29th Meeting of the Council of Experts Concerning the Follow-up of Japan’s Stewardship Code and Japan’s Corporate Governance Code

Material 5

Provisional translation

Reference Materials

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金融庁
Financial Services Agency, the Japanese Government

Contents

"Engagement-Enhanced Passive" Managers Adopted by GPIF

- GPIF has adopted passive investment models focusing on stewardship activity (**"engagement-enhanced passive"**), which includes a compensation structure that differs from regular passive investment, with aims of achieving sustainable growth of the overall market through stewardship activities, as well as diversifying and enhancing the approach methods of stewardship activities. Asset managers selected are engaged in stewardship activities according to their own situation, including efficient beta increases by narrowing down companies that have a significant impact on the index, and active involvement by top management.
- In order for effective implementation of stewardship activities, it may be **important to promote responses appropriate to their own situation (size, investment policy, etc.) based on the purpose of the Stewardship Code.**

Characteristics of Engagement through "Engagement-Enhanced Passive" Managers

Asset Management One	✓ Started in 2018. ✓ Engagement on 18 ESG issues is conducted by ESG analysts and the person in charge of voting rights who have over 20 years' experience, in collaboration with fund managers and analysts from the asset management division. The engagement activity makes tangible investee companies' challenges, contributing to the improvement of their corporate value.
FIL Investments (Japan)	✓ Started in 2018. ✓ Aims for efficient enhancement of β by urging companies with a strong impact on indices to make reforms, utilizing knowledge of analysts of active investments. The agenda of engagement is identified from the perspectives of creating corporate value, and the improvement of profitability and growth potential is pursued by enhancing companies' competitiveness.
Sumitomo Mitsui Trust Asset Management	✓ Started in 2021. ✓ Adopts a multi-engagement model in which the upper management (chairperson or president) actively participates in engagement. The effects of engagement are maximized for the increase of corporate value by combining a top-down approach based on ESG materiality and a bottom-up approach from the business operation levels, along with policy engagement.
Resona Asset Management	✓ Started in 2021. ✓ Engagement based on the analyses of integrated reports using AI. Aims to improve the corporate value of investee companies by encouraging disclosure in integrated reports and setting qualitative improvement as interim targets and triggers. At present, the scope has been expanded to the Securities Report and TCFD- based analysis.

(Source: Compiled by JFSA based on GPIF "Stewardship Activity Report for 2022/2023" (March 2023))

Collective/Collaborative Engagement Initiatives

- Initiatives for collective/collaborative engagement include those by the Institutional Investors Collective Engagement Forum and the Life Insurance Association of Japan, as well as those by the Investor Forum in the UK.
- **In order to conduct effective stewardship activities** that are appropriate for each investor's situation, **it may be beneficial for investors to utilize these collective/collaborative engagement initiatives.**

	Initiatives in Japan: Institutional Investors Collective Engagement Forum (IICEF)	Initiatives in Japan: Life Insurance Association of Japan	Initiatives in the U.K.: Investor Forum
Organization Overview	◻ Established in 2017 to support constructive, "purposeful dialogue" (collaborative engagement) conducted with companies through collaboration by institutional investors to contribute to appropriate stewardship activities of institutional investors	◻ Established to promote the sound development and maintain the reliability of the life insurance industry and thereby contribute to the improvement of people's lives ◻ The Association operates a **stewardship activities working group** to help revitalize the stock market and realize a sustainable society	◻ Launched in 2014 with the goal of placing stewardship at the center of investment decision-making by promoting dialogue, creating long-term solutions, and enhancing value
Activities	◻ The Forum operates an **institutional investor collaborative dialogue program** for collaborative engagement • Participating investors discuss issues common to Japanese companies and set the agenda • **The secretariat presides over and facilitates dialogue with the target companies and supports constructive dialogue between the companies and participating investors** • The main agenda includes: ✓ Realizing management that is conscious of cost of capital and stock price ✓ Identifying materiality and disclosing nonfinancial information ✓ Handling proposals with a high rate of opposition at general shareholders' meetings, etc.	◻ **Companies participating in the stewardship activities working group perform collaborative engagement** (commenced in FY2017) • The main agenda includes: ✓ Enhancing shareholder returns ✓ Enhancing disclosure of ESG information ✓ Enhancing disclosure of climate change information, etc.	◻ The Forum has developed a **Collective Engagement Framework that organizes legal risks, etc., and conducts collective engagement in a format that represents the views of participating investors** ◻ Holds events for investor-company dialogue ◻ Shares best practices
Participants	◻ Pension Fund Association, Dai-ichi Life Insurance, Sumitomo Mitsui DS Asset Management, Sumitomo Mitsui Trust Asset Management, Mitsubishi UFJ Trust and Banking Corporation, Meiji Yasuda Asset Management, Resona Asset Management (7 companies)	◻ Asahi Mutual Life Insurance Co., Japan Post Insurance Co., Gibraltar Life Insurance Co., Sumitomo Life Insurance Co., Dai-ichi Life Insurance Co., Taiju Life Insurance Co., Daido Life Insurance Co., Taiyo Life Insurance Co., Nippon Life Insurance Co., Fukoku Mutual Life Insurance Co., Meiji Yasuda Life Insurance Co. (11 companies)	◻ 54 companies (comprising asset owners and asset managers in the UK and abroad)

(Sources: Compiled by JFSA based on websites of relevant initiatives and interviews)

Collective/Collaborative Monitoring Initiatives and other Initiatives

Financial System Council "Asset Management Task Force" (3rd meeting) explanatory materials from the secretariat (excerpts)

- As part of asset owners' initiatives to monitor their asset managers, the Pension Fund Association of Japan plans to conduct collective/collaborative monitoring. Some companies are also undertaking engagement support initiatives.

	Collective/Collaborative monitoring initiatives by asset owners	Other Initiatives
	Pension Fund Association	**MFA, Inc.**
Organization Overview	☐ The Association was established as an association of employees' pension funds based on the Employees' Pension Insurance Act, and was reorganized into its current form, Pension Fund Association, in 2005 following amendments to the law ☐ Its main activities: • Pension totalization service • Member support service • Administrative service entrusted by the national government • Management of pension benefit funds	☐ MFA was established in 2022 to serve as an intermediary (agent) that supports the establishment of productive and creative dialogue between the capital markets and companies in the form it should have ☐ Missions: (i) Defining what it means to be "a responsible shareholder" (ii) Establishing an "engagement" model (iii) Creating forums for "fruitful dialog"
Activities	The Association plans to take the following actions to substantiate its stewardship activities ☐ **Implementing collaborative monitoring** • Monitoring of stewardship activities of trustee institutions in collaboration with each corporate pension plan (e.g., joint briefings, collaborative dialogue, etc.) ☐ **Establishment of the Corporate Pension Stewardship Promotion Council** • For the purpose of continuous and substantial efforts toward collaborative monitoring • The Council expresses its acceptance of the Stewardship Code	☐ **MFA is contracted by institutional investors and others to perform "engagement" on their behalf and provide support for the companies in which they hold shares** ☐ In representing and assisting institutional investors and others, MFA will (i) Engage in dialogue with management and executives (ii) Provide professional services to solve problems (iii) Engage in dialogue with other external stakeholders (financial institutions, etc.)
Participants	☐ As of August 1, 2023, there were1,216 members in total (participants in the above initiatives are being adjusted)	☐ Shareholders: Sumitomo Mitsui Trust Bank, CDI Human Capital, Industrial Growth Platform, Misaki Federation, Corporate Directions, Kyoto Bank, Kiraboshi Bank

(Sources: Compiled by JFSA based on websites of relevant initiatives and interviews)

Japan's Stewardship Code (excerpt)

Guidance 4-1.

Institutional investors should endeavor to arrive at an understanding in common[13,14] with investee companies through constructive dialogue[15,16,17] with the aim of enhancing the companies' medium- to long-term value and capital efficiency, and promoting their sustainable growth. In case a risk of possible loss in corporate value is identified through the monitoring of and dialogue with companies, institutional investors should endeavor to arrive at a more in-depth common understanding by requesting further explanation from the companies and to solve the problem.[18]

16 Constructive dialogue between institutional investors and investee companies should not be merely driven by the size of shareholdings. That being said, there are cases when it is appropriate for institutional investors to explain to investee companies how many shares they own/hold.

Guidance 4-5.

In addition to institutional investors engaging with investee companies independently, it would be beneficial for them to engage with investee companies in collaboration with other institutional investors (collaborative engagement) as necessary.[20]

Contents

The Basics of Being an Independent Director

- The Ministry of Economy, Trade and Industry, the Financial Services Agency (JFSA), and the Tokyo Stock Exchange (TSE) jointly published "The Basics of Being an Independent Director" for newly appointed or inexperienced independent directors as part of efforts to ensure and improve the quality of independent directors (January 25, 2024).

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社外取締役のことはじめ

社外取締役の皆様のご活躍が、企業の持続的成長と中長期的な企業価値向上の鍵となります。重要な役割を担う社外取締役としてご活躍されるにあたり、まずはじめに知っておいていただきたい内容について掲載しておりますので、是非ご参照ください。

1 取締役会の役割・責務を知る

- 企業戦略等の大きな方向性を示すこと
- 経営陣幹部による適切なリスクテイクを支える環境整備を行うこと
- 独立した客観的な立場から、経営陣・取締役に対する実効性の高い監督を行うこと

「コーポレートガバナンス・コード」【基本原則4. 取締役会等の責務】

2 社外取締役としての自身に期待されている役割・機能を知る

一般的に期待されている役割

1. 経営方針や経営改善についての助言
2. 経営の監督
3. 利益相反の監督
4. ステークホルダーの意見の反映

「コーポレートガバナンス・コード」【原則4-7. 独立社外取締役の役割・責務】

具体的な行動の在り方

就任時　会社側と協議の上、自らのミッションを明確に認識

就任後　取締役会に対する能動的な働きかけ
1. 適切なアジェンダセッティング
2. 活性化のための運営上の工夫 等

「社外取締役ガイドライン」 P.25~45

3 社外取締役としての5つの心得を知る

心得1 最も重要な役割は、経営の監督 中核は、経営陣の評価と指名・報酬
- ◆必要な場合には、社長・CEOの交代を主導することも含まれる
- ◆過度に細かい業務執行に立ち入らない
- ◆経営陣の適切なリスクテイクをサポートする

心得2 社内のしがらみにとらわれず、会社の持続的成長に向けた経営戦略を考える
- ◆社内の常識にとらわれない視点
- ◆中長期的な視点
- ◆ESGやSDGsを含めた持続可能性を意識した経営の重要性
- ◆各事業部門の利害にとらわれない全社レベルでの「全体最適」の視点

心得3 業務執行から独立した立場から、経営陣に対して遠慮せずに発言・行動

心得4 経営陣と、適度な緊張感・距離感を保ちつつ、信頼関係を築く

心得5 会社と経営陣・支配株主等との利益相反を監督

「社外取締役ガイドライン」 P.11~24　　(注)5つの心得は簡略化して記載

4 自身の役割を果たすために必要な知識・スキルを知る

不足を感じた場合は、研修・トレーニングも活用しながら、継続的に向上に努める。

全社外取締役に必要な知識・スキル		特有の知識・スキル
財務・会計・法務を含め、企業経営に関する基礎的な知識・知見等のミニマム・スタンダードとして必要な最低限のリテラシー	＋	それぞれの役割・機能に応じて求められる資質・背景に依拠する知識・知見

「CGSガイドライン」 P.61~63 ／ 「社外取締役向け研修・トレーニング活用の8つのポイント」 P.18

5 就任先企業のことを知る

その役割・責務を実効的に果たすために、能動的に情報を入手する。

就任前／就任時	就任期間中
◆就任先企業からの説明(経営戦略、事業、組織・ガバナンス体制、具体的な事業環境・製品等、内部の諸規程・運営等)	◆就任先企業からの説明(事業環境・製品、旬なテーマ等) ◆執行役員クラスまで含めた経営陣や事業部門とのディスカッション ◆現地視察における意見交換、監査役等や内部監査部門との情報交換等

「社外取締役ガイドライン」 P.44~45 ／ 「社外取締役向け研修・トレーニングの活用の8つのポイント」 P.19~20

参照ガイドライン等へのリンク

コーポレートガバナンス・コード　株式会社東京証券取引所

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コーポレート・ガバナンス全般に関する取組方法について知りたい場合
コーポレート・ガバナンス・システムに関する実務指針(CGSガイドライン)　経済産業省

研修・トレーニングを活用したい場合
社外取締役向け研修・トレーニングの活用の8つのポイント　経済産業省

社外取締役の在り方(位置付け、心得、行動の在り方等)について知りたい場合
社外取締役の在り方に関する実務指針(社外取締役ガイドライン)　経済産業省

コーポレートガバナンスに関する各種ガイドラインについて

経済産業省では、コーポレートガバナンス・コードを実践するための各種ガイドライン等を公表しております。理解を深める際や個別論点を検討する際等にご活用ください。

コーポレートガバナンス ガイドライン

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Opinions Voiced in the Japan Corporate Governance Forum (Details)

Evaluation of corporate governance reform

- In Japan, corporate governance has made **significant progress over the past decade** and is moving in the right direction overall.
- Corporate governance is the foundation of all corporate activities, and we have **an overall positive view** of JFSA's policies.
- **We fully support** JFSA's **Action Program**. We, too, are focusing on capital efficiency and the fulfillment of functions by independent independent directors, which are priorities of JFSA.
- While some investors are frustrated with the slow pace of reform, foreign investors appreciate the government's **steady** commitment to corporate governance reform.
- While independent directors made up at least one-third of the members of the board of directors of only a few companies in 2014, the percentage is now more than one-third in many companies listed on the Prime Market, representing **commendable progress in terms of the formal aspects** of corporate governance.
- Corporate **transparency is improving**. In particular, JPX-Nikkei 400 companies have begun to communicate about ROE and dividends, which has greatly improved transparency.
- It is good to see that companies themselves are recognizing **the need for corporate governance reform** and addressing it, including the fact that discussions on capital allocation are becoming more sophisticated.
- Corporate governance reform should have been promoted with the goal of increasing corporate value, yet I feel that Japanese companies still do not **understand the significance** of corporate governance reform and **view it as a formality**.
- Boards of directors of Japanese companies appear to be more **focused on corporate survivability** than on increasing corporate value.
- Many companies do not have the correct **financial literacy** and cannot speak the same language.
- **Many small and medium-sized listed companies** may not be able to keep up with the Action Program. **Many companies** know about corporate governance reform but **have not fully understood it**.
- As many companies have a P/B ratio of less than 1x at the moment, there is much room for Japanese companies to improve their corporate governance. It is good to provide guidance, such as guidelines, but **the authorities need a mechanism to effectively enforce reforms**.

