Financial Market Liquidity

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Government bond market

- Most liquid
- Little changed based on price based measures…
- …but quantity based measures point to more fragility

Our perspective

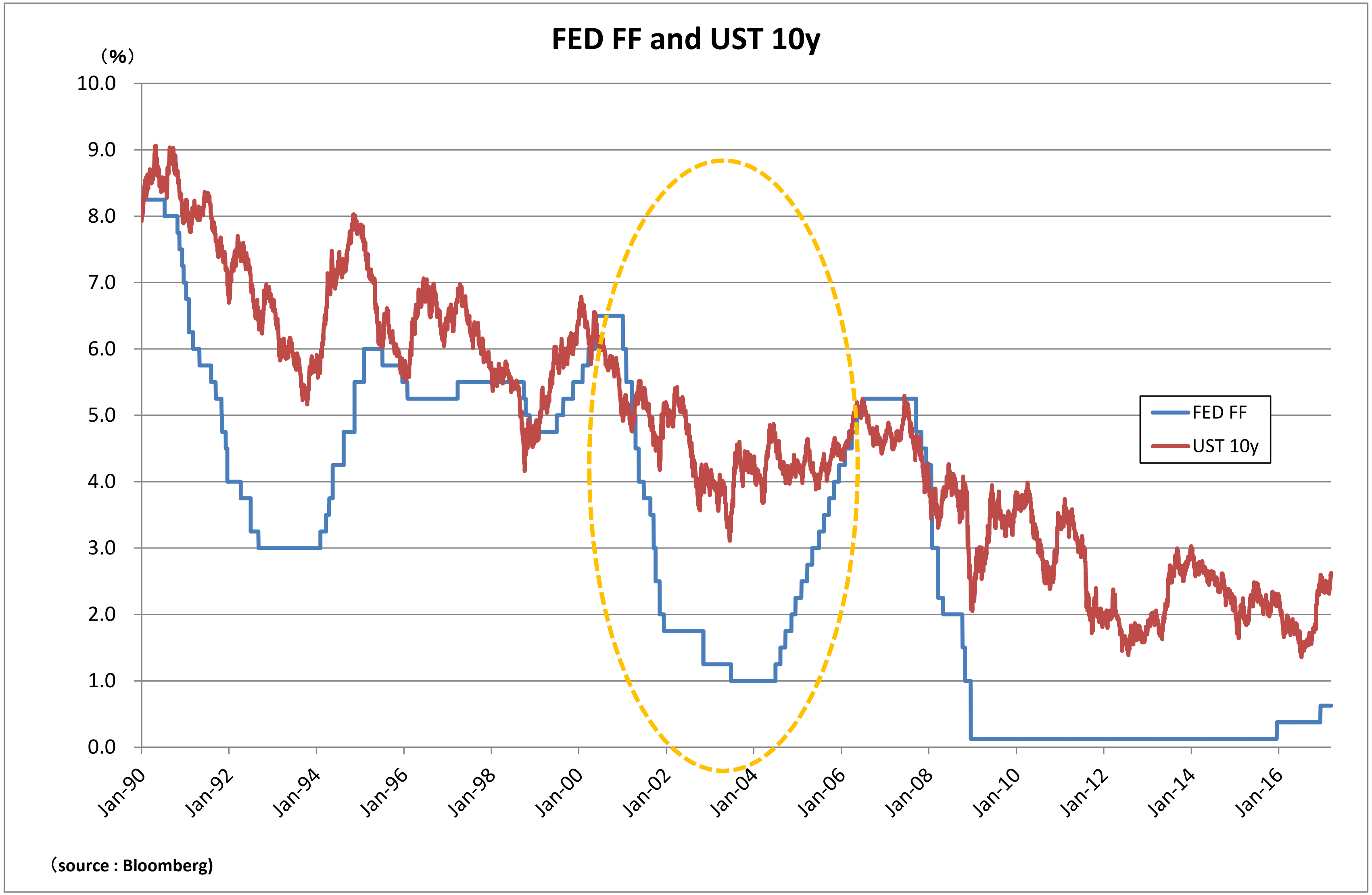
- Constraint
  - Operational capability
- Market
  - Bifurcation in liquidity
- Consequences
  - Diversification to be difficult

