

Minutes of the Fourth Council of Experts Concerning the Follow-Up of Market Restructuring

Date: Friday, November 25, 2022 10:00 – 11:30

Place: Tokyo Stock Exchange 9F Meeting Rooms 911, 912, 913

Attendees: See member list (Ms. Okina was absent)

[Kikuchi, Director, Listing Department, TSE]

The time has now come to begin the fourth Council of Experts Concerning the Follow-Up of Market Restructuring. Thank you for joining us today.

First of all, regarding attendance, Ms. Okina is absent and Mr. Kumagai is joining us online.

Now, I would like to begin proceedings straight away. First, let us explain today's agenda.

[Ikeda, Senior Manager, Listing Department, TSE]

Today, Mr. Koike, a council member, and Mr. Murao, Senior Managing Director at Nomura Asset Management, will give presentations on the Japanese Stock Market as Seen by Foreign Institutional Investors, based on Document 2. After each presentation, there will be time for questions and comments. We expect the presentations to take about 30 minutes.

We would then like to use the remainder of the time to delve deeper into transitional measures. First, TSE will explain the items to be discussed today and related data based on Document 3, which will be followed by a presentation by Mr. Kamio, a Senior Researcher from the Policy Research Department of the Daiwa Institute of Research, based on Document 4. After that we will ask for your feedback.

Please note that Document 5 is a summary of the results of the call for comments and Document 6 is an opinion submitted by the Ministry of Economy, Trade and Industry. Both these documents were explained during the preliminary explanation, and so will not be explained again today.

That covers everything.

[Kikuchi, Director, Listing Department, TSE]

Let's get started straight away with Mr. Koike and Mr. Murao's presentation. Please go ahead.

[Koike, member]

Thank you for this very valuable opportunity.

I will talk about "Project BRIDGE: Japanese Stock Market as Seen by Foreign Institutional Investors," in line with the presentation materials. Senior Managing Director Murao, our Equity CIO, is also here today.

In recent years, we have heard with increasing frequency that global investors are losing interest in Japanese stocks, but on the other hand, looking at corporate performance, competitiveness, and governance strengthening, including the progress made with the Corporate Governance Code, we have concluded that Japanese stock prices are undervalued compared to those in developed countries overseas.

Overseas client accounts for just under 15% of Nomura's total assets. Since April we have been able to travel abroad, and we have been exchanging views on Japanese equities while visiting overseas clients. Our findings are summarized in today's document.

Project BRIDGE was started to bridge the gap between companies and investors, and to bridge the gap between the reality at the company, its corporate value, and the market price of its stock. In April, May, and June we made our first round of visits to overseas investors, and we presented two points: that the Japanese stock market is undervalued and attractive, and that we will enhance corporate value by strengthening engagement with respect to the assets we manage.

To start us off, Mr. Murao will explain our opinion on the attractiveness of the Japanese market.

[Murao, Senior Managing Director, Nomura Asset Management]

I would like to tell you about how we view the Japanese stock market and how we have communicated that view to foreign investors.

Please turn to page 3. To make the case that the market is undervalued, we show a comparison of profit yields on the world stock market from the 1970s. The chart shows that profit yields on Japanese equities are higher, in other words, cheaper, than global profit yields, which are thought to be at a 50-year low.

Turning to page 4, when we say that equities are undervalued, there is always a counterargument from investors that the valuation should be low because the market ROE is low. While we do not dispute this, we would like to inform investors that this does not mean that there are no investment opportunities in the Japanese stock market.

The figure on the left compares the US S&P500 index to Prime Market stocks on TSE, and show how many stocks in each population have an ROE of 15% or more. The S&P500 index is approximately 58% (275 issues), while the TSE Prime Market is 21% (378 issues), so while Japan's share is lower in terms of composition, the absolute number is not inferior. 378 stocks is a large enough population to select stocks when building a portfolio based on so-called active management. More importantly, when comparing the population of stocks with ROE of 15% or more, 62% of the S&P500 stocks have a PER of 20x or more, while only 30% of Japanese stocks have a PER of 20x or more, and more than half of the stocks have a PER of 15x or less. This indicates that more undervalued stocks can be selected in Japan, in addition to the same highly profitable and high-growth stocks.

Page 5 shows what would have happened if we had actually invested in such a population. Japanese stocks with ROEs of 15% or higher have seen returns that are not out of line with the S&P500 index, but yet their valuation levels are low.

We did not only focus only on companies with high ROEs. Page 6 shows that efforts to improve profitability are being made through engagement by institutional investors, even in companies with low ROE.

In our engagement activities, we engage in ongoing dialogue on topics such as business strategy, financial strategy, and environmental, social, and governance initiatives to promote change.

On page 7 onwards, we introduce the changes that have occurred in the Japanese stock market since the introduction of the Stewardship Code. On page 7, we have included the percentage of independent directors, governance reform through the establishment of nomination and remuneration committees, and changes in the percentage of female board members in terms of diversity.

In terms of investor influence, on page 8, the number of shareholder proposals at general shareholders' meetings reached a record high of 292 proposals in 2022. The ratio of the number of companies with more than 20% opposition to proposals made by the company increased to 12%. In 2020 and 2021, the ratio declined due to some investment companies taking temporary measures to exercise voting rights on some proposals due to the COVID-19 pandemic, but in 2022, the ratio began to increase again. In other words, investors voices are getting louder and louder.

