies 1) Smart Location and Linkage, 2) Neighborhood Pattern and Design, and 3) Green Infrastructure and Buildings, as its three basic evaluation criteria.

The integrated (or multi-complex) development plan for the Futako-Tamagawa East area Redevelopment Project was based on three basic concepts: 1) emphasizing a close connection to nature with the theme of "from city to nature," 2) providing easy access to public transportation with a pedestrian-focused layout, and 3) creating a neighborhood that is easy to use for every generation. Once this plan had cleared all the mandatory criteria of the LEED ND examination, the optional criteria subsequently put forth by the project were highly evaluated, and, with a score of 66 points out of a potential 110, the project was awarded a gold certification. Grading thresholds for each certification are as follows: certified: 40–49 points; silver: 50–59 points; gold: 60–79 points; and platinum: 80–110 points.

The Futako-Tamagawa East area Redevelopment Project was highly evaluated, based on the following criteria:

(i) Smart Location and Linkage

- Development site within close proximity to public transportation
- Sufficient number of bus and train routes with sufficient service along these routes
- Close proximity of housing to places of work
- Consideration toward the conservation of natural habitats
- A long-term (at least 10-year) management plan to conserve the ecosystem

(ii) Neighborhood Pattern and Design

- Walkable streets that provide a safe, appealing, and comfortable environment for pedestrians
- Sufficiently compact development
- Access to parks and public facilities
- Active community outreach and involvement initiatives
- Universal design
- Tree-lined and shaded streetscapes

(iii) Green Infrastructure and Buildings

- Design and construction of buildings with excellent energy and water efficiency
- Measures to reduce the heat island effect
- Landscape irrigation systems with high water efficiency
- Excellent rainfall collection and water permeation functions
- Use of recycled materials in new infrastructure
- Highly energy efficiency in new infrastructure
- Historic resource preservation

"Walkable Streets" and "Diversity" Based on LEED ND System Design

The shift from an automobile-dependent society to building cities that are more human-focused represents LEED ND's most important objective. To realize this, the system is designed to evaluate "walkable streets," with the objective of allowing pedestrians to traverse the area safely, enjoyably, and comfortably; "rich diversity"; and "the preservation and restoration of natural habitats" highly. The system also assesses as important criteria whether there are a large number of shops and eateries on the ground floor facing the road, interesting spaces that attract people both during the day and at night, strict enforcement of speed limits for automobiles, and to what extent these aspects have been incorporated into the design in accordance with Woonerf prerequisites. Other aspects rated highly include: a diverse selection of transportation options, such as trams or the ability to travel by bicycle; green areas that control rainwater run-off and encourage permeation into the ground (bioswales) while separating walking routes from roads to improve safety; and roadside trees with large canopies to protect pedestrians from the sun. Moreover, the LEED ND evaluation system is designed to encourage the development of lively, comfortable areas with a large number of crossings and short block arrangements to allow pedestrians to come and go easily, and roads that are designed to encourage active foot traffic.

LEED ND also features a range of evaluation criteria pertaining to the greening of urban areas, including: preserving ecosystems such as existing trees, marshland, and bodies of water based on vegetation surveys on urban development; the restoration of natural habitats that were previously lost to development in the past; the extent to which preference has been given to species native to the area; and the avoidance of non-native invasive species introduction. Moreover, the system features a large number of evaluation criteria closely related to landscape and urban design, including: diversity pertaining to the hard elements of buildings, such as the use and age of buildings, scale, and layout of residences; diversity pertaining to soft elements, such as the variation of tenant business categories, user numbers, and how the area is used over the morning, afternoon, and evening; the existence of various facilities to provide convenience of living; access to open public spaces and recreation facilities; farmers' markets and community gardens to encourage urban agriculture; safe walking routes for children commuting to school on foot; the proportion of shade provided by roadside trees and canopies; and universal design.

