Sustainable Investing in Japan: An Agenda for Action

TIIP THE INVESTMENT INTEGRATION PROJECT

SASAKAWA PEACE FOUNDATION

Prepared by:
The Investment Integration Project (TIIP)

With support from:
The Sasakawa Peace Foundation

September 2019

Executive Summary

More than a quarter of assets under management (AUM) worldwide are invested in "sustainable" strategies, strategies that consider environmental, social, and governance (ESG) factors in pursuit of financial sustainability and/or environmental or social sustainability. Investors – both individual and institutional and at all wealth levels – are increasingly interested in integrating these strategies into their financial plans and investment portfolios, and asset managers and global financial institutions are embracing the approach and expanding related services and product offerings.

Interest in sustainable investing and sustainably invested AUM are growing rapidly in Japan. But despite this enthusiasm and growth, few mainstream investors, financial advisors, and investment consultants in Japan are embracing the practice.

We - The Investment Integration Project (TIIP) - partnered with The Sasakawa Peace Foundation (SPF) to examine why some investors and others in Japan's financial community do not incorporate sustainable investing into their practices, and to recommend breakthroughs needed to grow the practice in Japan. We also preliminarily identified barriers and opportunities for sustainable investing elsewhere in Asia (Singapore, Hong Kong, and China). To fulfill these objectives, we reviewed relevant literature on sustainable investing in Japan and consulted with more than 50 experts on Japan's financial industry.

We identified the following as the primary barriers to the widespread adoption of sustainable investing in Japan:

- **Visibility:** the Japanese financial community remains generally unaware of sustainable investing;
- **Evidence:** myths about sustainable investing are pervasive in Japan;
- **Tools:** there is a shortage of practical resources for the Japanese financial community that instruct on how to integrate sustainable investing into investment practices; and
- **Policy:** government and regulatory agency efforts to support sustainable investing are fragmented.

There are a series of practical steps that Japan's financial community can take to start to address each of these challenges, which we list in Table 1 below and detail in the "Recommendations for Action" section of this *Agenda*. In taking these steps, Japan, with the third-largest economy in the world, can begin to capitalize on increasing momentum for sustainable investing and, in doing so, help investors to promote social, environmental, and financial sustainability.

Table 1. Recommendations for addressing barriers to sustainable investing in Japan

VISIBILITY
- → Mobilize industry influencers (individuals and organizations) to publicly support sustainable investing.
- → Use social and other media to engage retail investors on sustainable investing.

EVIDENCE
- → Dispel myths about sustainable investing.
- → Connect investors to information about the what, why, who, and how of sustainable investing.

TOOLS
- → Provide investors with practical guidance for integrating sustainable investing into their practices.
- → Connect investors to capacity building opportunities (e.g. industry forums and sustainable investing workshops).
- → Establish a sustainable investing knowledge hub for Japan.

POLICY
- → Coordinate efforts by cabinet-level government agencies to support sustainable investing.
- → Embrace "soft law" approaches to guide investors in their implementation of sustainable investing-related regulations.

Introduction

More than a quarter of assets under management (AUM) worldwide are invested in “sustainable” strategies.[1]

Investors are embracing these strategies to protect and enhance the value of their investments and the health of the environmental and social systems that make profitable investment possible. They are:

- Avoiding investments with poor ESG performance (e.g. negative exclusionary screening);
- Emphasizing investments with positive ESG practices or that solve environmental and social challenges (e.g. best-in-class or impact investing); and
- Engaging with funds and companies to encourage ESG improvements and ESG risk mitigation (e.g. active ownership).

Evidence increasingly suggests that certain sustainable investing approaches can enhance financial performance, and that investors of all kinds – men and women, old and young, and at all wealth levels – are interested in incorporating sustainable investing approaches into their portfolios.[2]

Sustainable investment in Japan

Sustainable investment is growing rapidly in Japan. Sustainably invested AUM grew a staggering 300% between 2016 and 2018, from almost ¥57 trillion to nearly ¥232 trillion.[3]

Although this documented growth might be partly due to increased reporting, the Japanese government, businesses, and investors alike have launched or participated in a series of initiatives in recent years that have promoted the practice (see Box 1).[4]

Despite these important developments, sustainable investment appears to appeal solely to niche, boutique, and explicitly long-term investors (e.g. pension funds) in Japan and has not otherwise gained traction with the mainstream financial community.[5]

In short: sustainable investing is growing rapidly in Japan, but the mainstream financial community has yet to embrace the approach.

The Agenda for Action project

With support from The Sasakawa Peace Foundation (SPF), we - The Investment Integration Project (TIIP) - set out to understand the disconnect between the growth of sustainable investing in Japan and its uptake by mainstream investors, and to develop a plan - an *Agenda for Action* - that recommends breakthroughs needed to grow the approach.

Within this broad purpose, we:

- Identified the challenges and opportunities for sustainable investing in Japan;
- Identified sustainable investing resources available to asset owners in Japan and assessed their strengths and shortcomings;
- Examined sustainable investing resources that have been developed for asset owners in North America, Europe, or elsewhere that might be usefully adapted for Japan’s investors; and
- Determined what new resources are needed to support asset owners in Japan in their pursuit of sustainable investing.

Our efforts focused on asset owners in Japan, but we also considered the needs of Japan’s asset managers, financial advisors, and consultants and preliminarily assessed the needs of financial industry professionals elsewhere in Asia (Singapore, Hong Kong, and China).

To fulfill the project’s objectives, we reviewed the literature on sustainable investing in Japan and consulted with more than 50 industry experts who are supporting investors’ embrace of sustainable investing and working to bring it into the mainstream (see Attachment A).

Roadmap to the Agenda

In the sections that follow, we summarize the next steps needed to advance sustainable investing in Japan ("Recommendations for Action"), preliminarily explore how similar recommendations might be developed for other areas within Asia ("Implications for the Region") and provide closing thoughts on how Japan can work toward being a world leader in sustainable investing ("Conclusions").

Box 1. The growth of sustainable investing in Japan

Among the main factors driving the growth of sustainable investing in Japan are:

1. **The Japanese government thinks that it is important to integrate sustainable investment into finance.** The Ministry of Economy Trade and Industry (METI) published reports in 2014 and 2017 (*Ito Report 1.0* and *2.0)* recommending policies on environmental, social, and governance (ESG) integration and for cultivating "intangible assets." The 2017 proposal emerged from a Study Group on Long-term Investment that METI established in 2016. The group advocated for, among other things, increased corporate disclosure of ESG information and in-depth engagement between investors and corporations to improve long-term value creation and investment in intangible assets (e.g. human capital, research & development).

   Additionally, The Ministry of the Environment established Green Bond Guidelines in 2017, in part, to increase private sector investment in solutions to climate change in support of attaining goals established in the Paris Agreement (international agreement on climate change) and the United Nations Sustainable Development Goals (SDGs).

