Mizuho Custody Newsletter

April 2021 | Japan

Contents:

I. Market News

1. Companies promoted themselves to superior market at the TSE increased 20%

Among the companies listed on the Tokyo Stock Exchange ("TSE"), 36 companies "promoted" themselves to the 1st or 2nd Section from Mothers/JASDAQ which are for relatively new companies in FY2020, 20% up from the previous year, according to Nikkei Shimbun, Japan's leading financial daily. This was the first increase in two years. The rise was supported by a sharp recovery in stock prices and improved market conditions due to global monetary easing under the pandemic. Transition from Mothers market, which has a strong character of accepting growing companies, accounted for 90% of the whole move. Companies listed on Mothers market may switch their market to the 2nd Section in 10 years after their listing, but these cases were excluded as they are not voluntary.

In FY2020, the number of companies promoted themselves increased by 7 companies (24%) from 29 companies in FY2019, marking it the highest level in 2 years since FY2018 (52 companies), driven by the moderate economic expansion and stable market condition. On quarterly basis, from July to September, 11 companies switched upward, an increase of 3 companies (38%) from April to June, which has doubled compared to the same period last year. In the period from October to December, 10 companies moved up (11 companies in the same period last year) reaching double digits.

The Nikkei Stock Average plunged to JPY 16,500 level in mid-March, then rapidly recovered to around JPY 23,000 in mid-June, and gradually rose to around JPY 24,000 in autumn, approaching the level before coronavirus. Companies that had been preparing to apply for promotion, which usually takes 2 to 3 months to approval, decided to go forward, having seen the market condition getting better, and many companies were approved to go up in July to September or October to December.

Among the criteria for promotion, total market value is affected by stock prices, and in order to secure the number of shareholders required, it is common to do "off-floor distributions" where major shareholders sell their shares to an unspecified number of investors outside trading hours. Therefore, those companies prefer stable market condition.

Promoting themselves from Mothers market accounted for 89% of the entire "promotion" cases, going up from 46% in FY2018 year by year. Compared to the JASDAQ market, which has many mid-sized companies with long history, Mothers market's presence gets stronger as the market supports small and medium-sized companies with growth potential go up to a superior market by providing financing methods.

TSE will reorganize its market segments from current four segments to three in April 2022. Prior to this, the transfer criteria from Mothers market and the 2nd Section to the 1st Section was tightened in November 2020. Among the conditions, "total market value: JPY 4 billion or more" and "Net worth: JPY 1 billion or more" for the Mothers market and the 2nd Section were raised to "total market value: JPY 25 billion or more" and "Net worth: JPY 5 billion or more". This change is intended

to show clearly that the prime market as one for highly selected companies.

TSE announced the above change to begin from November 2020 in late July 2020. A senior researcher at a research institute said, "The announcement of the change prompted companies getting ready to apply for moving up to a superior market to take action by the end of October, which resulted in increase in the number of companies moved up to a superior market." An analyst of financial information service provider said, "It seems companies who are performing good enough to move from Mothers market to the 1st Section have been almost covered. From now on, less companies will apply for moving to an upper floor." With less than a year until the TSE's implementation of the new market segment, it is assumed that companies having potential for "promotion" may take "wait and see" approach to make sure how the implementation would affect the market and their business.

Information compiled from Nikkei Shimbun & Mizuho research

2. Strict eyes on the appointment of directors

Investors are monitoring corporate governance more closely than ever. At the AGM held in March for the companies with fiscal year ending in December 2020, many companies did not obtain high support from their shareholders on some proposals such as the appointment of outside directors due to their insufficient independency, reports Nikkei Shimbun, Japan's leading financial daily. Many AGMs are coming up in June for companies with their fiscal year ending in March, and they would have to deal with the similar issues.

At the AGM of a manufacturing company in March, about 73% of shareholders approved the company's proposal to reappoint an outside director who is from a shareholder of theirs, holding about 30% of their stake. In Japan, about 80-90% of shareholders used to approve company's proposals, partly based on cross-shareholding practice. However, thanks to the recent trend to unwind the cross-shareholding practice among many companies, approval rate of the proposals at many AGMs in March turned out to be less than 80%.

At the AGM of a service company, the approval rate for reappointment of an outside director who was the chairman of their largest shareholder was about 77%, about 3 points down from the previous year. It seems a major investment management company voted against the proposal, reflecting their policy to "scrutinize proposals of selecting outside directors whether candidates represent a major shareholder of the investee", as specified in their proxy voting standard.

Length of the tenure also drew strict attention. At the AGM of another service company, the proposal for reappointment of an auditor who has been with the company since 2000 got only 62% of the approval. A representative of a major asset management company said, "Many investors are looking more at independence of directors, and companies need to find right people very soon.

