Daiwa Securities

Seminar Report

Daiwa ESG Conference 2023

- Held ESG seminar for Japanese/overseas investors and bond issuers
- Diverse topics including academic reports, GX policy, major investor ESG investment stances
- This report provides seminar overview and key points

Strategic Memorandum DSTE487
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Seminar Report: Daiwa ESG Conference 2023

On 13 September 2023, Daiwa Singapore held its third "Daiwa ESG Conference 2023" for this year. This seminar provided investors and issuers, both those in Japan and overseas, with an introduction to ESG (Environment, Social, Governance) in Japan's bond market. 140 people from 20 countries attended or viewed this seminar. The seminar consisted of four parts, including the opening remarks. A wide range of topics was covered including academic reports, briefings from policy makers on "Green Transition (GX)," and the ESG investment stances of major investors. This report provides an overview of the seminar, as well as key points that the author feels are particularly important.

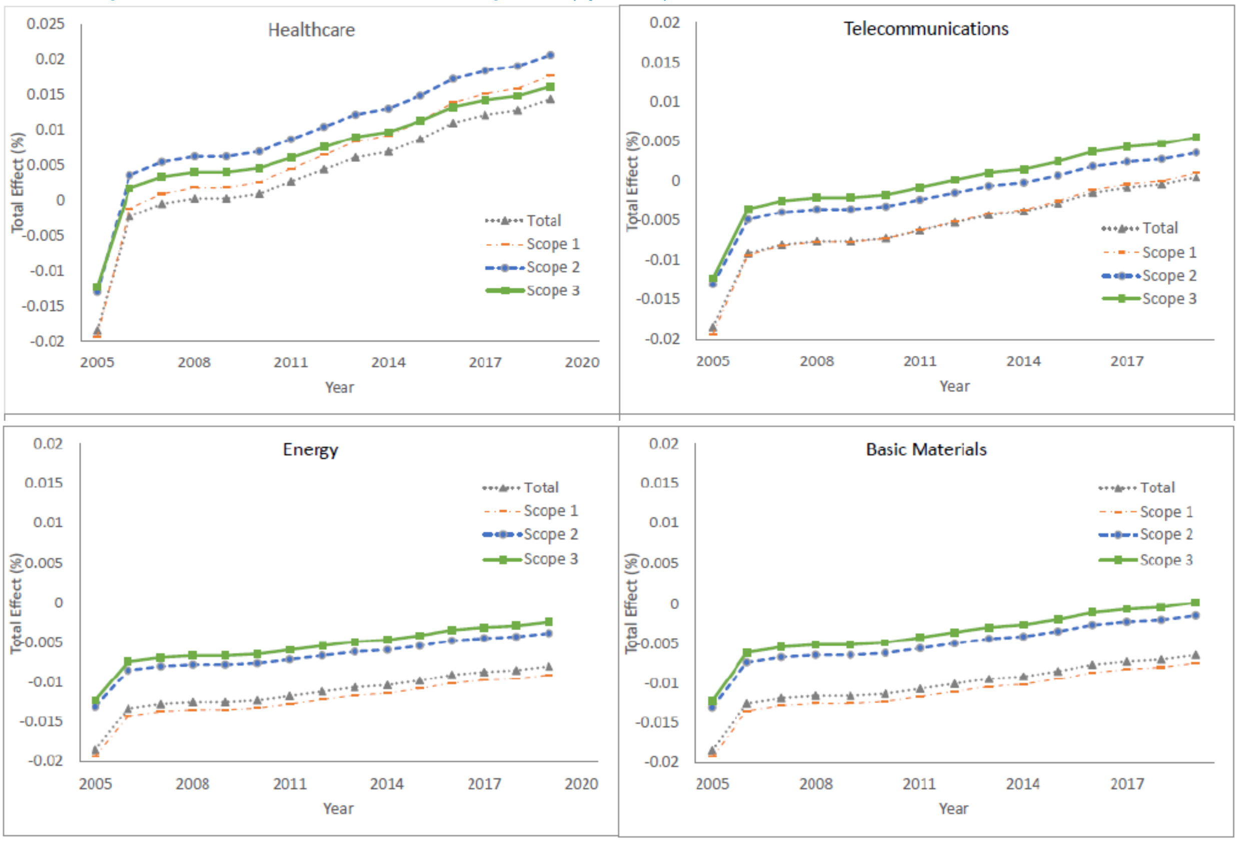
First, in the opening remarks, the author presented the ESG characteristics of the Japanese bond market under the title of "Japan's ESG Capital Market ~ From Green to Transition." Here, the author presented and explained the five main points of (1) expansion of Japan's ESG bond market despite headwinds overseas, (2) both investors and issuers viewing sustainable finance as an essence of their businesses (referencing BOJ survey) as one factor behind this market expansion, (3) BOJ's Funds-Supplying Operations to Support Financing for Climate Change Responses supporting market expansion, (4) greenium (green premium) situation in Japan's corporate bond market, and (5) market expectations for a sovereign ESG-labeled bond called "GX Economy Transition Bonds."

