

Disclosure Based on TCFD recommendations

SMDAM announced its support for the Task Force on Climate-related Financial Disclosures (TCFD) in December 2019. As an investment management firm, we will analyze the impact of climate change on investee companies, both risks and opportunities, and try to translate such an analysis into high-quality investment returns to clients over the long term. At the same time, through engagement we will contribute to realize a sustainable society by supporting the innovations and transitions of investee companies aimed at reducing greenhouse gases (GHG).

I. Basic Concept

1 Governance

1 Supervision by the Board of Directors

Our corporate philosophy and “the Principles of Fiduciary Duties and Sustainability”, which serve as the basic policy for our corporate activities, clearly state our intention, as an investment management firm and as a corporate citizen, to contribute to build a sustainable society. Therefore, sustainability initiatives, including for climate change, are positioned as the most important task of management.

Basic policies and action plans at the company level are developed through an established process in which the policies and plans are fully considered by the Sustainability Promotion Subcommittee at the practical level and by the Management Meeting, which is attended by the CEO and executive officers, and then approved by the Board of Directors.

In addition, the Board of Directors receives reports related to the progress of implementation plans twice a year, and performs monitoring to ensure that operations are being executed appropriately.

In addition, the Board of Directors also engages in lively discussions concerning matters such as ESG integration in investment processes, the status of stewardship activities, and sustainability-conscious business management, while Outside Directors with abundant knowledge provide advice to the management team.

2 Role of Management Team

In formulating company-wide policies and actions plans pertaining to climate change and other sustainability-related issues, the officer in charge of the Corporate Strategy Department leads associated discussions while coordinating with related internal departments. Those policies and plans are deliberated at Management Meetings attended by the CEO and Executive Officers and by other meeting bodies, after which they are approved by the CEO or the Board of Directors depending on their level of importance. The policies and plans are implemented under the responsibility of the CEO. Meanwhile, the Responsible Investment Officer, the pertinent officers in charge in the Investment Management Division and those in charge in the Corporate Division respectively demonstrate leadership in the areas of stewardship activities, asset management operations and risks and opportunities of SMDAM proper, and handle individual risks and opportunities with speed.

2 Strategy

1 Climate Change Risks and Opportunities

We recognize the following as risks and opportunities caused by climate change.

Risks

- A decline in assets under management due to stock prices falling worldwide as a result of economic losses caused by global warming
- A deterioration in relative investment performance due to SMDAM investee companies being negatively impacted by the transition to a carbon-free economy
- An increase in reputational risk due to our investment activities being regarded as inappropriate from the standpoint of the reduction of greenhouse gas (GHG) emissions and our investment products being considered a form of so-called greenwashing
- An increase in costs resulting from factors such as accommodating tighter regulations on climate change-related disclosure in Japan and overseas and procuring renewable energy in order to reduce our own GHG emissions

Opportunities

- An increase in new investment opportunities that include companies with innovative technologies that will contribute to the transition to a carbon-free economy and companies that can be expected to grow through a transformation of their business model
- An improvement in relative investment performance through enhancing our capacity for research and analysis of non-financial information such as endeavors to address the issue of climate change
- Expanded business opportunities from greater investor needs for investment products themed after solving or adapting to the issue of climate change

2 Impact on Business and Strategy

Investment

- We at SMDAM manage all of our active investment products while taking sustainability into consideration. Based on the increasing importance in recent years of such non-financial information, including that on climate change, we are working to further improve investment performance by conducting qualitative and quantitative research and analysis on the impact of non-financial information on stock and bond prices. Additionally, we support the practical application of innovations that will help smoothen the transition to a carbon-free economy and solve the issue of climate change through engagement in the form of dialogue with investee companies and the exercise of voting rights in our capacity as a responsible institutional investor.

Product Development

- We work to develop and provide investment products that accommodate shifts in customer needs. These include investment with sustainability integrated into the investment process in a consistent fashion and products intended to improve sustainability.

Operations

- With a target of effectively zero GHG emissions by SMDAM (Scope 1 & 2) by 2030, we are working to bring down our energy consumption through such measures as promoting efficient office use, procuring renewable energy, and promoting paperless operations. We also established a sustainability procurement policy in July 2021 and are working to reduce GHG emissions in our supply chain (Scope 3).

