

JGB Market & Debt Management Policy

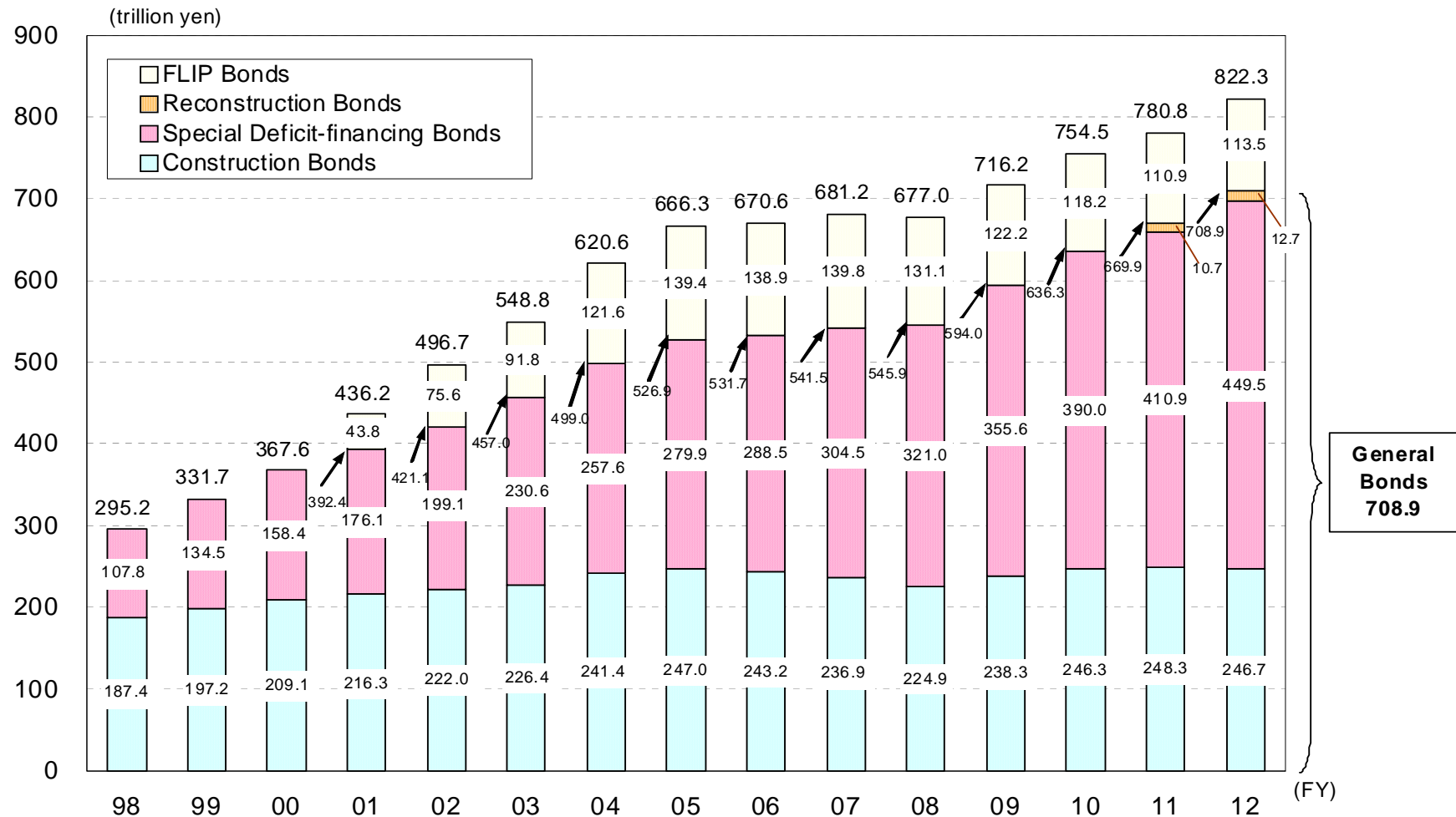
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October 12, 2012 (Fri)

Deputy Director-General of the Financial Bureau,
Ministry of Finance

Outstanding Government Bonds

- The government debt level is rising due to the increase in public work expenditures in 1990s, growing spending to fund the rising social security costs, and the falling tax revenues resulting from tax cuts and economic downturn
- In view of the substantial amount of JGBs outstanding, it is critical to ensure a stable issuance of JGBs



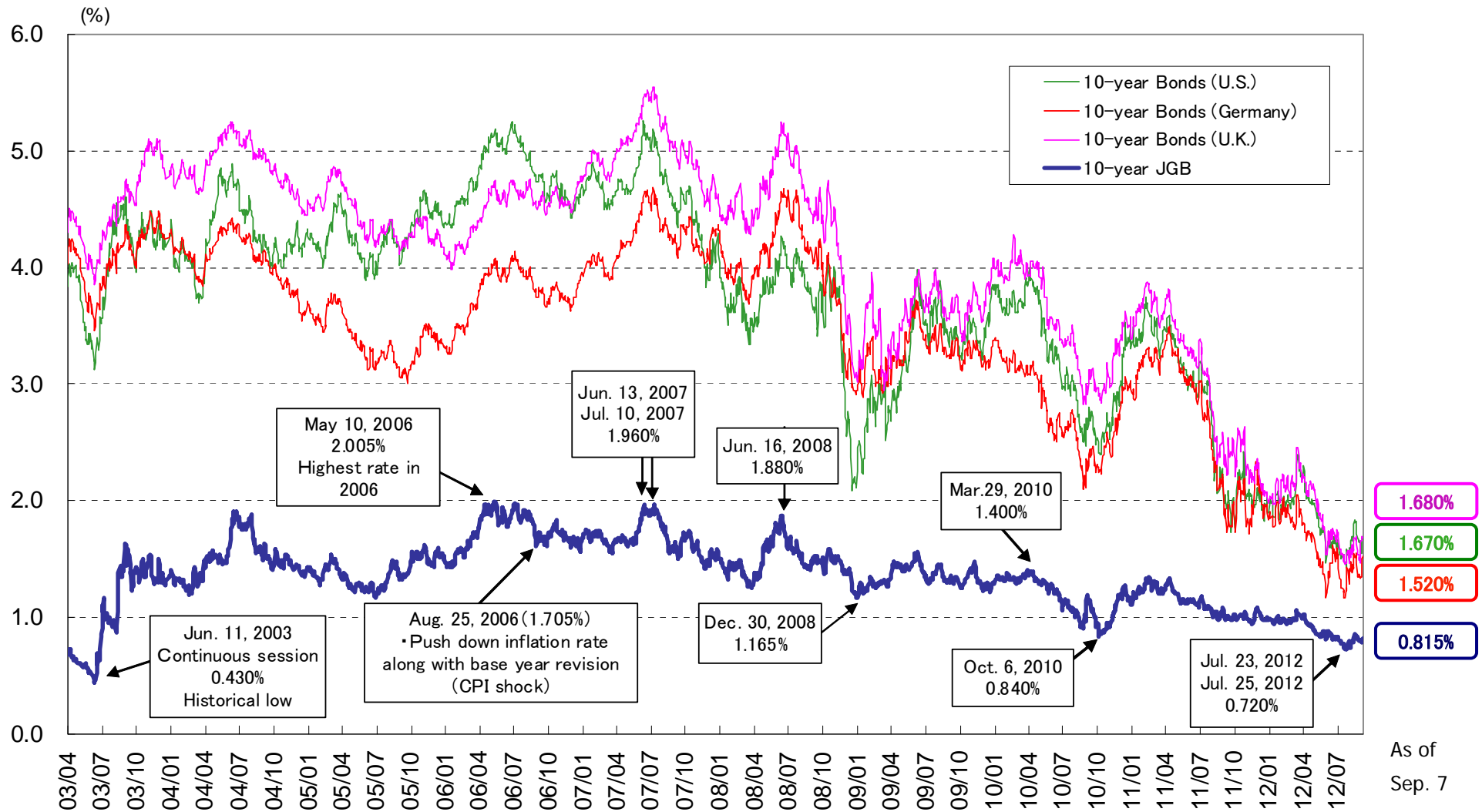
(Note1) Figures are based on nominal amount.

(Note2) FY2003 ~ FY2010 : Actual FY2011 ~ FY2012 : Estimates

(Note3) Special Deficit-financing Bonds include Refunding Bonds which were issued resulting from the takeover of debts transferred.

