Keidanren
Policy & Action

Promoting Constructive Dialogue between Companies and Investors

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Keidanren (Japan Business Federation)

Note: The Japanese version is the original and this English version is for reference purposes. If there is any conflict or inconsistency between the two versions, the Japanese version shall prevail.

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I. Introduction

COVID-19 has had a devastating impact on the global economy and its markets. Although efforts had been under way in Japan to implement “Society 5.0 for SDGs,” a vision aimed at solving social challenges and creating new value through a digital transformation in various fields, the clash with the coronavirus pandemic has exposed the fragility of Japanese society and highlighted the necessity of quickly developing a more resilient socioeconomic system. To that end, building financial and capital markets that ensure access to a stable supply of capital from a medium and long-term perspective and support the creation of a sustainable society will be a must. Furthermore, it will be necessary to generate a virtuous cycle for investors’ investments in Society 5.0-related fields and the corporate creation of new value.

For some years now, participants in the financial and capital markets have been criticized for, and compelled to reflect on, “short-termist” investment styles driven solely by the quest for short-term profits. That pressure has helped shift importance toward enhancing medium- to long-term value such as future corporate potential and business sustainability and fueled a rapid proliferation of opportunities for active investments in projects with a focus on sustainability and ESG—namely, environmental, social, and corporate governance-related criteria. From the standpoint of preserving business sustainability, the coronavirus pandemic has not only reaffirmed the importance of corporate capabilities in the arena of crisis response, but also set the stage for a renewed awareness of the importance of making investments from a long-range perspective as well as investing in companies that create value for a sustainable society. Signs of this are arguably evident as many institutional investors worldwide have called on the companies in their portfolios to focus on maintaining their levels of employment rather than pursuing short-term profits and they have also demonstrated a more flexible response to falling returns on equity (ROE) and reduced or canceled dividends in the exercise of their voting rights.

Additionally, corporate considerations for their diverse stakeholders and actions aimed at achieving sustained growth are trends that are becoming more widespread worldwide. The Business Roundtable, an association of chief executive officers from leading US companies, issued a statement in August 2019 underscoring a commitment to business policies and actions that place new emphasis on benefits for employees and local communities, complementing the shareholder-centric policies it has traditionally supported. Further, the January 2020 meeting of the World Economic Forum announced its commitment to “stakeholder capitalism,” the principles of which call on companies to work together with diverse stakeholders in the interest of sustained value creation. In keeping with the traditional view that it is “good for everyone,” many Japanese companies have long sought medium- to long-term gains in their own corporate value and solutions to social issues through those improvements. Moving forward, they will find it imperative to join with their diverse stakeholders in dealing with the coronavirus pandemic and the societal changes it brings.

In the near term, many companies will face the task of formulating business strategies that foresee a new sense of values and a business environment shaped by the transition from the current to post-coronavirus era, along with a heightened need to explain their new strategies from a long-term perspective through dialogue with their investors. Disclosure is the primary channel through which companies share information with investors. However, there is a limit to how well the provision of data alone can effectively explain business strategies from a medium- and longer-term perspective. It is precisely through dialogue with investors that companies will be able to overcome the challenges they face and foster awareness that helps boost their corporate value over the medium and longer term, and through which investors will be able to reap the benefits of corporate growth. Therein lies the value of constructive dialogue (engagement) between companies and investors.

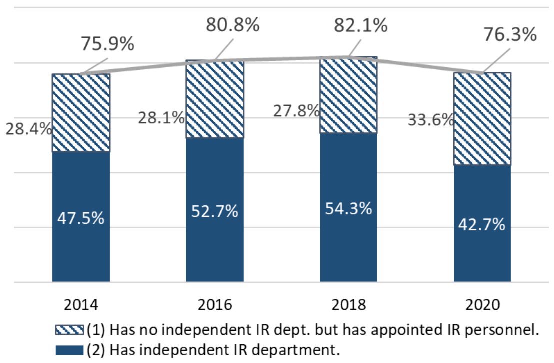
Achieving gains in corporate value over the medium and longer term will demand that companies in Japan constantly strive to improve the effectiveness of their constructive dialogue with investors. Although companies and investors have shown continued progress in their dialogue, they may still face challenges. This policy paper organizes information on the current status of efforts in dialogue and related challenges, and discusses the actions that each party is expected to take to promote constructive dialogue going forward.

II. Progress in dialogue between companies and investors

The Japan Revitalization Strategy approved by Japan's Cabinet in June 2013 integrated the enhancement of corporate governance as an important element of the nation's growth strategy. Subsequently, measures have been taken for further development of the business environment including the formulation and revision of the Corporate Governance Code and the Stewardship Code. These steps set the stage for significant progress by Japanese corporate undertakings aimed at strengthening governance and by institutional investor-led activities aimed at fostering better stewardship, and also encouraged steady improvements in mutual dialogue.

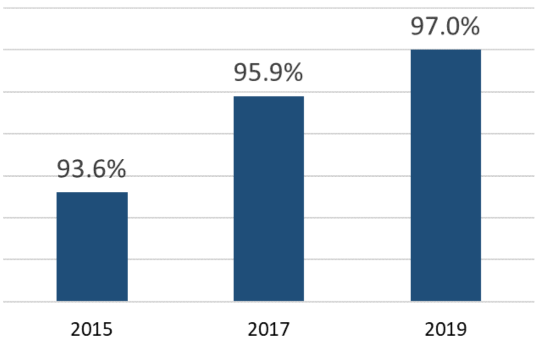
A recent Japan Investor Relations Association (JIRA) survey of corporate frameworks for dialogue with investors found that approximately 80 percent of publicly listed companies have dedicated investor relations departments and/or full-time IR personnel (Fig. 1). Additionally, it found that members of top management (company chairpersons, presidents, CEOs, and other executives with representation rights) were involved in the IR activities of over 90 percent of publicly listed firms (Fig. 2).

Fig. 1 Share of publicly listed companies with independent IR departments and/or IR personnel



Source: Chart prepared by Keidanren Secretariat with summary of findings from JIRA Fact-finding Survey on IR Activities (May 2020).

Fig. 2 Share of publicly listed companies with top management involvement in IR activities



Source: Chart prepared by Keidanren Secretariat with summary of findings from JIRA Fact-finding Survey on IR Activities (April 2019).