Market liquidity trends driven by…

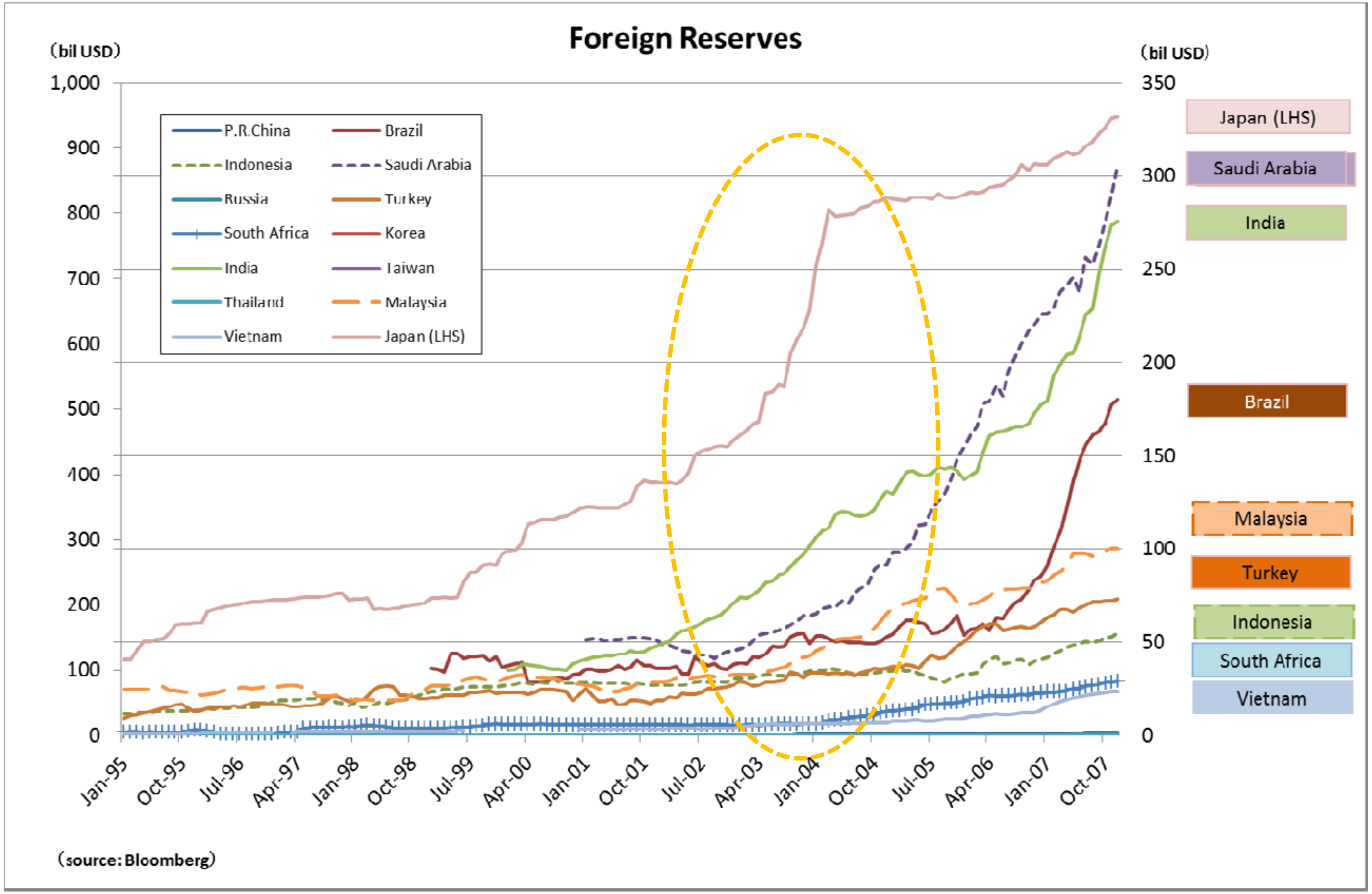
- Technology and competition
- De-risking continues amid tighter regulation
- Monetary policies