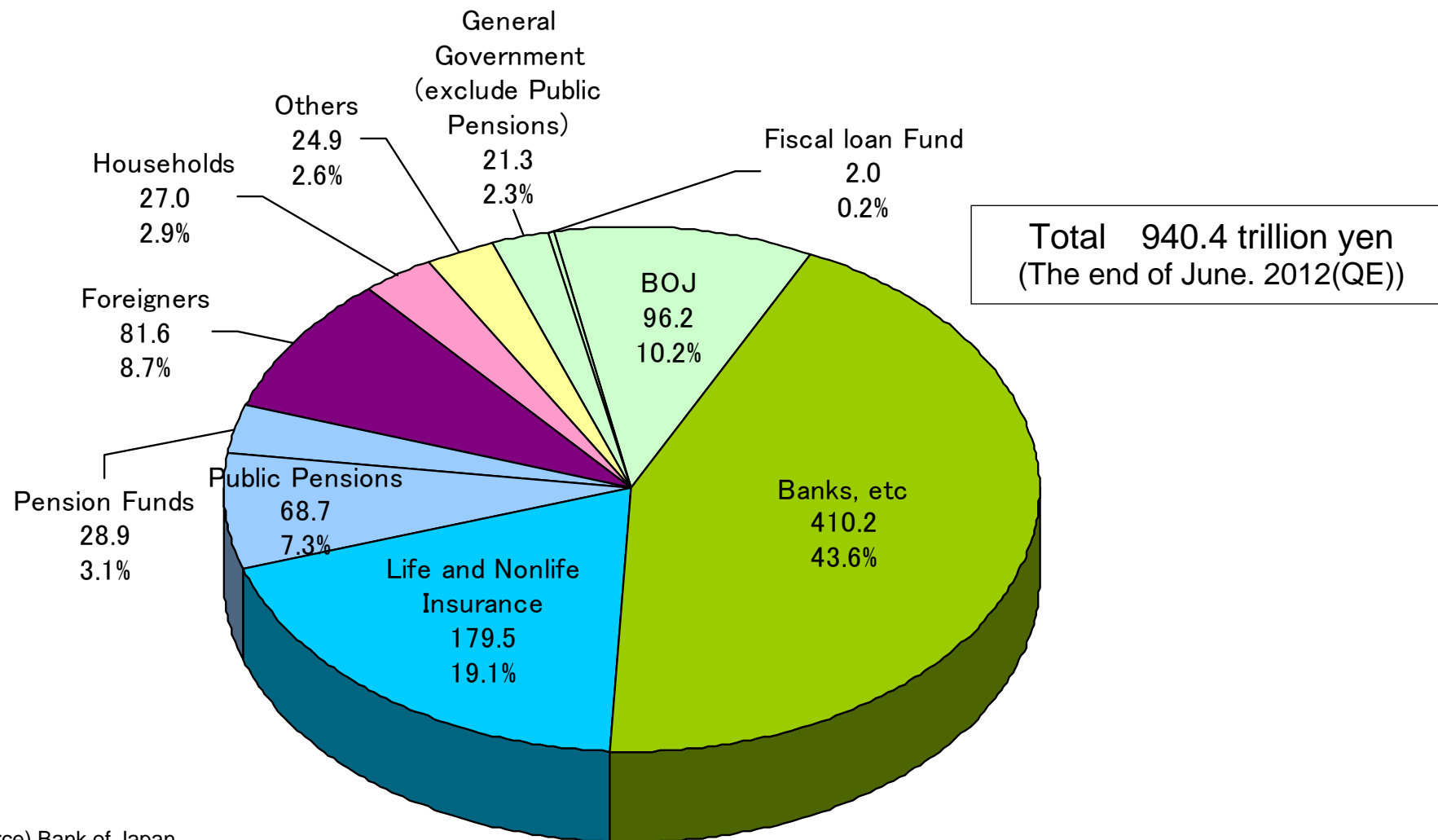
Long-Term Interest Rates

○ JGB long-term interest rates remain stable at low levels and reached the 0.7% level for the first time in 9 years since 2003, due to the strong investor demand for JGBs against the background of the European crisis and uncertainties surrounding the global economy.



Breakdown by JGB Holders

○ More than 90% of JGBs are held by domestic investors and backed by their abundant personal financial assets



(Source) Bank of Japan

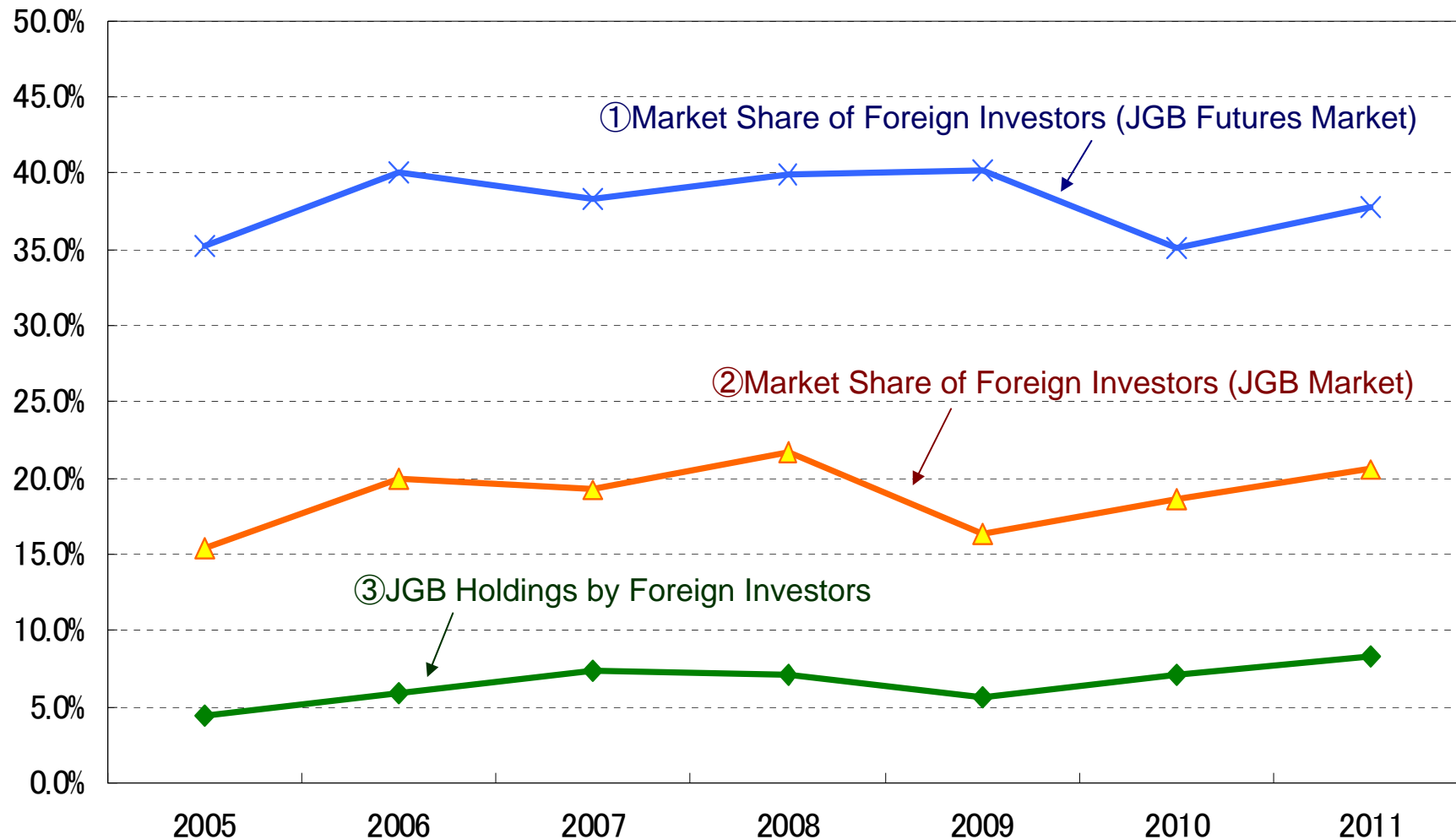
(Note1) "JGB" includes FILP Bonds and T-Bills.

(Note2) "Banks, etc." includes Japan Post Bank, "Securities investment trust" and "Securities Companies."

(Note3) "Life and Nonlife Insurance" includes Japan Post Insurance.