Further, steps were being taken to share information on investor views and resulting corporate responses to those views with all levels of management through internal reports and reports presented at meetings of boards of directors or management conferences (Figs. 3 and 4).

Fig. 3 Existence of mechanisms to share investor dialogue content across management hierarchy

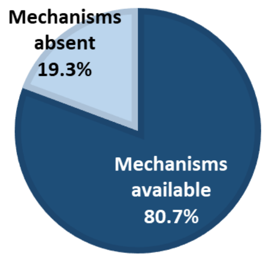
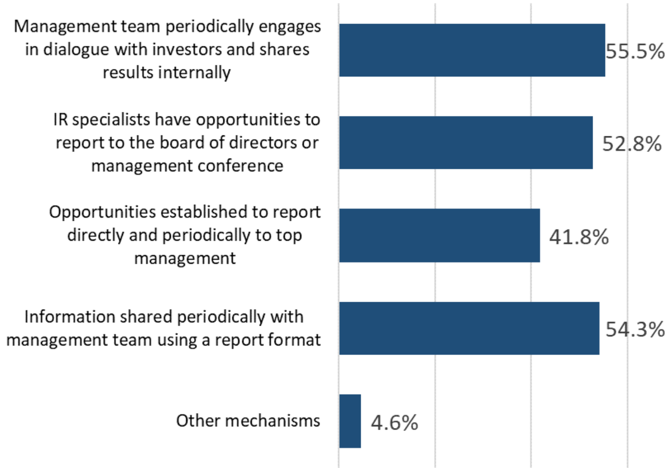


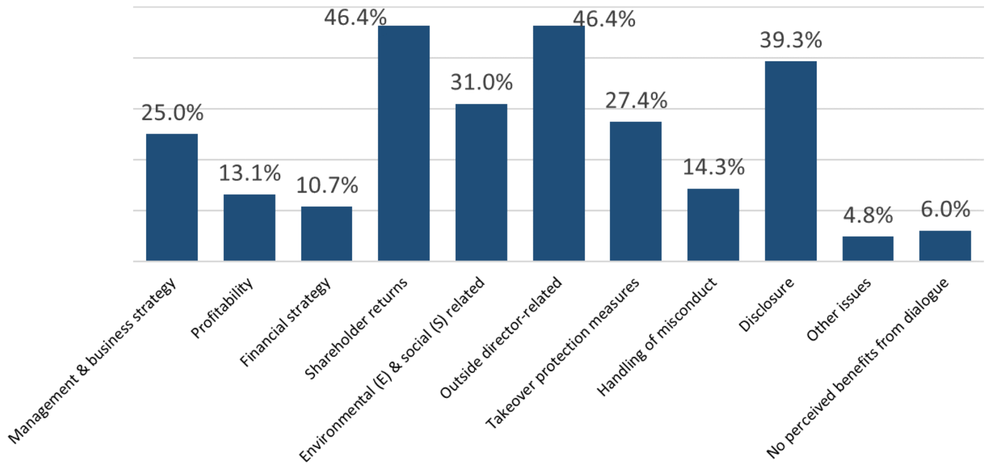
Fig. 4 Mechanisms to share investor dialogue content across management hierarchy



Source: Charts prepared by Keidanren Secretariat using data in list of aggregate results from Life Insurance Association of Japan questionnaire survey on measures to improve corporate value (fiscal 2019, for companies).

In response to corporate actions of this nature, many institutional investors now perceive that companies in their portfolios have shifted their views regarding outside directors (e.g., the number of outside directors, their independence, and attendance rates) as well as their policies on returns for shareholders and disclosure, and also feel the effectiveness of constructive dialogue with these companies (Fig. 5).

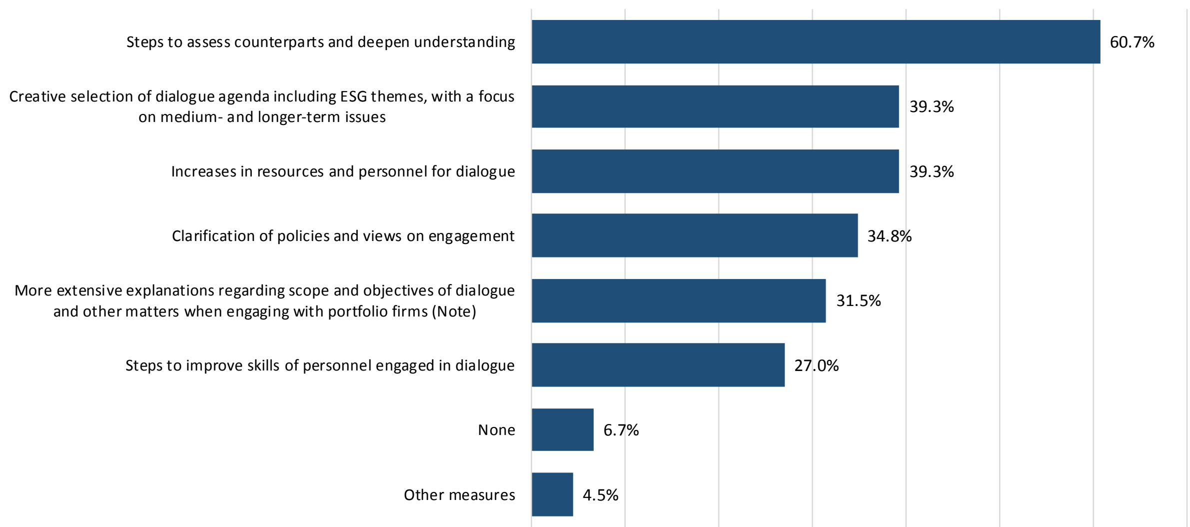
Fig. 5 Issues at portfolio companies perceived to have changed or benefited from effective dialogue as an outcome of stewardship activities



Source: Chart prepared by Keidanren Secretariat using data in list of aggregate results from Life Insurance Association of Japan questionnaire survey on measures to improve corporate value (fiscal 2019, for investors).

However, institutional investors have also been engaged in efforts aimed at improving the effectiveness of dialogue with their portfolio companies. Many have pursued measures not only to increase the frequency of dialogue but also to expand its scope and gauge actual conditions at the companies in their portfolios (Fig. 6).