Possible Applications for LEED ND Going Forward

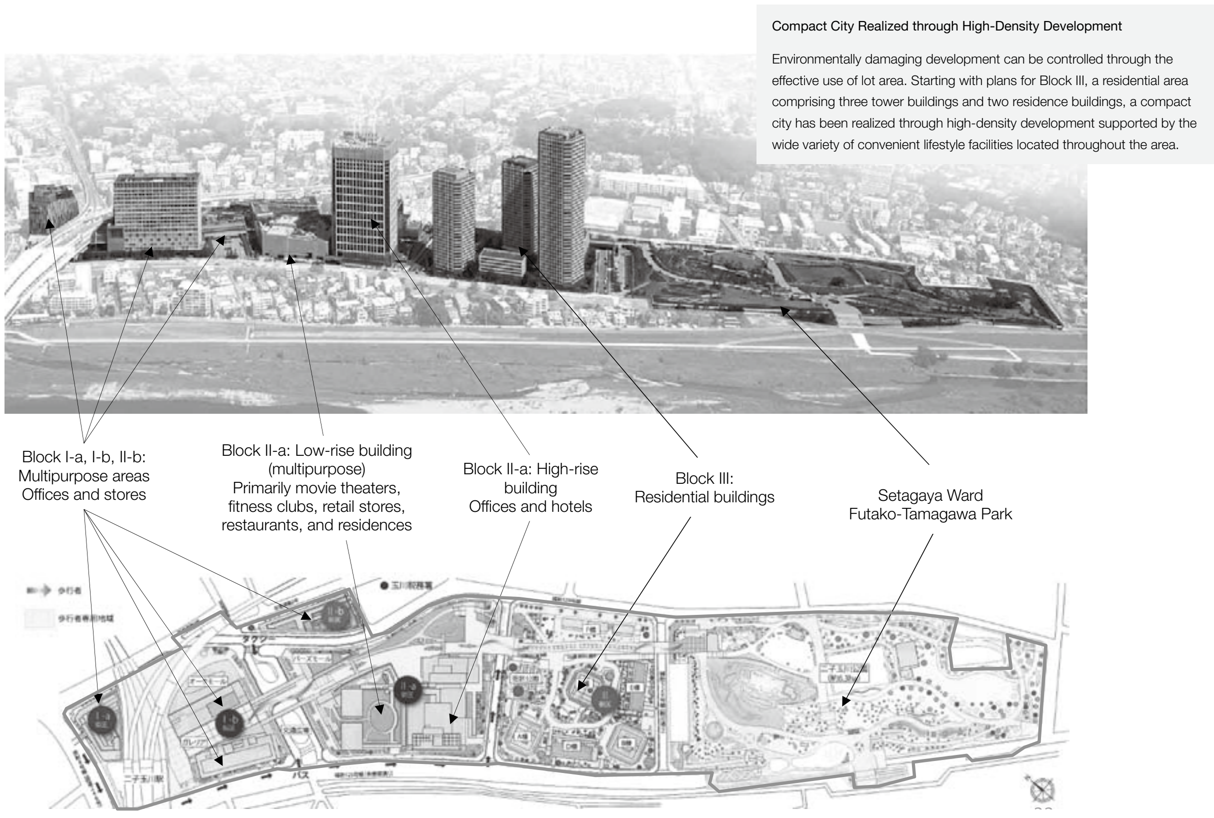
The planning and execution of the Futako-Tamagawa LEED ND project was led by a private redevelopment union, and worked toward the LEED ND criteria by fusing the redevelopment site with a park constructed by Setagaya Ward, enabling it to acquire a larger number of points. This system is therefore designed to place projects that cooperate with the public sector at a favorable advantage when it comes to scoring points. If we consider this from another perspective, LEED ND works to encourage cooperation between the public and private sectors, and between people working in different fields, thus representing a starting point for cross-sector initiatives. Moreover, the execution of LEED ND initiatives requires all stakeholders to determine whether it is possible to push forward with new strategies following the evaluation of current circumstances pertaining to relevant criteria. They will then be required to decide whether these policies are to be adopted and, if they are not, to clarify the reasons why. This is consistent with the idea of "comply or explain." Furthermore, limiting the maximum area of the plot to a relatively small range where everything is within walking distance has the advantages of making it relatively easy to determine whether LEED ND initiatives have been successful in revitalizing the area by conducting inspections, and allows changes to be made easily in rare circumstances where it is determined that such initiatives are failing to take effect.

If we consider projects going ahead overseas, we can see that LEED ND is a tool that can be used in a variety of ways. In the U.S., LEED ND is used as a guideline to revitalize entire cities through large-scale repair work to improve the living conditions of low-income families. It is also used as a set of prerequisites for the allocation of various support grants. Meanwhile, reports by institutions including the World Bank have strongly advocated the use of LEED ND in China, which continues to urbanize rapidly, as a reference point for the central government in providing guidance and allocating support grants to local governments in a bid to prevent out-of-control urban sprawl as suggested in *Sustainable Low-Carbon City Development in China*, published by the World Bank in 2012. Moreover, since the 2008 Olympics in Beijing, where the need for sustainable sport venues had already started to be recognized, LEED ND has become almost a standard to which athlete villages are constructed.

The scale of the Futako-Tamagawa project was large, and all construction represented new development. For much smaller sites, however, it would certainly be possible to engage in area-by-area development while leaving pre-existing structures intact. The strategies adopted by the Futako-Tamagawa project have established a starting point, and are expected to catalyze the application of LEED ND to further redevelopments in both urban and rural areas going forward. If LEED ND can be established as a guide to constructing a potentially huge market geared toward "reimagining cities" in a way that effectively leverages the passion of modern society, then it is likely to result in highly significant local revitalization initiatives in the future. At the same time, it may well be instrumental to solving social issues that are affecting all of Japan, including devising measures to counter the country's aging society, low birthrate, and declining population, helping to support a low-carbon society and the rise of compact cities, encouraging the renewal of public facilities, and correcting the population gap between Tokyo and other areas. To realize this, it is going to be necessary to encourage cross-sector initiatives between private businesses engaged in architecture and construction, landscape design, interior design, building facilities and equipment manufacture, and building operations management, in addition to cooperation between the public and private sectors. Collaboration from real estate developers, real estate investors and funds, and providers of financial functions is also going to be crucial. When such operations begin to take hold, the financial sector's role in community design and city management, including that of regional banks and local financial institutions, is likely to become more important and significantly more complex.