Foreign Investors' Presence

○ Foreign investors have a strong presence in the overseas market with a share of 20% of the JGB market and 40% of the JGB futures market



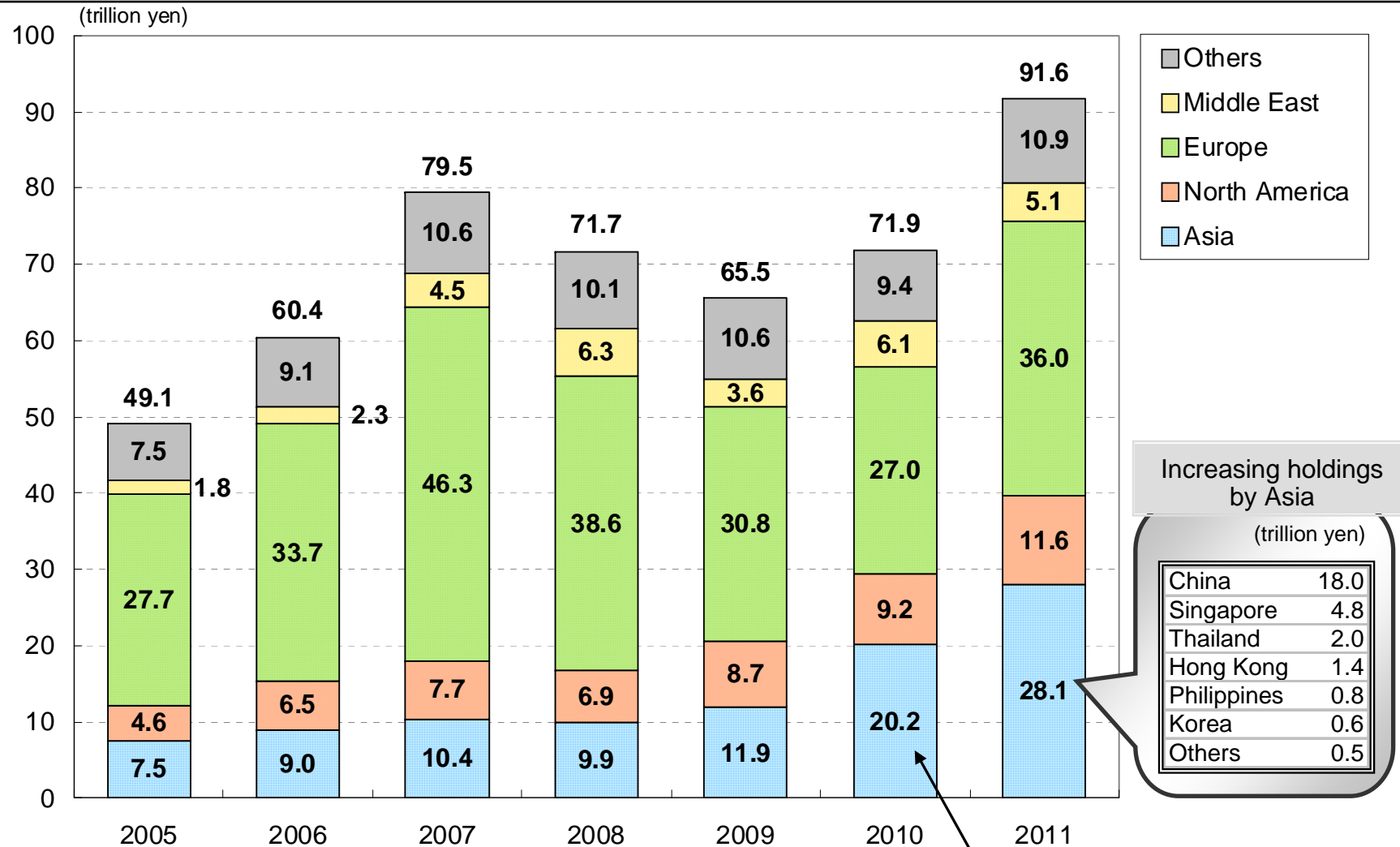
(Note1) Calendar base.

(Note2) "JGB" include T-Bills. The figures of ② excludes dealers' transactions.

(Source) Bank of Japan, Japan Securities Dealers Association, Tokyo Stock Exchange

Foreign Investors Bondholding by region

- Foreign (mainly Asian) investors have been increasing their JGB holdings
- China became the largest holder of JGB in 2010



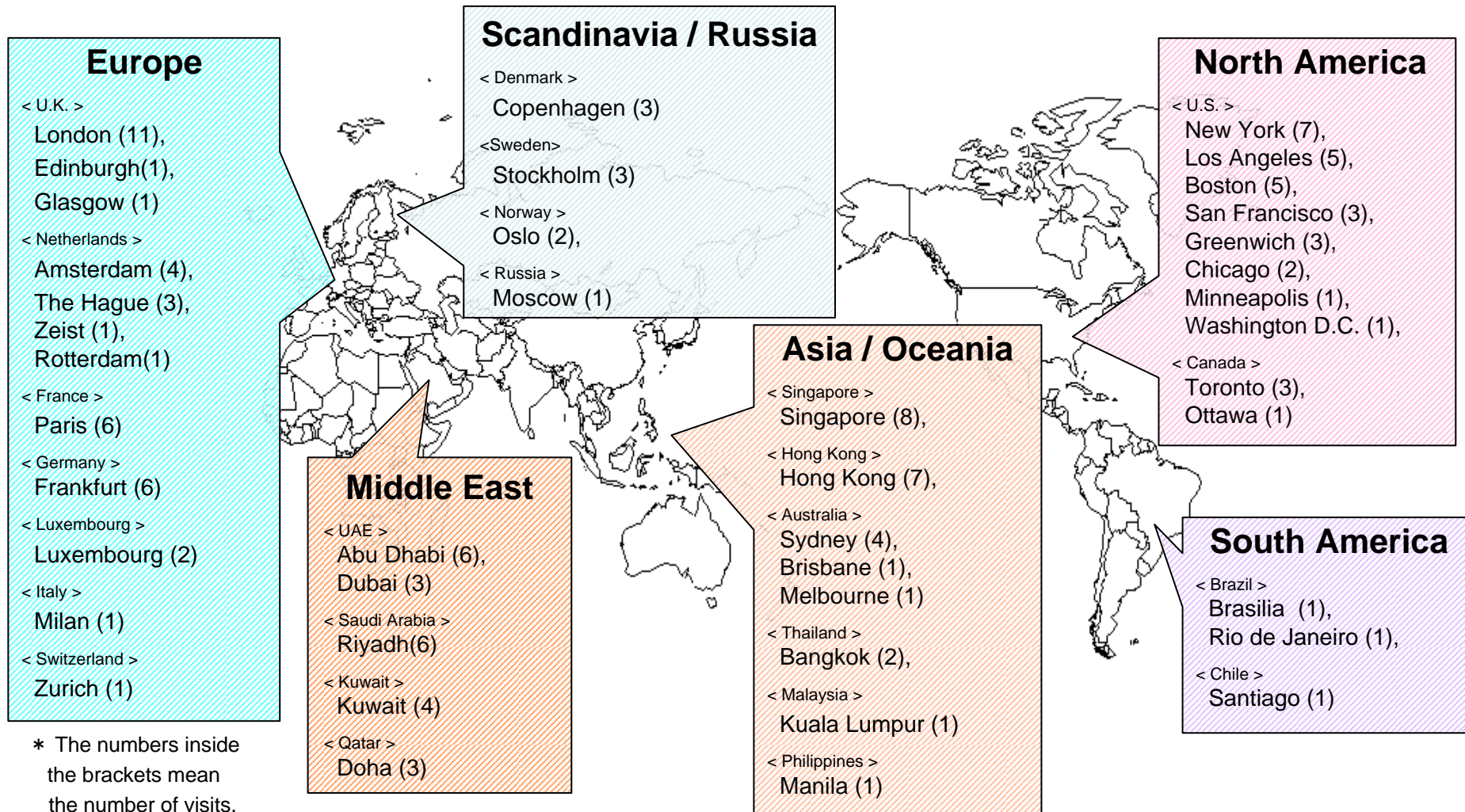
(Note) Figures includes bonds and bills other than JGB.

(Source) Bank of Japan, "Balance of Payments"

China became the largest bondholder in place of U.K.

