I

Overview

A. Introduction

The Government of Japan raises significant amounts from domestic capital markets to finance government expenditures, mainly through the issuance of Japanese Government Bonds (JGBs) and Treasury Discount Bills (Treasury Bills and Financial Bills, collectively T-Bill). These funding activities have been supported by a large and diverse community of domestic and overseas investors and intermediaries.

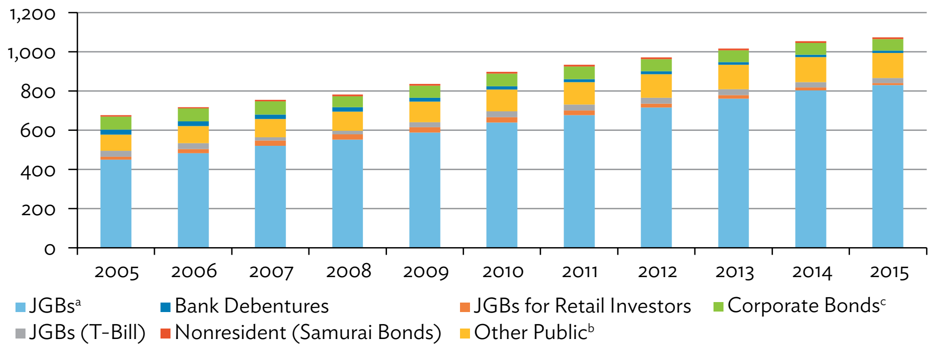
Japan offers a wide range of financial tools to meet a range of issuer and investor requirements. Aside from traditional bank instruments (e.g., loans), corporate bonds, commercial paper, and securitized products are also available in Japan's credit market. Securities lending and securities financing are also established. Various credit risks are pooled through securitized products, with the value of the underlying assets exceeding the risks taken by investors.

Among the major market participants in Japan's bond market are domestic and foreign securities companies that serve as dealers, brokers, traders, and underwriters in the primary and secondary markets. Local governments, government agencies, and local public corporations are the largest issuers of government bonds in the market excluding JGBs. The majority of JGB holders are from the public sector, commercial banks, and insurance companies.

The amount of outstanding bonds in the government bond sector has expanded enormously over the past 2 decades (Figure 1 and Table 1).

During the period 2005–2008, JGB issuance was on the decline as the central government's financial position improved. However, the economic slump that followed the Lehman shock in September 2008 led to a deterioration in the government's finances and an increase in issuance (Figure 2 and Table 2).

Figure 1: Publicly Offered Bonds Outstanding (JPY trillion)



JGB = Japanese Government Bond.
[a] Excluding JGB holdings of the Bank of Japan.
[b] "Other Public" refers to local government bonds and government agency bonds.
[c] "Corporate" includes asset-backed bonds and convertible-type bonds, and does not include commercial paper.
Note: Data as of end of December for each calendar year.
Source: Japan Securities Dealers Association. http://www.jsda.or.jp/shiryo/toukei/hakkou/files/hakkougakushoukanngaku.xls

Table 1: Publicly Offered Bonds Outstanding (JPY trillion)

	2005	2006	2007	2008	2009	2010	2011	2012	2013	2014	2015
JGBs[a]	448.8	482.2	520.1	551.7	587.3	638.6	676.9	715.3	760.7	802.7	830.0
JGBs for Retail Investors	15.3	22.0	26.5	27.5	27.7	27.2	23.4	20.3	17.8	14.9	11.2
JGBs (T-Bill)	30.3	29.0	16.8	17.1	25.4	30.0	30.0	30.0	30.0	28.1	25.7
Other Public[b]	82.9	88.1	94.4	99.1	105.8	111.5	115.3	121.1	126.0	127.8	128.0
Bank Debentures	25.8	23.4	22.2	21.3	19.4	17.2	15.2	14.0	12.5	11.8	11.4
Corporate Bonds[c]	66.5	66.6	67.8	56.9	61.4	63.8	63.6	62.4	61.5	60.4	58.4
Nonresident (Samurai Bonds)	6.9	6.4	7.6	9.1	8.9	9.3	9.8	9.3	8.8	9.2	9.1
Total[d]	676.4	717.7	755.4	782.7	835.9	897.6	934.2	972.3	1,017.3	1,054.9	1,073.8
JGB Holdings of the BOJ[a]	180.0	161.4	138.6	109.7	88.2	81.0	66.6	59.2	52.3	34.4	27.6

BOJ = Bank of Japan, JGB = Japanese Government Bond.
[a] Excluding JGB holdings of the BOJ.
[b] "Other Public" refers to local government bonds and government agency bonds.
[c] "Corporate" includes asset-backed bonds and convertible-type bonds, and does not include commercial paper.
[d] Outstanding value of privately offered bonds and notes may not be included.
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Source: Japan Securities Dealers Association. http://www.jsda.or.jp/shiryo/toukei/hakkou/files/hakkougakushoukanngaku.xls

Figure 2: Issuance of Publicly Offered Bonds (JPY trillion)

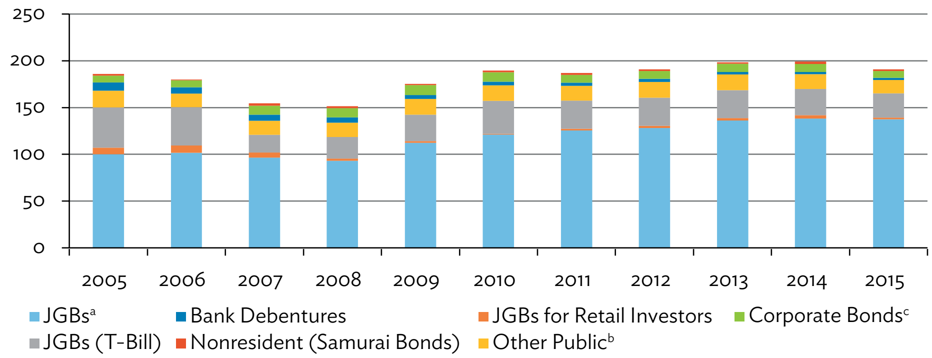

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Table 2: Issuance of Publicly Offered Bonds (JPY trillion)

