FIA Japan Newsletter

September 2013

FUTURES INDUSTRY ASSOCIATION JAPAN

Regulatory Reforms Reshape the Industry

Topics of the month

Increased Volume and Broker Industry Reform in Japan

Korea : Soft Landing or Killing The Golden Goose?

Regulatory news

EMIR Implementation Update

CFTC Approves Cross-Border Guidance

Japan FSA Plans to Relax Short Selling Rules

People Interview

Peter Jaeger, Managing Director, Bank of America Merrill Lynch

“Views on Japan’s Uniqueness and Potential”

Peter Jaeger

FIA Japan

CONTENTS

SEPTEMBER 2013

So Far, So Good

Mitch Fulscher, Chairman, FIA Japan

Economic data released by the Japan Government at the end of August show a positive trend. Industrial output, job markets and wages, consumer prices, and spending are slowly moving in a positive direction. The housing market also shows improvement. On the political front, Prime Minister Abe continues to look strong as the LDP made it successfully through the important summer elections. Among the critical issues included in the government's "strategy for growth", the TPP trade initiative and the sales tax increase are moving forward in spite of expected political resistance. We can sense optimism in Japan. Even the number of overseas visitors significantly increased as Japan again appears on the international radar screen. It is still early, and there is still much to be done as a part of Abe's critical "3rd arrow" reform and restructuring. Reforms to help Japan develop its financial market into a regional financial center are an important part of that initiative.

Global Regulatory Movement

The US and EU regulators continue to move forward aggressively to expand their control over their financial markets. However, Dodd-Frank, and EMIR regulations affect not only their respective domestic markets but also reach out to business conducted in all other major financial markets. The extra-territorial implications of these regulations present a critical risk to the global markets. FIA in Washington (FIA W) and other associations recognize the urgent need for international regulators and governments to understand the potential damage to the global markets from the proposed rules and requirements. As a result, it has become imperative for these trade associations to coordinate their efforts and activities in order to be effective on an international basis.

In response to this need, FIA W is creating a structure to be in a position to meet this challenge. FIA W and the Futures and Options Association (FOA), based in London, announced an agreement to cooperate together through the formation of "FIA Global", an umbrella organization based in New York. FIA Asia will also participate in the new structure. The objective of FIA Global is to be knowledgeable and effective while taking consistent positions on international issues, and to be recognized by the international regulators as they promote the adoption of global best practices.

As this important new structure unfolds, we will study this development and discuss its implication for Japan.

"Peter Jaeger Shares Views on Japan's Uniqueness and Potential"

Peter L. Jaeger

Bank of America Merrill Lynch, Managing Director,
Asia Pacific Head of Futures & Options and OTC Clearing

Peter Jaeger is Managing Director of Bank of America Merrill Lynch and Asia Pacific Head of Futures & Options and OTC Clearing for Bank of America Merrill Lynch. He joined BofAML in December 2012 from JP Morgan.

Peter worked in Futures & Options for 15 years at JP Morgan, holding country head, desk head, and sales roles in Japan and London. Prior to that he worked at Bank of America Tokyo Branch as a Futures salesperson, from 1990 to 1997

Peter is a Director of the Futures Industry Association–Japan, a Director of FIA Asia and an Outside Director at the Tokyo Commodity Exchange. He chairs the Legal & Regulatory Committee for FIA-Japan and has served on various committees and working groups for the TSE, OSE, TFX, and Eurex.

FIA-J：Recently you joined Bank America Merrill Lynch. How have you found things there?

I joined Bank America Merrill Lynch eight months ago and it's been absolutely exhilarating. With the marriage of Merrill's equity research franchise to Bank America's deposit base, balance sheet and fixed income pre-eminence, BofAML boasts a very compelling story. The heritage Merrill exchange infrastructure where we are co-located at every major exchange in Asia, the HFT business my colleagues in our Professional Trading Strategies Group have built, and our Asian Prime Brokerage offering give us plenty more ammunition to become the leader in futures and options in Asia Pacific.

My mandate is to rebuild our Asia Pacific futures & options business, so my first priority has been to assemble a team of top players. To my delight, everyone in Asia Pacific is excited by what we're doing here at BofAML, and many of the best people in the street have joined me. Everyone we've hired has been my first choice, and no one to whom we've offered a position has declined.

"Consensus is key to change in Japan."

FIA-J：Bank America Merrill Lynch has been through some hard times. How is it doing now?

