



# GPIF's Endeavor as a Universal Owner - Aligning Interests for Long-Term Value Creation -

年金積立金管理運用独立行政法人  
Government Pension Investment Fund

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August 20, 2019



Government Pension  
Investment Fund

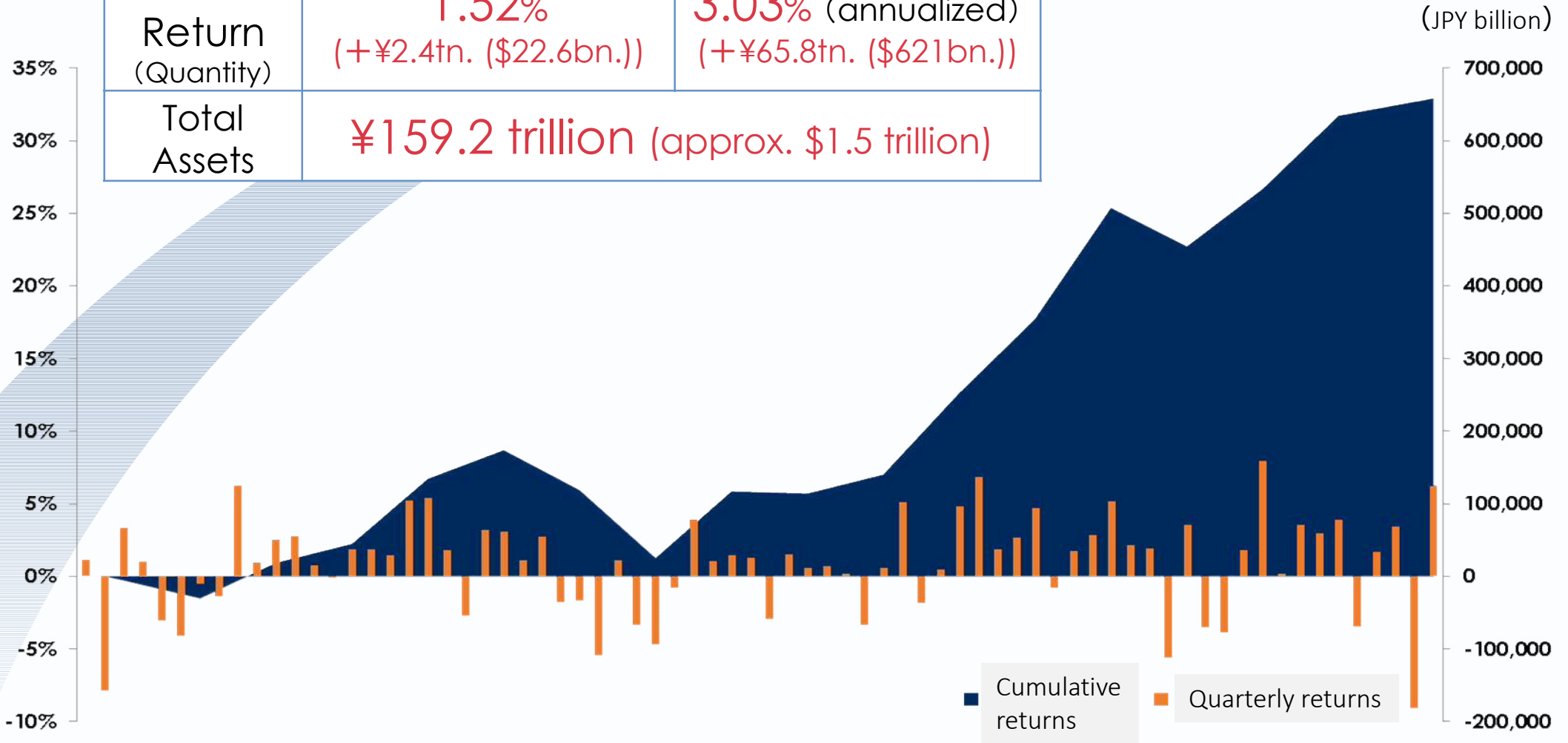


# About GPIF



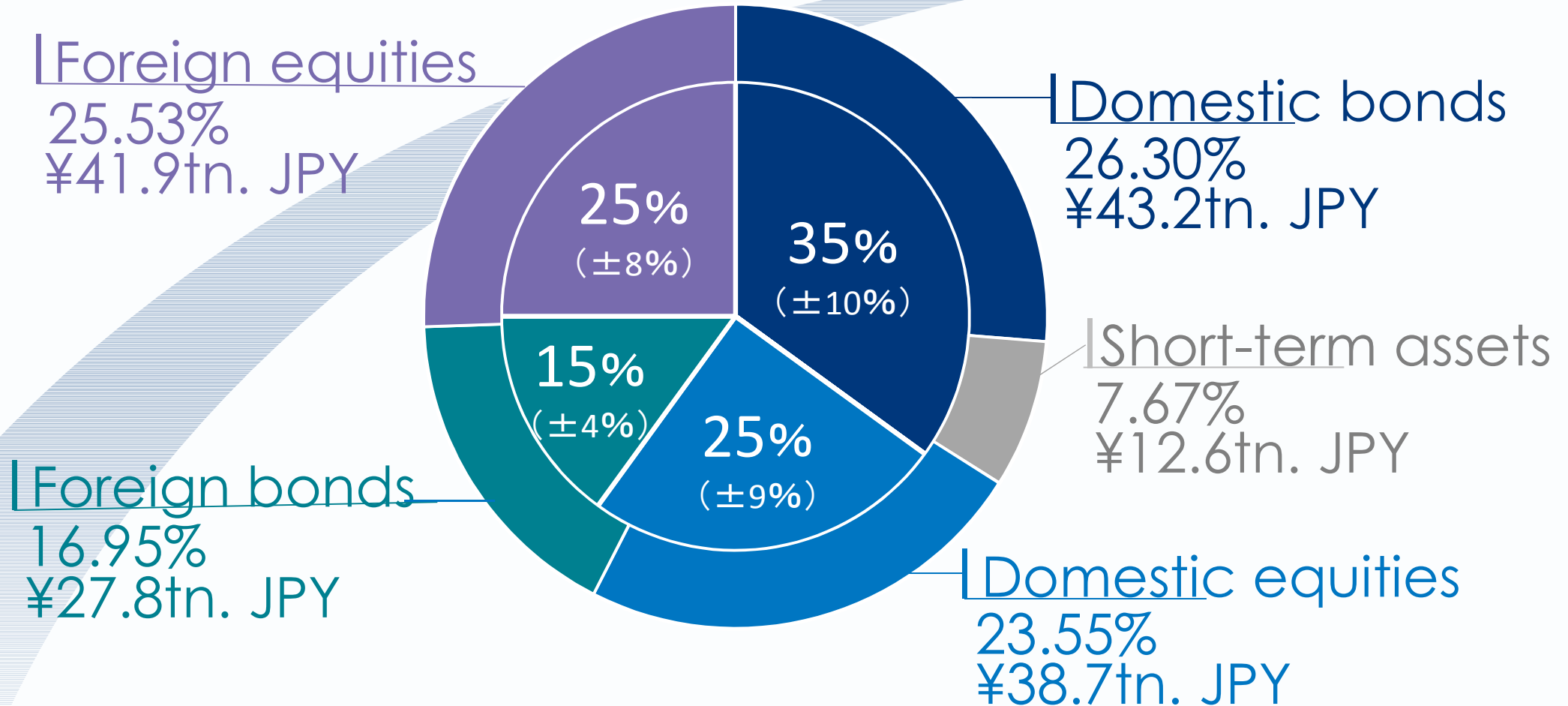