	2005	2006	2007	2008	2009	2010	2011	2012	2013	2014	2015
JGBs[a]	100.1	101.8	96.4	93.2	112.4	121.1	125.5	128.2	136.3	138.3	137.4
JGBs for Retail Investors	7.1	7.6	5.6	2.3	1.6	0.9	1.9	2.4	2.4	3.5	1.9
JGBs (T-Bill)	42.9	41.0	18.8	23.1	28.4	35.0	30.0	30.0	30.0	28.1	25.7
Other Public[b]	17.9	14.6	15.0	15.3	16.8	16.7	15.7	16.9	16.8	15.6	14.3
Bank Debentures	8.8	6.7	6.5	5.5	4.2	3.8	3.4	3.2	2.6	2.5	2.5
Corporate Bonds[c]	7.4	7.5	9.6	9.9	10.6	10.1	8.5	8.4	8.8	8.5	7.1
Nonresident (Samurai Bonds)	1.6	0.8	2.6	2.1	1.2	1.9	2.0	1.7	1.6	2.5	1.9
Total[d]	177.6	168.1	152.9	147.0	178.1	183.7	185.1	190.8	198.4	199.0	190.8
JGB Holdings of the BOJ[a]	44.3	31.7	23.5	11.1	10.6	9.8	10.4	14.1	14.8	9.5	11.4

BOJ = Bank of Japan, JGB = Japanese Government Bond.
[a] Excluding JGB holdings of the BOJ.
[b] "Other Public" refers to local government bonds and government agency bonds.
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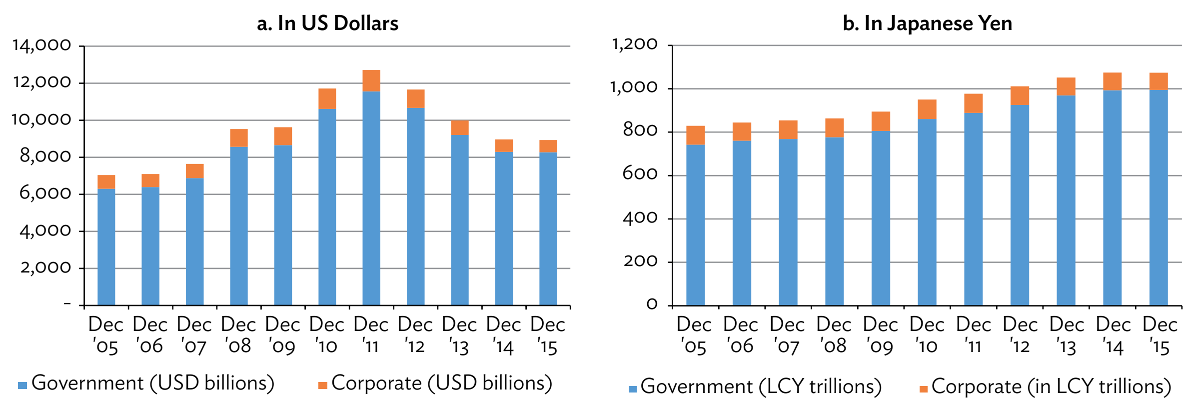
Note: Data shown for each calendar year
Source: Japan Securities Dealers Association. http://www.jsda.or.jp/shiryo/toukei/hakkou/files/hakkougakushoukanngaku.xls

The amount of bank debentures issued in 2015 stood at JPY2.5 trillion, down from JPY21.0 trillion in 2000. This decline suggests that Japanese industry's dependency on long-term credit from banks as a source of long-term capital came to an end in the first half of the 2000s, and also points to the weakness in financing for the private sector as a whole during the review period.

The total volume of publicly offered corporate bonds excluding commercial paper amounted to JPY7.1 trillion in 2015, remaining below the JPY10 trillion level for the fifth consecutive year and comprising less than 4% of total publicly offered bonds. Meanwhile, after being depressed in the aftermath of the Argentine government's default in 2002, the issuance of JPY-denominated foreign bonds (Samurai Bonds issued by nonresidents) has been steadily recovering. Today, JPY-denominated foreign bonds are once again used as an important financing source for foreign issuers due to their need to diversify currency risks.

