

How Institutional Investors Fulfill Their Stewardship Responsibilities (Overview)

The Japanese Stewardship Code defines the stewardship responsibilities of institutional investors as "the responsibilities of institutional investors to enhance the medium- to long-term investment returns for their clients and beneficiaries by improving and fostering the investee companies' corporate value and sustainable growth through constructive engagement, or purposeful dialogue, based on in-depth knowledge of the companies and their business environment." However, enhancing corporate value and expanding investment returns through purposeful dialogue is a classic case of being easier said than done. Therefore, fulfilling stewardship responsibilities requires various approaches.

The keys to fulfilling stewardship responsibilities are "practicality" and "efficiency." Practicality refers to ensuring the investment strategy process directly connects to activities that enhance the corporate value of investee companies and expand investment returns—that is, activities directly linked to stewardship responsibilities. Efficiency refers to whether the process for fulfilling stewardship responsibilities, particularly in passive management, is carried out efficiently without excessive effort.

Engagement activities genuinely aimed at enhancing corporate value and increasing investment returns have been executed in a wide variety of ways and require detailed company analysis, demanding significant effort and a high skill set. Therefore, effectiveness cannot be achieved without sacrificing efficiency. On the other hand, passive management, with its high holding ratios, emphasizes efficiency. Setting strict voting standards enhances management discipline and improves governance levels in listed companies. Funds flowing into engagement funds and long-term concentrated investment funds atop the passive investment foundation help resolve management challenges at their portfolio companies. From the perspectives of practicality and efficiency, a scenario in which both passive investment and concentrated active investment focused on enhancing corporate value serve as the wheels of a cart to drive the corporate value of portfolio companies higher seems both desirable and realistically achievable.

While asset owners should primarily allocate capital to active management that enhances corporate value, when investing in passive management, they must use asset-owner-led collaborative monitoring mechanisms to fulfill their role efficiently.

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1. What is the Stewardship Responsibility of Institutional Investors?

What is the stewardship responsibility of institutional investors? The Japanese Stewardship Code (hereinafter referred to as SC), established in February 2014, defines it as “the responsibilities of institutional investors to enhance the medium- to long-term investment returns for their clients and beneficiaries by improving and fostering the investee companies’ corporate value and sustainable growth through constructive engagement, or purposeful dialogue, based on in-depth knowledge of the companies and their business environment.” The SC has since undergone three revisions. The latest revision, implemented in June 2025, adds the following wording regarding **consideration of sustainability**: “(Omitted) through constructive engagement, or purposeful dialogue, based on in-depth knowledge of the companies and their business environment and **consideration of sustainability (medium- to long-term sustainability including ESG factors) consistent with their investment management strategies**”.¹⁸ (Note 1) was added, incorporating sustainability considerations. In all definitions, stewardship responsibility refers to the duty to enhance the long-term investment returns of “clients and beneficiaries” by promoting the corporate value and sustainable growth of the relevant company through engagement activities and other means.

Furthermore, the establishment of the Asset Owner Principles (hereinafter referred to as AOP) in August 2024 explicitly states that asset owners (such as pension funds) should also fulfill stewardship responsibilities. Consequently, even when outsourcing management to asset managers, asset owners must now be mindful of stewardship responsibilities. Specifically, Principle 5 of the AOP states: “Asset owners should take the necessary steps to contribute to the sustainable growth of investee companies, such as conducting stewardship activities either directly or through their investment managers, when pursuing investment objectives for the benefit of beneficiaries and others.”

Meanwhile, various investment strategies exist for equity investments. Broadly, these can be categorized into passive management, which tracks a specified benchmark, and active management, which aims to achieve excess returns relative to the benchmark. The investment objective of passive management is to track the specified benchmark. Since it requires holding the benchmark's constituent stocks continuously, it is inherently an ultra-long-term investment.

Active management encompasses a highly diverse range of investment strategies,

(Note 1) The bold text was not originally included in the SC and was added later.

differing in elements such as investment decision-making methodologies, investment horizons, target company characteristics, the number of holdings, and the flexibility of holding ratios. Examples include quantitative investing, which estimates stock prices and corporate value through quantitative analysis; short-term investing, which focuses on short-term stock price movements and company-related news; and long-term investing, which focuses on corporate value from a long-term perspective. Furthermore, a wide variety of investment strategies exist, including value investing in undervalued stocks where share prices are low relative to book value, growth investing in companies with expected sales and profit growth, concentrated investing limiting holdings to 30 stocks or fewer versus diversified investing across 100 or more stocks, long-only strategies buying positions in target companies, and long-short strategies also taking short positions. Recently, engagement funds have become increasingly active, aiming to enhance corporate value through engagement activities with investee companies.

