



Progress Report 2023

For Enhancing Asset Management Business in Japan

- Recommendations for Improving Trust and Transparency -

June 2023

Financial Services Agency

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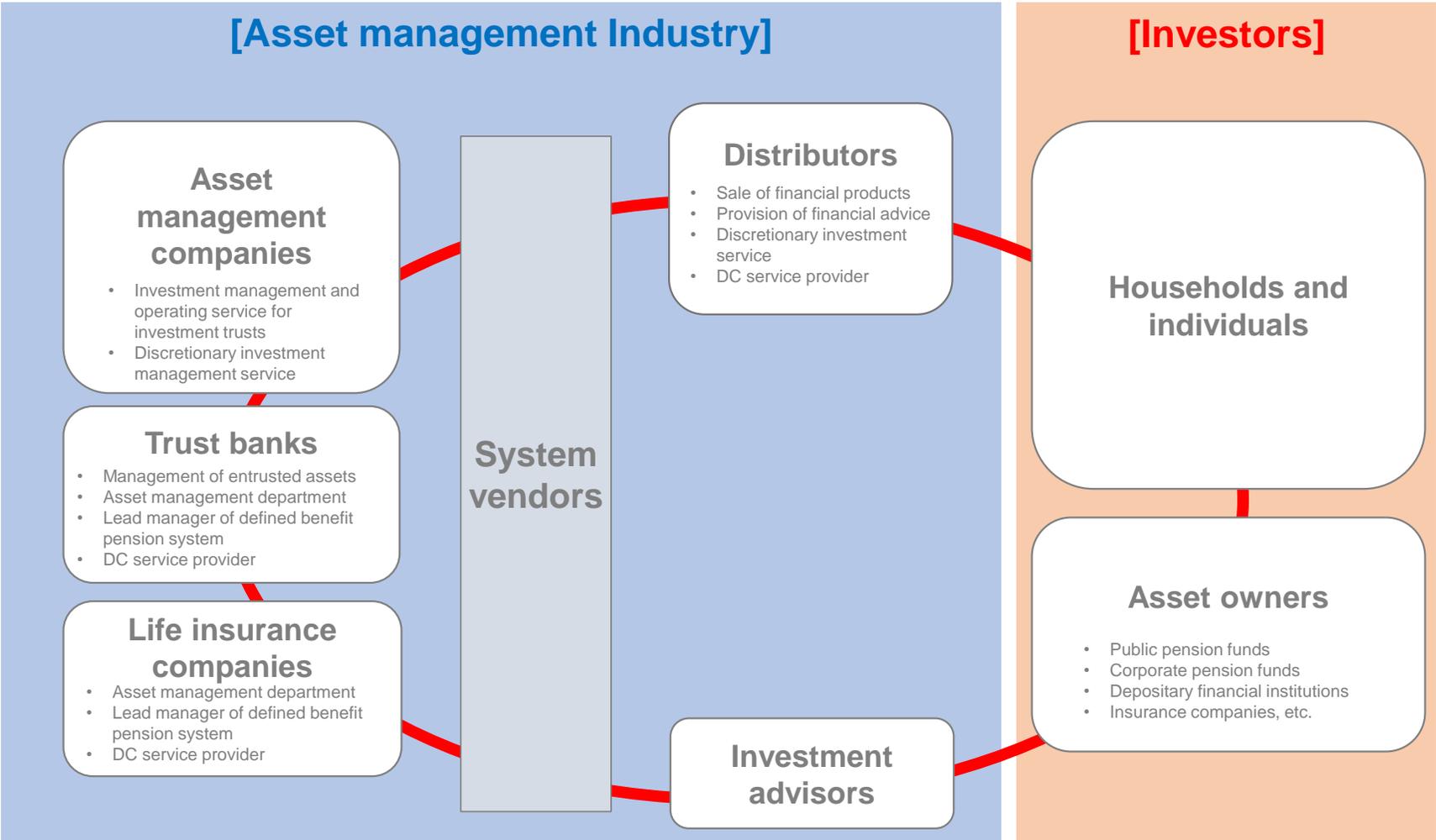
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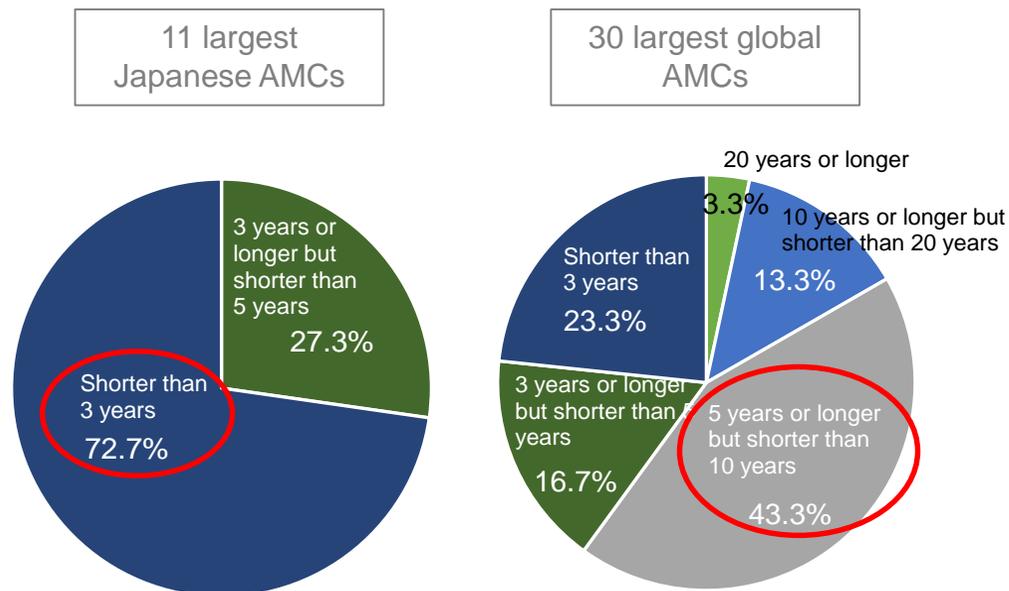
Asset Management Business in Japan

- Due to lack of service providers supporting back-office operations, asset management companies (hereinafter referred to as AMCs) have prepared full-functions for service in house, which has become a entry barrier. Since distributors have strong influence over AMCs' product development, which has discouraged competition among AMCs based on quality of investment management.
- Insufficient disclosure by AMCs and lack of expertise and human resources in many asset owners have also made it difficult for investors to differentiate AMCs by their capabilities.



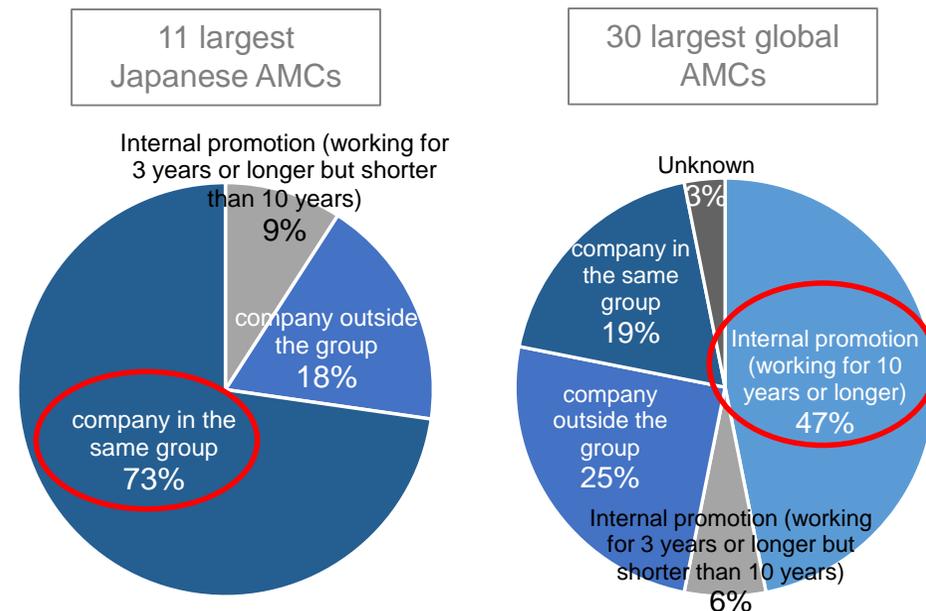
- Many CEOs of AMCs affiliated with large Japanese institutions have been in the position less than three years as of the end of December 2022. It is often the case that personnel transferred from parent companies become a CEO within three years after the transfer. Investor may have concerns that Japanese AMCs consider treatment of personnel is more important than their growth.
- Regarding global AMCs, CEOs who have been in the position for five years or longer and who got promoted internally are the largest in number.

[Figure 1] Terms of office of the CEOs of large AMCs



(Source) FSA, based on the data as of the end of December 2022 provided by AMCs for the 11 largest Japanese AMCs and based on the disclosure information on the AMCs' websites and news articles for the 30 largest global AMCs (including one Japanese AMC)

[Figure 2] Former positions of the CEOs of large AMCs

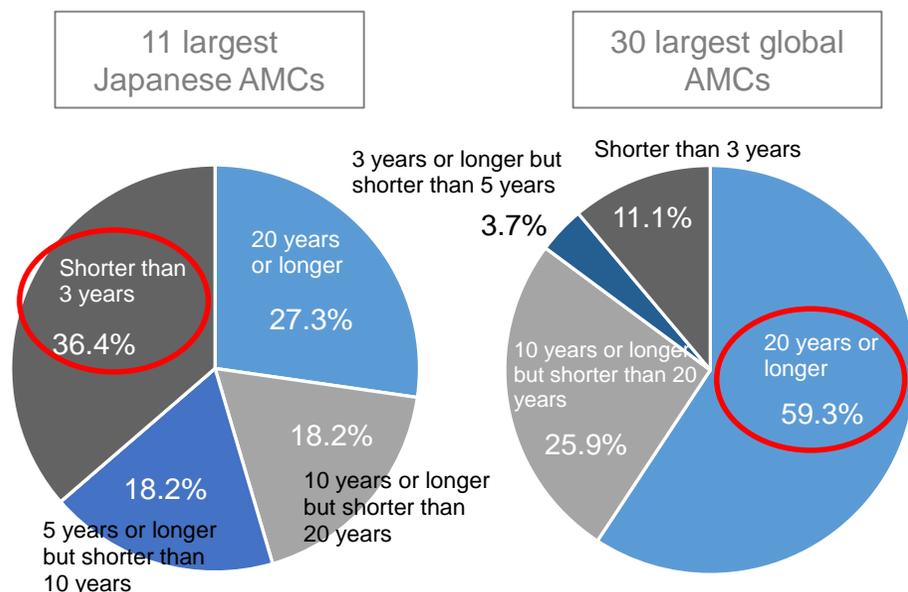


(Source) FSA, based on the data as of the end of December 2022 provided by AMCs for 11 largest Japanese AMCs and based on the disclosure information and news articles for 30 largest global AMCs (including one Japanese AMC)

(Note) Executives who worked for AMCs for three years or longer and got promoted to CEOs, are categorized into "internal promotion."

