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Grand Design for An Asian Inter-Regional Professional Securities Market

Shigehito Inukai

National Institute for Research Advancement (NIRA)

Capital Markets Association for Asia (CMAA)

21st Century Center of Excellence,
Waseda Institute for Corporation Law and Society

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**Grand Design for An Asian Inter-Regional Professional Securities Market
(AIR-PSM)**

March 2008

Shigehito Inukai

National Institute for Research Advancement (NIRA)

Capital Markets Association for Asia (CMAA)

21st Century Center of Excellence,
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March 31, 2008

Shigehito Inukai

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また、犬飼重仁のSibos2007(2007年10月2日Boston)における講演記録の本書への掲載は、SWIFT ジャパンをはじめとするSWIFT Groupの皆様のご厚意によって実現したものであり、この場をお借りして謝意を表したい。

編著者 犬飼重仁

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Executive Summary

《Shigehito Inukai's speech at Sibos2007, Boston, 02 October 2007》

Asian Inter-Regional Professional Securities Market (AIR-PSM)

It is a great honor and pleasure for me as a representative of the Asian region to have this opportunity to speak at Sibos2007. (Please refer P.9-11 for session information)

Today I would like to offer a brief outline of issues involved in the future establishment of a common Asian Inter-Regional Professional Securities Market or AIR-PSM as a venue for companies in Asian countries to issue securities and for sophisticated regional investors to conduct securities transactions.

In preparation for my presentation today, I read the summary of the discussions at last year's Sibos session regarding the reform of Asian securities markets.

I was impressed by the seriousness of the discussion of the issues involved on that occasion.

Asian Regional Economy and Trade

- Some Asian countries focus on their areas of comparative advantage, and specialise in producing intermediate goods
- A sophisticated division of labour structure has been formed across national borders in the region
- The result is superior and competitive "Made in Asia" products, e.g. electrical appliances and vehicles
- Deeper trade interdependency between Japan and other Asian countries has developed

Last year the question was posed as to whether securities market reform in Asia represents heaven, hell or purgatory.

The session record suggests that the majority opinion was that, regarding this issue, we are in purgatory. However, in my opinion, such reform also represents a significant opportunity for Asia.

When we discuss Asian market harmonisation, we should think about the issue by dividing the market into two areas, a regional economy/trade side and a capital market side.

Within Asia, manufacturing and trade are increasingly integrated, but in a way that differs from the EU and NAFTA.

For example, trade in the Asian region is characterised by the fact that

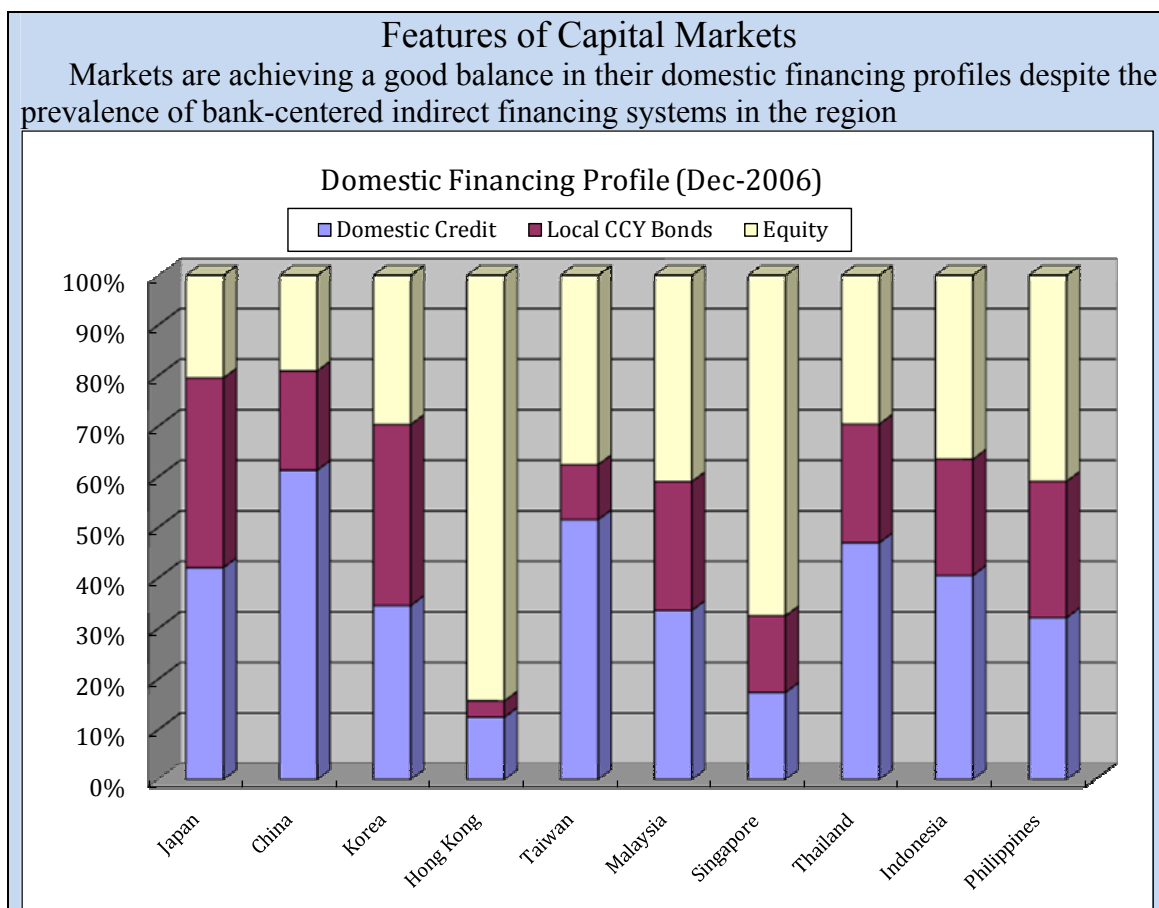
- (1) some countries focus on their areas of comparative advantage, and specialise in producing intermediate goods, and
- (2) a sophisticated division of labour has been formed across national borders in the region.

The result is increased regional productivity and the manufacture of superior and

competitive “Made in Asia” products such as electrical appliances and motor vehicles.

Deeper trade interdependency is also developing between Japan and other Asian countries.

As far as manufacturing and trade in the Asian region are concerned, this type of structure has formed over the past ten years, driven by necessity.



However, despite the fact that finance and the flow of goods are two sides of the same coin, the success achieved in trade cooperation in the region has not been matched by a comparable level of success in the development of a common regional capital market in order to increase regional competitiveness. However, I do not by any means want to indicate that the situation is hopeless.

The discussion of the issue requires that we correctly understand the status of the domestic capital markets in the major Asian countries.

There are two features of regional capital markets in particular that I would like to mention as background to the discussion.

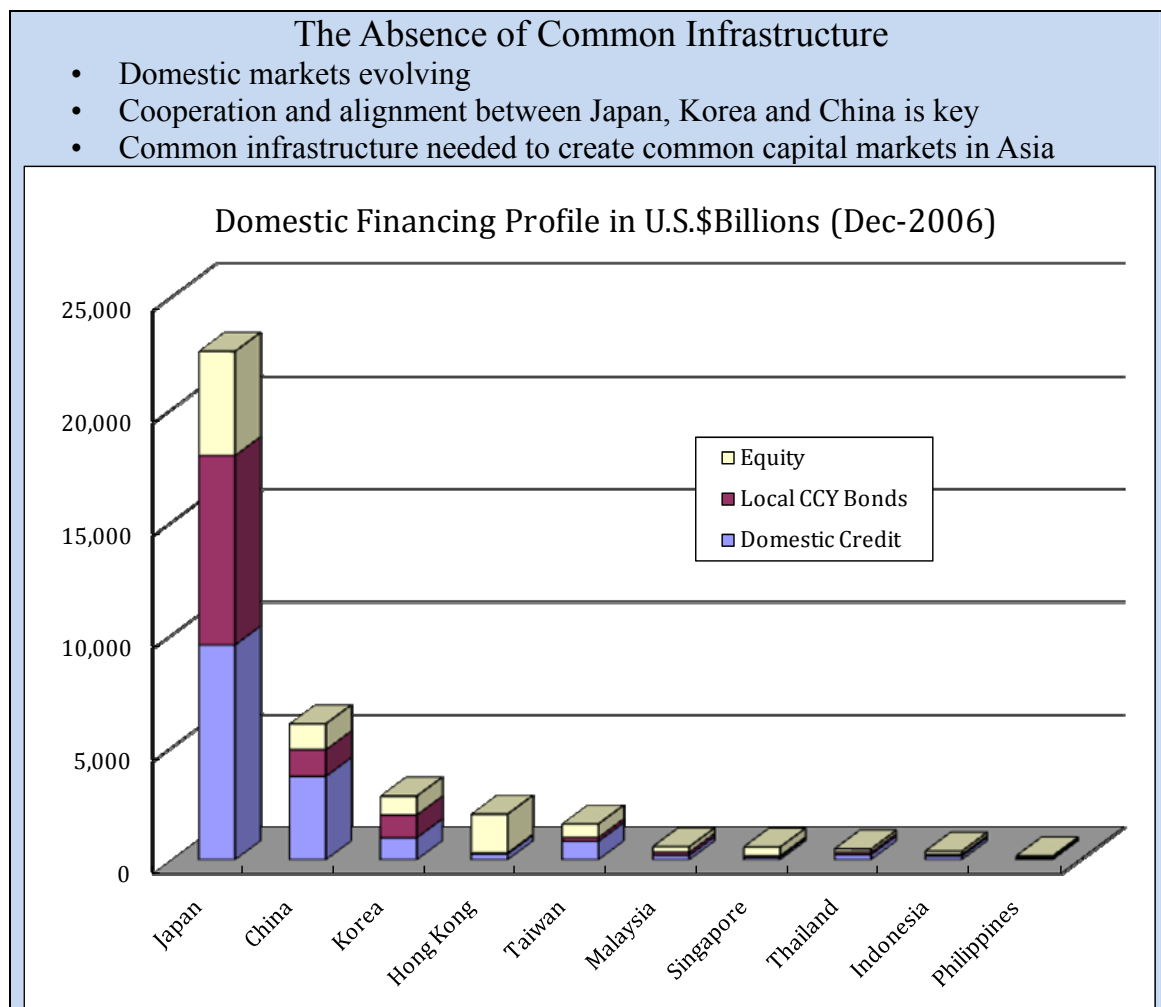
First, domestic capital markets in the Asian region are achieving a good balance in their domestic financing profiles despite the prevalence of bank-centered indirect financing systems in the region. Asian financial markets have long been known as bank-centered markets. However, over the past few years, the proportion of financing in the bond market has increased in China, Korea and other countries.

As this graph shows, the domestic financing profile, the split between banks, bonds

and shares, is becoming well balanced in almost all the major Asian countries other than Hong Kong and Singapore.

The second feature of Asian financial markets is the policy of dividing the domestic and foreign markets.

Apart from Japan, many countries are applying strict control of foreign exchange, funds, and securities, and are limiting cross-border funds transfers between domestic and foreign markets, based on their experience in the currency and financial crisis of 1997-98.



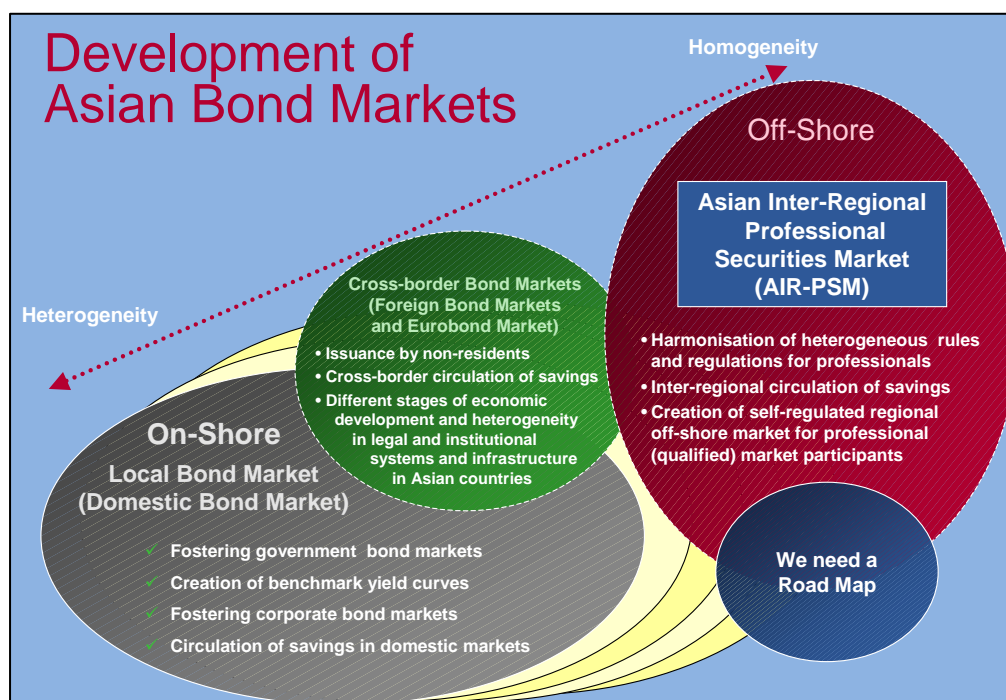
While domestic markets in Asian countries have evolved, we still face the problem of the absence of common infrastructure for the creation of a common capital market in Asia.

An Asian Inter-Regional Professional Securities Market, which would enable the abundant savings in the region to be circulated within the region, is yet to be developed as an important element in a common capital market.

As indicated in this graph, Japan, China and Korea are the largest domestic markets in the region, and cooperation between them will therefore be important in the development of an integrated inter-regional capital market.

Please focus on the size of the markets. The total size of the regional market is

equivalent to more than 30 trillion US dollars.



There are two camps in discussions related to the development of Asian Bond markets.

One prioritises the further development of domestic markets, or, alternatively, believes that the level of development of domestic markets is sufficient.

The other camp seeks to further develop domestic markets and to promote a cross-border inter-regional (offshore) market in the region at the same time.

This does not mean simply connecting domestic markets. A cross-border market would be, rather, a non-domestic market that co-exists within the region with domestic markets, but features the involvement of different players, rules and taxation schemes.

As an image of such a cross-border market, we might consider self-regulating markets like the Eurobond market. While the EU has recently tightened regulations and reduced the freedom of the market, the Eurobond market has traditionally been regarded as a freely accessible market.

Cooperation between market players and regulators in Asian countries will be extremely important in the development of a free and open market of this type in the region. Because Japan is by far the largest market in the region, Japan should play a leadership role, and discussions involving Japanese market participants should be promoted and facilitated.

However, harmonisation of traditional independent market practice in each of the region's countries may not be viable. If many to many interoperability among domestic markets in the region is sought, the matrix will be extremely complex, and not optimal for the region as a whole.

A preferable approach is to develop a common integrated market infrastructure for the requirements of professionals. Professor Hal S. Scott of Harvard Law School also indicates that off-shore integration is far more important than on-shore integration in the Asian region.

Harmonised Markets?

- Need to recognise diversity in Asia
- Harmonisation – what degree is required?
- Focus on common infrastructure i.e. a cross-border market accessible by Asian countries
- The concept of an Asian Inter-Regional Professional Securities Market (AIR-PSM) as a self-contained market, enabling savings accumulated in the region to circulate within the region

Given the level of diversity in the region, I do not believe that harmonisation is required at the level of the operations of each domestic capital market in the region. This is a virtually unachievable goal.

Instead, as I have indicated, a common, integrated infrastructure will be necessary. By this I mean a cross-border market commonly accessible by Asian countries together, created by means of harmonising rules and infrastructure for professionals.

We may call such a market an AIR-PSM (Asian Inter-Regional Professional Securities Market).

The AIR-PSM would be a self-contained market enabling savings accumulated in the region to circulate within the region.

We can certainly see development in each of the domestic markets in the region as a result of several arrangements in which the ADB, central banks and governments have co-operated in the last several years.

However, it is time for us to concentrate on the establishment of an open and free market for professionals similar to the Eurobond market. Such a market would be different from domestic markets and also different from NY and London.

An Asian Investment Banker's Perspective

- Huge Asian capital reserves provide an opportunity for Asian financial institutions to take the lead in capital markets in Asia
- Asian financial institutions are not leading the market in terms of capital disbursement and price making – European and US financial institutions still dominate in this area
- Why is it that Asian issuers need to raise capital in London or New York?
- Advanced Asian financial institutions have a responsibility to take the lead
- Why not integrate Asian capital markets to create a viable alternative to London and New York?

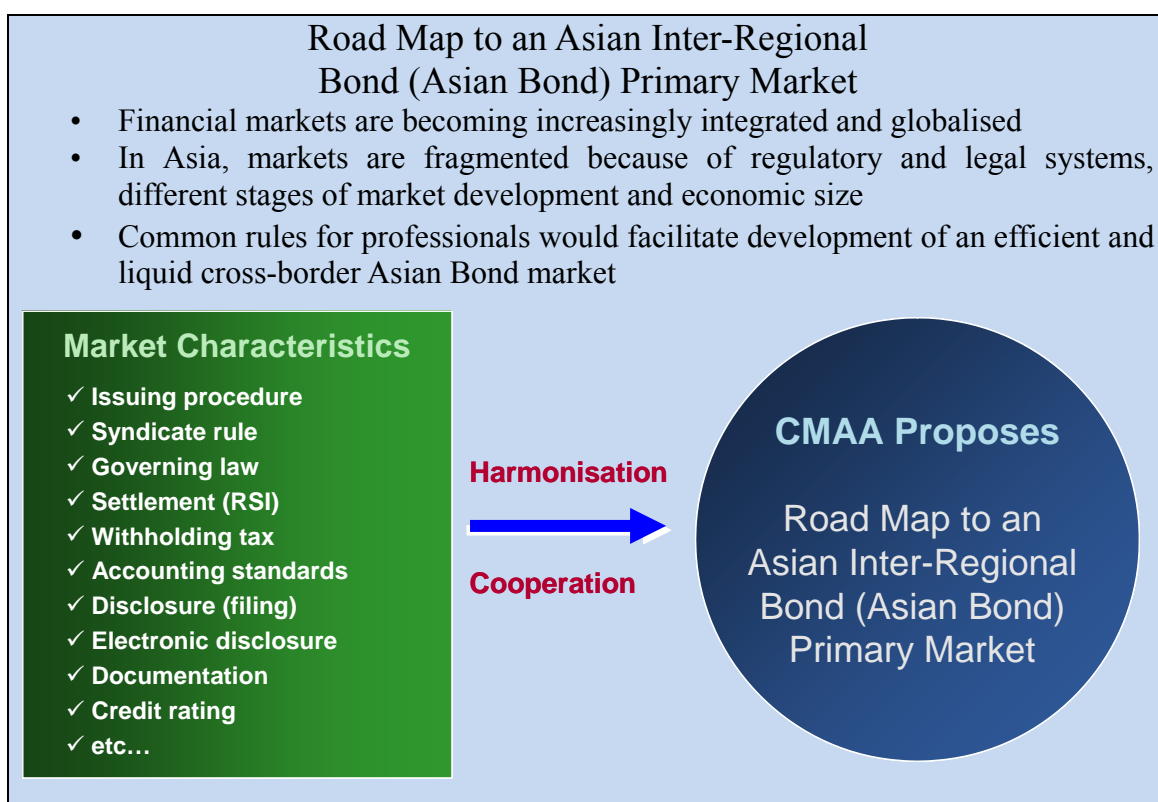
Purpose of Capital Markets Association for Asia (CMAA)

- Formulate self-governing rules for issuing entities and other users
- Coordinate opinions regarding legal systems and rules
- Foster dialogue with CMAA participants
- Conduct research, formulate proposals, increase awareness
- The ultimate purpose of the CMAA is to increase reliability and convenience for all financial and capital markets in Asia and to establish appealing markets for all users

The Capital Markets Association for Asia, or CMAA, has recently been formed with the aim of establishing an AIR-PSM. The members of the CMAA are mainly Japanese and Korean market professionals and practitioners. The screen shows the objectives of the CMAA.

Given the recognition that the Eurobond market is becoming more regulated under EU rules, expectations are growing regarding a self-regulated off-shore professional securities market in Asia. Naturally it is desirable that such a market should respect the principles of globalisation and should involve participants from around the world. For example, all the professional market players in attendance at SIBOS.

The value of such a market infrastructure will ultimately depend on how easy it is to use from the perspective of market participants, i.e., the extent to which it enables regional savings to circulate within the region.



The CMAA proposes a road map to an Asian Inter-Regional Bond (Asian Bond) Primary Market including issuing procedures, syndicate rules, governing law, regional settlement mechanisms etc... (Please refer P.39-51)

If you would like to learn more about the CMAA or the concept of an AIR-PSM, we would be very happy to provide you with further information.

(Shigehito Inukai)

Related Information
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Asia momentum - News for Asia Pacific customers and partners

New this year, *Asia Momentum* looks at Sibos from an Asian perspective, bringing you news from the conference that is relevant to Asia. We will share with you session highlights and comments from some of the 600 participants attending Sibos 2007 from the Asia Pacific region.

MARKET HARMONISATION IN ASIA PACIFIC: DESIRABLE, DO-ABLE?

Asia Pacific must harmonise to stay competitive



The 'Market harmonisation in Asia Pacific: desirable, do-able?' session took up the challenge laid down at Sibos last year that "Asia Pacific has to look after Asia Pacific" if it wants a more harmonised market in the region. In the absence of region-wide regulatory impetus, efforts for harmonisation will depend on the desire and involvement of the market players – and a spirit of cooperation rather than competition.

Speakers from the public sector, commercial banking, technology and academia put forward their views.

Ian Johnston

Session moderator Ian Johnston, Head of Asia Pacific, SWIFT, opened the discussion making an important observation "today we are focusing on harmonisation not integration." He added that "harmonisation is more of an Asian concept like yin and yang."

Karen Fawcett

A compelling call to action to create a single Asia Pacific market was issued by **Karen Fawcett, Group Head, Transaction Banking, Standard Chartered Bank**, at the session. A **single market** could bring huge benefits to the region, said Fawcett, while failure to act could be harmful to the region's current growth, particularly as labour costs have been "increasing astronomically" over the past couple of years. "What historically has been a relatively competitive environment is going to suffer tremendously if we don't sort out the complexity of dealing with a myriad of small, highly differentiated markets around Asia Pacific," she observed.

**"Imagine a harmonised economic block of three billion people. That would have real power."
Karen Fawcett, Standard Chartered Bank**

In terms of infrastructure, Fawcett's "picture of Asia Pacific nirvana (涅槃・至福・解脱の境地)" includes a **single payments infrastructure, a single clearing house for commodities, bonds and equities and CLS across all currencies.**

She also suggested a full commitment to electronic communication, and universal use of the English language for cross-border communication, leading eventually to a single Asian currency and a single economic environment.

“Given the number of countries involved in Asia Pacific, it is up to the people in this room to help this process of harmonisation,” she said. Recognising that Asia Pacific is “messy”, she suggested that the banking and business community needs to be far more proactive in working with the public sector. “So far, lots of groundwork has been done but there have been very few results,” she said. **“Imagine a harmonised economic block of three billion people. That would have real power.”**

Harmonisation, stressed Fawcett, is essential in order to **reduce business costs, speed up transactions and simplify day-to-day practice**.

However, it would **not be good for everybody**. “For the smaller, weaker players in the market, it will **mean potentially less revenues and a tougher competitive environment**.”

On the government side, she added, there will be concerns about lack of differentiation and pressure to accept the forces of consolidation among the smaller players.

“But we **believe that Asia Pacific must harmonise in order to stay competitive**,” she reiterated.

Shigehito Inukai (Please refer P.3-8 for full speech)

“I do not believe that harmonisation is required at the level of the operations of each domestic capital market in the region. This is virtually an unachievable goal.”
Shigehito Inukai, National Institute for Research Advancement

On the other hand, **Shigehito Inukai, Director of Policy Study and Senior Fellow, National Institute for Research Advancement**, said “given the level of diversity in the region, I **do not believe that harmonisation is required at the level of the operations of each domestic capital market in the region**. This is virtually an unachievable goal.”

He instead spoke about the **need for a common, integrated infrastructure**. “By this I mean a cross-border market commonly accessible by Asian countries together, created by means of harmonising rules and infrastructure for professionals.”

Inukai went on to describe an **Asian Inter-Regional Professional Securities Market** as a **self-contained market** enabling savings accumulated in the region to circulate in the region.

George Pilakis

“Asia Pacific can potentially leapfrog generations of infrastructure legacy, like it did with the mobile phone.” **George Pilakis, ANZ**

On the role of technology in harmonisation, **George Pilakis, Chief Information Officer and Head of Technology, ANZ**, said the **region could benefit from its lack of legacy and high level of IT literacy**. “Technology is the pivotal tool that is the enabler for opportunity,” he said. “Asia Pacific **can potentially leapfrog generations of infrastructure legacy**, like it did with the mobile phone. The region doesn’t need to reinvent business solutions that have already been created, but take them to the next step. But what is developed internally should also be extendable outwards.”

Esmond Lee

Esmond Lee, Head of Market Systems Development, Monetary Management & Infrastructure, Hong Kong Monetary Authority, added: “The objective of harmonisation is not another working group or conference but to boost business and reduce cost. **What the market needs are more facilitators**. Ideal solutions should be regional. Asia systems should be part of global.”

SWIFT standards

Responding to a question from the floor, the panelists agreed that SWIFT has an important role to play in Asia Pacific. **Inukai**, said he had “tremendous hope of relations with SWIFT,” particularly in the field of **cash management**. “In Europe, businesses do cash management very effectively,” he commented. “Asian countries can learn about cash management processing from Europe – and that definitely requires the help of SWIFT.”

Acknowledging that SWIFT now has far more representation in the region, **Fawcett** suggested this greater presence will make a “big difference” to all market participants. She called for a **constructive dialogue between SWIFT and public sector entities** – but this does not mean trying to achieve everything at once. “We should focus on specific things, like **the use of SWIFT standards** for clearing systems in the various countries,” she suggested. “What if everybody chose SWIFT for their standard? That would **move us immediately down a path** that is very easy to follow. **If we had all the clearing systems on the same standards that would do a huge amount.**”

Making progress in the next 12 months

To conclude the session, **Johnston** asked the speakers to provide a realistic assessment of **what delegates should go away and do, as the first steps towards harmonisation.**

Over the next 12 months, **Fawcett** said, she hoped to see two more countries in the region **using SWIFT for clearing and settlement services**, two more Asian currencies **added to CLS** and ten more banks in the region **on SWIFTNet TSU**. “Those are capabilities that are in place already to be adopted,” she said.

Pilakis said he hoped to see **more agreement on the understanding of the barriers**, such as price, legacy systems and education, and a **roadmap** which defines where we are now as a basis to move forward.

Inukai hopes to see **greater acceptance of global standards**, especially in Japan.

More thought on harmonisation for post trade settlement was highlighted by **Lee** as a focus area for the next 12 months, as well as moving from thinking about projects to completing projects.

An academic perspective on market harmonisation in Asia

Q&A with Shigehito Inukai, Director of Policy Study and Senior Fellow, National Institute for Research Advancement, Japan and Secretary-General, The Capital Markets Association for Asia.

Q. How can the Asian capital market benefit from market harmonisation?

Asia has enormous capital reserves, and is rapidly forming capital via trade surpluses and economic growth. Given this, there is no reason that Asian financial institutions cannot take the lead in Asian capital markets.

Isn't it somewhat strange that Asian bond issuers have to go to London or New York to obtain funds from Asian investors? Why not integrate Asia capital markets to create a viable option in addition to London and New York?

Q. What do you see as some of the challenges for an Asian Inter-Regional Professional Securities Market?

Cooperation from financial institutions is necessary but Japanese financial institutions are not necessarily proactive in dealing with business opportunities outside Japan. Regulation and market practice **favours a focus on the domestic market** – this is a challenge.

Q. Initially the focus for your Asian Inter-Regional Professional Securities Market is Japan and Korea, when do you plan to bring together a wider group of Asian countries?

In the next stage we plan to bring in China, Taiwan, Hong Kong and Singapore. We plan to do this **by the end of 2008**.

Q. Do you believe that some of the topics and issues being discussed at Sibos are relevant to Japan?

I feel that the topics being discussed at Sibos are extremely relevant to Japan, as well as helpful and potentially very influential.

This networking occasion is extremely helpful. Unfortunately, in Japan we do not have this type of event so I feel very privileged to be here. **In Japan there is no equivalent cross industry dialogue or opportunity to come together.**

Asia

“What was said about Asia was generally impressive, but I disagree with the comment that institutions in the region are finding it hard to come together to achieve a collective view. I can say from my experience that Asian institutions are very willing to change.”

Shigehito Inukai, Director of Policy Study and Senior Fellow, National Institute for Research Advancement (NIRA)

1. The Need for Common Financial and Capital Markets in Asia

While the liberalisation of the flow of goods has made headway as a result of negotiations on free trade agreements (FTAs) among Asian countries, the need to establish a common foundation for the financial sector remains.

The Experience of the Asian Financial Crisis and Consensus on Strengthening the Competitiveness of the Asian Region

Since the Asian financial crisis of 1997, Thailand, the Republic of Korea and other Asian countries have been putting into place a variety of measures to prevent a similar crisis from recurring. In 2000, the Association of Southeast Asian Nations and Japan, China and Korea (ASEAN+3) concluded an agreement on the Chiang Mai Initiative, a mutually supportive network designed to help countries in the event of a crisis. This marked the first in a series of cooperative crisis-prevention measures in Asia.

It has also been pointed out that the absence of infrastructure that would enable Asian countries to circulate their abundant savings within the region was one of the causes of the 1997 crisis.

It was this perspective that gave rise to the idea that in order to prevent a recurrence of a similar crisis, Asia needs to establish common and joint financial and capital markets in which Asian capital can be invested within the region over the long term.

What specific problems have to be addressed in order to establish a common foundation for Asia's financial sector?

A Common Foundation (1) - Harmonisation of Market Infrastructure

First and foremost, there is a need to harmonise laws and regulations governing regional cross-border financial and capital markets and to establish a common foundation of settlement and payment systems for cross-border transactions within Asian countries. To enable the establishment of a viable bond and securities market, a market for long-term capital, a variety of market infrastructures must be put in place, including legal and accounting systems, tax treatment (including a tax-exempt environment for professional market players), a rating system, a credit insurance system and an international securities clearing and settlement system.

For example, the European Union (EU) has established common principles governing regulations in financial markets modeled after British laws, and is now working to incorporate those regulations into each member state's legal system.

What is noteworthy is the relationship between the EU and Britain. Market integration may suggest monetary union, but Britain has retained its own currency while taking the initiative toward financial market integration among the 27 EU member states.

While it remains to be seen how successful this initiative is, this relationship could serve as a very useful reference as Asian countries embark on the establishment of a common foundation.

A Common Foundation (2) - The Asian Economic Community Model

What type of economic community should be established in Asia? Although Japan and other Asian countries are currently involved in establishing FTAs, it remains to be seen what type of model for economic community will be explored after these

agreements are finalised. However, what seems very clear is that Japan, Korea and China - the countries with the largest markets – need to take the initiative within the region.

The “Double Goose” Model as A New Development Model in Asia

In 2004, Professor Kang Xie of the Institute of World Economy, Shanghai Academy of Social Sciences, proposed a new Asian development model called the “Double Goose” Model, which calls for China on the one hand and Japan and Korea together on the other to cooperate in taking the leadership role in the region, forming a “Double Goose” that will fly in harmony.

This model merits serious consideration.

A Common Foundation (3) - Consensus on Strengthening the Competitiveness of the Asian Region

The development of a consensus regarding the strengthening of competitiveness in Asia as a whole is crucial. FTAs govern the flow of goods, but finance and the flow of goods form two sides of the same coin.