2. **Notable, quasi-governmental organizations have become vocal about sustainability issues.** The Government Pension Investment Fund (GPIF), for example – a large and influential universal asset owner – has labeled itself a "super-long-term" investor with a one hundred-year investment horizon. It has identified climate change and diversity as issues essential to long-term value creation and evaluates its external managers on their engagement with corporations on these and other ESG issues. GPIF became a signatory of the U.N.-supported Principles for Responsible Investment (PRI) in 2015, followed soon after by Japan's Pension Fund Association (PFA) in 2016.

   In addition, the Japanese Financial Services Agency (FSA) regulatory authority partnered with the Tokyo Stock Exchange to develop the Japanese Corporate Governance Code, which similarly emphasizes the importance of long-term value creation.

3. **National and regional organizations are raising awareness about impact investing, a popular sustainable investing approach.** The Japanese National Advisory Board (NAB) of the Global Steering Group (GSG) for Impact Investing issued a report in 2018 assessing progress across the seven social impact investment objectives that it established in 2015. These objectives ranged from utilizing dormant banks accounts for social impact investments, to introducing social impact bonds, and establishing measurable goals for corporate social and environmental impact. In 2018, the Asian Venture Philanthropy Network (AVPN) published its report *Driving ESG Investing in Asia: The Imperative for Growth* with recommendations for early-stage, intermediate, and advanced impact investors.

4. **Sustainable investing is growing worldwide.** The above developments in Japan and elsewhere in Asia are occurring alongside strong global momentum toward sustainable investing. As of 2018, assets invested in a variety of these strategies had reached $12 trillion in the U.S. alone and $30.7 trillion worldwide, or more than one quarter of professionally managed assets globally.

Developments such as these are increasing the pressure on Japanese investors and corporations to incorporate sustainability factors into their practices, a trend that is likely to continue in the coming years.

Sources:
Hall, Marissa (2018). "ESG: Evolution of sustainable investing and modern practice". June 2018. IP&E.com.
Ministry of the Environment, Government of Japan (2017). Green Bond Guidelines, 2017. March 2017.
US SIF Foundation (2018). "Sustainable investing assets reach $12 trillion as reported by the US SIF Foundation's biennial Report on US Sustainable, Responsible and Impact Investing Trends". *Press release*. Washington DC: October 31, 2018.

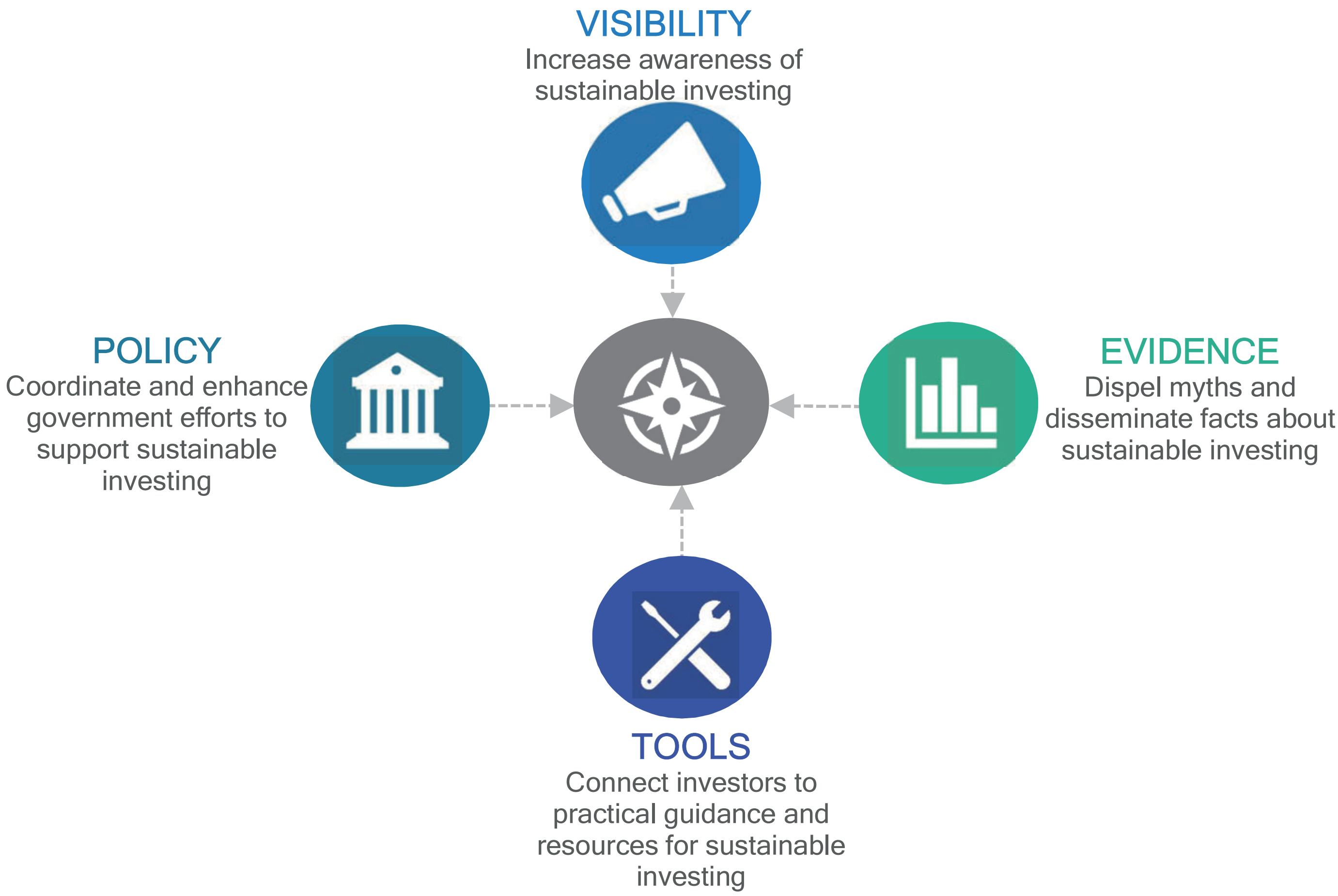
Recommendations for Action

In February 2019, we met with more than 50 experts on the Japanese financial industry to gather their insights on obstacles to, and opportunities for, sustainable investing in Japan. Despite working in different segments of the industry and approaching the issue from a range of viewpoints, these experts largely agreed on the main barriers to sustainable investing in Japan – namely, that:

the Japanese financial community needs access to high-quality information about sustainable investing and its benefits and to detailed implementation guidance, and investors need coordinated government support for their sustainable investing pursuits.