Over the past couple of years our CDS (Credit Default Swap) market rate has halved and our share price has doubled. Our colleagues on the Bank side in the US are making significant progress with the post-crisis issues. In F&O now, we're focused on growing revenue and market share. With Dodd-Frank, the futurization of swaps, the emphasis on CCPs, and the ascendancy of the CFTC as a global leader in the regulatory sphere, BofAML's senior management recognizes the importance of having a strong and truly global futures business. I believe that "the futures business model is the business model of the future".

A good futures business should be diversified across asset classes, client types, locations, and service types. Globally, the business needs a shared vision and shared systems to achieve unification. In turn, each region needs to carry its own weight and move the sail in the right direction to catch the local winds. Regional heads then need to direct their resources into the countries with the highest strategic returns.

I spent the first half of this year building the core of our sales and marketing team in Hong Kong, Singapore and Japan. We are active around the region, in Australia, India, Korea, Taiwan, Thailand, and Malaysia, to name a few. My colleagues in Operations and Technology are implementing new execution and order-routing capacity. The next step is to roll out the finished product to our pipeline of eager clients. Clients all want to deal with us, because they know we are building a first-class futures platform on a financially solid foundation.

FIA-J：How does Japan compare to (or differ from) other Asian markets?

Japan is home to some of the largest investors -- and some of the biggest futures users -- in the world. Japan is by far the largest modern economy in Asia with the largest pool of savings. The legal and financial infrastructures are both highly developed and there is due process and good protection for private property. But Japan is harder to navigate than commercial centers like Hong Kong or Singapore. It's more costly to operate a hedge fund in Japan than in Singapore, just as it's more costly to run a futures business in Japan. Corporate taxes are higher and labor laws are stricter. And almost all bureaucratic dealings must be done exclusively in the Japanese language.

The Abe government is trying to improve some of these areas, but it's unclear how much the voters buy into his rhetoric. Consensus is key to change in Japan. The willingness to support Abenomics could vaporize quickly if freer trade ends up hurting the Japanese consumer's wallet, if looser labor laws lead to rises in unemployment, or if a weak yen causes excessive inflation of essential imports such as gasoline.

FIA-J：There is a Japanese Government initiative unfolding to build a comprehensive exchange in Tokyo, which would be the leading exchange in Asia. Do you think the Government can achieve its aim?

Japan definitely has the technology, the talent, and the ability to build the leading exchange in Asia. The question again is consensus. If the legal framework is put in place to allow Japan's exchanges to meet the universal needs of investors throughout Asia and the world, and if the exchanges want to work together, I am optimistic. However, I don't think this aim can be achieved artificially, nor by government guidance alone.

"Japan definitely has the technology, the talent, and the ability to build the leading exchange in Asia."

FIA-J：Where do commodities markets fit in to the picture? How do you see it unfolding in Japan?

Commodity futures are clearly one of the key elements of any mature market. There are a million reasons why more and more investors and speculators want to trade derivatives on natural resources, foodstuffs, and for that matter unstoreable things like electricity, and uncontrollable things like weather. Japan is no exception. Japan's power producers are Australia's largest client for coal, yet almost no coal futures are traded in Japan. With 52 of Japan's 54 nuclear reactors still shut down, there should be even more need for power producers to hedge. But Japan's power industry has a system of price controls that discourages hedging. Futures on foodstuffs is a sensitive topic in a country whose government worries about self-sufficiency, and also in any country where agricultural interests are powerful. I think that Japan will gradually embrace hedging with commodity futures, but obstacles in tax and accounting laws need to be overcome before real progress can occur.

FIA-J：You have served on the FIA Japan Board for several years. What is your vision for our Association moving forward and, as Chairman of the newly formed Legal and Regulatory Committee, what are your plans for this committee?

FIA Japan will continue to be a unique and vital organization. Japan is unique in the world, but for centuries Japan has been adapting interesting and valuable things from overseas. All that means is that there is a Japanese way of doing things, and if you follow that way, you can get things done in Japan.   FIA Japan is a great example of a group that gets things done in a Japanese way.

In the Legal & Regulatory Committee, we look forward to tackling legal and regulatory obstacles to doing business here in Japan, in particular futures & options business. With the aim of promoting the Japanese derivatives markets, we can cover any aspect of financial law, commodities law, tax law, exchange rules, or the rules and regulations of SROs or other bodies, as well as government policies and initiatives. It is a large mandate but with everyone's collective experience and knowledge I'm sure we can make a difference.

FIA-J：Thank you for sharing with us your valuable input on these key issues.

Japanese and European Regulators Sign MoU on Funds

In July 2011 the Alternative Investment Fund Managers Directive (AIFMD) was enforced in Europe. Following this Directive's mandate for regulatory cooperation between various countries, FSA, METI and MAFF signed in July 2013 an information exchange agreement with 26 regulators from EU countries, including the UK and Spain. In Japan as well, the number of funds or fund managers from overseas has been expanding, while the number of Japanese fund managers who are active in Europe has also increased. The agreement makes it possible for regulators in each country to submit information upon request from a signatory regulator.

