

NEXTGEN ESG JAPAN



NextGen ESG Japan

Annual Report 2026

SDG
Impact Japan





Foreword

Dear Reader



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As we reach the midpoint of 2026, the NextGen ESG Japan Strategy stands at a defining moment, one where conviction meets evidence, and where purpose-driven investment has delivered undeniable results.

The performance of the portfolio has been broadly consistent with our original investment thesis. Since inception, our strategy has achieved annualized return of 16.40% (April 2022 ~ May 2026) and Sharpe Ratio of 1.48. The Sharpe Ratio suggests that returns have been generated with a relatively favourable risk-adjusted profile over the period. The combination of robust absolute returns and exceptional risk management validates our core conviction: deep, proprietary analysis of Japanese small and mid-cap companies uncovers genuine value creation opportunities that others overlook, while our rigorous approach to material risk factors protects capital during periods of market volatility.

At SDG Impact Japan, we have remained steadfast in our belief that these small and mid-cap enterprises, representing a significant portion of Japan's listed companies and employing millions across the nation—are the true engines of transformation in the Japanese economy. While others debated the merits of ESG, we focused on identifying emerging leaders who would drive positive change and innovation within this dynamic landscape.

The Japanese financial markets have demonstrated remarkable resilience, with foreign investments surging to new heights. This resurgence reflects more than favourable economic conditions, it underscores a fundamental shift toward responsible investing and the integration of Environmental, Social, and Governance principles into corporate strategies. The Japanese government's proactive policies, such as the Green Transformation initiative, have redefined the investment landscape, ensuring that sustainability is not merely an option but a necessity for long-term business success.

Extracting Investment Value Through Rigorous Analysis

Our experience provides a clear answer: investment value exists within ESG factors, but it is not freely given, it must be extracted through thorough, disciplined investment work. The notion that simply applying ESG screens or selecting companies with high third-party ratings will automatically generate outperformance is fundamentally flawed. Such approaches often rely on backward-looking data, generic metrics, and superficial assessments that fail to capture the true drivers of long-term value creation.

Extracting real investment value requires deep fundamental analysis, proprietary research, and active engagement with management teams. It demands understanding which ESG factors are truly material to a company's competitive position, which governance structures enable or constrain value creation, and which operational practices will prove resilient or vulnerable as markets evolve.

The facts speak clearly through our results: businesses across our portfolio are actively embracing sustainable practices not because of regulatory pressure or public relations concerns, but because these practices enhance operational efficiency, reduce risk, and strengthen competitive positioning. Our engagement work has revealed substantial opportunities that surface-level analysis would miss, from supply chain vulnerabilities that impact margins, to governance weaknesses that constrain strategic agility, to untapped efficiency improvements that expand profitability.

Rigorous ESG integration is not about virtue signaling or compliance exercises, it is about identifying material factors that drive long-term value creation and competitive advantage. The investment value comes not from holding "good" companies, but from recognizing undervalued businesses were addressing specific ESG factors can unlock significant value and then working alongside management to realize that potential.

This is investment work in its truest form: identifying mispriced assets, understanding the catalysts for value creation, and actively partnering with companies to capture that value. The ESG framework simply provides a more comprehensive lens for analysing the full spectrum of risks and opportunities that traditional financial analysis often misses.

Note: Performance data represent historical results and should not be construed as a guarantee of future performance. Sharpe Ratio is calculated using monthly net returns and a risk-free rate of 0%.
Source (performance data): Internal calculations based on the Fund's NAV, net of fees and expenses, from April 2022 through May 2026.

Difference

Our investment strategy is built on a contrarian thesis that has proven remarkably successful: Japanese small and mid-cap companies were fundamentally mispriced, offering exceptional value creation opportunities that the broader market overlooked.

Our approach emphasizes deep fundamental analysis and active engagement with management teams. What makes our approach proprietary is our own equity story analysis which combines strategic ESG factors, and a friendly-activist engagement approach that enables portfolio companies to unlock their full potential. This rigorous methodology has consistently identified companies with strong growth trajectories and sustainable competitive advantages.

Our investment process focuses on material factors that directly impact long-term financial performance. We conduct proprietary analysis on each portfolio company, examining operational efficiency, risk management practices, governance quality, and strategic positioning. We then work alongside management teams to drive measurable improvements—not as external critics, but as committed partners in value creation.

This collaborative approach has delivered tangible results:

- **Disciplined Performance:** Since inception, our strategy has focused on delivering sustainable returns with a favorable Sharpe Ratio, reflecting high-quality risk-adjusted performance. These results underscore our commitment to a structured and disciplined approach, avoiding excessive risk-taking or reliance on market timing.
- **Operational Excellence:** Through active engagement, we have facilitated improvements in operational efficiency, governance structures, and strategic decision-making across our portfolio companies—enhancements that translate directly into stronger financial performance and competitive positioning.
- **Value Creation Through Engagement:** Our deep partnerships with portfolio companies have unlocked value by addressing previously overlooked risks and opportunities, from supply chain optimization to talent retention and market expansion strategies. These efforts strengthen competitive positions, reduce operational and reputational risks, and unlock new opportunities for revenue growth and margin expansion—all of which drive superior long-term returns for our investors.

The Third Path Forward

The investment world has fractured into two camps: ESG believers and ESG critics, each claiming vindication while talking past one another. NextGen ESG Japan was built on the conviction that both sides miss the point.

We chart a third path—one that rejects both blind faith in ESG ratings and cynical dismissal of material sustainability factors. Our approach is grounded in evidence, focused on outcomes, and measured by results that matter to investors and society alike.

This third path recognizes that Japanese small and mid-cap companies are not abstractions in an ideological debate—they are dynamic businesses led by pragmatic management teams navigating real competitive pressures. Their resilience and adaptability, their capacity to evolve business models and embrace long-term thinking, position them to thrive amid complexity while generating superior returns.

Our mission has never wavered: identify and support the future leaders of sustainable business in Japan. As we move through 2026 and beyond, we remain committed to this focused, long-term approach—one that prioritizes tangible actions over rhetoric, measurable improvements over marketing claims, and genuine partnerships over passive ownership.

The third path is not about choosing between purpose and performance. It is about recognizing that rigorous analysis of material factors—whether financial, operational, governance-related, or environmental—leads to better investment decisions and stronger companies.

Every quarterly result reinforces what we have known from the beginning: when investment discipline meets genuine engagement, both investors and society benefit. This is the future of investing—not as ideology, but as evidence.

Outline

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Our mission

NextGen ESG Japan’s mission is to contribute to the global efforts to limit global warming to 1.5°C and shift to a sustainable path for humanity.

This strategy seeks transformational change in the business models of the companies we select. The core element of our philosophy is the belief that ESG factors can directly affect long-term business profitability.

NextGen ESG Japan is an outcome-driven strategy that occupies a distinct position in the global ESG investment universe by combining deep engagement, measurable sustainability targets, and a dedicated focus on small-medium size listed Japanese companies.

The objective of the strategy is to accelerate sustainable transition of businesses as well as to generate long-term capital appreciation by investing in a long-only concentrated equity portfolio of small and mid-cap Japanese companies.



01

Concept & Strategy

In an era where the alignment of investment strategies with environmental, social, and governance (ESG) principles is no longer optional but imperative, NextGen ESG Japan stands at the forefront of impact investing. Our strategy is designed to not only navigate the complexities of the modern financial landscape but to actively contribute to a more sustainable and equitable world.

This section of our annual report delineates the foundational concepts and strategic approaches that underpin our investment philosophy, showcasing our commitment to both financial returns and positive societal impact.

ESG for Return and Impact: Strategic Focus

Our investment philosophy is grounded in the belief that ESG considerations are not only corporate responsibility imperatives but also key drivers of financial performance, when managed properly and linked to core business of the companies. We focus on strategic ESG issues that have a strong link with company’s products and services, corporate strategy, and corporate value, so that our engagements are not only impactful in terms of societal benefits but also contribute to the long term financial sustainability and growth of our portfolio companies. This dual focus on return and impact is central to our strategy, reflecting our commitment to redefining the role of capital in achieving a sustainable future.