Page 9 shows that, as a result, changes in capital policies, such as dividends and share buybacks, have continued to occur. Page 10 shows that in the composition of investors, the ratio of financial institutions and business corporations is falling, while the ratio of foreigners and investment trusts is rising, and the ratio of outspoken shareholders is increasing.

Investors often ask why they should invest in Japan when the Japanese economy is not growing. In response, on page 11, we show that corporate earnings move quite differently from GDP by showing how Japan's GDP and corporate earnings have changed over time.

One of the topics that received a lot of attention from investors on these visits was the exchange rate. We visited investors during a period of rapid yen depreciation, and as you can see on page 12, we introduce our views on foreign exchange by explaining the real effective exchange rate and the current account balance. We sensed that investors are very concerned about the continued decline of yen assets.

In this sense, there is a high level of interest in the Bank of Japan's monetary policy and inflation trends, when presenting our views on inflation and our scenario analysis on page 13, we also presented our views on the Bank of Japan's monetary policy.

Finally, on page 14, we talk about the Kishida administration's New Form of Capitalism policies, which include measures to improve competitiveness in the medium- to long-term.

So that is what we explained to our investors.

It is the structure of the Japanese stock market that inspired me to share this information with foreign investors. As shown on page 16, the ratio of foreign corporations in the value share of the stock market has been increasing continuously, and foreign investors account for the majority of the share of trading by investment category. The need for foreign investors to have a proper understanding of the Japanese market was the reason why we visited foreign investors.

Page 17 shows the disparity in Japan's ROE levels compared to other countries and the trading trends of foreign investors. It indicates that there is a link between the two, since when Japan's ROE goes up, foreign investors buy.

[Koike, member]

Moving on, I will talk about the view exchanged during the visits to investors.

Page 19 shows that we have met with about 150 institutional investors in Europe, the Middle East, Asia, and North America, while page 20 provides an overview of these meetings.

46% of investors felt negatively about Japanese equities, while 26% felt positive and 28% were neutral. Investors showed a keen interest in engagement. We emphasized the undervalued Japanese market and our engagement as Nomura Asset Management in our explanation which generated a great deal of interest, which we assume was due to the high level of interest in

engagement. Otherwise, prices and monetary policy were the main topics of discussion.

On the next page onwards are individual comments. Please read what is written on these pages. On page 21, there are comments such as comments 1 and 7, which show that some investors agree that Japanese stocks are at their most undervalued level in 50-years. Meanwhile page 22, shows that there are also investors who do not see prospects for long-term growth, such as comment 12. What was a little surprising, and might possibly be due in part to the pandemic, were the comments about the lack of information about the market in the first place, such as comments 14, 15, 16, and 18. We believe this is an area that needs to be improved. Turning to page 23, as Murao mentioned, we have explained that we think the focus should be on corporate profitability and performance even in the absence of Japanese GDP growth, but there are some investors who have macroeconomic concerns. On page 24, some investors expressed hope for structural reform in Japan from a macroeconomic perspective rather than an economic one, such as comments 1, 3, 4, 5, 6, 7, and 8. Moving on to page 25, we confirmed that, with respect to the yen's depreciation, investors were highly interested in the outlook for the exchange rate, and were concerned about the outlook for the Bank of Japan's monetary policy and investor trends, including Japanese individuals who are inflating their foreign investments. As shown on page 26, we also received numerous questions about the trends and outlook for prices, which form the backdrop to the Bank of Japan's monetary policy. Page 27 shows that while the ability to buy stocks with high ROE at lower valuations was supported by active investors, many passive investors expressed a desire for the index itself to be reviewed and communicated to increase its attractiveness. Page 28 onwards relates to engagement. Page 31, shows that there were not many questions about the Kishida administration's policies, in part because his policies were a bit lacking in substance from April to June, but we were asked many questions about the easing of travel restrictions and measures to fight COVID-19.

At the beginning of next year, we plan to update the same investors on Japanese policy trends and other issues as a follow-up to the investor tour we went on this spring, and we would be happy to share any comments we receive at that time.

Page 32 is a suggestion that we gleaned from our dialogue with foreign investors. We felt that, despite everything, foreign investors expect the Japanese economy as a whole to grow. We were also able to confirm that there is room for improvement in regard to information disclosure. We feel that information is not being conveyed, including disclosure in English, which has been discussed at this meeting, and that activities that seek understanding are needed. With regard to engagement, there are not yet many examples of cases in which corporate reform through engagement has led to an increase in corporate value, and so, although we have been working hard to encourage engagement, I believe that investors are perhaps not really feeling the benefits of engagement. We also feel that there needs to be a discussion about markets and indexes that are attractive to passive investors, and how to show what markets and indexes already exist or whether new ones should be created.

Lastly, we have created a special Project BRIDGE page on our website that we are encouraging investors to visit. In particular, since it has been pointed out that there is a lack of information dissemination, I would like to mention that we are beginning to work on disseminating information to overseas investors from our website in English, while ensuring proper CEO engagement.

I have rushed through somewhat, but that is all from me.

[Kikuchi, Director, Listing Department, TSE]

Thank you.

Now I would like to move on to the question and answer session. Since one of our participants is joining us online today, I would appreciate it if you would first say your name before you start speaking. If Mr. Kumagai, our online participant, wishes to speak, I would appreciate him indicating such fact in the chat.

So, does anyone have any questions?