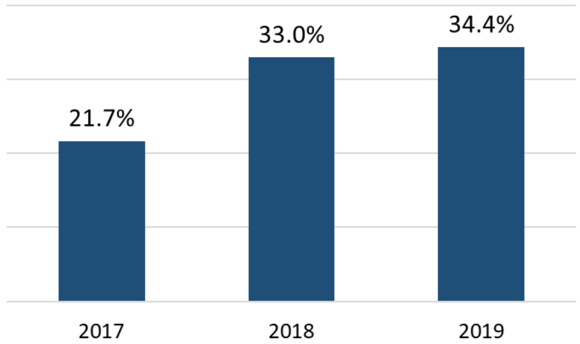
Fig. 6 Prioritized measures to improve the quality of dialogue, and future measures considered necessary to address recognized issues



Source: Chart prepared by Keidanren Secretariat using data in list of aggregate results from Life Insurance Association of Japan questionnaire survey on measures to improve corporate value (fiscal 2019, for investors).

In many instances, the outcomes of dialogue are reflected in the exercise of voting rights and other actions taken by institutional investors. According to surveys by the Japan Investment Advisers Association, the percentage of institutional investors and investment advisers that revise voting decisions on selected proposals after receiving explanations in advance from portfolio companies has risen year on year, and currently exceeds 30 percent (Fig. 7). Dialogue leads to the exercise of voting rights based on a better understanding of the purpose of proposals under consideration.

Fig. 7 Share of institutional investors and investment advisers that change their voting decisions in response to advance explanations from portfolio companies as a result of efforts in engagement



Source: Chart prepared by Keidanren Secretariat on the basis of findings from a Japan Investment Advisers Association questionnaire survey on compliance with Japan's Stewardship Code (sixth survey, conducted in October 2019).

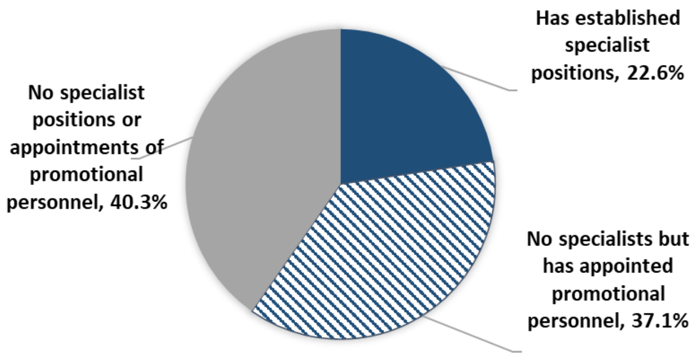
One idea that has permeated through Japan's corporate community for some time is that placing importance on the benefits for diverse stakeholders will translate into social contributions.[1]

Additionally, growing international interest in ESG investments in recent years has prompted companies and investors alike to move forward with the creation of frameworks to promote ESG-related disclosures and dialogue. For example, a survey by the Government Pension Investment Fund (GPIF) concerning the stewardship activities of institutional investors found that over 70 percent of the companies listed on the First Section of the Tokyo Stock Exchange engaged in the voluntary disclosure of

[1] The view that companies should exist for the benefit of society as a whole has been cited as an important element of Keidanren's Charter of Corporate Behavior since its establishment in 1991.

nonfinancial information including ESG themes, and that over 70 percent of all the companies had presented their investors with long-term visions.[2] For comparison, approximately 60 percent of institutional investors have established specialist positions for the promotion of ESG investment and financing (Fig. 8).

Fig. 8 Percentage of institutional investors that have created specialist positions for the promotion of ESG investment and financing



Source: Charts prepared by Keidanren Secretariat using data in list of aggregate results from Life Insurance Association of Japan questionnaire survey on measures to improve corporate value (fiscal 2019, for investors)

[2] Based on GPIF's Summary Report of the Fifth Survey of Listed Companies regarding Institutional Investor's Stewardship Activities (2020).

III. Actions required to foster constructive dialogue

Although efforts of this kind have shown a certain measure of success toward improving dialogue between companies and investors, various actions as described below will also be needed in order to achieve more effective levels of dialogue and enable companies to pursue gains in their value over the intermediate and longer term.

1. Full disclosure supporting constructive dialogue

First of all, corporate disclosure is the starting point for dialogue with investors. Although many companies in recent years have achieved qualitative and quantitative improvements in their disclosures of information, many investors still clamor for more complete disclosures.

To make medium- and long-term investment decisions, it is essential that investors have information that helps assess the future image of a company or its long-term vision. For example, in the context of statutory disclosures, the Cabinet Office Order on Disclosure of Corporate Affairs was revised in 2019 and now calls for corporate financial statements to include adequate descriptive information including information on management strategy and risk.

In response to this situation, members of the corporate community have noted that disclosures including voluntary disclosures through their annual reports will increase the clerical burdens and redundancy associated with ensuring the integrity of information that should be disclosed. Due to the broad-ranging nature of ESG-related information and the lack of established assessment criteria, in particular, some have raised concerns about the content, scope, and quality of information that should be disclosed.

In April 2019, Keidanren sent a mission to the US with the objective of promoting dialogue between corporate executives and foreign investors. Japan earned praise from

US institutional investors for the large number of Japanese organizations and companies that had become supporters of the Task Force on Climate-related Financial Disclosures (TCFD)[3] and also for the measure of progress Japanese companies had made with their disclosures of ESG information. Meanwhile, the US investors also cited deficiencies with the disclosure of basic information on matters such as the membership and roles of nomination and compensation committees, and suggested that disclosures should be made with a stronger awareness of the materiality and priority of their content.[4]

With that realization and in light of the expectations of materiality and priority, more Japanese companies look past the formalities, are mindful of the importance of constructive dialogue with their investors, and voluntarily adopt policies of full disclosure. That stance can be expected to win deeper levels of investor acceptance and understanding. As manifestations of this commitment, an increasing number of companies in recent years have followed the "comply or explain" principle in their corporate governance-related reports, choosing to explain circumstances that are not in compliance with the Corporate Governance Code. Additionally, others have applied a "comply and explain" policy, including explanatory details in their reports even when they are code-compliant. Further, some companies have resourcefully integrated charts and figures into their reports on business performance for their investors, providing forecasts of future performance under varying coronavirus pandemic scenarios.