- Regarding largest Japanese AMCs, more than 30% of CEOs have less than three years of experience in AMCs. Among largest global AMCs, CEOs with experience of working for AMCs for longer than 20 years are the biggest in number, and the grounds for their appointments as CEOs are disclosed to the public.
- AMCs in Japan are also encouraged to develop internal succession plans and disclose grounds for appointing CEOs.

[Figure 3] Numbers of years working for AMCs before taking over a CEO position



(Source) FSA, based on the data as of the end of December 2022 provided by AMCs for 11 largest Japanese AMCs and based on the information on websites and news articles for 30 largest global AMCs (including one Japanese AMC)

(Note) The number of years working both for AMCs and department of management of entrusted assets in trust banks are counted as the "number of years of working experience in AMCs."

[Figure 4] Favorable examples of disclosure of grounds for appointment of CEOs of large global AMCs

He has 39 years of investment experience, all with our company

Under the planned succession, he will become our next CEO

She has a global mindset, and significant leadership experience in all facets of our operations

He's led our mutual fund department in the Asia-Pacific region, the United States, and Europe

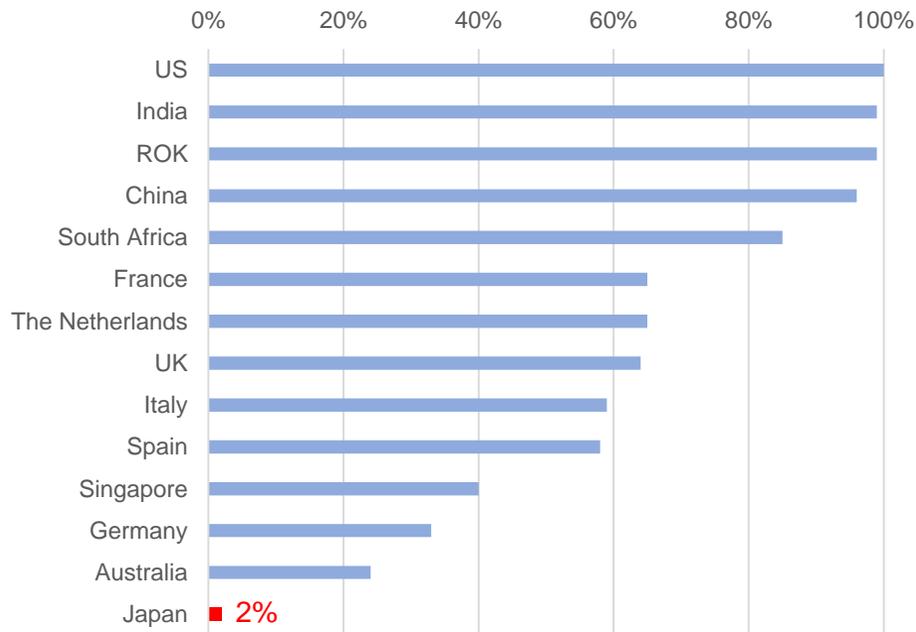
She has three decades of experience as an analyst, portfolio manager and CIO in the financial sector with global names

(Source) FSA, based on the information on the websites of 30 largest global AMCs

Transparency in Portfolio Management Teams

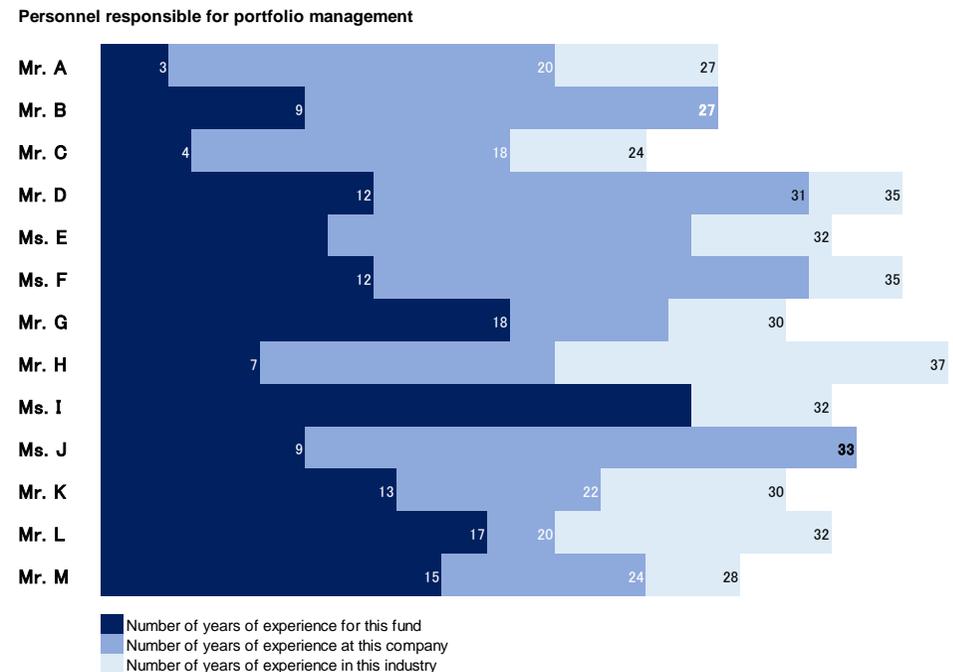
- Few AMC's disclose names and backgrounds of portfolio managers for each investment trust in Japan. Japan has the lowest percentage of funds where the names of fund managers are disclosed against the total number of funds compared with other countries.
- In reference to disclosure of global AMC's, Japanese AMC's are encouraged to initially start enhancing disclosure of portfolio management team of flagship funds and then expanding the scope.

[Figure 5] Percentage of mutual funds disclosing fund managers' names (against the total number of funds)



(Source) FSA, based on the "Global Investor Experience Study Disclosure" published by Morningstar (December 14, 2020)

[Figure 6] Favorable example of disclosure by a US AMC

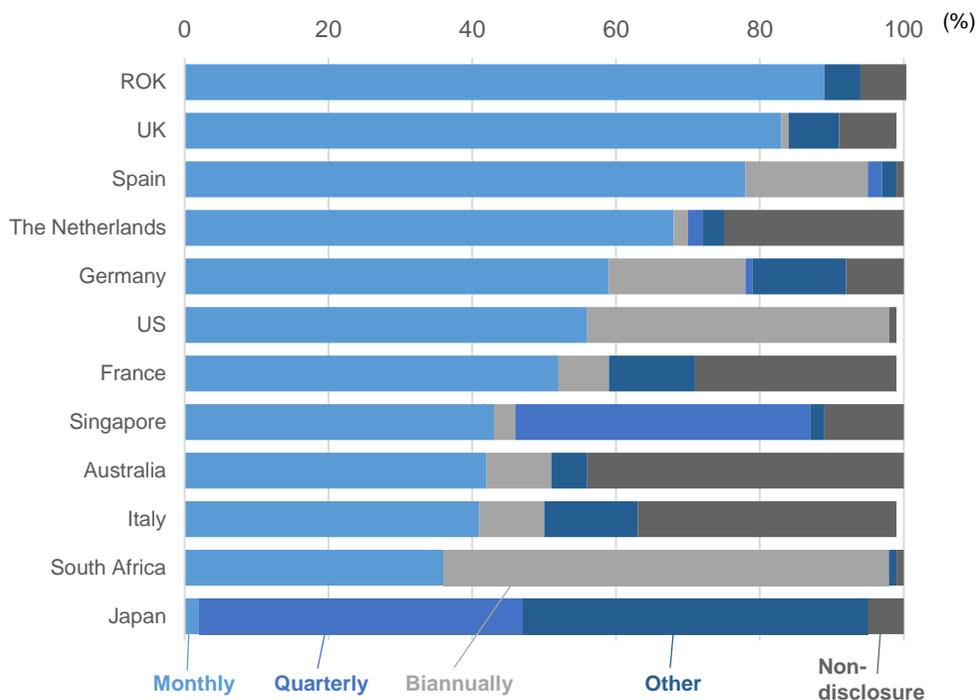


* Numbers in bold mean that the number of years of experience at the company and the number of years of experience in the industry are the same.

(Source) FSA, based on the website of a US AMC

- In many countries and regions, AMC's disclose holdings of mutual funds monthly or quarterly, but in Japan, the relevant information is disclosed only once or twice a year. Furthermore, foreign AMC's use HTML documents or Excel files for disclosure, but Japanese AMC's mainly use PDF files, which makes it difficult for investors or third parties to make secondary use of data.
- FSA expects the initiative from the self-regulatory body to propel data disclosure.