# First, Some Basics...

	FY2018	FY2001 to FY2018
Rate of Return (Quantity)	<b>1.52%</b> (+¥2.4tn. (\$22.6bn.))	<b>3.03%</b> (annualized) (+¥65.8tn. (\$621bn.))
Total Assets	<b>¥159.2 trillion</b> (approx. \$1.5 trillion)	



\*As of Apr. 1, 2019

# First, Some Basics...



Inside : Policy asset mix

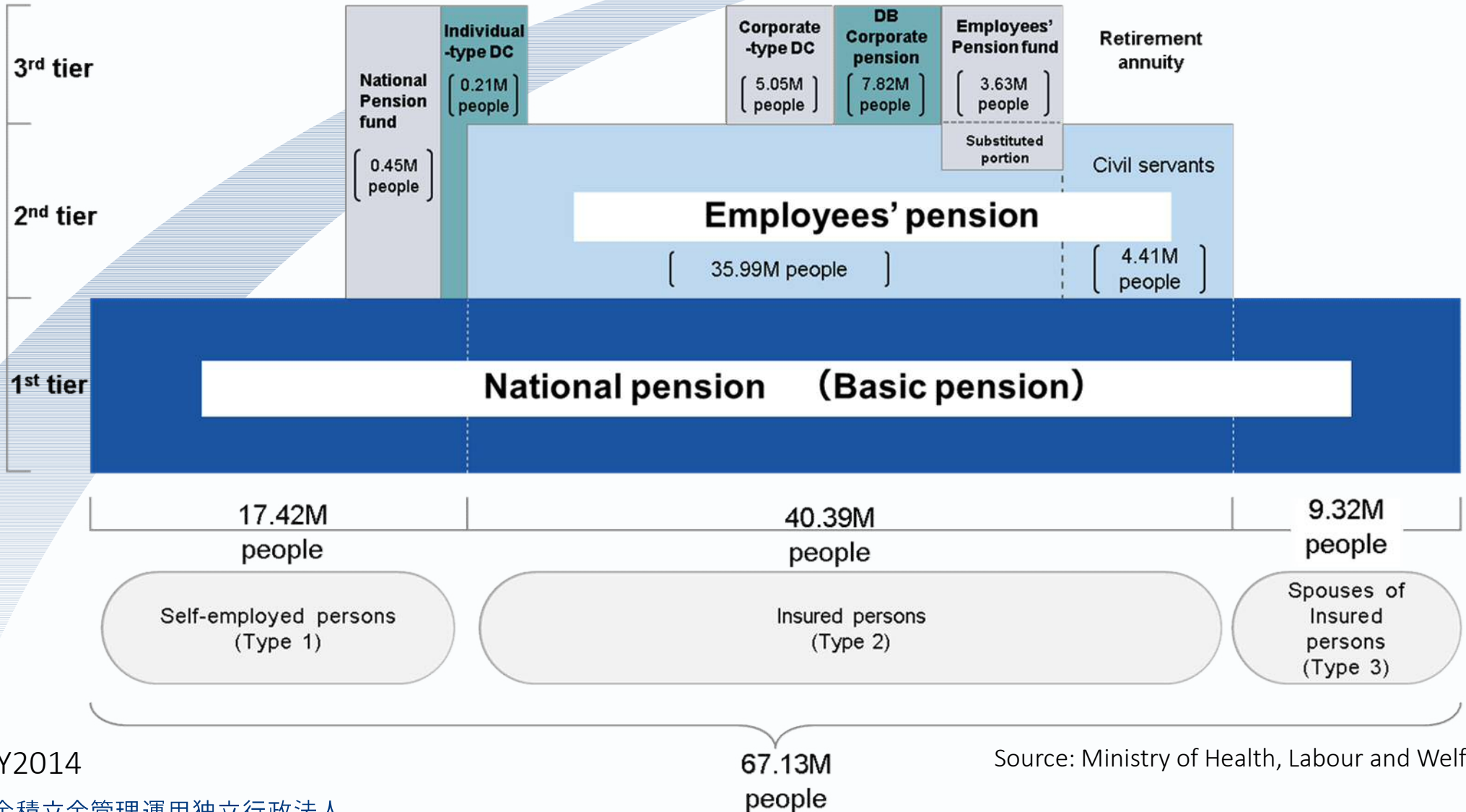
Outside : Actual portfolio as of March 31, 2019