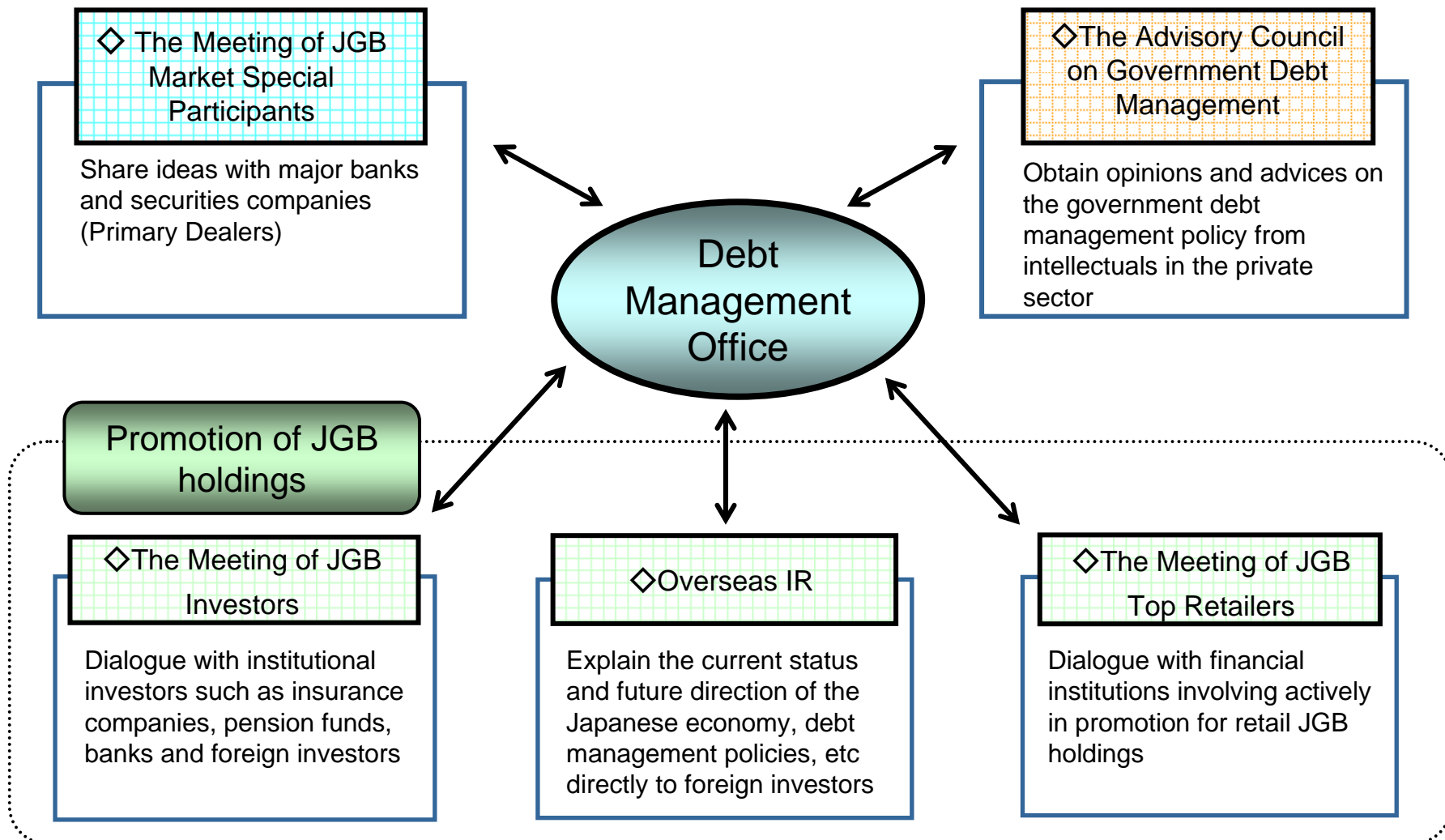
JGB IR Tours

○ JGB IR tours overseas are designed to assess market needs and maintain and enhance the confidence in JGB by providing existing foreign investors with accurate information about JGBs and the Japanese economy



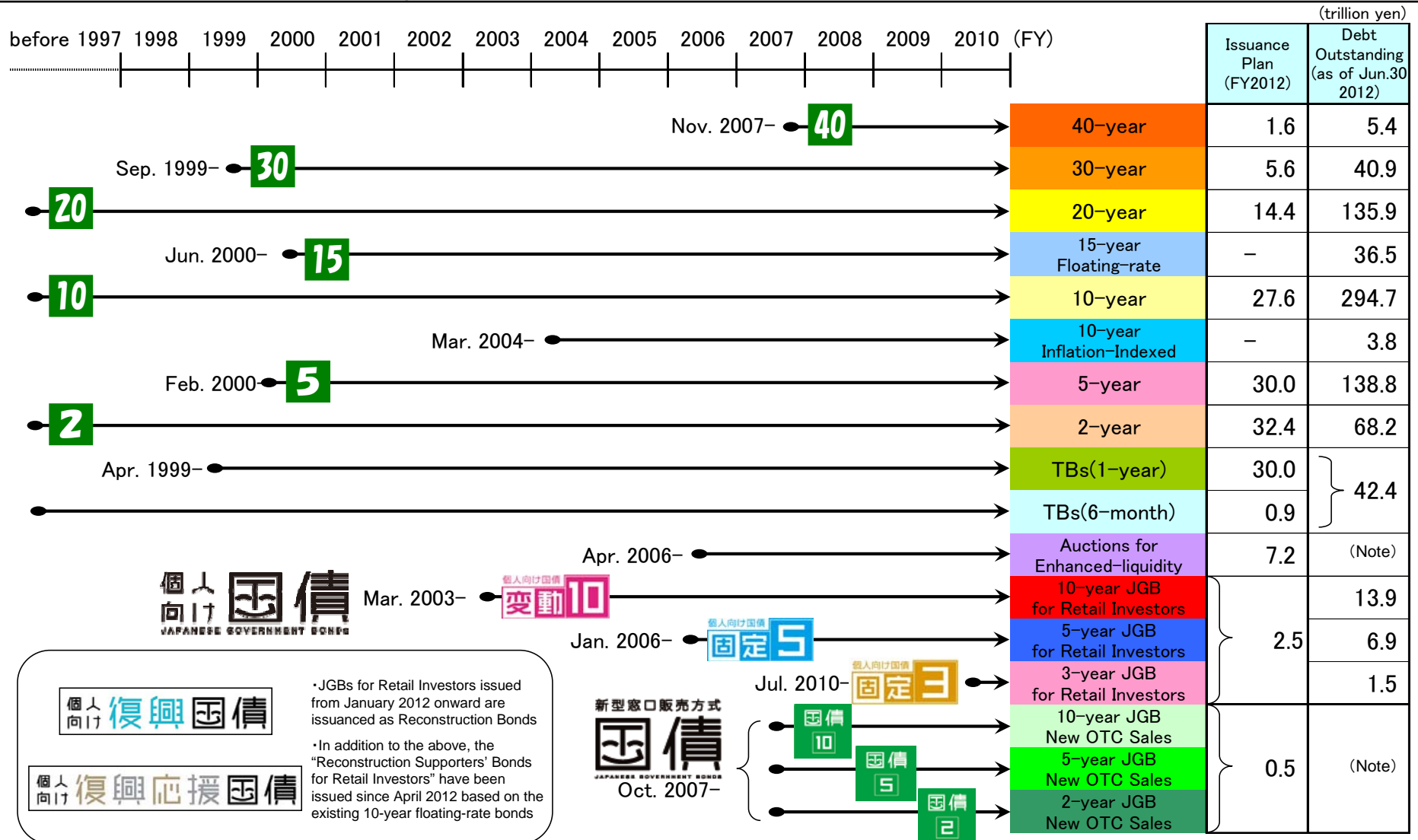
Dialogue with the Markets

- The MOF aims to promote the dialogue with the markets in order to assess market needs, ensure the stable JGB issuance, and implement appropriate policies to maintain and enhance the market liquidity of JGBs



Diversified JGB Product Portfolio

- The JGB product portfolio has been diversified to ensure stable issuance by assessing market needs and developing a deeper and wider investor base
- The 40-year bond was issued for the first time in 2007 to meet the needs from life insurance firms and pension funds
- In order to increase the JGB holdings by individual investors, we issue the JGBs for retail investors



個人向け復興国債
 個人向け復興応援国債

・JGBs for Retail Investors issued from January 2012 onward are issued as Reconstruction Bonds

・In addition to the above, the "Reconstruction Supporters' Bonds for Retail Investors" have been issued since April 2012 based on the existing 10-year floating-rate bonds