Amidst these diverse investment strategies, the manner of engagement with investee companies varies greatly, and there are a number of options for fulfilling what SC terms stewardship responsibilities. This paper focuses on Japanese equity investment strategies within this diverse landscape, examining how institutional investors should fulfill their stewardship responsibilities. We explore this from the perspectives of asset managers executing actual equity strategies and asset owners delegating management to these firms.

To state the conclusion upfront, the key to fulfilling stewardship responsibilities lies in "practicality" and "efficiency." "Practicality" means that the investment strategy process directly translates into activities that enhance the corporate value of investee companies and increases investment returns—in other words, activities directly linked to stewardship responsibilities. "Efficiency" refers to whether the process for fulfilling stewardship responsibilities, particularly in passive management, is carried out efficiently without excessive effort. Highly practical investment strategies can also sacrifice efficiency; these two concepts must be applied appropriately depending on the investment strategy.

While considering practicality and efficiency, we first present an example of an engagement fund, considered the most practical, and clarify the challenges that arise in fulfilling stewardship responsibilities through its investment process. Next, we examine what challenges arise in fulfilling stewardship responsibilities from the perspectives of practicality and efficiency for both active and passive management. Finally, we will present our views on collaborative engagement, which has recently

gained attention, and the nature of stewardship responsibilities on the asset owner side, offering an outlook on future approaches to fulfilling stewardship responsibilities.

2. What Are the Challenges in Fulfilling Stewardship Responsibilities?

(1) In the case of engagement funds

The most straightforward example of the stewardship responsibilities of institutional investors is the investment activities of engagement funds (hereafter abbreviated as EFs). While various investment strategies exist within EFs, the term generally refers to funds that engage in discussions with the management of investee companies "to enhance corporate value." As SC states, the investment objective is to engage in purposeful dialogue with investee companies and achieve investment results through proposals that enhance corporate value. The core of the investment strategy is fulfilling stewardship responsibilities itself. If stewardship responsibilities are not fulfilled, investment returns will deteriorate, and asset managers will likely be weeded out. Stewardship responsibilities and investment strategy are literally integrated, making this the most practical investment strategy.

Conversely, examining EF's investment process reveals the inherent challenges of fulfilling stewardship responsibilities. When selecting investees, EFs analyze business environments and other factors, engage external consultants, and carefully assess whether engagement from various perspectives can enhance corporate value. Furthermore, when actually engaging, significant time is required to analyze and meet with each company individually. Due to the effort and cost involved, the number of investee EFs that EFs can engage with simultaneously often falls below ten.

If EF cannot expand medium- to long-term investment returns through engagement, investment returns will deteriorate, making it difficult for the fund to survive. Therefore, EFs must focus entirely on selecting investee companies and conducting engagement activities. In short, fulfilling stewardship responsibilities requires high cost and effort, necessitates engagement skills and passion for engagement, and limits the number of investee companies. Without conducting meaningful engagement activities that enhance corporate value, even at the expense of efficiency, stewardship responsibilities cannot be fulfilled. Therefore, from a stewardship perspective, a practical investment strategy is likely incompatible with the concept of efficiency.

Incidentally, while EFs establish broad voting criteria, many emphasize the strong

individuality of voting decisions, stating they "judge case by case based on the content of dialogue with the management of investee companies." Quantitative criteria applied uniformly across investee companies, as seen in passive management discussed later, are rarely established. Engagement activities and proxy voting are integrated, and proxy voting decisions are highly individualized.