AIFMD specifies that any EU entity who is managing a fund on behalf of a non-EU entity or any fund that is sold/managed within the EU would fall under the scope of its regulations, even if said fund is a non-EU fund. Following the signing of the MoU, any fund that is managed in Japan but also sold in Europe, for example, could possibly fall under the scope of information request between the EU and Japanese regulators. Also, "on-site inspections would be permitted within the legal framework" of each country. However, METI commented that "the current MoU covers information sharing only. Any actions to be taken following a request for an on-site inspection would have to be further discussed".

The Japanese regulators are also signatories of the IOSCO information/collaboration agreement signed on May 9th 2011 between 80 countries throughout Asia, Europe and the US.

EMIR Implementation Update

The European Securities and Markets Authority (ESMA) recently provided more clarity on the cross-border application of the European derivatives regulatory reforms (commonly known as EMIR) by publishing a consultation paper on draft standards addressing extra-territoriality issues and took steps towards implementing the clearing obligation by proposing draft standards and enabling third-country clearinghouses to apply for recognition. Also, upon the passing of the September 15, 2013 compliance deadline, market participants will become subject to additional risk mitigation requirements.

For transactions between an EU entity and non-EU entity, EMIR essentially requires the trade to be cleared, if the non-EU entity would be required to clear if it were established in the EU, and imposes risk mitigation and reporting obligations on the EU counterparty. For transactions between two non-EU entities, ESMA has proposed that clearing and risk mitigation requirements, but not reporting, apply to such transactions when rules in those counterparties' jurisdictions have not been determined to be equivalent to EMIR and either: (a) one of the counterparties is guaranteed (above certain thresholds) by an EU financial counterparty or (b) both counterparties execute the transaction via their EU branches.

On the clearing front, before clearing obligations can be implemented, ESMA must first designate contracts subject to mandatory clearing, and draft standards for approval by the European Commission, European Parliament and Council. In that respect, in July ESMA published a discussion paper in which it sought market participants' views on related clearing standards. Also, for the clearing obligation to be implemented, ESMA must approve clearinghouses and certain clearinghouses established outside the EU, including the Japan Securities Clearing Corporation, have indicated their intention to apply by September 15 for recognition as a third-country clearinghouse. This recognition is necessary because market participants subject to EMIR will only be able to use non-EU clearinghouses if they have been recognized under EMIR.

With respect to reporting, market participants had expected that reporting obligations for interest rate and credit derivatives would begin in September or October 2013. However, ESMA recently announced that reporting for all five asset classes – interest rate, credit, foreign exchange, commodities and equity derivatives – is instead expected to commence on January 1, 2014. Additionally, ESMA has proposed to distinguish between exchange-traded and over-the-counter derivatives and only require reporting for exchange-traded derivatives beginning January 1, 2015.

Finally, on September 15 certain of EMIR's risk mitigation requirements will become effective and, as of that date, EU entities will be required to have procedures in place to achieve portfolio reconciliation and compression, as well as procedures for dispute resolution. To aid market participants in meeting these requirements, ISDA has developed the 2013 EMIR Portfolio Reconciliation, Dispute Resolution and Disclosure Protocol. EU entities will likely request their Japanese and other non-EU counterparties to adhere to the protocol so that EU entities can comply with those requirements.

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This update was prepared by the New York and Paris offices of Kramer Levin Naftalis & Frankel LLP. Please contact Fabien Carruzzo (fcarruzzo@kramerlevin.com) with any questions.

CFTC Approves Cross-Border Guidance

On July 12, the Commodity Futures Trading Commission approved the final version of interpretative guidance that outlines how the CFTC will apply Dodd-Frank regulations to cross-border transactions. The CFTC also approved an exemptive order that provides affected entities, including hedge funds falling under the U.S. Person definition, until October 10th to come into compliance with the panoply of rules promulgated by the CFTC under Dodd-Frank.

During the meeting, CFTC Chairman Gary Gensler stressed that the interpretative guidance is aimed at preventing risks taken abroad from flowing back to the U.S. To that end, the guidance is designed to make sure that foreign branches and guaranteed affiliates of U.S. banks cannot avoid compliance with Dodd-Frank rules unless they comply with comparable rules overseas. In practical terms, this means that these entities will not need to comply with certain CFTC rules if they comply with comparable rules in foreign jurisdictions, subject to a number of conditions and limitations.