[Matsumoto, member]

This is Matsumoto. You said that in the Japanese market, there are stocks

with ROE of 15% or higher, while PER is lower than that of U.S. companies. Why do you think that is?

[Murao, Senior Managing Director, Nomura Asset Management]

On page 5, we have included changes in the PER of stocks with ROE of 15% or more in Japan and the U.S. since 1993, and the gap between Japan and the U.S. has widened significantly since 2009, i.e., since the financial crisis.

The very relaxed monetary policy since 2009 has resulted in a unipolar focus on the U.S. market, with capital concentrated in companies with high profitability in the U.S., especially in intangible assets, and a gap caused by significantly higher valuations, which can be attributed to financial events. This is one reason.

This indicates that, although not included in today's presentation, the percentage of Japanese stocks in the MSCI ACWI Index is very low at 5%, but looking at the percentage of each country over the past 10 years, Japan is not the only country whose percentage has dropped. In fact, percentages have fallen in all countries except the U.S. In other words, we have a situation in which all funds have been concentrated in the United States.

Our viewpoint is that investors' financial attributes are overly oriented toward such stocks, and that they may be overlooking many other investment opportunities.

Another point is that while ROE is one indicator of growth rates, growth rates are naturally explained in such aspects as sales growth, meaning the growth rate of the business itself.

One of the things I was told by the foreign investors I spoke with, was that while they understand that ROE can maintain a high growth rate in the form of reinvestment, there are few companies in Japan that can increase their sales based on demand. Discounting is thought to be occurring because there are few companies in Japan that can achieve profitable growth.

Finally, and this was also pointed out by foreign investors, is the cyclicity of the market. Japanese companies are cyclical after all, and the trend is that there are few companies that can grow. While there are many companies that grow in line with the business cycle, experiencing zigzags, it was pointed out to us, that the number of companies that overcome the cycle to grow, is small.

Based on these perceptions, we understand that there may be a valuation gap, but this hasn't stopped us from talking to foreign investors about the possibility of considering a company as an investment opportunity if it is still at a reasonable discount.

[Sampei, member]

This is Sampei. Thank you for the opportunity to speak.

My analysis of the point just raised is similar, and I wrote about it in the Japan Association of Corporate Directors' magazine earlier this year. What I found in my analysis is that there are more companies in Japan with high ROE but low valuations compared to overseas. The reason for this is that the funds that are shareholders of such companies are dividend growth funds or high dividend funds. In other words, they do not expect to achieve earnings or top-line growth.

They have earned a good amount of money and so they have room to give back. Only returning profits to shareholders is expected, and rather than being undervalued, the market has become a market to recover shareholders' equity, which is an important issue that should be recognized.

[Kikuchi, Director, Listing Department, TSE]

Thank you.

I will now move on to explain the items we would like to discuss today, based on Document 3 that you have in front of you. As this was explained during the preliminary explanation, we will keep the explanation short.

[Monden, Manager, Listing Department, TSE]

I will now explain Document 3.

I will begin by explaining the issues we would like discussed as they are listed on page 2.

The first issue is when, in principle, transitional measures should end.

The second issue is, if a termination date is set, how should companies that have already disclosed plans that extend past the date be handled? Specifically, should plans be terminated across the board regardless of their duration, or

should they be exceptionally deferred until the deadline for the planning period, respecting each company's plan. Even if allowed until the deadline, is it possible to raise the criteria to a certain level?

The third issue relates to the renewal of the plan period, if a plan were to be deferred until the termination date, how long would the disclosure of plans be permitted beyond the termination date?

The fourth issue, also regarding the renewal of the plan period, is whether it is necessary to set a limit on the extension of the planning period even in cases where the planning period is extended to a date prior to the termination date of the transitional measures.

The fifth issue is whether it is necessary to treat each market segment differently, taking into account the differences between market segments, such as Prime Market, whose listed companies can change market to the Standard Market, and the Standard Market, whose listed companies are likely to be delisted.

The sixth issue relates to segment transfers. With the termination of transitional measures, it is anticipated that some companies listed on the Prime Market, in particular, will consider changing their market segment to the Standard Market. The issue is whether institutional support, such as simplification of examination procedures, is needed to address these market segment transfers.

These are the issues we would like you to discuss today. The remainder of this document is reference materials.

That's all from TSE.

[Kikuchi, Director, Listing Department, TSE]

We will continue with a presentation from our guest speaker. As mentioned at the beginning of this presentation, Mr. Atsushi Kamio from the Daiwa Institute of Research has joined us today. Mr. Kamio, please go ahead and give your presentation.

[Kamio, Senior Researcher, Policy Research Department, Daiwa Institute of Research]

My name is Kamio and I am from the Policy Research Department at the

Daiwa Institute of Research. Thank you very much for the opportunity to speak today.

As a researcher, I write reports on TSE restructuring system and the state of listed companies, which I then use to give lectures to listed companies, investors, and the media. In particular, I have given many lectures to listed companies on the system before and after the market restructuring, and I have also had a chance to hear from many individual companies.

Today, I would like to talk for about 10 minutes on the issues surrounding the transitional measures system and the situation at companies to which transitional measures apply. Parts of the document overlap with the explanation provided by TSE earlier, so I will skip over those parts.

Starting on page 1. We will be discussing transitional measures, and this page shows, from the perspective of transitional measures, that there are three types of listed companies in each of market. The left side of the chart shows the number of listed companies after the market restructuring and the number of companies to which transitional measures will apply, but what I would like you to focus on is the middle part, that relates to October 2022.

