

# Japanese Securities Market in Aging and Low-Growth Economic Environment

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## Abenomics

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- Abenomics is the combination of various economic policy initiatives, focusing on the exit from deflation.
- Abenomics may be a good case study for national governments to overcome economic issues related to aging and fiscal constraints
- Inflation expectation and wealth effect could be important. The materialization of growth strategy is demanded. Under the pressures from investors, the revival of corporate profitability started to gather great attentions.

## Securities Market Reform in Japan

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- Lessons from bubble economy: (1) Excess lending to properties backed by easy monetary policy, (2) Long-lasting deflation and NPL problem (balance sheet recession or death spiral) >> How to utilize capital market is the key
- Securities market as resource of risk money: Lower growth >> Risk capital for emerging and growth companies, for reorganization of matured companies
- Utilization of financial assets: Needs for managing assets for preparing aging society

## Changes in Investor Behavior and Bank/Brokerage Industry

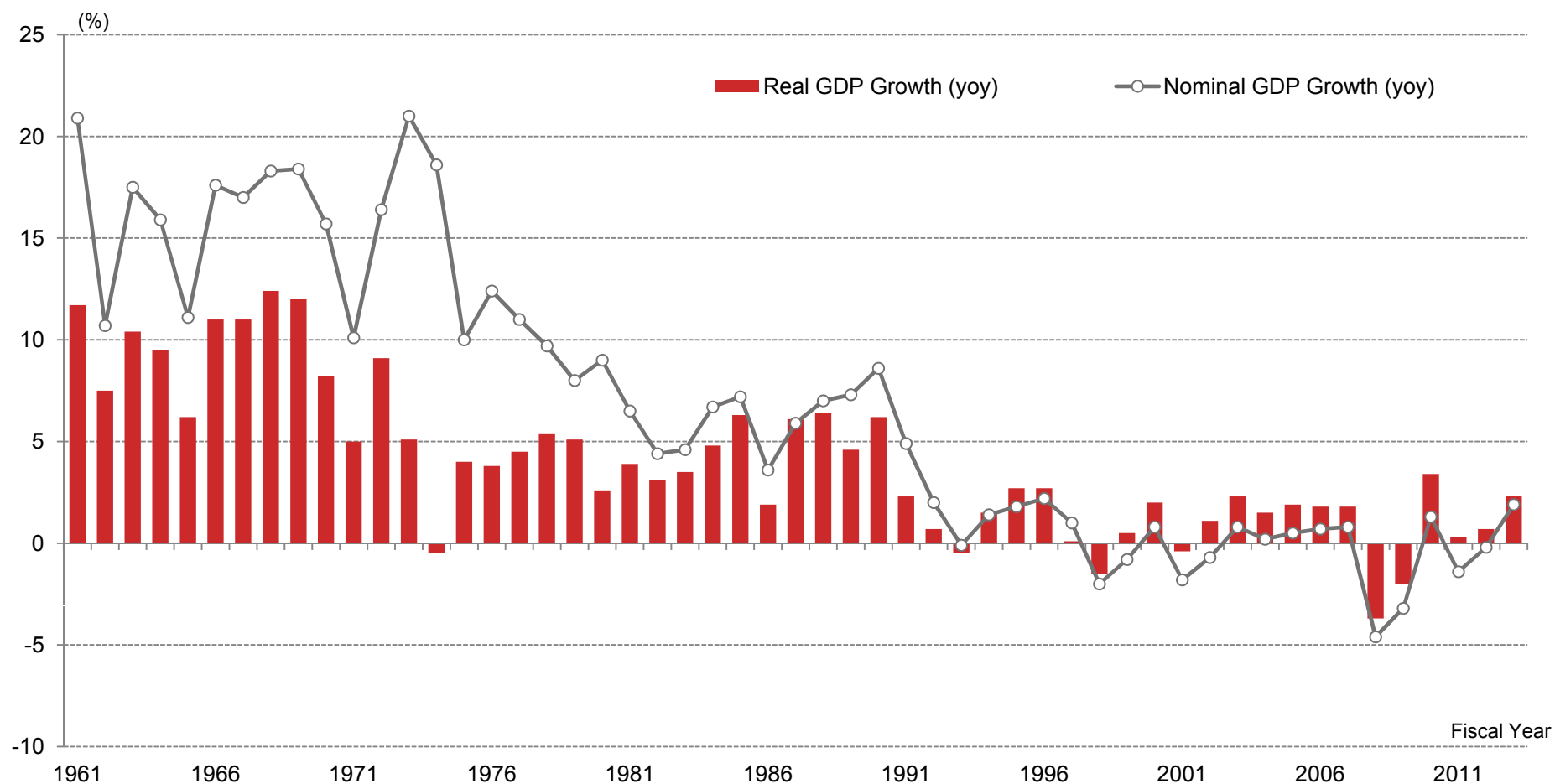
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- In Japan, financial behavior changed dramatically under low-growth economy
- Almost always, the opportunity for investment services players has been expanded under matured economy and aged society, reflecting the accumulated financial stock in Japan
- Asian countries may face economic issues similar to Japan's, and how to develop active capital market and healthy financial institutions will be key to overcome such problems.

# Primary Issues on Japanese Economy: Sluggish Growth and Deflation

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Japan's Economic Growth Rates (FY 1965-2013)

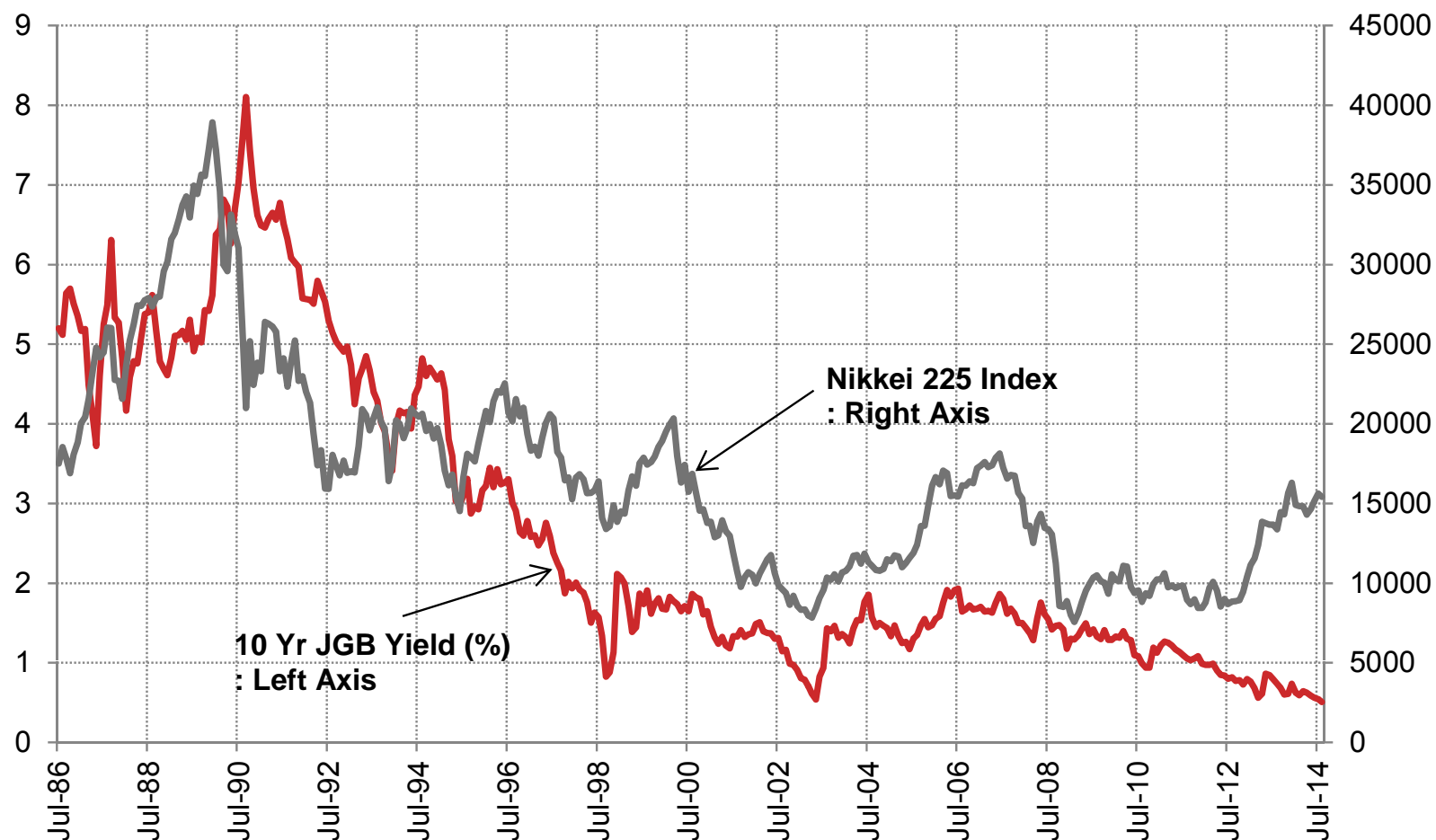


Source: NICMR based on Cabinet Office

# Extraordinary Market Environment After 1990

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Long-term Interest Rate and Share Prices (Monthly Last Prices, July 1986- August 2014)

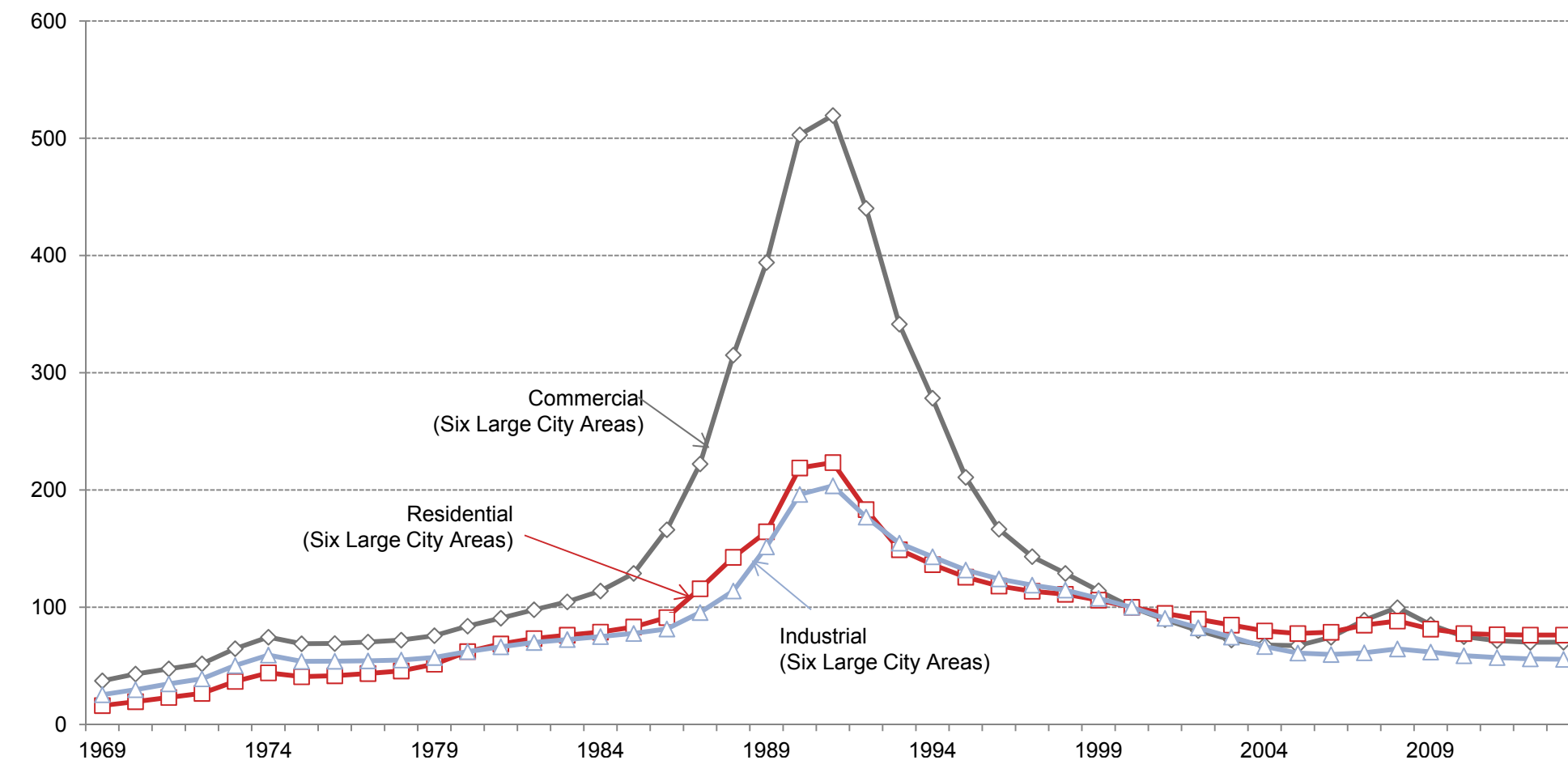


Source: NICMR based on Bloomberg

# Long-lasting Asset Price Deterioration

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Urban Land Price Index (Six Large City Areas, 1969-2013: As of the End of March)



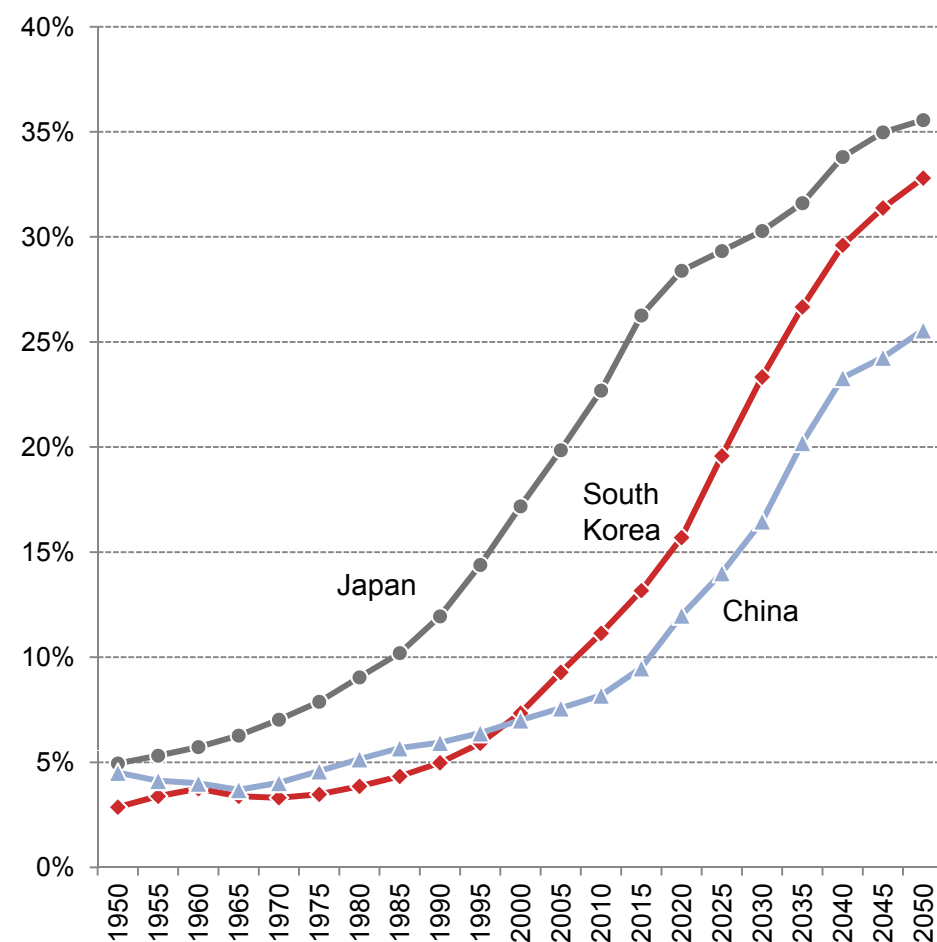
Note: Index in March 2000 = 100.0. 6 large city areas include Tokyo Metropolitan Area, Yokohama, Nagoya, Kyoto, Osaka and Kobe.