The Stewardship Code, action guidelines for institutional investors, requires investors to disclose their voting policies and the results of their votes by each proposals. Pension funds, who provides funds, are putting more weight on corporate governance, and financial institutions acting as their service providers also follow the trend by tightening up their proxy voting policies.

What efforts issuers would make for environment is also one of focal points for the AGMs in June. One of NGOs made shareholder proposals calling for development and disclosure of plans for decarbonization. An asset management company has been supporting in principle shareholder proposals seeking for disclosure on climate risks since this April.

In addition to corporate governance, investors are having stricter views on environmental measures. AGMs are no longer held for the sake of formality to win near-unanimous supports from shareholders. Now it is a place for management of issuers to be checked and monitored by their shareholders.

Information compiled from Nikkei Shimbun & Mizuho research

3. Survey with pension funds shows strong interest in ESG strategy

There is a growing momentum among Japanese corporate pension funds to invest in ESG strategy. Nikkei Shimbun, Japan's leading financial daily, has

conducted a survey with 104 leading pension funds, and 71% of the funds adopted or considering ESG strategy for their defined benefit pension plans. As more companies adopt this strategy, pension funds are increasing their ESG investment to ensure long-term stable investment.

The survey was conducted from January to February, asking respondents about how they review investment products, system changes, governance, etc. 120 companies were selected from ones with large market capitalization and by industry type. 104 of them, accounting for 87 percent of the ones selected, replied to the questionnaire.

In the past, companies' primary interest was how they could review the pension system to lessen their burden on pension payments. However, this time, many of them showed a strong interest in ESG strategy. The background is that Government Pension Investment Fund (GPIF) has expanded its ESG investment and been performing well.

According to the survey, 80 pension funds maintain defined benefit pension plans. 33% of them were willing to adopt ESG strategy. 39% of them already have ESG strategy in place. As for the reasons of their adoption of ESG strategy (allowing multiple answers), 61% of the funds answered "ESG would help making long term stable investment". This was followed by 44% of the funds answering "the company is giving more weight on ESG."

Partly due to volatile market in the wake of the global pandemic, 48% of defined benefit pension plans surveyed said they were either reviewing or considering to review investment portfolio (asset allocation).

According to the survey, 80% of defined benefit pension plans employ alternative investment. The scale of the alternative investment was small immediately after the global financial crisis, but it has expanded to the level of foreign bonds (94%) due to low interest rates. Among the alternative investment, real estates have been selected because of their high return. Over the past year, pension funds that needs to review their investment policies for defined benefit pension plans are getting more attentive and react quicker to market fluctuations than before.

Only 6% of defined benefit pension plans replied that they would lower or consider lowering the expected rate of return. A bank that has cooperated to the survey pointed out "For the past 10 years, many funds chose to review their portfolio because of losses caused by the global financial crisis. This movement drastically lessened the number of funds suffering from bad investment performance.

Information compiled from Nikkei Shimbun & Mizuho research

4. Proposed amendment on Corporate Governance Code calls for climate risk disclosure

Financial Services Agency ("FSA") and Tokyo Stock Exchange ("TSE") presented a proposed amendment to the Corporate Governance Code ("Code") for listed companies at the council of experts held on March 31. At the council, the new Code was agreed in principle. According to Nikkei Shimbun, Japan's leading financial daily, TSE plans to enforce it in June after receiving public comments.

In an effort to attract investment from overseas institutional investors, in particular, the new Code will require disclosure on climate change risks and enhancement of the board of directors to the companies to be listed on the Prime Market, which will take over the current 1st Section of the TSE according to the planned market realignment in April 2022. Companies will have to analyze and disclose risks for their businesses by climate change, and countermeasures for it, in order to attract funds from the market by demonstrating their active posture toward a decarbonized society. The new Code also will require at least one third of the board of directors of a listed company on the Prime Market are independent external personnel. It is likely that the companies will take actions from fiscal year 2022 based on the new Code.

With regard to information on climate change, companies will be required to disclose in line with the recommendations of the Task Force on Climate-related Financial Disclosures (TCFD) established by the Financial Stability Board (FSB). Risk analysis on the scenario of global warming and how they deal with the risks being in line with their business strategy shall be communicated to investors in clear and concise

manner. Environmental measures, including accountability to investors, will be the name of the game for corporate management.

For details on the revised draft of the Code asking for public comments, please visit the release from TSE at their website:
https://www.jpx.co.jp//english/rules-participants/public-comment/detail/d01/e20210407-01.html

Information compiled from Financial Services Agency, Nikkei Shimbun, Tokyo Stock Exchange & Mizuho research

II. New Equities Listing Approvals

Listing Date	Name of Company	ISIN Code	MKT
	(None)		

**Information compiled based on postings from the TSE (T), Mothers (M), NSE (N)、FSE (F), SSE (S) & JASDAQ (J), Tokyo Pro Market (P)*

***Board lot size is unified to 100*

III. Foreign Ownership Limit Ratio

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