Hiroki Hiramatsu

Figure 4.3.1: LEED ND Target Area and Bird's-Eye View



Pedestrian paths lead through the redevelopment area to the banks of the Tama River

1. Scale of the environmentally friendly real estate market: By May 2013, 205 properties had received CASBEE certification verified by an independent organization, the total floor space of which accounted for 9.14 million square meters. As of December 2015, 303 properties had received CASBEE certification verified by an independent organization (total floor space undisclosed); 74 properties had received the simplified CASBEE real estate certification (3.02 million square meters of floor space); and 4 areas had received CASBEE for Cities certification. Taking into account the median price per square meter of ¥1.1 million for environmentally friendly buildings (from ¥1.0 million–¥1.2 million, according to the 2013 summer special of Nikkei Architecture), the estimated market size of environmentally friendly real estate in 2013 was approximately ¥3.0 trillion. However, in 2015 this rose to approximately ¥5.1 trillion, representing a 70% increase between May 2013 and December 2015.* Moreover, the total number of properties in Japan that had received or were applying for LEED registration in 2013 was 90, covering a total floor space of 1.68 million square meters. As of the end of 2015, however, this had increased to 148 properties with a total floor space of 2.09 million square meters. Taking into account the median price stated above of ¥1.1 million, the estimated market size in 2013 was ¥560.0 billion. As of 2015, this had increased by 25%, to ¥700.0 billion. Globally, the total number of properties that had received or were applying for LEED registration in 2013 was 50,569, covering a total floor space of 882 million square meters. As of 2015, this had increased to 71,200 properties, covering a total floor space of 2.13 billion square meters, for a total increase in floor space of 141%.
   * As the total floor space for properties that have received CASBEE certification verified by an independent organization is undisclosed, for the sake of convenience, total floor space was calculated using the following calculation: average floor space for CASBEE real estate-certified properties x (number of properties that have received CASBEE certification verified by an independent organization + number of properties that have received CASBEE real estate certification).
2. In 2014, GBCI was integrated with the Global Real Estate Sustainability Benchmark (GRESB), an organization that assesses the extent to which real estate investments are sustainable.

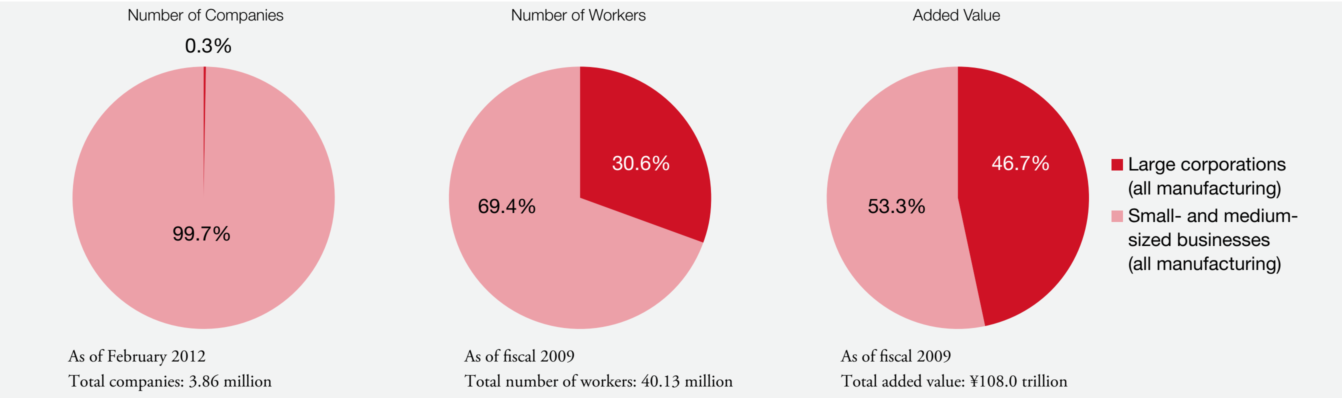
4. Private Equity

(1) What is private equity?

Overview

According to the *White Paper on Small and Medium-Sized Enterprises in Japan* (February 2012), at the time of publication the total number of companies in Japan stood at 3.86 million. This figure is over 1,000 times the number of listed companies in Japan, which number approximately 3,500, meaning that 99.9% of companies in Japan are unlisted. Private equity (PE) investment is the main form of investment used to finance this 99.9%. A large number of these companies are small to medium-sized enterprises, a few of which may be selected to form part of an investment portfolio. As we can see in Figure 4.4.1, 69.4% of all Japanese workers are employed at small and medium-sized businesses, and these businesses are responsible for creating 53.3% of total added value. We can naturally assume, therefore, that thinking seriously about investment in the PE sector is akin to thinking about the sustainable expansion of the Japanese economy.