In this section of the *Agenda* we outline four ways that industry leaders in Japan – investors, industry groups, and government alike – can begin to address these challenges and encourage widespread adoption of sustainable investing (see Figure 1). These recommendations reflect a combination of suggestions made by interviewees and our experience helping to address similar challenges in the U.S. and Europe.

Figure 1. Four dimensions for sustainable investing for action in Japan



VISIBILITY

Breakthroughs needed:

→ Mobilize industry influencers (individuals and organizations) to publicly support sustainable investing.

→ Use social and other media to engage retail investors on sustainable investing.

Despite the recent growth of sustainable investing in Japan and its uptake by notable investors (e.g. Government Pension Investment Fund (GPIF), Daiwa Securities, and Nissay Asset Management Corporation), the Japanese financial community is still generally unaware of the practice. Few Japanese investors know what sustainable investing is, and those that do are not necessarily convinced of its merits.

Mobilize industry influencers to publicly support sustainable investing

Interviewees suggested that sustainable investing advocates identify influential individuals – from Asia and elsewhere – who can help to increase the visibility of sustainable investing in Japan. In the U.S., for example:

- The Sustainability Accounting Standards Board (SASB) – which sets standards for corporate sustainability information reporting – recruited Michael Bloomberg and Mary Schapiro to serve as its Chair and Vice Chair, respectively. Bloomberg (former Mayor of New York City, founder of Bloomberg L.P. and well-known billionaire) and Schapiro (former Chair of the Securities and Exchange Commission) helped raise SASB's visibility – and thus the visibility of sustainable investing in the U.S. – with both corporations and investors.
- Larry Fink, the Chairman and Chief Executive Officer of BlackRock, the world's largest asset manager, has used his annual letter each year from 2015 through 2019 to implore corporate executives to balance their focus on short-term performance with a commitment to sustainable, long-term growth.[6] The first of these letters made such an impression on the U.S. financial industry that it is known to many in the industry simply as "the Fink letter."

Interviewees noted that a combination of Japanese investment leaders as well as noted, foreign industry leaders like Bloomberg, Schapiro, or Fink could play this role in Japan. They suggested, for example, that the Chairman and CEO of the Japan Securities Dealers Association and the Vice Chairman of The Life Insurance Association of Japan might be particularly effective influencers because they are leaders of major industry associations, as would the head of Japan's Pension Fund Association (PFA). Comparable influencers who would appeal to retail investors and financial advisors should also be identified.

Influential foreign and domestic industry organizations can be similarly helpful to publicizing sustainable investing in Japan. Like elsewhere around the world, sustainable investing-focused industry associations have emerged in Japan. These networks of asset owners, asset managers, financial advisors, and consultants work to advance awareness of sustainable investing, promote its uptake by investors, and address barriers to action (e.g. through policy advocacy and training). The U.N.-supported Principles for Responsible Investment (PRI), Japan Sustainable Investment Forum, and Japan Social Impact Investment Foundation are some of the organizations that are dedicated to cultivating the sustainable investing ecosystem in Japan.

Although numerous organizations are working hard to raise awareness about sustainable investing in Japan, additional support is necessary to bring it to the mainstream. Continuous, visible support for sustainable investing by organizations such as the CFA Institute, Money Management Institute, Investments & Wealth Institute, and others has slowly but surely increased industry awareness in the U.S. Each has made sustainable investing a major substantive feature of its programs and events for their members. Similar coverage by leading associations in Japan can serve this end. Interviewees identified Japan Investment Advisers Association, the Securities Analysts Association of Japan, Keidanren (i.e. the Japan Business Federation), and The Life Insurance Association of Japan as influential organizations that could be similarly effective ambassadors for sustainable investing in Japan. They might, for example, offer professional designations and networking opportunities related to sustainable investing, and host workshops and conferences focused on sustainable investing.

Once identified, sustainable investing experts should equip influencers to speak and write effectively about sustainable investing – what it is, why it is important, how it can benefit investors, and where to go for more information. In doing so, these experts might solicit insights and lessons learned from influencers from other markets and regions (e.g. the U.S. and Europe).

Use social and other media to engage retail investors on sustainable investing

According to interviewees, there has been minimal (if any) outreach to Japanese retail and individual investors about sustainable investing. These include the smaller, nonprofessional investors that buy and sell securities, mutual funds, or exchange-traded fund (ETFs) through a brokerage firm or savings account and who are the beneficiaries of various retirement and pension plans (public and corporate). Most pension plans assume that these investors just want high returns and are not interested in sustainability issues. Such assumptions directly contradict the trend data indicating that retail investors of all kinds (e.g. old and young, male and female) are interested in sustainable investing.[7]

Intentional outreach to these investors – through social and other media sources – can be an effective way to capture their attention. For example, in 2018 the U.S.-based mutual fund company American Century Investments (ACI) partnered with Nomura Asset Management to launch the Nomura ACI Advanced Medical Impact Fund. Composed of stocks of U.S. health care companies but offered exclusively to Japanese investors, the offering outpaced expectations and attracted unprecedented retail investor interest. The fund's managers credit its success, in part, to the fact that the fund's title highlights an issue of great concern in Japan (eschewing the more generic "ESG" or "sustainable investing" label) and to Nomura's use of YouTube and other social media outlets to engage retail investors about the product. As part of its social media campaign, Nomura partnered with the host of a YouTube channel with a relatively large number of viewers (and Millennial viewers in particular) who featured interviews with Nomura portfolio specialists and other discussions about the fund.

Media outreach efforts should focus on helping investors to understand how environmental, social, and governance (ESG) considerations correspond to their sustainability interests and goals. For example, most of the underlying equities in an ESG index might well be the same as those in a growth fund, but the fund prospectus would not necessarily explain to investors the link between their investment in the fund and its societal benefit.

Similar social and other media outreach to institutional investors might be equally useful for engaging that industry segment in sustainable investing. Interviewees suggested that The Kinzai Institute for Financial Affairs, Nikkei, and Japan Times would be helpful places to start.

EVIDENCE

Breakthroughs needed:

→ Dispel myths about sustainable investing.

→ Connect investors to information about the what, why, who and how of sustainable investing.

According to interviewees, myths about sustainable investing are pervasive in Japan. Many investors, for example, believe that:

- Sustainable investing is a form of philanthropy;
- It hurts financial performance (and therefore violates fiduciary duty);
- Investors cannot impact ESG issues (only the government can impact these issues); and
- Sustainable investing is a passing fad that most investors do not take seriously.

Put simply, not only is the Japanese financial community generally *uninformed* about sustainable investing (as described above), but it is also *misinformed* about the practice. Furthermore, asset managers, advisors, and consultants see little value in dedicating limited time and resources to exploring and integrating an approach that seemingly lacks a competitive track record.

