Mizuho Custody Newsletter

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I. Market News

1. Making entry easier for Investment firms

The Tokyo Metropolitan Government and the Financial Services Agency (FSA) have advocated making Tokyo as a "Global Financial City" and have been approaching asset management companies to do business in the city. The number of asset management companies has jumped up by approximately 60 from five years ago, reaching a total of 417. However, during the same period, Singapore went far ahead of Tokyo and had a total of 1,194 companies, up by 70%. Singapore played a role of "safe heaven" for companies relocating their base from Hong Kong out of concern due to political unrest. Tokyo cannot sit back and watch.

To turn around this situation, the government of Japan is taking various actions. The FSA is now promoting de-regulations for emerging and overseas investment firms to make easy entry to the industry. Currently, a company must have both investment department and asset administration department, but the new rules will allow companies without an asset administration department to enter the market. Additionally, FSA is also planning to introduce a new framework to ensure newly established investment firms to obtain seed money from institutional investors at their launch of business, in order to encourage more asset managers with unique feature and/or products even if they are small-sized. Through these efforts, the government aims to diversity investment objectives and provide more options for investors.

A manager of an asset management company operating in Japan says, "In terms of taxation, it is true that Singapore and Hong Kong are certainly attractive. However, taxation should be just one piece of items for making decisions on where to have an office. It is important to look more at actual economic situation in Japan first hand when investing in Japan. I think inexpensive living costs, such as rent and prices, is one of great advantages of having a business base in Japan.

The government aims to expand the base of asset managers. There have been complaints about burden of maintaining asset administration section in house, which has been keeping new entrants away.

Following discussions at the Financial System Council, FSA aims to submit a proposal to amend the Investment Trust Act in the regular session of the National Diet in 2024. In order to encourage new entries of firms specialized in investment to the industry, the amended act would allow companies specialized in managing investment trusts' assets to operate in the market.

In order to make entry easier for investment firms, the government will also review the "dual-calculation" practice of investment trust NAV, which is a unique practice in Japan. Both, investment firms and trustees have been responsible for independent calculation and reconciliation of NAVs. This practice started as an industry norm to ensure accuracy of calculations. At that time, there was a high risk of errors as everything was processed manually, but now it is completely computerized. This practice forces investment companies to bear significant costs for maintenance of the system. It is believed that an asset management company has to have over 100 billion yen AUC to survive in the investment trust business in Japan, which has made many entrants shy away from doing this business in Japan.

It is said that one reason foreign investment companies hesitate to enter the Japanese market is because Japanese investors are more demanding than Western investors, such as frequency of investment reports, etc. While Western investors thoroughly research investment companies in the selection process, they usually require only regular reports once they selected the investment managers. On the other hand, Japanese investors demand immediate updates whatever happens in the market. The representative of an asset management company believes that many Japanese investors want perfect services from their providers, which appear to be invisible costs. The person also says, “I hope that frameworks that facilitate long-term investments in Japan, which could eventually affect investors’ mindset to be more receptive to long-term investments.

Asset management business covers a wide range of activities, including calculating NAV of investment trust funds, calculating investment performance, and ensuring compliance with regulations. Investment firms will leave these roles to asset administration companies, so that they could focus on investment activities and improve efficiency. The FSA assumes that if asset administrators undertake all these roles, it will accelerate small-sized investment firms to enter the market. The FSA is planning to monitor and supervise operations of asset administration companies to ensure their service quality.

According to the FSA’s research for foreign asset managers about what makes them reluctant to enter into Japan, many of them replied difficulties in securing experts in specific fields such as compliance. For small-sized investment firms, labor costs is not a small burden. If they could concentrate on their unique investment strategy, such as utilizing derivatives to expand its investment performance or specializing in non-listed stocks, investors will have more investment options, which would make Japan market more attractive.

