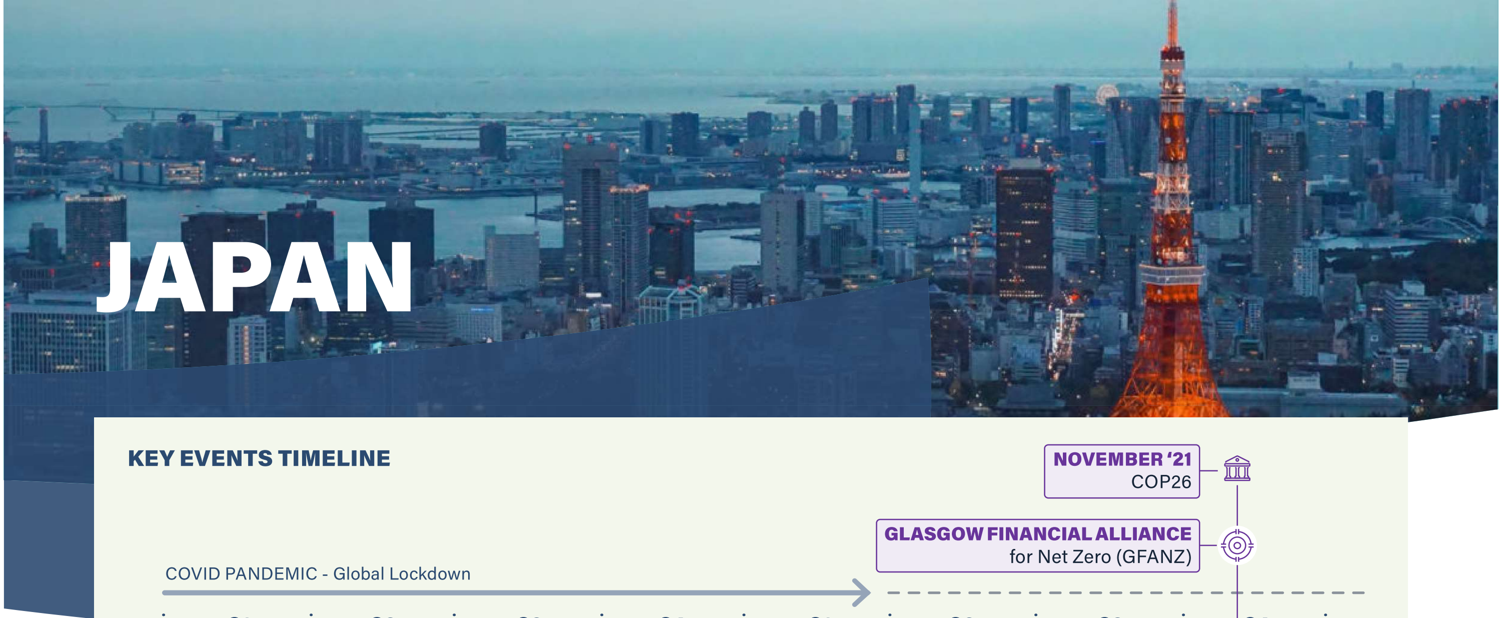
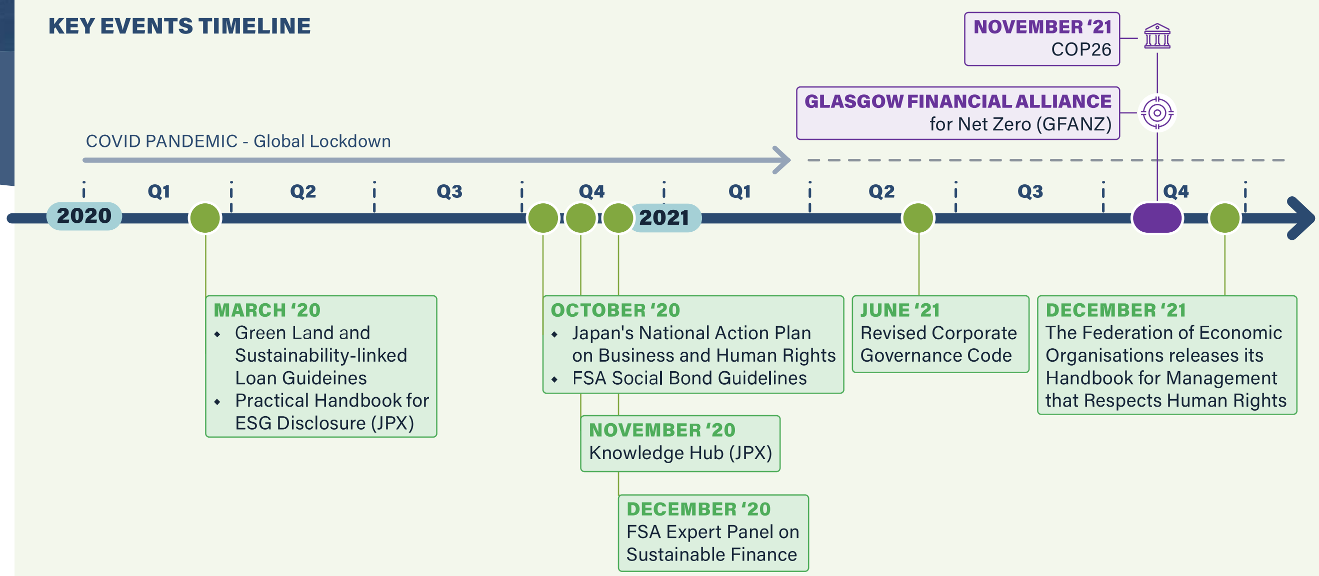