Opinions Voiced in the Japan Corporate Governance Forum (Details)

Issues related to dialogue between companies and investors

Effective implementation of stewardship activities

- In order to improve corporate governance at Japanese companies, we would like to see **domestic management companies actively increase the pressure on them**, because they engage with companies on a more routine basis and have no language hurdles.
- Another problem is that even if a portfolio company makes decisions that harm its corporate value, the companies that invest in it do not engage in stewardship activities unless there is external pressure to do so. There are numerous examples of directors who do not vote against other directors, taking advantage of the weak pressure from clients. **There is a lack of corporate commitment to autonomously fulfilling stewardship responsibilities to their clients.**
- In the U.S., under the Employee Retirement Income Security Act (ERISA), management companies face a risk of being charged with a breach of **fiduciary responsibility** if they do not exercise their voting rights in accordance with their **fiduciary duty** to their clients. However, the fact that the management companies in Japan do not have such a duty makes the problem more serious.
- Japanese companies voice discontent at the fact that **they can ascertain the potential equity value of their companies only through valuations by foreign investors**. Japanese companies lament that unless active investors are involved in valuations, their shares will be valued at a "Japan discount."
- For **major Japanese investors, different people are responsible for ESG, fundamentals, and voting**. Sometimes ESG analysts are not afraid to make proposals to companies that would lower EPS.
- The key is **to be able to use the engagement results in the exercise of voting rights.** It makes sense for an investment management company to make a shareholder proposal and vote on it if engagement is unsuccessful.
- From a feasibility perspective, we expect that management companies will engage TOPIX 500 component companies and this will lead to transformation in their corporate governance, including their disclosure practices and board composition, which will then spread to other companies listed on the Prime Market. **Activists also play an important role** in addressing companies not included in the TOPIX 500 Index.
- Active investors are pressuring companies to make changes to increase corporate value, including restructuring. On the other hand, passive investor engagement does not give them a sense of crisis and does not place pressure on their top management. This is not a situation that lends itself to creating value. Since selling shares is not an option, **Japanese passive investors should engage in a manner that can generate more value**.
- I would like to say that **not all passive investors are the same**. Some passive investors are engaged in very influential stewardship activities.

Opinions Voiced in the Japan Corporate Governance Forum (Details)

Issues related to dialogue between companies and investors

Effective implementation of stewardship activities

- Institutional investors still allocate much of their money to passive investments, but **it is not practical to engage with every company in which they passively invest**.
- Even if institutional investors do not engage with all of their portfolio companies every year, escalation takes place in the form of voting rights, and if there is no improvement on the part of the company, they oppose the proposal. **It is sufficient if institutional investors improve the governance of their portfolio companies through engagement once every two to three years, if not annually.** As an asset management company, basically we do not believe it is necessary to narrow the scope of passive investments.
- All investors should clearly indicate engagement **themes** and how they are **prioritized**.
- As it is difficult to engage with all **small and mid-sized companies**, we conduct **interviews on a three-year cycle**. Even during periods when there are no interviews, we share our thoughts and good practices regarding new and important issues from the perspective of a management company. In early June, resources are allocated to important matters and it is difficult to respond to dialogue unless it is urgent.
- Regardless of company size, when a request for dialogue is made, we ask the company to clarify its objectives. Since voting advisory firms began counting the number of times they have engaged in dialogue with shareholders to evaluate corporate engagement, companies have begun to **call on shareholders to engage in dialogue simply to score points** even though there is nothing particular to discuss. This is a waste of resources for both parties.
- Every fund is facing budget issues that are greater than ever before, and **collaborative engagement is important** in resolving issues raised. Companies respond favorably to investors' suggestions for solutions to problems for which they lack expertise, and we hope that such investor activity will be encouraged.
- If passive investors who are not paid a performance fee are **expected to improve the overall market, they need to be granted some benefits**.
- Collaborative engagement is very beneficial because it allows investors to introduce **different perspectives**, share ideas, and brainstorm.

Opinions Voiced in the Japan Corporate Governance Forum (Details)

Issues related to dialogue between companies and investors

Effective implementation of stewardship activities

- **When engaging, investors tend not to ask difficult questions, given their relationship with management.** As such, collective engagement can be effective. For example, a third party or a person designated by investors gathers key shareholder input, interacts with the CEO and independent directors, and identifies issues, all of which will help ensure effective engagement.
- The EU has **clear guidelines** for what is permissible in collaborative engagement, but clear rules have yet to be established in other regions.
- The current laws and regulations appear to allow for collaborative engagement and communication between investors, but some investors do not see it that way. Creating a **safe harbor** would be a relief not only to investors but also concerned compliance officers.
- Collaborative engagement is also necessary to elevate the level of boards of directors, and we support the idea of **clarifying the scope of joint holders**.
- Passive investors are long-term investors and look at environmental and social issues because they consider what will happen over long periods, such as 10 years, rather than short spans, such as one year. Accordingly, it is **meaningful** for these investors **to conduct engagement, even if it is on a small scale.** How to conduct engagement is a global issue, but collaborative engagement is a good idea.
- Investors with **global portfolios** may find it useful to utilize collaborative engagement.
- **Stewardship activities by the Bank of Japan (BOJ), which holds ETFs, may also be important** in preventing top management from defending itself and in making it easier for minority shareholders to have their opinions heard at shareholder meetings.
- For index investors, voting is also part of their fiduciary duty to their clients. For this reason, the argument that the BOJ should waive (or not exercise) its voting rights in relation to the **ETFs it holds** does not seem appropriate.

Opinions Voiced in the Japan Corporate Governance Forum (Details)

Issues related to dialogue between companies and investors

Resolving legal issues

- Since different issues arise depending on the tender offers, it is difficult to establish detailed rules, and it would be better to establish principles based on **the notion of fairness**.
- **The U.K. regulations** on tender offers should be referred to.
- I do not understand the logic behind not applying the same regulation to **in-market purchases and other purchases**.
- We are concerned that cases will emerge where people will **abuse partial tender offers** and shareholders will be forced to apply at a lower price.
- In **the privatization of a subsidiary**, the parent company can easily predict when the price of the subsidiary's shares will fall and make the acquisition more advantageous; thus, the risk of minority shareholders being harmed by the information asymmetry is significant.
- The tender offer rule in Japan allows for **partial tender offers**, but we wonder if it might be possible to revise the regulations so that, for example, if a company purchases more than 30% of the shares, it must purchase all of the shares.
- **Partial tender offers** are also possible in the U.S., but are not carried out because they violate the principle of fair treatment of shareholders.
- I think it is desirable to have regulations for **partial tender offers** and to include **Majority of Minority (MoM)** requirements. Listed subsidiaries are often capital inefficient due to the risk of their minority shareholders being harmed by their parent companies.
- **An acquirer** should not have voting rights on an acquisition decision **if it is the controlling shareholder.**
- **MoMs are also at risk of abuse,** as they favor proposals that are good for the company and cold-shoulder other proposals.
- **The paperwork** for submitting documents to the Kanto Local Finance Bureau **is complicated**. We are concerned about the time it will take the Finance Bureau to review applications and the possibility of information leakage in the review process.
- As for revisions to the tender offer rule, first, we support the idea of making in-market transactions subject to the rule and **the direction of shifting the rule to a European model**. Partial tender offers are not permitted in Europe, and moving in such a direction is desirable.

Opinions Voiced in the Japan Corporate Governance Forum (Details)

Issues related to dialogue between companies and investors

Resolving legal issues

- It is important to **clarify material proposal** in the large shareholding reporting rule.
- Clarifying the large shareholding reporting rule will **improve the transparency of the dialogue between investors and companies**. It will also allow domestic shareholders to communicate their constructive concerns in a more open manner to the companies in which they invest. In that sense, we view it positively.
- We expect that the scope of actions that do not fall under the category of material proposal (**white list**) will be broader than the scope of actions that fall under the category of material proposal (black list). In addition, as climate change initiatives gain momentum, it would be appreciated if the white list could be expanded to include these aspects as well.
- **Clarifying the scope of joint holders** is an important topic for the entire global investor community.
- Even if the engagement officer was not concerned about joint holders, **the compliance department of the management company has significant concerns**. Safe harbors are important for free collaborative engagement.
- Since the **custodian** is a nominal shareholder for foreign investors, it is difficult to ascertain which of them are the beneficial shareholders. Once the beneficial shareholders are identified, it will be easier for other investors to access the shareholders when exercising voting rights.
- With respect to the transparency of beneficial shareholders, **disclosure of the holdings of a particular investor could give the wrong message** that such investor is engaged in share acquisitions that could affect the companies in which it invests. As a result, there is concern that this will discourage long-term investors from gradually increasing their investments.
- While we understand the intent behind the regulations on the transparency of beneficial shareholders from the perspective of dialogue with companies, disclosing the number of shares held in Japan, where stock liquidity is not as high as it is in the U.S., may increase the sensitivity of share trading.
- The transparency of beneficial shareholders is very important for global investors.

Opinions Voiced in the Japan Corporate Governance Forum (Details)

Issues for seeking sustainable corporate growth and increased corporate value over the mid- to long-term

Improving the effectiveness of the board (independent directors' fulfillment of functions)

- The first step is to secure independent directors whose **mission is to maximize corporate value and protect minority shareholders**, and to ensure the independence of the board of directors.
- In substantiating corporate governance, **the skills and independence of independent directors are** particularly **important**.
- **Having a majority of independent directors** and a company with a nominating committee, etc. will promote the formation of an appropriate corporate governance culture.
- Having independent directors constitute **one-third** of the board **is insufficient to ensure the board's independence** from top management.
- The next step is to appoint a majority of independent directors. **Companies** that attract long-term investors are those with a nominating committee, etc., a board with a majority of independent directors, and **a high degree of transparency in decision-making** on capital policy and other matters.
- Supervisory and executive functions must be separated, and **we want companies to have boards with a majority of independent directors**. In order to increase corporate value over the long term, companies need governance that is capable of removing problematic management from office.
- In many Japanese companies, the CEO also serves as chairperson of the board of directors, but the person who controls the board's agenda and the person who executes business should be different, and the **chairperson should be an independent director**.
- **Legislation is needed to clarify the authority and responsibilities of nominating and compensation committees** even for companies other than those with a nominating committee, etc.
- I believe that Japanese companies need to establish **a board-level risk committee**, which is common in the U.S.
- **Companies should make it a market practice to hold meetings exclusively for independent directors** so that they can have frank discussions about the companies' performance, shareholder proposals, and M&A proposals. Another idea is to encourage companies to describe such meetings in their corporate governance reports.
- Some companies appoint independent directors from their **cross-shareholding companies**, but this harms the effectiveness of independent directors.
- There may be **room for improvement in the Tokyo Stock Exchange (TSE)'s independence criteria**. For example, we believe that personnel sent from a bank that holds cross shareholdings do not meet the independence requirement.

Opinions Voiced in the Japan Corporate Governance Forum (Details)

Issues for seeking sustainable corporate growth and increased corporate value over the mid- to long-term

Improving the effectiveness of the board (independent directors' fulfillment of functions)

- It is important to make sure that **the experience of candidates** for independent directors **is well disclosed**.
- It seems that independent directors generally tend to approve any agenda items of the board of directors. In addition, most independent directors are lawyers, accountants, and academics, and **few are business people**.
- It is **important** for independent directors to **have a substantive voice and influence** in board discussions.
- Some independent directors work with the interests of the CEO and the company in mind and do not represent the interests of the shareholders. It is important that **independent directors pursue the interests of shareholders**.
- It is important that directors respect top management while also being **willing** to consider whether decisions are truly in the best interests of shareholders and **challenge top management**.
- Gender diversity is important, but "**diversity of opinion**" is more important, and it is important to have external personnel who can challenge top management for the development of the company.
- The boards of directors should delegate their authority to the executive departments to focus on strategic discussions and reduce the **frequency of board meetings** from once a month to four times a year. It is not practical for foreign directors to visit Japan every month.
- Companies are obligated to **provide training** for independent directors **to help them understand their business**.
- **Training for directors is important.** Companies should be required to **disclose their performance**, not their policies, regarding director training.
- Independent directors play an important role in engagement. The best practice is **to allow independent directors and shareholders to engage with ease**.
- Sometimes, independent directors themselves are eager to meet with investors, but **their companies act as a gatekeeper, preventing them from doing so**.
- **Providing equity compensation** to independent directors is important for improving corporate value and making them conscious of the stock price; thus, companies should consider introducing this.

Opinions Voiced in the Japan Corporate Governance Forum (Details)

Issues for seeking sustainable corporate growth and increased corporate value over the mid- to long-term

Management with an awareness of profit-making and growth

- We appreciate that the government has taken up the issue of **management that is conscious of capital costs and stock price**. Since the issue of P/B ratios below 1x was taken up for discussion, foreign investors have been paying considerable attention to the Japanese market, **presenting an opportunity for the resurgence of Japanese stocks**.
- When taking into account various risks involved, investment by foreign investors is not worthwhile unless the ROE is at least 12%, and the reality is that even when we try to sell Japanese risk-weighted assets, an ROE of 8-9% is not very attractive to them. **Only about the top 10% of companies in Japan can produce the average ROE in the U.S.**, which inevitably limits the amount of money available for investment in Japan.
- We wonder why many Japanese companies want to have multiple businesses even though doing so could create a **conglomerate discount.** Some companies have increased their market valuation by reviewing their business portfolios, and this is an issue that needs to be considered.
- Many Japanese corporate managements **prefer to maintain the status quo**. For example, if a company's P/B ratio is over 1x, even if it has unprofitable businesses, it will not make efforts to further increase its corporate value by concentrating on its core businesses.
- The emphasis on sales rather than profit often prevents the divestiture or sale of businesses or sectors that are strategically unprofitable for the company, thus hindering the business metabolism. If companies do not select and concentrate on areas of strength, it will be difficult to create new industries with high added value. In addition, for this purpose, it is important to **educate and enlighten management on capital costs**.
- **Carve-outs** implemented for the purpose of reinvesting the proceeds from the sale in other businesses **are important**. As an investor, the restructuring of the portfolio is the most interesting aspect to watch and the part that shareholders can drive by asking the management if they are the best owner.
- Companies with large amounts of net cash are problematic. For companies with accumulated **retained earnings**, activists are taking notice and intensifying their demands, even if the P/B ratio is above 1x.
- The problem is that the cash flow multiple is more undervalued than the P/B ratio. Companies are not allocating the funds they raise efficiently and are letting them sit idle. In order for them to get out of this situation and increase their corporate value, legislative measures are needed to discourage the hoarding of cash, for example, **a retained earnings tax**.
- Companies are **buying back their own shares in the short term** to improve their P/B ratios, which is not always desirable.