Source: NICMR based on Japan Real Estate Institute

# Tough Constraints: Demography and Fiscal Position

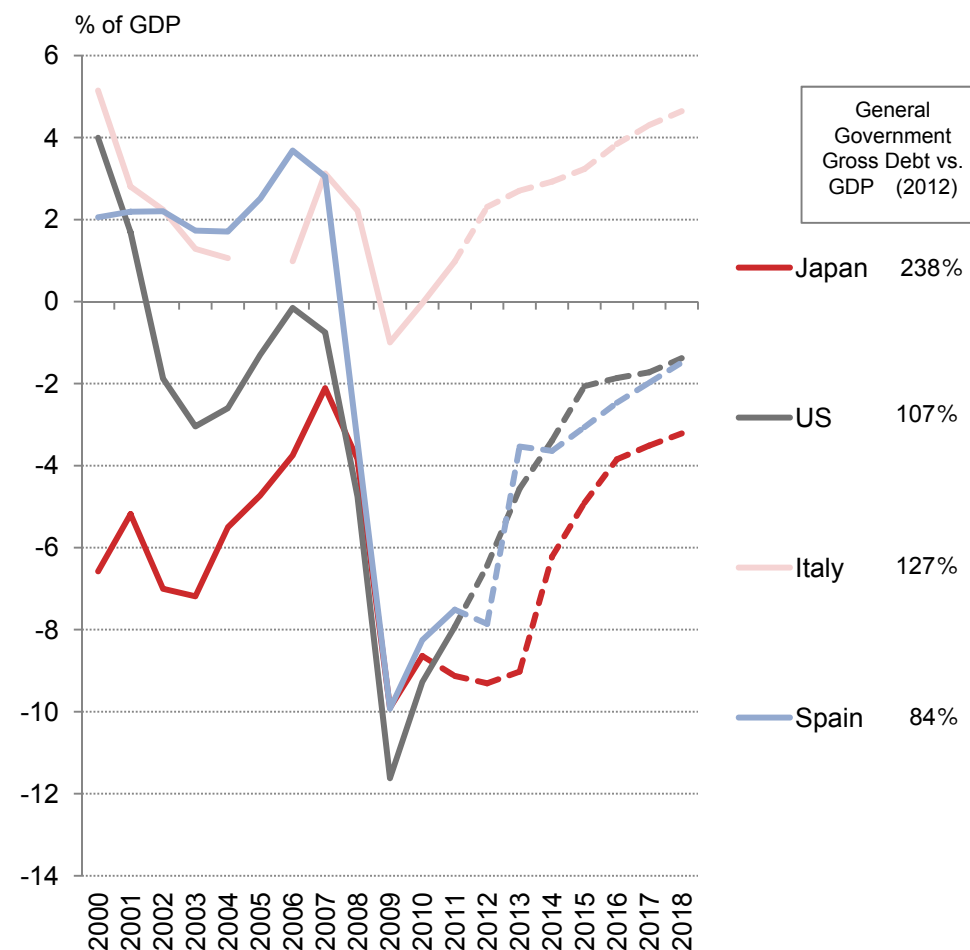
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Forecast for Population Aging  
(% of Over 65Yrs Old / Total Population)



Source: NICMR based on United Nations "World Population Prospect"

Budget Deficit: Primary Balance



Note: Dotted line represents projection  
Source: NICMR based on IMF WEO database

## Three Arrows

### 1. Bold Monetary Policy

- Introduction of Quantitative and Qualitative Easing
- Inflation Target: Achieve 2% Inflation in 2 Years

### 2. Flexible Fiscal Policy

- Fiscal Consolidation Plan
- Stimulus Fiscal Package

### 3. Growth Strategy

- “Japan Revitalization Strategy”
- Supply-side Reform (Deregulation, etc)
- Demand Creation (International Business Hub through Special Economic Zone, etc.)

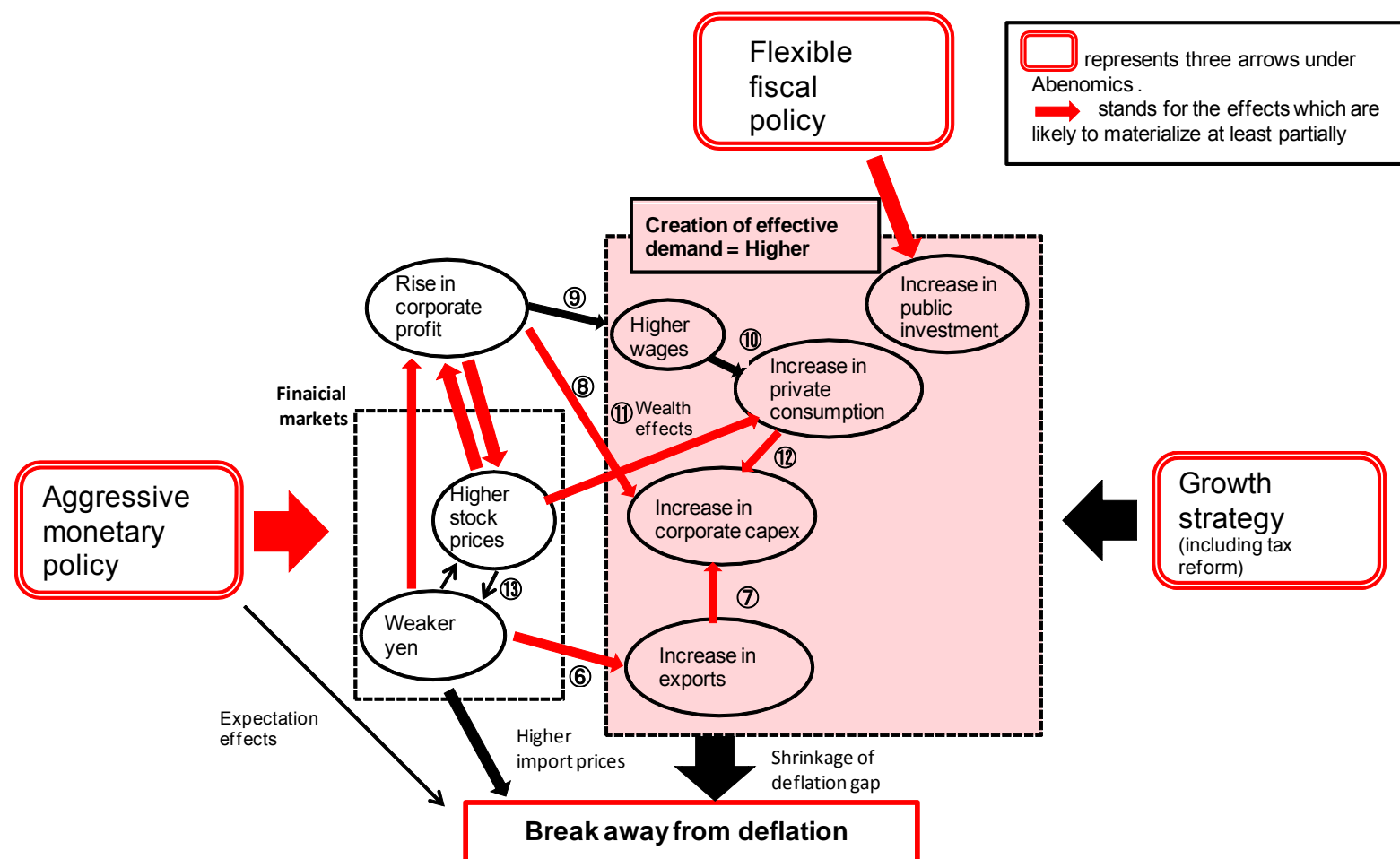
## Goal

Exit from  
Prolonged  
Deflation

Revitalization  
of  
The Economy

# How Abenomics Works?

- Various channels are supposed to function in order to boost effective demands under Abenomics



Source: Nomura



# Key Elements of Kuroda's Monetary Policy

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## Allocation of Funds to BOJ's Asset Purchase Program

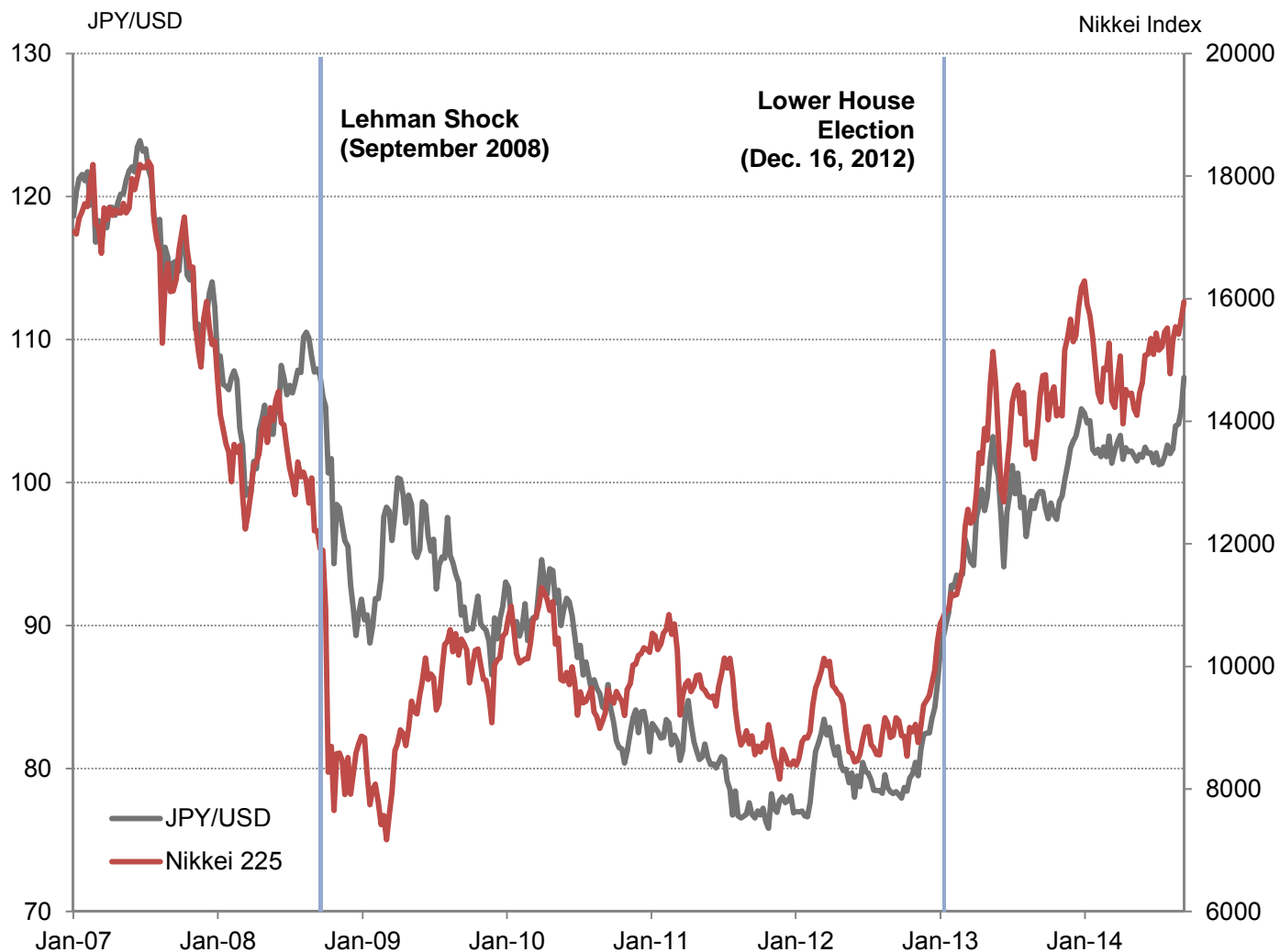
	Current maximum amount of purchases			(JPY Trillion)
	(End- Dec 2012)	(End-Jun 2013)	(End- Dec 2013)	Open-ended method 2014
Fund supply operations against pooled collateral	25.0	25.0	25.0	25.0
Long-term JGBs	24.0	34.0	44.0	2.0
Short-term government securities	9.5	19.5	24.5	10.0
Commercial paper	2.1	→	2.2	Maintain holdings outstanding as at end-2013
Bonds	2.9	→	3.2	Maintain holdings outstanding as at end-2013
ETFs	1.6	→	2.1	Maintain holdings outstanding as at end-2013
J-REITs	0.12	→	0.13	Maintain holdings outstanding as at end-2013
<b>Asset purchase funds</b>	<b>65.22</b>	<b>85.22</b>	<b>101.13</b>	<b>111.13</b>

Source: Nomura based on Bank of Japan

# Financial Market Responded to Abenomics

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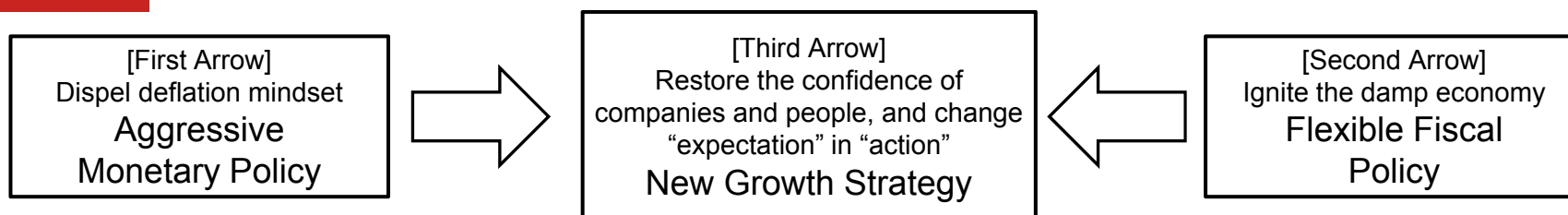
Currency Exchange Rates and Stock Price (Weekly Last Prices, 01/05/2007 – 09/12/2014)



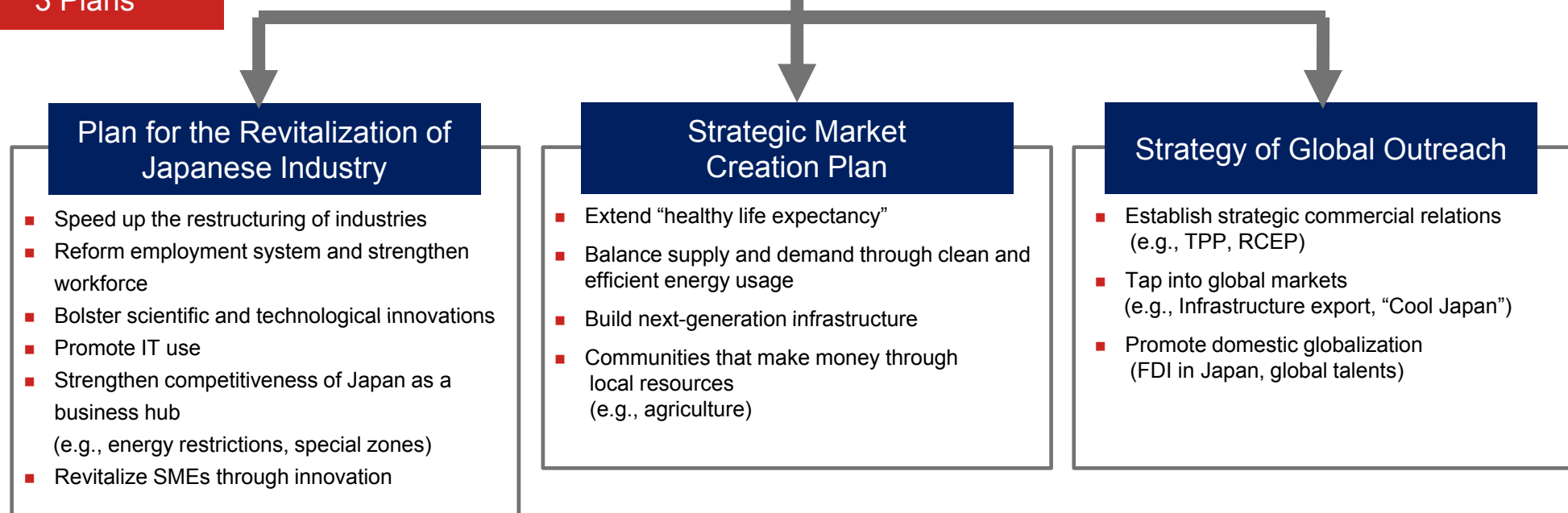
Source: NICMR based on Bloomberg

## Japan Revitalization Strategy

### 3 Policies



### 3 Plans



# Revised Japan Revitalization Strategy (June 2014): Overview

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## 10 Key Reforms to be Tackled

### Regain the Earning Power

1. Enhancement of Corporate Governance
  - Drafting of “Governance Code”
2. Reform of Public and Quasi-public Funds
  - Revision of Policy Asset Mix of GPIF
3. Provision of Risk Money
  - Promotion of Ventures, Crowdfunding, etc.

4. Pro-growth Corporate Tax Reform
  - Reducing the Effective Rate of Corporate Tax
5. Promotion of Innovation and the “Robot Revolution”

### Reinforcing Workforce- Promotion of Women’s Participation and Working Style Reform

6. Promotion of Women’s Participation

7. Reform of Working Styles

8. Utilization of Foreign Human Resources
  - Review of Training Programs for Foreign Workers

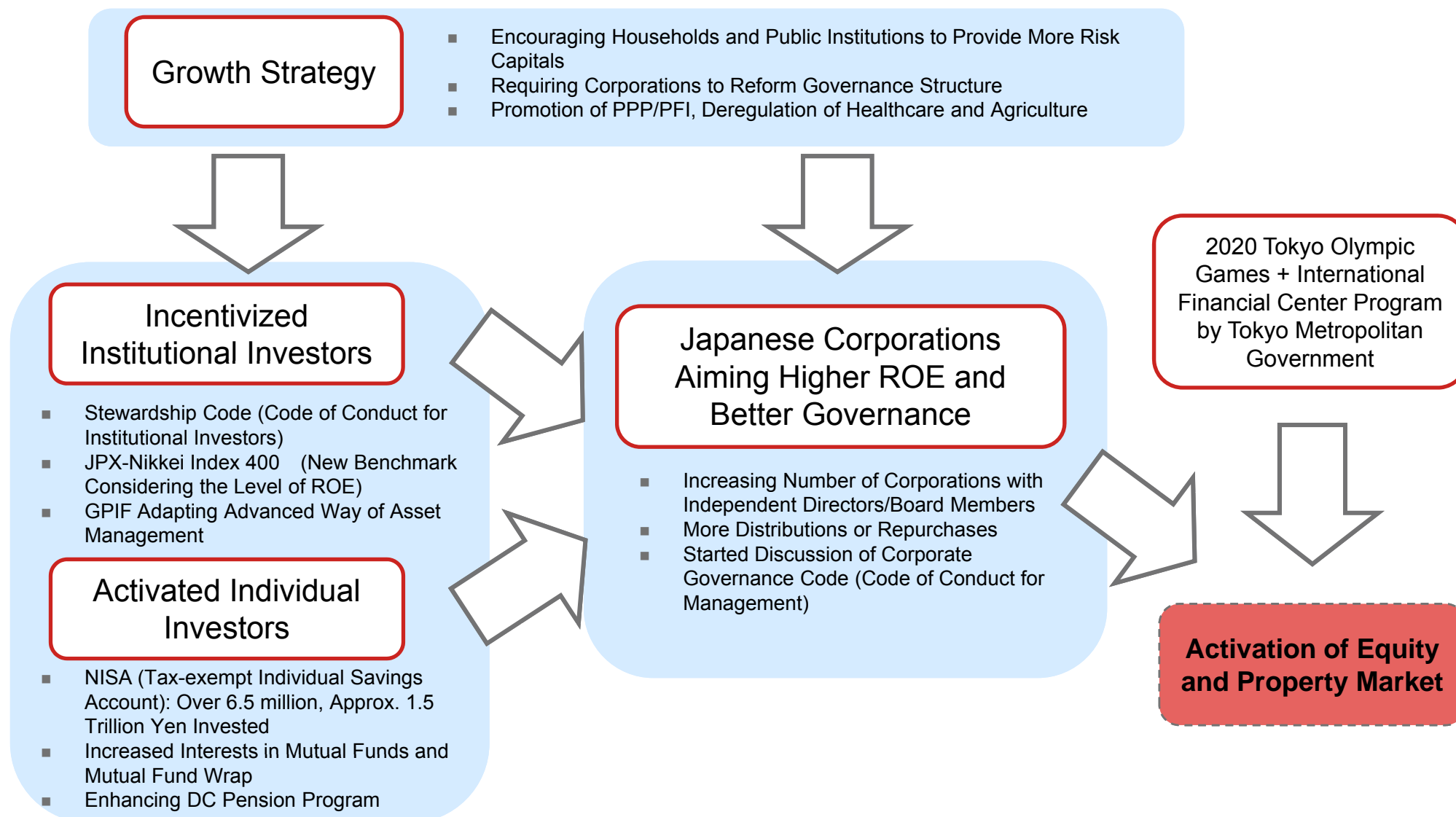
### New Growth Engines and Development of Industries that Play Central Roles in Local Economies