Targeting Untapped Potential: Small and Mid-Cap Investments in Japan

Our focus is on small and mid-cap listed equities in Japan, a market brimming with untapped potential and opportunities for significant ESG driven value creation. The choice of this focus area is strategic, informed by our deep understanding of the Japanese market dynamics and the unique opportunities it presents for impact investing. Our strong fundamental analysis, and engagement team, based on the ground in Japan, possesses the expertise and local insights necessary to identify and capitalize on these opportunities, promoting that our investments and engagements are both impactful and profitable.

A Friendly Activist Approach: Deep Dialogues and Dedicated Engagements

At the core of the investment methodology of the strategy is a friendly activist approach. We engage in deep constructive and focused dialogues and dedicated engagements with our portfolio companies, fostering a culture of openness and constructive collaboration. This approach is designed to drive meaningful

change from within, encouraging companies to integrate ESG considerations into their corporate strategies and operational practices. Our concentrated portfolio allows us to maintain a high level of engagement with each company, so that our interventions are tailored, strategic, and effective.

A Commitment to Sustainability

NextGen ESG Japan is aiming to dedicate to achieving clear and measurable sustainability objectives for transparency and accountability in impact investing. Our adherence to the sustainability objectives is a reflection of our core belief in the importance of embedding key material and financially relevant ESG considerations at the heart of our investment strategy.

In conclusion, the strategic approach of NextGen ESG Japan is characterized by a rigorous commitment to prudent portfolio construction, sustainability, strategic focus on high-potential Japanese equities, a collaborative engagement strategy, and a dual focus on financial returns and positive societal impact. Our strategy is uniquely positioned to offer an opportunity to contribute to a sustainable future while achieving strong financial returns. Through our dedicated efforts and strategic engagements, we are not only navigating the complexities of the ESG landscape but also actively contributing to shaping a more sustainable and equitable world.

The Fund currently invests in 25 Japanese companies to create economic Value and impact through active engagement. The 25 companies are screened using a proprietary ESG assessment model and then strategically selected based on a rigorous analysis that integrates both financial and ESG perspectives. Company selection is based on a bottom-up approach, and the portfolio is built with companies from a very broad range of sectors, including manufacturing, consumer products, financials, retail, etc.

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Theory of Change

Theory of Change

The Theory of Change for the NextGen ESG Japan defines how our investment and engagement strategy is designed to create long-term, measurable impact through listed equities, while generating long-term financial returns.

Designed in alignment with the GIIN framework*, it outlines the societal challenges we aim to address—such as decarbonization, human capital development, governance reform, and gender equality—and links them to intended beneficiaries, including portfolio companies and broader society.

It also clarifies how we, as investors, contribute to these changes through active engagement and portfolio design.

This structured framework serves as the foundation for setting non-financial goals and measuring progress across environmental, social, governance, and gender dimensions.

*GIIN Guidance for pursuing impact in listed equities 1 April '23

A The specific problems that the investment strategy will target



- Achieve corporate management that leads to sustainability impact realization
- Promote carbon neutrality (GHG emission reduction) and gender equality initiatives, especially in Japanese companies
- Strengthening human capital management and governance in Japanese companies to achieve this goal.
- Realize environmental and social impact of each issue by strengthening initiatives for other ESG issues of high importance for each investee company.

C How the investor will contribute to that change / How the intended impact will affect portfolio construction and management.

How to Contribute

- Identifying and analyzing key sustainability issues of portfolio companies and communicating them to the portfolio companies
- Engagement with portfolio companies to promote and deepen their efforts to address key sustainability issues
- Engagement for effective disclosure that also leads to best practices for portfolio companies

Portfolio construction and management

- Initial screening based on independent ESG assessment
- Selection of individual stocks, including analysis of performance from an ESG perspective and room for improvement in ESG initiatives
- Identification of ESG issues of high strategic importance and examination of hypotheses for addressing them

B The beneficiaries that would benefit

Short-term

- Reduction of GHGs in society as a whole through reduction of GHGs in portfolio companies and expansion of their contribution to GHG reduction
- Improving the overall wellbeing of portfolio companies through the promotion of gender equality in portfolio companies

Medium- to Long-term

- Accelerate society-wide GHG reductions by making portfolio companies best practices in GHG reduction and mitigation contributions
- Promoting gender equality throughout society by making portfolio companies best practices in gender equality

D The changes that the fund is seeking to achieve / The non financial targets that will play a material role in the selection of equities and ongoing evaluation of performance

Environment

- Improve the temperature trajectory path of each portfolio company to 1.5°C over a 3-5-year investment period.

Social

- Human capital of each portfolio company Improve management performance and disclosure of key social indicators for each company over a 3-5 year investment horizon

Governance

- Improve the quality of governance of each portfolio company and the disclosure of each company's key governance indicators over a 3-5 year investment horizon

Gender

- Gender balance and gender in leadership positions at portfolio companies Improve the gender pay gap over a 3-5 year investment period

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Fund Sustainability KPIs and Progress

Fund Sustainability KPI

As an integral component of our commitment to impact investment, NextGen ESG Japan employs a structured approach to monitoring and enhancing the ESG performance of our portfolio companies. Our framework is built around four sustainability objectives: Environment, Social, Governance, and Gender. Each objective is rigorously assessed through two key performance indicators (KPIs), enabling us to measure progress and drive impactful engagement.

Our approach is proprietary and tailored to the characteristics of our investment universe. We also review our fund KPIs on a regular basis to reflect evolving societal expectations, regulatory developments, and changes in the ESG initiatives undertaken by our portfolio companies. This year, we have incorporated our perspectives on carbon neutrality initiatives (Scope 3) and human capital management, while also strengthening our fund KPI relating to the gender pay gap.

This section details our objectives, KPIs, and the progress we have made, underlining our commitment to not only financial returns but also to making a positive impact on society and the environment. Progress against our KPIs is generally measured relative to the baseline established at the Fund's inception in April 2022. However, assessments of carbon neutrality initiatives (Scope 3) and human capital management commenced this year, while the gender pay gap KPI is measured based on the newly strengthened criteria.



Environment: Commitment to a Sustainable Future

KPI1 : Share of Companies with Carbon Emission Reduction Initiatives (Scope 1+2) / (Scope 3)

We measure the percentage of our portfolio companies disclosing both their current GHG emissions and their reduction targets. At present, our focus also includes companies whose initiatives are limited to addressing Scope 1 and Scope 2 emissions at domestic sites. This year, we have also incorporated our perspective on carbon neutrality initiatives (Scope 3) by assessing the extent to which companies calculate and disclose their material Scope 3 emissions, establish and disclose reduction targets, and develop roadmaps to achieve those targets. This KPI reflects our dedication to supporting our portfolio companies in their journey towards aligning with a 1.5°C pathway.

KPI2 : Portfolio Carbon Emission Intensity (WACI2) (Scope 1+2)

The Weighted Average Carbon Intensity (WACI) for Scope 1 and 2 emissions across our portfolio companies is calculated by dividing annual GHG emissions by annual sales, adjusted for our portfolio inclusion ratio. This metric underscores our commitment to reducing carbon footprint and enhancing transparency in emissions reporting.



Social: Enhancing Human Capital and Addressing Material Social Issues

KPI1: Share of Companies with Disclosed Policy and Management for Sector Material Social Issues

We track the percentage of our portfolio companies that disclose their policies, organizational structure to implement the policies, and actual initiatives to address material social issues pertinent to their business. Comprehensive disclosure is required for all identified critical social issues, emphasizing our focus on social responsibility and impact.

KPI2 : Share of companies that disclose human capital initiatives aligned with business strategy

This year, we introduced a new evaluation criterion focusing on human capital KPIs aligned with corporate strategy. We assess companies that disclose human capital KPIs logically linked to their corporate strategy and value drivers. Where such KPIs are not publicly disclosed for competitive reasons, we evaluate whether our engagement confirms that they are appropriately managed.

This KPI reflects our commitment to recognizing human capital as a key driver of corporate value and supporting our portfolio companies in advancing their human capital management practices.



Governance: Strengthening Corporate Governance

KPI1: Share of Companies that Incorporate Links to Sustainability Topic with Governance Structure

Our focus here is on the percentage of portfolio companies that have integrated sustainability considerations into their governance frameworks, including the establishment of a Sustainability Committee reporting to the Board and reflecting sustainability KPIs in director compensation. This KPI demonstrates our commitment to enhancing governance structures to support sustainability.

