

Recent Developments and Future Direction

A. Recent Major Developments

1. Japan Securities Clearing Corporation Merged with Japan Government Bond Clearing Corporation in October 2013

The merger between the Japan Securities Clearing Corporation (JSCC) and Japan Government Bond Clearing Corporation (JGBCC) took effect on 1 October 2013. JGBCC's OTC JGB clearing was amalgamated with JSCC's other clearing services. This combination of OTC JGBs, JGB futures, and interest rate swaps broadened JSCC's coverage of JPY-denominated bonds and interest rate products.

2. Shortening the Japanese Government Bond Settlement Cycle (T+1)

In November 2014, the Working Group on Shortening the JGB Settlement Cycle released the Grand Design for Shortening the JGB Settlement Cycle (T+1) to illustrate an overview of the policy for the domestic market participants to set T+1 as the standard settlement cycle for outright transactions of JGBs.⁵⁷

In June 2015, the Working Group on Shortening the JGB Settlement Cycle agreed to set the first half of FY2018 as the target implementation timing for T+1, based on the survey results from market participants. While transactions with nonresidents are outside the scope of the T+1 implementation, the Working Group will encourage market participants to take appropriate measures in accordance with the policy discussed by major market participants to enable a faster and smoother settlement administration.⁵⁸

3. Japanese Securities Depository Center Upgrades Book-Entry System and Adopts ISO20022 Standards

In January 2014, JASDEC adopted a Pre-Settlement Matching System and Book-Entry Transfer System based on ISO20022 standards, the next-generation international standard message format.

Also in January 2014, JASDEC further enhanced settlement safety by introducing delivery-versus-payment (DVP) settlement for stock lending transactions to reduce settlement risk relating to stock lending and borrowing transactions, which can also be used for corporate bonds.

⁵⁷ Outline of the Grand Design for Shortening the JGB Settlement Cycle (T+1): http://market.jsda.or.jp/shiraberu/saiken/kessai/jgb_kentou/files/grand-design_english.pdf

⁵⁸ Target Implementation Timing for Shortening the JGB Settlement Cycle to T+1: http://www.jsda.or.jp/en/newsroom/researches-studies/files/Target_Implementation_Timing.pdf

4. ASEAN+3 Multi-Currency Bond Issuance Framework Pilot Issuance Listed on TOKYO PRO-BOND Market

Please also see the reference to the purpose of the AMBIF and resulting opportunities for the Japan bond market in Chapter IX.J.

On 28 September 2015, the TSE, part of the JPX Group and the operator of the TPBM, approved the listing of the first AMBIF bond issued in ASEAN+3. Figure 28 provides a screenshot of the announcement on the JPX website.



The listing of this bond issued in Thailand also represents the first listing of THB-denominated debt securities on TPBM. For further information on the listing process on the TPBM, please refer to Chapter III.H.

5. Launch of New Bank of Japan Financial Network System in October 2015

The BOJ launched a completely updated version of its Bank of Japan Financial Network System (BOJ-NET) on 13 October 2015. BOJ-NET, which began operations in 1988, supports two separate services, the BOJ-NET funds transfer services, and the BOJ-NET JGB services for the settlement of government bonds.

Among its many features, the new BOJ-NET contains the following three significant distinguishing features:

- (i) use of the latest information technology infrastructure and standards including the adoption of the XML message format and the ISO20022 standard for greater interoperability with other market institutions;

- (ii) high flexibility to adapt to changes in financial services and the various needs of its participants and stakeholders; and
- (iii) enhanced accessibility to cope with changes in the financial environment, such as the globalization of financial transactions and the networking of settlement infrastructures.

As a result, financial institutions using the new BOJ-NET system are expected to improve their collateral and cash management efficiency, and achieve smoother settlement of JGBs. In addition, the new BOJ-NET allows BOJ to extend operating hours until 9 p.m., effective 15 February 2016. This gives the Japanese market a longer overlap time with the operating hours of international markets and encourages smoother cross-border settlement of Japanese yen and JGBs.