9. Developing Aggressive Agriculture

10. Vitalization of Health Industry and Provision of High-quality Healthcare Services
  - Establishment of Non-profit Holding-company system



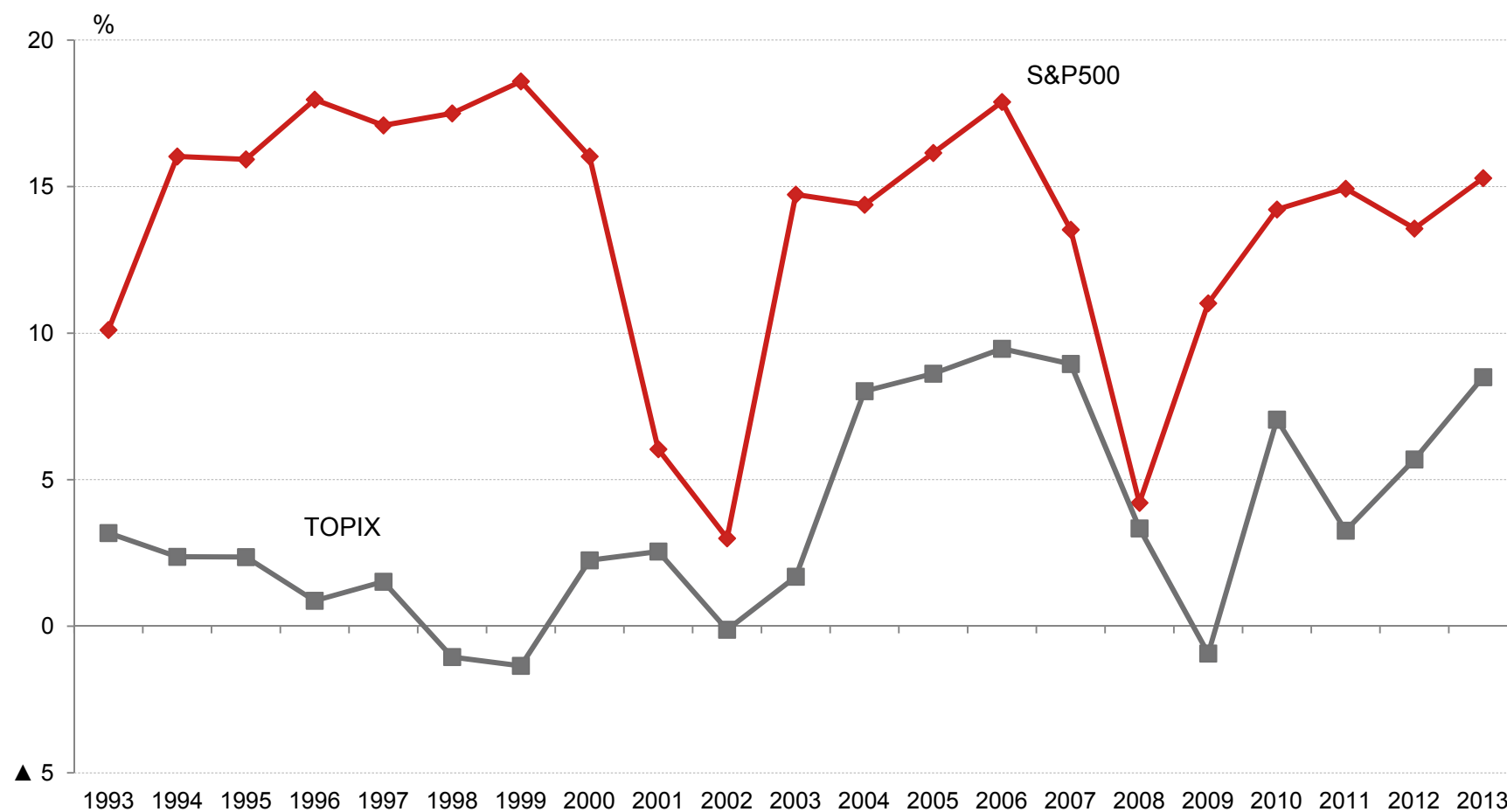
**Spreading Achievements of the Growth Nationwide**



# Growing Attention to Earning Power of Japanese Corporate Sector

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Historical Trend of Return on Common Equity: U.S. and Japan



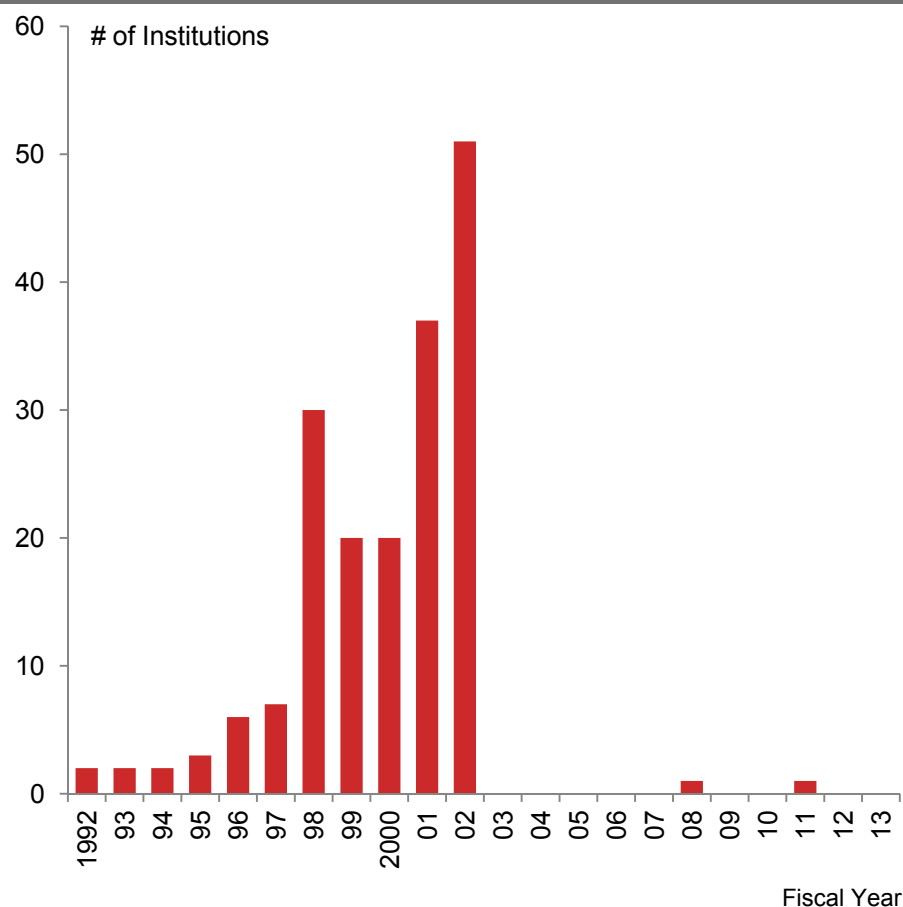
Source: NICMR based on Bloomberg

# Japan's Financial Crisis and Stagnant Banking Sector

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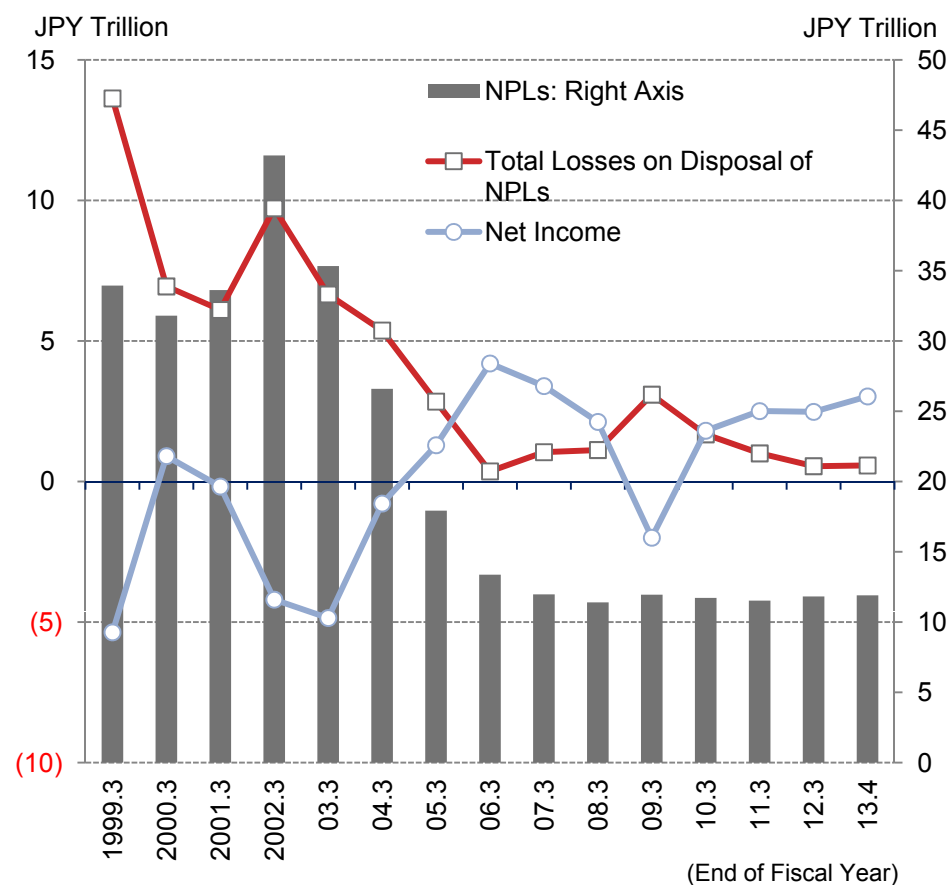
- A series of financial institution failures in late '90s created a crisis condition in the financial market
- Banking sector saddled with NPL problems remained unprofitable, unable to provide funding for growth

**Japan: Failures of Depository Financial Institutions**



Source: NICMR based on Deposit Insurance Corporation

**Non-Performing Loans and Losses:  
Deposit-Taking Financial Institutions**



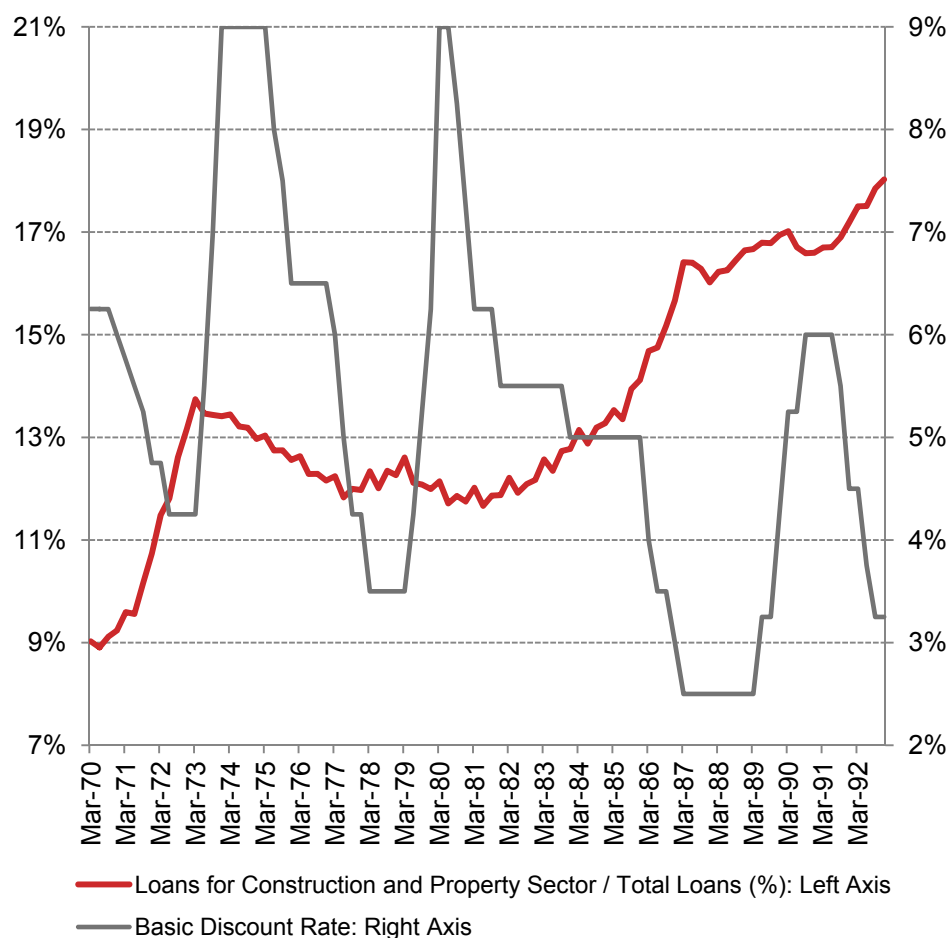
Source: NICMR based on Financial Services Agency

# Real Estate Bubble and Securitization

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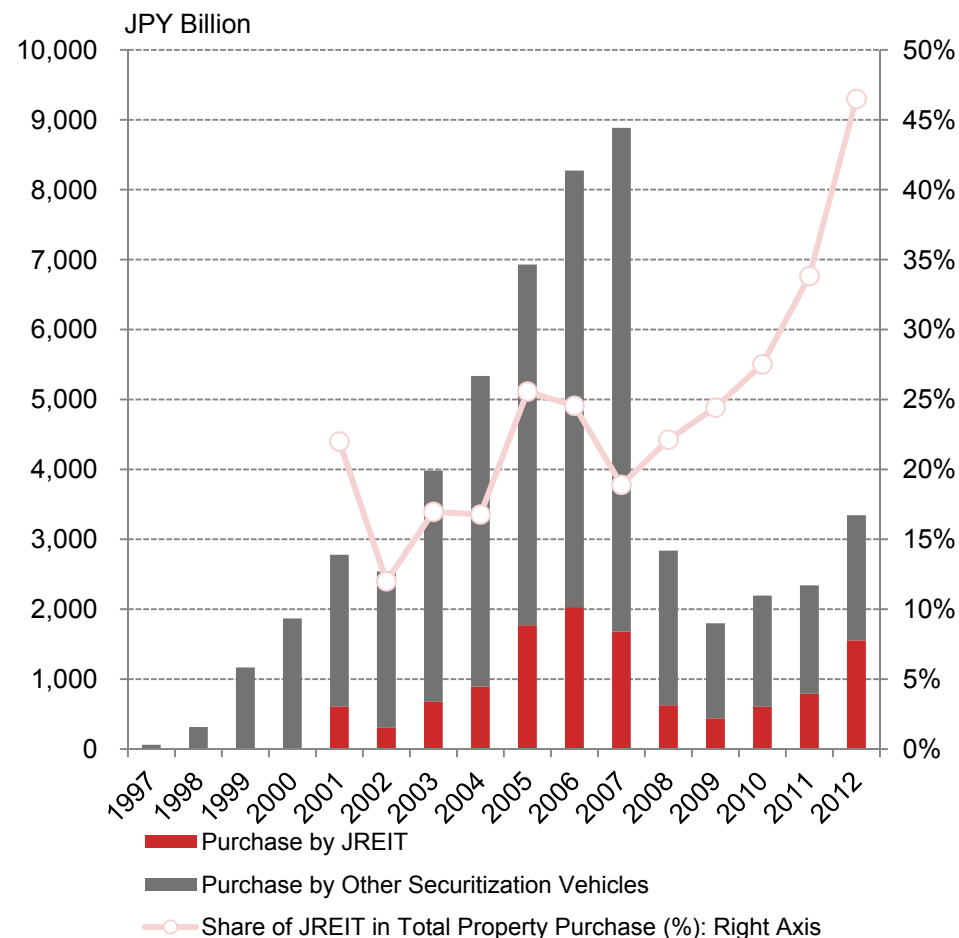
- Monetary easing in '80s to control rising value of yen led to an increase in construction and real estate lending
- Real estate transactions were reactivated through the introduction of securitization and REIT

