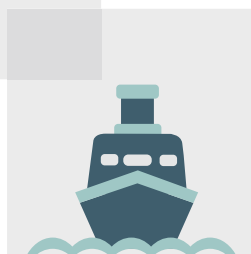
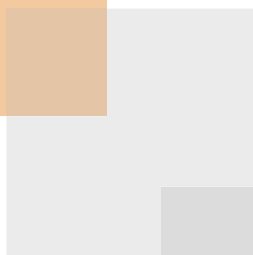


PERFECT STORM PROFITS AT RISK IN THE JAPANESE SEAFOOD INDUSTRY

EXECUTIVE SUMMARY

OCTOBER 2019



Planet Tracker

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ABOUT PLANET TRACKER

Planet Tracker is a non-profit financial think tank aligning capital markets with planetary limits. It was launched in 2018 by the Investor Watch Group whose founders, Mark Campanale and Nick Robins, created the Carbon Tracker Initiative.

Planet Tracker was created to investigate market failure related to ecological limits. This investigation is for the investor community where, in contrast to climate change, other ecological limits are poorly understood and even more poorly communicated, and not aligned with investor capital.

THE FISH TRACKER PROGRAMME

The Fish Tracker Initiative investigates the impact that financial institutions have in financing global wild-catch fisheries and seafood trade. Our aim is to align capital markets with sustainable fisheries management. Fish Tracker is a part of the wider Planet Tracker group of Initiatives.

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FOREWORD

The publication of this report is particularly timely because it coincides with a critical period in the development of the Japanese seafood industry which, historically, has been a leading force in supplying wild-catch fish to satisfy global demand. The future importance of seafood as a food source for the ever-growing global population is undisputed yet, as our report demonstrates, Japan's place in that market is now under serious pressure.

The facts speak for themselves. Seafood production in Japan has been in serious long-term decline since 1985 and is projected to continue to fall to 2025. To mitigate this decline, Japanese seafood companies have increased imports and invested in aquaculture. Since 2009, the share value of Japanese seafood companies has shown steady growth. The implication of these two trends is that, unless there is a recovery in wild-catch fish stocks to support a regeneration of industry growth, investors are facing the serious possibility of a seafood bubble which is ready to burst in the near future.

The overall message of our report is that it is not too late to turn things around. The focus of Planet Tracker is to use global capital allocation to stimulate companies and industries to adopt different and more sustainable practices.

Planet Tracker is concerned with studying different commodity markets to identify risk for investors arising from a variety of factors, but we are principally concerned with risk arising from the way in which natural environments are managed and how unsustainable practices undermine the stability of global investment portfolios.

We chose Japan as the focus of this study, not just because there are clear issues to be addressed, but also because, as our report highlights, the Japanese seafood industry potentially has such an important role to play in moving things in a positive direction.

The Japanese Government has also shown its willingness to address these issues through the revision of the Fisheries Act in 2018.

The financial lessons to be learnt from where the seafood industry is today give a clear message to investors and credit lenders who support companies in the industry. The solution to this may be complex – but it is not unachievable. We have set out detailed recommendations for action in our report, which we urge all the relevant interests, seafood companies, asset owners, credit lenders, regulators and Government to consider carefully, as they *all* have a part to play in creating sustainable wild-catch fisheries and sustainable profits for seafood companies.

I hope that the findings of the report will generate conversations and actions which will serve to regenerate the wild-catch fish stocks which underpin this important industry before it is too late.

"Japan was the biggest seafood country in the world but various combining factors in the last 30 years contributed to its marine resources decreasing to less than half of the peak catch volume. However, Japan is surrounded by some of the best fishing grounds in the world and we should do what it takes to replenish our marine resources. By both establishing large-scale, comprehensive frameworks and achieving detailed, continuous reforms, we will strengthen how we implement stock assessments, resource management and IUU measures in Japanese-specific ways."

*Shigeto Hase,
Director General, Fisheries Agency, 2018*

*Mark Campanale
Founder, Planet Tracker*

EXECUTIVE SUMMARY

Wild-catch fish and aquaculture produce, defined jointly as seafood, represent one of the world's most valuable globally traded food commodities, according to the UN Food and Agriculture Organisation (FAO).¹ Seafood is an essential part of the diet for billions of people and supports hundreds of millions of jobs.

Global seafood production peaked at 171 million tonnes in 2016, with wild-catch fisheries and aquaculture generating sales of \$130 billion and \$232 billion respectively. In 2017, the 100 top global seafood companies generated wild-catch fisheries and aquaculture revenues of \$101 billion.