The competitiveness of the Asian region as a whole will not increase unless both develop simultaneously. It is first necessary, however, to forge a consensus regarding the strengthening of Asia’s competitiveness through a cooperative structure similar to the EU or the North American Free Trade Agreement (NAFTA).

To that end, rather than remaining at the conventional level of government-led initiatives, as in the case of the Chiang Mai Initiative, this effort must come in the form of a partnership between the public and private sectors and academia as well as market professionals in the region, enabling actors from all fields across Asia to come together to proactively explore ideas for building a harmonised Asian market.

The most important factor in ensuring sustainable growth of Asia’s economies is to strengthen the international competitiveness of individual Asian countries as well as the regional market as a whole.

For some time now there has been a great deal of discussion in Japan on the subject of the nation’s revival. However, this discussion has generally been conducted without any awareness of the relationship between Japan’s revival and development in Asia. Given the present reality, mutual cooperation of increasingly interdependent Asian communities and strengthening of the regional market’s international competitiveness appear to be more important than any other issues.

Ever-Closer Trade Relations among Asian Countries

Here, the trade relationships in East Asia in recent years will be examined using the “degree of trade linkage,” an indicator of the closeness of bilateral trade relations. In the case of Japan’s exports among six East Asian countries (China, Korea, and Asean-4) and the United States, the linkage is strongest with Korea. The next highest index is for exports to the four ASEAN countries (Thailand, Malaysia, Philippines and Indonesia), followed by China and then by the United States, with the lowest index. China has the deepest ties with Japan in its exports, followed by Korea, the United States and four ASEAN countries, in that order. In the case of Korea, the closest linkages are with China, Japan and the four ASEAN countries for both exports and imports, with the East Asian countries dominating the first to third slots. In short, Korea, China and Japan

mutually maintain the closest relations in terms of exports.

When we discuss Asian market harmonisation, we should think about the issue by dividing the market into two areas, a regional economy/trade side and a capital market side.

Within Asia, manufacturing and trade are increasingly integrated, but in a way that differs from the EU and NAFTA.

For example, trade in the Asian region is characterised by the fact that

(1) some countries focus on their areas of comparative advantage, and specialise in producing intermediate goods, and

(2) a sophisticated division of labour has been formed across national borders in the region.

The result is increased regional productivity and the manufacture of superior and competitive “Made in Asia” products such as electrical appliances and motor vehicles.

As stated above, deeper trade interdependency is also developing between Japan and other Asian countries.

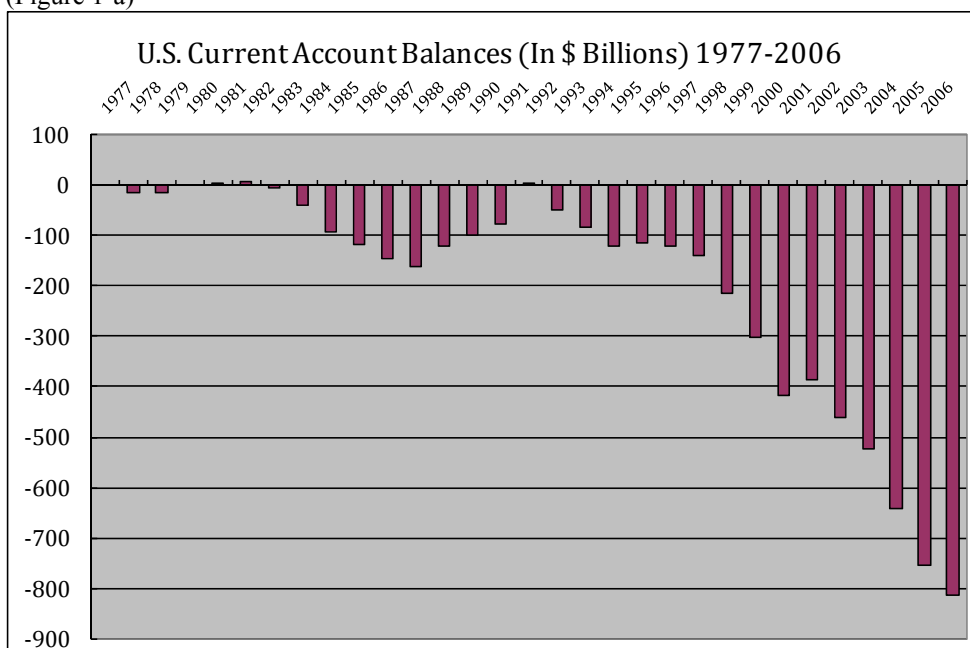
As far as manufacturing and trade in the Asian region are concerned, this type of structure has formed over the past ten years, driven by necessity.

However, despite the fact that finance and the flow of goods are two sides of the same coin, the success achieved in trade cooperation in the region has not been matched by a comparable level of success in the development of a common regional capital market in order to increase regional competitiveness.

Who finances the U.S. current account deficit?

The close relationship among Asian countries is evident in the link between the U.S. current account and foreign currency reserves held by Asian nations such as China, Japan and South Korea. The U.S. current account deficit has increased sharply since 2000, reaching \$811.5 billion at the end of 2006 (Figure 1-a, b).

(Figure 1-a)



Source: US Department of Commerce, Bureau of Economic Analysis
International Economic Accounts "Balance of Payments"

(Figure 1-b)

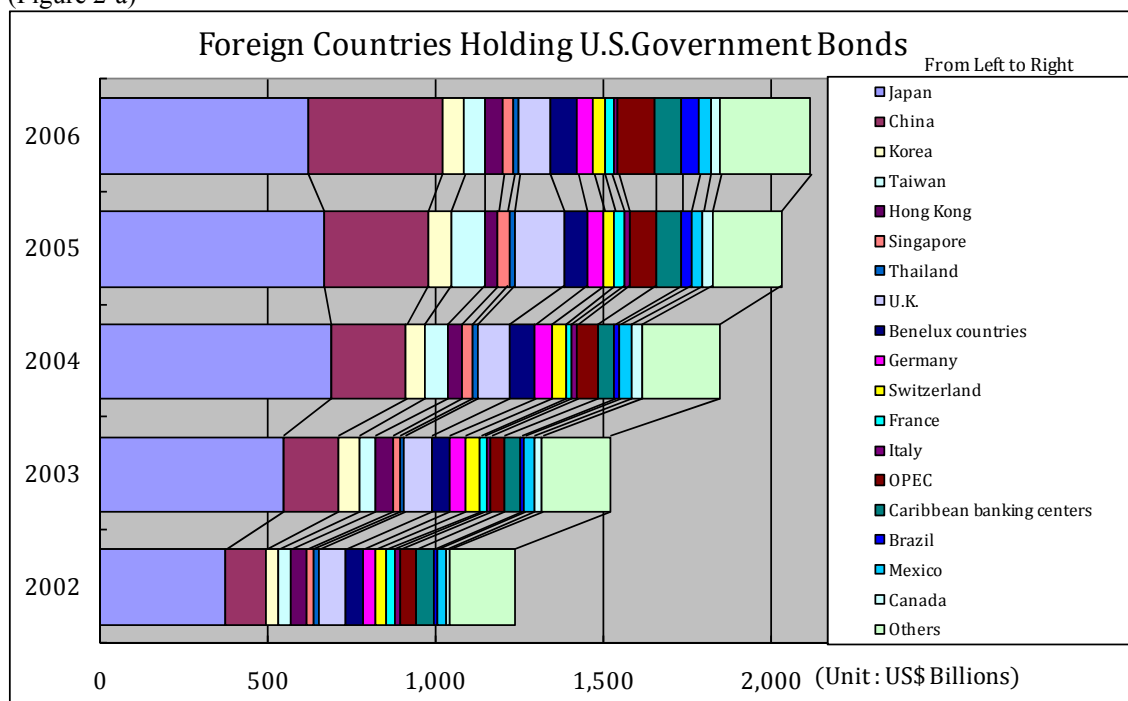
(In U.S. \$ Billions)

1991	1992	1993	1994	1995	1996	1997	1998	1999	2000	2001	2002	2003	2004	2005	2006
2.9	-50.1	-84.8	-121.6	-113.6	-121.6	-140.7	-215.1	-301.6	-417.4	-384.7	-459.6	-522.1	-640.1	-754.8	-811.5

Failure to Circulate Accumulated Capital was One Cause of the Asian Economic Crisis

It is noteworthy that of more than \$2 trillion in U.S. government bonds held overseas, more than half are held by Japan, China and other Asian nations (Figure 2-a,b).

(Figure 2-a)



Source: U.S. Department of the Treasury

(Figure 2-b) Holdings of U.S. Government Bonds

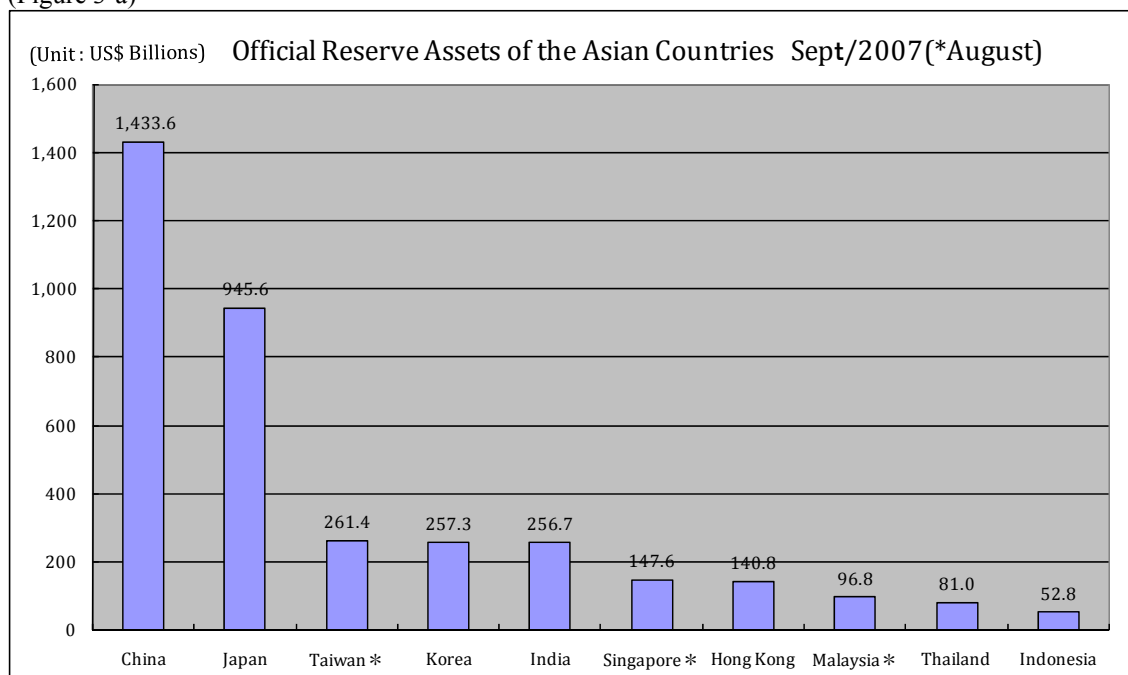
(Unit: U.S. \$ Billions)	2002	2003	2004	2005	2006
Japan	378.1	550.8	689.9	670.0	622.7
China	118.4	159.0	222.9	310.0	398.0
Korea	38.0	63.1	55.0	69.0	66.7
Taiwan	37.4	50.9	67.9	98.1	59.3
Hong Kong	47.5	50.0	45.1	40.3	53.8
Singapore	17.8	21.0	30.3	33.0	31.3
Thailand	17.2	12.0	15.0	16.1	16.9
U.K.	80.8	82.2	95.8	146.0	93.7
Benelux countries	49.9	52.1	74.4	68.3	80.8
Germany	37.3	47.8	50.3	49.9	45.9
Switzerland	34.0	46.1	41.7	30.8	34.3
France	22.9	17.0	20.1	30.9	26.4
Italy	16.3	13.0	12.9	15.4	13.2
OPEC	49.6	42.6	62.1	78.2	110.0
Caribbean banking centers	50.3	47.3	51.1	77.2	79.8
Brazil	12.7	11.8	15.2	28.7	52.1
Mexico	24.9	27.4	32.8	35.0	34.9
Canada	10.4	24.2	33.3	27.9	26.9
Others	192.1	204.8	233.5	209.1	268.0
Total Foreign Holdings	1,235.6	1,523.1	1,849.3	2,033.9	2,114.7

(Year-end figures)

This can be said to indicate that the U.S. current account deficit is being financed by investments in U.S. government bonds mainly conducted by Asian countries.

As of the end of September 2007, China held U.S. \$1,433.6 billion in foreign exchange reserves (the largest in the world) and Japan U.S. \$945.6 billion (the second largest), followed by Taiwan, Korea and India. Together, the Asian region's foreign exchange reserves exceed U.S. \$3.7 trillion, accounting for over half of the entire world's foreign currency reserves (about U.S. \$6.5trillion) (Figures 3-a and 3-b).

(Figure 3-a)



Source: IMF, etc.

(Figure 3-b) (In U.S. \$ Billions)

China	1,433.6	Sep-07
Japan	945.6	Sep-07
Taiwan *	261.4	Aug-07
Korea	257.3	Sep-07
India	256.7	Sep-07
Singapore *	147.6	Aug-07
Hong Kong	140.8	Sep-07
Malaysia *	96.8	Aug-07
Thailand	81.0	Sep-07
Indonesia	52.8	Sep-07
Total	3,673.6	

It can therefore be said that savings in Asia have financed the bulk of the U.S. current account deficit in recent years.

Lack of Infrastructure for Utilising Internal Funds in Asia

Funds accumulated in Asia are flowing into the United States and Europe through international intermediaries, and the bulk of those funds are then being cycled back into

Asia as direct investment by the United States and Europe.

The problem lies in the fact that the intermediation of this flow of funds is largely being handled by “international financial institutions and international clearing and settlement systems outside the Asian region.”

Fundamental Issue underlying Asian Bond Market Scheme

For example, non-Asian financial institutions are dominant as **lead managers in international bond and securities markets**, even for Asia-related bond business. Furthermore, they are effectively managing **global custody services**, or **international securities depository business** in the region.

In other words, there may be a hollowing-out of the international financial intermediation service function for Asia-based regional financial institutions in Asia. From this perspective, it can be argued that an Asian Bond and securities market is needed as a regional mechanism for directing savings in Asia toward investment in Asia.

In addition, Japan’s proactive involvement in initiatives to foster a bond and securities market in Asia will be instrumental in facilitating the globalisation of Japan’s financial sector and the enhancement of its competitiveness, which has declined significantly since the collapse of the bubble economy.

Former Malaysian Prime Minister Mahathir Mohamad and former Thai Prime Minister Thaksin Shinawatra have both advocated the establishment of an Asian Bond market in recent years. Their proposals are of tremendous importance and significance from the perspective of the region as a whole.

Good balance in the domestic financing profiles of Asian Countries

Any discussion of the issue of an Asian Bond and securities market requires that we correctly understand the status of the domestic capital markets in the major Asian countries.

There are two features of regional capital markets in particular that should be mentioned as background to the discussion.

First, domestic capital markets in the Asian region are achieving a good balance in their domestic financing profiles despite the prevalence of bank-centred indirect financing systems in the region.

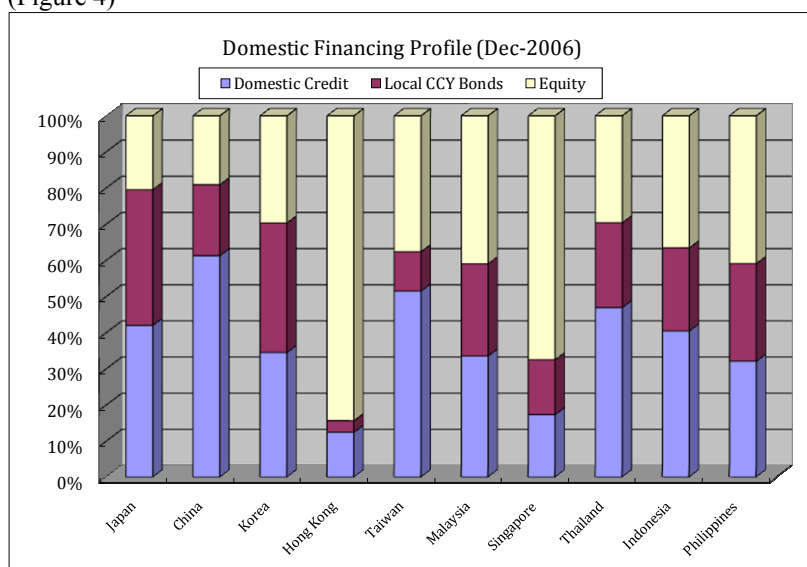
Asian financial markets have long been known as bank-centred markets. However, over the past few years, the proportion of financing in the bond market has increased in China, Korea and other countries.

As Figure 4 shows, the domestic financing profile, the split between banks, bonds and shares, is becoming well balanced in almost all the major Asian countries other than Hong Kong and Singapore.

The second feature of Asian financial markets is the policy of dividing the domestic and foreign markets.

Apart from Japan, many Asian countries are still applying strict control of foreign exchange, funds, and securities, and are limiting cross-border funds transfers between domestic and foreign markets, based on their experience in the currency and financial crisis of 97-98.

(Figure 4)



Source: BIS Quarterly Review, June 2007; data for Taiwan provided by the Taiwan Stock Exchange and the Central Bank of Taiwan.

Necessity for an AIR-PSM (Asian Inter-Regional Professional Securities Market)

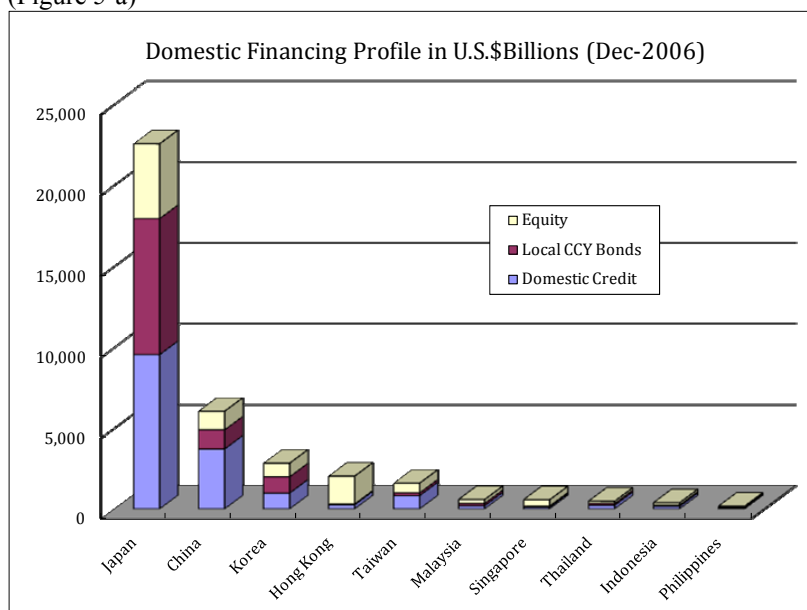
While the domestic markets of Asian countries have evolved, we still face the problem of the absence of common infrastructure for the creation of a common capital market in Asia.

An Asian Inter-Regional Professional Securities Market, which would enable the abundant savings in the region to be circulated within the region, is yet to be developed as an important element in a common capital market.

As indicated in Figures 5-a and 5-b, Japan, China and Korea are the largest domestic markets in the region, and cooperation between them will therefore be important in the development of an integrated inter-regional capital market.

The total scale of the markets in the region is more than 30 trillion US dollars.

(Figure 5-a)



Source: BIS Quarterly Review, June 2007; data for Taiwan provided by the Taiwan Stock Exchange and the Central Bank of Taiwan.

(Figure 5-b)

(In U.S. \$ Billions)

Market	Domestic Credit	Local CCY Bonds	Equity	Total
Japan	9,527.3	8,401.2	4,614.1	22,629.2
China	3,699.3	1,183.6	1,145.5	6,029.7
Korea	976.3	1,010.0	834.4	2,821.1
Hong Kong	255.1	51.0	1,715.0	2,036.1
Taiwan	818.9	173.0	595.6	1,587.5
Malaysia	193.8	146.2	235.6	576.3
Singapore	99.4	79.2	384.3	570.3
Thailand	223.3	109.7	140.2	475.0
Indonesia	154.6	87.6	138.9	381.1
Philippines	53.6	44.9	67.9	166.3
Total	16,001.7	11,286.4	9,871.2	37,272.5

Source: BIS Quarterly Review, June 2007; data for Taiwan provided by the Taiwan Stock Exchange and the Central Bank of Taiwan.

Given the level of diversity in the region, we do not believe that harmonisation is required at the level of the operations of each domestic capital market in the region. This is a virtually unachievable goal.

Instead, a common, integrated infrastructure will be necessary. By this we mean a cross-border market commonly accessible by Asian countries together, created by means of harmonising rules and infrastructure for professionals.

We may call such a market an AIR-PSM (Asian Inter-Regional Professional Securities Market).

The AIR-PSM would be a self-contained market enabling savings accumulated in the region to circulate within the region.

We can certainly see development in each of the domestic markets in the region as a result of several arrangements in which the ADB, Asian central banks and Asian governments have co-operated in the last several years.

However, it is time for us to concentrate on the establishment of an open and free market for professionals similar to the Eurobond market. Such a market would be different from domestic markets and also from NY and London.

One Asian investment banker's perspective

One Asian investment banker has commented as follows:

Asia has enormous capital reserves, and is rapidly forming capital via trade surpluses and economic growth.

Given this, there is no reason that Asian financial institutions cannot take the lead in Asian capital markets.

Isn't it somewhat strange that Asian issuers have to go to London or New York to obtain funds from Asian investors?

*Asia's capital markets are diverse, but it is essential for advanced financial institutions to integrate Asian capital markets **to provide Asian issuers with an option other than London or New York.***

Scale of Asian Bond Markets

The combined size of Asian bond markets is estimated at more than U.S. \$ 11 trillion, comprising nearly one-quarter of the total value (U.S. \$50 trillion) of the

world's domestic bond markets (Figure 6).

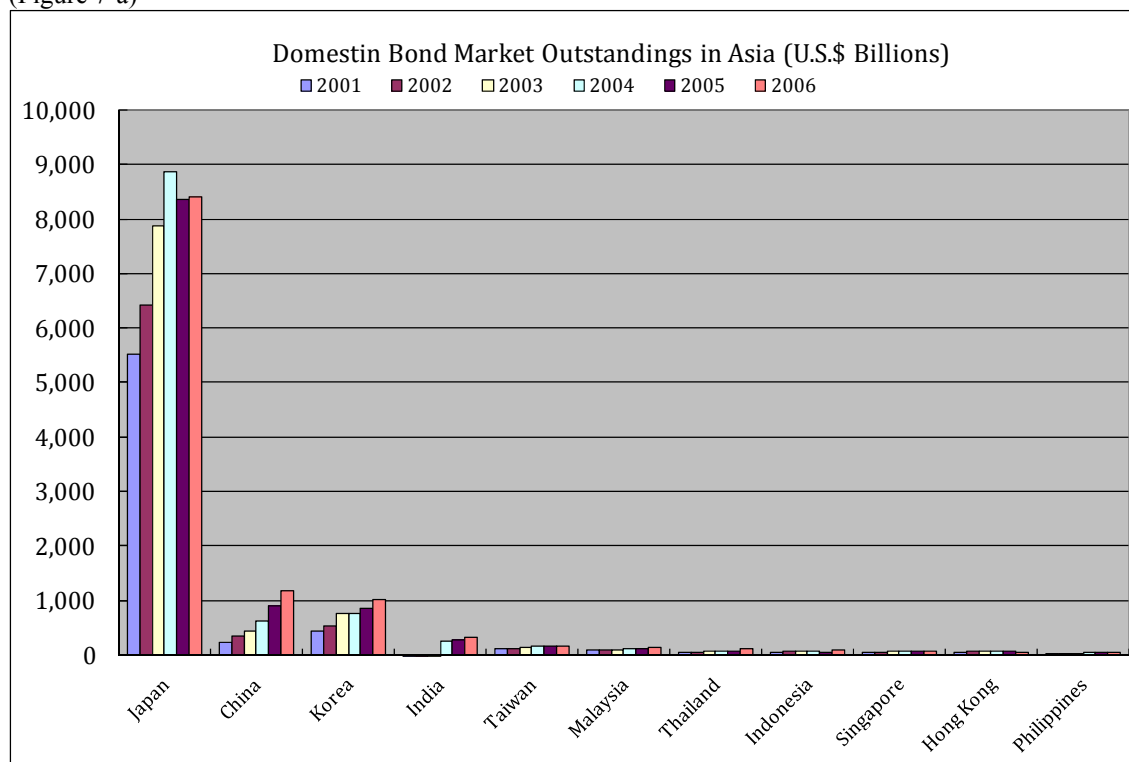
(Figure 6) Breakdown of the World's Bond Market Balances (2006) (In U.S. \$ Billions)

Region by residence of issuer	Corporate	Financial Institutions	Governments	Total Domestic	International Bonds
	a	b	c	a + b + c	
Global - Grand Total	5,746.7	20,530.2	24,008.6	50,285.5	18,448.9
U.S.	2,790.6	13,294.6	6,230.3	22,315.5	4,040.5
U.K.	23.1	379.4	835.1	1,237.6	2,509.1
Developed Europe (other than U.K.)	1,406.4	4,277.1	6,187.3	11,870.8	8,735.3
Offshore centers (other than HK,SG)	0.0	0.0	0.0	0.0	1,100.2
Japan	672.6	980.8	6,747.8	8,401.2	152.5
Offshore centers in Asia (i.e. HK,SG)	12.7	43.7	73.8	130.2	96.6
Asia other than Japan, HK and SG	496.9	673.2	1,910.6	3,080.7	227.7
Total Asia	1,182.2	1,697.7	8,732.2	11,612.1	476.8
Asia's ratio to World	20.6%	8.3%	36.4%	23.1%	2.6%
Others	450.4	881.6	1,916.8	3,248.8	999.3
International organisations	0.0	0.0	0.0	0.0	587.7

Source: BIS Quarterly Review, June 2007; data for Taiwan provided by the Taiwan Stock Exchange and the Central Bank of Taiwan. International bonds are classified by residence of issuer.

At the same time, Japan has the highest level of debt securities outstanding in the Asian region. The second largest bond markets in the region are those of China and Korea, which are significantly smaller than the Japanese market (Figure 7-a, b).

(Figure 7-a)



Source: BIS Quarterly Review, June 2007; data for Taiwan provided by the Taiwan Stock Exchange and the Central Bank of Taiwan, etc.

(Figure 7-b)

Domestic Bond Market Outstanding

(In U.S. \$ Billions)

	2001	2002	2003	2004	2005	2006
Japan	5,509.7	6,416.8	7,882.4	8,858.1	8,369.9	8,401.2
China	238.3	342.2	448.8	623.7	895.2	1,183.6
Korea	438.7	538.2	759.9	751.3	847.7	1,010.0
India	0.2	0.2	0.7	249.5	279.1	325.7
Taiwan	113.3	123.8	135.6	151.5	166.3	173.0
Malaysia	82.8	84.4	98.8	110.6	123.5	146.2
Thailand	37.2	48.3	59.6	68.0	80.5	109.7
Indonesia	49.2	58.2	65.7	61.2	54.7	87.6
Singapore	51.4	56.4	61.5	72.7	74.9	79.2
Hong Kong	52.1	58.1	60.5	62.9	65.8	51.0
Philippines	24.2	27.6	30.7	35.6	41.2	44.9
Total	6,597.1	7,754.2	9,604.1	11,045.1	10,998.6	11,612.1

Source: BIS Quarterly Review, June 2007, Taiwan Central Bank, ADB, etc.

These figures make the Asian bond markets collectively a close rival to the U.S. bond market in terms of scale. Asia's bond markets should not remain isolated as they are now. It is imperative to establish a **common "market"** to facilitate the effective allocation and efficient flow of long-term capital accumulated in Asia.

There are **two camps** in discussions related to the development of Asian bond markets. (Figure 8)

One prioritises the further development of domestic markets, or, alternatively, believes that domestic markets are sufficiently developed.

The other camp seeks to further develop domestic markets and at the same time to promote a cross-border inter-regional (offshore) market in the region.

This does **not** mean simply connecting domestic markets. A cross-border market would be, rather, a non-domestic market that co-exists within the region with domestic markets, but features the involvement of different players, rules and taxation schemes.

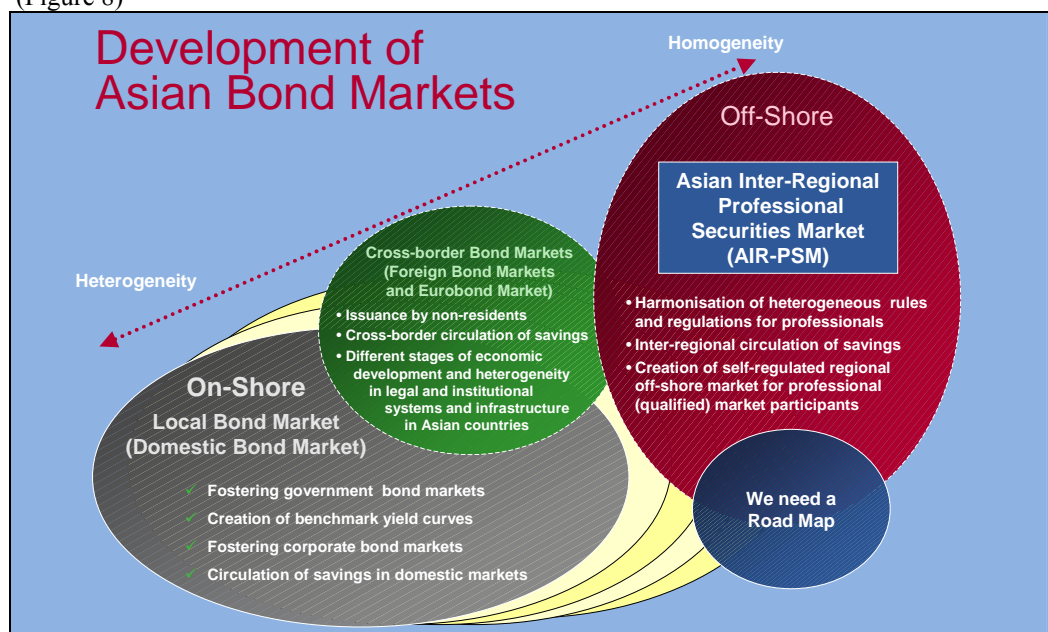
As an image of such a cross-border market, we might consider self-regulating markets like the Eurobond market. While the EU has recently tightened regulations and reduced the freedom of the Eurobond market, it has traditionally been regarded as a freely accessible market.

Cooperation between market players and regulators in Asian countries will be extremely important in the development of a **free and open market** of this type in the region. Because Japan is by far the largest market in the region, Japan should play a leadership role, and discussions involving Japanese market participants should be promoted and facilitated.

However, harmonisation of traditional independent market practice in each of the region's countries may not be viable. If many to many interoperability among domestic markets in the region is sought, the matrix will be extremely complex, and not optimal for the region as a whole.

