

Further Reforms of the JGB Market for the Promotion of Regional Bond Markets

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Gaisai Bond Issues

Unit: ¥ trillion

<u>Year</u>	<u>Number of Issues</u>	<u>Samurai Bonds</u>	<u>Number of Issues</u>	<u>Shogun Bonds</u>
1991	27	0.71	1	0.41
1992	37	1.57	0	0
1993	49	1.23	1	0.59
1994	60	1.26	0	0
1995	85	2.11	0	0
1996	154	3.79	0	0
1997	66	1.58	0	0
1998	10	0.15	0	0
1999	24	0.87	0	0
2000	63	2.38	0	0

New Miyazawa Initiative

Three measures under the NMI are related to regional bond market activities

- a. Acquisition of sovereign bonds by Japan Bank for International Cooperation**
- b. Use of credit guarantee and/or interest subsidies**
- c. Establishment of international guarantee institution**

Size of Government Bond Markets

Outstanding Government Securities (as of December 2000)

Hong Kong: \$13.94 billion

Singapore: \$24.97 billion

Australia: \$40.33 billion (as of March 2001)

US: \$2,966.9 billion

Japan: \$3,176.7 billion

Why the Tokyo Market Did not Capitalize on the NMI?

- Without joint effort by the region's economies, Japan alone cannot create a truly a regional bond market
- The Japanese government bond (JGB) market suffers from its own weaknesses

Government Bond Markets

	<u>Japan</u>	<u>United States</u>	<u>United Kingdom</u>
Turnover Ratio	6.9	22.0	7.0
Bid-Ask Spread (10-Year Bond)	7.0	3.1	4.0
Maturity Distribution			
< 1 Year	5%	21%	7%
1-5 Year	8%	62%	29%
5-10 Year	78%	0%	34%
>10 Year	9%	17%	30%
Average Issue Size (\$Billion)	8.2	13.9	5.6
Government Holding (%)	46.3	13.1	3.6
Non-Resident Holding (%)	10.0	36.9	14.4
Settlement	T+3	T+1	T+1
DVP-Basis Settlement	<ul style="list-style-type: none"> • 68% of registered JGBs and 43% of book-entry JGBs • All JGBs through BOJ-NET 	100%	100%
No. of Primary Dealers	None	37	16

Sources of Structural Problems?

Dual Role Played by MOF: Negative Consequences

A. Primary Market:

The lack of intense competition

B. Secondary Market:

Additional uncertainty on long term interest rates

Further Reform Measures: The JGB Market

- **Creation of the primary dealer system**
- **Adoption of the uniform-price auction method**
- **Introduction of when-issued trading**
- **Revamping the REPO market**

Creation of the Primary Dealer System

- Existence of primary dealers does not necessarily guarantee intense competition on the primary market but they are experts in pricing, market making, and distribution
- No primary dealer system: Japan and Germany
- Syndicated underwriting: Past norm
- Public auction systems are now used for:
2-, 4-, 6-, and 20-year bonds

Auction Methods: Government-Issued Securities

	<u>Japan</u>	<u>United States</u>	<u>United Kingdom</u>
Uniform-Price Auction	None	All Treasury Securities	<ul style="list-style-type: none">• Index-linked Bonds
Multiple-Price Auction	All JGBs <ul style="list-style-type: none">• 20-Year Bond: Competitive Auction Only• 2-, 4- and 6-Year Bond: Both Competitive and Non-competitive Auction• 5- and 10-Year Bond: Syndicated Underwriting	None	<ul style="list-style-type: none">• All Securities other than Index-linked Bonds

Introduction of When-Issued Trading

- Most advanced markets allow trading during the period between the time a new issue is announced and the time it is actually issued.
 - ◆ Ranging from one week to two-weeks (US market)
 - ◆ As short as two days (France)
- When-issued trading functions like trading in a forward market.
- Major Benefits
 - ◆ Minimize price and quantity uncertainties.
 - ◆ Lower underwriting risk
 - ◆ Increase revenue from the new issue
- By not allowing when-issued trading in Japan, the MOF foregoes these benefits.

Revamping of the REPO Market

Traditional Gensaki Market

- **European-style REPO (sell-and-buy-back)**
- **Ownership to the security is transferred to the buyer**
- **No marking-to-market**
- **Major instruments: Short-term Treasury and financing bills**

American-Style REPO market

- **Borrow and Lend**
- **No transfer of security ownership**
- **Marking-to-market**
- **Major instruments: All Treasury and corporate securities**

Creation of Regional Bond Markets (I)

A comprehensive study and detailed blueprint covering:

- 1. Asian Common Currency**
- 2. Credit Enhancement and Guarantee Agency**
- 3. Regional Clearing and Settlement Systems**
- 4. Cross-Border Securities Borrowing and Lending Facilities**
- 5. Cross-border Trading Systems**
- 6. Regional Rating Agency**
- 7. Harmonization of Regulatory Framework and of Accounting and Tax Rules**

Creation of Regional Bond Markets (II)

An Asian Version of the Lamfalussy Report (February 2001) for EU's Economic and Finance Ministers will be needed.

Mahalo!