On another subject, Japanese institutional investors are strongly reluctant to incorporate lock-up periods (a specified period of redemption restriction) in the agreement, making it difficult to promote long-term investment in the market. A local asset management company has been trying to incorporate 3-5 year lock-up period in agreement with clients on its view that long term perspective is essential for managing companies. However, investors fiercely resisted to their approaches, as the investors were very sensitive to the liquidity of their assets. This is in contrast to US university endowments, who do not regard 3-5 years as long-term investment. The asset managers with diverse investment strategies come up more in the market would affect local investors’ mindset and behavior.

In overseas markets, separation of investment and asset administration has been ongoing. In Europe, companies specialized in fund administration act as the main operators of investment trusts. They outsource investment management as well as distribution and clerical works.

FSA is also considering to introduce a new framework to contribute funds for newly established asset management firms. Pension funds and other similar entities tend to look at how well they did in the past, and to shy away from selecting new entrants due to the lack of past records. Individuals who have brushed up their skills as fund managers, longing for standing on their own are strong candidates for the new framework. Government-affiliated funds, public pensions, and private financial institutions are expected to participate as contributors. More details will be available from now on.

In Japan, asset management companies of major financial groups claim significant market share, which have been concerned to lead these providers to put the interests of affiliated sales companies before client benefits. FSA believes that of the more independent investment companies enter the market, the more intense competitions would be.

The total asset under management (AUM) in Japan’s asset management industry is approximately 800 trillion yen (circa USD 5,340 billion), which is about 1.4 times of the country’s Gross Domestic Product (GDP). In comparison, the United States has AUM of 50 trillion dollars (approximately 7,500 trillion yen), which is more than double of its GDP, and the United Kingdom has AUM of 13.5 trillion dollars, which is more than four times of its GDP. The government has just begun to reform the industry, clearly being aware of the importance of building a fortune.

Compiled from Nikkei Shimbun and Mizuho research.

2. ESG Bond issuance was record-high (April to September 2023)

Bonds to finance ESG (Environmental, Social, and Corporate Governance) related investments have been issued more often by more issuers. In the period from April to September 2023, some leading companies in real estate and telecommunication industry announced issuances, resulting in an increase by 50% in comparison with the same period last year, which made the record-high. The global uptrend for de-carbonization and government's support continue to drive investors to these instruments. Despite some market experts' outlook of interest rates to go higher, companies are still eager to issue "ESG bonds" as they can save fundraising costs.

ESG bonds are defined as "green bonds", which limit the usages of proceeds raised in the issuance to environmentally conscious projects, and "social bonds", which require the funds raised to be used to deal with social issues. According to a study by a local securities company, the issuance of ESG bonds amounted to JPY 1.75 trillion (circa USD 11.6 billion), already reaching 80% of the total amount issued in the fiscal year of 2022. The growth rate of ESG bonds issuance surpassed that of the overall bond issuance (which increased by 37% to JPY 7.87 trillion, circa USD 53.5 billion) within the same period (April to September 2023).

The global issuance of green bonds has grown to approximately USD 500 billion on annual basis at present since the adoption of the Paris Agreement, an international agreement on climate change in 2016, when the total issuance of ESG bonds was just USD 85 billion. The ESG bonds market, with a size of approximately USD 2 trillion, now surpasses the US high-yield bond market in scale. In the Japanese bond market, the total issued amount of green bonds exceeded JPY 2.5 trillion (circa USD 16.7 billion), and last year, a fishing and food company launched the first "blue bonds" in the country, which limit the usage of funds raised through its issuance for projects that are friendly for marine resources and environments.

The amount of green bonds issued from April to September 2023 has already reached JPY 951.2 billion (circa USD 6.3 billion), well exceeding last year's record of JPY 702.9 billion (circa USD 4.7 billion). A leading telecommunication company's financial and credit services subsidiary decided to issue bonds amounting to JPY 380 billion (circa USD 2.5 billion), which was the largest single deal among this year's issuances for institutional investors, excluding subordinated bonds. Funds raised through the case will be invested to the company's 5G initiatives and renewable energy projects.