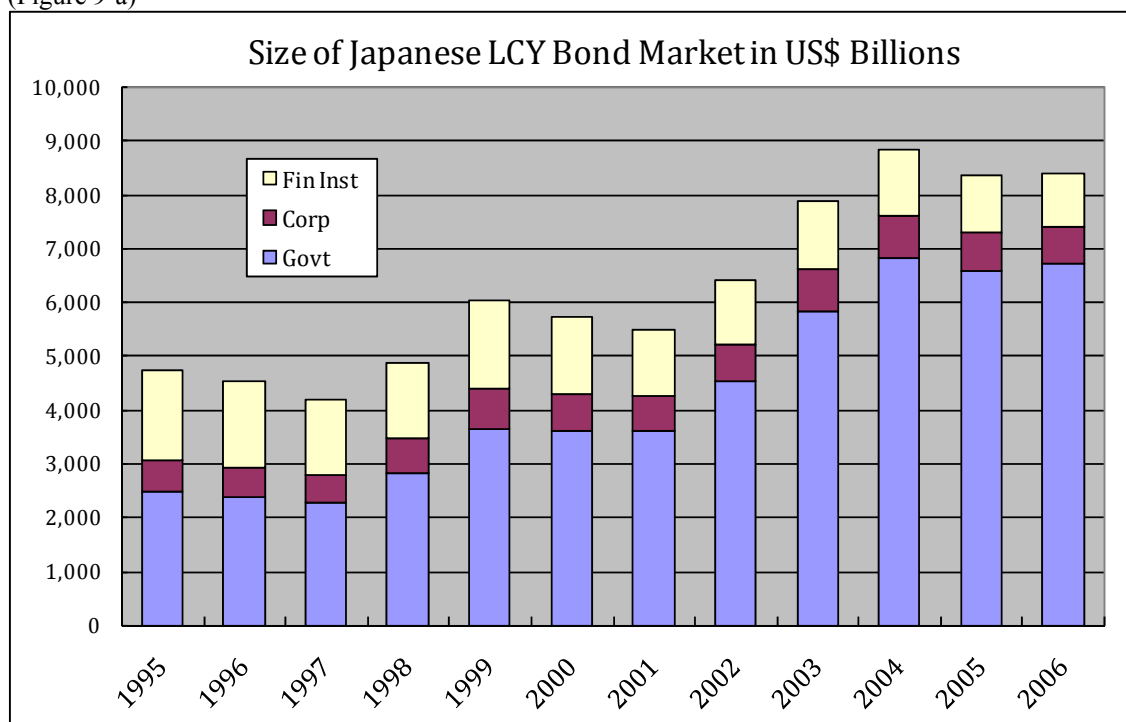
A preferable approach is to develop a common integrated market infrastructure for the requirements of professionals. Professor Hal S. Scott of Harvard Law School also indicates that off-shore integration is far more important than on-shore integration in the Asian region.

(Figure 8)



Looking at the individual bond markets in Japan, Korea, China and other Asian countries, we find that their composition is extremely simple for their size (Figures 9 and 10).

Although Japan has by far the largest outstanding balance of bonds, 80% are government and other public bonds, with only 20% made up of private sector bonds, including bank debentures and ordinary corporate bonds. Unfortunately, the balance of private sector bonds has not shown much growth in Japan (Figures 9-a, b, and c). (Figure 9-a)



Source: BIS Quarterly Review, June 2007

(Figure 9-b)

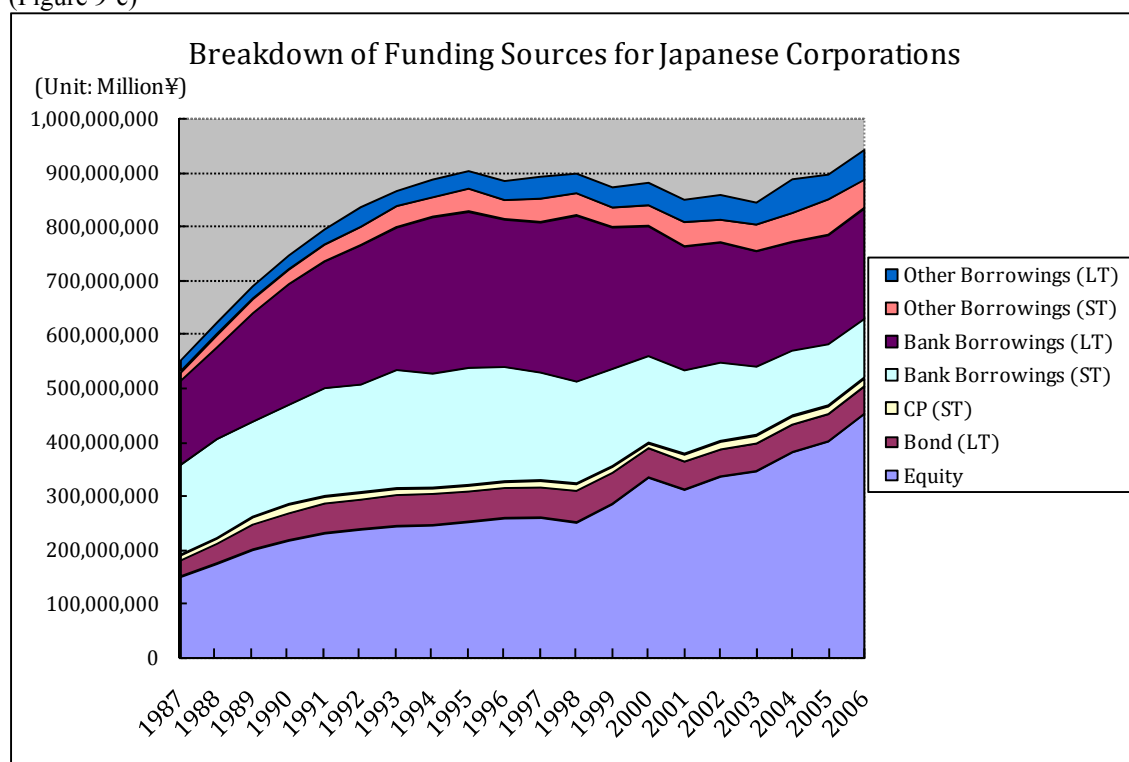
Size of Japanese Local Currency Bond Market

(In U.S. \$ Billions)

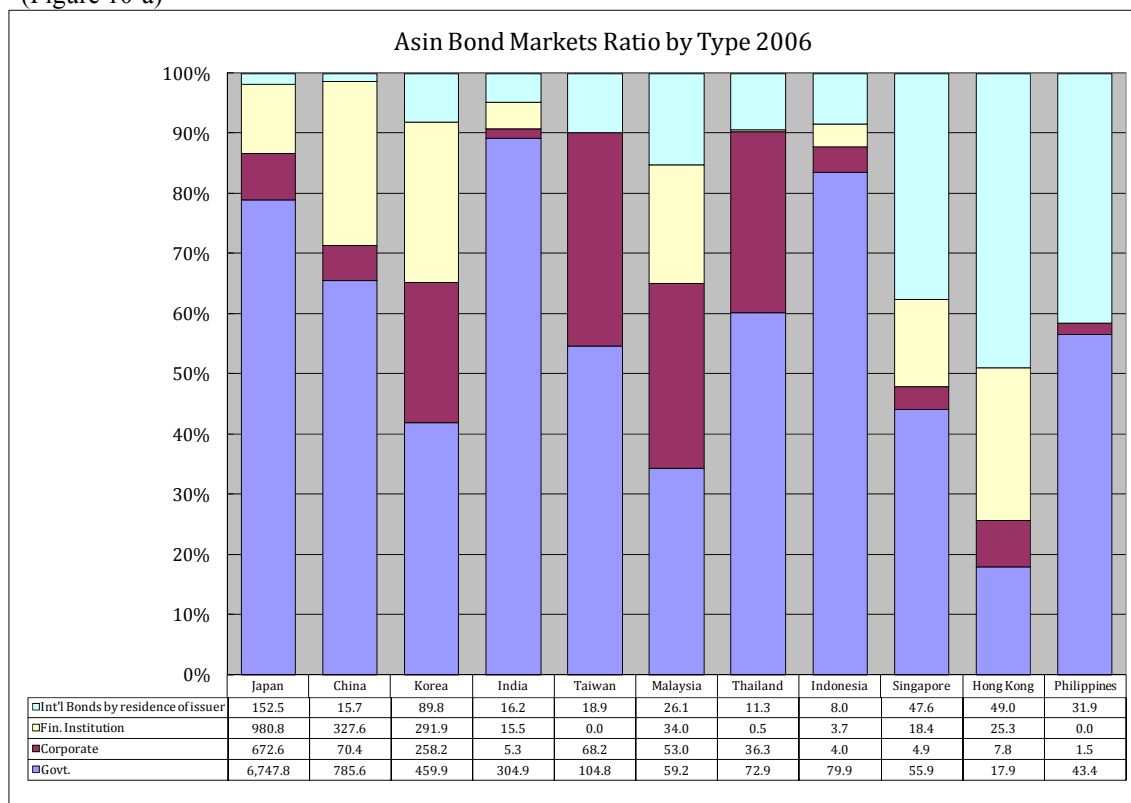
Date	Govt.	Corp.	Fin. Inst.	Total
1995	2,479.5	583.0	1,675.1	4,737.6
1996	2,393.6	562.1	1,574.9	4,530.6
1997	2,284.4	508.4	1,410.1	4,202.9
1998	2,832.7	648.6	1,422.6	4,903.8
1999	3,664.8	751.4	1,634.9	6,051.0
2000	3,618.1	678.5	1,440.6	5,737.2
2001	3,630.6	629.6	1,249.9	5,510.0
2002	4,543.7	701.9	1,171.4	6,417.0
2003	5,831.2	797.1	1,254.1	7,882.4
2004	6,836.7	787.4	1,234.0	8,858.1
2005	6,604.7	704.8	1,060.4	8,369.9
2006	6,747.8	672.6	980.8	8,401.2

Source: BIS Quarterly Review, June 2007, etc.

(Figure 9-c)



(Figure 10-a)



Source: BIS Quarterly Review, June 2007, Central Bank of Taiwan, ADB, etc. (In U.S. \$ Billions)

(Figure 10-b) Asian Bond Markets by Type 2006 (In U.S. \$ Billions)

	Government (1)	Corporate (2)	Financial Institution (3)	Domestic Market - Sub Total (1)+(2)+(3)	International Bonds by residence of issuer	Grand Total
Japan	6,747.8	672.6	980.8	8,401.2	152.5	8,553.7
China	785.6	70.4	327.6	1,183.6	15.7	1,199.3
Korea	459.9	258.2	291.9	1,010.0	89.8	1,099.8
India	304.9	5.3	15.5	325.7	16.2	341.9
Taiwan	104.8	68.2	0.0	173.0	18.9	191.9
Malaysia	59.2	53.0	34.0	146.2	26.1	172.3
Thailand	72.9	36.3	0.5	109.7	11.3	121.0
Indonesia	79.9	4.0	3.7	87.6	8.0	95.6
Singapore	55.9	4.9	18.4	79.2	47.6	126.8
Hong Kong	17.9	7.8	25.3	51.0	49.0	100.0
Philippines	43.4	1.5	0.0	44.9	31.9	76.8
Total	8,732.2	1,182.2	1,697.7	11,612.1	476.8	12,088.9

Source: BIS Quarterly Review, June 2007, Central Bank of Taiwan, ADB, etc.

As shown in Figure 10-b, the Chinese bond market, while on par with the Korean market in size, is also dominated by bonds issued by public institutions. The bond market in Korea is well-balanced among corporate bonds, financial institution bonds and government bonds and also maintains a specific level in terms of scale, as a result of tremendous efforts to promote the institutional development of the domestic financial and capital markets.

Looking at the percentage of corporate bonds in each nation's domestic bond market (Figures 10-a and 10-b), Taiwan, Malaysia, Thailand and Korea have relatively high

ratios.

Considering the size of the domestic economies of Asian nations and the fact that all of them commenced with indirect finance systems centering on banks, we can see that a considerable effort has been made with respect to private sector bonds, including corporate bonds, from the time of the Asian currency crisis in 1997 up to the present.

Need to Foster Asia's Financial and Capital Markets

Let us examine why and how we should promote regional financial and capital markets in Asia in the 21st century.

It has been repeatedly pointed out by experts that one of the causes of the Asian financial crisis was the fact that there was no infrastructure enabling the abundant savings held in Asian nations to be circulated within the region. While the series of initiatives taken by Asian countries, including the Chiang Mai Initiative, a mutually supportive network designed to help countries in the event of a crisis agreed upon among ASEAN, Japan, China and Korea in 2000, are important as a short-term response, the idea has come to the fore that in order to prevent a recurrence of a similar crisis and to enhance market competitiveness over the medium and long term, Asia needs to establish integrated bond and financial markets which enable Asian capital to be invested within the region over the long term, in addition to further developing each country's domestic financial market.

Significance of Global Flattening of Yield Curves

The U.S. Federal Reserve Board began raising the federal funds (FF) rate target in mid-2004 and pushed it up by more than 4 percentage points from 1.00% at the time to 5.25% in July 2006. Meanwhile, yields on long-dated U.S. government bonds did not increase significantly, with 10-year yields standing at levels just below 5% as of September 2006. This phenomenon is often referred to as a flattening of yield curves.

In his congressional testimony in February 2005, then Federal Reserve Board (FRB) Chairman Alan Greenspan called it a "conundrum." At the time, however, the FF rate target stood at 2.5%, while 10-year bond yields were just above 4%. The flattening trend has increased in pace over the last one and a half years. In June 2006, new Chairman Ben Bernanke observed that it is difficult to narrow down the factors behind the flattening of the yield curve, and low long-term interest rates are complicating decisions on monetary policy.

It is not well-known, however, that **the flattening of yield curves is not limited to the United States but has spread to bond markets around the world**, including emerging markets. Several factors occurring simultaneously around the world appear to be causing the flattening, including global steady inflation rates, global money gluts and strong appetites of pension funds and other institutional investors for domestic long-term bonds.

However, of particular importance is the fact that inflation has been tamed in emerging economies around the world. Encouraged by this development, these countries, in their efforts to divest themselves of the status of developing economies and promote savings and investment in their own or regional currencies, are overhauling old systems built around bank-oriented indirect finance and moving ahead with the development of new systemic infrastructure for financial and capital markets, including bond markets. In Asia, this trend is reflected in the drive towards the establishment of

an Asian Inter-Regional Bond Market.

The flattening of yield curves, seen even in countries in which yield curves were non-existent until recently, may be construed as a signal indicating the necessity for the full development of regional as well as domestic bond and capital markets.

Development of “Asian Standards” and Shared Regulations and Infrastructure for Financial and Capital Markets

The establishment of an Asian Bond market has to date been promoted by financial authorities, central banks and politicians in the nations concerned. Going forward, cooperation among market professionals, financial institutions, research institutions and policymakers will be important.

In particular, given the importance of the Japanese market, market participants, including Japanese companies, financial institutions and institutional investors, should take the initiative and cooperate in reforming the domestic financial and capital markets as the core of the Asian financial and capital markets.

In order to ensure further social and economic development in Asia, in addition to efforts to develop and strengthen domestic bond markets by Asian countries, it is necessary to foster inter-regional (cross-border) financial and capital markets (=AIR-PSM) within the region and develop various institutional foundations of markets as a regional harmonised market infrastructure, functioning to organically link the respective domestic markets in the region.

To that end, innovation of **market-related soft infrastructure** has become necessary, including common legal systems and self-imposed rules that would support the region’s financial and capital markets.

Simply carrying out these initiatives in sequence can be expected to lead to the establishment of **unique “Asian standards,” a set of common principles of market governance, and infrastructure for an Asian Inter-Regional Professional Securities Market (AIR-PSM).**

(Shigehito Inukai)

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2. International Bonds:

Definitions and Explanations - What are Eurobonds and Foreign Bonds?

The term **Eurobonds** does not refer to bonds issued in the Euro zone. It refers to bonds denominated in specific currencies and issued on markets other than the domestic markets of those currencies.

In other words, Eurobonds are bonds that are not registered on their respective domestic markets. They are bonds meant for cross-border clearing and settlement that are usually traded internationally by international syndicates. They are called “**Euro-yen bonds**” when denominated in the Japanese yen, “**Euro-dollar bonds**” when denominated in the U.S. dollar, and “**Euro-euro bonds**” when denominated in the euro.

Because the **Eurobond** market is essentially beyond the reach of control by the monetary authorities of individual countries, it has to date functioned as a free market with minimal regulations.

However, the originally free **Eurobond** market is beginning to become subject to the regulations that are being created for the immense “national” territory represented by the European Union. Some commentators therefore claim that Eurobonds are turning into a type of domestic bond that is issued and traded within the framework of **quasi-national regulations** in the region of Europe.

However, this assessment is premature. At present, the EU is attempting to create an entity that transcends national borders. The imposition of regulations from this level on the Eurobond market for the sake of its more sound development should not necessarily be regarded as negative, assuming that the public and private sectors cooperate in the establishment of those regulations.

Foreign bonds are bonds issued by nonresidents and denominated in the currency of the issue market. They are termed “**Samurai bonds**” when issued in the Japanese market and “**Yankee bonds**” when issued in the U.S. market.

Eurobonds and these **foreign bonds** may be termed **international bonds**.

Bonds issued by residents, usually denominated in the currencies of the country of issue, are called **domestic bonds** when payments for bond purchases, interest payments and redemptions are all conducted in the country of issue.

Given the above definitions, **Asian Bonds** or **Asian Inter-Regional Bonds** would be identical with **Eurobonds** in their original sense, as traded on a free market, and would be a type of **international bond**. Asian Bonds, however, would be bonds denominated in Asian currencies that could be traded freely within and outside Asia on a common non-domestic bond market (i.e., an Asian Inter-Regional Professional Securities Market).

(Reference is made to relevant sections of Keiji Matsumoto, “Cross Border Securities Transactions and Corporate Finance,” Kinzai Institute for Financial Affairs, Inc., 2006):

It is now presumably well known that the **Euromarket** is neither the Euro market,

in which the EU's common currency circulates, nor Europe at large. However, there are probably few people who could give a ready answer when asked what the Euromarket is **in legal terms**.

Legally and historically speaking, the Euromarket has been a market that **is exempt** from the legal regulations that exist for the protection of the investing public in each of nations free of securities and foreign exchange control regulations, including the euro zone.

In the relatively liberalised markets of industrialised nations including Japan, the definition of professional investors is made, and professional investors are exempt from regulations under their respective national laws.

The global federated markets in which these investors operate may be defined as the Euromarket from the legal perspective.

Investment funds are professional investors, and individual investors can participate in trading on the Euromarket through investment funds.

(Shigehito Inukai)

3. Proposal for the Establishment of an Asian Inter-Regional Professional Securities (Asian Bond) Market - A Road Map to an Asian Bond Primary Market -

Executive Summary

Upgrading of Market Participants and Market Infrastructure in the Asian Region

The development of an Asian financial and capital market as a regional asset is vital to the development of an Asian economic community. The upgrading of regional market infrastructure and the ability of market participants is an essential condition for the development of this market.

We must engage in full-fledged efforts to nurture financial professionals in Japan and Asia capable of “playing” in the global arena and build an international standard “**stadium**” for these players, in order to overcome the backwardness in the development of the Japanese and Asian markets.

The creation of a professional league, like the **J-League** and **Asian League** in the world of professional soccer, is necessary in the world of the financial and capital markets.

Leadership of this league should first be assumed by Japan and South Korea, which lead other Asian nations in terms of the scale and level of development of their domestic capital markets.

Necessity for an “Asian Inter-Regional Bond Market” as the Primary and Secondary Market for International Bonds

Recent developments in East Asia centering on Japan, have created the basic conditions, with efforts on the part of the relevant actors, for the establishment of an inter-regional financial market, like the Eurobond market, in which market professionals are able to freely conduct transactions. Such a market would ensure the further development and continued competitiveness of the region.

The establishment of market infrastructure such as legal systems and settlement systems has made some progress in the domestic financial and capital markets of major countries in the region. However, the development of a self-contained “Inter-Regional Bond Market” in Asia, a market in which international bonds are issued and traded, has been decisively delayed. Moreover, there is little recognition of the necessity for such a market.

With regard to international bonds, market participants in Asia still depend on the Eurobond primary and secondary markets, a cooperative system involving Britain and the three Benelux countries predicated on the utilisation of financial institutions in London and international securities clearing and settlement systems based in Europe.

In other words, it is a given that, outside domestic markets, the dealers and professionals (including **intermediary agents** involved in issuance, trading and redemption, rating organisations, lawyers and accountants) involved with securities issued by Asian issuers, and the systems (securities clearing and settlement systems and related legal systems, etc.) relevant to those securities, will not be Asian, but will rather

be based upon Eurobonds market system.

Given this, issuers in Japan and other Asian nations do not enjoy the same cost advantages or the same convenience (issuing in their own currencies, etc.) as European or U.S. issuers.

International bonds denominated in Asian currencies other than the Japanese yen face a variety of constraints in issuance and secondary market trading not only within their own countries but also in the Eurobond market. In addition, an environment enabling Asian financial institutions, including Japanese financial institutions, to hone their professional skills in order to compete with their European and U.S. counterparts on equal terms has not been fostered.

The establishment of an Asian Inter-Regional Bond Market (a Eurobond-type Asian Bond market) the type of shared regional offshore market that has not yet clearly taken shape in Asia, would not only be of great significance in providing a venue for the nurturing and training of regional professionals and the generation of market innovations, but also as creating a self-contained, highly cost-effective international bond market that also enables trading in bonds denominated in the respective currencies of the nations of the region, enabling regional savings to circulate within the region.

The realisation of such a market would require the establishment of a variety of different types of market infrastructure for a Eurobond market-type Inter-Regional Bond Market, based on specifically Asian elements and requirements.

By linking the domestic markets of Asian countries in a natural and organic manner, it would have the function of preventing a regional spread of economic contagion, as seen in the Asian financial crisis.

At present, what is required are more concentrated efforts to remove a variety of immediate institutional constraints (constraints in domestic legal systems, including inadequate familiarisation, constraints in tax laws, the absence of an efficient international securities clearing and settlement system) on the initiative of major market participants in the countries of the region, including Japan.

The potential for the development of an economic community is beginning to be apparent in East Asia, and it may be assumed that the main issuers and investors in an Asian Inter-Regional Bond Market would come from Asian nations. The involvement of market participants from outside the region would also be assumed. In other words, an Asian Inter-Regional Bond Market would be **open** to markets and market participants around the globe.

Creation and Sharing of a Vision for an Asian Inter-Regional Bond (Asian Bond) Market is Required

The Asian Bond Markets Initiative (ABMI), which has been promoted by Asian governments and the Asian Development Bank (ADB) over the past several years, is an extremely important initiative, and has produced a variety of important achievements.

More than ever, it is necessary now for market participants (market professionals) such as public sector securities-issuing organisations, private sector issuers, brokerage firms and institutional investors, all of which should be participants in an Asian capital market, to develop and share a vision for an Asian Inter-Regional Bond (Asian Bond) Market.

Proposal for a Road Map to an Asian Inter-Regional Bond (Asian Bond) Primary Market

The major points of the proposal are:

- (1) Necessity for market for Asian Inter-Regional Bonds (Asian Bonds) denominated in Asian currencies and proposal for a concrete program (road map) for its realisation,**
- (2) Proposal on points to consider regarding legal systems for an Asian Inter-Regional Bond (Asian Bond) Market (for Japanese issuers, Asian Bonds should be clearly defined as different from domestic corporate bonds under the new Japanese Company Law and should be issued with Japanese law as the governing law; we consider this to be possible),**
- (3) Proposal for the establishment of the Capital Market Association of Asia (CMAA), (CMAA was established in 2007)**
- (4) Proposal of a Dual Core approach as the securities clearing and settlement method.**

Background to the Proposal

The National Institute for Research Advancement (NIRA), in cooperation with the Corporate Finance and Treasury Association of Japan and the Japan Capital Markets Association (JCMA), launched the Study Group on Principles and Rules for a Regional Market and the Study Group on Integrated Regional Market Infrastructure (Chairperson: Prof. Hideki Kanda of the University of Tokyo Graduate School of Law) in July 2005 for the purpose of formulating proposals for a strategic vision toward the integration of financial and capital markets in East Asia.

Following this, consultations were held with market professionals, working group meetings were organised as required, and several exchanges of views were held with South Korean capital market experts in Japan and South Korea. In 2006, South Korean market experts who share a common sense of purpose with the team members volunteered to join the study groups, and intensive discussions were held between teams of Japanese and South Korean market experts. Since late 2005, the team has also been exchanging views with the Asian Development Bank (ADB), which has been promoting the Asian Bond Markets Initiative (ABMI).

On March 27, 2006, a **NIRA-ADB joint forum** was held in Tokyo, at which the results of studies conducted over the past eight months were presented to participants as a NIRA policy proposal (interim report). At the conclusion of the forum, the draft proposal prepared by the NIRA study team was endorsed by approximately three-quarters of the participants. The results of a questionnaire survey conducted following the forum are shown on Page 53.

The revised proposal presented in this paper is based on discussions held at the forum, and also reflects further consideration and discussion by study group members and other relevant individuals following the forum.

We would also like to mention the fact that this proposal has been formulated on the basis of voluntary and future-oriented collaboration and cooperation between private sector market experts in Japan and South Korea.

Detailed Discussion

Background: Basic Role of a Local Currency-Denominated Asian Bond Market

The main factor that brought about the Asian financial crisis and that also lies behind the continuing instability of the Asian currencies and economies is the dollar peg system. In other words, the major causes of these problems are the requirement for the revaluation of Asian currencies against the U.S. dollar and bloated foreign exchange risks associated with issuing securities denominated in dollars.

On the other hand, while settlements for regional trade among Asian countries are made in U.S. dollars, the dollars used in trade settlements are exchanged into the respective currencies of the countries involved; as such, the countries' own currencies can be said to be used in regional trade. Therefore, an Asian Bond market using local currencies would save these countries foreign exchange fees, and to the extent that they are backed by export claims (particularly long-term claims such as exports of plants), the existence of exchange risk-free local currency-denominated debts is necessary and warranted.

In addition, long-term capital remains fixed in local currencies when capital is exported to establish production bases in other countries. If funds for direct investment could be raised by issuing bonds denominated in the currencies of the countries in which production will be carried out, the issuers would be able to avoid exchange risks.

From the 1970s onwards, Japanese companies procured the funds necessary to support their rapid growth in the Euro capital market in the form of low-cost equity financing (convertible bonds and bonds with warrants); European and U.S. investors invested in Japan's high economic growth.

At present, the same relationship can be observed between Japan and South Korea, East Asia's industrialised nations, and the ASEAN nations, which are trying to catch up with them. Japanese and South Korean institutional investors, including investment trust funds, can play the role of providers of capital in yen-denominated and won-denominated equity financing by companies from ASEAN nations. This is clearly shown in the current BRICs boom.

In Asia, a broad practical base for the above-mentioned local currency-denominated bonds and equity-linked bonds already exists in the form of trade and direct investment. In addition, physical distribution is very active given the close geographical proximity of countries in Asia, and it therefore goes without saying that local currency-denominated bonds and equity-linked bonds are necessary and warranted in the region.

What is described above represents a flow of economic activities that would be generated naturally without any policy initiatives from the governments of countries in the region. Given the circumstances of foreign exchange policy, the degree of liberalisation of currency trading and accounting and disclosure practices in the various countries of the region, however, the starting point should be an Asian Inter-Regional Bond Market created by professional investors, on the model of the Eurobond market.

The Eurobond market itself remains fundamentally restrictive to major Asian currencies other than the Japanese yen. Given the fact that even the Korean won still

faces limited access to the Eurobond market, bonds denominated in other Asian currencies will find it difficult to utilise the market for some time to come.

Individual Issues and Assumptions

Q: How should we proceed with the building of a 21st century Asian common inter-regional bond market? Specifically, what problems will have to be dealt with in establishing a common Asian market infrastructure in financial and capital markets?

A: First, Asian countries need to harmonise their professional market-related legal systems. To date, financial authorities, central banks and politicians in Asian countries have made extraordinary efforts towards establishing an Asian Bond market. At present, continued efforts are under way within the framework of the ASEAN+3 Asian Bond Markets Initiative (ABMI), led by the Asian Development Bank (ADB) with the support of regional finance ministries. What will be important in future, in our opinion, is multifaceted cooperation among market professionals, financial institutions, think tanks and policymakers.

In particular, given the importance of the Japanese markets, Japanese issuing companies, institutional investors and others involved in market activities need to take the initiative in reforming Japan's domestic financial and capital markets as the core of the Asian financial and capital markets.

In addition, for the sake of the socioeconomic development of Asia, it will be necessary to foster regional financial and capital markets that transcend the boundaries of domestic markets as common regional professional market infrastructure, and establish the institutional base for such markets. What is necessary to that end is common Asian institutional systems that go beyond the existing frameworks of each country and support common financial and capital markets in the region.

For example, flexible and simple systems need to be put in place to ensure that legal, tax and other systems related to domestic financial and capital markets will not hamper issuance and secondary trading of international securities on the offshore markets.

We also need to develop simple rules to govern the disclosure and registration of information regarding such securities as well as international securities clearing and settlement systems (which should be designed to be self-contained within the Asian region to make the use of Europe-based clearing and settlement systems unnecessary).

Furthermore, it is hoped to develop a venue (presumably, a stock exchange) to list (i.e., disclose and register) securities that are issued in the joint inter-regional bond market rather than in the domestic markets of participating countries.

We also need to create an independent organisation of market participants to formulate voluntary trading rules for the joint inter-regional bond market.

What is required is specifically Asian soft infrastructure innovation to create an inter-regional securities market that can rival other existing international markets, including the Eurobond market, which has developed an integrated total system for registration of disclosure documents, clearing and settlement of securities, and issuance and secondary trading through the cooperation of Britain and the three Benelux

countries, and which is the representative primary and secondary market for free trading of international securities issued by blue-chip issuers.

Fundamentally, securities denominated in Asian currencies other than the Japanese yen still face a welter of constraints in issuance as well as in secondary market trading not only within the borders of the countries in which they are issued, but also in foreign bond markets including the Eurobond market. For example, in the Eurobond market, securities denominated in Asian currencies other than the yen either cannot be issued institutionally, are difficult to issue or are subject to delays in clearance and settlement. The establishment of an Asian Inter-Regional Bond Market which can accommodate issuance and secondary market trading of local currency-denominated bonds by Asian issuers would therefore be of great significance, in that it would enable issuance to be competitive even in terms of issue cost, which is impossible on the Eurobond market.

However, there are two important conditions:

- (1) The infrastructure of an Asian Inter-Regional Professional Securities Market should be designed to accommodate not only bonds but also issuance and secondary market trading of equity securities, and
- (2) A common Asian Inter-Regional Professional Securities Market infrastructure established in Asia should not be restricted exclusively to use by market participants from the Asian region. Asian market participants must not forget the fundamental requirement:

we need to build an advanced and open inter-regional securities market infrastructure in Asia, one that is open to all participants in global capital markets.

Continued efforts by means of independent and voluntary cooperation among governments, issuing companies, securities underwriters, rating organisations, lawyers and other market professionals and researchers in Asian countries should lead to the establishment in the near future of common market governance principles that can be termed “Asian Bond Standards” or “AIR-PSM Standards.”

Japanese market professionals and market experts, in addition to the Japanese government, as “all-star players” in the “Asian league,” have a tremendous responsibility to assist in this procedure.

“Asian Bond Standards¹” – Towards an Asian Bond Market

The Asian Bond Markets Initiative has been launched, and specific issues relevant to the development of an Asian Bond market are now being considered by the

¹ (Reference) The new agenda agreed upon at the ASEAN+3 Finance Ministers’ meeting held in Istanbul on May 4, 2005.

1. Study on the possible issuance of Asian currency-basket bonds (a Japanese proposal in the road map to the ABMI) - Seek economies of scale for the region as a whole by creating a common bond-issuing currency
2. Self-assessment by member countries (a Japanese proposal in the road map to the ABMI) - Seek to foster a more user-friendly bond market, with member countries conducting studies of obstacles to investment in an Asian Bond market pointed out by market participants.
3. Asian Bond Standards (a South Korean proposal) - Conduct a long-term study on the fundamental requirements for fostering an international bond market in East Asia (establishing market infrastructure and issuing procedures, etc.)

governments and finance ministries of Japan and other Asian countries, with the Asian Development Bank serving as secretariat. A variety of important achievements have already been made. Among these was the proposal of Asian Bond Standards in Korea.

To build on these achievements and to help further facilitate the realisation of the initiative, a NIRA research project is being carried out by a team led by market participants to offer concrete and highly feasible proposals regarding the development of market infrastructure, issuing procedures and other issues, which may be termed **Asian Bond Standards**.