Interviewees asserted that Japanese investors need access to objective, credible, and rigorous research that directly dispels these falsehoods. Although much evidence and data on the facts about sustainable investing have been developed by or for investors in other regions, these analyses are typically either unavailable in Japanese or are otherwise not specific to the Japanese market. These include, for example:

- Research by Merrill Lynch that asserts that investors perform well financially when they invest in environmental and socially sustainable organizations, and that highlights notable developments in impact investing (e.g. rapid growth caused in part by increased client demand and increased quantity and quality of ESG data);[8]
- Research published in the *Journal of Applied Corporate Finance* that dispels myths about financial performance and sustainable investing and corrects other falsehoods;[9] and
- The first comprehensive analysis of the financial performance of market rate private equity and venture capital impact investing funds, which was published by Cambridge Associates and the Global Impact Investing Network.[10]

As a first step in addressing this challenge, champions for sustainable investing in Japan might translate, adapt, and amend existing research on sustainable investing that has been conducted in or for other markets to meet the needs of each of the various segments of Japan's financial community. Where such evidence is lacking or does not reflect the realities of the Japanese financial markets, new research should be conducted. Existing or new, needed evidence includes:

1. Information about **what** sustainable investing is (and what it is *not*) and that clarifies the many different terms used to describe sustainable investing approaches (e.g. impact investing, ESG integration, socially responsible investing);
2. Data on the material importance of ESG factors and the connection between ESG factors and financial performance (**why** investors pursue it);

3. Information about client demand for sustainable investing strategies and products (**who** is investing sustainably and who wants to do so); and
4. Research on the strategies that investors use to impact the environment and society and on which asset classes are most beneficial for addressing which sustainability issues (**how** to invest sustainably).

Japanese investors also need *detailed* case studies of mainstream Japanese and other investors who have successfully adopted sustainable investing. Interviewees recommended that these case studies include all major industry segments (e.g. asset owners, asset managers, consultants and advisors) and both domestic and international examples. These might include, for example:

- *Pension funds* (California State Teachers' Retirement System, VicSuper Pty. Ltd., Pension Fund Association);
- *Insurance companies* (Allianz SE, AVIVA Investors, Dai-Ichi Life);
- *Diversified financial institutions* (UBS, Bank of America, Sumitomo Mitsui Trust Asset Management Co. Ltd); and
- *Asset managers* (Trillium Asset Management, Sonen Capital, Nissay Asset Management Corporation,).[11]

The growing number of sustainable investing-related awards and other formal acknowledgements in Japan provide one opportunity to disseminate success stories. For example, In 2019, the Tokyo Metropolitan Government awarded the first-ever Tokyo Financial Award in ESG Investing, which recognized Neuberger Berman East Asia Ltd., Robeco Japan Co. Ltd., Sompo Holdings Inc. and Sumitomo Mitsui Trust Asset Management Co. Ltd. as financial services companies that are working to advance sustainable investments.[12] Although the award is an excellent way to highlight reputable investors who have adopted sustainable approaches, it stops short of providing insights about how, specifically, these investors are integrating ESG considerations into their investment and other activities – practical information that would be exceedingly helpful to investors who are interested in sustainable investing but uncertain about the practicalities of actually doing so.

Of course, Japan is not devoid of domestic efforts to catalogue and communicate evidence about the prevalence and effectiveness of sustainable investing. These include, for example, the Japan Sustainable Investment Forum's (JSIF) annual survey of sustainable investing in Japan, the Japanese National Advisory Board of the Global Steering Group for Impact Investing's 2016 report, *Current State of Social Impact Investment in Japan*, and the CFA Society of Japan's 2014 guide on ESG integration, *Environmental, Social, and Governance Factors at Listed Companies: A Manual for Investors*, among others. However important these might be, interviewees indicated that such reports: (1) commonly target like-minded industry professionals (that is, they "preach to the already converted"), (2) can be perceived as overly subjective because they are oftentimes (but not always) produced by sustainable investing advocates, and (3) received some initial attention that was not sustained over time.

Simply providing investors with information about the what, why, who, and how of sustainable investing will not ensure that they retain, internalize, and act on the information. Efforts to produce and disseminate evidence must therefore be accompanied by appropriate training and education opportunities.

TOOLS

Breakthroughs needed:

- → Provide investors with practical guidance for integrating sustainable investing into their practices.
- → Connect investors to capacity building opportunities (e.g. industry forums and sustainable investing workshops).
- → Establish a sustainable investing knowledge hub for Japan.

Even if Japanese investors know about sustainable investing, are convinced of its merits, and understand how other investors invest sustainably (broadly speaking), they do not know where to start integrating it into their own practices.

Provide investors with practical guidance for integrating sustainable investing into their practices

Project interviewees indicated that the Japanese financial community lacks practical guidance on how to develop, implement, and maintain sustainable investing programs and policies. When showed examples of "how-to" guidance that has been developed for U.S.-based and other investors, interviewees affirmed that similar support would be useful in Japan. That is, that the Japanese financial community needs guidance that:

- Provides detailed instructions for building a sustainable investing practice from scratch;
- Suggests ways to integrate sustainable investing considerations across existing investment activities (e.g. in investment belief and policy statements, security selection and portfolio construction, manager due diligence, and corporate engagement) and through other, non-holdings activities; and
- Reflects global standards, best practices, and the nuances of the Japanese investment landscape.

Guidance should target and address the specific needs of each sector of the Japanese financial community. Japan's investment community is diverse - asset owners range from major public pension funds like GPIF to insurance companies like Sumitomo Life. These investors rely on a spectrum of intermediaries, including asset managers (e.g. Nissay Asset Management Corporation) and investment consultants (e.g. Russell Investments). This ecosystem is further reinforced by discretionary investment managers like trust banks (e.g. Mizuho Trust & Banking Co.) and the financial advisors affiliated with them. Each of these industry segments needs guidance that considers and addresses their unique functions, challenges, and competitive landscape. Additionally, individual firms might require more customized, one-on-one support.

Connect investors to capacity-building opportunities (e.g. industry forums and sustainable investing workshops)

Sustainable investing capacity-building events, workshops, and other learning opportunities have become more prevalent in and around Japan. Domestically, the PRI maintains the Japan Network, which enables PRI signatories to learn about global sustainable investing trends and key domestic issues. The Network also offers workshops and conferences in Japan. The CFA Society of Japan provides ESG seminars, some of which serve to reinforce guidance and materials produced by PRI.

The Japan Social Investment Forum provides learning groups and research and data to help promote sustainable investing. And the Social Impact Investment Foundation co-hosted an impact investment forum in 2018 to similarly catalyze impact investing activity in Japan. This is to say nothing of other efforts around the region that are targeting the broader investment ecosystem, such as the Asia Sustainable Finance Initiative in Singapore, or specific investor markets, like the Sustainable Finance Initiative of the RS Group in Hong Kong.