A leading real estate company is going to issue green bonds in the amount of JPY 230 billion (circa USD 1.5 billion). The issuance aims to refinance a portion of the interest-bearing debts incurred for developing new buildings in the central business district in Tokyo. These buildings have obtained certifications for their environmentally conscious initiatives. The developer plans to supply electric powers to the tenants with document that certificates the powers were not from fossil fuels.

Sustainability-Linked Bonds (SLB) have also been issued more. SLBs does not restrict ways funds are used, and their interest rates may vary depending on whether the issuer achieved the goal set at the launch of the issue, such as greenhouse gas emission reduction. The issuance amount increased by 27% to JPY 355.2 billion (circa USD 2.4 billion) from April to September 2023.

ESG bonds are expected to increase by approximately 40% from the fiscal year 2022 to around JPY 3 trillion (circa USD 20 billion) for the entire fiscal year of 2023. In October, a leading construction company announced the issuance of environmental bonds in JPY 10 billion (circa USD 66.7 million).

Demands for ESG bonds are strong. While interest rate may be less attractive, ESG bonds are useful for investors who wants to demonstrate their commitment to de-carbonization, which may allure "ESG funds" from the market. Among the downtrend of investments in fossil fuel sector gets stronger, "investors such as financial institutions began to show strong interest in ESG bonds as an alternative investment option." says a director at a local securities company.

The government also advocates the trend. Prime

Minister Fumio Kishida has declared the GX (Green Transformation) strategy as one of the pillars of economic policies of his administration. The Bank of Japan (BOJ) has also implemented measures to provide financial institutions with favorable lending conditions to encourage the private sector to tackle climate changes further more.

However, issuance might slowdown in the second half of the year. Corporate bond yields are determined by adding a certain spread to government bond yields. BOJ announced on October 31 to further increase the flexibility in its yield curve control (YCC). Previously, 10 year JGB rates were strictly controlled to be under 1% but BOJ announced to soften this hard limit. If the low-interest-rate policy were to be phased out, the outlook would become more unclear, and that might weaken investor demand. In fact, some companies has already postponed their bond issuances.

There are some challenges to further revitalizing the ESG bond market. Unlike ordinary corporate bonds, ESG bonds have obligations to disclose emission reduction progress even after the issuance. “Greenwashing” is also a concern, where issuers disguise taking environmental measures that would not bring actual improvements. According to a senior strategist at a local security company, there are cases where complexity of the technology applied makes it difficult to determine whether it actually helps to de-carbonization. Therefore, it is essential to establish frameworks in which companies could present how effective their investments are in clear and simple manner.

Compiled from Nikkei Shimbun and Mizuho research.

3. Segment revenue and cash flow information becomes mandatory disclosure

There are currently two types of quarterly disclosure requirements for listed companies in Japan. One is required by the Financial Instruments and Exchange Act (“Shihanki-Houkokusho”), and the other is the quarterly earnings reports required by the Tokyo Stock Exchange (TSE) rules (“Kessan-Tanshin”). With regard to these two disclosure reports, companies have been suffering from heavy workload and inefficiency in getting these two reports ready, due to many overlapping items to be disclosed and timing of issuance being very close.

On November 16, the amendment of the Financial Instruments and Exchange Act to integrate the quarterly securities reports (“Shihanki-Houkokusho”) into the quarterly earnings reports (“Kessan-Tanshin”) was approved at the Lower House plenary session. The amendment is likely to come into effect from April 2024, and the “Shihanki-Houkokusho” for the first and third quarters will be abolished and consolidated into the “Kessan-Tanshin”.