The issues and points for consideration that have to date been identified in this research are discussed below.

Issues and points for consideration:

1. Is it possible to develop an Asian version of the flourishing Eurobond market (which centers on Britain and the three Benelux countries) by employing the basic features of the self-imposed rules for the Eurobond market (the rules first set by the IPMA² and inherited by the ICMA³), but as a uniquely Asian market created by Asian market participants?
2. Instead of a grand design encompassing the entirety of the primary and secondary markets, is it feasible to commence with an intensive consideration of issues related to a **primary market** for Asian Bonds, given that it is more realistic and of greater importance and necessity? Considering the scale of the domestic financial and capital markets of Asian countries, the levels of understanding among market participants and the degree of development of relevant domestic legal systems and other infrastructures, it would be of great significance if Japan and South Korea were to cooperate in this consideration (We might recall here the successful hosting of the World Cup by Japan and South Korea).
3. What role should Japanese market participants play to that end? Who should take the initiative among government agencies, public and private sector issuers, regional economic bodies, intermediary organisations and investors? (Issuers may be of the greatest importance because they take the initial action in issuing securities). How should the role of intermediary organisations, particularly financial institutions that operate in cross-border Asian financial and capital markets, be considered?
4. South Korea can be an important partner for Japan as its market is the second largest in Asia after Japan's and it is seriously addressing the utilisation of market functions. What institutional constraints and obstacles to progress in the project exist in South Korea?
5. Among specific points for consideration, the following items can be considered of particular importance (for more detail, see the attached "Road Map to a Primary Market for Asian Inter-Regional Bonds (Asian Bonds)"):
 - ① It is necessary to establish a "Capital Market Association for Asia" (CMAA) (in the initial stage, looking toward the creation of a primary market for Asian Bonds led by the private sector) consisting of Asian issuers and Asian financial institutions, etc.

² IPMA: International Primary Market Association

³ ICMA: International Capital Market Association

② How should issuing procedures and syndicate rules be developed for Asian Bonds as Eurobond-type Inter-Regional Bonds (international bonds not issued on domestic markets)?

③ How should legal frameworks for issuance of Asian Bonds be shaped (and which countries' legal systems should be chosen as the basis for them)?

- There are calls for recognition under the new Company Law that Japanese issuers of foreign bonds (including Asian Bonds) should be able to use Japanese law as governing law, and to make this point explicit in the Company Law Enforcement Regulations. The CMAA proposal discussed below is part of this movement.

The requirement for the assignment of commissioned banks for corporate bonds under the Company Law will not represent a constraint in the development of “Made in Japan” international bonds (foreign bonds), because the requirement can be waived and a fiscal agent (FA) appointed

1) in the event that the value of each bond is one hundred million yen or higher (based on a conditional clause of Article 702 of the existing Company Law), and

2) in the case that a figure of less than 50 is obtained when the total value of the bond issue is divided by the lowest value of the individual bonds (Article 169 of the Company Law Enforcement Regulations). In addition,

3) **the CMAA is proposing that in the specific case of foreign bonds, the requirement for the assignment of a commissioned bank could be waived if offerings are made exclusively to professional investors, which are not bound by the securities and foreign exchange regulations of their home countries.**

- Can South Korean issuers issue bonds using South Korean laws as governing law?

Are there any problems with capital controls?

What are the constraints under the South Korean legal system and how can they be reconciled?

④ How should the clearing and settlement infrastructure for Asian Bonds as Eurobond-type Asian Inter-Regional Bonds be addressed?

How should Eurobond-type Asian Inter-Regional Bonds in Asia be designed so that they are not regarded as domestic bonds even when they do not utilise the European settlement systems?

As one suggestion, we propose a Dual Core Asian International CSD (central securities depository) approach. This proposal is based on a consideration of how two major international central securities depositories, Euroclear (Belgium) and Clearstream (Luxembourg), are utilised.

The Dual Core Asian International CSD approach means that when residents of Japan issue Asian Inter-Regional Bonds, they would use the South Korean CSD as the international central securities depository (ICSD), and when residents of South Korea and other non-Japanese issuers issue Asian Inter-Regional Bonds, they would use the Japanese CSD (Japan Securities Depository Center, and others) as the international central securities depository (ICSD).

Utilizing the central securities depositories that exist in different Asian countries as “Dual Core” ICSDs, just as Euroclear and Clearstream are utilised, it would

be possible to create a self-contained Asian Inter-Regional Bond Market in which Asian Bonds could be issued and traded within Asia without relying on the two major central securities depositories in Europe.

Incidentally, when bonds issued by British residents are cleared and settled through Euroclear or Clearstream, those bonds are recognised as Eurobonds (international bonds), rather than as British domestic bonds. It should be noted that bonds issued by Belgian residents are recognised as Eurobonds only when they are cleared and settled through Clearstream, not through Euroclear.

- ⑤ How should withholding taxes, which are supposed to be exempted on the international bond markets, and other taxes be treated in the Asian Bond market?
- ⑥ How should disclosure of information and registration of disclosure documents (registration, filing or listing) be handled for Asian Inter-Regional Bonds, which are international bonds? (For example, could the Tokyo or Osaka Securities Exchange be used as the junction point with Asia?)
- ⑦ It may be necessary to re-acknowledge and re-affirm the roles of Japanese and Asian financial institutions regarding international securities underwriting, corporate bond management and comprehensive investment management (global custody business).

(Shigehito Inukai)

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4. Proposal concerning a Road Map to an Asian Inter-Regional Bond (Asian Bond) Primary Market

Based on the view that we should commence with what is immediately feasible, the table below provides an outline of the market infrastructure, which may be termed **Asian Bond Standards or AIR-PSM Standards** that should be developed as a framework for the primary market (setting aside the secondary market for the moment). This road map is based on discussions between Japanese and Korean experts and the discussions at the NIRA-ADB Joint Forum held on March 27, 2006.

In preparing the framework below, the author drew upon the “Framework for a Road Map for an Asian Bond Format Modeled on the Eurobond Format,” circulated in a memo regarding “Asian Bond Standards”⁴, a new agenda for discussion in the ABMI proposed by Korean experts and agreed upon at the ASEAN+3 Finance Ministers’ Meeting held in Istanbul on May 4, 2005.

Road Map to an Asian Inter-Regional Bond Primary Market⁵

Category of proposal	FY2006-7 (Starting Point)	FY2007-8 (Original target year (at the point of 2006) for enforcement of the Investment Services Law [Financial Instruments and Exchange law] of Japan)	FY2009-10 (Original target year for enforcement of the Japanese version of the Financial Services and Markets Law)
1. Issuing Procedure	ICMA (the market association for the Eurobond market)	An Asian self-regulatory organisation → Creation of CMAA ⁶ (Initially, an association of issuers and issue markets in Asia)	Harmonisation by legal enforcement + CMAA
2. Syndicate rule (Subscription rules)	Eurobond syndicate (ICMA)	Asian Bond market primary standards (A model to be created on the basis of ICMA rules)	Asian Bond market primary standards
3. Governing Law (Issuing) (Governing law for issuance)	English law (“Made in the U.K.”) Due to constraints under the Commercial Code in Japan, since 1993 all bonds have been issued under English law	Laws of Asian countries ⁷ <ul style="list-style-type: none"> ▪ It has been confirmed that Asian Bonds as foreign bonds, can be issued under Japanese law (Made in Japan) (CMAA proposal P.46) ▪ Whether laws in Korea, an OECD member state, can be used as governing law needs to be verified ▪ Singapore law, others (In the Eurobond market, the accepted practice is to allow issuers from advanced countries to issue bonds under the law of their home countries)	Laws of Asian countries

⁴ http://www.mof.go.jp/english/if/regional_financial_cooperation.htm

http://asianbondsonline.adb.org/documents/Asian_Bonds_Standard_2005_May.pdf

⁵ It will be necessary to study rules for the secondary market separately as the primary market develops.

⁶ CMAA: Capital Markets Association for Asia

⁷ See Keiji Matsumoto, “Cross Border Securities Transactions and Corporate Finance,” Kinzai Institute for Financial Affairs, Inc., 2006

4. Settlement- (Please refer P.47-51)	Euroclear (Brussels, Belgium), Clearstream (Luxembourg)	Dual Core ⁸ Asian Inter-Regional CSD Approach (As a realistic solution enabling the early launch of the market, approach using custodian services (Plan C), and setting up a new and simple “Asian Inter-Regional CSD” (Plan A and A’) are option)	Dual Core Asian Inter-Regional CSD or Asian Inter-Regional (Core) CSD
5. Withholding Tax	Depending upon the policy of issuer’s country	May be exempt, based on the use of International Settlement as discussed above (to be confirmed)	Depending upon the policy of issuer’s country
6. Accounting Standards	Decided by country of bond issuer	Harmonisation of some accounting standards (Differences with international standards can be dealt with by specifying the differences)	International accounting standards are hoped
7. Disclosure (Filing) (including the filing of an Asian MTN Programme)	Securities exchange (Mainly LSE, Lux)	Major securities exchanges in Asia ▪ JPN (For instance, Tokyo or Osaka Securities Exchange) ▪ KOR (KRX) ▪ SGP (SGX)	Securities exchange (JPN, KOR (KRX), SGP (SGX), etc.)
8. Electronic disclosure	Introduced by each country	Harmonisation of regulations, linkage with EDINET ⁹ with XBRL	Harmonisation of regulations, linkage with EDINET
9. Documentation	Use of Eurobond (ICMA) format	Development of Asian Bond format (CMAA will develop a model format)	Use of Asian Bond format
10. Credit ratings	Market practices, market judgment	Market practices, market judgment (Market practices, including use of Japanese rating organisations)	Market practices, market judgment

With an eye on future progress toward the Asian Currency Unit (ACU) for Asian currency basket bonds now under consideration by the ADB, and in a bid to help make the positive efforts being exerted more fruitful, it seems essential to implement extra measures and, for example, create ACU-denominated bond futures and currency futures markets on securities exchanges within Asia (on the Tokyo or Osaka Securities Exchange, for instance) to make the Asian Inter-regional Bond (Asian Bond) Market more user-friendly.

Explanation of the Three Key Items in the Proposal for a “Road Map to an Asian Inter-Regional Bond (Asian Bond) Market”

- I Initiative to Establish the Capital Markets Association for Asia (CMAA)
- II Points for Consideration concerning Practical Legal Issues related to the Creation of an Asian Inter-Regional Bond Market
- III Framework for a “Dual Core Asian Inter-Regional CSD”

⁸ The “**Dual Core Asian Inter-Regional CSD**” approach is one in which Japanese residents use, for example, the South Korean CSD as the international central securities depository (ICSD) when they issue international bonds (Asian Inter-Regional Bonds), and residents of South Korea and other non-Japanese issuers use the Japanese CSD as the international central securities depository when they issue Asian Inter-regional Bonds. By utilising the central securities depositories in different Asian countries as “Dual Core” ICSDs, analogously to the two major central securities depositories for the Eurobond market, Euroclear and Clearstream, it will be possible to create a joint Asian Inter-Regional Bond Market enabling Asian Bonds (Asian Inter-Regional Bonds) to be issued and traded exclusively within Asia without relying on these two major central securities depositories.

⁹ EDINET (Electronic Disclosure for Investors' NETwork) is a network system for electronic disclosure of information operated and provided by the Financial Services Agency (FSA) for investors as one of its administrative services. “An electronic disclosure system for disclosure documents such as financial statements based on the Financial Instruments and Exchange Law.”

I . Initiative to Establish the Capital Markets Association for Asia (CMAA)

Given the likelihood that the Eurobond market, which has a long history as an international and offshore bond market, will increasingly become more like an onshore market following the EU directive for an integrated market, we propose the creation and development of an **Asian Inter-Regional Professional Securities Market (AIR-PSM** ; the offshore capital market as an Asian regional shared international bond market), with Asian issuers that have previously actively employed the Eurobond market and Asian underwriters as the main market participants and with support from the Asian Development Bank and U.S. and European financial institutions. Non Asian issuers and underwriters are also invited.

In terms of its relation to regulations employed in the domestic markets of the nations involved, the AIR-PSM would from the beginning be clearly defined as a common offshore inter-regional bond market, and we would seek to establish a market structure that would not impede the flow of funds between the onshore and offshore markets of the region, soliciting cooperation and coordination among the regulatory authorities of the countries concerned in order to avoid friction when domestic laws are revised.

The **AIR-PSM** would be a gateway for common international bonds denominated in Asian currencies that have not to date been accepted on the Eurobond market, and would enable these bonds to be cleared and settled within Asian time zones.

Considering the degree of maturation and market depth of Asian domestic markets as well as the level of development of domestic traders and institutional investors in Asian countries, it is desirable that major Asian issuers with considerable experience of issuing on the Eurobond market act as the main participants, with major Asian dealers and international securities companies with excellent records in cross-border transactions within the Asian region and elsewhere as advisors, in forming a Capital Markets Association for Asia (CMAA) as an entity that will promote the establishment of The **AIR-PSM** by setting rules and market practices for the primary market (issue procedures, syndication rules, and methods for information disclosure and filing and announcement of disclosure documents).

The concept of involving issuers in addition to underwriters at the initial stages of establishment of the framework emerges from the fact that the **AIR-PSM** is conceived of as a venue for procurement of long-term industrial funds, and also that, as Japan's experience of corporate bond market reform commencing with bond placement by the former Nippon Telegraph and Telephone Corporation suggests, the leadership and cooperation of issuers as users of the capital market will be necessary to ensure active trading in an Asian secondary market.

With regard to the establishment of the secondary market in particular, securities companies and investment banks that act as brokers of market transactions and intermediaries of financial transactions can do no better than avoiding the risk of holding their own positions by buying or selling against the market. Therefore, even without reference to reform of the Japanese corporate market, the firm commitment and leadership of bond issuers are obviously necessary for the establishment and development of a secondary market with limited liquidity.

The Asian Capital Markets Study Group, created in Tokyo in October 2003 at the

initiative of the National Institute for Research Advancement (NIRA) and the Japan Capital Markets Association (JCMA), were reorganised in 2007 with the participation of major Asian securities dealers and a small number of international securities companies with excellent records in cross-border transactions within and outside the Asian region to enable the creation of the CMAA.

Major private sector issuers with considerable experience in issuing on the Eurobond market will, as users of an **Asian Inter-Regional Professional Securities Market**, propose a framework of user-friendly market practices, and securities dealers participating as advisors will provide advice and guidance to help in the design of an institutional framework that is also acceptable to underwriting participants.

With respect to institutional design, the following working groups are to be established within the CMAA, and will discuss the formulation of proposals and recommendations in their respective areas. We recommend that some of these working groups present their first set of recommendations by the middle of 2008, to coincide with the Road Map.

- | |
|---|
| 1. Working Group on Market Practices, Law and Documentation (New Issue Practices, Market-making Rules, Syndication Rules, Disclosure, Governing Law and Underwriting Contracts) |
| 2. Working Group on Market Systems Infrastructure, Clearing and Settlement |

* Recommendations from the International Primary Market Association (IPMA) (now the International Capital Market Association (ICMA)) will be used as a reference when the Working Groups are engaged in consideration of details.

Role and Scope of the CMAA with the IPMA as a Reference

The CMAA will be concerned with new issuing procedures, including procedures for disclosure, in an Asian Inter-Regional Professional Securities Market, but it will be neither an exchange nor a regulator empowered by statute. The CMAA's rules will take the form of recommendations, which will be based on the general agreement of the major participants in the AIR-PSM. This agreement is to be secured on the basis of consensus among issuers and underwriters. The CMAA will have no power to sanction and members will be free to ignore any particular recommendation when launching an issue.

The CMAA will be mandated by its members to facilitate the operation of the AIR-PSM. The smooth functioning of the markets may involve legal or documentation questions, best market practice, clearing and settlement, regulation, disclosure and other factors.

In line with an increase in the number of major Asian dealers participating in the common Inter-Regional bond market and the development of the market itself, it is likely that an Asian Capital Market Dealers Association will be formed separately to help promote the market with the CMAA and an association of issuers. Until then, however, it is assumed that the CMAA will function as a self-regulatory organisation.

Practical issues

·Experience in cross-border transactions within and outside the region

→ Almost all the dealers that qualify are Japanese

- Liquidity
(Disparity in capital strength, financing capacity, trading capabilities, etc. among dealers within the region)
- Disparity in the depth of domestic financial and securities markets of countries in the region
- Differences in the securities trading environment
 - Universal banking → Countries other than Japan, South Korea = Non-OECD
 - Separation between banking and securities businesses
 - Japan and South Korea = OECD
 - Countries under Articles IV, VIII of IMF Articles of Agreement
 - Differences in regulations on foreign currency trading and foreign currency-denominated bond trading

(Hirohiko Suzuki)

II . Points for Consideration concerning Practical Legal Issues related to the Creation of an Asian Inter-Regional Bond Market

1. Starting point for foreign bonds in the Japanese market

(1) Domestic bonds

Protection of bondholders: Commissioned banks and meetings of bondholders under the jurisdiction of Japanese courts

Commissioned banks, appointed by issuing companies, are “obliged to manage corporate bonds for bondholders fairly and honestly on the basis of the duties of a good manager.”

Under the new Company Law, the duty of a commissioned bank is more clearly defined as in respect of “receipt of payments, protection of claims of corporate bonds and other matters concerning management of corporate bonds.”

Historically, this approach to the role of commissioned banks has been based on the thinking that because corporate bonds are acquired by the investing public, the principal should be guaranteed in the same way as bank deposits. Thus, the function of refinancing loans provided by the main banks was the historical starting point of corporate bonds.

(2) Foreign bonds

With respect to foreign bonds, by contrast, the international approach to the protection of bondholders of the place of issuance (the US or Europe) apply, based on the principle of bondholders’ own risk, and Japan follows this thinking.

2. 1993 Revision of the Commercial Code

In exchange for the abolition of issue limits on corporate bonds, the appointment of commissioned banks became mandatory. As a result, all foreign bonds of Japanese issuers have been issued using foreign laws as governing law.

Because fees associated with the heavy responsibility of commissioned banks were too high, trustees (despite the name, having rights but no duties) and paying agents or fiscal agents (mere paying agents for issuers) charging relatively low fees as per US or European market practice, or the method of no direct relationship between issuers and bondholders as per Swiss market practice, was used.

3. The Company Law which came into effect in May 2006

(1) Position of the Justice Ministry

The Company Law which came into effect from May 2006 provides a definition of corporate bonds (Article 2, No.23). As defined by this clause, only bonds that are allocated and redeemed according to the stipulations of the Company Law are regarded as corporate bonds.

Theoretically, therefore, it should be possible to issue bonds with Japanese law as the governing law that do not conform to this definition, and which would therefore be regarded as non-corporate bonds. Given this, it was at first hoped that Japanese issuers of foreign bonds would be able to issue foreign bonds as non-corporate bonds, with

Japanese law as the governing law. However, it was later indicated that foreign bonds issued by Japanese companies would be regarded as corporate bonds if issued with the Japanese Company Law as the governing law, since otherwise many amendments are needed in other laws as to the definition of “bonds”.

This means that Japanese corporate issuers cannot issue foreign bonds with the Japanese Company Law as the governing law for all practical purposes.

(2) Practical responses

For an issuing company, a bond is simply a vehicle for borrowing a large amount of money from a large number of investors.

On the other hand, if issuers choose not to appoint commissioned banks in placing foreign bonds to avoid the high fees involved, those foreign bonds, with a few exceptions, will fall outside the definition of corporate bonds under the Company Law and as such will not be regarded as corporate bonds under the Company Law.

Thus, foreign bonds are likely to be issued as “foreign non-corporate bonds that rank *pari passu* with corporate bonds.”

If they are not defined as corporate bonds, issuance of foreign bonds will not require a resolution by a board of directors. However, this was the interpretation of the Justice Ministry and did not represent a judicial decision.

For the sake of legal safety, therefore, issuing companies are in practice opt for the authorisation of issuance of foreign bonds based on a resolution of the board of directors as in the case of domestic bonds (no harm would be done in implementing a procedure that is not required as a precautionary measure, and there should be no practical problem in doing so because the system enabling lump-sum authorisation by representative directors already exists).

Because the bonds need to be subject to the negative pledge clause and the “*pari passu*” clause of existing foreign bonds, and because international consistency will be necessary, they may probably still be termed foreign corporate bonds outside Japan.

(3) Necessity of clarification of the rules for exemption from the requirement for the assignment of commissioned banks for corporate bonds under the Company Law

The new concept of “non-corporate bonds” was not popular among Japanese market practitioners. Under current market practice, Japanese issuer’s foreign bonds are governed by British Law, and issuers avoid the requirement of assigning a commissioned bank.

But this practice has been criticized, and it has been suggested that even in the case of foreign corporate bonds based on British Law, allocation and redemption of the bonds will be considered to be subject to the stipulations of the Company Law.

To avoid confusion and uncertainty in the market, the CMAA is proposing the revision of the Company Law Enforcement Regulations to the effect that in the specific case of foreign bonds, regardless of the governing laws, the requirement for the assignment of a commissioned bank could be waived if offerings are made exclusively to professional investors in and outside Japan.

CMAA Proposal

The requirement for the assignment of commissioned banks for corporate bonds under the Company Law should not represent a constraint in the development of “**Made in Japan**” **Asian Inter-Regional Bonds** (foreign bonds), because the requirement can be waived and a fiscal agent (FA) appointed

1) in the event that the value of each bond is one hundred million yen or higher (based on a conditional clause of Article 702 of the existing Company Law), and

2) in the case that a figure of less than 50 is obtained when the total value of the bond issue is divided by the lowest value of the individual bonds (Article 169 of the Company Law Enforcement Regulations). **In addition,**

3) in the specific case of foreign bonds, the requirement for the assignment of a commissioned bank could be waived if offerings are made exclusively to professional investors, which are not bound by the securities and foreign exchange regulations of their home countries. (i.e., the Company Law Enforcement Regulations should be revised)

4. Withholding tax

Nonresident holders of foreign bonds issued by Japanese private-sector issuers are exempt from the 20% withholding income tax. The special taxation measures law that stipulates this exemption provides for “exemption of the withholding tax for private foreign bonds issued on and before March 31, 2008.” The National Tax Agency confirms that foreign bonds as described in 3. (2) above issued by private-sector foreign issuers include not only corporate bonds but also non-corporate bonds.

5. Asian international bonds issued by Japanese issuers under the Company Law

Asian international bonds to be issued by Japanese issuers are expected to include straight bonds and bonds with share subscription rights.

Straight bonds are likely to be issued as foreign bonds using fiscal agents or under the exemption from the mandatory appointment of commissioned banks for corporate bonds with denominations of ¥100 million or more (Article 702 of the Company Law).

In the case of bonds with share subscription rights, as denominations of ¥100 million or more are not practicable, these bonds are likely to be placed as foreign bonds with the same seniority as corporate bonds. Then CMAA proposes the alteration of the Company Law Enforcement Regulations as above 3.-(3).

With regard to governing law, given the interpretation of the Justice Ministry that bonds issued without commissioned banks may not be regarded as corporate bonds regardless of whether they are domestic bonds or foreign bonds, Asian international bonds to be issued by Japanese issuers are likely to be governed by Japanese law to save costs.

(Keiji Matsumoto)

III. Framework for a “Dual Core Asian Inter-Regional CSD” <To Be Model> and <Can Be Model>

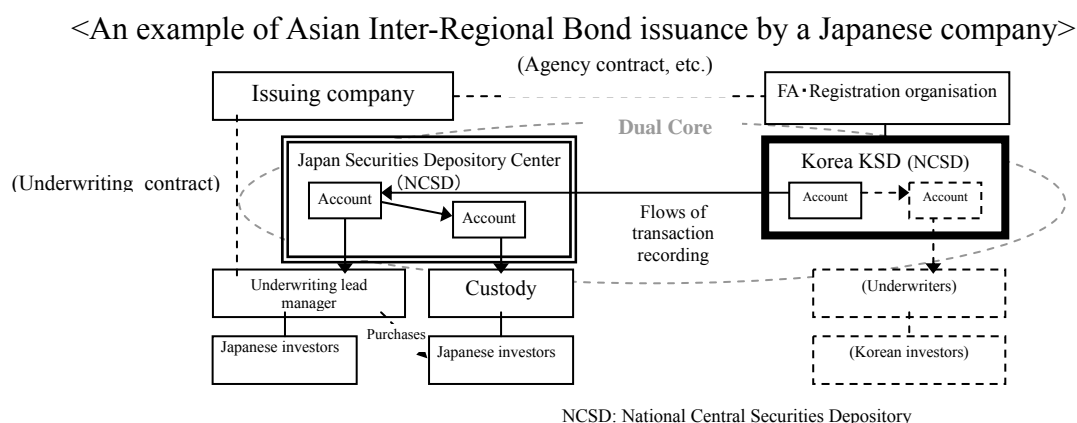
1. Concept

Japan and South Korea mutually cooperate in building a highly feasible framework of central securities depositories by maximizing the use of existing functions. The framework will provide safe, efficient and cost-competitive clearing and settlement services to the Asian Inter-Regional Bond (Primary) Market.

2. Basic scheme

<To Be Model: “Dual Core Asian Inter-Regional CSD”>

(1) Both Japan and South Korea improve their own issuance and settlement systems and also mutually cooperate in building the central securities depository framework, aiming to make this common Asian Inter-Regional Bond Market infrastructure available at an early date.



- i. An issuer conducts issuing procedures in the country in which the bonds will be issued using laws of the issuer’s home country as governing law.
- ii. An issuer uses the national central securities depository (NCSN) of the country in which the bonds are issued as the local securities depository.
 - ✓ A Japanese issuer issues an Asian Inter-Regional Bond using the Korea Securities Settlement Corporation (KSD) as the local securities depository.
- iii. A mechanism is established by means of linkage of the NCSN of the country in which the bonds are issued and the NCSN of the issuer’s home country enabling investors in the issuer’s home country to settle the Asian Inter-Regional Bonds at the same low cost as domestic bonds.
 - ✓ Investors in the issuer’s home country acquire the Asian Inter-Regional Bonds through the NCSN of the home country
 - In Japan, it can be assumed that the Japan Securities Depository Center (the home-country NCSN) links directly with overseas securities depositories (NCSNs, etc.) as in the foreign stock transfer system.
 - ✓ Investors in the country in which the bonds are issued can purchase the Asian

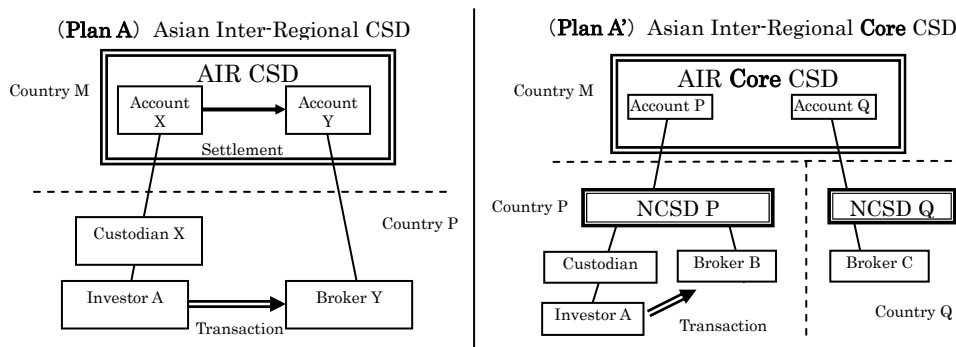
- ✓ Bonds through that country's NCSD.
- ✓ The NCSDs of both countries serve as the "Dual Core" to form a "Virtual Asian Inter-Regional CSD."
- ✓ Japan and South Korea, given the comparative depth of both their issuing companies and investors and their superior clearing and settlement infrastructures, mutually cooperate as a "Dual Core" in providing the concrete clearing and settlement infrastructure for the Asian Inter-Regional Bond Market.
 - It is a precondition that the infrastructure will be open to issuers from Asian countries other than Japan and South Korea. (However, most investors will probably be Japanese or South Korean due to the linkage between depository organisations.)
 - The NCSDs of Japan and South Korea will be required to further strengthen their cooperation in the areas of information technology (IT), institutional arrangements, business services, etc. and enhance the level of their services through institutional and system reforms in order to become internationally viable NCSDs (policy measures will be required).
- ✓ The feasibility of the following points should be verified:
 - Is this approach advantageous from the medium-term perspective compared to the alternative approaches to be discussed below? Is advance investment in NCSDs feasible?
 - Do the NCSDs of Japan and South Korea have sufficient human resources for planning and system development? (In particular, can the Japan Securities Depository Center play an international role at present?)

<Can Be Model> (The implementation of Plan A (A') and Plan C is deemed realistic and desirable)

(2) If the approach described above is judged as difficult to realise in an appropriate time frame, it may be possible to gradually develop the clearing and settlement infrastructure for the Asian Inter-Regional Bond market using the alternative approaches below ("**Can Be Model**") in order to eventually realise the "**To Be Model**" (such as the approach described above and "Asia Settle," etc.).

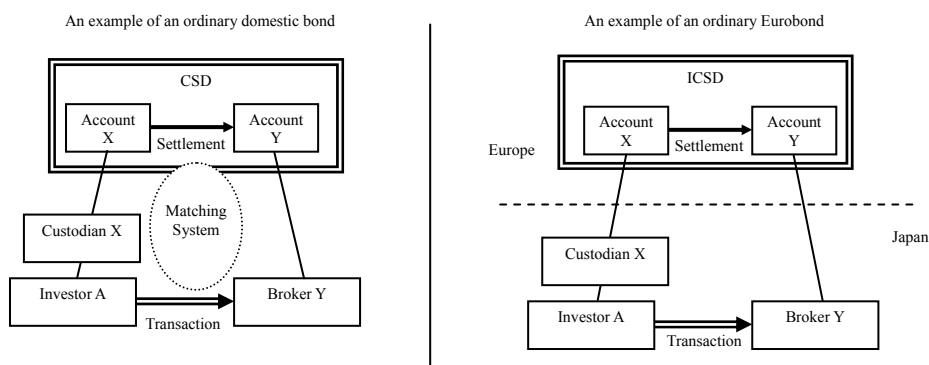
- i. **Plan A:** Market participants (including issuing companies) contribute capital to set up a new "**Asian Inter-Regional CSD**" in order to establish the cross-border clearing and settlement system.
 - ✓ Are there prospects for active transactions that can justify costs? It seems that it would be difficult to get the new CSD off the ground. What are the chances of its success? -- If we are able to simplify the functions and systems of the new CSD and thus minimize the initial investment and the running costs, this management model appears to be feasible.
 - ✓ Market participants may find the new CSD impractical and costly if there is no standard interface for different financial products (matching and settlement systems, etc.); a practical and reasonable standard interface (e.g., S.W.I.F.T.) would definitely be necessary for all market participants who would use the new CSD. In order to establish inter-operability it would also be necessary for the new CSD and related NCSDs to standardize the clearing and settlement system in the case of **Plan A'**, discussed below.