Interviewees indicated that more work needs to be done to offer effective capacity-building opportunities. They noted that, although existing events are helpful, they tend to appeal to those who already know about sustainable investing and are convinced of its merits rather than the broader industry – limiting their profile, credibility, and usefulness. To solve this, they suggested that there would be utility in:

- A forum convened by the Financial Services Agency (FSA), which might appear more credible to investors than events hosted by sustainable investing advocates who run the risk of seeming to lack impartiality;
- Integrating sustainable investing information into existing (and oftentimes required) continuing education, credentialing, and certification programs; and
- Sharing information via the Kinzai Institute of Financial Affairs, which multiple interviewees referred to as a particularly useful platform for providing ongoing support to financial advisors.

Overall, it is a combination of forums and workshops by mainstream investment organizations and associations that both are and are not primarily focused on sustainable investing that will help to broaden and deepen the appeal and utility of sustainable investing in Japan.

Establish a sustainable investing knowledge hub for Japan

In 2018, the Money Management Institute (MMI)—a U.S.-based network that supports money managers and financial advisors through industry advocacy, educational initiatives, regulatory affairs, publications, data reporting, and professional networking—launched the Sustainable Investing Initiative (SII) in partnership with Morningstar, an investment research company offering mutual fund, ETF, and stock analysis, ratings, and data. The SII provides a suite of sustainable investing educational resources, workshops, forums and thought leadership. Together with additional resources from The Forum for Sustainable and Responsible Investment and PRI Academy, SII offers a series of courses for financial advisors, asset managers, and investors on the entirety of the sustainable investing spectrum (from public equities to fixed income securities, to private equity investments). SII also maintains Harvest, a digital content platform for the investor community, through which financial organizations distribute their latest insights on sustainable investing, empowering investors to make the most informed decisions.

When asked whether a similar hub would be useful in Japan, interviewees responded that it most certainly would. A rigorously-curated platform would serve as a central repository for the distribution of sustainable investing research and commentary, both from within and outside of Japan. It would be structured so that individuals, firms, and associations could equally access and leverage its resources – all of which would be published in or translated into Japanese.

POLICY

Breakthroughs needed:

→ Coordinate efforts by cabinet-level government agencies to support sustainable investing.

→ Embrace “soft law” approaches to guide investors in their implementation of sustainable investing-related regulations.

Increasing the visibility of sustainable investing in Japan, disseminating evidence of its merits, and developing practical tools for integrating into investment practices will collectively go a long way to creating the breakthroughs needed to advance the practice. But interviewees identified one additional dimension that will also need to be addressed: the role of policy in creating an enabling environment for investor action.

Coordinate efforts by cabinet-level government agencies to support sustainable investing

Interviewees commented that Japanese governmental and regulatory agencies have launched various initiatives in support of sustainable investing, but that these efforts have been fragmented and at times confusing. Among the government initiatives that they cited are:

- The *Council on Investments for the Future*, a cabinet-level push for increased disclosure of non-financial information in public documents like annual reports and financial statements;
- A partnership between FSA and the Tokyo Stock Exchange to develop the *Japanese Corporate Governance Code*, which emphasizes the importance of long-term value creation;
- The launch of Japanese National Advisory Board, a satellite committee of the Global Steering Group for Impact Investing;
- The passage of the Dormant Deposit Utilization Act, which enables the use of funds from inactive bank accounts to finance social welfare activities;
- The creation in 2016 of the cabinet-level Sustainable Development Goals Promotion Headquarters; and
- The Ministry of Economy Trade and Industry (METI)-published *Ito Report 1.0* (2014) and *2.0* (2017) recommending policies on ESG integration and the cultivation of “intangible assets.”

Interviewees stated that information on which of these initiatives are successfully fostering an enabling environment for sustainable investing is not always shared across agencies. Although these efforts are not necessarily in conflict with each other, they do not appear to be intentionally reinforcing or complimentary. What’s more, individual ministries and agencies have jurisdiction over different segments of the financial community, and some segments answer to more than one regulatory body.

Although coordinating efforts at other levels of government is also important, interviewees stressed the importance of partnerships and communication at the *cabinet-level*. Cabinet-level agencies directly support Prime Minister and are empowered to promote an agenda that supersedes departmental or ministerial politics or constraints (i.e. the Cabinet Secretariat and Cabinet Office). These agencies can most effectively help to ensure that sustainable investing in Japan can advance in a coherent and comprehensive way.

Embrace “soft law” approaches to guide investors in their implementation of sustainable investing-related regulations

Interviewees heralded the introduction of new stewardship and governance codes as transformative for sustainable investing in Japan (i.e. Japanese Corporate Governance Code and Principles for Responsible Institutional Investors). They noted, however, that while these codes are positive developments on their face, their effectiveness is diminished by lack of implementation encouragement, requirements, and support. For instance, oversight entities do not specify when, whether, or how companies should educate board members on the codes.

Lack of systematic guidance means that the approximately 40,000 board members of Japan's approximately 4,000 publicly-listed companies might interpret and execute on the codes inconsistently at best and incorrectly at worst. This stands in contrast to other countries, like Pakistan, where the introduction of stewardship codes was accompanied by a government mandate requiring that directors go through at least 40 hours of education on good governance practices by an accredited program.[13]

Interviewees recommended that government use "soft law" techniques to promote the embrace of and fidelity to sustainable investing policies and regulations. That is, that they provide detailed guidance and implementation standards to ensure that investors not only do what a policy instructs that they do, *but that they do it well*. Soft law can also help the government to promote sustainable investing, more generally speaking. Specific approaches might include:

- **Awareness.** Japanese governmental agencies can spearhead stakeholder education and engagement (i.e. an awareness campaign) in support of sustainable investing regulations and policy and can encourage disclosure of participation in such activities. In the U.S., for example the government's Office of Social Innovation and Civic Participation collaborated across executive branch agencies to promote sustainable investment. This included helping to clarify rules for foundations' use of mission-related investments in for-profit companies to further charitable objectives and facilitating the Department of Labor's guidance to pension plans about the consideration of ESG factors without violating their fiduciary duty; both of which have helped enable increased investment in sustainable strategies.[14]

  A recent paper by The Ministry of the Environment, Japan – *Recommendation from the High-Level Meeting on ESG Finance: Toward becoming a big power in ESG finance* – suggests that the Japanese government spearhead sustainable investing education in ways like we are outlining here. Specifically, the Ministry recommends that the Japanese government convene an "ESG Finance High-Level Panel" of government and financial industry leaders. The purpose of the group would be to increase awareness and uptake of sustainable finance in Japan - in line with Prime Minister Abe's stated objective to competitively position Japan as a sustainable society and to support achievement of the SDGs and Paris Agreement goals.[15]

