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Who should be responsible for engagement in the era of passive investment?

In the world of investment management, the advantages of passive strategy are becoming clearer both in terms of investment costs and investment performance. As a result, on the investor side in the invest chain, there are concerns about a drop in motivation for engagement and a decline in the number of high-quality personnel required for this task.

While the advantageous aspects of passive management cannot be denied, at present passive managers are to some extent enjoying a free ride from those conducting engagement, and as a result of this trend, the investment chain as a whole could experience structural damage. If this happens, there is a risk that a weakening of engagement could also weaken corporate governance in the long term, and that this could impede sustainable increases in corporate value, and thereby also impede asset formation for Japanese citizens and the achievement of ESG objectives. This means that there is a risk of a decline in overall investment performance, and if that occurs, it could also result in passive managers suffering from a fallacy of composition.

How can this risk of loss of engagement functions be averted? I hope that there will be a debate on ways of ensuring the quality and quantity of personnel capable of performing high-quality engagement functions, including collective engagement, which can be said to be a function of public goods, and I hope that the results of this debate will be reflected in future revisions of the Stewardship Code.