TSE is requesting listed companies to enhance the content of their quarterly earnings reports (“Kessan-Tanshin”) in line with this amendment. They are now obligated to disclose information regarding revenue by business segment and cash flow, which were previously included in quarterly securities reports (“Shihanki-Houkokusho”) but not in “Kessan-Tanshin”. The integration into “Kessan-Tanshin” aims to reduce the burden on companies while ensuring disclosure level not to regress.

The new disclosure system is scheduled to be implemented from the first quarter (April to June, 2024) for companies with fiscal year ending in March, and from the third quarter (October 2023 to June 2024) for companies with fiscal year ending in September.

Under the new rules, the disclosure of information regarding sales and profits by segments must be indicated as footnotes in the quarterly earnings reports (“Kessan-Tanshin”). Companies have discretion to decide the segmentation of their businesses, such as consumer-oriented or enterprise-oriented. If a company would not include a cash flow statement in the “Kessan-Tanshin”, it would be obligated to include information related to cash flow, such as depreciation expenses and amortization of goodwill in the footnote.

Companies have been disclosing all of the above mentioned information in their quarterly and semi-annual securities reports, as well as its annual securities reports. However, it was not mandatory to disclose this information in the earnings reports, “Kessan-Tanshin”. The TSE sees the transition will cause no additional burden on companies, since it is just a switch of the media by the abolishment of the quarterly securities reports (“Shihanki-Houkokusho”). Rather, investors are very keen on obtaining segment information and cash flow, so TSE requires issuers to incorporate these information to ensure the disclosure level does not regress.

Under the new disclosure rules, the “review (opinion)” issued by an audit firm to ensure the accuracy of a company’s earnings report for the first and third quarters will become optional. The audit firm’s opinions were used to be attached to quarterly securities reports, but now the regulators put “timeliness” before accuracy of the reports.

Having said that, TSE will make it mandatory to acquire audit firm reviews for companies that had committed accounting fraud or had significant governance deficiencies. This is aimed to alleviate investors’ concerns that detection of irregularities might delay by having auditor’s review less often.

The revision of quarterly disclosures was positioned as the core policy by Prime Minister Fumio Kishida. TSE has been discussing the practical aspects by setting up a committee since June 2023, based on the reports compiled by FSA’s Financial System Council.

As for quarterly disclosures, an opinion to make quarterly disclosures to be at issuers’ discretion is now coming up. However, the FSA’s Financial System Council has expressed concerns that the idea was so generous that it could be perceived as a regression in disclosure and could decline the overall confidence of the Japanese market. As a result, the council has stated its policy to make quarterly disclosures mandatory for now. This policy will be included in the report to be compiled by the committee of the TSE sometime soon.

FSA emphasized the importance of establishing a market environment where issuers actively provide investors with comprehensive information with appropriate mindsets to disclosure, as a prerequisite for making it optional. It also stressed that companies have been facing challenges of how they could enhance disclosure within the framework of timely disclosure of the TSE, by acquiring knowledge of appropriate risk assessment, in particular on unforeseen events or incidents such as the global pandemic.

Under the circumstance, not a small number of Japanese companies still do not seem to be willing to enhance timely disclosure. In February 2020, TSE requested companies to proactively disclose risk information in the midst of the global pandemic. However, only a few companies made timely disclosures regarding revisions of performance forecasts before official announcement of their financial results. Similarly, after Russia’s invasion of Ukraine broke out, very small number of companies disclosed risk information on this subject.

In parallel with the revision of quarterly disclosure requirements, TSE urges companies to promptly disclose information regarding impacts if there were any changes in their business environment. The TSE lists up the following items as samples; impacts on their performance and finances, an overview of the scenarios on which companies make up their performance forecasts, and the scope of businesses to be affected by the changes.

TSE is striving to make the market more visible and flexible for investors to attract a wide range of investment funds from both domestic and international sources. At the end of March 2023, TSE requested the companies listed on the Prime and Standard markets to take measures to make their management to be more conscious of capital costs and stock prices. With regard to the revision of quarterly disclosures, TSE has been taking very careful approach to ensure that the revision would not result in deterioration of disclosure level, to keep investors interested in Japanese stocks.