The agency is now undertaking comparability determinations for six jurisdictions: Australia, Canada, the European Union, Hong Kong, Japan and Switzerland. These determinations will be based on whether those jurisdictions have requirements that are "comparable to" and "as comprehensive as" the equivalent requirements set by the CFTC.

Rice Futures: Test-listing Extended

The rice futures, launched on a trial-basis on the Osaka Dojima Commodity Exchange on August 8th, 2011 have been granted, on August 8th this year, a trial extension for two more years. The market size is still small, trading roughly one thousand contracts per day. Producers are still opposing the contract, amongst "fears that speculators could distort prices" (JA comment).

However, open interest has been increasing recently and major rice wholesalers have been entering the market. MAFF commented that "we expect the exchange rice price to become the benchmark in the future" and accordingly permitted the 2-year trial extension. The future of rice futures, though, really depends on how the market will develop in the next couple of years.

Japan FSA Plans to Relax Short Selling Rules

FSA is currently still planning to amend short-selling rules from November 2013. The rule change is to replace various ad-hoc regulations, such as the ban on naked short-selling. The relaxation of these rules is expected to greatly contribute to the development of the cash-equity market in Japan.

Topics of the Month

Increased Volume and Broker Industry Reform in Japan

2012 was a difficult year for all brokerage firms, with volume at a level far below that required for the industry to be sustainable. Both Japanese and foreign firms have actively closed business lines, sought to reduce costs and reduce headcount. By one measure, if volume on TSE falls below 1 trillion jpy per day traded, financial firms in Japan cannot sustain a level of fee income to offset their basic running costs. So the recent increase in volume, driven by the so-called Abenomics, is a welcome tonic.

But is the current volume increase sustainable, and does it augur better results for financial firms operating in Japan? Not necessarily so. Why not? Because the financial industry in Japan needs a long overdue productivity and capacity overhaul without which increases in volume will not be sustained.

Volume increase will only be self-sustaining over the longer term if they are matched with falling marginal costs to trade; and that can only be achieved with increases to productivity in the industry. If not, then investors will eventually run out of finding value because each successive trade does not become cheaper to process. Before the financial crisis, the Japanese financial industry was inefficient; Japanese firms used outdated technology and many relied on staff to process exceptions manually. Foreign firms built ‘duplicate’ infrastructure, one using local technology for local settlement, and the other was their foreign international systems they also put in place to connect to the rest of the world. This situation has not changed, in fact it’s gotten worse because since 2008 not only has the industry failed to maintain a level of investment to keep up with normal change, there has been active cost cutting disinvestment which has further reduced capacity.

So why is this different from the other major markets? Because in Japan the volume is so low it should be easy to process with the available technology. Consider that a large broker in Japan processing 25,000 transactions per day normally, might peak at 100,000 transactions and struggle to balance each day vs. the exchange. By contrast, the same firm’s brokerage operation in the US might easily process 1,000,000 per day, such that Japan seems backward by comparison. As a result in terms of costs, Japanese commission rates for investors may be 100 times higher than the level that could easily be achieved with technology and process improvements available today.

So what are the causes of the issue?

・Historically Japan has been dominated by software firms which charge for hosted service software on a per transaction basis, rather than on a per license basis. This means that there is no marginal decrease in cost for every additional transaction executed.

・There is dearth of skilled IT professionals providing in-house solutions for brokers. This has limited the ability of brokers to adapt and grow their business model without increasing costs.

・There is almost no price competition amongst Japanese software vendors; who prefer instead to keep prices for services, software and hardware far above identical services, software and hardware offered in other countries where vendors do compete.

・Brokers continue to maintain manual processes. This is linked to brokers’ continued use of outdated technology because of the false but widely held belief that Japan is different and can only be supported by a few incumbent Japanese software vendors.

Unless brokerage firms in Japan adapt, significant saving to investors cannot be provided. And unless savings are provided to investors, the volume increases will not be sustainable over the longer term. Additionally if firms do not invest in new technology and process improvements, then the industry will be capacity constrained, unable to absorb larger volumes in exactly the way that brokers could not cope with the post March 2011 earthquake volume; which should by any measure have easily been absorbed without problem.

Where firms do increase their investment in systems, those investments must be in automated systems and not simply paying more on a per transaction basis for the existing, outdated services. Without productivity and efficiency gains, the brokerage houses in Japan will fail to deliver cost savings to investors and investors will not grow their volume as a result.

This article reflects the personal views/analysis of Sean Lawrence and does not necessarily represent the official views of ABN AMRO Clearing nor FIAJ.

TOCOM Trading Platform: JPX Proposal

Japanese media reported in July that JPX group may have made an offer to TOCOM for the joint use of their Nasdaq-OMX powered derivatives platform, J-Gate, used by OSE. Both JPX and TOCOM have yet to make official comments on said proposal.