Figure 4.4.1: Overview of Japanese Companies



Source: Ministry of Economy, Trade and Industry

PE investment is, however, a very broad term, and as we can see from Figure 4.4.2, there are various approaches to such investment. Of these approaches, around 80% of PE investment can be explained in terms of two methods: buyouts, which account for over half of total PE investments by amount invested; and venture capital, which makes up around 20%–30%. Investment strategies can be subdivided into buyouts, venture capital, the purchase of distressed securities, and secondary buyouts. The form of interaction that takes place with the company to be invested in depends on the strategy. However, as the main focus for investment is unlisted companies, which are insusceptible to the influence of the markets because their shares are not publicly traded, they all share similar attributes. This section will explain PE investment in terms of buyouts, which account for over half of foreign and domestic PE investment.

Figure 4.4.2: Explanation of Each Strategy

Venture Capital	• An investment method to secure capital gains by investing in unlisted companies from a stage shortly after their foundation, and having them initiate an Initial Public Offering (IPO) or selling them to another corporation or fund. • Venture capital involves not only taking on common stock, but also convertible bonds and various other forms of stock.
Buyouts	• An investment method to secure capital gains by first purchasing a company with positive cash flows, working to enhance its corporate value by becoming deeply involved in its management and, finally, selling off the company's stock [for a higher price]. • Buyouts are often conducted by using borrowed money as leverage.
Distressed	• A investment method that aims to secure returns by purchasing bonds from a company that has experienced unprofitable business operations, converting a portion of this into stock, and actively contributing to the reorganization of management.
Secondary	• An investment method that arises when an investor's interest in a fund (3 types of funds above) is purchased for a reduced price after they are forced to sell midway through the investment due to extenuating circumstances. • In a broad sense, this investment method aims to secure capital gains by purchasing from the investor not only their interest in a fund, but also non-listed stock, for a reduced price, and then selling it off (this differs from the above approaches as it does not encompass involvement with investee management).

Source: Ark Totan Alternative Co., Ltd.

Investment Effects and Their Relevance to Responsible Investment

Possession of 51%–100% of a company's shares is necessary to implement a buyout investment. By taking control of the company's management, initiatives can be implemented to raise the company's corporate value, and, after holding this share of the company for a given amount of time, the investing party may choose to exit via a sale or through the execution of an IPO. The average holding period spans 2–5 years, and, by raising the company's investment value by 1.5 times–3 times over this period, buyout investors can secure the returns they require. The basis for these returns can be divided into three categories: A. the effect of enhancing corporate value (hands-on effect); B. the effect of leverage; and C. the effect of a multiple-based approach. The following will summarize how each of these is relevant to responsible investment.

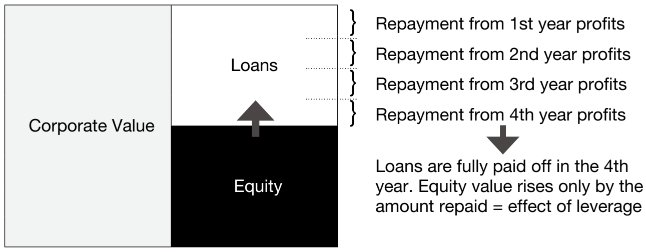
A. Effect of Enhancing Corporate Value (Hands-On Effect) and Its Relevance to Responsible Investment

As mentioned previously, buyout investments involve taking charge of 51%–100% of a company and asserting control over management. It is common in such circumstances for the manager of the PE fund to take on the role of company president, CFO, or other top executive, thereby asserting control over the company's management. As this representative comes into direct contact with the company, this activity is described as a "hands-on" approach. The basis for returns on the investment depend on the fund manager's managerial capabilities. However, as the investor (fund) is now directly responsible for the management of the company, it has also become responsible for ensuring the company's continuity. In other words, the fund now has a responsibility to the company's stakeholders. If the company's performance is improved over a short period of time, the company's value also increases over this period, in which case the fund may elect to sell the company to another company for a significantly higher price, or execute an IPO. The fund manager may have to work tirelessly for the first 100 days following the investment, initiating reforms to improve corporate value by executing a "100-day plan," over which significant improvements will be made to the company's governance framework. Everyday labor issues may also present difficult problems to management of the company, and to counter this, the PE fund will allocate staff who are accustomed to dealing with such circumstances. Environmental issues are also seen by PE funds as an opportunity to improve sales; thus, it has now become common for funds to target businesses that have some kind of affinity for the environment. In this way, ESG represents an important element to the creation of added value when adopting a hands-on approach. From an ESG perspective, therefore, activities to enhance corporate value and responsible investment are closely intertwined.