KPI2: Share of Companies with More Than 33% of Independent Board Members

We measure the proportion of our portfolio companies where at least one-third of the board comprises independent directors, promoting diversity and independent oversight in governance practices, in accordance with the corporate governance guideline in Japan.



Gender: Promoting Gender Equality

KPI1: Average Percentage of Women in Board / in Management Level

This KPI calculates the simple average percentage of women on the boards and in management positions across our portfolio companies, reflecting our commitment to gender diversity in leadership.

KPI2: Share of Companies with Improving Pay Gap Since Inception of the Fund

This year, we strengthened our fund KPI relating to the gender pay gap. In addition to assessing whether companies have improved their gender pay gap since they first began disclosing the relevant data, we evaluate whether they have identified the underlying causes of the gap and implemented concrete measures to address them. By emphasizing not only improvements in headline metrics but also efforts to address the root causes of the gender pay gap, this KPI supports the achievement of sustainable gender equality across our portfolio companies.

Progress Update (as of 2026 1Q)

All the KPIs have been improved since the inception of the fund in April 2022

		2026 1Q		2022 2Q	Change
Environmental 	a Share of companies with carbon emission reduction initiatives(Scope 1+2) / (Scope 3)	100% / 8.0%	◀	76.9% / -	+23.1% / -
	b Portfolio carbon emission intensity (WACI) (Scope 1+2)	0.42 tCO ₂ e/mil JPY	◀	1.52 tCO ₂ e/mil JPY	-1.10 tCO ₂ e/mil JPY
Social 	c Share of companies with disclosed policy and management for sector material social Issues	85.0%	◀	47.6%	+33.4%
	d Share of companies that disclose human capital initiatives aligned with business strategy	20.0%	◀	-	-
Governance 	e Share of companies that incorporate links to sustainability topic with governance structure	60.0%	◀	23.1%	+32.5%
	f Share of companies with more than 33% of independent board members	100%	◀	96.2%	+3.8%
Gender 	g Average percentage of women in board / in management level	21.6% / 10.6%	◀	13.5% / 7.3%	+8.1% / +3.3%
	h Share of companies with improving pay gap since inception of the fund	20.0%	◀	-	-



Through engagement, we aim to drive improvements in KPIs over a 3-5-year horizon.

* As this KPI has been added from Dec. 2025, there isn't comparison since inception.
KPIs are subject to revision in line with engagement progress, etc. 2. WACI = Weighted Average Carbon Intensity: Weighted average carbon intensity calculated by weighting the "ratio of CO2 emissions to sales" of each company in the portfolio by the percentage of each company's holdings. CO2 emissions are calculated based on the current information disclosed by each company, excluding companies that have not yet disclosed their CO2 emissions. Includes data from different years. The amount may increase or decrease due to changes in the scope of disclosure of portfolio companies, the composition of portfolio companies, or the replacement of portfolio companies. 3. Includes figures for different fiscal years. May increase or decrease due to changes in the scope of disclosure of portfolio companies, replacement of portfolio companies

> 04

Review of the Fund Sustainability KPIs

- GHG Emissions, Human Capital, and Gender Equality

Review & Introduction of New Fund KPIs

We regularly review our fund's KPIs to reflect evolving societal expectations, regulatory developments, and changes in the sustainability performance of our portfolio companies. As part of the latest review, we introduced new KPIs covering carbon neutrality initiatives (including Scope 3 GHG emissions) and human capital management to better support the sustainable growth and long-term value creation of our portfolio companies. We also strengthened the KPI related to the gender pay gap by adopting more rigorous assessment criteria.

1 GHG Emissions (Scope 3)

Background

Through our engagement with portfolio companies, we have observed that efforts to reduce Scope 3 GHG emissions remain less developed than initiatives targeting Scope 1 and Scope 2 emissions. At the same time, societal expectations and regulatory requirements surrounding Scope 3 emissions are increasing, including the introduction of the SSBJ Standards, which require companies to measure and disclose their Scope 3 GHG emissions. In light of these developments—both in the progress made by our portfolio companies and in the evolving regulatory and business environment—we have introduced a new KPI on carbon neutrality initiatives (Scope 3) to encourage and support further action by our portfolio companies.

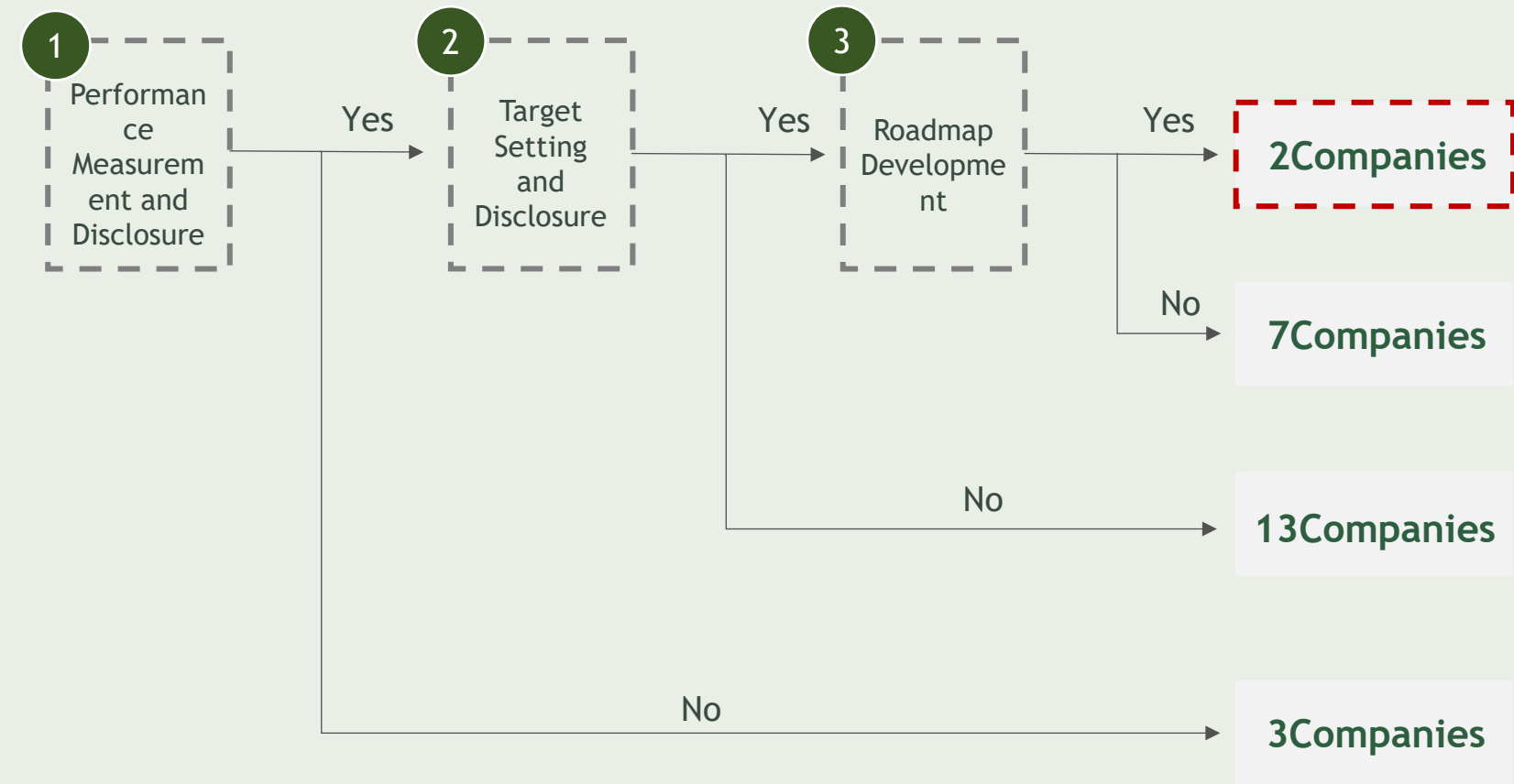
KPI Framework

We consider Scope 3*1 emissions reduction efforts to be effective when the following three conditions are met.

- 1 Whether Performance Measurement and Disclosure Are Conducted
- 2 Whether Targets Are Set and Disclosed
- 3 Whether a Roadmap Toward Target Achievement Has Been Established

*1 : Refers to the major categories among Scope 3 Categories 1-15 that account for the largest share of emissions.