Japan's seafood industry is the leader in the global listed equity wild-catch fishing market and is home to 23 of the top 100 listed companies worldwide, with revenues of \$37 billion from global seafood sales in 2017.²

Recent decades have seen a steep decline in Japan's seafood production which peaked in 1985 at 12.8 million tonnes (metric tonnes) and has since decreased by two thirds to 4.3 million tonnes in 2017 (3.3 million tonnes wild-catch and 1.0 million tonnes farm-raised) - see Figure 1.

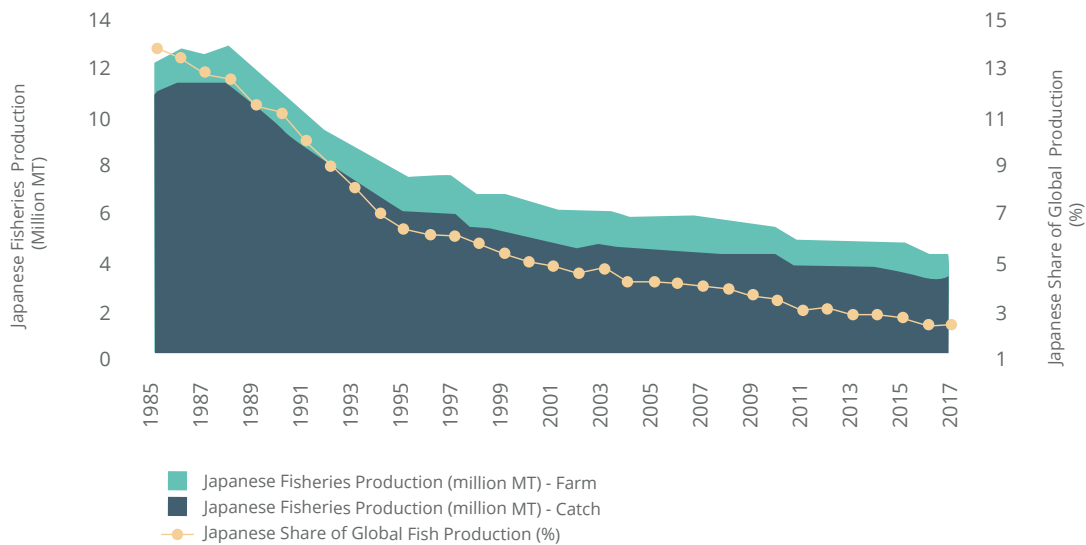


Figure 1: Japan's Fisheries and Global Market Share 1985-17.³

Japan's share of global seafood production has been impacted by overfishing as a result of growing competition from other nations. This has caused Japan's combined share of global wild-catch fish and aquaculture production to fall by 85%, from 13.4% in 1985 to 2.2% in 2017.

In 2016, a third of the world's fisheries were overexploited and just 7% under-exploited. By contrast, in 1975 only about 10% of global fisheries were overexploited while 40% were underexploited.⁴

Overfishing poses serious financial and reputational risks, not just to Japanese wild-catch companies, but to the investors and credit lenders who finance them. Currently they have limited ability to tell whether the companies they finance are sourcing wild-catch fish sustainably or not.



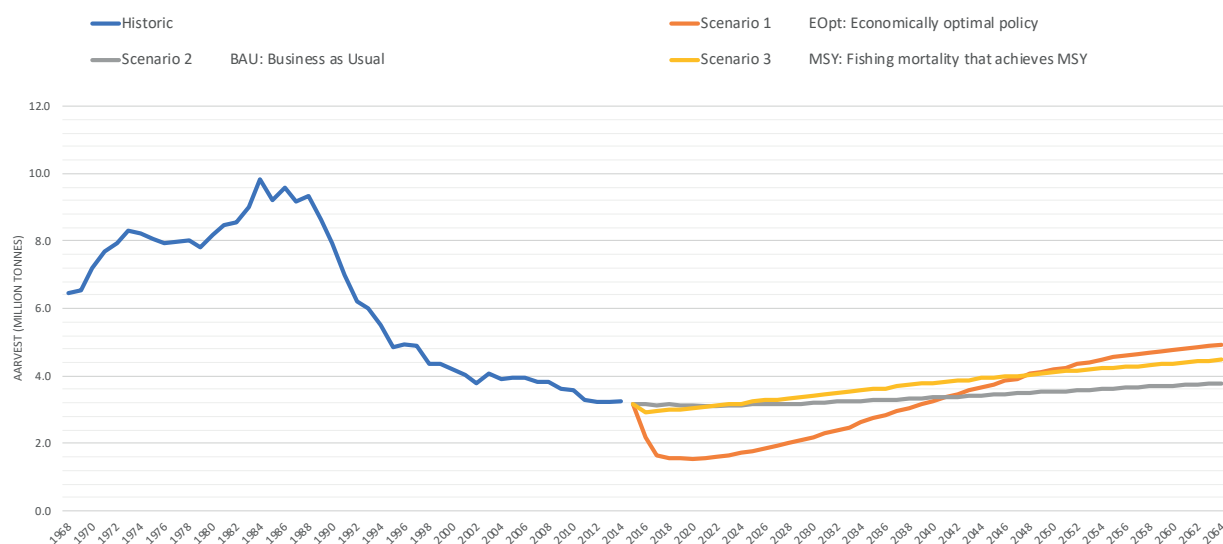
As a result investors and lenders face unpriced financial and credit risks and companies are experiencing lost revenues and escalating operating costs as vessels go further afield and stay out longer to catch dwindling stocks of fish.

