

## Sustainable Signals:

Understanding Individual Investors' Interests and Priorities from the Perspective of Japan

There are encouraging signs of demand for sustainable investing in Japan, according to [the latest “Sustainable Signals” survey](#) by the Morgan Stanley Institute for Sustainable Investing. Just over half (56%) of individual investors surveyed in Japan are interested in sustainable investing, and 29% say they are likely to increase their allocation to sustainable investments in 2024.

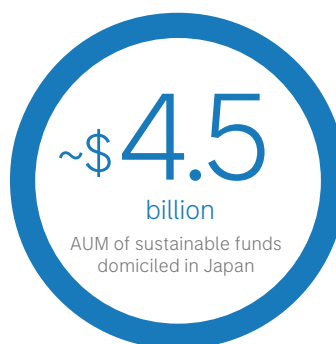
For individual investors, performance remains important with the survey indicating that Japanese investors prioritize maximizing financial returns (83% of respondents) over advancing positive social or environmental impact (74% and 72% respectively), with a majority believing that they can achieve both. Only 42% say that sustainable and financial gains are a tradeoff, versus over 65% in US and Europe. Furthermore, over 80% of Japanese individual investors say companies should address environmental and social issues, on par with US and Europe.

# 80%+

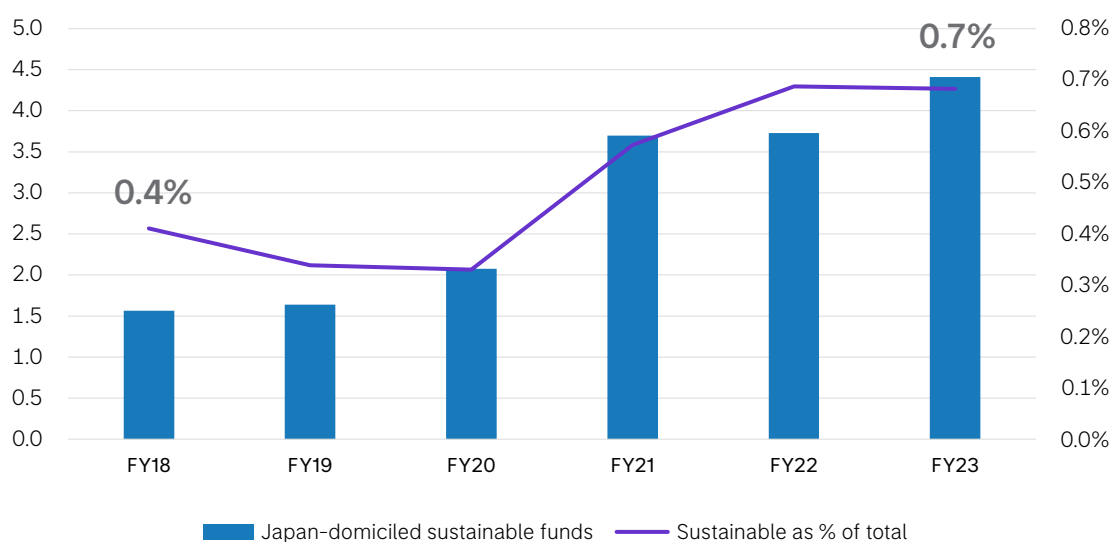
Japanese individual investors say companies should address environmental and social issues on par with US and Europe.

Majority of Japanese individual investors believe they can achieve both financial returns and positive social or environmental impact.