Disclosure and dialogue are mutually complementary. The process of utilizing dialogue to clarify investor expectations regarding matters for disclosure is also important. Institutional investors and especially those active at the global level hold equity stakes in other companies in the same industry as well as related fields in Japan and abroad, and are engaged in dialogue with each portfolio company on a continuing

[3] A total of 285 organizations and companies in Japan have become supporters of the TCFD, the largest number from any single nation (based on data posted on the TCFD Consortium website as of June 26, 2020).

[4] From Keidanren's report, "Outline of the mission to the US for constructive dialogue with investors (May 2019)."

basis. Through this dialogue with institutional investors, portfolio companies are better able to determine what information they should disclose.

2. Pursuing a virtuous cycle of qualitatively advanced dialogue

In their dialogues with investors to date, many companies have noted that the process has had a tendency to devolve into little more than a one-sided response to investor questions. Investors, on the other hand, have drawn the impression that their corporate counterparts in such dialogues tend to assume a defensive posture that undermines the development of more flexible discussions. To achieve more constructive dialogue, it is advisable that companies and investors reciprocally deepen their understanding of each other's concerns and objectives, and accordingly set the stage for a virtuous cycle of qualitatively improved level of dialogue.

Almost 40 percent of institutional investors have cited a lack of feedback from their portfolio companies regarding responses to the content of their dialogues.[5] Unless investors are able to discern the actions a company may pursue in response to dialogue, their discussions may be limited to little more than a transient, one-sided articulation of investor viewpoints. Companies need to be more forthcoming with the feedback they provide investors regarding any changes in their policies or actions that are based on the results of dialogue. To that end, it will be important for companies to step up management's direct involvement in dialogues with investors and demonstrate a unified company stance, provide their boards of directors with reports detailing dialogue content, and in other ways cultivate an organic framework that facilitates tangible changes in corporate behavior.

Nevertheless, some companies still question whether the constructive dialogues they hold with their investors have actually led to investments from a long-term perspective

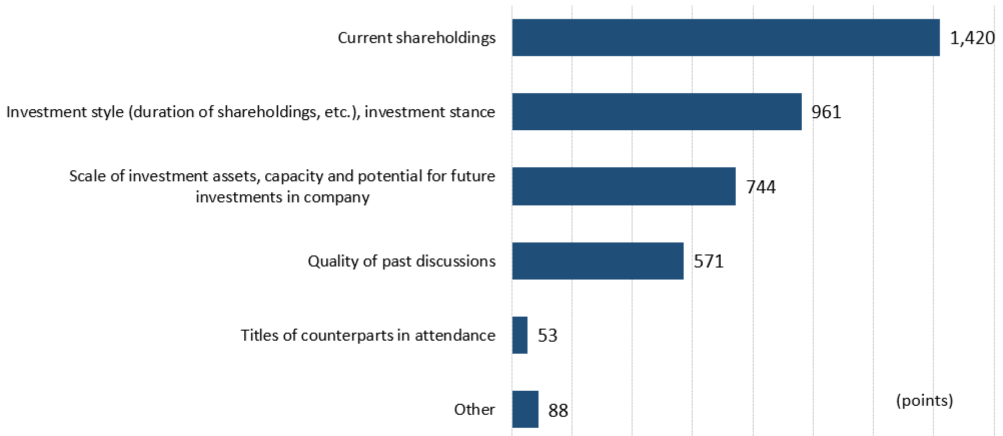
[5] Based on findings from a Japan Investment Advisers Association questionnaire survey on compliance with Japan's Stewardship Code (sixth survey, conducted in October 2019).

or influenced investor voting decisions.

It is important that investors clearly inform their portfolio companies about the value they place on dialogue as one of a series of processes that lead to investment decisions and the exercise of their voting rights, and that they encourage continued dialogue by actively providing their corporate counterparts with feedback on the decisions they have made as a result of dialogue. More and more institutional investors have established specialist positions for ESG-related analytical duties. Accordingly, internal collaboration by their departments for active and passive fund allocation, the exercise of voting rights, ESG assessments, and other operations will be extremely important in terms of assuring that the exercise of their voting rights is linked with the outcomes of dialogue on medium and long-term themes.

Many companies now select delegates for IR meetings with attention not only to investors' current shareholdings but also to their investment stance (Fig. 9). However, because the investment strategies and stances of different institutional investors are varied, more productive and constructive dialogue can be expected if an investor clarifies their stance in advance and on that basis selects clear themes and objectives for discussion—for example, important business challenges facing the counterpart company.

Fig. 9 How companies determine the importance of IR meetings (selection criteria for attendees, etc.)



Note: Respondents selected their three most important criteria. The top-ranked criteria counted as three points, the second-ranked as two points, and the third-ranked as one point. Bars in the chart show the point total for each criterion, obtained by aggregating the rank-weighted points multiplied by the numbers of respondents.

Source: Chart prepared by Keidanren Secretariat with GPIF's Summary Report of the Fifth Survey of Listed Companies regarding Institutional Investor's Stewardship Activities (2020).

Furthermore, given the strengthened need to identify beneficial shareholders (shareholders not on shareholder lists but who have the right to purchase shares and vote) for the purposes of dialogue, it is advisable to explore the creation of frameworks or systems that will make that identification process possible. Some companies perform shareholder determination surveys to identify beneficial shareholders not named in shareholder lists. Portfolio companies could be expected to foster smoother dialogue with institutional investors if they were able to gain insights into investors' circumstances (names of beneficial shareholders, the number of shares they own, etc.) without incurring those survey costs.[6]

