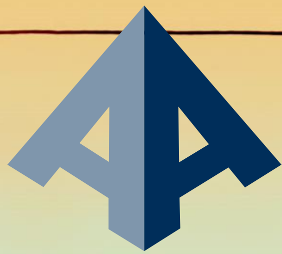

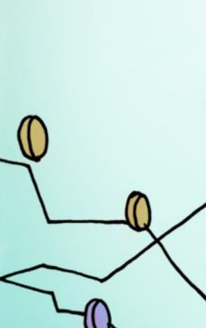

CG WATCH 2023

JAPAN

Ramping up CG reform

Japan leaps to second in ACGA rankings

Special report - May 2024

Founding Sponsor of ACGA

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Great

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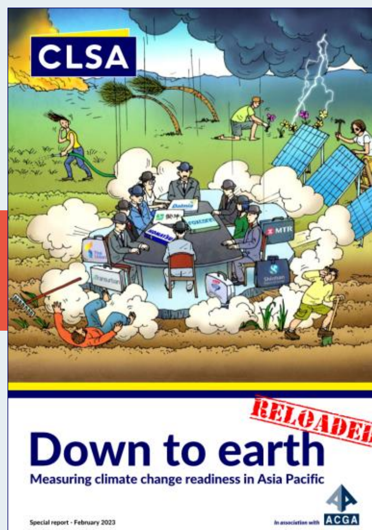
Through ACGA's lens



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Ramping up CG reform

Japan rises to second place in Asia Pacific CG rankings

Japan's significant strides in corporate governance (CG) have propelled it to second place in our top-down regional rankings, its best position in 20 years. Regulatory reform and progress among multiple stakeholder groups have played a crucial role. Investors are strengthening company engagement and employing tactical voting, while activism and active ownership are on the rise. Companies are improving CG disclosure and sustainability reporting, and director training quality is marching ever higher. Media coverage of CG is also expanding.

Regulatory reforms and gender diversity remain focus areas

At the regulatory level, the Financial Services Agency (FSA), Tokyo Stock Exchange (TSE) and Ministry of Economy, Trade and Industry (METI) are addressing longstanding issues. The securities commission launched an "Action Program" in April 2023 to accelerate CG reform and boost shareholder rights. The TSE is, at long last, driving hard on capital efficiency and corporate profitability to address low valuations among its issuers. METI is raising the bar for fairer and more transparent takeovers. The government is prioritising gender diversity in listed companies and women's empowerment more broadly. These efforts reflect a renewed sense of urgency, not seen for some time.

Closing the gap on other leading markets

But a score of just under 65% indicates that Japan is not out of the CG swamp yet. And with regulatory reform still a work in progress, it is too early to declare victory. Issuers have responded well to the TSE's cost of capital drive, but it is uncertain if their efforts will endure. Companies are improving CG disclosure, but still lag other leading markets. Investors may be voting and engaging more actively, but collaborative engagement is still rare. And director training remains insufficient for the massive task at hand. Even so, Japan is in its best position for a very long time, and we hope the momentum generated by the past two years' reforms will continue.

Activism surging as cross-shareholdings unwind

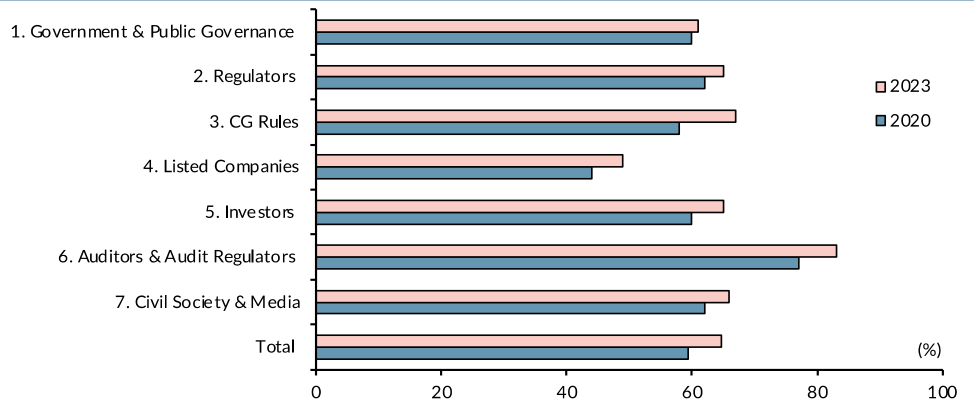
We look at the possibilities that emerge as the stock exchange and ministries put pressure on Japanese corporations to release the significant untapped wealth in cross-shareholdings and net cash. Moreover, we emphasise the role of activism in Japan's turnaround story, with a remarkable 156% YoY rise in such events in 1Q.

We highlight CLSA's top-10 scorers in Japan

CLSA's updated bottom-up CG scores reveal a 2.1ppt improvement among Japanese corporates versus 2020, driven by the independence and discipline pillars. By sector, hotel & leisure improved most while energy deteriorated. We also highlight the top-10 scorers and improvers within CLSA Japan coverage, as a proxy for firms actively committed to improving CG practices.

Japan's scores rise in all categories in 2023

Japan CG macro category scores: 2023 vs 2020



Source: ACGA

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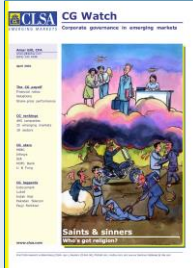
CG Watch through the years



Saints & sinners

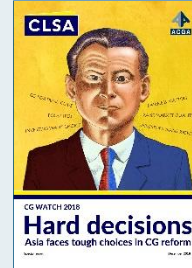
April 2001

Our first edition surveyed and ranked 495 stocks in 25 emerging markets. High CG scorers generally outperform. South Africa, HK and Singapore score well as do transport manufacturing, metals/mining and consumer.

On a wing and a prayer

September 2007

We include "clean and green" criteria in our corporate governance scoring. Climate change is now a matter of corporate responsibility, with attendant economic risks. Yet, Asian firms are largely ignoring the issue.



Hard decisions

December 2018

Regional markets face hard decisions in CG reform as mounting competition for IPOs raises pressure to lower standards. But there is still plenty of evidence of the push toward better CG. Australia maintains its lead, while Malaysia is the top mover.

Make me holy . . .

February 2002

Almost invariably, companies with high CG scores remained market outperformers this year. The top-CG quartile outperformed the country index in nine out of 10 Asian markets under CLSA coverage.

Stray not into perdition

September 2010

Corporate governance standards have improved, but even the best Asian markets remain far from international best practice. Our CG Watch rankings may surprise investors this year even more than the 2007 reordering.

Future promise

May 2021

Our latest edition of CG Watch is bigger and better than ever - two powerful reports provide unique perspectives on how markets and sectors in Asia are rising to the challenge of building sustainable growth.

Fakin' it

April 2003

Companies are smartening their act as stocks with high CG scores outperform. But much of the improvement is in form - commitment is not yet clear. Market regulations are moving up and it is time for regional shareholders to organise.

Tremors and cracks

September 2012

Cracks in Asian corporate governance have become more apparent since our last CG Watch. We provide CG and ESG ratings on 865 stocks , rank the markets and indicate issues investors should watch for in the tremors of Asian investing.

A new order

December 2023

Capturing the biggest ranking shift in 20 years, we see Japan surging and Hong Kong posting a precipitous slide. Strong governance pays, and firms with good CG scores tend to have higher social scores.

Spreading the word

September 2004

Our more rigorous CG survey of 10 Asian markets ex-Japan finds improvements in many of the 450 stocks we cover, following new rules introduced in recent years. CG also emerges as an explanation for beta.

Dark shades of grey

September 2014

This year, we rated 944 companies in our Asia-Pacific coverage. Japan has moved higher, while Hong Kong and Singapore have slipped. Corporate scores have fallen, particularly in Korea. We have revamped our environmental and social scoring.

The holy grail

October 2005

QARP (Quality at a reasonable price) is a guide for stock selection in the quest for high-CG stock performance. In the three years to 2004, the QARP basket of the largest 100 stocks in Asia ex-Japan beat the large-cap sample.

Ecosystems matter

September 2016

Governance matters and ecosystems are key. No one stakeholder drives the process; it is the collective interaction that delivers outcomes. Australia heads our bottom-up survey and joins ACGA's top-down survey at No.1. Asia is improving.

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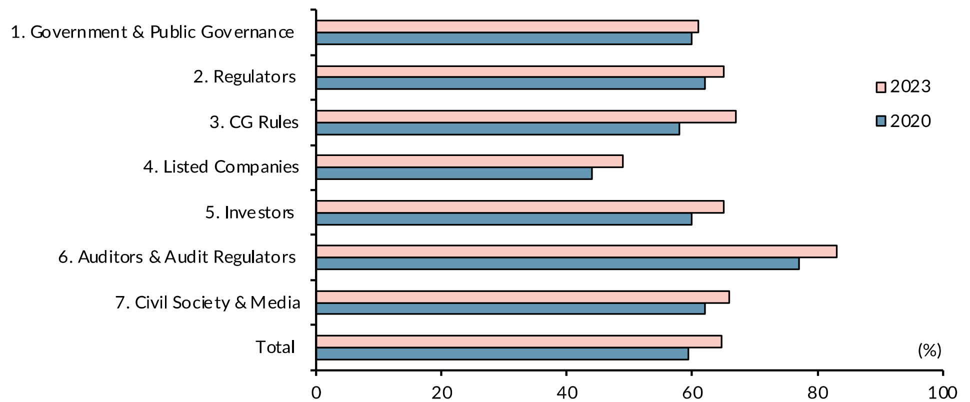
Japan - “A” for effort, “C” for disclosure

- Japan leaps into second place in our rankings from equal fifth in 2020. This its best showing in 20 years of CG Watch and primarily reflects the effort being made by multiple stakeholders. Disclosure on board governance still mediocre
- Robust TSE focus on capital efficiency and profitability to address low valuations of listed companies
- New FSA “Action Program” to accelerate CG reform and resolve some entrenched weaknesses in shareholder rights
- Government driving gender diversity and women’s empowerment; new TSE listing rules on gender diversity
- New METI guidelines promoting fairer and more transparent takeovers
- Companies improving CG disclosure, but poor by regional standards
- Investors strengthening individual company engagement and tactical voting, but collaborative engagement on CG remains limited
- Breadth and depth of activism and active ownership increasing
- Director training quality high, but quantity vastly insufficient
- Media coverage of CG is broadening and deepening

Japan’s scores rise in all categories in 2023

Figure 1

Japan CG macro category scores: 2023 vs 2020



Source: ACGA

Introduction

A new air of determination is driving CG policy in Japan

There has been a change of spirit in Tokyo over the past 12 to 18 months, a new air of determination. A somewhat ambiguous post-Shinzo Abe approach to CG reform has been replaced by a more focussed, energetic, and determined policy environment in which companies have been given their marching orders on capital management and financial regulators are starting to address some of Japan’s most entrenched governance challenges. Thorny issues like “allegiant shareholdings” (aka cross-shareholdings) are in the spotlight as never before and partly for business reasons: companies deciding they need to free up capital for new investment. The number of minority shareholder proposals increased significantly in 2023 and investors almost succeeded in toppling the formidable chairman and CEO of one the country’s leading firms. It feels like springtime again in Japan.

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Investors want to know if this time really will be different

Yet the question many investors want an answer to is, "Will this time really be different?" Having dived into Japan in early 2013 on the hope that promised CG reforms under the new Shinzo Abe administration would transform listed companies into sustainable value creators, many foreign institutional investors had their fingers burnt in the market collapse of early 2016. Although the market subsequently recovered, a large number remained sceptical. The good news for investors is that some of this worry seems to be subsiding: the Japanese stock market went on a tear during 2023, thanks in part to foreign money leaving China, and reached an almost 34-year high towards the end of January 2024. That in turn has given policymakers renewed confidence they are on the right track, with all key regulators showing greater ambition.

Despite ranking second in our survey, Japan's score should be much higher

Our aim in this chapter is to outline the core reasons for Japan's rise in ranking, where the main points of systemic weakness lie, and what could or should be improved further. Despite jumping into second place in our ranking on a score of just under 65%, an economy as advanced as Japan's should be doing a lot better. The sceptics are right to be wary as it may be hard for policymakers to maintain the current reform momentum and there is no guarantee the market will keep rising. Yet Japan has always had the capacity to surprise. We believe there is room for optimism.

Recapping CG Watch 2020

The government's new CG Action Program addresses longstanding problem . . .

After falling badly to 7th in our 2018 survey - largely the result of stagnant policymaking, weak enforcement, and sclerotic corporate governance practices - Japan rose two places to equal 5th in 2020. With the release of the new "Action Program" from the FSA in April 2023, the government indicated that it would finally stop kicking the can down the road on a range of longstanding regulatory weaknesses, as the table below highlights. It also shows that some problem areas from our previous survey remain.

. . . notably takeover, engagement and concert party rules

Figure 2

Japan: recap of selected 2020 recommendations

	Recommendations	Outcomes
1.	Urgent need to address longstanding weaknesses in shareholder rights regarding takeovers, concert party rules, the "act of making important suggestions", and other areas. There should be a safe harbour document for investors.	New FSA "Action Program" highlights the need to improve regulation of takeovers, collective action, and the act of making important suggestions. Work begins in mid-2023. No final resolution yet, though FSA working group released preliminary recommendations in December 2023.
2.	Need for greater transparency in regulatory funding and resources.	No substantive change in disclosure.
3.	Improve listed-company CG and ESG reporting.	Steady progress on ESG disclosure, very limited improvement in CG reporting.
4.	Merge the Business Report (under company law) and Yuho (under securities law).	No progress, although a reference to "enhancing the efficiency of disclosure of duplicate information" is in the Action Program.
5.	Produce a regulatory guide to key rules and regulations in company and securities law.	No progress.
6.	Investors should provide more substantive reasons for voting against.	No progress.

Source: ACGA

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1. Government and public governance

Japan moved up to 3rd with a score of 61%

Japan improved to 3rd in this category, from equal 4th in 2020, for reasons that have more to do with other markets than its own performance. Hong Kong's score collapsed from 65% to 55%, while Korea and Singapore (which shared 4th in our previous survey) both dropped points. Japan's score rose only one percentage point and remains well behind Australia at 71% and Taiwan at 67%.

Unlike most markets in the region, Japan has a focussed CG agenda

The Japanese government gained points for having a clearer and more credible CG strategy. Its approach is less fragmented than in the past, in our view, and it provides consistent support for the enforcement work of the FSA and TSE. We re-rated our score for the governance of banks and also took into account the government's efforts to promote women's empowerment. All these factors should have a positive effect on corporate governance and company management over the medium to long term.

PM Kishida's 'new capitalism' plan initially raised concerns that CG would be a low priority issue

Fortunately, the uncertain views of the new Fumio Kishida government in 2022 towards CG did not persist. When Cabinet approved the prime minister's "Grand Design and Action Plan for a New Form of Capitalism" in June 2022, with its focus on stakeholders, reducing quarterly reporting burdens and accelerating the establishment of start-ups, many in the investor community wondered if this marked the re-emergence of the anti-CG brigade. Over time, these fears have largely proved unfounded, with Kishida increasingly recognising the need for further capital market and governance reforms. Indeed, even the quarterly reporting "streamlining" proposal turned out well for investors (*see CG Rules below*).

Where scores remained the same

We saw little change in several areas, some of which continued to score well, such as the coherence of the regulatory structure governing the capital market and civil service ethics. Areas once again achieving a moderate score included access to the legal system to resolve shareholder disputes and the governance of state companies. Questions with entrenched lower scores relate to the independence of the securities commission (ie, FSA) from the government, the extent to which it is funded independently (eg, through a levy on the stock market rather than from the government budget), and whether there is a standalone anti-corruption commission.

Where scores fell

Areas where Japan lost points in government and public governance included the effectiveness of the fight against corruption - we saw little improvement or change here, hence reduced scores slightly - and the role, independence, and skill of the judiciary.

A more coherent CG strategy

CG policy in Japan is seeking to inculcate more substance, less formalistic compliance

While Japan lacks a single document outlining its policies in corporate governance, we believe that there is a greater degree of coherence to its approach than in the past. As the title of the FSA's new Action Program indicates, there is an attempt now to move beyond the form of governance and try to inculcate more substance among listed companies. The Program does this by seeking tangible improvements in three areas:

1. Management issues: Encouraging greater awareness of cost of capital, profit making, sustainability, and human capital.
2. Effectiveness of independent directors: Performance of the board, nomination and remuneration committees, and director quality.
3. Company-investor dialogue: Enhancing disclosure and addressing legal and market environment issues (ie, shareholder rights).

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The FSA wants companies to view CG as an interconnected system

The FSA rightly sees these issues as interconnected and mutually reinforcing. It says that they “must be addressed and dealt with simultaneously”. It adds a sense of urgency to the policy, stating that “it is vital to move the focus of reform from form to substance” and that producing ever-more detailed CG regulatory requirements might undermine the purpose of reform, namely “boosting the growth of listed companies and the increase of corporate value over the mid- to long-term”. While we do not fully subscribe to this argument - since half-baked regulation is arguably a large part of the problem in Japan - we certainly welcome the desire to avoid encouraging yet more boxticking by issuers (*a huge problem, as we show in our Listed Companies section below*).

Efforts by the TSE and METI are aligned with the FSA's Action Program

In terms of policy coherence, it is significant that both the TSE's aggressive efforts on cost of capital and METI's push for fairer corporate takeovers complement elements of the Action Program (*for more details, see the Regulators section below*). It is also important to note that, in a departure from normal practice, the FSA decided not to organise yet another revision of the Stewardship Code after the latest three-year cycle. This would have fallen in the first half of 2023 and represented the third revision of the Code since 2017. Given the Code is in robust shape, regulators decided to spend their political capital elsewhere. A good choice, in our view.

Women's empowerment

The Japanese government is pushing hard to empower women in business

With one of Asia's, if not the world's, lowest levels of female participation in corporate management and listed-company boards, the Japanese government in recent years has undertaken several efforts to address workplace gender inequality and promote greater diversity. In 2016 the “Act on the Promotion of Female Participation and Career Advancement in the Workplace in Japan” came into force. This required public- and private-sector companies above a certain size to measure gender diversity data, create action plans to address gaps, and disclose this information. The Act was revised in June 2019 and extended to more companies. Then in December 2020 the government approved “The Fifth Basic Plan for Gender Equality”, which outlined a series of specific targets across a range of areas including raising the proportion of women in leadership roles, supporting the development of female executives and managers, and fostering greater participation of women in science and technology.

In April 2023, the PM publicly supported targets for women directors and senior executives

The Kishida government has sought to build on this policy momentum. In January 2023, a new Cabinet Office ordinance mandated disclosure of the percentage of women in management positions and wage differences between male and female workers. In April 2023, the prime minister stated publicly, for the first time, that henceforth all companies should strive to fill at least 30% of “yakuin” positions (a broad category that includes senior managers, directors, and statutory auditors) with women by 2030. In June of the same year, his government released a new “Intensive Policy for Gender Equality and Empowerment of Women 2023” that aimed, among other things, at speeding up the appointment of women to leadership positions within listed companies. It also instructed the TSE to amend its listing rules to require such changes of Prime Market issuers (*see CG Rules below)*.

The ratio of women directors is rising steadily

These policies are starting to bear fruit, as the chart below from the Sustainable Stock Exchanges (SSE) Initiative shows. This uses Bloomberg data and indicates that while Japan remains well behind most other developed markets, it has made strides since 2021 in the ratio of women directors among the top 100 issuers. While such ratios in Japan typically include not only women directors, but women also sitting on Kansayaku or statutory auditor boards, there has been a notable move by companies to appoint women to boards, some for the first time in 2022 and 2023.

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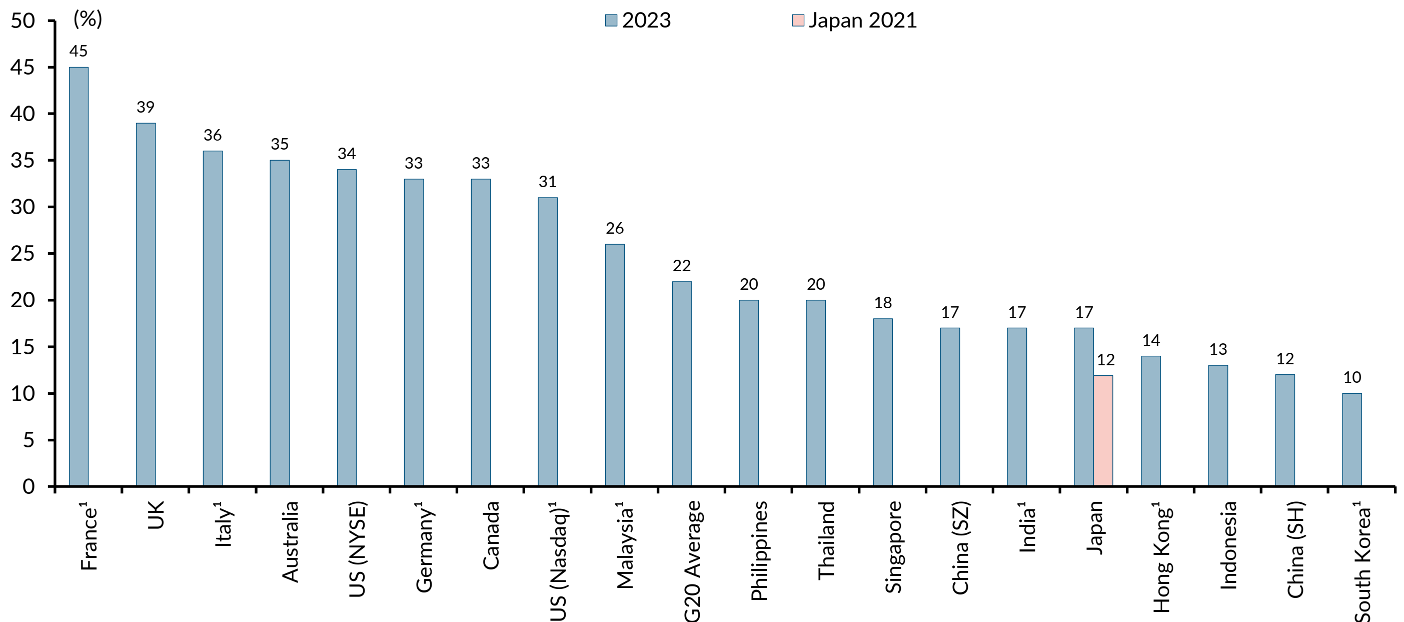
Figure 3

Percentage of women on boards in major markets



[1] Markets with mandatory minimum rules. Note: Average of top 100 issuers by market cap. Source: Sustainable Stock Exchanges Initiative, based on Bloomberg data

Yet, Japan is still far from OECD averages for female participation

Yet, Japan still has a steep climb to get more women into the ranks of senior management. Given that the full-time (“regular”) workforce participation of women peaks at 60% for the 25-29 age group, and drops steadily thereafter, it is not surprising that few reach the C-suite. According to Toyo Keizai, a business publisher, Topix 100 companies in Japan had an average of just under 15% of women in senior executive roles in 2022 compared to just below 30% for the Organisation for Economic Co-operation and Development (OECD) and almost 39% for the G7, excluding Japan, in the same year. On a more positive note, the ratio of listed companies with no female executives fell from 84% in 2013 to around 33% in 2021 (for issuers in the old First Section) and stands at just under 19% for current prime market firms.

Weak judicial logic

We have revised downwards our rating for the judiciary

Given the open access that minority shareholders have to courts to resolve disputes in Japan, and the large number of derivative actions (at least compared to other Asian jurisdictions), we have historically rated the country quite highly for judicial skill and lack of bias in the handling of company and securities law cases. But, a jarring judgement in late 2021 raised eyebrows about the nature of some judicial decision-making and led to lower scores in our survey.

A case in 2021 highlighted weak takeover rules in Japan

The case involved a tussle between Tokyo Kikai Seisakusho (TKS), a small listed company that makes newspaper printing machines, and Asia Development Capital (ADC), an investment fund with ties to allegedly shady “Chinese capital”. Over a three-month period in 2021, ADC bought 40% of TKS on the open market and took the company by surprise - which was itself surprising since ADC published numerous large-shareholding reports between July 2021 and the end of that year. Fearing a takeover, TKS called an EGM and won shareholder approval for a new poison pill in October 2021 to block ADC. It succeeded because it used the controversial “majority of the minority” mechanism that excluded ADC and a few other shareholders on the grounds that they were “interested” parties and should not be allowed to vote. Had ADC been allowed to vote its 40% holding, the poison pill would have failed.

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ADC sought an injunction against the TKS poison pill vote, but failed

ADC sought an injunction in the Tokyo District Court but failed. It then lost appeals in the Tokyo High Court and Supreme Court in late 2021. The judges based their decision on the following "circumstances": that ADC had built up its stake quickly; ADC did not inform the market of its intentions regarding TKS; and it continued buying the company's shares despite a request from TKS that it stop. In the language used in Japan in such situations, which draws on US legal norms, this looked like a "coercive" takeover attempt.

Some experts argue the judgement in favour of TKS had no basis in law

Some legal experts have argued that the court decisions had no clear basis in law. Writing in the *Nikkei Asia* on 9 November 2021, Stephen Givens, a foreign corporate lawyer well-known in Japan for his work on corporate governance, stated:

> "When the Tokyo District Court upheld last month the Tokyo Kikai Seisakusho board's exclusion of a 40% shareholder from voting at a shareholder meeting, it created a precedent that not only lacks any anchoring in law but is also dangerously open-ended.
>
> "One would normally expect at least some reference to case precedent or statute to justify a new rule that gives boards authority to exclude specified shareholders from voting at a shareholders meeting . . .
>
> "But in fact, the only legal authority the court offered was its own free-standing say-so that the board's action was "not unreasonable."

The judgement could have had wider implications for shareholder rights

Givens emphasised that the implications of this judgement could extend beyond the narrow purview of poison pills and potentially be used by companies, for example, to exclude shareholders who seek to call an EGM to remove directors. "Could companies exclude shareholders from voting on things shareholders have to decide if management thinks they will vote the wrong way? This would really turn corporate democracy upside down!", he told ACGA.

The mechanism used by TKS has no firm basis in Japanese law

One of the issues here is that the "majority of the minority" mechanism lacks any firm basis in Japanese law. It was introduced into the TKS case by the firm's legal counsel, who imported the "majority of the minority" term of art from the US and apparently convinced the court that his proposal was accepted law in the US. However, the context in the US is very different: it is not used to exclude so-called interested parties from voting on poison pills, but rather to allow minority shareholders a vote in the event of an unfair squeeze out following a partial takeover offer.

The case raises questions about judicial reasoning in Japan

The deeper issue for our purposes is what this case says about judicial reasoning in Japan. As Givens explains, Japanese courts tend to be "very conservative" in terms of results and produce the outcomes expected by "the establishment". But their methods are in fact "very radical". Judges decide cases based on what seems reasonable to them and rarely cite precedent. And on an appeal, a higher court will not refer to a lower court's judgement and state whether it got the decision right or wrong. It will effectively issue a fresh opinion.

Fortunately, the long-term impact of the case may be limited, as the Cosmo case shows

On a more positive note, the practical impact of this case is likely to be limited. Fast forward 18 months and funds controlled by veteran activist investor, Yoshiaki Murakami, lost a similar vote on a poison pill after being excluded from voting by oil refiner, Cosmo Energy Holdings. Cosmo used the same "majority of the minority" mechanism to exclude Murakami's funds, which owned a combined stake of around 20% at the time (June 2023). The activist indicated he wanted to increase his holding to 25%, so Cosmo called another EGM for mid-December 2023 to try to stop him. In the end, Cosmo acquiesced and allowed Murakami to vote, a likely admission that the company would have lost the vote even after excluding him.

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Investors in Japan are more willing today to vote in their own interests

Givens hailed these developments as a turning of the tide in the fiduciary thinking of domestic institutional shareholders, who "no longer believe they need to be protected from the threat supposedly posed by "abusive acquirers" offering generous premiums to buy their stock", as he wrote in the Nikkei Asia in November 2023. Shareholders today are more "mature, independent and sophisticated", he argued, and will act more in their own self-interest. In the end, the EGM vote became moot when a white knight stepped in to buy out Murakami.

2. Regulators

Japan moves into equal 2nd on improved score of 65%

After rising to 5th place in CG Watch 2020 on a much-improved score of 62%, Japan jumped into equal second with Taiwan on a score of 65%, leapfrogging Hong Kong (whose score dropped significantly) and Singapore (which stayed the same).

Regulatory effort drove the big jump in score

The prime reason for the rise in score and ranking in this category was regulatory effort on CG reform. There was little change in scoring for funding and capacity building, while Japan lost a few points on enforcement.

Regulators have shown a greater sense of urgency

Animating Japan's more energetic approach to policymaking over the past year is a sense that the time has come to do something bolder. With investments flowing away from China and into Japan, officials want to seize the moment and convince both global and local investors that the country's corporate sector can produce "sustainable value" over the longer term. What it needs is a much bigger push. At the same time, a changing of the guard to a younger, more open-minded group of officials also appears to be helping.

Improved corporate value remains the central tenet of CG reform in Japan

These reforms have been framed by the FSA as necessary measures to instil more substance into Japanese corporate governance. It notes that while there have been many changes in form over the past decade, it is not clear that these have always led to improved corporate performance - an issue on which there has also been insufficient research to date. Nevertheless, it believes that enhanced information disclosure and better dialogue between companies and investors will lead to increased corporate value - the Holy Grail of Japanese CG reform.

Capital market changes require more sophisticated policies and regulation

More specifically, the FSA is aware that the ongoing evolution of the capital market requires a regulatory response. Major changes include an increase in M&A activity and hostile acquisitions, the rise of passive institutional investment, and growing concerns around cross-shareholdings and parent/child listings. The agency is also responding to feedback received from investors and other market participants on weaknesses in the tender offer rule (ie, takeover regulation), the large shareholding reporting rule (ie, substantial ownership), joint holder regulations (ie, concert party action), and other matters. Getting these reforms right will be critical for laying the groundwork for the next phase of corporate governance and capital market reform.

2.1 Funding, capacity building, regulatory reform

Japan leapt into 1st place with a much-improved score of 67%

This sub-category saw a substantial increase in score from 58% in 2020 to 67% in 2023, pushing Japan into 1st place and well above Australia and Taiwan at equal 2nd on a score of 61%.

The FSA is taking a new approach to consulting foreign investors

The main factors behind the jump were significantly higher scores for the reform initiatives undertaken by the government, as noted, but also a new approach by the FSA to consulting foreign investors and an improvement in the company report archive on the JPX website.

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Where scores remained the same

Scores remained the same for regulatory funding and investment in new technology. We gave full marks once again for the ICJ electronic voting system run by JPX and Broadridge, but rated Japan poorly on the extent to which it encourages high standards of governance in listing applicants. No market in the region does well on the latter question.

Japan lost points for regulatory websites

There was only one question where Japan lost points in this sub-category: Do regulators have informative websites with English translations of all key laws, rules and regulations easily accessible? While the FSA website provides most of these documents in English, or links to them on other sites, the organisation of information could be clearer and more logical. Finding specific documents, including old or new policy reports and statements, is usually a time-consuming exercise. The search function is sometimes helpful, but does not list its results in chronological order.

JPX listing rules could be more user-friendly

While it is easier to find regulatory documents on the JPX website, making use of them is harder. Whereas documents on the government's Japanese Law Translation database contain an online table of contents, the same does not apply to the TSE listing rules. These come in a locked PDF format, thus necessitating a lot of scrolling back and forth, which is extremely frustrating.

Ramping up CG reform

The TSE's market restructuring initiative set the reform ball rolling

The past 12 to 24 months have certainly been among the most exciting in recent memory for Japan's small army of CG mavens. The ball began rolling in April 2022 with the TSE's restructuring of its old cash equity market divisions (1st Section, 2nd Sections, Mothers) into three new segments (Prime, Standard, Growth). The overarching goal, as in all CG reform efforts in Japan, is to "incentivize sustainable growth and medium- to long-term corporate value creation at listed companies". As the TSE said at the time, the old divisions created ambiguities, poor incentives for sustainable growth, and failed to provide an index with "functionality as an investable index". In contrast, the new Prime Market would comprise companies with better governance, high liquidity, and higher levels of dialogue with global investors. Standard Market firms would have "sufficient" liquidity and governance to be investable. And Growth Market firms would be smaller but with high-growth potential.

The Prime Market started with a surprisingly large number of issuers

There is not space here to delve into all the complexities of this reform, however a couple of broad observations are worth making. One early question was why the TSE allowed so many issuers onto the Prime Market if the aim was to keep this for the better governed firms? The simple answer is that companies were allowed to self-select. This meant that in April 2022 the Prime had 1,839 issuers, less than the 2,177 on the old 1st Section but more than the 1,466 on the Standard Market. Over time, the TSE has tightened the criteria for inclusion, including setting hard deadlines for when companies must meet these targets or move to the Standard, and identified almost 300 companies that do not meet the continued listing criteria for the top board. The restructuring has since moved in the right direction and already the Prime Market has fewer issuers: it was down to 1,655 by the end of February 2024, while the Standard had increased to 1,613.

Reforms are designed to protect retail as well as institutional investors

A second point worth emphasising is that these reforms have been designed to attract and protect not just global investors, but domestic as well. In 2014 the Japanese government launched the "Nippon Individual Savings Accounts" (NISA) scheme, designed to encourage people to move money from low or no interest-

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bearing savings accounts to higher yielding stocks and investment funds. NISA was revamped in early 2024 to encourage much greater investment in the stock market by individuals, including raising limits on investment amounts and making investments tax-free permanently. Clearly, increased retail participation necessitates more transparency from listed companies and stronger shareholder protection.

Market restructuring was the catalyst for the TSE's bolder reforms

More fundamentally, the market restructuring created the enabling environment for a range of bolder and more direct CG reforms. Indeed, the TSE gave a hint of what was coming in January 2023 when it published a summary of the discussions in its Council of Experts on the follow-up to the market restructuring. It cited four main areas: a focus on cost of capital and profitability; stronger internalisation by companies of the CG Code and the meaning of "comply or explain"; increased use of English-language disclosure; and more effective dialogue with institutional investors. As it said quite bluntly at the time: "Considering the purpose of this market restructuring is to contribute to the improvement of corporate value of listed companies, it will be meaningless unless we address the fact that about half of all listed companies have a PBR (price to book ratio) below 1."

First broadside on cost of capital

The TSE launched a campaign to improve capital management and profitability in early 2023

If anyone doubted the TSE meant business, they were in for a shock in March 2023 when the exchange announced it was henceforth "requesting" companies on both the Prime and Standard Markets to promptly "implement management that is conscious of cost of capital and stock price". Not only did around half of Prime issuers and 60% of Standard have a PBR of less than 1, but they had a return on equity (ROE) below 8% - which has been a minimum expected profitability standard in Japan for the best part of 20 years.

Issuers were told to develop a plan without delay

The TSE asked each firm to analyse its cost of capital and profitability, develop a detailed response with targets, timelines and specific actions, and disclose all of this to the market. While it did not set a deadline for disclosure, the exchange asked issuers to implement these actions without delay and keep shareholders updated through "proactive dialogue". Importantly, boards of directors should be involved every step of the way. The sense of urgency on the part of TSE was palpable: "This is our last chance," an exchange official told ACGA in mid-2023.

The target of PBR 1 should be a floor, not a ceiling

The exchange is certainly alive to the unintended consequences of its reform measures. Some issuers for example see the PBR 1 guidance as a ceiling not a floor, an issue noted in the Nikkei newspaper in April 2023 when the CEO of JPX, Hiromi Yamaji, urged companies not to stop when they reached a PBR of 1x, but to seek higher valuations. Nor did the exchange want companies to merely implement short-term measures, such as one-off share buybacks or higher dividends. The aim should be to consider capital management and profitability over a longer-term perspective.

Second broadside on cost of capital

The TSE began naming companies which complied in January 2023

If all this wasn't exciting enough, the TSE announced in late October 2023 that it was not entirely satisfied with responses so far and would soon publish a list of companies complying with, or considering, its request - and that it would provide examples of good disclosure and the views of investors. The first list comprising 815 Prime and 300 Standard companies duly came out on 15 January 2024, while separate reports on company cases and investors perspectives were released in early February.

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Whether boards have the expertise to manage capital well is open to debate

Will the TSE guidance work?

Investors, other market participants and the media have generally responded positively to the TSE's efforts on cost of capital, seeing it as a timely and necessary measure to address one of the biggest drags on the market. Yet some long-term observers remain concerned that many companies lack the expertise to implement effective action plans. Nicholas Benes, Representative Director, Board Director Training Institute of Japan (BDTI), questions whether the average board has the financial literacy to fully understand cost of capital:

Training is urgently needed to address gaps in the financial expertise of directors

> "While we applaud JPX/TSE's policy drive over the last 10 months, we really wonder whether it will bring about real change at many companies. TSE is asking boards to be involved - to lead the process - and drive a PDCA improvement cycle. But there is conspicuously no mention anywhere of the need for more training about cost of capital, finance, and so on. It is one thing to say you should use WACC and ROIC management, but another to meaningfully integrate those techniques and concepts into management at each division and by the CFO. The level of knowledge of those topics - let alone reading financial statements - is quite low among many directors."

Financial regulators share these concerns

Similar concerns were expressed by a financial regulator. He highlighted a range of obstacles, from companies lacking the necessary financial expertise to independent directors unable to challenge management, and weak engagement from largely passive institutional investors. He believes a "multi-layered approach" from different stakeholders is needed.