Compiled from Nikkei Shimbun, and Mizuho research.

4. Requirements for Prime listed companies gets more rigorous

Since the implementation of new market segments at the Tokyo Stock Exchange (TSE) in April 2022, TSE held a total of 12 follow-up meetings regarding the market segmentation review. In the latest follow-up meeting held on October 11, TSE discussed the following 2 issues as the main subjects: (1) How to achieve management conscious of capital costs and stock prices (“management conscious of capital costs, etc.”) and “promoting dialogue with shareholders”, (2) More disclosures in English from the Prime Market listed companies.

Regarding the issue (1), TSE announced the “Public

Release of the List of Disclosing Companies Concerning Efforts towards Achieving Management Conscious of Capital Costs and Stock Prices" on October 26. Since the market restructuring, TSE has been requesting Prime Market-listed companies to promote dialogue with shareholders and appropriate disclosure. The Prime Market is positioned as a market where companies focus on enhancing corporate value through constructive engagements with global investors. Being clearly aware of the importance of sincere responses to requests for dialogues from shareholders, TSE has been requesting companies to establish structures to facilitate such communication. From January 2024, the TSE will disclose and regularly update the list of companies that disclose their efforts towards achieving management conscious of capital costs, etc.

According to a survey by TSE, as of mid-July 2023, 379 companies listed on the Prime Market, have been disclosing their efforts on the above-mentioned subjects, which accounts for 31% of the total companies listed on the market. To analyze the breakdown, TSE took statistics on "the disclosure status" and "each company's Price-to-Book Ratio (PBR) and market capitalization". It revealed that 45% of the Prime Market listed companies with a PBR of less than 1 and with market capitalization of JPY 100 billion (circa USD 660 million) or more make the disclosures. On the other hand, it also turned out that companies with high PBRs or with small market capitalizations have been less positive to the disclosures than the above group, accounting for 45%. Some domestic and international investors took the outcome that some companies misunderstood that they would not have to deal with the TSE's requests if the PBR exceeds 1. The TSE expects companies to make further efforts for improvement, taking the following matters into consideration, such as shareholders' and investors' expectations, comparisons with domestic and international competitors, indicators that reflect capital profitability and market valuation other than PBR. The TSE aims that the publication of the list would facilitate investors to find companies that are positive with the disclosures requirement, which may support the companies' efforts and urge other companies to take actions.

The list will be published in both Japanese and English on the TSE website from January 15, 2024, and the status as of each month end will be updated by 15th of the following month. The initial publication will be based on the status of Corporate Governance Reports (CG reports) as of the end of December 2023.

Regarding the issue (2), in-depth discussions began at this follow-up meeting. TSE has expressed its intention to make disclosure of necessary information in English mandatory at the time of conclusion of transitional measures. However, TSE has not clearly mentioned specific documents and a clear timeline regarding English disclosure. Many members of the meeting opined that the mandatory English disclosure should be scheduled in phases. Some attendants referred to the situation in Taiwan and South Korea, where disclosure requirements are enforced in phases, based on company size, and opined that it was appropriate to introduce mandatory English disclosure in phases from March 2025 to coincide with transitional measures conclusion. Considering that the shareholding ratio of foreign corporations in the Prime Market was 30.8% as of the end of fiscal year 2022, some attendees suggested that companies with foreign investor ownership ratios over 30% should prioritize English disclosure based on the figure as of the end of FY 2022 as a guideline. In addition, another member expressed a view that companies that are constituents of indices such as TOPIX 500 and JPX Prime 150, generally recognized benchmarks by foreign investors, should be firstly obligated to information disclosure in unified style and with appropriate level of details and quality, so that companies listed on other markets could follow suit, which may impress foreign investors and eventually help raise reputation of Japan's stock market as a whole.