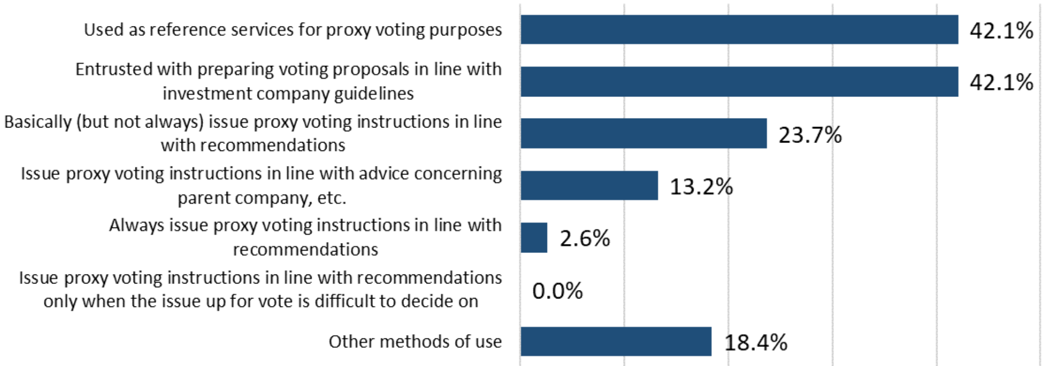
3. Appropriate utilization of proxy voting adviser functions

With the expansion trend in passive investing in recent years, proxy voting advisers now exert a heightened influence over the voting activities of institutional investors. According to a survey by the Japan Investment Advisers Association, over 30 percent of investment managers in Japan currently utilize the services of advisory institutions for

[6] Supplementary Principle 5.1.3 in the revised (June 2018) Corporate Governance Code states: "Companies should endeavor to identify their shareholder ownership structure as necessary, and it is desirable for shareholders to cooperate as much as possible in this process."

their proxy voting instructions.[7] Such institutions are most commonly utilized as reference services for proxy voting purposes, or entrusted with the task of preparing voting proposals in line with investment company guidelines (Fig. 10).

Fig. 10 How institutional investors utilize proxy advisers



Source: Chart prepared by Keidanren Secretariat on the basis of findings from a Japan Investment Advisers Association questionnaire survey on compliance with Japan's Stewardship Code (sixth survey, conducted in October 2019).

Recommendations from proxy voting advisers are to a certain extent prepared in line with institutional investor needs. If used properly, they can supplement institutional investor resources. However, portfolio companies have cited a number of issues with proxy voting adviser services: (1) the formulation process for proxy advisory guidelines lacks transparency and the study framework is inadequate; (2) proxy advisory guidelines are applied in a uniform, formalistic manner, sometimes leading to inappropriate proxy voting recommendations based on views not shared by the portfolio company; and (3) illogical recommendations are sometimes made regarding specifics that are not covered by proxy advisory guidelines.

This situation could encourage approaches to corporate governance that only satisfy proxy advisory guidelines in a formal sense. Furthermore, if a proxy vote is exercised in line with recommendations that are not based on adequate information, it could have an adverse impact not only on the portfolio company in question, but also on the investors

[7] Based on findings from a Japan Investment Advisers Association questionnaire survey on compliance with Japan's Stewardship Code (sixth survey, conducted in October 2019).

interested in boosting that company's medium- and long-term value as well as the asset owners to which the investment manager has fiduciary duties, and also would pose a risk to healthy market functions.

Reflecting this backdrop, the Stewardship Code as revised in March 2020 assigns importance to proxy voting advisers and other providers of services to institutional investors as contributors to the improved function of the investment chain as a whole, and on that basis mandates that proxy voting advisers develop their personnel and organizational frameworks, improve the transparency of their processes for the formulation of recommendations, and actively exchange views and opinions with portfolio companies as necessary.[8] Compliance with this Stewardship Code is required. Additionally, institutional investors are expected to reflect these perspectives in their selection and use of proxy voting advisers and pursue dialogue with said advisers as appropriate with attention to information obtained through their own dialogues with portfolio companies. Efforts to improve the advisory functions of these services will lead to the advancement of the investment chain as a whole. The efforts of asset owners also will be of value to the task of boosting the effectiveness of dialogue between portfolio companies and investment managers. For example, if asset owners evaluate the proxy voting of investment managers on the basis of their "no" vote ratios and other formalistic guidelines, that may only encourage a formalistic response by investment managers. As responsible members of the investment chain, asset owners should encourage investment managers to engage in effective stewardship activities.

4. The utilization of digital technology

Although many Japanese companies have continued with their efforts to spread their general shareholder meetings across a broader range of calendar dates, the timing for dialogue on pending proposals still tends to concentrate within a narrower time frame.

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[8] Financial Services Agency, Japan's Stewardship Code (March 2020), Principle 8, Guidances 8-2 and 8-3.

This has been cited as a factor that adds to the practical difficulty of studying proposals in detail, but also as a background factor behind the increasingly rigid utilization of proxy voting advisers by institutional investors.

In recent years, more and more companies have shifted to web-based postings of notices of convocation and related documentation for their shareholder meetings. However, the revised Companies Act enacted last year mandates that publicly listed companies release digital versions of their documentation for general shareholder meetings no later than three weeks prior to their scheduled dates for those events.[9] Furthermore, after the revised Companies Act goes into effect, regulations for financial instrument exchanges will be expected to incorporate provisions mandating efforts for even earlier releases of digital documentation. These regulatory changes will allow investors more time to study pending proposals than is possible under the current framework. Also, as a provisional measure effective this year, legal revisions by the Ministry of Justice recognized web-based disclosures of unconsolidated balance sheets and statements of profit and loss as meeting mandated submission requirements. Allowing this treatment to remain effective next year and thereafter in the interim leading up to the implementation of revised provisions in the Companies Act governing digital submissions will enable early submissions of unconsolidated financial documents and other important documentation. Additionally, countermeasures against the coronavirus pandemic have prompted many companies to move ahead with plans to hold hybrid virtual shareholder meetings. Virtual meetings have merit because they will complement pandemic countermeasures and facilitate remote participation in multiple shareholder meetings. It is anticipated efforts of this nature to boost the effectiveness of dialogue through efficiency gains provided by the utilization of digital technology will gain even more traction in the years ahead.

[9] Documentation for general shareholder meetings potentially might not be submitted at least two weeks prior to a scheduled meeting date, the deadline for issuance of convocation notices under current law.

More companies are also moving to adopt electronic proxy voting platforms for institutional investors. Over 1,000 companies already participate on the electronic proxy voting platform of Investor Communications Japan (ICJ, Inc.), a joint-venture of Broadridge Financial Solutions, Inc. of the US and the Tokyo Stock Exchange, Inc.[10] One advantage of this platform is that it allows companies to devote more time to studying pending proposals in detail.