(figures in parentheses indicate deviation limits)

# First, Some Basics...

## Japanese Pension System Overview

(All figures valid as of end-March 2015)

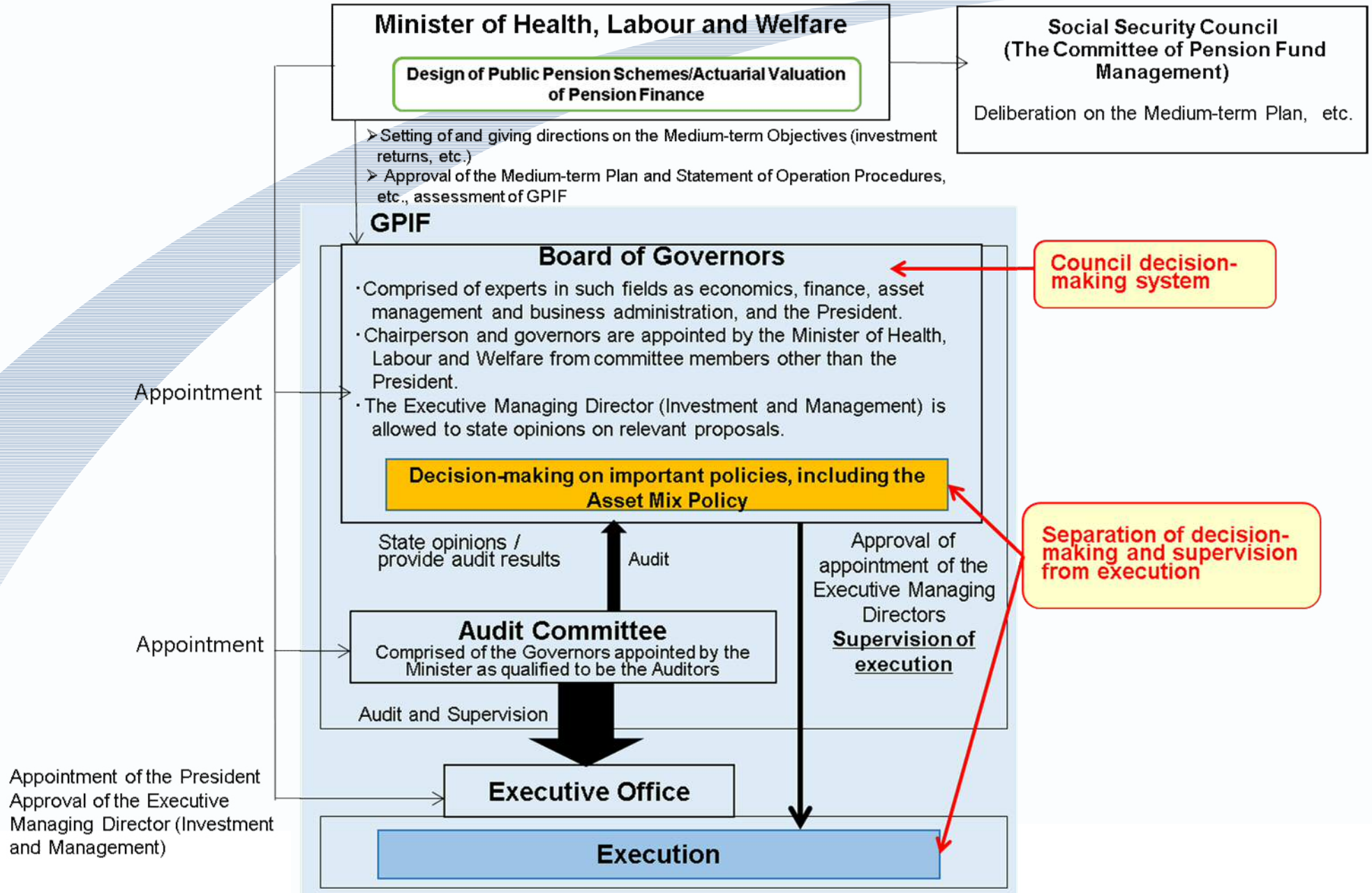


\*FY2014

Source: Ministry of Health, Labour and Welfare

