

Responsible Investment Framework

4 Sustainable Investment

The policy and systems framework that functions as the foundation for Daiwa AM's activities



ESG Investment Policy

Through its asset management business, Daiwa AM aims to make a positive contribution toward Beneficiaries' asset formation over the medium to long term. To achieve this goal, besides the appropriate selection of investment assets (i.e., stocks and bonds), enhancing the medium- to long-term corporate value and sustainability of the issuer companies and organizations (hereinafter "investee companies") is also extremely important, while maintaining the sustainability of society as a whole is also a prerequisite.

To enhance the medium- to long-term corporate value and sustainability of investee companies, it is vital to build

a good relationship with the environment (E) and society (S) based on appropriate governance (G). We believe that this can also contribute toward the realization of a highly sustainable society.

In playing a role as a link in the investment chain alongside Beneficiaries and investee companies, Daiwa AM is implementing measures that embody a focus on the key aspects of ESG. We have adopted the same ESG investment approach across the full range of the active investment, passive investment, and investment outsourcing that constitute our investment management strategies/products.

- 1 Through our asset management business, we aim to provide investment opportunities to companies that are actively working on ESG and SDG issues and to contribute to the realization of a highly sustainable society.
- 2 We will consider companies' ESG initiatives as factors that contribute to both medium- to long-term growth potential and risk reduction and will incorporate them in our investment decisions.
- 3 Through constructive dialogs, we call for companies to actively engage in ESG initiatives, and share ESG issues to help them improve their medium- to long-term value and sustainability.



In addition, based on the strategy outlined above, Daiwa AM has positioned the following items as its ESG Materiality (key issues), and is striving to accurately monitor the status of investee companies and industry as a whole, and to share its awareness of these issues.

For Daiwa AM's material ESG issues, see p. 16

ESG Integration

Since the Principles for Responsible Investment (PRI) were introduced in 2006, ESG has been a vital part of asset management. The companies that Daiwa AM invests in are also having to deal with climate change, human rights issues in the supply chain, etc., and have been brought to recognize the need to enhance their own sustainability. At the same time, it should not be forgotten that addressing these issues will also lead to the generation of new technologies and new business opportunities.

Daiwa AM views investee companies' initiatives to address ESG issues as leading to increased growth potential over the medium to long term, and as helping to

reduce risk, and we refer extensively to these initiatives when making investment decisions. By combining qualitative evaluation based on materiality-focused engagement with investee companies and other enterprises with quantitative evaluation undertaken by quantitative analysts, we are able to implement corporate valuation that integrates financial and non-financial information.

We also calculate our own unique ESG scores based on our Materiality, and use these scores when selecting stocks for inclusion in our portfolio and when implementing portfolio risk assessment.

Integration of ESG information, etc. into the investment process

The process that Daiwa AM uses for integrating non-financial information, including ESG information, into the asset management process, is as follows. The priority order for each process varies depending on the asset class and on the investment strategy.

First, starting from the various asset classes that are the target of investment, we decide on the investment universe through screening based on our general policy and the investment guidelines outlined in our individual strategies.

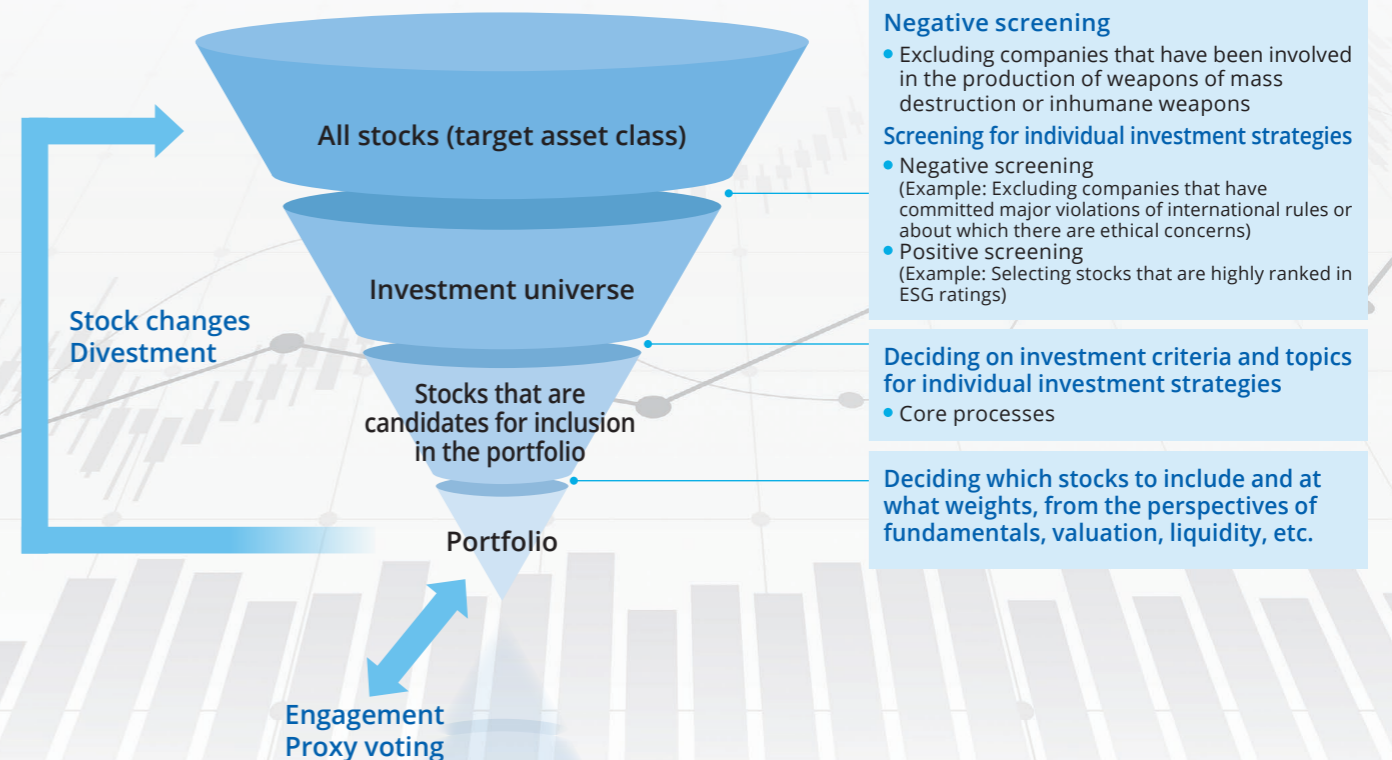
Based on the above, we then perform the selection of investment criteria and topics for each investment strategy, and decide on which stocks to include as candidates for inclusion in our portfolio. This is the core process that defines the purpose and characteristics of the investment strategy; in the case of ESG funds, ESG is included as a key

element in the process.

Finally, we take into account fundamentals such as performance, valuation (in terms of whether a stock is undervalued or overvalued), liquidity, etc., when building our portfolio when deciding which stocks to include and at what weights.

After the portfolio has been built up, we continue to revise it on a regular basis, and we take every opportunity to undertake engagement with investee companies. In engagement, we encourage companies to aim for further improvement from both a financial and non-financial perspective. In the case of equities, proxy voting provides an important way for us to express our views; for all shareholders meeting proposals, we implement proxy voting in accordance with Daiwa AM's Proxy Voting Policy.