Figures 3: Local Currency Bonds Outstanding—US Dollars versus Japanese Yen

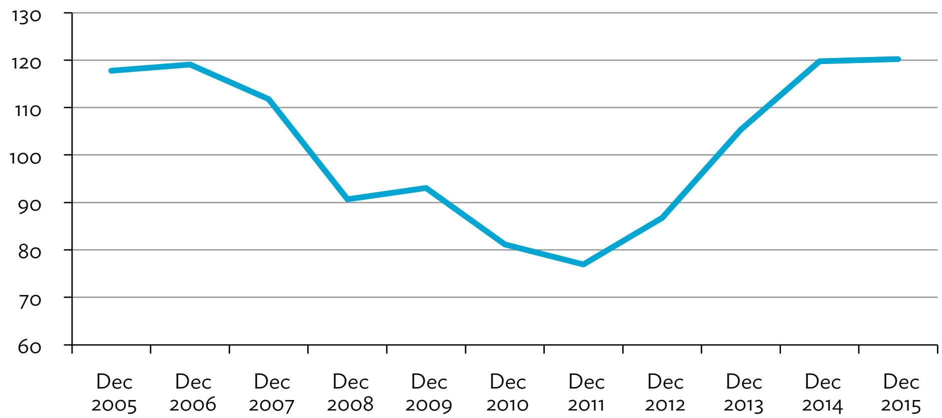


LCY = local currency.
Source: *AsianBondsOnline.*

Influence of Fluctuations in the JPY–USD Exchange Rate

According to data available on *AsianBondsOnline*, the total amount of local currency (LCY) bonds outstanding in the Japanese bond market was JPY1,074 trillion (USD8,931 billion) at the end of December 2015. Figure 3 shows total outstanding amounts denominated in US dollars and Japanese yen, respectively, between December 2005 and December 2015. It is significant that these graphs are based on the same LCY bond volumes, yet they have entirely different shapes due to the influence of fluctuations in the JPY–USD exchange rate (Figure 4).

Figure 4: Japanese Yen–US Dollar Exchange Rate



Source: ABMF SF1 based on data from *AsianBondsOnline*.

B. Liquidity-Enhancing Measures in the Japanese Government Bond Market[1]

In realizing the basic objectives of the Debt Management Policy—ensuring stable and smooth issuance of JGBs and minimizing medium-to-long-term financing costs—the issuing authorities have a keen interest in whether the JGB market has sufficient liquidity to enable transactions to be conducted freely in accordance with market participants' interest rate forecasts and investment strategies.

The JGB secondary market consists of brokers such as JGB Market Special Participants, who are also known as Primary Dealers, and investors. Basically, the maintenance and enhancement of liquidity should be achieved by the autonomous functioning of the market, which is stimulated by active transactions among such market participants. Consequently, the Ministry of Finance Japan's (MOF) Debt Management Office should support this autonomous functioning by arranging the appropriate amounts and maturities for auctions, and reopening issues in the primary market as needed.

In March 2001, the immediate reopening rule was introduced to principally treat a new JGB issue as an addition to an outstanding issue immediately from the issuance day if the principal and interest payment dates and coupon rate for the new issue are the same as those for the outstanding issue. In line with the immediate reopening rule, accrued interest emerges on new JGB issues. Accrued interest is a distinct practice in the trading of coupon bonds, and represents the interest accumulated since the last coupon payment date. When buying JGBs, investors pay the accrued interest for the period since the last coupon payment to sellers.

Under the JGB Issuance Plan for fiscal year (FY) 2014 (1 April–31 March), the central government increased the monthly size of JGB issuance through Auctions for Enhanced Liquidity by JPY100 billion and the overall JGB issuance through such auctions by

[1] Excerpts from the Ministry of Finance Japan's FY2014 debt management policies are available at https://www.mof.go.jp/english/jgbs/publication/debt_management_report/2014/saimu1-1-1.pdf

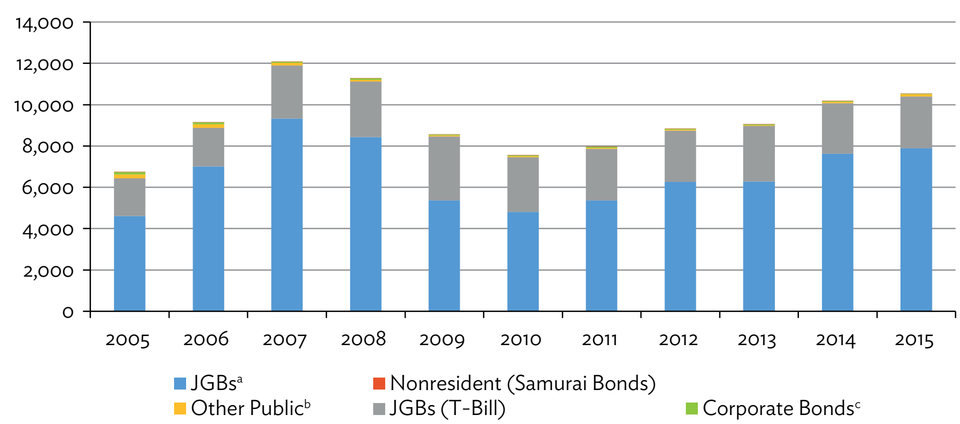
JPY1.2 trillion–JPY8.4 trillion. The coverage of such auctions is expanded to include all issues maturing in more than 5 years, other than on-the-run issues. Furthermore, JGB Market Special Participants are each required to make a bid for 3% or more of a planned issuance amount.

In FY2014, the government subjected 20-, 30-, and 40-year JGB issues to reopening in principle to secure market liquidity for each issue. As for 10-year JGBs, the government decided to adopt reopen issuances in April and May in cases where the spread between the coupon rate of the new bond being issued and the market JGB yield as of the auction date was less than 20 basis points.

C. Secondary Market Overview

Most Japanese domestic investors tend to hold bonds and notes until maturity. The selling of bonds and notes for switching, profit-taking, and loss-cutting is generally undertaken by institutional investors. With the exception of the impact of the global financial crisis, recent years have seen bond trading volumes in the secondary market continuously increase (Figure 5 and Table 3).

Figure 5: Trading Volume of Publicly Offered Bonds (JPY trillion)



JGB = Japanese Government Bond.

