Mizuho Custody Newsletter

February 2022 | Japan

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I. Market News

1. The government plan to establish a panel of experts to support startups

The Government of Japan plans to establish a panel of experts to support startups in February, reports Nikkei Shimbun, Japan's leading financial daily. They will seek ways to create an environment that is supportive for startups to grow, such as enhancing flexibility in unlisted stocks trading. They plan to compile a report by this summer.

The panel of experts will be established in the Cabinet Office. The panel is supposed to consist of those from related ministries and agencies, such as the Ministry of Economy, Trade and Industry (METI) and Financial Services Agency (FSA), in addition to those with experiences of starting up new businesses.

The report by the panel will be reflected into the "five-year startup plan" that the government will institute.

It has been pointed out that startups are less likely to grow in Japan than in the United States and Europe. The panel will discuss mainly on the following issues for breakthrough: (1) few institutional investors invest in venture capital ("VC"); (2) the amount and size of VC investments are small; and (3) the market for unlisted stocks is underdeveloped.

In principle, the rules set by Japan Securities Dealers Association (JSDA) prohibit to solicit ordinary investors to trade unlisted stocks. Such unlisted startups rely on bank loans as their main financial sources. Under the circumstances, ways to make long-term investments in those companies to spur their growth are very scarce.

According to the material prepared by the Cabinet Office, institutional investors account for only 5% of investment towards VC in Japan, compared to 75% in the U.S. The amounts invested per VC are small and they have few people with expertise in this field.

At a press conference at the beginning of the year, the Prime Minister Fumio Kishida announced that the year 2022 was the year that the government started to support many more startups to come out and that the government would put together the five-year plan. He said he would work on various aspects in this regard such as strengthening the supply of risk money, including public investment, and reviewing the initial public offering system.

The urgent recommendations prepared by the "Council of New Form of Capitalism Realization", which discusses important policies of the Kishida administration also touched upon startups.

The recommendation describes that the number of startups has been recently on the rise, but only 13.9% of the companies are 0-2 years old in Japan, which is lower than that of the U.S. (20.5%), the UK (22.4%) and France (22.8%).

It also mentions that very small number of startups have grown up to a certain level of market capitalization in Japan. As of 1 March 2021, there were 274 unicorns (non-public companies with market capitalization with more than USD 1 billion) in the United States, 123 in the People's Republic of China, and 67 in Europe, while there were only 4 in Japan.

Information compiled from Cabinet Secretariat, Nikkei Shimbun &

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Mizuho research

2. The government plan to prepare an information disclosure guidelines on human capital for corporates

The government plans to prepare information disclosure guidelines on human capital for corporates as early as this summer, reports Nikkei Shimbun, Japan's leading financial daily. Content of the disclosure, such as employee diversity and personnel training, will be discussed at a professional meeting. The ability and knowledge of workers are recognized as capital for generating new ideas, and investors are interested in them as factors that influence competitiveness and corporate value. Companies in Europe and the United States are leading the way, and they use the disclosure policy as a leverage to enhance companies' human resources strategies.

The Cabinet Secretariat will set up a professional meeting in February to specifically research items and evaluation methods for disclosure. They also plan to work with the Financial Services Agency ("FSA") with a view to obligate listed companies to describe them in their securities reports in the future.

Ratio of female and foreign employees and information on mid-career employees are also being considered as items to be disclosed. As for personnel training, policy of reskilling (relearning) and opportunities for learning outside the company will be potential items for disclosure. Measures to prevent harassment could also be one of them. The government intends to establish a mechanism that investment goes to companies that are willing to work for information disclosure on human capital, which could eventually enhance competitive edge of Japanese companies.

As for disclosure on human capital, companies in the United States and Europe are ahead of the rest of the world. The United States obligated information disclosure in this regard to companies in August 2020. There are examples of disclosure going so far as to delve into turnover rates and wages by gender and race. The European Union (EU) issued a directive in 2014 to obligate disclosure on "society and employees" for companies of a certain size. The United Kingdom, Hong Kong and India also require disclosure on human investment and human rights protection.

As digitization of the economy accelerates, know-hows and ideas owned by individuals have been valued more than ever. According to an intellectual property advisory service company in the United States, intangible assets accounted for 90% of corporate value for major companies in the United States in 2020, while it was only 32% in Japan.