Investment strategy implementation process



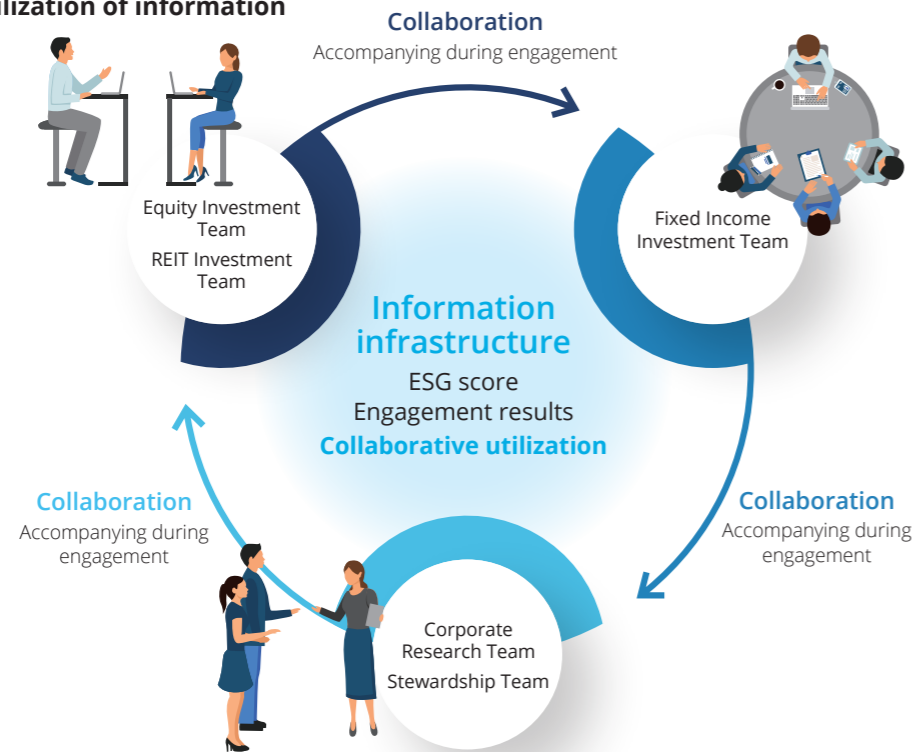
Research and analysis system for non-financial information, and information infrastructure

Daiwa AM has adopted a centralized research system, so that information from the Corporate Research Team and Stewardship Team can be used not only by the equity and REITs management teams but also by the bond management team. For both financial and non-financial information, investee company data collection and analysis, records of contact and engagement with investee companies and related

progress reports, etc. are collated by Daiwa AM's in-house information infrastructure using a system that enables all personnel involved with asset management to utilize them.

Daiwa AM has also put in place a system whereby all related parties, regardless of asset class, can participate in engagement with investee companies, and conduct engagement from their own particular perspective.

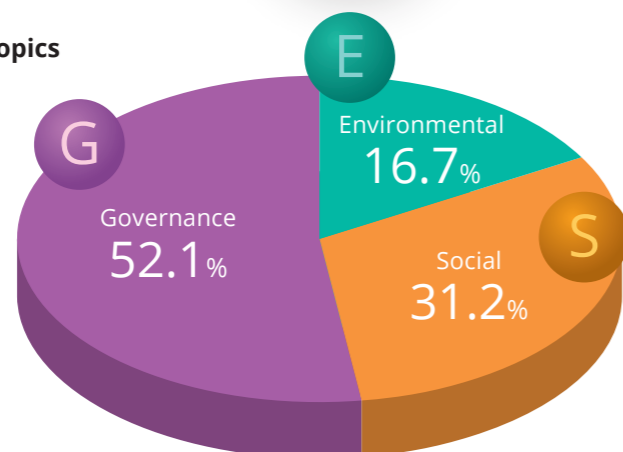
Collaborative utilization of information



ESG engagement

ESG-related engagement—Topics

- Composition of the board of directors **14.3%**
- Directors' remuneration **6.1%**
- Risk management **7.0%**
- Cross-shareholdings **9.8%**
- Long-term vision **14.9%**



- Climate change **14.1%**
- Natural capital **2.7%**
- A healthy, safe society **1.7%**
- Supply chain **3.6%**
- Diversity **7.5%**
- Human capital **18.4%**

Period covered: July 2024–June 2025

The share of engagement topics accounted for by the Environment (E) and Social (S) categories both fell over this period, from 18.1% to 16.7% in the case of E, and from 35.1% to 31.2% in the case of S, while the share accounted for by Governance (G) rose from 46.9% to 52.1%. This was because, although the number of instances of engagement in the E and S categories rose year-on-year, the number of instances of engagement in the G category rose more rapidly (by around 50% year-on-year). A major contributing factor to the rise in the number of instances of engagement in the G category was an increase in the share of engagement topics relating to cross-shareholdings (up from 8.7% to 9.8%) and to long-term vision (up from 13.1% to 14.9%), the background to which likely was the increasingly strict proxy voting policies adopted by Daiwa AM and by other asset management companies.

Within the E category, although the share of engagement topics relating to natural capital remained low as a percentage of all topics, in terms of the number of instances of engagement it increased by over 200% year-on-year, and we are paying close attention to this trend.

Equity ESG Integration (corporate value assessment and ESG data)

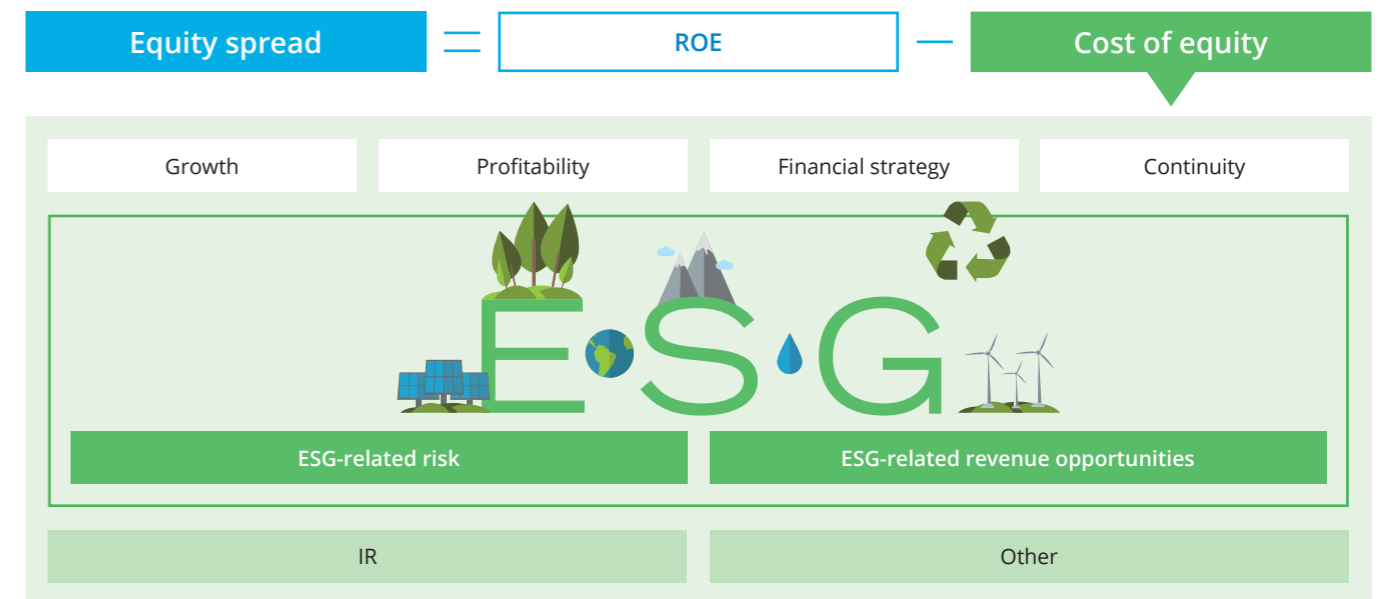
What interests equity investors most in terms of the minimum return they can expect to obtain from investee companies is equity cost. It is possible to measure the extent to which the value generated by a company can exceed this anticipated return.