  The FSA's partnership with the Japan Exchange Group, Inc. (JPX) to raise awareness about the recommendations of the Task Force on Climate-related Financial Disclosures (TCFD) provides an excellent model for the Ministry's ESG Finance High-Level Panel or any other future government-led efforts to promote sustainable investing and support successful investor compliance with related policies. In February 2019, the two agencies co-hosted a symposium for business leaders and investors at the Tokyo Stock Exchange. The symposium focused on helping stakeholders to understand how the TCFD recommendations can help companies to enhance value and to learn about their implementation in Japan.[16]

- **Subsidies.** Agencies can also offer subsidies (financing, grants) to encourage investor action on sustainable investment. In the U.K., for example, the government launched Big Society Capital (BSC) to use funds from dormant bank accounts to co-invest in financial intermediaries that provide funding to social enterprises (and assume most of the risk for such investments). The U.K. government also established The Investment and Contract Readiness Fund – a cross-sector fund managed by a third party, and The Social Investment Business – to provide grants for technical assistance to social enterprises seeking new forms of investment or competing for public service contracts – ultimately helping to build the pipeline of sustainable investment opportunities.[17]

- **Accolades.** Lastly, Japanese government agencies can publicly acknowledge and congratulate those investors who are adopting sustainable investing in credible and effective ways. The Tokyo Metropolitan Government's first-ever Tokyo Financial Award in ESG Investing, for example, highlighted sustainable investing best practices while also demonstrating that government is taking sustainable investing seriously.

The combination of these enhanced soft law approaches with more effective coordination of policy efforts at the cabinet level would promote more investor action on sustainable investing.

Implications for the Region

While the research that we conducted to develop this *Agenda for Action* focused on investors in Japan, we also preliminarily assessed the needs of financial industry professionals elsewhere in Asia (Singapore, Hong Kong, and China).

Interviewees largely reported that investors in Asia ex Japan confront many of the same obstacles to sustainable investing as those in Japan. Within these shared challenges, interviewees emphasized the **lack of “practice management” support and guidance** in these areas as a particularly substantial challenge, implying the need for practical, how-to guidance to support the integration of sustainable investing into practices.

They highlighted the following organizations and initiatives as particularly effective supports for sustainable investing in Asia ex Japan:

- **The Asia Sustainable Finance Initiative (ASFI)** is a multi-stakeholder forum headquartered in Singapore that aims to harness and amplify the power of finance to create resilient economies that deliver on the Sustainable Development Goals (SDGs) and the Paris Agreement. ASFI works across six focus areas to support financial institutions to better understand and incorporate material ESG risks and opportunities into decision-making processes (standards, research and tools, engagement, green financial solutions, regulations and guidelines, and capacity building);[18]

- **The Sustainable Finance Initiative (SFi)** is a community platform that promotes the growth of sustainable finance with private investors in Hong Kong. Among other things, it: (a) educates private investors, other stakeholders, and the public on sustainable finance through workshops, publications and peer-to-peer learning; (b) demonstrates the value of sustainable finance; (c) connects private investors with peers to change mindsets about investment, consumption, and sustainability; and (d) mobilizes private capital to help accelerate Hong Kong’s transition towards a sustainable finance hub. It was incubated by RS Group and launched in June 2018.[19]

- **The Asian Venture Philanthropy Network (AVPN)** is a funders' network based in Singapore that is committed to building a “vibrant and high impact” social investment community across Asia. It provides its members with opportunities for education and networking (e.g. conferences and workshops), connects them to social investment resources (e.g. reports, case studies), and facilitates opportunities for action (e.g. engaging policymakers, featuring collaborative funding opportunities).[20]

Although a helpful starting point, we think that this information should be augmented by detailed assessments of sustainable investing in Singapore, Hong Kong, China, India, and elsewhere to more effectively inform recommendations targeted to each area’s financial industry and unique needs.

Conclusions

Sustainable investment – the practice of investing in pursuit of financial sustainability and/or environmental or social sustainability – is increasingly popular. Major financial institutions are developing sustainable product platforms; leading index providers offer extensive families of sustainability indexes; and asset management firms provide opportunities and products that range across all asset classes. All told, sustainable investments now account for more than one fourth of AUM worldwide.

Japan, with the third-largest economy in the world, has an exciting opportunity to seize increasing enthusiasm for the practice and to become a world leader in sustainable investing.

Key to doing so will be coordination among asset owners, asset managers, and publicly-traded corporations and private businesses. Investors still look to the corporations in which they invest, just as corporations look to their investors, for the initial commitments to long-term value creation that is necessary to close a mutually reinforcing virtuous circle. Both parties in turn seek confirmation from the government and the public markets that the time has come for a shift to such strategies. With multiple spheres of influence in play, complicated dynamics impede the necessary alignment that, once achieved, will clear the path to fulfilling the potential for sustainable investment in the region.

Finally, there are important dimensions of sustainable investing not discussed in this *Agenda*; namely, corporations' disclosure of high-quality, standardized, and machine-readable sustainable data. Exploration of this and related issues – and development of practical solutions – will be crucial to ensuring successful execution of sustainable investing strategies in Japan.

Attachment A: Data Sources

TIIP collected and analyzed data from four sources to develop *Sustainable Investing in Japan - An Agenda for Action.*

1. **Literature review.** TIIP reviewed literature on sustainable investment and related practices and topics, and on integration of sustainable investment in Japan and Asia more broadly.

2. **Expert interviews.** TIIP interviewed a range of industry thought leaders and experienced investors about sustainable investing in Japan. TIIP research staff conducted interviews using an interview guide that ensured the systematic collection of comparable information across respondents while also allowing interviewers to pursue questioning specific to individual respondent's expertise and experience. TIIP provided select interviewees with an early draft of the guide; their reactions and feedback informed revisions and the content of this final version.

3. **TIIP's institutional knowledge and theoretical frameworks.** TIIP is an industry thought leader on sustainable investment theory and practice and has conducted various research projects related to sustainable investing and the topics explored through this project. This *Agenda for Action* builds on the work of TIIP's President William Burckart as appropriate and incorporates insights from *Fundamentals of Sustainable Investing: A guide for financial advisors (MMI, 2019), Bringing Impact Investing Down to Earth: Insights for Making Sense, Managing Outcomes, and Meeting Client Demand (MMI, 2015), Serving Client Demand for Impact Investing: A Hands-on Guide for Financial Advisors and Senior Management (MMI, 2014),* the *New Frontiers of Philanthropy: A Guide to the New Tools and Actors that Are Reshaping Global Philanthropy and Social Investing (Oxford University Press, 2014),* and the *Status of the Social Impact Investing Market: A Primer (UK Cabinet Office, 2013).* It also leveraged information from TIIP's advisory projects, including reviews of client engagements.

Interview respondents listed below (alphabetically by organization, then by first name). Note that company affiliations are listed for identification purposes only and do not imply endorsement by firms.