[Figure 7] Frequencies of disclosure of holdings by mutual funds in each country



(Source) FSA, based on the data of Ibbotson Associates Japan

[Table 8] Favorable example of the disclosure of holdings on the website of a US AMC

All issues held

All 370 issues: All | Equities | Bonds | Equivalent to cash | Investment funds

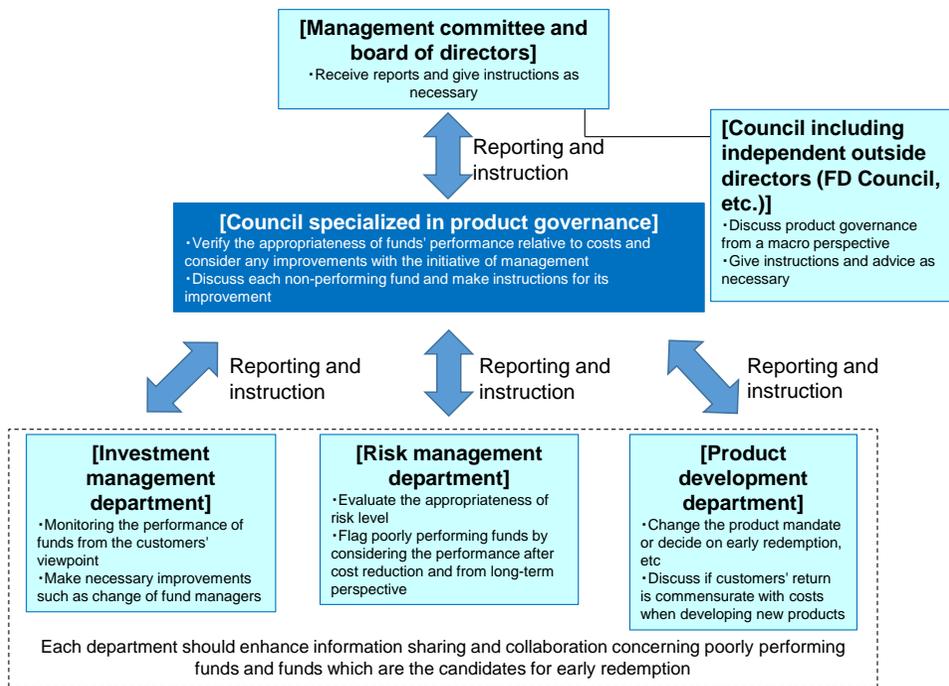
As of December 31, 2022

1-15 among all 370 issues				
Name of securities	Asset class	Number of equities	Market value	Weight (%)
Company T	Equities	170,302,358.00	\$17,028,532,818.00	8.75%
Company A	Equities	44,491,127.00	\$10,669,862,077.00	5.48%
Company M	Equities	12,485,588.00	\$6,619,609,046.00	3.40%
Company C	Equities	9,298,197.00	\$5,198,900,889.00	2.67%
Company D	Equities	54,890,751.00	\$4,610,823,084.00	2.37%
Company P	Equities	32,924,024.00	\$3,962,077,048.00	2.04%
Company B	Equities	12,615,067.00	\$3,719,930,957.00	1.91%
Company K	Equities	41,041,551.00	\$3,641,616,820.00	1.87%
Company Q	Equities	9,023,428.00	\$3,137,716,618.00	1.61%
Company W	Equities	24,020,059.00	\$2,958,790,868.00	1.52%
Company X	Equities	31,433,063.00	\$2,633,776,349.00	1.35%
Company Z	Equities	4,468,413.00	\$2,460,710,355.00	1.26%
Company I	Equities	27,076,457.00	\$2,388,955,801.00	1.23%
Company N	Equities	6,124,828.00	\$2,240,707,076.00	1.15%
Company O	Equities	4,064,213.00	\$2,199,971,468.00	1.13%

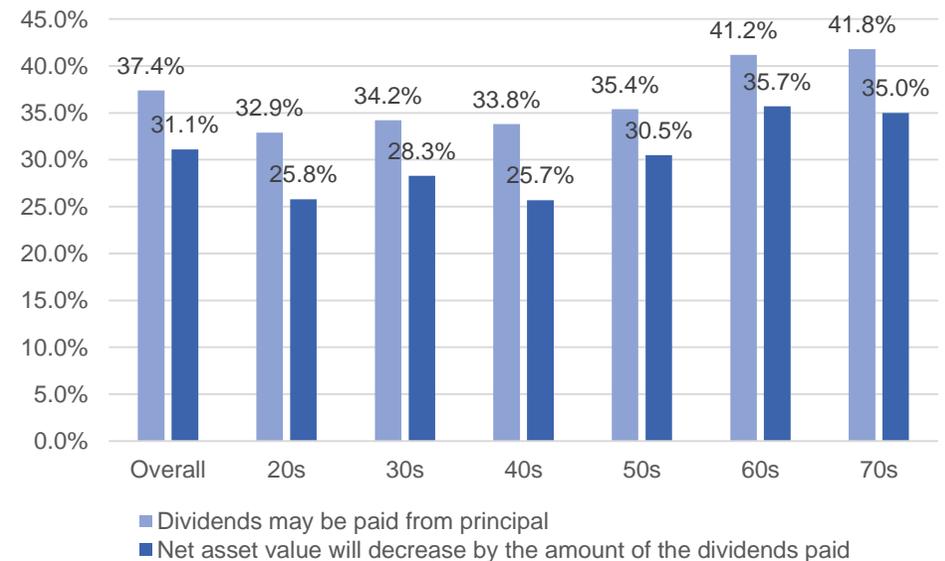
(Source) FSA, based on the website of a US AMC

- FSA encourages AMC to check regularly, (i) whether expected returns are commensurate with investors' cost, (ii) whether AMCs are managing investment trusts as originally planned and (iii) whether products are provided to originally targeted investors.
- Large AMCs have established product governance structures but have yet to ensure effectiveness. There are problems such that some AMCs have not set the criteria for flagging poorly performing investment trusts or that holders of investment trusts with monthly distributions are not fully aware of their significant characteristics.

[Figure 9] Example of a product governance structure



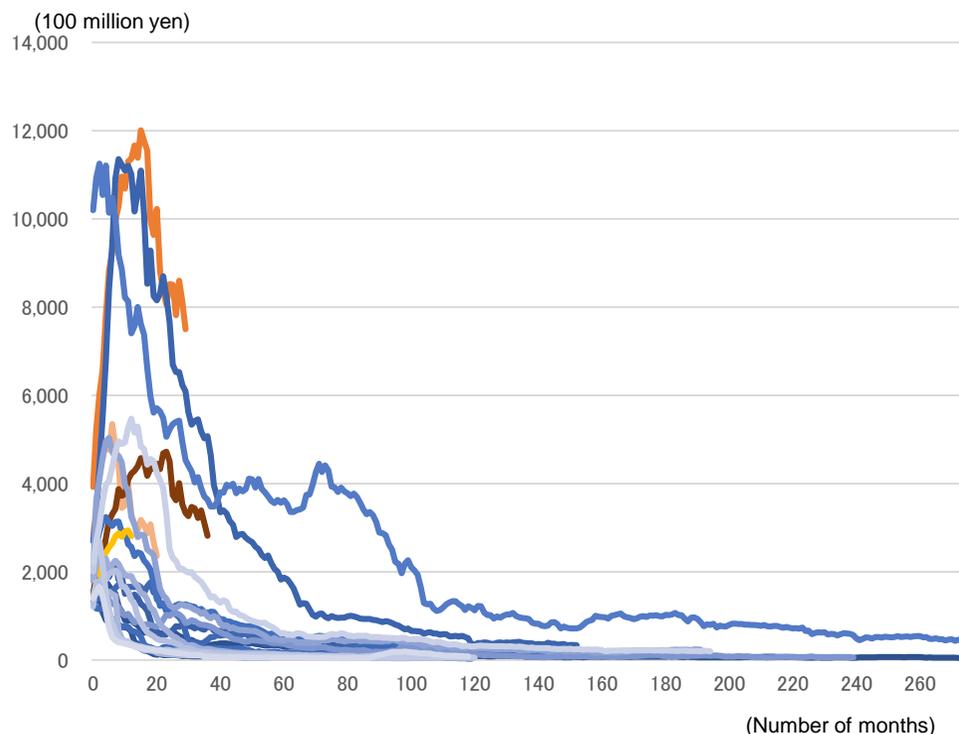
[Figure 10] Awareness concerning the significant characteristics of investment trusts with monthly distributions (among current and previous holders)



(Source) FSA, based on the "The Questionnaire Survey on Investment Trusts" (January 2023) by the Investment Trusts Association

- Most of the top 20 publicly offered investment trusts by initial amount of net assets have been rapidly declining in assets several months to one and a half years after launch. Most of them are old investment trusts, but similar trends are also observed for investment trusts that were established within the last five years. Due to such irresponsible product origination and sales, there are a number of investment trusts remained in the industry, which has added cost and operational burden for AMCs.
- Distributors are encouraged to focus on advice for building customers' assets, not on selling as many products as possible.

[Figure 11] Change in net assets of the top 20 investment trusts by initial amount of net assets



(Source) FSA, based on the QUICK data

(Note) The figure covers publicly offered open-ended equity funds in Japan (excluding ETFs) that had been ranked in the top 20 in terms of initial amounts as of the end of December 2022. Funds which were already redeemed are also included. For all covered funds, the figure shows changes in the balance starting from the end of the initial month (= 0), on a monthly basis. Funds colored other than blue are those established within the last five years.

[Table 12] International comparison of the number of mutual funds and the total AUM

	Japan	US	Luxembourg
[A] Assets under management (million dollars)	2,040,234	28,586,853	5,363,351
[B] Number of funds (pieces)	14,297	10,237	14,322
[A]/[B] Assets under management per fund (million dollars)	143	2,793	374

