Japan's Asset Management Business 2024/25

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Nomura Research Institute

Foreword

As the asset management industry gets the policies it long sought, it now needs to pursue in earnest the longstanding task of developing market-competitive investment capabilities. With the plan to transform Japan into an “asset management nation,” the authorities want to promote the healthy development of the asset management industry and make it one of the four major financial subsectors along with banking, insurance, and securities. But this will not be easy. If sector size is measured using the yardstick of operating income, the asset management industry will need to more than double its operating income to put itself on a par with the other three. However, operating income posted its recent peak in FY2021 and has not grown since then despite an increase in retail and pension fund assets under management. This is because fund inflows have been concentrated in passive funds with falling fees and in actively managed foreign equity funds, which re-entrust the management of those funds to overseas managers.

Many Japanese asset management firms have outsourced management as a stopgap measure to address increasingly diverse investor needs (mainly involving overseas assets) or to round out their own uncompetitive product lineups. They were able to grow so rapidly precisely because they flexibly outsourced operations to sub-advisories. However, few have been able to build the kind of market-competitive investment capabilities that were envisioned. Now it is becoming increasingly apparent that profits will not grow without those capabilities. The process will not be easy, but companies’ futures will hinge on their ability to build investment operations with a clear philosophy and process that can be trusted to deliver returns.

This report aims to provide a starting point for thinking about the future direction of the asset management business. Its intended audience includes the senior management and marketing/sales planning staff of asset management companies and financial product distributors. The asset management business is expected to play an increasingly important role as the transition from saving to wealth formation accelerates, and we hope this report adds to readers’ understanding of recent developments in Japan’s asset management industry.

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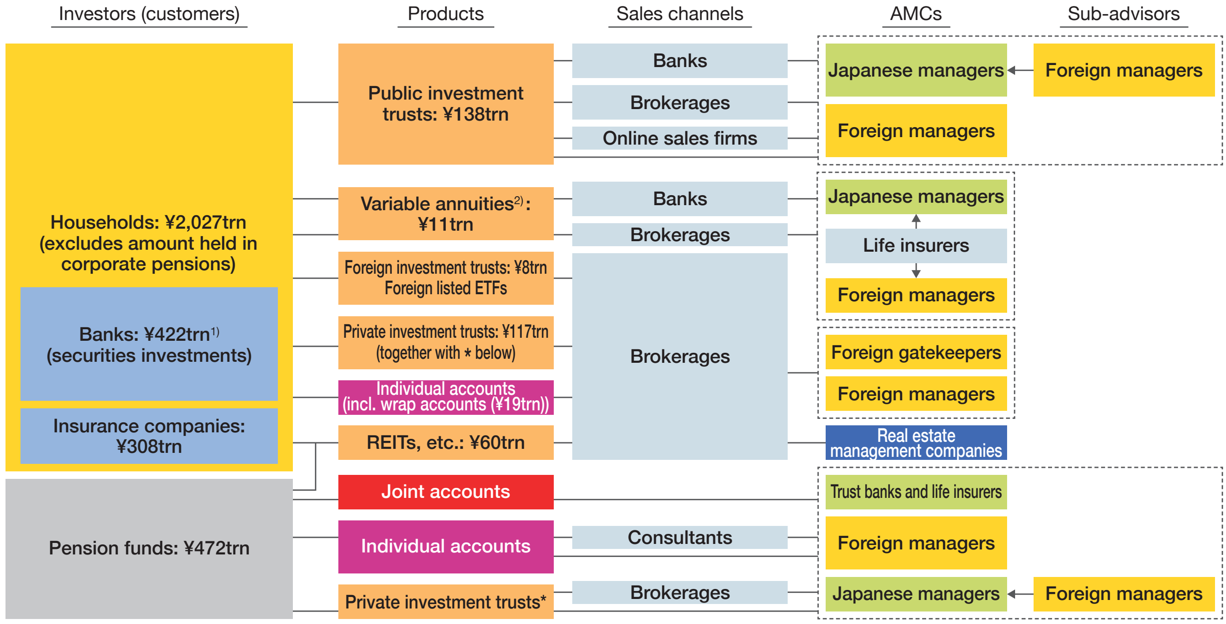
CHAPTER 1

Japanese investor trends

Mounting expectations for growth in Japan's asset management business

In FY2023, the industry was able to reverse the previous year's unusual decline in operating income despite an increase in average outstanding AUM. The causes of that result—a dramatic shift to passively managed public investment trusts and a decline in investment revenues due to more intensive price competition between passive funds—were still in evidence in FY2024, but operating income grew 10% YoY on a sharp rise in the market value of foreign bonds and both foreign and domestic equities. Expectations of industry growth have been rekindled as a result. Public investment trusts have seen unprecedented fund inflows amounting to ¥15trn in annualized terms since the new NISA program was launched in January 2024[1]. Further, changes to the basic portfolios of public pension funds and policies aimed at achieving more sophisticated management of pension fund reserves (including corporate pensions) have encouraged hopes of sustained growth in AUM. That said, companies will have to add more value in their investment operations to ensure that higher AUM leads to higher investment revenues. Pension funds and other asset owners will need to adopt a more rigorous process for selecting managers. Retail investors now have a much better understanding of the importance of financial knowledge. This means customers—whether pension funds or retail investors—are likely to become even more demanding when assessing whether they are

Exhibit 1. Overview of Japan's asset management business (as of end-March 2024)



Note1: Excludes Norinchukin Bank and Zenkyoren.
Note2: Value for variable annuities refers to policies in force in previous fiscal year (end-March 2023).
Source: NRI, based on various data

receiving services worth the investment fees they are paying.

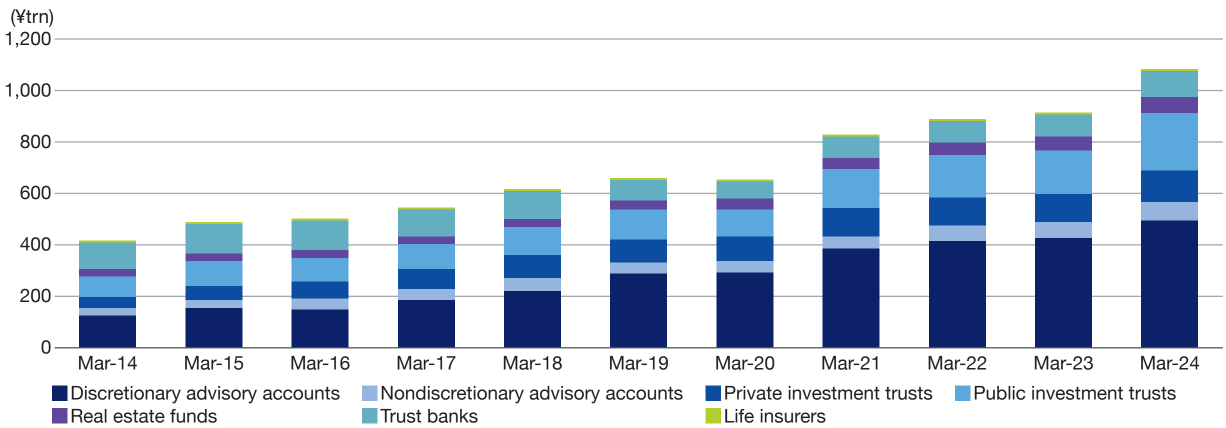
Below we provide an overview of the asset management business at the end of FY2023. Exhibit 1 illustrates Japan's asset management market as of end-March 2024 from four perspectives: investors, products, sales channels, and asset management companies (AMCs). The graphic offers a simple representation of who is managing whose money through whose meditation. There are three main types of customers for management firms in Japan: retail investors (households), corporations including financial institutions, and pension funds. After adjusting for the fact that funds invested by financial institutions consist basically of retail deposits, we estimate that Japanese investors hold assets worth ¥2,488trn in total, which is ¥198trn more than the figure a year ago. Households are responsible for ¥127trn of the increase and pension funds for ¥70trn. We estimate that ¥1,079trn of these assets[2)] are managed by AMCs, marking a ¥170trn YoY increase and topping the ¥1,000trn mark for the first time (Exhibit 2). This figure now represents fully 43% of all financial assets in Japan.

Household, pension fund, and financial institution trends

The breakdown of the ¥2,027trn in household financial assets has changed dramatically in recent years. Deposits and insurance previously accounted for more than 75% of the total, but their combined share has been gradually declining since FY2020 and slipped below 70% at the end of FY2023. In their place, the share of investment trusts and listed equities increased from 9% at end-FY2019 to 15% at end-FY2023. The main reason was the Tsumitate NISA program that began in 2018 and helped popularize long-term, diversified investments with regular contributions among retail investors. The new NISA program launched in January 2024 is especially popular among younger investors in their 30s. The government has also revealed plans to increase the contribution limit for individual defined contribution (iDeCo) investment accounts and raise the maximum age for both joining the program and starting withdrawals to encourage people of all ages to build their wealth. As these policies could have significant long-term effects, there are high expectations for sustained fund inflows into investment trusts.