The Action Program covers three main areas: management, independent directors, and investor dialogue/shareholder rights

FSA Action Program

Coming soon after the TSE's guidance on cost of capital - and overlapping with it to a degree - was a policy statement from the FSA in April 2023 titled, "Action Program for Accelerating Corporate Governance Reform: From Form to Substance". One of the more ambitious CG policy documents of recent years, the statement emanated from the agency's Council of Experts on the follow-up to the CG and Stewardship Codes. To recap, the Action Program covered three main areas:

1. Management issues: Encouraging greater awareness of cost of capital, profit making, sustainability, and human capital.
2. The effectiveness of independent directors: Performance of the board, nomination and remuneration committees, and director quality.
3. Company-investor dialogue: Enhancing disclosure and addressing legal and market environment issues (ie, shareholder rights).

It also touches on the duplication of reporting, subsidiary listings, and cross-shareholdings

Other specific issues included in the Program and of importance to investors include:

- ❑ Addressing the duplication of information provided in the Business Report (required under company law and published before the AGM) and the "Yuho" or annual securities report (required under securities law and typically published after the AGM). Ideally, there would be one report published prior to the AGM.
- ❑ Parent/child listings - disclosure and governance issues in "quasi-controlled listed companies".
- ❑ Reducing cross-shareholdings.

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The Business Report/Yuho issue is a long-term challenge and requires the involvement of numerous stakeholders, probably including the Ministry of Justice, and is unlikely to be resolved any time soon. The parent/child issue will be studied further by a TSE study group. And the issue of cross-shareholdings is something the FSA has the power to make policy on and is a current focus of attention (*see box titled "Swearing allegiance no more?" under Listed Companies).*

The FSA started with some of the most difficult legal obstacles affecting investors

But first, and wisely in our view, the FSA directed its energies towards a series of thorny legal and market environment issues. In March 2023 it formed a working group under its Financial System Council to deliberate on the tender offer and large shareholding reporting rules. It held six meetings between June and December 2023, when it published a report on its conclusions (*see box below*). While the main focus was on takeover rules and substantial ownership disclosure, including problems with "joint holder" (concert party) regulation, the group also discussed the issue of beneficial ownership and how this could be made more transparent (since holdings of 5% and below do not need to be disclosed). The ball is now back in the FSA's court. It completed a draft amendment to the Financial Instruments and Exchange Act (FIEA) and presented this to Parliament in mid-March 2024.

A new dawn for shareholder rights?

Japan's takeover and substantial disclosure rules urgently need updating

It is well recognised that Japan's "tender offer" (takeover) rules are limited and do not provide adequate protection for minority shareholders. Introduced in 1971, they were last significantly amended in 2006, as was the "large shareholding reporting" rule promulgated in 1990. Yet an increase in friendly and hostile M&A - and an official desire to increase business restructuring to enhance corporate value - is necessitating a rethink.

Takeover rules do not cover on-market purchases, among many other issues

The principal problems with the tender offer rule are as follows:

- On-market purchases are not subject to the rules because they are considered sufficiently fair and transparent already. Yet this allowed ADC to purchase its 40% stake in TKS without ever having to make a tender offer - something that could not happen in most developed markets.
- There is no mandatory general-offer rule such as the 30% threshold in France, Germany, or the UK (after which an acquirer must bid for 100% of the shares in the company). Instead, acquirers wanting to raise their stakes above 5% or 33% must do so through tender offers if they are making purchases through off-market trades or market trades that are off-floor (ie, trading large lots or baskets of securities through the Tokyo Stock Exchange Trading Network System or "ToSTNeT" for short). Such offers can be partial. The one-third threshold was selected because this is the level at which a shareholder can block a special resolution in a company meeting.
- Partial tender offers are also permitted between 33% and 66%, after which they are not permitted. In this sense, Japan follows the US system which also allows partial takeovers and has no general-offer rule. Opponents of the European/Anglo-Saxon general-offer rule argue that it could be bad for shareholders as it might inhibit offers to begin with. "Why should I have to buy the whole cake?", as one commentator told ACGA. The counter argument is that partial offers allow for a change of control with a limited investment and are inherently unfair to shareholders as they do not receive the control premium for all their shares. The acquirer effectively gets to control the whole cake while only buying a slice. In practical terms it is also the way in which partial offers have been used with third-party allotments that has brought harm to minority shareholders in Japan, as the following bullet explains.

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- Third-party allotments (private placements) are not subject to tender offer rules. Hence, acquirers can arrange a partial takeover at a fair price and then increase their stakes through being allotted new shares at a much lower price. This has been used to detrimental effect in Japan in the past, notably in the 2018 takeover of Nihon Nohyaku, a producer of agricultural chemicals, by Adeka, a specialty chemicals group and its largest shareholder with a 24% stake. Adeka increased this to 51% by offering to buy an additional 18% at a significant premium to the market price and then purchasing newly issued shares at the original market price to acquire the remaining 9%. This transaction caused considerable controversy.

Substantial disclosure and concert party rules have a range of unintended consequences for CG

The large shareholding/joint holder rules have also proved counterproductive over the past decade. While the original purpose may have been laudable - to inform the market about the intentions of substantial shareholders, including large investors working together to try to influence companies - these rules have had unintended consequences that are a negative for investor stewardship and corporate governance.

There is confusion in the market regarding the exact meaning of certain rules

Most notably, they have dampened collective engagement because investors are either confused, fearful or just reluctant to venture into a regulatory grey area. For example, although the joint holder (concert party) rules only apply to groups of investors who own more than 5% and intend to jointly exercise shareholder rights, such as entering into a voting agreement for an AGM or EGM, many investors think it applies to any group owning a combined stake of more than 5%. Similarly, with the linked regulation called the "Act of Making Important Suggestions" (Article 14-8-2 of the FIEA Order of Enforcement), there is a fear this will apply to any collective investor grouping, not just those with more than 5%. The Act is quite onerous and limits what investors can say to companies on topics such as dividends, asset restructuring, and business strategy without disclosing the same to the market. Consequently, some large asset managers have shied away from joining collaborative dialogues with companies, while smaller ones have often felt they need to tiptoe around difficult discussions with management.

An FSA working group recommended several improvements in late 2023

The FSA's working group took account of diverse market feedback during 2023 and erred on the side of caution by not endorsing an immediate shift to a European-style system of mandatory general offers (although it did raise this as a possibility for the future). Instead, it focussed on several discrete issues and made several recommendations, including among other things:

On-market trades should be covered by takeover rules

1. **Market trades:** The working group concluded that contrary to theory, these may not always provide sufficient information and fairness to the market, especially if voting rights are acquired quickly and there is a material risk of a change in corporate control. It therefore recommended that on-market trades should be subject to the 33% rule.

Partial tender offers need to be discussed further

2. **Partial tender offers:** The possibility of banning of partial offers was discussed in some depth by the working group, which noted that these were often seen as unfair to general shareholders. This could be because they may be "coercive", defined as a transaction where despite a dissatisfaction with the offer price, general shareholders reluctantly sell because they fear the company's value will fall under the new owner. Or there could be inbuilt conflicts of interest between controlling and general shareholders. Or shareholders may simply not be able to sell all the shares they tender. Conversely, some market participants argued that disallowing partial tender offers might hinder "desirable M&A deals". The working group did not take a position, but said partial tender offers should

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continue to be discussed. Meanwhile, acquirers and target companies supporting a deal should make more effort to win the understanding of the target company's shareholders for such partial offers.

The one-third threshold will be dropped to 30%

3. **One-third threshold:** This will be reduced to 30% in light of rules in other countries and the actual levels of voting rights exercised in Japan (ie, since not all shares are voted in shareholder meetings, owning a stake of 30% is usually sufficient to block a special resolution and to "have a significant effect on an ordinary resolution").

Rules on 'important suggestions' need to be relaxed somewhat

4. **Large shareholding reporting rule/act of making important suggestions**: The working group favours a relaxation of disclosure rules for "material proposals" not directly related to corporate control and which management can adopt or refuse (eg, changes in dividends or capital policies). Whereas proposals directly related to corporate control and which management does not have the power to adopt or refuse (eg, nomination of directors) should still be subject to existing disclosure rules.

Concert party rules also need to be relaxed

5. **Joint holder rules:** The working group recognises that existing rules have been having a "chilling effect" on collaborative engagement and clearly favours a relaxation of the current framework. It states that it is "appropriate to exclude" as joint holders any institutional investors whose aim is not to make joint material proposals nor engage in an ongoing voting agreement.

Though not completely a new dawn, the recommendations are positive for CG in Japan

The working group concluded by asking the relevant authorities (ie, the FSA) to "swiftly consider a draft amendment to the Financial Instruments and Exchange Act based on the content of this report". While its recommendations do not address all the issues raised by ACGA over the years, they are an important step in the right direction. The FSA duly finalised a high-level draft bill and sent it to Parliament in mid-March 2024. It is expected to be approved by June, after which work will begin on the detailed rules. These should be ready by March 2025.

METI wants fairer corporate takeovers

METI is seeking to set new market norms for fair takeovers

While the tender offer rules in the FIEA outline the regulatory framework for takeovers in Japan, a new set of guidelines from the Ministry of Economy, Trade and Industry (METI) aim to set best practice on how companies should manage takeovers in a fair and transparent manner. METI issued these for public consultation in early June 2023 and then published a final version on 6 August 2023. They are the latest in a long line of guidance documents on takeover-related matters since 2005, when METI and the Ministry of Justice (MOJ) first provided guidelines on takeover defenses, followed by management buyouts (MBOs) in 2007. More recently, METI issued guidelines on Fair M&A in 2019 that covered MBOs as well as takeovers of controlled companies by controlling shareholders (ie, cases where there is a conflict of interest).

The new guidelines are broader than previous policy documents and cover M&A between independent companies

The new guidelines are intended to cover "ordinary" acquisitions undertaken at arm's length between unrelated companies. METI hopes they will help to facilitate more M&A as an avenue for enhancing corporate value and limit the ability of boards to simply dismiss tender offers out of hand. Figures show that while the number of transactions was holding steady in the first half of calendar 2023 - up 3% to 1,828 cases - in terms of value they jumped 80% YOY, reaching US$47 billion. This is a notable increase even when one considers that one third was accounted for by the JIP buyout of Toshiba.

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Three core principles

The METI guidelines follow three core principles:

1. The need for companies to be conscious of long-term corporate value and shareholders' common interests;
2. A respect for shareholders' intent; and
3. A requirement for transparency.

The word "fairness" appears frequently, while the Guidelines recognise that partial acquisitions could be unfair to shareholders. Pricing should be on "best available transaction terms". And a great deal of onus is put on independent directors to ensure that transactions follow these principles.

Lingering grey areas

There are of course several grey areas. How should management communicate a new tender offer to the board? When should a board form a special committee to review a new offer? Under what circumstances should a company hold a "majority of the minority" (MoM) vote? Conscious of the controversy over MoM, METI argues that it should only be used in exceptional circumstances and hopes that clearer answers will emerge as the guidelines are used by the market.

The Guidelines appear to be having a positive impact

So far METI seems happy with the reception that the Guidelines have received. It notes they have been influential in several tender offers over the past year, including the landmark Nidec takeover of machine tool maker Takisawa in late 2023. Both companies reportedly followed the Guidelines and turned what could have been a hostile takeover into a friendly one. As the Nikkei Asia said on 13 September 2023, "Nidec proposed the buyout in July, without obtaining prior consent from Takisawa's management. That management, which had not previously commented publicly on the proposal, decided to accept the move on Wednesday, averting a hostile takeover."

Two entrenched weaknesses in the system underscore the need for the guidelines

What gives added urgency to the Guidelines are two entrenched weaknesses of the Japanese M&A system: directors do not have a fiduciary duty to accept the highest price in a tender offer bid; and courts have not been active in handing down judgements that help to set market norms due to a limited number of cases that reach them. Nor is there a Takeovers Panel in Japan that opines on issues of fairness and resolves disputes, unlike in the UK, Australia or Hong Kong.

The Japan Corporate Governance Forum

Regulators have created a new forum to communicate with foreign investors

A new feature of the CG regulatory landscape in Japan - and one which has arguably lent some weight to the renewed reform momentum - is a new consultation platform created by the FSA in September 2022 to engage with foreign investors and governance entities. Called the Japan Corporate Governance Forum, it encompasses a regular dialogue between the FSA and three foreign non-profit entities with a long-term stake in Japan: ACGA; the International Corporate Governance Network (ICGN), based in the UK; and the Council of Institutional Investors (CII), based in the US. Each organisation has met three times with the FSA since the launch of the Forum, either through online discussions or in-person meetings.

The forum allows for a more open, regular, and broader discussion

The primary benefit of the Forum is that it allows for a more wide-ranging, detailed and informal discussion of specific topics, such as the Action Program. While written submissions to regulatory consultations will remain an important avenue for expressing views on CG reform in Japan, the open style of the Forum has certainly allowed for a richer dialogue. In the case of the tender offer or large shareholding/joint holder rules, such communication is also essential if the FSA is to

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receive any input from the market. This is because any changes would take the form of amendments to primary legislation and, as such, must be debated and passed in Parliament. Under the Japanese system there does not need to be a preceding public consultation for legislative amendments. There does for changes to secondary legislation and Cabinet Orders, since these are not scrutinised by Parliament.

Regulatory funding and capacity

FSA spends about the same each year as ASIC in Australia

In CG Watch 2020 we did a deep dive into the funding behind the FSA and found that total expenditure for the agency's staff based in Tokyo and those working on securities supervision in the 11 Local Finance Bureaus around the country amounted to approximately ¥46 billion (US$420m at the time). While comparisons with other markets are fraught with complexities, we noted that this was more than the US$252m spent by the Hong Kong Securities and Futures Commission, which has a narrower remit, and about the same as the US$430m spent by the Australian Securities and Investments Commission, which has a broad remit thought somewhat different to the FSA's.

FSA budget requests declined slightly during Covid, then rose again

Budgetary figures available for the past four fiscal years for the FSA alone, from 2021 to 2024, show a moderate decline in funds sought followed by an uptick - from ¥25.8 billion in FY2021, falling to ¥22.6 billion in FY2022 and ¥23.2 billion in FY2023, then rising to ¥25.3 billion in FY2024. While personnel costs in the past have typically accounted for around 70% of the total budget, they increased to 81% in FY2023 and dropped back to 76% in FY2024. Property expenses accounted for the remainder. Note that actual expenditure can be less than requested amounts and the above numbers do not include the Local Finance Bureau. Overall, they show a stable funding environment.

FSA budgetary documents highlight its wider remit

While most of the FSA's expenditure goes on financial supervisory and related work, its budgetary documents like to highlight its broader remit. In its latest "Budget, Organisation, Capacity Request" it talks, for example, about funds requested to "support the stability of the economy and people's lives, leading to subsequent growth" through such things as:

- Promoting support for businesses in responses to changing socioeconomic conditions.
- Strengthening cyber security and economic security measures.
- Strengthening anti-money laundering measures.

JPX funding has also remained stable

The funding situation at JPX has also been quite stable. While the exchange does not provide figures for its spending on policy, regulatory and enforcement work, it says that there has been no significant change in its budget or personnel over the past three years. The staffing picture is similar to late 2020, when JPX Regulation had around 200 people out of the 1,000+ working for JPX and there were an additional 150 or so people working in the TSE and Osaka Exchange monitoring the market on a real-time basis and assisting with listed company disclosure.

2.2 Enforcement

Japan dropped to 7th place on a slightly lower score of 63%

After a strong performance in our last survey, when Japan enjoyed a nine-percentage point increase and rose from 8th to 5th place, this time it has slid three percentage points to 63% and slipped back to 7th place. This is not a reflection of any regression in enforcement outcomes, rather the fact that other markets are moving ahead faster, such as Australia, and so Japan's score fell slightly. We also rated Japan lower for the disclosure of its securities enforcement work.

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Enforcement outcomes - SESC

Moved under the FSA in 2001, the SESC gained powers over insider trading in 2014

The enforcement arm of the FSA, the Securities and Exchange Surveillance Commission (SESC), was originally established by the Ministry of Finance in July 1992. Nine years later, in January 2001, it moved to the FSA. The SESC gained additional powers in mid-2005 when it was allowed to impose "administrative monetary penalty payment orders", a basic tool in its enforcement kit. Among many other developments since, the Commission created a cross-border investigation office in 2011 and began administering insider trading regulations when they were introduced in 2014.

The SESC focusses primarily on market misconduct

Market surveillance forms the basis for the SESC's analysis of potential market misconduct and each year it examines suspicious transactions that could involve insider trading, market manipulation or fraud. It monitors "financial instrument business operators" (ie, intermediaries) and applies a risk-based approach to selecting those for inspection. It undertakes detailed investigations into the more serious cases of misconduct and, where appropriate, makes recommendations for administrative monetary penalties. It seeks to prevent future violations by sharing information with self-regulatory organisations (ie, industry bodies that can play an educational role vis-à-vis their members) and publishes a casebook with examples of typical malfeasance. The Commission also reviews corporate disclosure documents for evidence of reporting breaches and may recommend monetary penalties or voluntary improvements, as necessary. Finally, it undertakes investigations of possible criminal cases and files criminal charges with the public prosecutors' office.

Enforcement outcomes remain consistent each year

Each year the SESC publishes a detailed annual report covering its activities for the fiscal year (April to March). One noticeable feature is the consistency of enforcement outcomes, a phenomenon we have written about before in CG Watch. The total number of potential market misconduct cases hovers around 1,000 to 1,100 each year, with the past three years being no different. Typically, around 90% of these are for suspected insider trading, with most of the rest falling into the market manipulation category.

Most cases of misconduct relate to insider trading

Figure 4

Suspected market misconduct cases examined in Japan, 2018-2022

Fiscal year	2018	2019	2020	2021	2022
Insider Trading	977	976	900	922	1,024
Market Manipulation	70	78	60	43	29
Other cases	5	7	5	4	12
Total	**1,052**	**1,061**	**965**	**969**	**1,065**

Note: The years relate to fiscal years. Hence, "2022" is the year from April 2022 to March 2023.
Source: Securities and Exchange Surveillance Commission, Annual Report 2022-23

The SESC does not set a specific target for case numbers per year

The Commission says there is no particular reason why the number of cases examined remains so stable from one year to the next. It is rather an "organic outcome" of its approach. It does not set a specific target for each year and some cases are more complicated to examine and investigate than others. Moreover, there have been no major policy changes around enforcement for the past five to six years. It is also worth noting that most of the examinations, typically around 60%, are carried out by the Local Finance Bureaus.

Case numbers declined during Covid

In terms of aggregate enforcement outcomes, the latest figures from the SESC Annual Report FY2022 (ie, the fiscal year to 31 March 2023) show a predictable decline during the worst years of Covid, followed by a rebound in FY2022 (see

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Figure 5 below). In terms of types of cases, these have also remained largely the same: most relate to fines for market misconduct, with fewer fines for disclosure violations and recommendations for administrative action against securities businesses. Only a small number relate to criminal charges, most of which are for insider trading.

Administrative fines far outweigh criminal charges

Figure 5

Recommendations for fines and administrative actions, and filing of criminal charges, 2018-2022

Fiscal year	2018	2019	2020	2021	2022
Recommendations for fines	**43**	**35**	**24**	**17**	**21**
Market misconduct	33	29	14	12	14
Violation of disclosure regulations	10	6	10	5	7
Recommendations for admin action	**11**	**14**	**5**	**2**	**5**
Filings of criminal charges	**8**	**3**	**2**	**8**	**8**
Total	**62**	**52**	**31**	**27**	**34**

Source: Securities and Exchange Surveillance Commission, Annual Report, 2022-23

Case numbers appear low

We continue to find these numbers quite low for a market with more than 3,800 listed companies across the three main market segments (prime, standard, growth), 8,200 financial instrument business operators (FIBOs), and more than 11m Nippon Individual Savings Accounts (NISA) as of September 2023. Admittedly, we would not expect to see a lot of transgressions among individual investors, but it does happen.

Criminal prosecutions are considerably higher in some other markets

The Commission has traditionally argued that it works hard on prevention of malfeasance, both with Japan Exchange Group (JPX) and market intermediaries, and does not necessarily agree that the numbers are low. While its prevention work is to be commended, it is worth noting that the total number of recommendations and charges each year accounts for only 3%-6% of all cases examined. In contrast, the Australian Securities and Investments Commission (ASIC), working in a market with fewer listed companies (less than 3,000), undertakes enforcement action that results in a much larger number of cases and convictions. For the 2022-23 financial year alone (ending June 2023), prosecutorial authorities completed 44 criminal litigations and commenced 32 new cases. The courts criminally convicted 35 people or companies, handed down 21 custodial sentences (some of which were suspended), and issued 14 fines or non-custodial sentences. The numbers are even larger for civil litigation and administrative actions launched by ASIC.

Regulators make limited use of civil sanctions in Japan

Another feature of Japanese securities enforcement that is different from other markets in this region is the limited use of civil sanctions by the regulator. In a recent case, the SESC petitioned the Tokyo District Court for prohibition orders and stay orders in June 2022 against an unregistered market operator that was soliciting investments in various financial instruments and conducted a public offering of its corporate bonds without statutory notification. One of the things that made this interesting is just how few these cases are: there have only been one or two a year for most of the past eight years, according to the SESC website. In contrast, ASIC in 2022-23 issued 21 interim and final stop orders for misleading or deceptive disclosure in offer documents, and a further 78 interim stop orders under new powers regulating investment product design and distribution. This was on top of 57 instances of potentially misleading promotional material being withdrawn or amended.

Most SESC disclosure focusses on the front end of the enforcement chain

It is also worth highlighting that the focus of SESC disclosure in its English annual report and website is on the front end of the enforcement chain in Japan. That is, it discloses its recommendations for monetary penalties and the details of criminal

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charges filed but does not 'close the loop' by reporting on the outcomes of all these cases. It explains that almost 100% of its administrative recommendations are supported by the FSA and implemented, with 90% being accepted by the individuals or entities penalised; while criminal filings are almost all accepted by the public prosecutors' office. While the SESC occasionally loses in court, which is rare: in more than 90% of cases, the courts accept the prosecution's arguments.

The SESC does disclose the outcomes of court cases, but not in the timeliest or complete way

The SESC does, up to a point, disclose the outcomes of court judgements for criminal cases on both its Japanese website and annual report (with more detail in a supplementary data book) - although not in the most timely or complete manner. The information on the website is a little hard to find: one must first go to the criminal investigations page and find a link to a PDF file called "summary list of accused cases" (which is situated under a table of statistics); then trawl through cases spanning more than 20 years to find summary information about the court judgements for each case. The SESC does not issue timely press releases in either English or Japanese clearly stating the latest court rulings on criminal cases. The commission acknowledges this situation, but notes that it is "partly because the development of such cases for the criminal justice is beyond our control once they are before the courts". While this is certainly true, we felt we had no choice but to reduce the score somewhat for Question 2.16 on the transparency and accessibility of enforcement data since such press releases are common in other developed markets.

How regulators in some other markets provide more complete disclosure

Closing the loop

How do securities regulators in other markets in our coverage disclose the results of enforcement cases? The short answer is in a lot more detail than is available in Japan. Both ASIC in Australia and the Securities and Futures Commission (SFC) in Hong Kong communicate the conclusions of cases that go to court, or in Hong Kong's case the Market Misconduct Tribunal (MMT), in a timely manner. ASIC puts out regular press releases, while SFC announcements on MMT actions contain links at the bottom to all relevant earlier press releases on a case. ASIC also summarises major enforcement outcomes in a quarterly report, which provides links to all key press releases.

JPX enforcement numbers have remained stable too

Enforcement outcomes - JPX Regulation

Once again, we do not see a great deal of change in most enforcement outcomes at JPX either. Our analysis in CG Watch 2020 showed only a few cases each year where issuers were put "on alert" for serious breaches of the rules, given a "listing agreement violation penalty" (ie, monetary fine), or required to make fundamental changes to their internal controls and management systems. An equally small number were the recipient of a "public announcement measure" for breaches of such things as disclosure regulations (eg, late reporting, false accounts) or changing the way they used funds from capital raisings. Such issuers are typically required to publish an improvement report by a certain date and are then subject to an inspection period for five years. As Figure 6 shows, JPX enforcement in all these areas remains in the single digits.

Companies under supervision or to be delisted have increased in number

In contrast, a much larger group of listed companies are put "under supervision", with the possibility of facing delisting. As Figure 6 also shows, these numbers have steadily risen over the past few years.

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Figure 6

JPX enforcement action, 2020-2024

	2019	2020	2021	2022	2023
Designation of Securities on Special Alert[1]	3	3	2	4	5
Listing Agreement Violation Penalty	3	4	2	4	5
Public Announcement Measures	9	7	6	3	5
Improvement Reports[2]	7	7	6	4	3
Stocks either under supervision or to be delisted[3]	70	93	90	106	122

[1] Called "Securities on Alert" prior to January 2024;
[2] JPX often requests a follow-up report called an "improvement status report";
[3] Figures refer to number of JPX announcements, not issuers (some of which appear more than once in a year).
Source: JPX website, ACGA analysis. Calendar years. Figures refer to number of issuers disciplined.

JPX has a wide range of enforcement powers, but also sees itself as an educator

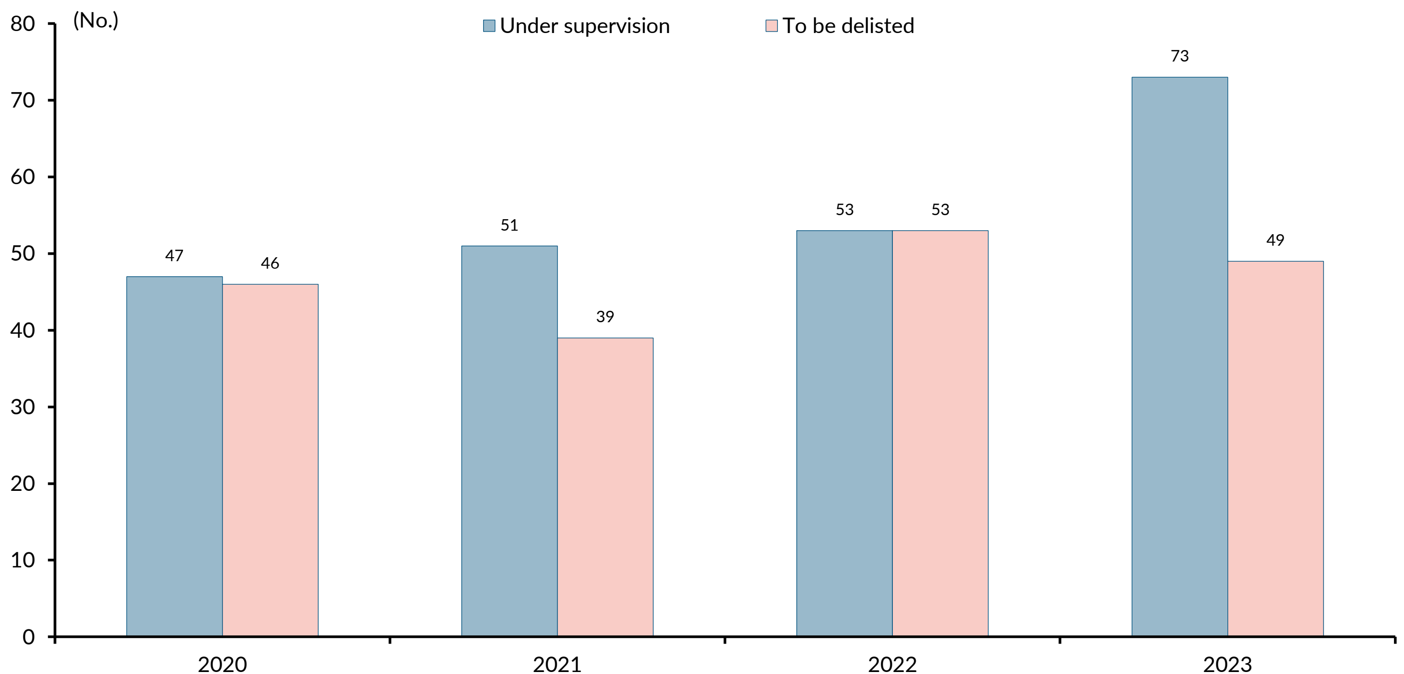
JPX has similarly defended its enforcement caseload in the past by saying that its goal is to be less of a policeman seeking to catch out and punish companies, but rather to encourage improved disclosure and corporate practices. Nevertheless, JPX has a wider range of sanctioning powers than most other exchanges and needs to be seen to be using them. Given that other developed market exchanges in Asia are more active enforcers, in particular Hong Kong, we have reduced JPX's score on Question 2.18 for enforcement track record. Over the past three calendar years (2021 to 2023), Hong Kong Exchanges and Clearing has commenced an average of 28 disciplinary actions per year and concluded 32 - and it does not have as extensive a regulatory toolkit as JPX.

Delistings are relatively high in Japan

One area where Japan is well ahead of Hong Kong and most other markets is in delistings. As Figure 7 shows, there is a healthy volume of delistings each year. Some are undertaken voluntarily, some at the behest of regulators.

Figure 7

Stocks either under supervision or to be delisted by JPX, 2020-23



Source: JPX website, ACGA analysis

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The "securities on alert" designation continues to evolve

Upgrading the "Securities on Alert" designation

One notable reform that the TSE introduced in late October 2023 was a set of amendments to the rules governing how issuers designated as "Securities on Alert" should improve their internal controls and management systems. These rules were first introduced in 2007 and famously applied to Olympus in 2011 after it committed serious accounting fraud (*see CG Watch 2012).* At the time, there were calls for the company to be automatically delisted given the excessive nature of its regulatory breaches. ACGA and others argued for it to be put on alert and rehabilitated. This is what happened and the company was able to stage a recovery, with its share price rising from a low of ¥156 in November 2011 to a high of more than ¥3,000 in late October 2022 (before settling around ¥2,200 in early February 2024).

The last amendment in 2013 pushed for faster improvements

The rules were successfully tweaked by the TSE in 2013 to encourage companies to make improvements more quickly. It is now seeking to introduce a range of higher standards with a view to ensuring companies implement improvements as effectively as possible. Key revisions include:

The current amendments focus on more effective improvements

- Making "de-designation" requirements clearer, including aligning the examination of a company's internal management system with the initial listing examination for its relevant market segment (ie, prime, standard, growth).
- A stricter timeframe for improving internal systems, now set at one year from designation. In the past TSE would allow a six-month extension if a company was making improvements but had yet to complete them. From now on, companies that have "not adequately developed" their internal systems by the one-year mark will be delisted.
- Establishing a new follow-up period: For companies that have not ensured their business continuity and profitability, the TSE will extend the "Securities on Alert" designation for up to three fiscal years.
- Changing the term "Securities on Alert" to "Securities on Special Alert", the aim being to "make it easier for investors to understand".
- Streamlining the segment transfer process from prime or growth to standard.

The revised rules took effect from January 2024.

3. CG rules

Japan improves one rank to 8th on a much-improved score of 67%

Following a significant improvement in score, though not ranking, in our last survey, Japan achieved another jump this time: from 58% to 67%. It is notable though that its ranking has only moved up one place to 8th, a reflection of the tough competition in this space and the fact that Japan is still playing catch-up on CG rules. Other markets typically score in the low to high-70% range, with Australia leading the pack at 83%. They have all been regularly and often systematically amending their CG rules for the past 20 years, whereas Japan has taken a more piecemeal approach.

Where scores increased

Areas where scores increased due to recent reforms included two questions on reporting and disclosure relating to CG and sustainability. We raised the score for revisions to the CG Code in 2021 - something we wrote about in our last CG Watch but did not score as it was published too late. An enhanced focus on the role of audit in the new CG Code led to an uptick in our score for audit committees, as did firmer guidance on nomination committees for our related question. The new METI guidelines on corporate takeovers resulted in a small improvement in the score for

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investor protection in the event of a takeover - a more substantial increase in score would require major amendments to tender offer rules, something the FSA should soon be addressing.

Where we re-rated scores

Our overall category score also strengthened due to a re-rating of some questions. Most notably, we decided to give full marks for the ability of minority shareholders to nominate directors. While the system may be somewhat complex and cumbersome, especially for institutional investors, it is possible to do so and plenty of shareholders try. We also increased the score for disclosure of director remuneration to bring our rating more in line with other markets, but would note that the current system still leaves a lot to be desired (as highlighted in the next category on listed companies). Similarly, we adjusted scores upwards (though only slightly) for financial reporting standards, the definition of independent directors, voting by poll, insider trading regulation, and the prompt disclosure of price-sensitive information. The other area we reconsidered was black-out rules governing director trading before results announcements: while there are no formal rules in Japan, the market norm is for most companies to have them and we are not aware of many directors transgressing.

Adding half-point scores allowed for more nuance

One methodological change that allowed for a more nuanced view on these issues was the introduction of a half-point scoring option. In previous CG Watches we only permitted full-point adjustments.

No scores fell

There were no areas in Japanese CG Rules where scores declined.

CG and non-financial reporting

The CG Code 2021 revision enhanced reporting in several areas

While CG reporting in Japan remains well below international standards in many areas, the regulator deserves credit for bringing in a range of improvements over the past three years. Some have been the result of the revised CG Code of June 2021 and emanate from the FSA's Council of Experts on the stewardship and CG codes. These touch on issues such as:

- **Diversity:** Companies should present policies and measurable goals for ensuring diversity across the organisation and promoting more women and foreign nationals, as well as hiring mid-career professionals for middle management positions.
- **English language disclosure:** Especially relevant for prime market issuers.
- **Nomination and remuneration committees**: Companies that do not have a "three committee system" are encouraged to form advisory nomination and remuneration committees and disclose not only their purpose and role, but policies to ensure the independence of such committees.
- **Director skills**: Companies should consider the composition of their boards in light of their business needs and strategy, and publish a "skills matrix". This should link to their diversity policy and the director nomination process.

Non-financial disclosure in the Yuho was upgraded from FY2022

A year later, in June 2022, a working group on corporate disclosure under the FSA's Financial System Council produced a set of recommendations for enhancing reporting on sustainability, human capital, gender diversity, and board governance in the statutory annual securities report ("Yuho"). On CG, this envisaged adding a new section to the Yuho on the functioning of the board and the activities of the nomination and remuneration committees. These proposals were turned into an

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amendment to the Cabinet Office Order on Disclosure of Corporate Affairs that was promulgated and came into effect on 31 January 2023. The changes applied to fiscal years ending on or after 31 March 2023, meaning that the first expanded Yuho reports would be required before the end of June 2023.

Companies must now say more about board activities and internal audit

More specifically, the new CG requirements covered two items:

1. Board and committee activities, including frequency of meetings, details of director discussions, and attendance statistics for directors and committee members.
2. How the company is working to ensure the effectiveness of internal audits.

While these amendments are very much welcomed, ACGA's analysis of listed company disclosure for FY2023 suggests there is some way to go before most issuers internalise the spirit of the new rules. *(See next section on listed companies.)*

Sustainability reporting

New sustainability reporting is also required in the Yuho

Strides have also been made in sustainability reporting. As noted, the Financial System Council working group in June 2022 and the amended Cabinet Office Order from January 2023 outlined the need for a new section in the Yuho on sustainability. The element that caught most people's attention was a requirement for reporting based on the four pillars of the Task Force on Climate-related Financial Disclosures (TCFD). This was only partial TCFD reporting, however. Issuers must outline how they were addressing “governance” and “risk management” processes for managing sustainability-related risks and opportunities, but only needed to report on “strategy” and “indicators and targets” if they had material items to disclose.

Issuers must also report on several metrics relating to women's empowerment

Other aspects of this rule change included mandatory reporting on human resources policies for achieving sustainability goals (under “strategy”) and any related policy targets and achievements (under “indicators and targets”). Issuers must also now report on the following metrics relating to women's empowerment, which is broadly considered part of sustainability:

- ❑ The percentage of women in management positions in the company or its consolidated subsidiaries.
- ❑ The percentage of male employees who took childcare leave from the company or its consolidated subsidiaries.
- ❑ The difference in wages between male and female workers at the company and its consolidated subsidiaries.

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Japan and ISSB

Japan was an early supporter of ISSB

Japan has made a major commitment to follow the new global standards on sustainability reporting released in mid-2023 by the International Sustainability Standards Board (ISSB). Not only does it have a seat on the ISSB Board, alongside China, Korea, and several other developed and emerging markets, but it also formed a domestic entity to develop the standards called the Sustainability Standards Board of Japan (SSBJ) in mid-2022.

SSBJ exposure drafts announced for March 2024

In early 2023, the SSBJ announced that it would issue exposure drafts no later than 31 March 2024, with final standards published no later than 31 March 2025. These deadlines were reaffirmed in an announcement on Christmas Day 2023. The standards were accordingly released for public comment on 29 March 2024.

Despite debate within the SSBJ, Japan's standards will align closely with ISSB S1 and S2

It is understood that there had been considerable debate within the SSBJ on what Japan's new sustainability reporting standards should comprise. Although the original purpose of the SSBJ was to develop standards that "build on the global baseline" established by ISSB, it appeared some members wanted standards that veered away from full alignment. The FSA, however, favoured standards that were closely aligned and have effectively won the argument. The Christmas 2023 announcement stated that the SSBJ would develop a standard equivalent to IFRS S1 on "General Requirements for Disclosure of Sustainability-Related Financial Information" and IFRS S2 on "Climate-Related Disclosures" as part of an effort to make the Japanese standards internationally consistent. In the end, the SSBJ chose to divide the Japanese version of IFRS S1 into two parts, a "universal sustainability disclosure standard" and a "theme-based sustainability disclosure standard", while leaving the proposed standard based on IFRS S2 intact.