Regarding what disclosure documents should be issued in English, the members' opinions were divided, and they did not reach to a unified consensus this time. Some members commented that materials deemed as "disclosure essential", such as financial summary, IR presentation materials, timely disclosure materials, and securities reports, should be prioritized and made mandatory. While securities reports are highly comprehensive compared to other documents, they contain a lot of items to be translated. In terms of efficiency and practicality, items that overseas investors are likely to be interested should be translated and reported first. On the contrary, other members stated that it takes tremendous resources for issuers to translate the whole parts of securities reports, while investors do not look at the report so much often as generally thought. In addition to these comments, some say that the TSE should obligate issuers to provide at least a summary of financial statements and timely disclosure in English. Others say that it is extremely disappointing that investors' needs toward timely disclosure materials and the efforts of companies to improve those documents do not match. These people believe that statutory disclosure documents such as timely disclosure materials, financial statements, and securities reports should form the basis of disclosure materials to be translated into English. Great many members suggested that it is desirable to distribute Japanese and English materials at the same time.

The concept of the Prime Market set by TSE consists of three core factors: (a) Market capitalization (liquidity) that can attract a large number of institutional investors, (b) Higher governance standards, and (c) Constructive dialogue with global investors. The series of requirements stated here seem to be in line with these concepts. To be listed on the Prime Market, an applicant company must meet these concepts. Therefore, companies aiming to be listed on the Prime Market should make every effort to fulfil the aforementioned requirements.

Compiled from Nikkei Shimbun, and Mizuho research.

II. New Equities Listing Approvals

Listing Date	Name of Company	ISIN Code	MKT
Nov-10	Kyobashi Art Residence Co., Ltd.	JP3253520005	P
Nov-16	Japan Eyewear Holdings Co., Ltd.	JP3389460001	S
Nov-22	VALUE CREATION CO., LTD.	JP3778520001	G
Nov-22	KET Inc.	JP3277030007	P
Nov-27	MY FARM, INC.	JP3860370000	P
Nov-29	AlbaLink Co., Ltd.	JP3126270002	P
Nov-30	M.D.B. Corporation	JP3167390008	P
Dec-04	ASMARQ Co., Ltd.	JP3119870008	S
Dec-06	Institute for Q-shu Pioneers of Space, Inc.	JP3244850008	G
Dec-08	WizBiz Inc.	JP3154130003	P
Dec-12	OutlookConsulting Co., Ltd.	JP3105380004	G
Dec-13	OFFICEBUSTERS CORPORATION	JP3197670007	P
Dec-13	Yottavias Co., Ltd.	JP3958800009	P
Dec-15	Kairikiya Co., Ltd.	JP3205680006	S
Dec-15	S&J Corporation	JP3161700004	G
Dec-18	Ame Kaze Taiyo, Inc.	JP3124690003	G
Dec-12 -Dec-18	Blue innovation Co., Ltd.	JP3831080001	G
Dec-19	WiLLDo Inc.	JP3154230001	P
Dec-19	ES-NETWORKS CO., LTD.	JP3163380003	G
Dec-20	Nyle Inc.	JP3641360007	G
Dec-21	MRSO., Inc	JP3860180003	G
Dec-22	Human Technologies, Inc.	JP3794460000	G
Dec-22	SPO Entertainment Inc.	JP3163700002	P
Dec-25	Nalnet Communications Inc.	JP3651950002	G
Dec-20 -Dec-26	Rococo Co. Ltd.	JP3984090005	S
Dec-27	yutori, Inc.	JP3949300002	G
Dec-22 -Dec-28	WASEDA GAKUSHUKENKYUKAI CO., LTD.	JP3993770001	S

**Information compiled based on postings from the Prime (PR), Standard (ST), Growth (G), Tokyo Pro Market (P), NSE (N)、FSE (F) & SSE (S).*

***Board lot size is unified to 100*

III. Foreign Ownership Limit Ratio

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