Pension funds, the largest institutional investors, are estimated to have held ¥472trn in assets at the end of March 2024. Of this total, public pensions accounted for ¥325trn (up ¥59trn from end-FY2023)

Exhibit 2. **AUM at asset management companies**



Note: Life insurers' AUM represents DB pension assets in special accounts.
Source: NRI, based on Japan Investment Trust Association (JITA) and Japan Investment Advisers Association (JIAA) data and financial statements of AMCs

and corporate pensions for ¥114trn (up ¥10trn). The growth in assets was due primarily to a sharp increase in asset prices and not to new fund inflows. Because of maturation, we can no longer expect investment funds at either public or corporate pension funds to continue growing because of an excess of contributions over distributions. Nevertheless, funds entrusted to asset managers could still increase. Public pension funds underwent a financial verification process for the first time in five years, and changes to their basic portfolio are currently being considered. It is hoped that a new basic portfolio might feature an increased allocation to asset classes with a high percentage of outside management, such as foreign bonds and both foreign and domestic equities, and a growing number of asset management companies are therefore anticipating increased revenues from pension funds.

Of the ¥730trn in investment securities held by banks and insurance companies, "other securities," which consist mainly of fund investments, stood at almost ¥120trn at the end of March 2024. This figure included ¥9trn at major banks, ¥21trn at regional and shinkin banks, ¥57trn at Japan Post Bank, ¥7trn at cooperative financial institutions, and ¥18trn at life insurers. Net fund inflows have declined but remain net positive, averaging around ¥5trn a year since FY2018. As the Bank of Japan proceeds to normalize monetary policy, we see little likelihood of the broader financial sector increasing its fund investments at historical rates. However, the importance of fund investments in financial institutions' investment securities portfolios has greatly increased since the introduction of accommodative monetary policy. It is difficult to envision these institutions returning to the practice of investing the majority of their funds in government bonds, and we think they will continue to focus on security investments, including outsourcing to AMCs.

1) Here we define fund inflows as purchases less sales and redemptions.
2) Trusts and life insurers' share of this total only includes assets managed on behalf of pension fund clients. Life insurers' portion only includes special accounts and not general-account assets with guaranteed returns such as fixed insurance and fixed annuities.

CHAPTER 2

Current state of asset management business

1 Current state of asset management business

This chapter surveys the business environment for firms specializing in investment trust and/or investment advisory services (hereafter asset management companies or AMCs) using proprietary survey results and other data.

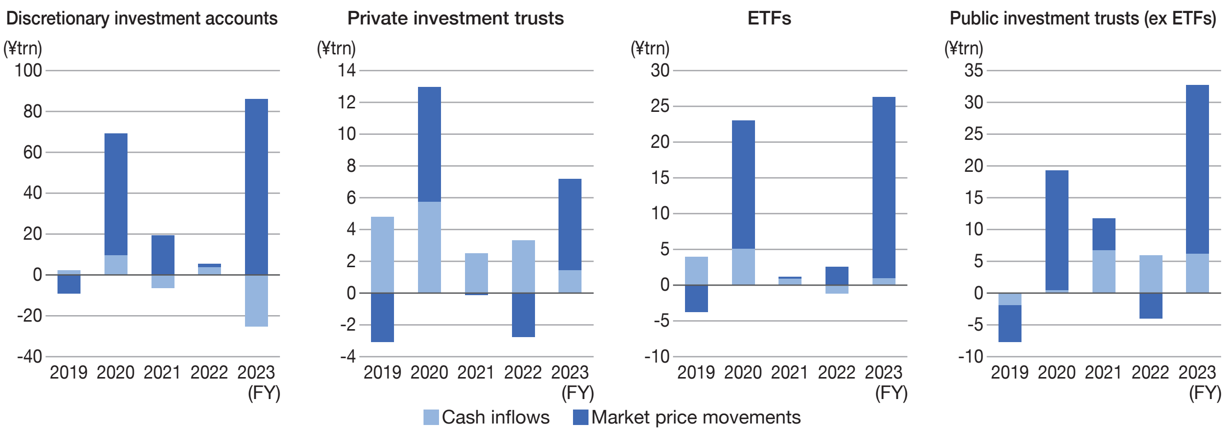
Operating income rises to new all-time high on sharp increase in AUM

In FY2023, AUM at AMCs increased in response to the weak yen and the rising market value of foreign and domestic equities. Exhibit 3 analyzes the components of AUM growth at AMCs over the last five years. AUM in discretionary investment products, the main buyers of which are public and corporate pension funds, rose ¥61trn from ¥377trn in the previous fiscal year. We estimate that market price fluctuations lifted assets by ¥86trn, while sales led to at least ¥25trn in net outflows. The outflows were driven mostly by the rebalancing needs of public pensions and other investors. We suspect they sold investments in foreign bonds and both foreign and domestic equities and used the proceeds to buy domestic bonds on their own.

AUM in private investment trusts, which are intended mainly for financial institutions, also increased by more than ¥7trn. Just under ¥6trn of this figure was due to fluctuations in market value, with net fund inflows amounting to a little less than ¥2trn. Net inflows to private investment trusts typically exceeded ¥5trn in the years up to FY2020 but have declined since then.

The outstanding balance of ETFs, which the Bank of Japan owns more than 80% of, grew more than ¥26trn in the last year. Most of this increase was due to an increase in market value, with net fund inflows

Exhibit 3. Components of AUM growth, FY2019–2023



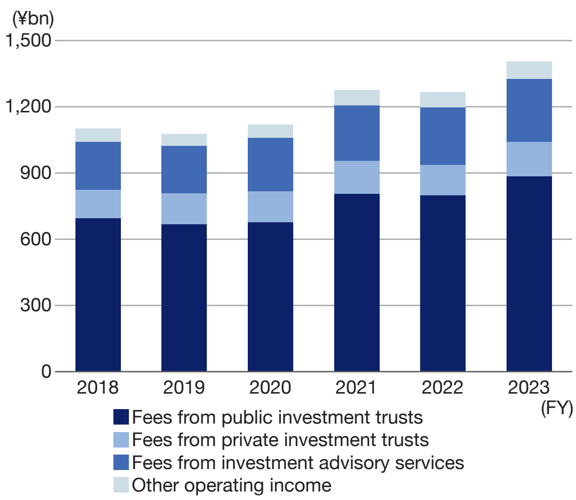
Notes: (1) Based on an analysis of AUM at AMCs. (2) Components for discretionary investment accounts exclude fund inflows resulting from transfer of asset management functions within major financial groups. (3) Figures for private investment trusts, ETFs, and public equity investment trusts (ex ETFs) treat distributions as fund outflows.
Source: NRI, based on data from JITA, JIAA, and NRI Fundmark

amounting to less than ¥1trn. The BOJ had been buying as much as ¥6trn in ETFs per year under its accommodative monetary policy, but it discontinued new purchases in March 2024, so we should not expect future fund inflows of the kind seen up to FY2020. Incidentally, ETFs not purchased by the central bank have experienced net fund inflows for 12 consecutive years in response to steady growth in holdings by banks and other financial institutions. The ban on actively managed ETFs was lifted in September 2023, and many AMCs view this as a source of potential growth.

Public investment trusts, whose main customers are retail investors, have experienced the largest fund inflows of any of the four product categories in recent years, posting annual inflows of around ¥6trn for the last three years. These inflows combined with an increase in market value of more than ¥26trn to produce a ¥33trn increase in outstanding assets in FY2023. In FY2024, fund inflows alone could reach ¥15trn as a result of the new NISA program launched in January.

Operating income at AMCs rose to all-time highs on AUM growth in all categories (Exhibit 4). Operating income climbed to an all-time high of ¥1.41trn,

Exhibit 4. **Operating income at AMCs**



Note: Data from most recent preceding fiscal year were used for companies whose accounting years do not end in March.
Source: NRI, based on financial disclosure provided by regular members of JITA and financial statements of public investment trusts (EDINET)

beating the previous record, set in FY2021, by more than 10%. In FY2022 and FY2023, operating income from the investment advisory and private investment trust businesses increased roughly in line with AUM, while income from the public investment trust business grew more slowly (10% over the two-year period) than AUM, which increased 22%. Average management fees on all public investment trusts fell sharply due to (1) an increase in the percentage of AUM invested in passive funds with low fees and (2) heightened fee competition among passively managed funds. Management fees have been falling throughout the investment management business since the late 2000s, with an especially pronounced decline in fees for public investment trusts.

A look at individual AMCs shows continued revenue growth for the public investment trust business, especially at US management firms. This is due to their foreign equity investments. Among domestic managers, some of the independent firms are reporting higher earnings from their private investment trust and investment advisory businesses as well as their public investment trust businesses. This is due mainly to their investments in domestic equities. In general, we are seeing growth in management fees at foreign and independent management companies. This indicates that even managers without a strong domestic marketing platform can grow their earnings in the current environment by leveraging financial institutions' "open architecture" approach to the investment trusts they handle.