I would like to direct your attention to the part that relates to the Prime Market. Listed companies are color-coded in purple, green, and gray. Purple are “companies subject to transitional measures” and corresponds to companies that were listed before the restructuring. Then there are “companies to which transitional measures are applied” that are actually subject to transitional measures, and “companies not subject to transitional measures” that were newly listed on or after April 4, 2022, after the market was restructured. These are companies to which transitional measures do not apply.

Moving on to page 2, I personally think there are four possible ways to terminate transitional measures based on these categories. These four are also illustrated on pages 5 and 6, and I will explain each one in detail.

The first way is to end transitional measures entirely at a specific time. For example, let’s suppose that transitional measures will end at temporary points in March 2025 and March 2027.

I think there are three factors that could be considered in the next step, which would be a phased termination.

Regarding the first method, which is to allow transitional measures up to the

planning period set by each listed company. Companies set various periods, such as three years or five years, and are allowed transitional measures up to that point. The second method is the termination of the renewal of the planning period for listed companies at a specific time, or the termination of the application of transitional measures for new companies that do not meet the criteria for continued listing. This termination of the new application of transitional measures will apply to cases in which companies met the criteria for continued listing during last year's market transition, but failed to meet the criteria for continued listing after that time. The third and final method is to raise the relaxed criteria for continued listing that apply to transitional measures.

I will skip the example of the schedule when violating the criteria for continued listing on page 3, as TSE has already covered this.

Page 4, and this was also partly included in the TSE's materials, covers the transition to the market when the transitional measures expire and a company fails to meet the criteria for continuing its listing.

I'd like to mention one thing. Although it is difficult for companies listed on the Standard Market to be newly listed on the Growth Market in terms of criteria, I feel that the listed companies themselves are gradually becoming aware of this and are now at a stage where they are beginning to seek concrete measures to address this issue.

Incidentally, the relaxed criteria for continued listing that applies to the transitional measures that I mentioned earlier are written on the right of each market segment in this chart. Compared to the criteria for continued listing, these are set at a fairly low level, and there is an argument for gradually raising this level.

Moving onto page 5. This slide discusses the four ways to end transitional measures and the factors I mentioned earlier. As shown in the figure on the bottom right, if we divide each method into options (1) to (4) and organize them on a horizontal axis, metabolism and a vertical axis, impact on the market, we get this image. This slide explains methods (1) and (2).

(1) is when transitional measures are fully terminated at a specific time. In this case, all listed companies on each market will be above the criteria for continued listing and will be homogenized. This is also expected to promote

metabolism. On the other hand, since many listed companies will be delisted or transferred between markets at specific times, I would imagine that there will be a significant impact on the market.

With regards to methods (2) to (4), I think the metabolism and market impact will vary depending on the combination adopted.

(2) allows for transitional measures up to the planning period set by the listed company. In this case, the initiatives of the listed company are respected and the impact on the market is minimal, but the promotion of metabolism is slowest. There are also many things to consider, including how long to allow for renewal of the planning period.

Moving on to Page 6. With (3), the renewal of the planning period or the application of new transitional measures is terminated at a specific time. As a result, transitional measures are not applied from a specific time, market metabolism is promoted and there is a somewhat significant impact on the market. In this case, the treatment of “companies subject to transitional measures” and “companies not subject to transitional measures,” which I talked about at the beginning, is on an equal footing. On the other hand, there is a need to consider things such as the actual timing of termination.

(4) is a case of raising the relaxed criteria for continued listing, and considering that the criteria will be raised several times, I would imagine that metabolism will proceed more slowly than in (3), and the impact on the market will be more gradual. However, I think we must consider the timing and level of the increase, and that there will be a delay to the timing at which “companies subject to transitional measures” and “companies not subject to transitional measures” end up on an equal footing.

Page 7 has been explained by TSE, so I will skip it. Page 8 shows the status of those companies that have disclosed their plans to meet the criteria and, as of now, disclosed their progress. The figure on the top left shows the change in status from the plan, in the order of “Improved”, “Deteriorated”, “Improved and Deteriorated”, “No Change”, and “Disclosed New Plan”. “Improved” includes companies disclosing that they have complied with the criteria for continued listing. The blue arrow and balloon corresponds to this. “Improved and Deteriorated” is a case where a company does not meet multiple criteria for continued listing and includes a mix of aspects that are improving and aspects

that are deteriorating depending on the criteria.

Overall, you can see that a large number of companies have “Improved”, but there is also a certain number of “Deteriorated” and “Disclosed New Plan” companies.

The two charts below show these figures broken down into companies with fiscal years ending between April and September and companies with fiscal years ending at other times.

The chart on the bottom left chart shows companies whose fiscal years end between April and September. Judgment by TSE of the criteria for continued listing started from companies whose fiscal year ends in April, and these are companies that have, you could say, been made to announce their progress and plans. This chart shows that while the situation at some companies has “Improved”, there are many “Deteriorated” and “Disclosed New Plan” companies.

The chart on the bottom right shows other companies whose fiscal years end at other times, which have not yet been judged by TSE, but that have voluntarily disclosed their progress. Since disclosure is voluntary, we have to assume that many companies want to promote the fact that their situation has improved.