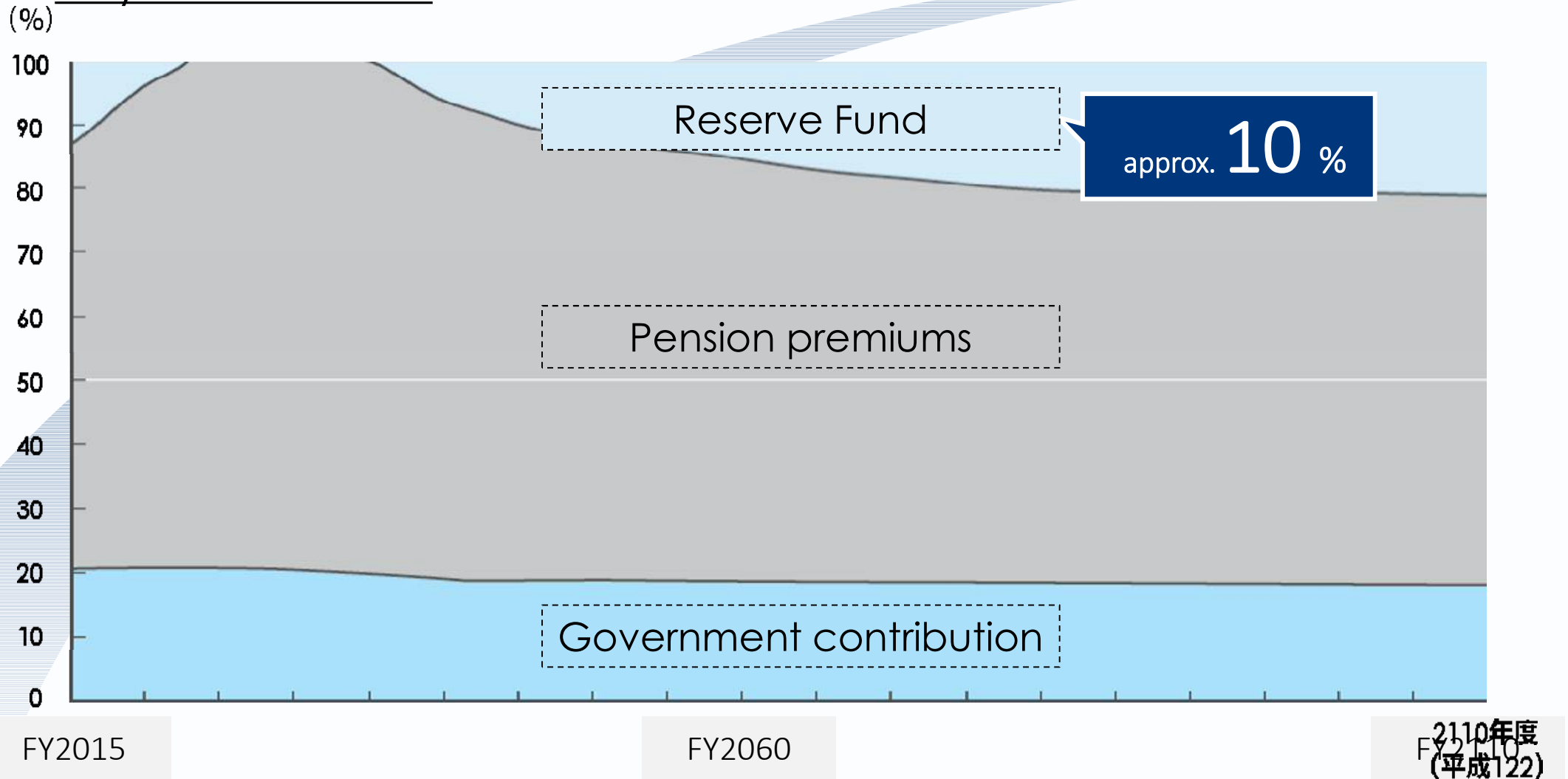
# First, Some Basics...

## GPIF Governance Structure



# First, Some Basics...

## Payout Structure



Note: Actuarial valuation conducted in FY2014. Assumes inflation rate of 1.2%, real wage growth of 1.3%, and real investment return of 1.7%