(Source) FSA, based on the IIFA's Q4 data in 2022

[Figure 13] Provision of advice for asset building

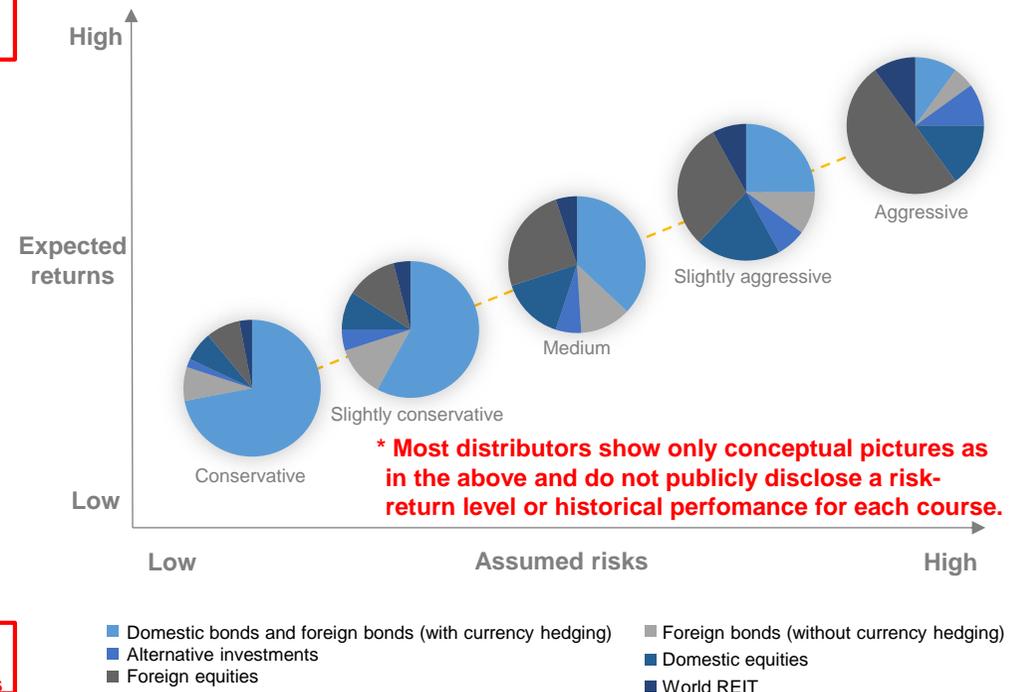
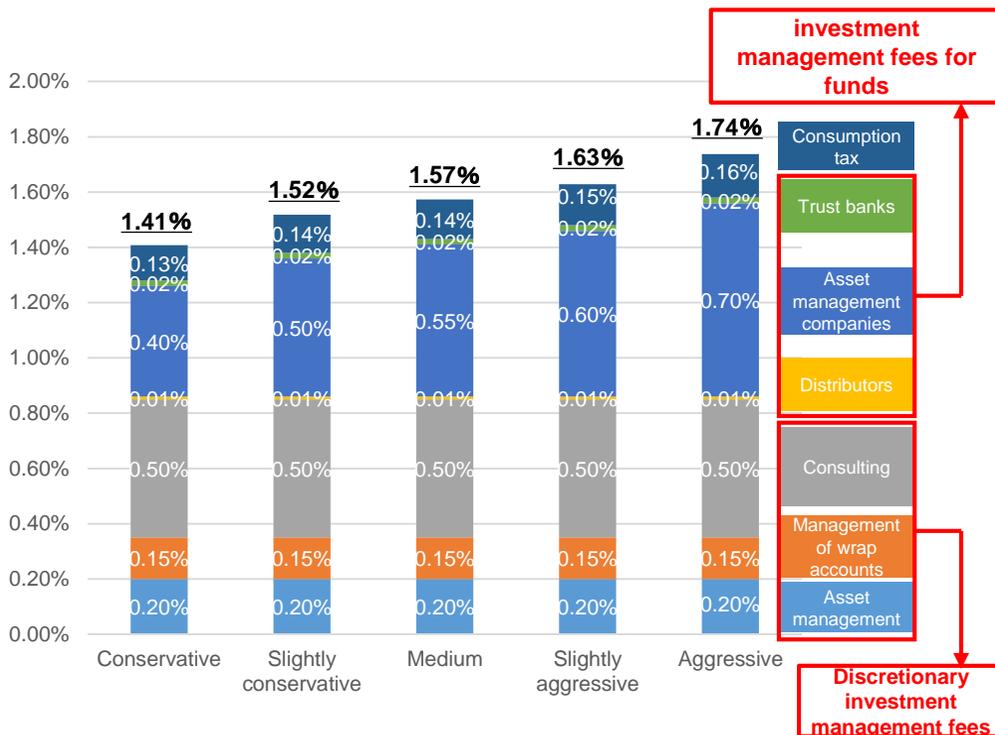


The Added Value of Fund Wrap Services

- Fund wrap services have been expanding in Japan. Some financial institution provides the service for a wide range of customers, by setting the minimum amount for the service at one million yen. However, without detailed disclosure, it is not clear whether fund wrap service is just a product combining multiple investment trusts or the service including provision of regular advice.
- In expanding the services to the mass market, financial institutions are encouraged to disclose the information regarding investment management teams, historical performance after cost deduction, composition of fees as well as the nature of the services.

[Figure 14] Favorable example of disclosure of fee structure

[Figure 15] Unfavorable example of disclosure of risk-return level



(Source) FSA, based on the marketing material of a financial institution

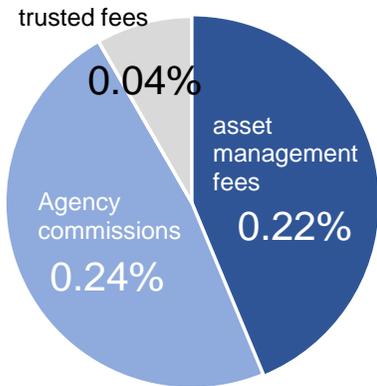
(Source) FSA, based on the websites and marketing materials of financial institutions

- Traditionally, almost half of investment management fees are split equally between AMCs and distributors regardless of whether investment trusts are managed passively or actively. Explanations regarding the services corresponding to the distributors' share of investment management fees are mostly the same among investment trusts although it is higher if they are actively managed.
- In the US, the average distributors' share from investment management fees is the same level for both active and passive funds.
- It is expected that reasonable explanations are made to customers regarding the services corresponding to the distributors' share.

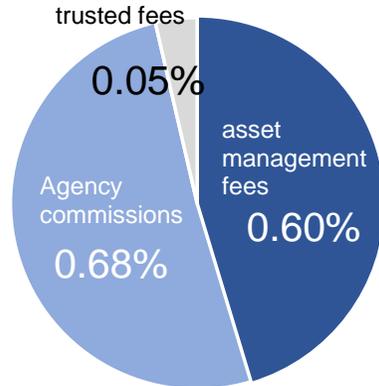
[Figure 16] Share of investment management fees



Average share for passive funds

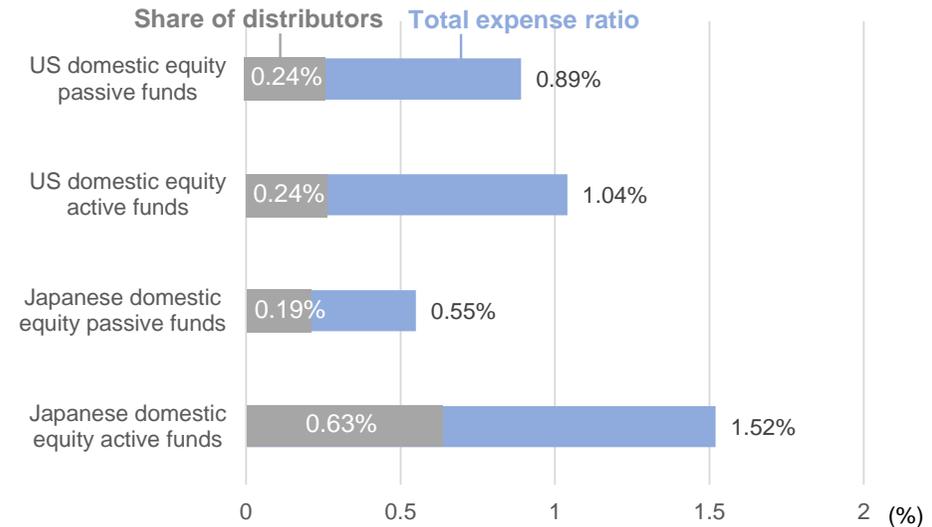


Average share for active funds



(Source) FSA, based on the QUICK data as of the end of December 2022; excluding ETFs, wrap funds and DC funds. The figures are simple average, excluding outsourced management fees.

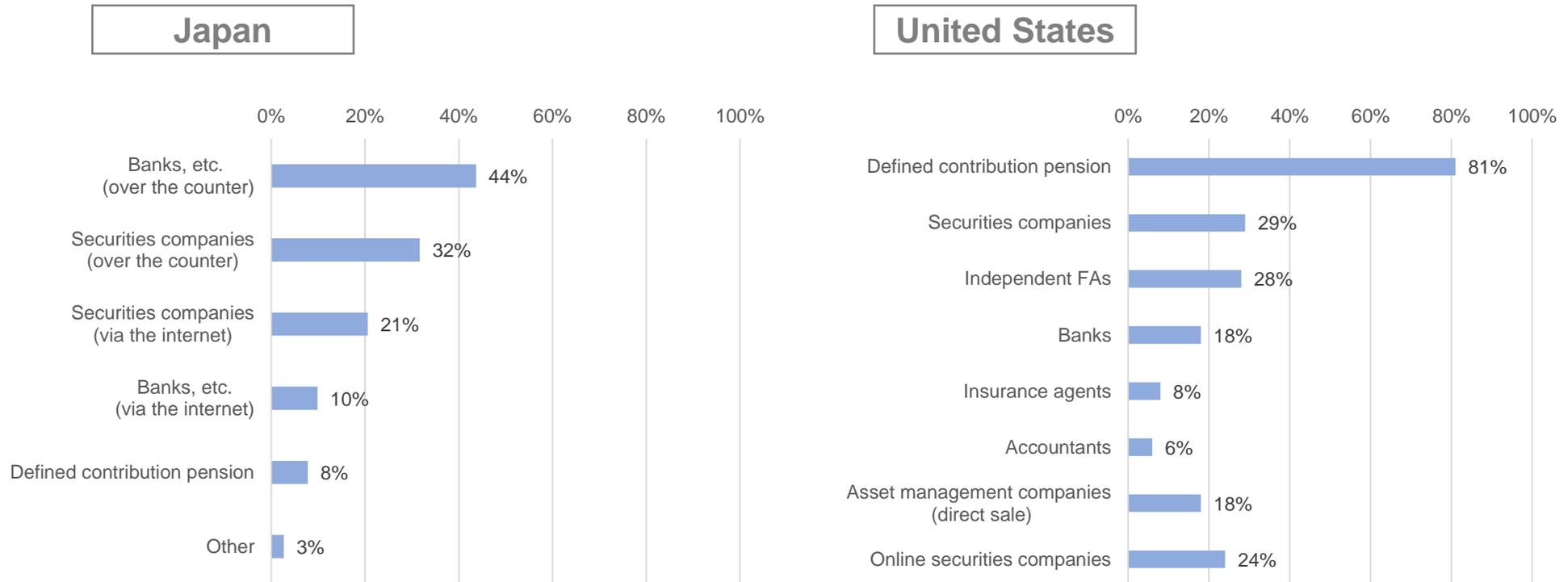
[Figure 17] Average of total expense ratios and distributors' share for investment trusts in Japan and mutual funds in the US



(Source) FSA, based on the data provided by Ibbotson Associates Japan as of the end of December 2022; For US funds, the data of A share is used. The "share of distributors" corresponds to the ratio of 12b-1 fees for US funds and that of agency commissions for Japanese funds in the total expense ratios. The figures are simple average.

- In order to promote a shift from savings to investment, it is important to diversify distribution channel. Compared with in the United States, the percentages of households or individuals who purchased mutual funds through the defined contribution (DC) pension system, or from independent financial advisors (FAs) or directly from AMC are small in Japan.
- In order to increase FAs, it is necessary that more financial institutions offer digital platforms to financial instruments intermediaries and investment trusts such as active ETFs, of which agency commissions are low, become widespread.