B. Future Direction

1. Enhancement of the Repo Market and Its Infrastructure

To vitalize the corporate bond secondary market, it is necessary to develop and enhance infrastructure and market features such as the corporate bond repo market and the corresponding clearing and settlement functionality. Such efforts are also likely to contribute to the expansion of the primary market.

Although the corporate bond repo market is expected to work as a financing and fund management tool for market participants and, potentially, even as a means of avoiding settlement failures, the drive for repo transactions is hampered by the fact that investors buy to hold, with only a small portion of the issuance volume remaining in the market for trading.

The JSDA and market participants are engaged in discussions on how to enhance the securities settlement service functions in advance based on the corporate bond repo market and the lending functions in Europe and the US in order to cope with the anticipated growth in issuance size and the expanding needs of corporate bond repo transactions in the future.

2. Enhancement of Functions of Settlement and Clearing Systems

A clearing house is an indispensable tool to mitigate settlement risk, improve efficiency for investors and market participants, and ensure liquidity. However, as the issuance sizes of and transactions in the corporate bond market are limited and the netting effect of corporate bonds would not be significant, the JSDA and market participants have not yet established a clearing agency like the one that exists for government bonds. Market participants need to hold discussions about the establishment of a clearing house for corporate bonds and other functional enhancements of a settlement and clearing system for corporate bonds in order to meet the anticipated growth in issuance size and other factors, including risk mitigation and regulatory requirements, that point to the need for a clearing house.

3. Promotion for Issuance and Intraregional Distribution of Foreign-Currency-Denominated Bonds Issued in the Tokyo Market

For the development of the bond market, the promotion of the issuance and intraregional transactions of foreign-currency-denominated bonds issued in the Tokyo market is an important issue.

For the smooth issuance and distribution of the foreign-currency-denominated bonds issued in the Tokyo market, it is important to be able to achieve DVP settlement for investors. In Japan, in the case of JPY-denominated bonds, DVP settlement is already possible by linking the securities transfer through JASDEC and the yen settlement through the BOJ.

Also, in overseas markets, international CSDs can provide the settlement function of foreign currency funds together with the securities settlement function. By doing so, they can achieve DVP settlement of foreign-currency-denominated bonds. However, JASDEC is currently not able to support such a function.

In Japan, private financial institutions already offer a settlement function for foreign currency funds. However, the full DVP settlement function for foreign-currency-denominated bonds issued in the Tokyo market has not been realized yet.

Taking into consideration the above mentioned points, and toward promotion of foreign-currency-denominated bonds issued and distributed in the Tokyo market, there will be a need to continue discussions and seek a better solution among market participants and related institutions.

4. Effective Use of New Bank of Japan Financial Network System

Please also refer to the information on the implementation of the new BOJ-NET system in section A.6 in this chapter.

The comprehensive implementation of various international regulations would generally increase demand for collateral, particularly for high-quality collateral assets that are typically government bonds such as JGBs or very high-quality corporate bonds. For example, demand for high-quality liquid assets is expected to increase as a result of the introduction of the Liquidity Coverage Ratio, which took effect in January 2015. As for the regulations for OTC derivatives transactions, mandatory central clearing of standardized OTC derivatives transactions would increase demand for collateral to be posted to central counterparties. In addition, margin requirements for non-centrally cleared derivatives, which took effect in December 2015, are very likely to increase the total amount of posted collateral and have a significant operational impact because of the resulting frequent deliveries of collateral.

As previously explained, it is becoming increasingly important to optimize the use of collateral across borders and to move collateral flexibly. Under these circumstances, enabling greater use of JGBs as prime high-quality collateral assets both in Japan and abroad will benefit not only financial institutions in Japan but also financial institutions elsewhere and, ultimately, the global financial system.

The recent launch and the extended operating hours of the New BOJ-NET system will help facilitate the use of JGBs as high-quality collateral assets worldwide.