Currently, TOCOM also uses a Nasdaq-OMX trading system and has already signed a 5-year extension contract with the technology provider starting from fall this year, however, the cost would be substantially lower if TOCOM were to use the OSE platform.

In July, JPX Group consolidated the TSE and OSE clearing houses into JSCC, as well as consolidated their respective cash markets. The next planned step is the merger of their derivatives markets in March 2014, moving the Group closer the government‘s vision of a Comprehensive Exchange.

However, the missing piece for this vision to be complete is commodity derivatives. There are still many options open to JPX, including incorporating TOCOM under its umbrella, or listing its own commodity products. A decision has yet to be announced. On the other hand, TOCOM is also considering its own options, in a time when trading volumes have been shrinking. TOCOM CEO Ezaki commented: “Our main priority when considering our options will lay with the business opportunities we could expect.“ Accordingly, the exchange is also considering collaborating with overseas exchanges, including CME Group.

The impact of system sharing on future merger discussions is a major issue, and the focus now is on how TOCOM will respond to its alternatives.

Formation of FIA Global

The Futures Industry Association based in Washington (FIA W) and the Futures and Options Association based in London recently announced that they have reached an agreement to cooperate together through the formation of “FIA Global” an umbrella organization based in New York. FIA Asia will also participate in this new structure. This new organizational structure will enable the associations to take a global position on cross-border issues, substantially increase the coordination and information flow among regions, and provide a powerful global voice to express the views of members in Asia, Europe and the U.S.

FIA Global’s board of directors consists of the three chairmen of the underlying affiliates and nine individuals with global responsibilities named from the underlying affiliate boards. In addition, the chief executives of the underlying affiliates will serve on the FIA Global board and FIA’s President and CEO, Walt Lukken, will serve as FIA Global’s CEO.

FIA J Chairman, Mitch Fulscher, noted that “significant new regulatory changes, including Dodd-Frank and EU extra-territorial issues, have created many new problems and challenges for global market players. FIA’s reorganization will help to coordinate their efforts to better address such international issues. FIA J will study this development and discuss its implications as to how we may continue to cooperate with them in the future.

Korea : Soft Landing or Killing The Golden Goose?

The KRX Index has been in the spotlight recently for declining to 1.1 billion options projected for 2013 from a staggering 7.3 billion traded in 2011 and 3.1 billion in 2012. While still being one of the most traded contracts in the world, the Korean index options volume has dropped significantly more than the global worldwide option trading volume (which ’only‘ decreased by 15% in 2012). Volatility, once the hallmark of options in Korea, has also declined. The FIA Busan event was a great opportunity to look at what happened to this market.

Although a key reason for the drop was the re-engineering of the KOSPI market by the authorities in order to reduce retail investor speculation, there are some technology points for consideration which, if implemented, would facilitate market access and sustain foreign institutional investment.

・Order routing: Independent Software Vendors (ISVs) cannot connect to the KRX Application Programming Interface (API). Without native APIs, global ISVs cannot access and directly develop Front End program (FEP), therefore causing a major dependency on local vendors. This FEP architecture is not conducive to facilitating access to KRX Matching Engine.

・Market data dissemination: Koscom has full ownership of the distribution of market data and even their members are not allowed to distribute their own market data to foreign participants. This is a major drawback for foreign ISVs to connect global players, especially from developing trading centers such as China.

・Infrastructure: Any server connected to the exchange must be hosted by a member. This setup rules out co-location and ASP services, which are widely in place across the globe. Moreover the Korean market access infrastructure is split between two centers, Seoul and Busan, which duplicates costs. In fact, trading derivatives means getting market data from Busan and routing orders from Seoul: two access points, two separate data centers, twice the costs.

One of the key aspects of the Busan FIA Asia event was to encourage local brokers to evaluate the buy vs build option: Korean FCMs should consider benchmarking their internal costs against ISV product offerings.

Guillaume Roux-Chabert
Patsystems Tokyo

Committee Activities

FIAJ Reorganizes its Committees

Following recent industry developments, such as the development of the comprehensive exchange, we have reorganized our standing committees' structure to be based on a functional approach rather than an industry-segment approach. As a result, the following committees have been created: Market Development Committee (focus on encouraging the growth of our markets), Legal & Regulatory Committee (mandated to cover not only governmental-level laws, but also SROs etc.) and Market Operations Committee (to cover exchange and CCPs procedures etc. and tackle any inefficiency). All three committees, as well as the Technology Committee, are actively recruiting industry professionals that wish to contribute to their respective objectives (contact: editor@fiajapan.org).