[Figure 18] Comparison of distribution channels of retail mutual funds between Japan and the US (numbers of investors by percentage, multiple answers permitted)

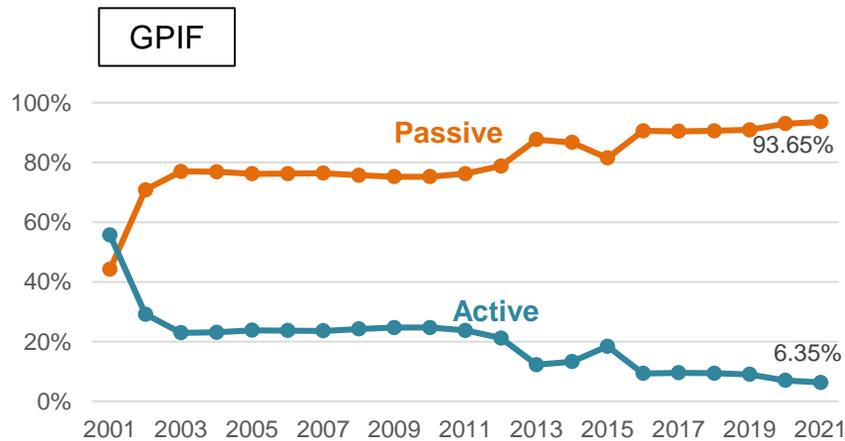


(Source) FSA, based on "Investment Company FACT BOOK 2022" published by the ICI Research Report and "FY2021 National Survey on Securities Investment (individual survey)" published by the Japan Securities Dealers Associations

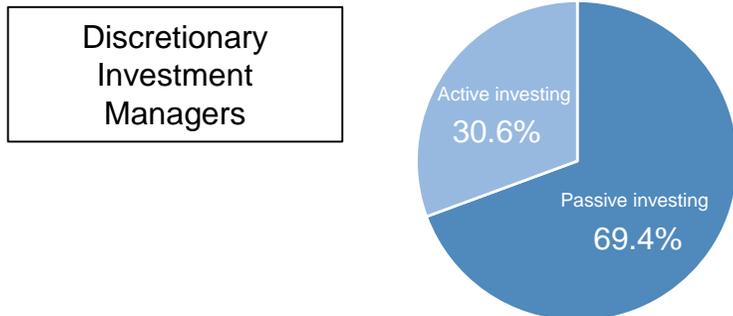
The Added Value of Actively Managed Funds

- The share of passive investing to active investing in Japanese equities is high in the portfolio of institutional investors.
- However, statistics shows that the percentage of actively managed large-cap retail funds that beat their respective benchmark index is higher in Japan than in the US and the EU.
- This means there is more opportunity for AMCs in Japan to increase the volume of actively managed funds in order for improving inefficiency in the capital market as well as increasing their management fees.

[Figure 19] Investment strategies selected by institutional investors of Japanese equities

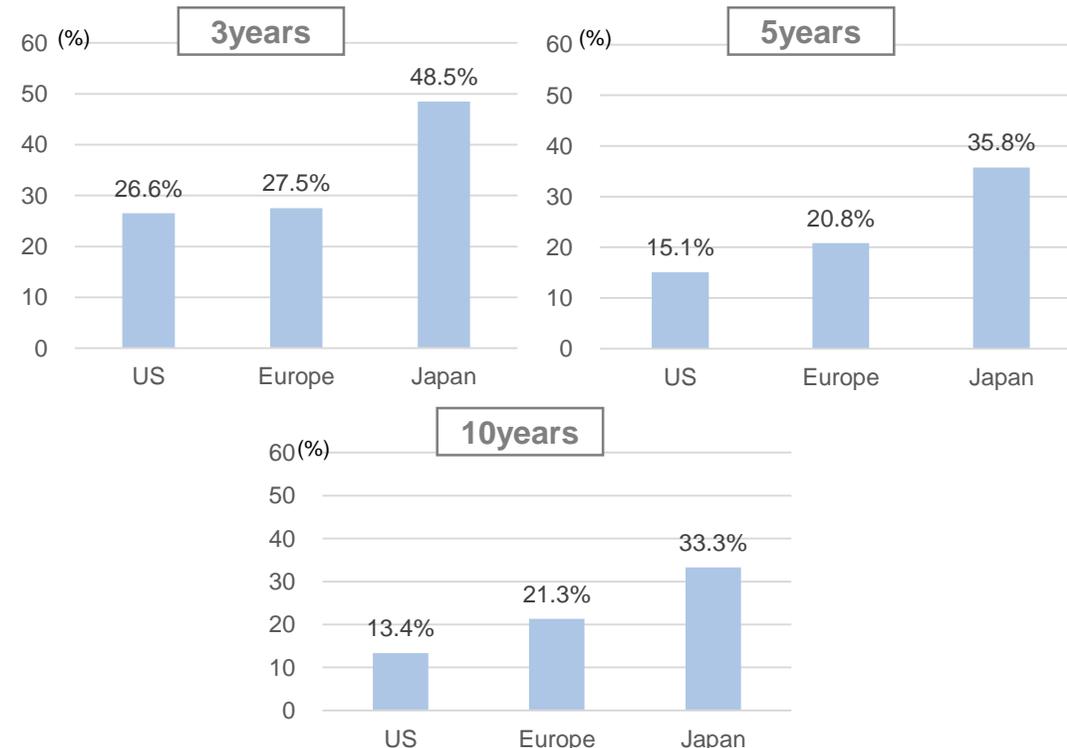


(Source) the FSA, Japan, based on the data published by the GPIF



(Source) FSA, based on the results of the questionnaire survey by the Japan Investment Advisers Association

[Figure 20] Percentage of actively managed large-cap funds that beat their respective benchmark index in Japan, the US and the EU



(Source) FSA, based on the data of Ibbotson Associates Japan. Benchmarks refer to TOPIX (including dividends) for Japan, S&P500 (including dividends) for the United States, and MSCI Europe (net; dollar-based) for Europe. This analysis is done using the data after deducting investment management costs as of the end of December 2022.

Data Disclosure for Evaluating Stewardship Activities

- For evaluating the effectiveness of stewardship activities, the results of AMC's exercise of voting rights are useful, but many AMCs disclose the results in the form of PDF files and it is difficult for third parties to compare and analyze data of multiple AMCs.
- In order to facilitate evaluation of the effectiveness of the AMC's stewardship activities and further promote their dialogues with corporates, AMCs are encouraged to promote data disclosure.

[Table 21] Disclosure of the results of the exercise of voting rights by case (at present, disclosed in the form of PDF files)

[Table 22] Comparison of the results of the exercise of voting rights by case (when the data is disclosed in the future)

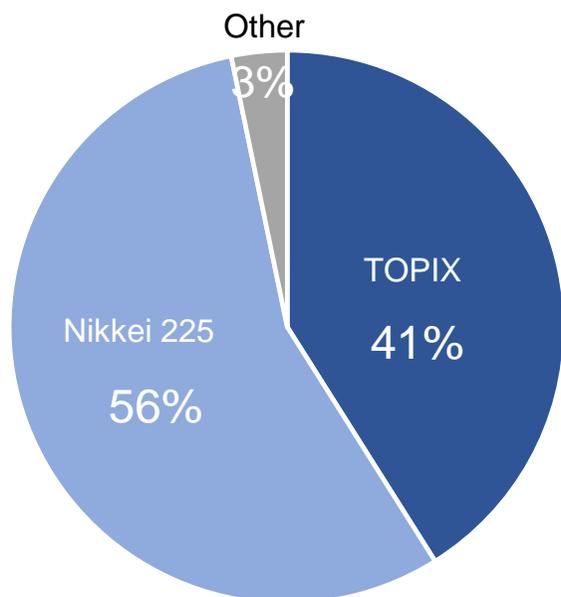
Enterprise code	Enterprise name	GM	Meeting date	Proposer	Proposal number	Category of proposal	Pros and cons/Reason	
xxxx	○○ Trading Co.	Ordinary	June 24, 2022	Company	1	Appropriation of surplus	Pro	Pro in line with the company's standards
xxxx	○○ Trading Co.	Ordinary	June 24, 2022	Company	2	Proposal concerning the articles of incorporation	Pro	Pro in line with the company's standards
xxxx	○○ Trading Co.	Ordinary	June 24, 2022	Company	3.1	Appointment or dismissal of a director	Pro	Pro in line with the company's standards
xxxx	○○ Trading Co.	Ordinary	June 24, 2022	Company	3.2	Appointment or dismissal of a director	Pro	Pro in line with the company's standards
xxxx	○○ Trading Co.	Ordinary	June 24, 2022	Company	3.3	Appointment or dismissal of a director	Pro	Pro in line with the company's standards
xxxx	○○ Trading Co.	Ordinary	June 24, 2022	Company	3.4	Appointment or dismissal of a director	Pro	Pro in line with the company's standards
xxxx	○○ Trading Co.	Ordinary	June 24, 2022	Company	3.5	Appointment or dismissal of a director	Pro	Pro in line with the company's standards
xxxx	○○ Trading Co.	Ordinary	June 24, 2022	Company	3.6	Appointment or dismissal of a director	Pro	Pro in line with the company's standards
xxxx	○○ Trading Co.	Ordinary	June 24, 2022	Company	3.7	Appointment or dismissal of a director	Pro	Pro in line with the company's standards
xxxx	○○ Trading Co.	Ordinary	June 24, 2022	Company	3.8	Appointment or dismissal of a director	Pro	Pro in line with the company's standards
xxxx	○○ Trading Co.	Ordinary	June 24, 2022	Company	4.1	Appointment or dismissal of an auditor	Con	The proposal does not satisfy the company's standards concerning independence.
xxxx	○○ Trading Co.	Ordinary	June 24, 2022	Company	4.1	Appointment or dismissal of an auditor	Pro	Pro in line with the company's standards
◆◆◆◆	△△	Ordinary	June 15, 2022	Company	1	Appropriation of surplus	Con	Effects f or boosting shareholder value or enhancing governance cannot be confirmed.
◆◆◆◆	△△	Ordinary	June 15, 2022	Company	2	Proposal concerning the articles of incorporation	Pro	The proposal is considered to contribute to boosting shareholder value or enhancing governance.
◆◆◆◆	△△	Ordinary	June 15, 2022	Company	3.1	Appointment or dismissal of a financial auditor	Con	Effects f or boosting shareholder value or enhancing governance cannot be confirmed.
◆◆◆◆	△△	Ordinary	June 15, 2022	Company	4	Payment of retirement allowance to a retired officer	Con	Governance concerning remuneration has not been developed.
◆◆◆◆	△△	Ordinary	June 15, 2022	Shareholder	6	Proposal concerning the articles of incorporation	Con	Effects f or boosting shareholder value or enhancing governance cannot be confirmed.
◆◆◆◆	△△	Ordinary	June 15, 2022	Shareholder	7	Proposal concerning the articles of incorporation	Con	Effects f or boosting shareholder value or enhancing governance cannot be confirmed.
◆◆◆◆	△△	Ordinary	June 15, 2022	Shareholder	8.1	Appointment or dismissal of an auditor	Con	Effects f or boosting shareholder value or enhancing governance cannot be confirmed.
◆◆◆◆	△△	Ordinary	June 15, 2022	Shareholder	8.2	Appointment or dismissal of an auditor	Con	Effects f or boosting shareholder value or enhancing governance cannot be confirmed.