According to a professor at a university in Japan, Japanese companies spent an average of 0.34% of their gross domestic product (GDP) on human resource development in the 2010s, which is lower than 1.86% in the United States and 1.34% in Germany.

Another issue on this subject in Japan is that human resources strategy does not weigh so heavily in company management. According to a survey of more than 600 companies conducted by a research firm in 2021, only 11% of the companies said their human resources department were "involved" in management decision-making, and 34% said they were "involved, if anything." According to a research firm in the United States, the percentage of "employees with enthusiasm" was only 5% in Japan, which there was a big difference to 34% in the United States and Canada and 20% globally.

Tokyo Stock Exchange ("TSE") and FSA decided to include companies' policies and targets to ensure diversity of employees at managerial positions in companies' disclosure documents in the Corporate Governance Code ("Code") revised in June 2021. As of December 2021, 67% of the companies listed on the TSE 1st Section and 46% of those listed on the TSE 2nd Section met this requirement. Among the 100 major companies listed on the TSE 1st Section, 86 companies presented a target for women to be promoted to managerial positions, but there were only 22 companies showing that for foreigners, and 21 companies showing that for mid-career employees.

Among 83 items contained in the Code, only a few of them calls for disclosure of human capital. In the governmental guideline, details of disclosure items specialized in human capital will be defined. Under the Code, companies are not required to disclose them if they explain reasons of non-compliance, but the government is viewing to make the disclosure compulsory in the future. Within the FSA, the Financial System Council has been making studies on

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new statutory disclosure items, including climate change, since September 2021, and will cooperate with the professional meeting of the Cabinet Secretariat.

Information compiled from Nikkei Shimbun & Mizuho research

3. FSA start discussion on quarterly disclosures

Financial Services Agency ("FSA") started a discussion on quarterly disclosures in which companies announce their financial performance every three months. It comes after the Prime Minister Fumio Kishida, who calls for a "new capitalism," announced a policy to review and take drastic measures against the market seeking for short-term gains, reports Nikkei Shimbun, Japan's leading financial daily. The United States retain quarterly disclosure system, while in Europe, even after the abolition of the legal requirement of quarterly disclosures, most companies continue to do so.

Review on companies' quarterly disclosures is one of the policies the Prime Minister publicized when he announced his candidacy for the presidency of the Liberal Democratic Party in August 2021. When the Prime Minister made his policy speech at the Diet in October, he said he would promote improvement of the market environment, such as enhancing non-financial information disclosures and reviewing quarterly disclosure requirement. In response to this, the FSA started discussions on quarterly disclosures at a working group of the Financial System Council.

Japan's quarterly disclosure practice became applicable to the listed companies by the rules set by the Tokyo Stock Exchange (TSE) in 1999, and was made mandatory by the Financial Instruments and Exchange Act established in 2008. It aimed at enhancing transparency of company management by providing timely disclosures of financial information to investors, as environmental changes surrounding the companies have been getting tough.

The global trend is quarterly disclosures. In the United States, it was introduced in 1970, and the former President Donald Trump made a request to the Securities and Exchange Commission (SEC) to review the legal disclosure requirement in 2018, but after that, the discussions on the issue evaporated. In Germany, legal requirement was abolished in 2015, but the stock exchange maintains the requirement in its rules. The UK and France abolished their legal requirement in 2014 and 2015, respectively, but most companies still continue quarterly disclosures.

In October 2021, the CEO of Japan Exchange Group, Inc. (JPX) said, "Even if the quarterly disclosure obligation was abolished, most listed companies would likely to continue it," denying the view that quarterly disclosures encourage companies to focus too much on short-term results. Many investors express their concern about widening of information gap. The FSA plans to compile the result of the discussions in a report by this spring.

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

4. METI announce a basic concept to establish CO_2 emissions trading market

The Ministry of Economy, Trade and Industry ("METI") announced its basic concept for establishment of a market where companies can trade carbon dioxide ("CO_2") emissions, reports Nikkei Shimbun, Japan's leading financial daily. It aims to reduce emissions, but companies' participation is voluntary and there are no penalties for companies failing to meet their emission reduction targets. As opposed to Europe, where companies are obligated to reduce greenhouse gas emissions by showing the amount that they may emit, it is a challenge for participants how they can make the market actually work. It is not clear how the participation of companies to the market can make difference, if they do not have clear goals about the emission.