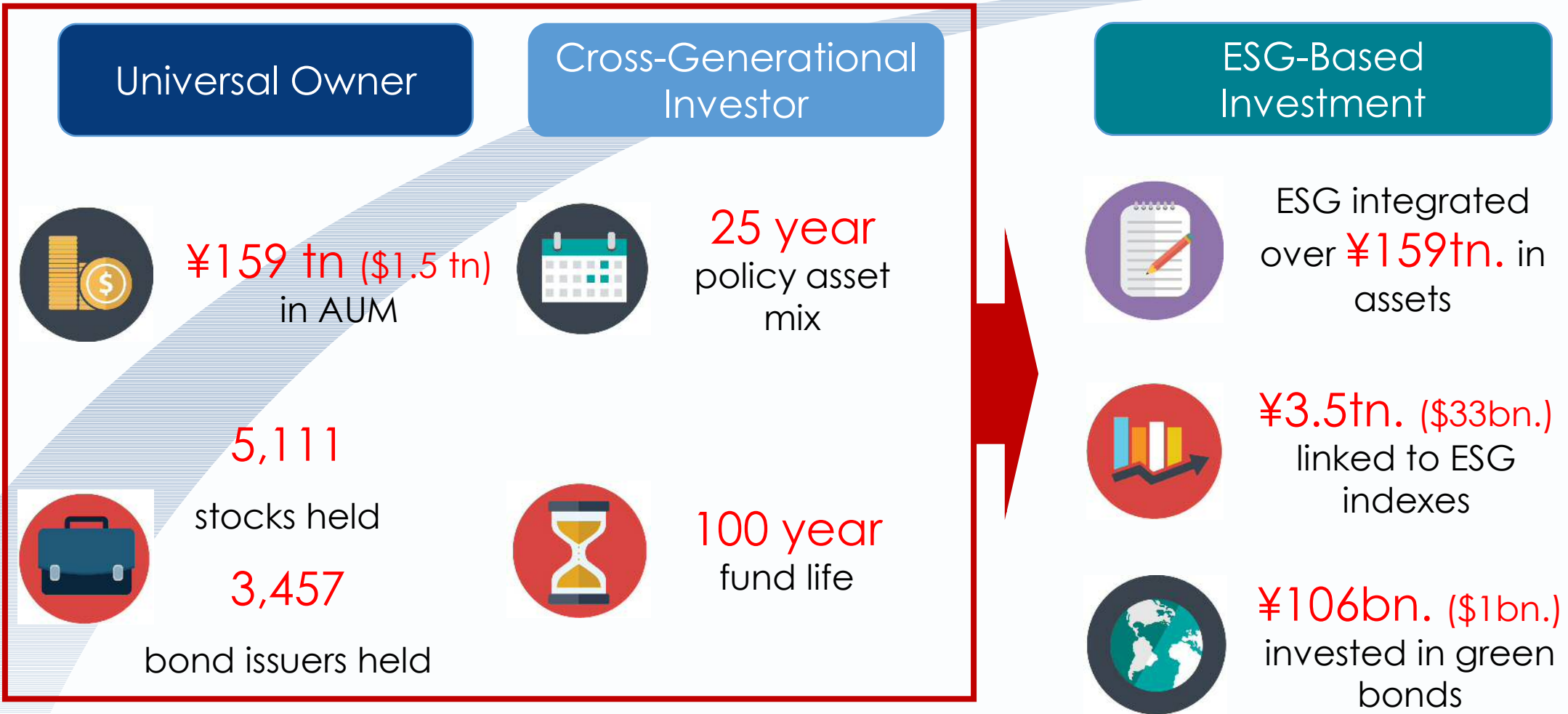
# Promoting Long-Termism: Driving ESG Investment





# Driving ESG Investment

## Quick Facts



Our objective is to make the market more sustainable, not beat it.



# Our Investment Principles

Our overarching goal should be **to achieve the investment returns required for the public pension system with minimal risks**, solely for the benefit of pension recipients from a long-term perspective, thereby contributing to the stability of the system.

Our primary investment strategy should be **diversification by asset class, region, and timeframe**. While acknowledging fluctuations of market prices in the short term, we shall achieve investment returns in a more stable and efficient manner by taking full advantage of our long-term investment horizon. At the same time, we shall secure sufficient liquidity to pay pension benefits.

We formulate the policy asset mix and **manage and control risks at the levels of the overall asset portfolio, each asset class, and each investment manager**. We employ both passive and active investments to attain benchmark returns (i.e., average market returns) set for each asset class, while seeking untapped profitable investment opportunities.

By **fulfilling our stewardship responsibilities (including the consideration of ESG (Environmental, Social, and Governance) factors)**, we shall continue to maximize medium- to long-term investment returns for the benefit of pension recipients.



# Driving ESG Investment: Why We Do It

## Investment Principle #4



Maximize long-term return for beneficiaries through ESG and other stewardship

## Proxy Voting Principles



To enhance long-term value, managers should consider ESG issues when voting.