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Note: Data shown for each calendar year

Source: Japan Securities Dealers Association. http://www.jsda.or.jp/shiryo/toukei/hakkou/files/hakkougakushoukanngaku.xls

Table 3: Trading Volume of Publicly Offered Bonds (JPY trillion)

	2005	2006	2007	2008	2009	2010	2011	2012	2013	2014	2015
JGBs[a]	4,611	7,010	9,335	8,438	5,374	4,806	5,362	6,263	6,275	7,626	7,894
JGBs (T-Bill)	1,818	1,872	2,555	2,681	3,084	2,647	2,498	2,476	2,694	2,449	2,500
Other Public[b]	193	163	127	89	50	49	50	48	41	51	107
Corporate Bonds[c]	122	98	73	73	49	47	50	54	45	49	31
Nonresident (Samurai Bonds)	15	10	7	7	6	5	4	3	3	6	6
Total[d]	6,758	9,153	12,097	11,288	8,563	7,553	7,964	8,844	9,058	10,182	10,536

JGB = Japanese Government Bond.
[a] Excluding JGB holdings of the Bank of Japan.
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[d] Outstanding value of privately offered bonds and notes may not be included.
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The increase in the trading volume of JGBs during the period 2005–2015 can be explained by a number of factors. Firstly, the government continued to issue massive amounts of JGBs during the review period, resulting in a large increase in the size of the JGB market. Secondly, brokers, dealers, and other financial institutions such as banks actively dealt in bonds and notes for trading gains. Thirdly, the government started to auction T-Bill, which are now actively traded by market participants with short-term cash management needs. “T-Bill” is the sum of “Treasury Bills (TBs)” and “Financial Bills (FBs)” with a maturity of 1 year or less and TBs and FBs have been jointly issued since February 2009. Fourthly, the growing so-called flight-to-quality trend among domestic and foreign investors has also played a significant part. Over the past several years, the movement into the JGB trading market was prompted by a worsening in the worldwide investment environment against the backdrop of prolonged economic stagnation and recurring turmoil in global financial markets.

Additionally, government securities significantly outweigh other categories of bonds in overall fixed-income trading volume. The dominance of government debt stems mostly from the difference in liquidity, which in turn is because the major market participants are Japanese banks with tremendous excess cash and a preference for outstanding liquidity given the Bank for International Settlement’s zero-risk weighting of Japanese government debt.

D. Japanese Government Bond Market

Amid the continued massive issuance volumes of JGBs, the proportion of bond issuance made through public auctions that more closely reflect market conditions has steadily increased under a market-oriented national debt management policy. This replaced the previous emphasis on noncompetitive, syndicated underwriting, where issue terms were based on the official discount rate or other benchmarks.

As far as the 10-year JGB is concerned, the syndicated underwriting system, which is a noncompetitive (conventional) system, was maintained until the syndicated underwriting system was abolished in 2006. In contrast, for government bonds of other terms, over a substantial length of time prior to 2006 they were issued as determined by the tender or auction conditions known as the partial price competitive tendering system.

For years, market participants and government officials have made efforts to realize fair market price formation. Currently, in principle, all government bonds are issued through auctions as the syndicated underwriting program for JGBs was discontinued in March 2006. The market-oriented transition of bond issuance has also been witnessed in pricing spreads among bonds with different credit qualities. For example, yields at the issue of government-guaranteed bonds and local government bonds were determined in reference to the yield at the issue of 10-year JGBs earlier in the month. From time to time, the spreads for issues among these three classes of bonds have deviated from market spreads. In recent years, however, as investors started to focus more on differences in credit quality, the spreads for issues among the three classes have increasingly tended to move more in line with credit spreads prevailing in the market.

Another case in point that demonstrates the increased market orientation in bond issuance is the growing portion of government-guaranteed bonds being issued through a competitive bidding process (as individual issues). Investors are also showing an increasing tendency to differentiate corporate bonds based on credit ratings by rating agencies and other factors. In response, many issuers go through a premarketing process to identify and estimate investor demands and determine the terms of issuance accordingly.

E. Liberalization of the Japanese Yen and the Corporate Bond Market

There is a need to identify in Japan a market that can serve as a good model for the development of corporate bond markets in emerging economies, particularly in Asia. Additionally, there has been a need to fully open the Japanese corporate bond market to global participants by making it easy to use for both domestic and overseas issuers and investors.

Formerly, there were a number of different regulations on the issuance of corporate bonds in Japan. The issue terms were uniformly determined according to a set formula, and issuance volumes were constrained as well. This rigid issuance mechanism was subsequently modified to allow issue terms and conditions to be determined in accordance with actual market practices and conditions, in line with other deregulation measures. A selection of significant steps undertaken in the liberalization of the Japanese yen and the corporate bond market is listed in Table 4.