2 Outlook for asset management business

Each August, NRI conducts a survey targeting the management of AMCs (Survey of Asset Management Companies' Management Priorities[3]) to learn how the industry is doing and what the consensus outlook is. The remainder of this section looks at how AMCs view the near-term business environment based on their responses to the survey.

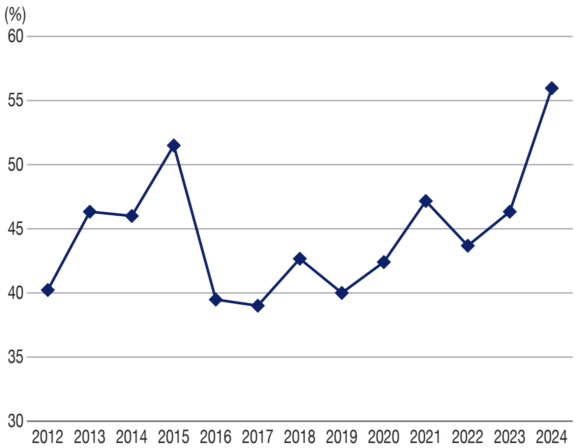
Medium-term business outlook continues to improve

We begin by looking at the medium-term business outlook for the asset management industry. Exhibit 5 shows trends in the percentage of survey respondents forecasting cumulative revenue growth of at least 50% over the next five years. This index has been trending higher since 2019 but increased a full 10ppt to 56% this year. Both AUM and management revenues exceeded the figures for 2015, which also topped the pre-Lehman peak.

The medium-term business conditions index was higher on the year for all three segments (Exhibit 6), with an especially large gain for the retail segment. In addition to the acceleration of fund inflows to investment trusts since the launch of the new NISA program as noted above, increased understanding of the need for individuals to make regular, long-term, diversified investments has fueled expectations of sustained growth at AMCs. The reading for the pension fund segment also surged 10ppt, with an especially large change in outlook observed at domestic management firms. Over the past few years, almost no domestic management firms expected pension fund revenues to grow by 50% over the next five years, but in the latest survey 20% of these firms fell into this category. Starting in the second half of FY2024, public pension funds will review their basic portfolios as a result of the financial verification process. We also expect concrete efforts by both corporate pensions and public pensions to develop more sophisticated asset management strategies in line with the government's plans to transform Japan into an "asset management nation." All of these developments are helping to fuel higher AMC expectations of the pension business.

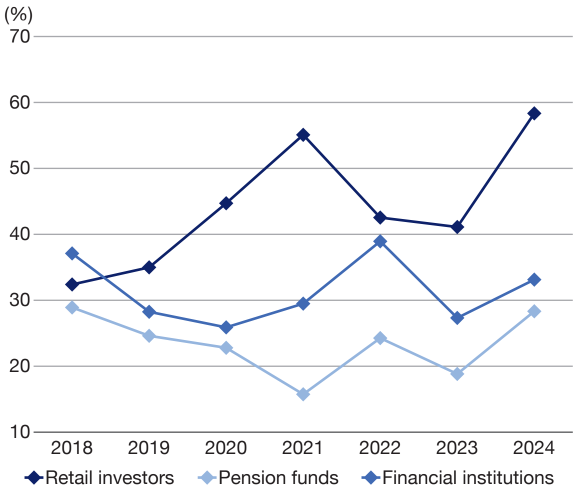
Exhibit 7 shows the medium-term outlook for fund inflows into the investment strategies offered by

Exhibit 5. **Medium-term business conditions index for asset management business**



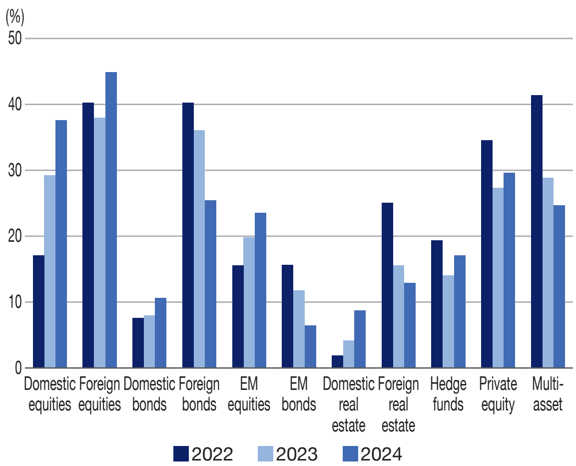
Note: Business conditions index defined as percentage of companies forecasting revenue growth of at least 50% over next five years.
Source: NRI, *Survey of Asset Management Companies' Management Priorities*

Exhibit 6. **Medium-term business conditions index, by segment**



Source: NRI, *Survey of Asset Management Companies' Management Priorities*

Exhibit 7. **Percentage of survey respondents forecasting at least 50% AUM growth from cash inflows over next five years (by asset class)**



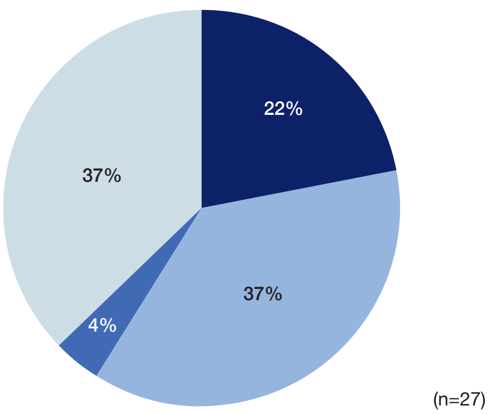
Source: NRI, *Survey of Asset Management Companies' Management Priorities* management firms. A growing number of firms now anticipate medium-term growth in fund inflows to equity strategies, and particularly to domestic and emerging market (EM) equities. Fewer companies expect higher inflows to bond, multi-asset, or foreign real estate strategies[4).

Strong interest in actively managed ETFs

This year's survey asked respondents whether they planned to enter the active ETF business and how they were addressing the issue of product governance, as both of these topics could have a critical impact on AMCs in the future.

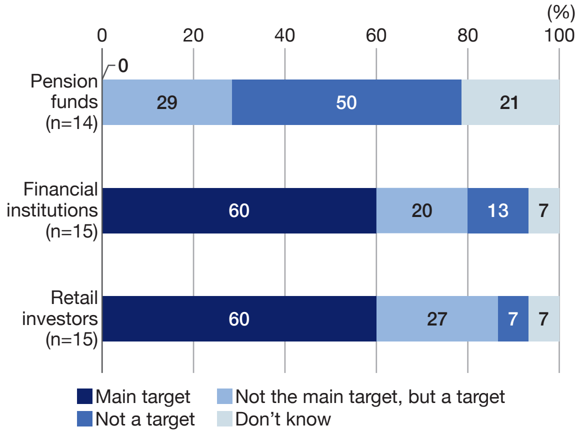
Exhibit 8 illustrates the responses from AMCs managing at least ¥1trn in assets when asked about their plans to offer domestically listed, actively managed ETFs (16 domestic firms and 11 foreign companies replied, for a total of 27). Ten firms, or 37% of the total, said they were "considering or plan to consider" doing so. When they are combined with the six firms (22%) that had already introduced such products, nearly 60% of AMCs expressed interest in active ETFs. Three of the companies that were "considering or planned to consider" the introduced of such products were foreign firms. One said that

Exhibit 8. **Plans to introduce domestic listed active ETFs (at 27 firms with AUM of at least ¥1trn)**



Source: NRI, *Survey of Asset Management Companies' Management Priorities*

Exhibit 9. **Intended buyers of active ETFs (at 15 firms with AUM of at least ¥1trn that had already introduced active ETFs or were either considering or planned to consider introducing them)**



Source: NRI, *Survey of Asset Management Companies' Management Priorities*

the decision "will hinge on whether the criteria for derivatives are relaxed to global levels." Both the disclosure requirements and the listing criteria concerning the use of derivatives for active ETFs are currently being reviewed. Depending on the outcome, we could see many more actively managed ETFs introduced.

The survey also asked participants what kinds of investors they expected to target when introducing active ETFs (Exhibit 9). Nearly 90% said they would target retail investors ("main target" + "not the main target, but a target"), and 80% said they planned to target financial institutions. At present, AMCs offer public investment trusts to retail investors and private investment trusts to financial institutions, but both are sold mostly through sales companies. As financial literacy improves and the institutional role of fund investment continues to change, ETFs that unbundle the sales company function could become an important channel for providing active funds.

Evolving product governance

In recent years, AMCs have been actively trying to enhance product governance to provide products that are in the best interests of customers. Below we provide an overview of existing initiatives along with

Exhibit 10. **Product governance measures that AMCs focused on or planned to focus on (up to three)**

Note: Data from AMCs managing public investment trusts.
Source: NRI, *Survey of Asset Management Companies' Management Priorities*

the outlook based on the findings of the AMC survey.