Opinions Voiced in the Japan Corporate Governance Forum (Details)

Issues for seeking sustainable corporate growth and increased corporate value over the mid- to long-term

Management with an awareness of profit-making and growth

- As has been pointed out, one of the challenges for Japanese companies is our unwillingness to take risks, which causes us to **miss out on upside return opportunities**. Therefore, we should give priority to increasing shareholder returns, total shareholder value, etc. Making innovation investments is also an important issue.
- Japanese corporate managements have forgotten the **concept of "time" in their investment activities**. In investment, "time" is what yields compound interest, and in some cases it is important to pursue M&A deals that should be conducted now. Engaging in discussion based on the notion of "time is a priority" and "this is what we should do now" is also important.
- In Japan, **the excessive attention given to various stakeholders' interests, etc.** seems to dilute awareness among Japanese corporate management about the stock price and prevent it from increasing.
- Despite the fact that a company is owned by its shareholders, many Japanese companies have prioritized the interests of stakeholders in the order of top management > employees > customers > suppliers > shareholders, in the name of multi-stakeholder capitalism, and **disregarded shareholders**.
- Japanese companies, even large ones, appear to lack **knowledge about capital costs and basic corporate finance** and might not know how to improve their capital policy and ROIC.
- In terms of the response to TSE's request to companies to improve their capital costs and stock price, we don't think it is difficult to calculate ROE or capital costs, but it is **difficult to find examples of good responses among small and mid-cap companies**.
- If a company is unsure about its ROE or capital costs, it could ask its largest foreign shareholder. Any **move by a Japanese company to approach foreign investors** in order to improve its management could be a very positive signal from an investor's perspective.
- In order for companies and investors to engage in dialogue on this topic for the realization of management that is conscious of capital costs and stock price, each party must have the same level of understanding of ROE, ROIC, capital costs, etc. However, many companies, especially small and medium-sized ones, are **not even aware of their own capital costs**. It would be useful to establish a platform to provide companies with information on capital costs, etc.
- **Even large companies often have a poor understanding** of capital costs. Japanese companies have become very conservative financially during the economic downturn, with some having sophisticated boards with a good understanding of portfolios and capital costs, while others do not.

Opinions Voiced in the Japan Corporate Governance Forum (Details)

Issues for seeking sustainable corporate growth and increased corporate value over the mid- to long-term

Management with an awareness of profit-making and growth

- From a foreign investor's point of view, it is particularly noteworthy that there are no **professional CFOs** in Japan. CFOs should be able to handle capital allocation and dialogue with investors, and they need to be trained/developed.
- In response to TSE's request, a framework for disclosure **from an angle and at a level preferred by investors** should be created, including in terms of capital costs, pricing power, withdrawal from unprofitable businesses, business models such as M&As, and resources to realize corporate value enhancement.
- If we can **eliminate as many of the failing companies as possible** identified in the process of raising the ROE of Japanese companies, they will know that Japan is taking this issue seriously.
- TSE's request relating to capital costs will **not activate reforms, unless it ultimately leads to the delisting of companies with a P/B ratio below 1x.**
- Japanese corporate management are irresponsible not only to their shareholders **but to all stakeholders**. As listed companies, their management should act to fulfill their responsibilities, including ESG, to all stakeholders, not just shareholders.
- Members of managements who fail to fulfill their responsibilities should be punished, and **strong enforcement**, such as delisting and increasing the independence of the board of directors to **increase the possibility of firing management (CEO)**, is needed.
- Unless companies themselves become autonomously and actively committed, they will just end when their P/B ratio and ROE reach 1x and 8%, respectively. To this end, it is necessary to establish a **system where members of management who fail to produce results are fired**, and to heighten management's sense of urgency.
- **Many management members of Japanese companies don't hold their own company's shares**, which provides no incentive to increase stock prices, so they tend to show little interest in their company's stock price and pay little attention to its long-term corporate value.
- It is important to give management not only "sticks" but also "carrots" and to **provide them with sufficient incentives at a level appropriate for their capabilities and responsibilities**.
- **Economic incentives for top management** are lacking in Japan. There is a concern that there will be no change from the status quo as long as this matter is left to the autonomy of companies, as has been done. Foreign investors are calling for a greater sense of urgency.
- In order to increase top management's incentives, **having them own more shares** is an option. This is more effective than performance-based monetary compensation.

Opinions Voiced in the Japan Corporate Governance Forum (Details)

Issues related to dialogue between companies and investors

Enhancing the disclosure as a basis for dialogue

- Demand for engagement from Japanese companies, **particularly TOPIX500 component companies**, is gradually increasing, which we view as an improvement in corporate governance.
- Some companies are willing to have one-on-one dialogue but are **unwilling to meet with groups of investors**.
- Looking at the investor relations of Japanese companies, we feel there is a large gap in perspective with foreign investors. For example, it is very unfortunate that there are still some cases where Prime Market-listed companies do not even have an opportunity for dialogue. In Japan, no **intervention measures exist for companies that refuse to engage in dialogue** with investors.
- Some companies are difficult to get in contact with, especially when we try to have a dialogue about sustainability issues. Not only independent directors, but even top management and IR personnel are not available for meetings in some cases; we want companies to be encouraged to **respond when contacted by institutional investors**.
- Annual shareholders' meetings are still concentrated and take place over an extremely short period of time; no progress is seen in the issue of investors' **lack of time to focus on small and medium-sized companies. Spreading out the timing of the meetings** is a key priority of the corporate governance reform.
- Most listed companies in Japan are **reluctant to submit annual securities reports prior to annual shareholders' meetings**. Japan is the only developed country in the world where shareholders must attend a shareholders' meeting with an annual report for the previous fiscal year.
- It is a good practice to disclose the annual securities report prior to the shareholders' meeting. The timing of the shareholders' meeting is not that significant of an issue; **timely information disclosure prior to the meeting is more important.** Even if the meeting were to be held in July, that would not pose any particular problem.
- **Moving the shareholders' meeting to the end of July** in order to disclose the annual securities report prior to the meeting is a welcome move from a foreign investor's perspective, as it will allow them time to understand and analyze the latest information on investee companies.
- If **a fiscal year closes in December** as in Europe and the U.S., the annual securities report can be prepared by the end of March, with the shareholders' meeting held before the consecutive holidays in May.

Opinions Voiced in the Japan Corporate Governance Forum (Details)

Issues related to dialogue between companies and investors		
	Enhancing the disclosure as a basis for dialogue	● Disclosure is very important because it serves both as a tool for investors to evaluate a company and **as a means to change corporate behavior.** On the other hand, making disclosures is costly, and aggregating and analyzing disclosed data is also costly; cost-benefit considerations are required. ● Relative to U.S. disclosures, Japanese companies' annual securities reports and integrated reports are clichéd and are all alike, failing to convey **management's message**. Further, some companies do not update their own websites, despite the disclosure of their information on EDINET. This is inconsiderate. ● IR is also very important, and companies with effective IR have been successful in **attracting foreign investors**. If top management decisively explain to foreign investors how they will make improvements, it should be very easy to attract investments. ● We also pay attention to **letters** from CEOs and others. ● In the U.K., when **20% or more of the votes are cast against** a shareholders' meeting proposal of a listed company, the company will be placed on a watch list of the U.K. Investment Association, and **future measures, etc. must be announced within the following six months**. This practice has been very effective and should be introduced in Japan as well.
	Promoting dialogue with global investors	● **A lockstep mentality is prevailing in Japan;** thus, we hope that corporate governance will be substantiated through the **presentation of good case studies and setting of appropriate incentives**. ● "Visualization" can be meaningful, but we are concerned that if the items of standards are overly increased, many companies may pursue compliance only as a formality. It is important to **narrow down the items of standards and apply them strictly** so that the number of companies that can secure the substantive aspects will increase. ● Creating a **knowledge hub,** like the JPX ESG Knowledge Hub, which focuses on board effectiveness and capital policy and lists best practices, should help companies better understand what true corporate governance is like. ● The number of companies that disclose information in English is slowly increasing, but a lack of progress is seen in **English disclosures by medium-sized companies**. ● It is important to release both Japanese and English disclosures **at the same time**. ● There is a **time lag** between Japanese disclosure and English disclosure. In addition, in Japan, only a small part of securities reports is provided in English. **Timely disclosure in English** is also important to foreign investors.

Opinions Voiced in the Japan Corporate Governance Forum (Details)

Issues related to dialogue between companies and investors

Resolving market environment issues

- Cross shareholdings have **not changed dramatically over the past 40 years**. We hope that Japanese companies will take steps to unwind them.
- As for cross shareholdings, insurance companies and other domestic investors also need to change. The reduction of cross shareholdings would lead to **encouraging corporate acquisitions** as well as corporate governance.
- **Top managements are protected** by cross shareholdings, as shareholder proposals are rejected due to the presence of a large number of cross-shareholders. A company with cross shareholdings is like a company with a **poison pill**.
- Regarding cross shareholdings, despite failing to generate sufficient returns, they are not reduced and are even increased in some cases. As to the purpose of new cross shareholdings, companies only say it is to maintain relationships with portfolio companies, **failing to provide rational reasons**.
- Cross shareholdings often hinder improvements in governance. Cross shareholders should be required to disclose and explain the **(negative) impact on governance** of such holdings.
- **In certain sectors**, we have heard that they cannot even bring up the issue of unwinding cross shareholdings for fear of the risk of transaction cancellations.
- Cross shareholdings have very negative effects on capital efficiency and governance. Discriminatory treatment of business partners with no cross shareholdings, if any, should be regulated somehow.
- We don't understand the logic that companies cannot continue to do business with each other unless they hold each other's shares. **Frankly speaking, from a foreign investor's perspective, it makes Japan a difficult market to invest in**.
- The **existing cross shareholdings are firmly entrenched**, and in some cases companies seem to use their counterparties as an excuse to maintain such holdings.
- For cross shareholdings, whether companies exercise their voting rights in accordance with their voting policies is not clear. The **results of the exercise of voting rights should be disclosed**.
- Addressing this issue is extremely important, as it has created a situation where a group of shareholders' votes against a company are never successful. How can we accelerate the reduction of cross shareholdings among companies that do not want to give theirs up?

Opinions Voiced in the Japan Corporate Governance Forum (Details)

Issues related to dialogue between companies and investors

Resolving market environment issues

- We know that **more than 80 companies have reclassified their shareholdings from cross holdings to net investments**.
- **Among banks, the pace of unwinding cross shareholdings varies widely.** Cross shareholdings account for half of the assets of certain banks. Publicly-traded companies should increase transparency properly to the satisfaction of investors.
- As long as cross shareholdings continue to exist, it must be said that investors with no experience investing in Japan cannot invest. Such companies should not be listed on the Prime Market, and **those that do not eliminate their cross shareholdings should be delisted.**
- Cross shareholdings are very problematic. **How the government responds to leading companies with cross shareholdings** is also important. If these companies change, it would present an opportunity for Japanese companies as a whole to change.
- Our understanding is that one of the reasons why the corporate value of Japanese companies has not improved is the **absence of a market for corporate control**.
- The most effective way to improve corporate governance in Japan is to properly **put in place a market mechanism that allows stock prices to increase through takeover bids and counter-proposals**.
- Japan has a problem in that there are **too many listed companies**.
- As to parent-subsidiary listings, TSE has an incentive to list them; therefore, rather than TSE, **the government should take the initiative**.
- What approaches should be taken for the **issues facing the Standard and Growth Markets**? Haven't they become full of zombie companies?
- **Dual-class shares** are a problem. The principle of one voting right per share should not be compromised. Hong Kong made a rule change in 2018 to accept dual-class shares in order to attract tech companies. The market initially acquired a large number of Chinese companies but soon stopped functioning well.

Opinions Voiced in the Japan Corporate Governance Forum (Details)

Issues for seeking sustainable corporate growth and increased corporate value over the mid- to long-term

Management with an awareness of sustainability issues

- We recognize the information disclosure efforts by Japanese companies and believe that they are **likely to pull ahead of U.S.** companies when it comes to sustainability disclosures.
- **ESG is one of the most significant risks faced by companies**, and corporate awareness and risk management should be disclosed by companies for investment analysis.
- **Japanese companies are doing well in collecting and disclosing data on carbon emissions.** A lower level of carbon emissions should lead to a higher evaluation of a company as having efficient management.
- **A company that values the well-being of its employees is likely to be sustainable**, but corporate value is more correlated with the E and S factors; it is not appropriate to consider the two as separate and independent.
- **For the ISSB standards to become a global standard** should be beneficial in advancing collaborative engagement as they align investors' views on certain topics, particularly those related to sustainability.
- As for sustainability disclosures, **international comparability** is desirable, and we want the ISSB taxonomy and the Japanese taxonomy to be unified.
- We wonder **how valuable** sustainability information disclosure is **to investors**. Despite a company's disclosure, "We will achieve our goals by 2050," the situation could change due to technological advances and top management also could be replaced by then, which means accountability cannot be fulfilled.
- The CSRD sets out disclosure items on anti-slavery and response to environmental destruction, but they are **areas in which the government should intervene**. Investors, who have neither the authority nor the means, should not be expected to impose sanctions against companies.
- We are **concerned about JFSA's emphasis on human capital**. JFSA sent a letter directly to ISSB to draw attention to the importance of human capital, which was a fantastic gesture. We want to know how JFSA will advance efforts on human capital from now on.
- The diversity of boards in Japan, **especially gender diversity**, is improving but still **significantly lower than in other countries**, and we expect further improvement.