S1 and S2 might only be mandatory at first for a small portion of large caps

The quid pro quo, however, is that IFRS S1 and S2 will likely be made mandatory only for a small number of the largest prime market firms and will not take effect until 2027. Other prime firms will not have to comply until somewhat later, perhaps 2030. An FSA working group was formed in February 2024 and will propose detailed rules in due course.

New METI group on sustainability data

METI is concerned about sustainability data integrity

Shortly before the amended Cabinet Office Order of January 2023 came into effect, METI formed a new working group in December 2022 to "promote the accurate and efficient collection" of sustainability data by companies and to encourage them to view this exercise not as a "necessary chore" but as having a strategic value to their businesses. The working group published an interim report in mid-July 2023 whose core message was that companies should seek to integrate regulatory compliance and disclosure/dialogue on sustainability with their business strategy, thereby enhancing the latter's sophistication and using sustainability data to develop new products and services.

Most issuers lack the systems for effective data collection

It is generally agreed that most issuers lack the tools and human resources to collect sustainability data from across their national and international operations and supply chains. They often delegate this work to less central parts of their organisation, whose job it is gathering data only for disclosure and compliance purposes. Companies should establish a high-level supervising department, such as under the CFO or CEO, that has the authority to lead this work, strengthen cooperation within the corporate group, and invest in the necessary IT systems.

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Opening the English window

Pressure has been building for more English disclosure

Pressure for more English-language disclosure has been building for some time in Japan and was explicitly recognised by the TSE's Council of Experts on market restructuring. Given that a core expectation of prime companies will be greater dialogue with global investors, communication in English is seen as a prerequisite.

A JPX survey in 2023 showed huge support for English financial reports

To get a clearer idea of what global investors wanted, the exchange swung into action with a survey in June 2023 and published the results in late August. It received 75 responses, of which 71 were from institutional investors. Not surprisingly, respondents voted overwhelmingly for English-language earnings reports (Tanshin), IR presentations, and the annual securities report (Yuho). Each received 85% or more in favour. A slightly lower proportion said they wanted translated earnings reports and timely disclosure materials at the same time as the Japanese.

Most agree that English reporting is improving, but not fast enough

Another key finding: a large proportion (75%) recognised that English-language disclosure was improving in Japan, but an almost equal number (72%) expressed dissatisfaction at both the speed of this disclosure and the lack of it for small- and mid-cap stocks.

Lack of English disclosure has a direct impact on investment decisions

And of particular concern: 41% said they discounted the value of companies with poor English disclosure, 35% excluded such companies from their investment universe, and 28% reduced their weightings. Meanwhile, 69% said they could not have in-depth dialogue at IR meetings due to language issues.

New rules require prime companies to report more in English from 2025

In late February 2024, JPX/TSE released new rules for public comment on making English-language disclosure mandatory for prime market companies. There were two key proposals. One was an obligation that prime companies should make every effort to disclose "material corporate information" simultaneously in Japanese and English. The second was a mandatory requirement to disclose financial results and timely disclosure notices in English and Japanese simultaneously. But there will be caveats: summary English disclosure is acceptable; and simultaneous disclosure will not apply if it causes any delay in releasing reports in Japanese. The new rules come into force in April 2025 and companies will be given a grace period of a further year if they apply.

Streamlining quarterly reporting

Plans to reform quarterly reporting rules initially caused a stir

In the second quarter of 2022, the new Kishida government began debating whether to simplify the country's quarterly reporting framework to ease the reporting burden on companies. This idea gained prominence in the PM's first "grand design and action plan for a new form of capitalism" in June 2022, although interestingly only three lines was devoted to it. It nevertheless caused quite a stir.

Japan has historically required two types of quarterly reports

What is the problem? Simply that Japan requires listed companies to produce two versions of their quarterly reports. The first, called the "Tanshin", has been required under TSE listing rules since 1999 and is effectively a preliminary earnings report covering "matters for which speedy disclosure is valued", as the exchange says. The second is a more substantive quarterly securities report, mandated under the FIEA since 2006 and enforced since 2008. The basic idea was to abolish the Q1 and Q3 securities reports required by the FIEA and integrate them into the TSE's quarterly earnings reports, thus simplifying reporting.

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An FSA working group supported the need for quarterly earnings reports

In late 2022, most members of an FSA panel formed to examine the issue agreed that quarterly reports in the form of Tanshins should remain mandatory. They disagreed however on the content of these reports and whether they should be reviewed by auditors.

The result is a simplified reporting framework, yet with substantive content

The TSE then formed a council of experts in mid-2023 to follow up on the work of the FSA panel and to examine the practical operation of the proposed reform, whose basic framework became law with an amendment to the FIEA in November 2023. In the same month the TSE published the conclusions of its council of experts and held a public consultation on the detailed regulations from mid-December to mid-January 2024. Key revisions include:

- The new quarterly reports required under TSE rules will be expanded to include, at least, the following: quarterly consolidated balance sheets and P&L statements; notes concerning going concern assumptions, significant changes in shareholders' equity, and changes in accounting policies; segment information; and notes concerning cashflow (unless quarterly consolidated cashflow statements are already provided).
- Reviews by auditors will be optional. They will, however, be required if the most recent audit opinion on the annual or semi-annual securities report was qualified (or quarterly report, if reviewed). The same will apply if a qualified audit opinion is issued on the most recent internal control audit report or if the most recent annual securities report is released late.

In short, fears that Japan would do away with, or significantly diminish, quarterly reporting proved groundless and it has maintained a solid framework. As one fund manager said, "I'm not sure if there is any information we will no longer get."

4. Listed companies

Japan returns to 8th place (equal) on an improved score of 49%

Japan performed badly in this category in 2020, dropping points and falling to 11th place. It has rebounded by five percentage points this time and resumed the 8th position it last held in 2018, ranking equal with Korea. Despite moving in the right direction, this remains a poor score for a market as advanced as Japan. On a brighter note, it highlights that Japan has a lot of low-hanging fruit that it could pick to achieve much higher scores in future surveys.

The 15 firms surveyed represented a range of sectors

For this section, we surveyed in depth the governance practices and disclosure of 15 large caps. These firms represented a range of sectors, including: autos, banking, chemicals, railways, pharmaceuticals, retail, telecoms, technology, consumer goods, electronics and industrial automation. Both English- and Japanese-language materials were reviewed.

Where Japan does well (or above average)

Japan scored highly on payments to INEDs

As Figure 8 below shows, Japan does best when it does not follow bad practices in other markets, namely stock options for independent directors. Listed companies typically pay such directors a fixed monthly fee only. A few offer restricted stock, but usually on terms that are tightly structured and transparent. We have also seen an improvement in the explanations provided for executive remuneration policies, with clearer short- and long-term targets, and a greater use of stock incentives.

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IR pages on websites are thorough, but lack names and contact details

Companies also tend to have easily accessible and comprehensive investor relations (IR) pages on their websites. One thing lacking is the names and contact details of their IR team - a simple thing to do and best practice in other markets. Despite a decent average score of 3/5, however, we have not recorded any improvement in IR disclosure practices since our last survey in 2020. Notably, no company scored higher than a 3.5. New English-language disclosure rules from the TSE - which came too late for this survey - should contribute to a higher average score in future.

Sustainability reporting quality varies widely

Japanese companies also do reasonably well in their approach to sustainability reporting - although not as high on average as one might expect. As Figure 8 shows, the average score is held down by some very poor scores (0, 1) for a few companies, although this is balanced to some degree by high scores (4, 5) for others.

Solid GRI-style reporting, but limited TCFD

There is solid GRI-style reporting across most large companies, some use of the SASB sectoral indicators, and partial TCFD reporting (several issuers got started on this before it became a requirement in the Yuho from FY 2023). Disappointingly, the value of materiality assessments still varies considerably and few companies make any attempt to link these to their operations or business strategies - again, a weakness we noted in CG Watch 2020.

Most nomination committees had independent chairs

One positive upside surprise was the high proportion of independent chairs on statutory and voluntary nomination committees, which in some companies do double duty as remuneration committees. It was good to see that in most companies a majority of directors on these committees were independent. And it was refreshing to note how often they met during the year: some four to five times, a few 10 or more times. While 10 meetings are arguably too many, it does at least show a more serious approach than one finds in many other listed companies in Asia, especially those with family owners, where the nomination committee gathers for a cursory chat once or twice a year under the watchful eye of the company chairman or his proxy.

Two thirds of companies had a women director on their nomination committee

Another positive trend: We added a new question on whether nomination committees were chaired by women or had at least one female director. While none of the 15 companies had a female chair, 11 of them had at least one woman on their nomination committee and some had two. This hopefully augurs well for board diversity in future.

Where Japan performs averagely

Board evaluation improving, but overall lacks narrative

One area where Japan has improved, albeit from a low base, is board evaluation. Companies are taking a more sophisticated approach to this process, such as using external consultants and disclosing evaluation methodology. While one company almost scored a perfect 5/5, overall scores were held down by a lack of narrative on the results and the steps the company intends to take to address areas of weakness: few companies offered anything but generic and often self-congratulatory verbiage. More specificity would be welcome.

No progress in disclosure of director remuneration

There has not, sadly, been any real progress on the disclosure of director remuneration. Companies are still only required to disclose the pay packets of executives earning ¥100m or more, a rule that dates to 2010. For some boards this results in most inside directors having their remuneration disclosed; on others it can be just one or two people. Independent directors, meanwhile, tend to just get a fixed monthly fee. It is worth noting that the overall score would have been worse on this question were it not for two companies with excellent disclosure and which earned 5/5.

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Reporting on audit committee skills and performance is limited

Scores were average too on the extent to which audit committees are independently led and competent in accounting and financial reporting matters. While there has been improvement in this space since the introduction of the third system of governance, the “audit and supervisory committee company” almost 10 years ago, there remains a gap in the quality of disclosure between the three systems. Companies with the new structure and those with “three committees” tend to be more transparent than firms with a traditional Kansayaku board. It is often difficult in the latter, for example, to work out who chairs this board or even if there is a chair. Scores were held down also by the fact that many members of these committees have no apparent accounting or financial management expertise.

Reporting on internal audit reporting remains sparse

We found little change in the extent to which companies talk about internal audit (IA). In a Kansayaku board company, IA will report to it and/or the CEO. Some organisation charts highlight that IA also reports to the board of directors. In a “three committee” company, IA reports to the audit committee and senior management. And in an “audit and supervisory board” company, IA typically reports to this committee and the CEO. In none of the companies surveyed did we find any explanation as to how this reporting relationship works, how conflicts of interest are managed, or if independent directors have any access to IA.

Figure 8

Japan listed companies scores, CG Watch 2023

Question	Average score	Range of scores
1. Does the company's board governance reporting compare favourably against international best practice?	2	0.5-3
2. How would you rate the quality of the company's ESG/sustainability reporting?	3	0-5
3. Does the company provide comprehensive, timely and quick access to information for investors?	3	1-3.5
4. Does the company undertake annual board evaluations, either internally or using external consultants?	2.5	0-4.5
5. Does the company disclose and implement a credible board diversity policy?	1.5	0.5-3.5
6. Does the company provide induction and/or ongoing training to all directors?	1.5	1-2.5
7. Does the company have an independent chairman and/or a lead or senior independent director?	0.5	0-5
8. Does the company disclose total remuneration of each member of the board of directors?	2.5	1-5
9. Are the independent directors paid partly or wholly in stock options or restricted share awards? Do they share in a percentage of company earnings or other commissions in addition to their base fee?	5	All get 5
10. Are audit committees (or an equivalent) independently led and competent in financial reporting/ accounting matters?	2.5	1-4
11. Does the company have an internal audit department that reports to the audit committee?	2.5	2-3
12. Does the company provide a detailed explanation of its executive remuneration policies?	3.5	2-5
13. Does the company have a nomination committee and is it independently led?	3	0.5-5
14. Does the nomination committee have a female chair or at least one female director?	1.5	0-2

Source: ACGA research. Based on 15 large caps from a range of sectors

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Where Japan does poorly

Board governance reporting is woeful

It is déjà vu all over again for our board governance reporting score - a disappointing 2/5. Despite improvements required in non-financial reporting in the Yuho, specifically on board and committee activities, we continue to find that most disclosure is generic and of little use to investors. There is more substantive reporting on cross-shareholdings in the Yuho and some CG reports, but often, this only serves to highlight what is not being divulged, namely a detailed rationale for continuing to lock up large chunks of equity in the shares of other companies.

Skills matrices are a welcome new feature, yet disclosure is often shallow

One new feature of board reporting in Japan is the "skills matrix", a requirement since the CG Code was amended in June 2021. Most of these matrices are quite superficial, however, providing merely a list of skills and ticks if a director has that skill. The skills are rarely defined and sometimes appear to overlap (eg, what is the difference between "industrial" and "production" expertise"?). Nor could we find thoughtful discussions as to what this might mean for board composition in the future, since few companies seem to be using their skills matrix to shape their director pipeline.

Only four of 15 issuers had credible board diversity policies and targets

Scores were even lower on whether companies have and disclose credible policies and targets on board diversity. Four issuers did well with a score of 3.5/5, in part because they have firm targets on gender diversity in their boards and/or management (eg, 25% female middle managers by 2025; 30% female directors by 2030). Yet most of the remainder (10 firms) earned a 1 or less. If anything reflects the depth of conservatism in Japan's male-dominated business environment, it is this data point.

Issuers remain reluctant to talk about director training

We also see little movement in the willingness of companies to talk about the induction and ongoing training they claim to provide directors, and whether executive as well as independent directors undertake this training. This has been a blackhole in CG reporting in Japan for as long as we can remember and, as we note above in the box titled "Will naming and shaming work?", how can boards get on top of capital management if directors lack the skills to understand basic financial metrics? Moreover, how can they make sound strategic decisions on sustainability and climate if they do not understand the complexity of these issues? One of the obstacles to widespread training, at least in the more conservative companies, is a cultural reluctance to "train" newly appointed independent directors. The assumption is that such people already know enough about governance or would not have been appointed to the board in the first place.

Only two companies had an independent chair, and none had a lead independent director

Finally, the lowest scoring question in our survey related to whether companies had an independent chair and/or lead independent director. Not surprisingly, few had the former - just two out of the 15 assessed. None had lead independent directors, a concept still under-utilised in Japan even though mentioned in the original CG Code of 2015.

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Swearing allegiance no more?

Cross-shareholdings remain a major obstacle to CG improvement in Japan

One of the most entrenched CG challenges in Japan is the persistence of cross-shareholdings between independent companies. Also called friendly or "allegiant" shareholdings, at worst these exist to protect incumbent management and directors from scrutiny by independent shareholders and possible removal from the board. In their defence, companies argue that these arrangements are often "strategic" investments, rather than purely financial ones, and help to maintain good client relationships or cement a business alliance.

Financial institutions have reduced their holdings significantly over 40 years

Over the past decade the FSA has put pressure on banks and insurers to reduce these holdings, with some success. The latest "Shareownership Survey" from JPX for fiscal year 2022 (to March 2023) shows the ownership share of financial institutions in other listed companies falling from a high of around 40% of market capitalisation in the mid-1980s to just 7% by the end of March 2023. This excludes trust banks, which hold securities on behalf of other institutional investors and whose share has risen from 10% to 23% over the same period.

The FSA is pushing non-life insurers to unwind faster following a pricing scandal

Following recent scandals in the insurance industry, however, the unwinding seems set to gather pace. Although formal announcement has yet to be made, it was reported in February 2024 that the FSA requested four major non-life insurers to sell all their holdings (around 5,900) in the coming years. This came after the regulator discovered price fixing between Tokio Marine & Nichido Fire Insurance, Sompo Japan Insurance, Mitsui Sumitomo Insurance, and Aioi Nissay Dowa Insurance. The aggregate value of their holdings in other firms is ¥6.5tn (US$43bn) or some 18% of all allegiant shareholdings in Japan on some measures. It is hoped that this action will put pressure on banks and other companies to unwind faster.

Market tailwinds should help companies to unwind faster

The good news is that there are some other tailwinds, starting with the substantial rise in the Japanese stock market over the past year. There has never been a better time to sell allegiant stocks. Shareholder pressure on listed companies is growing, with increasing requests for sensible explanations on the rationale for so-called strategic holdings and for tying up so much capital in this way. The TSE's March 2023 guidance on cost of capital is intended to facilitate more efficient long-term capital-management policies among companies, which in turn should lead to the selling down of more holdings.

Some companies are selling because they need the cash

The past year has also brought a new narrative to Japan: the corporate which sees cross-shareholdings as an impediment to achieving its business goals. Take Denso and Aisin, two Toyota affiliates, for example. In June 2023, Denso filings showed it had sold its entire stakes in Suzuki (US$116m), Honda (US$77m), Central Japan Railway, and Ibiden; and was down to around 20+ holdings from 44 in 2019. The company said it wanted to use the cash generated to "invest in creating corporate value as dictated by growth strategies". Aisin was even bolder, saying it would sell all its cross-held shares in 19 listed companies, including Denso and Toyota Industries, to raise capital for new investment in electric vehicle parts manufacture.

The ratio of friendly shareholders seems set to remain high

But it may be too early to pop open the champagne. A recent survey by legal journal *Shoji Homu* showed that the ratio of "stable shareholders" likely to vote in favour of management had fallen from a very high 69% in 2012 to a still high 57% in 2022. Allegiant holdings will be around for some time.

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5. Investors

Japan retains second place on a higher score of 65%

There is clear daylight in this category between the top two markets - Australia and Japan - and the rest. Japan showed steady progress with an increase in score of five percentage points to 65%. This followed more voting and engagement activity generally by domestic and foreign institutional shareholders, as well as a rise in activism and shareholder proposals. The large state pension fund, the Government Pension Investment Fund (GPIF), continued to play a leadership role through its policies for external managers and original research on investor stewardship developments and performance. Other domestic asset owners meanwhile are starting to collaborate more on governance and ESG issues.

Where scores increased

Areas where scores increased included: foreign investor promotion of CG through upgraded internal voting and engagement policies; a greater propensity among foreign investors to participate in collective or collaborative engagement of companies; physical participation in AGMs; domestic asset owner leadership; improvements by domestic asset managers regarding management of conflicts of interests; and more shareholder proposals from both retail and institutional investors.

Where scores declined

Areas where scores declined, though only slightly, included domestic asset manager promotion of CG (most funds take a low profile on policy and regulatory advocacy) and the willingness of domestic investors to participate in collective engagement efforts.

Regional stewardship leader

Japan wrote the first stewardship code in Asia in 2014

Among Asian countries, Japan is the clear leader in promoting investor stewardship. The FSA published the region's first Stewardship Code in February 2014 and has revised it twice, in 2017 and 2020. It chose not to do so again in 2023 in favour of investing time and political capital in a new "Action Program" on corporate governance, a decision we applauded. The Code laid the groundwork for the active approach subsequently taken by the GPIF to promoting stewardship among its external asset managers, a group which includes foreign as well as domestic asset managers. While the GPIF was not the first asset owner in Japan to get behind CG - an accolade that rightly goes to the Pension Fund Association (PFA) in the early 2000s - it is certainly the largest. And whereas the PFA's efforts were initially confined to influencing how domestic investment managers voted their shares, the GPIF's support for stewardship has pushed asset managers to engage as well as vote.

Japan's code has many more signatories than other markets in Asia . . .

Thanks to pressure from the FSA in particular, Japan's Stewardship Code has vastly more signatories than comparable principles in other markets: 331 signatories as of 31 December 2023, of which two thirds were investment managers and another quarter were pension funds. The remainder, in proportional order, were insurance companies, service providers (eg, proxy advisors, stewardship specialists, investment or HR consultants), and trust banks. Many of the signatories were foreign entities, especially in the investment management category, although foreign names can be found in all categories. Interestingly, while some of the 82 pension funds are organisations like GPIF, PFA and other industry or government employee entities, most are corporate pension funds - something that marks out the Japanese approach to stewardship as more inclusive than most other markets in Asia-Pacific. Big name corporate signatories include Daiichi Sankyo, Ebara, Eisai, Itochu, JAL, Konica Minolta, Mitsubishi, MUTB, Mizuho, NTT, Omron, Panasonic, Resona, and SMBC. The list goes on. Corporate participation should not be overstated, however. This development is of recent vintage and only a small fraction of listed companies have endorsed the Code.

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. . . yet code signatories account for only 18% of listed shares

A further reality check: as the PFA notes, the aggregate volume of shares held by domestic institutional investors required to endorse the Code amounts to only about 18% of market cap, which significantly limits their influence. Another 30% or so are held by banks and general corporates that are not required to sign up. ACGA's view is that listed companies and banks which hold equity in other listed firms should be held accountable for these investments and be required to sign the Code. It is not enough for company pension plans, with their severely limited human resources and investment expertise, to endorse on behalf of their parent. Directors are primary stewards within companies, and it is logical to expect that they should explain their stewardship of the company's capital and voting decisions.

GPIF as a stewardship catalyst

GPIF promotes stewardship through its external fund managers

While it is not the full story, one starting point for understanding how stewardship is evolving in Japan is the GPIF's annual "Stewardship Activities Report". The first part focusses mainly on the efforts of the fund - which cannot invest or vote directly - to engage with its external managers for equities, fixed income, and alternative assets on integrating ESG into their investment activities. It also engages with index providers and seeks to promote dialogue between investors and companies. The report goes on to describe the extent to which these managers are engaging with listed companies on ESG topics and the challenges they face. The last part lays out the GPIF's expectations for its managers and action plans.

GPIF managers are engaging with more companies

Data provided in the 2022/23 report, published in March 2023, show a significant increase in the number of meetings that GPIF's 31 external managers held with Japanese companies over the 2017 to 2022 period - the figure doubled from around 3,000 to more than 6,000 per year, while the number of companies investors met increased from around 850 to almost 1,000. Most of these meetings were with company executives, although a decent and rising proportion involved company presidents. There was a sixfold increase in meetings with outside directors. As for the issues discussed, governance accounted for 59%, environment for 23%, and social the remaining 18%. A critical point to note is that more than 80% of meetings were undertaken by passive investors, which comprise most of the GPIF's external managers. Some are using AI to make their life easier.

Passive and active managers focus on somewhat different things

What do managers talk to companies about? It depends to an extent on the type of manager you are. As Figure 9 below shows, both passive and active managers rated climate change and general disclosure as critical. Beyond this, passive managers put more emphasis on supply chain, misconduct, corporate governance, human rights, and diversity issues, whereas active managers tend be to more focussed on minority shareholder rights, board structure and evaluation, and capital efficiency.

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Figure 9

Critical ESG issues in Japan: Topics cited by GPIF external managers, as % of respondents

Passive managers of domestic equities		Active managers of domestic equities	
Climate change	100%	Climate change	100%
Supply chain	100%	Disclosure	100%
Disclosure	100%	Minority shareholder rights	100%
Misconduct	100%	Board structure, self-evaluation	100%
Corporate governance	100%	Capital efficiency	100%
Human rights & community	100%	Misconduct	86%
Diversity	100%	Diversity	86%
Biodiversity	83%	Supply chain	71%
Capital efficiency	83%	Others (governance)	71%
Board structure, self-evaluation	83%	Corporate governance	71%
Minority shareholder rights	83%	Labor standards	71%
Environmental opportunities	67%	Human rights & community	71%
Waste management	67%	Waste management	57%
Water stress, water security	67%	Biodiversity	57%
Deforestation	67%	Environmental opportunities	57%
Anti-corruption	67%	Pollution & resources	57%
Labor standards	67%	Health & safety	57%
Health & safety	67%		
Others (social)	67%		
Product liability	67%		

Source: GPIF, March 2023

Company views of investor engagement is improving

What impact are these managers having? Interestingly, and uniquely for Asia, the fund carries an annual survey of how listed companies view their stewardship efforts and those of other institutional investors. The latest survey is the 8th and was published in May 2023. It broadly shows that companies, which were often critical of investors in the past, are more impressed today with the effort being made prior to and in engagement meetings. For example, more than 60% of respondents said that investors appear to be using their integrated reports (ie, ESG reports) more effectively than before, while 30% said the same for using CG reports. Around 40% observed "desirable changes" in the attitude of institutional investors.

PFA as a stewardship catalyst

The PFA is re-emerging as a stronger voice in the stewardship space

A more recent, and somewhat radical, development over the past six months has been the re-emergence of the PFA as a stronger voice in the stewardship debate. In response to the government's plan to turn Japan into a "Leading Asset Management Center" and other pro-CG policies, the association is planning to form a group tentatively called the "Corporate Pension Stewardship Promotion Council". This entity, whose official name has yet to be decided, would be part of the PFA organisation and comprise any corporate pension fund that wished to join. The objective would be to create a collaborative framework for monitoring the external investment managers and trust banks that manage corporate pensions, with a view to resolving the practical difficulties that most corporate pension funds have in carrying out their stewardship responsibilities.

The PFA wants corporate pension funds to be more active stewards

As the PFA said when announcing this new strategy in late September 2023:

> "Unfortunately, corporate pension funds' stewardship activities do not have the expected impact on the domestic stock market. In addition, since the management of domestic stocks by corporate pension funds is outsourced to a fiduciary institution, the selection of companies to invest in and the engagement with those companies are not done by the pension funds themselves. It is the trustee institution that selects the companies to invest in and exercises engagement and shareholder voting rights over those companies, not the corporate pension plan."

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Corporate pension stewardship needs to be more visible and effective

While the "specific stewardship activities expected of corporate pension plans are to monitor the stewardship activities of their fiduciary institutions and to encourage them to engage in stewardship activities", said the PFA, it was also apparent that each corporate fund did this in its own way, was not always fully informed, and outcomes were suboptimal. "While the interest of corporate pension funds in stewardship activities is not low, specific efforts are not yet visible," the PFA warned, adding that "it is difficult to see concrete efforts being made".

The PFA is creating a platform for funds to collaborative

The collaborative framework being proposed would include such joint initiatives as:

- "Questionnaire-based collaborative surveys to check common items;
- "Joint briefings and collaborative dialogues on stewardship activities of fiduciary institutions;
- "Providing and publishing a summary report on stewardship activities and self-assessment of trustee institutions based on a predetermined format."

The PFA also intends to the council to become a signatory to the stewardship code and will publish its membership. Watch this space.

Voting, voting, voting

The PFA launched its voting policy in 2003

Japan could also be said to be a voting leader in Asia given the longevity of investor involvement in this area. Things began to get interesting in July 2002 when the PFA, which is both an investment fund and the peak industry body for corporate pension funds, began voting its shares with the explicit goal of improving listed company returns and governance. The Association developed a voting policy in 2003 that focussed on key governance challenges at the time and became influential among Japanese mainstream institutional investors. It was revised in 2007. Key principles included:

- Opposing the re-election of directors if a company has been making losses and not paying dividends for three years, or if its ROE has been poor for many years;
- Reducing executive remuneration if a company has been incurring losses and not paying dividends;
- Opposing retirement bonuses for outside directors and when a director resigns due to misconduct or if the company has been incurring losses;
- Approving share buybacks in principle, while noting that the distribution of profits to shareholders should strike a balance with the company's future business plans, employee compensation, and so on;
- Opposing private placements when a company has not provided sufficient explanation as to why it needs the additional capital;
- Opposing the (re)appointment of accounting auditors when a company does not provide a sufficient explanation as to their independence.

Many of these issues are still relevant in corporate governance in Japan today. Indeed, several of them are reflected in the latest version of the PFA's voting policy published in March 2022.

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GPIF developed a voting policy in 2017

Once the GPIF took stewardship seriously and began encouraging, then requiring, its external managers to integrate ESG into their investment process, it developed a voting policy too. Released in June 2017 and revised in 2020, the Fund's "Proxy Voting Principles" state, among other things, that its external managers should "exercise any and all voting rights" in line with its Stewardship Principles and develop their own voting policies and guidelines that will "contribute to the maximization of shareholders' long-term interests". These policies should be publicly disclosed, including each manager's voting records down to the individual company/resolution level and reasons for voting decisions "based on necessity and/or importance as appropriate". Managers should also explain their voting decisions to listed companies if requested.

GPIF managers vote largely in favour of management

What are the GPIF's managers voting for and against? As Figures 10 and 11 below show, there are marked differences between how investors approach management proposals compared to shareholder proposals, and between domestic and foreign equities. The vast majority of votes tend to be cast in favour of management proposals for appointing directors, statutory auditors, director remuneration and dividends. Votes for director bonuses and stock options are also high, but not quite as robust as the other categories. And echoing the PFA's policy from 2007, there was very little support for director retirement bonuses. Meanwhile, there was virtually no support for poison pills.

Shareholder proposals receive limited support

Given industry dynamics, it is perhaps not surprising that investors gave little support to most shareholder proposals, including those for directors and amendments to articles of association. Somewhat more robust though were votes in favour of shareholder proposals for statutory auditors (26%) and outside statutory auditors (43%). Proposals on dividends and the acquisition of treasury stock received a respectable 19% and 17% level of support, respectively. While less than 10% of votes supported changes to articles of association.

Figure 10

How GPIF managers voted on domestic equities, April to June 2022

(%)	Directors	Auditors	Remuneration	Bonuses	Retirement bonuses	Stock options	Dividends	Treasury shares	Articles	Poison pills
Management proposals										
Approved	88.7	89.3	95.6	85	13.7	78.9	97.5	na	98.6	5.7
Opposed	11.3	10.7	4.4	15	86.3	21.1	2.5	na	1.4	94.3
Shareholder proposals										
Approved	1.4	25.8	11.3	na	na	na	19.4	17.3	9.7	na
Opposed	98.6	74.2	88.7	na	na	na	80.6	82.7	90.3	na

Note: na means there were no proposals. Source: GPIF

Voting against is much larger at the AGMs of foreign companies

It is also noticeable how much bigger the appetite for voting against is at the AGMs of foreign issuers. As Figure 11 below shows, votes against management proposals for directors were 7.8 percentage points (or 69%) higher. There was almost six times as much opposition to director remuneration and almost double the votes against stock options. Conversely, poison pills received strong support, as did some shareholder proposals (eg, appointment of directors, stock options).

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Figure 11

How GPIF managers voted on foreign equities, April to June 2022

(%)	Directors	Auditors	Remuneration	Bonuses	Retirement bonuses	Stock options	Dividends	Treasury shares	Articles	Poison pills
Management proposals										
Approved	80.9	85.9	74.1	87.5	20	61.7	99.6	96	86.6	80.6
Opposed	19.1	14.1	25.9	12.5	80	38.3	0.4	4	13.4	19.4
Shareholder proposals										
Approved	72.9	77.1	22.4	na	25	75	na	na	34.7	100[1]
Opposed	27.1	22.9	77.6	na	75	25	na	na	65.3	na

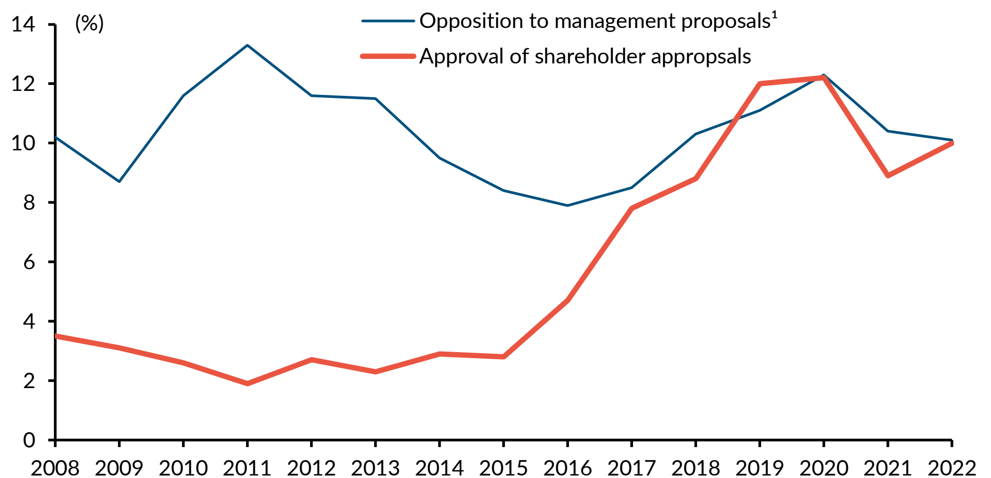
[1] Only one proposal; na means there were no proposals. Source: GPIF

Support for shareholder proposals rose somewhat after the GPIF brought in a voting policy and the Stewardship Code was revised in 2017

Looking at voting trends over time gives a more nuanced view - and shows how guidelines can influence behaviour. As Figure 12 below shows, the opposition of GPIF managers to management proposals in Japan has remained steady for the 15 years to 2022, while approval of shareholder proposals started rising slightly before the Stewardship Code was revised for the first time in May 2017 and investors were instructed to disclose voting records "for each investee company on an individual agenda item basis". They continued to rise afterwards. There may be many reasons for this change, but it seems reasonable to conclude that the revised Code played a part. It is likely that the GPIF's voting policy, introduced in 2017, had an impact too.

Figure 12

How GPIF managers voted on management vs shareholder proposals, 2008 to 2022 (domestic equity)



[1] Also includes abstention from voting. Source: GPIF

Voting on foreign equities shows a very different picture over time

As for voting on overseas listed companies, opposition to management proposals remained flat until 2017, when it started rising. In contrast, support for shareholder proposals has been of a completely different magnitude to Japan, rising from almost 30% in favour in 2008 to 52% in 2022, as Figure 13 below shows.

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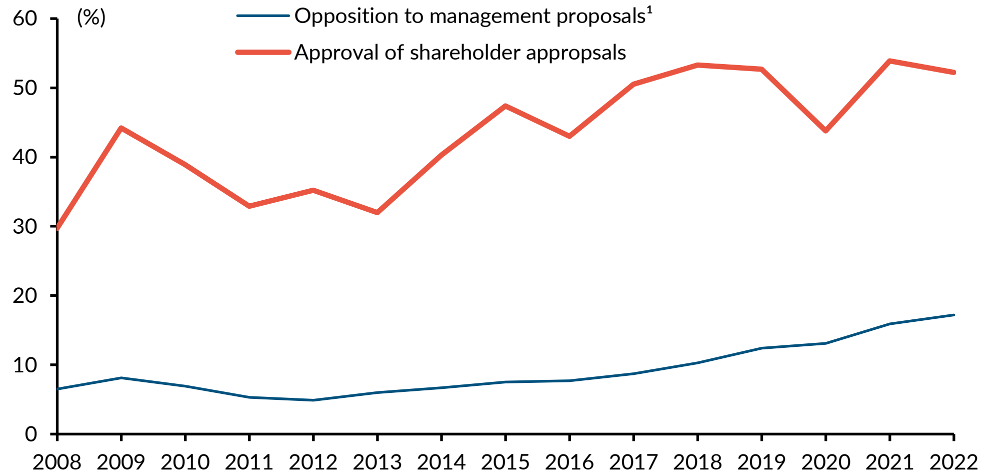
Figure 13

How GPIF managers voted on management vs shareholder proposals, 2008 to 2022 (foreign equity)



[1] Also includes abstention from voting. Source: GPIF

Energised voting - up to a point

2023 may be seen as a landmark year for active voting in Japan

It is possible that 2023 will go down in CG folklore in Japan as the year investors almost toppled the powerful octogenarian Chairman & CEO of Canon, Fujio Mitarai, with an unprecedented 49.41% vote against - a doubling of the opposition from the year before. The reason for investor ire? Both the complete absence of women on the company's board and disappointment over climate targets. This year, Canon recommended three new independent directors for election, one of whom was a woman. This will give the board a 10% female representation ratio.

Target voting against inside directors is on the rise

Investors used their votes to target the re-election of directors at other companies too. The chairman of Kyocera, Goro Yamaguchi, was hit with a 34% vote against, while its president, Hideo Tanimoto, suffered slightly higher opposition due to the company's large volume of cross-shareholdings. At Toray, the CEO, Akihiro Nikkaku, attracted an 18% vote against. At Softbank, an outside director, Kenneth Siegel, was opposed by 33% of votes. And at Toyota, support for Chairman Akio Toyoda dropped 11 percentage points to just under 85%. Material votes against were cast at numerous other companies.

But most votes remain in favour of most directors

How do the cases compare to the prime market as a whole? Data compiled by Japan Shareholder Services (JSS), a leading IR/CG advisory and research firm, indicates that votes in favour of both internal and outside directors at June 2023 AGMs hovered around the 95% mark and were slightly higher year-on-year. In other words, institutions are voting against director re-elections but only in a highly targeted manner and with a focus mostly on larger caps.

Retirement bonuses and poison pills still attract material votes against

JSS figures also highlight that votes against retirement bonuses (almost 19%) and poison pills (around 27%) were material, albeit on a small number of companies. The PFA's voting policy of the early to mid-2000s has clearly had an impact.

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Collective engagement is still in its infancy

Collective engagement

One of the more challenging areas for investors in Japan is collective or "collaborative" engagement, which involves asset owners as well as managers coming together, effectively with their competitors, to engage jointly with individual companies on CG or ESG issues. Historically, such action has been held back by the country's somewhat onerous and vague "joint holder" (concert party) rules, even though the stewardship code has supported it since 2017 and group meetings make eminent and efficient sense for all concerned. There are now signs that institutional investors have a greater propensity to cooperate on issues of common concern, although a few major companies still avoid group meetings.