(Legend: "Pro" means being for a shareholders' proposal, "Con" means being against a shareholders' proposal, and "-" means no exercise of voting rights.)

Enterprise name	Proposal	Approval rate	○○AM	xxAM	△△AM	□□AM	●● Insurance	▲▲ Insurance
A Sangyo Co., Ltd.	Change of the articles of incorporation	23.7%	Pro	Pro	Pro	Con	Con	Pro
	Appointment of a director	28.6%	Con	Con	Pro	Pro	Con	Pro
B Kogyo Co., Ltd.	Share split	22.9%	-	Con	Con	Pro	Pro	Con
		43.6%	Pro	-	-	Con	-	Pro
C Manufacturing Co., Ltd.	Change of the articles of incorporation	31.7%	Con	Con	Pro	-	-	Con
	Acquisition of treasury shares	46.2%	Pro	-	Pro	Pro	Pro	Pro
D Real Estate Co., Ltd.	Appointment of an auditor	37.2%	-	Pro	Pro	Con	Con	Pro
		11.5%	Con	Con	Con	Con	Con	-
E Holdings Co., Ltd.	Change of the articles of incorporation	19.5%	Pro	Con	Pro	Pro	Con	Con
	Revision of directors' remunerations	35.6%	Pro	Pro	Con	Pro	Pro	Pro
F Trading Co., Ltd.	Appropriation of surplus							
	Acquisition of treasury shares							

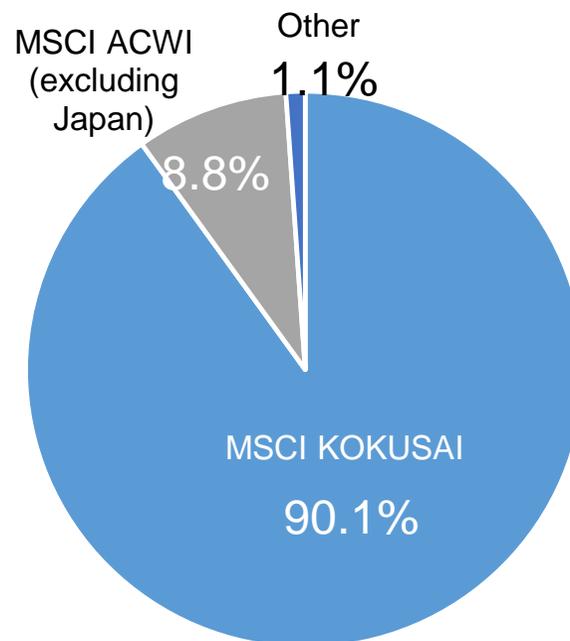
- Very limited indices are used for passively managed investment trusts. While investment management fees of index funds are decreasing in Japan, it is pointed out that some of index usage fees paid to index providers have been increasing year by year.
- In order to develop sustainable business models, AMCs should review grounds for selecting specific indices and also the way of setting investment management fees.

[Figure 23] AUM share of index of Japanese equities used for passively managed investment trusts



(Source) FSA, based on the QUICK data of investment trusts excluding ETFs as of the end of December 2022

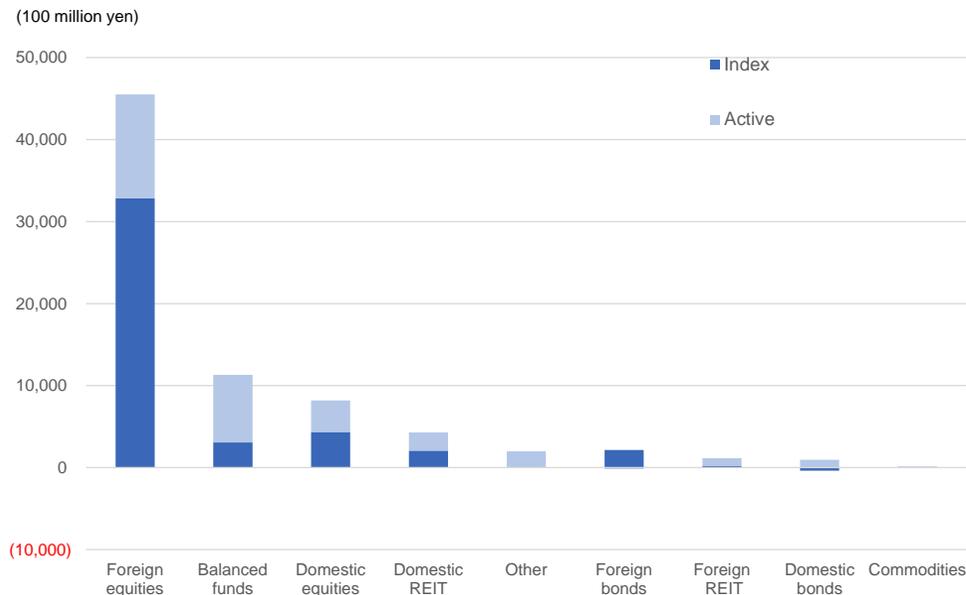
[Figure 24] AUM share of index of global equities used for passively managed investment trusts



(Source) FSA, based on the QUICK data of investment trusts excluding ETFs as of the end of December 2022

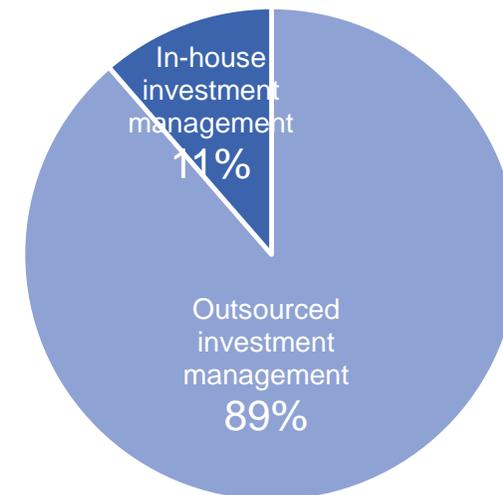
- Approximately 61% of total cash inflow into publicly offered investment trusts flew into global equities in 2022, and the investment decision of nearly 90 % of actively managed investment trusts are outsourced to AMCs based abroad. If such trend expands, it is likely that the AUM of AMCs in Japan may decrease and thus their investment management functions may deteriorate.
- AMCs are encouraged to enhance in-house investment management capabilities, for example, by hiring necessary human resources to manage global assets.

[Figure 25] Cash inflow in publicly offered investment trust in 2022 by types of invested assets



(Source) FSA, based on the data of QUICK; Tabulated based on the estimated amount of cash inflow for one year as of the end of December 2022

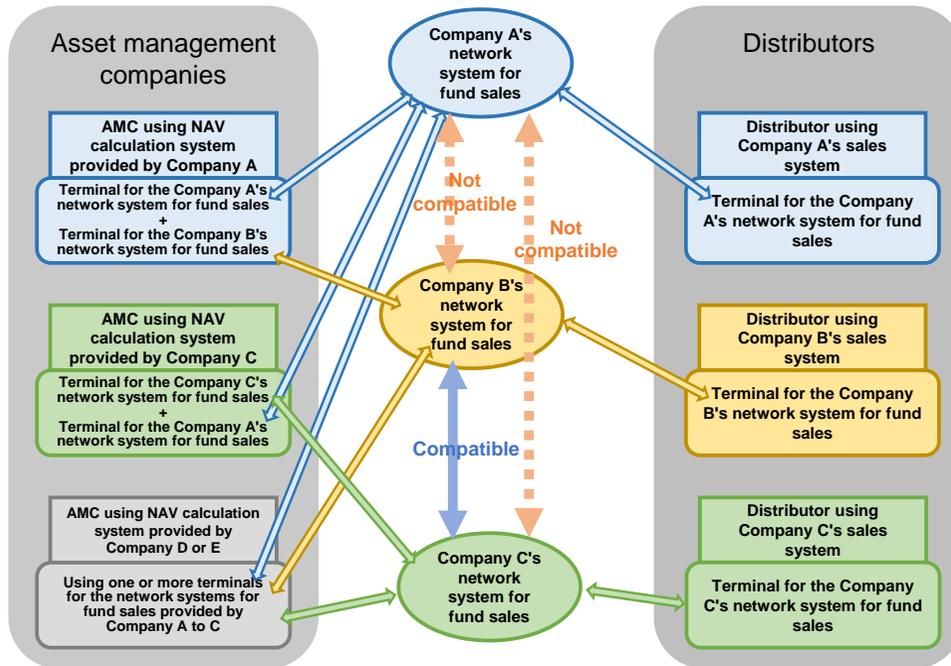
[Figure 26] Ratios of in-house vs. outsourced investment decision for global equity actively managed funds in AUM



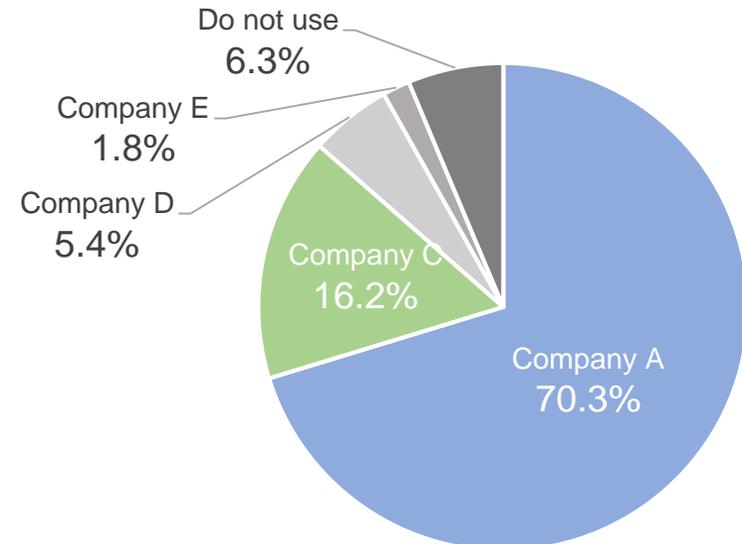
(Source) FSA, based on the QUICK data on investment trusts excluding ETFs, DC funds and SMA funds. Global equity (including domestic equity) active funds that were managed by Japanese AMCs as of the end of December 2022 and that are ranked in the top 100 in AUM are categorized into those under in-house investment management or those under outsourced investment management by the FSA's judgement.