Page 9 shows the status of companies to which transitional measures apply in terms of stock prices. Specifically, it shows the stock price of companies that disclosed their plans during the market transition phase. The period covered is from September 1 of last year, when the disclosure of plans started, to the end of October of this year. Looking at each market, performance was varied, with some companies achieving stock price performance in excess of 50%, while others experienced significant negative performance.

I would now like to talk about the actual plans of two listed companies that you have in front of you.

The first plan is from a company whose stock price performance increased more than 50% in the chart on page 9 in the document I just talked about.

If you look at the “Plan” disclosed last year, you can see that the company has properly recognized the issue of low capital productivity and has established measures to address it.

Then, it is committed to enhancing shareholder return. The consolidated

dividend payout ratio was raised significantly from the level in the past, and the dividend was increased substantially. These aspects may have caught the attention of investors and led to the rise in the stock price. That they have indicated cash flow allocation is also worth noting.

Next, if you look at the other document, the “progress status” disclosure document, you will see that it carefully describes the progress of the initiatives.

On the other hand, the other company’s stock price performance dropped by over 20%.

While there is a huge volume of materials and analysis has been conducted, the stock price does not seem to be on the verge of an upturn, possibly because the company’s strategies for growth and shareholder returns are insufficient for the market’s needs.

[Kikuchi, Director, Listing Department, TSE]

Thank you.

I would now like to use the remainder of the time to ask for members’ comments on the topics we would like to discuss today, based on Document 3 that you have in front of you. If you have any questions for Mr. Kamio, please also use this time to ask those questions.

We welcome comments or questions from anyone.

[Kumagai, member]

I would like to give my personal opinion on the six items listed in the TSE explanatory materials in Document 3.

First of all, regarding item (1), the date for the termination of transitional measures. Mr. Kamio mentioned the word “metabolism” in his explanation and I believe that one of the biggest themes of this Follow-up Council is to promote the metabolism of the market.

I see how to create a system that allows a healthy metabolism to function as our major mission. In this sense, it goes without saying that leaving transitional measures in place forever will prevent the promotion of metabolism.

From the outset, transitional measures were established as a way of easing the drastic changes in the system, and I believe they are merely exceptional measures. The longer the exceptions remain, the less effective market

restructuring will be.

In addition, given that transitional measures are not applied for companies that listed after the market reorganization in April 2022, I believe it is also important to terminate the transitional measures and put the treatment of all listed companies on an equal footing.

On the other hand, I understand that a certain amount of time is needed to implement reforms internally at companies and achieve results. In fact, I have seen some companies steadily accumulating results by disclosing their plans and implementing various corporate actions to satisfy the criteria for continued listing. We must also consider encouraging such positive initiatives by companies.

Taking all of the above into consideration, I suggest setting March 2025, three years after the market reorganization, as the date for termination. Even if a company becomes non-compliant with the criteria for continued listing after March 2025, the transitional measures will not apply. Given this, why not terminate the extension and renewal of the planning period for existing companies subject to the transitional measures?

From a listed company's perspective, there is generally a one-year improvement period after the end of the transitional measures, so in effect, the company can implement improvements until March 2026.

However, this improvement period is an opportunity to consider moving to another market segment or taking action toward delisting if it becomes difficult to meet the criteria for continued listing. In order to make the market more aware that there are companies in such situations, I believe that TSE should consider disclosing the beginning of the improvement period.

Next, regarding (2), the handling of companies that have already disclosed plans that extend past the termination date. Since some of the companies that plan to terminate their plans after March 2025 have been successful in meeting the criteria for continued listing, I think it would be good to introduce a provision that evaluates those companies.

For example, in the case of the market capitalization of tradable shares, have

a system that gradually raises the criteria, like setting at 8 billion yen by March 2026, and finally aiming at 10 billion yen by March 2027. However, this would be an exception within the exception that is transitional measures, so it must be a simple provision.

Next, regarding (3), the handling of companies that newly disclose a planning period that goes beyond the termination date. Some time has passed since the market restructuring and because the minutes of these meetings have been made public, it would seem that listed companies are becoming more aware of the market restructuring aims and the system.

I believe that companies that have newly established and disclosed a plan period that goes beyond the termination date should be required to enter an improvement period after March 2025, which coincides with the end of transitional measures.

Next, regarding (4), I'd like to comment on extending the plan period to a date prior to the termination date. I don't think there is any need to set a limit on the extension of the planning period when the planning period is extended to a date prior to the termination date.

The market looks at disclosures by listed companies, and we should leave such actions to be evaluated by the market. I believe that easily extending the planning period could have a negative impact on stock prices.

Moving on to (5), and whether to treat different market segments differently. From the perspective of promoting metabolism, the termination deadline should be the same for all markets.

On the other hand, for companies that have already disclosed a planning period that goes beyond the termination date, I said that TSE should consider introducing a provision to evaluate the results of their efforts, and one idea would be to change the treatment based on that evaluation method.

For example, in light of how difficult it is for companies listed on the Standard Market, to which transitional measures have been applied, to move to another market segment, if the evaluation deadline for the Prime Market is set for March 2027, the deadline could be set later or the speed of raising the criteria could be slowed down.

Regarding (6), whether institutional support for segment transfers is necessary following the termination of the transitional measures. I assume that a certain number of companies will change their market segment, such as from the Prime Market to the Standard Market, when transitional measures are terminated.

