



Summary of Discussions on Measures to Improve the Effectiveness of the Market Restructuring (Draft)

Exchange & beyond

Tokyo Stock Exchange, Inc.

January 25, 2023

I . Major Policies P2

II . Specific Initiatives

1. **Clarification of the End Date** of Transitional Measures P3

2. **Motivate Efforts to** Enhance Medium- to Long-term Corporate Value P6

a) Raise Awareness and **Literacy regarding Cost of** Capital and Stock Price P7

b) Improve the Quality of Corporate Governance P8

c) Further Expansion of English Disclosure Practices P9

d) Improve the Effectiveness of Dialogue with Investors P10

Reference Material P11



- In Japan's economy, the lack of a smooth transition of personnel and capital resources to growing areas has led to a prolonged slump in productivity. In order to ensure the sustainable development of the Japanese economy in the future, it is important to promote industrial metabolism and innovation in business and society.
- In doing so, individual listed companies can not only take measures independently, but they can also consider ways to increase productivity by exchanging factors of production and by implementing M&As with other companies. It is important for **TSE to create a framework to encourage** such efforts and thereby contribute to the improvement of productivity in the Japanese economy as a whole.
- **At this time, the government has decided to fundamentally expand and make permanent the NISA program in order to achieve financial inclusion, whereby the benefits of the financial and capital markets are widely available to all citizens, and the foundation has been established for households to actively shift their assets from savings to investments. In this context, the efforts of listed companies which receive risk capital are more strongly expected to increase their corporate value than ever before.**
- Under these circumstances, in order to ensure the effectiveness of the market restructuring which was implemented for the purpose of contributing to the improvement of listed companies' corporate value and to make this an opportunity for real change, it is essential that **TSE continue to work on these reforms with a sense of urgency.**
- In light of this background:
 - TSE should immediately make clear how the transitional measures will be handled in the future with respect to the continued listing criteria, which have been established as a measure for easing drastic changes, including the timing of termination, from the perspective of ensuring a healthy industrial metabolism.
 - In order to revitalize the capital markets, and ultimately the Japanese economy, **TSE should create a framework to motivate** listed companies that are not concerned about violating the continued listing criteria to take **action independently** to enhance their medium- to long-term corporate value, such as promoting **cost of capital-conscious** management, by taking advantage of the characteristics of the three market segments.
 - **These measures should be evaluated on an ongoing basis for further improvement.**

- In order to encourage listed companies to increase their corporate value and to ensure a healthy industrial metabolism, the transitional measures should be terminated as soon as possible, taking into consideration the amount of time it will take for the results of companies' initiatives to be realized.
- On the other hand, it is necessary to design the transitional measures in consideration of the fact that some listed companies have selected a market segment and made a plan without a set deadline, and that some listed companies have made steady progress in their efforts based on their plans.
- In addition, the revised transitional measures should be designed to be as simple and as clear as possible so investors can easily understand.
- If transitional measures are terminated and stricter exit criteria are applied, it would be necessary to ensure sufficient redemption opportunities for investors, and it would be appropriate to use the framework of the Securities to Be Delisted.

1. Termination Date of Transitional Measures

- **March 2025 (three years after the transition)** is appropriate.

Note: There are two opinions: one is that the transitional measures should last for three years followed by an additional one-year improvement period, and the other is that the improvement period should be included in three-year period.

- Leaving the transitional measures in place indefinitely will hinder the promotion of industrial metabolism, while a certain amount of time is needed for companies' efforts to produce results.
- Three years is appropriate in light of the general lead time required to achieve the management plan, gather investor opinions in the call for comments, and market valuation.

2. Handling of Companies Disclosing Plans that Extend Past the Termination Date

- **This should be uniformly terminated with no exceptions.**

- The design and operation should be as simple and as clear as possible, considering ease of understandability for investors.
- There is no need to be bound by the past, as there are usually rule changes that originate from TSE.

- **Exceptions should be made.**

- The new rules cannot be retroactively applied to a plan that has already been disclosed to be inadmissible.
- The new rules cannot be applied retroactively to disallow plans that have already been disclosed.
- It should be considered that some companies are making steady progress in their efforts.