Status of the 25 Portfolio Companies (as of March 2026)



With regard to initiatives toward carbon neutrality (Scope 3), 2 out of 25 portfolio companies (8.0%) are assessed as meeting our defined criteria.

2 Human Capital Management

Background

Human capital management generally refers to activities that turn traditional HR functions into drivers of efficiency, engagement, and revenue, maximizing the value of human capital through proper management and investment. Since the inception of the fund, we have identified human capital management linked to corporate strategy as a key thematic priority and have continuously engaged with our portfolio companies on the establishment and disclosure of KPIs to monitor progress in this area. While disclosure of human capital-related KPIs has generally advanced across companies, KPIs explicitly linked to corporate strategy have, until recently, largely remained at the conceptual or preparatory stage, with many companies refraining from formal measurement and disclosure. However, we are now observing increasing momentum, with more companies beginning to disclose—or preparing to disclose—strategically linked human capital KPIs, as their internal approaches become more clearly defined. In light of this development, we have decided to aggregate and disclose this KPI going forward.

KPI Framework

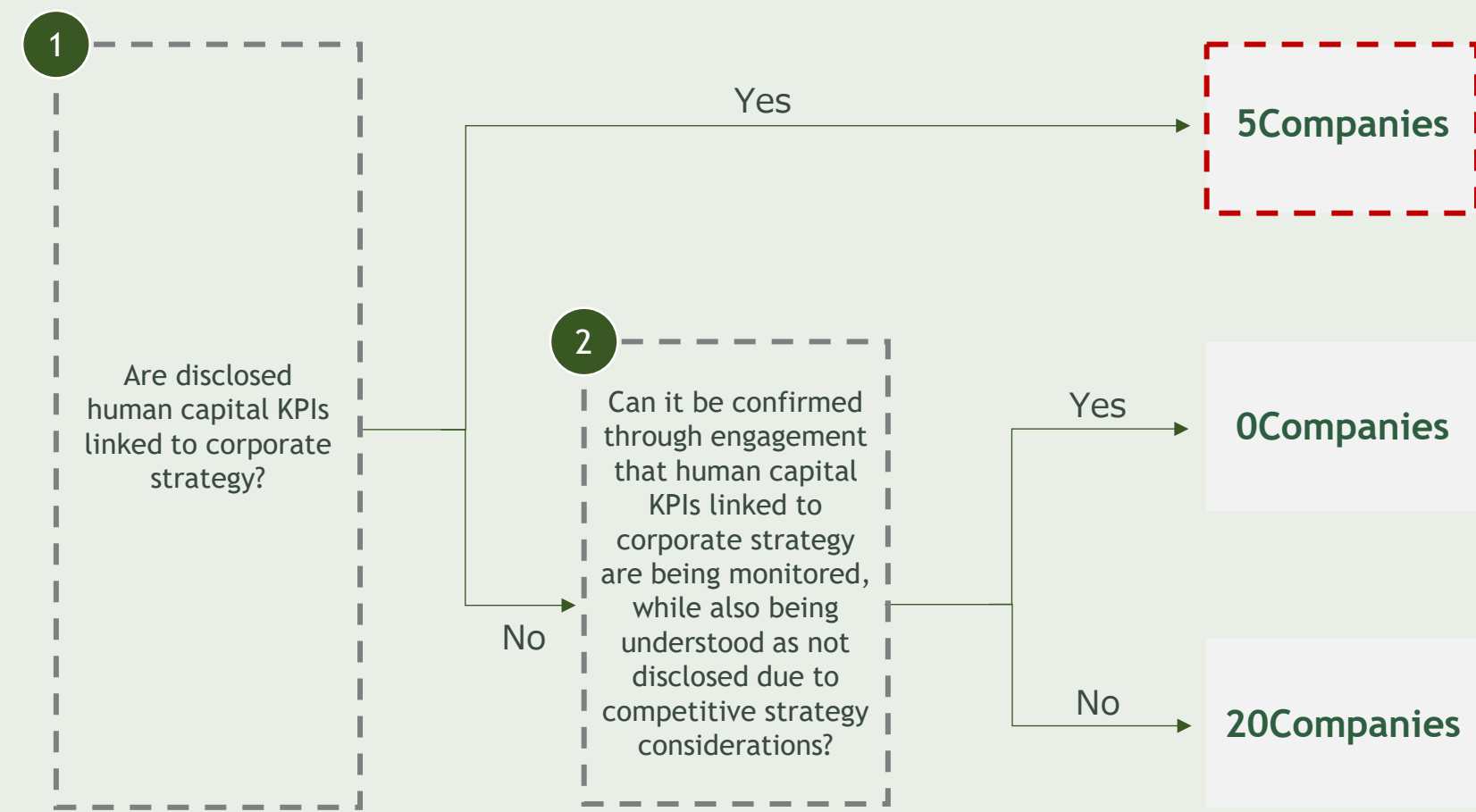
Taking into account each company’s circumstances, we assess KPIs linked to corporate strategy as valid when any of the following conditions are met.

- 1

It can be logically demonstrated that improvements in disclosed human capital KPIs contribute to strengthening corporate strategy and key value drivers.
- 2

We recognize that certain human capital KPIs can be logically linked to improvements in corporate strategy and underlying value drivers. These KPIs can also be assessed through ongoing dialogue with portfolio companies, including discussions on progress and key developments. At the same time, we understand that the disclosure of such KPIs may be limited in some cases due to competitive considerations.

Status of the 25 Portfolio Companies (as of March 2026)



With regard to human capital KPIs linked to corporate strategy, 5 out of 25 portfolio companies (20.0%) are assessed as meeting our defined criteria..

3 Gender Pay Gap

Background

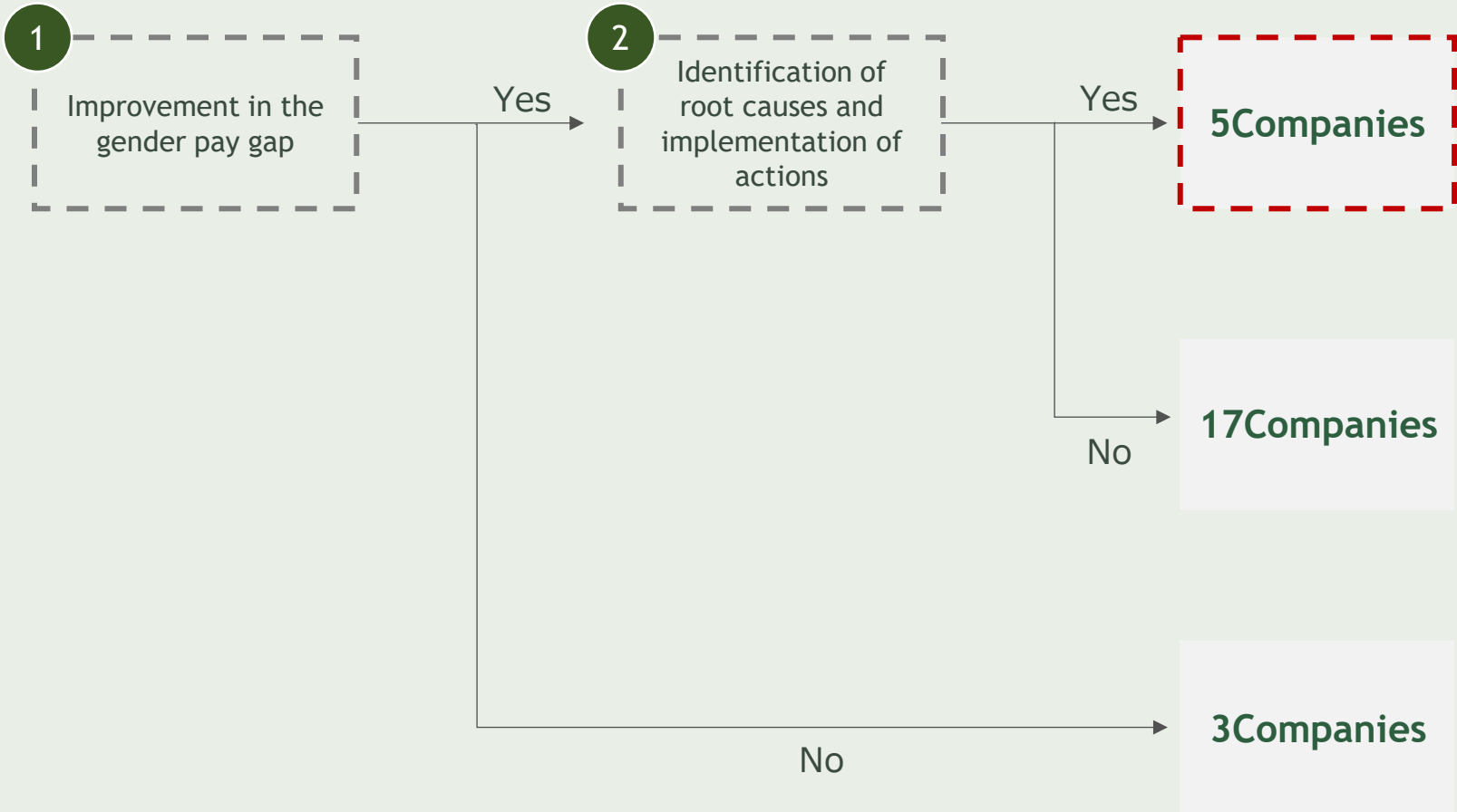
While more than 80% of portfolio companies have shown improvements in the gender pay gap compared to the time of initial disclosure, we have observed that only a very limited number of companies provide evidence—through disclosures or engagement discussions—of analyzing root causes and implementing concrete actions to address them. As a result, although headline figures for the gender pay gap appear to be improving, we believe that underlying structural issues may not yet be fully addressed. Accordingly, we have strengthened the gender pay gap KPI within our fund framework.