We conduct corporate valuation by integrating qualitative evaluation based on investee companies' approach to ESG, as ascertained through dialog with them, and the status of their related initiatives, into our unique long-term corporate value model.

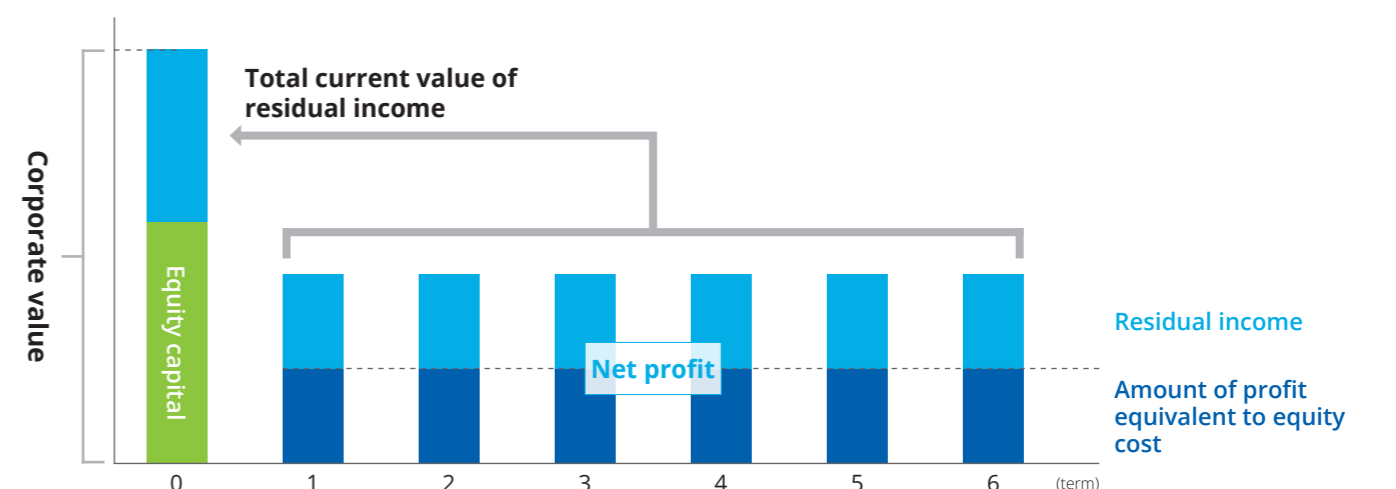
More specifically, our corporate research analysts adjust equity cost to reflect both financial data and non-financial data (including ESG data), and then use the equity spread (calculated by deducting equity cost from the return on equity) to calculate corporate value (see figure below). For example, if a company has outstanding corporate

governance, this means lower risks for investors, which in turn will lead to lower equity cost and thus higher corporate valuation. A further point is that, by breaking ESG evaluation down into risks and opportunities and reflecting the opportunities in anticipated long-term growth rates, we have a framework that enables us to determine, in detail, what impact a company's initiatives for ESG issues are having on its corporate value.

The residual income model (RIM) is utilized when using equity spread to determine corporate value. By using RIM, anticipated future net profit can be broken down into the amount of profit equivalent to equity cost and residual income (calculated as the equity spread x shareholders' equity). Discounting residual profit for each period by present value and then adding it to current shareholders' equity makes it possible to determine corporate value.



Residual Income Model (RIM)



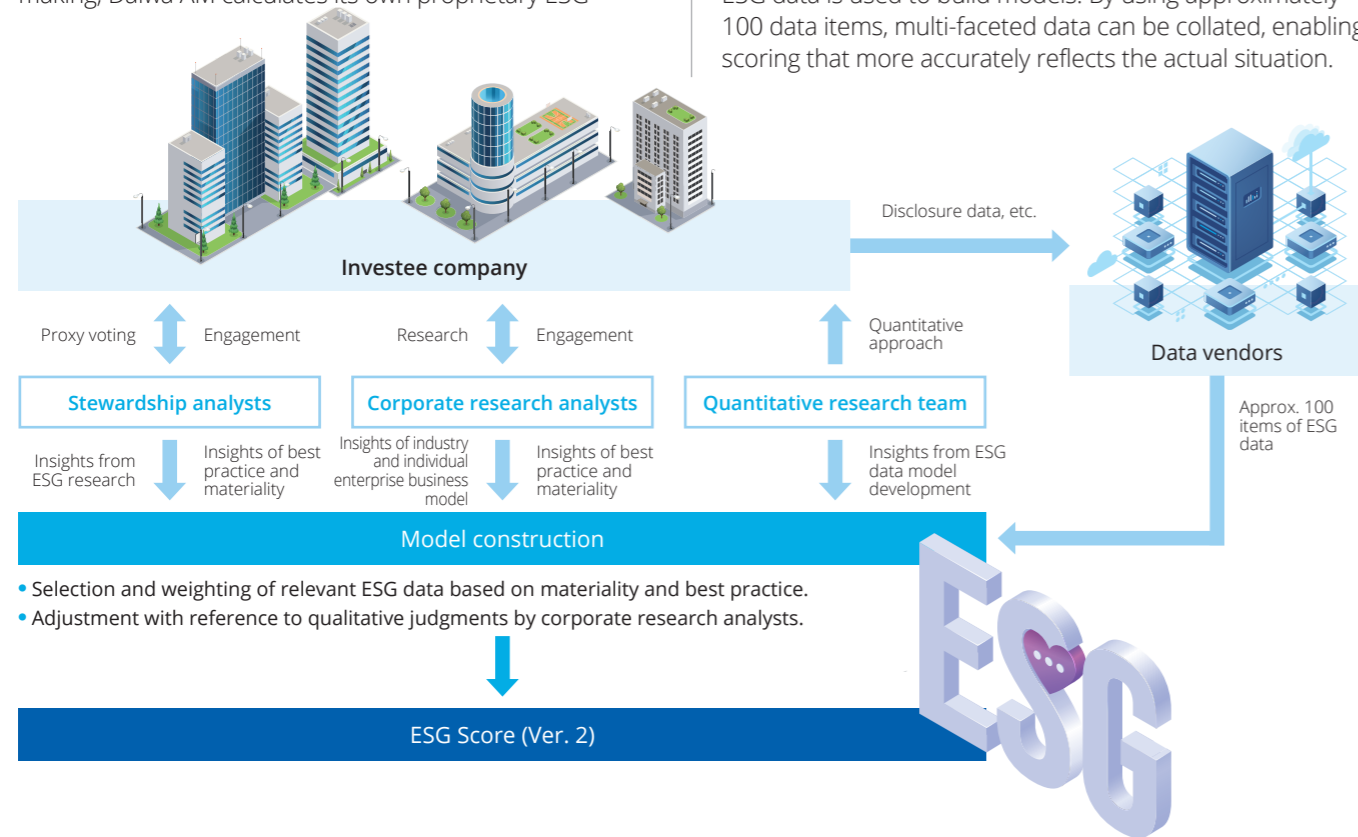
In-house ESG Score

What is our in-house ESG score?

With the aim of identifying companies' ESG-related risks and opportunities from multiple perspectives and then using this information effectively in investment decision-making, Daiwa AM calculates its own proprietary ESG

scores. In the spring of 2023, the existing ESG score system was revised, and Version 2 was introduced.

With this ESG score system, quantitative evaluation of ESG data is used to build models. By using approximately 100 data items, multi-faceted data can be collated, enabling scoring that more accurately reflects the actual situation.