Table 4: Liberalization of the Japanese Yen and the Corporate Bond Market

Year	Event
1970	The Tokyo capital market is inaugurated, the Japanese yen is internationalized, and the Asian Development Bank issues its first bonds in the Japanese market, effectively creating the first Samurai Bond.
1971	Nixon shock: Dollar–gold convertibility is suspended, followed by a shifting of the Japanese yen to a floating-rate system in 1973.
1972	GTE public stock offering in Japan (first foreign stock)
1973	Australian government bonds offered in Japan (first Samurai Bonds)
1974	First German deutschemark public offering of corporate bonds (Mitsubishi Heavy Industries)
1975	First Swiss franc public offering of corporate bonds (Mitsubishi Chemical)
1977	Expansion of foreign exchange reserves, yen interest rates fall due to a decline in private sector funding demand, record issuance of Samurai Bonds Lifting of the ban on the issue of Euroyen bonds by nonresidents; first issue by the European Investment Bank
1984	Japan–US Yen–Dollar Committee (Japan–US financial market friction prompts further internationalization of the Japanese yen) Substantial easing of issuer qualifications for nonresident Euroyen bonds Lifting of the ban on the issue of Euroyen bonds by residents; first such issuance by Mitsubishi Heavy Industries (Euroyen Convertible Bonds worth JPY30 billion, which included a 180-day restriction on the recycling of Euroyen bonds in Japan)
1985	Plaza Agreement (major industrialized countries' coordinated response to rising US dollar interest rates due to US trade and fiscal deficits); managed floating exchange rate system is implemented
1990	Weakening of the Japanese yen following the collapse of the bubble economy in Japan
1991	Issuance eligibility criteria are amended to abolish quantitative requirements and credit rating criteria became fully adopted.
1993	Abolishment of regulations on corporate bonds issuance ceiling limits and revision of the trustee company system
1994	Abolition of recycling restrictions on sovereign Euroyen bonds; first Alpine bonds issued[a]
1996	Foreign exchange controls are abolished under the "Tokyo Big Bang" by the Hashimoto Cabinet, including the abolition of recycling restrictions on Euroyen bonds issued by residents.
1996	Eligibility criteria for corporate bond issuance are abolished and bond covenants are deregulated. Eligibility criteria for issuing unsecured bonds and the duty to establish a debt restriction clause were also abolished.
1997	Onset of the Asian financial crisis; failure of Sanyo Securities, Hokkaido Shokutaku Bank, and Yamaichi Securities
1999	Appreciation of the Japanese yen in the wake of the bursting of the US information technology bubble; ban on the issuance of straight bonds by commercial banks lifted
2006	Electronic registration of corporate bonds certificates launched (complete dematerialization)
2010	Announcement of the commencement of the TOKYO PRO-BOND Market

US = United States.
[a] Alpine bonds refer to foreign-currency-denominated bonds issued in Switzerland by non-Swiss residents (e.g., Japanese domestic corporation).
Source: ABMF SF1.

F. Tide for Change in the Corporate Bond Market

1. Liberalization and Influences

Fortunately, over the past 2 decades, the impediments that had isolated domestic Japanese markets from foreign international markets were removed through the significant efforts of policy makers and market participants. In 2008, the Financial Services Agency (FSA) revised the Financial Instruments and Exchange Act, 2006 (FIEA) as part of its plan to enhance the competitiveness of Japan's financial and capital markets, thereby establishing the legal framework for markets oriented toward Professional Investors; that is, a private offering system for designated investors and financial instruments exchange markets. This provided the legal framework for the establishment of a new securities market for Professional Investors that was not predicated on full legal disclosure requirements.

In addition, the taxation system was reformed in FY2010 to reduce the tax to 0 on revenues from domestic corporate bonds held by nonresidents. This was seen as a particularly useful opportunity to put an end to the state of isolation of Japan's domestic markets.

Having undergone various systemic reforms, the corporate bond market in Japan has developed into a free and efficient market that plays an important role in corporate financing. Notwithstanding the global financial crisis, which generated a downward trend in the second half of 2008, the corporate bond market has generally demonstrated a record of recovery and expansion. In addition, the bond market's performance was significantly affected in the first half of 2011 by the tragic earthquake and tsunami on 11 March. Since then, amid a recovery of the overall Japanese economy, the corporate bond market has been poised for recovery as well, signs of which can be seen in the professional bond market, the TOKYO PRO-BOND Market (TPBM), and the nonresident bond market (Figures 6 and 7, and Tables 5 and 6).

Figure 6: Publicly Offered Corporate Bonds Outstanding (JPY trillion)

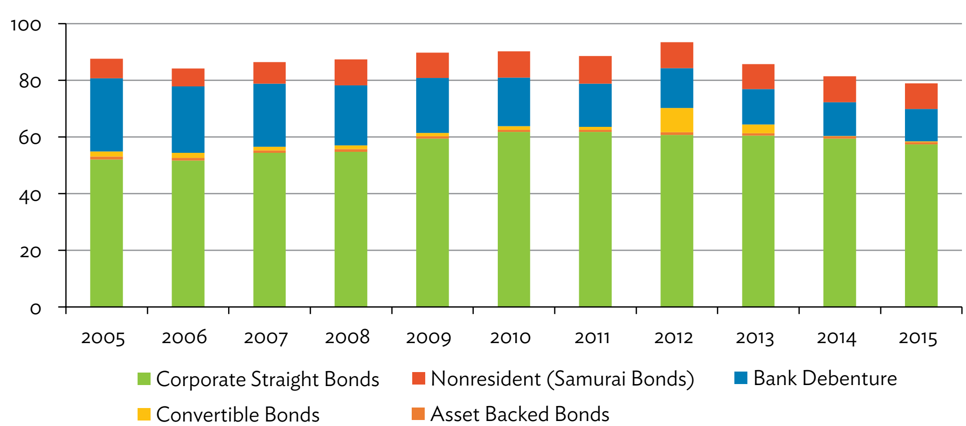

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Table 5: Publicly Offered Corporate Bonds Outstanding (JPY trillion)

	2005	2006	2007	2008	2009	2010	2011	2012	2013	2014	2015
Corporate Straight Bonds	52.0	51.6	54.4	54.8	59.4	61.8	61.7	60.7	60.4	59.3	57.4
Asset-Backed Bonds	1.0	1.0	0.8	0.9	0.8	0.7	0.8	0.9	0.8	0.8	0.7
Convertible Bonds	1.8	1.7	1.4	1.3	1.2	1.2	1.0	8.6	3.1	0.2	0.3
Bank Debenture	25.8	23.4	22.2	21.3	19.4	17.2	15.2	14.0	12.5	11.8	11.4
Nonresident (Samurai Bonds)	6.9	6.4	7.6	9.1	8.9	9.3	9.8	9.3	8.8	9.2	9.1
Corporate Bonds Total	87.6	84.2	86.4	87.3	89.7	90.3	88.6	93.5	85.7	81.4	78.9