Chart 1: Program of Daiwa ESG Conference 2023

Opening Remarks	**Japan's ESG Capital Market~from Green to Transition**		**Mr. Shun Otani**	Daiwa Securities Co. Ltd
Session 1	**Analysis on Corporate ESG Activities and the Credit in Japan**	ESG activities in Japan and impact on credit ●Analysis on Japanese companies' ESG activities and impact on credit spreads ●Analysis on Japanese CDS market in relation to CO2 emission	**Prof. Tatsuyoshi Okimoto**	Keio University, Japan
Session 2	**Japan's Path to Transition Economy**	Japan's path to transition economy ●Japan's current status around transition finance ●Japan's future ambition for transition	**Mr. Fumihiro Kajikawa**	GX Finance Promotion Office/ Office for Opening the GX Promotion Organization Industrial Science, Technology and Environment Policy Bureau Ministry of Economy, Trade and Industry, Japan
Session 3	**Current Stance and Ambition for ESG Investment**	Current stance and ambition for Japan Post Insurance ("Kampo") ESG investment ●Kampo's current stance and hurdles for ESG investment ●Kampo's mission for ESG investment and future ambition	**Mr. Takumi Kobayashi**	Japan Post Insurance, Japan
		Moderated by	**Daisaku Chabata**	Director, Sustainability Solutions Department

Session 1 ("Analysis on Corporate ESG Activities and Credit in Japan") was presented by Professor Tatsuyoshi Okimoto of Keio University, who also spoke at the May seminar in Tokyo. His presentation was followed by a Q&A session. In addition to the content as of the May seminar, the results of a study on the relationship between corporate CO2 emissions and credit spreads were also presented at the September seminar[1]. The carbon risk premium (CRP) was initially negative in the early 2000s, in other words, there was a relationship in which credit spreads were tighter for companies with higher emissions. That said, this relationship has been reversing in recent years as investors become increasingly aware of decarbonization risks. It was also reported that sectors with lower emissions, such as healthcare and telecommunications, were more likely to have positive CRP than those with high emissions, such as energy and basic materials.

Chart 2: Impact of Carbon Emissions on Credit Spreads (by sector)



Source: Reprinted from materials provided at the seminar.

In Session 2 ("Pathways to Japan's Green Transition (GX)"), Fumihiro Kajikawa of METI gave a presentation that mainly covered (1) overall picture of GX, (2) overview of transition finance, and (3) relationship with Asia. The author was left with the impression that a driver of this transition is the phrase "carrot and stick." Kajikawa touched on the approach of demanding carbon emission costs through the future introduction of carbon pricing, such as emissions trading schemes and GX surcharge (= stick). However, he also stated his hope for the formation of incentives such as government support (carrot) for the transition through GX funds and other means. Here, the GX Economic Transition Bonds will serve as a bridge to such financing. As for the GX bond issuance schedule, Kajikawa explained that the framework will likely be announced around early November, after second-party opinions are obtained. He added that the first bonds are then likely to be issued within this fiscal year, after a series of talks with investors.

[1] For details, refer to RIETI discussion paper *Credit Default Swaps and Corporate Carbon Emissions in Japan* (2022) *Tatsuyoshi Okimoto and Sumiko Takaoka.*

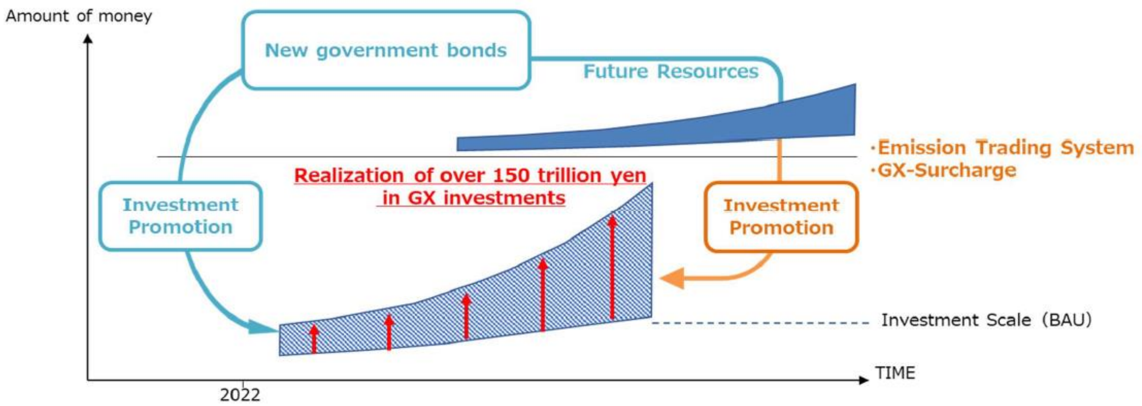
Chart 3: Growth-oriented Carbon Pricing

To promote the GX investment as described above, a **"Pro-Growth Carbon Pricing Concept"** will be embodied and implemented as soon as possible.