The data that ESG scores are compiled from

To build ESG scores, Daiwa AM collects data on sustainability related risks and opportunities from companies. The data collected (mainly via data vendors) includes data disclosed by individual companies themselves, data disclosed by organizations to which the companies belong, and third-party data from

independent research and estimates, etc.

The collected data then undergoes a process of selection based on Daiwa AM's core materiality and best practice, and is divided into the E, S, and G categories, and into more detailed topics and sub-topics.

Data on companies' ESG-related measures, risks, and opportunities			
	Filter		
	Our core materiality and best practice		
Category	Environment (E)	Social (S)	Governance (G)
Topics	<ul style="list-style-type: none"> Climate change Natural capital 	<ul style="list-style-type: none"> Social responsibility Human capital 	<ul style="list-style-type: none"> Governance system Risk management Capital efficiency improvement Communication
Sub-topics	<ul style="list-style-type: none"> Greenhouse gas emissions Response to climate change risk Energy shift Environmental pollution Safeguarding resources, etc. 	<ul style="list-style-type: none"> Contributing toward the building of a society in which people enjoy health and peace of mind Supply chain management Enhancing the value of human capital, etc. 	<ul style="list-style-type: none"> Appropriate decision-making and oversight Risk management system Compliance Balance sheet management to realize capital efficiency improvement Constructive dialog and appropriate communication with stakeholders, etc.

Note: Sub-topics consist of approximately 100 detailed data items.

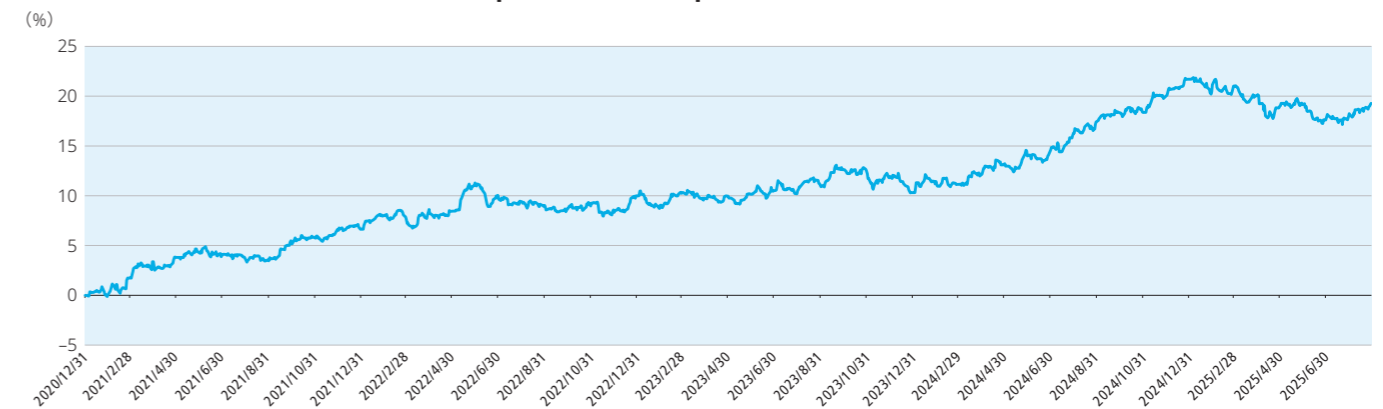
ESG score and performance

Using the ESG scores compiled by Daiwa AM, the universe of stocks was divided into five quintiles and then the performance disparity between the first quintile (highest scores) and fifth quintile (lowest scores) of stocks was analyzed. It was found that, over the period measured, the stocks in the first quintile steadily outperformed the

stocks in the fifth quintile, showing that, on average, the higher a company's ESG score, the better its performance.

Although performance deteriorated from the beginning of 2025 through to around July, at the time of compilation of this report it was improving again.

ESG score—cumulative returns (first quintile to fifth quintile)



Note: The stock universe comprised the stocks included in Japan's TOPIX 1000 index. When monthly rebalancing is executed, neutralization is implemented using Daiwa AM's proprietary industry classification.

ESG score analysis

We examined ESG score performance since 2023, for the ESG score referred to above, for each of E, S, and G.

Environment (E) performance showed steady improvement, a trend which was similar to overall ESG score performance.

With regard to Social (S), there was little change up until around the summer of 2024, after which performance improved.

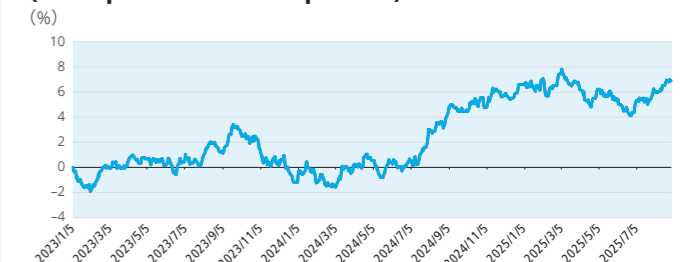
Governance (G) performance was negative until around May or June each year, after which it moved into positive territory. We believe this may have been due to the increase in the number of companies receiving shareholder proposals from activist investors, and to the fact that this component of the ESG score seeks to identify companies that have relatively low governance scores due to, for example, holding large amounts of cash during the period coming up to the annual shareholders meeting. It can be assumed that following the meeting, a reversal of this trend is observed. Also, we believe that the G performance also contributed to the significant decline in the overall ESG score during the period from the beginning of 2025 onward.

With the current model, the individual components that make up the ESG score are each given an equal weight. However, if one looks at the trends in the TOPIX 1000 stock universe over this period, it is apparent that the E score had the biggest impact on the overall ESG score. Going forward, we will continue to undertake research aimed at ensuring that our ESG score makes a positive contribution to asset management from the perspective of risks and opportunities in each sector.

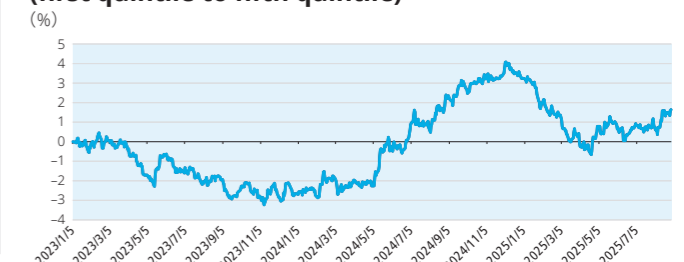
Environment (E) score—Cumulative returns (first quintile to fifth quintile)



Social (S) score—Cumulative returns (first quintile to fifth quintile)



Governance (G) score—Cumulative returns (first quintile to fifth quintile)



Collaboration with the Drucker Institute

Business alliance with the Drucker Institute

In 2022, Daiwa AM signed a comprehensive business alliance agreement with the Drucker Institute in California. The Drucker Institute is a research institute at Claremont Graduate University; the content of the agreement included granting to Daiwa AM the exclusive right to use the Drucker Institute Score (developed by the Drucker Institute to evaluate the corporate effectiveness of U.S. companies) in Japan, and also a project to collaborate on development of a Japanese equivalent of the Drucker Institute Score to evaluate the effectiveness of Japanese companies.

The Drucker Institute Score quantifies five principles advocated by American management theorist Peter Drucker: customer satisfaction, employee engagement

and development, innovation, social responsibility, and financial strength.

Results achieved through the alliance so far include: the establishment of a Daiwa AM US equities active fund that makes use of the Drucker Institute Score, gaining expertise in the scoring methodology by assigning Daiwa AM personnel to undertake research at the Drucker Institute in the U.S., the joint development of a Japanese equivalent of the Drucker Institute Score, and the establishment of a Japanese equities active fund using this new score.