Opinions Voiced in the Japan Corporate Governance Forum (Details)

Issues for seeking sustainable corporate growth and increased corporate value over the mid- to long-term

Management with an awareness of sustainability issues

- **Suitable personnel, regardless of gender, should receive the benefits of promotion.**
- Japan has a small **pool** of female directors and independent directors. There are few experienced personnel available, and a disproportionate number are academics and lawyers. There are abundant human resources with practical experience overseas; foreign national directors should be appointed. At an employee level, competent personnel should be hired from overseas as well.
- The goal of 30% female board members by 2030 seems **ambitious**, given the current situation in Japan. Since it is difficult to hire the right people from the outside or to promote them internally immediately, we **need to act quickly**.
- The goal of 30% female board members by 2030 appears to be a high hurdle, as we **might not be able to secure candidates**. Meanwhile, there is a large pool of foreign national women (candidates); one option is to take advantage of such pool.
- **In order to promote the substantiation** of corporate governance, we **need personnel to carry it out**. The shortage of female independent directors and IR and finance experts, especially at small and medium-sized companies, is a concern.
- Board diversity is indeed important, but **whether directors have necessary skill sets is fundamentally important**.
- A box-ticking-type of procedure implemented in the name of ensuring diversity also leads to the appointment of people of different races, genders, and identities as directors. But **those with the skills that are most appropriate for a company should be appointed as directors**.
- Efforts for increasing the number of independent directors on the board and diversifying gender are also important, and have been demanded as the role required of the board changes. It is important to weigh the **role of the board of directors**.

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Opinions Voiced in Interviews with Companies (Details)

Dialogue with investors (general)

- Basically, the President/Representative Director is in charge of dialogue with shareholders. Not limited to participation in dialogue, the IR department acts as the secretariat for the board of directors, the management meeting, and the sustainability committee, and also engages in shareholders' meeting operations. Disclosure materials are also prepared mainly by the **IR department, which is responsible for the administration of both strategy formulation and dialogue based on disclosures**.
- As for engagement, the CEO and CFO handle it when **its theme concerns the major direction of the company**. **Having someone who can answer questions about dialogue topics is valued**; e.g., an ESG agenda is handled by the department in charge of ESG, and a human capital agenda by director-level personnel of the HR department.
- Almost all of our dialogue is handled by **the director in charge of IR**. The content of our disclosures based on TSE's request are just typical of what we considered as a "necessary level of disclosure," and we didn't expect to be recognized so highly externally (e.g., being featured in a TSE case study).
- Under the supervision of the director in charge of engagement, the SDG promotion office, legal office, and finance/accounting department participate in dialogue. Dialogue partners are selected mainly from among domestic institutional investors with large shareholding percentages. The most common dialogue topic is ESG, and investors show a particular interest in E and S. A high level of interest is also seen in the founder's **succession**.
- Engagement is handled primarily by the CEO and CFO. The number of IR department personnel, which previously consisted of two to three members, was **increased** to five this year. We will increase the number of dialogues to enhance corporate value, by reaching out to investors that we were not able to approach before and responding to requests for dialogue from investors whom we were not able to respond to before.
- Having investors get to know our company is fundamental. The problem is that **disclosure is assessed as a risk where it is insufficient**; investors must be reassured. Both directors and business managers understand the idea of emphasizing ROIC and WACC, and they are conscious of meeting investors' expectations.
- Over the past few years, we have gradually increased the number of dialogues and devised a format. They are one of the important stakeholders, while there is also a need to respond to requests from JFSA and TSE for corporate governance reforms. We started **exchanging information with investors and others** and **providing feedback** on investors' requests **internally, including to board members and employees**.
- We focus on investor relations not only to utilize external perspectives in our management, but also to promote investors' understanding of our business and growth potential, which stem from the diversity of our business. Compared to other Japanese companies, a larger percentage of our shareholders are institutional investors, including foreign nationals and financial institutions, with foreign nationals accounting for about 60% of our shareholders. We have IR offices in NY and London, which enables **timely communication with investors in North America and Europe**.
- One of the matters for which top management's explanations helped to gain the understanding of shareholders is with respect to the fact that explanations provided by top management in plain language can deepen their understanding, as some of the investors are not familiar with our business model, or even more fundamentally, with a manufacturer's business model. From the standpoint of the IR department, **top management's explanations seem to take on a different significance to investors**.

Opinions Voiced in Interviews with Companies (Details)

Meaningful engagement, specific investor references and anecdotes

- In our case, dialogue always starts with (the topic of) the progress of business results, which we always receive questions on coupled with the post-business restructuring growth strategy. It felt very good when we had a good understanding of our company's unique circumstances, where we finally recovered to produce an operating profit after implementing business restructuring reforms under the turnaround plan, amid a period of challenging business results and the COVID-19 pandemic, and received advice based on such understanding. We are very grateful for dialogue in which we can receive advice such as, "**Even in the present situation, maybe you can try XX in this way.**"
- If it provides us with some insight that will contribute to corporate value improvement, even a finding/comment that is painful to hear is helpful. For instance, we set an ROE target of 10% or more in the management plan but have achieved over 10% for the last several years. Our investors, including overseas investors, pointed out that **our eyes were set too low**. In the wake of this dialogue, we made a statement, "raising the ROE target is under consideration," in the materials for the most recent management presentation.
- The total return ratio was set at 30-35% initially but raised to 50% several years ago. In dialogue with investors, many said we could aim for about 50%. We accepted this as it was financially feasible. At the same time, we began offering progressive dividends. In fact, our company had paid progressive dividends in the past, but recognizing many investors' focus on income gains, we presented it as our policy. In subsequent feedback from investors, this move was received better than expected. Another said: "There is a significant difference between what you actually do and what you disclose as your policy. But **disclosure represents management's confidence**, and we greatly appreciate that."
- Investors often express concerns over the sustainability of raw material procurement. In this regard, one investor suggested that we take actions to address it, as raw material procurement could constitute a risk for our company, by introducing us to an environmental NGO, providing examples of efforts by other companies, etc. to realize sustainable raw material procurement. Influenced by these investors, we conducted a two-year trial on sustainable raw material procurement. The examples of efforts by other companies introduce us to not only best practices but also those in the intermediate stages, providing us with **recommendations on initiatives that are easy to start as a first step**. These materials are also informative, as they colorfully reflect each investor's points of focus and policies.
- One investor **assigns its own unique ESG scores to issuers** and shows them to us in a radar chart format after collecting, analyzing, and evaluating issuers' non-financial information using its proprietary mechanism. This chart is **explained to us based on the data updated each year**, which enables dialogue that is satisfying to us as well. Regarding S, there were occasions when we were asked about how we actually approach the work, by comparison to public opinion after word-of-mouth data was collected by research firms. As such data is rarely delivered to management, honest feedback is very meaningful as we can use it as a hint for further internal efforts and have additional dialogue on its progress in the following year.
- Many investors come to us after **doing some research**, to some extent, **on our industry or our company**; in such cases, we can have a down-to-earth dialogue. The internal situation is not visible from the outside, and it is difficult to take actions in reality even if investors' claims are valid. However, we can have **fruitful dialogue in many cases with those who have read our disclosures carefully**. **As one of the attributes of investors who read disclosures carefully**, many of them **invest only for the long term and have a long-range vantage point**. Many of them have talks with us on a regular basis based on disclosures, continuing dialogue in the form of stationary observation.

Opinions Voiced in Interviews with Companies (Details)

Meaningful engagement, specific investor references and anecdotes

- As we have increased our company efforts over the last three to four years, many matters are included in engagement themes: CO_2 reduction roadmaps, human rights due diligence process, human capital disclosures, etc. In addition, last year we raised our guideline for the dividend payout ratio as a percentage of net income. We had already recognized its low level internally, but also had to confirm investor demand; **we are also changing**.
- One investor is an intensive reader of integrated reports and gives us detailed feedback. Our company's current analyst has been **evaluating us over a long time span** by taking tours of our plants since s/he was with previous companies and is capable of engaging in in-depth discussions about our management strategy and latest business portfolios. Better dialogue can be held with **someone who has been observing our company or our sector for a long time**.
- We were asked about the thinking behind setting the hurdle rate for return on invested capital at 10% or about our approach to business portfolios. We have adopted the concept of business-specific ROIC (business ROA) internally for more than 10 years, without disclosing it externally. In line with the concept of portfolio management, in 2022, we disclosed a diagram of the criteria for investment allocation decisions in six quadrants, which was well received by investors. Based on suggestions from investors, we also plotted our products in 2023 so that their positions in these six quadrants can be easily spotted. We received further questions from investors about the plotting of products not listed on the diagram. **As a result of these efforts for gradually increasing the level of disclosure, we received positive feedback from investors, who stated, "It is now easier to have concrete discussions."** In addition, we frequently receive requests to disclose ROIC by segment, as it facilitates concrete discussions about capital costs for each business, an ideal level of returns greater than such costs, and measures to improve ROIC figures that fall below the projections. We thus will need to consider such disclosure.
- One investor shares examples of disclosure, including IR materials, on the **linkage between non-financial information and financial information**. A lack of quantitative analysis is seen as an issue at our company, and the CFO is conscious of this issue as well; we are working on it internally. The said investor explained examples from other companies regarding the linkage between non-financial information and financial information, in terms of the disclosure of a long-term vision-based backcasting/standpoint, measures currently implemented, KPIs/KGIs in place, and the content of dialogue with investors. An image of the relevant pages of other companies' IR materials is shown to us.
- I think **investors are also exploring the connectivity** between sustainability efforts and business performance (sustainability efforts' impact on business performance). We find it meaningful to engage in **dialogue with those who are willing to figure out with us** how to use logic and systematize**,** **as we can gain insight**.

Opinions Voiced in Interviews with Companies (Details)

Meaningful engagement, specific investor references and anecdotes

- A common characteristic of meaningful engagement is that **suggestions/recommendations are made from an external point of view**. In our view, investors have an objective view of our business that is similar to an independent director's point of view as well as a variety of knowledge and insight that don't exist within a company. Such perspective may not necessarily harmonize well with our industry or our company's structure, but we appreciate it as there are times when it is missing in our specialized operations.
- We feel that we are engaging in good dialogue with **investors who present specific proposals**. Although the content varies widely, some investors want to discuss general corporate value with a broad agenda. We can have a fruitful dialogue with those **who can systematically show us** what kind of equity story we should follow to increase corporate value, associated with finance and other related data. In the course of such a dialogue, differences between their view and our view become extremely clear, and we can directly communicate our view as well.
- **Sector knowledge is important in terms of "counter-management,"** but we could have more meaningful dialogue if they tell us how they see things **from the perspective of an organizational theory**. Some of the investors who manage their own investment management company are able to discuss how to change an organization from a management's point of view based on their own experiences. It is great to get opinions and encouragement from people who are in the same position, as we, in our role as management, are not 100% sure about our efforts, either. It is **important for both parties engaged in a dialogue to see eye to eye**. In dialogue with top management, we receive harsh criticism more often. But we want to **value investors who grill us** for follow-up on past dialogues, to see what we have since completed or if any progress has been made.
- We have been **disclosing ROIC by business** since FY2023. This is based on a suggestion made during dialogue with investors on the difficulty of making decisions without capital efficiency KPIs for individual businesses. It had already been under consideration internally, but the suggestion **helped us finalize the decision**. Our main focus is on a B2C (business-to-consumer) business, but we also have a B2B (business-to-business) business, which is rare in our industry. Sometimes we are questioned about why we have the business, but investors will understand if we give them in-depth explanations on the synergies with B2C and products born from the (chemical) business. Investors who don't know much about our company may be concerned that it will lead to a conglomerate discount, but we explain to them that our research is all linked and that it will lead to a reduction of raw material costs, among other things.

Opinions Voiced in Interviews with Companies (Details)

Engagement with room for improvement, specific investor references and anecdotes

- As an example of an unsuccessful dialogue, a representative from one of our investors was unable to see eye to eye with us and another person from the same company (investor) had to intervene and ultimately settled the situation. His/her question was about our long-term vision, and s/he **grilled us by citing an idealistic theory** that a business company normally has a vision of itself in the future, and saying: "If such vision and plans for achieving the same are disclosed but the subsequent implementation of relevant measures is not explained, it is not possible to make a judgment as a long-term investor." We told him/her that our company was at the stage where we finally got out from under an operating deficit and just started earning profits steadily, and in this phase we still had a long way to go before we could have an ideal image, even though we saw it was there. In this meeting, s/he reproached us unilaterally and pressed us furiously, asking why we could not answer the question. No matter how many times the question was repeated, all we could say was, "We cannot do it now. We haven't done it." So no dialogue was established there. We are at a loss as to how to respond to those who, without a good understanding of our company's situation, come to accuse us for failing in this or that, based on standards for large companies with advanced IR/SR activities.
- **Those playing a consultant-like role who are hired/commissioned by investors and request dialogue with us about engagement hold dialogue with us like critics with no sense of ownership**. We don't find it very meaningful. Most domestic investors do not use these consultants, but foreign investors retain them in some cases.
- Frankly, we don't have many. We engage in dialogue with numerous investors, and some investors have opinions that are completely opposite to other investors'. As such, we try to capture the greatest common divisor-like opinions in the capital market. We accept the fact that there will be opinions that differ somewhat, and no dialogue has been meaningless to us. We have not been formally checked very often, either. Since my days as a section manager, I have been in charge of every engagement and engaged in dialogue with the same people (on the other side) every year. **The dialogue is never a mere formality because discussions build upon past discussions.** I am now on the board of directors; the board members' dialogue can make it somewhat easier to provide internal feedback. However, due to an increasing number of interviews, the roles are gradually being shared. Depending on who conducts the engagement, its impact on the company can vary.
- Suffice to say, it is difficult to engage in dialogue when it is **based on formal numerical standards**, such as "no foreign directors," " independent directors are not the majority," or "dividend payout ratio has not reached XX%." Speaking of foreign national directors, the purpose is to gain global knowledge. Since there are Japanese who also have global knowledge, it doesn't necessarily have to be a foreign national, **nor does it mean that global knowledge can be gained if a foreign national is formally appointed as a director**.

