

Summary of the Press Conference

Date and time: Tuesday, March 30, 2021, 3:30 p.m. - 4:15 p.m.
Venue: TSE Hall
Speaker: Kiyota Akira, Director & Representative Executive Officer,
Group CEO

Kiyota: First of all, I would like to report on the summary of recurrence prevention measures in light of the system failure of the equity trading system that occurred on October 1, 2020.

Since October of last year, the Council for Recurrence Prevention Measures and the Specialist Working Group have held discussions over a period of about six months, and the report was compiled last week on March 25.

Currently, we are at the stage of putting in place a set of rules to prevent a recurrence. Going forward, we will continue to make improvements by proceeding with responses while maintaining close communication with trading participants and other market participants through system failure drills and other means.

In response to the recent system failure, the JPX Group has decided to focus on “improving resilience” as one of the pillars for management issues. The entire JPX Group is determined to make further efforts to improve the reliability and stability of the market, and we ask for your continued support.

Going on to the second point, on April 1, 2021, we will establish a Center for Advanced Research and Development: DigiMa Lab. to design a future vision of JPX.

A report from The Investigation Committee of Independent Outside Directors in Relation to the System Failure last year proposed that we “consider further enhancements to in-house system development capabilities, design supervision skills, and maintenance capacity.”

In response to this proposal, we plan to take multilateral measures to strengthen resilience. Since last spring, our efforts include further promoting initiatives to accelerate digital transformation as well as working in a wide range of activities such as building a new concept market to create with users and considering an overall system design that will allow JPX to maintain and enhance its business competitiveness.

Through such efforts at the Center, we will strengthen in-house systems development and design capabilities and take on the challenge of further improving resilience while simultaneously enhancing the experience of investors, listed companies, market participants, and other stakeholders.

Reporter: With regard to the TSE system failure, the Council for Recurrence Prevention Measures compiled a report, and procedures for close cooperation between TSE and securities companies, etc. and necessary rules were developed for early recovery.

Could you tell us what measures the JPX Group expects to take in the future to prevent a recurrence of system failures, including those mentioned in the report?

Kiyota: I am aware that the report compiled means we are just at the start line and we need to steadily implement the contents in the report. Specifically, in addition to revising the rules and system documentation, we want to ensure that the necessary system development will be carried out at the exchange. We also ask that all trading participants adopt and apply these rules and by including the trading participants when conducting drills, we must make the rules effective ones.

As the proposed plan suggests in the report, we will conduct drills from first checking each of the functions and then step up the process to check a comprehensive scenario. Throughout this process, we will identify points for improvement and improve the effectiveness of operations.

The system failure last October caused a trading suspension for the entire day and based on reflections on the incident, the Council for Recurrence Prevention Measures and the Specialist Working Group have continued to hold discussions on how to prevent a recurrence. Going forward, just because this report has been released does not mean it is done, and since we have worked specifically on developing various rules with trading participants, the drills will be important to check whether they are effective. It is possible that once we start operations, problems that were not anticipated although not major, minor issues may be detected. We will work with the relevant parties to eliminate such problems one by one in our efforts to not only ensure that “Never Stop” continues but also improve resilience. This cannot be done without the cooperation of market participants, so together we will discuss and work on various issues surrounding the exchange.

Reporter: I would like to ask one more question.

On April 4, there will be just one year left until the TSE market restructure. I would like to ask again about the objective of the reform. Also, looking ahead to the overall transition, various specific movements have already taken place by companies aiming to meet the listing criteria for the new market segments, and it is expected that such actions will continue to go into full swing. How do you view these efforts made by these companies?

Kiyota: With regard to market segments, since the existing framework was left as it was when the cash equity markets of TSE and OSE were integrated in conjunction with the business combination of the two exchanges in 2013, from many investors' perspectives, they pointed out the low convenience due to unclear concepts of Mothers and JASDAQ and other factors. In addition, I feel that we received many comments regarding the 1st Section, mainly on the differences between the examination criteria for new listings and those for market transfers. Therefore, based on awareness of these issues, we began our review in 2018.