GPIF managers collaborate to an extent, but on ESG not CG issues

The GPIF's "Stewardship Activities Report 2022-23" highlights a few areas where its external managers have been collaborating. The emphasis is largely on ESG or sustainability initiatives that are global or regional in nature, such as Climate Action 100+, the Net Zero Asset Managers Initiative, and the Asian Investor Group on Climate Change. GPIF is also interested in seeing how its managers respond to Nature Action 100, an investor-led global campaign on biodiversity, and PRI Advance, which describes itself as a "stewardship initiative for human rights and social issues". What is missing from the Fund's report is any reference to its asset managers working together on core CG issues in Japan.

Less than 10% of companies say they have received a request for a collaborative engagement

GPIF provides more insight in its latest annual survey of listed companies, released in May 2023. In response to the question, "Have you ever received a request for conducting collaborative engagement?", only 9.6% said Yes. Of those who accepted a group meeting, two thirds went ahead, while the remainder were either preparing for such meetings or exchanged letters without meeting. The major themes for engagement and key counterparty foreign and local organisations mentioned by companies are in Figure 14 below.

Figure 14

GPIF company survey 2023: collaborative engagement topics and initiatives

Major themes
ESG as a whole
Response to climate change (decarbonization strategy, etc)
Deforestation
Cross-shareholdings
Governance of parent-subsidiary listings
Initiatives
ACGA (Asian Corporate Governance Association)
AIGCC (Asian Investor Group on Climate Change)
Climate Action 100+
Institutional Investors Collective Engagement Forum
PRI Collaboration Platform

Source: GPIF

More companies seem open to such an engagement

Promisingly, more than one third of the 90% of firms which had never received a request for collaborative engagement said they would do so if asked. Another 63% said they would consider it. Only 1.4% said it was their policy not to accept such meetings.

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IICEF is seeking to fill the collective engagement gap

Helping to fill the engagement gap locally is an entity highlighted above, the Institutional Investors Collective Engagement Forum (IICEF). Formed in October 2017 and comprising seven major institutional investors including the PFA, its goal is to “contribute to an increase in long-term corporate value and sustainable growth of companies, not to pursue short-term shareholder returns”. It primarily does this through writing letters and making suggestions to major listed companies on ways in which they could improve their governance. From time to time, it also seeks to engage directly with selected listed companies, as it did in early 2021 with Sumitomo Chemical and in April of the same year with Mitsui O.S.K Lines. In January 2023 IICEF met with outside directors and outside corporate auditors of Toray Industries to express concerns about misconduct at the company. More recently, in October 2023, it wrote to selected companies on the prime market seeking information and requesting meetings to discuss the TSE’s guidance on management that is conscious of cost of capital.

IICEF also contributes to regulatory consultations

IICEF is also somewhat unusual in that it is one of the few investor-backed bodies in Japan that contributes written submissions to regulatory consultations. It provided comments on the CG Code revision in 2021, the TSE’s market restructuring in 2022, and METI’s new guidelines on corporate takeovers in 2023.

Domestic asset managers have done little collaborative engagement to date

Beyond IICEF, there is little evidence in Japan of domestic asset managers undertaking collective engagement. In contrast, the picture is becoming more interesting in the foreign investor space. One line of activity, which is comparatively rare, involves a small number of major global investors joining forces to submit shareholder proposals to companies, as happened in 2023 at Toyota Motor and J Power (*see box below*). The other, which is becoming more common, involves larger groups of investors engaging in a sustained engagement effort focusing on large companies in Japan.

ACGA is helping foreign investors engage collectively

One of the more established initiatives here is, in fact, ACGA’s own Japan Working Group (JWG). This group was formed in 2016 to support ACGA’s policy and regulatory advocacy in Japan and today comprises around 30 investor members with more than US$26tn in assets under management. In 2021 it began formulating a plan to engage with half a dozen systemically important firms across a range of industries: autos, banking, chemicals, industrial appliances and consumer goods. JWG formed subgroups for each company engagement, led by one of our investor members, and developed a set of engagement topics and specific issues to discuss with company representatives. The groups typically have two meetings per year with each company, either online or in-person, and have in-depth discussions with executives and directors. While initial meetings tended to be with IR teams, JWG’s dialogue has evolved to include heads of sustainability, CFOs, and independent directors. This is a medium to long-term programme that seeks substantive and meaningful governance improvements in companies, something we believe will enhance corporate value over time. We also see governance improvements in Japan as fundamental not only for helping to achieve the TSE’s cost of capital reforms but making sensible risk-based decisions around sustainability and climate.

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Activism in Japan has become more varied and nuanced over time

Engaged (and sometimes enraged) shareholders

Gone are the days when activism in Japan meant a hard-nosed hedge fund trying to bash down the door of a staid company and raiding the cash vault. Activism has become more nuanced, varied, and longer term in outlook, while mainstream institutional investors are showing a greater willingness to file shareholder proposals and NGOs are stepping up the pressure on environmental themes.

Shareholder proposals showed a significant increase in 2023

One statistic that reflects this growing level of active ownership is the number of shareholder proposals put to AGMs. As proxy advisor, Glass Lewis has noted, it reviewed 387 shareholder proposals at 95 companies in the 2023 season, a 28% increase year-on-year for the number of proposals and 23% for the number of companies. "We expect that this trend will continue in future unless investors see the improvement of basic corporate governance issues, capital efficient issues, climate change related risk disclosure issues, etc," said Glass Lewis.

Proposals are coming from a range of retail, activist, and mainstream funds

Who is putting forward these proposals? It is a veritable smorgasbord of shareholders, such as:

- Kiko Network, a Japanese environmental NGO, which put forward climate-related proposals at six listed companies in 2023, including all three megabanks (MUFG, SMFG, Mizuho) and major power companies. The proposals follow similar efforts targeted at the banks in previous years and call for more disclosure on how they will meet their net-zero commitments.
- HSBC Asset Management, which filed a joint shareholder proposal with Amundi Asset Management of France at J-Power for the second year in a row in 2023. They called on Japan's largest coal-fired power generator to 'set and disclose credible short and medium-term emission reduction targets in line with the Paris Agreement'. Interestingly, the two investment giants worked with an Australian NGO, the Australasian Centre for Corporate Responsibility (ACCR), which is active in Australia on climate proposals at AGMs. The proposal was also supported by Man Group, another large investment institution based in the UK.
- APG Asset Management (Netherlands) and two other large European investors co-filed a climate-related shareholder proposal at Toyota Motor in 2023. Billed as the first-ever proposal to Toyota, the resolution asked the company to do a comprehensive annual review of its climate lobbying and how this reduced risk to the company from climate change and supported both the Paris Agreement goals and the firm's own 2050 net zero commitment. The co-filers included AkademikerPension of Denmark and Storebrand of Norway.
- Oasis Management (Hong Kong), which requisitioned an EGM at Fujitec in Japan in February 2023 to remove six incumbent outside directors and replace them with its own candidates. Shareholders voted to remove three of the incumbent outsiders (one resigned prior to the meeting) and supported four of the Oasis candidates. Shortly afterwards, the new board removed the incumbent chairman. The former chairman subsequently fought back by launching a lawsuit against the company in May 2023 and nominating eight new outside directors at Fujitec's June 2023 AGM (he failed to get any support). He then filed a further lawsuit in September.

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6. Auditors and audit regulators

Japan improved to equal second on a rise in score to 83%

After improving in score but not ranking in Auditors & Audit Regulators in 2020, Japan gained six percentage points this time and rose to equal second with Singapore and Taiwan. The higher score came on the back of mostly small increases across several questions, rather than a large gain in one or two areas. Scores also fell slightly on a couple of questions. It is worth noting that while Japan has tended to lag other Asian markets in the implementation of “key audit matters” (KAMs) and it remains unusual in having three sets of accounting standards in regular use (four if you count one rarely used), it has on the other hand been the leader in one area: having an “Audit Firm Governance Code”. This used to apply only to the Big 4 but is now being gradually adopted by other firms.

Where scores increased

Scores increased on several questions relating to rules and standards, including: more companies adopting IFRS; local auditing standards being fully converged with International Standards on Auditing (ISAs); effective rules on the independence of auditors; disclosure of audit and non-audit fees; and implementation of KAMs. They also increased for firmer regulatory efforts over accounting firms.

Where scores fell

Scores fell slightly on two questions: disclosure of enforcement and disclosure of inspection results.

Accounting standards

Most financial statements follow J-GAAP

International Financial Reporting Standards (IFRS) as issued by the International Accounting Standards Board (IASB) are still voluntary for listed companies in Japan, although their use is permitted. Most Japanese financial statements are prepared in accordance with accounting principles generally accepted in Japan (JGAAP), as issued by the Accounting Standards Board of Japan (ASBJ). Listed companies may also use US GAAP or a fourth version developed by the ASBJ called Japan's Modified International Standards (JMIS). JMIS were a set of accounting standards published by ASBJ in 2015 and comprise two parts: IFRS standards issued on or before 31 December 2012 and ASBJ modifications on goodwill and other comprehensive income. There have been further amendments since, mostly endorsing changes to IFRS standards. But since JMIS was developed in 2015, no company has reportedly applied the Standards.

ASBJ is an active participant in international standard setting discussions

The ASBJ has been an active participant in the international standard-setting process and routinely issues comment letters each year on major IASB exposure drafts. In 2023, for example, it released comments on amendments to such standards as IFRS 9, IFRS 7 and IAS12. It also issued exposure drafts on changes to JGAAP addressing electronic means of payment, leases, and other things.

It also participates in international fora

Outreach to standard setters in other countries is an important part of its remit. On 30 March 2023, the ASBJ met with the new UK Endorsement Board, formed in 2021 following new EU Exit legislation to take over IFRS responsibilities. Key topics discussed included intangibles, international tax reform, and the connectivity between sustainability and financial reporting. The following month, the ASBJ met with the Financial Accounting Standards Board (FASB) in the US to discuss topics such as accounting for crypto assets and the impact of the international tax reform.

Adoption of IFRS is on the rise

Adoption of IFRS in Japan, though limited to larger companies with global operations, is increasing. In July 2023, a JPX press release showed that the combined number of companies that had adopted IFRS, decided to adopt, or were planning to adopt was 274 companies, with 254 already adopting. Their combined market capitalisation was ¥400tn or 47.3% of the entire listed market cap as of 30 June 2023. Those considering comprised a further 143 companies.

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A few companies adopting IFRS have shifted their year-ends to December

One of the advantages for investors of companies adopting IFRS is that their financial year-ends may move from 31 March to 31 December, thus allowing AGMs earlier in the year and lessening the extreme clustering of meetings in late June. Technically, this would also allow such issuers to hold AGMs beyond the end of March, thus giving themselves more time to prepare and shareholders more time to consider their vote - as is the norm in other developed markets where four- to six-month deadlines for AGMs are common. Few issuers have availed themselves of this option, however, while most of those adopting IFRS have not changed their year-ends to December.

Auditing standards

The audit standard-setting process is becoming more transparent in Japan

Japan has also been making progress in auditing standards. These are formally set by the Business Accounting Council (BAC), an advisory body under the FSA, and developed by a sub-committee of the Japan Institute of Certified Public Accountants (JICPA) called the Auditing and Assurance Standards Committee (AASC). This committee comprises practitioners as well as academics and executives of major companies. JICPA undertook governance improvements to the standard setting process in 2022 and appointed an advisory panel to the AASC. Since January 2021 it has been publishing the meeting minutes and materials of the AASC on its website, although they are only in Japanese.

Japan has filled certain gaps in its auditing standards

In our 2020 survey, we marked Japan down slightly because its auditing standards were not fully converged with the International Standards on Auditing (ISAs). The main exception was ISA 720 on "The Auditor's Responsibilities Relating to Other Statements in Disclosure Documents containing Audited Financial Statements." This was subsequently mandated from fiscal years ending on 31 March 2022.

JICPA issues numerous amendments to auditing standards each year

Japan is committed to closely following ISAs and informs the market about new proposals issued by the International Auditing and Assurance Standards Board (IAASB). Such standards in recent years include ISA 570 on Going Concern, ISA 240 on Fraud, and ISSA 5000 on sustainability assurance. JICPA also has an active programme of issuing amended auditing standards and guidelines for public comment and did so on more than 30 occasions in 2023 - often releasing more than one exposure draft with each press release. It keeps a close eye too on global changes in ethical and independence standards for auditors, as issued by the International Ethics Standards Board for Accountants (IESBA). Standards for auditor independence in Japan are legislated for in the CPA Act, while JICPA has developed a Code of Ethics in conformity with the IESBA International Code of Ethics for Professional Accountants.

Key audit matters

Japan is catching up on key audit matters, but disappointment remains

As noted, the one area where Japan has lagged international developments in auditing reform relates to the use of "key audit matters" in the audit report. Whereas other markets adopted this measure soon after it became a global benchmark in late 2016, Japan only made it mandatory from fiscal years ending on or before 31 March 2021. According to interviewees, there is a consensus that while KAMs have been helpful for investors and encouraged more dialogue between audit committees, auditors, and other stakeholders, they are not providing the value they should. This is in part because the average number per report is just 1.3 - well below the three or more one finds in audit reports in other markets. There also appears to be broad agreement that KAMs in Japan could focus more on whether companies in certain sectors have properly assessed the materiality to their financial statements of major sustainability or climate risks.

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Audit regulation

Japan has had an independent audit regulator since 2004

The other series of questions in our survey on auditing looks at the work of audit regulators. In Japan, this role is taken up by the Certified Public Accountants and Auditing Oversight Board (CPAAOB), which was formed on 1 April 2004 and is a standalone regulatory body (council) established under the FSA. It exercises its statutory authority independently from the FSA.

The CPAAOB does not have the full suite of powers of some other audit regulators

The CPAAOB does not have the full suite of powers enjoyed by independent audit regulators in some other markets. Registration is carried out by JICPA, which also undertakes the bulk of audit-firm quality review inspections each year. CPAAOB then reviews this work and carries out deeper and more targeted inspections as necessary on a select number of mostly larger and mid-sized firms each year (usually around 10 or less). It does not have investigation power, as that is the purview of the FSA, however the latter consults the CPAAOB on its decisions and gives it an opportunity to deliberate and comment on the facts of each case and disciplinary action proposed. Sanctions are then issued by the FSA. Despite this more limited role for the CPAAOB, the involvement of the FSA in investigation and sanction means that this part of the process remains independent of the accounting profession. The CPAAOB does not have authority over standard setting.

Audit registration is being tightened

One improvement in this system in recent years has come in the area of registration. Previously listed-company audit firms, of which there were 125 at the end of June 2022, followed a "self-regulation" system. In May 2022, the CPA Act was amended and a registration system with a stronger legal basis was introduced. This provides for a "firmer gate", meaning that audit firms lacking a proper quality control and business management system will not be registered. Moreover, all registered firms must now apply the Audit Firm Governance Code, formerly only mandatory for large firms.

JIPCA is trying to improve its quality reviews

Another area of change has been in inspections, where JICPA is trying to make its quality reviews more effective. For example, it is taking a more flexible approach to inspections and responding to risks in firms as it proceeds. To free up resources, it has extended the cycle of inspections of major firms from once every two years to once every three years. It is also doing more detailed off-site research before inspections, with the aim of being more effective and targeted. These changes follow earlier criticism from the CPAAOB, which said in 2020 that: "While the quality of the JICPA's quality control reviews is improving, it remains questionable that the progress with the deficiencies identified through reviews is adequately confirmed in the next review. Also, regarding guidance for improvements, although efforts are being made in so far as possible to contribute to the voluntary efforts of audit firms, further inspections regarding the results thereof are necessary."

Enforcement and industry data

Japan scores well for detailed audit enforcement and industry data

Disclosure of enforcement data and industry capacity information is an area where Japan has traditionally scored well in our survey. The CPAAOB not only publishes a useful annual report that summarises its work, including inspections, disciplinary activity and other initiatives, it produces a "monitoring report" that provides more information on its inspection work and describes the structure and capacity of the audit industry in some detail; and another "case report" that includes pertinent case studies of deficiencies found in both individual firm quality control systems and inspections of audit engagements.

It could do better on translating reports more quickly

We have, however, cut scores for two questions (Q6.8 and Q6.9) due to delays in translation of some reports (see the appendix). The last annual report in English for the CPAAOB was published in July 2021, while it took almost nine months to translate the case report for Program Year 2021 (July 2021 to June 2022).

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7. Civil society and media

Japan moved up to 3rd on a score of 66%

After coming equal 4th with Taiwan for Civil Society & Media in 2020, Japan improved its score by four percentage points and rose one rank to 3rd. This was primarily due to higher scores for media coverage of CG policy, regulatory and corporate developments in Japan. We also gave a slightly higher score for the efforts of industry associations to promote CG and for original research carried out by professional and industry bodies. While the score remained high for director training, we reduced it slightly for the involvement of non-profit organisations in CG policy and advocacy.

Media

Media coverage of CG issues in Japan is deepening

Each time we do CG Watch, we find the depth and breadth of reporting and commentary on CG issues in Japan improving. Basic reporting on new regulations and policies is informative and quite detailed, with a genuine effort to cover key facts and to provide a balance of opinion. Tokyo not only has a large domestic media industry, it is also home to several foreign reporters and other writers who take an interest in CG issues. Some of the expert commentary from non-journalists on legal and corporate cases is extremely valuable and of a quality one does not find in most markets in the region. It has also been interesting to see how the use of social media is evolving, with some reporters producing regular updates on key developments.

Specialist publications focus on CG topics too

In addition to the mainstream media, there are also specialist publications that touch on CG developments. One worth highlighting is Shoji Homu, a legal journal that interviewed ACGA in 2023.

Industry bodies

Industry bodies have a range of agendas on CG

We slightly increased the (low) score on this question to reflect the range of pro-CG activities undertaken by business chambers, associations, and investment industry groups. The scoring challenge here is that this is a highly diverse category, comprising numerous entities with different agendas on corporate governance and its importance to Japan. Some organisations are clearly trying to slow down reform, others push it forward as fast as possible. The net impact is, therefore, somewhat limited.

From the conservative . . .

At the conservative end of the spectrum, propounding views that are strongly and consistently pro-management, are the likes of the Japan Business Federation (Keidanren) and the Kansai Economic Foundation (Kankeiren). They seek to play down the importance of new rules and best practices, such as those developed through the revised CG and Stewardship Codes, and play up a more multi-stakeholder, pro-sustainability/ESG/UNSDG line. While many investors might not quibble with the latter, they are less comfortable with explicit attempts to minimise the importance of governance, shareholders, and shareholder returns.

. . . to the more progressive

At the more liberal end of the spectrum are investment-industry groups, both formally constituted legal entities and informal discussion groups. The leading example of the former is the Institutional Investor Collective Engagement Forum (IICEF), an entity formed by the PFA and other major asset owners in 2017 to engage with companies and raise standards of transparency and accountability among listed companies (*see the Investor section above for more details*). Of the informal groups, of which there have been several, the most durable has been the Japan Stewardship Forum (JSF), which comprises many of the country's largest asset managers and gathers for study sessions and discussions several times a year. Both IICEF and JSF contribute submissions to regulatory consultations.

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A range of other business associations seek to play a practical role

In between are a range of established business chambers and industry bodies whose impact varies from minimal to constructive:

- **Japan Association of Corporate Executives** (Keizai Doyukai), which represents individual executives. It is limited in the type of policy statements it can release and we can find nothing on CG in recent years, although it did publish on diversity, equity, and inclusion in June 2023.
- **Japan Audit & Supervisory Board Members Association** (JASBA), the peak body for Kansayaku or "corporate/statutory auditors", whose primary role is to monitor the actions of directors and companies to ensure compliance with laws and regulations. It has an active programme of practical support for its members and in recent times has focussed on how climate and sustainability disclosure issues affect their work.
- **Japan Investment Advisors Association** (JIAA), the peak business body for the investment management industry. It carries out audits of its members to ensure they are complying with laws and regulations, contributes to FSA policy discussions, and has a Stewardship Study Group.
- **Life Insurance Association of Japan** (LIAJ), the peak body for the life insurance industry. It carries out a large annual survey of around 1,200 issuers and more than 200 life insurers to ascertain their views on governance and sustainability topics, and how they interact with each other. It then produces policy recommendations, mostly for companies but also for investors and government, on issues ranging from financial strategies (payout ratios and ROE targets), improving governance, shareholding voting, and ESG initiatives. *(See box below).*
- **American Chamber of Commerce in Japan** (ACCJ). It has a range of member committees that produce "white papers" outlining in detail its official position on major issues, "viewpoints" giving its position on a specific issue, and "public comments" on proposed government policy changes. In August 2023, it published a public comment on METI's new guidelines on corporate takeovers.

An annual LIAJ survey gives insights into corporate and investor perspectives on governance issues

LIAJ insights

One of the most interesting aspects of the LIAJ annual survey is the differing perspectives it gives from companies and investors on governance issues. While issuers see capex as vital in their long-term investment strategies, investors put more emphasis on investment in human resources. In terms of climate-related disclosures, the proportion of companies following TCFD recommendations doubled from 34% in FY2021 to 70% in FY 2022. Yet only 39% of investors use this information in their evaluations of or dialogue with companies. And the survey highlights the contrasting value that each side puts on the performance of external directors. "There is a possibility that investors' evaluation of external directors is low because they have few opportunities to come into contact", the survey says.

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Original research by professional bodies adds to the CG debate

Original research

Japan scores well on our question relating to original research by professional bodies and academics on corporate governance. It comes second in the region after Australia for research on an increased score for the consistency, breadth and depth of this effort.

Two interesting surveys cover IR professionals and statutory auditors

Among professional bodies, two substantive surveys worth highlighting in addition to LIAJ's annual exercise include:

- **Japan Investor Relations Association** (JIRA): An annual survey since May 2000 on the IR activities of listed companies. The most recent was published in April 2023 and focussed on "the degree of progress in responding to the CG Code".
- **Japan Audit & Supervisory Board Members Association** (JASBA): An annual survey on the structure of the corporate auditor (Kansayaku) industry. Key metrics include: numbers of listed companies with Kansayaku boards vs the two other governance systems; the size of these boards and their composition in terms of professional skills; and knowledge levels about auditing, finance, and accounting.

Academic research is even more extensive

Academic research continues to be extensive and timely. While there is not space to give a summary here, a review of the Social Science Research Network (SSRN) website for "Japanese corporate governance" will give a feel for the wide range of papers being produced by both local and foreign professors.

Director training

The quality of director training in Japan is high

Like other leading markets in the region, Japan scores well for the provision of high-quality director training. But unlike other places, its training environment is populated by a plurality of providers not just one main "institute of directors", which is very much the British model.

JACD is the longest established training entity, founded in 2002

The longest established director training body is the Japan Association of Corporate Directors (JACD), founded in March 2002. Its membership comprises executives and independent directors as well as some experts, academics, and institutional investors. JACD runs several training courses from the "Basics" (eight classes over almost five months), "Applied" (case learning over about three months for those who have done the first course or have experience as a director), and "The Chair's Program" (for board and committee chairs by invitation only). It also runs an annual seminar in the winter and offers a free outside director referral service for its members. Every year it gives out its "Corporate Governance of the Year" award to a small number of leading companies - an initiative supported by ACGA.

BDTI was formed in 2009

Another leading educational organisation is the Board Director Training Institute of Japan (BDTI), a "public interest" non-profit formed in 2009. It runs a range of programmes from standard courses that are open to the public and cover the governance basics, such as its "Governance School" and "Director Boot Camp" (in English), to more advanced courses focussing on the role of outside directors or conducting role play based on case studies. They also have a six-session course on "finance for non-finance people" designed for people like Japanese lawyers or engineers. About 40% of the people taking its courses are either directors or about to become directors. Another 40% or so are "executive officers" (shikko yakuin) who are usually sent by their companies because they are in the pipeline for potential appointment to the board. The remainder are individuals. BDTI also organises compliance training for executives, one-day courses tailored to individual

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companies, and seminars on governance trends. All of this is complemented by e-learning packages on company and securities law, and corporate governance. Interestingly, BDTI also provides direct access to CG report data on all listed companies (about 3,600 firms; its "GoToData" service) and an "all-in-one" corporate disclosure "dashboard" that covers the Yuho and voting reports as well and enables users to immediately machine-translate all three key disclosure documents.

BDTI provides figures on directors and others doing its courses

BDTI is also unique in providing the names of companies that have undertaken its one-day courses as well as statistics on the numbers of people being trained each year. Over the past two years, for example, it has seen participation grow from 318 individuals in FY2022/23 to an expected 555 people in FY2023/24, largely the result of scholarships for women and a higher-than-normal demand for customised training for corporations. It roughly estimates that usage of its e-learning package has increased from a tiny 111 users in FY2011 to more than 14,000 in FY2023 (which will end soon), thanks to large corporations using it.

JCGN was formed in 2012 through a merger of three older organisations

A third non-profit entity undertaking director training is the Japan Corporate Governance Network (JCGN), formed in 2012 through a merger of three older organisations working in corporate governance, one of which dated back to 1994 and was responsible for the country's first, albeit private, CG code in 1998. It has a range of individual and company members, runs seminars, workshops and training programmes, and aims to increase "governance literacy of board members" and contribute to "increasing long-term corporate and shareholder value".

It has been training independent directors since 2017

Since 2017, JCGN has been running a governance training programme called "MID" for independent outside directors (MID originally stood for "Master of Independent Directorship", but now just the acronym is used). Sponsored by TSE and JPX, the course follows the CG Code and comprises 18 sessions running over six months. More than 350 people have taken the course to date. JCGN also organises another governance course for board secretariat members - one of the few of its kind in Japan. This runs to eight sessions over four months.

Are these efforts enough?

A fair question to ask is whether all these efforts, as substantial as they are, are enough for Japan's needs? The answer is almost certainly a firm No. While an increasing number of individuals and companies are utilising director training services, such training is not mandatory for sitting or new directors - of which there are well over 30,000 in total across the more than 3,800 listed companies in Japan. Director training is required or expected in several Asian jurisdictions. Moreover, a METI survey in June 2023 found that about 31% of outside directors have less than three years of experience as an outside director at **any** firm, a figure which will not have changed much because the number of outside directors has risen since.

There is a cultural bar to expecting independent directors to undertake training

Moreover, as we found in our survey of listed companies, few issuers provide any tangible information on what training is being undertaken, who is taking it, the detailed content, or who the training providers are. Cultural factors, as noted in the Listed Companies section, also come into play. As BDTI notes, "Influenced by Japan's post-war economic "miracle", it is presumed that those with "management" (ie, top management) experience and an impressive CV must know enough about governance and therefore would make good outside directors." And further: "Even enthusiastic CEOs do not want to "force" outside directors, who think they are qualified, to take training."

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Downgrade watchlist

What to avoid

Factors that could force Japan's market score to fall in 2025:

- Loss of momentum for CG reform at the policy or political level, including any sign of backtracking on current direction.
- Limited follow up to the FSA's Action Programme of April 2023 - or legislative and regulatory reform that fails to provide robust improvements in shareholder rights.
- Loss of momentum for the TSE's cost of capital campaign.
- Loss of momentum for greater gender diversity in boards and management.
- No improvement in CG reporting by companies.
- Institutional investor commitment to CG declines.
- More questionable judicial decisions on takeover defences.

Next steps

Our recommendations for the next stage of CG reform in Japan include the following:

A much higher volume of training is needed

1. **Director training:** There is clearly a need for a much higher volume of board training in Japan. While mandating a set amount of training each year, say 10-15 hours, would be one way to proceed, such an approach runs the risk of becoming a box-ticking exercise like the Continuing Professional Development programmes in many countries. And the current training infrastructure in Japan would probably have difficulty ramping up quickly from a few hundred students each year to many thousands.

   More detailed disclosure by companies of their training should be mandated

   More detailed disclosure of board training by each company might be a better place to start. This should go beyond "comply or explain" disclosure, as currently required under the CG Code, and involve a mandatory requirement to disclose in detail the content of any training, who is undertaking it, and the duration of courses. Inside directors should be encouraged to undertake training as well as senior level executives being prepared for board roles. As one seasoned educator notes, "Inside executives are the easiest to train. All the company must do is order them to take the course and they can easily pay for it." Another agreed that firm disclosure was the way to go: "Many Japanese board members (particularly old boys) would not like to be forced to do something. At the same time, they are very concerned how they are perceived by others. So, my answer is that a strong level of disclosure will work better."

   Training in capital management and finance, among other things, is urgently needed

   In terms of content, it is broadly agreed that directors and would-be directors require training not only in board governance practice and regulation, but capital/financial management, sustainability/climate issues and reporting, and other timely topics such as cybersecurity and human capital management. If such training does not occur, boards at many companies will be left behind and, among other things, the TSE's cost of capital guidance will not achieve its goals.

   The substance of CG reporting needs to be transformed

2. **CG disclosure:** While revisions to the CG Code and amendments to the Yuho have helped to broaden the range of non-financial reporting in Japan, the depth of this disclosure is often shallow. Whether it is board diversity, director training, or the activities of board committees, much reporting remains formulaic and general. As in other markets, in contrast, ESG and sustainability reporting has steadily become more sophisticated and detailed. This is the result of many factors: market, societal, and political pressure; an ever-

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expanding framework of reporting standards; and the urgency of climate change and other environmental crises. Since governance arguably provides much of the foundation for sound corporate decision-making and risk management, this lack of transparency on the CG side of the equation is creating a worrying information imbalance in our view. Thought needs to be given as to how to deepen the substance of CG disclosure.

Cross-shareholdings need to be reduced and explained

3. **Cross-shareholdings:** Financial regulators and investors are keen to see a rapid reduction in allegiant shareholdings. Meaningful disclosure by each company of the rationale for any strategic or financial holdings is necessary. The oversight role of the board needs to be explained, in particular how independent directors approve or advise against such holdings. Is there an independent director committee that reviews all holdings at least once a year? *(For more details and our list of specific recommendations, see ACGA's 2024 letter on allegiant/cross-shareholdings.)*

Despite disclosure duplication, investors are still not getting the information they need before AGMs

4. **Business Report/Yuho:** There has been discussion for many years about the need to merge the Business Report, published several weeks before the AGM and comprising the meeting agenda and explanatory materials, a set of audited annual financials, and a range of non-financial information about the board and business operations. Although quite detailed, this document is not a substitute for the full annual securities report (Yuho) that must be published within three months of the year-end and is typically released after the AGM. Since the Yuho also contains audited financials, auditors must undertake a further audit to check if any material adjustments need to be made.

Investors are being asked to vote without complete information

Japan is unique in having such a duplicative reporting system for listed companies. Not only does it add work for auditors, not to mention cost, it means that shareholders do not receive the full annual report before the AGM yet are being asked to vote without complete and up-to-date information. This problem will only become more acute as the volume of non-financial information being added to the Yuho grows, such as on sustainability, cross-shareholdings, and board activities/performance. In fact, the information deficit doesn't stop here: the CG Report, required under the CG Code, also comes out after the AGM at most companies. And sustainability reports are usually published three months later.

The ideal solution would be one report, comprising the CG and sustainability reports as well

The ideal solution would be one report comprising all required financial and non-financial information published at least three to four weeks before the AGM, giving investors time to digest it. This would also need to incorporate content from the current CG and sustainability reports - or at least ensure that such documents were published at the same time as the Yuho. Meanwhile, listed companies could perhaps receive a waiver from releasing a business report and instead provide their AGM agendas and explanatory materials in its place.

But it may be hard to remove the business report for listed companies

Reducing the importance of, or removing, the business report is seen by most as a non-starter for the simple reason that this would require an amendment to the Commercial Act. It is assumed that the Ministry of Justice (MOJ) would not be in favour, even though this would affect only a few thousand listed companies. Few seem keen to negotiate with the MOJ.

A more elegant solution would be to have companies move to December year-ends

A more elegant solution would be for the FSA to require listed companies - starting perhaps with the top 200 - to shift their year-ends from March 31 to December 31. Then instruct them to delay record dates from year-end to, say, the end of February or March. This would allow them to hold their AGMs up until the end of May or June, thus giving them five to six months from year-end to publish their audited financials, CG Reports, and sustainability reports. In

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other words, the practice in most other developed markets. One can imagine a multitude of objections to these ideas, both practical and cultural. Yet the current situation is becoming untenable and a constructive and creative response is required.

Investors still face challenges attending AGMs

5. **AGM participation**: Another longstanding issue is the challenge that institutional shareholders often face in attending AGMs or EGMs as shareholders, with the right to ask questions and vote in the meeting if they wish. Most institutional shares are held in custodian bank nominee accounts, with the latter recognised as the shareholder of record on the register. Since many companies strictly limit participation to registered shareholders, mainstream asset managers can find themselves barred from meetings - even those who have put forward a shareholder proposal! Or they may be allowed to attend but cannot speak. Given the rising interest in investor stewardship and responsible investment, ways should be found to allow easier participation in AGMs by institutional investors.

It would be helpful if domestic and foreign investors could collaborate on company engagements

6. **Collective engagement:** After a decade of the Japan Stewardship Code, and seven years since it proactively encouraged collective or collaborative engagement, it seems time for domestic and foreign institutional shareholders to explore ways to cooperate more creatively. This is not to suggest individual engagement with companies does not have a place. On the contrary, it is valuable and necessary. But collective engagement achieves many things that individual cannot: it broadens the net to include investors who might otherwise not have the resources to speak to companies one-on-one; it allows for a deeper, richer discussion, since many voices and ideas come to the fore; and it creates huge efficiencies for both companies and investors. The GPIF's survey of companies suggest many more would be open to collective meetings than are currently holding them. And it is hard to see how the aims of the Prime Market restructuring will be achieved if collective engagement remains the exception rather than the rule. Company-investor dialogue needs to be significantly scaled up in Japan.

Company checklist

Actions companies could take over the short to medium term to enhance their governance practices and disclosure include the following:

Actions companies could take to enhance CG practice and disclosure immediately

1. **Composition/structure:** Benchmark board composition, structure and disclosure against global peers and local best practices.
2. **Board reporting:** Ensure reporting on board and board committee activities is meaningful. It should contain sufficient narrative for a reasonable investor to understand what the board and its committees have done during the year, how both inside and outside directors/auditors have contributed, and the key points of discussion and decisions. Disclosure should be specific to the company, not generic, and focus on the year in question. For Kansayaku companies, the name of the chair of any advisory nomination and compensation committees should be disclosed. There should also be meaningful narrative on the relationship between internal audit and the entity it reports to (ie, whether the board, audit committee, or Kansayaku board).
3. **Board leadership**: Appoint an independent chair or lead independent director.
4. **Board diversity policy**: Ensure any policy is meaningful, not generic, and contains sensible targets and action plans. Appoint at least one female director to the nomination committee.

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5. **Director training:** Develop a policy to make training for both inside and outside directors mandatory, focussing on issues and areas where directors' skills are lacking (eg, capital management; sustainability/climate issues; effective engagement with shareholders). Ensure there is an annual budget for training that also covers senior executives in the director pipeline.
6. **Skills matrix:** Define each skill clearly and explain why it is important for the company and how it supports the business strategy and mid-term plan. List each individual director by name and indicate the skills they possess (ie, rather than stating that “X number of directors have Y skill”). Show how the skills matrix is linked to the selection of new directors and helps to shape future board composition.
7. **Board evaluations:** Explain the company's policy for undertaking such evaluations and the process used. Utilise an external consultant at least once every three years, disclose their name, and describe the value they have brought to the process. Disclose the results of the evaluation in some detail and outline action points for improvement. A brief couple of paragraphs summarising such evaluations are rarely of benefit to investors.
8. **Director/executive remuneration disclosure:** Follow global/regional best practice and disclose the exact remuneration (broken down into its component parts) for each director by name and the top five key management personnel in the company.

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Activism crucial for Japan's turnaround

Corporate Japan has vast untapped wealth in cross-shareholdings and net cash. For decades, that was just trapped value. Now the stock exchange and the ministries are working together to apply pressure for an unwind. Scandals added leverage. With share prices above Bubble highs, the decision to unwind is easier. We look at the opportunities created by this accelerating change.

Activism is key to the Japan turnaround story. Activist events are up 156% YoY in Q1. No longer about greenmailing below-book losers, it is now focused on unbundling conglomerates and merging the marriage-shy in industries with diffuse market share, raising Japan's ROE. To understand the trajectory of a trade, investors need to anticipate the exit strategy. We drill down into three winner trades.

CLSA's updated bottom-up CG scores indicate a 2.1ppt improvement in Japanese corporates' governance versus 2020, driven by the fairness and independence pillars. Analysts noted improved board diversity, audit committee effectiveness, chairperson independence, and compensation fairness. We provide the top 10 scorers and improvers within CLSA Japan coverage.

Click to rate this research

The great crossholding unwind (5 April 2024)

Japan's accelerating unwind of cross-shareholdings has taken a jarring leap forward this year. Scandals presented an opportunity to bring pressure to bear on insurers and the Toyota group to unwind their vast, tangled mess of distortive crossholdings.

How did we get in this mess?

Japan got into the cross-shareholding game for the same reasons as Germany

CLSA
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The great crossholding unwind

Since time out of mind, cross-shareholdings and allegiant shareholders had been a feature of the Japanese market. Cross-shareholdings were a feature of other countries that were reduced to penury by defeat in The War. The crossholding structure of much of Europe looked like Japan's. Some still do. Germany, in particular, had many of the same features till the Schroeder government announced in late 1999 that it would abolish the 50% capital gains tax on the sale of crossholdings. Japan's government plans on driving an unwind *without* handing out any more lavish tax breaks: corporate profits booked in Japan are a multiple of 1990 levels, while the corporate tax take has, shamefully, halved over the same period.