In principle, a change of market segment requires initial listing application procedures. However, when many companies apply for initial listing, securities firms are required to respond to the market segment changes of existing companies, in addition to IPO investigation. As was discussed during this Council's third round of hearings with market participants, depending on the number of IPOs, it is undeniable that it may become difficult in practice to respond to the market segment transfers.

In light of this possibility, the procedure for moving from the Prime Market to the Standard Market, which is assumed to be the most common direction, albeit on a temporary basis should, ideally be simplified.

Finally, regarding other matters, I understand that there was some discussion about the creation of a secondary trading venue for delisted issues so that a certain amount of trading can take place even after delisting.

If a new market were to be created, it would take an enormous amount of time and would require various system investments by the companies involved. Given this, I believe that extending the system for designating securities under supervision/securities to be delisted, as suggested by TSE, would be a realistic solution.

[Sampei, member]

This is Sampei. I will start by stating my conclusions, and then I will explain my reasons.

Regarding (1), I believe that transitional measures should end after three years, at the end of March 2025.

Regarding the deferment period in (2), I believe that for companies that have disclosed plans that go beyond the three years as of the announcement of the end of the transitional measures, the maximum deferment period should be five years, until the end of March 2027, however, the name of the company, details of outstanding issues, and the deadline for the plan should be announced by

TSE and the company concerned.

Regarding updates to plans in (3), I believe that, in principle, extensions should not be allowed after announcing the date of the end of transitional measures.

While I accept extending the plan period until termination in (4), I believe that the name of the company, the details of the unachieved issues, and the deadline for the plan should be disclosed by TSE and the company in question.

For (5), I believe that the points should not be treated differently for each market segment and that no institutional support is necessary when changing market segment in (6).

The reason for setting three years for item (1) is that there is a public consensus that three years is the general lead time required to achieve business plans such as mid-term plans, and in fact, 60% of companies disclose plans for conformity within a period of three years.

In addition, many investors' opined in the call for comments that period of about three years is appropriated, and page 4 of Document 3, which I think is a very interesting analysis, indicates that three years is also an acceptable period for the market.

The reason I stated that the maximum deferment period should be 5 years for item (2) is due to considering the fact that five years can cover 94% of the companies to which the transitional measures apply. As mentioned earlier, the longer the planning period, the lower the market valuation, which means that it will be difficult to improve market capitalization by extending the period further, and this is not an effective measure to begin with.

As for the reason for establishing a deferment period, I believe that it was a failure on the part of TSE not to set a deadline in the first place, and suddenly setting a deadline later is a grave responsibility. Companies should have given proper consideration to market selection. There is a concern that backtracking on that consideration will create distrust.

However, at the same time, there is a problem with the attitude of companies that easily use or extend transitional measures. Therefore, as I mentioned earlier, it is necessary to publicize the name of the company, the details of the unachieved issues, and the deadline for the plan, and to encourage early

achievement of the criteria through so-called “name and shame” methods.

What is important is that, by publishing such information, it will be stored in an information database through primary information vendors, and institutional investors will be able to screen and find out which companies are eligible for (2) deferral, and what their status is, even if the plan is due to end by the end of the transitional measures.

This information will also be communicated to general investors through information dissemination services that use information databases, and this will help them understand the situation at the companies in which they are investing and increase predictability for investors.

We have also made it clear that to begin with the three market segments were designed based on different concepts and that there is no hierarchical relationship.

Therefore, a hierarchical transition from the Prime Market to the Standard Market, or from the Standard Market to the Growth Market, would run contrary to their concepts. Such a blurring of design concepts at such an early stage as this will lead to inconsistency in future decisions and is very dangerous.

Regarding the examination capacity, I think we have no choice but to examine them in order. We should let listed companies know as soon as possible about the lead time required for the examination and the possibility that the examination capacity may become strained as we approach the termination of transitional measures, and we should inform companies of the need to consider this issue as soon as possible.

[Nagami, member]

This is Nagami. I will also start off by stating my conclusions.

Regarding (1), I believe it is appropriate to terminate transitional measures across the board at the end of March 2025.

With regard to (2) and (3), I believe that deferral beyond the termination date should not be allowed, and with regard to (4), I believe that there should be a possibility of an extension until the end of March 2025.

Regarding (5), my stance is that the same treatment should be applied

regardless of market segment, and regarding (6), I think that examinations should be simplified.

Looking back on our discussions at the Follow-up Council, we received various feedback from domestic and foreign investors during the initial discussions, and I think there was a lot of discussion about the complexity of the market segmentation change and the message and other information were not conveyed.

While the transitional measures themselves are appreciated as a system that is kind to issuers, I think we should always remember that the subject of our discussions are investors, and I think it is important to have a clear line of communication between exchanges and investors.

From this perspective, I believe that it is of utmost importance to terminate transitional measures across the board within three years of market restructuring and to make the rules and operations as clear and simple as possible. No further deferrals should be allowed after that.

Also, as Mr. Sampei mentioned, 60% of companies can be covered in three years, and as a matter of fact, 10% of the companies meet the criteria within the first six months after market segmentation. If we simply multiply this figure by six, we would still be able to cover about 60% of the companies.

One point I find worrying, and I would like to ask TSE about this as well, is that page 6 of Document 3, refers to a “one year improvement period”, and I believe that the period during transitional measures is also, in a sense, a period of improvement and so I would like to know the difference between the “transitional measures period” and the “period of improvement”.

For example, can a company continue to be listed during the improvement period if it complies with the criteria?