B. Effect of Leverage and Its Relevance to Responsible Investment

Leverage, or LBO finance, is a term used to describe the purchase of a company through a combination of equity investment and loans. This approach aims to boost equity value by using the company's profits to repay the loans (see Figure 4.4.3). LBO financing uses company profits to repay loans—returns are first allocated to the equity holder (the PE fund), effectively eliminating this portion of company profits. A leverage approach allows the PE fund to benefit first from the company's efforts, and as the PE fund is seen to be profiting directly from the efforts of the company's employees, it is believed to have assumed a responsibility to execute management in a way that safeguards the company's interests going forward. If the PE fund, which represents both financier and owner, demonstrates reckless or extravagant behavior, directors and employees are apt to take note very quickly, potentially resulting in the deterioration of company activities. If this occurs, the company's profits, which represent the source of the PE fund's loan repayments, may be placed in jeopardy. Shareholders do have rights, but in order to exercise these rights to maximize profits they must also strive to maintain a stance as responsible investors when executing strategies based on leverage.

Figure 4.4.3: LBO Finance (based on a model of completion over four years)



Source: Ark Totan Alternative Co., Ltd.

C. Effect of a Multiple-Based Approach and Its Relevance to Responsible Investment

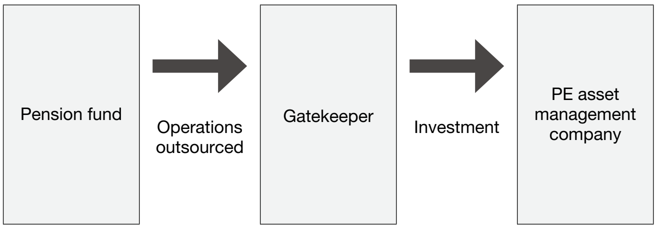
"Multiple" here denotes the EV/EBITDA multiple, which is calculated by dividing a purchase price (EV) by EBITDA, an indicator of profit. If the multiple is high, corporate value is considered to be high in comparison to profit and is deemed "relatively high," a common term used by those engaged in PE investment and M&A. There is no uniform standard pertaining to the multiple under which transactions will be made, but rather, specific multiples are determined by timing and industry. As it is best to make purchases when the price of the acquisition to be made is low, and sell at a time when the price is high, high investment efficiency can be secured by making an inexpensive acquisition when movement in the M&A markets is low, and by selling when the market is more vigorous and the purchase prices are experiencing a peak. This represents one aspect of investment returns acquired through a multiple-based approach. Moreover, the average multiple changes depending on the industry. For instance, if a logistics company were sold to become a logistics division of a company within a major manufacturing industry, it is possible to make the sale based on the multiple of the manufacturing industry, as opposed to that of the logistics industry. Either way, the transaction amount is based on the intrinsic value of the company to be traded, as determined by negotiations between the buyer and seller. Activities to acquire returns by taking advantage of fluctuations in market price and the differences in industry multiples give rise to responsibilities that buyers and sellers must honor to maintain trusting relationships. Omission of information that should have been communicated, or engaging in a transaction without communicating information accurately, may lead to claims arising following a sale. Depending on the circumstances, such actions may lead to litigation based on the allegations of breaching representation and warranty clauses. Responsible, sustainable transactions in PE investing are therefore also necessary when adopting a multiple-based approach.

(2) The Relationship Between PE and Responsible Investment in the Context of Pensions

General Structure of PE Investments at Japanese Pension Funds

Japanese pension funds are required to outsource their investments, and in general, these investments are outsourced to “gatekeepers,” which include trust banks and investment consulting companies. PE investment is no exception. Pension funds therefore impose rules concerning governance on these gatekeepers through the settlement of contracts (pension trust agreements/investment trust contracts) and the communication of investment guidelines (Figure 4.4.4).

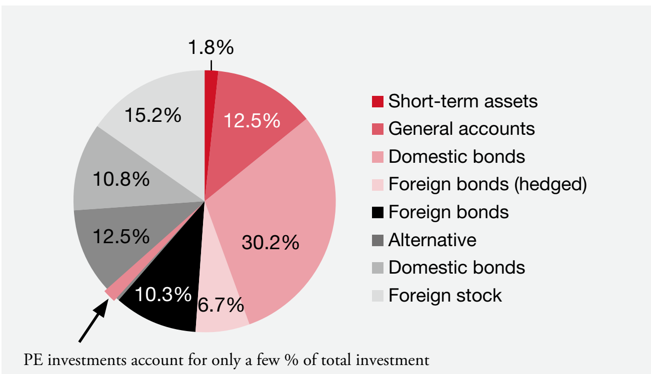
Figure 4.4.4: Structure of Outsourcing Operations for PE Investments



Source: Produced by Ark Totan Alternative Co., Ltd.

As of fiscal 2015, however, PE investments accounted for only a very small fraction of pension fund investment ratios, representing about 1%–4% of portfolios. Funds therefore cannot afford to channel resources into PE investments (Figure 4.4.5).