Legal & Regulatory Committee   Chairman Peter Jaeger

The newly formed Legal & Regulatory Committee (L&RC) will examine Japan's laws & regulations and monitor proposals by regulators and SROs, then prepare responses as appropriate with a focus on helping to identify and remove legal or regulatory obstacles to doing business in Japan. L&RC will work with our partners at regulators and SROs to maintain and enhance FIA-J's communication and relationships with them. We will work closely with other FIA-J committees and external groups to bring about progress in Japan, in keeping with FIA-J's aim of promoting Japan's listed derivatives markets.

L&RC has a very broad mandate, in that we can cover any aspect of financial law, commodities law, tax law, exchange rules, or the rules and regulations of SROs or other bodies, as well as government policies and initiatives.

Members: Peter Jaeger – chair (BofAML), Naoki Kurumada (Dot Commodities), Rebecca Weinrauch (Getco), Mike Ross

(OMGEO), and Koichiro Ohashi (White & Case).

Market Development Committee   Chairman Yoshio KUNO

The missions and mandates given to MDC are various, wide and virtually deal with anything related to help develop, promote and /or improve the market regardless of the underlying. At a recently held kick off meeting, we've made an initial review of the few agendas which were succeeded from our legacy committees. The agenda includes HFT, pre-execution risk control as well as promotion of commodity options.

While there are many other issues we listed, such as market promotion/education, SEF (Swap execution facility) and so on, we have decided to start with the HFT-related agenda to study and share the issues surrounding HFT with our members. We plan to coordinate with the Technology Committee which could provide valuable input from an IT point of view.

Currently, MDC consists of Messrs. Kurumada (Dot Commodity), Onosato (TOCOM), Yanakawa (Citi Bank), Kobayashi /Watanabe (Nomura Sec.) and Mogi (Nissan Century Sec.) as an adviser.

Technology Committee   Chairman Bruno Abrioux

FIA-J Technology Committee has now finalized the priority topics to work on based on the survey among its committee members and FIA-J Board members. In priority order, the following themes will be studied:

1) Standards: what to know about Japanese standards comparing to world standards when establishing a business in Japan. The intention is to create on a regular basis a series of whitepapers, each dealing with a specific set of standards.

2) Recommendations to Japanese Exchanges on what to improve to ease technical access to their respective markets. This topic will be a direct follow-up and deepening of the work initiated by the Market Operations Committee dealing with themes such as connectivity to exchange, co-location offers, test environment ease of access…

3) Straight-Through Processing ("STP"): How can technology simplify the overall life cycle of advanced STP while improving solution TCO (Total Cost of Ownership)? Starting from a generic trade life cycle, the committee will zoom in on specific areas where solutions improve effectiveness and through STP.

As a next step, those priority items will be subdivided on working threads where FIA-J Technology Committee welcomes any experts and thought leaders who want to directly contribute to the discussion. Appropriate presentation format (roundtable, whitepaper, webinar…) and target dates will also be confirmed within the next monthly committee review.

In parallel to these three priority themes, FIA-J Technology Committee will also support the working thread of the Market Development Committee on the "Impact of HFT". Last but not least, the committee targets to run a technical follow-up checkpoint on the coming Tdex+ / OSE OM merger and TFX system change that will keep IT teams busy in the coming months until their go-live, respectively set for March and February 2014.

Exchange News

JPX

OSE Night Session Liquidity Improvement Program

OSE implemented a program aiming to improve the liquidity for trading of Nikkei 225 Options during the Night Session, for the period from August 2013 to February 2014.

Through this program, OSE asks for the cooperation of designated Transaction Participants to actively provide liquidity during the night time period (from 8 p.m. to 3 a.m. the following day), in order to facilitate trading in Nikkei 225 Options.

Outline of Newly Developed Index

JPX along with Nikkei Inc. ("Nikkei") announced the basic concept of a new index, which is currently being jointly developed. The new index focuses on the importance of corporate management from an investor’s viewpoint, with a special awareness over capital efficiency and profitability. Its constituents are selected based on corporate performance indicators and data, such as ROE, as well as the stocks’ market liquidity.

The new index will be composed of issues listed on the JPX cash equity market and will measure shifts in market capitalization to reflect changes in the corporate value of the selected constituents. A list of constituents and their selection criteria is scheduled to be released in fall this year. JPX and Nikkei aim to commence calculation/publication by the end of the year. JPX and Nikkei expect the new index to serve as a new investment benchmark for domestic and overseas investors.