① **Government support for bold upfront investment** by issuing **new government bonds** (20 trillion yen over the next 10 years)

② **Introduction of carbon pricing to give incentives for GX investment**
(1) Full-scale operation of **emissions trading system** in high emission industries [**from FY2026**].
+ Allowance auctioning to be phased in gradually to **power generation companies** [**from FY2033**]
(2) Introduction of a **GX-Surcharge** on fossil fuel supply [**from FY2028**]

③ Strengthen financial support through public-private partnership



Source: Reprinted from METI materials.

Finally, in Session 3 ("Current Stance and Ambition for ESG Investment"), Takumi Kobayashi of Japan Post Insurance (JPI) divided his presentation into five sections to explain his company's initiatives regarding ESG investment. These sections were (1) about JPI, (2) ESG investment policy, (3) ESG investment framework, (4) ESG bond investment, and (5) future challenges. The author was particularly struck by the comments about the difficulty of engagement. Bond investment engagement[2] is different from equity investment engagement, which includes the exercising of voting rights, and it is true that some companies are not forward-looking in regards to engagement. In such cases, Kobayashi said JPI strives for two-way communication and conducts thorough preliminary research in order to share ESG issues and gain the trust of issuers. Also, measuring investment effectiveness has become increasingly important in recent years, given the growing trend toward impact investing. The quantitative effects of eight bonds with particular themes issued by international organizations and actually purchased by JPI were presented (Chart 4). Participants asked what is the next ESG theme that JPI is watching. Kobayashi answered that JPI is focusing on human rights, human capital, and natural capital while promoting investment without bias toward any particular theme.

[2] Strategic Memorandum (DSTE481): Engagement and investment performance- Active ownership.

Chart 4: Impact Assessment of ESG Bonds by International Agencies

- Considering two perspectives ((1) holding period and (2) availability of quantitative indicators),we selected eight bonds issued by five issuers for assessment (investment amount is approximately 114.4 billion yen) from international agencies' themed bonds we hold.
- The results of the impact assessment (attributable to our holding) are as follows.

Topics: Enhancement of Well-being

- Number of people benefitting from improved agricultural productivity: Approximately 520,000 people
- Number of people benefitting from the safety net program: Approximately 5,200 people
- Number of people benefitting from improved access to water sources : Approximately 3,100 people
- Women and girls completing secondary or tertiary education or other training: Approximately 140,000 people
- Skilled jobs for women generated: Approximately 10,000 people
- Number of people benefitting from new electricity connections: Approximately 210,000 people
- Number of COVID-19 vaccines purchased: For approximately 210,000 people

Topics: Contribution to Environmental Protection

- Annual GHG emission reduction/avoidance amount
  350,170 t-CO_2e
  Equivalent to 75,000 vehicles
  (Converted to annual emissions of passenger vehicles*)
- Annual renewable power generation
  448.9 million KWH
  Equivalent to 38,000 households
  (Converted to the annual electricity consumption of the average household*)

Source: Reprinted from Japan Post Insurance's Responsible Investment Report 2022.

Areas such as ESG and sustainable finance are unique and can greatly differ by country. Europe and other regions are now focusing on green aspects while utilizing taxonomy. In Japan, on the other hand, the public and private sectors are working together to nurture a transition market. Such institutional and conceptual differences are obstacles to cross-border ESG investment. Our hope is that this seminar and report will help to lower the hurdle of information asymmetry (= one party in a transaction having more or better information than the other party) and contribute to the development of sustainable finance markets where disciplined and active investment can take place.

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Benchmark index: TOPIX for Japan, S&P 500 for US, STOXX Europe 600 for Europe, HSI for Hong Kong, STI for Singapore, KOSPI for Korea, TWII for Taiwan, and S&P/ASX 200 for Australia.

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- There is a risk that you will incur losses on your transactions due to changes in the market price of financial instruments based on fluctuations in interest rates, exchange rates, stock prices, real estate prices, commodity prices, and others. In addition, depending on the content of the transaction, the loss could exceed the amount of the collateral or margin requirements.
- There may be a difference between bid price etc. and ask price etc. of OTC derivatives handled by our company.
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* The amount of the trading commission cannot be stated here in advance because it will be determined between our company and you based on current market conditions and the content of each transaction etc.
** The ratio of margin requirements etc. to the amount of the transaction cannot be stated here in advance because it will be determined between our company and you based on current market conditions and the content of each transaction etc.

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