Increased Credit Exposure for Property Sector in 1980s



Source: NICMR based on Bank of Japan

Real Estate Securitization after FY 1997: Transaction Values



Source: NICMR based on Ministry of Land ,Infrastructure and Transportation



# Securities Market Reform in Japan During the Last Two Decades

## Securities Market Reform in Japan: Historical Events

1996.11	“Japan’s Financial Big Bang” declared by PM Ryutaro Hashimoto
1997.10	Introduction of comprehensive securities account
1998.6	Financial Systems Reform Act (Most legislation became effective in Dec 1998)
1998.12	Start of mutual fund distribution by banks and insurers
1999.10	Liberalization of equity brokerage commission
2001.6	Koizumi administration declared “From Savings to Investment” in the economic and fiscal policy initiative
2001.6	Revision on Commercial Law (Introduction of Unit Share)
2001.7-9	ETF and J-REIT markets started at Tokyo Stock Exchange
2001.10	Defined Contribution Pension Law (Japanese version of 401 (k) plan started)
2003	Preferential tax rate system was introduced (10% on dividends and capital gains from the sale of listed stock)
2004.12	Deregulations on introducing broker system
2005.6	Enactment of Companies Act
2005.10	Postal offices started mutual fund distribution
2007.9	Fully enactment of Financial Instruments and Exchange Act
2007.12	Financial Services Agency “Plan for Enhancing Competitiveness of Financial and Capital Markets”
2009.1	Dematerialization of share certificates
2013.1	Integration of Tokyo and Osaka Stock Exchanges to create Japan Exchange Group (JPX)
2014.1	Introduction of NISA (Nippon Individual Savings Account) program

Source: NICMR based on various resources

- Enhancing competitiveness of financial market by conducting comprehensive regulatory reform

## Major Policy Initiatives in Financial Big Bang Reform

### “Free”: Liberalizing Entry, Instruments and Pricing

- Business Scope of Subsidiaries
  - (1) Deregulation on Businesses by Banks' Brokerage Subsidiaries or Trust Subsidiaries
  - (2) Allowing Mutual Entry by Insurers and Bank or Other Financial Businesses
- Straight Corporate Bond by Commercial Banks
- Insurance Distribution by Banks
- Liberalizing Equity Brokerage Commission
- OTC Derivatives on Securities
- Financing Methods for Nonbank Institution
- Financial Holding Company System
- Revising Foreign Exchange Act
- Developing Investment Trust Market
  - (1) Comprehensive Brokerage Account
  - (2) Investment Corporations (Company-type Funds)
  - (3) Privately Offered Investment Trusts
  - (4) Fund Sales by Bank Subsidiaries
  - (5) Fund Sales by Bank

### “Fair”: Clarifying Rules and Increasing Transparency

- Early Correction Measures for Banks
- Enhancing Disclosure

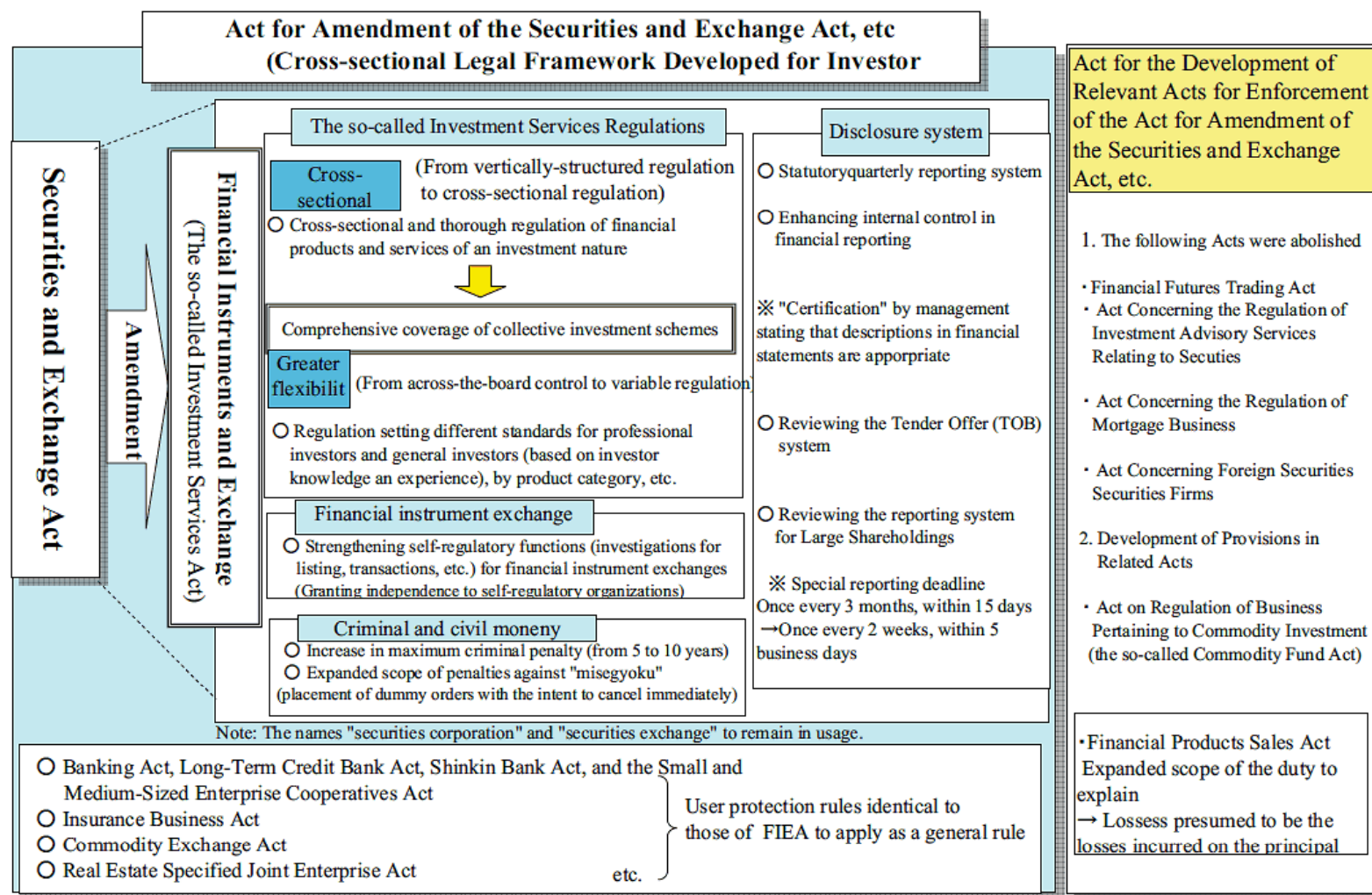
### “Global”: Developing Globally Competitive Regulatory, Supervisory and Accounting Systems

- Reforming Tax Systems on Securities Investment
- Developing Accounting System
- Transforming into New Financial Supervisory System

Source; NICMR based on MOF releases

# Financial Instruments and Exchange Act (Enactment in September 2007) **NOMURA**

Establishing a cross-sectional legislative framework for investor protection covering financial products



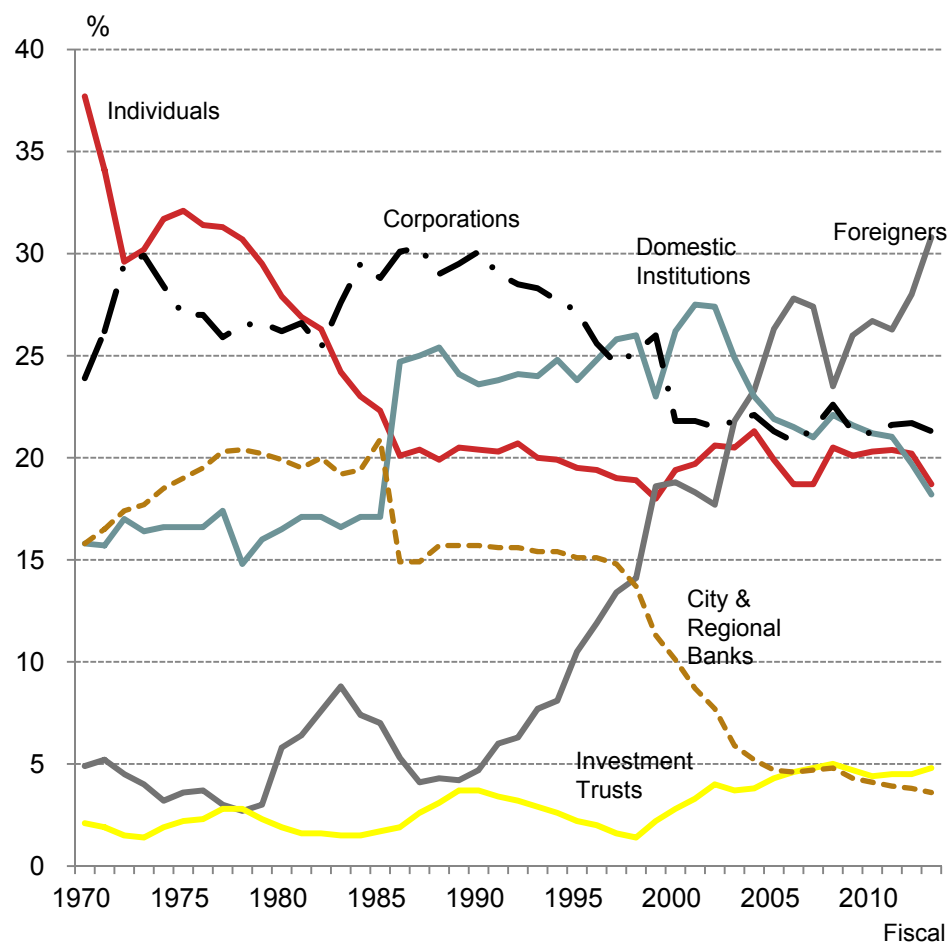
Source: FSA

# Impact of Securities Market Reform

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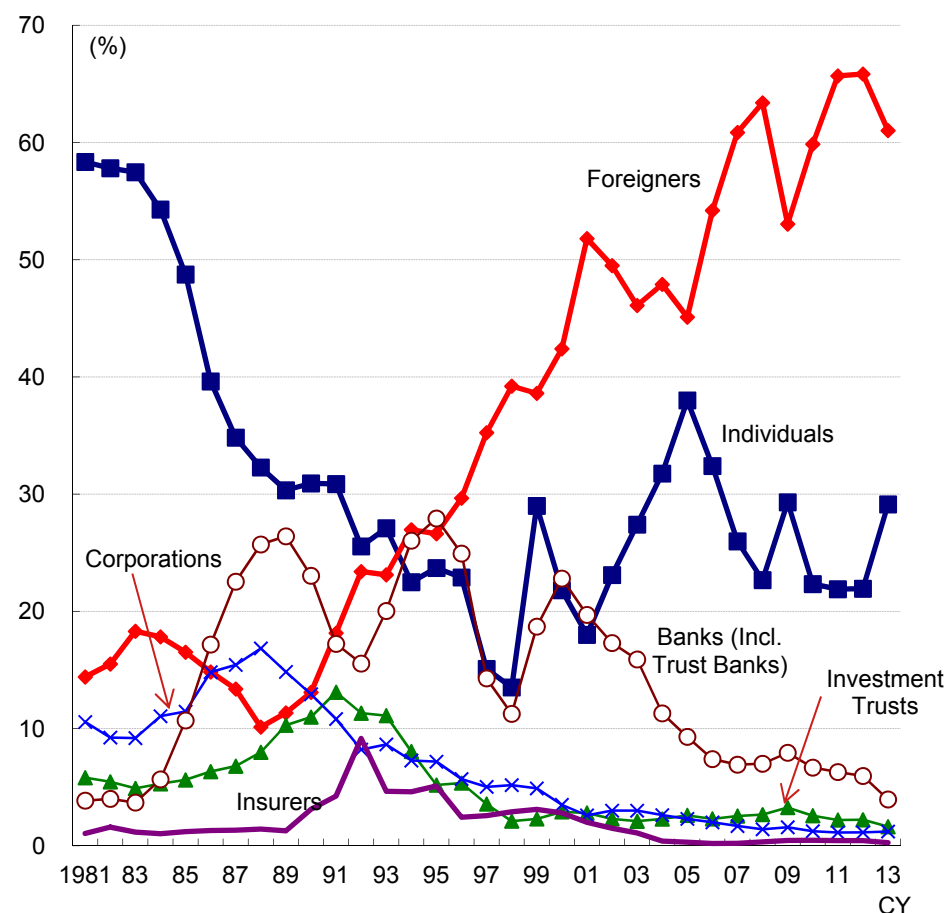
- Flow of foreign investment has increased significantly, but domestic money flow reform is only half way complete

Equity Holdings by Investor Type (FY1970-2013)



Note : National exchange basis. Domestic Institutions include Trust Banks, Insurers and Other Institutions. Trust Bank Data before FY1985 is included in City & Regional Banks category.  
Source: NICMR based on Survey by National Exchanges

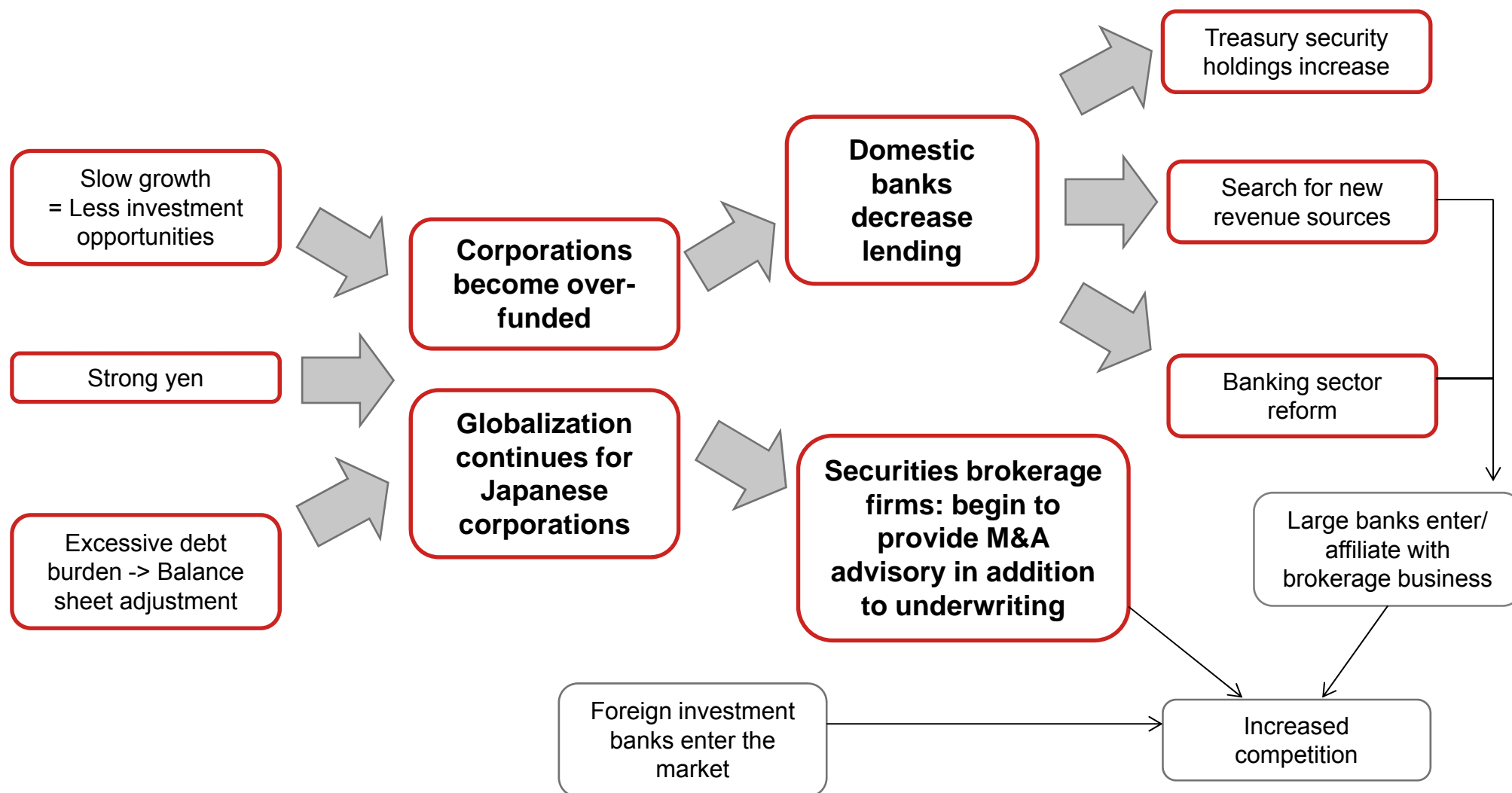
Shares of Equity Trading Values by Investor Type



Note : TSE Section 1 basis.  
Source: NICMR based on Survey by Tokyo Stock Exchange

# Changes in Corporate Sector and Responses by Japanese Banks/Brokers

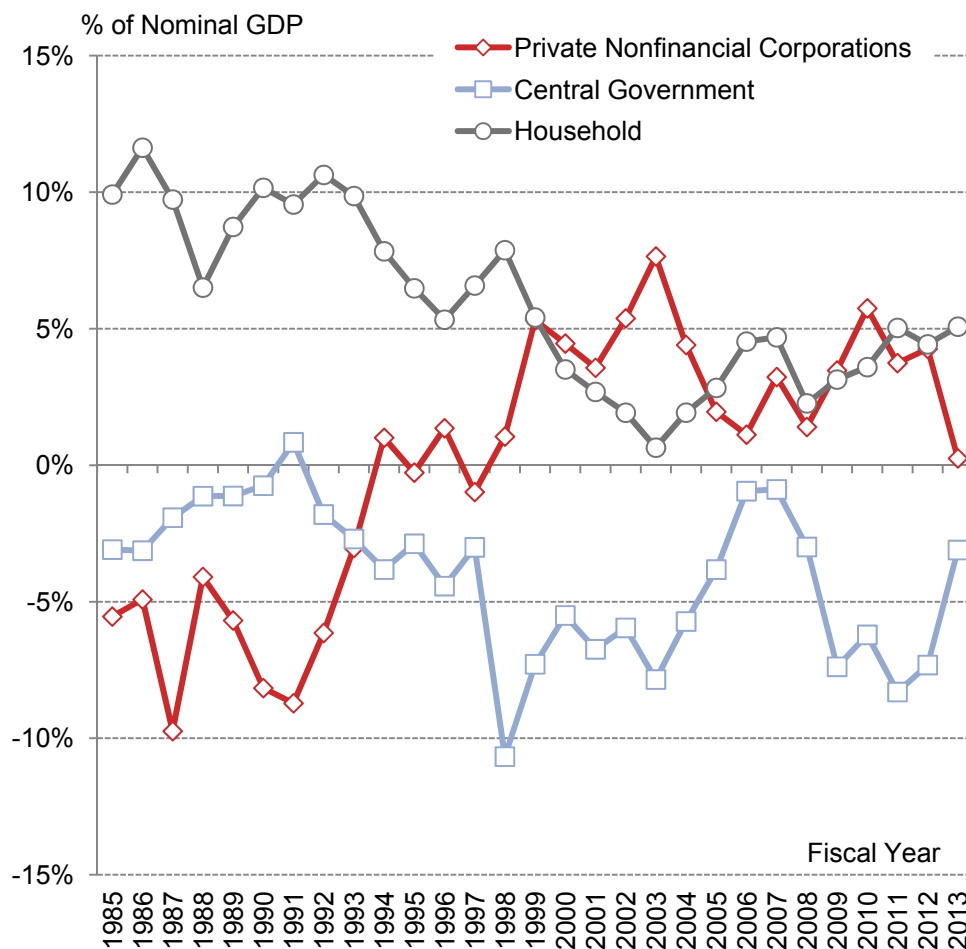
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# Corporate Sector Becomes Over-funded and Bank Lending Decreases