Exhibit 10 illustrates responses to a question asking AMCs that manage public investment trusts about initiatives to improve product governance that they had either focused on in the past year or were planning to focus on in the coming year.

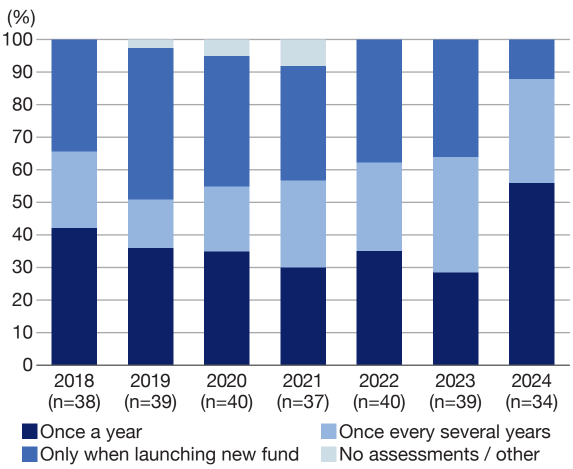
Of the measures undertaken during the past year, many companies said they had focused on policies aimed at "improving information sharing between investment, risk management, and product divisions," "increasing senior managers' involvement with product governance," and "incorporating the views of outside directors."

Following progress in such initiatives, a growing number of companies have opted to carry out periodic inspections of individual funds. Exhibit 11 shows the frequency with which AMCs assess the reasonableness of fees charged by funds. In the six years from 2018 to last year, the percentage of companies that did this "only when launching a new fund" was just under 40% on average, but fell to about 10% in this year's survey. Until last year, only about one third of companies said they looked at fees "every year," but this year more than half responded in this way.

Turning back to Exhibit 10, a look at the measures that companies plan to focus on in the coming year shows that they were far more likely to have plans to "identify intended customer attributes appropriate for individual products and provide information to sales firms" or "verify whether intended customer attributes are consistent with attributes of actual purchasers based on sales firm data" within the next year than to have actually done so within the past year, indicating this is a key target for many firms.

A report released this July by the Financial System Council's Working Group on Capital Market

Exhibit 11. **How frequently is reasonableness of management fees at individual funds assessed?**



Note: Data from AMCs managing public investment trusts.
Source: NRI, *Survey of Asset Management Companies' Management Priorities*

Regulations proposed adding supplementary rules to the Principles of Fiduciary Duty to encourage better product governance at AMCs and other originators of financial products. This was revised in September. The two measures noted above concerning intended customers are required under these supplementary rules.

The important thing here is how to efficiently encourage the sharing of information between companies originating financial products and companies selling them. The Japan Investment Trusts Association (JITA) is currently considering a framework for information exchange throughout the industry, and AMCs will need to respond to these developments going forward.

Taking one more look at Exhibit 10, we see that a certain percentage of companies said they had focused on (or intended to focus on) “investment organization disclosure” or “product governance disclosure.” These responses were more common at relatively large AMCs with outstanding public investment trusts of at least ¥500bn.

One notable development in this area is that some firms are now voluntarily disclosing the test results showing whether their funds are providing value to customers by comparing investment performance after fees and expense ratios with other firms. Such initiatives are being pursued by Nomura Asset Management, Mitsubishi UFJ Asset Management, and Resona Asset Management. The reports also indicate what sorts of corrective measures are being taken at funds that were determined not to be providing adequate value.

By disclosing such information, AMCs can demonstrate to investors that they are exercising rigorous quality control over their funds. In addition, allowing investors to see their own fund assessments provides an incentive to steadily improve products and enhance the value being offered. Over the long term, it is hoped that this will boost investor trust in the quality of the products being offered.

3) We have conducted this survey every year since FY2007, most recently in August 2024. Fifty-two companies (32 domestic and 20 foreign) chose to participate in the latest edition, and together they represent 72% of all invested assets.

4) See Chapter 3-(4) for a detailed discussion of demand for individual products.

CHAPTER 3

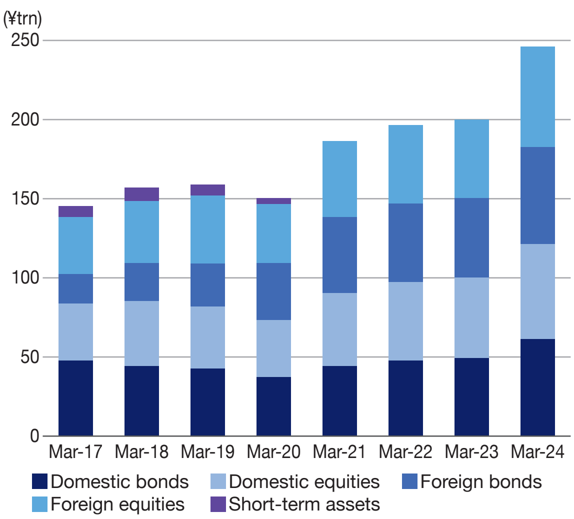
Market trends and product strategies by client segment

1 Pension funds need to improve investment capabilities

Japanese pension plans' reserves at the end of FY2023 (March 2024) were ¥472trn, up ¥74trn YoY (19%) on the weak yen and strong gains by domestic and foreign equities. They have now risen for four straight years starting in FY2020.

AUM at the Government Pension Investment Fund (GPIF), which is responsible for investing the reserves of Japan's national pension fund and the employee pension fund assets of private-sector employees, grew ¥46trn YoY to ¥246trn (Exhibit 12). Returns on domestic equities and foreign equities both exceeded 40%, and the decline in the yen meant that JPY returns on foreign bonds exceeded 15% as overseas rates rose. The overall return of 22.7% was second only to that of FY2020. As the GPIF's basic portfolio has roughly equal allocations to domestic bonds, foreign bonds, domestic equities, and foreign equities, there was a rebalancing between domestic bonds and the other asset categories. Its holdings of alternative assets increased ¥860bn YoY to about ¥3.7trn in FY2023 due to further growth in contributions and the impact of the weak yen. Alternative assets accounted for just 1.46% of total reserves vs. a maximum allocation of 5%, and the wide gap between these two figures points to the likelihood of steady growth in this category. Management fees rose ¥16.8bn YoY to ¥47.0bn as AUM increased and some active managers exceeded their target excess return. As a result, the fee ratio rose to 2.1bp of average outstanding assets from 1.5bp in the previous fiscal year. Public pensions underwent the financial verification in FY2024. The asset allocation of public pensions' basic portfolios will be altered in line with the new required return. Since this change will take effect starting in FY2025, we expect concrete new selections of asset managers will be made in FY2024 H2 and beyond reflecting the change to the basic portfolio.

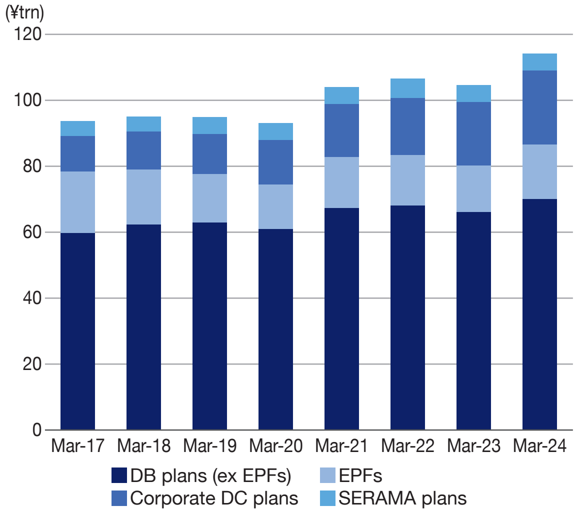
Exhibit 12. GPIF AUM and asset allocation



Source: NRI, based on GPIF annual reports

Corporate pension assets totaled ¥114trn at end-March 2024, up some ¥10trn, or 9.9%, over the previous year (Exhibit 13). DB pension plan and Employees' Pension Fund (EPF) assets increased by ¥4trn (6.5%) and ¥2trn (11.2%) YoY, respectively, marking the highest rate of AUM growth in three years. Although the number of participants in both plans fell 90,000 to 9.15mn during the year, investment revenues increased almost 10%. More companies reported reserve ratios in excess of

Exhibit 13. **Corporate pension AUM**



Note: EPFs: Employee Pension Funds; SERAMA: Smaller Enterprise Retirement Allowance Mutual Aid.
Source: NRI, based on data from Trust Companies Association of Japan and Organization for Workers' Retirement Allowance Mutual Aid

100% due to the growth in pension fund reserves and reduced projected benefit obligations, a result of higher interest rates. Consequently, we think many of these plans are not actively assuming more risk via asset allocation and are instead trying to meet performance targets by adopting specific investment strategies within each asset class.