Note: Data as of end of December for each calendar year.
Source: Japan Securities Dealers Association. http://www.jsda.or.jp/shiryo/toukei/hakkou/files/hakkougakushoukanngaku.xls

Figure 7: Publicly Offered Corporate Bond Issuance Volumes (JPY trillion)

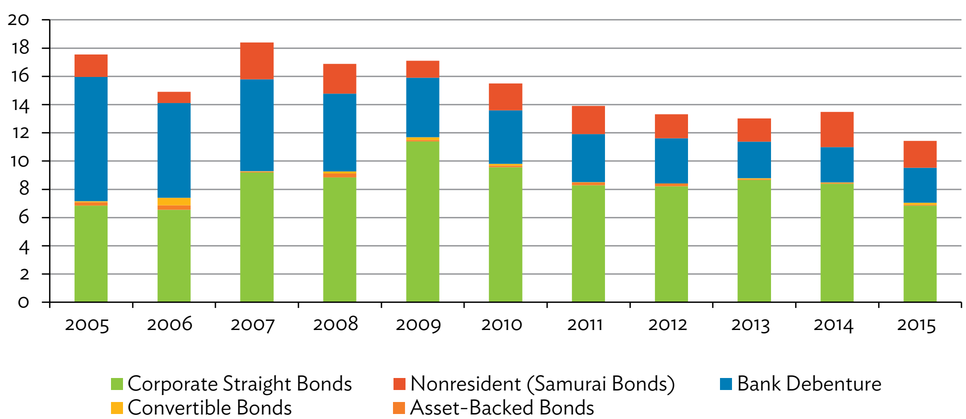

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Table 6: Publicly Offered Corporate Bond Issuance Volumes (JPY trillion)

	2005	2006	2007	2008	2009	2010	2011	2012	2013	2014	2015
Corporate Straight Bonds	6.9	6.5	9.2	8.8	11.4	9.6	8.3	8.2	8.7	8.4	6.8
Asset-Backed Bonds	0.2	0.3	0.1	0.3	0.1	0.1	0.2	0.2	0.1	0.1	0.1
Convertible Bonds	0.1	0.6	0.0	0.2	0.2	0.1	0.0	0.0	0.1	0.0	0.2
Bank Debenture	8.8	6.7	6.5	5.5	4.2	3.8	3.4	3.2	2.6	2.5	2.5
Nonresident (Samurai Bond)	1.6	0.8	2.6	2.1	1.2	1.9	2.0	1.7	1.6	2.5	1.9
Corporate Bonds Total	17.6	14.9	18.4	16.9	17.1	15.5	13.9	13.3	13.0	13.5	11.4

Notes: Data shown for each calendar year. Commercial paper not included. The outstanding values of privately placed bonds and notes may not be included.
Source: Japan Securities Dealers Association. http://www.jsda.or.jp/shiryo/toukei/hakkou/files/hakkougakushoukanngaku.xls

2. Developments in Issuance Methods and Price Discovery

The process for determining the method of the issuing condition has developed in the corporate bond market over the past 2 decades.

a. Proposal Method

In the corporate bond market, the proposal method was launched in 1988 based on the recommendation of the Securities and Exchange Committee of the MOF to abolish permanent fixed-member syndicates under a pre-agreed pricing matrix set by commissioned banks and introduce free competition among securities firms. Despite naming it the proposal method, the new measure was in fact a competitive bidding system. Since the issuer previously had no freedom to hold competitive bidding, the new method was welcomed by the users of the debt capital market in Japan.

The proposal method, however, soon collapsed because it was premature, given prevailing conditions in the Japanese domestic market, to expect the method to guide fair pricing. It created pricing that was too tight due to intensified competition among securities firms to win the lead manager position and neither issuers nor investors could confirm fair pricing due to undeveloped and illiquid secondary market conditions. Confidence in the pricing being offered by potential lead managers was often lacking. Consequently, new issue pricing under the proposal method was unable to perform its intended function because the majority of domestic investors did not trust the new issue price to be a fair price.

b. Negotiated Method

In 1991, Nippon Telegram and Telephone dropped the proposal method and introduced a new method to appoint lead manager(s). Even in the immature and undeveloped bond market, and amid declining liquidity in the secondary bond market, it was necessary to emphasize the determining of fair pricing in the market. In order to achieve fair pricing, the "JGB spread pricing new issue" under the negotiated method plus the fixed price reoffer with syndicate break for launching method (released to the syndicate selling group with the uniform fixed reoffering price) were developed and introduced in the corporate bond primary market.

Under the new negotiated method, Nippon Telegram and Telephone no longer requested pricing indication from securities firms. Instead, they put weight on the new issuance strategy proposal and commitment to secondary market maintenance in the selection of lead manager(s). As for new issue pricing, Nippon Telegram and Telephone emphasized discrete price discovery and a solid book-building process by the appointed or selected lead manager(s).

This new scheme aimed for fair pricing to reflect investor demand accurately under the prevailing market. For that purpose, the price talk with investors based on the JGB spread was introduced to find out the appropriate price as the benchmark to clear target issue amounts. As a result, the issuance of corporate bonds shifted to a flat sales price system. After several years, utilities companies, general business corporations, and some public sector entities adopted a similar concept.

This method is not applicable to discount sales since the sales price needs to reflect the prevailing market conditions. Since then, many issuers have tried various methods to realize fairer market pricing.