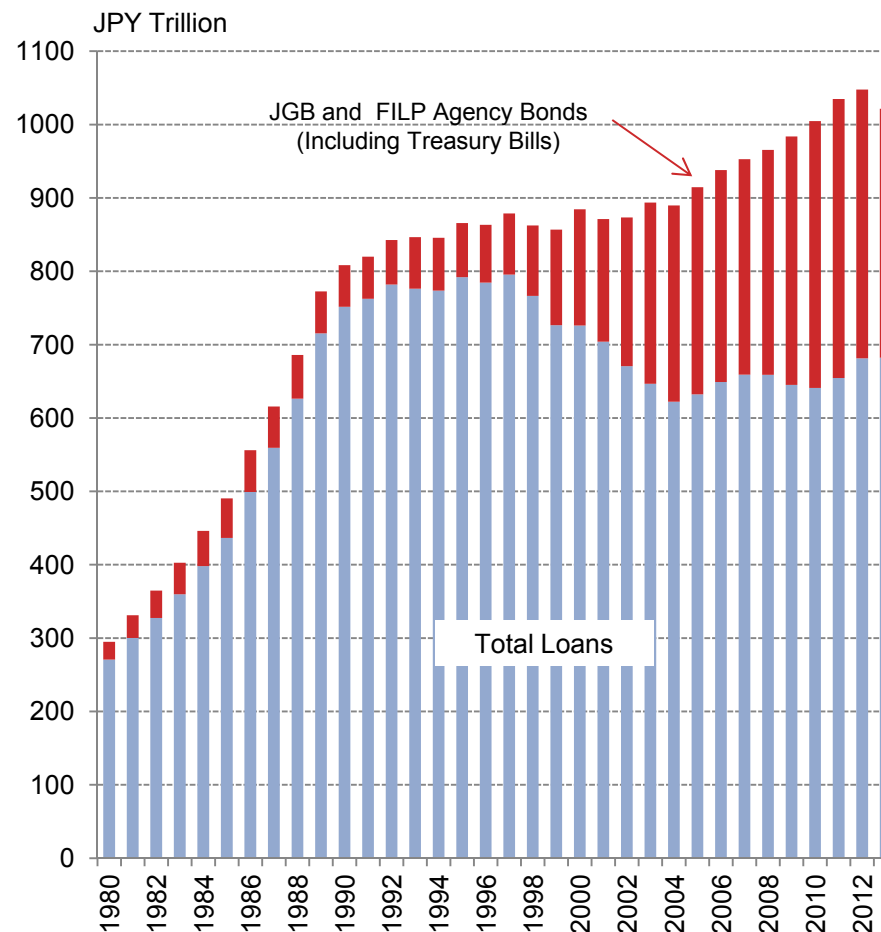
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Fund Balance by Sector (Flow base, % of Nominal GDP)



Note: Data for FY2013 is as of the first quarter (annualized).  
Source: NICMR based on Bank of Japan and Cabinet Office

Major Assets of Japanese Banks

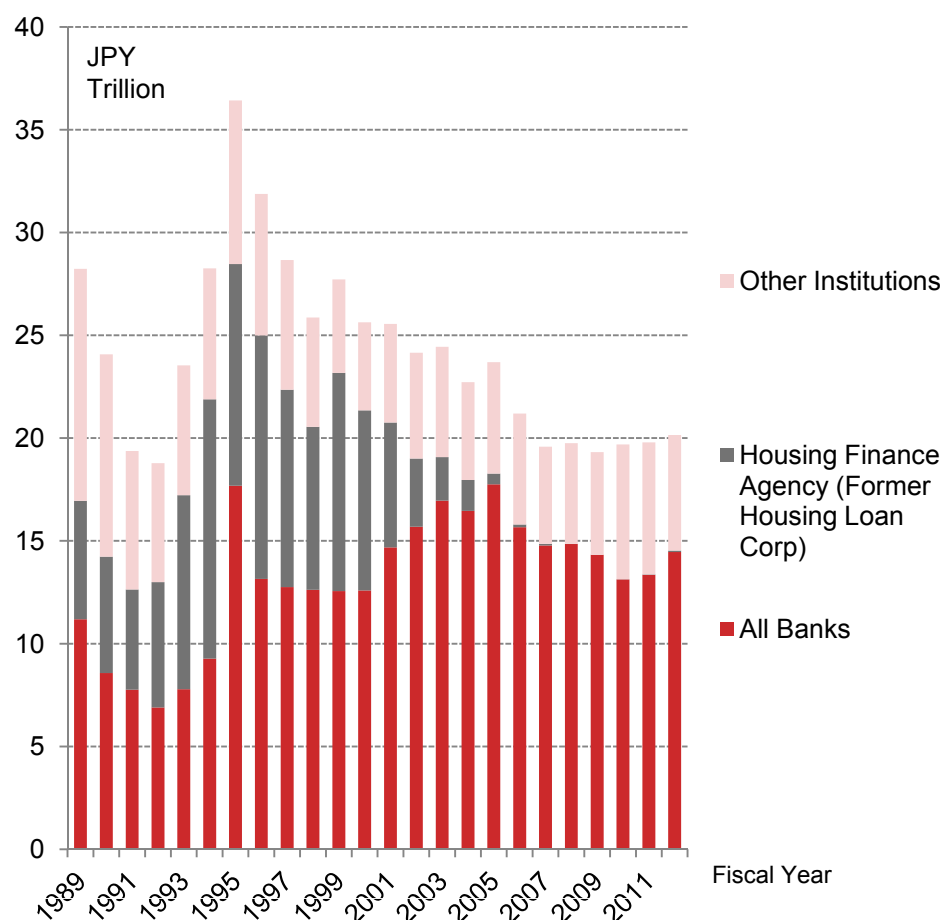


Note: Stock Data for Depository Institutions(End of Fiscal Year). FILP stands for Fiscal Investment and Loan Program  
Source; NICMR based on Bank of Japan

# Banks Shift Their Focus to Retail Financial Services

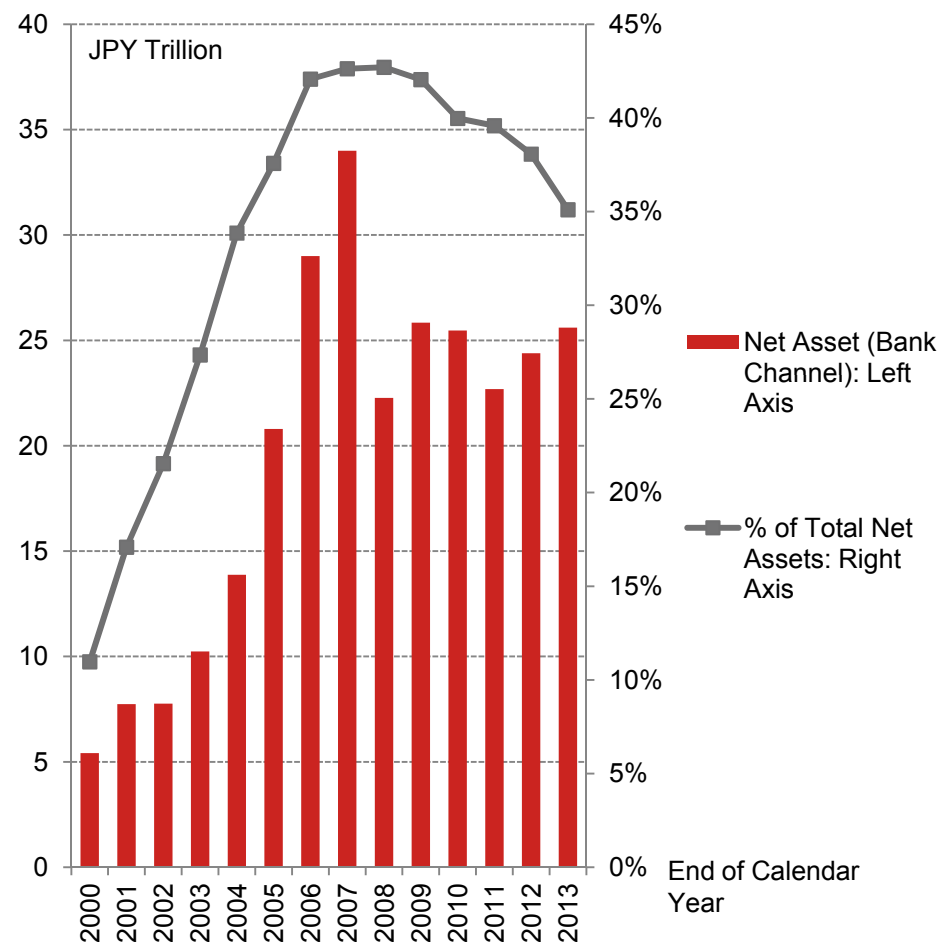
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Housing Loan Origination (FY1989-2012)



Source: NICMR based on Housing Finance Agency

Investment Trust Distributed Through Bank Channel  
(Publicly-offered Funds)



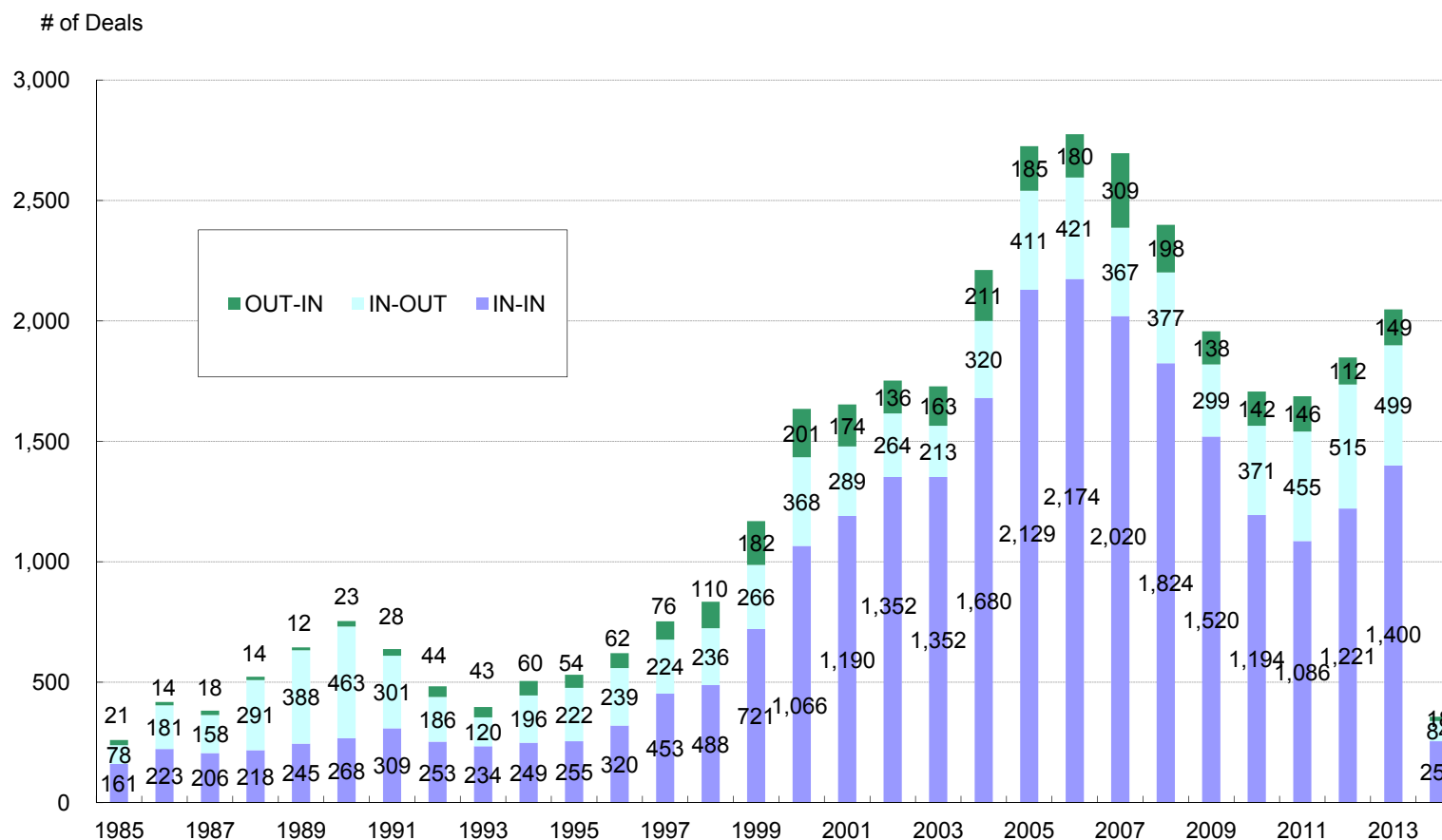
Note: Including MMF assets.

Source: NICMR based on The Investment Trust Association

# Expansion of Japanese M&A Market

- Japanese M&A market expanded as a result of failed Main Bank system, globalization and regulatory reform

M&A Deals in Japan: 1985 – February 2014

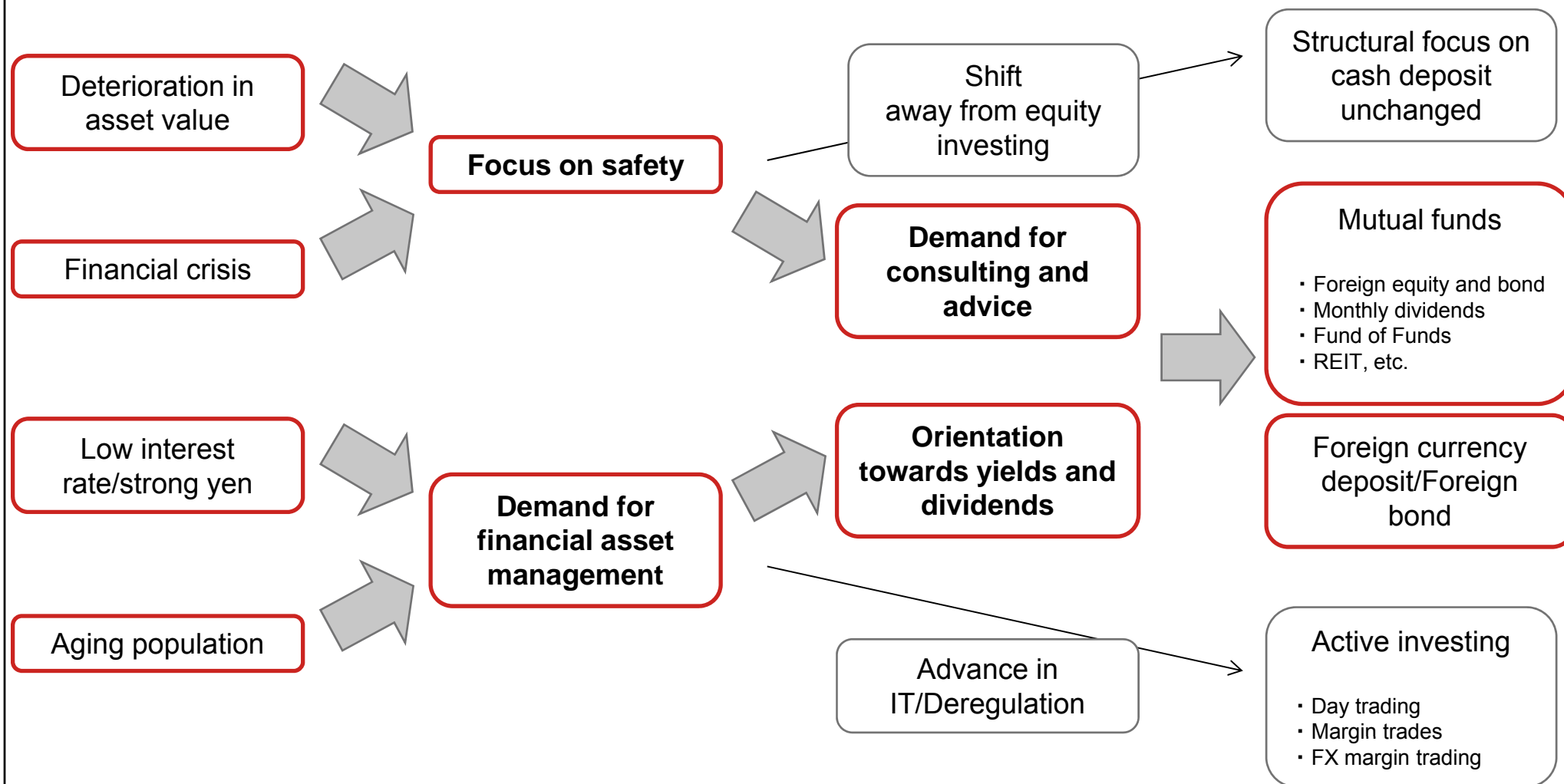


Note: Excluding mergers within group companies. Data for 2013 is January through August.  
Source: NICMR based on RECOF "MARR"