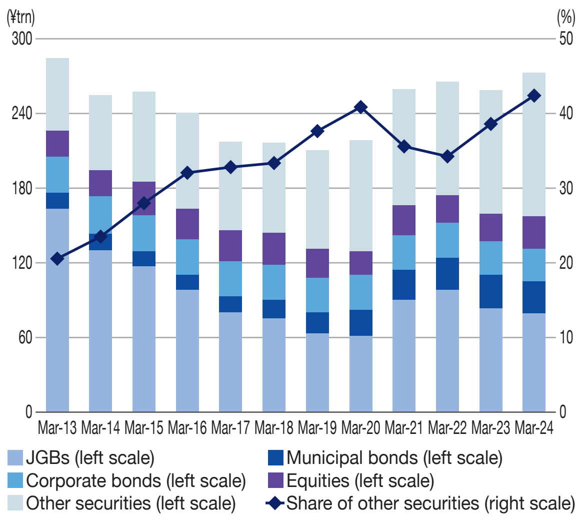
Corporate pension plans and other asset owners are trying to enhance governance and organizational structures as the government seeks to transform Japan into an "asset management nation." In the medium term, we expect larger corporate pension plans will put in place such structures and that smaller plans will consider mergers with larger ones.

AUM in corporate DC plans was up ¥4trn, or 21%, to ¥23trn at the end of FY2023 as foreign and domestic equities posted high returns and investment trusts rose to 60% as a percentage of total plan assets. The number of participants in corporate DC plans is currently growing by 3% a year, and average contributions per person are also increasing on an annual basis. We therefore project these plans will see continued growth in fund inflows, which amounted to ¥920bn in FY2022. Between now and the end of 2024, the authorities are considering revamping the upper limit on contributions, which currently stands at ¥55,000 a month for employees of companies without DB plans. If the limit is raised, we expect to see a further acceleration of fund inflows to DC plans.

2 Fund investments by financial institutions matured during QQE era

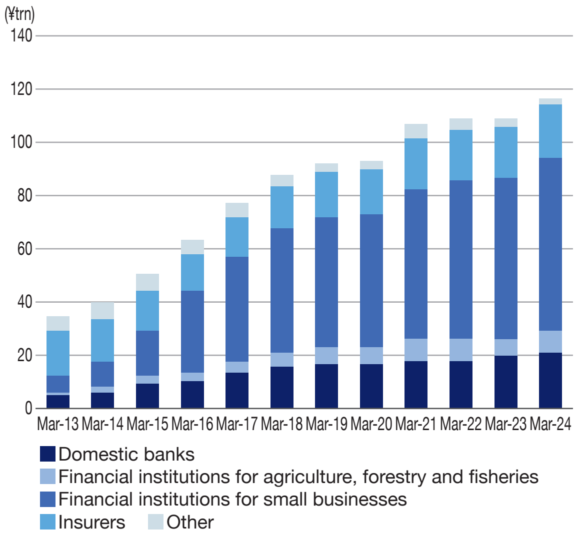
Japanese banks held ¥273trn in investment securities at the end of March 2024 (Exhibit 14). This figure peaked at ¥285trn in March 2013 before falling to ¥210trn in March 2019 as quantitative and qualitative easing (QQE), which was launched in April 2013, led banks to steadily reduce their holdings of JGBs. This downward trend then reversed, with investment securities holdings rising back to near-peak levels. Contributing factors included JGB purchases in response to increased debt issuance during the pandemic, an increase in holdings of "other securities" (the funds and foreign bonds that were viewed as a likely replacement for JGBs under QQE), and an increase in unrealized gains on foreign bonds due to the yen's decline. Funds remain an important component of financial institutions' securities investments. At the end of March 2024, holdings of other securities at Japanese banks represented 42.4% of all outstanding investments in securities, the

Exhibit 14. **Domestic banks' investment securities holdings by asset type**



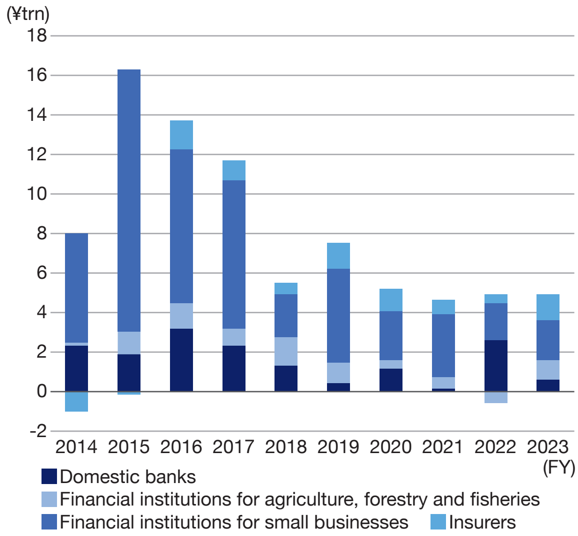
Source: NRI, based on Japan Bankers Association, *"Financial Statements of All Banks"*

Exhibit 15. **Investment fund balances by financial subsector**



Source: NRI, based on JITA data and Bank of Japan, *"Flow of Funds Accounts"*

Exhibit 16. **Fund inflows and outflows by financial subsector**



Source: NRI, based on Bank of Japan, *"Flow of Funds Accounts"*

highest percentage in recent history.

Outstanding investments in funds at domestic banks and other financial institutions totaled ¥116.7trn at the end of March 2024 (Exhibit 15). By financial subsector, financial institutions for small businesses (which include Japan Post Bank) held ¥64.7trn, domestic banks ¥20.9trn, insurance companies ¥20.7trn, financial institutions for agriculture, forestry and fisheries ¥8.1trn, and other institutions ¥2.2trn. All of these figures were up only modestly from the previous year, and the rate of growth slowed.

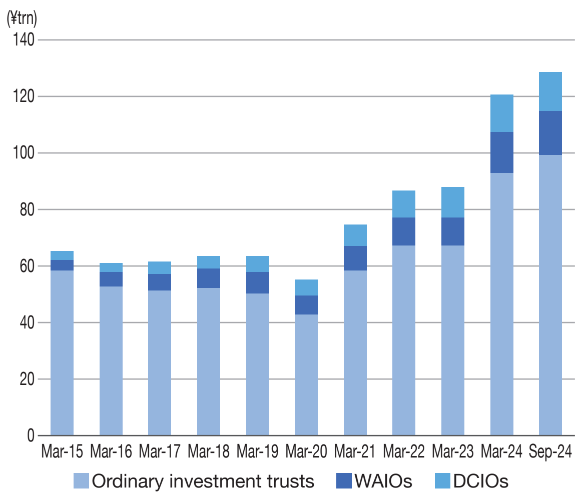
Investment funds are still experiencing net inflows of several trillion yen a year, although that amount is down substantially from the QQE era (Exhibit 16). Inflows in FY2023 totaled ¥4.9trn, with financial institutions for small businesses accounting for ¥1.8trn, insurance companies for ¥1.4trn, financial institutions for agriculture, forestry and fisheries for ¥1.0trn, and domestic banks for ¥0.6trn. As the BOJ proceeds to normalize monetary policy, we do not expect fund investments to continue growing at the pace they did during the QQE era, but we think financial institutions that have become more adept security investors will continue to use funds in their portfolios.

3 Retail business

Net fund inflows continue for equity investment trusts

AUM in public open-end equity investment trusts ex ETFs ("equity investment trusts" below) totaled ¥120.8trn at end-March 2024 (Exhibit 17), up ¥32.6trn on the year. The growth was attributable to ¥6.2trn in fund inflows coupled with a return of more than 30% on all equity investment trusts. The Jan–

Exhibit 17. **Public open-ended equity investment trust balances (ex ETFs)**

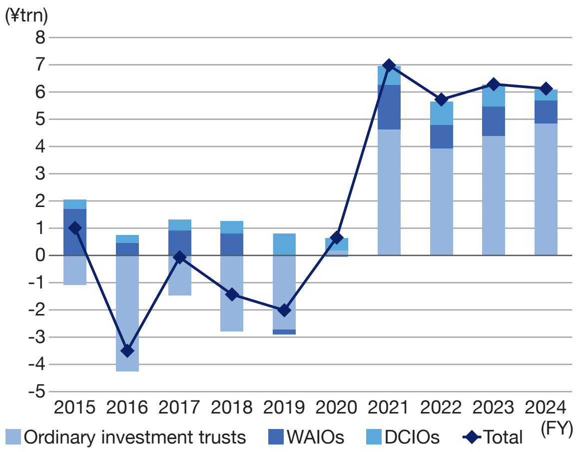


Note: WAIO = wrap account investment only; DCIO = DC investment only.
Source: NRI

Mar quarter alone saw inflows of about ¥3trn as the new NISA program was launched[5]. Fund inflows have continued in FY2024 despite the heavy market volatility sparked by the Bank of Japan's decision to raise the short-term policy rate in August 2024, and by the end of September outstanding assets stood at ¥128.7trn. All three sales channels for equity investment trusts—DC pension plans, fund wrap accounts, and regular channels—have seen continued net inflows (Exhibit 18). Below we examine the outlook for equity investment trust fund inflows and outflows by sales channel.