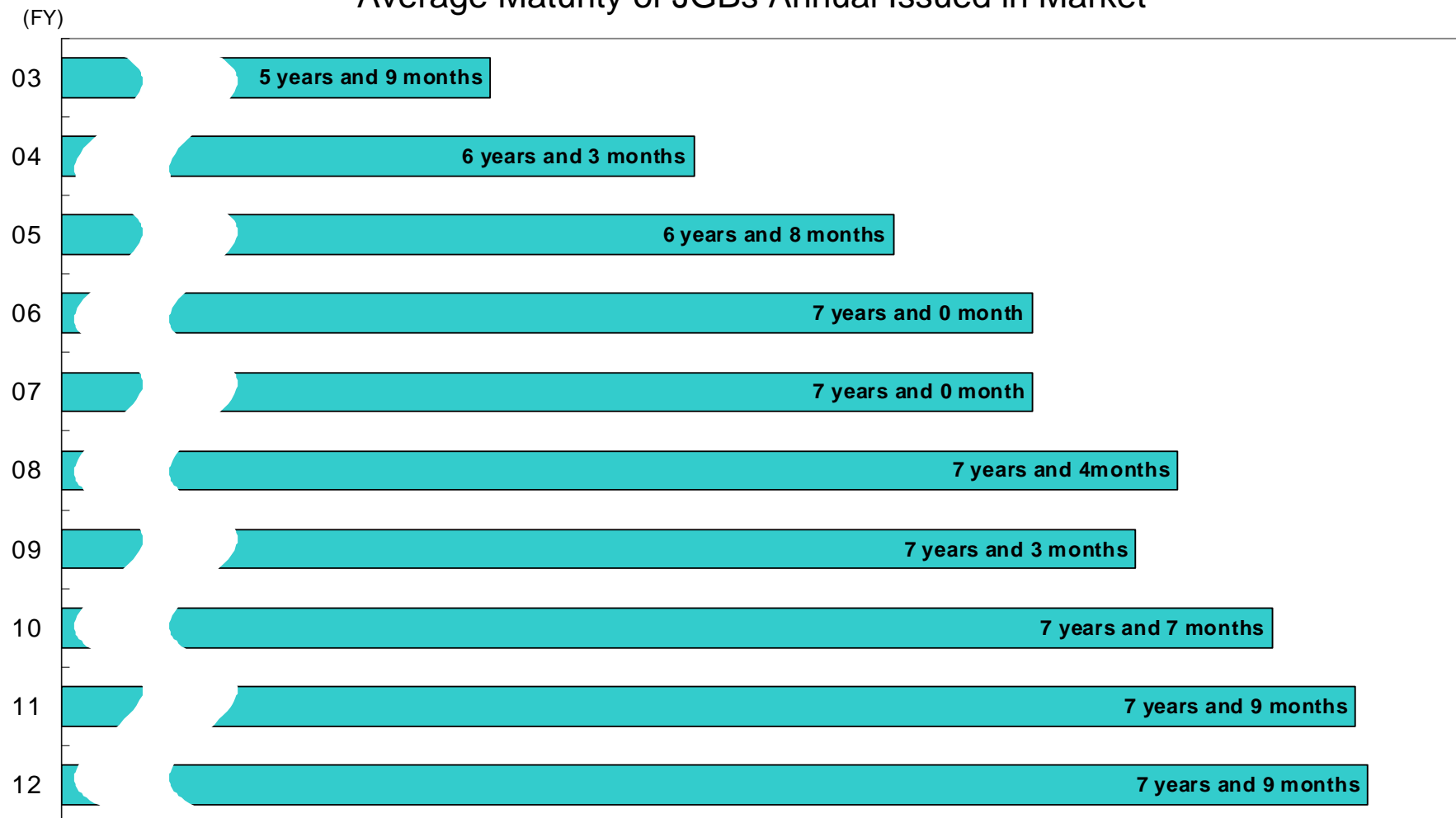
新型窓口販売方式
国債
 JAPANESE GOVERNMENT BONDS
 Oct. 2007-

(Note) The amounts of the Auctions for Enhanced-Liquidity and New OTC Sales are included in the amount issued through auction

Extending Average Maturity

- The average maturity has been extending as a result of the additional issuance of 10-year and 20-year bonds for the reduction of medium- to long-term refunding risk
- The extending average maturity and the diversified investor base play a part in the stable issuance of JGBs

Average Maturity of JGBs Annual Issued in Market



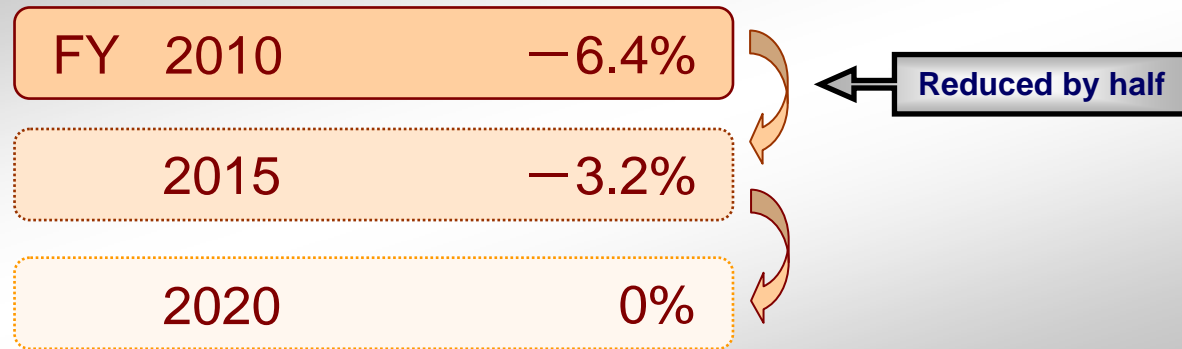
(Note) FY2005-2011: Actual figures, FY2012: Figure based on the initial issuance plan

Fiscal Consolidation Targets

- In order to facilitate fiscal rehabilitation and enhance market confidence, specific targets are set out for the primary balance (flow) and outstanding debt (stock) for each fiscal year

Flow

Consolidated Primary Deficit of National & Local Governments



Stock

Stable reduction of public debt ratio to GDP from FY 2021

Basic Rules on “Fiscal Management Strategy”

○ In order to ensure disciplined fiscal management, five basic rules have been established including the "pay-as-you-go" rule (new policies must be backed by revenue sources or reduction in expenditures)

1. Resource Assurance Rule (Pay-As-You-Go Rule)

Whenever policies that increase expenditure or reduce revenue are introduced, stable revenue sources must be secured by permanent reductions in expenditures or revenue-raising measures.

2. Fiscal deficit reduction rule

Fiscal condition must be steadily improved each year in order to achieve the flow targets.

3. Securing revenue sources for structural expenditures

Stable revenue shall be secured for structural expenditures such as social security costs required for pension and medical and care-giving benefits.

4. Basic principles for reviewing expenditure

Eliminate any unnecessary expenditure including those of the Special Accounts and drastically restructure the budget.

5. Stable management of local government finance

Both national and local governments will take measures for fiscal consolidation in mutual cooperation. The national government will not implement measures which transfers burden to local governments and hinders its autonomy.