# Behavior of Individual Investors and Strategic Moves in Securities and Assets Management Industry

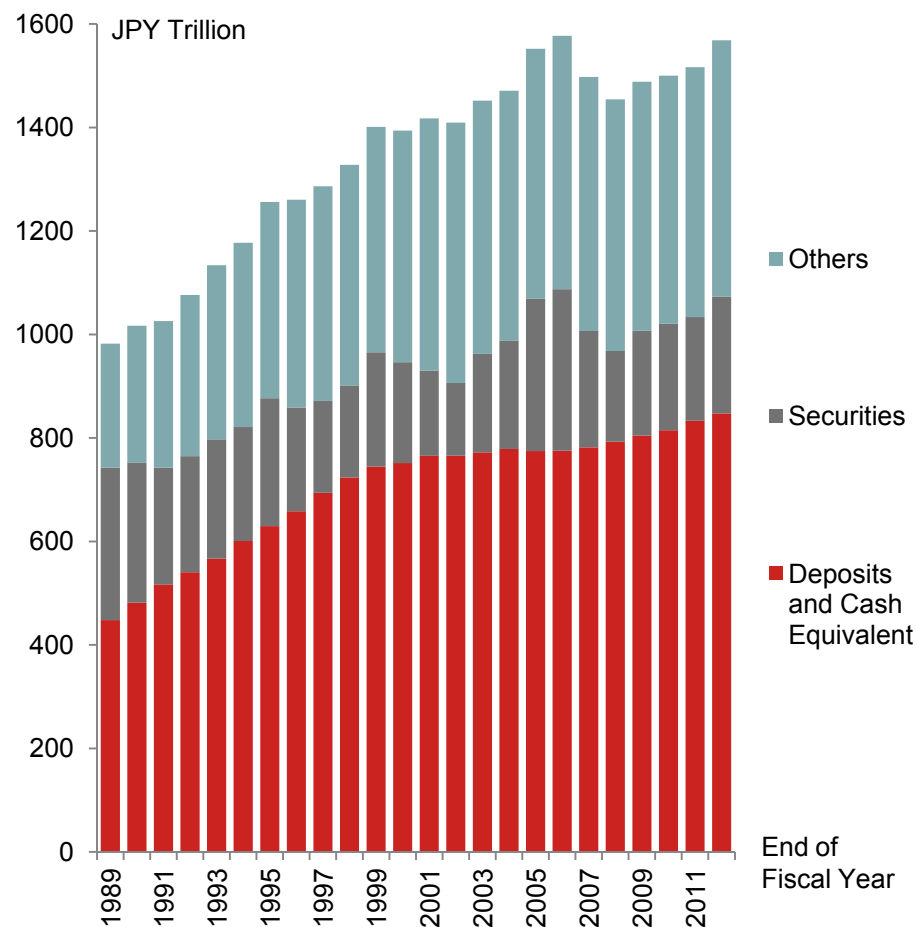
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# Japanese Household Financial Assets Retain Absolute Level, Despite Highly Dependent on Deposits and Cash Equivalent

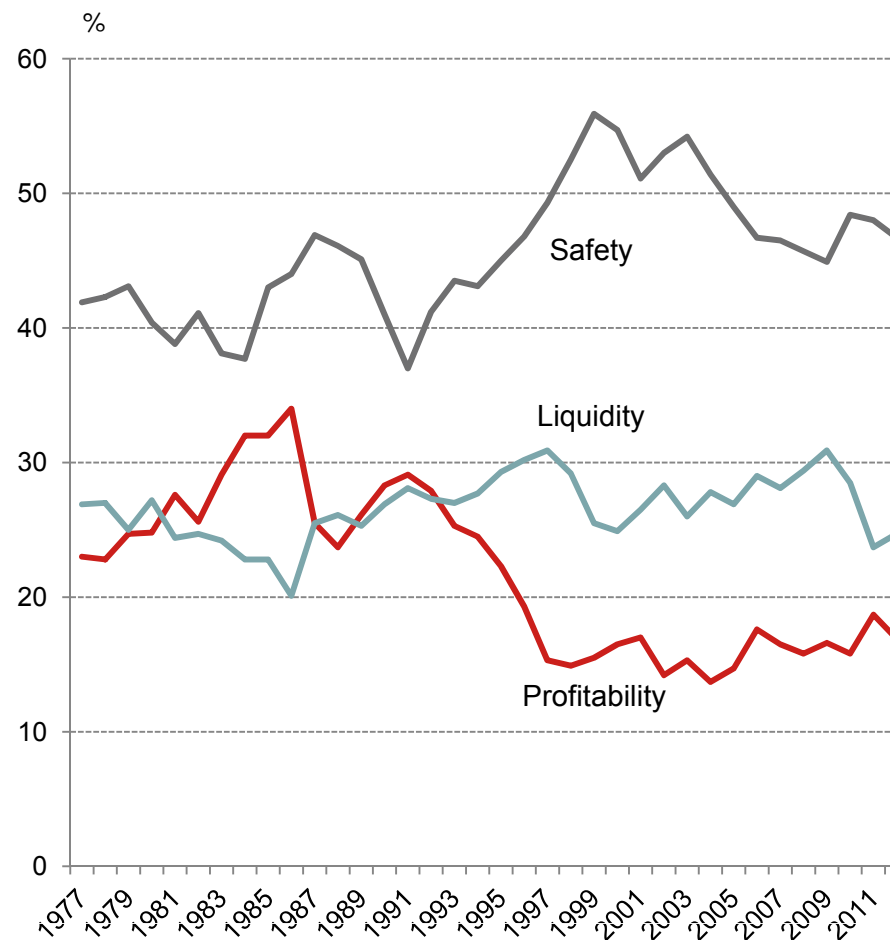
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Household Financial Assets in Japan (Level Data)



Source: NICMR bases on Bank of Japan

Criteria for Financial Products Choice  
(Household with Investment Experience)



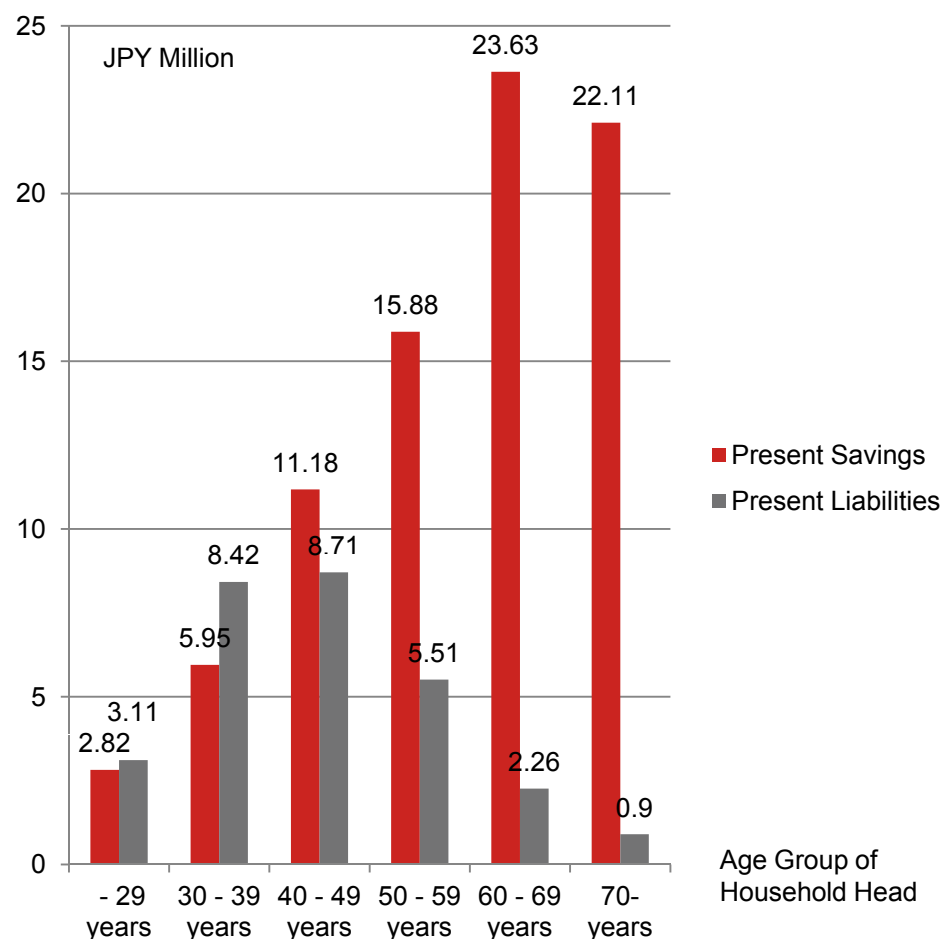
Note: Survey methods were revised in 2004 and 2007.

Source: NICMR based on The Central Council for Financial Services Information "Public Opinion Survey on Household Financial Assets and Liabilities"

# High Concentration of Japanese Household Financial Assets in Older Age Groups

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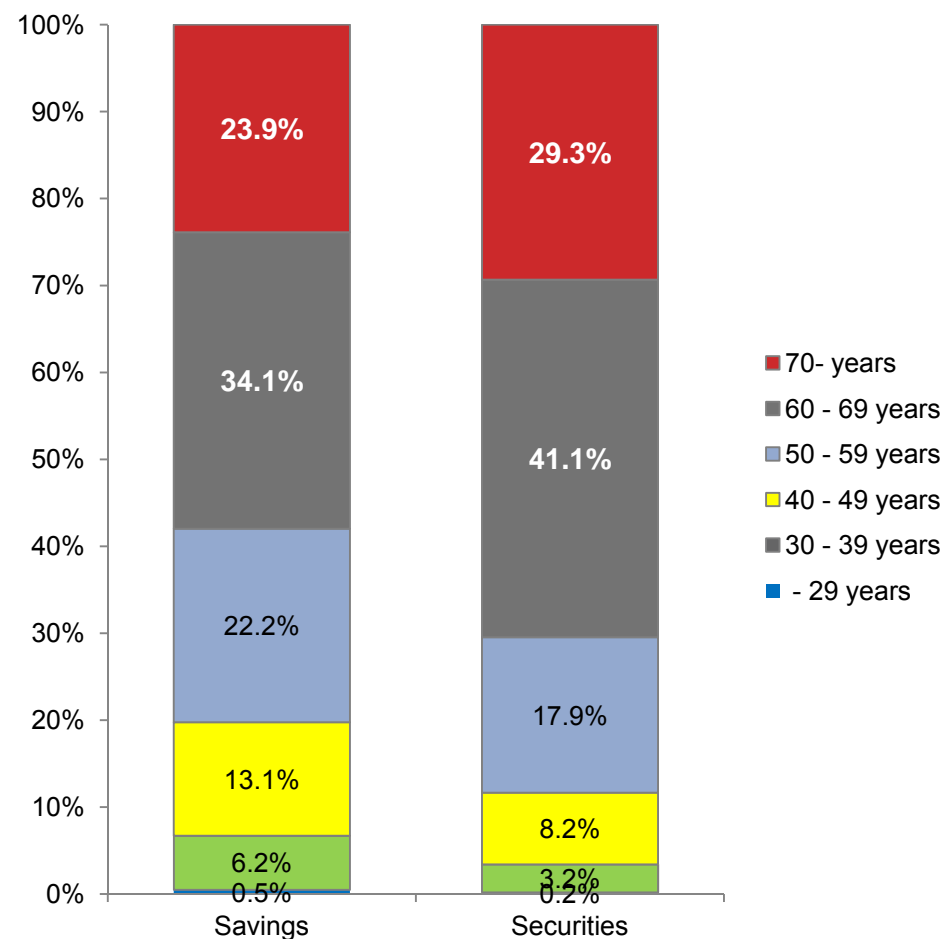
Average Household Savings and Liabilities  
(By Age Group of Household Head)



Note: Household with 2 or more persons

Source: NICMR based on Ministry of Internal Affairs and Communications "Survey of Household Economy" (2011)

Distribution of Financial Assets Holding by Age Group  
(Estimate)

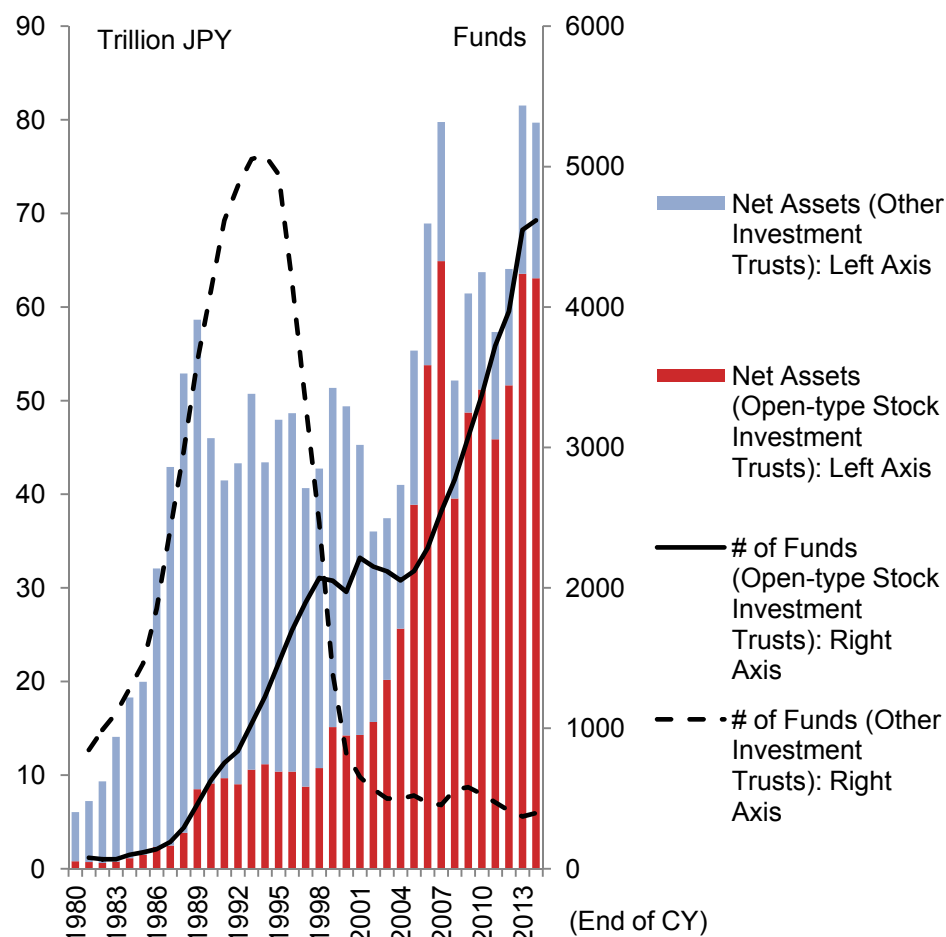


Source: NICMR Estimate based on Ministry of Internal Affairs and Communications "National Survey of Family Income and Expenditure" (2009)

# Structural Changes in Japanese Mutual Fund Market

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Increasing Assets of Open-type Investment Trust Funds



Source: NICMR based on The Investment Trust Association, Japan

Net Assets by Product Type of  
“Open-type” Stock Investment Trusts (February 2014)

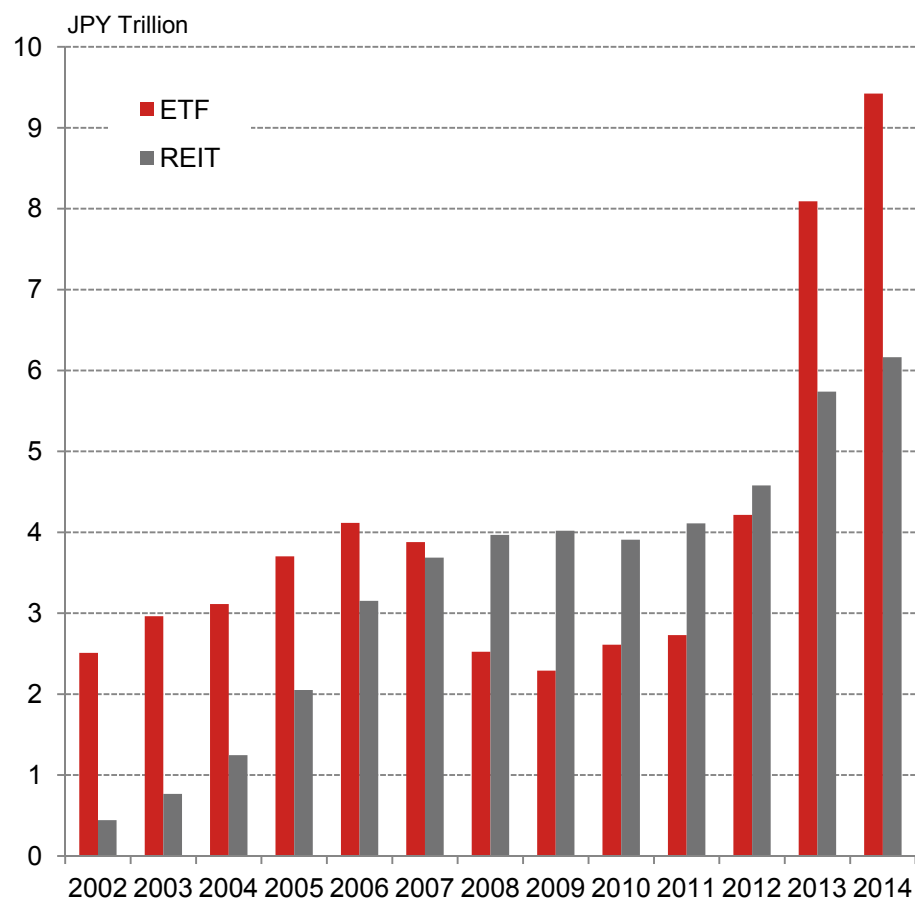
Feb-14			
	Net Assets (JPY Tril)	Share (%)	# of Funds
Domestic Stock Fund	4.4	7.0%	606
International Stock Fund	4.3	6.8%	631
Balanced Fund	14.9	23.6%	1,176
Monthly Distribution Fund	11.9	18.9%	386
Convertible Bond Fund	0.1	0.1%	7
Index Fund	10.2	16.2%	296
ETF	8.1	12.9%	114
Industry Index Fund	0.0	0.0%	9
Derivatives Fund	0.3	0.5%	77
Limited Open-Type Fund	0.4	0.6%	46
Fund of Funds	28.4	45.1%	1,769
REIT Fund	8.1	12.8%	250
Total-Open Type	63.1	100.0%	4,617