However, not many institutional investors in Japan utilize these electronic proxy voting platforms yet. Although over 90 percent of all institutional investors in the US and UK now utilize electronic proxy voting services,[11] as of October 2019 no more than 12.8 percent of institutional investors (with outstanding investment balances in Japanese stocks) in Japan utilized such online platforms for proxy voting purposes.[12, 13]

The utilization of electronic proxy voting platforms allows companies to confirm proxy voting instructions from institutional investors in a more timely manner, but that is not the only advantage. One benefit for institutional investors is that they have the opportunity to study information on pending proposals at an earlier date and can engage in such study for an extended period of time, right up to the date just prior to scheduled shareholder meetings (Fig. 11). Portfolio companies and institutional investors alike can also utilize this extended period for further dialogue.

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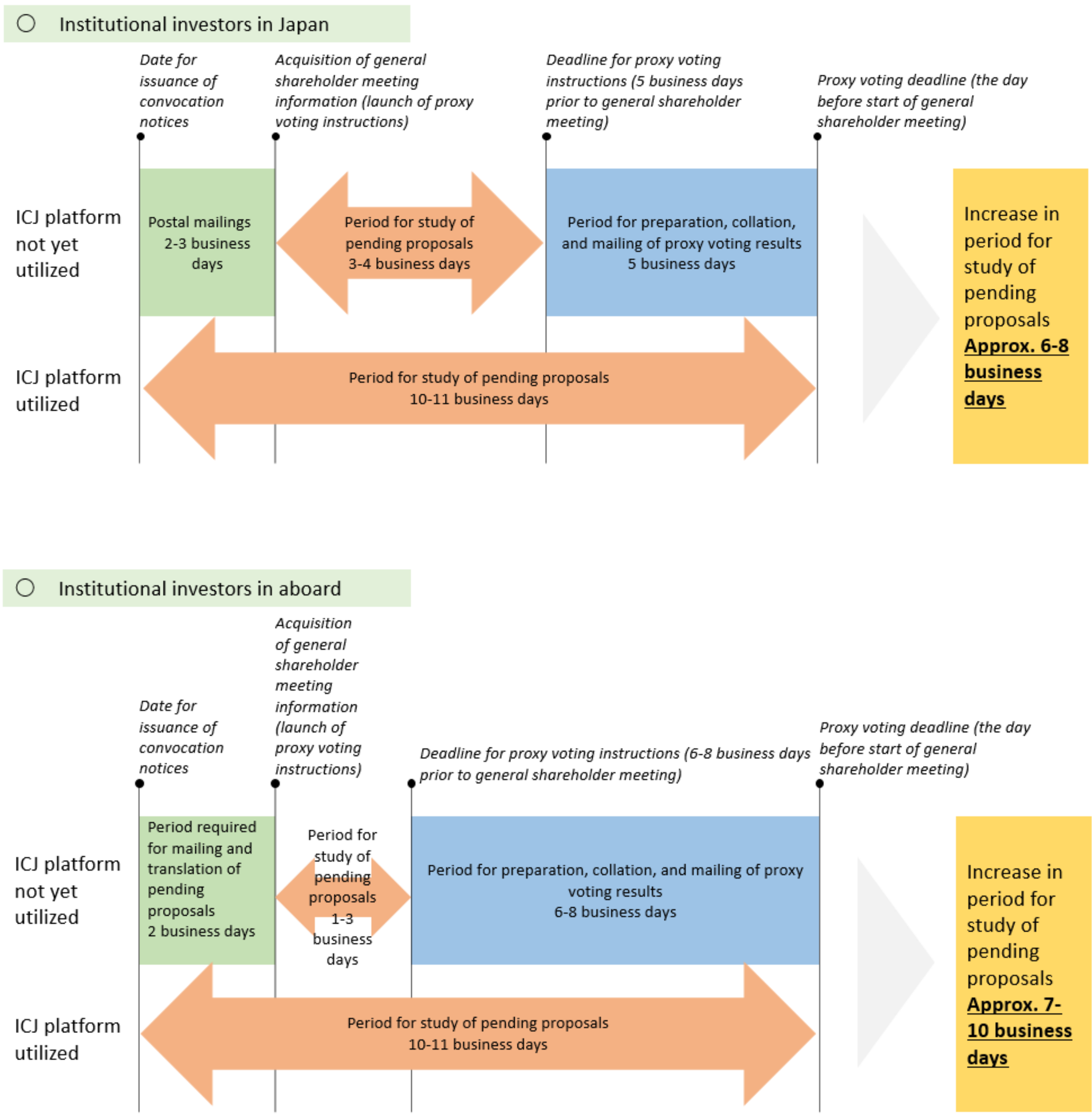
[10] Information on ICJ, Inc. website
[11] From Ministry of Economy, Trade and Industry study group reports on promoting digitization of general shareholder meeting-related processes (2016).
[12] Findings from a Japan Investment Advisers Association questionnaire survey on compliance with Japan's Stewardship Code (sixth survey, conducted in October 2019).
[13] Efforts to inter-link the platforms offered by different companies have recently gained momentum. The systems for the ICJ platform and the ProxyExchange platform run by the proxy voting adviser ISS have been linked together (information from ICJ website).

Fig. 11 Periods for study of pending proposals extended through use of ICJ's electronic proxy voting platform



Source: Excerpted from Ministry of Economy, Trade and Industry study group reports on promoting digitization of general shareholder meeting-related processes (2016).

Several factors may be cited to explain the lack of progress toward utilization of online proxy voting platforms. One is the burden of back-office processing involved to prepare paper-based and digitally based documentation due to the fact that such online platforms are not yet universally utilized by all companies. Additionally, in some cases, investment managers are obligated to obtain the consent of asset owners when they intend to utilize such platforms. Yet another factor is the heavy cost burden that companies may incur. In the interest of achieving more effective and productive dialogue, cross-sectoral initiatives backed by the sharing of best practices will be crucial, especially to encourage broader utilization of proxy platforms by institutional investors.