Opinions Voiced in Interviews with Companies (Details)

Engagement with room for improvement, specific investor references and anecdotes

- We are a little frustrated by investors who only ask **perfunctory questions** when their standard for **shareholder returns**, etc., is not achieved, saying, "Why does it not exceed this standard?" TSE's request for management to be conscious of capital costs and other factors essentially represents an expectation for improved profitability and growth. Our company business is in a growth industry with a future increase in demand expected, so our investors are divided into those who believe there is a need for further growth investments to increase future returns and those who believe there is a need for increased shareholder returns. Some foreign investors with high-level demands for shareholder returns ask for increased shareholder returns, while some hedge funds want to see more investments in growth; they cannot necessarily be classified by investor attributes, but probably by each fund's approach.
- **Even in meaningful dialogue, there are some topics for which perspectives differ between investors and a company,** and that part (of the dialogue) doesn't go anywhere even after exhaustive explanations are provided. One of them is the thinking as to conglomerates. Investors prefer risk management through diversification, by diversifying their investments. Companies have to consider diversifying risks within the company and thus conduct business portfolio management based on risk diversification. **Conglomerates tend to be negatively evaluated.** We focus on providing explanations covering synergies, but opinions often stay split even after meaningful dialogue. In addition, opinions can be split about how much leverage a business should have. For equity investors, higher/extra leverage is better, and they ask us to increase leverage (on the other hand, they want us to buy back shares), but the desirable level of financial health depends on the business. For a stable business centered on public works and domestic projects, increasing leverage is relatively feasible, but to increase leverage for a company engaged in a highly volatile business with many overseas projects is difficult as its counterparties in transactions often place weight on its financial health. **As a company, we believe that enhancing financial health will lead to higher corporate value over the medium to long term. However, many investors insist on higher leverage from a short-term perspective, and the dialogue often ends in vain.** However, even on these subjects, there is something we gain if we deepen discussions; they are **never meaningless as a dialogue**. As a result, in many respects, investor input is reflected in our business policy. In order to help investors understand the conglomerate's synergies, we try to explain how we understand them. Currently, some of the businesses are grouped together. The core competence of each business has its own target markets, but each core competence has evolved according to customer needs in each market. As a result, the original core competence is linked to other aspects of the business, such as being used in other markets. We explain these circumstances using case studies. It is difficult to quantify contributions made by a particular core competence in a particular business. We feel that the lack of quantitative explanations may cause a lack of persuasiveness, although we provide a qualitative explanation that without this project, the next project would not have developed.

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Engagement with room for improvement, specific investor references and anecdotes

- Impressions vary considerably depending on whom we have dialogue with. Some have informative/helpful and interactive discussions with us, while others just ask us prepared questions. We find that dialogue in which a question is just answered before moving on to the next question with no further discussion is not very meaningful. Our company values the enhancement of corporate value (shareholder value) over the medium to long term the most. The majority of investors also have a medium to long-term perspective, but on rare occasions they ask us **only individual, superficial questions**, such as short-sighted questions or questions about our own share repurchase plans (which cannot be answered); such dialogues are disappointing. These dialogues account for about 30% of the total.
- We sometimes have interviews that seem as if they are for filling out a check sheet, but that doesn't mean they are useless. We don't think it is a waste of time, as we can learn what items investors are checking. As a premise for this, one institutional investor uses a check sheet in interviews in accordance with its internal rules. **Going forward, we want check sheets to be filled out by administration** so that they can spend more time on substantive dialogue with management. Check sheets are probably fine-tuned for each industry with respect to emissions, supply chain items, etc.
- We don't have much pro forma engagement. On the other hand, investors who send in their answers to a preliminary questionnaire and **ask the same questions but no further questions** during the actual interview **may simply want to make sure that they ask questions**. One in ten institutional investors is like that. In addition, if in-depth questions are not presented about non-financial information and human capital, we get the impression that they are merely asking pro forma questions. An investor who engages in pro forma dialogue tends to be more of a passive investor. While passive investors may not need to have detailed engagement with the substance of individual companies, we get the impression that they do so just because they feel they have to.
- We have never found it insignificant. Naturally, our opinions cannot accord with all investors'. Disagreements and tense dialogues exist, but in the first place, **our goal is not to come to an agreement** with investors, but to have a dialogue with them. Asian hedge funds focus mainly on confirming short-term performance, but even such cases provide a learning experience because we can see what they are interested in.
- The biggest gap we see with investors in dialogue is in terms of **time horizon/frame**. Our company is oriented toward long-term management that creates value over the long term, but hedge funds, in particular, discuss topics over a shorter time horizon, such as our profits for next year; thus, our time horizons don't match theirs in some cases. Some of the investors who view us as a conglomerate question why our businesses are so diversified, suggesting that a company should be in a single business (Pure Play) as portfolios are constructed by investors. However, we try to sufficiently explain our belief that there is significance in having multiple businesses within a long-term time horizon.
- We also treat **engagement by activists as their opinions, just as we do for other investors**.

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Engagement with room for improvement, specific investor references and anecdotes

- In rare cases, some investors **ask for explanations on our disclosures, without reviewing them at all**. It is difficult to describe how we feel when they tell us: "We are approaching you for the first time because this is a great opportunity now that your company share price is at a historically low level."
- Sometimes, **engagement from an ESG perspective** feels like a formality. **The relation to our business performance** is ambiguous, and ESG themes and our short-term performance have quite different time horizons. Sometimes, we end up in **one-dimensional discussions completely detached from such perspective**. We do understand that ESG efforts are about creating future value, and that our ESG efforts can attract new funds or cause us to be introduced in a positive light, which leads to a better brand image. However, as it is difficult to clarify their individual relation to financial goals, we tend to get into individual specifics. Maybe we are still in a transitional period. We understand that in some cases, starting with form/appearances is important, and then meaning is created accordingly, but there are also **some things that conflict with financial results, such as short-term cost increases.** We try to find a way to reconcile these things, even though we are constantly struggling, to be honest.
- All dialogues are important to us, given the diversity of players in the market. That said, it is difficult to say that **dialogue just to review recent business results** is meaningful, as there are limitations on what we can say. Note that such dialogues are few in number; there are not many.
- We have some **checklist-based dialogues**. But personally, I don't feel bad about them. **The fact they have researched and prepared before asking precise questions is proof that they reviewed our disclosures, which is absolutely no problem. The worst thing is when they haven't studied**; I have a problem with asking questions about what was just explained in the middle of the earnings briefing (questions about the discussion process or internal feedback, etc. are acceptable but not about results, per se). We can't help it but many investors seem to consider us as merely a new investment target.
- There are still a certain number of investors who respond to us in a pro forma manner. Investors play various roles in the market, and we don't necessarily intend to deny their existence. **From an IR perspective, however, there are some dialogues that we believe do not lead to increased corporate value.** Our impression is that hedge funds run by individuals are only interested in short-term performance, concerned mainly with the validation of their own models and confirmation of the numbers they estimated. We cannot say dialogue with them will lead to increased corporate value.
- As for dialogues in which only an idealistic image is demanded/presented, they are not completely off the mark. For instance, narrowing down the product lineup is more effective in terms of using R&D expenses efficiently, but the production of a product that has been used by customers in part of their life cannot be easily ceased. **We understand their philosophy, but it lacks a customer perspective**. As a business company, we have to seek a balance between the two.

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Engagement improvement initiatives

Effective use of independent directors

- In accordance with requests from major Japanese institutional investors for dialogue with independent directors as well as recommendations from analysts that dialogues should be held to dispel investors' concerns over M&A discussions at the board meeting, **small meetings with independent directors** were held prior to the shareholders' meeting, the details of which were covered in an integrated report for purposes of wide distribution. In considering how to utilize investors' voices to improve our corporate value, small meetings with independent directors have become a key point at this time. Pursuant to a specific request from one analyst from a securities company to host a small meeting, we asked him/her to facilitate the meeting and decided to have the meeting be hosted by the securities company. We had asked our independent directors (attendees of the meeting) to express their frank opinions, as **we believed that having independent directors speak freely at a small meeting would convey a message to investors that decisions are made at our company based on a variety of opinions**. We also had confidence that they would not make any controversial statements as they are seasoned executives with experience engaging in talks with investors. The small meetings were well received by investors. Particularly, the fact that **only independent directors participated in the meeting and all of them participated was also greatly appreciated**.
- Our company's independent directors actively express their opinions at the board meetings, and some proposals are rejected because of their opinions. Our company is run by the founder, and some investors don't have an image of whether the board of directors really functions. To such investors, we **present the actual status of our independent directors and explain that the effectiveness of the board is ensured**.
- Our president has engaged in dialogue with many investors in Japan and overseas. We also have received many requests for dialogue with independent directors, and we are planning some change in our style to **increase opportunities for independent directors to participate in dialogue**. We are also planning to increase opportunities for not only the president but also each business company head to talk directly with investors.
- **Each business division head sometimes gives business briefings**, and **panel discussions by independent directors** are also held. Information is transmitted while the number of participating members is increased.
- We receive an increasing number of requests from foreign investors, **particularly from European investors**, for having direct dialogue with independent directors to hear how the board is committed to governance, board effectiveness, and environmental issues. On the other hand, an effective method for investor engagement by independent directors is an issue to be discussed.

Opinions Voiced in Interviews with Companies (Details)

Engagement Improvement Initiatives

In-house Feedback

- Useful opinions are fed back to management at monthly meetings of the Stakeholder Communication Committee and to the Board of Directors in the form of reports by the CFO on the status of business operations, including the content of dialogue with investors and updates on voting criteria. Whether or not to actually reflect the opinions of investors in management is a management decision, but **efforts are made to increase persuasiveness by adding data and other reinforcement**, rather than simply raising opinions. In addition, as independent directors are as proactive in their opinions from an external perspective just as investors are, feedback is also provided as necessary outside of reports on the status of business operations.
- In some respects, **dialogue with directors facilitates internal feedback**.
- The quality of engagement has improved each year as a result of two-way communication, with investor feedback to the board of directors and feedback to investors on how the board has acted as a result of their feedback. **Investors also become more serious when they think their views will be fed back to the board.**
- ESG-related topics are often new and take time to permeate to management, or are difficult to bring up within the company because of the costs involved in responding to them. However, a positive cycle has been established in which, **through engagement, we receive opinions from the investor's perspective on future prospects and other matters**, and a summary of these opinions is **reported to management and the board of directors**, which then **discusses the direction of future measures with the board of directors** based on these opinions.
- We are committed to communicating internally and externally, including through dialogue with the capital markets. The president himself places **great importance on internal dialogue**, and sometimes he himself goes to each factory to visit the worksites and engage in dialogue. Directors sometimes also conduct ESG briefings for internal and external audiences. We believe that explaining and making sure that people understand things internally also helps to **improve employee engagement**, and as part of this, we provide feedback on the content of our dialogue with investors. People appear very happy to receive praise from outside the company. We reaffirmed that employees are concerned about external evaluations, such as those from customers and the capital markets. Efforts are being made at all levels, including providing feedback to executive officers.
- Evaluation from capital markets naturally affects management. As a way of incorporating capital market evaluations into management, general capital market developments, including the results of the dialogue, have been reported to the board of directors twice a year (February and August) since FY 2022 and this will continue in the future. The P/B ratio is still below 1, but it used to be considerably low. The **members of the board of directors understand such market evaluations and consider management measures based on this understanding**.
- Immediately after financial results and investor evaluations, the board of directors also reports at least quarterly. Independent directors are particularly concerned **about what is lacking in the Company**, and careful feedback is provided.
- The president himself reports and discusses the results of interviews with investors at board meetings. Agenda setting has also been devised to stimulate discussion at board meetings. For example, this fiscal year, under a new management structure, **the newly appointed CEO actively met with investors and fed back investors' reactions to the board**. In particular, this time around, investors were highly interested in mid- to long-term growth, so the board's agenda was set to increase monitoring of that aspect.

Opinions Voiced in Interviews with Companies (Details)

Engagement Improvement Initiatives

Dialogue stance and selection of dialogue partners

- (From the perspective of the SDG Promotion Office), we have selected passive investors and active investors with a strong ESG focus. While we are unable to increase the number of dialogue partners without limitation due to resource constraints, **we review the questions that investors send us in advance and try to accept dialogue requests from investors who have insight into our challenges, even if their opinions are critical**.
- The Company **utilizes a shareholder identification survey** in advance to examine which investors would be effective to engage in dialogue with, and selects investors who have a good understanding of the Company and are willing to give us their critical opinions for dialogue. **Investors who make decisions mechanically and as a formality** cannot engage in meaningful dialogue with us, so we **exclude them from our selection for dialogue partners from the beginning**.
- Regarding **dialogue with overseas investors, we have narrowed down to approximately 80 companies for IR targeting**, and are in dialogue with several of them. If the other party is interested, we will continue to have a relationship with them. It is meant more for expansion purposes than for improvement purposes. **Regarding overseas investors that opposed appointment proposals, we may check their reasons** with them. We believe that if we know the reasons for the opposition, we might be able to remedy that.
- In the past, we have responded passively, but recently **we have been trying to ask reverse questions at the end of the dialogue**. We need investors to expect the stock price to rise, so we ask what would catalyze them to buy more, ask questions about the status of the stock price, etc. It seems that more and more questions are being asked at the presidential level at other firms, and investors are often answering them well. They have thought beforehand about the matters they want to confirm and what they think about our company. We may gain new insights, and investors have similar ideas about what we perceive as challenges. In addition, since the evaluation of the stock price level transition varies from investor to investor, we believe it is better to ask investors directly.
- The **management's dialogue partners** are selected primarily from **investors with whom they can discuss long-term perspectives**.
- Not only do we talk with investors and analysts after the earnings announcement, but we also have a **dialogue with them before the management policy meeting to ask them where the capital market is interested in our company**. Such dialogue will not only help management to use the opinions gained from these discussions, but also improve engagement by **controlling investor expectations**.
- We are not in a position to pick and choose our dialogues, and **the reality is that we meet with those who apply for a dialogue as long as schedules allow**. The dialogue is mainly in the form of responding to what is asked, so we answer questions flatly. On the other hand, **when we participate in conferences or travel overseas for roadshows, we are as selective as possible** and communicate our requests through our brokerage firms so that we can arrange meetings with the investors we wish to meet and have them arranged accordingly to the extent possible.