[Kikuchi, Director, Listing Department, TSE]

The improvement period will be the period granted regardless of whether transitional measures are applied. For example, companies newly listed on or after April 4, 2022, are not entitled to transitional measures and are therefore subject to the new system, but they are given a one-year improvement period if

they violate the criteria at the end of the fiscal year.

You are correct that we are still, in effect, in the improvement period for companies that are currently subject to transitional measures.

[Nagami, member]

In that case, as it relates to my concerns, I think that the transitional period, including the improvement period, could be terminated after three years. So assuming a one-year improvement period, I wondered whether March 31, 2025 or March 31, 2024 would be better as the end date for transitional measures, and I thought March 2024 would be somewhat radical so, as I said earlier, I think it should be March 31, 2025.

[Kanda, member]

Regarding (1), common sense dictates that the shortest period should be two years, and the longest should be five years at most.

As was mentioned earlier, if we extend the period to March 2025, that would be three years counting from April of this year, when the new market segments was introduced, and I think is reasonable.

Regarding (2), once a rule has been announced and approved, it is not possible to subsequently make a new rule and to apply that rule retroactively and then not permit plans upon the termination of the transitional measures, so I think plans must be approved.

Regarding (3), since companies are not applying transitional measures at this time or have not disclosed a plan that extends past the termination date, it really depends on the new rules that will be drafted. I think there are a number of ways to draft rules. I think there could be a rule that disclosure is not allowed in principle, or a rule that it is allowed until the end of transitional measures.

However, regarding the timing of application, as Mr. Sampei mentioned earlier, I wonder when the rules for the end of transitional measures will be announced and when they will take effect. If they are to take effect on April 1 of next year, then I think we will have to allow disclosure until the day before the effective date.

Regarding (4), if a plan has already been disclosed and the right to an

extension is based on the current rules, then extensions will have to be permitted, until the day before the effective date of the new rules. In other words, if April 1 is the effective date, I feel that we must grant extensions as with (4) until March 31. However, we need to check the current rules carefully. I feel that this is just a technicality and is something that should be decided.

Regarding (5), I do not think different treatment is necessary, but listening to what others have said, I feel that there are multiple items in the criteria for continued listing, and of the companies that are said to be in violation of the criteria, some companies are in violation of only one item and others are in violation of two or more items. In some cases, it might be possible to allow different treatment of companies which are only violating one criteria.

Or, a slightly more flexible approach could be taken by, for example, devising a method for calculating the market capitalization of tradable shares.

At any rate, I don't think we need to treat market segments differently. I feel that we could consider examining each criteria in detail, or rather we could conduct detailed examinations. In principle, I don't think this is necessary, but I think there may be something we can do to adapt slightly to the actual situation.

Regarding (6), I think that in principle it is not necessary to offer institutional support.

However, as Mr. Sampei has already mentioned, the structure on the TSE side could be an issue. If it can be handled by publicizing it as early as possible, that should not be a problem, but if that is not possible, I think some simplification is inevitable.

Finally, I would like to make one more point regarding the delisting process and the receptacle on page 6 of document 3. I agree with what is written here. I think a period this long is a good length of time, and I think it is realistic to utilize the current system of Securities Under Supervision and Securities to Be Delisted.

[Ando, member]

Listening to everyone's opinions, I get the impression that everyone's basic direction is almost the same.

From the standpoint of a company, I am worried that some continued listing criteria are difficult to improve just through self-help efforts. However, as a listed company, indicating management self-worth is also an important responsibility, so in conclusion, I believe that (1) should be terminated across the board at the end of March 2025.

On the other hand, Mr. Kanda made some legal comments, I think it would be good for the secretariat to put together a list of pros and cons, including legal perspectives, on the assumption that (1) will terminate by the end of March 2025, and then for us to work out the specifics.

Incidentally, the point Mr. Kanda made regarding (2) is a point that I have also been struggling with, and it is important to consider whether the termination date set voluntarily should be recognized as a “right”, since companies submitted conformity plans without there being any clarification in advance as to how long the transitional measures should be allowed, and whether it is acceptable to define “for the time being” ex post facto.

Another issue to consider when deciding when to end the planning period is capacity, such as the listing review by TSE. In this sense, it is necessary to consider the procedures for changing the market segment from the Prime Market to the Standard Market.

As Mr. Sampei has pointed out, market segment is only based on function and not on market hierarchy, so it may be difficult in terms of logic, but I am concerned about the administrative burden on TSE of having to redo the formal listing examination for market transfers.

I would like to reiterate my request for us to identify items for practical, not just ideological, consideration, including legislative aspects and practical issues for TSE and securities companies.

[Kuronuma, member]

It is difficult to make a decision based on logic, and I think that everyone has made valid comments. That said, I would like to state my own feeling on the matter.

Regarding the end of the transitional measures in (1), I said at the first

meeting that five years would be acceptable, but taking into account that it is important from the perspective of clarifying the concept as a market to end transitional measures at all companies as soon as possible, as has been mentioned, I am now thinking that three years, or three years plus a one year improvement period would be best.

Regarding (2), I am having trouble deciding this one, but I don't think there is any legal need. However, I think it would be better to allow exceptions, but to limit those exceptions to five years.

Regarding (3), if it is assumed that companies that have disclosed plans that extend past the termination date, before the announcement of the termination date, will be treated the same as (2), then I think some companies may rush to disclose plans just before the termination date is announced.