Going forward, the current four market segments will be reorganized into three market segments: Prime Market, Standard Market, and Growth Market, so that the characteristics of each market segment can be clarified. We are also reviewing TOPIX to further improve its functionality as an investable index in addition to market representativeness.

The transition to new market segments is about to start. Based on the new listing criteria for each market segment, we will be contacting each of the listed companies in July about their status. Then in the next step from September to December, listed companies will be asked to select a new market segment to join in reference to the Corporate Governance Code which will be revised.

I think you just pointed out that some listed companies are taking this step earlier. I think that companies are starting to make various preparations from the perspective of what steps need to be taken by, for example, reviewing the revised definition of tradable shares and examining the Corporate Governance Code after its revision.

Reporter: I have two questions. The first one is related to prevention of a recurrence mentioned earlier. I understand that the rules have been clearly created this time, but as you have just said, I think that unless various securities companies adopt and follow these new rules and also participate in the drills, basically operations cannot resume when a system failure actually occurs. What kind of communications will be carried out in the future so that these rules are thoroughly disseminated and as many securities companies as possible will participate in the drills? Please share with us your ideas or creative initiatives, if any to encourage companies to participate in the briefings and drills organized by your company.

The second question that I would like to ask is about the news the other day that Cboe Global Markets (CBOE) in the U.S. would acquire Chi-X. I think the competitive environment surrounding stock exchanges in Japan will also change. Could you share TSE's and JPX's views about this?

Kiyota: As for the first question regarding the recurrence prevention of system troubles, etc., we have held 9 working sessions with a wide range of market participants thus far. I believe that market participants and others are gaining an understanding, but not all trading participants have taken part. So, we will cooperate with the Japan Securities Dealers Association to actively provide explanations to trading participants in each region. In addition, when industry-specific meetings are held in Tokyo, we would like to ask for the opportunity to provide explanations. For institutional investors, such as The Investment Trusts Association, Japan, that play a very important role as investors, we are currently discussing the means of communication with them about how the new rules and decisions on measures to prevent a recurrence, etc. will impact the asset management industry, among other matters. Regarding your second question, it was reported that CBOE would acquire Chi-X. Chi-X is a foreign company to start with and was providing PTSs widely overseas. Chi-X currently has markets in Australia and Japan but has already sold its markets in Europe and other areas. This time, the Japanese market will be sold to CBOE. From the perspective of CBOE, I think that they are interested in the Japanese equity market to a certain extent and will enter the market with a view that there is sufficient business opportunity.

Given our recent system trouble, we have received many comments, including those that pointed out the problem of transactions concentrated in TSE and the need to develop PTSs as an alternative market. Of course, we did not make decisions on how the PTS market should be in Japan, and market participants and investors in Japan have probably not been properly educated to actively use PTSs. We did not place any restrictions on PTSs. If PTSs develop, there will surely be synergy from synergistic effects. At the moment, as was the case when the recent system trouble occurred, PTSs have a dependency on TSE in that if there is no price quoted at TSE, there will be no trading volume on PTSs. However, if there is trading volume on PTSs, we will also have trading volume on TSE, so I feel it's mutually beneficial. Therefore, we are also very interested in how CBOE, with Chi-X going under its umbrella, will focus on the Japanese PTS market and hope that we can cooperate with them where we can to expand the market in a win-win relationship. After all, since the entire US market is big, even though there are as many as 50 trading venues, everyone can survive. Unless the market size is large, the market eventually will not survive even if there are many trading venues.

PTS popularity was in the early 2000's and there were four or five PTSs in Japan. As a result, now there are only two PTS operators remaining. After the collapse of the bubble economy, it was a very difficult time in terms of market size. Then, when the market finally started to improve a little, there was the collapse of Lehman Brothers and the market environment became severe again. At present, however, the Nikkei Stock Average has recovered to the

JPY 30,000 level for the first time in more than 30 years, and the impact of Covid-19, which was thought to have a direct negative effect on market transactions, unexpectedly is significantly increasing stock prices and market volume, and recent trading volume on the market is on the rise.