Looking first at DC pension plans, most of the investment trusts offered through these plans are available exclusively via this channel and are referred to below as DCIO (DC investment only) investment trusts. DCIO funds have enjoyed steady inflows. Because DC plan participants make regular monthly contributions and typically have a long-term investment horizon, they tend not to make changes to their portfolios in response to short-term developments. Additionally, DC plans are still in the adoption phase of their life cycle. With DC plan participation likely to keep growing, we anticipate further increases in total contributions. Corporate and individual DC plans in aggregate have been gaining new participants at a rate of 700,000 per annum in

Exhibit 18. Fund inflows and outflows to public open-ended equity investment trusts (ex ETFs)



Notes: (1) WAIO = wrap account investment only; DCIO = DC investment only. (2) Fund distributions are treated as outflows. Figures for FY 2024 (ending March 2025) are through end-August (not annualized).
Source: NRI

recent years. As a result, DCIO funds saw net cash inflows amounting to ¥0.8trn in the year ending March 2024. In December 2024, the upper limit on monthly contributions to individual DC pension plans for public-sector employees will be raised to ¥20,000 from ¥12,000. In addition, the government discussed reforms to corporate and individual DC plans in the "Grand Design and Action Plan for a New Form of Capitalism" (2024 Revised Version) that was approved by the cabinet in June 2024. With regard to the corporate plans, the government is considering urging DC plans to review the default products and enhancing visibility to facilitate comparisons with other firms. For individual DC pensions, there are plans to consider raising the age limit for participants and raising the maximum contribution limit to encourage wealth formation. Given these changes, we are confident that DCIO funds will continue to see increased fund inflows and accelerated growth in AUM.

Turning next to fund wrap accounts, most of the investment trusts offered are available only through this channel and are known as WAIO (wrap account investment only) investment trusts. WAIO funds have experienced net inflows every year since FY2015 (except for FY2019 and FY2020) and saw net inflows of ¥1.1trn in FY2023. Fund inflows have picked up further in FY2024, and if they continue at the current pace, we estimate they will rise to a record ¥2.1trn for the full fiscal year, which ends in March 2025. A major factor this year is that leading securities firms and banks are selling more of these funds to high-net-worth customers. This has led to a growing number of new accounts funded with ¥10mn or more, and the average AUM per account has increased about 20% over last year.

In addition, many banks and AMCs have begun rolling out fund wrap services to regional banks and smaller securities companies, and this channel is expected to see gradual growth in both AUM and the total number of accounts. Net inflows to investment trusts via wrap accounts will likely continue as a result.

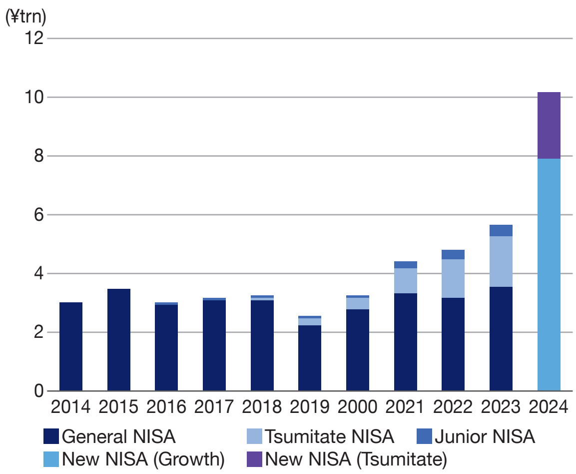
The third ("regular") sales channel, which consists of banks and brokerages selling investment trusts at their branches and online, is probably the most readily associated with the investment trust business in the public mind. We refer to investment trusts offered through this channel as ordinary investment trusts. Ordinary investment trusts collectively experienced net outflows for nine consecutive years through FY2019 before attracting a small net inflow in FY2020. Since then, they have reported net inflows of several trillion yen per annum. Inflows have picked up further with the launch of the new NISA investment account program in January 2024, and these investment trusts are now seeing net inflows of almost a trillion yen each month. If this continues, we estimate full-year inflows for FY2024 could rise some 160% over the year before to ¥11.6trn. We expect fund inflows to continue inasmuch as (1) the market turmoil seen in August this year did not result in a reversal of healthy fund inflows and (2) whereas fund inflows stagnated in the first month of the former NISA program in 2014 and also in the first three months after the launch of the Tsumitate NISA in 2018, they have continued at a healthy pace in 2024.

Purchases under new NISA program up 80% YoY as of end-June 2024

Below we provide a more detailed analysis of the impact of the new NISA program on the investment trusts market. Key changes to the new NISA program launched in January 2024 include an increase in the limit on tax-free contributions and a decision to make the program permanent. The new system offers two types of accounts: Tsumitate accounts, which are designed to encourage regular, long-term, diversified investment; and Growth accounts, which enable participants to invest in listed stocks as well. The upper limits on annual investments are ¥1.2mn and ¥2.4mn, respectively. Lifetime tax-free contributions are capped at ¥18mn, with the Growth component limited to ¥12mn. As of end-June 2024, participants in the new program had purchased ¥2.2trn in financial products in Tsumitate accounts and ¥7.9trn in Growth accounts, for a total of ¥10.1trn. In part because of the expansion of the tax-free limit, purchases under the NISA program at the end of June had already exceeded the full-year total for 2023 by 80% (Exhibit 19).

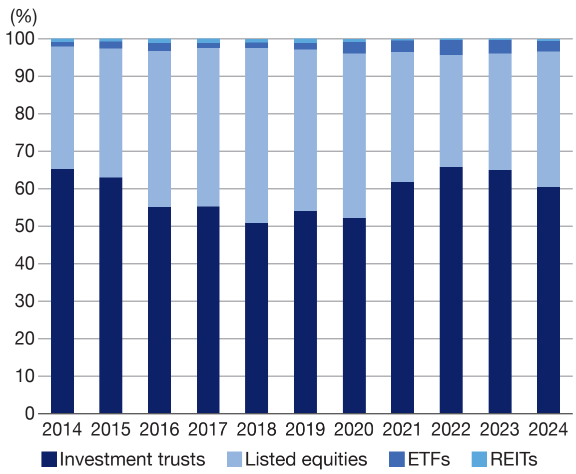
A breakdown of purchases in both Tsumitate and Growth accounts by product category shows investment trusts accounting for 60% of all assets acquired, listed equities for 36%, ETFs for 2.9%, and REITs for 0.5%. This has not changed much since 2014, with investment trusts consistently ranked first

Exhibit 19. **Securities purchased in NISA accounts**



Note: As of end-June 2024.
Source: NRI, based on FSA data

Exhibit 20. **Share of securities purchased in NISA accounts, by product category**



Note: As of end-June 2024.
Source: NRI, based on FSA data

and accounting for more than 50% of all purchases (Exhibit 20).

Fund inflows concentrated in NISA-eligible funds

Tsumitate and Growth accounts in the new NISA program have different fund eligibility requirements. In both cases, investment trusts must have a trust period of 20 years or more, must not offer monthly distributions, and must not use derivatives. In addition, funds for purchase in Tsumitate accounts must not charge sales commissions (i.e., they must be no-load funds), and trust fees must not exceed a certain threshold.

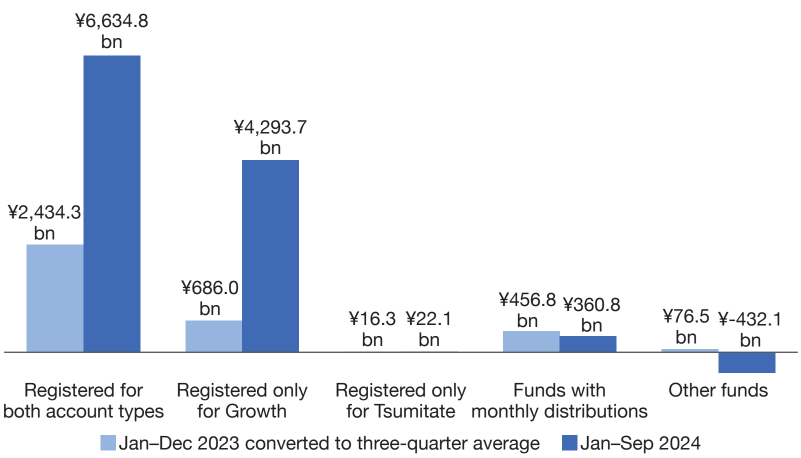
As of October 2024, there were 291 investment trusts eligible for purchase in Tsumitate accounts, 1,992 trusts eligible for purchase in Growth accounts, and 272 eligible for both. Although the Tsumitate accounts have stricter eligibility criteria, the need for registration with the FSA and the Japan Investment Trusts Association means that products eligible for purchase in Tsumitate accounts do not automatically qualify for purchase in Growth accounts.