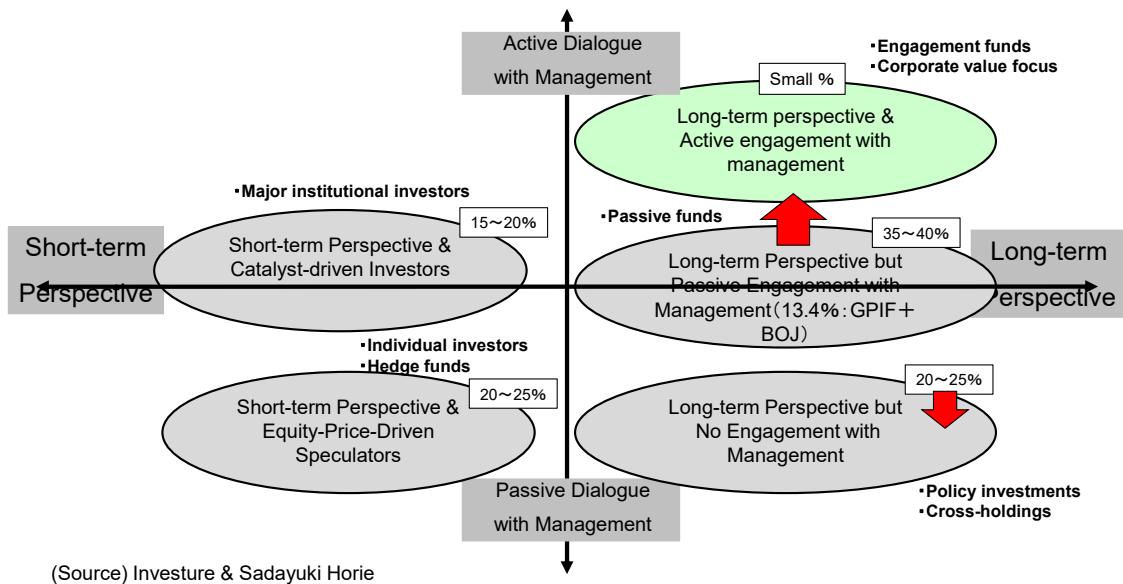
(2) Challenges in Fulfilling Stewardship Responsibilities from a Shareholder Structure Perspective

If investment strategies like EFs were truly mainstream in Japanese equity investing, vigorous discussions about corporate value would occur between investors and management, and criticisms such as stewardship responsibilities not being adequately fulfilled would likely not arise. However, as shown in Figure 1 on the next page, the proportion of Japanese stocks held by investment strategies that actively pursue EFs and engagement activities, such as concentrated investing, is small. The reality is that many investment strategies show little interest in dialogue with investee companies. The horizontal axis of Figure 1 represents whether an investor's evaluation of portfolio companies is short-term or long-term oriented. The vertical axis represents whether an investor prioritizes corporate value when engaging with portfolio companies.

There are rational reasons why many investment strategies show little interest in engaging with investee companies. The primary reason is the lack of incentive for engagement. For example, in short-term investing, the primary focus is on near-term stock price movements. Investors pay attention to events and factors that affect stock prices, as well as to what other investors know, leaving little incentive to discuss corporate value with investee companies. It is self-evident that without an incentive to engage, the capability for meaningful dialogue will not develop.

The second reason is cost. In passive management, the investment objective is to achieve returns close to a predetermined benchmark, resulting in lower management fees compared to active management. Furthermore, passive management requires holding most of the securities included in the benchmark. For passive managers to fulfill their stewardship responsibilities, they need to engage in dialogue with numerous companies. However, covering these costs solely from the management fees paid by clients is difficult. Efficiency is crucial for passive managers to fulfill their stewardship responsibilities precisely because of these management costs.

Fig. 1: Shareholder Structure of Japanese Equities: by Engagement Type and Investment Horizon



Among the objectives of the SC, it is pointed out that “Effective and appropriate stewardship activities by institutional investors ultimately aim to enhance the medium- to long-term investment returns for clients and beneficiaries. Therefore, both institutional investors and their clients/beneficiaries should share the understanding that the reasonable costs associated with implementing stewardship activities are necessary investment costs.” While it is desirable for clients to bear part of the costs associated with these activities, aside from the example of the GPIF (Government Pension Investment Fund) paying additional management fees for its “passive investment with engagement,” there are few reported cases where clients pay additional management fees for stewardship activities.

Some might argue that asset owners and other clients should choose investment strategies with a strong focus on corporate value. However, such strategies are typically long-term and concentrated. They tend to deviate significantly from benchmarks in the short term, making them difficult for clients to adopt. While experts widely acknowledge the significance of long-term investing, it remains a minority approach not only in Japan but in many countries. Given this reality, we should consider what constitutes an appropriate approach to fulfilling stewardship responsibilities.

3. In the Case of Active Management

Since active management encompasses a number of diverse investment strategies,

we will explain how stewardship responsibilities should be fulfilled for each individual.

(1) Investment Strategies with Limited Relevance to Stewardship Responsibilities

First, let us describe active investment processes that are inherently less connected to stewardship responsibilities due to their strategic characteristics. For example, quantitative investing is a strategy that estimates future stock prices and corporate value based on vast databases. Recently, quantitative models have evolved to incorporate diverse information beyond financial statements, such as text data from SNS (social networking services) and data analysis from CEO press conferences (including facial expression analysis). However, these models fundamentally do not incorporate processes involving dialogue with management and are largely unrelated to engagement activities.