Medium-term Fiscal Framework

- Establishing multi-year-indicative budgeting mechanism to accelerate the fiscal consolidation

Expenditure side

- FY2013–FY2015 Primary Balance Expenses shall be kept lower than 71 trillion yen (in substantial terms)

Bond issuance

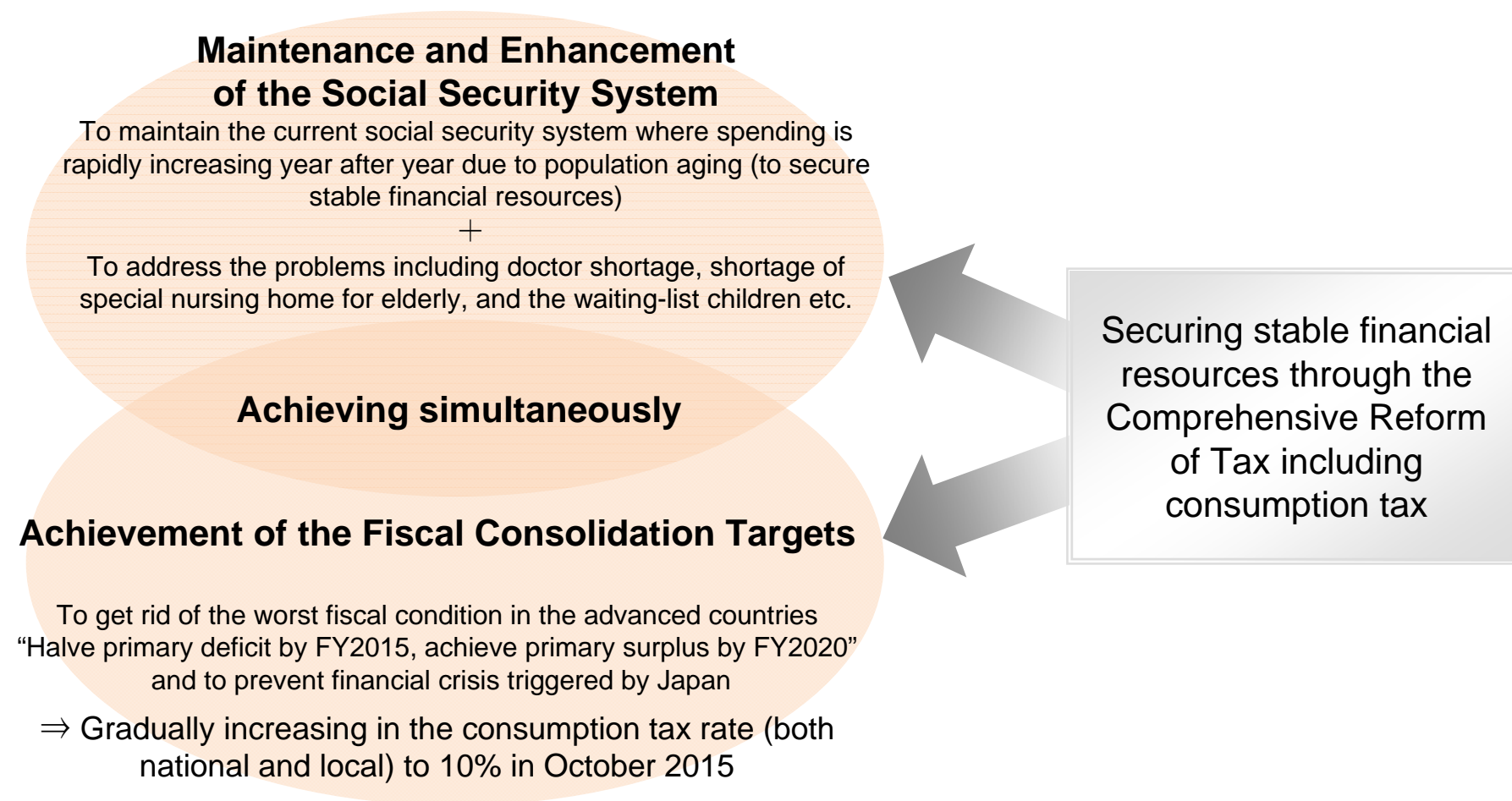
- The volume of public bond issues in FY2013 shall be kept lower than the initial FY2012 budget level (approx. 44 trillion yen) by utmost efforts
- The efforts shall be continued for FY2014 and thereafter (Excl. public bonds based on specific and legally-available repayment sources such as special pension-deficit financing bonds)

Revenue side

- The drastic tax reform must be proceeded based on the bills for the comprehensive reform of social security and tax and the Tri Party Agreement

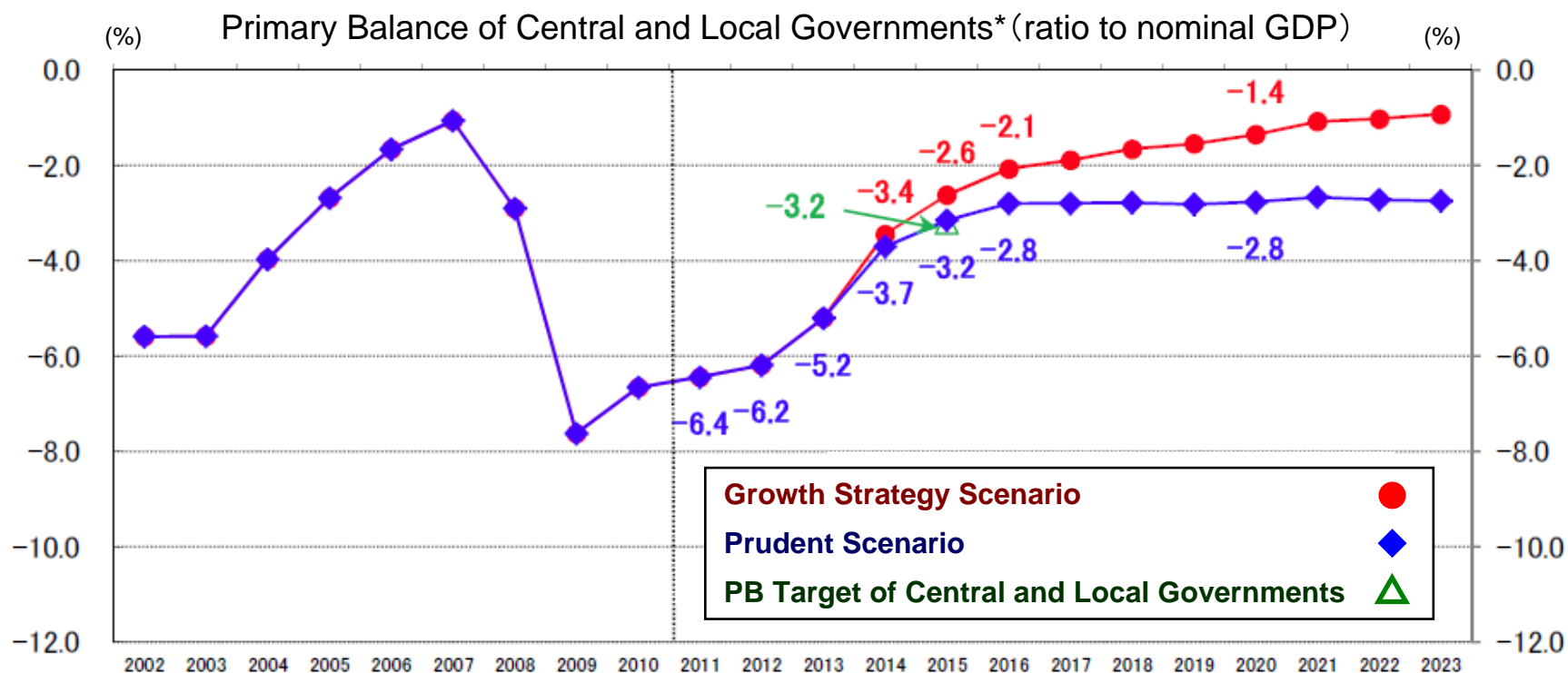
Promotion of Comprehensive Reform of Social Security and Tax

- Steady progress has been made in the efforts for the fiscal consolidation, including the enactment of the consumption tax increase (to 10% by October 2015) bill in August 2012



Load to Fiscal Consolidation in Terms of Primary Balance

- To ensure stable issuance of JGBs, the government needs to continue its fiscal consolidation measures and maintain market confidence
- The consumption tax hike and other fiscal measures will improve the primary balance and help the government to achieve its fiscal consolidation goal of reducing deficit by half by FY2015 from the FY2010 level



Growth Strategy Scenario : The average annual growth rate for the FY2011 – FY2020 period is approximately 3% in nominal and 2% in real terms.