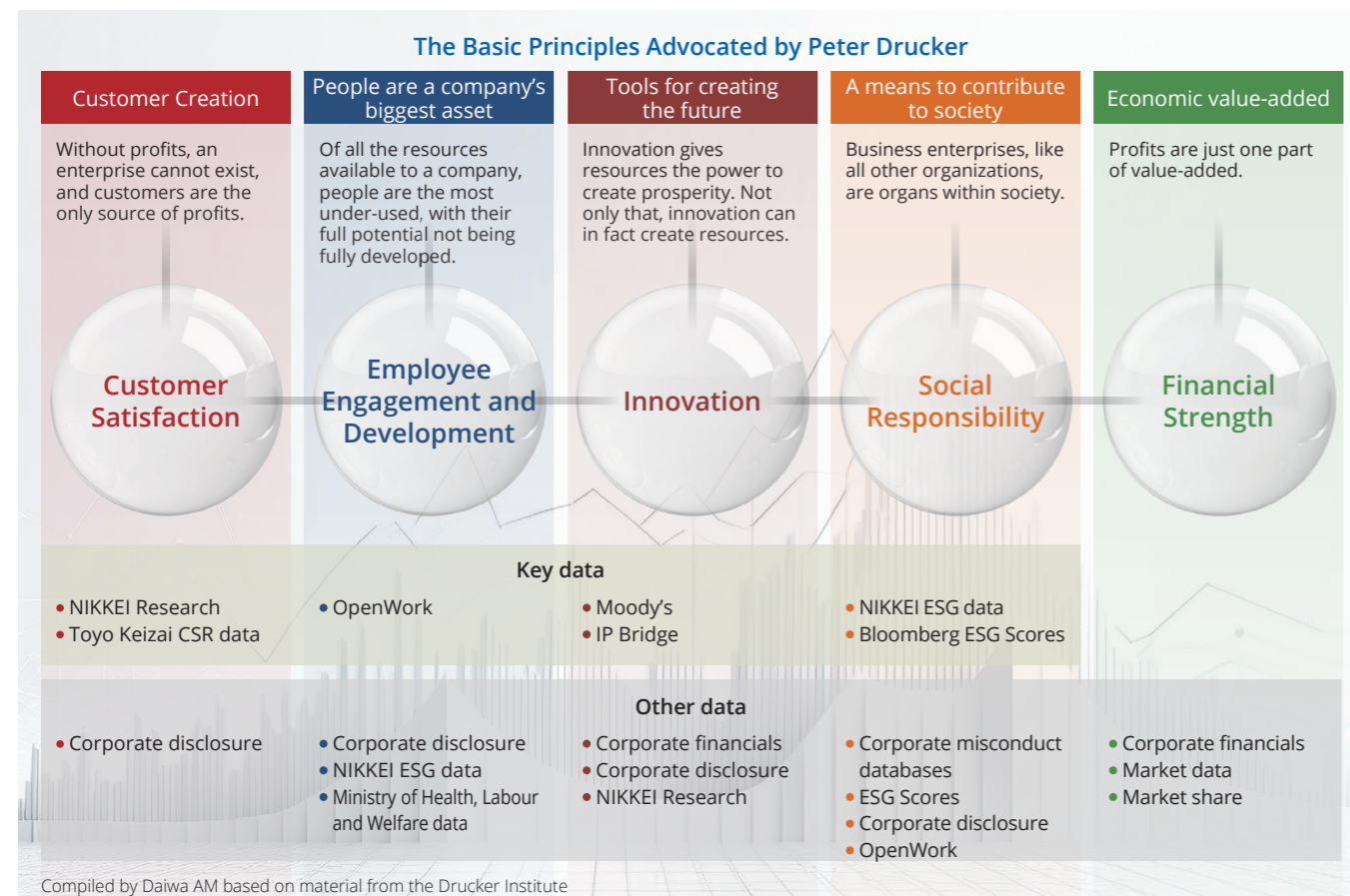
Going forward, we will be further strengthening this partnership with the Drucker Institute, and striving to generate as many tangible and intangible benefits as possible from this relationship.

Drucker Institute Score

Building on the data structure and methodology of the U.S. Drucker Institute Score and considering data availability in Japan, Daiwa AM has developed a Japanese equivalent of the Drucker Institute Score. By dividing Drucker's basic principles into five domains and visualizing them, it makes it possible to measure corporate value from the perspectives of diverse stakeholders in a way

that is difficult to do with conventional assessment. Elements such as human capital that generates profits and value, patents that can earn licensing fees, and the customer base that derives from high customer satisfaction and brand power, all contribute to high competitiveness and stable earning ability, and are thus vital for corporate growth.

Drucker Institute Score



Comments from the Fund Manager of the Drucker Institute Japan Equity Fund

Focusing on intangible assets that constitute "Mienai Chikara™"



Kazuhito Terashima
Senior Fund Manager
Beta Management & Investment Solution Department

The Drucker Institute Japan Equity Fund is an innovative active fund that selects Japanese stocks to invest in based on assessment of their fundamental growth potential, focusing on intangible assets that cannot be evaluated using conventional financial data alone. The most important feature of the Fund is that it uses the Japanese equivalent of the Drucker Institute Score which was developed using knowhow obtained through the business alliance between Daiwa AM and the Drucker Institute. In conventional active funds, normal practice is to have financial data play the central role when estimating corporate value. However, as has been seen with the dramatic growth of leading U.S. platform companies such as Microsoft, Amazon, and Apple, the transformation of the industrial structure is being accompanied by major changes in the perspectives needed when evaluating companies. There is a clear trend toward evaluating not only the revenue and assets recorded

in a company's financial statements, but also intangible assets such as the skills that the company possesses, its customer base, and the strength of its brand. The Drucker Institute Score visualizes "Mienai Chikara™ (Invisible Value Drivers)" that is the source of a company's competitiveness and growth, despite not being visible in its financial statements, and makes it possible to undertake corporate analysis that marks a new beginning when compared to conventional valuation methods and analysis that focuses on short-term performance. Of course, financial analysis is still an important element of corporate evaluation. The Drucker Institute Japan Equity Fund coordinates its operations with Daiwa AM's active, passive, and quant fund managers and corporate research analysts, sharing insights across departments; the Fund represents the adoption of an innovative financial model that emphasizes affinity with the Drucker Institute Score.

Given the issues affecting Japan's financial markets, such as the fact that a substantial percentage of the companies listed on the Tokyo Stock Exchange are trading at a price-to-book ratio (PBR) of less than 1.0, and given the reforms that the TSE is implementing, intangible assets and non-financial data are becoming steadily more important. The Drucker Institute Japan Equity Fund is a new active fund that makes it possible to identify companies with real growth potential as we enter a new era for Japan's financial markets. We believe that, by utilizing diverse perspectives different from those of conventional funds, as well as an innovative scoring system based on Drucker's management philosophy, we can realize investment in Japanese companies that are aiming for sustainable growth and enhance return on investment, thereby contributing toward medium- to long-term capital formation of our beneficiaries.

Initiatives at the Drucker Institute

For the past ten years, the Drucker Institute has published an annual ranking of America's Best Managed Companies based on the Drucker Institute Score. The ranking uses a comprehensive assessment framework formulated in accordance with the management thinking of Peter Drucker, analyzing organizational performance in terms of five areas: customer satisfaction, employee engagement and development, innovation, social responsibility, and financial strength.

In June 2025, the Drucker Institute announced the establishment of a new Data Innovation Team, which will build on the cutting-edge research that the Institute has achieved to date. The Team's members include faculty members from Claremont Graduate University, data scientists, business practitioners, and doctoral students (working as research associates and assistants). By adopting an assessment process that adds advanced AI and machine learning technology to existing knowhow and research methods, the Team aims to evaluate intangible assets with high precision. More specifically, its efforts can be expected to involve data collection that uses data scraping technology (applied to social media, etc.) to provide new indicators for evaluating companies.

