Improving the "Investment Environment in the EU and Japan" -

An EU perspective
on the new Japanese Corporate Governance Code

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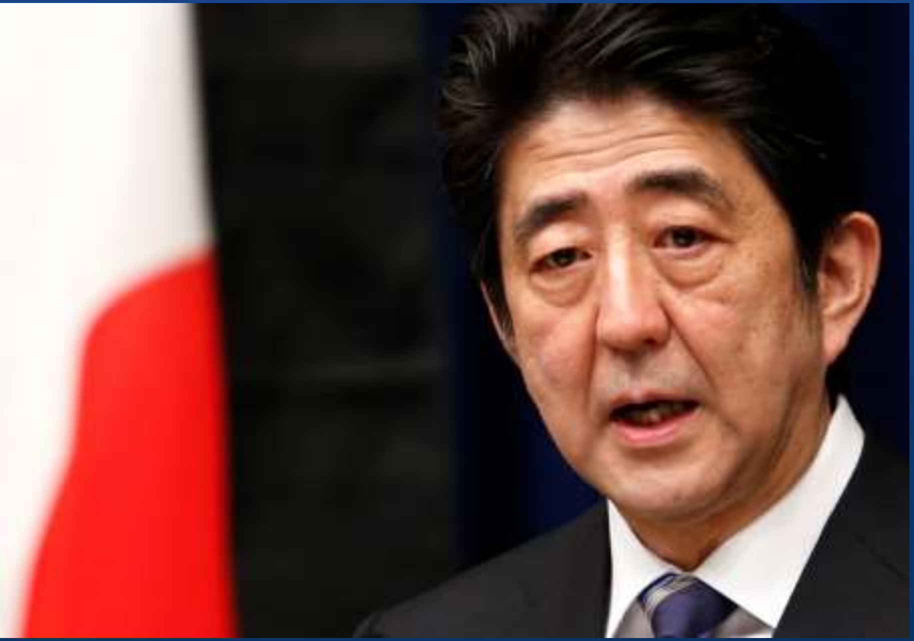
Better Corporate Governance is Part of PM Abe'sThird Arrow



Improved corporate governance is a pivotal factor in achieving higher levels of foreign direct investment

New Corporate Governance Code

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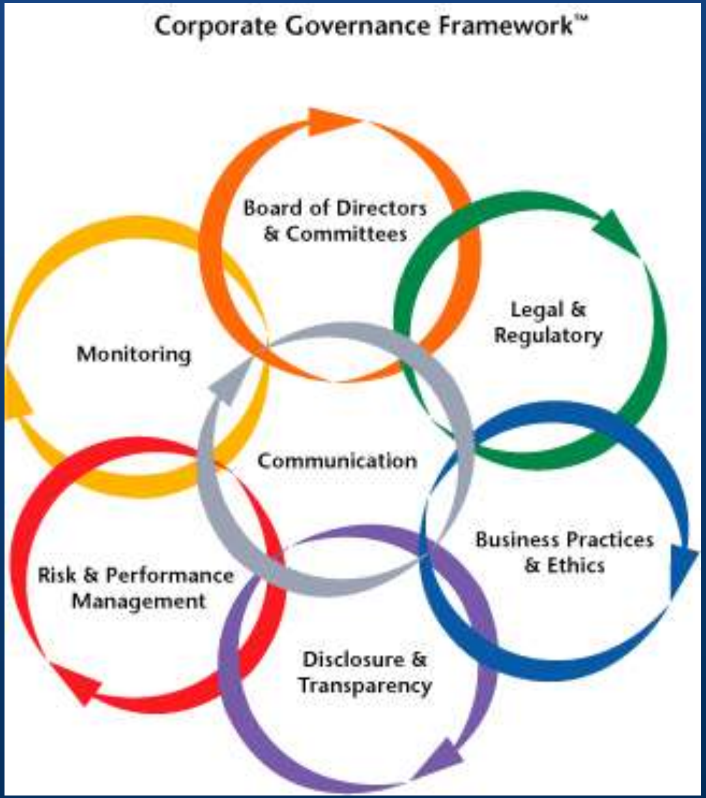
The Japanese Corporate Governance Code (JCGC) should encourage FDI as it seeks “growth-oriented governance” and its primary purpose is “to stimulate healthy corporate entrepreneurship, support sustainable corporate growth and increase corporate value over the mid- to long-term”.