Since listed companies should be aware that we are discussing when to terminate measures at these meetings, I think it would be better not to allow (3) in order to carry out the intent of (1), which is to terminate transitional measures across the board as soon as possible.

Regarding (4), if it means that companies that had a plan with a period shorter than the termination date, will be delisted if they fail to achieve the plan in that shorter period, then this is different from the concept in (1). If the purpose of (1) is important, then I think it would be better to terminate transitional measures at all companies in March 2025 or one year after that.

Regarding (5), I believe that different treatment for each segment is unnecessary.

Regarding (6), I do not have the information to make a decision at this time, but I believe that it is an issue to be decided by taking into consideration the prospects at TSE.

[Matsumoto, member]

I think that the transitional measures should end in March 2024.

I also think that the flow leading up to delisting on page 6 of Document 3 should be as described. There is a one-year improvement period even if the

criteria for continued listing are violated, so even if the transitional measures terminate at the end of March 2024, companies effectively have three years, and I think that is sufficient.

In addition, the various deferrals and extensions that are mentioned in (2) onwards should, in principle, not be granted.

The reason being that, I believe that there are usually also rule changes that originate with TSE, and that not all of them have to be approved because companies are permitted to come up with long plans. From the outset, I believe that this discussion itself is creating new rules and such rules do not need to be tied to the past.

I get the impression that discussions are based on the premise that individual companies should be able to maintain their listing through their own efforts. However, in Japan, the problem is that production factors are dispersed among various companies, resulting in inefficiency and low productivity. If the TSE rule can encourage companies to increase their productivity through exchanges and mergers of production factors, rather than individual companies trying to comply with the listing criteria, this will lead to an improvement in the productivity of listed companies in general and in society as a whole.

From this perspective, I believe that rather than giving consideration to ensuring individual companies conform, which they will not be able to do in time, it would be better to create rules that put pressure on companies to merge or break up, and exchange production factors.

[Koike, member]

I basically believe that it is okay for measures to continue until March 2025, for basically the same reasons as everyone else.

The key is discipline and reliability, and it is important to encourage metabolism in a disciplined market. Since transitional measures were initially established without setting a deadline, if measures are suddenly terminated without taking this into consideration, the credibility of listing rules will be lost not only among listed companies but also among various investors, including overseas investors, and I think this point should be kept in mind.

Although transitional measures are one of the issues to be discussed at this meeting, how to improve corporate value in the Prime Market, the Standard Market and the Growth Market, and how to nurture the Japanese stock market are more important topics, and I feel that publicizing disciplined market rules will also link to the governance activities of TSE as an exchange.

In that sense, I originally thought that a deferment period beyond the termination date was not necessary. However, listening to today's explanation, and looking at the actual progress and efforts of each company and other positive aspects, I believe that consideration should be given to companies that are putting out such information. Conversely, companies that are not communicating such information, even if they remain in the market, may not have the sense of responsibility needed to be listed on the stock market, so I thought, reading through today's handouts, that it would be a good idea to differentiate between them.

[Kikuchi, Director, Listing Department, TSE]

Thank you. We have heard comments from everyone, but there is still some time left, so if you have anything else you would like to say, please go ahead.

[Matsumoto, member]

I understand that corporate governance reform is basically a movement to incorporate the perspectives of investors and shareholders into the design of capital markets and the management of companies. Document 5 is a summary of the comments submitted. I would suggest that TSE create a contact point for accepting comments from investors and shareholders on a permanent basis.

For example, the Securities and Exchange Surveillance Commission (SESC) has a contact point that accepts submission of information if there is a problem and this has been the catalyst for many things. I think it would be a good idea for TSE to establish a permanent contact point where institutional investors or individual investors can offer their opinion, at any time, about what is wrong with a company or what is wrong with a rule.

[Nagami, member]

I would like to make two comments.

First, since time is still running out during this period, I believe that the

roadmap should be clarified as soon as possible and announced promptly at the beginning of the year, since I guess it will be difficult to announce it by the end of the year. I believe that this is extremely important to avoid further extending transitional measures.

While the discussion of transitional measures is important, other issues discussed thus far have been how to handle companies with low ROE and PBR. In this regard, as we heard during the presentation, I believe that we should have another discussion about the index and that we should compile a roadmap of actions to be taken.

[Kikuchi, Director, Listing Department, TSE]

I am sure you are aware of what you have said, but the index is being formally discussed at JPX Market Innovation & Research. Of course, we would like to receive your comments in some form in the future.

[Sampei, member]

I forgot to mention earlier that it seems hard to understand why the criteria are raised in stages. Ultimately, it is important that general investors and foreign investors be able to use the database to conduct simple screening and grasp the current situation, and confusion will arise unless information is conveyed without error.

I think we need to make the system simple, while considering the information transmission channels, such as how the information is ultimately conveyed to the people making investment decisions, and how it is disseminated.

[Kikuchi, Director, Listing Department, TSE]

Thank you. Finally, I will explain the schedule for next time.

[Ikeda, Senior Manager, Listing Department, TSE]

Thank you very much for the lively discussion again today.

From the next meeting onward, we would like to proceed with discussions with a view to organizing the issues, including ways to encourage improvements to PBR and ROE, which is something we have discussed in the past. That covers everything.

[Kikuchi, Director, Listing Department, TSE]

With that, I hereby declare today's meeting adjourned.

Thank you very much for your participation today. We look forward to talking to you all again at the next meeting.

End