
FY2019 Annual Stewardship Activity Report Summary

March 2020

The following is the summary of FY2019 Annual Stewardship Activity Report of the Pension Fund Association for Local Government Officials (the "Association").

1. Overview of stewardship activities by asset managers entrusted with stock investment

The Association observed improved efforts of asset managers' stewardship activities with the enhanced level of the overall activity. In addition, some asset managers implemented new, excellent initiatives which suggest the increased efficiency of stewardship activities of asset managers.

(1) Exercise of voting rights

It was confirmed that almost all asset managers entrusted with domestic and foreign stock investment exercised voting rights in compliance with the matters which the Association considers important, while implementing new, excellent initiatives.

- Compliance with the Association's guidelines
 - It was learned that all asset managers exercise voting rights in accordance with account criteria (specific criteria for exercising voting rights related to accounts entrusted by the Association) reflecting the Association's guidelines (domestic equities).
- Exercise of voting rights suited to the circumstances of companies
 - It was learned that when exercising voting rights in ways deviating from the principles of the account criteria, some asset managers are implementing an excellent initiative of making judgement separately through a committee, etc. (domestic and foreign equities).
 - It was also learned that some asset managers using an external service for the exercise of voting rights are implementing an excellent initiative of periodically examining service providers' advice-providing capability (domestic and foreign equities).
- Exercise of voting rights and engagement in an integrated manner
 - While almost all asset managers have already implemented the exercise of voting rights and engagement in an integrated manner, additional asset managers changed their process to achieve the integrated implementation (foreign equities).

In relation to the results of the exercise of voting rights, the following are the major proposal subjects for which the vote-against rate rose.

- Proposals related to the board of auditors/auditors (domestic equities)
⇒The vote-against rate rose to 21.1% (up 6.1 points from the previous year) due to such factors as the presence of asset managers that tightened the criteria related to outside auditors' independence as it did in the previous year.
- Proposals related to director remuneration, etc. (domestic equities)
⇒The vote-against rate rose to 23.2% (up 3.8 points from the previous year) due to such factors as the presence of an asset manager that revised the criteria so as to require a vote against the payment of retirement allowances in principle.
- Proposals related to director remuneration, etc. (foreign equities)
⇒The vote-against rate rose to 12.5% (up 2.6 points from the previous year) due to such factors as change of the benchmark and also because some asset managers shifted to the approach of closely examining all proposals.

(2) Engagement

It was confirmed that all asset managers entrusted with domestic stock investment and most of the asset managers entrusted with foreign stock investment implemented engagement activities in compliance with the matters which the Association considers important, while implementing new, excellent initiatives and specific initiatives.

- Engagement aimed at enhancing corporate value and sustainable growth
 - It was learned that all asset managers are conducting engagement activities aimed at enhancing corporate value and sustainable growth of investee companies (domestic equities).
 - It was learned that almost all asset managers are conducting engagement activities aimed at enhancing corporate value and sustainable growth of investee companies. On the other hand, the Association observed some cases in which asset managers' understanding of the engagement required by the Association was insufficient (foreign equities).
- Effectiveness of processes (e.g., PDCA cycle)
 - It was learned that all asset managers examined the effects of engagement and judged the success or failure of engagement (domestic equities).

- An excellent initiative by an asset manager was observed which resulted in further improvement of the engagement process by such way as conducting more detailed milestone management and enhancing management tools (domestic equities).
- Another excellent initiative was observed in which an asset manager established a committee to report engagement activities in a concentrated way so as to ensure sufficient discussion (domestic equities).
- Specific examples of engagement
 - Some cases of initiatives to improve the effectiveness of engagement were observed, such as discussion for connecting quantitative ESG evaluation to the calculation of corporate value and utilizing it for engagement, conducting dialogue with outside directors to confirm the effectiveness of the board of directors and encouraging companies to reduce cross-shareholdings (domestic and foreign equities).

The summary of the results of engagement activities is as follows:

- While some asset managers changed their structures for engagement by such way as increasing engagement staff and improving efficiency, others focused on engagement related to ESG. As a result, the number of cases of dialogue was 16,631 (up 16.2% from the previous year) for domestic equities and 4,071 (up 12.6% from the previous year) for foreign equities.

2. Overview of the Association's stewardship activity

The Association is required to fulfill its fiduciary responsibility of increasing the value of its assets for the insured over the long term and social responsibility as a public pension fund. In this connection, as the means to seek medium- to long-term enhancement of corporate value and sustainable growth of investee companies, the Association has been proactively committed to stewardship activities.

In addition, the Association entrusts asset managers to make stock investments in companies. The Association believes that conducting the stewardship activities through these asset managers is effective for fulfilling the stewardship responsibility as they have more opportunities to access investee companies and have in-depth insight on corporate management.

The specific initiatives implemented by the Association in FY2019 are as follows:

(1) Monitoring of asset managers in FY2019

For each fiscal year, the Association has been monitoring the stewardship activities of the asset manager of equities. For FY2019, the Association provided feedback regarding the evaluation of stewardship activities in FY2018 individually to entrusted asset managers that requested it.

(2) ESG investment initiative

Most of the active funds concerning domestic stocks adopted by the Association take into consideration ESG elements in the investment process. The Association characterizes funds adopted with the aim of earning excess return from the viewpoints of ESG (4 products) as ESG funds. In FY2019, the Association started investing in ESG bonds as part of in-house investment in domestic bonds.

3. Future initiatives of the Association

The Association will consider expanding the scope of assets covered by stewardship activities in light of factors such as governmental actions. The Association will also conduct necessary activities after considering promoting investment taking into consideration non-financial factors, including ESG factors, in addition to financial factors.