3 Impact on Finance

One study* has found that if outdoor temperatures were to rise by 2°C as of the year 2100, global GDP per capita in 2100 will be 15-20% lower than that it would be if temperatures remained unchanged from the first decade of this century. This is envisioned to have a negative impact on our profits through the decline in the market capitalization of global stock markets that would ensue. Conversely, on an individual sector and company level, there may conceivably be cases of performance growth through lifestyle shifts and technological innovations. We will work to keep any negative impact on finance to a minimum by ascertaining and investing in sectors and companies where growth can be expected in our capacity as an asset management firm whose forte is active investment. (The results of scenario analysis are indicated under “III.2. Analysis of Portfolio Transition Risks and Physical Risks” on p. 13.

At the same time, given that we are an asset management firm, we do not own production facilities that emit GHGs, and as such are not anticipating any major transition risks that would accompany operation. Additionally, we operate our businesses out of relatively small-sized offices that we maintain in major cities in Japan and overseas, and as such are not anticipating any major physical risks that would accompany climate change. Carbon offsetting, which is considered necessary to achieve effectively zero GHG emissions by 2030, is a factor that will increase costs. However, it is believed that any impact will be kept to minute levels.

*Overview of the IPCC's Special Report on Global Warming of 1.5°C (July 2019), Ministry of the Environment

3 Risk Management

1 Climate Change Risk Evaluation

We assess climate change risks of investee companies using proprietary ESG evaluations and assign scores based on those companies' relative performance within their same sector. The issue of climate change is also one of our priority ESG themes. We practice engagement primarily with sectors that have high GHG emission levels and with companies that have considerable room to improve their ESG scores. Meanwhile, for our leading investment products, we measure climate change risks in portfolio units, verify measurement values for our entire portfolio as well as those for the investee companies that comprise it, and utilize them in investment decisions pertaining to stock selections. For information on the conformance of our portfolio with the Paris Agreement, please see “III.3. Analysis of Conformance of Portfolio with Paris Agreement” on p. 14.

2 Management of Climate Change Risks

In cases where climate change risk metrics are included in the investment guidelines of specific products, the Investment Management Division autonomously manages them just as it does other constraints. In addition, the Risk Management Department monitors the status of compliance and issues requests to the Investment Management Division to take the necessary actions or decide on a policy to deal with situations in which thresholds are closely approached or encroached.

II. Progress in Immediate Term

In March 2022, SMDAM became a member of the Net Zero Asset Managers Initiative (NZAMI) for asset management firms aiming to realize a society with net-zero GHG emissions. We plan on disclosing our near-term targets as of 2030 on our website in the course of FY2022.

Our Board of Directors adequately monitored executive actions and also supplied advice upon SMDAM's joining of NZAMI so that our response to climate change risks would translate into benefits for our stakeholders (our customers, shareholders and employees as well as greater society).

In October 2021, we established a department to promote sustainability across the company in the form of the Sustainability Promotion Office. Every month, we hold Sustainability Promotion Subcommittee meetings intended to promote the execution of sustainability-related operations that include the management of SMDAM's climate change risks.

In FY2021, we conducted about 700 instances of exclusive engagements related to climate change and other environmental aspects across the globe. In those, we held dialogues largely to encourage high-quality information disclosure based on superior case examples of disclosure. Additionally, as a form of CDP collective engagement, we led efforts to encourage five Japanese corporations to acquire a CDP score.