Let's look at Japan's post-War story in fast-forward to understand the motivations for the muddle. After the War, the occupying Americans felt the *zaibatsu* conglomerates were responsible for Japan's behaviour and decided to break their power by passing their share certificates to the populace. Back in 1949, retail investors owned 69.1% of the market. Then that ratio plunged.

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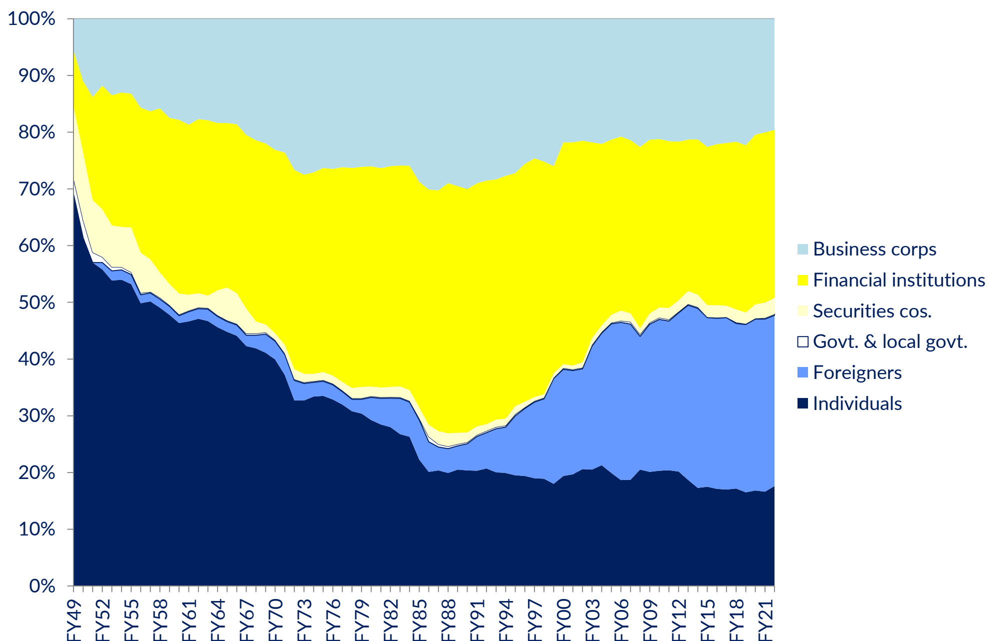
Plunge in retail ownership drives the rise in cross-holdings

Figure 15

Ownership of the Japanese stock market



Note: Data is from our report published on 5 April 2024. Source: CLSA, JPX

Fearing foreign takeover, Corporate Japan circled the wagons - and linked hands

Times were hard, people needed to eat. In two years, that ratio dropped by 12.1ppt. By FY70, it had dropped below 40%; by FY80, it had dropped below 30%; and by FY88, it had fallen below 20%. In March 2023, it was 17.6%. The selling never ended because Japan never developed an equity culture. The stock market fell hard in the post-Korean war slump, so the government reversed the foreigners' law and allowed companies to buy shares in each other to fend off speculators. Then, in 1964, Yamaichi Securities went bankrupt for the first time - and the government orchestrated a price-keeping operation (PKO) for the first time to mop up the brokers' mess. The Bank of Japan (BoJ), with a fund set up by brokers, started buying up stocks. Then, in 1965, the banks had to start buying too. A precondition of Japan's 1964 OECD entry was that Japan deregulate its securities market - so now, for the first time, it had foreigners to deal with too. The PKO funds looked for quiescent shareholders and what they found was the banks.

Moral hazard is habit forming

Moral hazard is habit forming. After the 1980s bubble collapsed, the Ministry of Finance (MoF) used its very substantial supervisory powers to try to bully the banks into halting share sales. Ten years later, in 2002-03, the government had bailed out the banks at vast expense. Understandably, it wanted to make sure it wasn't going to have to do this again, so it told the banks to sell off shareholdings below tier-1 capital. But, like a timid parent, it launched PKO 3.0 to try and cushion the blow. It set up the Banks' Shareholding Purchasing Corporation (BSPC) to buy from banks. Then, in March 2009, it rolled out PKO 4.0, authorising the BSPC to buy not ¥2tn now but ¥20tn.

Crossholdings caused business to ossify

In the early post-War days, banks' shareholdings were useful for debt governance. But since the bursting of the late-80s bubble, 'withdrawal of loan credit' emerged as a threat. When the market went into a downturn, as in the Lehman Shock, bank balance sheets were gutted by falling share prices, impeding their willingness and ability to lend, just when the need to supply liquidity was greatest. Banks were the

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first to come under Financial Services Agency (FSA) pressure to unwind crossholdings. Increasingly, however, other crossholdings came to be seen as "a security pact between incompetent managers". They protected the inept from the consequences of their actions and raised the suspicion of 'giving benefits', which is punishable as a criminal offence. Crucially, they also locked companies into relationships and old ways of doing things, which is kryptonite in an age of dynamic mega competition. If you want to make the jump from internal combustion engines (ICE) to electric vehicles (EV), it is incomparably harder if you have deep capital ties to ICE parts suppliers.

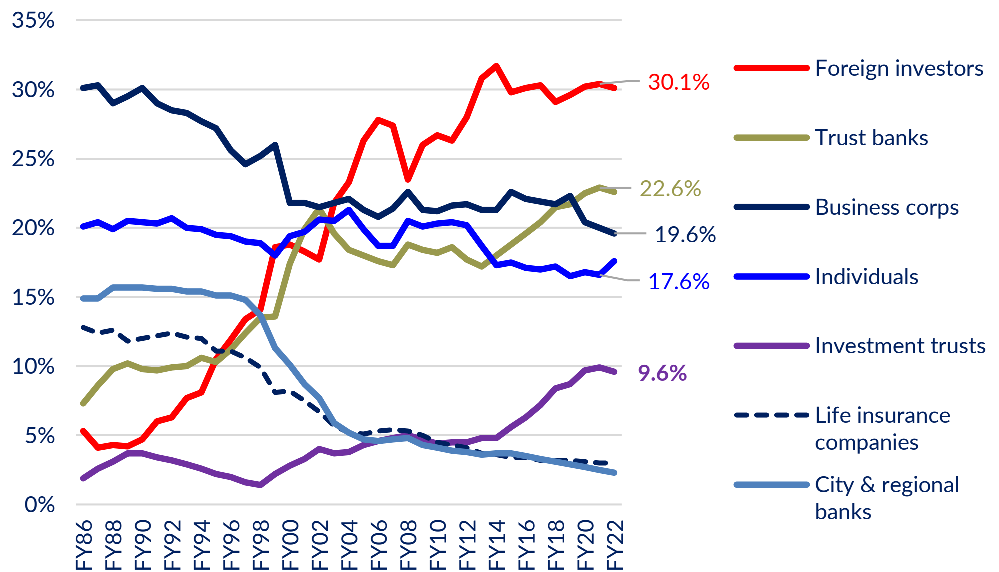
Japan urgently needs to build an equity culture

The upshot is that there were valid reasons for cross-shareholdings, as with Germany. The dramatic collapse in retail ownership was dealt with using a sloppy, biscuit-tin accounting, stopgap response that got out of control. That locked companies into outdated ways of doing things and put the whole financial system at risk. Foreigners have grown to be the biggest owners, but they are often flighty and undependable. They claim to be crusaders for good governance but, as shown in past Benthos reports, vote in line with entrenched management more than domestic funds. Japan urgently needs to build an equity culture.

Flighty foreigners soared to become the biggest owners

Figure 16

Ownership of the Japanese stock market



Note: Data is from our report published on 5 April 2024. Source: CLSA, JPX

Japan's CG push is now about enlightened self-preservation

When Japan talks of corporate governance, it's not of the goody-two-shoes variety: it's enlightened self-preservation. Back in December 2008, the vast governmental retirement fund, GPIF, had 75.9% of funds in domestic bonds and another 7.8% in foreign bonds. With deeply negative real yields, it needed to run, not walk, to get money out of bonds and into equities; it therefore needs those equities to raise their economic returns and it needs them to increasingly share the bounty with shareholders - with dividend hikes and buybacks. Finally, it needs to be able to trust companies not to cook the books. The change in market ownership has already gone a considerable way to passing the reins of power from (often allegiant) stakeholders to shareholders. In FY86, shareholders accounted for under a third of ownership; in FY99 they passed 50%; in FY22 - March 2023 - they passed 70%. Close, but no cigar yet.

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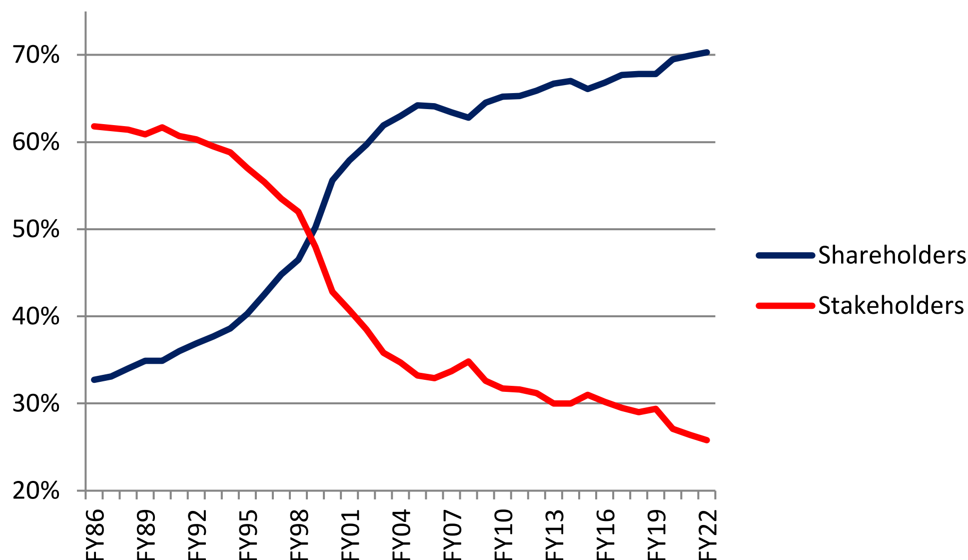
The reins of power are changing hands fast

Figure 17

Ownership of the Japanese stock market



Note: Data is from our report published on 5 April 2024. Source: CLSA, JPX. Stakeholders: city and regional banks, insurance, corporates. Shareholders: trust banks, mutual funds, retail investors, foreigners

TSE asked companies to submit improvement plans

JPX name and shame update

On 31 March 2023, the Tokyo Stock Exchange requested that all listed companies on the Prime and Standard markets should take action to implement 'management that is conscious of the cost of capital'. The aim was to get them to raise returns in order to get their share prices up. The exchange was particularly insistent that companies trading below book made such disclosures. On the Prime market, 40% of companies and 50% of those that trade below book have announced such improvement plans. On the Standard market, 11% of companies and 15% of those trading below book have complied. As described in '*Financial cost of poor governance*' (19 January), all Topix stocks were grandfathered onto the Prime index, but 177 companies later chose to downgrade to Standard because the governance requirements are lower there. Many of those are listed subsidiaries, avoiding the Prime market rule that listed subsidiaries have majority-independent boards, rather than a third on Standard. It's a bit like how developed economies burnish their carbon net-zero climate credentials by offshoring their smokestack industries. The TSE announced 'name & shame' updates for the number of companies that have complied in December, January and February, and it plans to update on the 15th of every month. Prime companies that had complied rose from 660, to 725 to 786.

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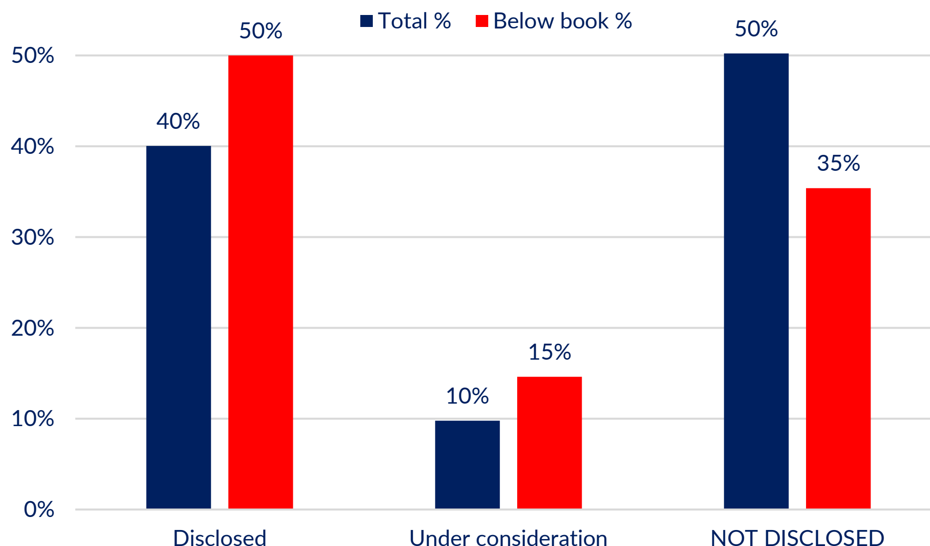
Half of Prime market's below-book companies submitted improvement plans . . .

Figure 18

Prime market: percentage of companies that have disclosed improvement plans

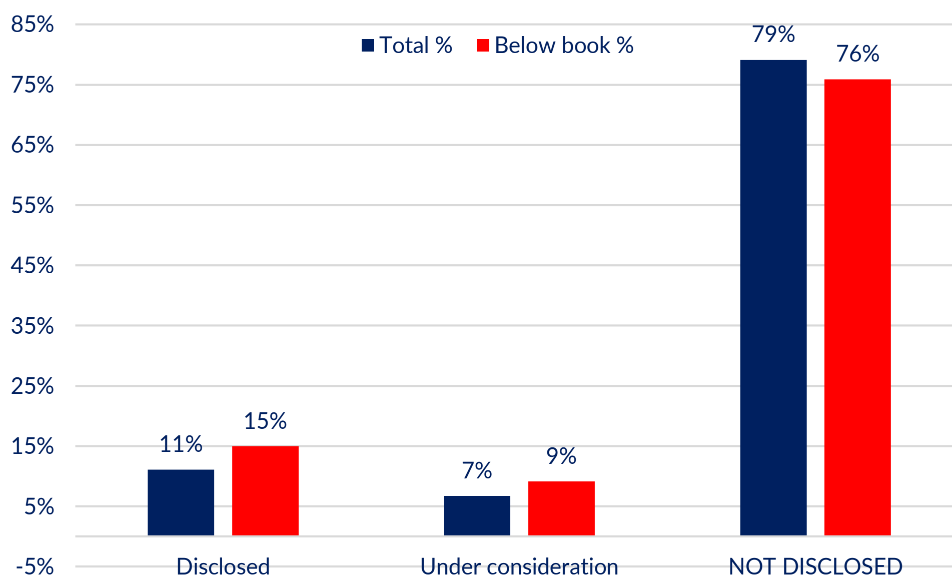


Note: Data is from our report published on 5 April 2024. Source: CLSA, JPX, Bloomberg

. . . but only 15% of below-book Standard market companies have

Figure 19

Standard market: percentage of companies that have disclosed improvement plans



Note: Data is from our report published on 5 April 2024. Source: CLSA, JPX, Bloomberg

As Figure 20 shows, the biggest company listed as not having disclosed is Toyota. Actually, it has disclosed improvement plans in considerable detail, but just not in the way the TSE wanted it laid out. People talk a lot about the issue of loser companies checking the box but not completing the homework, but there are also cases of managers that do the work but treat the checkbox with scant regard. The salient point is that the exercise is making companies think about raising returns in a way many never had before.

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Many majors haven't yet met TSE requirements for improvement plans

Figure 20

Companies that have not met TSE requirements for an improvement plan

Name	Ticker	PBR	Mkt cap (¥bn)
Toyota Motor	7203 JP	1.5	58,930
Keyence	6861 JP	5.9	15,879
Fast Retailing	9983 JP	7.2	14,069
SoftBank Group	9984 JP	1.3	12,536
Recruit Holdings	6098 JP	5.3	10,965
Nintendo	7974 JP	3.6	10,001
Tokio Marine Holdings	8766 JP	2.1	9,435
Oriental Land	4661 JP	8.3	8,552
Mizuho Financial Group	8411 JP	0.8	7,439
Canon	7751 JP	1.3	5,870
Japan Post Holdings	6178 JP	0.5	5,204
Renesas Electronics	6723 JP	2.4	5,028
Mitsubishi Heavy Industries	7011 JP	2.3	4,484
Mitsui Fudosan	8801 JP	1.5	4,466
MS&AD Insurance Group Holdings	8725 JP	1.1	4,407
Terumo	4543 JP	3.2	3,959
ORIX	8591 JP	1.0	3,859
Central Japan Railway	9022 JP	0.9	3,789
Mitsubishi Estate Co Ltd	8802 JP	1.6	3,713
NIDEC CORP	6594 JP	2.2	3,614
Dai-ichi Life Holdings	8750 JP	1.2	3,585
Otsuka Holdings	4578 JP	1.4	3,465
Suzuki Motor	7269 JP	1.5	3,443
Sompo Holdings	8630 JP	1.2	3,137

Note: Data is from our report published on 5 April 2024. Source: CLSA, JPX, Bloomberg

Toyota is a great example of a company that could easily raise ROE

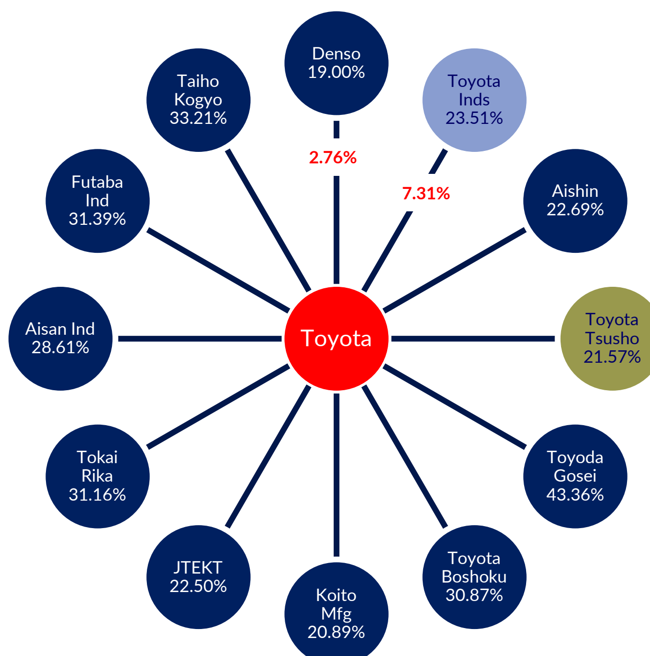
Toyota group's cross-shareholding unwind

Toyota, with its extensive cross-shareholdings, is a great example of a company that could quite easily raise its ROE without much effort.

Only four of these parts companies are core holdings

Figure 21

Toyota holdings in autoparts makers (navy), machinery (light blue) and trading companies (khaki)



Note: Data is from our report published on 5 April 2024. Source: CLSA, Bloomberg

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Toyota has equity holdings worth US$130bn

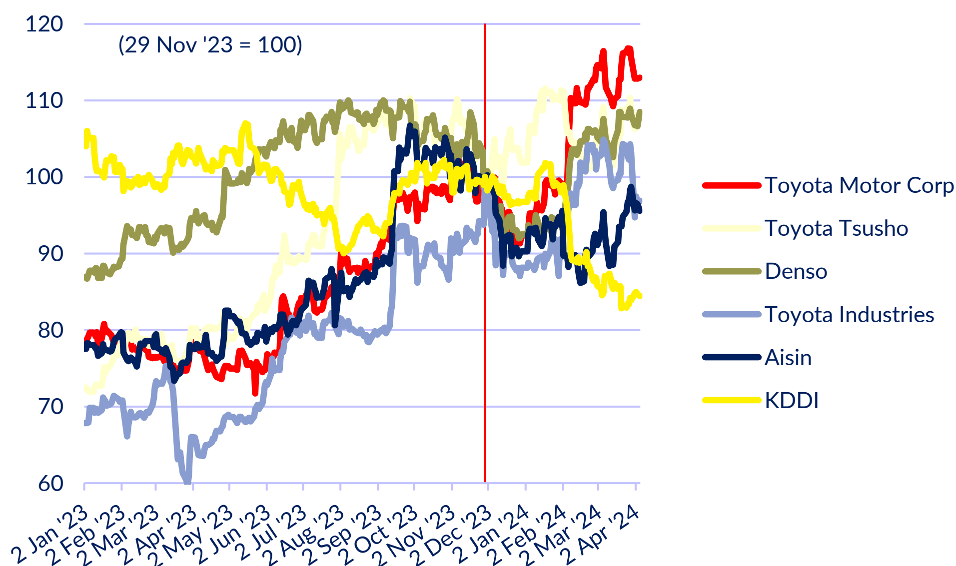
CLSA Toyota Motor
¥2,396 - BUY
Unpacking cross-shareholdings

Toyota has a bloated, 'eclectic' portfolio of 122 stocks worth ¥19.8trn (US$130.3bn). Most of that should be sold off. It includes US$69.4bn of itself - treasury stock accounting for 17.4% of shares outstanding. It should cancel them. The good news is that the unwind has already started, as discussed, at the start of the journey, in Christopher Richter's 14 August report '*Unpacking cross-shareholdings*'. Already, Toyota has started selling down its holding in KDDI, though it still has an 11.0% stake worth ¥1.13trn. Christopher suggests that Toyota's core stocks among the autoparts makers are Denso, Toyota Industries, Aisin Seiki and Toyota Tsusho. Denso and particularly Toyota Industries have large stakes in Toyota that are very large compared to their own market caps, which makes it a lot easier to bring them entirely in-house. It is not clear that it needs to hold on to Toyota Boshoku (seats, door trims and carpets), Toyoda Gosei (resin and rubber parts), Koito (headlights), JTekt (ball bearings) and Futaba (mufflers and exhaust manifolds). The feeling is mutual: Denso has sold its entire stake in three Toyota group companies: Hino, parts maker Toyoda Gosei and Aichi Steel. On 29 November, Denso announced it would buy back 125m shares from Toyota. Toyota Motor, Toyota Industries and Aisin would make a secondary offering from 256m Denso shares. Toyota's stake in Denso is to move from 24% to 20%, remaining an affiliate.

Toyota continues to benefit from the crossholding unwind

Figure 22

Toyota group stocks' performance relative to Topix



Note: Data is from our report published on 5 April 2024. Source: CLSA, Bloomberg

Scandals at group automakers accelerated the focus and unwind strategy

Toyota has stakes in six listed automakers. Daihatsu Motor, which it took over in July 2016, had to halt operations after being found to have falsified safety tests. In 2022, Hino was found to have falsified emissions data for its trucks and is being wedded with Mitsubishi Fuso Truck & Bus. Toyota Industries, tasked with developing diesel engines, was found to have cheated on certification tests. Issues at group automakers have been disrupting supply chains and damaging Toyota's hard-won brand image and quality. It clearly need to concentrate on the core, impose its own tried-and-tested management - and cast off the non-core businesses. When you're not doing what you're good at doing, you're doing what you're not good at doing, and nobody's going to pay you for that. This run of scandals has made Toyota accelerate these changes in its crossholding structure in a way that should significantly benefit shareholders.

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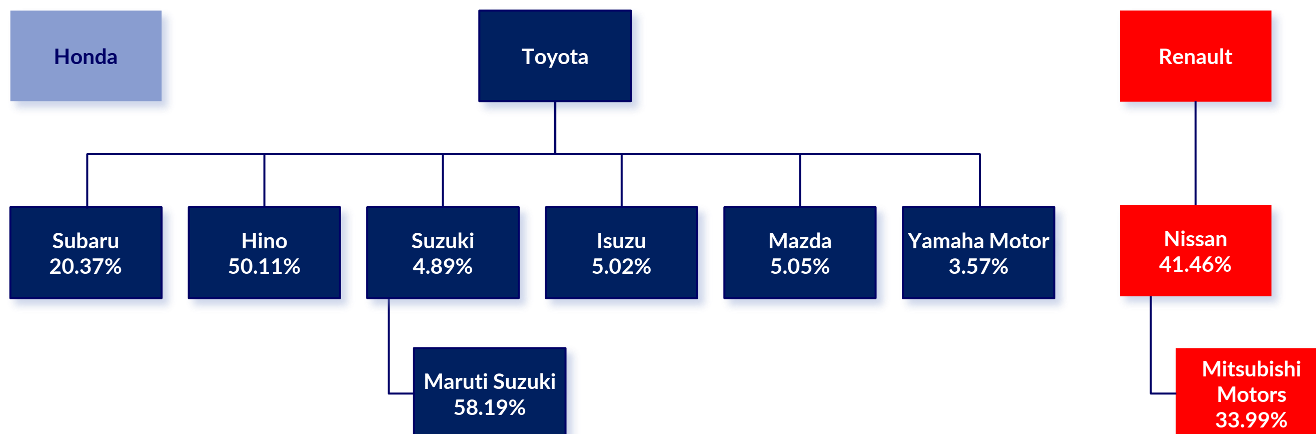
Figure 23

Cross-shareholdings between Japanese automakers



Note: Data is from our report published on 5 April 2024. Source: CLSA, Bloomberg

Casualty insurers went in the sin bin, so FSA made them sell crossholdings

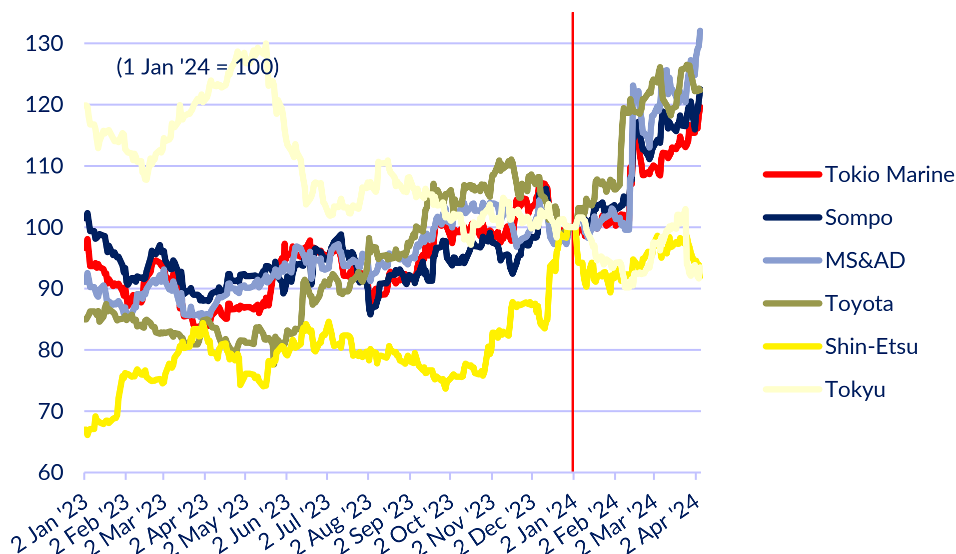
Scandals in the insurance sector trigger crossholding unwind

For a long time, the FSA has been leaning on the banks to unwind their enormous equity holdings. But a price-fixing scandal at the casualty insurers recently gave them a lever to pressure them too to unwind their holdings. They had been colluding to set premiums for corporate clients. Tokio Marine & Nichido Fire Insurance, Sompo Japan Insurance, Mitsui Sumitomo Insurance and Aioi Dowa Insurance together had a combined 5,900 strategic shareholdings totalling ¥6.5trn. The biggest stakes are in automakers Toyota, Honda and Suzuki, trading companies Mitsubishi Corp and Itochu, plus Shin-Etsu Chemical. Sompo says it plans to reduce crossholdings to zero by the end of FY30. Mitsui Sumitomo Insurance and Aioi Nissay Dowa, owned by MS&AD, said they aim to do so by the end of FY29. Tokio Marine hasn't set a date yet.

Insurers have been performing well

Figure 24

Relative performance of the casualty insurers and their biggest holdings



Note: Data is from our report published on 5 April 2024. Source: CLSA, Bloomberg

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High equity holdings + net cash (%) have the greatest unwind potential

Companies with the greatest unwind potential

In FY87, non-financial business corporations owned a peak of 30.3% of the market. By March 2023, that number had fallen to 19.6%. It needs to go a lot lower. It's not all cross-shareholdings; some of it is parent holdings in listed subsidiaries and affiliates. Holdings are broken into strategic holdings and shares available for trading. Companies can easily reclassify them to get around rules created by the proxy voting companies, such as Institutional Shareholder Services (ISS), about how much equity holdings are allowed to be as a percentage of the balance sheet. Figure 25 looks at Topix-500 companies where the total of equity holdings plus net cash is a large percentage of market cap.

Figure 25

Topix-500 companies where equity holdings plus net cash are a large percentage of market cap

Name	Code	Equity holdings, mkt value (¥bn)	Treasury stock, mkt value	Equity hdgs less treasury stock	# hdgs ex-treasury	Hdgs as % equity	Hdgs as % mkt cap	Net debt (cash) as % mkt cap	Net cash + eqy hdgs % mkt cap
SoftBank Group	9984 JP	31,848	19	31,829	72	272	247	102	**144**
TBS Holdings	9401 JP	1,016	16	1,000	40	105	134	(10)	**144**
TV Asahi Holdings	9409 JP	248	6	242	21	59	109	(34)	**143**
GungHo Online Entertainment	3765 JP	111	65	46	1	31	34	(103)	**137**
Suzuki Motor	7269 JP	4,471	62	4,408	64	154	129	(6)	**136**
Keisei Electric Railway	9009 JP	1,713	53	1,660	21	372	164	36	**128**
GMO internet	9449 JP	380	8	371	9	215	127	25	**103**
Kansai Paint	4613 JP	410	0	410	57	103	90	(9)	**99**
Toyota Industries	6201 JP	5,853	228	5,625	49	114	124	27	**98**
Medipal Holdings	7459 JP	304	26	278	47	39	57	(38)	**95**
Nissan Motor	7201 JP	769	13	756	10	12	33	(53)	**87**
JGC Holdings	1963 JP	48	27	20	30	5	5	(79)	**84**
DMG Mori	6141 JP	503	2	502	9	184	98	20	**78**
Takara Holdings	2531 JP	112	2	110	38	39	54	(22)	**76**
Sankyo	6417 JP	75	65	10	6	4	3	(73)	**76**
Suzuken	9987 JP	68	0	67	46	16	19	(54)	**74**
Kaken Pharmaceutical	4521 JP	49	28	21	24	15	16	(54)	**71**
Mochida Pharmaceutical	4534 JP	24	6	18	21	14	16	(55)	**71**
DeNA	2432 JP	93	18	75	2	35	41	(29)	**70**
Dai Nippon Printing	7912 JP	861	247	614	70	52	59	(11)	**69**
House Foods	2810 JP	158	12	146	53	45	49	(20)	**69**
Hisamitsu Pharmaceutical	4530 JP	94	37	58	61	21	20	(46)	**65**
Kyocera	6971 JP	1,777	201	1,576	22	50	57	(6)	**63**
Stanley Electric	6923 JP	142	30	112	19	20	25	(36)	**61**
Taisei Corp	1801 JP	419	1	418	61	47	40	(20)	**60**
Nippon Television Hdgs	9404 JP	269	2	268	26	29	44	(14)	**58**
TS Tech	7313 JP	31	16	15	14	4	6	(51)	**57**
TOPPAN INC	7911 JP	470	44	426	66	28	35	(22)	**56**
NOK	7240 JP	188	11	176	61	30	51	(4)	**55**
Taisho Pharmaceutical	4581 JP	151	27	125	31	15	18	(36)	**53**
Kokuyo	7984 JP	73	21	52	30	21	18	(34)	**52**
Wacoal Holdings	3591 JP	111	21	90	38	43	46	(4)	**50**

Note: Data is from our report published on 5 April 2024. Source: CLSA, Bloomberg

Softbank Group is a standout for its holdings of ARM, Alibaba, Softbank Corp and T-Mobile. Television companies are a major feature of the list, but they are protected by the Broadcast Law (1950), which limits foreigners' holdings to 20%. That limits an activist's ability to be a credible threat. Hibiki Path currently has a position in TBS Holdings, where Whitebox Advisors, Value Square and AVI have been there in the past. Kuri RMB Capital has tried with TV Asahi. Third Point has tried with Suzuki. Palliser currently has a stake in Keisei Electric, trying to persuade it to sell down its large and profitable position in Oriental Land; Elliott is trying the same with Mitsui Fudosan. Oasis had a position in GMO Internet. Then, toward the

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bottom of the list, Elliott had a position in Dai Nippon Printing. Dalton currently has a position in Hisamitsu Pharmaceutical. Oasis has one in Kyocera. Finally, Curi RMB Capital, Oasis Management and Japan Catalyst have filed positions currently operative in Taisho Pharmaceutical. There's already a wolfpack of activist companies pressuring them to release trapped value. That pressure seems only likely to intensify.

The unwind of Japan's vast cross-shareholdings continues to accelerate

The unwind of Japan's vast cross-shareholdings continues to accelerate. The rise in share prices makes selling them easier. With the market near or above Bubble highs (depending on whether you look at Topix or Nikkei), there is no longer the problem of selling at bargain basement prices. In almost all cases, there should be very considerable profits to realise. Governmental pressure being put on prominent companies to sell all crossholdings makes it easier to make the case that target companies should do likewise. There's a lot of trapped value to release.

Does activism work? (29 March 2024)

Activism is crucial to Japan's turnaround story; no longer nano-cap greenmailing

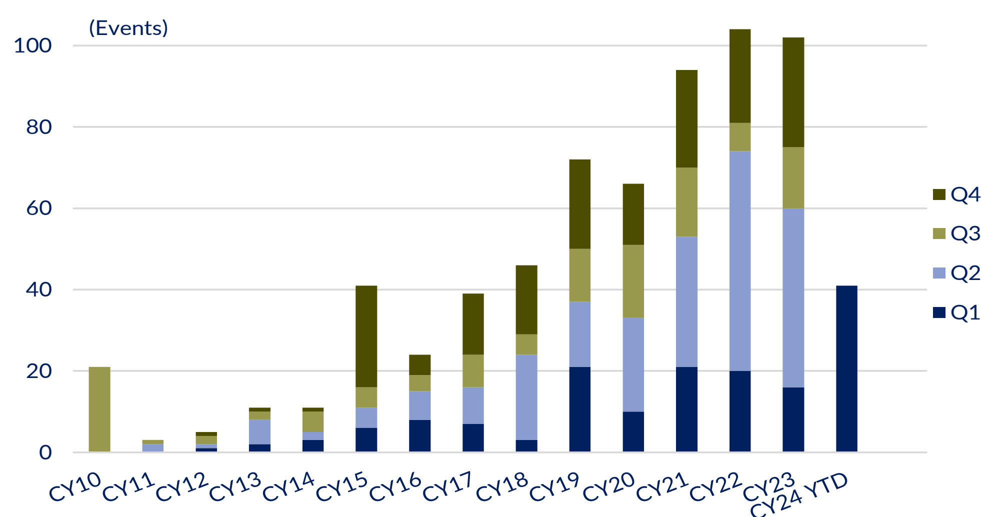
Japan had an adversarial relationship with activists: not any more. Activism is no longer about greenmailing below-book, cash-bloated companies - micro-caps that don't now move the needle. It is now about unbundling directionless conglomerates and agitating for mergers in mature sectors with diffuse market share: both are critical issues for the Japan turnaround story. Prominent activists have demonstrated leaving companies in better condition than they found them, so have government support. Understanding the exit strategy is key.

Activist events in 1Q are up 156% YoY

Activist events in Japan in 1Q are up 156% YoY, already at 40% of last year's total.

Figure 26

Japanese activist event counts



Note: Data is from our report published on 29 March 2024. Source: CLSA, Bloomberg

Last year, Benthos predicted that activist events would hit new highs in 2024. The privatisation of Toshiba was set to release a lot of activist money that would need to be put to work. Multiple expansion in other markets had left Japan - now the world's second-largest activist market - looking particularly inviting. Improving governance, through activism and plain vanilla engagement, is a crucial part of the Japanese equities story.

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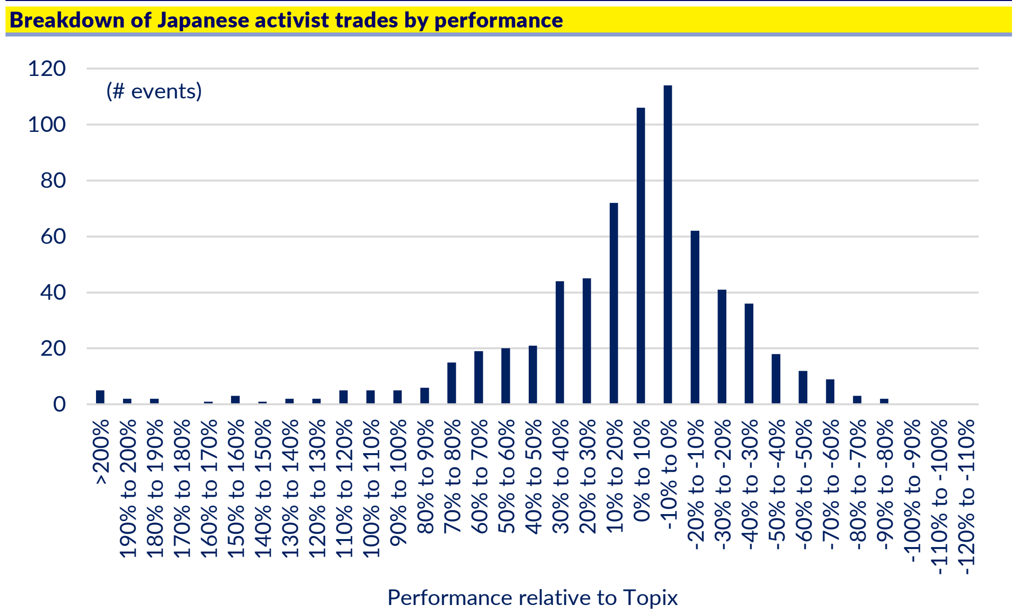
Median relative performance for activist trades over US$2bn is 0.0%

The median relative performance for Japanese activist trades is 3.6%; for those with market caps over US$2bn at inception, it is 0.0% - not much given the risks associated with such large position sizes. You can see in Figure 27 that the biggest group is those with *under*performance of up to 10%; 44% of trades underperformed. The range, however, is huge. Your risk isn't the actuarial risk. There's a group of activists you repeatedly see at the top, and a different set of names that frequently lose money on trades. Currently, the most profitable trade outperformed by 310%; of those over US$2bn market cap, the number to beat is 156%.

