

# Business Report

From April 1, 2012  
To March 31, 2013

Japan Government Bond Clearing Corporation

## (1) Review and results of operations

In April 2012, the Committee on Payment and Settlement Systems of the Bank for International Settlements (BIS-CPSS) and the Technical Committee of the International Organization of Securities Commissions (IOSCO) announced the “Principles for financial market infrastructures” (PFMIs) as a new set of international standards. Financial market infrastructures including the Company, which is a central counterparty (CCP), are expected to observe PFMIs at an early date. In addition, in relation to the Basel III capital rules that are applied to financial institutions effective March 2013, the interim rules for capital charges against exposures to CCPs are announced that are designed to expand the use of CCPs as well as seeking further improvement of risk management on the part of CCPs.

Amid these developments, the Company has been making efforts to accomplish various tasks toward expanding the Company’s user base and strengthening the Company’s conditions and systems as a prerequisite thereof, as well as increasing the benefits of using CCPs, in accordance with the “Roadmap for reducing the settlement risks of JGB transactions,” which drawn up in June 2010. Furthermore, the Company has tackled a number of challenges, including strengthening its risk management framework and responding to changes in the environment and the needs of participants, under the medium-term management plan formulated around the core objectives of strengthening its function as a CCP and reinforcing its operating base.

As part of its efforts to improve its risk management framework, the Company has formulated a plan of action designed to observe PFMIs including a plan to improve the scheme for ensuring liquidity funds in the event of default of participants. Additionally, the Company has developed a default handling system that performs necessary processes for smooth settlement and close out or manage the positions in the case of default of participants.

With regard to responding to changes in the environment and participants’ needs, the Company evaluated system specifications based on the functions and specifications of the new BOJ-Net announced by the Bank of Japan and discussion with clearing participants. In addition, the Company, as a CCP, made constructive proposals in the discussion aiming to the shortening of JGB settlement

cycle (to T+1 for outright transactions and to T+0 for GC repo transactions).

With regard to efforts toward increasing usage of our services, the Company, in order to ensure the smooth commencement of participation by trust banks specialized in asset management (scheduled for the first half of 2014), worked on necessary system enhancement based on its agreement with the Trust Companies Association of Japan. Meanwhile, the Company also held meetings to explain matters such as methods for transferring contracts of trust banks to the Company.

With regard to efforts to improve governance, the Company endeavored to increase transparency of management by continuing to provide proactive information disclosure through means such as explaining conditions of the operations to clearing participants through the Advisory Committee and enhancing the coverage of rules posted on its website.

With regard to the improvement of system infrastructure, the Company endeavored to improve its ability to cope with emergencies such as disasters or system failures through more extensive training and other measures aiming to maintain business continuity in emergencies. At the same time, the Company encouraged steady progress in its large-scale system development projects, including system enhancements to prepare for participation by trust banks specialized in asset management, the transition to ISO20022, and the new BOJ-Net. The Company also initiated a project designed to achieve system integration with the Japan Securities Clearing Corporation (JSCC) in order to ensure the steady and efficient progress of large-scale system development projects.

In terms of organizational structure, from the perspective of strategic execution of business activities and closer relationships with clearing participants, the Company established the Strategic Planning Office and the Customer Relations Group. In addition, from the perspective of further strengthening our operating base and improving market efficiency, the Company decided to enter into discussions with JSCC regarding a merger between the Company and JSCC.

With respect to operational performance for FY 2012, despite the decrease in the number of participants accompanying the merger completed in the second half of the year, operating income of ¥1,440 million was recorded, which was comparable to previous year. Selling, general and administrative expenses increased by 2.6% YoY to ¥1,240 million due to an increase in personnel expenses accompanying the increase in the number of employees and an increase in system operation expenses to prepare for emergencies such as disaster and system failure, in addition to other factors. As a result, operating income decreased by 8.8% YoY to ¥200 million. Ordinary income decreased by 7.6% YoY to ¥204 million, while income after taxes decreased by 1.8% YoY to ¥123 million.

## **(2) Capital investment**

The total amount of capital investment made during the current year was ¥341 million, which was mainly used for the improvement of system infrastructure, including development expenses for the system to handle defaults of participants.

## **(3) Financing**

There is nothing to report.

## **(4) Major issues to be addressed**

The Company, as part of the infrastructure to reduce risk and improve efficiency related to settlement by market participants, has played a part in the stabilization of the financial and capital markets in Japan since the commencement of its operations in 2005. It is now, however, required to further improve its risk management functions in compliance with international standards such as the PFMI announced in April 2012, and Basel III.

Under such circumstances, the Company, in order to strengthen its functions as a CCP, will take measures such as further sophistication of risk management, measures designed to achieve the shortening of settlement cycle, increasing usage, and strengthening governance and system infrastructure. At the same time, the Company will merge with JSCC to further strengthen its operating base and improve market efficiency. The Company, therefore, humbly asks its shareholders for their continued support and encouragement.