We looked at net fund inflows to investment trusts registered only for Tsumitate accounts, those registered for both account types, those registered only for Growth accounts, those with monthly distributions, and other investment trusts[6] (Exhibit 21). Fund inflows to NISA-eligible investment trusts from January to September 2024 were up over the three-quarter average for 2023, while trusts with monthly distributions and other investment trusts experienced lower or negative fund inflows. Investment trusts registered for both account types saw inflows amounting to ¥6.6trn, up 170% from last year. Investment trusts registered only for Growth accounts saw fund inflows of ¥4.3trn, up 530% over 2023. Investment trusts registered only for Tsumitate accounts had relatively few fund inflows and were up just 40% on the year, in part because there were relatively few such funds. Meanwhile, investment trusts with monthly distributions—which are not eligible for the NISA program—saw fund inflows of only ¥360.8bn[7], and other investment trusts experienced fund outflows amounting to ¥432.1bn. It is clear that fund inflows are concentrated in NISA-eligible funds.

Actively managed NISA-eligible funds also see robust inflows

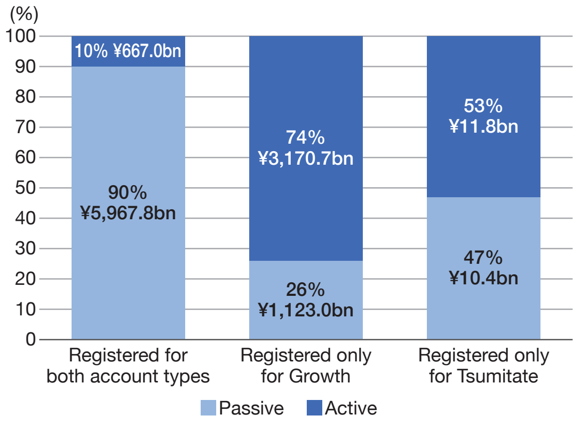
There were substantial inflows to active as well as passively managed NISA-eligible funds. Although passive funds accounted for 60% of net fund inflows to investment trusts between January and September 2024, that percentage varied greatly depending on the type of account (Exhibit 22). Fully 90% of inflows to investment trusts eligible for purchase in both types of account are to passive funds tracking indices like the MSCI ACWI and the S&P 500. In contrast, more than 70% of inflows to funds registered only for Growth

Exhibit 21. **Net fund inflows and outflows to open-ended equity investment trusts (ex ETFs and DCIO and WAIO funds)**



Note: Outflows due to distributions have been ignored. Net fund inflows include purchases made outside NISA program. Bars in graph vary in scale.
Source: NRI, based on data from FSA, JITA, and NRI Fundmark

Exhibit 22. **Net fund inflows to NISA-eligible funds by management style (Jan-Sep 2024)**



Note: Outflows due to distributions have been ignored. Net fund inflows include purchases made outside NISA program.
Source: NRI, based on data from FSA, JITA, and NRI Fundmark

accounts are to actively managed funds, many of which invest in Indian stocks or US growth stocks, including semiconductor-related firms. More than 50% of inflows to funds registered only for Tsumitate accounts were also to actively managed funds.

Finally, although our analysis has focused on NISA-eligible funds, it should be noted that not all fund inflows are for NISA accounts. NISA purchases accounted for some 40% of all purchases of NISA-eligible funds between January and June 2024, with the other 60% purchased outside the program. It is quite likely that a product's suitability for stable wealth formation is also one of the key selection criteria for funds purchased outside the NISA program. If so, investment trust sponsors probably need to pay close attention to the NISA eligibility criteria when designing new products.

4 Investment product market trends by investor segment

We have created product opportunity maps for three investor segments (retail, pension funds, and financial institutions) based on data from our latest Survey of Asset Management Companies' Management Priorities, conducted in August and September 2024. The maps show investment products characterized by strong demand (as assessed by AMCs) but limited supply (upper left quadrant) as well as those facing tough competition, with weaker demand and numerous providers (lower right quadrant). Exhibit 23 presents our product opportunity maps for a subset of products.

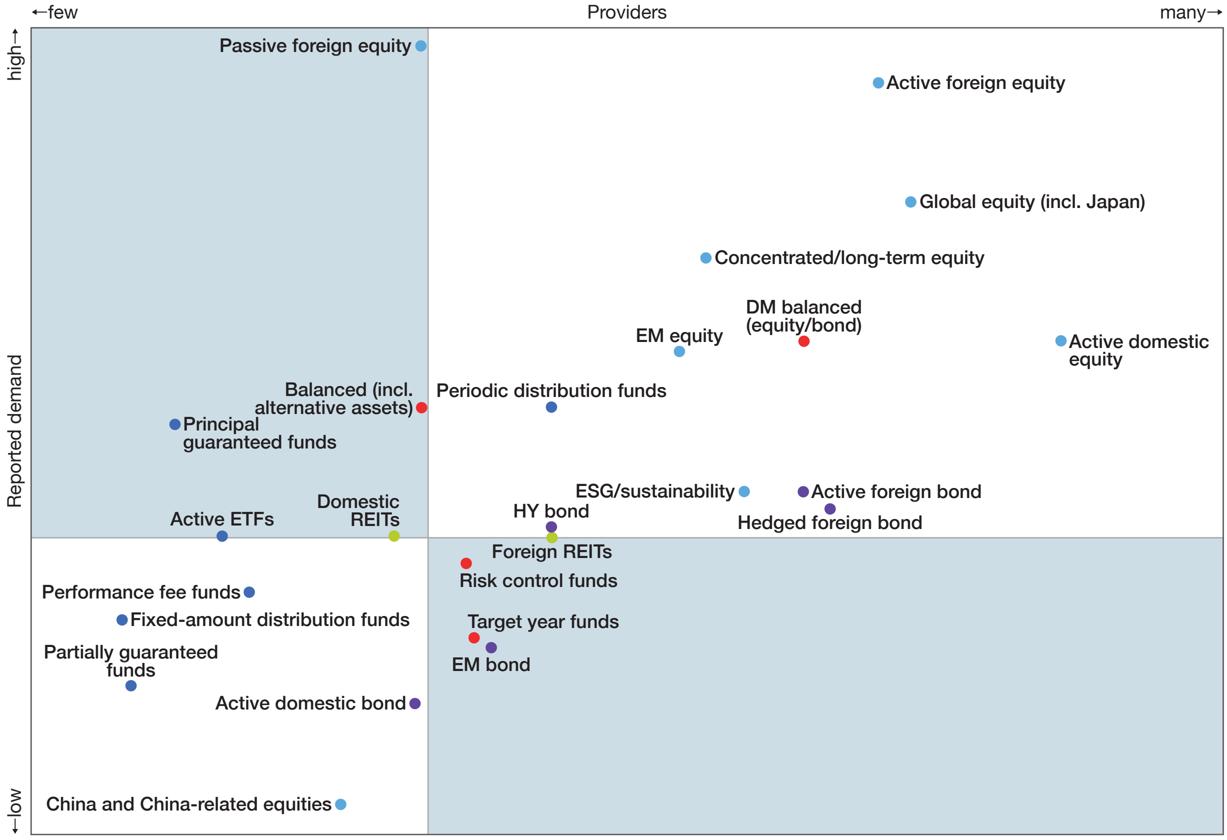
In the retail investor segment (Exhibit 23(a)), foreign equity products continued to garner the highest demand scores. Products ranking high on the demand scale include active and passive foreign equity funds and concentrated equity funds with long-term investment horizons. This result is consistent with actual fund flows into and out of public investment trusts. Within the actively managed foreign equity space, growth funds investing primarily in the technology sector, including Big Tech and US semiconductor-related stocks, saw even larger fund inflows than last year. Among passively managed foreign equity funds, there were continued inflows to passive funds tracking indices like the MSCI ACWI and the S&P 500. Actively managed domestic equity funds and EM equity funds also received high demand scores, although not as high as foreign equity funds. The data showed inflows to funds investing in domestic value and domestic dividend stocks as well as funds focusing on India and other emerging markets. Demand scores for China-related equity funds remained low in this year's survey.

In the bond space, actively managed foreign bond funds received the highest demand scores, followed by those investing in hedged foreign bonds (although scores for both were lower than in 2023). Scores for actively managed domestic bond funds and EM bond funds were both higher this year, albeit still low in absolute terms.