The Corporate Governance Code seeks balance between the overlapping business principles shown at the right of the slide



http://www.bedeawi.com/articledetailes.php?id=287

Traditional Regime vs. New Corporate Governance Code

Traditional Corporate Governance	New Corporate Governance Code
"Insider"-dominated boards & long-term employment	Specifies at least 2 Independent Non-Executive Directors on the Board of Directors & specifies the responsibilities of company Boards
Cross-shareholdings between banks and companies "Keiretsu" system	Requires companies to disclose their policy with respect to "cross-shareholdings"
Focus on stakeholders (employees, banks and trade partners) over shareholders	Is more focused on and requires more dialogue with shareholders
Low corporate competitiveness: low Return On Equity (ROE) makes Japanese companies unattractive to foreign investors	More focus on Return on Equity (ROE) – should encourage FDI
No requirement to comply to a standard	Takes a "Comply or Explain" approach to code
Insufficient transparency	Requires more information transparency

New Japanese Corporate Governance Code

- Focuses on 5 general principles:

Securing the rights & equal treatment of shareholders

Cooperation with stakeholders other than shareholders

Information disclosure and transparency

Responsibility of the Board

Dialogue with shareholders

- Code applies to all companies listed in the TSE First Section or Second Section—they are subject to all 73 principles of the code (5 general principles and their sub-principles)
- Code applies to all companies listed on Mothers or JASDAQ—they are subject to the 5 general principles.
- “Comply or Explain” approach: companies listed on the first and second sections of the TSE need to explain any non-compliance with the Governance Code in its entirety.
- All publicly traded companies are required to submit governance reports following annual shareholder meetings.

Views from the EU

- **A good start**

Changes should show full impact in 2016. So far, many Japanese companies made progress regarding :

- the **"Comply or Explain" requirement**:

  End of December 2015, out of 1,845 TSE1 and TSE2 companies that submitted Corporate Governance Reports to the TSE, 31% drafted some form of JCG guidelines in addition to their formal Corporate Governance reports.

- Increase in the number of **outside directors** among TSE-listed companies :

  July 2014: 65% ; December 2015: 90%

Views from the EU - Recommendations

Enhance diversity in Board composition

In a rapidly globalizing world, there is need for more global input in Japanese Boards from different nationalities, backgrounds & genders

- **Gender diversity** : In Europe, improvements still needed, but Japan lags behind

  Objective of "Abenomics": 30% women in corporate leadership positions by 2020

  Today, 3.1% of the Board seats are occupied by women among Japan's 30 largest companies

  (source: 2014 study from NPO Catalyst Japan)

  Example: Nomura, Hitachi have each a female Board Member; Toyota has a voluntary policy to improve

- **Foreigners** : Freer to ask difficult questions, not bound to cultural obligations (ex: Olympus scandal: Michael Woodford, British Chief Executive, exposed hidden losses at the company)

  Example: Takeda Pharmaceuticals has a foreign President since July 2014 and its Board has 2 Americans→ The management has been internationalized and the group has increased its external operations since 3 years ago.

Views from the EU - Recommendations

- **Board Roles**

  - Separation between the roles of Chair and CEO (not required in the Japanese Code):

The European experience has shown that firms with role separation outperform those combining both roles

  - Independent Non-Executive Directors (INEDs) should take up key decision-making positions (in leading/key Board committees).

In the UK, they can chair the Nomination, Audit and Remuneration Committees. It is an opportunity to more efficiently oversee the business.

Views from the EU - Recommendations

- **Stronger focus on shareholders and transparency**

➢ The "Comply or explain" requirement forces companies to give investors detailed disclosure about the company's situation

➢ More appointments of Investor Relations positions at companies that previously didn't have them

➢ Additional strength of audit and monitoring functions, particularly through the appointment of qualified INEDs to Boards

Enhance transparency for shareholders and potential investors

<u>Attract greater investment</u> from overseas institutions to achieve Abenomics' objectives and to make the best of the future EU-Japan Free Trade Agreement

Views from the EU

- **SUMMARY - Key Messages from EU Industry**

1. We welcome progress made by Japan in relation to corporate governance reform. It will contribute to increasing the profitability of Japanese listed companies and attracting more foreign investment.

2. Corporate governance is an important area discussed in the EU-Japan EPA/FTA where the EU aims to agree on mutually binding disciplines on corporate governance. In our view, the adoption of the Japanese Corporate Governance Code enables Japan to agree on such disciplines.

3. Implementation of the Code is key. Tokyo Stock Exchange is doing a commendable job of monitoring and we encourage them to continue doing so. In addition, it is important to raise shareholder awareness to the new system.