3. Corporate Bond Issuers and Holding Structure

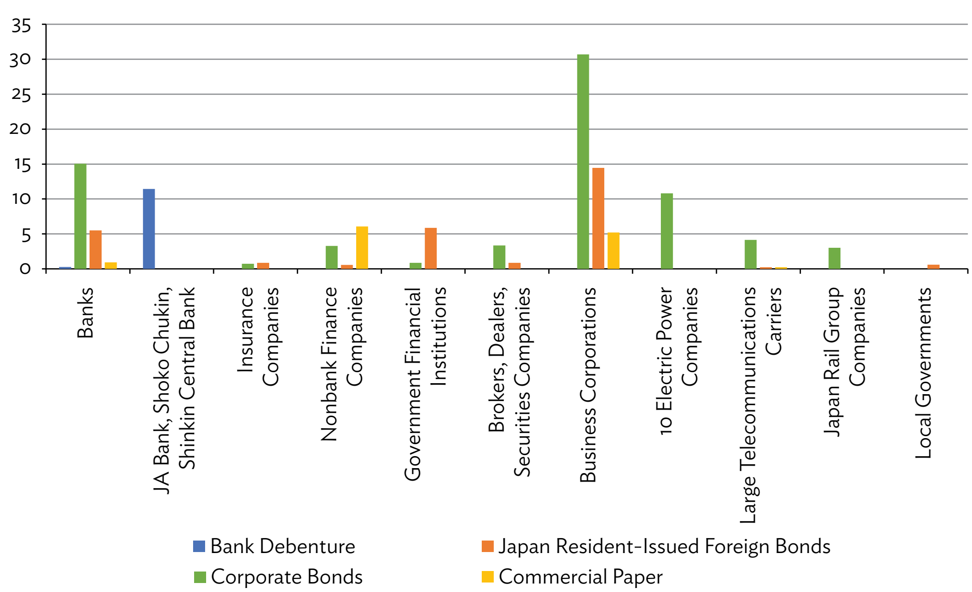
The Japanese corporate bond market remains a small market compared with the United States (US) and Eurobond markets. Although different types of companies have actively issued corporate bonds in the US and Europe (Eurobond market), the issuance of corporate bonds in Japan is still limited largely to

(i) fairly high-rated companies in specific sectors, including banks, electric power, telecommunications carriers, Japan Railways Group companies, and leasing and finance companies; and
(ii) small and medium-sized enterprise (SME) bonds that are issued and underwritten by bank(s) while utilizing the legal scheme known as Private Placement to Qualified Institutional Investors. (Significant numbers of small issuances have been made by SMEs.)

For a detailed look at the segmentation of the market, including the breakdown by type of bond or note available in Japan, please refer to Chapter III.D (Figures 19 and 21).

The breakdown of the corporate bonds at the end of March 2015 by issuing entities is displayed in Figure 8 and listed in Table 7.

Figure 8: Corporate Bond Issuing Entities by Structure (JPY trillion)



Notes: The figure uses the Bank of Japan definition of Corporate Bonds（事業債）. Data as of 31 March 2015.
Source: ABMF SF1 based on Bank of Japan 2015 Flow of Funds statistics. http://www.boj.or.jp/statistics/sj/

Table 7: Corporate Bond Issuing Entities by Structure (JPY trillion)

	Banks	JA Bank, Shoko Chukin, Shinkin Central Bank	Insurance Companies	Nonbank Financial Companies	Government Financial Institutions	Brokers, Dealers, Securities Companies
Bank Debenture	0.3	11.4	–	–	0.0	0.0
Corporate Bonds	15.0	0.0	0.7	3.3	0.9	3.4
Japan Resident-Issued Foreign Bonds	5.5	0.0	0.9	0.6	5.9	0.9
Commercial Paper	0.9	0.0	–	6.1	0.0	0.0

	Business Corporations	10 Electric Power Companies	Large Telecommunications Carriers	Japan Rail Group Companies	Local Governments	Total
Bank Debenture	–	–	–	–	–	11.7
Corporate Bonds	30.7	10.8	4.1	3.0	–	71.9
Japan Resident-Issued Foreign Bonds	14.5	0.0	0.2	0.0	0.6	29.0
Commercial Paper	5.2	0.0	0.2	0.0	–	12.4

Notes:
1. Data as of 31 March 2015.
2. The Bank of Japan's definition of "Corporate Bonds" for flow of funds statistics includes industrial securities (jigyousai: 事業債). Corporate bonds other than bank debentures issued by financial institutions are included in Industrial securities or Japan resident-issued foreign bonds (external securities issued by residents). Industrial securities are bonds issued domestically by joint-stock corporations. They correspond to secured or unsecured bonds under the Financial Instruments and Exchange Act and include (i) straight bonds (e.g., electric power bonds, Japan Rail bonds, large telecommunications carrier bonds such as NTT bonds, and ordinary business corporations bonds); and (ii) bonds with warrants.
3. "Business Corporations" indicate ordinary business corporations other than the three commercial issuer types stated separately.
4. '–' indicates no issuances under this categorization.

Source: ABMF SF1 based on the Bank of Japan Guide to Japan's Flow of Funds Accounts. http://www.boj.or.jp/en/statistics/outline/exp/data/exsj01.pdf

The main holders of corporate bonds in Japan are banks—including as securities custodians on behalf of individual investors—insurance companies, and pension funds, with the remaining types of investors being relatively minor players (Figure 9 and Table 8).