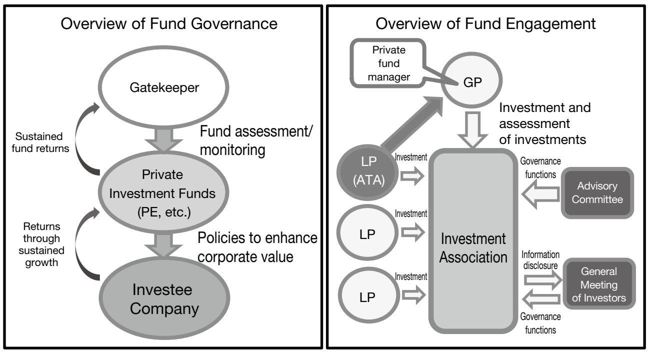
Figure 4.4.5: Asset Allocation of Defined Benefit Corporate Pension Plans (based on actual figures)



Source: Results of the Fiscal 2014 Survey on Pension Fund Management Trends (JPMorgan Asset Management (Japan) Limited)

It is the current trend for every aspect of pension fund operations to be entrusted to these gatekeepers. Being responsible for all aspects of PE investment, these gatekeepers are required to have a specialist knowledge of and experience in manager selection and cash management, as well as overseeing the governance of PE-specific funds and fund engagement efforts (Figure 4.4.6).

Figure 4.4.6: Fund Governance and Fund Engagement



Source: Ark Totan Alternative “Basic Policy on Stewardship”

(3) Responsible Investment in Private Equity (Conclusion)

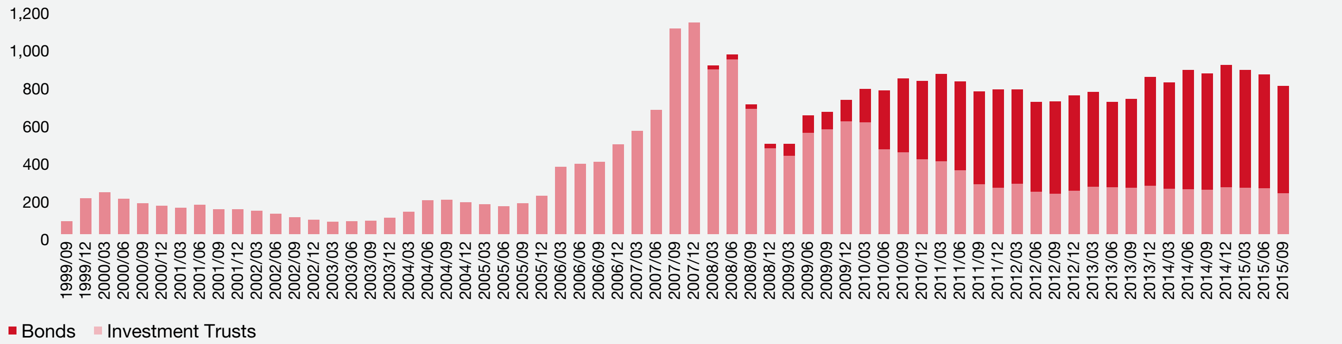
As previously stated, a responsible approach to PE investments is easy to implement and clearly gets results. Before sustainable investment, responsible investment, and ESG investment were formally defined, PE investment naturally occurred in a world of investment where such approaches had yet to be established. Its actions were naturally geared toward results that satisfied all the parties involved, and has proliferated because these parties have been able to prosper. The first PE/VC investments were implemented with the objective to reconstruct post-war Europe, and were executed through the U.S. Marshall Plan in the 1950s after the Second World War. Peter Brooke, who started the first PE investments, did so because he felt an affinity for the U.S.’s ideas on responsible investment and its sense of responsibility to the world, which emphasized the use of U.S. funds to influence the world in a positive way. In this way, the compassionate ideas that form the basis for responsible and sustainable investments are rooted in PE investment. Although the manner in which PE investments are implemented may vary from generation to generation, their underlying concept reflects an unchanging philosophy.

Shunsuke Tanahashi

Appendix

Trends in the Sustainable Investment Balance of Financial Products for Individual Investors

(¥ Billion)



Note: Total balance of publicly offered SRI investment trusts and bonds for individual investors

List of Works Related to Sustainable Investment

(Taken from the *Securities Analysts Journal* October 2013–September 2015)

- "Crowdfunding: Current Trends and Future Outlook," Atsuo Akai, January 2014
- "Important Role of Principles for Responsible Institutional Investors in Improving Long-Term Corporate Value in Japan," Sadayuki Horie, August 2014
- "The UK Stewardship Code and Implications for Japan," Ryoko Ueda, August 2014
- "Stewardship Code in Japan—From the Viewpoint of Investment Firms," Daichi Soda and Yosuke Mitsusada, August 2014
- "Influence of Japan's Stewardship Code on Companies," Tamami Ota, August 2014
- "ESG Factors in Corporate Valuation: Case Analysis of Utilization of ESG Information by Japanese Institutional Investors," Yasuyuki Sugiura and Hiroshi Miyai, October 2014
- "TSE Initiatives to Promote Timely Disclosure," Ryota Yasui, December 2014
- "Outline of Japan's Corporate Governance Code," Motoyuki Yufu, August 2015
- "My Hopes and Concerns Regarding Japan's Corporate Governance Code," Toshiaki Oguchi, August 2015

Author Biographies

Executive Summary

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Minako Takaba is a senior analyst and vice president at MSCI Inc. in its ESG Department. In 2000, she graduated from Aoyama Gakuin University with a degree in international political economy. Ms. Takaba went on to Yokohama National University Graduate School of International Social Sciences, earning a master's degree in 2002. She then joined KPMG AZSA Sustainability Co., Ltd., where she was involved in corporation-focused CSR consulting activities, after which she became a CSR manager at Vodafone Japan/SoftBank Mobile. That experience led her to RiskMetrics Group (currently, MSCI Inc.) in 2007, where she was involved in ESG research. Currently, she supervises ESG research on Japanese equities, and serves as a sector analyst for the global consumer and trading industries.