KPI Framework

The following two conditions must be met for gender pay gap remediation to be assessed as substantively effective.

- 1 Improvement in the Gender Pay Gap Compared to Initial Disclosure
- 2 Identification of Root Causes and Implementation of Actions

Status of the 25 Portfolio Companies (as of March 2026)



Following a tightening of the fund’s definition of the gender pay gap KPI and a subsequent re-aggregation of the data, 5 out of 25 portfolio companies (20%) are now assessed as meeting our defined criteria.



05

Deep Analysis

- “Global and Japan Trends”,
“Human Capital: Wage Growth and Productivity”

1 . Global and Japan Trends

Global Trends: Strong Regional Differences

2025 was a year in which the direction of ESG-related regulations and policies diverged significantly across regions.

In the United States, the Trump administration's shift in energy policy has had broad implications for the climate and clean energy sectors. Following an executive order issued in January 2025, subsidies and loan disbursements under the Inflation Reduction Act (IRA) were temporarily frozen, and multiple reports point to a wave of project cancellations and revisions across the clean energy sector since the administration took office. In March 2025, legal defense of the SEC's climate disclosure rule was withdrawn. However, these developments remain largely confined to the federal level. State-level regulations such as California's SB-219's GHG emissions disclosure requirements remain in force. In addition, many large corporations continue to pursue voluntary climate disclosures, and there remains a strong view that a full repeal of the IRA would be difficult to achieve in practice.

In Europe, the February 2025 Omnibus I package introduced major simplifications to the CSRD, CSDDD, and the EU Taxonomy. Following a provisional agreement between the European Parliament and the Council in December 2025, the amending directive was formally adopted and published in the Official Journal of the European Union in late February 2026. While the regulatory framework itself remains in place, the scope of covered companies and the implementation timeline have been narrowed.

In contrast, China continued to expand renewable energy at record levels in 2025, with newly installed capacity reaching an all-time high and cumulative installed capacity surpassing thermal power generation for the first time.

While changes reflecting industrial structures and political contexts were observed across regions, dialogue and regulatory developments related to ESG continue in different forms across jurisdictions.

Japan Trends: Progress in Regulatory Development

Against this backdrop of global developments, Japan experienced a year of steady progress in strengthening its frameworks for engagement and disclosure.

In March 2025, the Sustainability Standards Board of Japan (SSBJ) finalized Japan's first sustainability disclosure standards, comprising the Application Standard, General Standard, and Climate Standard. Aligned with IFRS S1 and S2 while incorporating Japan-specific adjustments, voluntary application will begin from fiscal year ending March 2026. Mandatory adoption for Prime-listed companies is expected to be phased in between 2027 and 2029, depending on market capitalization. Greenhouse gas disclosures, including Scope 3 emissions, are also expected to fall within the scope of mandatory reporting, with implications extending across entire supply chains, including small and mid-cap companies. The introduction of Scope 3-related KPIs in our fund framework reflects these evolving external regulatory and market developments.

In June 2025, Japan's Financial Services Agency (FSA) published a third revision of the Stewardship Code (the first revision in five years). The key focus areas of the revision are (i) the institutional promotion of "collaborative engagement," in which multiple institutional investors engage with companies on shared themes, and (ii) the requirement to disclose information on beneficial ownership positions during engagement activities. The Code itself has been streamlined and made more principles-based, with a clearer emphasis on encouraging substantive stewardship activities. The collaborative engagement that our Fund is pursuing with the asset owner is perfectly aligns with the purpose of this revision.

As the institutional foundations for disclosure and engagement continue to strengthen, NextGen ESG Japan will further enhance the quality of its responses and contributions to this transition through active engagement with its portfolio companies.

2. Human Capital: Wage Growth and Productivity

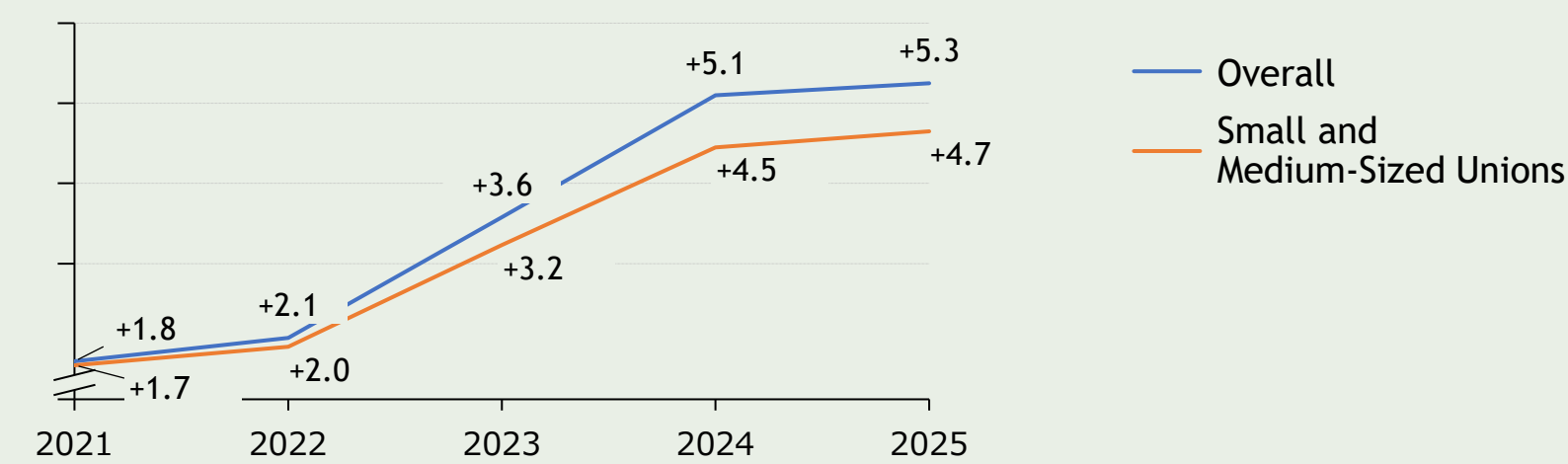
Building on the strong wage growth seen in 2024, the 2025 spring wage negotiations in Japan also resulted in sustained high levels of pay increases. According to final data from Keidanren, large companies recorded an average wage increase of 5.39%, exceeding 5% for the second consecutive year and marking the second-highest level since comparable data began in 1976. The final aggregation by Rengo also showed increases of 5.25% overall and 4.65% for unions with fewer than 300 members, both higher than the previous year.

The sustained wage growth has been primarily driven by labor shortages and intensifying competition for talent. However, it remains an open question whether wage increases are directly translating into improvements in corporate value. In fiscal year 2024, real labor productivity growth was limited to +0.2% year-on-year, indicating that productivity gains have been relatively modest compared with nominal wage increases. In addition, real wages have remained negative as wage growth has not kept pace with inflation, and many observers point out that sustained wage increases will require corresponding improvements in productivity.