Dr. Michelle Bligh, President of Claremont Graduate University, commented that "This is about pushing the

boundaries of how we measure and define corporate success. With this new team, we're combining the timeless wisdom of Peter Drucker with the power of modern data analytics." Attention is increasingly focused on how the Drucker Institute will leverage these new initiatives to become a leader in corporate evaluation, generating more diverse, effective indicators and methods. By integrating the power of AI and data science with Peter Drucker's thinking, the Institute will be taking the measurement of organizations' fundamental value to a new level.



Michael Kelly
Executive Director
Drucker Institute

Shuhei Arai
Research Fellow, Drucker Institute
(on assignment from Daiwa AM)

Initiatives Relating to Individual Asset Products

Equities (Active)

Contributing Toward the Enhancement of Investee Companies' Corporate Value Through Multi-Faceted Analysis

Important features of Daiwa AM's engagement activities include encouraging investee companies to implement measures oriented toward realizing sustainable growth and enhancing corporate value, and encouraging them to actualize those parts of corporate value that are currently undervalued. By undertaking multi-faceted surveys of the issues facing companies, undertaking engagement with appropriate content and methods, and encouraging companies, from an equal footing, to undertake the transformations needed to address the issues, we are working to bring about higher returns. Our fund managers, corporate research analysts, and stewardship analysts are working together to support enhancement of the corporate value of large numbers of investee companies, thereby also contributing toward sustainable growth for society as a whole.

On unique innovation by Daiwa AM is "Lingagement™," which combines linkage with engagement. "Lingagement™" involves: (1) The holding of information exchange meetings; (2) Introducing companies that have implemented best practice; (3) Providing opportunities to establish relationships with experts in related fields, etc. Regarding the holding of information exchange meetings, a fifth meeting was held in November 2025, with the theme of

"Aiming to Realize High ROE: Expanding Intellectual Property and Innovation, and Ensuring that this is Reflected in Corporate Value." The meeting brought together representatives of many investee companies, along with experts in related fields, for discussions about intellectual property and innovation. (see p. 42)

Our team also engages in dialog with government authorities, sharing ideas, from the perspective of institutional investors and minority shareholders, about the issues affecting efforts to enhance corporate value and the actual situation in this regard, and about the effectiveness of government regulations, etc. Particularly given the recent trend toward not having parent companies and their subsidiaries both listed on the stock market and toward taking companies private, we have vigorously made the case for strengthening measures to protect minority shareholders. Looking ahead, Daiwa AM will be proactively contributing toward the building of an environment that is conducive toward enhancing corporate value and safeguarding the rights of minority shareholders.



Equities (Passive)

Promoting ESG Investment Through Index Funds

The last few years have seen an ongoing global transition toward a decarbonized, sustainable society, particularly in Europe, and ESG-aware investment has become increasingly important. There has been regional variation in this respect. In some regions, such as Europe, ESG-related assets under management, including index funds, have increased substantially, and the pace of implementation of ESG measures by both companies and investors has accelerated. In the U.S., by contrast, with an adverse political climate, there has been growing criticism of ESG, and many companies now prefer to use the terms "sustainability" or "corporate value enhancement," framing it in a way

that is more obviously directly linked to business value. With the spread of this trend, it can be anticipated that sustainability-focused initiatives will be able to put down stronger roots, both in the U.S. and in the rest of the world, leading to enhanced long-term performance for companies.

Our team provides funds linked to indexes which incorporate ESG assessment; we aim to give investors the opportunity to undertake ESG investment which is low-cost and easy to get started with. The advantage of ESG investment using index funds is that it can be expected to provide an improvement in terms of both risk and returns over the long term, through low-cost investment management

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based on clear, transparent rules. While there is still room for further verification regarding the performance of ESG indexes, some research results indicate that, over the long term, the trend will be for ESG indexes to outperform their parent indexes.

Daiwa AM currently provides five ESG index funds (including low-cost

publicly offered investment trusts, and ETFs). We are also proceeding with projects to provide institutional investors, both in Japan and overseas, with ESG-related funds that meet their needs.

As regards engagement, Daiwa AM's Engagement Policy and related information are disclosed on our

website; we also inform investee companies about our stewardship activities. With regard to ESG data, such as ESG rankings and carbon emissions, for the component stocks of ESG indexes, we are aiming to realize more easy-to-understand disclosure, through efforts that include liaison with index providers.



Outsourcing

Implementation of ESG-related Monitoring with Respect to Outsourced Fund Managers

When performing due diligence with respect to outsourced fund managers, we verify the outsourced fund manager's ESG-related internal systems and policies, and their involvement in various initiatives. Particularly in the case of ESG investment, we focus on verifying whether concrete disclosure of ESG-related information is possible.

After a fund has been launched, we continue to implement regular review and hold meetings with the outsourced fund manager, and we exchange views with them regarding ESG issues relating to fund management. We implement proactive monitoring, periodically updating the due diligence questions used with reference to global standards such as PRI. In addition, we verify the implementation status of engagement undertaken by the outsourced fund manager.

In this fiscal year, we have been working to strengthen communication with outsourced fund managers regarding human rights issues. Daiwa AM has formulated a Human Rights Policy and implements initiatives to foster respect for human rights; building on this foundation, we believe that it is vital to embody respect for human rights not only in our own business activities, but throughout our network of outsourced fund managers.

We recognize that human rights initiatives are currently still in the early

stages of implementation. As a first step, we are striving to verify the current implementation status at outsourced fund managers.

For example, we have added questions about human rights to the due diligence process that is implemented, in principle, on an annual basis. We confirm the current status of implementation of measures to address human rights issues relating to fund operation, for example by verifying whether the outsourced fund manager has incorporated human rights risk appraisal into its operational processes. We also check what kind of human rights initiatives the outsourced fund manager is implementing in their own company.

As regards efforts to strengthen monitoring, we have been exchanging views with external experts regarding business and human rights issues, and implementing preparations for measures to further strengthen communication in this area.

Looking ahead, we will continue to examine the implementation status of individual companies in line with the responses that we receive from outsourced fund managers, and will be taking steps to address problems in advance, for example by determining which outsourced fund managers are lagging behind their peers in terms of implementation.

ESG Integration in Fixed Income Investment (credit risk assessment and ESG data)

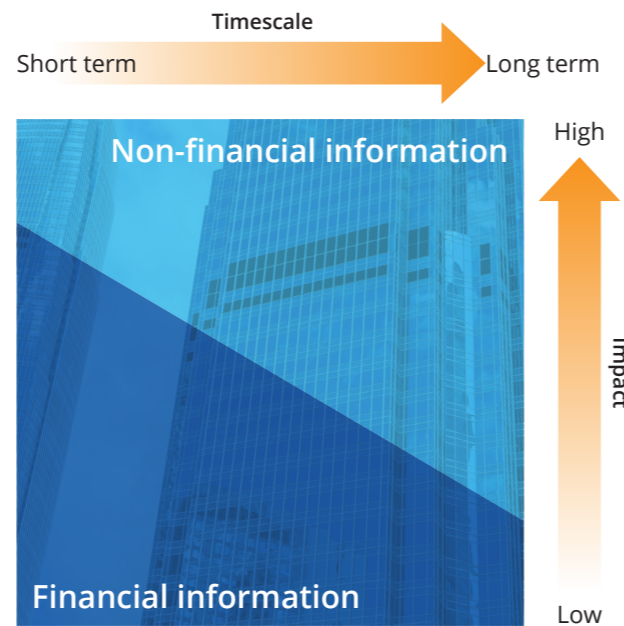
The impact of ESG factors on credit risk

We recognize that non-financial information is the foundation that underpins the financial information of the future. This is because the way in which companies address ESG issues, which are the key element in non-financial information, and how successful they are in addressing them, affects the future financial performance of that company.