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III. Status of Portfolio

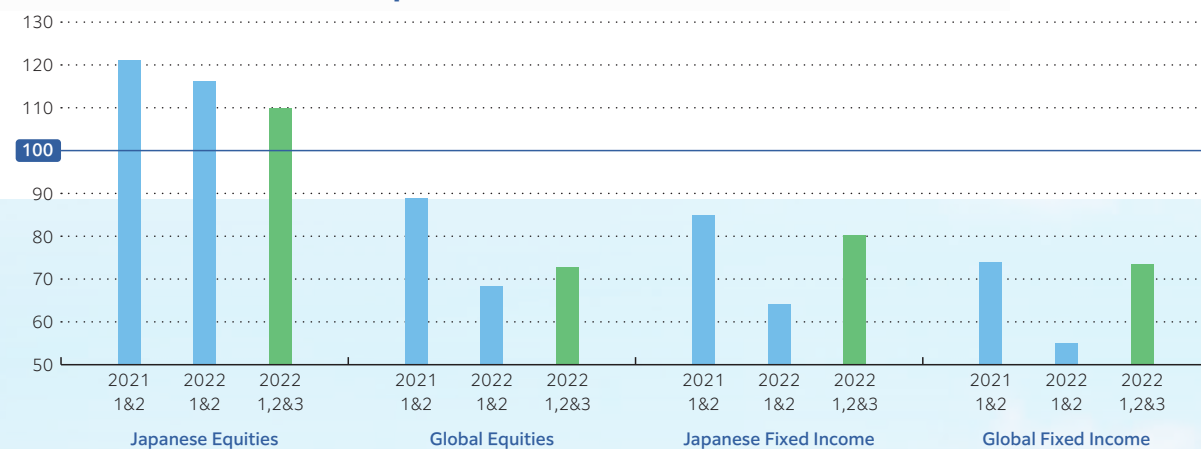
1 GHG Emissions in Portfolio

We performed a comparative analysis between SMDAM portfolio that we manage in-house or consign to external parties and benchmarks for carbon footprint, or GHG emissions per million USD of portfolio value as of the end of March 2022. SMDAM portfolio consists of four asset classes, namely Japanese Equities, Global Equities, Japanese Fixed Income and Global Fixed Income

*2: Externally-consigned fixed income excludes FOF and listed investment trusts. Global and Japanese fixed income exclude government bonds and government institution-related bonds.

A look at our carbon footprint (Scopes 1, 2 & 3) as of March 2022 shows that while results for Japanese equities exceeded benchmarks, results for other asset classes fell below them. Japanese equities were impacted by the overweighting of materials and industrials with both high value and carbon footprint.

Our Portfolio and Carbon Footprint for Each Asset Class (Benchmark=100)



Source of data: MSCI*3 used for 2022. Sustainalytics used for 2021.
 Benchmarks: TOPIX used for Japanese equities. MSCI KOKUSAI used for global equities. Nomura BPI (corporate bonds) used for Japanese fixed income. Bloomberg Global Aggregate Ex-Japan (corporate bonds) used for global fixed income. Benchmarks were applied to portfolios managed by SMDAM as of March 2022. Global and Japanese fixed income exclude government bonds and government institution-related bonds.
 Portfolio emissions = $\sum [\text{GHG emissions of issuers} \times (\text{Market value of portfolio holdings}) \div \{(\text{Issuer market cap}) + (\text{Total issuer interest-bearing debt})\}]$
 Carbon footprint = GHG emissions per million USD of portfolio value = Portfolio GHG emissions \div Portfolio value
 Changes from previous year
 We expanded the scope of aggregated assets to newly include external consignees (excluding FOF and listed investment trusts). Scope 3 was also made a new target for GHG emissions.
 *3: For details, please see the disclaimer on p. 54.

While various means of contributing to the realization of carbon neutrality by the year 2050 exist, our policy will be to focus on engagement while making divestment an option based on the philosophies of "Just Transition" and "Leave No One Behind" under SDGs. We are insistent in our requests to investee companies that they proactively conform with a decarbonized society, meaning that they reduce GHG emissions while simultaneously promote the creation of value as those who will usher in the green revolution.

2 Analysis of Transition Risks and Physical Risks in Portfolio

Using the "CVaR" analysis tool supplied by MSCI, we performed an analysis of the transition and physical risks in our portfolio. For the purpose of that analysis, in addition to the most difficult scenario of halting the rise in average outdoor temperatures until the year 2100 to 1.5°C, we used scenarios in which that rise was 2.0°C and 3.0°C. The purpose of this scenario analysis is to quantitatively ascertain the latent damage to our portfolio caused by climate change stress. More so than extracting accurate forecast figures, it is designed to enable us to draw up a future image of a scenario in which we subject our portfolio to stress without taking sufficient action.

Transition risks	Policy risks	... An increase in costs pertaining to GHG emitted by investee companies over the period between now and roughly 15 years in the future
	Technological opportunities	... Growth in profit through contributions associated with the transition to a low-carbon society, such as the cultivation of new markets and the absorption of GHG
Physical risks		... Costs resulting from the impairment of noncurrent assets and suspension of business activities due to natural disasters such as typhoons and floods

Latent Damage to Value of Portfolio by Temperature Rise Scenario/Asset Class (As of March 2022)