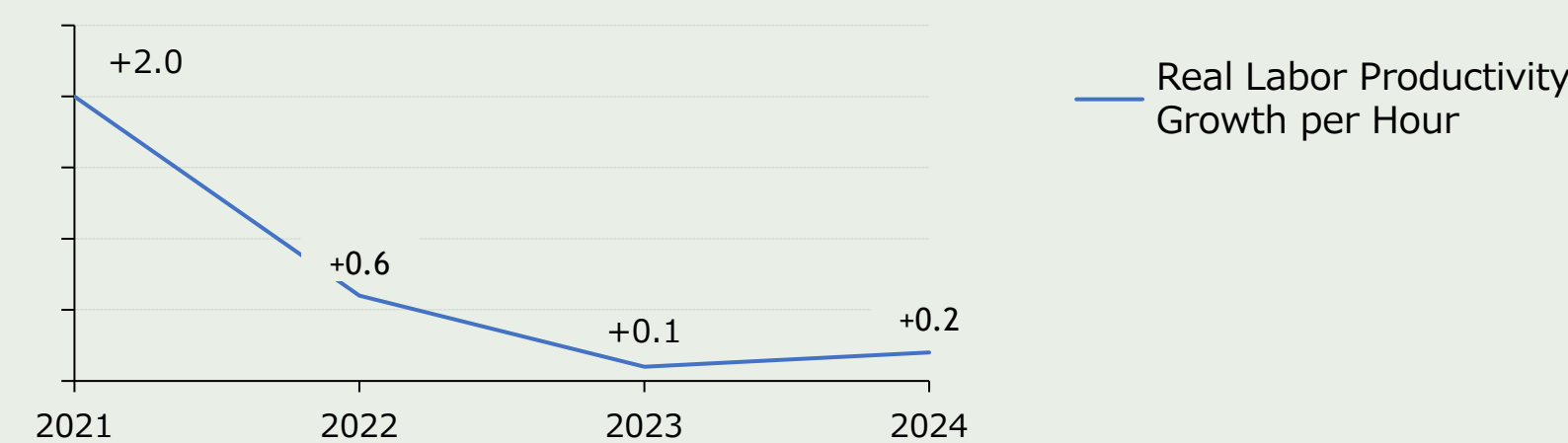
From an investor perspective, a key question is the source of funding for wage increases. If higher wages are financed solely through margin compression, they do not contribute to improvements in ROIC or ROE. Sustainable wage growth therefore requires an increase in value added through measures such as greater price pass-through and structural transformation of business models, ultimately underpinned by genuine improvements in labor productivity.

In our engagements with portfolio companies, NextGen ESG Japan encourages framing wage increases not as a cost item, but as an investment in human capital, and examines how such investments translate into improvements in free cash flow and capital efficiency. Continuously questioning the link between wages, productivity, and corporate value creation remains a core element of our engagement approach.

Reference: Trend in Average Wage-Based Wage Growth (%)



Reference: Trend in Real Labor Productivity Growth (%)



Source: Japanese Trade Union Confederation (RENGO), “Trends in Wage Increases Based on Average Wage Method since the Establishment of RENGO”; Japan Productivity Center, “Labor Productivity Trends in Japan 2025 - Overview.”

➤ 06

Engagement Cases

1

Infrastructure and Materials Company

Company Overview

A leading Japanese non-ferrous metals and infrastructure-related manufacturer engaged in optical fiber and communication cables, power infrastructure, and automotive components. Amid accelerating investment in AI-driven data centers, the company’s optical solutions business has attracted growing expectations for expansion. Improvements in profitability and capital efficiency have been positively received by the market, contributing to a significant increase in investor attention and a strong rise in the share price.

Strategic ESG Engagement

Since the inception of the fund, we have conducted engagement from both financial and sustainability perspectives. At the time of initial investment, our financial focus was on growth in the U.S. telecommunications cable business and profitability improvements driven by portfolio restructuring. From a sustainability perspective, we have engaged in ongoing dialogue on key topics closely linked to the business, including global ESG governance structures, GHG emissions reduction, supply chain management, human rights, and gender diversity.

Deepening Investment Conviction through Continuous Engagement

Early-stage dialogue with the company provided important insights, particularly that management quality was improving and that leadership capabilities were being strengthened in a more systematic manner. Based on these observations, we continued to maintain our investment position, recognizing the potential for medium- to long-term value creation and a possible reassessment by the market.

The company has also acknowledged the relevance of our engagement approach, which links sustainability considerations with financial impact. At its request, we have held regular meetings with the current Representative Director since 2023.

Direct engagement with senior management, who have decision-making authority over both strategy formulation and execution, has not only deepened our understanding of the company but also significantly strengthened our conviction in its ongoing transformation, particularly the shift in both the magnitude and quality of earnings growth.

2023 Initial Engagement
Initial Dialogue to Enhance the Effectiveness of ESG Management

In our initial engagement in 2023, we focused on discussions aimed at improving the effectiveness of ESG management. We exchanged views on the progress of sustainability-related indicators, global information-sharing and governance frameworks, as well as proposed enhancements in disclosure related to the introduction of Economic Value Added (EVA) and organization-wide initiatives to improve capital efficiency.

We also discussed the company’s purpose-setting project led by a group of younger employees, focusing on its impact on employee decision-making and motivation, as well as the degree of internal penetration, which strengthened our conviction in the evolution of the corporate culture. On the environmental side, we deepened our understanding of the company’s approach to Scope 3 emissions reduction and the rationale for incorporating GHG-related metrics into executive compensation.

2024 Engagement
Deepening Discussion on Business Portfolio Transformation and Strategy Execution

In 2024, we further advanced discussions on the optimization of the company’s business portfolio. We engaged in dialogue on the progress of embedding the newly defined corporate purpose, its linkage to improving employee engagement, and the ongoing globalization of business operations.

We also deepened discussions with the management team regarding the balance between long-term capital efficiency improvement and growth investments.

2025 Engagement
Advancing Discussions on Capital Efficiency Management and Enhanced Value Creation

In the third engagement year (2025), amid increasing market confidence in the company’s growth trajectory, we focused our discussions on human capital management as a key enabler of further growth. While there was a shared recognition of the importance of human capital management, we highlighted remaining challenges in linking these initiatives to future cash flow generation, as well as the lack of externally observable KPIs to assess progress.

We also conducted a comparative financial analysis with peer companies to clarify how the company’s human capital strategy is positioned. Using data-driven insights, we noted that its approach is less clearly articulated externally compared to peers that enhance enterprise value through increases in operating profit per employee and strategic headcount expansion. We also pointed out that wage growth has not been fully aligned with operating profit growth, suggesting limited evidence of a differentiated or evolving human capital strategy. We proposed the need for a clearer strategic framework to ensure sustained talent acquisition and retention.

The management team positively acknowledged the uniqueness of our analytical perspective and the quality of the insights provided. They also confirmed internal discussions are underway to simplify business disclosure segments in line with ongoing portfolio restructuring, with the aim of better reflecting the financial impact of strategic initiatives.

2025 Engagement Materials

Current Status and Today's Discussion Topics

Current Situation Assessment

- While your share price has performed strongly in recent months, the gap between the current market price and our estimated intrinsic value remains relatively large compared with peers, reflecting a significant expectations-driven premium and resulting in elevated share price volatility.
- To sustain and further enhance the current strong share price performance and valuation while reducing share price volatility, would it be beneficial to communicate more clearly your medium- to long-term strategy and progress toward enhancing corporate value, including the direction of the next Medium-Term Management Plan?

✓ The market has developed a better understanding of the Company's ROIC- and EVA-driven business portfolio transformation strategy over the course of the current Medium-Term Management Plan, while initiatives to enhance capital efficiency have continued to progress steadily.

✓ As industries continue to mature, technological transformation accelerates, and talent becomes an increasingly scarce and critical management resource amid a declining population, it may be worth considering framing the Company's long-term value creation story from the perspective of human capital as well.

In today's ESG meeting, based on our analysis from a human capital perspective, we would like to discuss the Company's approach to enhancing corporate value, with a particular focus on its human capital management strategy.