Source: NICMR based on The Investment Trust Association, Japan

# Diversification in terms of Asset Classes and Markets

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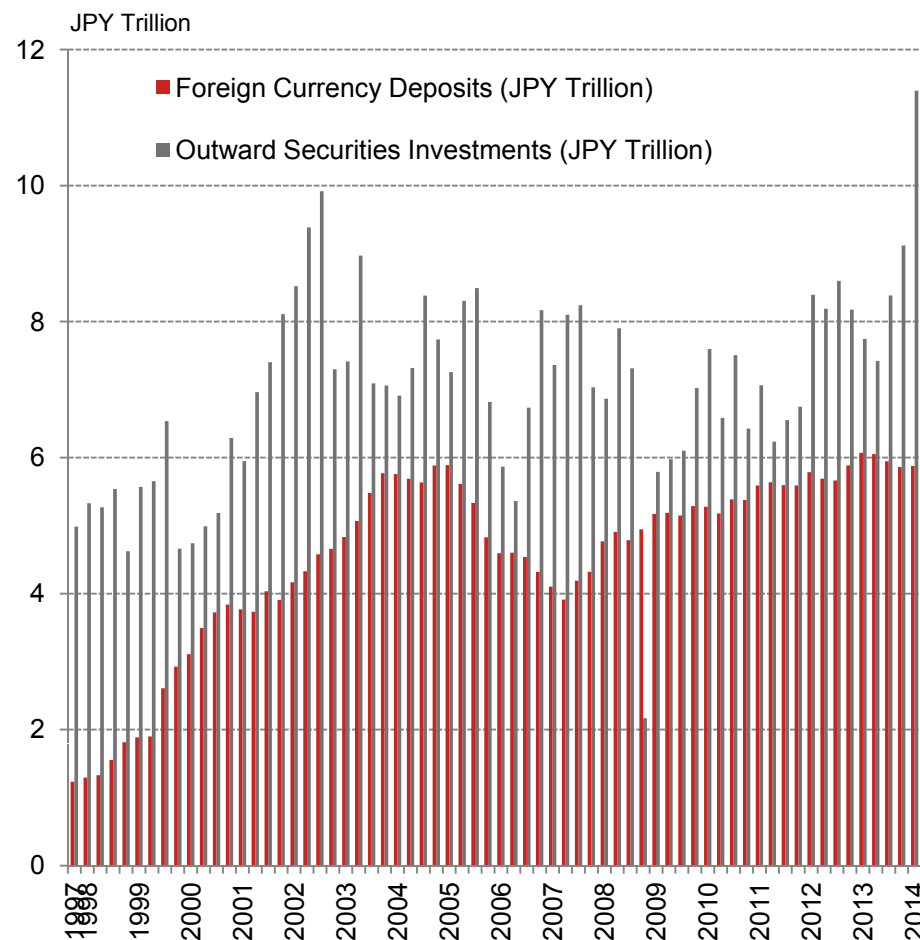
ETF and REIT in Japan: Change in Net Assets  
(End of Calendar Year)



Note: ETF data for 2014 is as of end of February. REIT data for 2014 is as of end of January.

Source: NICMR based on The Investment Trust Association, Japan

Household Sector in Japan : Foreign Currency Deposit and  
Securities Investment Abroad (1997 Q4 – 2014 Q1)

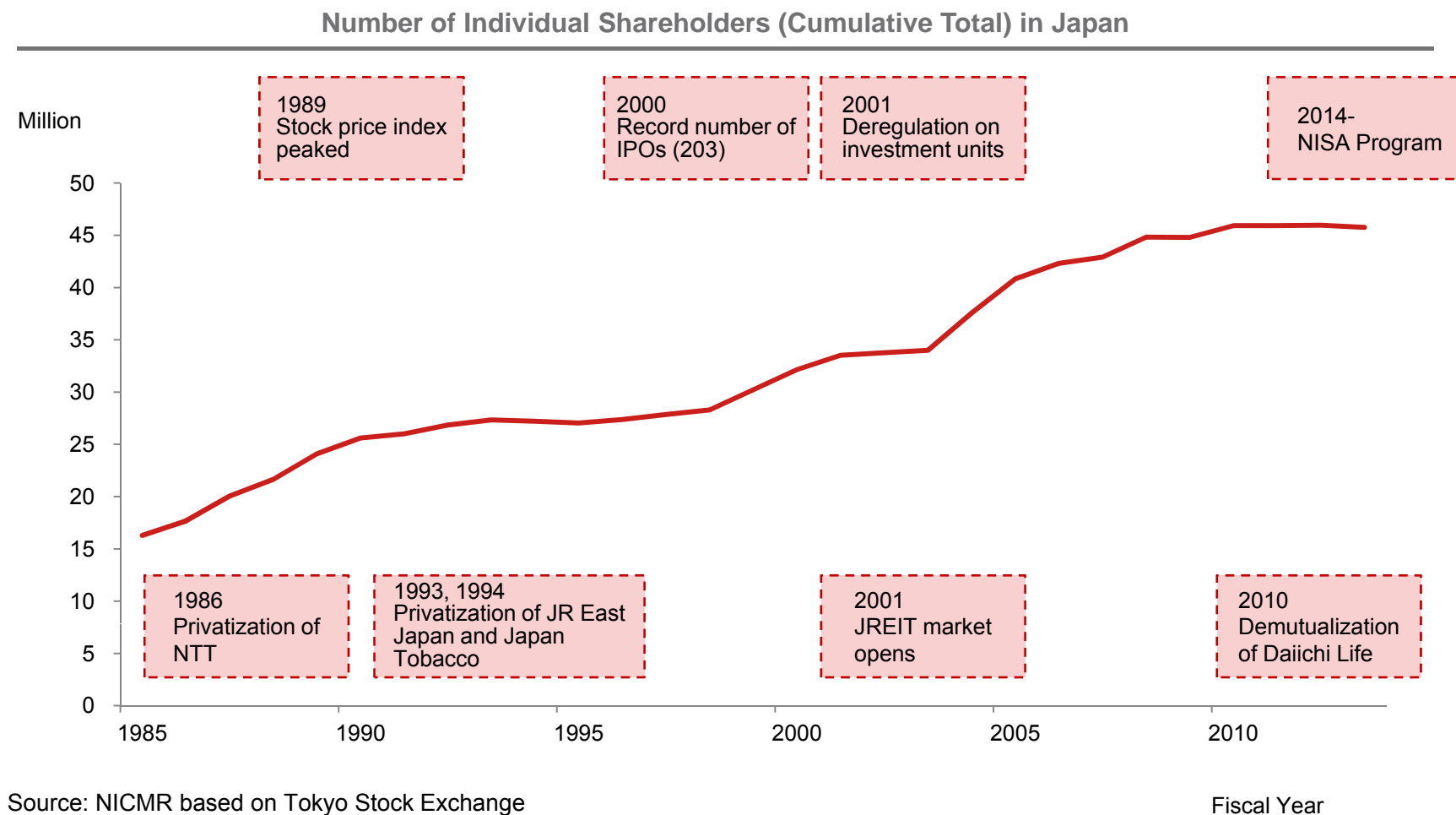


Source: NICMR based on Bank of Japan "Flow of Funds"

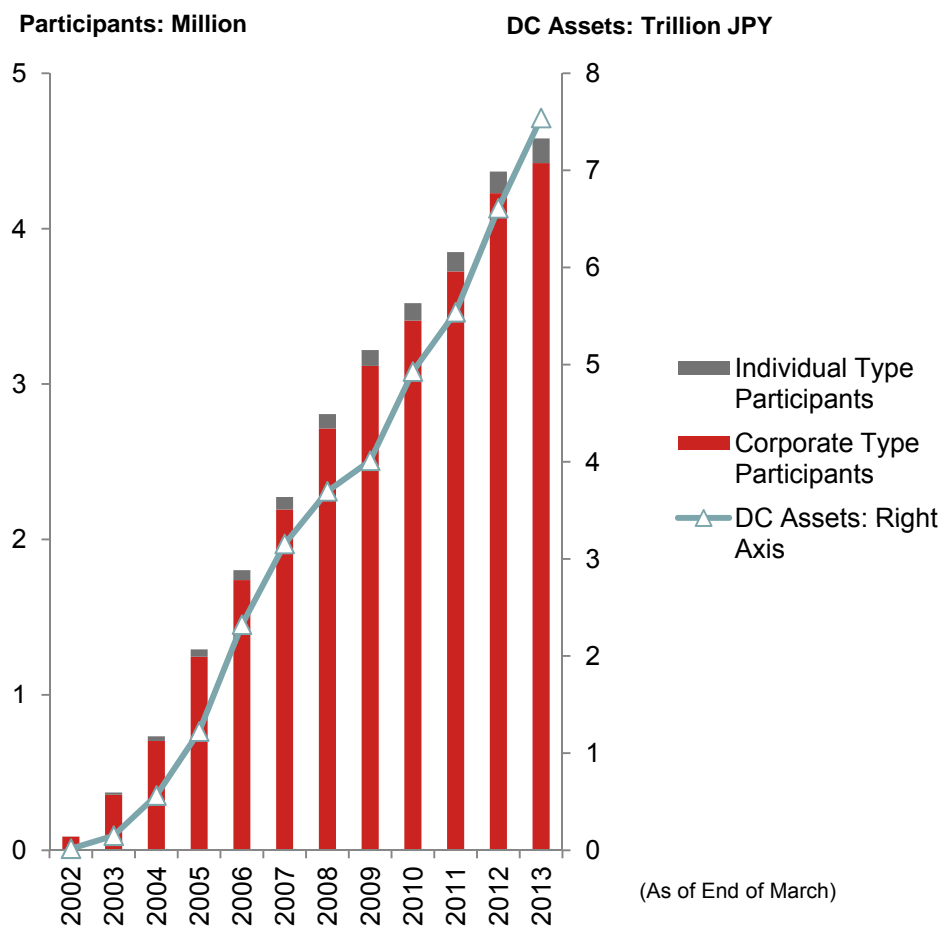
## Steadily Increasing Individual Investors

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- A series of privatization projects and regulatory reforms contributed the cultivation of individual investors

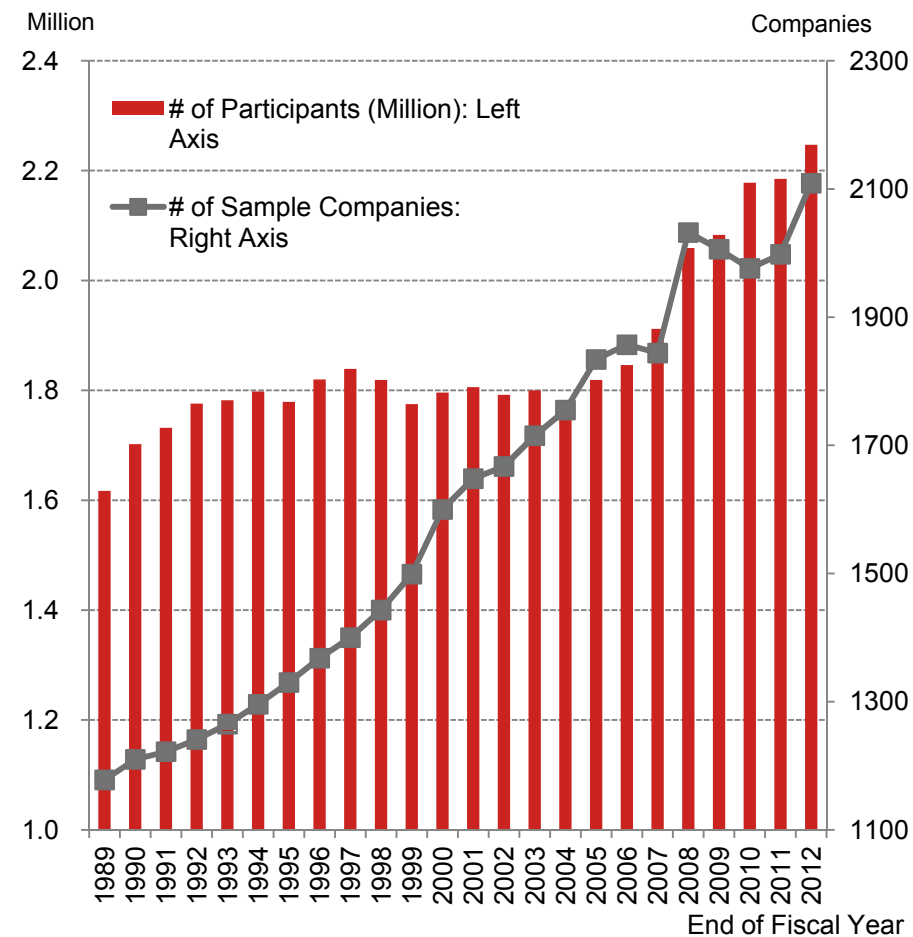


## Defined Contribution Pension Assets in Japan



Note: Numbers are the total of Corporate Type and Personal Type  
 Source: NICMR base on Association of DC Plan Administrators

## Employee Stock Purchase Plans in Japan



Source: NICMR based on Survey by Tokyo Stock Exchange

# Case Study: NISA (Nippon Individual Savings Account)

## What is NISA?

- On termination of the reduced tax rate from 20% to 10% imposed on income gains and capital gains of listed stocks etc. at the end of 2013, NISA was introduced in January 2014.
- Residents in Japan who are over 20 years old are able to open NISA accounts. Dividends and capital gains from invest in listed shares, stock investment trusts. Etc. are tax-exempt.
- The upper investment limit of NISA is one million yen per year (accumulated base:5 million yen).

## Outline of NISA

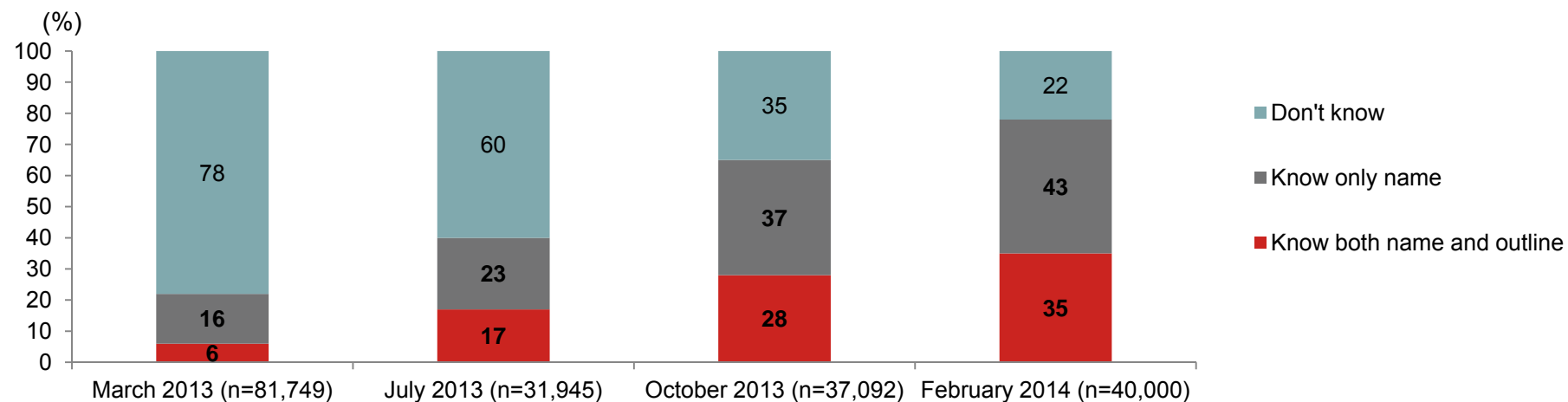
<b>Who is eligible?</b>	Anyone who lives in Japan and is at least 20 years old.	<b>How much can be invested?</b>	A maximum of ¥1 million (approx. US\$10,000) a year can be invested in a NISA up to ¥5 million (approx. US\$50,000) in total. (Unused portion of maximum ¥1 million investment of each year cannot be carried over to following years)
<b>What income is exempt from tax?</b>	Dividends and capital gains from investment in listed shares, stock investment trusts, etc. through a NISA.		
<b>Where can a NISA account be opened?</b>	It can be opened at securities firms (for investing in listed stocks, stock investment trusts, ETFs and REIT) and banks (only for investing in stock investment trusts).	<b>How long is the tax-exempt period?</b>	5 years at longest. After the 5 year period, the investor can hold onto the asset and invest up to ¥1 million yearly under the NISA scheme. Thus the scheme offers a total tax-exempt duration of up to 10 years.
<b>How many NISA accounts can be set up by one person?</b>	Only one.	<b>When can the assets held in the NISA be sold?</b>	Any time. However, if the assets are sold before the tax-exempt period of five years is over, the portion of tax-exempt capital used to purchase the assets cannot be reused within that period.