Ms. Takaba also co-authored "The Environmental Strategies of Financial Institutions" (Kinzai Institute for Financial Affairs, Inc., 2005). She is a JSIF committee member.

Chapter 1 Trends of Institutional Investors

1. Responsible Investment of Pension Funds

Tsukasa Kanai

Tsukasa Kanai is the senior manager of the Management Planning Department and head of CSR at Sumitomo Mitsui Trust Bank, Limited, and also serves as a member of its Board of Directors. Upon graduating from Osaka University's School of Law in 1983, Mr. Kanai joined Sumitomo Trust & Banking Co., Ltd. After serving in the London office and the Pension Investment Department, he was appointed to the Head Office as Executive of the Corporate Social Responsibility Office in the Corporate Planning Department in 2005. In April 2012, he became the senior manager of the Management Planning Department while also overseeing the CSR Promotion Office at Sumitomo Mitsui Trust Bank, Limited. He has managed all aspects of the Sumitomo Mitsui Trust Group's CSR activities, including ESG investing. He is a member of a committee for addressing the Principles for Financial Action toward a Sustainable Society, and the steering committee of the Multi-Stakeholder Forum on Social Responsibility for a Sustainable Future.

Mr. Kanai co-authored major works, including "All about Strategic Pension Management," "CSR Management and SRI," "SRI and New Business and Finance," and "The Beginner's Guide to Natural Capital."

2. Responsible Investment: Initiatives at the Resona Bank Asset Management Division

Minoru Matsubara

Minoru Matsubara is the chief manager of the Asset Management Business Planning Division at Resona Bank, Limited. Mr. Matsubara joined Resona Bank in 1991, assigned to the Pension Trust Fund Management Division. He continued on to undertake asset management and planning duties at the Investment Planning Office and Public Fund Management Division, the Pension Trust Fund Management Division, the Trust Fund Management Division, and the Fund Management Supervisory Division. He assumed his current role in April 2009.

Mr. Matsubara was also a visiting researcher at the Research Institute for Policies on Pension and Aging in 2000 and 2005. He is also a member of the Securities Analysts Association of Japan's Planning Committee and Investment Performance Standards Committee, as well as the ESG Research Committee for the Analysis of Corporate Value (from June 2015). He is a JSIF committee member.

Mr. Matsubara also coordinates the MPT Forum, is the chairman of the PRI Corporate Working Group, and is a committee member at the Forum of Investors Japan.

[Column] The Perception of Japan from Overseas

Takeshi Mizuguchi

Takeshi Mizuguchi is a professor at the Faculty of Economics, Takasaki City University of Economics. He is the Representative Director & Secretary General at JSIF. After his employment at Nichimen and Eiwa Audit Corporation, Mr. Mizuguchi became a lecturer at the Takasaki City University of Economics in 1997, and subsequently assumed his current role in 2008. His main fields of research include environmental accounting, the disclosure of environmental information by corporations, and responsible investment. On April 1, 2015, Mr. Mizuguchi went to London for a one-year overseas research visit at EIRIS, an ESG research institution. His main written works include the co-authored "What is Social Investment" (*Nihon Keizai Hyouronsha*); "Accounting and Investment to Change Society" (*Iwanami Shoten*); "A Basic Knowledge of SRI" (Japanese Standards Association); the co-authored work "Management and Accounting for the Environment," (*Yuhihaku*); "The Environment and Trends in Finance and Investment" (*Chuokeizaisha*); and "Responsible Investment: Changing the Future through Capital Flows" (*Iwanami Shoten*).

Chapter 2 Trends of Individual Investors

1. Investment Trusts

Masaru Otake

Masaru Otake is a JSIF committee member working concurrently at a financial information provider. Mr. Otake graduated from Hosei University's Faculty of Social Sciences in 2007, and in 2009, he completed the first stage of the Ph.D. program at the Graduate School of Global Environmental Studies of Sophia University, receiving a master's degree in environmental studies. His fields of research include environmental finance and SRI.

2. Bonds

Ken Tokuda

Ken Tokuda is engaged in bond underwriting activities for domestic and foreign issuers at Daiwa Securities Co. Ltd.'s Debt and Capital Markets Department. Mr. Tokuda joined Daiwa Securities in 2005, where he was involved in sales activities at the company's branch offices. He also worked in the Daiwa Group Human Resources Department at the Head Office and went on to study overseas before assuming his current position. Mr. Tokuda graduated from Keio University's Faculty of Economics before earning a master's degree in economics from the Kenan-Flagler Business School, University of North Carolina, at Chapel Hill.