A Corporate Value Creation Story Can Be Built Around Human Capital, Alongside Financial Capital

Corporate value

Financial Capital

ROIC-WACC

Invested Capital

Illustrative Discussion Points

- How can asset efficiency be further improved?
- (How should the balance between capital deployment and capital recovery be optimized?)
- Which markets offer opportunities to deploy capital at a high marginal ROIC?, etc.

Value Created Through Human Capital

Value Added per Employee (Productivity – Personnel Cost per Employee)

Number of Employees

Illustrative Discussion Points

- What is the Company's human capital strategy? (higher value added per employee or headcount growth?)
- How can workforce productivity be further improved?
- How should the Company balance value creation with investment in its workforce?, etc.

Source: Impact-Japan, Asuka Corporate Advisory Co., Ltd.

Your Company's Workforce and Productivity Profile (1)

- Compared with peers, which are enhancing corporate value by increasing either operating profit per employee or workforce size, the Company's progress has been relatively modest.
- While peers have generally increased average salaries in line with operating profit growth, the Company's average salary growth has remained relatively limited.

Number of Employees × Operating Profit per Employee

Operating Profit per Employee (JPY million)

Number of Employees (FY2017/3 Year-End = 100)

◆ indicates the latest fiscal year (FY2025/3)

Operating Profit per Employee Growth × Average Salary Growth (Parent Company)

Average Salary (FY2017/3 = 100)

Operating Profit per Employee Index (FY2017/3 = 100)

◆ indicates the latest fiscal year (FY2025/3).
*Company A: FY2024/3, reflecting the transition from a holding company to an operating company.

Source: Asuka Corporate Advisory, based on annual securities reports and other public disclosures.

Outcomes and Ongoing Engagement

Approximately six months after our dialogue, the company announced its new medium-term management plan, in which productivity improvement and the maximization of human capital were elevated to key management priorities. This shift reflects an enhanced commitment to strengthening management execution, and we believe our engagement may have contributed, at least in part, to this development.

In addition to growing investor confidence in the company's growth trajectory driven by AI-related demand, the market has also begun to recognize these efforts to strengthen management capabilities. The company is also advancing initiatives to enhance corporate governance as a global organization, including improving decision-making speed through a clearer separation between oversight and execution.

Going forward, we will continue to closely monitor how ongoing management reforms translate into both sustainability and financial impact, and we will further advance our engagement with the aim of supporting long-term corporate value creation.

Your Company's Workforce and Productivity Profile (2)

Workforce Size and Operating Profit per Employee by Business Segment

Operating Profit per Employee (JPY million)

Number of Employees (FY2017/3 Year-End = 100)

◆ indicates the latest fiscal year (FY2025/3)

Workforce and Asset Composition

Workforce Composition (Headcount) (As of March 31, 2025)

Asset Composition (JPY mn) (FY2025/3 Year-End)

- Your Company - Infrastructure
- Your Company - Electrical Equipment & Electronics
- Your Company - Functional Products
- Your Company - Services, R&D and Others

Source: Asuka Corporate Advisory, based on annual securities reports and other public disclosures.

Resource Allocation (R&D Expenditure and Capital Expenditure)

As a Percentage of Revenue

R&D Expenditure

Capital Expenditure

Index (FY2017/3 Year-End = 100)

Source: Asuka Corporate Advisory, based on annual securities reports and other public disclosures.

2

Precision Components Manufacturer

Company Overview

Since its founding, the company has consistently focused its business on a specific core component, leveraging standardization by application as a key source of competitiveness. It supplies products to both the transportation equipment sector and the consumer and industrial equipment sectors. The company has a highly globalized business structure, with the majority of its production and sales conducted overseas, and employs approximately 20,000 consolidated employees.

In recent years, under its medium-term management plan, the company has been expanding its business beyond core products into solution-oriented areas, while pursuing group-wide expansion including through M&A. Against this backdrop of a global supply chain and growth strategy, human rights management has become an increasingly important priority for the company.

Strategic ESG Engagement

For the Fund, which targets the improvement of sustainability performance and disclosure across portfolio companies over a 3-5 year investment horizon, human rights represents a core engagement theme within the social (S) pillar.

We do not treat human rights as a mere compliance issue. Rather, in line with the UN Guiding Principles on Business and Human Rights, Japan’s national “Guidelines on Respecting Human Rights in Responsible Supply Chains,” and emerging European regulations on human rights and environmental due diligence, we position it as a critical management issue that contributes both to enhanced societal trust and long-term enterprise value creation. In recent years, public attention has increasingly focused on human rights issues that can undermine corporate value, including forced labor involving migrant workers and workplace harassment.

In our dialogue with investee companies, we frame the topic from two perspectives: (1) risk mitigation and (2) competitiveness enhancement. The former aims to reduce risks such as negative screening outcomes, divestment, or termination of business relationships, while the latter focuses on strengthening brand value and building resilient, globally competitive supply chains.

We continue to encourage companies to treat human rights initiatives and related disclosures as strategic priorities that contribute directly to long-term value creation.

Engagement Process on Human Rights Issues

Since initiating dialogue on human rights in early 2025, the Fund has deepened a two-way engagement approach, moving beyond one-sided requests toward a collaborative model in which external experts provide insights in response to consultations from the company.

The company follows an annual cycle in which it discloses the prior year’s initiatives on its website at the beginning of the following year, and determines its annual activity plan at year-end through a committee process. Within this framework, the company sought our input on how and to what extent it should disclose its supplier human rights risk assessment activities.

In response, we shared materials outlining investor expectations regarding human rights due diligence, including the identification and prioritization of high-risk areas, expected disclosure indicators, key considerations across the value chain, and relevant leading practices among peer companies.

Beyond aligning with common Japanese market practices, we have also provided ongoing feedback through continuous dialogue on the direction of more advanced practices required to support the company’s corporate philosophy and its future global management framework.

2025 Engagement Materials

Why We Would Like to Discuss Your Human Rights Initiatives Today

In light of growing domestic and international expectations for respect for human rights, establishing a supply chain that fulfills the Company's responsibility to respect human rights has become increasingly essential. We believe that enhancing the effectiveness of these initiatives is critical to strengthening competitiveness and supporting long-term corporate value creation.

Human Rights and Environmental Due Diligence Is Accelerating in Europe, Shifting from CSR to a Legal Obligation
The EU's Corporate Sustainability Due Diligence Directive (CSDDD), adopted in 2024, marks a shift toward mandatory human rights and environmental due diligence. While Japan continues to rely on a "soft law" approach based on voluntary compliance, Europe and North America are moving toward legally binding "hard law" requirements. Consequently, Japanese companies are increasingly expected to prepare for mandatory human rights due diligence, both directly and indirectly.

Directly Linked to Competitiveness Assessment
A fair and transparent supply chain is fundamental to fulfilling corporate responsibility to respect human rights. Achieving this requires the ability to optimize human and financial resource allocation and execute efficient operations throughout the supply chain, which we believe directly contributes to corporate competitiveness.

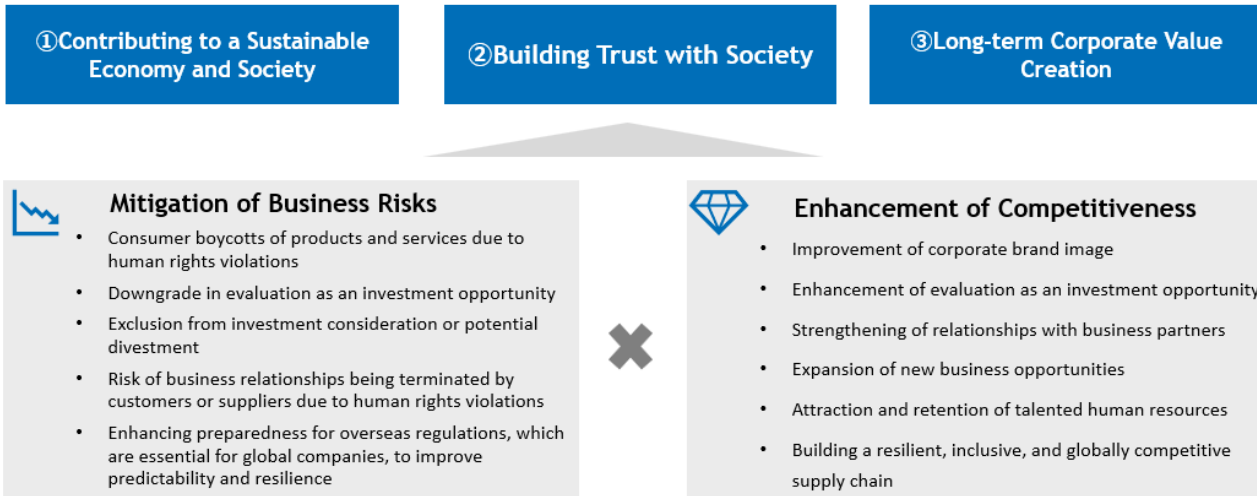
Contributing to long-term corporate value creation
We believe that continuously building and improving a stable and resilient supply chain through human rights initiatives can mitigate business risks, enhance the international competitiveness of products and services, and contribute to maximizing future cash flows.