Organization	Name	Role
Asia Sustainable Finance Initiative	Jeanne Stampe	Founder
Asia Value Advisors	Philo Alto	Founder & CEO
Asian Corporate Governance Association	Jamie Allen	Secretary General
Asian Venture Philanthropy Network	Caroline McLaughlin	Director of Partnerships
	Patsian Low	Director, Asia Policy Forum
	Roshini Prakash	Knowledge Senior Manager
C4 Capital for New Commons	Xavier Arnaudo	Founder
CFA Institute	Bob Dannhauser	Head Global Private Wealth Management
Chief Executives for Corporate Purpose	Brian Tomlinson	Research Director, Strategic Investor Initiative
Crosspoint Advisors	Hiroshi Nonomiya	Representative Director and Partner
Dai-Ichi Life	Miyuki Zeniya	General Manager, Responsible Investment Center
Daiwa Institute of Research	Mariko Kawaguchi	Senior Principal, Research Division
Daiwa Securities	Masaaki Amma	Senior Advisor to the Board
Domini Impact Investments	Shin Furuya	Impact Investing Strategist

Government of Japan	Satoshi Ikeda	Chief Sustainable Finance Officer, Director of the International Affairs Office, Financial Services Agency
	Akiko Shintani	Deputy Director, Sustainable Finance Group, International Affairs Office, Financial Services Agency
	Taiki Suda	Officer, International Affairs Office, Financial Services Agency
Government Pension Investment Fund	Kenji Shiomura	Director, Economist/Strategist, Investment Strategy & ESG, Stewardship
	Mina Yagi	Investment Strategy & ESG
	Tetsuya Oishi	Managing Director, Investment Strategy & ESG Department
Impact Investing Exchange	Robert Kraybill	Managing Director
Independent	Charles Yang	Independent Consultant
Japan Center for International Finance	Rintaro Tamaki	President
Japan Sustainable Investment Forum	Masaru Arai	Chair
KPMG	Sumika Hashimoto	Senior Manager, Japan Integrated Reporting CoE and Corporate Governance CoE
	Yoshiko Shibasaka	Associate Partner, Japan Integrated Reporting CoE and Corporate Governance CoE
Kyoto University *Graduate School of Management*	Yasuyuki Kato	Professor, Financial Engineering and Investment Theory
Mizuho Bank	Kotaro Sueyoshi	Senior Manager, New Business Promotion Office, Retail & Business Banking Coordination Department
Morgan Stanley Mitsubishi UFG	Mitsuhiro Saito	Executive Director
Nissay Asset Management Corporation	Mafumi Lisa Tamaoki	General Manager
	Toshikazu Hayashi	Chief Analyst, ESG Investment Promotion
Perella Weinberg Partners	Jameela Pedicini	Executive Director, Co-lead, Mission-Aligned Investment
RS Group	Leonie Kelly	Project Director of Sustainable Finance Initiative
	Ronie Mak	Managing Director
Social Impact Investment Foundation	Fumi Sugeno	Business Development, Senior Officer
	Nanako Kudo	Executive Director
	Yuko Koshiba	Impact Officer
Sumitomo Life	Toshio Fujimura	General Manager, Investment Planning Department
	Shiro Kodama	Deputy General Manager, Investment Planning Department
Sumitomo Mitsui Trust Asset Management	Hiroyuki Horii	Executive Officer, General Manager, Chief Stewardship Officer, Stewardship Development Department
	Hisaya Kambayashi	General Manager, Senior Stewardship Officer, Stewardship Development Department
	Takeshi Wada	Senior Stewardship Officer, Stewardship Development Department
Sumitomo Mitsui Trust Bank	Toyoda Shunsuke	Section Manager
Symphony Financial Partners	John Trammell	Managing Director, Global Strategic Initiatives

The Board Director Training Institute of Japan	Nicholas Benes	Representative Director
The Investment Integration Project	Steve Lydenberg	Founder and Chief Executive Officer
The Research Institute for Policies on Pension and Aging	Ryujiro Miki	Specially Appointed Researcher
The Sasakawa Peace Foundation	Mari Kogiso	Director Gender Investment and Innovation Department
	Karthik Varada	Project Coordinator, Gender Investment and Innovation Department
Third Arrow Strategies	Tracy Gopal	Founder
UBS	Mario Knoepfel	Director of Sustainable Investing, Asia-Pacific
University of Oxford *Saïd Business School*	Robert Eccles	Visiting Professor of Management Practice
Wells Fargo Private Bank	Lloyd Kurtz	Senior Portfolio Manager, Head of Social Impact Investing
World Wildlife Fund	Jean-Marc Champagne	Head of Environmental Finance
	Keith Lee	Sustainable Finance Engagement Manager
	Sam Hilton	Senior Research Analyst, Environmental Finance

Attachment B: About TIIP and SPF

The Sasakawa Peace Foundation (SPF). SPF is a Japanese private foundation established in 1986 to enhance international cooperation. SPF has set its focus on five key areas: addressing a variety of societal challenges that fast-emerging Asian countries currently face, stimulating greater socioeconomic progress through women's empowerment, promoting understanding and strengthening relationships with Muslim-majority countries, further strengthening Japan–U.S. relations, and developing programs to promote the long-term sustainability of the world's oceans.

The Investment Integration Project (TIIP). TIIP's mission is to help investors understand how healthy environmental, social, and financial systems can benefit their portfolios. TIIP provides thought leadership, research, and consulting services that support investors' pursuit of system-level investing, an advanced sustainable investing approach that focuses on managing systemic risks and investing in solutions to systemic problems.

Endnotes

[1] Global Sustainable Investment Alliance (GSIA) (2018). *2018 Global Sustainable Investment Review*.

Both TIIP and GSIA use "an inclusive definition of sustainable investing, without drawing distinctions between this and related terms such as responsible investing and socially responsible investing." This definition includes: negative/exclusionary screening; positive/best-in-class screening; norms-based screening; ESG integration; sustainability themed investing; impact/community investing; and corporate engagement and shareholder action.

At the start of 2018, sustainably invested assets in the five major markets (U.S., Europe, Japan, Canada, Australia and New Zealand) totaled $30.7 trillion.

Boston Consulting Group (BCG) (2018). *Global asset management: The digital metamorphosis.* July 2018.

BCG estimates global professionally managed assets at $79 trillion in 2018 (across all markets). A conservative estimate, therefore, is that sustainably invested assets worldwide account for ¼ of all professionally managed assets worldwide.

[2] Evidence includes:

Cambridge Institute for Sustainability Leadership (2015). Unhedgeable risk: How climate change sentiment impacts investment. Cambridge, UK: November 2015.

Eccles, Robert and Mirtha Kastrapeli. The Investing Enlightenment: How Principle and Pragmatism Can Create Sustainable Value through ESG. State Street Corporation. 2017.