Investment strategies with short holding periods also have a tenuous relationship with the stewardship responsibilities defined by the SC. These strategies aim to capture capital gains through short-term trading by estimating stock prices days, weeks, or even months ahead. Consequently, the core of their investment activity involves gauging what information other investors possess and inferring what data is currently priced into the stock. They then make stock price forecasts based on the assumption that their own information will be reflected in the price. For example, they compare their own earnings forecasts with the consensus estimates (the average of earnings forecasts by securities analysts, etc.) published quarterly by companies, and make investment decisions accordingly. While they may visit investee companies to verify information held by other investors, this activity is solely to probe what others know; it does not reflect a deep interest in the company's future trajectory. It is more accurate to describe their relationship with investee companies as "interviews" rather than "dialogue."

Another strategy focuses on catalysts that can impact short-term stock prices. This is known as event-driven investing, which involves gathering information that may signal impending acquisition proposals or estimating bankruptcy probabilities based on data and information relevant to such risks. While they may actively engage with investee companies, their primary focus is on whether some event will occur that significantly impacts the stock price in the short term. Consequently, they have little interest in promoting corporate value enhancement or the sustainable growth of the investee company and do not pursue such purposes. This strategy also involves conducting interviews rather than having dialogues with the investee company.

Given the nature of the investment strategies described here, fulfilling stewardship

responsibilities is not anticipated. Consequently, asset managers should explain that such investment strategies involve "conducting interviews rather than dialogues," as the SC states. Naturally, clients should accept this explanation.

(2) Concentrated Investing

Concentrated investing is an investment strategy that narrows holdings to approximately 30 stocks or fewer ^(Note 2). It possesses distinct characteristics that set it apart from other investment strategies. First, it is an absolute-return-oriented approach, unconcerned with benchmarks. Second, it selects stocks based on a long-term perspective. Concentrated investing evaluates corporate value based on a long-term perspective. While various investment styles exist for estimating corporate value, strategies include selecting companies which are expected to sustain future profit growth sufficient to maintain high ROE, or investing in companies whose stock prices are significantly undervalued relative to the book value estimated from financial statements. However, a common feature of all concentrated investment approaches is the focus on investing heavily in so-called "undervalued stocks," those whose share prices are significantly below their estimated corporate value. The aim is to achieve high absolute returns as share prices converge toward their estimated corporate value. When the goal of achieving high absolute returns is met, outperforming the benchmark becomes a secondary effect ^(Note 3).

The process of evaluating corporate value necessitates deep discussions with investee companies regarding their business environment and other factors, making engagement activities—the core of stewardship responsibility—indispensable. Precisely because the strategy is concentrated, it allows for time-intensive dialogue with investee companies and deep analysis of each one. As with EF, stewardship responsibility naturally becomes central to the investment strategy.

(3) Diversified Investment

In contrast to concentrated investing, so-called diversified investing—where one invests in a large number of stocks, say 100—makes it difficult to conduct deep analysis on all investee companies, as is done with concentrated investing. Diversified investors

(Note 2) While holdings may exceed 30 securities, some investment strategies concentrate over 90% of holdings in just 5 to 10 top positions, meaning the number of holdings alone is not the sole measure of concentration. Furthermore, a high "active share"—indicating deviation from the benchmark holdings—of 90% or more is also a characteristic of concentrated investing.

(Note 3) The target absolute return is 15-20% annually. Since the long-term average return of the stock market is less than 10%, achieving a high absolute return can outperform the benchmark over the long term.

often hold stocks with high weightings in their benchmarks for risk management purposes. This means investments aren't always based on deep analysis of every portfolio company, leading to varying levels of engagement intensity. Some holdings may target short-term catalysts, similar to the short-term investing mentioned earlier, creating little incentive for deep discussions about corporate value with those companies.

However, for Japanese asset managers, a reality exists where significant human resources are allocated to important flagship funds with large asset sizes, and top talent within the firm is assigned to them. For such funds, deeper analysis than that conducted for concentrated investment funds is sometimes possible. Encouraging these teams to function effectively may help fulfill the core stewardship responsibilities.

However, for diversified investments, only a minimal number of investee companies warrant the deep analysis required to fulfill stewardship responsibilities. Therefore, stewardship is unlikely to become the core of the investment strategy. If sufficient human resources can only be allocated for certain funds, the asset manager should explain that "activities vary in intensity depending on the investee company and do not uniformly involve deep dialogue."