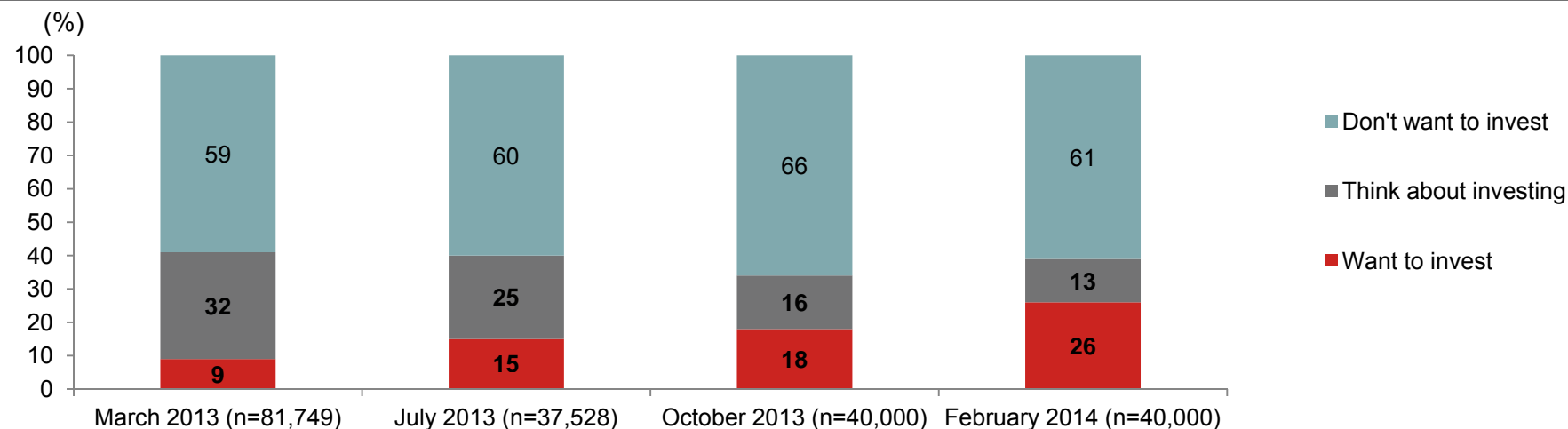
## Case Study: NISA (Cont'd)

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### Recognition of NISA



### Intention to Make Investments through NISA



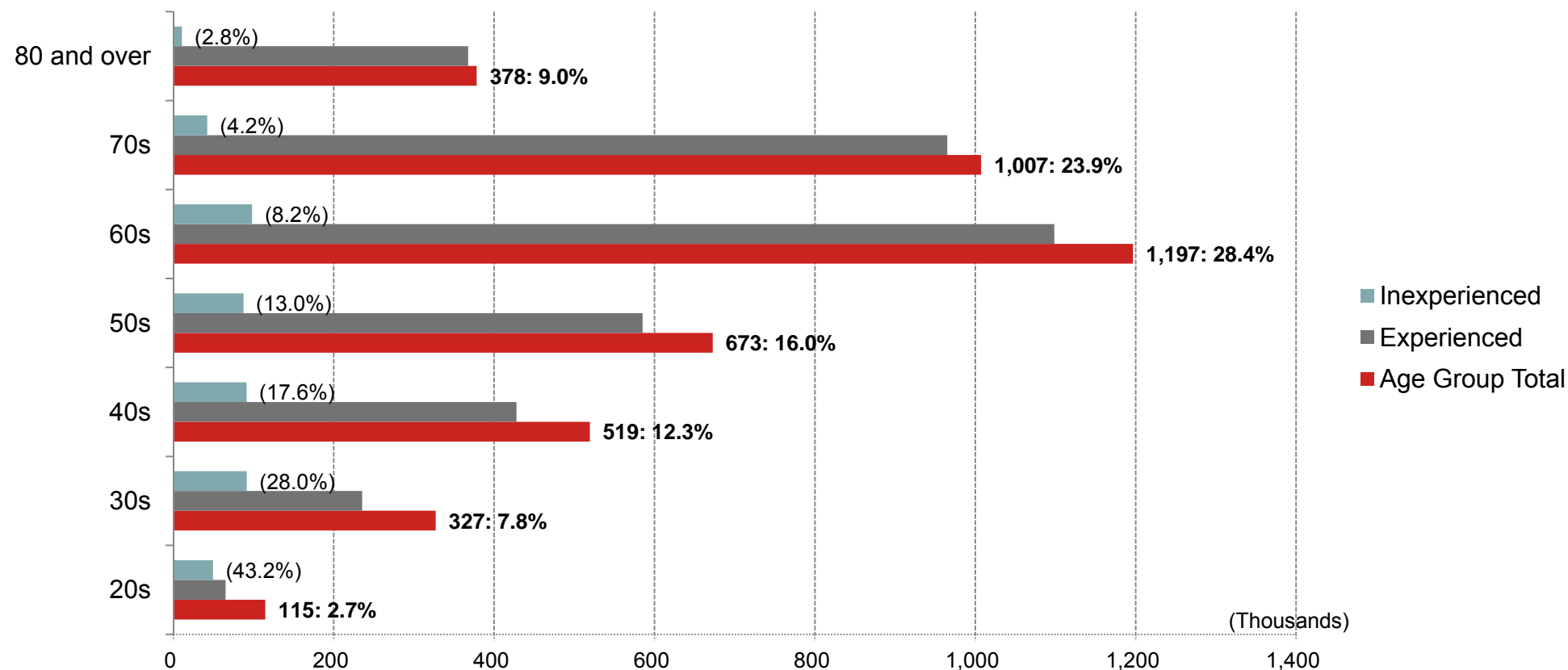
## Analysis for NISA Account Holders (As of March 2014)

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■ As of end of June 2014, the number of NISA accounts exceeded 7.2 million. It has been only for 6 months since NISA formally started.

■ However it seems the retired consists more than 60% of account holders. Also the inexperienced investors only consist 11.2% of NISA users.

### NISA Account Holders (at Brokerage Firms) Profile: By Age and Investment Experience



Note: The survey was conducted in March 2014 only for NISA investors with broker-dealers. Figures in parentheses indicate the percentage of inexperienced investors of each age group.  
Source: NICMR based on the survey by Japan Securities Dealers Association

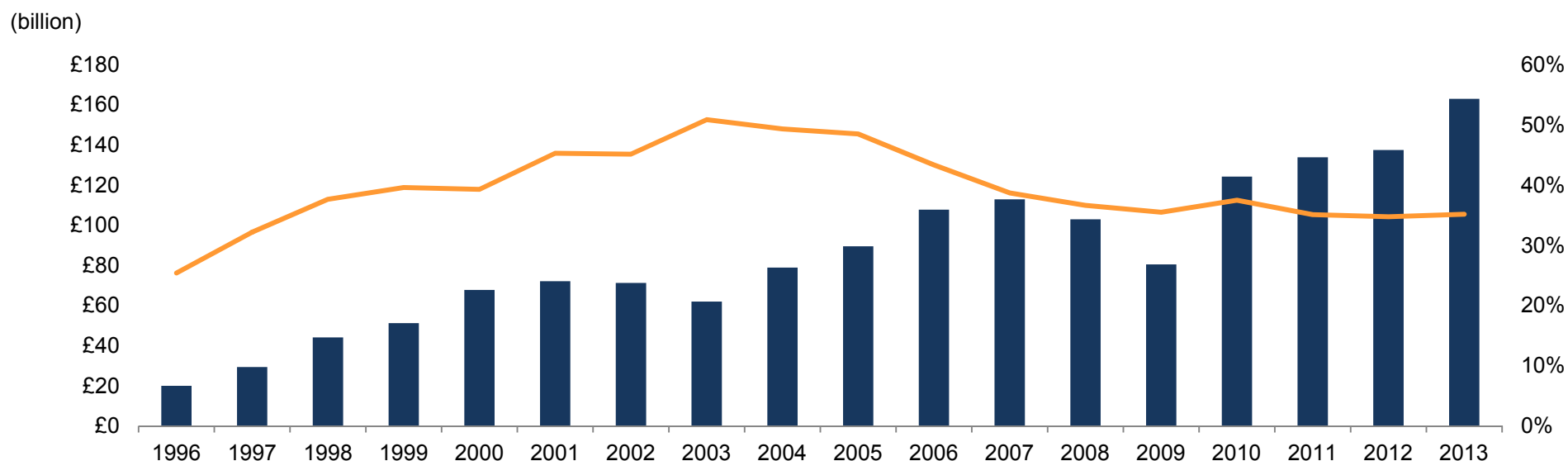
# Future of NISA and Needs for Revision

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## Future of NISA

- According to the government assumption, the fund size of NISA is expected to grow to approximately 25 trillion yen in coming 5 years.
- While the most investors in NISA today are elderly people who sold equity in 2013 to cope with the termination of reduced tax rate for income and capital gains, the target generation such as in 30s and in 40s are still in wait and see stance.
- UK ISA has been growing through several reforms including the change from temporary system to permanent, the introduction of Workplace ISA and Junior ISA.
- Japanese FSA started to discuss the introduction of “Child NISA” or other additional features on NISA

## Total Value of Funds in UK ISA and Percentage of Total Retail Fund Market



Source: NICMR based on IMA

■ Total value (LH)

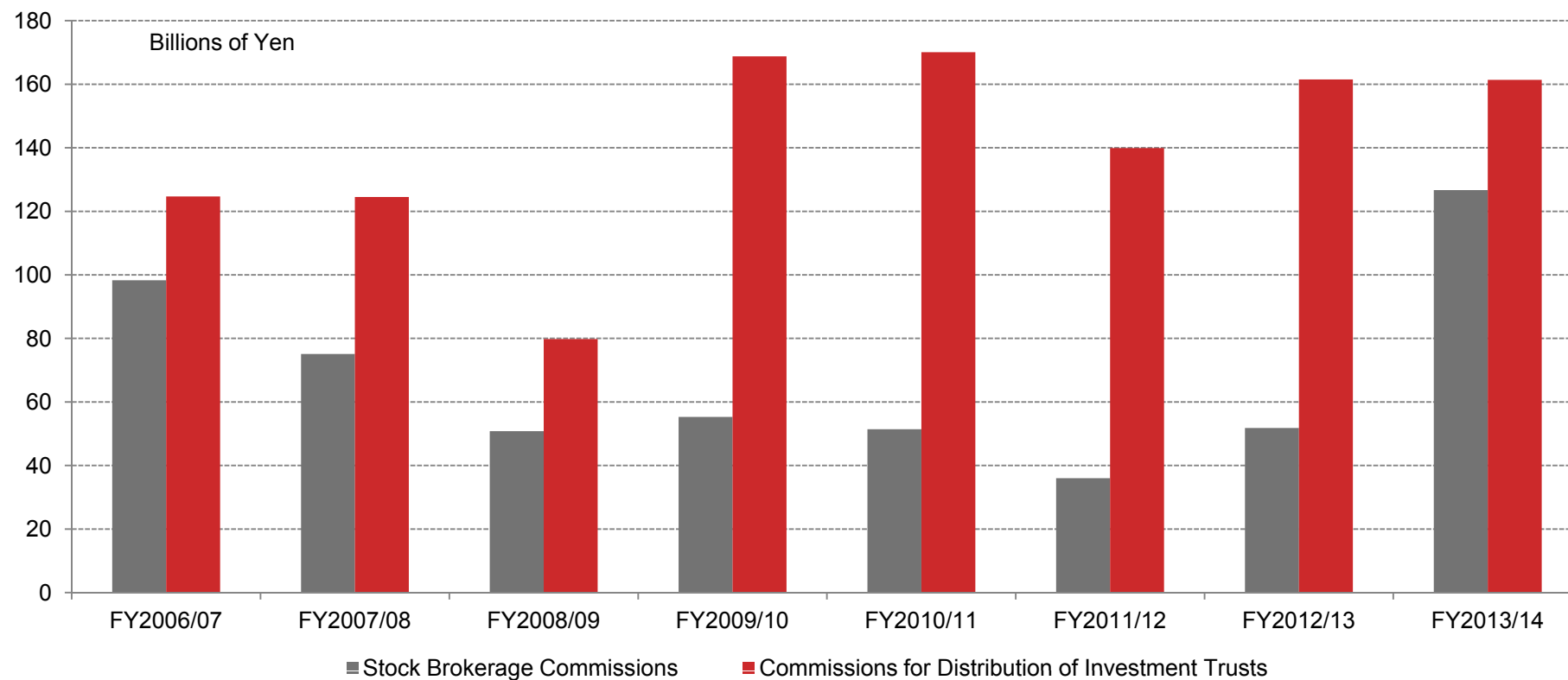
— Percentage of total retail investment (RH)

# Transformation of Retail Brokerage Business

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- Create synergies between wholesale(manufacturing of investment products) and retail(distribution) businesses
- At the same time, enhance consulting sales, wealth management, DC/employer related businesses for expanding investor base

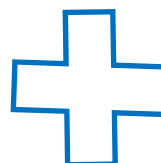
Nomura's Retail Division: Changes in Major Revenue Accounts



Source: Financial Results of Nomura Holdings

- Advices and Values Provided by Securities Firms: More Diversified and More Technically Demanding

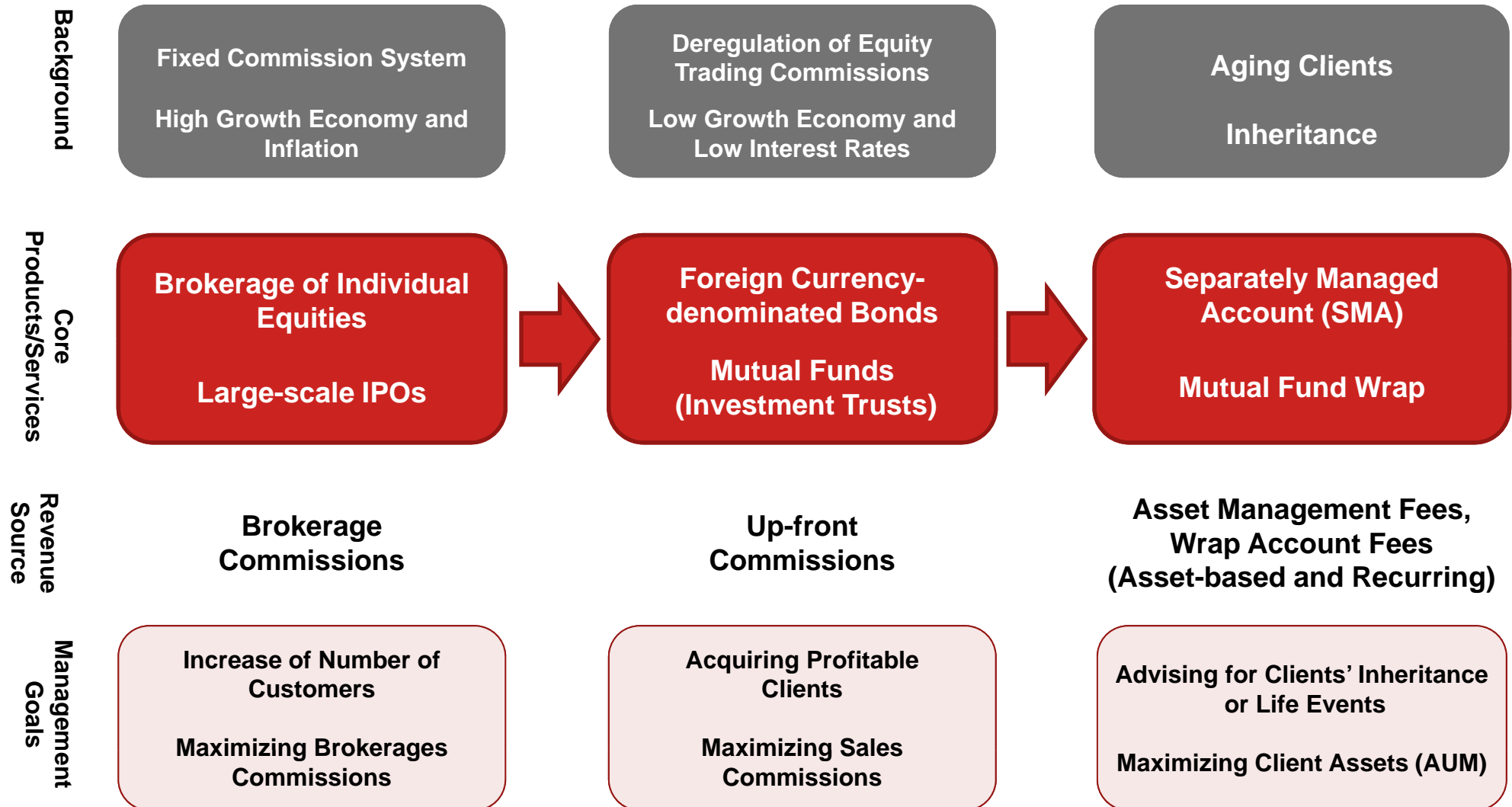
Major Business Types	Significances
<ul style="list-style-type: none"> <li>• Broker (Agent)</li> <li>• Dealer (Principal)</li> <li>• Underwriter</li> <li>• Offering/ Selling</li> </ul>	<ul style="list-style-type: none"> <li>• Capital formation/raising</li> <li>• Providing investment opportunities</li> <li>• Intermediaries of public securities market</li> </ul>



Major Business Lines	Significances
<ul style="list-style-type: none"> <li>• Retail (Distribution/Wealth Management)</li> <li>• Asset Management</li> <li>• Wholesale                         <ul style="list-style-type: none"> <li>– Global Markets (Equity/Fixed Income/ Derivatives)</li> <li>– Investment Banking</li> </ul> </li> <li>• Others (Banking, Trust etc.)</li> </ul>	<ul style="list-style-type: none"> <li>• Financial planning/consulting</li> <li>• Financial product manufacturing</li> <li>• Advisory/Providing solutions</li> <li>• Providing risk capital to economy</li> </ul>

# Historical Transition of Retail Investment Service in Japan

**NOMURA**



Source: NICMR