Your risk isn't the actuarial risk: the range of outcomes is huge

Figure 27

Breakdown of Japanese activist trades by performance



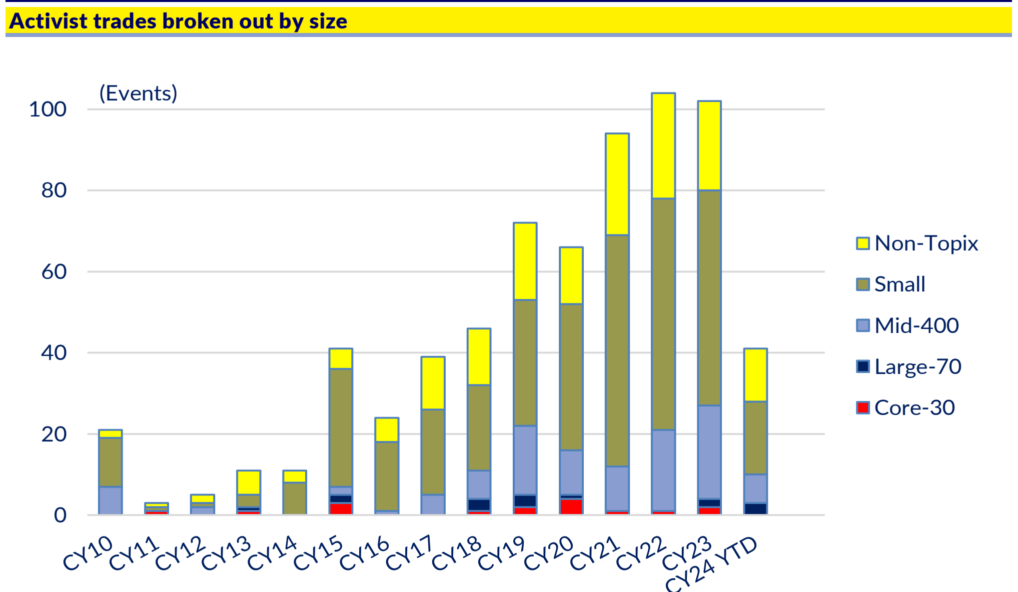
Note: Data is from our report published on 29 March 2024. Source: CLSA, Bloomberg

Overwhelmingly, the targets have been extremely small, but that's changing fast.

Most activist targets are tiny, though that's changing fast

Figure 28

Activist trades broken out by size



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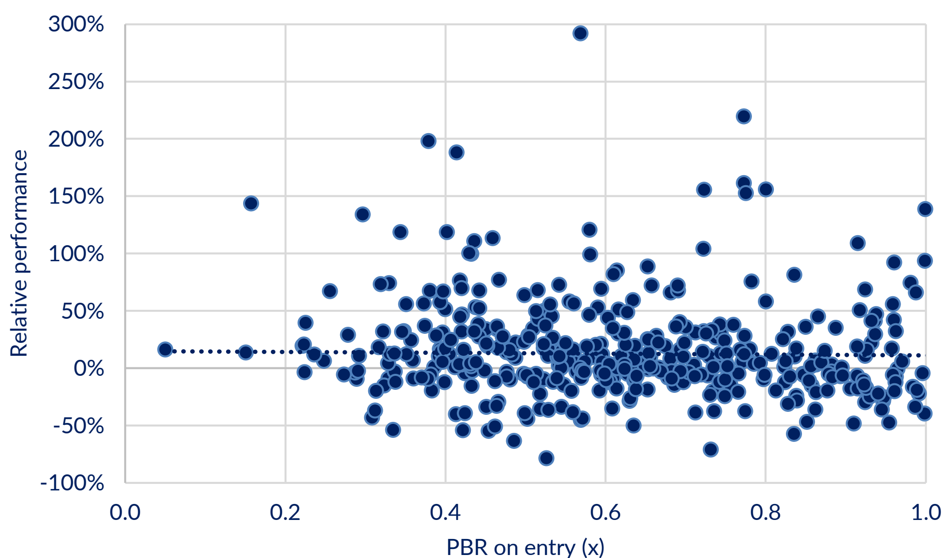
Just because it trades below book doesn't mean it'll outperform

Just because a stock is trading below book - or even tangible book - is absolutely no guarantee of success. However much a company spent on its factory, if nobody wants to buy the product any more, the plant may well be worth nothing - minus the cleanup costs. The average activist target traded at 1.24x book on entry.

Figure 29

Relative performance of targets trading below book on entry



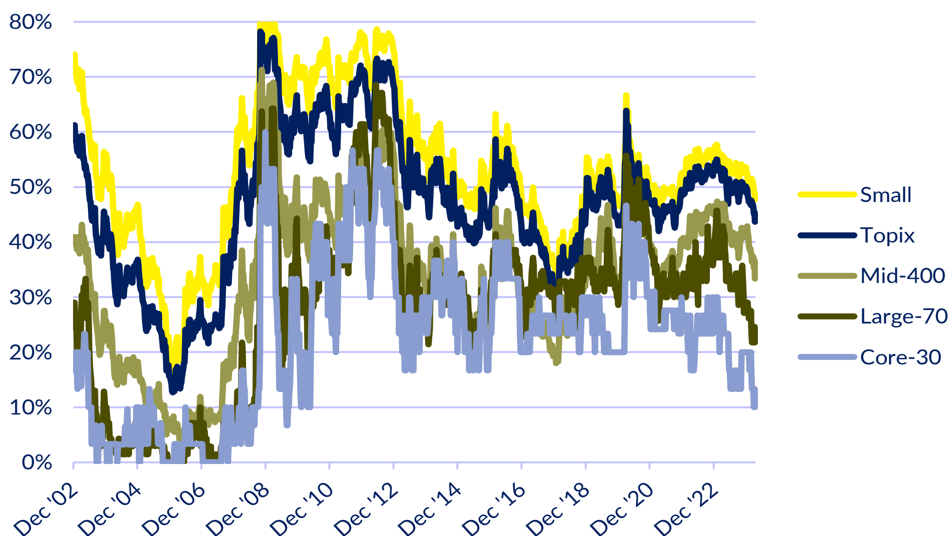
Note: Data is from our report published on 29 March 2024. Source: CLSA, Bloomberg

Nowadays, trading below book is mostly an issue of tiny companies

Activism in Japan has changed a lot. The focus used to be just finding companies that both trade below book and have lots of cash, then demanding they buy back shares - essentially, greenmailing. That's getting harder and harder to do outside the small and nano-cap space. Currently, 84% of companies trading below book are on Topix Small - so, outside the top 500 companies. The ultra-cash-rich companies are also mostly very small.

Figure 30

Percentage of Topix companies trading below book, by company size



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Focus has moved to unbundling conglomerates and agitating for mergers

But the activists have got bigger too, and the rise of Japan to become the world's second-largest activist market has brought the global leviathans into the market. Small cap trades don't move the needle for them. Increasingly, activist investing has had to move on to new strategies. One new focus is unbundling conglomerates. Seven & I is a great example: it has a great business - convenience stores - and a far less attractive business, Ito Yokado. Another major focus has been finding industries with diffuse market share and brokering (often shotgun-) marriages between them. Activism that leaves a company better than they found it makes the activist attractive to governmental bodies: greenmailing doesn't.

A small number of names dominates the upper echelons of performance

The table below shows the top-performing activist trades, continuing through 28 March if the trade hadn't been exited. The list of fund names is somewhat different if you look exclusively at larger targets over US$2bn. But if you can put up performance numbers of this kind, you are likely to grow a lot bigger. This report is going to look a little deeper at three trades that are still in play: papermaker Hokuetsu and phone-cracker Sun Corp both from Oasis, plus Effissimo's blowout trade in shipper Kawasaki Kisen.

Figure 31

Top-performing Japanese activist trades

Name	Ticker	Fund	Perf. Rel. Topix (%)	PBR at outset (x)	Mkt cap at outset ($m)
EM Systems	4820 JP	United Managers Japan	310.3	1.2	116
Kawasaki Kisen	9107 JP	Effissimo Capital Management	291.9	0.6	1,365
Sun Corp	6736 JP	Oasis Management	239.9	1.6	169
Japan System Techniques	4323 JP	MIRI Capital Management LLC	228.2	1.2	83
Dream Incubator	4310 JP	United Managers Japan	219.6	0.8	76
CyberAgent	4751 JP	Taiyo Pacific Partners LP	199.8	2.2	1,083
Gamecard-Joyco Hdgs	6249 JP	Tower Investment Management	198.1	0.4	162
PeptiDream	4587 JP	Taiyo Pacific Partners LP	187.3	20.0	1,221
Hokuetsu Corp	3865 JP	Oasis Management	174.4	0.4	874
Dream Incubator	4310 JP	Varecs Partners	157.1	0.8	76
Nintendo	7974 JP	Oasis Management	156.0	0.8	14,262
Uchida Yoko	8057 JP	Strategic Capital Inc/Japan	155.5	0.7	268
Kito Corp	6409 JP	Misaki Capital Inc	152.8	0.8	214

Note: Data is from our report published on 29 March 2024. Source: CLSA, Bloomberg

Effissimo had to endure K-Line underperforming for years before it took off

Kawasaki Kisen: Effissimo and the patience of Job

Japan has three major shipping companies and a long tail of smaller players. Kawasaki Kisen, or K-Line, was the third of those three. Effissimo, a fund composed of former team members from the Murakami Fund, actually first triggered a filing as a holder of K-Line shares back in August 2015. It didn't file that it 'might make important proposals' till November 2018, which is when the Benthos database treats the trade as starting. Between those two dates, it underperformed Topix by 42%. By the lows in March 2020, it had underperformed another 43%, as Figure 32 shows. From then, it shot up, outperforming over 500% to June 2022 and Effissimo filed its first sale of the stock in November 2022. The Benthos database counts that as the end of the trade - because of the need to have a constant definition. But Effissimo started buying again, taking its position back up to 38.5% and the stock had another run to relative highs in January 2024, by which time it had outperformed 1,028%. It took its stake from 36.60% to 38.52% with the reporting obligation triggered on 27 December. Then on 22 March, it filed a form saying it 'might make important proposals'. That could be an official AGM proposal, though it could also be related to private discussions. As yet, there has been no public disclosure what those proposals might be.

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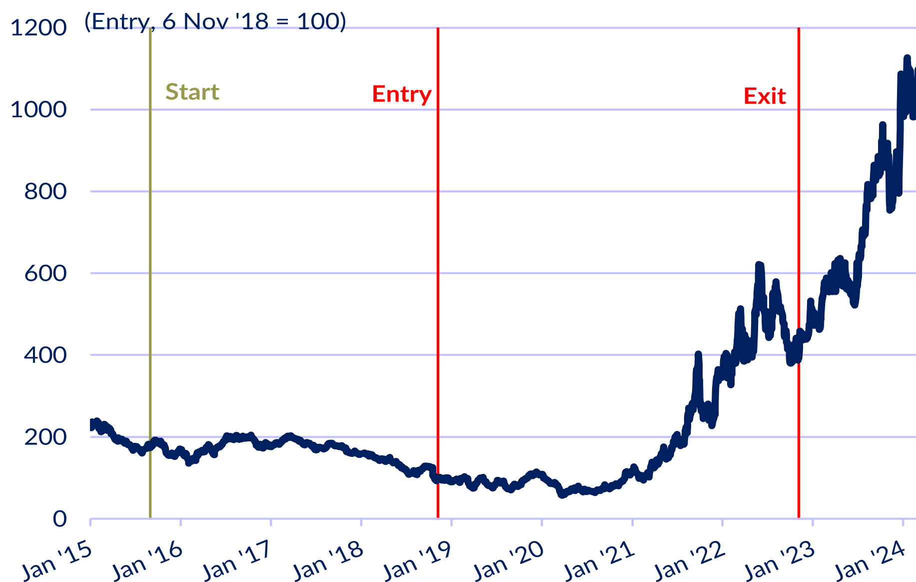
It required the patience of Job, but this is likely Japan's most successful activist trade

Figure 32

Effissimo's involvement in Kawasaki Kisen: performance relative to Topix



Note: Data is from our report published on 29 March 2024. Source: CLSA, Bloomberg

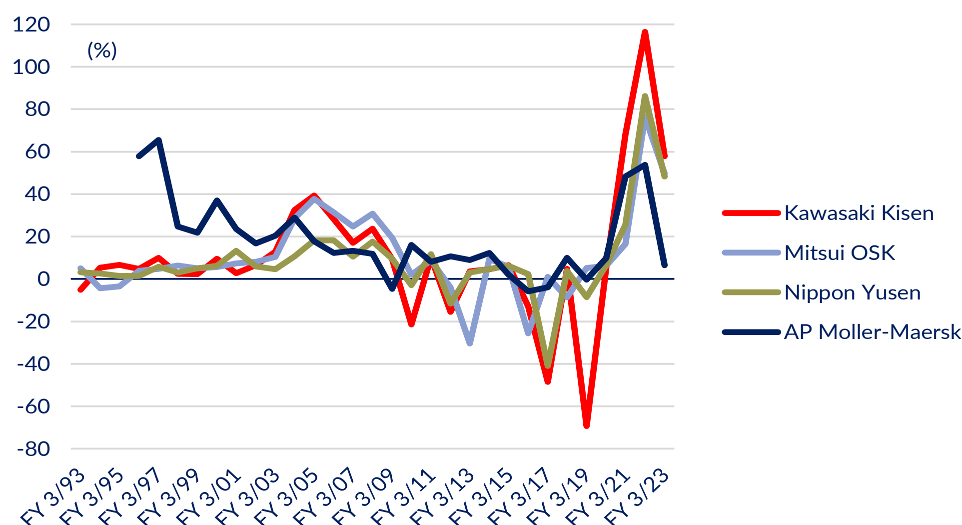
Containership merger was a major driver of the profit turnaround

As Figure 33 shows, the turnaround in performance at K-Line was particularly dramatic, with its ROE bottoming out at minus 69% in FY3/19, exploding upwards to plus 117% in FY3/22. Even in FY3/23, it was above the FY3/22 cyclical peak of global number one Maersk. To be fair, it's easier to achieve high ROEs after smoking 61% of your equity, as K-Line did between FY3/15 and FY3/19. But operating margins also got dramatically better. A major driver of that turnaround was the merger of its container shipping business with those of Japanese peers, Nippon Yusen and Mitsui OSK. The new company, Ocean Network Express, or ONE, was established in July 2017. Even that only won it global share of 7%, against Maersk's almost 20%. From the start, Mitsui OSK president Junichiro Ikeda said it would take about three years for the integration to take effect.

Turnaround of K-Line's ROE was dramatic, even compared to peers

Figure 33

ROEs for shippers



Note: Data is from our report published on 29 March 2024. Source: CLSA, Bloomberg

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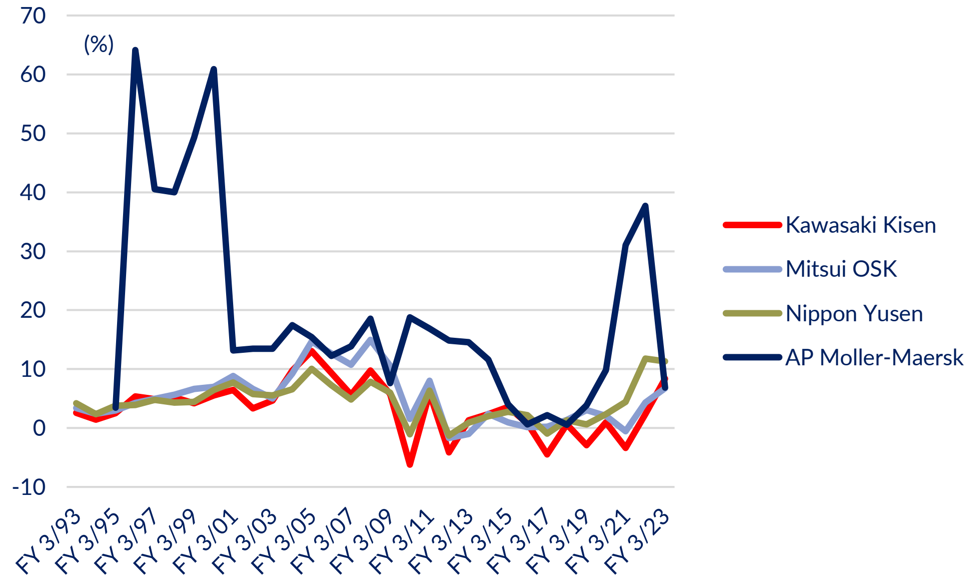
Operating margins also improved considerably

Figure 34

Operating profit margins for shippers



Note: Data is from our report published on 29 March 2024. Source: CLSA, Bloomberg

Combination of crumbling yen and higher shipping rates helped a lot

It helped that global shipping rates exploded upwards: the Shanghai container index bottomed in April 2016 and rose 467% to its February 2022 highs; the Baltic Dry Bulk index rose 1800% between February 2016 and October 2021. Of course, Japanese shippers also benefited in a big way from the collapse of the yen, which has yet to reach a clear inflexion point. The business is deeply cyclical, and the Halcyon days of 2022 have passed, but the consensus seems reasonable in forecasting earnings to hold up at FY3/21 levels or better.

Pricing improved considerably during Covid

Figure 35

Shipping rates

Note: Data is from our report published on 29 March 2024. Source: CLSA, Bloomberg

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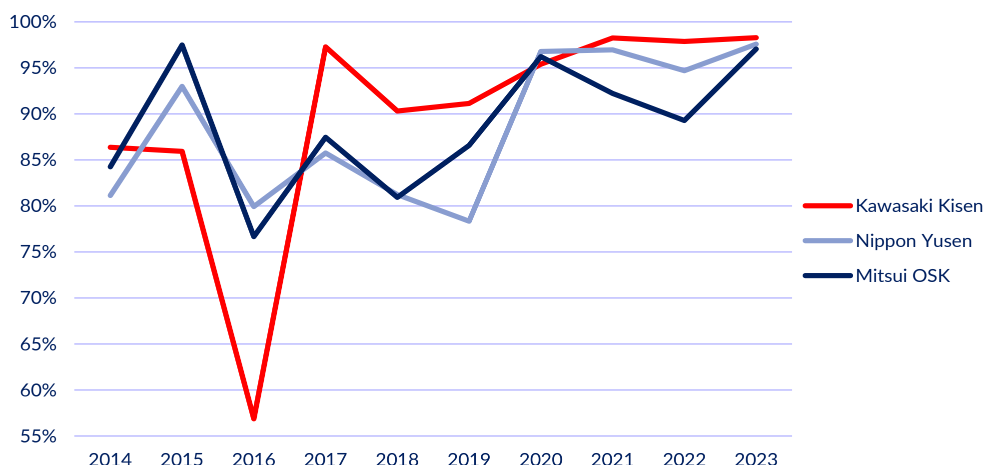
What's needed isn't JVs but full merger catalysed by activists

But the merger of the container shipping businesses in 2017 was a long way from being a marriage of the three companies' whole businesses - more like friends with benefits. The global giants are much more focussed on one business, such as Maersk's tight focus on container shipping. K-Line owns fleets in dry cargo bulk carriers, container shipping, LNG carriers, Ro-Ro ships, tankers, as well as running container terminals. Its two domestic peers aren't very different. Clearly, what is needed is a merger of the three or, at the very least, an exchange of assets to make each of them more focussed in core businesses, with greater scale. In June 2016, when Effissimo voted against re-election of K-Line CEO Eizo Murakami, his support collapsed to just under 57%. On 31 October 2016, the three shipping companies announced the container shipping merger ONE. In the June 2016 AGM, Murakami's re-election support roared back up to 97%, despite proxy giant Institutional Shareholder Services (ISS) recommending voting against. Effissimo held a 38.4% stake as of the record date for the 2017 meeting, up from 29.7% the year before.

Effissimo has made K-Line CEOs abundantly aware of its ability to oust them

Figure 36

AGM re-election votes for shipping company bosses



Note: Data is from our report published on 29 March 2024. Source: CLSA, companies

Exit through merger or risk shares slumping when the cycle turns down

CEO Murakami loudly proclaimed, when asked, that K-Line had not consulted with Effissimo about the merger; pressure from Effissimo had nothing to do with it. It's never quite clear why Japanese companies are so keen on proclaiming they don't listen to their shareholders - but they take a pride in listening to their customers. The current CEO, Yukikazu Myochin, doubtless is now deeply conscious that an 8% ROE is the least Effissimo will accept. Effissimo retains a 38.52% stake in K-Line and hasn't shown up on the registers of Mitsui OSK or Nippon Yusen. But its most logical exit from the vast stake would be selling it to an industry peer - a prelude to M&A. And the only way to avoid a slump in the share price when the cycle ultimately turns is to agitate for a merger. Thinking through possible exits is crucial to understanding the trade. This industry is surely going to consolidate - and probably soon.

Hokuetsu: Oasis and Warring States

Paper's a mature industry where activism is needed to force consolidation

The pulp & paper sector is a highly domestic industry that reached maturity and started declining 20 years ago, without really passing through the shakeout stage. It has diffuse market share and hence returns well below the cost of capital. It is desperately in need of consolidation, and Oasis' investment in Hokuetsu is likely to have a domino effect on the rest of the industry, catalysing M&A. Activism and engagement is necessary to force consolidation among companies that don't like, trust or respect each other very much.

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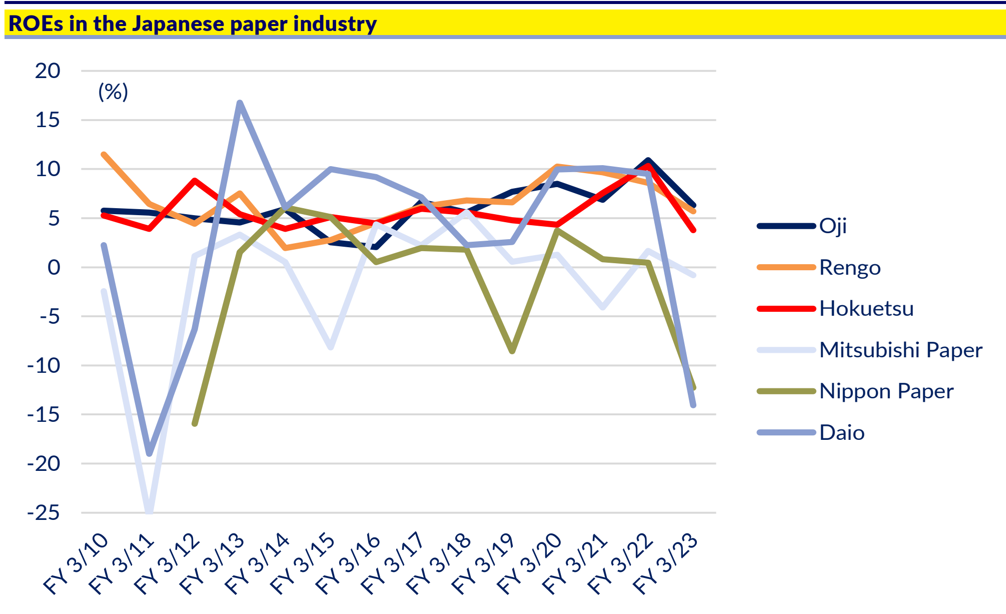
Japanese paper industry suffers diffuse share and poor returns

Figure 37

ROEs in the Japanese paper industry



Note: Data is from our report published on 29 March 2024. Source: CLSA, Bloomberg

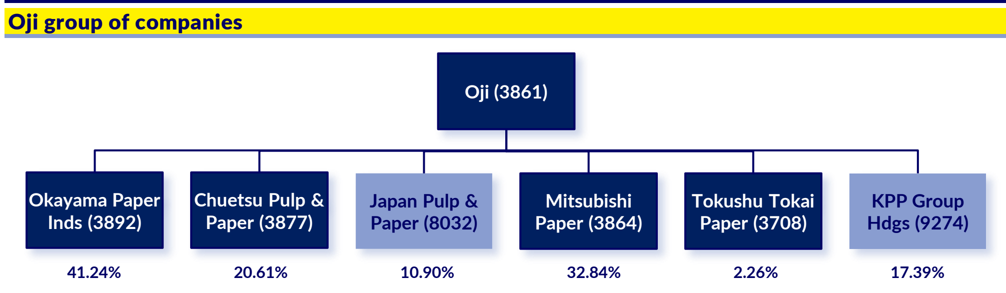
Story starts with Oji's attempt to acquire Hokuetsu in 2006

When Hokuetsu announced plans for a highly efficient new production line in Niigata in 2006, market leader Oji Holdings launched Japan's first hostile bid by an established group for a rival on 23 July 2006. The stated logic of the acquisition was that acquiring Hokuetsu's efficient plant made it easier to shutter less efficient plants, raising capacity utilisation. Hokuetsu quickly brought in white knights with a 24% stake from Mitsubishi Corp and 10% from Nippon Paper - both of which have since been unwound with little obvious benefit for the buyers. Oji's 34% premium had been attractive, the rationale clear. The objections seemed to revolve largely around parochial pride, not price. Hokuetsu implemented a poison pill and sought an alliance with a Korean peer. Oji admitted defeat in a 29 August press conference and officially bowed out on 5 September. Oji has since bought less-than-controlling stakes in a number of other industry players as well as paper wholesalers, but industry consolidation has not really proceeded, while industry conditions have worsened as demand continues to fall. Just as in the oil refining industry, consolidation makes it easier to close less efficient plants and raise ROE.

Oji has since acquired less-than-controlling stakes in a large number of peers

Figure 38

Oji group of companies



Note: Data is from our report published on 29 March 2024. Source: CLSA, Bloomberg. Wholesalers in light blue

That leaves Hokuetsu and Daio, plus two other major isolates, industry leader Nippon Paper and box maker Rengo. Former Daio chairman Mototaka Ikawa was convicted of misappropriating ¥5.5bn of company money to gamble in foreign casinos. The resulting scandal caused a catastrophic rift in the board in 2012, which caused the Ikawa family to sell a stake of over 20% in Daio to Hokuetsu. That made

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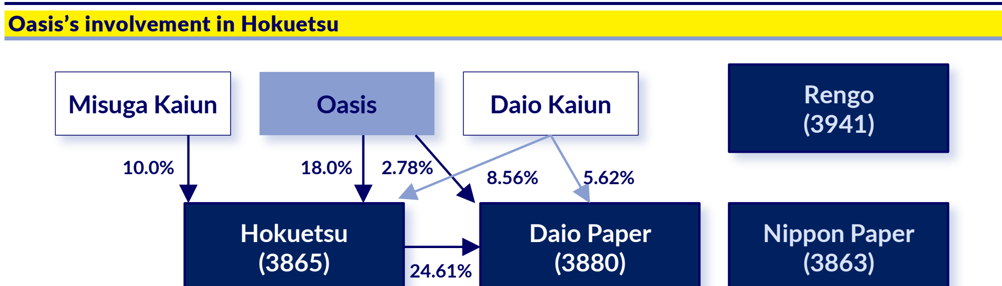
Daio an equity-accounted affiliate. Relations are frosty after Daio issued a convertible bond in 2015 that drove down Daio's share price by 30%, damaging Hokuetsu's balance sheet. Hokuetsu sued them that December. Daio Kaiun in Figure 39 represents Daio Paper's ousted founding family, the Ikawa family; Misuga Kaiun is a Daio Kaiun group company. On 22 December 2023, Hokuetsu announced a poison pill that would be triggered if Daio Kaiun and group companies continued raising their holding to above 20%. However, between Oasis and the Daio Kaiun group they own 36.56% of Hokuetsu. How can you exit such large positions without offloading into an M&A deal?

Between Oasis and Daio Kaiun, they own 36.6% of Hokuetsu

Figure 39

Oasis's involvement in Hokuetsu



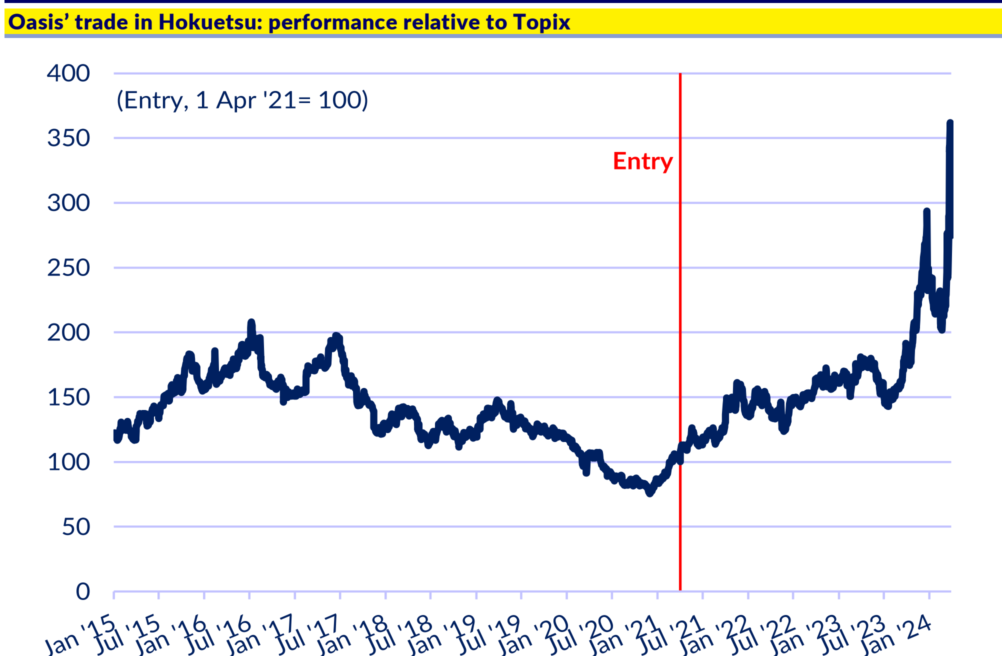
Note: Data is from our report published on 29 March 2024. Source: CLSA, Bloomberg

Oasis showed up as a shareholder of Hokuetsu on 1 April 2021, though buying started on 25 January that year. At the time, it was trading at 0.4x book and had large unrealised gains on its holding in Daio Paper. Since then, Daio's shares have collapsed, but Hokuetsu's shares have surged, taking it to 1.6x book.

Since Oasis initiated a position in Hokuetsu, the shares have surged

Figure 40

Oasis' trade in Hokuetsu: performance relative to Topix



Note: Data is from our report published on 29 March 2024. Source: CLSA, Bloomberg

Plants may not be worth their book value

Capacity utilisation has collapsed in the paper industry. January utilisation was lower than at the nadir of the global financial crisis. Clearly, significant amounts of capacity needs shuttering. That might well mean that book is overstated for many players.

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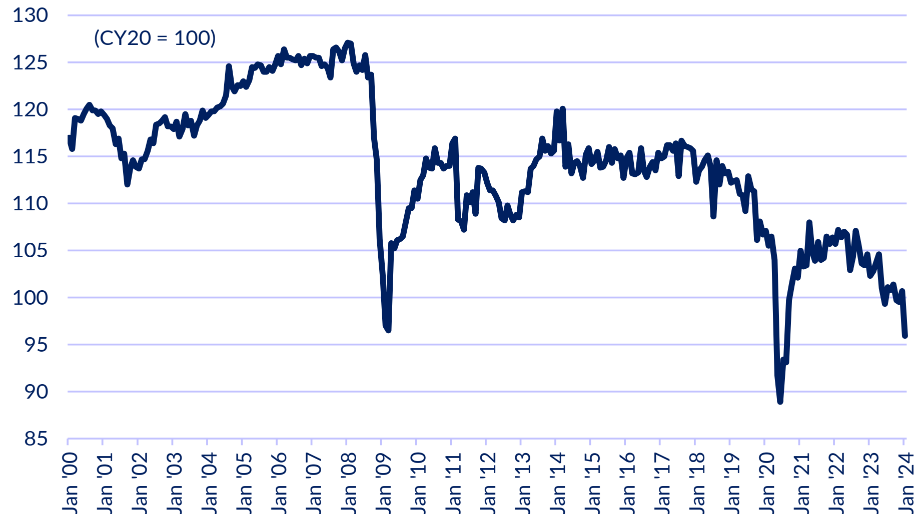
This is an industry with substantial amounts of excess capacity

Figure 41

Capacity utilisation in Japan's paper industry (seasonally adjusted)



Note: Data is from our report published on 29 March 2024. Source: CLSA, METI

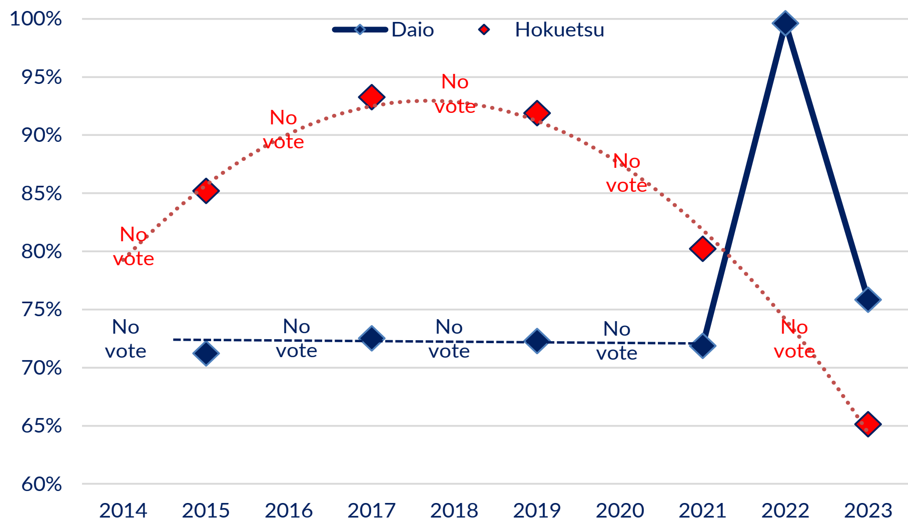
Oasis' original aim was to get Hokuetsu to sell those Daio shares

The original aim of Oasis was to pressure Hokuetsu to sell its holdings in Daio, encouraging other shareholders to vote against reelection of chairman Sekio Kishimoto (78), citing 'the lack of synergies achieved which might have justified the risks involved in holding such a large investment'. Hokuetsu CEO Kishimoto has repeatedly refused to meet Oasis yet, by far its top shareholder. Hokuetsu is one of those rare companies that only holds board election votes every other year, so voting against Kishimoto is one tool that can't be used this year. A shareholder proposal is certainly possible.

Votes for CEO Kishimoto have fallen to worrying levels

Figure 42

CEO votes at Hokuetsu and Daio



Note: Data is from our report published on 29 March 2024. Source: CLSA, companies

Hokuetsu-Daio business partnership is under consideration

On 13 February 2024, Hokuetsu and Daio announced they will begin considering a business partnership in areas such as production technology, raw material purchasing and logistics. The aim is to conclude the partnership agreement by May, though such agreements have fallen apart for Hokuetsu in the past.

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Paper industry remains in Warring States Period, replete with feuds and sudden allegiance changes

Hokuetsu had previously signed a business and capital alliance with Mitsubishi Paper but dissolved it in 2005. Then it entered into a basic agreement to merge the two companies' sales divisions in 2014, but Mitsubishi Paper unilaterally cancelled it in 2015. Mitsubishi Corp had been a white knight for Hokuetsu against Oji, but Mitsubishi Paper became an equity-method affiliate of Oji in 2018. The picture you get is of an industry still in a Warring States Period, replete with petty feuds and sudden changes in allegiance. Hokuetsu seems to have more than its fair share of feuds.

Activism catalyses consolidation: Hokuetsu attractive below ~¥1,800

Hokuetsu and Daio have serious trust issues. The Daio board also mistrusts the Ikawa family. Joining them will not be difficult. The tricky bit for Oasis now is the exit. If Hokuetsu can be merged with Daio, it would then be a logical move to try merge it with Nippon Paper or Oji, if only as an exit route for Oasis. The shares had a big run-up, then collapsed 25% from its 25 March peak. At 20x twelve-month forward earnings, it is still expensive compared to its history. But it is an industry overdue for significant consolidation and Hokuetsu is likely to be at the centre of those changes. The shares seem attractive below 20x, below ¥1,800, on the expectation of consolidation ahead. The period from end-March to AGMs in late June is generally a hot period for corporate action.