Edmans, Alex (2011). Does the stock market fully value intangibles? Employee satisfaction and equity prices. Journal of Financial Economics 101 (2011) 621–640.

Global Impact Investment Network (2017). Evidence on the Financial Performance of Impact Investments. Abhilash Mudaliar and Rachel Bass. November 2017.

Harvard Business School (2015). Corporate Sustainability: First Evidence on Materiality. Khan, Mozaffar N., George Serafeim, and Aaron Yoon. Harvard Business School Working Paper, No. 15-073, March 2015.

Holder, Michael (2018). "Evidence links ESG performance to better investments". GreenBiz. January 10, 2018.

Journal of Sustainable Finance (2015). ESG and financial performance: aggregated evidence from more than 2000 empirical studies. Gunnar Friede, Timo Busch, and Alexander Bassen. Journal of Sustainable Finance & Investment, 5:4, 210-233.

LPL Financial. Sustainable Investing: Strategic Discovery. April 2017.

Morgan Stanley Institute for Sustainable Investing (2015). Sustainable Reality: Understanding the Performance of Sustainable Investment Strategies. March 2015.

MSCI (2017). Foundations of ESG Investing. Part 1: How ESG Affects Equity Valuation, Risk and Performance. Giese, Linda-Eling Lee, Dimitris Melas, Zoltan Nagy, and Laura Nishikawa. November 2017.

Nuveen and TIAA Investments (2017). Responsible Investing: Delivering competitive performance. Amy O'Brien, Lei Liao, and Jim Campagna. July 2017.

Oxford University and Arabesque Partners (2014). From the Stockholder to the Stakeholder: How Sustainability Can Drive Financial Performance. Gordon Clark, Andreas Feiner, and Michael Viehs. September 2014.

Skroupa, Christopher P. (2017). "How Intangible Assets Are Affecting Company Value in the Stock Market". Forbes.com. November 2017.

University of Pennsylvania (2016). Great Expectations: Mission Preservation and Financial Performance in Impact Investing. Jacob Gray, Nick Ashburn, Harry Douglas, and Jessica Jeffers. The Wharton Social Impact Initiative of the University of Pennsylvania. September 2016.

US SIF Foundation (2016). The Impact of Sustainable and Responsible Investment. June 2016.

World Economic Forum (2013). From the Margins to the Mainstream: Assessment of the Impact Investment Sector and Opportunities to Engage Mainstream Investors. World Economic Forum. September 2013.

[3] GSIA (2018).

[4] These include, for example, establishing Japan's first Stewardship Code and first Corporate Governance Code, and the Japanese Government Pension Investment Fund (GPIF) and Pension Fund Association signing the Principles for Responsible Investment (and GPIF's Chief Investment Officer serving on the board) and encouraging managers to incorporate ESG considerations into investment selection.

[5] GSIA (2018).

The Global Sustainable Investment Alliance released *2018 Global Sustainable Investment Review* in late March 2019, near the conclusion of the *Agenda for Action* project. It described growth trends similar to that of the *2016 Review*, which noted that sustainably invested AUM grew a staggering 242% between 2016 and 2017, from almost ¥56.3 trillion to nearly ¥136.6 trillion. The data also indicated, however, that despite this growth, sustainably invested AUM represented just 3.4% of Japan's total AUM in 2016, compared to 21.8% in the United States and 52.6% in the European Union - the third largest economy in the world, Japan accounted for just 2% of global assets invested in sustainable strategies in 2016. As such, the *Agenda for Action* project was originally conceived to examine why the share of total AUM invested in sustainable strategies in Japan lagged that of other major economies.

When confronted with the data from the *2018 Review*, investors and others interviewed for the project were encouraged by the sustained, rapid growth of the practice in Japan but asserted that most of their clients and partners remained uninformed about and uninterested in sustainable investing and that it was very much an approach used only by a select few types of investors (niche, boutique, explicitly long-term).

Put simply, project interviewees described a disconnect between the reported *2018 Review* data and what they are experiencing on the ground.

[6] "BlackRock CEO Larry Fink tells the world's biggest business leaders to stop worrying about short-term results." April 14, 2015. Businessinsider.com.

[7] See for example: Morgan Stanley Institute for Sustainable Investing (2017). *Sustainable Signals: New Data from the Individual Investor.* August 2017.

Schroders Global Investor Study 2016. *What investors think about responsible investing.*

Waggoner, John (2017). Millennials, women drive assets to ESG strategies: *The number of ESG funds has increased sharply over the past few years, and interest is growing among advisers*. InvestmentNews. November 7, 2017.

Women's Philanthropy Institute at the Indiana University Lilly Family School of Philanthropy (2018). *How Women and Men Approach Impact Investing*. May 2018.

World Economic Forum (2013). *From the Margins to the Mainstream: Assessment of the Impact Investment Sector and Opportunities to Engage Mainstream Investors.* World Economic Forum. September 2013.

[8] Snider, Anna (2018). *Impact Investing: The Performance Realities.* Chief Investment Office Global Wealth & Investment Management, Bank of America Merrill Lynch. June 2018.

[9] Kotsantonis, Sakis, Chris Pinney, and George Serafeim (2016). "ESG Integration in Investment Management: Myths and Realities". *Journal of Applied Corporate Finance*. Vol. 28, No. 2. Spring 2016.

[10] Cambridge Associates (2015). *Introducing the Impact Investing Benchmark.* June 2015.

[11] In their recent publication, *Guidance and Case Studies for ESG Integration: Equities and Fixed Income*, the CFA Institute and PRI include a case study of Nissay Asset Management Corporation. The case study usefully highlights Japanese investor embrace of sustainable investing. It also highlights the need to more readily collect and disseminate such information about Japanese investors – of the 33 investors profiled in the report, Nissay was the only investor from Japan.

[12] Walker, Danielle (2019). "4 companies win inaugural ESG award from Tokyo Metropolitan Government." *Pension & Investments.* March 4, 2019.

[13] See Benes, Nicholas (2018). "Public Comment to the Proposed Revisions to Japan's Governance Code". April 27, 2018, which makes this same point about education as crucial to effective policy implementation.

[14] Napach, Bernice (2015). *DOL Clears Way for Impact Investing in Retirement Plans*. October 22, 2015.

Wilkinson, Davide (2016). *Steps to Catalyze Private Foundation Impact Investing.* White House Blog. April 21, 2016.

[15] Ministry of the Environment, Government of Japan (2018). *Recommendation from the High-Level Meeting on ESG Finance – Toward becoming a big power in ESG finance.* July 2018.

[16] www.jpx.co.jp/english/corporate/sustainability/news-events/20190212-01.html

[17] Schwab Foundation for Social Entrepreneurship and World Economic Forum (2013). Breaking the Binary: Policy Guide to Scaling Social Innovation.

[18] www.asfi.asia

[19] www.sustainablefinance.hk

[20] avpn.asia