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Engagement Improvement Initiatives

Dialogue stance and selection of dialogue partners

- The control is in place by the time of the interview. Although there are many requests for dialogue with top management, investors with insufficient understanding are addressed by the head of the IR department, **minimizing the number of less meaningful interviews**.
- As our governance and disclosure has improved, there is a sense that the quality of engagement has improved. **We feel that the basic trust that has been built up by those in charge so far** is working. Because of this, we are rarely given strong opinions when we change something, and we get a lot of advice. **We believe that investors' views differ greatly depending on their past level of trust**, and this continues even once the stock is sold.
- The IR department is trying to **make the agenda clear before conducting interviews**. In particular, when we have a dialogue with top management, we make an appointment after clearly indicating in advance which topics the investors are interested in and which topics we would like to discuss with them. This is welcome on the part of investors, and although it is simple, it works very well.
- We try to disclose information correctly and fairly, like I imagine all companies do. In addition, we basically meet with all investors who request it as long as we are able to make arrangements, and will not turn down an offer. On the other hand, we may target, prioritize, or change the person in charge. The adjustments are **done in such a way that those who are capable of in-depth discussions are handled by those in higher positions, while those who are driven mainly by numbers are handled by the staff**.
- Since the last fiscal year, we have been trying to enhance the **briefing sessions for each business unit**. This is because some investors asked for some basic information, and the head of the business unit explains the business model and the medium- to long-term strategy for each business. As much as possible, we try to **provide information that we believe will help investors make medium- and long-term investment decisions**. We also try to **pick up as many opinions as possible**. As IR, we try to provide feedback to management not only from investors and analysts who have opinions from a short-term perspective, but also from those who can give us long-term opinions.

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Engagement Improvement Initiatives

Enhancing the disclosure and promoting dialogue with global investors

- **As a way to encourage people to read the materials in advance, the company's own website**, which was old and difficult to read, **was updated over the course of about a year**. Although the renewal efforts were not directly the result of dialogue, it was a spontaneous realization that came from a series of dialogues. Prior to IR/SR meetings, we also try to inform investors of the URLs of the documents we want them to look over.
- The content of the briefing is transcribed in the evening of the day of the financial results briefing and published **using a disclosure platform**. It also shows what kind of explanation the president actually gave at the financial results briefing, what kind of questions were asked, and how he answered them. This is just one example, but we are committed to disclosing everything possible.
- In anticipation of the TSE's ongoing expansion of English-language disclosure, we have begun disclosing English translations of important documents. We already disclose our main documents, such as securities reports, financial results presentation materials, and PBR improvement plans, in English, although there is a slight time lag. **In principle, the different language websites are a mirror of each other, so that a single click on the Japanese website will switch to the same page on the English website**, which is a step forward in English disclosure.
- **Analysis and other information related to M&A, which are frequently asked in dialogue** with investors, were disclosed in the integrated report. Because there were cases of large M&As that did not go well, even though not all of them failed, the capital market had the impression that we were not good at M&A, and investors were concerned about whether we would be able to carry out M&As in the future. Therefore, we felt it was necessary to properly organize and explain what went wrong with the M&A and what was successful, and decided to include this information in the integrated report. **Other items that investors relatively often ask about**, such as how the company conducts **ROIC management**, are also **included in the integrated report to ensure that they are well communicated to investors.**
- The Company has a small market capitalization, which means that it is not an investment target from a liquidity perspective. Some U.S. investors do not extend their reach to small-cap Japanese stocks. **We believe that we need to increase our market capitalization**, and we must **work steadily to promote our appeal.** Mainstream U.S. investors are buying for passive management, but not for active management. We are still **experimenting** with approaches.
- Within asset management companies, there is a division between those who make voting decisions and those who make investment decisions. For this reason, we have traditionally prepared **a document** "Governance and Sustainability Initiatives" **that collects only the points that those exercising voting rights focus on.**
- We try to **give investors materials in advance**. If it is a dialogue before the General Assembly, we present materials on the General Assembly proposal and the skills matrix, as well as the results of the effectiveness evaluation, and we also present materials on the results and issues to get feedback from investors.
- It has been four to five years since we started publishing the integrated report, and with the help of management, we are brushing up the report while considering **how to connect the words to strike a chord with investors**.

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Engagement Improvement Initiatives

Enhancing the disclosure and promoting dialogue with global investors

- During the dialogue on ESG themes, we prepare a 20-30 page PPT document and explain the most recent progress for about 30 minutes, followed by a discussion. Instead of repeating what is disclosed in the integrated report, **the explanation focuses on the changes that are being made based on investors' opinions**.
- In order to realize a fruitful dialogue, it is necessary to communicate in an easy-to-understand manner, for example, in the integrated report, **what stage the company recognizes it is at**.
- The characteristics of foreign investors are not necessarily due solely to regional factors, but there are **distinctive features depending on the region and the type of investor**. North American investors are highly interested in individual businesses, and we receive feedback that they want us to make solid growth investments to grow their businesses. On the other hand, European investors, many of whom are value investors in addition to growth investors, often ask about shareholder returns. In addition, European investors often ask questions not only about financial indicators, but also about sustainability, environment, and governance from active fund managers themselves, whereas North American active investors rarely ask about such items.
- I believe that Japanese institutional investors also consider non-financial values as part of ESG integration when making investment decisions, but **my impression is that in Europe, non-financial values are also evaluated by fund managers**. **Overwhelmingly, European investors** have expressed a desire for dialogue on topics focused on sustainability, such as requests to hold small meetings **on specific themes within sustainability** (e.g., "water").
- **Disclosure is a fundamental tool for dialogue**, and we are working to expand our disclosure. Perhaps a dialogue may take place to fill in the checklist when the disclosure information does not fill in the checklist on the part of the investor, but we have not experienced any engagement just to fill in a checklist.

Cross-shareholding

- Based on the dialogue, the company announced its policy to reduce its cross-shareholding by 50%. Despite being perceived internally as a bold decision, the company announced its policy to reduce its cross-shareholding by 50% over three years because, in talking with investors, it believed that it would not be able to gain their understanding unless it reduced its cross-shareholding by this amount. One investor pointed out that this would still leave 50%, so we additionally stated a policy for subsequent reductions. Although there was some protest from internal sales and other parties, the decision was **made top-down as a company policy**. What I feel every day in my interactions with investors is that acting in silence is not appreciated. **If a policy has been established, it is important to disclose it, including the direction.**
- Some investors, for example, may present their own numerical standard for cross-shareholding and told that we must meet it. **Since it takes time to reduce cross-shareholding**, there are some difficulties even if we are asked to reduce them right away.

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About Institutional Investors

- In particular, I think it would be **more meaningful** for institutional investors participating in SR meetings **if they could read through the disclosure materials, especially those provided in advance, even if only briefly, so that they can start the dialogue with a clear line of sight**. Then, taking into account the individual situation, it would be a fulfilling dialogue if the investor could lean in and offer advice rather than just asking questions from an idealistic viewpoint at all times. It would be ideal if we could make improvements based on the advice, report back in the next dialogue, and get additional advice.
- In most cases, the staff is informed in advance, but **if ESG and other issues are included in the dialogue agenda, it would be helpful if the staff is informed of these in advance so that the arrangements can be made smoothly**.
- Perhaps due to differences in management styles, **there are cases where different management teams within the same management company,** whether in Japan or overseas, **each apply for dialogue**, and **the reality is that the dialogue covers overlapping topics,** such as business performance and mid-term management plans. We don't know if it is okay to ask them to adjust internally, but as long as they have different management teams, we consider them different investors and take up dialogue.
- We receive many requests for additional disclosure from investors, but we are at the very limit of what we can disclose, and if we disclose more than this, it would reveal sensitive information about our business and business operations, and our competitors would be able to see it. In light of this, we are spared by refusing to disclose any more or by explaining things vaguely. Investors would probably prefer to receive detailed information, but there is a struggle because it would also leak information to competitors. Investors understand this point and are **probably trying to get as much information out as possible while probing the very edge of the market**.
- It will be easier to explain and persuade management and board members if they are introduced to good examples of other companies and cases that have led to improved performance and increased corporate value. The investor's opinion may seem outlandish at first, but five years later it is often seen to be true. Therefore, we try not to take opinions negatively even if they differ from our own point of view. On an individual basis, there are those who approach dialogue with a belligerent attitude, or those with whom dialogue ends simply with a yes or a no. However, **we hope that we can have a positive discussion about what we are not achieving and how we can do it, taking into account examples from other companies**.
- **If there is a strong request from a new investor, we may be open to dialogue.** In such cases, the investors do not understand the company's situation, so at first we feel that they make formal comments and have a harsh view of the founder's management. However, as we continue our dialogue, we are deepening our relationship with investors through dialogue, as they come to understand our unique way of doing things and the advantages of our company and are able to give us advice on this basis.
- **The level of shareholder return depends on the company's growth stage**, and there are times when it should be used for investment in growth rather than return. The discussion would be more engaging if it were based on the company's stage, in the form of whether returns should be reduced and put into investment for growth, or whether it is time to increase returns.

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About Institutional Investors

- We would like to ask investors **whether sustainability disclosure is really necessary and beneficial in investment decisions**. While the quality of corporate disclosure needs to be improved, we **expect investors to engage in in-depth dialogue based on an understanding of our situation**, rather than simply asking one-size-fits-all questions or simply demanding a level of shareholder return, etc.
- In terms of corporate governance, we believe that, although the formal aspects are in place, the effectiveness of the substantive aspects needs to be improved, but **we feel that there is a polarization between those investors who only respond formally to stewardship and those who are willing to work on the substantive aspects**. Engagement is bidirectional, and with the same direction, we want to improve corporate value over the medium to long term, and we hope to increase dialogue with as much substantive depth as possible.
- For example, some investors say that society should respond in a certain way to climate change, so we should do the same. There are opinions that include such views, but we hope that it is understood that our base is to enhance corporate value, and that we are acting based on social demands within that context. Individual shareholders, institutional investors, domestic investors, and foreign investors each act based on various ideas, which is fine. Our **basic stance of increasing the value of our company should be shared by all investors**.
- Currently, there are not many dialogues that can lead to a return for the company from a medium- to long-term perspective. Not necessarily hedge funds, **but I have the impression that there are still many investors with a short-term perspective**, so I hope we can have a more constructive dialogue. We hope to receive more and more useful advice.
- **The purpose of the dialogue is not to agree with investors, but we want them to have a long-term management perspective as a time frame.** We get the impression that the trend over the past few years **has been for the capital markets to shift their focus more toward the short term**. We are sure that the macro situation has affected the company, but **we would like to see an evaluation of the company's long-term management**.
- Some people say, "Since portfolios are set up on the investor side, companies should be a single business (Pure Play)," but **the fact that a fund reconfigures its portfolio and a business company reconfigures its business portfolio are two different dimensions**. While shares can be easily bought and sold, a business company with employees cannot easily let go of a business. We would like to see an assessment of the value creation of a diversified portfolio of operating companies, not only from a financial and short-term perspective, but also from a long-term perspective.
- We understand that short-term performance is important, but we would be happy if people could give us an external awareness of not only the most recent performance, but also a better **understanding of the characteristics of the industry and the business**. In particular, our commercial products are special and perhaps even peculiar among durable consumer goods. We believe that investors look at various industries in a flat way, and we would appreciate their understanding of this as well as their opinion. It is not a product where everyone can be a customer, and there are industry characteristics that arise because of this. We feel that it is difficult for investors who look at a company as a brand to understand it.

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Requests and Opinions

About Institutional Investors

- New investors are increasing in number, partly due to the recent focus on Japanese stocks. However, I have **the impression that there is a gap in competence even among newcomers**. Even if someone is a newcomer, if they are knowledgeable in analyzing other industries, they will ask sharp questions. I feel that there is a clear difference in the ability of investors to ask questions, whether they simply want to be told what to do, or whether they ask questions about what they don't understand in assessing the value of a business.
- There was a lot of formality-level engagement for a while after the Stewardship Code was established, but **it has improved a lot in the last few years**. However, it is true that there are times when we are interviewed from an ESG perspective or from the responsible investment department, but there are cases where we feel that we are being engaged with according to a template. As a company, we would be grateful if people could go into more detail and discuss with us the initiatives we should take and the policies we should follow after proposing them. **Some only tell us examples from other companies, but it is often questionable whether it will work in our company**, and it is hard to be uniformly told what to do. Specifically, the ratio of female managers is often mentioned, but we would appreciate it if people could indicate what the industry as a whole should do and how we should address this issue as a set.
- Companies also need to think about how to approach their disclosures, but there are many investors about whom we wonder if they are really looking at the disclosures. While we have issued various reports such as integrated reports, corporate governance reports, annual securities reports, business reports, etc., **we feel a sense of futility when we are asked again what we have already disclosed**.
- Institutional investors are increasingly demanding IR events. Evaluated company events are **evaluated based on the number of events**, such as suggestions that it would be great if we could do small meetings with the CEO at least twice a year, small meetings with the CFO, small meetings with external parties if possible, briefing sessions in the IR and R&D departments, plant tours and laboratory tours, etc. We know the advantages of each and would like to do so if possible, but most events are now hybrid events, which increase the burden on the organizers. **Please understand that there are limits to resources on the IR side**. In addition, since events are very labor intensive, we would like to ask for quality feedback from institutional investors. We would like to mutually enhance each other.

(To voting advisory firms)

- The company is a generalized company in Europe and the U.S., and is considered something like a rating agency. The great thing about the West is that these companies are coming out of the private sector. If I may add, Company A is too busy to meet with us. Whenever we call on them, we cannot engage in dialogue. There isn't a balance between the size of the influence and the system. Company B meets with us and we have dialogue with them regularly. If we can have a dialogue, we would like to hear their true feelings about approval or disapproval and the future direction. In light of what would happen if there were a shareholder proposal or proxy fight, etc., **we want to have a dialogue on a regular basis**.
- In the interests of fairness, although the decision to recommend approval or disapproval is made in a by-the-book manner, it would **be nice to see a little more flexibility**.
- Speaking only about voting rights, **it is true that different advisory firms have different views**, and it is sometimes difficult to know which way to turn.