Chapter 3 Shareholder Advocacy

Akemi Yamasaki

Akemi Yamasaki graduated from Hitotsubashi University's Faculty of Law in 1981. After working some time at a major Japanese securities firm, Ms. Yamasaki joined a think tank.

There she was involved in SR/IR consulting work and research as well as the study of corporate governance and ESG. Ms. Yamasaki is a JSIF committee member. She co-authored many books and wrote reports and articles on the stewardship code, corporate governance, proxy voting, and SRI/CSR/ESG.

Chapter 4 Sustainable Finance

1. Principles for Financial Action

Keisuke Takegahara

Keisuke Takegahara is General Manager of the Economic & Industrial Research Department at the Development Bank of Japan Inc. (DBJ). Mr. Takegahara graduated from Hitotsubashi University's Faculty of Law in 1989 and in the same year joined the DBJ. He assumed his current position in 2016 after gaining experience in the Research Department and Policy Planning Department as the chief representative in Frankfurt and as General Manager of the Environmental Initiative & Corporate Social Responsibility-Support Department. Mr. Takegahara oversees DBJ finance certification programs including the Environmentally Rated Loan Program. He is also the head of the Steering Committee for the Principles for Financial Action towards a Sustainable Society, and is engaged in various activities at public institutions including the Ministry of the Environment, the Ministry of Agriculture, Forestry and Fisheries, and as a member of NEDO's Technology Committee. He has co-written works, including "Environment Ratings," "Responsible Finance," and "What We Can Learn from Germany's Urban Environment Model."

2. Community Investment and Crowdfunding

Shunji Taga

Shunji Taga currently serves as an executive director and a small and medium-sized enterprise management consultant at the Japan NPO-BANK Network. Mr. Taga was born in Hiroshima in 1965. He was involved in the 1994 establishment of Mirai Bank, which is known as the first NPO bank in Japan. Further, he has been a participant in A SEED Japan's "Eco Savings" project since 2003.

In fall 2004, Mr. Taga realized that the revision to the Financial Instruments and Exchange Act of Japan threatened the existence of NPO banks in Japan. Seeking to save these NPO banks, he organized forums and helped bring about the evolution of the current Japan NPO-BANK Network. Since then, Mr. Taga has continued to strive daily to further advance the development of NPO banks and social finance throughout Japan.

[Column] Micro-Investment: Investing Small, Enriching Japan's Future

Masayuki Oki

Masayuki Oki is a private investor, but his main occupation is as a systems engineer. Mr. Oki became interested in socially responsible investing while researching potential companies to invest in. He first came across micro-investment in 2008 and began to get involved in such activities the following year. He felt a strong connection to this new form of investment because he sympathized with its objectives. He now works to communicate the benefits of investments that are geared toward more than just earning money through his blog, *My Journal of the Search for Good Investments from Shintokorozawa*.

3. Environmentally Friendly Real Estate

Hiroki Hiramatsu

Hiroki Hiramatsu is the CEO of Woonerf Inc. He is a Faculty and an accredited LEED professional of the U.S. Green Building Council (LEED AP BD+C: New Buildings and LEED AP ND: Neighborhoods). In 2015, he was elected as the first LEED Fellow in East Asia.

Mr. Hiramatsu graduated from Osaka University of Foreign Studies in 1984 and started his career at a Japanese-U.S. securities company. In 2002, he left his position as a managing director at the Merrill Lynch Fixed Income Division to pursue landscape design and green building. In 2006, he established Woonerf Inc.

Mr. Hiramatsu is the chairman of the Ministry of Environment Principles for Financial Action for the 21st Century's Green Real Estate Working Group and is a JSIF committee member. He is also a member of the CASBEE subcommittee for real estate assessment.

4. Private Equity

Shunsuke Tanahashi

Shunsuke Tanahashi is a partner and CEO at Ark Totan Alternative Co., Ltd. Mr. Tanahashi graduated from Tokyo University's Faculty of Economics, and holds an MBA from the University of Michigan. He is a chartered member of the Securities Analysts Association of Japan.

Mr. Tanahashi joined Mitsubishi Trust Bank (currently, Mitsubishi UFJ Trust Bank) in 1996, where he specialized in asset management and was seconded to the Research Institute for Pensions and Policies on Aging (currently, the Research Institute for Policies on Pension and Aging). From 2005–2006, he was the only Japanese "Expert Group Member" to contribute to the establishment of the UN's PRI. In 2008, he joined Goldman Sachs Asset Management and, in 2009, went on to join Ant Capital Partners, where he headed up the firm's investor relations team. He established Ark Alternative Advisors in October 2010.

As CEO of Ark Totan Alternative, Mr. Tanahashi works to promote alternative investment among Japanese institutional investors in a bid to change investor attitudes and the way that funds are selected. He is also the chairman of PRI Japan Network's Private Equity Working Group.

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