Integration of Clearing Organizations under JSCC

Following JPX’s integration process, OSE’s derivatives clearing organizations were integrated into Japan Securities Clearing Corporation (JSCC) in July 2013. JSCC is now the Central Counter Party (CCP) for both TSE Derivatives and OSE Derivatives, unifying margins for Futures and Options and integrating operations for margin and fund settlement.

Furthermore, on June 25, 2013 the Boards of Directors of both Japan Securities Clearing Corporation (JSCC) and Japan Government Bond Clearing Corporation (JGBCC) announced resolutions to conduct a stock swap agreement and a merger agreement to be effective on October 1, 2013. Following the merger, JSCC will expand its range of clearing services to include Japan Government Bonds.

JPX to Re-launch Super-Long-Term JGB futures

JPX announced its decision to re-launch Super-Long-Term (20-year) JGB futures (SL-JGB futures) based on JGB market conditions and discussions with investors. The re-launch is scheduled for April 2014, following the integration of the TSE’s and OSE’s derivatives markets.

SL-JGB futures were listed on TSE in July, 1988, but were suspended due to little demand. JPX has determined, however, that the demand for SL-JGB futures is expanding in the context of an increase in issue amounts and trading volume of Super-Long-Term JGBs in the cash market.

TSE to Publish New Indexes

In response to the various indexing needs of its market participants, TSE will begin calculating and publishing the “TOPIX Ex-Financials” which excludes ”Banks”, ”Securities and Commodities Futures”, ”Insurance“, “Other Financing Business” sectors from TOPIX.

TSE will also begin calculating and publishing the “TOPIX Net Total Return Index” and “TOPIX Net Total Return Currency Hedged Index” to meet the market demands of capturing the Net Total Return Indices which are calculated in consideration of tax on dividends.

These indexes will be published from September 2, 2013.

TFX

Click Kabu 365 Promotional Campaign

TFX will begin a promotional campaign for Click Kabu 365 aimed to acquire new clients. For four straight months, from September 1st until the end of this year, TFX will offer a JPY 2,000 present in cash for newly opened trading accounts that trade at least three contracts of any Click Kabu 365 indices within a month from the account opening.

Planned Incentive Scheme in Euroyen Futures

TFX is considering a transaction incentive for the back-months contracts of the Euroyen Futures, which would start in mid September. Currently trades of EY futures are concentrated in the nearer term contracts - over 90% of the transactions are dominated by the first four contracts. The contents of the incentive scheme are (1) introduction of market-makers and (2) payment of financial incentive for transactions in the 7th and beyond contract months.

TOCOM

Phillip Securities Japan Acquires Agricultural Product & Sugar Market Membership

In July, Phillip Securities Japan acquired Broker Membership in TOCOM's Agricultural Product & Sugar Market. The firm is the Japanese subsidiary of Phillip Capital, a major Singapore-based financial institution. Phillip Securities Japan has traded precious metals, oil and rubber as a TOCOM Broker Member since May, 2012.

TOCOM expects that this new membership will bring a new set of international customers, including investors and commercial hedgers, which will connect to the Agricultural Product & Sugar Market (launched in February 2013).

Future Events

FIA Japan "Cool-Off" Summer Party – Sep 10

Our annual "Cool-Off" Summer Party will be held at the exclusive Ark Hills Club on Tuesday, September 10. Under the leadership of the new board, FIA Japan has been active and we wish to discuss with our members how we can further enhance the role of our association, while enjoying cool beer at the end of a very hot summer!

To participate, please contact our Executive Secretary, Ms. Ogawa (ogawa@fiajapan.org).

SFOA / FIA Conference (Burgenstock Conference) – 25-27 September, Geneva Switzerland.

The Swiss Futures and Options Association and the Futures Industry Association are pleased to announce the Global Forum for Derivatives Markets, September 25-27, 2013, at the InterContinental Hotel in Geneva. Also known as the Bürgenstock meeting, now in its fourth decade, the forum has a long history of attracting distinguished speakers and prominent names from the economic, academic and political worlds for high-level debate and discussion. The conference has proven to be an ideal forum for encouraging closer cooperation among market participants and international regulators.

Market Forum – 8 November, Tokyo

The 9th Annual Market Forum event will be held at Otemachi Sankei Plaza on November 8th. It is a gathering of around 400 participants mainly coming from the local trading community. As registration has started in September, please visit the website of the organizer if you are interested.

NPO Japan Financial Security Industry Market Forum.

2014 FIA-Japan Tokyo Conference

FIA-J is currently working on a plan to hold a Tokyo conference in 2014, targeting the month of October. The theme of the conference is "Tokyo – Regional Financial Center". More details will be made available as our Conference Task Force moves forward with the programing, venue, etc.

Start marking your calendars!