Investors and lenders are also exposed to the reputational risk of companies in which they invest that import fish caught unsustainably or illegally. Global seafood firms apply a variety of different norms and values to their sourcing, which are seldom equivalent to Japanese standards.

If investors and credit lenders adopt policies that support the sustainability of wild-catch seafood stocks, these financial risks can be mitigated. Similarly, when seafood firms are prepared to apply sustainable fishing practices, they can reduce their exposure to financial and reputational risks and strengthen market positioning to grow future revenues.

If fisheries were managed sustainably to achieve their maximum sustainable yield, the global industry could earn an estimated \$51 billion to \$83 billion extra every year, part of which would transition back to investors and credit lenders.^{5,6,7}

Research published in October in the journal Marine Policy (Vol. 108) finds that Japanese fisheries alone could generate an extra \$5.5 billion a year by 2065 if catches are reduced in the short term to allow stocks to rebuild - see Figure 2.



K. Tokunaga et al (2019) Alternative outcomes under different fisheries management policies: A bioeconomic analysis of Japanese fisheries.

Figure 2: Catch Trajectories Under Three Policy Scenarios.

Leading Japanese funds are among the biggest investors, including Japan’s Government Pension Investment Fund, the world’s largest pension fund, as are many of the world’s biggest asset managers including BlackRock, State Street and Vanguard, all based in the United States.

Japan’s seafood industry, as the world leader, including Japanese companies whose interests include seafood production, has a unique role to play by using its influence to ensure fisheries are managed sustainably to achieve maximum sustainable fish production (maximum sustainable yield) which will secure both industry and investor positions.

Planet Tracker analysed a group of 41 Japanese listed companies (see Appendix 8) active in the seafood business with a combined market capitalisation of \$134 billion in 2019.

This report focuses on seven key risks facing these companies and the investors and credit lenders that finance them and makes recommendations on how to address these risks.



Investors are Not Pricing or Reporting on Seafood Risk

Investment performance of Japanese seafood companies is being compromised by the following factors adding risk to shareholder capital and lender credit:



Declining seafood stocks: Reducing catch and increasing operating costs resulting in lower profit margins.



Industry accounting standards: Provide no mechanism to value wild-catch seafood asset values on company balance sheets.



Climate change: Warming sea temperatures impact distribution range, migratory habits and stock size of wild-catch fisheries.⁸



Traceability of fish catches: Investors have no mechanism to obtain public and independently validated data on seafood type or when, where and how much is caught or purchased by seafood companies.



Transparency of operations: Lack of supply chain transparency and performance disclosure by seafood companies makes it impossible for investors to link company revenue figures with fisheries that are over-fished or at risk of overexploitation.



Opaque subsidiaries: Planet Tracker found 2,900 subsidiaries of the 41 listed companies assessed in this report. It is difficult to determine how many of these operate in the seafood industry. Investors in the 41 seafood companies have no visibility of these subsidiaries' operations, liabilities and performance.



Industry inefficiencies: The wild-catch fishing industry is failing to realize annual economic benefits from \$51 billion to \$83 billion^{9,10,11} because of fisheries mismanagement where biomass has been reduced below maximum sustainable yields, leading to higher access and extraction costs.¹²



Ten of the Top 15 investors in the sector are Japanese, accounting for 51% of the equity of the leading 41 Japanese seafood companies by market capitalisation.