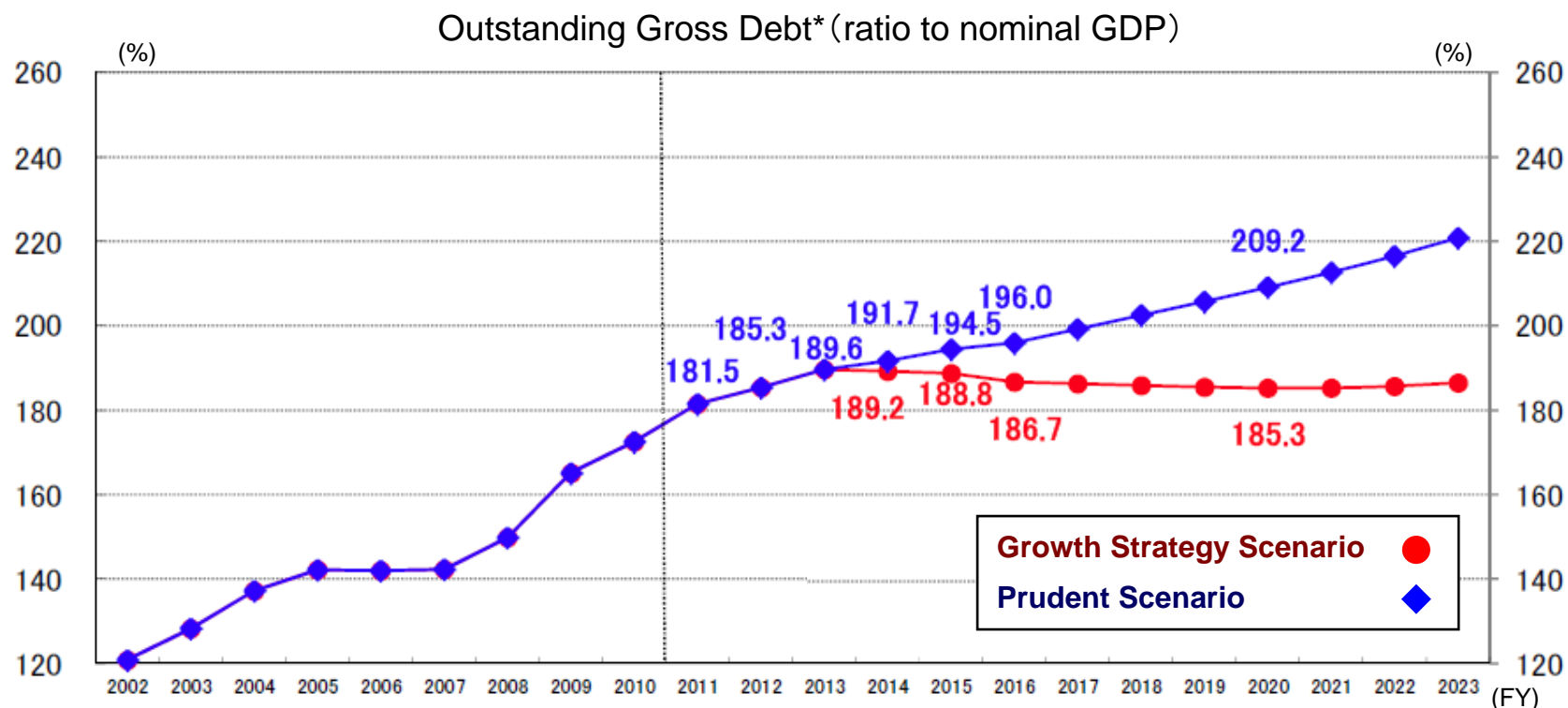
Prudent Scenario : The average annual growth rate for the FY2011 – FY2020 period is mid-1% in nominal and over 1% in real terms.

(Note*) Excluding the expenditures and fiscal resources for the recovery and reconstruction measures.

(Source) Cabinet Office “Economic and Fiscal Projections for Medium to Long Term Analysis” (August 31, 2012)

Load to Fiscal Consolidation in Terms of Outstanding Gross Debt

○ To ensure a stable decrease in the national & local debt/GDP ratio, further reforms will be necessary in addition to the consumption tax hike



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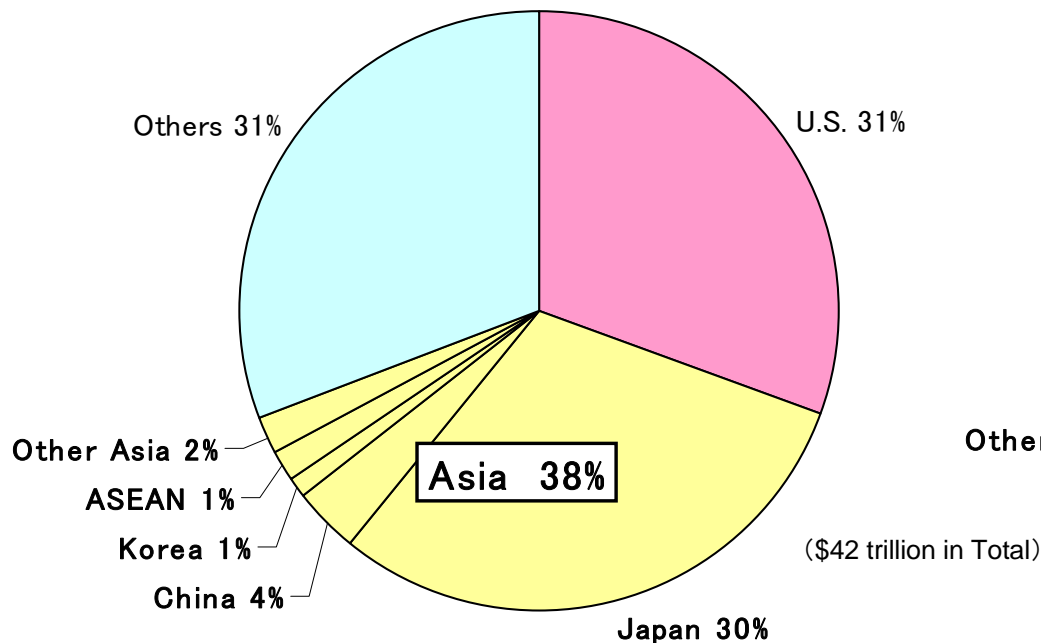
(Source) Cabinet Office “Economic and Fiscal Projections for Medium to Long Term Analysis” (August 31, 2012)

Position of JGB Market in Global Bond Market

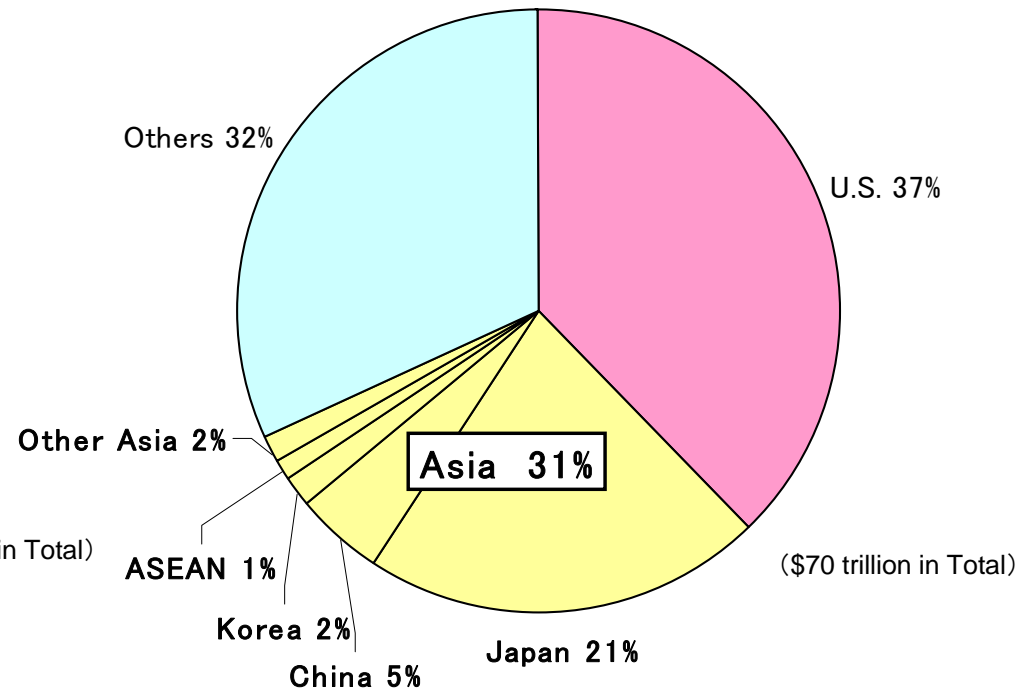
- The JGB market accounts for 30% of the global government bond market. It is one of the world's largest government bond markets along with the US treasury market
- Asian bond market (incl. China, Korea, and ASEAN) accounts for approx. 40% of the global government bond market. It is expected to increase its presence by Asian economic growth
- Stability and growth of the JGB and Asian bond markets is an important theme for the international financial market

Share of Secondary Market for Outstanding Bonds (End of 2011)

[Government Bonds]



[Public/Corporate Bonds]