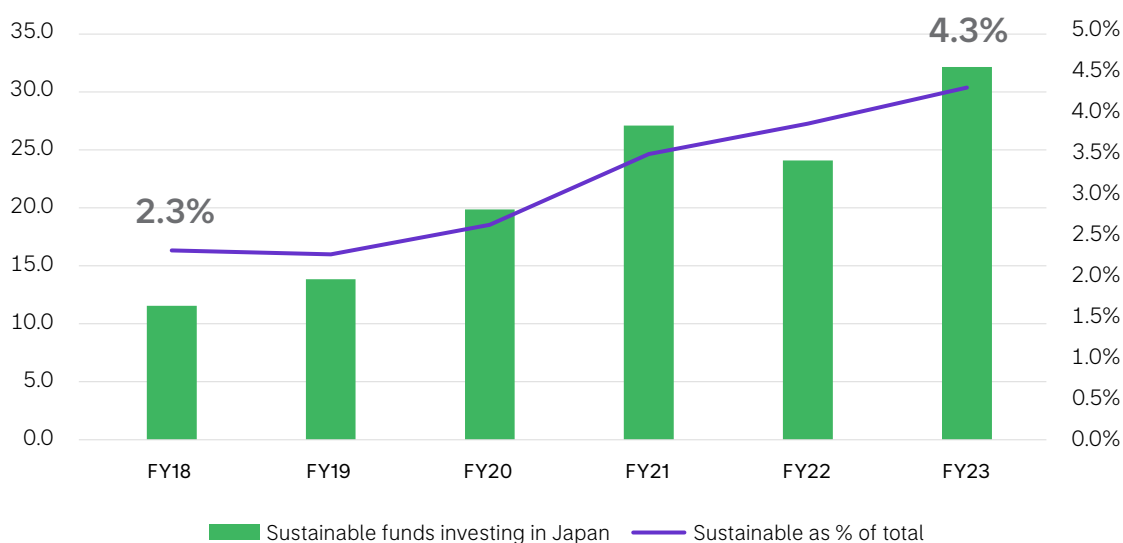
This comes at a time when sustainable assets under management (AUM) in Japan have been on an upward trend with the AUM of sustainable funds domiciled in Japan at ~\$4.5 billion and with those invested in the country at \$32 billion.



### Japan-Domiciled Sustainable Funds AUM (USDbn)



### Sustainable Funds Investing in Japan AUM (USDbn)



Source: Morningstar data as of Feb 9, 2024

These numbers still trail those of Europe and the U.S., where over 80% of investors express interest in sustainable investing, and sustainable AUM reached \$3 trillion and \$330 billion respectively in 2023.

So, what opportunities exist that may drive further adoption of sustainable investing in Japan and better meet growing investor demand?

## Improve Data Quality and Transparency

Amongst Japanese individual investors, the biggest perceived barrier to sustainable investing is lack of transparency and trust in reported data. But there are signs that this may change. The Japanese Financial Services Agency (FSA) has mandated companies required to file an annual securities report including all listed companies in Japan, to disclose sustainability related information in the annual securities report from March 2023. In addition, upcoming issuance of draft sustainability disclosure rules in March 2024 by the

Sustainability Standards Boards of Japan (SSBJ) will encourage Japanese corporates to improve their ESG disclosures, with the final standards scheduled to be issued no later than end of March 2025. This should help investors gain greater access to more consistent and comparable ESG related disclosures across industries and markets, which may lead asset managers to have more conviction over adopting a sustainable investment strategy.

## Increase Sustainable Investment Product Offerings

An ambitious government strategy, known as the Asset Management Strategy<sup>1</sup>, to channel substantial Japanese household financial assets of \$14 trillion from savings into investments may also help drive sustainable investing in the region. On average, Japanese households keep more than half of their assets in cash<sup>2</sup>, which is significantly higher compared with 13% in the U.S. and 35% in Europe. The Japanese government is working to change this and incentivize households to allocate more of their assets to investment products. As part of this initiative, Investment Trust Association of Japan announced the inclusion of new sustainable investment products such as sustainable mutual funds and ETFs to the list of New Individual Savings Account (NISA<sup>3</sup>) eligible products.

An ongoing challenge is that at the moment, of the over [2000 products](#)<sup>4</sup> that are now under the individual tax incentives scheme, only around 80 are sustainable investment products. Investors have a sense of this

limited availability, with 44% of Japanese individual investors interested in sustainable investing citing lack of financial products available for their portfolio.

For asset managers considering how to increase the number of available products, our survey suggests that key themes to address are “Climate Action”, “Healthcare”, and “Circular Economy”, as these were the most popular themes amongst Japanese individual investors interested in sustainable investing. Our analysis of existing sustainability funds suggests that Climate Action is well represented but there could be potential for further investment in health-related themes.

In addition, the supply of climate action products could be boosted by the Japanese Government’s Green Transformation Plan<sup>5</sup>, which requires around \$1 trillion in initiatives, of which over 80% needs to come from private sector.