Sun Corp: Oasis and the nugget that everyone overlooked

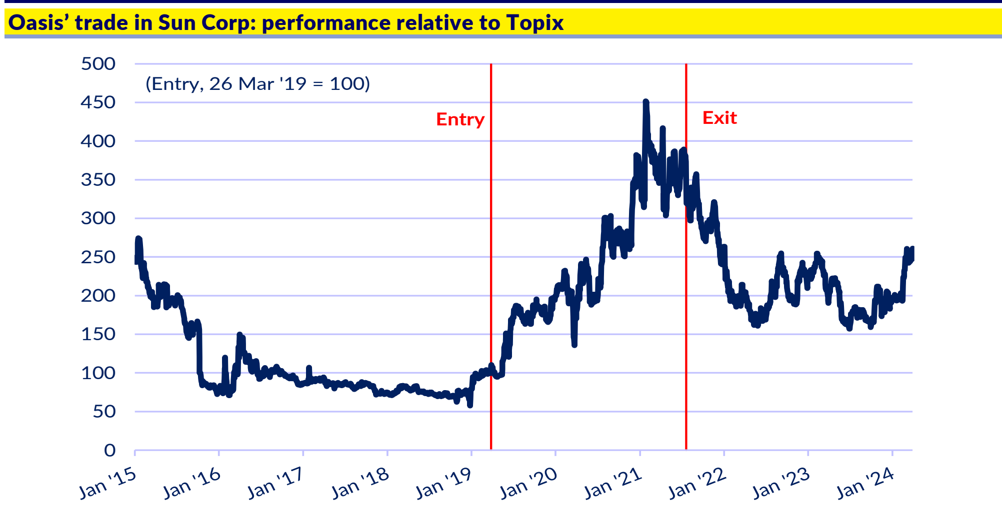
Story centres around acquisition of an iPhone cracking company

Oasis' immensely successful investment in Sun Corp revolves around a subsidiary that was worth far more than Sun or the market understood, and a domestic business that was losing money, in need of a turnaround. Sun Corp was established in 1971, originally producing electronic ticket machines for what is now Omron, then expanding into computers for pachinko, video games and telco equipment, notably iPhone mahjong apps. As sales slumped in 2007, Sun bought Israeli software solutions company Cellebrite Mobile Communication, effective 3 August that year. By FY3/14, Cellebrite's mobile data solutions division had overtaken Sun's pachinko parts and other core revenues. The aim of the purchase had been phone-to-phone transfer technology, but Cellebrite's business took off when it acquired the FBI, CIA and Interpol as clients. It helped them gain access to locked iPhone data, including by assailants in the 2015 Paris and San Bernadino shootings. That put it in the media eye repeatedly as sales and profits soared. On 26 December 2018, an Israeli business newspaper, The Calcalist, disclosed Sun had been in talks with Australia's Macquarie Group and private equity firm KKR about selling up to 50% of Cellebrite, which Sun said it valued at US$400m (¥44bn that day).

Sun was a hugely successful trade, and looks attractive again

Figure 43

Oasis' trade in Sun Corp: performance relative to Topix



Note: Data is from our report published on 29 March 2024. Source: CLSA, Bloomberg

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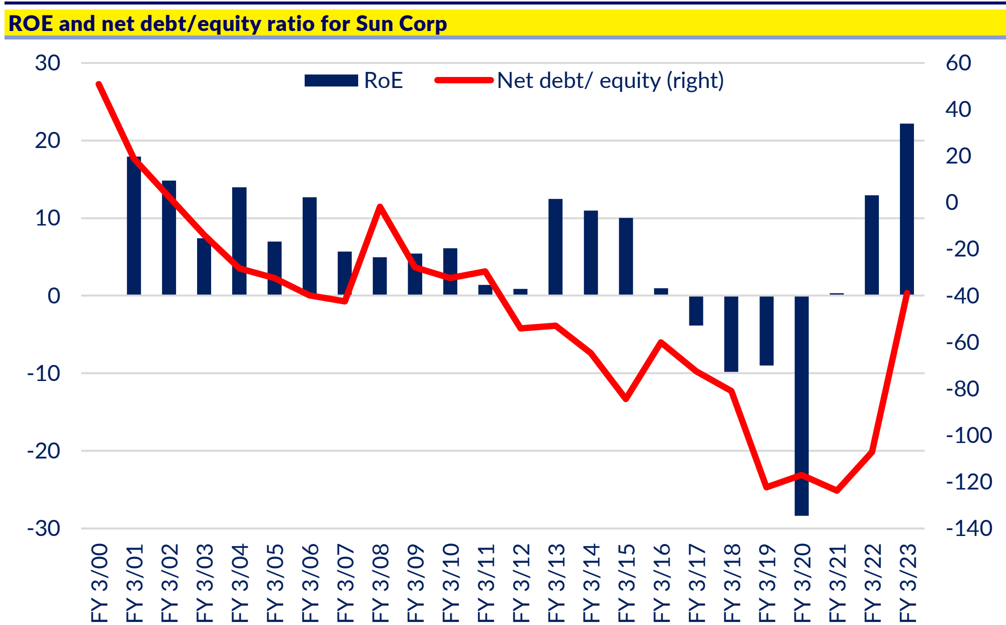
Oasis ousted the board and put in its own, selling shares three months later

Oasis first showed up in filings on 26 March 2019 with a 9.2% stake in Sun, though it had started buying on 21 January that year. At the filing date, Sun had a market cap of ¥19bn and Oasis estimated the value of Cellebrite at ¥150bn or more, not the ¥44bn Sun had discussed. Sun was trading on 1.6x book but had net cash at 122% of equity. On 17 June 2019, Sun announced it had sold off a 24.42% stake in Cellebrite for ¥11.9bn - at broadly a two-thirds discount to the value estimated by Oasis. The buyer was an Israeli venture capital company, Israel Growth Partners Capital. Obviously, it was not as if Sun needed the cash. Sun had slid into the red in FY3/17, with an ROE of minus 9.0% in FY3/19 sliding to minus 28% in FY3/20 - when it actually cut actual dividends, to zero. At the June 2019 AGM, over 40% of shareholders voted against reelection of four out of five directors, including president Masanori Yamaguchi, who stepped down as chairman. With the original business in trouble and the crown jewels being sold at a deep discount, Oasis decided that, instead of waiting for the June 2020 AGM, it would call an extraordinary general meeting on 8 April 2020. The four directors that Oasis proposed dismissing were all dismissed, and it succeeded in putting three directors of its choice onto the board. It then ramped up its stake to 11.1%, then 13.0% then 14.8%, then 16.2% that month. Exit for Oasis - defined as the first sale of shares - was disclosed in July 2021, the same month when a Nasdaq listing was announced for Cellebrite.

Sun didn't need the cash; its core business was in trouble - but it sold crown jewels

Figure 44

ROE and net debt/equity ratio for Sun Corp



Note: Data is from our report published on 29 March 2024. Source: CLSA, Bloomberg

Sun played dog-in-a-manger, making little use of a prize asset

Cellebrite's market cap, when it first traded, was US$634m, though it is now trading at US$2.4bn. Sadly, Sun now only owns 47% of that, after selling off half its stake at a fraction of what it was worth. Even so, what it still owns is worth ¥166bn, against Sun's market cap of ¥82bn. Sun is trading at a 50% discount to the value of its stake in Cellebrite - or to put it another way, the market values Sun's core business as worth a lot less than nothing. On 18 March, Oasis hiked its stake in Sun from 16.15% back up to 18.79% in an off-market trade, with disclosure on 26 March. On the same day, Leopard Asset Management, an Israeli investment manager, filed publicly its intention to ask Sun to return capital, either through distributing Cellebrite shares as a dividend in kind or have Sun do a share buyback.

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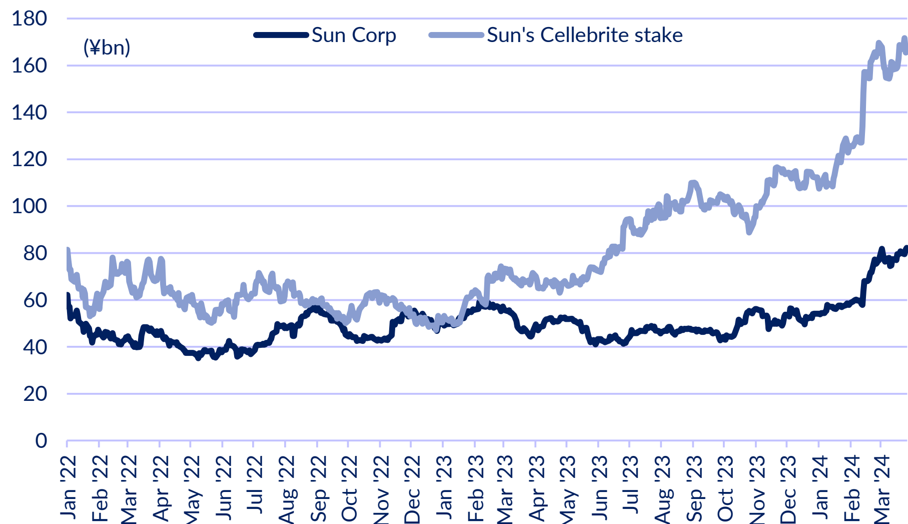
Sun's stake in Cellebrite is worth more than double Sun

Figure 45

Sun and its stake in Cellebrite



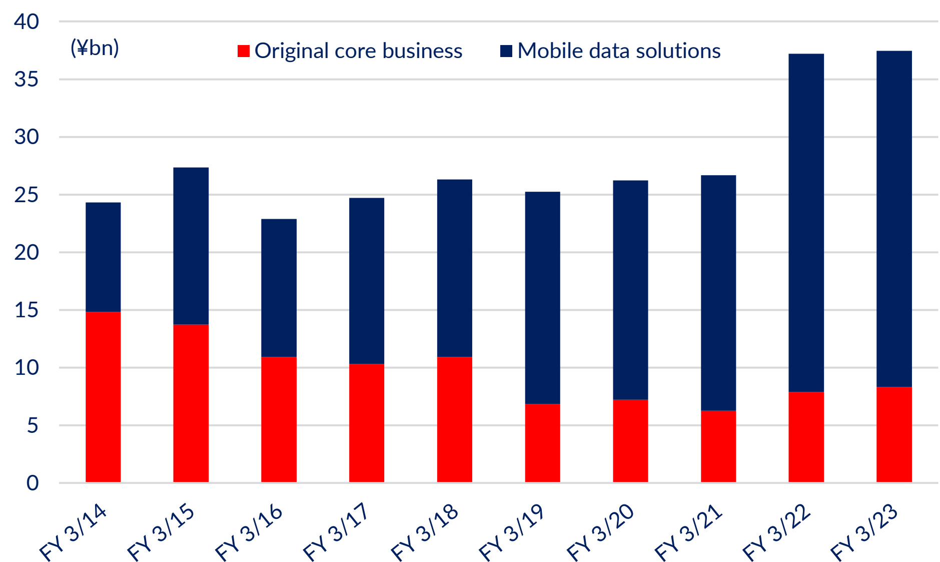
Note: Data is from our report published on 29 March 2024. Source: CLSA, Bloomberg

The trouble is that when you break Sun up into the Mobile Data Solutions business (essentially Cellebrite) and the rest, the original business has been shrinking for years, at a compound rate of over 6%/year.

Sun's original business has been shrinking at 6%/year . . .

Figure 46

Breakdown of Sun Corp sales



Note: Data is from our report published on 29 March 2024. Source: CLSA, Bloomberg

And the original core business hasn't made a profit since FY3/14. If Sun sold off its stake in Cellebrite, or distributed Cellebrite shares to Sun shareholders, would Sun still be a viable company? It could certainly do a massive buyback with the proceeds. It doesn't have the cash to buy the half of Cellebrite that it rashly sold, however. There don't currently appear to be meaningful synergies, so Sun's not bringing much to the Cellebrite party. How do you persuade management to do what is not in their personal best interests? If you can't persuade Sun to distribute the value of its

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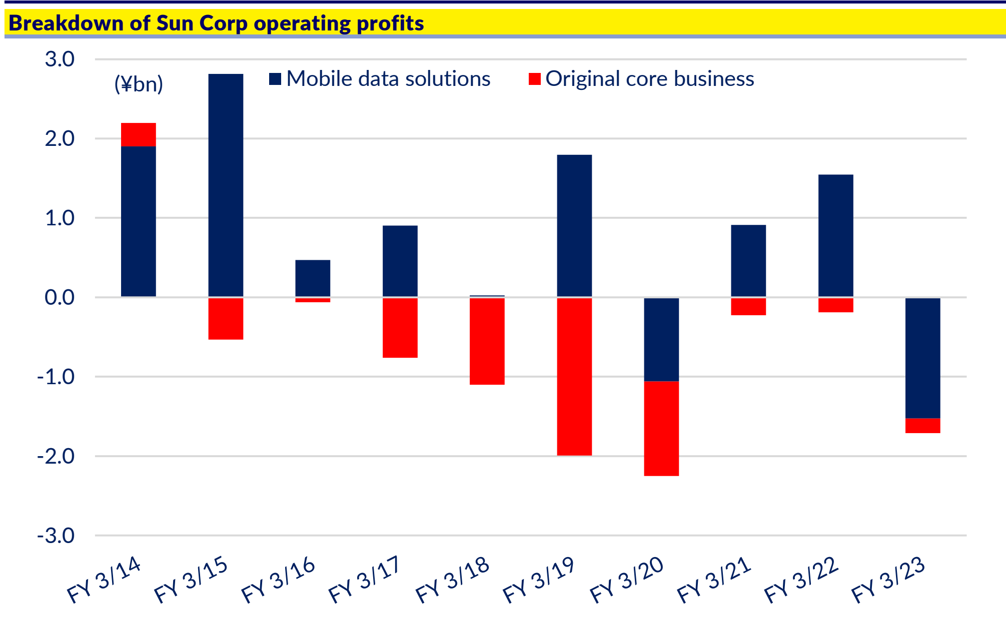
Cellebrite holding, it makes sense to buy out Sun as a way of getting hold of almost half of Cellebrite on the cheap - then the Sun husk can be offloaded. The temptation must be for cornered management to partner in an MBO while it is still deeply undervalued, taking advantage of Japan's relatively lax shareholder protections, like Unizo did with Lone Star. Either way, the investment seems attractive. In January 2021, Sun shares peaked at ¥3,980, but the yen value of Cellebrite has risen over 400% since then. The sole reason this isn't in the Benthos model portfolio is that it's so small, but it is highly attractive.

. . . and hasn't made money in years

Figure 47

Breakdown of Sun Corp operating profits



Note: Data is from our report published on 29 March 2024. Source: CLSA, Bloomberg

Government twigged: activism is crucial to the Japan turnaround story

Back in the Noughties, when the Murakami Fund, Steel Partners and The Children's Investment Fund (TCI) ruled the roost in the activist space, the ministries' approach to activism seemed adversarial. On 24 January 2008, Ministry of Economy, Trade & Industry (METI) vice minister Takao Kitabata gave a speech thundering 'to be blunt, shareholders in general do not have the ability to run a company, and they are fickle and irresponsible. They only take on a limited responsibility but they greedily demand high dividend payments'. He proposed allowing Japanese companies to ignore the principle that all shareholders be treated equally. Times have changed dramatically. The ministries are working together, and working very closely with all investors, including, notably, activists, to improve governance and corporate structure. Greenmailing has a very dark history in Japan, with origins in organised crime. But ValueAct's involvement in Olympus is a great example of activist involvement that left companies in better condition than they found them. The mandarins now fully understand the importance of activists and engagement funds as allies to pressure companies to up their game. Activists in Japanese are called 'shareholders that speak'. But why would any investor not speak - and cajole?

> *Alleyn: Who are you?*
>
> *Fennyman: I'm . . . um, I'm the money.*
>
> *Alleyn: Then you may remain, as long as you remain silent.*

Shakespeare in Love (1998)

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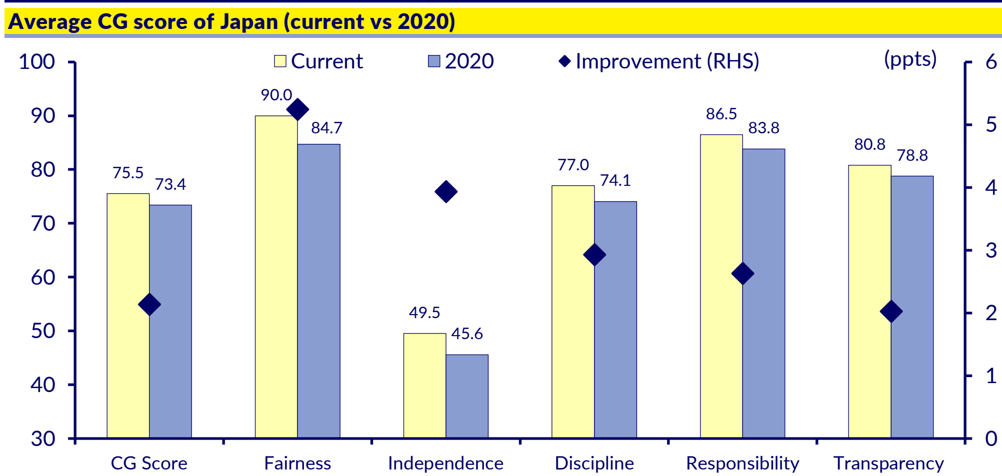
CLSA bottom up scoring shows CG improvement

CLSA's updated bottom-up CG scores indicate a 2.1ppt improvement in Japanese corporates' governance versus 2020, driven by the fairness and independence pillars. Analysts noted improved board diversity, audit committee effectiveness, chairperson independence, and compensation fairness. We provide the top 10 scorers and improvers within CLSA Japan coverage.

Figure 48

Average CG score of Japan (current vs 2020)



Source: CLSA

Hotel & leisure saw largest CG improvement

Hotel & leisure have seen the most improvement compared to 2020 (+6.4ppts) driven by fairness and independence pillar, although they are still the lowest scoring among all sectors. In particular, CLSA analysts saw improvement in diversity of board members (CG17), chairman's independence (CG12), they also saw fewer cases of companies being involved in accounting scandals (CG14), less evidence of any conflict of interest on the board/among senior management (CG21), controversies regarding share trading by board members or company placements (CG23) as well as better investors' access to senior management (CG11).

Energy sector saw the biggest drop relative to other sector

The energy sector's CG score has worsened the most relative to other sectors (-6.9ppts) as discipline and independence pillars weakened. In particular, CLSA analysts are getting more concerned about government interference in company operations (CG05), board diversity (CG17) and fair board and executive remuneration (CG24), as well as genuine independence of boards (CG15).

Hotel & Leisure are the top CG improvers

Figure 49

CG score change vs 2020 by sector

	CG Score	Discipline	Transparency	Independence	Responsibility	Fairness
Hotels & Leisure (5)	6.4	(2.8)	8.3	12.2	0.0	15.0
Internet, Media and Telecoms (13)	6.2	6.2	2.1	6.1	19.7	1.7
Transport & Infrastructure (6)	4.7	1.5	9.1	14.0	(3.5)	8.6
Consumer (46)	4.5	7.1	4.3	8.9	(0.5)	11.6
Conglomerates (4)	4.5	2.5	3.3	13.2	13.3	0.0
Autos (18)	2.4	2.7	8.5	5.9	(4.4)	3.1
Technology (50)	1.5	3.0	1.2	3.3	2.1	2.9
Property (22)	1.1	6.3	0.2	(9.0)	8.2	7.3
Financial Services & Insurance (3)	0.4	0.0	6.7	5.6	0.0	0.0
Healthcare (10)	(0.7)	(2.0)	3.0	(2.1)	3.5	0.2
Power (2)	(1.5)	0.0	0.0	0.0	0.0	0.0
Materials & Capital Goods (17)	(3.2)	(3.0)	(5.0)	(3.1)	1.9	(1.4)
Energy (3)	(6.9)	(8.9)	(5.8)	(7.6)	(2.8)	(4.2)

Source: CLSA. Numbers in brackets shows coverage that exist since 2020

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Financial services is the top scorer

By sector, financial services is the top scorer while hotel & leisure is the bottom scorer. Financial services outperform in transparency and discipline pillars. In particular, CLSA analyst are on average more confident on management teams' understanding of the cost of capital (CG02), and think there is better access to senior management (CG11), an effective audit committee (CG13) voting practices (CG16) and financial disclosures (CG08).

Hotel & leisure remains the bottom scorer even after improvement

Hotel & leisure, relative to other sectors, underperformed particularly in responsibility and discipline pillars. In particular, our analysts have more concerns around the timely disclosure of price sensitive information (CG10), related party transactions that may harm interests of non-controlling shareholders (CG19) and the primary financial interest of controlling shareholders (CG20), while few disclosed return on capital targets (CG06).

Financials and conglomerates are top scorers

Figure 50

Current CG Score by sector

	CG score	Discipline	Transparency	Independence	Responsibility	Fairness
Financial Services & Insurance (3)	82.6	94.4	100.0	58.3	100.0	70.0
Conglomerates (6)	82.3	76.7	93.3	77.8	73.3	100.0
Consumer (50)	80.3	82.4	84.2	55.0	92.5	95.8
Power (2)	78.3	65.0	90.0	44.2	100.0	100.0
Property (22)	77.9	83.8	92.5	35.5	93.6	91.4
Healthcare (14)	76.0	70.7	90.0	54.4	82.9	88.2
Transport & Infrastructure (8)	75.6	82.5	80.6	52.7	82.5	85.6
Japan average	75.5	77.0	80.8	49.5	86.5	90.0
Materials & Capital Goods (30)	74.5	78.1	74.5	53.9	83.6	87.7
Energy (3)	73.9	64.4	76.7	61.1	88.9	83.3
Internet, Media and Telecoms (13)	73.6	63.6	79.2	46.8	97.4	85.8
Technology (54)	73.0	75.1	73.0	47.3	85.6	88.6
Autos (21)	71.0	83.5	79.0	33.3	75.6	86.9
Hotels & Leisure (6)	66.4	66.1	74.2	53.1	58.9	80.8

Source: CLSA. Numbers in brackets shows number of current stock coverage

Top CG scorers include Mitsui, Nippon Express, TechnoPro, Pigeon and Ebara.

Mitsui and Nippon Express top the rankings of CG scores

Figure 51

Top 10 Japan CG Scorer

Ticker	Company name	Sector	Subsector	Analyst	CG score
8031 JP	Mitsui	Conglomerates	na	Edward Bourlet	95.0
9147 JP	Nippon Express	Infrastructure	Other infrastructure	Oliver Matthew	93.5
6028 JP	TechnoPro	Technology	Others	Jun Kato	92.0
7956 JP	Pigeon	Consumer	Other consumer goods	Jun Kato	92.0
6361 JP	Ebara	Capital goods	Other capital goods	Edward Bourlet	92.0
2802 JP	Ajinomoto	Consumer	Food products	Jun Kato	92.0
4452 JP	Kao	Consumer	Cosmetics	Jun Kato	92.0
6506 JP	Yaskawa Electric	Technology	Equipment/Machinery	Morten Paulsen	92.0
6301 JP	Komatsu	Capital goods	Heavy machinery	Edward Bourlet	92.0
7936 JP	Asics	Consumer	Other consumer goods	Nigel Muston	90.5

Source: CLSA

Top CG improvers list includes consumer companies Aeon, Mandom and Japan Tobacco as well as LY Corp and Softbank Group.

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Top improvers include consumer, internet and telecom companies

Figure 52

Top Japan CG improver versus 2020

Ticker	Company name	Sector	Analyst	CG score	2020 CG	Change (ppts)
8267 JP	Aeon	Consumer	Nigel Muston	69.2	30.3	38.8
4917 JP	Mandom	Consumer	Jun Kato	87.5	58.0	29.5
4689 JP	LY Corp	Internet	Oliver Matthew	89.0	59.7	29.3
2914 JP	Japan Tobacco	Consumer	Nigel Muston	75.2	46.7	28.5
9984 JP	Softbank Group	Telecoms	Oliver Matthew	78.8	53.7	25.1
3923 JP	Rakus	Technology	Hideo Noda	85.7	61.7	24.0
6702 JP	Fujitsu	Technology	Hideo Noda	67.4	45.3	22.0
4755 JP	Rakuten Group	Internet	Oliver Matthew	72.5	51.7	20.8
9432 JP	NTT	Telecoms	Oliver Matthe w	77.3	57.3	19.9
3659 JP	Nexon	Internet	Jay Defibaugh	77.6	57.7	19.9

Source: CLSA

We published our latest CG Watch in 2023, with new CG scoring

CLSA CG Scoring framework. In our CG scoring framework, we have 24 questions on the five principles of corporate governance: transparency, fairness, responsibility, independence and discipline, which comprise 90% of the total CG score. We give a 10% weighting to ACGA's market score as regulators and policies, civil society and media play a critical role in defining the corporate governance.

10% weighting for ACGA market score

Figure 53

CLSA CG watch questionnaires and design

Sections	Weighting (%)	Number of questions	Core issues addressed
Discipline	18	6	Management sticks to clearly defined core businesses with discipline, does not harm the interests of shareholders and is free from government interference.
Transparency	18	5	Management provides timely disclosures without controversial accounting and provides good access to senior management.
Independence	18	6	Board acts in an independent way, with proper checks and balance mechanisms through independent audit committees including board diversity measures.
Responsibility	18	3	Management's interests are aligned with the listed company and there has been no misconduct by management or related party transactions which harmed the interests of minority shareholders.
Fairness	18	4	There has been no conflict of interests between board and senior members and the company does not have a weighted vote structure, with fair compensation.
ACGA market score	10	1	Market scores provided by ACGA through Biennial CG Watch, which assesses markets on different stakeholder and thematic categories including 1) government and public governance, 2) the regulatory environment, 3) domestic corporate governance rules, 4) listed companies, 5) investors, 6) auditors & audit regulators and 7) civil society and the media.
Total	**100**	**25**	

Source: CLSA

For detailed description of our scoring framework, please refer to our Sharpening Tools report (*link*).

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Appendix 1: Overall market rankings and scores

Australia stays on top while Japan jumps to 2nd place and Hong Kong falls to 6th

CG Watch 2023 market rankings and scores (%)

Market	Previous ranking	2023	2020	Change vs 2020 (ppt)
1. Australia	1	75.2	74.7	+0.5
2. Japan	=5	64.6	59.3	+5.3
=3. Singapore	=2	62.9	63.2	-0.3
=3. Taiwan	4	62.8	62.2	+0.6
5. Malaysia	=5	61.5	59.5	+2.0
=6. Hong Kong	=2	59.3	63.5	-4.2
=6. India	7	59.4	58.2	+1.2
8. Korea	9	57.1	52.9	+4.2
9. Thailand	8	53.9	56.6	-2.7
10. China	10	43.7	43.0	+0.7
11. Philippines	11	37.6	39.0	-1.4
12. Indonesia	12	35.7	33.6	+2.1

Note: Total market scores are not an average of the seven category percentage scores. They are an aggregate of the exact scores for each of the 108 questions in the survey, converted to a percentage. Total points for each market out of 540 were: Australia (402.5); Japan (349); Singapore (339.5); Taiwan (339); Malaysia (332); Hong Kong (320); India (321); Korea (308.5); Thailand (291); China (236); Philippines (203); and Indonesia (193). The denominator for Australia was 535, not 540, as one question on SOEs does not apply. Source: ACGA

Market scores by category

Market scores by category: 2023 vs 2020

(%)		AU	CH	HK	IN	ID	JP	KR	MY	PH	SG	TW	TH
1. Government & Public Governance	**2023**	**71**	**32**	**55**	**45**	**32**	**61**	**52**	**37**	**29**	**56**	**67**	**35**
	2020	68	29	65	45	31	60	60	32	28	60	68	35
2. Regulators	**2023**	**66**	**56**	**62**	**53**	**29**	**65**	**57**	**58**	**25**	**63**	**65**	**50**
	2020	65	52	69	53	24	62	53	53	27	63	66	51
- Funding, capacity, CG reform	***2023***	*61*	*44*	*54*	*52*	*35*	*67*	*51*	*56*	*25*	*56*	*61*	*45*
	2020	*62*	*42*	*62*	*51*	*31*	*58*	*45*	*53*	*27*	*56*	*62*	*47*
- Enforcement	***2023***	*72*	*69*	*72*	*54*	*22*	*63*	*64*	*60*	*24*	*71*	*70*	*54*
	2020	*68*	*64*	*76*	*56*	*16*	*66*	*62*	*54*	*26*	*70*	*70*	*56*
3. CG Rules	**2023**	**83**	**63**	**75**	**73**	**40**	**67**	**65**	**79**	**48**	**77**	**71**	**75**
	2020	82	63	75	69	35	58	56	77	45	75	66	76
4. Listed Companies	**2023**	**76**	**39**	**53**	**60**	**36**	**49**	**49**	**66**	**48**	**58**	**55**	**51**
	2020	79	51	59	65	38	44	48	66	55	60	63	60
5. Investors	**2023**	**69**	**22**	**33**	**46**	**20**	**65**	**56**	**42**	**25**	**39**	**40**	**35**
	2020	66	18	34	44	19	60	44	43	21	39	38	38
6. Auditors & Audit Regulators	**2023**	**82**	**49**	**82**	**69**	**65**	**83**	**73**	**92**	**62**	**83**	**83**	**79**
	2020	86	43	81	54	59	77	70	86	60	81	76	76
7. Civil Society & Media	**2023**	**82**	**26**	**50**	**74**	**44**	**66**	**43**	**53**	**33**	**64**	**62**	**46**
	2020	80	22	60	78	38	62	36	44	36	64	62	49

Source: ACGA

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Appendix 2: ACGA market-ranking survey

1. Government & public governance

			AU	CH	HK	IN	ID	JP	KR	ML	PH	SG	TW	TH
1.1	To what extent does the current government administration (executive branch) have a clear and credible long-term strategy for promoting corporate governance reform to support capital-market and business-sector development?	2023	2.5	2	0	1	1	4	2	0	2	2	4.5	1
		2020	2	1	1	2	1	3	4	0	2	2	4	1
1.2	To what extent does the current government provide consistent political support for the policy and enforcement work of financial regulators (ie, securities commissions and stock exchanges)?	2023	2.5	2	2	1	1	3.5	1	1.5	1	2.5	4	2
		2020	2	2	3	2	1	3	4	1	1	3	4	2
1.3	To what extent has the central bank or equivalent financial authority set effective guidance for the governance of banks?	2023	3.5	2	3.5	3	3	3	3	4	3	4	3	2
		2020	3	2	4	3	2	2	3	4	3	4	3	2
1.4	Is there a coherent structure to the regulatory system governing the securities market, including the IPO regime? (ie, one without clear conflicts of interest involving either the securities commission or the stock exchange; without fragmentation and disagreement between different regulatory authorities; and where there is a clearly definable securities commission or bureau taking the lead on enforcement)	2023	4	3	3	3	2	4	3	3	3	4	4	4
		2020	4	3	3	3	2	4	3	2	3	4	4	4
1.5	Is the securities commission formally and practically autonomous of government? (ie, not part of the ministry of finance; nor has the minister of finance or another senior official as chairman; nor unduly influenced by government)	2023	3	0	2.5	2	2	2	1	1	1	1	1	2
		2020	3	0	3	2	2	2	1	1	1	1	2	2
1.6	Is the securities commission funded independently (eg, a levy on securities transactions or capital market participants) and not dependent on an annual budgetary allocation from government?	2023	3	0	4.5	3	4	2	4.5	5	1	0	4.5	5
		2020	3	0	5	4	4	2	5	5	1	0	5	5
1.7	Is there an independent commission against corruption (or a group of agencies) with broad powers to tackle public- and private-sector corruption?	2023	3.5	0	3	1	2	2	3	1	0	3	2	0
		2020	3	0	3	1	2	2	3	1	0	4	2	0
1.8	How far advanced is the government in tackling public- and private-sector corruption?	2023	3	1	3	1	1	2.5	2	1	1	3	2	0
		2020	3	1	3	1	1	3	2	0	1	3	2	0
1.9	To what extent has the government sought to achieve and maintain high standards of civil service ethics and accountability?	2023	4	1	2.5	2	1	4	5	1	1	3	4	1
		2020	4	1	3	2	1	4	5	1	1	3	4	1
1.10	To what extent is the judiciary able to act independently of government, and is also perceived as unbiased and clean in relation to company and securities cases?	2023	5	1	4	5	1	3	2	1	1	4	4	0
		2020	5	1	5	2	1	4	2	1	1	5	4	0
1.11	To what extent is the judiciary adequately resourced and skilled in handling company law and securities cases?	2023	5	2.5	4.5	3	1	3.5	3	2.5	2	5	3.5	2
		2020	5	2	5	3	1	4	3	3	2	5	3	2
1.12	Does the legal system allow minority shareholders and other stakeholders fair and efficient access to courts to settle disputes? (ie, in terms of the cost of going to court and the range of legal remedies available).	2023	3.5	3	0.5	2	1	3	2	1	2	1	3	2
		2020	4	3	1	2	1	3	2	1	1	1	3	2
1.13	Does the government follow best practice standards as regards listed SOE governance? (ie, it requires them to follow the same governance standards as private-sector issuers, refrains from interfering in their governance, and so on)	2023	na	3	3	2	1	3	2	2	1	4	4	2
		2020	na	3	3	2	1	3	2	1	1	4	4	2
	2023 category score (out of 65)		42.5	20.5	36	29	21	39.5	33.5	24	19	36.5	43.5	23
	Category percentage (rounded)		71	32	55	45	32	61	52	37	29	56	67	35
	Rank		1	10	5	7	11	3	6	8	12	4	2	9

Source: ACGA

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2. Regulators

Funding, Capacity Building, Regulatory Reform			AU	CH	HK	IN	ID	JP	KR	ML	PH	SG	TW	TH
2.1	Is the securities commission sufficiently resourced in terms of funding and skilled staff to carry out its regulatory objectives?	2023	4	1	4	3	2	4	4	4	1	2.5	3	3.5
		2020	4	1	5	3	2	4	4	3	1	2	4	4
2.2	To what extent has the securities commission been investing in surveillance, investigation and enforcement capacity and technology over the past two years?	2023	4	4	4	4	2	3	3.5	3	0	2.5	2.5	3.5
		2020	4	4	4	3	2	3	3	3	0	2	3	4
2.3	Is the stock exchange (or exchanges) sufficiently resourced in terms of funding and skilled staff to carry out enforcement of the listing rules?	2023	2.5	1	3	2	2	4	1	3.5	2	4	3	3
		2020	3	1	3	2	2	4	1	3	2	4	3	3
2.4	To what extent has the stock exchange been investing in surveillance, investigation and enforcement capacity and technology over the past two years?	2023	2	1	1	2	1	2.5	1	2	1	3	2.5	2
		2020	1	1	1	2	1	2	1	3	1	3	3	2
2.5	Has the government and/or securities commission been modernising legislation over the past two years to improve corporate governance and address relevant local CG problems?	2023	3	1.5	1	4	2	4.5	4	1	3	3	4	2
		2020	3	1	2	3	2	3	4	1	4	3	5	2
2.6	Has the stock exchange been modernising its listing rules and best-practice codes over the past two years to improve corporate governance?	2023	2	3.5	2.5	1	0	4	3.5	4	2	3	4	2
		2020	3	2	4	1	0	3	2	3	2	4	5	2
2.7	Do financial regulators (securities commissions and stock exchanges) undertake public and written market consultations prior to major rule changes?	2023	5	1	4	0.5	1	3.5	1	3.5	1	3	2	2
		2020	5	1	5	2	1	2	1	3	1	3	2	2
2.8	Do the securities commission and stock exchange have informative websites with English translations of all key laws, rules and regulations easily accessible?	2023	5	4	5	5	2	3	3	5	3	5	3.5	5
		2020	5	5	5	5	1	4	3	5	3	5	3	5
2.9	Does the stock exchange provide an efficient, extensive and historical online database of issuer announcements, notices, circulars and reports archived for at least 15 years and in English?	2023	5	4	5	2	3	2.5	2.5	5	1	4	3	2
		2020	5	4	5	2	3	1	2	5	1	4	1	2
2.10	Has the stock exchange or another organisation developed an open electronic voting platform ("straight through processing") for investors?	2023	0	3	0	5	4	5	4.5	0	0	0	5	0
		2020	0	3	0	5	3	5	4	0	0	0	5	0
2.11	To what extent does the current IPO listing regime (including rules, guidance, support of investment bank sponsors) prepare companies to implement an effective and meaningful corporate governance system prior to listing?	2023	1	0	0	0	0	1	0	0	0	1	1	0
		2020	1	0	0	0	0	1	0	0	0	1	0	0
	2023 sub-category score (out of 55)		33.5	24	29.5	28.5	19	37	28	31	14	31	33.5	25
	Percentage (rounded)		61	44	54	52	35	67	51	56	25	56	61	45
	Rank		2	10	6	7	11	1	8	4	12	4	2	9
Enforcement														
2.12	Do financial regulators in your market have a reputation for vigorously and consistently enforcing securities laws and regulations?	2023	3	3	3	2	1	2.5	3	2.5	1	2.5	3.5	2
		2020	3	2	3	2	1	2	3	2	1	3	3	2
2.13	Have their efforts improved and evolved over the past two years?	2023	4.5	4	3	3	1	3	4	2	1	4	4	3
		2020	4	3	3	3	1	3	4	1	1	4	3	3
2.14	Does the securities commission have robust powers of surveillance, investigation, sanction, and compensation?	2023	5	4	5	5	1	3	4	5	2	5	5	4
		2020	5	4	5	5	1	3	4	5	3	5	5	5
2.15	Have the government and its law enforcement agencies had a successful track record prosecuting all forms of market misconduct over the past two years, including insider trading, market manipulation, fraud, embezzlement, and false disclosure?	2023	4	4	4	2	1	3	3	2	1	4	3	3
		2020	3	4	5	2	0	3	3	2	1	4	3	3
2.16	Does the securities commission disclose multi-year data on its enforcement activities, with explanations as to what the data means and detailed announcements on individual cases?	2023	5	4	5	4	1	3	2	5	0	3	3	3
		2020	5	4	5	4	0	4	2	3	0	3	4	3
2.17	Does the stock exchange (or related agencies) have an effective range of powers to sanction breaches of the listing rules?	2023	3.5	3	3	3	3	5	4.5	4	3	4	4.5	3
		2020	3	3	3	3	3	5	4	4	3	4	4	3
2.18	Has the stock exchange (or related agencies) had a successful track record enforcing breaches of the listing rules over the past two years?	2023	1.5	3	3	2	1	2.5	2	3	1	3	3	2
		2020	2	3	3	3	1	3	2	3	1	3	3	2
2.19	Does the stock exchange disclose detailed data on and explanations of its enforcement activities?	2023	2	4	5	1	1	3	3	4	1	3	2	2
		2020	2	4	5	1	1	3	3	3	1	2	3	2
2.20	Have the government and regulatory authorities taken steps to minimise and control conflicts of interests between the commercial and regulatory functions of the stock exchange?	2023	4	2	1	2	1	3	2	1.5	1	3	3	3
		2020	3	2	2	2	0	3	2	2	1	3	3	3
2.21	Do financial regulators receive efficient and committed support from other national enforcement agencies and institutions (ie, the police, attorney general, courts)?	2023	3.5	3.5	4	3	0	3.5	4.5	1	1	4	4	2
		2020	4	3	4	3	0	4	4	2	1	4	4	2
	2023 sub-category score (out of 50)		36	34.5	36	27	11	31.5	32	30	12	35.5	35	27
	Percentage (rounded)		72	69	72	54	22	63	64	60	24	71	70	54
	Rank		1	5	1	9	12	7	6	8	11	3	4	9
	2023 category score (out of 105)		69.5	58.5	65.5	55.5	30	68.5	60	61	26	66.5	68.5	52
	Category percentage (rounded)		66	56	62	53	29	65	57	58	25	63	65	50
	Rank		1	8	5	9	11	2	7	6	12	4	2	10