(Specific comments on handling)

- Even if exceptions are made, the rules should be simple and easy for investors to understand.
- Criteria should be raised gradually to assess progress toward conformance.
- While deferring until March 2027--five years after the transition--at the most, which would cover most companies, the names of companies, details of the non-compliant criteria, and the deadline for plans should be made public to encourage early achievement in a way that 'names and-shames,' so to speak.

3. Disclosure of Plans Beyond the Termination Date

- Disclosure of plans beyond the termination date should not be permitted after the announcement of the termination date.

Note: Some commented that this should not be allowed from the time the specific proposal for handling was published, and others commented that this should not be allowed after the effective date of the revised rules.

4. Extension of the Planning Period to a Date prior to the Termination Date of the Transitional Measures

- There is **no need to set limits**.
 - Inappropriate extension of the planning period could negatively affect the stock price and should be left to the market's assessment.

5. Necessity to Treat Each Market Segment Differently

- In principle, there is **no need** to treat them differently.
 - If criteria are raised in stages as in 2. above, one idea is to differentiate the rate at which criteria is raised.

Note: Some commented that different treatment could be considered depending on the number of non-compliant criteria and the type of non-compliant criteria.

6. Institutional Support Regarding Segment Transfers

- **Given that the concept of these market segments is that each market segment is independent, it would be inappropriate to eliminate the review process for market segment transfers.**
- On the other hand, **taking into consideration the practical burden on TSE and securities companies, it is conceivable to encourage early action and, if necessary, to introduce institutional support.**

Note: In the call for comments, there was an opinion that if the deadline of the transitional measures were set to be shorter than the period in the disclosed plans to meet the criteria, the premise of market selection would change. In that case, a market selection/transition period needs to be set again.

Other

- In order to secure opportunities for investors to sell their shares in companies to be delisted, it would be practical to utilize the framework of the Securities Under Supervision and Securities to Be Delisted, and extending the designation period to six months would be appropriate.

- Considering that the purpose of this market restructuring is to contribute to the improvement of corporate value of listed companies, it will be meaningless unless we address the fact that about half of all listed companies have a PBR below 1. Whether or not we can take any steps forward to improve financial indicators such as PBR is a point of discussion at the council.
- **Since the main actor in enhancing corporate value is the company itself, it is necessary for listed companies to independently** redesign management by backcasting from their future vision and move toward balance sheet management and cash flow management.
- **In order to motivate such efforts, TSE should promote** measures such as a) raise awareness and **literacy regarding the cost** of capital and stock price, b) improve the quality of corporate governance, c) further expansion of English disclosure practices, and d) improve the effectiveness of dialogue with investors, in accordance with the characteristics of each market segment.
 - **In promoting such measures, it is appropriate for TSE to create a framework** for autonomy in corporate management to function, rather than to micromanage individual companies.

II .2.a) Raise Awareness and Literacy regarding Cost of Capital and Stock Price

- In Japan, there are many cases where management is unaware of the cost of capital and stock price. It is necessary to improve management's awareness and literacy of these concepts and allow autonomy in corporate management functions.
- First, TSE could encourage management to properly identify the company's cost of capital and capital efficiency, evaluate those statuses and its stock price and market capitalization, and disclose policies and specific initiatives for improvement as necessary. This could be a catalyst for promoting dialogue with investors and improving management literacy.
 - In particular, companies with a PBR consistently below 1x (i.e., not achieving capital efficiency in excess of their cost of capital, or achieving capital efficiency in excess of their cost of capital but future growth potential is not adequately expected by investors) should be required to disclose their policies and specific initiatives for improvement.
 - In addition, disclosure of progress should also be encouraged from the viewpoint of further strengthening awareness of evaluation by investors.
- In addition, the Code of Corporate Conduct introduced by TSE in 2007 should be reviewed and revised as necessary to clarify the responsibilities of listed companies, such as awareness of the cost of capital and respect for shareholders' rights/protection of minority shareholders' rights, and to ensure their effectiveness, while taking into account subsequent developments in corporate governance and other factors.
- In addition, in order to raise awareness among management in listed companies, TSE could be proactive in promoting understanding and recommending stock compensation plans, providing training opportunities and sharing best practices to improve literacy related to capital markets and corporate governance.