Opinions Voiced in Interviews with Companies (Details)

Requests and Opinions

To the Financial Services Agency and Tokyo Stock Exchange

- When a request is issued by the TSE, etc., it is a momentary shock, but on the other hand, if the request is made public, **it becomes easier to make moves within the company** because the request has been issued and it is necessary to do so. We can use the **requests as leverage to** move forward, which we appreciate, but small- and mid-cap companies like ours are perplexed when requests are issued for large-scale initiatives that cannot be undertaken without external help, such as consultants. In such cases, **it would be helpful if there are relaxed deadlines and timeframes** to facilitate efforts by each company according to their individual circumstances, so we would like you to continue to give consideration to this issue.
- There has been a bit of a buzz in the internal news that our disclosure has been selected by the TSE Casebook as a "company with outstanding dialogue with shareholders and investors." We are relieved **that the direction of the IR Department's efforts has been objectively proven to be correct.**
- **Simultaneous disclosure in English** is also a high hurdle. We inevitably have to outsource to a translation company, **but the translation company cannot finish the draft on the same day it is received**. This has to change from a fundamental approach, and there are also systemic problems on the part of translation companies. It is true that this is a heavy burden for smaller companies. We just have to decide to do it and execute it if that is what the market demands, and **we believe we can eventually do it if we are given enough time.**
- **The number of disclosure items in the securities report is increasing, and** we are wondering **what the future relationship will be with integrated reports, which have a strong free-standing meaning.**
- **We would like to see the Japanese market revitalized**. Even with the start of the new NISA, it is a shame that personal assets will flow to the US. Now is also a good time to get more initiatives underway. Since foreign investors have a certain percentage to allocate to Japan, they need to increase their percentage in Japan or they will not get their money's worth in small- and mid-cap stocks. We also feel that it will be difficult without raising the status of the Japanese stock market, so we hope that you will actively pursue this initiative.
- The number of disclosures, such as the securities and CG reports, has increased over the years, and so has the workload. Since there is some overlap, we would like to document only what is really important and **for you to consider reducing unnecessary disclosures.**
- I believe that investors' opinions will be realized in five years because JFSA and TSE are working on it. The method of first putting it into a soft law, the Corporate Governance Code, and then finally into disclosure standards, suits Japanese people. Japanese people are so serious that while only 30% disclosed a year ago, 80% did so this year. We would like to see **measures that take advantage of the diligent nature of the Japanese people**. Also, when **changing systems, etc., it is easier for us to do so if the changes are drastic** rather than half-heartedly made in stages or in a transitional manner.
- The burden of disclosure on companies, including sustainability disclosure, is increasing. Where it has been pointed out that there is a widening gap between firms with respect to governance, **there is concern that an increased burden of disclosure** can be handled by firms with adequate human resources, but that it will be difficult for those without such human resources to cope **and that the gap between firms will widen further.**

Opinions Voiced in Interviews with Companies (Details)

Requests and Opinions

To the Financial Services Agency and Tokyo Stock Exchange

- The Working Group on Tender Offer Rule and Large Shareholding Reporting Rule of the Financial System Council has recommended that, as a principle of conduct for institutional investors, they should respond to questions from issuing companies about their holdings, and that, in the future, such responses should be required under the legal system. We welcome these recommendations. **Even in making requests to companies, investors should at least state whether they own stock.**
- Since we are not promoting initiatives at the request of the government, etc., it is difficult to give our opinions. When discussing where to benchmark, investors have sometimes suggested that overseas companies should be used as benchmarks, so we are not only comparing with companies listed on the TSE. While this is not a request, we feel **that it would be good if more companies aim to become global excellent companies**.
- **The disclosures are not made just for the sake of disclosure, but are also compiled as information for the internal corporate organization**, so the fact that disclosure is required does not mean that there is a hassle, and we do not believe that the disclosure items are excessive. If overlapping disclosure is required, we would be happy to review it, but we are aware that there has already been discussion about securities reports or financial statements, and there are no additional items that we would like to request action on.
- In the past four to five years, requests for listed companies have been increasing, and as a company we have been **investing resources to respond to these requests**. The pressure is on to compete in the free performance while doing the regulation performance that corresponds to the system, and the fact that you have to look aside. There are thousands of companies, and we want our reality to be understood. **With regard to sustainability disclosure, it is important to consider how to enhance corporate value in the face of uncertainties.** We think there are things that investors themselves do not understand, so we hope that companies and investors will discuss and study each other to create a desirable state.
- There are issues that need to be addressed to reform and revitalize corporate governance, but it would take a lot of effort and time to respond to all the various information disclosure requirements. It is difficult to deal with various standards when they are in disarray, so **it would be appreciated if only the general framework is set and there are areas that can be freely moved**. Important themes differ for each type of business, and it is difficult to deal with them if they are stipulated in detail. We would also like to see a **certain amount of time** between the rules being gradually stipulated and the actual disclosure. If we try to get data from dozens of group companies, it will be necessary to build a system. **We would like to refer to a collection of good examples of companies that have successfully responded** in a variety of areas.
- There is an overlap in requests for sustainability and climate change disclosure between Japan and other countries, increasing the burden on companies. While there are a variety of ESG evaluation organizations, the large number of subjects that the evaluation organizations need to investigate does not allow them to properly check and evaluate all of them. **It would be good if disclosure standards are standardized internationally to clarify what to look at to get the necessary information.** In addition, we are sometimes told by European investors that they cannot invest in the future if we do not meet these standards, but it is difficult to conform to all the standards, so **we hope that the standards will be standardized**.

Opinions Voiced in Interviews with Companies (Details)

Requests and Opinions

To the Financial Services Agency and Tokyo Stock Exchange

- While our awareness of stock prices is high, there are some factors that are beyond our control. Essentially, we understand that the greatest effort we can make is to improve performance, and **our mission is to increase the numerator, even if it is ROE**. We hope that discussion will not turn to strengthening returns to support the stock price.
- Although the criteria for exercising voting rights differ between global and Japanese investors, I wonder if there is something wrong about the fact that opposition increases when there are more foreigners as shareholders. I know that you are constantly discussing with METI and others **what Japanese companies can do to make domestic and foreign investors and the GPIF, which manages our pension funds, happy**, and I hope that you will continue these discussions. Both companies and investors need to think about this. While we are grateful that you are leading the charge on cost of capital and sustainability initiatives, **companies cannot respond in a one-size-fits-all manner**. Discussions should continue in the future.
- As a request to JFSA, **some activists are increasingly appearing in the media, and we feel that a trend is beginning to emerge where only the parts of their arguments that are considered correct are extracted and endorsed**. On the corporate side confronting activists, we feel that their opinions are still short-term in perspective and are intended to create their own benefit, and that excessive media exposure and attention, good or bad, is questionable. We hope that the authorities will draw a line from such a trend and control it well when necessary.
- One request to the TSE is that the **TDnet CG report entry site is not user-friendly and the presentation does not work as desired**. We feel that improvements are being made, but the system could be a little more flexible.
- We have another request for JFSA and TSE. Although progress has been made in organizing quarterly reports and financial statements, the same information is required to be disclosed in securities reports, notices of convocation of general meetings of shareholders, corporate governance reports, and other documents. The number of items to be disclosed has increased, the colorization of the securities reports has progressed, and the **securities report is starting to morph into an integrated report**. We think the issuing company needs to sort this out, but could you please put some rules in place to sort it out in the first place? We are also required to disclose the securities report as soon as possible, and our manpower is limited, so we would very much appreciate it if you could help us sort out this issue.

Opinions Voiced in Interviews with Companies (Details)

Initiatives to ensure increased Corporate Value

General Comments / Ensuring the Effectiveness of the Board

- When the board chairperson is external, the chairperson naturally participates in the pre-meeting before the board meeting, so from that point on, outside knowledge is brought in. For example, we can receive advice based on experience at other companies in advance to use on the day. On the day of the board meeting, the chairperson, who is also an independent director, handles the agenda himself, so the meeting proceeds with a more tense atmosphere compared to the days when the chairperson was an internal director. While it depends on the style and qualities of each individual, in our case, **having someone from outside the company chair the meeting has improved the objectivity and transparency of the discussions**.
- We are incorporating independent directors because we believe that prime companies will eventually require a majority of independent directors and that it is better to do this early. In the past, we had just one, but two years ago they became the majority. While there were some reservations when there was just one, I think it has become easier to speak up when there are two. The more this number increases, the easier it will be to make a statement. **With a majority, the number of internal directors became small, so the opinions of independent directors naturally became more important.** It has had a profound effect in moving the board from an inward-looking posture to an outward-looking awareness.
- In the officers' skills matrix, we were told that we should clearly show the logic as to why we consider those skills important. We accepted the investor's request and try to show in writing why the skills are needed. **The part of the skills matrix where everyone is circled is the same as if everyone was not circled.** From this perspective, only those with top management experience are allowed to have a circle against the global management items, for example.
- Although **officer compensation** was based on profit, as was the case with many companies, many investors told us that **we should also focus on capital efficiency**. Therefore, **we also incorporate ROE and ROIC perspectives**, and this is also evaluated.
- Corporate culture and the sense of top management are also important. Some managers think that independent directors lack knowledge, but the **attitude of the top management is important, and the sense of the top management is propagated to other directors and employees**.
- In terms of diversity, there is only one woman on the board of directors, and we believe this needs to be improved. **One person makes a difference, but as with independent directors**, we believe that **more change will come as the number increases**.
- We could clearly see the **importance of diversity on the board of directors** through engagement, and we realized that **we need to work on the board of directors**, as we have also set a goal of 30% female officers by 2025. We believe this was an situation that gave us a sense of what investors are focusing on and what trends we can expect to see in the future.

Opinions Voiced in Interviews with Companies (Details)

Initiatives to ensure increased Corporate Value

General Comments / Ensuring the Effectiveness of the Board

- As a secretariat, we are most concerned about how to make the board of directors meeting fruitful. In addition to explaining the meeting to the directors in advance, **the secretariat believes that the most important thing is to set the schedule and agenda**. Our board of directors is gradually moving to a monitoring model, with input from independent directors. The authority has been delegated to the executive side for the past two to three years to allow more time for discussions on the mid-term management plans and the larger direction of the company.
- Independent directors have given us many opinions, and in addition to the questionnaire for evaluating the effectiveness of the board of directors, we have received comments at board of directors meetings such as "we should have more discussions like this" and "we cannot have deep discussions without such materials and figures," and we are **improving the agenda setting and explanation methods** on a daily basis. The effectiveness evaluation identified the enhancement of discussions on growth strategies and ensuring adequate deliberation time for important agenda items as issues to be addressed, but the situation is gradually improving. Currently, **approximately 70%** of the board meeting time is devoted to **strategic discussions** (mid-term management plan, human resource development, M&A) and reports on the execution of duties. There are other matters to be resolved, such as individual investment projects, but in general, there are many matters to be reported and deliberated, and the **majority of the time is spent exchanging and discussing opinions**.
- We continue to be a company with a board of auditors as our institutional design. Although not a matter of insistence, the institutional design is also discussed in the evaluation of the effectiveness of the board of directors. At the current time, we do not see the benefit of transitioning to a company with an audit committee system, as the system is working to improve the effectiveness of the board of directors. We are unique in having a governance committee. In addition to the response to the Corporate Governance Code, we are discussing the contents of the effectiveness evaluation and how to address the issues, and **how to establish an appropriate system for the company, based on the internal situation**.
- **Immediately following each board meeting, a review meeting is always held with only independent officers** and the results are reflected in the items to be discussed the following year. At the review meeting, the participants are asked to evaluate whether the management and agenda setting were appropriate, as well as to self-evaluate their own discussions. The results of the review meetings are fed back to the relevant departments and executives, with the secretariat undertaking those that need improvement in the short term. Items that should be considered in the medium term are reviewed throughout the year and reflected in the following year's agenda, which is discussed by the Corporate Governance Committee before being reflected in the following year's initiatives.
- The **spirit of corporate governance has long been rooted in the company and has been passed down from generation to generation**, as evidenced by our participation in preparatory meetings for the OECD's Corporate Governance Principles from the time they were formulated. We believe that this is **best manifested in our corporate philosophy**. We are constantly discussing how to make this understood globally. On the other hand, **it is true that culture has changed over time**, and we continue to discuss how to deepen corporate governance.

Opinions Voiced in Interviews with Companies (Details)

Initiatives to ensure increased Corporate Value

General Comments / Ensuring the Effectiveness of the Board

- The "**Board Culture**" was documented in writing in the Basic Governance Policy. It clearly states the approach to be taken by the board of directors, including the need to ensure both the delegation of authority to promote speedy and autonomous decision-making and transparency in business execution (Empowerment & Transparency), as well as the need to express opinions from a broad perspective. The Governance Committee discussed that new directors should be given not only the skills on the skills matrix, but also the mindset of what kind of board culture they should participate in to fulfill the functions of the board of directors, and that this mindset should be communicated externally, and this was incorporated into the Basic Governance Policy.
- The goal is for useful discussions to take place at board meetings. **The board of directors is also changing** in order to improve effectiveness, and **the results of the effectiveness evaluation are discussed within the board over time**. Independent directors actively participate in dialogue with investors, and the dialogue is planned to include not only the chairperson but also other independent directors. The independent directors are also very positively advancing with initiatives, and we feel that they have the desire to further develop the company and lead it to the next stage.
- On the executive side, we consider it a bad thing that information is not properly communicated to the board of directors, resulting in the board idling, so we try to give the board **time to digest the information** after it has been given to them. Specifically, we have established a **meeting of independent directors prior to the board meeting, where discussions are held exclusively by independent directors**. At the independent directors meeting, matters discussed by the board of directors are discussed accompanied by the relevant executive officers as necessary, and minutes are not kept of these meetings. We try to help them understand the nature of any problem by clearing up questions and having a frank discussion.
- **Even if people change, the initiatives that have taken root as a system are carried on.** While brushing up under the new structure, the spirit has been carried on, and we have realized that once something is on track, it does not change even if the people change.
- **As we join the ICGN** and absorb what is required internationally, we are also discussing whether the board of directors could take on a role of leading in some situations, rather than merely supervising. For example, with regard to ESG, trying to play a leading role in how to consider the direction to take, not just receiving and monitoring reports from executives. **The ICGN was the catalyst for the board of directors to gain a leadership perspective in ESG.** Where ESG-related factors are used as KPIs for executive compensation, the ICGN and others have adopted international standards in this area. With regard to ESG, we have established a Sustainability Committee, whose members are on the executive side, but all independent directors are in attendance. The contents of the Committee are used as a springboard for the board of directors, and once a quarter, in addition to the discussions of the Sustainability Committee, the board of directors, which is independent of the Committee, also holds discussions.
- We feel that the **Board Secretariat plays an important role** in ensuring the effectiveness of the board of directors. In this regard, **we would like to discuss with other companies** what initiatives they are pursuing in the secretariat.