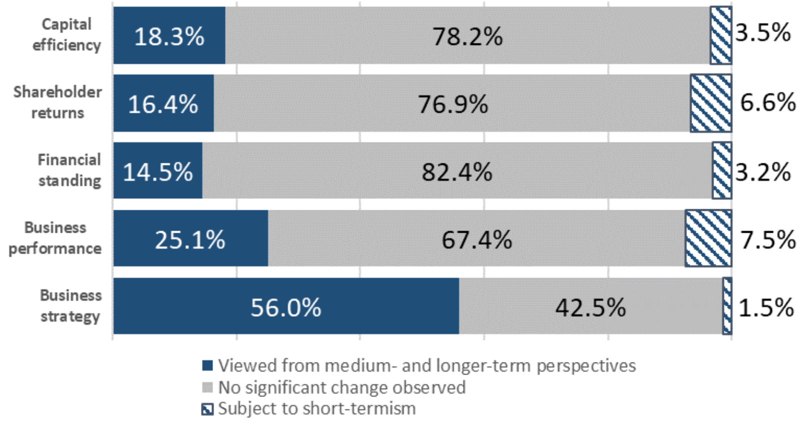
Recent times have witnessed a surge in modalities available for online dialogue. These have significantly mitigated the time and space constraints that such dialogue formerly faced. Efforts should be made to expand the potential for dialogue through the resourceful utilization of online platforms not only to help investors that face constraints on in-person assembly due to coronavirus-related countermeasures, but also for the purposes of dialogue with physically distant investors or collaborative engagement when dialogue with multiple institutional investors is a necessity. Utilizing online modalities for dialogue not only just prior to general shareholder meetings but on a continuous basis throughout the year will help improve the effectiveness of dialogue as well as facilitate proxy voting based on it. It is advisable that all parties take such opportunities as revisions to proxy voting guidelines for institutional investors and the corporate releases of integrated financial reports to further expand the opportunities for dialogue outside the time frames usually set for general shareholder meetings.

5. Dialogue based on longer-term perspectives

(1) Presenting long-term visions and value-creation stories

In the IR meetings they have held in recent years, many companies have assumed their timelines for discussions with institutional investors and particularly discussions concerned with business strategy were based on medium and longer-term perspectives (Fig. 12).

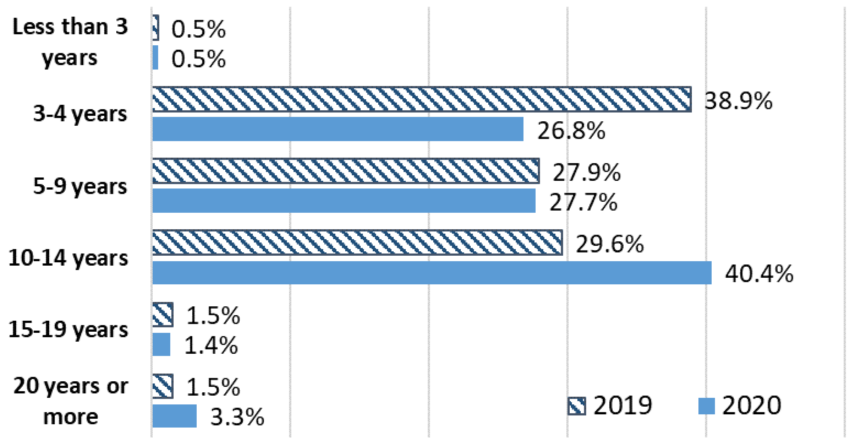
Fig. 12 Timelines for discussions of individual topics with institutional investors at IR meetings



Source: Chart prepared by Keidanren Secretariat with excerpted material from GPIF's Summary Report of the Fourth Survey of Listed Companies regarding Institutional Investor's Stewardship Activities (2019).

As noted earlier, over 70 percent of portfolio companies set out long-term visions during their dialogues with institutional investors. However, many of those companies have set periods of around three to five years for their long-term visions—a timeline customarily associated with medium-term business plans. To achieve constructive engagement with investors on the basis of business strategies that extend over longer periods of time, it will be advisable for companies to formulate and present long-term visions of their future business in increments not of years, but of decades. Actually, rapidly increasing numbers of companies have very recently begun formulating long-term visions that stretch out over longer periods (Fig. 13). It is anticipated this trend will gain additional momentum in the future.

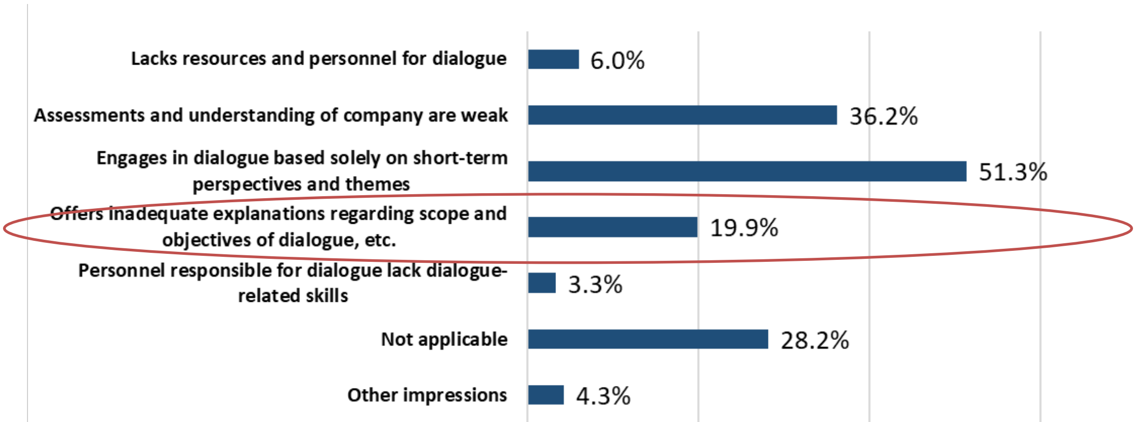
Fig. 13 Estimated timelines for long-term visions that listed companies present to institutional investors



Source: Chart prepared by Keidanren Secretariat on the basis of GPIF's Summary Report of the Fifth Survey of Listed Companies regarding Institutional Investor's Stewardship Activities (2020).

Meanwhile, as a survey by the Life Insurance Association of Japan discovered, a significant share of corporate respondents feel that institutional investors still prefer to deal solely with short-term themes during their dialogues (Fig. 14). Although institutional investors apply varying investment strategies, in the interest of boosting their own profits by promoting the sustained growth of their portfolio companies, it is hoped they will place more weight on dialogues that are anchored in medium- and long-term perspectives.