- ✓ **Plan A'**: The “Asian Inter-Regional CSD” could be positioned as an “Asian Inter-Regional **Core** CSD.” An “Asian Inter-Regional **Core** CSD” would have linkages with Asian NCSDs and custodians, providing a convenient system for users.



ii. **Plan B:** Asian Bonds are cleared and settled like Eurobonds (Existing international CSDs are used)

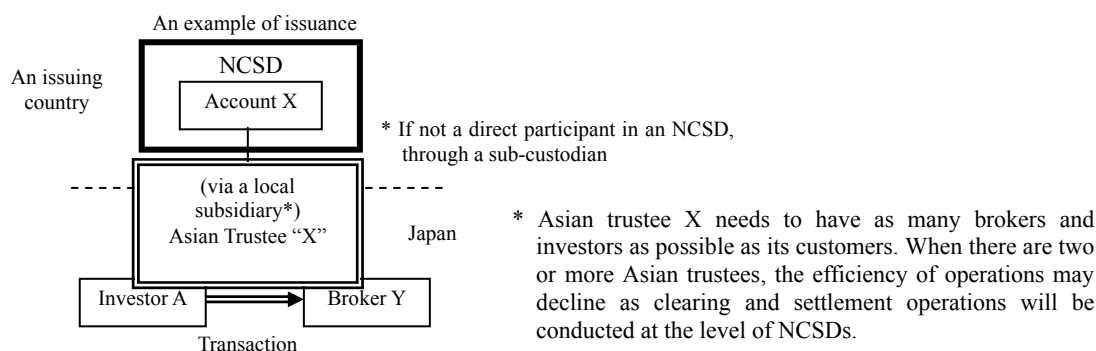
- ✓ Current ICSDs (such as Euroclear) for Eurobonds would also be used for Asian Bonds. Because they would be treated as ordinary Eurobonds, the approach would not require separate initial costs.
- ✓ This would enable the same level of usability for Asian Bonds as for Eurobonds. However, if we assume Asian Inter-Regional primary and secondary markets, this approach would not be efficient because the clearing and settlement infrastructure is not located in the Asian region. In addition, it is not compatible with the concept of the establishment of a self-contained, highly cost-effective Asian Inter-Regional Professional Securities (bond) Market.
- ✓ This approach is likely to present problems concerning a time lag in fund settlements and the limited current acceptance by ICSDs of Asian currency-denominated bonds.



iii. **Plan C:** A major Asian custodian bank (an Asian trustee) provides clearing and settlement services by linking up with a local securities depository (a local NCSD, etc.) (with the expectation that centralised depository services will be realised through competition in the region).

- ✓ Is it likely that a custodian service provider will emerge to undertake the above-described services in the Asian region? It will probably depend on potential custodian banks' business strategies and the fees they can hope to earn from

- providing such services.
- ✓ If mutual efforts of NCSDs in the region make the “Dual Core Asian Inter-Regional CSD” approach a reality, they can play the role of a major custodian service provider as they are.
- ✓ Further, it is also possible that an NCSD acts as an Asian trustee and establishes direct links with local securities depositories. If this scenario was applied to Japan and South Korea, it would equal the “To Be Model” described above.



3. Other issues

(1) Legal problems involved in securities settlements

i. With respect to governing law for securities clearance and settlements, in Japan, under Article 13 of the Rules Concerning the Application of Laws, the applicable law is the governing law of the country in which the objects are located.

After the ratification of the Hague Convention, it becomes possible to apply the governing law of the country of the account management organisation an investor uses, in line with an account contract (application of the current legal doctrine concerning the depositing of securities by two or more depositors) .

- ✓ Legal frameworks for the clearing and settlement of foreign securities in South Korea and other countries need to be clarified.

ii. The harmonisation of laws concerning securities clearance and settlements in Asian countries is desirable (trends at the International Institute for the Unification of Private Law (UNIDORIT) should be followed).

(2) Other points to be considered

i. If it is possible for Asian Inter-Regional Bonds to use a domestic NCSD through the “Dual Core” approach or other methods, it is hoped that these bonds, like domestic bonds, will be recognised by the Bank of Japan as eligible to function as collateral bonds and that it will be possible to use the collateral loan system.

ii. High-liquidity issues may be considered for handling by central counterparty (CCP) clearing corporations in each country.

- ✓ Debt assumption and netting by CCP can be expected to reduce counterparty risks

and enable economizing on liquidity.

- ✓ In Japan, the scope of bonds to be handled by the Japan Government Bond Clearing Corporation (JGBCC), the independent CCP, may be expanded to include Asian Inter-Regional Bonds. However, this would require that the Asian Inter-Regional Bonds are eligible for handling by the Japan Securities Depository Center.

iii. Whichever approach is used, it will be desirable to help develop custodians (“Asian trustees”) to expand and integrate depository services for domestic and foreign securities.

- ✓ In Japan, the use of custodian services is expanding as a result of the implementation of the central depository system for non-government bonds.
- ✓ Custodian banks should consider a framework that makes it easier to raise settlement funds (such as a scheme to enable securities to be cleared enabling them to be easily used as collateral and a scheme to economise on liquidity by offsetting).
- ✓ The market will gain considerable depth if rating services and tripartite repurchase agreements involving deposited securities are expanded.

(Satoshi Yoshida)

5 . Some Supplementary Remarks on a Common Currency Unit

With regard to the establishment of the Asian Inter-Regional Professional Securities Market (Asian Bond market) we have proposed, we believe that every possible effort should be made to avoid domestic law-based responses to the issues involved (options will be limited if the traditional method of country-by-country response is adopted).

Envisioning the Asian Inter-Regional Professional Securities Market (Asian Bond market) as an offshore market independent of any of the countries involved, an effort to seek the cooperation of the public sectors of East Asian countries, as was done in the case of the EU regulations, is worth considering.

In this case, when the exchange rates of East Asian currencies become stable, the development of a supranational offshore market for AIR-PSM (international bonds), dominated by the East Asia Currency Unit (EACU¹⁰), which was proposed by NIRA in 2005 and which the private sectors of East Asian countries will likely come to consider making use of in the future, should come within sight (recall that interbank settlements of eurocheques, proposed by European banks in the early 1980s, later came to be made in the European Currency Unit (ECU), supported by exchange rate stability under the European Monetary System).

In any event, the emergence in the near future of a situation in which the use of a common currency unit is dominant in the private sector should provide important support for the development of a supranational AIR-PSM (Asian Bond market).

(Kazuaki Sono, Shigehito Inukai)

¹⁰ NIRA Market Governance Report 2005, Grand Design for Comprehensive and Cross-sectoral Market Legal Framework Part II Supplementary Chapter 2.4 Proposal on the Initiative to Establish an “East Asian Free Securities (Bond) Market” (i.e., “the Asian Inter-Regional Professional Securities Market (Asian Bond market)”).

1. The development of a regional financial and capital market is indispensable for the development of an East Asian economic community. To achieve this, it will be essential to upgrade the capacity of regional market participants.

2. In the world of financial institutions and institutional investors, the inexperience of buy-side participants and the obsolete patterns of sell-side participants have stymied reforms of Japan’s financial and capital markets. The situation should be corrected by fostering more financial professionals who can take an active part in the international arena.

3. In East Asia, centering on Japan, the situation is becoming ripe for proactive efforts to establish a Eurobond market-type free market to ensure the competitiveness and further development of the region. A free securities market would also enable professionals to be nurtured and trained. We therefore propose the creation of an East Asian free securities (bond) market.

4. The obstacles to the creation of a free securities (bond) market as an offshore market that effectively integrates both onshore and offshore markets are no longer insurmountably high. However, nobody seems to be taking action to remove the remaining obstacles. If nothing is done, there are genuine concerns that the Japanese financial and capital markets and the Tokyo international financial market might remain merely enormous local markets.

5. It is possible to assume that the main participants among both issuers and investors in a free securities (bond) market in East Asia, which is beginning to display signs of the possibility of becoming an economic community, will be from East Asian countries. Thus, it is highly desirable that financial instruments should be developed to cater to their needs and convenience.

6. Seeking to mitigate the risk of unexpected fluctuations in exchange rates and pursuing the achievement of exchange rate stability among Asian currencies, we propose the creation of a basket of major East Asian currencies, including the Japanese yen, the Chinese yuan and the Korean won, with the timing of appropriate adjustments of the Chinese yuan’s exchange rate as the trigger for implementation, and also propose the commencement of discussions to pave the way for the issuance and trading of Asian Bonds using the basket of East Asian currencies as the common unit of account. We tentatively call this the East Asia Currency Unit (EACU) as the unit of account for bonds. In the present world of unregulated foreign exchange trading, the creation of a common unit of account is deemed possible even as a private agreement regarding foreign exchange transactions, based on consensus among market participants.

7. Active discussion of the problems to be overcome should be launched with a vision of the creation of an East Asian free securities (bond) market as the target to be achieved.

**6 . NIRA-ADB Joint Forum:
“The Prospects for an Asian Bond Market”
(March 27, 2006)**

Questionnaire Results

Following the conclusion of the Forum, in which approximately 90 people participated, a questionnaire was distributed. It is noteworthy that approximately three-quarters of respondents to the questionnaire expressed favorable opinions with regard to the tentative proposals that were presented.

Strongly agree	Agree to some extent	Do not agree	Regarding the establishment of a Eurobond market-type Asian Bond market	Number of respondents	%	Percentage of positive opinions
12	1	0	Must be established	13	25.5%	78.5%
14	13	0	Should be established	27	53.0%	
4	4	0	The domestic capital market and Eurobond Market are sufficient	8	15.7%	
0	0	1	Is unnecessary	1	1.9%	
1	1	0	No opinion	2	3.9%	
31	19	1	Total	51	100.0%	
60.8%	37.3%	1.9%				

Strongly agree	Agree to some extent	Do not agree	Regarding the establishment of AIPMA(Asian International Primary Market Association) (Name of organisation later changed to CMAA)	Number of respondents	%	Percentage of positive opinions
8	2	0	Must be established	10	19.6%	74.5%
12	16	0	Should be established	28	54.9%	
2	11	0	No opinion	13	25.5%	
22	29	0	Total	51	100.0%	
43.1%	56.9%	0.0%				

Strongly agree	Agree to some extent	Do not agree	Regarding the establishment of a dual core settlement system	Number of respondents	%	Percentage of positive opinions
5	1	0	Must be established	6	11.8%	66.7%
7	5	0	Alternative proposals should be implemented first	12	23.5%	
7	9	1	Should be established	16	31.4%	
7	9	0	No opinion	17	33.3%	
26	24	1	Total	51	100.0%	
51.0%	47.0%	2.0%				

Very clear	Clear to some extent	Not clear	Points to be aware of in terms of practical legal issues	Number of respondents	%
17	31	3	Total	51	100.0%
33.3%	60.8%	5.9%			

7. Asian Bond Markets and Cross-Border Securities Settlement - Toward Cooperation between Japan and Korea -

1. Introduction

The 1997 financial crisis in Asia convinced Asian countries of the need for regional financial and monetary cooperation in addition to cooperation in the trade of goods. Since the crisis, there have been numerous initiatives to promote economic cooperation in the region; for example, free trade agreements (FTA) and economic partnership agreements (EPA) have facilitated trade in goods and services and investment. The Chiang Mai Initiative (CMI) attempts to prevent the recurrence of a currency crisis by ensuring liquidity through bilateral swap agreements (BSA). From the supply side, the Asian Bond Market Initiative (ABMI) promotes regional bond markets in order to channel the enormous amount of accumulated savings in Asia into regional investment opportunities and to enhance the market infrastructure for the issuance and trading of bonds. From the demand side, the Executives' Meeting of East Asia Pacific Central Banks (EMEAP), a forum of central banks and monetary authorities in the East Asia and Pacific region formed to strengthen financial cooperation among its members, has launched the Asian Bond Fund (ABF1, ABF2) to purchase bonds issued in the region, in order to promote the development of regional bond markets and to circulate accumulated funds. However, Kawai (2007) points out that the Asian region displays less activity in terms of capital transactions than the US and the EU, despite the scale of its trade in goods and its high level of GDP growth (see Figure 1).

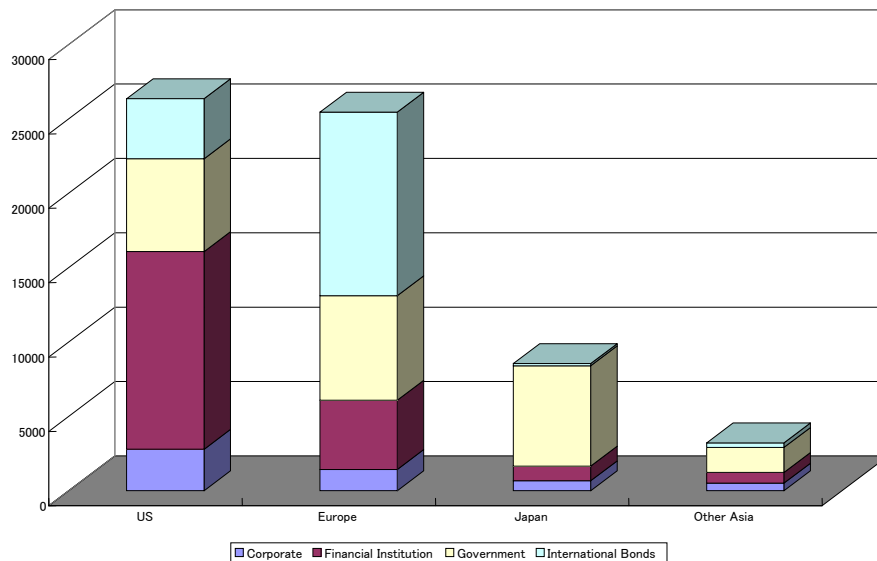
ASEAN+3 countries are currently endeavoring to develop and foster Asian Bond markets which can facilitate greater access to long-term local currency financing. Nevertheless, Asian regional bond markets are still fragmented and illiquid because of a lack of mutual recognition and involvement of the private sector and the absence of a regional base of investors and dealers. Asian countries also face other problems: Financial markets in the region are at different stages of development, and there is considerable heterogeneity in terms of legal and institutional systems¹¹. Harmonising different rules and regulations and building market infrastructure will therefore be an extremely important aspect of the process of developing and fostering an Asian Bond market because it will promote cooperation between regional financial markets and develop linkages between them. This study focuses in particular on cross-border securities settlement in the region because it will be impossible to obtain trust from international investors and develop Asian Bond markets without a safe and efficient settlement system in the region¹².

The purpose of this paper is to briefly outline the necessity for Asian Bond markets and then to comparatively identify some regulatory impediments to fostering the market in the legal and regulatory frameworks of Japan and Korea. Lastly, the feasibility of a “Dual Core Approach” and an alternative method of cross-border securities settlement using existing systems will be reviewed.

¹¹ METI's report of Asia PPP study points out that the direct financing markets in Asia still have not been developed enough to solve the double mismatch problem and foreign corporations still feel that it is difficult to issue corporate bonds in the local market.

¹² Oh(2004) and Huh (2005) point out the major reasons for establishing a new ICSD in the region as 1)low coverage of Asia by the existing ICSD and 2) “the third time zone problem”, the fact that business is conducted in Asia outside the business hours of the Europe and the U.S.

Figure 1) Comparison of Size and Composition of Global Bond Markets



Source) BIS (December 2006, US billion dollar)

2. Rationales for the Development of a Well-functioning Asian Bond Market

Economies which are highly dependent on bank financing bear heavy economic burdens in an economic or financial crisis owing to the absence or under-development of bond markets. As demonstrated by the Asian financial crisis in 1997-98, bank-dependent economies suffer from a so-called “double mismatch” in currency and maturity, i.e. they borrow short-term money in foreign currencies and invest funds domestically for the long-term. Out of the absence of bond markets, there is also a lack of information regarding the interest rates determined in the bond markets, which consequently impedes the development of derivative products such as interest rate swaps and bond derivative transaction (bond forward and options).

The diversification of the financial market through the development of regional bond markets would make both savers and firms better off. For example, savers would have more portfolio options for investment in bond markets. As a result, more savings would be mobilised in the medium- and long-term to fund the investments, and small and medium-sized enterprises (SMEs) that rely on only bank loans would be able to easily access to regional bond markets by issuing Asian Bonds in the region using the vehicle of securitization¹³. In addition developing Asian regional bond markets would provide more business opportunities to Asian financial intermediaries in the regional financial markets.

Excessive dependence on the US dollar can cause exposure to sudden reversal of foreign capital flows and the risk of currency crisis. It also generates the possibility of substantial loss from the weakening of the dollar because most Asian countries hold their foreign exchange reserves in the form of US dollars.

We therefore need to develop Asian local currency bond markets and regional market infrastructures to enable circulation of the funds accumulated in Asia in order to provide

¹³ Please refer to Korean SMEs’ CBO issuance in 2004 (Page 66).

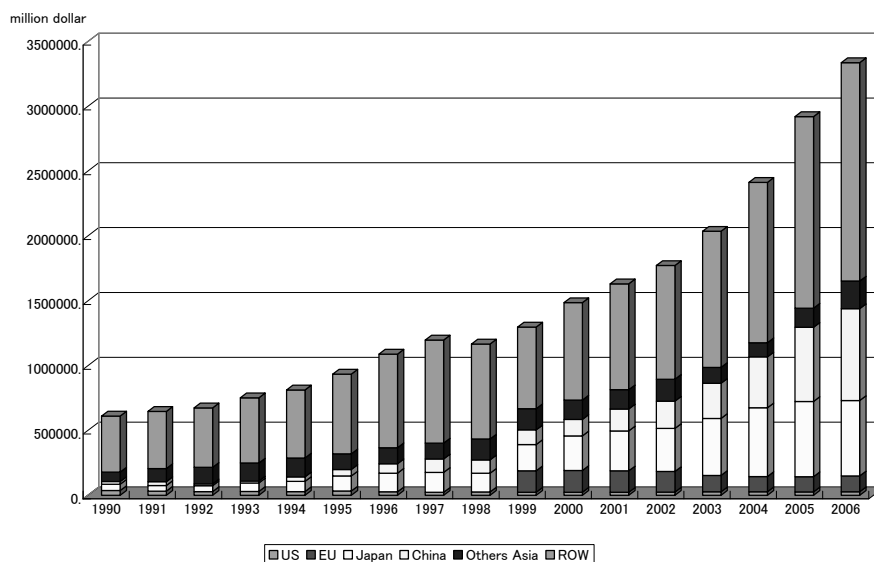
more opportunities to earn higher returns on the rapid economic growth in the region. Given the above, there are sufficient needs to develop well-functioning regional bond markets that are complementary to bank-centered markets to utilise effectively the accumulated funds in the region and to enhance the necessary infrastructures to minimize market risk.

2.1 Foreign Exchange Holdings in Asia after the Financial Crisis

As of 2006, Japan held 581.5 billion US dollars in foreign exchange reserves, the US held 272.1 billion dollars, the Euro Area (including the European Central Bank) held 122.3 billion dollars and other Asian countries held 1.5 trillion dollars. The share of foreign exchange holdings by Asian countries has been increasing since the crisis in 1997 and reached a level of approximately 45% of the world's total foreign exchange reserves in 2006.

These rapidly accumulated foreign exchange holdings are utilised in part for bilateral swap agreements between Asian countries under the CMI and the purchase of Asian bonds under the ABF 1 and ABF2. However, the current situation is that the US current account deficit is being supplemented by Asia's portfolio investments in US government bonds and by the foreign exchange holdings of Asian countries. As of October 2006, major Asian countries held 56.7% of total US treasury securities holdings. The funds accumulated in Asia flow into the US and European countries and a large proportion of these funds return to Asia in the form of portfolio investments or hedge funds. Additionally, these funds are largely intermediated and settled by financial institutions and settlement systems outside Asia.

Figure 2) Foreign Exchange Reserve Holdings



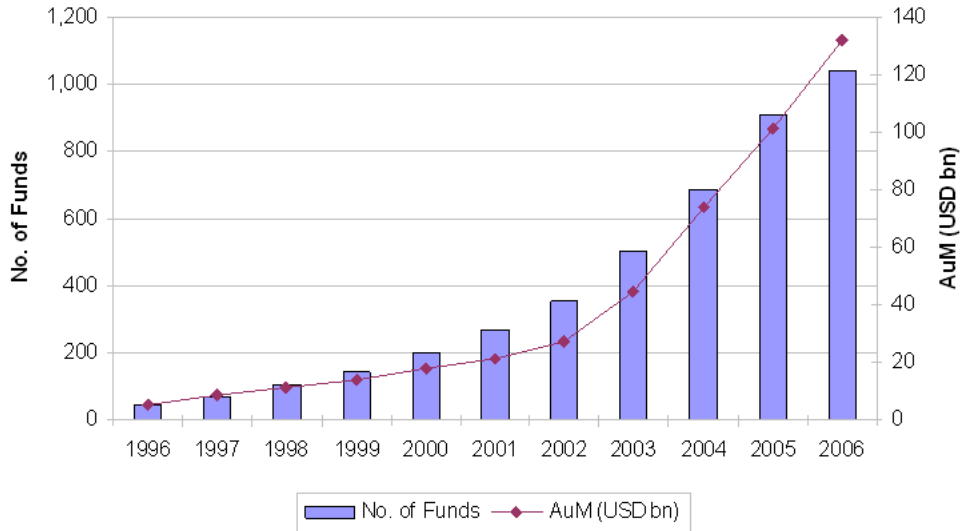
Source) IMF, International Financial Statistics (IFS) Online

2.2 Hedge Funds in Asia

Based on EurekaHedge Asia and Japan Hedge Fund Directory (2007), the total size of the Asian hedge fund is estimated at U.S. \$ 132 billion as of end-2006, up 30% from our end-2005 estimate of U.S. \$ 101 billion. The number of funds managed in Asia has also

increased to over 1000 as of end-2006. And the Asian hedge fund is expected to continue to be on an exponential growth curve on both the number of funds and the size of assets.

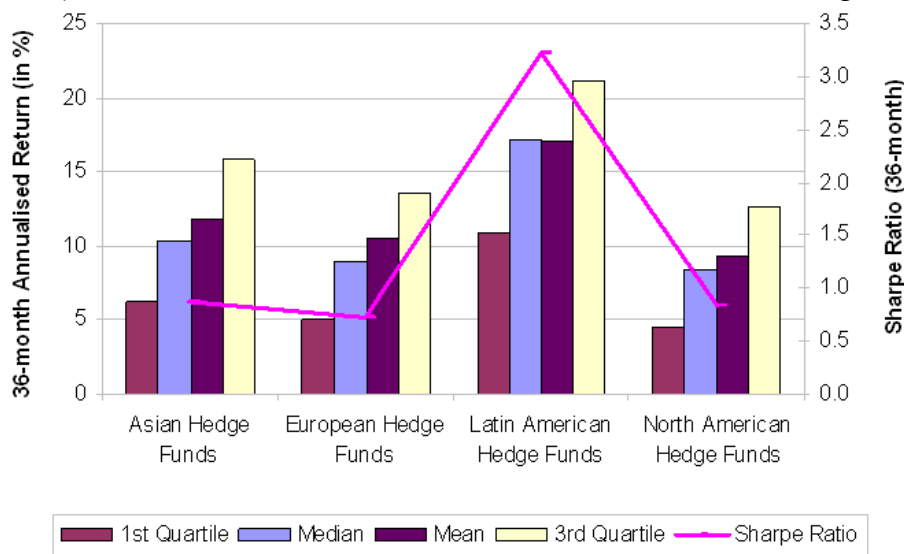
Figure 3) Growth in Single Manager Asian Strategy Hedge Funds



Source) Key Trends in Asian Hedge Funds, EurekaHedge (2007)

One of the factors behind this growth is the fact that hedge funds are seeking high returns based on the high economic growth in India, China. Figure 4 shows that return on hedge fund investments in Asia is better than those in North America and Europe¹⁴. As end of 2006, Asian countries held approximately 45% of the world total foreign currency reserves and Asian funds are used to purchase US treasury bills and then some of those funds return to Asia in the form of hedge funds.

Figure 4) Returns of Asia/Euro/Latin American/North American Hedge Funds



Source) AsiaHedge, HedgeFund Intelligence

¹⁴ The return on Latin American Hedge Funds is the highest but because of unstable political and economic conditions; Asia Hedge Funds are expected to grow stably at the current pace.

2.3 Portfolio Investment Flows in Korea and Japan

It is very important to understand the inter-country mechanism of portfolio investment flows in Asia. Korea and Japan, which represent a large share of the financial market in the region, invest in bonds issued mainly in the UK and the US (JPN: 36.1%, KOR: 59.9%) and Asia itself in a small portion (JPN:0.7%, KOR:8.9%). In the case of equity, Korea invests 22.8% in Asian stocks and 17.7% in US/UK stocks while Japan invests 6.4% in Asian stocks and 54.1% in US/UK stocks. The interesting point is that the UK and the US prefer Asian equity to debt securities and they mainly invest in Asian stocks (UK: 21.6%, US: 22.5%) while Asian countries prefer UK/US bonds to equity. These CPIS statistics show that Asian capital is re-directed into Asia by US and European countries and these portfolio investments are intermediated by financial institutions outside the region.

Table 1) Portfolio Investment Flows: Long-Term Debt Securities (million US dollar, 2006)

from into	HK	IND	JPN	KOR	MAL	PH	SG	TH	UK	US	Asia (%)	US/UK (%)	Global Total
China	2,484	3	414	152			731		1,052	1,305	33.4	20.8	11,325
Hong Kong		26	701	2,444	29	198	2,653		6,022	1,660	33.7	42.8	17,966
Indonesia	171		435	77	108		2,341		1,243	2,582	29.3	35.8	10,698
Japan	2,247		....	793	37	8	1,658	3	54,978	35,499	2.1	40.5	223,253
Korea	8,864	8	5,752	--	132		5,611	127	6,776	9,507	39.6	31.5	51,705
Malaysia	3,621	7	1,038	204			2,790	59	4,876	4,605	35.6	43.7	21,694
Philippines	720		1,493	21	14		516		2,978	4,939	14.6	41.8	18,922
Singapore	3,692	89	3,136	300	29	502		449	4,052	8,518	28.3	43.4	28,954
Taiwan	742		10	33			363		3,194	220	19.1	56.8	6,007
Thailand	475		111	94		25	933		807	1,702	31.9	48.9	5,130
Vietnam	226		37	5			66		202	238	27.6	36.3	1,212
UK	19,414	30	90,660	2,759	833	489	5,071	322		245,365	10.0		1,201,395
US	45,849	91	563,401	25,075	579	1,535	19,951	168	458,441		18.1		3,625,226
Asia (%)	12.3	14.6	0.7	8.9	10.4	15.7	21.5	20.8	5.5	5.5			
US/UK (%)	34.5	13.3	36.1	59.9	42.2	43.3	30.5	15.9					
Global Total	189,303	909	1,811,986	46,491	3,346	4,670	82,159	3,073	1,559,315	1,275,516			16,295,314

Source) Author's Calculation from Coordinated Portfolio Investment Survey (CPIS) Data, IMF

Table 2) Portfolio Investment Flows: Equity Securities (million US dollar, 2006)

from into	HK	IND	JPN	KOR	MAL	PH	SG	TH	UK	US	Asia (%)	US/UK (%)	Global Total
China	100,009	--	9,853	1,681	13	(c)	6,913	10	14,976	73,912	44.5	33.4	266,123
Hong Kong	....	....	11,014	4,156	441	--	18,719	7	29,315	85,833	16.0	53.7	214,490
Indonesia	(c)	....	456	3	39	(c)	1,336	1	3,184	11,490	7.0	55.9	26,237
Japan	6,918	....	....	1,809	217	....	4,534	7	173,596	543,506	1.2	65.7	1,091,617
Korea	2,254	....	3,358	--	113	(c)	4,530	--	28,197	114,155	4.8	67.0	212,337
Malaysia	751	1	493	48	....	(c)	7,771	111	4,201	10,781	27.5	44.9	33,383
Philippines	192	....	109	1	12	....	423	1	976	6,050	6.7	63.8	11,014
Singapore	2,858	7	3,772	490	1,558	2	....	80	12,277	43,911	9.4	60.3	93,207
Taiwan	3,414	....	2,646	61	89	....	2,337	3	21,232	74,228	6.2	68.9	138,499
Thailand	872	12	1,049	9	53	1	3,248	--	5,455	11,054	16.3	51.3	32,203
Vietnam	(c)	....	--	120	....	....	109	14	238	....	42.6	41.8	570
UK	48,147	--	52,107	1,354	190	....	3,851	90	--	673,978	7.0		1,516,407

US	15,537	3	224,136	5,180	236	95	15,801	113	340,777	....	12.5		2,096,152
Asia (%)	33.4	5.6	6.4	22.8	67.5	2.6	53.1	13.8	21.6	22.5			
US/UK (%)	18.2	0.8	54.1	17.7	11.4	81.2	20.9	12.0					
Global Total	350,846	359	510,418	36,819	3,753	117	93,973	1,694	1,362,010	4,328,962			13,779,537

Source) Author's Calculation from Coordinated Portfolio Investment Survey (CPIS) Data, IMF

Table 3) Savings utilization in the region

	Foreign Reserve (Dec 2006)	CMI (May 2006)	ABF1 (Jun 2003)	ABF2 (Dec 2004)	US Treasury Securities* (Oct 2006)
Amount (U.S. \$)	1.52 trillion	75 billion	1 billion	2 billion	1.22 trillion

* It includes Japan, China, Korea, Taiwan, Hong Kong, Singapore, Thailand, and India.

2.4 Hollowing-out of Financial Intermediation Functions in Asia

Issuance of international bonds by Asian companies in Euro bond markets is generally handled by foreign financial institutions and settlement systems outside the region. American and European investment banks have a monopolistic position in international bond markets. (Table 4) Few Asian companies and Japanese financial institutions deal with Samurai bonds in the international bond market. This situation could lead to hollowing-out of financial intermediation functions in Asia.

Table 4) Performance of Lead Managers in International Bond Markets
(As of Aug 2005)

Company	Rank	Share (%)	Amount (million \$)	Fee (%)	Issue Number
Deutsche Bank AG	1	7.50	131,937	0.29	622
Citigroup	2	7.00	123,301	0.26	495
Barclays Capital	3	5.60	97,407	0.24	426
JP Morgan	4	5.60	97,366	0.33	435
HSBC	5	5.20	91,102	0.24	463
UBS	6	4.60	80,237	0.47	400
Morgan Stanley	7	4.20	73,159	0.30	233
BNP Paribas Group	8	4.10	71,995	0.23	303
Goldman Sachs & Co	9	4.00	69,891	0.21	174
Lehman Brothers	10	4.00	69,719	0.22	237
Credit Suisse First Boston	11	3.90	68,499	0.49	276
ABN AMRO Bank NV	12	3.40	59,421	0.29	289
Dresdner Kleinwort Wasserstein	13	3.30	57,055	0.23	316
Merrill Lynch & Co	14	3.20	55,339	0.24	243
Royal Bank of Scotland	15	2.60	45,288	0.39	224
Societe Generale	16	2.60	45,135	0.17	139
Hypovereinsbank	17	1.90	33,789	0.28	233
Nomura Holdings Inc	18	1.80	30,747	0.22	146
Bank of America	19	1.70	30,035	0.37	205
Landesbank Barden-Wuerttemberg	20	1.60	27,295	0.27	240

Source) Bloomberg, Jeon YongSuk (2005)

Even in Korea-related international bond business, only three Korean companies appear among the top 20 companies: the Korea Development Bank, Daewoo Securities,

and Woori Securities & Investment. The top five European and American companies hold more than 50% of the market share. This low market share of Korean financial institutions is due to the lower level of development of domestic financial markets, the low credibility of domestic securities companies, and their lack of risk management ability and networks overseas.

Since the Asian financial crisis, Asian countries have restructured their financial markets into market-based systems, and demand from firms for direct financing has been increasing, but the structure of domestic financial markets in most of the countries is extremely weak, and their financial services markets have also been eroded by foreign capital.