BIS, CGFS Papers No 55 Fixed income market liquidity, Jan 2016

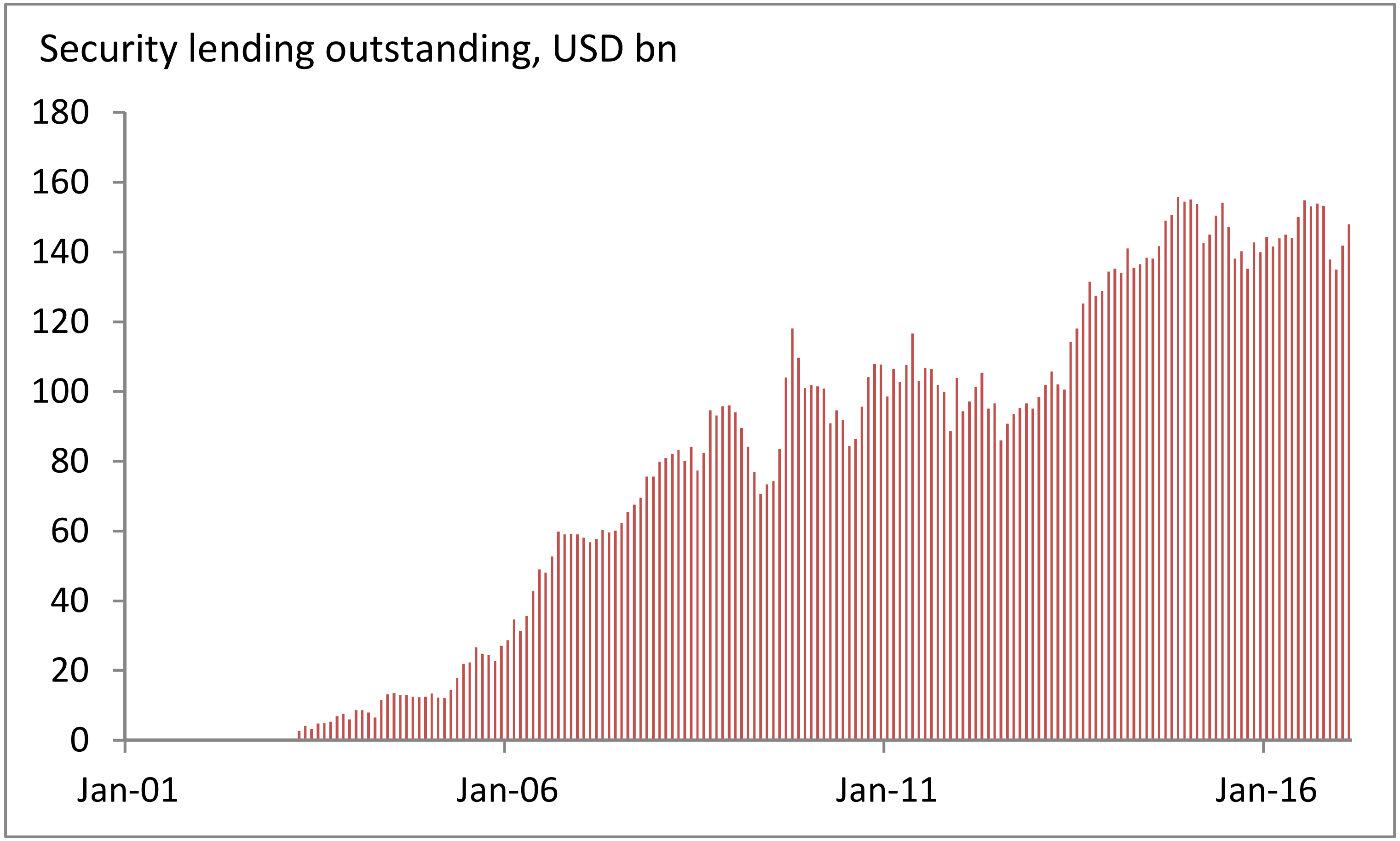
An example of 2003



Accumulation of foreign reserves play a part



Security lending



Our mandate

(Provisional Translation)

April 4, 2005
Ministry of Finance of Japan

Guidelines for the Management of Foreign Assets held in the Foreign Exchange Fund Special Account

The Ministry of Finance announces the fundamental rules for the management of foreign assets (foreign exchange, etc. under the provisions of Article 1 of the Foreign Exchange Fund Special Account Law, excluding the Special Drawing Rights and gold and silver bullion) which are held in the Foreign Exchange Fund Special Account (FEFSA) in terms of objective, principles, eligible assets, and risk management practices as follows:

1.Objective

The objective of the management of the FEFSA foreign assets is to ensure sufficient liquidity in order to be prepared for purchases and sales of foreign exchange, etc. needed to secure the stability of Japan's currency.