<sup>1</sup> FSA's Report on Working Group on Capital Market Regulations and Asset Management Task Force of the Financial System Council: [01.pdf \(fsa.go.jp\)](#)

<sup>2</sup> BOJ “Basic Figures – Flow of Funds for the Third Quarter of 2023” report published on Dec 20, 2023.

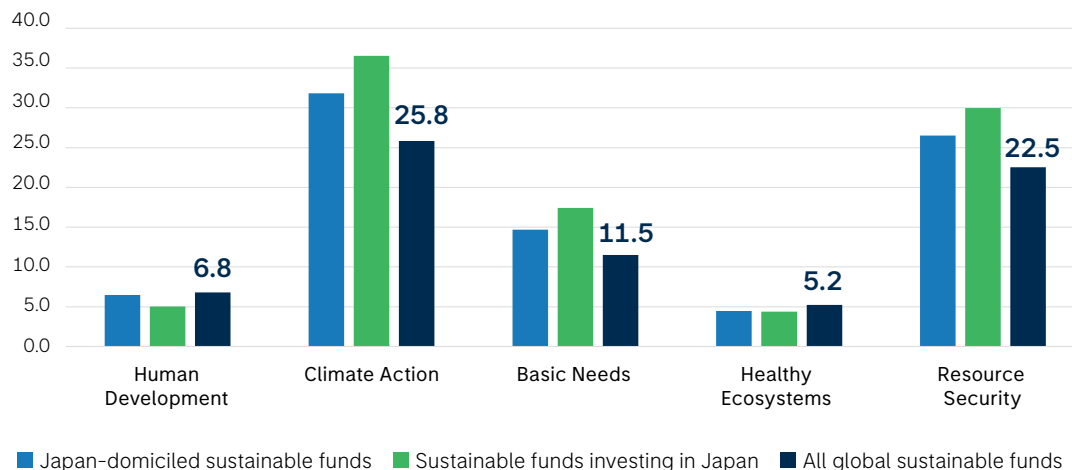
<sup>3</sup> NISA refers to an expanded tax-exempt investment vehicle to help spur investment by individual investors.

<sup>4</sup> NISA eligible products last updated on Feb 9, 2024 for mutual funds and Jan 18, 2024 for ETFs, REITS, etc.

<sup>5</sup> Outline of the Basic Policy for the Realization of Green Transformation: [https://www.meti.go.jp/english/press/2023/pdf/0210\\_003b.pdf](https://www.meti.go.jp/english/press/2023/pdf/0210_003b.pdf)

### Equity Fund Exposure to Sustainability Themes

average % of portfolio involved in theme



Source: Morgan Stanley Institute for Sustainable Investing, "Sustainable Signals: Understanding Individual Investors' Interests and Priorities." Data as of January 26th, 2024.

## Help Inform Investors on Sustainable Investing

Maximizing financial returns are the top priority for Japanese individual investors, and a majority believe that it's possible to do that while also advancing positive environmental and social impact. Our survey showed, however, that individual investors are looking for more guidance on how to do this. Over half of Japanese individual investors interested in sustainable investing expressed limited knowledge about how to get started in sustainable investing (53%), and they indicated that they lack the tools necessary to measure sustainable impact

(56%), with more than one-third conveying a lack of financial advice.

This provides Japanese Financial Advisors and Asset Managers an opportunity to upgrade their expertise in sustainable investment to help educate their clients and better understand their needs, and by offering a more diversified and targeted products that can be a solution for their investment objective and goals.

### In summary, to meet growing individual investor demand in Japan, there are opportunities to:

- Improve data quality and align corporate sustainability disclosures with the ISSB/SSBJ standards.
- Channel \$14 trillion of Japanese household financial assets from savings to investments via new government incentives and include sustainability products by the Investment Trust Association of Japan to the New Individual Savings Account (NISA) platform.
- Increase the number of available sustainable product offerings from asset managers, taking into account key themes of interest, as well as industries that are currently underinvested in need of transition finance.
- Continue to grow the sustainable investing expertise of financial advisors and asset managers to better educate and inform investors.



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