It is called "carbon pricing" to make efforts to reduce CO_2 emissions by pricing them. Emissions trading and carbon taxes, which are levied on companies based on their emissions, are the mainstream on this subject in the world. METI and the Ministry of the Environment ("MOE") have studied these efforts respectively towards a full-scale introduction.

In January, Prime Minister Fumio Kishida directed to explore carbon pricing in preparation to formulate "clean energy strategy" this summer, with a view to promote economic growth through making efforts for decarbonization. Although the whole picture is still

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unclear, METI aims to start emissions trading in advance on a full-scale in April 2023.

In the concept announced on 1 February, “GX (Green Transformation) league”, a structure that constitute of companies working on decarbonization, will be established, and participants to the league are allowed to trade emissions.　The government plans to institute details of the market structure with companies that are willing to support the concept, and to make a trial this autumn.

Participating companies will set interim reduction targets in 2023-2030 and they can sell the amount they reduced more than their targets in the market.　The government has set a goal to reduce greenhouse gas emissions in FY2030 by more than 46% compared to that in FY2013.　Companies will be asked to set targets above this level.

If participants fail to achieve their target, they will have to buy the amount lacked to achieve the target in the market.　However, there will be no penalties for not purchasing emissions and failing to meet the targets. This appears to be special considerations for the industries that are cautious about uniform regulations.

A professor at a graduate school said, "Companies are not required to buy emissions in the market because it is not a regulation.　The market does not seem to work actually to reduce emissions."　For companies that have not set their reduction targets, participation to the program seems to mean very little to them.

METI list up conditions to participate in the program such as (1) to achieve decarbonization in 2050, (2) to set emission reduction targets for 2030 and announce progress every year, and (3) to support decarbonization of their parts suppliers.

According to METI, more than 200 Japanese companies plan to achieve decarbonation by 2050, which include major companies such as steelmakers, power and oil industry with high emissions.　If all of these companies actually participate, it will cover around 50% of Japan's total energy-related emissions.

While it is not controlled by regulations, the government seems to be counting on pressure from the financial sector as they are enhancing ESG investments.　The government will also consider giving preferential treatment to companies that actively promoted decarbonization through emissions trading or other means, such as subsidies or government procurement to encourage participation.

METI is aware of concerns over effectiveness of the program.　The basic concept also refers to the possibility of shifting it to regulations, such as mandatory participation, if it finds efforts are insufficient.

In emissions trading in the European Union (“EU”), the authorities decide the emission amount to be reduced and subject that are obliged to reduce.　In 2020, 11,000 facilities with high emission, including power plants and factories, and 600 airlines were the subject of the reduction obligation.　They are now required to reduce emissions by 2.2% every year.　If it doesn't reach that amount, they have to buy in the market.　If they do not do so, they would be fined for EUR 100 per ton.

In METI’s plan, it is difficult to predict the total amount of reduction as companies decide whether to participate and what their targets are.　The MOE opines that emissions trading needs to be regulated like in Europe, and they are considering to review carbon tax whose levels are lower than that of the European countries as a pillar of carbon pricing.

Globally, the combination of emission trades and carbon tax has been recognized as the main method to encourage companies to decarbonize.　In the EU, the front runner on this issue, cross-border carbon tax, which is de facto tariff, is under consideration as a solution to clear inequalities between companies located in EU where they have to pay high costs to achieve their goal for decarbonization and those located in less regulated areas.　Japan also needs to create a view of the whole structure of the program as soon as possible to catch up with the global trend of decarbonization.

Information compiled from Nikkei Shimbun & Mizuho research

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New Equities Listing Approvals

Listing Date	Name of Company	ISIN Code	MKT
Mar-10	POVAL KOGYO	JP3856400001	T
Mar-11	CEL	JP3423610009	T
Mar-17	Moriya Transportation Engineering and Manufacturing	JP3927420004	T
Mar-18	Repertoire Genesis	JP3981300001	M
Mar-23	TORICO	JP3636100004	M
Mar-24	SBI Sumishin Net Bank	JP3400650002	T
Mar-28	Mental Health Technologies	JP3921340000	M
Mar-30	GiXo	JP3264600002	M
Mar-30	AnyMind Group	JP3164770004	M

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

***Board lot size is unified to 100*

III. Foreign Ownership Limit Ratio

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