## Stewardship Principle #4



Managers should integrate ESG



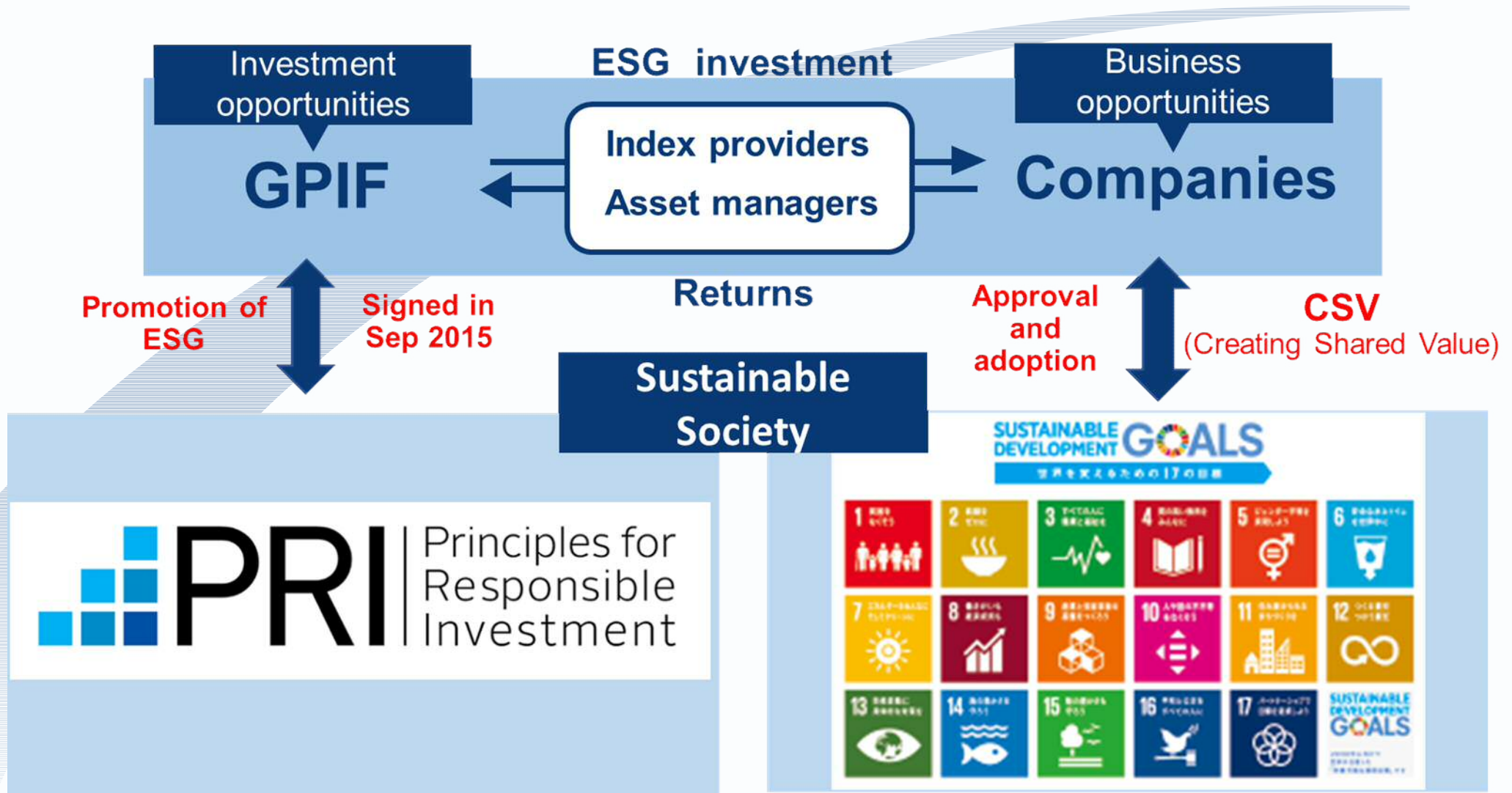
Managers should proactively engage



Managers should sign on to PRI

Prevent Short-Termism to Create Long-Term Value

# Driving ESG Investment



# Driving ESG Investment

## Holistic Approach

PRI

TCFD

Thought Leadership

Global Asset Owner Forum

Fixed Income ESG Research

30% Club/30% Coalition

Climate Action 100+

Research on ESG Disclosure

## Portfolio Approach

### Direct

Adoption of ESG Benchmarks

Green Bond Investment with Intl. Institutions

### Indirect

ESG Integration-Based AM Evaluations

Stewardship-Based AM Evaluations

Engagement with Index Providers

AI Research



# Promoting Long-Termism: Holistic Approach





# Holistic Approach: Improving the Global Market

Signatory of:



Signed in September 2015. Hiro Mizuno was designated MD in January 2017 and joined the Asset Owner Advisory Committee and the SDGs Advisory Committee.



Signed in November 2016.



Signed in November 2016.



Hiro Mizuno is one of the founding members of the Climate Financial Leadership Initiative launched in January, 2019.



Announced support in December 2018.



Joined in October 2018.



# Holistic Approach: Fixed Income ESG Research

The GPIF and World Bank Released a Joint Study On the ESG Investment Environment for Fixed Income Investors

## Results

- ESG investing is increasingly becoming mainstream.
- ESG factors pose a material credit risk for fixed income investors.
- Many issues remain in ESG definitions, data, engagement, and supply/demand balance.





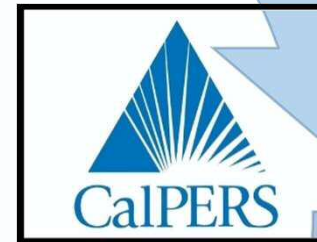


# Holistic Approach: Global Asset Owner Forum

GPIF Co-Created the Global Asset Owner Forum With CalPERS and CalSTRS to Discuss Common Challenges Facing Global Asset Owners

## Themes

International Initiatives  
ESG Disclosure  
AM Compensation  
ESG Research/Ratings  
etc...



CALSTRS



Others...



# Holistic Approach: Thought Leadership

- GPIF's ESG activities were featured in a Harvard Business School (HBS) case study entitled “Should a Pension Fund Try to Change the World? Inside GPIF's Embrace of ESG”
- The case, written by Profs. Rebecca Henderson, George Serafeim, Josh Lerner and Naoko Jinjo, was taught in HBS's “Reimagining Capitalism” class.





