Notes on Media Briefing by Atsushi Saito, Director and Representative Executive Officer, Group CEO, Japan Exchange Group, Inc., on February 24, 2015

I have three items on the agenda today.
The first topic is about the revisions to the listing rules for the draft of the corporate governance code. Please refer to the handout for reference.
The government's growth strategy "Japan Revitalization Strategy-Revised in 2014" was released last June, and FSA and TSE established a panel of experts last August and have discussed a draft corporate governance code since then.
The draft code was published last December, and we are now reviewing comments from the public.
The draft will be formalized by the expert panel soon.
The corporate governance code set out in the government growth strategy is based on a "Comply or Explain" approach, which means that listed companies either comply with the principles and guidelines set out or explain why they do not.
There is no room for unexplained non-compliance.
We will review the listing rules in response to the government strategy.
To facilitate the smooth appointment of independent outside directors, we will also re-examine the way it is treated in the rules so that listed companies are not hesitant to appoint outside directors.
Simply put, there are two groups; those considered as lacking independence and those considered independent but requiring some disclosure.

The next topic is on developing listing rules to launch an infrastructure fund market. Please refer to the handout as needed.
The government has listed the launch of an infrastructure fund market in its growth strategy. In order to move in the same direction as Abenomics, we are working together with the relevant ministries and other parties.
The wide range of assets targeted includes renewable energy power plants, public facilities (concession), airports, railroads, and motorways. We hope the TSE infrastructure fund market will promote future infrastructure development.
The infrastructure fund market is particularly well-developed in the US, and in Australia and Singapore in Asia.
We believe that the infrastructure fund market will allow private sector funds to be used more effectively and support Abenomics in the same way as TPP.

Infrastructure funds, in general, are said to be less affected by economic trends. Like REITs, they are known to be medium-risk middle-return products, where importance is placed on stable income. Thus, the rules are also designed to consider such aspect.
The tax benefits are currently limited as compared to REIT. Therefore, we will continue working to improve the situation.

Lastly, we will be establishing a special regulation on the listing criteria for the three Japan Post group companies.
As in the case of NTT or JT, shares will be sold in privatization that will be conducted in several phases. We have decided, therefore, to apply a special regulation on the listing criteria for liquidity in preparation for the listing application in the same way as for past cases.
Privatization of state-owned enterprises is a global trend and has a significant effect on a nation's economy.
Privatized companies such as NTT, JT, and the various JRs, have substantially improved efficiency and profitability, and have become the main drivers of the Japanese economy.
Also, since privatized companies are already familiar to investors, a wider range of people including those unfamiliar with equity investments may become shareholders. This will be a great opportunity to advance the trend from savings to investment, which is a long-standing issue in the securities market in Japan.
However, past experience both at home and abroad shows that when share prices fall after listing, investors are left to bear the losses, but when they soar, the parliament will be rife with criticism that the people's assets were sold cheaply.
If we leave the roots of a problem unattended, this great opportunity may end up having severe implications. In order to prevent such a situation, proper assessment of corporate value, in other words, pricing is crucial.
Pricing these three Japan Post companies before listing will be most challenging.
Specifically, the holding company, Japan Post, needs to properly disclose information that will be used for pricing, because it is understood that its two financial subsidiaries that account for most of the group's revenue will eventually have to leave the group under the law.
The holding company will need to disclose at least when and how these subsidiaries will be leaving the group, and its growth strategy centered on its postal and logistics business.
Even though the holding company and its subsidiaries are going to be listed at the same time, unless the prices of the subsidiaries are determined, the price of the holding

company will also be difficult to determine.
What JPX can do is to firmly request appropriate pricing and thorough information disclosure from Japan Post and other related parties.
Details on the three matters related to the listing rules that I mentioned earlier will be provided in a separate session after this briefing.

Q&A:

Q: My question is about the stock market conditions. The Nikkei Average reached a 15-year high. I believe this price is the highest since you joined TSE and after you became the top of the company. You may have some difficulties talking about the stock market, but do you have any thoughts on the current conditions?

A: Daily average trading value for stocks is hovering around JPY 2.7 trillion, closing today at more than JPY 18,600. Stock markets reflect the state of the economy. When measures being implemented are reasonable and appropriate, the assessment is reflected in share prices. I believe the share prices today reflect investor sentiment, or investors' way of thinking.

The government is tackling TPP, agriculture, employment, and healthcare, which, for a long time, have remained unchanged in Japan's social structure. Investors welcome the approach of the Abe government.

So far, the social structure has not undergone any fundamental reform. Reforms may be unpopular and hard to accomplish but are absolutely necessary and can no longer be avoided. Avoidance has resulted in a public debt of more than JPY 1,000 trillion, double the GDP. The fiscal budget is JPY 100 trillion but the tax revenue is only about JPY 50 trillion. This situation is unsustainable, and the people have to make some degree of sacrifice. The government is moving to address the issue, and it is the most visible attempt as compared to previous administrations.

The distribution theory is palatable, but so are financial resources. Fair distribution is important, but what if we have no funds to distribute? We are unable to discuss fair distribution at the same time unless we encourage people to generate funds and seek fund growth. If the distribution theory runs ahead of everything else, we may end up with unemployment or difficult problems related to Japan's future. The Abe administration is using a key word, growth. There may be room for debate, but the market is appreciating the move to create assets for distribution.

As I said before, the market is appreciating the process and the approach, but there is no outcome as yet. Whether the outcome is negative or positive, the stock market will respond accordingly.

Q: The stock market is high despite subdued excitement. Could you share your views on the 15-year high?