Although the market does not move solely on stock prices, it is true that rising market prices generate energy, and the energy grew strong enough to drive the index to reach JPY 30,000, thereby expanding the equity market. And as it expands, we understand that even if Chi-X's management changes, it's a positive for the growth of PTS itself.

Reporter: I recall you mentioned at the last press conference that you would consider reviewing support for the local exchange in Myanmar. Increasing crackdown on citizens has been reported especially for this weekend. Could you share your thoughts on this?

Kiyota: Yes. I am very concerned about the situation after the coup d'état in Myanmar. We go back to a period when Myanmar was transitioning from military rule to civilian rule, led by then President Thein Sein to democratize the military regime and was greatly welcomed by the rest of the world. Around the same time, the Myanmar government asked the Japanese government and the Financial Services Agency (FSA) for cooperation in building a capital market in Myanmar. Together with the FSA, JPX and the Daiwa Institute of Research (DIR) of Daiwa Securities Group, my former employer, agreed. Myanmar Economic Bank and these two groups - JPX and DIR - together invested capital and established Yangon Stock Exchange as a joint venture. This was part of the national policy to support Myanmar. For that reason, JPX assigned an representative to be stationed locally, and DIR also assigned several representatives there to provide guidance.

Never did I imagine that Myanmar would go back to military rule once again. Moreover, that the military regime would take over the administration in a coup. As you pointed out earlier, the political situation in Myanmar has become extremely grave. It is quite worrying the military, which is supposed to protect the people, is apparently killing people. Given the background that we had cooperated with capital market development in Myanmar as part of the Japanese government's policy, we are currently in consultations with the government. I personally feel that if it was a private company that took part in the establishment of Myanmar's stock exchange, from a business viewpoint they may have no choice but to pull out. That's probably the current situation.

However, as to whether or not Myanmar should be abandoned as part of national policy, until the Japanese government's position is firm, we cannot take any steps. We are currently monitoring the situation while in various

communications with the government. We are ready to withdraw this Myanmar support at any time once the government presents a clear direction.

Reporter: Nomura Holdings' issue has been attracting a great deal of attention in the market. Although there are presumably many issues that remain unclear, what are your views on this case? How do you feel about the issues pointed out, such as impact on the market and that risk management was lax?

Kiyota: My first impression was that an unexpected incident occurred in the securities market and then I became aware of the spread. About 10 years ago when BNP Paribas announced that it was no longer trading subprime securities, the vast majority of people in the world probably had no inkling as to what had just happened. I did not realize it either. I think you remember that within a few days after the announcement, we realized the seriousness of the matter, and the world was caught up in the Lehman Brothers crisis. Although this recent case is not as serious, when you think about it as an incident, it reminds me of the Lehman Brothers crisis in that an unexpectedly huge loss was suddenly brought to light.

I am familiar to some extent with the prime brokerage business that Nomura Securities operates in the U.S. because it was part of the business also formerly conducted by Daiwa Securities New York. The so-called prime brokerage is a business model to earn commission for handling cash management, procurement and lending of stocks and so on when a large institutional investor or such party trades large amounts of securities such as stocks and bonds. From the limited articles, commentaries and other reports I have read, my sense is that the loan part of the prime brokerage business, which involved lending money and in return receiving share certificates as collateral for the loan, was affected because the share certificates obtained as collateral crashed as a result.

If the money lent is repaid, stocks can be returned, but since the hedge fund itself was probably close to going bankrupt, the money could not be collected. Therefore, it is my understanding that although we do not know the rules or the terms of the contract, the securities companies engaged in this prime brokerage business end up taking positions for those share certificates, and those positions contain the stocks that significantly decline.