# Promoting Long-Termism: Direct Portfolio Approach





# Direct Portfolio Approach: ESG Benchmark Adoption



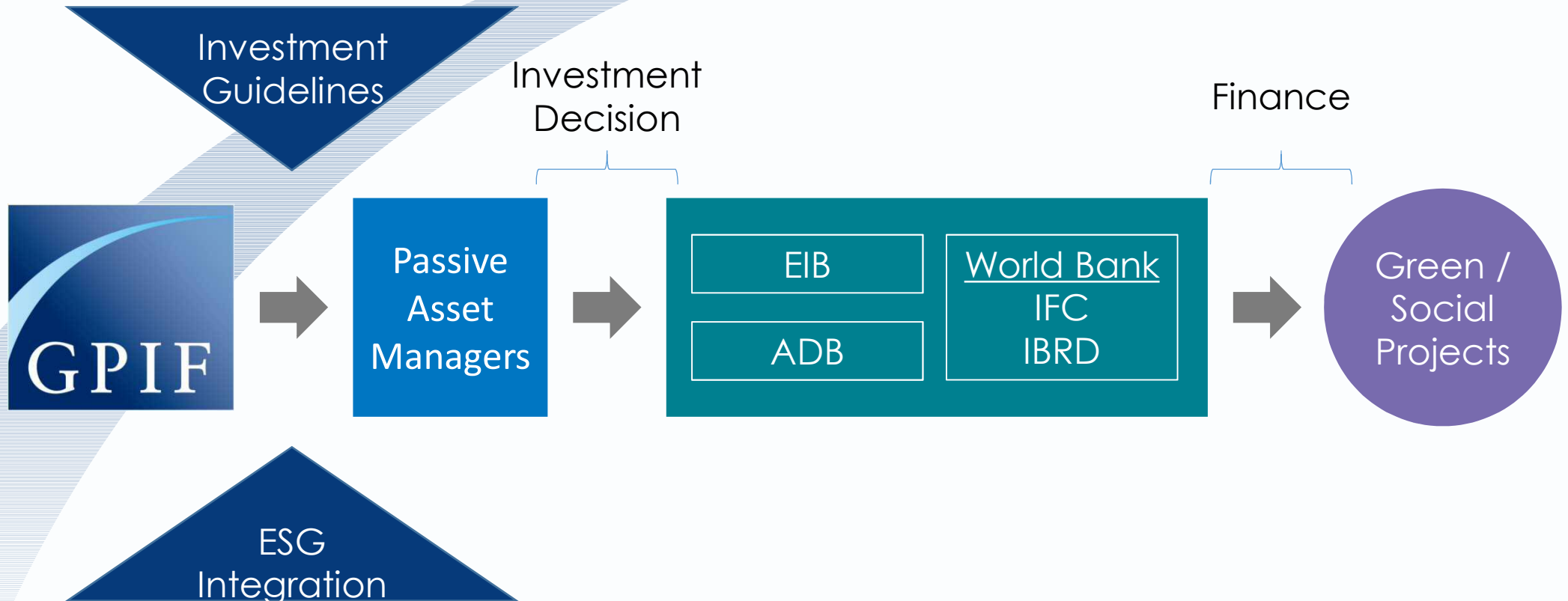
<u>Concept</u>	ESG	ESG	Diversity	Low Carbon	Low Carbon
<u>Asset Class</u>	Domestic Equities	Domestic Equities	Domestic Equities	Domestic Equities	Foreign Equities
<u>Cumulative Returns*</u>	3.90%	5.17%	5.77%	5.10%	9.16%
<u>Excess Over Benchmark*</u>	-0.99%	0.28%	0.65%	0.21%	0.21%

- All benchmarks overweight companies with **high metrics/positively screen**
- Benchmarks **do not divest** from any specific industry



# Direct Portfolio Approach: Green Bond Investment

The GPIF Has Partnered with the World Bank and Other Multi-National Institutions to Mobilize Capital to Green Projects





# Promoting Long-Termism: Indirect Portfolio Approach





# Indirect Portfolio Approach: Our Expectations

## We expect our asset managers to:



Understand and apply GPIF's Stewardship Principles and Proxy Voting Principles



Implement an internal compensation scheme that promotes long-termism



Practice good governance and work to prevent conflicts of interest



Improve disclosure with respect to voting, ESG materiality and TCFD recommendations



Integrate ESG in line with investment style

## We promote this through:

### Passive Managers

- Having passive managers practice **active ownership**
- Engaging with **index providers**

### Active Managers

- Introducing **performance-based fee structure** and multi-year contracts
- Commission research to **understand manager dynamics**



# Indirect Portfolio Approach: ESG-Based Evaluation

All managers are required to integrate ESG into investment processes and engage with companies.

## Integration

- We define ESG integration as the explicit and systematic inclusion of ESG issues in investment analysis and investment decisions.

## Engagement

- GPIF requires each external asset manager to identify and engage on critical ESG issues.

## Evaluation

Investment Policy revised to include ESG Integration

Weight	Equity passive	Equity Active
100% Qualitative	30%	10%
	70%	90%

Active managers should generate quality alpha

Stewardship activities

Investment policy, management process, organization, human resources, etc.





# Indirect Portfolio Approach: Passive Mandate

## Index Provider Engagement



### What We Engage On

Index Governance

- Internal Structure
- Transparency
- Conflicts of Interest etc.

Index Consultation

- Provide input on index construction, evaluation process, etc.



# Indirect Portfolio Approach: Passive Mandate

## Manager Engagement

Asset Managers

GPIF

Propose Business Model

Select Based on Model

Selection

“New Passive Investment”

- Create engagement plans
- Select assessment metrics
- Measure stewardship outcomes

Has the manager:

- Set appropriate KPIs?
- Established an appropriate engagement framework?

Assessment

Equity passive

30%

70%



GPIF checks achievement

Contract Awarded

Stewardship activities

Investment policy, management process, organization, etc.