- The network systems for fund sales which enable electronic communication between AMCs and distributors on investment trusts are operated by a small number of IT vendors. Lack of compatibility in data linkage among the network systems requires manual work or multiple network terminals for AMCs. Two IT vendors are also dominant players in the market of net asset value (NAV) calculation systems of investment trusts because those systems are usually sold to AMCs together with the network terminals.
- The Investment Trust Association, in collaboration with the FSA, is encouraged to take actions to resolve this inefficiency.

[Figure 27] The network systems for fund sales



[Figure 28] Market share of NAV calculation system (number of AMC users)

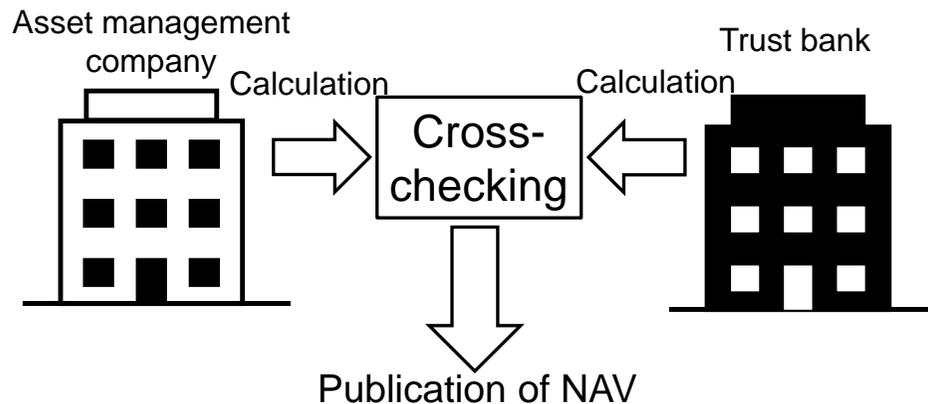


(Source) FSA, based on the attachment to the document, "Request for Improving Connection of the Network Systems for Fund Sales," (February 7, 2019) published by the Working Group on Streamlining Business Operations for Investment Trusts under the Investment Trusts Association

(Source) FSA, based on the data provided by AMCs as of the end of July 2022

- The Japanese unique business practice which requires AMCs and trust banks to respectively calculate net asset values (NAVs) of investment trusts and cross-check the results of calculation every day (double-check calculation) remained, and this is recognized as a factor increasing cost for AMCs by introducing NAV calculation system and hiring IT or fund accounting staff by themselves.
- Introduction of a single-party calculation framework under the initiative of trust banks as well as the Investment Trust Association is encouraged for AMCs to benefit from economies of scale in back-office operation and to lower the barriers to entry for new AMCs.

[Figure 29] Figure describing double-check calculation of Net Asset Value (NAV)



Neither industry-common materiality rule exists nor a single penny of error is allowed in NAV calculation

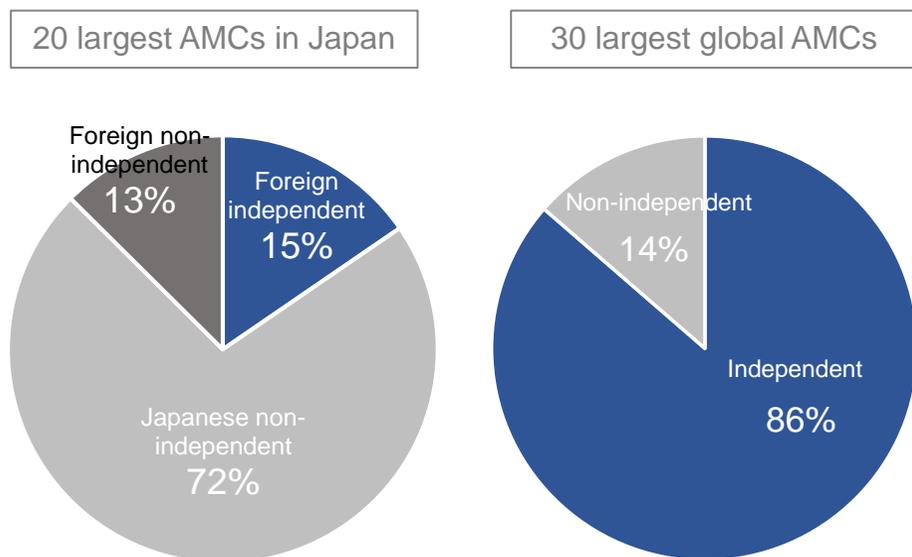
[Figure 30] Change in the number of AMCs in Japan



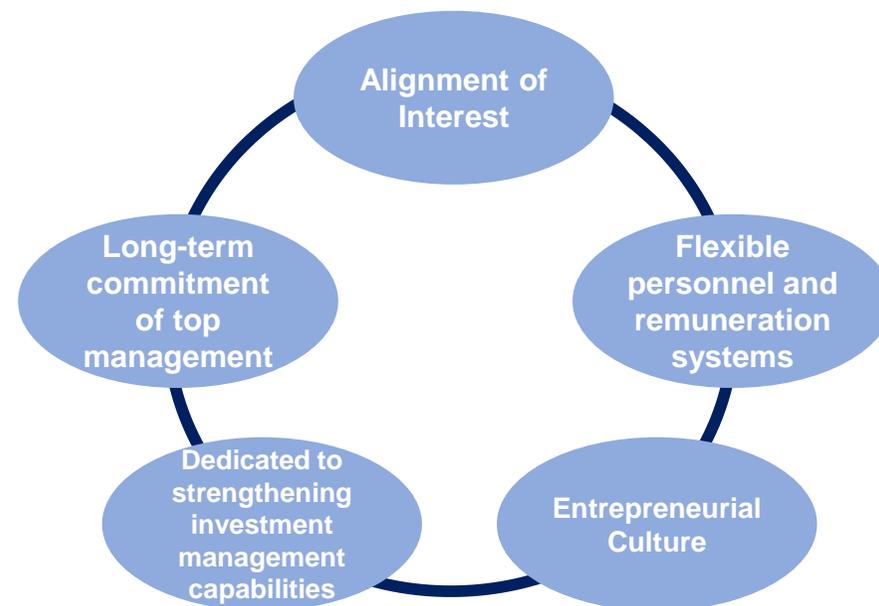
(Source) FSA, based on the FSA's Annual Report

- Independent AMCs, which do not belong to financial institutions have grown in AUM in the world. There is a survey showing that annual performance of independent AMCs is higher than that of non-independent AMCs by 0.62% on average. However, in Japan, independent AMCs have not been able to be dominant players.
- Even non-independent AMCs are encouraged to establish their managerial independence from their parent groups and to make their personnel and remuneration systems more flexible in order to hire more talents in investment management teams.

[Figure 31] Share of independent and non-independent AMCs in AUM



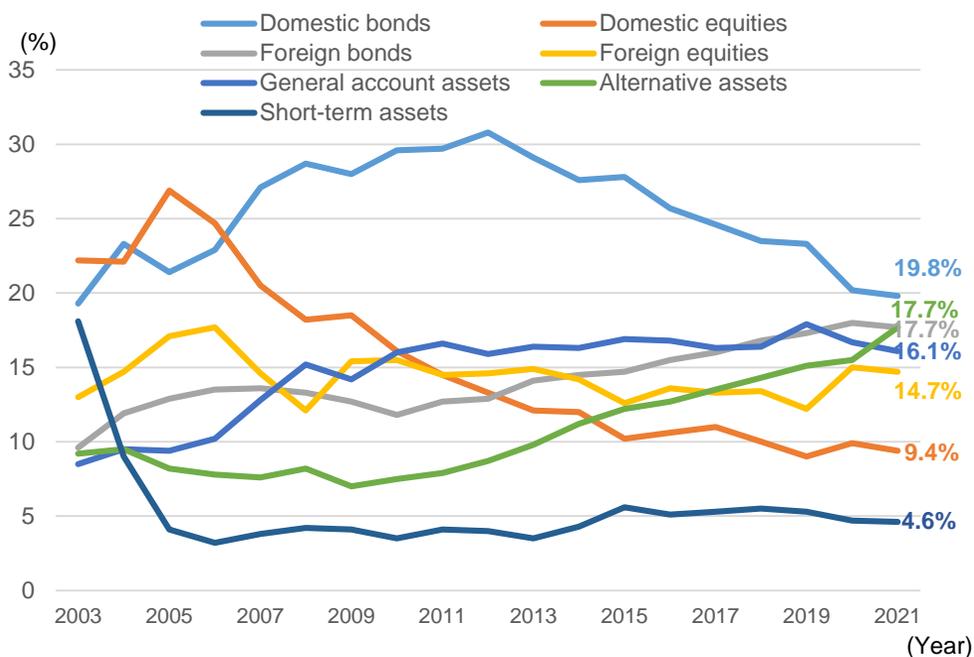
[Figure 32] Strengths of independent AMCs



(Source) FSA. The pie chart for 20 largest AMCs in Japan is based on the data as of the end of March 2022 provided by AMCs. The chart covers AMCs that hold domestic publicly offered investment trusts, privately placed investment trusts, and discretionary investment management agreements and are ranked in the top 20 in terms of the total amounts of those entrusted assets. The pie chart for 30 largest global AMCs covers companies that are ranked in the top 30 in terms of the total amounts of open-end mutual funds and ETFs under their management. Categorization of independent and non-independent is based on the FSA's judgment.