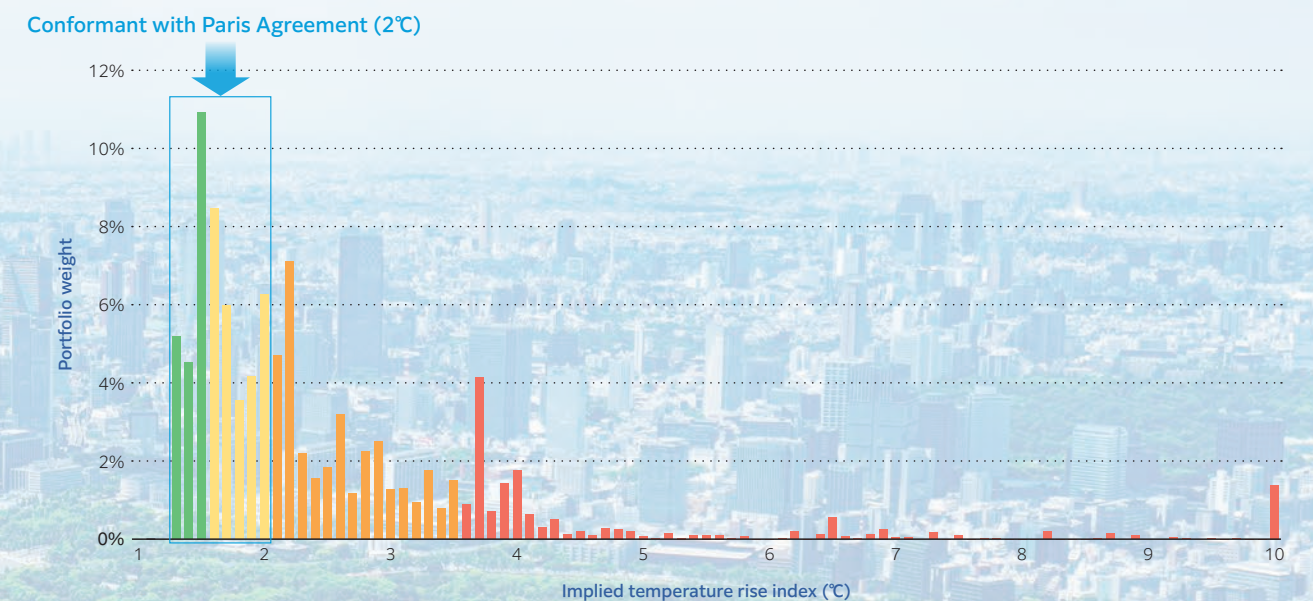
Asset class	Companywide portfolio	Japanese Equities	Global Equities	Japanese Fixed Income	Global Fixed Income
Scenario	1.5°C				
Transition risks + Physical risks	[Heatmap showing damage to value]				
Transition risks	[Heatmap showing damage to value]				
Policy risks	[Heatmap showing damage to value]				
Scope 1	[Heatmap showing damage to value]				
Scope 2	[Heatmap showing damage to value]				
Scope 3	[Heatmap showing damage to value]				
Technological opportunities	[Heatmap showing value creation]				
Physical risks (by cause)	[Heatmap showing damage to value]				
Coastal flooding	[Heatmap showing damage to value]				
Excessive heat	[Heatmap showing damage to value]				
Typhoons	[Heatmap showing damage to value]				
River flooding	[Heatmap showing damage to value]				
Physical risks (by region)	[Heatmap showing damage to value]				
JP	[Heatmap showing damage to value]				
CN	[Heatmap showing damage to value]				
US	[Heatmap showing damage to value]				
TH	[Heatmap showing damage to value]				
SG	[Heatmap showing damage to value]				
Other	[Heatmap showing damage to value]				

The results of this analysis indicate that transition risks (policy risks plus technological opportunities) in our portfolio are extremely limited. Conversely, physical risks to our Japanese equities and fixed income, which account for a large percentage of our portfolio, are high. Based on these results, we will engage in dialogue with high-risk investee companies so that they adequately deal with latent risk as we aim to lower the risks in our portfolio.

3 Analysis of Conformance of Portfolio with Paris Agreement

For the implied temperature rise index, we indicate conformant climate change target estimates in "°C" units based largely on the GHG emission targets that our investee companies have committed to. We have arrived at the result that 49% of our portfolio will be conformant with the 2°C scenario under the Paris Agreement in the future. On the other hand, investee companies that will not be conformant with the Paris Agreement at all under existing plans (the area indicated by the red line graph) constitute 16% of our portfolio. To lower climate change risks in our portfolio, adequate risk management for those investee companies will be of the essence.

Distribution of Implied Temperature Rise Index (As of March 2022)



For information on the status of our portfolio (FY2021), please see our website.
<https://www.smd-am.co.jp/english/corporate/vision/fiduciary/03/>