4. In the Case of Passive Management

What about passive investment, Japan's largest equity investment strategy estimated to hold over 35% of outstanding shares, as shown in Figure 1? It is a fact that one reason the SC was established in Japan was to ensure that passive investors holding such significant stakes fulfill their stewardship responsibilities. Guideline 4-4 of Principle 4 also states: "Passive investors have limited options to sell shares of investee companies and therefore have a greater need to promote medium- to long-term corporate value enhancement. Institutional investors should therefore engage more proactively in dialogue and exercise voting rights from a medium- to long-term perspective when implementing passive investment strategies." This statement expresses that expectation. On the other hand, passive investment faces various challenges in fulfilling stewardship responsibilities, such as insufficient coverage of stewardship costs by management fees or the question of whether the necessary capabilities to conduct such activities exist in the first place. Therefore, it is essential to explore measures to enhance "efficiency" in fulfilling stewardship responsibilities.

(1) Challenges of Passive Management

The investment objective of passive management is to deliver returns matching a

specified benchmark. To achieve this objective, asset managers hold the benchmark's constituent stocks as closely as possible to the benchmark's weightings. While some hedge funds predict benchmark changes and aim to profit from them, passive managers rarely engage in similar behavior to achieve even slight outperformance. This is because investment guidelines—contractual agreements with clients—require that tracking error (the deviation from the benchmark's return) be kept below a specified threshold.

In active management, the investment objective is often to achieve excess returns relative to a benchmark, requiring detailed research on investment targets. Consequently, relatively high management fees are frequently charged to clients. In contrast, passive management aims to replicate the benchmark, so such research is not inherently required, resulting in significantly lower management fees. When managing enormous sums like GPIF, the passive investment ratio inevitably becomes high. Moreover, since achieving high absolute returns is also an investment goal, there is an incentive to pay additional management fees to engage in engagement activities, even for passive investments. However, for individual clients or relatively small asset owners, the incentive to pay such additional costs is less likely to materialize.

In other words, passive management lacks incentives to achieve returns above the benchmark, and it isn't easy to justify the cost of engagement activities sufficient to fulfill stewardship responsibilities. This is why efficiency becomes crucial.

(2) Efforts to Improve Efficiency

Passive management is already making an effort to improve efficiency. Since passive managers cannot sell their holdings in investee companies, proxy voting is significant in practice. This is because they have an annual opportunity to express approval or disapproval regarding matters such as director candidates proposed by investee companies or the fairness of tender offer (TOB) prices, which have recently increased. Given their often high ownership stakes, their approval or disapproval can sometimes hold the casting vote. Shareholder meetings for Japanese listed companies with March fiscal year-ends are concentrated in June. Scrutinizing all the meeting proposals for nearly 2,000 listed companies within such a short period is challenging.

Given this situation, significant efficiency improvements have been implemented in the voting process. It is now common practice to feed various data—such as meeting proposals, the firm's own voting criteria, integrated reports, securities reports, and earnings announcements—into AI (artificial intelligence). The AI then drafts proposals, which humans ultimately review. While complex proposals requiring value judgments on takeover bid prices are handled individually, the reality is that significant efficiency

gains have been achieved for the exercise of voting rights on the majority of proposals (Note 4).

(3) Challenges from the perspective of practicality in exercising voting rights

While efficiency gains in the voting process are advancing, some argue that practical challenges remain. Many asset managers establish “voting criteria,” explicitly outlining various quantitative and qualitative standards, and generally determine their stance on shareholder meeting proposals based on these criteria. Concerns have been raised that mechanically exercising voting rights based on these criteria may be problematic in practice.

For example, Principle 5 of the SC states: “Institutional investors should devise voting policies that contribute to the sustainable growth of investee companies, rather than relying solely on formalistic criteria.” Some interpret this as suggesting that mechanically exercising rights based on voting criteria is undesirable. However, establishing numerical benchmarks, such as ROE, to assess whether shareholder value is being eroded over the long term, and consistently opposing the appointment of directors who fail to meet these benchmarks, is precisely the kind of mechanical voting that is the essence of passive management focused on efficiency. From the client's perspective, clearly opposing directors who fail to meet targets is desirable as it enhances management discipline.

If the exercise criteria are established from the perspective of enhancing shareholder value, formal judgments should be regarded as being designed to contribute to sustainable growth. The SC's June 2025 revision also calls for the reaffirming of the intent of comply-or-explain. Therefore, exercising voting rights diligently in accordance with strict criteria should be explained as contributing to sustainable growth.