Table 5) Performance of Lead Managers in Korea-related International Bond Markets
(As of Aug, 2005)

Company	Rank	Share (%)	Amount (million \$)	Fee (%)	Issue Number
JP Morgan	1	14.00	1,238	0.50	6
Citigroup	2	12.30	1,088	0.46	9
Barclays Capital	3	8.60	762	0.29	7
ABN AMRO Bank NV	4	8.40	743	0.16	6
UBS	5	7.20	642	0.99	5
BNP Paribas Group	6	6.60	580	0.60	11
Credit Suisse First Boston	7	5.50	483	0.15	3
Deutsche Bank AG	8	5.10	451	0.61	3
HSBC	9	3.90	348	0.28	6
Korea Development Bank	10	3.80	340	0.30	4
Daiwa Securities SMBC Co Ltd	11	3.70	326	0.30	5
Merrill Lynch & Co	12	3.70	325	1.38	4
Bank of America	13	3.20	282	n/a	6
Standard Chartered PLC	14	3.20	280	n/a	16
Mizuho	15	1.90	168	0.35	1
Nomura Holdings Inc	16	1.90	168	0.00	5
Lehman Brothers	17	1.70	150	n/a	1
Goldman Sachs & Co	18	1.10	100	n/a	1
Daewoo Securities Co Ltd	19	1.10	100	0.30	2
Woori Investment & Securities Co Ltd	20	1.00	92	0.30	1

Source) Bloomberg, Jeon YongSuk (2005)

3. Legal and Regulatory Impediments to Building an Asian Bond Market

Asian bond markets are very fragmented compared to EU bond markets because each country has heterogeneous legal and regulatory frameworks which impede the development of cross-border bond markets. In this section we therefore review legal and regulatory impediments, in particular in Japan and Korea, in order to study the feasibility of the “Dual Core Approach” to cross-border settlement and consider the requirements for common rules, the so-called “Asian Bond Standards,” in the region to enable a cross-border Asian Bond market.

3.1 Withholding Tax

A Korean resident is defined as an individual who has a domicile or has been residing in the country for at least 12 months. Neither residents nor non-residents pay capital gains tax on securities transactions, however securities transaction tax is levied on stock

transactions (not bonds transactions). Tax rates are often reduced or completely waived under the applicable double taxation treaties, or agreements between Korea and the investors' countries.

Tax on Returns from Foreign Investors' Holding of Local Bonds

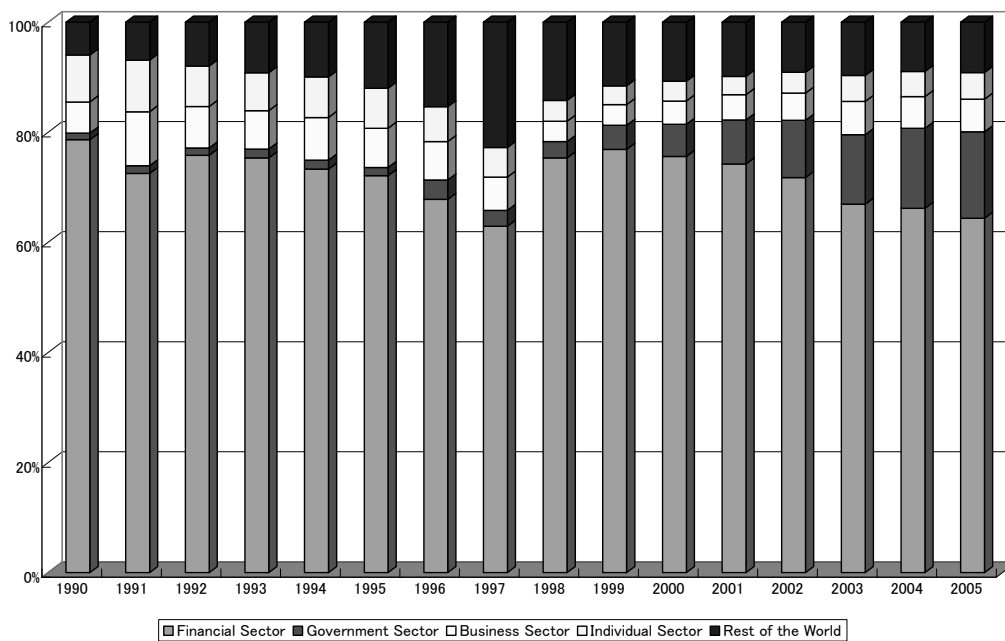
	Withholding tax on interest income	Capital gains tax
Japan	No withholding tax for JGBs if a number of requirements are satisfied	No Tax
Korea	14% withholding tax. (Combined taxes result in an effective rate of 15.4%.)	10% of gross proceeds or 25% of capital gains, whichever is lower.

Source) AsianBondsOnline, Asian Development Bank; updated by the authors

Foreign ownership of bonds increased to 22% in 1997. Following the crisis it decreased sharply, reaching 9% in 2005. Since then, foreign investors have favored stocks over bonds. The share of foreign investment in stocks increased to 22.9% of total stock investments in 2005.

The participation of foreign investors in the Korean bond market is extremely limited compared with that of other countries, in particular EU countries. One of the reasons for this low participation is withholding tax on the interest income from bonds and cumbersome tax reclaim procedures. In Korea, withholding tax is levied on the interest income earned by non-residents. The Korean bond market is therefore not particularly attractive to foreign investors.

Figure 5) Composition of Ownership of Bonds (Korea)



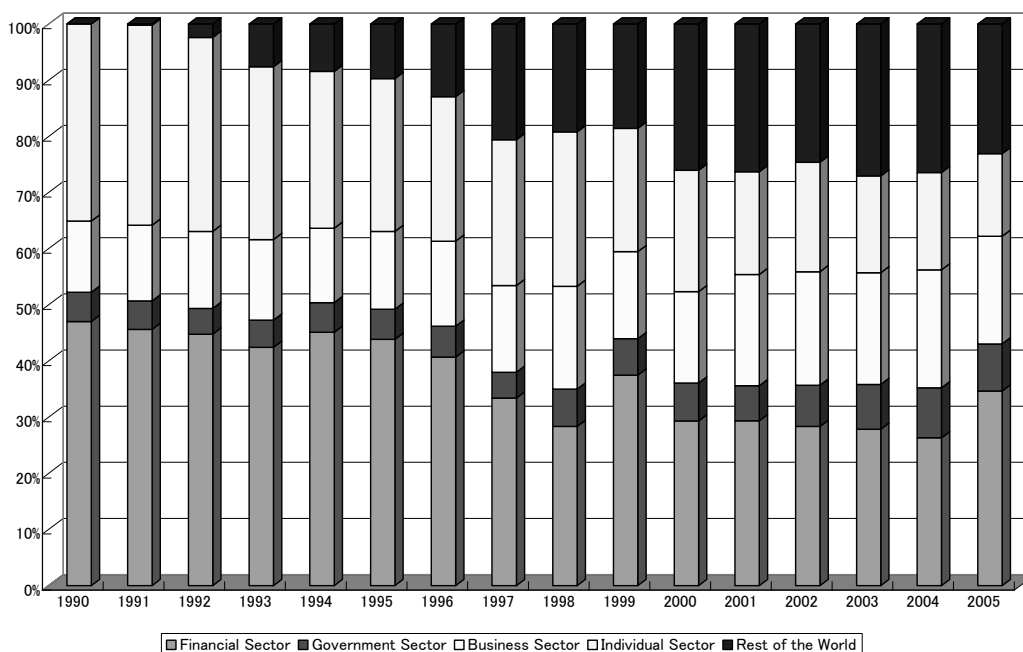
Source) Bank of Korea, Flow of Funds

* Bonds consist of government & public bonds, financial debentures, corporate bonds and external bonds.

Another factor of low foreign participation is that the underdeveloped Korean repo market makes foreign investors feel difficult to effectively hedge volatility and risks and to make arbitrage trading. Also the history of the Korean repo market is also short and the scope of participants is extensive, and the majority of institutional investors therefore prefer the call market to the repo market.

Therefore withholding tax should be reduced or exempted in order to attract more foreign investments and activate domestic bond markets as well as to develop Asian regional bond market. In addition, higher transaction costs and exchange rate risk hinder the purchase of Korean bonds by foreign investors. Building an efficient and standardised repo market could provide an instrument to hedge against risk and to facilitate cross-border transactions in the regional bond market.

Figure 6) Composition of Ownership of Stocks (Korea)



Source) Bank of Korea, Flow of Funds

3.2 Regulations on Securities Issuance

Won-denominated bonds issued in Korea by non-residents are called “Arirang bonds.” The Korean regulatory authority has been promoting this market by reducing the burden of documentation in the Korean language. However, securities issued by non-residents in Korea are required to be graded by local credit rating agencies¹⁵. Recently non-residents have issued dollar-denominated bonds, so called “Kimchi bonds,” in the domestic market. This is expected to contribute to the development of the domestic financial market and the effective utilisation of the foreign currency reserves accumulated since the crisis.

¹⁵ There are four local credit rating agencies, Korea Investor Service (KIS), Korea Ratings, National Information and Credit Evaluation (NICE) and Seoul Credit Rating & Information (SCRI).

Issuance of Local Bonds by Non-residents

	Japan	Korea
Bond issuance by non-residents	allowed	Allowed (prior to MOFE or permission from MOFE if necessary)
Local rating/ Local listing	Not required/Not required	Required/ Not required
Governing Law	Japanese law	Korean law
Documentation	Japanese	Korean
Time required to obtain approval	1-2 weeks	n.a.
Typical duration of issuance process	2-3 months	2 weeks

Source) Takeuchi (2005)

3.3 Capital Control

Non-resident investors in Korea are required to obtain an “Investment Registration Certificate” (IRC) from the Financial Supervisory Service (FSS). Additionally, non-resident investors are not allowed to trade directly on the over-the-counter (OTC) market.

Credit and loans of more than 1,000 million won denominated by a borrower in local currency and granted by institutional investors require Bank of Korea approval. Furthermore, won purchases by foreign investors must be associated with securities transactions.

Capital Controls

	Local Currency		Foreign Currency	
	Outward	Inward	Outward	Inward
Japan	No restrictions		No restrictions	
Korea	No restrictions		Not to exceed amount imported and declared	Reporting Required

Source) AsianBondsOnline, Asian Development Bank

3.4 Risks in Cross-border Linkages

Cross-border linkages of clearing and settlement determine the form of depository, credit, securities lending, and custodian services. The choice of settlement services and functions determines the design of the linkages. This is because the form of the central securities depository (CSD) and the applicable legal framework differ in each country. Cross-border linkages can also reduce costs to participants of meeting various collateral requirements, and reduce the number of intermediaries engaged in cross-border settlements. However, because they operate under differing governing laws, CSDs must design linkages carefully to ensure that risks can be reduced. This means that they must address legal and operational problems which are more complex and challenging than those confronted in their domestic operations.

Clearing and Settlement of Bonds

	Japan	Korea
International Linkage	Euroclear (ICSD) ¹⁶	Euroclear, Clearstream ¹⁷ CMU (Hong Kong) JSSC (Japan) ¹⁸
RTGS/DVP	Yes	Yes
Settlement Cycle	T+3	T+0
Settlement Organisation for Government Bonds	Bank of Japan-NET JGB Services owned by the Bank of Japan	Korea Securities Depository (KSD) operated by the Korea Stock Exchange (KRX)
Settlement Organisation for Unlisted Corporate Bonds	Counterparties settle transactions at registrar banks using Japan Bond Settlement Network (JB Net). A book entry system will be set up in January 2006.	KSD operated by KRX.
Settlement Organisation for Bonds Traded on a Stock Exchange (Government and Corporate)	Bank of Japan-NET JGB Services for listed JGBs; Delivery of physical certificates for listed corporate bonds.	KSD operated by KRX.

Source) AsianBondsOnline (<http://asianbondsonline.adb.org>); updated by the authors

4. On the Feasibility of a “Dual Core Approach”

More attention has recently been paid to regional settlement intermediary in Asia in order to enhance regional market infrastructure as a public infrastructure¹⁹. Hong Kong and Korea have each proposed a regional settlement system owing to the inconvenience and limitation and the low coverage of ICSD, Euroclear and Clearstream. The Hong Kong Monetary Authority (HKMA) has proposed the establishment of “AsiaClear” as a regional settlement infrastructure for clearing and settling Asian Bonds. This would bilaterally connect the existing clearing and settlement systems (NCSD) in the Asian region using IT. Korea has proposed “AsiaSettle” as a new regional ICSD, pointing out the limits of bilateral linkages. Japan has proposed a dual core approach to cross-border securities settlement using the existing systems JASDEC and KSD. This chapter will explore the feasibility of a dual core approach from the perspective of Korean law and systems.

Table 6) Comparison of Proposed Regional Settlement Systems

	Country	Linkage	
AsiaClear	Hong Kong	Bilateral Linkage	Virtual CSD
AsiaSettle	Korea	Multilateral Linkage	New ICSD
Dual Core Approach	Japan	Bilateral Linkage	JASDEC-KSD
Regional Settlement Intermediary (RSI)	ADB	Multilateral Linkage	Asian ICSD

With regard to the issuing of securities using the law of the issuer’s country as

¹⁶ Euroclear expands the coverage of Asian securities settlement with Japanese government bonds.

¹⁷ KSD opens accounts to deposit international bonds owned by Korean investors (one-way linkage)

¹⁸ When Korean firms are listed on the stock exchange in both Korea and Japan, JSSC opens the consolidated accounts at KSD to deposit the listed stocks (one-way linkage especially for depositing stocks)

¹⁹ Please refer to http://asianbondsonline.adb.org/documents/14_ADB_Rhee_Taylor.pdf for recent discussion

governing law and the sale of the securities overseas (i.e. the issuance of securities by Japanese firms based on Japanese law and their sale to Japanese and Korean investors, or the issuance of securities by Korean firms based on Korean law and their sale to Korean and Japanese investors), there would be no problem regarding the purchase or depositing of securities by foreign investors other than certain matters relating to linkages between the NCSD of the two countries.

First, there is no impediment to the issuing of securities under Japanese law and their sale to Korean investors. Under the current system, foreign currency-denominated securities held by Korean investors are deposited at Euroclear or other international CSDs appointed by the KSD. Japanese securities held by Korean investors could therefore be deposited at JASDEC.

However, there are some problems in the regulations when securities issued by Korean firms are sold to Japanese investors. Foreign investors who purchase Korean securities must observe Articles 7-5 and 7-19 of the “Securities Business Supervision Regulation” (Chapter Two). Japanese investors must register at the Korea FSS themselves or through a proxy appointed by them. Foreign investors must open accounts at authorised foreign exchange banks. However, to enable monitoring, omnibus accounts are not permitted²⁰. The revision or abolition of the above regulations is required for a dual core approach to operate smoothly (JASDEC should register under its own name or be excluded from the above regulations)

Based on Article 7-28 of the “Foreign Exchange Transaction Regulation”, sellers of securities overseas can deposit at international settlement organisations or foreign CSD. Securities issued by Korean firms can therefore be deposited at JASDEC. However, issuance must be reported to the MOFE and additionally Korean securities cannot be cleared using Korean currency (won) overseas because the Korean won is not an internationalised currency.

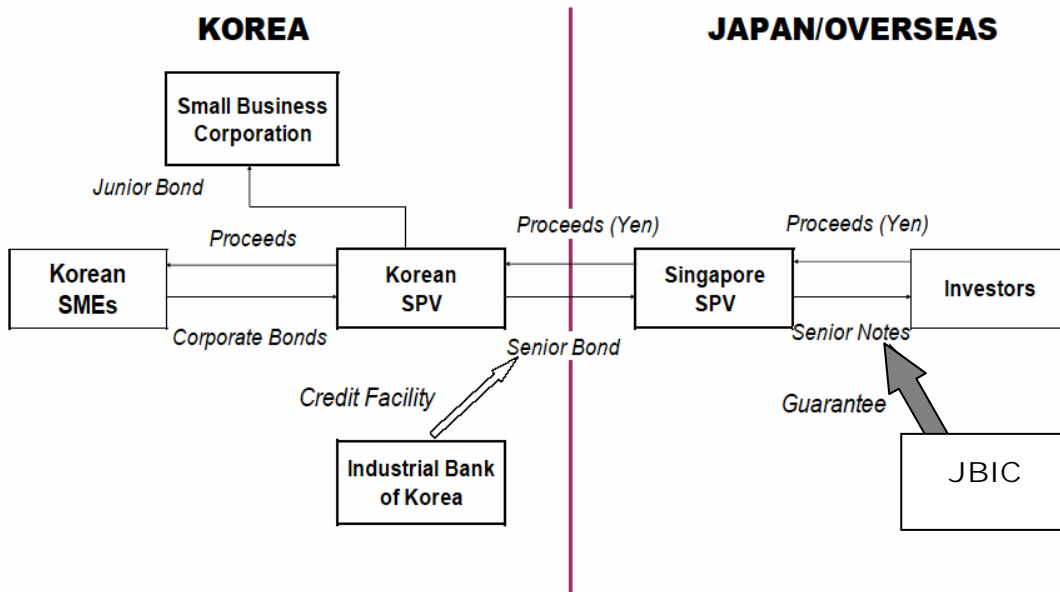
Regulations and institutional frameworks must be revised or abolished in order to enable the smooth settlement of international Asian Bonds like Eurobonds rather than Samurai bonds or Arirang bonds by an international Asian CSD using a dual core approach. The question of whether international Asian Bonds can be regarded as international bonds like Eurobonds is also linked to the problem of circulation overseas. To issue and circulate bonds overseas, it will be necessary to link each NCSD and deposit the securities undertaken. This requires each NCSD to deposit and circulate the issued securities.

For example, if a Japanese firm tries to issue international Asian Bonds in Hong Kong (or Singapore) and sell to Asian investors, each Asian NCSD will have to open an omnibus account in its own name, and then each investor can deposit securities at CCASS (or DCSS)²¹. In this case, trading among domestic investors in each country will not affect the omnibus account at CCASS (or DCSS) in the name of the relevant foreign CSD because they are traded among domestic investors.

²⁰ According to Foreign Exchange Liberalization Plan announced in May 2006, foreign investors will be permitted to have omnibus accounts at ICSD in order to facilitate investments in Korea’s local bond and monetary stabilization bonds. This Plan aims to make Korea Won an international currency for a medium-long term task.

²¹ The CCASS, or Central Clearing and Settlement System, is wholly owned by Hong Kong Exchanges (HKEx); DCSS is the Debt Securities Clearing and Settlement System operated by the Stock Exchange of Singapore (SGX).

Figure 8) Pan-Asia CBO Issuance by Korean SMEs

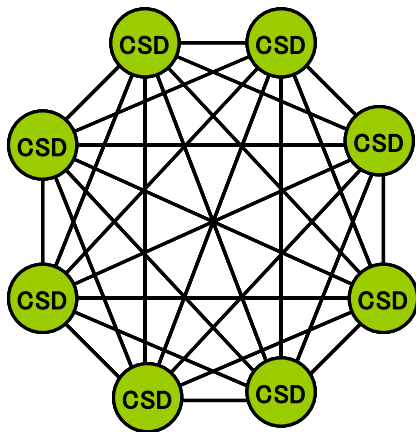


Source) Japan Bank for International Cooperation (JBIC)

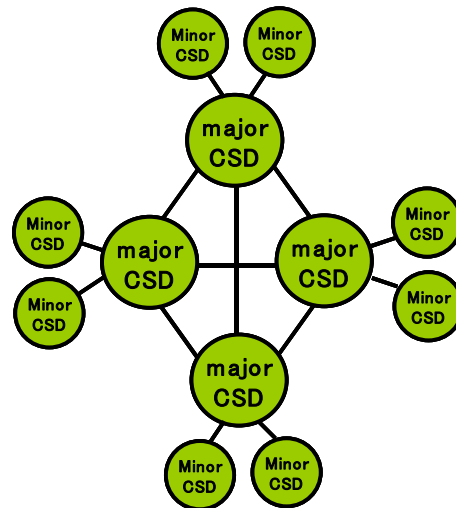
Another possibility for regional settlement system would be to establish a separate Asian CSD to enable settlement, clearance and depositing in the region, as in the “AsiaSettle” model proposed by Korea (Oh et al, 2004)

Figure 9) Bilateral Linkages between NCSDs

(1) Eurolinks Real- Time Network
(Spaghetti Model)



(2) European Financial Superhighway
(Canneloni Model)



Source) Huh, Hang Jin (2005)

5. Summary and Conclusion

Fostering Asian Bond markets could offer an alternative which will provide opportunities for long-term financing and enable the circulation of savings and

highly-accumulated foreign exchange reserves in the region. However Asian Bond markets are very fragmented because of different and heterogeneous regulatory and legal framework of each country and the size of Asian Bond markets is very small compare with those of bond markets in US and EU. Therefore it is very important to link these fragmented Asian Bond markets or create regional common bond markets for the Asian bond markets with depth and volume. Cross-border securities settlement in the region, achieved through the linkage and cooperation of regional financial markets, is one of the essential elements in ensuring that an Asian Bond market functions effectively and regionally. Furthermore, legal and institutional impediments need to be cleared away or each country's laws and regulations should be harmonized or adjusted to correspond to international standards or "Asian Bond Standards" in order to further develop an Asian Bond market, with cooperation of the government of each country.

Under the current legal framework in Korea, when stock is issued overseas, Korean law should be the governing law, but the governing law of depository receipts of overseas securities is the governing law of the country in which the securities are deposited. The fact that the overseas issuance of bonds depends on the laws of the country of issuance represents a problem. Korean securities-related laws require systematic reorganisation in the near future in order to avoid excessive dependence on English law and New York state law and to enable issuance of "Asian Inter-Regional Bonds" in a common regional off-shore market (Asian Inter-Regional Professional Securities Market).

(Hyun Suk†)

†This paper was written when the author worked at National Institute for Research Advancement (NIRA) and it doesn't represent the official view of ABMI Task Force of Japan Bank for International Cooperation (JBIC) where the author currently belongs to.

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8 . Issues related to Bond Market Legal Systems in Asia

The Current Situation

Few Asian countries have well-developed bond markets. Apart from government bond markets, and also aside from a handful of countries like the United States and Britain, there are actually few countries in the world that have well-developed markets for corporate bonds.

Having said this, however, many countries in recent years have been gradually developing bond markets. In seeking to develop viable bond markets, Japan, South Korea and other Asian countries are facing difficult problems with regard to legal systems and market infrastructures as well as constraints arising from conventional market practices.

For example, electric power companies in Japan regularly issue corporate bonds, but there is some question as to whether these electric power bonds can be described as ordinary corporate bonds. Electric power bonds are placed as general mortgage bonds, bonds secured by blanket mortgages on the company's property. General mortgages provide bondholders with prior lien, enabling them to receive repayments from corporate assets of issuers ahead of other creditors. In this sense, electric power bonds are positioned as something different from ordinary corporate bonds.

In Japan, however, ordinary listed companies are not issuing corporate bonds frequently. Although they are quite active issuers of equity-linked bonds, they do not issue many ordinary straight corporate bonds. Yet, Japan is now seeing an increasing amount of corporate bonds.

There are quite a number of problems to deal with in an effort to develop bond markets in other Asian countries that are at different stages of development in terms of their respective financial and capital markets.

The Future of Legal Systems for Corporate Bonds

In discussing the modality of bond markets in Asia, including Japan, it is necessary to consider, among all market infrastructures, the development of settlement infrastructure, including securities settlement (delivery and receipt of funds and securities). When we focus on legal aspects, there is the problem of "the future of legal systems for corporate bonds." For example, we have to deal with (1) securities issuance procedures, including whether program issuance is possible; (2) problems related to the Securities and Exchange Law and the Financial Instruments and Exchange Law, including information disclosure systems; and (3) problems with legal frameworks for bonds (many of which are related to legal systems for companies), as the basic point of discussion necessary for market infrastructure development.

< Application of Law with an International Scope >

The first issue that needs to be addressed is the modality of application of law with an international scope. While Japanese companies issue many cross-border equity-linked and other foreign bonds, it is not necessarily clear which national laws are applicable. If we assume that corporate bonds are governed purely by "the relationship of private law," it can then be said that it is determined by rules of international private

law under the principle of party autonomy. However, this is not necessarily the case.

For example, under the Company Law of Japan, resolutions adopted at meetings of bondholders need to be approved by courts, and there is a strong argument that this is also applicable to corporate bonds Japanese companies issue overseas as “forcible provisions.” Still, this interpretation has yet to become an established theory.

< Commissioned Companies and Meetings of Bondholders >

Secondly, there are problems concerning commissioned companies for corporate bonds and meetings of bondholders. In light of actual defaults experienced in Japan in recent years, there are ongoing discussions on the modality of commissioned companies and on the problem of whether meetings of bondholders can actually be convened.

In particular, there are the following problems concerning the unique Japanese system of commissioned companies for corporate bonds. When the revised Commercial Code of 1993 made the designation of commissioned companies mandatory as a measure in exchange for the abolition of the regulatory ceiling on the amount of corporate bond issuance, a Justice Ministry official presented the interpretation that “when contracting parties to foreign bond issuance designate the Commercial Code as governing law for corporate bond indentures in foreign bond issuance, all relevant Commercial Code provisions regarding corporate bond indentures are applicable, in principle, including forcible provisions such as provisions regarding the mandatory designation of commissioned companies.” Since then, it has become the established practice that British law serves as governing law for Eurobonds issued by Japanese companies under the FA (fiscal agent) formula without designating commissioned companies.

Subsequently, the new Company Law put into force in 2006 provided the definition of corporate bonds²³. A Justice Ministry responsible for the new law referred to the mandatory designation of commissioned companies in his explanation of the definition, generating renewed debate as to whether Eurobonds, Asian Bonds and other so-called foreign bonds issued by Japanese companies, regardless of governing law for their issuance, can be exempt from the mandatory designation of commissioned companies under the Company Law, a factor which would push up the cost of foreign bond issuance, and whether foreign bonds can be issued at all as bonds that are not corporate bonds as defined by the Company Law not pursuant to the mandatory designation of commissioned companies.

Recently, Justice Ministry officials confirmed that with the enforcement of the new Company Law, it now is theoretically possible for Japanese companies to issue bonds that are not defined as corporate bonds under the Corporate Law. Thus, Japanese companies are now in the process of looking for ways to issue bonds under that formula, on the basis of primary and secondary market practices for ordinary Eurobonds. One point of concern here was that there are no written tax-related provisions for such bonds. But the National Tax Agency’s relevant division has confirmed that the definition of foreign bonds issued by private-sector issuers subject to exemptions from the withholding income tax on interest income under the special taxation measures law also covers “bonds with the same seniority as corporate bonds” including Euroyen bonds

²³ Under the new definition of corporate bonds (Article 2, item 23 of the Company Law), only bonds that are allotted and redeemed in accordance with provisions of the Company Law are deemed corporate bonds, and companies were allowed to issue bonds that are not defined as corporate bonds.

issued overseas by residents.

However, aside from foreign bonds, it would not be so easy to actually issue bonds domestically that are not defined as corporate bonds under the Company Law, given that primary and secondary market practices have yet to be established for such bonds and legal frameworks for them have yet to be developed.

Under the circumstances, as a short-term solution for the sake of smooth issuance of foreign bonds, it is deemed desirable to issue foreign bonds as previously, as corporate bonds as defined under the Company Law while seeking to clarify exemptions from forcible provisions of the law, including the mandatory designation of commissioned companies. It is safe to say that Justice Ministry officials responsible for lawmaking are also moving in that direction.

More specifically, it concerns the following two cases in which the requirement for the designation of commissioned companies is waived: (1) when the value of each corporate bond is ¥100 million or more under the so-called FA formula that does not designate commissioned companies (the proviso of Article 702 of the current Company Law; and (2) when the number obtained from dividing the total amount of corporate bonds by the minimum value of the amount of each bond is less than 50 (Article 169 of enforcement regulations of the Company Law).

Going forward, however, in order to secure more stable issuance of foreign bonds, it seems desirable to permit exemptions from the mandatory designation of commissioned companies in cases, even if limited to foreign bonds, other than cases (1) and (2) above.

< Application of Laws to Bonds Other Than Corporate Bonds >

The third issue has to do with bonds issued by entities other than business corporations. A variety of organisations, including local public entities and public-private (third-sector) entities, have recently begun issuing bonds, and the market has even seen the emergence of school bonds (bonds issued by educational corporations) and hospital bonds (bonds issued by medical institutions). In Japan, however, these bonds have not been regarded as securities under private law, with neither the Commercial Code nor the Securities and Exchange Law being applicable to them. This certainly raises questions as to whether the current situation is acceptable. However, it should be noted that the Financial Instruments and Exchange Law, which replaced the Securities and Exchange Law in 2007, applies to such bonds (with the exception of hospital bonds).

< Dealing with Samurai Bonds in Case of Default >

Lastly, there is the problem of how to handle sovereign bonds issued by foreign governments and other issuers in Japan in case of default. Since samurai bonds, issued as yen-denominated bonds in Japan, are issued by foreign governments, there have been no previous experiences of default. In recent years, however, samurai bonds issued by Argentina and Uruguay have gone into default. While meetings of holders of these bonds were held in Japan, neither the Commercial Code nor the Company Law was directly applied to these cases of default.

Compared with loans, the handling of defaults on bonds is less clear. Most of the problems involved are related to contracting clauses.

The first issue is whether the principal can be cut on a majority vote of bondholders when default is about to occur. This concerns the corrective action clause (CAC). In the

absence of a system in which the principal reduction on a majority vote of creditors is approved by court, like the system under the Company Law, the question is whether the principal cut can be implemented immediately when creditors hold a meeting and decide to cut the principal on a majority vote despite objections from the minority.

The second issue has to do with commissioned companies. The question is whether it is possible, in case of default, to choose commissioned companies for samurai bonds, like those for Japanese corporate bonds, or their equivalents (in some cases, such entities have been designated in advance), and have them enact judicial proceedings on behalf of creditors.

Third, there is the issue related to the pari passu clause. The meaning of pari passu is not clearly understood if Uruguay and Argentina state that they will not pay even if we sue them. This raises the question as to how to ensure an orderly recovery of claims and how to negotiate repayments when sovereign debtors indicate that they cannot pay back funds.

It is necessary to reconsider legal frameworks for international bond markets, including the points discussed above, bringing to bear the experience of market professionals to develop basic market tools and apply broader perspectives.

(Hideki Kanda - English translation by NIRA secretariat)

9 .Experience of a Japanese Law Firm in Legal Practice related to Cross-Border Securities – Considerations concerning Euro & Samurai Bonds, Foreign Exchange Control and Governing Law*

Introduction

The legal practice of cross-border securities has a long history centering on the Euromarket, and its development has largely been the result of the work of European and U.S. lawyers. It is, however, both unexpected and surprising how little is known about this area of legal practice in Japan. Minutes from the Corporate Law (Modernisation) Subcommittee (the “Corporate Law Subcommittee” below) of the Legislative Council of the Ministry of Justice, which addressed the new Corporate Law to be enforced in May this year, indicate Japan’s current stance in this matter: substantive discussion on legal practices related to cross-border securities was suspended and postponed without precise understanding of practices already in use. Thus, legal revisions that should have been made under the new Corporate Law have not been made. Japan remains an insular nation.

Major recent currency market developments are the shift to the floating exchange rate system following the Nixon Shock of 1971 (the suspension of gold-dollar convertibility) and then the move to the managed floating rate system under the 1985 Plaza Agreement, the sharp fall of the British pound in the 1990s brought about by currency futures trading and hedge fund activity, and the Latin American and Asian currency crises (both these latter representing situations in which forces of the global market economy overwhelmed foreign exchange controls by national governments). It is noteworthy that as the scheme of East Asian economic integration at the state level has come to a near-stalemate, the Asian Bond Markets Initiative (ABMI)¹, proposed from the private-sector perspective (avoiding the delicate political issue of Asian monetary integration), has been making headway in practical terms.

The author has been involved in legal practice relating to cross-border securities since the launch of the Tokyo capital market in 1973 but has not to date provided his fellow legal practitioners with sufficient relevant information in this area. This article therefore attempts to offer a brief outline of legal practices related to cross-border securities.

1. Offering of Securities by Domestic Issuers for Subscription Overseas

A viable primary issue market for securities requires the existence of a secondary market for the securities issued.

Thus, the depositary receipt (DR) method was initially employed for public subscriptions of Japanese equity shares in foreign countries. Depositary receipts were issued to investors in the United States and Europe in exchange for original stock certificates deposited with U.S. and European financial institutions, and those depositary receipts were listed for trading on the New York and London exchanges. The method started with American depositary receipts (ADRs) in the U.S. market and then spread to the Euromarket as Euro depositary receipts (EDRs). But the DR method is no longer in use and has been replaced by the original stock method. This duplication of

* This paper is an English translation of an extract from the book “Cross Border Securities Transactions and Corporate Finance,” Kinzai Institute for Financial Affairs, Inc., 2006, published by the author

work and costs represents sheer waste given that Japan's securities exchanges now require timely disclosure by issuers and stocks are priced with the participation of investors from around the world. However, the DR method remains in place for Chinese and Indian stock because the secondary markets for original stocks have yet to be fully developed in these jurisdictions.