Prepared by SIJ  

Our Fund's Key Dialogue Points on Human Rights

Significance of Corporate Responsibility to Respect Human Rights

Fulfilling corporate responsibility to respect human rights is a critical initiative that can both mitigate business risks and enhance competitiveness, contributing to (1) a sustainable economy and society, (2) increased trust from society, and (3) long-term corporate value creation.

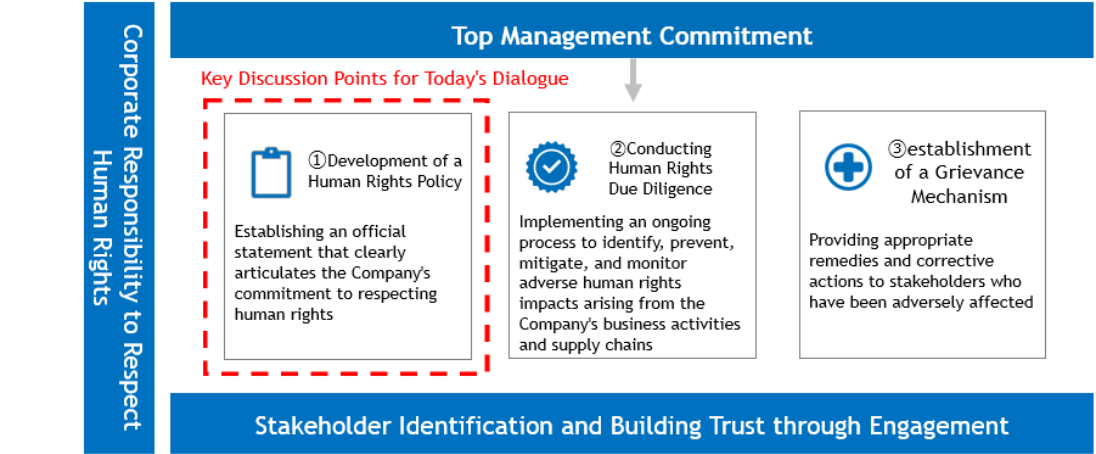


Prepared by SIJ based on [the Guidelines on Respecting Human Rights in Responsible Supply Chains and other relevant guidelines.](#)  

Our Fund's Key Dialogue Points on Human Rights

Key Discussion Points for Today's Dialogue

Our Fund believes that strong commitment from top management is essential to advancing corporate initiatives on respect for human rights. Through constructive dialogue, we aim to contribute to enhancing the effectiveness of your human rights initiatives. Today, we would like to discuss the process of developing a human rights policy and your human rights governance structure, focusing on one of the three key actions outlined under the "Corporate Responsibility to Respect Human Rights."



Reference: "Guiding Principles on Business and Human Rights" and "Guidelines on Respecting Human Rights in Responsible Supply Chains"  

Our Fund's Key Dialogue Points on Human Rights

Development of a Human Rights Policy

Fulfilling the responsibility to respect human rights requires companies not only to establish a human rights policy, but also to ensure its effectiveness through effective implementation. The Japanese guidelines outline the following five requirements for a human rights policy.

- Five Effectiveness Requirements**
- 1 Approved by top management, including executives
 - 2 Developed through a process that incorporates internal and external expertise and reflects operational realities
 - 3 Clearly articulates the Company's expectations for respect for human rights among employees, business partners, and other stakeholders directly involved in its operations, products, or services
 - 4 Publicly available and communicated internally and externally to all employees, business partners, and other stakeholders
 - 5 Embedded in business policies and procedures to ensure the implementation of the human rights policy across the organization

Prepared by SIJ based on [the Guidelines on Respecting Human Rights in Responsible Supply Chains and other relevant guidelines.](#)  

Outcomes and Ongoing Engagement

These dialogues have led to concrete company actions and ongoing internal implementation. Progress has been observed in several areas, including: (i) enhanced disclosure through prioritization of risks and the addition of process-related indicators, (ii) consideration of more sophisticated assessment methodologies for high-risk suppliers, (iii) development of due diligence and assessment frameworks in relation to M&A and overseas expansion, and (iv) strengthening of grievance and remediation mechanisms.

In addition, we observe a clear shift not only in individual initiatives but also in the company's overall approach to human rights disclosure. The company has begun to proactively raise questions with investors based on its own assessment of key issues, and through such dialogue, is advancing both disclosure and operational practices in parallel. We view this as a strong example of constructive engagement.

Going forward, we will continue to support the company in advancing toward global best practices in human rights management and disclosure, and will maintain our engagement as it moves into the next stage of sophistication.

> 07

Collaborative Engagement

Collaborative Engagement

From the first quarter of 2025, we initiated a collaborative engagement with an asset owner, an investor in the Fund. The third revision of Japan’s Stewardship Code highlights the importance of proactive stewardship activities by asset owners and strengthened collaboration with asset managers. Through this partnership, we aim to enhance the effectiveness of our engagement activities, and to further promote constructive dialogue that contributes to long-term corporate value creation.

Collaborative Engagement Cycle



※ Our collaborative engagement is conducted in a manner that does not fall under “joint holders” as defined by the Large Shareholding Reporting Regime, and we do not intend to engage in any material proposals related to control or the exercise of corporate influence.

Significance of Collaboration

Enhancing Engagement

By combining the asset owner’s perspective with our engagement expertise, we aim to generate synergies between both parties and achieve more effective dialogue with portfolio companies.

Contribution to Corporate Value Enhancement

Through ongoing dialogue with portfolio companies, we support their efforts to address ESG issues and enhance long-term corporate value creation.

Sharing and Accumulation of Knowledge

We share engagement outcomes between both parties and leverage them to continuously improve our engagement approach and the framing of key discussion topics.

FY2025 Results (Key Themes)

- › Visualization of the virtuous cycle between the creation of social value and the enhancement of economic value
- › Clarifying Social Outcomes and Setting KPIs for Regional Revitalization
- › Disclosure of Targets, Progress, and Initiatives for GHG Emissions Reduction
- › Human Capital Strategy Aligned with Business Strategy



NextGen ESG Japan Annual Report 2026

Investment Manager: dLab Asset Management Limited <https://www.dlab-am.com/>

Investment Advisor: SDG Impact Japan Inc. <https://sdgimpactjapan.com/jp/>,
Asuka Corporate Advisory Co., Ltd. <https://jp.asuka-advisory.com/en/>

For more information, please contact us at <https://sdgimpactjapan.com/contact/>

This annual report for NextGen ESG Japan has meticulously outlined our fund's strategic focus on ESG engagement, demonstrating a profound commitment to sustainability and positive impact across our portfolio companies. From our foundational concept and strategy to our rigorous sustainability KPIs showcasing progress in critical areas such as GHG emission reductions, human capital development, and gender equality, we have detailed our proactive approach and tangible outcomes.

Through the pressing ESG issues in Japan, we've highlighted the strategic engagements that drive both environmental stewardship and social responsibility. In particular, our engagement case with a leading semiconductor manufacturer exemplifies our commitment to fostering sustainable growth and resilience as we navigate global challenges.

This annual report demonstrates our unwavering dedication to leveraging ESG integration as a catalyst for sustainable investment, aligning financial returns with the broader goal of achieving a sustainable and equitable future for all. Through strategic engagement, targeted feedback, and a commitment to continuous improvement, we not only navigate the complexities of the modern financial landscape but actively contribute to shaping a more sustainable world, offering our investors the opportunity to be part of this vital journey towards responsible capitalism.

SDG
Impact Japan



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