Fig. 14 Corporate impressions of investors during dialogues



Source: Chart prepared by Keidanren Secretariat using data in list of aggregate results from Life Insurance Association of Japan questionnaire survey on measures to improve corporate value (fiscal 2019, for companies).

Additionally, one survey found that over 70 percent of investment managers had not received any ESG mandates (for ESG-indexed investments or the development of portfolios containing issues with favorable ESG elements) from client asset owners.[14] To foster improved dialogue between companies and institutional investors from a medium- and longer-term perspective, it is hoped that asset owners will evaluate investment managers from a variety of vantage points including ESG themes.[15]

[14] Findings from a Japan Investment Advisers Association questionnaire survey on compliance with Japan's Stewardship Code (sixth survey, conducted in October 2019).

[15] In a joint research report released by Keidanren, the University of Tokyo, and the GPIF, the GPIF presented five action plans including consideration of incorporating Society 5.0 and SDGs into investment principles and the like and promoting constructive engagement and conducting research on appropriate evaluation methods to connect ESG with Society 5.0 (from "The Evolution of ESG Investment, Realization of Society 5.0, and Achievement of SDGs—Promotion of Investment in Problem-solving Innovation" [March 2020]).

When explaining their long-term visions to institutional investors, many companies experience difficulty despite the importance of presenting clear stories oriented toward value creation as well as connections between the generation of long-term cash-flow and nonfinancial information, including ESG themes.[16]

Keidanren, the University of Tokyo, and the GPIF have released in March 2020 a joint research report that is aimed at contributing to the achievement of the “Society 5.0 for SDGs” vision through advances in the field of ESG investment. That report analyzed elements in long-term visions presented by companies and assessed their effectiveness in giving an impression of growth potential to investors. Three elements in particular earned high marks: business development based on “people”; solving global issues; and the creation of new markets. Drawing from these findings, companies gained an understanding that they should formulate long-term visions that would appeal to investors by focusing on those three elements.[17]

Another point from the corporate perspective was that many questions raised by institutional investors during dialogues on ESG themes were for the purpose of negative screening. Rather than scrutinizing future corporate images or visions for negative factors, steps should be taken to explore ways of advancing ESG investments that lead to sustainable growth or otherwise allow companies and institutional investors alike to engage in assessments backed by positive dialogue.

(2) International frameworks for disclosure and assessment methods

Recent years have brought a proliferation of opportunities to assess ESG-related

[16] According to JIRA Fact-finding Survey on IR Activities (April 2020), “presenting investors with ESG-related viewpoints or positions as straightforward information in the context of medium- and long-term business strategies” was the task that the largest share of respondent companies considered difficult in relation to disclosure and dialogue regarding nonfinancial information (including ESG themes).

[17] Using a questionnaire format, the analysis collected data on the types of long-term visions companies had in mind and subjected that data to natural language processing. For further information, see “The Evolution of ESG Investment, Realization of Society 5.0, and Achievement of SDGs,” a joint research report released in March 2020 by Keidanren, the University of Tokyo, and the GPIF.

undertakings and tie them to new investments. In the process, a diversity of institutions and organizations at the international level have issued a range of varying guidelines on methods for the disclosure of nonfinancial information including information on ESG themes. Moreover, efforts to strategically institutionalize environmental undertakings at the national and regional levels are gaining momentum.

In Japan, companies have for some time been engaged in independent projects aimed at showing more consideration for their diverse stakeholders and achieving sustainable growth. However, many of those companies feel perplexed by the prospect of having to explain their projects within the applicable context of a new framework. Against this backdrop, several private companies have joined together and launched studies focused on proper approaches to ESG information disclosure and engagement with attention to the salient features of the Japanese setting.

Principally, ESG projects and other corporate-led undertakings should be flexibly defined in terms of the ideals and business operations of the companies. Meanwhile, as different standards and guidelines exist, companies are facing the burden of deciding which set of standards to meet or satisfying multiple standards. In their dialogues, it is advisable that companies and investors specify those things that bear materiality and on that basis strive to organize and consolidate assorted standards and guidelines into an international framework.

It would be desirable for members of the corporate sector, under this framework, to engage in disclosures that apply to each company while continuing to demonstrate ingenuity of their own. From the standpoint of utilizing information, to investors the idea of having a fixed framework for methods of disclosure would assure the comparability of disclosed corporate information as well as promote its effective use. Assessments of that information by investors with diverse values will ultimately improve the efficiency of undertakings led by society as a whole.

Japan should actively participate and assume the lead in discussions aimed at developing international frameworks and standards for disclosures and assessment methodologies that will contribute to the achievement of ESG mandates as well as the SDGs.

IV. Concluding remarks

In terms of realizing Society 5.0, a vision aimed at solving social challenges and creating new value through the digital transformation, efforts in constructive dialogue (engagement) by corporations and investors will be instrumental to the development of a virtuous cycle for investments in the Society 5.0 domain and the corporate-led creation of new value. It is imperative that companies look beyond pure compliance with formal frameworks for disclosure and take the initiative to pursue constructive dialogue with investors by applying their ingenuity and actively involving their top management in the process. Investors, too, should adopt medium- and long-term perspectives and on that basis assume the initiative in dialogues with their corporate counterparts. Additionally, they should strive to build a virtuous cycle for constructive dialogue through active feedback explaining the decisions they arrive at as a result of dialogue. In the near term, there have been signs that meetings between investors and companies that had been restricted by the coronavirus pandemic will begin moving toward a gradual reopening while improvising and integrating measures to avoid the "three Cs" (closed spaces, crowded places, and close-contact settings). Going forward, it is anticipated they will build even deeper relationships during the engagement process by flexibly adapting to a variety of likely environmental changes.

In response to the expanding coronavirus pandemic, Keidanren itself plans to take advantage of the opportunities created by the utilization of online conferencing tools and the promotion of varied dialogue strategies, collect data on advanced cases, and disseminate information to its member companies. Additionally, in the interest of promoting improvements in constructive dialogue, it will continue to actively exchange views and opinions with investment managers, asset owners, proxy voting advisers, and investors in Japan and abroad.

Keidanren (Japan Business Federation) is a comprehensive economic organization with a membership comprised of more than 1,500 representative companies, nationwide industrial associations, and regional economic organizations of Japan.

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