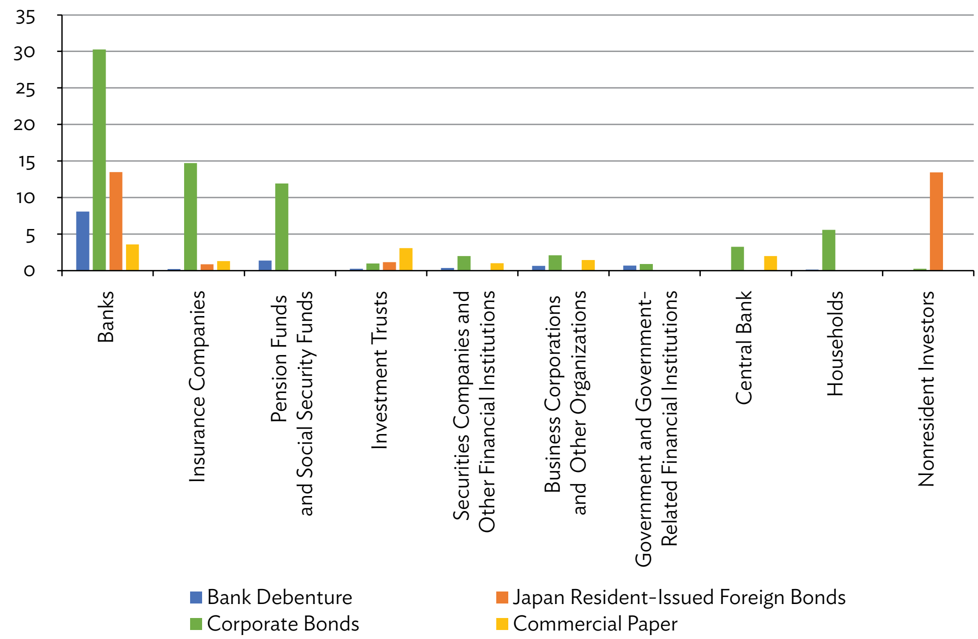
The investor base in Japan for foreign bonds, which comprise corporate bonds issued in the US and Europe (Eurobonds) that are aimed at Japanese residents—is very narrow in comparison to the investor base for corporate bonds issued in Japan by resident issuers.

4. Low Liquidity and Vitalization in the Corporate Bond Market

There are many complex factors behind the small size of the corporate bond market in Japan. For starters, many investors hold corporate bonds until redemption, which limits liquidity in the corporate bond market and restricts the size of the secondary market.

It is believed that a vitalization of the corporate bond market is needed to promote the diversification and decentralization of financing methods used by private companies, as well

Figure 9: Corporate Bond Holdings by Structure (JPY trillion)



Notes:
1. Data as of 31 March 2015.
2. The Bank of Japan definition of "Corporate Bonds" includes "事業債" to avoid using "etc.", which is vague and open to interpretation.

Source: ABMF SF1 based on Bank of Japan 2015 Flow of Funds statistics. http://www.boj.or.jp/statistics/sj/

Table 8: Corporate Bond Holdings by Structure (JPY trillion)

	Banks	Insurance Companies	Pension Funds and Social Security Funds	Investment Trusts	Securities Companies and Other Financial Institutions	Business Corporations and Other Organizations
Bank Debenture	8.1	0.2	1.4	0.2	0.4	0.6
Corporate Bonds	30.3	14.7	11.9	1.0	2.0	2.1
Japan Resident-Issued Foreign Bonds	13.5	0.8	0.1	1.1	0.0	0.0
Commercial Paper	3.6	1.3	0.0	3.1	1.0	1.5

continued on next page

Table 8 continued

	Business Corporations and Other Organizations	Government and Government-Related Financial Institutions	Central Bank	Households	Nonresident Investors	Total
Bank Debenture	0.6	0.7	0.0	0.1	0.0	11.7
Corporate Bonds	2.1	0.9	3.2	5.6	0.2	71.9
Japan Resident-Issued Foreign Bonds	0.0	0.0	0.0	0.0	13.4	29.0
Commercial Paper	1.5	0.0	2.0	0.0	0.0	12.4

Notes: Data as of 31 March 2015. The table uses the Bank of Japan definition of Corporate Bonds (事業債).
Source: ABMF SF1 based on Bank of Japan 2015 Flow of Funds statistics. http://www.boj.or.jp/statistics/sj/

as the expansion of asset management opportunities for investors, leading to a strengthening of the financial and capital markets. This, in turn, will result in the steady development of the Japanese economy. To this end, market participants need to take measures to vitalize the corporate bond market in their daily business activities to establish a sound and liquid market.

Since the global financial crisis, the vitalization of the corporate bond market has become a particularly important issue. At the onset of the crisis, liquidity in the short-term money market became extremely tight and many companies shifted to bank loans. In some cases, it was difficult to borrow from banks, and new and rollover issuance conditions were very unfavorable in the corporate bond market. In light of these circumstances, private corporations recognized the need to diversify their financing methods and sources of funds. Similarly, it has become increasingly essential to develop a corporate bond market with high degrees of transparency and liquidity to enable the steady financing of large amounts of money on a long-term basis.

Because strengthening the equity capital of banks and other financial institutions has become a major issue of global financial regulatory reform following the financial crisis, it is believed that banks' loan activities will change accordingly. It is expected that improving corporate bond market functions within a new regulatory environment will result in the proper development of financing mechanisms, including bank loans, and contribute to the advancement, enhancement, and stability of Japan's financial and capital markets. The development of the TPBM was in line with this approach.

Furthermore, developing the infrastructure of the corporate bond market in Japan and creating a more efficient market with higher levels of transparency and liquidity will increase the participation of foreign issuing corporations and investors, including those from Asia. It will also help the Japanese financial and capital markets play a role more suitable for the economic scale of Japan in global markets.

Building a market that meets the needs of Professional Investors such as institutional investors will contribute to improving the diversity of corporate bond issuers, market usability, and the diversification of asset management methods for investors, as well as enable Japanese market participants to utilize the human resources and information-analysis skills held by Japanese financial institutions. Strengthening the corporate bond market will also assist the Japanese capital market in playing an important role as a primary regional market within Asia.