2. Principles

The principles under the objective are as follows:

(1)The foreign assets held in the FEFSA should be managed with maximum attention given to safety and liquidity. Under these constraints, profitability should be pursued.

(2) The foreign assets should be managed with maximum care to prevent any disruptive impact on financial or foreign exchange markets. The Ministry of Finance will maintain close communication with the relevant currency or financial authorities as necessary.

3. Eligible Assets

In each currency deemed necessary based on the objective stipulated in 1, the foreign assets should be invested in such bonds as central government bonds, agency bonds, supranational bonds, and securitized bonds which offer high liquidity and certainty of redemption; and in deposits in foreign central banks or domestic and foreign financial institutions which have high credibility and ability to provide liquidity.

4. Risk Management

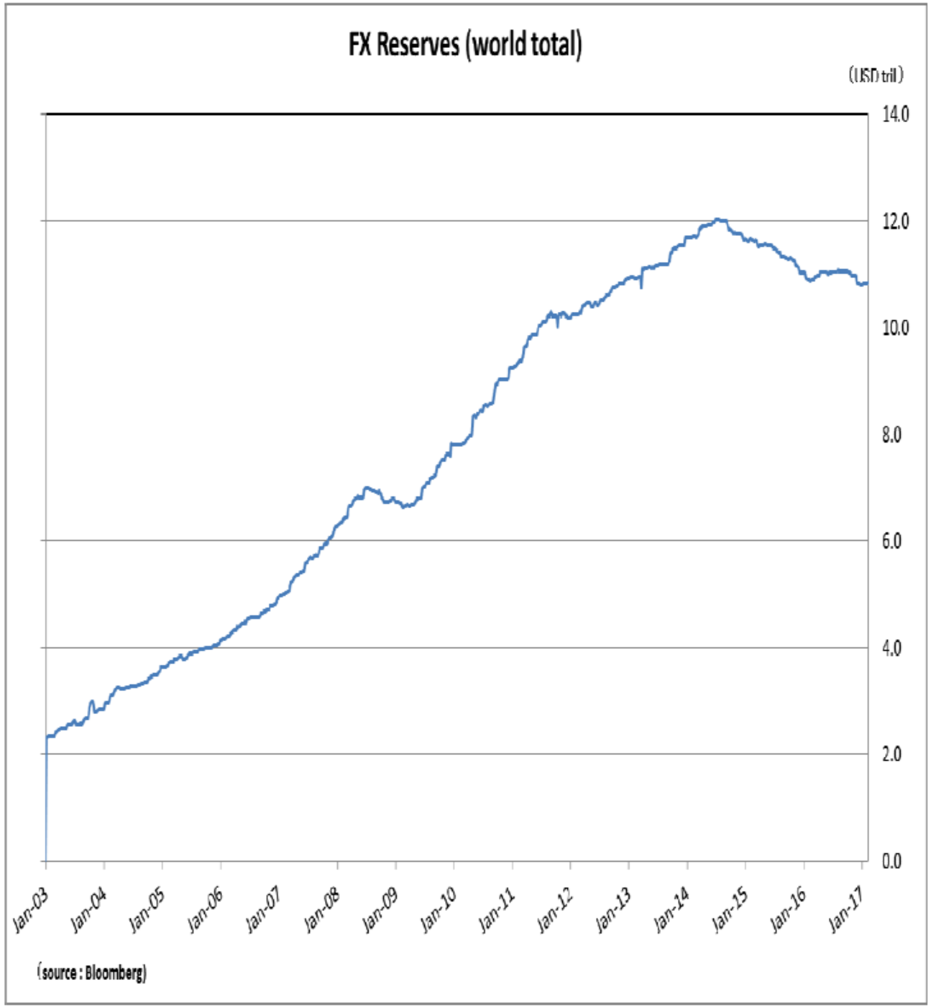
In the management of the foreign assets, risks should be managed appropriately based on comprehensive consideration of safety, liquidity, and profitability. The main risk management practices are as follows:

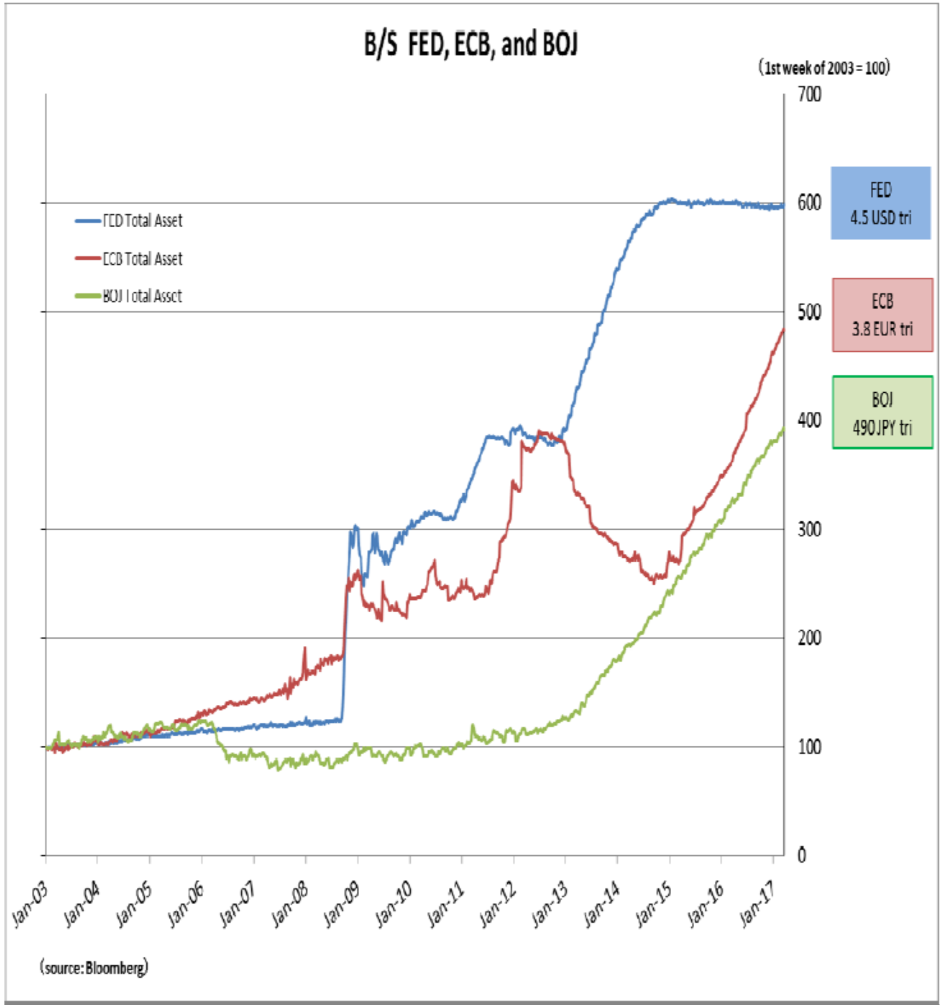
(1) Credit risk should be managed appropriately by using various ratings and financial statements for deposit institutions and bond issuers to ensure that the foreign assets are not exposed to excessive risk.

(2) Liquidity risk should be managed appropriately based on the objective stipulated in 1 in such a way that a certain amount of foreign assets can be converted into a form that is ready for settlements of foreign currency transactions within a very short period, at low cost, and with the least impact on markets.

(3) Interest risk should be managed appropriately referring to duration (degree of bond price changes corresponding to a given level of interest rate changes) and maturity structures of the eligible assets in markets to ensure that the foreign assets are not exposed to excessive risk from interest rate fluctuations.

What we can do





Thank you