I think Nomura Securities and Credit Suisse have been mentioned now. We don't know how much the maximum loss was, but in individual hedge fund cases and from what we have heard, the positions held by this hedge fund, its total amount was between like JPY 1 tril. and JPY 3 tril. Even if it is a total loss, if we consider this as an incident for an individual hedge fund, I think it would be different for it flowed through the network from the Lehman

Brothers crisis which involved several hundreds of trillion yen in securitized products incorporating subprime loans that were sold all over the world.

Therefore, although we do not have the full story yet, I was very interested in seeing how Monday's New York market would react yesterday. The Dow Jones rose to an all-time high although it did not exactly rally upward, and while the tech-heavy NASDAQ fell slightly, there was no major upheaval. Looking at the Japanese market today, Nomura Holdings stock prices have also dropped but as it is also the ex-dividend date, there was no noticeable upheaval. I am not sure whether the market has worked in this incident to some extent or whether it was a wait and see situation until new information becomes available but I hope that the market will not get caught up in a major confusion.

Reporter: Regarding a company called Modalis Therapeutics, which was listed on Mothers last year, some shareholders sold their shares during the lock-up period. I don't think such a case was anticipated as part of the system. Is there anything the exchange can do to prevent a recurrence? I would appreciate it if you could tell us how you intend to respond going forward.

Kiyota: Under the securities listing regulations, shareholders who acquired shares immediately before a company's listing are requested to enter into a lock-up agreement with the issuing company for 6 months from the listing date. It is extremely regrettable that such an incident occurred this time. Although this case is not prohibited by law and there are no set penalties in the exchange rules, the rule has been decided, so we would like to request that such a case never happens again. I think we need to make efforts so that investors are aware of this clear-cut rule.

Reporter: With regard to the Nomura Holdings incident mentioned earlier, there is not much information disclosure because there are customers involved and on our end, we would like some more information. There's only an explanation about the possibility of incurring losses but I wonder if further disclosure of information is possible. What are your thoughts about this?

Kiyota: Regarding the Nomura Holdings incident, I spoke with Mr. Okuda, Group CEO of Nomura Holdings, and asked him to make timely and appropriate disclosure of any developments. Mr. Okuda responded that he would make sure to do so. I believe that, if there are any developments in the future, information will be disclosed in an appropriate and timely manner.

Reporter: When did you speak to Mr. Okuda?

Kiyota: Yesterday morning.

Reporter: As we come to the end of this fiscal year, there are quite a number of commodity futures business operators that have either withdrawn or discontinued their business. Please tell us if you consider this to be a sort of inevitable shakeout. Or if the Comprehensive Exchange is one of the pillars of JPX, for example, would you consider setting a target number of contracts traded for commodity derivatives?

Kiyota: Since the transition to a Comprehensive Exchange took place last July, the market itself has not expanded as quickly as we expected. Although the market has grown slightly since before the product transfers, it has not necessarily moved as expected. In addition, there were instances where electricity futures became subject to trading restrictions as a result of too much volatility. However, as TOCOM's electricity futures are still listed on a trial basis, there is little we can do to create movement. Under these circumstances with the market being not as active as we had expected, it is possible that some commodity futures business operators have decided to exit the business after experiencing an extended sluggish period in the commodity market and exhausting their energy as a company in terms of business continuity because they are unable to keep up with the market even though the Comprehensive Exchange was established. For this point, we hope to restore and revitalize the market as soon as possible in an effort to ensure that commodity futures business operators currently active in the market can get back on track. We have transitioned to a Comprehensive Exchange for this purpose and will strive to introduce many financial order flows to OSE and TOCOM. In addition, we will direct as many order flows as possible from overseas institutional investors. Furthermore, we will promote listings of attractive commodity products. It has been decided that the CME Group Petroleum Index Futures will be listed this autumn. I hope that electricity futures will be listed on the main energy derivatives market and in the future that natural gas futures will also be listed as a main commodity on the comprehensive energy market. On this point, we will work closely with the government, the Ministry of Economy, Trade and Industry, and the Financial Services Agency as we aim to list new and attractive products.