JAPAN

KEY EVENTS TIMELINE



10 Year Reflections

Over the past decade, Japan's sustainable investment landscape has experienced significant growth and change. 2013 marked a foundational year for responsible investing, beginning with the Abe administration's Japan Revitalization Strategy in 2013, which laid the foundation for sustainable and responsible investment in Japan. In the same year, the Government Pension Investment Fund (GPIF) underwent a governance restructuring, leading to the diversification of its portfolio by cutting down on bond investments, primarily in Japanese government bonds, and increasing its equity proportion. The subsequent years saw the introduction of the Japanese Stewardship Code (2014) and the Corporate Governance Code (2015) by the Financial Services Agency (FSA), solidifying the framework for responsible investments and corporate transparency.

In 2015, GPIF became a signatory of the Principles for Responsible Investment (PRI), in a move that catalysed ESG's growth in the country. GPIF, as a PRI signatory, subsequently published its Responsible Investment Policy and amended its stewardship responsibilities to ensure asset managers consider ESG factors in their engagement activities. Moreover, GPIF required detailed reporting from asset managers on their PRI activities and stance.

In 2017, the Stewardship Code and the Ito Report were updated, the Japan Exchange Group joined the Sustainable Stock Exchanges. TCFD (Task Force on Climate-related Financial Disclosures) garnered attention, leading the Ministry of Economy, Trade and Industry (METI) to develop TCFD guidance and initiate a consortium in 2018. Japan led in TCFD support and was a significant backer of Science Based Targets and RE100 initiatives. In 2019, the Ministry of Foreign Affairs released the National Action Plan (NAP) focusing on Business and Human Rights. The following year, METI published the Ito Report on Sustainable Corporate Value, specifically addressing human capital considerations. The 2021 update to the Corporate Governance Code was significant due to its inclusion of a mandate for appointing a minimum of one-third independent external directors, as well as a new section addressing sustainability.

> *'Over the past decade, Japan's sustainable investment landscape has experienced significant growth and change.'*

Japan's bond market has also seen strong growth. In 2014, the first green bond was issued, followed by subsequent issuances by commercial banks and local governments. The Ministry of Environment's (MoE) Green Bond Guidelines in 2017 and the Financial Services Agency (FSA)'s Social Bond guidelines in 2021 bolstered this section of the market. In May 2021, the MoE, METI, and FSA jointly formulated foundational guidelines for climate transition finance following the publication of ICMA's Climate Transition Finance Handbook (December 2020). In 2022, the Japan Exchange Group (JPX) launched an ESG Bond Information Platform. There have been notably more transition-labelled bonds issued in Japan than in other countries.

Finally, sustainable investment trusts witnessed significant growth from 2020 onwards, with the funds surpassing previous records. In 2023, guidelines for ESG Investment Trusts were issued by the FSA, aiming to streamline the sustainable investment process.

10 Year Forward Look

Japanese sustainable investment has been and will be marked by collaborative efforts between the public and private sectors. Combined initiatives have allowed Japan to quickly advance in responsible, sustainable investment. A hallmark of Japan's responsible investment is its emphasis on transitional strategies, influenced by its manufacturing-centric economy. Instead of rapid shifts, Japan is innovating in areas like battery technology, green fuels, and environmentally friendly steel production. The global adoption of Japanese green technologies, such as electric railways, showcases Japan's contribution to reducing GHG emissions.

At the 2023 PRI in Person event, Prime Minister Fumio Kishida announced that seven public pension funds (worth $600 billion) would become PRI signatories[1]. This is another indicator of Japan's increasing commitment to responsible, sustainable investment. The FSA is developing the Draft Basic Guidelines on Impact Investment, indicating forthcoming discussions and advancements in this sector.

Finally, the Japanese government is advocating for Green Transformation (GX), in order to 'change the industrial and social structure to shift away from fossil fuels', with an emphasis on clean energy. The government plans to raise $1 trillion in transition finance for Net Zero by 2050. The key strategy to raise this finance is the government's Climate Transition Bonds. These sovereign transition bonds are the world's first and will be worth JPY 20 trillion ($130 billion), aimed at renewable uptake and industrial innovation by attracting private sector investment worth JPY 130 trillion ($870 billion) or more, which is said to be necessary for decarbonisation in Japan. All in all, responsible investing, particularly investing in the net zero transition, looks to become increasingly mainstream in Japan over the next 10 years.