Emerging Insights for Investors

Japanese Seafood Companies can:

- **Secure Sustainability Certification:** Demonstrate global leadership by transitioning towards full certification by an internationally recognised standard such as the publicly accessible Marine Stewardship Council (MSC) Fisheries Standard or an equivalent.
- **Adopt Full Traceability:** Carry independent observers and/or vessel monitoring systems (VMS) on all vessels to record catches. Companies can then publicly report on where their seafood has been caught, under which quota and from which vessels. Full traceability creates conditions in which Japanese fisheries are better able to demonstrate industry-leading legal labour conditions and support full employment in the sector.
- **Report Operations Transparently:** Publicly report each year on their beneficial ownership of subsidiaries and related vessels and transport and processing infrastructure, eligible quotas, their fishing activities, catch data and taxes accrued to the Government of Japan.
- **Biological Reporting:** Apply International Accounting Standard (IAS) 41 or equivalent to audited company accounts for wild-catch fisheries, fully reporting on biological stock values, to improve sector wide accounting evaluations.
- **Adopt a Sustainability Policy:** Implement and report against a credible sustainability policy, with independently verifiable performance. This could include adopting Norges Bank Investment Management Policy on *Ocean Sustainability Expectations Towards Companies* by 2020 (see Appendix 5).



- **Report in English:** Publish annually all traceability, transparency, beneficial ownership, sustainability policies and sustainability performance data in English as well as Japanese so as to ensure that global financial data providers accurately report on Japanese seafood companies' activities. Planet Tracker research found certain companies publishing high quality sustainability reports not available in English which limits the ability for improved investment decision-making.

Asset Owners and Credit Lenders can:

- **Require Sustainability Certification:** Only invest in, and issue credit to, companies and fisheries fully certified by, or transitioning towards, an internationally recognised standard such as the MSC Fisheries Standard or an equivalent.
- **Conduct Due Diligence and Monitoring:** Assess companies annually to ensure they meet all sustainability requirements as set by the credit lender.
- **Mandate Full Traceability and Transparency:** Request independently validated reports on when, where and by what method fish used by company operations have been caught and under which quota.
- **Establish Sustainability Policies:** Ask seafood companies without sustainability policies to adopt and implement these in order to mitigate investment risks detailed in this report.
- **Adopt Sustainable Investment and Lending Principles:** Utilise the Principles for Investment in Sustainable Wild-caught Fisheries launched at the World Ocean Summit in 2018 to assess seafood investment opportunities for portfolios, with 3rd party compliance verification.¹³ These Principles were designed by a coalition of asset managers, banks, conservation organisations and foundations. As the Government of Japan is a global leader in supporting the SDGs, there is a convergence between these Principles and their alignment with the UN Principles of Responsible Investment and the UN SDGs.

Japanese Regulators and the Japanese Ministry of Agriculture, Forestry and Fisheries can:

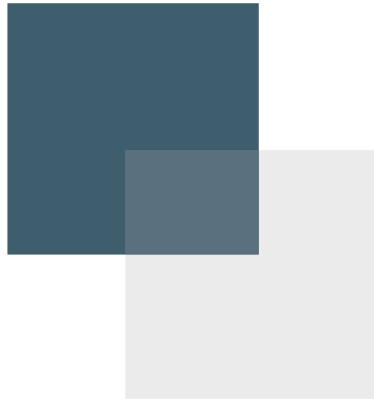
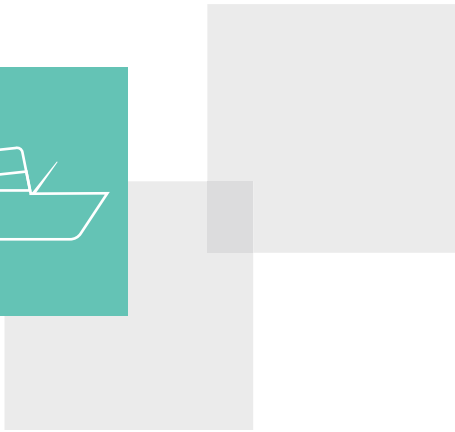
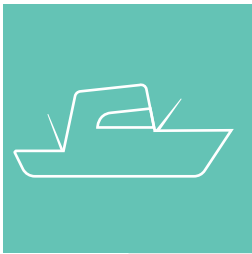
- **Mandate On-Ship Monitoring:** Require all vessels registered to Japanese companies and their subsidiaries and related parties to carry independent observers and/or use VMS tools to record catch – such schemes are beginning to roll out in other global fisheries. Such tools can also enable accurate reporting of tax revenue from seafood production to the Government of Japan.
- **Mandate Vessel Ownership Disclosure:** Require companies regulated by the Japan Financial Services Authority to annually disclose and publish any beneficial ownership in vessels and related processing and transport infrastructure by their company.
- **Require transparent sourcing for wild-catch fisheries:**
 - Level the playing field between Japanese companies and foreign operators
 - Reduce mislabelling of seafood
 - Improve food safety
 - Decrease wasted by-catch
 - Decrease market access to criminal elements
 - Monitor fish transshipment events
 - Assert sovereignty and rule of law in Japan's Exclusive Economic Zone.

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FUNDERS



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