Tech Corner

arrownet-Global: gateway to JPX Co-Location

On July 10th, FIA-J Technology Committee Chairman attended the 7th annual edition of TradeTech Japan. Among various presentations, the "arrownet-Global" solution developed by NTT Communications Corporation (NTT Com) in partnership with Tokyo Stock Exchange (TSE) came as a striking business-enabling initiative. In a nutshell, "arrownet-Global" allows trading participant based in Singapore or Hong Kong to reach directly the Japan Exchange Group (JPX) Co-Location, located on arrownet, through a highly-reliable and ultra-low-latency network. It is also to be noted that TSE connectivity service can be extended as far as Chicago for US-based trading participants.

When asked what benefits this solution launched in April 2013 brings to the overall financial community, Hosokawa-san from NTT Com answered: "Low Latency and reliable network are crucial to the success of financial industry clients. NTT Communications expects that our partnership with TSE and the launch of arrownet-Global will be part of the initiatives to ensure that our clients enjoy the lowest latency, highest reliability and capacity." Hosokawa-san continued: "arrownet in Japan has been a highly reliable low latency network service offered by TSE since 2009, for financial service institutions to connect with its trading/information systems and also co-location racks in Tokyo. The newly launched arrownet-Global allows overseas financial institutions to directly connect to "JPX Co-location (all)" and TSE's system, thereby strengthening the exchange's value proposition while on-boarding a new pool of investors."

Focusing on the technology, while the connectivity to Chicago uses PC-1 link, the Asian network relies on the NTT Com newly constructed Asia Submarine cable Express (ASE). In addition to its industry leading ultra low latency (figures announced by NTT Com are around 64 milliseconds between Tokyo and Singapore and around 43 milliseconds between Tokyo and Hong Kong), ASE has been especially designed to bypass the Bashi Channel, a known spot with high-risk of earthquake and typhoon, thus offering high reliability. From a contractual point of view, a one-stop-shop approach has been privileged with a basic plan featuring in the same contract the ASE cable (for Singapore or Hong Kong), PC-1 (for Chicago) and arrownet. Customers can also subscribe to optional services like JPX Co-Location (Tokyo), and Proximity Services (NTT Com Tokyo DC, NTT Com Singapore DC, NTT Com Hong Kong Financial DC). Talking about commercial and technical merits, Hosokawa-san commented: "NTT Communications provides end-to-end network solution with its Ethernet Leased Line service, which connects the clients' system in Hong Kong or Singapore all the way through to "JPX Co-location (all)" and TSE's system in Tokyo. Clients will be able to enjoy one-stop services from ordering to network infrastructure design and maintenance, with NTT Communications as the single contact point. Prominent financial institutions have started to use the service."

Without any doubt, this partnership supports further JPX's Asian Strategy to "approach Asian investors via enhanced trading infrastructure functionality" as presented in JPX's Medium-Term Management Plan (FY2013-FY2015) issued March end this year. We can expect this technology initiative to be followed by some other interesting ones that FIA-J Technology Committee will continue to report upon.

Past Events

AIMA Japan Hedge Fund Forum 2013

AIMA Japan (Alternative Investment Management Association) held its Hedge Fund Forum on June 27th at the TSE. The one-day event was well attended by industry professionals.

During his keynote speech, Professor Heizo Takenaka – ex-Finance Minister – spoke positively on "Abenomics"and its potential effect on improving the economy. Following a question on financial reforms, Mr. Takenaka commented that financial regulators in Japan have a very strong position, but often they resist change. This can be a challenge for implementing reforms being suggested through the government's initiatives.

FIA-Japan was originally established in Tokyo in 1988 as a nonprofit organization by foreign and Japanese futures industry participants and later reorganized as a “General Incorporated Association” (“Ippan Shadan Hojin”). It is the only organization in Japan of its type with a membership drawn from the entire cross section of the derivatives industry. It has over 60 members representing the various corporate sectors participating in the derivatives industry in Japan. Their Mission is to encourage the growth and success of the Japan financial marketplace and its development as a regional and global financial center.

Editor`s Note

Summer 2013 in Japan has broken many records, including record-high temperatures, and will stick in our memories as a rather unusual summer. Braving the heat and suffering from the Government’s guidance on limiting the use of air conditioning (dubbed “Cool Biz”), governmental bodies and exchanges have been rather busy pushing through reforms or preparing for their future strategies. The industry is still very much focused on the Comprehensive Exchange and how TOCOM will end up fitting into this picture…or not.

FIA Japan is too in the midst of major internal changes to adapt to this evolving environment, revamping our committee structure, while maintaining our course to hold another conference in Tokyo in fall 2014.

Finally, do join us at our “cool off summer party” on September 10th !

Tony Crane