A: I observe the situation calmly. I think you know better but given the circumstances in Ukraine and Greece, the global environment is not necessarily wildly excited at the moment. Overseas investors account for about 60% of trading in Japan, and we see that trading is being conducted very calmly.

Q: Annual spring wage negotiations are going into full swing. Is JPX planning to raise its pay?

A: Last year, JPX raised it by two percent, about JPY 5,500, mainly for younger staff. As the company has yet to negotiate with the union, there have been no decisions made, but we will keep pace with other companies.

Q: Will it be at the same level as last year?

A: I cannot say anything concrete at this moment, such as the level, increment, payment method, or scope. Since our business is largely affected by the external environment, JPX has strived to turn fixed cost into variable cost. Therefore, when the company turns in a profit, it should pay bonus, and I believe it has done so. However, as a wage raise will increase fixed cost, I, as a corporate manager, will need to be cautious.

Q: You mentioned that TSE will apply the special regulation for the three Japan Post companies. Can you provide any specifics?

A: There is a criterion that requires 35% or more shares to be floated. Like NTT and JT, because Japan Post is huge, the special provision will allow its listing if other conditions are satisfied even though less than 35% of shares will be listed.

Q: For Japan Post group, its growth strategy, in particular, is important. What information are you going to request it to disclose?

A: Its equity story, along with the rationale, should be disclosed. It has already been announced, so the company would be thinking about its plans for acquisitions.
Japan Post, underwriters, and the audit firm are obviously carrying out their discussions and preparations, so JPX will demand proper pricing and thorough information disclosure.

Q: Information on independent outside directors to be disclosed will be only their attributes. Are there any risks involved if it makes investment decisions more difficult, or if some people in the gray zone come into the picture? Could you give us your view on this?

A: Detailed information will be provided after this briefing. This review will make things much easier to understand for issuers. The requirement itself will not be changed, and we will ask to disclose attributes.

Q: Then shareholders can discuss the matter with each company?

A: Basically, that is not an area for us to intervene. Dialogue is essential between shareholders and the agents of the company, meaning the executive officers and directors. This is also written clearly in the governance code.

Q: I have two questions. First, will this bring the rules on par with those in Europe and the US? Second, if this leads to a more favorable assessment for stocks in Japan among overseas investors, how would you view the effect of the larger inbound fund flows?

A: Let me answer your second question first. We see that the situation has already been well-received by overseas investors. They were watching the market with some doubts over why stock prices in Japan were rising. After watching the process of the corporate governance code being drafted and its imminent incorporation into the exchange rules, they see Japan seriously working on it. If you visit investors overseas, you will understand how they view Japan. When I visited investors in Europe, they highly appreciated the process we are going through. Therefore, I would like to say that overseas investors are evaluating the situation highly.

For the first question, on comparing the situations in Europe and in Japan, different countries have different customs and circumstances. In the US and France, a majority of outside directors are required, whereas, in Japan, only two are requested.

As you may know, the Companies Act requires one outside director, whereas the exchange rules require at least two. I would like everyone to understand that this difference is tremendous effort. It is more significant than simply the number. The number may not be enough, but I believe this event is a major turning point and should be appreciated.

Q: The description says that this applies to all markets including JASDAQ and Mothers. Does this mean two or more outside directors are requested for listed companies in all markets including JASDAQ and Mothers?

And for the second question, could you describe why you reviewed disclosure? Was this to respond to a request from listed companies?

My final question is about the relation between better corporate governance and ROE. While you mentioned it was well-received by overseas investors, I think there is also a very skeptical view. Do you think that better corporate governance will raise corporate profitability as the Abe administration sets out?

A: As you know, the code clearly excludes the UK, Germany, and France. The code is not applied to the Standard market or AIM in the UK, the entry market in Germany, and Alternext market in France. Since markets for emerging companies are open to venture businesses, JPX basically will not impose such demands for 1st and 2nd Section companies on companies listed on Mothers or JASDAQ. However, we will go one step further to require explanation if companies are unable to apply the five basic principles. No explanation is required for other than the five principles.

For the second question, I heard that there were some cases where independent outside directors were not appointed without specific reason.

For the third question, it is difficult, but while I think there is a correlation between corporate governance and ROE, it is not easy to express mathematically.

After we began calculating the JPX-Nikkei 400, some companies started not to allocate term profits to retained earnings and aimed to improve their capital efficiency. Others started M&A or repurchased company stocks. As a result of various policies being adopted, ROE will rise in many cases.

Therefore, this is not a question of appointing one outside director will increase X% of ROE, or that five will increase it by X%. With companies focused on paying employees salary and keeping their business afloat, the economy has been stuck in deflation. In terms of GDP, the gap between Japan and China or the US is becoming wider, which is caused by the gap between capital efficiencies.

I use ROE in symbolic terms, meaning increase profitability by using capital effectively to raise productivity and overcome international competition.

No matter how much we are talking about the distribution theory, if there is no money to go around, even if we were to issue paper to be distributed, it's the same as living in a dream.

Rather than enjoying ourselves and sacrificing our children, grandchildren, and great-grandchildren, if we appoint multiple or many outside directors, and this leads to a change in the corporate management style and corporate growth, then, this will be this generation's first step toward fulfilling our responsibilities.

Q: My question is about the infrastructure fund market. Do you have a target or blueprint for the number of funds you want to see listed in the future?

A: There is no numerical target, but investment in infrastructure carried out by using only government funds may be inefficient. Investment using private sector funds, especially money from investors like shareholders, could result in better efficiency in, for instance, road maintenance. In this sense, while I cannot give a specific number but the more, the better.