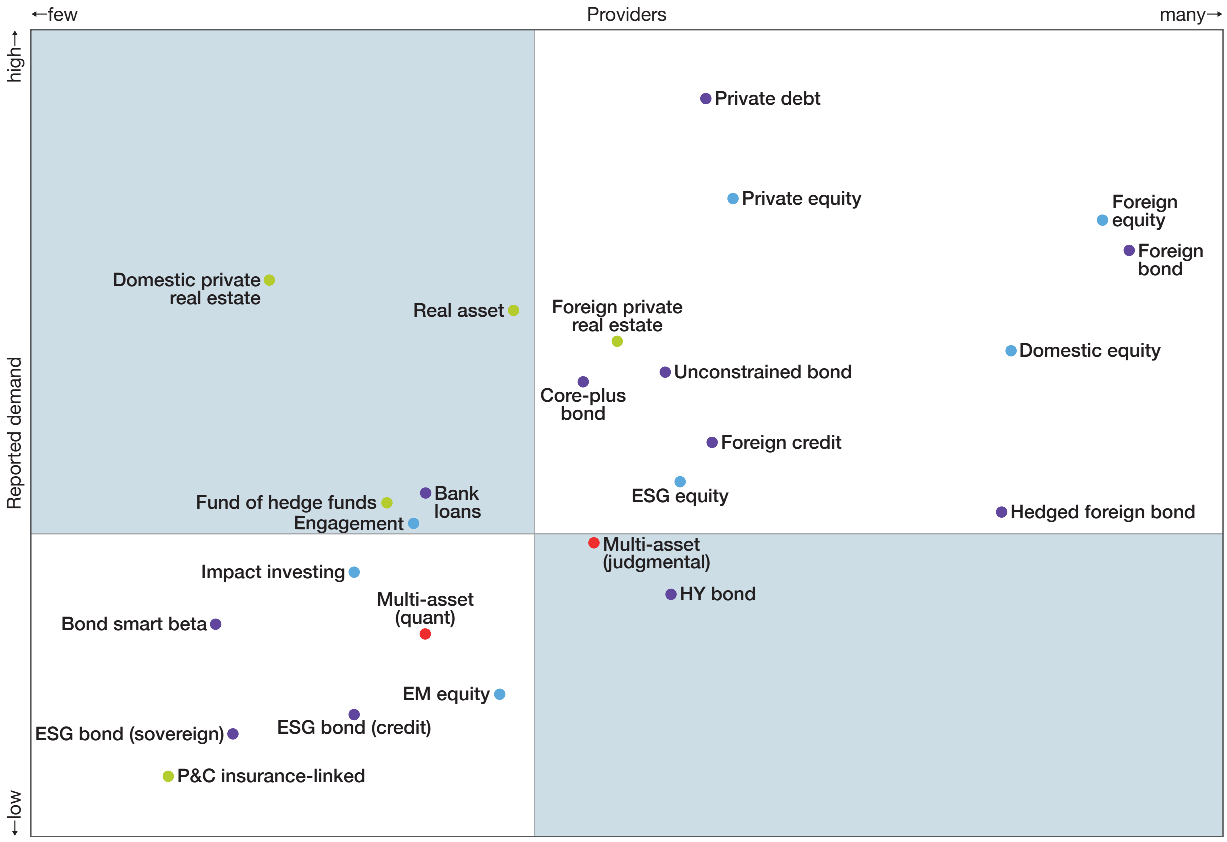
Demand scores for balanced funds holding developed market (DM) equities and bonds and balanced funds holding alternative assets were both higher this year. We attribute this to greater interest from retail investors in response to the new NISA program. Among funds with distinctive features,

Exhibit 23. Product supply/demand maps by customer segment

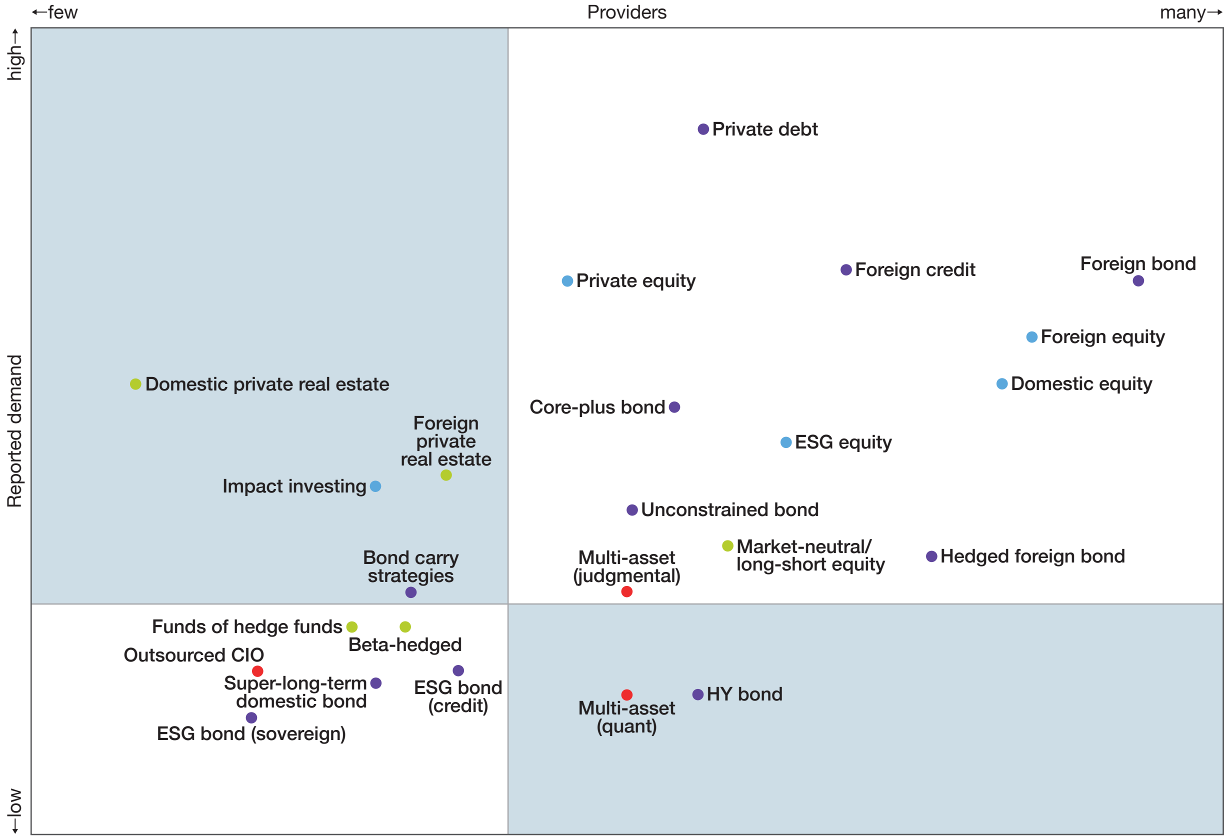
(a) Products for retail investors



(b) Products for pension funds



(c) Products for financial institutions



Note: Vertical axis is indexed and shows strength of demand from customers (based on AMC assessment of demand). Horizontal axis indicates number of AMCs offering each type of product and is indexed by number of providers and not by value.
Source: NRI, based on *Survey of Asset Management Companies' Management Priorities*

periodic distribution funds and principal guaranteed funds ranked high on the demand scale, but there are few providers of the latter.

In the pension fund segment (Exhibit 23(b)), in contrast to the retail segment, scores for the equity and bond categories were mixed. Among equity products, private equity (PE), foreign equity, and domestic equity strategies continued to garner high demand scores, while the score for ESG equity strategies fell sharply, perhaps because of mounting anti-ESG sentiment in the US. The score for impact investment strategies was also lower.

In the bond space, the demand score for private debt increased and was once again highest overall. Scores for foreign and unconstrained bond strategies remained high as well. Meanwhile, the score for high-yield (HY) bond strategies was lower than last year.

The rankings of multi-asset funds are essentially based on perceived demand from corporate pension funds because public pension funds have yet to allocate to these strategies. Compared with 2023, the demand score for judgmental strategies was substantially lower, although they still ranked higher than quant strategies. Among alternative assets, domestic and foreign private real estate (including private REITs), along with real asset strategies, continued to receive high demand scores. Demand for funds-of-hedge-funds, while still low, was up sharply over 2023.

The results for equity and bond strategies were also mixed in the financial institution segment (Exhibit 23(c)). In the bond space, private debt had the highest demand score, followed by foreign credit and foreign bonds, all of which increased over last year. Private debt strategies saw an especially large increase. We think domestic financial institutions have grown more interested in private debt strategies as they seek higher yields and risk diversification in response to rate cuts in the US and Europe.

In the equity space, private equity once again ranked first and was followed by foreign equity and domestic equity, both of which also increased over 2023. Scores fell for ESG and impact investment strategies, although they were still relatively high. There was generally less demand for multi-asset strategies, with judgmental strategies seeing an especially large drop over last year.

5) In terms of fund inflows and outflows, we treat distributions as fund outflows in this section unless otherwise noted.
6) We did not take into account fund outflows due to distributions.
7) Since income distributions amount to about ¥200bn each month, we estimate there would actually be net outflows if distributions were taken into account.

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