Opinions Voiced in Interviews with Companies (Details)

Initiatives to ensure increased Corporate Value

General Comments / Ensuring the Effectiveness of the Board

- In addition to board meetings, there are **offline meetings (free discussion forum)** with internal and external directors as members, which have been expanded over the past two years. **They regularly exchange opinions on selected themes**, taking into account side information such as voices in the marketplace and developments in the legal system. These offline meetings were triggered by a **proposal from an independent director who wanted to have a more in-depth discussion** in the evaluation of the board's effectiveness. The topics to be covered during the year are decided in advance and are generally conducted monthly. In addition, from April 2024, **a management committee dedicated to themes related to sustainability will be established outside of the regular offline meetings**. We will begin this spring, hoping that board members can discuss based on discussions at offline meetings. The chairperson of the Corporate Governance Committee conducts interviews with all directors when evaluating the effectiveness of the company. The Corporate Governance Committee is established as an advisory committee to the board of directors, where topics to be addressed at the following year's offline meeting are discussed and decisions are made based on the opinions of the board of directors members. The Corporate Governance Committee has a slightly larger number of independent directors, and its chairperson is also an independent director, but the theme of the committee is decided after having each of the internal and independent directors express their thoughts. Recent themes have included human capital, new business development, internal controls, and specific businesses. The board of directors has an important decision-making and monitoring function, **but if it only discusses the issues at board meetings, it will have to make decisions with inadequate information**. We believe that **increasing the ratio of offline meetings will lead to more active discussions at board meetings**. In addition, outside and internal directors are given factory tours to gain an understanding of the work site, and audit committee members are also invited to visit overseas locations. While we have heard that these activities outside of the board meetings are burdensome, they are doing quite well, and we believe they are very significant.
- As a means of ensuring the effectiveness of the board of directors, in addition to providing feedback on market views, we conduct a questionnaire and interviews with all directors once a year. Based on the results, management issues to be taken up in the future are prioritized and reflected in the agenda of the board of directors. Topics, such as how they view opportunity and risk in relation to TCFD and what kind of company they want to be, will be discussed. Execution tends to take a short-term perspective, and there are conversations that can be had only with directors. There are many items that come up for discussion at board meetings, and we cannot discuss them at leisure, but we try to **discuss the long-term strategic plan**, as there is time before we submit it as a mid-term management plan.
- Our board of directors is **very diverse, active, and varied in opinion**. There is a clear separation between execution and supervision, with the board of directors strengthening its independence and supervisory function as a monitoring board, while the authority over business execution is substantially delegated from the board of directors to the management and executive side. Therefore, the status of dialogue with investors is not reported at every board meeting, but capital market concerns, the status of investor relations and analyst assessments are shared with the board as appropriate. The opinions of the capital markets are also used effectively in board discussions, **for example, when discussing business plans and performance forecasts, independent directors ask how the capital markets view them**.

Opinions Voiced in Interviews with Companies (Details)

Initiatives to ensure increased Corporate Value

Management with an Awareness of Profit-making and Growth; Acceptance of TSE Requests

- With limited resources, we are trying to **tackle** requests, etc., from the TSE **head-on and implement them in an honest manner**. We are promoting reforms in areas of the company that are not being done, using requests, etc., as leverage. The disclosed PBR improvement plan includes clear figures for ROE, DOE, net cash allocation, etc. It is no exaggeration to say that these figures were developed through dialogue at IR/SR meetings. Regarding the level of specific numbers, it is possible to ascertain through dialogue what level will satisfy investors, so these were **set through a series of related dialogues**, such as for ROE, we expect at least 8 percent, and in the future 10 percent, and so on. This is an example of how what was gained from the dialogue was **directly applied to the formulation of strategies and plans**.
- The impetus for the PBR improvement plan came from an overseas institutional investor who attended the previous year's general shareholders meeting and directly asked, "TSE has requested it, but when will your company disclose it? As an investor, I cannot make a correct voting decision without such disclosure." We were aware that we needed to do it, of course, but this question prompted us to set targets and make specific moves, leading to the disclosure. Since the **question was asked at a general shareholders' meeting**, all board members, including independent directors, were on stage to hear it, so the mindset was that they all had to do it. As a result, subsequent internal coordination was easy.
- The Company has not yet exceeded a PBR of 1. Although PBR is low on an industry level, it doesn't mean that we can have a low PBR just because other companies do, so we need to improve it. We are also aware of the trend of TSE and government initiatives, as well as trends around the world, and feel that there is a trend toward adopting a Western-style approach, such as the way in which independent directors should be appointed. This is a **natural trend** given that a significant portion of stock trading is conducted by overseas parties. If we know the direction we are going in, **it is better to do it from the beginning, as it will be appreciated by the market**, and we are working on it.
- The TSE's request for management to be aware of the cost of capital is excellent, and the rising share price is a result of this. The question of cost-of-capital conscious management is often asked both in the dialogue before the general meeting of shareholders and in the dialogue on ESG themes, and the general manager of the Finance and Accounting Department accompanies us to explain the issue. **I feel that management with an awareness of the cost of capital has not yet fully permeated Japan.** In terms of our company, we invest more than 100 billion yen a year in capital expenditure and our management is rather focused on PL, but we have received opinions from investors that **we should shift to a more BS-focused management**, and we are in the process of studying this. This point has been sternly pointed out by the external directors, although the stock price has been on an upward trend for the past few years and performance has not been poor, so investors have not been that severely critical.
- One of the things we have yet to do is to "take action to realize management that is conscious of the cost of capital and stock price," and overseas investors are asking us to do so. **The recent rise in stock prices is probably due in part to expectations of how far Japanese companies are willing to go in improving governance.** The Company has not reached disclosure and is in a subordinated situation. Discussion will begin at the March board meeting and will be disclosed in the integrated report by July or August. The numbers themselves are calculated and shared internally, but need to be consistent with the investor's measurement methodology.

Opinions Voiced in Interviews with Companies (Details)

Initiatives to ensure increased corporate value

Management with an awareness of sustainability issues

(Human capital)

- The employee engagement score will be disclosed as a KPI in a document to be released in May or later this year. The survey is conducted globally and the score can be used as an indicator since it can be low or high depending on the branch.When collecting feedback from overseas offices, we see that some countries have lower response rates than others, so we have taken **steps such as creating questionnaires in multiple languages other than English**. This may also provide insight into the cause of the low response rate by enabling a comparison across different offices. Improving the response rate is another KPI.
- The Company has set ambitious goals for women's empowerment, including the ratio of women in management positions. **Since women are the main target customers of our business, the challenge is how to enhance the number of female managers and officers.** Female employees are asked to engage in dialogue with each other, and the opinions raised there are extracted and reflected in implementation. The company has branches throughout Japan and employees are often transferred to other locations. However, some employees have voiced that it is difficult for them to transfer after marriage. In response, the company has been creating a more comfortable working environment by establishing the "My Area" system, which allows employees to work only in the area of their choice without compromising employment conditions, and alternatively by offering greater benefits to employees who are willing to relocate to other regions.
- In developing a vision for human capital management, numerical targets have been set for individual disclosure items, but we have also been discussing what we should essentially be aiming for, rather than just tracking numerical data. From this perspective, we believe that **we must look at where the essential goals of so-called "global excellent companies" are set**. Regarding human capital management and the rate of male employees taking maternity leave, which is required to be disclosed, the directors and the executive team share the view that while the company's progress does not fall below the norm, the company has yet to reach a point where it can lead with a firm belief in its approach, and that accordingly, these areas need to be addressed.
- **There are opportunities to acquire foreign subsidiaries** that operate globally, and **such foreign subsidiaries may also be used as a reference**. The current discussion focuses on the need to organize concepts such as job-based employment. An analysis of overseas companies shows that each individual is oriented toward career advancement and that human resources tend to be attracted to career paths that enable them to achieve the same. Although no conclusion has been reached, we are considering the creation of a system in which individuals can strive to develop their careers, including opportunities such as transfers within the company.
- Regarding the disclosure of human capital, many investors first present what they are concerned about and then specifically ask for information, such as figures indicating employees' engagement and our approaches to women's empowerment, rather than merely demanding a range of disclosure. **They work with us and present what we should aim to achieve in the future,** rather than merely requesting us to disclose as much as possible.
- Since the business cannot run without the involvement of people and requires various types of jobs, human capital is emphasized as materiality. It is an easy story to tell, but we have not pursued how human capital is linked to increased corporate value as well as **how it shows up in business results. Since this cannot be achieved immediately, we will work on the matter patiently.**
- With regard to human capital management, the reality is that headquarters does not necessarily comprehend all the personnel information of group companies around the world. **Information related to human resources is difficult to consolidate because of strong local factors, such as each country's systems and industry customs.** We often hear from some investors that, if the company values diversity in its human resources, they want the company to disseminate such information more widely.

Opinions Voiced in Interviews with Companies (Details)

Initiatives to ensure increased corporate value

Management with an awareness of sustainability issues

(Sophistication in managing non-financial information)

- The company is working to strengthen its non-financial activities. In response to the comments received during discussions between the CFO and investors that non-financial activities would become more important in the future, we started to engage in non-financial activities relatively early and have spent several years testing the validity of the regression analysis models as a corporate project. **In the corporate management dashboard**, the company manages plans and results **by visualizing what financial and non-financial activities are linked to what financial indicators to improve corporate value**. At the beginning, we started the exercise as a hypothesis and are working to make it more sophisticated and advanced. Investors have pointed out that non-financial activities (CO_2 emissions, engagement, ratio of female managers, etc.) are not tied to executive compensation. We have been considering this issue. The disclosure system for non-financial activities has also been reviewed since last year. The Company has the Disclosure Committee, a subordinate body of the Management Committee, that used to review financial information for statutory disclosure documents. However, in response to the recent increase in requests for disclosure of non-financial information, the committee has been engaged in **strengthening and reviewing the disclosure of non-financial information**, by adding members from sustainability, human resources and intellectual property departments.
- Some investors raise in-depth questions from an integrity perspective about the numerical targets in the CO_2 reduction roadmap. However, more investors ask to **specifically indicate the investment amount and its returns with regard to the various options and their timing included in the roadmap for achieving the reduction targets**. While there are many uncertainties and we closely watch external trends, including regulations, we receive many requests to consider the paths to the goal and to **disclose the consideration process as much as possible**.
- While the company discloses its method toward net-zero emissions as environmental measures, it has not disclosed specific information about **financial impact**. There are many variable factors and we have not disclosed any figures that could be misleading. However, as the regulations for emissions will be specifically defined starting this year, this has become **the immediate challenge**.

(Resilience)

- The expression "resilience" was determined through discussions by the Sustainability Committee, based on meetings that included experts. The Sustainability Committee consists of all members of the Board, including outside members. In case of a problem, **one of our functions is to support customers in maintaining their supply chain**, since a trading company has helpful information. We focus on resilience because some people think a trading company would be worthless if it did not have such a support function.
- The company mentions resilience in its management policy. When the COVID-19 pandemic caused instability in business performance and the capital markets, we became aware that the company's **business diversity provides overall stability, which is its strength**. Resilience is important from a sustainability perspective as well and has been referred to in the management policy.
- **Building relationships with suppliers leads to business sustainability** and resilience in terms of procurement.

Contents

Outline of the Revised G20/OECD Principles of Corporate Governance

Background

- In light of changes in the economic and social environment associated with climate change and the COVID-19 shock, the OECD Corporate Governance Committee, chaired by Masato Kanda, Vice-Minister of Finance for International Affairs, has started to undertake a review of the G20/OECD Principles of Corporate Governance. In October 2021, the G20 Rome Summit approved the start of the review work for the Principles. In November 2022, the progress of the work was well received at the G20 Bali Summit. Following a public consultation (September-October 2022) and adoption by the Corporate Governance Committee, the revised Principles were adopted by the OECD Council at the Ministerial Level in June 2023, and endorsed at the G20 Finance Ministers and Central Bank Governors' Meeting in July 2023 and the G20 New Delhi Summit in September 2023.
- The Principles are the only international standards in the area of corporate governance that are endorsed by G20 Leaders and followed by 53 developed and developing countries around the world, including the G20 members and OECD countries. The Financial Stability Board and the World Bank also use them as an important standard in the financial sector when evaluating each country's regulatory framework for corporate governance.

Purpose of the Revision

✓ **Improved access to the stock market by companies**

The stock market is essential for companies to raise funds and allocate their capital efficiently. With the number of listed companies declining in recent years, the revision is to support the efforts of each jurisdiction to help improve access to capital for companies and provide investment opportunities for households, while promoting investor protection.

✓ **Corporate governance that contributes to the improvement of corporate sustainability and resilience**

Provides a corporate governance framework to help companies address the challenges of flexibly adapting business strategies to a changing environment and increasing business value over the long term, following the COVID-19 shock.

Main details of the revision

✓ **Sustainability**

As international disclosure standards on sustainability are being developed, the revised Principles add a new chapter, VI. Sustainability and resilience. New principles are added on disclosure and corporate governance frameworks.

✓ **Stewardship activities by institutional investors**

The amount of assets under management by institutional investors continues to increase, and they have become the largest shareholders of listed companies in a large number of countries. Indexed investments, especially by large institutional investors, are on the rise, but this investment strategy has relatively low incentives for engagement. The content of the Principles has been revised with regard to accountability and corporate engagement by institutional investors. Text regarding ESG assessment and data providers has been added.

Revision of the UK Codes

- The UK Financial Reporting Council (FRC) revised the UK Corporate Governance Code on January 22, 2024. This is a limited revision which addresses the important issue of internal controls in particular. The main revision to the content is to require explanation in the annual report of the method of reviewing risk management and the internal control framework and the results thereof.
- On February 27, 2024, the UK FRC announced that it had initiated a review of the UK Stewardship Code. A public consultation is scheduled to begin after the shareholders meeting season this summer and the revision will be implemented early next year.

Main revision to the content of Corporate Governance Code

- The following wording in blue font was added to Section 4, Provision 29, which sets forth internal controls.

29. The Board should monitor the company's risk management and internal control framework and, at least annually, carry out a review of its effectiveness. The monitoring and review should cover all material controls, including financial, operational, **reporting** and compliance controls. **The board should provide in the annual report:**

- **a description of how the board has monitored and reviewed the effectiveness of the framework;**
- **a declaration of effectiveness of the material controls as at the balance sheet date; and**
- **a description of any material controls which have not operated effectively as of the balance sheet date, the action taken, or proposed, to improve them and any action taken to address previously reported issues.**

Perspectives in the review of the Stewardship Code

- As part of the review process, the UK FRC announced that the review will focus on, amongst other topics, the extent to which the Code:
  - supports long term value creation through appropriate investor-issuer engagement that drives issuers' prospects and performance
  - creates reporting burdens on issuers as well as Code signatories and
  - has led to any unintended consequences, such as short-termism in targets and outlook for issuers.

(Source) Prepared by JFSA based on UK FRC "FRC Revises UK Corporate Governance Code" (January 22, 2024), UK FRC "Statement: FRC policy update - launch of the UK Stewardship Code 2020 review" (February 27, 2024)