# Indirect Portfolio Approach: Active Mandate

## Performance-Based Fee Structure

### Concept

- We should pay active managers **based on alpha** generated

- If no alpha is generated, active managers should receive the **same fees as passive** managers.

- Payment should be **linked to long-term** performance

### Our Expectations

Set appropriate alpha targets

Maintain capacity for stable excess returns

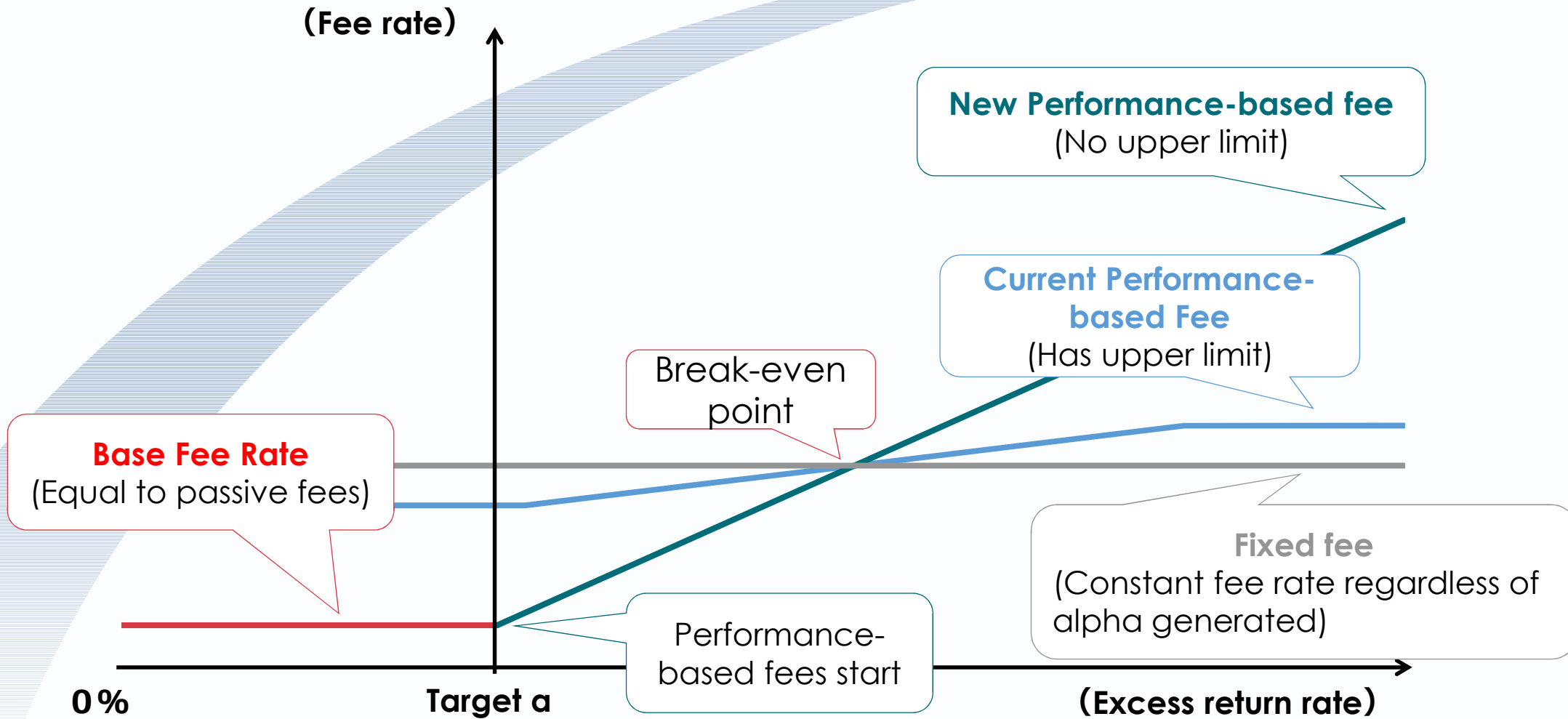
Aim for long-term sustainable performance

Alignment Not Reduction



# Indirect Portfolio Approach: Active Mandate

## Performance-Based Fee Structure





# Indirect Portfolio Approach: Active Mandate

Understand internal dynamics at asset managers

## Mercer Compensation Scheme Analysis

What we wanted to test:



1) Does pay scheme contribute to long-term returns?



2) Does pay scheme result in short-termism?

How we tested it:



Questionnaires and interviews with asset manager C-level executives

Our findings:



Positives

- Managers generally have compensation structures that avoid short-termism
- Leading asset managers take context, history, etc. into account in pay structure



Negatives

- Most managers don't use structure strategically
- Few asset managers compensate ESG staff appropriately



# Indirect Portfolio Approach: AI-Based Research

Understand internal dynamics at asset managers

## AI-Based Research

FY2017 Commissioned Research

**Analyze massive amounts of domestic equity active manager transaction data to understand:**

- **Actual investment style** based on behavior, not self-assessment
- Changes in investment styles ("**Style Drift**")
- **Formation of bubbles** due to many managers practicing a specific investment style

FY2018 -19 Commissioned Research

- Expand research to other asset classes
- Apply analysis to selection and evaluation of asset managers



# Our Common Endeavor As Universal Owners





# Our Common Endeavor As Universal Owners

In order to overcome short-termism in our investment chain and fulfill our fiduciary duty,

Partnership With Other Asset Owners is Key



Together we have an immense responsibility to bolster the sustainability of global capital markets.