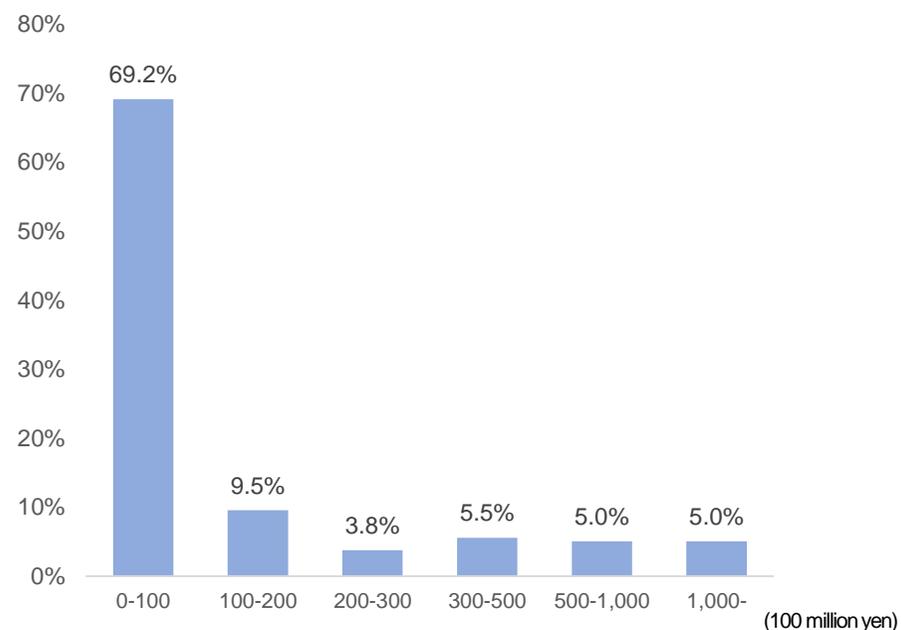
- The asset composition of defined benefit corporation pension (DB) in Japan has changed over time, by expansion of investment in alternative assets. It is said that there is still lack of expertise and human resources for investment management of DBs. The draft amendment of the Financial Instruments and Exchange Act 2023 requires DBs to consider the best interests for participants.
- In order for small-sized DBs to diversify their portfolios, AMC's are encouraged to contribute to making alternative assets available to them.

[Figure 33] Changes in asset composition of DBs



(Source) FSA, based on the "Corporate Pension Survey (FY2021 Overview)" by the Pension Fund Association

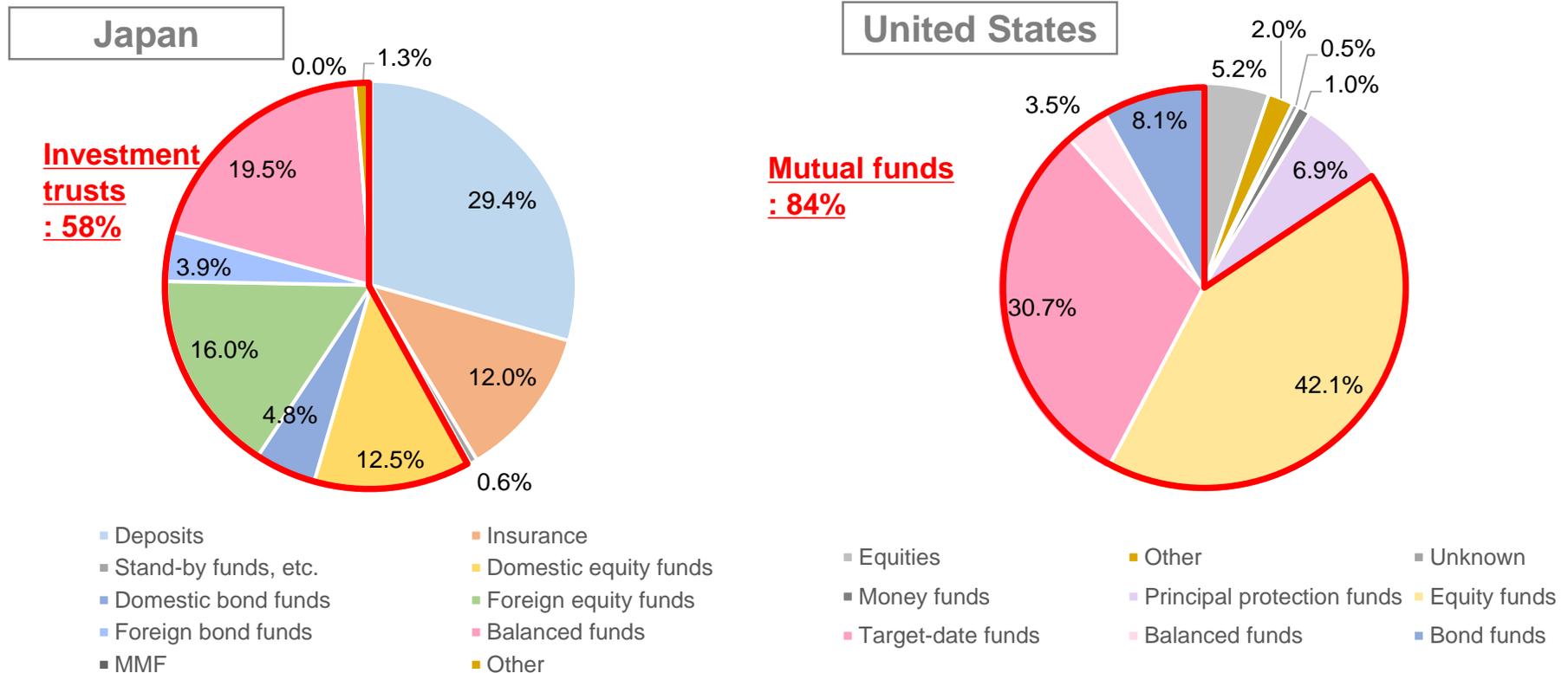
[Figure 34] Share of Corporate DB Pension System by size



(Source) FSA, based on the "Corporate Pension Survey (FY2021 Overview)" by the Pension Fund Association. 700 fund-type DBs and 1,027 contract-based DBs are covered out of 12,108 DBs as of the end of March 2022.

- The percentage of investment trusts in the corporate DC portfolio was less than 40% as of the end of March 2010, rising to 58% as of the end of March 2022. On the other hand, the latest percentage of mutual funds in the portfolio of US 401(k) plan is 84%.
- There is more room for DC participants in Japan to take advantage of the tax exemption on capital gains and investment opportunity.

[Figure 35] Comparison of corporate DC portfolios between Japan and the US

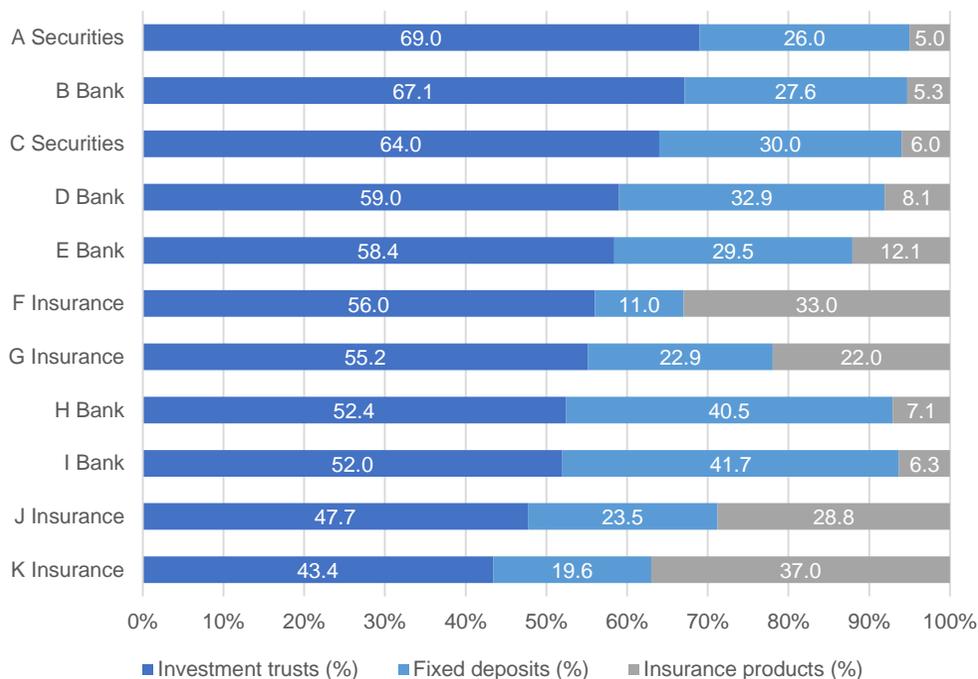


(Source) FSA, based on the "Defined Contribution Pension Statistics as of the end of March 2022" by the Liaison Council of DC Service Providers for the Japan pie chart and based on the "401(k) Plan Asset Allocation, Account Balances, and Loan Activity in 2019" by EBRI/ICI for the US pie chart.

Corporate DC Portfolios by DC Service Providers

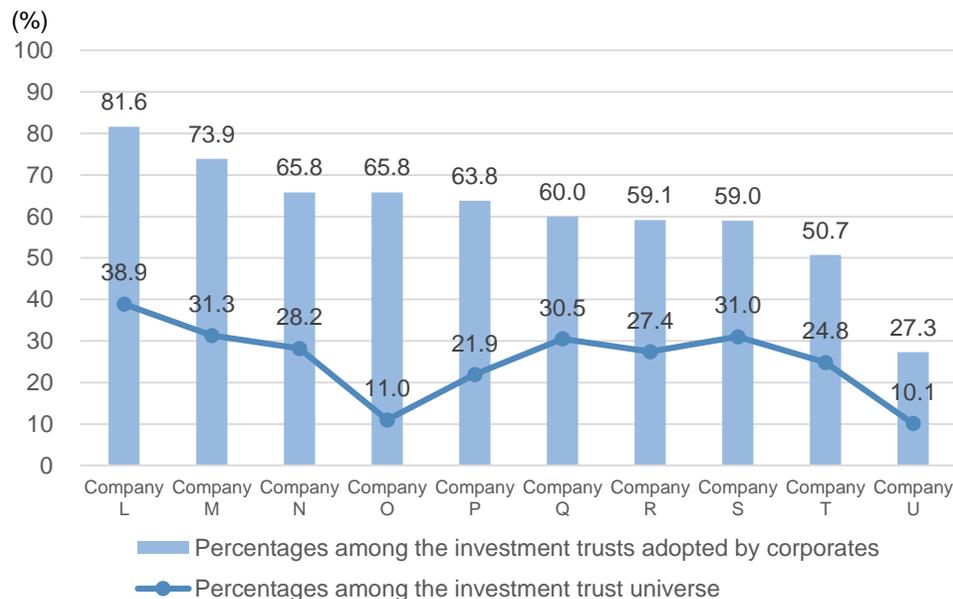
- Corporate DC portfolios are skewed to principal protected products such as deposits and insurance when DC services are provided by specific banks or insurance companies. Investment trusts developed by the affiliate AMCs of DC service providers account for 10% to less than 40% in the universe of investment trusts offered by DC service providers. Those account for mostly at 60% to 70% among the investment trusts that corporates actually adopted for participants.
- Corporates should select the best products for their employees, without considering the relationship with DC service providers.

[Figure 36] Percentage of investment trust in the participants' portfolios by DC service providers



(Source) FSA based on the data provided by individual financial institutions

[Figure 37] Percentage of investment trusts developed by the affiliated AMC in number among the universe and the investment trusts corporates adopted by DC service provider



(Source) FSA based on the data provided by the top 11 DC service providers in AUM