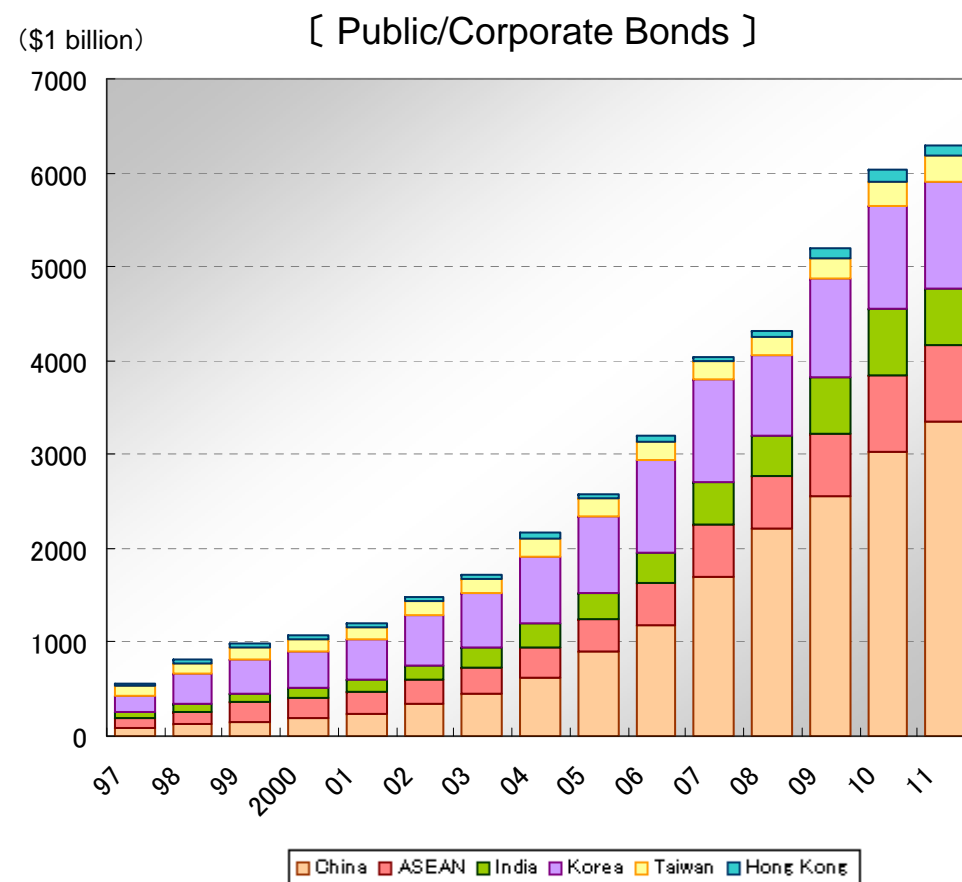
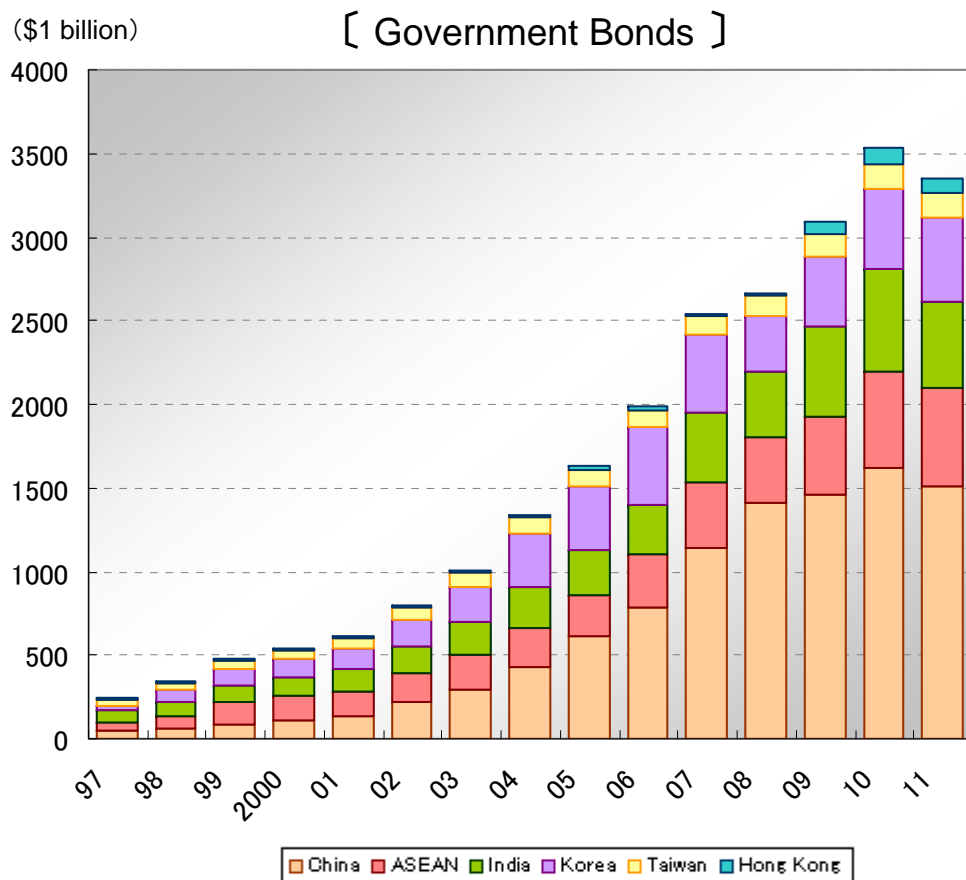


(Source) BIS, Asian Development Bank "Asian Bonds Online"

Growing Asian Bond Market

- The Asian Bond Market Initiative (ABMI) was launched in 2003 in the aftermath of the Asian financial crisis in 1997
- By 2011, Asian bond market increased its size approx. 15 times (from the 1997 level; excl. Japan)
Especially, Chinese market grew significantly and expanded approx. 30 times
- The JGB market plays a leading role as the largest market in Asia by providing settlement and other market infrastructure services and enhancing institutional frameworks

Amount Outstanding of Bonds Issued in Asian Market (Excl. Japan)



(Source) BIS, Asian Development Bank "Asian Bonds Online"

Japan's Contributions to Asian Bond Market Initiative (ABMI)

- Japan made the largest-scale investment of \$200 million in the ABMI activities in support of the issuance of local currency-denominated bonds
- Japan contributed to the issuance of local currency-denominated bonds and the expansion of the regional bond market through the ABMI activities

History

- In order to mobilize Asian savings to fund investments in the region, ASEAN + 3 (Japan, China, and Korea) finance ministers agreed to cooperate in the development of the Asian bond market (launch of ABMI) at the meeting held in Manila in August 2003

Japan's contributions

- Japan, along with China, made the largest-scale investment of \$200 million in the CGIF, a \$700 million fund established to support smooth issuance of local-currency denominated bonds in Asia
- Japan acted as the co-chair of multiple taskforces and led the discussions
- Japan provided technical assistance for the growth of the Asian bond market

ABMI's achievements

- Diversification of bond issuers and bond types
 - Issuance of local currency-denominated bonds by ADB and other international institutions and Japan's leading manufacturers and retailers
- Expansion of the intraregional bond market
 - The amount of bonds issued in the market increased from \$360 billion (1997) to \$5,487 billion (2011)
- Smooth issuance of bonds that were necessary to stimulate the post-Lehman-crisis economy

Japan's Contributions to Asian Bond Market

- Japan provides active support for the sound development of JPY- and RMB-denominated bond markets through purchasing Chinese government bonds
- As one of its important missions, Japan will assume a leadership role and make contributions to the development of the Asian bond market as a whole

Enhanced Cooperation for Financial Markets Development between Japan and China (December 25, 2012 Beijing)

- Supporting sound development of JPY and RMB bond markets
 - RMB-denominated bonds issued by Japanese companies in overseas markets
 - Application process is underway for the Japanese authority to invest in Chinese government bonds
- Encouraging the private sector to develop JPY-denominated and RMB-denominated financial products and services in the overseas markets

The Comprehensive Strategy for the Rebirth of Japan (Cabinet Decision on Jul. 31, 2012)

[Financial Strategy]

- Improvement of the Asian bond market
 - Establishment of the "Intraregional Shared Program for Bond Issuance";
 - Promotion of discussion on the intraregional bond settlement system
- Liberalization and deregulation of financial and capital markets in Asian countries
 - Target: Increase the size of the Asian bond market by half by 2015 (6 ASEAN countries; from the 2011 level)