Policy & Regulatory Drivers

In Japan, the growth of the sustainable and responsible investment market during the reporting period was accelerated by policy and regulatory developments. These developments were the result of collaboration between the government and regulators alongside market participants.

The Japanese FSA established the Taskforce on Sustainable Finance in 2020, made up of business, financial, and academic experts and observers from relevant ministries and agencies. The Taskforce was initially brought together to discuss issues and policies to achieve carbon neutrality by 2050, and later broadened to wider sustainable finance issues. The first report was released in 2021, and since then the Taskforce has been following up on the issues raised in this report.

The government launched Japan's National Action Plan on Business and Human Rights in 2020, and started the Liaison Conference of the Relevant Ministries and Agencies. Since then, follow-up roundtables have been held regularly to facilitate and implement human rights issues across the business sector including Guidelines on Respecting Human Rights in Responsible Supply Chains issued by METI. In October 2020, the FSA announced the Social Bond Guidelines. The Ministry of the Environment launched the Green and Sustainability-linked Loan Guidelines in 2020 and revised them in 2022. The guidelines are consistent with the internationally recognised Green Loan Principles and Sustainability Linked Loan Principles and intend to provide a framework for borrowers, lenders and other parties. The guidelines present measures and interpretations in line with the characteristics of the Japanese market and ensure credibility of greenness and reduction of administrative cost for borrowers.

Finally, the FSA announced the Code of Conduct for ESG Evaluation and Data Providers in December 2022 and called for endorsement of the Code to data providers.

Industry Collaboration

The development of industry guidelines is becoming more commonplace. The Federation of Economic Organisations (Keidanren) revised Chapter 4 on Respect for Human Rights in its Charter of Corporate Behaviour Implementation Guide. It published the Handbook for Management Respecting Human Rights in December 2021. The handbook provides specific information for officers in charge of practical implementation in their organisations. The Japan Exchange Group (JPX) issued the Practical Handbook for ESG Disclosure in May 2020 and launched the JPX ESG Knowledge Hub. On this platform, listed companies and other parties can access ESG investment and sustainable finance information as of November 2020. In 2022, JPX initiated a website on listed companies' ESG information and launched a platform on ESG bonds in July, where lead underwriters for bond issuances provide details of ESG bonds issued within Japan.

1. All currency figures on this page (namely JPY to USD) are converted as of November 2023.

Customer Drivers

The retail market saw a substantial expansion in ESG and sustainable investment trust funds during 2021 and 2022. After peaking in 2008, the sustainable investment trust funds lingered at a low level until a remarkable increase in 2021 and 2022, reaching close to JPY 4 trillion ($ 27 billion), quadrupling the original 2007 peak. This resurgence was mainly in dollar-dominated funds due to a weaker yen and a depressed domestic equity market. Most of these funds focused on specific ESG themes rather than broader ESG-themed funds, with some releasing impact reports outlining the fund's ESG targets, alongside disclosures such as total carbon emissions and carbon offsets used to achieve net zero emissions of the funds. Increased reporting has notably heightened retail investors' awareness regarding the impact of ESG funds. To further promote and facilitate sustainable investment for retail investors, the FSA updated its guidelines regarding ESG investment trusts in March 2023 and plans to initiate a stakeholder dialogue aimed at improving sustainable investment products.

Market Drivers

In Japan, Sustainable Investment assets under management continued to increase by 59.2 % to JPY 493.6 trillion ($ 2,874 billion) in 2022 from JPY 310.0 trillion ($ 4,289 billion) in 2020[2]. The proportion of sustainable investing assets relative to total managed assets in 2022 was 33.6% compared to 24.3% in 2020. ESG equity investing levelled off since 2018, while green and sustainable bonds increased rapidly from 2019. Mainstream investors embraced ESG Integration and sustainability-themed investing focused on investment impact in 2021.

JSIF reported in the GSIR 2020 that using sustainable investment to drive positive outcomes was still in the early stages in Japan due to legislation that limited shareholder activism. However, by tightening the voting rights standards for domestic investors and introducing non-Japanese proxy advisors' criteria for climate change and board gender diversity, the shareholders' actions were drastically altered and the number of shareholder proposals increased considerably for 2023 AGMs.

Sustainable Investment Association in the region – Japan SIF

The Japan Sustainable Investment Forum (JSIF) was formed in 2003 as Japan's not-for-profit organisation promoting the concept and practices of sustainable and responsible investment in the country. JSIF provides a forum for the interactive exchange of ideas and research for financial institutions, academics, government organisations and other interested parties in the field of sustainable investment. JSIF also encourages companies to provide disclosures of non-financial information to build a sustainable society through the sound development of the financial market. JSIF is a member organisation of the Global Sustainable Investment Alliance (GSIA) and contributes to the market study of Japanese sustainable investing. Visit JSIF's website.

2. The denominator of the above figures was based on the flow-of-funds figures released by the Bank of Japan. The proportion calculated by the reported figures by the institutions that replied to JSIF's survey was 61.9% in 2022 against 51.6% in 2020.