(4) The Approach to Exercising Shareholder Rights in Passive Investment

In contrast to active management, I would like to present an interesting case study regarding how passive management should exercise shareholder rights, including voting rights. One example is the tender offer (TOB) for Fujisoft that was finalized on February 19, 2025. Two investment funds, KKR and Bain Capital, announced takeover bids. Ultimately, KKR's higher bid succeeded. At an extraordinary shareholders' meeting held in May, the company's delisting was resolved. If an active manager held Fujisoft shares, it would be considered standard practice to make an investment

(Note 4) Even listed companies facing investors commonly feed various data into AI to generate anticipated Q&A for shareholder meetings. It is no exaggeration to say that engagement forums are taking on the appearance of AI versus AI.

decision by comprehensively evaluating the prices offered by the two investment funds and their post-acquisition growth stories, and then tendering shares to one of the takeover bids. Conversely, most passive funds reportedly chose not to tender to either offer, instead opting to sell their shares via a squeeze-out (a mandatory buyout of minority shareholders). This was deemed a rational choice to minimize tracking errors relative to the benchmark by holding shares until just before delisting. This approach followed a different objective than active management's goal of selling at a higher price to deliver greater returns to clients.

Another example concerns the investment judgment regarding the price of Aeon's tender offer for Tsuruha Holdings. Major shareholder investment funds raised doubts about whether Aeon's offered price was too low, leading to the tender offer's eventual approval at the May 2025 shareholders' meeting. If an active manager held shares in Tsuruha HD, and they judged Aeon's TOB price to be below their perceived fair value, they would likely oppose the bid, believing a higher TOB price was appropriate.

On the other hand, what investment decision would passive management make? Suppose the passive manager, like the active manager, judged the TOB price to be below fair value. Passive management would likely hold not only Tsuruha HD but also Aeon, and the holding ratio for Aeon, with its larger market capitalization, would probably be greater. If the TOB price is below fair value, it means Aeon can acquire the target company at a lower price than fair value, which is beneficial. Therefore, from a portfolio-wide perspective, supporting the TOB is the appropriate investment decision, as it increases Aeon's corporate value, which holds a greater weight in the portfolio.

Indeed, I understand several passive funds voted in favor of Aeon's TOB.

These two cases demonstrate that even if investors share the same assessment of the target company's management decisions, passive and active management approaches lead to different actual investment actions and voting behaviors. This case is also interesting when considering what shareholder responsibility entails. What does this mean?

The stock market serves various roles, including liquidity provision, price discovery, and efficient capital allocation. In these two cases, it is clear that passive management failed to fulfill the price discovery function. In the first case, it abandoned price discovery for both tender offer prices. In the second case, it prioritized the impact on the portfolio over the validity of the takeover bid price. While it is true that the price discovery function is expected more from active management and less from passive management, what then is the function that passive management, which holds a high proportion of holdings in the stock market, actually fulfills within the stock market?

As mentioned earlier, exercising voting rights according to strict criteria and leveraging numerical strength to enhance management discipline are core functions—that is, efficient investment actions. Furthermore, passive asset managers need to collaborate and seek improvements through stewardship activities regarding common challenges faced by investee companies. In this sense, collaborative engagement plays a significant role in passive investing.

5. The Importance of Collaborative Engagement

Collaborative engagement is defined in the SC as “engaging in dialogue in collaboration with other institutional investors.” Principle 4 of the SC states: “Institutional investors should strive to share understanding with investee companies and work to improve issues through constructive 'purposeful dialogue' with them.” Furthermore, Guideline 4-6 states: “When institutional investors engage in dialogue with investee companies, conducting such dialogue independently is one option, but collaborating with other institutional investors to engage in dialogue is also an important option. (Omitted)” This highlights the use of collaborative engagement.^(Note 5)

As explained, there is a significant difference in how stewardship responsibilities are fulfilled between active and passive management. Figure 2 on the next page compares the engagement activities of both approaches, clearly showing substantial differences.

Passive management requires holding most of the benchmark's constituent stocks continuously. Even if an investee company faces significant management challenges deemed difficult to resolve, selling is challenging. Furthermore, when lacking both the incentive and the cost allocation to address specific management issues at individual companies, a "broad and shallow" approach is appropriate; selecting engagement themes focused on everyday, lowest-common-denominator matters across the entire market. For passive management, it is crucial to contribute to long-term corporate value enhancement by demanding that investee companies achieve specific goals, such as raising the proportion of independent directors to over half, thereby elevating governance standards. Such engagement is more efficient when conducted jointly by multiple passive managers rather than individually by each firm, reducing the burden on both managers and investee companies. Considering the efficiency of engagement in

(Note:5) Incidentally, to align with promoting collaborative engagement, the scope of "joint holders" and "significant proposal activities" under the large shareholding reporting system (a simplified reporting system for institutional investors holding 5% or more) has been clarified, creating an environment more conducive to utilizing collaborative engagement. This amendment is also expected to play a role in deepening engagement activities.

passive management is key to sustaining these activities over the long term.