In the case of fixed income investment, based on the perspective that the sustainability of a bond issuer will affect its ability to generate stable cash flow in the future, we implement assessment that takes into account the environment (E), social (S), and governance (G) elements of ESG in light of the manifested timescale.

Those bond issuers that take a proactive approach to ESG issues have lower governance-related risk, in relation to misconduct, lawsuits, compliance issues, etc., and can be expected to display stable long-term performance and reduced credit risk in the future.

We also focus on human capital management, from the perspective of verifying whether bond issuers have put in place a robust organizational structure able to maintain competitiveness during an era of dramatic change.



The ESG integration process in relation to fixed income investment

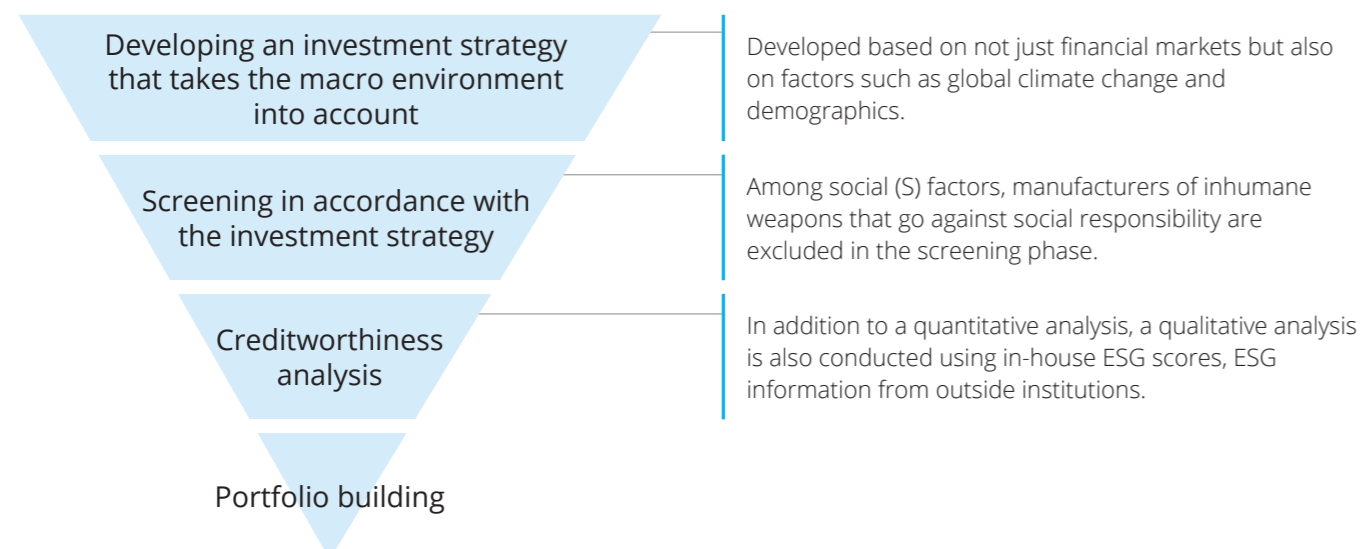
In Daiwa AM's ESG integration process, having constructed an investment strategy that takes the macroeconomic environment into account, and after performing negative screening to exclude companies that manufacture inhumane weapons, etc., we have our team of credit analysts perform creditworthiness analysis.

When implementing creditworthiness analysis, besides financial analysis focused on repayment ability, we also undertake both quantitative and qualitative assessment of non-financial information, including ESG.

A key feature of fixed income investment is that because the investment is for a fixed period, provided

that the bond issuer does not default during that time period, the return that one can expect to make at the time of making the investment is fixed.

The longer the investment period, the greater the impact that non-financial information can have on the perceived creditworthiness of the bond issuer. By including not only financial analysis of the bond issuer but also evaluation of non-financial information in the credit risk analysis process, we aim to implement appropriate credit risk analysis, control downside risk, and strengthen investment performance.



The non-financial information that we focus on, and our credit analysis perspective

Daiwa AM identifies the non-financial information that the industry, and bond issuers, should be focusing on, and strives to control downside risk by analyzing and evaluating the degree of impact that this non-financial information could have.

For example, as a case study of credit analysis in relation to the Environment (E), in the blast furnace segment of the steel industry, decarbonization is an important issue. Very large amounts of carbon dioxide are emitted during the process of using carbon to remove oxygen from iron ore, so in order to make the industry carbon neutral, there is a need to comprehensively replace existing technology with new, low-carbon technology. It is estimated that, for the Japanese steel industry to achieve carbon neutrality, individual steelmakers will need to spend several trillion yen on R&D and new equipment.

Given this business environment, in order to be able to compete effectively against leading foreign steelmakers, besides individual companies' technology development efforts, there is also need for multi-faceted, comprehensive strategies that include seeking funding support from countries that might not have been considered in the past, and undertaking a comprehensive overhaul of the global supply chain. Viewed from a medium- and long-term perspective, delays in technology development and rising manufacturing costs represent financial risk factors; this is why we are focusing on the implementation status of

measures to become carbon neutral.

In the chemical industry, an important indicator for credit evaluation in relation to the Social (S) aspect is supply chain management, including the issues of safety and quality. Demand for chemical products is very wide-ranging; chemicals play a vital role in the manufacturing of a diverse range of products, including cars, electromechanical machinery, consumer goods, etc., so there is a need to put in place systems that ensure a stable supply of products that meet customers' quality requirements. For the chemical industry as with the steel industry, the investment burden relating to complying with regulatory requirements aimed at the realization of carbon neutrality is important as a long-term risk factor.

With regard to the evaluation of governance (G), unlike the situation with E and S, timescale assessment is generally challenging. This is because the actualization of G-related risks may take a long time, or it may take the form of a sudden, dramatic change. Having said that, Daiwa AM implements measures to determine, as early as possible, the emergence of G risks, for example by developing an understanding of corporate culture and ethos through interviews with bond issuers, by evaluating bond issuers' stance when engaging in dialog with investors, and by examining the appropriacy of the capital allocation envisaged by a company's long-term vision as expressed in its medium-term business plan, etc.

Assessment of non-financial information is the key to reducing downside risk



Norio Endo
Senior Credit Analyst and Sustainability Leader
Fixed Income Investment Department

What makes fixed income investment different from equity investment is that because the upside returns are limited, the key to enhancing investment performance is controlling downside risk. From this perspective, the most important aspects of fixed income investment is the effective utilization of non-financial information, including ESG, in investment decisions with regard to bond issuers.

We view the initiatives that individual companies are implementing now in relation to ESG issues as affecting their financial performance in the future; we recognize that non-financial information is the foundation for future financial information.

When performing analysis of creditworthiness, if the investment timescale is short, then recent financial information is important, whereas the longer the investment timescale, the more important non-financial information is.

Given this background, by incorporating the evaluation of non-financial information into the credit risk analysis process alongside analysis of the bond issuer's financial information, we are aiming to control downside risk, improve the balance of risk and return, and, ultimately, improve investment performance.

More specifically, after verifying and analyzing the current response of each bond issuer to ESG issues, and then assessing the impact that this can be expected to have on future results and performance, we go on to forecast the impact on bond ratings and bond prices, and undertake investment decision-making from a perspective that seeks to ensure that the risk is commensurate with the return.

ESG Funds

ESG fund definitions and ESG funds

Daiwa AM has clarified the definition of ESG funds, and formulated criteria for ESG fund certification. These criteria are based on the guidelines issued by the regulatory authorities in Japan, while also referencing similar guidelines issued by regulatory authorities in other countries.