II .2.b) Improve the Quality of Corporate Governance

- Since the establishment of the Japan's Corporate Governance Code, listed companies have made progress in their efforts to improve governance, but **polarization has become more apparent, and there are still a significant number of companies that have little** awareness of the need to gain insight in order to improve their own management.
- Corporate governance has so far tended toward formalism but improving quality should be more focused from now on.
- “Comply or Explain” has become a formality for some companies. For example, there are some companies whose Explanations have been “under consideration“ for several years. TSE should re-emphasize the purpose of the “Comply or Explain” principle, clearly state **sufficient and insufficient** cases of Explanations, and encourage companies that do not properly implement “Comply or Explain” to correct the situation as necessary.
- In addition, while the number of listed companies that have nomination committees and remuneration committees is increasing, there are many cases where the roles and functions of these committees are not clear. Therefore, TSE should continue to encourage disclosure of the status of activities of nomination committees and remuneration committees, investigate the actual status of their **roles, functions, and** activities, and compile and publish the status and examples.

- Quite a few foreign investors cite a complete lack of information as a reason for their reluctance to invest in Japan.
- In particular, given that the Prime Market is for companies committed to dialogue with global investors, English disclosure practices, which are the foundation of dialogue, should be encouraged **to further expand the range of documents covered and to eliminate the time lag between publication of those documents in Japanese and English**, and possibly made mandatory in the future.
- In doing so, it is necessary to consider factors such as the scope of documents to be covered, **timing of disclosure**, etc., taking into account the burden on listed companies and the status of use by investors.
- In addition, English disclosure practices should be promoted **with foreign investors in mind** as a matter of course for companies that have capital needs **to achieve future growth**. Thus, it is necessary to encourage voluntary disclosure to progress in the Standard Market and Growth Markets as well.

II .2.d) Improve the Effectiveness of Dialogue with Investors

- It is important to gain insight into how to improve one's own management capabilities through dialogue with stakeholders, including investors, but some companies remain reluctant to engage in such dialogues.
- In particular, listed companies in the Prime Market are expected to focus on constructive dialogue to improve their corporate value. From the perspective of encouraging constructive dialogue with investors, TSE should require companies to clarify the status of dialogue between management and investors and the content of such dialogue.
- While CEOs and other members of management are expected to play a central role in dialogue with investors, independent directors are also expected to actively respond to requests from investors for dialogue, as they are in a position to supervise management in response to shareholder requests.
- However, the number of independent directors who engage in dialogue with investors is currently limited, and some independent directors are not fully aware of their roles. Therefore, educational activities are needed to ensure that independent directors properly understand the roles expected of them.
- On the other hand, while investors should play an important role in appropriately encouraging listed companies to increase their corporate value, only a few investors are involved in dialogue at present, and it is important to encourage asset owners, including corporate pension funds, to **increase awareness and interest in dialogue with companies.**

(Reference) List of Members of the Council

Members:	Ando Satoshi	Director, OMRON Corporation
	Kanda Hideki	Professor, Gakushuin University Law School
	Koike Hiroyasu	President & Chief Executive Officer, Nomura Asset Management Co., Ltd.
	Kumagai Mitsumaru	Deputy Chairman of the Institute, Daiwa Institute of Research Ltd.
	Kuronuma Etsuro	Professor, Waseda University, Waseda Law School
	Matsumoto Oki	Chairman & CEO, Monex Group, Inc.
	Nagami Yo	CFO, RAKSUL INC.
	Okina Yuri	Chairperson, The Japan Research Institute, Limited
	Sampei Hiroki	Principal, Astonering Advisor LLC

(in alphabetical order by surname)

Observers: Financial Services Agency
Ministry of Economy, Trade and Industry