Fig. 2: Engagement Characteristic of Active/Passive Managers

	Active Investment	Passive Investment
Investment Policy	Research individual stocks and select investment targets based on the manager's judgment	Buy and hold the constituents of benchmark index
Number of Holdings	Approximately 10–100 stocks	The number of benchmark constituents
Investment Period	Flexible buying and selling based on stock price movements	Generally, no trading; ultra-long-term holding
Engagement Policy	To improve the performance of funds they manage	To improve benchmark returns
Engagement Purpose	To make buy/sell decisions	To encourage long-term corporate value growth in index constituents
Target Companies	Specific companies held by the fund	Broad coverage, focusing on stocks with high index weightings
Approach	Seeking improvements on specific issues to the company	Engaging key companies on market-wide issues while communicating messages to all companies
Characteristics of Dialogue Themes	Management issues specific to individual companies	Primarily market-wide themes
Response to Problematic Companies	Dialogue, voting, and divestment	Hold, engage, and vote
Countermeasures Against Free Riders	Generally unnecessary	Seek collaborative action (understanding and evaluation by asset owners is also important)

(Source) Yuki Kimura (Editor) "Practices and Prospects of Stewardship by Institutional Investors," Dobunkan Publishing, 2025

In Japan, the Collaborative Dialogue Forum for Institutional Investors (hereinafter referred to as the Collaborative Dialogue Forum) was established in October 2017 ^(Note 6). This general incorporated association was established to support collaborative, purposeful dialogue (collaborative engagement) between institutional investors and companies, aiming to contribute to appropriate stewardship activities by institutional investors. Currently, seven asset owners and asset management companies ^(Note 7) are members. The Forum operates the "Institutional Investor Collaborative Dialogue Program," a platform for multiple institutional investors to conduct collaborative dialogue (collaborative engagement) with companies. Activities include compiling and documenting shared views to send to investee companies and requesting meetings as

(Note 6) Incidentally, in 2017, the Life Insurance Association of Japan also established a "Stewardship Activities Working Group," which implements collaborative engagement similar to the Collaborative Dialogue Forum. Ten life insurance companies participate in this working group. For fiscal year 2024, collaborative engagement is being conducted on four themes: ① Enhancing shareholder returns, ② Integrated disclosure, ③ Strengthening climate change disclosure, and ④ Disclosure of measures for management mindful of capital costs and stock prices.

(Note 7) As of October 2024, seven companies are participating: the Corporate Pension Federation, Dai-ichi Life Insurance, Sumitomo Mitsui DS Asset Management, Sumitomo Mitsui Trust Asset Management, Mitsubishi UFJ Trust and Banking Corporation, Meiji Yasuda Asset Management, and Resona Asset Management.

necessary.

Of course, passive managers can also simultaneously pursue their own unique themes for engagement with investee companies to differentiate themselves from others. Passive managers are encouraged to utilize such collaborative engagement, clearly distinguishing between areas requiring differentiation and those requiring collaboration, to develop practical approaches.

6. How Asset Owners Fulfill Their Stewardship Responsibilities

The stewardship responsibilities asset owners should fulfill vary significantly depending on their scale. Unlike overseas asset owners, most Japanese asset owners do not invest directly; instead, they primarily outsource management to asset management firms and have minimal investment staff. Only a minimal number of asset owners, such as the GPIF, possess large asset bases and substantial investment staff. For these owners, activities emphasizing efficiency, similar to passive management, are essential. What constitutes practical activities for asset owners in this situation?

For asset owners delegating management to asset managers, the most crucial aspect of fulfilling stewardship responsibilities is selecting funds where stewardship is central to the investment strategy and entrusting capital to them. As shown in Figure 1, the assets under management (AUM) of investment strategies centered on stewardship responsibilities represent only a few percent of the Japanese equity market. Increasing the proportion of investment strategies that are highly practical from a stewardship perspective is crucial for enhancing corporate value over the medium to long term. As mentioned earlier, such investment strategies also carry a significant risk of deviating from the benchmark, making them difficult for asset owners to adopt. However, it is equally clear that as the scale of these investment strategies expands, it will enhance management discipline at investee companies, ultimately leading to increased corporate value over the long term.