As outlined below, Daiwa AM has formulated criteria for two types of ESG fund. Funds belonging to each of

these two categories have already been certified, and are listed in the table below (“Daiwa AM’s ESG Funds”). Besides implementing monitoring to check whether the actual management of each fund is in conformity with the fund certification criteria, we also aim to ensure that there is ample information disclosure which brings across information to customers in an easy-to-understand way.

Daiwa AM’s ESG funds

Daiwa AM’s ESG funds position ESG as a major factor when selecting targets for investment, for example by focusing on ESG risk management in relation to the entire portfolio, or by investing in companies that are emphasizing ESG or the achievement of the SDGs, so as to help bring about the transition to a sustainable society, and it is also important to enable effective disclosure in relation to the above.

Impact funds

A key feature of impact funds is that they should realize not only economic returns but also social returns*, and that it should be possible to realize effective disclosure in relation to these social returns.

* Social returns include environmental returns.

Daiwa AM’s ESG funds

Impact fund	Code	Fund Name
●	2785	Decarbonization Technology Fund (Carbon ZERO)
●	2790	Decarbonization Technology Fund (estimated dividend type) (Carbon ZERO estimate dividend type)
	2800	Global Water Resources Equities Fund
	3256	Women’s Advancement Support Fund (Tsubaki)
	3356	Tsumitate Tsubaki
	3388	Social Problem Resolution Support Fund (Bridge for Smiles)
●	3410	Clean Tech Equity & Green Bond Fund (capital growth type) (Mirai Earth capital growth type)
●	3411	Clean Tech Equity & Green Bond Fund (estimated dividend type) (Mirai Earth estimated dividend type)
●	3417	Clean Tech Equity Fund (capital growth type) (Mirai Earth S capital growth type)
	3470	iFree All World Equity Index All Country
	3488	Global Life Equity Fund (capital growth type) (Bright Life (capital growth type))
	3489	Global Life Equity Fund (estimated dividend type) (Bright Life (estimated dividend type))
	3510	iFree ETF MSCI Japan Human and Physical Investment Index
	3513	iFree ETF FTSE Blossom Japan Index
	3514	iFree ETF MSCI Japan ESG Select Leaders Index
	3515	iFree ETF MSCI Japan Empowering Women Index (WIN)
	3711	DC Daiwa SRI Fund

Making the ESG fund certification process more rigorous

“ESG-washing,” which involves investment activity that pretends to embody concern for the environment and for society regardless of the reality of the situation, has become a problem, and countries throughout the world are tightening up controls relating to ESG investment. In Japan, the Financial Services Agency issued a related Guideline in March 2023, outlining the scope of ESG investment trusts, and the information disclosure items that need to be provided in relation to ESG investment trusts.

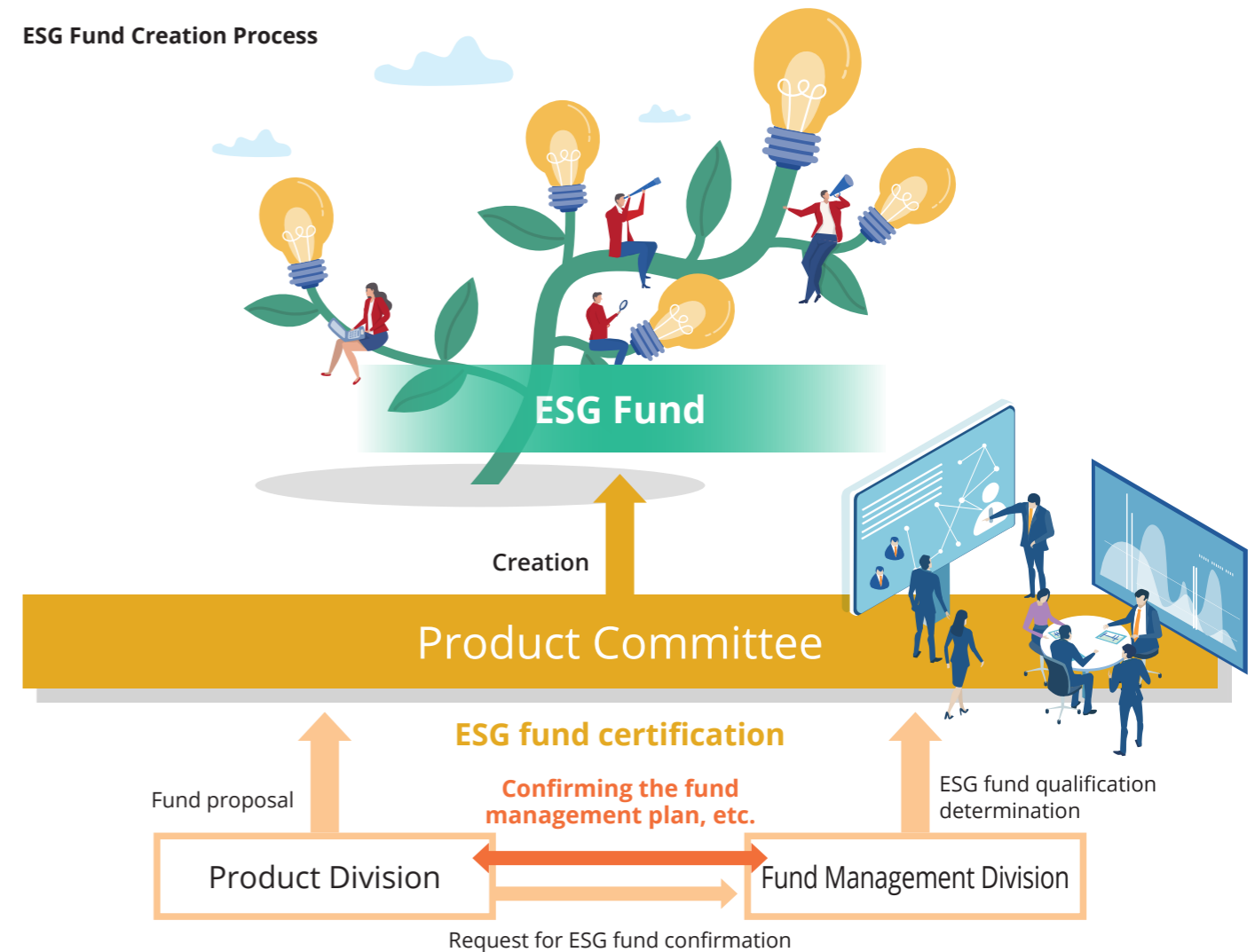
In line with this, Daiwa AM is putting a system in place to provide publicly-offered ESG funds.

The figure below explains the measures taken in the

ESG fund creation process to prevent “ESG-washing.”

When the Product Division asks the Fund Management Division to confirm a particular new ESG fund proposal, the Fund Management Division verifies whether there are any problems with the fund management plan, and whether the proposed fund meets the ESG fund criteria set by Daiwa AM. The verification results are submitted for deliberation at a meeting of the Product Committee, which is attended by members of the senior management team, after which, if approved, it is certified as an ESG fund. Once the certified fund has been established, it undergoes verification by the Product Governance Committee (see p. 97).

ESG Fund Creation Process



Dialog with ESG Data and Index Providers

Daiwa AM has created its own proprietary ESG score system, but we also make use of other ESG score systems provided by third parties, as part of the management process for our ESG index funds, etc. We hold meetings and exchange views, as needed, with ESG index providers and with ESG assessment and data providers in regard to

these third-party ESG scores. In addition, Daiwa AM is a member of the Index Advisory Panel established by JPX Market Innovation & Research, in which capacity we express our views regarding ESG indexes, the TOPIX index, etc.