Source: ACGA

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3. CG rules

			AU	CH	HK	IN	ID	JP	KR	ML	PH	SG	TW	TH
3.1	Do corporate and financial reporting standards (ie, rules) compare favourably against international standards? (ie, on frequency and timeliness of reporting; robust continuous disclosure; detailed MD&A; sufficient narrative and notes to the P&L, balance sheet, cashflow; and so on)	2023	5	5	5	4	2	4.5	5	4	3	5	4.5	5
		2020	5	4	5	4	2	4	4	4	3	5	4	5
3.2	Do CG reporting standards compare favourably against international standards? (ie, requirements for a Report of the Directors; CG statements or reports; board and committee disclosure; director biographies; internal controls and audit; discussion of risk factors)	2023	4	2	4	4	2	4	3.5	4	3	3	3	5
		2020	5	2	4	4	2	3	3	4	3	3	3	5
3.3	Do ESG/sustainability reporting standards compare favourably against international standards? (ie, stock exchange ESG reporting rules; a sustainability section in the annual report; a separate GRI or TCFD Report; a company law provision that directors have a responsibility to report on environmental and social/stakeholder matters)	2023	4	2	4	4	1	4	3	4	2	5	5	5
		2020	4	2	4	2	1	3	1	4	1	5	5	5
3.4	Is quarterly reporting mandatory, is it consolidated, and does it require P&L, Balance Sheet, and Cashflow statements with an explanation of the numbers?	2023	1	4	1	3	4	5	4	5	4	1	4	5
		2020	1	4	1	3	4	5	4	5	4	1	4	5
3.5	Is timely disclosure of "substantial ownership" required (ie, when investors acquire a 5% stake or sell down below 5%) as well as "creeping" increases/decreases of one percentage point? Disclosure of any change should be within 3 business days.	2023	5	5	5	4	4.5	4	4	5	3	5	2	2
		2020	5	5	5	4	4	4	4	4	3	5	1	2
3.6	Must directors disclose on-market share transactions within three business days?	2023	3	5	5	5	3	2	3	5	3	5	5	2
		2020	3	5	5	5	2	2	3	5	3	5	5	2
3.7	Must controlling shareholders disclose share pledges in a timely manner?	2023	2	5	5	2	1	3	4.5	0	2	3	3	0
		2020	2	5	5	3	1	3	0	0	0	3	4	0
3.8	Is there a closed period (a "blackout") of at least 60 days before the release of annual results and at least 30 days before interim/quarterly results during which directors cannot trade their shares?	2023	5	3	5	5	1	3	1	2	3	5	1.5	1
		2020	5	3	5	5	0	2	0	2	3	5	0	0
3.9	Are there clear rules on the prompt disclosure of price-sensitive information?	2023	5	4	5	4	3	4.5	4	5	5	5	5	4
		2020	5	4	5	4	2	4	4	4	5	5	5	4
3.10	Are there clear rules on the timely and meaningful disclosure of related-party transactions, calibrated for the size/materiality of transactions, and that allow minority shareholders to approve major RPTs?	2023	4	3.5	5	3	0	3	3	5	1	5	2	5
		2020	4	4	5	3	0	3	3	5	1	5	1	5
3.11	Are there clear rules prohibiting insider trading, with strong deterrent penalties?	2023	3.5	4.5	5	3	1	3.5	4.5	5	2	5	3.5	4
		2020	4	4	5	3	0	3	4	5	2	5	3	5
3.12	Is voting by poll mandatory for all resolutions at general meetings, followed by disclosure of results within one day?	2023	4.5	4	4	4	1	3.5	1	5	1	5	4.5	5
		2020	4	4	4	3	1	3	1	4	1	5	4	5
3.13	Is there an up-to-date national code of best practice - and accompanying guidance documents - that takes note of evolving international CG standards and is fit for purpose locally (ie, addresses fundamental CG problems in the domestic market)?	2023	4.5	2.5	3	3	2	4.5	4	4	2.5	3	4	4
		2020	5	3	3	3	2	4	3	4	3	3	4	5
3.14	Is there a stewardship code (or codes) for institutional investors based on the "comply or explain" standard and that seeks investor signatories?	2023	5	0	1.5	5	0	5	4	5	0	2	4.5	5
		2020	5	0	2	4	0	5	5	4	0	1	4	5
3.15	Is there a clear and robust definition of "independent director" in the code or listing rules? (ie, one stating independent directors should be independent of both management <u>and</u> the controlling shareholder; that does not allow former senior executives or former professional advisors/auditors to become independent directors after short "cooling-off" periods, nor people with business relationships)	2023	3	2	2	2	2	3.5	3	3	2	3	3	2
		2020	3	2	2	2	2	3	3	3	2	3	3	2
3.16	Must companies disclose the exact remuneration of individual directors and at least the top five key management personnel (KMP) by name?	2023	5	3	4	4	2	2	2	3	1	3	2	4
		2020	5	3	4	4	2	1	3	3	1	2	2	4
3.17	Are fully independent audit committees mandatory and given broad powers to review financial reporting, internal controls and risk management, and communicate independently with both the external and internal auditor?	2023	4.5	3	4	4	2	2.5	4	4	2	4	3	4
		2020	4	3	4	3	1	2	4	4	2	4	3	4
3.18	Are largely independent nomination committees mandatory and given broad powers to nominate directors?	2023	4	2	2.5	4	2	2	3	4	1	4	2	4
		2020	4	2	2	4	2	1	3	4	1	4	2	4
3.19	Can minority shareholders easily nominate directors?	2023	5	2	2	4	2	5	5	3	2	3	5	3
		2020	4	2	2	4	2	3	5	3	2	3	5	3
3.20	Is there a statutory or regulatory requirement that directors convicted of fraud or other serious corporate crimes must resign - or are removed from - their positions on boards and in management?	2023	5	4	3	3	3	4	2.5	5	5	5	3	5
		2020	5	4	3	3	3	4	1	5	5	5	3	5
3.21	Are pre-emption rights for minority shareholders - their right to buy any new shares issued by the company on a pro-rata basis - firmly protected? (ie, new shares issued for cash must keep to strict caps of no more than 5-10% of issued capital and a 5-10% discount to the current share price; shareholders can approve the extension of such placement mandates at each AGM; and/or measures have been introduced to allow for much faster rights issues)	2023	4	1	2	1	2	1	1.5	3	1	3	1.5	2
		2020	3	1	2	1	2	1	1	3	1	3	2	2
3.22	Must companies release their AGM proxy materials (with final agendas and an explanatory circular) at least 28 calendar days before the date of the meeting?	2023	5	3	4	4	3	2	3	4	4	2	5	4
		2020	5	3	4	4	3	2	3	4	3	2	3	4
3.23	Are there clear and robust rules for the protection of minority shareholders during takeovers and voluntary delistings (taking companies private)?	2023	4	3	4	3	1	2.5	2	3	2	4	4	5
		2020	3	3	4	3	1	2	2	4	2	4	4	5
3.24	Are institutional shareholders free to undertake collective engagement activities without an undue burden from concert-party rules?	2023	5	3	5	5	3	2	3	5	3	4	5	5
		2020	5	3	5	5	3	2	3	5	3	4	5	5
	2023 category score (out of 120)		100	75.5	90	87	47.5	80	77.5	95	57.5	92	85	90
	Category percentage (rounded)		83	63	75	73	40	67	65	79	48	77	71	75
	Rank		1	10	4	6	12	8	9	2	11	3	7	4

Source: ACGA

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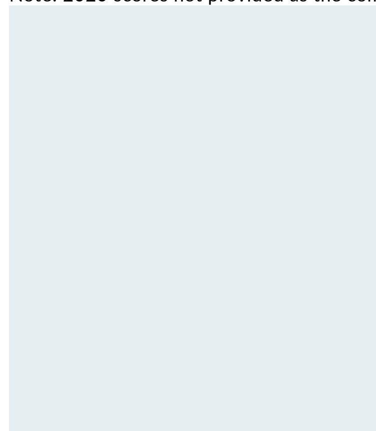
4. Listed companies

		AU	CH	HK	IN	ID	JP	KR	ML	PH	SG	TW	TH
4.1	Does the company's board governance reporting compare favourably against international best practice?	2	2.5	2	2.5	1	2	2	2	2.5	2	2	1
4.2	How would you rate the quality of the company's ESG/sustainability reporting?	3.5	1	3	3	1.5	3	4	2.5	3	3	4.5	1.5
4.3	Does the company provide comprehensive, timely and quick access to information for investors?	4	2	2.5	4	3.5	3	2.5	4	3.5	3	4	4
4.4	Does the company undertake annual board evaluations, either internally or using external consultants?	2	0	1	2.5	2	2.5	1	3	2	2.5	3.5	1.5
4.5	Does the company disclose and implement a credible board diversity policy?	3.5	0.5	1	1.5	0.5	1.5	1	2	1.5	1.5	3	1
4.6	Does the company provide induction and/or ongoing training to all directors?	3.5	1	2	4	2.5	1.5	1.5	4	3	2	3	2
4.7	Does the company have an independent chairman and/or a lead or senior independent director?	5	0	1.5	2	1.5	0.5	3	3.5	0	4	0	1
4.8	Does the company disclose total remuneration of each member of the board of directors?	5	4	4.5	4.5	0.5	2.5	1	5	1	3	2.5	4.5
4.9	Are the independent directors paid partly or wholly in stock options or restricted share awards? OR: Do they share in a percentage of company earnings or other commissions in addition to their base fee? (Note: We largely deduct scores for this type of compensation, which we consider creates potential conflicts of interest for INEDs. We give higher points where such compensation is not provided.)	5	5	4.5	1.5	1.5	5	4	2.5	4.5	4.5	4	5
4.10	Are audit committees (or an equivalent) independently led and competent in financial reporting/ accounting matters?	5	3.5	4.5	4	4.5	2.5	3.5	4.5	3.5	4.5	4	4
4.11	Does the company have an internal audit department that reports to the audit committee?	3	3	3	4	1.5	2.5	3.5	3.5	3.5	3.5	4	3.5
4.12	Does the company provide a detailed explanation of its executive remuneration policies?	5	0.5	2	2.5	1	3.5	2	2	1.5	2.5	2	2
4.13	Does the company have a nomination committee and is it independently led?	4.5	3.5	3	4.5	2.5	3	3.5	4.5	2	3	1.5	3.5
4.14	Does the nomination committee have a female chair or at least one female director?	2.5	0.5	2.5	1.5	1	1.5	1.5	3	2	1.5	0.5	1.5
	2023 category score (out of 70)	53.5	27	37	42	25	34.5	34	46	33.5	40.5	38.5	36
	Category percentage (rounded)	76	39	53	60	36	49	49	66	48	58	55	51
	Rank	1	11	6	3	12	8	8	2	10	4	5	7

Note: 2020 scores not provided as the company survey substantially changed. Source: ACGA



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5. Investors

			AU	CH	HK	IN	ID	JP	KR	ML	PH	SG	TW	TH
5.1	Are domestic institutional investors (asset owners and managers) working to promote better corporate governance in your market through publicly announced policies on CG, ESG, voting or stewardship?	2023	4.5	1	1.5	4.5	0	3.5	3	2	1	1	3	3
		2020	4	1	2	5	0	4	3	2	1	1	3	3
5.2	Are foreign/international institutional investors (asset owners and managers) working to promote better corporate governance in your market through publicly announced policies on CG, ESG, voting or stewardship?	2023	3	2	4	2	1	4.5	3	2	1	4	3	3
		2020	3	2	5	2	1	4	3	2	1	4	3	3
5.3	Do a majority of domestic institutional investors exercise their voting rights, including voting against resolutions with which they disagree?	2023	5	2	2.5	4	2	5	4	3	2	1	2.5	3
		2020	5	1	2	4	1	5	3	2	1	1	3	3
5.4	Do a majority of foreign/international institutional investors exercise their voting rights, including voting against resolutions with which they disagree?	2023	5	3	5	4	3	5	5	3	3	4	4	3
		2020	5	3	5	4	3	5	5	3	3	5	5	3
5.5	Do domestic institutional investors actively participate in annual general meetings?	2023	0.5	1	1	1	1	1	1.5	2	2	1	2	1
		2020	1	1	1	1	2	1	1	2	2	1	2	1
5.6	Do foreign institutional investors actively participate in annual general meetings?	2023	0	0	1	0.5	1	1.5	1.5	1	1	1	0	1
		2020	0	0	1	1	2	1	1	1	1	1	1	1
5.7	Do activist funds exist that seek to address specific company issues or transactions?	2023	2	0	1	1.5	1	5	4	1	0	1	1	0
		2020	2	0	2	1	1	5	3	1	0	0	0	0
5.8	Do domestic asset owners (in particular state pension and investment funds) play a leadership role in prompting responsible investment and investor stewardship?	2023	5	1	1	1	0	3.5	3	3	0	1	0	1
		2020	5	1	1	1	0	3	3	3	0	1	2	2
5.9	To what extent do domestic institutional investors engage in regular individual or collective engagement with listed companies?	2023	4.5	1	1	3	1	2.5	2.5	3	1	1	2.5	2
		2020	5	0	1	3	0	3	2	4	0	1	2	2
5.10	To what extent do foreign/international institutional investors engage in regular individual or collective engagement with listed companies?	2023	2.5	1.5	3	2.5	2	3	3	2	2	3	1.5	1
		2020	3	1	3	2	2	2	3	2	2	3	2	1
5.11	Are domestic investors effectively disclosing how they manage institutional conflicts of interest?	2023	3	0	2	2	2	3.5	0	2	1	1	1	2
		2020	3	0	2	2	2	3	1	2	1	1	0	2
5.12	Do domestic institutional investors disclose voting down to the company level, and give substantive reasons for voting Against?	2023	3	0	0	4.5	0	4	4.5	0	0	0	1	4
		2020	3	0	0	5	0	4	5	0	0	0	0	5
5.13	Do any proxy advisory services operate locally?	2023	5	2.5	0	5	0	4	3.5	3	0	1.5	0	0
		2020	5	2	0	5	0	4	3	4	0	3	0	1
5.14	Do retail shareholders see the annual general meeting as an opportunity to engage with companies, ask substantive questions, and put forward shareholder proposals?	2023	4	1	2	1	2	3.5	1.5	4	2	4	3.5	2
		2020	4	1	2	1	2	3	1	3	2	4	3	2
5.15	Have retail shareholders formed their own (ie, self-funded) associations to promote improved corporate governance?	2023	5	0	0	1	0	0	3	2	3	4	0	2
		2020	5	0	0	1	0	0	0	3	3	4	0	3
5.16	Do retail shareholders or individuals launch public activist campaigns against errant directors or companies?	2023	4	0	2	1	0	3.5	2.5	3	1	5	4	1
		2020	3	1	3	1	0	3	1	2	1	5	3	1
5.17	Do retail shareholders (or government agencies acting on their behalf) undertake lawsuits against errant directors or companies?	2023	3	2.5	1	1	1	2.5	2	0	1	0	5	1
		2020	3	2	1	1	1	3	2	0	1	0	5	1
	2023 category score (out of 85)		59	18.5	28	39.5	17	55.5	47.5	36	21	33.5	34	30
	Category percentage (rounded)		69	22	33	46	20	65	56	42	25	39	40	35
	Rank		1	11	9	4	12	2	3	5	10	7	6	8

Source: ACGA

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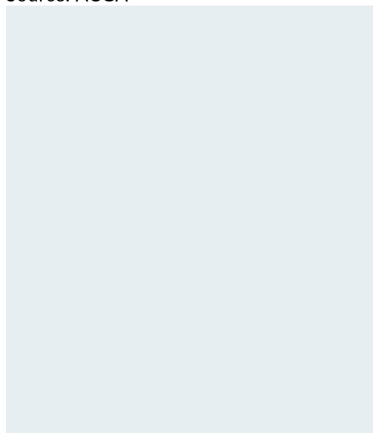
6. Auditors & audit regulators

			AU	CH	HK	IN	ID	JP	KR	ML	PH	SG	TW	TH
6.1	Are local accounting standards for listed companies fully converged with International Financial Reporting Standards (IFRS)?	2023	5	4	5	3	4	4.5	5	5	5	5	5	5
		2020	5	4	5	3	3	4	5	5	4	5	5	5
6.2	Are local auditing standards for listed companies fully converged with International Standards on Auditing (ISAs)?	2023	5	3	5	4	4	5	4	5	5	4.5	4.5	5
		2020	5	3	5	3	3	4	4	5	4	4	4	5
6.3	Has the government or accounting regulator enacted effective rules on the independence of external auditors? (eg, by introducing limits on the non-audit work that external auditors can do; requirements for audit-partner rotation; whistleblower protection for auditors; a positive duty for auditors to report fraud; and so on)	2023	4	2	4	3	4	4.5	4	4	3	4	3.5	4
		2020	5	2	4	2	3	4	3	5	3	4	3	4
6.4	Is disclosure of audit and non-audit fees paid to the external auditor required, with accompanying commentary sufficient to make clear what the non-audit work is?	2023	5	2	4	4	3	4.5	5	4	5	4	5	5
		2020	5	2	5	4	3	4	5	4	5	4	4	5
6.5	Are extended auditor reports focussing on "key audit matters" (KAMs) required?	2023	5	5	5	5	2.5	2.5	5	5	5	5	5	5
		2020	5	5	5	4	0	2	4	5	5	5	5	5
6.6	Has the government established an independent audit oversight board (AOB) with clear and independent powers of registration, inspection, investigation, sanction (over both auditors and audit firms), and standard setting?	2023	3.5	3	4	3.5	3	4	4	5	2	3.5	4.5	4
		2020	4	0	3	3	3	3	3	4	2	3	5	4
6.7	Does the audit regulator exercise effective and independent disciplinary control over the audit profession?	2023	3	2.5	3	4	3	3.5	4	4	2	2	3.5	2
		2020	3	1	3	3	4	3	3	3	2	2	3	2
6.8	Does the audit regulator disclose its enforcement work and other activities on a timely and detailed basis?	2023	4.5	2	5	3	3	4.5	2	5	1	3.5	3	2
		2020	5	2	5	3	3	5	2	5	1	4	2	2
6.9	Does the audit regulator publish a detailed report on its inspection programme, audit quality, and audit industry capacity (ie, the level of skills and experience in the CPA profession) every one to two years?	2023	4	1	4	3	3	4.5	1	5	1	5	4	4
		2020	5	1	4	2	2	5	1	5	1	5	3	4
6.10	Does the audit regulator proactively seek to promote capacity, quality and governance improvements within audit firms? (This could include, among other things, requiring firms to meet a set of "audit quality indicators". Or creating an "audit firm governance code". Or pushing small firms to consolidate.)	2023	2	0	2	2	3	4	2.5	4	2	5	3.5	3.5
		2020	2	0	2	1	3	4	3	4	1	5	3	3
	2023 category score (out of 50)		41	24.5	41	34.5	32.5	41.5	36.5	46	31	41.5	41.5	39.5
	Category percentage (rounded)		82	49	82	69	65	83	73	92	62	83	83	79
	Rank		5	12	5	9	10	2	8	1	11	2	2	7

Source: ACGA



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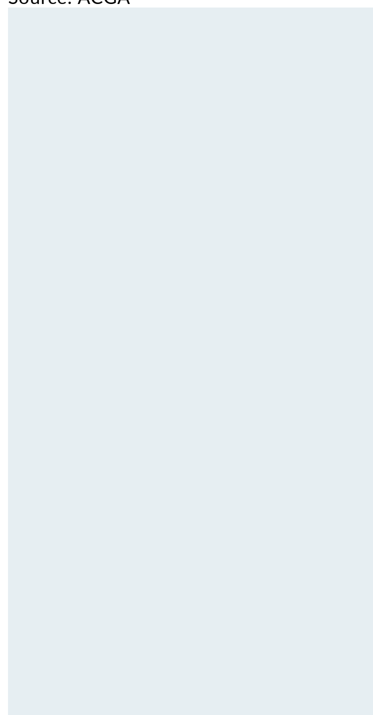
7. Civil society & media

			AU	CH	HK	IN	ID	JP	KR	ML	PH	SG	TW	TH
7.1	Is there a high quality provision of director training in the market, particularly through an institute of directors?	2023	5	2.5	5	3.5	4	5	0	5	4	5	4	5
		2020	5	2	4	3	3	5	0	4	4	5	3	5
7.2	Is there an institute of company secretaries (or equivalent) actively engaged in company secretarial training?	2023	5	1	4.5	5	4	1	1	5	0	4	1	4
		2020	5	1	4	5	4	1	0	5	0	4	2	5
7.3	Are other professional associations - of accountants, financial analysts and so on - helping to raise awareness of good corporate governance and ESG?	2023	4	1	2.5	3.5	2	3	1.5	2	2	3	3.5	0
		2020	4	2	3	3	1	3	1	1	2	3	2	0
7.4	Are business associations - chambers of commerce, business federations and investment industry bodies - working with their members to improve corporate governance and ESG?	2023	2.5	1	0.5	3.5	1	1.5	1	0	1	2	2.5	3
		2020	2	0	1	3	1	1	0	0	1	2	3	4
7.5	Are other non-profit organisations working to raise standards of corporate governance and ESG?	2023	5	1	2	4.5	2	4	5	2	1	1	4	1
		2020	5	0	3	5	2	5	5	3	2	1	5	1
7.6	Are these groups also involved in public policy discussions and consultations with a view to improving corporate governance and ESG?	2023	4	0	3.5	3.5	2	3	4	2	2	3	2	3
		2020	4	0	5	5	2	3	4	2	2	3	3	3
7.7	Are professional associations and academic organisations carrying out original and credible research on local CG practices?	2023	5	2	1.5	4	2	4.5	4	2	1	4	3.5	1
		2020	5	2	3	5	2	4	4	1	1	4	3	1
7.8	Is the media able to actively and impartially report on corporate governance policy developments and corporate abuses?	2023	3	1	1	3.5	2	4	2	3	2	3	4	2
		2020	3	1	2	4	1	3	1	2	2	3	4	2
7.9	Is the media sufficiently skilled at reporting on corporate governance?	2023	3.5	2	2	2.5	1	3.5	1	3	2	4	3.5	1.5
		2020	3	2	2	2	1	3	1	2	2	4	3	1
	2023 category score (out of 45)		37	11.5	22.5	33.5	20	29.5	19.5	24	15	29	28	20.5
	Category percentage (rounded)		82	26	50	74	44	66	43	53	33	64	62	46
	Rank		1	12	7	2	9	3	10	6	11	4	5	8

Source: ACGA



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Companies mentioned

Aeon (8267 JP - ¥3,262 - SELL)
Aichi Steel (N-R)
Aioi Dowa Insurance (N-R)
Aioi Nissay Dowa Insurance (N-R)
Aisan Industry (N-R)
Aisin (7259 JP - ¥6,118 - BUY)
Ajinomoto (2802 JP - ¥5,483 - SELL)
Alibaba (BABA US - US$69.61 - BUY)
ARM (N-R)
Asia Development Capital (N-R)
Asics (7936 JP - ¥6,755 - O-PF)
AVI (N-R)
Canon (7751 JP - ¥4,421 - U-PF)
Cellebrite (N-R)
Chuetsu Pulp & Paper (N-R)
Cosmo Energy Holdings (N-R)
Curi RMB Capital (N-R)
CyberAgent (4751 JP - ¥981 - O-PF)
Dai Nippon Printing (N-R)
Daifuku (6383 JP - ¥3,354 - BUY)
Daihatsu (N-R)
DAI-ICHI LIFE HOLDINGS (N-R)
Daiichi Sankyo (4568 JP - ¥4,556 - BUY)
Daio Kaiun (N-R)
Daio Paper (N-R)
Dalton (N-R)
DeNA (2432 JP - ¥1,524 - SELL)
Denso (6902 JP - ¥2,908 - U-PF)
DMG Mori Seiki (N-R)
Dream Incubator (N-R)
Ebara (6361 JP - ¥13,075 - O-PF)
Effissimo Capital Management (N-R)
Eisai (N-R)
Elliott (N-R)
EM Systems (N-R)
Fanuc (6954 JP - ¥4,510 - BUY)
Fast Retailing (9983 JP - ¥40,870 - U-PF)
Fujitec (N-R)
Fujitsu (6702 JP - ¥2,490 - O-PF)
Futaba Ind (N-R)
Gamecard-Joyco (N-R)
Glass Lewis (N-R)
GMO Internet (N-R)
GungHo (3765 JP - ¥2,250 - U-PF)
Hibiki Path (N-R)
Hino Motors (7205 JP - ¥499 - SELL)
Hisamitsu Pharma (N-R)
Hokuetsu Kishu (N-R)
Honda Motor (7267 JP - ¥1,813 - BUY)
House Foods (N-R)
Ibiden (4062 JP - ¥6,049 - U-PF)
Institutional Shareholder Services (N-R)
Israel Growth Partners Capital (N-R)
Isuzu Motors (7202 JP - ¥1,996 - SELL)
Ito Yokado (N-R)
Itochu (N-R)
JAL (N-R)
Japan Catalyst (N-R)
Japan Post Hldgs (N-R)
Japan Pulp & Paper (N-R)
Japan System Techniques (N-R)
Japan Tobacco (2914 JP - ¥4,100 - O-PF)
JGC (1963 JP - ¥1,549 - BUY)
J-Power (N-R)
JR Central (N-R)
JTekt (6473 JP - ¥1,386 - BUY)
Kaken Pharma (N-R)
Kansai Paint (4613 JP - ¥2,058 - BUY)
Kao (4452 JP - ¥6,257 - U-PF)
Kawasaki Kisen (N-R)
KDDI (9433 JP - ¥4,290 - U-PF)
Keisei Electric Rail (N-R)
Keyence (6861 JP - ¥65,200 - BUY)
Kito (N-R)
KKR (N-R)
Koito (7276 JP - ¥2,372 - O-PF)
Kokuyo (N-R)
Komatsu (6301 JP - ¥4,457 - BUY)
Konica Minolta (N-R)
KPP Group (N-R)
Kuri RMB Capital (N-R)
Kyocera (6971 JP - ¥1,918 - O-PF)
Kyoritsu Maintenance (9616 JP - ¥3,258 - BUY)
Lasertec (6920 JP - ¥40,620 - O-PF)
Leopard Asset Management (N-R)
Lone Star (N-R)
LY Corp (4689 JP - ¥359 - O-PF)
Macquarie (MQG AU - A$185.97 - O-PF)
Maersk (N-R)
Mandom (4917 JP - ¥1,290 - U-PF)
Marubeni (8002 JP - ¥2,670 - BUY)
Maruti Suzuki (MSIL IB - RS12,503.5 - O-PF)
MatsukiyoCocokara (3088 JP - ¥2,384 - BUY)
Mazda Motor (7261 JP - ¥1,776 - BUY)
Medipal (N-R)
MHI (7011 JP - ¥1,342 - O-PF)

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MIRI Capital Management (N-R)
Misaki Capital (N-R)
Misuga Kaiun (N-R)
Mitsubishi (N-R)
Mitsubishi Corp (8058 JP - ¥3,492 - BUY)
Mitsubishi Estate (8802 JP - ¥2,884 - U-PF)
Mitsubishi Fuso Truck & Bus (N-R)
Mitsubishi Motors (7211 JP - ¥497 - BUY)
Mitsubishi Paper (N-R)
Mitsui (8031 JP - ¥7,190 - O-PF)
Mitsui Fudosan (8801 JP - ¥1,622 - BUY)
Mitsui OSK Lines (N-R)
Mitsui Sumitomo (N-R)
Mitsui Sumitomo Insurance Co. Ltd. (N-R)
Mizuho (N-R)
Mizuho Financial (N-R)
Mochida Pharma (N-R)
MS&AD INSURANCE GROUP HOLDINGS (N-R)
Murakami Fund (N-R)
MUTB (N-R)
Nexon (3659 JP - ¥2,402 - BUY)
Nichido Fire Insurance (N-R)
Nidec (6594 JP - ¥6,787 - SELL)
Nintendo (7974 JP - ¥7,524 - SELL)
Nippon Express (9147 JP - ¥8,057 - U-PF)
Nippon Paper (N-R)
Nippon TV (N-R)
Nippon Yusen (N-R)
Nissan Motor (7201 JP - ¥579 - BUY)
NOK (N-R)
Nomura Real Estate (3231 JP - ¥4,173 - BUY)
NTT (9432 JP - ¥172 - U-PF)
Oasis (N-R)
Oasis (N-R)
Ocean Network Express (N-R)
Oji Paper (N-R)
Okayama Paper (N-R)
Olympus (7733 JP - ¥2,240 - O-PF)
Omron (N-R)
Oriental Land (4661 JP - ¥4,712 - O-PF)
Orix (N-R)
Otsuka Holdings (N-R)
Pan Pacific International (7532 JP - ¥3,772 - BUY)
Panasonic (6752 JP - ¥1,397 - BUY)
PeptiDream (N-R)
Pigeon (7956 JP - ¥1,409 - U-PF)
Rakus (3923 JP - ¥1,668 - U-PF)
Rakuten Group (4755 JP - ¥810 - U-PF)
Recruit (6098 JP - ¥6,487 - U-PF)
Renault (N-R)
Renesas (N-R)
Rengo (N-R)
Resona (N-R)
Round One (4680 JP - ¥696 - BUY)
Sankyo (N-R)
SBI (N-R)
Sekisui House (1928 JP - ¥3,434 - BUY)
Seven & I (3382 JP - ¥1,975 - U-PF)
Shin-Etsu Chemical (4063 JP - ¥6,320 - SELL)
SMBC (N-R)
SMFG (N-R)
SoftBank (N-R)
Softbank Corp (9434 JP - ¥1,854 - O-PF)
Softbank Group (9984 JP - ¥8,108 - O-PF)
SOMPO HOLDINGS (N-R)
Sompo Japan Insurance (N-R)
Sony Group (6758 JP - ¥12,935 - BUY)
Stanley Electric (6923 JP - ¥2,800 - BUY)
Steel Partners (N-R)
Strategic Capital (N-R)
Subaru (7270 JP - ¥3,531 - BUY)
Sun Corp (N-R)
Suzuken (N-R)
Suzuki (N-R)
Suzuki Motor (7269 JP - ¥1,786 - O-PF)
Taiho Kogyo (N-R)
Taisei (1801 JP - ¥5,294 - SELL)
Taisho Pharmaceutical (N-R)
Taiyo Pacific Partners (N-R)
Takara (N-R)
Takisawa (N-R)
TBS (N-R)
TechnoPro (6028 JP - ¥2,966 - BUY)
Terumo (4543 JP - ¥2,641 - BUY)
The Children's Investment Fund (N-R)
Third Point (N-R)
T-Mobile (N-R)
Tokai Rika (N-R)
Tokio Marine & Nichido Fire Insurance (N-R)
TOKIO MARINE HOLDINGS (N-R)
Tokushu Tokai Paper (N-R)
Tokyo Electron (8035 JP - ¥37,660 - BUY)
Tokyo Kikai Seisakusho (N-R)
Tokyu Fudosan (3289 JP - ¥1,167 - BUY)
Toppan Printing (N-R)
Toray (N-R)
Toshiba (N-R)
Tower Investment Management (N-R)

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Toyoda Gosei (N-R)
Toyota Boshoku (N-R)
Toyota Industries (6201 JP - ¥13,950 - U-PF)
Toyota Motor (7203 JP - ¥3,649 - BUY)
Toyota Tsusho (N-R)
TS Tech (N-R)
TV Asahi (N-R)
Uchida Yoko (N-R)
United Managers Japan (N-R)
Unizo (N-R)
Value Square (N-R)
ValueAct (N-R)
Varecs Partners (N-R)
Wacoal (N-R)
Whitebox Advisors (N-R)
Yamaha Motor (7272 JP - ¥1,392 - BUY)
Yaskawa Electric (6506 JP - ¥6,112 - U-PF)

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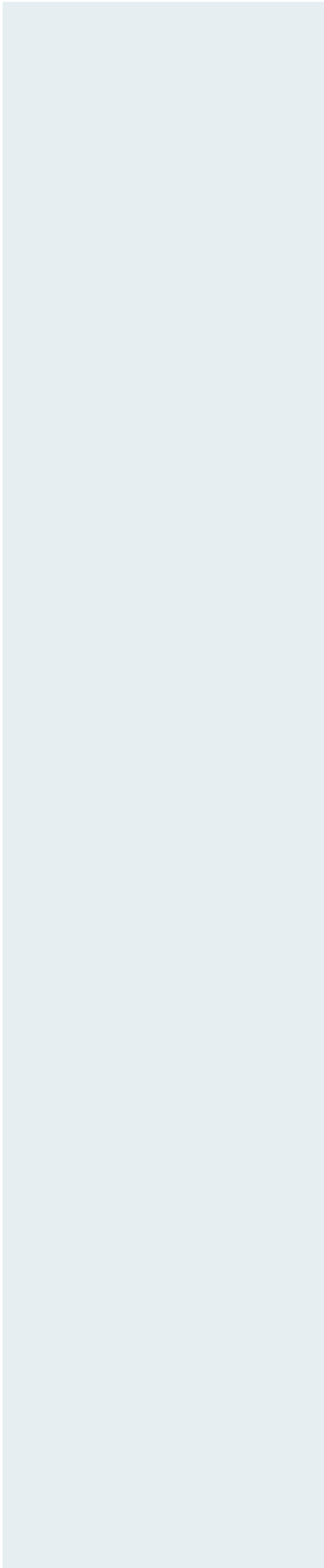

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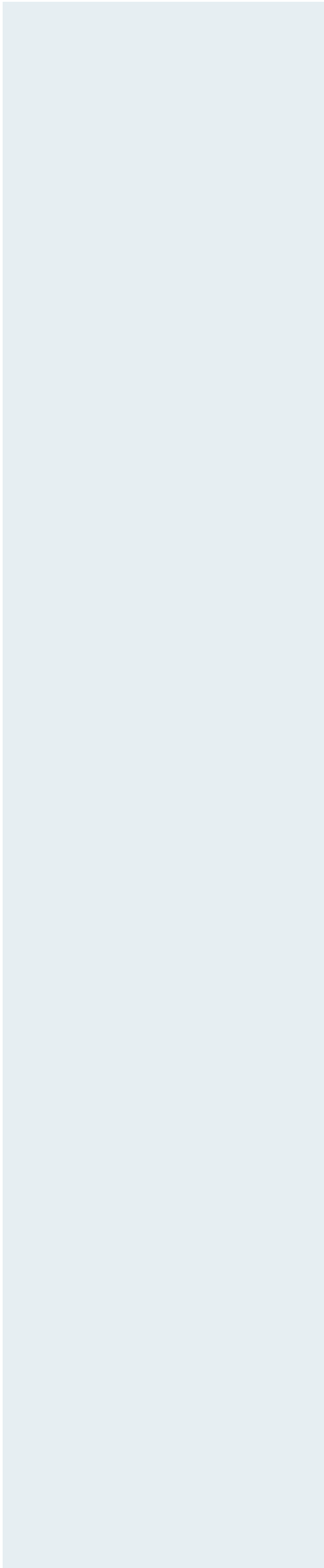

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