Select funds where stewardship responsibility forms the core of the investment strategy, and ensure these funds deliver high returns to asset owners. By enabling this investment cycle to function, we can fulfill our responsibility to accumulate sufficient assets to meet promised payments to beneficiaries. Entrust funds to managers capable of fulfilling stewardship responsibilities, and enhance the importance of engagement activities that improve the corporate value of investee companies—this very cycle of funds should be the fundamental role that asset owners should play within the investment chain.

Entrusting funds to investment strategies where stewardship responsibility is key to high returns is the most direct path for asset owners to fulfill their duties. However, when such strategies are not adopted, fulfilling this role as efficiently as possible is the most rational decision. Driven by this awareness, the Corporate Pension Federation took the initiative to establish the Corporate Pension Stewardship Promotion Council (hereinafter referred to as the Promotion Council) in August 2024. This organization was established so that corporate pension funds could collaboratively monitor the stewardship activities of asset managers (collaborative monitoring). The Promotion Council's activities are explicitly stated to correspond to the "collaborative monitoring" initiative outlined in Supplementary Principle 5-1 of the Asset Owner Principles.

The SC requires asset owners to undertake the following activities: ① Encourage asset managers to engage in practical stewardship activities (Guideline 1-3); ② Clearly communicate the matters and principles required of asset managers regarding stewardship activities (Guideline 1-4); ③ Monitor asset managers' stewardship activities (Guideline 1-5); ④ Report annually to beneficiaries (Guideline 6-2). The Promotion Council was established because it was deemed inefficient for each corporate pension fund to conduct stewardship activities individually.

By supporting the stewardship activities that each corporate pension fund should implement, the Promotion Council can efficiently monitor asset managers' stewardship activities, consolidate information on these activities, and participate in joint briefings. For example, it can conduct: ① Regular surveys on everyday items (questionnaire-based surveys regarding asset managers' stewardship activities), ② Joint briefings and collaborative dialogues (holding briefings for each asset manager and conducting collaborative dialogues with them), and ③ Receiving summary reports (reports prepared by asset managers detailing their own activities and self-assessments). The Promotion Council's website states that joint monitoring of asset managers' stewardship activities by corporate pension funds enables substantive implementation.

7. Future Outlook

The establishment of the SC has raised awareness of stewardship responsibilities even in passive investment. Over the past decade, both asset managers and asset owners have engaged in trial and error regarding how to fulfill these responsibilities. However, there are questions about how much awareness existed of enhancing the effectiveness of investment activities from the perspectives of practicality and efficiency, as this paper points out. There is a risk that, overly focused on simply complying with the SC's wording, emphasis may have been placed on superficial

compliance.

For instance, some asset owners are said to take the SC wording at face value, indiscriminately demanding engagement from asset managers regardless of whether they employ active or passive investment styles. Without consensus between both parties on the appropriate engagement approach for each investment style and the cost-effectiveness of engagement, the effectiveness of such activities cannot be guaranteed.

As is evident from the EF's investment process, fulfilling stewardship responsibilities is not as straightforward as it sounds. Genuine engagement activities aimed at enhancing corporate value and investment returns are highly individualized, demanding detailed company analysis, significant effort, and advanced skill sets. In other words, achieving the necessary impact to fulfill stewardship responsibilities inherently requires sacrificing efficiency.

Conversely, passive investing with high ownership ratios significantly improves listed companies' governance levels. By prioritizing efficiency and setting strict voting standards, passive investors exercise voting rights to enhance management discipline. With capital flowing into EF and long-term concentrated investment funds built upon this passive foundation, the management challenges of their portfolio companies can be addressed. From the perspective of practicality and efficiency, passive investing and concentrated active investing focused on enhancing corporate value should work hand in hand. This approach, where both work together to increase the corporate value of portfolio companies, represents a desirable and realistically achievable model.

While asset owners should primarily allocate capital to active management that enhances corporate value, when investing in passive management, it is crucial to efficiently fulfill their role by leveraging collaborative monitoring mechanisms led by asset owners.

Fulfilling stewardship responsibilities is a means to an end; the ultimate goal is to enhance the value of investee companies and, consequently, expand investment returns. Achieving this goal is not easy. However, the most direct path to ultimately fulfilling the objectives SC aims for may be for active and passive managers to operate with practicality and efficiency in mind, aligned with their respective investment objectives. At the same time, asset owners clearly recognize the differing purposes of both approaches, and appropriately set investment guidelines to support the fulfillment of these objectives.

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