The existence of the secondary market is also important for the primary issue market in the bond industry, but it is not as important as it is for the stock market because there is an alternative means of recovering the funds invested, namely holding bonds to maturity. In the case of convertible bonds (CBs), the market for the stocks into which the bonds are converted, or the market where convertible options can be separated and traded, are the most important.

Issuance of so-called external bonds in the post-war period began with the U.S. market, which was regulated by the 1933 U.S. securities Act, and then shifted to the unregulated Eurodollar market, the German mark market, the Swiss franc market and the Euroyen market. At present, the primary issue markets for convertible bonds of Japanese issuers are the Euroyen market and the Alpine (yen-denominated) Euro Swiss franc market.

It is now presumably well known that the Euromarket is neither the Euro market, in which the EU's common currency circulates, nor Europe at large. However, there are probably few people who could give a ready answer when asked what the Euromarket is in legal terms. Legally speaking, the Euromarket is a market that is exempt from the legal regulations that exist for the protection of the investing public in industrialised nations, including the euro zone. Roughly speaking, under securities law in Japan, securities can be privately placed with qualified institutional investors by simply filing reports with the Financial Services Agency (but only in respect of investment fund securities). Foreign securities companies can, from outside Japan, freely solicit subscriptions from designated financial institutions among these qualified institutional investors. In the fairly liberalised markets of other industrialised nations, the definition of professional investors is broader than the category of qualified institutional investors in Japan, and professional investors are exempt from regulations under their respective national laws. The global federated markets in which these investors operate may be defined as the Euromarket from the legal perspective. Investment funds are professional investors, and individual investors can participate in trading on the Euromarket through investment funds.

In the Euromarket, there are a variety of practices that make trading more convenient for participants. The International Primary Market Association (IPMA) has been established as a self-regulating organisation to help disseminate knowledge about these trade practices and to maintain order in the Euromarket given the expansion of the Euromarket itself as well as the increase in the number of market participants. The IPMA HANDBOOK consists of guidelines, often referred to as recommendations, and standard contract forms. (The Euromarket now appears to be moving from being a free market towards becoming a regulated market. With the introduction of the Prospectus Directive and the Transparency Directive, the self-regulated markets in EU member states are coming under EU-wide official regulations. The adoption of international accounting standards (IAS) is being imposed. These developments deserve close attention.)

2. Offering of Securities by Foreign Issuers for Domestic Subscription

The public offering by General Telephone and Electronics, Inc. (GTE) in 1972, the first case of a domestic public offering of foreign stocks, adopted the original stock method instead of the depositary receipt format because the U.S. stock market was already an efficient market. As the Tokyo Stock Exchange (TSE) did not have fully developed listing criteria at the time, GTE stocks were not listed on the TSE and were traded under a system that is, in effect, the same as the present system for foreign stock trading (Japanese securities firms acquire stock certificates to be held by U.S. custodians and hand custody receipts to Japanese investors)². Indeed, this can be described as a judgment with great foresight, given the present status of foreign stock trading on the TSE, where trading flows are very limited and prices are formed essentially in home markets and most foreign issuers have de-listed their stocks from the exchange.

The first case of a domestic public offering of foreign bonds was the 1973 issuance of Australian government bonds, placed within the samurai bonds framework in line with recommendations issued on February 5, 1973, by the Securities and Exchange Council. Asian Development Bank bonds and World Bank bonds had been offered prior to this, but they were accorded special treatment as international financial institutions exempt from disclosure requirements under the Securities Act. Thus, given the present framework for samurai bonds, it would be appropriate to regard the Australian government bond as the first samurai issue in accordance with the aforementioned Securities and Exchange Council recommendations.

Subsequently, the issuance of samurai bonds reached a record high in 1977, but in that particular year, ironically, the European Investment Bank (EIB) was permitted to issue the first Euroyen bond as a nonresident. After issuer qualifications for nonresident Euroyen bonds were substantially eased (at the same time, the ban on the issuance of Euroyen bonds by residents was lifted) following the Japan-U.S. Yen-Dollar Committee in 1984, issuers increasingly shunned the rigid, high-cost samurai bond market in favor of the Euroyen bond market, a trend that has essentially been sustained until the present.

3. Governing Law for Eurobonds

The author is often asked the question: “Why are Eurobonds governed by the laws of the issuer’s country, when international loan contracts are governed by the laws of the lender’s country?” It is true that German mark bonds, which disappeared with the birth of the euro, and Swiss franc bonds (including yen-denominated Alpine bonds), are governed by German law and Swiss law, respectively. However, this can primarily be traced to the fact that bond underwriters are registered in Germany or Switzerland and the places of subscription are Germany or Switzerland. In a manner of speaking, they are samurai bonds issued in Germany or Switzerland.

In the case of more recent Swiss bonds, subscriptions are also solicited from outside Switzerland (the Euromarket). But the lead managers for these bonds still have to be banks located in Switzerland, and under the unique Swiss system, from the viewpoint of bond issuers, bondholders are the Swiss banks that underwrite the bonds. Swiss bond issuance contracts provide that “an issuer is exempt from obligations of payments to investors if the issuer pays principal and interest to the Swiss bank concerned,” while issuance contracts for Swiss CBs provide that “when an issuer complies with the request for conversion made by the Swiss bank concerned, it is deemed that the issuer complies

with the request for conversion by holders of CBs.” This is a special Swiss circumstance in which Swiss banks are required to treat information on customers as classified information.

As for German mark bonds, the issuance of Euromark bonds, for which subscriptions could be solicited outside Germany, was quite active from the early stages. In the case of Euromark bonds, it may have been theoretically possible to adopt the domestic laws of the issuer’s country outside Germany as governing laws, since they did not involve special circumstances such as those for Swiss bonds. However, it was understood that the German laws were the governing laws because Euromark bonds, like German mark bonds, were prepared in the German language, including issue contracts, and the secondary markets after public offerings were securities exchanges in Germany. These working practices are understood to be the same as those applicable to Samurai bonds, which are denominated in yen, prepared in the Japanese language and are governed by Japanese laws, and for which the secondary market after public offerings is the TSE.

However, for Eurobonds (historically, Eurodollar bonds), including Euroyen bonds, public offerings are made on a global scale (in countries where local securities regulations are applicable, public offerings are made with exemption from such local securities regulations) with English as the language used, and their secondary market after issuance is the global inter-bank market. In this sense, it is reasonable to adopt the domestic laws of the issuer’s country as the laws governing these bonds. From the standpoint of investors around the world, it would be unfair to adopt the domestic laws of any particular country. For issuers, adopting the domestic laws of their own countries makes it easier for them to respond to investor claims. That said, less industrialised countries have historically tended to use English when issuing in the Euromarket, and given this, adopting British laws as the governing law may well be described as fair.

In the case of CBs, it is more desirable to adopt the domestic laws of the issuer’s country as the governing laws in order to avoid misinterpretation, because CBs are products closely linked to stocks, which are governed by the domestic laws of the countries in which the issuing companies were founded. At one time, for warrant bonds governed by British laws, there were provisions for a meeting of those with subscription warrant rights which is not found in Japanese law. As a legacy of this practice, in the case of CBs at present, matters for decision at bondholder meetings include “an alteration in the contents of subscription rights, which is not possible under Japanese law.” It seems somewhat strange that nobody dares to challenge this simply because of precedent.

In the world of bonds, governing laws should follow the country-of-origin principle. Under current circumstances, corporate bonds that should be labeled as “Made in Japan” are instead marked as “Made in the U.K.”³

4. Foreign Bonds, Foreign Exchange Control and Liberalisation of the Yen

While the currency of denomination for bonds is the currency of a sovereign state, bonds are used not as a means of payment but as a means of high-risk, high-return savings. Bonds require disclosure of information on the creditworthiness of issuers. Unlike currencies, however, for bonds there is no institution to control supply, such as a central bank in the case of currencies. However, the markets control the supply of bonds through interest rates. Money laundering regulations and the Patriot Act are not

applicable to bonds.

Bonds are created under contracts and, as such, terms and governing laws can be varied for bonds under the principle of freedom of contract. Unlike currencies, which only sovereign states have the right to issue, bonds represent credit that can be created by the private sector. However, because the value of bonds is expressed by denomination in existing currencies and because they are paid for in existing currencies (aside from the ECU basket account, which was transformed into the euro, but even in this case the currency basket backs up the currency account), issuance of bonds is fundamentally affected by policies that restrict foreign exchange transactions in the countries of the currencies concerned and policies for the liberalisation of those currencies (for example, the Chinese yuan cannot be taken out of the country at present).

These relationships may be summarised together with the governing laws as follows, with Japan's foreign exchange policy and yen liberalisation policy as the core:

Yen-denominated bonds Foreign currency-denominated bonds	Domestic issuers	Foreign issuers	Governing law for bonds
Domestic market (Securities Exchange Law)	Domestic bonds <i>(May be possible theoretically, but not practical)</i>	<i>Samurai bonds</i> Shogun bonds	Japanese law
U.S. market (1933 Act)	× <i>\$ denominated foreign bond</i>	× N.A.	U.S. law
Swiss market — Including Euro Swiss bond (Swiss law)	<i>Alpine bond</i> <i>SFr denominated foreign bond</i>	○ N.A.	Swiss law
Euromarket (Euromarket trade practices)	Euroyen bond <i>\$,Euro-denominated foreign bond</i>	○ N.A.	Domestic laws for issuers from industrialised nations (British law for issuers from Japan and less-industrialised nations)

- × : Nonexistent
- Italic* : Made possible by the easing of foreign exchange controls and liberalisation of the yen
- N.A. : Not applicable to Japan
- : Made possible by the Japanese government relinquishing licensing rights for Euroyen bond issuance by nonresidents
- () : Governing law for underwriting (trading)

The history of the relationships in the above table may be explained as follows:

- 1970 : The Tokyo capital market inaugurated = internationalisation of the yen :
Asian Development Bank bond
- 1971 : Nixon Shock : Dollar-gold convertibility suspended—shift of the yen to the floating rate system in 1973
- 1972 : GTE stock public offering in Japan (first foreign stock)
- 1973 : Australian government bond (first samurai bond issue)
- 1974 : 1st German mark public offering of a corporate bond (Mitsubishi Heavy Industries)
- 1975 : 1st Swiss franc public offering of a corporate bond (Mitsubishi Chemical)
- 1977 : ①Expansion of foreign exchange reserves, yen interest rates drop due to a decline in private-sector fund demand : a record issuance of samurai bonds
②Lifting of the ban on the issue of Euroyen bonds by nonresidents : 1st issue by the European Investment Bank (EIB)
- 1984 : Japan-U.S. Yen-Dollar Committee (Japan-U.S. financial market frictions prompting further internationalisation of the yen)
①Substantial easing of issuer qualifications for nonresident Euroyen bonds
②Lifting of the ban on the issue of Euroyen bonds by residents : Euroyen bonds, 1st issue=Mitsubishi Heavy Industries' Euroyen CB worth ¥30 billion (180-day restriction on the recycling of Euroyen bonds to Japan – ban on bringing them in)
- 1985 : Plaza Agreement (major industrialised nations' coordinated response to dollar interest rate rises due to the U.S. trade and fiscal deficits) : the managed floating exchange rate system
- 1990 : Weakening of the yen following the collapse of the bubble economy in Japan
- 1994 : Abolition of recycling restrictions on sovereign Euroyen bonds
1st Alpine bond issue
- 1996 : Foreign exchange control abolished under the Tokyo Big Bang by the Hashimoto Cabinet – Abolition of recycling restrictions on Euroyen bonds issued by residents
- 1997 : The Asian currency crisis, and failures of Sanyo Securities, Hokkaido Shokutaku Bank, Yamaichi Securities
- 1999 : Appreciation of the yen in the wake of the bursting of the U.S. IT bubble

5. Currency Market and Bond Market

The relationship between the currency market and the bond market may be broadly described as follows.

The place of the key currency in international financial transactions is increasingly being taken by the US dollar and the Euro. Despite Japan's economic strength, which is greater than that of the EU, and the yen's high degree of liberalisation, the yen has yet to establish itself as a key currency in the international financial market.

The financial market was formerly supplementary to the trade market. Today, however, the international financial market, consisting of the currency market and the capital market, is independent of the trade market.

Unlike the currency market, the capital market, which comprises bonds, stocks, and their futures and derivatives, is a private-sector market beyond the reach of sovereign authority, a free market in terms of both issuance and secondary trading (as long as governmental regulations, such as foreign exchange control laws, are not imposed at the local level). Funds flow freely to markets where risks and returns are fair.

At the macro level, division of the market into the Euro zone market, the US market and the Asian market is no longer viable at a time when the advancement of information

technology has made it possible to transfer funds and financial products instantly. Needless to say, from the micro perspective, regulations on dealers in financial products and restrictions on financial products for the protection of consumers exist at local levels. However, with particular reference to the latter restrictions, the Euromarket is well-known as a market for professionals (market participants for whom regulations at local levels can be exempted), and is increasingly making its presence felt as a global federated market.

Unlike the currency market, not only bonds denominated in key currencies but also bonds denominated in yen and various other currencies are issued and traded on the Euromarket.

On the other hand, as long as countries remain sovereign states, their own currency markets will continue to exist within their boundaries, and this will require the existence of local capital markets trading in bonds denominated in the currency of their country.

6. From U.K. Law Only to Split Law to Japanese Law Only to U.K. Law Only

Split law is the term used to refer to the operations of the London office of the former Hamada & Matsumoto (presently, Mori Hamada & Matsumoto) Law Firm, which was closed down in 1994. The term was coined by John Edwards, an influential partner with the former Linklaters & Paines. Issuance of Euro equity-linked bonds by Japanese companies became very popular prior to 1980, as firms sought to avoid the high cost of issue resulting from domestic regulations and practices and also favored flexible pricing in accordance with their corporate strength and creditworthiness. These bonds and their underwriting were governed by British law. Regular members at due diligence and documentation meetings for Japanese equity-linked bonds were the former firms Linklaters & Paines and Slaughter & May of Britain, who were lead underwriting managers, and such former law firms as Blakemore & Tsunematsu, Hamada & Matsumoto, Aoki & Christiansen, Tomotsune & Kimura and Mitsui & Yasuda, on the Japanese issuers' side.

Around 1980, there were only a little over 10 Japanese lawyers who were capable of dealing with Eurobonds, despite the fact that they were being issued in overwhelming numbers. Engagement in practice relating to Eurobonds was limited to those lawyers who were well versed in English and British and U.S. securities-related legal practices, having studied overseas (a limited number at that time), and who were interested in securities-related business. Moreover, too much time and energy was being wasted as the role of Japanese lawyers at due diligence documentation meetings was initially to act as interpreters. While Japanese lawyers were able to make preparations before those meetings by reading disclosure documents and internal documents written in Japanese, British law firms could not do the same and required one to two weeks of due diligence meetings.

Pre-war external bonds were governed by Japanese laws but payment and other procedures in foreign countries were conducted in accordance with systems in place in the countries of payment, as represented by fiscal agents. Underwriting operations followed the laws of the countries of the lead underwriting managers.

In order to cope with the sharp rise in Eurobond issuance in the early 1980s, the former Hamada & Matsumoto law firm came up with the idea of a reversal of the split in the pre-war split law method. Under this method, bonds were governed by British laws, as before, but underwriting contracts were governed by Japanese laws. This

coincided with a shift by Japanese issuers from U.S. and European securities firms to London-based subsidiaries of Japanese securities companies as lead managers for Eurobonds. Bonds were left governed by British laws as bank guarantees and financial covenants were commonly required at the time. This made the designation of trustees necessary or desirable but the Japanese Trust Law could not be used due to its ambiguous applicability.

An underwriting contract is a contract designed to warrant that the accuracy of a prospectus (it is often called an offering circular, a prospectus or an information memorandum, but is not covered by the Securities and Exchange Law of Japan and as such is not a prospectus as provided for by the Securities and Exchange Law) prepared by an issuing company for the issuance of a Eurobond are correct, that it states all material facts, and that it does not contain any misleading expressions. An underwriter pledges to underwrite and solicit subscriptions for the corporate bond in accordance with terms and conditions provided for by the contract.

Because the preparation of a prospectus is central to Eurobond issuance procedures, the global standard for cross-border securities calls for the preparatory work to be led by British or U.S. lawyers when an underwriting contract is governed by British or U.S. state laws and to be led by Japanese lawyers when an underwriting contract is governed by Japanese laws.

This formula was used for nearly half of Eurobond issues in the 1980s because it allowed Japanese-only discussions based on company documents written in Japanese and shortened the duration of due diligence and documentation meetings to about three days.

However, at that time, it was deemed important for representatives of issuing companies to visit Europe as part of a “road show” and to attend signing ceremonies. Bonds were governed by British law. Thus, it was convenient to ask British law firms engaged in bond-related documentation work to be responsible for signing and closing procedures. At this juncture, the former Linklaters & Paines (currently known as Linklaters) adopted a flexible approach to this collaborative work, coining the term “split law issue,” while Slaughter & May rejected a collaborative approach. Slaughter & May subsequently had to shut down its office in Japan.

Because the split law approach entailed the overlapping of some work and was wasteful in that sense, Japanese laws were subsequently adopted as the governing laws of bonds by issuers of good standing that could resort to the fiscal agent method. The former Hamada & Matsumoto law firm established a London office in 1987 partly because all procedures from signing to closing had to be conducted in London and the help of British law firms could not be enlisted as the entire process was governed by Japanese law (for details, see Section 7).

The London office was shut down in 1994 because of the collapse of Japanese firms’ Euro equity-linked bonds with the collapse of the bubble economy. But the final blow came when the Ministry of Justice announced the “mandatory designation of a commissioned company for a Euroyen bond” in the wake of the revision of the Commercial Code in 1993.

The Japanese office of Linklaters subsequently hired foreign lawyers and paralegals who could speak Japanese, and is now well positioned to handle Euroyen bond issuance work with an efficiency matching that of Japanese law firms. In April 2005, when foreign law firms were allowed to employ Japanese lawyers and form partnerships with

Japanese law firms in the last step toward the full opening of Japan’s legal service market, Linklaters formed a partnership with the Yasuda group of the former Mitsui & Yasuda law firm and now commands a near-monopoly on legal practice related to the underwriting of Euro equity-linked bonds governed by British law issued by Japanese companies.

While magnanimous, Linklaters, backed with British history and tradition, is a law firm able to expand its business by assimilating itself in local markets. Though it is a formidable competitor, this author pays the firm due respect.

As indicated above, however, it is unfortunate that the present stance of the Ministry of Justice is preventing Japanese law firms from engaging in fair and free competition with Linklaters and other foreign firms in the Eurobond market.

The discussion above may be summarised in table form as follows:

Underwriting government law	British law	Japanese law
Bond governing law		
British law	Post-war — Present	The early 1980s — Collapse of the bubble (1991) (Almost half of issuance)
Japanese law	Pre-war	The latter half of the 1980s — 1993 revision of the Commercial Code (A few cases)

The “manufacture” of “Made-in-Japan” Eurobonds by Japanese companies is being conducted (on an OEM basis) with the assistance of British lawyers (i.e., is governed by British law) rather than in Japan (governed by Japanese law). Japan is the only industrialised nation in this type of situation. This is an important point that should have been settled in the official interpretation or the revision of the Corporate Law. (See subsequent Sections 8 and 9)

7. Japanese Law Firms have not “Inherited” Eurobond Underwriting DNA

The collapse of the bubble economy led to a sharp decline in the issuance of Euro equity-linked bonds by Japanese firms under the slump of the Japanese equity market. Of the four major securities companies that were the main players in Euromarket finance through their London subsidiaries, Yamaichi Securities Co. failed in 1997 and the three other firms suffered from *sokaiya* (underground shareholders) payoffs and other scandals as well as the stock market slump. Only Nomura Securities Co. remains independent; the underwriting divisions of Daiwa Securities Co. and Nikko Securities Co. were merged with Sumitomo Mitsui Bank and Citibank, respectively.

Prior to the collapse of the bubble economy, three of the four securities firms that almost monopolised the underwriting of Euro equity-linked bond issues by Japanese companies (other than Nomura) adopted Japanese laws as the governing laws for underwriting contracts for which they acted as lead managers. As was mentioned above, Japanese law firms acted as counsel for the underwriting side enabling due diligence

and documentation meetings to be efficiently conducted in Japanese. The split law approach was employed for nearly half of all Euro equity-linked bonds that were issued. The former firms Hamada & Matsumoto, Aoki & Christiansen, Tomotsune & Kimura and Mitsui & Yasuda, mentioned earlier as Japanese law firms that served on behalf of Japanese issuers prior to 1980, moved to the side of the underwriters and led due diligence and documentation meetings as well as preparing offering circulars. In the case of the split law approach (in which bonds are governed by British laws and underwriting contracts are governed by Japanese laws), not only underwriting contracts but also underwriting group contracts and selling group contracts were governed by Japanese laws. Not limited to these, further documents were required, from invitation telexes to signing memoranda and closing memoranda. Knowledge of Euromarket practices was essential.

As the presence of purely Japanese securities companies declined, issuance of Euroyen bonds governed by Japanese laws dwindled, as indicated above. Because the split law approach was inefficient due to the engagement of both British and Japanese law firms, and since Linklaters and other foreign law firms hired Japanese staff to enhance their capacity to conduct due diligence and documentation meetings in Japanese (by forming partnerships with Japanese lawyers after the legal service market was completely liberalised in April 2005), both underwriting contracts and bonds reverted to being governed exclusively by British laws. Since the 1993 revision of the Commercial Code, no Japanese law firm has served as the sole legal counsel for underwriters of Euro equity-linked bonds. During the last 15 years, Japanese law firms have not inherited the “DNA” for Eurobonds and Euro equity-linked bonds.

8. Corporate Law Subcommittee Discussion on Bond Governing Laws

The issue was addressed at the 26th and 27th meetings of the Corporate Law Subcommittee.

According to document No. 28, distributed at the 26th meeting of the Corporate Law Subcommittee, a practical, to-the-point question appears to have been posed: “Should it be understood that provisions concerning commissioned companies and meetings of bondholders are not applicable when a domestic company issues corporate bonds overseas?” However, subsequent discussions on the matter became confused, with statements such as the following being made: ① “at present, commissioned companies have, in practical terms, not been used for foreign bonds,” and ② “for global offerings, in which a single bond is placed in two or more countries, it is impractical to make distinctions on the basis of the engagement or non-engagement of commissioned companies or bondholder meetings.” Based on these discussions, the conclusion was drawn that “at the present time, it is difficult to provide legislation that covers all these issues, and therefore it would seem most prudent not to set anything firmly in law.” However, it seems to this author that the above discussions overlook the following facts. First, concerning ①, as a result of the Ministry of Justice’s official interpretation that the 1993 revision of the Commercial Code calls for the mandatory engagement of a commissioned company for any foreign bond placement⁴, Eurobonds that were issued, albeit in only a small number of cases, with Japanese law as the governing law prior to this legal interpretation⁵ ceased being issued entirely, and no commissioned companies have been engaged since then because all Eurobonds are now governed by British laws. Second, concerning ②, global offering is a method used in public offerings of stocks

and is not used for bonds because of differences in practice. While bonds are issued in the U.S. market in a registered form, they are issued in the Euromarket in a bearer form.

Further, document No. 25, distributed at the 25th meeting, contained a suggestion that “provisions for commissioned companies and meetings of bondholders should be made applicable to corporate bonds issued by foreign companies in the Japanese market.” But this suggestion appears to overlook the fact that a Japanese court has already approved the application of those provisions to such bonds⁶.

As things stand now, even young lawyers who have studied abroad believe that “All Eurobonds are governed by British laws” and have little knowledge of the distinction between governing laws for underwriting contracts and governing laws for bonds. Indeed, we cannot accuse Ministry of Justice officials involved in the preparation and enactment of the Corporate Law of being not fully aware of the new law’s potential impact on legal practices. It can be assumed that these officials were simply too busy or too preoccupied with the comprehensive overhaul of the Corporate Law to be aware of the issue. The minutes from the Legislative Council’s discussions show that panel members simply ran out of time. The minutes also indicated no trace of discussion concerning the potential impact on legal practices of the extraterritorial application of the provisions for the mandatory engagement of commissioned companies.

9. Requests for Substantive Enactment

The system of engaging commissioned companies for bonds (the system is the same as that under the 1993 revised law except for the change in name from “*kanri kaisha*” to “*kanrinin*” (administrator); “commissioned company” is used in English, as it is in the case of samurai bonds) may be a well-designed scheme, even by international standards. The use of commissioned companies enables an excellent balance between the interests of issuers and the interests of investors.

However, in the case of Eurobonds, as is shown by the migration of samurai bond issues to the Euromarket from the samurai market (in which conventional market practices require the engagement of commissioned companies) as mentioned in Section 2, issue cost considerations are important and bondholders’ meetings that only assume only Japanese resident investors and the involvement of Japanese courts are not acceptable in foreign markets. However well designed, a system or institution is meaningless if it cannot be put to practical use.

The fiscal agent approach and the lack of involvement of courts in bondholder meetings are standard in the Euromarket. They are considered to be necessary and sufficient conditions for issuers, who are not required to put up collateral. Even with domestic bond issues under the existing Commercial Code, it is market practice to use fiscal agents for bonds with a par value of ¥100 million or more that are exempt from the requirement to engage commissioned companies.

However, as pointed out in Section 6, as long as the Ministry of Justice’s official interpretation stands, which states that it is mandatory to engage commissioned companies for all foreign bonds governed by Japanese law, all Eurobonds issued by Japanese issuers will be governed by British laws, in line with the fundamental rule of legal practice, that legal risks that need not be taken should not be taken. Clearly, if such official interpretation is not changed, legislative solutions are called for⁷. This has been explicitly indicated by public comments by the Japan Capital Markets Association and others.

Under the 1993 revision of the Commercial Code, in terms of legal practices, Japan became the only industrialised nation whose companies cannot issue Eurobonds governed by domestic laws. In other words, all Eurobonds issued by Japanese issuers are governed by British laws and are handled exclusively by British law firms. The legal costs they impose are based on a monopoly, and these costs are affecting Japanese industry. The decade since the revision of the 1993 Commercial Code has been a lost decade for Japanese issuers and law firms.

10. The ABMI Roadmap and Asian Bond Standards

While the Asian Bond Markets scheme is rapidly shifting from the research stage to a practical phase, media coverage has been inadequate, and the private sector seems as yet not to fully appreciate its importance.

The Asian Bond Markets Initiative (ABMI), the origin of which may be traced to the Chiang Mai Initiative in the wake of the Asian currency crisis, was officially endorsed by the ASEAN+3 (China, South Korea and Japan) Finance Ministers' Meeting held in Manila on August 7, 2003. Since then, six formal working groups have been formed with several member countries responsible for each area and the ABMI has recently been making concrete progress at a rapid pace.

(1) ABMI Roadmap

At its meeting in Tokyo in November 2004 the Focal Group proposed the concept of the ABMI Roadmap as the framework for the ABMI. Under the Roadmap, the Focal Group will inherit the results achieved so far, will integrate information and will take the lead in working towards practical implementation, by, for example, conducting an in-depth study on the "Asian Bond Standards" discussed below, which will potentially have an impact on other issues, and taking the Asian Bond Website (<http://asianbondsonline.adb.org>) established by Working Group #5 (Singapore and Japan), which is used for sharing information and exchanging views, under its direct control. The Focal Group meets twice a year.

(2) Asian Bond Standards

South Korea has proposed "Asian Bond Standards," which were addressed in the Istanbul agreement of May 4, 2005.

In these standards, bonds are classified into three categories:

- (i) Domestic bonds
- (ii) Bonds issued by a country in the region ("samurai bonds")
- (iii) Bonds not registered in a country in the region ("Eurobonds")

While recognizing the importance of all three categories of bonds, the ABMI only names bonds in category (iii) "Asian Bonds." (they are so called because "Eurobonds" may be confused with euro-denominated bonds)

The market for Asian bonds is considered to be the market countries in the region should cooperate in developing.

The purpose of developing a bond market in which East Asian countries can issue bonds without relying on investors in Europe or the United States is to mobilise regional savings within East Asia.

The ABMI Roadmap calls for the initial stage of issuance on a contract basis, the establishment of self-regulatory organisations like the International Primary Market

Association (IPMA) and the International Securities Market Association (ISMA), as well as the creation of central depository organisations for real-time clearance of Asian Bonds, similar to Euroclear and Clearstream.

The ABMI has made it clear that its intention is not to create Asian bond markets separate from the Eurobond market that are exclusively for Asian investors and issuers.

Despite this denial of the creation of exclusive markets, the ABMI is apparently seeking to develop “Asian bond standards” for the following reasons:

(i) The so-called Euromarket now appears to be in transition from a free market to a regulated market. With the introduction of the Prospectus Directive and the Transparency Directive by EU member countries, their self-regulated markets are now coming under EU-wide official regulations. In addition, with regard to accounting rules, the use of International Accounting Standards (IAS) is being imposed. Under these circumstances, East Asian countries that have been using the Eurobond market to date now see practical merit in developing an Asian bond market as a new Euromarket.

(ii) U.S. dollars held in European countries helped launch the Euro bond market; huge amounts of US dollars are currently held by East Asian countries.

(iii) The U.S. dollar and the euro are now the two key currencies. While it may be difficult for the Japanese yen or any other Asian currency to take up the role of a key currency anytime soon, the creation of a market for yen-denominated bonds, bonds denominated in other Asian currencies, or bonds denominated in a basket of East Asian currencies is possible (the Japanese proposal addressed by the above-mentioned Istanbul agreement provides an effective means of hedging exchange risks between Asian currencies and the key currencies, the additional printing of which Asian countries have absolutely no control over).

(iv) Even in an IT-driven era, physical distribution remains region-centered and thus it is only natural to form a regional economic bloc and develop a regional capital market with it.

What is interesting about the South Korean proposal is its realistic approach; while Asian Bonds are at first to be governed by British laws, the eventual goal is to issue Asian Bonds governed by the domestic laws of East Asian countries. This is an approach Japan has already had experience of with its participation in the Euromarket.

11. NIRA's Proposals Regarding the ABMI

As developments so far indicate, the ABMI cannot make much headway if it has to wait for the outcome of intergovernmental talks among East Asian countries for each step it takes. Likewise, the initiative cannot move ahead if it waits until East Asian countries develop their domestic institutions and infrastructure.

Therefore, the ABMI should initiate action beginning with bonds that are not registered in any country of the region (Asian Bonds=Eurobonds), category (iii) of the South Korean-proposed Asian Bond Standards. This means the launch of a free market for trading by private-sector professional investors exempt from local regulations in Asian countries to varying degrees. Issuers should include the Asian Development Bank and other international institutions, governments in the region, governmental agencies and multinational corporations that have an adequate level of disclosure and high credit ratings.

Such a bond market for professional investors, unlike the CB market, should be able to handle units of issuance (face value) in excess of ¥100 million. If so, under the

existing Japanese Commercial Code (as well as under the new Corporate Law), the less costly fiscal agency (FA) method can be adopted with corporate bonds governed by Japanese laws. The domestic placement of corporate bonds with a face value of ¥100 million by Mitsubishi Corp., which was devised to counter the mandatory engagement of commissioned companies under the 1993 revision of the Commercial Code but took advantage of exemptions under the same 1993 revision, is now serving as the model to be followed by all corporate bond issuers.

If Asian Bonds are settled through Euroclear or Clearstream and trading in them commences on the interdealer market, such a market can be inaugurated almost immediately under the current legal framework and at the initiative of the private sector alone.

(Keiji Matsumoto **)

¹ Asian Bonds Online HP <http://asianbondsonline.adb.org/regional/regional.php>

² Masaaki Kanayama, "Problems Involved in Public Offerings of Foreign Stocks," *Shoji Homu* (Business Law and Practice), No.611, 1972

³ Pre-war foreign bonds were governed by Japanese laws. Takeo Kurusu, "Studies on Foreign Bonds and the Foreign Corporate Bond Law," *Yuhikaku*, 1967

⁴ This interpretation was made repeatedly in Tetsu Aizawa, "Q & A: New Corporate Law," *Shoji Homu* (Business Law and Practice), July 25, 2005

⁵ Keiji Matsumoto, "Issuance on the Euromarket of Corporate Bonds Governed by Japanese Laws," *Kokusai Shoji Homu* (International Business Law and Practice), Vo.16 No.5, 1988

⁶ Keiji Matsumoto, "Legal practice of Commissioned Companies for Eurobonds (and Samurai Bonds) under the Commercial Code and the Asset Securitisation Law and the Collateralised Bond Trust Law" *Kokusai Shoji Homu* (International Business Law and Practice), Vo.32 No.2, 2004

⁷ Shuya Nomura, "The Corporate Bond System under the New Corporate Law," *Jurist*, No.1295, August 1-15, 2005

** Japanese attorney-at-law

10. Development of a Securities Clearing System in Japan by the Japan Securities Depository Center (JASDEC)

1. What is the Japan Securities Depository Center (JASDEC) ?

The Japan Securities Depository Center (“JASDEC” below; this term will also be used for the current Japan Securities Depository Center, Inc.) was established as a non-profit foundation on December 6, 1984 with the objective of streamlining the delivery of stock certificates.

On May 27, 1985, JASDEC was designated as a depository under the Central Securities Depository Law (1984 Law, No.30, “CSDL” below) by the Minister of Justice and the Minister of Finance and commenced depository services on October 9, 1991.

In the process of reforming the securities clearing system, there was growing debate on the corporatisation of JASDEC. Given the pressing need for the reform of the securities clearing system in Japan, it became essential to build a securities clearing system which is globally competitive and convenient for market users. Thus it became necessary to develop as soon as possible a securities clearing organisation to implement the securities clearing system, equipped with globally competitive capability.

There were also discussions along these lines at the Financial System Council of the then Ministry of Finance. In its report submitted in June 2000 entitled “The New Financial Framework for the 21st Century”, the Council indicated that “It is preferable that a securities clearing organisation which handles various types of securities should emerge”.

In addition, the Council proposed in the same report that it would be essential to establish a securities clearing organisation structured to “be constantly self-motivated to improve its own services in order to respond positively and flexibly to environmental changes”, and “for this to be realised, it would be critical to improve governance to appropriately reflect user opinions and to ensure contestability.” The Financial System Council also proposed that “the way JASDEC is managed should be reviewed from a broad perspective, including governance functions and organisational structure.”

In accordance with this proposal, the Committee for Reform of the Securities Clearing and Settlement System within the Japan Securities Dealers Association (JSDA) established a working group “to review the structure and management of JASDEC”, which discussed JASDEC’s governance and other operational functions, and the pros and cons of its corporatisation.

As a result of these discussions, a report was submitted in September 2000, which recognised the need for JASDEC’s corporatisation from the viewpoint of expandability and increased operational efficiency.

Upon its corporatisation, it was decided that JASDEC should be structured in a manner that ensures that its governance function reflects user opinions.

In the process of corporatising JASDEC, the aforementioned Advisory Board on Securities Delivery and Clearing Reform formed a special committee to review specific matters such as basic corporate philosophy and the amount of capital, and in November 2001, the committee submitted a report entitled “Specific Framework for Corporatisation of JASDEC.”

Corporatising JASDEC was judged to be a preferable approach to realising the

reform of the securities clearing system. The relevant authorities commenced the tasks required to change the CSD (Central Securities Depository) to enable JASDEC's corporatisation. The changes to the CSD were instituted in April 2002, officially making JASDEC a company with shares.

The process of corporatising JASDEC was not the same as that used in the case of the Tokyo Stock Exchange, the legal person (corporate) status of which remained the same when the legal entity as a legal person with members was restructured as a company with shares.

This is because the Japanese judicial system governing the legally incorporated foundations like JASDEC, which were public-interest corporations, differs significantly from the legal system governing business corporations, i.e., profit-making corporations.

And there is no system under existing legislation that allows public-interest corporations to restructure themselves to become another kind of legal entity such as profit-making corporations, while maintaining their legal person (corporate) status.

Thus, as a means of converting a public-interest corporation to a business corporation, the authorities adopted the method of transferring the operation of the incorporated foundation to the business corporation after its dissolution, in order to enable the practical corporatisation of the public corporation.

In terms of specific procedures, a new company to which depository services were transferred was established in January 2002, and through subsequent capital injection, the framework of the business corporation was laid out.

In June 2002, JASDEC became a business corporation after the authorities concerned approved the transfer of business.

In addition, the Law Concerning the Transfer of Short-term Bonds (CP: Commercial Papers) was put into force, which governs the issuance of electronic commercial papers. Because the depository organisation is required by law to be a business corporation, JASDEC had to become a business corporation in order to process electronic CPs.

On January 10, 2003, JASDEC was designated under the Law Concerning Book-Entry Transfer of Corporate Bonds, etc. (2001, No.75, termed Law on Bond Book-Entry Transfer below) as a depository agency, to handle various kinds of securities, and began to play a crucial role in the paperless issuance of bonds under the law.

The corporate policies of JASDEC, as a business corporation, are

- (1) to focus on users and pursue highly transparent management,
- (2) to provide functions equivalent to those of an overseas CSD, and
- (3) to provide extremely safe and less expensive services.

Given its public nature as a social infrastructure, many of JASDEC's directors are representatives of participating securities firms and banks, in order to ensure governance by participants.

An Operations Committee was formed to take opinions from business experts and make changes on their basis. Subcommittees were also formed for different projects, the proceedings of which are published on the JASDEC website.

2. JASDEC and the promotion of reform of the securities clearing system

In recent years, many countries have vigorously proceeded with reform of their

securities clearing systems in order to enhance their competitiveness in capital markets.

Japan is also engaged actively in the reform process, employing IT technologies and launching the DVP (Delivery Versus Payment = a clearing system to avoid outstanding balances) and STP (Straight Through Processing = electronic processing of trading through settlement).

(1) Establishment of short-term corporate bond (electronic CP) depository and clearing system

On January 10, 2003, JASDEC was designated a depository institution under the “Law Concerning Book-Entry Transfer of Corporate Bonds, etc.” and commenced operation on March 31.

Traditionally, commercial papers were in the form of paper notes and had to be delivered to the assignee for settlement in Japan since 1987.

Under the new JASDEC system, CP processing became paperless, completing the process of CP issuance, redemption, and transfer through the electronic paper book-entry system. Through this system, the settlement cycles can be shortened, potential risks pertaining to the delivery of printed securities are eliminated, and custodial costs are also abolished.

JASDEC’s short-term corporate bond depository and clearing system adopts the DVP clearing system, which handles individual securities and related capital in a set (also called gross=gross type, BIS 1 model). The DVP clearing system, which settles individual accounts on a real time basis, ensures the security of transactions and materialises the settlement of accounts, which satisfies issuer’s need for quick financing.

The limited type of the face value of CP notes was also harming distribution.

As stamp duty is imposed by individual paper note, the issuers tried to reduce the printing cost by issuing CP in a larger face value.

Electronic commercial papers avoid such constraints, enabling the issuance and transfer of CP in smaller values. And as a result electronic commercial papers creates flexibility in capital management and financing.

(2) Implementation of the general DVP clearing system

The DVP clearing system is essential to avoiding the principal risk (due to non-payment of price or non-receipt of securities notes).

In addition, coordinated operation between the DVP clearing system and the STP system is required for efficient DVP settlement.

In particular, there was a significant need for such settlement with institutional accounts.

The general DVP settlement system for stocks, etc. was commenced in May 2004 to launch the DVP clearing scheme for the settlement of shares for securities firms, trust banks targeted at institutional investors, and standing proxy (custodian) banks.

The securities gross type (=capital net type) DVP clearing system was introduced to this settlement system, linking the settlement order information for the clearing of securities such as stocks, via the pre-settlement matching system (PSMS) , which enabled efficient DVP settlement.

This DVP clearing system settles securities transactions by each settlement order, i.e., by the gross of individual transactions.

The JASDEC DVP Clearing Corporation (JDCC), a wholly owned subsidiary of JASDEC, undertakes clearing services as CCP (Central Counter-Party=clearing organisation to accept debts and credits for those concerned and settle the account) by taking collaterals from the DVP clearing parties and managing risks.

While the capital is settled in a net amount at the end of the day, as the DVP Clearing Corporation (JDCC) manages risk, DVP clearing with no principal risk is realised. DVP clearing parties are required to pledge a membership fund (cash) to DVP Clearing.

In terms of settlement of stocks, the Stock Exchange DVP Settlement System has been operating for Exchange Trading (stock exchange trading/DVP settlement was launched in the Tokyo Stock Exchange and the Osaka Securities Exchange in May 2001).

The Japan Securities Clearing Corporation has also implemented DVP as CCP since January 2003), but the DVP settlement for institutional investors has not been realised yet, nor is there an international standard.

The general DVP clearing system used as a model the DVP clearing system of the US's DTC, and it has raised the level of security and efficiency of Japanese stock settlement to a global standard.

3. Expansion of Pre-Settlement Matching System (PSMS)

The Pre-Settlement Matching System (PSMS) enables institutional investors, securities firms and trust banks to handle post transaction checking via electronic processing (eliminating the person-hours required to send FAXes or make calls).

JASDEC implemented the Pre-Settlement Matching System (PSMS) for domestic trades by domestic institutional investors in September 2001.

In February 2002, PSMS was expanded to cover trades by non-resident investors, public offering, placement, and trading of corporate bonds with share warrants (convertible bonds and corporate bonds with share warrants before the revision of the Trade Act on April 1, 2002).

In addition, in May 2003, PSMS was expanded to cover Japanese Government Bonds (JGB), futures/options and transmission of information on net asset value per share and information on price setting/termination from securities investment trust management companies to trust banks.

When the general DVP clearing system was launched in May 2004, the operational linkage with PSMS was materialised.

To further improve the level of services, PSMS commenced operation to handle JGB repo trading and commenced providing pre-settlement matching services for the newly established Japan Government Bond Clearing Corporation (JGBCC).

Since January 2006, PSMS has been connected to the depository and clearing system for short-term corporate bonds (CP) as well as for general bonds.

4. Implementation of depository and clearing system for general bonds (corporate bonds, investment-and-loan bonds, and local bonds)

Historically, in Japan the settlement of corporate bonds, investment-and-loan bonds, and local bonds was processed through the renewal of registration at about 160 registration agencies throughout the country. While the "Japan Bond Settlement

Network”, commonly called JB-Net, functioned to connect the registration agencies and market players, and the system to electronically process DVP settlements existed via a linkage with BOJ Net, there were still many physical invoice transactions issued in writing. Thus the overall depository and clearing system for general bonds was still inefficient and it remained difficult to increase its quality.

It was considered that a hierarchically structured depository and clearing system was required to enable efficient settlement. Efforts have therefore been made to enact related laws to enable reform of the securities clearing system in Japan.

In January 2003, the “Law Concerning Book-Entry Transfer of Corporate Bonds, etc.” went into effect to allow paperless settlement of general bonds.

In January 2006, JASDEC inaugurated its book-entry transfer system for Corporate Bonds, becoming the only clearing agency which processes book-entry transfers in Japan. As this system presupposes the application of STP in the DVP settlement, it led to a significant advance in the application of STP/DTP in securities settlement in Japan. The transition period for existing bonds issued as cash bonds and registered bonds ends in January 2008. The efficiency of corporate bond settlement should significantly improve when the transition is completed, and the liquidity of the Japanese corporate bond market is also expected to increase significantly.

5. Toward the establishment of a depository and clearing system for investment funds

The Law Concerning Book-Entry Transfer of Corporate Bonds, etc. is the legal framework to advance a paperless depository and clearing system related to the beneficiary rights of investment funds, as in the case of short-term corporate bonds and general bonds, but it is different in that the places of short-term corporate bonds and general bonds, the focus on origination and termination.

JASDEC set up a Trust Fund Subcommittee to provide the foundation for paperless processing in origination/pricing, transfer, and termination/redemption of trust funds. After intensive discussions, the subcommittee published an outline of the system in September 2004. With the efforts made by concerned parties, the JASDEC trust fund depository and clearing system commenced operation in January 2007.

6. Paperless processing of stock certificates (computerised processing of stock certificates)

Paperless processing of stock certificates is the final goal of computerising processing of securities instruments. The computerised processing of stock certificates was the last procedure to be initiated in the gradual transition to computerisation because intensive study of its effects was required.

This is because stock trading emphasises investor rights (right to self-interest and right to common interest) such as dividends and voting rights, and these rights of stock owners are registered on a stockholder list. In addition, there are many stockholders, the majority of whom are keeping their stock certificates on hand.

JASDEC has been providing depository services as a depository center for stock certificates since 1991. At present, about 75% of issued shares of listed companies are deposited with JASDEC. In terms of the settlement of the shares listed at stock exchanges between securities firms, JASDEC facilitates deposit of securities without

any physical delivery of securities. In a similar manner, transactions by institutional investors and non-residents are processed by securities firms (brokers and dealers) and custodian banks in most cases through JASDEC's depository and clearing system without any physical delivery of securities.

In this sense, while computerisation of securities trading had in fact been broadly implemented, there was a limit to the extent that administrative costs required for depositing and transferring share certificates or the cost on issuers was reduced, since there were a relatively large number of actual stock certificates.

The Legislative Council of the Ministry of Justice proposed in 2003 to introduce a system which promoted computerisation, and in the following year the Financial Services Agency and the Ministry of Justice submitted a proposal for the revision of the Law Concerning Book-Entry, Transfer of Corporate Bonds, etc. and the Commercial Law to the Diet, which passed the revisions.

Before the listed companies and market players actually adopt this system, administrative procedures, market practices, and computer system design need to be considered.

Furthermore, it is essential to familiarise investors (stock holders) with the new paper-less system and raise the ratio of the pre-depository of the paper based stock certificates with JASDEC in order to ensure a smooth transition. The computerisation of stock certificate processing is scheduled to be realised in 2009.

7. Summary

The reform of the securities clearing and settlement system in Japan has made significant progress through the establishment of clearing agencies and the realisation of cross-sectoral computerisation of securities processing, which have advanced institutional reforms. As a result of efforts made by the business sector, including JASDEC, the implementation phase may be in the final stage.

While at present there is some cost in terms of system investment in developing the securities clearing system, it is desirable that not only market players but also investors and issuers enjoy the benefits of computerisation through the improvement of user convenience and cost reductions via the realisation of STP, DVP, and paperless processing.

In order to achieve this goal, both JASDEC and market players should set up a specific goal to improve the efficiency of the securities clearing system and to raise Japan's global competitiveness.

JASDEC's basic corporate philosophy (established in June 2006) is that it "recognises its public role as the only securities depository center in Japan, and the continuous changes in both the domestic and the international environment and investment structures surrounding the capital market, while, from the viewpoint of both investors and users, JASDEC contributes to the development of society and the functions of the securities market, as a leader of the reform in the securities clearing and settlement system aimed at building highly credible, convenient and efficient securities clearing infrastructure." It is essential for market players (=JASDEC sponsors) to share this concept and cooperate with each other to improve the level of capital market infrastructures in Japan as well as in the Asian region, under a national strategy.

(NIRA Secretariat)

Appendix

June 19, 2007

The Charter of the Capital Markets Association for Asia (CMAA)

(Revised on July 11, 2007 / September 06, 2007 / December 06, 2007 / February 28, 2008)

1. Background to the Establishment of the Capital Markets Association for Asia (CMAA)

Following on from the publication of a report by the Study Group on the Internationalization of Japan's Financial and Capital Markets (Ministry of Finance) in March 2003, a forum entitled "Keio-NIRA Asian Capital Markets Study Forum" was held on October 18 and 19, 2003 at Keio University in Tokyo under the joint auspices of the Center of Excellence (COE), Keio University (headed by Professor Naoyuki Yoshino), and the National Institute for Research Advancement (NIRA; Former Chairman: Mr. Yotaro Kobayashi, Chief Corporate Advisor of Fuji Xerox Co., Ltd.), a think tank under the supervision of the Cabinet Office.

A total of 60 participants from six Asian countries joined the forum, including officials from the finance departments of leading issuing companies in bond and capital markets, institutional investors, working-level managers of Japanese and foreign banks and securities firms, and representatives of regulatory authorities, securities depository organisations, rating agencies, law firms, research institutes and the press.

The presentation of research papers in English by a total of 20 researchers, ten from Japan and ten from other Asian countries, was followed by intensive discussions.

The establishment of the Asian Capital Markets Study Group was also announced at the forum. The Study Group, a voluntary association of regional private-sector companies and financial institutions, was formed to enable the opinions of market participants to be reflected in the Asian Bond Market Initiative being promoted by the Association of Southeast Asian Nations (ASEAN), Japan, China and South Korea.

(Minutes) <http://www.nira.go.jp/newsj/kanren/150/157/index.html>

Following this, in accordance with the concept of the foundation of the Asian Capital Market Study Group, studies on the establishment of international bond markets in the Asian region were conducted by NIRA and other relevant organisations.

On March 27, 2006, a joint NIRA-ADB forum was held in Tokyo, at which the results of studies conducted by NIRA were presented to participants as a NIRA policy proposal (interim report).

The atmosphere of the forum, encompassing the presentation of the proposal, panel discussions, and exchanges of opinions between participants, was positive and energetic.

At the conclusion of the forum, a questionnaire survey on the draft proposal prepared by the NIRA study team was conducted, and the proposal was endorsed by approximately three-quarters of participants.

(Minutes) <http://www.nira.go.jp/newsj/kanren/170/178/index.html>

On May 15, 2006, NIRA announced the "Proposal for the Establishment of an Asian Inter-Regional Bond (Asian Bond) Market -- A Road Map to an Asian Inter-Regional Bond Primary Market." (In addition to Japanese and South Korean joint researchers, the study group that prepared the proposal was participated in by numerous scholars, market practitioners, and observers).

(Proposal)

Japanese <http://www.nira.go.jp/newsj/kanren/170/179/index.html>

English <http://www.nira.go.jp/newsj/kanren/170/179/proposal.pdf>

The results of NIRA's research have been published by LexisNexis as a book entitled *Ajia Ikinai Kokusai Sai Shijyo Sosetsu Koso – Ajiabondo Shijyo e no Rodo mappu* ("Vision for the Establishment of an Asian Inter-Regional Bond Market – A Road Map to an Asian Bond Market") (written and edited by Shigehito Inukai, representative of the NIRA study team).

http://www.nira.go.jp/pubj/shinkan/s200703/s200703_2.html
http://www.yushodo.co.jp/press/ln_asian_intl/index.html

The aim of NIRA's May 2006 proposal, mentioned above, was as follows:

(1) to foster financial market personnel in the Asian region;
(2) to establish a forum for the generation of market innovations; and
(3) to create and foster regional financial and capital markets, including an Asian inter-regional capital market, a self-contained market enabling savings accumulated in the region to circulate within the region.

At this time, NIRA also proposed the establishment of the Capital Markets Association for Asia (CMAA) in order to facilitate financial and capital market transactions by market participants, including Asian companies as the principal users of the market, by establishing and fostering financial and capital markets in the Asian region.

To enable these goals to be achieved, the Capital Markets Association for Asia (CMAA) was established as a voluntary association by NIRA study team members and others on June 19, 2007. Mr. Nobuyuki Idei, Founder & CEO of Quantum Leaps Corporation (former Chairman of Sony Corporation) is Chairman of the CMAA, and Mr. Keiji Matsumoto, one of the founders of the legal office "Hamada and Matsumoto (Current Name: Mori, Hamada and Matsumoto)," is the Association's Vice Chairman.

2. The Purpose of the Capital Markets Association for Asia (CMAA)

- (1) Formulation of self-governing rules for issuing entities and other users of the regional financial and capital markets
- (2) Coordination of opinions of issuing entities and other users of the capital markets as well as institutional investors, intermediaries and other market participants regarding legal systems and rules related to the capital markets in the Asian region, including Japan
- (3) Engaging in efforts to reach out to all relevant quarters so that the accumulated results of exchanges of opinion, discussions and research by CMAA participants will be put into practice, including the presentation of results in the form of proposals.
- (4) Conducting research, formulating proposals, spreading information and conducting activities to increase awareness concerning the establishment and creation of legal structures, rules, practices and other market infrastructure for the Asian Inter-regional Professional Securities Market (AIR-PSM), an important constituent element of capital markets in the Asian region.
- (5) Research concerning the fostering of financial personnel and financial education for Asian financial capital markets and the presentation of proposals.
- (6) The ultimate purpose of the CMAA is, through the above activities, to increase the reliability and convenience of all financial and capital markets in the Asian region and to establish appealing markets for all users.

3. About the CMAA

- (1) Name: Capital Markets Association for Asia (CMAA)
- (2) Status of Study Group: A voluntary organisation bringing together participants who agree with the purpose of establishment of the CMAA. Basically, members join in an individual capacity, but corporate entities are not prevented from joining.
- (3) Membership fee: No membership fees
- (4) Admission to the Association: Admission of new members is decided by the Chairman or Vice Chairman based on the recommendation of several existing members.
- (5) Framework for activities: At present, Mr. Shigehito Inukai (Director of Policy Study and Senior Fellow, NIRA), Secretary-General of the CMAA, and Mr. Masaaki Uchiyama (President & CEO, TradeWin Co., Ltd.), Secretary of the CMAA, are acting as liaison for the CMAA.
The CMAA holds a regular meeting once a month (normally on the first Thursday of the month, from 6:30 p.m.) at NIRA or at venues provided by members of the Association. Individual Working Group meetings are held as necessary.
- (6) Inauguration: The inauguration of the CMAA was officially announced at the "General

Meeting for the Establishment of the Capital Markets Association for Asia” held on June 19, 2007, from 15:30-17:30, in TradeWin’s Conference Room.

4. CMAA’s Areas of Research (Working Group)

We establish the following working groups within the CMAA. Deliberations will commence from the areas of greatest interest and concern to participants.

Following their establishment, the working groups will commence discussions towards the formulation of proposals and recommendations in their respective areas.

We expect some of these working groups to present their first set of recommendations by the end of March 2008, to coincide with the publication of the Road Map.

- | |
|--|
| (1) Working Group on Market Practices, Legal and Documentation (New Issue Practices, Market-making Rules, Syndication Rules, Disclosure, Governing Law and Underwriting Contracts) |
| (2) Working Group on Market Systems Infrastructure, Clearing and Settlement |

With respect to market rules, we will refer to the Recommendation of the IPMA (now the ICMA) in considering details.

5. Structure of CMAA (as of February 28, 2008)

(©Founding members) (Officials: 13; Members: 22)

◎ Chairman	Nobuyuki Idei	CEO of Quantum Leaps Corporation
◎ Vice Chairman	Keiji Matsumoto	Lawyer, Matsumoto Law Office
◎ Secretary-General and Executive President	Shigehito Inukai	Director of Policy Study and Senior Fellow, NIRA Visiting Professor, Waseda University

Officials (in random order)

◎ Satoshi Yoshida	General Manager, IT Planning Department, Daiwa Securities SMBC Co., Ltd.
◎ Hirohiko Suzuki	Director, Investment Banking Division, Barclays Capital Japan Limited
◎ Masaaki Uchiyama	President & CEO, TradeWin Co., Ltd.
◎ Mamoru Fujimoto	Managing Director, TradeWin Co., Ltd.
◎ Ryoji Sato	Senior Administrative Officer, General Manager of President’s Office, Legal Department and Risk Control Department, Hitachi Capital Corp.
◎ Masaharu Murakami	Senior Manager, Planning Section, Payment Solutions Sector, NTT DATA Corporation
◎ Toru Yoshimi	Vice President, Commercial Division, SWIFT Japan
◎ Nobusuke Tamaki	Executive Director, Treasury Department, Deposit Insurance Corporation of Japan
◎ Kazuyuki Hirai	Director, Quality Management Department, Chuo Mitsui Information Technology Co., Ltd.
◎ Kenichi Maeda	Senior Manager, Global Planning Dept., Global Markets Planning Division, Mitsubishi UFJ Securities Co., Ltd.

Members (in random order, limited to official members of the Association)

◎ Yasuhiro Harada	Chairman & CO-CEO, Rating and Investment Information Inc. (R&I)
◎ Keiichiro Hashimoto	CEO, Fitch Ratings Ltd.
◎ Masahito Miyachi	Senior Advisor, Office of Regional Economic Integration, Asian Development Bank (ADB)
◎ Mineo Yato	Director, Investment Banking Division, Nikko Citigroup Limited
◎ Katsunori Kudo	Senior Advisor for Capital Markets, Nomura Securities Co., Ltd.
◎ Tsuyoshi Ando	Senior General Manager, Capital Markets Group, Global Investment Banking Groups, Mizuho Securities Co., Ltd.
◎ Ryu Mishima	Director, Head of Origination II, Global Capital Markets, Deutsche Securities Inc.
◎ Yusuke Masuda	Director, Japan Asia Holdings Limited
◎ Yasumasa Nakayama	Syndication, Fixed Income, Morgan Stanley Japan Securities Co., Ltd.
◎ Choi, Hosang	Economist/Senior Vice President, FSB Research Center, Shinhan Bank
◎ Naoko Morizane	Manager, Marketing New Financial Systems Business Planning Division, NEC Corporation
◎ Takayuki Nakamura	General Manager, Financial Planning Office and Investor Relations Office, Management Planning Division, REICOF Co., Ltd.
◎ Hironao Fukushim	Deputy Head, Investment Banking Headquarters, ORIX Corporation

◎	Shupu Jiang	Finance & Treasury Dept., Komatsu Ltd.
◎	Katsunobu Katayama	Group Vice President, Risk Management Group, Toyota Financial Services Corporation
◎	Ittetsu Mori	Manager, International Finance Section, Corporate Finance Division, Mitsubishi Electric Corporation
◎	Takayuki Aoi	Treasury Department, Finance Division, Fujitsu Limited
◎	Takaki Nakano	Finance & Accounting Office, Sumitomo Chemical Co., Ltd.
◎	Tomohiko Koga	Manager, Commercial Property Investment Planning Department, Mitsubishi Estate Co., Ltd.
	Katsumasa Suzuki	Lawyer, Mori, Hamada and Matsumoto
	Joanne O'Callaghan	Head of Communications Asia Pacific, SWIFT Hong Kong
	Akihiro Era	Senior Advisor, Brown Brothers Harriman Investment Service

Liaison Official in charge of Korean members concerned

◎	Hyun Suk	Bond Market Specialist in Charge of ABMI Task Force, International Finance Department I, Japan Bank for International Cooperation (former Visiting Researcher, NIRA)
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Observer Members

Toshiro Nishizawa	Deputy Director General, JBIC Institute, Japan Bank for International Cooperation (Senior Economist, International Finance Group)
Seigo Baba	Deputy Director, Division II, International Finance Department I, Task Leader, ABMA Task Force, Japan Bank for International Cooperation
Tsutomu Kawasaki	Chief Fund Manager, Pension Fund Association
Hiroshi Tsunoda	Director, Securities Sector Committee, International Bankers Association (IBA)
Rene Karsenti	Executive President, ICMA (International Capital Market Association)
Masaki Deguchi	Secretary of Corporate Finance and Treasury Association of Japan (CFTAJ) and Japan Capital Markets Association (JCMA)

Advisors

Hideki Kanda	Professor of Law, Graduate School of Law and Politics, University of Tokyo
Kazuaki Sono	Professor Emeritus, Hokkaido University and Tezukayama University
Tatsuo Uemura	Dean of the Faculty of Law and the School of Law, Waseda University, and Director, 21st Century Center of Excellence, Waseda Institute for Corporation Law and Society
Tony Grundy	Joint Managing Partner, Tokyo, Gaikokuho Kyodo-Jigyo Horitsu Jimusho Linklaters (Linklaters Tokyo)

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Editor of this Report

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Shigehito Inukai

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2000-Present	Senior Professional (General Manager), Mitsubishi Corporation
1987-1994	Executive Director, Mitsubishi Corporation Finance PLC, London
1975	Joined Mitsubishi Corporation

(Education):

2002	Completed Advanced Management Program (AMP), Harvard Business School (HBS)
1975	B.A., Political Science, Keio University

(Research Interests):

Policy related to financial and capital market systems, financial ADR, corporate finance, and cash management

(Major Publications):

As co-author:

- S. Inukai, *Grand Design for an Asian Inter-Regional Professional Securities Market (AIR-PSM)*, LexisNexis, 2008 (in English)
- T. Uemura / H. Kanda / S. Inukai, *Grand Design for Financial Services and Markets Legislation*, Toyo Keizai, 2007 (in Japanese)
- S. Inukai / K. Tanaka, *Towards a Japanese Financial Ombudsman System*, LexisNexis, 2007 (in Japanese)
- S. Inukai, *Initiative for the Establishment of an Asian Inter-Regional Bond Market*, LexisNexis, 2007 (in Japanese)
- N. Yoshino / N. Tamaki / S. Inukai, *Enhancing Market Functions in Japan*, Keio Press, 2006 (in English)
- S. Inukai, et al, *Electronic Commercial Paper*, Toyo Keizai, 2004 (in Japanese)
- S. Inukai, et al, *Global Standards and Liquidity Management*, Ric Telecom, 2000 (in Japanese)

As editor and author (NIRA publications):

- Proposal for Strategic Local Government Bond Market Reforms*, NIRA, 2006 (in Japanese)
- Grand Design for the Financial Services & Market Act in Japan (NIRA Market Governance Report 2005 1/2/3)*, NIRA, 2005 (in Japanese)

(NIRA Projects):

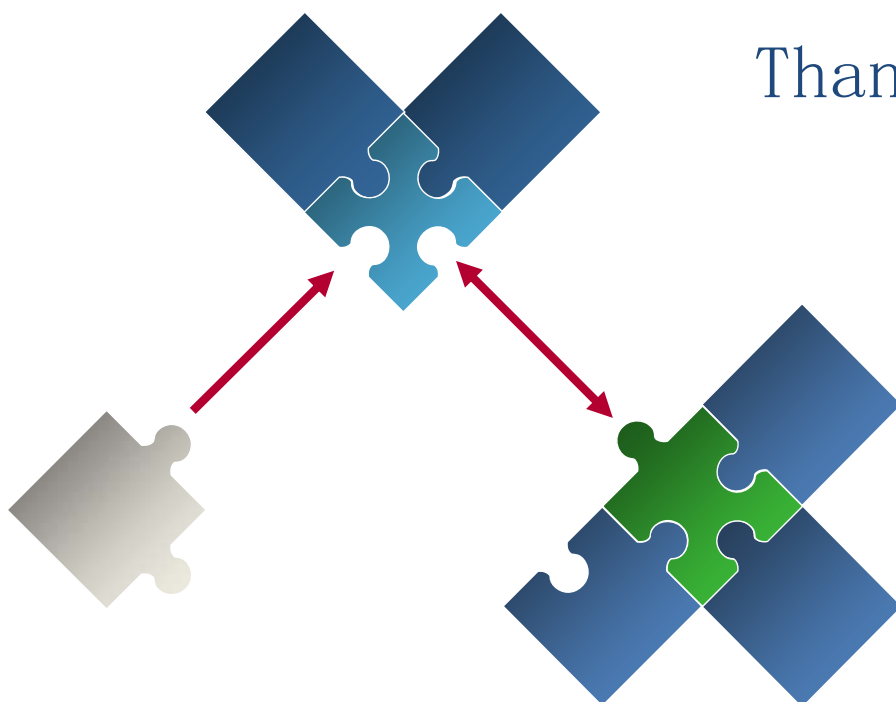
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(31st March, 2008)

Thank You



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